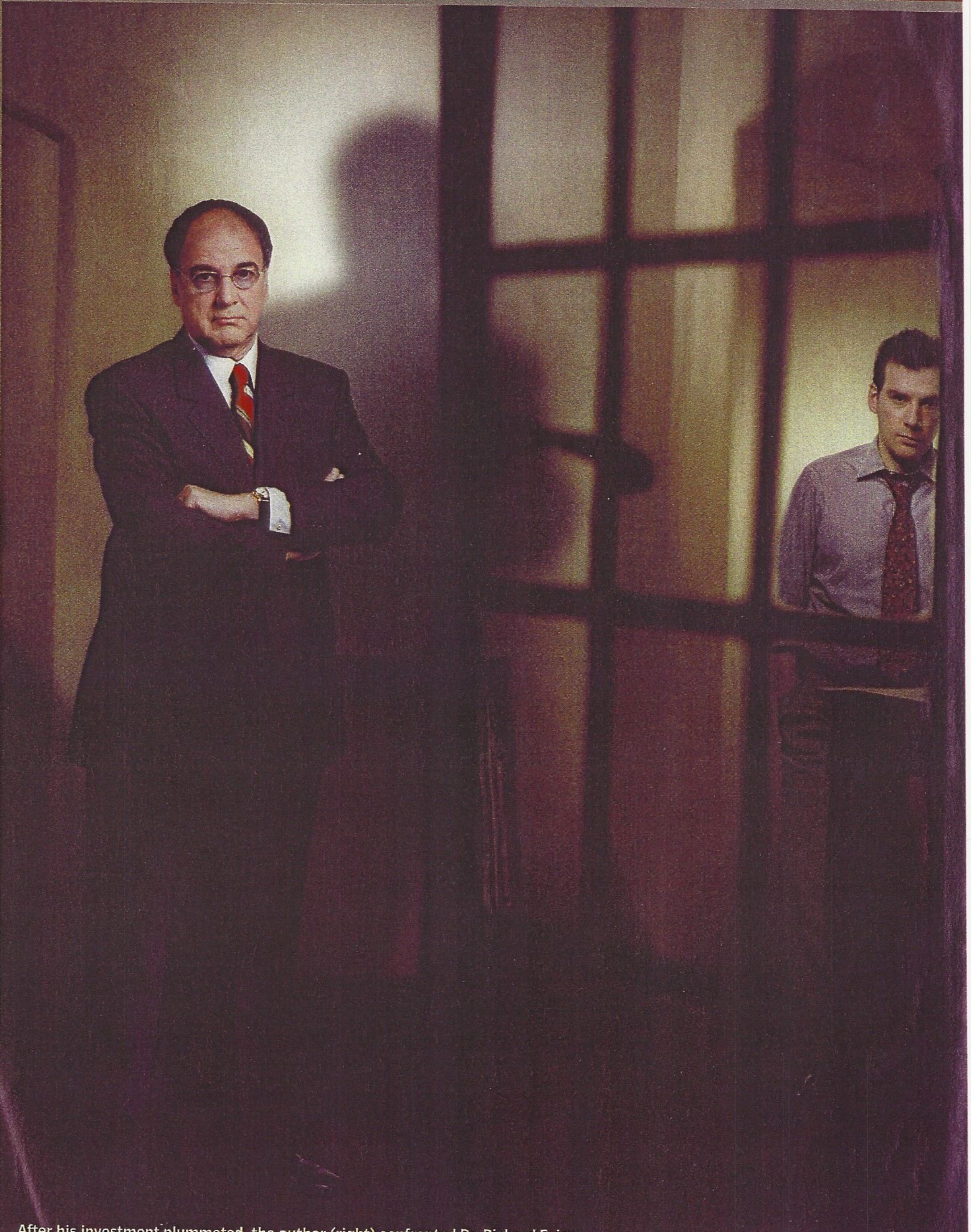

After his investment plummeted, the author (right) confronted Dr. Richard Fuisz.

ONE INVESTOR'S MISTAKE

Our writer owned only one stock. When it imploded, he discovered just how little he knew about it.

CONFESSION OF A DUMB INVESTOR

BY WILLIAM GREEN

On May 25, 1999, Fuisz Technologies announced disastrous news. Its CEO, Ken McVey, would resign immediately to pursue "personal interests." The stock lost more than a third of its value within hours, then kept plunging in the weeks that followed. In just six months, it had dropped 80%. And I, a supposedly savvy financial journalist, had ridden it down the entire mind-numbing way. ▪ Fuisz, a small firm that's developing new forms of various drugs, was no idle flirtation for me. It was the only stock I owned. I'd researched it intensively and held it for two years, smugly assured that I—unlike lesser investors—understood the company's rich promise. Trusting my judgment, my father-in-law had bought the stock too. Now we'd both lost thousands of dollars. When Fuisz imploded that day in May, I felt physically sick. How could I have been so wrong?

As my ego convalesced, I recalled an interview I'd done with famed fund manager Sir John Templeton. He'd warned me that regular investors should avoid buying individual stocks, since we know so much less than professionals. Perhaps he was right. But even the pros hadn't seen the Fuisz debacle brewing. Prestigious firms like Citigroup and Hambrecht & Quist had owned hefty stakes at the time it tanked. Highly paid analysts at Salomon Smith Barney, Lehman Bros., Credit Suisse First Boston and CIBC Oppenheimer had also failed to see the impending disaster. They'd all rated Fuisz a "buy" in the months before it blew up.

If these so-called experts couldn't tell that a stock was about to implode, what chance did the rest of us have? When our stocks soar, we congratulate ourselves on knowing what we're doing. But owning a blow-up like Fuisz—or Cendant, Oxford Health, Ciena or Sunbeam—humbles you fast. Suddenly you see how tough it is to divine what's really going on inside a company.

FUISZ (PRONOUNCED FUSE) had always been a confusing stock. Six months after going public in late 1995, it quadrupled, hitting its all-time high of $31.50. The company had no profits but a sexy story: It promised to change the way we take drugs. Fuisz was working with Johnson & Johnson, for example, to create a Tylenol tablet that would dissolve instantly in your mouth.

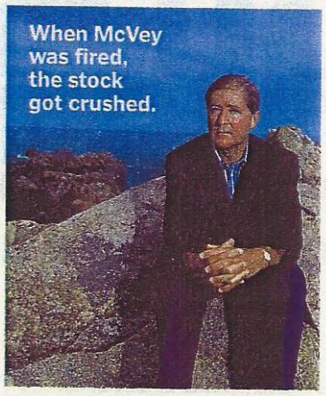
Overhyped and overpriced, the stock got crushed. By early 1997, it had tumbled to $5.62. I began to research the company around that time for an article in *Forbes*. I interviewed investment bankers, venture capitalists, customers, rivals, mutual fund managers, equity ana-

PHOTO ILLUSTRATION BY DAVID S. WAITZ

lysts, short-sellers—the sorts of experts a regular investor never gets to quiz. I toured the firm's factory in Chantilly, Va. and grilled five of its top executives, spending hours with the chairman and the CEO.

I concluded that the stock was tantalizingly cheap. Short-sellers had spread rumors that the technology didn't work, that the firm's pills were too fragile. I know less about science than the average nine-year-old, but I called the director of new-product development at Boots, a blue-chip English firm making an ibuprofen tablet with Fuisz, and he was "very enthusiastic" about the technology.

Others were equally effusive. An analyst at Alex. Brown told me Fuisz could ultimately generate revenues in the "hundreds of millions" and said the stock could hit $20 within 18 months. One of the largest shareholders raved, "This could be a billion-dollar company. The technology is absolutely sensational."


When McVey was fired, the stock got crushed.

Duncan Kendall

My article ran in April 1997, and I bought the stock on June 12. By then it had climbed to $10, yet it still seemed like a bargain. I expected a rich payoff, but I had more riding on this than mere dollars. I would prove myself a bold and brilliant contrarian.

I had just one niggling concern. The company's founder and chairman, Dr. Richard Fuisz, struck me as an emotionally volatile eccentric. He'd flared when I asked pointed questions about the firm's technology, and he'd railed against "ferocious" short-sellers for spreading rumors that he was a "fraud" who'd been "jailed." He certainly wasn't a typical corporate chieftain: He told me he'd been an actor, a talk show host, doctor, an inventor, the head of a Russian modeling agency and a supplier of computers to the KGB.

Still, he'd recently resigned as CEO, hiring Ken McVey to replace him. McVey, who'd been a high flier at an Irish drug firm called Elan, seemed clever and levelheaded. As one fund manager recently told me, Wall Street "came in because McVey came in." But Dr. Fuisz continued to chair the board and own 21% of the stock, which would give him far more clout than I realized.

DURING THE NEXT YEAR I became obsessed with my stock, often checking the price every few hours. As both a journalist and an investor, I read hundreds of postings on a Yahoo! message board devoted to Fuisz, spoke to Dr. Fuisz again, chatted with two major shareholders and studied endless financial reports. Everything looked rosy, and the stock surged. At one point, I was up 55%—and my father-in-law, who'd bought a week or so earlier than I, had almost doubled his money. Boy, did I feel smart.

And then, just as I started to daydream about being the next Warren Buffett, weird stuff started to happen. This past January, in the midst of the Internet stock craze, Fuisz announced that it was selling an online drugstore it had launched. The buyer? Dr. Fuisz. I was mystified. Eight days before the sale agreement, I'd received a press release touting the store's "rapid expansion." Now I was being told it was a dead loss. But why, then, did Dr. Fuisz want it? Later, digging deep inside a proxy statement, I found that he was charged just $2.4 million, which was payable in installments by 2003—an unusually sweet arrangement. The stock fell 25% in the two weeks after the sale was announced.

Another thunderbolt struck on Feb. 17. Logging on to Yahoo! that day, I was hit with explosive news: Fuisz was suing Elan, accusing its powerful rival of stealing trade secrets and reneging on a deal to manufacture Fuisz products. (The suit was later settled.) With the collapse of this deal, I read, fourth-quarter earnings would fall far short of expectations. This was damaging enough, but the company also disclosed that Dr. Fuisz was personally suing Elan for breach of contract. I pored over a copy of his lawsuit (also later settled) and found he'd recently tried and failed to sell his 4.2 million Fuisz shares to Elan for about $70 million in Elan stock. In other words, our founder, chairman and biggest shareholder had secretly been negotiating to bail out.

Over four days, Fuisz plunged to $6.75. In one hellish month, the stock had been slashed in half. And for the first time, I began to sense how little I really knew about what was going on inside this firm. After all, Dr. Fuisz claimed he'd sealed his sale to Elan in November, yet we weren't told about the deal until three months later.

THE PRESS RELEASE said CEO McVey was leaving the company to pursue "personal interests." But I found out this was a lie.

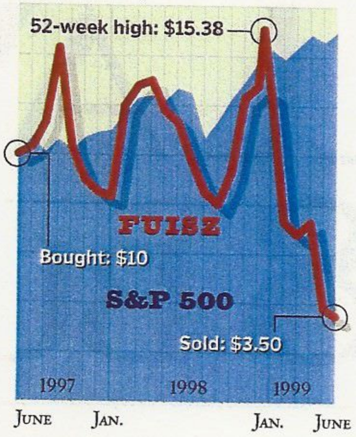
Still, I held on, willing myself to believe McVey would restore calm. I no longer dreamed of fat profits, but I sure as hell wasn't going to take a loss. Then came the deathblow. I was in my office on May 25 when my father-in-law called with chilling news: "Did you see McVey resigned?" I logged on to Yahoo! and felt a rush of helpless panic: Oh, my God! The stock had plummeted to $4. My father-in-law and some unfortunate *Forbes* readers were getting massacred. Confused and embarrassed, I didn't know what to say. My father-in-law told me that he was cashing out, then raced to call his broker. What had I done?

The press release said McVey was leaving to pursue "personal interests." But this was a lie. I soon learned that Dr. Fuisz (with board approval) had ordered McVey to resign or else be fired. Amazingly, the new acting CEO would be Dr. Fuisz himself—the very man whose efforts to sell his own shares and buy the online store had helped decimate my stock. I felt like I'd been mugged.

If there was any pleasure amid this misery, it came from watching Wall Street's "experts" look like hapless fools. CIBC, which just months earlier had set a price target of $18, dropped coverage of the stock altogether, as if it no longer existed. Salomon Smith Barney, a longtime Fuisz fan, downgraded it to "neutral"—a euphemism for "sell." Of course, this backpedaling came too late to save those who'd heeded the analysts' bullish advice. I confronted Michael Tong, the analyst who followed Fuisz for Salomon, asking him if there'd been a warning sign he should have detected. "Not that much," he said. "Unless you get into the [private] board meetings, the frictions aren't transparent." It sounded as if he couldn't wait to get off the phone.

With McVey out of the firm, I finally conceded defeat. After a few weeks of wishful procrastination, I sold out on June 18 at $3.50. I'd lost 65%, while the S&P 500 had risen 50%. Yet I still didn't understand what had happened.

Looking for answers, I had lunch with a money manager who owned a huge stake in the firm. He confided that he too had been "blindsided." Two years ago, he'd assured me that Dr. Fuisz was "brilliant" and "honorable." Now he fumed about the doctor's attempt to sell his stock to Elan: "It was a bailout….He didn't give a damn for his shareholders."



Note: Monthly close data. Source: Bloomberg.

AS THE STOCK ROSE, the author began to daydream of being the next Warren Buffett.

FEELING DUPED and thinking of writing about this fiasco, I called Dr. Fuisz and arranged to meet him in Virginia. His firm had made a fool of me, and I wanted to know what he had to say for himself. By then, the stock had fallen 90% in three years, yet he seemed quite chipper: "Everything is going great. The company has never been more in control."

So why was the stock at $3.50? One reason, he said, was that "foolish rumors" were being spread on Internet message boards by "ignorant" investors. Above all, though, he blamed McVey's "bad management," saying he was fired because "his performance wasn't satisfactory." (Tony Lazos, a Fuisz director, agrees, saying that McVey "ran the company into the ground." It's certainly true that the company hadn't brought a major product to market under McVey and that it was running out of cash.)

I said I didn't think it had helped that Dr. Fuisz had tried to rake in $70 million by selling his own shares to Elan. He disagreed and bridled at the idea that he'd tried to line his own pockets. "I didn't need that f------ money," he snapped. "Nobody will believe it, but I did it for the shareholders. I thought, 'Jesus, boy. If Elan is a shareholder of that many shares, our investors are secure because Elan is Elan.'" As for the online drugstore, he said it had monthly sales of $60 and was worth only $50,000: "It was a white-knight act to buy it for $2.4 million. That's what the sophisticated investor understands."

Having learned to take nothing involving this company on faith, I tracked down McVey, who was living in a hotel in the Channel Islands. McVey denounced Dr. Fuisz as "paranoid" and "certifiable. You're dealing with someone who's lost it." What did he think of the chairman's attempts to sell his shares to Elan? "He is absolutely prepared to do anything to look after No. 1," McVey hissed. "The man is greed personified." ("Desperate people say desperate things," responds Fuisz.)

The sale of the drugstore to Dr. Fuisz seemed to anger McVey even more. Indeed, said McVey, he has asked the Securities and Exchange Commission to investigate. "Richard will be accused of knowingly and willfully stealing assets from Fuisz Technologies," he asserted. (That's "absurd," says Dr. Fuisz.) For good measure, McVey said he's asked the SEC to investigate Patrick Scrivens, the firm's CFO, for selling his Fuisz stock at $15 right before the big fall. (The SEC won't comment on any of these charges; Scrivens didn't return my calls.) McVey then vowed, "I'm going to get those bastards."

Listening to McVey's diatribe, I couldn't help feeling delighted that I'd sold my stock. For all I knew, it might still soar, but this food fight was just too messy for my taste. Dr. Fuisz had told me, "In my mind, I'm as honest and truthful as I can be at all times." Yet, McVey was now telling me that the doctor should be "in jail for securities fraud." Which of them should I believe? Had they both gone nuts?

Back home, I perused the Fuisz message board on Yahoo! to see if anyone else knew what was going on. "We are completely in the dark," lamented one shareholder. Another pleaded helplessly, "All I want is the truth, the full truth, not one person's version of the truth." Yes, I thought, that's what we all want. Unfortunately, analyzing stocks is not that simple. Indeed, these long-suffering shareholders were about to endure yet another shock. On July 26, Fuisz announced that it would be acquired by Biovail, a Canadian drug firm, for just $7 a share. On Yahoo!, disappointed investors cursed Dr. Fuisz.

I, meanwhile, had to consider another issue: what to do with the cash sitting in my brokerage account since I'd sold Fuisz. I'd heard enticing tidbits about a hot firm in the oil game. But no, I wasn't going down that route again. My days of gambling on individual stocks were over.

I decided to close my brokerage account and invest the remnants in the Third Avenue Value Fund. Its manager, Marty Whitman, is a Yale finance professor and one of the smartest stock pickers around. Pondering my plan, I glanced at a recent letter he'd written to shareholders. And there, to my astonishment, I discovered that he'd just lost more than $40 million investing in a Japanese bank that went bust. "I really think I should have known better," he confessed. Still, these mistakes "go with the territory," he wrote. "After all…Warren Buffett had USAir."

For the first time in weeks, I felt a little better.