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DOLE HIS NEW GROWTH PLAN

CHINA BUILDING A NETWORK OF U.S. BUSINESSES

BusinessWeek

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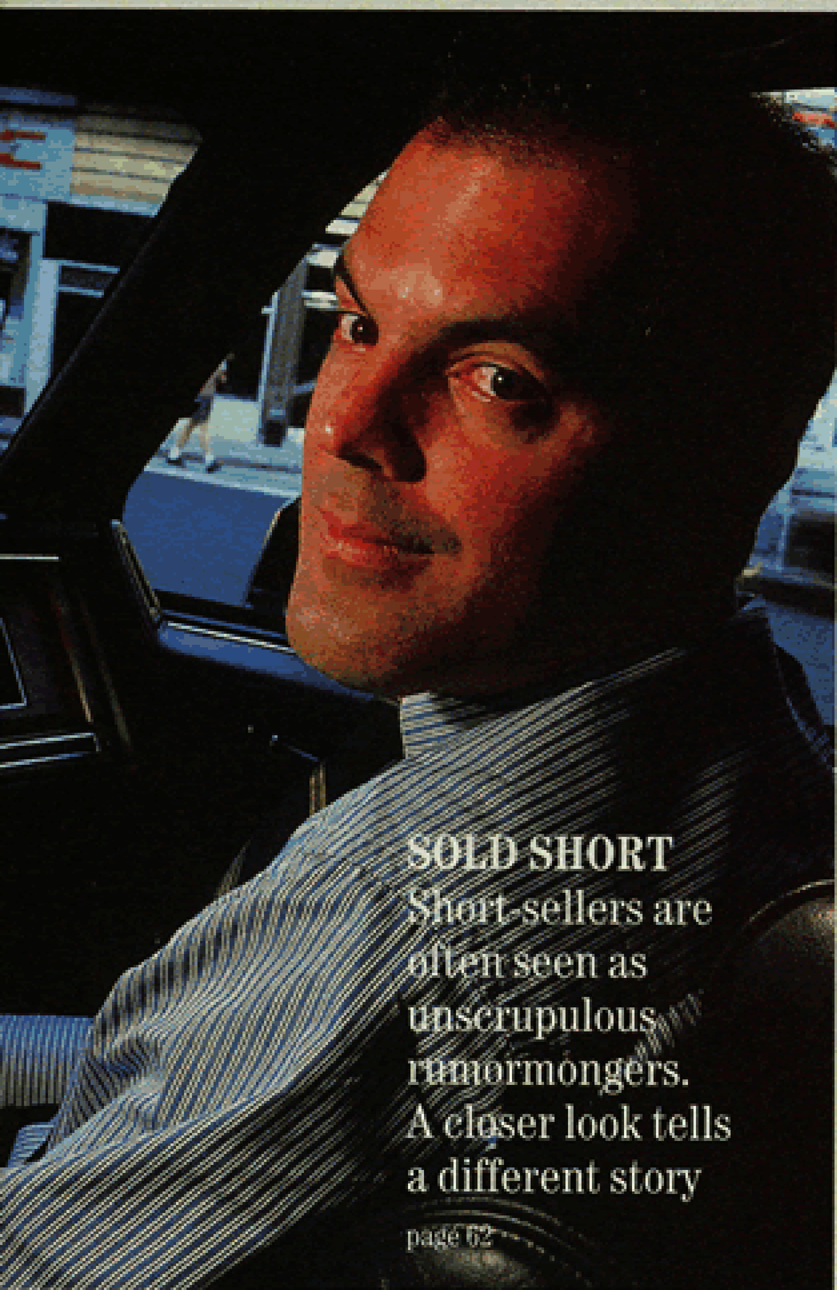

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Get back to the budget, guys
Mandate bomb scanners now
Don't sell the shorts short

THE SECRET WORLD

Widely despised, shorts are often seen as unscrupulous rumormongers. A closer look tells a different story

Solv-Ex President and Chief Financial Officer W. Jack Butler is the kind of man who might have been called a captain of industry, back in the days when that really meant something. An erect, dignified man in his late seventies, he spent 35 years with Mobil Oil and served as chairman of Mobil Saudi Arabia in the heady days of the 1970s. Solv-Ex has a process for turning oil-laden sand into crude oil—a vital, almost unimaginably lucrative process, if it succeeds. And to Butler, it's more than that. "I don't just want to make money," he says. "I want to do something for my country."

But Solv-Ex Corp. is under attack. Picking at a salad in a café near his Park Avenue apartment, Butler stoically ticks off the problems. Rumors of improprieties and involvement by penny-stock manipulators. A Securities & Exchange Commission investigation. An incessant drumbeat of negative publicity has slashed the company's share price by 60% over the past few months and has so hurt its reputation that its efforts to finance its sand-into-oil project, up in Alberta, Canada, have been gravely harmed. "We feel we're a good company," he says. "Operating ethically. Good technology." And it would succeed, he insists, if it weren't for a mudslinging campaign by a small band of stock-bashing traders: the short-sellers.

Cover Story

About half a mile downtown, a man about half Butler's age, polo-shirted and barefoot, is staring at a stock-trading screen that shows some cheerful information: The Dow Jones industrial average is falling. Something resembling panic seems to be taking place, and at trading desks around the country, men and women are picking up their phones and yelling "Sell!" This man is on the phone with his trader, but he's buying—replacing stocks that he had previously borrowed and sold, hoping that their prices would decline. They have. But there is one stock he borrowed and sold that he is not replacing. It is Solv-Ex. For he feels Solv-Ex has a long way to go before it stops falling. The company, he asserts, is burning cash like an overheated furnace—one that will eventually blow up.

Short-sellers. They're as old as Wall Street. And though much has changed there, this has not: No one on the Street is more widely despised. Short-sellers were profiteers in the 1929 crash; aggressive "stock-busters," led by the flamboyant Feshbach brothers, in the 1980s; and, nowadays, secrecy-worshipping, often embattled traders who bet on what is almost

ILLUSTRATIONS BY HANOCH PIVEN

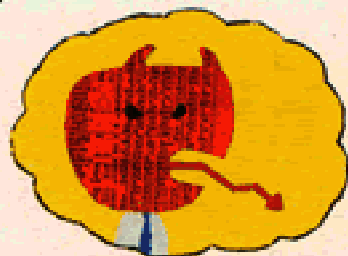
The Truth About Those That Sell Short

The murky world of short-selling is beset by a host of misleading—and sometimes downright false—perceptions. To clear up a few:

DATA: BUSINESS WEEK

PERCEPTION

Short-selling makes share prices decline.



REALITY

Yes, shorts sometimes seek bad publicity that hurts stocks. But since they can't sell an issue when it's falling, they can't really torpedo stocks.

OF SHORT-SELLERS

un-American—that share prices will collapse. The bull market made them suffer until just the past few weeks. An investor who put $100,000 in the hands of a typical short-seller at yearend 1990 would have $50,400 by the middle of this year.

But the misery that has enshrouded the market lately—NASDAQ in particular—has been mother's milk for short-sellers. In recent weeks, they have come roaring back, with shorts gaining 10% in June and another 10% to 15% through mid-July, according to Harry Strunk, a Palm Beach (Fla.) investment consultant who tracks short-sellers (chart, page 66). The short-seller revival is likely to exacerbate their reputation as piranhas—particularly among investors in small-cap stocks, who often view short-sellers as the assassins of Corporate America. "Small companies can be seriously affected by short-sellers. Some of these shorts target particular issuers and don't know a damn thing about the companies they're shorting," says Edward Mishkin, a prominent New York securities lawyer and a vocal critic of short-sellers.

BET OR PUSH? Even among hardened pros on Wall Street, particularly institutional investors, small-stock underwriters, and brokerage analysts, shorts are shunned and hated. "Fund managers will tell you: 'I don't want anyone shorting my stock.' They don't want anyone making money on their mistakes," says one Wall Street executive who routinely deals with both shorts and "longs"—conventional investors. The detractors of short-sellers maintain that shorts don't just bet on share-price declines, they make them happen. Shorts are blamed for the travails of dozens of high-flying stocks that have taken heavy hits during the recent NASDAQ massacre: Solv-Ex, Diana, WellCare Management, Presstek, SyQuest Technology, and a host of other high-tech companies. "Short-selling and bear raids are part of the business," concedes Solv-Ex CEO John S. Rendall. "But when you put out false rumors and get the SEC involved—that, I believe, is criminal activity."

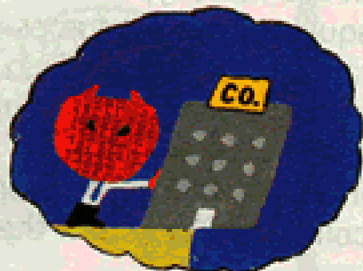
Are shorts the bane of Wall Street? Are they villains or scapegoats, responsible whistle-blowers or venal rumormon-

PERCEPTION

Short-sellers are a destructive force in the markets.

REALITY

Shorts add to liquidity in the markets—selling when markets are rising and buying when buying is needed most—during market declines. Shorts expose accounting irregularities and mismanagement. They also counter the hype from companies and brokerages that is so rampant on the Street.



PERCEPTION

Voracious short-sellers destroy companies by cutting off their access to capital.

REALITY

Companies targeted by shorts are often in shaky financial health and thus are unwise investments.

PERCEPTION

"Naked" short-selling—selling stocks that haven't been borrowed—is rife in the markets and helps drive share prices down.

REALITY

Naked shorting takes place, but its prevalence has been exaggerated by critics. Market makers can "go naked" in the normal course of business, but they risk heavy penalties if they do so to bet that a stock will fall.

PERCEPTION

Short-sellers spread lies about companies.

REALITY

Sometimes. But more often than not, their research is among the most detailed and accurate in the investing community.

Because of their contrarian stance and the liquidity they provide, shorts have an overwhelmingly positive impact

gers? To find the answer, BUSINESS WEEK delved into the world of the short-sellers. It wasn't always easy, for shorts cherish their privacy, and many fear attention with an intensity that can border on paranoia. The picture that emerged is dramatically at odds with the conventional view of short-sellers as hood-like market-manipulators.

To begin with, only a tiny fraction of short sales are bets on the direction of stocks. The vast majority—perhaps 98% by one informed estimate—are merely efforts to hedge stock holdings or take advantage of arbitrage opportunities with other forms of investment. Traders who exclusively short-sell are but a tiny cadre of market players—a handful of partnerships and small brokerage firms. Despite their raptor-like image, they are often victims—not perpetrators—of stock manipulation. And though they can certainly put a dent in stocks by leaking stories to the media, the image of "stock-busters" who can drive down share prices is overblown. Exchange and NASDAQ rules ban short sales while a stock is declining. This "uptick rule," which allows shorting only when the most recent price change was positive, makes it tough to beat down stocks by short-selling alone.

Cover Story

To be sure, there are instances of questionable practices by shorts, such as the aggressive short-selling that allegedly led to the demise of the Adler Coleman & Co. penny-stock trade-clearing firm last year. Regulators are investigating charges by Mishkin, the court-appointed trustee, that shorts engaged in such nefarious practices as "naked" short-selling—shorting stocks that haven't been borrowed. Federal authorities are investigating the short-selling of Organogenesis Inc., a biotechnology company, because of allegations that false information was spread about the company (BW—Apr. 22). But the overwhelmingly negative publicity overshadows the contributions shorts make to the market—particularly in raging bull markets, when Wall Street hype runs rampant.

Because of their contrarian stance and the liquidity they bring to bear, short-sellers have an overwhelmingly positive impact on the market. They are often the market's first line of defense against financial fraud—frequently alerting regulators to scams and accounting irregularities, as was the case with now defunct ZZZZ-Best and College Bound. And short-selling abuses have often been exaggerated. Naked short-selling certainly happens, but vastly more commonplace is the "short squeeze," a chain of events that can be a blatant effort to punish short-sellers by forcing them to buy stocks when they are artificially high (illustration below).

REALITY CHECK. The market's hostility toward short-sellers makes shorting a risky strategy often best left to professionals. Still, everyday investors have a great deal to learn from short-sellers. Even when they are wrong or their timing is off, short-sellers offer a refreshing reality check on the unvarnished bullishness so prevalent on Wall Street. Short-sellers include some of the most talented analysts in the investment arena and are noted for their adroit, labor-intensive research. One short-selling partnership even includes among its analysts a retired physician to evaluate biotechnology stocks. But at bottom, what gives shorts an edge is sheer shoe leather.

"Shoe leather" might well be Manuel Asensio's middle name. Like most short-sellers nowadays, Asensio has his fingers in other pies—from conventional money management to municipal-bond underwriting. But short-selling is clearly his first love. Asensio, who runs Asensio & Co., a New York investment boutique, is a rarity among short-sellers, for he is anything but secretive. For the first time since the 1980s, when the flamboyant Feshbach brothers of Palo Alto, Calif., made some highly publicized stock pans, shorts have a self-appointed... well, "point man" might be the word. "I respect what he does," says one short who has never met Asensio but has read his research and respects the guts shown by his public stance on stocks. "He is totally associated with his

ILLUSTRATIONS BY LISA KNOUSE BRAIMAN/BW

Four Ways Shorts Get Stung

There are four distinct types of short squeezes. All force short-sellers to buy back stock, thereby driving up share prices.

DATA: BUSINESS WEEK

THE TRADE

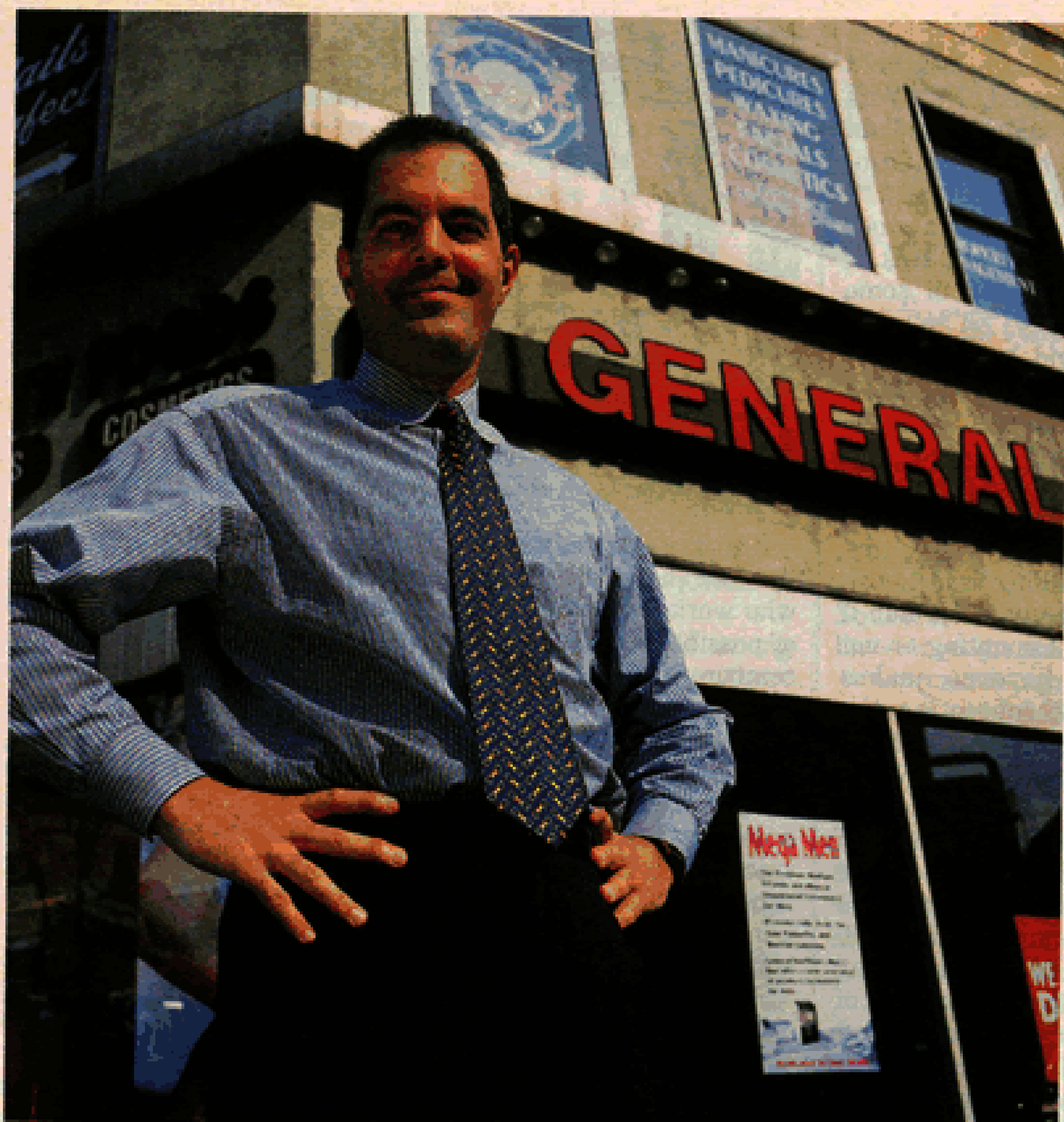
A short-seller sells shares that are borrowed, either from an institutional investor or—more perilously—from a retail brokerage. Shares in any margin account can be borrowed if they haven't been fully paid for. The short hopes to eventually replace the borrowed stock at a lower price, pocketing the difference.

THE MARKET-FORCES SQUEEZE

In the most typical short squeeze, market forces or favorable news drive up share prices. If prices move up sharply, shorts must immediately put up more collateral—or return the shares.

THE INSTITUTIONAL SQUEEZE

Institutional shareholders—mutual funds and pension funds—who loan out shares to short-sellers can demand their return at any time. When that happens, the shorts must hand them over.



DANUTA OTFINOWSKI

calls"—his short picks—"and that is something you don't see much of nowadays." At least, not among short-sellers.

A native of Cuba who came to the U.S. with his family in 1962, the 41-year-old Asensio began trading while he was a student at Harvard University in the early 1980s. After stints as a venture-capital dealmaker and an investment banker at Bear Stearns & Co., he went into business for himself. Asensio manages about $100 million, mostly for wealthy clients. It's a small operation—just three analysts aside from Asensio, all squeezed into a cramped suite of offices in midtown Manhattan. "I never subordinate my own judgment or fact-finding," says Asensio. Not surprisingly, he routinely puts in 14-hour days and hasn't taken a vacation since February—of 1993.

DETAILS, DETAILS. Although his embrace of the limelight sets him apart from most shorts—he even issues press releases announcing his short picks—as an analyst, Asensio hews strictly to the exhaustive, detail-oriented approach that is the short-sellers' stock in trade. A good example is his short sale of General Nutrition Cos. shares last January. Red flags were fluttering: a high price-earnings ratio, selling by corporate insiders, and oversaturation of the health-food market. "I saw nothing but bad news in the future. There were problems with the vitamin market, insiders were bailing out, same-store sales were weak. What more can you need?" Asensio recalls.

OPEN HAND

Like his peers, Asensio does exhaustive research—but he's far from secretive

There was more. Asensio got wind of an upcoming study on the benefits of "antioxidants" such as beta carotene—a nutritional supplement that is widely promoted at GNC stores. He began by calling secretaries and receptionists at hospitals where the study had been taking place. "I got a flavor of what was going on, a smell," Asensio recalls. He liked the odor. On the day of the release of the study, which cast doubt on the efficacy of beta-carotene supplements, Asensio hired a lawyer to get hold of it the instant it was available in Washington. Not a messenger service? "No way. I use the A-Team," says Asensio.

Asensio shorted the stock—and issued a press release dumping on the company. Nothing happened. "Their defense was that beta carotene was only a small percentage of their sales," says Asensio. "But I said at the time: 'The problem is store traffic, stupid!' People come into the stores for antioxidants." Eventually, GNC announced that same-store sales were on the wane, and the shares fell. GNC stock, which traded at 23 in early January, is now at 14. (A spokesman declined to comment on Asensio but says GNC "firmly believes our business strategy is in place and working.")

Nowadays, Asensio's No. 1 stock is a company that he despises—and the feeling is mutual. It is Diana Corp., a Milwaukee company that is in the process of dramatically shifting its product line from meat distribution to telecommunications equipment. Asensio thinks Diana is an ill-managed company that has put out misleading information; Diana says Asensio has been doing the same thing. "He has continually made misstatements about our

THE ACCOUNT SWITCH

If shareholders move shares from margin to cash accounts, shorts must return any shares borrowed from the margin account.

THE HYPE SQUEEZE

Common among thinly traded shares. The company, or stock promoters, intentionally pressure shorts by praising the stock to small investors or issuing overoptimistic press releases to drive up the share price.

THE BUY-IN

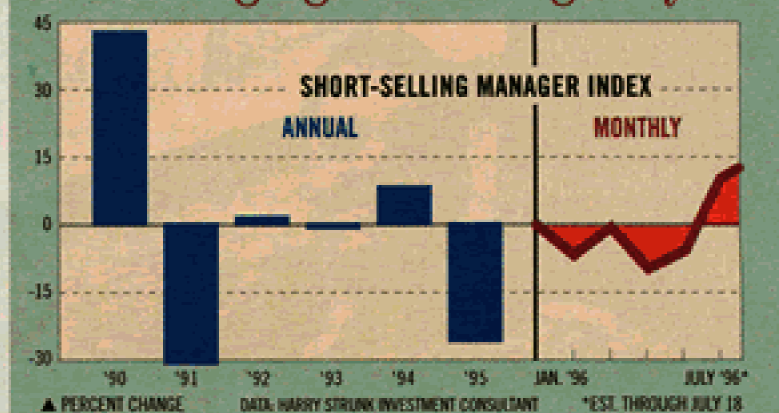
When shorts must return borrowed stock, the shares must be bought on the open market. Thus, short-sellers can sustain huge losses if prices have risen—and since their purchases drive up prices still further, they boost the pain of fellow short-sellers.

company," fumes Diana Chief Executive Richard Y. Fisher.

Asensio has shared his views with the message boards of America Online Inc., where they are welcomed. But Wall Street is another matter. Asensio and other shorts complain that brokerage analysts and fund managers have a uniformly hostile attitude and are loath to even return their calls. "I would love for someone to call me and tell me that a stock that I own is a piece of s—," says Asensio. "But I'll talk to some pension-fund manager who owns $4 million of some stock, which he bought with employee money. I'll tell him something is wrong with the company—and he gets emotional! It is ridiculous. It is irresponsible." Another short says he attempted to bring accounting irregularities to the attention of a company's auditors and found that his calls were not returned. "I wound up faxing them," says the short. The accounting allegations were eventually acknowledged and corrected by the company.

The whistle-blowing element of short-selling is a sensitive subject. Short-sellers don't like to trumpet it, but if they feel that a company is using improper accounting or not making adequate public disclosures, they have no qualms about contacting the companies' auditors, the exchanges, the SEC, and lawyers seeking to bring class actions on behalf of disgruntled investors. And then there's the financial press. "I like talking to the press. We're like investigative reporters ourselves," says one short. Another short-seller keeps a small stack of articles from financial publications in which he was a source—all exposing fraudulent and shady companies that ripped off thousands of shareholders. Indeed, many prominent financial frauds of recent years were targeted by short-sellers long before they were picked up by regulators and the press. Shorts exposed the troubles besetting WellCare Management Group Inc. and Future Healthcare Inc. in recent months.

Cover Story



The saga of WellCare, a Kingston (N. Y.) HMO, epitomizes the role shorts play as whistle-blowers. "We talked to doctors who worked for the company," one short recalls. When word of possible accounting improprieties surfaced last March, the company pointed the finger at "untruths circulating as rumors" coinciding with a "buildup of a substantial short position in WellCare's stock."

For a while, the company hanged tough, hiring a private investigative firm, Kroll Associates Inc., to look into the badmouthing of the company. But the shorts were on the right track. Two months later, WellCare restated its previously reported 1995 earnings—slashing them by 80%. A spokesman admits that "some of the issues [short-sellers] raised had some accuracy" but that others were "overstated."

WellCare was a smashing victory for the shorts, as was SyQuest Technology Inc., a disk-drive maker that has attracted shorts because of its propensity to consume cash—often a tip-off of financial woes. The shares have fallen to $6 from a takeover-fed high of $17 in May. (SyQuest won't comment on the shorting of its stock.) Aggressive accounting

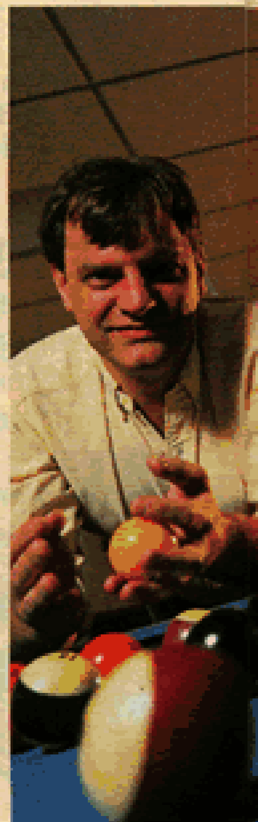
THE 'BAD BOYS' OF CHICAGO ARBITRAGE

When Chicago Stock Exchange officials showed up at the trading firm Scattered Corp. for a routine audit two years ago, principal Leon A. Greenblatt was ready. He answered the door with a toy dart gun sticking out of his pocket, a pool cue in his hand, and a shot of Jack Daniels splashed on his face. Ushering his guests into a room without a table, he handed over the firm's records 10 pages at a time. These days, the auditors ask Greenblatt to send his books across the street to their offices.

No, the Chicago Stock Exchange doesn't like Leon Greenblatt—and it's not just because of his, well, unconventional personal style. Three years ago, at age 33, Greenblatt did something that brought down upon him the kind of regulatory wrath—a $6 million fine—that is usually reserved for insider traders and penny-stock peddlers. Greenblatt provoked the Chicago exchange's ire during an audacious arbitrage play on the shares of bankrupt steelmaker LTV Corp. Greenblatt sold more LTV stock than actually existed, replacing it with cheap warrants—and reaping a $27 million profit in 22 trading days. So far, he has gotten away with it—and won a little-noted legal victory in the ongoing war between longs and shorts.

A judge said the partners may be "gamblers" and "sharpies," yet he upheld their LTV victory

Scattered principals Greenblatt, Andrew Jahelka, and Richard O. Nichols may be "reckless gamblers, sharpies, wise guys, exploiters of loopholes, even violators of the letter or spirit of the rules," wrote Appellate Judge Richard A. Posner, one of the federal judiciary's leading economic thinkers, in a February, 1995, ruling. Posner noted that Scattered's trading in LTV helped bring together the price of the stock and its underlying value, thereby playing a valuable role in the marketplace. Thus, the firm furthered—not violated—the objectives of securities law, the judge concluded, upholding a Scattered victory in a lawsuit brought by disgruntled LTV investors in a lower court. The $6 million fine the Chicago exchange levied on Scattered is on hold pending



PHOTOGRAPH BY MICHAEL L. ABRAMSON; CHART BY RAY VELLA/BW

and stock sales by corporate officers are other red flags. Recently, shorts have zeroed in on Lone Star Steakhouse & Saloon and Landry's Seafood Restaurants, as well as two manufacturers of sunglasses—Oakley and Sunglass Hut Trading—because of high insider selling. Sunglass Hut Corp. CEO Jack B. Chadsey says his recent stock sale still leaves him with a large stake in the company and does not reflect any lack of confidence in the company.

EXPERT OVERSIGHT? Specialized expertise is another area where shorts can bring powerful resources to bear. One short-seller, who has a physician on staff, is shorting Oxigene Inc., a New York pharmaceutical company. The physician-analyst studied a company-sponsored clinical study of its flagship product, an anticancer medication, and found it offered scant evidence that the product is effective. As is often the case, however, the company has a dramatically different point of view. Ronald Pero, Oxigene's chief scientific officer, says the shorts are dead wrong and that the study offers evidence of the drug's efficacy.

Right or wrong, research like this is often shared among shorts, which gives rise to the not unjustified view that there are "rings" of short-sellers. Actually, "rings" may be a bit pejorative, since institutional investors—and brokerages, of course—are similarly ready to share stock picks. But there's a darker side to short-selling that has recently gained attention in the wake of the failure last year of Hanover Sterling, a penny-stock broker, and the subsequent failure of Adler Coleman, the clearing firm that executed Hanover's trades. Trustee Mishkin found that Hanover and Adler were driven out of business by short-sellers. The shorts, in response, accuse Mishkin of enacting a short squeeze that deliberately gave them losses. The two sides are slugging it out in court.

Mishkin maintains that what happened to Adler Coleman is the tip of the iceberg. He recently stated in court documents that one of the shorts allegedly involved in the Adler Coleman failure, Fiero Brothers, went on to target Solv-Ex.

Many financial frauds of late were targeted by shorts well before regulators spotted them

That is denied by John Fiero, the head of the firm, who notes that he has both bought and sold short Solv-Ex shares. "I'm a trader, not a short-seller," says Fiero.

If the bankruptcy court determines that Adler Coleman was driven out of business by the shorts, it would be a rare legal victory for the "longs." In one landmark case involving short-selling by Scattered Corp., a Chicago stock-trading firm, Scattered won a ringing victory (box). Moreover, shorts are often the victims of manipulation in short squeezes. Squeezes have become commonplace in recent months and have only abated during the recent market setback.

A squeeze can be quite benign—perhaps a bull market putting pressure on short-sellers. But it can also be a deliberate effort to put shorts under pressure and push up prices by forcing shorts to buy back their shares. To bet on a share-price decline, short-sellers must sell stocks that they borrow. There are two sources of stock loans: institutions and brokerage accounts. Institutions lend shares for a small fee—usually just one-quarter of 1% of the value of the shares. Brokers are permitted to lend shares from their own accounts and from customers' margin accounts that have not been fully paid for.

But shares available for short-selling are growing increasingly scarce—particularly for the NASDAQ issues that are most popular with short-sellers. One brokerage executive, who requested anonymity, notes that institutions are increasingly chary about lending shares to shorts. The result is that shorts must borrow stock from retail brokerages, leaving

TRICK SHOTS Greenblatt (left) and Nichols cover all the angles

appeal. The U.S. Supreme Court on Oct. 2, 1995, let stand the Posner ruling. The Chicago Stock Exchange declined to comment on Scattered or the legal issues involved.

Sentiment still runs hot against the likes of Scattered—and no wonder. Greenblatt flaunts a bad-boy image even as he continues to profit from bankruptcy arbitrage. "He plays it fast and loose, and the people who are the most pissed off are the old-timers who don't understand the game," says one exchange member.

Greenblatt makes a fetish of secrecy, providing only sketchy details of his arbitrage strategies. In a typical trade, Scattered sells the stock of a company about to emerge from bankruptcy while buying newly issued shares or warrants that replace the old stock. If the old stock trades at a higher price than the new issue, Scattered can make money.

In LTV, Scattered found a huge anomaly: The company had announced a plan of reorganization under which its existing stock would be replaced by new stock. Stockholders received warrants entitling them to purchase some of the new stock at a price of about 3.2¢ per share. Even after the plan was confirmed, the old stock traded at an average of 18¢. Since the warrants greatly outnumbered the existing shares, Scattered kept selling stock and buying warrants until it had sold 180 million shares—58 million more than existed.

BLIND BANDWAGON. Speculators apparently were betting that the stock would rise just before its terminal plunge. Others simply didn't understand or investigate the planned fate of the old shares. Certainly, the facts were no secret: LTV repeatedly warned that its stock price was unsustainable.

Greenblatt relies on a creative interpretation of the rules. He claims, for instance, that as a market maker performing arbitrage, his firm is exempt from the rule requiring short-sellers to settle up within several days. Asked how he finds his deals, Greenblatt merely smiles. He warns off those who might seek to imitate his strategies: "You have to have the proper experience. If you don't, you get wiped out." An all too familar experience for short-sellers in recent years.

By Greg Burns in Chicago

There are certainly cases of excess. Just ask Organogenesis or Adler Coleman's bankruptcy trustee

Cover Story

themselves open to short squeezes involving customers demanding delivery of their certificates.

A vivid—and unusually blatant—example of a short squeeze took place with Solv-Ex. On Feb. 5, after the stock fell 30% in a matter of days, the company faxed to brokers and shareholders a "Notice to Shareholders." "To help you control the value of your investment on a steady basis," the notice read, "we suggest that you request delivery of the Solv-Ex certificates from your broker as soon as possible."

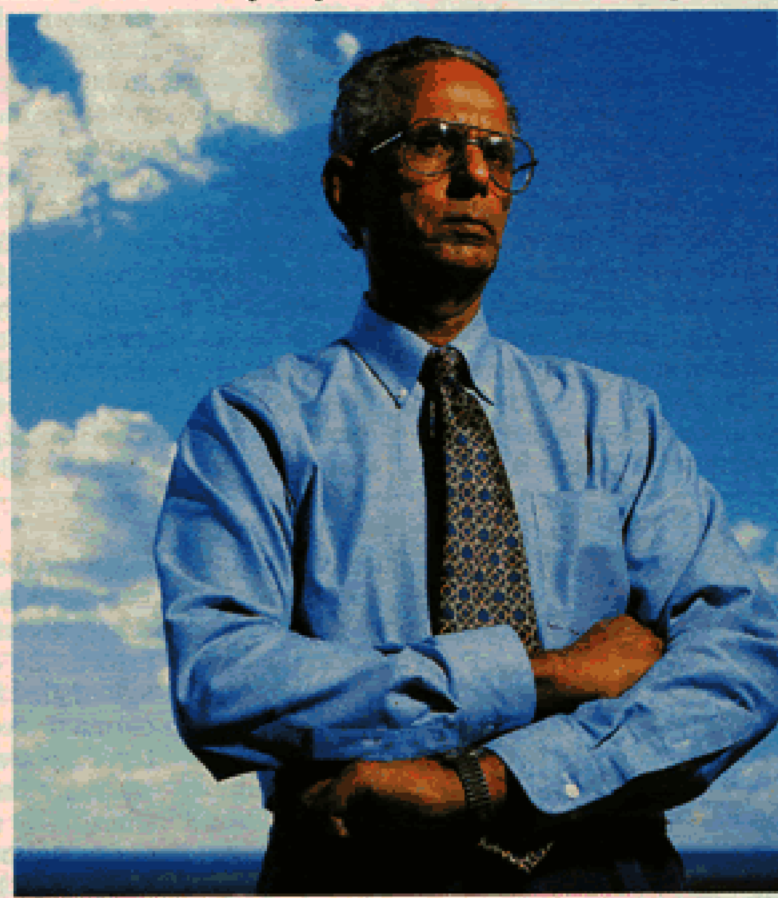
It worked. Solv-Ex shares began climbing again, approaching the old highs by Feb. 21. "I was bought in at around that time," one short-seller recalls ruefully. Says a stock-loan official at a major brokerage firm: "Very few short-sellers know the mechanics of short-selling. What they don't understand is that when a stock is not available from institutional sources and comes from the Street, they can get squeezed." The risks are magnified, he says, if the source of the stock loan is a brokerage that makes a practice of squeezing shorts.

LOOPHOLES. Short squeezes are not a problem for one of the most lucrative, little-noted, and troublesome forms of short-selling—shorting of private-issue stock sold abroad under Regulation S of the securities laws. According to short-sellers and regulators, who are looking into beefed-up regulation of Regulation S stock, such short sales are carried out by favored foreign investors—or sometimes, illegally, by corporate insiders. No matter who carries them out, however, the deals are invariably extremely lucrative.

When used to raise capital for small companies, Regulation S stock is usually sold at a discount to the prevailing market price. The stock may not be sold in the U.S. for at least 40 days. The existence of such offerings is often considered a red flag by shorts because of the dilutive effect of the stock when it is eventually sold in the U.S.—and because they show that the company may be having trouble raising capital. Shorts insist that insiders sometimes buy such cut-rate stock through foreign shell corporations and then sell short in the U.S. market—locking in the profit between the discounted shares and the shares sold in the U.S. The SEC last year acknowledged abuses in Regulation S offerings, including improper short sales, and is considering tightening the rules.

But any rule changes are unlikely to curb foreign investors, who often sell short—quite legally—to lock in their profits. Solv-Ex, which has made heavy use of offshore offerings, recently disclosed that the Curacao-based GFL Advantage Fund bought 530,000 cut-rate shares in a Regulation S offering and then sold short in the U.S. a half-million shares—one-quarter of Solv-Ex' short interest—locking in a profit that probably exceeded $2 a share, or $1 million. (The filing says the short sale was conducted "to hedge GFL's downside market exposure at the time.") GFL was still short as of early July—in the midst of Solv-Ex' campaign against the shorts.

FOREIGN PRESSURE. The offshore shares have been registered for sale in the U.S., where they will further dilute the equity of Solv-Ex' hard-pressed shareholders. So Solv-Ex executives seem to be right. Short-selling is hurting the shareholders—though the problem is from Solv-Ex' overseas friends and not from home-grown short-sellers.



UNDER ATTACK Solv-Ex CEO Rendall hired Kroll Associates to investigate short-sellers' activities

ERIC SWANSON

But what about the other shorts in Solv-Ex—the ones who are betting that it's a hot-air balloon? Are they right? Or is the company correct in its view that shorts are a roadblock on the path to oil-patch immortality? Ultimately, the markets—both the oil and stock markets—will answer that question. But so far, the outlook for Solv-Ex is not so good, because the shorts are playing hardball. Somehow, a short-seller obtained a company-sponsored engineering report and "project financing study" and had them evaluated by an engineering firm of his own. The short-seller's study contends that the Solv-Ex process is not "particularly unique, nor does it appear to be capable of being effectively protected by defensive comprehensive patents," nor is it particularly different from competing oil-extraction methods. The evaluation goes on to estimate that the project, at full capacity, will yield a $10.5 million annual loss, vs. the $24.7 million profit projected by the company. CEO Rendall strongly disputes the study and has commissioned Kroll Associates, the private investigative firm that worked for WellCare, to probe the short-sellers' activities.

That's the way it is in the world of short-selling: charge and countercharge, study vs. study. The shorts can be nasty at times. But their excesses are like a drop of ink in the ocean—an ocean of Wall Street hype. For the first time in this bull market, short-sellers are finally beginning to see the playing field tip, just a bit, in their favor. They are unlikely to wind up winners if the bull market picks up speed again. Nor will they pick up any friends. In their ceaseless, profit-driven quest for rotten apples, short-sellers will continue in their role as the market's hated—but indispensable—prophets of doom.

By Gary Weiss in New York