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REVIEW

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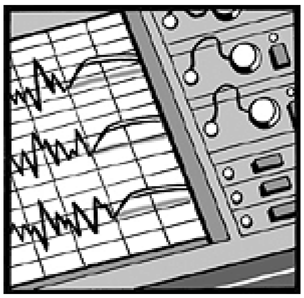
William Waitzman for Barron's

True or false? If a CEO wants to lie about the performance of his company, trusting investors have no real way of divining the real story.

One might be quick to answer true, given the recent disclosures by the SEC in charging companies such as **HealthSouth** and its founder, Richard Scrushy, with massive accounting fraud, and the company's own admission that its "financial statements should not be relied upon."

Yet investor-relations expert Laura Rittenhouse -- who has for the past five years examined CEOs' shareholder letters of 100 big companies and ranked them by the quality of their disclosure -- says the answer could very well be false.

"Just about everyone I speak to says they don't read the letters because they're so full of spin," says Rittenhouse, president of andBEYOND Communications and a former investment banker at Lehman Brothers who has become a friend of this writer. But, she adds, the letter can be a valuable indicator of not only a CEO's grasp of his business, but can even act as a kind of "lie detector."

Rittenhouse, who recently reviewed Scrushy's 2001 letter, found several red flags that might have raised investors' suspicions. To wit: Although the letter states that EPS grew 14%, the income statement shows a 27% decline in earnings for shareholders. (This kind of dissonance was true of some of Enron's former letters as well.) Next, HealthSouth flunked on Rittenhouse's measure of "capital stewardship," with talk about strengthening balance-sheet ratios by adding more debt. (We kid you not.) The company's definition of strengthening? Better diversification of debt maturities.

Last but not least, Scrushy boasts of the company's maintaining its record as "the Fortune 500 company with the second-longest streak for meeting or exceeding analysts' expectations." We shudder to even think about No. 1.

Lest anyone think talk is cheap, Rittenhouse says that stocks of the 2001 bottom-ranked 25 companies fell by 18% in 2002, while the 25 top-ranked companies fell by only 13%. Earnings of those full of spin declined $26.7 billion, as opposed to a $4.1 billion decline for the spin-free.