JOHN B. JUDIS: THE COMING REPUBLICAN BREAKDOWN

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CNN's Skewed "Cold War" • A Social Security Solution • Wall Street Vigilantes

Literary License

How "Queer Theory" mindlessly sexualizes Henry James, William Shakespeare, and just about everything else.

BY LEE SIEGEL

To further insulate the Social Security Trust Fund from politics, the law establishing a new investment system could mandate that the Trust Fund not hold more than a certain percentage of any corporation—maybe ten percent for starters. (Whether this constraint would even matter would depend on how much the market grows relative to the Trust Fund. If the market does very well, the constraint won't matter.) The law could empower the new investment board to inform Congress and the public about any legislation that might adversely affect the Trust Fund; the Senate could expand procedural rules that now protect Social Security from legislation that would use its revenues to finance changes in the non-Social Security budget. A supermajority in the Senate could be required to pass legislation that the board declared would harm the long-run financial viability of the Trust Fund.

If this sounds unrealistic, consider how well the TSP has worked for its members. By holding the S&P 500, the TSP has gotten a high return on its investment. It has done so with considerably lower administrative costs than the typical 401(k) account—and without political interference. In other words, the TSP seems like a perfect model for the Social Security system. So well has the TSP worked, in fact, that it might be worthwhile to consider having a new Social Security investment board hire the TSP overseers to handle its investments.

What about the other half of the privatizers' argument—that individuals will make better investment decisions than the government? Although many people find such logic intuitively convincing, the opposite is more likely to be true.

The vast majority of the public has little experience or understanding of the principles of investment. Survey after survey has shown that even most investors don't fully understand basic investment principles. Appreciating the advantages of diversification, understanding a risk-return trade-off, distinguishing between real and nominal returns—all of these require education, and education is expensive. Merely sending a pamphlet to every worker will not accomplish much. (You could mandate that workers choose from a limited set of investment choices, but then what's the point of having individual accounts in the first place?)

Individual accounts need individual managers, and the managers charge fees. Administrative fees will eat into benefits, and, over time, the impact of even seemingly small fees can be large. For example, an annual maintenance charge of one percent, roughly the average for mutual funds, would eat up about 20 percent of the system's benefits over a typical beneficiary's 40-year working career. So beneficiaries would lose out, unless they invested far better than government would have. Privatizers insist that's possible, but it's common Wall Street knowledge that, over the long term, index funds, which the government would be using exclusively, outperform all but the savviest and richest investors.

So Trust Fund investment in stocks and corporate bonds is good for Social Security, but what would it mean for the economy as a whole? Actually, it would have a positive effect: if the Trust Fund buys private securities, it will have fewer Treasury bonds than otherwise. Thus the first impact of a change in portfolio policy would be that the public, that is, individual investors, would end up holding less in private securities and more in Treasury bonds.

To be sure, this would happen in any system that hitched Social Security to the stock market, whether through individual accounts or through a government body, because money flowing into individual accounts instead of the Trust Fund would not be available for buying Treasury bonds. But, just as private securities bring greater profits, they entail greater risk. And, over the long term, Social Security as a whole can—and will—tolerate more risk than individual investors will collectively. After all, the stock market might fluctuate, but the large Trust Fund will have enough reserves to cover short-term dips. So, in effect, by investing in private securities on behalf of workers, the government would increase the pool of people sharing the risks in the economy.

This is good for Social Security because the riskier investments bring higher returns over the long run. It is good for the economy because it lowers the cost of bearing risk, making it less expensive to finance private investment. And, since direct government investment is good for individual citizens, too, it makes a whole lot of sense—no matter what the stock market does tomorrow.

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Wall Street's vigilante.

GET SHORTY

By Craig Karmin

Hemispherx Biopharma, a little-known pharmaceutical company based in Philadelphia, has struggled to survive for most of its 32 years, accumulating debt and reporting losses for much of that period. Despite working with the prestigious Johns Hopkins University, the company has had virtually no sales.

But the summer of 1998 seemed to bring a long-awaited breakthrough: Hemispherx's drug Ampligen suddenly began attracting national attention as a treatment for chronic fatigue syndrome (CFS). One patient, Richard Wendel, a 45-year-old accountant who says he was diagnosed with CFS four years ago, began participating in clinical trials for Ampligen last December. Almost immediately, he started to feel better. His

memory came roaring back, and his speech patterns returned to normal. "I'm alive again," Wendel says from his home in Reno, Nevada.

Enter Manuel P. Asensio, a wiry, 43-year-old financier who makes his living betting on the downfall of certain stocks. In Wall Street parlance, Asensio is a short-seller. And he's just made Hemispherx his latest target. Pacing in his midtown Manhattan office, he grumbles about the dozens of outraged phone calls and e-mails from CFS patients that day. "I used to call them the perpetually tired," he says. "Now I call them the actively tired."

The day before, September 22, the Cuban-born head of his own investment bank had blasted Ampligen on the Internet as a toxic, "medically useless" drug promoted by Hemispherx management for the sole purpose of defrauding investors. Although the company's publicly traded stock had recently enjoyed an impressive rally, climbing from a price of 4¼ on July 9 to a high of 13 3/16 on September 9, Asensio valued the shares at less than $1, ending his post with a signature "strong sell" recommendation.

As financial reports go, this one ranked among the bluntest and meanest ever offered on Wall Street. But, for Asensio & Company, it was standard issue. In a matter of hours, Hemispherx's stock plunged more than 30 percent to 5¼. "They called me a criminal at least a dozen times today," Asensio says, referring to a conference call the company's management held shortly after the short-seller issued his report.

Asensio bristles at the very suggestion. After months of research, he is convinced that it's the company's chairman and CEO, Dr. William Carter, who's suspect. Asensio says that Ampligen has never been approved by the Food and Drug Administration after 25 years and that other drugs do what it sought to do, only better and more safely. He charges that Hemispherx has been hyping its stock by issuing more than 18 million stock options to brokers and other insiders at a below-market value. And, in his most personal attack, Asensio wrote that Carter stands accused of extorting money from an HIV patient, who says he agreed to purchase $1 million of Hemispherx stock in exchange for admittance to a clinical trial for Ampligen. At the time, the drug was being tested as a treatment for HIV.

Not surprisingly, Hemispherx's management has threatened litigation against Asensio & Company on charges of stock manipulation and attempt to defraud Hemispherx investors. If proved, the charges could destroy Asensio's business, but he is unfazed. "I've made a total of eighteen short-sell recommendations," he remarks. "They all threaten to sue, but none of them ever follows through."

Although short-selling goes back to at least the nineteenth century, the practice really took off in the 1920s, when Joseph Kennedy Sr., father of the future president, used the technique as a way to supplement his rum-running business. Here's how it works: Suppose a short-seller believes the share price of 100 for a company—let's call it Startup Inc.—is too high. He finds someone who owns, say, ten shares of this company, borrows them, and sells them in the open market for $1,000. Three months later (or one month, or ten months), the short-seller's hunch proves correct, and Startup Inc.'s share price has fallen to 50. The short-seller then buys back ten shares for a total of $500, returns them to their original owner, and keeps the $500 difference for himself, minus a small fee to the owner for the privilege of borrowing the shares.

Although it is legal, short-selling is restricted in the United States, and there are many in business and government who wouldn't mind seeing it eliminated altogether. Short-sellers are almost always blamed when any individual stock tumbles, and they were collectively blamed for the crash of 1929 (though a Senate committee eventually exonerated them). Last year, Malaysia, blaming short-sellers for the collapse of its currency, eliminated the practice, and, two weeks ago, Japan took similar measures.

Short-selling is also frowned upon in the financial world, but not because most short-sellers don't play by the rules. They do, though many have been known to give their shorted stocks a push, frequently by firing off damaging (and sometimes false) information about a company via Internet chat rooms. Rather, the short-sellers' bad rep is due to the fact that they only profit from the misfortune of others. They prey on small start-ups, newborn biotech or high-tech firms, assuming fraud or failure where others see bold entrepreneurship.

But short-sellers see themselves as cops on the beat for an industry willfully oblivious to its miscreants. None believes this more emphatically than Asensio, a Wharton and Harvard Business School graduate, whose essay "A Free Market Solution to Persistent Stock Fraud" is posted on his website. In the treatise, he argues convincingly that securities industry regulators and shareholder class-action lawsuits are inadequate. Only short-sellers "possess the resources and incentive powerful enough to combat the strong forces of a concentrated stock promotion.... There is no substitute for the profit incentive."

Wall Street, especially in a boom, is indeed skittish about hurting companies' feelings. Analysts shy away from saying anything that might anger company management, fearing they will be denied access to top executives in the future. Instead, they play up good news and sugarcoat the bad.

Since known short-sellers are usually denied access to company officials, and because many investors will not loan their shares to people they know will short them, most shorts operate quietly. Even the outspoken Asensio refuses to say how many people work for him, revealing only that there are four employees in his Manhattan headquarters and a second office in Washington, D.C., which operates under another name. He relies primarily on outside researchers to provide information on the 300 or so companies he is currently targeting.

But, if Asensio's secrecy resembles that of his peers, his trademark public announcement of companies he's shorting is unheard of on Wall Street. "He's sort of an

agitator, likes to stir things up," said one New York short-seller, who, like most in the business, spoke only on the condition of anonymity. "He hasn't been wrong, but he's a bit of an egomaniac."

It's a week after Asensio's strong sell recommendation for Hemispherx, and, after an initial round of heavy selling, things are not going as planned. The company has mounted a spirited defense, touting the early clinical-trial successes and attacking Asensio by name, a move he terms "unusual." Carter has also managed to convince many people who own shares or stock options not to sell. Hemispherx's share price ends the day at 6, meaning it has actually *gained* ¾ of a point since Asensio's scathing report. "He's done a fabulous job," Asensio says with detached admiration, as if his newest project were a game of chess.

Still, Asensio is confident of checkmate in the end. "Anyone who is a thoughtful investor has left," he assures me. "The people who are still here are involved in ripping off the public. They are inside promoters and paid-for stock brokers who are working the phones and getting paid. In vulgar Wall Street language, it's a stock rig, and it's a very good rig. But rigs always fall apart. If they didn't, our capitalist system wouldn't work."

Few doubt that Asensio is battle-tested; every strong sell report brings a wave of hate mail and Internet denunciations. When Asensio issued a sell recommendation for the oil exploration company Solv-Ex Corporation ("Solv-Ex's plant is ill-designed and will not produce bitumen. Management is corrupt. We believe Solv-Ex's shares will soon be worthless"), he claims the firm sent a detective to follow him and harass his doorman and friends. But, far from being intimidated, Asensio published 27 reports about the company, describing in meticulous detail what he called "management's fraudulent activities." Solv-Ex repeatedly denied all charges—and it continues to do so, even though the company has filed for bankruptcy protection and has been charged by the Securities and Exchange Commission with issuing false and misleading public statements.

It is, however, the story of another company, Diana Corporation, that reveals the true extent of Asensio's influence—and why the climate of excess and hype during the recent bull market has presented him with so many opportunities. In 1996, Diana, an obscure Milwaukee-based meat distributor, announced its new subsidiary was offering computerized switching equipment essential to Internet service providers. The news took by storm investors on the lookout for the next Cisco Systems or Lucent Technologies—or anything that promised to exploit the powers of the Internet. In just three months, shares of Diana skyrocketed from less than 16 to more than 100.

Such a phenomenal run attracted the attention of Asensio, who says he consulted with some of the top software and hardware engineers in the country. After receiving documents and testimony that indicated Diana's technology was merely a reconfiguration of an older, obsolete product, Asensio accused the company of bogus promotion and maintained that the vaunted technology was essentially worthless: Diana's shares plummeted to 20, staged a minor comeback to 40, then sank to single digits. Diana has since been delisted from the New York Stock Exchange, has shed its meat business, has moved to Calabasas, California, and now operates under the name of Coyote Network Systems. Asensio, meanwhile, says his firm pocketed $30 million from the short.

A day after my last meeting with Asensio, the unprecedented happens: a company actually follows through on its threat of litigation. Hemispherx files suit in federal court against Asensio & Company, alleging fraud in an effort to manipulate the price of the stock. The company seeks $320 million in damages—the decrease in the value of Hemispherx's shares since Asensio's sell recommendation plus punitive damages. "I don't know his background; it's possible he's uncovered some misrepresentations in the past, but this time he's flat-out wrong," Carter tells me shortly before the suit is announced. "Mr. Asensio has gone one bridge too far. His core assertions about Hemispherx are wrong on the face."

Asensio denies all the charges, says he's hired an attorney to have them dismissed, and will be countersuing. But, in the court of the investment community, the early verdict is against him. The week after the suit is filed, Hemispherx's share price has rebounded to 8⅞—almost a full point above its price *prior* to Asensio's strong sell report. "It's really an extraordinary performance by them, given the black marks this company has on its record," says Asensio, who goes on to note that most of the companies he's shorted enjoy a temporary bounce after the shares initially plunge.

This reminds me of something Asensio said the week before: "It's a lot easier to get people to believe a story than it is to tear it down." It's an interesting, if counterintuitive, supposition, but one Asensio bases on several experiences. The first was probably in 1961, when he was a seven-year-old boy in Cuba and his father sent him to live with an aunt in Brooklyn. Manuel Sr., "a late believer in the revolution," stayed behind, convinced he was helping to build a new democratic Cuba. "I remember crying and my father telling me not to cry," he recalls. But, not long after young Asensio arrived in New York, his father's faith in the Castro regime would prove misplaced: Manuel Sr. was arrested on trumped-up charges and imprisoned. It would be two years before Asensio would see his father again.

As we return to the subject of short-selling, Asensio's composure has abruptly crumbled, and, for the first time, he appears upset. His face is slightly flush; his dark eyes are burning. His voice starts to rise as he exclaims, "If a man lies, you've got to pull him down and say he's lied." Then he collects himself again. "But, if you're diligent, one source telling the truth can be more powerful than a hundred on the other side. If you see our work, you see reasons to be optimistic about life."

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