LAWSON KROEKER
INVESTMENT MANAGEMENT

As We See It

> "Over the short term the market is like an election and any damn fool with money can vote. However, over the long haul, it's like a scale, and the values will eventually be properly weighed."
> –Benjamin Graham

The bull market recently celebrated its fifth anniversary. A dramatic rise in prices has been associated with this period. In fact, if the Dow closes over 2700 this year (a figure pierced in August) it will have risen of 40% in 1987 alone. The only other years in this century when such dramatic moves have been made were 1908, 1915, 1928, 1933, and 1954. What we have been experiencing is quite rare.

The rise in prices has created a market which now is anything but undervalued. Traditional measurements such as dividend yield, price to book relationships, and the price earnings ratio all suggest caution is in order.

For example, the Standard & Poor's 500 now yields 2.7%. According to the latest Ibbotson-Sinquefield study, the average annual dividend return from stocks over the sixty-one years ending December 31, 1986, was 4.8%. The average annual yield, prior to 1987, varied from a high of 8.3% in 1950 to a low of 3.0% in 1972. Today's 2.7% yield is lower than any of the sixty-one years covered in the study.

Bonds, on the other hand, offer a generous current return relative to returns offered during most of the period. Over the sixty-one years the average annual yield on long-term Treasury bonds varied from a high of 13.6% in 1982 to a low of 2.0% in 1941 with an average of 5.0% As of this writing, long-term Treasury bonds are available at yields approaching 10%.

The Standard & Poor's 500 generated a compound annual total return (dividends, reinvested dividends and appreciation) of 10% during the period covered by the Ibbotson-Sinquefield study. With the current return on long-term Treasuries approaching the total return generated by the stock market over an extended period, bonds appear very competitive in the relative valuation battle.

While traditional measures of valuation suggest the stock market is high priced, they are not useful in predicting its short-term direction nor the duration of the period of overvaluation. For example, during much of the 1960's the market was "overvalued". A sense of value and historical relationships, however, is helpful in making investment choices in the present.

As investment managers we must continue to participate in the markets as we find them. For now we are cautious. Our strategy with respect to stocks is to maintain buying reserves to emphasize stocks with above average yield, stocks which we feel are misunderstood by Wall Street, and stocks in industries which are out-of-favor. Also, we are drawn toward bonds which still offer historically high rates of interest.

At some point, as Benjamin Graham observed, value will prevail.

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