LAWSON KROEKER
INVESTMENT MANAGEMENT

As We See It

"You can observe a lot just by watching"
—Yogi Berra

One of the frailties of human nature is the tendency to find comfort with the conventional wisdom or position. The majority tend to focus on a particular event or idea, pursue it to an extreme, or until their attention is caught by some new folly more captivating than the first. Such herd mentality is frequently seen in the securities markets.

The most pronounced fad at the moment is the takeover/leveraged-buyout mania. The prices paid in one takeover quickly become the benchmark by which additional potential rumored targets are valued. Traditional benchmarks for valuing a company such as its book value, price-earnings ration, or yield are increasingly shunned for more "enlightened" LBO value, takeover value, or private-market value statistics. The increasingly optimistic assumptions underlying the estimates of such theoretical values eventually will drive prices to absurd levels from which disappointments will result.

Another popular idea in today's investment environment is that of asset allocation. Asset allocators are those who use historical data to ascertain the relative attractiveness of cash, bonds, and stocks–positioning portfolios accordingly. Known as tactical asset allocation, this methodology has become very popular, largely because some of these systems had their users in very conservative positions at the time of the October, 1987, crash. More recently, the systems have not worked as well. They pointed to heavy cash positions when both stocks and bonds were doing very well.

The crowd or herd mentality is also illustrated by the increasing acceptance of foreign stock investment. While the U.S. stock market has generated very impressive returns since 1982, many foreign markets have shown even better results. The "faster horse" has gotten the attention of investors and is but one more example of how an idea or strategy becomes increasingly popular the longer it works. However, once the crowd is there, the opportunity presented by that strategy often has passed.

Financial history is littered with examples of the dangers of investing with the crowd. Relying on the supposed rationality of a private or corporate buyer gives no assurance of safety. For example, Chevron and duPont, respectively, purchased Gulf Oil and Conoco at the peak of the energy mania. During the late 1970's and early 1980's asset allocators advocated significant exposure to real estate just as returns from that investment medium were peaking. Many additional examples could be cited.

Investing against the crowd is very difficult as it goes against human nature. Most of us feel more comfortable doing what others are doing. To invest successfully it is important to have a sense of what others are thinking and doing. It is important not because it reveals investment opportunity, on the contrary, it is often a warning of what should be avoided.

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450 Regency Parkway, Suite 410 | Omaha, Nebraska 68114-3701 | *tel* 402.392.2606 | *fax* 402.392.2597 | www.lawsonkroeker.com