LAWSON KROEKER
INVESTMENT MANAGEMENT

As We See It

"It was New York City's worst week. But it was New York City's best week.
We have never been braver. We have never been stronger."

– Mayor Rudolph Giuliani

It seems that each generation experiences a defining moment, a life-changing event that remains indelibly fixed in their minds. It is a moment when, years later, they will remember where they were and what they were doing at the time of the event. For one generation, that defining moment was the attack on Pearl Harbor. For another, it was the assassination of President Kennedy. For the current generation, it is likely to be the September 11th reprehensible terrorist attacks on the World Trade Center and the Pentagon.

Whenever one of these defining moments occurs, we are abruptly challenged in terms of our ability to evaluate the course of future events. There is now a new element which must be factored into the equation, and we are not sure how the future will be altered by that element. We realize our invulnerability has been punctured and a world that seemed safe is now suddenly dangerous. And, since we are not quite sure how this will impact the future, a feeling of uncertainty arises.

As a result of the event, fear and uncertainty appear where confidence and opportunity once reigned. This fear and uncertainty works its way into the stock market very quickly. While over the long term markets move on fundamentals, emotions take over from time to time. Once the stock market is dominated by emotion rather than fundamentals—positive as well as negative—it is likely to go to an extreme. Understandably, the market often overreacts to catastrophes and especially geopolitical shocks. Unfortunately, one never knows in advance how far or long the market will move on emotion.

In today's environment, valuation rules have come into question. The new economics of uncertainty makes growth and earnings hard to forecast, and the proper price to pay for those earnings in doubt. Only one thing is clear: the nature and size of risk have changed, and we are recalibrating them in everything we do.

It is unlikely that fear will dissipate quickly. As with previous generations, we will once again have to learn to live with geopolitical uncertainty. Much of the last half of the last century can be characterized as having considerable geopolitical uncertainty. For those who grew up during the Cold War of the 1950s, '60s, and '70s, there were air raid drills at school, home bomb shelters, fear of a nuclear attack on Offutt Airbase, and occasional crises that heightened the uncertainty. These included the downing by the Soviets of the U2 spy plane, the Cuban missile crisis, and the assassination of President John F. Kennedy.

Additional crises, and the market's reaction to them, are shown on the reverse side in a table compiled by Ned Davis Research, Inc. The table shows that past negative stock market reactions to these crises were usually retraced rather quickly. Following the September 11th attacks, the DJIA declined 14.25%. That decline was nearly retraced by the middle of October. Hence, the market's reaction to this crisis was not atypical. This does not necessarily mean the market has seen its lows. That will be determined by future economic and geopolitical events.

Farther back in our history, pirates—who came from the same part of the world as today's terrorists—were the terrorists of their day as they attacked our shipping and captured our seamen. Pirates were the main reason Congress established a navy in 1794. In 1805, American marines marched across the desert from Egypt, forcing the pasha of Tripoli to free American captives (chiefly seaman). This exploit is recalled by the U. S. Marine Corps anthem: "From the Halls of Montezuma to the Shores of Tripoli." We and other countries continued to conduct raids to suppress the pirates. Eventually the situation was controlled through the colonization of North Africa, the Arabian Coast, and the Persian Gulf by the British, French, Dutch, Portuguese, and Spanish. History illustrates how countries that cannot live in peace with their neighbors and disrupt the prosperity of commerce risk losing their independence within the international community.

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CRISIS EVENTS, DJIA DECLINES AND SUBSEQUENT PERFORMANCE

Event	Reaction Dates	Date Range % Gain/Loss	DJIA Percentage Gain Days After Reaction Dates 22	63	126
Fall of France	05/09/1940 - 06/22/1940	-17.1	-0.5	8.4	7.0
Pearl Harbor	12/06/1941 - 12/10/1941	-6.5	3.8	-2.9	-9.6
Truman Upset Victory	11/02/1948 - 11/10/1948	-4.9	1.6	3.5	1.9
Korean War	06/23/1950 - 07/13/1950	-12.0	9.1	15.3	19.2
Eisenhower Heart Attack	09/23/1955 - 09/26/1955	-6.5	0.0	6.6	11.7
Sputnik	10/03/1957 - 10/22/1957	-9.9	5.5	6.7	7.2
Cuban Missile Crisis	10/19/1962 - 10/27/1962	1.1	12.1	17.1	24.2
JFK Assassination	11/21/1963 - 11/22/1963	-2.9	7.2	12.4	15.1
U.S. Bombs Cambodia	04/29/1970 - 05/26/1970	-14.4	9.9	20.3	20.7
Kent State Shootings	05/04/1970 - 05/14/1970	-4.2	0.4	3.8	13.5
Arab Oil Embargo	10/18/1973 - 12/05/1973	-17.9	9.3	10.2	7.2
Nixon Resigns	08/09/1974 -08/29/1974	-15.5	-7.9	-5.7	12.5
U.S.S.R. in Afghanistan	12/24/1979 - 01/03/1980	-2.2	6.7	-4.0	6.8
Hunt Silver Crisis	02/13/1980 - 03/27/1980	-15.9	6.7	16.2	25.8
Falkland Islands War	04/01/1982 - 05/07/1982	4.3	-8.5	-9.8	20.8
U.S. Invades Grenada	10/24/1983 - 11/07/1983	-2.7	3.9	-2.8	-3.2
U.S. Bombs Libya	04/15/1986 - 04/21/1986	2.6	-4.3	-4.1	-1.0
Financial Panic '87	10/02/1987 - 10/19/1987	-34.2	11.5	11.4	15.0
Invasion of Panama	12/15/1989 - 12/20/1989	-1.9	-2.7	0.3	8.0
Gulf War Ultimatum	12/24/1990 - 01/16/1991	-4.3	17.0	19.8	18.7
Gorbachev Coup	08/16/1991 - 08/19/1991	-2.4	4.4	1.6	11.3
ERM U.K. Currency Crisis	09/14/1992 - 10/16/1992	-6.0	0.6	3.2	9.2
World Trade Center Bombing	02/26/1993 - 02/27/1993	-0.5	2.4	5.1	8.5
Russia Mexico Orange County	10/11/1994 - 12/20/1994	-2.8	2.7	8.4	20.7
Oklahoma City Bombing	04/19/1995 - 04/20/1995	0.6	3.9	9.7	12.9
Asian Stock Market Crisis	10/07/1997 - 10/27/1997	-12.4	8.8	10.5	25.0
U.S. Embassy Bombings Africa	08/07/1998 - 08/10/1998	-0.3	-11.2	4.7	6.5
Russian LTCM Crisis	08/18/1998 - 10/08/1998	-11.3	15.1	24.7	33.7
Mean		-7.1	3.8	6.8	12.5
Median		-4.6	3.9	6.7	12.1

Days = Market Days

Source: Ned Davis Research, Inc., September 2001