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TABELL'S MARKET LETTER April 26, 1965

On November 18th, over five months ago, the Dow-Jones Industrial Average reached an intra-day high of 897.00. On Friday, a new all-time intra-day high was reached at 921.51. Translating this into terms of actual prices of the 30 stocks in the Industrial Average, this means a rise from 89 3/4 to 91 7/8, which is equivalent to just a shade above 2%. This is certainly not a dynamic rise, but considering the news uncertainties during the past five months, it is a creditable performance. The market has chosen to ignore the problems of Viet Nam, the international money risk, the domestic credit picture, and the threatened steel strike, and has concentrated on the very favorable business background and the favorable earnings trend.

In this respect, the market pattern is quite different from the 1957-1961 advance which was based largely on a willingness to pay a much higher multiple for relatively static earnings. The earnings on the Dow-Jones Industrials for the 1955-1961 period were in a six-year plateau between $28 and $35. The price-to-earnings ratio doubled from 12 times earnings at the 1957 low to 24 times earnings in 1961, while actual earnings in 1961 failed to reach the $35 level of 1957.

The overspeculation and overvaluation that existed in 1961 and early 1962 is not present today. At the 1962 low of 525, the Dow-Jones Industrials were earning $33 and selling at roughly 16 times earnings. Since that time earnings have shown a steady increase with $46.51 reported for 1964. In the last two years, the price of the Industrial Average has just about kept pace with the earnings rise. For the last two years, the price/earnings ratio has been hovering around the 19 times earnings level. While 19 times earnings is historically high, it is considerably below the over-inflated 24 times earnings of 1961. Estimates for 1965 range between $50 and $52 on the Dow-Jones Industrials. Taking the lower figure and applying the 16 times earnings that prevailed at the 1962 low would result in a price level of 800 if investor confidence were impaired by outside news developments. Applying 20 times earnings to the $50 figure would result in a price level around 1000. In either event, the price range over the foreseeable future indicates a swing of not more than 10% in either direction.

Under such circumstances, the action of individual stocks is much more important than the action of a general average. This certainly has been the case for the last two years and there is no indication of a change in the selective pattern. This has been borne out by the technical background of the market. Since the Kennedy assassination lows, the market has advanced in a series of rather moderate upward moves followed by a consolidating period and an advance to new highs. During this period, individual stocks and groups have followed diverse patterns. Many stocks reached their highs six months ago while others appear to have just started upward moves. It is a period in which it does not pay to generalize about the market. Selectivity continues to be the key. In our recommended list, we attempt to achieve this goal. The sum total of all issues in the list has acted much better than the averages since the first of the year. A compilation of the price action of the list along with a few changes and additions will be furnished to your Account Executive at the end of the month.

From a general-market technical point of view, the averages indicate a further advance to the 928-930 level. If the technical pattern since 1963 continues, the attainment of this level will result in another consolidating period. In the past, these consolidating periods have been followed by an upside breakout and an advance to new high territory. Obviously, at some point this pattern will change From a technical viewpoint, a change in trend will be signalled by two indicators. One is our breadth index. A divergence between it and the Industrial Average would give a warning signal. This has not happened. The breadth index has been in an uptrend channel since late 1963 and has confirmed each new high in the average. Another indicator is the 200-day moving average of the price of the Dow-Jones Industrials. This average price for the last two hundred days is now at about 874. A breaking of this line would give a warning signal. A downward trend in the moving average itself would indicate a decline of at least intermediate term proportions. It appears unlikely, barring unforeseen news events, that this latter development could occur before at least two months at a minimum.

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Dow-Jones Ind. 916.41
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