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## TABELL'S MARKET LETTER

March 11, 1966

Market action continues interesting. Last Monday saw the Dow-Jones Industrials register the sharpest dip yet on the current decline. The Index was off 14.58 points and an intraday low of 914.81 was reached. This drop was followed by a rally which continued until roughly 2 p. m. on Thursday when the announcement by a major New York bank of a hike in the prime rate aborted what had been, to that point, a strong rise. Another rally attempt on Friday was snuffed out by late selling.

So far, none of this has been particularly surprising. On February 4th, just three days before the Dow reached a peak at 1001.11, this letter pointed out in fairly strong terms, the vulnerability which then existed. Last week, while suggesting that the market might go lower, we stated - "that the bottom of the present decline, when it occurs, will become an important buying opportunity for equities, much as the bottom last June offered the best such opportunity in a number of months". We went on to suggest a list of seventeen stocks to be added to our Recommended List on any further weakness.

At a time like the present, unfortunately, there exists a tendency among market analysts to play a sort of numbers game with the Dow. One pundit says the downside objective is 910; another says a new low would indicate 875, and various other figures are offered for the confusion of the investor. Technical analysis is, unfortunately, not all that precise. One possible downside objective for the Dow was indeed reached at last Monday's low. There are further possible downside objectives in the 910-875 area, most of them centering roughly around 890. What is most important, we think, is that at present levels investment odds are now more favorable than they have been for some time, and that the concern of the investor at the present juncture should be the seeking out of appropriate stocks to be purchased with reserve cash.

One way of demonstrating the present investment odds is to examine stock prices in relation to current earnings. The Dow-Jones Industrial Average earnings for the year just ended probably amount to something in the area of \$53.50. For 1966, it appears safe to take \$60.00 as a reasonable estimate. A study of P/E ratios over recent years shows a few well defined trends. In 1954, investor confidence began increasing sharply, and between 1954 and 1958 the average P/E for the Dow was 19.9. Then, with the 1958-1959 bull market rise the average price earnings ratio climbed to another plateau, and since 1958 the average price earnings ratio for the Dow has been 18.2, with a range of 16.2 low in 1962 and 24.2 high in 1961. Present prices mark the Dow at 17.3 times earnings, a ratio well below the 1958-1965 average.

The following table shows the level of the Dow for three different levels of earnings at five different P/E ratios.

	R	A	T	I	O
	1954-8 Avg	1962-Low	Current	1958-65 Avg.	1961-High
Earnings	13.9	16.2	17.3	19.2	24.2
\$42.80 (1965 less 20%)	594	693	740	821	1032
\$53.50 (1965)	743	867	930	1027	1295
\$60.00 (1966-Est)	834	972	1032	1152	1452

The table is instructive. With the Dow at 1000, as it was in February, it was in a position to increase substantially only if an earnings advance were coupled with a rise in the P/E ratio. Meanwhile, the risk was substantial. A mere leveling-off of earnings, coupled with any drop in the P/E ratio, could have produced severe losses, and an unforeseen earnings decline could have led to a major disaster. At 930, the situation is quite different. Even with stable earnings a rise in the P/E to its average level could produce worthwhile capital gains. If earnings, as expected, increase to \$60.00, even a decline to the 1962 low P/E would yield a price somewhat above the present. Major losses could be sustained only by return of the price earnings ratio to its former plateau of over eight years ago. At the moment, at least, this appears unlikely.

It thus appears far more important at this stage to recognize that the investment situation has been drastically altered, and make plans to take advantage of it rather than playing fruitless guessing games about the eventual low in the Dow-Jones Industrials.

Dow-Jones Ind. - 927.95  
Dow-Jones Rails 254.40

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