TABELL'S MARKET LETTER

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MEMBER NEW YORK STOCK EXCHANGE, INC
MEMBER AMERICAN STOCK EXCHANGE

October 22, 1971

About a year and a half ago, the Institutional Investor magazine emblazoned its cover with the deathless phrase, "This isn't a bear market. This is the way things are going to be from now on." The line tended to evoke nervous chuckles. At the time, the monetary squeeze was exerting its full pressure, the economy was halfway into a recession, the end of which was not clearly visible, and earnings comparisons were proving, to say the least, disappointing. Under the circumstances, a plunge in equity prices was a logical expectation, and plunge they did, with the sickening thud typical of a bear market.

Time passed. Prices bottomed in May, and by August, the obvious signs of a bull market were manifest. The warning, implicit in the magazine cover, was forgotten, as the recession ended, money flowed into the economy, and earnings projections began to improve. As we progressed to the Fall of 1971, the universal expectation was for an improving economic picture for 1972. Yet, in this totally different environment, stock prices were behaving in a manner much reminiscent of the Spring of 1970.

We suggested in last week's letter that such behavior was totally consistent with our conception of supply/demand forces affecting the equity market, and we discussed some of these forces in detail in our letter of September 3. It is worth reiterating them here, however, because it seems important to us to understand just why the market has behaved as it has in the face of a quite obviously improved fundamental outlook. It is arguable, in other words, that this is the way things are going to be from now on.

To begin with, we have to disabuse ourselves of the notion that earnings have anything -- except tangentially -- to do with the aggregate level of stock prices. Now before the foregoing sentence brings the collective wrath of the financial analyst community down on our head, we suggest that it be re-read -- with particular emphasis on the phrase "aggregate level". Earnings, of course, have a great deal to do with the prices of stocks relative to each other. The price of all stocks taken together is something else again. It is obviously possible for this figure to rise when, and only when, demand for stocks exceeds supply, and to fall when, and only when, the reverse is the case.

The demand for all investment media, stocks included, derives ultimately from the rate of corporate and personal savings. This annual savings increment must be divided, in some way, between stocks and other forms of investment. Just how this division takes place cannot, of course, be documented, but it obviously must depend to some degree on prospective rates of return offered by other investments vs. those offered by equities. The division having been made, net demand for equities can be arrived at by subtracting from potential demand the total number of new common stock offerings. The residual figure is what will ultimately exert the upward or downward push on the stock market.

Thus, in simplest terms, if stocks offer high rates vis-a-vis bonds and new offerings of common stock are low, it is potentially bullish for stock prices. If the relative rate offered by bonds (and other investments) is high, and new offerings of equities are at high levels, the implications are negative. This is precisely the case at the present time. Bond yields are well above stock yields and have obviously been attracting fairly substantial amounts of individual and institutional money. Meanwhile, new offerings of equities have been at record or near-record levels since June. Net result -- the stock market posted a high last April and has not been near that high ever since.

Now, as suggested above, this exercise is intended as an explanation rather than a forecast. As we noted in last week's letter, we do not see, in the present picture, the plethora of broad distributional patterns which would suggest a bear market of the 1969-1970 scale. The most plausible downside objective, as we suggested last week, is 850-835, the upper part of which range was touched during last week's trading. Also, on the plus side is the fact that a speculative binge, which normally has to be liquidated in a bear market, never really got off the ground this Spring. Under these circumstances, we think it probable that a near-term bottom may be at hand. Nonetheless, the factors mentioned above will remain with us and should be taken into account in stock market decisions. We think, in other words, that capital protection, as well as capital enhancement, should be a major factor in investment decisions in the months ahead.

Dow-Jones Industrial (11:00 a.m.) 859.08
S&P (11:00 a.m.) 96.29
AWT:mn

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