TABELL'S MARKET LETTER

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We had the pleasure last week of attending a meeting of the Market Technician's Association, a professional organization composed of our fellow practitioners of market analysis and one dedicated to raising the standards of that profession. The theme of the meeting was the growing use of technical analysis by professional investment managers and the conclusion was, indeed, that such use had been increasing. A secondary theme emerged, suggesting that the reason for this increasing use was that, over the past two or three years, at least, technical analysis had been "right" or more useful in determining portfolio policy, while fundamental analysis had been "wrong" or less useful. Now, obviously, as practicing technicians, we are willing to defend the use of technical analysis, but in this case we would also like, at least partially, to defend our fundamentalist brethren. To the extent that fundamental analysis has been "wrong" since the early part of 1973, it is not, in our view, that the principles of security analysis have been incorrect but that inept security analysis has been incorrect.

Let us illustrate what we suggest by this statement. From the first quarter of 1973 through the third quarter of 1974, corporate profits rose steadily, earnings on the Dow, for example, increasing from just over $70 to just under $100. During precisely the same period, the stock market went through the most severe bear market it had seen since the 1930's. In the fourth quarter of 1974, earnings flattened out and will undoubtedly decrease rather sharply in the first quarter of 1975. That same period has seen one of the sharpest rises in the stock market during the postwar period.

To the extent, therefore, that the fundamental analyst has concentrated on forecasting quarter-to-quarter earnings changes and making buy and sell recommendations based thereon, he has, in fact, been wrong. Yet precisely that error has been committed over and over again. It is quite easy to demonstrate the fallacy of this sort of approach in terms of the averages as we have done above, but the mistake tends to be committed more often in terms of individual stocks. All too often buy and sell recommendations are made on nothing more than a projection of increasing or decreasing earnings. The now-thoroughly-discredited "one-decision" theory was nothing more than an extension of this fallacy, suggesting, two years ago, that the favorite growth stocks were appropriate conservative investment vehicles because their earnings were continuing to increase, without regard to the price being paid for those earnings.

None of this, however, is a criticism of security analysis itself. It is simply a criticism of security analysis misapplied. The suggestion that technical work, to the extent that it was able to forecast the market decline of 1973-74 and the subsequent rise in 1975, was correct and that fundamental analysis, to the extent that it failed to anticipate these phenomena, was incorrect, raises some interesting points about the relative roles of the people who are, or should be, involved in portfolio strategy decisions --- the security analyst, the technician and the portfolio manager.

We have often suggested, not entirely facetiously, to our fundamentalist colleagues, a golden rule that the security analyst should be prohibited from ever using the words "buy" or "sell". We are, incidentally, perfectly willing to extend the same prohibition to the technician. It is the third party, the portfolio manager, who should ultimately make the buy or sell decision. Quite obviously, inputs from the security analyst and the technician should be important to him in that decision, but they will not be the sole inputs, since he must also concern himself with the nature and objectives of the funds under management.

What we are saying, in other words, is that it is the role of the security analyst to present facts about individual companies and industries. These facts include shorter-and-longer-range earnings projections, assessment of the factors that might cause changes in these projections, analysis of financial condition and, not least, an assessment of the relative value offered by a given security at a given price both on an historical basis and compared with alternative investment opportunities. All of this can be done without once uttering the two "no-no" words above. The technician, equally, can concern himself with identifying the major and minor trends for an individual security and for the general market and with an assessment of the prospects for a reversal of those trends. This also can be accomplished without specific suggestions of purchase or sale. The portfolio manager, adequately supplied with the inputs mentioned above, coupling them with his own professional expertise and knowledge of the requirements of and risk aversion of the funds under management, is well-equipped to make the ultimate purchase or sale decision.

Dow-Jones Industrials (12:00 p.m.) 783.09
S & P Comp. (12:00 p.m.) 83.79
Cumulative Index (4/10/75) 468.23
AWT/jb

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