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STOCK ANALYSIS

By Heinz H. Biel

No Bed Of Roses

By now we have digested the multitude of economic forecasts for 1970. As usual, they varied a great deal, and the end result is confusing rather than enlightening. However, whether we have a major recession or continuing inflation, or a combination of both; whether we experience a financial crisis or an easing of credit policies, one thing is sure: This is not likely to be a year when the investor can delude himself and expect to rest on a bed of roses.

It is pretty obvious by now that the American economy has stopped booming. Residential construction, except for mobile homes, is in a real slump. Color TV sets don't sell. Automobile production and sales are running well below earlier projections. Retail sales are flat, at best. A growing number of the economists' "leading indicators" have turned negative. Yet there is no sign of a letup in inflation. Prices continue to rise, especially the cost-of-living index, which includes "services" and such items as urban transportation costs (like the 50% increase in New York City transit fares).

Strangely, despite the slowdown in business, which is the intended result of the Federal Reserve's anti-inflationary monetary policies, the rate of unemployment has remained at a low level. While no one wants to see the human misery that goes hand in hand with joblessness, the side effects of near-full employment are the excessive demands of certain labor unions for huge increases in wage rates and fringe benefits. A financially strong giant like General Electric can afford to put its foot down and accept a three-month strike rather than submit to unreasonable wage hikes. But what can the smaller entrepreneur do when confronted by the overwhelming strength of the Teamsters?

It is unrealistic to expect that the cost-push type of inflation, fueled by sharply rising labor costs, can be controlled, or even alleviated, merely through restricting credit, *unless* we are prepared to provoke a depression of such magnitude that massive unemployment will break the power of the labor unions. Obviously for political, social and economic reasons, this is completely out of the question. Since our fiscal policies, as reflected in the new tax bill, also are not anti-inflationary, particularly, too, because of steadily increasing expenditures by the states and municipalities, we had better have no illusions and be prepared for continuing inflation close to the present pace of around 6% a year. This also means that interest rates will not, cannot, decline appreciably, since the lender will always demand a fair return *plus* compensation for inflation.

Investors' Choice

The stock market has been grappling with these problems all through 1969 and may have adjusted itself to present realities such as high interest rates and a profit squeeze for cyclical and labor-intensive industries. Whether the adjustment is adequate is another question, but the market itself seems to say that it is. While a great many individual stocks are still making new lows, the most broadly based averages, like the NYSE index and the S&P industrials, seem to find strong support near the lows of last summer. This is a hopeful sign and the bottoming-out process may be nearing completion.

The lure of exceptionally high interest rates is continuing, of course. Brokers report an unusual amount of bond buying by small investors, but this is probably savings-bank money rather than funds which normally would flow into common stocks. Large investors, whether they be individuals or institutions, undoubtedly have large sums of money sitting on the sidelines, but they invest mostly on a short-term and highly liquid basis, just waiting for the right moment to jump back into the market.

The temptation to settle for a secure, high yield is great, particularly when one has qualms about the stock-market outlook. Yet as soon as a degree of confidence returns, the attraction of the stock market can become difficult to resist. A safe yield of 8% or 10% a year quickly loses its appeal when you can see a chance of making 20% or more in stocks. There are virtually hundreds of deeply depressed stocks that may have little to commend themselves at the moment but will snap back vigorously as soon as the investment climate improves. The near-term outlook for a company like *Chrysler* is uninspiring right now, but 1970 is not the end of everything. It requires little imagination and not much of a bull market to visualize Chrysler selling at 40 (its 1968 high was 72⅞!) or 20% above its current market price.

There is no apparent reason for being or getting bullish at this time, but neither is there cause for increasing pessimism. What was so bearish for the stock market a year ago was the severely restrictive monetary policy of the Federal Reserve, designed to combat inflation. This restrictiveness has its limits. To go beyond such limits and to prolong it unduly can have serious consequences. This opinion is expressed by a growing number of prominent economists, a few members of the Federal Reserve Board and several members of President Nixon's Cabinet. It is not unrealistic, therefore, to conclude that as far as credit conditions are concerned we have seen the worst. Only the timing and the degree of easing remain in doubt. The stock market, which has already shown how sensitive it is to changes in credit conditions, is likely to respond promptly to any visible indication that the Federal Reserve Board is easing up.

The entire country has been aroused by the growing pollution of the air we breathe and the filth in our rivers and lakes. The stock of any company involved in pollution control has skyrocketed, often to levels that seem utterly unsupportable by actual facts ~~and figures and by~~ realistic possibilities. My choice in this group is *Joy Manufacturing*. This stock, too, ~~has had a sharp advance, but even its~~ present price is not unreasonable in relation to S&P's earnings forecast for the current fiscal year of $2.80 a share *vs.* $2.55 for last year. Joy's principal business is specialized coal-mining machinery, and recent legislation for the protection of the miners should benefit this company.

Pollution-control devices account for only a very small part of *Westinghouse Electric's* sales. If this company can escape the kind of strike that has been crippling GE since last October, Westinghouse should have a pretty good year, with earnings holding close to the estimated $3.75 a share for 1969. In fact, if the economy should improve during the second half, profits could approach the $4 level, a record. The division manufacturing heavy apparatus for the utility industry should be working at capacity for some years to come. At a price in the 50s, Westinghouse Electric is a solid investment. ■

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