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# Thoughts for Investors

## FALL NEWSLETTER

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***"Money is of a prolific generating nature. Money can beget money, and its offspring can beget more."***

– Benjamin Franklin

The stories of Year 2000 doom and gloom recently prompted the Wall Street Journal to critique several books on the subject of Y2K preparedness. Each book received a score of one chicken to five chickens (the sky really is falling.) The mild ones recommend such things as reintroducing yourself to your neighbors by taking over food. Wilder ones suggest getting a gun "if you are comfortable with that."

It seems a little extreme to be thinking about arming yourself for January 1st. There is value though in thinking about what lies ahead. So I gazed into my crystal ball, looking for visions of the financial future of the United States of America.

The first thing I saw was a vision of J.P. Morgan who told me "Any man who is a bear on the future of this country will go broke." I also saw five other things that suggest a bright future for this country and continued appreciation for the stock market.

### 1.) Low Inflation

The most visible economic phenomenon of this and the last decade has been declining inflation in the U.S. In the 1970's the consumer's mantra was "better buy it today because it will be more expensive tomorrow." We raised prices to our customers anticipating our suppliers raising prices to us. Today however,

consumers demand lower prices and the mantra is "don't buy it today because it will be on sale tomorrow." We demand lower prices because we know that raw material costs are stable and manufacturing processes are more efficient. The most successful companies are those that oblige. Intel recently reduced the price of its Pentium III chips by 40% and the stock has appreciated considerably. Contrast that with the cereal companies (see summer 1999 newsletter) who relentlessly raised prices over the last decade. Today their stock prices are at all-time lows as unit volume growth rates, and therefore profits, have declined dramatically. Low inflation continues to lengthen the country's expansionary business cycle. This has given U.S. companies the confidence to invest for the future and do it at very favorable costs.

### 2.) Increasing Productivity

Most economists are shocked that U.S. productivity has increased so much. They remain shocked that this deep into an expansion it's still increasing. In fact, nonfarm productivity increased at a seasonably adjusted rate of 4.9% during the third quarter of this year, it's biggest increase since 1992! Long time clients will immediately understand the reason for this. Technology has allowed us to leverage scarce resources (people) as well as abundant resources (computing power). Indeed, technology teaches us that there is no such thing as a scarce resource. In another recent Wall Street Journal article, Brian Wesbury, Chief Economist of Griffin, Kubik, Stephens and Thompson in Chicago points out that several big

contributors to the US's GDP have never been included in that calculation. 1999 will be the first year that software will be included in the GDP. This is also the first year that telephone banking, wire transfers, and the effect of automated teller machines (ATM's) will be included. All these have had a significant impact on productivity for years. Now that they are included, the GDP should continue to expand and productivity should continue to increase.

### 3.) Best Upper Educational System in the World.

There is no question that fine schools, colleges, and universities exist outside the U.S. Yet for sheer number, the U.S. contains the largest, most diverse and best collection of colleges and universities in the world. Operating in a competitive arena as opposed to operating as a protected national treasure, they have differentiated themselves by their curriculum, location, teaching staff, research capabilities and even their job placement statistics. As a result, U.S. colleges and universities have attracted the world's best and brightest students. Furthermore, upon graduation they often remain in this country to fulfill their dreams. Their successes serve to attract more of their countrymen.

### 4.) World's Most Stable and Dynamic Democracy

In yet another Wall Street Journal article, U.S. Supreme Court Justice Antonin Scalia points out that one of the keys to the U.S.'s long running success is not that the majority rules but rather that the minority has the right to be heard. Sometimes it takes the legal system to assure that, other times the press or the internet do the job. The result is an uninterrupted flow of ideas that challenge current practices. History can be a blessing or a curse. For the U.S., our short history (compared to Asia or Europe) means that very little is sacred besides the Declaration of Independence, and the Constitution. Certainly business practices are not sacred. In countries with long histories sometimes-great economic and social

energy is expended in keeping the status quo. I've written before about the significance of the fall of the Berlin Wall ten years ago on November 9. That single political event doubled the number of consumers in the world. The U.S.'s stable and dynamic democratic system is still the only worldwide economic and governmental infrastructure capable of bearing the weight of all those individual needs.

### 5.) Unparalleled access to capital

While many people in the U.S. bemoan the paperwork and taxes required to start a business, the process is relatively easy compared to the rest of the world. Starting a business in India requires a Herculean effort in time, paperwork, patience, payola, and luck. In the U.K. precious start-up capital must be used to protect creditors. Contrast this with the U.S. where capital is usually used only for revenue generation and accountants and attorneys will sometimes accept equity in lieu of cash payments for their services a potential win-win for both sides.

Besides the access to human capital, the U.S. offers unparalleled access to financial capital as well. The U.S. has the most advanced venture capital system in the world. In most countries it's the government that determines what will be funded. This is hardly the best-qualified group to make that decision. Furthermore, if you are not a native your chances decrease dramatically. In the U.S., the government funds only basic research. You and I as individuals own the opportunity to participate in venture funding for new products. This is regardless of our nationality or social background.

In summary, I have a confession to make. I have no crystal ball. There, was no vision of J.P. Morgan. Yet the five items I outlined are real. They continue to point to a bright future for both the U.S. economy and the stock market, be it 2000 or 2001 or 2010.

## AUDI PARTEM ALTERAM

*Hear the Other Side*

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If you would like to discuss the topic of this newsletter, or our team's approach to investing, please feel free to contact us by email at [al.boris@alexbrown.com](mailto:al.boris@alexbrown.com).

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