

Reprinted from:

THE WALL STREET TRANSCRIPT

"The Information Center for Business and Finance"

Published Monday Volume I, III

Number 6

Copyright 1976 by
WALL STREET TRANSCRIPT CORPORATION
120 Wall Street, New York, N.Y. 10005

Single Issue - \$15.00 August 9, 1976 Pages 44,417 to 44,472

PENSION FUND and MONEY MANAGERS

The following discussion with a leading investment manager is one of a planned series of interviews to be presented by The Wall Street Transcript. Through these dialogues in depth, we hope to present to our readers, each week, extensive and informative discussions of industries and topics currently of interest to professionals in the business and financial world.

Of course, as with all views of others published in The Wall Street Transcript, the statement in our editorial box should be noted as it is applicable in its entirety to this conference material. As a matter of policy The Wall Street Transcript does not at any time, in any way, endorse any views, opinions, or statements of others. As a newspaper, we concern ourselves with reporting as accurately as possible what others have said. Their views are their own. Under no circumstances is this material to be construed as an offer to sell, or as solicitation of an offer to buy, any security referred to herein.

Richard A. Holman
Editor and Publisher

TWST: What does The Boston Company of Louisville do, as distinguished from The Boston Company?

Mr. Todd: Well, we're a subsidiary of The Boston Company, operating an investment counseling firm out of Louisville and have a professional staff of about five people, managing mostly pension accounts. We have, approximately \$1.2 billion under management in the Louisville office, a good bit of which is in pension assets of three major state retirement systems: the State of Louisiana, the State of Kentucky, and Kentucky Teachers'. Our accounts range in size from one-half million to \$400 million.

TWST: Now, how much of the money that you're managing is in debt and how much in equity?

Mr. Todd: About \$800 million is in debt, and about \$350 to \$400 million is in equity. Now that is the unique nature of a public retirement fund, which in most of those cases has a very low equity ratio. In a typical corporate pension fund, we manage about \$200 million in corporate pension assets, the typical equity ratio would be more like 60 percent. In a public fund it will range from 20 to 40 percent.

TWST: How do you think that those ratios will change over the years? Will they remain the same?

Mr. Todd: I think they'll come closer together. Because, if you go back 5 or 6 years, you will find that the typical private pension fund had 70 or 80 percent in equities, and the typical public fund, if they had any equities at all, was probably about 10 percent. So they're beginning to move closer together. I don't think they will ever come all the way together because the risk tolerance level of a public fund is less than it is for a private fund.

TWST: How long have you been managing this money?

Mr. Todd: We've been managing pension money in Louisville



BOSWORTH M. TODD, JR. is president and a director of the Boston Company of Louisville, Inc. Born in Frankfort, Kentucky, he received a B.S. degree in Commerce from the University of Kentucky and a M.B.A. degree from the Harvard Graduate School of Business Administration. He served in the Air Force and was subsequently a broker with J.J.B. Hilliard & Son and more recently a vice president of The Kentucky Trust Co. before founding the Boston Company of Louisville, Inc. He has been an instructor in Investments and Corporate Finance at the University of Louisville. He is presently a member of NYSSA and The Louisville Society of Financial Analysts. Mr. Todd, his wife and three sons live in Louisville where he enjoys fishing, golf and jogging in his spare time.

for about 20 years, but we started The Boston Company of Louisville in 1967 and then in 1968 we became the investment advisor to the Kentucky Retirement System. Then, about three years later, the Kentucky Teachers' Retirement System, and then about two years ago, the State of Louisiana.

TWST: What have you read, if anything, that you found particularly interesting on investment strategy, in the last three to six months?

Mr. Todd: There was an article in "The Public Interest" magazine by Peter Drucker, entitled: "Pension Fund Socialism" which was a summary of a book that Peter Drucker has since had published. I think it was one of the most thought-provoking things I've read on this whole area. Basically what it says is that the pension funds will continue to have large cash flow for another fifteen or twenty years, and within the next ten years will end up owning half of common stocks in America. I think that means there will continue to be a two-tier market. It means there will continue to be a steady demand for common stocks, particularly the higher grade type. It's also of interest to us to continue to go after that type of business.

TWST: How do you think you would define the kind of stock that the funds would be interested in? Has the tier one era passed?

Mr. Todd: I don't think the era has passed--I think there will always be a nifty fifty, but just the names will change. You go back and look, as we did recently, at a list of the favorite stocks

ten, fifteen years ago, a good many of the names have dropped off with new names on board. **McDonald's Corp** is now one of the fifty largest stocks in market value in the S&P 500.

TWST: Do you see any signs of new companies getting into the list, Smokestack America, or other kinds of companies that would not have been normally considered a few years ago in the so-called go-go market?

Mr. Todd: I think so, I think you've got really two trends there. One is the arrival in tier one of some former smaller growth stocks. I just cited the fact that **McDonald's Corp** was a few years ago a very small company. Now it pays a dividend, is a very large company, and is considered a seasoned investment. The other trend is the popularity, which I think is a secular, and not just a flash in the pan, for **Smokestack America**. You had, for example, in the fall of last year, both **U.S. Steel** and **IBM** yielding 4%, suggesting that cyclical growth was becoming quite popular, at the same time the traditional growth stocks were getting pretty cheap. This does not mean that U. S. Steel was overvalued, it just meant that this basic area was a new major thrust, which I think will continue, and one reason I say that is what Alan Greenspan said in his Council of Economic Advisors' Report, which was part of the president's economic report in January. He asked the question how much business investment will there have to be in the years ahead if we are to achieve a target of 5% unemployment by 1980, given the assumption of continued 6% real GNP growth, and 4% productivity gains, if, at the same time we are seeking to achieve those noble unemployment goals, we expect to obey the pollution laws and expect to honor the goal of trying to have some form of energy independence, namely keeping oil imports down to 36% of consumption. He pointed out that in the past three or four years business investment had only been running about 10.5% of GNP. His answer was, that if we expect to achieve our unemployment goals, capital spending is going to have to run at least 12% of GNP over the next four years. Therefore, I think that companies in the basic industry are going to continue to do well, even beyond this market cycle.

TWST: What segments of the market on the equity side do you see outperforming the stock market over the next six months to a year?

Mr. Todd: Well, I would be more comfortable looking out over the next year, year and a half, or two years. I still think that your basic stocks, including steel, chemicals, and papers, are going to continue to show good relative performance. I think some of the growth stocks that have been neglected will outperform the market, including such things as **IBM**, which I think has been neglected for years, and then some turnaround growth stocks, which have got some new products under way, which would include **Procter and Gamble** and **Eastman Kodak**.

TWST: Do you think that these market performers will be the same sectors that will outperform the economy on a sales and earnings basis?

Mr. Todd: Yes, I do. I think that every bull market and every business cycle has its own personality. I think that in 1970-72 it was the glamour growth stocks, the consumer non-durables, because they were better able to withstand the problems that were unique to that economic period—the problems with capacity shortages, difficulty in raising prices, stop-go economics, the hangover of a war, and an overvalued dollar, so that in that period the nifty fifty was **Avon** and companies of that type. This time around, it's an entirely different sector. In fact, I think the last seven or eight years are not really very meaningful in trying to get a handle on what may lie ahead. I think it's more useful to go back into the late fifties and early sixties to get a feel of the type economy we may be experiencing now.

TWST: What do you find then?

Mr. Todd: Well, you found interest in aluminums, papers, chemicals, steels, automobiles. For example, take **General Motors**. I think **General Motors** will outperform the market. It's been underperforming the market for years, until recently. But look at what's begun to happen there. Number one, for many years, from the early sixties up through 1973, you had the imports gaining a rising share of the market in the automobile industry. That not only took away a share of the market, it put a lid on the price increases that they could enjoy. With the revaluation of the dollar, plus the rising living standards in Germany and Japan, where hourly labor rates there are not that much different on a currency-adjusted basis from our now, you now would pay more for a Rabbit than you would for a Vega. As a result, more of the revenues of the automobile industry will filter down to the domestic manufacturers. Furthermore, I think they'll be able to get through price increases. They will also be able to disguise price increases by virtue of the fact that you're downsizing the big car. For example, I think **General Motors** can take out about a hundred and sixty dollars of manufacturing costs just by reducing the length and weight of the Buick LeSabre or the Oldsmobile Delta, and that's only a small factor this year, it's only about 18% of the 1977 model, but it will affect 90% of Detroit's output by the end of the decade. So I think **GM**, which has had a 6 or 7 dollar average earning power over the last 6 or 7 years, will have an average earning

power of 9 or 10 dollars over the next 3 or 4 years, and will probably pay up a 5 or 6 dollar dividend.

TWST: What do you think is the case for basic industry? Why do you see them outperforming sales and earnings-wise?

Mr. Todd: In most cases in basic industry, you still don't have prices that they get for their goods up to a level that will attract new investment. The paper industry still does not get a price that could justify significant new investment. Neither does the steel industry and neither do some of the other areas in that basic group. I think there's more to go and this is an area, obviously, that has to be watched. I think the steel industry has a lot longer way to go in terms of having to get price increases that will justify new what they call "greenfields" plant expansion and they may not get that far. I think if the basic-type stock has had it in this market, as some people fear by virtue of recent weakness in **Dow Chemical** and some of the others, then I think this bull market is over. But I don't think the bull market is over. But I think the thing to watch for some sign of this third up let in the market coming is to watch for some sign of revival in the basic stocks.

TWST: What do you think will trigger that?

Mr. Todd: I think just the passage of time and renewed confidence that the economic recovery, which is a very normal one, is intact, plus the fact that I think the market is hesitant because it knows so very little, really, about Jimmy Carter.

TWST: What do you think would be the reaction if he is elected, as seems likely?

Mr. Todd: I think the market will mark time for a while until it gets a better feel of what his economic policies are. I read this morning in the "New York Times" that he had a dinner yesterday with some business leaders here in New York, and had some conciliatory remarks to say, but at the same time I was a little bit frightened to read recently that he had to be talked out of his earlier goal of 2% interest rates, so I think he's got an educational job ahead of him to learn the realities of interest rates and inflation potential and unemployment goals that are realistic. I just don't think that we can have 2 or 3% unemployment, which I think was one of his targets. But interestingly enough, I am told that one of his economic advisors, recently had a meeting with one of the well-known labor leaders in this country who wanted to find out what was Jimmy Carter's thinking about economic matters. Upon hearing the advisor recite the traditional party platform platitudes, the labor leader said, "I really don't want to talk about that. I want to know what is Carter going to do to provide business incentives that will provide the jobs that will get the private sector moving again." Now that's refreshing. I think we've come a long way. I think labor has seen what's happened in England and doesn't want to see a repetition of that here. I think this is going on all over the world.

TWST: How do you go about focusing in? Are there primary factors that attract you to a company, that you look for?

Mr. Todd: Well, we rely pretty heavily on reports we receive, the research studies that we receive from our friends in the street, plus the people in Boston. I think if we have a good feel of the economic overview this pretty well dictates the direction we will go in looking at particular stocks and industries. In a diversified portfolio we are trying to, in effect, starve the weaknesses and feed the strengths of various economic sectors. If the paper industry is attractive, as we believe, then we emphasize it. If the type problems we're having in the economy are high raw material costs, this may adversely affect cosmetic stocks. Or, in the case of railroads, or drug stocks, the problem may be excessive regulation. Thus, we diminish investment in those areas. For one thing, they may have been the popular group last time around, and may not present the relative value this time. Then too, we look at the charts to see if there are any signs of market interest, some early signs of relative strength.

TWST: What do you think might turn out to be some of the surprises in the marketplace for the rest of the year?

Mr. Todd: That's a good question. I think there will be some disappointments. We are beginning to see some now. Yesterday there was an earnings disappointment in **Ingersoll-Rand**, and recently in **Dow Chemical**. The market is very sensitive to any shortfall in the earnings expectation. This bull market is getting a little bit mature. It dates from either October or December, 1974, and will be two years old in another few months. You've already had an 80% move in the market, so you're now entering the tired phase where it's more selective and becomes increasingly skeptical. It's hard for me to say at this point without the benefit of hindsight what stocks are likely to have the disappointments. But I think that's what's beginning to now happen.

TWST: Is your overall reaction bullish towards the market?

Mr. Todd: It's bullish, but it's mildly bullish. I would say this: I would go along with the consensus view that the market probably has another 10% on the up side left in it, 10 or 15%, over the next 6, 8, 9 months, but where I differ from a lot of people is that I don't think the subsequent correction will be all that bad. I think market timing, which now seems to be coming into vogue, is something very few people have done successfully in the past. It's something that with hindsight should have been used more in the recent break, when you had a 50% decline in

the market. I don't think it's nearly so relevant in the next bear market. I think the next bear market may be no more serious than what you had in '62 and '66 when you had about a 20% decline over a few months, a subsequent recovery later that year that recouped most of what you'd dropped. I think it's more important that you identify the values that you want to be in and try to ride them through. I think the buy-hold philosophy is right for this market. It was wrong, obviously, in recent years. I really think that, looking out over the next 7 or 8 years, you've got substantial under-utilized capacity in this country that's going to be used; you've got a lot of excess labor to be utilized; and I think you've got a Federal Reserve that's on a course to provide a steady policy on money supply to provide the funds to finance the growth. So, I don't see that we're in for anything serious. If we have a recession in '77, it will be a growth recession, where the real GNP would plateau for a couple of quarters. This might give us a '62-type market break, but '62 was different from what we're having now. We don't have an overvalued market this time. Back in '62 we had IBM selling at 60 times earnings. Now it's 17 times earnings. So I don't think that we've got the type of speculation, either in small stocks or speculation in the P/E ratios of big stocks, this time around, to cause much concern.

TWST: Where would you say, if anywhere, that you're most contrary to what you perceive to be accepted positions on the street?

Mr. Todd: I would say a greater interest in bonds than, and traditionally we've had that interest in bonds, more so than most money managers, and they have treated us very well and we're glad we've had that interest. We were dragged into the bond market without really that much knowledge or interest but quickly developed the capacity because at the time we got into it, interest rates were about 6 1/2%, and very shortly after we got in the business, interest rates were 8 or 9%, which was historically competitive with the total return on stocks. And we felt that there was an excess supply of bonds because there was a tax deduction incentive to business to sell bonds instead of stocks. At the same time, we had been in a bull market since 1942, and the yields on common stocks were down to 3%, simply because there was a scarcity of new offerings of stocks. Business really didn't have the incentive to sell additional stock. So there was a distortion of current investment return, and therefore we felt that a more conservative balance was better.

If there's anything other than consensus opinion in our thinking besides bonds, I guess it's that we're more heavily weighted in basic stocks and have been for some time.

TWST: What do you see as the case for pro and con investing in bonds now?

Mr. Todd: Well, I think that the case pro bonds is that high grade bonds maturing in 8 or 10 years will give you an 8 1/2% return, and that's a contract, that's not a hope, which is what you're getting when you buy a stock. Because, let's face it, half of the expected return on common stock is hope that the growth will in fact materialize that will give you a total return competitive with bonds. The return that's available on a high grade bond is not much less than it is on lower grade bonds, about one per cent less. The return on the more stable bond, namely the bond in the 5 to 10 year area as opposed to the 25 year bond, offers a very small sacrifice in yield. You can get 8 1/4% on intermediate maturity as opposed to 8 3/4 or 9% on a longer-term bond. So we don't think you're being amply rewarded for the additional risk of price volatility for the longer term. However, I will admit that the Pension Reform Act suggests broad diversification as an investment policy. Therefore I think there should be some longer maturities in a bond portfolio, although they should not dominate it.

TWST: What do you see as the drawbacks to bonds now?

Mr. Todd: Well, the drawbacks to bonds, I think, is that the total return on bonds over the next 10, 15, or 20 years is likely to be less than for common stocks. I recently saw an article in "Pensions and Investments" quoting a new study by Ibbotson and Sinquefeld in which they projected that the total returns on stock would be about 4% a year greater than bonds over the next 20-30 years, so that maybe you'll get 6% real return on stock and 2 or 3% real return on a bond. If inflation stays around 6%, this implies a 12% return on equities.

TWST: Getting back to the stock market, what have you been selling in the last six months?

Mr. Todd: Well, we sold Utah International because we were disappointed there in the change in the political climate in Australia where 80% of their earnings are derived, and shortly thereafter we noticed that Utah decided to sell out to General Electric. I think that we've also been disappointed in utility stocks. Some of the utility stocks have been very disappointing, and we've sold some of the medium grade utility stocks. We still like American Telephone and one or two of the higher grade electrics, such as Texas Utilities, Public Service of Indiana...

TWST: What have you been buying?

Mr. Todd: Well, we still like Dresser Industries, where we see that that company fits in with our strategy on basic industry. It's about 10 times earnings. We think earnings will grow at

least 15% a year for the next 3 or 4 years because they had strong demand for their basic compressor business, both in this country and abroad, both for general industry and for the energy industry. I think that International Paper continues to look attractive. One high flyer that we reluctantly buy because it's 30 times earnings is Hewlett-Packard, but we're intrigued with what that management has accomplished, with their seemingly superior technology, and mini-computers, which I think will continue to be a rapidly growing area. I think McDonald's, at 20 times earnings is attractive. Now that it pays a dividend, it will take on additional sponsorship from buyers that traditionally could not buy a non-dividend paying stock. It still has a good bit of room for growth. I don't see why it can't continue to grow at about 20% a year for the early future years.

TWST: Have there been some stocks that you have been interested in that you did a preliminary study of and then rejected?...

Mr. Todd: Yes.

TWST: ...and you find there's any pattern?

Mr. Todd: There doesn't seem to be any pattern. We looked at Coors, for example, and decided to pass, first, because we saw that Anheuser was going to get more aggressive, and second, Philip Morris bought into Miller's, introduced "Lite" beer, and gained a significant market share. They're building some new plants, and we felt "Lite" was a product quite similar in concept and marketing style to the Coors line. We also were concerned by the fact that 90% of the Coors stock was still owned by the family, so that you have a pretty thin market. That's really what I think stopped us on that one. We looked at Polaroid when it was depressed and decided to forget it, which hindsight proves was wrong, because the stock has shown some recovery. But we were concerned that Polaroid was going to face increased competition from Kodak, which has happened, and which may take a while longer for that competitive position to stabilize, although I don't think Polaroid is by any means dead. We looked at Xerox when it was down because we owned it and were thinking about averaging down. We decided to keep what we had but not add to it, because they had similar problems--competition from both IBM and Kodak in their traditional lines. There's evidence that they got out of the computer business in order to focus their energies in competing in the copier business with their new competitors. We still think the jury is out on how Xerox is doing in maintaining their market share, but we're a little bit concerned. We're watching it very carefully.

TWST: Any other companies that you took a look at and...

Mr. Todd: Well, there's a stock that we've looked at and decided not to add to it. I guess every major institution owns it, and that's General Electric. It just doesn't seem to have the rate of growth that would justify the price-earnings ratio. Typically, it's had a growth rate of about 8% a year, and it seems to be selling at about 14 or 15 times earnings, a 2.8% yield, without really all that much visibility. Look at their consumer-durable line. We don't see that they've done all that much in their consumer-durable line. I think Sony has done a better job than they have in gaining market share in TV, for example. I think Whirlpool has done a better job in some of their hard goods, although I do think GE will do well in providing equipment for the energy industry.

TWST: What in your view do you feel is unique about your money management philosophy?

Mr. Todd: I don't know that our philosophy itself is so unique today. It was unique a few years ago because it was conservative. I don't think a conservative philosophy is particularly unique today. I think the nature of the type of business we have is unique, in the fact that 90% of our business is in managing a small number of large pension funds, particularly public funds. We are somewhat unique in that we have achieved a satisfactory result for those accounts because we were conservative when it was unusual to be this way. Also, I guess that our running a billion dollars out of Louisville, Kentucky, is a bit unusual, particularly when much of our cash flow is going into corporate bonds. We do spend an awful lot of time in the corporate bond area.

TWST: Do I take it that you see, even from this point, increasing institutionalization of the marketplace?

Mr. Todd: Very definitely. And I think the thing that made me realize that that was going to continue was reading that Drucker article which really pointed to the fact that we, by virtue of the youthfulness of the pension fund industry, still have 15 or 20 years to go before it becomes a mature industry. Now the only thing that worries me about the viability of pension fund industry and the growth of institutionalization of money is that I worry about the viability of the Social Security System. I recently saw a memo by Arthur Laffler in which he described its problems of underfunding. He talked about the unfunded past-service liability of the Social Security System amounting to about 2.7 trillion dollars. Well, that didn't mean much to me until I figured up that it amounted to about \$30,000 debt per family. When we talk about a 500 or 600 billion dollar federal debt, that's peanuts compared to the Social Security System. Well, what that really means is that I will never get my

Social Security checks. It will eventually become strictly a welfare system. The only way I will ever get anything will be if they advance the age that I receive benefits to age 68 and/or make it taxable income, and do some other things of that sort. But I think it's one of the reasons why I'm concerned about the pension fund industry because I think the pension fund industry is, by and large, in strong shape. The Social Security System is not. I do not think that they will ever merge the two, but I do think that we've got some problems ahead to deal with on Social Security and we've got to either tell the American people we're going to have to break our promise to give you Social Security checks, or our grandchildren are going to be paying 40 or 50 percent of their salary in Social Security deductions.

TWST: What are one or two of the stocks you own now where you think you are most alone in right now?

Mr. Todd: Well it would have to be, just by virtue of its small size in the marketplace and its large size in our own accounts, **Dresser Industries** or perhaps **U.S. Steel**. Although **U. S. Steel** has been the darling in the marketplace in the recent past, I think it has a lot of nervous owners. We're less nervous about it than I think most people are. It's only about five times next year's earnings.

TWST: Do you see any major change in the economy over the next year either up or down?

Mr. Todd: No, I think the recovery we've had this year to date is very healthy and on track for continued growth at least through '77 because, you know, it was up nine percent in the first quarter. People were a little bit apprehensive because it was up about half that in the second quarter. Well, what you've really had is a six or seven percent growth in the first half, which is in line with what everyone was projecting for the year as a whole. So, I think we're on track for a very normal recovery and I don't see where there are any problems: We're not fighting a war; floating currencies do work; Europe is recovering; Portugal did not go communist; we haven't had any war in the Middle East; the wholesale price index has come down slightly in each of the last three months and I think those who've talked about the disinflation scenario may have something there. I think you have to be an old man to be bullish in this market as **Barton Biggs** and **Peter Bernstein** recently said. The older fellows are pretty bullish. It's the younger people that are spooked by any run up in the market.

TWST: Where do you put yourself?

Mr. Todd: I put myself in the old man's category; I'm pretty bullish.

TWST: What kind of reading do you like to do in general? To keep up with the marketplace?

Mr. Todd: Well, I think the **Wall Street Transcript** is a good publication to start. I guess, in addition to the usual things like **The Wall Street Journal** and **The New York Times**, there are a couple of interesting things that I do read. One is the **Media General Financial Weekly**. Another is **Harvard Magazine** which started out as an alumni magazine and now has become a right interesting magazine for general reading. For example, they had an article on "The Future of the Economy" that was extremely interesting. It pointed out that there's really no energy crisis because the number of hours you have to work to pay for your gasoline is no more now than it was in 1968. So that's a false problem. There's no such thing as leisure, according to the article, because there are more people working for pay now than there were 20 years ago. People would rather work harder to have the money to have a motorboat than to work less and have a canoe. There were a lot of frothy things like that in the article that made you think. For example, Sweden and Denmark will soon have a higher living standard than we do. Just as we passed Britain as the most prosperous nation in 1900, we too are likely to be passed by some other smaller European nations in the next few years. This may make us wake up to the fact that we've really got a fundamental problem and that is the three percent growth rate in this country is too low. I don't know what we'll do about it.

TWST: What do you think it ought to be?

Mr. Todd: I think it ought to be closer to five or six but you've got to quit eating your seed corn in order to achieve it. You've got to save more and spend less. I think we spend too much on housing in this country. We let the consumer spend too much. We let the government spend too much. And I think if you look at Japan, you will notice their government is a very much smaller portion of GNP than it is in this country. Their savings rate is much higher and as a result their plant reinvestment is much higher. That's the whole secret of it. I think as more economists in this country start to study the economic miracle of Japan, they may learn some lessons from it.

Other publications that I think are worth reading include **The London Economist**. Once in a while they'll have a real stimulating article, "America's Third Century" by **Norman Macrae**, was a recent article in there.

TWST: What do you find is your best source of investment ideas now?

Mr. Todd: I would say that the best source comes from a handful of analysts that we talk to, both in the Street and in Boston, and people that we've worked with for years and know very well. I particularly like to come up and see them on a face-to-face basis as I did today, when I talked to a few. And they will come down to Louisville. You know Wall Street has discovered mid-America. So they're in Louisville two or three times a week to see us.

For general reading I like **Business Week**, **Fortune**, **Forbes**, **Barron's**, to get some background. I think **New York Magazine** has interesting articles in it. I will read that each week simply because of its writing style--it's fun to read.

TWST: Do you think there's been any change in investment approach following ERISA -- any meaningful change that you can transfer to the marketplace?

Mr. Todd: There is one interesting phenomena that's come out of ERISA which can be documented. This comes from **A. G. Becker**, their measure of these pension funds is that 1975 was the first bull market where the equity ratios in pension accounts did not rise. The median commitment to equities among pension accounts declined from 71% at the end of 1974 to 66% at the end of 1975 in spite of a bull market.

TWST: What does that mean to you?

Mr. Todd: That means that pension funds are increasingly risk-averse. They now realize that the Pension Reform Act has much to say about fiduciary responsibility. Furthermore, its passage coincided with the trough of the roughest break in the stock market since 1937, a 50 percent decline. People realized they hadn't made any money in the market in 10 or 15 years. Management in many cases realized that their pension contributions were now a much higher portion of reported earnings than in the past. Their volatile pension returns made long range budgeting difficult. So, I think today they want more assurance of the return, realizing that the price for that may be a lesser return. Hence the interest in bonds and guaranteed contracts and in people whose stock philosophy is market timing. I think market timing is important. I think it can be overdone, because if a market timer misses the first few months of the recovery of the market, he's missed half the percentage move... If he waited till March or April to get it back into the market he missed half of the move in the bull market. The Dow went from 580 in December '74 to about 780 by March '75. Well, that percentage move was substantial, more than the subsequent move from 780 to a 1000 today. I also find it ironic to look back and see that the crowd is usually wrong. It was just about two years ago this time that **Harry Browne**, the well-known writer of the book on "How You Can Profit From the Coming Devaluation", the implication of which I guess was to buy gold, filled Carnegie Hall for his speech, at \$100 or \$200 a seat, when gold was a lot higher than it is now. That gloom contrasts with back in '66, '67, when **Bache** was oversubscribed several times over with their underwriting of the new **Manhattan Fund**, the growth fund that **Jerry Tsai** managed. He had achieved a very good reputation in managing growth money. His successful underwriting subsequently led the mutual fund industry to spawn a whole host of small growth funds which in turn led to the excesses of '68. Well, all that's been unwound. I don't see any sign at this point of excesses taking place in the stock market. Maybe some of the speculative interest that would be there has been drained off into the options market.

TWST: What about options? Do you use them in any way?

Mr. Todd: We have not used options; we have thought about it and we probably will go into options in the future but I must admit that we're reluctant to do it and if we do, it will be to use it as a conservative supplemental tool such as selling a spread of calls against long positions in a pension account to provide some incremental income. We would consider options once the Congress passes a law exempting pension accounts from being taxed on their option income.

TWST: You were talking about the enabling legislation.

Mr. Todd: I think once the enabling legislation is passed, we probably, along with every other pension fund manager, will take a close look at providing the additional service to clients of developing an option strategy for them. I think at this stage of the bull market it is probably a pretty good time to do that. The bull market's beginning to get tired and if you're ever going to sell calls against your long position now is the time to do it. I think it should be an area where you use judgment and maybe don't sell options against everything you own. I think the other use of options is -- I've seen this to be very effective -- where an individual, in a high bracket, has got a low cost concentration in a stock, one which has had a big run in the market. He would like to sell it but hates to pay the capital gains tax and still likes it for the longer term. Instead he sells some calls against it. He recognizes that if he's wrong he can always deliver his own holding. I have seen a good bit of that done.

TWST: Thank you very much.