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I can't argue with the methodology that my friend, and a regular contributor to this report, Michael O'Higgins, follows. Essentially, he buys out-of-favour stocks and other relatively depressed asset classes. And had you followed the advice he has provided to the readers of this report since March 1999, you would have done extremely well, and without taking any major risks. I therefore think that it will be well worth your time to read the following piece, which is brief and to the point.

Beating the Dow with Value

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For those of you who don't know anything about me, I am a US-based money manager who entered the investment business as a stockbroker in early 1972, the last year of the "Nifty Fifty" mania, and got a quick, albeit quite expensive for my clients, education on the dangers of overpaying for stocks during the ensuing 1973-74 bear market, in which the market averages declined by 48% and the average high p/e growth stock, of which my employer, Spencer Trask & Co., was one of the prime promoters, fell over 80%. It was that traumatic experience which led me to develop the "Dogs of the Dow" strategy, which I later exposed to the investing public in my best-selling book, *Beating the Dow* (HarperCollins, 1991), and to start my own money management firm in early 1978.

Since then, I have tended to be a more cyclically-oriented value investor who normally restructured his portfolios annually at year end and held the positions for the following 12 months. This investment approach has worked reasonably well as the performance of my flagship offshore fund shows (see Figure 1).

Recently, however, I have begun increasingly to believe that, once something is bought cheaply enough, it may need never be sold or at least not for many years. Part of this change is due to the obvious success of such outstanding long term investors as Warren Buffet. But it is also due to my observation of the performance of many of my own investments AFTER I have sold them and replaced them with other seemingly more undervalued securities. This idea was further confirmed recently when I reviewed the performance to date of the recommendations that I have made on four different occasions to the readers of the *Gloom, Boom & Doom Report* (GBD) over the past seven-and-a-half years.

Figure 1 O'Higgins Fund Limited
(August 31, 1997- December 10, 2007)

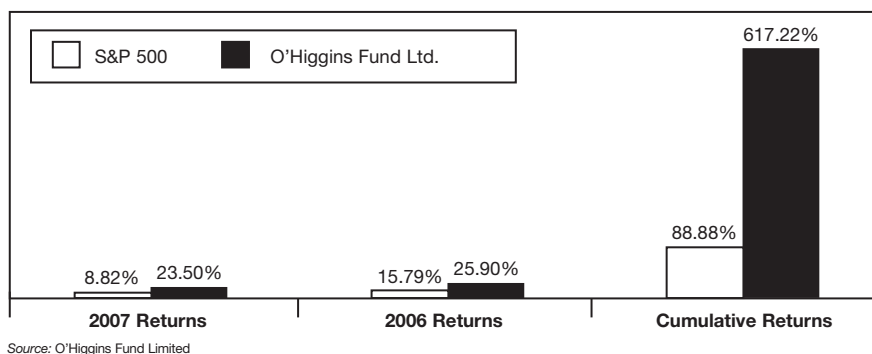
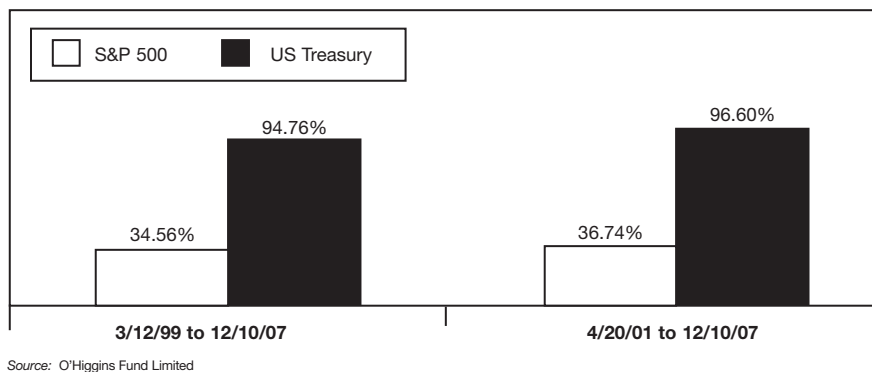


Figure 2 Beating the Dow with Bonds



In my first two GBD pieces, "Beating the Dow with Bonds" (March 12, 1999) and "The Outlook for Stocks vs. Bonds" (April 20, 2001), I pointed out how much cheaper bonds were than stocks, how the declining price of gold was forecasting a benign inflation environment and how much long term US Treasury interest rates were likely to decline given their historical relationship to the long term rate of inflation. The investment which I recommended to capitalize on this forecast was long term US Treasury 0% Coupon Bonds. As can be seen from Figure 2, an investor who followed my advice at the time and held on until today would have earned over three times the S&P 500 total return from either of those dates.

My third GBD article, "Beating the Dow

with Gold" (February 28, 2003), alerted its readers to a major shift in the inflation outlook which the price of gold was signaling. Gold, which at US\$850/oz. in January of 1980 was almost exactly the same price as the Dow Jones Industrial Average (DJIA), had fallen to 1/44 the price of the DJIA (\$250/11,000) by the summer of 1999 and was still very cheap at 1/23 the DJIA (\$350/7,991) in February of 2003 as the article was being written. Given the fact that over the longer term the price of gold had averaged close to 1/10 the price of the Dow, it seemed reasonable to anticipate that the gold's price could easily more than double over the next several years even if the Dow Jones merely stayed at the then depressed level of 7,900. Furthermore, because gold mining stocks normally move three

Figure 3 **Beating the Dow with Gold**

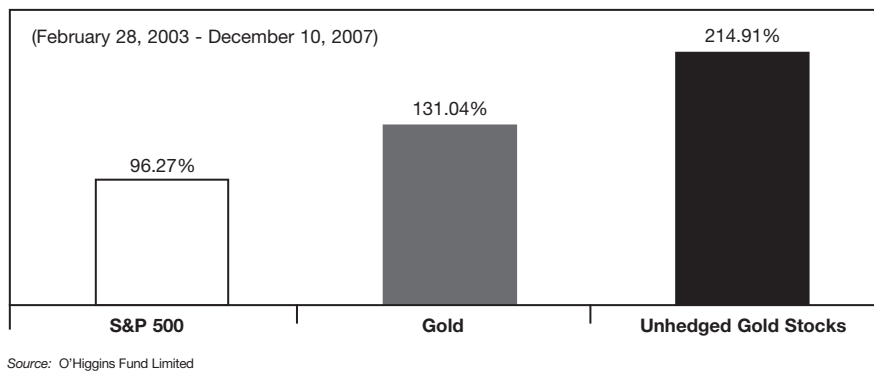


Figure 4 **Beating the Dow with Dow Dogs**

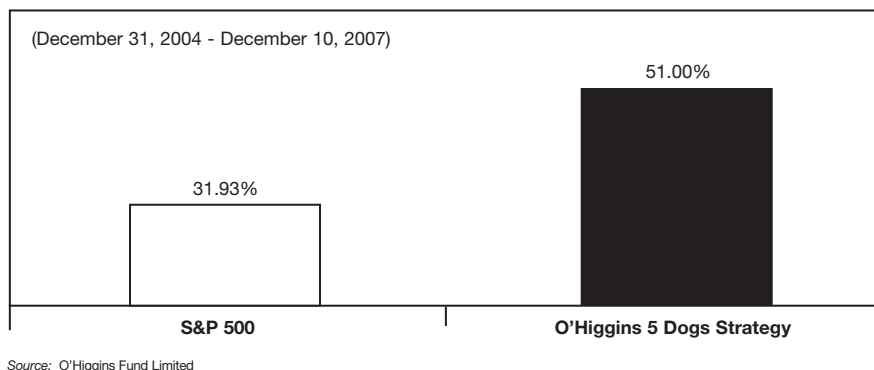


Figure 5 **Dogs of the Dow: Comparative Historical Returns**

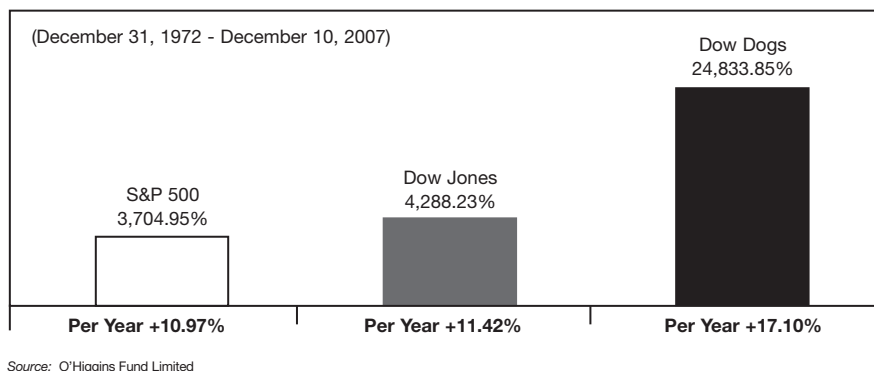
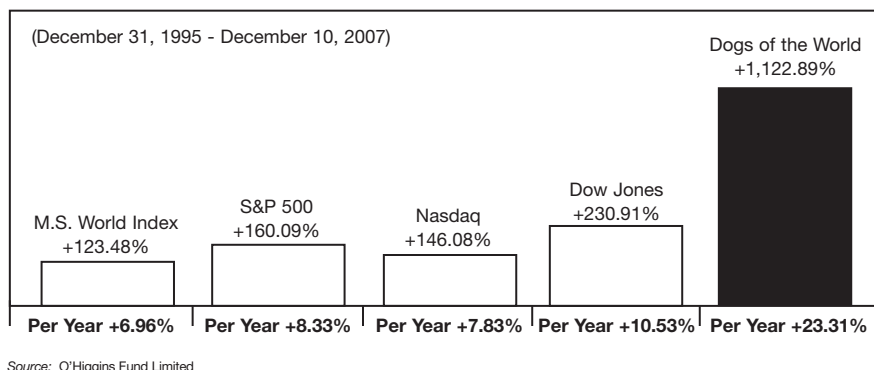


Figure 6 **Dogs of the World**



to five times faster than the underlying metal, an investment in a portfolio of unhedged gold stocks should do even better. Since then, the price of gold has risen by 131% to \$808/oz. and a portfolio of unhedged gold mining stocks would have returned 214.91% while the S&P returned 96.27% (see Figure 3).

More recently, in January of 2005, I contributed another article to GBD entitled "Beating the Dow with Dow Dogs" in which I explained how, because of the decline in long-term interest rates and the rise in the earnings yield (e/p) on common stocks, stocks were once again fundamentally more attractive than bonds for the first time since the third quarter of 1980. As a result, I suggested that my pet "Dogs of the Dow" strategy would be a viable way to "beat the Dow". Since then, my Dow Dogs have produced total returns of 51% while the S&P returned 31.93% (see Figure 4).

So where does one find "value" in today's investment world? In my view, given that the main focus of the current US Federal Reserve Board remains one of fighting DEFLATION, investors should avoid bonds entirely and concentrate on investments which can protect them from a rising inflation rate – i.e. stocks and commodities. Within those two categories, we have our portfolios invested equally among four themes: (1) the **Dogs of the Dow** (C, GE, GM, HD and PFE); (2) the **Dogs of the World** (EWK, EWI, EWQ, EWN and TTF); (3) **Precious Metals & Mining** (PMPX); and (4) **Energy** (ENPIX).

Why do we view these investments as representing "value" in today's marketplace? Well, my five Dogs of the Dow, a strategy which has outperformed the Dow by over 60% annually since 1972 (see Figure 5), are trading at roughly 50 cents on the Dow Dollar relative to their 2000 highs and yielding almost double the DJIA in dividends. My five Dogs of the World, a strategy which has returned nine times the return of the MSCI since 1995 (see Figure 6), are selling at roughly a 1/3 discount to the S&P on a valuation basis. Gold, despite having almost tripled since we originally bought it at US\$280/oz. in January of 2002, remains at a substantial discount to the DJIA at its present ratio of 1/17 compared to the long term average of 1/10 and Crude Oil, while having gone up nine times since its 1998 low, and probably double from here if India and China, which are currently consuming approximately two barrels per person – up from 1 bbl/pp in 1990 – annually compared to 25 bbl/pp in the US and rates in the teens in most other developed countries, continue to grow at anywhere near their current rate and the growth in the supply of oil continues to trail demand.

Time will tell if I'm right but that's my story and I'm sticking to it.