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WHEN TO HOLD 'EM AND WHEN TO FOLD 'EM – PART II – EXAMPLES

The following examples are anecdotal, meant only to illustrate the application of the foregoing techniques, not necessarily to prove their efficacy.

PRICE MOMENTUM AND *VALUE LINE* "TECHNICAL" RANKS — LUCENT TECHNOLOGIES

Lucent Technologies was the Bell Laboratories division of American Telephone & Telegraph, spun off to the latter's shareholders in 1996, after which it became the world's most widely held common stock. Adjusting for splits and spin-offs, from the time the stock was initially traded in 1996 to its high on March 6, 2000, Lucent rose over ten-fold, from $7.40 per share to $76.10 per share. On July 28, 2000, at a price of $65, *Value Line* dropped its "Timeliness" rating on Lucent from a #2 to a #3. On August 16, 2000, at a price of $41, while still a "Timeliness" #3, the service dropped its "Technical" rating on the stock from a #3 to a #4, at which time, it might have been classified as a "Bad #3." It was not until October 20, 2000, at a price of $21 per share, that the "Timeliness" rating dropped to a #4. By the end of 2000, Lucent was selling at $10.98 per share; by the end of 2001, it was selling at $5.14 per share; and, before the end of 2002, the stock was selling at 55¢ per share. Had we purchased Lucent at its peak, but sold it when its "Technical" rank went to a #4, our loss would have been held to 31%, rather than the 99% loss experienced by those who rode it to its bottom in 2002.

PRICE MOMENTUM AND *VALUE LINE* "TECHNICAL" RANKS — ENRON

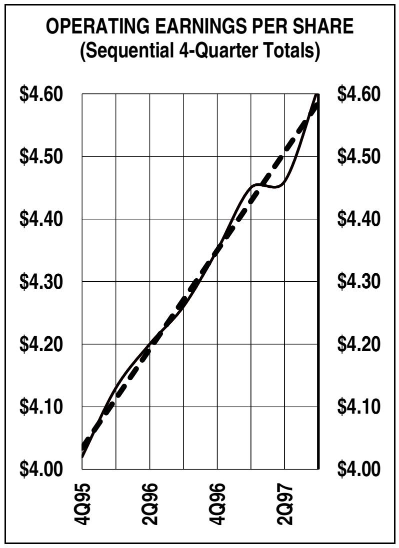
Enron's price peaked at $90.75 per share in August 2000. On December 15, 2000, at a price of $72, Enron's "Timeliness" rank was downgraded from a #2 to a #3. On May 4, 2001, at a price of $62.88, while still a "Timeliness" #3, Enron's "Technical" rank was downgraded to a #4, in which case it might have been classified as a "Bad #3." On June 22, 2001, at a price of $49.62, Enron's "Timeliness" rank still remained a #3, but its "Technical" rank was downgraded further, to a #5, in which case we might have called it a "<u>Very</u> Bad #3." In November 2001 (ironically, while still rated A- for quality by *Standard & Poor's)* the price of Enron's stock fell to 25 cents per share, and the company filed for bankruptcy. Had we purchased Enron at its peak but sold it when its "Technical" rank dropped to a #4, our loss would have been held to 31%, rather than the 99.7% loss experienced by those investors who rode it to the bottom.

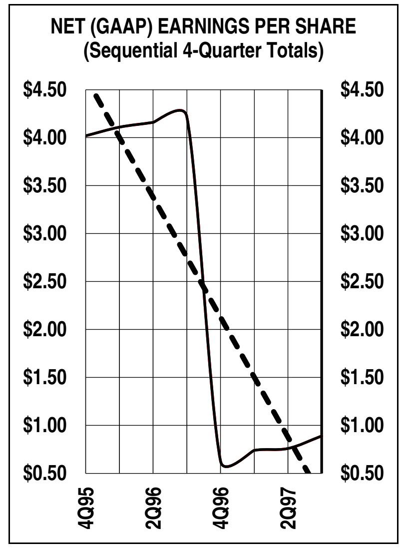
INDUSTRY CONTAGION AND *VALUE LINE* INDUSTRY RANKS — SIERRA PACIFIC RESOURCES

On March 15, 2002, at a price of $16.70 per share, Sierra Pacific Resources, an electric utility serving parts of Nevada and California, carried both *Value Line* "Timeliness" and "Technical" ranks of #3. The electric utility industry was troubled, however. Out of the 97 industries and sectors into which the *Value Line* service then categorized the stock market, electric utilities in the west were ranked #81, utilities in the central part of the country were ranked #84, and eastern utilities were ranked #85. There was a good case, then, for classifying the stock as a "Bad #3." On March 17, 2003, Sierra Pacific sold at $2.85 per share, having lost 83% of its value over the previous twelve months.

"OPERATING" VERSUS "NET" EARNINGS — GOODYEAR TIRE & RUBBER

Goodyear Tire & Rubber provides an example of a company with chronic and sizable write-offs. The first chart to the right shows the company's operating or core earnings as reported by *Value Line* for eight quarters between 1996 and 1997. The second chart shows the company's net earnings without any adjustments for these "so-called" non-recurring gains and losses, as reported by *Standard & Poor's* over the same period.

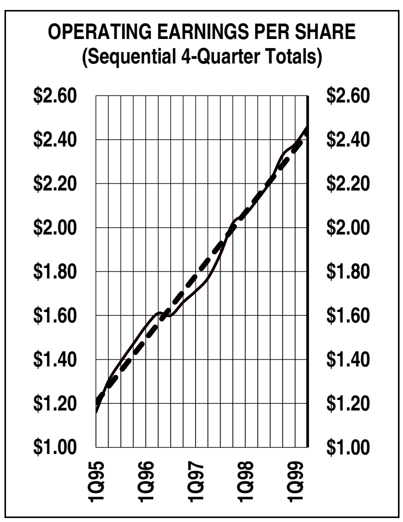


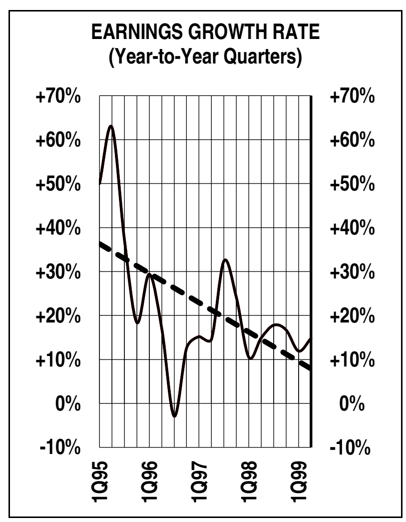


Clearly, operating earnings indicated a company on a track of sustained growth, while net earnings seemed to reveal a company getting deeper and deeper into trouble. The latter seems to have been the case. In late 1997, shortly after the last of the data points for the above charts became available to the public, Goodyear Tire was selling at over $63 per share. By early 2003, its price had dropped to $3.35 per share, a decline in value of 95% over the period.

TRENDS IN EARNINGS GROWTH RATE — XEROX

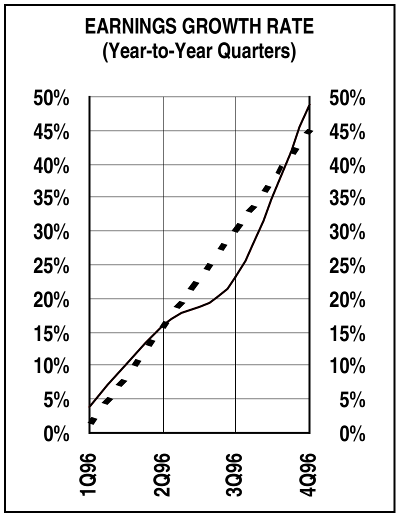
As seen in the first of the charts to the right, Xerox's earnings rose steadily over the four years between early 1995 and early 1999. The company's rate of growth, however, was slowing dramatically over this period, as indicated in the second chart. In May 1999, the stock hit a high of $63 per share.

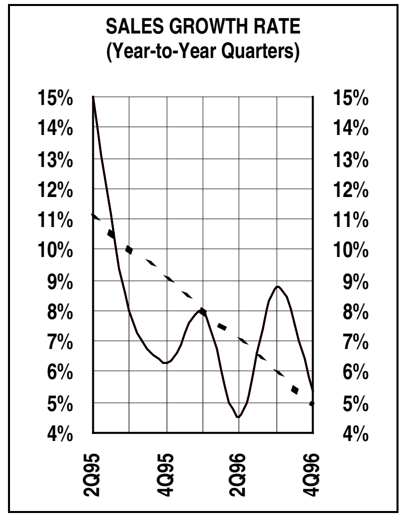




In the second half of 1999, earnings comparisons went negative. Operating earnings were down 94% in 2000 and in the red in 2001. Net earnings, in fact, were in the red in both years. The price of the stock went into free fall, bottoming out in December 2000 at $3.75 per share, a decline of 94% over the 19-month period. It would clearly have been more helpful to Xerox shareholders to have extrapolated the trend line in the second chart, rather than the one in the first chart.

TRENDS IN SALES GROWTH RATE — EASTMAN KODAK





As seen in the first of the two charts to the right, at the end of 1996, it was apparent that Eastman Kodak's earnings were growing like gangbusters and that the rate of growth was even accelerating. As seen in the second chart, however, the rate of growth in sales had been in a secular decline for two years.

On February 19, 1997, shortly after release of the financial statements that put the last of the above data in the public domain, Eastman Kodak's price peaked at $94.75 per share, and it has been in an almost steady decline ever since. On September 26, 2003, the stock made a new low of $20.39 per share, for a decline of 78% over the past six and one-half years. Clearly, earnings growth is not the whole story when we are trying to foretell the future. Sales growth is even more apt to be a leading indicator.

INSTITUTIONAL HOLDINGS — FORD MOTOR

Ford Motor's price peaked on April 19, 1999 at $67.87 per share. About a year later, at prices in the neighborhood of $50 per share, major financial institutions began to exit the stock. They continued to be net sellers over a period of fourteen months in 2000 and 2001 until 37% of those that had held Ford at the beginning of the period were out of the stock completely at the end of the period, at which time the stock was selling at about $30 per share.

MAJOR FINANCIAL INSTITUTIONS HOLDING STOCK	
S&P Report	**Number**
Mar-01	1,011
Feb-01	1,204
Jan-01	1,204
Dec-00	1,227
Nov-00	1,360
Oct-00	1,350
Sep-00	1,314
Aug-00	1,545
Jul-00	1,553
Jun-00	1,563
May-00	1,598
S&P Source: Vickers Stock Research, covering approximately 4,500 financial institutions, including banks, college endowments, insurance companies, investment companies, and "13F" money managers.	

Though somewhat delayed in their action, the move was a good one for those institutions that made it, in that the stock continued to decline, making a low on March 11, 2003 of $6.58 per share, 90% below its 1999 high and still well below the prices received by those intuitions that sold. The monthly changes in the number of institutions holding Ford Motor over the period, as reported by *Standard & Poor's*, is presented in the adjacent table.

INSIDER TRANSACTIONS — JETBLUE AIRWAYS

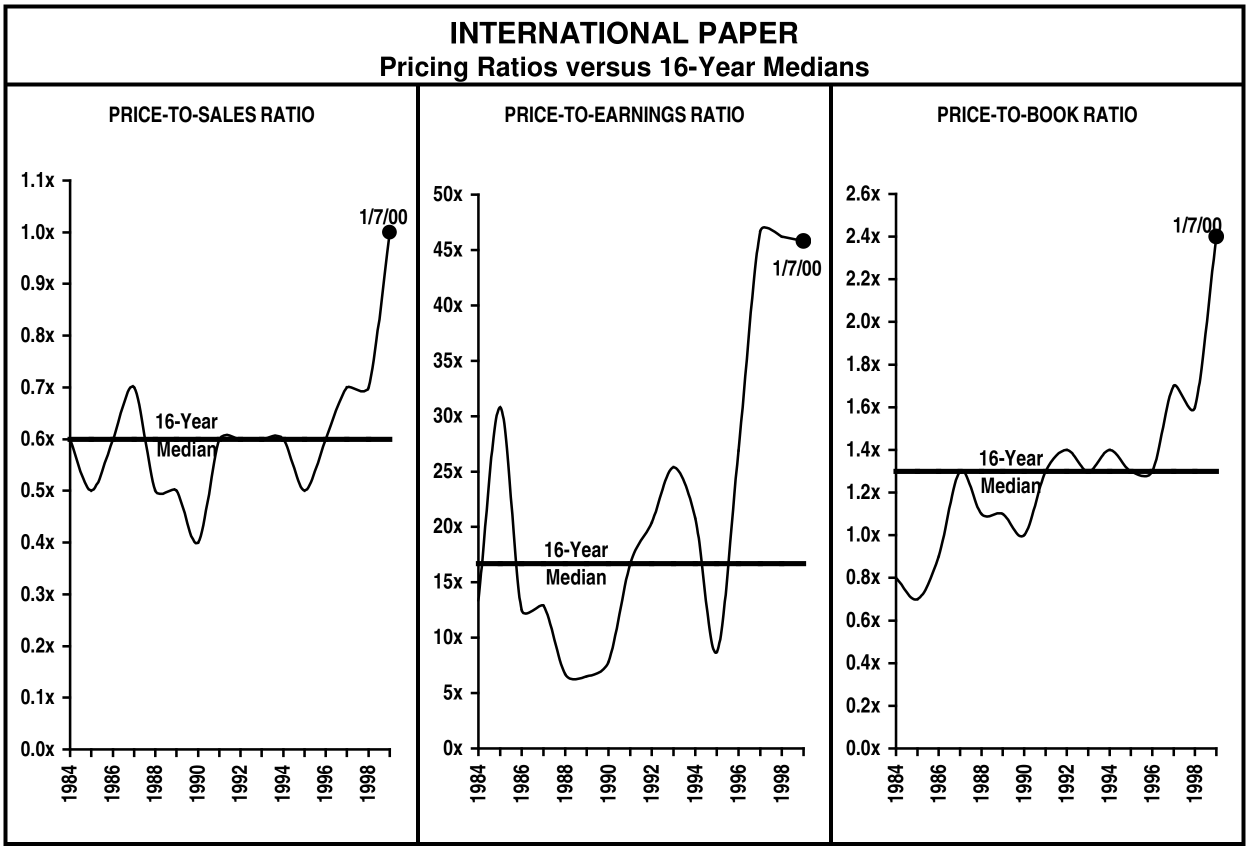
JetBlue shareholders might have benefited significantly by reacting to published insider activity in their company's common stock in 2003. The price of JetBlue peaked on October 9, 2003 at $70.72 per share. Between January 1, 2003 and October 8, 2003, there had been 91 open market sales of their stock by insiders and only 3 purchases. The total shares sold amounted to 2.7 million, of which 1.5 million was sold by George Soros in June. There were 30 times as many sales as purchases, and the total number of shares sold was over 100 times the 25,600 shares purchased. By December 5, 2003, the stock had sold as low as $25.44 per share, and so had lost 64% of its value in fewer than sixty days . A summary of this insider activity appears in the table below:

JETBLUE AIRWAYS					
INSIDER OPEN MARKET TRANSACTIONS					
Period	Ending	Sales	Purchases	Sales-to-Purchase Ratio	
10 months	10/8/03	91	3	Trades	Shares
Total Shares Traded		2,722,733	25,600	30-to-1	106-to-1
Average Trade		29,920	8,533	-	3.5-to-1

VALUATION — INTERNATIONAL PAPER

Cyclical companies tend to lend themselves well to valuation tests. The paper industry historically has been among the more faithfully cyclical of industries, and International Paper has tracked its industry well.

Following a twelve-month rise from $39.27 on January 29, 1999 to a peak of $60.85 on January 7, 2000, International Paper's price per share was 1.03 times its sales per share, as compared to a median over the previous 16 years of 0.59 times; its price-to-earnings ratio was 12.2x, as compared to its 16-year median of 6.6x; and its ratio of price-to-book value was 2.4x, as compared to its 16-year median of 1.3x. It could have been argued, then, that, on the basis of these three yardsticks, the stock was selling anywhere from 75% to 175% above its traditional value. These three measures are charted below:



Ten months later, on October 17, 2000, the stock had declined 54% to $28.25 per share.

Bubbles — Nortel Networks

The chart on the opposite page provides a fourteen-year history of the growth of the common stock of Nortel Networks, its development into a major bubble, and its subsequent collapse. The upper graph shows the price of the stock, and the lower graph shows its R^2P/E.

Though Nortel had formed a minor bubble in 1993, the stock would probably not have been owned by a *Value Line* subscriber during that time, since its "Timeliness" rank had dropped to a #5 just prior to formation of the bubble, and it remained a #5 throughout the duration of the bubble. During the preceding four years, however, the stock's R^2P/E was relatively stable and its price had more than doubled.

Between 1994 and 1999, the stock rose nearly fivefold, from an adjusted $4 to about $20 per share. Because the R^2P/E remained relatively stable in the 1.0x to 1.5x range over this period, we might classify this portion of Nortel's rise as "legitimate" (meaning that it could be justified by a rise in Nortel's earnings and/or the rise in the market as a whole that approximated the rise in the price of the stock).

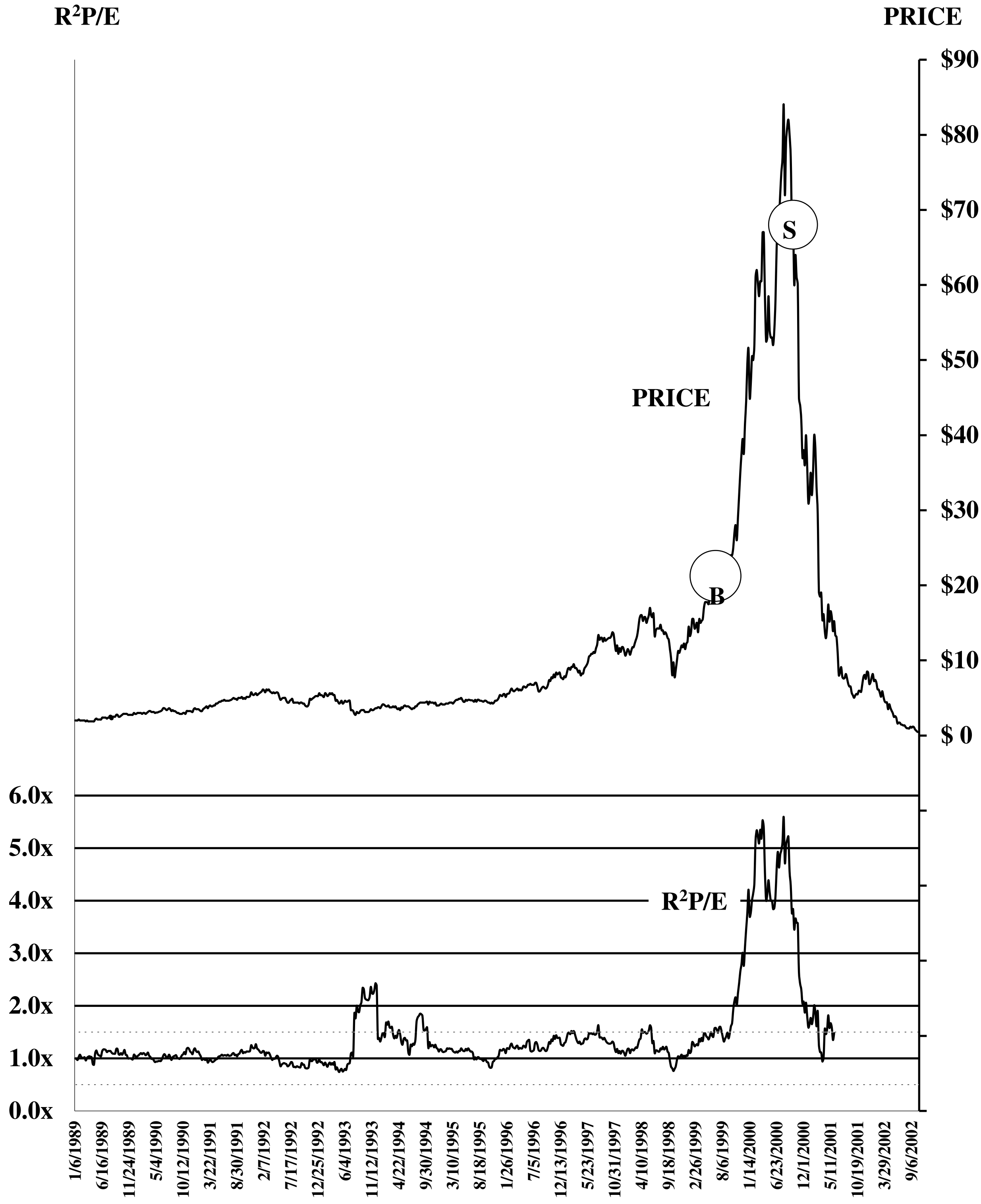
Nortel became a major bubble on June 24, 1999 at a price of $24 per share (indicated by a **B** on the chart) when its R^2P/E broke through the 1.5x level and began a sustained rise. On July 25, 2000 the stock hit an all-time high of $86 per share.

The sell signal for a stock in "bubble phase" came just two months subsequent to, and 21% below this high, on September 29, 2000, at a price of $68 per share (indicated by an **S** on the chart), when the *Value Line* rating was downgraded from a #1 to a #2.

For any who missed the first sell signal, it was followed by two more. The second came on November 24, 2000 at a price of $37 when the *Value Line* rating went from #2 to #3; and a third came on February 23, 2001 when the *Value Line* rating experienced an unusual two-step downgrade from a #3 to a #5, at a price of $29.55 per share. (Nortel's earnings turned negative in the second half of 2001, and so its R^2P/E is undefined from that point forward.)

Nortel continued to tumble until it reached its low of $0.43 per share on October 10, 2002, 99.5% below its all-time high, 99.4% below the first *Value Line* sell signal for a "bubble," 98.8% below the second sell signal, and 98.5% below the third.

NORTEL NETWORKS



NOT THE BEST WAY TO PICK A MONEY MANAGER

Let us suppose that we spent 1999 New Year's Eve studying the past year's performance of mutual funds. By selecting funds that went up the most in 1999, we theorize, we shall be selecting the best managers and therefore stand the best chance of doing well going forward.

Our 1999 stars were the following:

MUTUAL FUND	1999 TOTAL RETURN
Berkshire Focus Fund	+143%
PBHG Technology & Communications Fund	+244%
ProFunds-Ultra OTC Fund	+230%
Van Wagoner Post-Venture Fund	+237%
WWW Internet Fund	+167%
Average	+204%

We invest $10,000 in each, for a total of $50,000.

Lo and behold! See what happened:

	Total Return				VALUE OF ORIGINAL
MUTUAL FUND	2000	2001	2002	2000-2002	INVESTMENT
Berkshire Focus Fund	-16%	-72%	-59%	-90%	$1,000
PBHG Technology & Communications Fund	-44%	-52%	-54%	-88%	$1,200
ProFunds-Ultra OTC Fund	-74%	-69%	-70%	-98%	$ 200
Van Wagoner Post-Venture Fund	-21%	-60%	-65%	-89%	$1,100
WWW Internet Fund	-57%	-52%	-49%	-89%	$1,100
Average/Total	-42%	-61%	-59%	-91%	$4,600

Our $50,000 went to $4,600 - a loss of 91% on our original investment.

It would appear that some money managers may be in need of a better discipline for deciding when to sell.

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