From Wall Street To Tractor Pulls

With apologies to Eric Clapton...

What'll you do when you get poorer
And they've been ripping off your hide?
You've been buying and holding much too long.
You know it's just your foolish pride.

> *Dow Jones, you've got me on my knees*
> *Dow Jones, I'm begging, darling please*
> *Dow Jones, darling won't you ease my worried mind*

I tried to call it a correction
When the bubble came on down
Like a fool, I fell in love with you
And read the chart as upside down

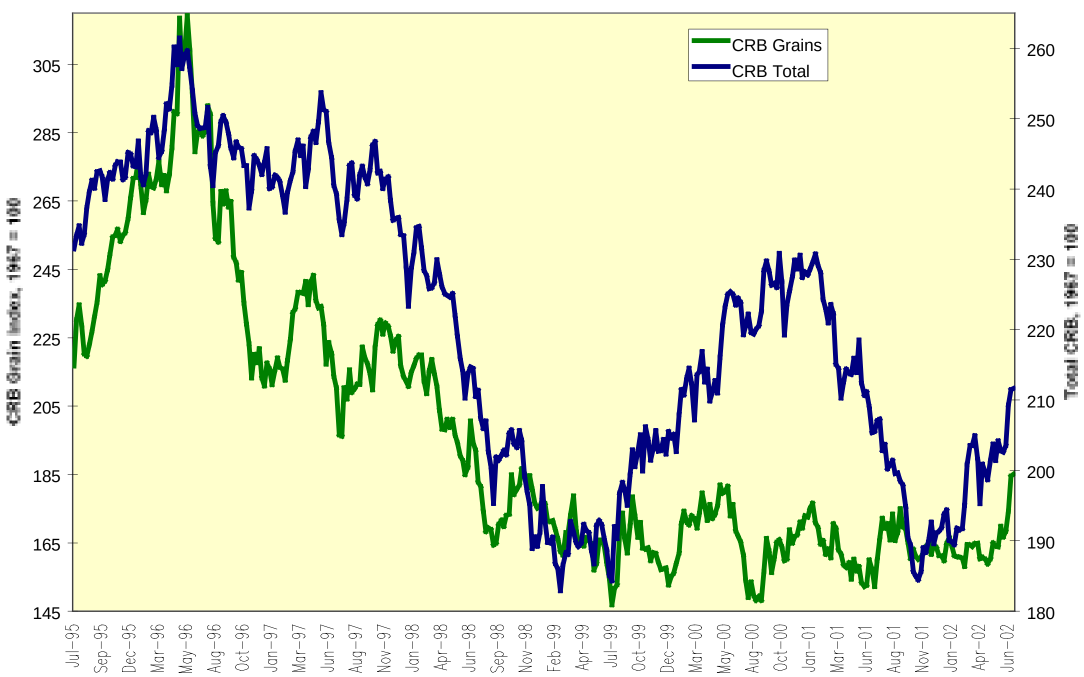
> *Chorus*

Let's make the best of the situation
Before I finally go insane
Please don't say you'll only go one way
And flush my money down the drain

The last time we had a market this bad at this point in the year was 1970, also the year the above-referenced *Layla And Other Assorted Love Songs* was released. While the broad market recovered to make a new high in January 1973, it would not cease its wandering in the wilderness until August 1982. And that was in nominal dollar terms during the worst prolonged inflationary episode in American history.

But there's always a bull market somewhere. Even today, owners of bonds, real estate and precious metals are doing fine. And, for the first time in six years, we have the makings of a sustainable grain price rally due to the weaker dollar, increased farm subsidies, and the residual effects on agricultural investment of years of weak prices. In addition, the perfectly awful financial status of Brazil and Argentina may disrupt the increasingly important Latin American crop this coming winter. Moreover, grain prices have not participated in any of the recent moves higher in either energy or precious metals: They have some room to run.

Can Grains Catch Up?



As sure as day follows night, the prime beneficiaries of higher farm commodity prices will be the suppliers of farm equipment. Next, banks will be eager to extend credit for fencepost-to-fencepost planting. This and speculative attention will drive farmland prices higher and lead to a fiscal crisis on the farm. Hollywood celebrities will pick up the banner and produce a new generation of cloying banker-as-villain films, possibly starring Britney Spears as the hard-working farm wife. The asteroid won't be able to hit too soon.

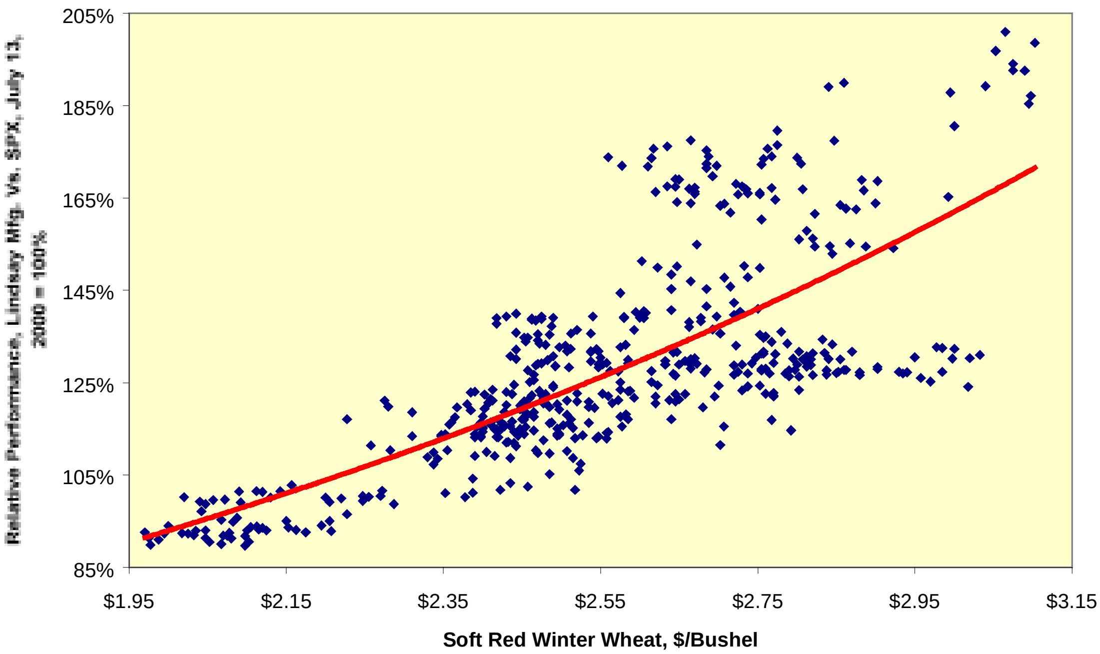
Oh, Deere

That will be then, this is now. The farm machinery stocks haven't done too badly at all in the midst of the recent carnage. Deere, which is known best for its bean-green tractors, is down 0.25% on the year, which beats the more construction-oriented Caterpillar's 12.9% loss. But as we move into more specialized equipment, the returns get quite good. AGCO, which adds hay tools, sprayers and forage equipment to the mix, is up 10.65% in 2002, and a whopping 76.3% over the past year. CTB International, which produces automated feeding, watering and ventilation equipment, has a 2002 return of 3.95% and a one-year total return of 28%. Lindsay Manufacturing, which makes irrigation equipment, has a 2002 return of 21.4%. Want more? How about Paul Mueller, which makes dairy-related equipment: It has pulled ahead by 10.3% so far in 2002.

That sound you hear is the laughter from the feed store telling you that ain't mud on your boots, city slicker.

Per the patterns noted so often in this space, we should expect these equities relative performance to the S&P 500 to rise and fall as a call option on their underlying commodity. Let's take Lindsay Manufacturing's relative performance as a function of wheat prices; wheat often is grown on land too dry for corn or soybeans.

(Artificial) Rain Makes Grain



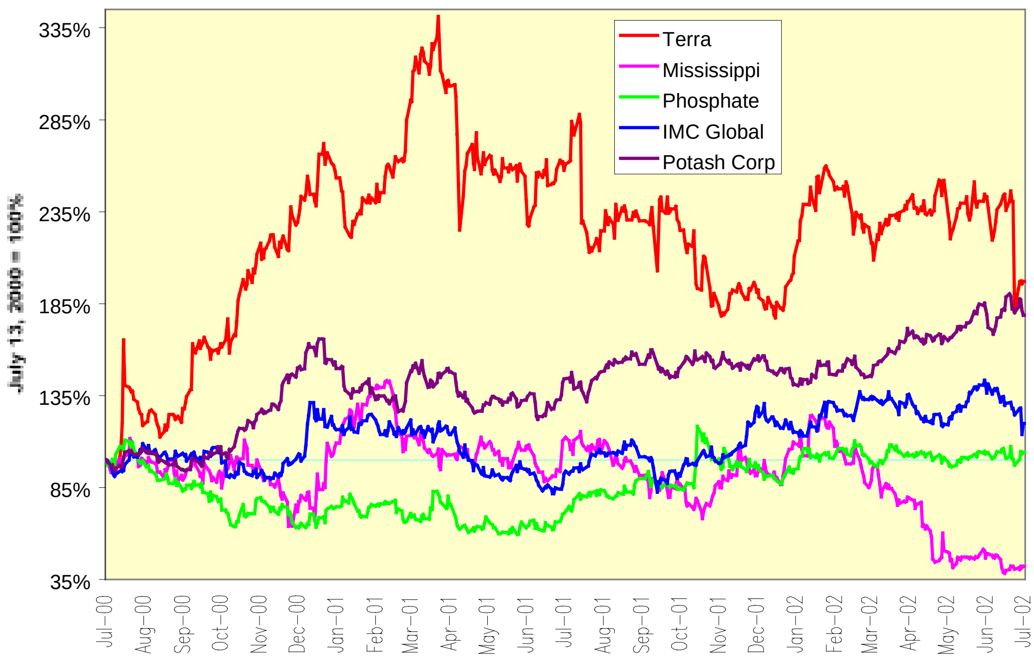
Sure enough, Lindsay's relative performance increases exponentially as function of wheat prices.

So-So Living Through Chemistry

Agricultural chemicals, including fertilizers, have not been able to capture the rent of higher farm commodity prices yet. Several of these providers, including Monsanto, made big bets on biotechnology that fizzled in the face of global resistance to genetically modified seeds. It's such a relief to know the French national character won't be affected adversely by a few stray soybean genes, isn't it?

Others, such as Terra Nitrogen, Potash Corporation of Saskatchewan, Phosphate Resource Partners, IMC Global and Mississippi Chemical, have been faced with a combination of higher raw material and energy prices and weak demand growth. Only Potash Corporation has been able to outperform the S&P 500 on a consistent basis over the past two years, a brief burst by Terra Nitrogen excepted.

Not So Fertile Fields



But, the name of this game is buy low and sell high, and if farm incomes improve, so will demand growth for fertilizer. Given the world's surplus of natural gas production – the feedstock for ammonia – it might be better to focus on the hard-rock mineral producers, Potash Corporation and Phosphate Resource Partners.

Staying The Course
A recent advertising campaign by Jim Beam Brands proclaimed "you always come back to the basics." Note how they didn't say you would have fun in doing so. Our recent distresses, far worse than I thought would be the case, have caused many to wonder about the wisdom of equity investing.

The *Layla* album was released in December 1970. Since that time, the annualized pre-tax return on the S&P 500 with dividends reinvested has been 11.57%. That includes the worst inflation in U.S. history, one presidential resignation and one impeachment, at least three energy crises, the end of the Viet Nam war, the Persian Gulf war, double-digit interest rates, numerous currency crises, disco, the Internet bubble and stiff recessions in 1974-75, 1980-82, 1990 and 2001.

Had you sold everything on June 30, 2000, this return would have been 13.77%, higher, yes, but unless you were new to the market during the peak of the bubble, we're probably not talking about change-your-lifestyle money. The worst, my friends, is never when you can say, "this is the worst." So, let's all take a breather from the fool's game of wondering where the bottom is and focus on what the indisputable long-term trend will be.