

GARY NORTH'S

REMNANT REVIEW

e-mail bonus:

year2000@garynorth.com

Matt. 6:33-34

Preparing the Remnant for the far side of the crisis

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[Because there is so much important information being published on the World Wide Web, I cannot put into *Remnant Review* everything that I read that I think is important. There just isn't enough space. This is why I also publish *Reality Check*, a free e-mail newsletter. I usually send it out monthly. There is another factor, too. The Web has a great feature: instant access to documents. I can insert a click-through link into the text of my newsletter that allows readers to go straight to the original source document. This way, I can offer my analysis of a document in my newsletter, and readers can verify the accuracy of what I am saying about the document simply by clicking through and reading the original. The advantage to the reader is obvious. Instant verification is not possible with a paper-based newsletter. If you are not yet a subscriber to *Reality Check*, sign up by sending an e-mail subscription request to ice@ballistic.com]

THE ABANDONMENT OF FUNDAMENTALS

Market sentiment has now turned bullish, according to John Mauldin, whose Millennium Wave Investments organization uses a very sophisticated and accurate proprietary stock market forecasting system that says that market sentiment is just about all that matters. His system indicates that mid-cap stocks have become the focus of buyers' interest in the last few weeks. This indicates that "value investing," a la Warren Buffett, may be coming back into favor. The question is: For how long? (More on this later in this report.)

Terry Easton, who has a completely different proprietary system, reports that his system's "crash indicators" signal ended. This took place at the same time that Mauldin's system went bullish. This indicates that the public has decided that this stock market cannot hurt them.

Is this a new bull market, despite Greenspan, despite short-term interest rates, despite low earnings? No one knows, but the rule is: don't fight the tape (or the electronic chart). In this issue, I cover the implications of the market's rebound. Is it a technical move or fundamental?

Bad Times for Value Investing

When we think of fundamentals in investing, we think of Warren Buffett. It has been a tough time for Buffett since mid-1998. In 1998, his legendary holding company, Berkshire Hathaway, peaked in price at about \$80,000 a share. (Buffett never splits the shares.) It then lost half of its value by mid-March, 2000. But just in one week, it rose by \$10,000. The comeback of the Dow Jones in relation to the Nasdaq benefited Buffett and his investors.

It was also in 1998 that the inflow of money into the stock market from mutual funds peaked. So did the price of the average stock. So did the advance/decline ratio. This may be about to change. There seems to be a shift of investor's sentiment in favor of Old Era stocks.

Buffett buys stocks and holds them. He is the opposite of a day trader. He also does not try to beat the market by timing its moves. He buys what he believes are undervalued stocks.

He has a major problem: he cannot sell his holdings at the top. He is too visible. His portfolio is too well known. He cannot buy enough puts or short positions to hedge his entire portfolio. If he tried, his shares' prices would fall. But if Buffett cannot get out today, how will stock mutual fund managers sell in response to redemptions by fund shareholders? If Buffett's stock lost half of its value during what has been perceived by the public (inaccurately) as a boom market, what will happen when this "boom" ends?

Think of the problem facing the under-40 managers of stock mutual funds. They are sitting on top of tens of billions of dollars in assets, or more. These managers move in packs. There are probably fewer than 5,000 of them. They talk with each other. They listen to the same gurus. They follow the same statistics. They face the same marketing problem: getting customers to buy more fund shares. In a panic, they will face the same marketing problem: trying to get investors in the fund not to redeem their shares.

Buffett does not face the threat of share redemptions. He does not have an army of clerks sitting at the receiving end of toll-free telephone numbers. He has not promoted ownership of Berkshire Hathaway shares on the basis of participating in a family of funds with telephone switch capabilities. He does not have 100,000 investors who have been told, "Our mutual funds are liquid. Just call, toll-free, and switch to a money market fund at any time."

He has followed the strategy of Benjamin Graham since the mid-1950's. He has accumulated a gigantic fortune. So have his early investors. Yet he has been stumped by this market. The performance of Berkshire Hathaway has led some business commentators to speculate -- intellectually speaking -- that Buffett's main problem is that he is a master of the Old Economy. The New Economy is something else again. It has new rules. The New Economy has nothing to do with interest rates, price/earnings ratios, return on investment, and other traditional sources of capital appreciation.

Buffett does indeed sound old fashioned when he comments on the use of stock options as the primary compensation scheme used by new technology firms. He sounds old fashioned when he says of technology stocks that he doesn't have any insights into which of the companies possess a long-term advantage. In any case, in the late stages of a boom, a wise investor assumes that at some point

in the future, the field will be cleared of the corpses of companies that possessed no advantage, and the prices of those that have survived the consolidation phase will be lower -- possibly much lower.

Let me quote my friend Bob Anderson, a curmudgeon with decades of investment experience. He taught economics at Hillsdale College until he replaced me at the Foundation for Economic Education in 1973. He had previously taught at Grove City College. He administered FEE's portfolio successfully for a decade and a half. Recently, he read a *Wall Street Journal* article about a conservative investor who finally threw in the towel last fall and bought tech stocks. His portfolio is up 40%. This triggered Anderson's skepticism regarding the Nasdaq.

In every mania the last buyers in make the most money quickest, but inevitably lose the most when it all collapses. A mania ends when everyone is convinced that the only way to profit from the madness is to join the madness. This is where we are today. It will continue until the influx of last fall's liquidity expansion [Y2K-related] is consumed by further investor indebtedness. For this reason, it's critically important to watch the Federal Reserve Bank Credit data weekly (Friday's WSJ). Now more than ever it's important to listen to what Greenspan does and not what he says! If further doses of credit expansion are not forthcoming, the party is over.

Again, this assessment comes from an old-fashioned investor. Those long-term observers who believe that American investors are in the final stages of a mania, throwing caution to the wind and abandoning years of experience, are not persuaded that this New Era is going to be any different from all of the previous ones. A tech stock portfolio that rises 40% in half a year is being pushed up by other late-coming investors who also did not believe in the sector, but who then concluded that they could no longer stay out. The fear of being left out is powerful.

Is Cisco Kidding?

One of the most popular Internet companies to buy is Cisco Systems. It sells hardware for the Internet. There is no doubt that it is a company with a huge growth potential. It is growing 2.5 times faster than Microsoft is. But investors pay for that widely perceived potential. The P/E ratio is around 200. There is no dividend. It has a market capitalization of over half a trillion dollars -- three times larger than Dell Computer, and over two times larger than IBM, which has a P/E of 30. It is now larger than Microsoft. Am I to believe that Cisco Systems is a better buy than IBM? (Check the latest stats for yourself: www.cnetinvestor.com/quote-detail.asp?symbol=CSCO).

Why would anyone buy this company's stock? Not for dividends, certainly. Not because it is an unknown firm, ready for some spectacular move. Maybe someone would buy it because of the greater fool theory: someone else may buy it later for more money. But, eventually, the greatest fool appears. The game ends.

Would you buy it for its future potential? Presumably, this is the rational motivation. But this means that you think there will never be a major

fall in its price, due to the economy or a change in investor sentiment regarding tech stocks. You will not be able to buy it much cheaper, later, so you buy it now. You buy and hold. For how long? No one knows. When will there be a dividend? No one knows.

Warren Buffett would not buy Cisco Systems shares. It pays no dividend, so it would not qualify as a Graham/Dodd company. Its book value would be hard to estimate. It has earnings, unlike most dot.com companies. Amazon has a negative earnings/share: -\$2.2. Cisco is a giant by comparison: 37 cents. But IBM has \$4.12.

In early March, both Merrill Lynch and Lehman Brothers recommended buying Cisco. I could not find any advisory service on *c.netinvestor.com* that recommended selling it. Its price was around \$70.

The Old Economy invests on the assumption that there will be a positive return. Because of income taxes, corporations may pay low dividends and plow profits back into development. Capital gains taxes are lower than income taxes. But the goal is capital appreciation. When the Old Economy seeks money from investors, it offers reasons to believe that there will be money. A good reason to believe this is that there has been money for a long time.

One reason why the dot.coms are so popular is that there is a reason for their lack of a track record of profitability. The industry is about five years old. Investors can calm themselves by saying, "This is an investment in a new and very different future -- a future with exponential profit potential (which I will need to justify today's 200+ P/E)."

Warren Buffett does not deny that the Internet is real. He just cannot determine the criteria for predicting which companies will be successful. The New Economy's criteria are hazy at best. The clarity of Graham/Dodd fundamentals is missing from the New Economy.

Then there is the question of competition. The Internet does provide useful information, especially price information. I can go to Amazon and find the price of a new book. I can then check Barnes & Noble's site. There will not be much difference. The item is standard. The mailing costs are standard. Neither company has a significant edge on the other. Neither company ever will. The competition is too fierce. The technology is too widely available. These dot.com companies have very limited advantages over their competitors -- advantages that can be overcome in a few months when someone develops a new piece of software. This means that these firms will never become profit centers. Let me quote Bob Anderson again:

Virtually none of the dot.com companies are earning much, if any, profit. Yet their valuations, market caps, are sometimes at triple-digit multiples of their sales. The mania frenzy into these companies is like buying options on their future. The payoff from owning these dot.com companies, so the reasoning goes, will come tomorrow. . . .

Austrian economic theory points out that pure profit will be zero in a market where participants have full knowledge. It is the absence of information which creates the potential for profit. But the very essence of the internet is its ability to provide instant

and accurate information to all market participants at virtually no cost. For instance, dot.com companies have come into existence solely for the purpose of comparing the offerings of other dot.com companies. Neither amazon.com nor Barnes & Noble.com can sell their books at a higher price than their lowest cost competitor. The lowest-priced book offering made by a dot.com company is immediately known and compared to all other dot.com companies trying to sell the same book. Those dot.com companies, whose function it is to make price comparisons for book consumers, provide this information cost-free to consumers.

As I see it the ultimate dilemma for the internet will be its tendency to continually strive toward efficiency monopolies, and in the process, virtually eliminate any possibility for the multitude of competing companies to earn profits along the way. Competition, driven by fully-informed consumers, almost guarantees little or no profit can be made by these dot.com sales companies. Total market information, readily available at no cost to consumers, makes the absence of profit for dot.com sales companies a permanent condition on the internet. At least the railroads enjoyed some semblance of a natural monopoly until the internal combustion engine was invented and the state-subsidized road building! But in today's internet neither capital nor laws are a barrier to entry, and full market information is available to consumers.

It seems to me that it's a wide-open game to massive losses as firms compete for the business of these fully informed consumers. Even without the certainty of technological innovations destroying the internet as we know it today, the potential for future profitability under these conditions seems bleak.

Open entry is a force to contend with. There will always be industry leaders, but in a fast-moving market, any lead will be expensive to maintain. Maintenance costs may be imposed in the form of price competition. They may come in the form of more expensive advertising. But they will come.

If some clever fellow could develop a way to forecast the future of the internet, he might be able to develop criteria for successful internet marketing. This way, he could spot the "comers" that will become survivors. If someone does this, he will not sell this information to the general public. It will not do most investors any good -- only his investors. But the task is probably impossible. The essence of the Internet is its adaptability. This totally decentralized entity changes too fast. No company can exploit anything like a monopoly. No model can, either.

Find Me If You Can!

A major key to profitability on the Web is to get your Web page listed on the first page of AltaVista or Yahoo or some other major search engine (about a dozen). There are now about a billion pages on the Web, and it's growing exponentially. No single search engine searches more than 15% of these pages.

If there are 30 "hits" on the first page, and hundreds or thousands of "hits" behind them, the searcher probably will not spend a lot of time looking

beyond the first 30. He might go to the next page of links, but that's it. Every company does what it can to get on that first page.

I ran www.garynorth.com for three years. If you searched for "Y2K and some other topic" in 1999, you probably got a link to a page on my site on page one or two of your search engine. The more obscure the other topic, the more likely that my link was on page one of the search engine's results. But at the end of 1999, my site had over 6,000 pages. I had over 5,000 other Websites that linked to mine (an important criterion for search engine placement of links at the front). My site was unique. But I did not sell anything on it, so all those hits were freebies. It was a financial loss for me to run it. That's the case for most Web sites.

The search engines are magnificent tools, but they are still primitive. It is still very difficult to screen out the noise: pages that have little or nothing to do with what the researcher is looking for. So, profits generated exclusively from Websites are few and far between.

The average Website is a lost cause for generating new business. A Website cannot earn a profit unless it is tied into traditional print advertising, follow-up sales techniques, and direct mailings. The tried-and-true methods of direct response advertising will work, and work well (without postage!), but there are very few advertising companies that offer these techniques, and very few independent copywriters who sell their services to the general public. The average Web-based company will not be able to locate people with these skills. The better-known practitioners are mostly graybeards, as I am. There are not many of us still operating. There haven't been for a generation. David Ogilvie was the last of the great ones.

The secret of a successful Website for all but the most travelled sites is a combination of traditional print advertising and a Web page. Also important -- and virtually ignored -- is the autoresponder letter (e.g., sales@bigbucks4me.com). As a direct response copywriter, I see the enormous potential of the Web. But I see almost no examples of the successful use of these tools on the Web. I used them to build a mailing list of 36,000 names, but I am an exception. I learned my trade pre-Web.

So, when I look at today's Web, I see that it will take years to make it work at the retail level for the vast majority of companies. In fact, I don't think it will ever work well for most companies with today's Web technology. New technologies will come, so I don't want to dismiss completely the medium's usefulness for most firms, although I really think that most firms will never do well with the Web without adopting direct marketing techniques. Understand, I am not talking about business-to-business Internet sales and service. This side of Web commerce will soon become indispensable. That's why I see **FedEx** as the better Internet stock play than UPS. I am talking about retail sales.

I mention this because I can see what will happen when the euphoria of the Web has worn off retailers. A tiny number will make it work; most will not. But retail firms will be pressured by price competition from the Web.

Let me give you an example. I am a biblioholic. I love used books. I own about 15,000 of them. But I rarely go into a used book store unless I am in a big city that has a large store like Powell's or the Strand in New York City, where I can walk down aisles of books organized by topics. I may buy at

a "friends of the library" book sale because I can buy good books for a dollar or less. But I do not bother with most mid-sized used book stores. Here's why: www.bookfinder.com. With this service, I can search for any used book. I get a list of stores that sell this title on-line, with the list arranged from the lowest price to the highest. I have seen price differences of 20 to one. I can order books on-line, as with Amazon. I get delivery by UPS or the U.S. Postal Service.

At some point, book store owners will use Bookfinder to price their books. This has not happened yet, fortunately for me. But that Website has affected my buying habits. I think millions of other people will change their buying habits, too, at least for some kinds of purchases. Intense price competition and a wide variety of sites are combined on the Web.

So, local retailers will have to adapt to the Web's price competition or else suffer reductions in business. Repeat customers are the lifeblood of any business. But repeat customers have an incentive to go shopping for better prices. Any consumer who is dedicated to one type of product has an incentive to shop. He will find cheaper ways to buy on the Web. Wal-Mart eliminated many local shops. Now the Web will take its toll on the survivors. They had better learn how to fight back. They had better learn how to use the Web.

Keys to survival locally will be large inventories, available for purchase now, and good service. I am thinking of NAPA, O'Reilly, and other auto parts stores. When an important gizmo on your car breaks, you will not go on the Web to buy it. Anyway, the guy who can repair your car probably won't. Retailers will have to make their money by servicing the products they sell. There are also pure service companies, such as a dry cleaners or a shoe repair shop. But the service industry is labor-intensive. Profit margins for most retailing firms that add services will fall from today's levels.

Won't the Web companies that make it onto the first pages of search engines take the lion's share of new business? Yes, but only through intense price competition. The Web will squeeze profits by making available better information on alternatives. I think Amazon will be struggling with negative earnings for years to come. When will investors ever get paid?

The crucial and ignored fact is this: Amazon's customers are the winners, not Amazon's investors. The investors have provided the capital that allows Amazon to gain market share by losing millions of dollars a year in the company's attempt to gain customers. This is true of virtually all of the dot.com companies. Their customers are being subsidized by hopeful investors. But today's customer loyalty is very recent. It is not based on decades of experience. It is based on loss-producing discounts and convenient technology. These discounts are being provided by the investors. Technology is replaceable by a competitor at any time without warning. When the party ends -- the party of mania-driven investors -- the dot.com customers will go elsewhere in search of discounts. In a recession, they will cut back on their purchases.

What are the basics that are being sold in the Internet? Hardly any. There are discount drug prescription companies, but they are not widely used yet. The items that most people will continue to buy in a recession are sold at Wal-Mart or the local discount store. The dot.coms appeared in the middle of the longest boom in American history. Their profit models are boom-based.

What the Web is doing in an unprecedented fashion is delivering information inexpensively to customers. Smart buyers are learning how to buy more wisely. As specialized information on price becomes more available through the Web, customers are able to play off sellers against sellers as never before – even across political and geographical boundaries.

The Internet's technology is cutting marketing costs. Historically, this has led to profitable companies. But to maintain their profits, the companies had to invest in more cost-cutting technologies. They had time to do this in the old days because they had beaten their competitors. It took time and money to catch up. But the Web's technology is different. It's electronic. The huge physical barriers to entry of, say, Standard Oil or General Electric, do not exist on the Internet. A few million dollars will fund a major venture. If a new technology is available, it will be funded and exploited fast.

Cost savings will have to be passed on to the customers as fast as a new technology is implemented. The introduction of a new technology will not give the patent-holder any long-term advantage. It will only keep him at the front of a very fast race. The beneficiaries will be customers, not investors. I offer as an example the Web browsers. Mosaic never was a serious contender. It was replaced by Netscape Navigator. Microsoft's Internet Explorer took away Netscape's initial advantage in just three years. It did so with price competition: free. It's hard to compete with free, especially when the product comes installed on every Windows machine.

Today's investors are investing in New Era companies on Old Era assumptions. The main Old Era assumptions are these: (1) market share can be maintained without huge infusions of new capital; (2) there is a profitable lag time between new technology and new competition; (3) consumers must bear expensive information costs in discovering alternatives; (4) customer loyalty is not easily eroded by price competition alone. The fourth assumption is the most naive today. The number-one market-building strategy of the dot.coms is price competition. Customer loyalty in the dot.com universe is based almost exclusively on price competition. Therefore, it can be bought off: "Discount!"

We are seeing a massive transfer of wealth from investors to consumers, company founders, and venture capitalists. Investors do not perceive this yet. They are peering into the future with Old Era glasses. They are willing to do without dividends and even positive earnings on the basis of the New Era's promise of "big profits, one of these days." The New Era's promise is based on Old Era assumptions about consumer behavior. But the New Era's technology is changing consumer behavior.

Better Times for Value Investing

Then what kinds of stocks should people invest in? First, companies that perform services that are unique or local and therefore less vulnerable to price competition. Disney is an example. Local trash collection companies are another. In contrast, companies that sell information services that can be sent over phone lines will face serious competition. For example, there are many English-speaking engineers in India who are ready to work for 20 cents on the dollar. Second, companies that act as support centers for Internet sales. FedEx is an example. Third, companies that cater to the super rich, who are not concerned about price competition. Fourth, companies that are selling at

low P/E multiples, but that have a long track record. They have survived recessions in the past. This is "value investing," and it is out of favor today. It will not be out of favor during and after the next recession. What Buffett did with Berkshire Hathaway is what wise investors will try to imitate when Greenspan's boom turns into the Greenspan's bust: buy low and hold.

John Mauldin of Millennium Wave Investments spends his days tracking investor sentiment. I recently visited with him at length in his office and looked at the mounds of research he compiles each day. Basically, they analyze every trade (tick by tick) every day on the New York Stock Exchange and determine investor demand and where there are positive dollar flows.

As you might expect, for the past months, investor demand has been concentrated in the largest-cap stocks and in a small number of industries. But a few weeks ago, those trends began to change. Investor demand for the large cap stocks is still high, but there has been a clear move by investors into mid-cap stocks.

Mauldin's data do not tell us why -- just that it is happening. I can guess why. Investors are nervous about buying stocks that have already made huge moves, and are looking for value in the next tier of stocks. Nothing has dissuaded them that the game still has more upside, and they're looking for something with some room for even more growth. How do you take advantage of this shift? He recommends three funds. Two are highly rated Morningstar mid-cap funds:

Fund	Performance:	1 year	3 year	5 year
Maxus Laureate (MXSPX)		66.7%	32.7%	26.7%
Wayne Hummer Growth (WHGRX)		31.4%	24.4%	21.4%

These funds have high technology and service allocations and thus they have done well. But their long-term record shows the managers are fairly nimble and can move to new stocks.

The last recommendation is a contrarian one. **The Lindner Large Cap Fund (LDNRX)** had a change in management in March of last year and is now a relative value fund. The fund managers first look for the best managed companies and then sort them to find the best relative value, adjust for risk and choose for the portfolio. Though the name says large-cap, it is actually split between large- and mid-caps. Since re-organizing, it has beaten its benchmark. The new strategy, if they implement it as they advertise, seems to be working, and they are positioned precisely where investors should be. If we see a true move to value by investors, this fund should do well. (Thanks to Tony Sagami for the data on these funds.)

I would put a stop on all these funds of between 7-10%. If a major correction or bear market starts, they will fall along with all mutual funds. But for now, they are running in front of the investment mob.

For those of you who need more income potential, but are worried about the downside risk, I would suggest the **Gateway Fund (GATEX)**. This fund has a very simple but effective strategy that has done very well in both up and down markets. The fund simply buys the stocks of the S&P 100 (not 500). That means the fund buys and holds the bluest of the blue chips. It then sells covered

call options against those stocks. What this does is "sell away" all the upside potential greater than 20% a year to option speculators looking for a quick profit. The fund collects between 12-15% a year by selling the call options. The fund also collects the dividend income of the stock that it owns.

The result is that the fund regularly and reliably collects about 13-16% a year from options and dividends. Subtract about 1% in management fees, and we see how this fund has averaged 11% compounded since its inception in 1983. This is below the indexed stock market, but it was safer.

Most importantly, portfolio manager Patrick Rogers will purchase "put" options or portfolio insurance whenever their proprietary market timing indicator flashes bear market warning signs. What they essentially do is take some of their call option income and spend a small piece of it on portfolio insurance. This is why the fund should hold its value during difficult market conditions and is a good fund to own today if you hold stocks.

I am not saying it won't have losing periods. In the 5 months in the middle of 1990, when the S&P 500 was losing 15%, the fund went down 4%, but quickly rebounded. So, it is not perfect, but it is as "Steady-Eddy" a fund as there is for these type of higher returns. Plus, it is a good place to park your funds while you are waiting for something else to commit it to. Call **800-354-6339** for more information.

Beyond Value Investing

Economic fundamentals are still reliable guides to investing. The Old Era still operates in most investment sectors. If the Internet makes these old line firms more efficient, this will be good for their customers. But look for industries with lag time between the introduction of a new technology and price cuts. Look also for barriers to entry. Not every cost reduction must be translated into lower prices and lower profits if an industry requires huge capital investments.

What bothers me most about the New Era stock market mania is that it demands that investors suspend their belief in economic fundamentals. When the Federal Reserve raises interest rates, the market should go down, not up. Rising interest rates historically have been associated with stock market corrections. But the public no longer believes this. Nothing seems to affect investor confidence these days. This, too, shall pass.

Market sentiment can overcome all economic fundamentals for a while, but always - always - the fundamentals reassert themselves. Those who remind investors of this fact get few people to listen to them in the final phase of a market boom. Each New Era seems to have overcome the fundamentals. But always, the fundamentals reassert themselves.

Not many people believe this any more, and those who do usually have gray hair. Even among them, the faith in economic fundamentals is beginning to waver. The free market under Clinton/Greenspan seems to have banned recessions. It seems to have created a self-perpetuating wealth machine. The trouble is, it seemed to have done that in the past, too. In 1931, Viking Press published a slim volume titled, *Oh, Yeah?* It was a compilation of pre-1931 assurances by economists, financiers, and businessmen that the prosperity

of the 1920's was irreversible. It ended with some of the last words (1931) of "Silent Cal" Coolidge: "The country is not in good condition."

The concept of economic fundamentals is more extensive than just P/E ratios and interest rates. It has to do with the fundamental values of a society. Most economists dismiss such considerations as unscientific, but I think Americans over age 50 have some understanding of the ethical cause-and-effect relationships in society. "Honesty is the best policy." "Little by little." "Easy come, easy go." "Personal debt is dangerous." "Make do with what you have." "Enough is enough." "Put something away for a rainy day."

Then there is Max's law: "Buy the best, pay cash, take delivery."

This is a mental outlook and a way of life. It can sustain you as you slowly accumulate wealth over a lifetime. It also sustains people who are on a faster track. I recently loaned my 17-year-old son a copy of Robert Kiyosaki's book, *Rich Dad, Poor Dad*. He went out and bought his own copy. This book is a very good introduction to building wealth. I wish I had read it at age 17. Of course, I probably would not have bothered to earn a Ph.D., which, financially speaking, has been one of the worst possible investments for about 1,000,000 American investors since 1968. Kiyosaki's father did just that. He was superintendent of schools for Hawaii at one time, but then he lost his job. He is the poor dad in the book. Kiyosaki was trained in the art of making money by a friend's father, who did not seem to have much money. He had a bundle. His son now runs a billion-dollar empire that his father left to him.

The secret of great wealth, the rich dad taught, is buying underpriced assets that throw off income and also appreciate. If you can buy them with below-market debt, so much the better. The rich dad would have approved of real estate investor Jack Miller's line: "The easiest way to become a millionaire is to borrow a million dollars and pay it off." Your renters pay you to pay it off. But it's not just real estate, as the book shows. It's a way of thinking. You do not take on debt for non-producing consumer goods, such as a new car or even a home that you intend to live in. You rent, wait, look for bargains, and accumulate. You avoid getting into the debt trap.

Here is a simple strategy to remind anyone of the reality of depreciation. Cars depreciate. Wise car owners plan for this. They put away money, month by month, to buy their next car. They collect interest while they are waiting. They begin shopping early, before their present car dies. They use the Web to monitor prices (www.kbb.com) and find bargains. They buy 3-year-old cars. They let the other guy lose the high depreciation that hits in the first two years. Then they pay cash.

This is obvious. Nothing revolutionary here! But because people do not think ahead and plan ahead, most car buyers do not do this. They are present-oriented. They buy on impulse, or when their car breaks down, and they finance the purchase. They wind up paying high interest for a depreciating asset. They get into debt early, and they never get out.

They make rich dads richer.

The debt trap grabs Americans early in life. This reduces their mobility. It reduces their ability to make investments. They wind up paying interest instead of collecting it. They begin their careers on the wrong side

of the debt relationship.

In a recession, the interest rate clock keeps on ticking. It does not care whether the debtor is in tight financial conditions. People collect debt burdens in good times, usually in the second half of a boom, when consumer confidence is rising. Then they get trapped. Residential real estate today is a good example. Prices are rising. Homes don't stay on the market long. Everyone wants to move up. But when recession hits, home equity will disappear. Bargains will appear like flowers in spring.

There will be another recession. That's when investing works best. Meanwhile, get experience. I want my children ready for the opportunities. I have told my son what I think is the best occupation around: auctioneer. In good times and bad times, somebody is selling off the assets in an estate. Auctioneering is one of the recommended occupations in *The Millionaire Next Door*. Here is a profession with 20,000 people in the U.S. -- not very many -- that is the 11th highest paying occupation, or so those in the industry say. I know of no college that teaches auctioneering. There are several auctioneers' "colleges" that are in fact seminars that teach one-week or two-week introductory courses. You can get a list of these courses from the National Auctioneers Association, 8880 Ballantine, Overland Park, KS 66214-1985.

The best entry-level book on conventional stock market investing that I know of is Mark Skousen's *Scrooge Investing*. It has just been updated. It's called -- get this! -- *The New Scrooge Investing*. (Where do they think of these things?) It's published by McGraw Hill (\$22.95). This is a good book to hand to your newly graduated senior in college before he gets a credit card. Arrange to give him a debit card and tell him, "Stick with this!" If you toss in \$1,000 and tell him that he won't have to pay it back until the day he gets a credit card, you'll do him a great favor. If he has a credit card already, ask him to trade it for the debit card and the \$1,000 bonus.

There is a money management course that I regard as crucial. The younger a married couple is, the more benefit they will derive from it. If churches would get their deacons to take this course and then teach it to church members, there would be fewer divorces. Something in the range of 50% of divorces in the U.S. involve disputes over money, one study reports. The course is published by Crown Ministries. It's called *Small Group Financial Study*. The materials sell for \$45. The course is taught by someone who has gone through it as a student. To find out if a course is being taught in your area, visit their Web site, www.crown.org, or send a FAX to 407-331-6001. Let them know your city and zip code. Be sure to include your phone number and mailing address.

Conclusion

Economic fundamentals always reassert themselves. Every New Era always returns to the norm. The statistical phenomenon known as regression to the mean always reasserts itself. This is why trend-following eventually produces losses for the investors who follow the pack. A small percentage will get out early by abandoning their trend-following just in time, but most people will continue to follow the trend, like lemmings, if not over a cliff, then at least to middle-class capital. But the pain of having returned from the exhilarating realm of wealth on paper will cripple millions of them emotionally.