

Sather Financial Group, Inc.

Comprehensive Wealth Managers

Half Priced Hamburgers?

Instead of talking in terms of financial markets, credit default swaps and derivatives, let's talk in terms of burgers. Yep, that's right. Let's talk in terms of big fat juicy hamburgers. We can all relate to that much better than a bunch of esoteric Wall Street lingo.

Since the beginning of modern history, "hamburger stands" have sold burgers, malts and fries. For their effort they received money (also known as profit). While the burger business has its ups and downs, over the long run it is a pretty good business.

Historically, when the owner of a burger stand wanted to sell their store they got about 14 times the historical earnings. No rocket science--just selling burgers.

From time to time throughout history, we have things like Mad Cow disease or Oprah or some crazy diet of the day that causes a variety of valuation issues with our burger stands. Other times people are so excited over the new "secret sauce" they become euphoric and want to offer 25 times earnings for burger stands.

However, now the average burger stand sells for a significant discount to the averages.

That is where we are today. We own a bunch of really good burger stands that sell burgers, malts and fries each and every day. Nothing has changed in this area. However, because of some issue or crisis, people freak out and act as if no one is ever going to eat a burger again. As such, people offering to buy burger stands are offering 30% to 50% below what burger stands usually sell for.

We saw this same behavior during the Great Burger Bust in 1929 and again in the Burger Debacle of '73 and '74. We also had a Burger Embargo in '81 and '82 and the Black Monday Burger Blowout in 1987.

Obviously, this is not the first time, and it won't be the last time, that burger stands go on sale. However, on the average, we have never seen burger stands this cheap as a whole.

In fact, only five times in the past 100 years has the average burger stand price declined two years in a row. After two years of declines the market for burger stands has increased by an average of 60% after a two year decline. Evidently, after two years we come to our senses and recognize our love of burgers and malts.

Whenever burger stands have gotten this cheap, over the next year or two they have increased in price by 40% to 60% (even though they are still making the same old burger). That should be no surprise. If the typical burger stand sells for 14 times earnings during a normal year, but current offers are only 9 times earnings, then common sense would tell us that once things return to the average we will experience close to a 50% gain from where we are today.

The conclusion I take away from this is that if we are going to be in the burger business, occasionally nonsensical people will offer us ridiculous offers (both high and low). If we are plagued with a bunch of low offers we are under no obligation to accept their offers. All we need to do is wait for a reasonable offer.

The concept of reversion to the mean will take place and, instead of having burger stands trading for 9 times earnings, they will trade back up to their historical average of 14. This does require discipline and patience.

So the moral of the story is to go and enjoy a good burger, an old fashioned malt and some fries while we wait for the market (burger or stock) to resume rational behavior.

Call with questions.

Sincerely,

Dave

Dave Sather, President
CERTIFIED FINANCIAL PLANNER™

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