

Impressions

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Why can't the world be like Disneyland?

If man is to survive, he will have learned to take a delight in the essential differences between men and between cultures. He will learn that differences in ideas and attitudes are a delight, part of life's exciting variety, not something to fear.

Gene Rodenberry- Creator of Star Trek

I owe the title of this lead article to my assistant Sue Ferrell who responded with the above question after hearing the story I am about to tell you.

It may come as a surprise to many of you but I have a soft spot for Disneyland, and over the years have visited it many times. I like it far more than Universal Studios or Knott's Berry Farm. In mid June, our son turned 30 and given his record of vehicle accidents and moving violations, this was a minor miracle so my wife and I flew down to Southern California to celebrate with him.

On the Friday before his birthday, we all trucked out through the terrible traffic to the park. I have not been there since the opening of the Disney California Adventure Park adjacent to the original. California Adventure is the one with the big Mickey Mouse

looking thing as the centerpiece (it is a roller coaster, and a good one, in disguise).

It was one of those wonderful California days not too hot and when it did get warm a gentle zephyr would spring up like magic to cool everyone down, either that or you went on a water flume ride and got cool that way. I have never understood why people wear tight white pants and colored underwear when they know they are going to get wet.

By mid afternoon the place was packed and the lines for the rides started to stretch out to an hour or two, even at the dumbed down, politically correct Pirates of the Caribbean. There seemed to be someone standing in every square foot of the park except at **It's a Small World**, which is the single most aggravating thing in the park.

My real joy in Disneyland is watching the actions of 100 to 200 thousand of my fellow humans. I could sit all day on a bench in front of the Haunted Mansion behind the shelter of sunglasses and just watch.

The reason for my joy is that every variety of the human race is at Disneyland with every possible permutation. It reinforces one of the basic concepts of humanity, that man is a social animal and unless physically separated, segregated by government action or for political power, mankind is going to socialize and mix with each other. There is a natural melting pot.

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There are probably more languages spoken each summer day at Disneyland than were spoken by Star Trek's universal translator, there were women in the hijab, the shayla and adaya. There were men arguing in Arabic in line in front of Jews speaking Hebrew and Yiddish. One could hear Castilian Spanish and the Mexican variety, there were Buddhist Monks and Nuns in line for the Indiana Jones ride. There were families of African American women and Caucasian men and vice versa, Asians with African Americans. Then there were the families of blond blue-eyed Nordic stock with Asian and African American babies and gays and lesbians as couples and as families.

There were the snotty, unkempt American teenagers with the ever-present cell phones and stereo headsets, baggy pants on the boys and low-rise pants and crop tops for the girls. I am convinced that hip hugging tight pants and short tops are part of a sinister plot to torture overweight teenage girls. There were pre teen girls in their Wonder Bras and matrons without bras and guys with so many metal piercings that you constantly scanned the skies to be sure a thunderstorm wasn't developing as they were targets for lightning.

What you did not see or hear was the wailing of police and ambulance sirens coming to clean up the results of the latest political statement by some disadvantaged group. You did not see paramilitary forces armed with machine guns patrolling the area, no armed helicopters overhead, no attempt to route or control the crowd; no whiff of tear gas in the morning. There was no pushing, shoving or fighting between what we are constantly told are traditional enemies. There were no attempts at extortion except at the food stands, no beggars in the streets mewling for spare change, an oxymoron if there ever was one.

I am certain that it was not all sweetness and light but whatever ugliness may have invaded was far away. What was happening was that a quarter of a million people took one day to decompress and live in a world of fantasy and make believe. They all focused on one thing, having fun. When people focus on common goals many of the daily struggles fade to insignificance and people get along better.

The Disneyland experience reminded me of those lines from Richard II:

**This other Eden, demi paradise,
This fortress built by nature for herself
Against infection and the hand of war
This happy breed of men, this little
world
This precious stone set in the silver sea
Which serves it in the office of a wall
Or as moat defensive to a house
Against the envy of less happier lands**

The handling of the issues posed by diversity has always been a special skill of the United States. For three centuries our history has been written in the streams of immigration and because all who came here united in seeking a better life, they were willing to accept common principals, common language and common history to create that vision. Now pundits tell us that we need special training and sensitivity to the need for diversity. That the American melting pot no longer works. That maintaining the separateness of each culture is the only way to survive. Bunk! Go to Disneyland. That will put that argument to rest!

Disneyland and the other theme parks give us a glance of what the world could be if we could find common goals and aspirations. There is in every society some common denominator. What is needed is to find it and educate the citizenry to both its existence and its usefulness.

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Alexis de Tocqueville said that “... **Without common ideas there is no common action, and without common action men still exist, but a social body does not.**”

Long live Disneyland.

Responses

Our last newsletter headlined on a particularly stupid piece of legislation here in Washington that has broad impacts for the state's economy and some lessons in how economies get in trouble. Of all the articles I have ever written that one on the CAO got the most reaction which is somewhat amazing because I was not sure anyone read this scribbling.

Shortly after we sent it out, we received a call from King County Executive Ron Sims' office chastising us for what they termed misrepresentations. When asked what exactly was misrepresented they could not or would not provide actual references. Then we received an email from our Governor Christine Gregoire's office taking me to task for calling her a thief as far as the election. The statement was that Christine did not steal the election and asked for a retraction that I am happy to supply herein. Governor, I am sorry I called you a thief, you are not a thief and I now know that. You are rather, a corrupt opportunist.

The CAO takes on a more ominous cast in light of the inexplicable Supreme Court decision in Kelo v City of New London that expands eminent domain from public use to public benefit. You see, the CAO is the logical absurdity in the other direction as it takes land that might in the future produce higher levels of taxation and condemns it to produce nothing but still not be available for public use! This is government at its finest!

ENERGY

The prices of energy have continued to stay high for almost a year now and we are all used to paying the mid \$2 for gasoline. We got through last winter without it being an outlier for cold and the summer has until recently been relatively mild.

The standard wisdom is that China, India and other third world nations need oil to provide the production we have outsourced. The second part of the conventional wisdom is that Hibbert's Peak has been passed. Hibbert's Peak is a theory by a Shell oil geologist that sometime in the 21st century we would reach the peak in worldwide production and then begin a slow but steady decline.

The third leg of the conventional wisdom on oil is that inflation is creeping back into the mix and that means energy prices will be up because they always go up in inflationary times.

This is all very cool stuff, intellectually stimulating and thinking about it keeps portfolio managers off the streets, out of bars so the world is a safer place. There is only one problem (okay two).

First, it is not new. We have heard this all before many times. In 1981, Dow Jones News carried a story containing a huge mistake to the effect that Union Pacific Resources had defined the reserves in the then hot exploration area The Overthrust. It was one of those mistakes were someone added a zero so the number was 40 trillion cubic feet not 4 trillion. The effect was that none of the major oils like Exxon, Chevron etc. could open for trading because of buy order imbalance.

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Finally, an hour later they all opened up 2 or 3 points and were trading like crazy when Dow Jones ran a correction to the earlier story and they all traded down and finished down for the day.

That day was one of the tipping points of the great energy crash of the 1980's. In the previous 10 years we had seen the price of crude go from \$4 a barrel to \$35 and in the next ten it go from \$35 to \$12 and we would be talking endlessly, it seemed, about a natural gas bubble.

In the midst of all this panic and crazy pricing three smart fellows began liquidating oil investments, they were the late Marvin (pull up a couple of chairs and join us) Davis, Richard (the Bass Brothers) Rainwater and Phillip Anschutz.

These are very smart people who buy cheaply and sell dear and they sold near the top of that cycle and laughed through the 1980's and most of the 1990's at the predicament of the fools who bought from them. Then sometime in the 1990's they started to reacquire properties and reserves. So they were right twice.

The second problem is that the bears on energy talk endless about a bubble developing in the stocks but it are hard to make the case for over investment with the numbers in the chart the chart in the next column.

It appears as if we are in normally secular revaluation of energy stock in the index. Tech had its run and now energy is the game. These moves are long term in nature decades sometimes and are therefore full of backing and filling. Nevertheless, there are some weird things going on in energy.

Recently it was announced that Phillip Anschutz (yes the same guy) was selling a large piece of his production in the current hot

spot for gas exploration to a group of California Municipal Utilities. So the question I am asking myself is: who do I think is smarter a municipal utility in California who can get rate relief to assuage fuel pricing mistakes or Phil Anchutz? The answer precedes the question.

	Energy	Technology
	Feb-05	Mar-00
Weight of stocks in S&P 500	8.8	33.5
Forward PE	14.5	38.3
Price to Book	3.2	14.3
Sector Mutual Fund Flows (\$ millions)	383	2,978

I am not predicting a price crash what I am saying is that there are some very weird things going on in energy that bear watching. Look at the chart below

	Crude Oil	Heating Oil	Gasoline
4/1/05	317,062	104,110	212,252
6/24/05	328,496	113,166	216,240

The numbers are in thousands of barrels and represent the stocks of these critical components of the energy chain in storage. They do not include any storage in the Strategic Petroleum Reserve.

What makes these numbers interesting is the heating oil number. Why is that going up? No one needs heating oil during the summer and the refineries shift to gasoline in the late spring so it should fall in early summer.

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The real issue is that there are a lot of financial types playing the energy futures with their house's money betting on ever higher prices while the background experienced operators are selling property.

I am convinced that we are in a secular bull market for energy issues. The Chinese use about 1.7 barrels of oil per person per year while we in the west use about 17 and the numbers are similar for India. Unless we start using a lot less oil there is going to be high demand for a long time. We are no longer finding huge new fields of oil and gas domestically and while Russia has a lot of oil it is difficult to get it to market and it comes with Vladimir Putin attached which is the devil's bargain. Russian oil is also long way from anyone who cares and between it and the markets are a lot of really unsavory folks. So in all likelihood energy stocks have a ways to go before they get topky.

All the forgoing does not mean that all areas of energy will do well. Tanker stocks have tipped over from a shortage of tonnage to an equilibrium and oversupply. Land drilling companies will do well due to capital discipline in this market and the need to get more production from each well in addition to the greater difficulty of drilling each well.

There will be a lot of acquisitions at some point in the future since few companies are not replacing production with the drill bit and cost of capital is low, cash flow high and Wall Street has a deal for you. The oil operators know that currently the prices of acquisitions is very high leaving only the usual bad buyers around (Canadians, Europeans, Russians) The Chinese attempt to buy Unocal may either be the most brilliant move in history or they may have the Japanese disease and are buying assets at the top which will come back to the market later. Are Phillip Anschutz and Chevron smarter

about US oil than the Chinese? Again not even a good question.

STRAWS IN THE WIND

A great part of the investment process revolves around seeing patterns and drawing conclusions about seemingly unrelated facts and one of the ways those facts can be turned into money is by watching the actions and statements of people who are known to be forward thinkers and combining that with other knowledge.

So here are the unrelated facts. The 10 year US Treasury stubbornly refuses to move much above the 4.00% yield mark regardless of 9 interest rate hikes, 2. A huge number of houses are being purchased using interest only loans, 3. Warren Buffet who has already invested about \$10 billion in the utility industry says to a group of utility executives that they may invest another \$5 to \$10 billion in the same area. 4. Citigroup sells \$400 billion in assets under management to Legg Mason for 1,500 brokers, some stock and a bit of cash while Deutsche Bank sells the Morgan Grenfell Fund (once a really hot investment manager) division to Aberdeen Management.

Here is my conclusion: the economic growth of the United States is going to continue at the current rates or slower for the next year at least, inflation is not a problem and returns on invested assets are going to be quite low on an absolute basis and lower still after fees.

Utilities produce returns of about 9 to 14% per year of which 5% is dividend income which enjoys a favorable tax status. They tend to get 4 to 5% rate increases per year and their transmission assets represent huge capital investments which are becoming more valuable due to lack of new building (no

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one wants high tension power lines in their back yard)

At current interest rates, the spread between the cost of capital and the steady returns of the utilities is very attractive particularly if you are convinced that rates will not rise due to the slowing economy.

Investors are tired of the low returns from the stock market they don't feel they can play the hedge fund game but they all know or think they know real estate. So we see bidding wars for condos, we see condo developments pre-sold before the foundations are poured.

Low interest rates and the spate of new products from the mortgage industry have made real estate speculation within the reach of everyone and in places like San Francisco (median house price \$633,000) 40% of the mortgages are interest only and these are not refinances or small loans they are million dollar packages!

So seeing all of this Citicorp reasons it is better to have 1,500 more incipient fanatics out selling product that \$400 billion in assets generating fees. If you are supposed to buy your straw (summer) hats in the winter, then since it is summer, I think I will go shopping for winter clothes.

Good Luck,

Dennis Gibb