

We then further averaged those numbers to take out any sensitivity to a particular year and, therefore, the "average variance" and the "average return" are numbers that contain 16 years' worth of information.

From a statistical sense, and for Mr. Gordon's benefit, I say this is a highly rich statistical body, so that if we have a significant statistic, we can be quite confident in it.

We have tested besides the book value rate of return another very important subsidiary rate of return, that earned by the stock market investors should they decide to invest in the industry through the mechanism of this stock and bond market, rather than investing hard, cold cash in machinery, or research and development. We know in the stock market there is certainly a continuum of returns that are related to risk. Government bonds yield the lowest of most taxable bonds. Then come AAA corporations, AA corporations, going up to mortgages, and third mortgages, each with higher and higher yields, and more and more risk.

The same with common stock. The blue chips have low yields as opposed to the speculative shares and computer shares which have on average, for an extended period of time as an industry group, high yields.

Therefore, we felt it necessary to test the validity of our definition of variance, our definition of risk, in the stock market first.

The chart presented in the study on page 20, I believe, is a test of the relationship measured at market value. The fact that it has a high statistical significance, the fit is very tight, and forms an upward sloping line, is to us a true validation of our measure of risk, that we have not quantified a stable measure of risk.

We may then proceed to ask the second question which concerns the real economy, the second chart found on page 19; that is, what is the pattern really dependent on, do rate of returns and risks go hand in hand, and if they do, what can we say about individual corporations. I must correct myself, not individual corporations, but individual industries.

(The chart follows:)