SoundAdvice

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As we publish, the Senate is still debating the tax overhaul bill. If it gets through the Senate, it still needs to go through the reconciliation process, so its final form is still uncertain. If the corporate tax rate is actually reduced from 35 percent to 20 percent, the benefit is not as large as it may seem because most corporations do not pay taxes at the 35 percent rate. Howard Silverblatt, a Senior Industry Analyst, Index Investment Strategy, for S&P Dow Jones Indices, estimates that the effective tax rate of the S&P 500 companies is currently 25.6 percent. Michael Thompson, President and Chairman of Standard & Poor's Investment Advisory Services, estimates that each one-percent reduction will add one percent to the earnings of the companies that comprise the S&P 500.

Accordingly, a 20 percent corporate tax rate is estimated to add 5.6 percent to the earnings of the S&P 500, or close to $7.00 to the 2017 earnings projection. From the context presented in this issue, the relatively high P/E of the S&P 500 reveals that this benefit is already largely built into stock prices.

The *Sound Advice* Portfolio is up 7.0 percent this year. We have an average profit of 74 percent based on the prices at which each position was recommended.

The *Sound Advice* investment returns in prior years have been calculated independently by the Hulbert Financial Group. They are as follows:

18.69% in 2016 vs.
9.54% from the S&P 500

From 2000-2016
10.30% Annually vs.
2.37% from the S&P 500

How High is Too High?

As the market inexorably rises into new all-time high territory, we know that stock prices are high. We also know that stock prices have been rising for a long time. This bull market will be 105 months old on December 9, making it one of the longest in post World War II history. Only the bull market that ended in March, 2000, lasted longer for 113 months, which ended with a bear market that took prices down 50 percent. Are we there yet? Are stock prices too high?

The way to address this question is to put today's market into context. To see how high prices really are, we can measure stock prices against their current earnings, look at the historical range, and assess growth prospects.

Operating Versus Reported Earnings

First, we need to define exactly what type of earnings we are going to use: "*operating*" earnings or "*reported*" earnings. The distinction is important. *Reported* earnings conform to GAAP (Generally Accepted Accounting Principles) and include unusual special charges for things like gains and losses on the sale of assets, and impairments on assets such as inventory, good will, contracts, or even impairments on the value of a company's major assets, such as land, mineral rights, or oil leases.

Operating earnings do not include these special charges. Whenever considering a large group of companies, such as the 500 companies that make up the S&P 500 index, there are always special charges, at least on some of them. This is why *operating* earnings are usually 10 to 15 percent higher than the earnings that are actually reported. Moreover, GAAP does not define *operating* earnings, so it is left up to the management of an individual company to determine what is "unusual".

One of the most egregious examples of depending on *operating* earnings as a guide was during the 2008 financial crisis when there were massive losses on bad mortgage loans. Banks did not include in their *operating* earnings a significant portion of these losses because they were unusual. Although these loans were written off later, the profits were still included.

Today, most earnings projections are for *operating* earnings because they are easier to project. The media misuses this metric and invariably leaves out the term "*operating*" when quoting P/E ratios for the S&P 500.

For the S&P 500, the trailing 12 months (TTM) *reported* earnings are $107.23 per share. The *operating* earnings are $118.75 per share, which is 10.7 percent higher. This distinction matters when considering the TTM price/earnings (P/E) ratio for the S&P 500. At close to its recent high of 2,648, the TTM P/E ratio is 22.30 based on *operating* earnings. Based on *reported* earnings, the TTM P/E ratio is 24.69.

Putting it into Context

To put these P/E ratios into context, we can go back to the end of 2009 and see the range of P/E ratios during the economic recovery. Based on *operating* earnings, the TTM P/E ratio has ranged from a low of 11.95 to a high of 21.38 through the 2017 third quarter. Based on *reported* earnings, the TTM P/E ratio has ranged from a low of 13.01 to a high of 24.34. With this context, we can see that the S&P 500 is high. But is it too high?

What is driving stock prices is, of course, anticipated growth. Estimates are that *operating* earnings for the S&P 500 will end up to be $125.11 for 2017, and that *reported* earnings will end up at $114.92. Based on those estimates, the TTM P/E is 21.17 and 23.04 respectively, both of which are still at the high end of the range during the recovery.

As we look out to the end of 2018, earnings projections become fuzzy and are moving around. At the moment, the consensus is that S&P 500 *operating* earnings will end up being $144.21 per share, and that *reported* earnings will end up at $132.86. Based on these projections, the forward P/E is 18.36 and 19.93 respectively. These P/Es are less lofty but closer to their respective averages of 17.30 and 19.20 since 2009. However, both of these earnings projections are more than 20 percent higher than the current TTM earnings, and more than 15 percent higher than the 2017 year-end projections. These growth rates are high in comparison to the average of 10.7 percent year-over-year increases that have taken place during the recovery.

If we make a more reasonable assumption that earnings will grow 10.7 percent from today's levels in 2018, we are still looking at P/Es of 20.14 based on operating earnings, and 22.31 based on reported earnings – both of which are still at the high end of the historical range.

Reasons to be Cautious

It is not safe to bet on events that are already anticipated by the market. If the events actually happen, there is usually not much of a positive reaction because they were already anticipated. Of course, if they don't happen, the disappointment will translate into sinking prices.

We must keep in mind that the market delivers returns in waves, and not in measured doses. We have already had a long wave up, and prices are historically high, whether we measure them by either *operating* or *reported* earnings – as long as we make the distinction and keep them in their proper contexts. Accordingly, we are continuing to make out portfolio recommendations with caution in mind.

Energy & Natural Resource Selections

Oil ministers meet in Vienna on November 30 to decide on extending oil production limitations. OPEC countries need oil prices higher because of the need to balance their budgets. The table to the right shows the price of oil they required to balance their 2017 budgets. Saudi Arabia needed an oil price of $73.10 per barrel. On average, the OPEC countries needed $77.68 per barrel. With oil prices below these necessary prices, OPEC will continue to urge for oil production cutbacks wherever they can exert pressure.

One of OPEC's largest targets is Russia, which agreed to production cuts in the meeting. However, Russia produces slightly more than Saudi Araba and has new oil production coming on stream in 2018. Although it will benefit from higher oil and gas prices, Russia can get by with a lower price of $49.90 to balance its budget. So the agreement to cut back its production may change in the June OPEC meeting.

Meanwhile, these cutbacks are advantageous for US oil and gas producers which have more production coming on stream from the fracking boom.

Chesapeake Energy (CHK) is in a favorable position to benefit from the secular shift to clean burning natural gas fuel for power generation globally and in the Asia-Pacific region in particular, led by China's transition away from coal. More than 50 percent of the volume growth in the US in the near future will be used for export in the form of liquefied natural gas (LNG). Expanding exports along with the replacement of coal-fired power plants around the world is bound to ensure strong natural gas demand.

CHK has a portfolio of close to 8 million net acres of oil and gas assets inside the US, in the Powder River Basin, Eagle Ford, the Marcellus and Utica shale, along with the Haynesville/Bossier and Anadarko Basin regions. These large domestic assets make CHK well situated to participate in the resurgence of the US shale drilling.

The consensus is that CHK will earn 86 cents per share during the next four quarters, starting with 23 cents for the

Requisite Oil Prices

Prices Needed to Balance 2017 Budgets

OPEC Country	Balancing Price	2016 Oil Production
Algeria	63.80	1,348,361
Angola *	83.00	1,769,615
Ecuador *	78.00	548,521
Libya	102.00	348,686
Iran	54.70	3,990,956
Iraq	54.10	4,451,516
Kuwait	46.50	2,923,825
Nigeria *	127.00	1,999,885
Qatar	46.80	1,522,902
Saudi Arabia	73.10	10,460,710
United Arab Emirates	68.00	3,106,077
Venezuela *	216.00	2,276,967
Weighted Average	77.68	34,748,021
Competing Country		
Russia	49.90	10,551,497
US	n/a	8,856,809

Source of Oil Production: US Energy Information Administration
Source of Balancing Prices: International Monetary Fund
* Estimated figures provided by RBC Capital Markets

fourth quarter. At $4.00 per share, CHK's forward P/E ratio is close to 4.7 – very cheap. A forward P/E ratio of 10 puts the stock at $8.60, more than double the current price.

Chevron (CVX) announced in November that it consummated the second phase joint venture with state-owned Nigerian National Petroleum Corporation (NNPC). The project involves the production of natural gas liquids and condensate from Sonam and Okan fields in the Niger Delta. Nigeria, one of the biggest oil producing countries in Africa, represents a very significant portion of the total production volumes of Chevron. Last year, Chevron's Nigerian operations accounted for 235,000 barrels of oil equivalent per day.

Chevron's remaining holdings are set to increase production and revenue, including the two massive Australian projects, the Gorgon and Wheatstone, both of which had required large capital outlays that are no longer needed in CVX's forward-going cap-ex budget. The company is making large investments in its 1.5 million acre position in the prolific Permian Basin to boost its output by 400,000 barrels of oil per day in the next few years. CVX is well-positioned to see earnings growth in the years ahead, along with an attractive dividend that management says is "sacrosanct."

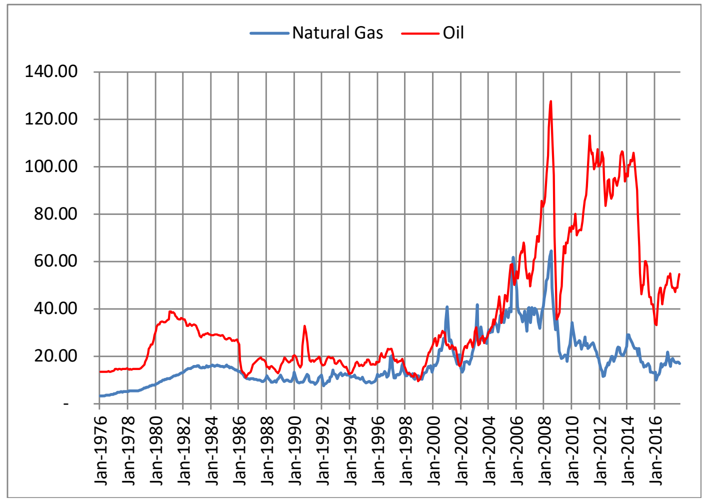
Chicago Bridge & Iron (CBI) has been through the ringer this year, but Patrick Mullen, who took over as CEO on July 1, is "resetting" the company culture by enhancing efficiency and risk management, optimizing interface management, and accelerating innovation. The company has made significant progress, including instituting a cost reduction program as well as improvements in project execution and risk management. The benefits of these programs are expected to be realized in upcoming quarters.

The consensus among analysts is that CBI will earn $195 per share during the next four quarters, starting with 47 cents in the fourth quarter. This puts the forward P/E ratio under 10 which is very cheap.

CBI is in the process of selling the company's Technology Operations business which is expected to produce sale proceeds in excess of $2 billion. After taxes, the sale proceeds could be used to eliminate the company's $1.8 billion of debt. The intent is to negotiate a long-term strategic alliance with the ultimate buyer because the engineering and techniques developed by that division are still useful to CBI.

Fidelity Select Natural Gas Fund (FSNGX) is a diversified way to participate in the growth of the natural gas industry through strong companies. Natural gas provides the same energy as oil for pennies on the dollar, and natural gas is more environmentally friendly. One barrel of oil provides approximately 5.8 million British Thermal Units (BTUs) of energy. At the current price of $63.57 a barrel, that is the cost of 5.8 million BTUs. However, with the current market price for natural gas at $3.06 for one million BTUs, 5.8 million BTUs will cost $17.75. Thus, the same amount of energy is available for approximately 28 cents on the dollar, if it is in the form of natural gas rather than oil.

The Cost of Energy Equivalents of Oil and Natural Gas



The updated chart shows the historic relationship between the costs of these two forms of energy. The red line shows the price of a barrel of oil since the mid-1970s. The blue line shows the price of natural gas multiplied by 5.8 to approximate the same amount of energy contained in a barrel of oil. The fact that natural gas provides energy for pennies on the dollar will translate into an expanding natural gas industry.

ICON Energy Fund Class S (ICENX) is also a diversified way to participate in the expansion of the energy sector with a basket of substantial companies. The hallmark of this fund has been its ability to look for changes within the energy sector to capture value, rather than simply depending on rising oil prices. This fund is a good way to capture today's values and profit from the recovery and changing landscape on a diversified basis with professional management.

Valero Energy (VLO) continued to see its crack spreads – the profitable difference between the price of oil and the price of gasoline and other refined products -- widen in all its geographical areas. Valero's total-debt-to-capital ratio stood at 29% at the end of the third quarter, below its major competitors, Marathon Petroleum, Andeavor, and Phillips 66. This gives the company greater flexibility to leverage its position in the marketplace. For the longer run, we continue to see Valero in a unique position to benefit from a US conundrum. Prior to the US shale revolution, most US refineries were constructed to process imported oil which is a heavy (thick) and sour (high sulfur) grade. The oil from fracking US shale cannot be processed at these refineries because it is light sweet crude. Additionally,

Hospitality REITs Comparison Table

Company Name	Symbol	Recent Stock Price	Dividend Yield	Stock Market Cap Rate	Portfolio Value @ 7.5% Cap Rate ($Millions)	Stock Value	Discount (-) Premium (+)
RLJ Lodging	RLJ	21.68	6.1%	10.9%	9413.79	38.21	-43.9%
Hospitality Properties	HPT	29.99	6.8%	10.1%	11,616.3	48.11	-37.7%
Hersha	HT	17.55	6.4%	8.9%	2,257.6	19.19	-8.6%
Host Hotels & Resorts	HST	19.79	4.0%	9.4%	21.6	25.75	-23.2%
Apple Hospitality	APLE	19.48	6.2%	8.2%	6,114.9	21.86	-10.9%

The table above shows the "Stock Market Cap Rate" (what the stock price is paying for the underlying real estate portfolio) for several comparable hospitality stocks. The "Stock Value" column shows the current value of the stock assuming the underlying portfolios are valued using a cap rate of 7.5 percent, which is close to the average cap rate on recent hotel transactions. The last column shows the discount or premium at which the stock is trading based on a 7.5 percent cap rate valuation of each company's real estate portfolio.

Hospitality Properties (HPT) has the second largest discount. However, this company is externally managed by RMR which charges high fees and suppresses value. As long as RMR continues to externally manage HPT, we do not expect to see significant growth. **Host Hotels and Properties (HST)** is very small, with only 749 thousand shares outstanding, which may lead to excessive volatility. Growth may be limited by its small capitalization.

refineries on the east and west coast do not have access to the US crude oil pipeline network, so they must rely on imported oil arriving in US ports for their feedstocks. This is evidenced by the fact that we are still importing nearly half of our oil needs, while US storage tanks in Cushing, Oklahoma, are brimming with the light sweet crude fracked from US shale.

Valero is well-positioned to take advantage of this conundrum because it has the flexibility to refine substantial quantities of both US light sweet as well as heavy sour crude. It also has access to the US pipeline network for delivery to its gulf coast locations. This flexibility allows VLO to capture the highest margins among its competitors. It can take advantage of the best discounts for its feedstocks, whether it's low or high-quality crude, or light sweet or heavy sour.

Real Estate Selections

Our posture is still defensive with regard to real estate stocks. Commercial real estate prices are historically high because low interest rates have pushed down real estate cap rates to historically low levels (like bond yields). The *Sound Advice* portfolio only includes real estate stocks offering an extraordinary value now. Two REITs currently exist in the hospitality industry along with one mutual fund.

Hersha Hospitality (HT) has completed its upgrading cycle. As future quarters are included, the trailing income will include upgrades to the portfolio, which is bound to cause the net operating income and the net asset value to increase.

During the last several years, Hersha has reported several hotel transactions at cap rates ranging from 5.4 to 8 percent. To be on the conservative side, we can establish a "Main Street" cap rate at the high end of this range of 7.5 percent for valuation purposes.

Based on the latest trailing four quarters' financials, including the most recent 2017 third quarter results released at the end of October, and using a 7.5 percent cap rate to evaluate the company's real estate portfolio, we value HT at $19.19 per share which is higher than the current price. This valuation is low because the third quarter income suffered from the disruption from Hurricane Irma to their south Florida properties, which led to the closure of six hotels in September. Following the dissipation of the storm, the company's primary focus was devoted to resuming operations at four of those least impacted by the storm. The disruption was more significant at the Cadillac Miami Beach and Parrot Key hotels where more substantial reparations are required.

Looking into 2018, the company sees a recovery in the region based on the reopening of the Miami Convention Center and a diminished supply of competing hotels. Meanwhile, revenue growth remained healthy from its eight hotels on the West Coast and its 10 New York City hotels. The dividend yield is attractive and lowers the risk profile.

RLJ Lodging Trust (RLJ) is selling at a steeper discount to its hotel assets than HT. Based on the latest trailing four quarters' financials reported, including the most recent 2017 third quarter, and using a 7.5 percent cap rate to evaluate the company's portfolio, we value RLJ at $38.21 per share which is considerably higher than the current price. The high dividend yield is also attractive and lowers the risk profile.

Third Avenue Real Estate Value Investor Fund (TVRVX) is a global real estate fund which means it is not confined to US real estate with low cap rates. Management looks for growth more than current income by focusing on real estate operating companies which, unlike REITs, can reinvest profits back into the business. Management also searches for opportunities in different aspects of a real estate company's capital structure by investing in senior debt in addition to equity. Also unlike the typical REIT, management will go to cash when asset prices are generally high. Cash is preserved for scooping up opportunities.

TVRVX is loaded with good values substantially below net asset value (NAV) with strong growth prospects. Management has a similar approach to ours because it is very price conscious, especially in relation to net asset value. Just as we do at *Sound Advice,* they eat their own cooking – they invest a substantial amount of their personal assets into their funds.

Medically-Related Selections

The cloud of uncertainty still blankets the healthcare industry now that the repeal and replacement of the Affordable Care Act (Obamacare) is dormant. We are comfortable with our current recommendations in this sector based on their own individual merits.

Boston Scientific (BSX) has been a global medical technology leader for three decades by providing a range of high performance solutions aimed at addressing medical needs and reducing healthcare costs. BSX's medical products are well suited for an aging population.

One of BSX's premier products is a subcutaneous implantable cardioverter-defibrillator (S-ICD) for the treatment of patients with ventricular arrhythmias and the prevention of sudden cardiac death. In November, the American Heart Association (AHA), the American College of Cardiology (ACC), and the Heart Rhythm Society (HRS) updated guidelines to formally recommend the use of S-ICDs. The Boston Scientific EMBLEM™ MRI S-ICD System is the only S-ICD on the market, and the only implantable defibrillator available that does not touch the heart.

Stryker (SYK) is continuing to fuel growth through acquisitions. In September, it purchased Novadaq Technologies to enhance its position in the endoscopy market. Novadaq's extensive research team is also bound to expand Stryker's capabilities in imaging. In late October, Stryker acquired the majority of Vexim which expands its portfolio of minimally invasive technologies and complements Stryker's interventional spine business. Stryker's healthy balance sheet has allowed it to make many acquisitions in the recent past which are now paying off, such as Mako whose surgical robots have been used in 50 percent of the 9,400 Mako knee surgeries since the launch in mid-2016.

For the full year, the company expects earnings to be within the range of $6.45 to $6.50 on organic sales growth of 6.5% to 7.0%.

SYK is best known for its orthopaedic devices for artificial knees and hips. The company provides a diverse array of innovative medical technologies, including reconstructive, medical and surgical, as well as neuro-technological and spine products.

Tekla Life Sciences Investors (HQL) is a good way to invest in the most explosive profits in the healthcare industry with a portfolio of biotech companies. Over the last 15 years, biotechnology has become a major industry and the source of the world's top breakthrough drugs. Biotech companies tend to be high risk and high reward investments which makes diversification essential.

Financials

Banks will benefit from rising interest rates. The Federal Reserve's most recent "Stress Test" on US banks revealed that US banks have sufficient levels of capital to weather severe situations similar to those of the 2008-09 melt-down. Our two recommended banks were given a clean bill of health.

JP Morgan Chase (JPM) expects to earn $6.89 per share in 2017. Strong growth is expected in the immediate years ahead. JPM is expected to earn $7.68 per share in 2018. At a forward P/E ratio of 15, JPM would be $102 by the end of 2018. JPM is still currently cheap in comparison to the rest of the market.

Wells Fargo (WFC) expects earnings to be $4.05 per share in 2017, and $4.32 per share for 2018. At a P/E ratio of 15, WFC would be $65 in 2018. WFC is also currently cheap in comparison to the rest of the market.

Small Caps

Numerous studies show that small caps perform better over the long run than the market as a whole. Small Caps are pure plays on the early stages of new industries and inventions. They have more dynamic and entrepreneurial management, and they are much more likely to be the target of an acquisition or merger, which is usually quite profitable.

Third Avenue Small-Cap Value Investor Fund (TVSVX) invests in companies with small capitalizations using the same value-oriented approach as it does with its real estate value fund (TVRVX). Management scours the investment universe for companies that combine the three main features: creditworthiness, a meaningful discount to a conservatively estimated net asset value, and the ability to consistently grow NAV, with an initial targeted holding period of three to five years. A patient and price conscious acquisition is a critical first step in both protecting capital and in realizing an attractive investment return.

Special Situations

The rest of our portfolio falls into other market sectors, with companies that are presenting extraordinary values within their respective industries. Here they are in alphabetical order.

Apple (AAPL) has inaugurated a badly-needed upgrade cycle by introducing the iPhone 8 and 8 Plus in September, aimed at the mainstream market, and its premium smartphone, dubbed the iPhone X, which retails at a relatively high price point, beginning at $999.

The iPhone 8 will likely account for most of the customer upgrades in the coming quarters, both in the US and in the Chinese market. Initial reports are that demand is overwhelming supply for the iPhone X. These phones are becoming one of the hottest holiday gifts.

Earnings are widely estimated to grow at double-digit rates for the next few years, stemming from direct iPhone sales, a booming services business, along with new additions to the Apple Watch and Apple TV programs. It is interesting to note that Apple's products, other than iPhones, accounted for most of the company's revenue growth in the most recent third quarter.

The company has a pristine balance sheet, with as much cash as long-term debt. The company carries the highest A++ financial rating. Earnings growth should also lead to dividend increases and more stock buy-backs. The P/E is close to 15, which is still at a discount to the rest of the market.

Intel (INTC) announced in November a new partnership with Advanced Micro Devices (AMD) to build discrete GPUs (graphics processing units) for ultra-thin laptops and notebooks. NVIDIA has a 70% share of the GPU market. Previously, AMD has lacked the of financial resources to compete with NVIDIA. Intel has lacked the GPU technology. The AMD-Intel partnership should also enable Intel to capture more of the data center and self-driving markets.

The recent Mobileye acquisition launched Intel into the burgeoning assisted-driving and autonomous vehicle arena, and extends to markets for autonomous ships, planes, drones, and a wide range of weapons. Tesla has announced that it will be using Intel's chips instead of those from NVIDIA to power its massive infotainment console. The new Model 3 and new versions of Tesla's Model X and Model S will rely on the Intel chips. Intel is also a supplier to Alphabet's GOOGL Waymo self-driving car unit. Fiat Chrysler has joined Intel's automotive partner base. The company's team also includes BMW.

The size, diversity, and industry dominance of Intel offers a relatively safe investment in a high-growth, and often high-risk business. Intel can leverage new technology into its existing large platform without introducing unacceptable risks. A history of established cash flow and an attractive dividend, along with the currently low P/E ratio, diminishes the risk profile of the stock. Yet, substantial growth prospects have been introduced that now justify a higher P/E and thus, a higher stock price.

The company forecasts 2017 earnings of $3.25 a share. The current price/earnings (P/E) ratio is still modest and considerably below the rest of the market. The current dividend yield is also attractive which lowers the risk profile.

International Business Machines (IBM) increased its share buy-back program in November by $3 billion, raising the total to $4.5 billion. IBM is turning into a growth stock but it is not priced like one. Growth is emerging from the company's "strategic imperatives" division, which include businesses like cloud computing, analytics, mobility, and security. IBM's "Z system" of mainframe computers is also promising. The latest iteration is the z14, released in mid-September. According to IBM, the z14 mainframe is the biggest reinvention of its mainframe technology since the reinvention of Linux and open source software 15 years ago.

Watson, IBM's super computer, is the closest thing to artificial intelligence because it can "think" like a human. Watson cognitively scans a world of data and applies relevant information to what it learns about a company's business and systems to create new revenue streams, reduce expenses, and make existing operations more efficient.

IBM is a good value now. The company expects 2017 earnings to be $13.80 per share. The stock is still selling at a P/E ratio substantially below the market. At $160 per share, the stock is only 11.6 times earnings, as compared to the overall market of 24. A P/E ratio of 15 puts IBM above $200 per share.

While we are waiting for growth, the $6.00 annual dividend provides an attractive yield.

NCR Corp (NCR) announced in November that it collaborated with Samsung to launch the NCR Silver

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Quantum, a point-of-sale (POS) commerce station featuring an integrated payment device with mobile wallet acceptance capability, customer display, loyalty scanner, and Samsung Galaxy tablet. It also gives merchants a more efficient way to manage back-office operations.

The company expects to earn $3.10 to $3.20 per share for 2017. The P/E is currently below 11, a considerable discount to the rest of the market. At a P/E ratio of 15, the stock belongs close to $47 per share.

NCR makes automatic tellers (ATMs), retail point-of-sale (POS) workstations, self-service kiosks, and other self-service checkout systems. 485 million people use NCR products every day, and there is room for substantial growth in the US and around the world.

Symantec (SYMC) reported disappointing quarterly earnings in early November which depressed the stock price. The primary reason was because of a shift in demand for Symantec's Integrated Cyber Defense platform. While this shift is lowering near term profits, it is a validation that customers are designing Symantec's multi-product platform into their future security architectures, which will lead to more reliable revenue over the longer term.

Symantec is the world's leading cyber security company offering organizations strategic, integrated solutions to defend against sophisticated attacks across endpoints, cloud, and infrastructure. Symantec operates one of the world's largest civilian cyber intelligence networks, allowing it to see and protect against the most advanced threats. Our mantra with this stock has been "If there ever was a more certain growth industry, protection from cyber espionage is it."

Tetra Tech (TTEK) reported its fourth quarter earnings in November of 63 cents per share, slightly higher that expectations. Revenue also grew above expectations. The strongest growth came from the Water, Environment and Infrastructure segment with revenues 8.7 percent higher than one year ago. Tetra Tech's backlog from ongoing operations reached a record high of $2.54 billion, an increase of 8 percent year-over-year.

Tetra Tech is a leading company in water technologies and environmental remediation. The company's backlog reveals a robust pipeline with major governmental organizations like the US Department of State, Environmental Protection Agency (EPA), US Army Corps of Engineers, and the US Air Force, which should continue to bolster growth. TTEK has a very healthy balance sheet.

Xerox (XRX)expects 2017 earnings to be in the range of $3.28 to $3.44. This puts XRX below 10 times earnings - very cheap, especially in comparison to the rest of the market. The dividend yield is also attractive.

XRX has new separate leadership and goals which is bound to translate into better focus execution. CEO, Jeff Jacobson, is bringing a new enthusiastic corporate culture and a three-year strategy for growth by rolling new products aimed at mid-size companies which are stronger growth targets than large-scale businesses. The new line of "ConnectKey" workplace assistants has had positive results, as a way of connecting workstations to an office Xerox printer (copier) with a variety of cloud applications. Xerox is shipping 29 new ConnectKey products around the world, which is improving fourth quarter revenue.

XRX has made good progress this year optimizing its balance sheet to support both a strong cash flow in the future as well as its investment-grade credit profile. The company ended the third quarter with $1.8 billion in cash, and operating cash flow was $44 million higher than one year ago.

Hedging the Portfolio

The **ProShares UltraShort S&P 500 (SDS)** is a reverse ETF that essentially short-sells the market and will benefit from down-drafts in the S&P 500. It is designed to produce two times the daily fluctuations of the S&P 500 index. A decline of say, 1.0 percent in the S&P 500 will cause SDS to increase by 2.0 percent. Conversely, an increase in the S&P 500 will cause SDS to decline in the same fashion. We have been tracking SDS and confirmed that it is performing as it should, with daily premiums and discounts within 0.5 percent. It is also very liquid.

ETFs for Rising Interest Rates

The Fed's swollen bond portfolio has a preponderance of longer term bonds. That means that the upcoming reduction of the Federal Reserve's long-term bond holdings will add a disproportionate amount of upward pressure to long-term bond yields. This is important because our recommended ETFs are designed to benefit from an increase in long-term bond yields.

Rising inflation will also push up long-term bond yields in order to furnish investors with a real return in the vicinity of 3 percent. With inflation pushing above 2 percent, yields should be close to 5 percent, giving these ETFs a tremendous upside potential.

Our recommended ETFs differ in the amount of leverage used. You can choose among them depending on your investment objectives and risk tolerance.

The **Direxion Daily 20 Plus Year Bear 3 Shares (TMV)** uses 3:1 leverage.

The **Proshares UltraShort Lehman 20 Plus Year Treasury (TBT)** uses 2:1 leverage.

The **Proshares Short 20 Plus Year Treasury (TBF)** uses no leverage.

The price action of these ETFs is based on the changes in long-term Treasury bonds, as measured by benchmark bond indexes, only in the opposite direction, and then multiplied by the leverage each ETF uses. For example, a decline of say, 1.0 percent in their respective benchmarks will cause TMV to increase by 3.0 percent, TBT by 2.0 percent, and TBF by 1.0 percent. Conversely, an increase in their respective benchmarks will cause these ETFs to drop in the same fashion.

We can project the movements of these ETFs based on any given scenario. We have been using the Federal Reserve's prediction, which was as good as any. As part of the Federal Reserve's quarterly Federal Open Market Committee (FOMC) meetings, each of the committee members makes a prediction regarding the future path of interest rates. Those predictions are plotted in the so-called "Dot Plot".

The most recent Dot Plot was taken at the September meeting. The median prediction was that the Federal funds rate would be 2.125 percent at the end of 2018, and 2.69 percent at the end of 2019. The FMOC is predicting that the Federal funds rate will rise in the months ahead because the Federal Reserve wants to bring short-term interest rates back to more normal levels from the extremely low levels used to stimulate the economy out of the 2008-09 crash.

We are using the Fed's dot plots of Federal funds as a means to predict changes in short-term interest rates, and making the assumption that long-term interest rates will move in tandem in order to maintain the same long-term real returns that exist today. While this should be a reasonable guide, it will be changes in inflation expectations that will ultimately govern long-term interest rates and the behavior of of these ETFs.

Recently we have seen a flattening of the yield curve (the difference between short and long-term interest rates) because the Fed has been raising (normalizing) short-term interest rates while a perceived mild inflation rate has kept long-term interest rates low. However, we are predicting that this flat condition will change as inflation heats up, and forces long-term interest rates up from historically low levels. However, in the spirit of trying to be conservative, we can assume that the yield curve will remain as flat as it is today, which means that long-term Treasury bond yields move in accordance with the Dot Plot target points. Accordingly, long-term Treasury bonds would be yielding 3.95% by the end of 2018, and 4.51% by the end of 2019.

Here is what would happen to each ETF:

TMV would rise from $18.65 to $33.12 by the end of 2018, and to $42.85 by the end of 2019.

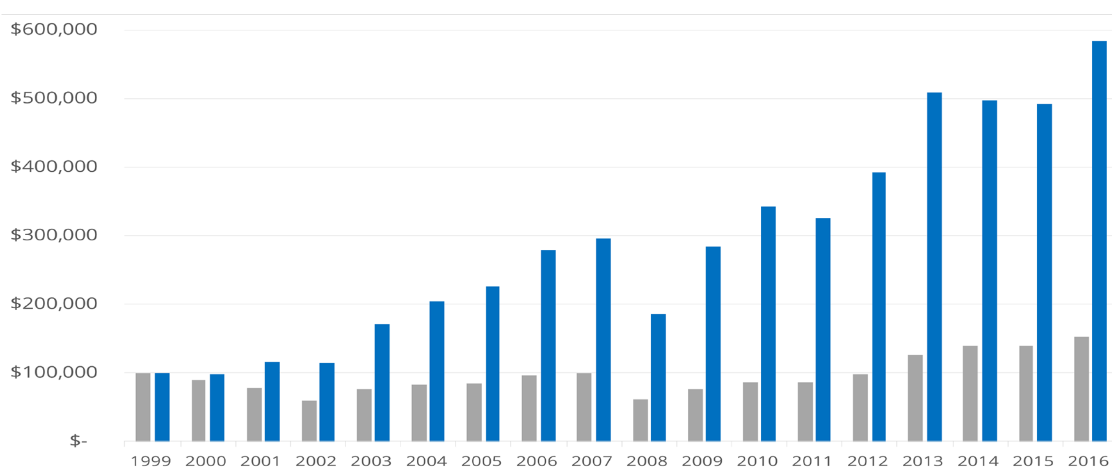
TBT would rise from $35.05 to $51.41 by the end of 2018, and to $61.05 by the end of 2019.

TBF would rise from $22.26 to $26.96 by the end of 2018, and to $29.38 by the end of 2019.

The Erosion Factor

As we point out regularly, these ETFs suffer from erosion because they decline slightly faster than they increase with an equivalent change in bond yields, particularly with higher leverage. To gauge this factor, we can assume that Treasury bond yields simply tread water, rising and falling by an unusually large amount, say, 0.03 percentage points (3 basis points) every day, and thus go nowhere. By the end of 2018, TMV would decline to $17.61 (5.6%), TBT would decline to $34.00 (3.0%), and TBF would decline to $22.01 (1.1%). While not insignificant, this erosion factor is nominal in comparison to the price swings caused by a change in bond yields.

Sound Advice vs the S&P 500



This chart shows the growth of $100,000 invested in the S&P 500 (in gray), which would have grown to $152,379, versus $100,000 invested in the *Sound Advice* recommendations (in blue), which would have grown to $584,161.

Energy/Natural Resources	Symbol	Price / NAV	Yield	Action	Limit
Chesapeake Energy Corp	CHK	$4.07	0.00%	BUY	$4.50
Chevron	CVX	$118.99	3.63%	BUY	$123.00
Chicago Bridge & Iron	CBI	$16.32		BUY	$19.00
Fidelity Select Nat. Gas Fund *	FSNGX	$23.63	0.52%	BUY	$25.00
ICON Energy Fund Class S *	ICENX	$12.64	0.44%	BUY	$14.50
Valero	VLO	$85.62	2.80%	BUY	$88.00
Real Estate					
Hersha Hospitality Trust	HT	$17.55	6.38%	BUY	$19.19
RLJ Lodging Trust	RLJ	$21.68	6.09%	BUY	$24.00
Third Avenue Real Estate Value Investor *	TVRVX	$35.32	0.47%	BUY	$37.00
Medically Related					
Boston Scientific	BSX	$26.28	0.00%	BUY	$28.00
Stryker Corp.	SYK	$156.00	1.09%	BUY	$160.00
Tekla Life Sciences Fund	HQL	$18.91	0.00%	BUY	$22.00
Financials					
JP Morgan Chase	JPM	$104.52	2.14%	BUY	$108.00
Wells Fargo	WFC	$56.47	2.76%	BUY	$59.00
Small Caps					
Third Avenue Small-Cap Value Investor Fund *	TVSVX	$23.63	0.28%	BUY	$25.00
Special Situations					
Apple	AAPL	$171.85	1.33%	BUY	$178.00
Intel	INTC	$44.84	2.43%	BUY	$49.00
International Business Machines	IBM	$153.97	3.90%	BUY	$165.00
NCR Corp	NCR	$31.29	0.00%	BUY	$35.00
Symantec	SYMC	$28.97	1.10%	BUY	$35.00
Tetra Tech	TTEK	$50.00	0.72%	BUY	$52.00
Xerox	XRX	$29.66	0.94%	BUY	$33.00
ETFs for Rising Interest Rates					
ETF - Direxion Daily 20+ Yr Bear 3X	TMV	$18.65	0.00%	BUY	$22.00
ETF - ProShares Short 20+ Year Trsry	TBF	$22.26	0.00%	BUY	$24.00
ETF - ProShares UltraShort 20+ Year Trsry	TBT	$35.05	0.00%	BUY	$40.00
Hedges					
S&P 500 ProShares Ultra Short ETF	SDS	$42.07	0.00%	BUY	$48.00

This table has live prices, charts & buy limits on our website: http://www.soundadvice-newsletter.com/members

Notes to the table: The right hand column is the highest recommended price limit for purchases.
See our website for live pricing and buy limits: **http://www.soundadvice-newsletter.com/members**
* It is no longer possible to offer live pricing on our recommended mutual funds.

General Comments: Our statistics are based on the assumption that $10,000 is invested in each position. When a new position is added, we assume the same $10,000 amount is invested in the new recommendation. When we recommend adding to a particular position, as we have done over the years, we assume another $10,000 is invested again in that position.

If you are picking and choosing, you can focus on the sector of the portfolio that matches your investment objectives. Alternatively, you may have a higher degree of comfort with certain industries, funds, or stocks because of past experience or your profession. In that case, you may want to invest more heavily in one sector, or in one or more individual recommendations.

As always, broad diversification will temper volatility, add to safety, and improve long-term performance.

Capital Competition: Real Estate versus Stocks: The **Sound**Advice Risk Indicator

There are few forces that are more important to a market's destiny than the amount of capital that is available to it. In a normal situation, capital will flow easily between markets as their underlying conditions change. But if a market becomes dangerously superheated, it will absorb a larger proportion of available investment capital than economic conditions and market demand can justify. This change will be reflected not only in the rising market's prices but also in the prices of competing markets, which will be lower than their underlying fundamentals would indicate they should be. Over the last 100+ years, we can see this titanic struggle between the stock market and its foremost competitor for investment dollars: real estate.

To reveal this phenomenon, we have set up an equation in which we divide the Standard and Poor's 500 Stock Index average by the median price of a new house for each month over the last 100+ years. This equation exhibits an elegant financial minuet as each market has taken turns outperforming the other.

As we look at the historical data, we find that there is a range in which the price disparities are so strong that they are too great to be accounted for by the fundamental economic conditions underlying each market. Every time prices get into these danger zones it has meant that the prices in one market or the other have gone too high, and that they are in imminent danger of falling.

We can, therefore, label this new tool the **Sound**Advice "Risk Indicator," since it will allow us to locate the point at which prices are so high when compared to competing markets that they have come loose from their moorings and are on the verge of declining or under performing the other market.

What is too high? When stock prices are very high relative to house prices, the **Sound**Advice Risk Indicator will rise over the line marked 2.0, revealing a high-risk time for stocks. In contrast, when the indicator drops below the line marked 1.0, it means that it is a very low-risk time to buy stocks. Notice from the chart how the **Sound**Advice Risk Indicator has oscillated back and forth, revealing the ongoing struggle between Stocks and houses for investment capital. We have labeled these long vacillations Supercycles.

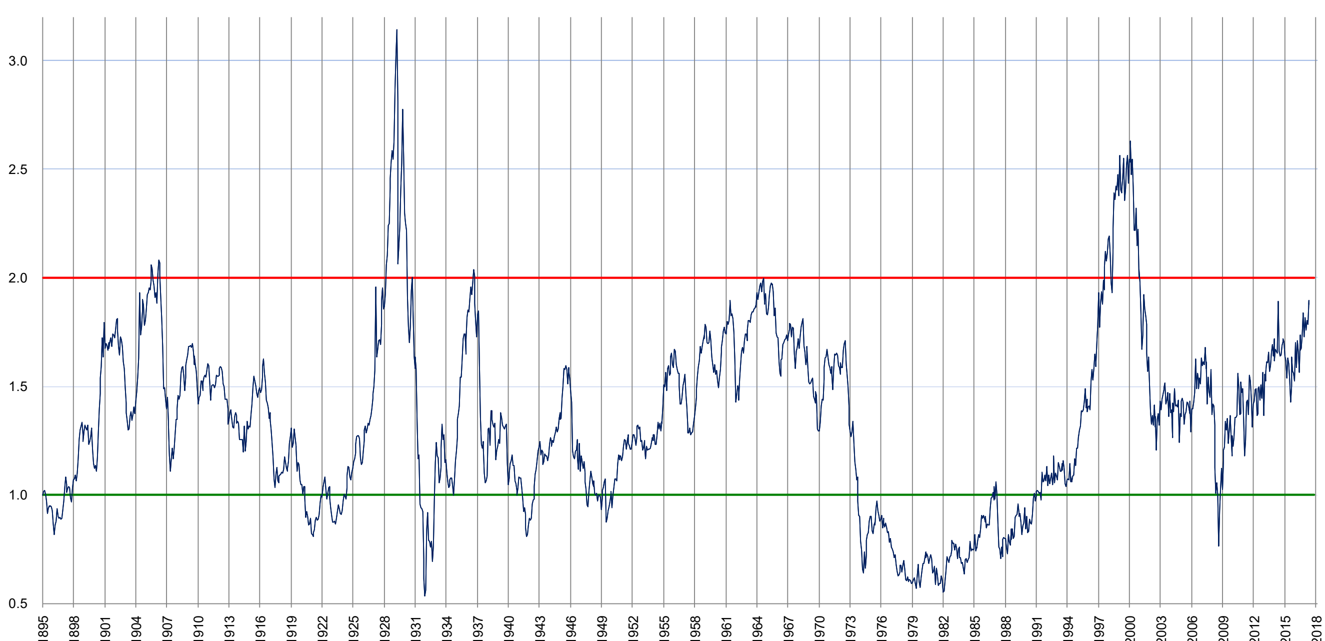
The figures show that over the entire century-plus, stock prices have outperformed housing prices. Just based on the price growth of each investment market and assuming no leverage was used, a $25,000 investment would have grown to $15.6 million in stocks and to $1.72 million in houses.

> The New York Times
>
> ***"Cardiff's equation reveals an elegant financial minuet as each market takes turns outperforming the other."***

But though an investment beginning with $25,000 in 1895 could have made money being in either stocks or housing and simply leaving it there over such a long period of time, had the investor followed the signals of the **Sound**Advice Risk Indicator he would have made $618 million, or 39.7 times more money—the difference between profits the buy-and-hold stock market strategy would have yielded by itself and the profits that the **Sound**Advice Risk Indicator would have provided.

The February 2009 reading of 0.77 marked the low for this cycle as well as the beginning of Supercycle 6. **Based on latest median house price of $324,900 for September, and with the S&P 500 at 2647 at the end of November, the SoundAdvice Risk Indicator reads 1.88.**

The **Sound**Advice Risk Indicator



Business Cycles and Stocks:
The **Sound**Advice Diffusion Indexes

If the Supercycles identified by our Risk Indicator are the solemn, inexorable seasons that roll across the market's landscape, business cycles are the highly visible, sometimes serene but frequently blustery fronts and storms that we actually perceive as weather. The Risk Indicator has given us a reliable tool to determine the investment season in the stock market. This information is all-important; there will be no heat waves in January, no blizzards in July. But in our search for fair winds, we need to know more than the season. We also must be able to predict the shorter-term weather -- the bull and bear markets that fluctuate along the path of Supercycles.

The data we need is contained in the leading and lagging economic indicators published monthly by The Conference Board. We have hand picked the most sensitive of these economic indicators to produce our "Diffusion Indexes" which function with amazing accuracy as predictors of the birth of cyclical bull and bear markets in stocks.

To construct our **Sound**Advice Diffusion Indexes, we observe changes in each of our selected indicators over a six-month period, and take the percentage of those increasing.

When the **Sound**Advice **Diffusion Index of LEADING Indicators** drops to zero, it is time to buy stocks aggressively, regardless of how negative the atmosphere may be. This is not just an empirical coincidence. It is also logical. In order for all of the leading economic indicators to be giving off a zero value compared to six months before, it is nearly certain that the soft economy is providing an atmosphere for stable or declining interest rates.

This Diffusion Index gave us a zero reading in April, 2009, close to the bottom, officially giving us an "Aggressive" signal. That signal came at a time when the Risk Indicator was below 1.0, which revealed that Supercycle 5 came to an end, and that Supercycle 6 was born.

The **Sound**Advice **Diffusion Index of LAGGING Indicators** gives "Caution" signals when all three of its individual lagging economic indicators rise above their respective levels of six months earlier, providing a 100 percent reading. This reading reveals that the US economy is strong enough to put upward pressures on interest rates.

Current Status

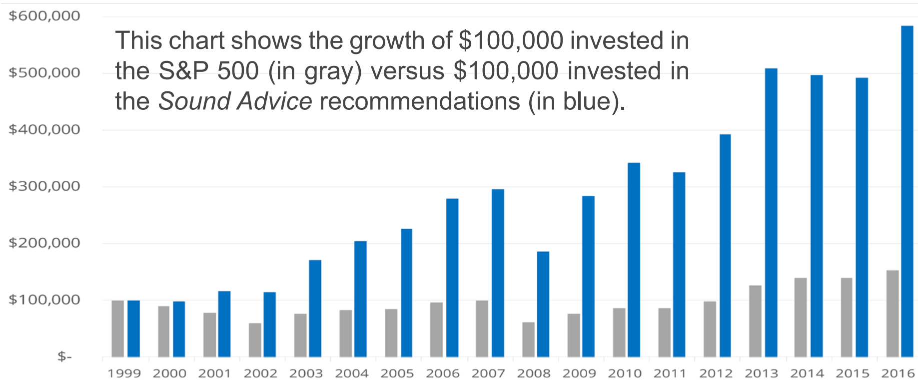
The Sound Advice **Diffusion Index of LEADING Indicators dropped to zero in September because of weakness in the employment and building permit components caused by the temporary impact of the hurricanes. While this was an official reversal of our Caution Signal, we did not change our cautious approach to the market because it is likely that this Aggressive signal will be reversed soon, as the affected area begins to rebuild and hire the massive number of workers needed for rebuilding.**

Indeed, the leading indicators rebounded in October (the most recent data). The Conference Board commented that the strength in the leading indicators became more widespread, rising at a 5.9 percent annual rate which is faster than in the previous six months. As a result of this strength, the Sound Advice **Diffusion Index of LEADING Indicators jumped from zero to 66.7 percent.**

Our next official "Caution" signal will come from a 100 percent reading on the Sound Advice **Diffusion Index of LAGGING Indicators, which was 66.7 percent in October. The one lagging indicator that kept this Diffusion Index from rising to 100% was the Duration of Unemployment, which is certain to recover in the months ahead as people go back to work in the areas affected by the hurricanes (as well as in the recent wildfire areas of California).**

Track Record of the **Sound**Advice Diffusion Indexes

Aggressive	S&P	Caution	S&P
Sep-74	68.1	Apr-76	101.9
Jul-76	104.2	Dec-76	104.7
Oct-78	100.6	Jun-79	101.7
Nov-79	100.0	Oct-83	167.7
Aug-84	164.5	Jun-85	188.9
Jul-86	240.2	Aug-87	329.4
Feb-88	258.1	Jun-88	270.7
Mar-89	280.0	Mar-93	449.7
Mar-95	493.2	Dec-98	1,141.0
Jun-00	1,429.4	Dec-00	1,320.3
Jun-03	974.5	May-05	1,191.5
Jun-06	1,276.7	Mar-08	1,325.4
Apr-09	848.2	Mar-12	1,370.3
Mar-15	2,080.0	May-15	2,111.9
Sep-17	2,492.8		
Ave +/-	30.2%		3.8%



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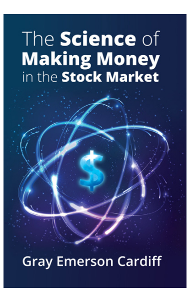

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