

## Don't Fight the Fed

Once again, this old Wall Street axiom has proved to be a reliable guide, and still needs to be heeded.

In our January 1, 2022, issue of *Sound Advice*, we warned that *“historically low interest rates and bond yields have pumped up stock prices in 2021, but as we roll into 2022, those buoyant forces will be attenuating. By April, these forces will be gone, and the specter of rising interest rates will start haunting the markets.”*

Following the Federal Reserve meeting in the last week of January, Chairman Powell confirmed that the quantitative easing (QE) bond-buying program would proceed at just \$30 billion in February (down from \$80 billion per month), and would officially end in March, at which time interest rate increases would begin.

By the time the quantitative easing (QE) program ended in March 2022, the Federal Reserve had pumped up M2 (a broad measure of the money supply) by 41.1 percent since April 2020. To put this into context, M2 has averaged an annual growth rate of 6 percent since 1980, rarely increasing by low double-digit rates.

As the year progressed, the Federal Reserve realized that it must arrest the inflationary spiral by raising interest rates aggressively from historic lows. By the end of July, inflation had risen to 9.1 percent, and the Federal Reserve had raised its Federal Funds rate from zero to 2.5 percent. However, the remaining large gap revealed that the Federal Reserve was still “behind the curve”, playing catch-up to quell the inflationary spiral that it had contended was only transitory.



*Gray Emerson Cardiff,  
Editor Since 1988*

Investment returns in prior years have been calculated independently by the Hulbert Financial Group and concur with ours. From 2000 through 2021, the *Sound Advice* model portfolio averaged a 9.5% annual return versus 5.7% from the S&P 500.

In July, Chairman Powell said the Federal Reserve is “strongly committed” to reducing inflation but that it could come with a cost to general economic growth and the labor market in particular. *“We think it is necessary to have growth slow down. The economy probably will grow below its long-run trend for a period of time. We need a period of growth below potential in order to create some slack.”* Indeed. The large gap between inflation and interest rates meant that interest rates had much further to rise in order to force the economy to slow down significantly.

In August, Powell delivered a stern commitment following the Federal Reserve’s symposium in Jackson Hole. He said that the central bank will use its tools forcefully to attack inflation by moving to a purposefully restrictive policy stance to return inflation to 2%, warning that higher interest rates, slower growth, and softer labor

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market conditions will bring “some pain” to households and businesses.

In the September Federal Reserve meeting, it raised the Federal Funds rate by another 0.75 percentage points (75 basis points) and indicated that another hike by 1.25 percentage points will be needed by the end of the year. Powell said, “My main message has not changed since Jackson Hole, the FOMC [Federal Open Market Committee] is strongly resolved to bring inflation down to 2%, and we will keep at it until the job is done.”

We have yet to see “some pain”. At the end of September, the Conference Board reported a significant increase in consumer confidence, which is important because consumer spending is two-thirds of US GDP. So the Federal Reserve’s job is not done.

## The Sound Advice Indicators

Because of the correction in the stock market and the continued rise in house prices, the **Sound Advice Risk Indicator** (page 10), which compares the S&P 500 index to house prices, was 1.83 in September. The risk in the stock market has declined but is still above average.

The **Sound Advice Diffusion Indexes** (page 11) remain in “Caution” mode. During “Caution” signals over the last 47 years, the S&P 500 has either crashed, meandered, or climbed moderately, recording an average decrease of 0.9 percent. With the market down 25 percent+, this time is proving to hold true once again.

It is still a risky investing landscape now, and it will remain so until interest rates stop increasing. When will that be?

The Sound Advice Diffusion Index of Leading Indicators (page 11) is bound to tell us. It has been extraordinarily accurate at revealing such times in the past. During “Aggressive” signals, the S&P 500 climbed an average of 31.5 percent.

## The Sound Advice Portfolio

All of the Sound Advice model portfolio recommendations are made with our current “Caution” mode in mind. Our portfolio is made up of selections that are most likely to prosper despite adverse market

conditions or will directly benefit from inflation and rising interest rates.

These selections, as well as their dividend yields, and buy/hold/sell recommendations, are summarized in the table on page 9 and sorted by investment objective categories and then in alphabetical order. Our individual stock recommendations are special situations offering a compelling value proposition. We are also recommending liquid electronically traded funds (ETFs) and mutual funds investing in sectors that are bound to benefit in the months and years ahead from fundamental changes in geopolitical, medical, and economic landscapes.

## A Downside Hedge

We employ a downside hedge as part of the portfolio because it dampens volatility, especially during adverse market conditions. The **ProShares UltraShort Russell 2000 (TWM)** short-sells the Russell 2000 index and is designed to produce two times the daily fluctuations of the Russell 2000 index. A decline of say, 1.0 percent in the Russell 2000 will cause TWM to increase by 2.0 percent. Conversely, an increase in the Russell 2000 will cause TWM to decline in the same fashion.

We are using this hedge because of the inherent weakness in the Russell 2000 stocks in comparison to the S&P 500 stocks. Many of the stocks in the Russell 2000 have negative earnings. During the first three quarters of 2021, the total earnings of the Russell 2000 stocks were actually negative. The total has since turned positive but is still low, which makes the overall trailing twelve-month (TTM) price/earnings (P/E) ratio very high, currently 52. This lofty P/E ratio makes the Russell 2000 index more vulnerable than the S&P 500, offering more downside profit potential.

Another reason the Russell 2000 is more vulnerable is because it is comprised of companies with small capitalizations. Small cap stocks have a higher risk/reward profile. They perform better during good times and worse during adverse conditions. Small caps are more heavily adversely impacted by rising labor costs and inflation.

**Historical Real Rates of Return**

Years	30 Yr Note (Avg. Yield)	CPI Annual Increase	Real Rate
1980 - 2000	8.6	4.3	4.3
2000-04	5.7	2.6	3.1
2005-09	4.5	2.6	1.9
2010-14	3.6	2.0	1.6
2015-18	2.9	1.9	0.9
2019-21	2.1	3.2	(1.1)
Average			<b>2.8</b>

**ETFs for Rising Bond Yields**

Until March of this year, the most significant force on the Treasury bond market was the Federal Reserve’s quantitative easing (QE) program. For two years, at the rate of \$80 billion per month, the Federal Reserve purchased more than one-half of all US Treasury securities issued. However, the Federal Reserve stopped buying bonds in March, ending the QE program. The largest buyer of Treasury bonds is now gone.

In September, the Federal Reserve officially entered and started a “quantitative tightening” (QT) program, to let Treasury securities mature without replacing them, up to a maximum amount of \$95 billion per month. This QT program is effectively the reversal of quantitative easing (QE), and is another mechanism the Fed has started to use to impede economic activity and quell inflation.

Until inflation is tamed, bond yields have nowhere to go but up. The three ETFs listed below are designed to benefit from rising long-term Treasury bond yields. They 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 daily changes in long-term Treasury 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 benchmark bond indexes will cause TMV to increase by 3.0 percent, TBT by 2.0 percent, and TBF by 1.0 percent.

These ETFs are in our portfolio because bond yields should continue escalating, especially with persistent inflation which is forcing the Federal Reserve to continue tightening its monetary policy.

The question is not whether bond yields will continue rising in the months ahead, but how much will they rise?

We can look back at history to find the answer. Bond investors have traditionally demanded a positive real return, which means over and above the inflation rate. The table above shows that since 1980, long-term Treasury bonds have yielded 2.8 percentage points above the inflation rate. Real yields were lower during the Federal Reserve’s four quantitative easing (QE) programs, which began in 2008, but QE programs are over now. (Before the QE programs, the average real return was 3.7 percentage points above the inflation rate.)

If we fast-forward through the volatility that most assuredly lies ahead during the Federal Reserve’s monetary and quantitative tightening, and assume that inflation simmers down to the Federal Reserve’s target of 2 percent, the yield on long-term treasury bonds should increase to the range of 4.8 percent to 5.7 percent. Of course, if inflation remains stubbornly higher, bond yields will be commensurately higher.

So far this year, TMV is up 145 percent, TBT is up 88 percent, and TBF is up 39 percent. Although these ETFs have risen with the rise in bond yields this year, there is still considerable upside. The table above shows the approximate upside potential of our selected ETFs at the end of 2023 at various levels of long-term Treasury bond yields. The first row shows today’s ETF prices at today’s long-term Treasury bond yields. Note that the approximate price of these ETFs would rise dramatically as Treasury bond yields rise. The erosion factors discussed below are included in each of these approximate projected ETF prices.

**ETF Upside Potential**

Date	20-Year Bond Yields	ETF Prices		
		TBF	TBT	TMV
9/30/2022	4.10	22.30	31.81	133.65
12/31/2023	4.00	21.20	28.58	112.82
12/31/2023	4.50	22.61	32.50	136.68
12/31/2023	5.00	23.92	36.12	158.77
12/31/2023	5.50	25.13	39.48	179.23
12/31/2023	6.00	26.25	42.59	198.20
12/31/2023	6.50	27.29	47.85	215.78

## The Erosion Factor

ETFs based on daily changes have an erosion factor because they decline slightly faster than they increase with an equivalent change in the underlying index. This factor becomes greater as the leverage of the ETF increases. To gauge this factor, we assume that Treasury bond yields simply tread water, rising and falling by a significant amount, say, 0.03 percentage points (3 basis points) every day, and thus go nowhere. By the end of 2023, TMV would decline by 8.1 percent, TBT by 5.0 percent, and TBF by 2.3 percent.

## Special Situations

These are stocks of individual companies that are presenting extraordinary values within their respective industries. Here they are in alphabetical order:

**Apple (AAPL)** announced in the week of September that it cancelled its iPhone 14 production boost after seeing flat demand. Of course, the stock price reflected disappointment.

AAPL was added to the portfolio in 2016 at \$29.08 per share (adjusted for the 4:1 split in 2020). We have been recommending holding off on adding to the position but continuing to hold AAPL. It is still too high. High price/earnings (P/E) ratios anticipate high growth rates which is a disaster waiting to happen. At the end of July, Apple reported its quarterly earnings of \$1.20 per share. When added to its last three quarters, the trailing twelve months (TTM) earnings declined slightly from the prior TTM. That lack of growth is disappointing for a stock with such a high P/E.

Our buying target is still \$125 per share. At that price, the TTM P/E would be close to 20, which is still higher than we like to bet on, but it is much more reasonable than the current ratio.

**Cisco Systems (CSCO)** is a direct beneficiary of the major new upgrade cycle into the fifth generation (5G), which is able to download data 100 times faster than the previous generation of 4G, because demand will be accelerating for faster equipment. Cisco also has a substantial and growing Cyber Security division. If there was ever an inexorable growth market, cyber security is it.

Cisco is transitioning from a network equipment seller into a contractual subscription and services company that generates recurring revenues from the equipment it sells, leading to a more reliable income stream. During the past five years, CSCO's annual recurring subscription revenues and services have more than doubled and now represent close to one-half of total revenues.

**Crown and Castle International (CCI)** is also benefiting from the bright future of 5G wireless technology because a higher density of large and small cell sites and related infrastructure is required. The company is seeing a strong leasing environment as customers deploy 5G with 5,000 small cell deployments expected by the end of the year to meet the growing demand and expects to double them next year.

The company has an unmatched portfolio of 40,000 towers, 115,000 small cells on air or under contract, and 85,000 route miles of fiber concentrated in the top US markets. Management believes its portfolio positions Crown and Castle to achieve its long-term annual dividend per share growth target of 7% to 8%.

CCI presents a relatively low risk way of investing in this high-tech area because of its ownership of hard assets comprised of cell towers, active small cell nodes on buildings, and 80,000 miles of fiber cable concentrated in the top US markets. These assets are difficult to create because of scarce locations in urban areas, zoning and governmental regulations, and sheer cost. As a result, there are high barriers to entry for competitors. Furthermore, income is secure, and growth is assured because these assets are leased to credit-worthy tenants with pre-determined escalating rent clauses.

The company emphasizes sharing its growth with its stockholders. The dividend has been increased every year since 2014 at an average rate of 9 percent. The 2021 dividend was increased by 11 percent.

**Intel (INTC)** is the only advanced semiconductor manufacturer, based in the US, building state of the art manufacturing plants for the western world. This puts Intel on a long-term growth path to become the nation's premier chip producer.

In August, the “Chips and Science Act” was passed. Aimed at boosting national security by bringing chip production to US shores, the \$52 billion package includes benefits for US companies producing computer chips. Benefits include tax credits to encourage investment in chip manufacturing and funding for the innovation and development of other US technologies.

Intel has the size, diversity, industry dominance, and financial health to make 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. The dividend is well-covered thanks to its strong cash flow. Earlier this year, the company announced a five percent addition to the quarterly payout, increasing it to \$0.365 per share.

**JP Morgan Chase (JPM)** has been suffering because the Treasury yield curve has been inverted, with short-term interest rates faster and higher than long-term rates. This tends to squeeze profit margins for banks because the increase in short-term rates raises costs on attracting deposits while income from long-term loans does not rise commensurately. Recessionary fears also raise the specter of declining loan demand.

According to Chairman and CEO Jamie Dimon. “JPM is well prepared to handle a recession. It’s not going to change how we run the company ... We invest, we grow, we expand, we manage through the storm.”

The company took a substantial charge against second quarter earnings to anticipate and cover adverse circumstances that may be ahead. JPM is down substantially since the first of the year. The dividend yield is now close to 4 percent, which makes a good value for the stock of what is considered the world’s highest quality banking enterprise.

**Moderna (MRNA)** is a pure investment play on Messenger RNA (mRNA) technology. This revolutionary approach is certain to provide solutions for not only vaccines, but cures and treatments for the most deadly and debilitating diseases haunting humanity.

In addition to Covid and seasonal respiratory vaccines, Moderna is developing vaccines for latent viruses, including Ebola and other more prevalent latent viruses. There are two ongoing HIV Phase 1 trials and a Phase 2 Zika vaccine trial. Other potential vaccines also in trials are for the Epstein-Barr virus (EBV) and for the Cytomegalovirus (CMV) which is the leading cause of birth defects in the US. News of approval would be very positive for MRNA because revenues would likely be in the range of \$2 to \$5 billion annually, and it would

be a bridge to new horizons from Moderna’s Covid-19 vaccines.

Moderna is also working on therapeutics using mRNA technology for oncology and cardio applications, along with treatments for autoimmune diseases. Collaborating with other companies on these fronts is a priority, as evidenced by recent joint ventures with Metagenomi and Carisma Therapeutics. Metagenomi and Moderna are collaborating to develop solutions against genetic diseases using gene-editing enzymes. Carisma Therapeutics and Moderna are collaborating to use Moderna’s mRNA technology to develop solutions against solid tumor cancers, which kill 80 percent of all cancer victims.

MRNA has crashed from \$495 per share in September 2021. Behind the deflation was the consensus that revenue from Moderna’s revolutionary and highly effective messenger mRNA Covid-19 vaccine, called Spikevax, would be declining in the years ahead. This expectation is already reflected in the current price of the stock, as evidenced by the absurdly low price/earnings (P/E) ratio. Even if the expected earnings drop were to occur, of say 50 percent to \$14 per share, the P/E ratio would still be 10 with MRNA at \$140. A P/E of 10 is still a very modest P/E. Therefore, the downside risk in MRNA is limited even under such a draconian scenario because it is already anticipated in the price of the stock. However, based on the first six months of earnings results, it is unlikely that such a draconian scenario will occur. Earnings were 49 percent higher for the first six months of 2022, to \$13.85 per share, compared to the same period in 2021.

Moderna’s Omicron COVID booster vaccine showed potent neutralizing responses against Omicron and variants BA.4 and BA.5, regardless of prior infection in people. The company began ramping up supplies of its next generation booster, ahead of a potential outbreak this fall. During the first half of 2022, the company signed Advanced Purchase Agreements for expected delivery of vaccines in 2022 for \$21 billion. This compares to last year’s revenue of \$17.6 billion.

The Board of Directors recently approved the new share buyback program for an additional \$3 billion, adding to the \$18 million purchased since the start of the share repurchase program in 2021. If a substantial earnings decline does not happen, MRNA is bound to recover profoundly. For example, even a modest P/E of 10 on last year’s earnings would push MRNA back up above \$280 per share, double the current price.

**Valero Energy (VLO)** is an oil refiner that makes its money from the “crack spread”, which is the profit margin derived from purchasing crude oil, turning it into refined products such as gasoline and jet fuel, and selling those refined products. Valero has the ability to achieve discounts for its crude oil feedstocks because it has the unique ability to refine substantial quantities of a variety of crude oil types, with access to the US pipeline network for delivery to its gulf coast locations. This flexibility and access allow Valero to capture the highest margins among its competitors because it can take advantage of the temporary gluts of crude, whether it's low or high-quality crude, or light sweet (low sulfur) or heavy sour (high sulfur) crude, and receive the best available discounts for its feedstocks.

Environmental policy-driven mandates have led to substantial closures of refining facilities in the US and Europe in recent years. Shell, for example, reduced its refineries from 54 to 8. Many other companies have responded to government incentives to convert large oil refineries to bio-fuel refineries which produce a comparatively small amount of energy-equivalent fuel. This has reduced overall refining capacity dramatically, leaving China as the world's largest refiner. Clearly, refining shortages are here for the foreseeable future.

Valero is diversifying from a pure oil refiner to a “green” company through its joint venture with Diamond Green Diesel, which is producing renewable diesel at large profit margins. Renewable diesel is made from animal or plant waste material which reduces greenhouse gas emissions up to 80 percent because it only releases as much carbon dioxide as the material originally contained. It does not gel at low temperatures which means it can be easily transported through pipelines.

Cash flow from diesel production turned positive in 2016 and is increasing. Renewable diesel volumes are expected to quadruple production capacity by 2023. Use for sustainable aviation fuel is expected to be a primary escalating demand factor. With diesel prices escalating along with other refined products, this has become a more significant growth aspect for VLO.

Management maintained the dividend throughout the pandemic and is expected to continue to do so, which provides an attractive yield.

### Other Medically Related Selections

**Boston Scientific (BSX)** is well-suited for an aging population. This company 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 in a wide range of critical areas, including cardiac rhythm and intervention, oncology, urology, and neuromodulation. The company's stream of new inventions acquisitions continues to add to promising growth prospects.

**Stryker (SYK)** is also well-suited for an aging population. This company has a diverse array of innovative medical technologies, including reconstructive, medical and surgical, as well as neuro-technological and spine products. Its orthopaedic devices for artificial knees and hips lead the industry. With 28 consecutive years of dividend growth, SYK has a very high return on equity which is propelled by organic sales growth and its strong balance sheet, giving the company the ability to continue to make strategic and synergistic acquisitions.

### The Best in Biotech ETFs

Biotech companies offer the most explosive profits because they are the source of the world's top breakthrough vaccines and treatments. Their stocks are often volatile, making diversification essential. This can be accomplished by investing in a diversified electronically traded fund (ETF) investing exclusively in a portfolio of biotech companies. We are recommending two top performers. All have pulled back substantially, offering timely buying opportunities.

**ARK Genomic Revolution Multi-Sector (ARKG)** is an actively managed biotech ETF investing in companies expected to benefit by incorporating technological and scientific developments and advancements stemming from mapping the human genome. Breakthroughs and advancements have cut the cost substantially of mapping the human genome which is opening new opportunities and putting this sector on the cutting edge of many new innovations.

**Virtus LifeSci Biotech Products (BBP)** is a passively managed biotech ETF that weighs the portfolio selections essentially equally, as opposed to the more typical practice of weighing selections according to market capitalization. This is an important aspect because biotech ETFs who weigh their portfolio selections essentially equally have been the best performers by far because they have larger investments in smaller biotechnology companies which are acquisition targets for large pharmaceutical companies looking for ways to revitalize their drug portfolios by scooping up smaller companies.

## Real Estate

Our three cumulative preferred stocks provide very attractive high yields and are inherently safe because any unpaid dividends must be retroactively restored first before any common dividends can be paid. In addition, these preferred stocks have a “liquidation preference” which must be paid out in full in the event of a liquidation of the company before any proceeds are paid to common stockholders. In all three cases, there is substantial equity in the respective common stocks, evidencing that the market does not expect liquidation to be plausible.

These preferred stocks are trading below the company’s call price (the right of the company to purchase the preferred at a certain “call” price), or have no call feature at all, which is very unusual for preferred stocks. These preferred stocks have a small number of outstanding shares, which is typical for preferred stocks in general. Accordingly, we recommend using limit orders rather than market orders.

**Hersha’s Preferred D (HTPRD)** was recommended when the stock price was under \$4.00 a share as the pandemic was gaining momentum in early 2020 and the company suspended all dividends to preserve liquidity. We believed that the eventual resumption and payment of preferred dividends would propel this stock back close to its call price and liquidation preference value of \$25. In April 2021, the company resumed the dividends on its preferred stocks and made up for unpaid preferred dividends of \$1.64 per share annually. In the second quarter, Hersha closed the sale of six non-core hotel properties outside of New York for \$436 million. Net proceeds were used for a significant net debt reduction of \$460 million, which is allowing Hersha to recast its existing credit facility and eliminate all corporate-level debt maturities through 2025.

Property level cash flow from its hotel portfolio more than doubled to \$46.4 million in the second quarter from the prior quarter and reached the results of the second quarter of 2019 prior to the Covid-19 pandemic.

The price of this preferred is still below its call price of \$25, offering an attractive discount.

**RLJ’s \$1.95 Series A Cumulative Convertible Preferred (RLJPRA)** is the only RLJ preferred stock and cannot be converted into common stock until the price of the common stock is significantly above \$100 per share.

This means that the preferred is essentially not callable without an astronomical rise in the price of the common stock (RLJ).

During the first half of this year, operating revenue from its hotel portfolio recovered beyond the pre-Covid level. The Board recently authorized a meaningful increase of the quarterly common stock dividend, demonstrating the ability to generate sustainable free cash flow. The company accretively recycled capital into common share repurchases, and acquired a high quality boutique lifestyle hotel in the high growth market of Nashville. The company also successfully exited its financial covenant waivers which required minimum financial performance measurements.

This is an opportunity to lock in a safe extraordinary current yield. It is hard to imagine that this yield will remain this high indefinitely, which means the price of this preferred stock will rise significantly.

**RPT Realty 7.25% Series D Cumulative Convertible Perpetual Preferred (RPTPRD)** is simply not callable by the company. This means that we can lock in a very high yield for as long as we desire. It pays an annual dividend of \$3.62. This is the only RPT preferred stock for RPT Realty. This is a convertible preferred stock, convertible into 3.796 shares of the common stock (RPT) at the holder’s option.

RPT Realty is a real estate investment trust (REIT) that owns 49 shopping centers across the eastern US, consisting of urban-infill neighborhoods, and power center properties with national chain store tenants, market-leading supermarket tenants, as well as a strong lineup of smaller national retailers.

In 2020, the company maintained the dividend on its preferred stock but suspended the dividend on its common stock. The dividend on the common stock was resumed for the first quarter of 2021 and increased in the fourth quarter. That means the preferred dividend is more secure because common dividends cannot be paid without paying the preferred dividend.

Funds from operations (FFO) have risen sharply this year as the Company added signed leases for 1.0 million square feet. The company has continued to upgrade its portfolio by acquiring in markets like Boston, Atlanta, Miami, and Tampa and selling in markets like Chicago and Detroit.

**Third Avenue Real Estate Value Investor Fund (TVRVX)** has an advantage over other mutual funds during recessions. Unlike the typical REIT, management will go to cash when asset prices are generally high. Cash is preserved for scooping up opportunities. It is a global real estate fund which means it is not confined to US real estate with low cap rates which translate to high valuations. 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.

Management 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 their personal assets into their funds.

### US Infrastructure

The bi-partisan infrastructure bill enacted in November 2021 will benefit both PSCI and RTM during the next 10 years.

**Invesco S&P SmallCap Industrials ETF (PSCI)** is based on the S&P SmallCap 600 Capped Industrials Index which is designed to measure the overall performance of the securities of US industrial companies with small capitalizations (caps). These domestic companies are engaged in the business of providing industrial products and services, including engineering, heavy machinery, construction, electrical equipment, aerospace and defense, as well as general manufacturing. They will reflect the positive impacts more strongly than larger companies from an increase in infrastructure spending. Small cap construction companies are also typically domestic companies operating inside the US. It is likely that a government-sponsored program will stipulate that US companies are to be employed to perform the services. Even absent such stipulations, construction projects tend to employ local companies as subcontractors even when general contractors are national companies.

The portfolio is more diversified than the typical peer in the category. Management has maintained an emphasis on stocks with low financial leverage and strong returns on equity. This ETF rebalances its investments quarterly

to maintain an equal weighting in its holdings. This strategy tends to improve and maintain diversification as well as deliver a stronger longer-term performance.

### Basic Materials

**Invesco S&P 500 Equal Weight Materials ETF (RTM)** invests in the common stocks that comprise the S&P 500 Equal Weight Materials Index. All 29 sections are prime examples of basic materials companies outside of the oil and gas industries. Basic materials companies are bound to benefit substantially in the years ahead with increased infrastructure spending.

This ETF rebalances holdings quarterly to equalize their values, which ensures a greater degree of evenly weighted diversification which adds stability and safety to a portfolio. This practice often provides a superior performance because it offers exposure to many stocks that are under-weighted in most other portfolios and are therefore targets for new capital.

### Consumer Staples

**Invesco S&P 500 Equal Weight Consumer Staples ETF (RHS)** is unique because it invests equal amounts in a collection of 33 consumer staple stocks within the S&P 500 index.

Consumer staples are those unexciting products we use every day without much thought, ranging from food, beverages (including alcohol), household goods (including cleaning supplies), hygiene products, and tobacco. These are products that people are unable (or unwilling) to remove from their budgets regardless of their financial situation. The nature of these products makes this sector defensive and much less vulnerable to recessions and bear markets.

RHS rebalances the investments at the beginning of each calendar quarter, which has given RHS a superior performance over other consumer staples funds because it has given investors exposure to many consumer staple stocks that are under-weighted in most other portfolios and targets for new capital.

## Portfolio Summary Table

This table is updated and live on our website:

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Income with Growth	Symbol	Price / NAV	Yield	Action	Limit
Hersha Hospitality Trust - Preferred D *	HTPRD	\$18.71	8.77%	BUY	\$25.00
RLJ Lodging Trust - Preferred A *	RLJPRA	\$24.58	7.93%	BUY	\$28.00
RPT Realty 7.25% Preferred D *	RPTPRD	\$43.82	8.27%	BUY	\$52.00
Growth with Moderate Income					
Cisco Systems	CSCO	\$40.00	3.70%	BUY	\$42.00
Crown and Castle	CCI	\$144.55	4.07%	BUY	\$151.78
Intel	INTC	\$25.77	5.39%	BUY	\$27.06
Invesco Consumer Staples ETF	RHS	\$153.69	2.97%	BUY	\$161.37
JP Morgan Chase	JPM	\$104.50	3.83%	BUY	\$109.73
Valero	VLO	\$106.85	3.67%	BUY	\$112.19
Growth					
Apple	AAPL	\$138.20	0.59%	HOLD	\$125.00
Boston Scientific	BSX	\$38.73	0.00%	BUY	\$40.67
Genomic Revolution Multi-Sector	ARKG	\$32.84	0.00%	BUY	\$34.48
Invesco Basic Materials ETF	RTM	\$142.58	1.91%	BUY	\$149.70
Invesco Small Cap Industrials ETF	PSCI	\$79.43	1.23%	BUY	\$83.40
Moderna	MRNA	\$118.25	0.00%	BUY	\$124.16
Stryker Corp	SYK	\$202.54	1.37%	BUY	\$212.67
Third Avenue Real Estate Value Investor *	TVRVX	\$18.95	0.00%	BUY	\$23.00
Virtus LifeSci Biotech Products	BBP	\$45.40	0.00%	BUY	\$47.67
ETFs for Rising Bond Yields					
Direxion Daily 20+Treasury Bear Shares 3X Leverage	TMV	\$133.65	0.00%	BUY	\$140.33
Proshares Short 20+Treasury - 2X Leverage	TBT	\$31.81	0.00%	BUY	\$33.40
Proshares Short 20+Treasury - No Leverage	TBF	\$22.30	0.00%	BUY	\$23.42
Hedges					
ProShares UltraShort Russell 2000	TWM	\$19.48	0.00%	BUY	\$20.45

**Notes to the table:** The right hand column is the highest recommended price limit for purchases.

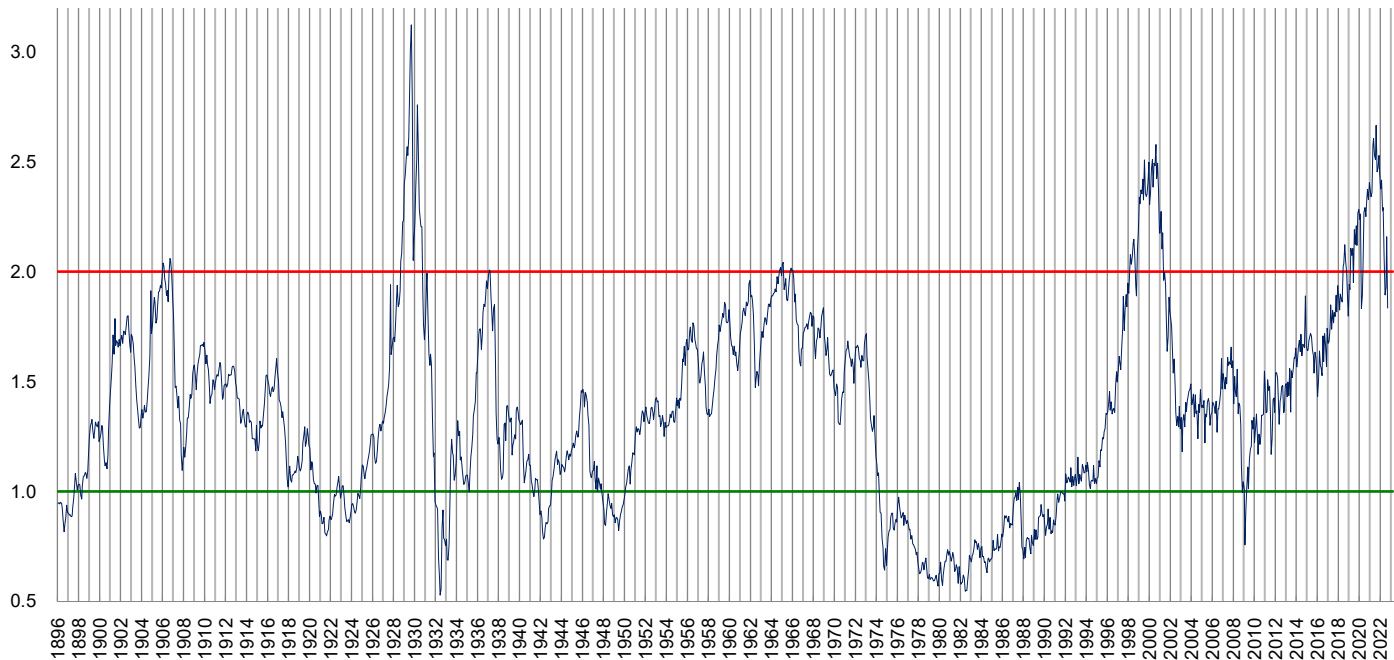
\* It is not possible to offer live pricing.

**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 SoundAdvice 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 120+ 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 based on the ratio of the S&P 500 Stock Index to median price of new houses 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 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.

But though an investment beginning with \$25,000 in 1895 could have made money being in either stocks or housing, had an investor followed the signals of the **Sound Advice** Risk Indicator, he or she would have made \$685 million versus \$24.5 million by simply holding stocks through the ups and downs, or 26.5 times more money.

A brief walk through history shows just how reliable this indicator is. The first recorded time the Risk Indicator rose above 2.0 was in February 1906, after the eight-year-old Dow-Jones average doubled since 1903. The market peaked in September of 1906. A massive sell-off in October would later be labeled the Panic of 1907. Stock prices trended downward for 14 more years until the end of 1921 while, searing inflation after World War I boosted house prices 48 percent. The combination of falling stock prices and rising real estate prices forced the Risk Indicator to fall below 1.0 in 1920, just in time for the Roaring 20's when stock prices tripled. Then, in October 1928, the Risk Indicator rose above 2.0 again. On Tuesday, September 3, 1929, the Dow

**The New York Times**

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

peaked at 318.17. The October crash marked the beginning of a decline that lasted until July 8, 1932. Houses had declined only by 15 percent compared with the 85 percent loss in stocks. The relative superior performance of houses caused our Risk Indicator to fall below 1.0 at the beginning of 1932.

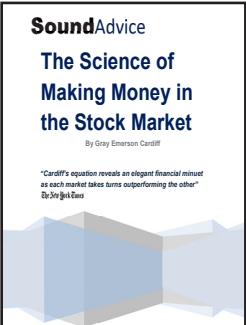
As America's GNP began posting positive gains and with 46 percent growth in three short years, stock prices would triple. Then the Risk Indicator crossed 2.0 in March 1937. This time, the signal came only one month after the zenith in stock prices. As stock prices retreated 50 percent, house prices remained relatively steady, causing the Risk Indicator to fall below 1.0 again in June 1941, within 9 months from the bottom.

As U.S. corporations expanded to meet growing demand, and the economy came to a rolling boil during the Eisenhower years, the stately rise would multiply stock prices by ten times until November 1964, when the Risk Indicator crossed over 2.0 again. The stock market would continue to climb into 1968, and then crashed into late 1974, wiping out the inflation-adjusted gains scored by investors since 1954.

However, a switch to an investment in houses would avoid all that and double in price by the time the next signal came for stocks in May 1974, as the Risk Indicator fell below 1.0 again, as the Dow careened below 700.

It would not be until March 1998 when the Risk Indicator would cross 2.0 again, after stocks were up by more than tenfold. The Dot-Com bubble would push stocks higher into early 2000, but then began another 50 percent retracement. A switch to houses would produce a 44 percent gain through the end of 2008 while stock prices were lower by 17 percent. In February 2009, with the Dow careening below 700 once again, the Risk Indicator quietly dropped below 1.0 to 0.77 as the S&P tumbled under 700. Since then, the stock market has delivered stunning gains as the S&P 500 has quadrupled. For the sixth time in the last 125 years, the Risk Indicator rose above 2.0 again in July 2018.

**With the latest median house price at 466,300 in July 2022 (the latest data) and with the S&P 500 averaging 3850 in September, the Sound Advice Risk Indicator read 1.83.**



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## Business Cycles and Stocks: The SoundAdvice 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. 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 five-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 five 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 December 2008, 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.

## Track Record of the SoundAdvice Diffusion Indexes

Drumming the last 47+years, after each “Aggressive” signal, the S&P 500 climbed an average of 31.5 percent. During “Caution” signals, the S&P 500 either crashed, meandered, or climbed, recording an average decrease of 0.9 percent.

Aggressive	S&P 500	Caution	S&P 500
Sep-74	68.12	Apr-76	101.9
Jul-76	104.20	Dec-76	104.7
Oct-78	100.58	Jun-79	101.7
Nov-79	100.00	Oct-83	167.7
Aug-84	164.48	Jun-85	188.9
Jul-86	240.18	Aug-87	329.4
Feb-88	258.13	Jun-88	270.7
Mar-89	280.00	Mar-93	449.7
Mar-95	493.15	Dec-98	1,141.0
Jun-00	1,429.40	Dec-00	1,320.3
Jun-03	974.50	May-05	1,191.5
Jun-06	1,276.66	Mar-08	1,325.4
Dec-08 (1)	865.58	Apr 10 (2)	1,197.3
Sep 10 (3)	1,122.08	Jun 12 (4)	1,359.8
Sep-12 (5)	1,437.82	Nov 14 (6)	2,044.6
Mar-15	2,079.99	May-15	2,111.9
Sep-17	2,492.84	Feb-18	2,705.2
Mar-20 (7)	2,761.98	Nov 21 (8)	4,667.4
Ave +/-	31.5%		-0.9%

### Quantitative Easing (QE) Overriding Signals

- (1) QE-1 announced 4 months before Aggressive signal
- (2) QE-1 terminated into existing Caution signal
- (3) QE-2 announced but already in Aggressive mode
- (4) QE-2 terminated into existing Caution signal
- (5) QE-3 announced, changed to Aggressive mode
- (6) QE-3 terminated into existing Caution signal
- (7) QE-4 announced, changed to Aggressive mode
- (8) QE-4 terminated into existing Caution signal

### A Powerful Overriding Force

Most of the time, the Diffusion Indexes are excellent detectors of the natural business cycle and a path to the science of making money in the stock market. However, the forces of the natural business cycle can be dominated by extraordinary changes in monetary policy during emergency situations.

The COVID-19 pandemic was the most recent example. In mid-March 2020, the Federal Reserve declared the institution of its fourth “Quantitative Easing” (QE) program whereby it dropped the Federal Funds rate to zero and commenced buying massive amounts of US Treasury bonds. With its mighty power, the Fed drove down interest rates and infused massive amounts of liquidity into the US economy. The money supply mushroomed.

At times like this, we need to ignore readings from the Diffusion Indexes. Interest rates are dropping by the Federal Reserve’s mandate, just as if the Diffusion Index of Leading Indicators had plunged to zero. Conversely, whenever the Federal Reserve declares an end to its QE program, we return to our Diffusion Indexes to follow their readings. If the Diffusion Index has moved to a “Caution” signal during the QE program, we should follow that reading. This is the most likely pattern of events because the economy will likely have strengthened in order for the Federal Reserve to end its QE program.

The impact of the Federal Reserve’s four QE programs on existing Diffusion Index signals are noted in the footnotes under the track record table.

### Current Status

In November 2021, the Federal reserve announced the end of its latest QE program. Accordingly, the “Caution” signal became effective from the Diffusion Index of LAGGING Indicators.

The latest reading was zero for the Diffusion Index of LEADING Indicators but was offset by a 100 percent reading from the Diffusion Index of LAGGING Indicators..

Our next “Aggressive” signal will come when the Diffusion Index of LEADING Indicators drops to zero as long as it is not offset by a 100 percent reading from the Diffusion Index of LAGGING Indicators.

## Sound Advice versus the S&P 500

