

SoundAdvice

Advising Investors for 35+ years

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The New Normal

History tells us that the level of interest rates is a driving force on the stock market. If we are to be successful investors, we must determine the prospects for interest rates. In the words of American philosopher George Santayana, "Those who do not remember the past are condemned to repeat it."

The inverse relationship between interest rates and stock prices is historically visible, and the power of the impact is logical for three primary reasons:

One, bonds are an alternative to stocks. In fact, the bond market is larger than the stock market. Stock yields and growth prospects must compete with the certainty of bond yields.

Two, interest rates have an impact on corporate cash flow. Interest expenses on corporate debt are substantial for most companies. Depending on the relative amount of debt, changes in interest rates impact cash flow and can even threaten the vitality of debt-laden companies.

Three, future earnings and dividend growth are evaluated by discounting future projected earnings and dividends to a present value. The level of interest rates determines the annual discount rate. The higher the discount rate, the lower today's present value will be. This is especially pronounced for stocks with small or no dividends trading at high price/earnings (P/E) ratios, such as the handful of tech stocks discussed later that are bloating the S&P 500 Index.

Accordingly, the critical question we now face is "What is the new normal interest rate?"

The Old Normal

We are likely near the peak of short-term interest rates because the economy is bound to be softening in the months ahead. Our reliable **Sound Advice Diffusion Indexes** reveal that eventuality (see below). We also know that the Federal Reserve's mandate is to keep inflation stable at 2 percent, and the Fed will use its mighty tools to achieve that goal, including slowing down the economy. It is only a matter of time.

Bond investors traditionally demand a positive real return, which means a yield over and above the inflation rate. Since 1980, long-term Treasury bonds have yielded 2.7 percentage points above the inflation rate. (See the nearby table – Historical Real Rates of Return.)

Historical Real Rates of Return

Years	(Avg. Yield)	Increase	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
Average Prior to QE programs			3.7
2010-14	3.6	2.0	1.6
2015-18	2.9	1.9	0.9
2019-22	2.4	4.1	(1.8)
Average Including QE programs			2.7



Gray Emerson Cardiff,
Editor Since 1988

For 2022, the *Sound Advice* model portfolio gained 4.02% versus a loss of 19.44% from the S&P 500.

Since 1999 through 2022, the *Sound Advice* model portfolio more than doubled the return of the S&P 500.

If we assume that inflation simmers down to the Federal Reserve's target of 2 percent, history tells us that the yield on long-term treasury bonds will stabilize in the vicinity of 4.7, which is close to where they are now, and become the new normal for the foreseeable future.

As the economy slows down under the pressure of the Federal Reserve's resolve to quell inflation, the yield curve is bound to return to its normal shape as short-term interest rates fall below long-term interest rates. Treasury bills will yield considerably less than long-term Treasury bonds, which is normally the case when the Federal Reserve is not tightening monetary policy.

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A Higher Normal?

The 2008-09 financial crisis changed the economic landscape for more than a decade. To combat systemic economic weakness, the Federal Reserve's four consecutive quantitative easing (QE) programs were used to stimulate the economy. The QE programs instituted buying massive amounts of Treasury bonds, pushing yields to historically low levels. As a result, real Treasury bond yields were artificially low during those QE programs from 2008 to 2022. Prior to the QE programs, the average real return on long-term Treasury bonds averaged 3.7 percentage points above the inflation rate. (See the table – Historical Real Rates of Return.)

If that real return represents the unfettered historical norm, the implication is that the new normal would be in the vicinity of 5.7 percent at a 2 percent inflation rate. That is close to one full percentage point (100 basis points) above current long-term Treasury bond yields.

Conclusion

The normalization of long-term interest rates means that they will stay where they are, or potentially rise from current levels, and stay there for the foreseeable future. This is not a buoyant force on stock prices.

Bonds will remain more attractive than they were during the prior 10+ years, adding competition for stocks.

Most companies locked in lower long-term interest rates on their debt during the QE programs. Corporate debt also expanded substantially during those years. As corporate debt matures, it will need to be refinanced at higher interest rates. Typically, corporate interest expenses will be rising, impacting earnings.

Additionally, discount rates are now higher, reducing the present value of earnings and dividend income from stocks.

We must be careful and selective with our investment choices. We should avoid companies with high debt loads, especially if a significant amount has floating interest rates or much of it matures soon for refinancing. We should also avoid stocks with high P/E ratios and little or no dividend yield.

The Sound Advice Diffusion Indexes

Our **Sound Advice Diffusion Indexes** (page 10) have had a trustworthy track record over the last 47 years. All market crashes have occurred during "Caution" signals. When the stock market was not crashing, the S&P 500 either meandered, climbed moderately, or declined in an extended bear market, recording an average decline of 0.6 percent. Conversely, during "Aggressive" signals, the S&P 500 climbed an average of 31.5 percent, and the market never crashed. These have been times of declining or low interest rates, along with declining or low inflation.

At the beginning of 2022, our **Sound Advice Diffusion Index of Lagging Indicators** was in "Caution" mode. Once again, this warning proved prophetic. The S&P 500 Index ended the year down 19.4 percent. As a result of heeding our caution signal and positioning our holdings accordingly, the *Sound Advice* portfolio gained 4.02 percent in 2022. In addition to telling us the general direction of stocks ahead, the "Caution" signal told us where to invest, such as areas that would benefit from rising inflation and interest rates while hedging for downside profits.

As we began 2023, we had a completely different situation. Our **Sound Advice Diffusion Index of Leading Indicators** dropped to zero in December 2022. This signal revealed that the economy was going to be softening in the months ahead which also meant the end of the Federal Reserve's interest rate hikes was on the horizon. Our investment mode changed from "Caution" to "Aggressive".

Our trustworthy **Sound Advice Diffusion Indexes** told us we were at the beginning of a bull market. In hindsight, we see that the December 2022 signal has also proved prophetic.

The Sound Advice Model Portfolio

We eat our own cooking at *Sound Advice*. The editor and affiliates are investors in the **Sound Advice Diversified Growth Fund**, which invests exclusively in all of the *Sound Advice* Model Portfolio recommendations. The editor is the manager and is also an investor in this Fund, on a side-by-side basis with other investors. You can request a prospectus on the log-in page you used to download this issue of *Sound Advice*.

Our individual stock recommendations are special situations offering a compelling value proposition. We are also recommending liquid electronically traded funds (ETFs) investing in sectors that are bound to benefit in the months and years ahead. All of the recommendations, as well as their dividend yields, and buy/hold/sell recommendations, are summarized in the table on page 8 and sorted by investment objective categories and then in alphabetical order.

An Equally Weighted S&P 500 ETF

Invesco S&P 500 Equal Weight ETF (ticker symbol RSP) invests in all of the S&P 500 stocks but on an equally-weighted basis. RSP rebalances its portfolio each quarter to maintain its equal weights. This rebalancing process preserves value by reducing stocks that have recently outperformed while adding recent laggards. Our trustworthy **Sound Advice Diffusion Indexes** are telling us we are in a bull market, which means investing in the S&P 500 stocks is a good idea, but this is a much better alternative to the S&P 500 Index.

The S&P 500 Index is comprised of 504 stocks of reputable companies, but each of the 504 stocks is not weighted equally. Each holding is weighted according to its capitalization (the number of shares outstanding multiplied by the price of the stock). The implication is that it is a diversified balanced index, but it is not.

The unequal weighting has caused 9 stocks to dominate the S&P 500 Index and comprise 29 percent of the Index, as opposed to 1.8 percent if they were equally weighted.

These 9 stocks are Apple, Microsoft, Amazon, Nvidia, Alphabet Class A (Google Class A), Alphabet Class C (Google Class C), Tesla, Meta Platforms Class A, and Berkshire Hathaway Class B. The average trailing-12-month (TTM) price/earnings (P/E) ratio for these 9 stocks is close to 100, which is very high by historical standards.

The additional weighting of these 9 stocks has boosted the S&P 500 Index by 30 percent more than if each stock were evenly weighted. **In fact, removing these 9 stocks reveals that the balance of the S&P 500 Index is actually down 5.0 percent for the year.**

Bloated by these 9 stocks, the TTM P/E ratio for the S&P 500 Index is now 23.4. In contrast, the P/E ratio of RSP's evenly-weighted portfolio of the S&P 500 stocks is currently close to 17, which makes RSP a far better value.

A Downside Hedge

We include a downside hedge as part of the portfolio because it reduces risk and dampens volatility, especially during adverse market conditions. Based on the reasoning discussed above, we are using the **ProShares UltraShort S&P 500 (SDS)** as our downside hedge, which is designed to produce two times the daily fluctuations of the S&P 500 Index. A decline of say, 1.0 percent in the Index will cause SDS to increase by 2.0 percent. Conversely, an increase in the Index will cause SDS to decline in the same fashion.

Since the beginning of the last bull market in 2009, the TTM P/E ratio of the (weighted) S&P Index has averaged 21.5. One standard deviation from the average is 5.0 percentage points, which means this P/E ratio has been within plus or minus this amount 68 percent of the time, for a range of 26.5 to 16.5. The current P/E ratio is near the high end of the range, which, means this Index currently has hidden risks with limited upside.

Another sign that the weighted S&P 500 Index is inflated is revealed from our **Sound Advice Risk Indicator** (page 8), which compares the weighted S&P 500 Index to house prices for more than 125 years. The latest reading for July was 2.22 which puts the weighted S&P 500 Index significantly above the high-risk watermark of 2.0.

Special Situations

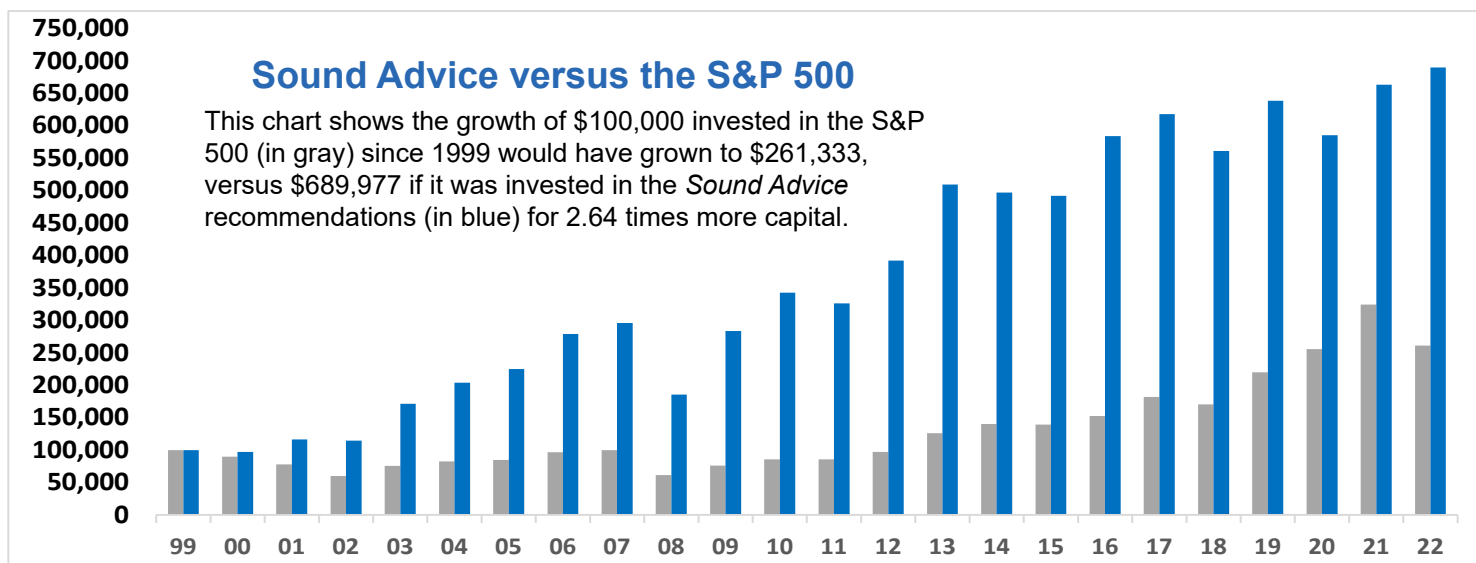
The following stocks are individual companies presenting extraordinary values within their respective industries. Here they are in alphabetical order:

Apple (AAPL) was added to the portfolio in 2016 at \$29.08 per share (adjusted for the 4:1 split in 2020). When the price/earnings ratio (P/E) expanded, we recommended holding but not buying AAPL because its high (P/E) ratio was anticipating an unrealistically high growth rate.

Revenue has been declining for three quarters in a row, especially for iPads and Macs. Smart phone shipments have been soft. Geopolitical risks are growing as exemplified by China's ban on iPhones for its government employees. China is a large market for Apple. It also has vital production facilities there, which it is working on moving to friendlier shores.

We recommend investing under \$135 per share. This price target puts the TTM P/E at 23 which is on the high side for

The Sound Advice Model Portfolio



most stocks but a reasonable value for AAPL's long-term prospects.

Cisco Systems (CSCO) announced in September it agreed to buy the cybersecurity company Splunk for \$28 billion. Named after "spelunking", the hobby of exploring caves and mines, splunking in the computer world is the exploration of information caves and the mining of data.

Splunk's primary business is the backbone security system in data centers, providing customers with artificial intelligence (AI) and other tools to analyze their data and detect security threats. The acquisition is a good strategic fit because it will give Cisco a much-needed bolster to its cloud security offerings. Cisco management said the purchase will immediately boost cash flow in its cyber security division in the first year after closing, which is expected by the end of September 2024.

CISCO is a direct beneficiary of the major upgrade cycle into the fifth generation (5G), which can download data 100 times faster than the previous generation of 4G. Operating in 5G requires upgrading to faster equipment. The rollout of 5G is bound to boost growth for several years.

Crown and Castle International (CCI) has an extensive portfolio of communication infrastructure assets comprised of 40,000 cell towers, 115,000 small cells, and 85,000 route miles of fiber 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. 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 and the industry experienced several headwinds this year including rising interest rates which have added to expenses. The amount of its floating rate debt exposure has been reduced from 32 percent to 9 percent, along with a reduction in secured debt which will allow greater access to that market if it becomes attractive in the future. Only 7 percent of debt matures through 2024. The company has also reduced operating expenses to offset increased interest expenses.

Another headwind was the consolidation of Sprint and T-Mobile which reduced demand. However, the consolidation was not materially impactful and the adjustment has been absorbed.

These headwinds have battered CCI down to a very attractive price with an exceptionally high dividend which is covered by the company's cash flow, even under drastic scenarios of rising interest expenses. Management believes CCI is positioned to return to the company's long-term annual dividend per share growth target of 7% to 8% beyond 2025.

JP Morgan Chase (JPM) is a good value for what is considered to be the world's highest quality banking enterprise with diversified businesses and prudent underwriting policies. JPM became an even better value when it acquired most of the assets of the failed First Republic Bank. JPM has been taking substantial quarterly charges against earnings to anticipate and cover adverse circumstances that may lie ahead. The annual dividend is \$4.00 for an attractive yield.

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

Moderna has 48 programs in development, including 36 in ongoing clinical trials, with a recently-increased R&D budget of \$4.5 billion. Moderna's strong balance sheet with essentially no debt should sustain the transition to new revolutionary vaccines and treatments, which offer tremendous upside potential.

On September 13, Moderna had its R&D investor presentation in New York. CEO Shephane Bancel introduced the meeting with the basic premise that Moderna was founded to develop a platform using nature's information molecule, mRNA, to treat and prevent many diseases. He noted that regular pharma has a 90 percent failure rate because it employs an analog way to make drugs, not an information-based process like the mRNA approach. He noted that Moderna has a 100 percent success rate with three out of three vaccines. He also noted that Moderna uses the same mRNA platform to code different instructions for many specific treatments. This speed and efficacy lowers costs and substantially increases prospects for success.

In a subsequent Blumberg interview, Bancel said revenue from Covid vaccines is projected to be \$6 to \$8 billion this year based on lower post-pandemic needs, which will sustain the business while it develops other vaccines and treatments. He noted that Covid will look like Flu over time. Moderna is currently conducting trials for a Flu vaccine and plans to offer a combined Covid and Flu vaccine by 2025.

Moderna's first vaccine beyond Covid will be for the Respiratory Syncytial Virus (RSV), a highly contagious seasonal respiratory virus and a leading cause of lower respiratory tract infections and pneumonia. Positive test results have allowed the company to file several regulatory submissions for patients of 60 years and older, and more are scheduled in coming months. The company has begun manufacturing supplies for the 2024 commercial launch. Applications have been submitted in major markets around the world. This multibillion-dollar market is bound to be a significant growth catalyst for MRNA. By 2028, the company plans to have a single Covid, Flu, RSV vaccine.

Another significant development in the works is a new vaccine for the Cytomegalovirus (CMV) which is the leading cause of birth defects in the US. The Phase 3 trial on women of childbearing age has enrolled 80 percent with full

enrollment expected soon. Potential revenues would be in the range of \$2 to \$5 billion annually.

Results have been promising from Moderna's personalized cancer vaccine used in combination with Merck's monoclonal antibody Keytruda. This personalized cancer vaccine uses cells from the patient's tumor and subjects them to RNA sequencing. The cancer vaccine is designed to prime the immune system so that a tailored anti-tumor response is generated that is specific to a tumor's mutation signature. The result of a phase 2 study was announced in June that a personalized cancer vaccine reduced the risk of cancer metastasis or death in melanoma by 65 percent on 157 patients with high-risk stage III/IV melanoma. The phase-3 study is now enrolling. Moderna is scaling manufacturing capacity to be ready for commercialization.

In his Blumberg interview, Bancel was excited about new developments regarding the ability to see fragments of cancer cells in a blood draw, allowing the detection of cancer in early stages, before it graduates into more serious later stages. Data will be transmitted through the cloud to Moderna's IT system, and Moderna will use AI algorithms to analyze and compare an individual's particular cancer cell mutation to the hundreds of thousands of possibilities and to the treatments that are currently effective. Bancel said Moderna will be able to analyze and develop a treatment customized for an individual patient within 30 days. Over time with more and more data, the process will become more efficient and accurate.

RLJ Lodging Trust (RLJ) was introduced in our August 8 mid-issue email update, along with **Hersha Hospitality Trust (HT)**. We noted that we have been following and analyzing two real estate investment trusts (REITs) for many years. We already had their preferred stocks in our Model Portfolio, paying 8+ percent income. Both companies have diversified portfolios of premium hotel and resort properties.

At the time of our August mid-issue update, the common stocks of these REITs were presenting compelling values. An announcement was made in the final days of August to purchase **Hersha Hospitality Trust** at a large premium over the price of the common stock. If you acted on our advice, you would have reaped a 50+ percent profit. Based on the experience with Hersha, it is clear that RLJ is a likely acquisition target at a stock price considerably higher than it is now.

How do we know this? Because we can put a pencil to REITs because their primary asset is a portfolio of real estate properties.

We can establish a value on a real estate portfolio by using a capitalization rate (cap rate). In real estate parlance, a cap rate is the percentage yield of the net operating income divided by the value of the portfolio. This is just like the yield of a bond whereby the coupon income from the bond is divided by the market value of the bond. For example, if a portfolio provides \$100,000 of net operating income (NOI), and the portfolio is worth, say \$2 million, it will have a cap rate (yield) of 5 percent.

In this example, if we did not know the value of the portfolio but we knew the NOI is \$100,000, we use a reasonable cap rate to determine the portfolio value. We can calculate the value of the portfolio by dividing the NOI by a cap rate. Using a cap rate of, say 5 percent, we divide a \$100,000 NOI by 0.05 and arrive at a value of \$2 million.

We can apply this principle to evaluating the portfolios of REITs. With an individual REIT, we can obtain the NOI of its portfolio in the 10Q and 10K financial statements the company files with the Securities and Exchange Commission (SEC). We can then assume a conservative cap rate and derive the value of the portfolio. After adding other assets, subtracting liabilities and the liquidation value of any preferred stock, we arrive at the equity, or net asset value, available to common shareholders. Dividing that equity by the number of shares outstanding gives us a net asset value per share of stock.

We can arrive at a reasonable cap rate by looking at recent comparable property sales. Hersha sold off non-core hotel real estate assets in recent years. Property sales occurred at a weighted average cap rate of 6.0 percent from 2016 through 2018. Because cap rates generally follow the trends of long-term interest rates, cap rates increased into 2022 along with the increase in long-term interest rates. In mid-2022, Hersha sold \$505 million of non-core properties at a 7.3 percent cap rate. That cap rate was based on the 2019 pre-pandemic NOI of the properties which, although higher than the current NOI, reflected the stabilized income potential of those properties. Because these sales were not the best assets in the portfolio, a lower cap rate would be a reasonable cap rate for high-end hotel properties. However, to be reasonably conservative, we can use a higher cap rate of 7.5 percent based on the current NOI of the properties.

On Monday, August 28, KSL Capital Partners announced a consummated agreement to purchase Hersha Hospitality Trust for \$10 per share of HT, which was a 59.2 percent premium to the latest closing price. We can see why KSL is willing to pay \$10 per share because KSL is effectively paying a 9.3 percent cap rate for Hersha's real estate portfolio. That is a bargain price to pay for a high-quality real estate portfolio.

RLJ Lodging Trust (RLJ) has a larger and more diversified portfolio of hotel properties than Hersha's. RLJ has 97 premium-branded, high-margin, focused-service and compact full-service hotels located in 23 states and Washington DC. This company also suffered during the pandemic. As it began to recover, we recommended the company's only preferred stock, which is still in the *Sound Advice* Model Portfolio (see below). Since the pandemic, the company's operating revenue has recovered beyond the pre-Covid level. This is a low-leveraged REIT because the company's debt is only 41 percent of its assets.

The portfolio's NOI for the trailing four quarters totaled \$398 million. Using a 7.5 percent cap rate produces a portfolio value of \$5.3 billion. Adding other assets and subtracting liabilities leaves the company equity of \$3.6 billion. After subtracting the liquidation value of the company's only preferred stock of \$322 million leaves equity for the common shareholders of \$3.23 billion. Dividing that equity by the 156 million shares of RLJ outstanding translates to a net asset value of \$20.68 per share. With RLJ at \$9.79 per share, near its multi-year low, the net asset value represents a 111 percent premium.

Even using a 9.3 percent cap rate to evaluate the real estate portfolio, which is the effective bargain cap rate KSL paid for Hersha's portfolio, translates to a net asset value of \$14.11 per share. Acquiring this portfolio at a price based on a 9.3 percent cap rate would be incredibly cheap, but it would still be a 44 percent premium over the current price of RLJ.

Although RLJ is an attractive acquisition target at a stock price considerably higher than it is now, even without an acquisition, the stock price has considerable upside potential as the market recognizes the discount to net asset value.

The \$0.40 annual dividend (4 percent) has been increased three times since last summer and is still well-covered by the company's cash flow.

RLJ's \$1.95 Series A Cumulative Convertible Preferred (RLJPRA) is RLJ's only preferred stock. This preferred stock has a liquidation preference of \$25.00 per share, and the stock is currently trading below that price.

Preferred stocks can and do often trade above their liquidation values, but an acquisition of the company would likely result in receiving the liquidation preference price. Accordingly, we recommend confining purchases below \$25 per share.

The dividends for this preferred only consumed 11.1 percent of the company's cash income in 2022, making the 8+ percent income yield secure. This is an opportunity to lock in a safe and extraordinary current yield with some upside profit potential to \$25 per share.

Valero Energy (VLO) 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 unique ability to achieve discounts for its crude oil feedstocks because it can refine a variety of crude oil types. 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. The company's refineries also have access to the US pipeline network from its gulf coast locations.

Environmental policy-driven mandates have led to substantial closures of refining facilities in the US and Europe in recent years. This has reduced overall refining capacity dramatically, leaving shortages for the foreseeable future. Instead of reducing oil refining capacity, Valero is diversifying 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. Renewable diesel does not congeal at low temperatures which means it can be easily transported through pipelines. Cash flow from diesel production turned positive in 2016 and is increasing. Use for Sustainable Aviation Fuel (SAF) is expected to be a primary escalating demand factor. Valero's Port Arthur plant is being upgraded to produce close to 50 percent of the plant's current renewable diesel production capacity to SAF. After completion in 2025, this plant is expected to be one of the world's largest SAF manufacturers.

Sector ETFs

Included in the *Sound Advice* model portfolio are the following electronically traded funds (ETFs) investing in sectors that are bound to benefit in the months and years ahead from fundamental changes in geopolitical, medical, and economic landscapes. These ETFs contain a portfolio of stocks, much like a mutual fund but ETFs are liquid and trade like stocks with their own ticker symbols. Their prices are determined by the value of the portfolio of stocks they hold.

Artificial Intelligence

Global Robotics and Automation Index ETF (ROBO) is investing across the entire spectrum of robotics and automation. Close to 60 percent of the portfolio is in robotics technologies, and 40% is in the technology controlling the robots – sensing, computing actuation, artificial intelligence (AI), and integration. ChatGPT, the open, generative AI chatbot, is giving us a glimpse into the next technology frontier. Artificial intelligence will play an increasingly greater role in the way companies operate around the world.

Since its inception in 2013, ROBO has essentially matched the return of the S&P 500 Index which is commendable considering the rise of the S&P 500 Index and the infancy of AI and robotics over that period. Based on the growth prospects of its holdings, this ETF is bound to out-perform the S&P 500 in the long run.

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.

ARK Genomic Revolution Multi-Sector (ARKG) is an actively managed biotech ETF investing in companies expected to benefit by incorporating technological and scientific developments, along with advancements stemming from mapping the human genome. Technological breakthroughs in artificial intelligence and other high-tech advancements have cut the cost substantially of 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 because they have larger investments in smaller biotechnology companies which have become acquisition targets for large pharmaceutical companies looking for ways to expand.

Balanced Sector ETFs

The following ETFs rebalance their holdings quarterly to equalize the values, which offers a greater degree of evenly weighted diversification and adds stability as well as safety to a portfolio. This practice often provides a superior performance because it offers upside from stocks that are often under-weighted in the portfolios of other ETFs and mutual funds.

Health Care

Health care stocks have several traits that make them desirable long-term investments. They are well-suited for an aging population, which exerts disproportionate demands on the industry. As the world's population continues to age, this trend is inexorable, making the health care sector defensive in nature and more insulated from economic cycles than other sectors.

One of the main criticisms of most health care ETFs is that they are dominated by a relatively small number of large companies, such as Johnson & Johnson, which distort the performance of the typical health care ETF portfolio.

Invesco's S&P 500 Equal Weight Health Care ETF (RSPH, formerly RYH) tracks the S&P 500 Equal Weight Health Care Index, which tracks 65 health care stocks represented in the S&P 500, but weights each holding evenly. Both the Index and RSPH are rebalanced quarterly. This approach has given RSPH a better performance than the large health care ETFs. This ETF had a 10-to-1 split in mid-July, which increased the number of shares by 10 times the amount you previously held, and the price was adjusted to one-tenth of the previous share price.

Consumer Staples

Invesco S&P 500 Equal Weight Consumer Staples ETF (RSPS, formerly RHS) invests 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), and hygiene products. 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. This ETF had a 5-to-1 split in mid-July, which increased the number of shares by 5 times the amount you previously held, and the price was adjusted to one-fifth of the previous share price.

US Infrastructure

The Infrastructure Investment and Jobs Act, enacted in November 2021, targeted \$1.2 trillion to fund improvements, repairs, and upgrades for a wide range of infrastructure needs, from bridges and highways to water and electric grid systems. This infrastructure spending will benefit both of the following two ETFs in the years ahead.

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, and construction projects tend to employ local companies as subcontractors even when general contractors may be national companies.

Invesco S&P 500 Equal Weight Materials ETF (RSPM, formerly RTM) invests in the companies that comprise the S&P 500 Equal Weight Materials Index. The portfolio contains 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 had a 5-to-1 split in mid-July, which increased the number of shares by 5 times the amount you previously held, and the price was adjusted to one-fifth of the previous share price.

Portfolio Summary Table

Income with Growth	Symbol	Price	Yield	Action	Limit *
RLJ Lodging Trust - Preferred A	RLJPRA	\$24.05	8.11%	BUY	\$25.00
Growth with Moderate Income	Symbol	Price	Yield	Action	Limit *
Cisco Systems	CSCO	\$53.76	2.90%	BUY	\$56.45
Crown and Castle	CCI	\$92.03	6.80%	BUY	\$96.63
Invesco Consumer Staples ETF	RSPS	\$30.04	0.53%	BUY	\$31.54
JP Morgan Chase	JPM	\$145.02	2.76%	BUY	\$152.27
RLJ Lodging	RLJ	\$9.79	4.09%	BUY	\$10.75
Valero	VLO	\$141.71	2.88%	BUY	\$148.80
Growth	Symbol	Price	Yield	Action	Limit *
Apple	AAPL	\$171.21	0.56%	HOLD	\$135.00
Genomic Revolution Multi-Sector	ARKG	\$27.86	0.00%	BUY	\$29.25
Golbal Robotics & Automation ETF	ROBO	\$50.36	0.24%	BUY	\$52.88
Invesco Basic Materials ETF	RSPM	\$31.02	0.45%	BUY	\$32.57
Invesco Health Care ETF	RSPH	\$27.40	0.66%	BUY	\$28.77
Invesco Small Cap Industrials ETF	PSCI	\$99.46	0.85%	BUY	\$104.43
Moderna	MRNA	\$103.29	0.00%	BUY	\$108.45
S&P 500 Equal Weight ETF	RSP	\$141.69	1.79%	BUY	\$148.77
Virtus LifeSci Biotech Products	BBP	\$50.03	0.00%	BUY	\$52.53
Hedges	Symbol	Price	Yield	Action	Limit *
ProShares UltraShort S&P 500	SDS	\$37.11	2.18%	BUY	\$38.97

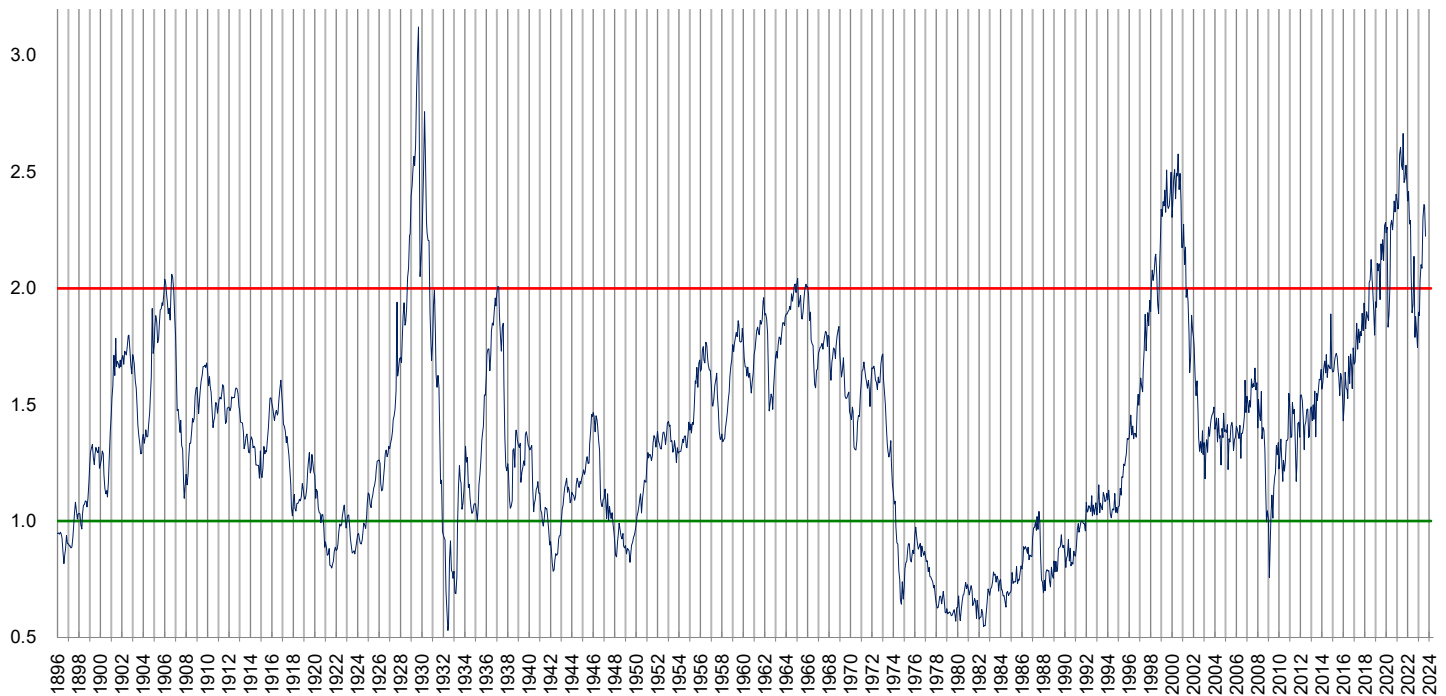
* **Note to the table:** The right hand column is the highest recommended price limit for purchases.

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 \$578 million versus \$26.4 million by simply holding stocks through the ups and downs, or 23 times more money.

With the latest median house price at 436,600 in July 2023 (the latest data) and with the S&P 500 averaging 4,409 in September, the **Sound Advice** Risk Indicator read 2.22.

The New York Times

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

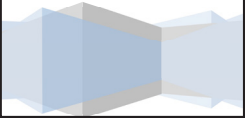
SoundAdvice

The Science of Making Money in the Stock Market

By Gray Emerson Cardiff

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

By John Jackson



Available for Kindles and Ipad, as well as in paperback

The Science of Making Money in the Stock Market (The 2022 Edition)

This is the book that explains all of the **SoundAdvice** indicators, including the Diffusion Indexes and Risk Indicator, and exactly how they work, along with a detailed history to back up the track records.

Use the link: <https://www.amazon.com/dp/B09M547W93>

Price \$7.99 (Free for Kindle Unlimited). Free to share with friends and relatives.

Business Cycles and Stocks: The SoundAdvice Diffusion Indexes

The Risk Indicator reveals long macro cycles. An analogy can be made to the way radio waves work. Long radio waves have frequencies which are assigned to various radio stations, allowing you to distinguish them on your radio. Riding along the path of these long waves are short waves that produce the sound you actually hear on a particular station. These short waves are like the bull and bear markets revealed by the Diffusion Indexes.

While the path of the long cycles revealed by the Risk Indicator may be in a certain direction, there are bull and bear markets along the way. Of course, these relatively short bull and bear markets are significant during our investing careers. Even during times when the Sound Advice Risk Indicator is above the "low risk" reading, such as it is now, there have been substantial bull markets. We will rely on our Diffusion Indexes to reveal when that will be.

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.

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.

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.

Track Record of the SoundAdvice Diffusion Indexes

During 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 0.6 percent.

Signal Dates (Month-Year)			
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
Dec-22	3,912.38		
Ave +/-	31.5%		-0.6%

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

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

The latest leading and lagging economic indicators were published in late August for the month of July.

Our current “Aggressive” mode was established by a zero reading for the Diffusion Index of LEADING Indicators in December 2022 based on the leading indicators for November 2022. This index dropped to zero again in March. It read zero percent again based on latest leading indicators.

Our next signal will be a “Caution” signal from a 100 percent reading on the Diffusion Index of LAGGING Indicators which recorded 33 percent based on the latest lagging indicators.