

# SoundAdvice

Advising Investors for 34+ years

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## Another Credit Crunch?

The collapse of Silicon Valley Bank rattled markets in March and brought into question the competence of regulators. There was little question regarding the incompetence of the bank's management, which allowed the core of its capital to reside in long-term Treasury bonds that were purchased before interest rates started rising. At that time, the bank's \$21 billion bond portfolio had an average yield of 1.8 percent. Of course, the value of the portfolio dropped precipitously as rising interest rates pushed up bond yields. However, these bonds were held in a "hold to maturity account" which allowed the bank to value them at par and ignore the steep drop in value. When customer deposit withdrawals began increasing as capital dried up for its start-up and venture customers, the bank was forced to move these bonds out of that special account and devalue them to current market prices, leading to the collapse.

This is astonishing for two reasons. The first is that the bank's management would invest in long-term Treasury bonds at historically low interest rates and continue to hold them while growing inflationary pressures were obvious and bound to lead to a rise in interest rates and bond yields (and thus a drop in bond prices).

The second is that the bank's bond portfolio was not hedged, which is a common practice among most banks. During 2022, the *Sound Advice* portfolio included three such hedges designed to make profits from rising bond yields. Our largest profit of 150 percent came from an ETF with 3x leverage (TMV). The ETF with 2x leverage returned 92 percent (TBT). Even the ETF with no leverage (TBF) returned a profit of 42 percent.

Signature Bank collapsed the same weekend in mid-March, and the stocks of other banks suffered in the weeks that followed, especially those of many other regional banks. Naturally, this stoked memories of the 2008-09 great financial crisis.

A systemic fallout was stemmed by Federal actions. The deposits still remaining in Silicon Valley bank were guaranteed above the \$250,000 limit, and a special "Bank Term Funding Program" was quickly established to give all banks necessary cash to honor withdrawal of deposits. Additionally, Treasury Secretary Janet Yellen said that other deposit guarantees will be made in the event more systemic risks appear.

The avoidance of systemic contagion does not mean that there won't be other consequences. Regulators missed this one and will be increasing their surveillance and tightening up regulations on regional banks. And gone are the days when depositors will leave deposits substantially greater than the \$250,000 FDIC insurance limit. This is certain to lead to a reduction in lending activity and introduce a credit crunch. While the severity is not likely to be the credit crunch of the great financial crisis of 2008-09, it is bound to be immediate and significant, resulting in diminished overall economic activity in the months ahead.



**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, averaging an 8.76% annual return versus 4.27% from the S&P 500.

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## Continued Resolve

During the news conference following the Federal Reserve's mid-March meeting, Chairman Powell said the Federal Open Market Committee (FOMC) considered a pause in rate hikes in light of the banking crisis, but ultimately unanimously approved the decision to raise rates due to intermediate data on inflation and the strength of the labor market. In its prepared statement, the committee said,

*"The U.S. banking system is sound and resilient...but recent developments are likely to result in tighter credit conditions for households and businesses and to weigh on economic activity, hiring, and inflation..."*

As long as the Federal Reserve continues to keep interest rates high in its resolve to quell inflation, the economy is bound to soften, along with a sharp drop-off of inflation this year. The added weight of the new credit crunch adds to the certainty.

Smaller monthly increases in the CPI will produce declining year-over-year increases. Monthly CPI increases have averaged 0.27 percent since July. If that average continued, inflation as measured by year-over-year changes of the CPI, would drop below 3.3 percent in 12 months. However, if monthly increases of the CPI were to average 0.16 percent as the economy softens, inflation would drop below three percent by September and stabilize at 1.9 percent in 12 months.

The expectation of declining inflation is providing a foundation under stock prices. The majority of investors can see that the Federal Reserve's tight monetary policy will be ringing out inflation in the foreseeable future. The bank crisis now adds to that certainty. As a result, the end of the Federal Reserve's tight monetary policy is visible.

## The Sound Advice Diffusion Indexes

At the beginning of 2022, our **Sound Advice Diffusion Index of Lagging Indicators** (page 11) was in "Caution" mode. Once again, this warning proved prophetic. The S&P 500 index ended the year down 19.44 percent. 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 a result of heeding our caution signal and positioning our holdings accordingly, the *Sound Advice* portfolio gained 4.02 percent in 2022.

By contrast, we had a completely different situation as we began 2023. Our **Sound Advice Diffusion Index of Leading Indicators** dropped to zero in December 2022 (page 11). This signal revealed that the economy had softened sufficiently to allow room for interest rates to decline. This meant that the end of the Federal Reserve's interest rate hikes was visible and we removed our "Caution" signal.

Our **Sound Advice Diffusion Indexes** 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. During "Aggressive" signals, the S&P 500 climbed an average of 31.5 percent, and the market has never crashed. These have been times of declining or low interest rates, along with declining or low inflation.

## The Sound Advice risk Indicator

Our **Sound Advice Risk Indicator** (page 10), which compares the S&P 500 index to house prices, reveals when risk is extremely high (above 2.0) in the stock market and when it is extremely low (below 1.0). High-risk readings have presaged every major crash or extended bear market, and its track record spans more than 125 years. The latest reading increased to 2.06 because the latest median house price dropped to \$426,500 in January from \$469,900 in December.

During times when the **Sound Advice Risk Indicator** is revealing high risk in stocks, such as it is now, there have still been substantial bull markets. The "Aggressive" signal from the **Sound Advice Diffusion Index of Leading Indicators** is telling us that another bull market is on the horizon.

## The Sound Advice Portfolio

Our 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) investing in sectors that are bound to benefit in the months and years ahead.

We eat our own cooking at *Sound Advice*. Among the editor and affiliates, we invest in all of the *Sound Advice* portfolio recommendations. This includes the *Sound Advice* Diversified Growth Fund which is managed by the editor. The editor is also an investor in this fund, on a side-by-side basis with other investors.

## Adding Intelligence to the Portfolio

ChatGPT, the open, generative artificial intelligence (AI) chatbot, is giving us a glimpse into the next technology frontier. Artificial intelligence will only grow smarter and play a greater role in the way we live our lives and the way companies around the world operate.

We believe it is a good time to add the **Global Robotics and Automation Index ETF (ROBO)** to the portfolio.

ROBO is investing across the entire ecosystem of robotics and automation, aiming to capture automation as a megatrend. Close to 60 percent of the portfolio is in robotics technologies, and 40% is in the technology underneath the robots -- the sensing and computing actuation, AI, and integration. ROBO invests the whole ecosystem of automation because while growth in automation is relentless, it's not necessarily moving sector by sector in lockstep.

Lauren Hein, head of advisor relations of ROBO, says:

*"We look at the 11 subsectors that make up the automation ecosystem. We look for market and technology leaders in those sectors. We look at a company that's going to be able to really penetrate that market and provide solutions... We are investing in companies like Machine Vision, Cognex and Keyence from Japan and Samsara. Ultimately, we don't care where a company is located. We just care that they're leaders in some component of the automation megatrend."*

ROBO has over \$1.3 billion in assets which makes it liquid and tradable. It has a broadly diversified portfolio of stocks of 80 different companies, with no more than 2.2 percent in any single holding. The top 10 holdings are as follows:

**Cognex:** A manufacturer of machine vision systems, software and sensors used in automated manufacturing to inspect and identify parts, detect defects, verify product assembly, and guide assembly robots.

**Harmonic Drive Systems:** A Japanese company that makes equipment and components for industrial robots, semiconductor manufacturing equipment and other systems.

**IPG Photonics:** A manufacturer of high-performance fiber lasers used in industries including medical devices and telecommunications.

**Kardex Holding:** A Swiss logistics company that provides automated storage solutions.

**Samsare:** a maker of software that helps track fleets of vehicles and other equipment.

**Fanuc:** A Japanese manufacturer of factory automation products including lasers, robots, and electric injection molding machines.

**Zebra Technologies:** A mobile computing company specializing in technology used to sense, analyze, and act in real time through integrated platforms to evolve and meet customers' needs.

**ServiceNow:** Develops cloud computing platforms to help companies manage digital workflows for enterprise operations.

**Automation Tooling Systems:** A Canadian company that designs and builds factory automation systems.

**Keyence Corp:** A direct sales organization that develops and manufactures automation sensors, vision systems, barcode readers, laser markers, measuring instruments, and digital microscopes.

Since its inception in 2013, ROBO has essentially matched the return of the S&P 500 which is commendable considering the rise of the S&P 500 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 future.

## A Downside Hedge

We employ a downside hedge as part of the portfolio because it reduces risk and 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.

The overall trailing twelve-month (TTM) price/earnings (P/E) ratio is extremely high, currently 33. This lofty P/E ratio makes the Russell 2000 index more vulnerable than the S&P 500, offering more downside profit potential.

Including a hedge like this as part of a portfolio dampens the overall volatility and adds a measure of safety.

**ETFs for Rising Bond Yields**

The two ETFs listed below are designed to benefit from rising long-term Treasury bond yields. They differ in the amount of leverage used.

**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 TBT to increase by 2.0 percent and TBF by 1.0 percent. These were stellar investments in 2022. TBT was up 92 percent, and TBF was up 42 percent.

We are likely near the peak of short-term interest rates because the economy is bound to be softening in the months ahead. However, even assuming inflation subsides to 2 percent, yields on long-term Treasury bonds are still too low.

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.) Real yields were lower during the Federal Reserve’s four quantitative easing (QE) programs, which began in 2008, but QE programs are over now. It is important to note that before the QE programs, the average real return was 3.7 percentage points above the inflation rate.

If we assume that inflation simmers down to the Federal Reserve’s target of 2 percent, the yield on long-term treasury bonds should stabilize in the range of 4.7 percent to 5.7 percent. Of course, bond yields will be commensurately higher if inflation remains stubbornly higher.

The nearby table – ETF Upside Potential -- 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.

**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, TBT by 0.7 percent, and TBF by 0.2 percent.

**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
Average Prior to QE programs			<b>3.7</b>
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			<b>2.7</b>

**ETF Upside Potential**

Date	20-Year Bond Yields	ETF Prices	
		TBF	TBT
3/31/2023	3.80	21.13	27.96
12/31/2023	4.70	23.17	33.23
12/31/2023	5.70	25.29	38.77

## Special Situations

These are stocks of 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 high (P/E) ratios anticipate high growth rates which is a disaster waiting to happen. We are recommending buying under \$135 per share. This price target puts the TTM P/E at 22 which is on the high side for most stocks but a reasonable value for AAPL.

**Cisco Systems (CSCO)** is a direct beneficiary of the major upgrade cycle into the fifth generation (5G), which is able to download data 100 times faster than the previous generation of 4G. Operating in 5G requires upgrading to faster equipment. The rollout of 5G is just beginning which means several years of growth prospects are ahead.

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 nearly one-half of total revenues.

**Crown and Castle International (CCI)** is also benefiting from the future of 5G wireless technology because a higher density of large and small cell sites and related infrastructure is required.

CCI presents a relatively low risk way of investing in this high-tech area because of its unmatched portfolio of hard assets comprised 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. 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.

Management believes its portfolio positions Crown and Castle to achieve its long-term annual dividend per share growth target of 7% to 8%. The company is committed to sharing its growth with its stockholders. The dividend has been increased every year since 2014.

**JP Morgan Chase (JPM)** has seen deposits grow during the banking crisis as funds have moved from regional banks to large money-center banks. JPM may continue to remain somewhat volatile while the banking crisis exists, which may provide buying opportunities.

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. The company 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.

Prospects for Moderna's revolutionary messenger mRNA Covid-19 vaccine, called Spikevax, pumped up MRNA to its peak of \$495 per share in September 2021. As this and Pfizer's solution caused the pandemic to subside, the consensus grew that the company's revenue would begin declining, and the stock crashed to below \$140 in 2022. In 2023, Covid-19 vaccine revenue is projected to be \$5 billion, down from \$18.4 billion in 2022. However, the company has 48 programs in development, including 36 in ongoing clinical trials, and increased its 2023 R&D budget to \$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.

In late February, the FDA granted a "Breakthrough Therapy Designation" to the personalized cancer vaccines being developed in a collaboration between Moderna and Merck, whereby cells from the patient's tumor are analyzed and subjected to RNA sequencing. Personalized cancer vaccines are designed to prime the immune system so that a patient can generate a tailored anti-tumor response specific to their tumor's mutation signature.

Breakthrough designations are granted to expedite the development and review of drugs that are intended to treat a serious condition, and when preliminary clinical evidence indicates that the product may demonstrate substantial improvement over available therapies.

Also granted a breakthrough designation was Moderna's vaccine candidate for the Respiratory Syncytial Virus (RSV), a

lower respiratory tract disease, after the vaccine showed an efficacy of 83.7 percent in January in older adults and was generally well-tolerated with no safety concerns.

RSV is a highly contagious seasonal respiratory virus and a leading cause of lower respiratory tract infections and pneumonia, causing a particularly large burden of disease in infants and older adults, with an estimated 5.2 million cases and nearly half a million hospitalizations.

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

**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 has the ability to refine substantial quantities of 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 for delivery to its gulf coast locations.

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 shortages of refined products for the foreseeable future.

Meanwhile, 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. Use for sustainable aviation fuel is expected to be a primary escalating demand factor. With diesel prices rising along with other refined products, this has become a more significant growth aspect for VLO.

## 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. There is substantial equity in the respective common stocks, evidencing that the market does not expect liquidation to be plausible. In all three cases, the value of each company’s real estate portfolio would have to drop precipitously from its current value before any portion of the liquidation preference would be jeopardized.

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. The price of this preferred is still substantially below its call price and liquidation preference of \$25, offering an attractive discount and high current yield.

This is one of three preferred stocks. The total dividends for all three preferred stocks were only 10.2 percent of the company’s cash income in 2022. Accordingly, this income is secure because it could only be jeopardized by an unimaginable catastrophe.

Hersha Hospitality Trust is a real estate investment trust (REIT) which owns and operates luxury and lifestyle hotels in urban gateway and regional resort markets. The Company’s 27 hotels totaling 4,125 rooms are located in New York, Washington DC, Boston, Philadelphia, South Florida, and California. The company would have to be liquidated with its portfolio value substantially below its current value before the full liquidation preference to be jeopardized. Evidently

the market does not think that will happen because the common stock is reflecting significant equity.

**RLJ's \$1.95 Series A Cumulative Convertible Preferred (RLJPRA)** is RLJ's only REIT's preferred stock, and it 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). This preferred stock has a liquidation preference of \$28.50 per share.

The dividends for this preferred was only 10.0 percent of the company's cash income in 2022, making this income secure.

RLJ Lodging Trust is a hotel investment company that owns premium-branded, high-margin, focused-service and compact full-service hotels. The Company's portfolio consists of 96 hotels with approximately 21,200 rooms located in 23 states. During the first half of this year, operating revenue from its hotel portfolio recovered beyond the pre-Covid level, and the company no longer has financial covenants requiring 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, for a high current yield. This is the only 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, which offers long-term upside growth potential. This preferred stock has a liquidation preference of \$50 per share.

The dividends for this preferred was only 3.9 percent of the company's cash income in 2022, making this income secure.

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.

## Sector ETFs

We are also recommending 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, and they 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.

### 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 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. Technological breakthroughs in artificial intelligence and other high-tech 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 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.

## Balanced ETFs

The following ETFs rebalance their holdings quarterly to equalize the values, which ensures 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 exposure to many stocks that are under-weighted in most other portfolios and are therefore targets for new capital.

### Health Care

**Invesco's S&P 500 Equal Weight Health Care ETF (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 RYH are rebalanced quarterly. This approach has given RYH a better performance than the large health care ETFs over the last 10 years.

Health care stocks have several traits that make them desirable 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. The remedy is to invest in an ETF like this one, that spreads its sections evenly on a percentage basis, rather than by the capitalization of the holdings. Historically, this equal-weight approach has worked well and provided a more stable and superior investment return.

### Consumer Staples

**Invesco S&P 500 Equal Weight Consumer Staples ETF (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), 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.

### US Infrastructure

The bi-partisan infrastructure bill enacted in November 2021 will benefit both of the following two ETFs for many 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.

**Invesco S&P 500 Equal Weight Materials ETF (RTM)** invests in the common stocks 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. China's economic reopening from its Covid lock-down will also be exerting new demand for basic materials.

## Portfolio Summary Table

This table is updated and live on our website:  
www.soundadvice-newsletter.com

Income with Growth	Symbol	Price / NAV	Yield	Action	Limit
Hersha Hospitality Trust - Preferred D *	HTPRD	\$19.41	8.45%	BUY	\$25.00
RLJ Lodging Trust - Preferred A *	RLJPRA	\$25.06	7.78%	BUY	\$28.50
RPT Realty 7.25% Preferred D *	RPTPRD	\$47.53	7.63%	BUY	\$50.00
Growth with Moderate Income					
Cisco Systems	CSCO	\$52.26	2.83%	BUY	\$54.87
Crown and Castle	CCI	\$133.84	4.68%	BUY	\$140.53
Invesco Consumer Staples ETF	RHS	\$170.06	2.68%	BUY	\$178.56
JP Morgan Chase	JPM	\$130.31	3.07%	BUY	\$136.83
Valero	VLO	\$139.60	2.81%	BUY	\$146.58
Growth					
Apple	AAPL	\$164.86	0.50%	HOLD	\$135.00
Genomic Revolution Multi-Sector	ARKG	\$30.09	0.00%	BUY	\$31.59
<b>Golbal Robotics &amp; Automation ETF</b>	<b>ROBO</b>	<b>\$54.72</b>	<b>0.09%</b>	<b>BUY</b>	<b>\$57.00</b>
Invesco Basic Materials ETF	RTM	\$161.95	1.69%	BUY	\$170.04
Invesco Health Care ETF	RYH	\$290.65	0.63%	BUY	\$305.18
Invesco Small Cap Industrials ETF	PSCI	\$93.60	1.05%	BUY	\$98.28
Moderna	MRNA	\$153.55	0.00%	BUY	\$161.23
Virtus LifeSci Biotech Products	BBP	\$49.37	0.00%	BUY	\$51.83
ETFs for Rising Bond Yields					
ProShares Short 20+Treasury - 2X Leverage	TBT	\$27.96	0.00%	BUY	\$29.36
ProShares Short 20+Treasury - No Leverage	TBF	\$21.13	0.00%	BUY	\$22.19
Hedges					
ProShares UltraShort Russell 2000	TWM	\$15.50	0.00%	BUY	\$16.28

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

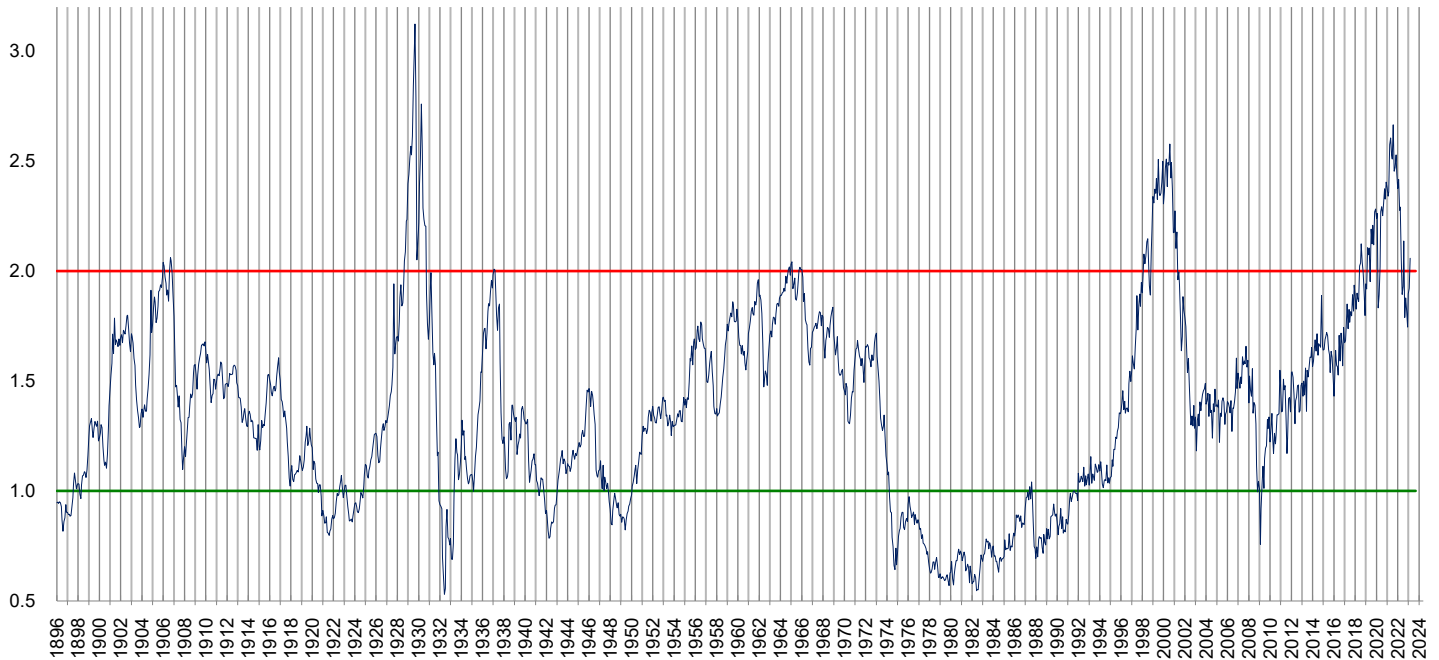
\* It is not possible to offer live pricing.

**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 \$619 million versus \$23.3 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

**The New York Times**

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

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 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 426,500 in January 2023 (the latest data) and with the S&P 500 averaging 3,968.56 in March, the *Sound Advice* Risk Indicator read 2.06.**



**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"  
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## 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.

## 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

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.

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

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. Our next signal will be a “Caution” signal from a 100 percent reading from the Diffusion Index of LAGGING Indicators which recorded a 33 percent in February (the latest reading).

