



The **SoundAdvice** portfolio is up 20.8 percent so far this year. This compares to 11.8 percent for the S&P 500. We have an average gain in the **SoundAdvice** Model Portfolio of 41.9 percent based on the prices at which each stock or mutual fund was recommended.

In this Issue, we update all of our current recommendations. We begin with our "No-Brainer", the reverse ETFs that will benefit strongly from a rise in yields on long-term Treasury bonds.

We then update all of our other recommended positions in alphabetical order. See the table on page 7 for buy limits and other information on each recommendation.

Due to an improvement in economic conditions and significant increases in the leading indicators, we will not get the green light soon from our Diffusion Index of Leading Indicators. See page 10. Accordingly the cautionary signal given by our Diffusion Index of Lagging Indicators in April, close to the peak of the market still stands.

A green light would also mean a lasting decline in interest rates is at hand. But such is not the case. For reasons we explain, quite the opposite is inevitable.

On page 10 and 11, we examine the foreclosure situation. Unfortunately, not much of an improvement has occurred, so we still cannot see a light at the end of the tunnel

*-Gray Emerson Cardiff*

## Another Opportunity for a No-Brainer?

We have seen some volatility in our three reverse ETFs that are designed to benefit from an increase on long-term Treasury bond yields. The ETF with the most leverage, TMV with 3:1 leverage, got close to \$60 a share as 30-year Treasury bond yields approached 3 percent. These ETFs have since settled back as yields pulled back, which is giving us another opportunity to invest.

It is interesting to see these ETFs in action and understand exactly how they work. Each ETF is using futures and other derivatives to match the reverse of the percentage changes in yields as measured by the 20+year index of Treasury bond yields. The ticker symbol of this index is AXTWEN. If for example the change in AXTWEN is a decline of say, 0.5 percent in a given day, TBF (the reverse ETF using no leverage) should increase by 0.5 percent. TBT, which uses 2:1 leverage, should increase by 1.0 percent. TMV, which uses 3:1 leverage, should increase by 1.5 percent. Of course, these ETFs are set up to match the reverse of the increases in AXTWEN, which will produce corresponding declines in the prices of these ETFs in accordance with prescribed leverage. These ETFs have been behaving as they should on a daily basis during the recent past few months.

It is worth noting that the daily compounding can result in greater volatility over a longer period than the simple change in the index over the same period. In addition, the daily compounding may add up to a result that is different than the simple change in the index over the same period.

To exemplify, we look back at the period from December 31, 2008, when 30-year Treasuries were yielding 2.69 percent – close to today's yield. By July 23, 2009, yields had climbed to 4.6 percent. If we use the daily history of percentage changes in these yields, and apply three times the reverse of these daily changes to today's price (rounding to \$50.00 a share) of TMV (which uses 3:1 leverage), TMV would climb to \$192.55 per share. However, looking at the simple difference of the yields would put the price of TMV at \$156. So the daily compounded has boosted our profit by 23 percent.

In this example, the daily compounding has magnified our gain. However, the daily compounding magnifies losses as well. In fact, this compounding is more powerful on down days because the daily percentages are taken of a higher number for the previous day's close.

To exemplify the downside, say we start with TMV at \$50 a share. The next day, Treasury yields increase 6 basis points from 2.65 percent to 2.71 percent. That is a change of 2.26 percent. Multiplying by 3 is a change of 6.79 percent which pushes the price of TMV up \$3.40 to \$53.40. Now, suppose yields drop back down the next day by 6 basis points and return to 2.65 percent. That is a decline of 2.21 percent. Multiplying by 3 is 6.64 percent which is \$3.55 of TMV's prior close of \$53.40. This decline brings the price back to \$49.85. So we have lost 15 cents on a return to the same yield on Treasuries.

Despite this negative aspect, these ETFs are worth a substantial investment right now. Even if we lost a little ground as these ETFs tread water, the upside

# The History of 30-Year Treasury Bond Yields



This graph shows the yields of 30-year Treasury bonds since 1977. As you can see, the recent lows are historic. Yields have been close to the recent lows only once before -- after the 2008-09 meltdown as systemic risks in the banking system fueled a capital flight to safety. The yield reached a low of 2.69 percent in December, 2008. After climbing to 4.7 percent in March 2010, yields plunged below 2.5 percent in July, 2012. Source: Yahoo! Finance

is worth it. These are still no-brainers as long as we can stand the ride and can wait until interest rates head back up. It's not a question of whether they will, it is only a question of when. In addition, there is no reason that long-term Treasuries will not climb significantly higher than 4.6 percent. For example, long-term Treasury yields continued a hypothetical pattern of inching up 2 basis points one day, and declining one basis point the following day, yields would reach 5.22 percent, and TMV would climb to \$371 a share. Of course, the climb will not be this orderly, but a yield of 5.22 percent on long-term Treasuries in two years is a reasonable expectation.

## Double Up

The recent pull back in these ETFs provides another opportunity to invest. We have to go back to the depths of the 2008-9 financial crisis to find Treasury yields close to this low. That was when the entire banking system was facing systemic risks, and there was a massive capital flight to safety as capital poured into Treasuries.

The three ETFs we are recommending are:

**Proshares Short 20 Plus year Treasury (TBF-NTSE)** uses no leverage;

**Proshares Ultrashort Lehman 20 Plus year Treasury (TBT-NTSE)** uses 2:1 leverage;

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

When yields on Long-term Treasury Bonds start heading back up, these ETFs will rise substantially.

**If you have not invested, we recommend that you do so now. If you have already taken a position, we recommend that you double it now.**

You can manage your risk by measuring the amount you invest, and choosing the ETF whose leverage that matches your risk tolerance and investment objective. You can also invest in stages, buying at different times and averaging your cost basis – as we are doing now. We do not see much room for long-term rates to go lower. The greatest and most explosive movement will be upward, and the profit potential is enormous with these ETFs.

Keep in mind that “Operation Twist” is an artificial situation and not permanent. A yield curve this flat is highly abnormal. Long-term rates are usually much higher to account for the uncertainties of inflation in the decades ahead.

Gains will be substantial with merely a return to 4.6% on 30-year Treasury bond yields -- not high by historical standards (see the chart above). Normally, these yields are 3 percentage points above the inflation rate, offering a real return after adjusting for inflation.

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As the economy recovers, expectations of increasing inflation will return. This alone will force long-term interest rates upward. There will be additional upward pressure because our national debt has grown alarmingly in recent years. It is close to \$15 trillion when external debt is included (debt owed to creditors outside the country) bringing the total close to 100 percent of our GDP.

This debt needs to be financed through the sale of Treasury bonds -- and there will be historically high amounts of sales. This will add downward pressure to Treasury bond prices which will increase their yields.

It is simply a matter of time when today's historically low yields on long-term Treasuries will be just that -- history. This comes as close as you can get to a "No-Brainer".

## Portfolio Updates

Here are updates on the rest of our recommendations, in alphabetical order:

**Agrium (AGU)** is up again since our last issue, extending our profit to 719 percent. We originally recommended this stock and continue to hold it because it is the largest farm products retailer in North America, and because it is a wholesaler to the rest of the world. In order for emerging markets to meet their needs for food, they will either have to import foodstuffs from the more advanced countries or, better for the fertilizer industry, use fertilizer to improve their crop yields. Either way means more use of fertilizers.

AGU was recently featured in Investor's Business Daily: *Farming has a growing global customer base with a growing demand curve...Agrium supplies products to farmers globally. South America and North Africa are expanding their agricultural footprints, and there have been upswings in farming in China and India in the last few years ... Farm acreage in the U.S. has stayed constant, but from a global perspective, they're chopping down trees and pushing into the Amazon...Emerging markets are demanding more expensive foods in their diets.*

**AMN Healthcare (AHS)** has been strong primarily on better than expected jobs growth. AHS provides temporary health care staffing services to the healthcare industry, ranging from nurses to physicians.

When we first recommended this stock, it rocketed 45% in three months, jumping way ahead of the market based on optimism about the economy, and especially job creation. The initial run up in price provides a road map for how we expect AHM will play out.

The rationale for buying AMN Healthcare is a two-fer. AMN is not just an opportunity to invest in healthcare, which is traditionally a non-cyclical industry, but it is also a chance to buy into a health care business that will benefit from a recovery in the economy. We have a 58 percent gain and expect considerably more.

**Associated Estates Realty Corp (AEC)** is the most

undervalued apartment REIT in the sector. It was once a low-income apartment REIT, but that is no longer the case. AEC has disposed of its older properties, most of which were sold during real estate's more buoyant years, and has replaced them with class A apartment properties. The equity of its apartment portfolio translates into a stock value that is nearly double the current stock price. It pays a nice yield as well. We have a small profit, and expect much more ahead.

**Boston Scientific (BSX)** is a classic turnaround story. It has had flat earnings this year due to lower demand for surgeries that require the company's devices produced by its cardiology and cardiac rhythm Management segments. However, a brighter day is ahead from innovations and acquisitions.

BSX recently received approval in Europe for use of its unique pacemakers which are not impacted by MRI scans. This is an important advancement because a significant number of patients with pacemakers have other conditions requiring MRI scanning.

BSX's new LATITUDE™ NXT Remote Patient Management system enables physicians to monitor patients with pacemakers remotely, as well as to conduct remote monitoring of general heart health status, blood pressure, respiratory events, and sleep apnea trends.

Other BSX innovations include its Epic Vascular Self-Expanding Stent System, designed to open blocked arteries. In addition, the recent acquisition of Cameron will enhance its cardiac rhythm management business. Cameron has a defibrillator (S-ICD) that is implanted without touching the heart or blood vessels. The device is pending likely FDA approval.

The new CEO, Mike Mahoney, is from Johnson and Johnson, and is committed to following through with the current austerity program aimed at curbing operating expenses through a restructuring program which is targeted to save between \$650 million and \$750 million annually.

We do not have a profit in BSX, but expect to within the next 12 months. That's not just our opinion -- BSX is buying back its own stock in an aggressive share-repurchase program. This alone will boost earnings, not to mention the introduction of new innovative products. Gains from the current price should be substantial.

**CGM Real Estate Fund (CGMRX)** is up 10 percent this year, extending our profit to 56%. We got back into it again after the 2008-09 crash in REIT prices.

CGMRX is as good as it gets for a REIT fund. CGMRX put on quite a fireworks show between 2003 and 2007 (+89.7%, +35.5%, +27%, +29%, +34.4%). We made a 145% profit during that period.

Ken Heebner, has run the fund since its inception in 1995. He is known as "The Mad Bomber" because he has never been considered cautious. He either outperforms or underperforms significantly, and this fund can be volatile,

but Heebner's good years are really good. We watch his portfolio choices closely, so that we can judge whether the holdings make sense to us.

We have had input from a few subscribers that this fund is closed to new investors. We double checked with the fund by calling the number shown on the table on page 7, and they assured us that is not the case. However, some brokerage firms may be telling customers the fund is closed because they do not have a means to buy it. If your broker is telling you the fund is closed, we recommend pursuing the problem with your broker, or simply call the fund directly.

**Chesapeake Energy (CHK)** was included in the portfolio earlier this year because it has natural gas assets worth in excess of \$27 a share. The shares were cheap for two reasons: low natural gas prices and poor corporate governance.

Since then, natural gas prices have climbed 50 percent, and Carl Icahn bought a stake and has been instrumental in removing the founder, Aubrey McClendon, as chairman of the board and replacing several other board members.

The spotlight is now on the board to maximize shareholder value. We have a 16 percent profit for the short time we have owned CHK but expect a great deal more.

**CommonWealth REIT (CWH)** conducted an earnings call since our last issue. and made the following statement:

"With the weak leasing market conditions, declining occupancy in a CAD [cash available for distribution] payout ratio above 100%, many investors may question the security of the company's dividend rate going forward. Obviously, the stock price for the company has indicated that the market anticipates a possible dividend reduction, because the dividend yield has been over 10% for almost a year.

Given all these dynamics and unless market conditions start improving meaningfully, it may become necessary for the Board of Trustees to adjust the dividend rate during the next couple of quarters in order to retain more cash flow as we increase occupancy at our properties in the future.

Funds from operations FFO has been well in excess of the dividend payments. However, the above reference to CAD (cash available for distribution) being above 100% is after capital expenditures are deducted. These capital expenditures include tenant improvements, leasing costs, building improvements, and development activities.

If the second quarter's FFO and capital expenditures are assumed to continue without improvement, the dividend would need to be adjusted to \$0.37 a share from \$0.50 currently, in order to have CAD be less than 100%. This would be a 9.3% yield on the current stock price.

Normally, capital expenditures are amortized over a number of years, and therefore are not included in the FFO calculation, which is the standard source of funds for dividend payments. However, the company's comments are

including capital expenditures in the reference to CAD and dividend coverage. By these comments, we must assume a dividend adjustment is likely.

The current price of the stock already assumes that the dividend will be reduced, based on the current yield. Accordingly, we do not see significant downside from here even with a reduction of the dividend. In fact, the stock price is likely to improve with a dividend adjustment because the cloud of uncertainty will be removed, and the new dividend will be dependable going forward.

We regard this latest decline in the stock as a buying opportunity. The underlying real estate portfolio is worth more than double the current capitalization of the company.

**Comcast (CMCSA)** is up 41 percent this year, extending our profit to 85 percent. This is considered the best managed cable company. Earnings are growing nicely – up 23% from a year ago. With its acquisition of AT&T's vast cable assets in 2004, and then its joint deal with Time Warner to acquire bankrupt Adelphia's cable business, it became the largest cable company.

Its recent purchase of the controlling interest in GE's NBC Universal division, is a growth engine. CMCSA is adding new and original program content, along with sports offerings, as an attraction to existing and new customers.

CMCSA also offers a package for full home control, which includes security, and energy management. Called XFINITY, it should be another source of growth, once it is marketed in an understandable way. It offers customers the ability to maneuver between video, phone, voice and home security, using any device -- from a phone or laptop to their television. CMCSA has embarked on a new advertising program to clarify, and correct the vague campaigns of the last two years.

CMCSA reinstated its dividend in 2008, which along with revenues, profits, and cash flow, has increased each year since.

CMCSA is also an indirect play on the real estate recovery. The housing recession has had a dampening effect as foreclosures and the accompanying financial stress has reduced customers. New signs of life in the housing market will be a strong benefit.

**Fidelity Select Natural Gas Fund (FSNGX)** is a play on the yawning gap between the energy equivalents of oil and natural gas. In comparison to oil, an equal amount of energy in the form of natural gas costs less than 20 cents on the dollar.

The US is self-sufficient in natural gas with only 9 percent imported from Canada. At pennies on the dollar versus oil, natural gas is bound to have a growing role in America's energy needs as well as independence from importing oil.

This fund is well positioned to benefit from an expanding natural gas industry, and should bring strong profits in the

months ahead.

**Hambrecht & Quist Life Sciences Fund (HQL)** is a closed-end fund (CEF), which means it trades not at its Net Asset Value (NAV) but at whatever price the market sets, which can create a discount or a premium to NAV. HQL is currently trading at a discount to its NAV.

We think HQL is a superior way to gain exposure to biotech on a diversified basis, which is a volatile sector. However, the most explosive profits in the entire healthcare industry can be found here. HQL is up 30% this year, extending our profit to 50%. This mutual fund has climbed inexorably most of the year, and should continue to do so.

The Fund began purchasing up to 12% of its own shares on the open market beginning in July. The share repurchase program is intended to increase the Fund's net asset value per share and to reduce the discount the stock has from the net asset value.

**Leucadia (LUK)** is a holding company with a portfolio in excess of \$9 billion of assets acquired by its two principals, Ian Cumming and Joseph Steinberg, who have been compared to Warren Buffett in their success at identifying lucrative investments that can be purchased substantially below their intrinsic value. In fact, Buffet continues to team up with the Leucadia team on joint venture investments.

Skillful investing has produced double digit growth rates in its assets since 1979. After a bad year in 2008, assets have since grown by 150 percent according to Morningstar.

We think that Leucadia is valued well below the market prices of its disparate parts. This stock is bound to recover with the economy.

**Masco (MAS)** manufactures a wide range of products for home construction and remodeling. Masco covers everything from kitchen cabinets and faucets to windows and paint.

Not surprisingly the shares got hammered during the downturn. Management had been through tough times before, and began cutting costs even before the housing sector went into free-fall.

We added MAS to the portfolio in October last year at \$7.49, when it was languishing in the doldrums. It has since climbed 92 percent.

Masco is moving to consolidate debt, close unprofitable plants, formulate and implement new systems, streamline global supply chains and cut personnel to cut costs. MAS expects to save \$150 million of gross cost reduction before

inflation with these policies.

**Maxim Integrated Products (MXIM)** is in excellent financial health with \$1.0 billion of cash and plenty of cash flow to support operations, as well as pay its quarterly dividend of \$0.22 per share.

On the data center front, MXIM just introduced its new transmitter chipset (40G) which supplies 4 times the bandwidth with very little electrical power. This is an important development because electrical power is the most critical constraint in data centers – those floors of computer servers that supply the “Cloud” we are all going to in droves for data and applications.

MXIM's press release said “Data centers and data communication networks need to significantly increase data density while staying within their already constrained power budgets. Maxim's QSFP+ transmitter solution addresses both challenges. The QSFP+ modules supply 4x the data throughput in only 1.5x the area of a single-channel SFP+ solution. Equally important, Maxim's chipset enables 4 x 10Gbps QSFP+ modules to consume less power per channel than single SFP+ modules. Service providers and network operators can now enjoy the benefits of a low-power solution that extends system life, reduces operational expense, and conserves valuable energy resources.”

MXIM also makes highly integrated analog and mixed-signal semiconductors. It has recently won notoriety for its solid state battery that harvests ambient energy. The device captures low-level

energy forms, such as from photovoltaic cells, vibrations captured by a piezoelectric element, and heat captured by a thermoelectric generator. This device can eliminate the need to run expensive power cables to remote locations or reduce the frequency of battery replacements.

We have a profit of 36 percent but expect more. Even if MXIM's price ratios merely rise to the valuations of its average years, the share price should easily double from here.

**Paychex (PAYX)** has been showing some life. Its core business is payroll services for small to medium sized companies. Accordingly, its revenues and earnings directly mirror the employment situation. Downside is limited because the balance sheet is pristine with no long-term debt exposure.

Based on the current price, the yield is close to 4 percent. This is a classic “buying straw hats in winter” opportunity that offers considerable potential for capital appreciation, along with safety, and a nice yield.



PAYX is up 10 percent this year, extending our profit to 22 percent, but there is a larger profit ahead with a recovery in the economy.

Pfizer (PFE) is still cheap because the patent expired on its blockbuster drug, Lipitor. However, there are many new, potential blockbusters in the pipeline.

PFE's restructuring plans have included the spin-off of its animal health unit along with the sale of its nutrition unit to Nestle for \$11.8 billion.

PFE is buying back its own shares with much of the proceeds of the Nestle sale. We agree with that decision. We have a profit of 41 percent and expect more. The stock is cheap and has nowhere to go but up.

**Retail Opportunities Investment Corp (ROIC)** is up 12 percent this year, extending our profit to 15 percent

This REIT began as an IPO in October 2009, just after the REIT sector had been decimated by the 2008 melt-down. It started with a fresh slate in a real estate market replete with bargains, with no debt and no problems. It is a simple model: buy distressed retail properties with high-quality demographics, refurbish them, and then lease them at a premium.

ROIC's shopping centers have high occupancy. Funds from operations (FFO) more than cover the dividend. As new properties are added, along with tenant upgrades, FFO should continue to rise, along with the dividend and price of this REIT.

**Stryker (SYK)** is best known for its orthopedic devices: artificial knees and hips, but it's much more. SYK provides a diverse array of innovative medical technologies, including reconstructive, medical and surgical, and neuro-technological and spine products.

SYK recently announced the release of their System 7 – the next generation of surgical power tools. It has many other new products with over 100 patents.

SYK is up 7% this year, extending our profit to 27%. More profits are assured by joint replacements on aging baby boomers.

**Symantec (SYMC)** has continued to climb. In late July, the company replaced its CEO and president with Steve Bennett who had a strong track record at Intuit and General Electric.

SYMC is the dominant supplier of software for computer security and protection against viruses and other nuisances. New markets are opening up for SYMC as the world moves to smart phones and other mobile devices, and hackers are starting to find security holes.

Recent acquisitions of Nukona, Inc, a provider of mobile application management, and Odyssey Software, a leading provider of mobile device management, enable SYMC to offer mobile apps that protect against hackers by authenticating users and encrypting sensitive files. SYMC is

also collaborating with Red Hat to deliver solutions that help customers deploy agile private and hybrid clouds, as well as create resilient data centers.

Earnings per share are starting to run ahead of expectations. The company's investment in cloud security and for mobile devices is starting to pay off. SYMC repurchased 19 million of its own shares during the first quarter. More recently on August 30, one of SYMC's directors (Geraldine Laybourne) purchased 897 shares at a price of \$17.88.

**Tellabs (TLAB)** has also shown some life recently after the stock drifted down close to the company's net assets of \$2.91 per share. There is no long-term debt, and other assets and liabilities offset each other. Subtract that \$2.91 from the current share price and you are buying the entire business for practically nothing.

TLAB is still operating at close to break-even in net earnings. Results have been sluggish due to declines capital expenditures from telecom companies and a weak pricing environment. However, this is not a permanent situation. The upside potential is good, especially from the wireless sector. Eleven of the Fortune 50 companies now rely on services provided through Tellabs' equipment. There is nowhere to go but up. It is only a question of when.

**Tetra Tech (TTEK)** is a leading company in water technologies. It designs complex and intricate plans that are used by local and national governments to meet future water needs, including desalinization.

TTEK has a healthy balance sheet, and water and environmental remediation are definitely growth industries. Recent contracts include remediating NASA's Kennedy Space Center and Cape Canaveral Air Force Station, along with environmental remediation services at U.S. Navy, Marine Corps, and other Department of Defense locations primarily in California and the southwestern United States.

The biggest potential business lies outside the United States in countries like China and India, where environmental concerns have been at best an afterthought. Only now are their governments starting to recognize the consequences. As governments around the world make this a priority, Tetra Tech should be a prime beneficiary.

TTEK is up 25 percent this year, extending our profit to 68 percent, and we see more profits ahead.

**USAA Precious Metals & Minerals Fund (USAGX)** is down 10 percent this year, which has reduced our profit to 11 percent. This sector has been under pressure due to weakness in the economy and strength in the dollar. However, we do not expect this situation to continue much longer.

USAGX is the best diversified way to invest in precious metals. It regularly ranks among the top-performing funds. Morningstar also rates it highly and it has accomplished these ratings without taking on oversized risk.

<b>Income With Growth</b>	<b>Sym</b>	<b>Exchange</b>	<b>Price</b>	<b>Yield</b>	<b>Limit</b>	<b>Action</b>
Associated Estates Realty Corp	AEC	NYSE	\$ 15.37	4.68%	\$ 17.00	BUY
CommonWealth REIT	CWH	NYSE	\$ 14.86	13.46%	\$ 20.00	BUY
Retail Opportunity Investment Corp	ROIC	NASDAQ	\$ 12.61	3.17%	\$ 13.00	BUY
<b>Diversified Growth</b>						
CGM Realty Fund	CGMRX	800-343-5678	\$ 29.83	0.87%	\$ -	BUY
Comcast	CMCSA	NASDAQ	\$ 33.53	1.94%	\$ 35.00	BUY
Leucadia National Corp.	LUK	NYSE	\$ 21.11	1.18%	\$ 23.00	BUY
Masco	MAS	NYSE	\$ 14.05	2.14%	\$ 15.00	BUY
Paychex	PAYX	NASDAQ	\$ 33.47	3.82%	\$ 35.00	BUY
Pfizer	PFE	NYSE	\$ 23.78	3.70%	\$ 25.00	BUY
Stryker Corp.	SYK	NYSE	\$ 53.82	1.58%	\$ 55.00	BUY
Xerox	XRX	NYSE	\$ 7.26	2.34%	\$ 7.50	BUY
<b>Energy/Natural Resources</b>						
Agrium	AGU	NYSE	\$ 98.20	0.46%	\$ 99.00	BUY
Chesapeake Energy Corp	CHK	NYSE	\$ 19.19	1.82%	\$ 21.00	BUY
Fidelity Select Nat. Gas Fund	FSNGX	800-544-8888	\$ 31.00	0.18%	\$ -	BUY
Tetra Tech	TTEK	NASDAQ	\$ 26.71	0.00%	\$ 28.00	BUY
USAA Precious Metals & Minerals	USAGX	800-862-6909	\$ 27.95	0.29%	\$ -	BUY
<b>Aggressive Growth</b>						
AMN Healthcare	AHS	NYSE	\$ 8.31	0.00%	\$ 9.00	BUY
Boston Scientific	BSX	NYSE	\$ 5.41	0.00%	\$ 6.50	BUY
ETF - Direxion Daily 20+ Yr Bear 3X	TMV	NYSE	\$ 49.99	0.00%	\$ -	BUY
ETF - ProShares Short 20+ Year Trsry	TBF	NYSE	\$ 28.46	0.00%	\$ -	BUY
ETF - ProShares UltraShort 20+ Year Trsry	TBT	NYSE	\$ 14.90	0.00%	\$ -	BUY
H&Q Life Sciences Fund	HQL	NYSE	\$ 14.96	7.22%	\$ 17.00	BUY
Maxim Integrated	MXIM	NASDAQ	\$ 27.32	3.22%	\$ 30.00	BUY
Symantec	SYMC	NASDAQ	\$ 17.88	0.00%	\$ 19.00	BUY
Tellabs	TLAB	NASDAQ	\$ 3.55	2.26%	\$ 4.00	BUY

ROWS IN **BOLD** INDICATE A CHANGE IN ACTION OR LIMIT

Prices are as of 9/4/2012. See our website for live pricing and buy limits.

<http://www.soundadvice-newsletter.com/members>

Yields on funds do not include distributions of capital gains. Note that all fund distributions fluctuate annually.

Mark Johnson, who has managed the fund for the past 17 years, has shown a talent at making the right decisions during his tenure. Since we consider funds managed by industry veterans superior to index funds, we cannot think of a better way to play gold and precious metals than this fund.

As in the case with CGM Real Estate Fund (CGMRX), we have also had e-mails from a few subscribers that this fund is closed to new investors. We double checked with the fund by calling the number shown on the table on page 7 and they assured us that the fund is open to new investors. Some brokerage firms may not have a means to buy it. We recommend pursuing the problem with your broker, or simply call the fund directly.

**Xerox (XRX)** has bounced back since our last issue. XRX is transforming from a seller of printers and copiers, which have thin profit margins and are highly dependent on economic conditions, to a company providing services on those machines. The revenue from services is more profitable and less cyclical. Now, half of XRX's revenues come from services.

Earnings are expected to be in the range of \$1.07 to \$1.12 per share this year. At close to 7 times earnings, these shares are really cheap, and any kind of recovery will bring a high capital gain.

## 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 100+ years, we can see this titanic struggle between the stock market and its foremost competitor for investment dollars: real estate.

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

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

We can, therefore, label this new tool the SoundAdvice "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 underperforming the other market.

What is too high? When stock prices are very high relative to house prices, the SoundAdvice 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 SoundAdvice Risk Indicator has oscillated back and forth, revealing the ongoing struggle between Stocks and houses for investment capital. We have labeled these long vacillations Supercycles.

The figures show that over the entire century-plus, stock prices have outperformed housing prices. Just based on the price growth of each investment market and assuming no leverage was used, a \$25,000 investment would have grown to \$8,235,294 in stocks and to \$1,192,553 in houses.

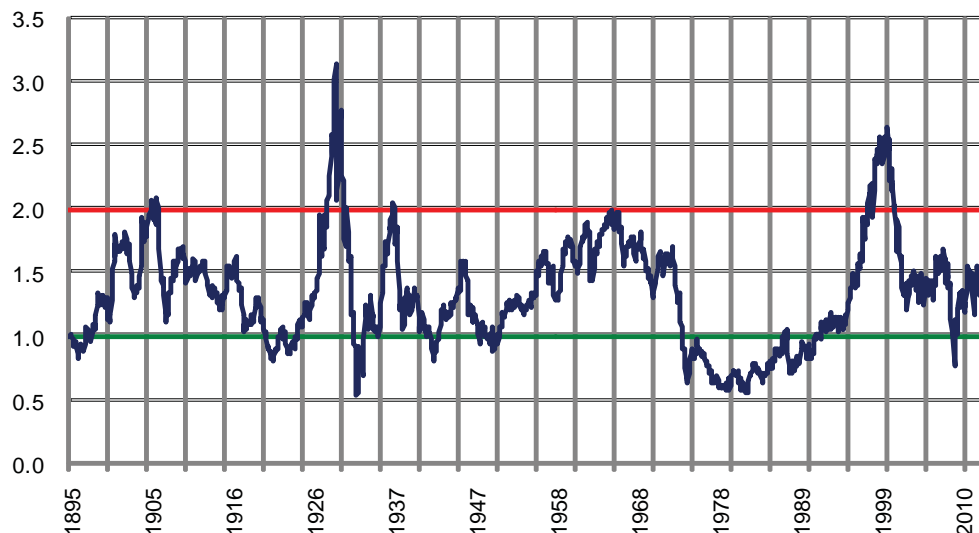
But though an investment beginning with \$25,000 in 1895 could have made money being in either stocks or housing and simply leaving it there over such a long period of time, had the investor followed the signals of the SoundAdvice Risk Indicator he would have made \$327,319,116, or 39.7 times more money—the difference between profits the buy-and-hold stock market strategy would have yielded by itself and the profits that the SoundAdvice Risk Indicator would have provided.

These figures illustrate why it is so important to remain aware of the Supercycles that are at work within markets.

### The SoundAdvice Risk Indicator

The latest reading for the SoundAdvice Risk Indicator is 1.5. This reading reveals that stock values are average in relation to house prices. The February 2009 reading of 0.77 marked the low for this cycle as well as the beginning of Supercycle 6.

See *The Science of Making Money in Turbulent Markets* for a complete explanation of the SoundAdvice Risk Indicator and its track record. (You received a copy of this book with your subscription, and you will also receive an updated copy when you renew your subscription.)



## Business Cycles and Stocks: The SoundAdvice Diffusion Indexes

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

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

To construct our SoundAdvice Diffusion Indexes, we observe changes in each of our selected indicators over a six-month period. For every indicator that is unchanged from its value during the six month span, we will attach a value of one half point (0.5). If an indicator falls below its level six months prior, it will be given a value of zero. If an indicator is higher than it was six months before, it is assigned a value of 1.0. The sum of all of these figures will be expressed as a percentage of the total number of indicators. If, for example, one indicator is up (+1) at the end of a six-month period, one is unchanged (+0.5), and one is down (0), the diffusion index will be (1.5)/3 or 50 percent.

When the SoundAdvice Diffusion Index of Leading Indicators drops to zero, it is time to buy stocks aggressively, regardless of how negative the atmosphere may be. This is not just an empirical coincidence. It is also logical. In order for all of the leading economic indicators to be giving off a zero value compared to six months before, it is nearly certain that the economy as a whole must be very soft, which is the atmosphere necessary to produce a lasting decline in interest rates.

**The Diffusion Index of Leading Indicators:** As far back as February and March 2009 we were projecting that our Diffusion Index of leading indicators soon would hit zero and mark an important buying opportunity. We made that projection by assuming that the leading indicators would not improve in the current economic environment. In fact that signal arrived in March, very close to the bottom, officially giving us an "Aggressive" signal. The market subsequently climbed 61 percent.

An "Aggressive" signal coming at a time when the Risk Indicator was below 1.0 revealed that Supercycle 5 came to an end, and that Supercycle 6 was born.

**The SoundAdvice 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 which reveals that the economy is about to put upward pressures on interest rates. This index hit 100% in March (reported in April), telling us to move to a cautious approach. This signal came very close to the 2012 peak of the market.

Our next signal will come from a zero reading from our Diffusion Index of Leading Indicators. The latest reading for June was 66.7 percent.

Last month we mentioned that we would see an aggressive signal soon if the individual leading indicators that make up our Diffusion Index of Leading Indicators remained at last month's levels. However, do to significant increases in all of the leading indicators, we will not see a new signal in the months ahead unless the leading indicators (as the economy) show renewed weakness.

### Track Record of the SoundAdvice Diffusion Indexes

If we had followed the signals from our Diffusion Indexes over the years, we would have done very well indeed. The results are shown below. After each "Aggressive" signal, the S&P 500 climbed an average of 34.4 percent. During "Caution" signals, the S&P 500 declined an average of 1.1 percent.

Aggressive	S&P	Caution	S&P
Sep-74	68.1	Apr-76	101.9
Jul-76	104.2	Dec-76	104.7
Oct-78	100.6	Jun-79	101.7
Nov-79	100.0	Oct-83	167.7
Aug-84	164.5	Jun-85	188.9
Jul-86	240.2	Aug-87	329.4
Feb-88	258.1	Jun-88	270.7
Mar-89	280.0	Mar-93	449.7
Mar-95	493.2	Dec-98	1,141.0
Jun-00	1,429.4	Dec-00	1,320.3
Jun-03	974.5	May-05	1,191.5
Jun-06	1,276.7	Mar-08	1,325.4
Apr-09	848.2	Mar-12	1,370.3
Ave +/-	34.4%		-1.1%

See *The Science of Making Money in Turbulent Markets* for a complete explanation of the SoundAdvice Diffusion Indexes and their track record. (You received a copy of this book with your paid subscription, and you will also receive an updated copy when you renew your subscription.)

The rising swell of home foreclosures began in 2007 as a symptom of faltering real estate markets across the country. But as the swell turned into a tidal wave, falling real estate prices have compromised the assets of the US banking system and the fabric of the US and worldwide economies. Indeed, the state of the nation's real estate markets and the economy have become one and the same. We cannot have a sustainable recovery in the economy without the removal of the bulk of foreclosed homes overhanging the market.

We have seen all this before. It was back in the 1980s. After years of loose and questionable lending practices, regulators were forced to liquidate hundreds of savings and loans and dump their foreclosed real estate onto an already-depressed real estate market. As values dropped, the downward spiral continued until most of the real estate was sold at steep discounts. The crash was worse in some parts of the country, but the damage to the whole US economy was substantial. Does this sound familiar?

We have the same situation today. It's like the old good news/bad news jokes, except this is no laughing matter. The bad news is that today's crash has been damaging to both real estate prices and the national economy.

The good news is that we have the tools to determine when the bad news will be over. This will give us a tremendous opportunity not only to invest in real estate for pennies on the dollar at the right time, but also in other investments as well as those that benefit from a recovering economy.

### The Key Indicator

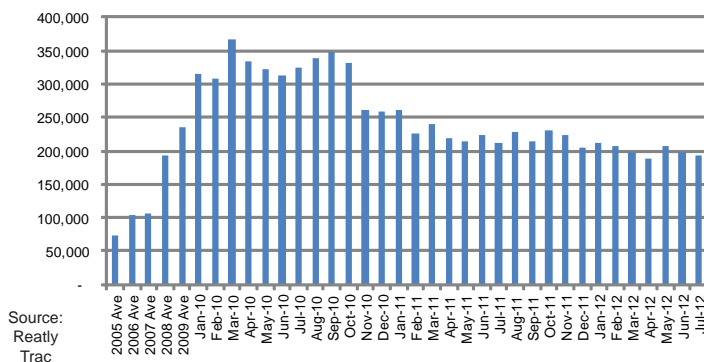
The secret is to focus on foreclosure rates. Realty Trac in Irvine, California has an extensive database. You can access foreclosure information on local markets from their website [www.realtytrac.com](http://www.realtytrac.com). We use some of their data here to gauge the state of the nation and its real estate, and plan to continue to do so in future issues of SoundAdvice.

What we are looking for is a significant decline in the number of foreclosures. When this happens, the bulk of the overhanging inventory of foreclosed properties will have been digested, and the real estate recovery can then begin as well as in the economy. In the late 1980s, this was the best indicator for knowing when the recovery was near. As foreclosure rates dropped, the ensuing recovery began. For nearly two decades, fortunes were made from real estate purchased for pennies on the dollar during the S&L Crises of the 1980s.

The following chart shows US foreclosure rates. In 2005, foreclosure rates averaged 74,892 properties per month. In 2006 and 2007, foreclosures were slightly above 100,000 per month. However, by January 2010, foreclosures climbed to over 300,000 per month, and foreclosures continued at over 300,000 each month through October.

We saw the beginnings of a decline in the 2010 fourth quarter. At first, the decline was due largely to a freeze in foreclosures by several major lenders. The downtrend continued as Federal and state foreclosure prevention efforts allowed distressed homeowners to stave off foreclosures. However, foreclosure rates remained abnormally high.

### US Foreclosure Rates - Monthly Averages



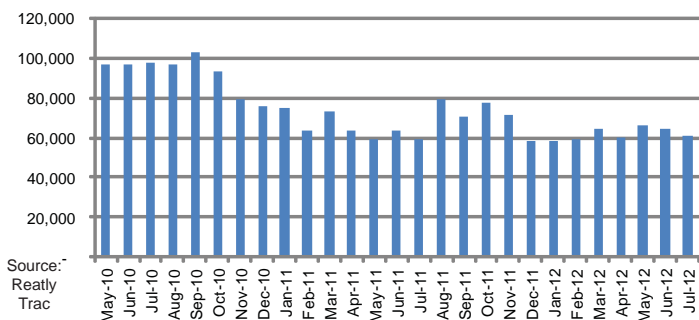
### Dissecting the Foreclosure Process

It's important to keep in mind that the foreclosure process is comprised of three distinct stages: new default filings by lenders; then auctions as lenders attempt to sell these properties; and finally, bank repossessions of those properties not sold through auctions. The sheer number of foreclosures is actually the aggregate of the number of properties in each of these three stages.

We can get an early glimpse of a change in trends by focusing on changes in the first step of the foreclosure process: new default filings. After all, a significant change in the first step of the foreclosure process must ultimately lead to a significant change in the aggregate number.

The following chart shows new default filings in the US by month since May 2010. Through October 2010, new default notices were hovering around 100,000 per month. In November 2010 they began declining but have remained stubbornly high during the last several months.

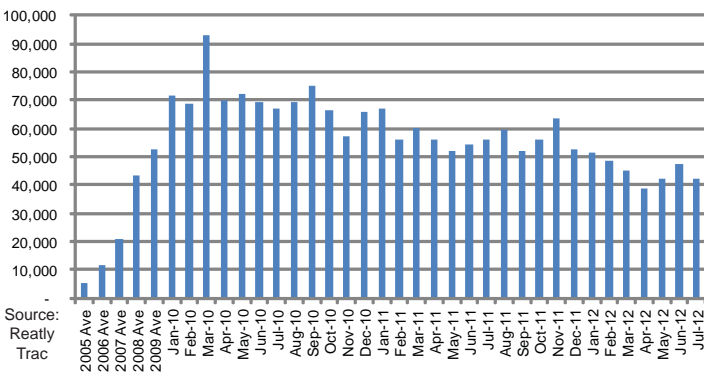
### US New Default Notices



One fourth of the nation's foreclosures have been in California for the last few years. The following chart shows all stages of the foreclosure process in California (including auctions and bank repossessions).

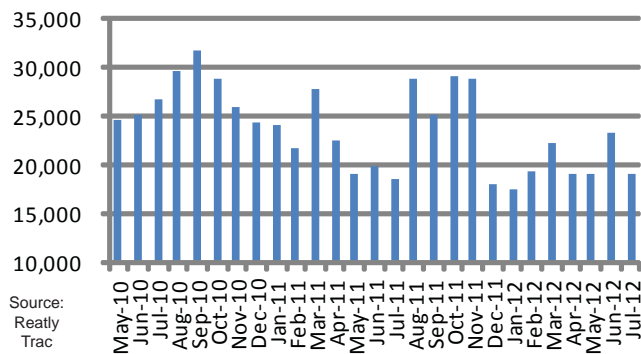
In 2005, California foreclosures averaged 5,138 properties per month. Foreclosures doubled in 2006, and again in 2007, and again in 2008. By 2010, foreclosures were close to 70,000 each month, with a spike of 93,000 in March. Foreclosure rates remained high in 2011 and began modest declines during the first five months of 2012. However, there has not been much of an improvement since.

California Foreclosures - Monthly Averages



The following chart shows new default notices in California. After declining somewhat earlier this year, new default notices rose sharply in June by 22 percent and then dropped by an equivalent amount in July.

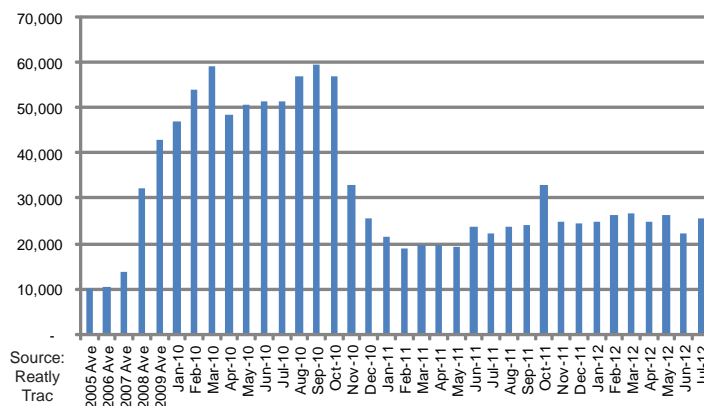
California New Default Filings



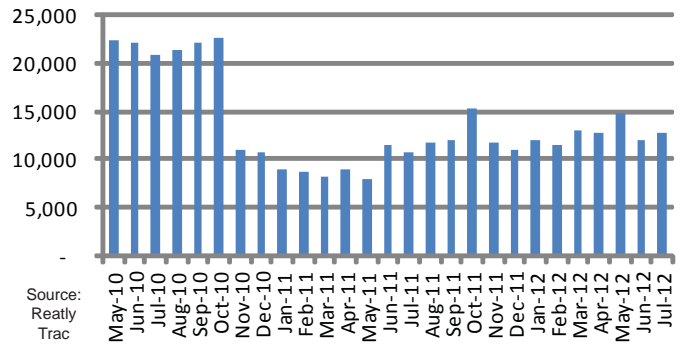
Florida is the next highest foreclosure state with 11 percent of the nation's foreclosures. See the chart below. Foreclosure rates climbed from 10,000 per month in 2005 and 2006 to 47,000 in January 2010, and stayed in the 50-60,000 range through October. After dropping sharply in late 2010 and early 2011, foreclosures have since remained above 20,000 per month.

The chart above shows new default notices in Florida

Florida Foreclosures - Monthly Averages



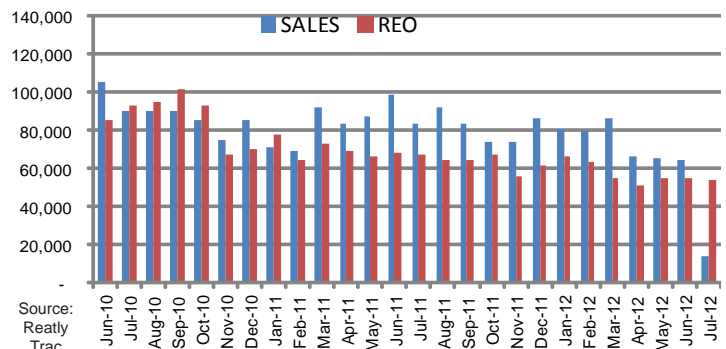
Florida New Default Filings



which dropped sharply in late 2010 and early 2011. They have since been uptrending. June saw a 19 percent drop but July saw a similar increase.

The Inventory

At the other end of the foreclosure process is what the banks have not been able to sell. This inventory is called "real estate owned", or REO for short. Each month more REO is added to the inventory. However, each month there are a number of properties sold from the inventory. Below is a chart of the REO (in red) and sales (in blue) since June, 2010.



On balance, there have been 267,568 more properties sold than have been added to the REO inventory, or 17.9% of the current inventory of 1,497,222 foreclosure properties listed for sale.

Conclusions

The latest national readings for July show that new default filings nationally were essentially unchanged. The drop in California bodes well for 25% of the inventory. However, we will need to see more declines before we can count on a trend. The spike in Florida is not encouraging. On balance, the mixed results do not point to a significant drop in foreclosure rates in the immediate future.

We will be tracking foreclosure metrics closely both nationally and in key states in these pages of SoundAdvice to be among the first to know when the end of the foreclosure crisis is at hand. Stay tuned.

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