



The *Sound Advice* portfolio is up 25.7 percent so far this year, assuming an equal amount was invested in each position at the beginning of the year. If we look back to the beginning of last year, the portfolio is up 52.8 percent. We have an average gain of 65 percent based on the prices at which each stock, ETF, or mutual fund was originally recommended.

We have several action items this month. We are selling **Comcast (CMCSA)** along with **Masco (MAS)**. We are also selling **CGM Real Estate Fund (CGMRX)** and replacing it with a fund that is having a stellar performance and is bound to bring us better investment returns. The rationale and details regarding these moves are discussed in detail in this issue.

-Gray Emerson Cardiff

The Best Real Estate Fund

Choosing the best real estate mutual fund is not easy. There are 15+ no-load real estate funds from which to choose, and sorting them out is a project. We have done that recently, and here are the results.

The first question is: Why invest in a real estate mutual fund, and why now?

Most of the time, above average investment returns can be earned. So far, the current year happens to be an exception. However, over the last 10 years, real estate funds have outperformed the S&P 500.

Therefore, just finding the average real estate mutual fund will likely bring you investment returns that are superior and more reliable than the stock market over the long run. Moreover, at certain times, investment returns are exceptional from real estate funds, especially the funds that perform consistently better than the averages. We believe the months immediately ahead will be one of those times.

The Big Cycle

We all know about business cycles and their impact on investments. However, the business cycle is particularly powerful on real estate because financing is typically employed. Not only does financing introduce leverage, but its availability and cost can either starve the market or pump it up. Often these cycles are long and span a generation, so the majority of investors do not remember or know about them.

The best time to invest in real estate is after it has crashed and has begun to recover. At these times, lenders are nervous and they are just beginning to lend again, albeit very carefully after having been burned by loose policies prior to the crash when values were high. Also at these times, with lending shut off as a result of the crash and the economy is in the tank, there has been no significant

development of new properties for several years. As the economy recovers, shortages in supply start to appear, and rental rates begin to escalate. As memories fade and lenders relax their grips on their growing stashes of money, liquidity returns to real estate, and we are off to the races again. Over the span of many years, real estate prices recover steadily and handsomely.

During the economic expansion, the investment returns are excellent. First, for each 5 percent increase in rental income, net operating income (after operating expenses) increases by a larger percentage, from 7 to 10+ percent, depending on the type of real estate and level of expenses, because expenses are relatively fixed. Since the value of the real estate is measured by the net operating income, the value goes up sharply.

Not to get bogged down in too many numbers, but a brief illustration is important. A property with, say, \$15,400 in rental income and operating expenses of \$5,390 (35 percent of income), would have an annual net operating income of \$10,010. Today, capitalization rates are around 7 percent, which puts the value of the property at \$143,000 ($\$10,010/0.07$). Let's say the mortgage is \$75,000 (approximately 50 percent of value), which leaves an equity of \$68,000.

Now, let's raise the rent by merely 5 percent. Assuming expenses stay the same, the net operating income increases to \$10,780. At a 7 percent capitalization rate, the property is worth \$154,000. Subtracting the mortgage leaves equity of \$79,000. Note that this is a growth in equity of 16.2 percent, all from a mere 5 percent increase in rental income.

This simple example illustrates why commercial real estate can do so well during even a modest recovery; why real estate mutual funds are especially good during the expansive phase of the business cycle.

Which Fund is the Best?

During the last 10 years, the **CGM Real Estate Fund (CGMRX)** has had the best return of all funds with an annual return of

Annual Returns of Real Estate Funds

Fund Name	Symbol	10 Year	5 Year	3 Year	1 Year	YTD
Third Avenue Real Estate Value Institutional	TAREX	8.74	6.45	14.57	18.11	7.49
Third Avenue Real Estate Value Investor	TVRVX			14.30	17.83	7.32
Forward Real Estate Investor	FFREX	7.73	4.48	10.97	8.10	4.72
Vanguard REIT Index Investor	VGSIX	9.76	6.77	12.00	6.85	4.01
Cohen & Steers Realty Shares	CSRSX	10.75	7.12	10.93	6.80	4.15
Managers Real Estate Securities	MRESX	10.73	7.72	11.66	6.35	3.63
DFA Real Estate Securities I	DFREX	9.52	6.48	11.91	6.33	3.41
ASTON/Harrison Street Real Estate N	ARFCX	9.31	7.03	12.58	6.22	2.53
Fidelity Real Estate Investment	FRESX	9.66	7.62	12.17	6.12	3.50
CGM Realty	CGMRX	14.97	3.24	9.16	5.83	4.92
Morgan Stanley Inst US Real Estate P	MUSDY	10.17	5.62	10.26	5.72	2.99
SSgA Clarion Real Estate Institutional	SSREX	8.81	3.31	11.02	4.79	2.46
American Century Real Estate Investor	REACX	8.89	4.56	12.95	4.72	2.09
Alpine Realty Income & Growth Institutional	AIGYX	7.54	7.51	11.83	4.57	2.55
ProFunds Real Estate UltraSector Investor	REPIX	3.70	(2.20)	12.78	4.30	1.61
Neuberger Berman Real Estate Trust	NBRFX	11.27	8.08	10.46	4.05	0.85

14.97 percent through late September. That is the principal reason we have had it in our model portfolio. However, like most REITs, it has not done well over the last year.

The largest REIT mutual fund, the **Vanguard REIT Index Investor Fund (VGSIX)**, is designed to represent the average of all real estate investment trusts (REITs), and it is the benchmark of the industry. Over the last 10 years, it has earned an average annual return of 9.76 percent. During the last year, it has returned 6.85 percent.

In our continual quest to find the best investments possible, we surveyed the real estate mutual fund industry again to see if there would be a better investment. The table above summarizes our results for the annual investment returns for 16 real estate mutual funds over the last 10 years, 5 years, 3 years, 1 year, and year-to date (YTD). The funds are ranked based on their performance during the last year.

Twelve of the funds did not do as well as the **Vanguard REIT Index Investor Fund (VGSIX)**. However, only three funds did better, with the Third Avenue Real Estate Value Funds leading the pack by a substantial margin, especially during the last year. Third Avenue also lead the pack YTD as well as for the last 3 and 5 years.

The top fund, the Third Avenue Real Estate Value Institutional Fund (TAREX), requires a \$100,000 minimum investment. However, the **Third Avenue Real Estate Value Investor Fund (TVRVX)** only requires a \$2,500 minimum investment and has had returns within a whisker of the Institutional Fund since its inception on 12/31/2009. In fact, both funds share the same portfolio. The primary difference is that the Investor fund has slightly higher expenses than the Institutional fund at 1.34 percent per year versus 1.09 percent. Because the Investor Fund at a \$2,500 minimum is

more bite size, and the differences are negligible, we basing our recommendation on it rather than Institutional Fund.

The Third Avenue Management

Third Avenue has a seasoned team of managers. Co-lead manager Michael Winer has headed the management of the Real Estate Value funds since their inception. Prior to taking the lead role, he was a real estate securities analyst at Third Avenue and with extensive experience in the real estate industry before joining Third Avenue.

After serving as a senior analyst for more than six years, Jason Wolf became co-manager in 2010, and became co-lead manager in January 2013 alongside Mr. Winer. Also on the team is senior analyst Ryan Dobratz since 2006.

These managers and their analysts expend great effort visiting prospective companies and their properties, and assessing property management teams, along with analyzing financial statements in order to determine intrinsic values.

All three managers invest in the fund. Mr. Winer has more than \$1 million invested, while Wolf and Dobratz own between \$100,000 and \$500,000.

The Third Avenue Investment Approach

Although past results are not a guarantee of future results, they are an indication of management's competence and the success of their approach to selecting stocks.

For all of the Third Avenue Funds, management looks for 4 fundamental characteristics before they make investments:

- 1) The issuer has an especially strong financial position.
- 2) The common stock is selling at a price that reflects at least a 20% discount from Net Asset Value ("NAV").

3) There is comprehensive disclosure including reliable audited financial statements; and the common stock trades in markets where regulations provide substantial protections for investors.

4) The prospects are that over the next three to seven years, NAV will be increasing by at least 10 percent annually (including dividends).

One of the REITs that meets this criteria is Commonwealth REIT (CWH) which is owned by the Third Avenue Real Estate Value Funds. We have had CWH in our portfolio for the same reason – a steep discount to NAV. Third Avenue became interested when activist investors Corvex Management and Related Fund Management began their proxy fight to oust the management, and views the investment as a “risk arbitrage situation”. Third Avenue management believes that the activists are likely to be successful, in which case there might be a 60% or greater gain over 18 to 24 months.

The Fund’s management team also become activists at times. For example, Forest City Enterprises, the largest portfolio holding, climbed significantly after Third Avenue management actively persuaded the management of Forest City to make improvements.

Recent Additions

In the recent REIT sell-off, Third Avenue purchased Post Properties as it traded near its 52-week low. The drop allowed the fund to establish its position at a substantial discount to NAV of the high-quality apartment portfolio in high growth markets.

Tanger was also added, an REIT with a leading position in factory outlet centers which have been well occupied with strong rental rates due to the value offered to customers. Over the last 5 years, Tanger’s centers have averaged 97 percent occupancy with rental rates growing 15 percent annually. Tanger has a strong balance sheet in the retail sector with debt equal to only 30 percent of assets.

Hersha was also added at a significant discount to NAV, a REIT with 64 high-quality hotels in urban areas with barriers to entry for competitors. Hersha has limited service hotels which have higher profit margins and less volatile cash flows than full service hotels, along with having more flexibility to adjust room rates as economic conditions change.

Brookdale was also added at a significant discount to NAV, the largest operator of US senior housing centers for those who are generally in good health but require a base level of health care. Brookdale’s portfolio is currently leased at 88%, which is only 6% below the pre-crisis peak. Pent-up demand and an aging US population is bound to drive up occupancy and lead to strong NAV growth as seniors often use proceeds from home sales to move in and pay rent.

The Fund’s management believes that these four additions meet their four investment characteristics. In addition, because of their niche assets and business strategies, each company is an attractive takeover candidate.

REOCs versus REITs

Management also emphasizes real estate operating companies, or REOCs, which unlike REITs, are not forced to pay out nearly all of their net income in distributions. With the ability to retain cash, REOCs can develop properties and capture profits from the difference between construction costs and completed market values.

TARP Warrants

As an example of management’s value oriented but also creative approach, earlier in the year Third Avenue management invested in TARP warrants. These are 10-year options that were issued by banks to the US Treasury in return for capital infusions during the 2008-09 financial crisis as part of the Troubled Asset Relief Program (TARP). To recoup part of its investment, the Treasury recently sold these warrants which now trade publicly with 5 to 6 years of life remaining on them.

Third Avenue bought the warrants on PNC Financial Service for the Real Estate Value Funds. The rationale was that this strong bank will benefit from rising loan demand as real estate recovers, as well as increasing interest rate margins as interest rates rise during the economic recovery. This lines up with the rationale behind our “No-Brainers”.

The PNC (PNC/WS) warrants allow for the purchase of PNC common stock at \$67.33 until 12/31/2018. At the time of Third Avenue’s purchase, the common stock was trading at that price which was also close to the book (liquidation) value per share. The warrants were purchased for \$11.

PNC stock is currently \$73.5 and the warrants are close to \$16. At the time of the purchase, the base-line projection was that book value will grow at a minimum of 8 percent per year, which would provide an annual investment return from the warrants of 25 percent during each of the next 5 years. If the stock price expands to just 1.5 times book value, which is still conservative, the return climbs to 41 percent annually. So far, the strategy is proving to be on the right track.

In Front of the Herd

Whether investing in REOCs, REITs, or TARP warrants, or any real estate-related investment, Third Avenue management focuses on value and discounts to NAV. This means they are investing in companies when they’re out of favor.

This approach is contrary to most mutual fund managers who are following the herd (or are the herd). That is why the investment returns of Third Avenue Funds are often sharply different from their peers. From our table, we can certainly see the difference during the last five years. With its unique and value-oriented approach, superior performance is bound to continue.

Accordingly, we are replacing the **CGM Real Estate Fund (CGMRX)** with the **Third Avenue Real Estate Value Investor Fund (TVRVX)**.

The History of 30-Year Treasury Bond Yields



This graph shows the yields of 30-year Treasury bonds since 1977. As you can see, yields are still close to historic lows.

Source: Yahoo! Finance

Our “No-Brainers”

Our “No-Brainers” are ETFs designed to benefit from rising long-term Treasury Bonds. We have dubbed these ETFs as “No-Brainers” because interest rates always rise after a recession during the recovery. It is as simple as that.

Congressional wrangling and concerns over the debt ceiling are here again. Although we have become somewhat desensitized to all of this, the uncertainty is casting a pall over the markets, which is likely to continue through the mid-October deadline.

Uncertainty causes a flight to safety where investors move their money into investments that are perceived to be safe. Such investments still include Treasury bonds, even though yields are still historically low. We have included the chart above of 30-year Treasury bond yields, as we do from time to time, to illustrate the historical context in regard to where yields are today.

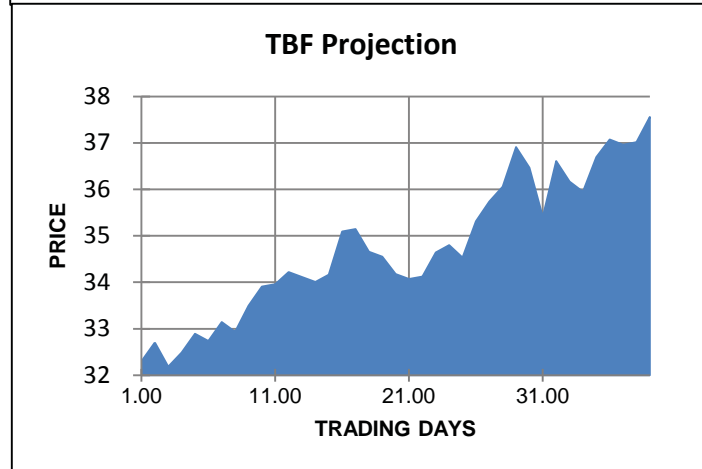
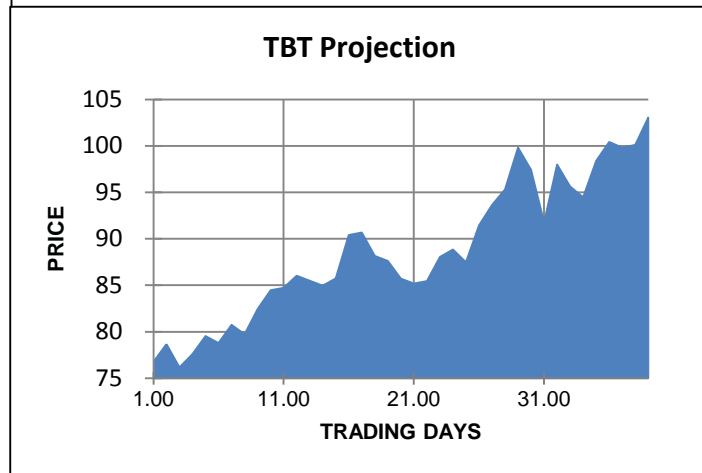
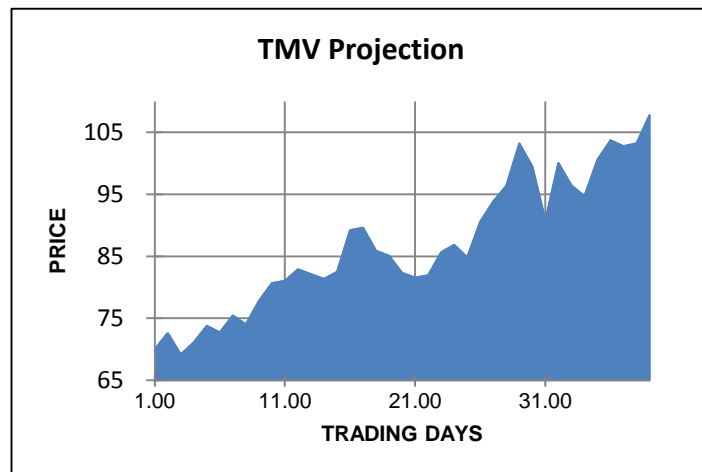
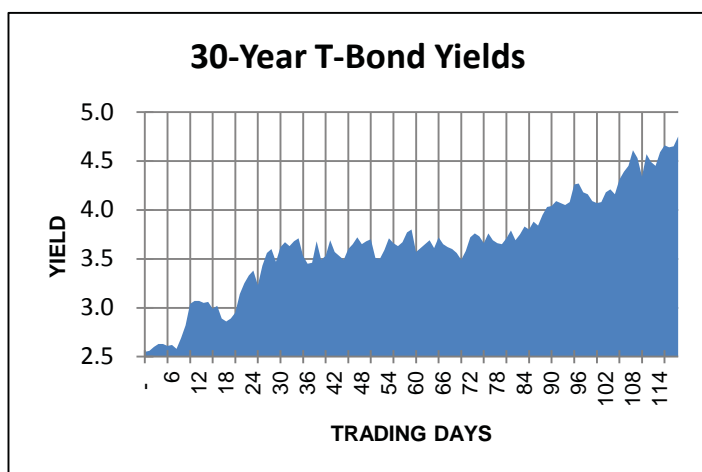
The Federal Reserve’s September 18 decision to delay tapering its bond-buying programs was unexpected, and the announcement also contributed to downticks in Treasury bond yields. Since our last issue, 30-year Treasury bond yields declined from 3.71 to a low of 3.67 percent, but have since inched up slightly. As long as political blustering and the threat of a government shutdown continues, Treasury bond yields are likely to remain in this range barring any extraordinary economic news.

However, looking beyond these near uncertainties, it is important to keep the big picture in mind. By delaying tapering, the Federal Reserve is telling us that it will stoke the economy until the recovery is firmly on track. That is the best possible scenario for our “No-Brainers”. The delay in tapering means the recovery will be more robust and ultimately force bond yields higher.

The underlying strength in the economy can be seen in the recent readings from the **The SoundAdvice Diffusion Index of Leading Indicators** (see page 11) which clocked in at 100 percent again in August, for the sixth consecutive month in a row. In fact, except for March with a reading of 67.7 percent, 100 percent readings have been recorded every month since December 2012. We have been tracking this index since the early 1970s, and at no time has a string of six consecutive 100 percent readings occurred. Clearly, the recovery is already inexorable, and is being fueled by the continuation of the Federal Reserve’s massive continued bond-buying.

The most recent time long-term Treasury bond yields rose significantly was from December 18, 2008 to June 10, 2009, (118 trading days) when 30-year Treasury bond yields rose from 2.55 percent to 4.75 percent, or 220 basis points. The pattern of this rise is shown on the following chart.

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Our No-Brainer ETFs did not exist during this entire period, so we don't have historical track records to view. However, we know how these ETFs work, and can model them to get an idea of the profit potential.

The price action of these ETFs is based on the changes in long-term treasury bonds, specifically BlackRock's iShares 20+ Year Treasury Bond ETF (symbol TLT) which holds a portfolio exclusively of long-term Treasury bonds with an average maturity length of 27.5 years. The prices of our No-Brainer ETFs fluctuate in accordance with the daily fluctuations of TLT, only in the opposite direction, multiplied by the leverage each uses. For example, a decline of say, 1.0 percent in TLT will cause TMV to increase by 3.0 percent, TBT by 2.0 percent, and TBF by 1.0 percent. Conversely, an increase in TLT will cause our No-Brainers to drop in the same fashion.

To construct our models, we start with a projection of an increase in 30-year Treasury bond yields. A conservative approach would be to assume that long-term Treasury bond yields will not rise beyond 4.75 percent -- not any higher than the last peak. We can use the pattern of the last 38 days of the 220 basis point rise when yields rose from today's yield of 3.68 percent to the peak of 4.75 percent. In that scenario, our No-Brainers would rise to the following levels:

- TMV** would climb to \$107, for a 57 percent gain.
- TBT** would climb to \$103, for a 37 percent gain.
- TBF** would climb to \$37.5, for a 17 percent gain.

See the charts on the right which display these projections.

While the pattern of today's rise is unlikely to be exactly the same as the previous rise, we believe this projection serves as a minimum expectation. After yields rose to 4.75 percent on the last rise, the economy was considerably weaker than it is today and went into a decline. However, this time it is likely that bond yields will be marching substantially higher in view of many years of stimulus from the Federal Reserve, and the inevitability of the end of its quantitative easing program. When that happens, the Fed will start tapering its bond buying, and ultimately start selling off its massive portfolio of Treasury bonds. Accordingly, it is not unreasonable to assume the current upswing in long-term Treasury bond yields will not end at 4.75 percent.

Portfolio Updates

Here are updates on the rest of our recommendations in alphabetical order. The table on page 9 details our buy limits and other information on each recommendation, and organizes them by investment objective. Also see our website for live pricing.

Agrium (AGU) is down 15 percent this year, trimming our profit to 620 percent. AGU has a broad mix of agricultural products and services that are poised to benefit from a growing need as arable land continues to disappear around the world and the need for higher food production per acre

is needed. Growth is also fueled by an expanding worldwide population and growing per-capita income exerts demand for crops.

At less than 10 times earnings, AGU is an excellent value with promising growth ahead from a broad array of agricultural products and services. In September, AGU announced plans to raise its common stock dividend by 50% to an annualized \$3 per share.

AMN Healthcare (AHS) is up 21 percent this year, extending our profit to 164 percent. AMN Healthcare provides temporary healthcare staffing services to the healthcare industry, ranging from nurses to physicians. We recommended this stock at an average price of \$5.35 based on the rationale that it was a two-fer. AHS was 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 healthcare business which will benefit from a recovery in the economy.

As the stock advanced and its price/earnings (P/E) ratio expanded, ultimately climbing over 25, we recommended holding off on purchases. The stock price still remains above our upper buy limit.

Associated Estates Realty Corp (AEC) is down 9 percent this year trimming our gain to 7 percent. In recent months we have noted AEC has been reducing debt and diversifying into California, both of which are certain to benefit the bottom line.

This continues to be the most undervalued apartment REIT in the sector. The net equity of its apartment portfolio translates into a stock value of \$27 per share. So the stock is still trading at a steep discount. It pays a nice yield as well.

Boston Scientific (BSX) is up 101 percent this year. BSX's medical products are well suited for an aging population in the US as well as emerging markets around the world, especially in India, China, Brazil, and Russia. Emerging markets only accounted for 4 percent of revenue in 2012, so there is considerable room for growth.

In September, BSX opened its first Chinese branch in Shanghai of the Boston Scientific Institute for Advancing Science (IAS) as well as its new Innovation Center. Through these facilities, BSX will foster local talent to develop new technologies uniquely suited to the China market.

Chesapeake Energy (CHK) is up 57 percent this year giving us an equivalent gain since we added it to the portfolio last year. CHK is the second largest producer of natural gas and pioneered the use of fracking technology to produce oil and liquids from shale. We added CHK to the portfolio because it was cheap. It was suffering from 3 primary problems, all of which were temporary or could be remedied.

The temporary problem was low natural gas prices which have since nearly doubled. Poor corporate governance was another problem. Shortly after we recommended CHK, Carl Icahn purchased a substantial stake and was instrumental in changing the corporate governance by removing the founder, Aubrey McClendon, as chairman of the board and replacing several other board members. Doug Lawler officially took over as CEO in June, coming from Anadarko Petroleum and its predecessor Kerr-McGee. In August, as part of

the reorganization and effort to reduce expenses, Lawler announced that four more top executives are leaving the company. In September, substantial layoffs were announced.

The third problem was that the company was suffering from a financial squeeze. In September, the company announced that no more asset sales will be required.

With the financial squeeze and related distractions behind it, the company will be able to put more of its capital budget toward drilling and focus on improving production and revenue.

Comcast (CMCSA) is up 20 percent this year, extending our profit to 107 percent. We added CMCSA to the portfolio when it was cheap, and represented a good investment value. However, the doubling in price has made it expensive and vulnerable. **Accordingly, we recommend selling now and taking your profit.**

Commonwealth REIT (CWH) is up 37 percent this year since activists Corvex Management and Related Fund Management began their proxy fight to oust the management. These activists stated that they believe CWH is worth at least \$40 a share, and \$50 with better management.

The discount of the price of the stock to underlying value of this REIT's net real estate assets has been the primary reason for our recommendation. Based on the company's recently released second quarter financials, we evaluated the value net equity of the company's real estate by applying an 8 percent capitalization (cap) rate to the net operating income of the real estate, and determined the net assets translate to \$40.35 per common share.

In June, Corvex Management and Related Fund Management announced they had consents from holders of over 70 percent of the outstanding shares approving their proposal to remove the entire Board of Trustees. CWH management contested the validity of the consent solicitation, and the matter went into arbitration.

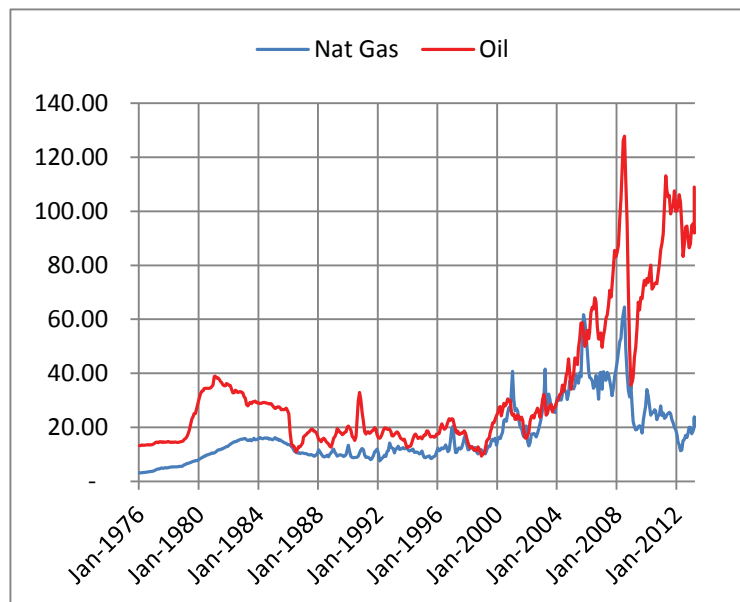
In August the arbitration panel struck down a rule recently adopted by management that only shareholders with at least 3 percent ownership for 3 years could seek changes to the company's board. The stock responded favorably to the news. The panel scheduled a hearing for further deliberations beginning on October 7.

We noticed that the managers of the Third Avenue Real Estate Value Funds, who are always on the prowl for discounts to net assets, recently increased their CWH position after adding 1.3 million shares earlier in the year.

Fidelity Select Natural Gas Fund (FSNGX) is up 20 percent this year which is close to our profit. This is the only mutual fund that concentrates on the natural gas industry, and a diversified play on the gap between the energy equivalents of oil and natural gas.

One barrel of oil provides approximately 5.8 million British Thermal Units (BTUs) of energy. One barrel of oil today is close to \$100, so that is the cost of 5.8 million BTUs of energy. On the other hand, with a market price for natural gas at \$3.50 for one million BTUs, 5.8 million BTUs will cost \$20.30 (5.8x3.50). So the same amount of energy is available for approximately 20.47

The Cost of Energy Equivalents of Oil and Natural Gas



cents on the dollar -- if it is in the form of natural gas.

To illustrate the point, we continue to display the historic relationship between the costs of these two forms of energy in the above chart because it demonstrates that today's disparity is not a normal situation.

The red line shows the price of a barrel of oil since the mid-1970s. The blue line shows the price of natural gas multiplied by 5.8 to approximate the same amount of energy contained in a barrel of oil. Note that for most of the time (36 years), the two forms of energy are closely aligned. This stands to reason. After all, energy is energy, and it should cost approximately the same regardless of the form in which it comes. However, that is not the case today.

The US is self-sufficient in natural gas with only 9 percent imported from Canada. At 20.30 cents 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.

Freeport-McMoRan Copper & Gold (FCX) is up 10 percent since it was recommended last month as a timely addition to the portfolio. We had a good ride during the recovery coming out of the previous recession with Phelps Dodge, earning 643 percent from March 2003 to December 2006. FCX subsequently purchased Phelps Dodge and now has those valuable copper assets, along with oil and gas, some gold, and other precious metals. The current recovery should bring good fortunes as well.

Hambrecht & Quist Life Sciences Fund (HQL) is up 33 percent this year, extending our profit to 109 percent. The most explosive profits in the entire healthcare industry can be found here in biotech companies. This is a volatile sector, so diversification is crucial. HQL is a superior way to gain exposure to biotech on a diversified basis.

ICON Energy Fund Class S (ICENX) is up 4 percent since

it was added to the portfolio a few months ago because the demand for energy accelerates with an economic expansion. The best time to invest is when the economy is coming out of a slump, before demand increases.

It takes energy to make everything, and especially large amounts to make the most vital materials and substances, such as chemicals, plastics, and to run data centers.

In addition, there is always the possibility of geopolitical disturbances threatening supplies and driving up energy prices.

Most energy mutual funds have not been able to match the performance of the Energy Equity Index. However, this fund not only beat the Energy Equity Index resoundingly, it has turned in the best performance – by far – of all energy funds. (See the April 1, 2013, Issue for a complete analysis of all no-load energy funds.)

Masco (MAS) is up 26 percent this year, extending our profit to 187 percent. We added MAS to the portfolio at \$7.49 after the shares got hammered during the recession. However, after the share price rocketed we put the stock on "Hold" because the price/earnings ratio got too rich, ultimately approaching 30 times earnings. The high price/earnings ratio is already anticipating a steep growth rate, and makes it vulnerable. **We recommend selling and taking your profit.**

Maxim Integrated Products (MXIM) is unchanged this year, leaving our profit at 52 percent. MXIM specializes in high-performance electronic chips that convert digital signals into analog format so that we can hear them. Such chips are in every cell phone. MXIM also makes integrated power management chips (PMIC) for portable devices makers to extend battery lives.

MXIM is in excellent financial health with more than \$1.5 billion of cash and plenty of cash flow to support operations. The investment and resources necessary to develop MXIM's analog chips, and the years it takes to develop them, is an entry barrier for new competition. Once developed, these chips have long and profitable product lives.

Pfizer (PFE) is up 15 percent this year, extending our profit to 75 percent. We added PFE to the portfolio when it became dirt cheap as the expiration date approached on its blockbuster drug, Lipitor. However, its future was brighter due to the arsenal of new pharmaceutical products. Pfizer is now poised to launch several blockbusters in cancer, heart disease, and immunology.

Pfizer is the world's largest pharmaceutical firm, with annual sales near \$60 billion. Pfizer's large size gives it economy of scale and the resources to finance the research and development of new drugs. It has more than 80 drugs in the development stage and 90 in the discovery stage.

Retail Opportunities Investment Corp (ROIC) is up 7 percent this year, extending our profit to 31 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.

ROIC buys distressed retail properties with high-quality demographics, refurbishes them, and then leases them at a premium. As new properties are added, along with tenant

upgrades, FFO is bound to continue to rise, along with the dividend, and push the price of this REIT upward.

Stryker (SYK) is up 23 percent so far this year, extending our profit to 63 percent. SYK is best known for its orthopedic devices: artificial knees and hips. SYK also provides a diverse array of innovative medical technologies, including reconstructive, medical and surgical, as well as neuro-technological and spine products.

More profits are assured by accelerating demand for joint replacements on aging US baby boomers. As life expectancies continue to increase, and obesity trends continue, more and more hip, knee, and spinal procedures will be needed.

SYK's purchase of Trauson Products earlier this year offers another source of substantial growth. Trauson is China's largest manufacturer of orthopedic implants where 194 million people are now over the age of 60, and whose numbers are climbing rapidly (expected to double by 2050). This demographic bulge is also gaining wealth, so the number of potential candidates is mushrooming. In addition to giving SYK access to the Chinese market, Trauson also broadens SYK's customer base. Trauson devices are generally purchased by lower-income hospitals that cannot afford Stryker's more expensive products. With the diversity of products, SYK can serve both of China's developing and developed areas.

As the economies improve here and elsewhere, revenue growth is bound to increase from the elective hip-and-knee surgeries. In addition, there were a significant number postponed during the recession and uncertain economic times that will become more affordable. Stryker's cash-rich balance sheet (with over \$2 billion in net cash) and robust cash flow, gives SYK multiple avenues for growth through mergers and acquisitions.

Symantec (SYMC) is up 31 percent this year, extending our profit to 48 percent. SYMC is the dominant supplier of software for computer security and protection against viruses and other nuisances through its leading flagship brand, Norton and its relatively new product "Norton Zone" allows users to safely access, sync, and share photos, videos and documents from any of their PC, Mac, Android, or iPhones and iPads.

Protection from cyber espionage is definitely a growth industry. There was a 42 percent surge in attacks during 2012. Mobile malware increased by 58 percent, and 32 percent of all mobile threats attempted to steal information, such as e-mail addresses and phone numbers. This year's data shows that cyber criminals aren't slowing down.

We added SYMC to our portfolio when it was cheap and when the company was suffering from operational inefficiency and lack of direction. Steve Bennett has since taken over

and has streamlined operations while giving SYMC stronger direction. The stock has advanced recently to the point where the valuation is a little too high. We have an upper buy limit of \$23 a share.

Tellabs (TLAB) is unchanged this year. TLAB designs and manufactures hardware and systems for the telecommunications industry. It is still trading below its net asset value.

The company's balance sheet at the end of its most recent quarter shows cash and equivalents of \$1.13 billion, which works out to \$3.14 per share. Adding in its other assets, including properties and equipment (less depreciation), but excluding the paper assets of Goodwill and Intangibles, TLAB's assets total \$1.42 billion, or \$3.95 a share. The company has no debt, but short-term liabilities total \$507 million, leaving net assets of \$912 million, or \$2.54 per share.

TLAB's fiber optical systems and products accounted for 41 percent of TLAB's total revenue in 2012. The company's fiber optical systems combine all of a building's communications networks into one, improving security and eliminating the need for future re-cabling. They save 80% of energy consumption over conventional copper wire Ethernet network systems in addition to saving up to 70% of the cost of ownership.

The recent alliance with Wesco's strong distribution network should be a substantial boost to sales and revenues.

We noticed that the shrewd management team at Third Avenue recently added 1.3 million shares of TLAB to their portfolios, after purchasing 1.9 million shares earlier

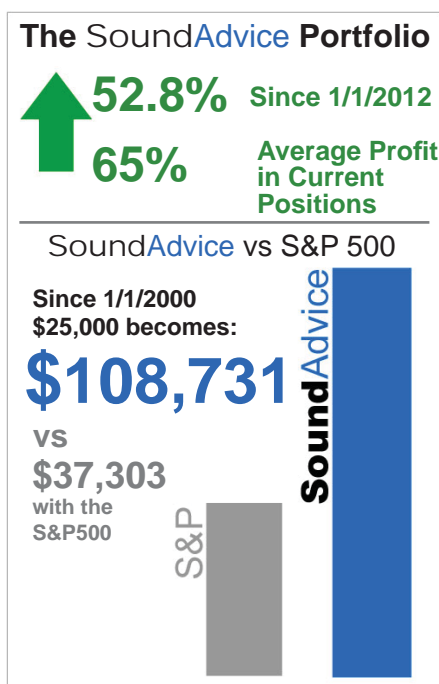
in the year.

Evidently, Third Avenue sees the same value we do. With the stock trading close to its net assets, there is very little downside risk. As profitability comes into focus, the market will anticipate a brighter day ahead and bid up share prices. Capital gain potential is very large from the current depressed price.

Tetra Tech (TTEK) is down 2 percent this year, trimming our profit to 68 percent. The stock price fell after one-time charges translated into disappointing earnings for the second quarter. We view the dip as a buying opportunity.

TTEK is a leading company in water technologies and environmental remediation with a healthy balance sheet and a backlog of approximately \$2 billion in signed contracts to clean up military bases across the US.

While there is plenty to clean up domestically, the greatest growth potential continues to be outside the United States in China and India, where environmental concerns have been an afterthought. Only now are these governments starting to recognize the consequences. As these and other governments around the world make this a priority, Tetra Tech should be a prime beneficiary. The board of directors recently authorized a



Income With Growth	Sym	Exchange	Price	Yield	Limit	Action
Associated Estates Realty Corp	AEC	NYSE	\$ 14.74	5.16%	\$ 16.00	BUY
CommonWealth REIT	CWH	NYSE	\$ 21.81	4.59%	\$ 25.00	BUY
Retail Opportunity Investment Corp	ROIC	NASDAQ	\$ 13.79	4.06%	\$ 15.00	BUY
Diversified Growth						
CGM Realty Fund	CGMRX	800-343-5678	\$ 30.65	1.57%	\$ 31.00	SELL
Comcast	CMCSA	NASDAQ	\$ 44.74	1.45%	\$ 40.00	SELL
Masco	MAS	NYSE	\$ 21.12	1.42%	\$ 15.00	SELL
Pfizer	PFE	NYSE	\$ 28.88	3.05%	\$ 30.00	BUY
Stryker Corp.	SYK	NYSE	\$ 67.65	1.26%	\$ 74.00	BUY
Third Avenue Real Estate Value Investor	TVRVX	NYSE	\$ 28.37	2.96%	\$ 32.00	BUY
Xerox	XRX	NYSE	\$ 10.37	1.64%	\$ 11.00	BUY
Energy/Natural Resources						
Agrium	AGU	NYSE/TSE	\$ 84.92	2.36%	\$ 95.00	BUY
Chesapeake Energy Corp	CHK	NYSE	\$ 26.21	1.34%	\$ 29.00	BUY
Fidelity Select Nat. Gas Fund	FSNGX	800-544-8888	\$ 37.07	0.15%	\$ 39.00	BUY
Freeport-McMoRan	FCX	NYSE	\$ 33.42	3.74%	\$ 37.00	BUY
ICON Energy Fund Class S	ICENX	800-435-5697	\$ 22.76	0.00%	\$ 25.00	BUY
Tetra Tech	TTEK	NASDAQ	\$ 25.98	0.00%	\$ 28.00	BUY
USAA Precious Metals & Minerals	USAGX	800-862-6909	\$ 15.42	2.88%	\$ 20.00	BUY
Aggressive Growth						
AMN Healthcare	AHS	NYSE	\$ 14.05	0.00%	\$ 12.00	HOLD
Boston Scientific	BSX	NYSE	\$ 11.52	0.00%	\$ 13.00	BUY
ETF - Direxion Daily 20+ Yr Bear 3X	TMV	NYSE	\$ 67.69	0.00%	\$ 79.00	BUY
ETF - ProShares Short 20+ Year Trsry	TBF	NYSE	\$ 31.99	0.00%	\$ 35.00	BUY
ETF - ProShares UltraShort 20+ Year Trsry	TBT	NYSE	\$ 75.12	0.00%	\$ 83.00	BUY
H&Q Life Sciences Fund	HQL	NYSE	\$ 19.36	0.00%	\$ 21.00	BUY
Maxim Integrated	MXIM	NASDAQ	\$ 29.49	3.26%	\$ 33.00	BUY
Symantec	SYMC	NASDAQ	\$ 24.73	0.00%	\$ 23.00	HOLD
Tellabs	TLAB	NASDAQ	\$ 2.28	0.00%	\$ 2.50	BUY

Prices are as of 9/27/2013. 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.

\$100 million common stock repurchase program.

USAA Precious Metals & Minerals Fund (USAGX) is down 42 percent this year as the price of precious metals suffered. Rising interest rates (as lead by rising bond yields) have strengthened the dollar which has adversely impacted all commodity prices. However, this is not a permanent situation.

When the economy gets more traction, the money created in recent years in the Federal Reserve's qualitative easing programs will be sloshing through the economy, putting upward pressure on the prices of commodities including precious metals. USAGX is the best diversified way to invest in precious metals. It is the top-performing fund in the sector, and has constantly out-performed precious metal equities for ten years.

Xerox (XRX) has climbed 52 percent this year. We have been recommending XRX because it has been transforming from a

seller of printers and copiers to a company providing services on those machines. The strongest growth should come from the company's expansion into information technology (I.T.) services, especially in the healthcare industry where technology is needed to reduce costs.

In September, XRX signed a 3-year, \$89 million contract to manage the medical bills for the Department of Labor's Office Worker's Compensation Programs. XRX also launched its Pharmacy Benefits Management Program with Healthcare Solution's Cypress Care division which is saving the insurer 33 percent on processing claims. The Department of Homeland Security awarded XRX a three-year, \$16 million contract in September.

At less than 10 times 2013 earnings, XRX is at a steep discount to the overall market and cheap in comparison to its competitors like IBM and Canon.

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 \$9,947,059 in stocks and to \$1,354,255 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 \$395,354,732, 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 1.60. This reading reveals that stock prices are slightly above 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 SoundAdvice 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. Our next signal will come from a zero reading from our Diffusion Index of Leading Indicators. The latest reading is 100 percent.

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, and to move to a cautious approach.

This has been a critical indicator in the past and has aided in avoiding severe declines, most notably the crash of 2008-09. However, since then, the Federal Reserve's Quantitative easing program has been holding short-term rates artificially low to stimulate the economy.

This index hit 100% in 2012 when the economy began to turn around, and marked the low-point of the long term Treasury bond yields. This indicator was instrumental in recommending our "No-Brainer" ETFs designed to profit from rising Treasury bond yields. We have continued to be bullish about stocks due to the Federal Reserve's extraordinary monetary policy which has been distorting the natural business cycle this time.

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 increased an average of 0.5 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%		0.5%

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.)

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