

SoundAdvice

Advising Investors for 30+ years

May 2019 Issue

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“Sell in May and Go Away”

Now that May is here, the above saying comes to mind, which is based on the belief that most of the stock market gains are earned from November through April, leaving May through October when the market is generally stagnant or declines. We updated our study on this topic to determine just how accurate this saying is.

We start with the daily closing prices of the S&P 500 since 1965. Each year the S&P 500 has averaged a 7.8 percent return, but to see if this return was seasonal, we divided each year into three segments: January through April, May through October, and November through December. The results are as follows: On average, January to April delivers the best results with a 4.2 percent return. May through October averages a scant 0.3 percent. The November-December period averages 3.1 percent.

To make the study more relevant to the current year, we can look at years when there was a strong rally in January through April, like we have had this year, with a rise of close to 17 percent. There are only 7 years since 1965 when the market averaged a 17 percent return from January through April. In those years, the S&P declined an average of 2.7 percent from May through October.

Accordingly, our study shows that it generally pays to “Sell in May and Go Away”, especially after a strong January to April rally which has extended the and made it more vulnerable.

Today’s market seems no exception. We can measure the market’s vulnerability by looking at the S&P price/earnings (P/E) ratio.

The trailing 12-month (TTM) earnings of the S&P 500 were \$152.30. With the S&P 500 index at 2,926, the TTM P/E is 19.21. This is close to the TTM P/E reached at the peak of the market last summer of 19.37. The average since the bull market began in 2009 has been 17.52.

The TTM P/E is substantially higher than at the



Gray Emerson Cardiff, Editor

So far this year, the *Sound Advice* model portfolio is up 13.2 percent.

The *Sound Advice* investment returns in prior years have been calculated independently by the Hulbert Financial Group and concur with ours. They are as follows:

From 2000-2018
9.5% Annually versus.
2.8% from the S&P 500

peak of the previous bull market when it was 17.09 at the end of the third quarter of 2007. During that bull market, the TTM P/E averaged 17.48.

Accordingly, the market is extended and vulnerable by TTM P/E historical standards. The S&P P/E ratio is well above average and even higher than at the peak of the last bull market. The market is also vulnerable according to the Sound Advice Indicators. Our *Sound Advice* Diffusion Index of Lagging Indicators (page 11) gave us a new Caution Signal. Subsequently, our *Sound Advice* Risk Indicator (page 10) climbed over 2.0 in July 2018, revealing a high-risk time for stocks.

The Portfolio

We continue to recommend that you keep a substantial amount of cash on the sidelines. Our portfolio recommendations are made regarding the money you have allocated to the stock market, and in accordance with our current cautionary mode. We believe that they are exceptionally strong values; trading at a significant discount to the rest of the market, which should give them buoyancy in both good and bad market conditions over the longer term.

As long as we are in a Caution Mode, we continue to recommend hedging your portfolio.

ProShares UltraShort S&P 500 (SDS)

essentially short-sells the market and will benefit from down-drafts in the S&P 500. It is designed to produce two times the daily fluctuations of the S&P

500 index. A decline of say, 1.0 percent in the S&P 500 will cause SDS to increase by 2.0 percent. Conversely, an increase in the S&P 500 will cause SDS to decline in the same fashion. We have been tracking SDS and confirmed that it is performing as it should, with daily premiums and discounts within 0.5 percent. It is also very liquid.

Energy & Natural Resource Selections

In April, the Trump administration eliminated the waivers from sanctions against Iran. Effective at the beginning of May, the sanctions are back on. Oil prices spiked on the news until Saudi Arabia was urged to fill the production void. Of course, the Saudis agreed, but it still needs at least \$70 a barrel to support its public spending.

The US became a net exporter of oil late in 2018, which will also support oil prices. We are still importing nearly half of our oil needs because most US refineries were constructed prior to the US shale boom and designed to process imported crude oil which is a heavy (thick) and sour (high sulfur) grade. Additionally, refineries on the east and west coast do not have access to the US crude oil pipeline network, so they must rely on imported oil arriving in US ports for their supplies. Meanwhile, US storage tanks in Cushing, Oklahoma, are brimming with the light sweet crude fracked from US shale which is now available for exporting.

All of these cross-currents point to choppy but generally level energy prices in the foreseeable future.

Adams Natural Resources (PEO) is a candidate for steady income. This fund has been in operation since 1929 and has 80+ years of distribution history. PEO has an objective and recent history of making quarterly distributions that add up to at least 6 percent annually. These distributions are usually a mix of dividends and long-term capital gains.

This is a closed-end fund, which means it

trades like a stock and can be bought and sold during market hours. The price of PEO is not tied directly to the NAV of the underlying portfolio, so it can trade at a discount or a premium. This is an advantage now because PEO is currently trading at a substantial discount to its NAV. Although PEO has typically traded at a discount over the last several years, the discount now is as large as it gets, at 16.9 percent. In addition, PEO also has a lower expense ratio of 0.78 percent, versus the industry average of 1.14 percent.

Chesapeake Energy (CHK) is off to a strong start in 2019 with the integration of the large acreage positions in the Brazos Valley acquired in the WildHorse acquisition. The company is seeing a significant amount of cost savings and strong performance. As a cushion against price fluctuations, approximately 63 percent of the company's 2019 forecasted oil, natural gas and NGL production revenue is hedged.

At today's oil and gas prices, CEO Doug Lawler expects cash flow to be meaningfully stronger in 2019, as the company continues to leverage capital efficiency and costs.

Chevron (CVX) reported first-quarter earnings of \$1.39 per share in late April, which beat expectations. As we have been expecting, oil and gas production was up sharply from the company's fields in the Permian Basin and from its Wheatstone project in Australia.

Chevron is an integrated oil company, which means it has operations in production as well as refining. This gives CVX diversification because the company's oil and gas production (upstream) benefits from rising oil and gas prices while the refining operations (downstream) tend to benefit from lower oil prices. This diversification adds financial stability during times of volatile oil prices.

CVX has an attractive annual dividend of \$4.48 per share.

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Fidelity Select Natural Gas Fund (FSNGX) is an open-end fund which means it trades at the NAV of its portfolio set at the close of the market each day. It is a diversified way to participate in the growth of the natural gas industry through strong companies.

Natural gas provides the same energy as oil for pennies on the dollar, and natural gas is more environmentally friendly. One barrel of oil provides approximately 5.8 million British Thermal Units (BTUs) of energy. However, with the current market price for natural gas at \$2.60 for one million BTUs, 5.8 million BTUs will cost \$15.08. Thus, with a barrel of Brent crude oil costing \$64, the same amount of energy is available for approximately 24 cents on the dollar if it is in the form of natural gas rather than oil.

The updated chart shows the historic relationship between the costs of these two forms of energy. The red line shows the price of a barrel of oil since the mid-1970s. The green line shows the price of natural gas multiplied by 5.8 to approximate the same amount of energy contained in a barrel of oil. The fact that natural gas provides energy for pennies on the dollar will translate into an expanding natural gas industry.

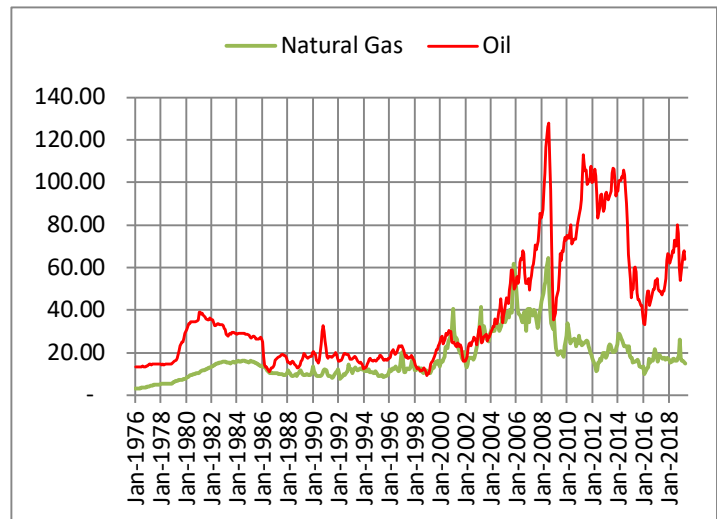
Valero Energy (VLO) reported earnings of 34 cents per share. That was down from \$1.09 per share, a year earlier but above expectations. Valero has been a large buyer of Venezuelan heavy crude and has been substituting light crude oil from North America and other sources which has compromised margins.

Fortunately, Valero has the flexibility to refine substantial quantities of both US light sweet as well as heavy sour crude. It also has access to the US pipeline network for delivery to its gulf coast locations. This flexibility allows VLO to capture the highest margins among its competitors because it can take advantage of the temporary local gluts of crude, whether it's low or high-quality crude, or light sweet or heavy sour, and receive the best discounts for its feedstocks.

Real Estate Selections

The *Sound Advice* portfolio only includes real estate stocks offering an extraordinary value now. Commercial real estate prices remain historically high as low interest rates have pushed down real

The Cost of Energy Equivalents of Oil and Natural Gas



estate capitalization (cap) rates to historically low levels (like bond yields).

Our two recommended REITs in the hospitality industry offer excellent values, high dividend yields, and new growth trends. They also pay attractive dividend yields which also reduces risk by putting a floor under the stock price.

A major drag on the hospitality industry has been the proliferation of Airbnb and similar competition. However, this is changing in major metro areas. New York City is the most recent to pass a measure prohibiting transient rentals of fewer than 30 days at a time without the host being present. San Diego, Los Angeles, San Francisco, Boston, Washington DC, Philadelphia and Miami have also passed similar measures.

Both of our selected hospitality REITs have reported several hotel transactions in recent years. Hersha sold 20 properties from 2016 through 2018 for an average cap rate of 6.5 percent. In the spirit of being conservative and to anticipate a rise in capitalization (cap) rates along with interest rates in general, we use a cap rate of 7.0 percent for valuation purposes.

Hersha Hospitality (HT) has a bi-coastal portfolio of 48 high-quality hotels. The company's funds from operations (the standard measure of performance for a REIT) are 22 percent higher than one year ago.

Hospitality REITs Comparison Table

Company	Symbol	Recent Stock Price	Dividend Yield	Stock Market Cap Rate	Portfolio Value @ 7% Cap Rate (\$Millions)	Stock Value	Discount (-) Premium (+)
RLJ Lodging	RLJ	18.41	7.2%	11.4%	9,069	38.43	-52.1%
Hersha	HT	18.57	6.0%	9.3%	2,873	36.51	-49.1%
Hospitality Properties	HPT	26.00	7.8%	11.0%	12,888	54.40	-52.2%
Host Hotels & Resorts	HST	19.24	4.2%	9.6%	22	27.51	-30.1%
Apple Hospitality	APLE	16.45	7.3%	9.0%	6,695	23.02	-28.5%

The table above shows the “Stock Market Cap Rate” (what the stock price is paying for the underlying real estate portfolio) for several comparable hospitality stocks. The “Stock Value” column shows the current value of the stock assuming the underlying portfolios are valued using a cap rate of 7.0 percent, which is close to the average cap rate on recent hotel transactions. The last column shows the discount or premium at which the stock is trading based on a 7.0 percent cap rate valuation of each company’s real estate portfolio.

Hospitality Properties (HPT) is trading at a large discount. However, this company is externally managed by RMR which charges high fees and suppresses value. As long as RMR continues to externally manage HPT, we do not expect to see significant growth. **Host Hotels and Properties (HST)** is very small, with only 749 thousand shares outstanding, which may lead to excessive volatility. Growth may be limited by its small capitalization.

Based on the trailing four quarters, and using a 7.0 percent cap rate, HT is worth \$36.51 per share which is substantially greater than the current price of the stock. This value should be a conservative estimate because Hersha’s two premier hotels in Miami, the Courtyard Cadillac Hotel and the Parrot Key Hotel, were closed because of Hurricane Irma. Bringing them back on line will add substantially to revenues in the next four quarters. The company projects these two hotels will contribute substantially to the entire portfolio by 2020.

RLJ Lodging Trust (RLJ) is worth \$38.43 per share which is also substantially higher than the current price. We anticipate improvement in net operating income (and thus the value of the stock) because of the company’s mission to sell its non-core assets since the merger with FelCor, and to renovate and upgrade significant properties.

Third Avenue Real Estate Value Investor Fund (TVRVX) is loaded with good values substantially below their net asset values (NAV) with strong growth prospects. Management has a similar approach to ours because it is very price conscious, especially in relation to net asset value. Just as we do at *Sound Advice*, they eat their own cooking – they invest a substantial amount of their personal assets into their funds.

This fund is a global real estate fund which means

it is not confined to US real estate with low cap rates. Management looks for growth more than current income by focusing on real estate operating companies which, unlike REITs, can reinvest profits back into the business. Management also searches for opportunities in different aspects of a real estate company’s capital structure by investing in senior debt in addition to equity. Also, unlike the typical REIT, management will go to cash when asset prices are generally high. Cash is preserved for scooping up opportunities.

Medically-Related Selections

Boston Scientific (BSX) has been a global medical technology leader for three decades by providing a range of high-performance solutions aimed at addressing medical needs and reducing healthcare costs. BSX’s medical products are well suited for an aging population, and the company’s stream of new inventions acquisitions add to promising growth prospects. The company has made acquisitions that have added numerous products with significant growth potential, including Claret Medical, VENITI, and Augmenix.

Stryker (SYK) has a strong balance sheet which gives it the ability to make strategic acquisitions, many of which are coming to fruition. Mako’s surgical robots are now being used in the majority of knee surgeries. Earnings are expected to grow

11 percent this year, far above the industry average of 2.8 percent.

Stryker is best known for its orthopaedic devices for artificial knees and hips. The company also provides a diverse array of innovative medical technologies, including reconstructive, medical and surgical, as well as neuro-technological and spine products. Of course, demand for Stryker's products will grow as America and the rest of the world ages.

The Best in Biotech ETFs

Over the last 15 years, biotechnology has become a major industry and the source of the world's top breakthrough drugs. Biotech companies offer the most explosive profits in the healthcare industry. However, stocks of individual biotech companies are often volatile and can have unforeseen risks, which makes diversification essential. This diversification can be accomplished by investing in a diversified biotech electronically traded fund (ETF) investing exclusively in a portfolio of biotech companies. We are recommending two top performers. Over the last 10 years, those passively-managed biotech ETFs that weighted their portfolio selections essentially equally, as opposed to market capitalization, have been the best performers by far.

This difference stands to reason. Large pharmaceutical companies continue to shrink their internal research and development (R&D) efforts. To revitalize their drug portfolios, they are turning to acquiring biotechnology companies. As a result, the biotech industry has been a hotbed of merger and acquisition (M&A) activity, as smaller biotechs tend to be purchased by the larger ones, often resulting in extraordinary profits in the smaller biotech firms. An ETF allocating its investments based on market capitalization will have disproportionately larger investments in the largest firms and much less in the smaller firms. However, an ETF allocating evenly will have larger allocations in the smaller biotech companies which are generally more likely to benefit from extraordinarily profitable acquisitions. Among the equal weighted biotech ETFs, the top performer by far is **Virtus LifeSci Biotech Products (BBP)**. This ETF seeks investment results that correspond to the price and

yield performance of the LifeSci Biotechnology Products Index, which tracks the performance of biotechnology companies, and covers companies that design drugs ranging from entrepreneurial start-ups to global giants that have completed multiple human clinical trials and have received FDA approval to sell and market at least one drug.

Since December 2018, three of the fund's holdings have since been acquired: Tesaro (by GlaxoSmithKline), Celgene ((by Bristol-Myers Squibb), and Loxo Oncology (by Eli Lilly). Turning to the actively managed biotech ETFs, a top performer has been **ARK Genomic Revolution Multi-Sector (ARKG)** which focuses on the revolution stemming from mapping the human genome. Breakthroughs and advancements have cut the cost substantially of mapping the human genome which is opening up new opportunities and making this sector the cutting edge of new innovations. This ETF invests in companies that are expected to substantially benefit from extending and enhancing the quality of human and other life by incorporating technological and scientific developments and advancements in genomics into their business.

Financials

JP Morgan Chase (JPM) reported first quarter earnings in mid-April of \$2.65 per share and is now expected to earn \$9.94 per share in 2019. JPM is still cheap, especially in comparison to the rest of the market. At \$113 per share, the forward P/E is 11.37. At the relatively modest P/E ratio of, say 14, JPM would be \$139 which is substantially above the current stock price.

Wells Fargo (WFC) also reported first quarter earnings in mid-April of \$1.20 per share, considerably above expectations. WFC is now expected to earn \$4.80 per share in 2019.

WFC is also currently cheap in comparison to the rest of the market. At \$48 per share, the forward P/E is 10. At a P/E ratio of 14, WFC would be \$67.20, substantially above the current stock price.

Small Caps

Numerous studies show that small caps perform better over the long run than the market as a whole. Small Caps are pure plays on the early stages of new industries and inventions. They have more dynamic and entrepreneurial management, and they are much more likely to be the target of an acquisition or merger, which is usually quite profitable.

Third Avenue Small-Cap Value Investor Fund (TVSVX) invests in companies with small capitalizations using the same value-oriented approach as it does with its real estate value fund (TVRVX). Management scours the investment universe for companies that combine the three main features: creditworthiness, a meaningful discount to a conservatively estimated net asset value, and the ability to consistently grow NAV, with an initial targeted holding period of three to five years. A patient and price conscious acquisition is a critical first step in both protecting capital and in realizing an attractive investment return.

TVSVX distributed \$2.05 in December, \$1.98 of which was a long-term capital gain and the balance was a short-term capital gain.

Special Situations

The rest of our portfolio falls into other market sectors, with companies that are presenting extraordinary values within their respective industries. Here they are in alphabetical order.

Apple (AAPL) reported earnings for the first quarter on the last day of April which were in line with expectations. While revenue was down by 17 percent from the same period one year ago, the company's earnings guidance for next quarter was higher than analysts expected. The company said that it plans to spend \$75 billion buying back its own shares. The stock was up 4 percent in after-hours trading on the news.

AAPL remains a good value, especially in view of the \$245 billion in cash in the company's coffers. This amounts to \$51 per share. Subtracting this cash from \$200 per share means we are actually paying \$149 per share for the company. This puts the TTM P/E close to 12.5, substantially below the rest of the market.

Carnival Cruise Lines (CCL) has strong growth prospects because of the company's dominance in the industry, efficiencies of scale, and favorable demographic trends driving a lasting increase in demand. It is also cheap, especially when compared to the rest of the market.

Earnings in 2019 are projected to be close to \$4.45 per share. With the stock price at \$55 per share, the P/E is 12.4.

During the last 5 years, the median P/E has been 19. Looking at another measure of value, CCL has traded at an average enterprise value multiple of 11 during the last five years. A common practice is to multiply a company's EBITDA (earnings before interest, taxes, depreciation, and amortization) by such a multiple to calculate its enterprise value. Based on the most recent four quarters of EBITDA, an enterprise value multiple of 11 puts the enterprise value at \$87 per share, which is substantially above the current stock price.

Intel (INTC) reported first quarter earnings in late April which were okay but the company's estimate of 2019 full year earnings were \$4.35 per share, lower than the previous guidance of \$4.50. The stock price dropped 10 percent on the news.

At \$52 per share and earnings of \$4.35, the stock is trading at a P/E ratio of 12. Such a low P/E anticipates very little or no growth. While that may be the case this year, it is not the longer term outlook. Intel has the size, diversity, and industry dominance to offer a relatively safe investment in a high-growth, and often high-risk business. Intel can leverage new technology into its existing large platform without introducing unacceptable risks. A history of established cash flow and an attractive dividend, along with the currently low P/E ratio, diminishes the risk profile of this stock.

International Business Machines (IBM) reported first quarter earnings in mid-April of \$2.25 per share, slightly higher than expected. Revenue was down slightly. The company reiterated its guidance of at least \$13.90 in earnings per share for all of 2019. This guidance puts the current P/E close to 10, which anticipates little or no growth.

The company is at an inflection point as the growth is now driven by the company's so-

called “Strategic Imperatives” which includes cloud-computing revenue, analytics, mobile and security. Within those imperatives is IBM’s cognitive-solutions segment, which includes software, analytics and its artificial intelligence platform, it calls “Watson”, which can “think” like a human.

IBM is set to acquire Red Hat in the latter half of 2019 which CEO Ginni Rometty and many analysts believe will be transformative because it launches IBM into the enormous and growing hybrid modern data center market.

At a P/E of 12, which is still modest, the stock would be over \$167 per share. The \$6.00 per share dividend provides an attractive yield.

NCR Corp (NCR) remains a good value with a P/E close to 10, a considerable discount to the rest of the market. Earnings per share are expected to be between \$2.75 and \$2.85 in 2019. NCR is continuing its cost saving initiatives, which are expected to result in savings of about \$100 million in 2019.

NCR makes automatic tellers (ATMs), retail point-of-sale (POS) workstations, self-service kiosks, and other self-service checkout systems. 485 million people use NCR products every day, and there is room for substantial growth in the US and around the world.

NCR owns nearly three-quarters of the burgeoning self-checkout market. Using their smartphones, or a handheld scanner provided by the store, customers scan items from the shelves as they add them to their cart. At checkout, they input either device into the register, and it spits out the tally.

Symantec (SYMC) is the world’s leading cyber security company offering organizations strategic, integrated solutions to defend against sophisticated attacks across endpoints, cloud, and infrastructure. Symantec operates one of the world’s largest civilian cyber intelligence networks, allowing it to see and protect against the most advanced threats. Our mantra with this stock has been, “If there ever was a more certain growth industry, protection from cyber espionage is it.”

On average, corporations increased budgets by 20 percent in 2018 to shield against cyber-crime. Symantec also increased its share buyback authorization to \$1.3 billion.

ETFs for Rising Bond Yields

With yields barely above the inflation rate, long-term Treasury bond yields are low, both from a historical perspective and from just plain common sense.

Our recommended ETFs are essentially short-selling bonds and will prosper from rising bond yields. They differ in the amount of leverage used. You can choose among them depending on your investment objectives and risk tolerance.

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

The **Proshares UltraShort Lehman 20 Plus Year Treasury (TBT)** uses 2:1 leverage.

The **Proshares Short 20 Plus Year Treasury (TBF)** uses no leverage.

The price action of these ETFs is based on the changes in long-term Treasury bond indexes, only in the opposite direction, and then multiplied by the leverage each ETF uses. For example, a decline of say, 1.0 percent in their respective benchmark bond indexes will cause TMV to increase by 3.0 percent, TBT by 2.0 percent, and TBF by 1.0 percent.

Slow global economic growth, along with the federal reserve’s relaxed monetary stance, have kept bond yields down. This makes the opportunity in these ETFs greater, even without an increase in interest rates in the foreseeable future.

Long-term treasury bonds are yielding less than 3%, not much more than the yield on shorter term treasury bonds. This is very unusual. Why would investors buy 30-year treasury bonds for nearly the same yield as on 10-year treasury bonds?

Additionally, long-term treasury bonds offer almost nothing in real terms, after adjusting for inflation. This has not been the case historically, as can be seen from the following table.

Years	30 Yr Note (Avg. Yield)	CPI Annual Increase	Real Rate
1980-84	12.0	7.6	4.4
1985-89	8.4	3.6	4.8
1990-94	7.7	3.7	4.0
1995-99	6.3	2.4	3.9
2000-04	5.7	2.6	3.1
2005-09	4.5	2.6	1.9
2010-14	3.6	2.0	1.6
2015-18	2.9	1.9	0.9
Average			3.1
	Current Inflation Rate		2.0
	Theoretical Target Yield		5.1
	Average Since 2000		1.9
	Current Inflation Rate		2.0
	Theoretical Target Yield		3.9

We can see from the history since 1980, that investors have demanded a real return of 3.1% on long-term treasury bonds. With today's inflation rate in the vicinity of 2 percent, 30-year treasury bonds should be yielding 5.1 percent, not 3.0 percent. If we only look at recent history, since 2000, a low inflationary period, investors have demanded a real return of 1.9 percent. This would put the yield on long-term treasury bond yields at 3.9 percent. Accordingly, even in a low inflationary environment, the yields on long-term treasuries are too low at 3.0 percent. They belong much higher, even without a rising interest-rate environment.

The table below shows the impact on the prices of our selected ETFs at various long-term treasury bond yields. The first row shows today's ETF prices with long-term Treasury bonds yielding 30 percent. Note that the price of these ETFs would rise dramatically with yields at 4 percent, and even more so at 5 percent.

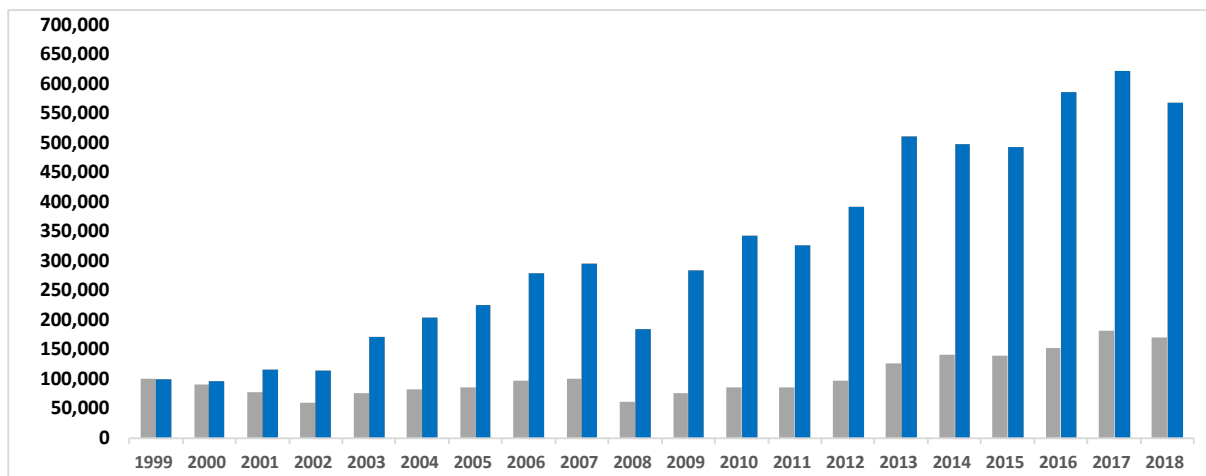
Bond Yields	ETF Prices		
	TBF	TBT	TMV
3.00	22.00	33.71	17.05
3.50	23.79	39.19	21.21
4.00	25.66	45.34	26.20
4.50	27.63	52.31	32.24
5.00	29.70	60.15	39.49

The Erosion Factor

As we point out regularly, these ETFs suffer from erosion because they decline slightly faster than they increase with an equivalent change in bond yields, particularly with higher leverage. To gauge this factor, we can assume that Treasury bond yields simply tread water, rising and falling by an unusually large amount, say, 0.03 percentage points (3 basis points) every day, and thus go nowhere. By the end of 2019, TMV would decline to \$16.33 (4.2 percent), TBT would decline to \$32.92 (2.4 percent), and TBF would decline to \$21.79 (0.9 percent). While not insignificant, this erosion factor is nominal in comparison to the price swings caused by a change in bond yields.

Sound Advice vs the S&P 500

This chart shows the growth of \$100,000 invested in the S&P 500 (in gray), which would have grown to \$170,645, versus \$100,000 invested in the Sound Advice recommendations (in blue), which would have grown to \$561,174.



See our website for live pricing and buy limits: <http://www.soundadvice-newsletter.com/members>

Energy/Natural Resources	Symbol	Price / NAV	Yield	Action	Limit
Adams Natural Resource Fund	PEO	\$16.97	6.00%	BUY	\$17.82
Chesapeake Energy Corp	CHK	\$2.91	0.00%	BUY	\$3.06
Chevron	CVX	\$120.06	3.73%	BUY	\$129.00
Fidelity Select Nat. Gas Fund *	FSNGX	\$21.80	0.37%	BUY	\$22.50
Valero	VLO	\$90.66	3.97%	BUY	\$95.19
Real Estate					
Hersha Hospitality Trust	HT	\$18.57	6.03%	BUY	\$19.50
RLJ Lodging Trust	RLJ	\$18.41	7.17%	BUY	\$19.33
Third Avenue Real Estate Value Investor *	TVRVX	\$28.90	1.41%	BUY	\$29.90
Medically Related					
Boston Scientific	BSX	\$37.12	0.00%	BUY	\$38.98
Genomic Revolution Multi-Sector	ARKG	\$32.71	0.00%	BUY	\$34.35
Stryker Corp.	SYK	\$188.91	1.10%	BUY	\$198.36
Virtus LifeSci Biotech Products	BBP	\$41.84	0.00%	BUY	\$43.94
Financials					
JP Morgan Chase	JPM	\$116.05	2.76%	BUY	\$121.85
Wells Fargo	WFC	\$48.41	3.55%	BUY	\$50.83
Small Caps					
Third Avenue Small-Cap Value Investor Fund *	TVSVX	\$18.62	0.37%	BUY	\$19.00
Special Situations					
Apple	AAPL	\$200.67	1.46%	BUY	\$210.70
Carnival Cruise Lines	CCL	\$54.86	3.65%	BUY	\$57.60
Intel	INTC	\$51.04	2.35%	BUY	\$53.59
International Business Machines	IBM	\$140.27	4.28%	BUY	\$147.28
NCR Corp	NCR	\$28.95	0.00%	BUY	\$30.40
Symantec	SYMC	\$24.21	1.16%	BUY	\$25.42
ETFs for Rising Interest Rates					
ETF - Direxion Daily 20+ Yr Bear 3X	TMV	\$17.05	0.00%	BUY	\$17.90
ETF - ProShares Short 20+ Year Trsry	TBF	\$22.00	0.00%	BUY	\$23.10
ETF - ProShares UltraShort 20+ Year Trsry	TBT	\$33.71	0.00%	BUY	\$35.40
Hedges					
S&P 500 ProShares Ultra Short ETF	SDS	\$30.93	0.00%	BUY	\$32.48

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

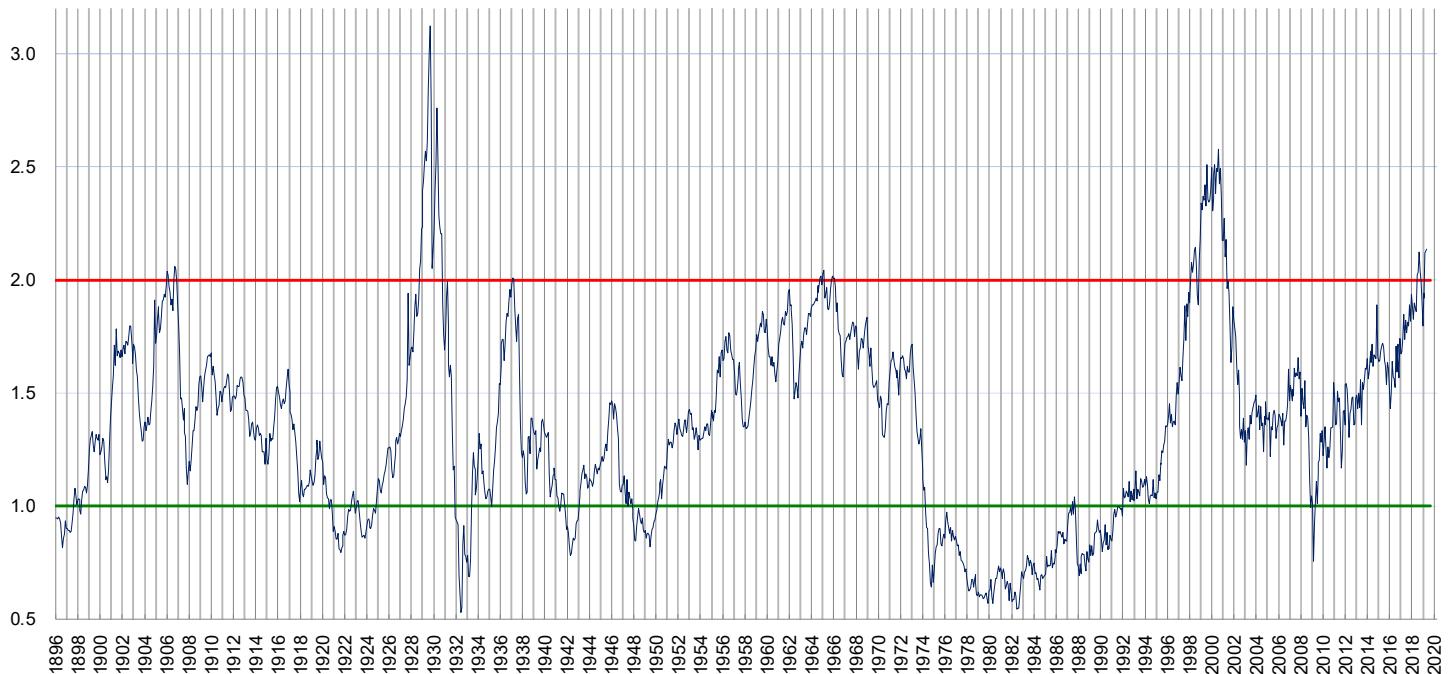
* It is not possible to offer live pricing on our recommended mutual funds.

General Comments: Our statistics are based on the assumption that \$10,000 is invested in each position. When a new position is added, we assume the same \$10,000 amount is invested in the new recommendation. When we recommend adding to a particular position, as we have done over the years, we assume another \$10,000 is invested again in that position.

If you are picking and choosing, you can focus on the sector of the portfolio that matches your investment objectives. Alternatively, you may have a higher degree of comfort with certain industries, funds, or stocks because of past experience or your profession. In that case, you may want to invest more heavily in one sector, or in one or more individual recommendations.

As always, broad diversification will temper volatility, add to safety, and improve long-term performance.

Capital Competition: Real Estate versus Stocks: The SoundAdvice Risk Indicator



There are few forces that are more important to a market's destiny than the amount of capital that is available to it. In a normal situation, capital will flow easily between markets as their underlying conditions change. But if a market becomes dangerously superheated, it will absorb a larger proportion of available investment capital than economic conditions and market demand can justify. This change will be reflected not only in the rising market's prices but also in the prices of competing markets, which will be lower than their underlying fundamentals would indicate they should be. Over the last 120+ years, we can see this titanic struggle between the stock market and its foremost competitor for investment dollars: real estate.

To reveal this phenomenon, we have set up an equation based on the ratio of the S&P 500 Stock Index to median price of new houses for each month over the last 100+ years. This equation exhibits an elegant financial minuet as each market has taken turns outperforming the other.

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

We label this new tool the **Sound Advice** "Risk Indicator," since it will allow us to locate the point at which prices are so high when compared to competing markets that they have come loose from their moorings and are on the verge of declining or under performing the other market.

What is too high? When stock prices are very high

relative to house prices, the **Sound Advice** Risk Indicator will rise over the line marked 2.0, revealing a high-risk time for stocks. In contrast, when the indicator drops below the line marked 1.0, it means that it is a very low-risk time to buy stocks. Notice from the chart how the **Sound Advice** Risk Indicator has oscillated back and forth, revealing the ongoing struggle between Stocks and houses for investment capital. We have labeled these long vacillations Supercycles.

But though an investment beginning with \$25,000 in 1895 could have made money being in either stocks or housing, had an investor followed the signals of the **Sound Advice** Risk Indicator he or she would have made \$437 million, or 26.5 times more money than by simply holding stocks though the ups and downs.

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

The New York Times

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

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

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

As U.S. corporations expanded to meet growing demand, and the economy came to a rolling boil during the Eisenhower years, the stately rise would multiply stock prices by ten times until November 1964, when the Risk Indicator crossed over 2.0 again. The stock market would continue to climb into 1968, and then crash in 1975, wiping out the inflation-adjusted gains scored by investors since 1954. However, a switch to an investment in houses would avoid all that and double in price by the time the next signal came for stocks in May 1974, as the Risk Indicator fell below 1.0 again, as the Dow careened below 700.

It would not be until March 1998 when the Risk Indicator would cross 2.0 again, after stocks were up by more than tenfold. The Dot-Com bubble would push stocks higher into early 2000, but then began another 50 percent retracement. A switch to houses would produce a 44 percent gain through the end of 2008 while stock prices were lower by 17 percent. In February 2009, with the Dow careening down through the 700s once again, the Risk Indicator quietly dropped below 1.0 to 0.77 as the S&P tumbled under 700. Since then, the stock market has delivered stunning gains as the S&P 500 has quadrupled. **For the sixth time in the last 123 years, the Risk Indicator rose above 2.0 again in July 2018.**

With the latest median house price at \$315,200 in February and with the S&P 500 at 2940, the Sound Advice Risk Indicator reads 2.14, revealing the risk in stocks is high.

As remarkable as the **Sound Advice** Risk Indicator has been, it does not pinpoint the exact time. In the past 123 years, its signal has ranged from being only one month after the zenith to as much as four years early. While the Risk Indicator has been early, it has never been wrong. An expensive crash was inevitable. A 50 percent decline took a 100 percent recovery just to break even.

To help us narrow down the timing as well as gage the potential severity of an upcoming decline, we have our Diffusion Indexes.

Business Cycles and Stocks: The SoundAdvice Diffusion Indexes

Track Record of the SoundAdvice Diffusion Indexes

After each "Aggressive" signal, the S&P 500 climbed an average of 30.0 percent. During "Caution" signals, the S&P 500 either crashed, meandered, or climbed, recording an average increase of 3.3 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
Mar-15	2,080.0	May-15	2,111.9
Sep-17	2,492.8	Jan-18	2,823.8
Ave +/-	30.0%		3.3%

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 **Sound Advice** Diffusion Indexes, we observe changes in each of our selected indicators over a six-month period, and take the percentage of those increasing.

When the **Sound Advice Diffusion Index of LEADING Indicators** drops to zero, it is time to buy stocks aggressively, regardless of how negative the atmosphere may be. This is not just an empirical coincidence. It is also logical. In order for all of the leading economic indicators to be giving off a zero value compared to six months before, it is nearly certain that the soft economy is providing an atmosphere for stable or declining interest rates.

This Diffusion Index gave us a zero reading in April, 2009, close to the bottom, officially giving us an "Aggressive" signal. That signal came at a

time when the Risk Indicator was below 1.0, which revealed that Supercycle 5 came to an end, and that Supercycle 6 was born.

The **Sound Advice Diffusion Index of LAGGING Indicators** gives "Caution" signals when all three of its individual lagging economic indicators rise above their respective levels of six months earlier, providing a 100 percent reading. This reading reveals that the US economy is strong enough to put upward pressures on interest rates.

Most of the time, this Diffusion Index has been a timely indicator of oncoming bear markets because a rising interest rate environment is a dangerous time for stocks. The times when this Index has not performed in a timely fashion is when monetary policy has been established and enforced, regardless of fluctuations in economic strength. A prime example is the quantitative easing (QE) programs that were used to bail out the economy from the 2008-09 meltdown. In recent years, the economy has strengthened, sufficiently at times to push this Diffusion Index to 100 percent. However, interest rates did not rise because they were being held artificially low by the Fed's massive QE bond-buying activities. During the QE programs, the Fed's assets grew by more than 5 times, from under \$900 billion in 2008 to \$4.6 trillion.

That has changed now because quantitative easing has been reversed into quantitative tightening. Instead of buying, the Federal Reserve has started reducing its current inventory of \$2.8 trillion of Treasury bonds and \$1.8 trillion of mortgage-backed securities. This means that we will no longer have a QE program holding interest rates artificially low.

Current Status

The Diffusion Index of LAGGING Indicators climbed to 100 percent for December, giving us a new Caution Signal in January, very close to the peak in the market. The latest data for March caused a 100 percent reading.

Our next signal will come from the Diffusion Index of LEADING Indicators, when it drops to zero, which would take a surprising softening in the US economy. The latest reading for this Diffusion Index is 66.7 percent.

Concurrence

There are times when signals from the **Sound Advice** Risk Indicator and the Diffusion indexes are out of sync, when one is signaling caution and the other is not. This occurred in August 1987, when the Diffusion Index of Lagging Indicators switched into caution mode, just prior to the October 1987 Crash that took stocks sharply for a brief period. Non-concurrence also occurred in March of 2008, when the Diffusion Index of Lagging Indicators switched into caution mode, just prior to the 2008-09 bear market crash. Both of these crashes were brutal, but relatively short-lived. Once the Risk Indicator plunged below 1.0, a very profitable bull market followed.

Then there are times when both indicators concur, signaling the same thing at roughly the same time. This happens when the Risk Indicator is above 2.0, indicating the end of a supercycle, and the Diffusion Index of Lagging Indicators switches into caution mode, indicating the end of a business cycle. Of course, this concurrence indicates that a more vicious and potentially longer-lasting bear market, or series of bear markets, is bound to follow, eventually taking stock prices down substantially – usually by 50 percent -- until the Risk Indicator falls below 1.0 again. We have this concurrence today.

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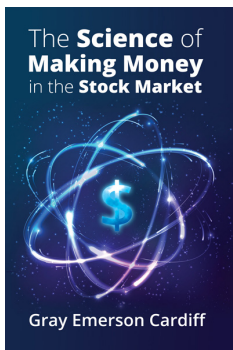
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