

Defense! Defense!



October 21, 2015, was "Back to the Future Day." That was the day Doc and Marty McFly travel back to the future from 1985. Marty was wearing Nike sneakers. If he would have acted on his fashion sense before he left, and invested \$10,000 in Nike stock at 42 cents per share, he would have arrived with his stock at \$132, for close to a \$4.7 million profit.

He would have done almost as well with Apple. In the store window where Marty purchases the sports almanac in 2015, there is an Apple Macintosh labeled "Antique Computer". Apple was trading at \$114. Marty could have bought it for \$1.29 in 1985.

There is nothing like a time machine to bolster your investment performance.

In one of the movie's timelines, when Marty travels back to the future, he sees that the Cubs won the World Series this year. He meets an old man that says, "I wish I could go back to the beginning of the season and put some money on the Cubbies." Having grown up around Chicago, I have been a dormant Cubs fan for decades. I was hoping the movie got this one right.

Since we do not have a time machine, we have more mundane investment results to report.

The *Sound Advice* Portfolio is up so far this year, by 3.5 percent, as compared to 2.2 percent from the S&P 500. We have an average profit of 52 percent, based on the prices at which each position was recommended.

- Best regards,

-- Gray Emerson Cardiff, Editor

This is the chant heard at football games. That's because all good football teams have a strong defense. We should always keep that in mind as investors because successful investing is achieved by defending ourselves against adverse markets.

On October 28, the Federal Reserve finished its 2-day meeting. As expected, it announced that it was not going to change its current monetary stance of near-zero interest rates, which was established after the 2008-09 melt-down as an emergency measure to bail out the economy.

What was not expected was that the fed opened the door for a possible change in this stance for its upcoming mid-December meeting. This sent a shockwave into the markets, obliterating a 100+ point rally in the Dow. Although the market recovered, bolstered by rallies in bank stocks on the prospects of being able to charge higher interest rates, the message was clear: When the Federal Reserve finally abandons its emergency monetary policy and starts raising interest rates, it will not be good for stocks and bonds.

In recent issues, we have noted that the stock market is dangerously high, based on the 1.3 ratio of the total capitalization of the stock market (stock prices of all publicly traded companies multiplied by their respective amounts of shares outstanding) to the gross domestic product (GDP) of the US. This ratio rose above 1.2 in the late 1990s prior to the 2000-02 bear market that took stocks down nearly 50 percent. It also rose above 1.1 just prior to the 2008-09 bear market which took stocks down nearly 50 percent again.

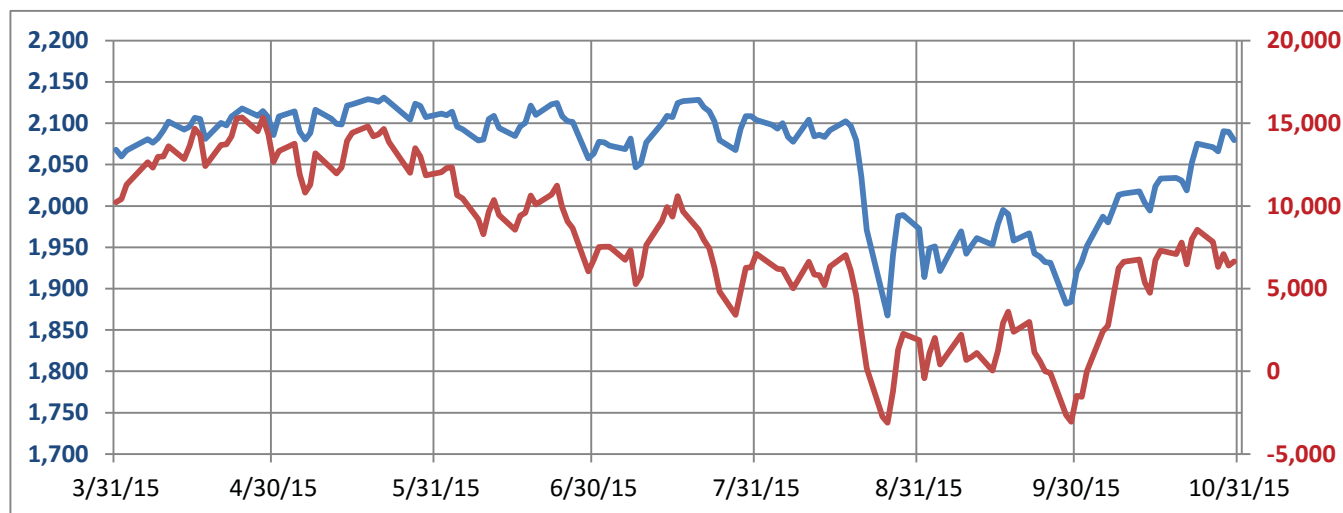
In our June 29, 2015, issue, we announced that our Diffusion Index of Lagging Indicators (page 11) rose to 100 percent, issuing a caution signal. Subsequent readings have been 100 percent every month since then, including the latest one announced in late October (for September). This is worth mentioning to eliminate the possibility that the current caution signal could have been a one-month fluke.

We have also noted that the breadth of the market began deteriorating in May. This was problematic because a healthy bull market will have broad participation among a wide range of stocks. However, participation will narrow as it runs out of gas. Near major tops, the largest capitalized stocks continue to rise because they are the easiest places for money managers and mutual funds to put incoming cash. This causes popular market averages to continue rising because they are heavily weighted by the stocks of the largest companies. However, the overall breadth of the market will be deteriorating. The breadth of the market is revealed by tracking the number of stocks that advance on the New York Stock Exchange, and subtracting the number that decline. The cumulative total is the "advance-decline line" or ADL.

This breadth deterioration led to the down-drafts and volatility we saw in August. Since then, we have not seen any significant divergence between the S&P 500 and the ADL, although some negative divergence appeared during the last week of October. A chart since March is on the following page.

Over please ...

Stock Market Breadth Since March, 2015



From this perspective, we can conclude that stocks in general are dangerously high, particularly with rising interest rates on the horizon and our Diffusion Index of Lagging Indicators flashing caution. Accordingly, it is an appropriate time to include in our portfolio an ETF that will benefit from a declining stock market.

The **ProShares UltraShort S&P 500 (SDS)** is a reverse ETF that 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 performs as it should, with daily premiums and discounts within 0.5 percent. It is also very liquid.

As with any reverse ETF, SDS will erode slightly over a long period of time because it will decline slightly more than it will increase with an equal movement in the S&P 500. The erosion factor is nominal in comparison to normal market movements, but it can add up over an extended period. The 2:1 leverage amplifies this erosion factor as well.

Accordingly, SDS is not a long-term holding proposition. However, for the near term, it will serve as a counter-balance to the rest of our portfolio in a general market correction. The 2:1 leverage factor means that it will better serve this purpose without making a large investment. It is also in the aggressive segment of our portfolio. See the table on page 9.

We are also recommending three ETFs designed to benefit from the inevitable rise in long-term Treasury bond yields. We have dubbed these ETFs as “No-Brainers” because interest rates and bond yields always rise during an economic recovery, especially as a recovery evolves into a vibrant economy. These ETFs differ in the amount of leverage used, and 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 bonds, specifically BlackRock’s iShares 20+ Year Treasury Bond ETF (symbol TLT) which holds a portfolio exclusively of long-term Treasury bonds. The prices of these 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 these ETFs to drop in the same fashion. We can project the movements of these ETFs based on any given scenario.

As part of the Federal Reserve’s economic projections, each member of the Federal Open Market Committee (FOMC) makes a prediction regarding the future path of interest rates. Those predictions are plotted in the so-called “Dot Plot”, and medians are taken to formulate the Federal Reserve’s official prediction.

The most recent Dot Plot was taken at the September meeting. The September Dot Plot predicts that the Federal funds rate will be 0.375% at the end of 2015, 1.375% by the end of 2016, and 2.375% by the end of 2017. Assuming long-term Treasury bond yields move in accordance with the latest Dot Plot predictions of the Federal Funds rate, here is what would happen to each ETF:

TMV would rise to \$34 by the end of 2015, to \$55 by the end of 2016, and to \$87 by the end of 2017.

TBT would rise to \$50 by the end of 2015, to \$69 by the end of 2016, and to \$93 by the end of 2017.

TBF would rise to \$26.3 by the end of 2015, to \$31 by the end of 2016, and to \$36 by the end of 2017.

Whether or not the Federal Reserve actually raises interest rates in the December meeting is not critical to the longer

term performance of these ETFs. Amending the latest Dot Plot to no increase in 2015 would simply mean that there would be no significant change in the prices of these ETFs in 2015. As long as the 2016 and 2017 targets were met, the projected prices of these ETFs would remain unchanged.

As we have pointed out in the past, these ETFs suffer from erosion because they decline slightly faster than they increase with an equivalent change in bond yields. This erosion factor is nominal in comparison to the price swings caused by a change in bond yields, but it can become significant over an extended period of time.

Energy Selections

Our primary thesis remains the same: The industry has been decimated by the oil glut, caused primarily by over-production from the US fracking boom. However, under the pressure of brimming oil storage tanks, the price of oil has fallen below the cost to drill, and new drilling is certain to continue declining. It is only a matter of time until the glut will disappear.

We also know that US production will continue falling off because of the nature of fracked oil wells. Production drops 70 percent during the first year from the typical fracked well. This requires a substantial amount of new wells to be added to maintain overall production levels. We know that is not happening because the domestic drilling rig count has plunged 50 percent since October 2014.

US production has been tapering off since the peak in early June. As of the week ending 10/23/2015 (the latest week reported), US production is down by 498 thousand barrels per day. There were 480 million barrels of oil in US storage tanks, which equates to only 68 days of oil imports into the US.

As production continues to decline and becomes more pronounced, draws from storage tanks are certain to be substantial. That means the oil glut will disappear, the price of oil will recover, and that is bound to translate into stellar profits from carefully chosen oil and gas stocks.

On October 28, the price of West Texas Intermediate (WTI) crude oil rose sharply by \$2.98 on the news that Mexico's national oil company (Pemex) received a permit to import up to 75,000 barrels per day of US light (WTI) crude oil. This could be the first step in ending the long-standing US ban on exporting crude oil, which was established in 1973 during the first energy shortage, and aimed at protecting US supplies of oil. Of course, freedom to export US oil could alleviate temporary gluts.

Here are updates to our energy portfolio, in alphabetical order.

Chevron (CVX) reported third quarter earnings in the final trading day of October of \$1.09, resoundingly beating expectations of \$0.79.

CVX is a vertically integrated oil company which means it has operations in all phases, from exploring and drilling, to transporting and refining, and even to retail sales at its gas stations. Profits vary from these various stages of production, depending on price demand for oil and for refined products. High oil prices boost margins from drilling but squeeze margins from refining. When oil prices are low, profit margins expand from refining, but not nearly enough to offset declines in drilling profits. This quarter is a case in point. While drilling (upstream) profits were poor, profits from refining (downstream) were higher, which helped balance overall earnings.

This quarter's earnings do not quite cover the dividend, but management has pronounced the annual dividend of \$4.28 per share as "sacrosanct." Accordingly, the current yield of more than 5.5 percent puts a floor under the stock price while we wait for a recovery in oil prices.

Chesapeake Energy (CHK) has taken a beating from the crash in oil and gas prices. However, CHK has substantial assets. Morningstar's (<http://www.morningstar.com>) current valuation of CHK is \$19 a share, which is still close to 3 times the current price of the stock. All CHK has to do is survive to bring us a stunning profit from here.

CEO Doug Lawler's recent statement is encouraging:

"We understand that our debt structure and gathering commitments add to the challenges of the commodity price environment, and there are several questions out there in the market, such as: can Chesapeake generate sufficient cash flow to weather this storm? And can the portfolio and operational strengths overcome these significant obstacles?"

The answer is definitively, yes. We have tremendous flexibility and optionality given the breadth and diversity of our portfolio."

Fidelity Select Natural Gas Fund (FSNGX) is a diversified way to participate in the recovery 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.

The drop in the price of oil brought the energy-equivalent costs of oil and natural gas closer, but a substantial disparity still exists. One barrel of oil provides approximately 5.8

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million British Thermal Units (BTUs) of energy. At \$45 a barrel, that is the cost of 5.8 million BTUs. However, with the current market price for natural gas close to \$2.30 for one million BTUs, 5.8 million BTUs will cost \$13.34 (5.8x\$2.30). So the same amount of energy is available for 30 cents on the dollar, if it is in the form of natural gas rather than oil.

An updated chart is below, showing 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 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. Most of the time, the costs of the two forms of energy have been closely aligned. They have moved closer together, but remain substantially apart. This difference still translates into an expanding natural gas industry.

ICON Energy Fund Class S (ICENX) is also a diversified way to participate in the recovery with a basket of substantial companies. In the past, this fund has achieved growth even during periods of declining energy prices. ICON management looks for changes within the energy sectors to capture value, rather than simply depending on rising oil prices. For example, the profit margins expand on pipelines when the price of oil is low, because the cost and price of storage and transportation have little to do with the price of oil. This fund is a good way to capture today's values and profit from the recovery and changing landscape on a diversified basis.

Transocean (RIG) has been sharply impacted by the drop in oil prices. As we reported in our mid-October email update, management is proposing to eliminate the next 2 dividends, one for December 2015 and one for March 2016.

Management is saying that in view of the currently challenging offshore drilling conditions, all necessary actions need to be taken to improve the company's long-

term competitiveness, including reducing operating costs to enhance underlying cash flow, making investments in the fleet, and scrapping rigs that are no longer viable. Additionally, management is recommending the elimination of the next two dividends in order to maintain as much flexibility as possible as reflected in a strong, liquid balance sheet.

Although the decision appears prudent, it was comforting to know that the dividend was defining a floor under the stock price because the dividend provided an attractive yield, and a further decline in the stock price would have made the yield even more so. Accordingly, the complete elimination of the dividend increases the near-term risk to the stock price.

On the other hand, the dividend elimination is presumably expected by the market, and the stock price has actually increased recently. This indicates that the market is looking beyond this negative event to the increased likelihood of the company's survival through these harsh times.

We continue to recommend RIG because its prospects of survival are being improved, along with the prospects of longer-term growth from here. However, it may be at the expense of increased short-term volatility without the floor provided by the dividend.

The US still imports close to 7 million barrels per day. Deep water drilling is still a necessary source for the US and the world's oil needs, especially as US fracking drops off. Long-term profits from RIG should be stellar from here.

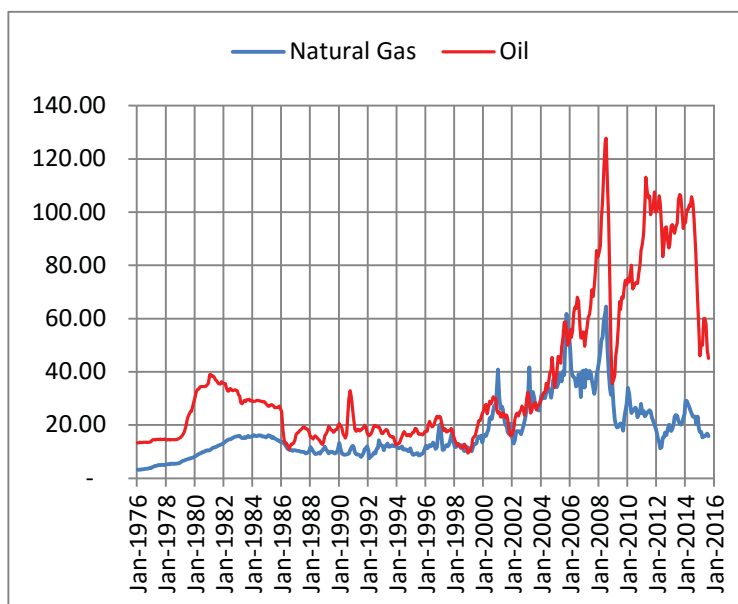
Valero Energy (VLO) reported a 38 percent jump in third quarter operating earnings in the final days of October. VLO also hiked the quarterly dividend by 25 percent to 50 cents per share, which brings the current yield over 3 percent.

Valero is the largest oil refiner in the US. It owns 15 refineries with a capacity for 2.9 million barrels per day. The company also has 7,400 retail outlets in the US, Canada, UK, and Ireland, under the brands Valero, Beacon, Ultramar, Shamrock, and Texaco. Valero is one of the few energy companies that can benefit from lower oil prices because refining margins generally expand during such times. This is evidenced by the 30 percent rise in refining margins during the third quarter, to \$14.38 per barrel from \$11.81 one year ago.

Most US refineries are not set up to handle the light, sweet, crude oil that is coming from fracking US shale. Valero's refineries are notable exceptions because they are the most flexible refineries, allowing Valero to capture the highest margins among its competitors. Valero's refineries are also well positioned geographically, even for accessing the low-cost Maya crude from Mexico, heavy sour oil that Valero buys for an even larger discount than from glutted US oil.

VLO remains an astonishing value. Earnings are expected to be in the vicinity of \$8.00 per share in the year ahead. This puts VLO's forward price/earnings ratio (P/E) under 8, which is a low P/E for any stock and a deep discount from the overall market.

The Cost of Energy Equivalents of Oil and Natural Gas



Real Estate Selections

Low interest rates for so many years have pushed down real estate capitalization (cap) rates (the yield before debt payments are considered) to historically low levels. As a result, commercial real estate prices are historically high, and the average real estate investment trust (REIT) does not present a particularly good value.

In the longer run, a rising economy will push up rental rates which will more than compensate for added interest expenses caused by rising interest rates. However, this benefit is most likely to translate into profits only on real estate stocks offering an extraordinary value now.

Hersha Hospitality (HT) is selling at a discount to its hotel assets because most of its major properties have been undergoing renovations and not producing their full income potential. Income is rising from new acquisitions and completed renovations.

Third quarter funds from operations (FFO) climbed 17.7 percent from a year ago. Revenue per available room (RevPAR) grew 6.9%. HT's Manhattan portfolio reported 4.2% RevPAR growth which outperformed the market. RevPAR grew by double digits from HT's Boston, Miami, and California hotels. This followed second quarter revenue of 13.9 percent.

We estimate the net asset value (NAV) of Hersha's hotel properties is at least \$29.22, based on the net operating income of the most recent four quarters. We expect the NAV of HT to increase as renovations and new acquisitions add to revenue.

Retail Opportunities Investment Corp (ROIC) 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, funds from operations (FFO) is bound to continue to rise.

This trend continued in the most recent third quarter, ending with a strong 18.2 percent increase in funds from operations (FFO) and occupancy of 97.1 percent. ROIC also pays an attractive dividend which lowers its risk profile.

CEO and President Stuart Tanz summarized the results:

"2015 is shaping up to be one of the strongest years on record for the company. In just the first nine months, we have already achieved our portfolio growth objective for the year, securing \$310 million of grocery-anchored shopping center acquisitions. Additionally, we continue to maintain our high occupancy at over 97% and have already leased more than double the amount of space that was originally scheduled to expire in our portfolio for the entire year."

Third Avenue Real Estate Value Investor Fund (TVRVX) is replete with stellar values substantially below 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, in making decisions on whether to buy, hold, or sell a particular company. The managers expend great effort analyzing financial statements, visiting companies and their properties, and assessing management teams to come up with their estimates of intrinsic value. An additional similarity to *Sound Advice* is that members of management eat their own cooking – they invest a substantial amount of their personal assets into their recommendations by investing into the funds they manage.

TVRVX has a number of distinguishing characteristics. This is a global real estate fund. 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 looks for opportunities in different points of a real estate company's capital structure by investing in senior debt in addition to a company's equity. Also unlike the typical REIT, management will go to cash when asset prices are generally high. Cash is preserved for scooping up opportunities in distressed times.

Specifically, the management team looks for 4 fundamental characteristics before making 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.
- 4) The prospects are that over the next three to seven years, NAV will be increasing by at least 10 percent annually (including dividends).

Medically-Related Selections

This sector is defensive because medical needs persist regardless of financial conditions. The world's inexorable demographic aging trends and the commensurate increase in medical care needs translates into strong growth prospects for this industry.

Boston Scientific (BSX) jumped 8 percent on the late-October third quarter earnings report. Overall revenue grew 9%. BSX's cardiovascular business revenue increased 9 percent, and its interventional cardiology revenue increased 7 percent. Growth from these segments is important because stents and implantable heart-rhythm devices account for more than one-half the company's overall sales.

The company increased its 2015 full-year earnings forecast range to 90-92 cents per share, up from 88-92 cents.

BSX has medical products that are well suited for an aging population. The company's mission is to transform lives through innovative medical solutions that improve the health of patients around the world. 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 has more than 900 US patents.

Pfizer (PFE) turned in another strong quarter of earnings in late October. Third quarter earnings of 34 cents per share also lifted full year earnings expectations to \$2.18 per share from \$2.07.

As we have noted in past issues, PFE has an arsenal of new pharmaceutical products, with 88 in clinical development and 30 in late stage development or registration. PFE has rebuilt its pipeline and transformed its R&D approach. The company is well positioned with several break-through drugs and treatments.

Third quarter results were bolstered by rising sales for PFE's *Pneumovax* pneumonia vaccines, its cancer drug *Ibrance*, and its blood-thinner *Eliquis*. These results are very encouraging because these drugs are PFE's potential blockbusters.

Stryker (SYK) provides a diverse array of innovative medical technologies, including reconstructive, medical and surgical, as well as neuro-technological and spine products, although SYK is best known for its orthopedic devices for artificial knees and hips. Continued growth is 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.

In October, SYK reported earnings of 79 cents per share, surpassing expectations. Stryker now expects full-year earnings to be in the vicinity of \$5.10 per share.

We expect continued growth in SYK because of the company's cash-rich balance sheet and strong cash flow, which give it avenues for continued diversified growth through acquisitions. The most significant recent acquisitions was MAKO Surgical, which recently received FDA clearance for its knee and hip applications, enhancing SYK's robotic reconstructive solutions. Other recent acquisitions include Small Bone Innovations, Pivot Medical, Berchtold Holding, as well as Trauson Products, China's largest manufacturer of orthopedic implants.

Stryker is buying back \$2 billion of SYK in 2015, following the purchase of \$100 million in 2014.

Tekla Life Sciences Investors (formerly Hambrecht & Quist Life Sciences Fund - the symbol is still HQL) is in our portfolio because the most explosive profits in the entire healthcare industry can be found in biotech companies. Over the last 10 years, biotechnology has become a major industry which now provides the world's top drugs. This sector has outperformed the broad market during the last one, five, and ten year periods.

Biotech companies tend to be high risk and high reward investments which makes diversification essential. This fund is an excellent way to invest in this sector.

Small Caps

Numerous studies show that small caps perform better over the long run than the market as a whole. This is especially true during a recovering economy. Small-cap stocks perform better than large-cap stocks because they 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. They also tend to be domestic companies without substantial overseas exposure, and therefore are not buffeted by the currency fluctuations that are currently haunting larger companies. Here more than ever, attention to value is paramount.

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. TVSVX management scours the investment universe for companies that combine the three main features: creditworthiness, a meaningful discount to a conservatively estimated net asset value (NAV), 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.

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.

Agrium (AGU) is a Canadian company offering a broad mix of agricultural products, from wholesale fertilizers to retail farm products, aimed at increasing the efficiency of food production. AGU products will be in growing demand as arable land continues to disappear around the world while population and per-capita income increases. This translates into a need for greater crop output per acre through the use of AGU's products.

AGU's diversification tends to protect it from swings in the markets and brings steady sources of growing free cash flow which allows it to expand for future growth. Close to one-half of AGU's earnings come from its retail stores offering farm products, and the other half comes from its wholesale sales of fertilizers, mostly nitrogen-based but also from potash and phosphates.

AGU is trading at close to 12 times next year's earnings estimate of \$7.25 per share. This is a good value with a growing dividend.

We are not alone in our view. The company's CEO, Charles Magro, purchased 3,800 shares in September, after a similar purchase in July.

Jeff Ubben, founder, CEO and CIO of ValueAct Holding, recently increased his AGU holding by 25 percent to 10 million shares. ValueAct Holdings concentrates on acquiring significant ownership stakes in a limited number of companies that it believes are fundamentally undervalued.

Disney (DIS) launched its trailer for *Star Wars: The Force Awakens* during Disney-owned ESPN's Monday Night Football broadcast in mid-October. As we noted in our mid-October email update, the overwhelming demand for

tickets knocked out several movie ticket websites, including Fandango, for a brief period. The initial demand indicates that this will indeed be one of the largest openings for a movie of all time, if not the largest. Most published estimates for the worldwide box office take are the \$2 – 2.5B range, putting it in second place behind 2009's *Avatar* for the highest grossing movie in history. However, many predict it will easily surpass both. It's already set to smash other records, opening in more than 4,500 theaters, the most ever, and has already secured the exclusive use of every IMAX screen in the US for the first month after release.

Disney-Pixar also announced some big titles in October for younger viewers, including *Finding Dory*, a sequel to 2003's hugely popular *Finding Nemo*, as well as *The Incredibles 2*. These and the upcoming Thanksgiving Day release of *The Good Dinosaur* add to Disney's list of high-profile releases in the near future.

As much attention as Disney's endearing movies and characters get, they comprise only half the company's earnings. The rest comes from its cable networks -- the Disney Channel, ABC, the ABC Family Network, and the largest by far, ESPN and its sister networks. We added DIS to the portfolio when last quarter's earnings disappointment caused DIS to drop, giving us the opportunity to recommend it on a dip. It has since recovered, adding to our portfolio profits.

Last quarter's earnings disappointment was caused by a decline in ESPN revenues. That stoked fears of the fragmentation trends in the media landscape, with younger audiences watching television in different ways than on the traditional multichannel cable and satellite platforms. However, CEO Bob Iger notes that not one new platform has talked about launching without coming to Disney first for its programming content.

Although still a highly profitable unit of Disney, ESPN has been under pressure to reduce costs because it no longer can depend on steady growth from cable and satellite subscribers. ESPN is also feeling the squeeze on the cost side. Its NFL "Monday Night Football," now costs \$1.9 billion a year -- a 72% hike over the prior contract ending in 2013. The new NBA contract more than doubled to \$1.4 billion per year.

Disney is scheduled to release third quarter earnings during the first week of November, and ESPN could disappoint again.

In November, Disney will launch DisneyLife in Britain for \$15 a month, its first stand-alone subscription service with access to Disney and Pixar movies, as well as episodes of Disney Channel programs along with Disney's books and music. Although Disney has no plans to offer a stand-alone subscription service in the US, DisneyLife is a hedge for Disney. After running the platform in Europe, Disney will be better able to launch a US version if and when it becomes attractive to do so.

We originally recommended Disney (DIS) largely based on

the anticipation of the *Star Wars* movie opening, and DIS has been rising recently, making our position profitable. The anticipation is often worth more than the event itself. The movie opens on December 18th, and we recommend DIS until then. If there is a game-changing earnings report, we will advise with an email update.

Ford (F) reported strong third quarter earnings in late October of 45 cents per share, up 89 percent from one year ago. As we have been pointing in previous issues, earnings have been depressed because of down time and preparation for 24 new or refreshed vehicles, including Ford's new all-aluminum F-150 truck which weighs 700 pounds less than last year's model and gets close to 30 miles to the gallon. The F-150 is Ford's best-selling vehicle in the US and the company's most profitable product, even as volume has been held back by production capacity.

On the cost side, Ford is reducing the number of platforms it uses to produce its models, from 27 in 2007 to 9 by 2016, which will save billions of dollars through economies of scale, and give Ford more agility to adapt to changes in demand.

The strong third quarter earnings affirm Ford's decision to remake its best-selling vehicle into a lighter aluminum model. Sales of F-Series pickups reached a nine-year high, and sold for \$2,000 more than a year ago.

Earnings are expected to be \$1.93 next year, putting the forward price/earnings (P/E) ratio below 7. This P/E ratio is far too low for a stock offering a solid dividend along with growth prospects.

Freeport-McMoRan Copper & Gold (FCX) is the world's largest copper producer. It has suffered from a decline in copper prices which have been undermined by a slowdown in world-wide growth, principally in China. In October, FCX reported a loss of 15 cents a share, which was below expectations of an 8 cent loss.

FCX management is targeting significant additional reductions in capital spending and operating and administrative costs in response to weak market conditions in order to reduce costs to preserve its most valuable resources for anticipated improved market conditions in the future.

Chief Executive Richard Adkerson said, "We're prepared to do whatever it takes - whatever it takes - to keep our operations generating positive cash flows to protect our liquidity and hold onto these assets for a better day."

Freeport's primary strategic objective is "significant" reduction of its \$20.7 billion debt, and anticipates improved cash flow in 2016 and 2017 as it winds down project spending and increases production. The company also expects to provide detailed plans on how it will make its oil and gas business self-supporting.

We made a 643 percent gain during the last expansion, from March 2003 until December 2006, on Phelps Dodge, the largest copper producer back then, which was subsequently purchased by FCX. This was at a time when

China was expanding and exerting high demand for copper and other commodities. Now that China has grown into the world's second largest economy, it is transforming into an economy fueled by its own consumers, which has made its growth slower. However, recent devaluations of the yuan are bound to stimulate the Chinese economy.

Sooner or later, expanding economies around the world will be exerting increasing demand for the assets held by FCX. Evidently activist investor Carl Icahn agrees. He reports a stake of 88 million shares of FCX, which makes him its largest shareholder. He says, "When they are throwing stocks like this on the dump heap, it is time to buy them."

NCR Corp (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.

As we reported last month, NCR is expanding into the software sector. It recently launched a cloud-based software system for ATMs called Kalpana aimed at lowering costs for users. It also recently launched its cloud-based platform for the ATMs operated by the Industrial and Commercial Bank of China which has demonstrated substantial cost savings, especially in comparison to the bank's manual cash management system.

In late October, NCR reported mixed earnings. Revenue growth was positive by 5 percent, but currency losses from a strong dollar produced a 2 percent loss. The stock responded positively on this news, jumping 7 percent.

Even with currency headwinds, NCR expects to earn from \$2.70 to \$2.80 per share in the year ahead. At less than 10 times earnings, NCR is a value play.

Symantec (SYMC) is the dominant supplier of software for computer security and protection against viruses and other nuisances through its leading flagship brand, Norton. Nearly all of the Fortune 500 companies are Symantec customers. According to Symantec's latest annual Internet Security Threat Report, cyber-attacks against large corporations have jumped by 40% this year. If there ever was a more certain growth industry, protection from cyber espionage is it.

Advanced threats are on the rise, including ransomware, remote access trojans, advanced persistent threats (APTs) and zero day attacks. The process of discovering these advanced threats on individual computers, local area networks, and email gateways is cumbersome and often inefficient. In late October, SYMC introduced Symantec Advanced Threat Protection, the first solution that can detect and remediate

advanced threats from an organization's central console, rather than from a multitude of individual computers and local area networks.

Symantec Advanced Threat Protection includes a product called Symantec *Cynic*, a cloud-based service to discover and identify today's most advanced threats. It also includes another product called *Synapse*, which has the capability to collect suspicious activity across endpoints, networks, and email.

This new product follows SYMC's most recent focus on protecting devices from hackers, through its so-called "Internet of Things" (IoT) division. Things needing protection are devices controlled by an internal computer that is accessible by the internet. A prime example is a modern automobile, where hackers can literally steer the car and disable or lock the brakes from their remote keyboards. The risk of hackers tracking and hijacking extends to a wide range of devices, from industrial controls and medical devices to ATMs (especially those running on a *Windows* operating system), along with a plethora of consumer electronics.

Tetra Tech (TTEK) is a leading company in water technologies and environmental remediation with a healthy balance sheet for growth in strategic markets.

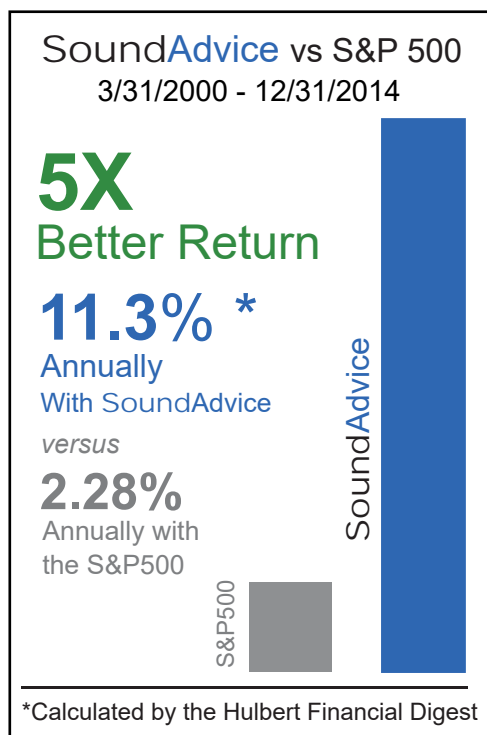
TTEK's latest contract was awarded in October for \$600 million to provide engineering services to develop infrastructures in 80 countries for providing access to clean water, sanitation, health care, schools, and energy, as well as transportation infrastructure.

This follows September's contract to conserve forested areas in Indonesia which are among the planet's most biologically diverse and carbon-rich ecosystems and offer the potential to mitigate global climate change through carbon sequestration.

Xerox (XRX) is continuing to transform from a seller of printers and copiers to a company providing business services in the form of business process outsourcing, information technology (IT) services, and document outsourcing (printing as a service). The services side now amounts to 55 percent of revenue. These outsourcing arrangements are long term in nature and encompass a wide range of profitable services for larger customers and result in contract renewals of close to 90 percent.

In late October, XRX reported earnings of 24 cents per share excluding one-time charges and amortization, beating expectations of 22 cents.

The company still expects to earn from \$0.95 to \$1.01 per share, which puts the stock price close to 10 times earnings, very cheap relative to the rest of the market.



Income With Growth	Sym	Exchange	Price	Yield	Limit	Action
Hersha Hospitality Trust	HT	NYSE	\$ 24.60	4.55%	\$ 28.42	BUY
Retail Opportunity Investment Corp	ROIC	NASDAQ	\$ 18.31	3.28%	\$ 19.00	BUY
Third Avenue Real Estate Value Investor	TVRVX	800-443-1021	\$ 31.44	1.40%	\$ 34.00	BUY
Diversified Growth						
Agrium	AGU	NYSE	\$ 94.23	3.31%	\$ 110.00	BUY
Disney	DIS	NYSE	\$ 115.04	1.15%	\$ 118.00	BUY
Ford Motor Company	F	NYSE	\$ 14.75	3.39%	\$ 17.00	BUY
Freeport-McMoRan	FCX	NYSE	\$ 11.82	1.69%	\$ 14.00	BUY
NCR Corp	NCR	NYSE	\$ 27.15	0.00%	\$ 30.00	BUY
Pfizer	PFE	NYSE	\$ 35.06	3.19%	\$ 36.00	BUY
Stryker Corp.	SYK	NYSE	\$ 96.71	1.10%	\$ 105.00	BUY
Tetra Tech	TTEK	NASDAQ	\$ 27.00	1.19%	\$ 27.00	BUY
Third Avenue Small-Cap Value Investor Fund	TVSVX	800-443-1021	\$ 22.58	0.00%	\$ 24.00	BUY
Xerox	XRX	NYSE	\$ 9.69	2.58%	\$ 11.00	BUY
Energy/Natural Resources						
Chesapeake Energy Corp	CHK	NYSE	\$ 7.45	0.00%	\$ 10.00	BUY
Chevron	CVX	NYSE	\$ 94.96	4.51%	\$ 100.00	BUY
Fidelity Select Nat. Gas Fund	FSNGX	800-544-8888	\$ 25.48	1.30%	\$ 30.00	BUY
ICON Energy Fund Class S	ICENX	800-828-4881	\$ 12.44	0.72%	\$ 14.00	BUY
Transocean	RIG	NYSE	\$ 16.70	0.00%	\$ 17.00	BUY
Valero	VLO	NYSE	\$ 68.03	2.94%	\$ 70.00	BUY
Aggressive Growth						
Boston Scientific	BSX	NYSE	\$ 18.86	0.00%	\$ 19.50	BUY
ETF - Direxion Daily 20+ Yr Bear 3X	TMV	NYSE	\$ 27.99	0.00%	\$ 34.00	BUY
ETF - ProShares Short 20+ Year Trsry	TBF	NYSE	\$ 24.67	0.00%	\$ 26.00	BUY
ETF - ProShares UltraShort 20+ Year Trsry	TBT	NYSE	\$ 43.92	0.00%	\$ 47.00	BUY
S&P 500 ProShares Ultra Short ETF	SDS	NYSE	\$ 19.20	0.00%	\$ 22.00	BUY
Symantec	SYMC	NASDAQ	\$ 20.70	2.90%	\$ 23.00	BUY
Tekla Life Sciences Fund	HQL	NYSE	\$ 26.79	0.00%	\$ 28.00	BUY

Notes to the table:

Prices are as of 11/1/2015. See our website for live pricing and buy limits:

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

Yields on funds may include capital gain distributions.

This table has live prices, charts & buy limits on our website: <http://www.soundadvice-newsletter.com/members>

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, 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. The table above divides the portfolio into four sectors; Income with Growth, Diversified Growth, Energy and Natural Resources, and Aggressive Growth.

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 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 \$12.2 million in stocks and to \$1.54 million in houses.

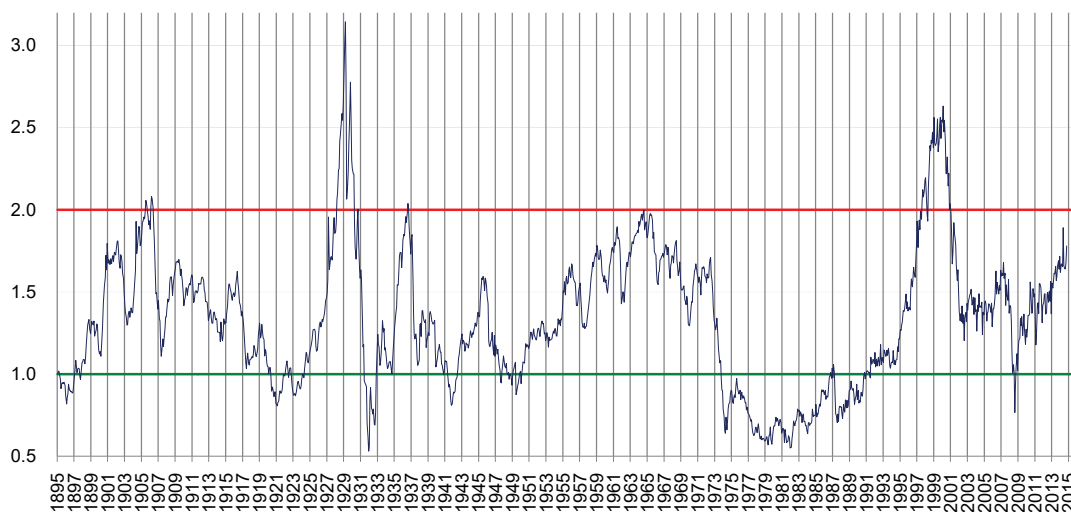
But though an investment beginning with \$25,000 in 1895 could have made money being in either stocks or housing and simply leaving it there over such a long period of time, had the investor followed the signals of the SoundAdvice Risk Indicator he would have made \$483 million, or 39.7 times more money—the 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 1.69. This reading reveals that stock prices are 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 soft economy is providing an atmosphere for stable or declining interest rates.

This Diffusion Index gave us a zero reading in March, 2015.

The previous zero reading was 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.

However, the March 2015 signal was usurped.

The SoundAdvice Diffusion Index of Lagging Indicators gives "Caution" signals when all three of its individual lagging economic indicators rise above their respective levels of six months earlier, providing a 100 percent reading which reveals that the economy is about to put upward pressures on interest rates.

This 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. Although we operated under the "Caution" signal, we have continued to be bullish about stocks because of the Federal Reserve's expansive monetary policy and its quantitative easing program, which has been distorting the natural business cycle.

The lagging economic indicators released in June, 2015, (for May) caused the SoundAdvice Diffusion Index of Lagging indicators to hit 100 percent, giving us a new caution signal.

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 31.7 percent. During "Caution" signals, the S&P 500 increased an average of 1.9 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
Ave +/-	31.7%		1.9%

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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