

Words from the Wise

eResearch Corporation is pleased to provide an article by Keith Richards of **VALUETREND**.

In this article, Mr. Richards looks at the market sectors in both Canada and the USA and analyzes the annual sector rotation. Hero to Zero and back again.

The article is reproduced below, beginning on the next page, or you can go directly to it at the following link: <http://www.valuetrend.ca/todays-hero-becomes-tomorrows-zero/>

You can also visit the **VALUETREND** website at the link below:
<http://www.valuetrend.ca/>

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Bob Weir, CFA: Director of Research

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Wednesday, May 31, 2017

Words from the Wise

By: Keith Richards (bio at end)

At ValueTrend, we pride ourselves in being one of the more open and “fully disclosing” Portfolio Managers on the street. Our clients receive very detailed e-mail updates on the existing positions held within our models, including current and future expectations as to when we might be selling these holdings, or buying new positions in the future.

Most Portfolio Managers do not give a heads-up to their clients on these kinds of moves.

While this information only goes out to our clients, I like to reprint the occasional “ValueTrend Update”, which is the name of our e-mailed client update.

BTW—even as a non-client, if you subscribe via our website’s newsletter sign-up, you will get an abbreviated version of these updates sent to you. The newsletter covers a birds-eye view of our current and future positioning, so it may be of value to you even if we do not disclose the individual stock or ETF names we are trading.

Today’s blog is taken from our most recent client update.

“There are times to buy blue-chip stocks, cyclical stocks, corporate bonds, U.S. Treasury instruments, and so on. And there are times to sit on cash, because sometimes cash enables you to take advantage of investment opportunities.”

- John Templeton

We are making some moves in your ValueTrend Equity Platform that we thought you would like hearing about.

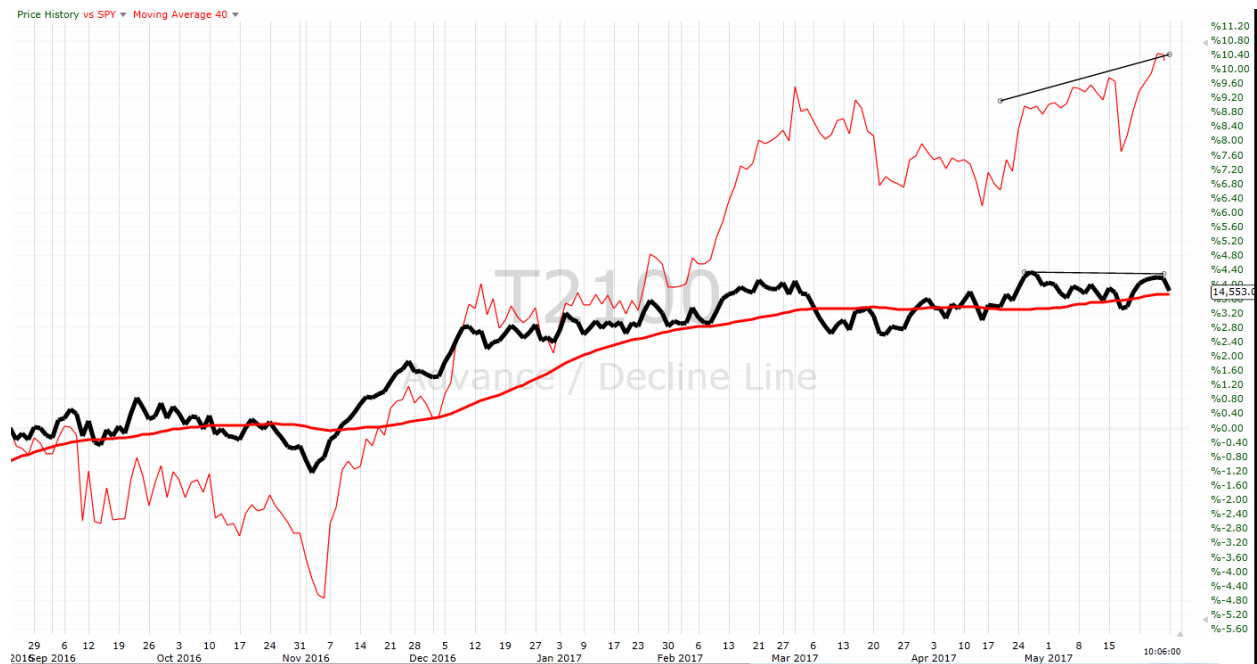
Our outlook for the stock market is for choppy or possibly bearish behavior this summer. No, we cannot say for sure that a correction will happen. Assuming markets do decline – pinpointing the timing of that occurrence is unlikely.

Despite the fact that we cannot be certain of what the markets will do, we can quantitatively measure risk and return...and make decisions to overweight or underweight stocks based on that quantitative data. With this in mind, here are a few factors from our “Bear-o-meter” that are making us cautious right now:

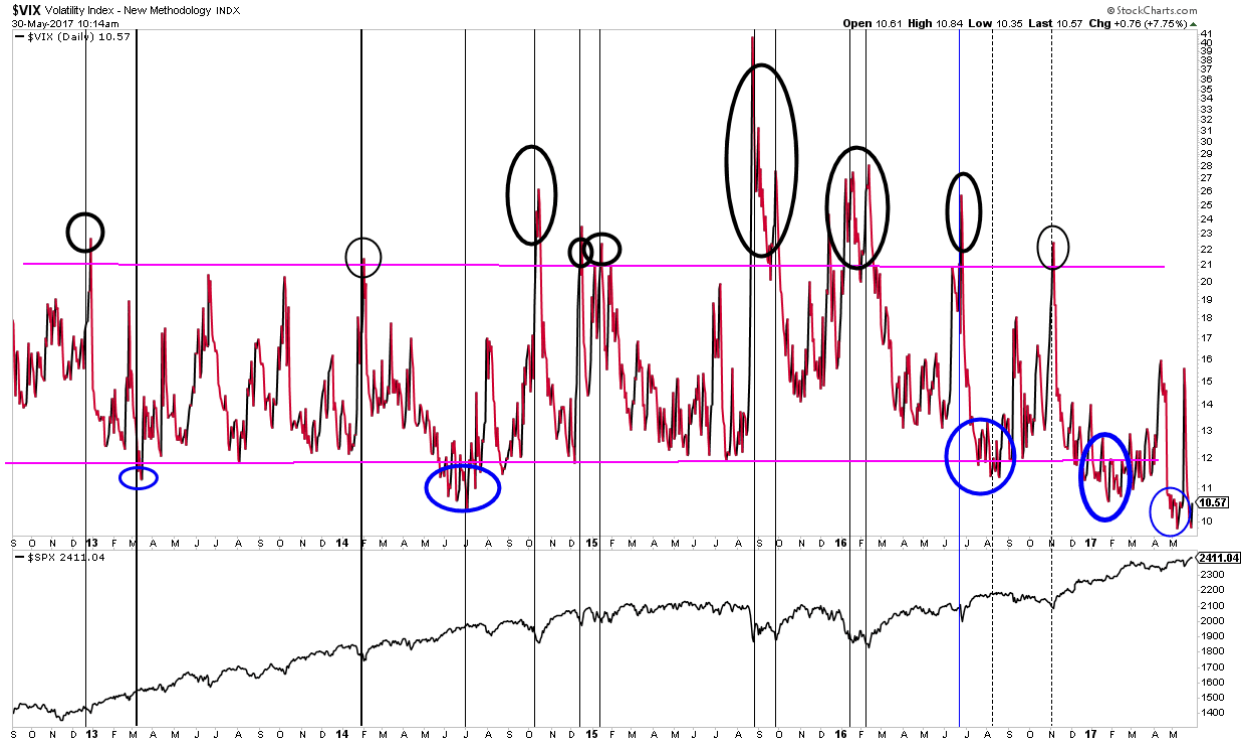
- **Seasonality:** We are into the “Worst Six Months” period for the stock market, which does not end until November. Studies have proven that – over time – it is wise to be cautious over the summer months – especially coming into the fall.
- **Sentiment:** Sentiment studies show a current high confidence level of “dumb” money. Dumb money tracks retail investors through mutual fund and ETF flow, as well as small speculator trades. These less-knowledgeable investors are confident right now, and that is bad – because they are usually wrong at market extremes. Interestingly, smart money is also confident, which is unusual –

sentimentrader.com shows that returns are typically flat to negative in the month following such coincidences following a new market high.

- **Breadth:** Markets have risen on only a few concentrated sectors that are rising, with more sectors falling. Such a development is akin to a doctor's patient who appears healthy externally, but displays internal signs of disease. Note the failure to make new highs on the black AD line below, vs. the new highs on the S&P 500 (red line). Chart courtesy www.freestockcharts.com.



- **Volatility:** The "VIX" is a measurement of option premiums. It measures implied volatility on the markets. It shows us when investors are confident, or when they are worried. When investors are too confident, the VIX is low – and that is a bad thing. You need some investor fear in order to keep the market from running away on itself. Right now, as shown on the chart on the next page, the VIX is exceedingly low – meaning that investors are too bullish, and don't think there will be much volatility. It is currently at the same level as it was in 2007 – when investor confidence was high. Does anyone recall what happened after 2007?



- Elliott Wave Prognosis:** This is not part of our "Bear-o-meter", but we thought you would find it interesting. According to Elliott Wave Theory, markets move in 3 "up" waves with 2 pull backs separating these 3 waves. Each wave has characteristics. The final wave is characterized by a rapid rise and lower volatility (see the above comment re the VIX). There is a good chance that we are ready for a strong correction in the coming months. Please read [this blog](#) for details. Below is a chart of the current market with its waves marked on it.



What We Are Doing About It

The ValueTrend Equity Platform hit new highs recently, and we want to keep those gains.

We are now at 33% cash in the equity model. We expect to raise a little more—perhaps even as high as 40% cash- in the coming weeks by selling a few more positions. We will also be looking for an entry point into the U.S. long treasury bond via an ETF. We expect that as/if/when the market corrects – money will flow back into bonds (which sold off over the winter) as a safe haven. That should make them rise a bit over the summer, plus pay the portfolio some interest.

Remember that ValueTrend has consistently had its BEST years when markets are down. That's right – bad news for most investors is good news to our clients! Yes, you will still see some volatility. The only way to avoid such volatility is to completely step out of the market, which would imply that we are 100% certain of its direction. Sorry folks, nobody is THAT good!

Our strategy is to SELL when risk vs return potential is high, and then use that cash to BUY when the blood is running on the streets. We hold the cash then leap on opportunities when our indicators flash green.

Most of you have been with us long enough to have seen us do this effectively before. We cannot tell you the exact date or time we might re-enter with the cash we raise. Nor can we assure you that the markets will fall and provide us with cheap buying opportunities on stocks. They could keep rising, and we might regret holding cash.

However, we can say with a HIGH degree of certainty that market conditions are quantitatively, historically, and logically high risk right now! We can also assure you that it will not be emotion that keeps us in or out of the markets this summer. We will follow our system, and hopefully this should duplicate the success we have had in past market sell-offs.

Again, to quote John Templeton:

"To buy when others are despondently selling and to sell when others are avidly buying requires the greatest of fortitude and pays the greatest ultimate rewards."

Keith on BNN

I will be on BNN's call-in show MarketCall on Monday June 12th from 1:00pm to 2:00pm. Tune in to BNN to catch me live on BNN's premier call-in show, where viewers like yourself can ask my technical opinion on the stocks you hold.

Call in with questions during the show's live taping between 1:00 and 2:00 pm. The toll free number for questions is 1 855 326 6266. You can also email questions ahead of time to marketcall@bnn.ca – but it is important that you specify the question is for me.

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See **About The Author** below.

ABOUT THE AUTHOR



ValueTrend Founder and Owner, Keith Richards, has been in the securities industry since 1990. ValueTrend manages over \$100 million through a discretionary investment service for high-net-worth clients.

Keith Richards has been in the securities industry since 1990 and is a highly regarded member of the small, exclusive community of Chartered Market Technicians in Canada. Mr. Richard's articles appear regularly in INVESTORS DIGEST, MONEYLETTER, GLOBE AND MAIL, and the TORONTO STAR newspapers.

His appearances on BNN Television have inspired producers to acknowledge him as **“one of [our] most accurate technical analysts.”** Mr. Richard's first book, SMARTBOUNCE: 3 ACTION STEPS TO PORTFOLIO RECOVERY, is available in bookstores and directly through his blog page www.valuetrend.ca/blog/. His second book, SIDEWAYS: USING THE POWER OF TECHNICAL ANALYSIS TO PROFIT IN UNCERTAIN TIMES was released in late 2011. He has been critical of the commission-based, follow-the-pack approach to investing – where brokers succeed regardless of performance.

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