

*Real Investment Report*

# Examining The Most Hated Bull Market Ever!



- *Examining The Most Hated Bull Market Ever*
- *Sector & Market Analysis*
- *401k Plan Manager*

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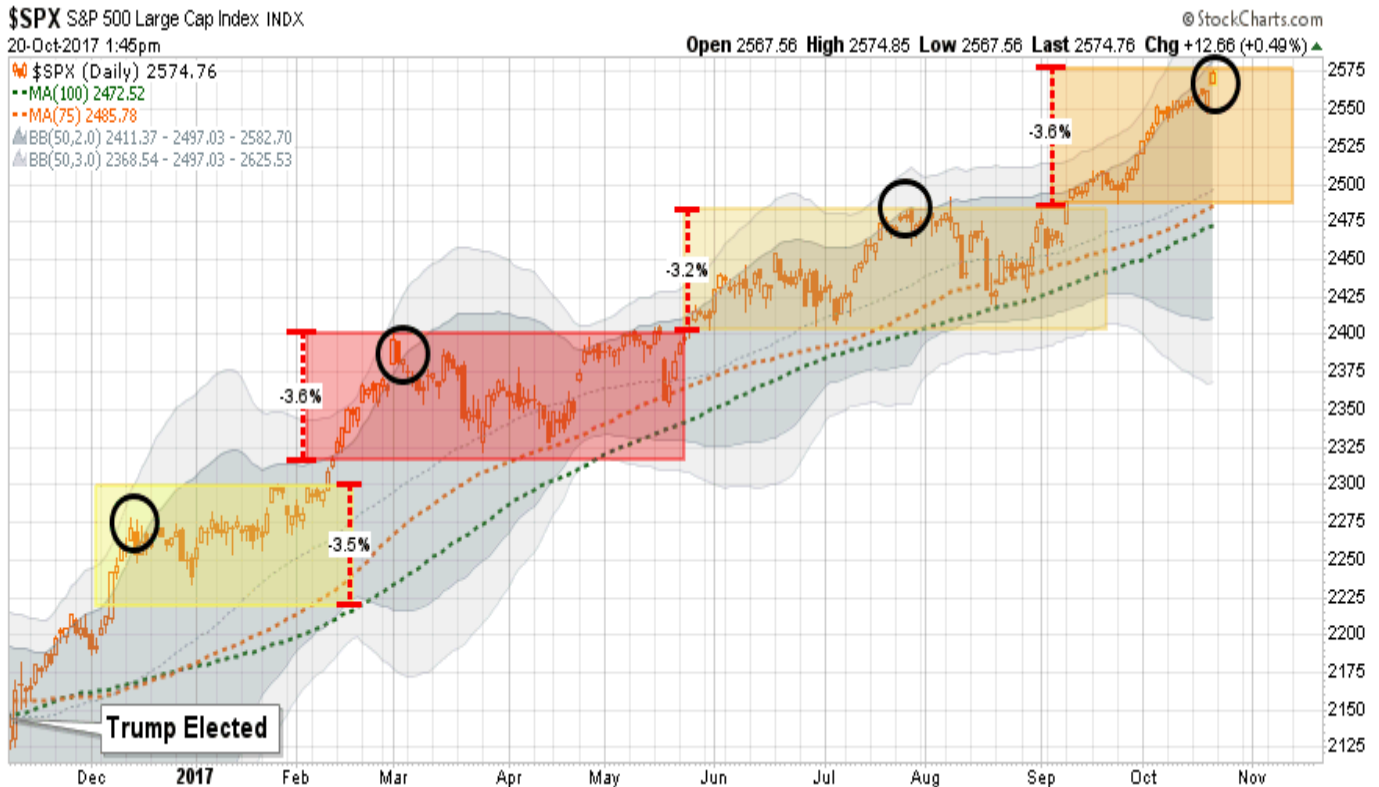
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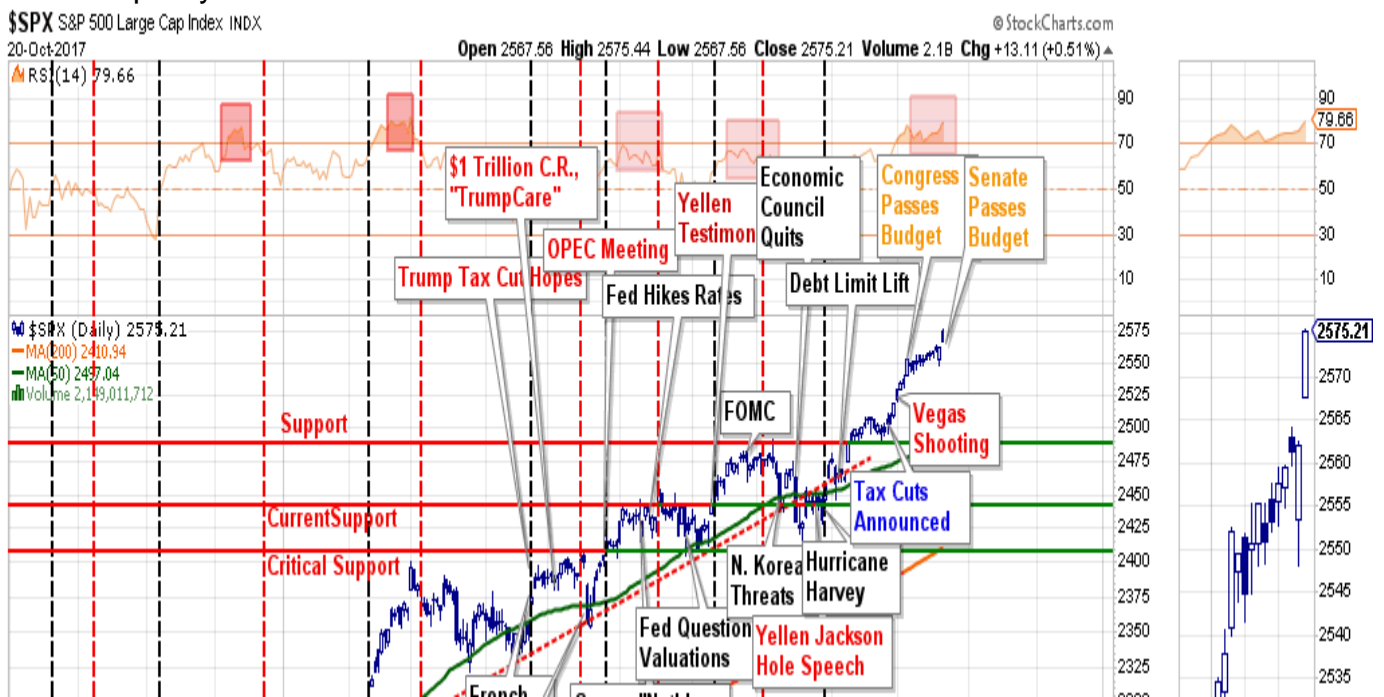
# Examining The "Most Hated Bull Market Ever"

From [lastweek:](#)

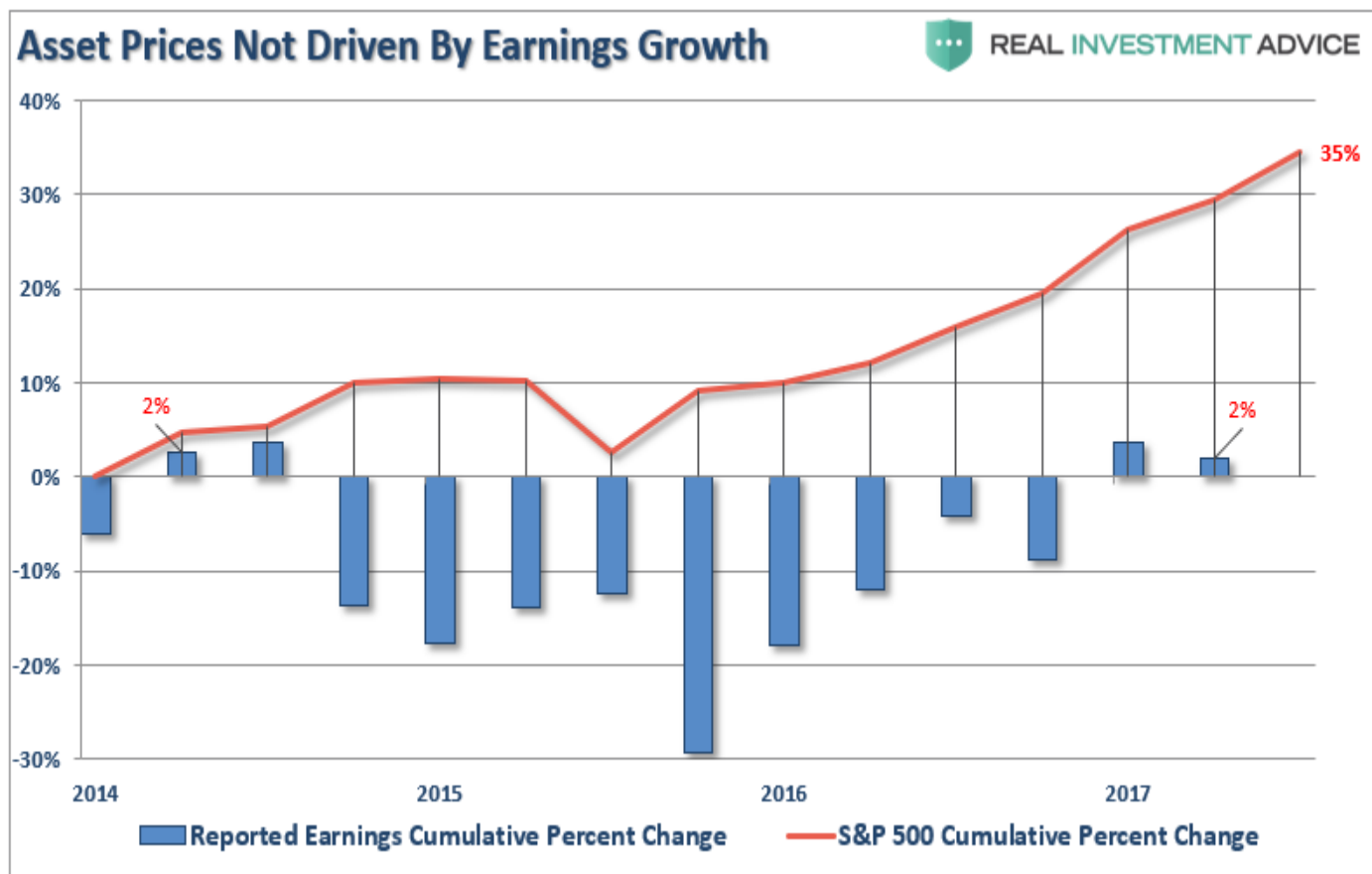
*"The seemingly "impervious" advance since the election last November, has had an interesting "stair step" pattern with each advance commencing from a breakout of a several month 3%-ish consolidation range. Furthermore, each advance then pushes to a 3-standard deviation extreme, black circles, of the 50-dma before beginning the next consolidation trading range."*



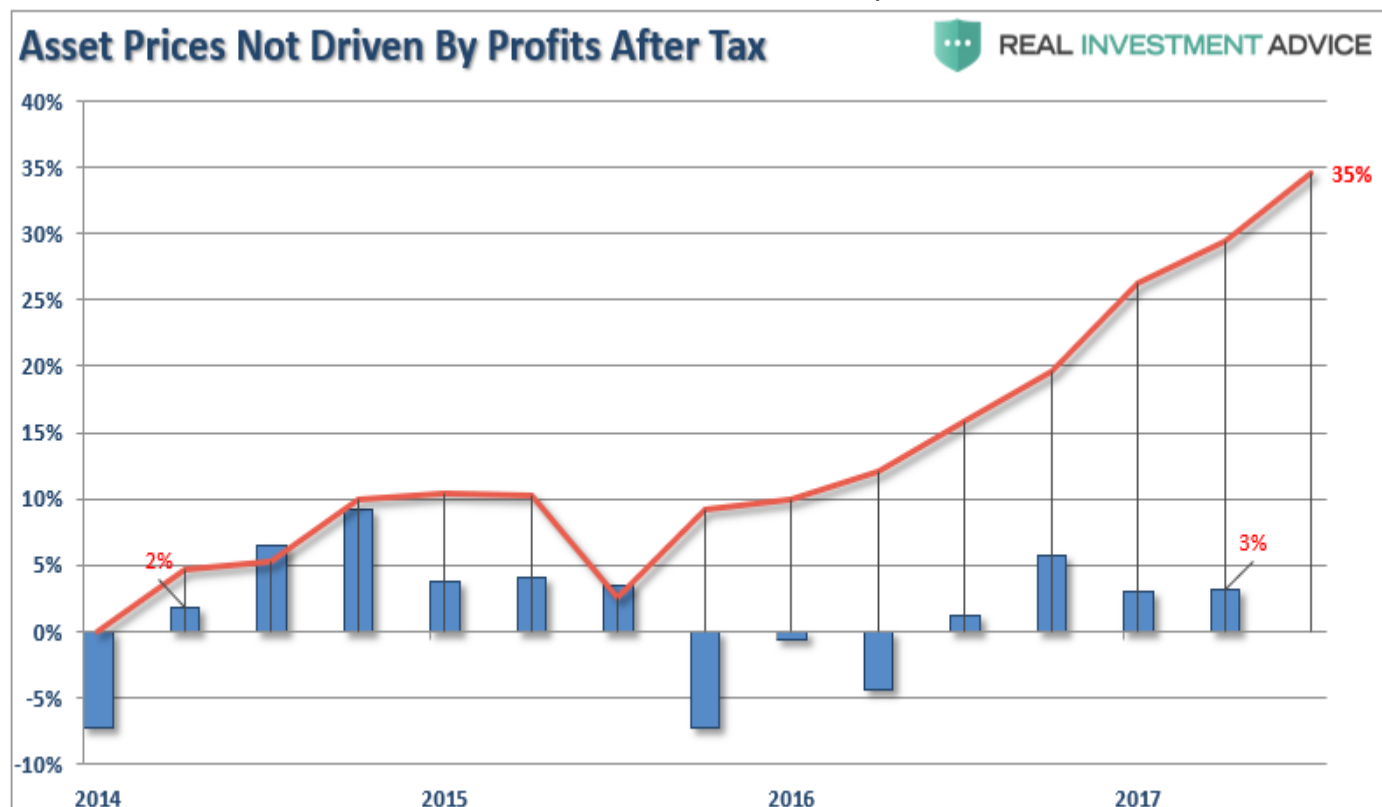
The last leg higher has been directly responsive to the ramp up in the political "marketing surge" surrounding "tax cuts and tax reform." With the House having already passed their respective budget resolutions, late Thursday, the Senate passed a budget blueprint for the next fiscal year. **With both of the "budget resolutions" in place, it was seen as clearing a hurdle to the goal of overhauling the tax code.** This is not new, of course, as the entire rally for the markets since the election has been driven by hopes of lower taxes, despite disaster, floods, fires and Central Bank threats of liquidity extraction.



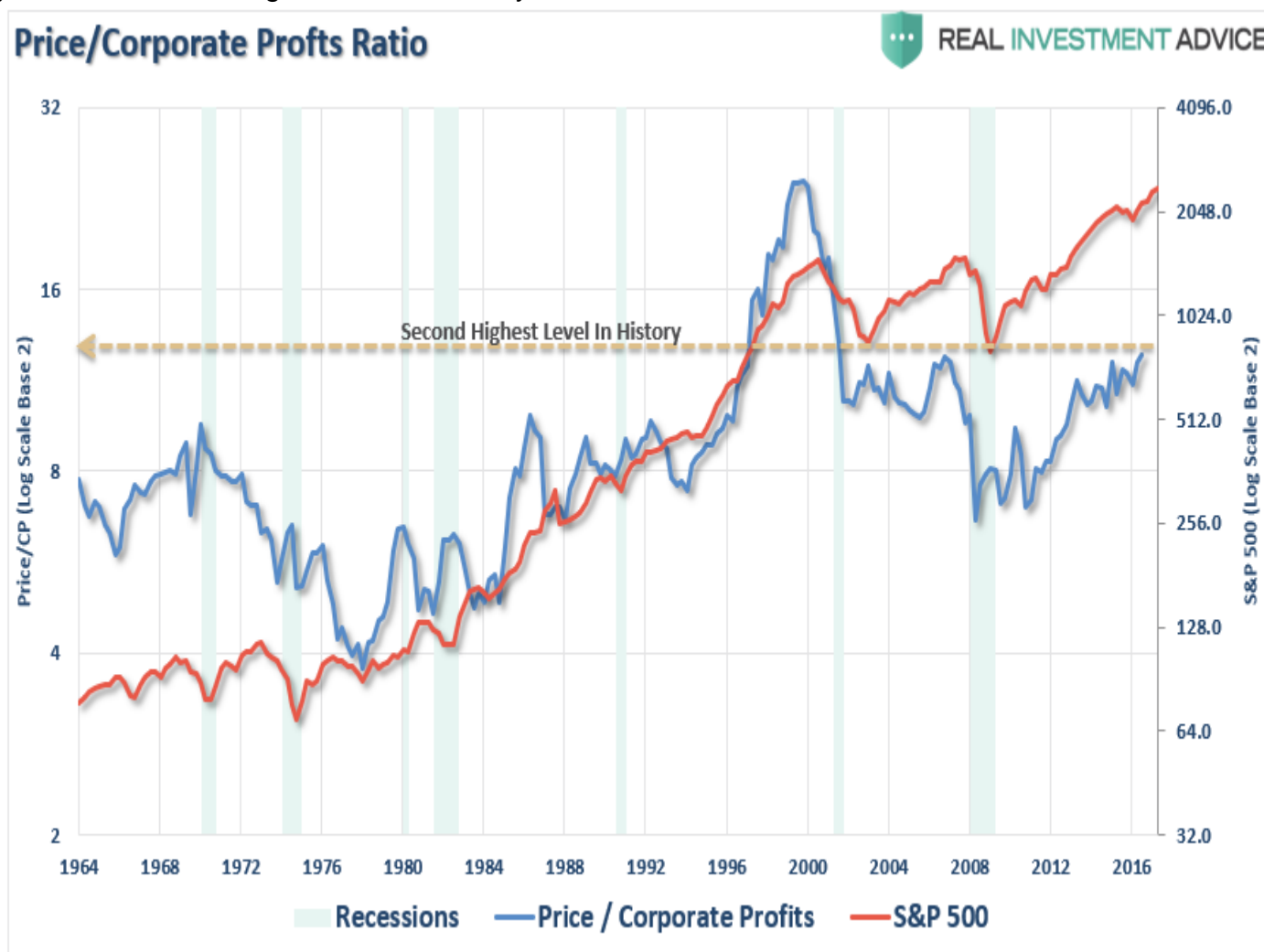
The bulls are clearly in charge which keeps us allocated to towards equity risk currently. Do not be mistaken, this "rally" ~~is~~ all about tax cuts. **Despite many who are suggesting this has been a "rational rise" due to strong earnings growth, that is simply not the case as shown below. (I only use "reported earnings" which includes all the "bad stuff." Any analysis using "operating earnings" is misleading.)**



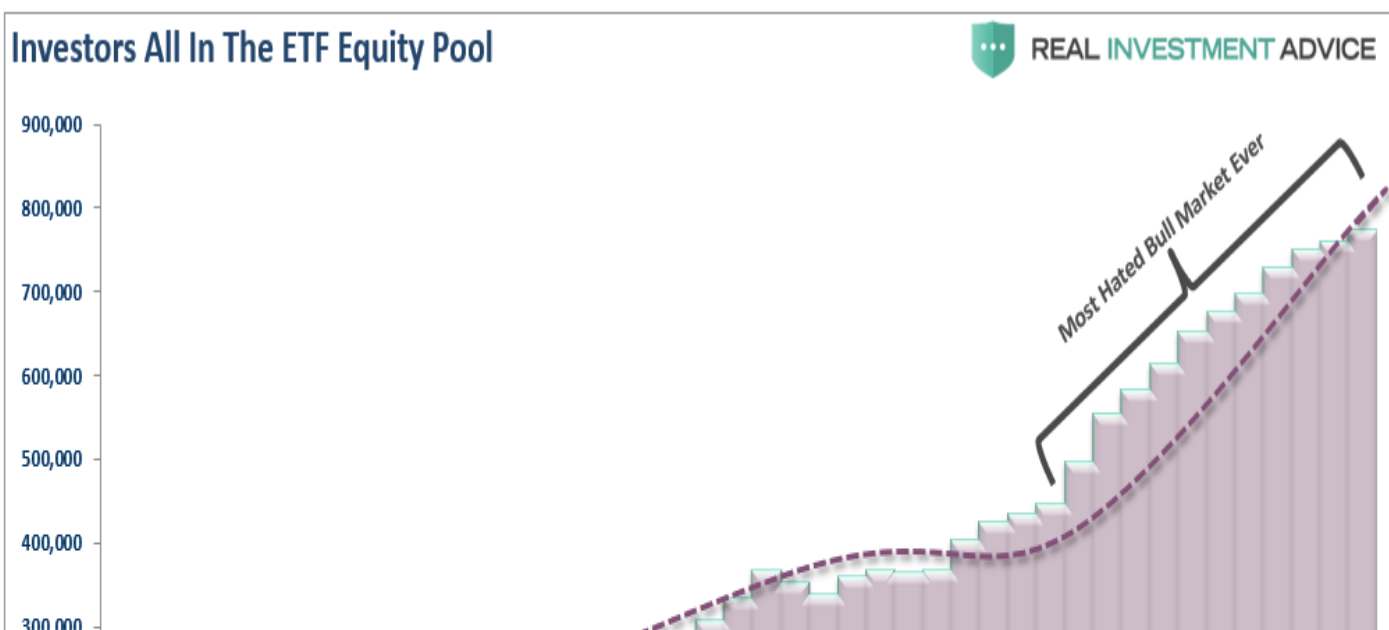
Since 2014, the stock market has risen (*capital appreciation only*) by 35% while reported earnings growth has risen by a whopping 2%. **A 2% growth in earnings over the last 3-years hardly justifies a 33% premium over earnings.** Of course, even reported earnings is somewhat misleading due to the heavy use of share repurchases to artificially inflate reported earnings on a per share basis. However, corporate profits after tax give us a better idea of what profits actually were since that is the amount left over after those taxes were paid.



Again we see the same picture of a 32% premium over a 3% cumulative growth in corporate profits after tax. There is little justification to be found to support the idea that earnings growth is the main driver behind asset prices currently. We can also use the data above to construct a valuation measure of price divided by corporate profits after tax. As with all valuation measures [we have discussed as of late](#), and forward return expectations from such levels, the P/CPATAX ratio just hit the second highest level in history.



The reality, of course, is that investors are simply chasing asset prices higher as **exuberance overtakes logic and their actions prove the case.** According to data from FactSet, stock-based exchange-traded funds have seen nearly \$16 billion in inflows over the past week, which represents an acceleration from recent positioning. Over the past month, about \$31.3 billion has gone into stock-based ETFs. The chart below of data from ICI shows much of the same with monthly equity ETF inflows surging since the election.



The same is seen when we also add in equity mutual funds for a look at total equity asset flows.



noted:

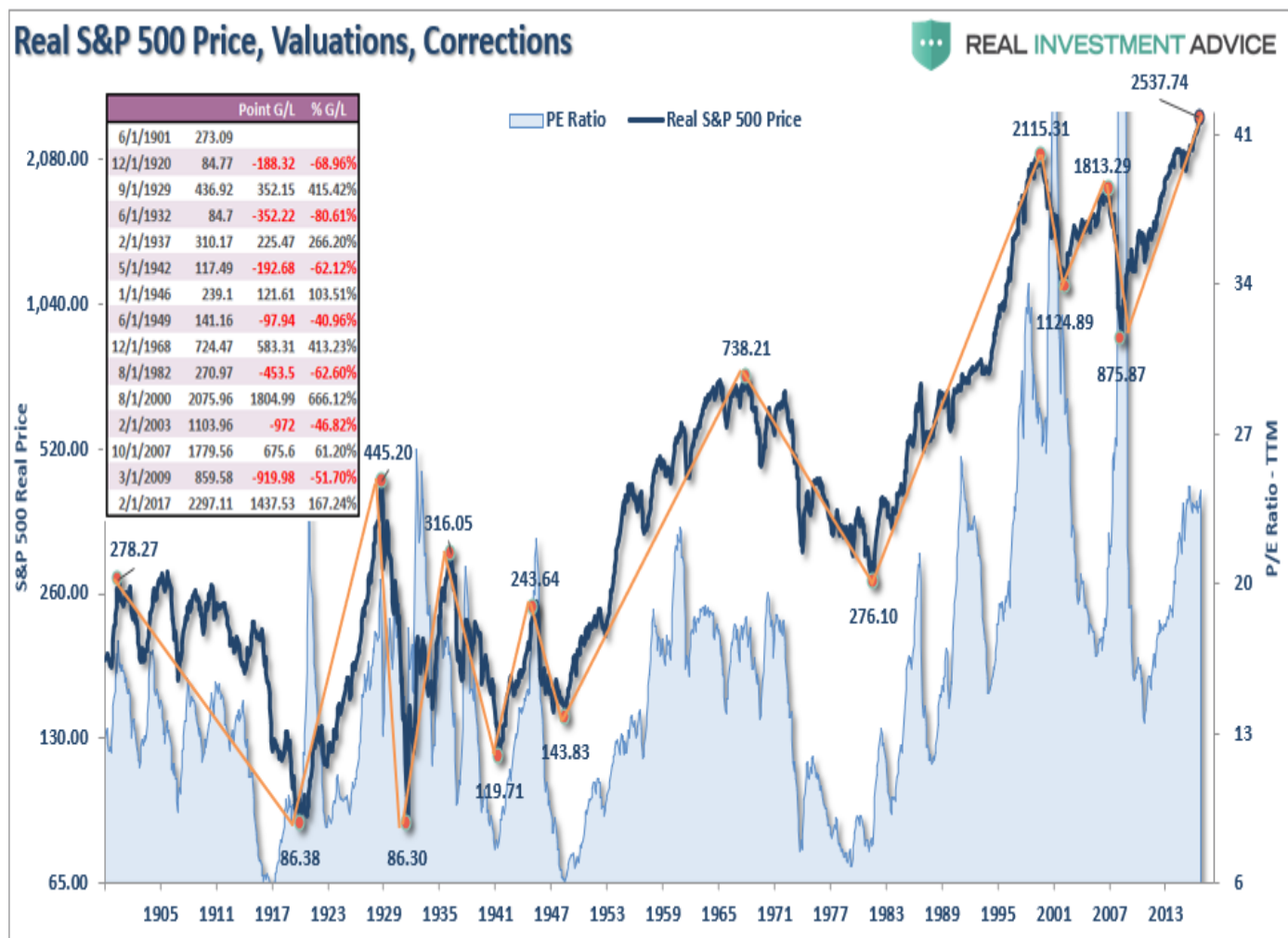
*"Consumer sentiment surged in early October, reaching its highest level since the start of 2004. **The October gain was broadly shared, occurring among all age and income subgroups and across all partisan viewpoints. There is an unmistakable***



**sense among consumers that economic prospects are now about as 'good as it gets.'"**

**Most hated bull market ever...hardly.**

Historically speaking, **you only witness such exuberance in the latter stages of an expansion, not the beginnings of one.** The latest survey indicates that consumers do not anticipate an economic downturn anytime in the foreseeable future, which from a contrarian perspective may be a clear warning sign. **Clearly, the expected benefits of tax cuts and reforms is leading investors to overpay for something today they are hoping will become fairly valued tomorrow.** In other words, instead of prices catching "down" to market fundamentals, investors are hoping fundamentals will "catch up" to prices. Unfortunately, there isn't a previous case in history where this has been the case.

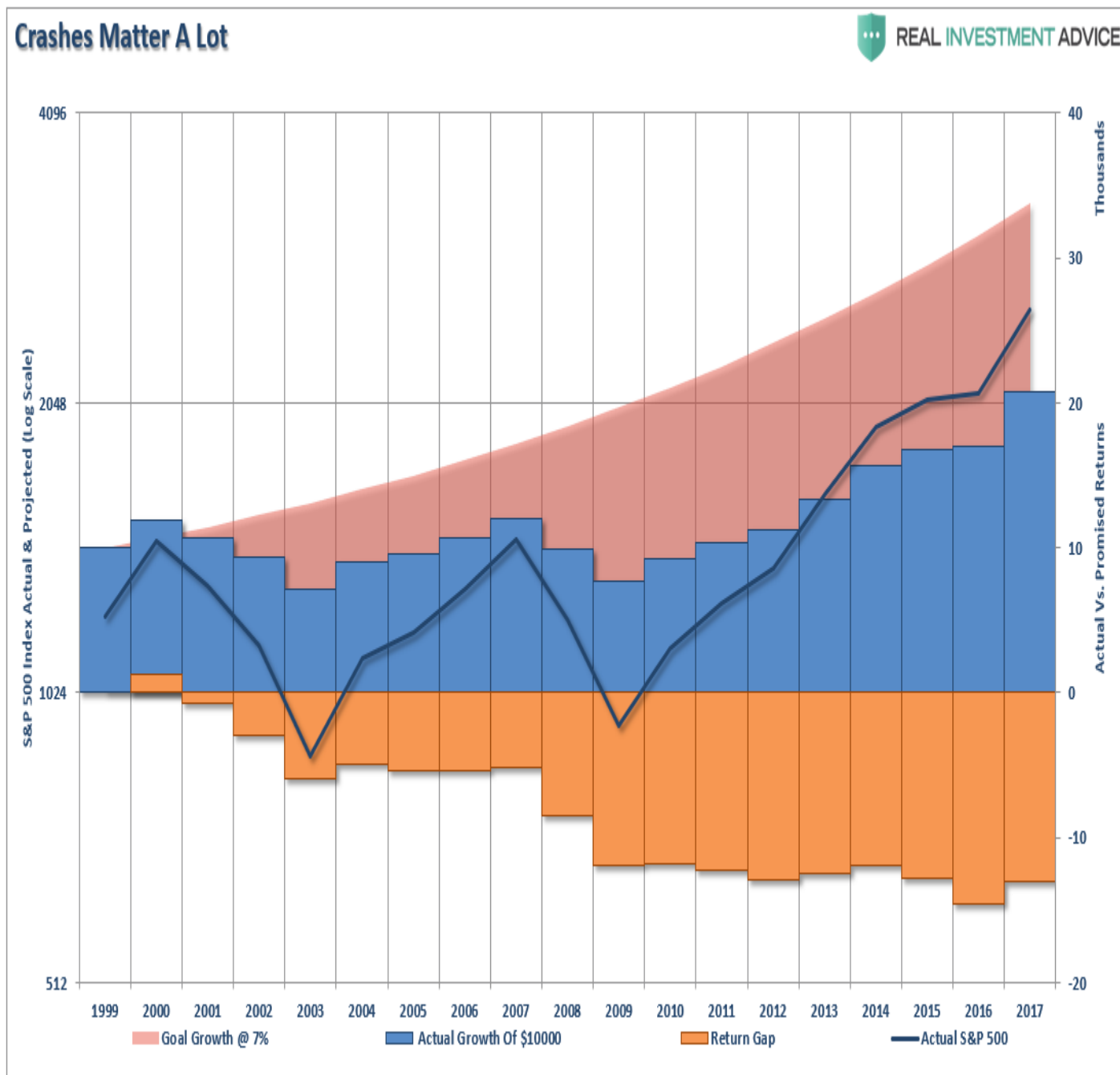


Also, when we look at 20-year trailing returns, there is **sufficient historical evidence to suggest total, real returns, will decline towards zero over the next 3-years from 7% annualized currently.**

*(These are trailing 20-year total real returns, not forward)*



Re-read that last sentence again and look closely at the chart above. From current valuation levels, the annualized return on stocks by the end of the current 20-year cycle will be close to 0%. **A decline in the next 3-years of only 30%, the average drawdown during a recession, will achieve that goal.** For investors, this is crucially important. In the article ["Apathy & The Death Of Your Financial Goals,"](#) I discussed the reality of the damage caused by market drawdowns. As I stated: *"Crashes matter, a lot."*

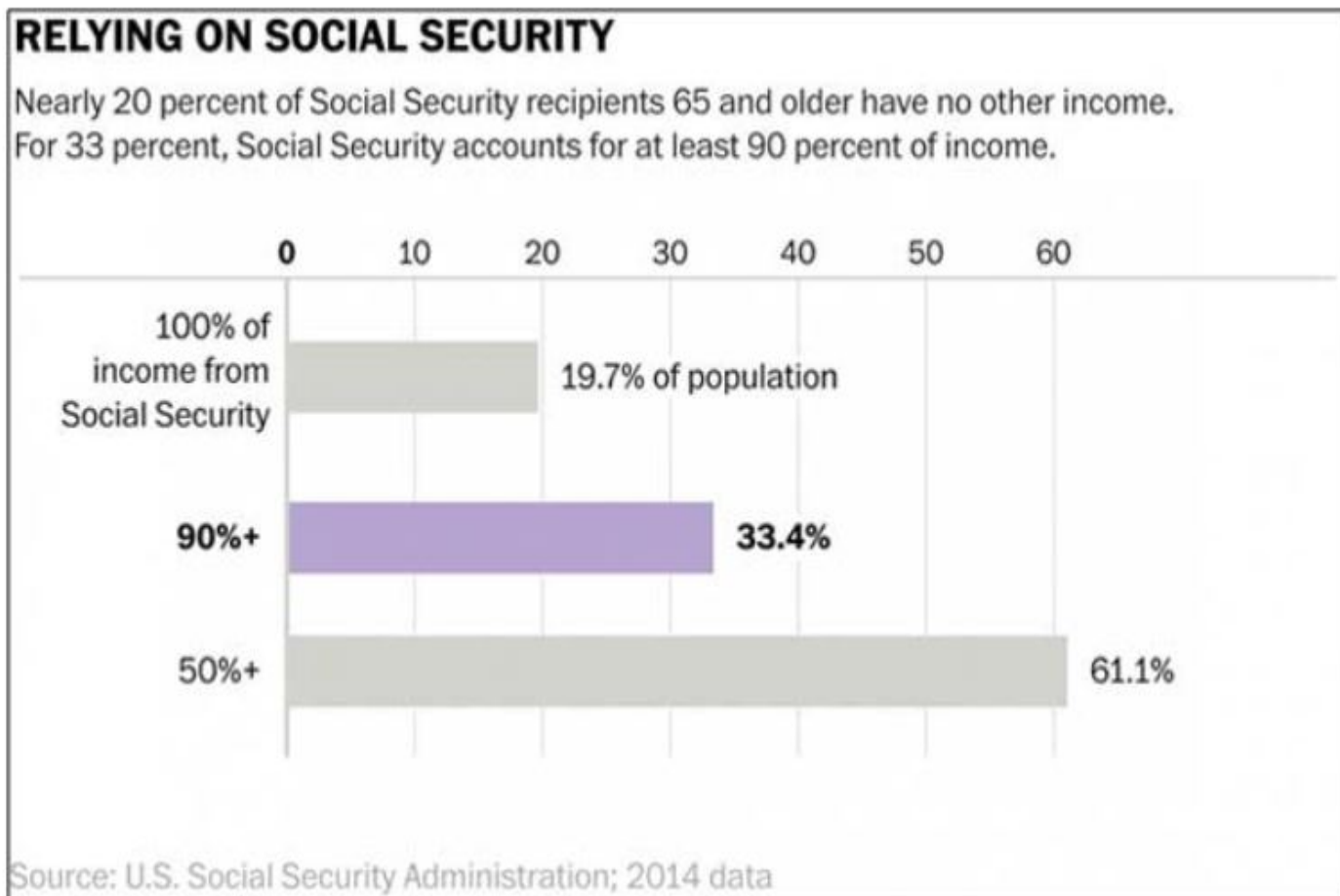


**While investors may "get back to even," eventually, following a crash, the shortfall from their actual financial goal continues to build.** This is why using some method of risk management, such as a simple moving average crossover, can help alleviate some of the financial damage caused by drawdowns.

- **YES!** You will miss out on some gains in the market.
- **YES!** Sometimes you will be "stopped out" and have to "buy back in."
- **YES!** You will be much more successful in obtaining your financial goals long-term.

After all, isn't that why you invest in the first place? **What I can assure you of is that you WILL be wrong from time to time and you WILL lose money. But that is the inherent nature of investing. It is a "RISK" based endeavor.** However, I can absolutely guarantee that trying to

"passively index" in the current market environment will absolutely wind up screwing up your long-term goals. Think about it this way. **IF investing was as easy as just buying a bunch of stuff and sitting on it, then why are so many Americans dependent on Social Security for retirement?** Via Jared Dillian:



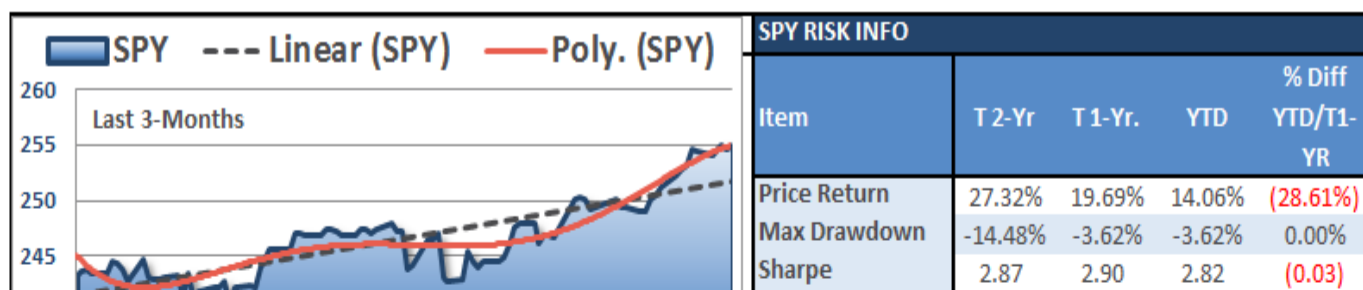
- 19.7% of retirees get 100% of their income from Social Security.
- A full third (33.4%) depend on it for 90% of their income.
- And 61.1% get at least half their income from Social Security.

The federal government's unfunded 75-year liability for Social Security and Medicare combined is **\$46.7 trillion**. Are you absolutely sure you want to rely on the Government for your retirement? Think about it the next time someone tells you to just "*buy and hold*."

## Market & Sector Analysis

Data Analysis Of The Market & Sectors For Traders

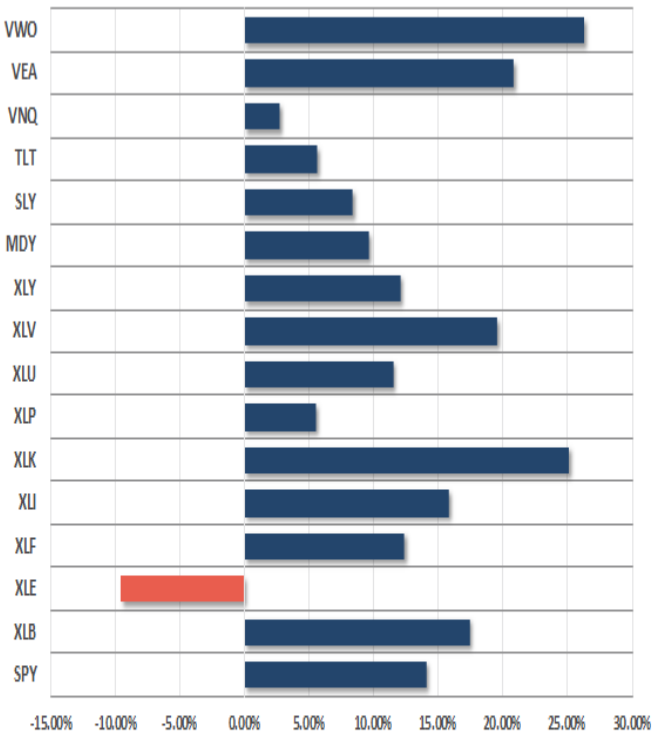
### S&P 500 Tear Sheet



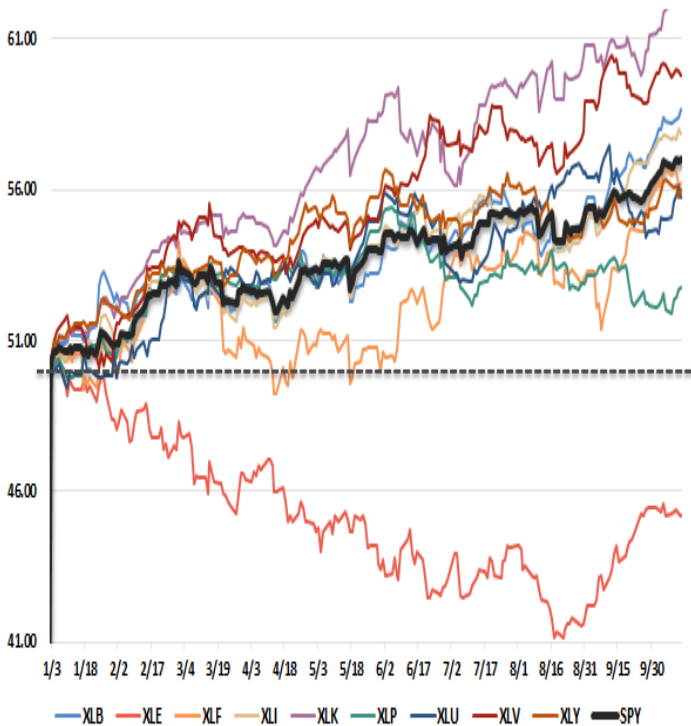


# Performance Analysis

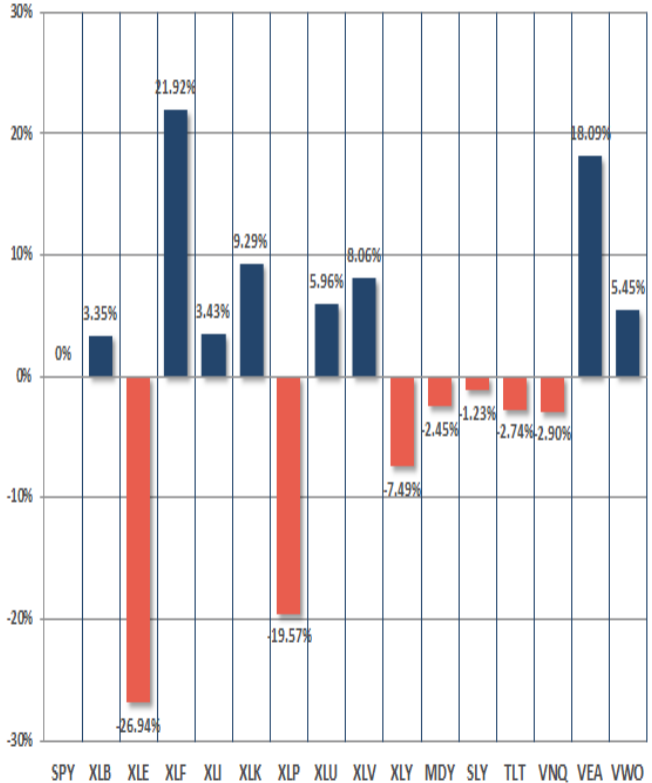
Year To Date Performance



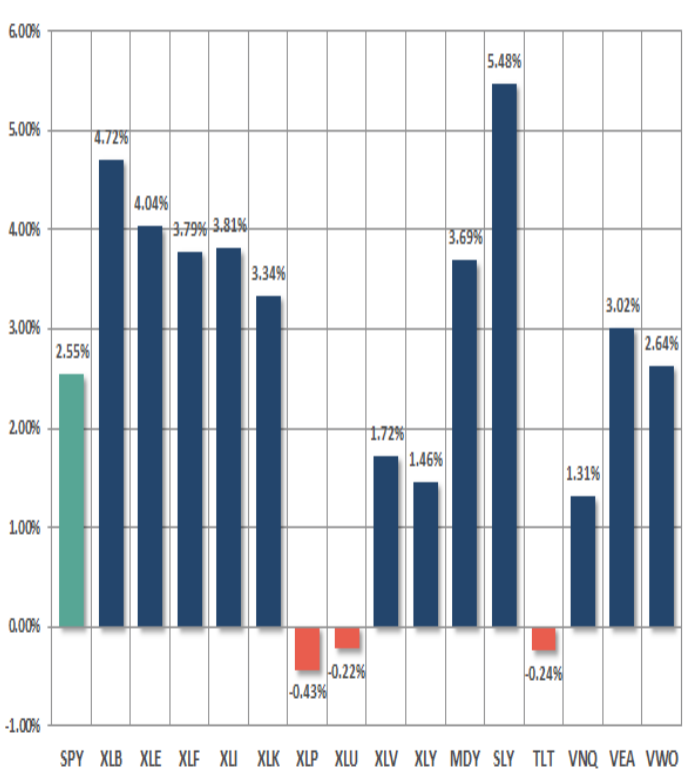
YTD Price - S&P Sectors Recalibrated To \$50/share



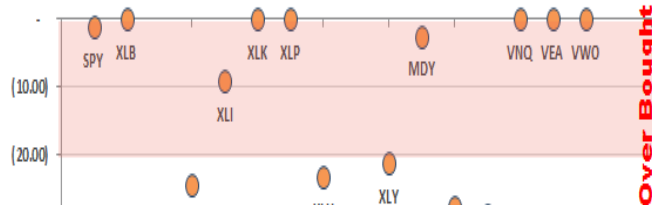
Year To Date Performance Relative To S&P 500



Price Deviation From 50-Day Moving Average



Overbought/Oversold 14-Periods



Size / Sector ETF YTD Trading Range



# ETF Model Relative Performance Analysis

	RELATIVE PERFORMANCE	TICKER	ETF NAME	Current Price	Model Position Price Changes Relative to Index					SHORT WMA	LONG WMA	% DEV - Short M/A	% DEV - Long M/A	Buy / Sell Signal
					1 Week	4 Week	12 Weeks	24 Weeks	52 Weeks					
	BENCHMARK	IVV	ISHARS-SP500	256.63	0.20	1.78	3.25	7.13	19.76	250.03	244.24	2.64%	5.07%	BUY
TACTICAL	SECTORS	XLB	SPDR-MATLS SELS	58.35	0.57	2.29	2.34	2.82	6.21	55.58	53.98	4.99%	8.10%	BUY
		XLE	SPDR-EGY SELS	68.14	(0.10)	1.71	1.40	(6.68)	(22.14)	65.57	67.04	3.92%	1.64%	SELL
		XLF	SPDR-FINL SELS	26.13	(1.04)	3.71	2.11	3.92	14.79	25.14	24.45	3.94%	6.86%	BUY
		XLI	SPDR-INDU SELS	72.06	(0.04)	2.07	1.52	1.50	6.15	69.25	67.60	4.06%	6.59%	BUY
		XLK	SPDR-TECH SELS	60.50	0.71	1.22	2.02	4.13	7.96	58.29	55.91	3.80%	8.21%	BUY
		XLP	SPDR-CONS STPL	54.57	1.21	(2.96)	(4.18)	(8.23)	(15.56)	54.89	55.15	-0.58%	-1.05%	SELL
		XLU	SPDR-UTIL SELS	54.15	1.14	(2.88)	(1.64)	(2.39)	(6.36)	53.99	52.79	0.29%	2.57%	BUY
		XLV	SPDR-HLTH CR	82.42	(0.77)	(1.99)	(1.49)	2.04	(1.37)	80.81	77.92	1.99%	5.78%	BUY
		XLY	SPDR-CONS DISCR	91.22	(0.75)	(0.01)	(3.15)	(5.84)	(4.13)	90.20	89.33	1.13%	2.11%	BUY
	SIZE	MGK	VANGD-MG CAP GR	106.75	0.44	(0.19)	0.15	1.78	4.20	103.80	100.23	2.85%	6.50%	BUY
		IJR	ISHARS-SP SC600	74.59	(0.88)	3.60	1.44	(0.25)	3.65	70.81	69.86	5.34%	6.77%	BUY
CORE	Equal Weight Market	RSP	GUGG-SP5 EQ ETF	96.54	(0.15)	0.52	(0.89)	(1.53)	(1.58)	94.09	92.53	2.60%	4.33%	BUY
	Dividend	VIG	VANGD-DIV APPRC	96.03	0.16	(0.26)	(0.76)	(2.16)	(3.10)	93.71	92.34	2.47%	3.99%	BUY
	Real Estate	VNQ	VIPERS-REIT	84.79	1.59	(2.43)	(2.01)	(4.71)	(17.70)	83.76	83.39	1.23%	1.68%	BUY
	International	IDV	ISHARS-INTL SD	33.98	1.14	(1.49)	(1.76)	(0.30)	(3.75)	33.54	32.63	1.31%	4.14%	BUY
		VWO	VANGD-FTSE EM	45.18	1.62	(1.51)	2.81	4.87	1.30	43.75	41.62	3.27%	8.55%	BUY
FI	Intermediate Duration	TLT	ISHARS-20+YTB	125.85	1.63	(2.58)	(3.12)	(4.26)	(24.12)	125.78	123.71	0.06%	1.73%	BUY
	International	BNDX	VANGD-TTL INT B	54.69	0.12	(1.62)	(2.88)	(6.50)	(21.04)	54.63	54.44	0.12%	0.47%	BUY
	High Yield	HYG	ISHARS-IBX HYCB	88.33	(0.28)	(1.87)	(3.70)	(6.89)	(18.07)	88.31	88.00	0.02%	0.38%	BUY
	Cash	BSV	VANGD-SHT TRM B	79.78										

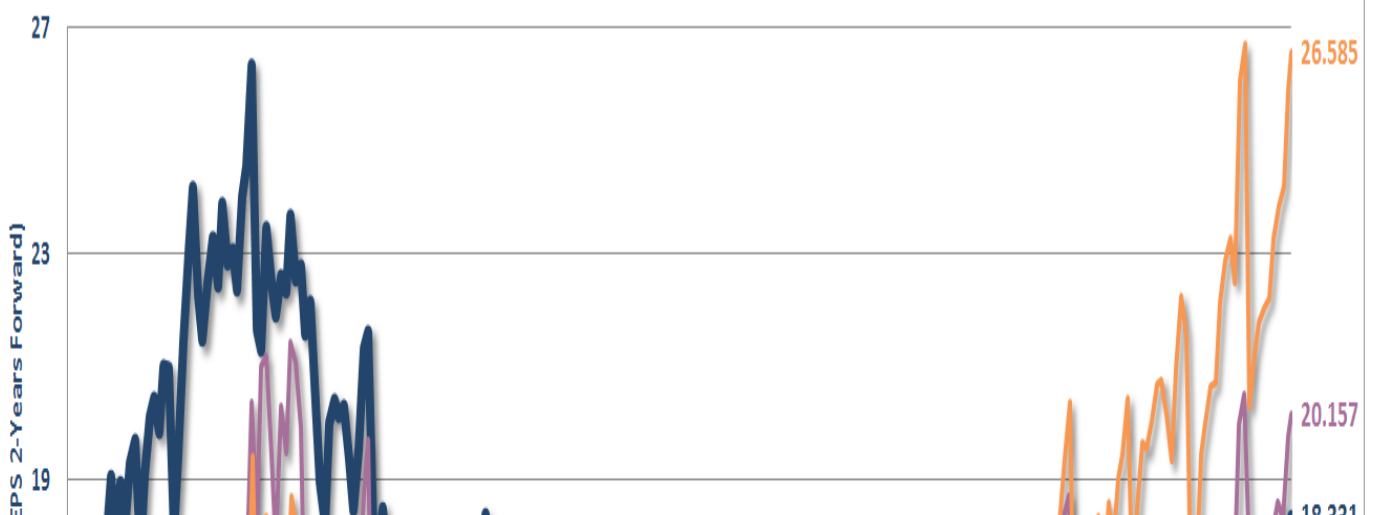
REAL INVESTMENT ADVICE

## Sector & Market Analysis:

The bull market continues to be fueled by hopes that tax cuts and tax reform will lead to higher reported earnings for corporations. **While it is true that tax cuts will improve earnings, whatever improvement is given is likely already priced into forward operating estimates over the next two years.** With small caps and the Russell 2000 at the highest valuations since the "dot.com" crash, the risk of disappointment is elevated.

### Current P/E Based On 2-Year Forward Estimates

REAL INVESTMENT ADVICE



But that is a story for another day. Currently, there is little concern for such matters as investors continued to pile into equities last week in anticipation of "tax cuts" by Christmas. • As I noted on Friday, don't be surprised if we see Dow 24,000 by the time [\*"Santa visits Broad & Wall."\*](#)

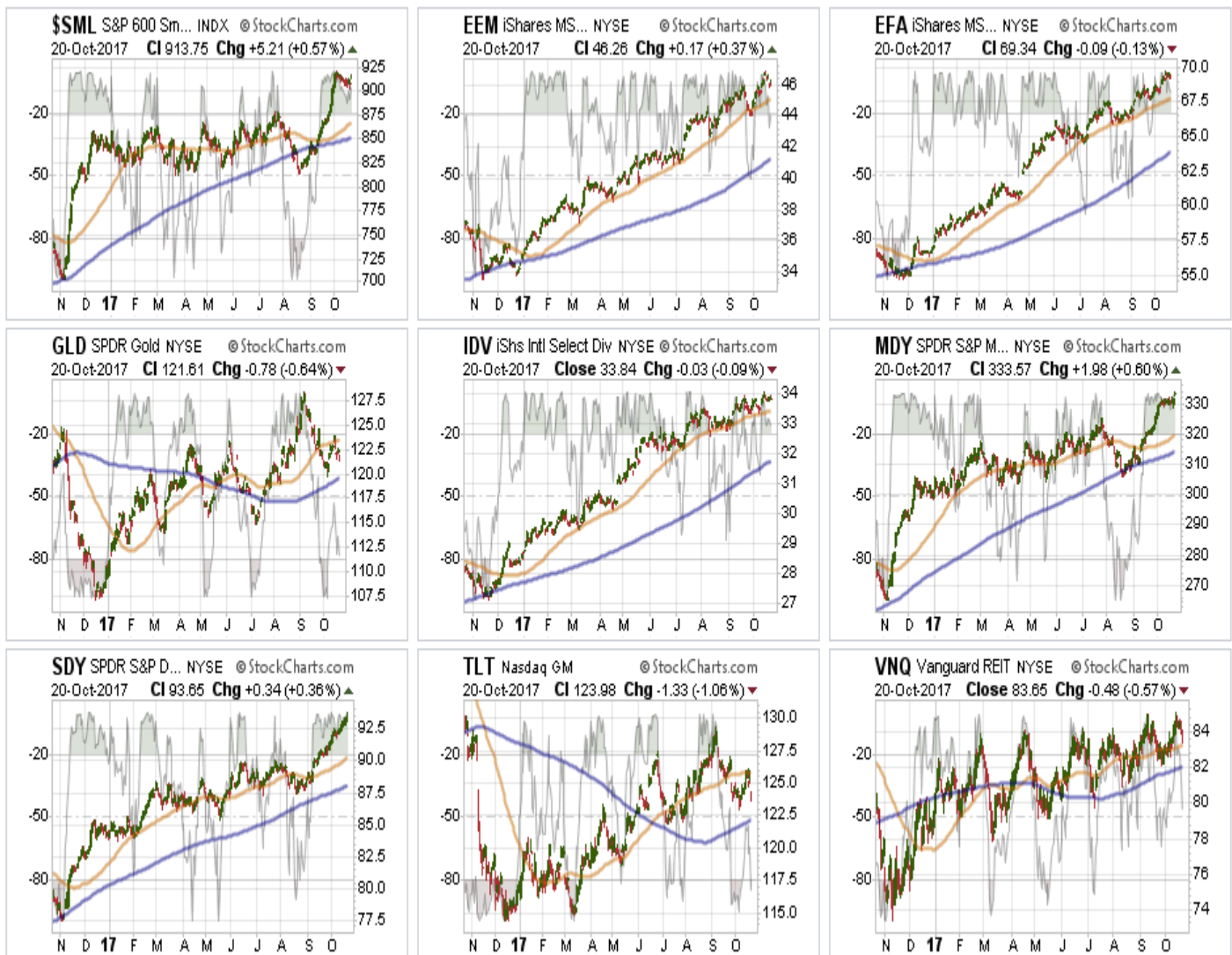


**Technology, Industrials, and Materials** - continued their charge again this past week as movement toward tax cuts boosted these sectors higher. These sectors are EXTREMELY overbought short-term. Taking some gains in is likely a good idea at this juncture, but remain weighted in these sectors for now. **Financials and Healthcare** had stumbled a bit previously but regained their footing this past week as bank earnings came in and the Administration has agreed to bail out "ObamaCare" for at least 2-years (*translated that means "forever" in Government speak*). Trends remain bullish, but are overbought as is the market in general. **Energy** as I stated over the last couple of weeks, had mustered a decent oversold bounce but the trends and backdrop remain sorely negative. As I penned previously:

***"With oil prices struggling at \$52/share, the current price move is largely done for now."***

While the underlying technicals are beginning to improve, the sector must stay above the 50-dma while working off the extremely overbought condition that currently exists. A violation will likely return the sector back to its previous downtrend. **We continue to remain out of the sector entirely currently, but if the recent improvement can reverse the negative trends we will add weight to portfolios.** **Discretionary and Staples** remain under pressure as the consumer weakness continues to spread through the underlying companies. That story is a macroeconomic story that is being ignored by the rest of the market currently, however, **it will eventually be the "tail that**

**wags to dog.** •While Discretionary remains in a positive trend, **Staples are showing significant weakness. Reduce exposure with the break of the 200-dma for now.** •Utilities, as noted last week, were VERY oversold and the pop in interest rates following the announcement of the Trump Tax Plan led to a violation of the 50-dma. However, as stated last week, Utilities have picked up performance lately and are testing previous highs. Remain long the sector and move stops up to recent lows.



**Small and Mid-Cap stocks** have stalled over the last two weeks and remain extremely overbought. •Stops should be moved up accordingly. As stated two weeks ago:

*"The moves to new highs for both markets provides some impetus for the market's push higher in the short-term."*

We previously took some gains out of these sectors but remain long for now. •**Emerging Markets and International Stocks** continue to hold support and money has been chasing performance in these sectors as of late. Remain long these sectors for now.

**NOTE:** Correlation between all markets is extremely high. What goes up together also comes down together. •

**Gold** • Last week, the precious metal failed to break back above the 50-dma. As money is chasing equities currently, and there is NO FEAR of a crash, gold has temporarily "lost its luster" as a safe haven. **With the recent passage of budgets in both the House and Senate, the push to "tax reform" has gained a lot of steam over the last week. This makes gold a much less optimal investment at the moment.** We continue to watch the commodity currently, but remain on the



sidelines for now. **S&P Dividend Stocks**, after adding some additional exposure recently the index broke out to new highs and continues to climb. We are holding our positions for now with stops moved up to recent lows. Take some profits and rebalance accordingly. **Dividend stocks have gotten WAY ahead of themselves currently as the yield chase continues. Bonds and REITs** took a hit this week as "tax reform" moved forward and the expectations for higher inflation, wages, and economic growth pushed rates higher. While the economic benefit from tax reform is "WAY OVERSTATED," we will continue to add more exposure if rates push towards 2.5-2.6% which is our target for this reversal.

## Sector Recommendations:

The table below shows thoughts on specific actions related to the current market environment. •

*(These are not recommendations or solicitations to take any action. This is for informational purposes only related to market extremes and contrarian positioning within portfolios. Use at your own risk and peril.)*



						OVERWEIGHT	BUY	HOLD	REDUCE	SELL	Notes
		Over Bought / Sold	50/200 DMA	Trend	Action	OVERWEIGHT	BUY	HOLD	REDUCE	SELL	
XLV	Discretionary	OB	Positive	Positive	Hold			X			Reduce To Target Weight
XLK	Technology	OB	Positive	Positive	Hold			X			Reduce To Target Weight
XLI	Industrials	OB	Positive	Positive	Hold			X			Reduce To Target Weight
XLB	Materials	OB	Positive	Positive	Hold			X			Reduce To Target Weight
XLE	Energy	OB	Negative	Negative	No Position						No Position/Improving
XLP	Staples	OS	Positive	Positive	Reduce			=>	X		Below 50 & 200-dma
XLV	Health Care	OB	Positive	Positive	Hold			X			Reduce To Target Weight
XLU	Utilities	Improving	Positive	Positive	Hold			X			Hold
XLF	Financials	OB	Positive	Positive	Hold			X			Reduce To Target Weight
\$SML	Small Caps	OB	Positive	Positive	Hold			X			Reduce To Target Weight
EEM	Emerging Mkt	OB	Positive	Positive	Hold			X			Reduce To Target Weight
EFA	International	OB	Positive	Positive	Hold			X			Reduce To Target Weight
GLD	Gold	Declining	Positive	Positive	No Position						Watching
IDV	Int'l Dividend	OB	Positive	Positive	Hold			X			Reduce To Target Weight
MDY	Mid Cap	OB	Positive	Positive	Hold			X			Reduce To Target Weight
SDY	SP500 Dividend	OB	Positive	Positive	Hold			X			Reduce To Target Weight
TLT	20+ Yr. Bond	OS	Positive	Positive	Hold			X			Hold
VNQ	REIT's	Declining	Positive	Positive	Hold			X			Hold

LEGEND: X = THIS WEEK => PREVIOUS DECLINING <= PREVIOUS IMPROVING

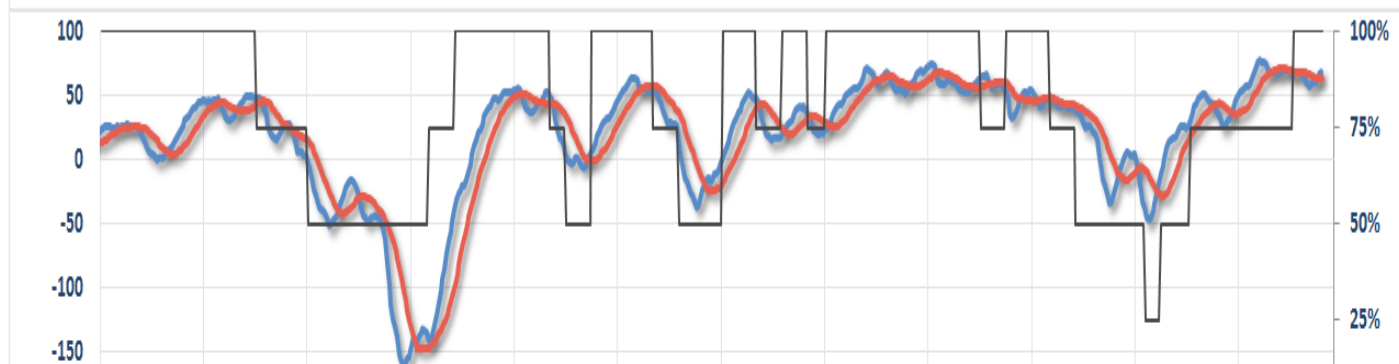
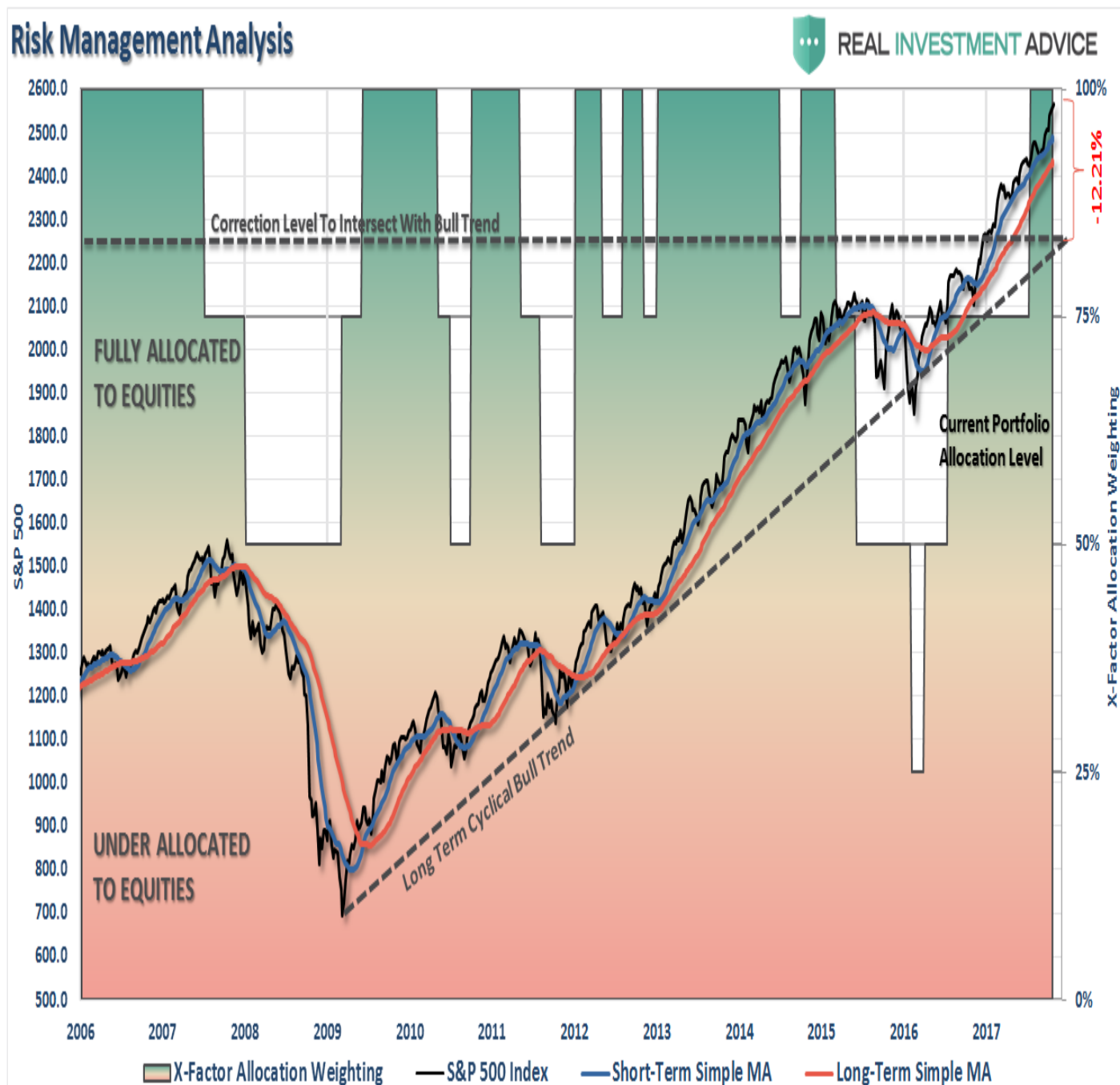
**Portfolio Update: No changes this past week.** We used the pop in interest rates to move cash management accounts, and larger cash holdings, into our cash allocation strategy providing for better yields. • **We also added some new bond exposure to accounts and are looking for additional opportunities if rates push higher over the next couple of weeks.** We remain extremely vigilant of the risk that we are undertaking by chasing markets at such extended levels, but our job is to make money as opportunities present themselves. **Importantly, stops have been**



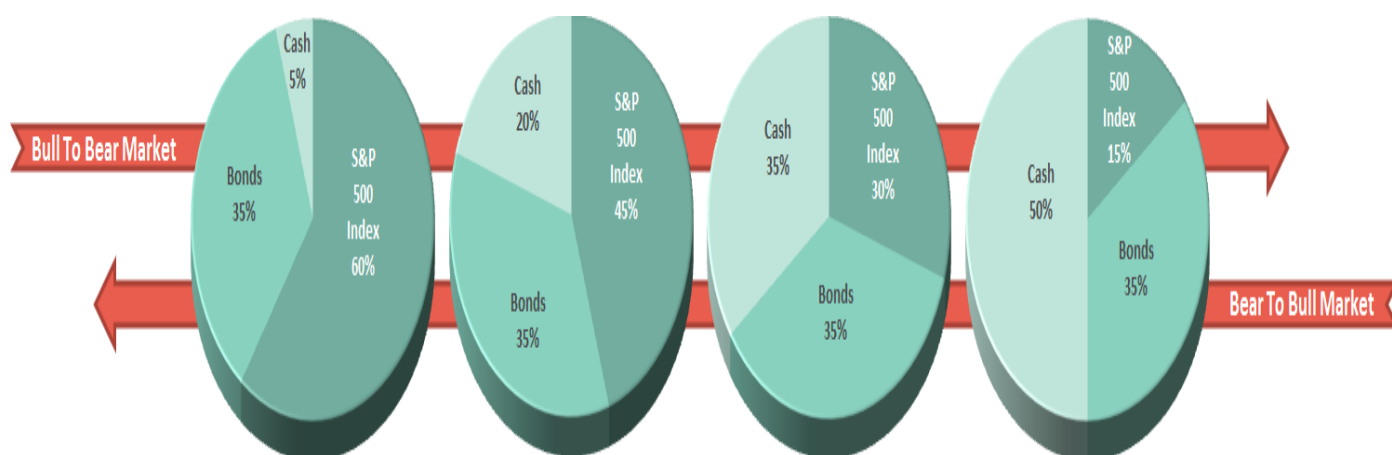
**raised to trailing support levels** and we continue to look for ways to "de-risk" portfolios at this late stage of a bull market advance. **As always, we remain invested but are becoming highly concerned about the underlying risk. Our main goal remains capital preservation.**•

## THE REAL 401k PLAN MANAGER

The Real 401k Plan Manager - A Conservative Strategy For Long-Term Investors



**There are 4-steps to allocation changes based on 25% reduction increments. As noted in the chart above a 100% allocation level is equal to 60% stocks. I never advocate being 100% out of the market as it is far too difficult to reverse course when the market changes from a negative to a positive trend. Emotions keep us from taking the correct action.**



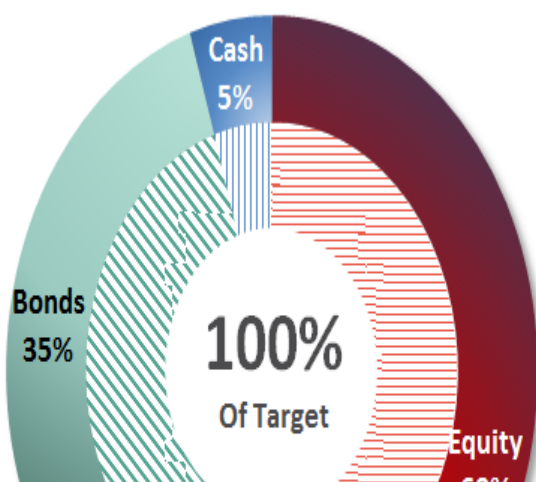
## Tax Cut Melt-Up

As noted last week, **bullish trends remain in place, so portfolio allocations remain at target levels for now.** Furthermore, the markets continue to push extremes on all fronts and, as noted in the chart above, it would require a near **13% decline** just to intersect with the support and the long-term bullish trend. Extreme deviations from long-term trends don't last forever, so caution is advised with overly aggressive exposure. I continue to suggest taking the recent advance as an opportunity to **rebalance risk in portfolios by trimming overweight equity exposure and adding to fixed income exposure is a prudent goal this week.** Specifically, **reduce small and mid-capitalization exposure back to TARGET percentages. Use the cash raised from rebalancing to increase bond exposure back to target weights as well.** All NEW contributions to plans should currently be adjusted to cash or cash equivalents like a stable value fund, short-duration bond fund or retirement reserves. Stop loss levels should be moved up accordingly. If you need help after reading the alert; don't hesitate to [contact me](#).

## Current 401-k Allocation Model

The 401k plan allocation plan below follows the K.I.S.S. principle. By keeping the allocation extremely simplified it allows for better control of the allocation and a closer tracking to the benchmark objective over time. *(If you want to make it more complicated you can, however, statistics show that simply adding more funds does not increase performance to any great degree.)*

### Current Portfolio Weighting



### Current 401k Allocation Model

#### 5.00% Cash + All Future Contributions

*Primary concern is the protection of investment capital*

*Examples: Stable Value, Money Market, Retirement Reserves*

#### 35.00% Fixed Income (Bonds)

*Bond Funds reflect the direction of interest rates*

*Examples: Short Duration, Total Return and Real Return Funds*

#### 60.00% Equity (Stocks)

*The vast majority of funds track an index.*

*Therefore, select on ONE fund from each category.*

## 401k Choice Matching List

The list below shows sample 401k plan funds for each major category. In reality, the majority of funds all track their indices fairly closely. Therefore, if you don't see your exact fund listed, look for a fund that is similar in nature.

Common 401K Plan Holdings By Class			
Cash	Stable Value	Equity	
	Money Market	Large Cap	Vanguard Total Stock Market
Fixed Income	Retirement Savings Trust		Vanguard S&P 500 Index
	Fidelity MIP Fund		Vanguard Capital Opportunities
	G-Fund		Vanguard PrimeCap
	Short Term Bond		Vanguard Growth Index
			Fidelity Magellan
	Pimco Total Return		Fidelity Large Cap Growth
	Pimco Real Return		Fidelity Blue Chip
	Pimco Investment Grade Bond		Fidelity Capital Appreciation
	Vanguard Intermediate Bond		Dodge & Cox Stock
	Vanguard Total Bond Market		Hartford Capital Appreciation
	Babson Bond Fund		American Funds AMCAP
	Lord Abbett Income		American Funds Growth Fund Of America
	Fidelity Corporate Bond		Oakmark Growth Fund
	Western Asset Mortgage Backed Bond		C-Fund (Common Assets)
	Blackrock Total Return		ALL TARGET DATE FUNDS 2020 or Later
	Blackrock Intermediate Bond		
	American Funds Bond Fund Of America	Balanced Funds	Vanguard Balanced Index
	Dodge & Cox Income Fund		Vanguard Wellington Fund
	Doubleline Total Return		Vanguard Windsor Fund
	F-Fund		Vanguard Asset Allocation
International			Fidelity Balanced Fund
	American Funds Capital World G&I		Fidelity Equity Income
	Vanguard Total International Index		Fidelity Growth & Income
	Blackrock Global Allocation Fund		American Funds Balanced
	Fidelity International Growth Fund		American Funds Income Fund
	Dodge & Cox International		ALL TARGET DATE FUNDS 2020 or Sooner
	Invesco International Core Equity		
	Goldman Sachs International Growth Opp.	Small/Mid Cap	Vanguard Mid Cap Growth
<div> <p>The above represents a selection of some of the most common funds found in 401k plans. <u><b>If you do not see your SPECIFIC fund listed simply choose one that closely resembles the examples herein.</b></u> All funds perform relatively similarly within their respective fund classes.</p> </div>			Fidelity Mid Cap Growth
			Artisan Mid Cap
			Goldman Sachs Growth Opportunities
			Harbor Mid Cap Growth
			Goldman Sachs Small/Mid Cap Opp.
			Fidelity Low Price Stock Fund
			Columbia Acorn US
			Federated Kaufman Small Cap
			Invesco Small Cap