



Rotation Will Be Key This Winter

Keith Richards

The *Walking Dead* is a television show produced by AMC—owned by Disney Corp (a stock our ValueTrend Equity Platform holds. More on this stock below). It's a zombie show – and I believe the zombies portrayed in the show accurately depict similar mindlessness that “the herd” (i.e. most small retail investors) exhibit when viewing the market. Back in March and April, the crowd was optimistic. Well, the zombies (or “dumb money”) were optimistic. Not so much for the institutional and sophisticated money side of the market (“smart money”). They were bearish at the time. It was one of the reasons why I opted to raise the cash level in the ValueTrend Equity Platform to over 50% of our holdings over the summer. We like to follow the smart money, and trade opposite the dumb money—especially when the two groups diverge aggressively in opinion. By the end of August—after an 11% decline on the S&P500—this pattern had reversed. Smart money was at record levels of confidence, while the zombies were selling first and asking questions later. Again, this inspired us to begin looking for buying opportunities with the cash we had held since April. We bought back into the market in the first week of October. In both cases, the zombies showed

us what not to do, and the smart money led the way to higher returns.

Right now, www.sentimentrader.com (which is where I view this type of data) shows us that smart money is fairly pessimistic, although not outright bearish. Conversely, now that the markets are nearly back to their spring highs, zombie confidence is back in full force. Sentimentrader also notes some concerns surrounding newly optimistic Wall Street market targets and option premiums. All in, it would appear that the zombie herd is back—and that, like in *The Walking Dead* series, is not such a great thing.

As I write this column, the S&P500 is having a bit of trouble breaking through a ceiling of around 2130. That ceiling, which technical analysts like me call “technical resistance” has been in place since the very beginning of 2015. It is my belief that the S&P will eventually blow through that substantial overhead barrier. But after such a significant ride from the double-bottom low of September, it is time for the market to pause. And that pause will provide a new wave of opportunities to review and purchase high quality stocks for your portfolio.

It is my opinion that any short-termed stagnation by the markets will be followed by a new level of sector rotation as the market struggles to break the aforementioned ceiling. For this reason, in the first week of November, I took a little off of the table (raising 10 percent cash) in my equity platform by selling a few stocks. The current environment calls for active market, sector and stock rotation. The investment industry sometimes propagates the belief that you always have to be fully invested, and that you should avoid portfolio



turnover. As this market, and other markets I have traded in over the years have proven, a blanket “buy and hold” at all costs mentality is actually a riskier and costlier investment strategy than a carefully planned system of buying and selling assets. It is my opinion that markets, sectors and stocks are now changing and will continue to change leadership rapidly in the coming months and years. This rotation will require more than just a buy-and-hold approach.

I'd like to provide you with a few ideas of what we are holding in our ValueTrend Equity Platform at this time. (In future articles, I will keep readers abreast of what we might be looking to as the market begins its next cycle of rotation.)

Right now, we are overweight on the Canadian side in yield stocks such as the Canadian banks, telecom, and specific energy transportation companies (not energy stocks!). For example, we hold Bank of Montreal (BMO-T) within the banking sector. The banks have been an excellent trade over the past two years. Having ridden the sector up in 2014, we sold all of our Canadian bank holdings in early January 2015. The downtrend that ensued justified this move. Now, that downtrend has ended for the big banks, and we have entered via two bank stocks on the breakout. Our investment in this bank in early October at around \$75 is opportunistic. It won't likely be held for more than a few months. BMO generates a more predictable amount of profit from their U.S. segment. With signs of positive economic activity in the U.S., they should benefit from stronger loan growth. Whether U.S. interest rates rise in 2015 or 2016, it is highly probable they will be rising before the Bank of Canada moves higher. This will positively impact margins and we suspect help the stock. Collecting close to a 4.5 percent dividend makes the wait worthwhile.

BCE (BCE-T) is our favorite within the telecom sector. BCE had been trading in a sideways range from \$52 to \$56 since early 2015. The strong breakout in early October gave us the signal to step in at \$56. Recently, the stock pulled back to just above our buy point—a typical neckline breakout test. We view this as a buying opportunity on the stock for those who missed it in October. This strong household name has a diverse business model that should continue to benefit from the unique regulated environment they enjoy. Wireless has provided decent growth that we expect to continue. Although the media division has been challenged, the Wireline predictability provides a cash-flow stream that is significant. Recent investments the company has made should positively impact the stock going forward. We may hold this one for a while.

Keyera Pipeline (KEY-T) is a stock we hold within the energy transportation sector. The sector in general is a bit oversold, and we think that Keyera might just get back to its \$50 highs over the winter.

On the U.S. side, we are overweight in technology, U.S. banks, and consumer discretionary stocks. We hold BB&T Corp (BBT-N) – a regional bank for a trading target of \$41. This stock is a trading candidate to us: we bought it around \$35 and look at the \$41 target as a fairly quick profit potential. We hold Intel (INTC-US) in the technology sector. We bought this stock in early October at \$31 on the breakout from its downtrend. The company has evolved so that dependence on the PC market has decreased. It has proven that it can adapt and innovate in new areas. Its strength in cloud and servers has little to do with what the consumer is spending. Expect business spending on more powerful servers to be a positive for Intel. Overall it is a more diversified technology company that recognizes and adopts changing trends quickly. These qualities make it a name we are confident will continue to be at the forefront of change. Technology tends to be strong until the New Year from a seasonal perspective – we monitor such positions for potential rotation from January onwards.

We also hold Disney (DIS-US) on the consumer discretionary side. What can I say about this behemoth, other than...Disney magic! We've held the stock for almost two years, and haven't regretted that decision. The upcoming Star Wars, Marvel and other ventures make it one of the few stocks that we feel comfortable holding for the long term. Having said that, a trend change for Disney will inspire us to sell the stock without hesitation!

It's vital to understand that these sectors will stay positive and potentially outperform for a period of time, but not forever. Inevitably, it will be time to rotate out of them into the new and upcoming market leaders. Buy and hold is no longer an option if you wish to experience lower volatility and superior performance in your portfolio.

Keith Richards, Portfolio Manager, can be contacted at krichards@valuetrend.ca.

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