December 2017 / Second Report

Volume 41, Issue No. 24

THE MONEYLETTER®

STRATEGIES FOR SUCCESSFUL INVESTING

MARKET WISDOM

The months ahead?

WHAT LOOKS GOOD

Keith Richards

Markets tend to be strong in the final month of the year. The tendency is for the year's big movers to continue to lead until the end of December, while the laggards continue to sell off due to tax loss selling and other reasons. Come January, stock market participants start to re-examine the prior laggards in an effort to uncover some oversold or underappreciated bargains.

As a result, there can be a noticeable degree of rotation from leaders to laggards at the beginning of the year. The well-known "Dogs of the Dow" strategy is designed to benefit from this phenomenon. Same with the small-capped rotation strategy in January.

One strategy that might make sense is to take gains on anything you suspect has run too high - and may be vulnerable to a period of underperformance – as year-end approaches.

For example, technology stocks, or the NASDAQ index, have gone up in value significantly. If you think those markets might take a breather in the New Year, you could realize some profit by selling some of your positions as the year comes to an end.

Then, you can buy a stock or ETF in an underperforming sector that has a good chance of rebounding in January. It's a game of odds, but those odds are somewhat in favour of a rotation of the guard from strong to weak sectors for the first month of the year. It is my opinion that the market is ripe for a stronger-than-normal tendency for sector and stock-specific rotation from strong to weak performers in the coming weeks.

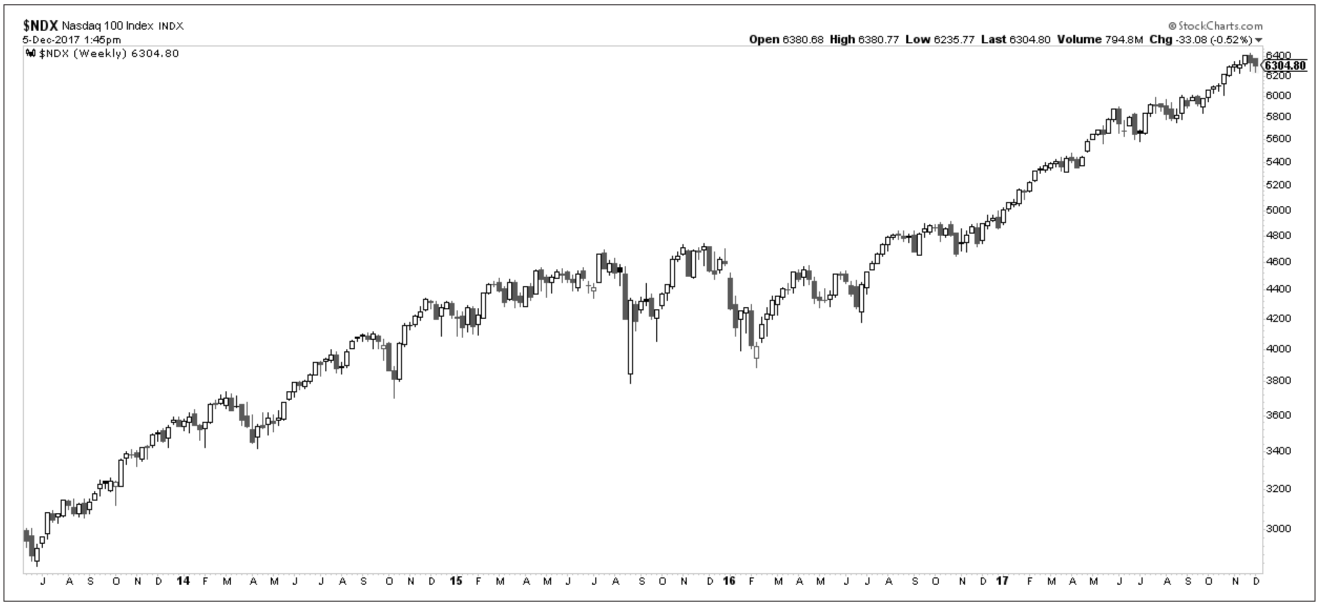
Good Value , But Overlooked

Recent examples of overlooked, good-value stocks that we at ValueTrend have rotated into include Fairfax Financial (FFH-T). We like the fact that Fairfax, run by Canadian business icon Prem Watsa, is invested in and has ownership of a variety of companies. The company has the majority of its investments in various international insurance entities, including wholly-owned subsidiaries; Northbridge Financial, Odyssey and Crum & Forster. Some of the non- insurance investments include The Keg, Sporting Life, Thomas Cook and Cara Operations. The consistency of the cash flow provided by the insurance businesses is one of the appealing parts of the investment. The company previously had been hedging their portfolio, which was costly. This chapter is in the past, and a brighter future is anticipated.

Banks and Energy

We like the Canadian banking scene, and recently bought the least-loved of Canadian banks, CIBC (CM-T, $120.22). This bank has the lowest PE ratio of the group and looks likely to

Keith Richards is a Portfolio Manager at ValueTrend Wealth Management. Sponsoring investment dealer: Worldsource Securities Inc. Member: CIPF and IIROC. He provides commentaries on equity markets and stocks during television and radio interviews and is a frequent guest on Business News Network. He also writes a monthly business column for Investor's Digest of Canada.
krichards@valuetrend.ca.



play catch up to the other big banks. After some delays in closing, they have acquired Private Bank of the U.S. in June. This represents a renewed effort to do business in the United States. They have since followed up with a small deal for Geneva Advisors, headquartered in Chicago. It is expected that, including future acquisitions in the medium term, 25 per cent of earnings will be generated from holdings in the United States. The company has digested some weakness surrounding above-market exposure to the Canadian housing market, and its evolving branding of some business lines. We think that the potential return and compensation at this point is greater than the risk.

We are also moving some allocation to the U.S. banking sector. We bought the BMO U.S. Bank ETF (ZUB-T, $29.25). This is a currency-hedged play on a sector that remained sideways during much of 2017. As the rotation into underperforming and overlooked sectors continues, this ETF should benefit.

Go outside

Despite the overvaluation of many U.S. stock sectors, we do think that the consumer staples sector in the U.S. could begin to move after a period of relative underperformance in 2017. Currently, we own Mondelez (MDLZ-Q, $42.92), with an eye to selling it in the mid-$40's. We may take on other consumer staple stocks into the New Year.

We've also been buying into the Canadian energy sector through companies like Nuvista (NVA-T, $7.94) and Vermillion Energy (VET-T, $44.8). The sector has been trading sideways, along with the price of oil since 2015. But WTI oil has broken out through that two year ceiling price of around $55. We feel the next stop of oil is $62 – and that should drag the Canadian energy sector – and these stocks – up with it.

We are trying to keep some money outside of Canada and the U.S., given the potential overvaluation of these markets. Vanguard FTSE Developed Nation ETF (VI-T, $29.30) is a way to get some exposure to world markets, and a little bit outside of the potentially overvalued North American markets. The ETF buys stocks and indexes in all of the developed nations except North America. It is currency-hedged against declines in the Euro or Yen, and others. ▼

Keith Richards, Portfolio Manager, can be contacted at krichards@valuetrend.ca. He may hold positions in the securities mentioned. Worldsource Securities Inc., sponsoring investment dealer of Keith Richards and member of the Canadian Investor Protection Fund and of the Investment Industry Regulatory Organization of Canada. The information provided is general in nature and does not represent investment advice. It is subject to change without notice and is based on the perspectives and opinions of the writer only and not necessarily those of Worldsource Securities Inc. It may also contain projections or other "forward-looking statements." There is significant risk that forward looking statements will not prove to be accurate and actual results, performance, or achievements could differ materially from any future results, performance, or achievements that may be expressed or implied by such forward-looking statements and you will not unduly rely on such forward-looking statements. Every effort has been made to compile this material from reliable sources; however, no warranty can be made as to its accuracy or completeness. Before acting on any of the above, please consult an appropriate professional regarding your particular circumstances.°