Sunday April 4, 2010
Volume 2, Issue 15

5-Step Investing

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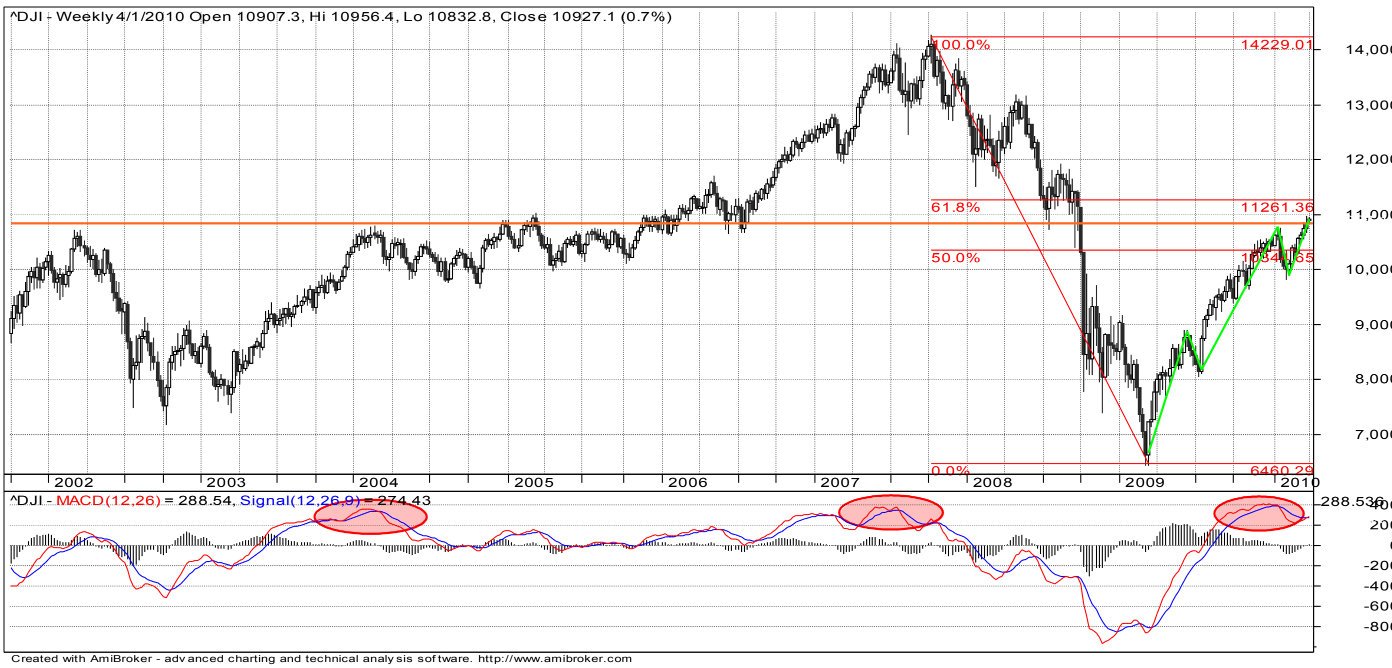
Step 1 – Broad Market Trend

Primary Trend:	Upward.	Started March 6, 2009 at 6626.
Intermediate Trend:	Upward.	Started February 12, 2010 at 10012.

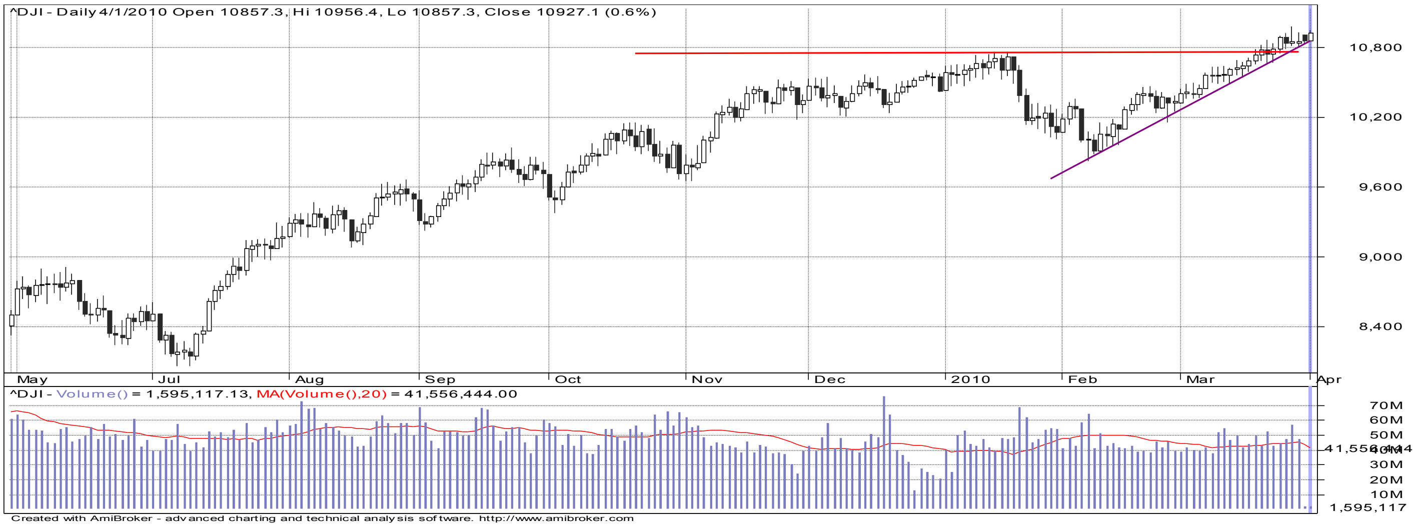


The Dow Jones Industrial Average (^DJI) advanced 0.7% during a four-day last week, finishing at 10,927. As you know we have been watching progress against the Orange 10826 line. This line did not serve as resistance to the current trend but it may serve as support if the market were to head a bit lower. That is important. The next point of interest is the 11261 Fibonacci line, which is a 2.9% gain away.

At this point on technical terms alone it looks like the broad market is in an upward trend which if it continues can be anticipated to gain at least 2.9% more. If it falls, support is at the Orange line 0.9% point at 10826. So your reward/risk ratio in the current market is (2.9/0.9) = 3.2, meaning that you have 3x more to go up than to go down. You want an investment where the possible range of upward movement is much greater than downward movement. This present market qualifies in that regard.

Step 2 – Near Term Market Trend

Intermediate Trend. Upward. Started February 8, 2010 at 10195.
Short Term Trend. Upward. Started March 1, 2010 at 10337.



Last week I remarked “Nevertheless, the market has plowed steadily upward on lighter volume since early February. The prudent thing to do is to recognize that we are in an uptrend but be aware that a reversal could be forthcoming and set the stop loss levels tight and accordingly.”

The uptrend continues. Two additional facts: 1) the shorter-term daily view above shows a market respecting a 45 degree trend line. This is an honest line --- not too steep and not too shallow and traditionally a line that could carry for some time. Note the number of times the market has dropped and has touched but not dropped below the trend line through the months of February and March. When this trend line is breached (it is presently at 10856) then our concern should heighten. But until then, you can assume that the short term trend of this market will be bullish.

Second fact: volume is not growing even through the growth period of February through early April. This is a principle reason to be prudent --- this market does not have a lot of new buyers wanting to own DJI stocks, and so if a downturn should materialize the sellers will quickly have their way and prices could fall far quicker than the 45 degree angle that marked the ascent. Keep your stop losses up to date.

Step 3 – Asset Classes

The charts below are not the price of the security. They are the ratio of the price of certain ETFs to the value of the SPY (S&P 500 ETF).

Bonds (AGG) continue to under-perform relative to the S&P 500. It should be underweight in your portfolio. No sign of need to shift to this safer asset class.

Real Estate (ICF) continues to outperform relative to the S&P 500. It should be overweight in your portfolio.

Gold (GLD) has weakened relative to the S&P 500. It should be under-weight in your portfolio. Confirms that there is no need to shift to GLD for safety.

Step 4 – Current Portfolios

ETF Hedge Fund

There is no indication that you should prepare to hedge for a downside intermediate term correction yet, although in the near term a short pullback in prices is to be expected after the present run-up. While there are questions regarding the length and duration of the existing uptrend, there is no reason to disregard the model recommendations at this point. When securities hit the stop loss the monies should go into cash until the next weekly investment cycle. Remember to update your stop loss levels every week.

Security	Weight	Long-Term	Medium Term	Short Term	Price Now	Stop Loss
SPY (S&P5 ETF)	Overweight	BUY (Jan 25) (109.77)	BUY (Mar 19) (115.97)	BUY (Feb 11) (108.13)	117.8	113.12
AGG (Bond ETF)	Out	Stop loss of 103.95 was hit on Apr 1. Current price is 103.84. Current status is cash in this ETF for the next week until we get a potential re-buy signal.				
ICF (REIT ETF)	Overweight	BUY (Jan 25) (50.15)	BUY (Mar 5) (54.36)	BUY (Feb 16) (50.30)	57.48	54.70
GLD (Gold ETF)	Underweight	BUY (Feb 1) (108.35)	SELL (Jan 29) (105.96)	BUY (Apr 1) (110.26)	110.26	105.37

Current Recommended weights for portfolios:
Conservative: Bonds 30%; S&P 55%; Real Estate 15%; Gold 0%
Aggressive: Bonds 5%; S&P 60%; Real Estate 35%; Gold 0%

Base weights for portfolios:
Conservative: Bonds 50%; S&P 30%; Real Estate 10%; Gold 10%
Aggressive: Bonds 25%; S&P 25%; Real Estate 25%; Gold 25%

Rules for Adding New Money to Existing Portfolios or Building from Scratch

1) Only add new monies to securities with BUY in Long-Term, Medium Term and Short Term. Otherwise, keep the money in a money market fund.
2) Do not increase the overall size of the portfolio more than 12% a week, in order to limit market risk.
3) Always enter the noted stop loss amount with each investment. Do not enter a purchase without an associated stop loss amount.

Rules for 401K Portfolios

1) Segment your 401K portfolio offerings into Equity, Bond, and Money Market. Most equity funds (Large Cap, Small Cap, International, Growth, Value) are very tightly correlated and should be considered as a single asset class. Of these, if you have an S&P Index fund, choose this as your Equity fund. Most bond funds (government, mortgage) are tightly correlated. Of these, if you have a government bond fund, choose this as your Bond fund. You typically will not have a Real Estate or Gold option for 401K portfolios.
2) Apply the Medium Term recommendations above to these two fund options by using the Bonds recommendation for the Bond fund, and the S&P recommendation for the Equity fund. Calculate the percent allocation for the equity fund as the sum of the S&P, Real Estate, and Gold recommendations.
3) Remember that most 401K options have limitations on the frequency with which you can trade the funds or other

Step 5 – New Ideas

See the "The Final Word" below.

The Final Word

This week's final word comes from Dan Miley, an experienced fundamental investor and long-time good friend of mine from Philadelphia. He discusses how you can effectively use a stock screener and a top-down fundamental investing strategy to determine high value investment candidates.

Stocks to Study

I would like to bring a few stocks to your attention for further study and possible investment. There is a huge universe of stocks available, so it is important to use a stock screener. Charles Schwab, along with many other brokers, offers pre-defined stock screeners but I like to create my own. However, before starting to use any screener, it is important to pick a time horizon as well as an investing technique. My time horizon is medium term (about 5 years) and I tend to be a mixed growth/value investor; that is I seek growth stocks at a reasonable price that will double in that time period. So after picking my first criterion (time horizon and investing technique), my second criterion is Schwab's Equity Rating. I only take stocks that Schwab rates "A" (strong buy) or "B" (buy) – this helps me reduce the stock universe from 4,130 stocks down to about 900. Obviously, few of us, if any, have the resources to buy 900 stocks, so I further refine my criteria to find growth stocks at a reasonable price. Here are my criteria (after Schwab's rating of A or B is included):

1. **Five Year Revenue Growth greater than or equal to 15%.** This means that if growth continues at this rate revenue will have doubled in about 5 years. This brings us down to around 150 stocks.
2. **Five Year Earnings per share (EPS) growth greater than or equal to 15%.** Revenue is fine, but if the company is not making money consistently, then I am not interested. Now we are down to around 50 stocks.
3. **Estimated Five Year EPS growth greater than or equal to 15%.** As mentioned, we would like to double our earnings in 5 years, so if the estimates are correct, then EPS will have doubled. This brings us down to 20. We are getting close to a reasonable number to study.
4. **Return on Equity (ROE) greater than 15%.** ROE measure a company's profitability by determining how much profit a company generates for the shareholder's equity. It is expressed as percentage and is calculated by dividing net profits by shareholder's equity. This brings us down to 14 stocks.

I then sorted the 14 stocks in descending order of ROE (after all, I am the potential shareholder, so return on my equity is most important). Here is how you could look at the first five on this list:

1. **Provident Services (PRSC)** provides case management and transportation services for state and local agencies, including Medicaid. With passage of the Health Care Reform Act, I think that this company has great potential for growth over the next 5 years. A few words of warning, however, government contracting includes the risk of a capricious Congress changing its mind and the company's debt is higher than I would like. Still, it is definitely worth considering.
2. **Allegiant Services (ALGT)** provides leisure travel services and air travel to small to medium cities. With the improving economy, this may be one to watch. However, because of my prior failures with airline stocks, I would avoid this one. You are, of course, free to think otherwise.
3. **Noble Corp. (NE)** provides offshore drilling services for the oil and gas industry. With recent news, this company is definitely worth considering, but be careful not to pay too much.
4. **Lincoln Educational (LINC)** provides career oriented post-secondary educational services. With many folks seeking re-training, this looks like another stock to consider.
5. **Cognizant Technical Solutions (CTSH)** is a provider of custom information technology (IT) consulting and technology services, and outsourcing services. As the economy improves, and with 37 million more people going on the health care roles, both government and commercial interests will have need for IT services. Therefore, although this stock is #5, I highly recommend it for purchase.

Stock picking is an art as well as a science, and there are no guarantees in either area. But I think with a disciplined numerical approach as well as good instincts (and luck!), one can out-perform the market.