WELCOME!
BUSINESS CYCLES, MARKET CYCLES, AND STOCK SECTORS

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The Peter Dag Portfolio

www.peterdag.com
peterdag.blogspot.com
THE PETER DAG PORTFOLIO

- TWICE A MONTH - 17 PAGES
- THE GLOBAL BUSINESS CYCLE (once a month)
- THE US ECONOMY (once a month)
- MARKET UPDATE
OUTLINE

- BUSINESS CYCLE
- OUTLOOK
- THE MARKETS (COMMODITIES, BONDS, SECTORS FOR A STRONG AND WEAK ECONOMY)
- STOCK SELECTION
- TIMING DECISIONS
- ETFs AND MUTUAL FUNDS
- RISK AND PORTFOLIO MGT
INVESTMENT PROCESS

- Economic Scenarios
  - Expected Strong & Weak Sectors
    - Stock Selection
      - Strong fundamentals
      - Outperforming market
      - Low volatility
    - Measuring Risk
      - Financial risk
      - Short-term interest rates
      - Bond yields
      - Technical
    - Decreasing Risk
      - Increase equities
        - Add to strongest positions
        - Reduce weakest positions
        - Add new positions
    - Rising Risk
      - Reduce equities
        - Reduce weakest positions
        - Increase cash
        - Hedge portfolio with shorts
  - Performance
BUSINESS CYCLE

BUSINESS AND FINANCIAL CYCLE CONFIGURATIONS

- STOCK MARKET
- MONEY SUPPLY
- YIELD CURVE
- DOLLAR

- ISM INDEXES
- INVENTORY CYCLE

- COMMODITIES
- INTEREST RATES
- INFLATION
OUTLOOK
BUSINESS CYCLE

LEADING INDICATORS

- MONETARY BASE
- HOUSING STARTS
- PROFITS
- ORDERS
St. Louis Adjusted Monetary Base (AMBSL)
Source: Federal Reserve Bank of St. Louis

Shaded areas indicate US recessions as determined by the NBER.
2009 Federal Reserve Bank of St. Louis: research.stlouisfed.org
HOUSING STARTS

Shaded areas indicate US recessions as determined by the NBER.
2009 Federal Reserve Bank of St. Louis: research.stlouisfed.org
PROFITS

Nonfinancial Corporate Business: Profits After Tax (NFCPATAX)
Source: U.S. Department of Commerce: Bureau of Economic Analysis

Shaded areas indicate US recessions as determined by the NBER.
2009 Federal Reserve Bank of St. Louis: research.stlouisfed.org
OUTLOOK
BUSINESS CYCLE
COINCIDENT INDICATORS

- EMPLOYMENT
- PRODUCTION
- INCOME
- SALES
INDUSTRIAL PRODUCTION

Industrial Production Index (INDPRO)
Source: Board of Governors of the Federal Reserve System

(Natural Log of Index 2002=100)

Shaded areas indicate US recessions as determined by the NBER.
2009 Federal Reserve Bank of St. Louis: research.stlouisfed.org
SO FAR IT LOOKS LIKE A GOOD OLD FASHION BUSINESS CYCLE WITH COINCIDENT FOLLOWING THE LEADING THE LEADING WILL RISE AFTER THE LAGGING INDICATORS DECLINE
OUTLOOK
BUSINESS CYCLE

LAGGING INDICATORS

- INTEREST RATES
- LENDING OFFICERS
- FINANCIAL RISK
- UNIT LABOR COSTS
- INFLATION
- COMMODITIES
CREDIT CYCLE
(NOTE THE 1992, 2002 RECESSIONS AND BEGINNING OF BULL MARKETS)
TIGHTENING CREDIT CONDITIONS HAPPEN WHEN THE ECONOMY OVERHEATS AND INTEREST RATES RISE.

NOW CREDIT IS BEING TIGHTENED AS THE ECONOMY SLOWS DOWN. WHY?

LENDERS DO NOT TRUST THE BORROWERS AS FINANCIAL INSTITUTIONS FAIL.
FINANCIAL RISK SOARING
INFLATION DECLINING
GOOD NEWS

Personal Consumption Expenditures: Chain-type Price Index (PCEPI)
vs. Consumer Price Index For All Urban Consumers: All Items (CPIAUCSL)
vs. Producer Price Index: Finished Goods (PPIFGS)

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2009 Federal Reserve Bank of St. Louis: research.stlouisfed.org
INFLATION follows

Producer Price Index: Finished Goods (PPIFGS) vs. Industrial Production Index (INDPRO)

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2009 Federal Reserve Bank of St. Louis: research.stlouisfed.org
COMMODITIES FOLLOW

Industrial Production Index (INDPRO)
vs. Spot Oil Price: West Texas Intermediate (OILPRICE)
vs. Natural Gas Price: Henry Hub, LA (GASPRICE)

Shaded areas indicate US recessions as determined by the NBER.
2009 Federal Reserve Bank of St. Louis: research.stlouisfed.org
INTEREST RATES FOLLOW

Industrial Production Index (INDPRO) vs. 3-Month Treasury Bill: Secondary Market Rate (WTB3MS)

Shaded areas indicate US recessions as determined by the NBER. 2009 Federal Reserve Bank of St. Louis: research.stlouisfed.org
THE MARKETS
ALL COMMODITIES HAVE THE SAME CYCLICAL TURNING POINTS
COMMODITIES & THE FED HAVE THE SAME CYCLICAL TURNING POINTS
THE FED AND FINANCIAL RISK

FINANCIAL RISK AND TREASURY BILLS

RATES ON 13-WEEKS TREASURY BILLS

MONETARY BASE STARTED SLOWING DOWN RAPIDLY UNTIL THE CRISIS EXPLODED
THE FED AND FINANCIAL BUBBLES

- AGGRESSIVE EASING IN 1998 WAS FOLLOWED BY THE TECH BUBBLE
- AGGRESSIVE EASING IN 2002-2004 WAS FOLLOWED BY THE HOUSING/COMMODITY BUBBLES
- AGGRESSIVE TIGHTENING IN 2005-2006 CAUSED THE HOUSING BUBBLE TO IMPLODE AND SUBPRIME DEBACLE
MAN-MADE (FED) COMMODITY BUBBLES
DOLLAR, COMMODITIES, GOLD, AND PURCHASING POWER
INFLATION, COMMODITIES, AND SHORT-TERM INTEREST RATES

- INFLATION, COMMODITIES, AND SHORT-TERM INTEREST RATES HAVE THE SAME TURNING POINTS
- THEY FOLLOW THE DOWNTURN OF THE ECONOMY
- THEY ANTICIPATE THE UPTURN OF THE ECONOMY
STOCK SELECTION
SELECTION OF ASSETS DEPENDS ON GROWTH
LIST STRONG SECTORS
SECTORS FOR A STRONG ECONOMY AND BEATING THE S&P 500

- METALS AND MINING
- ENERGY
- ELECTRONICS
- INTERNET
- COMPUTER SOFTWARE & SERVICES
- CONGLOMERATES
- TELECOM
SECTORS FOR A WEAK ECONOMY AND BEATING THE S&P 500

- TOBACCO
- HEALTH SERVICES
- INSURANCE
- BANKS, REGIONALS, S&L
- FINANCIAL SERVICES
- REAL ESTATE/REITs/TRUSTS
- AEROSPACE & DEFENSE
IF YOU KNOW
WHY YOU BUY
YOU ALSO KNOW
WHEN TO SELL
SELECT STOCKS
STOCK SELECTION

- USE FAN CHARTS TO CHECK PERFORMANCE OF STOCKS
- CHOOSE STOCKS WITH LOWEST VOLATILITY AND BEST PERFORMANCE
- PERFORM FINANCIAL ANALYSIS (WWW.PETERDAG.COM)
EXAMPLE OF FAN CHART: WIRELESS COMMUNICATION
STOCK PRICES AND THE NEED FOR TIMING

S&P 500

6.75% GROWTH SINCE 1932
BOND YIELDS AND STOCK PRICES
FINANCIAL RISK AND STOCK PRICES
UNEMPLOYMENT CLAIMS AND STOCK PRICES
TECHNICAL ANALYSIS

- OVERBOUGHT/OVERSOLD INDICATORS
- TRADING VOLUME
- SENTIMENT INDICATORS
- MOVING AVERAGES
- DIRECTIONAL INDICATORS
OVERBOUGHT/OVERSOLD INDICATORS

- THEY STAY OVERSOLD FOR A LONG TIME AND OVERBOUGHT FOR A SHORT TIME IN BEAR MARKETS

- THEY STAY OVERSOLD FOR A SHORT TIME AND OVERBOUGHT FOR A LONG TIME IN BULL MARKETS
VOLUME PATTERNS

- **BEARISH:** STRONG VOLUME FOLLOWING A STRONG RISE

- **BULLISH:** STRONG VOLUME FOLLOWING A SHARP DECLINE
SENTIMENT INDICATORS

SAME PROBLEMS AS
OVERBOUGHT/OVERSOLD
INDICATORS
DIRECTIONAL INDICATORS
The market bottoms when this indicator reaches this level.
STRATEGY
GAMES THEORY AND INVESTMENT STRATEGY

(ADJUST MIX STRONG/WEAK ECONOMY SECTORS AS NEW INFORMATION BECOMES AVAILABLE)
HEDGING IN A DOWN MARKET

- SELL POOR PERFORMING STOCKS & USE CASH TO HEDGE PROFITS AND REDUCE VOLATILITY

- FOR EVERY $ OF SH-DOG-PSQ YOU HEDGE $1 DOLLAR OF LONG POSITIONS

- ONLY STRONG STOCKS ARE NOW EXPOSED TO MARKET DECLINES
FEEDBACK

BASED ON

PERFORMANCE
USE FAN CHART TO ISOLATE WEAKEST STOCKS
ETFs & MUTUAL FUNDS
SELECT THE STRONGEST ETFs & MUTUAL FUNDS USING FAN CHART
RISK MANAGEMENT & PERFORMANCE
INVESTMENT PROCESS

ECONOMIC SCENARIOS

EXPECTED STRONG & WEAK SECTORS

STOCK SELECTION
- Strong fundamentals
- Outperforming market
- Low volatility

PERFORMANCE

MEASURING RISK
- Financial risk
- Short-term interest rates
- Bond yields
- Technical

PERFORMANCE

DECREASING RISK
- INCREASE EQUITIES
  - Add to strongest positions
  - Reduce weakest positions
  - Add new positions

RISING RISK
- REDUCE EQUITIES
  - Reduce weakest positions
  - Increase cash
  - Hedge portfolio with shorts
CONCLUDING THOUGHTS

- SHORT LIST OF STOCKS ... 10-15 max
- DIVERSIFICATION ... waste of money & time
- LONG-TERM INVESTING ... illusion
- NEED TIMING MODEL ... a must
- THE BUSINESS CYCLE ... WORKS
- MOMENTUM ... WORKS
- AVOID FALLING KNIVES ... bad strategy
- HEDGE YOUR PORTFOLIO ... use SH, DOG, PSQ
- USE INVESTMENT PROCESS ... a must
- IF YOU LEAVE THE TABLE ... can’t win
- TOO COMPLICATED? ... buy CDs
THANK YOU!