Investment trends

Fig. 1. The S&P 500 declined almost 13% since its high in February. The slide stopped as soon as the average touched the 200-day moving average. The price pattern looks eerily similar to what happened in 2018.

Fig. 2. The industrial stocks ETF (XLI) also declined sharply below the 200-day moving average. This is a sign the industrial sector of the economy is struggling and is facing difficult times.

Fig. 3. The transportation stocks ETF (IYT) has performed poorly since early 2018 when the business cycle started to slow down. The decline below its 200-day moving average is further confirmation goods are not being shipped, reflecting the difficulties of the industrial sector.

Portfolio Strategy

Observations. I liked to challenge my students with mind-stretching questions. For instance – Is there a difference between communism and parliamentary regimes? The response was a smile as if I were joking. What is communism if not control of major parts of the economy? Well, I insisted, is it any different, say, in a socialist or fascist society where they allowed private ownership and acquired control by offering huge benefits to cooperating firms such as government contracts, protections from foreign and domestic competition, freedom from certain regulations? What about the privileges now enjoyed by agriculture, green energy, aerospace, insurance, medical delivery ,….? Power is the unifying concept. Tomatoes, “tomahtoes”.

Market Trends

The stock market. The long-term fundamental outlook – defensive. Emotions blind the decision-making process. You do not see what is in front of you. As documented in the following pages, the economy is doing well – hard to believe amid the hyperventilation of the press. Consumers’ sentiment remains high with extraordinary trust in government policies according to the University of Michigan. The above chart shows our outlook and strategy. We are facing a slow growth economy not ready yet to turn around. In such environment a defensive strategy is the only winning approach with bonds still being the star performers.

Long-term technical model – Bearish.
Near-term technical indicators – Bearish.
Seasonality – Bullish from October to April.
Sentiment – More negative – which is bullish.

Strategy. Bonds have protected us. We raised some cash, ready to buy when our indicators tell us to do so.
**The US economy.** Despite of the current volatile environment consumers seem to have a positive attitude.

![Confidence in Government's Economic Policy Chart](image1.png)

Their optimism is close to record levels. They are also quite confident about the efficacy of government policies (see above chart). The reason, of course, is a strong labor market and income growth rising a solid +4.0% y/y. This growth is accompanied by stable spending – up +4.5% y/y. Housing starts and construction are holding up. However, autos, a major sector of the economy, keep slowing down. The main problem remains the manufacturing sector still trying to reduce an inventory buildup. The outcome is weak manufacturing activity (see above chart). Durable goods are declining quite sharply (-3.9% y/y) with consumer durable goods plunging (-5.4% y/y). The business cycle indicator of the Chicago Fed points decidedly down, reflecting a weakening economic environment. Our business cycle indicator is still pointing to slower growth.

**Commodities & Gold.** Gold has been performing like TLT (ETF: long Treasury bonds) since 2009. The point is TLT tends to move in the same direction as gold in times of uncertainties. Yields, meanwhile, will continue to head lower (and bond prices up).

**Inflation.** The price index of consumer expenditures is up 1.7% y/y. The slowing economy will place a cap on inflation and continue to depress commodity prices.

**Short-term interest rates.** Global central banks will keep printing money. But it will not solve the Covid-19 crisis.

**Bond yields.** Yields are collapsing, proving us correct. Their historical decline, however, is worrisome because it reflects an economic turbulence not yet visible.

**Bottom line.** The US and global economy will keep growing slowly. This economic scenario favors investment in defensive sectors and bonds. This has been and will continue to be our strategy.

**Global trends.** It is simply amazing that the main global health hazards (bird flu, SARS, swine flu, and coronavirus) have all originated in China (bats?). Yet we treat China with velvet gloves for their role in the global community. If one says they are an underdeveloped country selling cheap production facilities rather than improve their cleanliness and standard of living one risks sounding like a heretic. But this is what happens when a country is not resting on sound economic pillars. There was a time when some progressives told us China’s system is the most flexible one because one man can change the direction of the country and get things done. Well we are seeing the result of their system. These people should learn major calamities come from regimes where there is concentration of political power. China is a continuous risk to the global health and economic system. See also their pollution. Yet the press does not dare to be outraged about a country not producing anything but cheap labor, health problems, and global economic and financial endangerment.

**Global equity markets.** Sinking.

**Global bond yields.** Lower.

**The Dollar.** The Dollar has been correcting but remains in an uptrend.
**Dag’s Exclusive Model Portfolios**

Objective of our portfolios: minimize risk and volatility while achieving attractive returns.

**Managed Equity Portfolio.** Our position in bonds continues to reduce the volatility of the portfolio. Our conservative strategy is producing the desired results with positive returns. The S&P 500 was down -5.54% year-to-date and this portfolio was up +4.43% year-to-date on 3/4/20 @ 10:49am. We sold 3% of the portfolio from each: MSFT (65 shares), DHR (75 shares), and ITW (65 shares).

<table>
<thead>
<tr>
<th>Symbol</th>
<th>Description</th>
<th>Shares</th>
<th>Price as of 3/4/20</th>
<th>Most Recent Value</th>
<th>Change since last purchase</th>
<th>Change since last purchase</th>
<th>Allocation %</th>
<th>Dividend Yield</th>
</tr>
</thead>
<tbody>
<tr>
<td>AWK</td>
<td>AMERICAN WATER WORKS</td>
<td>140.1223</td>
<td>$135.57</td>
<td>$18,996.88</td>
<td>$612.40</td>
<td>3.33%</td>
<td>5.04%</td>
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<td>AAPL</td>
<td>APPLE INC</td>
<td>46.632</td>
<td>$295.06</td>
<td>$13,761.07</td>
<td>$2,464.88</td>
<td>21.82%</td>
<td>3.65%</td>
<td>1.00%</td>
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<tr>
<td>ATO</td>
<td>ATMOS ENERGY CORP</td>
<td>134.0721</td>
<td>$109.13</td>
<td>$14,631.41</td>
<td>$1,380.55</td>
<td>10.42%</td>
<td>3.88%</td>
<td>2.10%</td>
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<tr>
<td>BDX</td>
<td>BECTON DICKINSON&amp;CO</td>
<td>40.0000</td>
<td>$246.73</td>
<td>$9,869.20</td>
<td>($1,041.43)</td>
<td>-9.55%</td>
<td>2.62%</td>
<td>1.30%</td>
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<tr>
<td>CTAS</td>
<td>CINTAS</td>
<td>65.9005</td>
<td>$280.27</td>
<td>$18,469.91</td>
<td>$684.62</td>
<td>3.85%</td>
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<td>DHR</td>
<td>DANAHER CORP</td>
<td>120.1255</td>
<td>$151.53</td>
<td>$18,202.85</td>
<td>$217.93</td>
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<td>HOME DEPOT INC</td>
<td>60.3898</td>
<td>$233.58</td>
<td>$14,101.06</td>
<td>($146.78)</td>
<td>-1.03%</td>
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<tr>
<td>ITW</td>
<td>ILLINOIS TOOL WORKS</td>
<td>90.0929</td>
<td>$172.51</td>
<td>$15,668.26</td>
<td>($428.09)</td>
<td>-2.66%</td>
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<td>MSFT</td>
<td>MICROSOFT CORP</td>
<td>46.6045</td>
<td>$167.37</td>
<td>$7,800.20</td>
<td>$766.47</td>
<td>7.98%</td>
<td>2.07%</td>
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<tr>
<td>V</td>
<td>VISA INC CLASS A</td>
<td>69.7076</td>
<td>$188.78</td>
<td>$13,159.60</td>
<td>$639.10</td>
<td>5.10%</td>
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<td>TLT</td>
<td>20+ T. BND ETF</td>
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<td>16.66%</td>
<td>20.05%</td>
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<tr>
<td><strong>Cash &amp; Cash Investments</strong></td>
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<td></td>
<td></td>
<td>$126,736.05</td>
<td></td>
<td>33.60%</td>
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<tr>
<td><strong>Account Total</strong></td>
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<td></td>
<td>$377,242.56</td>
<td>$20,075.05</td>
<td></td>
<td></td>
<td>8.71%</td>
<td></td>
</tr>
</tbody>
</table>

The above portfolio may not reflect current recommendations or actions. Past performance is no guarantee of future results.

**ETF Portfolio No. 1.** Change. 16.6% in TLT. 83.4% in cash.
**ETF Portfolio No. 2.** Change. 16.6% in XLK. 83.4% in cash.
**Fidelity Mutual Fund Portfolio.** Change. 16.6% in each: FTBFX, FSCSX. 66.8% in cash.
**Vanguard Mutual Fund Portfolio.** Change. 20% in VUSTX. 80% in cash.
**Vanguard ETF Portfolio.** Change. 100% in cash.
**SPY-XLU.** Change. 100% in cash.
**SPY-TLT-XLU.** Change. 25% in TLT. 75% in cash.

The performance parameters of each portfolio are: the compound annual return (CAGR), volatility (STD DEV), the amount gained or lost in the worst year, and the greatest loss suffered by the portfolio (MAX DRWDNS).

CAGR is the rate at which an investment would have grown if it had increased at a steady rate.

The performance data in the table have been updated as of the end of February and will be updated again at the end of March.

**Note –** The major overwhelming advantage of our timing models is that they considerably reduce the volatility of the portfolios (STD DEV) and the size of the losses (MAX DRWDNS and WORST YEAR) compared to the buy-and-hold strategy for the S&P 500. They offer an unbiased and quite successful risk management tool.
Relative strength analysis

The table below shows the 30 stocks in the Dow Jones Industrial Average and 30 ETFs. They are ranked by price action and relative strength – near term and long term. The most attractive investments are those displaying rising price and rising strength relative to the S&P 500. UP means price and relative strength are rising. DOWN means price and relative strength are declining.

<table>
<thead>
<tr>
<th>DOW JONES 30 STOCKS</th>
<th>MAJOR ETF SECTORS</th>
</tr>
</thead>
<tbody>
<tr>
<td>Symbol</td>
<td>Name</td>
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<tr>
<td>XXX</td>
<td>AAPL</td>
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<tr>
<td>XXX</td>
<td>AXP</td>
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<td>BA</td>
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<td>CAT</td>
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<td>CSCO</td>
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<td>XXX</td>
<td>CVX</td>
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<tr>
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<td>DIS</td>
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<td>XXX</td>
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<td>XXX</td>
<td>MCD</td>
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<td>MMM</td>
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<tr>
<td>XXX</td>
<td>MRK</td>
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<tr>
<td>XXX</td>
<td>MSFT</td>
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<tr>
<td>XXX</td>
<td>NKE</td>
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<td>XXX</td>
<td>PFE</td>
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<td>XXX</td>
<td>PG</td>
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<td>XXX</td>
<td>TRV</td>
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<tr>
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<td>WMT</td>
</tr>
<tr>
<td>XXX</td>
<td>XOM</td>
</tr>
</tbody>
</table>

Investment implications of the above table

1. Price momentum – rising prices are more likely to continue to go up than decline.
2. Relative strength momentum – rising relative strength is likely to continue to increase because it is a function of the degree of success or failure of a company.

Industrials, commodity and energy sensitive sectors, and financials continue to underperform the market. The strongest sectors and stocks are the defensive ones. The particularly attractive stocks and ETFs have been flagged with “XXX”.

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Market Update: Sunday, March 15, 29, 2020
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Editor. Since 1977.
THE FRAMEWORK OF OUR INVESTMENT STRATEGY

Financial history repeats itself. Why not take advantage of it!

The following information and charts closely reflect the approach to managing portfolios and portfolio risk discussed in Dr. George Dagnino’s books Profiting in Bull or Bear Markets (McGraw-Hill Education) available also in Mandarin, Easy Ways to Beat the Market with ETFs and Investing Wisely - It is Easier Than You Think.

THE US BUSINESS CYCLE

Fig. 4. The business cycle is in Phase 4. In this phase the economy keeps slowing down. Short-term interest rates, bond yields and inflation decline. Housing and auto sectors are weak. Earnings growth declines and credit risk rises. The stock market is more volatile.

1. Income and spending (see Fig. 5). Good growth.
2. Autos and housing (see Fig. 6). Housing strong. Autos weak.
3. Capital investments (see Fig. 7). Improving.
4. Durable goods orders (see Fig. 8). Weak.
5. Commodities (see Fig. 9). Stable at low levels.
6. Inflation (see Fig. 10). Rising.
7. Interest rates (see Fig. 11). Yields likely to decline.
8. The Dollar (see Fig. 12). Firm.
9. Stock market - long-term (see Fig. 13, 14). Cautious.
10. Stock market - near-term (see Fig. 15). Down.
11. Foreign markets (see Fig. 16 to Fig. 19). Stalled and underperforming the US market.

The investment environment – The economy is doing better than expected given the global disruption due to the coronavirus. The labor market is strong, consumers are very optimistic about the economy and trust government’s policies. The trend of unemployment claims suggests jobs are plentiful. The major headwind remains the industrial sector. Its weakness -- and the uncertainties created by the virus -- will keep the economy on a slow-growth economic path.

The bottom line. A defensive investment strategy is fully justified under these conditions.
Income and spending – solid growth

Fig. 5. Personal income (red) and consumer spending (blue) have been growing at a strong 4.0% y/y and 4.5% y/y respectively. This is very good news showing the economy is on a sound footing. It reflects strong consumer optimism and high confidence in government’s policies (source: University of Michigan consumer survey).

Autos and housing – mixed picture

Fig. 6. Auto sales (blue, left) remain at high levels but have been declining slowly since 2016. Housing starts (red, right) have been soaring.
Fig. 7. Capital investments (blue, left) are up +0.9% y/y. This is a minor improvement but bodes well for the economy. Industrial production (red, right) is still weak -- -0.8% y/y.

Fig. 8. Buyers are shying away from big ticket items. Orders for durable goods (blue) are down -3.9% y/y. Consumer durable goods orders (red) declined a sharp -5.4% y/y -- mostly caused by the weakness in autos.
Copper – weak

Fig. 9. Copper prices, an important industrial metal, have been in a downtrend since 2018 when our business cycle indicator started declining. The downtrend in our business cycle indicator suggests further weakness in copper and the overall commodity complex.

Inflation – rising

Fig. 10. Producer prices (green) rose +2.5% y/y. The price index of consumer spending (red) -- a measure of inflation followed closely by the Fed -- rose +1.7% y/y. According to our proprietary leading indicator of inflation (blue), inflation is likely to continue to rise.
**Bond yields—down (prices up)**

*Fig. 11.* The trend of our business cycle indicator (lower panel) is down. Bond yields (upper panel) will keep heading lower as long as our business cycle indicator is declining.

**Dollar—firm**

*Fig. 12.* The Dollar (upper panel) strengthens when our business cycle indicator (lower panel) declines. The odds favor the strength of the dollar to continue as long as our business cycle indicator heads lower.
GLOBAL STOCK MARKETS

**US long-term outlook: defensive**

*Liquidity* (see Fig. 13). Bearish.

*Spreads* (see Fig. 14). Bearish.

**US near-term technical outlook: down**

*Momentum* (see Fig. 15). Down.

**Foreign markets (Fig. 16, Fig. 17, Fig. 18, Fig. 19):** They have stalled and keep underperforming the US stock market. Note how the main turning points remain the same among all equity markets.

---

**Liquidity – not improving**

![Liquidity Chart](chart-image)

**Fig. 13.** Liquidity stopped increasing since early this year and the stock market stopped rising. The trend of liquidity has not changed for several weeks, pointing to a volatile market ahead.
Bond spreads (inverted) – bearish

Fig. 14. Bond spreads (inverted in the chart) -- a measure of credit risk -- continue to rise. Rising spreads is a reliable indicator pointing to stock market weakness.

Near-term momentum - bearish

Fig. 15. This indicator (lower panel) suggests the market may be close to an important bottom. It is to early to tell, however.
Fig. 16. The “rest of the world” market has stalled and is underperforming the US market. The graphs in the lower panel show the strength of the world market relative to the S&P 500. Note how all the equity markets have perfectly synchronized turning points at major tops and bottoms.

EUROPE

Fig. 17. The European market has stalled and is underperforming the US market. The graphs in the lower panel show the strength of the European market relative to the S&P 500.
Fig. 18. The Chinese market has stalled and is underperforming the US market. The graphs in the lower panel show the strength of the Chinese market relative to the S&P 500.

Fig. 19. The emerging markets have stalled and are underperforming the US market. The graphs in the lower panel show the strength of the emerging markets relative to the S&P 500.
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