CAPITAL IDEAS RESEARCH YOU CAN REALLY USE

Volume 15	December 4, 2016.	Number 9

2016 Annual Review of Bond Substitutes, Special Situations, Risk / Return, & Rebalancing

Win as if you were used to it, lose as if you enjoyed it for a change.

- Ralph Waldo Emerson
Essayist, Poet, Philosopher

Over the years I have started off this annual performance review with that appropriate quotation. Apart from its obvious admonition about behaviour, it more subtly refers to maintaining a perspective. And that also is a big part of any review. It is so easy to get caught up in the elation or disappointment of the moment and lose the overall view. That is what these annual reviews are all about – keeping everything in our field of sight.

With markets grinding away at all-time highs, there isn't much a value investor can do but sit and wait for the inevitable bear market. Just like last year, there was a lot of sitting on existing positions. The only buying I did was to add on to an existing position from in Ensign (TSX: ESI) in September. I did sell half of two US based telecoms that had doubled in value, AT&T (NYSE:T) and Verizon (NYSE:T) in order to hold the remaining open positions as "free stock". You'll remember that those stocks are highlighted in the tables in bold green.

To give you an idea of the type of decline that would get me interested in buying, let's take Royal Bank (TSX: RY). It currently trades at $89; by my calculations an under-valuation entry point would be around $61. That is over a 30% drop and at that, it would still be the equivalent of my buy price of say Potash of $29.21 that still managed to fall another 34.6% from what I considered a bargain buying price. [1]

An 11 year position in stodgy Manitoba Telecom (TSX: MBT) finally paid off when BCE announced it would acquire the company for about $40 a share. The sale is expected to close by early 2017.

[1] See Table 3 NYSE: POT.

As you know, last year in addition to this year's add-on to Ensign in the energy sector, I also bought Husky Energy (TSX: HSE), Conoco Phillips (NYSE:COP) along with Potash Corp. (NYSE:POT) from the materials sector at what were until that time decade low valuations. Obviously the market disagreed using its own valuation metrics and relentlessly pounded crude oil and potash to multi-decade lows and with it those commodity based stocks. Only Ensign was spared a dividend reduction.

If that sounds like I should buy some more, I have, starting with Ensign. I am just waiting for some type of sustainable price bottom to establish itself on the others.

But I'm not the only one who saw a bargain among this group (albeit at substantially lower prices than what I paid). In September, Agrium Inc. (TSX: AGU) announced it was merging with Potash Corp. The deal should close by the summer of 2017. This highlights what happens when you buy quality companies with strong balance sheets that are dominant in their industries. When their stock prices fall to bargain levels, they become takeover targets for competitors or others who are eager to establish a presence in their market. That is why I focus on balance sheets and don't become fazed when a stock underperforms or gets pummeled in the short term. I know others are looking at the same things that caused me to buy the company's stock in the first place. Agrium Inc. with Potash Corp. is going to be a major player in the global agricultural chemical sector. Keep on re-investing those dividends at these ridiculously low prices.

As I always say in this review, if you have been with me for more than a couple of years, please excuse the repetitiveness of any reminders or admonishments. I keep them included because they are as important now as they were when I first mentioned them, like this one: *Your own individual performance is highly dependent upon when you began receiving my advisories, which ones you chose to act on and the weighting you gave each of them in your portfolio.*

After 11 years of performing these reviews, I have closed only 11 positions. Buying and holding are more than just words, I actually do it. So let's see how we're doing.

Closed Positions

Table 1 on the following page shows the performance of our closed positions. Generally it will include stocks that have at least doubled from my original purchase price and so that just enough shares are sold to cover their original cost, leaving the balance as an open position with an effective cost of $0.00. Those stocks are easily recognizable in bold green.

But closed positions can also include companies that have disappointing price performance, deteriorating company fundamentals or other negative factors.

Table 1
Closed Positions
As of November 16, 2016.
(all amounts in currency of exchange traded)

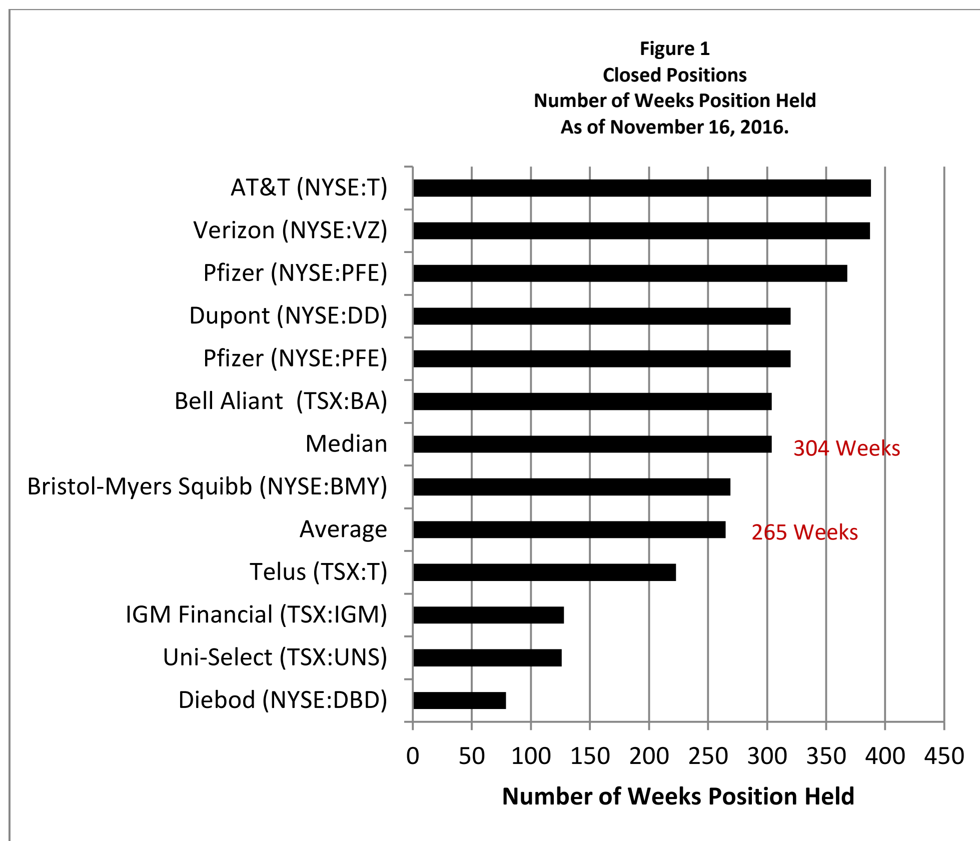
		Bought		Cumulative Dividends Per Share Since	Sold		Total Gain / - Loss		Annualized Return
Name	**Symbol**	**Date**	**Price**	**Bought**	**Date**	**Price**	**$**	**%**	**%**
Diebold	NYSE:DBD	Nov. 8, 2010	$32.51	$1.93	May 17, 2012	$36.11	$5.53	17.0%	10.9%
Telus	**TSX:T**	**Nov. 21, 2008**	**34.01**	**8.27**	**Mar. 5, 2013**	**71.99**	**46.25**	**136.0**	**22.2**
IGM Financial [1]	TSX:IGM	Nov. 16, 2010	42.18	5.85	May 3, 2013	45.99	9.66	22.9	8.7
Bristol Myers	**NYSE:BMY**	**Mar. 14, 2008**	**20.90**	**6.75**	**May 15, 2013**	**43.49**	**29.34**	**140.4**	**18.5**
Bell Aliant [2]	**TSX:BA**	**Nov. 21, 2008**	**22.01**	**12.17**	**Sept. 24, 2014**	**31.00**	**21.16**	**96.1**	**12.2**
Pfizer	**NYSE:PFE**	**Nov. 7, 2007**	**22.94**	**6.24**	**Dec. 5, 2014**	**32.04**	**15.34**	**66.9**	**7.5**
Pfizer	**NYSE:PFE**	**Oct. 9, 2008**	**16.01**	**4.56**	**Dec. 5, 2014**	**32.04**	**20.59**	**128.6**	**14.4**
DuPont	**NYSE:DD**	**Oct. 10, 2008**	**32.12**	**10.59**	**Dec. 5, 2014**	**73.04**	**51.51**	**160.4**	**16.8**
Uni-Select	TSX:UNS	Feb.28, 2013	23.01	1.41	July 30, 2015	51.98	30.38	132.0	41.7
AT&T	**NYSE:T**	**Sept. 17, 2008**	**29.00**	**13.20**	**Mar. 3, 2016**	**38.09**	**22.29**	**76.9**	**7.9**
Verizon	**NYSE:VZ**	**Oct. 6, 2008**	**27.63**	**15.16**	**Mar. 16, 2016**	**53.09**	**40.62**	**147.0**	**12.9**
Average								**102.2%**	**15.8%**

[1] Small TFSA position unrelated to larger Table 2 positions.
[2] Bell Aliant was taken over by Bell Canada. I used the takeover price in this table even though I elected to take part cash and part BCE stock.

Lots of green here, but that is to be expected on closed positions. Note the last two green additions in March 2016 of AT&T and Verizon, two boring telecoms that garnered not so boring total returns of 76.9% and 147.0% over eight years. The balance that was not sold to recover their cost remains listed in Table 3 as Open US Bond Substitutes.

But from my perspective what is far more meaningful than just looking at returns, is seeing what it took to obtain them. And you know it isn't easy, it takes a lot of patience, discipline, and confidence in value investing.

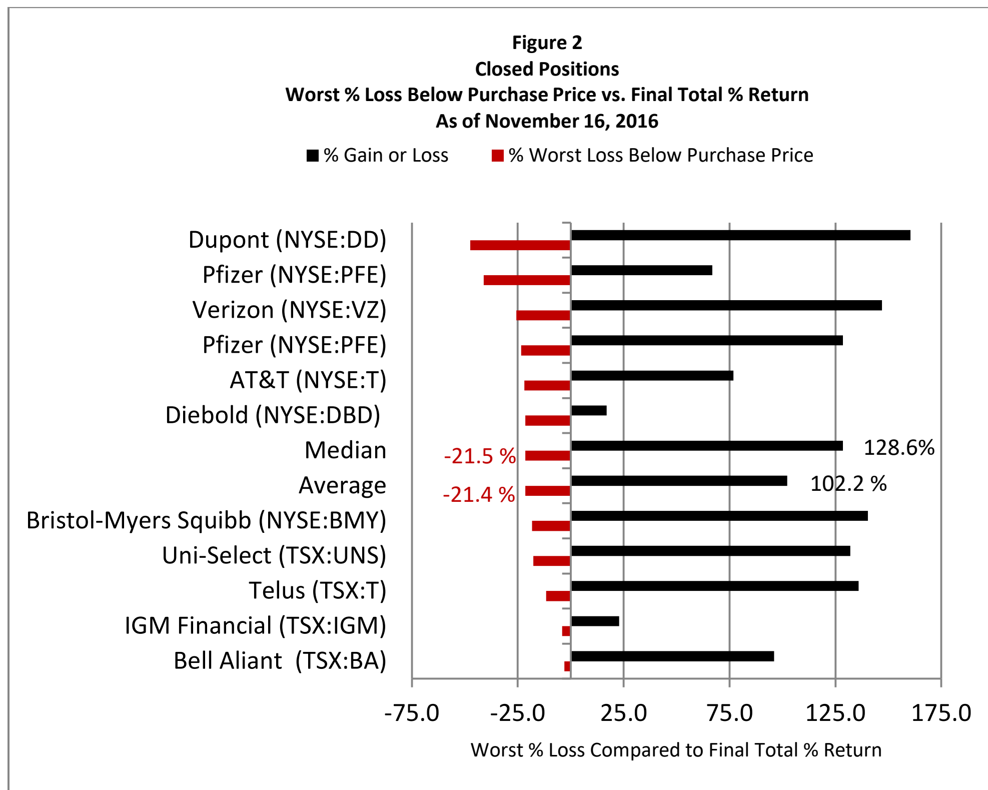
Figure 1 on the next page shows how many weeks these closed positions were held. The returns we just saw in Table 1 did not come overnight, they took years to unfold.



This is no get rich quick scheme; the median holding period has been 304 weeks. That would bring us back to 2010 when Apple introduced iPhone 4, Vancouver hosted the winter Olympics and the BP oil spill occurred in the Gulf of Mexico.

Once again I want to highlight DuPont throughout because it dominates many of the charts and tables. It appears in fourth position from the top, that makes it the fourth longest held closed position at 320 weeks. Remember that number.

Now look at Figure 2 on the next page that shows the day to day risks required to obtain the returns in Table 1. It is not such a pretty sight. The red bars show the lowest intra-day percentage decline from the initial purchase price after the stock was bought and contrasts that with the black bar that shows the stocks total return when sold.



DuPont leads the list with a 47.5% decline after buying it. But 320 weeks later (that 320 from the previous chart) on December 5, 2014 when it was sold, it had more than recovered with a total return of 160.4% (black bar). In other words, the return on DuPont was 3.4 times its worst risk.

Let's review how terrible this DuPont investment appeared to be. I bought it and then it proceeded to drop by half. Then I had to wait almost six years to finally sell it for over one and a half times what I paid for it. Was it worth the wait? Of course, but how many others would have given up much earlier and ended up losing money on what could have been a fabulously profitable position.

Let's look at what the chart tells us in another way. Let's say an investor entered all the positions in Figure 2 with $10,000 and a pre-determined stop loss at $7,850. That investor would have lost 21.5% on half of the positions even though every one of them ended up being profitable with a median return of 128.6%.

The average loss on all closed positions was 21.4% and the gain 102.2%. That is a 4.7 times greater reward than risk, and you'll remember what that means from the past series on "Accepting Losses". It would take some sort of evil genius skill to lose money with those favourable odds. Small wonder they are closed positions, and at that, many of them continue to grow and profit as cost free open positions.

Why be so confident? Because I only buy blue chip companies selling at 15 year low under-valuations that have strong balance sheets and have a record of paying uninterrupted dividends for at least 15 and preferably 20 years. That gets rid of the junk.

But closed positions do not make up an entire portfolio. By definition most of them will have done well, otherwise they would not have been closed and sold for a healthy profit. That leaves the open positions that still have additional room to grow.

Open Canadian Bond Substitutes

There were no changes in holdings. However there was a noteworthy event that I mentioned earlier. Manitoba Telecom that appears first on the list in Table 2 because it is the oldest on the list having been bought 11 years ago, it is to be acquired by BCE for $40 a share in the new year. It currently trades at a discount to that price.

Notice that Royal Bank, Bank of Nova Scotia and Great West Life all have gained over 100% but are not in bold green. That is because the two banks were reduced positions and I'm so far fine with their weighting in the overall portfolio. As for Great West Life, I can be as greedy as the next guy when I think there could be more upside, I'll keep holding on to it to see how far it will go.

If the most recent addition, Husky Energy is taken out from "Total Gain / - Loss Since Bought %" column in Table 2 below, the average total gain would be 103.4%. Since Husky Energy has only 75 weeks under its belt, it has many more weeks to go to reach the median 304 week holding period of a closed position. Just as interest rates, crude oil cannot stay at artificially induced low levels indefinitely. Market forces eventually take over and they always win and so will the energy sector. [2]

Finally, I do call them bond substitutes and for that I like to look at the "Average Yield on Cost Column" that averages out to 6.0% compared to the TSX's trailing yield of 2.83 %. [3]

Table 2
Performance
Open Canadian Bond Substitutes
As of November 16, 2016.
(all amounts in CAD)

Name	Symbol	Bought		% Yield on Cost [1]	Cumulative Dividends Per Share Since Bought	Closing Price	Total Gain / - Loss Since Bought		Annualized Total Return Since Bought
		Date	Cost				$	%	%
Manitoba Telecom	MBT	Dec. 9, 2005.	$37.50	3.5%	$24.59	$37.81	$24.90	66.4%	4.8%
IGM Financial	IGM	Sep. 29, 2008.	37.01	6.1	17.13	36.36	16.48	44.5	4.6
Royal Bank	RY	Oct. 9, 2008.	40.01	8.3*	19.65	86.03	65.67	164.1	12.7
Bank of Nova Scotia	BNS	Oct. 23, 2008.	38.41	7.7*	18.71	70.61	50.91	132.5	10.4
Great West Life	GWO	Nov. 20, 2008.	22.01	6.4*	9.79	34.44	22.22	101.0	9.1
Telus	**T**	**Nov. 21, 2008.**	**17.01**	**10.8***	**10.32**	**41.68**	**34.89**	**205.1**	**15.0**
IGM Financial	IGM	May 16, 2012.	42.01	5.3	9.88	36.36	4.33	10.1	2.2
Husky Energy	HSE	June 4, 2015.	23.91	0.0	0.30	14.05	-9.56	-40.0	-29.7
Average				**6.0%**				**85.5%**	**3.6%**

* Asterisk indicates raised dividend in past 12 months
[1] Yield on Cost: Recent quarter's dividend times 4 quarters divided by the original purchase price expressed in percentages

---

[2] As I proof read this today, energy stocks we own have risen 7.2% to 14.7% since yesterday's close.
[3] Trailing yield of TSX:XIC 2.77% + MER 0.06% = 2.83%

Open US Bond Substitutes

Table 3 below is a similar analysis for US stocks, most of which are readily recognizable names.

As I mentioned, in the past 12 months I sold enough of AT&T and Verizon to recover my cost and they now have joined the bold green family of free stocks. This year I'll have my eye on BB&T that appears twice on the list because it is one I doubled up on after it fell almost 60% in late February 2009 from my initial purchase price. Now, almost 7 years later with all of those additional re-invested dividends, that double-upped position has become extremely profitable.

Again recent purchases in mid-2015 of energy stock Conoco Philips (NYSE:COP) and another commodity based stock Potash (NYSE:POT) dragged down the overall average annualized returns. A better measurement of the average stock in the portfolio's performance is the "Total Gain / - Loss Since Bought % " column that shows an average 72.8% return even after the losses in those recently acquired stocks and Nokia.

Table 3
Performance
Open US Bond Substitutes
As of November 16, 2016.
(all amounts in USD)

		Bought					Total Gain / - Loss Since Bought		
Name	**Symbol**	**Date**	**Price**	**% Yield on Cost** [1]	**Cumulative Dividends Per Share Since Bought**	**Closing Price**	**$**	**%**	**Annualized Return Since Bought %**
BB&T	BBT	Oct. 18, 2007.	$36.83	3.3%*	$9.14	$42.82	$15.13	41.1%	3.9%
Pfizer	**PFE**	**Nov.7, 2007.**	**22.94**	**5.2***	**8.56**	**31.96**	**17.58**	**76.6**	**6.5**
Bristol Myers	**BMY**	**Mar.14, 2008.**	**20.70**	**7.3***	**11.99**	**56.20**	**47.49**	**229.4**	**14.7**
General Electric	GE	Jun. 6, 2008.	30.01	3.1	6.60	30.74	7.33	24.4	2.6
General Electric	GE	Sep. 16, 2008.	22.33	4.1	6.29	30.74	14.70	65.8	6.4
AT&T	**T**	**Sep. 17, 2008.**	**29.00**	**6.6***	**16.86**	**47.93**	**22.79**	**78.5**	**7.4**
Verizon [2]	**VZ**	**Oct. 6, 2008.**	**27.63**	**8.4***	**14.60**	**45.78**	**32.75**	**118.5**	**11.7**
Pfizer	**PFE**	**Oct. 9, 2008.**	**16.01**	**7.5***	**6.88**	**31.96**	**22.83**	**142.6**	**11.6**
DuPont [3]	**DD**	**Oct. 10, 2008.**	**29.95**	**5.1**	**13.86**	**68.88**	**48.50**	**161.9**	**14.6**
BB&T	BBT	Feb. 23, 2009.	16.80	7.1*	6.81	42.82	32.83	195.4	15.0
Nokia	NOK	Nov.4, 2010.	10.74	2.7*	2.02	4.12	-4.60	-42.8	-8.9
PPL Corp. [4]	PPL	Aug. 8, 2011.	23.08	6.6*	7.35	32.87	17.14	74.3	11.1
Exelon	EXC	Apr. 12, 2012.	37.81	3.4*	6.49	31.60	0.28	0.7	0.2
Exelon	EXC	Nov.13, 2012.	30.01	4.3*	5.43	31.60	7.02	23.4	2.4
Conoco Phillips	COP	July 7, 2015.	58.51	1.7	2.48	44.38	-11.65	-20.0	-15.1
Potash Corp.	POT	July 9, 2015.	29.21	3.4	1.51	17.58	-10.12	-34.6	-27.1
Average				**5.2%**				**72.8%**	**3.6%**

* Raised Dividend in past 12 months

[1] Yield on Cost: recent quarter's dividend times four divided by the original purchase price expressed in percentages.

[2] Inital Cost of Verizon was $29.61. It was adjusted downward by $1.98 to $27.63 to account for the spin-off of Frontier Communications in July 2010.

[3] Initial Cost of DuPont was $32.12. It was adjusted downward by $2.17 to $29.95 to account for the spin-off of Chemours Company in July 2015.

[4] Initial cost of PPL Corp was $25.33. It was adjusted downward by $2.25 to $23.08 to account for the spin-off of Talen Energy in June 2015.

With only a few exceptions most of the companies raised their dividends in the year and the overall average yield on cost was 5.2% compared to 1.9% for the S&P 500. [4]

While I was buying POT on the NYSE, some of you were either buying or eyeing pot on the TSX with far greater success. For example AW of British Columbia and IF of Alberta either bought or were closely following the following marijuana stocks.

Name	Symbol	Purchase Price	Recent Price	% Gain
Aphria	APH	$1.44	$5.17	259%
Aurora Cannabis	ACB	0.62	2.75	344%
Canopy Growth	CGC	1.97	10.60	438%
Golub Capital BDC	OGL	1.72	14.72	756%
Mettrum Health	MT	2.73	5.10	87%
Pharmacan Capital	MJN	---	1.55	

Inasmuch as I'd like to credit for this "misunderstanding" and claim that I really meant to say buy pot and not the symbol POT, I can't. But it does bring up a very important point that I want everyone to understand. I would never buy these stocks because they do not fit in with my investment style that requires 15 to 20 years of past annual reports to get an idea of a firm's balance sheet, earnings performance, dividend policy, and an idea of valuation levels over many business cycles. But that is my investment style and what I am comfortable with. It doesn't mean that it is better or even right. So by all means, when you something you like, give it a shot. Just follow the general percentage guidelines for dollar allocations to any position and that will keep you out of trouble. [5]

And for sure in this case, at least for now, the spectacular returns of these pot stocks contrast markedly with the 34.6% loss on my recent NYSE:POT purchase. However, check back in 10 years' time and we'll see which marijuana stocks survived on their own or through mergers and compare their total returns to the newly merged behemoth Potash and Agrium Corporation that short of a catastrophic event will still be in business and paying dividends.

Special Situations

The stocks appearing below as Special Situations in Table 4 are not large blue chip companies. What distinguishes them is that they are all selling at historic under-valuations, have bullet-proof balance sheets with little or no debt, sell at a fraction of their book value and usually have a long history of paying uninterrupted dividends. Most will be under-followed smaller companies. But you know that from last year's pre-amble.

[4] Trailing yield of TSX:XUS 1.76% + MER 0.10% = 1.86%

[5] You know the drill, 1.5% to 2.0% of the portfolio value for bond subs. For TFSAs, the smaller dollar amount of the previous bond sub calculation or one twelfth the value of the TFSA. (Reminder, I have reduced the dollar allocation per TFSA stock from one eighth to one twelfth for household TFSAs because they have now grown to a more reasonable size to allow for more diversification.)

But here is where it gets interesting. Last year I cheekily wrote: *So far the only thing special about these positions compared to the other categories is their lack of profits (albeit their losses fall within the expected range).*

What a difference a year makes. The average stock has a total gain of 24.5% compared to just 1.1% last year and this is mostly on account of those many purchases of Reitmans as it declined beginning to pay off and adding on to Ensign in September.

Table 4
Performance
Open Special Situations
As of November 16, 2016.
(all amounts in currency of exchange traded)

		Bought		Cumulative Dividends Per Share Since Bought		Total Gain / - Loss Since Bought		Annualized Return Since Bought
Name	**Symbol**	**Date**	**Price**		**Closing Price**	**$**	**%**	**%**
US Treasury 2 YR Bear ETN	NYSE-ARCA: DTUS	May 6, 2011.	$46.01	$0.00	$31.00	-15.01	-32.6	-6.9%
Goodfellow Inc.	TSX:GDL	Dec. 14, 2011.	7.82	2.24	10.05	4.47	57.2	9.6
Goodfellow Inc.	TSX:GDL	Jan. 18, 2012.	7.81	2.24	10.05	4.48	57.4	9.9
Reitmans	TSX:RET.A	Jan. 23, 2014.	5.81	0.55	6.77	1.51	26.0	8.6
Reitmans	TSX:RET.A	Sept. 5, 2014.	5.77	0.45	6.77	1.45	25.2	10.7
Ensign Energy	TSX:ESI	Dec. 4, 2014.	10.01	0.96	8.41	-0.64	-6.4	-3.3
Reitmans	TSX:RET.A	Sept. 14, 2015.	4.86	.25	6.77	2.16	44.4	36.9
Ensign Energy	TSX:ESI	Sept. 8, 2016.	7.99	.12	8.41	0.54	6.8	6.8 [1]
Average							**24.5%**	**9.4%**

[1] Simple not annualized return because held for less than a year.

As in other years the perennial poor performer continues to be the first one, the US Treasury 2 YR Bear ETN. I originally bought this as a position on interest rates rising and they have, but as I described last year in this space, there has been a sizeable tracking error due to the way the Exchange Traded Note (ETN) is constructed. But even at that, this looks like it is turning around and becoming a play just as much on rising US inflation and interest rates. Just in this month alone it has moved from $29 to $32 or 10.3% (even a dollar higher than its November 16th price in the above table) and volume is picking up from its anemic levels. This adds a new wrinkle and if the new US administration pursues an expansionary economic and fiscal policy, interest rates and inflation will rise faster than assumed in the pricing of this ETN. What I wrote last year may just be finally happening:

> *A very possible scenario is that once rates start moving up, they move more rapidly than the Federal Reserve would like and the ETN would begin advancing more quickly to the upside than the futures market is currently forecasting. We'll see. But the bottom line is that there is way more upside to downside on this position. It has been a surprise how poorly the ETN tracks the actual 2 year Treasury interest rate. But bad luck can often be offset by good luck as I bought this USD denominated*

security when the CAD was at $1.02 and it is now $0.75. The gain on the appreciation of USD has practically covered the loss on the security.

Still, if you do not own it, I wouldn't be tempted into buying it with new money unless it is for a tiny dollar amount and with speculative money only. There are too many problems with tracking errors with this ETN.

Having looked at returns, but how about the risks that were taken along the way to achieve them?

All Positions - Risk / Reward

We previously looked at the risk / reward of closed positions in Figure 2 on page 5. Now we'll expand the list to include all stocks, both open and closed that are mentioned in this report.

If you are new, I bet you are wondering how come this is the first time that you have seen anything like this - someone describing risk and losing money with real life examples from his portfolio. It is because smoothed out performance from multi-year annualized returns can hide treacherous periods of sharp and often intolerable losses. Everyone should know about this beforehand so that no one is suddenly and unexpectedly confronted with an unpleasant surprise. When one is prepared for the worst, there is less of a chance of abandoning positions at the worst possible time only to miss the inevitable recovery.

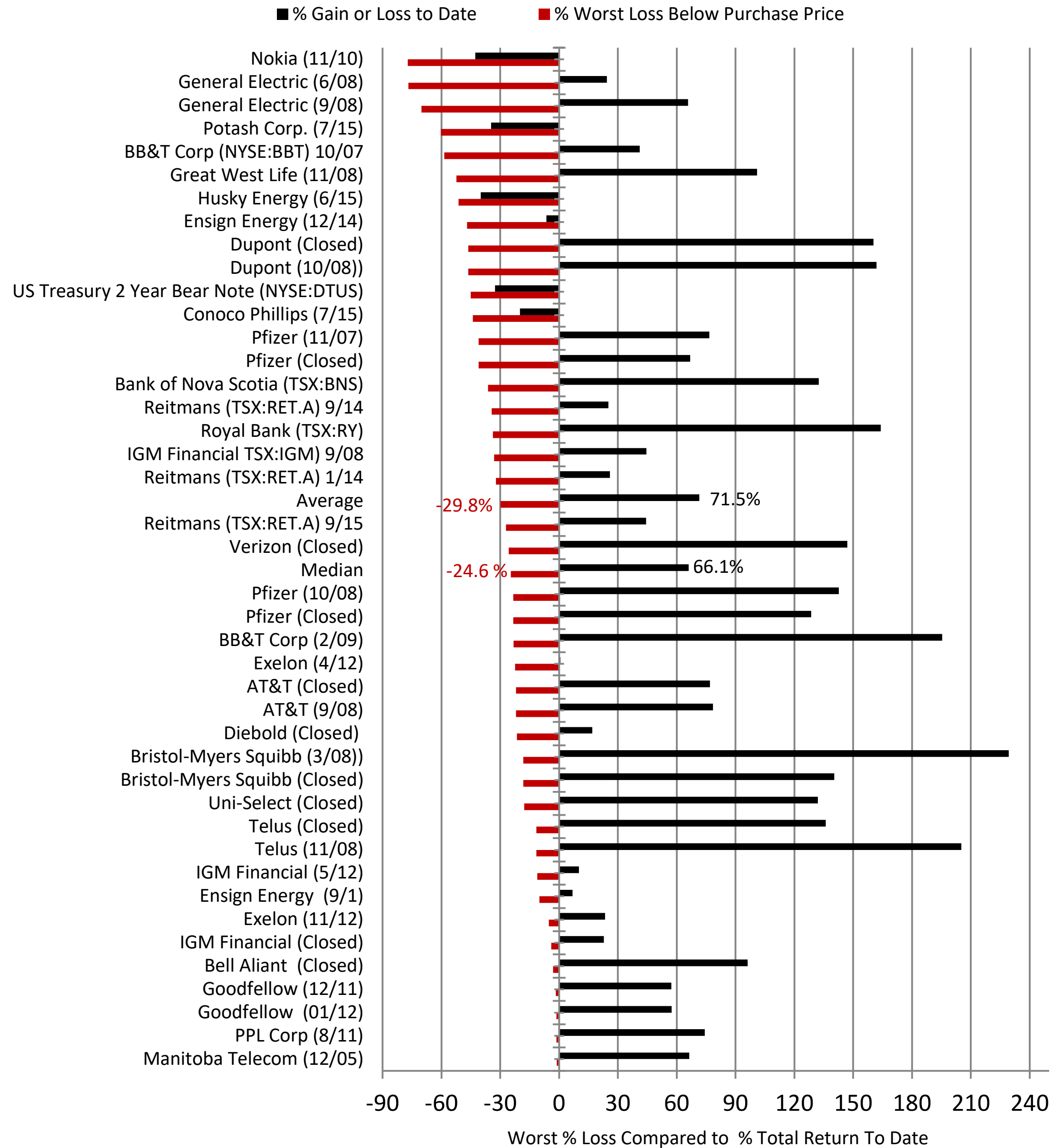
Figure 3 on the next page shows what many of us had to endure, both good and bad, over the entire period. It ranks each stock from the worst dollar loss from its original purchase price (top) to the least (bottom). A name can appear more than once because it was an addition to an existing position or partially closed with the remainder held open. [6]

We want the black lines showing total return to be long and to the right and the red lines showing the losses after the initial buy to be short and to the left. And the great majority of the holdings follow that pattern except for my most recent purchases of Potash, Husky and Ensign. But while I don't like it, it is not unusual. Refer back to Figure 1 on page 4 where we saw that the median holding period of a closed position is 304 weeks. Those three recent acquisitions are still in their infancy at less than 75 weeks.

From just a passing glance the returns (black bars) for almost all of the positions dwarf any unrealized losses (red bars) required to obtain those returns. Of the 42 positions, 36 are profitable with an average gain of 71.5% against an average loss after purchase of 29.8%. In other words 75% of the positions are profitable with a reward to risk ratio of 2.4:1. Those are the sort of odds we all want our side.

---

[6] Additions of the same stock are usually made to lower its average cost. Partially closed positions are generally ones where the initial cost is recovered and the remainder held open is essentially free stock (highlighted in bold green throughout the report).



I always like to highlight something negative to keep a balance. Earlier we looked at DuPont, now how about General Electric in the second and third positions from the top? (Meaning it had the second and third worst losses of all holdings.) From Table 3 on page 7 we learn that I made my first purchase in June 2008 at $30.01 and if I thought it was a bargain at that price, I bought more at an even lower price when it hit $22.33 in July 2008. But as you can see in the chart above, that was just a resting point on its journey to over a

70% decline. But eight years later, they are up 24.4% and 65.8% respectively, not great, but a lot better than realizing a loss up to 70%.

Why doesn't everybody show their performance in the same way as I do in Figure 3? There would be fewer disappointed investors out there, but there would also be a lot less investors handing over their money to the investment industry once they learned what is hidden underneath those multi-year annualized return numbers.

Before moving on to my annual rebalancing nudge for the Balanced ETF Portfolio, I want to emphasize how important it is for readers to understand the risk side of the risk / reward equation. It is often, if not always, overlooked when discussing performance because most investors over-estimate their risk tolerance and run at the first sign of trouble. Again, look at the average loss of almost 30% per position, even if that loss is eventually dwarfed by profits that are two to three times greater than that initial risk.

Rebalancing of Balanced ETF Portfolio

As I repeat each year[7], November is as good a time as any to rebalance one's portfolio. It should be reviewed once a year anyway and so why not have a few seasonal indicators working for you at the same time? (Even if their long term validity is questionable.) The period from November to May is usually strong for stocks. Combine that with periods surrounding holidays that also demonstrate strength (between US Thanksgiving and the beginning of the New Year) and you have a confluence of positive seasonal factors.

Since I am still in the process of selling off USD ETFs and re-allocating them to their CAD equivalents, my rebalancing will most likely be different from yours. However, what you may want to be aware of is that when updating the blue cells in my Excel *Portfolio Set-Up & Rebalancing* Worksheet, I am continuing to keep my equity exposure to 40% of its target of 50% (or 80% of target). Also, you may want to apply that same 80% of target to your fixed income ETFs as well because it is as close to a certainty that in the coming year interest rates are going to finally rise in earnest. Therefore, the fixed income ETFs in our portfolios are going to fall in price (albeit by far less than the standard fixed income ETFs used in passive portfolios with durations of seven plus years or more). [8]

In anticipation of this, I have placed a lot of extra cash over and above reserves for buying bond subs, special situations and hedging into a two year ladder of GICs using at the most 6 month intervals. That way, every six months or less I'll have a GIC maturing that will be re-invested at a higher interest rate and I won't be stuck holding a 5 year GIC at historically low rates. Alternatively, one can allocate a fixed amount of cash every two to three months to two year GICs so that in two years' time one would have a GIC maturing every few months and then one can decide what maturity intervals make the most sense in that interest rate environment. Remember to make sure your GICs qualify for CDIC protection per institution per account. It is trickier than it first appears to be. See this video.

[7] I'm a little late this year.
[8] TSX: CLF, BXF, and CBO have durations of less than 3 years.

Conclusion

It is too bad that everyone could not have started off at the same time when I began publicly making these recommendations. Forget about my lucky (and not so lucky) stock selections. I have had one of the more unheralded but powerful diversifiers working for me over all of these years – time. While I may have recent buys losing, older ones are grinding away profits, and sometimes hefty ones that more than offset the losses of the newer acquisitions. The end result is an ever growing overall portfolio that has been making all-time new highs.

Now for my usual caveats that are best remembered whenever someone is trying to sell you something, especially if it has to do with money. First, always be mindful that any presentation of performance that has less than 10 years of data (or even better 15 years) is pretty well meaningless and most likely the result of luck. Second, unless I make any new additions or deletions to my "Bond Substitutes", "Special Situations", or "Closed Positions" be prepared to hear nothing more about them until next November when we will do this all over again.

I also like to always remind everybody that this is in real time, with real money and I treat investing like a business. You won't hear me gloating over successes or moaning over failures. That is all part of it. What matters is the risk-adjusted performance of the portfolio over the longer term and that it meets one's goals. This is not about self-promotion, excitement or entertainment. Anyone looking for a thrill can easily find it elsewhere.

Finally, if you do not hear from me again in 2016, thank you for the past year. Have a happy and peaceful holiday.

Fred

NOTE

Permanent Alert and *Capital Ideas* are paid subscription publications of Dimensional Investment Planning Inc. focusing on the relationship between financial and investment planning. It is published when there is something worthwhile to convey.

While the information and planning strategies presented in this publication are believed to be effective, there is no guarantee that they will perform that way in the future. Performance is historical and does not represent future results. Neither Dimensional Investment Planning Inc. nor the author assume any liability whatsoever for any loss arising from any use of this publication or its contents. Any and all such liability is hereby expressly disclaimed.

This publication is designed to provide accurate and authoritative information from sources considered reliable, but no representation or warranty, express or implied, is made as to its accuracy or completeness. The information contained herein has been distributed for educational purposes only and contains the current opinions of the author and such opinions are subject to change without notice. It is not, and is not to be construed as an offer to sell or solicitation of an offer to buy any securities. It is published with the understanding that Dimensional Investment Planning Inc. and the author are not engaged in rendering legal, accounting, or other professional advice. If legal or other professional advice, including financial, is required, the services of a competent professional person should be sought.

© MMXVI by Dimensional Investment Planning Inc. All rights reserved.