CAPITAL IDEAS

RESEARCH YOU CAN REALLY USE

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2017 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

With markets at all-time highs and an eight and a half year advance, I used this year to do some partial selling of long held positions to recover their initial cost and effectively hold the remainder for "free". These positions are identifiable by their green font and will appear in both the Closed and Open position tables.

As you'll see, when I use the term "long held', I'm not kidding. The positions I sold just in this past year alone had an average holding period of 8.8 years and although their average total return was 104.2%, it is of little consolation to those who are more recent arrivals and were not able to obtain those particular stocks at what then were attractive prices. (Although it is amusing listening to various media experts advising readers and listeners to buy say bank stocks at these lofty prices when we had already done so 10 years ago at less than half their current price and still hold them.)

As the markets have advanced over the past eight and a half years, blue chip bargains have become scarcer and scarcer. Although there were still bargains to be had in recent years (think energy and material sectors, along with under-followed small caps), by their nature, they have been more volatile and their dividends not as secure as the type of stable stocks that were on sale in 2008-9.

But this is where it gets interesting for newer arrivals, those long held stocks with the 100% + returns that I have partially sold in the past 12 months had an average unrealized loss before becoming profitable of 31.4%. As you'll see in the following Exhibits, I can't seem to be able to shake that 30% average loss number. I have quipped in the past that a profitable strategy for others might be to note the price that I buy something and then wait for a further 30% decline before acting. But then, one misses the ones that don't drop as well as the re-invested dividend while waiting - perhaps a compromise would be to buy a portion at my price and the remainder at a lower one?

I did add three positions this year. Early on I added on to the small cap Special Situation Goodfellow (TSX:GDL), in the spring initiated a position in another Special Situation type stock Accord Financial (TSX:ACD) and just recently bought my first Bond Substitute in almost two and a half years in Enbridge (TSX:ENB). When the new positions for Accord and Enbridge were bought they were yielding 4.1% and 5.1%, well over twice the current interest rate on Government of Canada Benchmark 10 Year Bonds and at least 50% greater than the trailing yield on the TSX. [1] That is what we are looking for.

And as I remind everyone each year before beginning this review, remember that *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.*

I'll try to let the Exhibits speak for themselves, but when I do comment, don't be taken back by my focus on the negative. For those who have been following me over the past decade plus, there has been a lot to be happy with in the following pages, but learning often comes from adversity. Besides, I can't stand the usual performance review that emphasizes everything that was rosy, spins what was mediocre and conveniently ignores everything else, and I bet you can't either

Closed Positions

Exhibit 1 on the next page shows the performance of the 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 and will appear in the tables for both the Closed (Exhibit 1) and Open (Exhibits 6, 7 & 9) positions.

[1] 10 Year Government of Canada Benchmark 10 Year Bond Yield: 1.94% , iShares Core S&P / TSX Capped Composite Index Trailing Yield (TSX:XIC) : 2.74%

Exhibit 1
Closed Positions
As of November 10, 2017.
(all dollar amounts in currency of exchange traded)

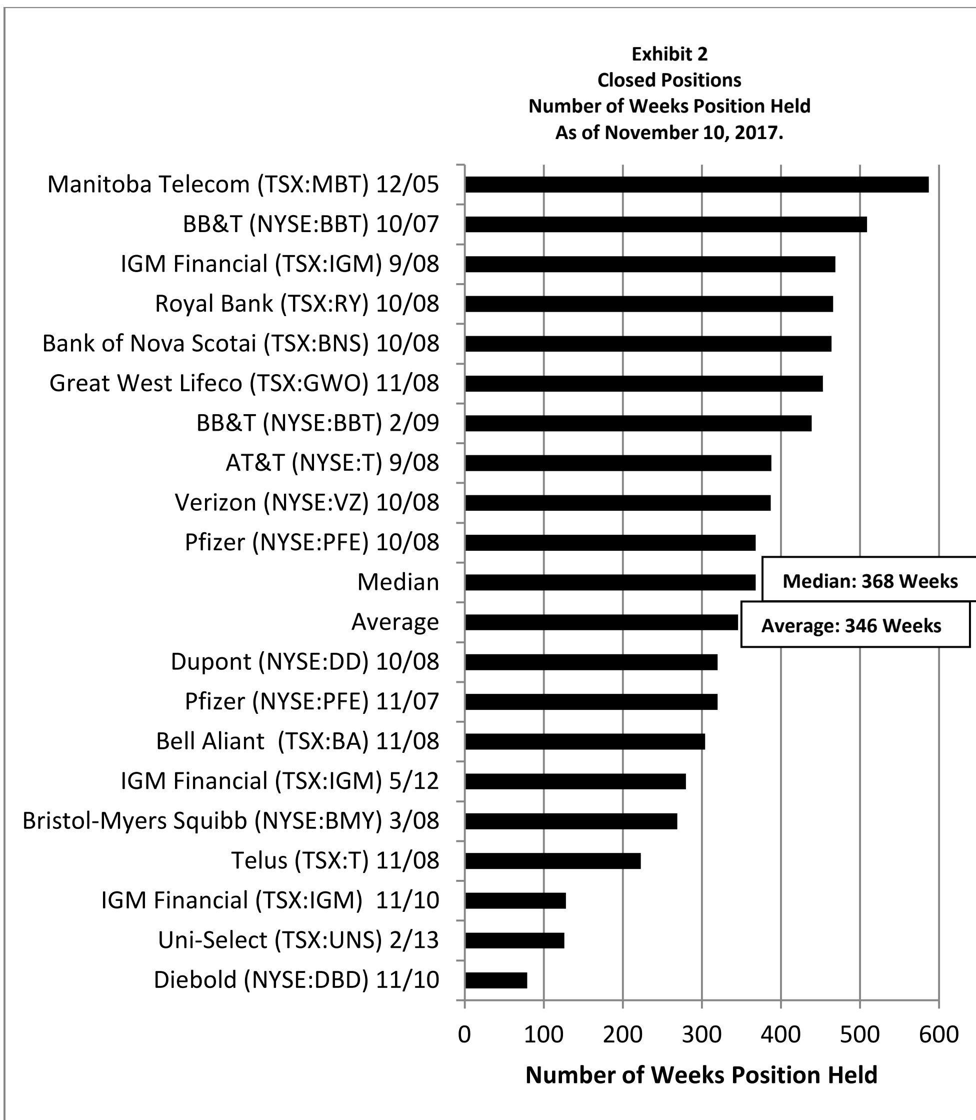
Name	Symbol	Bought Date	Bought Price	Cumulative Dividends Per Share Since Bought	Sold Date	Sold Price	Total Gain / - Loss $	Total Gain / - Loss %	Annualized Return %
Diebold	NYSE:DBD	Nov. 8, 2010	$32.51	$1.93	May 17, 2012	$36.11	$5.53	17.0%	10.9%
Telus	TSX:T	Nov. 21, 2008	34.01	8.27	Mar. 5, 2013	71.99	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 [3]	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
Manitoba Telecom [4]	TSX:MBT	Dec. 9, 2005	37.50	24.59	Mar. 23, 2017	39.85	26.94	71.8	4.9
BB&T	NYSE:BBT	Oct. 18, 2007	36.83	9.74	Aug. 4, 2017	48.40	21.31	57.9	4.8
BB&T	NYSE:BBT	Feb. 23, 2009	16.80	7.41	Aug. 4, 2017	48.40	39.01	132.2	15.3
Great West Life	TSX:GWO	Nov. 20, 2008	22.01	10.87	Aug. 9, 2017	36.30	25.16	114.3	9.1
Royal Bank	TSX:RY	Oct. 9, 2008	40.01	22.22	Sept. 27, 2017	95.19	77.40	193.5	12.8
Bank of Nova Scotia	TSX:BNS	Oct. 23, 2008	38.41	20.97	Sept. 27, 2017	80.00	62.56	162.9	11.4
IGM Financial	TSX:IGM	Sep. 29, 2008	37.01	19.38	Oct. 5, 2017	43.25	25.62	69.2	6.0
IGM Financial	TSX:IGM	May 16, 2012	42.01	12.13	Oct. 5, 2017	43.25	13.37	31.8	5.3
Average								**103.0%**	**12.8%**

[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.
[3] Dupont Merged with Dow in 2017 and changed symbol to DWDP.
[4] Manitoba Telecom 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.

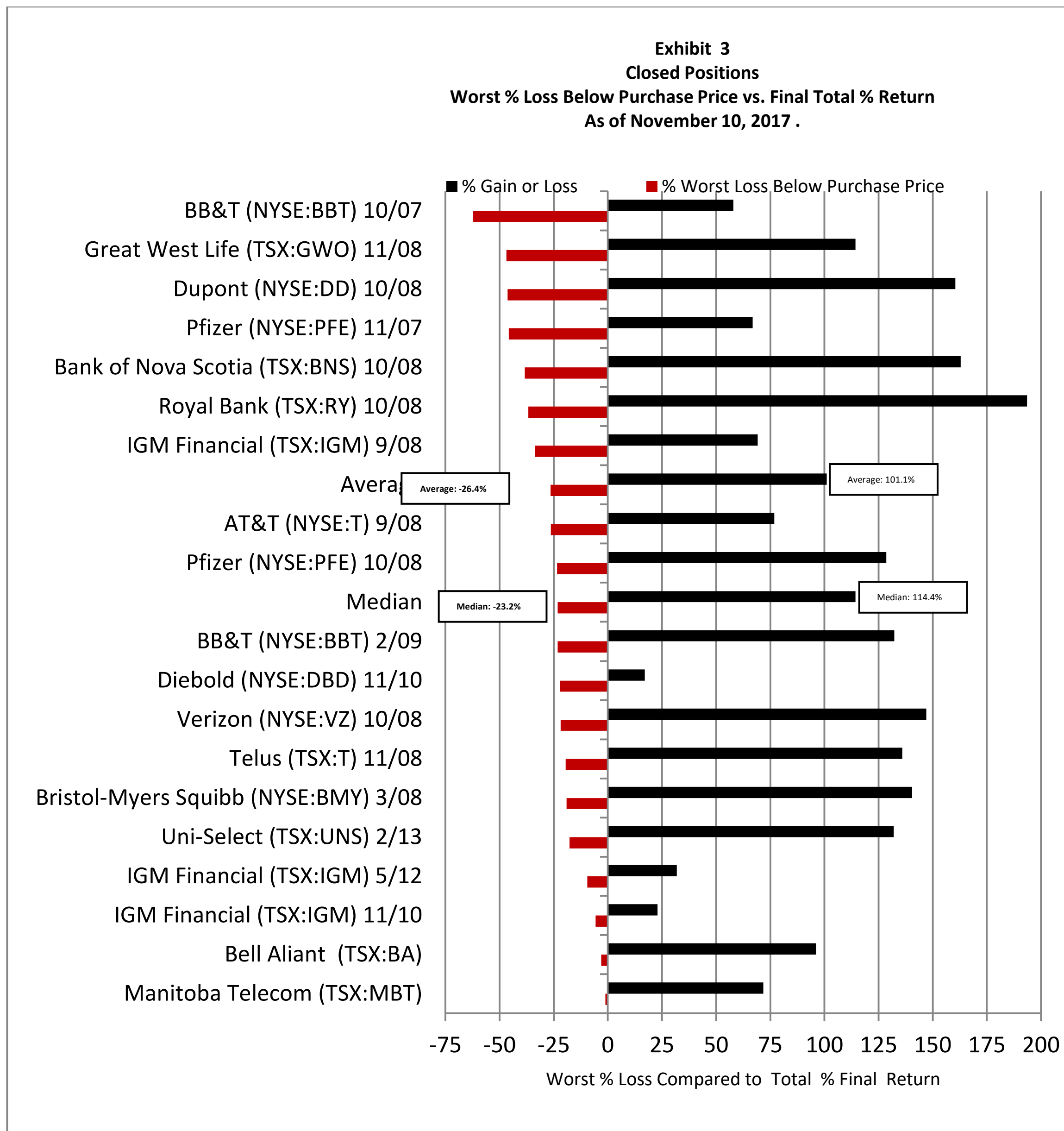
Don't be overly impressed by all of the green and great returns, after all these are closed positions and I try to take at least partial profits on anything that advances by 100%. So eventually, by definition, all winners become at least partially closed.

Another misconception that I have found people might have is that the average annualized return of 12.8% is the return one would average year in and year out in this portfolio. It isn't, it is the average annualized return of each stock in Exhibit 1 over the time that each of those stocks happened to be held. For example, take Bell Aliant's 12.2% annualized return from November 21, 2008 to September 24, 2014 (304 weeks). Compare that to Royal Bank's 12.8% return from October 9, 2008 to October 5, 2017 (466 weeks). They both have about the same annualized return but Royal Bank continued at it for 162 more weeks. Again From Exhibit 1, that translates into a total gain in the period held of 193.5% for Royal Bank and 96.1% for Bell Aliant.

Exhibit 2 on the next page is so important. It shows how many weeks these closed positions were held. These returns took years to come to fruition. The median number of weeks is 368, that is just over 7 years.



Now look at Exhibit 3 on the next page that shows the day to day risks required to obtain the returns in Exhibit 1. Sausage making indeed! 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 stock's total return when sold.

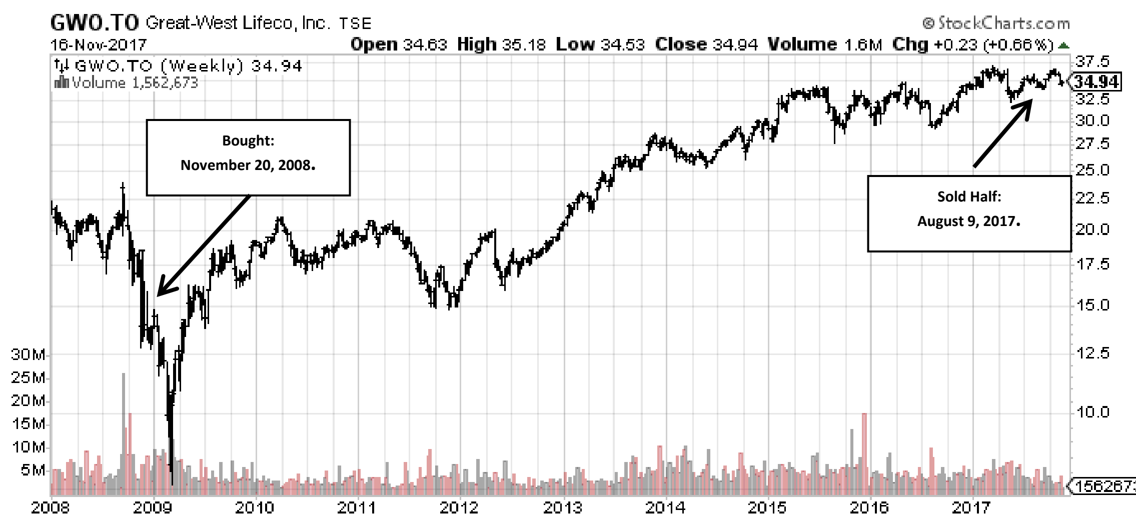


The average unrealized loss before a position became profitable was -26.4% and the average gain 101.1%. So on average if one panicked and sold after a 26.4% loss, instead of making 101.1%, the impatient investor would have been stuck with a substantial loss instead (and would have either abandoned investing in stocks altogether or at the very least regretted ever contacting me and moved on – only to repeat the same process all over again with the same result). Remember from Exhibit 2 that the time from buying to selling took on average 346 weeks or nearly 7 years to complete. And at that in most cases only a portion of the stock was sold to recover its initial cost.

Now let's take a specific example, Great West Life and apply the cold data from Exhibit 3 to a weekly price chart on the next page to get more of an emotional feel for what Exhibit 3 is really telling us. We know from the red bar above for Great West Life that it had an unrealized

loss of 46.8% before being partially sold to recover its cost with the black bar showing a gain of 114.3%. Now see what this looks like on the weekly logarithmic total return price chart below.[2]

Exhibit 4
Great West Life Total Return
Weekly
2008 - 2017



Source: StockCharts.com

What I want to highlight here is simply how brutal the decline of the stock was immediately after I bought it on November 20, 2008. This was not any ordinary garden decline, it was sharp and fast. The 46.8% loss to its lowest price on March 9, 2009 took just 16 weeks but I did not waiver and hung on and you know why. The stock on November 20, 2008 met all of my blue chip stock requirements; it was undervalued and had a high dividend yield among other attributes. I limited the size of the purchase to no more than 2% of the portfolio, so even if the stock went to zero, I would lose no more than 2% of my portfolio.

Well look what happened, as sharply as it fell, it just as rapidly advanced from its low in March 2009 and never looked back although it did take its time to advance to over a 100% gain triggering my selling half on August 9th of this year to recover its initial cost and allowing me to hold the remaining balance as an open position for effectively no cost.

See why I did not waiver? I was buying an established blue chip company with a long record of profitability and generous dividend payments at what at least then before it collapsed was a favourable price. But that was just the company. In terms of risk management and the portfolio, I limited the size of the position to no more than 2% of the portfolio and since half of the portfolio is invested in fixed income, even if I bought 25 of these type of stocks, did not hedge, and they all went to zero, I'd be down 50% of the portfolio rather than 100%. Instead, as

[2] In earlier write-ups I have briefly mentioned that StockCharts has its own way of presenting total return charts where it adjusts past prices downward to account for dividend payments. Therefore historical prices on the chart will not coincide with actual prices, but the price movements are all correct because the adjustments are relative to each other. If you are interested, more information and the rationale can be found here.

you have seen the opposite happened and now I am holding almost all of these closed stocks after a 100% advance forever for free.

Open Canadian Bond Substitutes

Exhibit 6 on the next page is almost all green with "free stocks" from this year's partial sales of Great West Life, Royal Bank, Bank of Nova Scotia and IGM Financial. Manitoba Telecom that appeared last year as an Open position moved to Closed in Exhibit 1 as it was bought out by BCE and assumed no share exchange. I chose to receive a combination of BCE stock and cash for Manitoba Telecom just like I did when BCE bought Bell Aliant even though I am recording it for these annual performance reviews to be conservative as a straight sale with no BCE stock.

As a result I have accumulated a welcomed position in BCE from these share exchanges even though I have as yet to buy BCE outright. Exhibit 5 is a total return chart of BCE from the first share exchange with the Bell Aliant merger onward that explains a good part of its growing presence in my portfolio and of course the re-invested dividends don't hurt the compounding either.

Exhibit 5
Bell Canada Enterprises
Weekly
June 1, 2014 – November 20, 2017

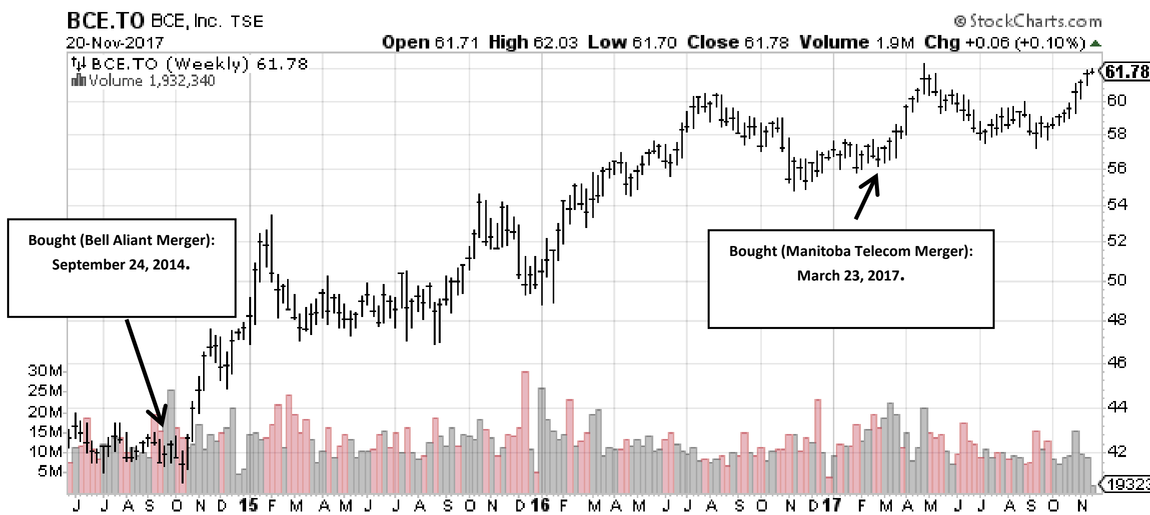


Exhibit 6 Performance Open Canadian Bond Substitutes As of November 10, 2017. (all dollar amounts in CAD)									
		Bought			Cumulative Dividends Per Share Since Bought		Total Gain / - Loss Since Bought		Annualized Total Return Since Bought
Name	Symbol	Date	Cost	% Yield on Cost [1]		Closing Price	$	%	%
IGM Financial	**IGM**	**Sep. 29, 2008.**	**37.01**	**6.1%**	**$19.38**	**$44.19**	**$26.56**	**71.8%**	**6.1%**
Royal Bank	**RY**	**Oct. 9, 2008.**	**40.01**	**8.7***	**23.05**	**99.84**	**82.88**	**207.1**	**13.2**
Bank of Nova Scotia	**BNS**	**Oct. 23, 2008.**	**38.41**	**7.9***	**21.71**	**83.16**	**66.46**	**173.0**	**11.7**
Great West Life	**GWO**	**Nov. 20, 2008.**	**22.01**	**6.7***	**11.24**	**34.71**	**23.94**	**108.8**	**8.6**
Telus	**T**	**Nov. 21, 2008.**	**17.01**	**9.3**	**12.04**	**48.47**	**43.50**	**255.7**	**15.2**
IGM Financial	**IGM**	**May 16, 2012.**	**42.01**	**5.4**	**12.13**	**44.19**	**14.21**	**34.1**	**5.5**
Husky Energy	HSE	June 4, 2015.	23.91	0.0	0.30	16.68	-6.93	-28.9	-13.1
Enbridge	ENB	Nov. 2, 2017.	47.69	5.1*	0.00	46.29	-1.40	-2.9	-2.9 [2]
Average				**6.2%**				**102.3%**	**5.5%**

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

Two points I want to highlight from Exhibit 6. First are the holdings' average yield on cost of 6.2%, that is 125% greater than the trailing yield on the TSX and 226% more than the yield on 10 year Government of Canada Bonds. I was once asked why I use yield on cost as a measurement when it does not reflect the stock's current yield that is generally lower, often far lower. The reason is because that although these positions are categorized as equity in our portfolio, I really consider them as stocks that are so desirable that they become more like "bond substitutes" and their yield on cost is a comparable measure to the yield to maturity on the date that a bond is purchased. And of course, unlike a bond's coupon that is fixed, a stock's dividend can change. When it is increased, so is its yield to cost, unlike a bond where the buyers yield to maturity when bought remains the same if held to maturity.

The second point is to help everyone understand how the Exhibits relate to one another regarding the green open positions in Exhibit 6 and their closed counterparts in Exhibit 1. Let's take an extreme example like Telus to make the point, it has a total percentage return (and that is just so far because it is open) of 255.7%. Now refer back to Telus's equivalent total return in Exhibit 1 of 136.0%. What that means is that Telus is not only an effectively cost free stock but has gained another 119.7% since it was partially sold to recover its cost. How'd you like to be Mr. Darren Entwistle or at least in Telus's stock bonus program?

Open US Bond Substitutes

Exhibit 7 on the next page is a similar analysis for US stocks, most of which are readily recognizable names.

Exhibit 7
Performance
Open US Bond Substitutes
As of November 10, 2017.
(all dollar amounts in USD)

Name	Symbol	Bought Date	Bought Price	% Yield on Cost [1]	Cumulative Dividends Per Share Since Bought	Closing Price	Total Gain / - Loss Since Bought $	Total Gain / - Loss Since Bought %	Annualized Return Since Bought %
BB&T	BBT	Oct. 18, 2007.	$36.83	3.6%*	10.37	$46.13	$19.67	53.4%	4.4%
Pfizer	PFE	Nov.7, 2007.	22.94	5.6*	9.82	35.18	22.06	96.1	7.0
Bristol Myers	BMY	Mar.14, 2008.	20.70	7.5*	13.55	60.86	53.71	259.5	14.2
General Electric	GE	Jun. 6, 2008.	30.01	1.6	7.56	20.49	-1.96	-7.1	-0.7
General Electric	GE	Sep. 16, 2008.	22.33	2.1	7.25	20.49	5.41	24.2	2.4
AT&T	T	Sep. 17, 2008.	29.00	6.8*	18.82	34.22	24.04	82.9	6.8
Verizon [2]	VZ	Oct. 6, 2008.	27.63	8.5*	16.91	44.88	34.16	123.6	9.3
Pfizer	PFE	Oct. 9, 2008.	16.01	8.0	8.14	35.18	27.31	170.5	11.6
DowDuPont [3]	DWDP	Oct. 10, 2008.	23.39	6.5*	15.70	69.97	62.28	266.3	15.4
BB&T	BBT	Feb. 23, 2009.	16.80	7.9*	8.07	46.13	37.40	222.6	14.4
Nokia	NOK	Nov.4, 2010.	10.74	1.2	2.15	4.91	-3.68	-34.3	-5.8
PPL Corp. [4]	PPL	Aug. 8, 2011.	23.08	6.8*	8.93	36.29	22.14	95.9	11.4
Exelon	EXC	Apr. 12, 2012.	37.81	3.5*	7.79	41.30	11.28	29.8	4.8
Exelon	EXC	Nov.13, 2012.	30.01	4.4*	6.73	41.30	18.02	60.0	9.9
Conoco Phillips	COP	July 7, 2015.	58.51	1.8*	3.54	52.99	-1.98	-3.4	-1.5
Potash Corp.	POT	July 9, 2015.	29.21	1.4	1.91	19.07	-8.23	-28.2	-13.2
Average				**4.8%**				**88.2%**	**5.7%**

* 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. In 2017 adjusted by .781 for merger with Dow.
[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.

The average yield on cost is 4.80% compared to the S&P 500's trailing yield of 1.85% and US 10 Year Bond Yield of 2.35%.

Apart from General Electric, as expected the longer held positions are doing the heavy lifting while waiting for the more recent purchases of Conoco Philips and Potash to turn around. Nokia has been a disappointment, whenever it has shown any traction it has a habit of giving it back just as quickly. Some consolation is from it being bought when the CAD was trading at parity to the USD largely offsetting its 34.3% loss by the currency gain. I am still holding on.

Exelon had a good year, like most value stocks that I buy, it took its time trading between $26 to $37 (I bought it in 2012 just under $38 and then doubled up at about $30), but in 2017 broke out to five year highs over $40 and has so far managed to stay there. I like utilities not only for their high yields that pay you as you wait for the price to appreciate, but also for their generally lower volatility and fit with my stock valuation method. It is not a coincidence that Benjamin Graham in his book the *Intelligent Investor* went so far as to call it "The Public-Utility Solution" Here are a few of his observations:

> *If we turn to the field of public-utility stocks we find a much more comfortable and inviting situation for the investor. Here*

the vast majority of issues appear to be cut out, by their performance record and their price ratios, in accordance with the defensive investor's needs as we judge them. [3]

.....In comparison with prominent industrial companies as represented by the DJIA (Dow Jones industrial Average), they offered almost as good a record of past growth, plus smaller fluctuations in the annual figures – both at a lower price in relation to earnings and assets. The dividend return was significantly higher. The position of the utilities as regulated monopolies is assuredly more of an advantage than a disadvantage for the conservative investor. Under law they are entitled to charge rates sufficiently remunerative to attract the capital they need for their continuous expansion and this implies adequate offsets to inflated costs. While the process of regulation has often been cumbersome and perhaps dilatory, it has not prevented the utilities from earning a fair return on their rising invested capital over many decades. [4]

Little has changed since that was written nearly 45 years ago. I monitor many utilities in both Canada and the US (including both Telecoms and Pipelines) and patiently wait for them to meet my buy level valuation zones. They have been few and far between over the past decade with investors reaching for yield and driving their prices well above bargain levels. There are going to be a lot of disappointed income oriented investors who ignored heeding valuations in coming years.

Special Situations

The stocks appearing as Special Situations in Exhibit 9 on the next page 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 reasonable debt levels, 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.

While the price of these stocks can be volatile, their businesses are far less so and that is why I own them. Two years ago in 2015 when they were struggling 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).*Then last year their average gain jumped to 24.5%, and now we have gone full circle with my 2015 comment just as appropriate now as it was then. Except for US Treasury 2 YR Bear ETN (NYSE-ARCA:DTUS) I am as optimistic now as I was when I bought them on their future prospects it is just taking more time. I'm happy to own the company, its stock price will follow.

I have three unequally weighted positions in Goodfellow and Reitman's, and a double position in Ensign Energy. Their balance sheets continue to be strong as shown in Exhibit 8.

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[3] Benjamin Graham, *The Intelligent Investor,* (New York: Harper & Row, 1973), p. 190.
[4] Ibid., p.193.

Exhibit 8 Price, Selected Balance Sheet Ratios, & Ownership As of November 10, 2017.					
Name	**Symbol**	**Price**	**Book Value**	**Long Term Debt to Equity**	**Operator Ownership**
Goodfellow	TSX:GDL	$8.15	$12.50	0.00	54.1%
Reitmans	TSX:RET.A	4.55	9.42	0.00	57.0
Ensign	TSX:ESI	6.72	10.40	0.45	18.2

All of these companies continue to trade at a large discount to book value and their book value is above their average cost. When these companies trade at just their book value they will all be profitable. Ensign has an acceptable Long Term Debt to Equity ratio of well under 1.00 with Goodfellow and Reitmans having none. Goodfellow and Reitmans have more than half of their stock owned by company insiders putting their interests in alignment with their shareholders. And let's not forget Reitman's and Ensign's current dividend yield of 4.5% and 7.9%.

My guess is that the odds favour at least one of these companies being sold or taken private. I say this because the major shareholders of Goodfellow and Reitmans are into their seventies and beyond and would prefer retirement. When the price of oil stabilizes at higher levels and if Ensign's stock remains depressed, it could well be a takeover target. Even if none of that happens while these companies show improvement in their profitability, their share prices will respond. An extreme but good example is what happened to the price of Ensign in just one day. On April 11, 2016 it closed at $6.34 and the next day closed at $8.20, a 21% increase.

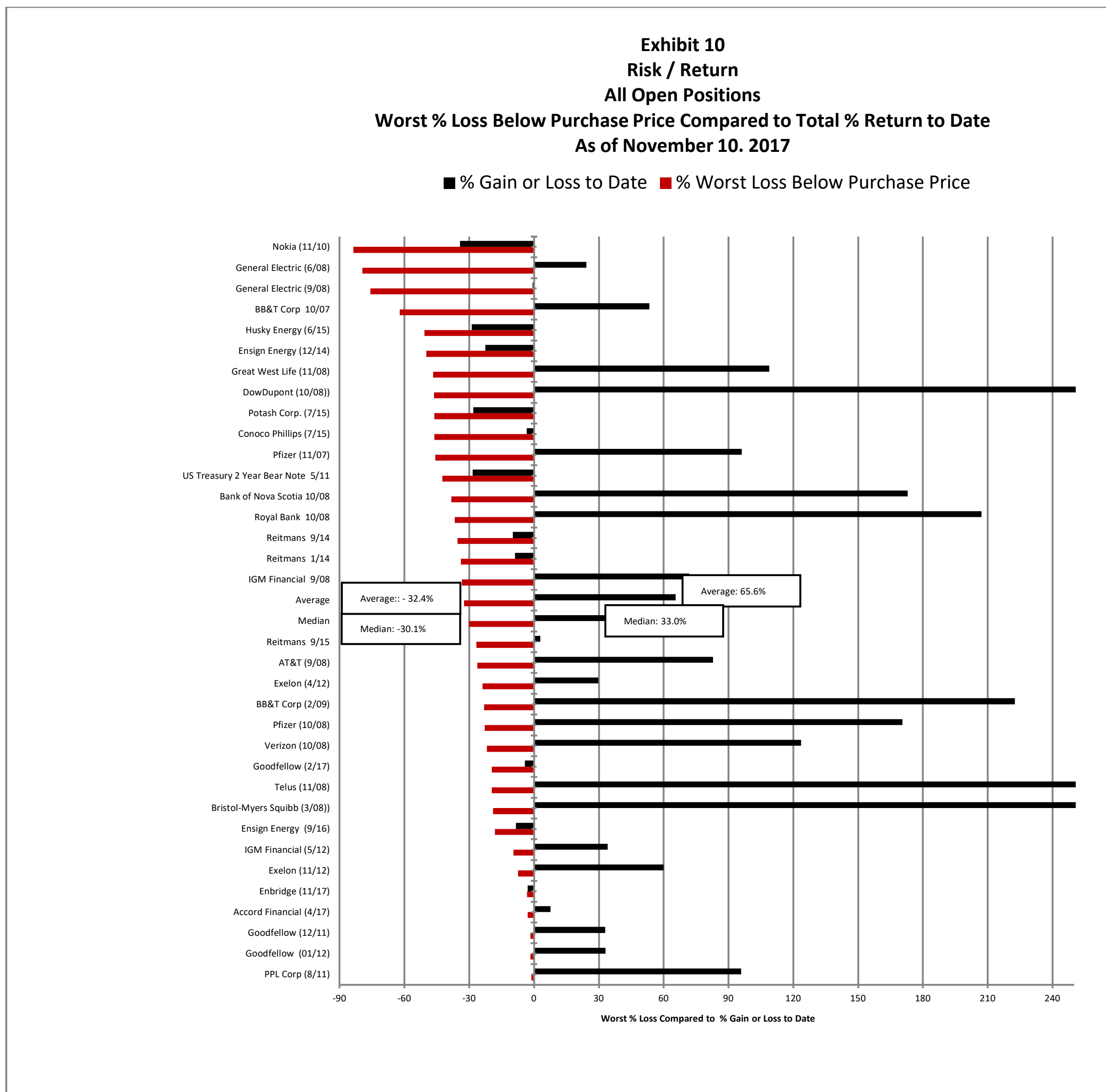
Exhibit 9 Performance Open Special Situations As of November 10, 2017. (all dollar amounts in currency of exchange traded)								
		Bought		Cumulative Dividends Per Share Since Bought		Total Gain / - Loss Since Bought		Annualized Return Since Bought
Name	**Symbol**	**Date**	**Price**		**Closing Price**	**$**	**%**	**%**
US Treasury 2 YR Bear ETN	NYSE-ARCA: DTUS	May 6, 2011.	$46.01	$0.00	32.96	-$13.05	-28.4%	-5.0%
Goodfellow Inc.	TSX:GDL	Dec. 14, 2011.	7.82	2.24	8.15	2.57	32.9	4.5
Goodfellow Inc.	TSX:GDL	Jan. 18, 2012.	7.81	2.24	8.15	2.58	33.0	5.0
Reitmans	TSX:RET.A	Jan. 23, 2014.	5.81	0.75	4.55	-0.51	-8.8	-2.4
Reitmans	TSX:RET.A	Sept. 5, 2014.	5.77	0.65	4.55	-0.57	-9.8	-3.2
Ensign Energy	TSX:ESI	Dec. 4, 2014.	10.01	1.44	6.32	-2.25	-22.5	-0.8
Reitmans	TSX:RET.A	Sept. 14, 2015.	4.86	0.45	4.55	0.14	2.9	1.3
Ensign Energy	TSX:ESI	Sept. 8, 2016.	7.99	0.60	6.72	-0.67	-8.4	-7.2
Goodfellow Inc.	TSX:GDL	Feb. 28, 2017.	8.51	0.00	8.15	-0.36	-4.2	-4.2 [1]
Accord Financial	TSX:ACD	April 11, 2017.	8.83	0.18	9.32	0.67	7.6	7.6 [1]
Average							-0.6%	-0.4%

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

All Open Positions - Risk / Reward

Exhibit 10 is the most important chart in this review. It is a little different from previous years where I included both open and closed positions. In an effort to be thorough by including closed positions with their open counterparts I was inadvertently double counting the most favourable

holdings and thus distorting the average and median calculations. That is just the opposite of my intention with these reviews, I want to make them as bad as possible so nobody will be unpleasantly surprised when the inevitable periods of losses or underperformance occur while waiting for positions to advance to their full potential (usually by 100%). The format of the chart will look familiar because it is similar to Exhibit 3 that showed the results for closed positions.



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. Just 12 of 34 open positions have black bars overlapping red bars signifying a loss position and the cumulative gains on other profitable positions dwarf those 12 open cumulative losses. Even more significant but not discernible from Exhibit 10 is that the median 165 week holding period of those 12 losing positions is less than half the 368 week median of closed positions (Exhibit 2). Apart from General Electric (476 weeks), Nokia (365 weeks) and the US Treasury 2 Year Bear ETN (339), they are still “incubating”.

If there ever was a real life example of letting one's winners ride it can be found in the median and average calculations of the losses and gains. As shown in Exhibit 10 the median worst loss of open positions was 30.1% and their median gain about the same at 33.0%. But that does not take into account the long tails of very profitable positions such as DowDupont with a 266.3% return, it just shows the returns of the stock in the middle position. The average calculation does and it shows about the same loss level of 32.4%, but the gain is double at 65.6%. A 2:1 return to risk ratio on open positions.

Rebalancing of Balanced ETF Portfolio

I don't know about you, but this is getting way too long so let's wrap it up here. As I repeat each year, 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.

Everyone's situation is going to be different for rebalancing. I have a lot of cash after having sold a number of USD denominated ETFs in anticipation of a 3-5% pull back so that I could re-invest the proceeds in their CAD hedged equivalents. That pullback has not materialized, so I am still waiting. But that is my situation. Assuming one was fully invested in the Balanced ETF portfolio one would be way over target allocation on equities, especially International and US Large Cap. Those should be sold down. As for REITs, US / International are under and Canadian over target by about the same dollar amount, so Canadian REITs could be sold with the proceeds used to buy US / International REITs.

Overall, the rebalancing will see a reduction in equities and an increase in fixed income, with at least half of that fixed income increase going into a 2 Year GIC ladder using the staggered phase-in method that we have covered over the past year.

Finally, if you do not hear from me again in 2017, thank you for the past year. Have a happy and peaceful holiday season.

Fred

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