Switzer Super Report

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A good year for sleeping

So there was a bit of data out of the US last week that caused a few jitters, but I'm not running scared yet - far from it. I actually think we might be at the beginning of quite a secular bull run and, as I keep telling you, any correction we do see will be brief, and should be used as an opportunity to buy.

To help you with those buying decisions, today in the *Switzer Super Report* we have our updated Income-Oriented Portfolio for 2014. Paul Rickard explains a couple of changes, and why we have down-weighted our allocations to the yield stocks, given their outperformance last year.

Also today, we have Gary Stone with charts on Invocare and why the company that deals in death, might be about to experience a bit of life, and in *Buy, Sell, Hold - what the brokers say*, the analysts had a busy start to the year, Oil Search and Qantas got upgrades, as Newcrest got a double downgrade.

Sincerely,

Peter

Peter Switzer

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Do I see a secular bull market looming?

by Peter Switzer

A lot of friends and family think I have a great job – TV, radio, newspapers, speeches, newsletters, webinars, etc. – and often I come up with the smart Alec reply that "It's a tough job, but someone has to do it!" Of course, it's not a job, it's a business – The Switzer Group is a business that employs around 40 Aussies nowadays but I have great people, which makes the business work.

However, one tough job I do have to do with Paul Rickard and others in our team is set the course for the investments of our financial planning clients, our subscribers to this newsletter and for those who follow my views in the media.

This is a tough job and I have to help do it.

The year ahead

By now you'd know that I am bullish again on stocks, and have nominated the 6000-mark as the level that the S&P/ASX 200 index should get to over the course of 2014. I'm not saying it ends there – it could be higher or lower – but I think at some time we will see the numeral six on the index.

My argument is primarily economics based, with global economies heading in the right direction, and with a lower dollar, as well as interest rates, likely to help local stocks keep on tracking up. Sure, there are some curve balls out there, with the big one likely to be China, but stock markets always have highs and lows to deal with.

When you think about it, the stock market is like one never-ending preoccupation with football, which a lot of males are afflicted by. You have a good run with your team winning, you might even win the premiership or the flag, but then you are back in the pack. However, because you're addicted you keep turning up hoping for a big win.

But unlike footy, if you play your investing game right, you can win seven out of 10 years, and if your portfolio is well-balanced, you can average around 10% per annum, including dividends, over a decade.

Market conditions

Now all these numbers are "averages", which can hide the fact that sometimes a bull market can last a really long time, or a surprisingly short time. I don't usually preoccupy myself with bull or bear markets, and whether they are cyclical or secular – I usually make an annual assessment of whether or not I want to be in or out of the market. But that doesn't mean I ignore analysis of whether we are in or out of a secular bull market, which, of course, is the best market of all for long-only players.

Last week on my Switzer program, which my son Marty hosted, Gary Stone of Share Wealth Systems told him that he thinks we are in a secular bull market. When Marty asked him to explain "secular" to the viewers he simply said: "long-term."

So Stone, who only a year ago was trying to work out whether the secular bear market was over, is now in the secular bull market camp. This gives me confidence that my one-year call to be in stocks is not a big call and that makes sleep easier.

But what are others saying?

Nouriel Roubini or Dr Doom, who called the GFC crash accurately, now thinks the USA will have a good 2014 with equities, and that also helps my sleeping pattern.

"The advanced economies, benefiting from a half-decade of painful private-sector deleveraging, a smaller fiscal drag, and maintenance of accommodative monetary policies, will grow at an annual pace closer to 1.9%," he said in an opinion piece on the *Project Syndicate* website on Tuesday.

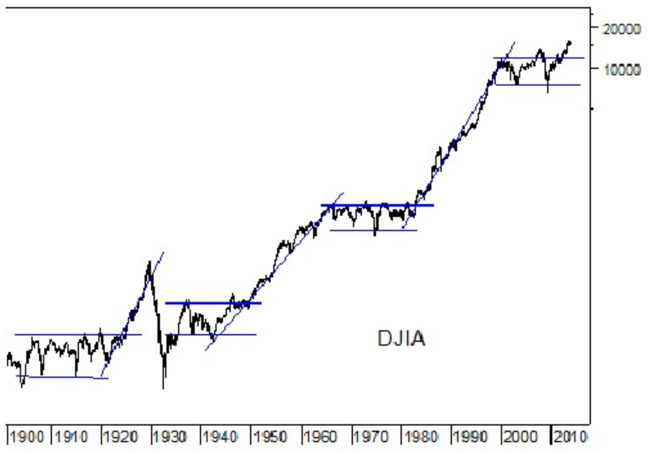
He likes the US positives of the shale-energy finds, better labour and housing markets and manufacturing coming back to America. These are good foundations for the burgeoning economic recovery and stocks. He is also bullish on emerging economies, which is good for commodities, if he is right.

The secular story

All of this is good for my one-year view but what about the secular story.

Between 1982 and 1999 it was largely seen as a secular bull market, despite the 1987 Crash, which was a part of a cyclical bear market. In 1999, just before the Dotcom Crash, Warren Buffett warned that the next 17 years would be more like 1966-82, which was a secular bear market. So, if he is right and secular markets stick to a 17-year time slot, then we could be in a cyclical bull market within a secular bear market that goes to 2017!

The chart below makes interesting reading, and shows how steep rides up in a secular bull market are followed by a sideways period called a secular bear market.



Source: Forbes.com

Writing for the *Financial Sense* website, John Maudline also tackled the question about whether we are in a secular bull market yet.

He thinks we are still in a secular bear market and so the rally since 2009 is a cyclical bull market.

If it is a secular bull market, we need to see profit margins hit all-time highs, and so the US reporting season will be important to watch over the next three weeks.
Next, the global economy will have to show better than expected growth, and it will have to look sustainable. In reality, the global economy is looking stronger, but the sustainability question will be a big watch for me this year, along with China.

Finally, secular bull markets start at low P/Es and we are now at high P/Es. However, you could argue that the secular bull market started a few years ago and Maudlin and his ilk just missed it!

I can't see any reason why secular bear and bull markets must adhere to rigid timeframes, and when central banks go for something outside the square, such as QE3-like policies in the USA, Japan and Europe, you could end up with longer or shorter secular markets.

I don't know if we are in a secular bull market but I will keep testing it and sharing my views with you. That said, I feel 2014 will be a good year for sleeping, whether we are in a secular bull or bear market.

Our high-income stock portfolio for 2014

by Paul Rickard

We have made some changes to our high-income stock portfolio for 2013. These include sector and stock rebalancing, base lining for the start of the year, and the replacement of Coca Cola Amatil, Rio Tinto and UGL with Dexus, Leighton Holdings and Orora.

Importantly, we have marginally reduced our overall exposure to the "yield" based sectors (through stocks such as the major banks and Telstra) and marginally increased our exposure to some of the cyclical industries that may benefit from a recovering economy.

With the S&P/ASX200 increasing by 15.1% in 2013, and company earnings (particularly for banks and Telstra) growing at a much lower rate, forecast dividend yields have fallen. Our income-biased portfolio is forecast to generate a yield of **5.01% pa** in 2014, franked to 90.4%.

Construction rules

The construction rules we applied are:

- We used a 'top-down approach' looking at the industry sectors, and introduced biases that favour lower PE, higher yielding sectors;
- So that we are not overly exposed to a market move, we have determined that in the major sectors (financials, materials and consumer staples), our sector biases will not be more than 33% away from index. For example, the 'materials' sector weighting on the S&P/ASX 200 is 17.8%, and under this rule, our possible weighting is in the range from 11.9% to 23.7% (i.e. plus or minus one third or 5.9%);
- While property trusts have limited tax advantages to an SMSF, the sector has underperformed and is now looking reasonable value – so we have included an exposure in the portfolio. Consumer discretionary, which was the best performing sector in 2013, is in the main low yielding, and as a very diverse sector, is extremely difficult to replicate without introducing massive single stock risk. Accordingly, we have taken a little more exposure to the "cyclicals" through the selection of stocks from the industrial sector. Our portfolio is thus overweight financials, consumer staples, utilities and telecommunications; underweight materials and consumer discretionary; and broadly index-weight the other sectors

With these sector allocations, we would expect this portfolio to moderately underperform relative to the benchmark price index in a strong bull market, and moderately outperform in a bear market.

On a sector basis, our portfolio compares as follows:

Sector	ASX 200 Weight*	Portfolio Weight	Difference
Consumer Discretionary	4.7%	0.0%	-4.7%
Consumer Staples	8.2%	10.0%	1.8%
Energy	5.9%	6.0%	0.1%
Financials	37.5%	43.0%	5.5%
Health Care	4.7%	3.0%	-1.7%
Industrials	6.5%	9.0%	2.5%
IT	0.8%	0.0%	-0.8%
Materials	17.8%	13.0%	-4.8%
Property Trusts	7.0%	5.0%	-2.0%
Telecommunications	5.3%	7.0%	1.7%
Utilities	1.6%	4.0%	2.4%

** ASX 200 index weights as at 31 December, 2013*

Stock rules

The stock rules are:

- We require 15 to 20 stocks (less than 10 is insufficient diversification, over 25 it is too hard to monitor), and have set a minimum stock investment of $3,000;

- We confined our stock universe to the ASX 100;
- We avoided stocks from industries where there is a high level of exogenous risk, such as airlines or general insurance;
- Within a sector, the stocks are broadly weighted to their respective index weight. That said, we have applied some biases – in the financials sector, for example, we favour the Sydney Head Office banks CBA and Westpac over ANZ, and to a lesser extent NAB; and
- Of course, we looked for companies that pay (where possible) franked dividends and have a consistent earnings record.

Portfolio

Our income-biased portfolio per $100,000 invested (using prices as at the close of business on 31 December 2013) is listed below.

Forecast returns

Using consensus analyst forecasts from FN Arena, the portfolio has the following characteristics:

- Forecast PE for 2014: 14.73
- Forecast dividend yield for 2014: 5.01% pa
- Franking: 90.41%

For an SMSF in the accumulation phase, the 5.01% dividend yield will translate to a return of 5.98% pa (after tax), and for a fund in pension phase, the income return will increase to 6.95% pa.

In a bull market, we expect that the income-biased portfolio will underperform relative to the standard S&P/ASX200 price index due to the underweight position in the more oriented "growth" sectors, and conversely in a bear market, it should moderately outperform.

We will keep a close eye on the portfolio, and report back in coming editions of the *Switzer Super Report*.

Important: *This content has been prepared without taking account of the objectives, financial situation or needs of any particular individual. It does not constitute formal advice. Consider the appropriateness of the information in regards to your circumstances.*

Sector	Stock	Price 31/12	Value	PE (F)	Div (F)	Franking
Consumer Staples	Wesfarmers	$44.04	$5,000	20.8	4.41%	100%
	Woolworths	$33.85	$5,000	17.2	4.13%	100%
Energy	Woodside	$38.90	$3,000	13.7	6.52%	100%
	Origin	$14.07	$3,000	20.6	3.55%	100%
Financials	ANZ	$25.05	$7,000	13.1	5.32%	100%
	CBA	$77.80	$14,000	15.6	4.95%	100%
	NAB	$34.83	$10,000	12.9	5.83%	100%
	Westpac	$32.38	$12,000	14	5.89%	100%
Health Care	Primary	$4.95	$3,000	16	3.92%	100%
Industrials	Brambles	$9.15	$3,000	18.6	3.34%	30%
	Leighton	$16.11	$3,000	10.1	6.14%	50%
	Toll Holdings	$5.68	$3,000	13.9	4.91%	100%
Materials	BHP	$37.99	$10,000	12.7	3.65%	100%
	Orora	$1.16	$3,000	13	4.91%	67%
REIT	Dexus	$1.01	$5,000	12.6	6.07%	0%
Telecommunications	Telstra	$5.25	$7,000	16	5.52%	100%
Utilities	AGL Energy	$15.03	$4,000	14.1	4.32%	100%
			$100,000	14.73	5.01%	90.41%

Charts promise life for Invocare

by Gary Stone

Invocare is a consumer discretionary sector business that owns and operates funeral homes, cemeteries and crematoria. It has continuously traded on a high PE Ratio of between 18 and 31 over its 10 years of being listed on the ASX. Its PE Ratio is currently 26.9. It has continued to increase its dividend year after year and its earnings per share every year bar one, making it a great long-term prospect for a buy and hold portfolio.

But it's the chart that looks interesting at the moment.

A dull run

After a run-up from $8.52, starting in January 2013, to a high close in May 2013 of $12.15, Invocare's share price (IVC) has taken an eight-month breather and closed on Friday at $11.22.

Source: Beyond Charts

The near 50% increase in the Invocare share price to May 2013 then had a 61.8% Fibonacci retracement to around the $10.10 zone, which is shown on the chart with the blue horizontal rectangle. This zone has formed a strong support zone, which can be used as a stop loss area for a long-term position in Invocare.

Since May last year, the Invocare share price has been making lower highs as shown by the declining black trend line. The blue horizontal support zone and this descending black trend line, form a descending triangle, which is typically a bearish pattern.

A bright spot

However, Invocare may have enough going for it to resist the force of the bearish pattern. This includes its sound fundamentals, the 61.8% Fibonacci retracement support zone, primary bull market conditions that exist for equities at the moment and last, but not least, the breakout above the black descending triangle that occurred on Christmas Eve.

Following the Christmas Eve breakout, a 10-day period of indecision followed, where Invocare traded between $11.00 and $11.20, with this range finally broken on Friday 10th January, when another small breakout occurred, and it closed at $11.22.

Whether the pull of the bearish pattern turns this into a false breakout, or the strengths that Invocare has going for it take its price higher, will be known in the next two to three weeks. To confirm the breakout and continue rising, the share price must rise above $11.50. To confirm the false breakout, the share price must fall back into the range demarcated by the descending triangle.

If a position is taken at these price levels, a stop loss should be set just below $10.00 to protect a large move to the downside. However, the upside might be quite large, given Invocare's price growth over the last 10 years and the current equities primary bull market conditions.

Gary Stone is the founder and Managing Director of [Share Wealth Systems](#).

Buy, Sell, Hold – what the brokers say

by Rudi Filapek-Vandyck

Local stockbrokers were surprisingly busy in the first full week of January, upgrading and downgrading individual ASX-listed stocks in what is usually a slow week.

Amidst an overall flat-lining profile for commodities in general, with the optimists anticipating better times later in the year, the overall view remains that iron ore is destined for lower prices as the year unfolds, yet nobody is projecting mayhem in 2014. A growing number of analysts are succumbing to the view that the outlook for crude oil prices is for weakness, not strength this year.

In the good books

Oil Search (OSH) was upgraded to Neutral from Sell by Citi. Citi has rolled forward its oil and gas sector valuations and adjusted for lower 2014-15 Brent crude forecasts (ca 10%) and an offsetting lower Aussie dollar. The result is a target price increase for Oil Search to $8.42 from $8.22 and thus an upgrade to Neutral.

Atlas Iron (AGO) was upgraded to Outperform from Neutral by Credit Suisse. Credit Suisse has slightly increased its iron ore price forecasts over the next two years. While mild, the flow-through impact on Atlas earnings forecasts is still significant.
Credit Suisse also upgraded Mt Gibson Iron (MGX) upgraded to Neutral from Underperform for the same reason.

David Jones (DJS) was upgraded to Neutral from Underperform by BA-Merrill Lynch. The broker has tempered its negative view on David Jones' sales in the period ahead. The result is a lift in earnings forecasts and a target price increase to $2.90 from $2.50.

Upgrades

Order	Company	Old Rating	New Rating	Broker
1	Atlas Iron	Neutral	Buy	Credit Suisse
2	Beadell Resource	Neutral	Buy	Citi
3	David Jones	Sell	Neutral	BA-Merrill Lynch
4	Mount Gibson Iron	Sell	Neutral	Credit Suisse
5	Oil Search	Sell	Neutral	Citi
6	Qantas Airways	Sell	Neutral	Credit Suisse
7	Regis Resources	Sell	Neutral	Credit Suisse
8	Sirtex Medical	Neutral	Buy	UBS

Sirtex Medical (SRX) was upgraded to Buy from Neutral by UBS. The broker was positively surprised by dose sales well ahead of forecast for Sirtex in the second quarter. UBS is not assuming such growth ad infinitum, but it's enough to see a target price increase to $15.00 from $12.60 and an upgrade to Buy.

Qantas (QAN) was upgraded to Neutral from Underperform by Credit Suisse. The broker believes airline market dynamics appear to have stabilised somewhat and expects Qantas' upcoming strategy day to provide some positives. On the basis of share price weakness, the broker has upgraded.

In the not-so-good books

Nib Holdings (NHF) was downgraded to Sell from Neutral by Citi as the broker believes the market is pricing in overly ambitious growth expectations for Nib. The company intends to increase its premiums by 10% by FY15 and expects modest policyholder growth, and Citi expects customers will be more difficult to attract at the price.

Downgrades				
Order	Company	Old Rating	New Rating	Broker
9	Cardno	Buy	Neutral	JP Morgan
10	Henderson Group	Buy	Neutral	Credit Suisse
11	Newcrest Mining	Buy	Sell	Credit Suisse
12	NIB Holdings	Neutral	Sell	Citi

Cardno (CDD) was downgraded to Neutral from Overweight by JP Morgan. The incumbent CEO has announced his retirement and JP Morgan sees market caution until the new, unknown CEO establishes himself.

Newcrest Mining (NCM) was downgraded to Underperform from Outperform by Credit Suisse. While the broker expects a weaker AUD from here, it is also forecasting a gold price below US$1000 by late 2014. The impact is a drop in Newcrest's target price to $8.20 from $8.75 and a double-downgrade straight to Underperform.

Earnings Forecast in cents per share

Positive Change Covered by > 2 Brokers						
Order	Code	Company	Previous EF	New EF	Change	Recs
1	BDR	Beadell Resources	60.00%	80.00%	20.00%	5
2	SYD	Sydney Airport Holdings	17.00%	33.00%	16.00%	6
3	PNA	Panaust	57.00%	71.00%	14.00%	7
4	OSH	Oil Search	43.00%	57.00%	14.00%	7
5	DJS	David Jones	-38.00%	-25.00%	13.00%	8
6	AGO	Atlas Iron	-25.00%	-13.00%	12.00%	8
Negative Change Covered by > 2 Brokers						
1	NCM	Newcrest Mining	-13.00%	-38.00%	-25.00%	8
2	HGG	Henderson Group	50.00%	25.00%	-25.00%	4
3	CDD	Cardno	40.00%	20.00%	-20.00%	5
4	PRY	Primary Health Care	14.00%	13.00%	-1.00%	8

The FNArena database tabulates the views of eight major Australian and international stock brokers: BA-Merrill Lynch, CIMB, Citi, Credit Suisse, Deutsche Bank, JP Morgan, Macquarie and UBS.

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Did you know?

January is typically a slow month for auctions and property sales, so we don't have any auction clearance data for the first few weeks of the year. But what we do have is the Housing Industry Association's data on new home sales for November, which were up by 7.5% to their highest level in two and a half years. Importantly, the graph below shows that over the past year or so, while the increases have been rapid, we are coming off a 15-year low and are now just at the five-year average. Hardly cause for bubble concern, just yet.