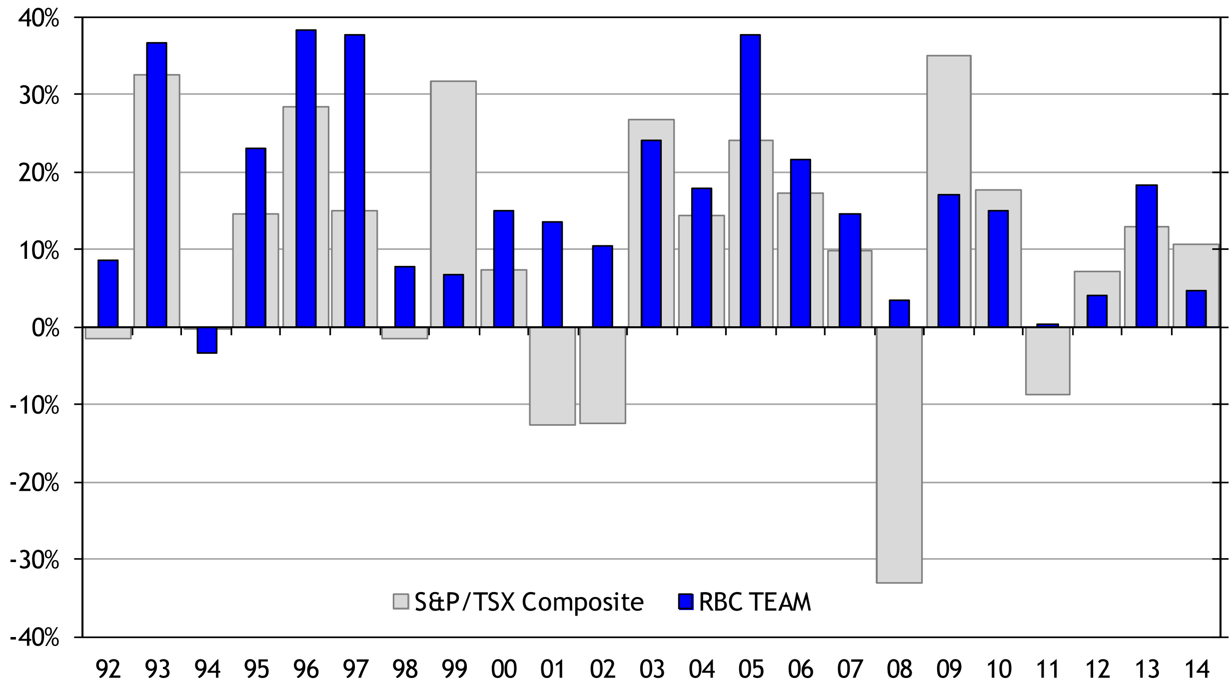
December 21st 2015

"Won2One" with Nick Foglietta

Tactical Equity Income Model Portfolio Record



Tactical Equity Income Model Present Conditions:

TEAM Model Asset Allocation: **0%** Equities/ 10**0%** Fixed Income
S&P/TSX 60 Closing Value: 13,024
TSX 200 Day Moving Ave: 14,264
% Above/Below 200 Day Moving Ave: **8.70% Below**
Levels for change: 100% stocks - **TSX 14,977** and 100% fixed income – **TSX 13,550**

Weekly Quote

Nobody knows what the future holds, and it's bad enough just getting old,

Live my life in self-defense, you know I love the past, 'cause I hate suspense…

If "Diane Young" won't change your mind….right on time!

Song: Diane Young Artist: Vampire Weekend - the lyrics just struck a chord with me.

Review of Nick's 2015 Forecast

It's the most "humbling" time of the year….!

This week I review and critique my 2015 forecast published Jan 5th 2015. It is still listed on my website and you may want to browse through it before you read today's editorial.

Back on January 5th I started off with a bold statement:

"Standing up to be counted" or "choosing to go right when everybody else is going left"…I believe investors are going to be called to make this type of decision in 2015.

*Investors will have to make a serious decision…**are you a "buy and hold" investor, or are you a "tactical" investor.***

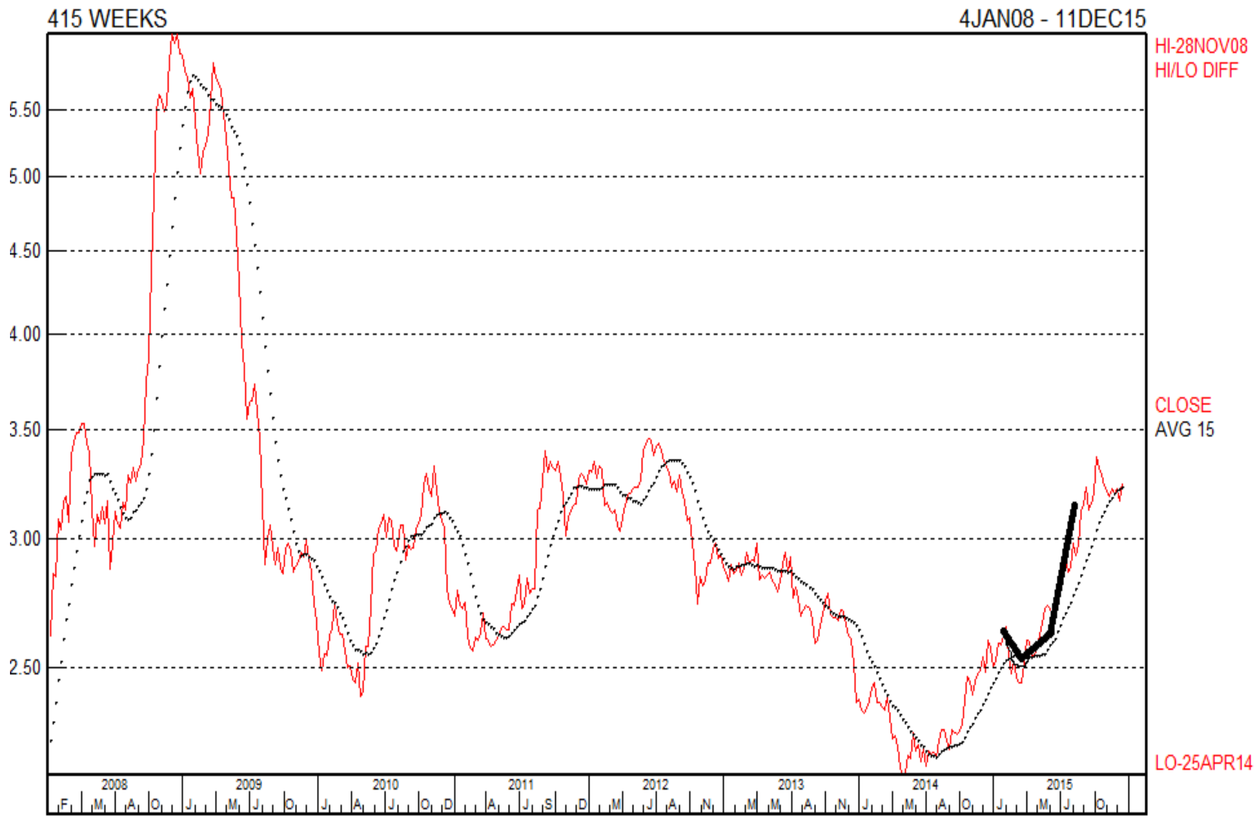
For Canadian investors, the statement above was mostly true. The TSX closed December 31st 2014 at 14,632. As of Friday, Dec 18th, 2015 it closed at 13,024 or **11.00% below the start of the year**. I would argue this was enough of an index loss to make a "tactical approach" worth the time and effort.

But the index loss is really just the start of what happened in 2015. And even though, I got the US Fed's interest rate hike cycle completely wrong, the 2015 forecast was not too bad in the big picture.

Let's take a more careful look at what happened as expected and what did not even come close to happening as forecast!

The first prediction in the 2015 report was that **low quality corporate bonds would underperform high quality issues in 2015**. This was the best call of the year. The analysis this call was based upon was the gradual weakening of the global economy in 2015. As the economy slowed and the huge and growing pile of low quality debt that had fueled the prior couple of years' growth sensed that there might be a future game of "financial musical chairs" to be played, my thought was that **government yields would go down a little bit and that low quality bonds would rise in yield**.

The chart below shows Moody's Corp Bond Index-BAA. The thin, red line is what actually happened. The fat, black line is from my forecast for 2015.



The two lines overlap quite nicely.

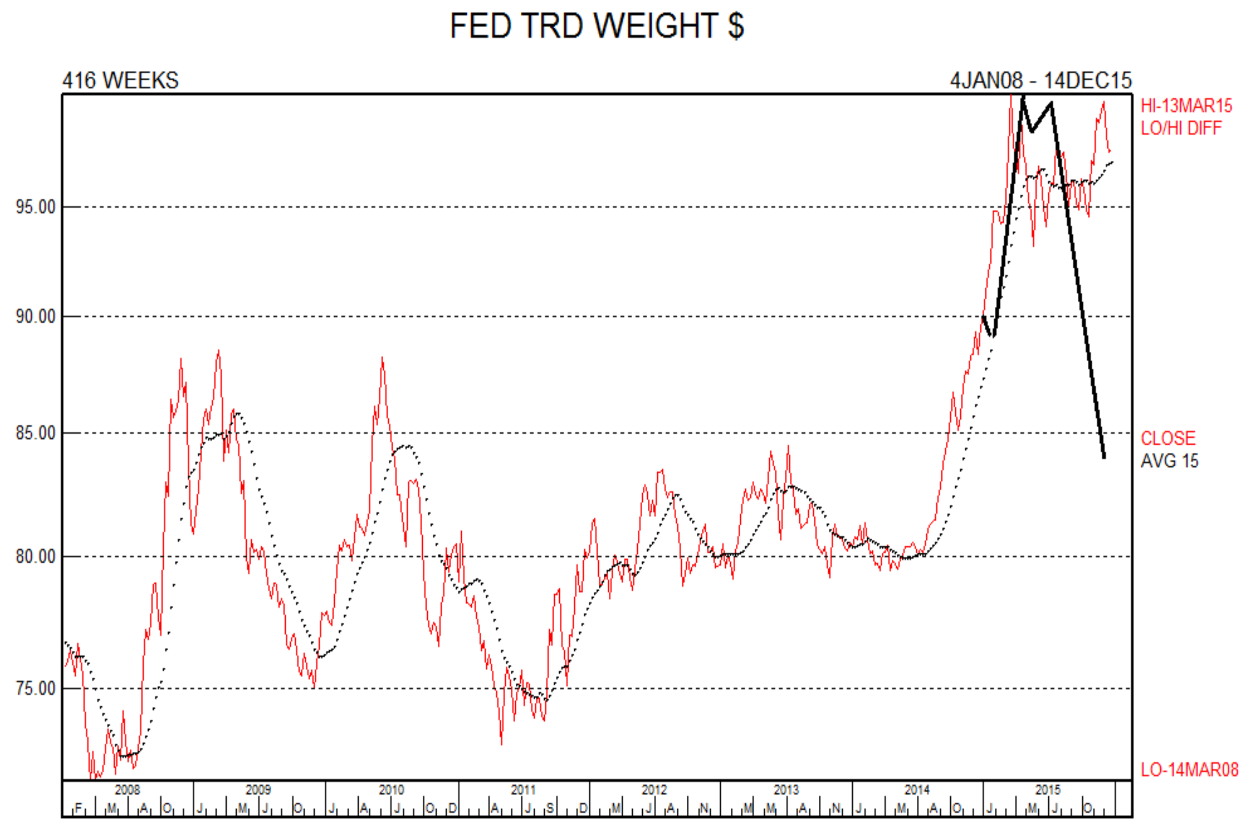
I would expect more of the same pattern to extend into 2016. The challenges that formed this opinion a year ago have grown…not shrunk.

The second prediction for 2015 looked at **the sharply rising US dollar index**. The forecast was looking for two FED funds rate increases in March 2015 and again in June 2015 reaching a rate of 0.50%. At that point, I felt the FED would back off making any more increases to the FED funds rate and the US dollar would begin to retreat.

Obviously, my prediction (which was really only a reiteration of what the FED said it was planning to do in the first six months of 2015) did not come close to reality. It took all the way to December 16th 2015 to get the first 0.25% interest rate increase!

Before I show the actual and predicted chart from the 2015 report, I want to clarify an interesting outcome in the currency markets. **Even without raising interest rates the US dollar was the strongest currency on earth.** Ironically, it was the constant **threat** of raising interest rates that kept the US dollar on solid footing.

Therefore, it will be interesting to see how the US dollar trades going forward now that the interest rate increase has actually occurred and the potential trouble it may cause.



The first six months of the forecast was right for all the wrong reasons. I stated that the decline in the US dollar would begin when the FED "blinked" on continuing to raise interest rates in 2015…heck, they never even got started to have a chance to blink!

But interestingly enough my greatest concern written below for the 2015 forecast is actually more valid now than then:

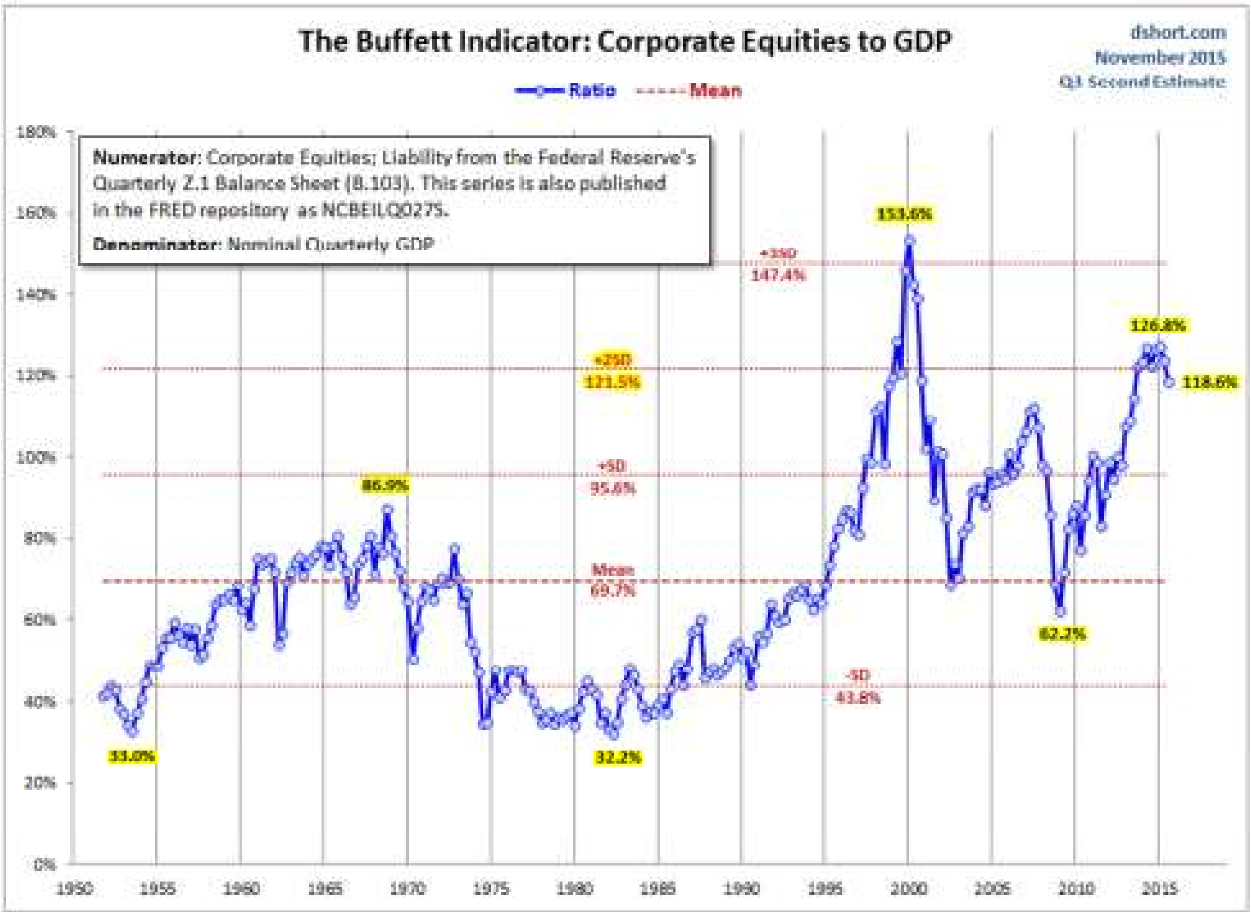
"My greatest concern for 2015 comes later in the year as the ***markets digest the inability of the FED to raise interest rates any further.*** *There is a huge difference in perception when the FED is "managing" the interest rates and when "interest rates are managing the FED."*

What makes this more difficult in 2016 is that, at least, I was giving the FED 0.50% to play with and be able to cut again. Hey, if the US is already entering a recession (as discussed last week) the FED will have no scope to cut rates without heading to a negative interest rate policy decision.

It would not surprise me if 2016 was the year that the US dollar reversed and came down…maybe even a lot! This is not a consensus call. I will discuss this more in my 2016 forecast.

The third section of the 2015 forecast looked at **stock markets**. In the US, the stock market is sitting nearly 2% below where it started the year. In Canada, stocks are down about 11.00%.

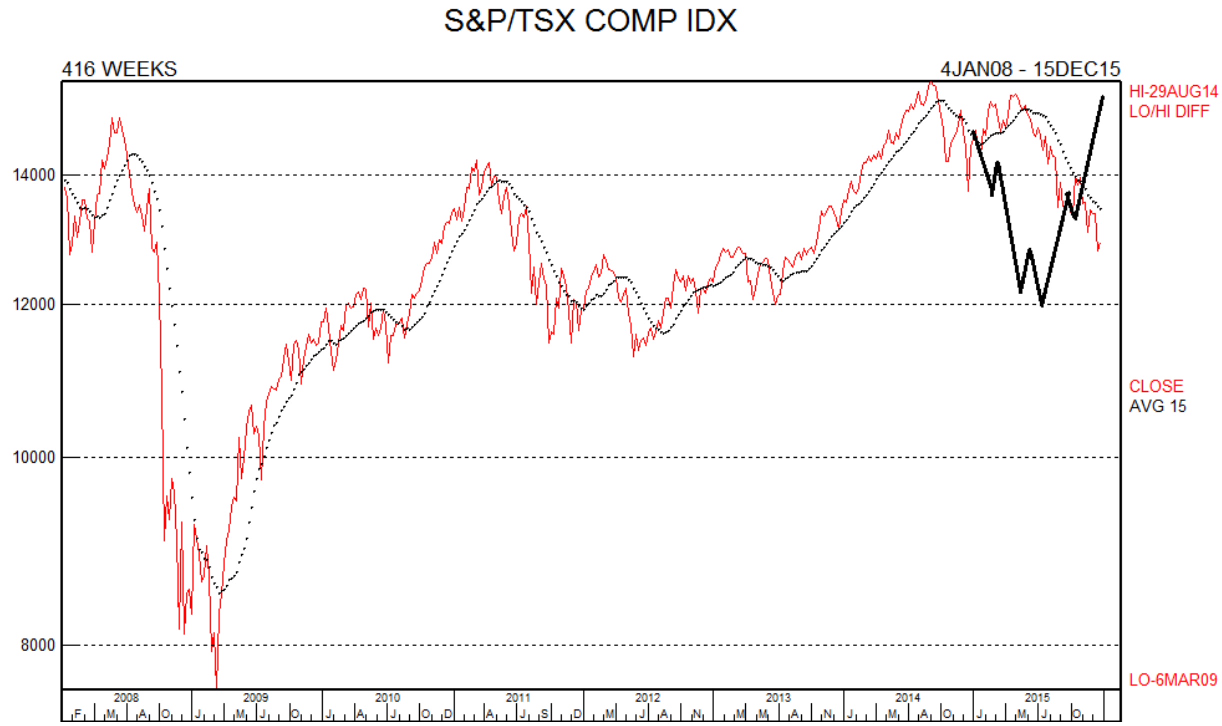
In the 2015 forecast I used Warren Buffett's favourite indicator of stock market valuation. It showed the S&P500 to be at the second most expensive level in history at that time at 123.4% market capitalization to GDP ratio. The chart below is the updated version of the same chart.



One could make the case the correlation above has already topped out for the cycle. Looks a bit early to call…we will see.

When I look at the Canadian stock market situation my forecast is almost exactly six months out of sync. When the US Fed failed to raise interest rates early in 2015 it played havoc with the timing of what I anticipated to be early weakness in Canadian stocks and then, the subsequent recovery once it was clear the US Fed could not raise interest rates too far.

The chart below shows what the actual TSX did in 2015 with the red line and the black line was my forecast from last January.



As stated at the end of the stock market section of the 2015 forecast, "*It should pay to follow the TEAM Model allocation".* The timing of when to pay attention was not even close to right but the wonderful thing about TEAM is that it requires no "crystal ball" to tell the future…it requires us to follow the strategy.

The final sections of the 2015 forecast looked at geopolitics, a China/Japan crash, Eurozone challenges, and Gold and Oil prices. Each of these short comments contained some good calls and some bad calls. You are welcome to go back and read them for yourself in the 2015 forecast.

In summary, the 2015 forecast gets a C+ rating in my books. If the Fed had stuck closer to its 2015 year end forecast, maybe I would have earned a better grade?

I will publish the 2016 forecast in early January.

About the author: Nick Foglietta is a Vice President, Investment Advisor at RBC Wealth Management in Nanaimo, B.C., Canada. He has been managing money since 1988.