



Numbers: "Lies, damn lies and statistics." - M. Twain
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- **Charts:** when in doubt as to where the market is going, some like to look at the "charts" which track the performance of individual stocks or indexes: this is called **'technical analysis'**. The chart for the **TSX Composite** for the last month shows a market that surged nearly 10% in two weeks and since then has traded in a wide range of 9,800 and 10,200 points. In technical terms, the market seems to have established upper and lower resistance levels. The overall direction of the market is up so one can reasonably expect that over time, in the absence of bad news, the trading range will narrow until some good news pushes the market forward past the old mark. When this might happen is not clear.

- **The Golden Cross:** this is a little esoteric but interesting. Technical traders who rely on charts will compare the short-term moving average price of a stock or an index with its long-term moving average price. A so-called golden crossover occurs when the short-term moving average price curve (such as the 15-day) for a security or an index crosses the long term moving average price curve (such as the 50-day) breaking above the long-term moving average or resistance level. When this happens to a major index, the **Golden Cross** supposedly indicates that a bull market is on the horizon and is reinforced by high trading volumes. Using a longer horizon with more popular indicators, Friday's **S&P 500** closed at 887 comfortably above the 50 day moving average of 850 and approaching the 200 day moving average of 925. The **Golden Cross** may be a bit of self-fulfilling technical voodoo, but that matters little if it prompts a feverish round of buying.

- **Quantitative (or 'quant') analysis:** there are many other methodologies for making investment decisions. A popular approach is to look at ratios, the best known being the **price/earnings** ratios. **George Vasic**, strategist at **UBS Securities Canada Inc.** estimates that the **TSX Composite** is trading at 13.5X estimated *forward earnings* (investors are buying shares at a price of 13.5 times each dollar in estimated future earnings). The average P/E from 2004 to mid-2008 was 14.5X forward average earnings and on that basis Canadian stocks may be a buy *if* a recovery occurs in the second half of 2009. Other analysts look at *actual* P/E ratios and stocks on both sides of the border on this basis have been cheap or fairly priced. **Robert Shiller**, the **Yale University** economist, has analyzed **S&P 500** earnings on an inflation adjusted basis and finds that the current multiple of 15.6X is in line with the 127-year average, suggesting US stocks are fairly valued. P/E ratio analysis is problematic however because of insufficient focus on the tangible value of the business, especially in times when companies are losing money. Analysts therefore recommend other ratios such as **price/ cash flow, price/ book value, or enterprise/ operating cash flow** (confused yet?). On a price to book value basis, using the past 30 years as a guide, at 449 points the **S&P 500** is attractive at 2X book value compared with the long term price/book value ratio of 2.4X. The Canadian market looks better with a price to book value ratio of only 1.6X for the **TSX 60**. Ratios are popular because they can be transparent and quick to calculate: sometimes they are neither and can have poor predictive qualities to boot.

- **Economic indicators:** The ever-helpful **Globe and Mail** identified in this Saturday's issue 6 key economic indicators -- jobs, housing, income, consumers, business conditions and finance. In spite of the paper's best efforts, the results are confusing and illustrate the challenge with economic indicators: based on the Globe's analysis 2 indicators are up, 3 are down and one is unknown and the link to stock market valuations is not abundantly clear. Not only that, but experience shows that such indicators are inaccurate in the short term (revisions are common); not all measures are equally important; and, their importance varies. In bad times, investors are overwhelmed with information and there is, out of necessity, a tendency to select information (and ignore contradictions) that confirms a previously held view. This can cause investors and analysts to become overly confident in their conclusions.

- **Numbers are confusing:** **Mark Twain's** statement refers to the seductive power of numbers. Analysts themselves also warn that market analysis is a tricky art that often depends on interrelated and hard to discern variables and in volatile times their predictive quality may be severely reduced. In our view, to guard against both factors, investors are best served by holding the bulk of their capital market assets in a well-balanced well-diversified portfolio of quality instruments that is rebalanced semi-annually. What should matter currently to most investors is to maximize yield (for short term protection and long term return) and a view that markets are behaving in an efficient and normal manner in which the laws of averages operate. A moderate view of domestic and global economic and inflation trends should inform the asset allocation process, but only in a modest fashion.

- **CCR --- Consumer confidence revival:** Bearing in mind the foregone discussion and provisos, according to **Stéfane Marion**, the **National Bank's** (NBF) Chief Economist and Strategist, based on May data from the **Conference Board of Canada**, the index of Canadian consumer confidence jumped from 75.2 to 88.5. The 13-point jump in confidence is the biggest monthly increase on record and equivalent to a four-standard deviation move. This boost in consumer confidence is consistent with the coming economic recovery expected by NBF in the second half of 2009. NBF recommends that investors have overweight exposure to the Canadian consumer discretionary sector.

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