2017 Investment Plans

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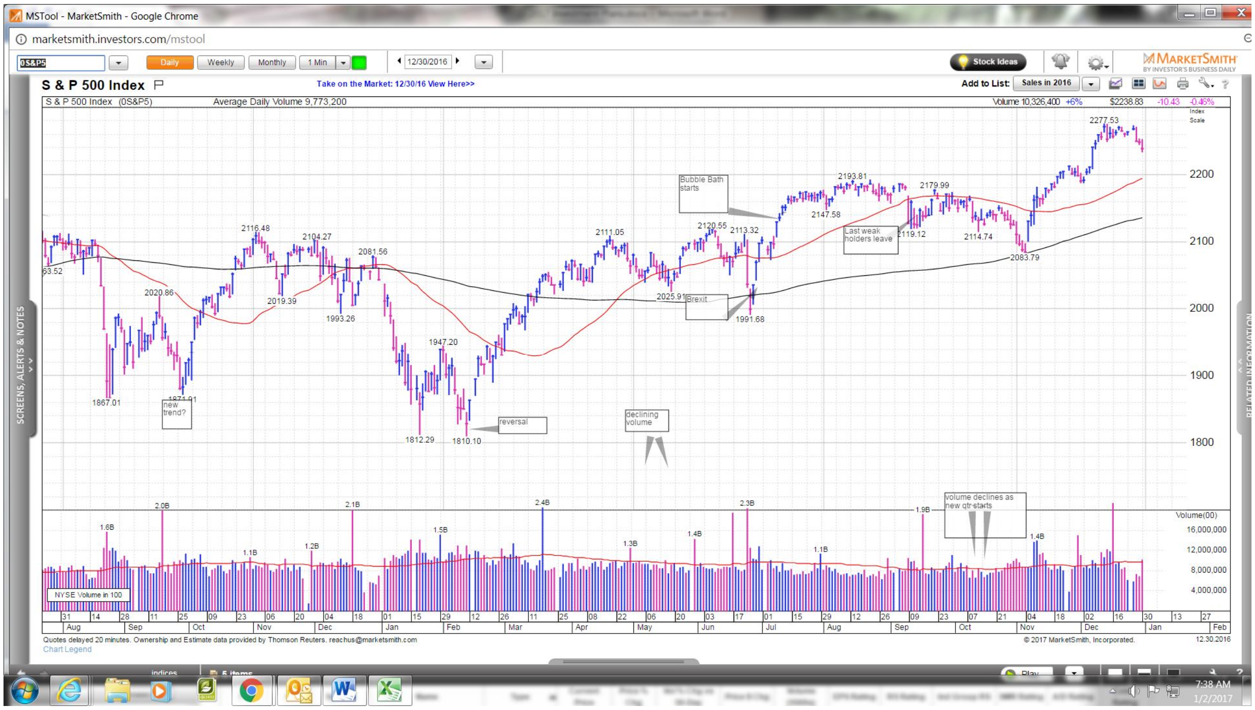
Sometimes investing is easy, and I think 2017 will be one of those years. I think at least one of the major averages will be up at least 20%. Sit back and enjoy the ride.

If you had just bought the ETFs for the major indices (DIA, SPY, and QQQ) last year, you probably would have beaten most of the pros. Including dividends, the Dow gained 15.7%, the S&P 500 gained 11.5%, and the NASDAQ gained 8.6%. You will probably have a good chance to do better this year.

Like the past few years, investors were cautious and full of complaints as the market went up. All the elements were in place for a big rally. Low interest rates, improving domestic economic data, improving earnings, cash on the sidelines, foreign money looking for better returns than the negative rates at home, and pent up demand. Everything was in place for a big rally except investor confidence. Then something good happened. Trump's election released the animal spirits that had been repressed. Now, after a big surge, investors are almost embarrassed by their giddy behavior, even though it is justified.

As the chart of S&P 500 below shows, the market executed a classic double bottom pattern last year. The first bottom was on September 29, 2015 and the second bottom (a bit lower just as it should be) was on February 11, 2016. The big reversal on that day off a new low marked the beginning of the end of that double bottom correction.

You can see confidence start to return in the chart below. The psychology behind bull markets is based on how people act when they decide that things are actually better than they thought. They change their minds and want to invest based on optimism rather than fear. For example, the Brexit vote on June 28, 2016, was supposed to ruin the market and destroy commerce, but investors took it as unexpected good news. The same thing happened with Trump's surprise election. There was a huge downturn in market futures as the "experts" predicted Armageddon, but that reversed in only a few hours as investors decided that a business-oriented president might actually be good for business.



I think the optimism that used to characterize America has returned. Trump is a good salesman and a turn-around artist, and America needs both right now.

America is a turn-around opportunity and Trump knows how to turn around a good business that has been badly managed. We are like an old country club that has fallen on hard times. People are washing their dogs in the pool and parts of the golf course have been turned into a soccer field. The restaurant is not open on any predictable schedule and it only sells pre-packaged salads anyway. The staff has gotten control of the payroll system and now they all have big incomes and no responsibility. They act like they own it even though they are not even members. They elected a president who was more interested in being worshiped than in improving the property. Hardly anyone pays dues anymore and many of the wealthier members have left to join the new country club on the other side of town where they can still play golf.

Now, Trump has gotten control of the country club before they burned down the buildings. Things will change. Dues will be collected and they will be deposited in a local bank, not the one in Botswana that the staff had set up. The packs of stray dogs roaming freely will be rounded up. The restaurant menu will be published in English again. Graffiti will be painted over. The teenagers who show up at night to drive on the putting greens will be arrested. Some of them will be offered jobs if they promise to behave. The numerous larger than life size statutes that the former president erected of himself will be removed. The scores of employees who were paid to just stand there and admire the statues will be fired.

Below is a partial list of Trump's plans and goals. It does not take a lot of imagination to predict the investment opportunities from each one. Any one of these could make a good year; taken together, they could be great.

- Border control
- Lower taxes for both businesses and individuals
- Fewer regulations, especially in finance and energy
- Repatriation of the $2T of US corporate money currently held overseas for tax reasons
- Repeal of ObamaCare
- Government employees with business experience who are used to getting things done and being accountable.
- Energy independence
- His enthusiastic support for achievement, success and wealth will stimulate risk-taking activity
- One trillion dollars of infrastructure spending
- Decentralize and let the states make more decisions independently

During bull markets, valuation is less important than the flow of investment money. The investor who spends time looking for a "good deal" may be left on the sidelines or end up with some crummy, underperforming stocks. True, stocks can go up because they are undervalued, but they can also go up when they are fully valued because the economy has gotten better or the company has new products or new ways of competing. Stocks are not like poker chips that never change; they grow and expand with new ideas and products. Future demand is more important than current value.

Here are some sources of new money to fuel the rally.

- Cash that has been on the sidelines all along as people had no confidence
- Foreign investors looking for a better deal than they can get in their own country (higher rates, safer markets, better assets)
- $2T of corporate money currently forced overseas by our tax policies
- Money currently in bonds that will flow out as rates rise and bond values fall.

Here are a few specific ideas.

- Demand should be strong for "bond replacements" especially from the investors who are selling declining bonds but are used to income. One of my favorites is DVY, an ETF for dividend stocks that meet certain objective criteria for excellence. It had a total return of 20.9% in 2016. Another favorite is BDJ, a closed end fund of dividend stocks that mysteriously trades below its net asset value. It had a total return of 14% in 2016 and pays dividends monthly, a feature that income investor enjoy.
- Income investors seeking "bond replacements" should also be attracted to REITs. Foreign investors are often especially eager to find convenient ways to invest in American real

estate. I would stay away from REITs with retail properties because Amazon is in the process of killing that category, but I love hotel and apartment REITs. Hotels are a leading economic indicator; they can re-price their rooms every day and business travel should increase as the economy expands. Apartments are good when rates are rising because it is harder to qualify for home loans. HPT is one of my favorite hotel REITs; it had a total return of 27.8% last year. IRT is a good apartment REIT. It had a total return of 26.9% last year.

- Biotechs have been unfairly beaten up by fears of government price controls. It is always good to be in some biotechs before the big ASCO meeting in June because that is when new blockbuster discoveries are announced. MRK and BMY seem to be the leaders in immunotherapy research, probably the most promising new cancer idea in decades.
- There is probably no need to take the extra risks of investing in foreign stocks when foreigners are clamoring to invest in our assets.
- Everyone can see that an attempt at energy independence will stimulate the energy industry. The early cycle part of the industry is oil field equipment and services. You can buy XES which is an ETF for this sector.