ANALYTICS INVESTMENT ADVISORS, LLC

Conceptual Confluence

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This month's commentary juxtaposes Victor David Hanson's recent article "The Coming Post-Obama Renaissance (October 2, 2011) against a recently released book by Matthew McCall, with Foreword by Tobin Smith, *The Next Great Bull Market, How to pick Winning Stocks and Sectors in the New Global Economy*, (John Wiley & Sons, 2010).

A summary of Victor David Hanson's major conclusions follows:

1. The American Constitution is unique, providing a singular and stable form of government not present in Russia, China, the Islamic world and even the European Union;

2. Brilliant new technologies and entrepreneurialism have the potential to double our proven oil and gas reserves, which will result in savings of hundreds of billions of dollars of imported fuel, reduce energy prices worldwide, create millions of new jobs, while providing a window of opportunity for solar batteries and alternative energies to become more efficient and cost competitive;

3. A change in government will give impetus to a recovery that should have occurred two years ago releasing hoards of cash and a sense of psychological certainty in the business community, which will in turn stimulate hiring, increase disposable income, GDP and corporate profits;

4. The general rejection of President Obama's socialistic policies will result in greater tax revenues, tax simplification, tax reduction, greater tax compliance, less regulation, entitlement reform and budgetary discipline; and,

5. The return to fiscal sanity will again generate a sense of American exceptionalism, an appreciation of U.S. Global power, moral international citizenship and restored confidence. The American public always knew, but temporally forgot, that a country cannot print money and borrow endlessly, and that bureaucrats are less efficient than private enterprise. Having been slapped out of their collective trance, a sadder, but wiser, America will soon turn loose a renewed economic vigor not seen for decades.

The recent tepid recovery from the greatest recession since the last depression will result in what McCall calls the "Great Restructuring", in that the investment world is now totally different than it has ever been. The "Next Great Bull Market", as he calls it, is going to: 1) be initiated by industries and companies that are able to best feed, clothe, entertain, employ and provide modern health care to the "Great New World Middle Class"; and, 2) provide unique ways for exchange traded funds (ETFs) to take advantage of the benefits of alternative, global and niche markets.

An exchange-traded fund is a hybrid between a stock and mutual fund, offering the best characteristics of each; namely, instant diversification, tax efficiency, intraday trading, low expense ratios, low fees, passive investments, transparency, leverage and short selling, convenience, exposure to alternative and niche sectors, and sound risk management through the judicious use of stop orders. It is constructed to replicate a particular market index; i.e. the ETF for the S&P500 is SPY, and the ETF for the Nasdaq 100 is QQQ. The following sectors, industries and themes, as described by McCall, are most likely to lead this offensive.

1. *Water* is becoming a scarce commodity as millions of people around the world do not have regular access to clean water. It is not only the undeveloped areas of the world where water is in short supply. Former prime minister of Australia, John Howard, announced in 2006 that his country was suffering from the worst drought in 100 years. While there is no true water utility ETF available in the United States that concentrates on the Dow Jones U.S. Water Index, PowerShares Water Resource ETF (AMEX:PHO) provides some exposure to large-cap utilities in that the five top holdings are Tetra Tech(TTEK), Danaher Corp (DHR), USR (URS), Itron (ITRI) and Valmont Industries (VMMI).

2. *Infrastructure Build-Out* is required in both the United States emerging markets where continued growth is predicated on efficiency and swift transportation. In this category there are four ETFs from which to choose: SPDR FTSE 100 ETF (GII); iShares S&P Global Infrastructure Index (IGF); PowerShares Emerging Markets Infrastructure (PXR); and, PowerShares Dynamic Building and Construction (PKB).

3. *Alternative Energy* is typically defined as solar, wind and nuclear energy. These components are accounted for in ETF representing the DAX global Nuclear Energy Index (NLR) which covers suppliers of uranium, pure nuclear power companies and U.S. based Utilities, and includes: Canada 28%, Japan 22%, United States 22%, France 12%, and Australia 11%.

4. *Commodities* include: precious metals (gold and silver), prices of which are driven by global inflation, a weak U.S. dollar, and geopolitical uncertainty; industrial materials (copper, aluminum zinc, nickel, lead and iron), all of which are tied to the global economy; coal and steel; and, agricultural commodities. The ETFs that represent these sectors are: SPDR Gold ETF (GLD), SPDR Silver ETF (SLV); PowerShares DB Base Metals (DBB), Metal Vectors Steel (SLX) and Market Vectors Agriculture Agribusiness ETF (MOO)

5. *Health Care* is becoming more of an economic issue as the population ages. The Center of Disease Control and Prevention and the Administration on Aging estimates the percentage of people over 65 will increase from 12.4% in 2010 to 20% by 2030. Several ETFs that have recently captured this rapid growth are: iShares Dow Jones U.S. Medical Devices (IHI), IShares Dow Jones US Healthcare Providers (IHF), and SPDR SD&P Biotech (XBI).

6. *Hyperinflation* is a condition resulting from a return to rapid growth resulting from sharp increases in aggregate (pent-up) demand after a recent recession, and a corresponding lag in supply and production of consumption goods (70% of GDP). While I don't think the economy is at that point presently, given 77% capacity to utilization ratio and 1% to 1.5% core inflation, this economic variable could be a significant consideration in the future. In this context an appropriate choice is iShares Barclays TIP Bond ETF (TIP), where principal and interest payments of the TIP rise and fall with inflation and deflation.

7. *Frontier Markets* are typically thought of as underdeveloped countries which have inherent significant political risk. The BRIC countries (Brazil, Russia, India, and China) in the 1990's were not considered to be emerging markets, thus putting them in frontier market category. In

addition to political risk, liquidity, currency and concentration risk must also be seriously analyzed. Because of these additional considerations, ETFs are a particularly useful investment tool, of which the following provide a range of options: PowerShares MENA Frontier Countries (PMNA), Claymore/Bank of NY Mellon Frontier Market (FRN), Market Vectors Africa (AFK), and SPDR S&P Emerging Europe GUR). The first two ETFs invest in several regions of the world; the third ETF invests only in Africa, whereas the last investment choice concentrates on Eastern Europe.

8. *Peak Oil* is defined by Investopedia as a hypothetical date referring to the world's peak crude oil production, after which production rates begin to decline. According to the International Energy Agency (IEA), global oil output could peak in 2020, in part due to a reduced level of investment in new oil exploration infrastructure resulting from the global recession. One can chose to invest in energy commodities through United State 12 month Oil (USL) (oil), United States Gasoline (UGA) (gasoline), SPDR S&P Oil & Gas Exploration and Production (XOP), or a basket of five energy commodities (light crude, brent crude, heating oil, gasoline and natural gas) PowerShares DB Energy (DBE).

Which of these themes will best capture a resurgent U.S. Economy? The sectors referenced above; large-cap growth, health care, energy, real estate investment trusts and consumer discretionary have recently presented the best relative strength (which according to our research explains approximately 70% of the variability associated with total return) and thus make up the major portions or our portfolios. These ETFs and their allocation will be the subject of next month's commentary.

Given that: 1) Victor David Hanson postulates that "as in every literary, historical or cinematic masterpiece, times must grow darkest before sunrise and deliverance"; and, 2) McCall's charts indicate that the Dow has found its low for the decade and is now in its tenth year of consolidation after peaking in1999 and bears eerily similarities to former historical patterns, could provide supporting rationale for an optimistic market outlook and the beginning of a new bull market in the near future. Lets' hope so!