

TOUCHSTONE UPDATE

Richmond | Goodman Wealth Management

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Dash for Trash

It certainly has been an interesting start to the year. The headlines are screaming about how the TSX is up over 3% year to date... a nice start considering last year's abysmal return (at the index level).

What we have found interesting is which stocks have led the performance so far. The day to day volatility has been enormous with moves of several hundreds points on the indices within hours. It seems not to matter what the fundamentals are to the business...if it starts to run, investors jump on board for fear of missing out.

We call this the "Dash for Trash". We've seen this "event" before. Why have we given this rally such an unpleasant nickname? It's hard not to given the following:

Would you buy this company (name not provided to "protect the innocent")?

| Strategy Variables | | | | | | | |
|---------------------------------|---------|-----|--------|--|-----|-------------|----|
| Quarterly Earnings Moment... | QEM | 21% | | | 36% | -4.4% | C- |
| Qtrly EPS Momentum Next... | QEMNEXT | 21% | | | 1% | -51.1% | E- |
| EPS Estimate Revision 3 Mo... | ERCYM3M | 13% | | | 2% | -78.5% | E- |
| Rel Strength 3M(full stk onl... | RS3M | 13% | | | 28% | 83 | A- |
| Quarterly Earnings Surprise | ESRP | 8% | | | 21% | +9.7% | A- |
| Industry Relative QEM Next... | IR QEMN | 8% | | | 0% | -51.1% | E- |
| Price to Forward Earnings | P/E CYM | 8% | | | 0% | 362.8x | E- |
| ROE using EST EPS | ROE | 4% | | | 6% | +0.5% | C- |
| Price to Book Value | P/B | 4% | | | 7% | 1.9x | D+ |
| Market Capital (in \$ million) | MKT CAP | | 400.00 | | | \$10,619... | A+ |
| Current View Variables | | | | | | | |
| Median EPS Growth-Curren... | CYMGRO | | | | | -75.1% | E- |

Source: Morningstar

In the above table are several of the fundamental attributes that we look at when considering a company of purchase. For the purpose of this discussion we only need to bring your attention to the far right column, where the company is "graded" by our system. If the system gave "F's", they would receive them for sure.

- Earnings momentum is going down the drain: "E"
- Analysts are rapidly dropping their forecasts: "E"
- Its Price/Earnings ratio (a measure of value) is beyond horrible: "E"
- The expected growth in earnings is dim (they are expected to decline by 75%): "E"

If asked how such a stock would perform going forward, we expect that most would say it would perform like we all expected Donald Trump to perform. Badly. Well just as surprising as The Donald has been, so too has this stock and many others that look just as unappealing. This stock is UP year to date to the tune of +32%...making a mockery of reasonable investors who simply cannot justify buying something that would take 362 years of earnings to justify its price. Yet this stock is one of Canada's largest companies and hence has a profound effect on the overall return of the Canadian market.

So while there have been many risky stocks with high double digit returns, one has to ask where the money came from to push them higher. The short answer is that it has come from investments previously made in good, solid companies. Investors frantically trying to recoup their losses in the commodity sector are rushing toward riskier assets once again. To do so, they sell everything else and line up to enter the race.

We don't expect the flow from good toward bad to continue. We sure hope not, as it would mean a new paradigm (don't you just hate that word?) in investing, whereby trash trumps quality (sorry Donald - couldn't resist the pun).

In the spirit of brevity, we will end on that note. However, we felt it important to communicate with you the underpinnings of the market so far this year.

We hope you get a chance to enjoy the March Break and we always welcome your comments in regard to anything we publish.

DOUGLAS GOODMAN and PHILIP RICHMOND

Directors, Wealth Management • Portfolio Managers
Richmond|Goodman Wealth Management
Richardson GMP Limited

Tel. 416.941.6715

Email Richmond.Goodman@RichardsonGMP.com

Toll Free 1.866.989.2599

Connect with us:

<http://touchstonestrategy.blogspot.ca/>

www.RichmondGoodman.com

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