Thackray Newsletter

— Know Your Buy & Sells a Month in Advance —

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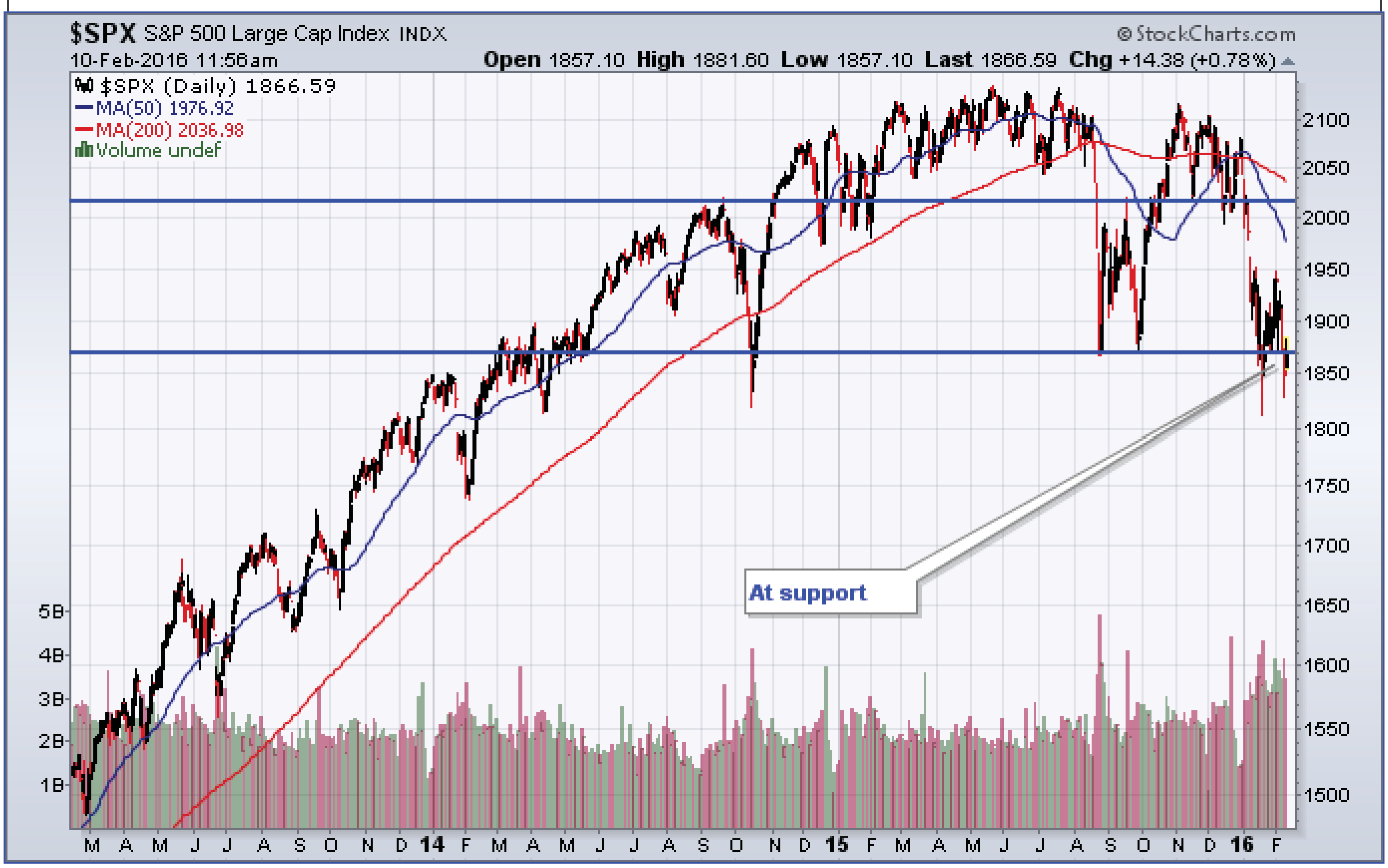
Market Update

Let's not kid ourselves. The stock market has not been behaving well, and technically it is not strong. It is oversold, but it could be that way for long time. A few weeks ago I was watching the ticker screen and noticed that the S&P/TSX Composite printed 11,600. I recalled that this was the same value of the S&P/TSX Composite on the

S&P 500 Technical Status

The S&P 500 has not been able to rally, as there has been a lack of positive catalysts. Earnings, as expected have been lack lustre and are currently expected to decline by 4.1% (Thomson Reuters January 29, 2016). Stronger earnings could have helped boost the stock market but given that we are past the bulk of the earnings season, it is going to have to be stronger than expected economic numbers that is going to be needed to drive the market higher.

The S&P 500 is currently at support and if it breaks this level, the next level of support is in the 1750 area. If the S&P 500 breaks the current level of support, it does not necessarily mean that it is going to the next lower level of support. It does become more problematic if the current level of support is broken and the S&P 500 is not able to move higher after several attempts. On the positive side, the S&P 500 will probably "muddle" higher over the next couple of months, unless the economic news is particularly bad.



Horizons Seasonal Rotation ETF (HAC :TSX)
Portfolio Exposure as of **January 31st** 2016

Symbol	Holdings	% of NAV
	Canadian Dollar Exposed Assets	
	Equities	
	Horizons S&P 500® Index ETF	41.1%
	Horizons S&P/TSX 60™ Index ETF	30.5%
	Horizons BetaPro S&P 500® Bull Plus ETF	10.4%
	United States Dollar Exposed Assets	
	Equities	
	Consumer Discretionary Select Sector SPDR Fund	9.7%
	iShares Silver Trust	5.4%
	US Dollar Forwards (February 2016) - Currency Hedge **	1.4%
	Cash, Cash Equivalents, Margin & Other	1.5%
	Total (NAV $145,067,700)	100.0%

** Reflects gain / loss on currency hedge (Notional exposure equals 68.1% of current NAV)

The objective of HAC is long-term capital appreciation in all market cycles by tactically allocating its exposure amongst equities, fixed income, commodities and currencies during periods that have historically demonstrated seasonal trends. The Thackray Market Letter is for educational purposes and is meant to demonstrate the advantages of seasonal investing by describing many of the trades and strategies in HAC.

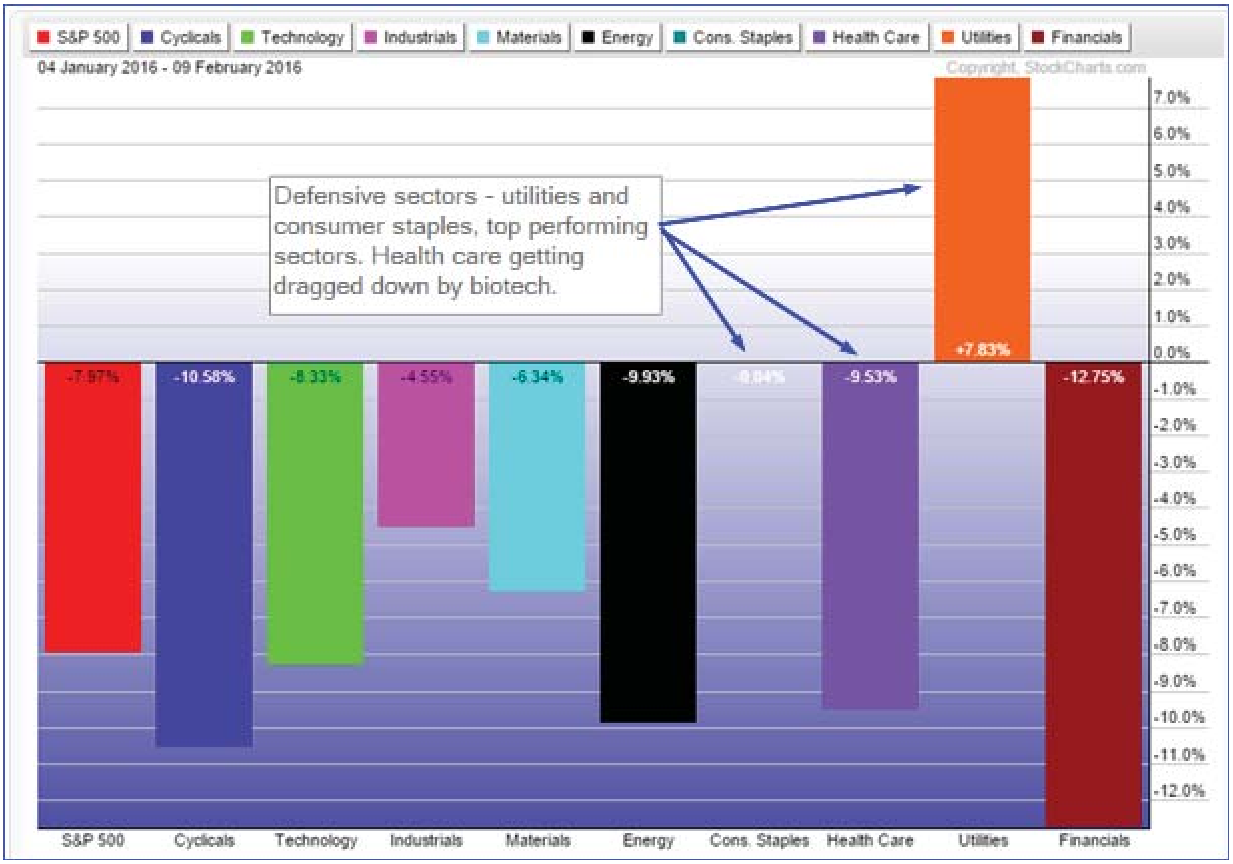
day that HAC was launched on November 19th, 2009. In other words, the Canadian market had done a round trip in six and half years. Fortunately, HAC was solidly in the green, starting at $10 and currently trading above $15.

The stock market has been defanged. Jim Cramer of CNBC developed the acronym FANG (Face Book, Amazon, Netflix and Google) in order to show the lack of breadth in the overall stock market. These four stocks have been the darlings that everyone has favored over the last few years. Until recently, it seems that even when the stock market would trend down, the FANG stocks would still perform well. The market breadth in the U.S. stock market has been getting narrower over time and the FANG stocks still managed to hold up. Over the last two weeks, FANG stocks have started to underperform.

I am not saying that we are starting a bear market, but when the top performing stocks start to underperform…it is a concern. What would make me feel much better is if the FANG stocks started to become market leaders once again.

Typically at this time of the year the defensive sectors underperform the stock market. That is not the case this year, as they are the leaders. The utilities sector has been the strongest sector of this year, followed by consumer staples. Health care has been negative with the market, mainly because the biotech sector has dropped precipitously.

From an overall market perspective is typically expected that the defensive sectors will outperform when the market is correcting. Investors seek safety and more stable earnings when the market is in turmoil. If the market is able to stabilize and improve and the defensive sectors continue to outperform this will be sending a signal that the market is internally weak. When this happens it is the result of investors wanting to still be in the stock market but are scared to take risk. In this scenario it will mean the market and is likely to have another correction. I will endeavor to track this relationship over the next few months in my newsletters.



The FANG stocks remind me of the Nifty-Fifty in the early 1970's. At the time, everyone kept piling into the Nifty-Fifty stocks believing that even if the stock market went down, these fifty large cap blue chip stocks would hold their value. The names in the Nifty-Fifty included many companies that investors would recognize today, such as IBM, Johnson & Johnson and McDonalds. It also included companies that have struggled and even have gone bankrupt over time, such as, Polaroid and Eastman Kodak. The point is that when these stocks finally did start to correct, it was the start of a bear market.

What the HAC is going on

Seasonal investing is a long-term discipline based upon historical trend probabilities. In other words, like every other investment discipline, there are times when it does not work. Not all sector seasonal trades outperform the broad market, all of the time. When things do not work, it is the reaction to the situation that is important.

Staying within its mandate, HAC has been taking measures to reduce risk during the current stock market decline. A lot of the sectors in the stock market that HAC would typically invest in at the current time have a higher beta than the stock market. HAC has deferred to broad market positions, waiting for the sectors to show increasing relative strength. In addition, HAC has exited a number of sectors when stops were triggered and rolled the proceeds into broad market positions. For example, HAC typically invests in the small cap sector from mid-December until the beginning of March. Over the years, HAC has executed this trade successfully. This time around, in mid-December HAC entered into the small cap sector which started on a positive note. In January, the broad markets were not performing well and small caps were underperforming. As a result, a stop-loss was triggered on its small cap position and the proceeds were reinvested into the broad market.

Another example, HAC invested in the U.S. financial sector in mid-December. The sector originally started out by outperforming the S&P 500, but as the possibility of the Federal Reserve increasing interest rates started to diminish the sector started to underperform. When the U.S. banks released their earnings in mid-January, they beat expectations, went down in value while the market went up, and as a result HAC exited its U.S. financial position. It is possible that the U.S. financials will outperform if the market has a strong rally, but from a risk-reward position it makes sense to exit.

In addition, HAC was partially under hedged with its U.S. assets, based upon seasonal tendencies of the USD to outperform in the last few months of the year. HAC benefitted from this position. In January, HAC moved to a full currency hedge position based upon seasonal trends and improving performance of CAD/USD.

HAC has also been shifting assets from the U.S. stock market into the Canadian stock market. In autumn, HAC primarily invested in the U.S. stock market except for the Canadian banks. In January, HAC started to increase its holdings in the Canadian stock market. In autumn, the U.S. stock market tends to outperform the Canadian stock market (see *Thackray's 2016 Investor's Guide*, page 115).

In the new year, the relative seasonal trend is neutral. Given that the seasonally strong period for energy starts later this month, and it is possible for the energy sector to start to gain some traction, HAC decided to increase its weighting in the Canadian stock market.

Sector Updates and Opportunities

Silver –

Silver bullion has been performing well since the beginning of the year. HAC has benefitted from being invested in this segment of the market. Silver, like gold has benefited from the reality that the U.S. Federal Reserve will more than likely not raise rates four times in a year. Silver is seasonally strong at this time of the year, into March. Silver, like gold, is still running on the momentum of the expected delay in the Federal Reserve rate rise schedule.

The danger with a silver investment at this time currently is that if the stock markets start to stabilize, silver could start to underperform. This also applies to investors in gold and gold stocks. It is something to monitor and investors should consider exiting if the stock market gains traction and silver starts to underperform. As of month end, HAC held a position in silver bullion.

My Call: Silver has performed well, but its catalyst for outperformance, the delay in the Federal Reserve rate hikes is probably fully baked into silver's price. Silver will likely underperform if the stock market starts to rally in earnest. Consider selling if market starts to rally.

Industrials

The industrial sector has recently been outperforming the S&P 500. This is typically good news for the broad market. The outperformance has not come from strong absolute performance, but rather more or less treading water while the S&P 500® has been declining. Nevertheless, outperformance is still a good thing. The seasonally strong period for the industrial sector lasts from January 23rd, to May 5th. The sector is currently overbought and a better entry opportunity may lie ahead. As of month end, HAC did not hold a position in the industrials sector.

My Call: Industrials will slightly outperform in its seasonal period as investors become more confident in U.S. growth.

Materials (U.S.)

The materials sector (U.S.) is largely made up of chemical companies. It also holds other subsectors such as gold miners. Gold miners have been performing well since the start of the year, helping to give the sector a boost. More recently, chemical companies have also started to outperform. Chemical companies have a strong seasonal track record at this time of the year. The sector has become overbought and a better entry opportunity may lie ahead. As of the end of the month, HAC did not hold a position in the materials sector.

My Call: Materials will slightly outperform in its seasonal period as investors become more confident in U.S. growth.

Eastman Chemical

Eastman Chemical is a new seasonal trade in my *Thackray's 2016 Investor's Guide* (page 21). The stock has clearly demonstrated a strong positive seasonal trend from January 28th to May 5th and a strong *negative* seasonal trend from May 30th to October 27th.

My Call: Eastman Chemical will break its downtrend line and outperform in its strong seasonal period that started on January 28th.

Consumer Discretionary

The consumer discretionary sector typically performs well at this time of the year, but has recently started to underperform the S&P 500®. The main culprit has been one of the FANG stocks, Amazon, which "tanked" after its earnings were released (Amazon makes up a large part of the consumer discretionary sector). The sector could come back and outperform, if investors start to drive up Amazon once again. At the end of the month, HAC held a position in the consumer discretionary sector.

My Call: *The consumer discretionary sector will probably perform slightly above market over the next two months.*

Retail

The retail sector seasonal trade is classified as one of the stronger seasonal trades. From January 21st to April 12th, during the time period of 1990 to 2015, the retail sector has produced an average gain of 8.5% and has been positive 77% of the time. More importantly, it has outperformed the S&P 500®, 81% of the time in this period (see *Thackray's 2016 Investor's Guide*, page 9). Currently, the sector is underperforming the S&P 500®. Investors should watch for improving relative performance before entering the sector. At the end of the month, HAC did not hold a position in the retail sector.

My Call: The current retail seasonal trade is a strong trade. The sector is currently consolidating. Relative to the market, the sector is oversold. The sector should once again outperform the S&P 500 in its seasonal period that lasts up until mid-April.

TJX

TJX is a strong seasonal trade that starts on January 22nd (*Thackray's 2016 Investor's Guide*, page 11). TJX is considered an off-price retailer and as such it tends to be more defensive. The end result is that the stock has done relatively well over the last few months in the market turmoil.

My Call: The TJX trade has worked well in the past. This year TJX has been outperforming ahead of its seasonal period. This will probably mute its outperformance in its seasonal period.

Energy

The energy sector starts its seasonal period on February 25th. The sector has recently started to outperform the S&P/TSX Composite. No one knows where the bottom is for oil, although everyone is calling out a number. The situation can change very rapidly based upon inventory numbers or possibility of talks among OPEC and non-OPEC countries. From a seasonal perspective, we are entering the time when the energy sector can perform well. It is not a guarantee that it will, but March and April tend to be strong months for the sector. Combine the sector's strong seasonal tendency with improving technicals, a good entry point into the sector could be developing.

My Call: The energy sector is showing signs of improving relative performance. The seasonal period for the energy sector is expected to produce positive results, despite possible long-term bearish conditions for oil.

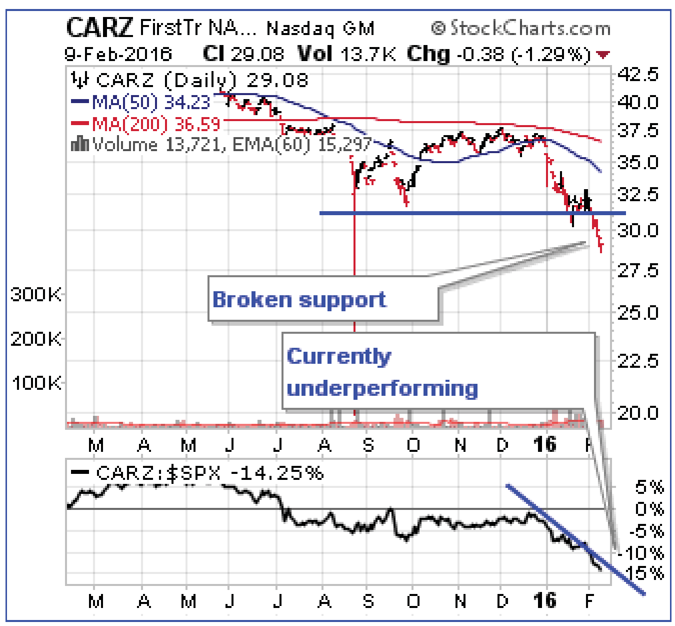
Canadian Banks

Do you want to play energy….buy Canadian banks. Canadian banks seem to be moving lock stock and barrel with the price of Crude oil. Although this is somewhat expected, due to their exposure to the oil patch. It is a bit unusual to see Canadian banks rise few percent one day and down the same amount a few days later, largely based upon the movement in the price of oil.

It is difficult to show how the price of oil is effecting the price of bank stocks as energy sector and banks make up a large percentage of the S&P/TSX Composite. Nevertheless, outside of the Canadian banks outperforming into their Q4 earnings reports at the beginning of December, there is a similar tendency of price movement between oil and the Canadian banks in the graph below.

My Call: Canadian banks will probably outperform in their seasonal period, which lasts up until mid-April.

Automotive



The automotive sector has been hit hard recently, as would be expected when world-wide growth is contracting. Nevertheless, its seasonally strong period is approaching, February 24th (see *Thackray's 2016 Investor's*

Guide, page 23). If the stock market starts to rally, this sector could perform particularly well. The sector needs to be monitored closely for an entry opportunity later this month.

> *My Call: The auto sector is expected to outperform in its seasonal period. Look for stronger than expected economic numbers to help move this sector, or higher than expected car sales.*

Linamar

Linamar is a new seasonal strategy in my *Thackray's 2016 Investor's Guide* (see page 33). Linamar is driven by the seasonal trends of the auto sector. Currently, Linamar is starting to show signs of improving relative performance, but still has not broken its down trend line.

> *My Call: Linamar will probably outperform the S&P 500 once the market starts to maintain positive momentum, possible later this month. The seasonal trade starts on February 24th.*

Brooke's Rant–

It is not nice to be negative

I was brought up to be positive, not negative. Negative was a bad thing. Today, we do not have to look too far to see the prevalence of negative statements. Currently, the presidential candidates in the US are throwing mud at each other like they are trying out for an international mud wrestling competition. Imagine would it would be like if Bernie Sanders and Donald Trump running against each other. For sure it would be entertaining.

Negativity is not the sole purview of politicians: central banks have also become negative. Central banks have now become ensconced with negative policies. Specifically, negative interest rate policies. In 2014, the euro zone implemented negative interest rate policies which essentially charged banks for leaving money at the central bank.

The objective of a negative interest rate policy is to encourage banks to lend money. The effects of this policy are questionable. When interest rates are so low already how can you force more borrowing. Negative interest rates have probably had some impact on helping individuals borrow for homes, but its effect on businesses has been nominal. If businesses do not want to borrow at very low rates already, they are probably not going to borrow at slightly lower rates. For business it is all about the economic outlook. The euro zone has recently introduced even lower negative rates and is planning a third round of greater negative interest rates in March. How negative can you go?

One of my favorite train wreck countries, Japan, recently announced that it was going to start on the path of negative interest rates. Japan currently has a debt to GDP ratio of 238%. In other words, Japan is trying out another strategy as its quantitative easing program has been failing to lift the countries inflation rate to its 2% target.

So what is the problem with negative interest rates on bank deposits at the central bank, other than its very limited effectiveness? It is another form of misallocation of capital. Forcing people and companies to borrow is not part of the natural economic system.

The problem with misallocation of capital is that it somehow corrects itself down the road and when this happens the outcome is…negative. Although the Federal Reserve's first round of quantitative easing was probably necessary to provide functioning liquidity to the markets in 2008, the subsequent rounds probably caused more damage than benefit as it caused a misallocation of capital. The main beneficiary of the quantitative easing programs has been the financial markets and not the economy.

Japan currently has a different negative interest rate brewing: negative yields on government debt. Japanese ten year government bonds have just gone into negative territory, with the current yield of -0.01%. Investors can pay the government to look after their money or they can stuff it in their mattresses. Someone should track mattress sales in Japan…there might be a good business opportunity. On a serious note, a negative ten year yield probably signals it is a good time to short government debt. At least you would not have to pay the carrying charge of a positive yield.

For a country that sells more diapers to senior citizens than to babies, it is going to be impossible for Japan to pay off its debt. Japan has so far been able to operate with a high level of debt because it has been able to finance its debt internally from its loyal citizens. It is just a matter of time before Japan has to seek financing from outside its country. Foreigners will not be willing to lend at next to nothing, or even worse yet, negative interest rates.

I am not sure how Japan can solve its long-term debt problem. It seems like I am one of a few people that believes Japan is in trouble. Japan believes that it can return to yesteryear, as a huge industrial machine with rising productivity. This would allow Japan to pay its debt down with a rapidly expanding economy sometime in the distant future. The world is different now– it is much more competitive and Japan is going to have trouble expanding at the rate it did in its "glory years." Paying down such a large debt is almost impossible. Good luck with your growth ambitions Japan.

A more likely scenario is that Japan finances is debt way out on the curve sometime in the distant future, perhaps writing its debt out thirty years. If the world does not catch on, they might be able to get away with it. If they can pay next to nothing for a large number of years, at least they will have time before a large "balloon" payment implodes the country.

All of this negative talk is making me too negative. Let's hope central banks can have something positive to report in the future....It's not nice to be negative.