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The Swiss Association of Market Technicians

Ron William, Vice President & Head of the Geneva chapter of SAMT hosts an interview in January 2013 with **Martin J. Pring**, *Chairman of Pring Turner Capital*

Mr. Pring was a guest speaker at the SAMT Geneva Chapter October 2012 meeting.

"Investing in the Second Lost Decade"

Ron William & Martin Pring
Geneva, October 2012

Martin J. Pring entered the financial markets in 1969 and has grown to become a leader in the global investment community.

He founded Pring Research in 1981 and began providing research for financial institutions and individual investors around the world. Since 1984, he has published the "Intermarket Review," a monthly market letter offering a long-term synopsis of the world's major financial markets. An audio visual presentation on key financial markets, called The Infomovie Report, is also published on a weekly basis.

He is also chairman of Pring Turner Capital Group, a money management firm, and president of pring.com an educational, technically-oriented website. Demanded as a speaker worldwide, he is the author of several outstanding books including, the classic "Technical Analysis Explained," now in its fourth edition. The book is, as quoted in Forbes, "widely regarded as the standard work for this generation of chartists."

Martin will talk about his latest book, co-authored with partners Joe Turner and Tom Kopas, "Investing in the Second Lost Decade." He will show how he uses technical analysis to navigate secular and cyclical trends in stocks, bonds and commodities.

On March 24, 2000 the S&P Composite began a secular bear market and by June 1 2012 had lost 17% from that peak. When adjusted for inflation the drop exceeded 30%. In this presentation Martin Pring will explain why he thinks the secular bear market in equities has further to run and why the buy/hold approach will continue to be a failed strategy.

In doing so he will outline the root causes of secular bears and the conditions that will signal the next secular bull. Long-term trends in commodities and interest rates are germane to this analysis and will also be covered. Finally, he will introduce the Dow Jones Pring Business Cycle Index (DJPRING), a new rules-based index that capitalizes on these concepts®.

Ron William: How did your journey start within the industry many years ago?

Martin Pring: I started within the financial industry after being fired from my marketing job and was thinking at the time what else could I do? I was living in Toronto, Canada at the time and had gone through all of the advertising agencies, marketing departments and felt like I had exhausted a lot of the options. Thereafter, I realized that I could get involved with the brokerage business in Canada, which was a closed shop at the time in the UK. So it was purely by force of circumstance.

RW: How did you progress to working for the Bank Credit Analyst?

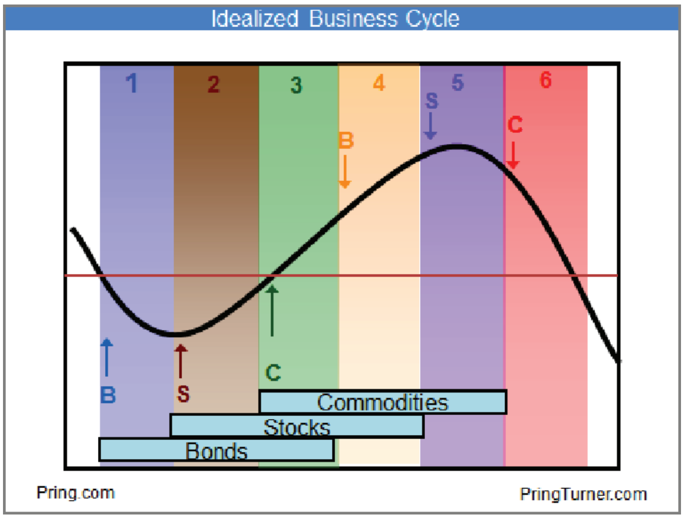
MP: After my training, I was transferred to an office, part of A. E. Ames brokerage, in a little town called Owen Sound, which is about 100 miles north of Toronto and was the office manager. I ran into one of my clients who used to subscribe to the Bank Credit Analyst and he let me look at some of their research reports. I was very impressed because they were explaining exactly why we had experienced high interest rates, and commodity inflation back in the mid-1970s, which is something that no one else could explain to me at the time. I thought this was very good, although the technical analysis perspectives were not as good and rather poor commentary.

THE BANK CREDIT ANALYST

So I went back to our office in Toronto and looked into our library and they had all the back copies of the Bank Credit Analyst. I then reviewed all of their technical analysis perspectives and did extensive research to see how they could have done a little bit better on some of their market calls. Then I wrote to their research departments with all of this information and later received a call to discuss more of my forecasting analysis. So I joined them on a part-time basis and as luck would have it I was transferred to their institutional sales department in Montréal and one thing led to another and I then became a full-time employee. That's how I began my writing career.

RW: During that time as an official analyst at the Bank Credit Analyst, how did you start your specialization on business cycles?

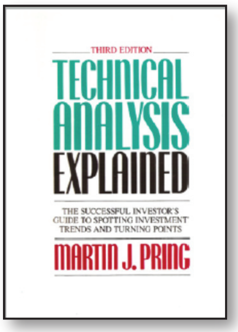
MP: Well, because that is what they did. The Bank Credit Analyst was not analyzing quality of credit, but rather trends of credit which is of course very much tied with monetary policy and the business cycle, with related economic analysis. So I was able to learn a lot of these important principles and supplement them with my technical analysis. They also had a library of very good historic economic books and one of them was called "Turning Points in Business Cycles" by Leonard Ayres, written in 1939. He was also



the same person that developed the advance/decline line. The book explained how the business cycle ran through a series of chronological sequences, six turning points of which securities coming onto the market and the stock market peaking with the over-supply, then interest rates turning about. This was a definite sequence of the business cycle, in terms of financial markets. So I took that a step further and created my six stages of the business cycle.

RW: What was the main premise behind writing "Technical Analysis Explained"?

MP: From time to time we would get representatives from the media calling in and I would pick up and answer a few questions. One of the guys by the name of Kiril Sokoloff, who later became a great friend, was working as an editor for a business week newsletter, a subsidiary of McGraw-Hill. We continued talking and then at one point he asked me if I would be interested in writing a book? I was interested and already had lots of material that I had been assembling over the past 3-4 years and would have liked to get a book written. At the time, there were some great books out there, but none covered the subject from A to Z. So they asked me to write the book and now I am working on its 5th edition.



RW: When was the first book published and how different was it from future editions?

MP: The first edition of "Technical Analysis Explained" was published in 1979. I am great believer in historical data and we had a lot of historical data at the Bank Credit Analyst and I wanted to share this data. At the time, no one had access to data on the Dow Jones Index going back to the beginning of the 19th century. So I decided to include a small section at the end of the book with some of this historical data. McGraw-Hill decided to photocopy all of this material and make it half of the book commentary. *Barron's* reviewed the book and this is one of the points they raised, that it was more of a data book than a technical analysis explained book. So after a couple of years I decided to redo the book and write the second edition, take out all the data and put in the meat. From that point, it began to gain some credibility in the business. Every few years I take another look at the book and decide to update it again. It is now the 5th time that I have gone through this process.

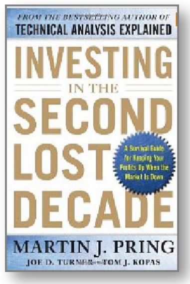
RW: "Technical Analysis Explained" has since earned its title as one of the best technical analysis books in the industry, which has also been translated into many languages around the world. How do you feel about how successful the book has become over the years?

MP: Every time I write a new edition, there is always new ground to cover. Markets change and if you are any good you change as well and pick up new creative ideas. You realize how things fit together in terms of the technical approach, inter-market work, inter-asset work and come up with new stuff all the time.

> **"...THE VELOCITY OF MONEY CIRCULATION HAS DECLINED AND THAT IS WHY WE HAVE NOT SEEN TREMENDOUS INFLATIONARY PRESSURES DEVELOP. BUT THE LONG-TERM MOMENTUM OF THE VELOCITY OF MONEY HAS STARTED TO TURN UP."**

RW: Your new book, "Investing in the Second Lost Decade" co-authored by yourself and business associates, has just been published. Please explain the key themes within the book.

MP: The main premise behind writing the book was to share our technical approach at Pring Turner Capital. How we analyze markets and how we manage portfolios. We felt that the next decade is going to be a very difficult one. Stocks will continue to be in a secular bear market where inflation-adjusted prices will continue to go down, or at the very best, move in a sideways trading range. We also think that the secular trend for bond prices (uptrend for bond prices, downtrend for yields) is probably on its last legs. There isn't enough proof of this yet, but we do have certain characteristics in place. It takes a few years for some of this evidence to fall into place.



At the same time we think that commodity prices are going to continue their secular bull market that began in 2002. In summary, stocks in a secular bear market, commodities in a secular bull and bonds are just about to reverse their secular trend. We believe the long-term environment is going to be very difficult for investors, so we tried to provide them with a book that if they were not interested in buying our ETF or money management, then at least we were giving them an idea of what to expect in the future.

Even though we are in a secular bear market for stocks, there are still pockets of opportunities, for example between 2009 and today, has been a period where the stock market has risen substantially in value. This is where we apply our business cycle analysis and sequential analysis from an investment point of view to try and take advantage of these pockets of opportunity and reduce risk during the down phase of the secular bear market in equities. The key point is to be risk averse because the law of large losses tells us that if you have a large loss, it takes a much larger amount to get back to break even. So the point of our strategy is to create as little risk as possible, while maintaining profitable gains. As a result, our average accounts have doubled since 2000, whereas the S&P500 has only risen 20% in terms of total returns and we have done this with only half the beta risk.

RW: How have you been able to formulate this strategy within the new Dow Jones Pring US Business Cycle Index (DJPRING) and the ETF (DBIZ)?

MP: A couple of years ago Dow Jones Index approached me and said they were familiar with our business cycle work, would I be interested in creating an index based on the work that we have done. We have now created an aggregate index based on the idea that markets operate on the business cycle and can be fitted into six stages. This is derived from three financial markets: stocks, bonds and commodities. Each one has two turning points, a top and a bottom. We created models to try and identify which if these stages we were in. So for example, Stage 3 is when everything is bullish and we have looked back as far as the 1950s to see how all these Stage 3s have performed, which were the best assets to be in, also the best sectors and allocation of stocks.

> **"...BOND PRICES HAVE PEAKED, STOCK PRICES ARE STILL GOING UP, BUT WITHIN THE TERMINAL PHASE OF THE CYCLICAL BULL MARKET AND COMMODITY PRICES ARE JUST BEGINNING THEIR CYCLICAL PHASE. IT ALL DEPENDS ON HOW QUICKLY COMMODITY AND BOND YIELDS GO UP, AS TO HOW LONG THE STOCK MARKET CAN CONTINUE TO GO UP."**

This index has now been developed and it has a symbol of DJPRING. We used the strategies for the index and integrated them with the ETF (The AdvisorShares Pring Turner Business Cycle ETF) (DBIZ). It is not exactly the same as the index because the index uses ETFs and ETFs involve a management fee. So we try and lower our management fees by buying individual stocks based on those preferred sectors. For example, if a particular stage called for an allocation to the banking sector, then we would look for the best yielding bank stocks, the best performing in terms of relative strength and so forth.

RW: In terms of your current market outlook, why have inflationary pressures not appeared yet despite massive central bank quantitative easing and government yields at historic low extremes?

MP: I believe the key reason is the fact that velocity of money has been declining for 10 years or so. Governments can increase the money supply, but they still need to get people to use that money and use it faster and faster. However, the velocity of money circulation has declined and that is why we have not seen tremendous inflationary pressures develop. But the long-term momentum of the velocity of money has started to turn up. Moreover, bonds are in the process of turning on a cyclical and secular basis. Long-term government yields have been declining since September of 1981, which is 31 years and the average secular trend for bonds is around 27 years. So we are overstaying our welcome on this bear market in long-term government yields. All these factors suggest to me that we are now embarking on a commodity bull market. A technical review of the Commodities Raw Industrials, which is a good economic sensitive indicator (without weather-related markets), has just crossed above its 12-month average. Moreover, a ratio of commodities versus bonds, which is the ultimate inflation/deflation measure is also starting to turn up. So we have the fundamental signals with velocity of money turning up and the technicals also heading north. It might bounce around for a few months, but at this stage, it looks to me that we are entering the inflationary part of the cycle.

RW: Which stage of the business cycle are your models suggesting that we are currently in…?

MP: Our models are currently signaling Stage 2, which is when bonds and stocks are bullish, while only commodities are bearish. This has proven true for the last year and a quarter, when it would have been best to have avoided commodities. As of last month, the barometers have turned to Stage 4. However, the way that I calculate it is by using a two-month moving average to avoid whipsaws, and so this is not yet at Stage 4. Stage 4 is when bonds are about to turn bearish, while stocks and commodities are bullish. So if we only look at the individual month, December [2012] signaled Stage 4, but we need another two months of further price data to achieve that point. Even so, a lot of the sector rotations do look like they are moving to a Stage 4 type of environment. This is an environment where commodities such as gold averaged 14% and copper 24% monthly gains on an annual basis. It's not the most intense part of the cycle, but it still is very much a strongest stage in terms of inflationary pressures.

RW: Within the context of a potential Stage 4 of the business cycle, you would be expecting a further rise in the stock market. How much of a bullish signal would this be, given that US stock prices, such as the S&P500, are already very over-extended, having more than doubled in value since 2009 and now looking to make new all-time highs?

MP: Typically the business cycle will trigger a recovery phase and the growth path rolls over and then we move into a recession. However, occasionally what can happen is that we can experience a growth recession, where the growth path goes down, but it doesn't go beneath zero and acquires renewed strength, allowing it to grow again, before turning down later. We have already seen one of these growth recessions take place about six months ago. The same chronological sequence of bonds, stocks and commodities is experienced, but it's just not as intense in terms of volatility and the rotation happens faster. So where I think we are now is that bond prices have peaked, stock prices are still going up, but within the terminal phases of the cyclical bull market and commodity prices are just beginning their cyclical phase. It all depends on how quickly commodity and bond yields go up, as to how long the stock market can continue to go up.

RW: Is there a particular trigger point? At what stage would you expect a price acceleration in commodity prices to adversely impact the stock market?

MP: It's important to look at the technical positions and gauge how they might be affecting the stock market. Previous cycles do not offer any particular trigger point, for example such as a 12-month rate-of-change rising above 50% or whatever it might be. Each cycle is different because the makeup is not just between stocks, bonds and commodities. There are all kinds of other things going on such as housing and so forth. Therefore, it's important to review the overall economic picture in order to understand at which point rising commodity prices may adversely impact the stock market. Once again, it's very important to look at the technical positioning in the market to get that.

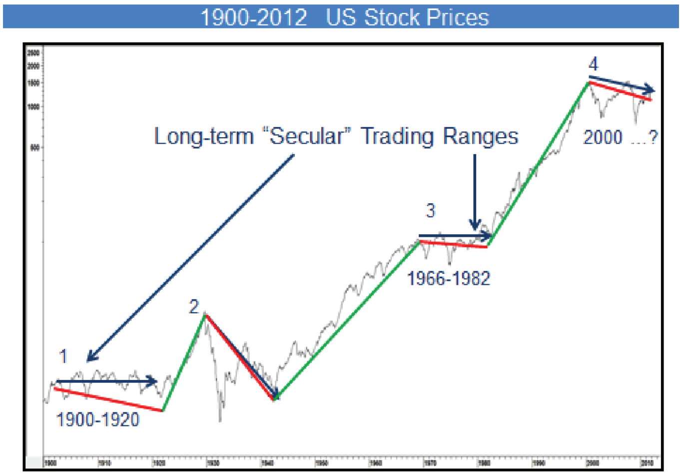
The character of the market is different in each cycle. For example, the S&P500 can serve as a coincident indicator of the market; or something like utilities, telecoms, or financials are generally speaking, leading indicators; and resource-based stocks are traditional lagging indicators. The market is made up of all of this stuff. For example, in the year 2000, technology, which tends to be a lagging indicator, was one of the principal drivers of the stock market rally, but the advance/decline line peaked in 1998. So underlying stocks were declining between 1998 and 2000, but in real-terms, you could see the market rising because these stocks were gaining more and more of the index weighting. In summary, all I am saying is that the market can be rising, but with different variables driving it at different times and it's the character of the market which is important.

RW: How would you compare the character of the current secular bear market in stocks to prior bear cycles such as 1966-1982?

MP: All these secular bear markets have three things in common. One is psychology; they move to an extreme of optimism and then an extreme of pessimism. A measure of price-to-earnings, as used by Robert Shiller, we rose up to a 45 multiple in the year 2000 and the previous peak was 32. The traditional benchmark for a secular bull market is 22 times and usually a secular bear ends when price to earnings reaches 7 to 8 times. So a huge swing in psychology takes place and that's characteristic of all bear markets.

The second thing is that you usually have a structural problem. It's relatively easy to get out of a recession, because inventories adjust and so forth and its takes a few policy adjustments to recover. However, a really important structural problem is much more difficult to overcome. For example, the technology boom in 2000, housing bust in 2007, or even the canal boom in the 1830s and the railroads in the 1870s. These structural problems take a long time to work through the system. So what typically happens is that the government comes along and tries to help and this usually hinders the whole process. We have already seen this in recent years, during the technology and housing boom, where the government comes in and tries to print more money and run up the budget deficits.

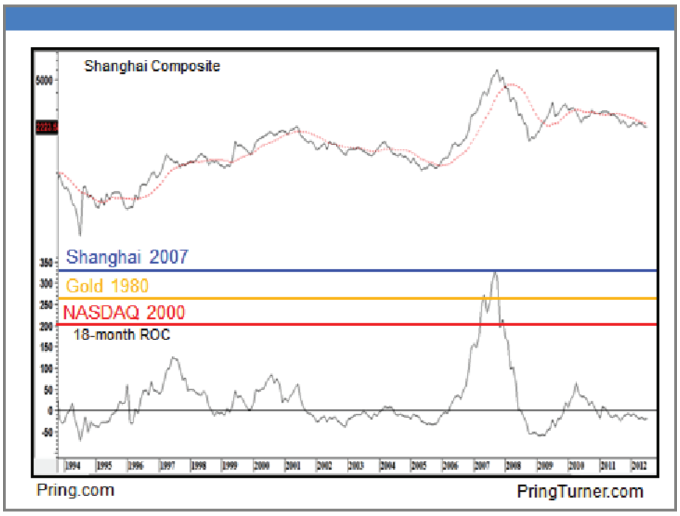
The third thing is rising, or excessively high, commodity prices, which is the kiss of death to the stock market on a secular basis. Taking into consideration these three characteristics, we are on par with what happened during the bear market of 1966-1982.



RW: Looking towards the Asian countries, we have just recently witnessed two important political changes in countries such as China and Japan and corresponding early stage recoveries in their domestic markets. What is your technical perspective of their local stock market performance?

MP: I believe that China is beginning a cyclical bull market, within a long-term trading range that began in 2007. There isn't a lot of historical stock market data on China, but one of the proxies that I use is an 18-month rate-of-change of the Shanghai Composite which rose up to 360%. In my research, whenever a market's rate-of-change rises above 200%, as it did with the Nasdaq in 2000, gold in 1980, and many other markets, almost invariably that indicates a rush of sentiment to the optimistic side. That often means the market needs to work its way down over the next 5-10 or 15-20 years and correct the excessive levels of optimism as reflected in the 18-month rate-of-change. So we saw an extreme in China that I feel will still take several more years before we surpass the high of 2007.

As far as Japan is concerned, I do not have any evidence that the secular bear market which began in December of 1989 is over. Although, of course, I do believe that in



terms of time duration, it really has run its course. So my expectation is for Japan to eventually lead its way out of its secular bear market and perhaps even the one that the world is now also in. In summary, I believe that Japan is currently experiencing a cyclical bull market recovery. However, whether it has broken its secular bear market is another question.

RW: What do you see as the big themes or trading opportunities into the new year of 2013?

MP: I believe the big opportunities are in the commodity-based resource areas. As I mentioned before, I think that we are currently moving into Stage 4 of the business cycle, which has historically offered an average of 24% annualized returns on copper. The chart of copper looks like it's about to break to the upside. It also looks like it has a terrible top, but I think that top is going to fail based on the fact the whole economy is going to improve here. I am not so sure about precious metals, although they usually correlate with commodities.

Meanwhile, I feel that countries such as India and China are pretty good opportunities. This is also because the US market has been underperforming for the last six months to the rest of the world. Although, that relationship is very oversold and I expect a bounce here over the short-run. The main trend is against the US, relative to the rest of the world. Also, the relative performance of Europe is improving and we have been recommending a number of European ETFs. We have also been recommending Hong Kong.

RW: In the many years that you have been dedicated to the industry, how would you describe the evolution of technical analysis? Past, present and future…?

MP: I believe that it is very much growing in importance. One key reason is that we have organizations like the International Federation of Technical Analysis (IFTA) and the Market Technicians Association (MTA) that are promoting it as a profession and giving it accreditation. A related point is that in the old days a lot of people would give wild market predictions and gave technical analysis a bad name. Now I believe it's become a more serious proposition, with the formation of these technical analysis societies and the educational aspects of their development.

The second reason is that over the years we have seen a shortening of time horizons. In the old days, people used to invest for a long period of time, one or two years or so. Now with the advent of tick charts and intraday services, we have more intraday trading. So the focus has become smaller and smaller. This has got to be one of the advantages of technical analysis, because it is very difficult to do this using fundamental analysis. Things don't change that much. Whether you were a tape reader or a chart reader, technical analysis has come into its own because of the narrowing of time horizons.

RW: What role has technical analysis educational support played within the industry? How would you compare to past years when you were starting out in your career?

MP: When I started out in the industry there was nowhere that you could achieve an accreditation in technical analysis. There were lots of books written, but as I said before none of them really covered the subject from A to Z. In order to learn about technical analysis, you basically had to read books. There were not that many people teaching it, not compared to how it is now being taught at universities and financial workshops. There are a lot more educators now and that means a higher level of sophistication and accuracy of analysis is going to improve from a technical point of view. Although, of course from a psychological perspective, you still have to learn how to master your own emotions and the emotions of the markets. ■

To watch a Bloomberg interview with Martin Pring from Geneva in October 2012, please click on the image at left.

For additional information about Martin Pring, go to www.pring.com

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