



Markets This Week

June 17, 2006

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Investment Idea

Question: How can I use mosaic theory in my investment research?

Answer: Mosaic theory is defined as a method of analysis which involves collecting both public and non-public (often non-material) information about a company in order to determine the proper value of the company's share.

For example, the company's president makes a public announcement that a company will be expanding into new profitable product lines, but does not disclose any more information. Your friend owns a large grocery store and tells you that the company was making inquiries about a particular product which is very profitable and currently available only in Australia. Hence, you have a potential to put the two pieces of information together (based on mosaic theory) and perform analysis that incorporate public and non-public information.

Quiz

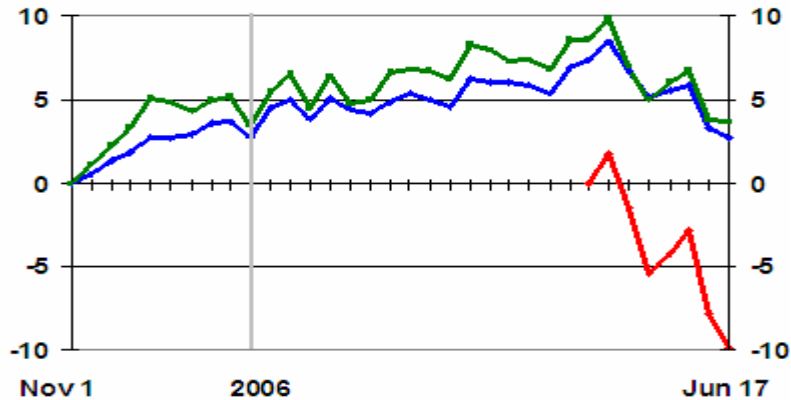
Which of the following is an example of financial analysis based on mosaic theory?

- A) Listening to the company's teleconference
- B) Putting together public and non-public information
- C) Technical analysis
- D) Buying based on tips from a broker

Answer at the bottom of the newsletter.

Our Results (Cumulative %)

Chart 1



Symbol	One-week %	Since Inception %	We Bought On	We Sold On	Expected Return %	Risks	Reasons
Members Info	-2.84	-12.36	May 1, 06	-	Market + 4	Medium	Trend investing
Members Info	-1.43	-7.26	May 1, 06	-	Market + 2	Low	Investment style
InvestWELL Picks (Average)	-2.13	-9.81					
Passive 60/40	-0.51						
S&P 500	-0.06						

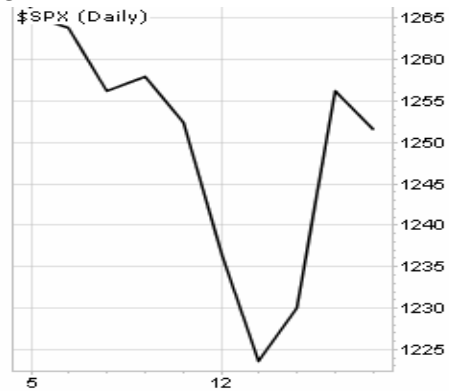
Last week, **InvestWELL Picks** underperformed the general market by over 200 bps. There are only two positions in our InvestWELL Picks which means that the portfolio will be subject to a greater volatility.

Market Highlights

Jun 11 – Jun 17, 2006

- Last week, the US equities were very volatile but largely managed to hold at the level of the previous week's close (Chart 2 & 3). Currently, many traders and investors are very anxious about the market, which has caused an increased volatility.

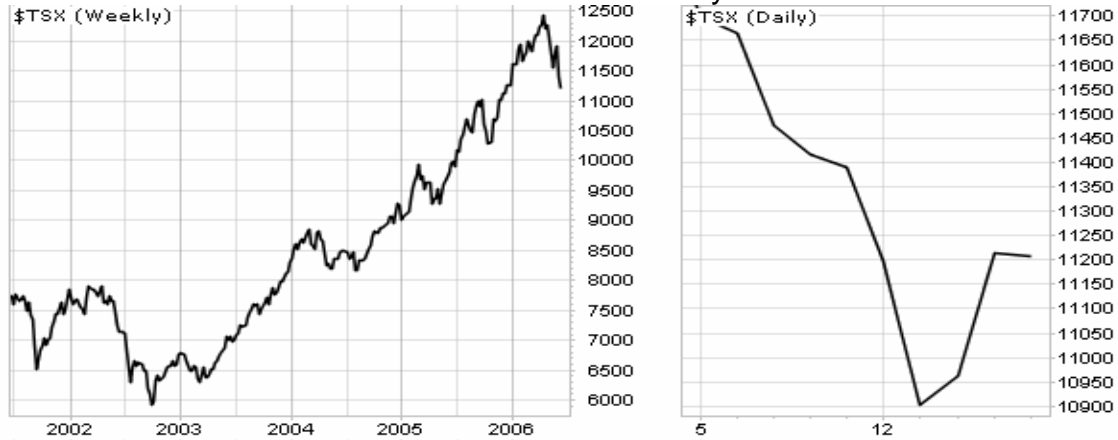
Charts 2 & 3. S&P 500: 5 Years and Last 10 Days



Charts courtesy of StockCharts.com

- The Canadian equities have also held fairly well given the overall weakness of the market (Chart 4 & 5). Many analysts are beginning to voice an opinion that the commodity prices have turned the corner.

Charts 4 & 5. TSX Canada: 5 Years and Last 10 Days



Charts courtesy of StockCharts.com

- The steep equity downturns usually lead to the flight to safety e.g. money moving to gold or government bonds. However, over the last month this relationship has not worked for gold (Chart 6). As equities fell, the gold prices went into a near free fall. Is this a sign that investors are losing faith in gold altogether?

Chart 6. Gold Prices – 1 Year.



Chart courtesy of Galmarley.com

- The volatility index, know as VIX, is one of the best measurements of the investors' anxiety in the market (Chart 7). Currently, the VIX index is at a level unseen in 2 years, which may indicate that the market is ready for a short-term rebound.

Charts 7. Volatility VIX (red line) – 2 Years



Chart courtesy of StockCharts.com

Worth Watching

- Many people are getting very concerned about the amount of overvaluation of the real estate. The recent report published by Global Insight and National City claimed that 39% of all US houses were deemed to be "extremely overvalued", based on median sales prices, median income, population and historic values. In addition, a well respected scholar, Robert J. Schiller, who predicted the end of the high-tech bubble, stated that the US real estate has the highest valuations since 1890!

Behavioral Finance Indicators (see explanation)

Based on our behavioral indicators, the markets will experience a short-term rebound in the near future. The current correction was a very good reality check for investors who thought that the markets go only in one direction – up. It is worth pointing out that the equities were quite overbought between January and April, which may not bode well for the market prospects in the next few months.

Please consider the following factors:

- Chart 8 – the divergence between prices (black line) and the advancing/declining line (red line) is tightening but the two started to diverge in February this year.
- Chart 9 – a low confidence of small investors (as represented by AAll, i.e., the ratio of bulls/bears). Small investors are usually a contrary indicator.
- Chart 10 – the rising put/call equity ratio indicates that small investors are losing their confidence that the market will advance (red line). Again, an excellent contrary indicator.

Charts 8 - 10: Advancing/Declining Line, AAll and Equity Put/Call Ratio



Charts courtesy of StockCharts.com and DecisionPoint.com

Answer to the Quiz:

B is correct. Mosaic theory combines both public and non-public information. It helps to improve the quality of financial analysis.

Thank you for reading Markets This Week.

Please feel free to share it with your friends.

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