

# One Man's Story: How to Reliably Get Above-Market Returns

## I. Introduction

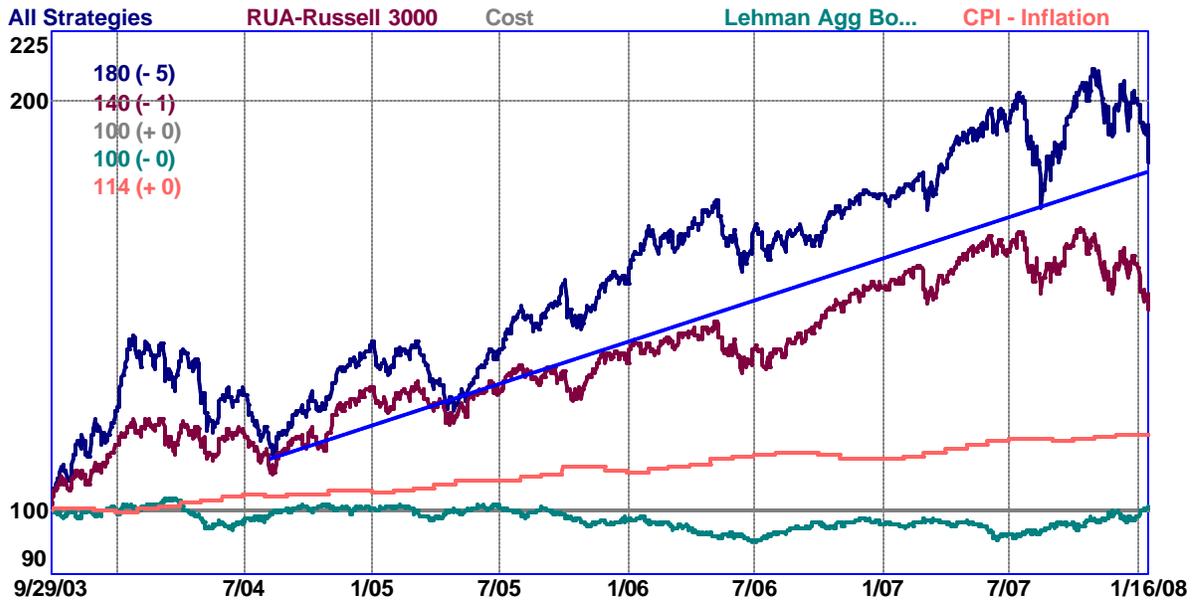
- A. Business model
- B. Overview
  - 1. Allocation
  - 2. Strategies
  - 3. Guidelines
- C. Disclaimer

While I have been conscientious in the calculations and data that are presented, I may have made errors in my calculations. Past returns are not a guarantee of future returns. Adoption of any of the ideas or actions reviewed here is done at your own risk.

- D. Handouts and access to materials

## II. Weight to Equities

- A. Historically based Monte Carlo demonstration. (See handout "Monte Carlo Planning".)
- B. Personal allocation (See handout "Personal Investments: Allocation and Methodology".)
- C. Does it work? Overall Performance & Risk Perspectives



The beginning date coincides with the earliest date for the Lehman Aggregate Bond Index, given here by the iShares ETF AGG.

The yield of the trendline is 15.2%. Above the line is breathing room; below the line is time to look at escaping further damage.

An alternative to mutual funds.

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At what point would you rather have the passive investing, maroon line of the Russell 3000 than the average returns reflected in the dark blue line of active investing? At what point would you rather be in bonds? Are bonds safer?

With volatility, two questions count. What percent of the time are the returns inferior and below market returns? Did you have to sell during that time period?

If one stock goes up 10% and another goes down 5%, which has the greater risk? (Risk is defined by standard deviation. Even if a stock performed every day on the trend line of the previous page, it would have a high standard deviation and by definition be risky.)

#### D. Adjust asset allocation to lifecycle

I start by defining fixed income as the total of salary and earnings from work, Social Security benefits, pension income, annuity income, any royalties, bond coupons or interest, dividends and all other interest, such as from personal loans or certificates of deposit. In other words, fixed income is any source of regular payments not coming from withdrawal of original investment or capital gains. I then decided that the sum of these fixed income sources as a percent of what is needed to support ones living expenses should at least equal ones age. In other words, the percent of living expenses coming from equity withdrawals should not exceed 100 minus ones age. Equity withdrawals come either out of capital gains or a reduction of assets.

If secure fixed income sources provide for 100% of living expenses, all remaining assets should be invested in equities or other opportunities for capital gains. This is the best way to cover the risk of inflation, and the optimum stewardship of money which will probably go to heirs or charities.

The calculation of living expenses should include that for dependent heirs, i.e. heirs who are disabled or not able to financially support themselves. In such cases the inheritance is necessary and must be secure; it should be perceived as an entitlement rather than a gift.

Immediate annuities are a viable way to purchase a pension if fixed income does not meet the above threshold. These are available without load. A very nice calculator is available at [www.immediateannuities.com](http://www.immediateannuities.com) Other options include certificates of deposit (international and domestic), TIPS, and ETFs of Treasuries and short-term bonds.

### III. Allocate by Selection Method

The performance charts are available at [www.wenzelanalytics.com](http://www.wenzelanalytics.com) A link is on the navigation panel of each page. A link on the report downloads a pdf file if you want to print it.

#### A. Three Methods

1. Strong Rationale : Portfolios, history and performance.
2. Tested Source: Portfolios, history and performance.
3. Statistically Derived
  - a. Portfolios, history and performance.
  - b. Database and research process.
    - 1). Fields are selected and placed in a view in Stock Investor Pro. Currently I have about 120 fields (columns). While I keep exploring with new fields, I have found a set of about 20 variables that consistently differentiate the best screens.
    - 2). Using the utility program, this set of user files is backed up, and then restored to the monthly applications each existing on a separate folder.
    - 3). The view is exported from each month and appended to an Access database.
    - 4). Respective tables are created in Access and joins are made to connect the data for each month with the returns and rank-relative-strength for four weeks, thirteen weeks, twenty six weeks and fifty two weeks later.
    - 5). The data are pared down, excluding stocks under one dollar and with less than a 5,000 shares traded daily over the past ten days.
    - 6). For faster processing, I will often take a sample of say 80,000 records from the remaining total of over 400,000, and export only select fields for analysis.
    - 7). The data are imported in KnowledgeSEEKER for data mining.

- 8). The results of days of exploration in KnowledgeSEEKER trees are logged into a hierarchical format in Excel for easier comparisons.
  - 9). Screens are compared and test runs made on the current data in Stock Investor Pro to see how many stocks are selected, what stocks are selected, and the diversity of stocks.
  - 10). The list of stocks for each screen are exported to TeleChart for a technical analysis rating.
- c. One current screen

A mega-cap screen is one of the screens I have recently developed. If I have my calculations right, it compares favorably to the top AAIL Stock Screens over a recent three year period in terms of return monthly and longer-term returns, standard deviation, consistent adequate monthly count, and turnover. This is one of about 45 screens; I am still in the process of running comparisons. The screen is:

PRICE	Price	>1
AVD_10D	Volume--Average Daily 10d	>5
EXCH	Exchange	<> OTC
SMG_DESC	Sector	<> Fin
RRS_26W	% Rank-Rel Strength 26 week	>41
RPCFPS_A3Y	% Rank-Price/CFPS-Avg 3 years	<11
RROE_12M	% Rank-Return on equity 12m	>81
RMKTCAP	% Rank-Market Cap Q1	>91
PRCHG_GM3Y	Price Change 3yr Annual	>17.8<88.8
RSHRINSTN	% Rank-Institutional shareholders	<91

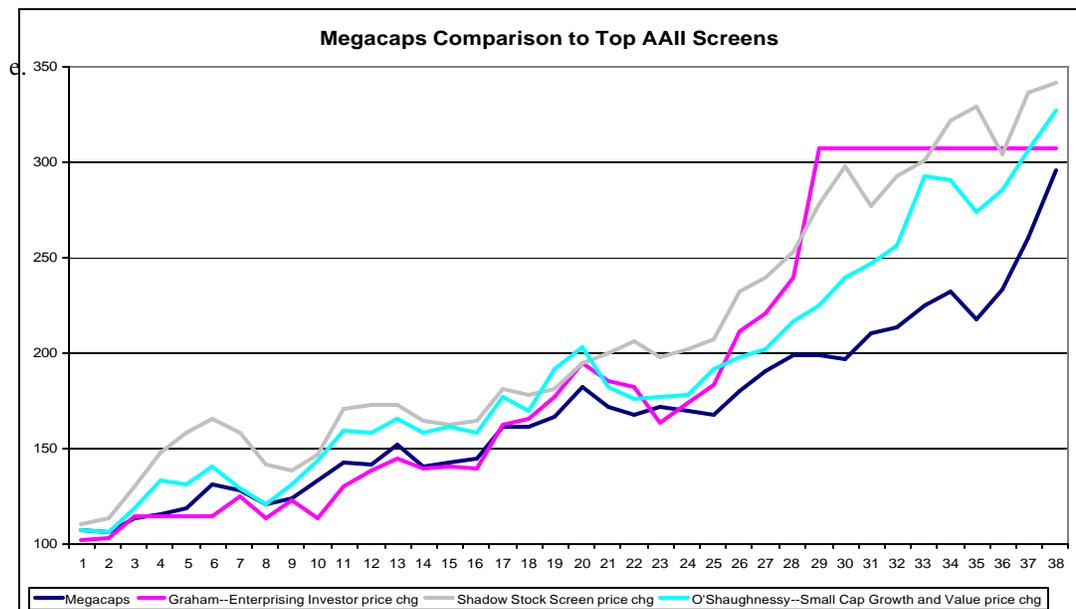
A recent run of the screen gave the following stocks:

Ticker	Company	Sector
BVN	Compania de Minas Buenaventura	01 - Basic Materials
GGB	Gerdau S.A. (ADR)	01 - Basic Materials
KPN	Koninklijke KPN N.V. (ADR)	09 - Services
PKX	POSCO (ADR)	01 - Basic Materials
SNP	China Petroleum & Chemical Cor	06 - Energy
STO	StatoilHydro ASA (ADR)	06 - Energy
TEF	Telefonica S.A. (ADR)	09 - Services
TMX	Telefonos de Mexico, S.A. (ADR)	09 - Services
UL	Unilever plc (ADR)	05 - Consumer Non-Cyclical

- d. A comparison to the best of the AAIL screens is shown in the chart on the next page.

While on the chart, the Megacap screen trails the others, the volatility is less and the returns after the first month are higher. While the AAIL screens take one month returns, the dependent variable I solve for is an average of rank-relative-strength for 4, 13, 26 and 52 weeks going forward. That gives better returns in down markets and over longer time periods. When I test many of the AAIL screens, I often find a few critical months in the history where only two or three stocks met the screen and had very high returns. Such aberrations are not dependable.

One important test of a screen is to remove a variable and see what it does to returns and the monthly count over say a five-year period. Then restore the variable and do the same with each variable in succession. Usually there are two or three variables which do the heavy lifting. It is not unusual with the AAIL screens to find that returns go up when removing a variable. The next test is to experiment with different values for each range.



f. An example of the KnowledgeSEEKER hierarchical tree for the Megacap screen is attached.

B. May analyze by other dimensions, but they are occasional, not driving.

1. Market cap
2. Growth/Value
3. Domestic/Foreign; Currency base
4. Sector

#### IV. Implement Guidelines

A. Do top down: Every selection has to fit into a portfolio.

B. Base final selection and selling on technical analysis or prescribed durations.

1. Refuse to sell during short-term oversold markets.
2. Contain timing to a designated portfolio.

C. Monitor emotions.

1. Ones own
2. Market sentiment
3. Temperature of all media and resource materials

D. When to sell a ten-bagger? Watch for parabolic rise and position allocation.

E. When to sell a loser? Ignore basis. Will stock go up within time frame?

F. Stay organized and use tools that give constant perspective. (List Attached)

1. Pivot tables. (May be time for a demonstration.)
2. Fund Manager position and portfolio comparisons.

a. Like Yahoo position comparisons

G. Question the experts, screen the garbage.