The Insider Trader

Issue 105 December 2015

2016 A Pick & Mix Year

Markets at a glance

***Trendspotter Signals** (click on links to obtain up to-date signal)*

[Dow Jones (DJ)]

[S&P 500 (SP)]

[£/US$ (BP)]

[US Dollar Index (DX)]

[Crude Oil (CL)]

[Gold (GC)]

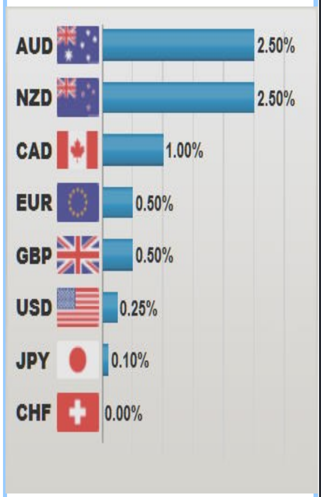
[Coffee (KC)]

[Sugar (SB)]

[Wheat]

[Cotton]

[Rough Rice]



As we approach the close of 2015 it has not been a spectacular year for the US indices. As I write the Dow Jones is up 1% and the S&P 500 is up 2%. The best performer out of the majors has been the NASDAQ 100 QQQ as technology has been a bright spot up 11% Year to Date.

The good news is against this back-ground of fairly low index returns we have had stocks that are up 40,50 and even 100% and I am not talking about small caps, these are S&P500 stocks like Amazon. We also did very well from the GMCR short. The heatmap shows this.

Biotech has had a volatile year but be-fore you get too upset and call the bio-tech boom over (which I do not believe it is) the XBI is still up a very respectable 11.5% so far this year and could run up in the last few weeks of the year.

Looking forward to 2016 I believe we will have to be nimble and it's going to be a case of picking stocks both long and short so it's going to be a pick & mix year again.

Seasonally we are in the bullish period and the seasonal system remains long until at least April, however, 2016 is an election year with the US elections being held on the 8th November. Historically markets do not like elections or mid-term elections which are held on even years. The chart shows that whilst markets still go up in even years the returns are histor-ically better in odd years.

November is still some time away so I would not become too worried about the elections yet but it will be in the back-ground. As stated in my last newsletter local TV stations stand to do well as ad-vertising spending will boom and TGNA should benefit.

S&P500 Heatmap YTD what's happening under the surface http://www.finviz.com/map.ashx?t=sec&st=ytd

Aerospace & Defence spending to remain high

The recent sad events in Paris and the general unrest around the world will mean that government spending on defence will have to remain high and any notion of cutting back on security spending is highly unlikely. There are a few ETFs that cover this sector one being ITA you can read more here https://www.ishares.com/us/products/239502/ishares-us-aerospace-defense-etf

You have a crossover of companies that are involved in civilian and military aerospace. Two names I still like in this are **Transdigm (TDG)** and **Spirit Aero Systems (SPR)** both involved in aerospace parts. In the more traditional defence areas ROK, RTN and LLL all stand to do well. The biggest holdings are shown in the table opposite.

If we do have more terrorism attacks then this will not be good for the commercial airline sector, however, I believe flying will continue to be a bright spot and a lot has been learnt since September 2001. Fuel prices remain low, airlines have become far more efficient so this should be a good year for airlines; a few stocks to look at DAL, VA and LUV. The have been a bit choppy the last few months but overall are in good up trends.

Ticker	Name	Weight (%)	Sector
BA	BOEING	8.73	Industrials
UTX	UNITED TECHNOLOGIES CORP	7.77	Industrials
LMT	LOCKHEED MARTIN CORP	6.89	Industrials
RTN	RAYTHEON	6.11	Industrials
GD	GENERAL DYNAMICS CORP	5.83	Industrials
NOC	NORTHROP GRUMMAN CORP	5.68	Industrials
PCP	PRECISION CASTPARTS CORP	5.11	Industrials
COL	ROCKWELL COLLINS INC	3.52	Industrials
TDG	TRANSDIGM GROUP INC	3.46	Industrials
LLL	L-3 COMMUNICATIONS HOLDINGS INC	3.36	Industrials

Alcoa (AA) – Spin off—50% up side in 12 months

Alcoa Inc. produces and manages primary aluminium, fabricated aluminium, and alumina worldwide. The company operates through four segments: Alumina, Primary Metals, Global Rolled Products, and Engineered Products and Solutions. The Engineered Products and Solutions segment offers titanium, super alloy investment, and aluminium castings; fasteners; aluminium wheels; integrated aluminium structural systems; architectural extrusions; and forgings and hard alloy extrusions. The company's products are primarily used in the transportation, including aerospace, automotive, truck, trailer, rail, and shipping; packaging; building and construction; oil and gas; defence; consumer electronics; brazing; power generation; and industrial applications.

Alcoa has been a terrible investment; the stock is down 40% in 2015 and down from $40 in 2008 to around $9 so why would you consider buying this zombie stock? Well Alcoa is due to spin off its Manufacturing Business in the second half of 2016 and I believe the

Company is approaching a point where it will be re rated. A full outline is here

https://www.alcoa.com/global/en/investment/pdfs/15_investor_day/Combined-Presentations.pdf

What we have is the old Alcoa which frankly is still going to struggle but may have a small bounce and the new higher margin business which has good potential and will attract new investors. I will initially hold both parts but then likely sell Alcoa and keep the higher margin new part of the business. If you recall I did this with **Dean Foods (DF)** and Whitewave which I still own. Whitewave (WWAV) is the higher margin plant extra products such as soya milk where as Dean was the low margin dairy business.

At $9 I can see this stock move up by 50% to near the $14 mark. You can spread bet this or just buy stock. If you spread bet it will be adjusted to reflect the spin off.

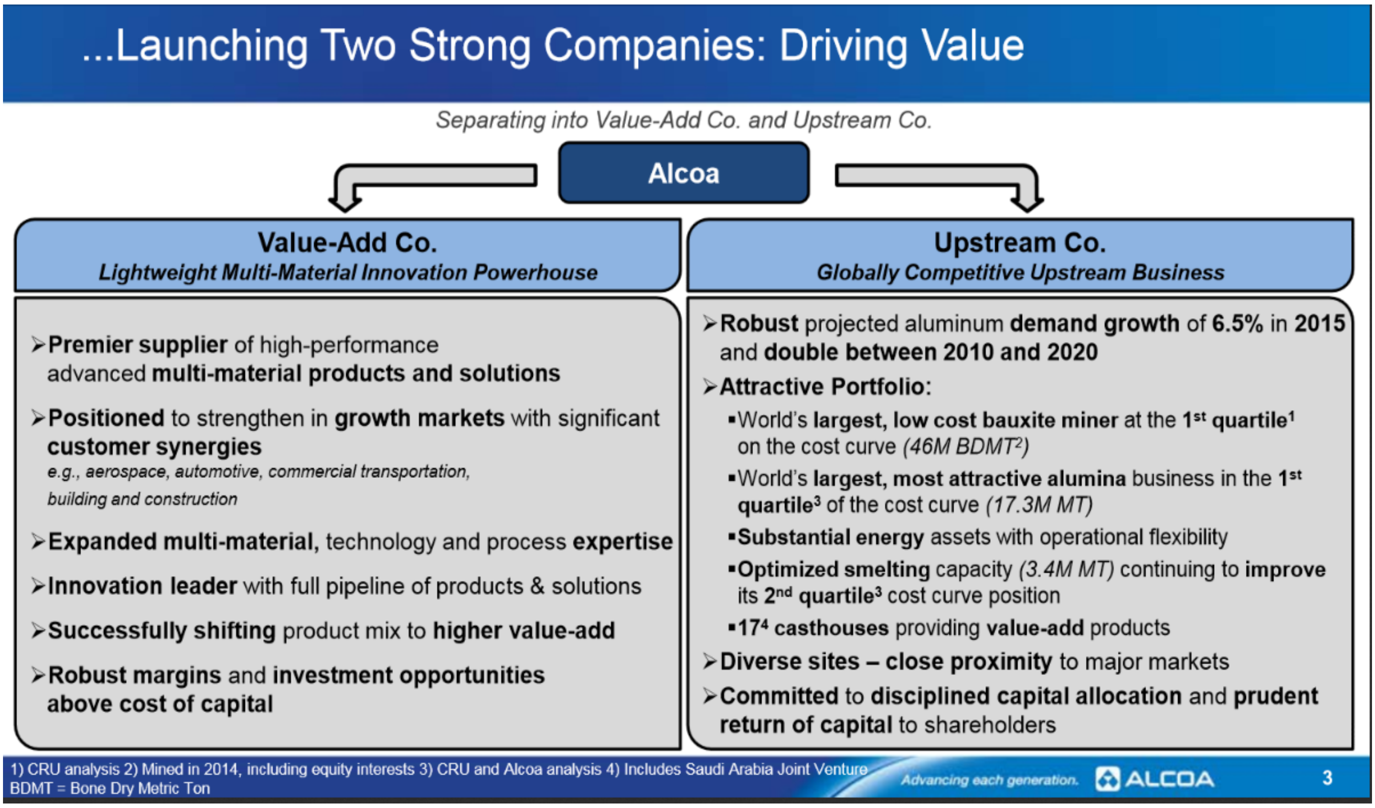
Even if I have got this totally wrong then I think the downside is limited for Alcoa especially after the horrendous 2015 and this is sill an S&P500 stock and even pays a dividend.

Alcoa: A Sum-of-the-Parts Valuation

The company is worth nearly $15 a share, based on applying peers' multiples to the cash flows of its businesses. Just the units that make products are worth more than the $9.25 stock price.

Business	EV/Ebitda Multiple	Ent. Value Per Share
Alumina	6.2	$4.49
Primary Metals	6.0	0.67
Global Rolled Products	8.0	3.17
Engineered Prod. & Solutions	11.2	11.31
Transportation & Construction	7.8	1.48
Net Debt		-5.43
Minority interest in Alcoa World Alumina		-1.80
Preferred stock		-0.04
Equity Investments*		1.08
Total		**$14.93**
Current stock price		**$9.25**

EV=Enterprise value; Ebitda=earnings before interest, taxes, depreciation and amortization. *Excludes carrying values of two Brazilian hydro plants and includes Saudi Arabian joint venture. Source: Elliott Management



Chemicals – Agriculture – A year of Consolidation

I believe 2016 is going to be a big year for chemicals and agriculture stocks and we are going to see some mergers as the industry needs to consolidate. It's hard to know exactly how this will play out but I remain a fan of FMC which I mentioned in my 19th November update. I have since bought more shares.

This is a fairly simple trade and it can go 3 ways which are all positive for FMC shareholders

1. Monsanto (MON) or another similar company comes in and buys them out. Monsanto has been trying to do a deal with Syngenta but they are resisting, doing a deal with FMC would be much easier.

2. Activist shareholders call for a shake up and that will include selling or spinning off parts of the business. This would be a slower path but still positive

3. The company just starts doing better and the share price starts to catch up. The board is shaken up.

In this trade we have a powerful ally in Larry Robbins of Glenview Capital (which has had a terrible 2015) but has a very good history. Robbins just upped his stake http://www.nasdaq.com/article/larry-robbins-adds-to-stake-in-fmc-cm534214

A few of our old deals were we had Glenview on side included the TripAdvisor/Expedia split and Tenet healthcare.

I think we can get back at the $60 level for a nice 50% upside in the next 12 months. If you look at the chart the down trend looks like its ended and we are moving higher. FMC is an S&P500 stock so it's easy to trade via a spread bet or own stock.

I would like a quick (6 month kill) and get option 1 but even the slower option should be a good return in 2016.

As I am writing this news of a Dow Chemical (DOW) and DuPont (DD) merger is just coming out.

Work in process

I have plenty of new ideas and work in process, however, it's not a case of just quantity but rather having quality opportunities. We should have a good number of takeovers, spin offs and mergers next year that we can profit from.

For now I would like to take this opportunity to thank you for your continued support and wish you a wonderful Festive season and a healthy and prosperous 2016.