



In a scene from the movie *Margin Call*, a banker looks out of his car window and says, "Look at these people, wandering around with absolutely no idea what is about to happen." That's an accurate portrayal of the current state of the perspectives of many advisors, who fear that an EU sourced Armageddon may be just around the corner, and consumers, who just helped push Black Friday results up 6.6% over last year's holiday frenzy.

News flow moves between extremes from the sometimes positive news about the US economy to the "terrifying" (word choice of Mohamed El-Erian) news out of Europe. These divergent perspectives have piqued advisors' concerns about both the outcome and volatility associated with this crisis.

At Toews, the concerns expressed by several of our advisors (especially those new to Toews) relate to how our system will perform given all of the unrest. "We've never seen volatility like this," commented one advisor. Another advisor asked, "How can the Toews system function when the markets behave indecisively, and with such big one day moves?" A question that hasn't been asked, but is poignant is, "What is the historical outcome when one day volatility increases?"

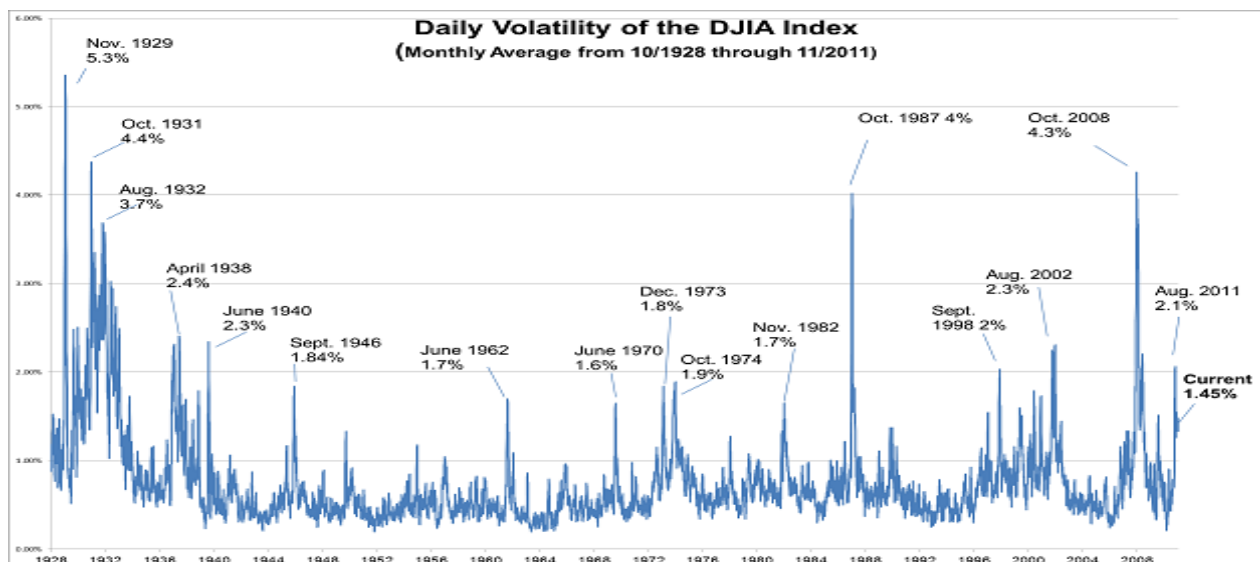
As scientists of the markets, I thought this would be a good time to share not only our experiences in navigating volatile markets, but a portion of our studies that look all the way back to 1928, providing a thorough historical examination of volatility as it relates to our system.

Let's start with the first assertion: "We've never seen volatility like this!"

Why this is important:

One day volatility has a direct impact on our system's primary vulnerability. When we exit, if market moves are significant before we re-enter, the Toews system can under perform or have outright losses.

Using Dow Jones Industrial Price data that looks back to October of 1928, the market has moved by an average of .75% per day (monthly average), with a range of .2% to 5.4%. The current monthly average is 1.45%.



As the above graph shows, while daily volatility is elevated, it's not at unprecedented levels. During our period of management, we've seen similar levels of volatility on 11 separate occasions. Each time, news flow and huge market gyrations bring calls to our office like those that we're receiving now. Our system is modeled to address this volatility. Despite the elevated volatility that we've experienced, our system has produced a compelling performance advantage relative to the markets, and has dramatically reduced downside participation during significant downturns.

Now on to the more relevant question: **What is the historical outcome for the markets when one day volatility increases?**

The answer: **High one day volatility is a predictor of significant market trends, an environment that our system favors.**

Average daily % change (past month)	Average Index Gain or Loss 1 Year Later
0-.49%	13.5%
.5-.99%	15.0%
1.0-1.49%	21.0%
1.5-1.99%	27.8%
2-2.5%	31%
Greater than 2.5%	40%

Table based on the DJIA, 10/28 - Present

When the market has one day moves averaging between 1.5% and just over 2%, as it has over the past few months, the index has ended roughly 30% higher or lower one year later.

How this relates to Toews

We refer to this as a best/worst type of market for our system. As one day volatility increases, the system becomes more vulnerable to under performance. However, the outcome from that same volatility tends to produce big market moves. If the market moves significantly higher, we are in a position to potentially capture those gains. If the market makes a big move lower, our relative performance improves, and we aim to capture big gains during the market rebound (as we did during 2008/2009). Further, the size of the trends tends to dwarf any underperformance or losses that occur during whipsaw markets.

Despite all of the headlines and volatility, our management team **prefers** the current environment to lackluster markets that rarely produce significant market moves. The key for advisors is to avoid exiting the system before big trends play out (cautionary data point: peak redemptions from our system occurred in late 2007/early 2008).

Market Environment

The coordinated efforts by central banks to alleviate the EU crisis produced significant gains on

Wednesday this week. Yet, even as global equity markets surged, the cost to fund Italian debt remained static. We offer two critically important observations: 1) if larger EU economies (Italy, Spain) become unable to fund their debt, the problem may escalate outside of the capacity of even Germany and France to contain, and; 2) if the situation expands to encompass all of the EU as stated above, we face the prospect of a debt/banking crisis that will surpass the sub-prime crisis in its likely impact on financial assets and the global economy.

This is overtly not a market that will be friendly to modern portfolio theory based portfolios. As we saw in 2008/2009, when the turbulence of crises escalates, correlations across asset classes tighten, and all assets move lower together.

Even fixed income may not be the panacea of safety that it has been over the past 3 decades. As we discussed in our webinar series earlier this year, and as documented in the book *This Time is Different* by Rogoff and Reinhart, sovereign debt crises tend to produce hyper-inflation ultimately. Fixed income tends to be the most vulnerable asset class during these periods.

The path to navigate these markets is straightforward, but requires constant execution: 1) stay committed to equity markets, the best performing asset class that helps protect investors against inflation; and 2) hedge your equity portfolios against losses. Both are pillars on which the Toews system is built.

Disclosure

Past performance is no guarantee of future results. Investments are subject to risk, and any of the Toews investment strategies may lose money. Investment return and principal value of an investment will fluctuate so that an investor's portfolio may be worth more or less than their original investment. Any investment strategy referenced or presented is not appropriate for every investor and individual clients should review with their financial advisors the terms and conditions and risk involved with specific products or services. Toews' actively managed portfolios may underperform during a variety of types of markets including bull markets.