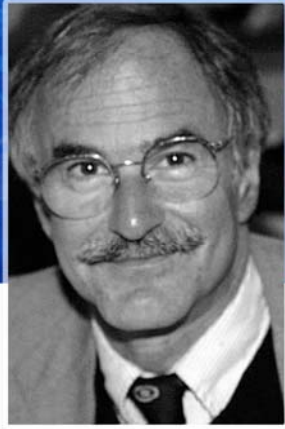


The PAD System Report



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WAITING FOR THE CORRECTION

In Samuel Beckett's depressingly sad drama "Waiting For Godot," Vladimir and Estragon wait in vain throughout the play for the title character to appear. Godot never comes. We have likewise been waiting for months for The Correction, but we are perfectly happy to watch the market continue to rise against a wall of worry. Popular unrest in the Arab world, which has spread to many countries beyond Tunisia and Egypt, has only caused minor hiccups to stocks, and even a bloodier battle in Libya could only take the market down for three days. More Arab autocrats could be toppled, and the political chaos and potential short-term loss of oil supplies could still push the market down more sharply. Oil prices at the \$150 level (still unlikely) could even push the economy back into recession. At home, the looming fiscal confrontation between the Obama administration and the Republicans in Congress could lead to a government shutdown, and further embarrassment for the US. Neither side seems willing to adopt the recommendations of the National Commission on Fiscal Responsibility and Reform, which would put us back on a sustainable path to deficit reduction. But the level of understanding and bipartisanship in Congress reminds us of another repeated line in Godot: "Nothing to be done." More ominously, the most recent "flight to safety" did not seem to buoy the US dollar as much as the Swiss franc. Americans still benefit

mightily from the dollar's status as the world's key reserve currency, and any demotion, although unlikely, would lead to a painful decline in the US economy, stocks, and living standards.

Although Europe has been pushed out of the headlines, we are still convinced that the weak economies in the eurozone will be forced to reschedule their debts. It is only a matter of time for Greece, and Ireland and Portugal may not be far behind. A government default will certainly push markets down around the world, as it did last year.

We are also concerned about the rising interest in US stocks displayed by the average American investor. A spate of new IPOs, and a rich valuation of anything to do with social media is also a red flag. It is not much of a secret that the investing horde is wrong most of the time, most recently selling in panic in March 2009, and then missing the near-doubling in the subsequent two years. If the recent mutual fund inflow data does presage a broad return to the market, expect further upward movement in prices that will eventually end in tears, as always.

RECOMMENDATION: VL MAP remains in the SELL range at 50%. Continue to hold cash reserves of 25%-30%. Only a few Model Portfolio stocks are currently cheap relative to

their 3-5 year appreciation potentials. (2/28/11 6:10 PM PST)

MODEL PORTFOLIO-C

PORTFOLIO STATISTICS: Weighted year-ahead performance rank: 2.60; Weighted safety rank: 2.38; Portfolio MAP: 78%. (These statistics and more can be found on the subscriber's corner of our website.)

UPDATES ON PORTFOLIO STOCKS:

Value Line has commenced its "rollout" of 3-5 year appreciation potentials to 2014-16. This rollout has improved the long-term appeal of many of the stocks in our portfolio. When this rollout process begins, VL MAP normally ticks up by 10 percentage points. This year is no exception: the VL MAP jumped to 50% in spite of a strong rally in the last month. Nonetheless, we are still in the SELL range, and further rallies will push the VL MAP down to levels which will force us to take a few more chips off the table. By the same token, it will take a sizeable correction just to get VL MAP back to the NEUTRAL range.

Zhongpin is one of only three stocks in the Model Portfolio which can be bought under the PAD rules at current prices. The stock has retreated into the high teens, at the same time its 3-5 year appreciation potential has been raised to 40-60, meaning the stock can now be bought up to 20. The story here remains the same: rapid growth and rising incomes in China leading to rapid increases in the demand for meat, especially pork. A slowly rising yuan makes earnings even more attractive in depreciating dollars.

Linear Technology is another stock with 100% 3-5 year appreciation potential to the low end of the range: the stock is hovering just under 35, with 3-5 year appreciation potential of 70-105. Earnings should double by 2014-16. The company beat VL earnings estimates for the

most recent quarter, and raised the dividend again, as it has for many years. This year should witness an all-time earnings record, and LLTC's specialty chips are in high demand. The company spends heavily on R+D, which is another PAD plus.

SunTech Power has rallied sharply, yet the stock still has the greatest 3-5 year appreciation potential (25-40) of any stock in our portfolio. Its ranking for year-ahead performance has also improved to "3." The Chinese have clearly picked this industry as one of their green tech national champions, and that should assure growth for many years. Nonetheless, we do not recommend charging into the stock now. We are still concerned about the degree to which sales and earnings are driven by subsidies in Europe, which are not sustainable in the long run.

GenProbe has surged to new recovery highs above 60. Latest earnings came in above Value Line estimates. The company is buying back stock, and making small but strategic acquisitions (GTI Diagnostics). The pipeline looks promising: the Aptima HPV assay is already marketed in Europe, and clinical trials are well underway in the US. The PROGENSA PCA3 assay is marketed in Europe and clinical trials are complete in the US. This product is a much more precise test for prostate cancer. The APTIMA Trichomonas test is also marketed in Europe and has completed trials in the US. GenProbe has B++ financial strength and has a high ranking of "90" for price growth persistence. We expect a boost in 3-5 year appreciation potential when the stock is next reviewed in mid-March.

American Medical Systems has quietly inched up to 22, and its 3-5 year appreciation potential has been boosted back to 40-60, making the stock a buy up to 20. The GreenLight laser system for prostate reduction continues to be improved, and the market for this product will likely grow as fast and as steadily as a 60-year old's prostate. And we are not even going to talk about their products for ED. TMI.

C. R. Bard is an ideal PAD stock for a conservative investor. The company produces record earnings every year, invests in future growth (R+D is 7.1% of sales), and is conservatively managed (financial strength is a terrific A++). Price growth persistence is a strong “90,” and beta is a low 0.6. The stock should soon break 100 and then will likely split 2-for-1. We will hold all of the extra shares. Unfortunately, this one is only cheap enough to buy when the market is severely oversold.

Intuitive Surgical has risen sharply, but Value Line has increased 3-5 year appreciation potential to 415-620. We are happy to hold our remaining shares, since Value Line projects that earnings in 3-5 years should just about double the record level expected for 2011. The stock also has financial strength of A+, and price growth persistence is a top “100.”

Cognex has been downgraded to a “3” for year-ahead performance, but its 3-5 year appreciation potential has been further boosted to 50-75. Although we prefer a “3” stock with terrific 3-5 year appreciation potential to a “1” stock with no 3-5 year appreciation potential, we are concerned that much of the long-term potential for Cognex is now based on an expansion of the p/e, rather than growth in earnings. This is a key PAD warning sign, and may put CGNX near the top of any sell list we create this year.

Stryker has pushed over 60, and Value Line has increased 3-5 year appreciation potential to 115-140. The company is again on track to set new earnings records every year. Finances are strong enough (A++) to support both stock buybacks and a modest and steadily growing dividend. The company, a Boomer play on hips and knees, is expanding into stroke treatment with the purchase of Boston Scientific’s Neurovascular division. We have adjusted SYK’s maximum buy price to 60, to reflect the dividend.

TBT, our negative ETF bet on long-term US interest rates, rallied over 40 before settling back as investors “rushed to quality” with unrest

in the Middle East. If the United States cannot get its fiscal house in order soon, the rush to quality will start heading somewhere else. Long rates should rise over the rest of the expansionary cycle, even if outyear deficits are reduced. We hope they will be, but TBT is our protection if they are not. QEII, which we support, will end this year. These purchases have provided a cushion under bond prices. At some point the Fed will need to shrink its bloated holdings of Treasuries, and the long-end is a likely place to start.

II-VI has reported rapid growth in sales and earnings, and the stock has pushed above the low-end of its 3-5 year appreciation potential, which is now 50-75. Even though we have lightened up already, the stock is a prime candidate for a new Sell List.

FEI has fully rewarded our patience, and our willingness to stick with a stock ranked “4” for year-ahead performance. The stock has doubled from its 2010 low, and is now ranked “1” for year-ahead performance. 3-5 year appreciation potential has been raised to 60-95, meaning the stock can now be bought up to 30. Earnings are soaring, and should double 2010’s record over the next 3-5 years. Nanotechnology will continue to grow in worldwide importance, and this bet on the very small should continue to pay off very big.

Cognizant continues to soar. The stock has hit record highs above 70 (up from the mid-teens two years ago), as earnings break new records. Value Line still expects earnings to double again over the next 3-5 years. We think it likely that the stock will split 2-for-1 this year. Unfortunately, even though Value Line keeps moving the goalposts, with 3-5 year appreciation potential now 75-110, the stock has charged past the low end of that range. We have lightened up once, and will probably have to do so again. Our only hope is that Value Line raises 3-5 year appreciation potential in its next review, since VL inexplicably lowered 3-5 year appreciation potential a bit during the rollout to

2014-16.

Taiwan Semiconductor had its 3-5 year appreciation potential raised to 20-30, and its year-ahead performance ranking is now a "1." Although the silicon foundry company came in below VL estimates for the latest quarter, it still set an eps record. Growth should continue, fueled by the migration to ever smaller circuits. On tap are 20 nanometer widths, which are the

same width as a bacterial flagellum. The yield is a plus here, and the only negative is that some of the 3-5 year appreciation potential is based on p/e expansion.

ADVICE: Hold remaining stocks. Switches are not OK until the VL MAP returns to the neutral range at 60%. The maximum buy prices of our current favorites are listed below.

<i>Shares</i>	<i>Company (Ticker)</i>	<i>Recent Price</i>	<i>Value</i>	<i>Advice</i>
400	Amer Med Systems (AMMD)	21.9	8,764	Buy @ 20
250	Automatic Data (ADP)	50	12,500	Buy @ 38
100	Bard C.R. (BCR)	97.8	9,780	Buy @ 63
200.13	Celgene (CELG)	53.1	10,627	Buy @ 43
102.12	Cephalon (CEPH)	56.3	5,750	Buy @ 50
501	Cognex (CGNX)	27.9	13,983	Buy @ 25
160	Cognizant (CTSH)	76.9	12,300	Hold
300	FEI Corp (FEIC)	33.5	10,060	Buy @ 30
338.13	Fiserv (FISV)	63.3	21,393	Buy @ 48
300	GenProbe (GPRO)	62.9	18,860	Buy @ 40
30	Intuitive Surgical (ISRG)	328	9,840	Hold
150	II-VI (IIVI)	51.2	7,680	Hold*
258.99	Linear Technology (LLTC)	34.6	8,950	Buy @ 35
80	Precision Castparts (PCP)	142	11,340	Hold
400	Proshares Ultra Short Treasuries (TBT)	37.6	15,050	Hold
160	Sigma Aldrich (SIAL)	63.9	10,222	Hold
323.30	Stryker (SYK)	63.3	20,450	Buy @ 60
900	SunTech (STP)	9.5	8,550	Hold
1450	Taiwan Semiconductor (TSM)	12.3	17,820	Buy @ 11
160	Thermo Fisher (TMO)	55.8	8,930	Buy at 38*
600	Zhongpin (HOGS)	18.6	11,150	Buy @ 20
CASH	Money Mkt Fund		100,000	
TOTAL			\$354,000	*Advice change

WWW.PADSYSTEMREPORT.COM: subscribers can renew online, and check the status of their subscription. Subscribers also have access to back issues, the current issue in PDF format, and the PAD Portfolio Excel spreadsheet, which summarizes short-term rankings, 3-5 year appreciation potentials for all PAD portfolio stocks, and measures of the Portfolio-weighted overall ranking for year-ahead performance, safety, and MAP.

Note: New subscribers baffled by the details of the PAD System should purchase a copy of Daniel Seiver's *Outsmarting Wall Street* (3rd edition, Probus/McGraw Hill, 1994). This book contains a full discussion of the PAD System and all of its rules. Although out of print, it is regularly available on Amazon.com for \$5 -\$10, shipping included. A number of public libraries also have copies.