Market Outlook

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Highlights

Market Risk Index has increased to 91%, largely on worsening valuations. Valuations have climbed to the 97th percentile. Even if we limit our lookback period to only periods after 1990, valuations are still in the 90th percentile. If the market closes out the year near today's levels, our equity return forecast will fall under 2%, meaning that stock prices have been bid up enough that they should become more sensitive to any short-term increases in bond yields.

The psychology score was unchanged for the week, but there were still some new extremes set on individual indicators. The equity put/call ratio hit its lowest level since January 2018. Rydex Ratio reached a new cycle high. Volume going into levered ETFs over inverse ETFs is also at very high levels and hitting the longest stretch of positive readings since January 2018. While several individual indicators are attempting to reach new cycle extremes, it still appears that the Jan 2018 cycle peak for our investor psychology composite will hold.

Breadth and new high/low data have been strong during this December melt-up, and each day that passes seems to remove another stumbling block from the breadth and momentum front. Every day that passes also seems to bring another index – that was previously highlighting an internal struggle in the market – to new all-time highs. Even the High Low Logic Index has been improving (not a buy signal but not as bad as it was). If valuations are starting to look as bad as they did toward the end of the 1990s bull market, breadth looks decidedly better. Investors know this, and it seems to be a key argument being used to justify increasing risk here.

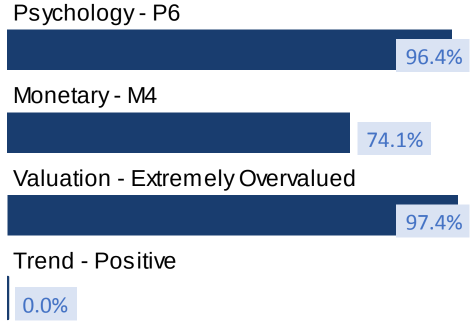
Breadth indicators are used to answer binary questions like whether a higher high in an index is more or less likely, and most are suggesting higher highs for cap-weighted indices in 2020. However, breadth indicators don't do a great job of answering questions concerning the magnitude of a move to expect. Whether an ultimate price high is another 1% higher or 100% higher, it doesn't matter for a breadth indicator. Valuations do a better job of answering these questions of magnitude, and betting too heavily on breadth here implies that investors are either growing overconfident in their ability to get out before the crowd or growing too comfortable with the idea that stock valuations have reached a permanently high plateau.

Market Risk Index

Elevated

91.0%

Category Percentiles



Biggest Psychology Influences

Flow of Funds	Positive
Leveraged Investments	Negative
Option Activity	Negative
Surveys	Negative

Biggest Monetary Influences

Falling Bond Yields	Positive
Velocity	Negative
Yield Curve	Negative

Valuation

7-10 Year Rtn Forecast	2.3%
10Yr Treas Yield (on 11/30)	1.8%

Price Trends

US Equities	Positive
Intl Equities	Positive
REITs	Positive
Broad Commodities	Positive

Market Risk Index scales from 0 to 100%. Higher readings correspond with higher risk markets. Scores below 25% are bullish. Scores between 25-75% are neutral, and scores above 75% are markets vulnerable to major drawdowns.

Chart – S&P 500: Percent of Stocks Trading Above 200dma

Eighty percent of S&P 500 stocks are trading above their 200 day moving average. It's the most participation since January 2018. Does it mean the market is overbought and is likely to take a breather soon? Yes, but it also implies that the market will see higher prices in 2020.

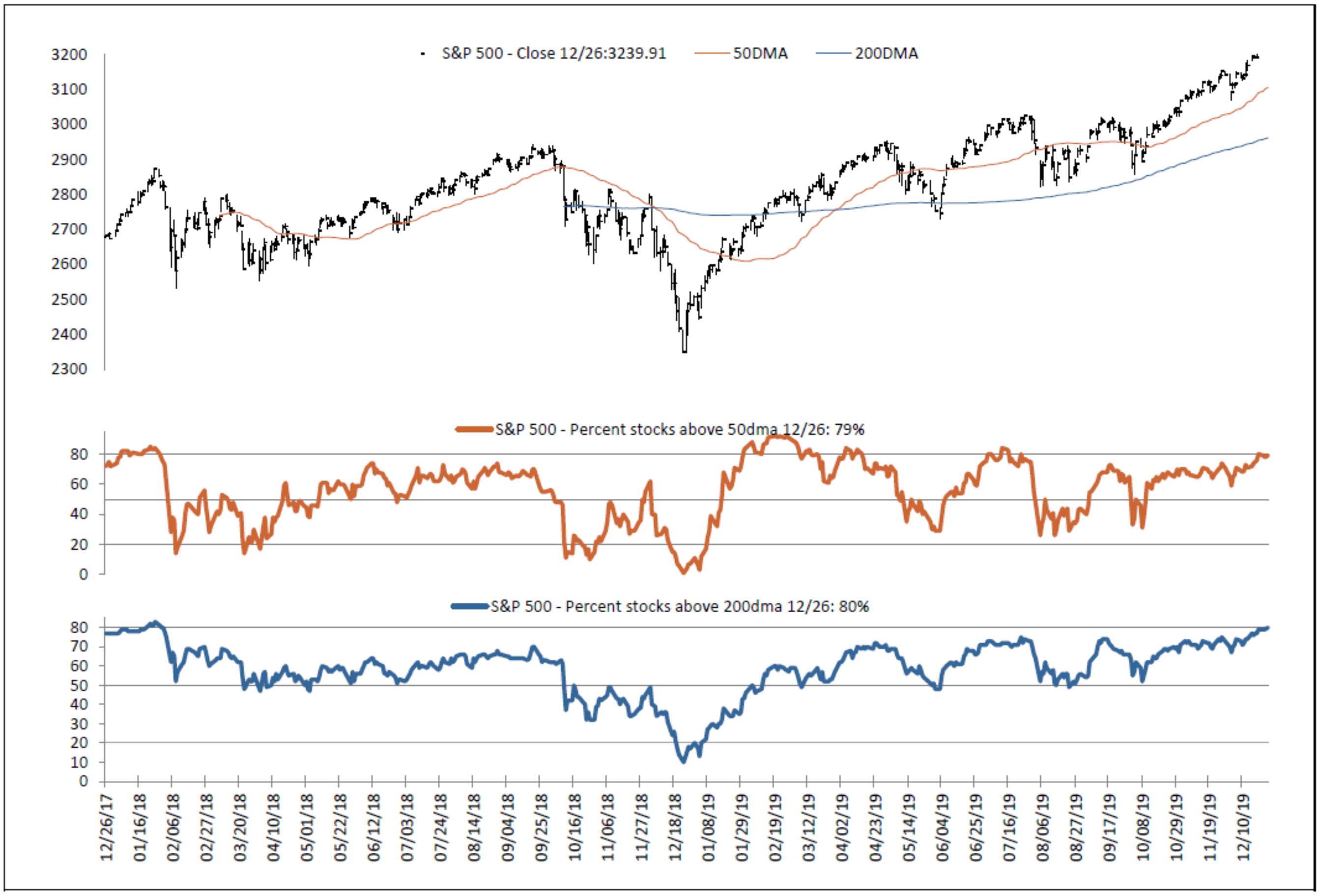


Chart – Rydex Ratio makes new cycle highs

Rydex ratio climbed above 81%, surpassing the previous peak on Jan 30, 2018. This is the highest reading since 1994 when Rydex family was only made up of two new funds, and readings on this indicator were much more volatile. All things equal, for Rydex investors, this is arguably their favorite bull market of all-time.

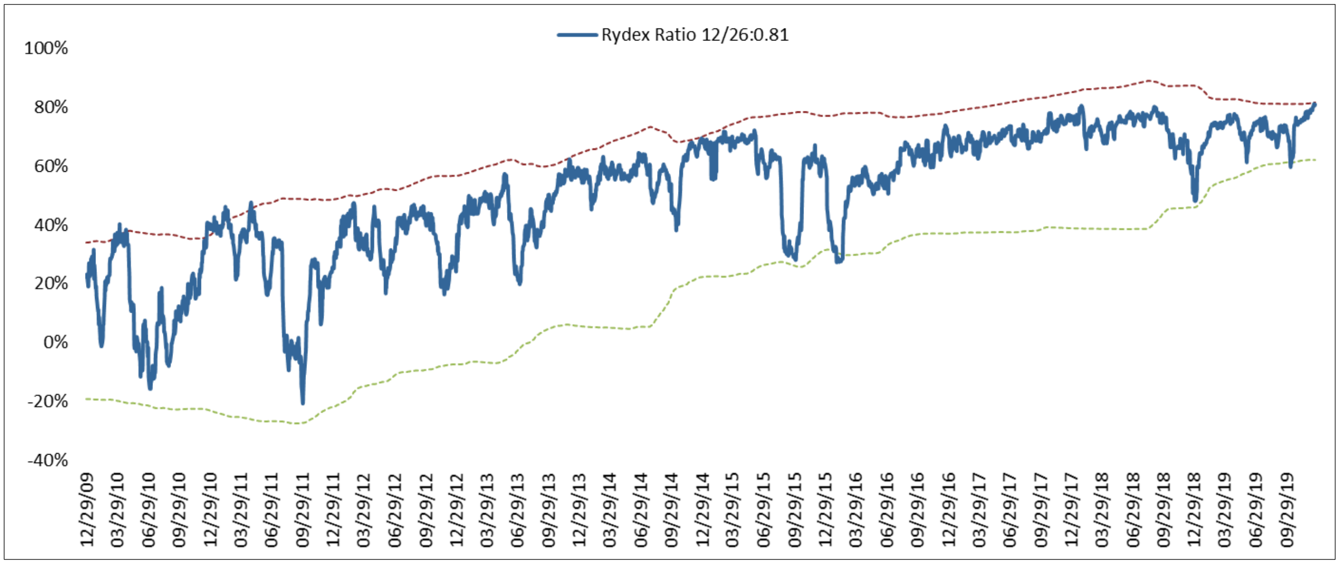
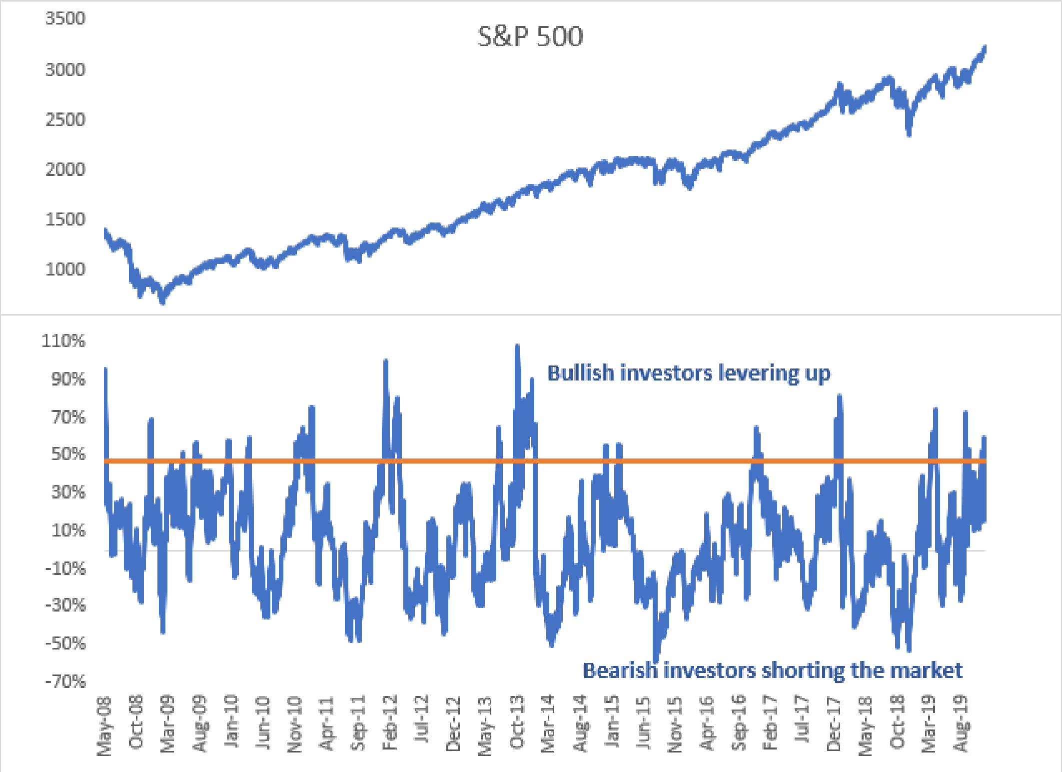


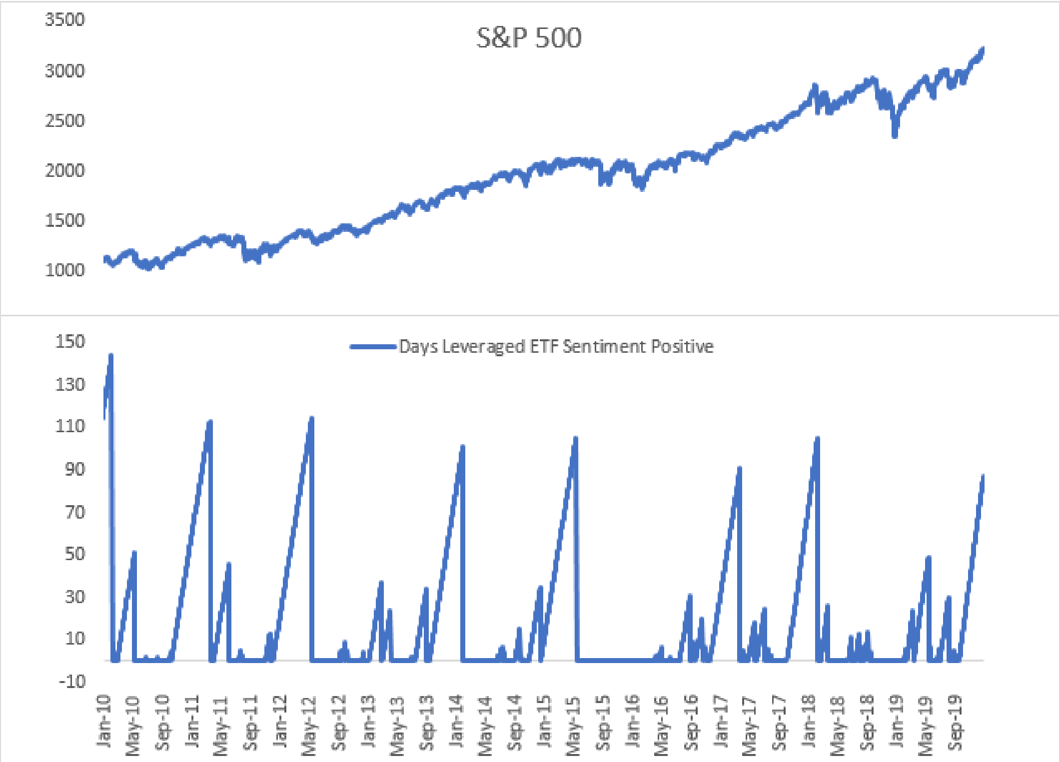
Chart – Levered ETF Sentiment continues to hit extremes



Source: Cypress Capital

Chart – Consecutive Trading Days with Positive Leveraged ETF Sentiment

This is the most length of positive sentiment from levered ETF investors since the January 2018 peak.



Source: Cypress Capital

Chart – Lowest Equity Put/Call readings since January/February 2018

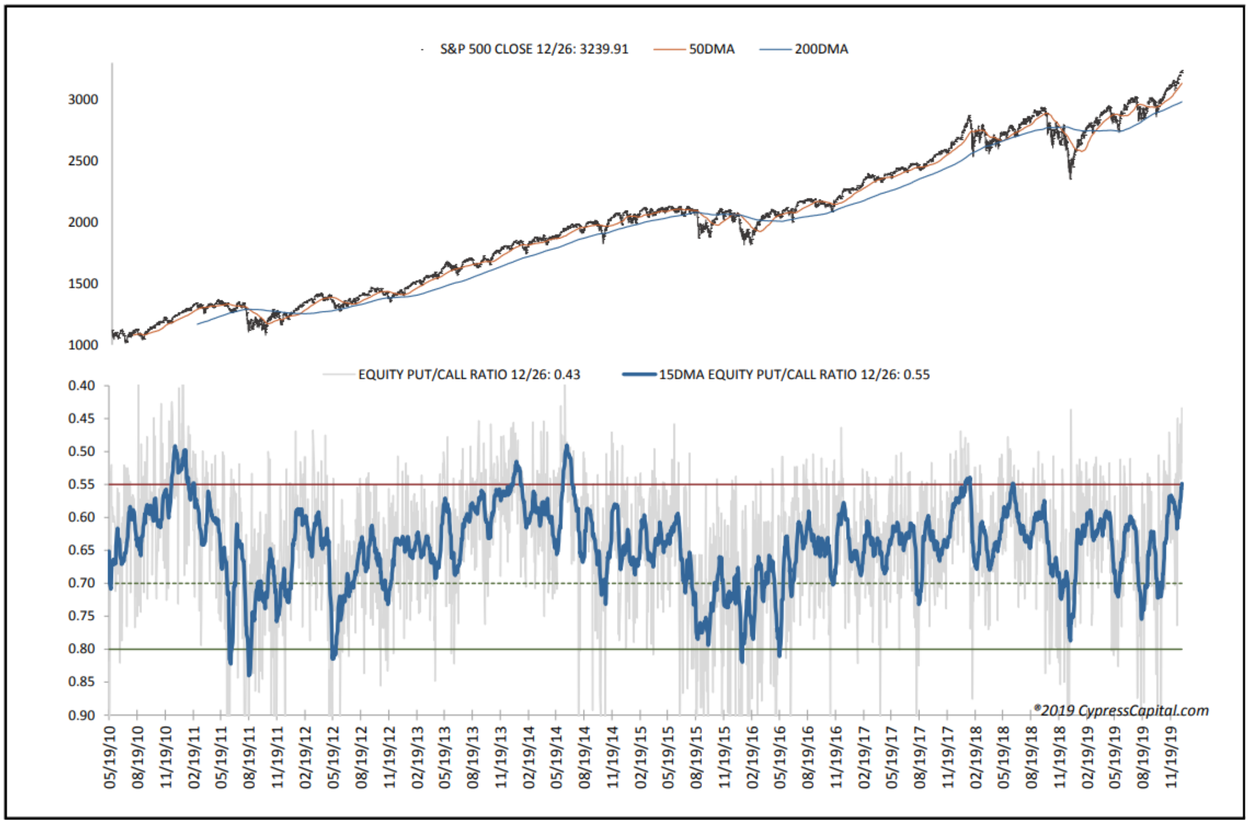
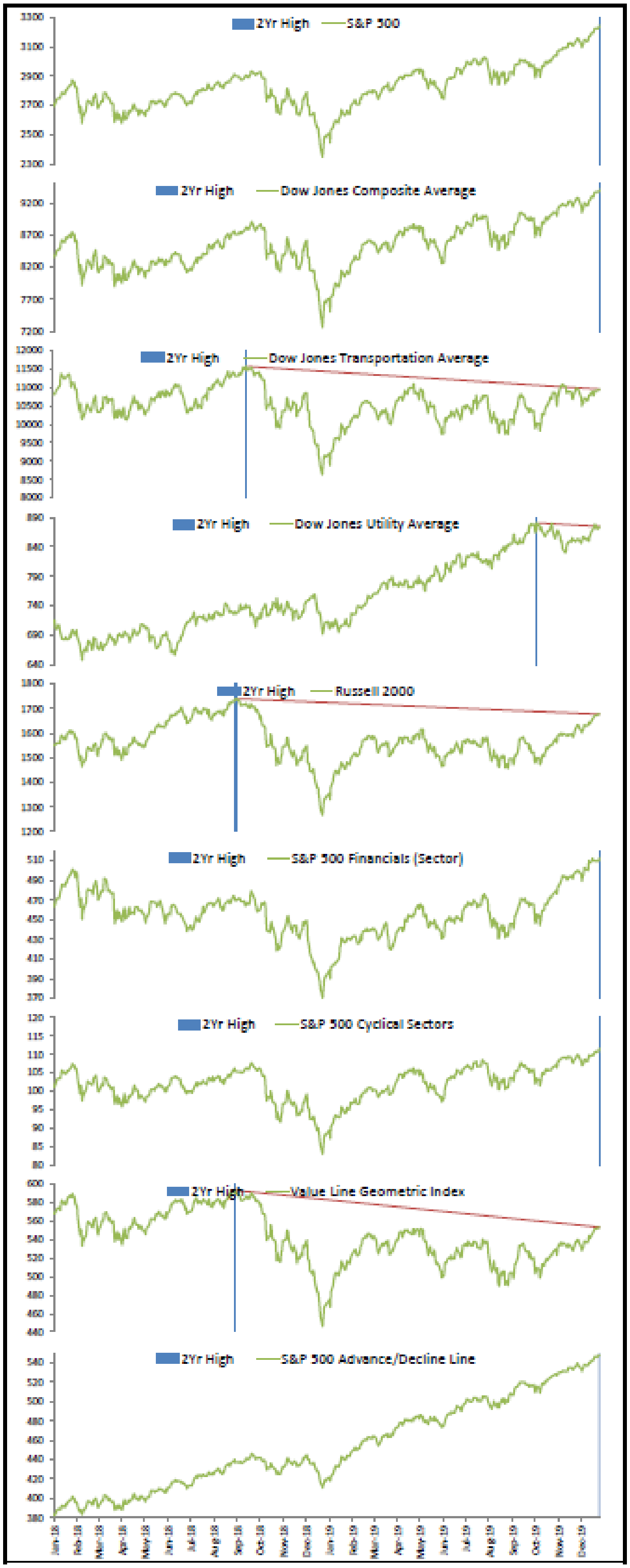


Chart – Breadth: Major Index Participation



Participation, in terms of indices making new highs simultaneously, has been improving for the first time since 2018. The Dow Transports, Russell 2000, and Valueline Geometric Index are the only key US indices yet to surpass their 2018 highs.

Asset Management – Portfolio Lineup

The essence of investment management is the management of risks, not the management of returns.
– Benjamin Graham

Select Dividend – Bottom up risk managed dividend portfolio of up to 40 stocks that can hold cash and fixed income when markets aren't presenting attractive individual equity opportunities. Portfolio built upon Cypress Capital's own metrics that measure dividend quality and safety. The portfolio is divided 75/25 into payers and growers. Payers are stocks with above average yields and a long-term history of paying dividends, where the dividend is perceived to be safe. Growers are companies with high total shareholder yields and perceived to be high quality, franchise companies. The portfolio is generally made up with familiar, household names.

Global Allocation – Multi-asset class portfolio that invests in low cost exchange traded funds across eight asset classes based upon the margin of safety offered by each asset class in an effort to avoid significant drawdowns.

Strategic Income – Disciplined, value biased income portfolio that practices patience in awaiting excellent risk reward opportunities in fixed income. Disciplined in its refusal to reach for yield and put capital at risk of permanent impairment.

Asset Neutral – Absolute return focused multi-asset class portfolio that allocates assets based upon the margin of safety offered in each asset class. Portfolio can go defensive and hold up to 100% cash in some environments.

US Opportunity – Concentrated value portfolio of up to 50 stocks that increases allocations to cash and fixed income when the margin of safety offered by equities is too narrow. Portfolio quantitatively buys the cheapest, highest quality stocks that it can find. Quantitative sell discipline sells individual holdings based on value and momentum factors.

Contact us for more information.