



# Market Outlook

By Mark T Dodson, CFA

## Highlights

Market Risk Index dropped to 90.9% on improving monetary conditions, but some of that improvement was offset by a new market cycle extreme in the psychology composite. To put the current reading in context, any MRI reading above 90% in a market still in a positive trend is incredibly rare and difficult to achieve without a lot of notable sentiment, economic and valuation extremes.

Monetary conditions managed to improve modestly on the drop in bond yields that has occurred over the last few weeks. In normal times, this drop in yields would result in more substantial improvement to our monetary score, but the drop in yields has also pushed the yield curve within a few basis points of being inverted again, neutralizing most of the improvement. The yield curve is back in territory that is precarious for the economy and stock market investors.

The lesson that central bankers learned from the Great Depression resulted in the post 2008 approach that we now call quantitative easing. Unfortunately, the book for what you do after quantitative easing hasn't been written yet. After the failed attempt to unwind it, it now sounds like the Fed is going to run some live experiments on monetary policy to try to generate some more inflation, using us as guinea pigs. If the experimentation works, and they manage to create more inflation in the prices of goods and services, stocks aren't currently priced for it. Regardless of how much experimentation the central bankers do, it's also going to be a tall feat to normalize the yield curve without asset prices taking a hit.

Investor psychology, in a surprise to us, managed to reach another cycle extreme. The Investor's Intelligence Survey, leveraged ETF sentiment, and a handful of indicators that measure market internals all moved in the wrong direction, pushing investor psychology further into uncharted territory for this bull market. The extremes in psychology are pervasive as well. Of the 11 categories of psychology indicators that we follow, only two score as modestly positive, Flow of Funds and Volatility, and volatility has begun losing points as a result of a pickup in stock market volatility. Flow of Funds is where we track buyback activity, and that has stayed positive the entire cycle, and this seems unlikely to change before the onset of a bear market.

### Market Risk Index

Elevated

90.9%

### Category Percentiles

Psychology - P6

98.3%

Monetary - M4

72.7%

Valuation - Extremely Overvalued

97.5%

Trend - Positive

3.9%

### Largest Psychology Influences

Volatility	Positive
Leveraged Investments	Negative
Option Activity	Negative
Surveys	Negative

### Largest Monetary Influences

GDP Growth (Below Avg)	Positive
Yield Curve	Negative
Velocity	Negative

### Valuation

7-10 Year Rtn Forecast	2.2%
10Yr Treas Yield (on 12/31)	1.9%

### Price Trends

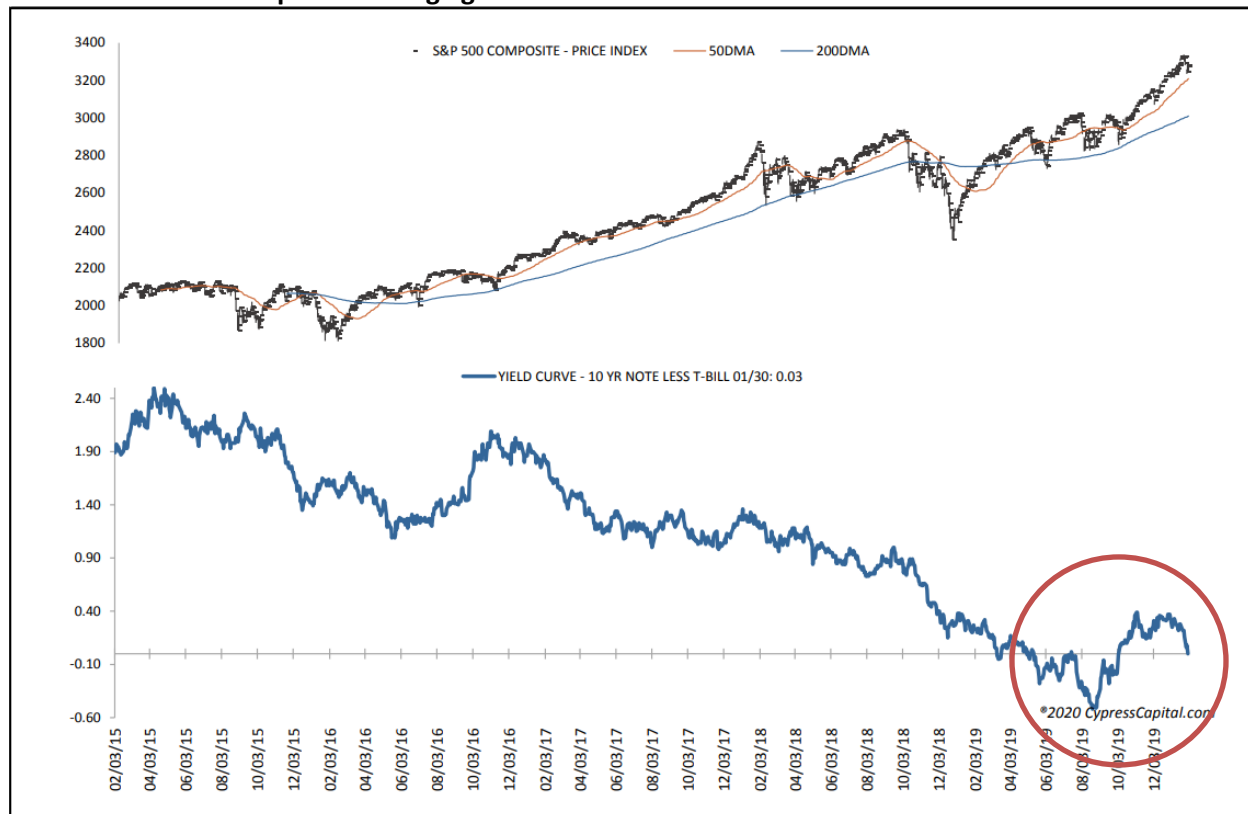
US Equities	Positive
Intl Equities	Positive
REITs	Positive
Broad Commodities	Negative

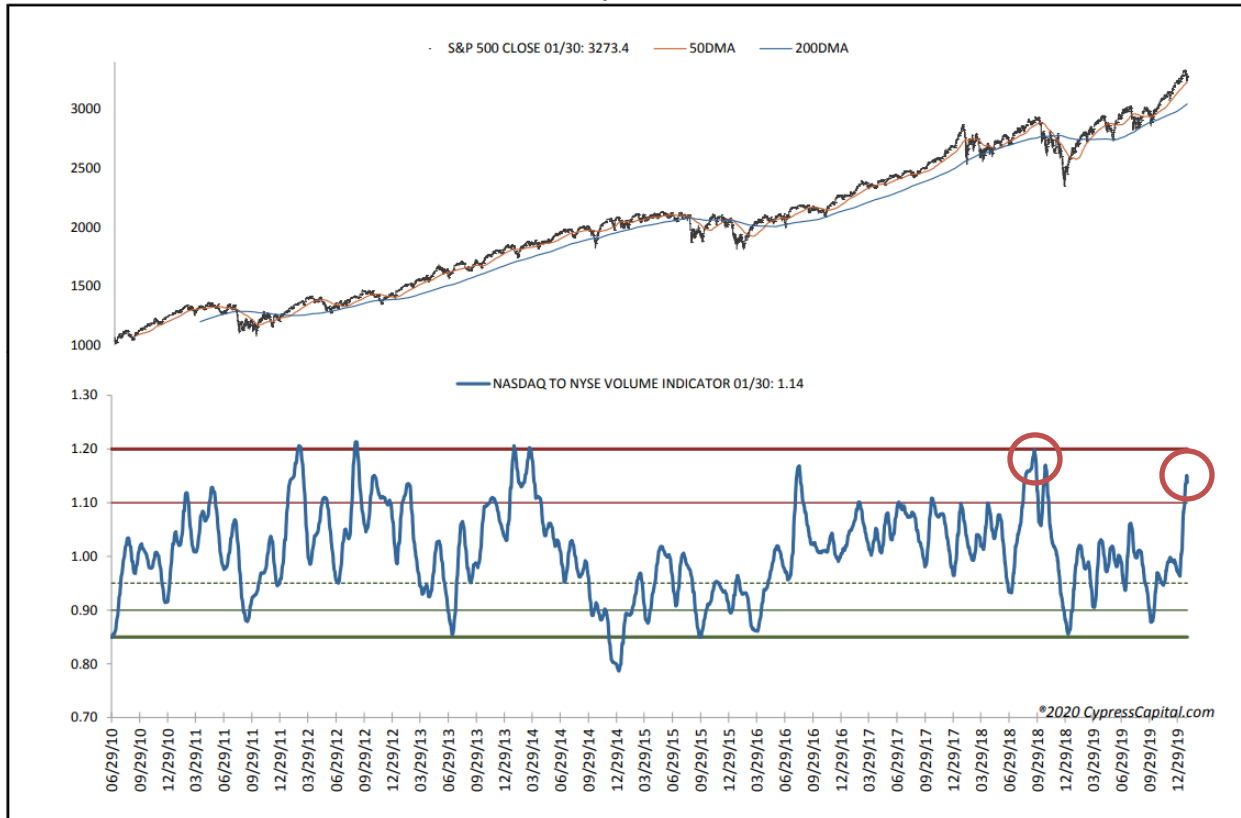
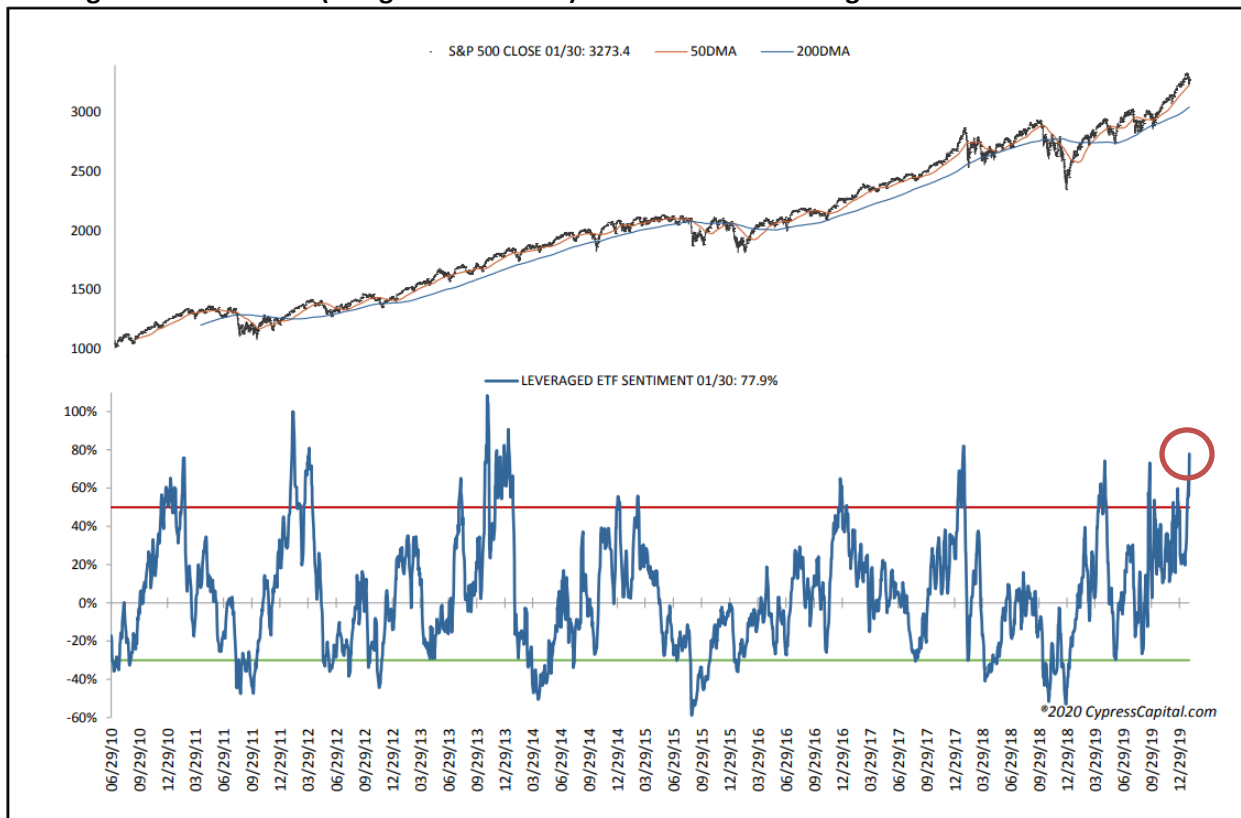
Market Risk Index scales from 0 to 100%. Higher readings correspond with higher risk markets. Scores below 25% are bullish. Scores between 25-75% are neutral, and scores above 75% are markets vulnerable to major drawdowns.

Coronavirus is understandably taking a lot of the blame for the market's recent weakness, but extremes in sentiment and valuations reached in the last month have suggested the market has been waiting on a catalyst for at least some kind of reset to investor euphoria.

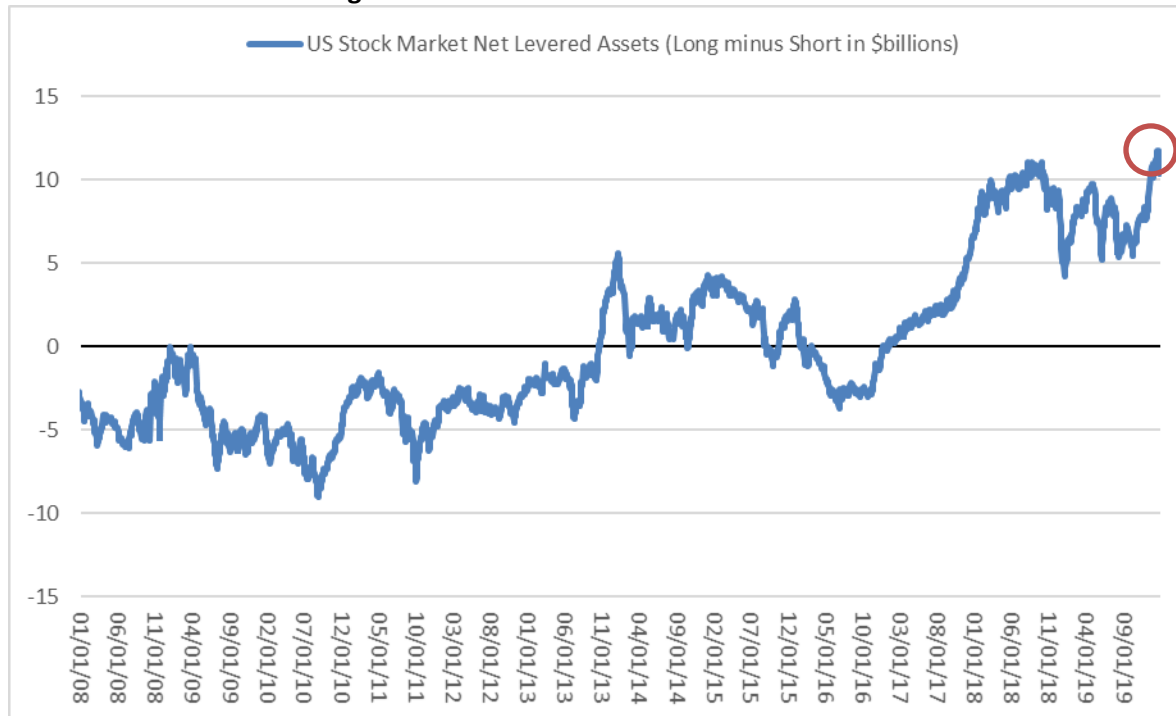
Note on price trends – our trend analyzer for broad commodities turned down, continuing a pattern of false starts for commodities that has been ongoing for most of this market cycle. This has been one of the worst cycles for commodity returns ever, and the sideways market for the last four years in commodities has been doubly painful for pure trend followers. That seems unlikely to change until the current stock market cycle ends. We still recommend investors keep a bias toward gold here – we initiated a position in the precious metal last spring.

### Yield Curve on the cusp of inverting again



**NASDAQ to NYSE Volume Indicator hit its first euphoric extreme since Fall 2018****Leveraged ETF Sentiment (using dollar volume) broke out to a new high**

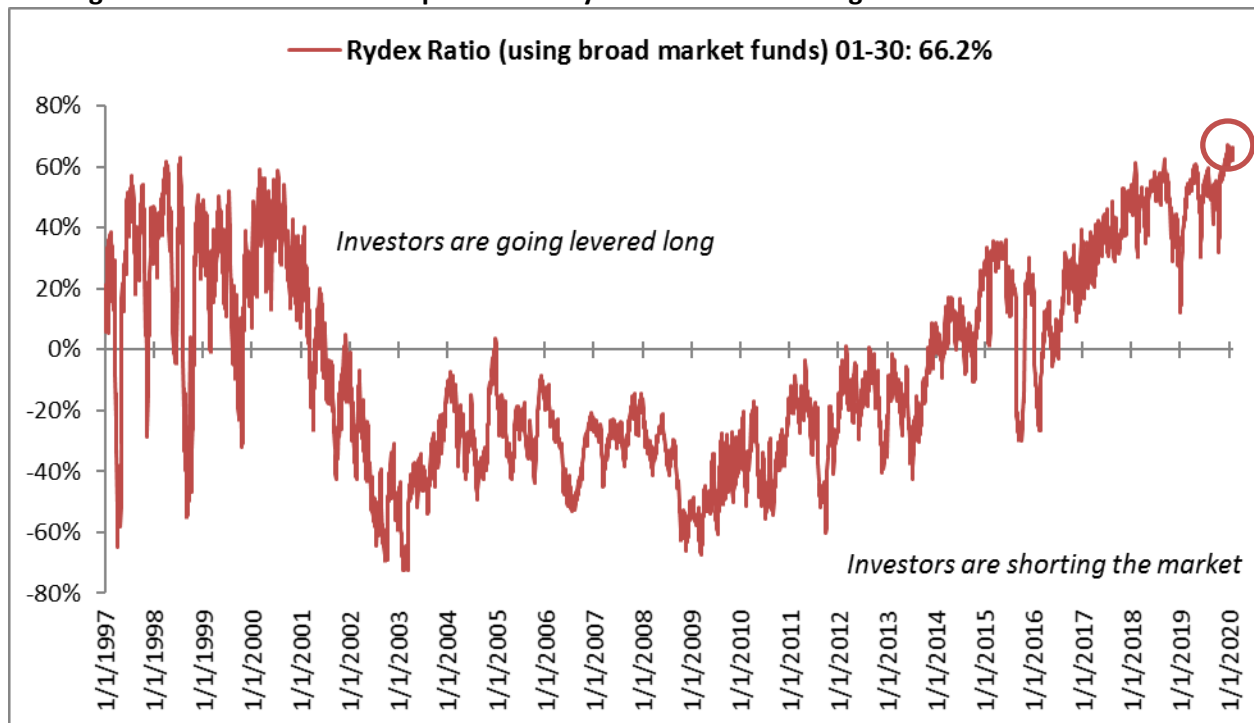
### Net US Stock Market Leverage reached a new record this month



Calculation includes levered and inverse funds (Rydex, Direxion, Proshares) and Margin Debt

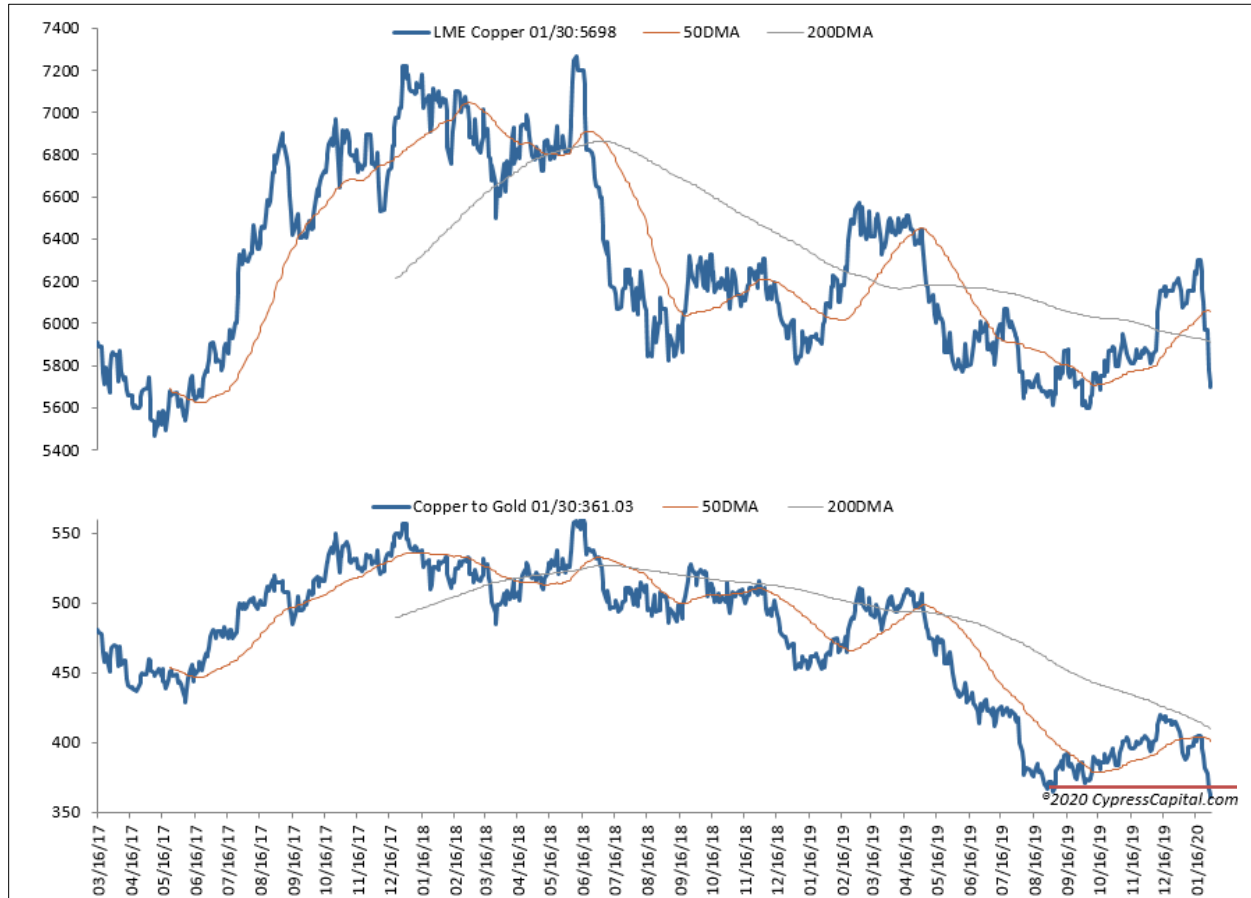
Source: Cypress Capital

### Leveraged Mutual Fund Investors pushed the Rydex Ratio to 20 Yr. highs this month



**Sharp drop in copper prices – Copper to Gold ratio makes a lower low**

Our favorite economist, Dr. Copper, is growing more cautious.



## 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.

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