



Market Outlook

By Mark T Dodson, CFA

Highlights

Market Risk Index jumped to 91.2% on another record extreme from our psychology composite – the worst reading since October 2000. The monthly releases from ICI's trends in mutual fund investing and the Conference Board's Consumer Confidence survey pushed the risk score for Psychology higher. Consumer Confidence bounced, and mutual fund cash levels dropped to super low levels. Even option activity managed to set new records again with hedging activity from smart money OEX option traders surging further into all-time high territory.

Jobs numbers released this morning surprised to the upside, but of the 100 plus indicators and metrics that we incorporate into Market Risk Index, this isn't one of them. In part, because it's a lagging indicator and also because the series can be revised so much – numbers from 2019 were revised down by half a million jobs from the headline numbers.

Instead, Consumer Confidence data on the job market is a better indication of stock market drawdown risk. These series aren't really subject to much revision (except for the most recent month). It's soft data, but it captures the economic mood and intensity of animal spirits. When the public is too excited about job prospects, it's usually the best of economic times, and stock market returns suffer. At the close of January, consumer confidence in the job market hit the highest level since December 2000. Many of the responses from the Consumer Confidence survey are highly correlated, and as you can guess, most climbed in January and are near levels from 2000.

The last few volatile weeks have thrown a wrench in the works of this momentum market, but the Trillion Dollar Club (Google, Amazon, Microsoft, and Apple) managed to throw their trillion dollar weight around and push the cap-weighted indices to new highs this week. Now, similar to when we saw the psychology extremes in January 2018, we start the clock looking for clues from breadth and other key market indices on the likelihood of the high print for 2020. International equities and within US markets, the Valueline Geometric index and Dow Transports, have been unable to participate in new highs during January's momentum surge, but markets have been ignoring those warnings for some time, so we are looking for a broader set of clues.

Breadth and timing aside, the baskets of indicators that we follow were chosen purely for their statistical efficacy historically, without an agenda, mostly with the Warren Buffett's Rule #1 mandate in mind - don't lose

Market Risk Index

Elevated

91.2%

Category Percentiles

Psychology - P6

98.7%

Monetary - M4

72.7%

Valuation - Extremely Overvalued

97.5%

Trend - Positive

0.2%

Largest Psychology Influences

Flow of Funds (Buyback activity)	Positive
Leveraged Investments	Negative
Option Activity	Negative
Consumer Confidence	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%

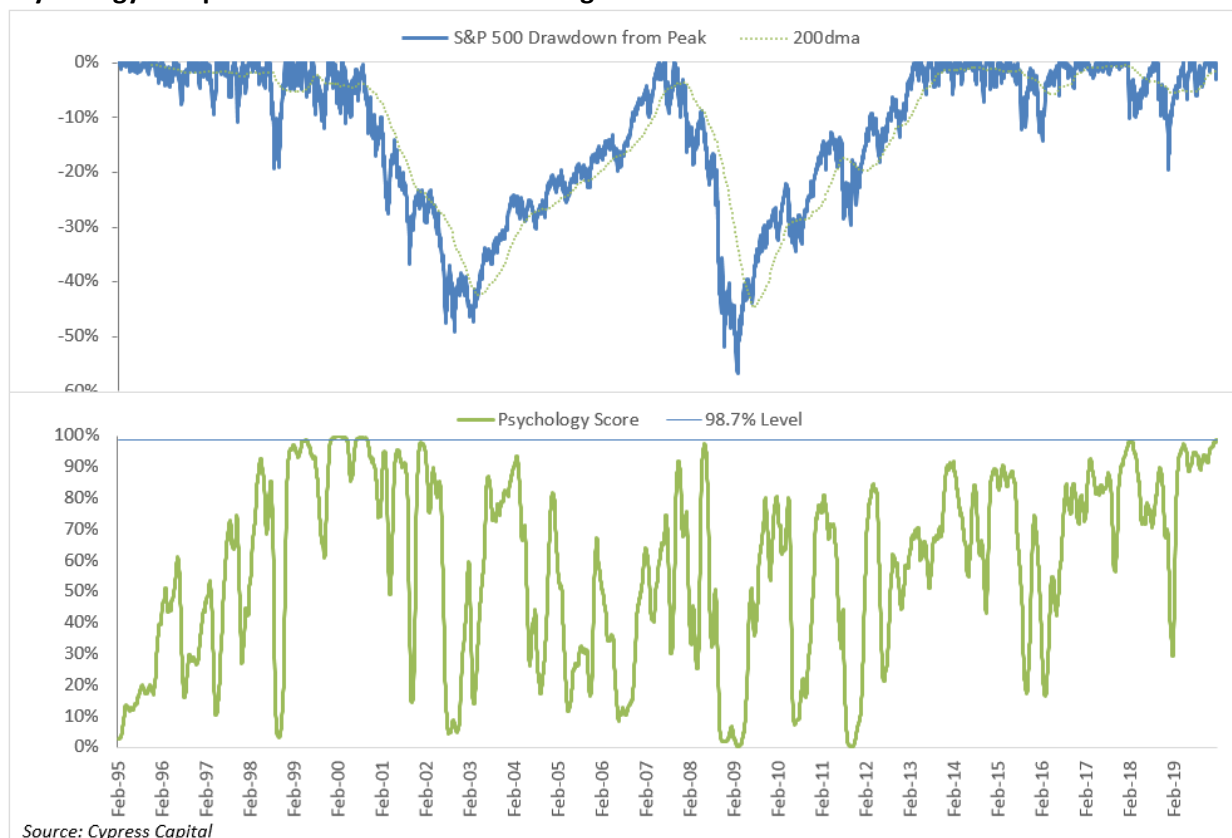
Price Trends

US Equities	Positive
Intl Equities	Positive
REITs	Positive
Broad Commodities	Negative

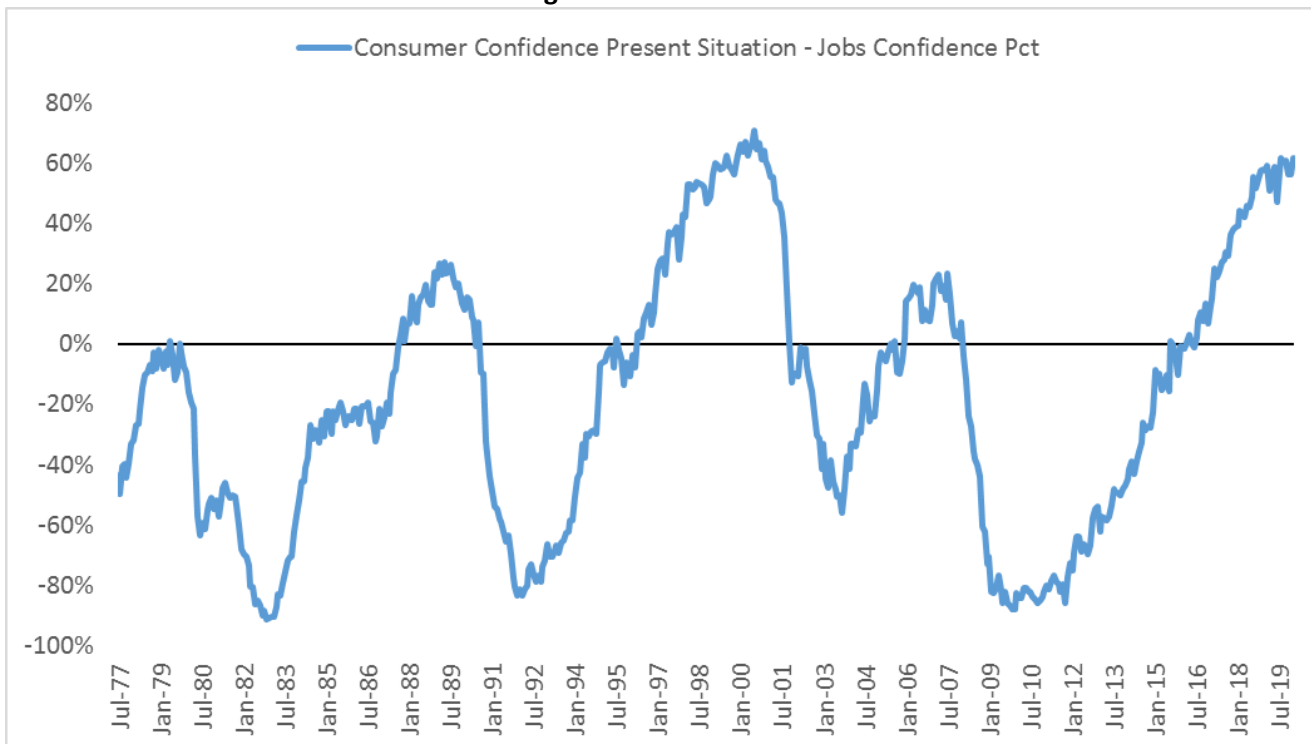
Market Risk Index scales from 0 to 100%. Higher readings correspond with higher risk markets. Scores below 25% are bullish. Scores between 25-75% are neutral, and scores above 75% are markets vulnerable to major drawdowns.

money. With the extremes that we are seeing in psychology and valuations, a number of which are record level extremes, this isn't a good time to be initiating positions in the stock market.

Psychology Composite reached its worst reading since October 2000



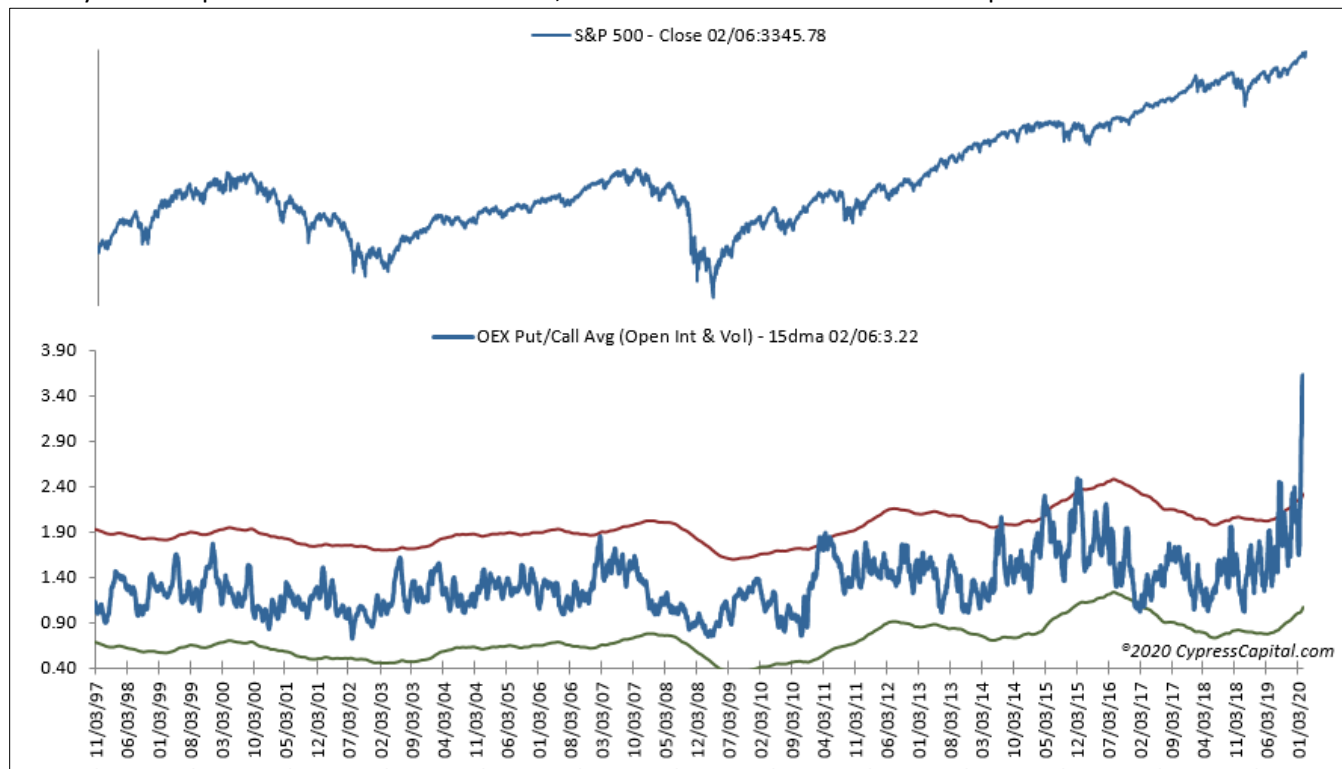
Consumers Confidence in Job Market is at highest levels since December 2000



Source: Conference Board, Cypress Capital

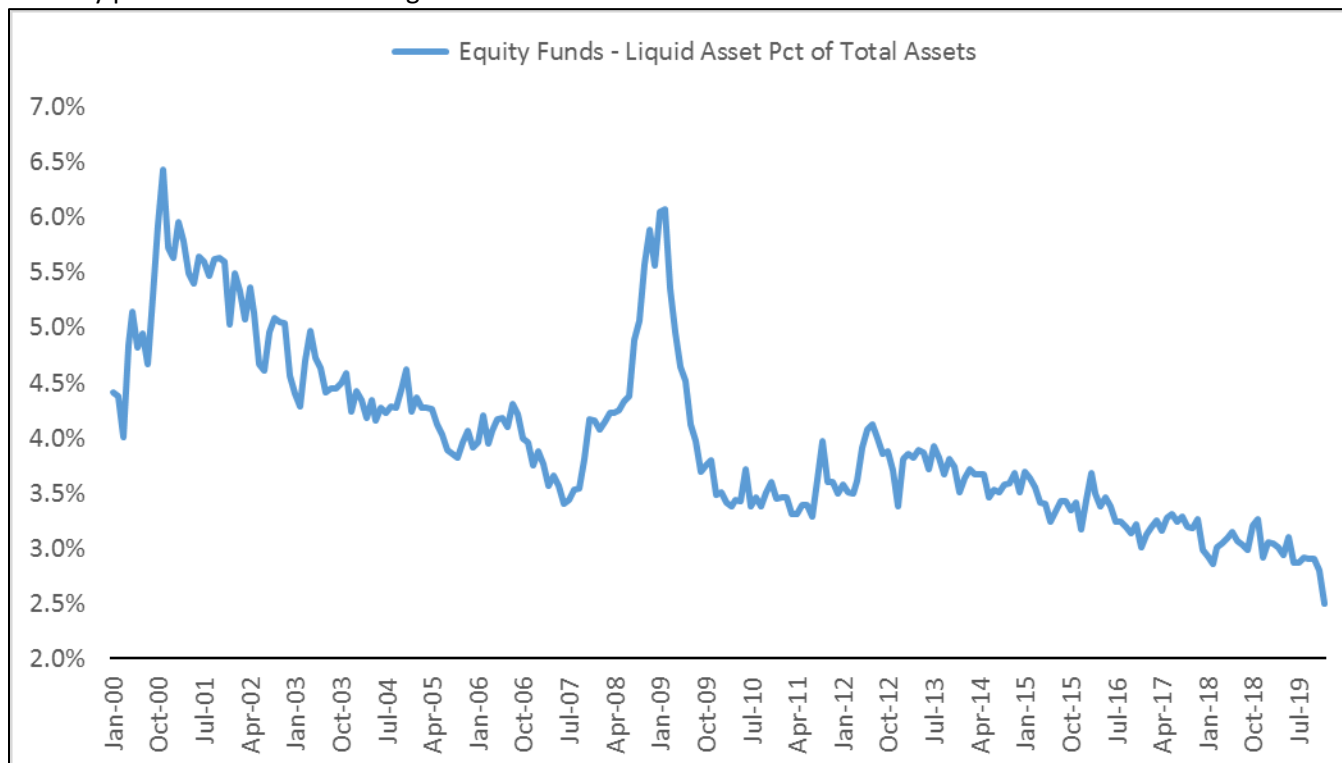
OEX Put/Call readings continued to set new all-time records in hedging activity

Activity in OEX options isn't what it used to be, nonetheless these extremes are impressive.



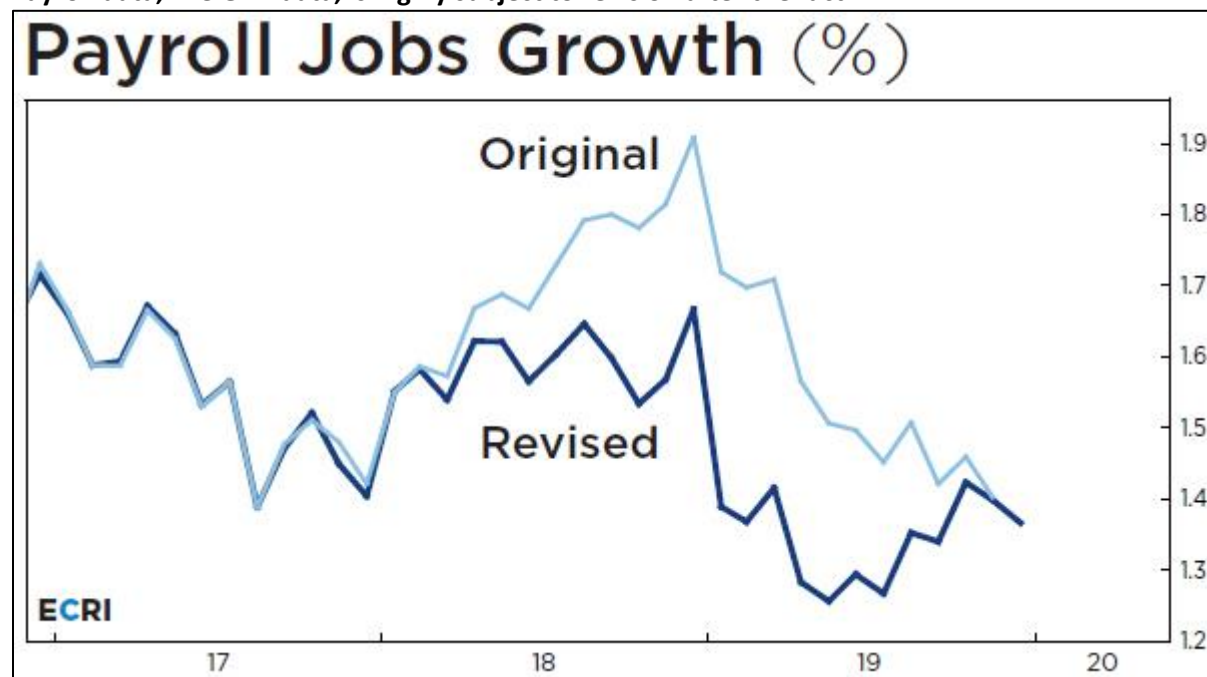
Cash Levels in Equity Mutual Funds drops to all-time lows

The simplest short-term way for a mutual fund manager to protect a career when passive cap-weighted indices are leading is to hold as little cash as possible. Both mutual funds and individual investors are setting aside very little dry powder. FOMO is running hot.



Source: ICI, Cypress Capital

Payroll data, like GDP data, is highly subject to revision after the fact



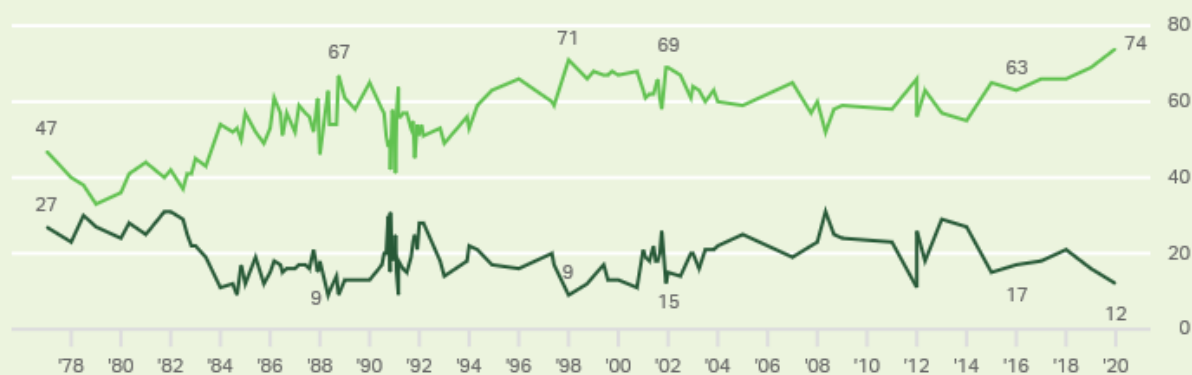
Source: ECRI

Gallup Poll reveals All-Time Record Financial Confidence by the American Public

About Three in Four U.S. Adults Say They Will Be Better Off Financially Next Year

Looking ahead, do you expect that at this time next year you will be financially better off than now or worse off than now?

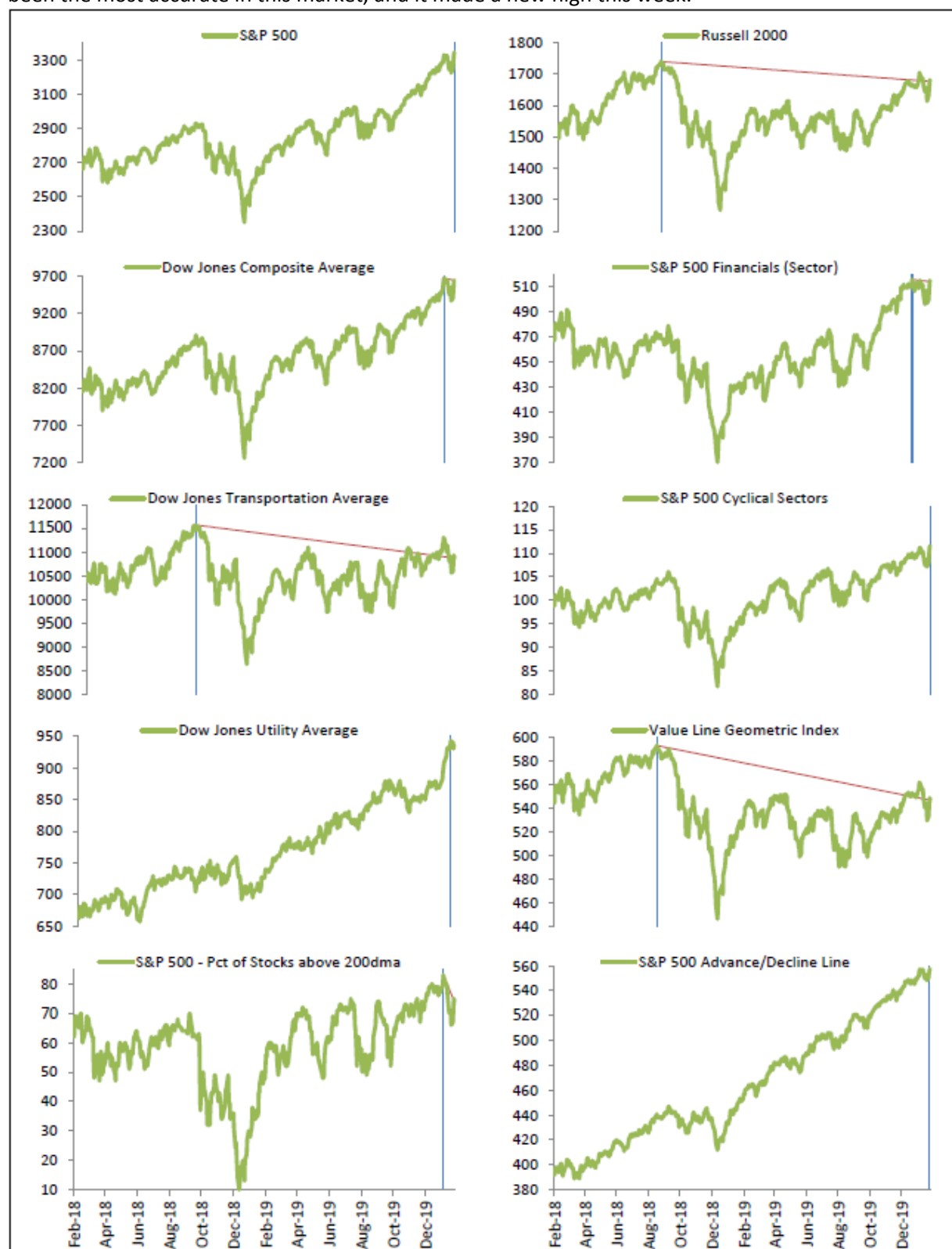
■ % Better off ■ % Worse off



GALLUP

Stock Market Breadth

The Dow Transports, Russell 2000, and Valueline Geometric averages have been the fly in the ointment for this market's Dec-Jan momentum rally. With the first stumbling blocks to the S&P 500's momentum occurring over the last couple of weeks, the count begins for nascent signs of waning breadth. The advance decline line has been the most accurate in this market, and it made a new high this week.



Source: Cypress Capital

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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