



Market Outlook

By Mark T Dodson, CFA

Psychology crosses into the worst decile of readings

Both monetary and psychology conditions deteriorated and pushed Market Risk Index up to 84%. It is the highest reading since mid-March when MRI was beginning a move lower after its ultimate peak on February 24, 2020. This the quickest our MRI has hit elevated levels like this so soon after a bear market. It's a process that is normally measured in years, not months.

Our psychology composite has broken into the worst decile of readings, a level that denotes markets with acute levels of enthusiasm. It requires a broad swath of indicators to hit extremes simultaneously – a pervasive move of indicators. The Levered Investments category surged enough in the last week to push the composite over that 90% threshold, as dollar volume flowing into levered relative to inverse ETFs climbed to the highest level since February 24th. The current reading on that indicator is in the worst 2 percent of all readings going back to 2006, when levered and inverse ETFs were first brought to market.

One category that remains unusually neutral is Surveys. Professional investors are enthusiastic, while the pessimism of individual investors widened. This is the widest disparity between the two groups of investors that we have ever seen. AAI's weekly survey is also the biggest anomaly within the psychology composite.

There are still no signs of our monetary composite making a strong push into a favorable environment because the yield curve continues to stay around 40-50bps wide, and uncertainty among the public is keeping money demand running hot (and velocity low).

Our eyes are glued to the dollar here. If the pace of its current decline persists, it could become uncomfortable for the Fed. Meanwhile, the falling dollar has coincided with TIPs yields falling below their previous all-time lows and a sharp move higher in commodity prices, but without any corresponding move higher in nominal US Treasury yields. It's early yet, but this is a stag-flationary combination of price moves.

Short-term correlations between the dollar and asset classes are also running unusually high, so a short-term dollar rally from these oversold levels would likely correspond with a correction for several asset classes, and a delay in govt stimulus could be a catalyst. Likewise, should the dollar's decline persist, this overvalued, frothy momentum market could get frothier.

Market Risk Index

Elevated

84.0%

Category Percentiles

Psychology - P6



Monetary - M4



Valuation - Extremely Overvalued



Trend



Largest Psychology Influences

Volatility	Positive
Fund Flow s	Negative
Option	Negative
Leveraged Investments	Negative

Largest Monetary Influences

Falling Yields	Positive
Monetary Aggregates & Velocity	Negative
Yield Curve	Negative

Valuation

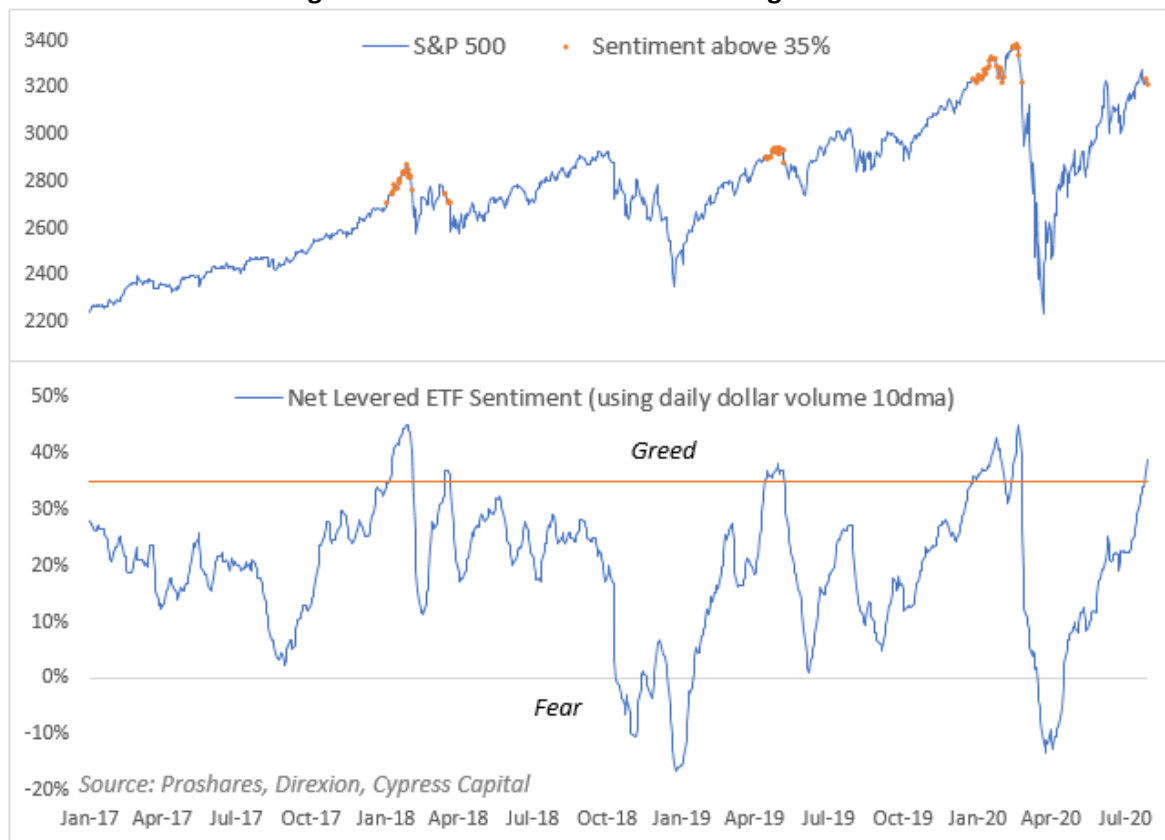
7-10 Year Rtn Forecast	1.7%
10Yr Treas Yield (on 07/28)	0.6%

Market Trends

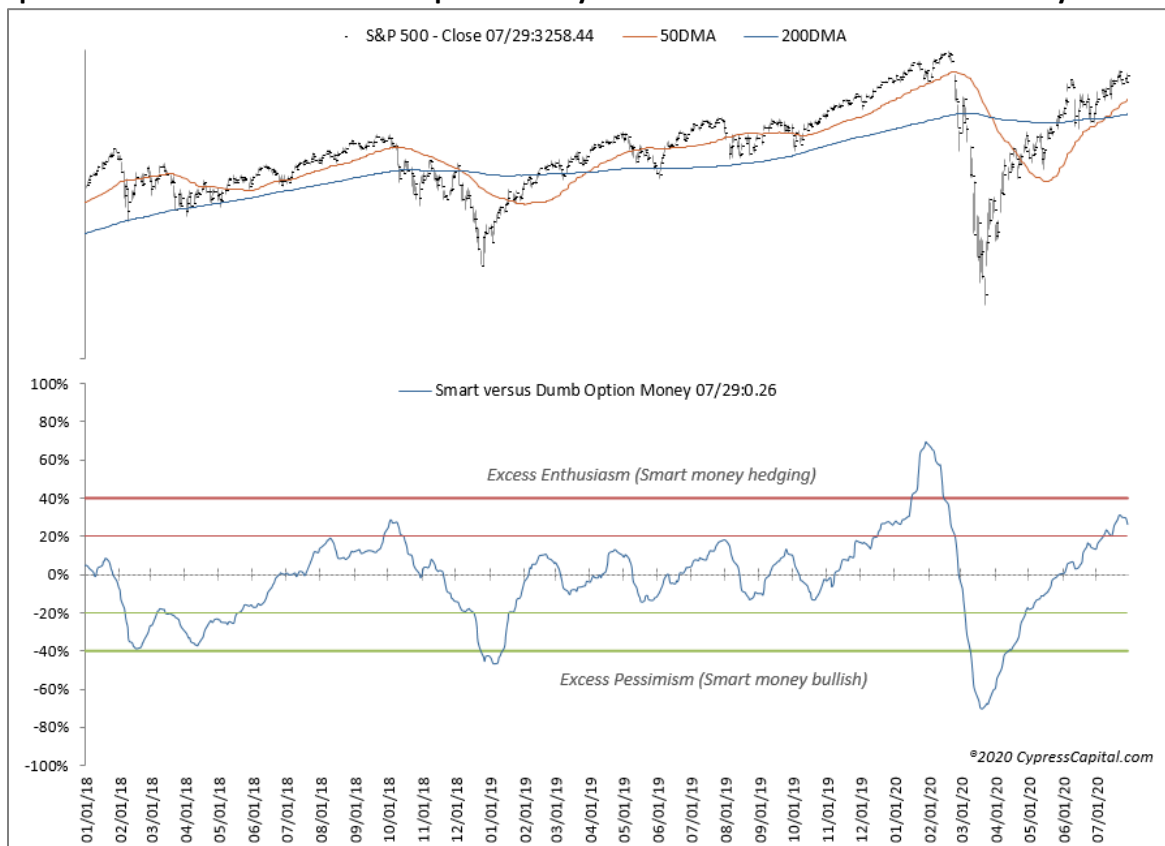
US Equities	Bullish
Intl Equities	Bullish
REITs	Neutral
Broad Commodities	Bullish

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.

Net dollar volume flowing into Levered vs Inverse ETFs is hitting extremes.

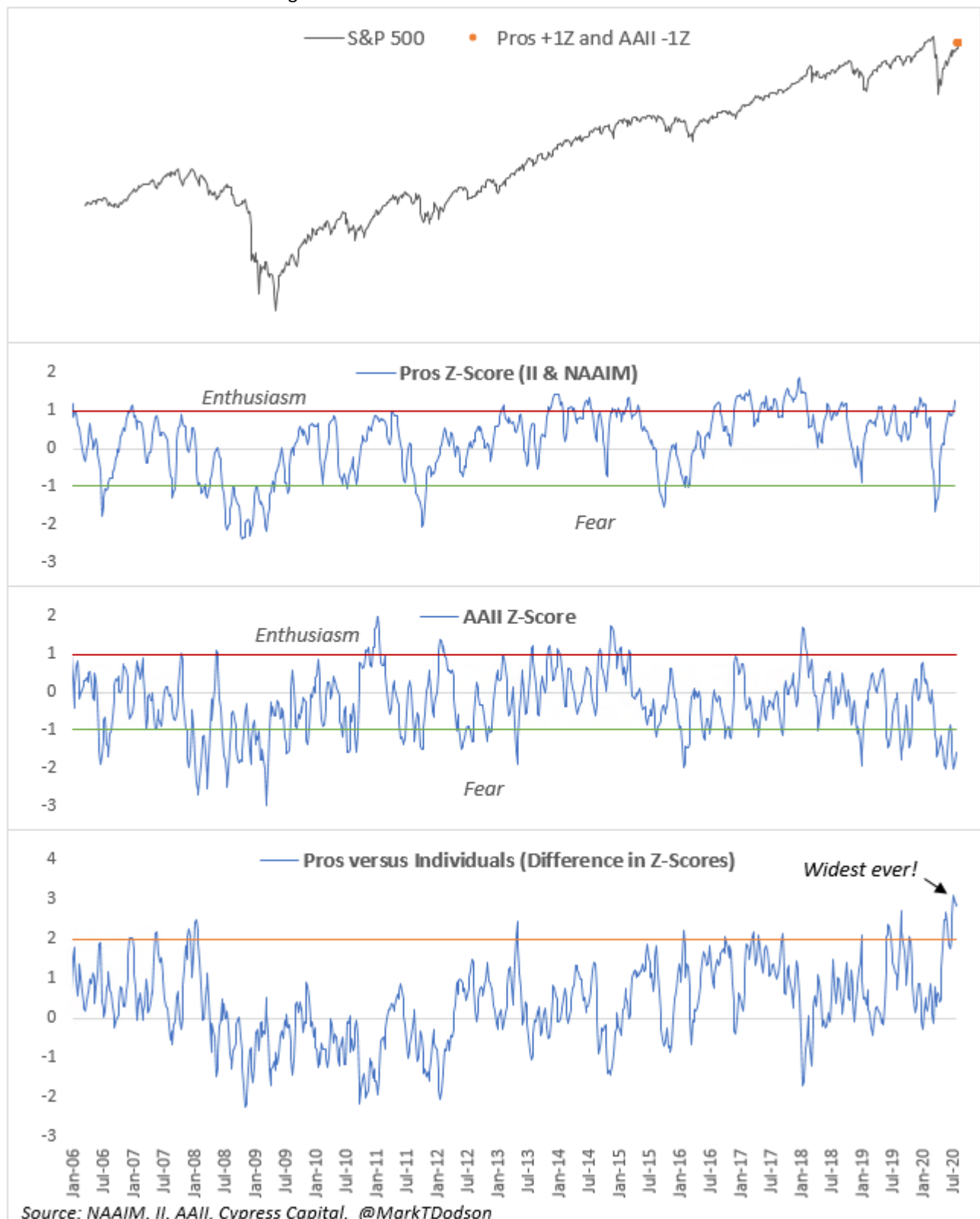


Spread between smart and dumb option money widened further into extreme territory



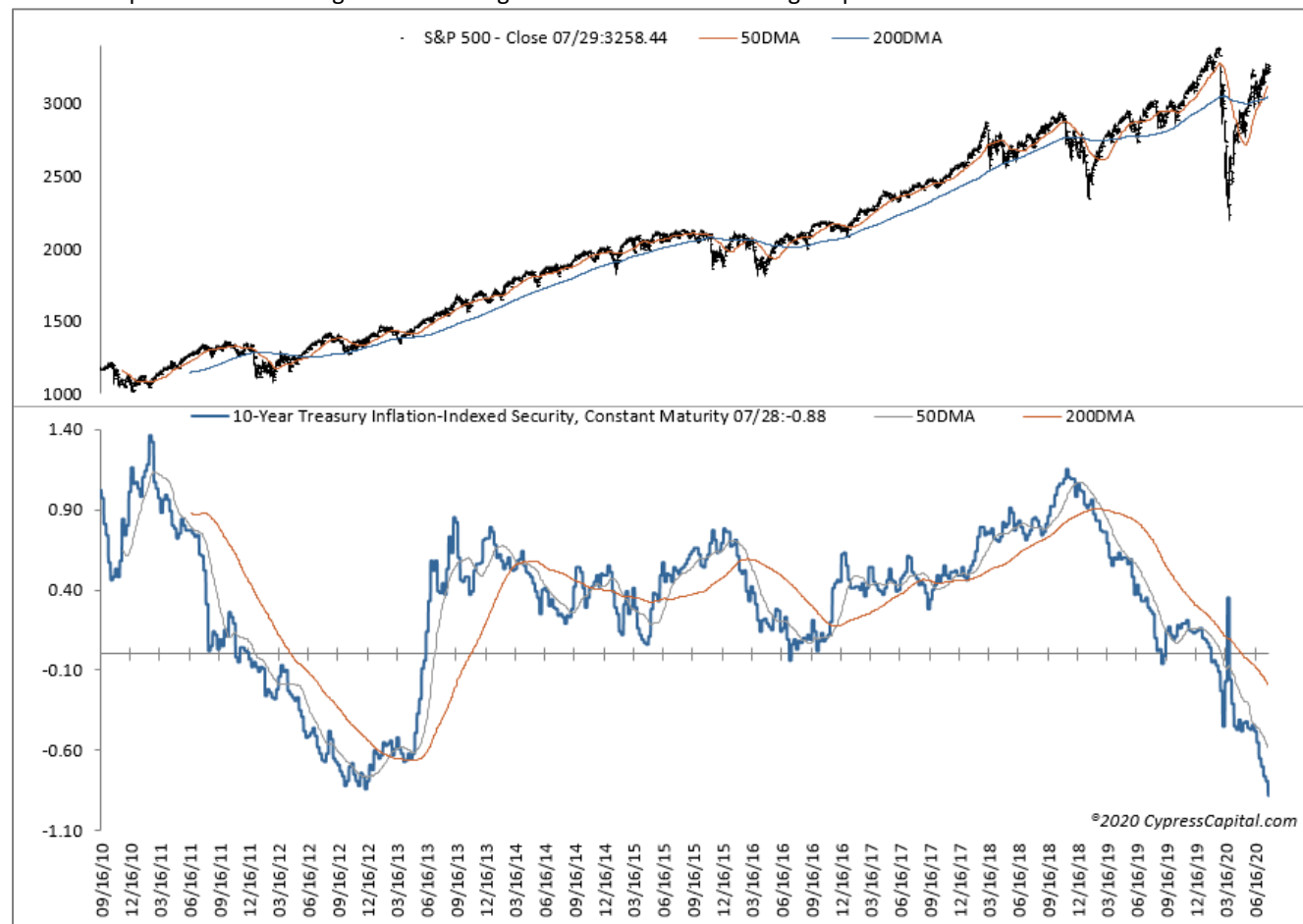
Record spread between Professional and Individual investor sentiment

Both the Investor's Intelligence survey and the NAAIM equity exposure survey of advisors are over 1 standard deviation into enthusiasm territory. Meanwhile, individual investors are hitting an extreme in the other direction. Pros have never been this bullish while individuals were this pessimistic. These are all contrarian indicators, but one group is going to prove smarter than the other over coming months.

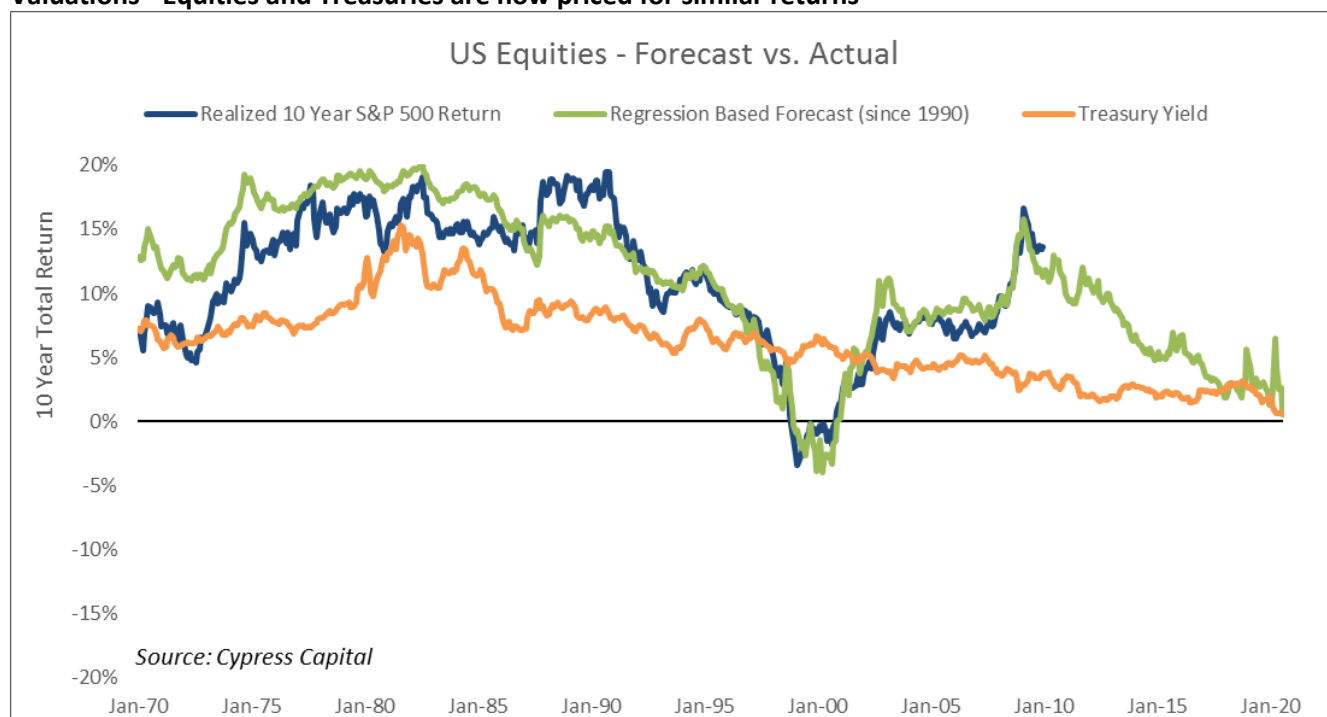


TIPS yields have fallen to new lows

Inflation expectations are rising with the falling dollar. You can see it in higher prices of commodities and TIPS.



Valuations - Equities and Treasuries are now priced for similar returns

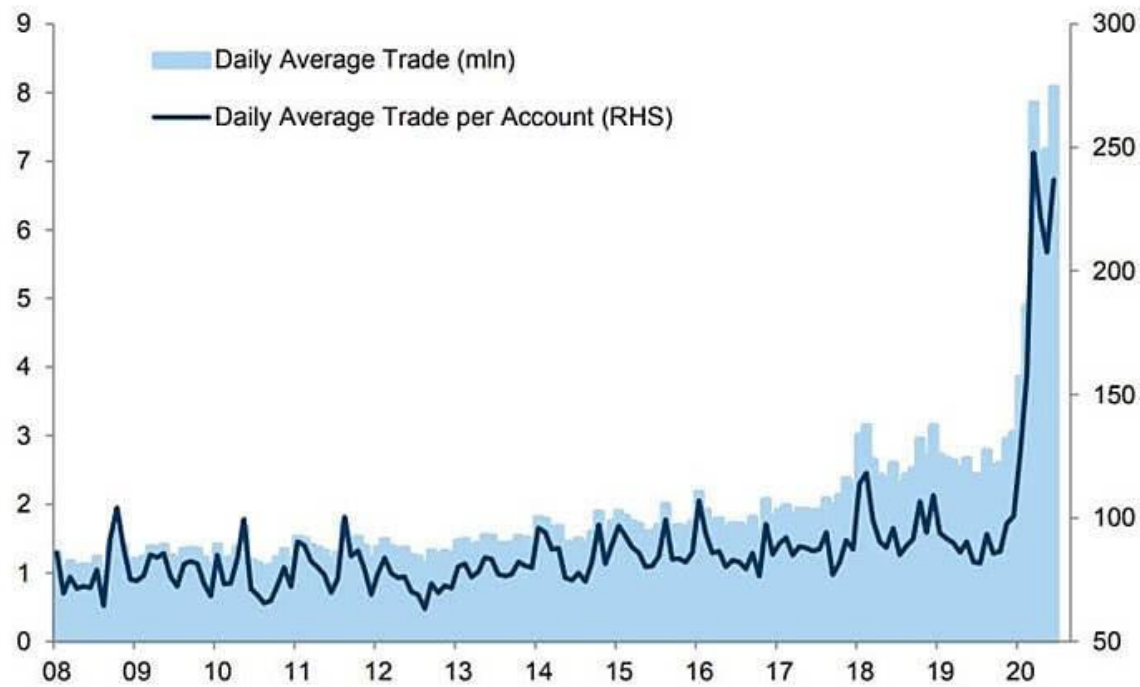


Still no signs of Retail Investors backing off their enthusiasm for day trading

This enthusiasm for day trading is a different message than the one coming from AAI's survey, but as we've mentioned ad nauseum, that survey is measuring a different generation of investors.

Exhibit 3: Retail investor activity remains very elevated

US online brokers retail trades



Source: Company data, Goldman Sachs Global Investment Research

Homeownership climbs to the highest since 2008

It's not only equities that young investors are buying, it's homes too.

Homeownership Boom

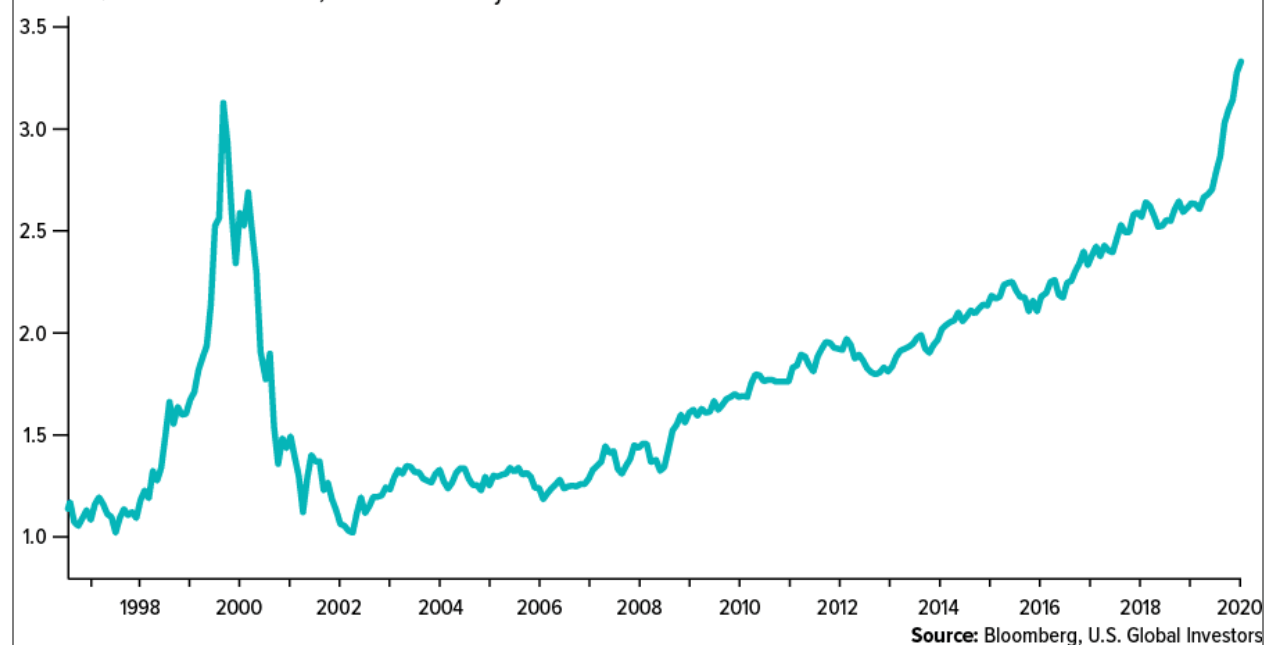
The U.S. rate jumps to the highest level since 2008



Source: Census Bureau/Bloomberg

Ratio of NASDAQ 100 to S&P 500 is higher than in 2000**Tech Stocks Now More Overvalued Relative to the Market Than During Dotcom Bubble**

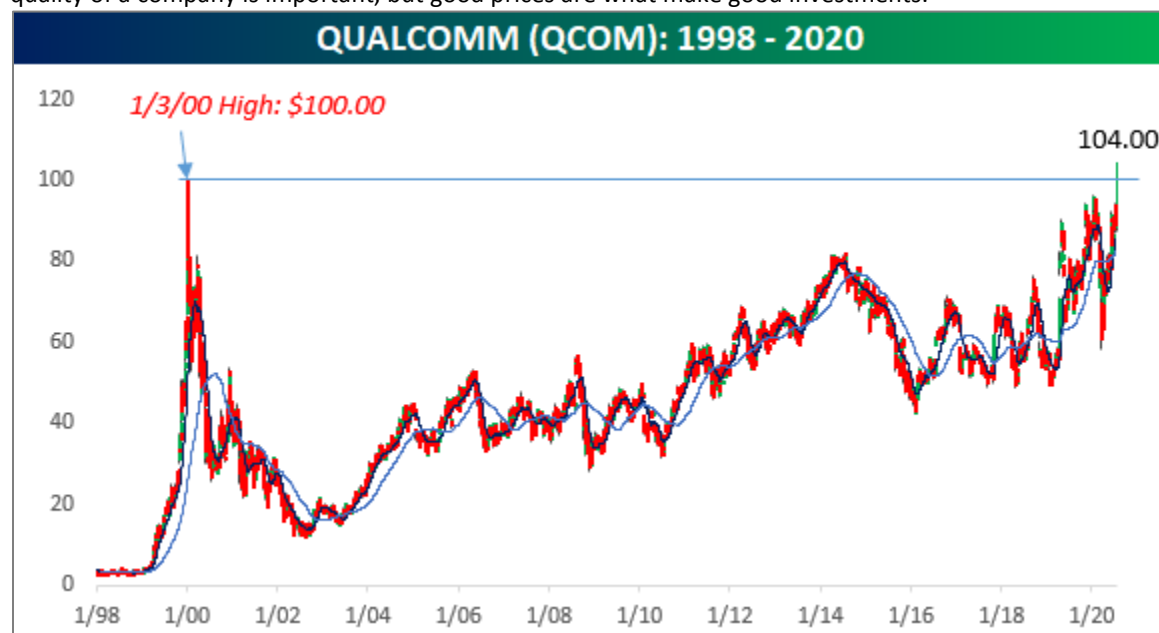
NASDAQ 100 Index/S&P 500, Jan. 1997 – July 2020



Source: Isabelnet

Qualcomm Breaks Even

If you bought QCOM when the chart above was last peaking, you finally broke even on your investment this week. The quality of a company is important, but good prices are what make good investments.



Source: Bespoke

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.