



# Market Outlook

By Mark T Dodson, CFA

## Psychology Crosscurrents

Market Risk climbed to 88.4% on a slight bump in the monetary composite risk score. Both psychology and Valuation stayed at the 100<sup>th</sup> percentiles for the second week in a row.

There were a couple of conflicting signals in the psychology composite this week. Our detrended version of the equity put/call ratio (3-39wk avg) triggered a significant buy signal, but there was also a key sell signal on the NASDAQ High Low Logic Index. The latter, which only gives sell signals when too many highs and lows are occurring at the same time, gives us more evidence of a bifurcated market as well as a sign that fiery animal spirits are beginning to waver. Still, having seen the last 4-5 years produce an abnormally large number of these signals, we'd be more alarmed about it if NASDAQ High Low Logic crossed above 6, or its cousin, the NYSE version, also triggered a sell signal.

The same can be said for our detrended version of the equity put/call ratio. This method came about after the late 90s spent considerable periods with the public locked in a euphoric mindset. That buy signal could coincide with the start of a short-term summer rally, but it doesn't indicate a rebuilding of the wall of worry. The 15-day moving average of the equity put/call ratio just this week began to leave greed territory, so the detrended version would simply be signaling this is the point where we see a resurgence in greed. It's what bulls should hope for because a shift to a more risk-averse mindset implies a more severe correction from here.

The collapse in Bitcoin, a proxy for excess speculation, has us leaning toward the latter. A 45% drop over five weeks is the kind of collapse that can serve as a wake-up call for investors who saw every speculative investment through rose-colored glasses. Elon Musk/Bitcoin made the most headlines for Bitcoin this week, but with time, investors will likely look back at the crypto-ransomware payment for the Colonial pipeline as more consequential. It could mark the point where the government began to perceive, rightly or wrongly, cryptocurrencies as more of a national security risk.

Speculative sentiment across financial markets is still very high by historical standards. Measuring the level of speculative fervor might be relatively easy, essential for risk management, but forecasting when it will turn isn't. Should we see another levered push by speculators, the message coming from our monetary composite leaves us confident that there will remain a growing inflationary narrative serving as a headwind for markets that will last for many months.

### Market Risk Index

Rec Allocation 25% Underweight

**88.4%**

### Category Percentiles

Psychology - P6



Monetary - M4



Valuation - Extremely Overvalued



Trend



### Largest Psychology Influences

Levered Investments	Negative
Flow of Funds	Negative
Volatility	Negative
Technicals	Negative

### Largest Monetary Influences

Inflation	Negative
Interest Rates	Negative
Velocity	Positive

### Valuation

7-10 Year Rtn Forecast	-0.7%
10Yr Treas Yield (on 05/18)	1.6%

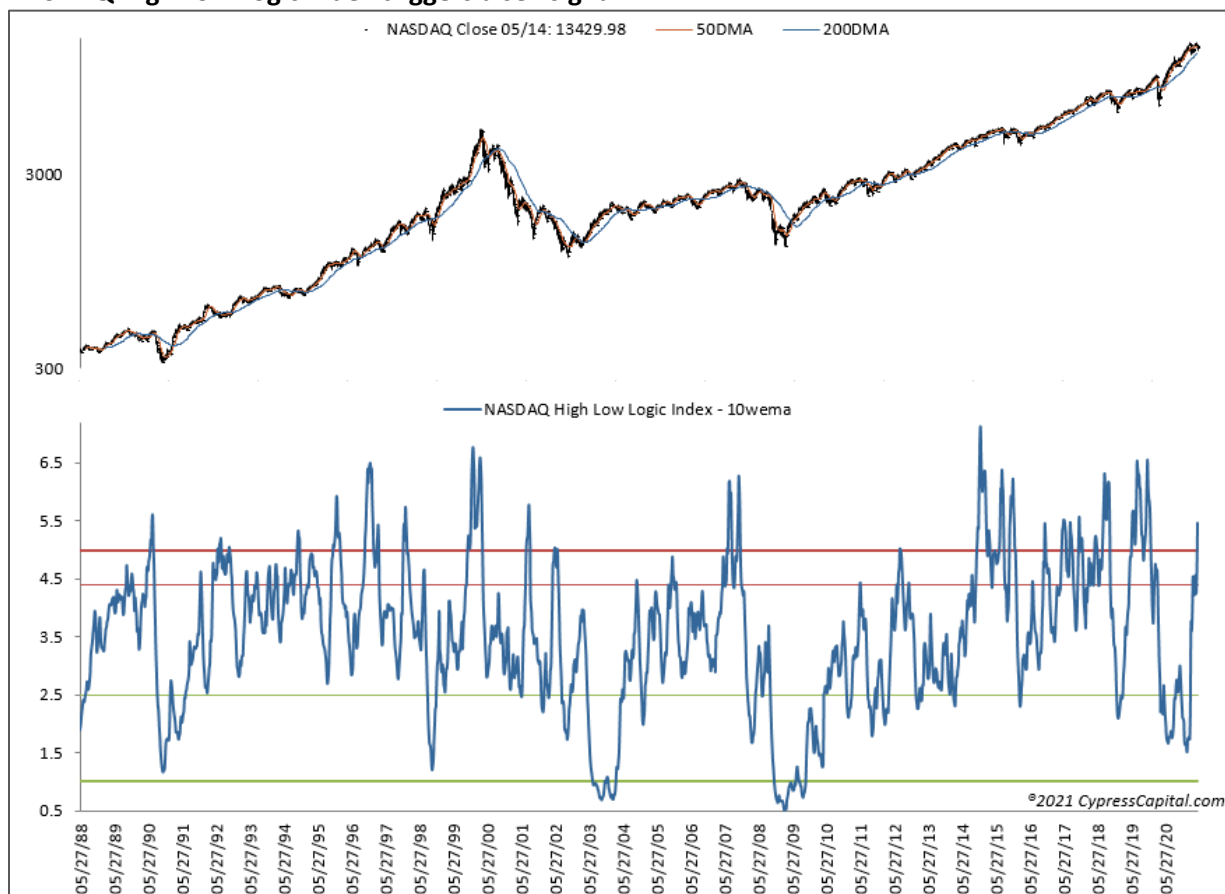
### Market Trends

USEquities	Bullish Investment
Intl Equities	Bullish Investment
REITs	Bullish Investment
Broad Commodities	Bullish Investment

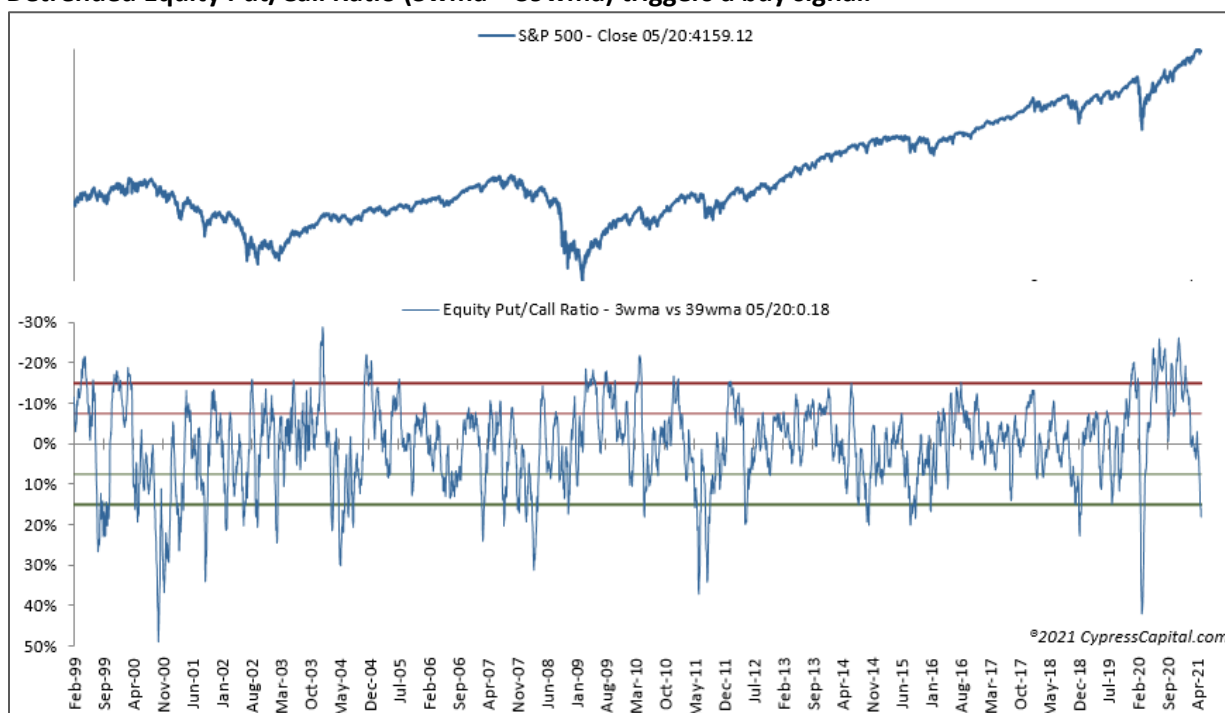
Market Risk Index scales from 0 to 100%. Higher readings correspond with higher risk markets. Scores below 25% are bullish. Scores between 25-75% are neutral, and scores above 75% are markets vulnerable to major drawdowns.

## Charts of the Week

## NASDAQ High Low Logic Index triggers a sell signal.



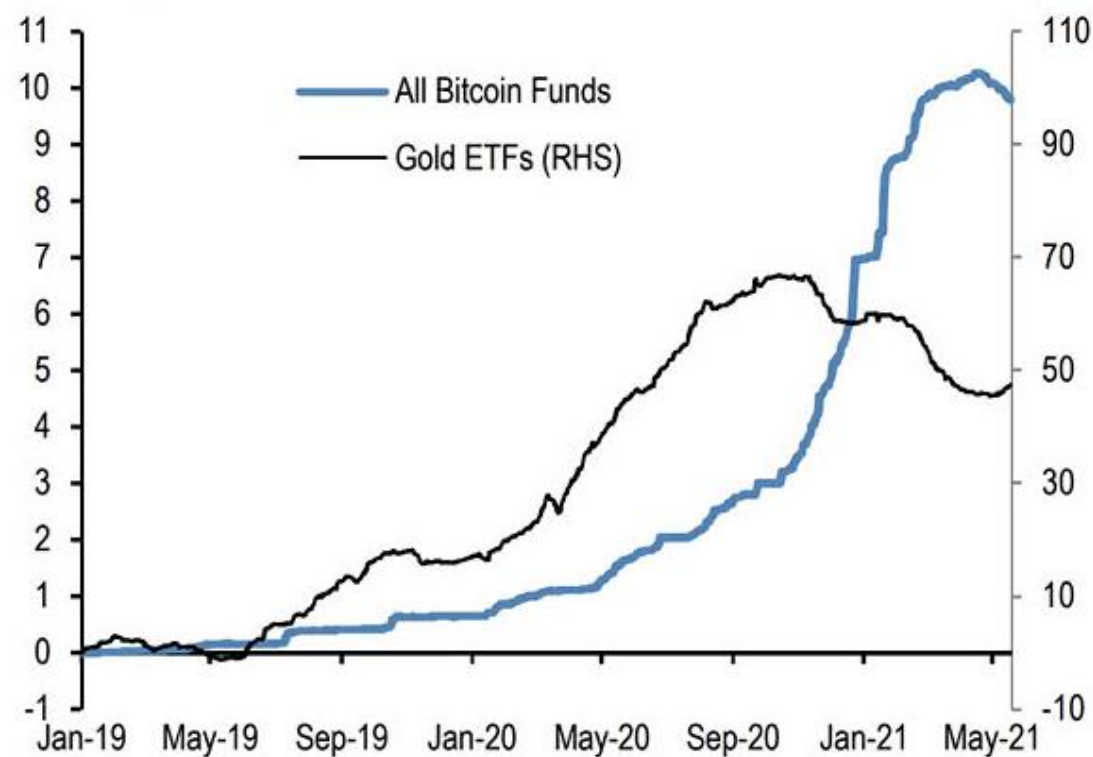
## Detrended Equity Put/Call Ratio (3wma – 39wma) triggers a buy signal.



Recent flows showing a nascent shift out of Bitcoin and into Gold.

**Figure 4: Cumulative Flows in all Bitcoin funds and Gold ETF holdings**

Both the y-axis in \$bn



Source: Bloomberg Finance L.P., J.P. Morgan.

Fund Managers have been dumping their tech stocks.

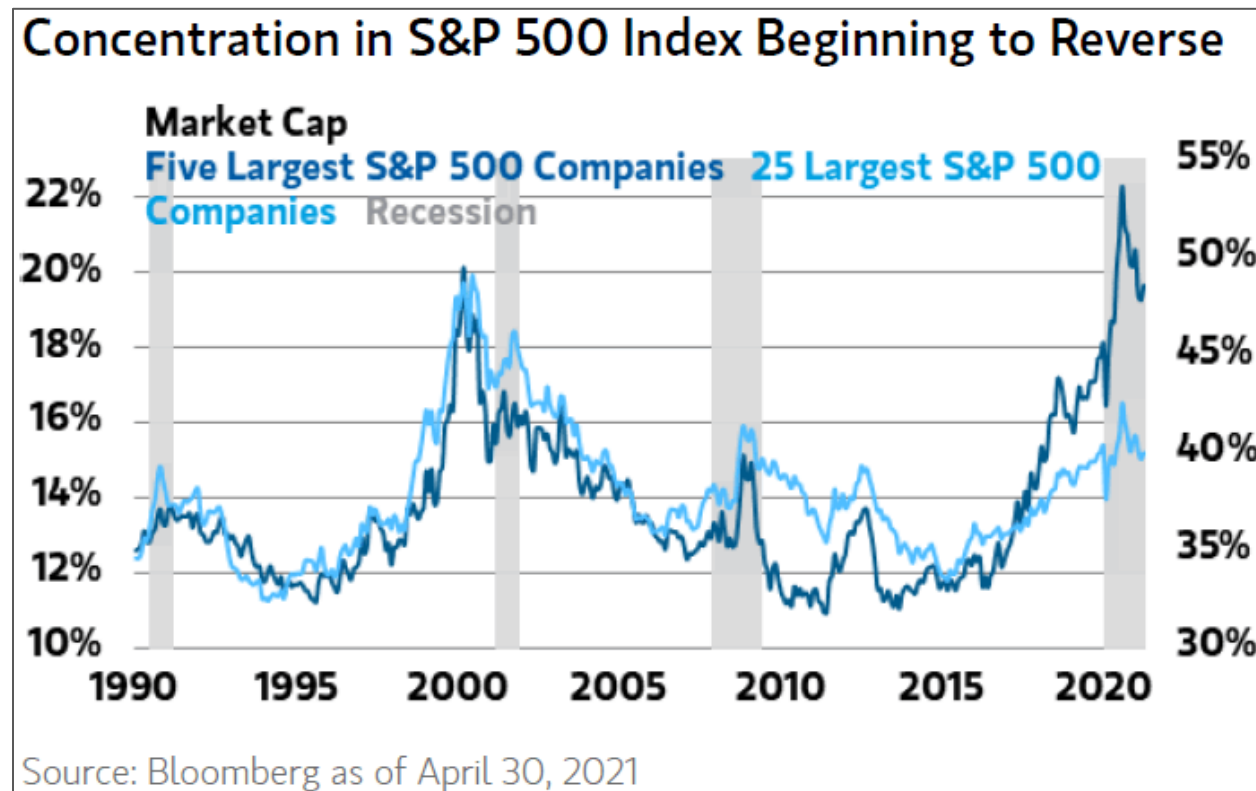
**Exhibit 17: FMS tech z-score at all-time lows**

Z-score of FMS tech allocation since 2003



Source: BofA Global Fund Manager Survey

Has FAANG dominance ended?



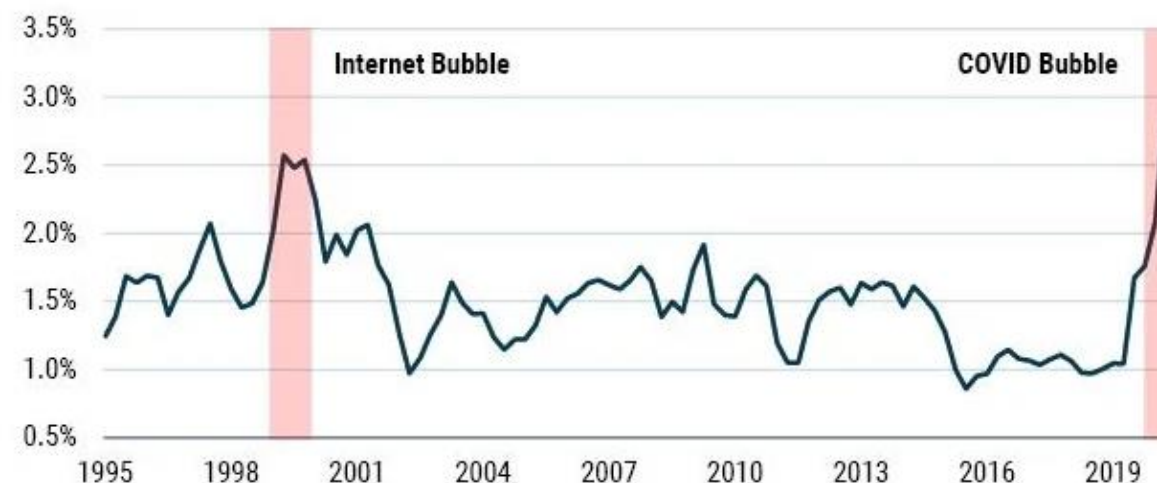
The Coinbase IPO coincided with Bitcoin's peak.



Source: John Authers

A surge in Equity Issuance is a classic sign of a frothy market.

## EXHIBIT 2: U.S. EQUITY ISSUANCE AS PERCENT OF U.S. GDP



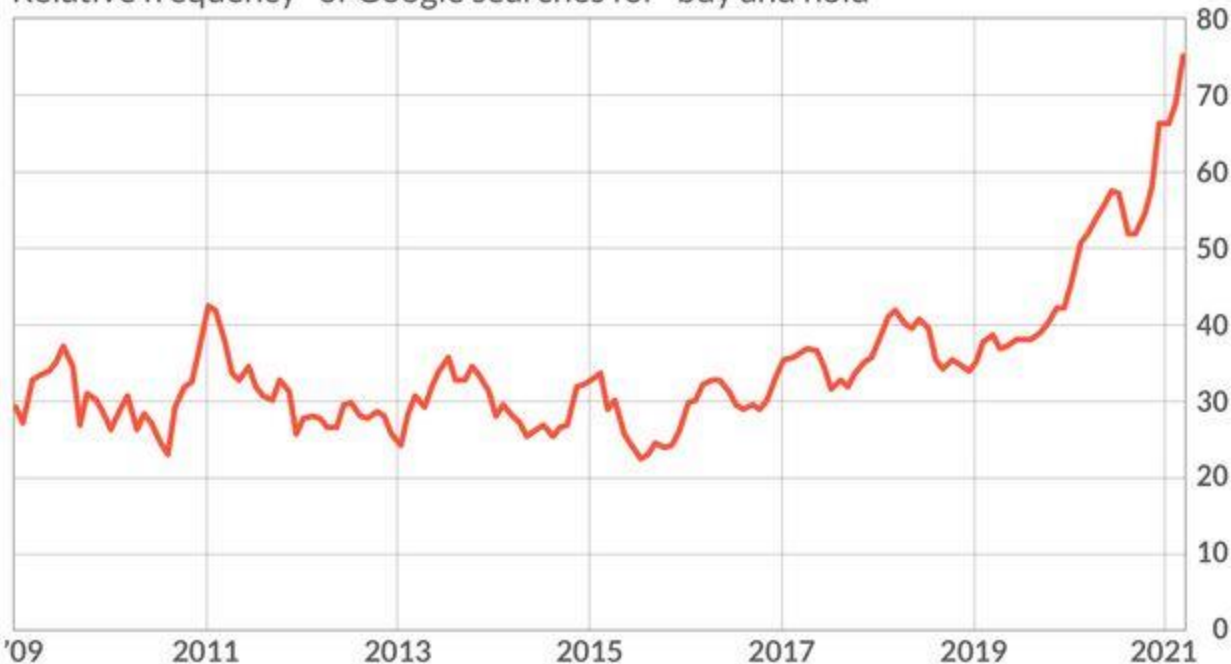
Data as of 3/31/2021 | Source: Goldman Sachs

Source: GMO

Buy and Hold is hitting Peak Popularity

## Stock market timing is out of favor

Relative frequency\* of Google searches for "buy and hold"



\*Six-month moving average of monthly readings. A month's reading would be 100 if the number of searches that month were the greatest of any in the sample.

Source: Google Trends

Source: MarketWatch

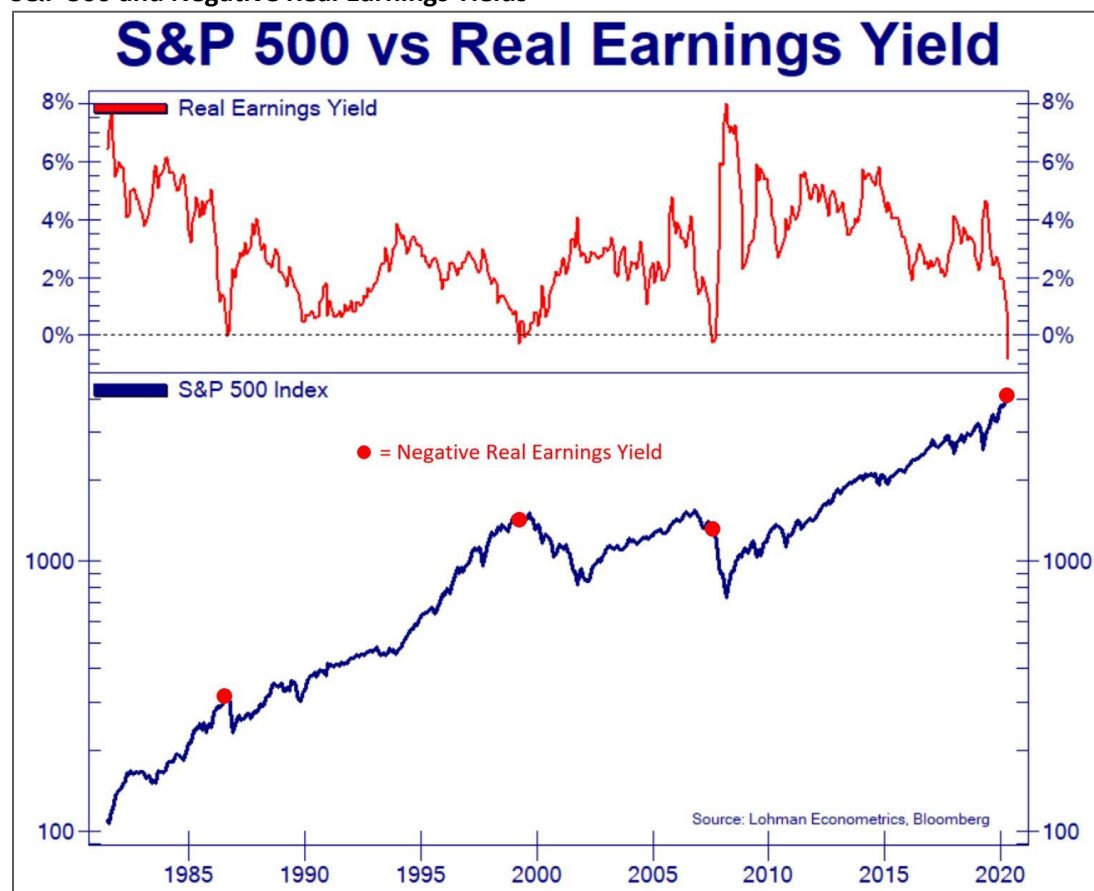


Real Earnings Yield for stocks falls below 0% to a 40-year low.



Source: @Not\_Jim\_Cramer

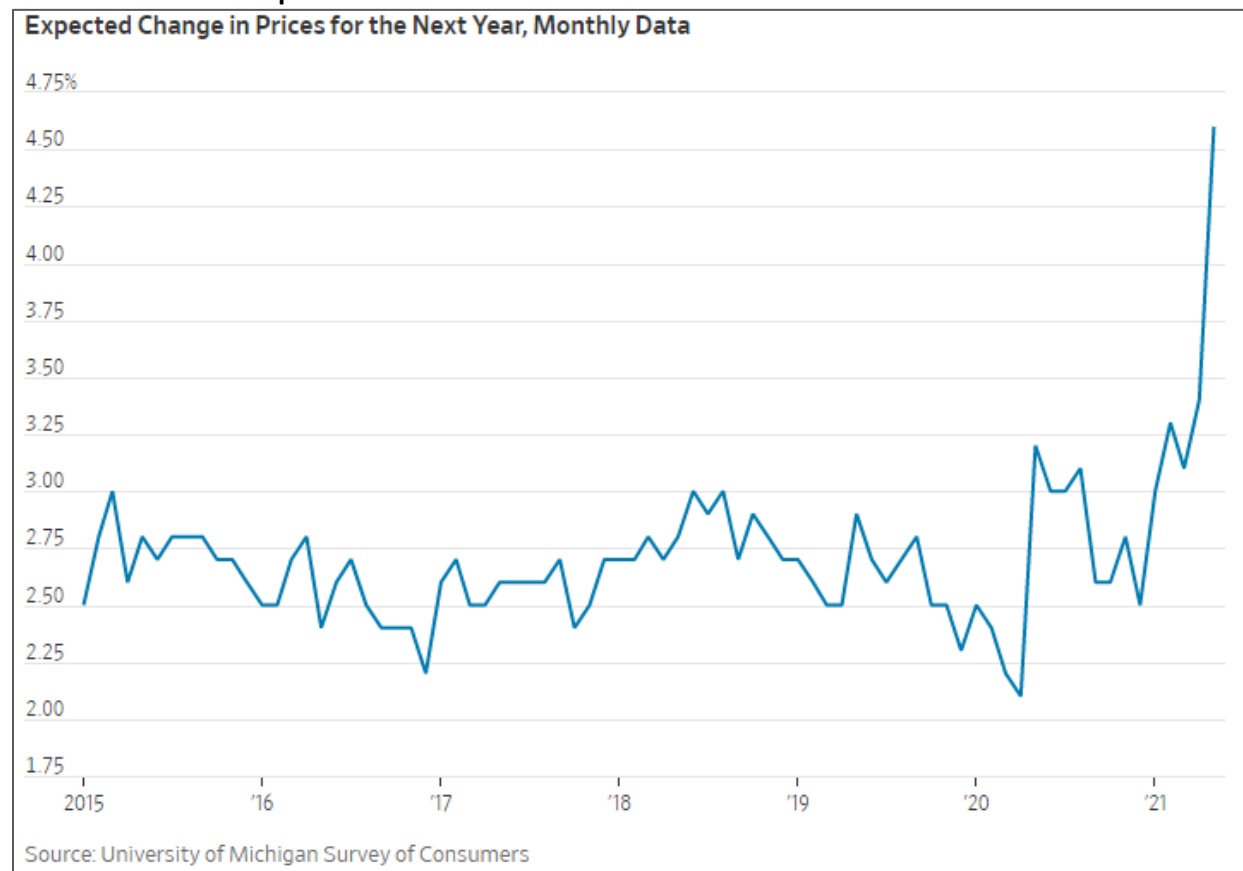
S&P 500 and Negative Real Earnings Yields



Source: @Not\_Jim\_Cramer

**Retail Sales surpass Inventories for the first time.**

Source: Liz Ann Sonders

**Consumer inflation expectations break out.**

Source: WSJ

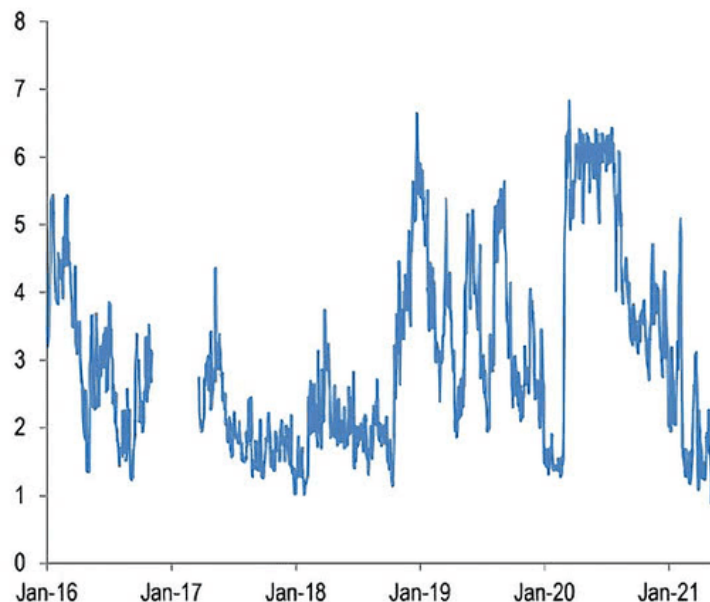
Short-selling activity has fallen to new lows.

### Chart A10a: Quantity-On-Loan on the SPY US ETF

DailyShot.com

18-May-2021

On loan quantity as a % share of share outstanding. Last obs is for 07th May 2021.



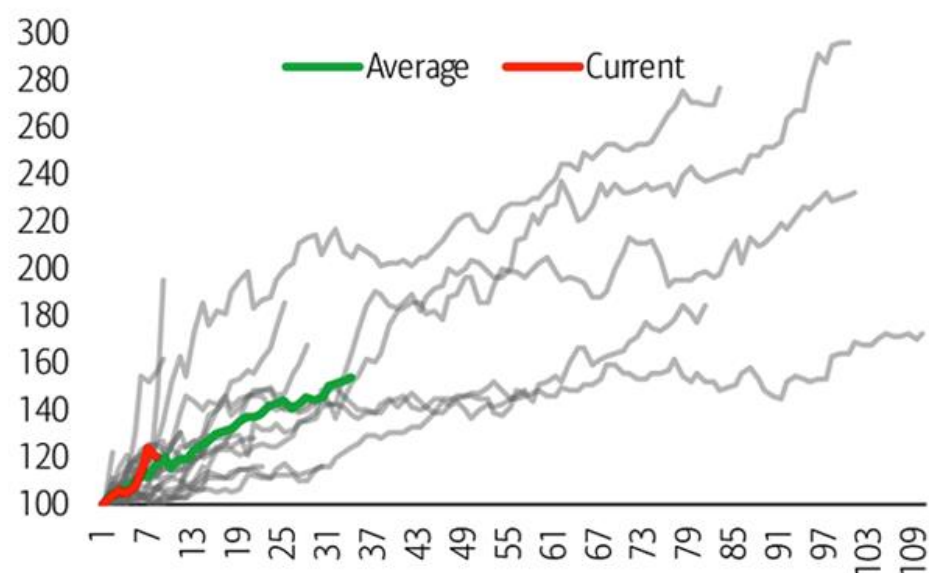
Source: Datalend, J.P. Morgan

Source: DailyShot

Value is only one-quarter of the way through an average out-performance cycle.

### Exhibit 3: Current Value cycle vs. historic Value cycles

The current Value is eight month old, compared to 33 month for the average cycle



Source: FactSet, BofA US Equity & Quant Strategy



## 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. A portfolio built upon Cypress Capital's metrics that measure dividend quality and safety. The portfolio is divided 75/25 into payers and growers. Payers are stocks having above-average yields with 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 of 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 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. The 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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