



Market Outlook

By Mark T Dodson, CFA

Plant trees that other men will sit under.

Market Risk Index improved to 48.4%, a firm neutral reading, supported primarily by short-term psychology indicators. Daily readings on the Psychology composite hit their most bullish readings (bullish for the stock market) between May 12th and May 19th and have started to reverse as the market found support and rallied. Longer leading gauges of investor psychology will have to do more heavy lifting, which requires additional market weakness and persistence in volatility that eventually wears down deep-rooted animal spirits.

The drop in MRI was supported by a slight improvement in Monetary conditions, as the rate of change on corporate bond yields has slowed – the first signs of a peak in yields after their steady ascent began last November. The Interest rates category is still the most significant negative influence on the Monetary composite, followed by inflation, so the improvement is only marginal. Inflation and tighter liquidity concerns remain front and center. Inflation pressures have been stubborn, with pandemic stimulus-induced inflation now exacerbated by an oil supply shock. Meanwhile, the Fed is hammering away at the wealth effect to rein in inflation. It should do the trick, but it isn't some operation done with military precision – it's more like a guy trying to fix a stuck natural gas valve with a sledgehammer.

Stock market weakness has lingered long enough to put a bearish shift in play for Market Trend at some point this summer, which would be the first move to a bearish trend in over six years. Unlike traditional trend-following tools, our version is best described as a tool that serves as a warning for a second leg down in the stock market that is either clearly weak or a bear market is well underway. If history is a guide, we will warn of a bearish shift in trend about the time monetary conditions and stock market valuations make significant improvements.

In bear markets, Market Risk Index overshoots neutral and moves into the lowest quartile of readings. Those are environments where the margin of safety for owning equities is very high, but also environments fraught with pessimism and negative emotions. It's in those environments that investors can "plant trees that other men will sit under."

Market Risk Index

Rec Allocation 15% Underweight

48.4%

Category Percentiles

Psychology - P3



Monetary - M4



Valuation - Extremely Overvalued



Trend



Largest Psychology Influences

Surveys	Positive
Volatility	Positive
Flow of Funds	Negative
Bank Sentiment	Positive

Largest Monetary Influences

Interest Rates	Negative
Exchange Rates	Positive
Inflation	Negative

Valuation

7-10 Year Rtn Forecast	2.2%
10Yr US Treasury Yield	3.0%

Market Trends

US Equities	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.

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.

[Contact us](#) for more information.

ⁱ Benjamin Graham, Intelligent Investor