



Market Outlook

By Mark T Dodson, CFA

Big Improvement in Psychology Offset by Shift to Bearish Market Trend

Market Risk Index dropped to 76.1%. The Psychology Composite saw a monster one-week improvement dropping from 81.3% to 51.8% in a single week. The Leveraged Investments category has improved to neutral, which never wavered in signaling how extreme the speculative enthusiasm in markets has been until now. The Surveys category is nearing its maximum bullish readings, similar to what it reached during the July bottom. The signs of capitulation that we have been consistently looking for have not been met, but they are drawing closer.

The fly in the ointment here is that Market Trend shifted bearish in the last week, so Market Trend readings are now part of the Market Risk Index calculation and affect week-to-week movements. The net result is that the high Market Trend risk score offset much of the improvement in Psychology. As a result of the shift to Bearish trend, we have decreased our recommended allocation to a target of 25% underweight equities.

Another seismic shift this week – the Inflation category of the Monetary Composite has moved to neutral. Inflation has been a headwind for Monetary conditions since the spring of 2021 and never let up in its warnings no matter how many times the word transitory was uttered from the mouths of central bankers. Maybe it’s a coincidence, unlikely, but it took headlines of the UK bailing out their pension system to move our basket of leading inflation indicators away from being a bearish influence on markets. We think inflation pressures have been whipped for now, and it’s because a recession is in play. We wouldn’t be surprised if this Fed gets spooked into pausing their rate hikes very soon.

Market Risk Index

Rec Allocation 25% Underweight

76.1%

Category Percentiles

Psychology - P4



Monetary - M4



Valuation - Extremely Overvalued



Trend



Largest Psychology Influences

| | |
|-----------------|----------|
| Surveys | Positive |
| Volatility | Positive |
| Option Activity | Positive |
| Flow of Funds | Negative |

Largest Monetary Influences

| | |
|--------------------|----------|
| Interest Rates | Negative |
| Exchange Rates | Positive |
| Lending & Leverage | Negative |

Valuation

| | |
|----------------------------------|------|
| 7-10 Year Equity Return Forecast | 3.1% |
| 10Yr US Treasury Yield | 3.7% |

Market Trends

| | |
|-------------------|--------------------|
| US Equities | Bearish Trade |
| Intl Equities | Bearish Trade |
| REITs | Bearish Trade |
| 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.

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