Market Outlook

By Mark T Dodson, CFA

Yield Curve is crying wolf – few are listening.

Market Risk Index climbed to 66%. In a reversal of recent trends, the risk score for Monetary Conditions increased while Psychology and Valuations improved.

Technical Indicators were the second largest negative influence on the Psychology Composite for the second week in a row. Breadth has narrowed markedly since the failure of SVB, with gains in the cap-weighted indices being driven by the largest of the large-cap stocks. It's a suspect development for a market to grow so narrow in leadership after experiencing a bullish Zweig Breadth Thrust just a few weeks ago.

Also worth noting this week, the Consumer Expectations Gap set a new cycle high in April, climbing to the most optimistic reading since March 2001. Note that in March 2001, those uber-high optimism readings occurred a full year after the dot-com bubble burst. The lesson in that instance was that the denial phase of a bear market goes well beyond what most of us expect. Having lived through it, we remember how investors were trying to catch falling knives when that bear market had barely shown its fangs.

On the Monetary front, the Yield Curve inversion surpassed the depths of the 1929 and 1973 inversions this week to become the second most pronounced yield curve inversion in over a century. It has a real shot at displacing the Volker inversion from 1981 over the coming weeks.

The yield curve inversion is also six months old, so by our estimation, the headlines of banking troubles are merely the first shots across the bow in a battle likely to last well into 2024. We suspect that the recent sanguine readings from our Monetary Composite today will be short-lived, as the yield curve continues to signal that market-induced tighter monetary conditions are forthcoming.

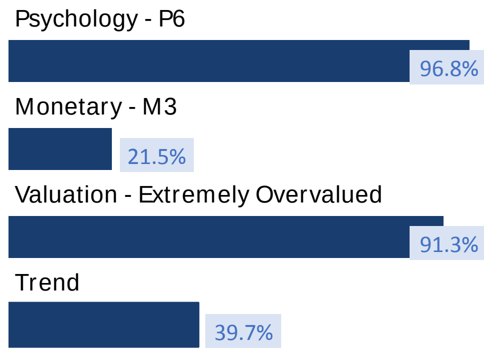
With equity positioning barely off all-time highs and Consumer Expectations near all-time highs, it is clear that for the fourth time in our career, the yield curve inversion is again treated like the little boy who cried wolf. History still rhymes.

Market Risk Index

Rec Allocation 25% Underweight

66.0%

Category Percentiles



Largest Psychology Influences

Leveraged Investments	Negative
Technical Indicators	Negative
Flow of Funds	Negative
Volatility	Negative

Largest Monetary Influences

Interest Rate Spreads (Yield Curve)	Negative
Inflation	Positive
Lending & Leverage	Positive

Valuation

7-10 Year Equity Return Forecast	3.1%
10Yr US Treasury Yield	3.4%

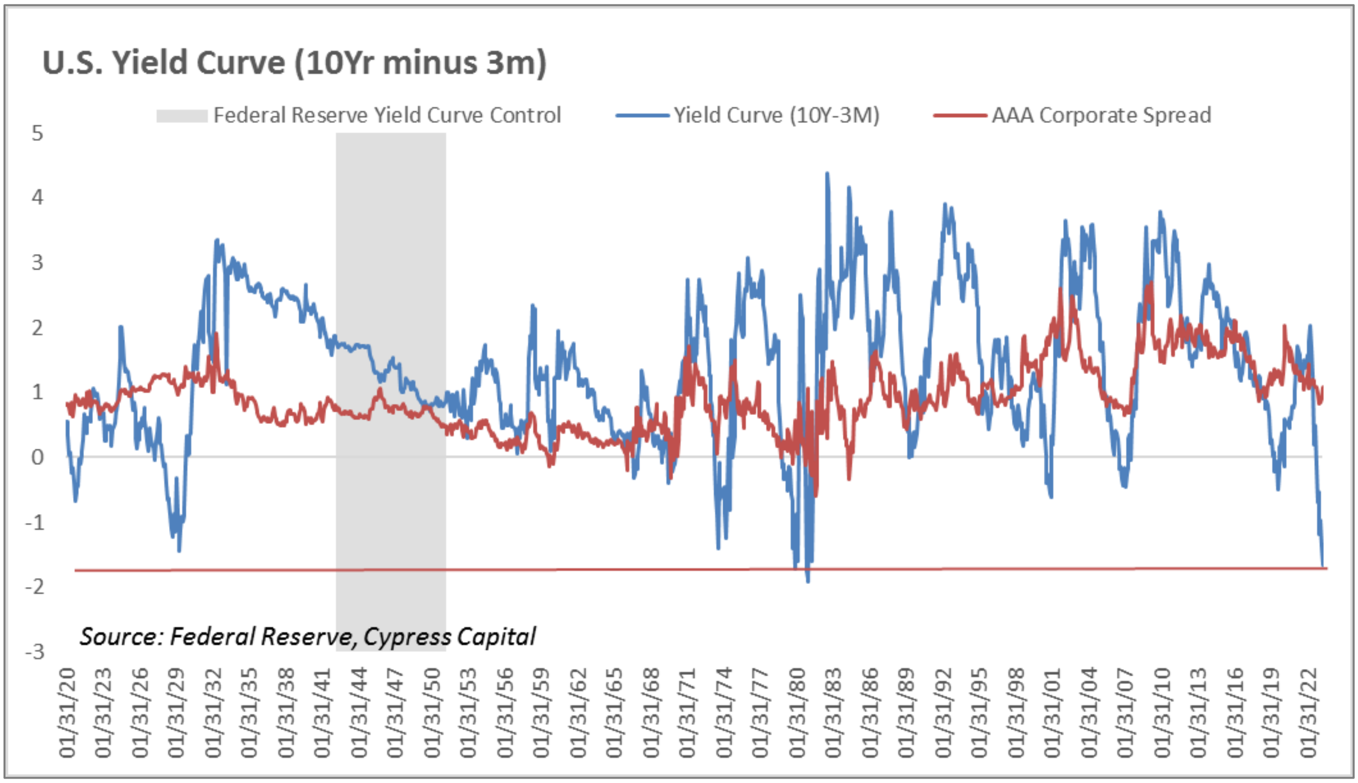
Market Trends

US Equities	Bullish Trade
Intl Equities	Bullish Trade
REITs	Bearish Trade
Broad Commodities	Bearrish Trade

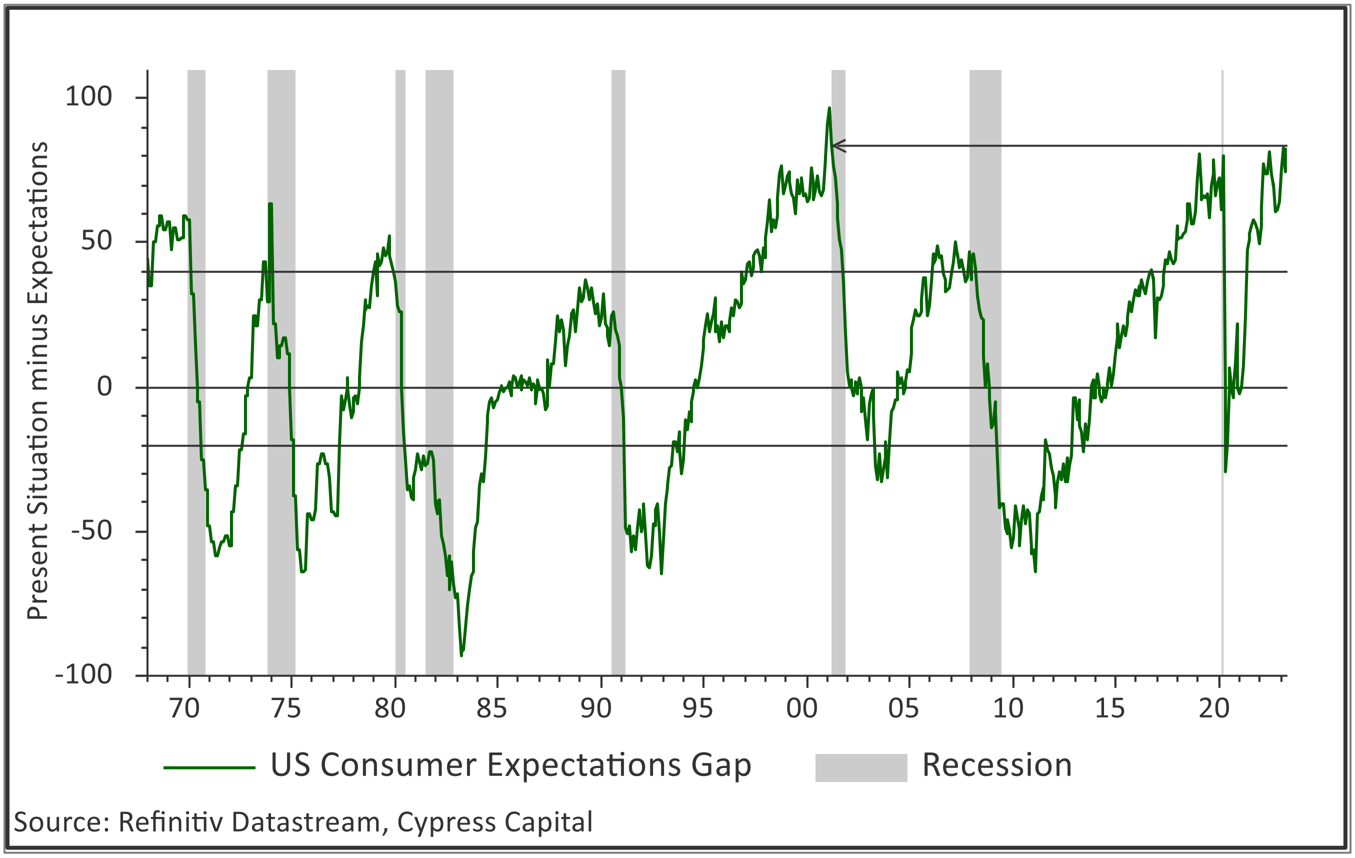
Market Risk Index scales from 0 to 100%. Higher readings correspond with higher risk markets. Scores below 25% are bullish. Scores between 25-75% are neutral, and scores above 75% are markets vulnerable to major drawdowns.

Charts of the Week

Yield Curve Inversion becomes the second most severe in a century!

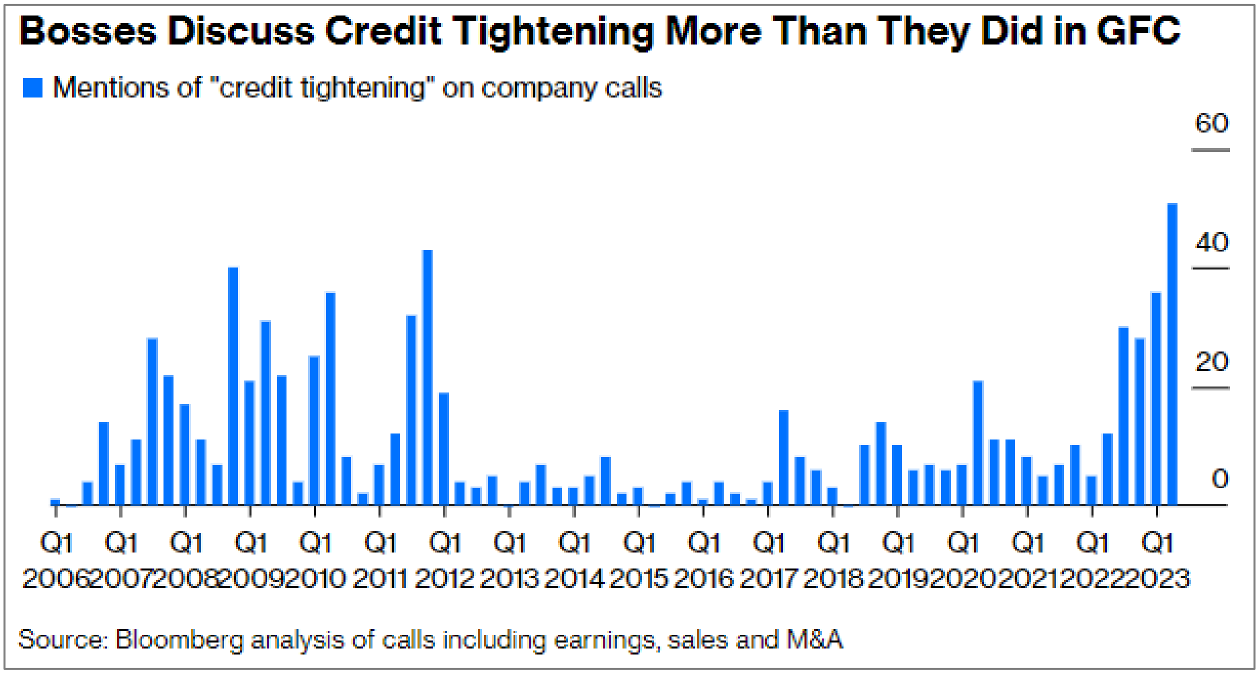


Consumer Expectations Gap sets a new cycle high - the most positive since early 2001.

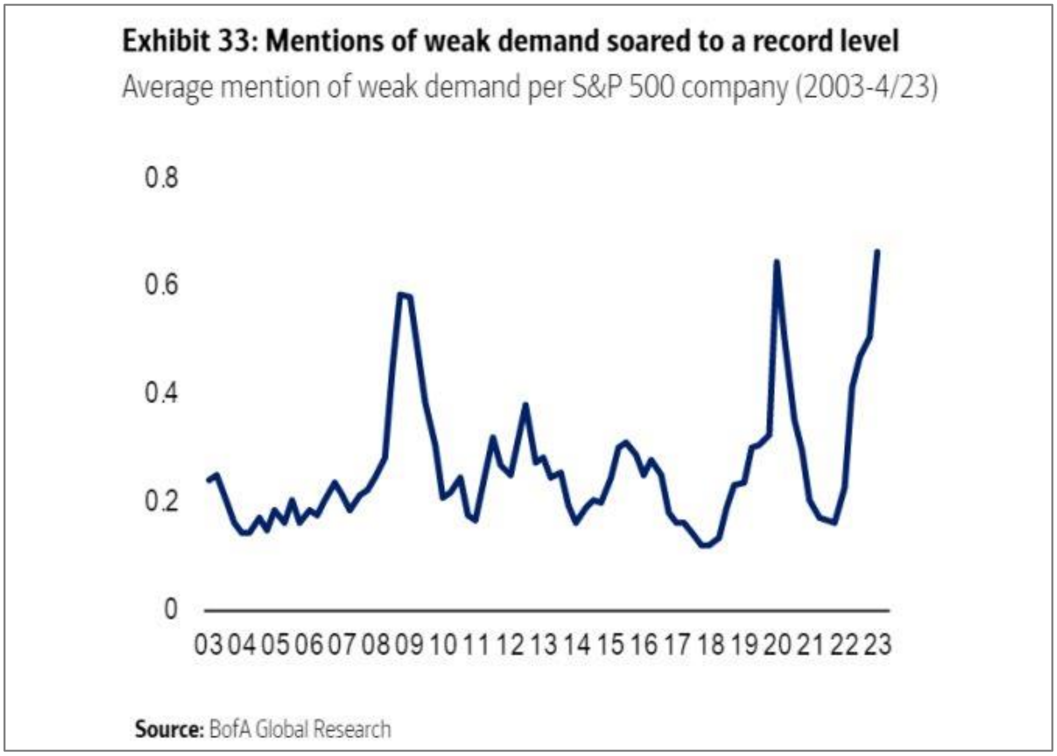


Technology versus S&P 500 is back to Nifty Fifty and Dot-Com Highs.

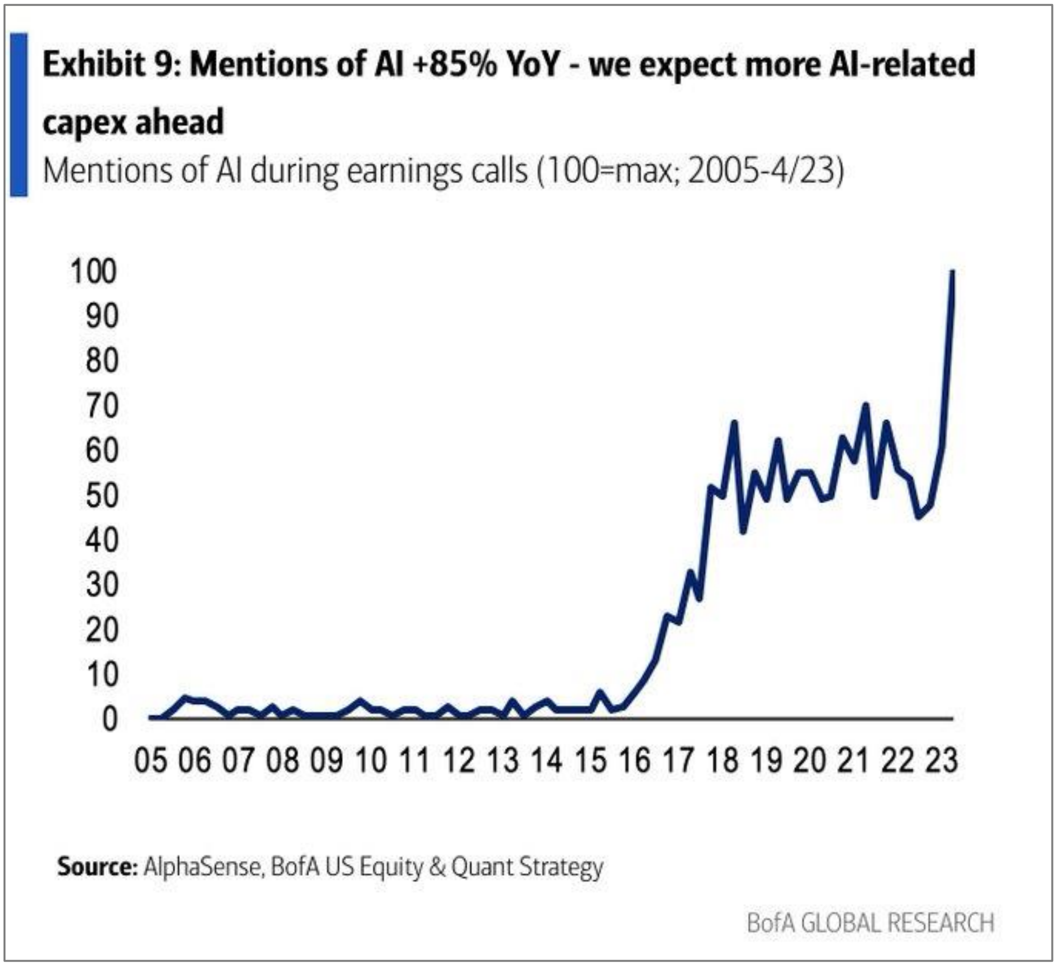
Earnings calls have been full of mentions of Credit Tightening.



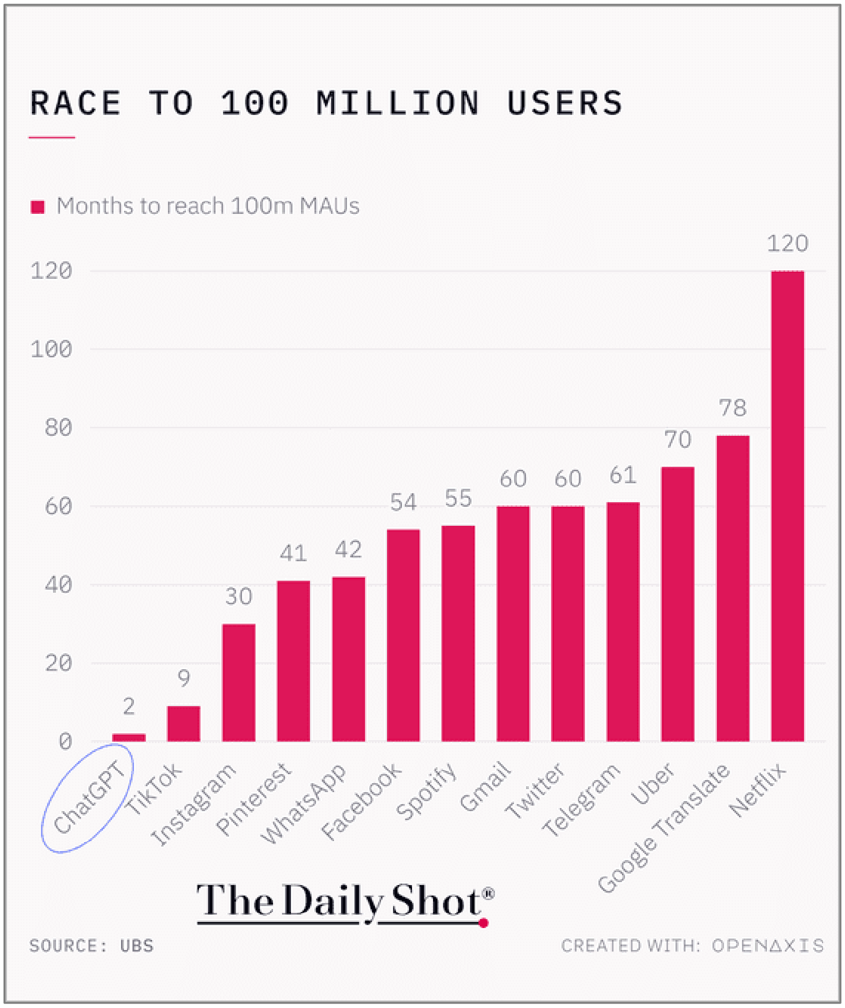
Mentions of Weak Demand have also been very popular on earnings calls.



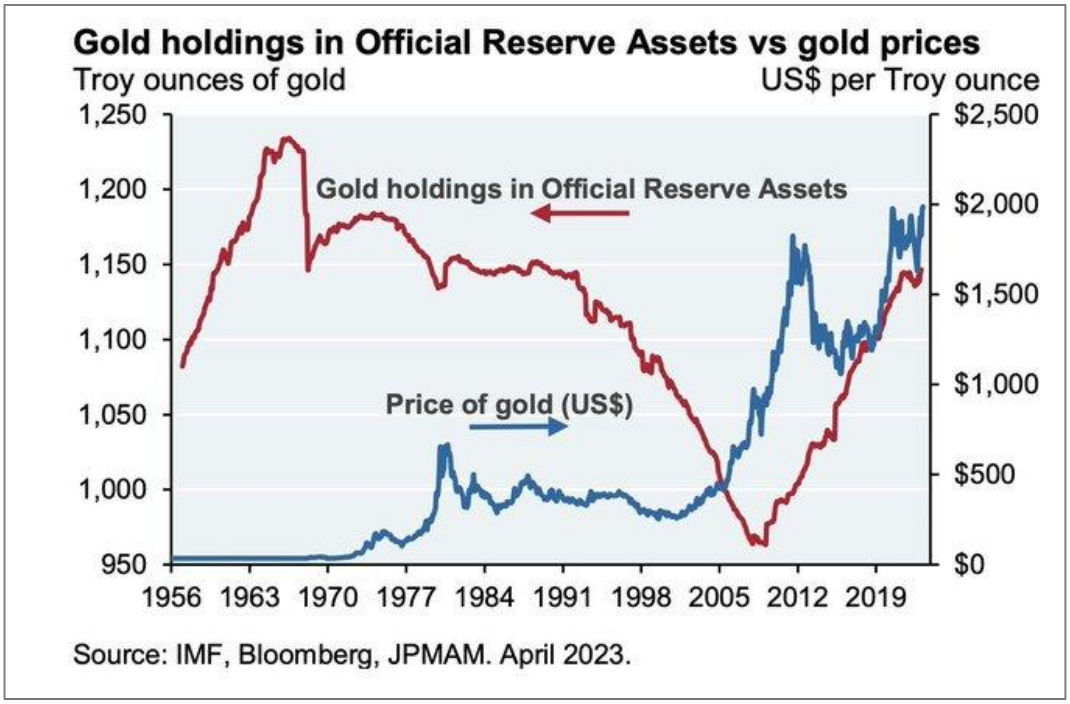
Most impressive is the record number of mentions of Artificial Intelligence on Earnings Calls.



ChatGPT, the poster child of Large Language Model AI, hit 100MM users in only 2 Months!

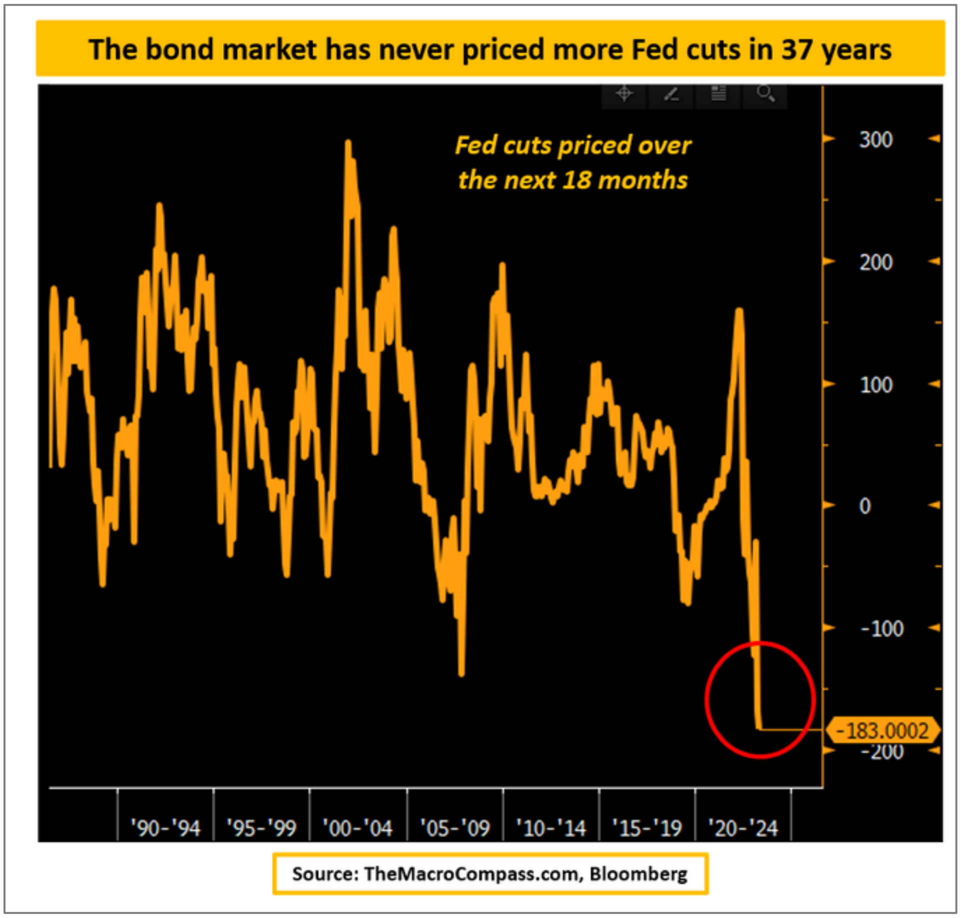


Central Banks appear to have spent the last 15yrs printing money and buying gold with the proceeds.

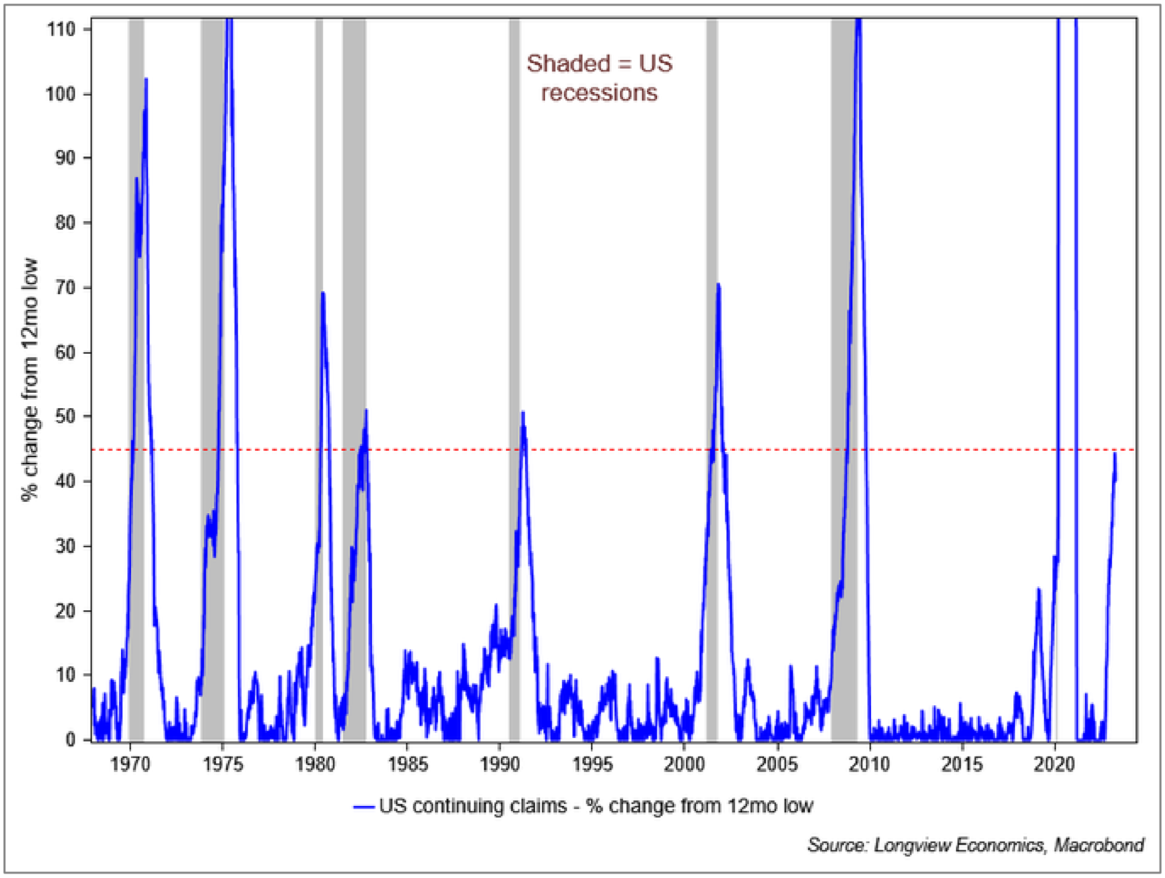


Higher interest rates have made Federal Government Interest Payments go parabolic.

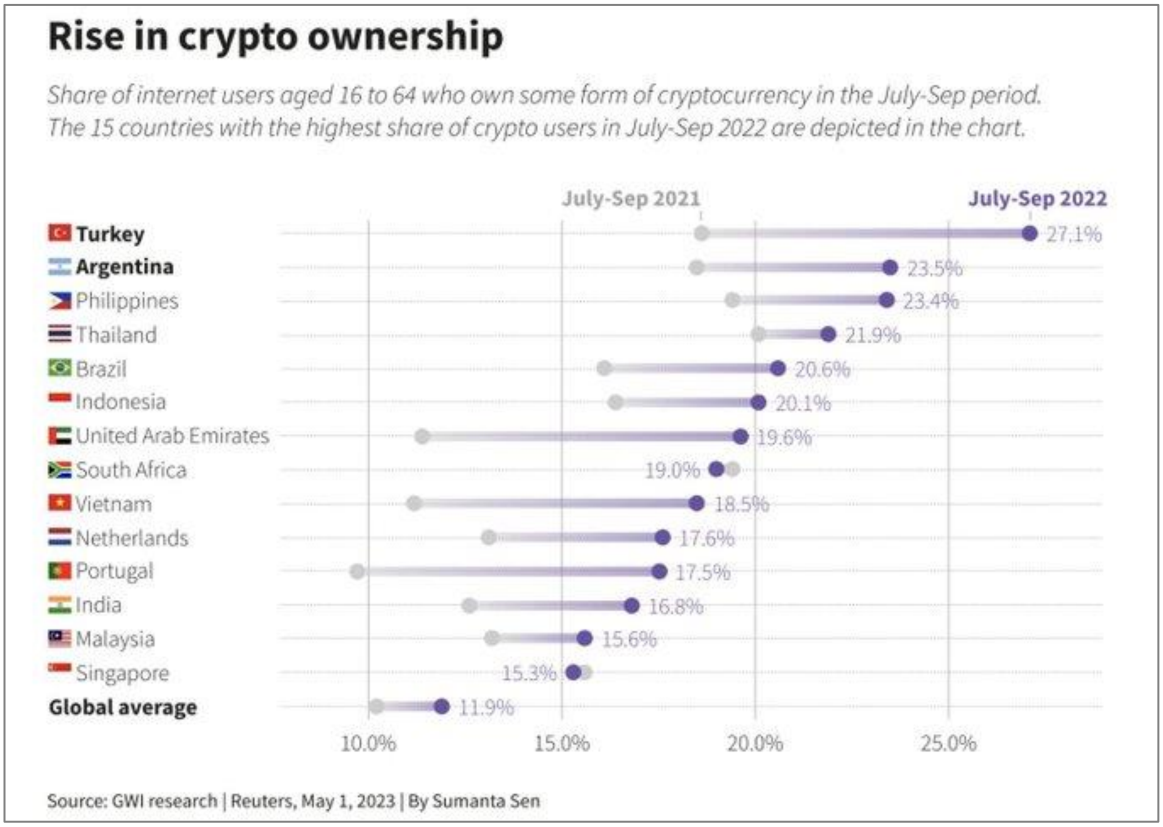
Fed rate cuts that markets are pricing in over the next 18 months have recessionary implications.



Continuing Claims are knocking on recession's door.



Crypto ownership by country looks like a referendum on governance.



Sell in May - great table of average six-month holding periods.

Sell In May? The Next Six Months Are The Weakest

Various S&P 500 Index 6-Month Returns

6-Month Period	Average % Change	% Higher
Nov-Apr	6.9%	76.4%
Oct-Mar	6.5%	69.9%
Dec-May	5.3%	70.8%
July-Dec	4.8%	71.2%
Sept-Feb	4.6%	68.5%
Aug-Jan	4.5%	69.9%
Mar-Aug	4.2%	71.2%
Feb-July	4.1%	71.2%
Jan-June	4.0%	68.1%
June-Nov	3.3%	67.1%
Apr-Sept	2.6%	64.4%
May-Oct	1.7%	64.4%

Source: Carson Group, FactSet 4/25/2023 (1950 - Current)
@ryandetrick

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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.