Cypress CAPITAL

Market Outlook

By Mark T Dodson, CFA

The Thumb-Nosing Bull Market

In the week that a new bull market was officially confirmed, our Market Risk Index crossed above 75%, which denotes market environments with substantial drawdown risk. All three of our counter-cyclical factors worsened (Psychology, Monetary, and Valuation).

We saw a notable uptick in speculative readings across our Psychology composite in the Leveraged Funds and Options categories. Our Smart versus Dumb Option Money Indicator matched the Euphoria readings from January 2020. Also, Leveraged ETF volume officially crossed into Euphoria territory and has nearly driven the level of assets in Leveraged ETFs into the red zone.

This is also the lowest VIX reading ever during the week when a new bull market is confirmed. VIX is already lower than the lowest lows achieved during the previous bull market. You usually see VIX readings this low a couple of years into a bull market advance.

Meanwhile, our Monetary Composite continues to tighten, moving out of the best third of readings, primarily due to softening fixed income markets. Both equity and fixed income markets behave as if there is only enough liquidity to drive pockets of strength. An AI-narrative-driven rally in Tech stocks sucks liquidity out of small-cap stocks and bonds. Then, a surge in small and mid-cap stocks sucks liquidity out of Tech stocks...and also bonds. The recent weakness in bond prices has driven the Interest Rates category back into being a bearish market influence.

It's a new bull market beginning with late-cycle breadth while the Fed is still tightening into one of the steepest yield curve inversions in history, with valuations having nowhere to run except straight back into bubble territory. It's a new bull market that fights the Fed – the first to begin before the Fed starts to ease.

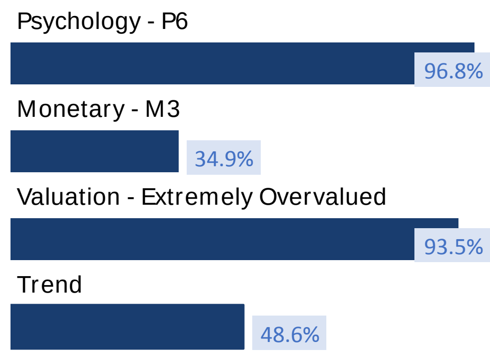
This bull market thumbs its nose at historical precedent and the laws of financial gravity.

Market Risk Index

Rec Allocation 25% Underweight

76.3%

Category Percentiles



Largest Psychology Influences

Leveraged Investments	Negative
Option Activity	Negative
Consumer Confidence	Negative
Flow of Funds	Negative

Largest Monetary Influences

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

Valuation

7-10 Year Equity Return Forecast	2.5%
10Yr US Treasury Yield	3.7%

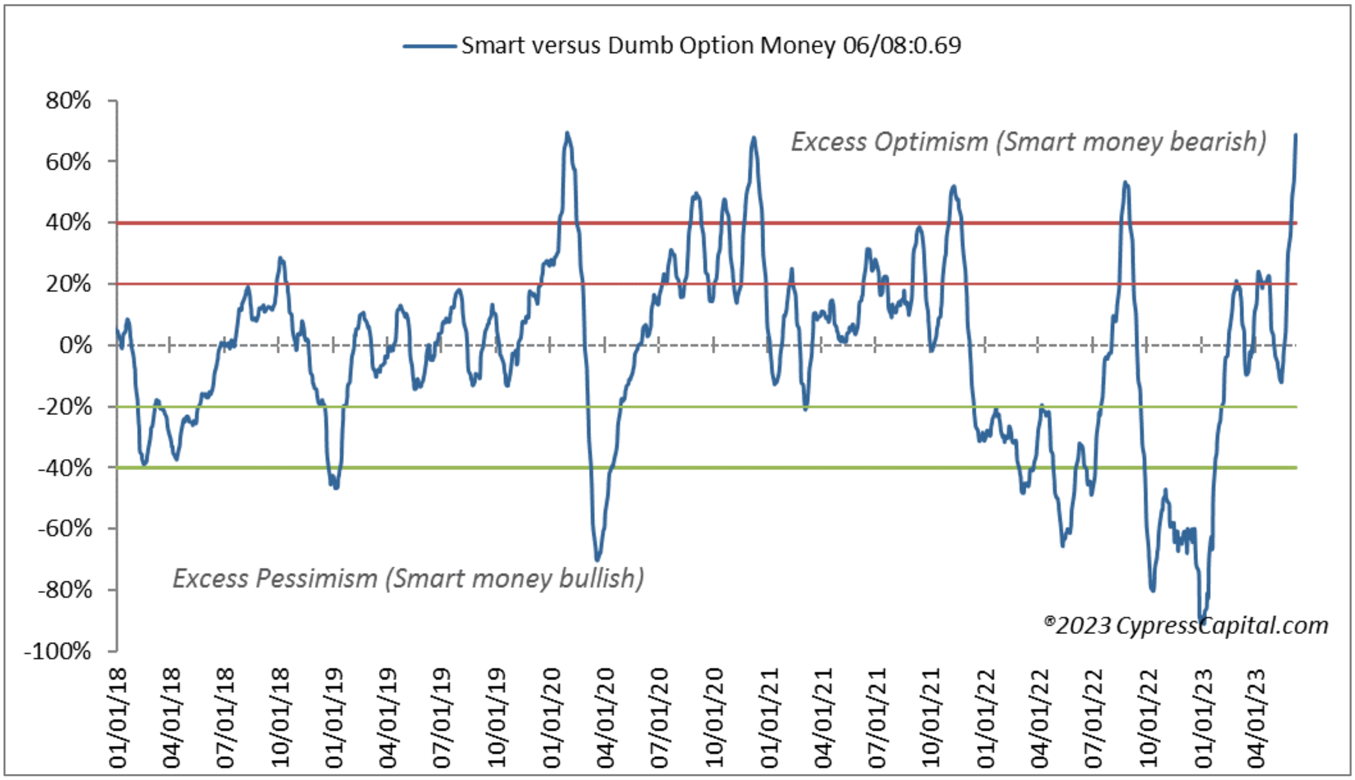
Market Trends

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

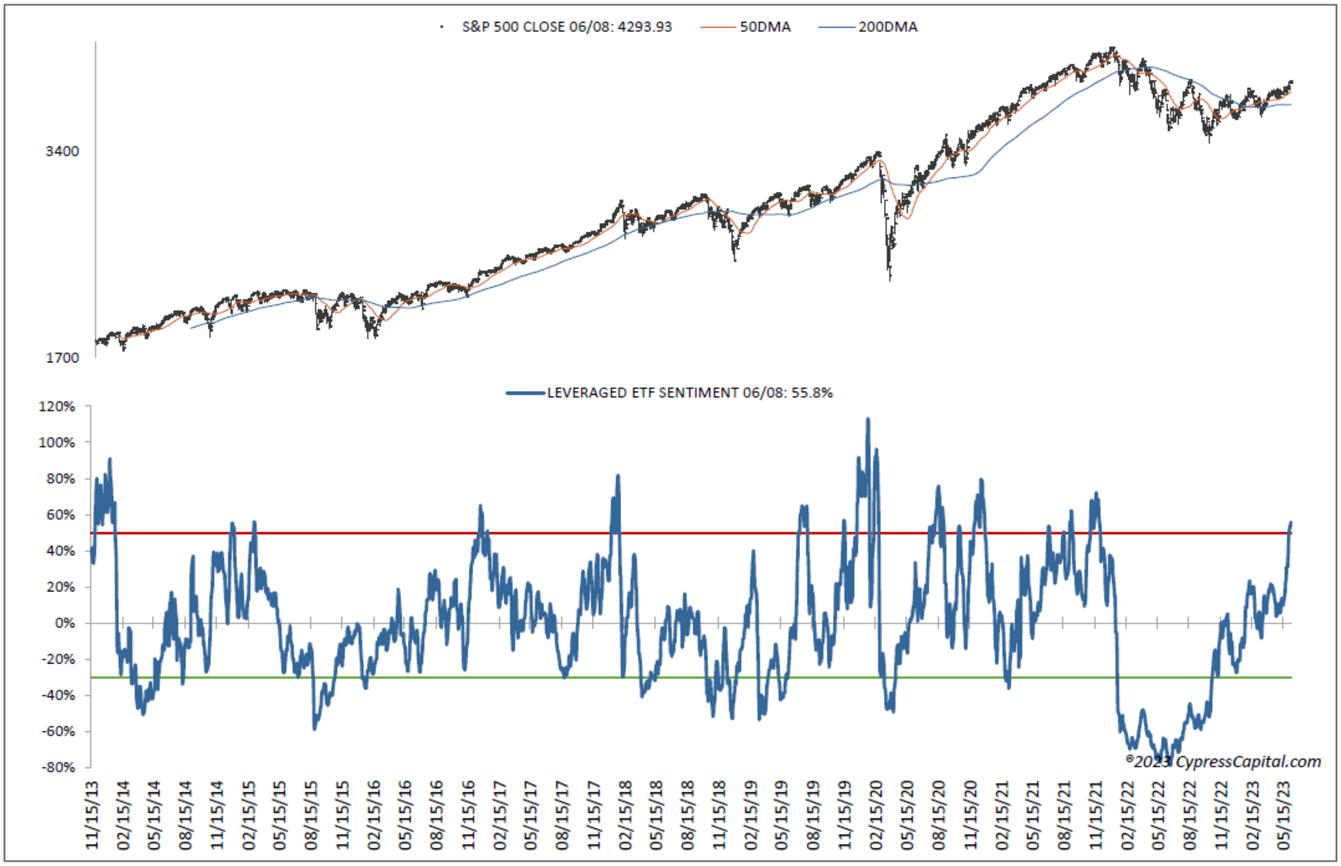
Market Risk Index scales from 0 to 100%. Higher readings correspond with higher risk markets. Scores below 25% are bullish. Scores between 25-75% are neutral, and scores above 75% are markets vulnerable to major drawdowns.

Charts of the Week

Smart versus Dumb Option Money surges to Excess Optimism

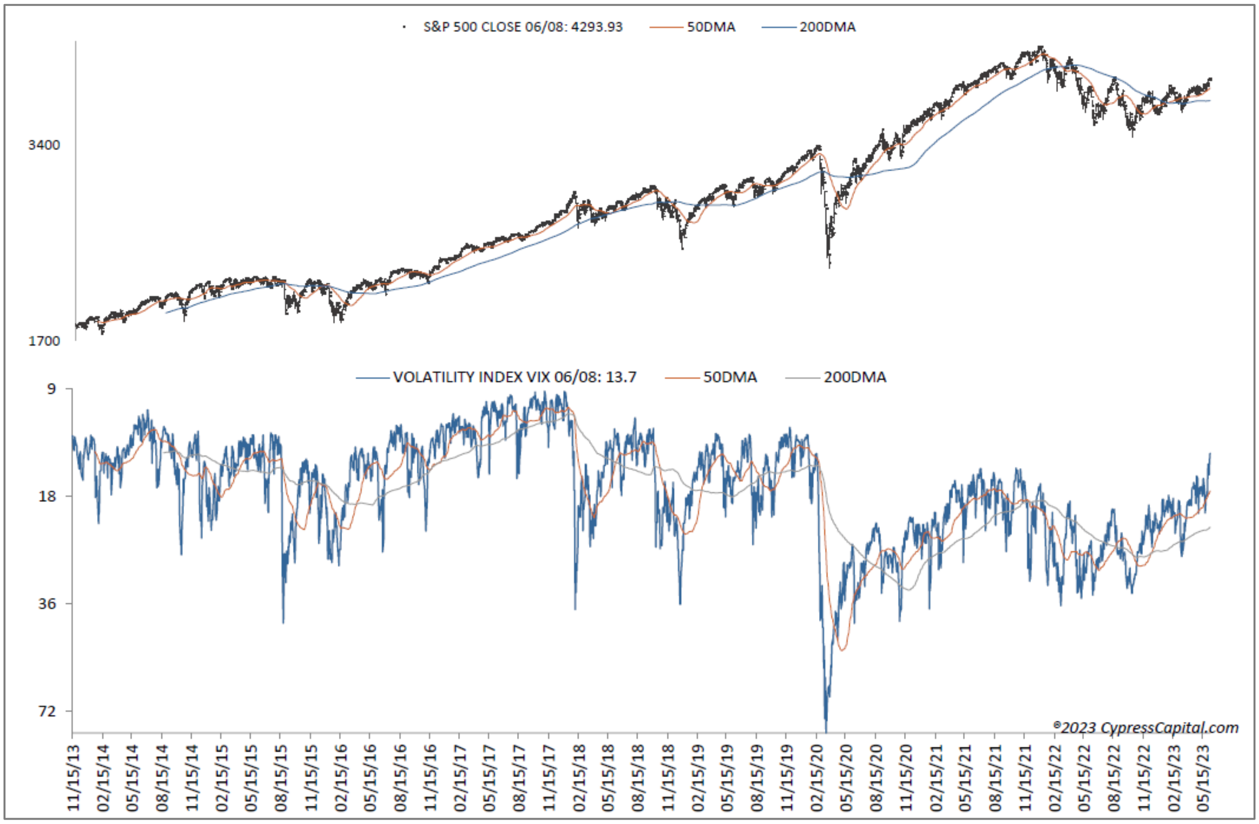


Leveraged ETF Volume Sentiment is Euphoric.

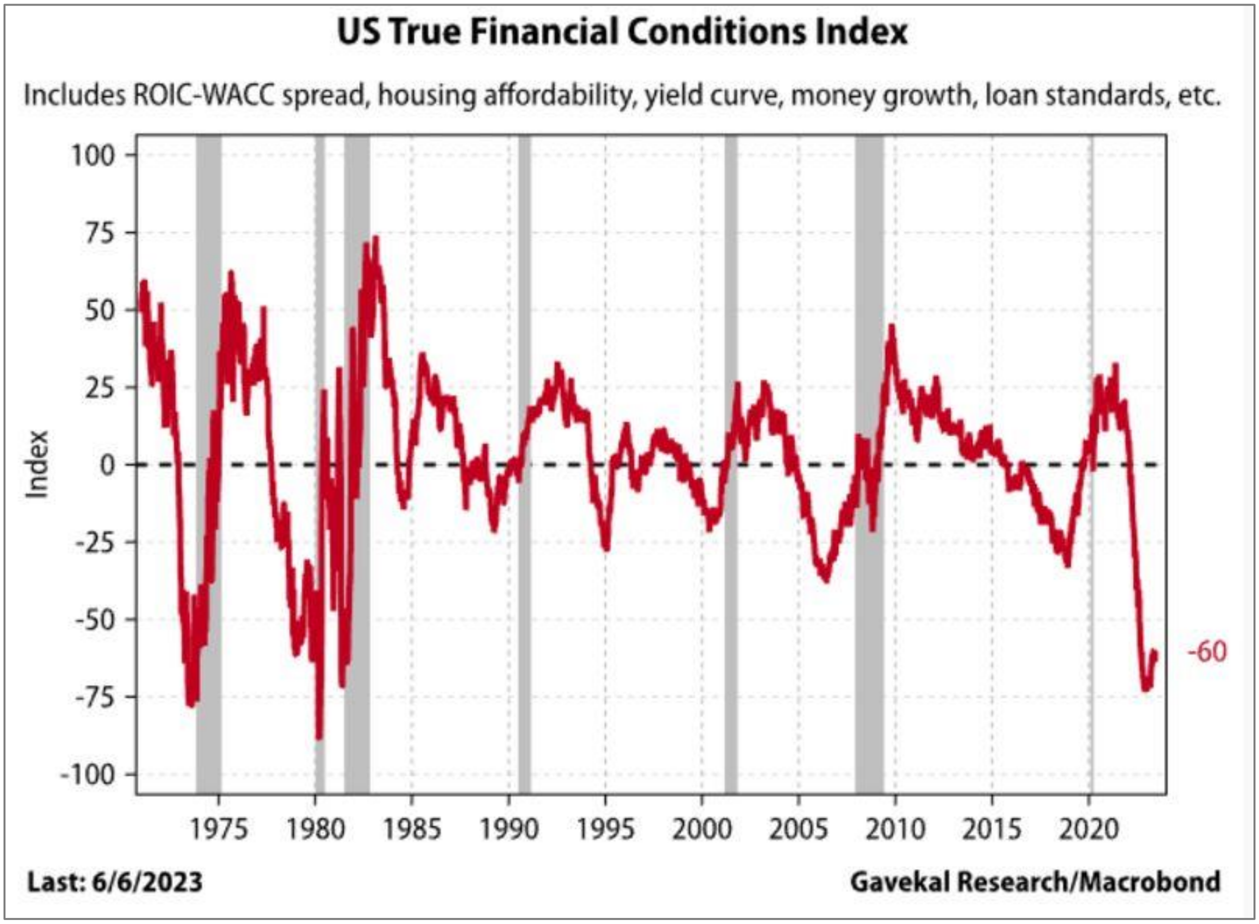


The ratio of Leveraged to Inverse ETF Assets is becoming enthusiastic.

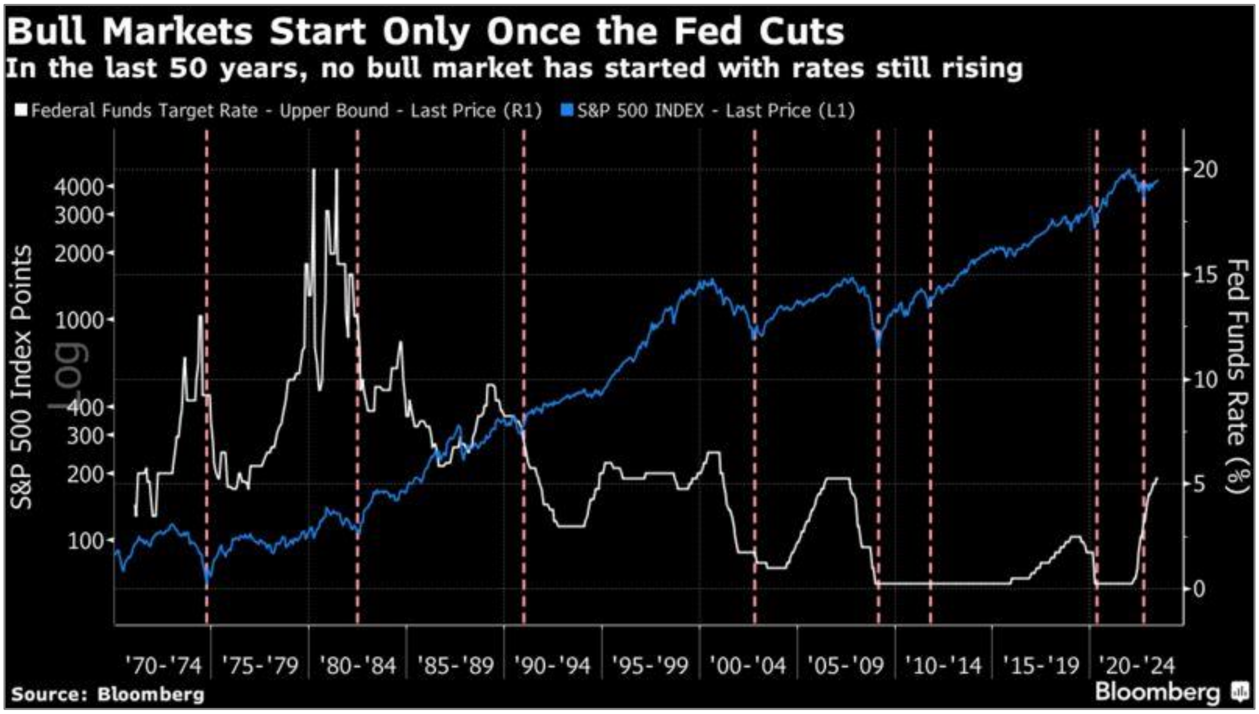
Lowest VIX on record during the week a new bull market is confirmed.



Weakest Financial Conditions since the 1980s.



Bull Markets Start Only After the Fed Start Cutting – not this one.

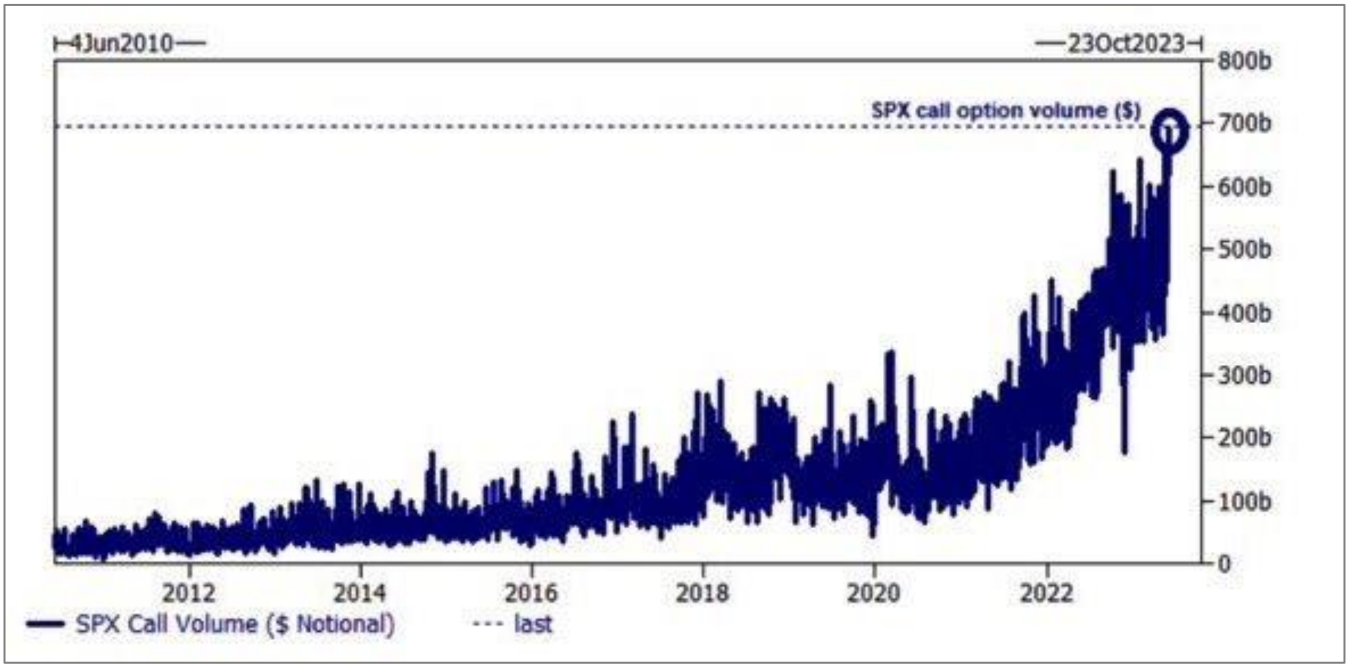


The spread between S&P 500 Earnings Yield and 10Yr Treasuries is the lowest since the 2007 Bull Peak.

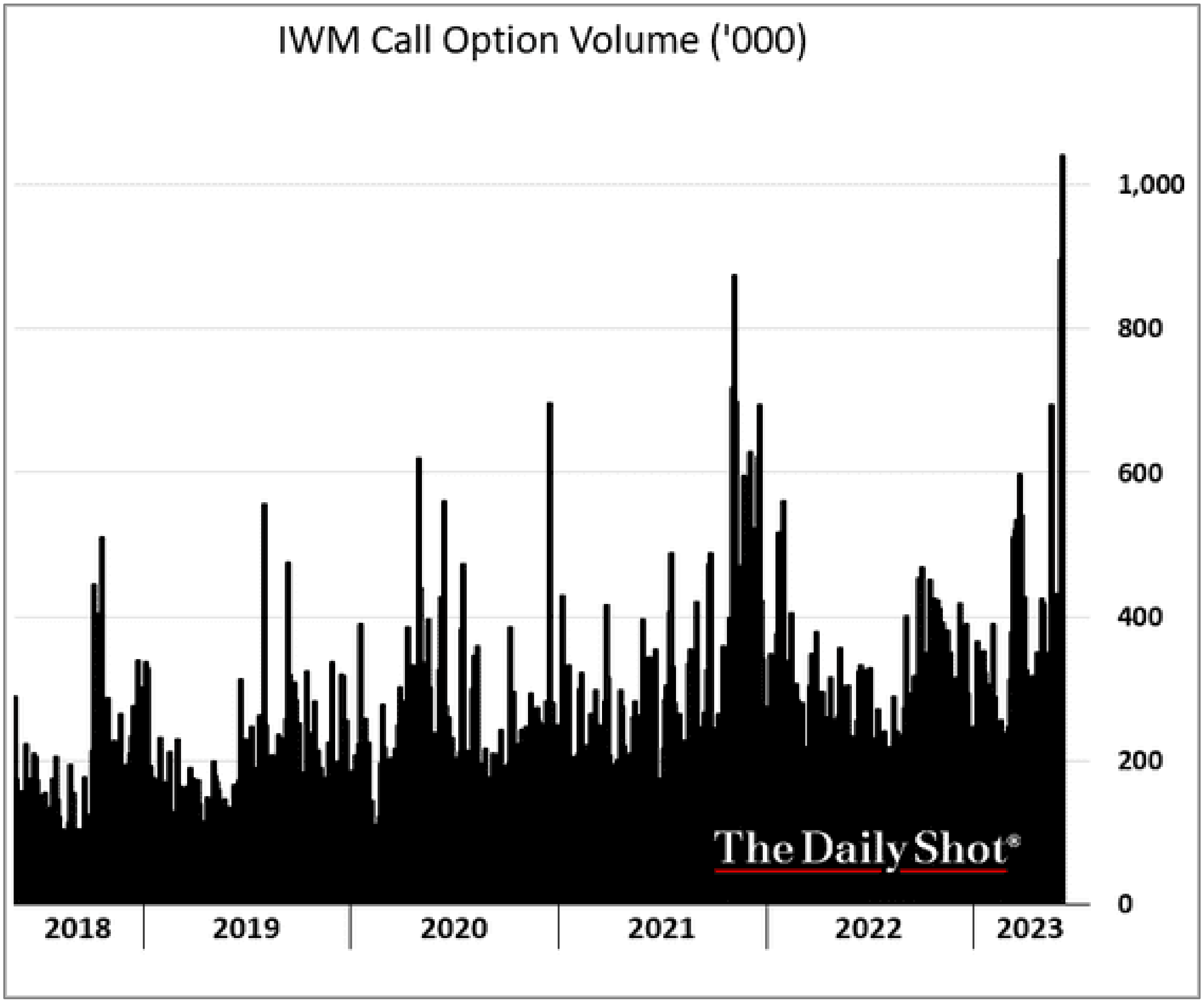
Record Concentration – largest five stocks make up nearly one-fourth of the market's value.

Apple and Microsoft make up nearly 15% of the stock market.

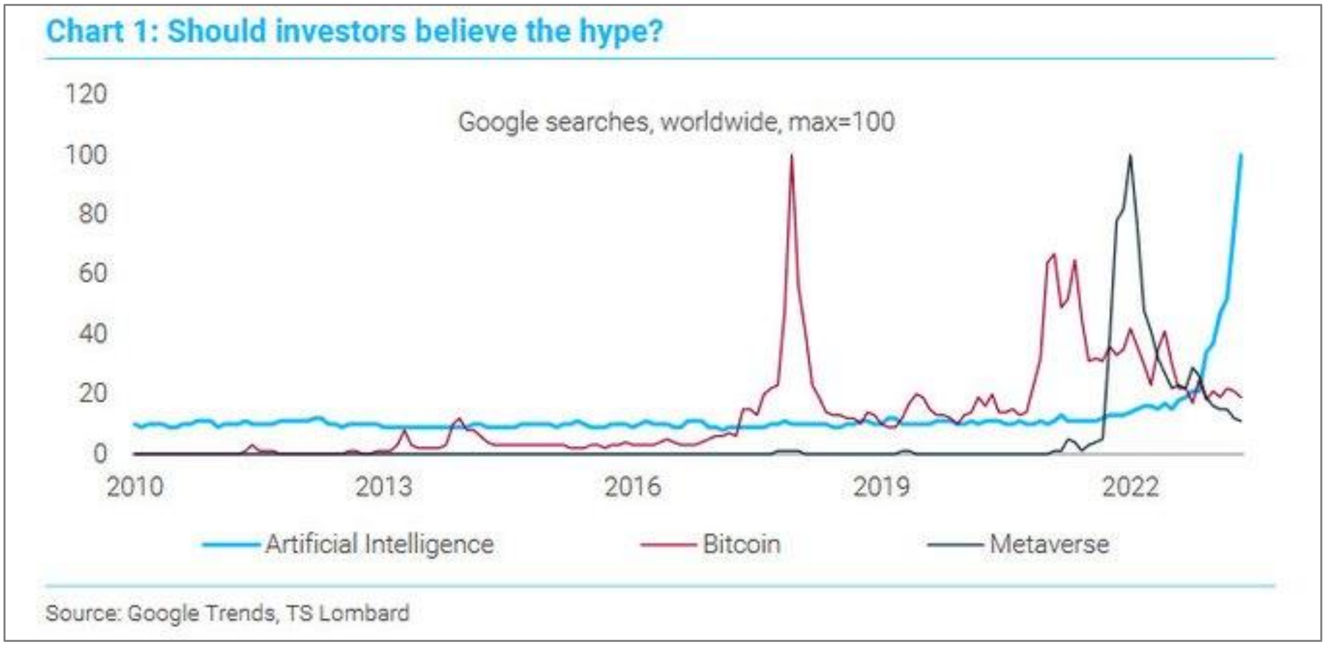
Call Option Volume on the S&P 500 sets a new record.



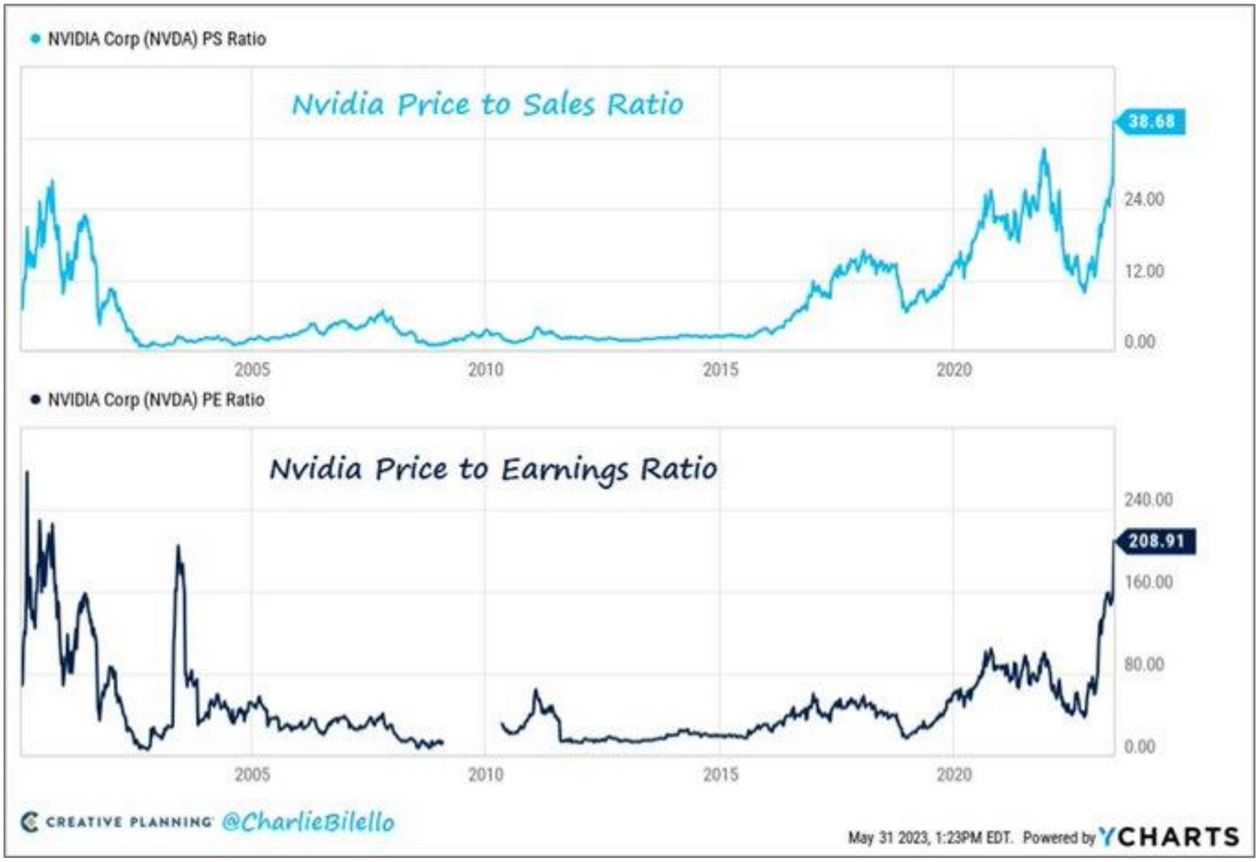
All it took was a one-week rally in small-cap stocks, and Call Option volume on the Russell 2000 set a record.



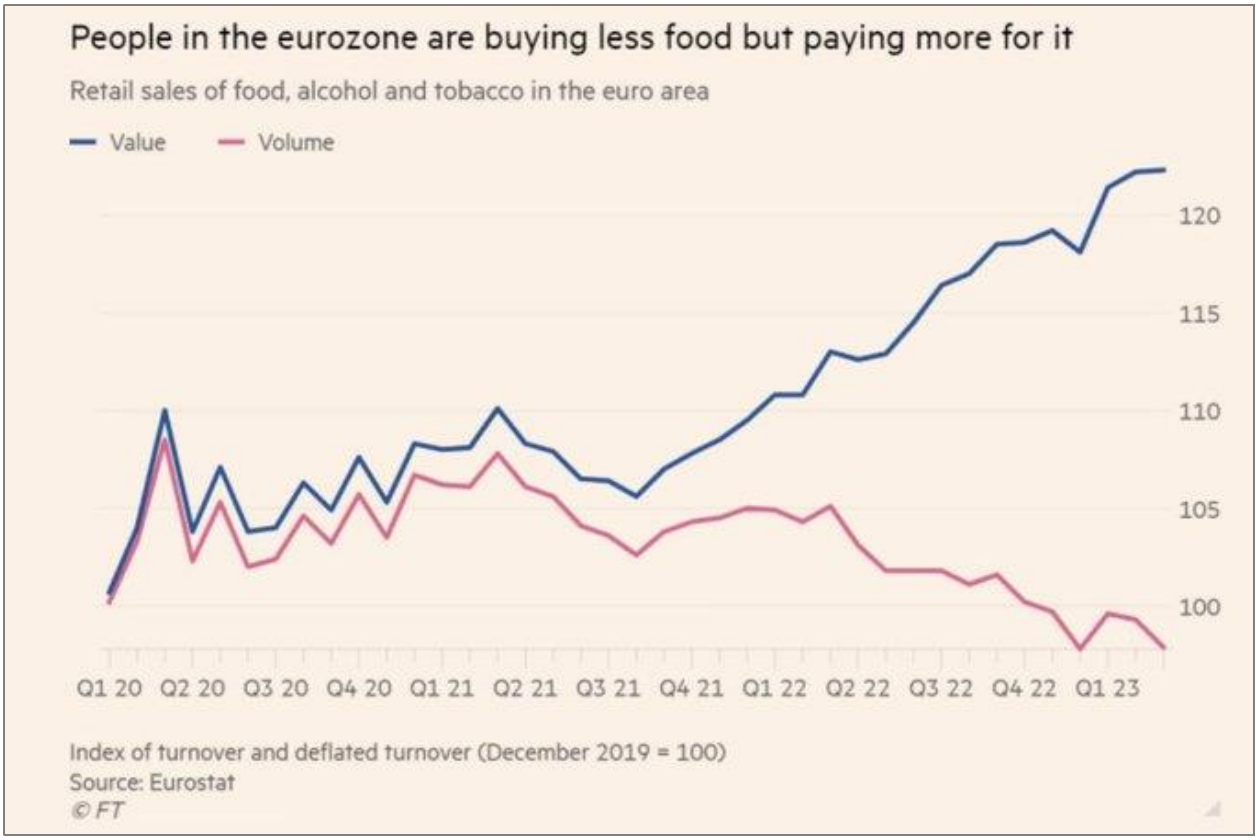
AI Search volume sets a record, already hit Bitcoin levels.



Enthusiasm for AI drives Nvidia valuations to the stratosphere.



Inflation robs the people – Food sales are setting highs while food volume is setting new lows.



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.