



Market Outlook

By Mark T Dodson, CFA

Record Gap between GDP and GDI Growth

Market Risk Index improved to 74.6%, hugging the line that highlights market environments vulnerable to significant drawdowns. Monetary Conditions improved as the bond market hems and haws between signaling Goldilocks and indications of tight monetary policy.

Both Investor Psychology and Valuation worsened, but given that they are in the worst five percent of readings, they can have minimal additional impact on our quantitative view of the risk picture for financial markets.

Net bullishness from the American Association of Individual Investors survey climbed to the highest level since mid-2001. The Consumer Confidence Survey was released for June, showing an expected bump in Consumer Confidence. Both the Expectations Gap and Consumer Confidence in the Job Market remain near all-time highs – inconsistent with readings in the early stages of any other bull market on record.

A curious thing in the economy happened this week as GDP revisions were released. While GDP growth is still positive year over year, Gross Domestic Income, the red-headed stepchild way to measure the nation's economy, has declined for the second quarter in a row. It's the widest divergence between the two measures of the economy on record, having broken the previous record from Q4 2007.

In theory, both measures should yield the same result, but in other instances where their results have diverged, the informational edge has gone to GDI growth. This is the seventh time since 1947 that GDI growth has been negative while GDP growth was positive. The previous six times this occurred, the economy was either already in recession or a recession was forthcoming the next quarter.

Market Risk Index

Rec Allocation 25% Underweight

74.6%

Category Percentiles

Psychology - P6



Monetary - M3



Valuation - Extremely Overvalued



Trend



Largest Psychology Influences

Leveraged Investments	Negative
Option Activity	Negative
Flow of Funds	Negative
Bank Sentiment	Negative

Largest Monetary Influences

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

Valuation

7-10 Year Equity Return Forecast	1.6%
10Yr US Treasury Yield	3.7%

Market Trends

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

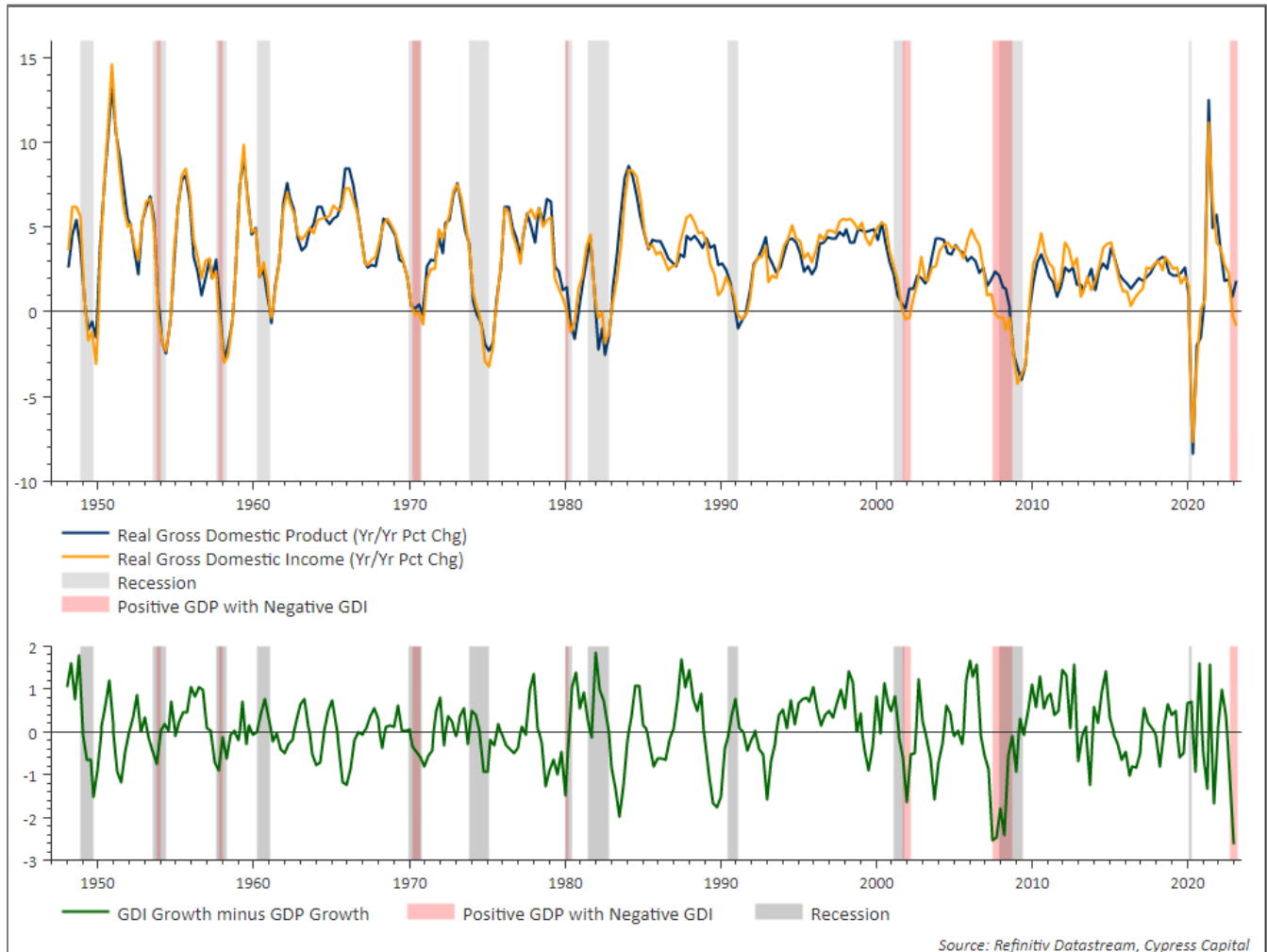
Market Risk Index scales from 0 to 100%. Higher readings correspond with higher risk markets. Scores below 25% are bullish. Scores between 25-75% are neutral, and scores above 75% are markets vulnerable to major drawdowns.

With the second quarter coming to a close, we have no changes in recommended allocations to report. Still, we spent most of the quarter trimming equity positions on market strength inside managed portfolios.

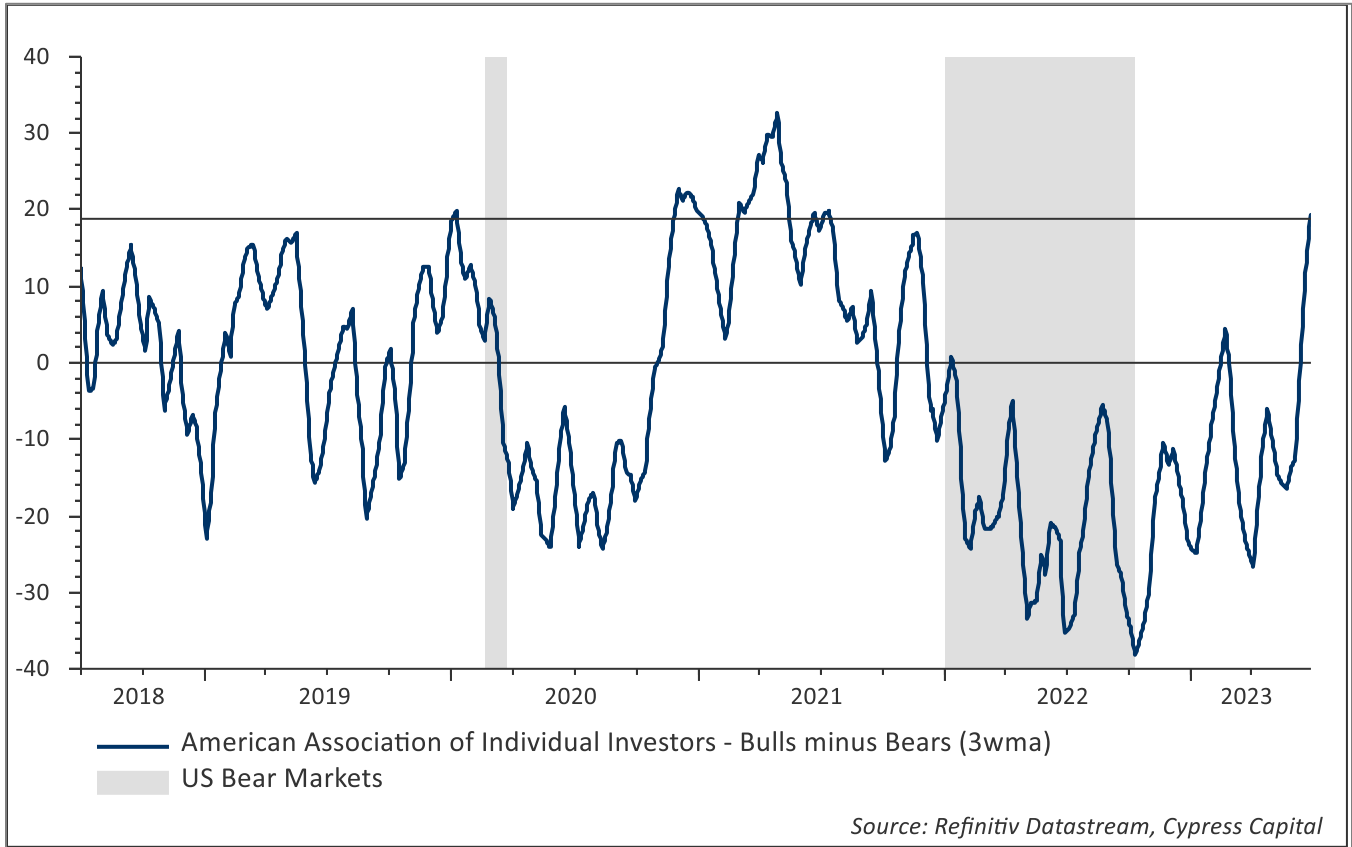
Charts of the Week

Two Measures of the Economic Output – Two Different Messages

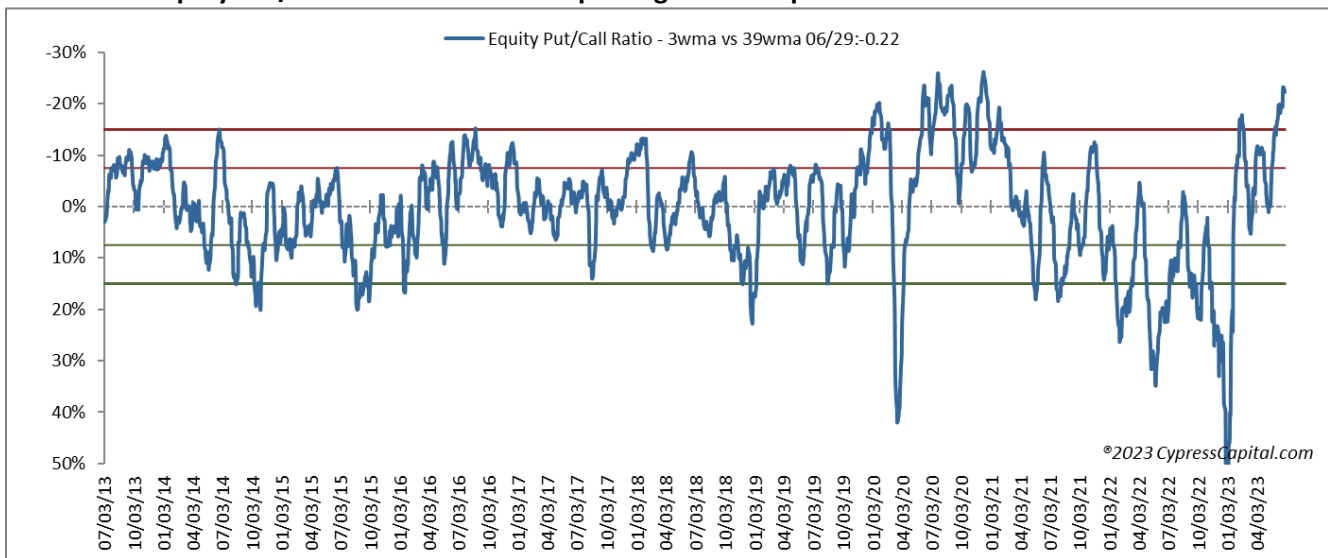
The spread between Gross Domestic Product and Gross Domestic Income growth set a record. In every other instance where GDI growth was negative, and GDP growth was positive, a recession was either already underway or forthcoming.



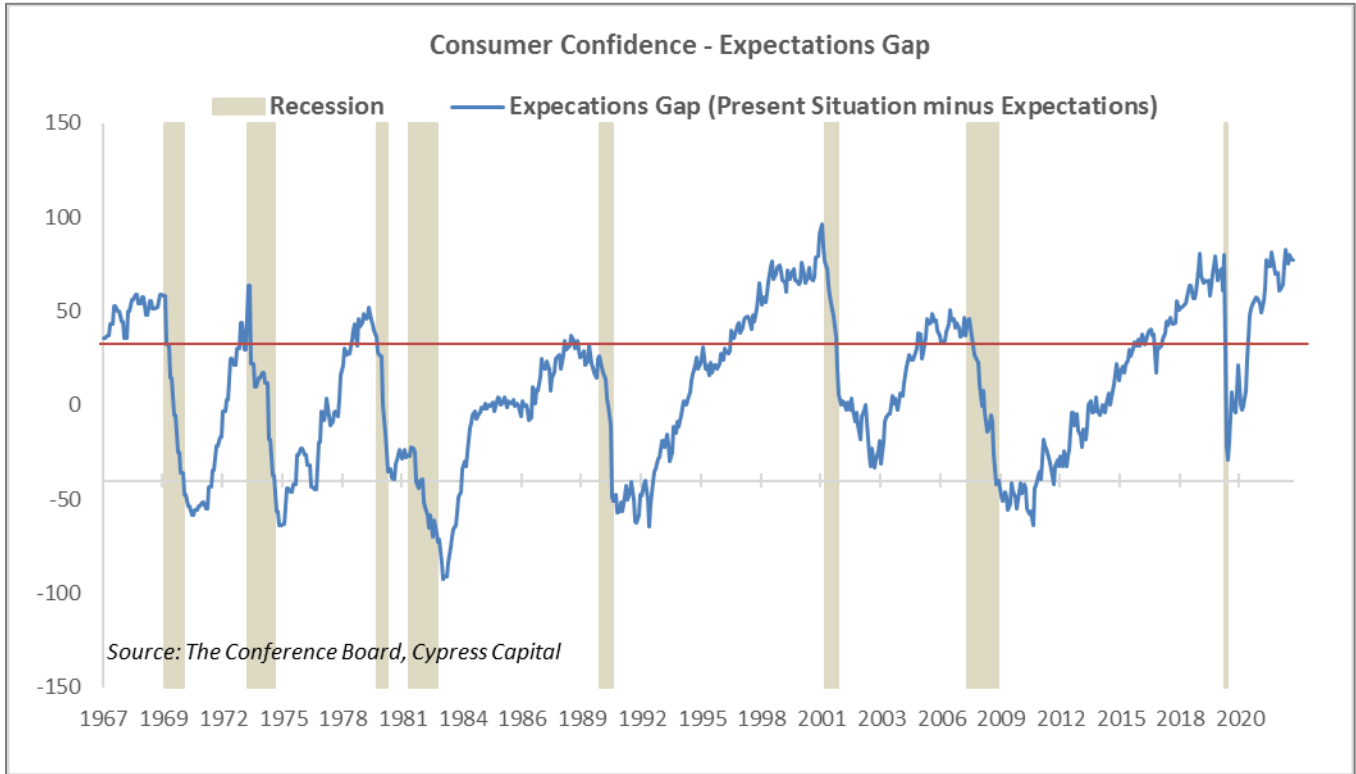
Individual Investor Net Bullishness has climbed to the highest level since mid 2021.



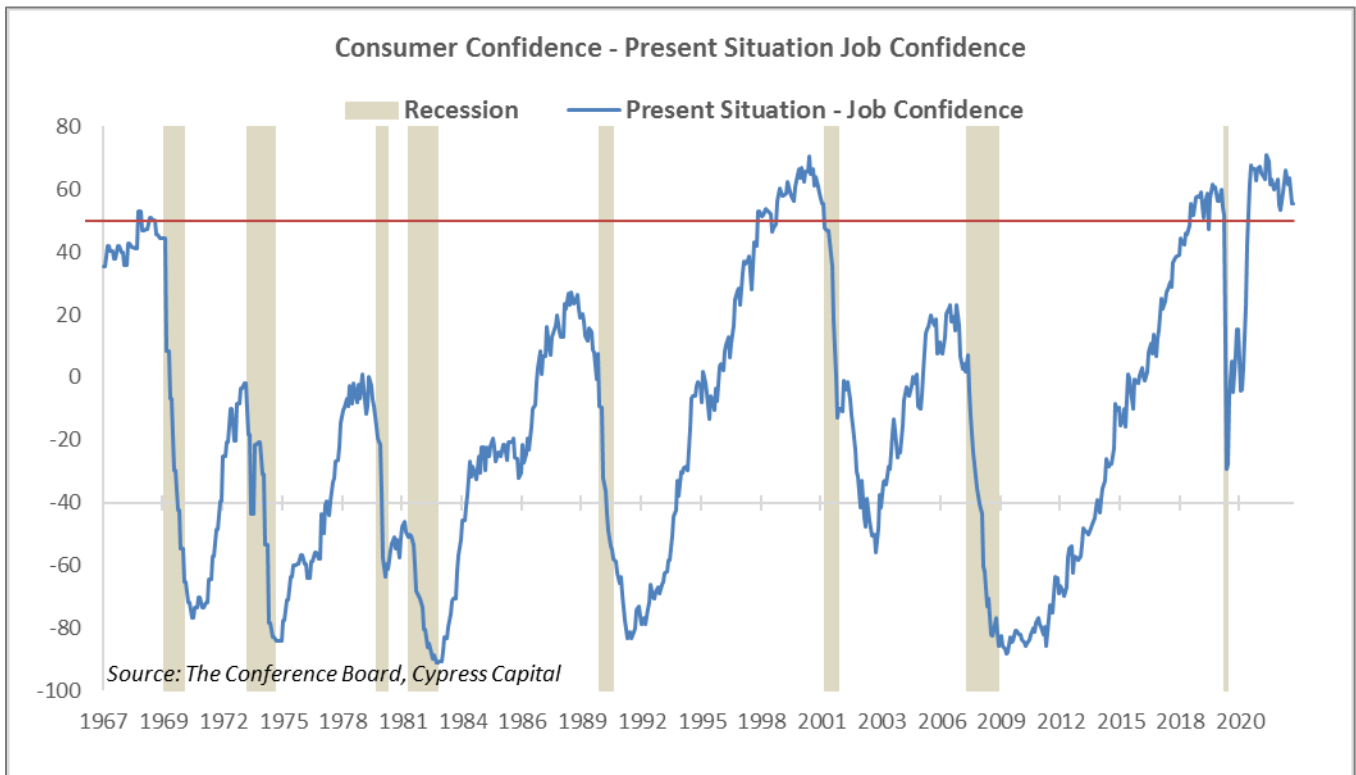
De-Trended Equity Put/Call Ratio is close to surpassing 2021's euphoric extreme.



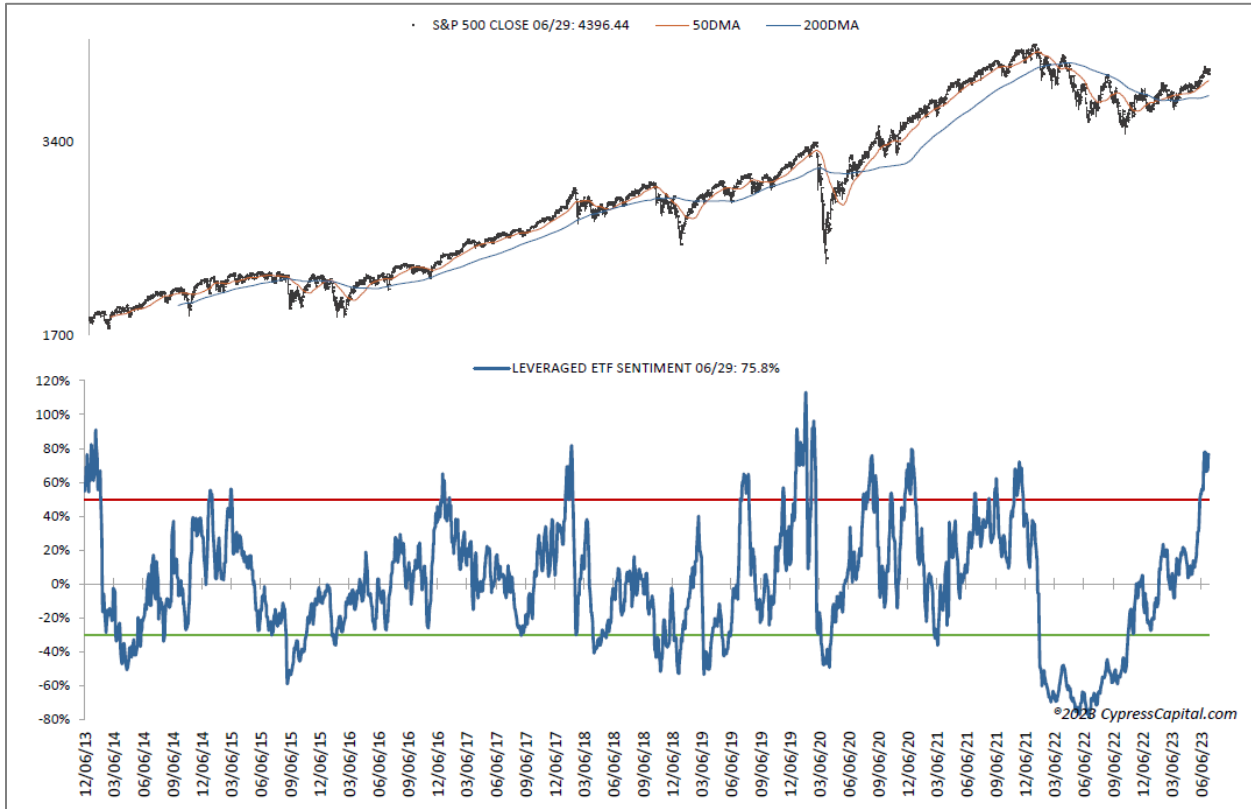
Consumer Confidence Expectations Gap is hovering at highs.



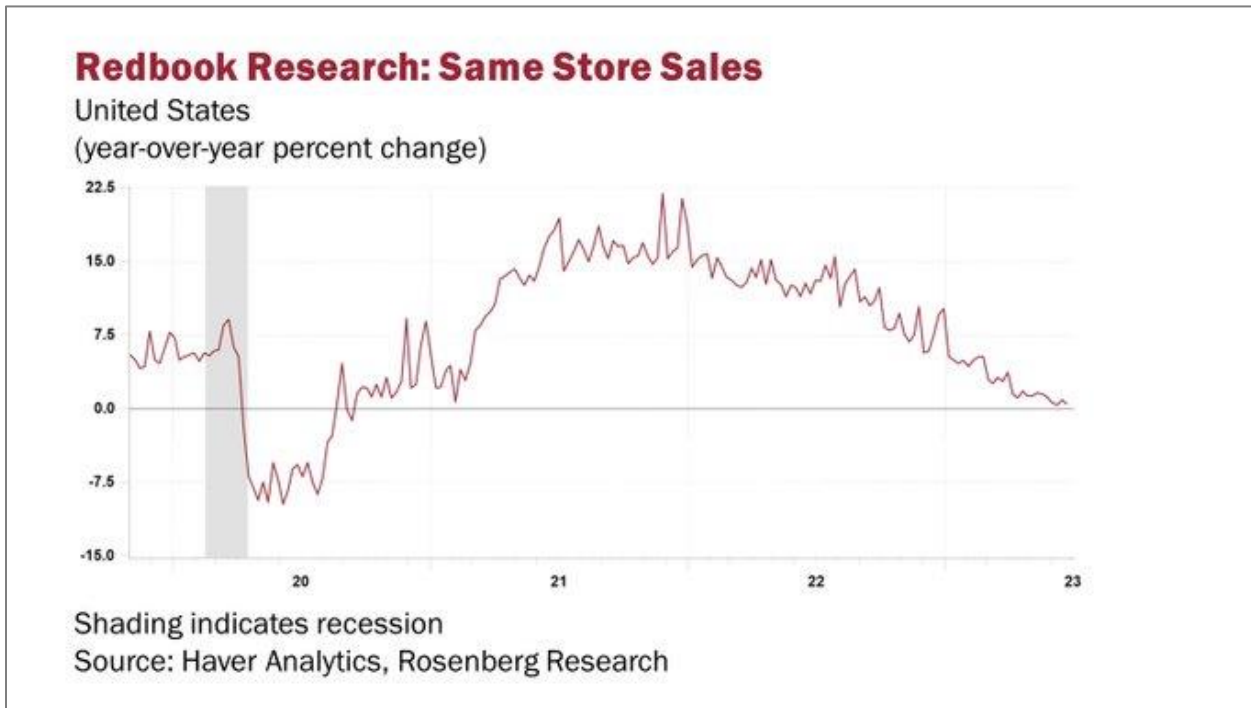
Consumer Confidence in the Job Market softened but has remained resilient and elevated.



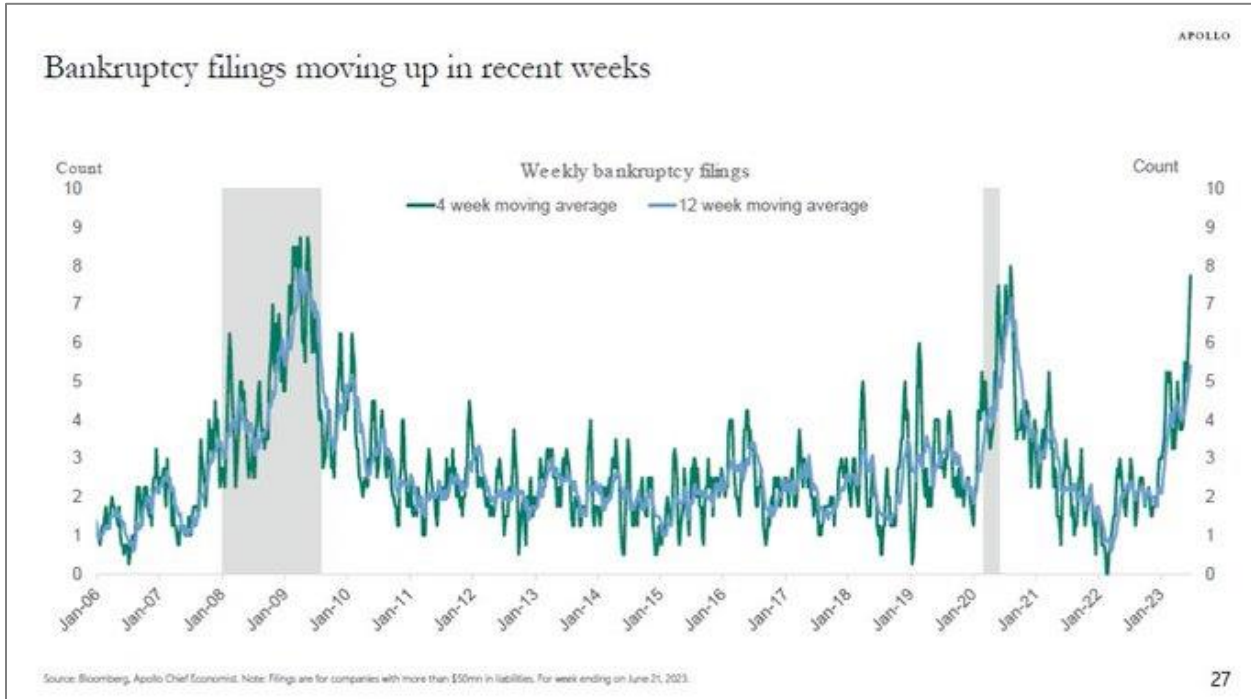
Leveraged ETF Volume Sentiment hit the highest levels since early 2020.



Same Store Sales continue to soften.

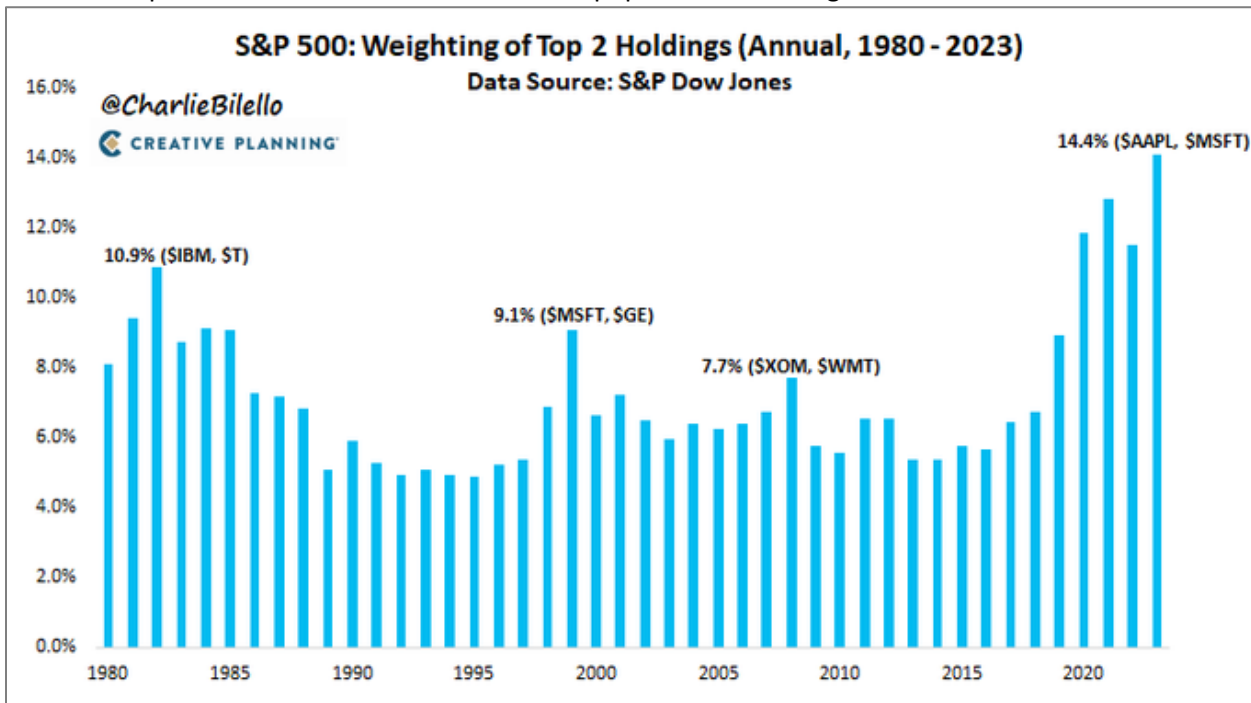


Weekly Bankruptcy filings are creeping up.

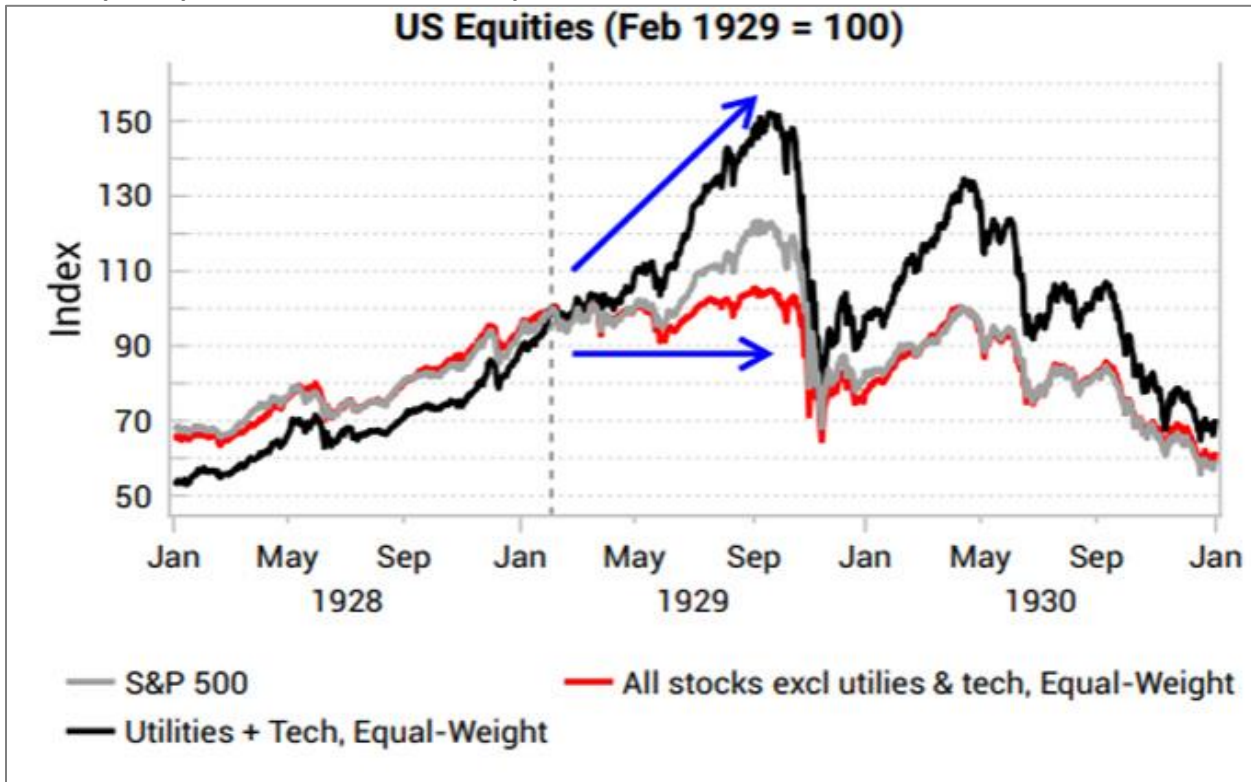


Apple and Microsoft make up more than 14% of the S&P 500.

Don't be surprised if anti-trust headlines become popular over coming months.

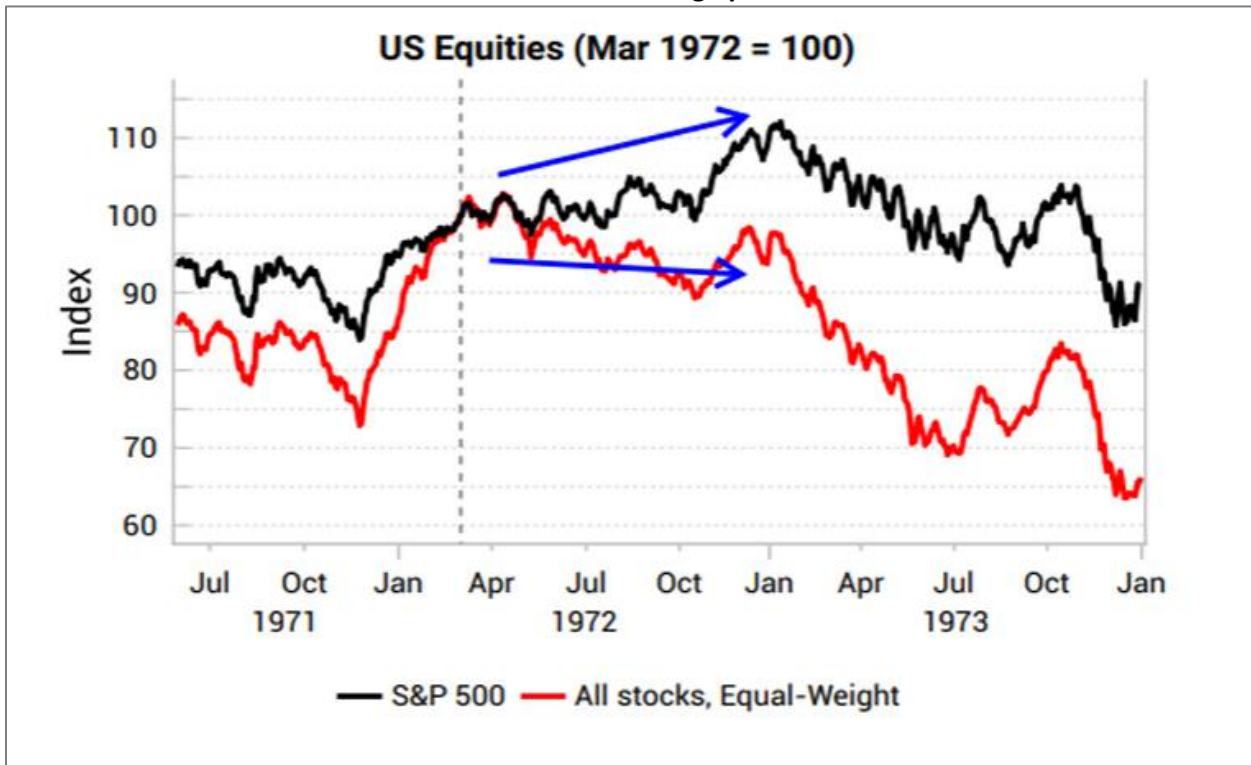


Narrow participation markets are often a precursor to bear markets. See 1929 below.



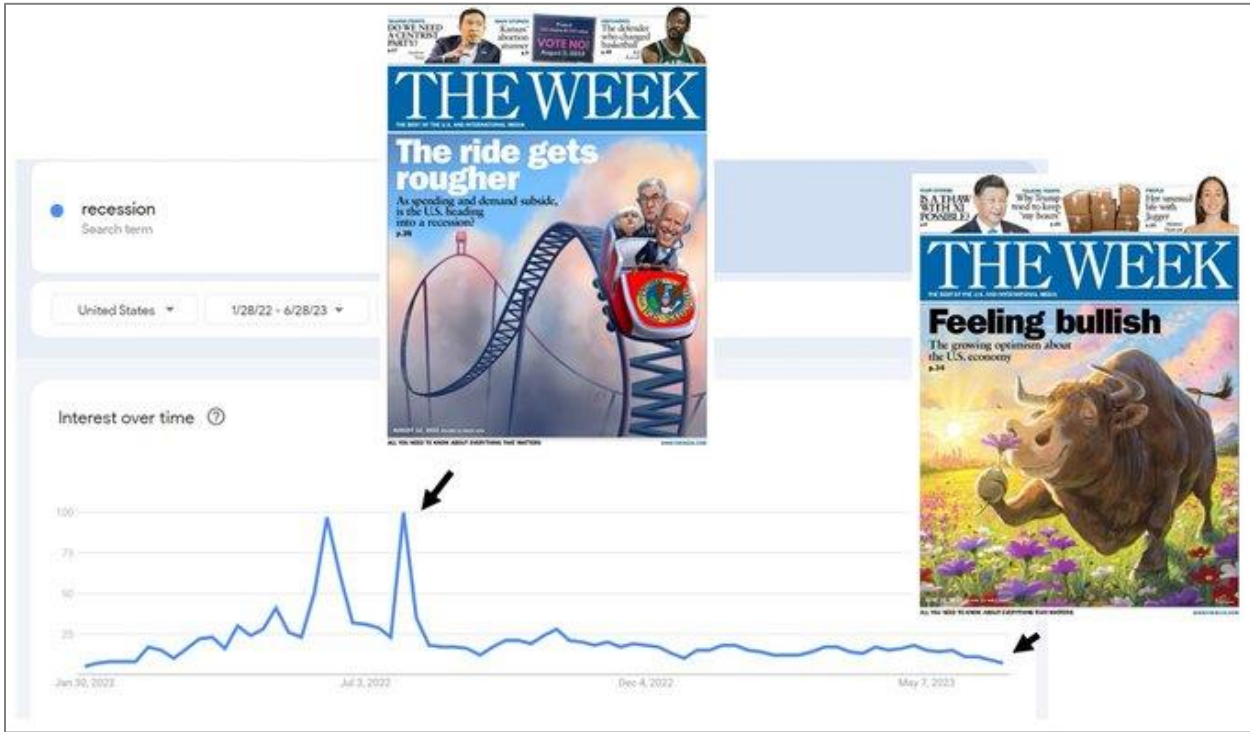
Source: Variant Perception

The same can be said for the market environment leading up to the 1974 bear market.



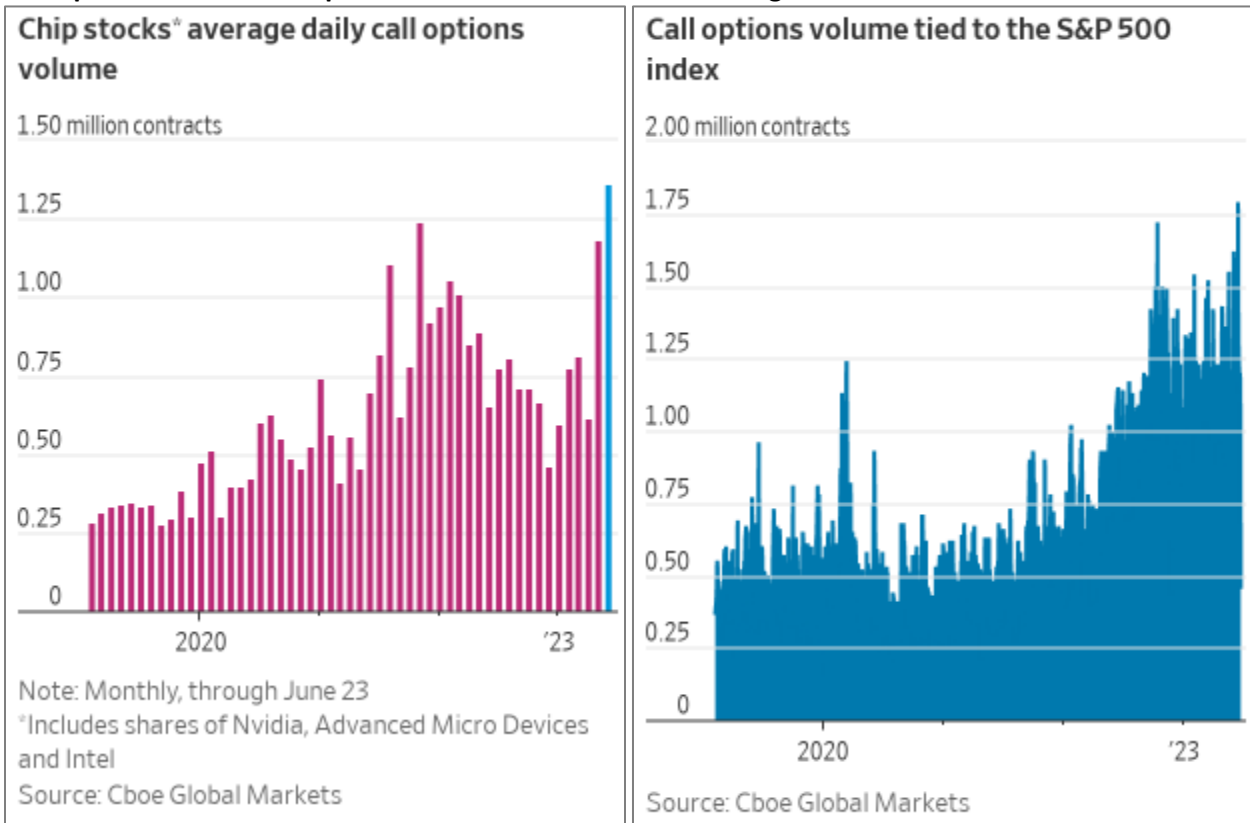
Source: Variant Perception

Magazine Cover Sentiment is Bullish Again.

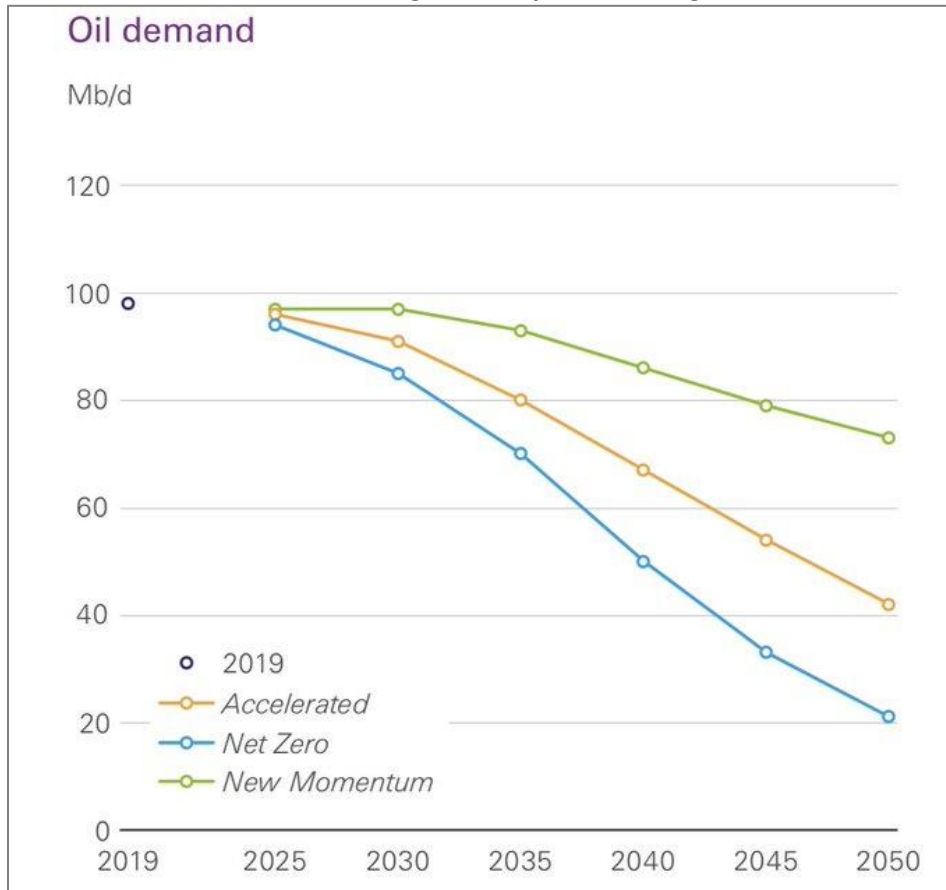


Source: @Peter_Atwater

Call Options Volume in Chip stocks and the S&P 500 are setting records.

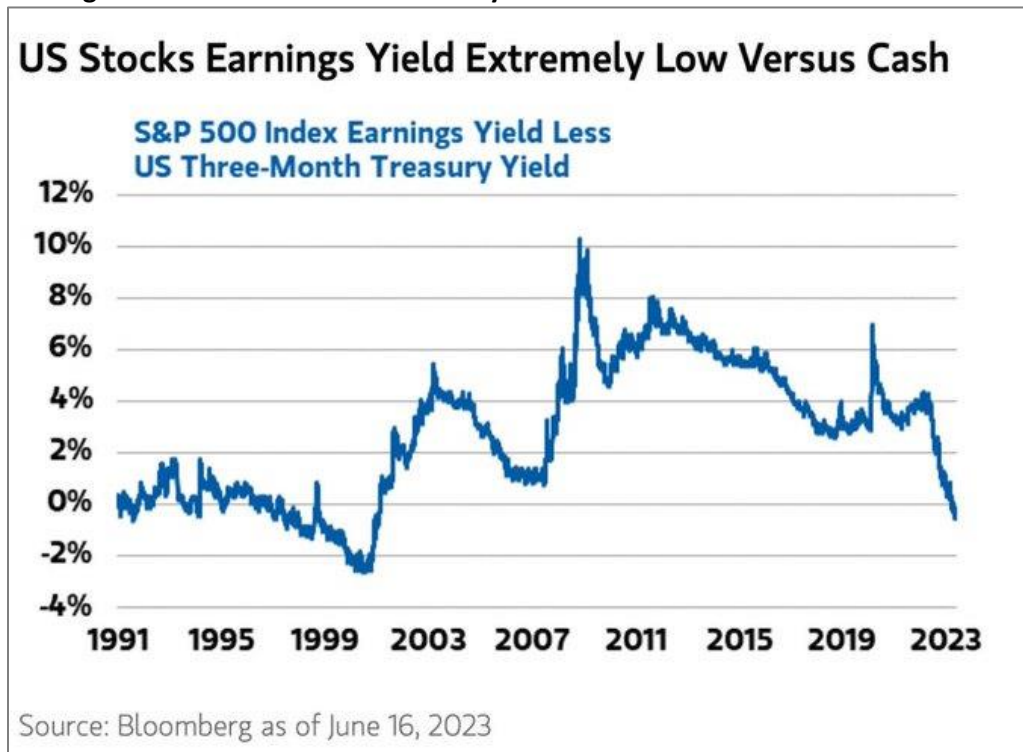


BP's Outlook for Oil Demand has global despots sweating.



Source: Michael Arouet

Earnings Yield on stocks falls below the yield on Cash for the first time since 2000.



Savings Rates aren't far from record lows.

Chart 9: US consumer savings rate only 4.1%, below 9% LT average...
US personal savings rate since 1929



Source: BofA Global Investment Strategy, Global Financial Data

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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