



Market Outlook

By Mark T Dodson, CFA

Banks Continue to Tighten Their Belts

Market Risk Index increased to 78.6% this week, still above the 75% level associated with market environments ripe with bear market level drawdown risk. Both Psychology and Monetary Conditions worsened but were partially offset by improved Valuations on recent stock market weakness.

Bank Sentiment became one of the four largest detractors from the Psychology Composite. The Senior Loan Survey was released for Q3, and banks continue to tighten lending standards – banks have never tightened lending standards to this extent without a recession occurring. Loan Charge-offs tend to swell about nine months later – with 2020 being an exception – as \$5 trillion in stimulus bailed out everyone's bad decisions.

Leveraged Investments and Options Activity showed signs of peaking this week, as two weeks of stock market weakness caused aggressive investors to re-think their euphoric levels of risk-taking. However, the improvement was only marginal and has not been significant enough to cause a retreat from the high-risk readings coming from the Psychology Composite.

With so little fuel for even a run-of-the-mill cyclical bull market and Treasury bills priced to return more than the stock market for the first time since 2000, we don't anticipate increasing equity allocations until the weight of the evidence shifts in favor of a better risk-reward for stocks.

Market Risk Index

Rec Allocation 25% Underweight

78.6%

Category Percentiles

Psychology - P6



Monetary - M3



Valuation - Extremely Overvalued



Trend



Largest Psychology Influences

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

Largest Monetary Influences

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

Valuation

7-10 Year Equity Return Forecast	1.6%
10Yr US Treasury Yield	4.0%

Market Trends

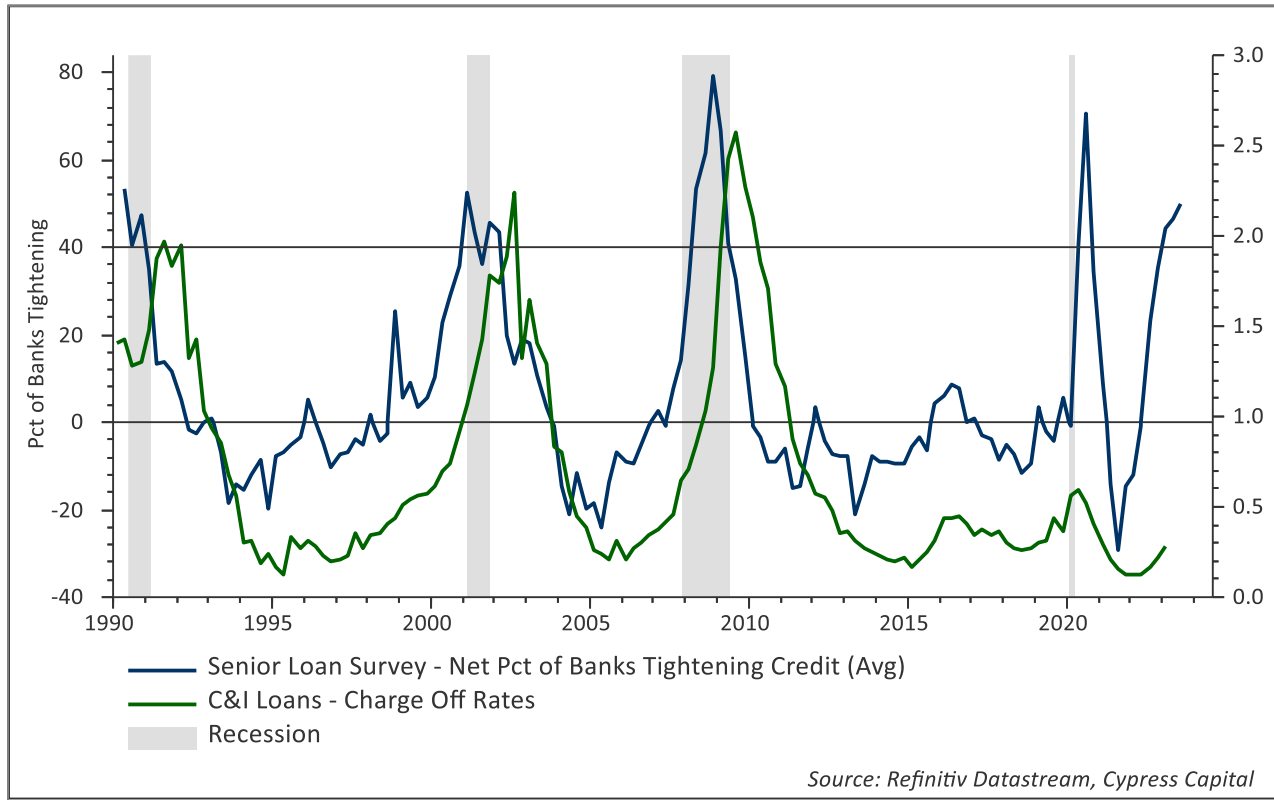
US Equities	Bullish Trade
Intl Equities	Bullish Trade
REITs	Bullish Trade
Broad Commodities	Bullish Trade

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.

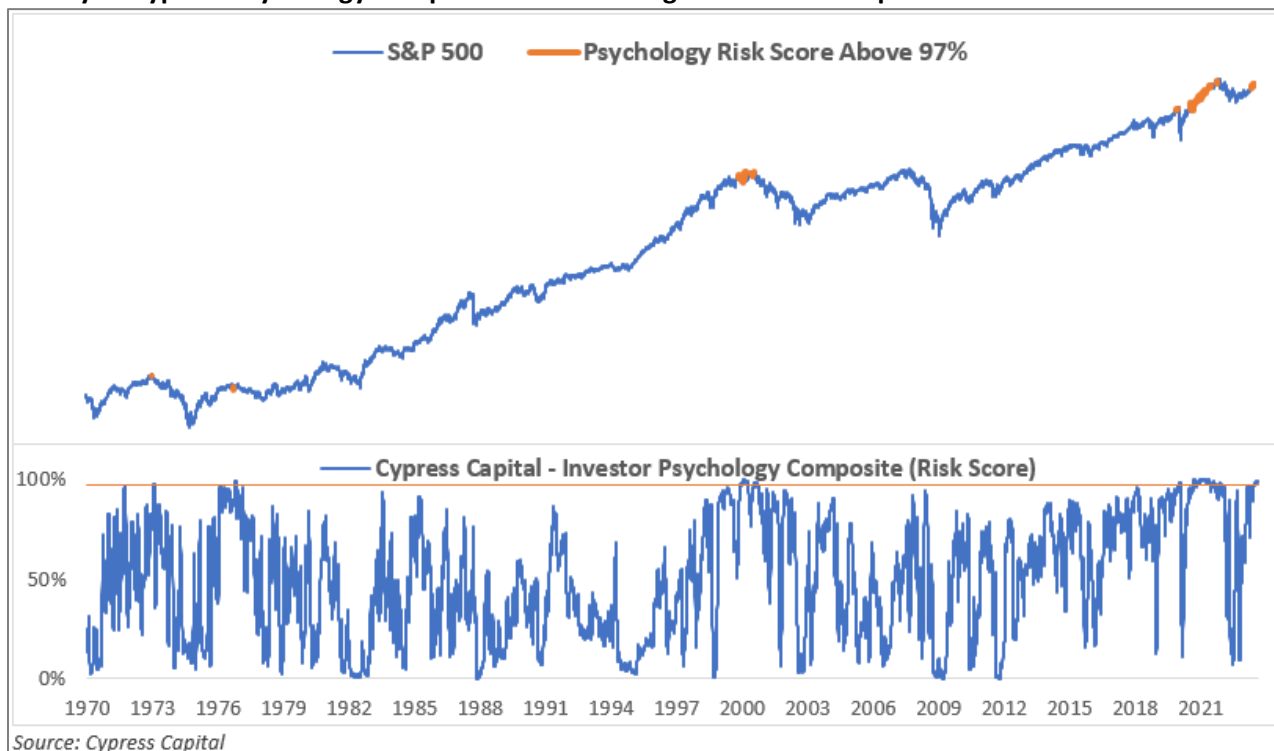
Charts of the Week

Banks continue to tighten Credit.

Banks have never tightened Credit to this degree without a recession. Commercial & Industrial loan charge-offs tend to peak around nine months later on average.



History of Cypress Psychology Composite Score readings above the 97th percentile

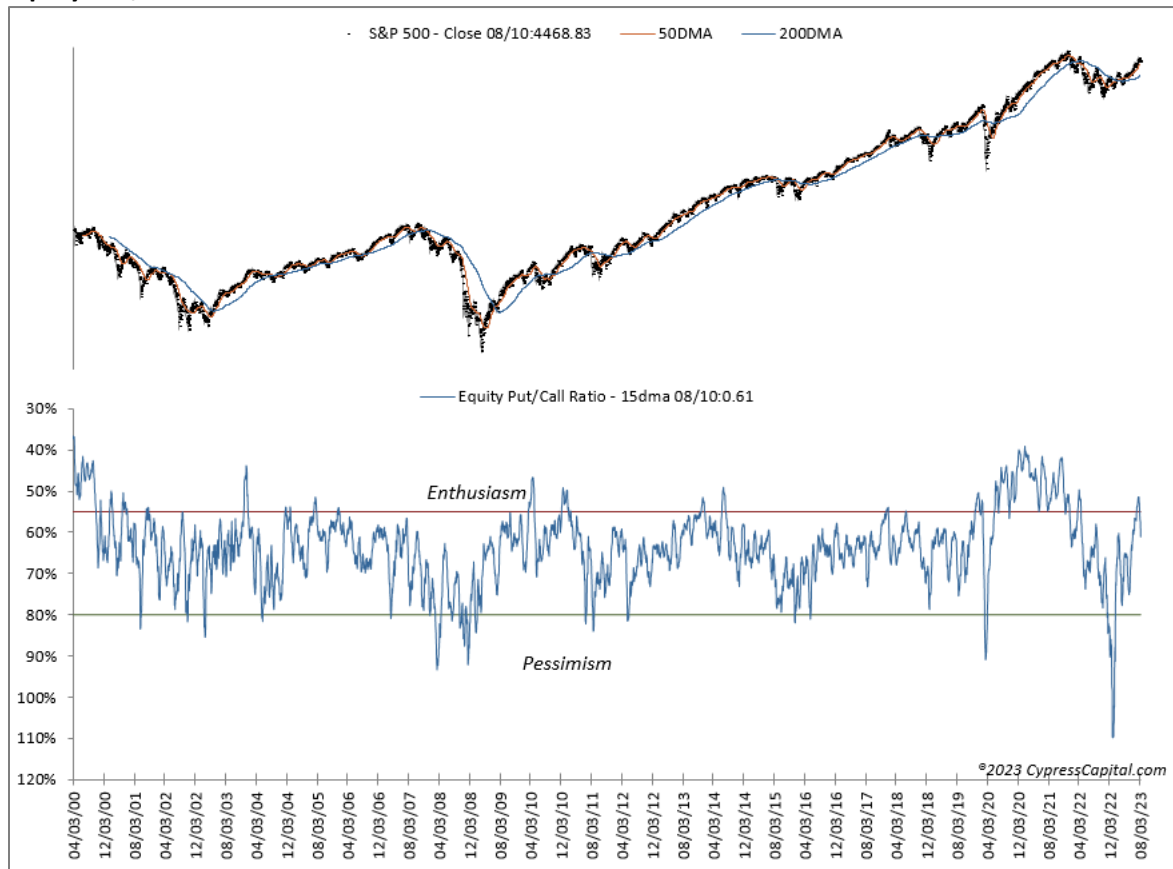


In case you missed it, the earnings yield on the S&P 500 has fallen below Treasury-Bill yields.

Cash is priced to return more than the stock market for the first time since 2000, another period when investors became desperate to avoid missing out on Tech stocks' promise.

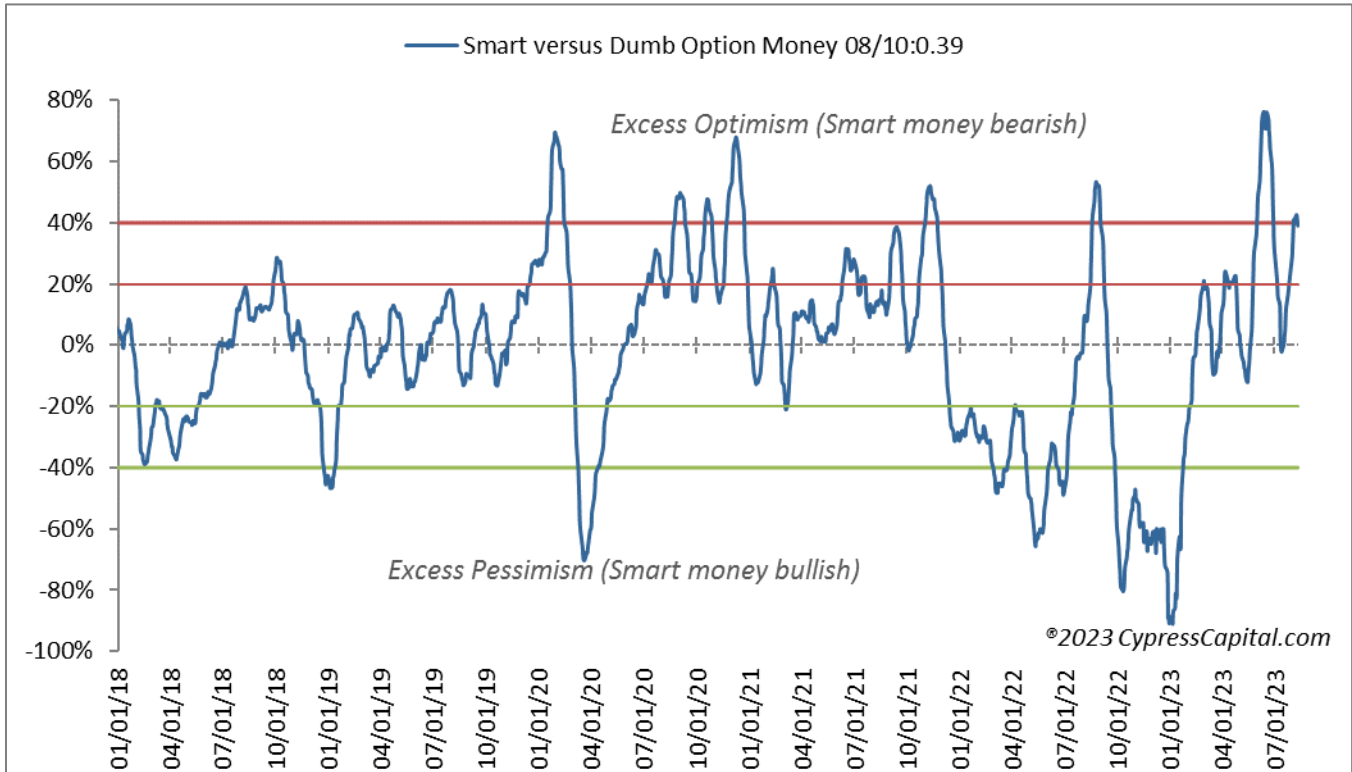


Equity Put/Call Ratio retreated from Greed.

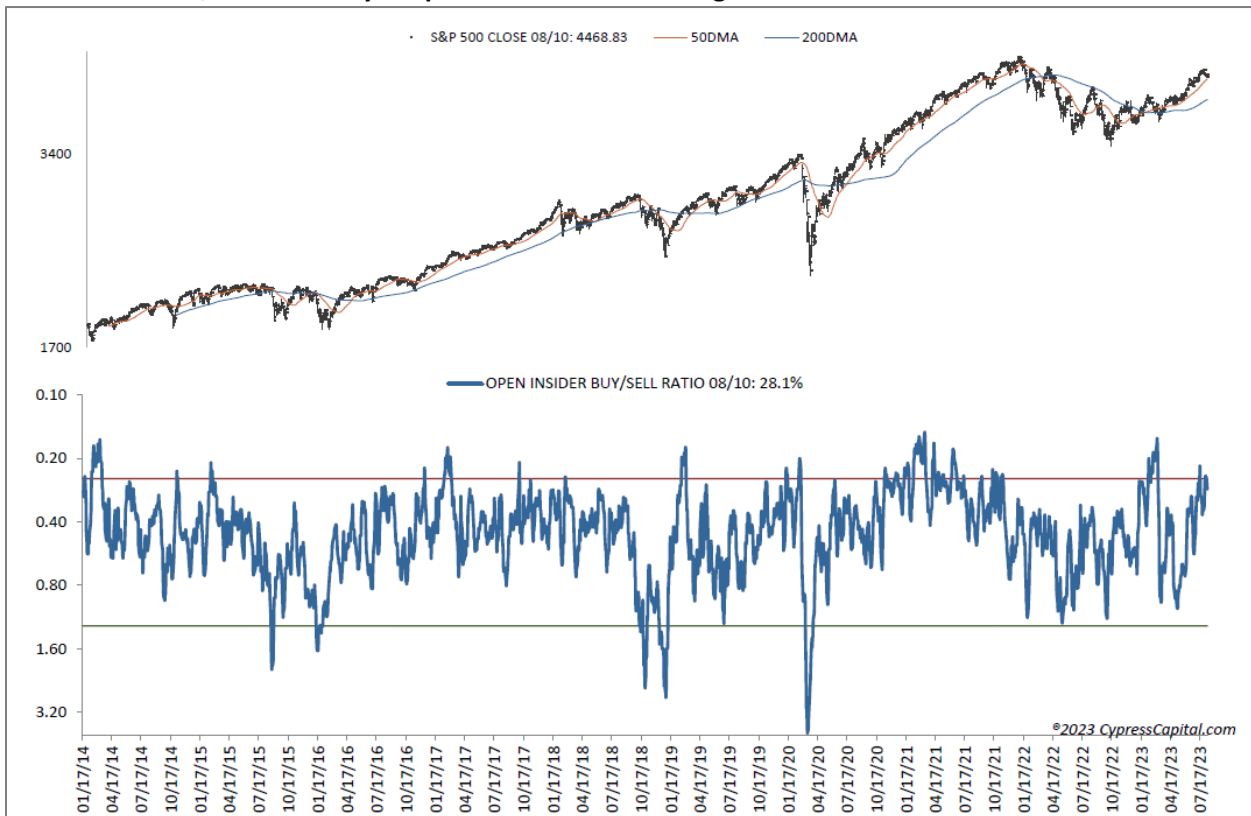


However, Smart versus Dumb Option Money moved back into the red zone.

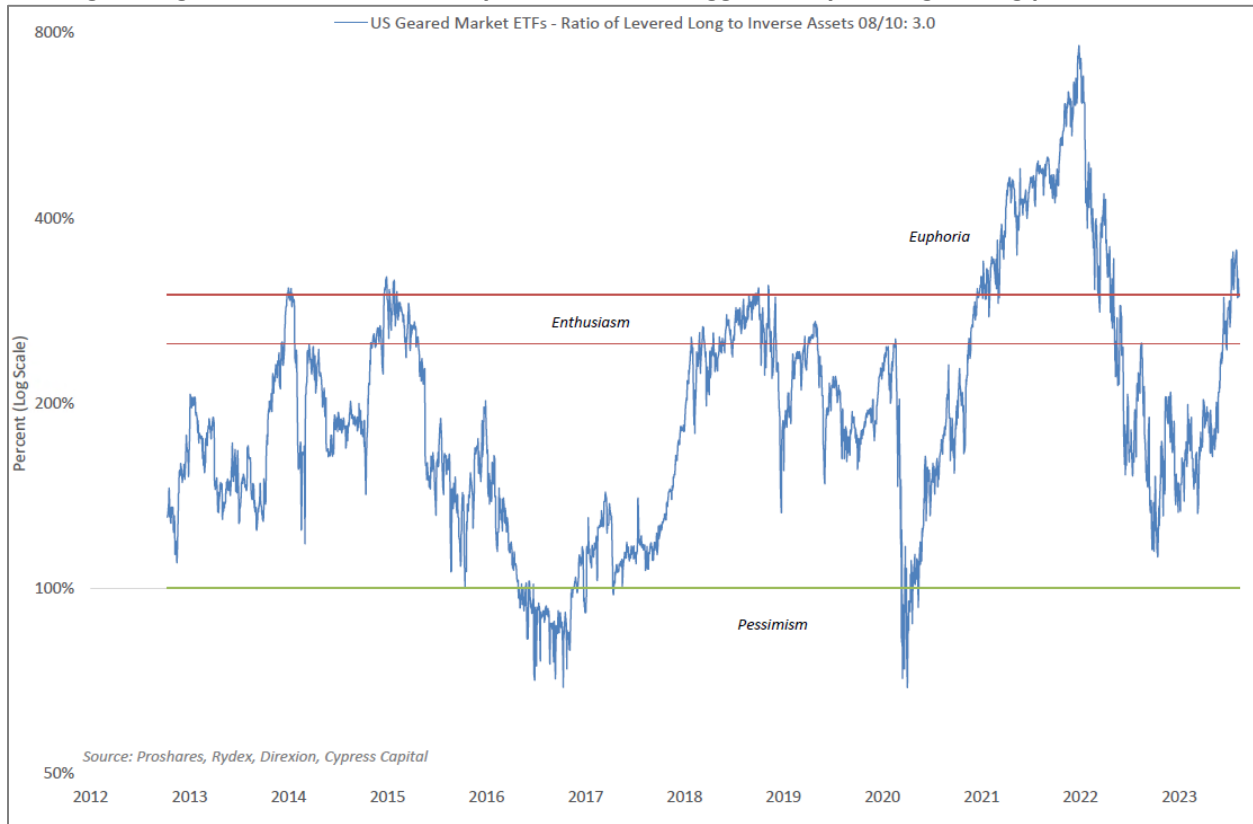
The dumb-money retreat in optimism wasn't enough to offset the increase in bearishness from smart money options traders.



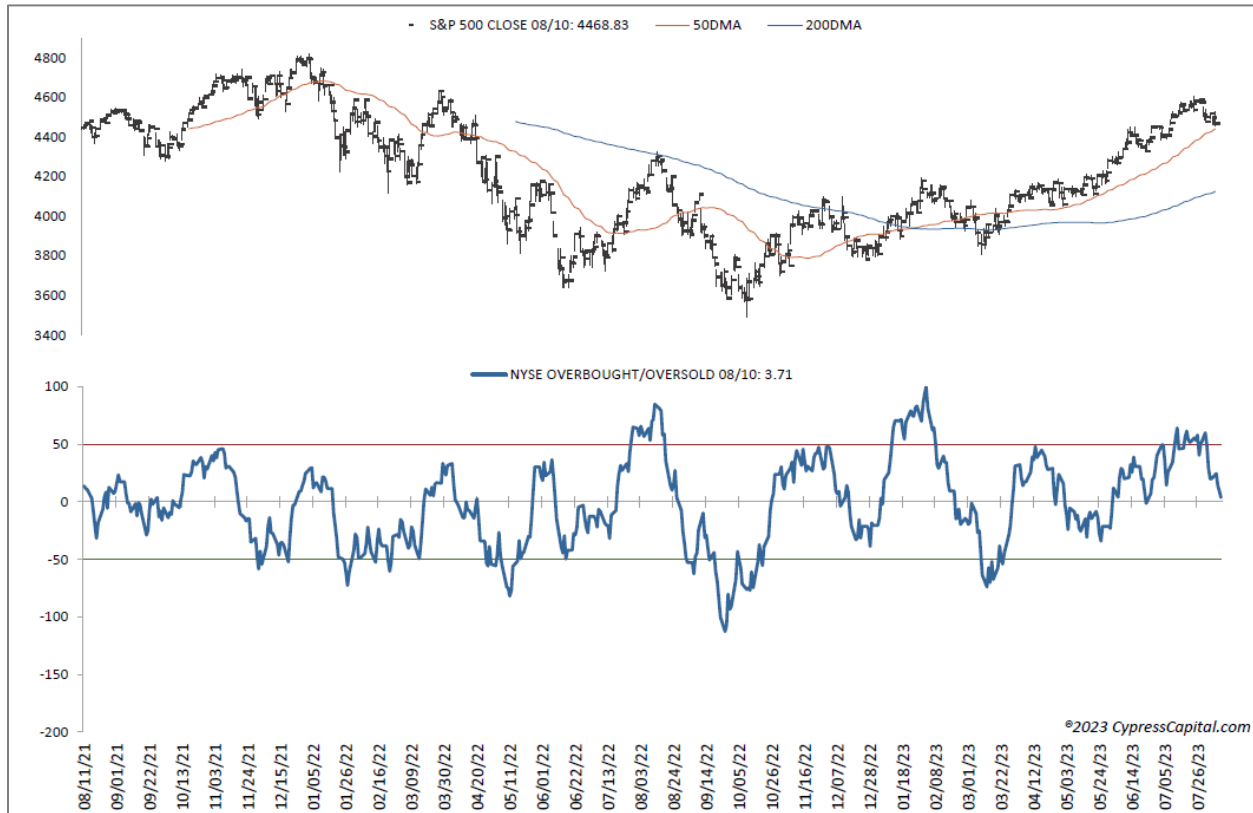
Similar to above, smart money Corporate Insiders haven't grown more bullish.



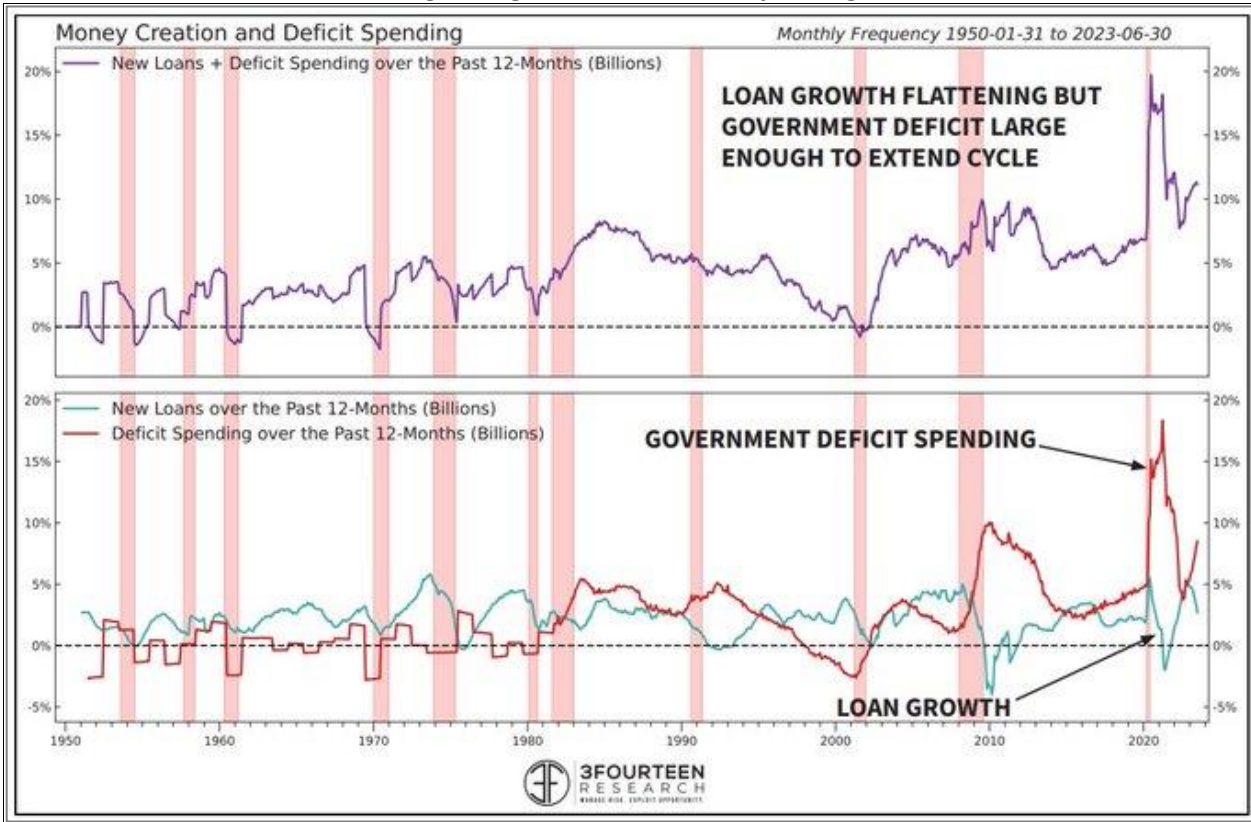
Leveraged long ETF investors stubbornly held onto their aggressively leveraged long position.



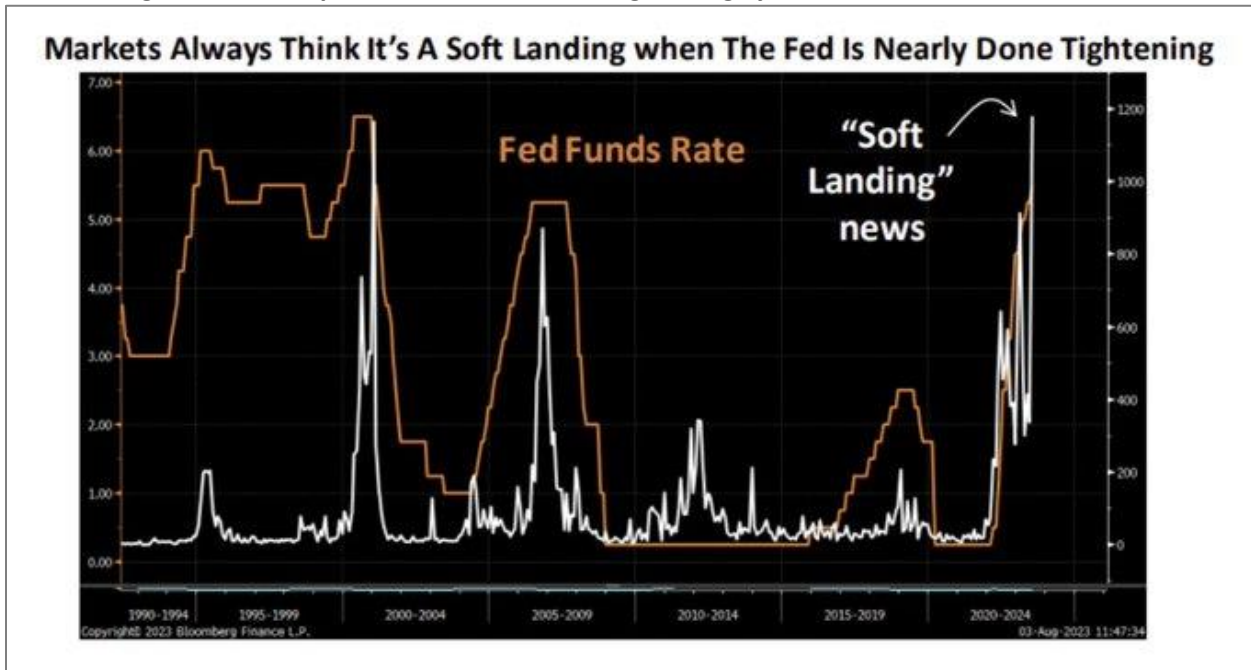
Back to Neutral - recent pullback has alleviated the stock market's overbought condition.



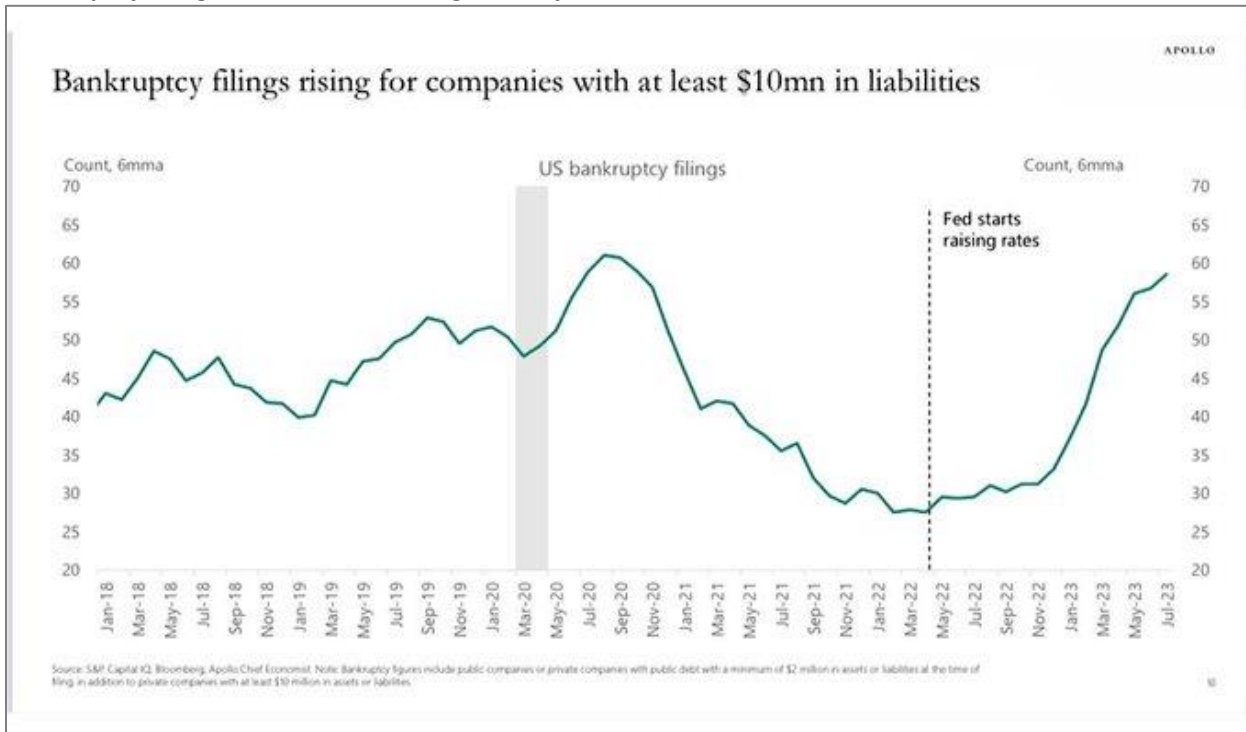
A Bull Market whose existence hinges on government deficit spending?



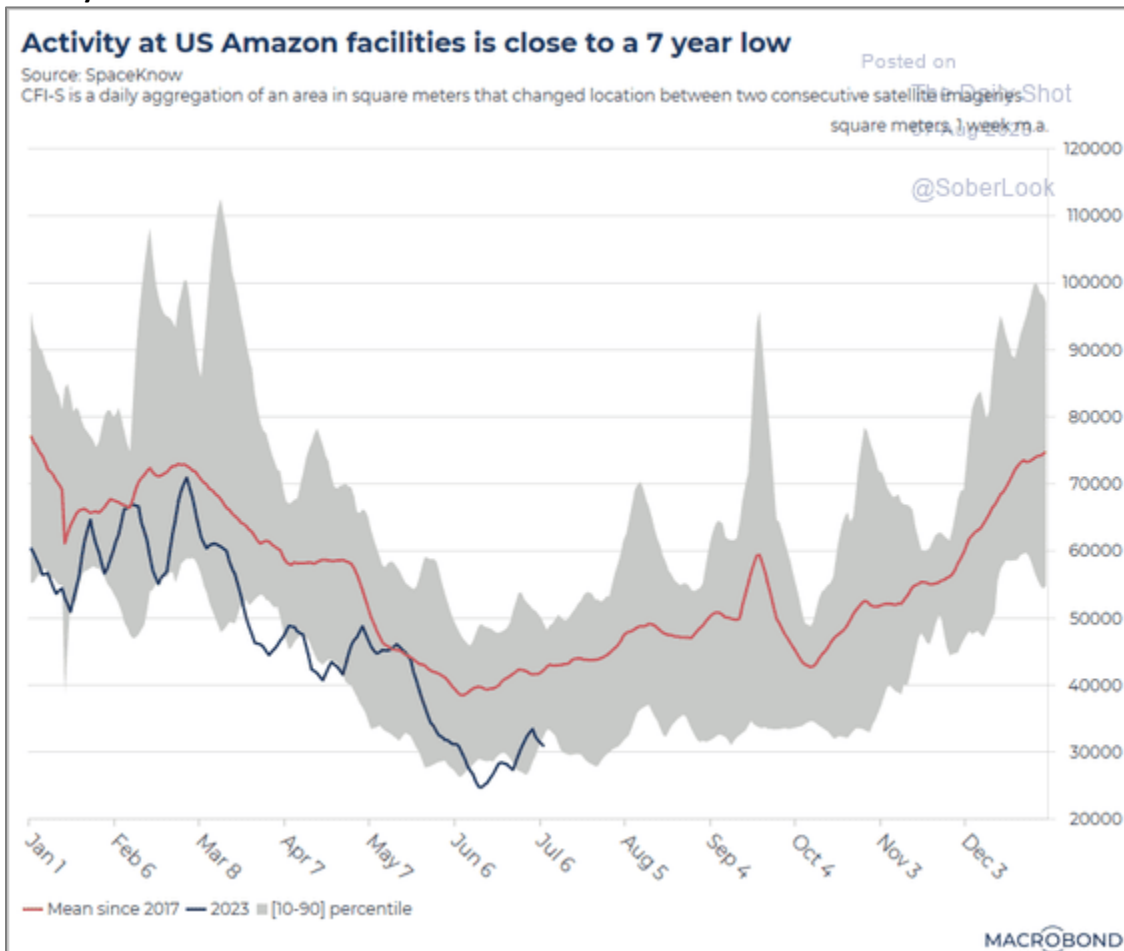
Soft Landing news stories peak at the ends of Fed tightening cycles.



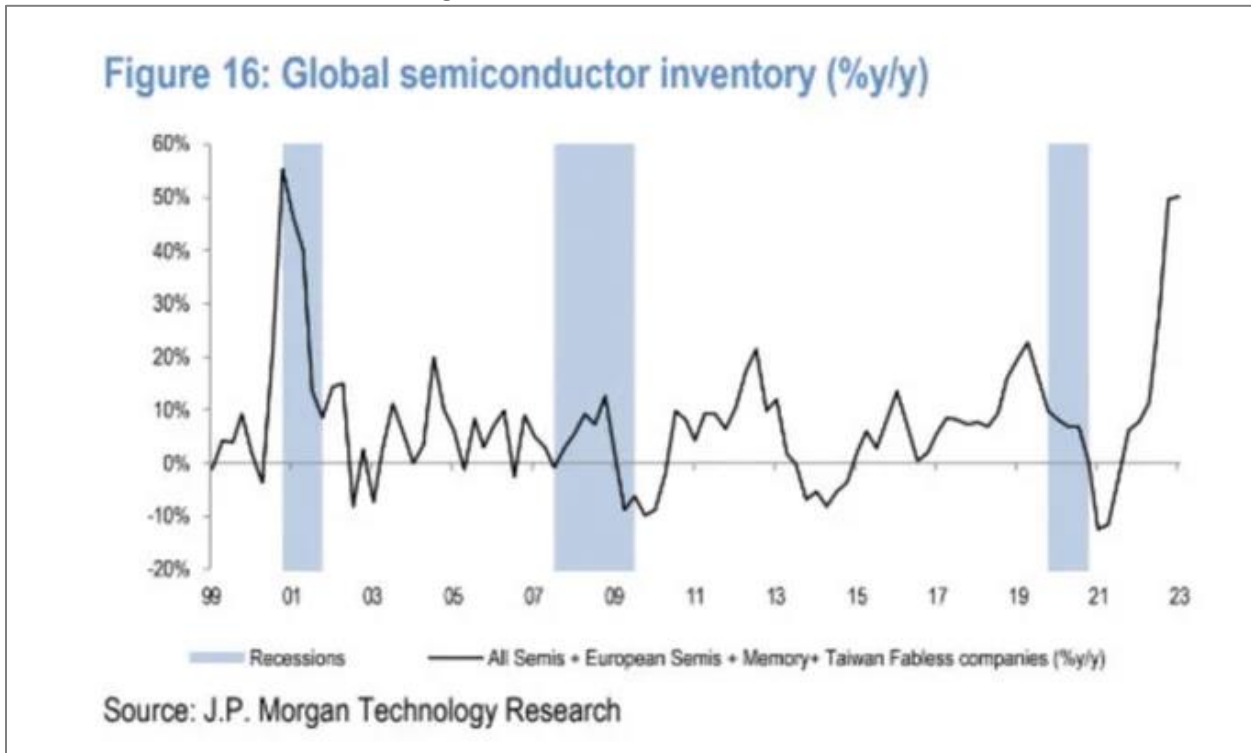
Bankruptcy filings have been climbing steadily in 2023.



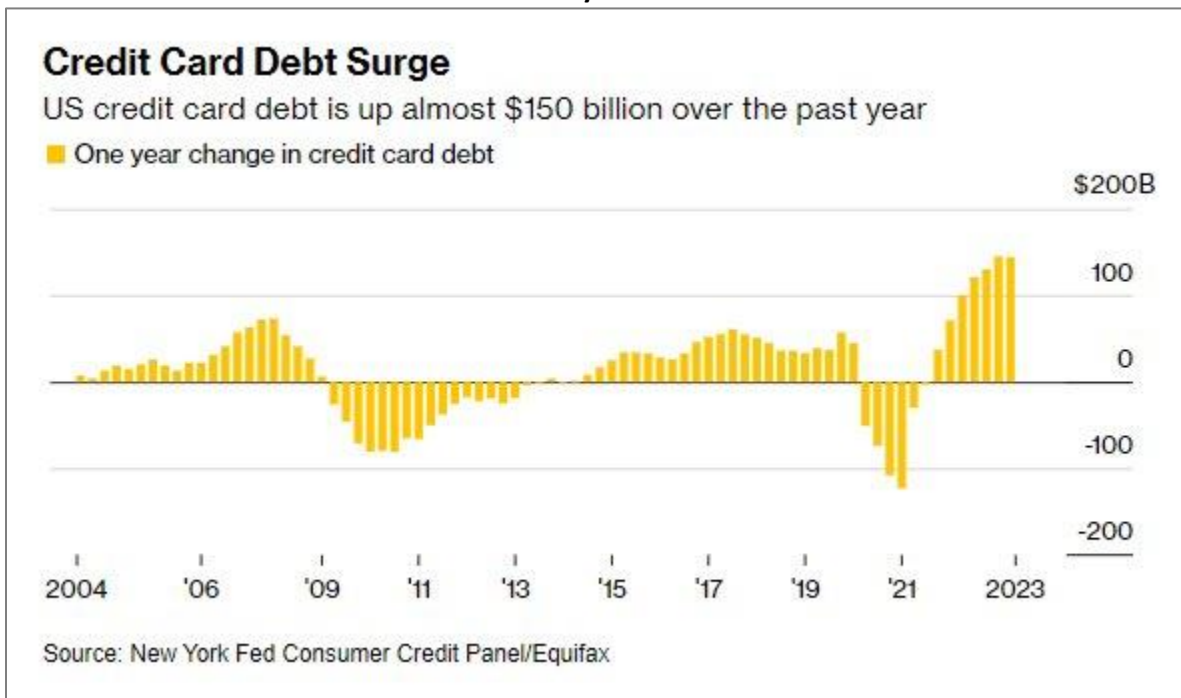
Activity at Amazon Facilities has hit a 7-Year Low.



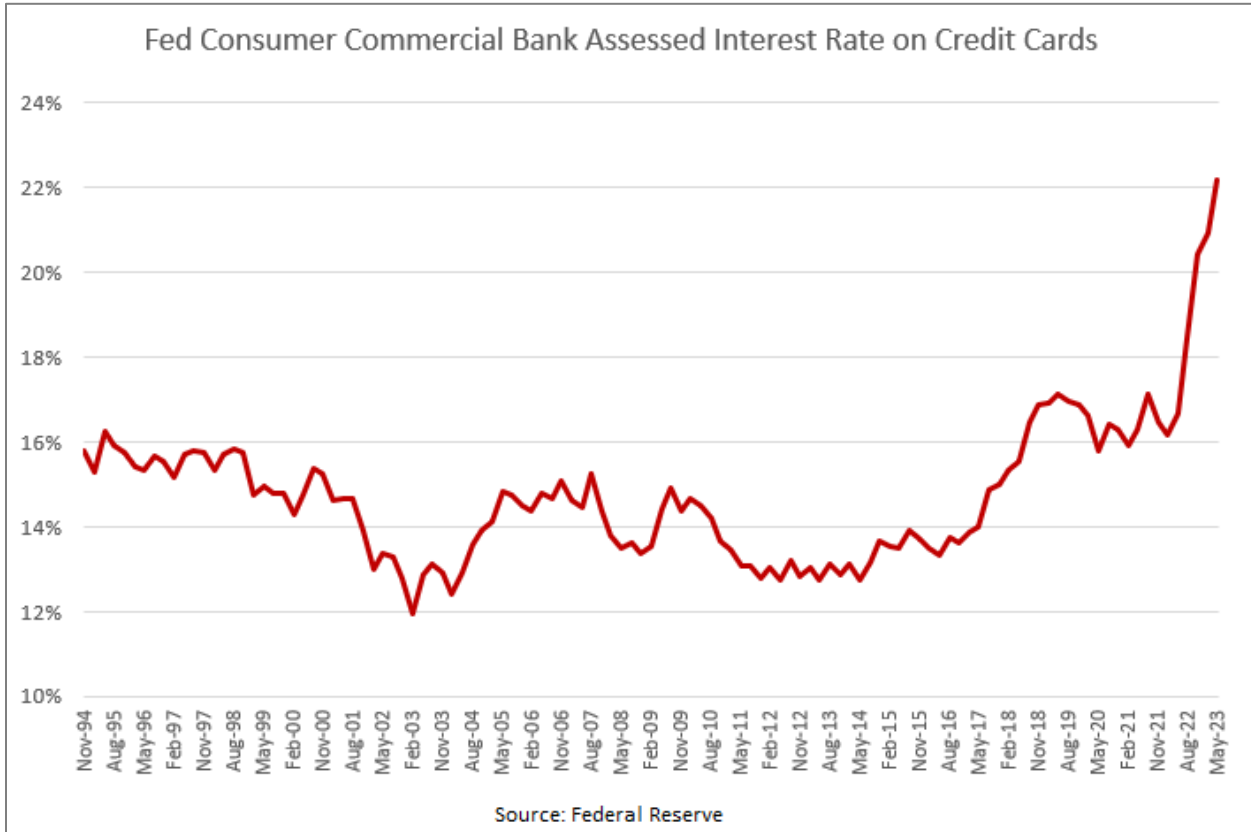
Semiconductor inventories have surged.



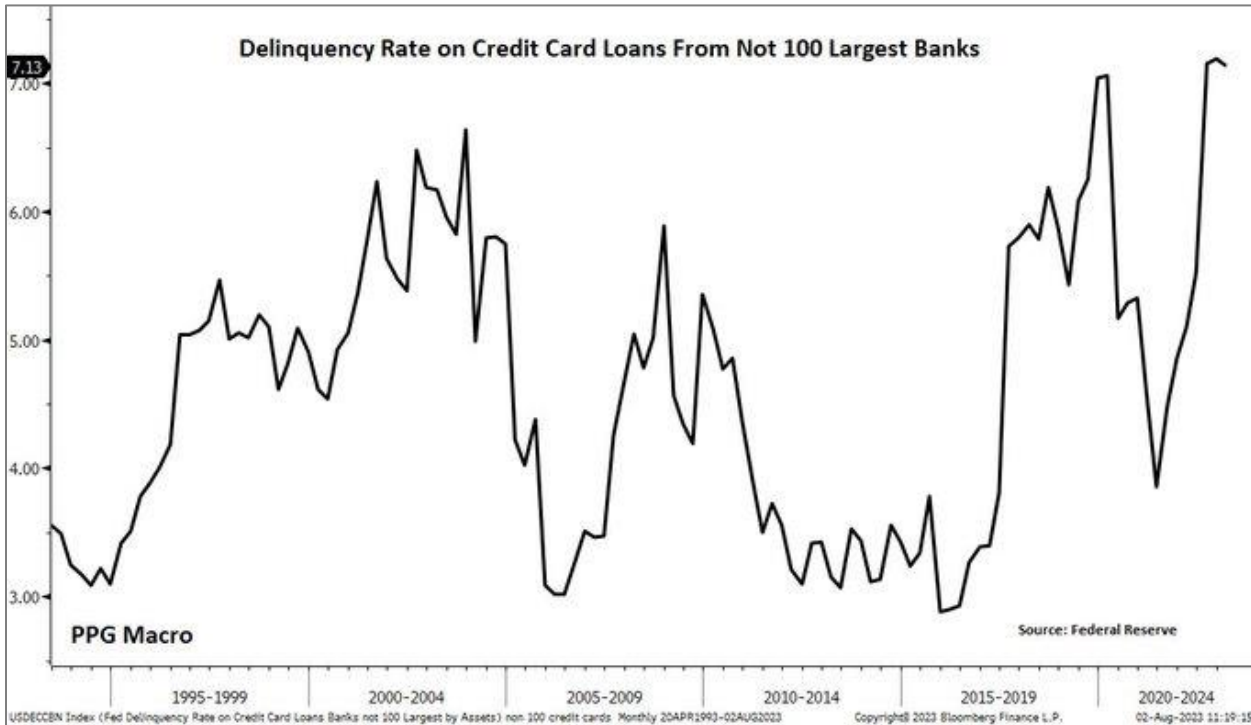
Credit Card balances have ballooned in the last year.



Those credit card balances are paying record interest rates.



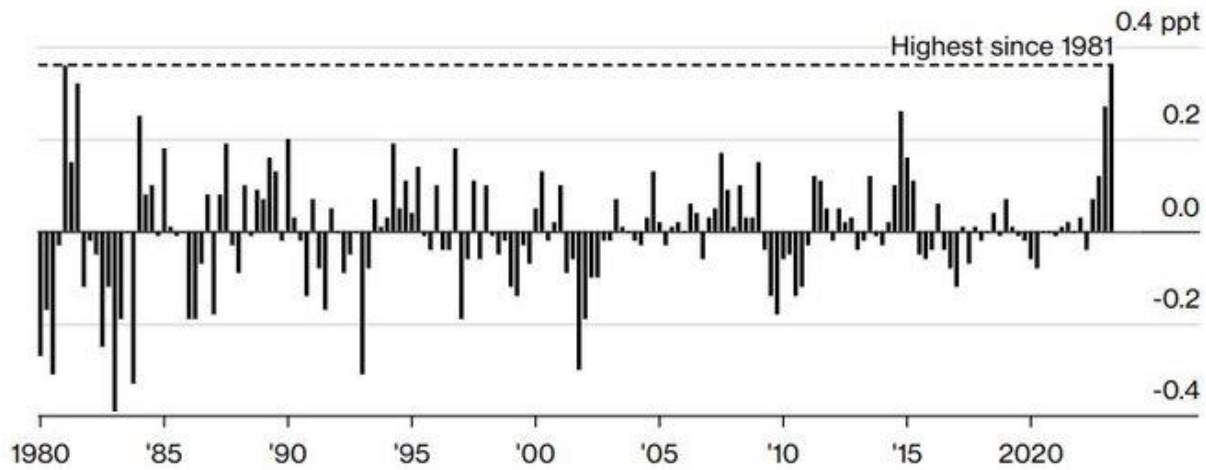
Delinquencies on credit card loans are also climbing.



Manufacturing construction from On-shoring activity has given GDP the highest lift since 1981.

Factory-Building Boom Gives US Economy a Lift

■ Contribution to GDP growth from manufacturing construction

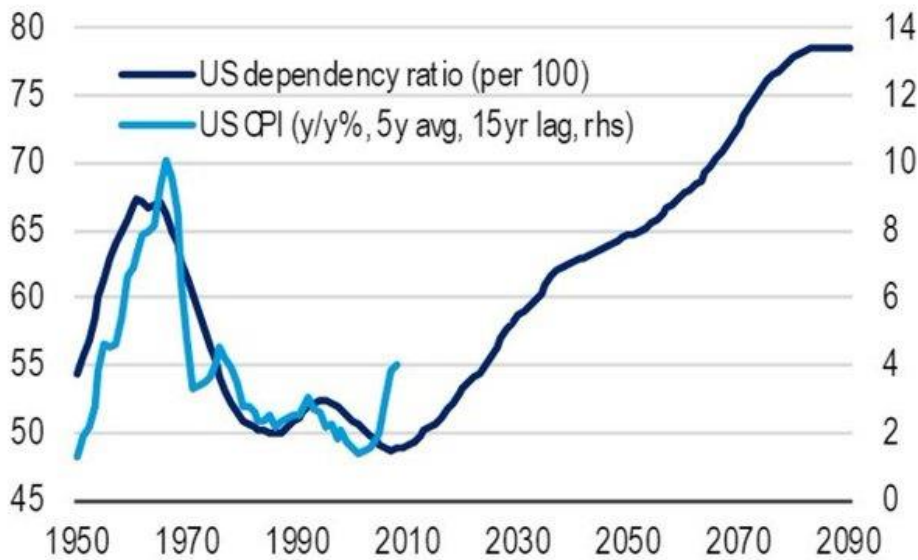


Source: CEA calculations based on Bureau of Economic Analysis data

Do aging demographics drive inflation?

Exhibit 6: Aging demographics = higher inflation

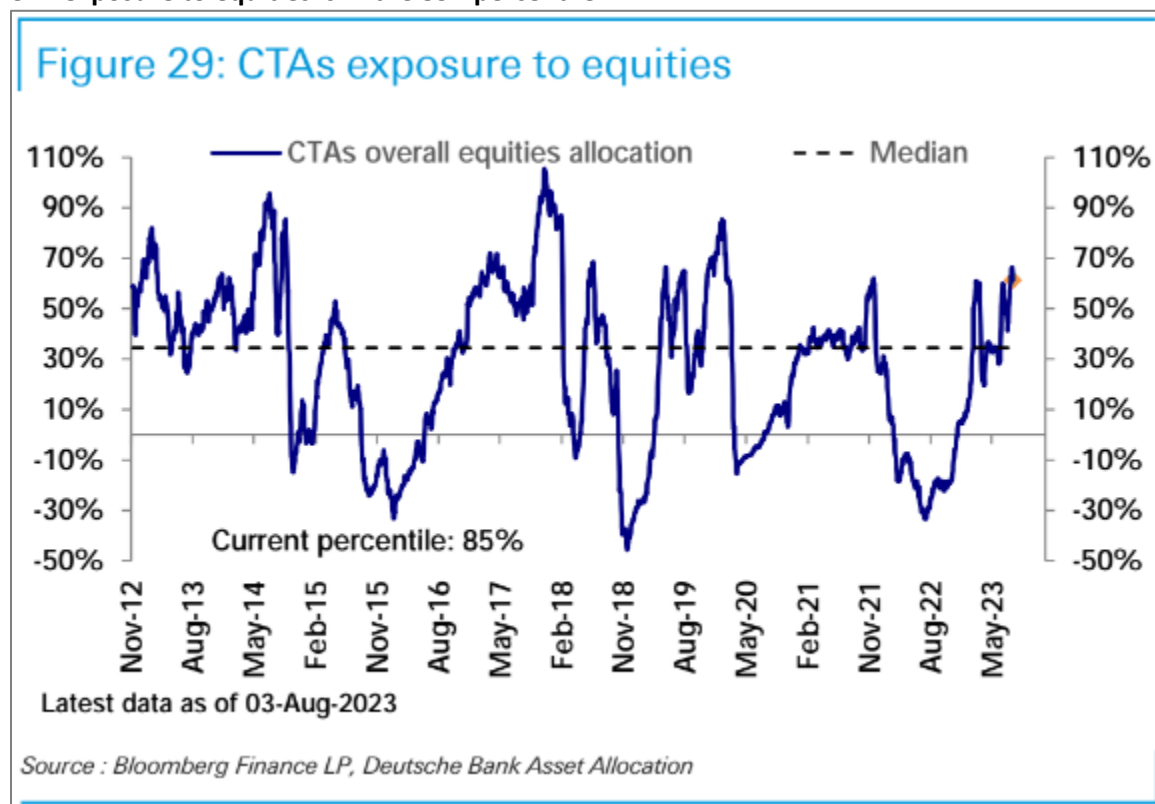
US dependency ratio vs US CPI



Source: BofA Research Investment Committee, Haver, United Nations

BofA GLOBAL RESEARCH

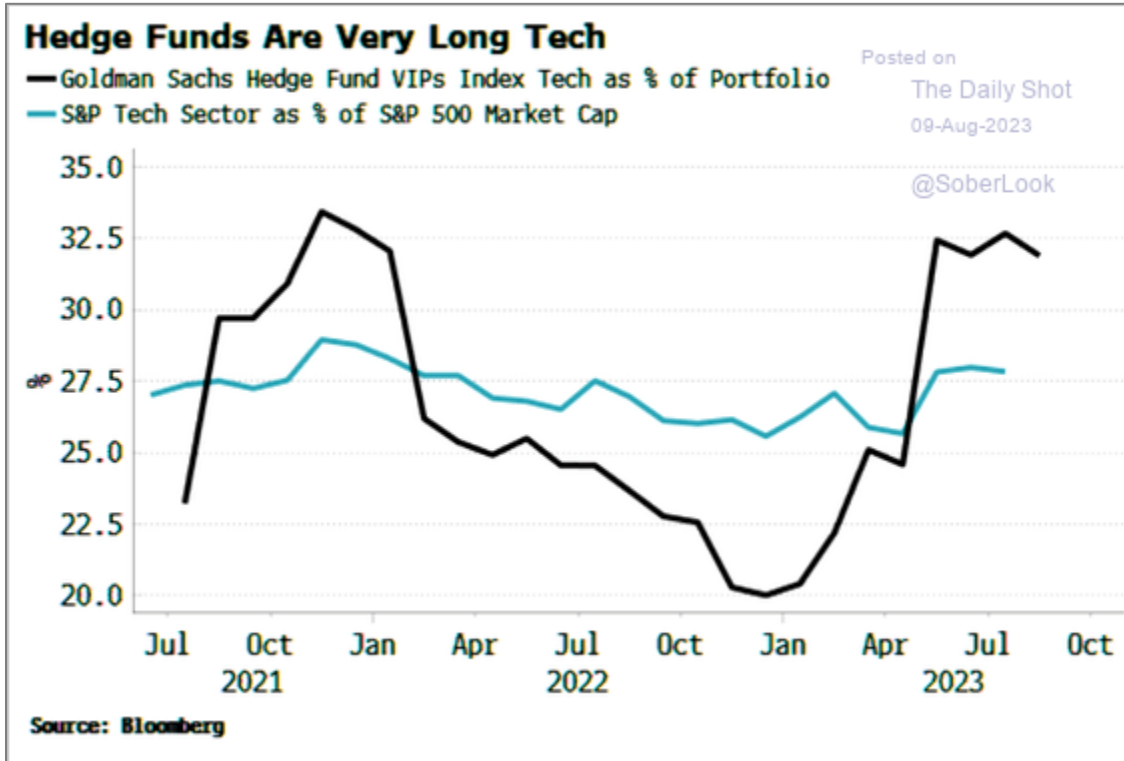
CTA exposure to equities is in the 85th percentile.



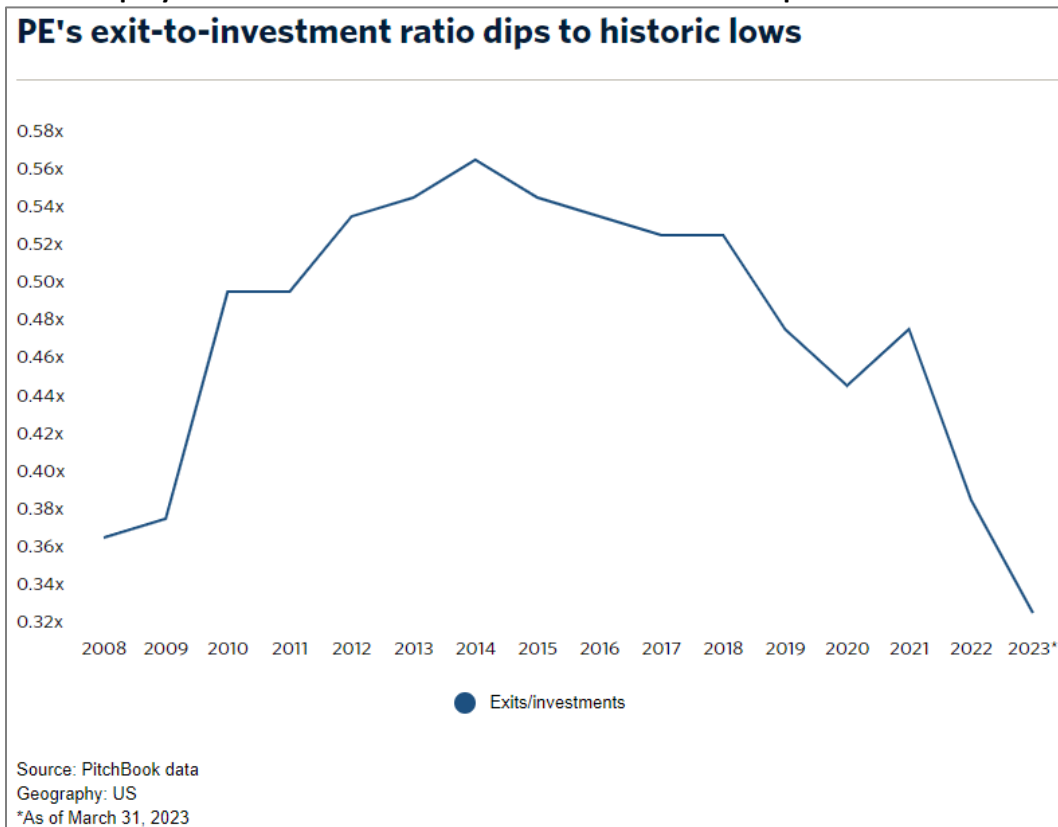
Asset Manager Equity Futures positioning is back to the levels from the bull market peak.



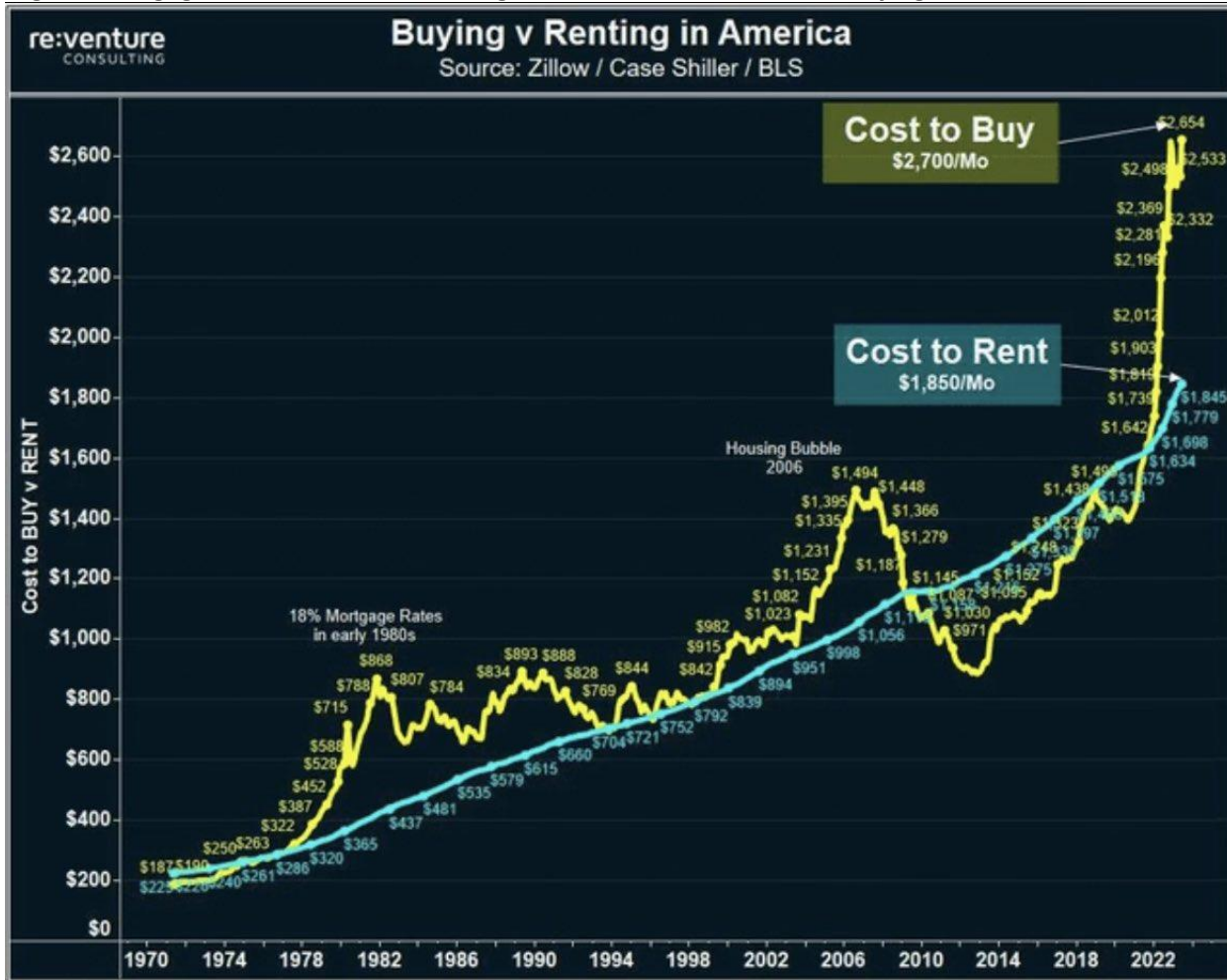
Hedge Fund exposure to Tech is back to the levels when the NASDAQ bull market peaked.



Private Equity firms continue to market down the value of their portfolios.



Higher Mortgage rates have made renting much more attractive than buying a house.



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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