



Market Outlook

By Mark T Dodson, CFA

Welcome back to the Casino.

Market Risk Index fell to 75.3% on more improvement in Monetary Conditions. Psychology moved into the worst one percent of readings since 1970, arguably putting the current stock market environment on a who's who list of the most euphoric markets over the period.

While inflation upticks are becoming a concern for markets expecting Fed rate cuts, inflation is not at a level that has traditionally been a problem for bull markets, so the score is still favorable in the Monetary Composite. Notably, the recent improvements to monetary conditions have been a function of the euphoria that we see in markets, as falling risk aversion bears a striking resemblance to central bank liquidity being injected into an economy.

The Investor Surveys category, now close to its maximum negative score, helped push Psychology into the worst one percent of readings. NAAIM Exposure Index, the Investors Intelligence Survey, and the AAIL survey of individual investors show uniform extremes in bullishness. The NAAIM exposure index set a new bull market high, reaching the highest level since November 2021, the previous bull market peak for the NASDAQ.

Net exposure to markets Leveraged ETFs and funds is within a few percent of the 2021 all-time highs, and net US Equity exposure of Asset Managers is hovering at all-time highs. Options markets are also showing signs of extreme speculation, with the notional volume of securities traded in options markets surpassing the volume of the underlying securities. That hasn't happened since the frothiest period of 2021. When the volume in the derivatives underlying financial assets sees more trading than the financial assets themselves, that's bucket shop behavior – a market that has become a casino.

Market Risk Index

Rec Allocation 25% Underweight

75.3%

Category Percentiles

Psychology - P6



Monetary - M3



Valuation - Extremely Overvalued



Trend



Largest Psychology Influences

Leveraged Investments	Negative
Surveys	Negative
Consumer Confidence	Negative
Fund Flows	Negative

Largest Monetary Influences

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

Valuation

7-10 Year Equity Return Forecast	0.9%
10Yr US Treasury Yield	4.3%

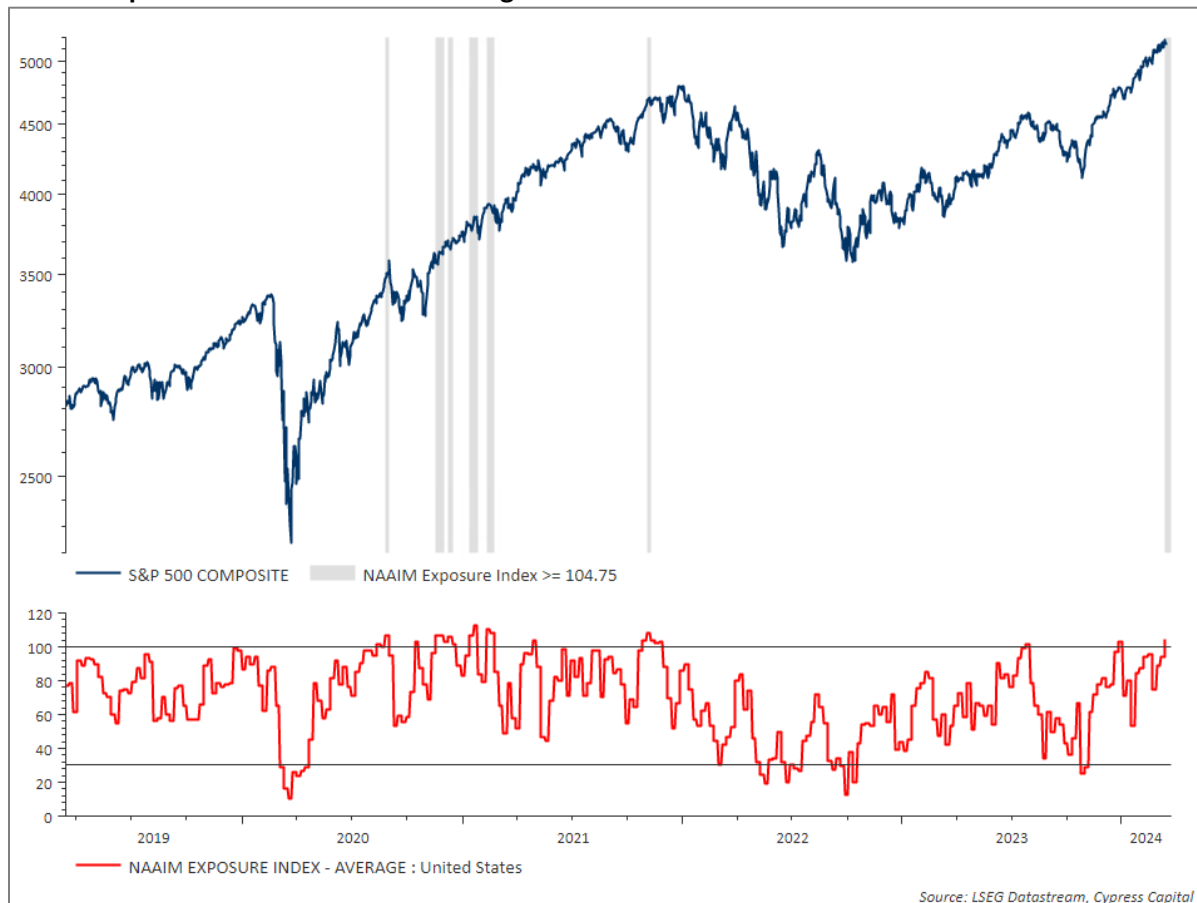
Market Trends

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

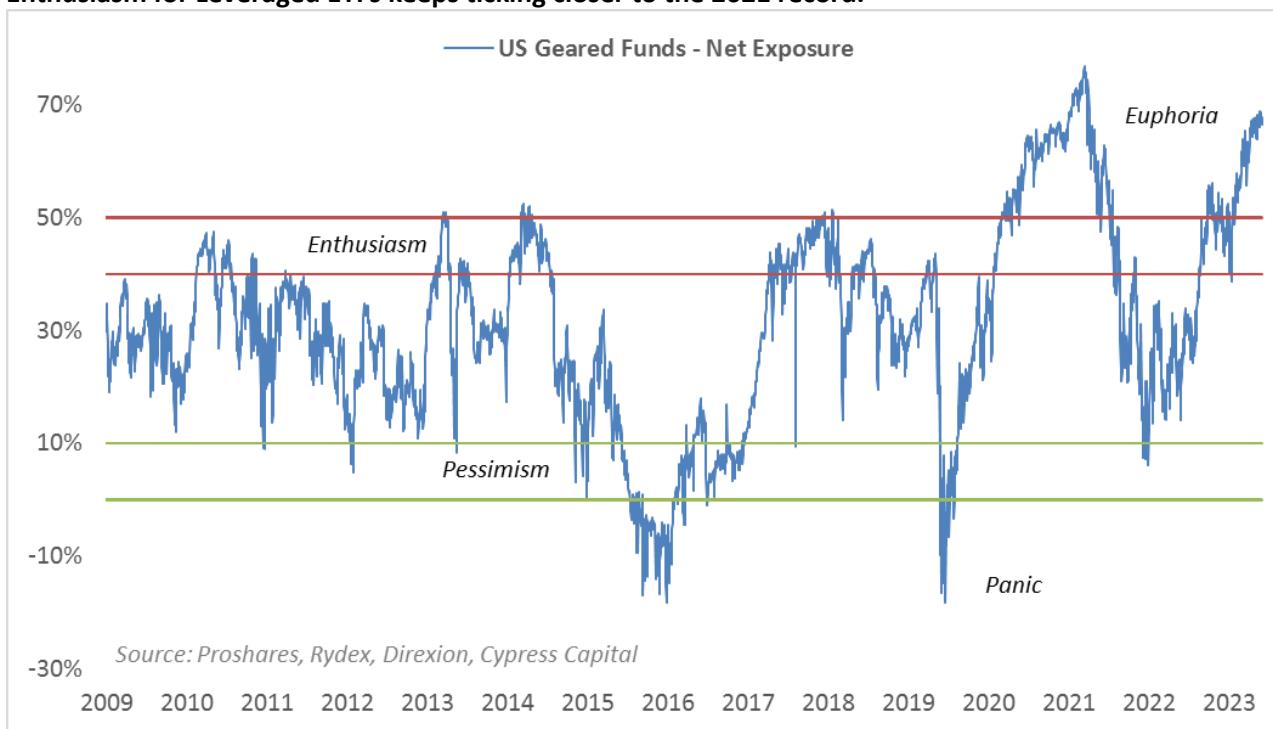
Market Risk Index scales from 0 to 100%. Higher readings correspond with higher risk markets based on our model & opinion. Scores below 25% are bullish. Scores between 25-75% are neutral, and scores above 75% are markets vulnerable to major drawdowns.

Charts of the Week

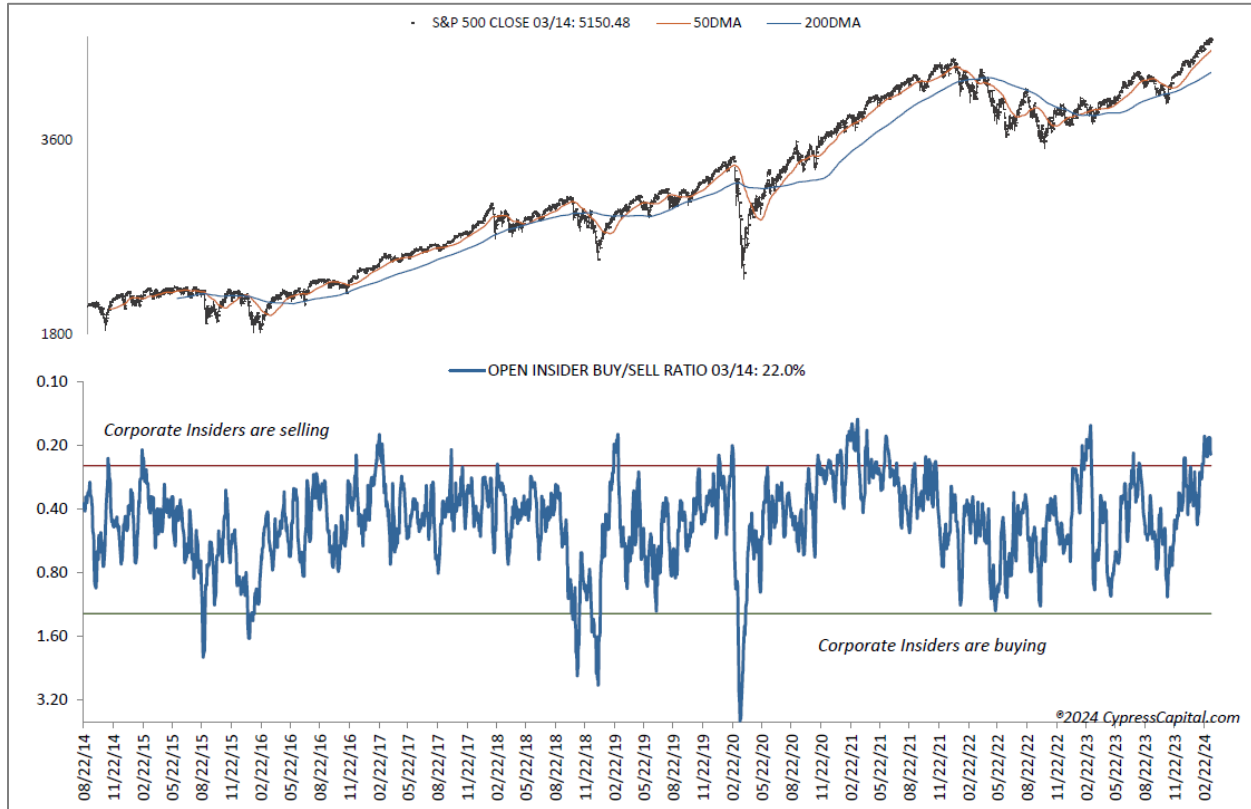
NAAIM Exposure Index climbed to the highest level since November 2021.



Enthusiasm for Leveraged ETFs keeps ticking closer to the 2021 record.



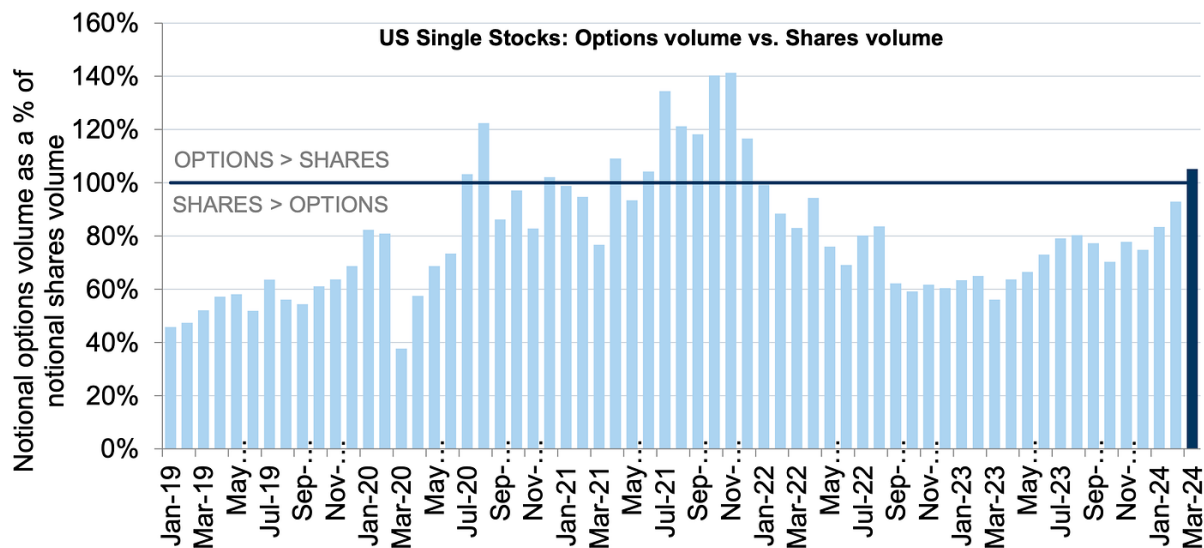
Corporate Insiders have been persistent sellers for three weeks in a row.



Options volume has surpassed underlying stock volume for the first time since the Covid-bubble.

Exhibit 1: Options volume surpassed that of shares during this month after a period of 2 years, largely driven by semiconductor related volumes

Notional options volume vs. notional shares volume for US single stocks since 2019



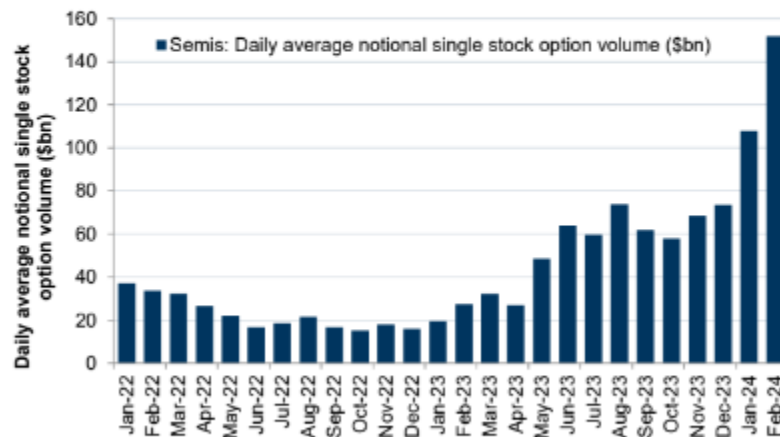
Source: Goldman Sachs Global Investment Research, OptionMetrics

Options volumes on Semiconductor stocks are up more than 450%.

It made up over 40% of single-stock options traded on S&P 500 stocks in February.

Exhibit 2: Options volumes on Semiconductor stocks YTD are 455% above this time last year...

Daily average notional single stock option volumes for SMH ETF constituents since Jan 2022 (\$bn)



Source: Goldman Sachs Global Investment Research, Factset

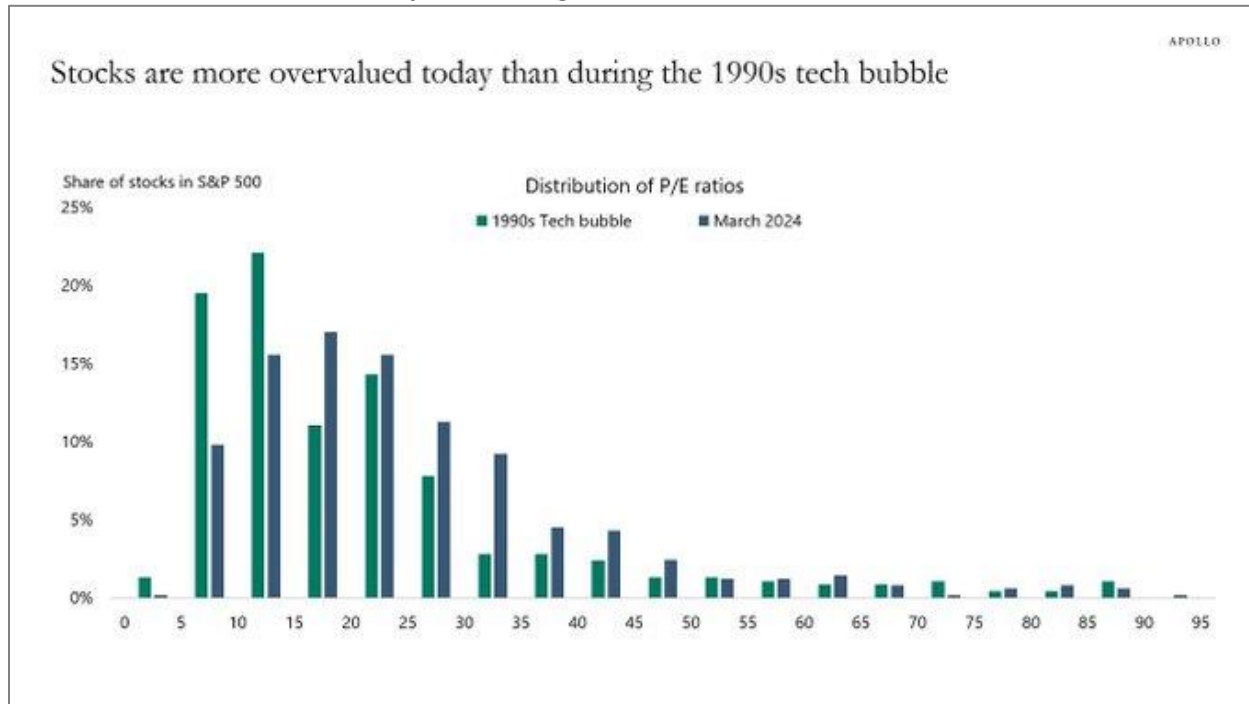
Source: @GunjanJS

We've only seen this much call buying at such a premiums a handful of times – in 2000 and 2020-21.



Source: SentimenTrader.com

Stocks are more overvalued today than during the tech bubble.



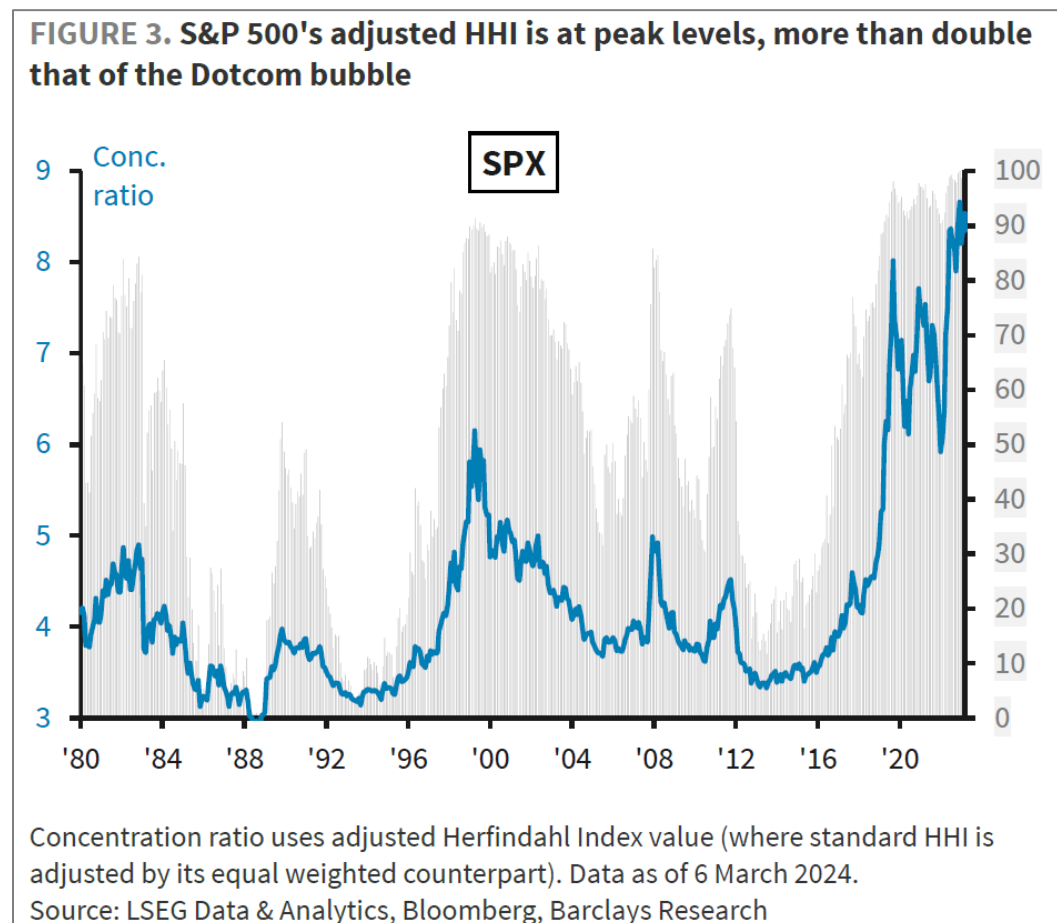
Median PE of the largest 10 stocks took out the 2000 highs, but so did the smallest 490.



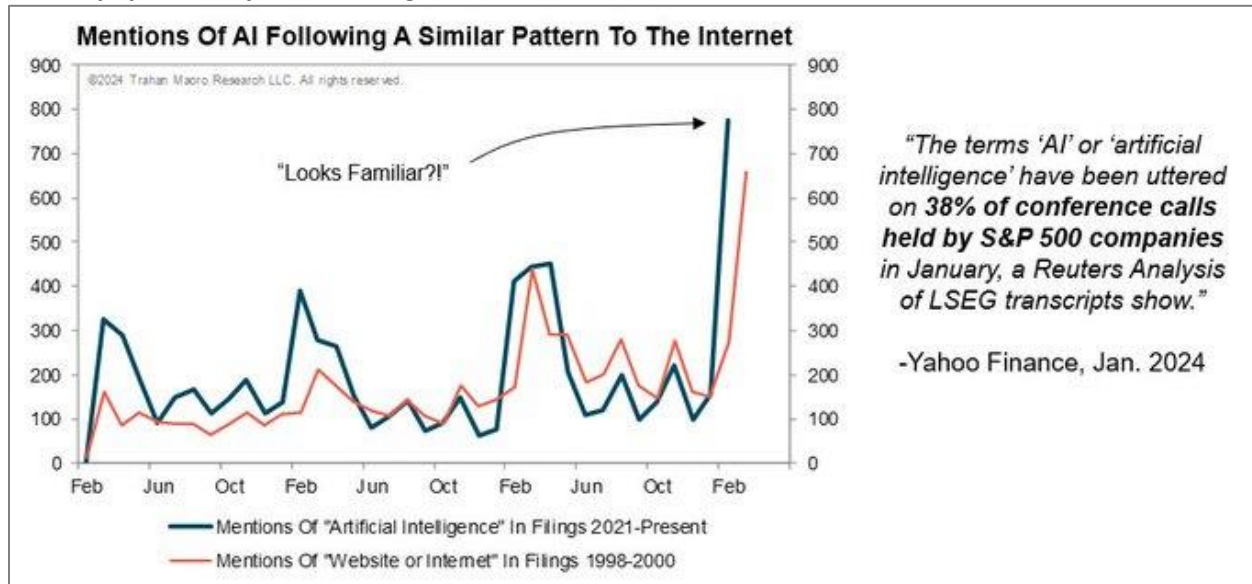
Tech is as popular as it was in 2000.



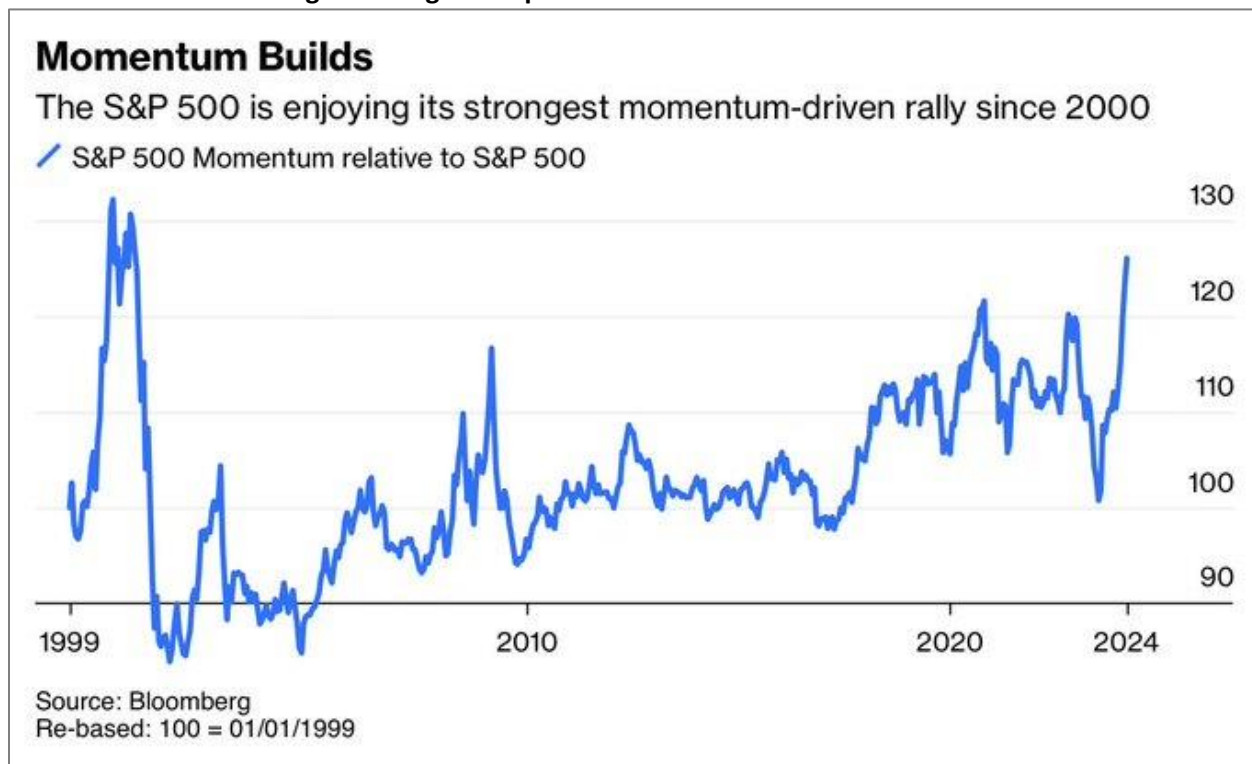
Stock market concentration is more than double the Dotcom bubble.



AI is as popular a topic on earnings calls as the Internet was in 2000.



Momentum Factor seeing its strongest outperformance since 2000.



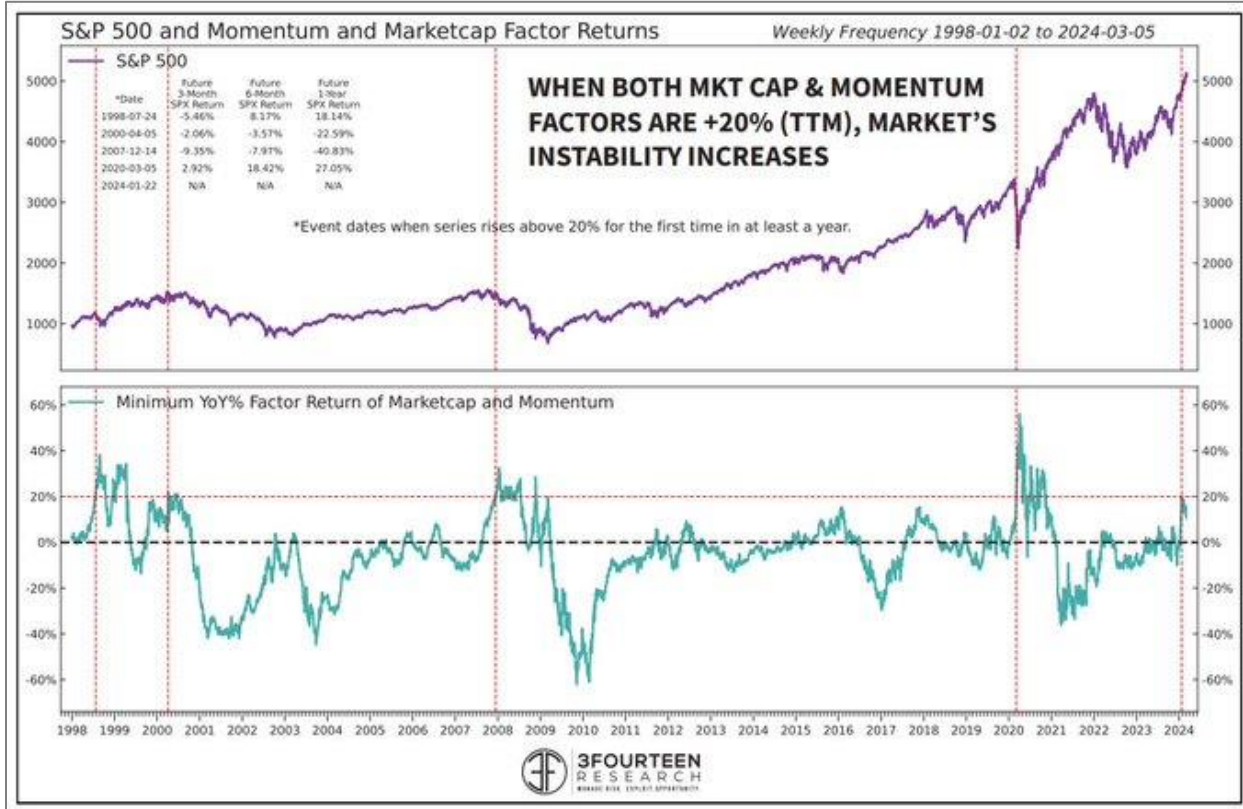
The weight of Momentum Stocks is at all-time highs, surpassing 1929 and the Nifty 50 eras.



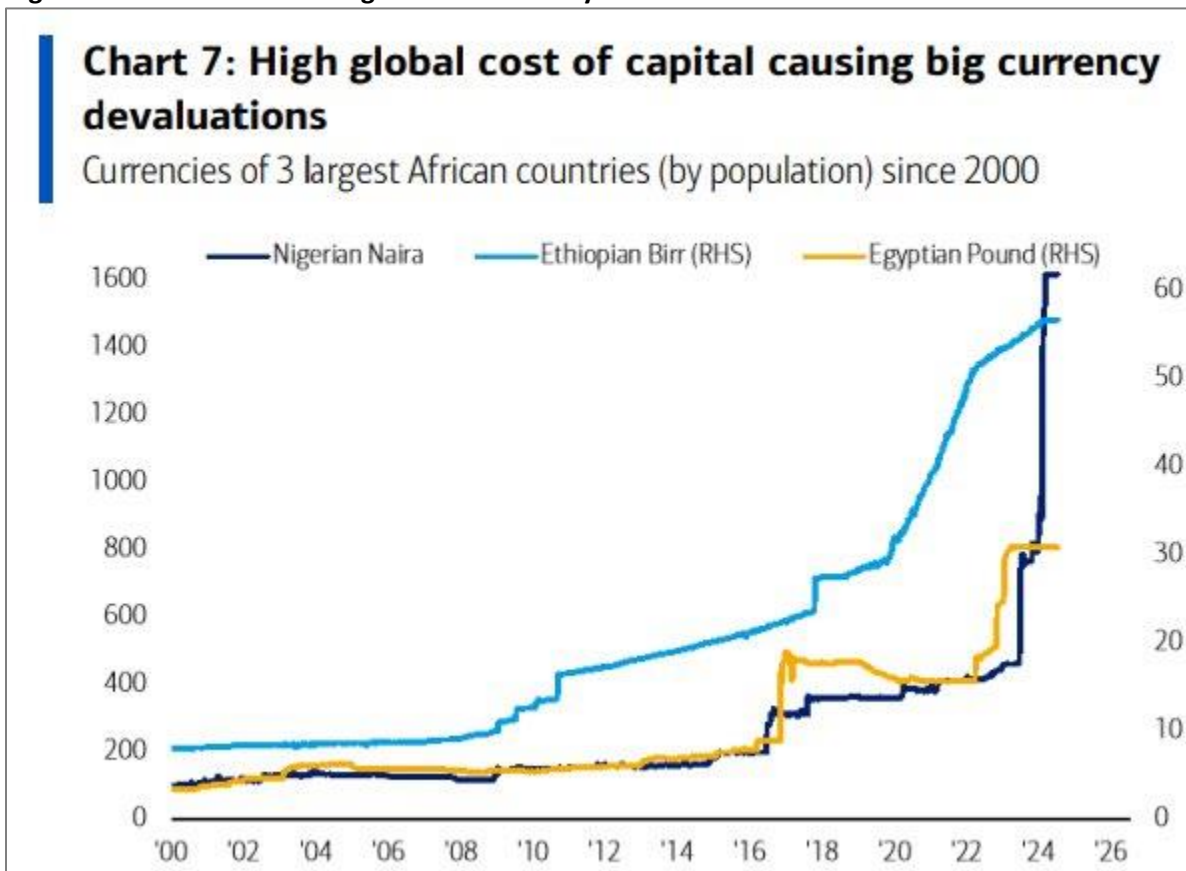
Positioning in Mega-cap Growth and Tech is in the 96th percentile.



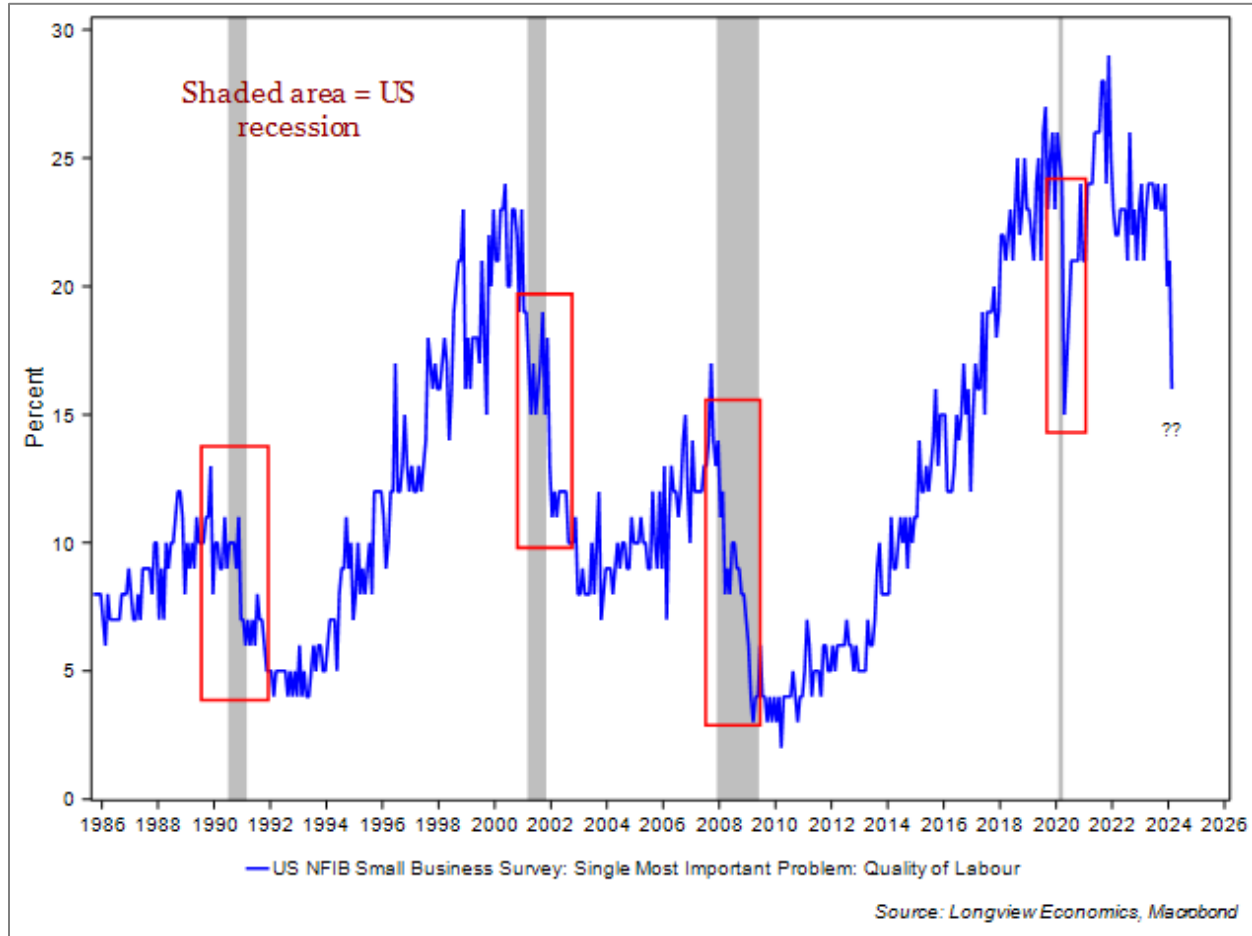
Historically, when Market Cap and Momentum are this popular, market instability increases.



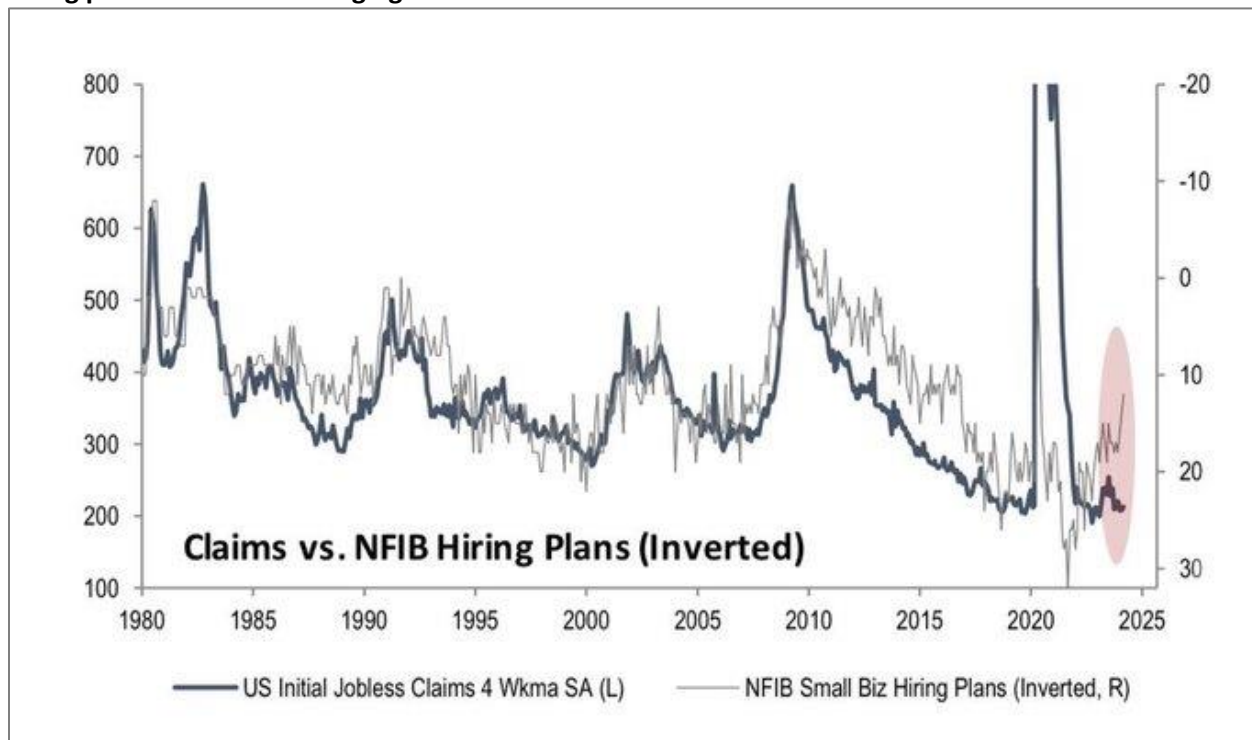
High interest rates are starting to cause currency devaluations.



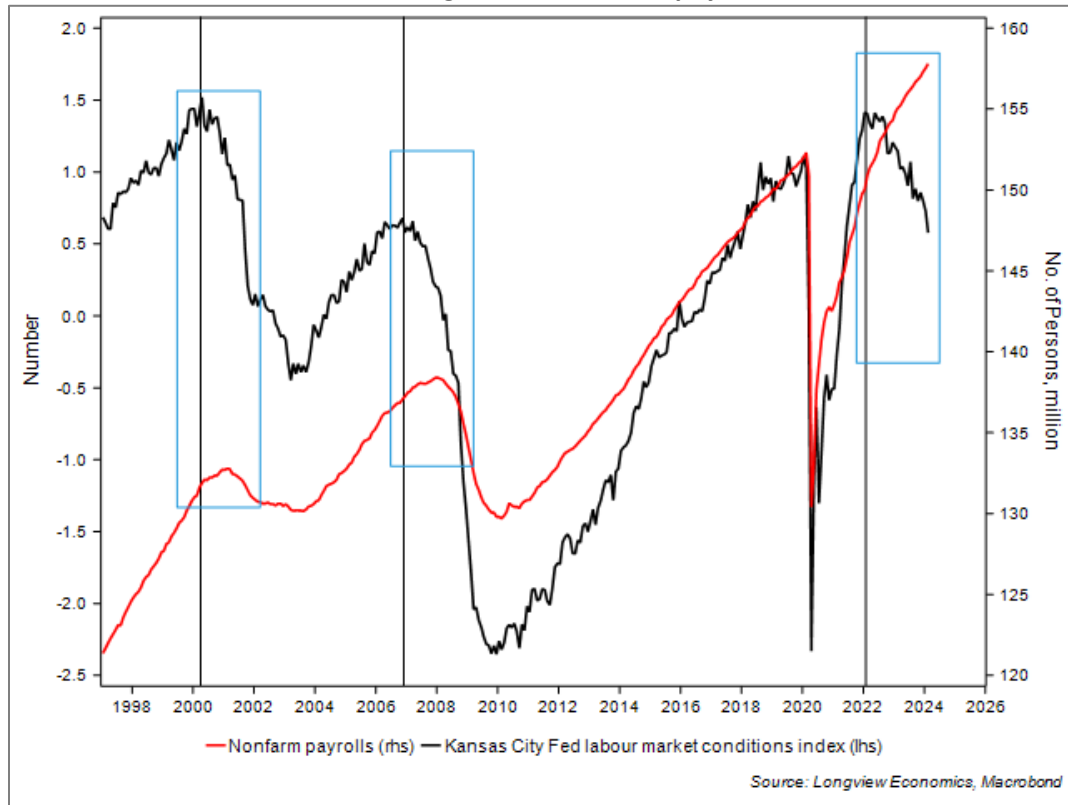
Quality of Labor as a Concern of Small Businesses tends to drop sharply in recessions.



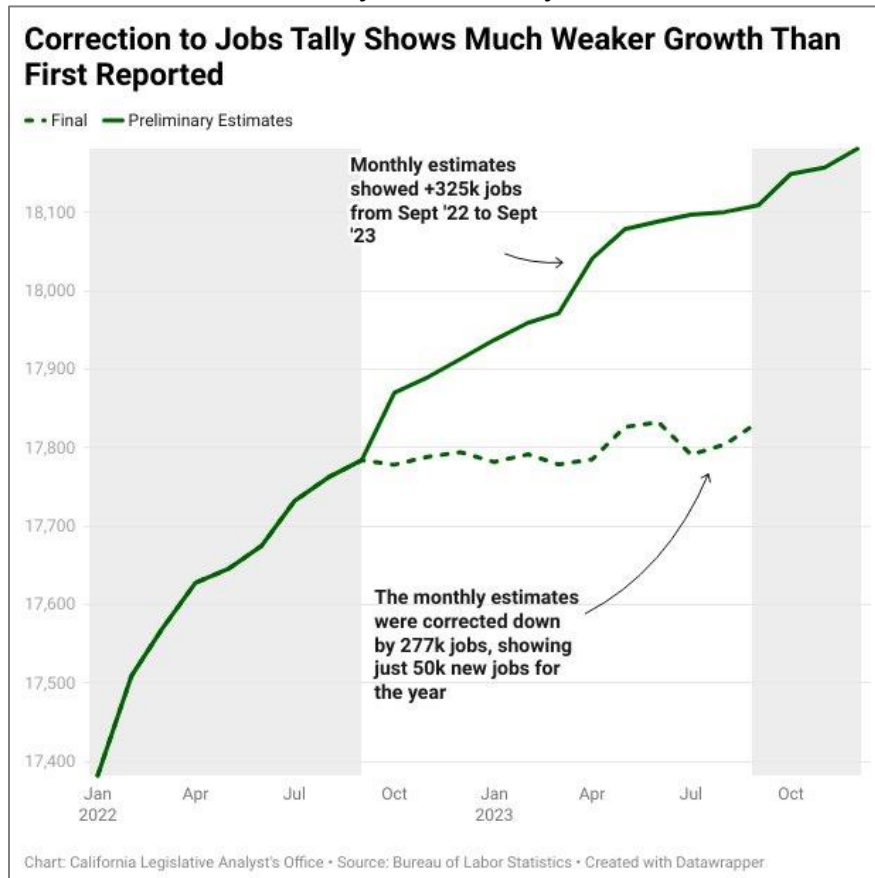
Hiring plans have been diverging from Jobless Claims.



Labor Market Conditions have diverged from Nonfarm payrolls.



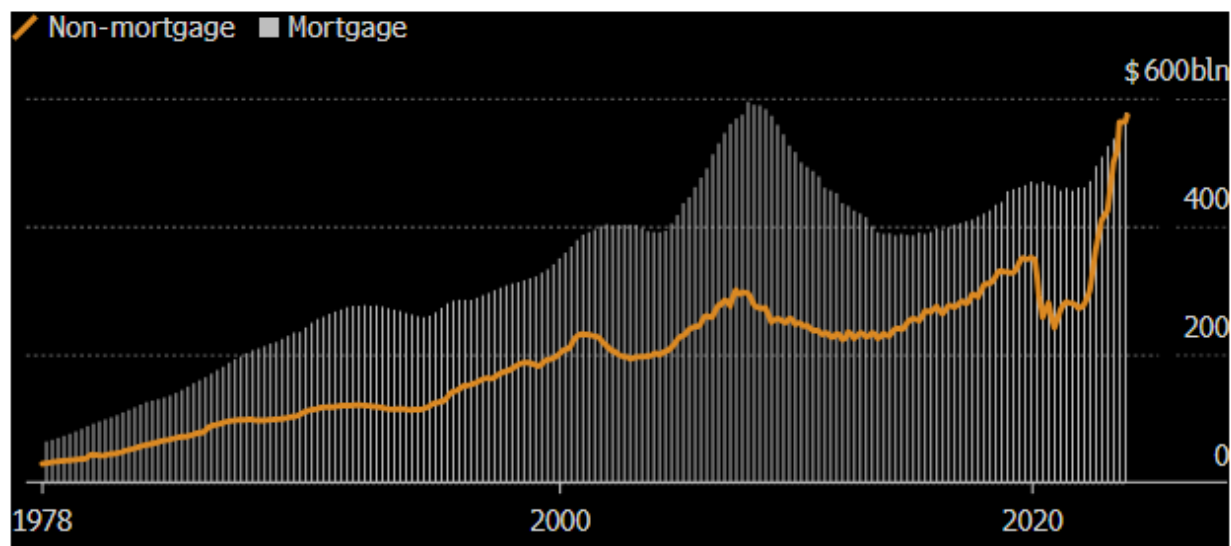
California made a massive adjustment to its job numbers from 2023.



Non-Mortgage interest payments have surpassed mortgage interest payments for the first time.

Interest Payments by US Households

Seasonally adjusted annual rate



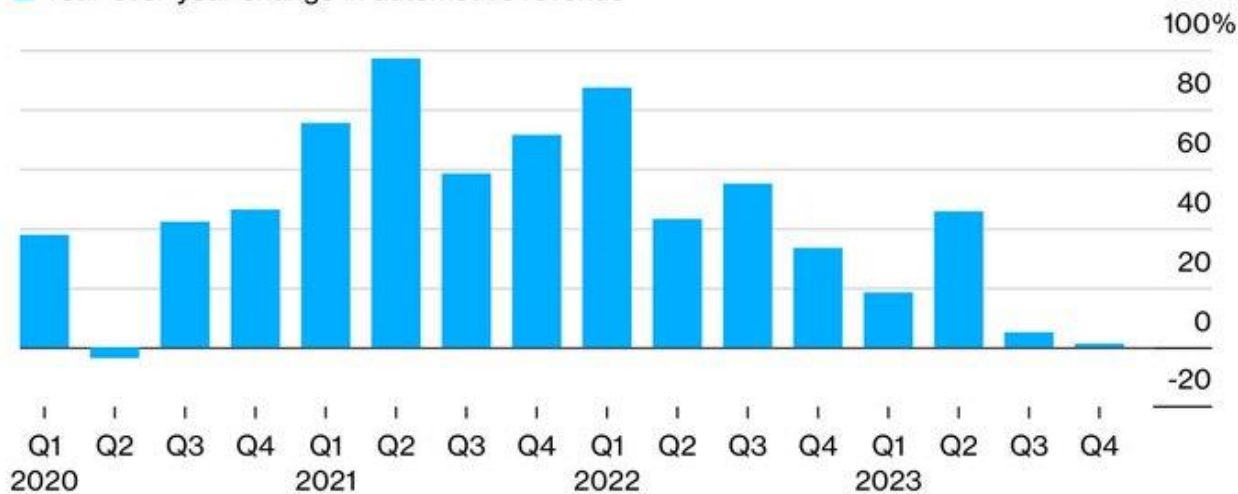
Source: Bureau of Economic Analysis

Tesla's Revenue Growth has slowed dramatically.

Tesla's Sales Slowdown

Automotive revenue increased just over 1% last quarter

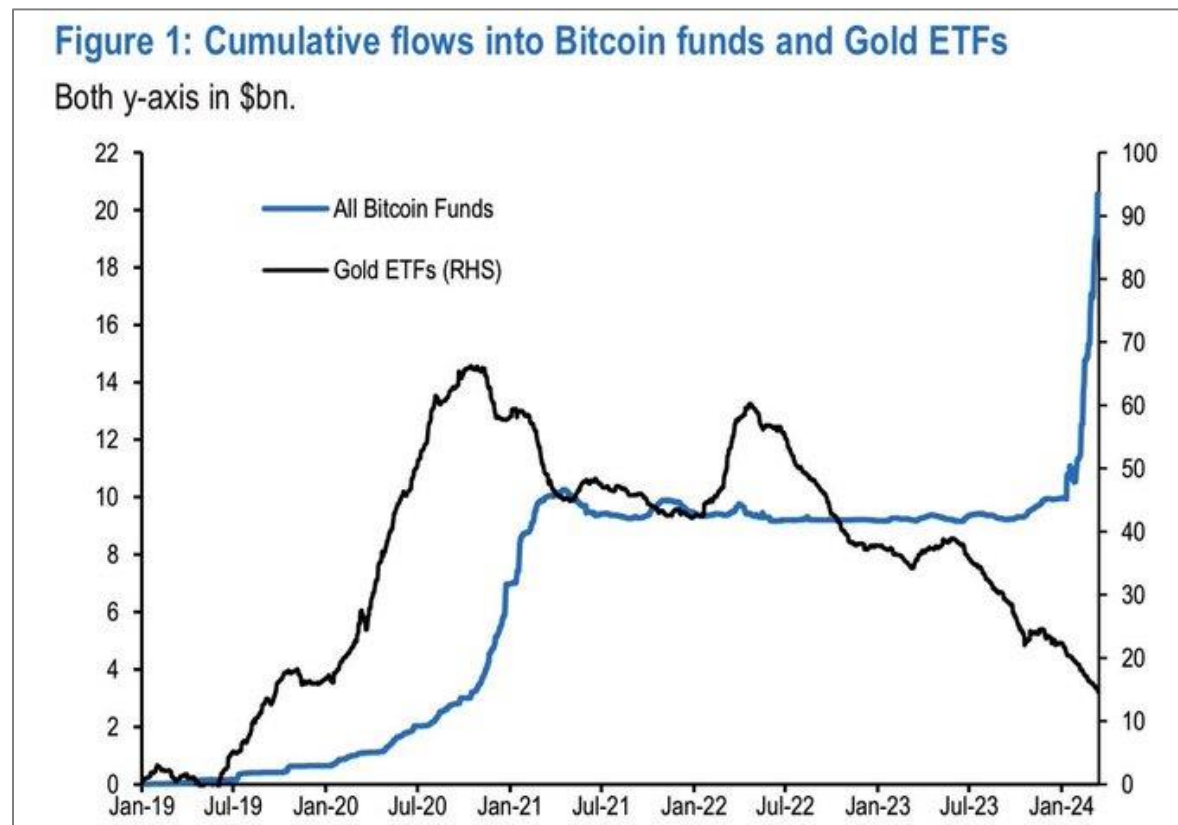
Year-over-year change in automotive revenue



Retail isn't buying gold, but global central bankers are.



Gold funds are out – Bitcoin funds are in.



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.