



Market Outlook

By Mark T Dodson, CFA

Bullishness among newsletter writers is pervasive

Market Risk Index edged up to 74.2%. Valuations and Monetary Conditions worsened but were partially offset by a slight improvement to the Psychology Composite.

Psychology improved marginally, but the Investor's Intelligence survey worsened. Bullishness among professional investors climbed to the highest level since the days leading up to the Volmageddon market drawdown in 2018. Stocks have fallen by 0.3% on average over the next 12 months when bullishness has become this pervasive among professional newsletter writers.

Table: Stock Market Returns when Advisors Are Bullish
Investors Intelligence Bears/Bulls (3wma) below 25%

	1M	3M	6M	1Y
Average	0.4	0.3	1.1	-0.3
Median	0.4	0.7	0.8	-2.9
Max Gain	7.3	11.3	21.2	30.0
Max Loss	-7.3	-8.2	-12.4	-22.2
Win Rate	54%	56%	54%	38%
Buy & Hold Return	0.7	2.0	4.1	8.3
Buy & Hold Win Rate	61%	65%	69%	74%

S&P 500 price returns since 1965

Monetary Conditions are likely at their best readings for this bull market, as getting uber-bullish readings from Monetary conditions would require the yield curve to normalize. However, normalizing the yield curve almost certainly implies that the Velocity and Aggregates categories will worsen, both of which are recessionary events.

The Valuation Composite moved into the worst one percent of readings, and our bottom-up return forecast for stocks over the next 7-10 years fell to 0.06%, the lowest level since August 2021, right at the height of the COVID-stimulus bubble.

While we did not change our equity allocations this week, we did increase the duration of our position in TIPS across our Global Allocation portfolios. Last fall, we initiated a position that lengthened our duration in Treasury Inflation-Protected Securities when real

Market Risk Index

Rec Allocation 25% Underweight

74.2%

Category Percentiles

Psychology - P6



Monetary - M3



Valuation - Extremely Overvalued



Trend



Largest Psychology Influences

Leveraged Investments	Negative
Surveys	Negative
Consumer Confidence	Negative
Option Activity	Negative

Largest Monetary Influences

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

Valuation

7-10 Year Equity Return Forecast	0.1%
10Yr US Treasury Yield	4.4%

Market Trends

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

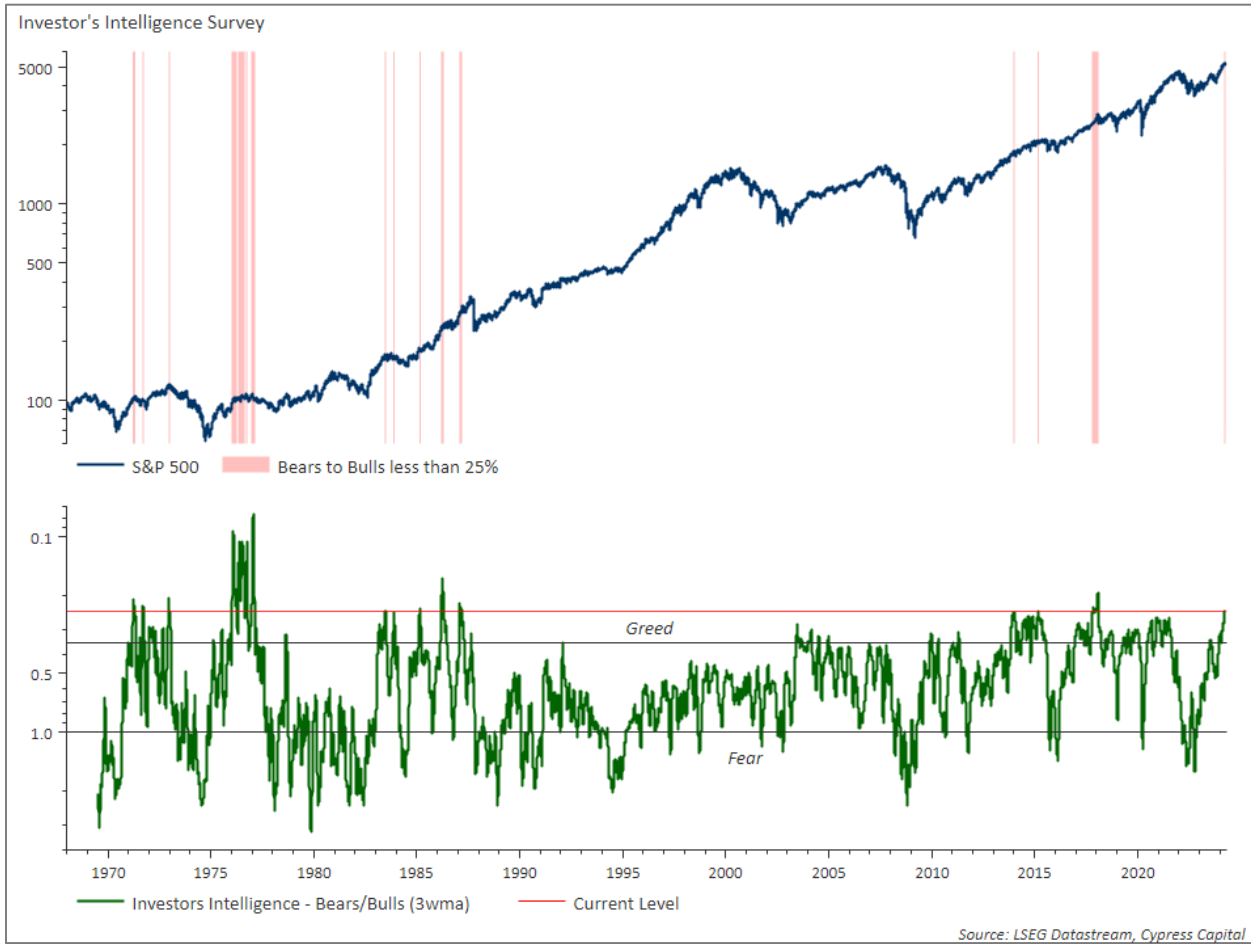
Market Risk Index scales from 0 to 100%. Higher readings correspond with higher risk markets based on our model & opinion. Scores below 25% are bullish. Scores between 25-75% are neutral, and scores above 75% are markets vulnerable to major drawdowns.

yields had grown to the highest level in 20 years. The timing of that purchase (within days of the bottom of the bond market selloff) was impeccable, and extremely lucky.

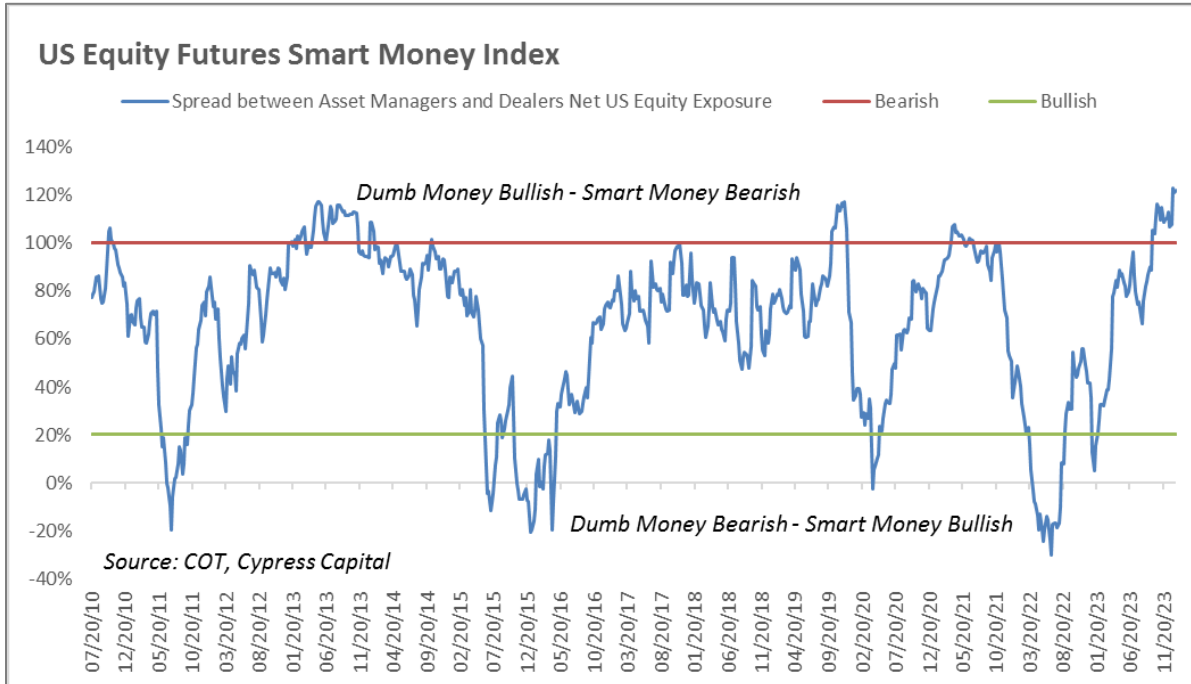
This additional increase in the position has a different motive and is in part driven by the condition of our Monetary Composite. The breakeven inflation rate on TIPS is still well below the prevailing inflation rate, as the bond market has persistently over-estimated a return to pre-Covid inflation levels. Yet, inflation appears to have stopped declining ten months ago. We believe that TIPS are the most compelling offer in fixed income today and a hedge against a Fed that may be too dovish in the face of persistent inflation.

Charts of the Week

Investor's Intelligence Ratio of Bears to Bulls hits the lowest since early 2018.

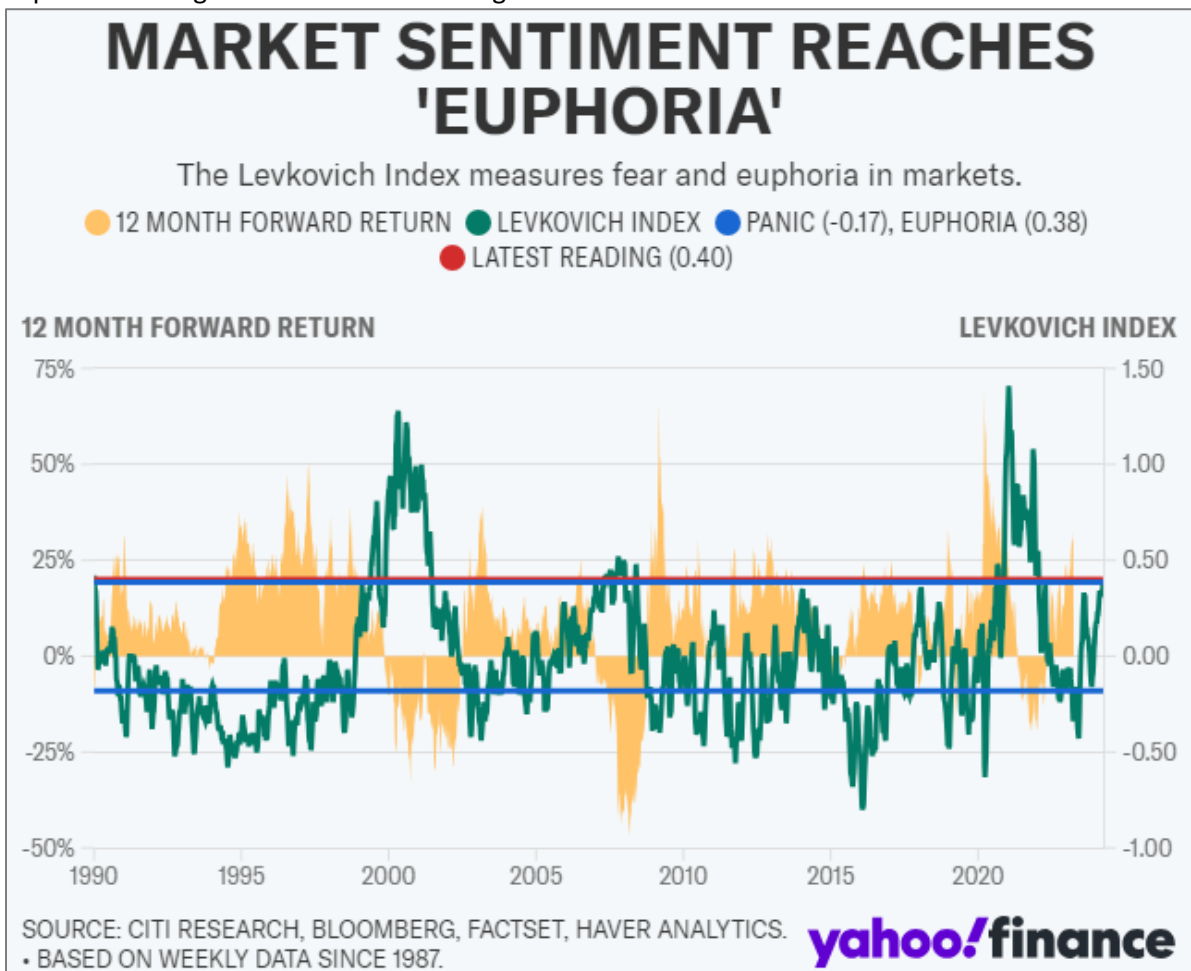


The divergence between Smart and Dumb Money Confidence in stocks stayed close to record levels.



Levkovich Index of investor sentiment hits Euphoria for the first time since 2021.

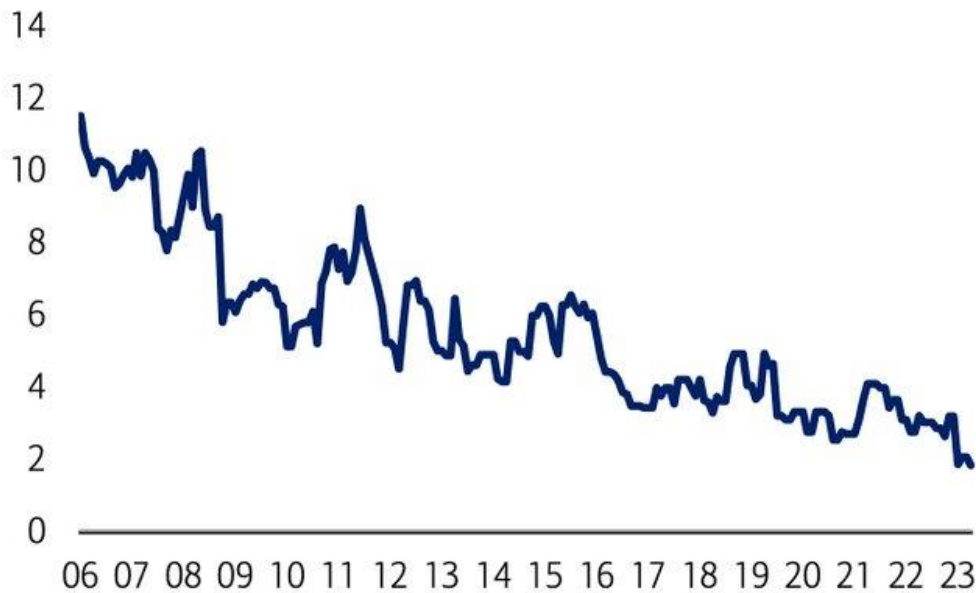
Euphoria readings are associated with negative 12 month forward returns.



Wall Street Strategists' recommended cash allocation falls to a record low.

Exhibit 4: Cash allocations dropped m/m to a survey history low

Average recommended allocation to cash by Wall Street strategists (2006-3/2024)



Source: BofA US Equity & Quant Strategy

BofA GLOBAL RESEARCH

Record Crowding in High Momentum Stocks.

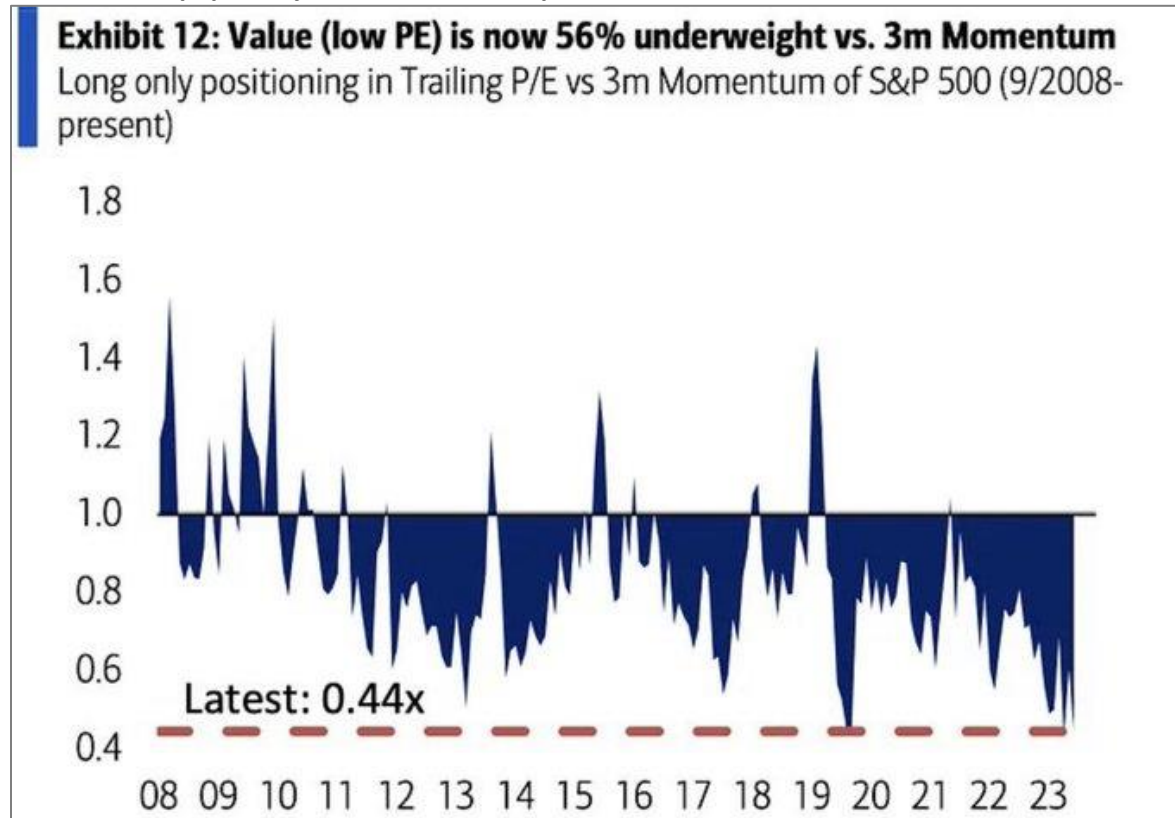
Figure 8: Record High Momentum Crowding (99.8%ile)

Crowding in Stocks with Strongest Price Momentum, Right Tail

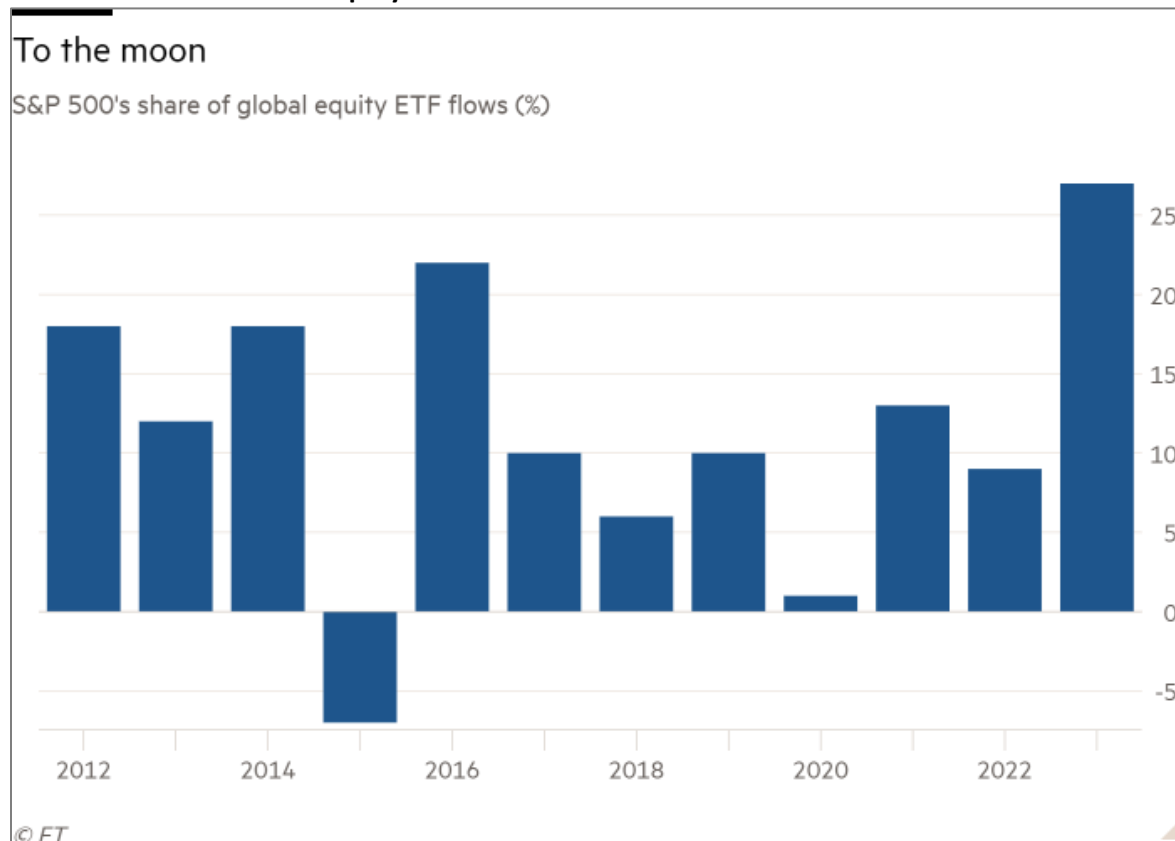


Source: J.P. Morgan Equity Macro Research

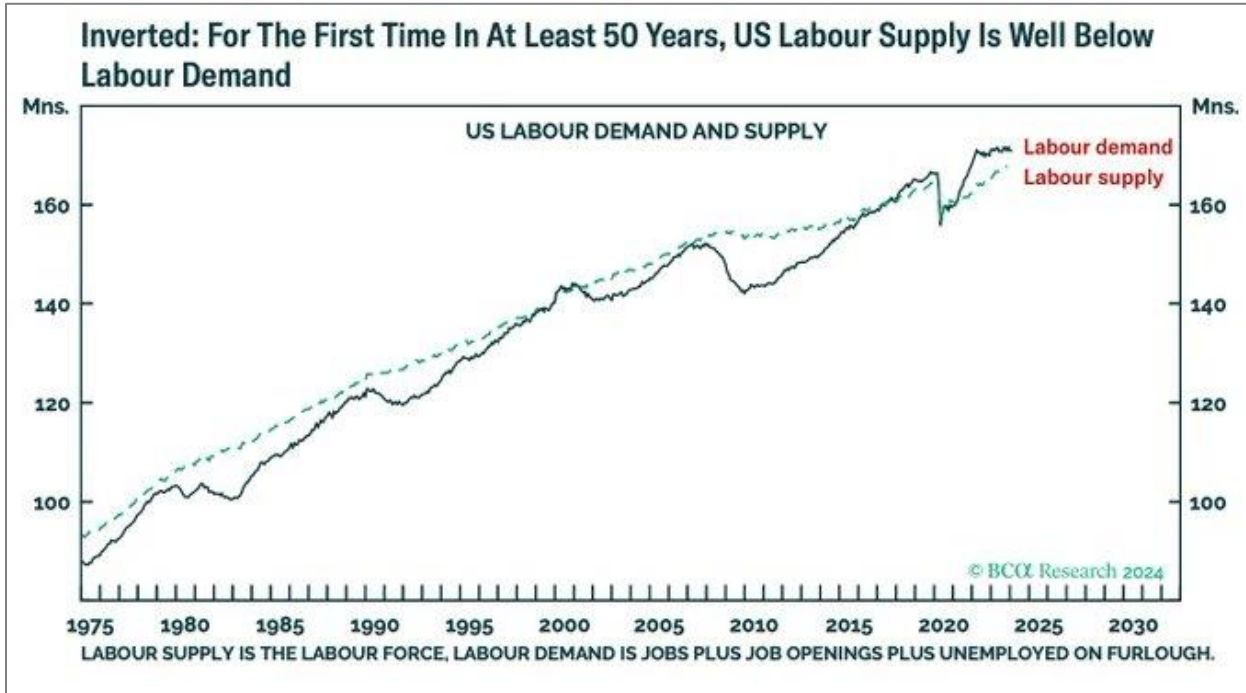
Momentum's popularity has come at the expense of value stocks.



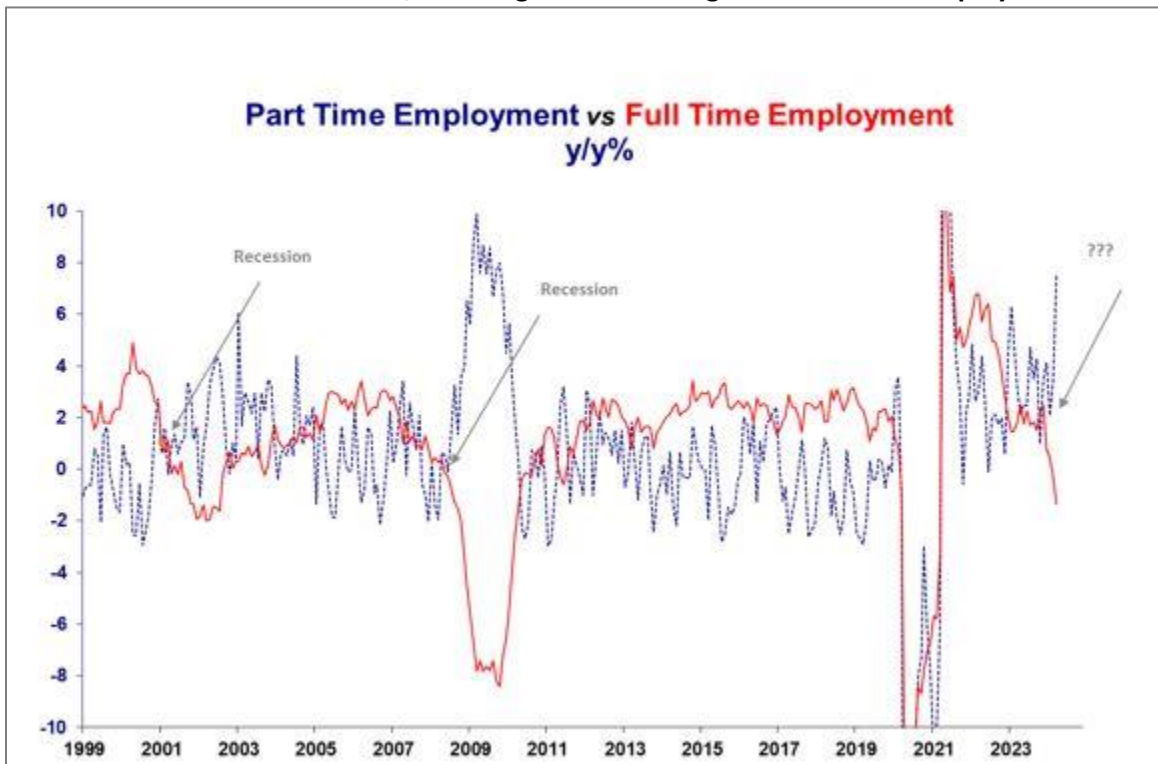
S&P 500's share of Global Equity ETF flows sets a new record.



Can inflationary pressures subside when Labor Demand is still outpacing Labor Supply?

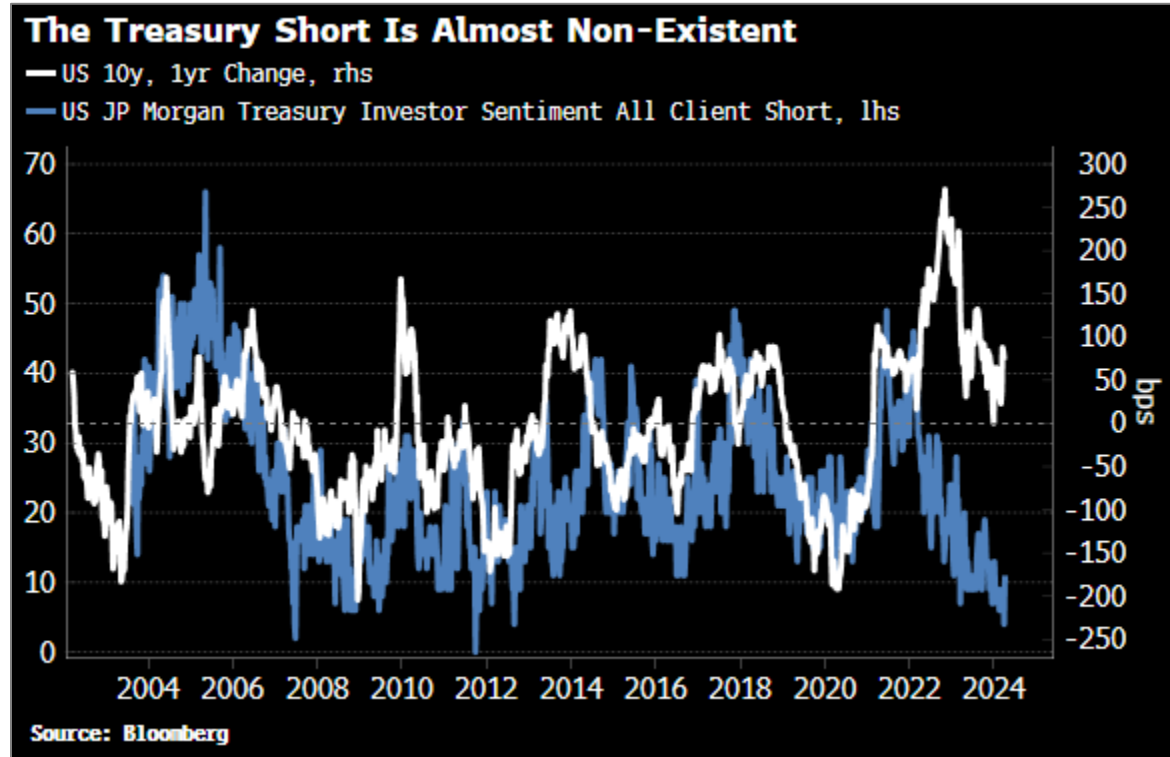


Jobs market continues to run hot, but the gains are coming from Part-Time Employment.

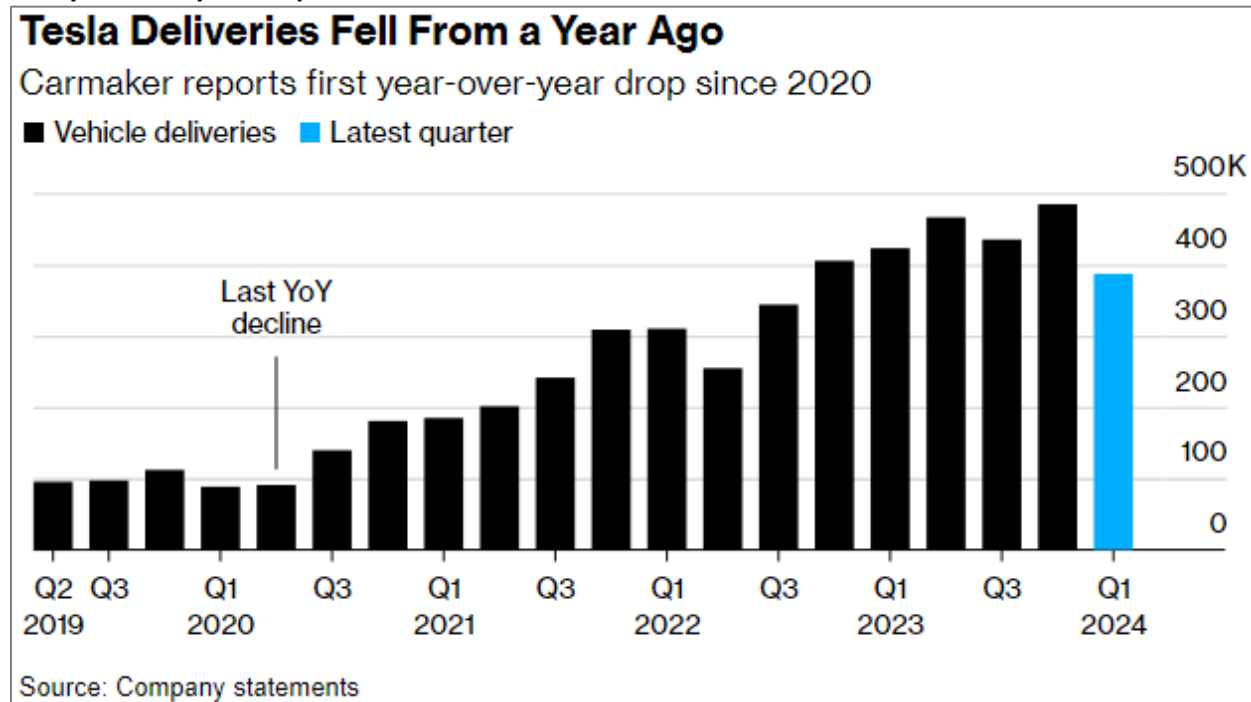


Source: Steph Pomboy

Treasury Sentiment - Investors are confident that rates will not go higher.



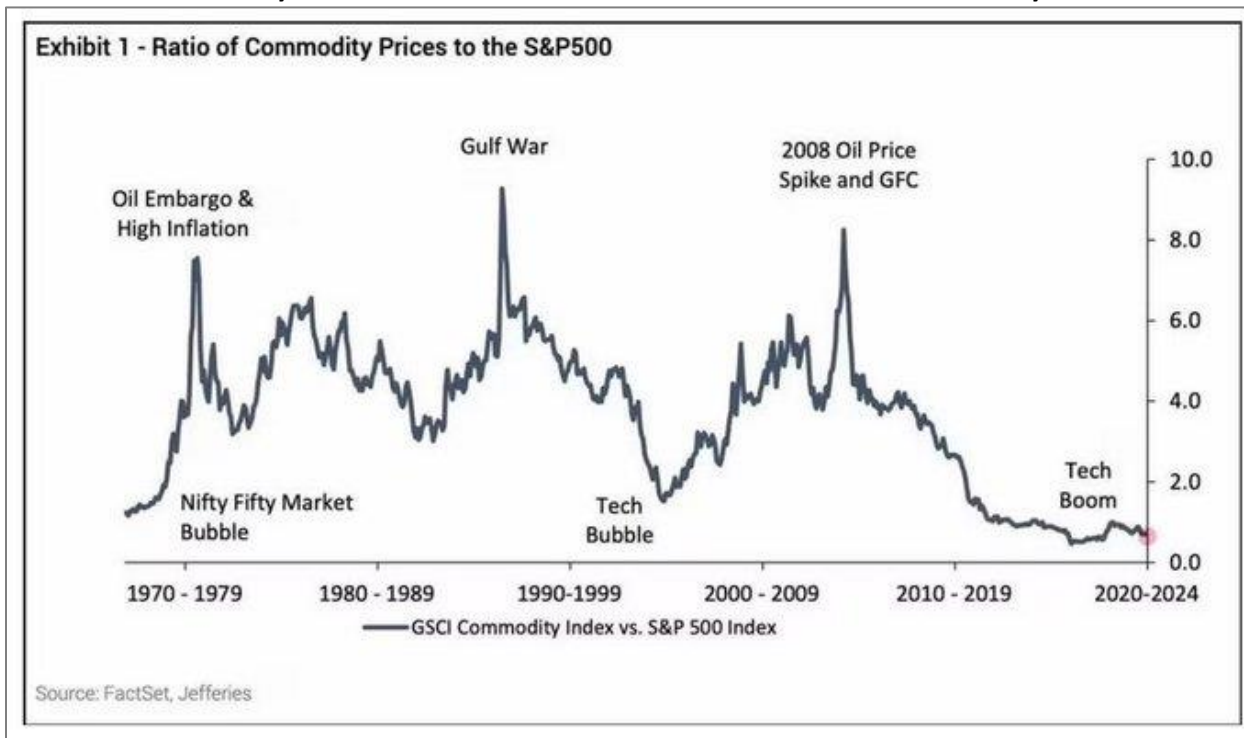
First year-over-year drop in Tesla Deliveries since the 2020 recession.



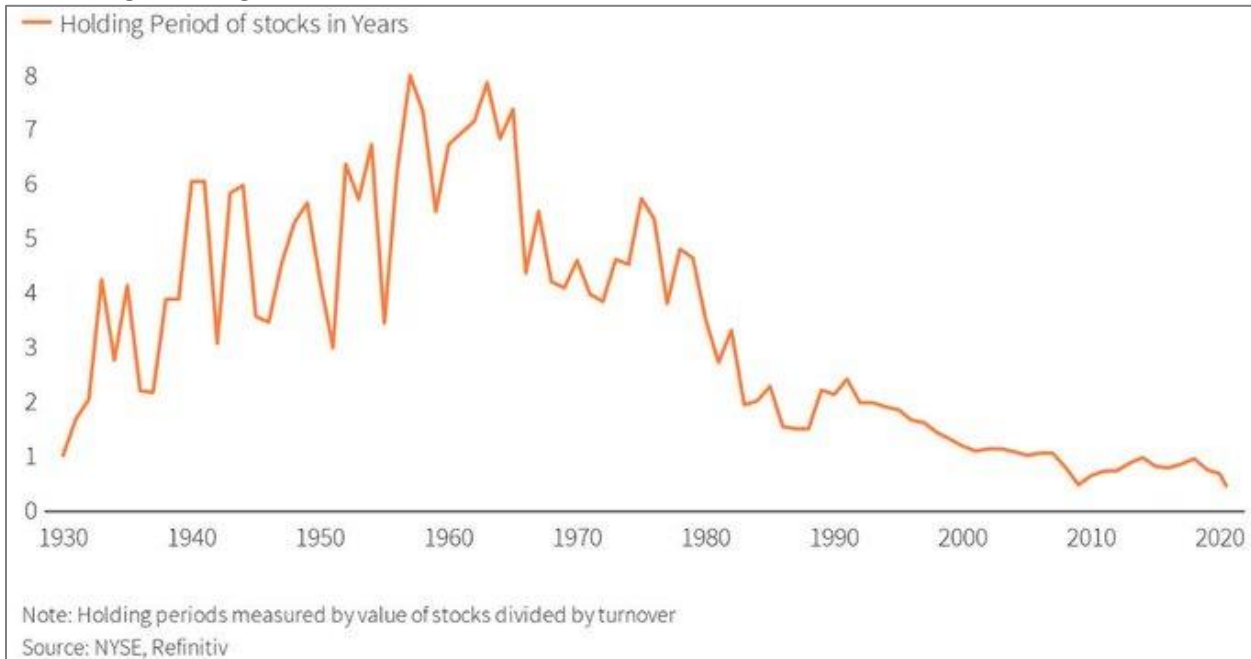
Tech versus Commodities outperformance breaks the dot-com record.



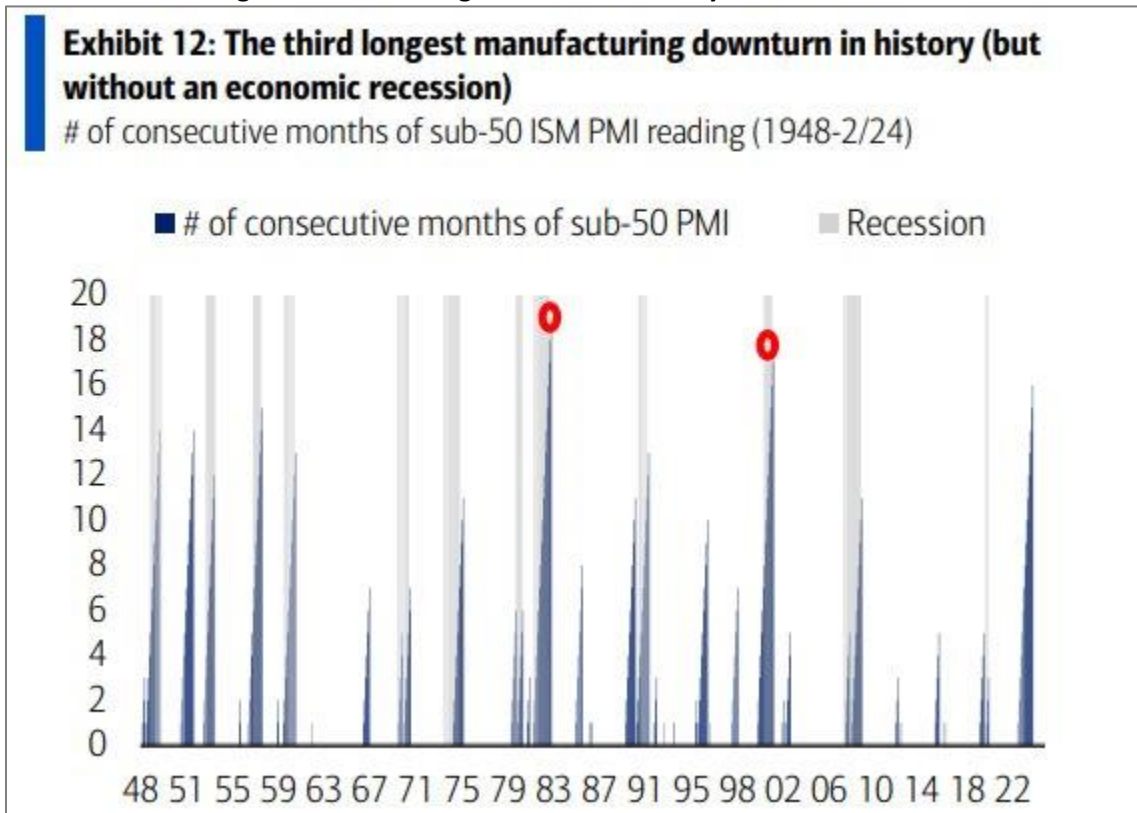
Commodities have only been this out of favor three times in more than half a century.



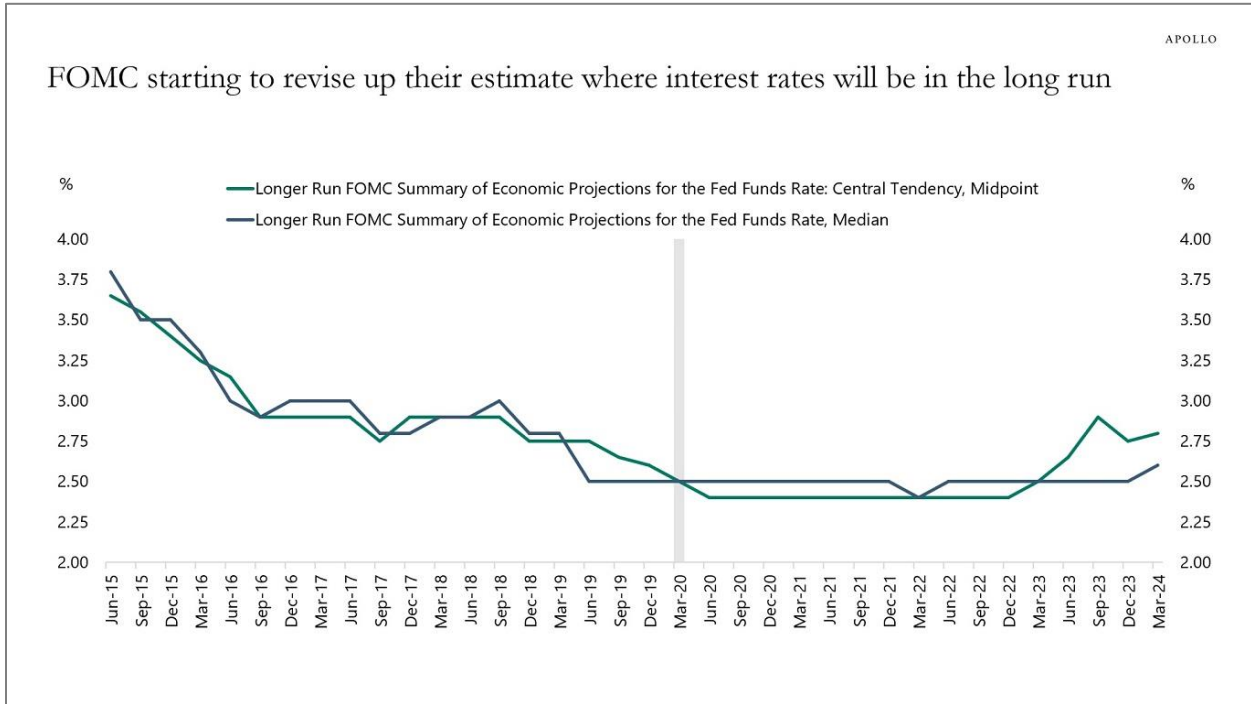
The average Holding Period for stocks is at record lows.



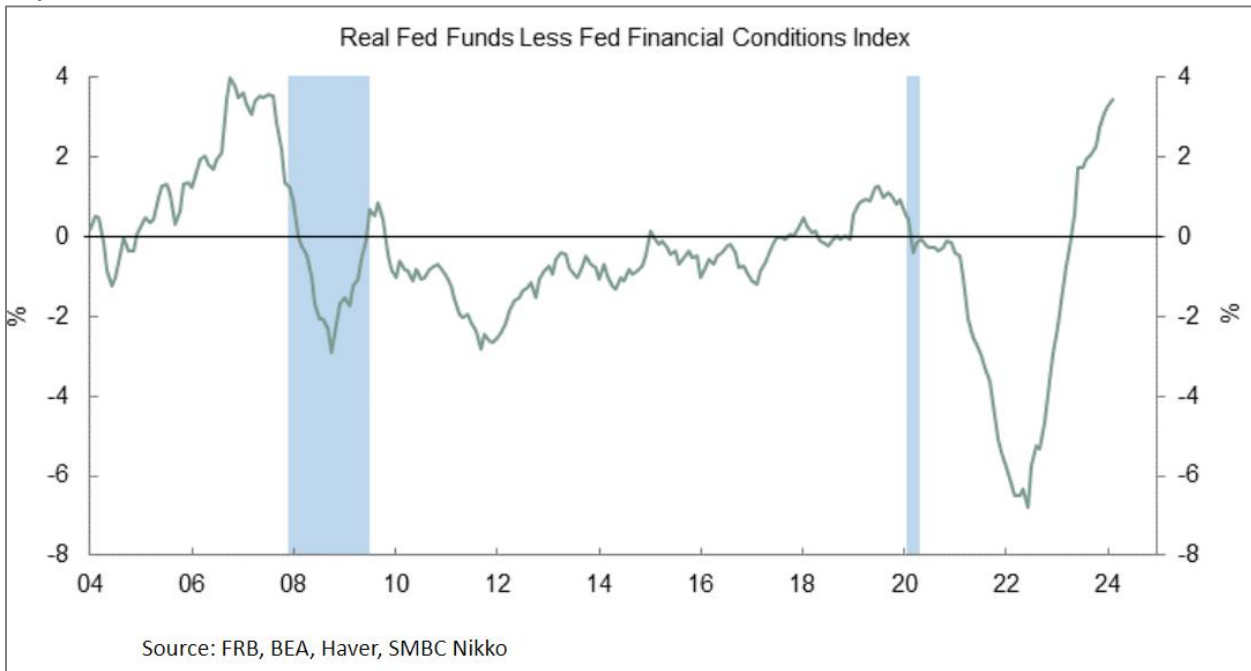
This is the third longest manufacturing downturn in history.



The Fed is increasing its estimate for interest rates in the long run.



Gap between the real Fed Funds and Fed Financial Conditions Index is the widest since 2007.



Investor appetite for corporate credit has driven spreads as narrow as they've ever been.

Nothing to See Here

Investment grade credit spreads are as narrow as they've ever been

Yield Spread of BAA Corporate Credit Over 5-Year Treasuries



Source: Moody's Investors Service, Bloomberg

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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