



# Market Outlook

By Mark T Dodson, CFA

## Overweight in a Narrow Market

Market Risk Index climbed to a bull market high of 87.1% on a worsening of all three counter-cyclical factors of our asset allocation model. We'd note bull market peaks in 2020 and 2022 both had MRI readings above slightly above 90%. Monetary Conditions are a rounding error away from a 50<sup>th</sup> percentile reading, having moved from the best third of readings early in the year to a more neutral reading now. Psychology moved into the worst three percent of readings, and Valuations moved into the worst 0.3% of readings in history, eclipsed only by the dot-com era valuations.

One detractor for Valuations came from the average equity allocations to equities. The Financial Accounts of the United States data was released for Q1, and the average equity allocation in the United States climbed to 50%, matching the level from December 2021, a level that implies negative stock returns over the next 7-10 years. Using the change in stock prices during the second quarter and month to month changes in the AAI Allocation survey, we estimate that the average allocation will finish the second quarter within one percent of the dot-com era high.

Appetite for financial leverage broadened as net exposure to US stocks using Leveraged ETFs set another new cycle high and finished the week just shy of a new all-time high. Assets in Leveraged ETFs outnumber Inverse ETF assets by nearly 7 to 1. However, Technicals were responsible for much of the deterioration in the Psychology Composite this week.

Unlike the highs earlier in the year, recent highs in widely followed cap-weighted indices are notable for how lonely they are, as they are driven by hot performance in a handful of mega-cap names. Only two sectors joined the market to make new highs, participation that is reminiscent of the dot-com era. The last two bull market peaks had five and six sectors making new highs alongside the market. The advance decline line has also failed to confirm recent highs, and new lows have made a habit of outnumbering new highs in recent weeks, enough to trigger another "Titanic Syndrome" for the NASDAQ.

*Note: A Market Outlook will not be released next week because of upcoming travel.*

### Market Risk Index

Rec Allocation 25% Underweight

**87.1%**

### Category Percentiles

Psychology - P6



Monetary - M3



Valuation - Extremely Overvalued



Trend



### Largest Psychology Influences

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

### Largest Monetary Influences

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

### Valuation

7-10 Year Equity Return Forecast	0.0%
10Yr US Treasury Yield	4.4%

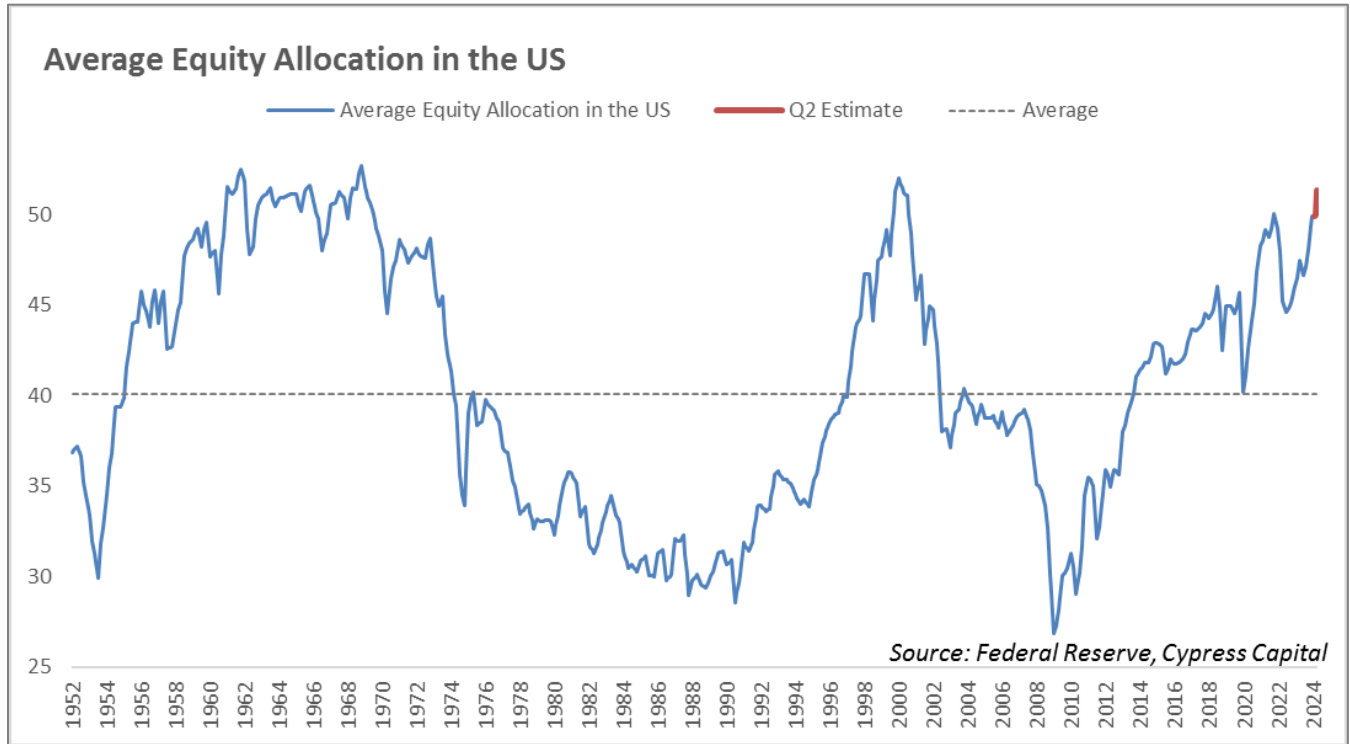
### Market Trends

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

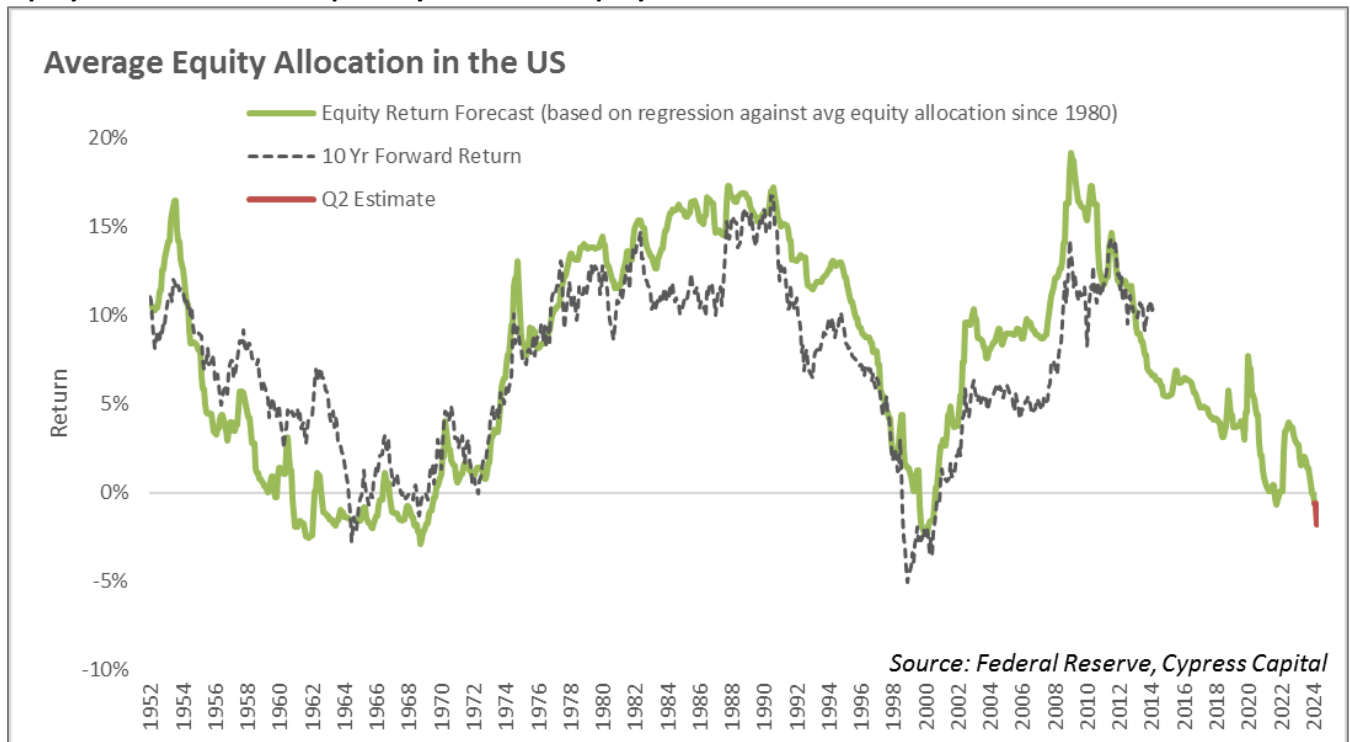
*Market Risk Index scales from 0 to 100%. Higher readings correspond with higher risk markets based on our model & opinion. Scores below 25% are bullish. Scores between 25-75% are neutral, and scores above 75% are markets vulnerable to major drawdowns.*

**Charts of the Week**

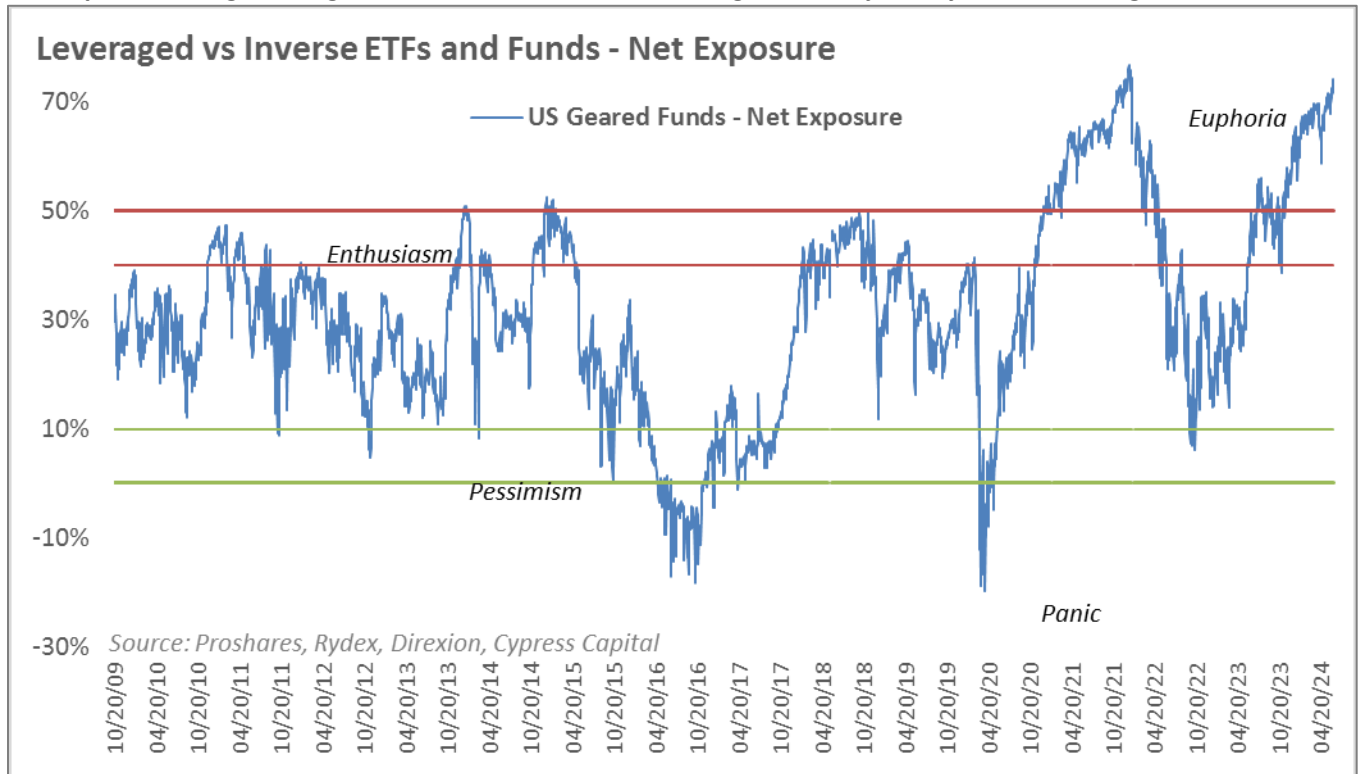
**Household Equity Allocations matched the 2021 bull market peak in Q1.**



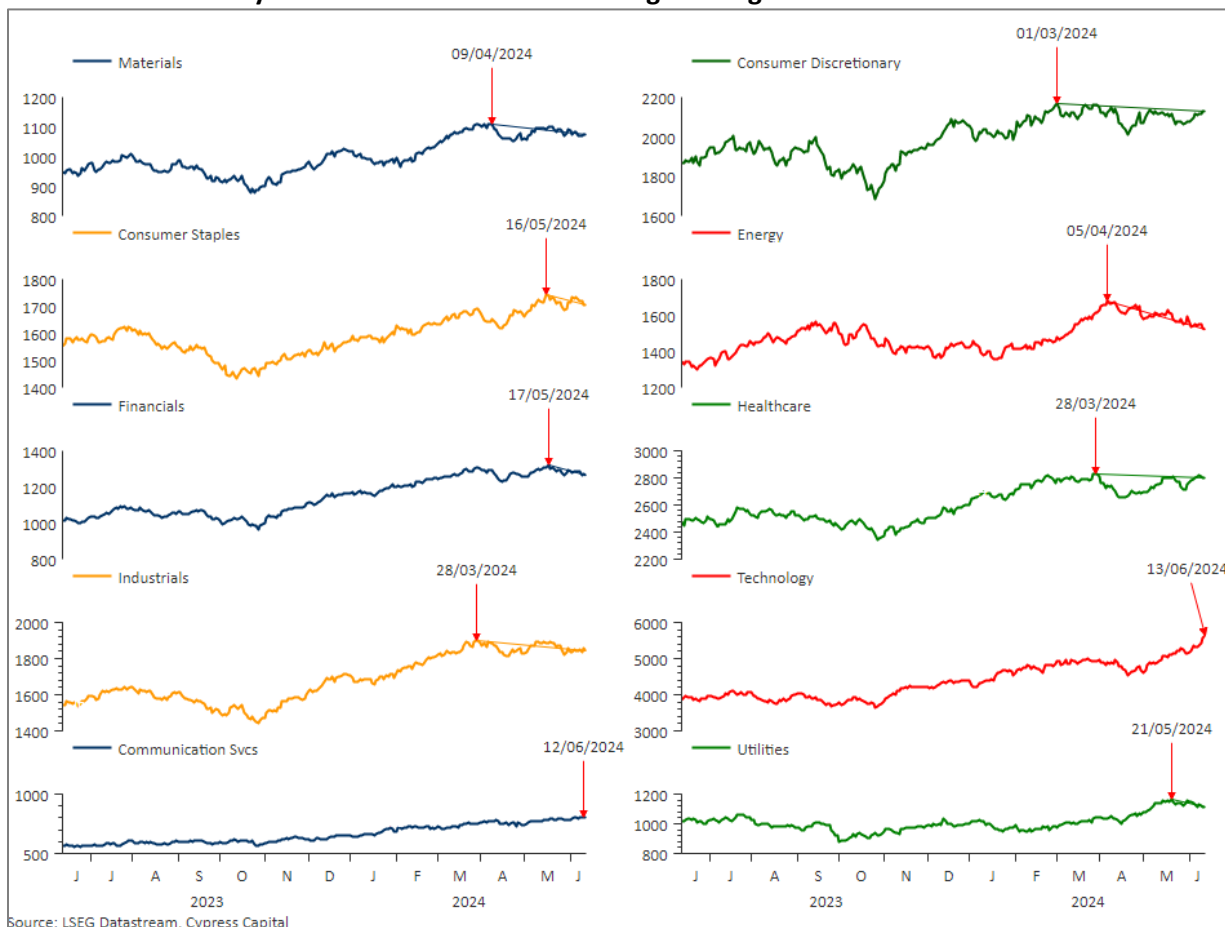
**Equity Return Forecasts implied by Household Equity Allocations have fallen below zero.**



**Net Exposure using Leveraged ETFs set a new bull market high and are just shy of a record high.**

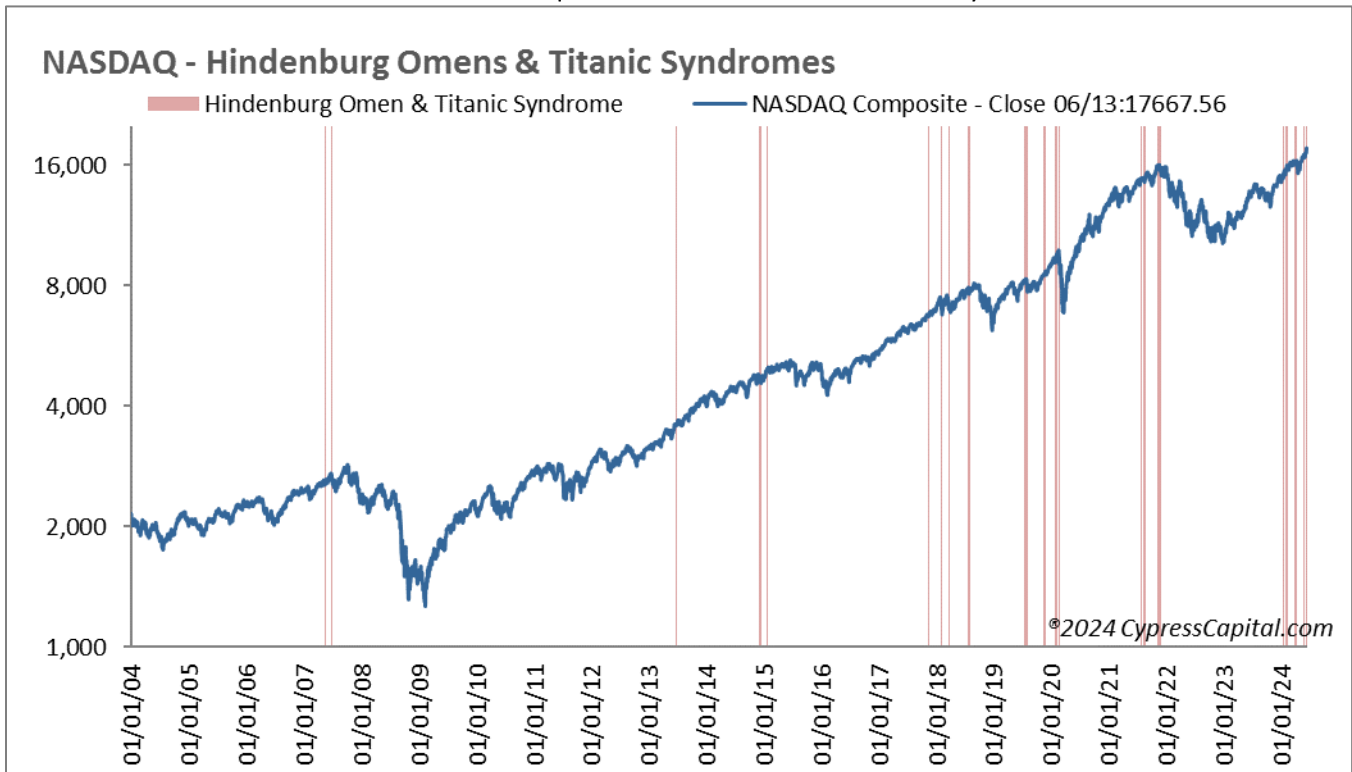


**Narrow market - only two of 10 sectors made new highs along with the S&P 500 this week.**

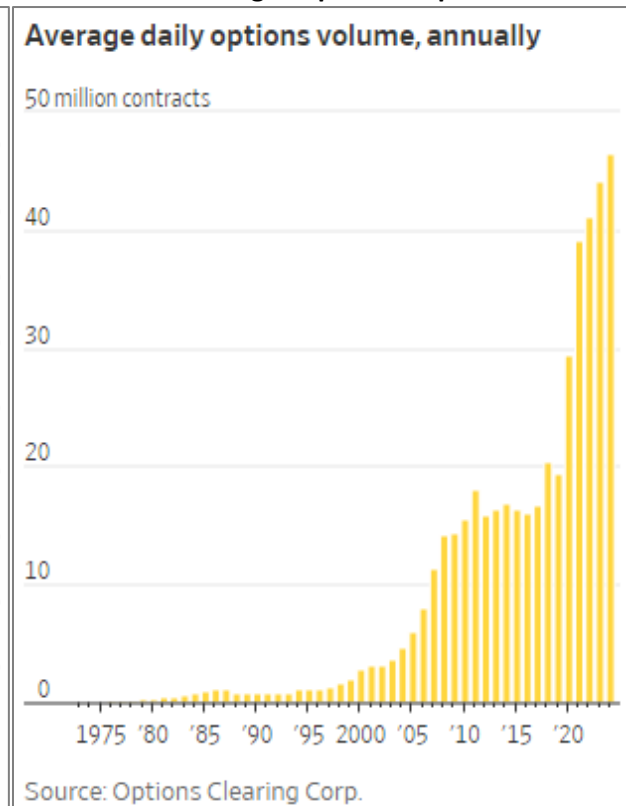
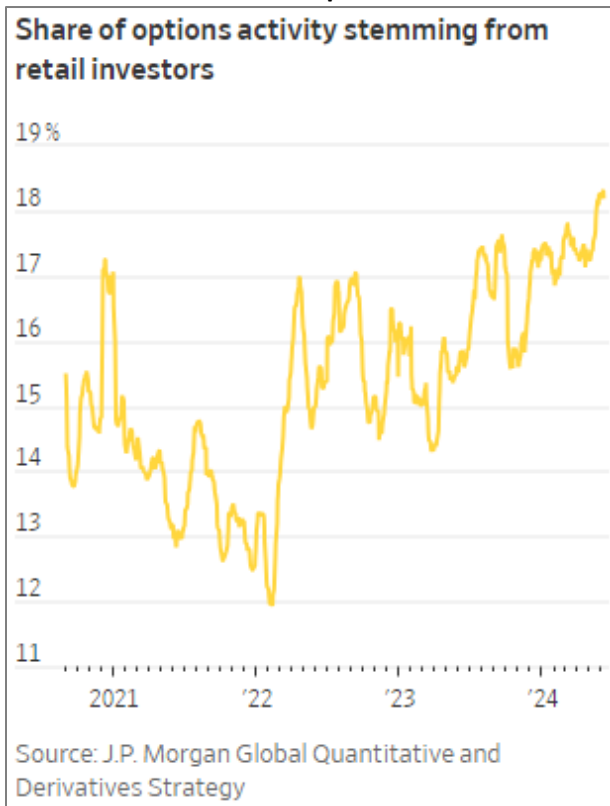


**Another combined Hindenberg Omen & Titanic Syndrome this week for the NASDAQ.**

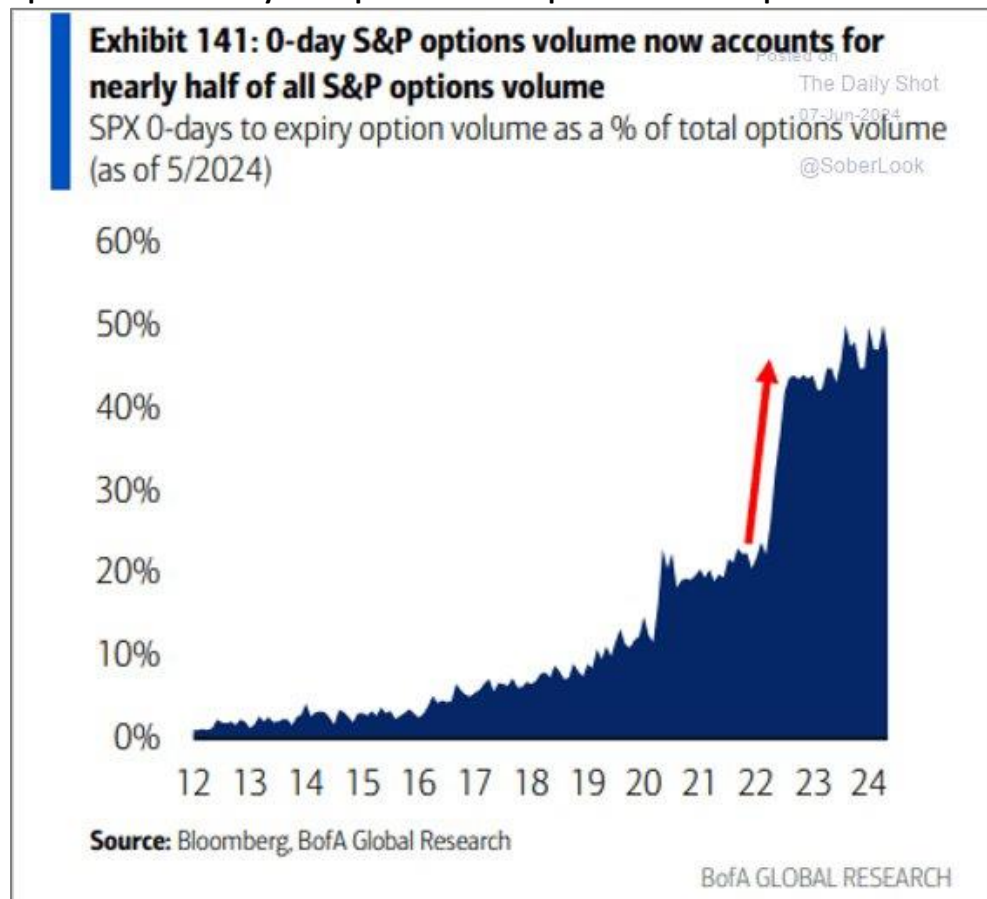
The ominously named signals are designed to pick up periods where stock market rallies have unfavorable market internals. Both have become more frequent occurrences over the last six years.



**Retail Investors' share of options volume set record. Total volume has gone parabolic post-Covid.**



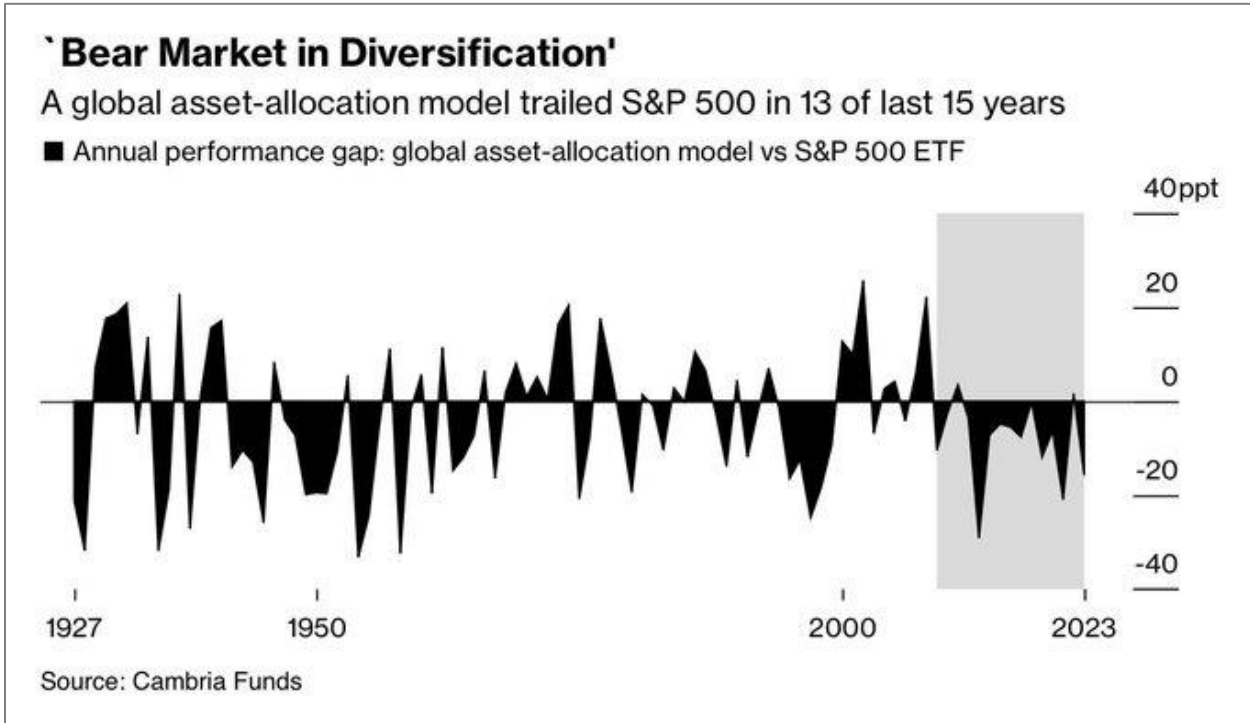
Options with zero days to expiration make up half of all S&P options volume.



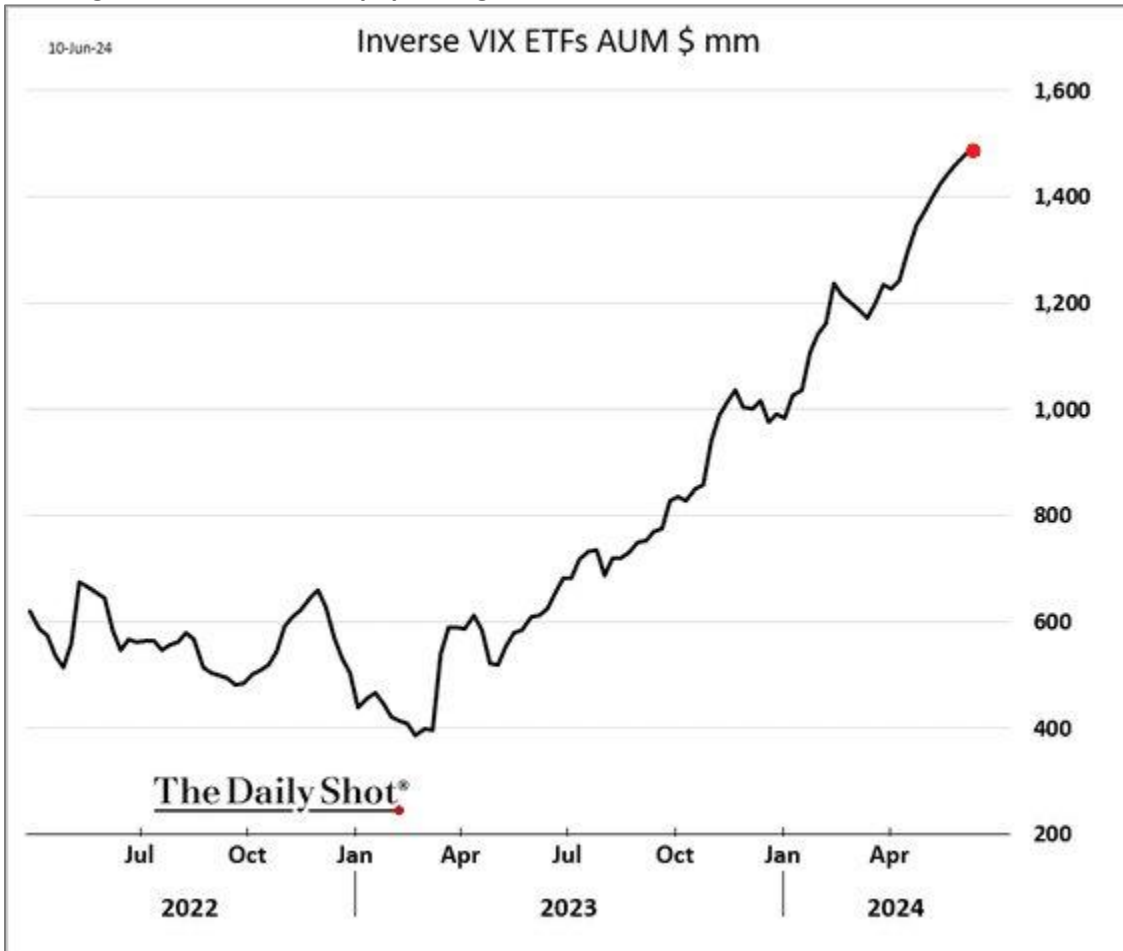
Animal spirits in India – volume on Nifty 50 options surpasses the S&P 500.



A lost decade for diversification - prudent investing is out of favor.



Shorting the VIX has become popular again.





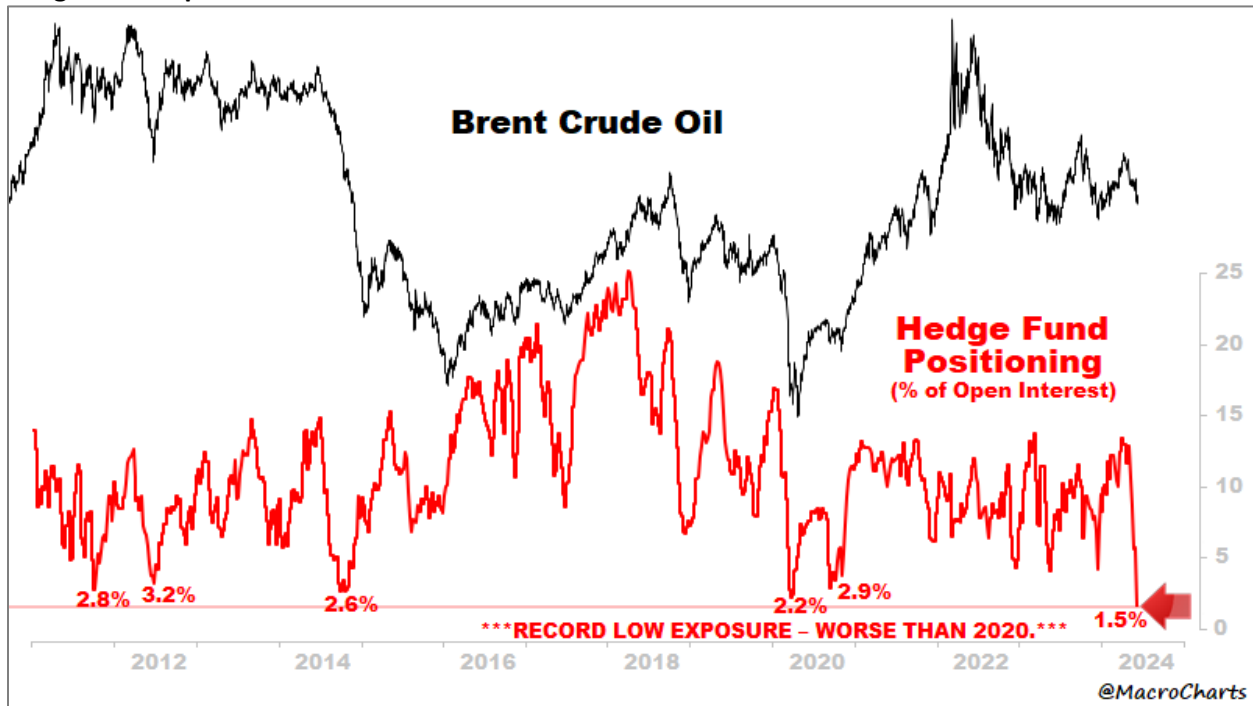
**Stock Market Concentration is close to 100-year highs.**

**Top 10% of stocks by size versus the entire US stock market**

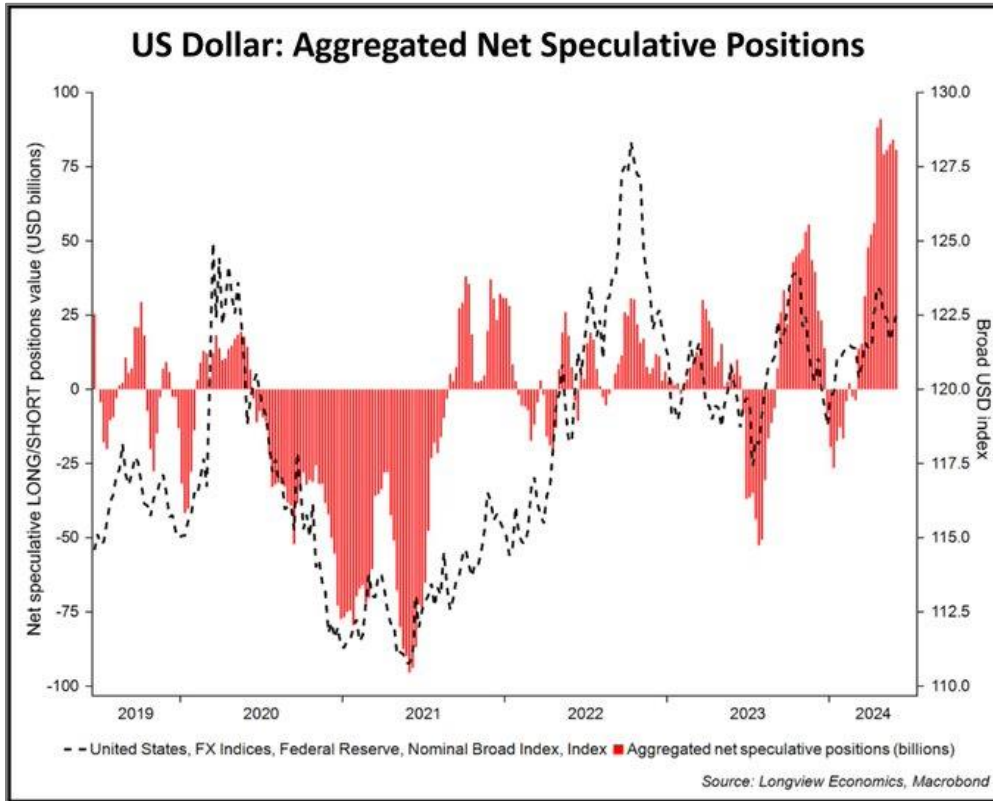


Source: Kenneth R. French database, Deutsche Bank.

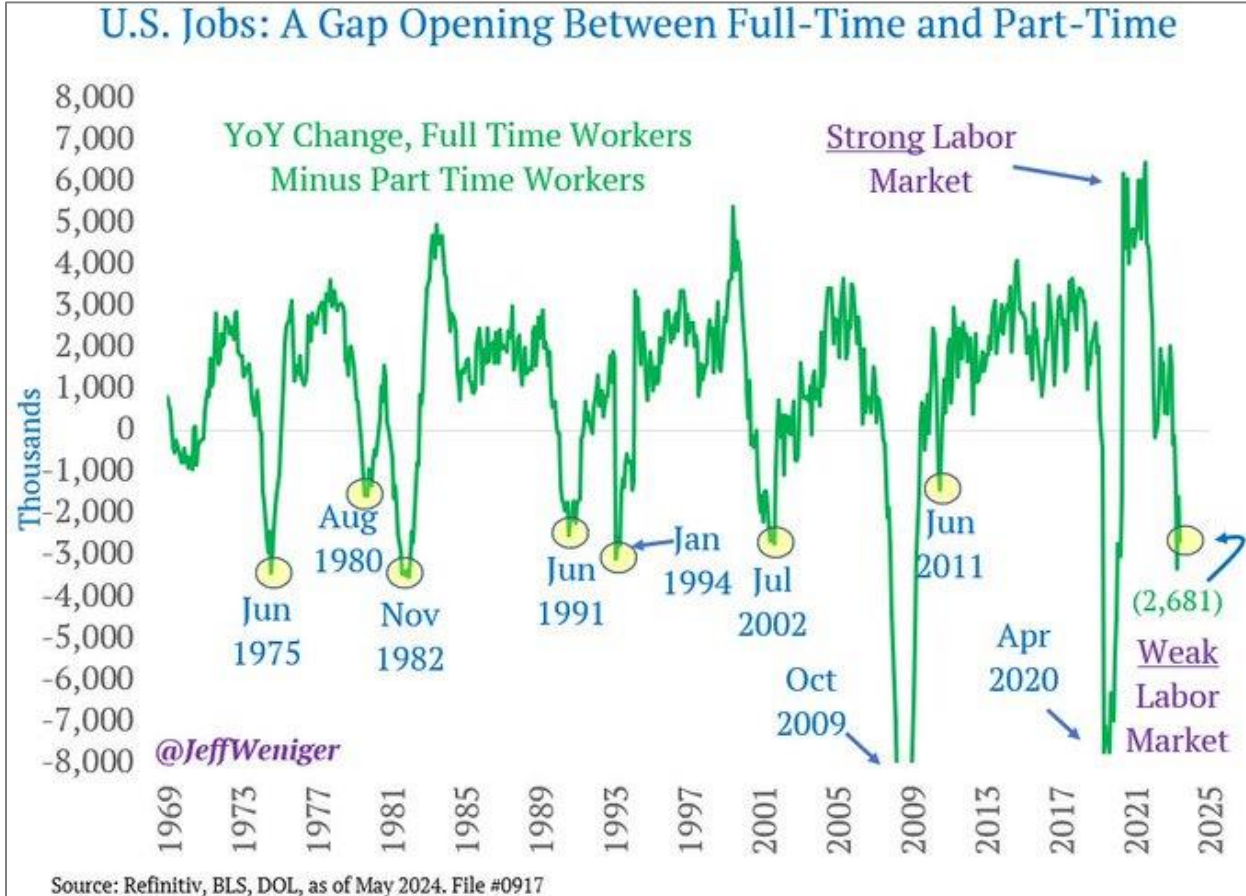
**Hedge Fund Exposure to Crude Oil hits a record low.**



**Speculators are Long the US Dollar.**

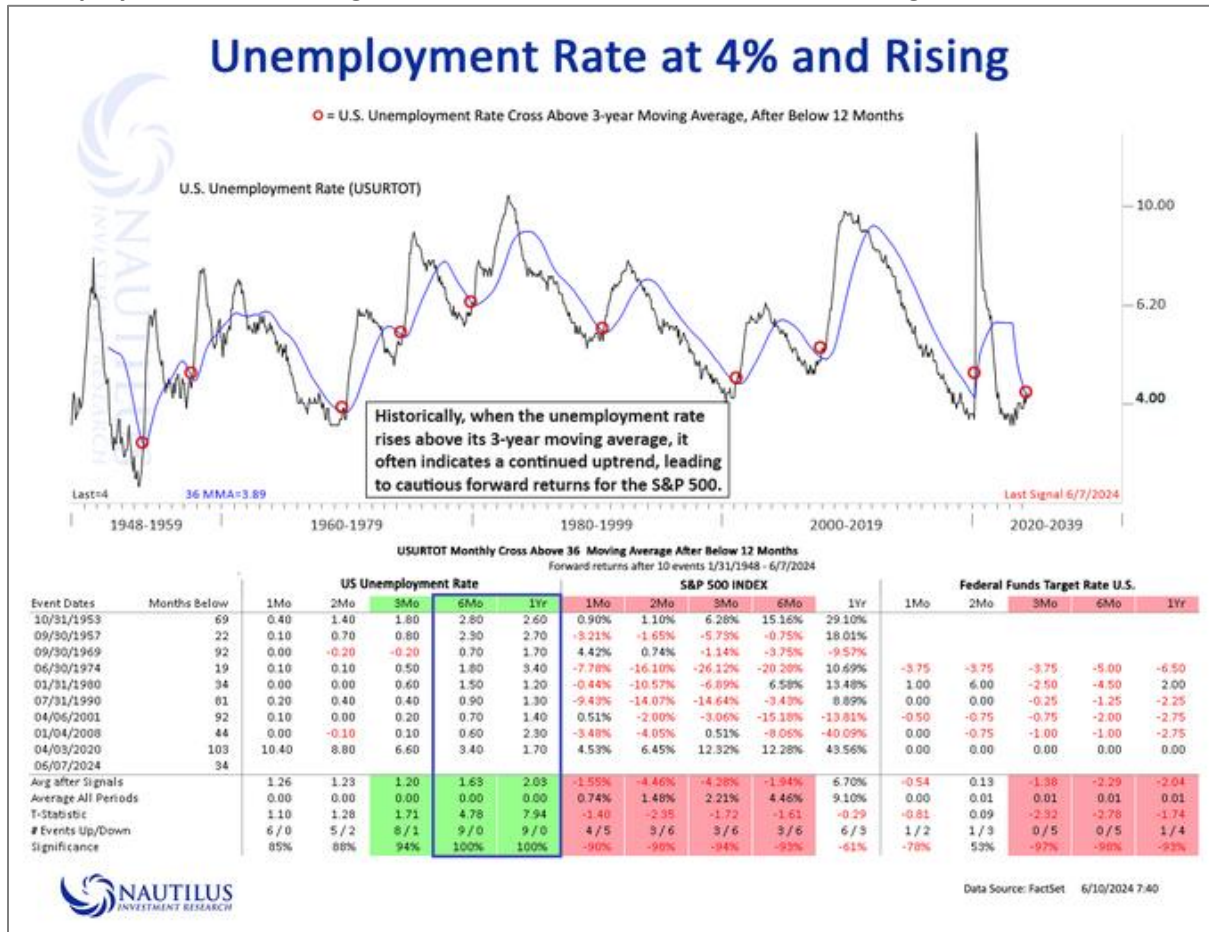


**Softening Labor Market**

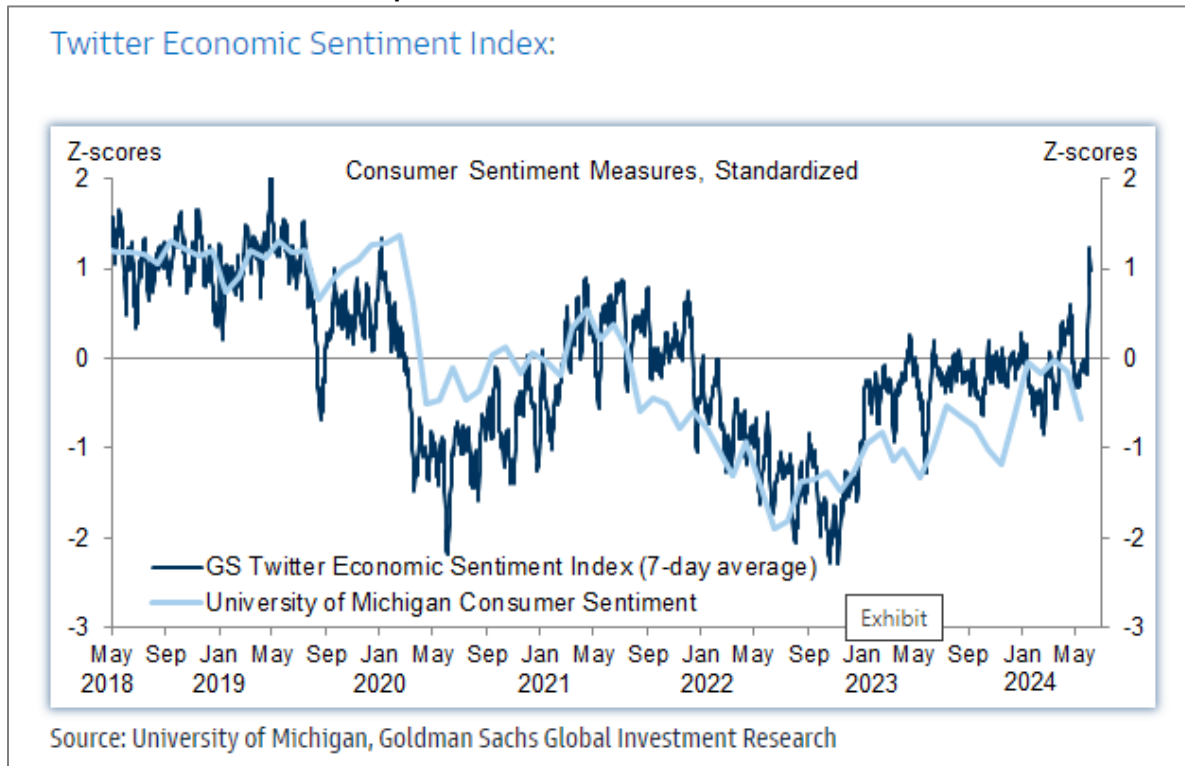




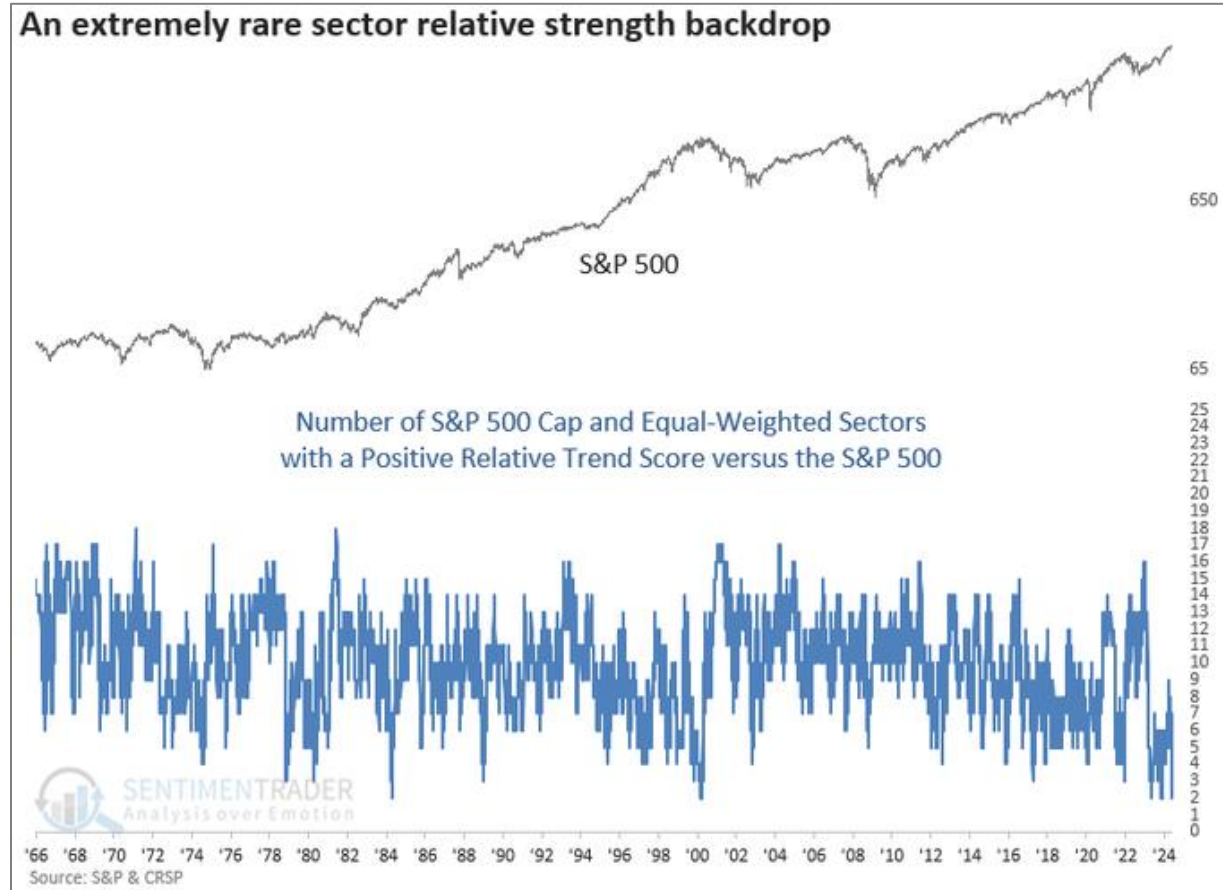
Unemployment Rate crossing above its 3YMA has been a decent risk-off signal for stocks.



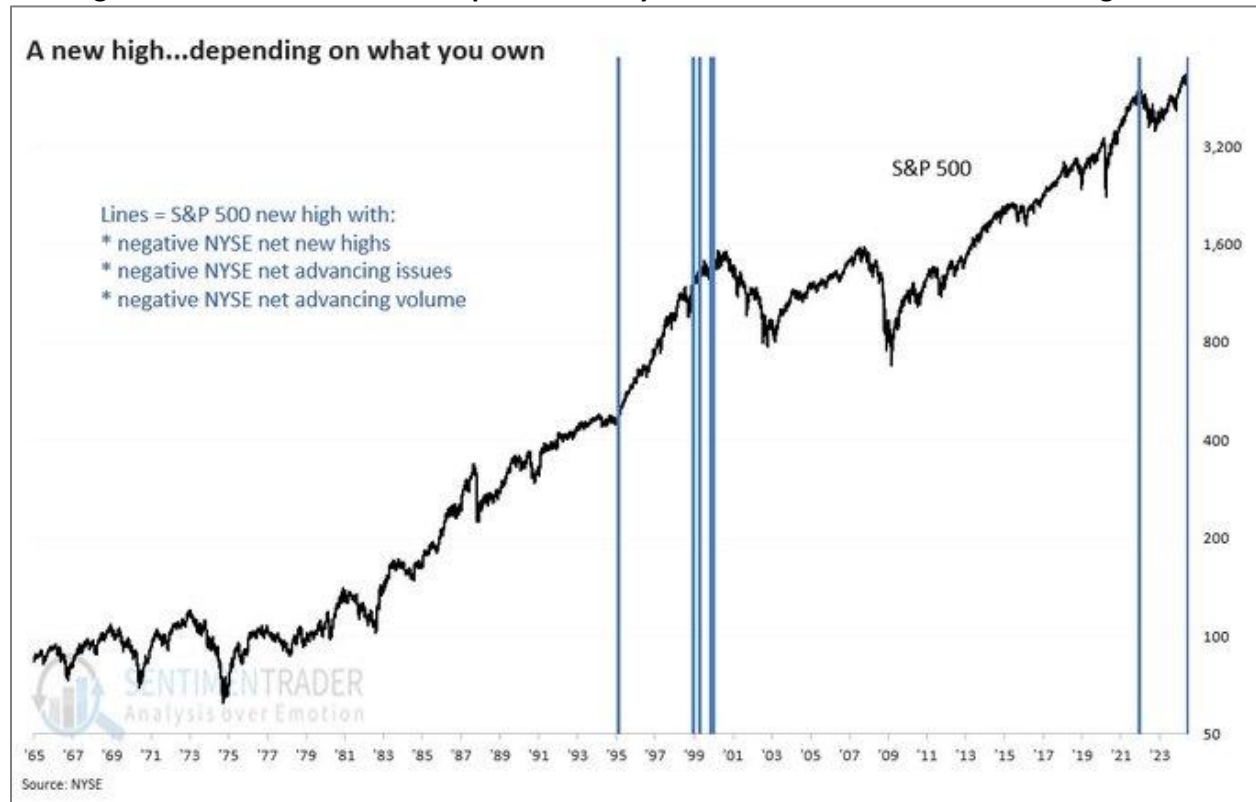
Sentiment on Twitter is back to pre-Covid levels.



**Worst Sector Breadth since 2000.**



**New highs in the S&P 500 when the inputs for all key measures of market internals are negative.**



Semiconductor weighting overtakes Utilities for the first time since 2000.



## 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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