



Market Outlook

By Mark T Dodson, CFA

Bull Market is going as Dot-Com Era for Halloween.

Market Risk Index improved to 86.3% as Monetary Conditions reversed some of its recent deterioration. Psychology increased to 98.5%, the closest to the worst one percent of readings since April of this year. Outside of this year, readings above 99% for the Psychology Composite have only occurred in 2000 and 2021.

Should the sharp rise in yields over the last six weeks hold or continue, it will be difficult for the Fed to follow through with another rate cut in November. It hasn't stopped Asset Managers (traditionally dumb money) from taking their long position in Treasury futures to another record high, fighting the trend higher in yields.

Higher yields have also brought the yield curve (the 10Yr minus T-Bill version) closer to a positive slope since the first month of inversion over two years ago. However, rapid progress toward reversion doesn't usually come from the long end of the curve - it's the opposite. Over the last 100 years, in the three months leading up to a yield curve reversion, Treasury bill yields dropped more than 75 basis points with no change in 10Yr Treasury yields on average. The only reversions that bucked that trend with the 10-year yield doing more heavy lifting and climbing in the months leading up to the yield curve reversion occurred in 1921, 1969, 1981, and 2007. All were associated with bear markets and recessions.

If there is a mixed message from Monetary Conditions hovering near the 50th percentile, valuations are decisive in their assessment of equity markets, again scoring in the 100th percentile for overvaluation. Price to Peak earnings, the Price to Book ratio on US stocks, and even Shiller's Cyclically Adjusted PE ratio are only a modest, incremental rally away from taking out their dot-com era highs. Stocks priced relative interest rates and inflation also look excessive, with our Rule of 20 PE having climbed to the highest level since the dot-com era and consequently surpassing the high from September 1987 this year.

Even relative to the level of money in the economy, something that hasn't been in short supply, the stock market is looking frothy. The market cap of the S&P 500 is now twice the value of MZM, something not seen since early 2001. In the past, the value of stocks rarely got 10 to 15% above the value of money in the economy before correcting. That all changed right around

Market Risk Index

Rec Allocation 20% Underweight

86.3%

Category Percentiles

Psychology - P6



Monetary - M3



Valuation - Extremely Overvalued



Trend



Largest Psychology Influences

Leveraged Investments	Negative
Consumer Confidence	Negative
Flow of Funds	Negative
Surveys	Negative

Largest Monetary Influences

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

Valuation

7-10 Year Equity Return Forecast	-0.7%
10Yr US Treasury Yield	4.2%

Market Trends

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

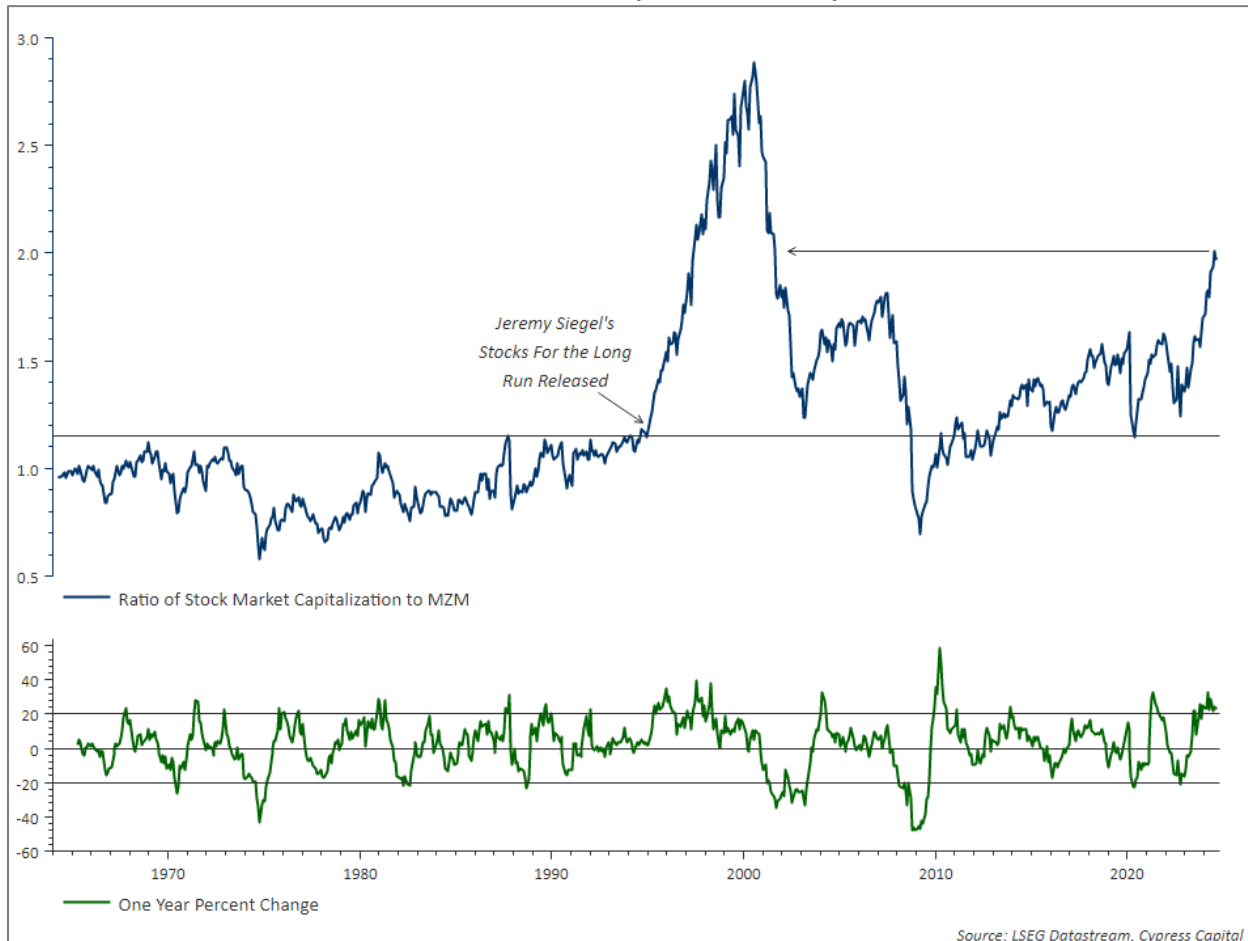
Market Risk Index scales from 0 to 100%. Higher readings correspond with higher risk markets based on our model & opinion. Scores below 25% are bullish. Scores between 25-75% are neutral, and scores above 75% are markets vulnerable to major drawdowns.

the time Jeremy Siegel published *Stocks for the Long Run*, the bible of buy and hold investing. Since then, stock values have never fallen below the level of money in the economy outside of the 2008 financial crisis.

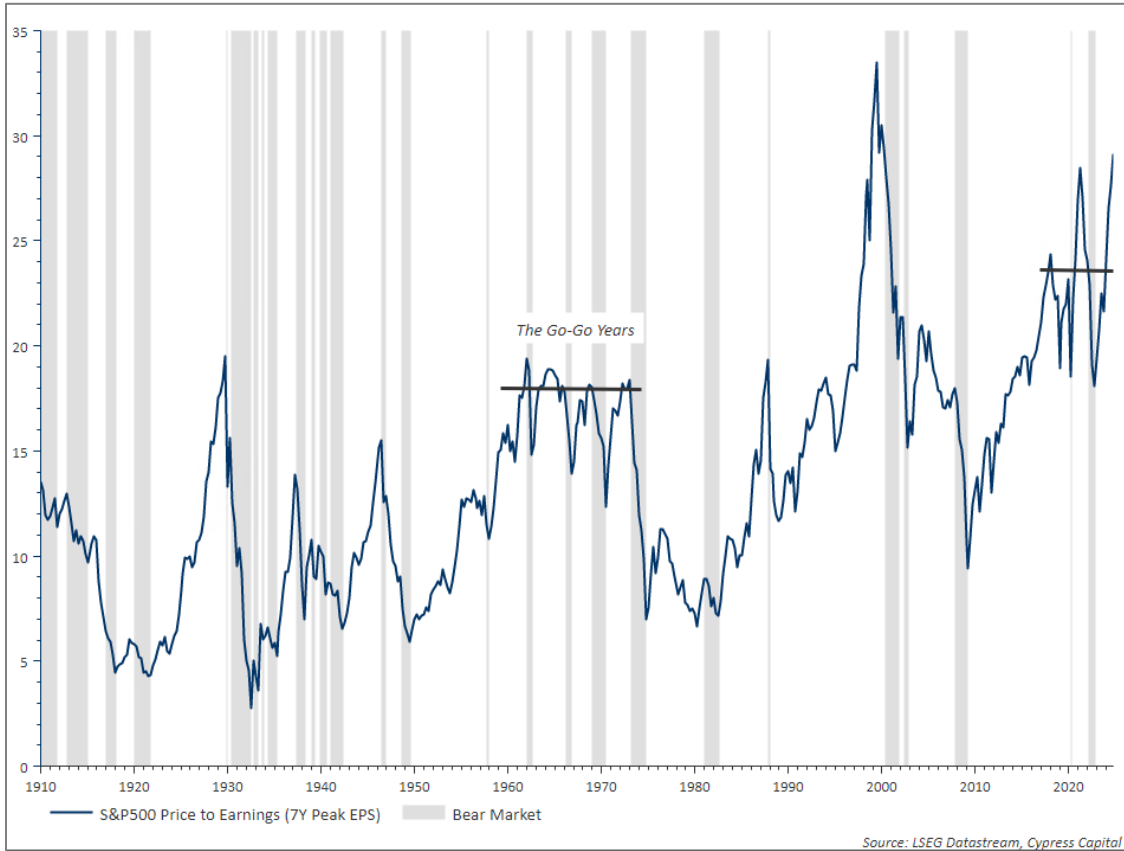
Do momentum and breadth support the idea of more new highs over the coming months? Yes, but if you have any notion of fundamentals or margin of safety in your process, using dot-com era highwater marks as your basis for bull market price targets is analogous to a speculator wearing a prudent investor costume for Halloween.

Charts of the Week

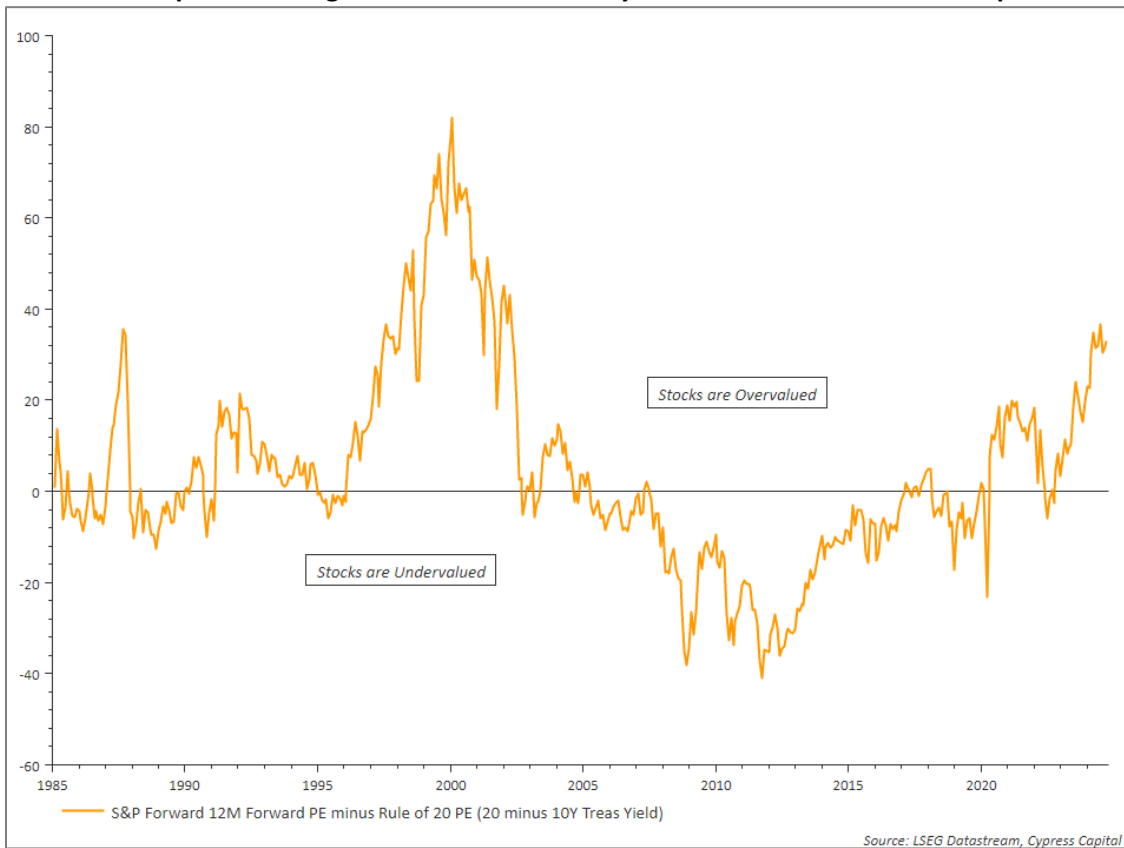
The stock market's value is twice the value of money in the economy for the first time since 2001.



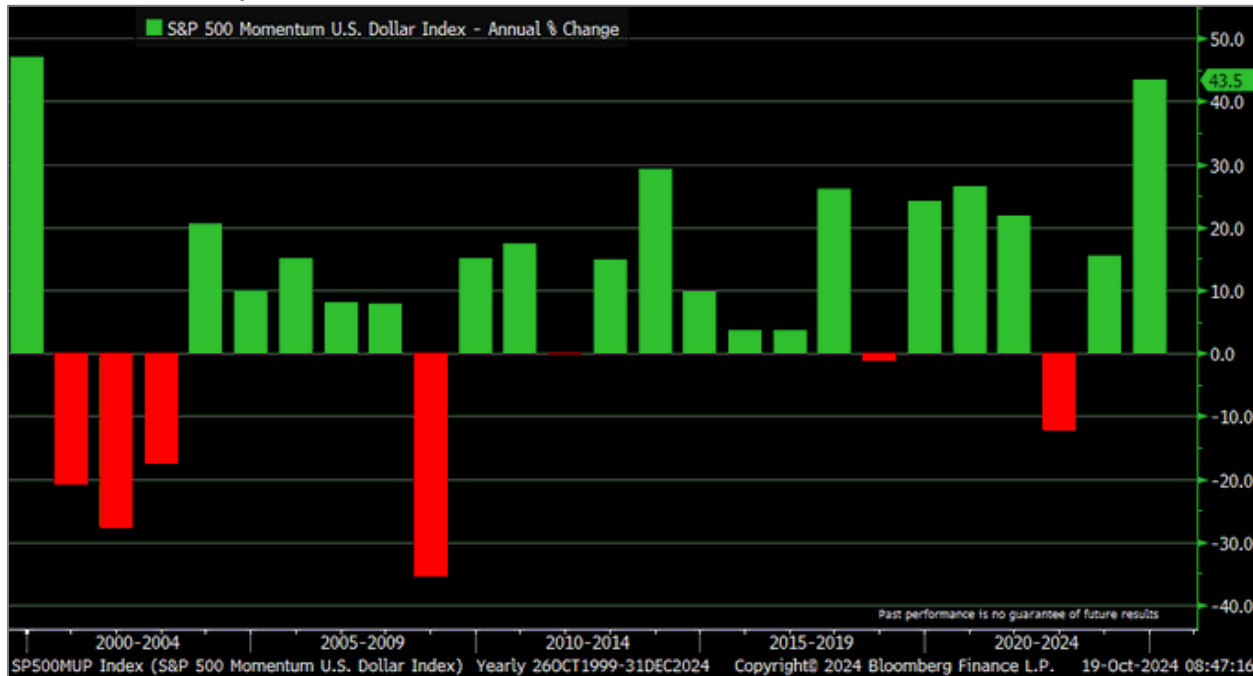
Price to 7Yr Peak Earnings is above 2021 levels.



Stocks look expensive using the Rule of 20 PE – only the dot-com era was more expensive.

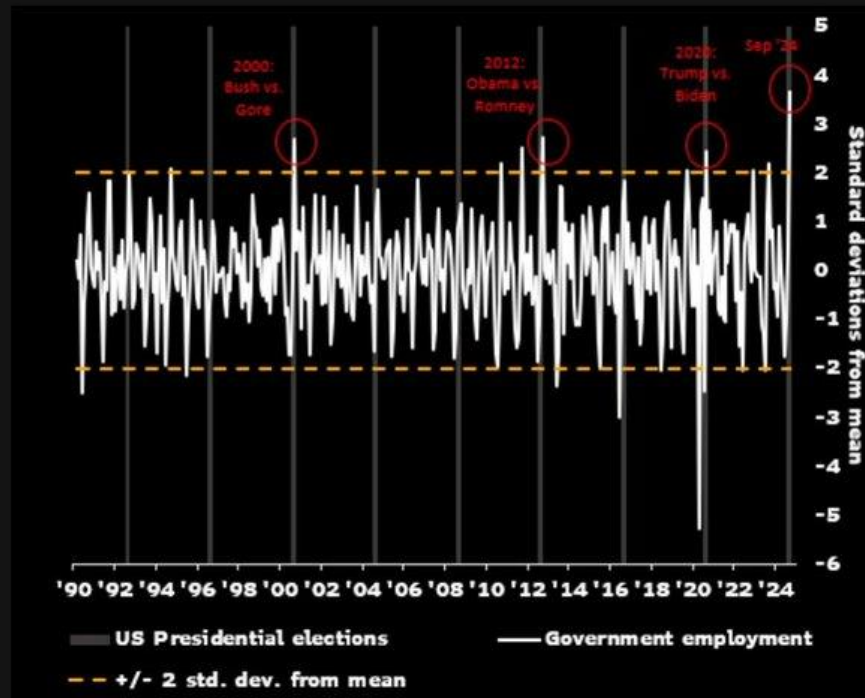


Momentum hasn't partied like this since 1999.



Do politicians hire government workers in election years to massage job numbers?

Anomalous Spike in Government Jobs in September



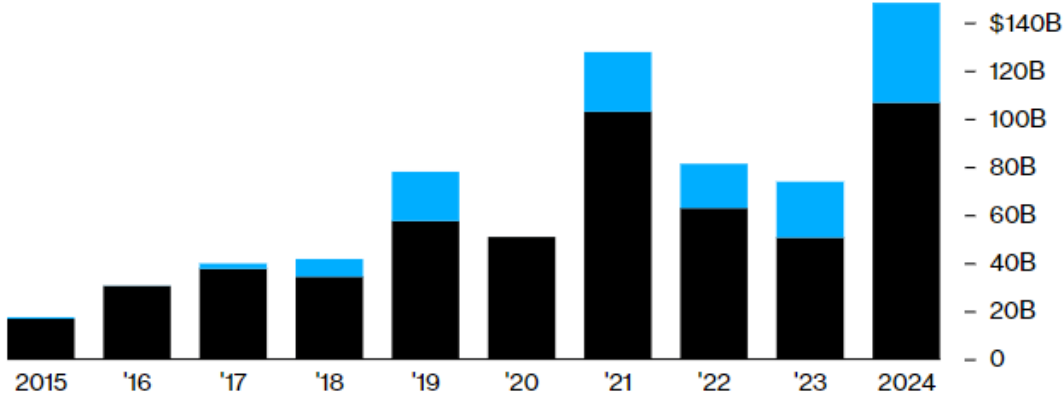
Source: BLS, Bloomberg Economics. Note: Data show the non-seasonally adjusted change in government employment in the CPS survey.

Global Investors US Equity Flows surpassed the 2021 record.

Global Investors Pile Into US Equity ETFs

Flows from both regions combined have beaten 2021's record haul

■ Europe ■ Asia Pacific



Source: Bloomberg Intelligence
 Note: Data in 2024 is year-to-date

Record stock market concentration.

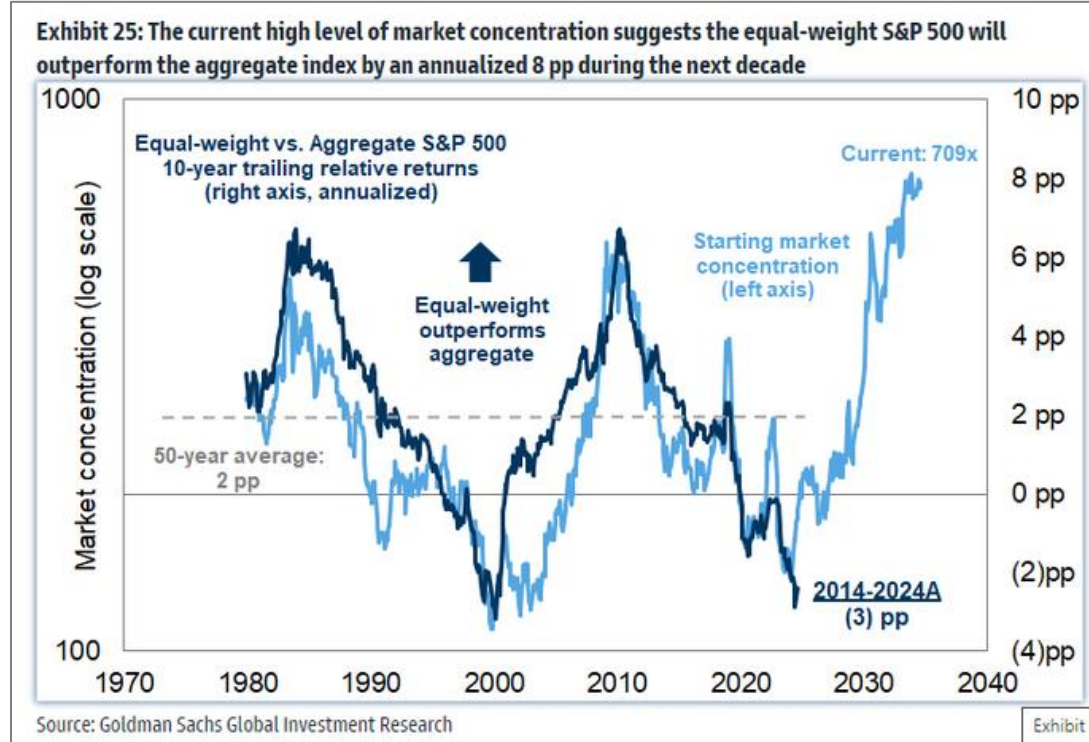
Exhibit 8 : US equity market concentration 1925-2024



Universe consists of US stocks with price, shares, and revenue data listed on the NYSE, AMEX, or NASDAQ exchanges. Series prior to 1985 estimated based on data from the Kenneth French data library, sourced from CRSP, reflecting the market cap distribution of NYSE stocks.

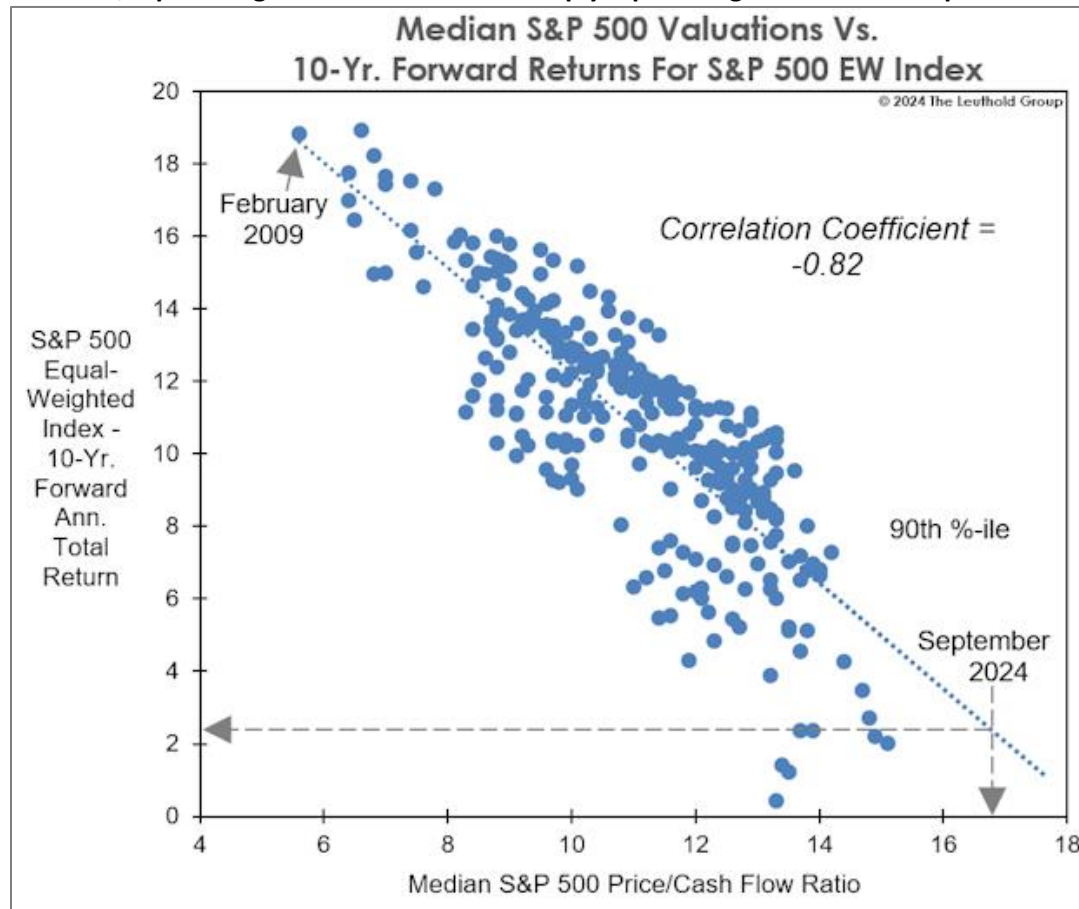
Source: Compustat, CRSP, Kenneth R. French, Goldman Sachs Global Investment Research

High levels of Market Concentration imply that equal-weighted indices should outperform.



Source: John Authers

However, equal-weighted valuations don't imply equal-weighted indices are priced for high returns.



Source: Leuthold Group

The United States economy has grown to twice the size of Europe's since the 2008 Financial Crisis.

America's economy is nearly twice the size of the eurozone's. They were similar in 2008.

Gross domestic product, current prices

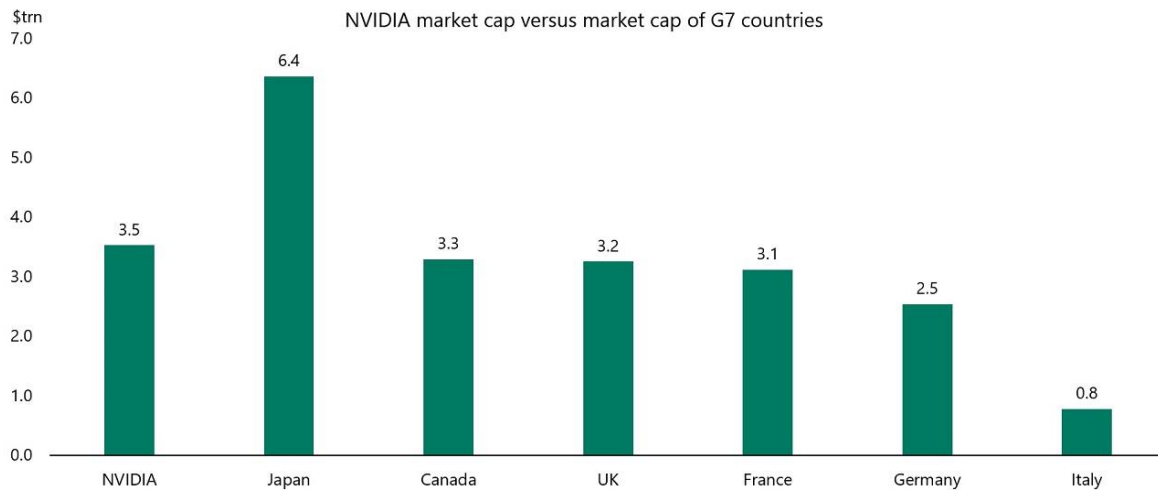


Source: International Monetary Fund

NVIDIA moves global stock market indices more than most countries.

Global equity returns are basically all about NVIDIA

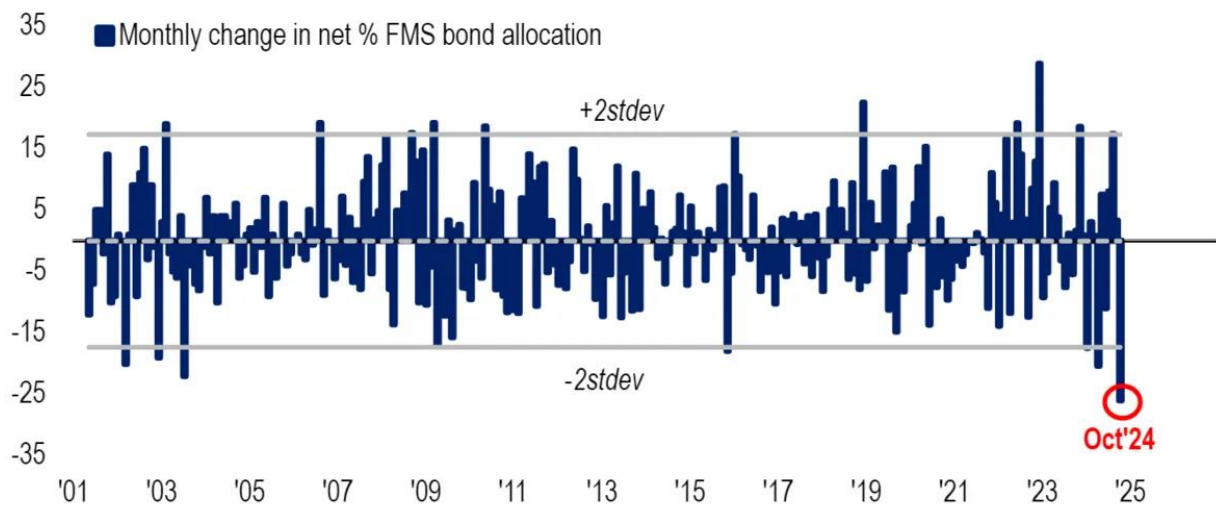
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Record reduction in bond allocations among fund managers.

Chart 1: October FMS shows record monthly reduction in bond allocation

Monthly change in net % FMS bond allocation

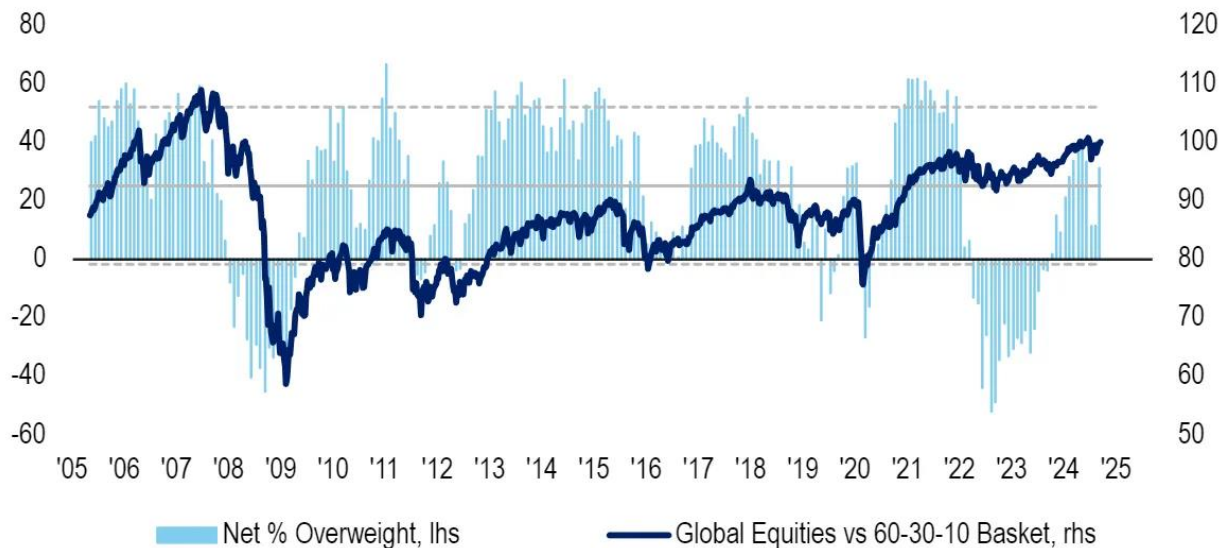


Source: BofA Global Fund Manager Survey

Fund Managers put that money into stocks.

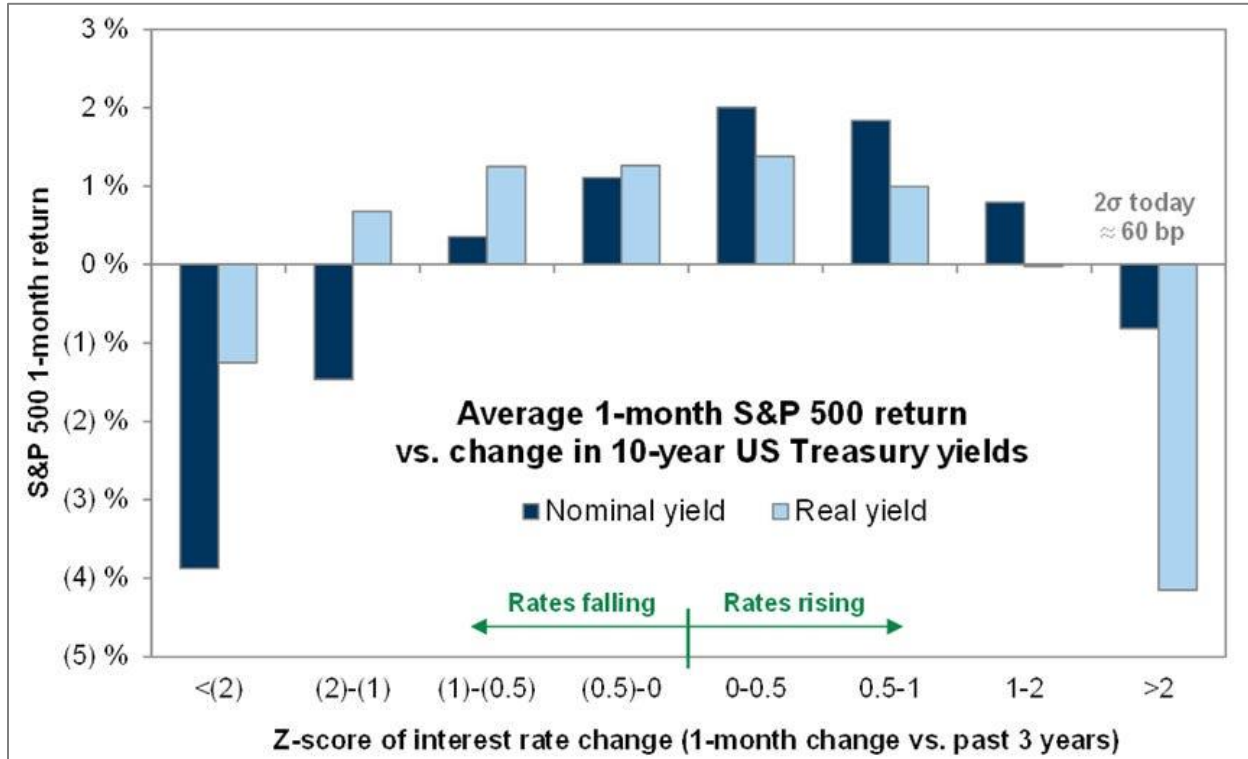
Chart 11: October FMS sees biggest monthly increase in equity allocation in 4 years

Net % FMS OW Equities

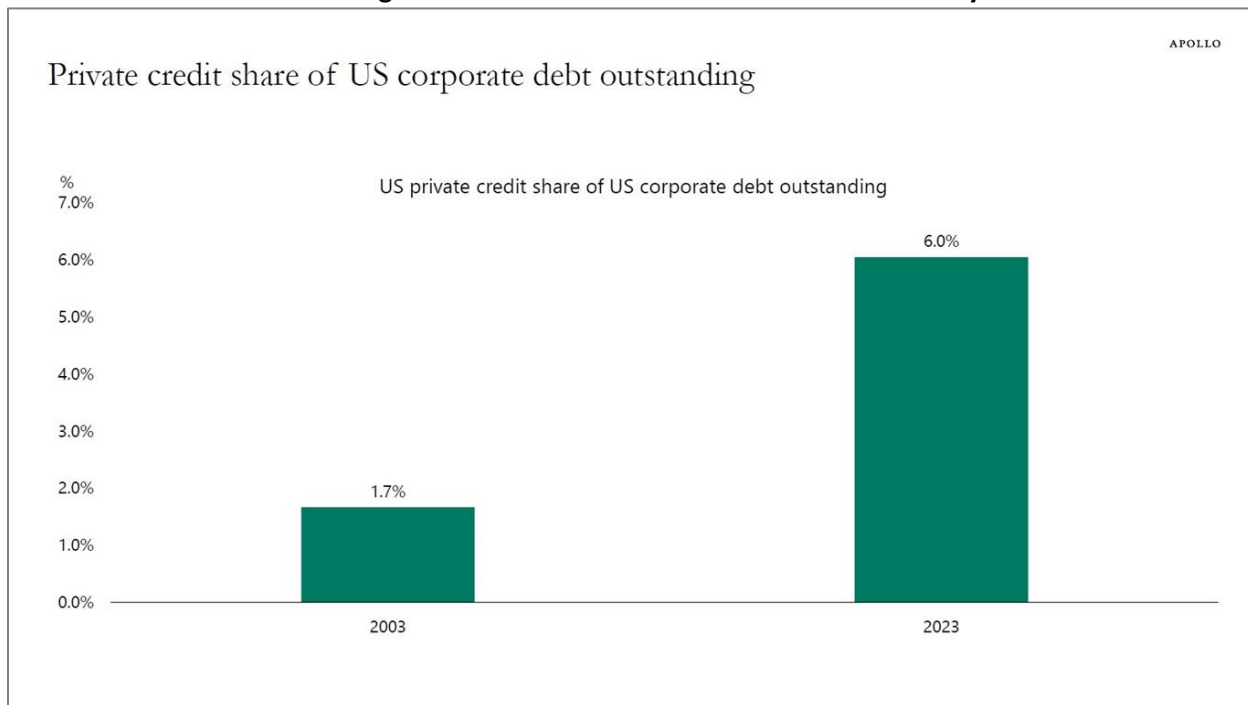


Source: BofA Global Fund Manager Survey

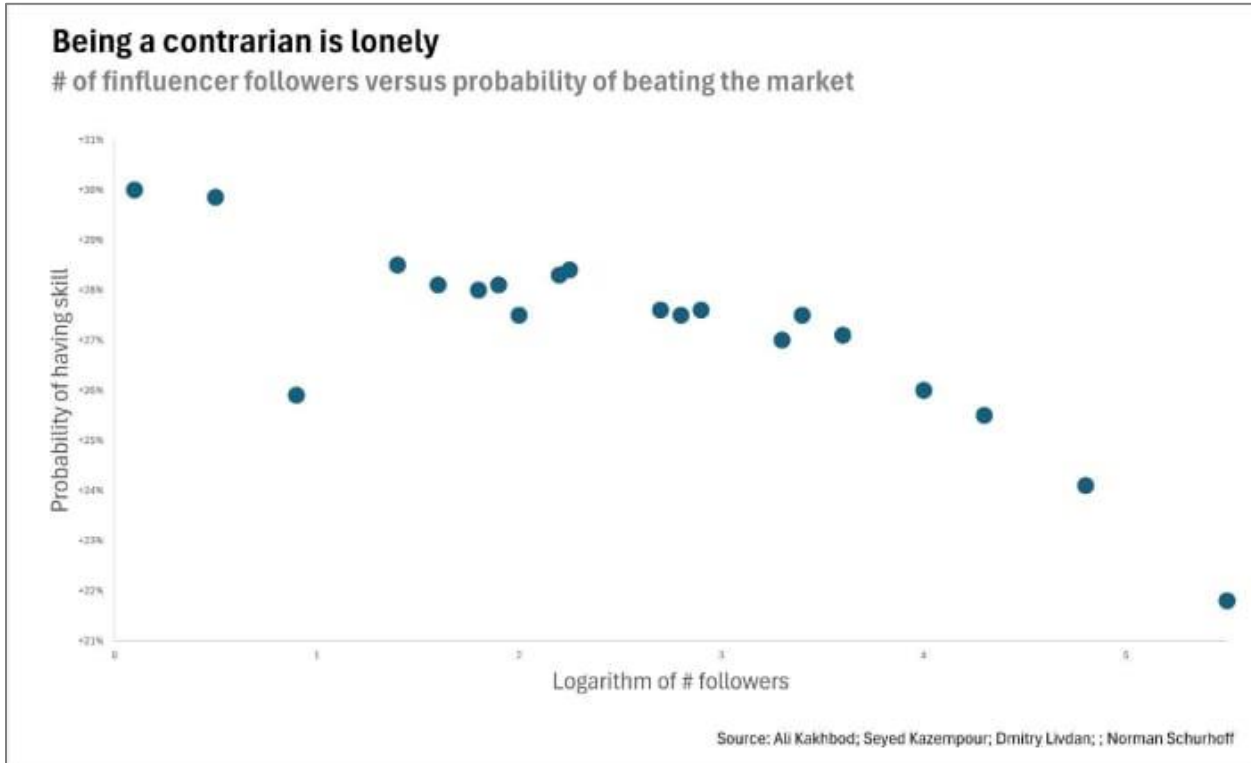
Rise in yields since the Fed rate cut is within 5-10bps of the point where stocks tend to get concerned.



The new era of shadow banking – Private Credit has ballooned over the last 20 years.



An inverse, linear relationship between a fin-fluencer's follower count and beating the market.



Source: Mark Hulbert

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.