Market Outlook

By Mark T Dodson, CFA

Is MZM Growth signaling the end of the Covid-Stimulus spend down?

Market Risk Index climbed to 85.1%, above the 75% level that denotes markets with high drawdown risk but shy of the 90% level that marked the end of the previous two bull markets. Both Monetary Conditions and Psychology worsened.

Psychology moved back into the worst five percent of readings. It's a given that extreme readings in sentiment (and valuations) are becoming easier to dismiss because they have been a hallmark of the post-COVID investment era. The lack of repercussions for speculative excess provides more fuel for animal spirits – investors have grown comfortable with the government-funded speculation era. Taking excessive risk feels riskless.

Case in point - futures positioning in US Equities shot up to another all-time high. Leveraged ETF asset exposure also increased and is within three percent of 2021's frothy extremes. The Surveys category has edged back toward Euphoria after a brief reprieve. Individual Investor allocations to equities climbed to the highest level since 2021, and the Consumer Confidence survey release for May showed consumers over the last three months have never been more optimistic that stock prices are headed higher. Anecdotally, we have seen the pictures circling this week of Nvidia CEO, Jensen Huang, signing female undergarments like he's a rock star. There are lead singers, famous guitar players, and then there are nerds whose stock price adds a trillion dollars to its market cap in six weeks. This image was better than a bull on the cover of Barron's as a picture that captures the speculative moment.

Breadth is also beginning to worsen visibly. This week's highs in the most widely followed cap-weighted US indices are the loneliest of the bull market. Less than half the S&P 500 stocks traded above their 50-day moving averages the day the S&P 500 broke to a new all-time high. The NASDAQ is more obscene with more new lows than highs, and our NASDAQ Overbought/Oversold indicator gave a negative reading while the NASDAQ Composite was hitting new highs on NVDA strength.

The Monetary Composite risk score has rapidly increased to a neutral score, now just shy of the 50th percentile. Monetary Aggregates and Velocity categories are softening. MZM growth for the month ending in May turned positive for the first time since October 2022. (The

Market Risk Index

Rec Allocation 25% Underweight

85.1%

Category Percentiles

Psychology - P6: 96.5%

Monetary - M3: 46.8%

Valuation - Extremely Overvalued: 99.5%

Trend: 36.1%

Largest Psychology Influences

Leveraged Investments	Negative
Option Activity	Negative
Surveys	Negative
Consumer Confidence	Negative

Largest Monetary Influences

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

Valuation

7-10 Year Equity Return Forecast	0.1%
10Yr US Treasury Yield	4.5%

Market Trends

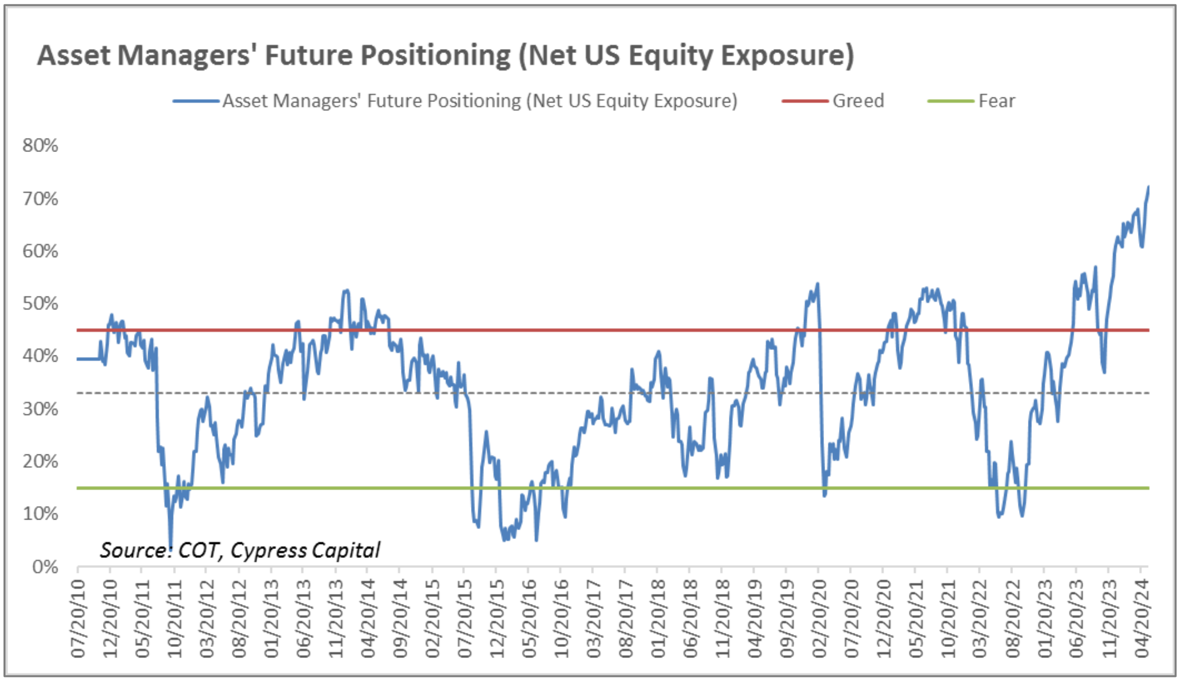
US Equities	Bullish Investment
Intl Equities	Bullish Investment
REITs	Bearish Trade
Broad Commodities	Bullish Investment

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.

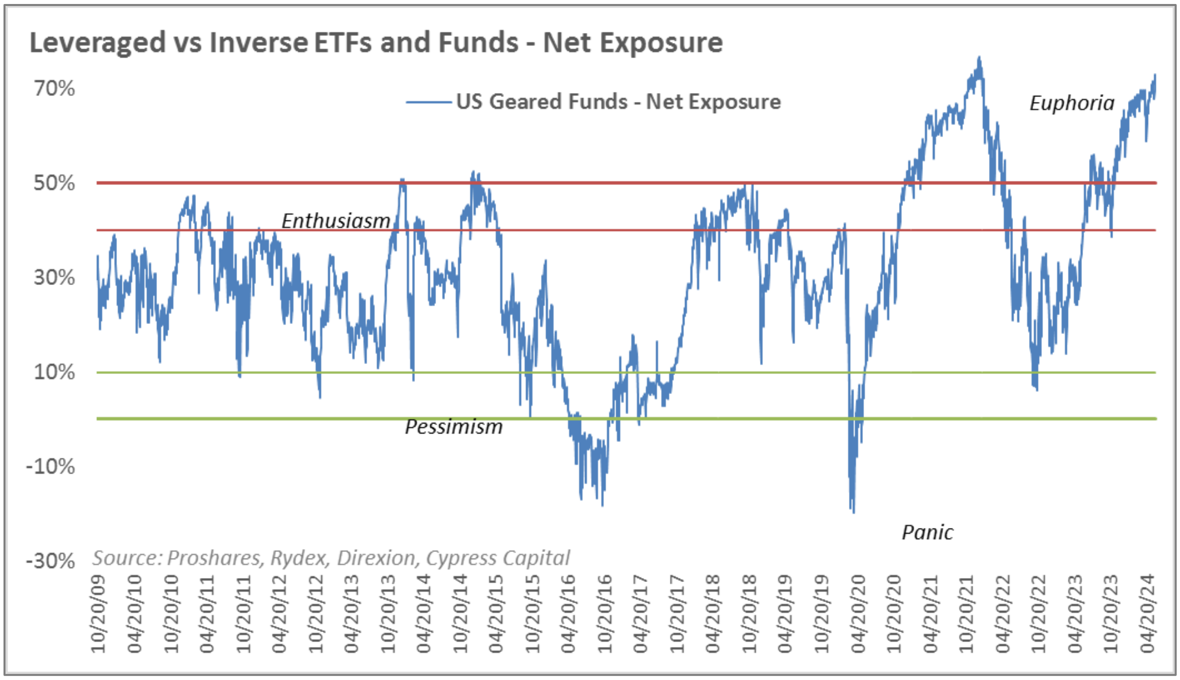
Federal Reserve stopped publishing MZM figures in 2021, but we continue calculating it internally.) Is that a sign that liquidity is increasing and financial conditions are easing further? No – it's the opposite. The Fed isn't adding liquidity into the economy; bank lending has been soft; consumers appear to have spent down excess COVID stimulus; and even the rate of change on the Federal deficit has turned negative. Absent those signposts of incrementally easier money, it means Households wanted to hold more of their assets in cash, not less. It is the first sign of belt-tightening by Households in the economy since the bull market began – nascent signs that financial conditions might be starting to tighten.

Charts of the Week

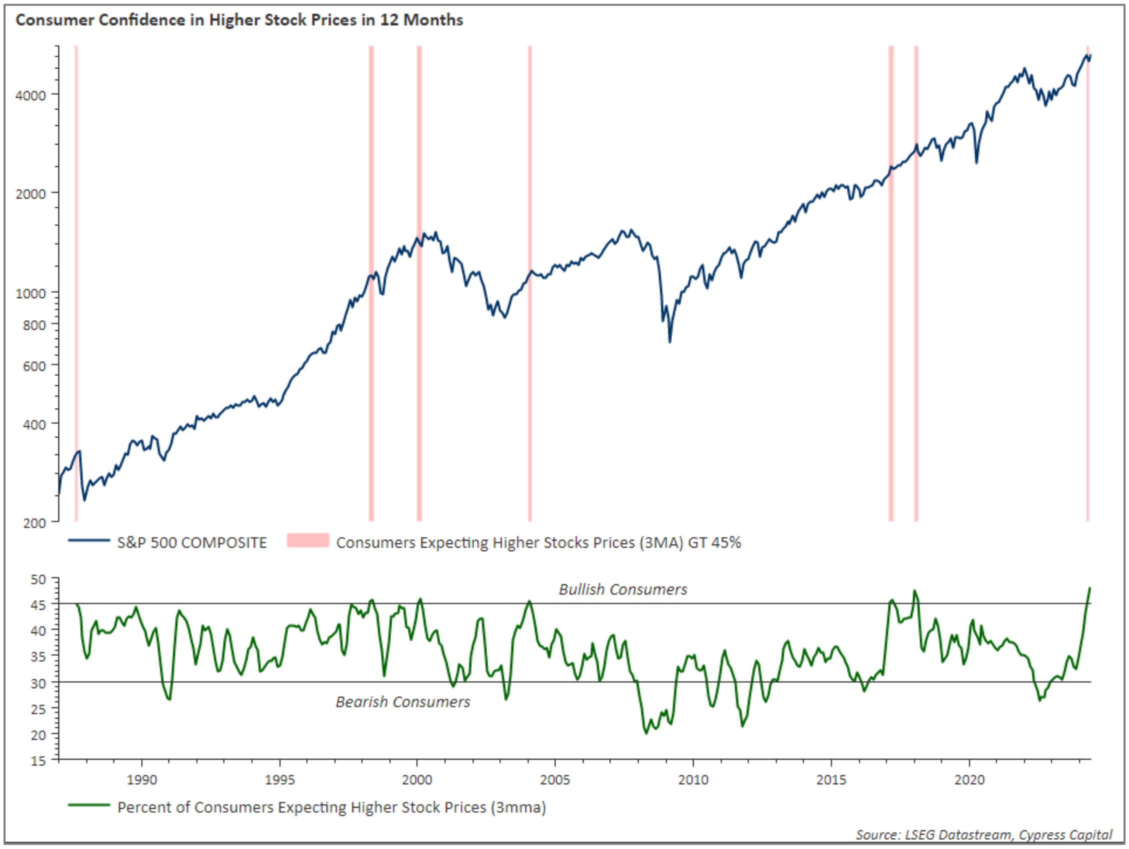
Asset Managers' Futures Positioning shoots even higher into record long exposure.



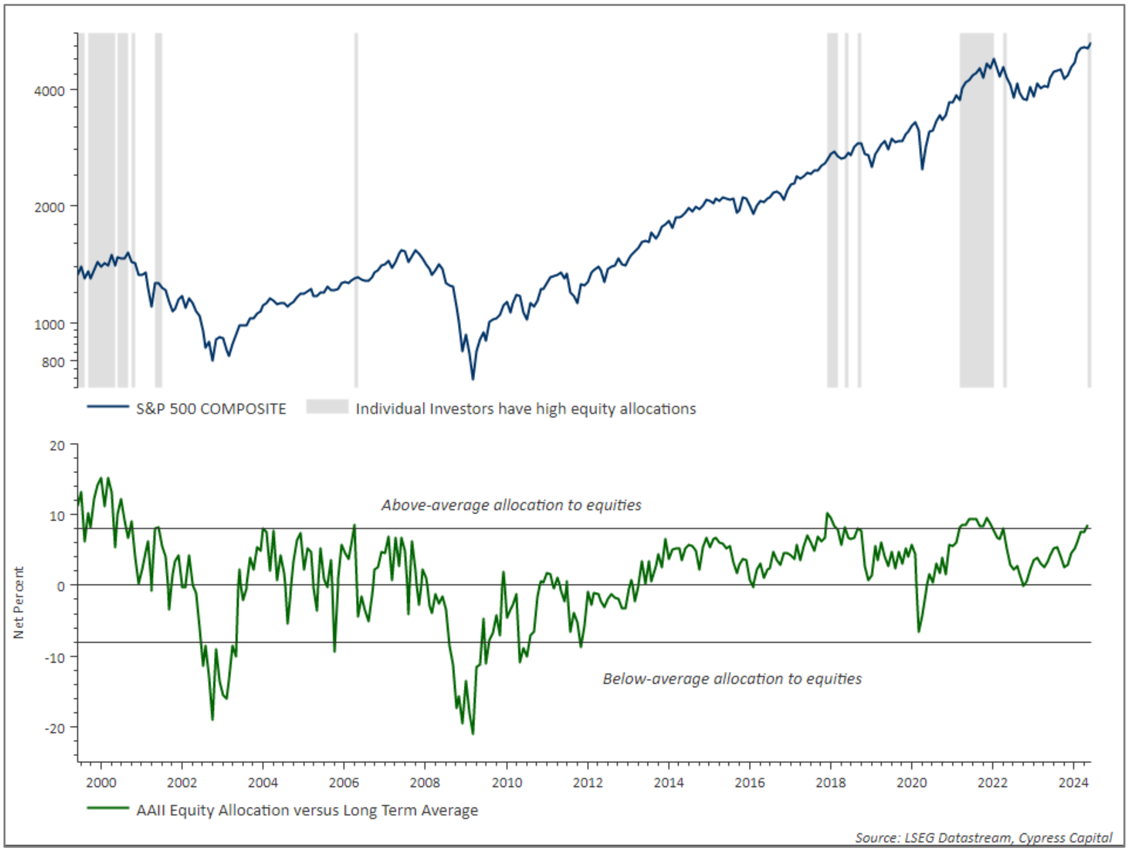
Investor Net Exposure using Leveraged ETF assets moved within 3% of the 2021 peak.



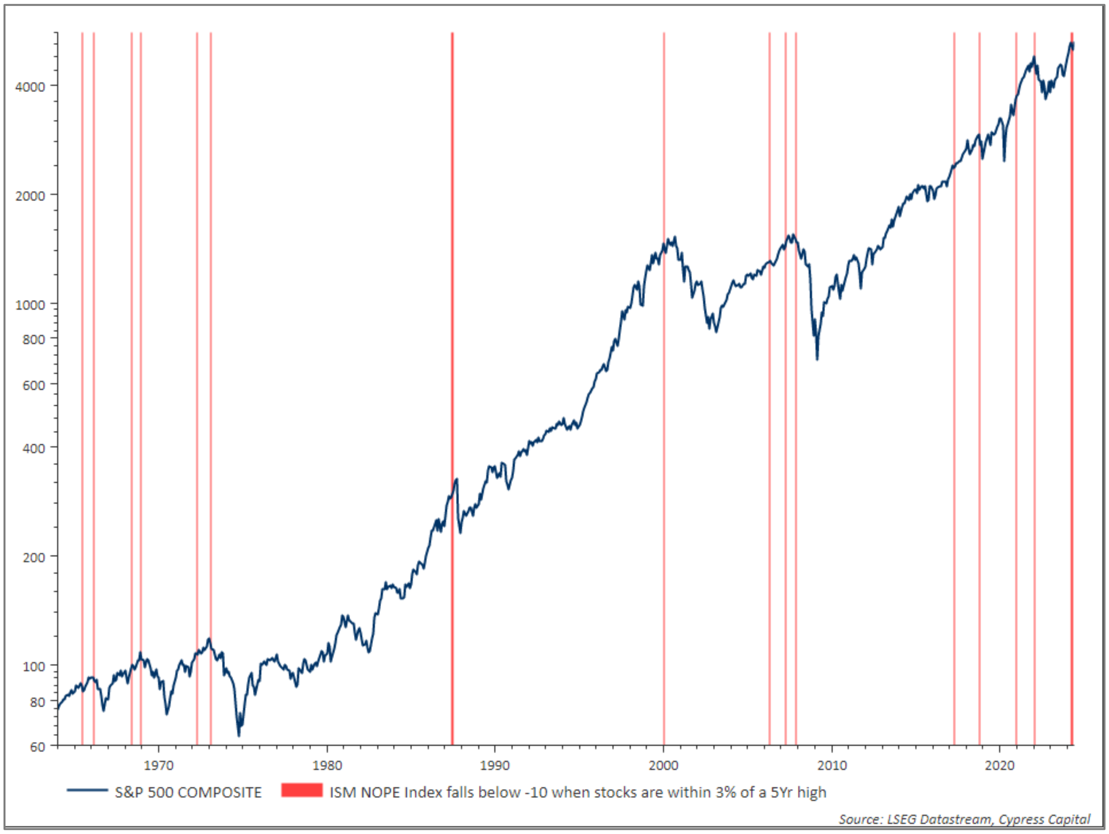
Record number of Consumers expect higher stock prices.



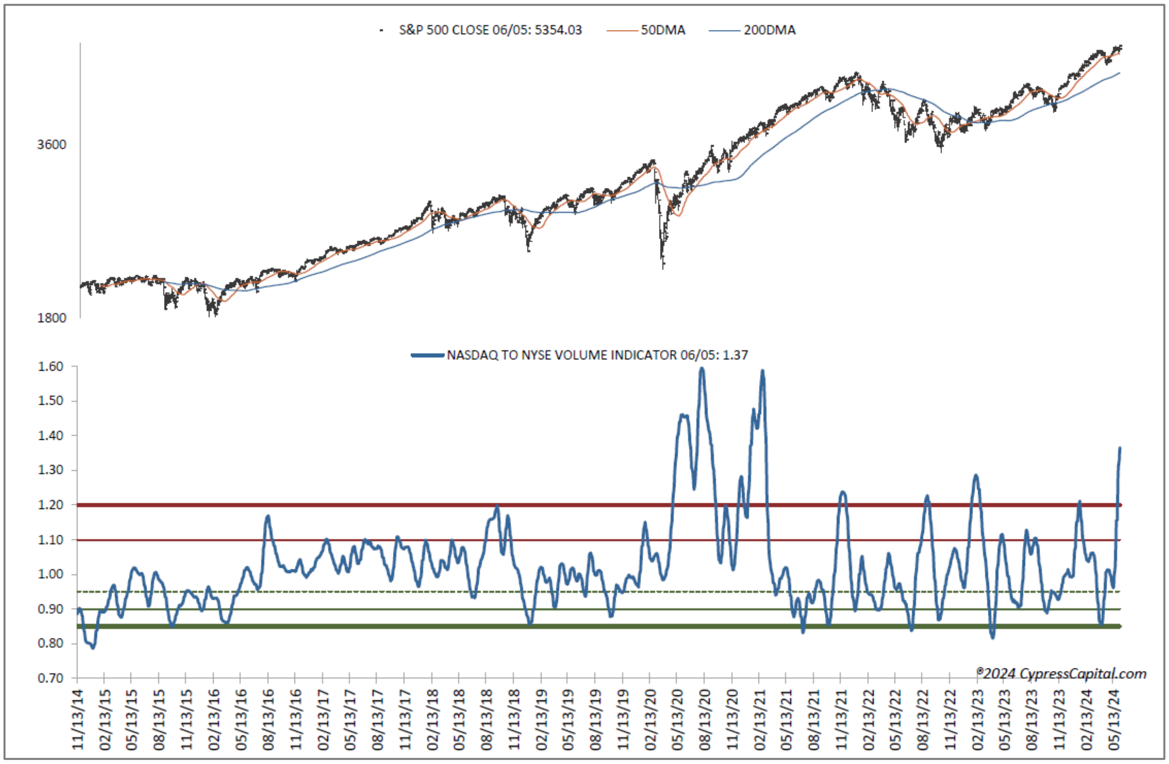
AAII Allocation Survey: Individual Investors are overweighting equities like they did in 2021.



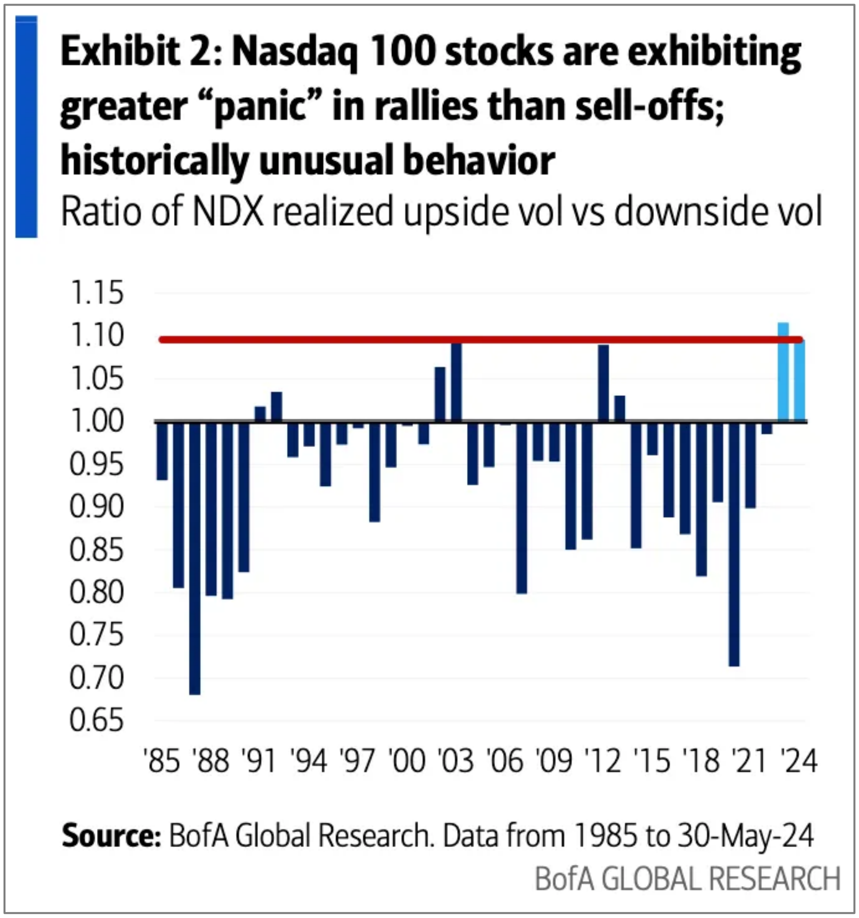
All the times that Leuthold Group's ISM NOPE Index has fallen under -10 with stocks at new highs.
We did a stagflationary version of ISM indices after last month's reading, but we like their NOPE Index better. It takes the New Orders Index (currently contracting) and subtracts the Prices Index (currently expanding).



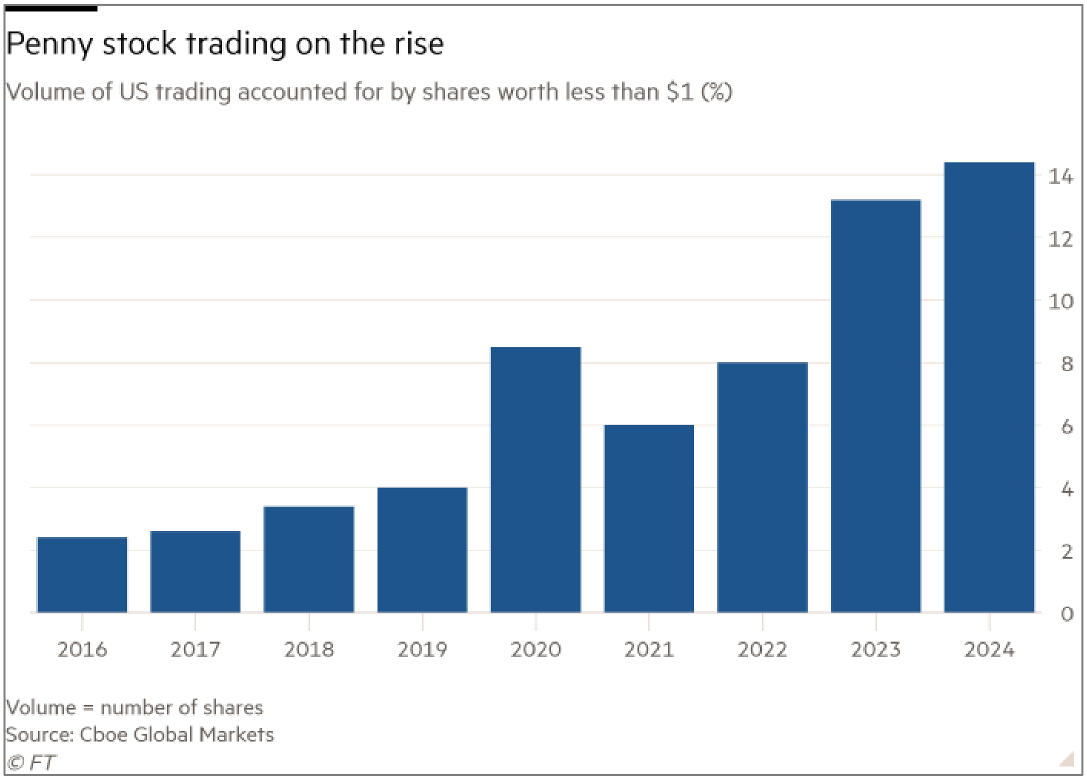
NASDAQ to NYSE Volume Indicator shoots to the highest level since the SPAC bubble in 2021.
Nvidia is almost single-handedly driving this.



Panicked FOMO buyers - upside vol is higher than downside vol.

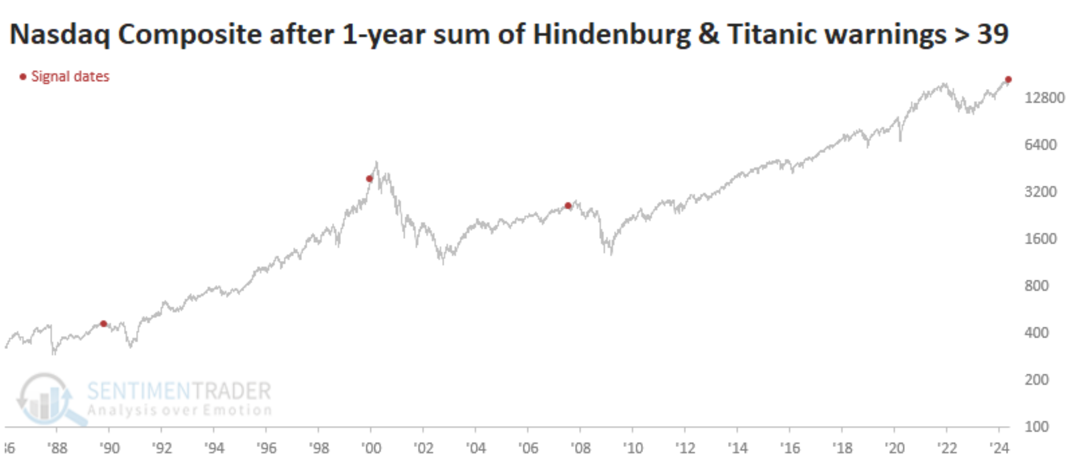


Record Penny stock volume suggests speculative froth is still rampant.



History of clustered Hindenburg and Titanic Warnings on the NASDAQ

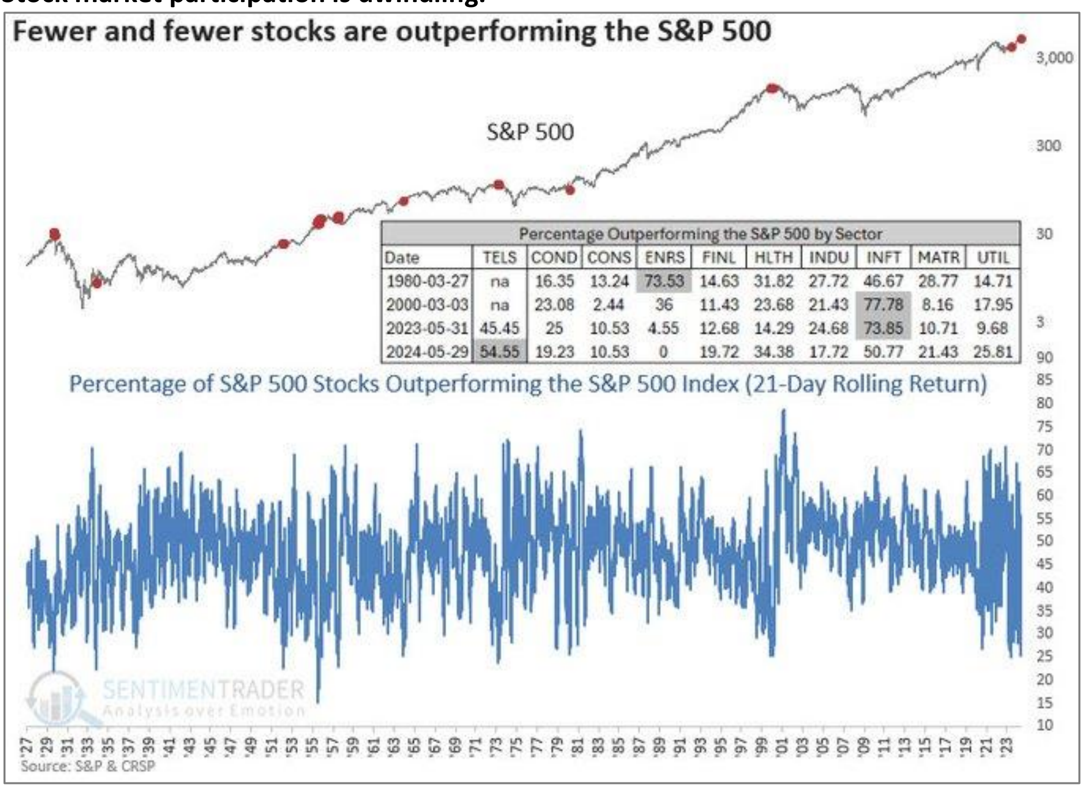
We showed a different version of this a couple of weeks ago, with clusters of combined warnings.



Dates of 3 Signals	1 Week Later (%)	2 Weeks Later (%)	1 Month Later (%)	2 Months Later (%)	3 Months Later (%)	6 Months Later (%)	12 Months Later (%)
1989-10-16	1.4	-2.1	-1.5	-2.9	-4.5	-5.5	-28.5
1999-12-21	3.3	-0.9	8.3	12.0	24.4	3.9	-35.8
2007-07-26	-0.9	-1.6	-0.9	3.2	6.7	-10.5	-11.1
2024-05-24							
Mean	**1.3**	**-1.5**	**2.0**	**4.1**	**8.9**	**-4.0**	**-25.1**
Median	**1.4**	**-1.6**	**-0.9**	**3.2**	**6.7**	**-5.5**	**-28.5**
% Positive	**67%**	**0%**	**33%**	**67%**	**67%**	**33%**	**0%**
Avg Max Loss	-0.8	-2.1	-4.4	-4.4	-5.4	-13.9	-27.2
Avg Max Gain	1.8	2.8	3.6	7.2	13.1	13.7	13.7
Z-Score	0.9	-5.7	-0.5	0.4	0.5	-2.5	-5.3

© SENTIMENTRADER Numbers are % return after signal; Risk = avg max loss; Reward = avg max gain; Z-Score +/- 2 suggests significance.

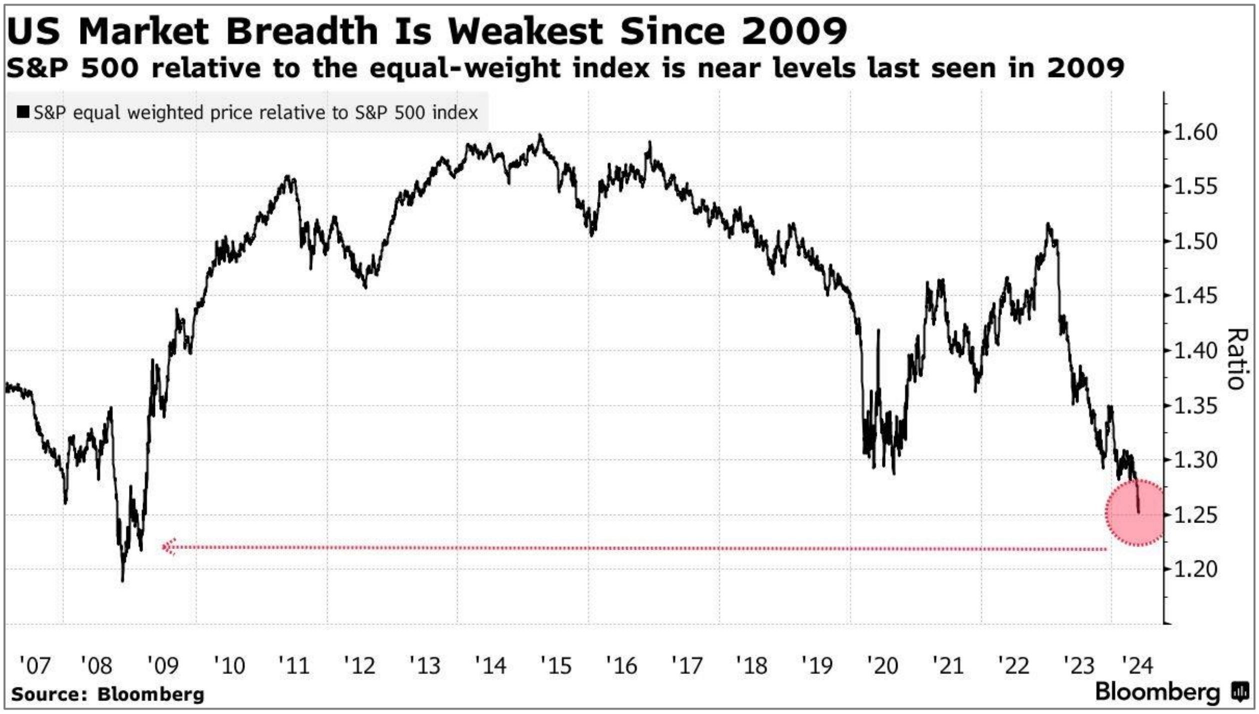
Stock market participation is dwindling.



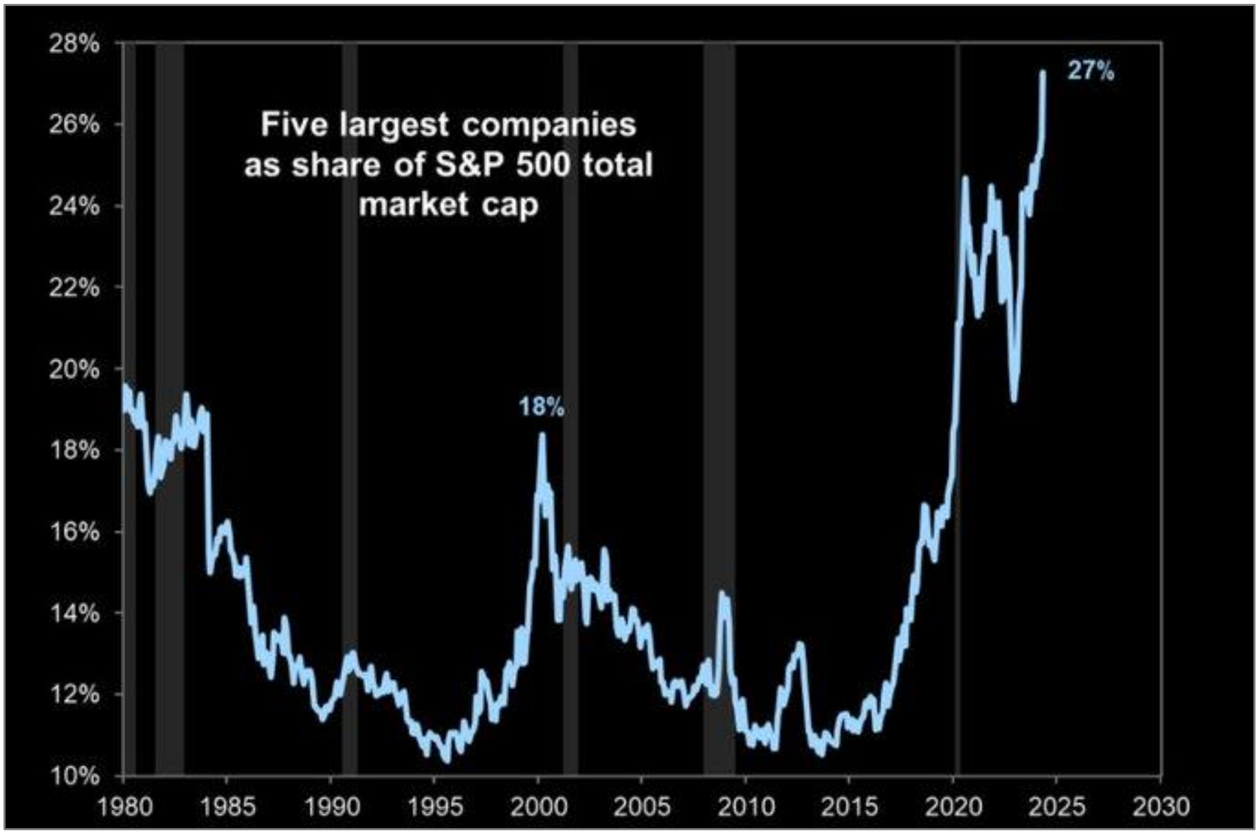
Percentage Outperforming the S&P 500 by Sector

Date	TELS	COND	CONS	ENRS	FINL	HLTH	INDU	INFT	MATR	UTIL
1980-03-27	na	16.35	13.24	73.53	14.63	31.82	27.72	46.67	28.77	14.71
2000-03-03	na	23.08	2.44	36	11.43	23.68	21.43	77.78	8.16	17.95
2023-05-31	45.45	25	10.53	4.55	12.68	14.29	24.68	73.85	10.71	9.68
2024-05-29	54.55	19.23	10.53	0	19.72	34.38	17.72	50.77	21.43	25.81

The average stock is not keeping up with the market.



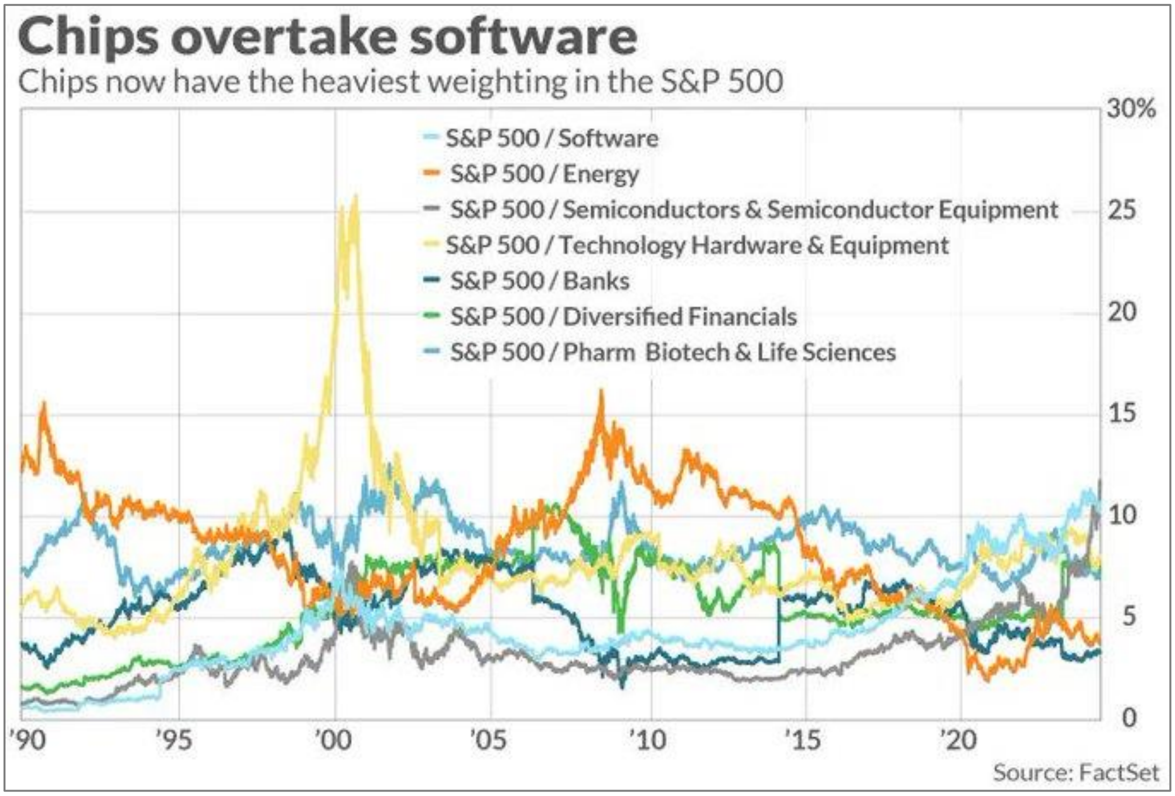
Stock Market Concentration blows past the Covid record.



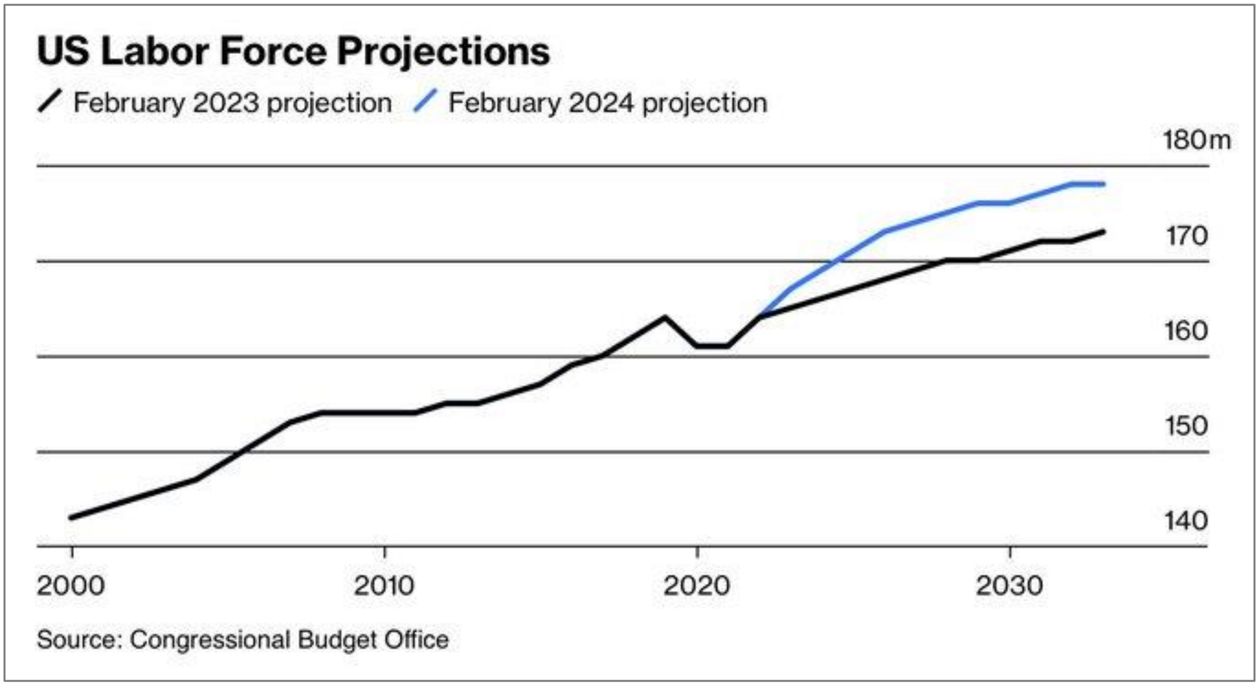
Source: Michael Arouet

Technology weight has reached a record high, surpassing the dot-com era bubble.

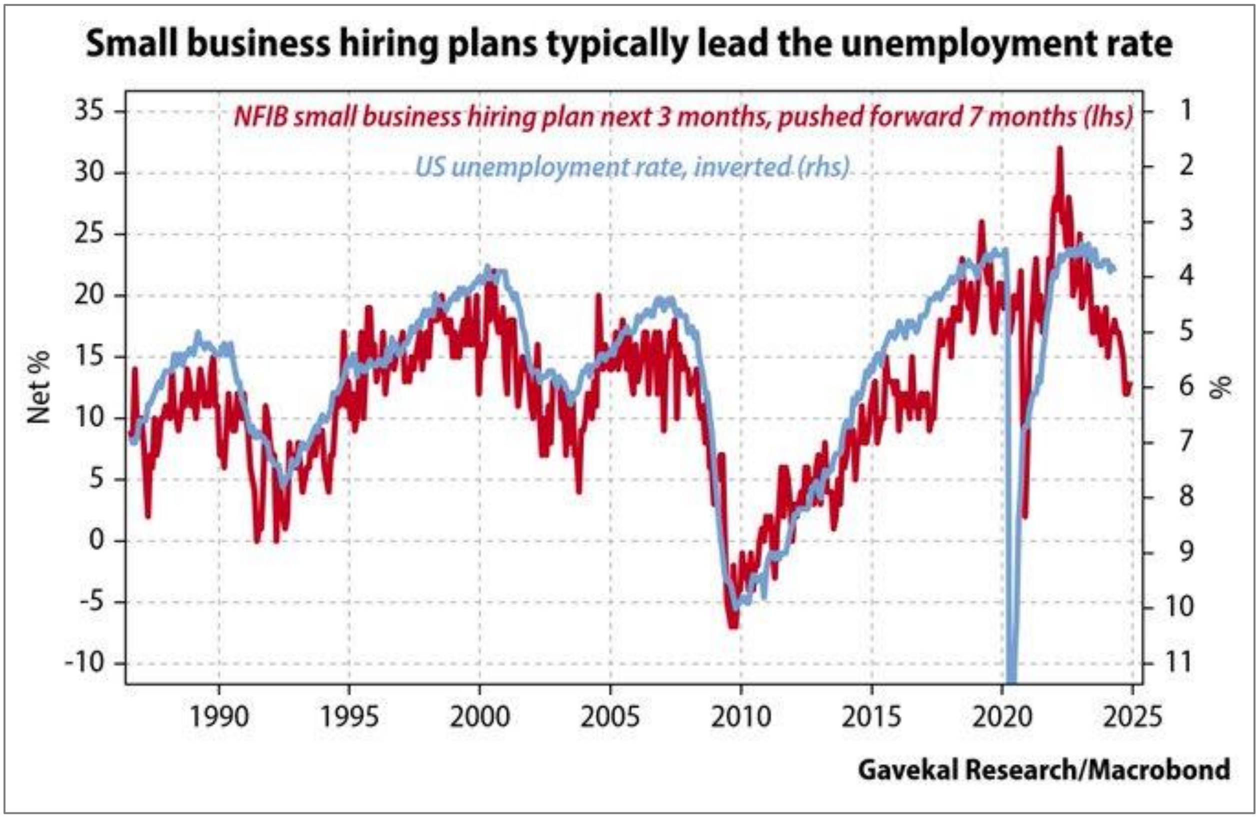
Semiconductors overtake Software for the heaviest industry weighting in the S&P 500.



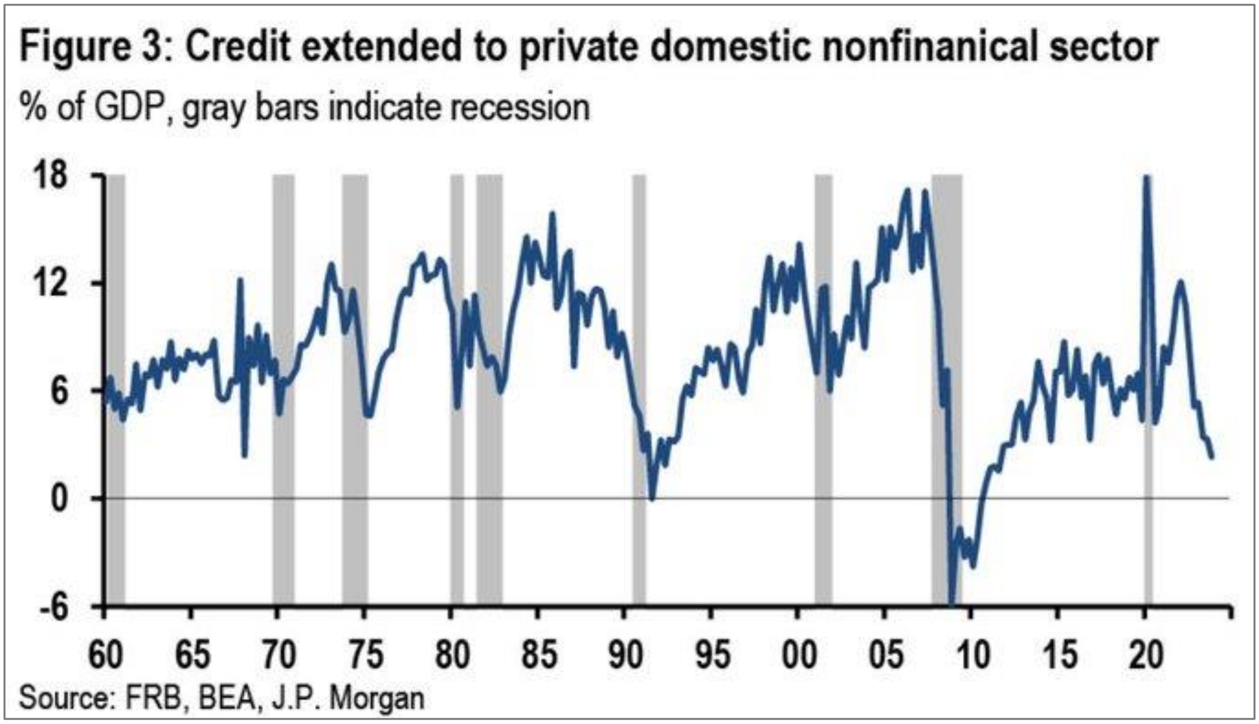
Un-officially recorded immigration (over 1.2mm people) helped growth and inflation in 2023.



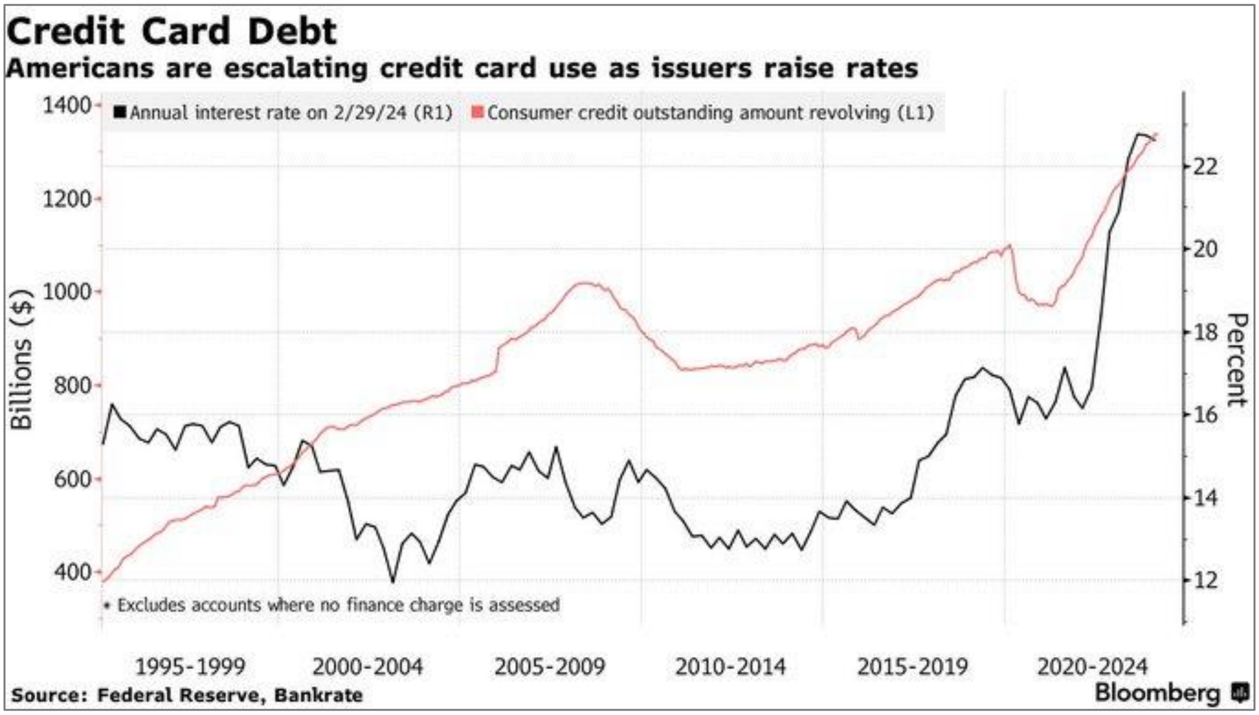
Hiring Plans imply higher unemployment over the next seven months.



Credit growth continues to soften.

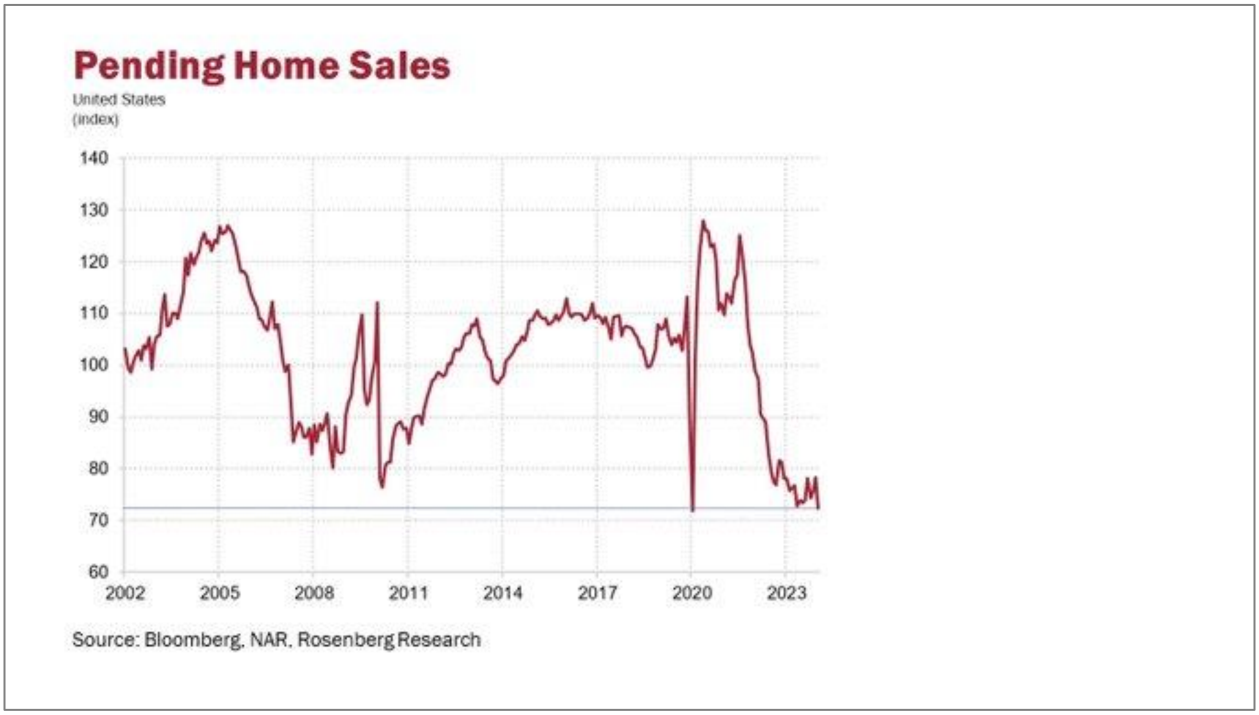


Not the case with credit cart debt, which is expanding as households feel the pinch of inflation.

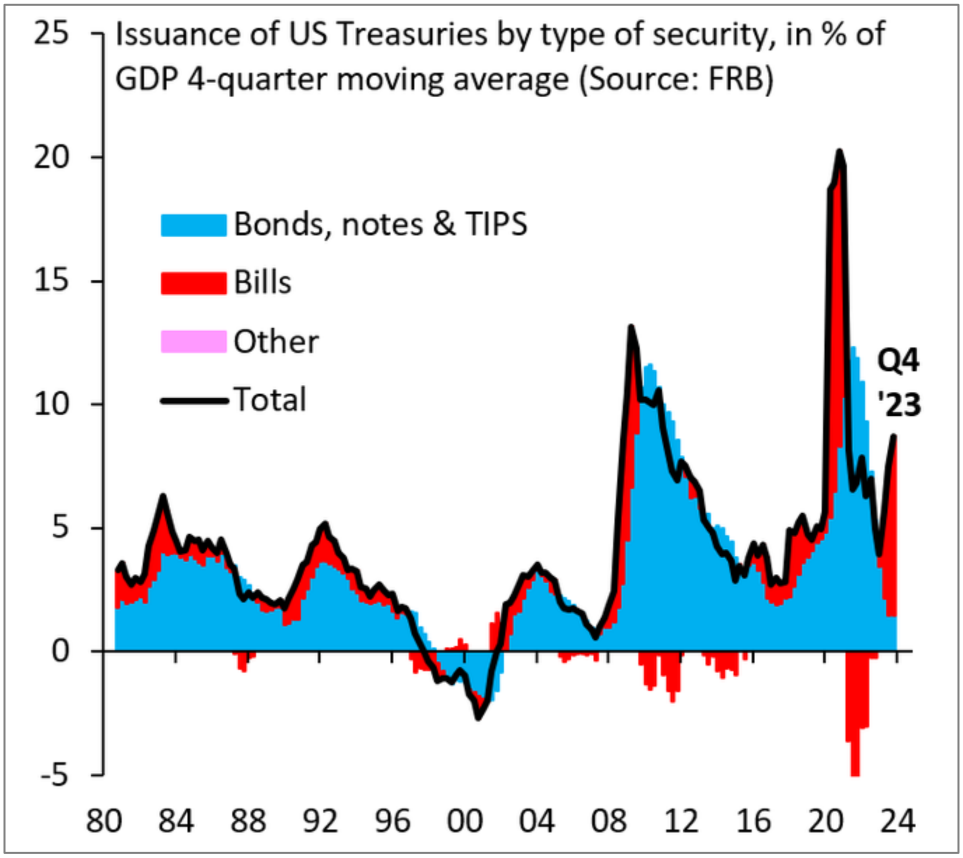


Chicago PMI looks recessionary.

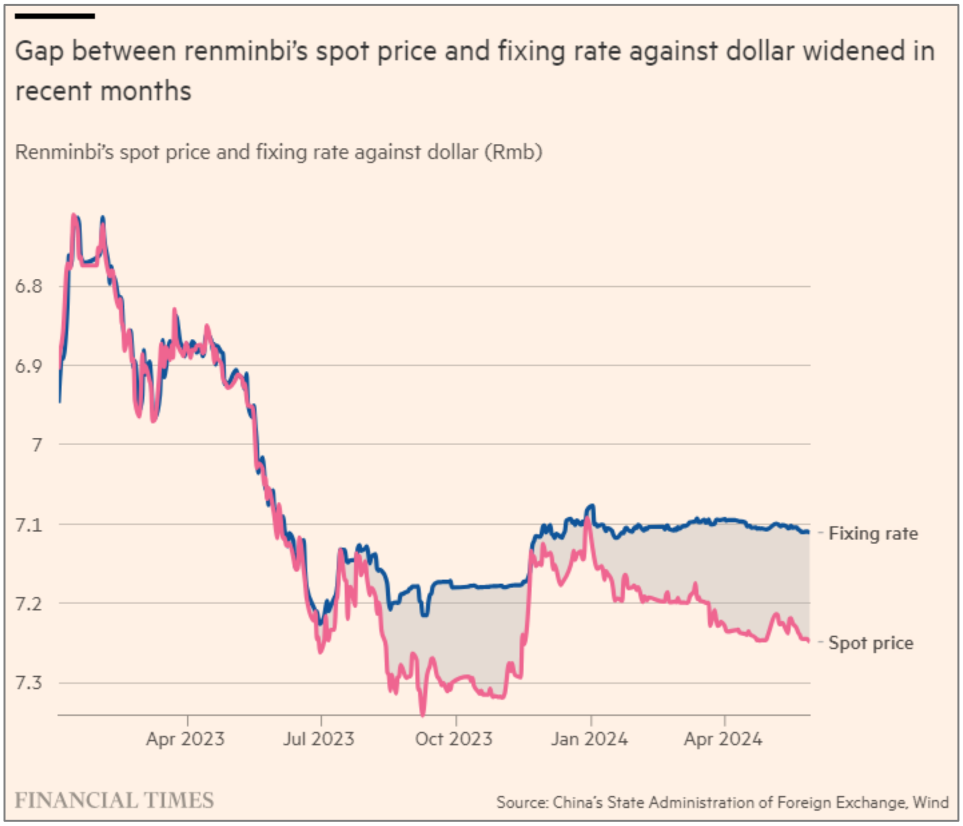
So do Pending Home Sales.



The Federal Government is funding a boom with an approach typically reserved for financial crises.

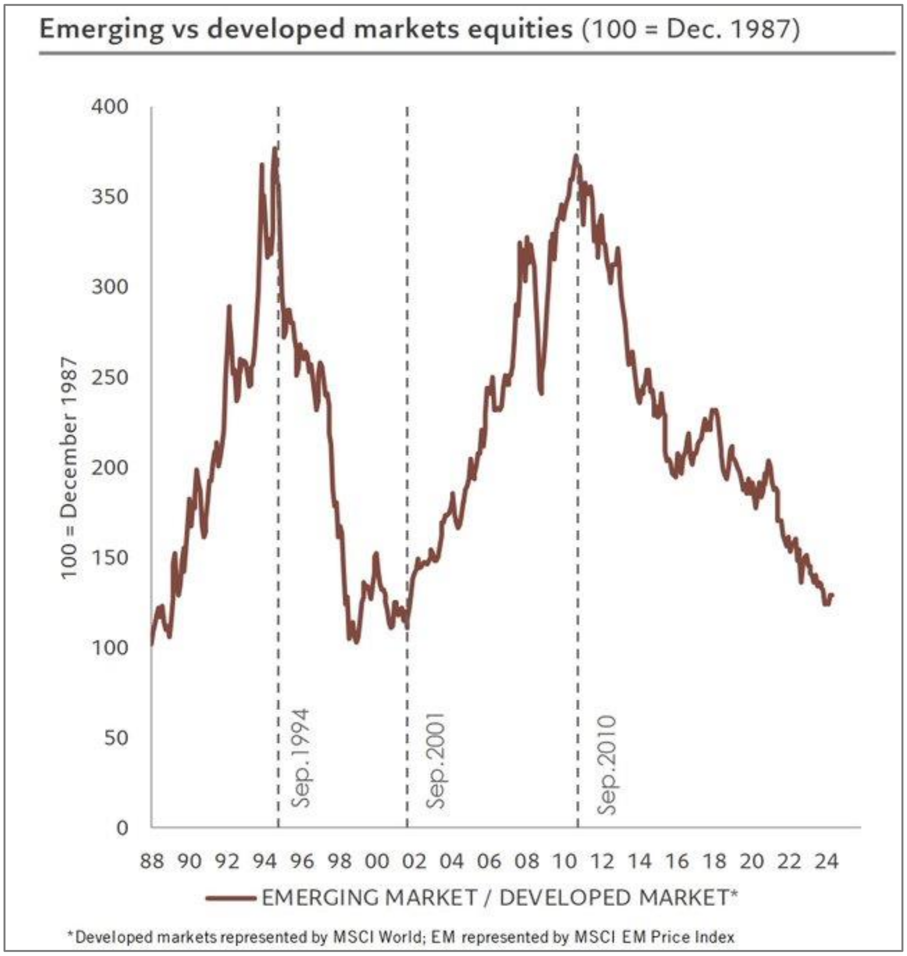


Traders are betting heavily on a revaluation of China's currency.

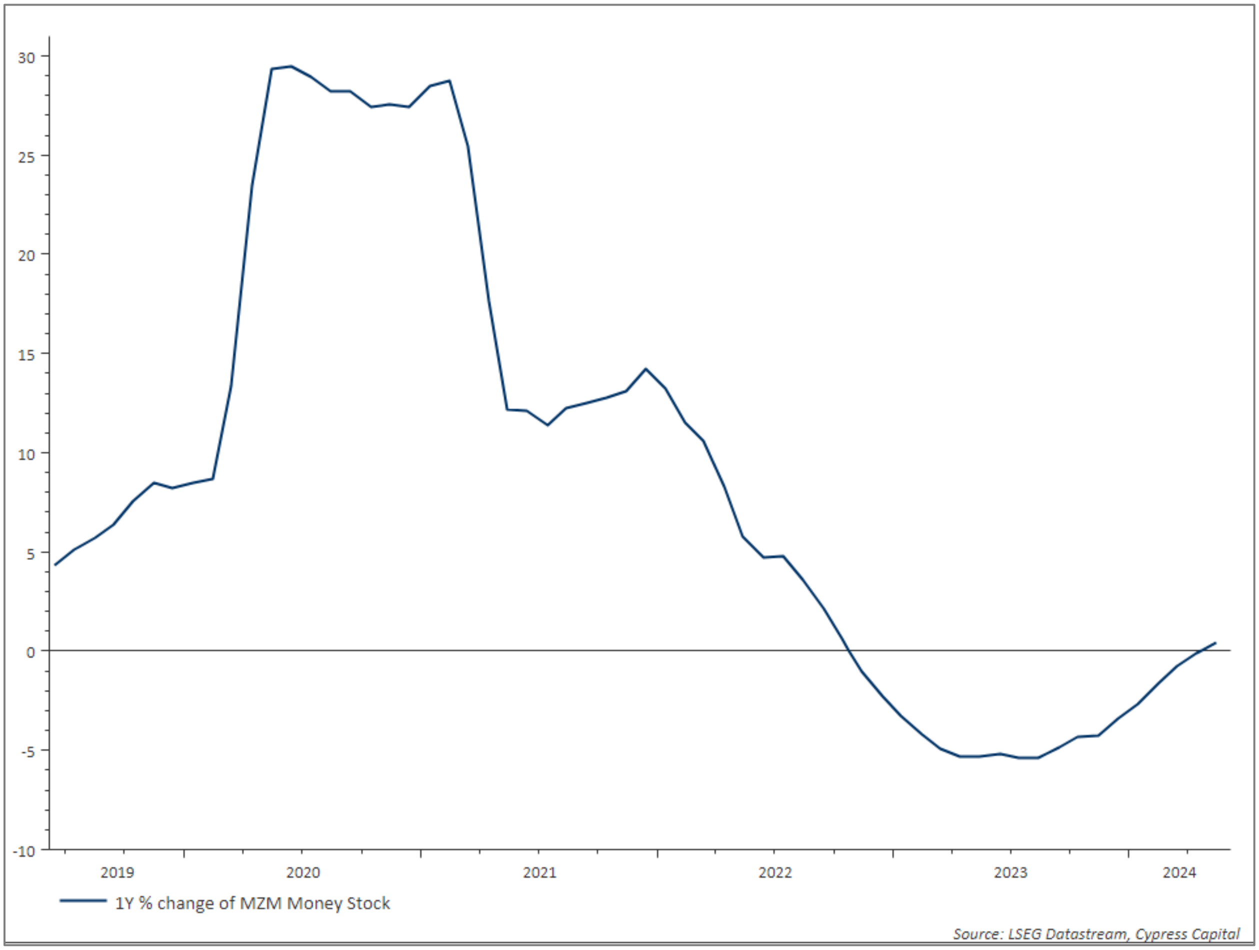


China's labor market cost advantage is gone.

The Emerging versus Developed Market Pendulum has swung to an extreme.



MZM Growth turns positive for the first time since the bull market began.



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.