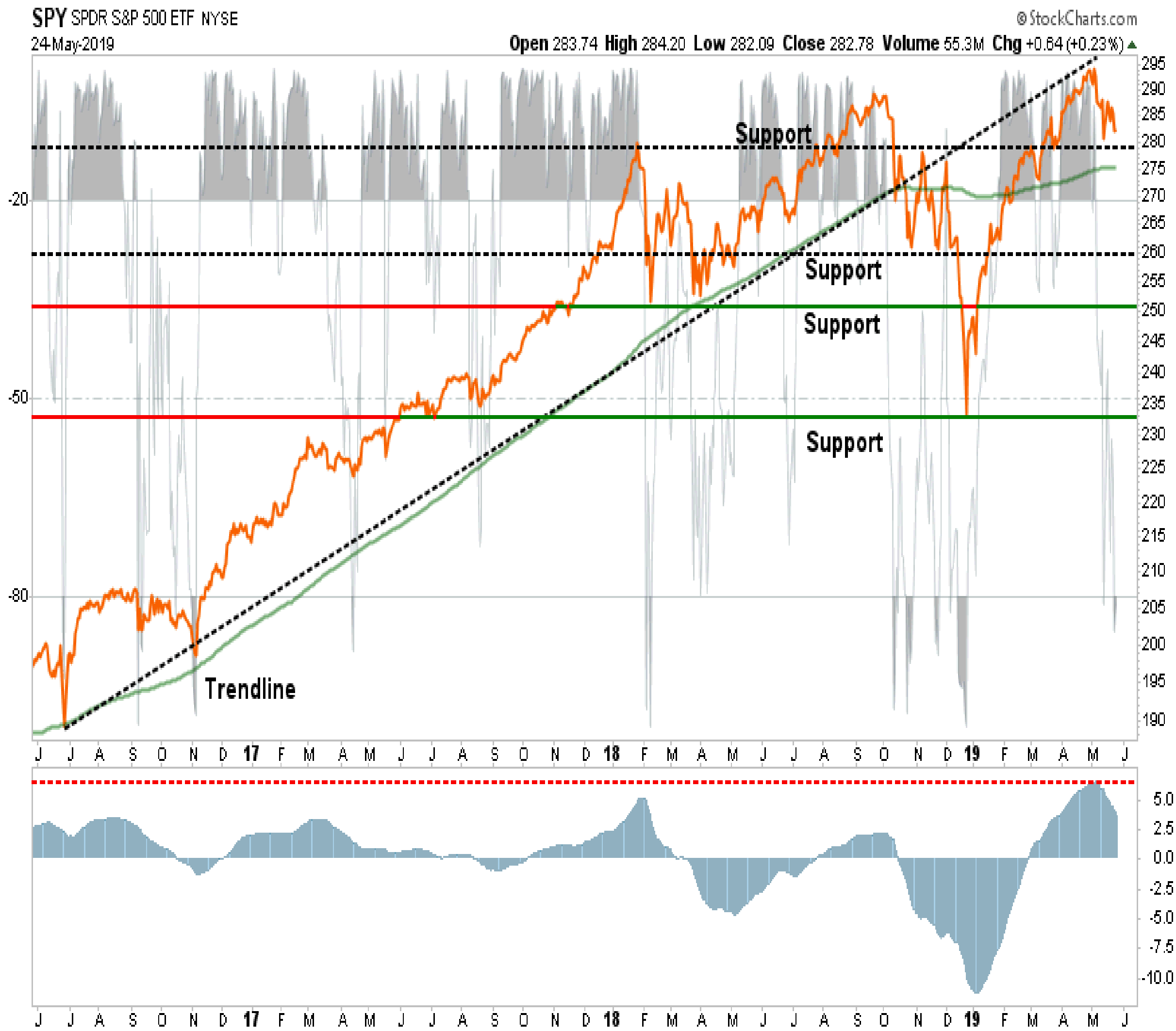
Since the markets were closed yesterday for *"Memorial Day,"* there isn't much for us to update technically from this past [weekend's missive.](#) However, I did provide an update yesterday for our **[RIAPRO subscribers](#)** ***(Try 30-days FREE)*** with respect to where the S&P 500 is currently trading and why we expect a short-term bounce. To wit:



- *As noted previously, SPY tested, and failed, at the bottom of the uptrend line from both the 2017 post-election bounce and the 2016 lows.*
- *SPY has now corrected the overbought condition and is testing support from the January highs with the 200-dma close below.*
- *The ?buy? signal in the lower panel was also massively extended, as noted several weeks ago, suggesting the reversal we have seen was coming as we warned then.*
- *The correction last week has set up a tradeable opportunity into the end of the month.*
- *Short-Term Positioning:* ***Bullish***
    - *Last Week: Take profits and hold.*
    - *This Week: Add 1/2 position to portfolios with a target of $290*
    - *Stop-loss remains at $275*
- *Long-Term Positioning:* ***Neutral***

With that said, what we are expecting is a short-term rally within the context of a market in the potential transition from *"bull" to "bear."* This is point I made in April of 2018 in [*"10-Reasons The Bull Market Ended In 2018."*]

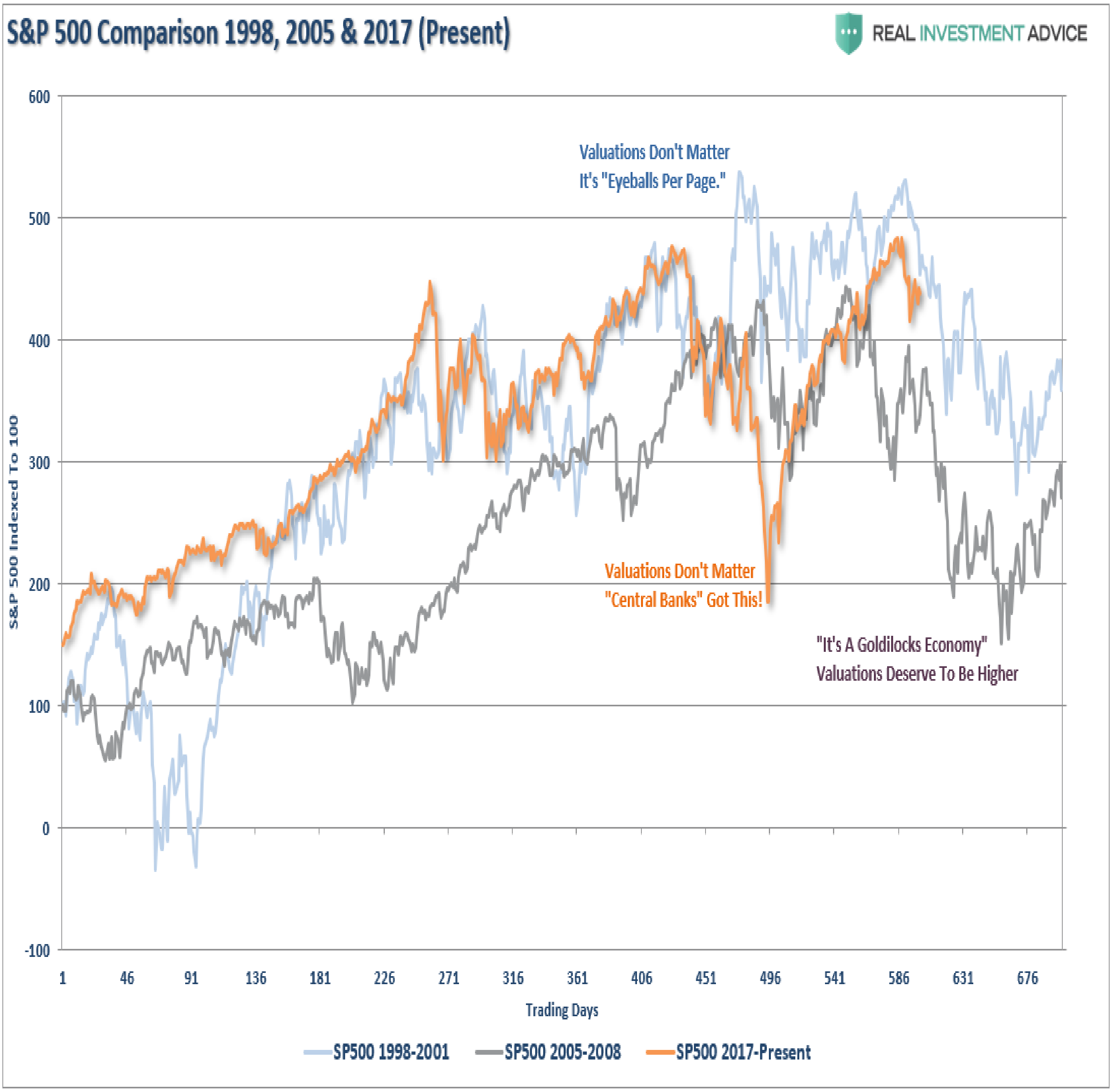
> *"There is a reasonably high possibility, the bull market that started in 2009 has ended. We may not know for a week, a month or even possibly a couple of quarters.* ***Topping processes in markets can take a very long time."***

Or, as my friend Doug Kass often quips:

> ***"Tops are processes. Bottoms are an event."***

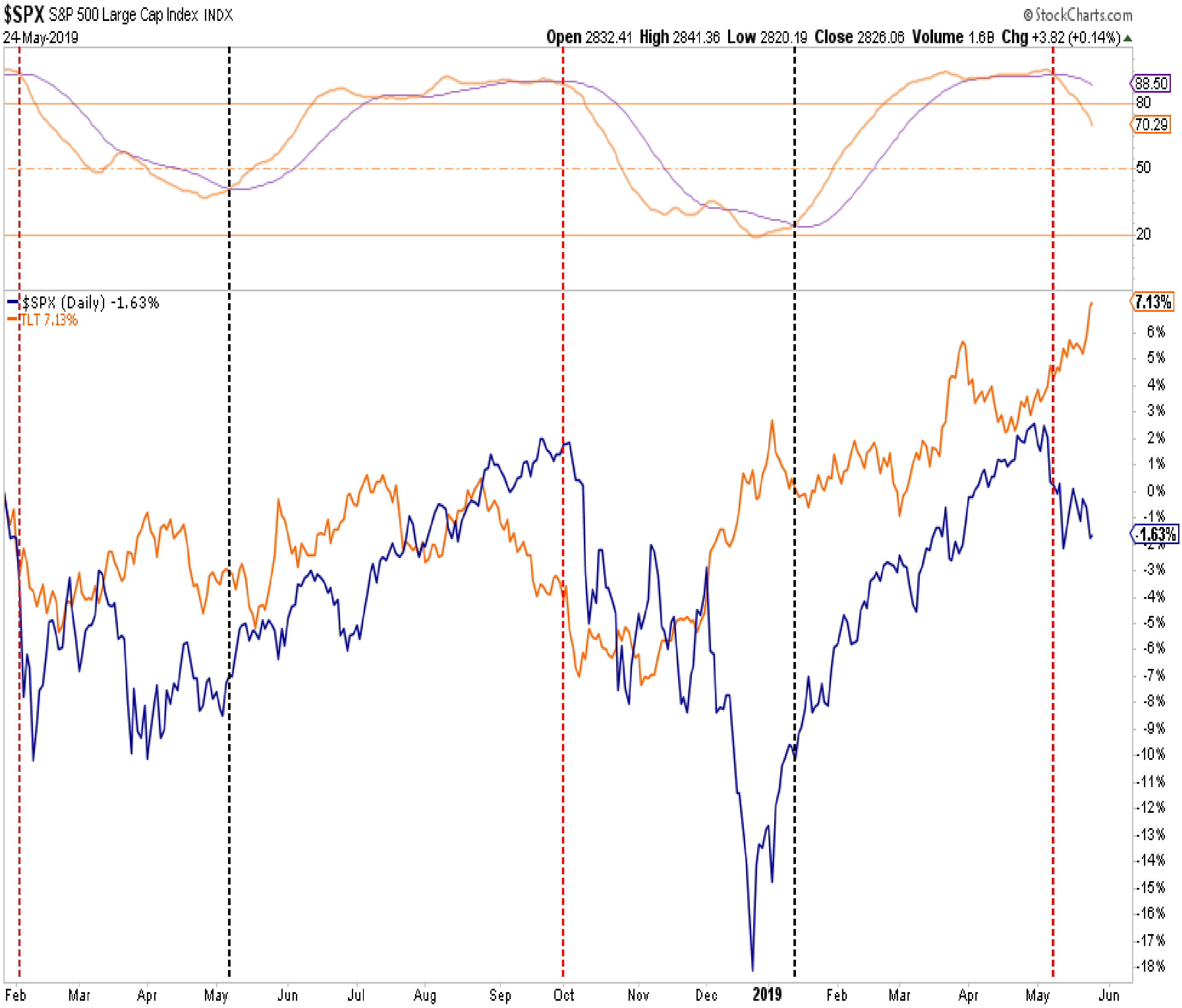
This is shown in the chart below which I explained this past weekend:

> *"Just one other thing, I don?t like market comparisons because no two market cycles are alike. However, price patterns are important because they represent the ?psychology of the herd.?* The chart below shows the market in the months leading up to the Dot.com crash, the Financial Crisis, and where we are currently."



> *"Again, no two market cycles are the same. The drivers which facilitate the bull run, and the catalyst which ends it, are ALWAYS different. **It is just investor behavior which is always the same."***

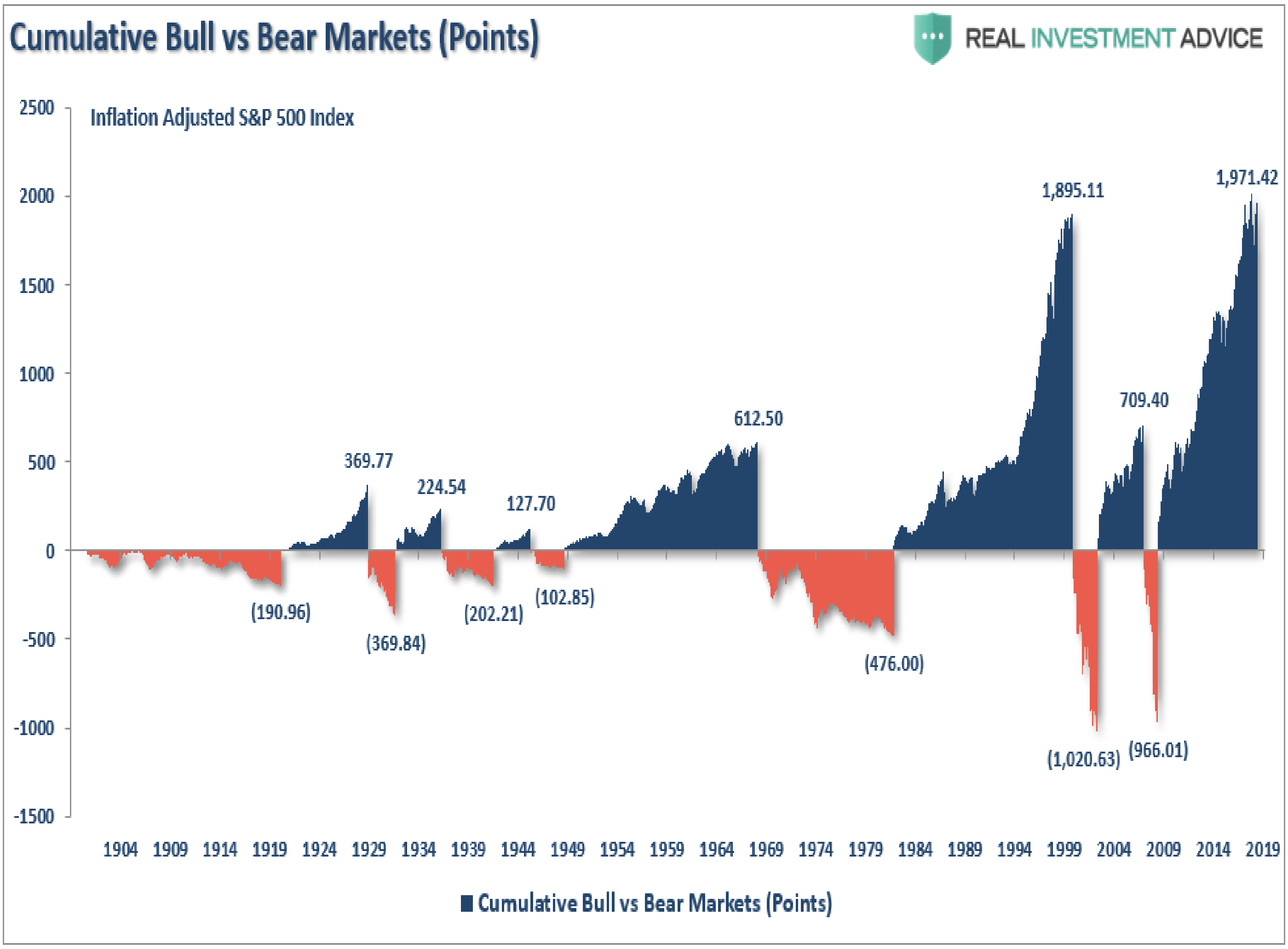
Importantly, the market has now registered its third sell signal since the January 2018 peak. I have overlaid the performance of bonds relative to the market to help you better understand why chasing equities isn't always the best solution to making money. *(This is specifically why we run risked managed 60/40 allocation models.)*



Buying Because I Have To. You Don?t.

> ***"So, why are you buying?"***

This is an interesting email I got last week given the comments above and last week's [*"7-Measures Suggest A Decade Of Low Returns."*](#) ***(Note:** We recently shifted exposure in our portfolios from more "offensive" to "defensive" by overweighting Healthcare, Utilities, and Real Estate while underweighting Technology, Discretionary, Materials, and Industrials. Also, we lengthened duration in our bond portfolios and eliminated emerging market exposure due to the "trade war.")* There is a difference between views of long-term fundamentally driven potential outcomes and short-term opportunities in the markets. As a portfolio manager, **we buy "opportunity" because we have to.** If we don?t, we suffer career risk, plain and simple. **However, you don?t have to.** If you are truly a long-term investor, you have to question the risk being undertaken to achieve further returns in the market. Think about it this way. **The markets have returned more than 300% since the 2009 lows in the longest bull market on record.** *Yes, it is still just one bull market.* Assuming that you were astute enough to buy the *?cherry picked?* low, and didn?t spend the bulk of the bull market rally simply getting back to even, **you would have accumulated years of excess returns towards meeting your retirement goals. If you went to cash now, the odds are EXTREMELY high that in the years ahead you will far outpace investors who remain invested.** Sure, they may get an edge on you in the short-term, and chastise you for *?missing out,?* but when the next *?mean reverting event?* occurs the **decline will destroy most, if not all, of the returns accumulated over the last decade.** *(That isn't a theoretical assumption. It's historical fact.)*



While we may indeed be shifting exposure and taking on some additional risk, we do so very cautiously. We continue to run an overweight position in cash and fixed income while also reducing exposure risk by shifting our allocations.

The ?Rothschild 80/20? Rule

When discussing portfolio management, it is often suggested that you can?t *?time the market.?* **That statement is correct.** You can not effectively, and repetitively, get *?in?* and *?out?* of the market on a timely fashion. I have never suggested that an investor should try and do this. However, [I HAVE discussed managing risk]() by adjusting market exposure at times when *?risk?* outweighs the potential for further *?reward.?*

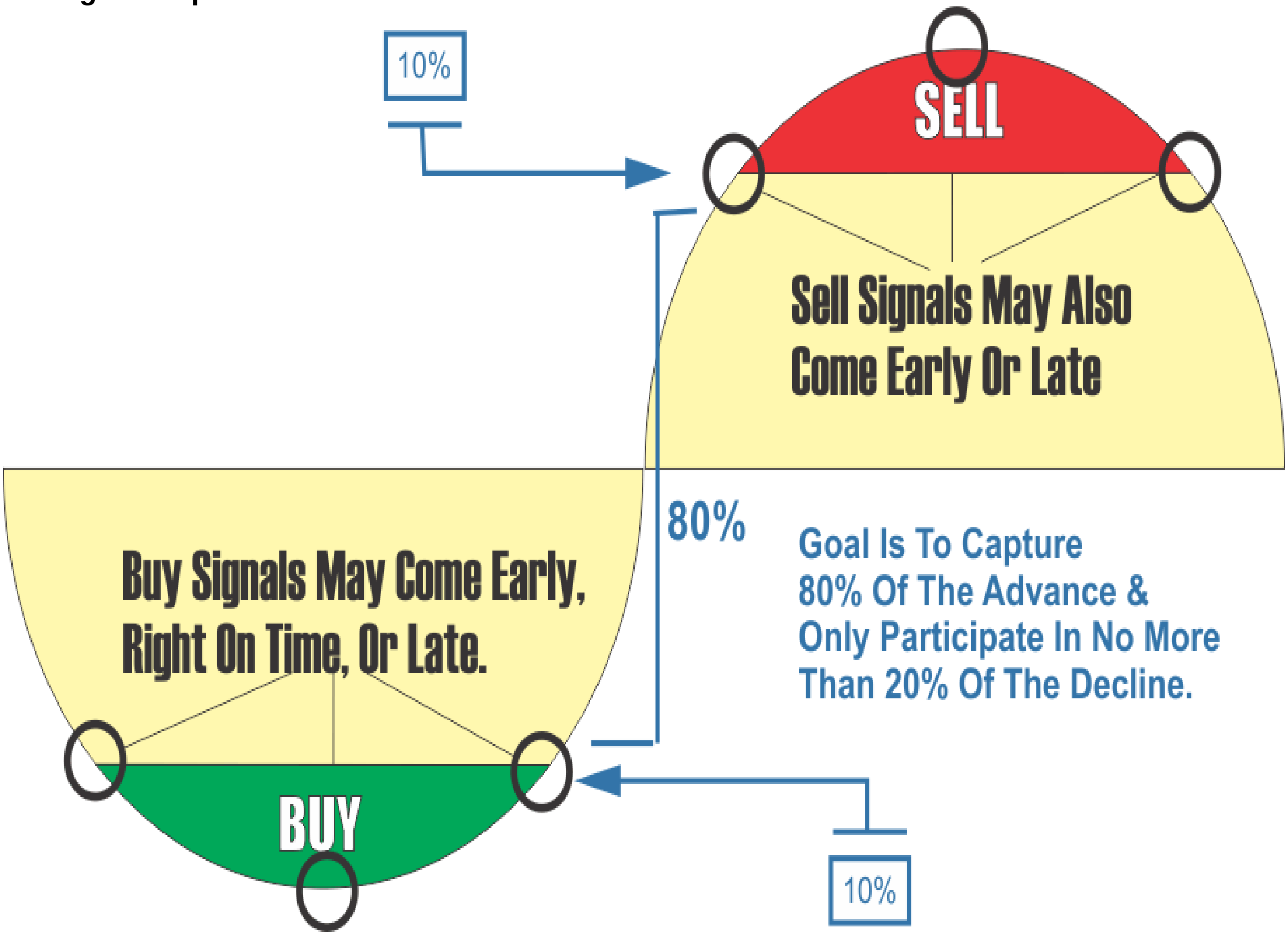
> ***?While I am often tagged as ?bearish? due to my analysis of economic and fundamental data for ?what it is? rather than ?what I hope it to be,? I am actually***

> ***neither bullish or bearish.*** *I follow a very simple set of rules which are the core of my portfolio management philosophy which focuses on capital preservation and long-term ?risk-adjusted? return.?*

As a long-term investor, I don?t need to worry about short-term rallies. I only need to worry about the direction of the overall market trends and focus on capturing the positive and avoiding the negative. As Baron Nathan Rothschild once quipped:

> ***?You can have the top 20% and the bottom 20%, I will take the 80% in the middle.?***

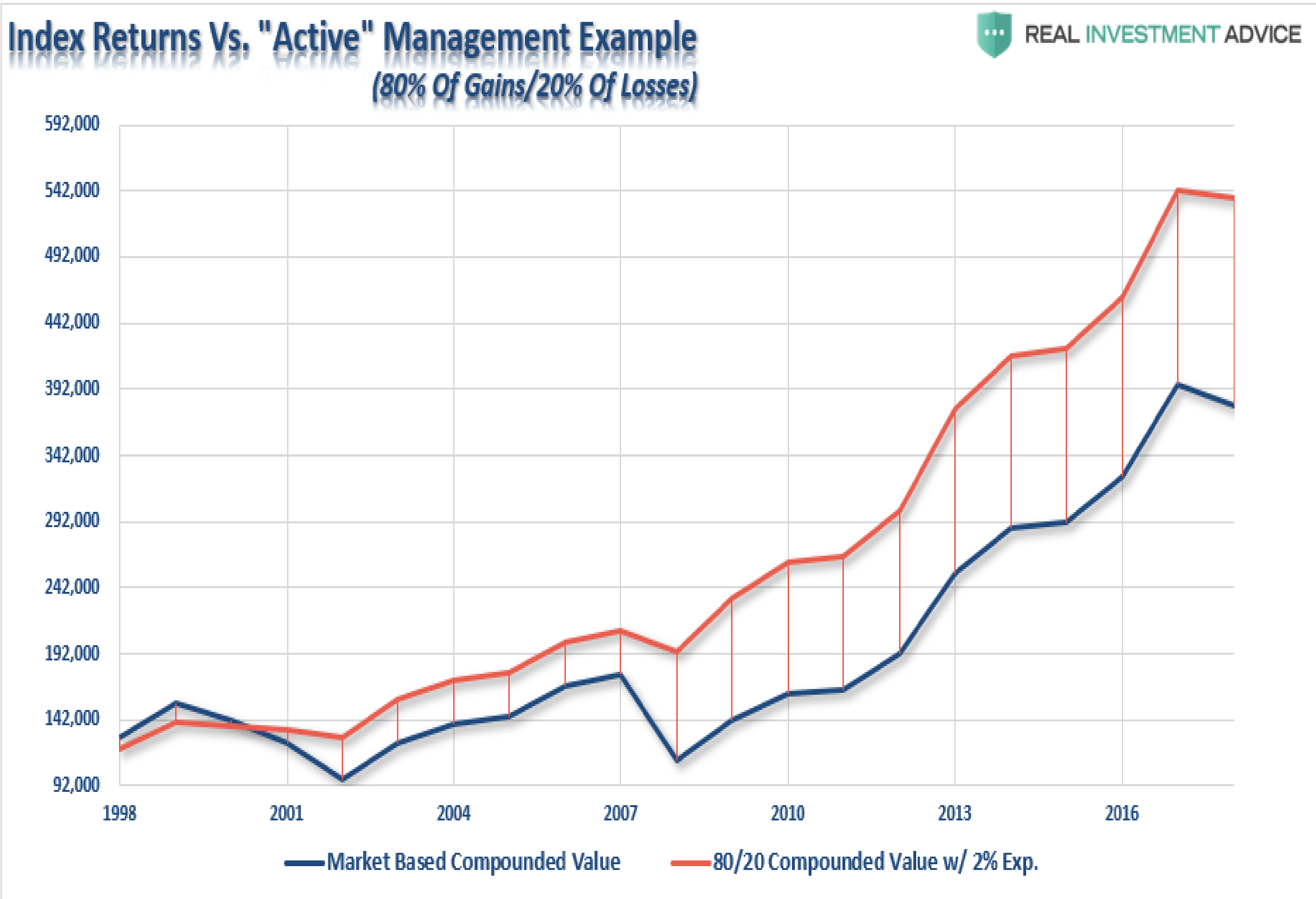
This is the basis of the 80/20 investment philosophy and the driver behind the risk management process.



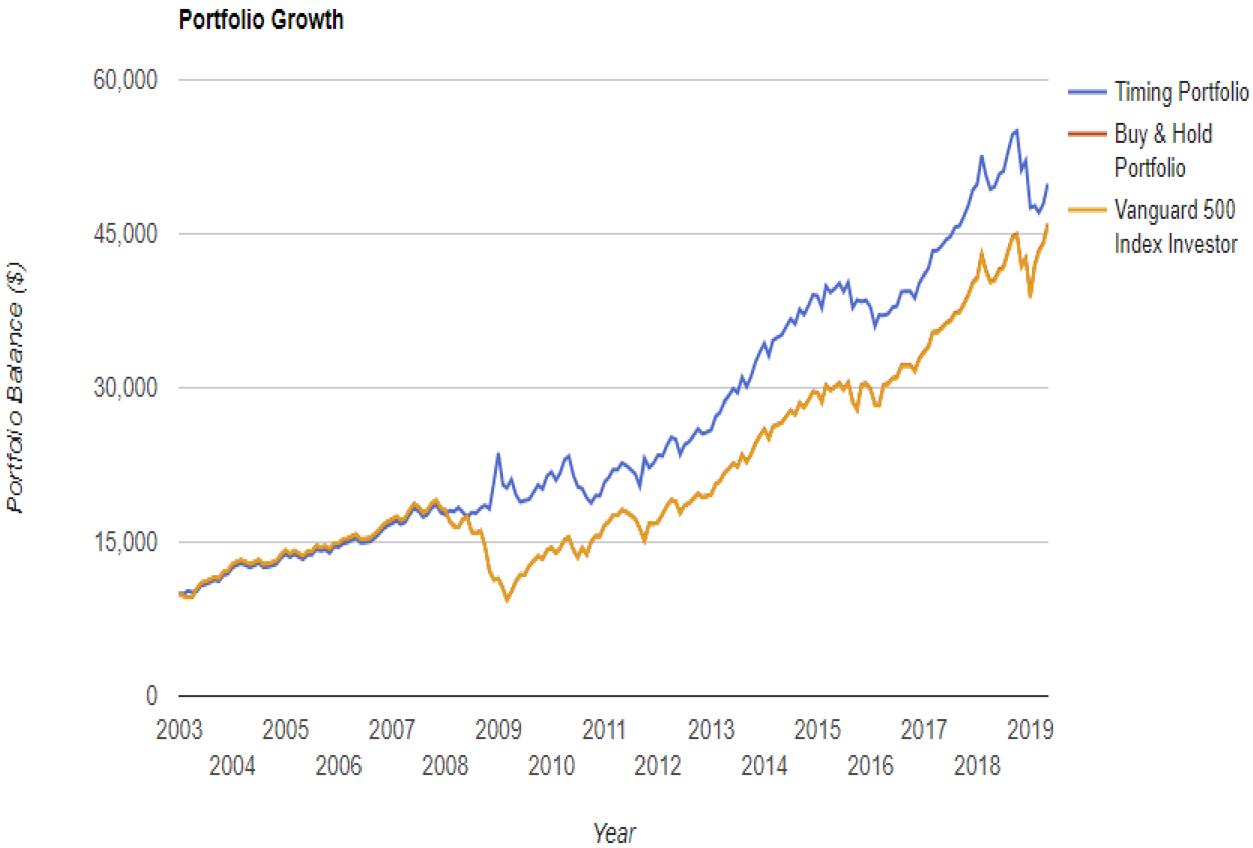
While you may not beat the market from one year to the next, you will never have to suffer the *?time loss?* required to ?*get back to even.?* **In the long run, you will win**. As shown in the table below, a $100,000 investment in the S&P 500 returns a far lower value than the *?Rothschild 80/20 Rule?* model. **This is even if I include a ridiculous 2% management fee.**

Date	Value	Initial Investment of $100k		80/20 Rule	Market Based Compounded Value		80/20 Compounded Value		80/20 Compounded Value w/ 2% Exp.	
1/1/1998	28.34%	$	128,337.95	22.67%	$	128,337.95	$	122,670.36	$	120,216.96
1/1/1999	20.89%	$	155,141.79	16.71%	$	155,141.79	$	143,166.47	$	140,303.14
1/1/2000	-9.03%	$	141,129.66	-1.81%	$	141,129.66	$	140,580.36	$	137,768.76
1/1/2001	-11.85%	$	124,406.14	-2.37%	$	124,406.14	$	137,248.68	$	134,503.70
1/1/2002	-21.97%	$	97,079.02	-4.39%	$	97,079.02	$	131,219.06	$	128,594.67
1/1/2003	28.36%	$	124,606.56	22.68%	$	124,606.56	$	160,985.63	$	157,765.91
1/1/2004	10.74%	$	137,992.76	8.59%	$	137,992.76	$	174,821.09	$	171,324.66
1/1/2005	4.83%	$	144,663.99	3.87%	$	144,663.99	$	181,582.43	$	177,950.79
1/1/2006	15.61%	$	167,249.74	12.49%	$	167,249.74	$	204,262.16	$	200,176.92
1/1/2007	5.48%	$	176,422.95	4.39%	$	176,422.95	$	213,224.76	$	208,960.26
1/1/2008	-36.55%	$	111,936.22	-7.31%	$	111,936.22	$	197,637.03	$	193,684.29
1/1/2009	25.94%	$	140,967.14	20.75%	$	140,967.14	$	238,643.13	$	233,870.26
1/1/2010	14.82%	$	161,860.01	11.86%	$	161,860.01	$	266,938.74	$	261,599.97
1/1/2011	2.10%	$	165,256.44	1.68%	$	165,256.44	$	271,419.84	$	265,991.44
1/1/2012	15.89%	$	191,516.66	12.71%	$	191,516.66	$	305,924.00	$	299,805.52
1/1/2013	32.15%	$	253,079.86	25.72%	$	253,079.86	$	384,595.63	$	376,903.72
1/1/2014	13.52%	$	287,296.25	10.82%	$	287,296.25	$	426,193.49	$	417,669.62
1/1/2015	1.38%	$	291,260.94	1.10%	$	291,260.94	$	430,898.67	$	422,280.69
1/1/2016	11.74%	$	325,454.97	9.39%	$	325,454.97	$	471,368.67	$	461,941.30
1/1/2017	21.61%	$	395,785.79	17.29%	$	395,785.79	$	552,858.89	$	541,801.71
1/1/2018	-4.23%	$	379,044.06	-0.85%	$	379,044.06	$	548,181.70	$	537,218.07

Here is a chart to illustrate the deviation more effectively. *(Capital appreciation only.)*



Yes, it?s only a bit more than a hundred thousand dollars worth of difference, but the reduced levels of volatility allowed investors to emotionally *?stick?* to their discipline over time. **Furthermore, by minimizing the drawdowns, assets are allowed to truly *?compound?* over the long-term.** An easy way to apply this principle is to use a simple moving average crossover. In the chart below, you are long equities which the S&P 500 index is above the 12-month moving average, and you switch to bonds when the S&P 500 falls below the 12-month average. *(You can run this back test yourself at [Portfolio Visualizer)](#)*



Portfolio	Initial Balance	Final Balance	CAGR	Stdev	Best Year	Worst Year	Max. Drawdown	Sharpe Ratio	Sortino Ratio	US Mkt Correlation
Timing Portfolio	$10,000	$49,883	10.34%	11.76%	33.93%	-7.87%	-20.60%	0.79	1.30	0.43
Buy & Hold Portfolio	$10,000	$45,962	9.79%	13.40%	32.31%	-36.81%	-50.80%	0.68	1.00	1.00
Vanguard 500 Index Investor	$10,000	$45,817	9.77%	13.40%	32.18%	-37.02%	-50.97%	0.67	0.99	1.00

No, it?s not perfect every time. But no measure of risk management is. **But having a discipline to manage risk is better than not having one at all.** Get it. Got it. Good.

How To Add Exposure

I have also received quite a few emails asking how to add exposure to the market, particularly if in a large cash position currently. The answer is more in line with the age-old question:

> *?How do you pick up a porcupine? Carefully.?*

Here are some guidelines to follow:

1. **Move slowly.** There is no rush in adding equity exposure to your portfolio. Use pullbacks to previous support levels to make adjustments.

2. **If you are heavily UNDER-weight equities, DO NOT try and fully adjust your portfolio to your target allocation in one move.**This could be disastrous if the market reverses sharply in the short term. Again, move slowly.
3. **Begin by selling laggards and losers.** These positions are dragging on performance as the market rises and tend to lead when markets fall. Like *?weeds choking a garden,?* pull them.
4. **Add to sectors, or positions, that are performing with, or outperforming,** the broader market. *(We detail these every week* ***at RIAPRO.)***
5. **Move *?stop loss?* levels up to current breakout levels for each position.** Managing a portfolio without *?stop loss?* levels is like driving with your eyes closed.
6. **While the technical trends are intact, risk considerably outweighs the reward.** If you are not comfortable with potentially having to sell at a LOSS what you just bought, then wait for a larger correction to add exposure more safely. There is no harm in waiting for the *?fat pitch?* as the current market setup is not one.
7. **If none of this makes any sense to you ? please consider hiring someone** to manage your portfolio for you. It will be worth the additional expense over the long term.

Evidence Is Mounting

While we did rebalance exposures to the market in portfolios recently, as the bullish trend does currently persist, there is growing evidence of *?cracks?* appearing. The bull market is understandably aged and the weaker fundamental and economic backdrop has a more decisive impact on an *"aging bull."* **Therefore**, **it is extremely important to remember that whatever increase in equity risk you take, could very well be reversed in short order** due to the following reasons:

1. *We are in the late stages of the bull market.*
2. *Economic data is weakening*
3. *Earnings are beating continually reduced estimates*
4. *Volume is weak*
5. *Longer-term technical underpinnings are weak and extremely stretched.*
6. *Complacency remains high*
7. *Share buybacks are set to slow (which have comprised about 80% of the markets bid.)*
8. *The yield curve continues to flatten, and invert, which applies economic pressure.*

What you decide to do with this information is entirely up to you. As I stated, **I do think there is enough of a bullish case being built to warrant taking some equity risk on a very short-term basis. We will see what happens over the next couple of weeks.** However, the longer-term dynamics are turning more bearish. **When those negative price dynamics are combined with the fundamental and economic backdrop, the *?risk?* of having excessive exposure to the markets greatly outweighs the potential *?reward. ?*** *Investing is not a competition. It is a game of long-term survival.*