

Bulls Chant

Into A Megaphone - "All-Time Highs"



In this issue of, "Bulls Chant Into A Megaphone - 'All-Time Highs:'"

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- ***Sector & Market Analysis***
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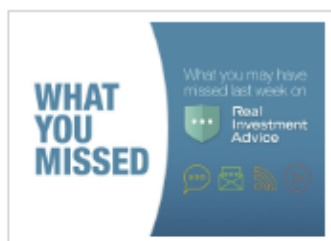
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#WhatYouMissed On RIA This Week: 08-07-20

Written by Lance Roberts | Aug 7, 2020

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Bulls Charge To All-Time Highs

As discussed previously in [*"Insanely Stupid,"*](#) we noted the market remained confined to its consolidation channel, but the bullish bias was to the upside.

*"While the market has not been able to push above the recent July highs, support is holding at the rising bullish trend line. **With the short-term 'buy signals' back in play, the bias at the moment is to the upside.***

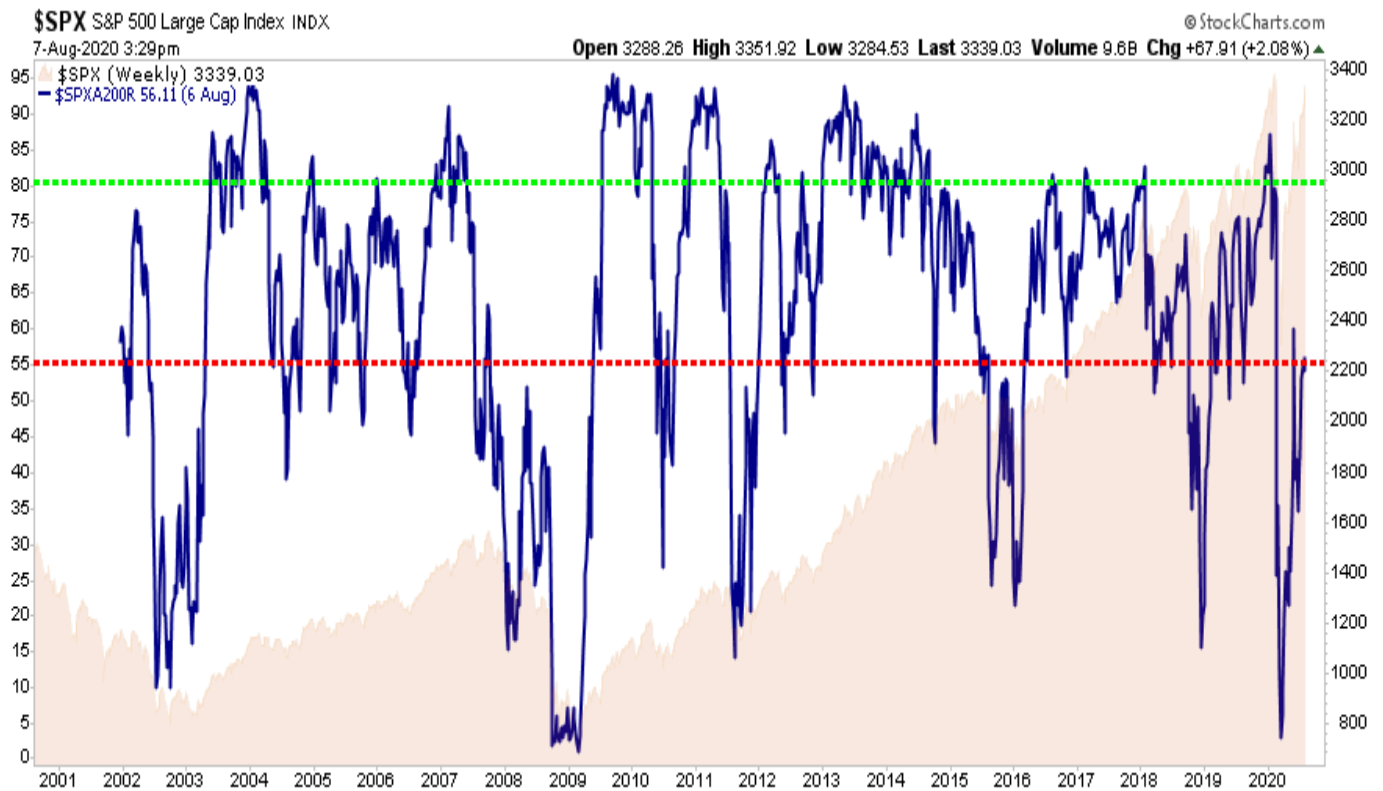
*However, as we have discussed over the last couple of weeks, July held to its historical trends of strength. **With a bulk of the S&P 500 earnings season behind us, we suspect the weakening economic data will begin to weigh sentiment in August and September.***



While weaker economic data has not yet dented the *"bullish sentiment"* at this juncture, it doesn't mean it won't. **However, as we have discussed over the last several weeks, a breakout of the consolidation range, which was capped by the June highs, would put all-time highs into focus.**

A Weighted Distortion

The concern is that what you see with the market, is not necessarily what you get. The chart below shows the number of stocks trading above the 200-dma versus the S&P 500 trading above its 200-dma.

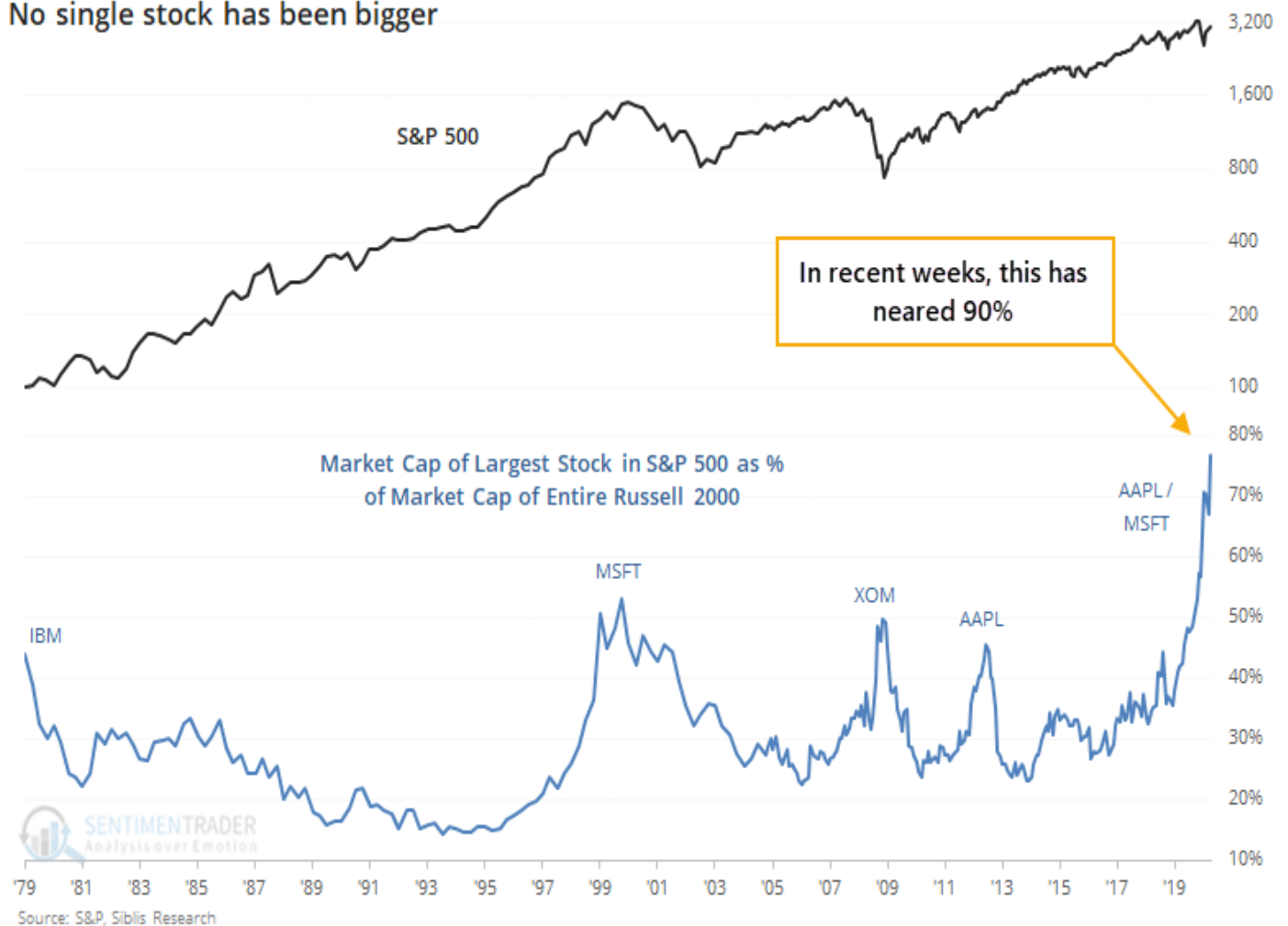


In theory, if the "market" is above its 200-dma, then a large number of stocks, usually about 80%, should also be. However, such is not the case, as only 55% currently do so.

The market is currently being driven to new highs by the "chase" into the largest mega-capitalization stocks. Sentiment Trader noted this on Friday:

"The biggest stock in the U.S. and nearly the world, Apple, keeps powering higher. At the end of June, the value of Apple alone was nearly 80% of the Russell 2000 index's market capitalization. As of today, it's nearly 90%. This is astounding - in the past 40 years, no single stock has come close to dwarfing the value of so many other companies."

No single stock has been bigger

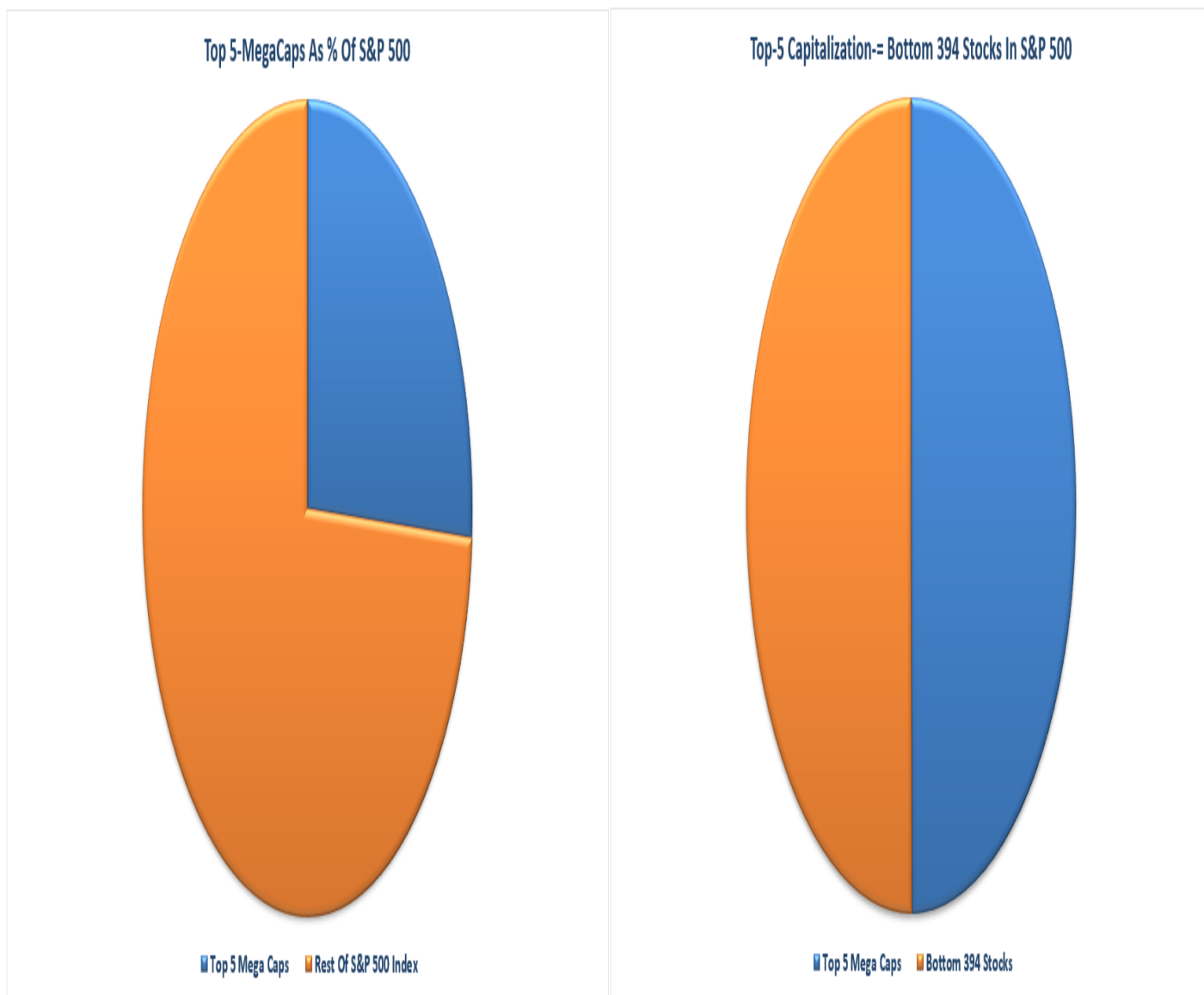


By itself, this data point does not have a lot of historical relevance. However, it does tend to be more of an indication of underlying *"exuberance"* in the market.

The point here, however, is the top-5 stocks are distorting the overall market participation.

Let Me Explain The Math

Currently, the top-5 S&P stocks by market capitalization (*AAPL*, *AMZN*, *GOOG*, *FB*, and *MSFT*) make up the same amount of the S&P 500 as the bottom 394 stocks. Those same five also comprise 26% of the index alone.



What investors are missing is that the top-5 stocks are distorting the movements in the overall index.

For each \$1 put into each of those top-5 stocks, the impact on the index is the same as putting \$1 into each of the bottom 394 stocks. Such is clearly not a true representation of either the market or the economy.

As we have noted recently, if you own anything OTHER than those top-5 stocks, your portfolio is likely underperforming the market this year.

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Exuberance Abounds

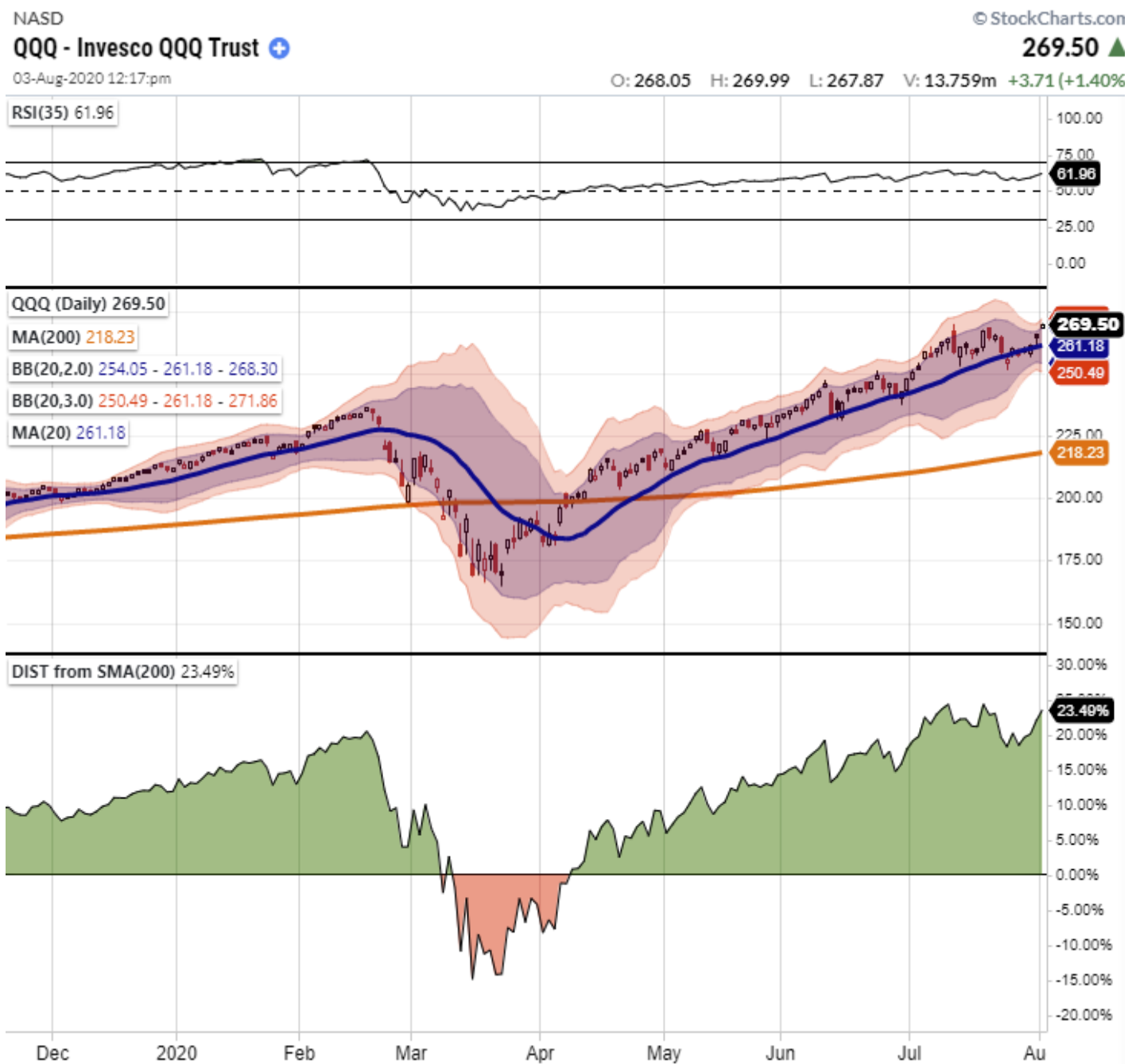
This past week, we discussed with our [**RIAPro Subscribers \(Try Risk-Free for 30-days\)**](#) the dangers of chasing markets, which have deviated extremely from their long-term means. **The risk, of course, is that markets always, without exception, revert to the mean. The only question is the "timing" of the event.**

Specifically, we noted the deviation of the Nasdaq from its 200-dma, which remains near a record high.

"Moving averages, especially longer-term ones, are like gravity. The further prices become deviated from long-term averages, the greater the 'gravitational pull' becomes. An 'average' requires prices to trade above and below the average level. The risk of a reversion grows with the size of the deviation."

The Nasdaq currently trades more than 23% above its 200-dma. The last time such a deviation existed was in February of this year. The Nasdaq also trades 3-standard deviations above the 200-dma, which is another extreme indication.

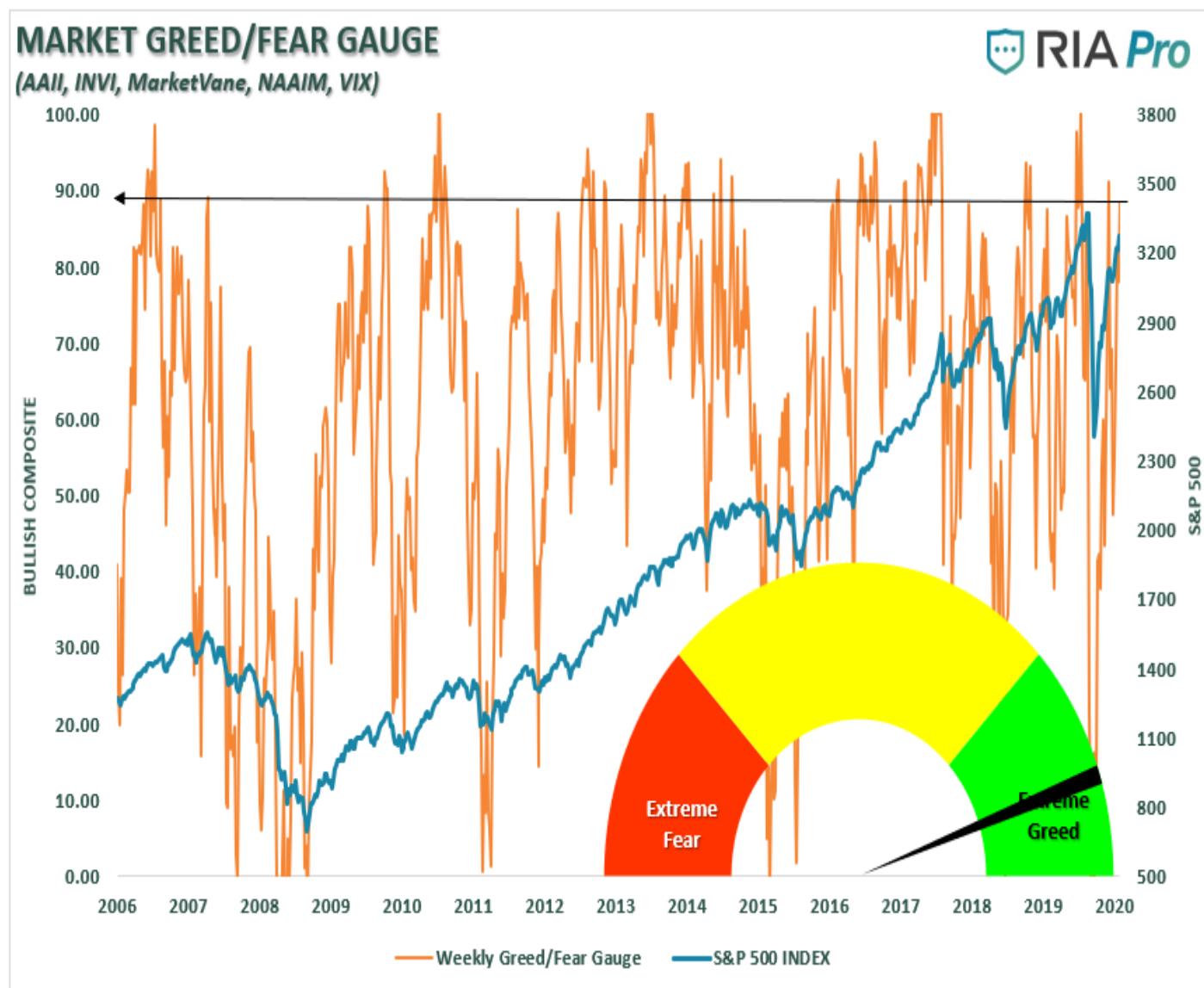
Such does not mean the market is about to crash. However, it does suggest the 'rubber band' is stretched so tightly any minor disappointment could lead to a contraction in prices."



Again, this deviation is driven by the largest cap-weighted names. Still, there are also more extreme signs of speculative appetite currently flowing into the markets.

The Greed Factor

The [RIAPro sentiment gauge](#), which is based on actual investor positioning, is at more extreme levels.



The put/call ratio is also at a historic low, which suggests that investors have given up hedging risk in portfolios entirely. I have marked the previous points where the put/call ratio was this imbalanced.

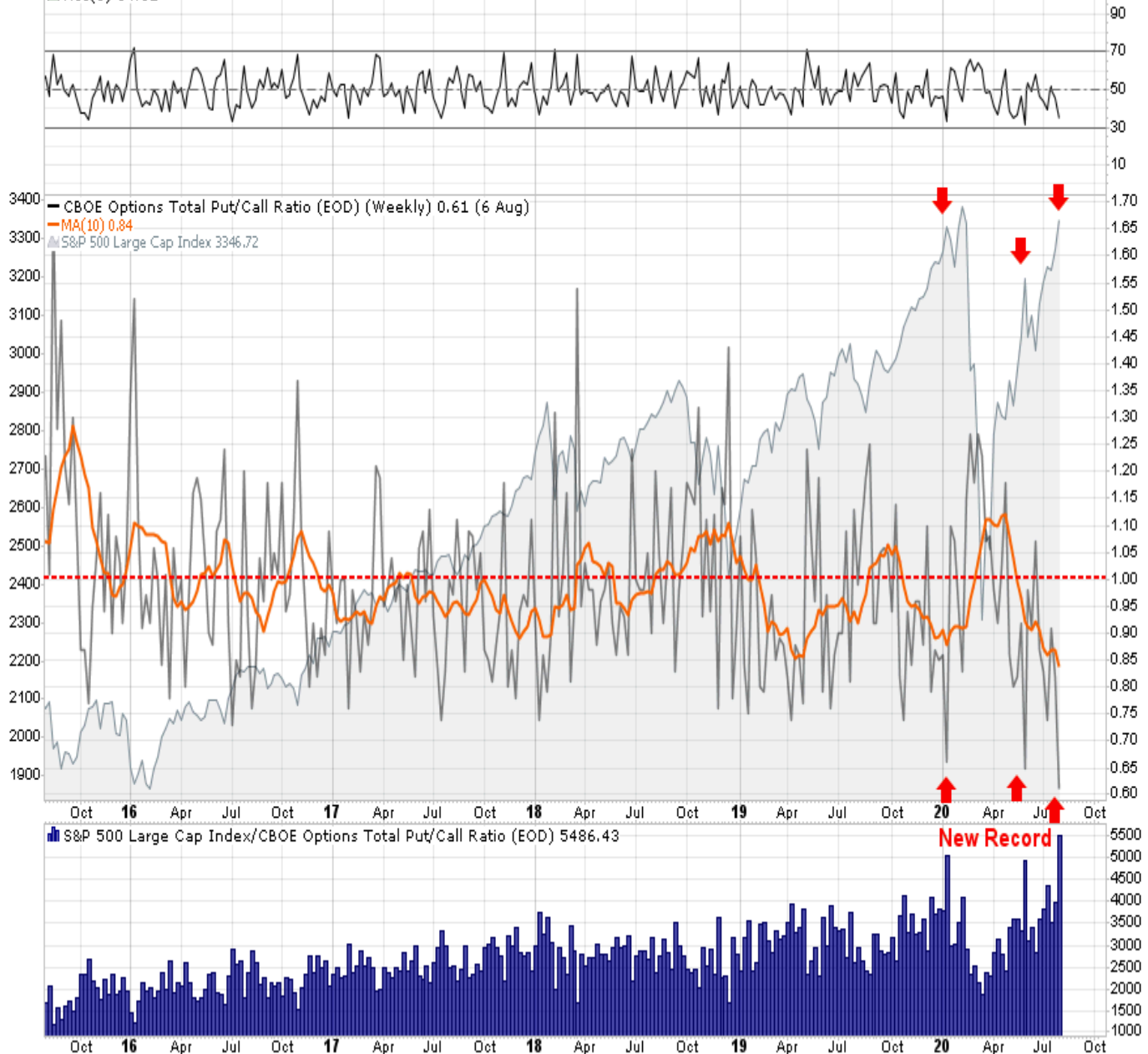
\$CPC CBOE Options Total Put/Call Ratio (EOD) INDX

6-Aug-2020

© StockCharts.com

Open 0.67 High 0.74 Low 0.61 Close 0.61 Chg -0.21 (-25.61%)

▲ RSI(6) 34.52



Importantly, this is all very *"bullish"* for now.

The point about these indicators, is that in the short-term (*a few days to a few weeks*) it suggests the markets will likely continue to rise. Such is because *"momentum"* is a tough thing to kill.

However, longer-term, they have a long history of suggesting increasing levels of risk, which eventually leads to less pleasant outcomes.

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The Megaphone

In the short-term, there seems to be little worry about. I thought this sentiment was summed up best by Jeffrey Marcus, who manages the [TPA Analytics long-short portfolio for RIAPro:](https://twitter.com/TpaResearch/status/1291459674240421893?s=20)

<https://twitter.com/TpaResearch/status/1291459674240421893?s=20>

However, in the longer-term, the bulls may be walking into a trap.

While the bulls are chanting "*all-time highs*," it falls within the context of an ongoing topping process referred to as a "*megaphone*" pattern. Here is the definition:

"A broadening formation is a price chart pattern characterized by increasing price volatility and diagrammed as two diverging trend lines, one rising and one falling.

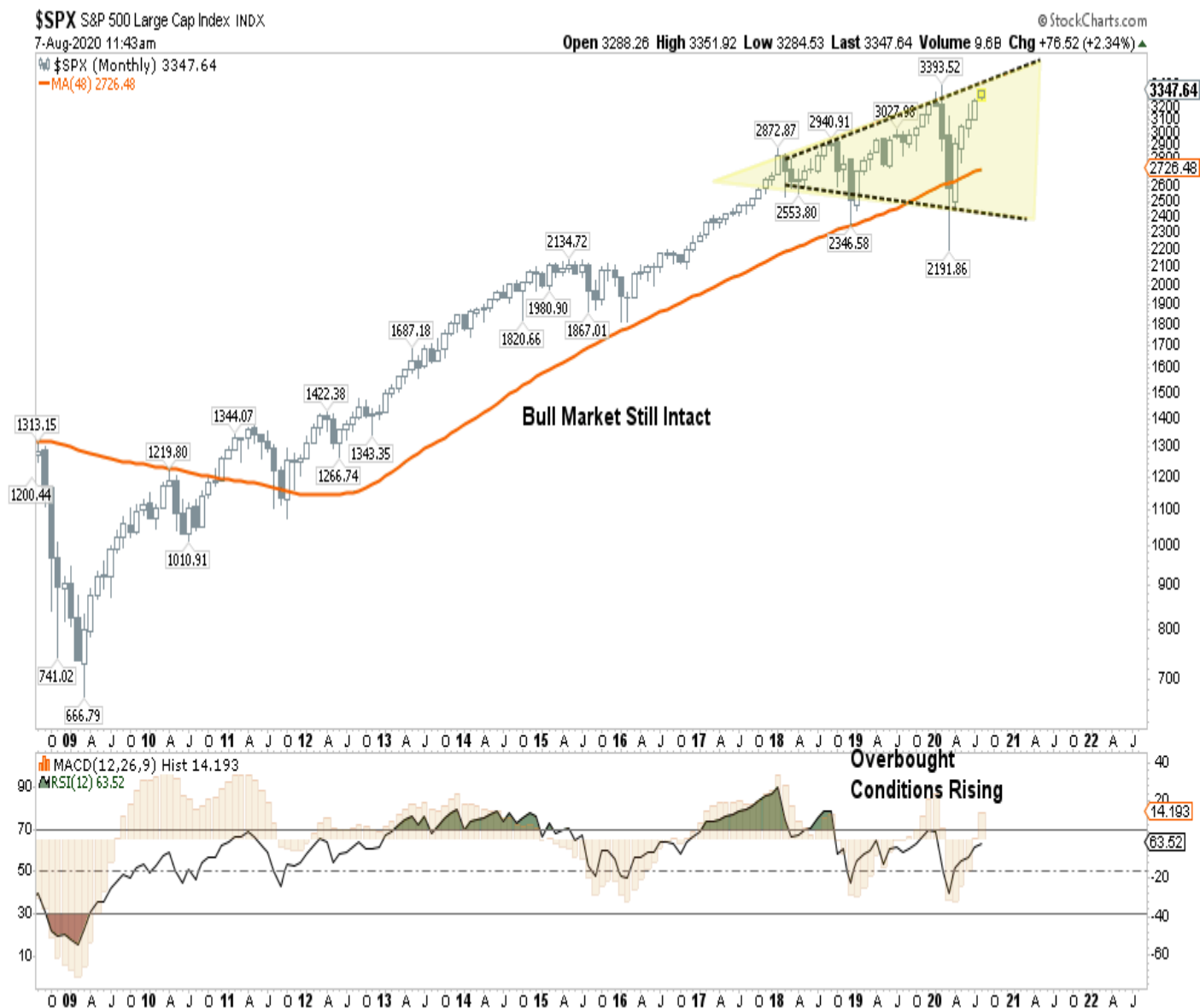
These formations are relatively rare during normal market conditions over the long-term since most markets tend to trend in one direction or another over time. The formations are more common when market participants have begun to process a series of unsettling news topics. Topics such as geopolitical conflict, a change in Fed policy, or a combination of the two, are likely to coincide with such formations.

Broadening formations are generally bearish for most long-term investors since they are characterized by rising volatility without a clear move in a single direction."


It's Just A Chart

This broadening, or megaphone, pattern is seen below on the monthly chart. Importantly, despite the "*correction*," in March, the "*bull market*" that began in 2009 remains intact as the low monthly close did not break the 4-year moving average.

Furthermore, this is a "*monthly*" chart, so it is very slow to form. As such, it is critical to consider this analysis in context. **The chart does not mean the markets are about to crash, nor is it a useful tool to try and "*time*" the market.**



The market will hit new highs as it reaches the top of the upper trendline, where it will meet more formidable resistance. With the market back to a more extreme overbought condition, the "low hanging fruit" has been picked.



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Risk/Reward Ranges

Nonetheless, as discussed below, the current levels of "bullish sentiment" and "momentum" keeps our portfolios allocated toward "risk." However, we are moving closer toward the "exit," so we are not the last one trying to get out of the theater when someone yells "fire."

With the markets closing just at all-time highs, we can only guess where the next market peak will be. Therefore, to gauge risk and reward ranges, we have set targets at 3500, 3750, and 4000 or 4.4%, 12.2%, and 19.5%, respectively.

7-Aug-2020

Open 333.28 High 334.88 Low 332.30 Close 334.57 Volume 56.8M Chg +0.24 (+0.07%)▲



Here are the current risk/reward ranges:

- **+4.4% to 3500 vs. -4.3% to June high breakout support.**
- **+4.4% to 3500 vs. -5.7% to the 50-dma.**
- **+12.2% to 3750 vs. -9.6% to the 200-dma**
- **+12.2% to 3750 vs. -11.5% to the June consolidation lows.**
- **+19.5% to 4000 vs. -22.17% to the March closing low. (Not shown)**

Given there is no good measure to justify upside potential from a breakout to new highs, you can personally go through a lot of mental exercises. While there is certainly a potential the market could rally 19.9% to 4000, it is also just as reasonable the market could decline 22.2% test the March closing lows. Completion of the "megaphone pattern" discussed above would be a 37.43% decline.

Just in case you think that can't happen, just remember no one was expecting a 35% decline in March either.

As we said last week, *"risk happens fast."*

Portfolio Positioning

Let me restate our position for the last several weeks.

?With our portfolios almost entirely allocated towards equity risk in the short-term, we remain incredibly uncomfortable.?

Such remains the case this week. While we certainly enjoy the markets lifting our client's portfolio values higher, we are keenly aware of the risk.

As Chuck Prince, CEO of Citigroup, once stated:

"When the music stops, in terms of liquidity, things will be complicated. But as long as the music is playing, you?ve got to get up and dance. We?re still dancing,? - July 2007

Note the date.

Just as it was then, stocks kept running well into 2008. But eventually, the music stopped, and poor Chuck was left without a chair.

Given we are now getting more extreme short-term overbought conditions, the risk of a short-term reversion has risen.

As noted last week, we have continued to maintain our equity exposure to the markets. Still , we have continued to *"hedge around the edges,"* by adjusting our bond duration, adding a long-dollar position to hedge our gold exposures, and adding more *"defensive"* names to our equity allocation.

Our job remains the same, protect our client?s capital, reduce risk, and try to come out on the other side in one piece.

While we are certainly more bullish on markets currently, as momentum is still in play, it doesn?t mean we aren?t keenly aware of the risk.

Pay attention to what you own, and how much risk you are taking to generate returns. Going forward, this market will likely have a nasty habit of biting you when you least expect it.



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The MacroView



#MacroView: Fed Wants Inflation But Their Actions Are Deflationary

Written by Lance Roberts | Aug 7, 2020

A CNBC article states the Fed is expected to make a major commitment to ramping up inflation. While the Fed may want inflation, their very actions continue to be deflationary.

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See You Next Week

By Lance Roberts, CIO

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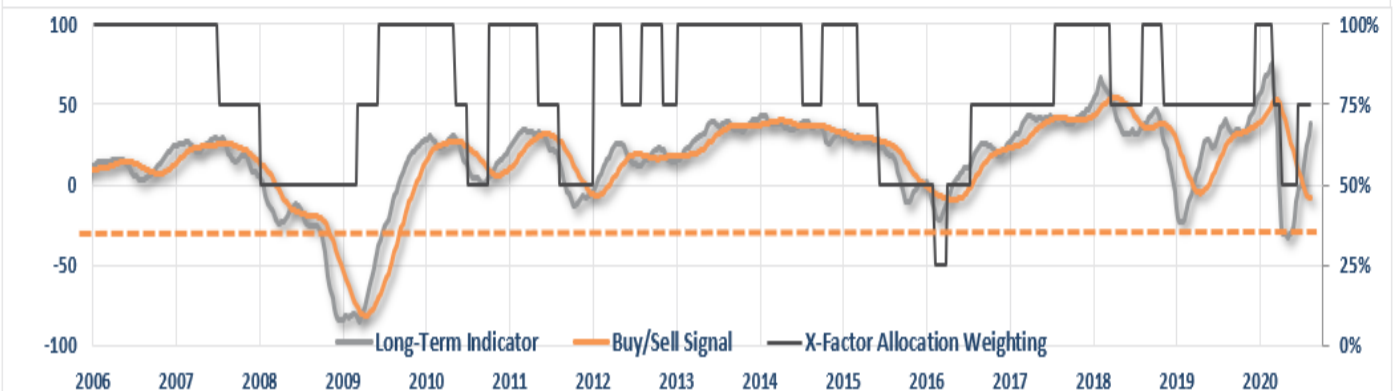
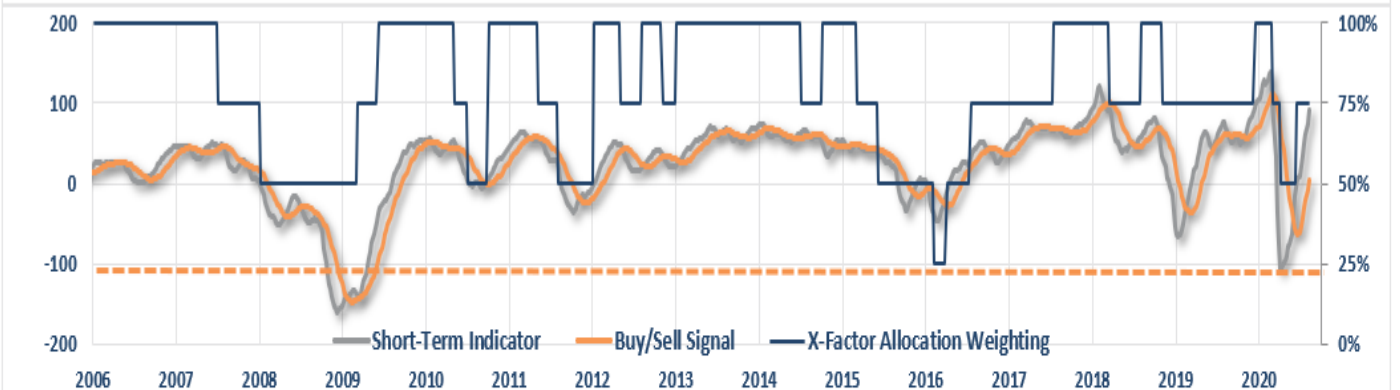
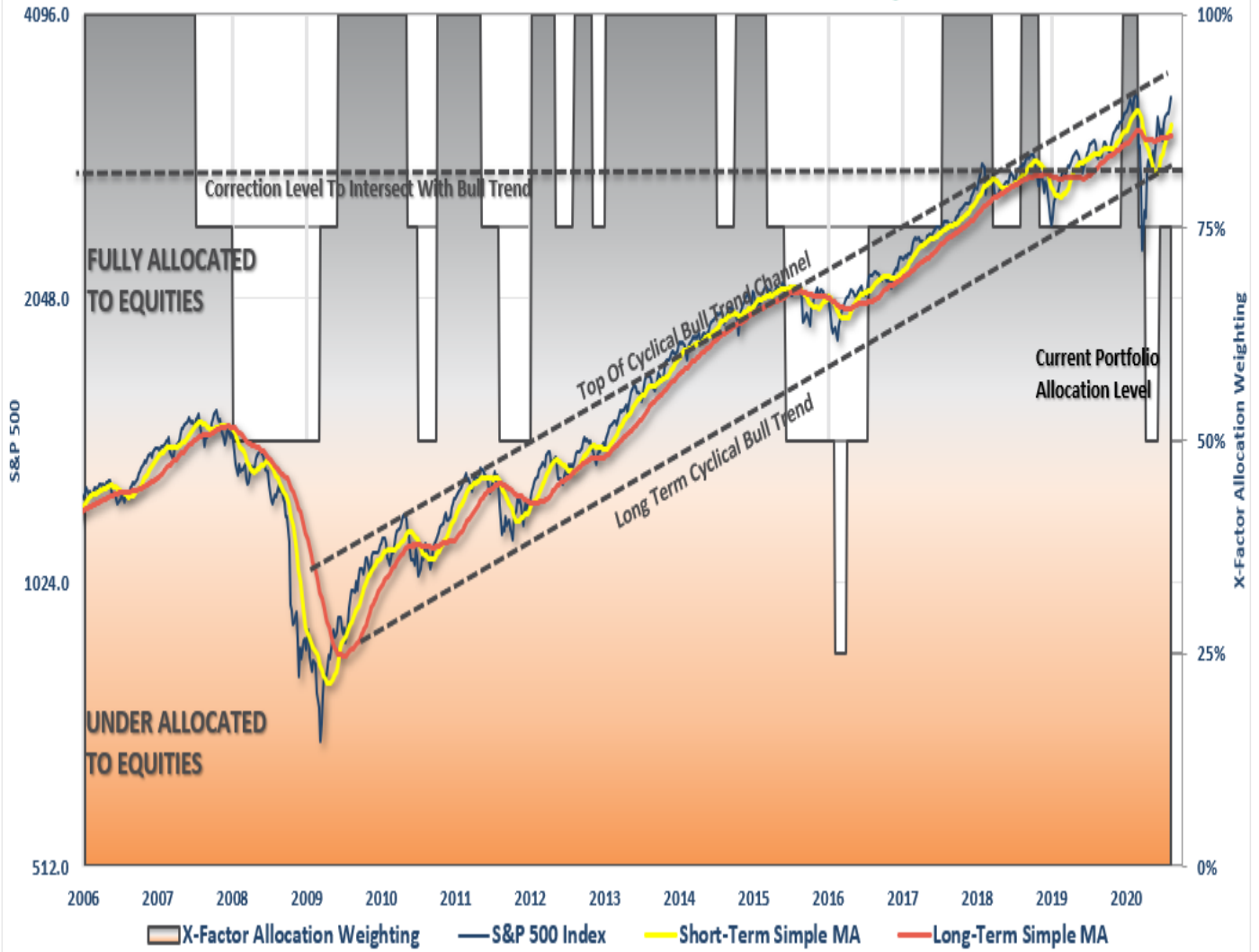
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Current Portfolio Weighting



Current 401k Allocation Model

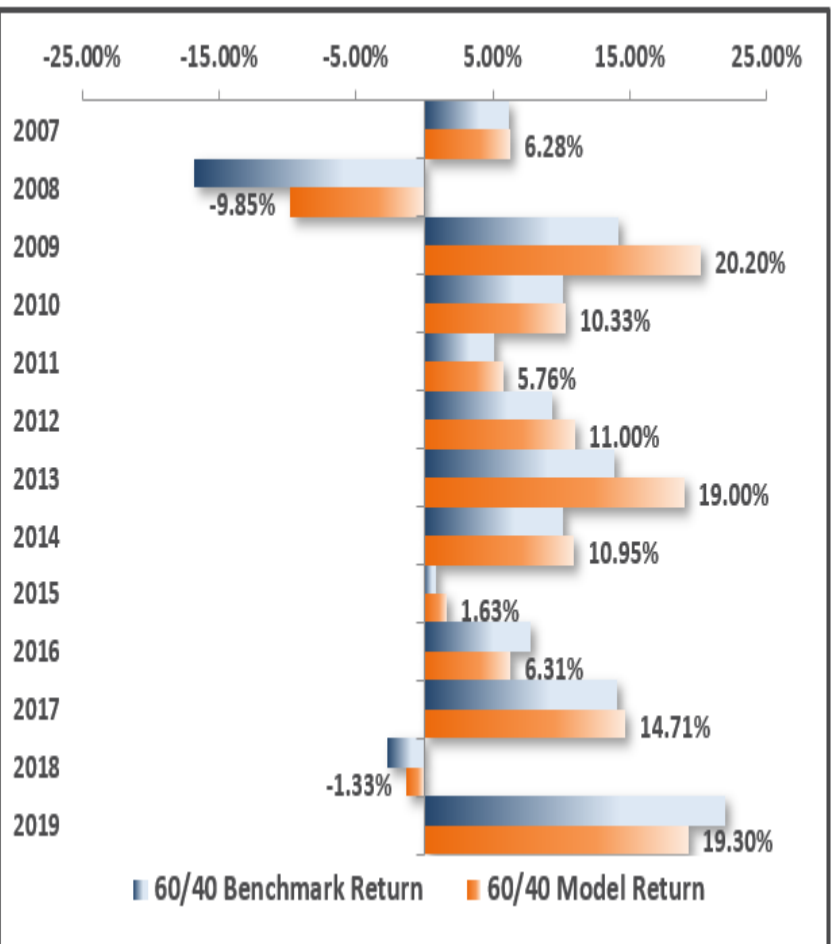
20.00% Cash + All Future Contributions

Primary concern is the protection of investment capital

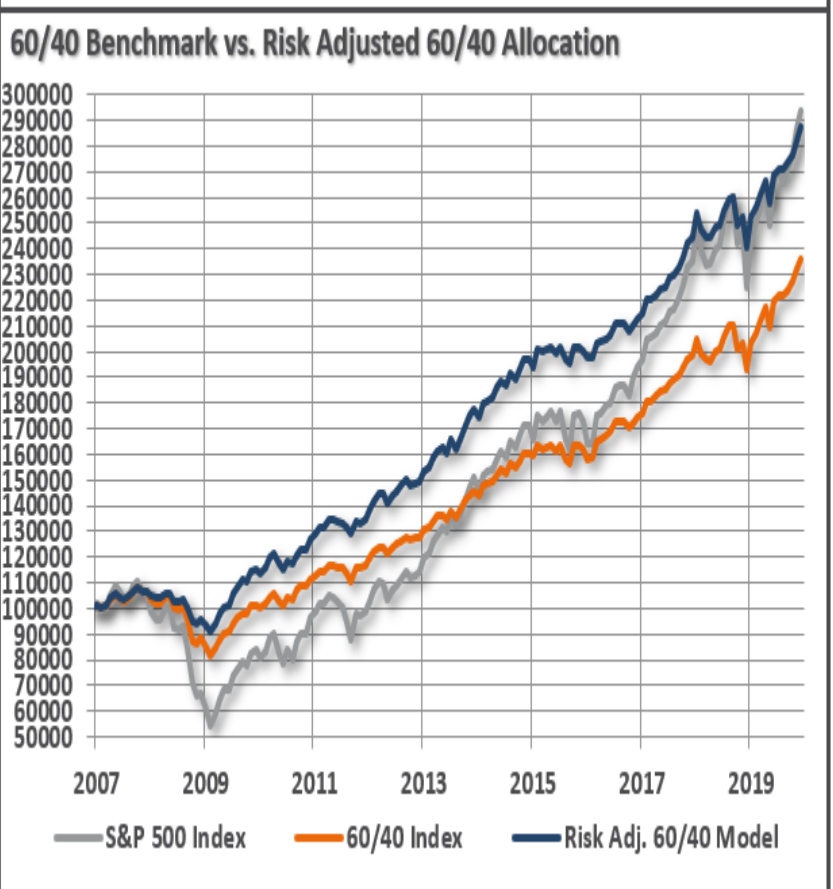
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Model performance is a two-asset model of stocks and bonds relative to the weighting changes made each week in the newsletter. Such is strictly for informational and educational purposes only and should not be relied on for any reason. Past performance is not a guarantee of future results. Use at your own risk and peril.

Year	60/40 Benchmark Return	60/40 Model Return
2007	6.15%	6.28%
2008	-16.79%	-9.85%
2009	14.22%	20.20%
2010	10.17%	10.33%
2011	5.14%	5.76%
2012	9.33%	11.00%
2013	13.91%	19.00%
2014	10.08%	10.95%
2015	0.83%	1.63%
2016	7.79%	6.31%
2017	14.12%	14.71%
2018	-2.72%	-1.33%
2019	21.96%	19.30%



Portfolio vs Benchmark Statistics	
Number of Up Years	11
Number of Down Years	2
Best One Year Return Of Benchmark	21.96%
Best One Year Return Of Model	20.20%
Worst One Year Return Of Benchmark	-16.79%
Worst One Year Return Of Model	-9.85%
Benchmark Return 2007-Present	123.78%
Model Return 2007-Present	173.11%
Total Alpha Generated	49.33%
Mean Annual Return Of Benchmark	7.25%
Mean Annual Return Of Model	8.79%
Beta Of Model vs Benchmark	0.86
Jensens Alpha	2.30%
Sharpe Ratio	0.29



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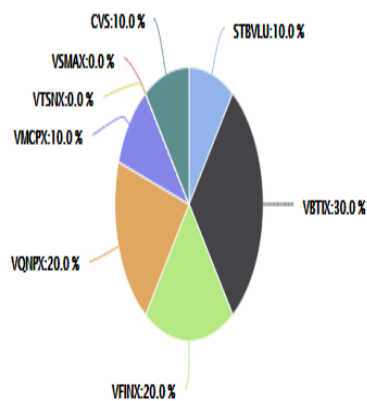
Retirement Income (My Portfolio Annual ROR 9.44 %)		—
Current account balance	10,000	
Estimated Retirement Balance	632,861	
Estimated Retirement Balance (Inflation Adj)	620,204	
Monthly Income	2,768	
Monthly Income (Inflation Adj)	2,713	
My Cumulative Contribution	172,934	
Employer Cumulative Contribution	103,760	

RIAPro Portfolio

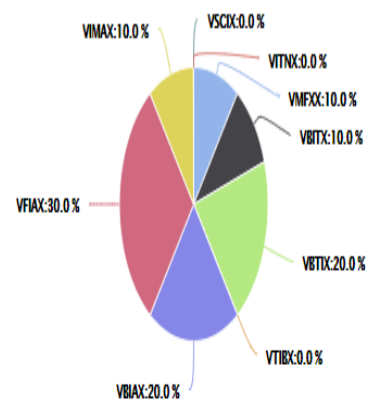
RIA PRO MODEL PL ▾

Retirement Income (RiaPro Annual ROR 9.02 %)		—
Current account balance	10,000	
Estimated Retirement Balance	609,786	
Estimated Retirement Balance (Inflation Adj)	597,590	
Monthly Income	2,667	
Monthly Income (Inflation Adj)	2,614	
My Cumulative Contribution	172,934	
Employer Cumulative Contribution	103,760	

My Fund Composition



RIAPro Fund Composition



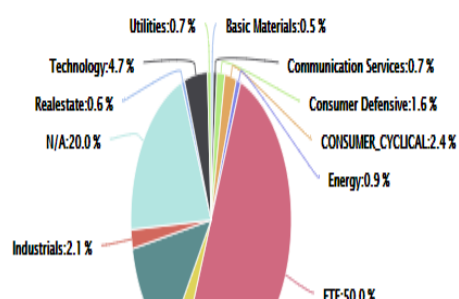
My Asset Composition

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My Sector Composition



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