In this issue of "Speculative Mania Continues As It 'Goes Up In Smoke.'"

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- ***Sector & Market Analysis***
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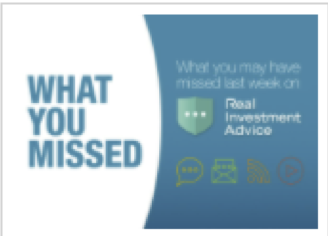
Catch Up On What You Missed Last Week



#WhatYouMissed On RIA This Week: 2-12-21

Written by Lance Roberts | Feb 12, 2021

Here is what you might have missed from the RIA Crew last week. A compilation of our best blogs, newsletter, podcasts, the daily radio show and commentary from RIAPRO.NET.

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Market Review And Update

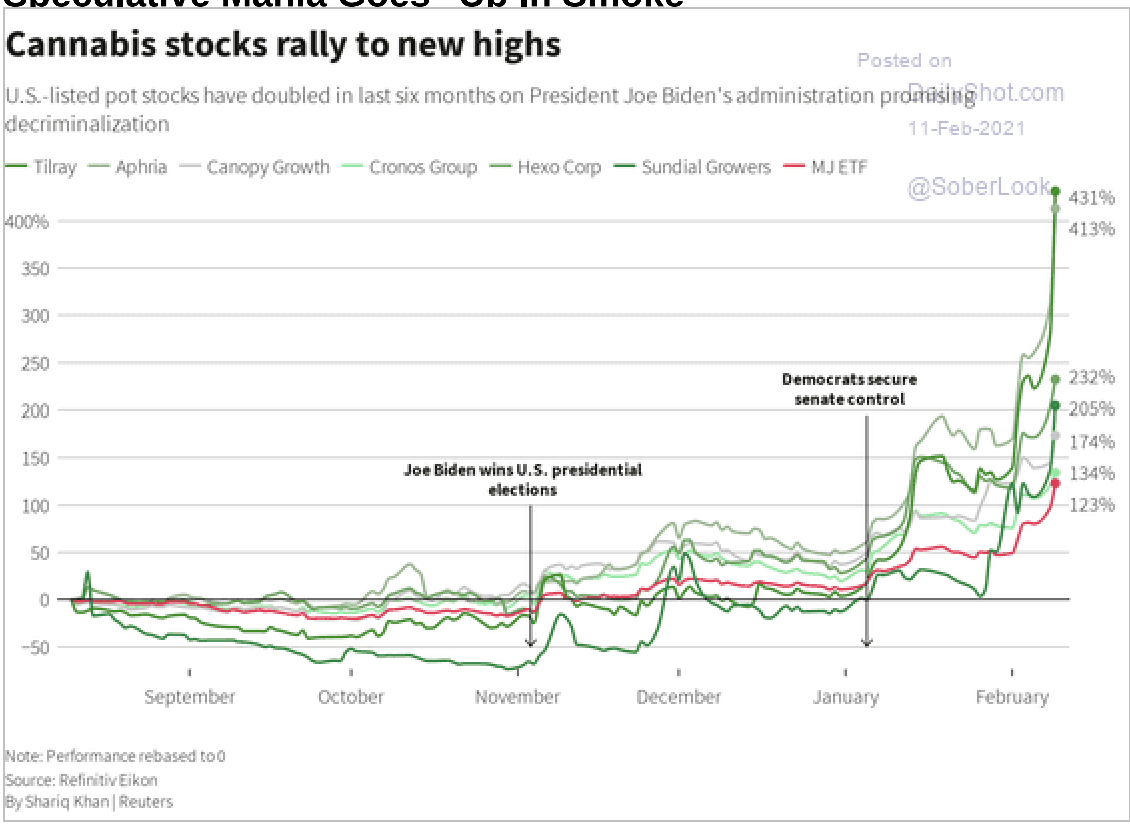
Last week, we discussed how the market successfully retested and held the 50-dma and rallied enough to turn money flows back positive. We addressed this point on Thursday in our daily ***"3-Minutes"*** **video** ***(subscribe for daily updates)***, https://www.youtube.com/watch?v=hntNXBaJWcE ***As previously noted:***

> *"While the money flow 'buy signal' will likely trigger next week, the market is already trading 2-standard deviations above the 40-dma.* ***Such suggests that the upside may be more limited over the next couple of weeks."***

As the market struggled to hold gains, as denoted by the two red-dashed lines, that was the case. Notably, the entire week's gains came in the last hour of trading on Friday. With the money flow signals still positive, the overall bias to the market remains bullish for now. **However, the rally is still at risk currently, given the more extreme overbought and bullish conditions.** Speculation remains rampant, and **there are many indicators from relative strength to participation that suggest we could see another correction in March or early April.** When our money flow indicators turn lower again, we will suggest reducing risk accordingly. However, the problem with all technical indicators is two-fold:

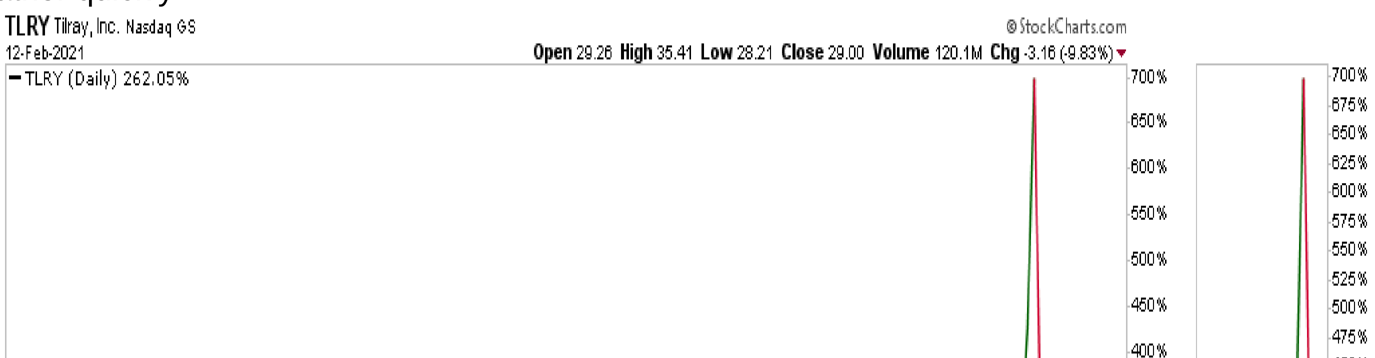
1. *They don't distinguish between a 5% correction and a 20% drawdown; and,*
2. ***Secondly, the corrections often occur so quickly you don't have much time to decide just how defensive you need to be.***

Speculative Mania Goes "Up In Smoke"

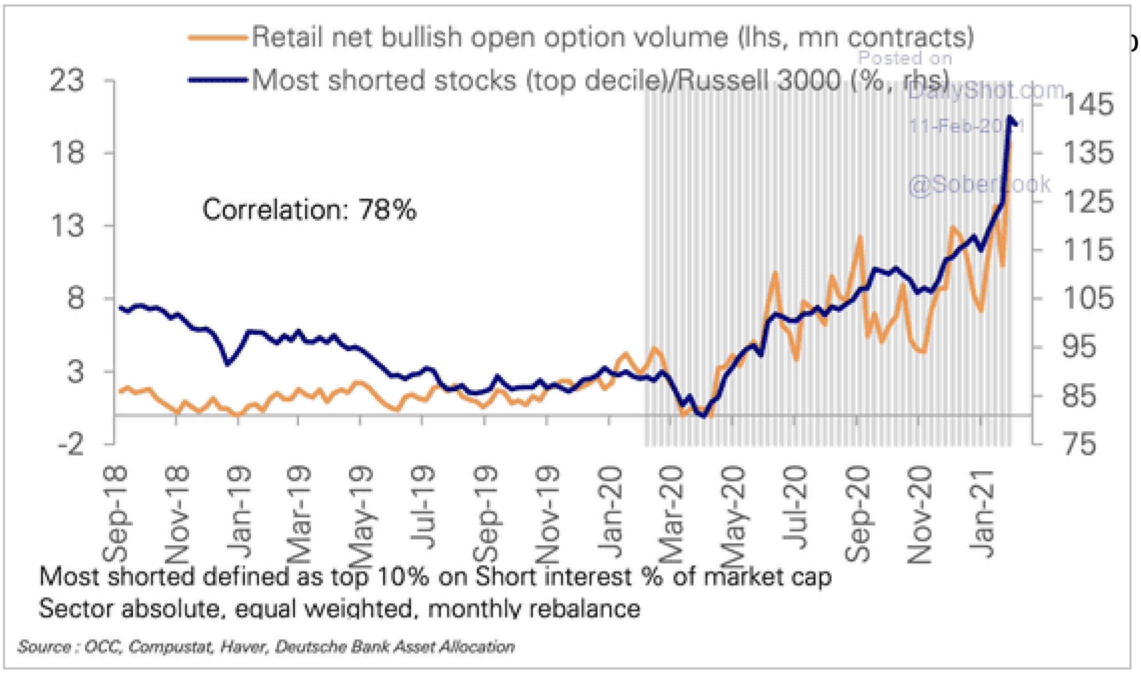


...d their sites away ...st itself into names

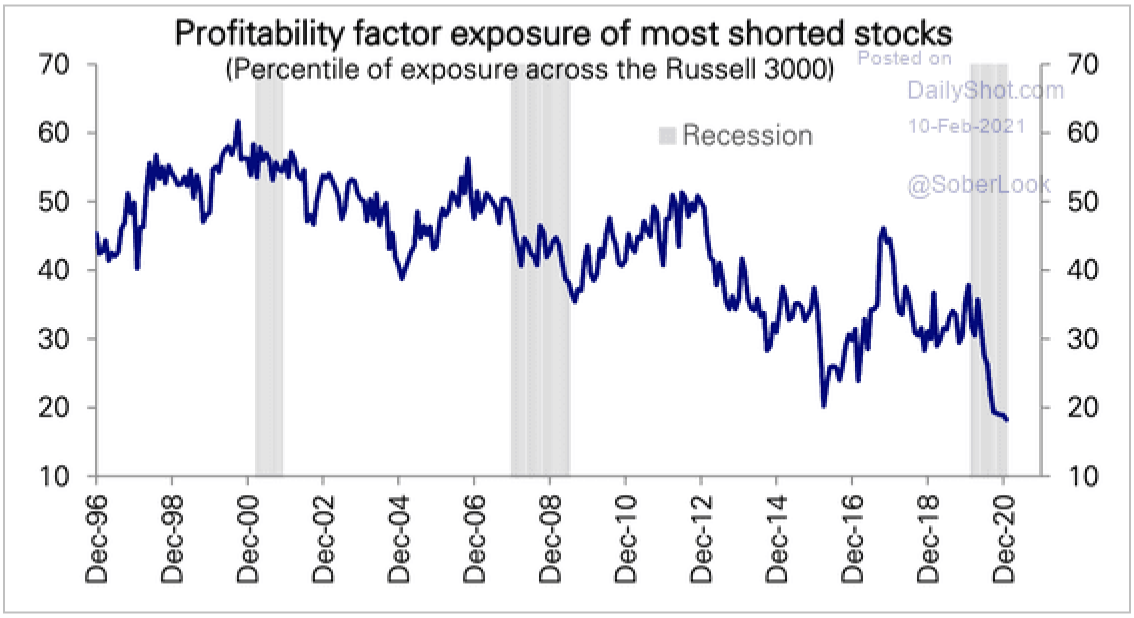
However, this time it looks like *"Reddit"* traders learned their lesson to *"get out early"* as the trade went *"up in smoke"* rather quickly.



rs continue to piling up on the

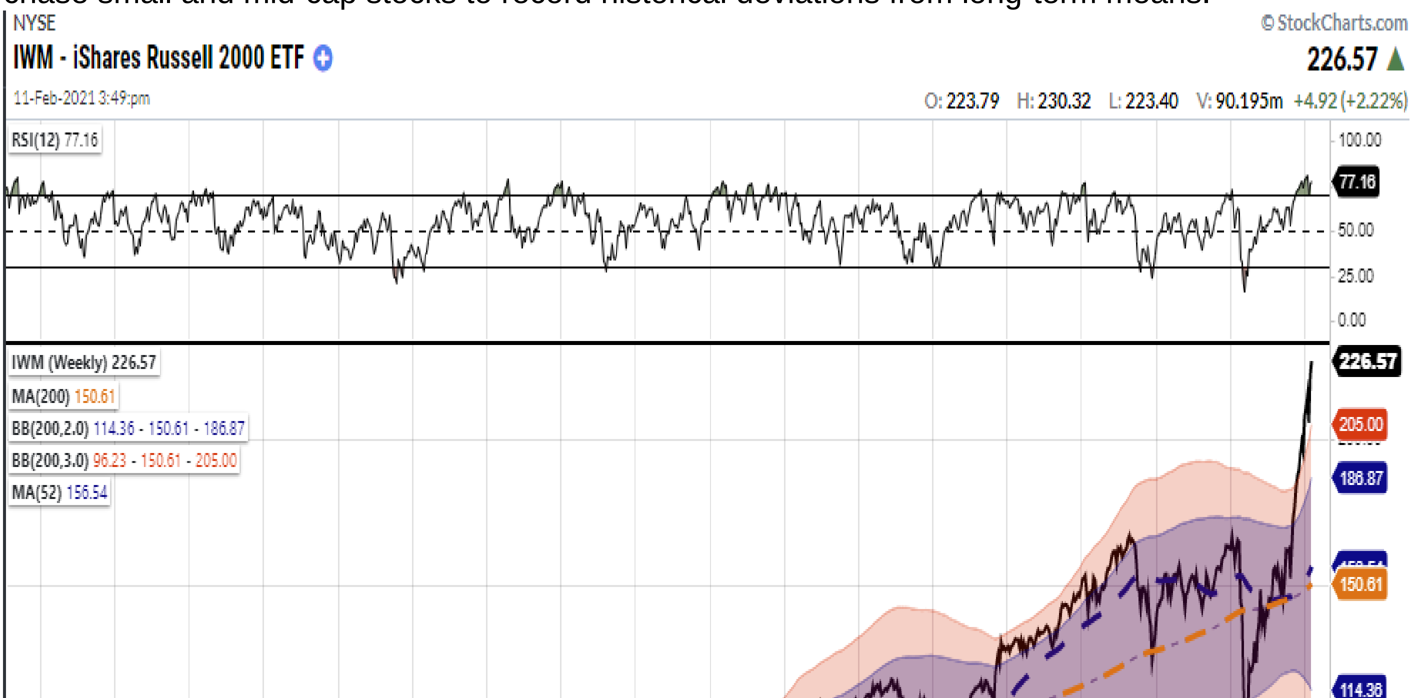


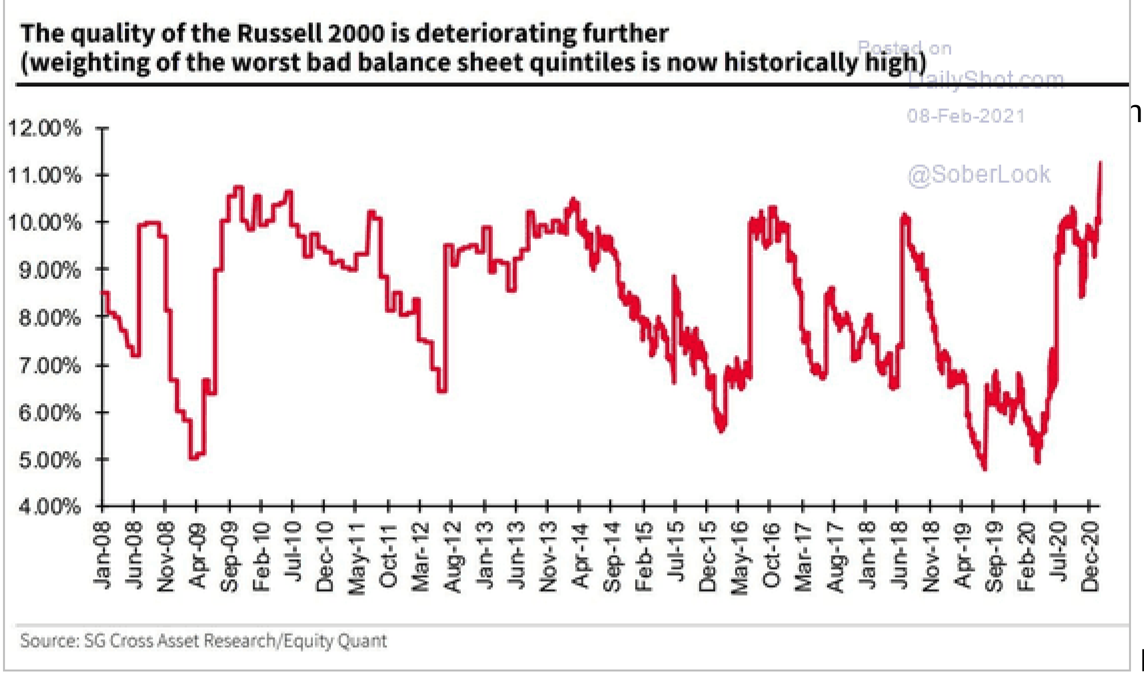
However, those



And as investors

chase small and mid-cap stocks to record historical deviations from long-term means.





ng the most.

But these are just

a view of the signs. I did a much more extensive review of the current speculation in [***"Is This The Biggest Bubble Ever?"***](https://www.youtube.com/watch?v=06AlnzePi0A) https://www.youtube.com/watch?v=06AlnzePi0A As my colleague Doug Kass noted previously:

> ***?It is growing increasingly clear to me that global stock markets are in the process of making a speculative move (driven by global liquidity) that may even compare to the advances that culminated in the seminal market tops in the Fall of 1987 and in the Spring of 2000. No longer is the market hostage to the real economy or sales and profit growth*** *? stuff I have spent four decades analyzing.* ***Instead, liquidity is seen as an overriding influence, actually it has become the sine quo non. As such, historical valuations become increasingly irrelevant, and price momentum is the lodestar.****?*

He is right. What could go wrong?

Two Important Threats

The question of what could wrong is extremely difficult to answer. **The reason is that historically, the thing the *"goes wrong,"* is almost always something no one is talking about.** In February 2020, estimates were for a raging bull market, and then the world was shut down by a pandemic.

> *"Stuff Happens," and always when we least expect.*

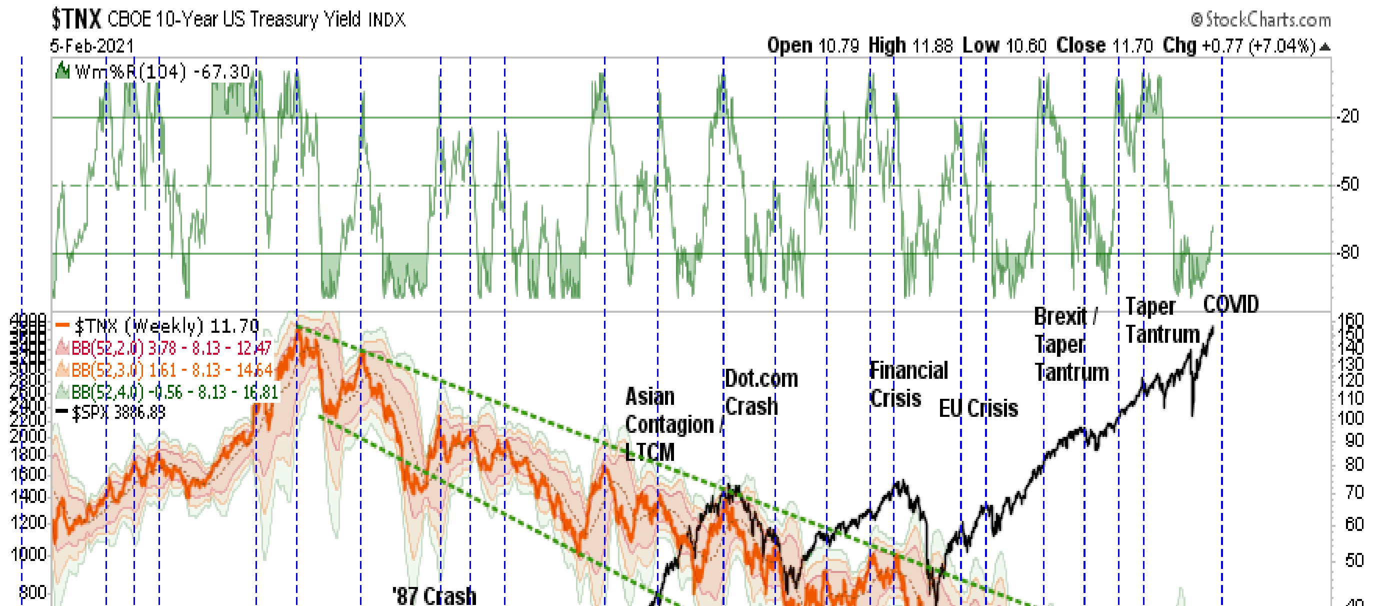
There are, however, two threats that could severely limit the market in the months and quarters ahead. **Inflation and Interest Rates.**

Interest Rates

With an economy pushing $85 trillion in debt, the entire premise of the *"consumption function,"* as well as *"valuation justification"* for the stock market, is based on low-interest rates. However, that is rapidly ending as the rise in rates is now approaching a "*danger zone"* for the markets. As noted by *SentimenTrader* on Thursday:

> *"The march higher in the yield on 10-year Treasury notes took a breather in recent days, but it's mostly been a steady rise for most of the last 6 months. So much so that the 1-year z-score, a measure of how unusual the move is relative to recent history, just reached 1.5 standard deviations for the 4th distinct time in the past decade."*

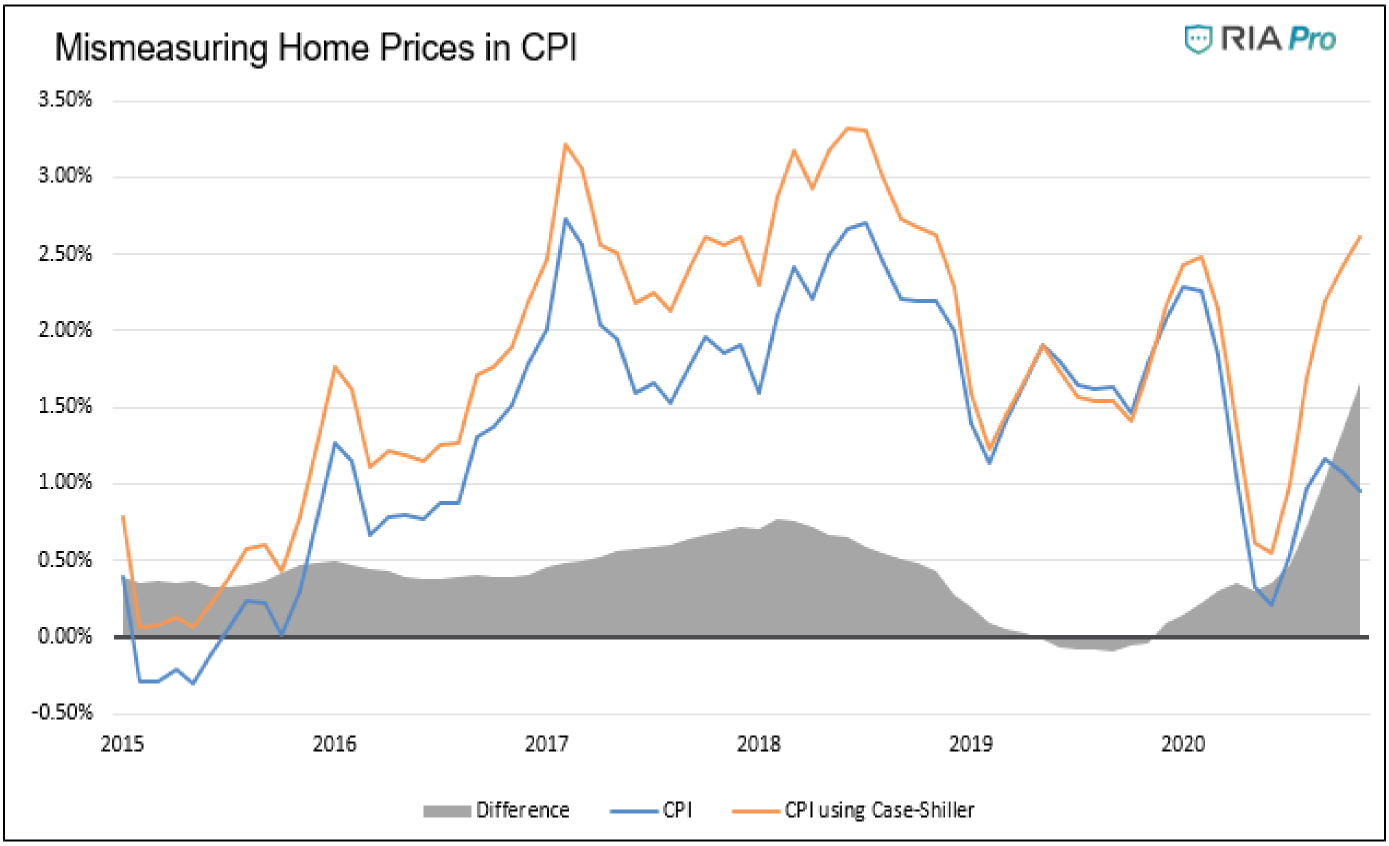
As discussed in ***"Dollar & Rates Issue A Warning,"*** interest rates are rapidly approaching the 1.5% to 2.0% barrier, where higher payments will collide with disposable income. Historically, such has not ended well for markets.



Inflation

The second threat is inflation. as noted by Michael Lebowitz for our ***RIAPRO Subscribers*** ***(30-day free trial.)***

> *"In February 2019 we wrote MMT and its Fictional Discipline. "In 1998, the Bureau of Labor Statistics (BLS) changed the way they calculated real estate prices within CPI. The BLS replaced an index based on actual home prices with what is now called owner?s equivalent rent (OER). OER is a rental equivalence that calculates the price at which an owned house would rent." Since 2019, OER has risen 5.12% while the Case-Shiller Home Price Index (CS) is up 13.73%. OER comprises nearly a quarter of the CPI calculation. The graph below replaces OER with the CS Index in the CPI calculation to show how inflation is understated due to the sharp divergence between actual home prices and the BLS flawed methodology to compute home prices. Per the graph, CPI would be 2.62% and rising, versus .96% and trending lower. The low CPI reading provides cover for the Fed to keep printing, but at what cost?"*



When it comes to the stock market, there is a decades-long correlation between interest rates and inflation. **More importantly, as with debt, consumers may handle higher prices or debt payments, but not both.** While investors may be able to justify higher inflation or rates in the short-term, it is unlikely they can justify both. **As inflation and rates slow economic growth due to the absorption of disposable income via higher prices and interest payments, the market will begin to reprice risk quickly.** Such could be a problem sooner than many think.

The Reason To Focus On Risk

During the past week, we made no substantive changes to our portfolios. It seems like a good time to review why we chose to *"focus on risk"* given the seeming *"insanity"* in the markets currently. **As investors, our job is to navigate the waters within which we currently sail, not the seas we think we will sail in later.** Higher returns are generated from the management of *?risks?* rather than the attempt to create returns by chasing markets. That philosophy got well defined by Robert Rubin, former Secretary of the Treasury when he said;

> *?As I think back over the years, I have been guided by four principles for decision making.* ***First, the only certainty is that there is no certainty. Second, every decision, as a consequence, is a matter of weighing probabilities. Third, despite uncertainty, we must decide and we must act. And lastly, we need to judge decisions not only on the results, but on how they were made.*** *Most people are in denial about uncertainty. They assume they?re lucky, and that the unpredictable can be reliably forecast. This keeps business brisk for palm readers, psychics, and stockbrokers, but it?s a terrible way to deal with uncertainty.* ***If there are no absolutes, then all decisions become matters of judging the probability of different outcomes, and the costs and benefits of each. Then, on that basis, you can make a good decision.?***

A Simple Philosophy

It should be evident that an honest assessment of uncertainty leads to better decisions, but the benefits of Rubin?s approach, and mine, goes beyond that. **For starters, although it may seem contradictory, embracing uncertainty reduces risk while denial increases it.** Another benefit of acknowledged uncertainty is **it keeps you honest.**

> *?A healthy respect for uncertainty and focus on probability drives you never to be satisfied with your conclusions. It keeps you moving forward to seek out more information,* ***to question conventional thinking*** *and to continually refine your judgments and understanding that difference between certainty and likelihood can make all the difference.?*

We must recognize and be responsive to changes in underlying market dynamics if they change for the worse and be aware of the inherent risks in portfolio allocation models. **The reality is that we can?t control outcomes. The most we can do is influence the probability of specific outcomes, which is why the day-to-day management of risks and investing based on probabilities rather than possibilities is essential to capital preservation and investment success.** It is just something to consider.

The MacroView

#MacroView: Why Stimulus Doesn’t Lead To Organic Growth

Written by Lance Roberts | Feb 12, 2021

If you need help or have questions, we are always glad to help. ***Just email me.*** See You Next Week **By Lance Roberts, CIO**

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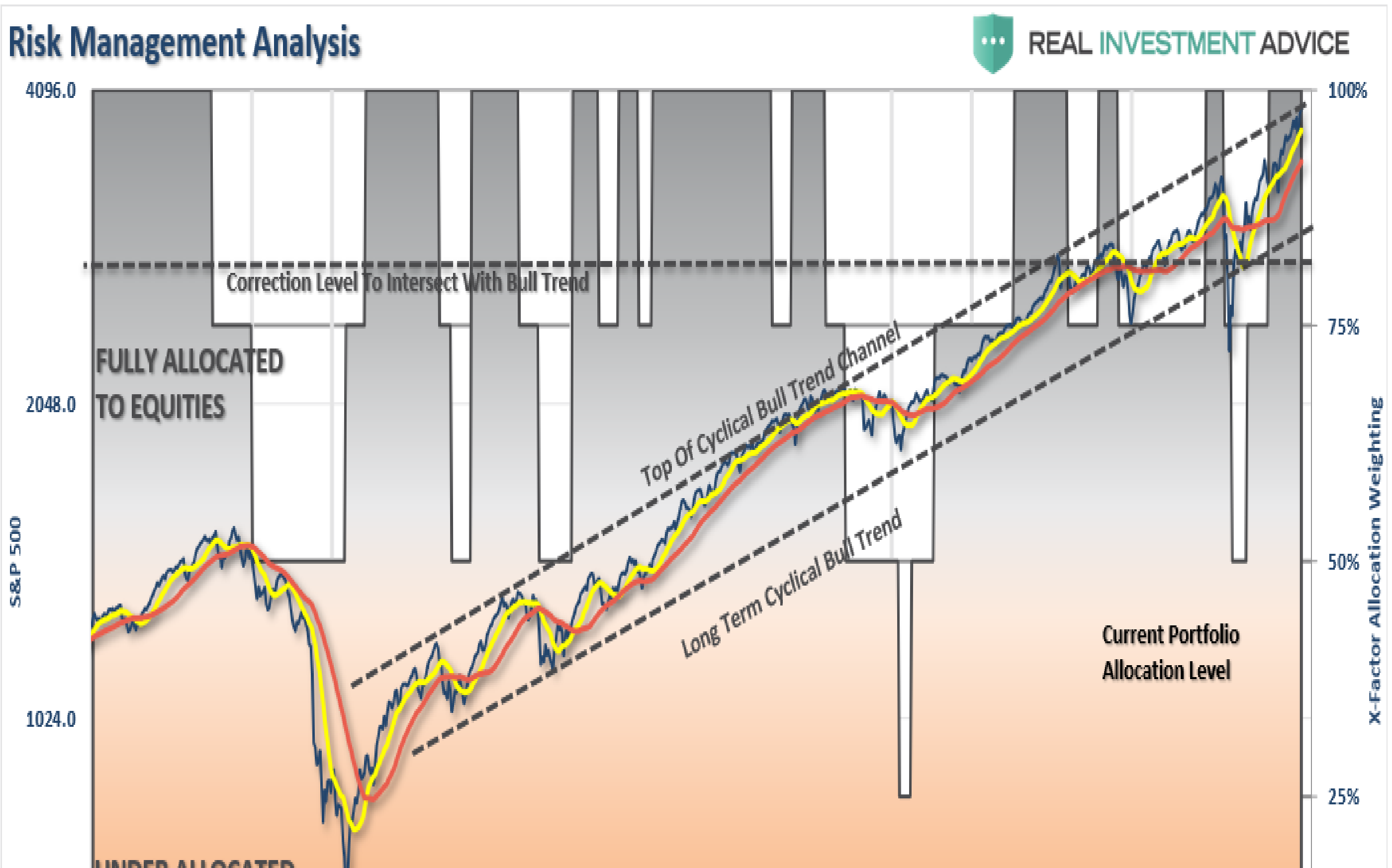
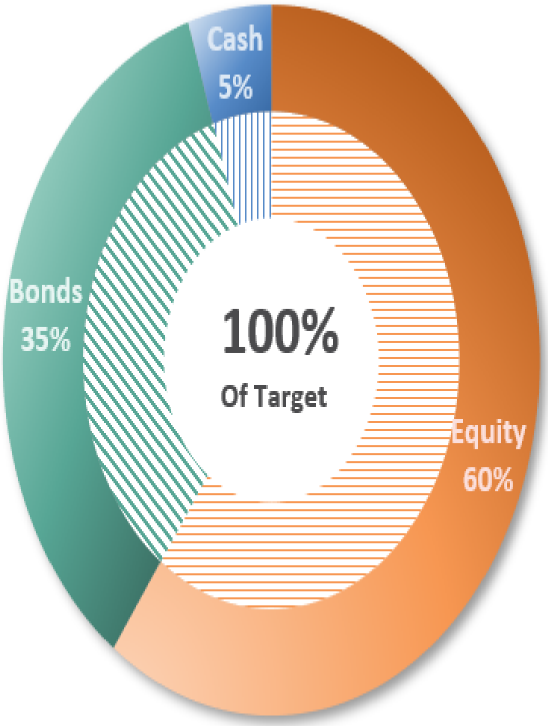
THE REAL 401k PLAN MANAGER

A Conservative Strategy For Long-Term Investors



Current Portfolio Weighting



Current 401k Allocation Model

5.00% **Cash + All Future Contributions**

Primary concern is the protection of investment capital

Examples: Stable Value, Money Market, Retirement Reserves

35.00% **Fixed Income (Bonds)**

Bond Funds reflect the direction of interest rates

Examples: Short Duration, Total Return and Real Return Funds

60.00% **Equity (Stocks)**

The vast majority of funds track an index.
Therefore, select on ONE fund from each category.
Keep it Simple.

20% Equity Income, Balanced or Conservative Allocation
30% Large Cap Growth (S&P 500 Index)
5% International
5% Mid-Cap

Portfolio Instructions:

Allocation Level To Equities	Recommendation	When To Take Action
Less Than Target Allocation	Hold Current Exposure	Hold Exposure
Equal To Target Allocation	Hold Current Exposure	Hold Exposure
Over Target Allocation	Hold Current Exposure	Hold Exposure

Commentary

This past week, the market struggled to gain ground as the overbought conditions begin to apply a *"gravitational force."*

Currently, all of our indicators remain positive, with money flows currently suggesting there is support for prices at current levels. However, those money flows are showing some signs of weakness which suggests that in the near future, the next few weeks, we will see a correction in the market similar to what we saw at the end of January or potentially more.

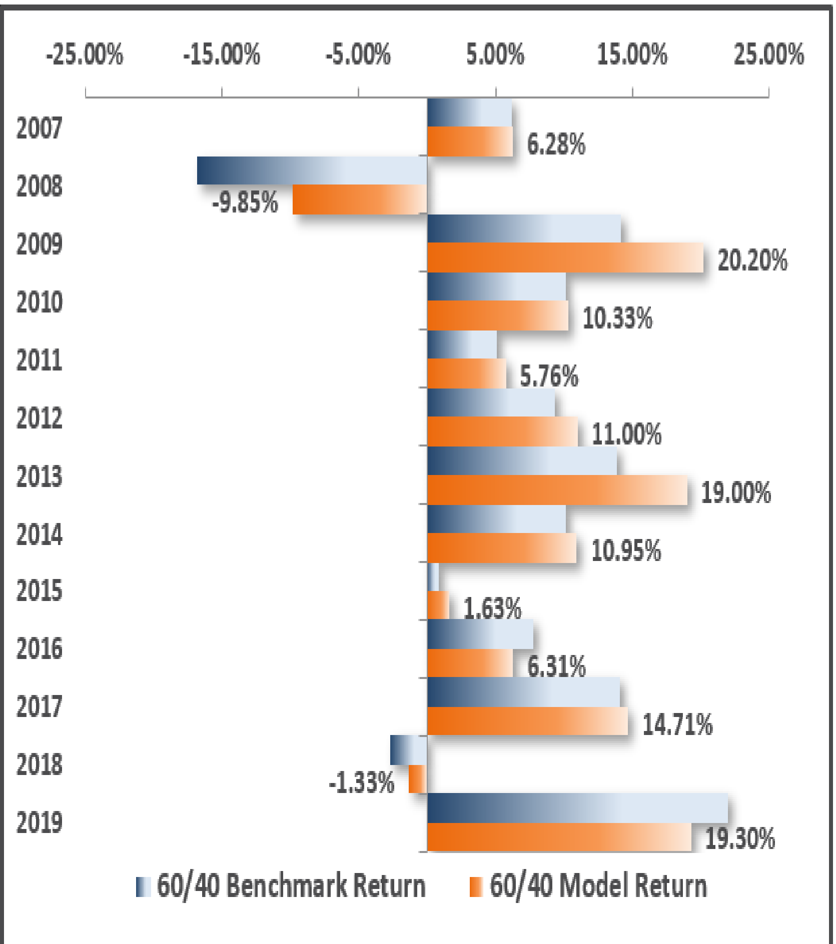
There is a lot of risk built up in the market currently, but there is also no immediate trigger to cause a reversion so there is no need to become overly cautious at the moment.

Maintain exposures, but rebalance positions that have grown to outsize weightings in portfolio. Particularly in small/mid cap and international funds which are eggregiously overbought.

If you need help after reading the alert, do not hesitate to [contact me](#).

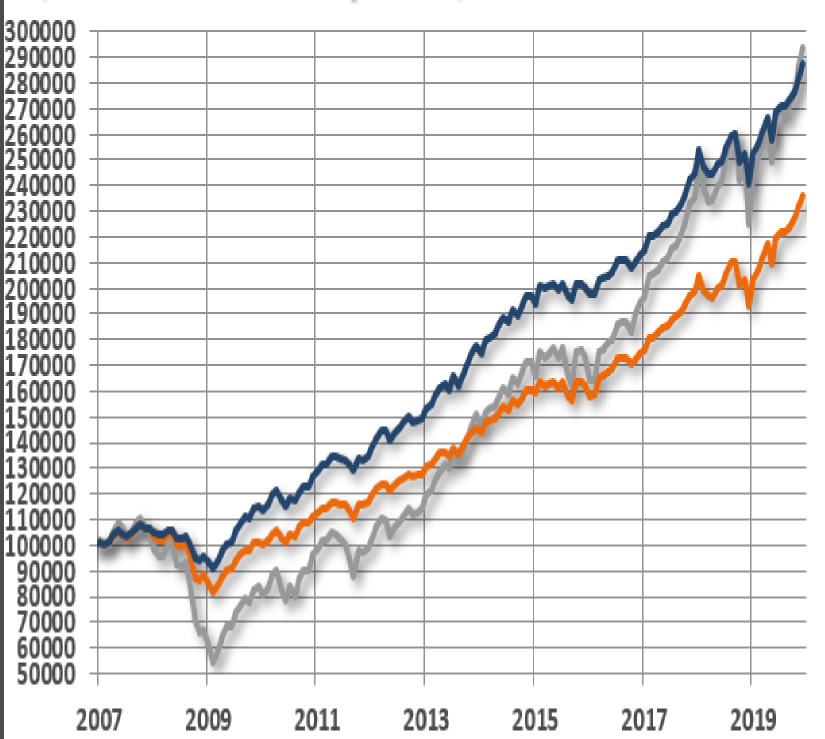
Model performance is a two-asset model of stocks and bonds relative to the weighting changes made each week in the newsletter. Such is strictly for informational and educational purposes only, and one should not rely on it for any reason. Past performance is not a guarantee of future results. Use at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

60/40 Benchmark vs. Risk Adjusted 60/40 Allocation



401k Plan Manager Live Model

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