

Is The Market Turning?

Since the “blow-out” in 2013 - the bull market that caught many money managers unaware - the U.S. stock market has essentially gone nowhere since year end. The S&P 500 was down -3.6% in January, up +4.3% in February, and up +0.69% in March. In fact all of the major indexes (the Dow, S&P 500, and NASDAQ) are, for the most part, flat or up marginally year-to-date, with no real progress in either direction.

Is the global market uptrend sustainable or is it now giving way to a cyclical bear market? There is still insufficient evidence to answer the question conclusively. But the warning signs have increased.

Warning signs...

According to the Shiller CAPE P/E ratio, the S&P 500 is overvalued by 53%. Investor participation is at levels not seen since 2007, and margin debt is at an all-time record high. Additionally, historical market patterns and cycles indicate an unfavorable risk-versus-reward:

- **Market Cycles** The current bull market is now at 60 months, old by historic standards. Depending on how one measures, the average length of a bull market over the last 113 years was 53 months, with very few lasting longer than the average. *
- **Presidential Election Cycle** We are in the 2nd year of the Four Year Presidential Cycle, and over the last 80 years the average decline in the 2nd year was 21%. *

While the current market breadth is still positive on balance, the majority of our global indicators peaked last year and have been reaching lower highs. This is typically not indicative of a robust bull market.

The main driving force of the current bull market has been the Fed’s Quantitative Easing (QE) stimulus program. However, on December 18, 2013, the Fed announced that it would begin to taper its asset purchase program by \$10 billion per month beginning in January 2014. Purchases are currently at \$55 billion a month, down from \$85 billion in December, and will be cut to \$45 billion soon (in April). And according to Janet Yellen’s testimony a couple of weeks ago, the taper will likely continue into year end, with rates possibly moving up in 2015. A rising interest rate environment, if not managed well, may create headwinds for the market...and the economy.

On the plus side...

Company earnings cycle was at a crossroads last year - the Earnings Per Share (EPS) growth for the S&P 500 slowed from over 30% in Q1 of 2011 to -0.9% in Q1 2013. Since World War II, this type of earnings deceleration has occurred only 14 times. In eight cases, recessions followed, with dire implications for stocks. In the six other cases, earnings reaccelerated, reflecting a stable economic environment and providing bullish conditions for stocks.

Thanks to higher sales growth and higher margins, earnings reaccelerated in the subsequent three quarters, with the stock market moving up strongly into year-end. Although an external shock could derail the global economy, we believe that earnings will likely continue to grow, albeit at a modest pace.

* Sy Harding, Street Smart Report

OUR CORE TENETS

Be Intentional, Be Informed

We encourage individuals to be intentional about their live choices... and informed about their money.

Manage Risk

We seek to keep portfolios in-tune with the risk/reward of the *current* market environment.

Own The Best, Ignore The Rest

We strive to keep client portfolios focused squarely on the market’s leadership.



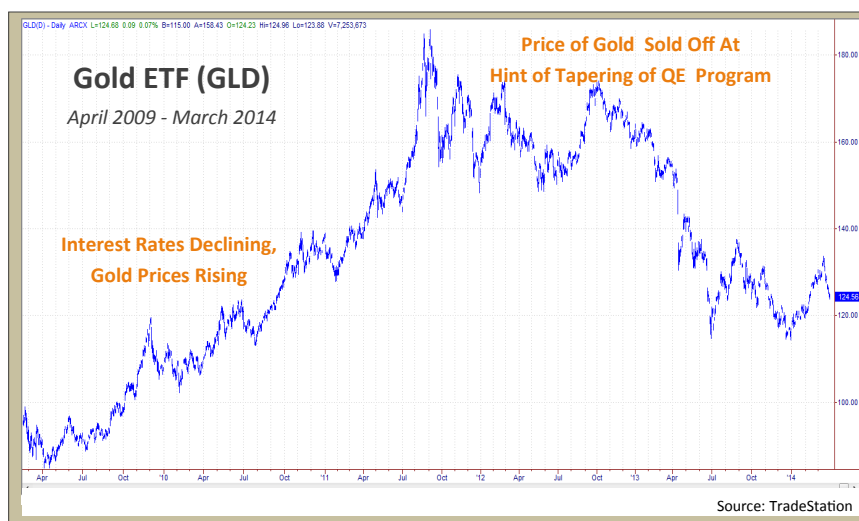
ALEXIS
ADVISORS

What about “safe haven” assets?

Many ascribe to a traditional asset allocation approach - taking a longer view to “buying and holding” a set allocation to stocks, bonds and alternative assets, such as gold. This approach can have a place, particularly when interest rates are declining. However, bond and gold prices are typically linked to interest rate trends. With the Fed having started to taper its QE program, and contemplating raising interest rates in 2015, it may be worth considering taking a more tactical, active view to these two asset classes.

Bonds and gold are often considered “safe haven” assets, typically performing well when stocks are declining. In today’s interest rate environment, it maybe worth considering that there may be times to “hold ‘em,” and times to “fold ‘em.”

- **Hold ‘Em** If the economy begins to show significant signs of inflation and there is a larger cut in the Fed’s bond-buying program, as mentioned, the stock market may run into trouble. This would likely usher in another round of global uncertainty - and as such, we may see temporary buying of safe haven assets.
- **Fold ‘Em** However, if the economy continues to chug along and the current trend remains intact with the Fed gradually continuing its taper program, we may to see more selling of both bonds and gold.



Wrap Up...

The stock market can always become more over-valued and remain extended for a long time before reality sets in. And market tops are typically slow in forming. While we believe that the stock market continues to be due for a breather, in reality, this is just “a view” ... and there are many conflicting perspectives out there:

- **Hedge Fund Billionaire Seth Klarman** Klarman recently returned \$4 billion to his investors because he can’t find anything he’s comfortable buying, apparently willing to give up the fees rather than take the risk.
- **Jim Paulson, Wells Capital Management** *“We’re going to come to a wider acceptance that there is pretty good economic momentum here. Good economic news will be good news for stocks.”*

If the economy continues to gradually improve, an incremental taper will likely not destabilize the stock market, but if inflation picks up, and the Fed believes it needs to act more aggressively, this may be the impetus for a market decline. Our strategy is to *maintain that we are in a bull market until proven otherwise*, and to keep our eyes squarely focused on our quantitative models. The models help us stay focused on what the current price action *is doing*, rather than what we think it should be doing. With that in mind, we will not leave before the party is over, but along the way, will likely raise or maintain a cash position, patiently waiting for cheaper prices.

Join The Conversation

www.alexisadvisors.com

Information contained herein is for informational purposes only and is subject to various interpretations and time-frames, and should not be considered investment advice. Advice may only be provided after entering into an advisory agreement with Alexis Advisors, LLC (“Advisor”). Advisor does not assume any legal liability or responsibility for any incorrect, misleading or altered information contained herein. Past performance is not indicative of future results while changes in any assumptions may have a material effect on projected results. Advisors, LLC is a Registered Investment Advisor with the Commonwealth of Virginia.

Third Party Research Disclaimer: Third party research is provided for information purposes only and has not been prepared by Alexis Advisors, LLC. The information contained herein is based upon sources which we believe to be reliable, but no representation, express or implied, is made with respect to the accuracy, completeness or reliability of the information or opinions in the reports.