Bear-o-meter remains neutral despite investor sentiment getting risky

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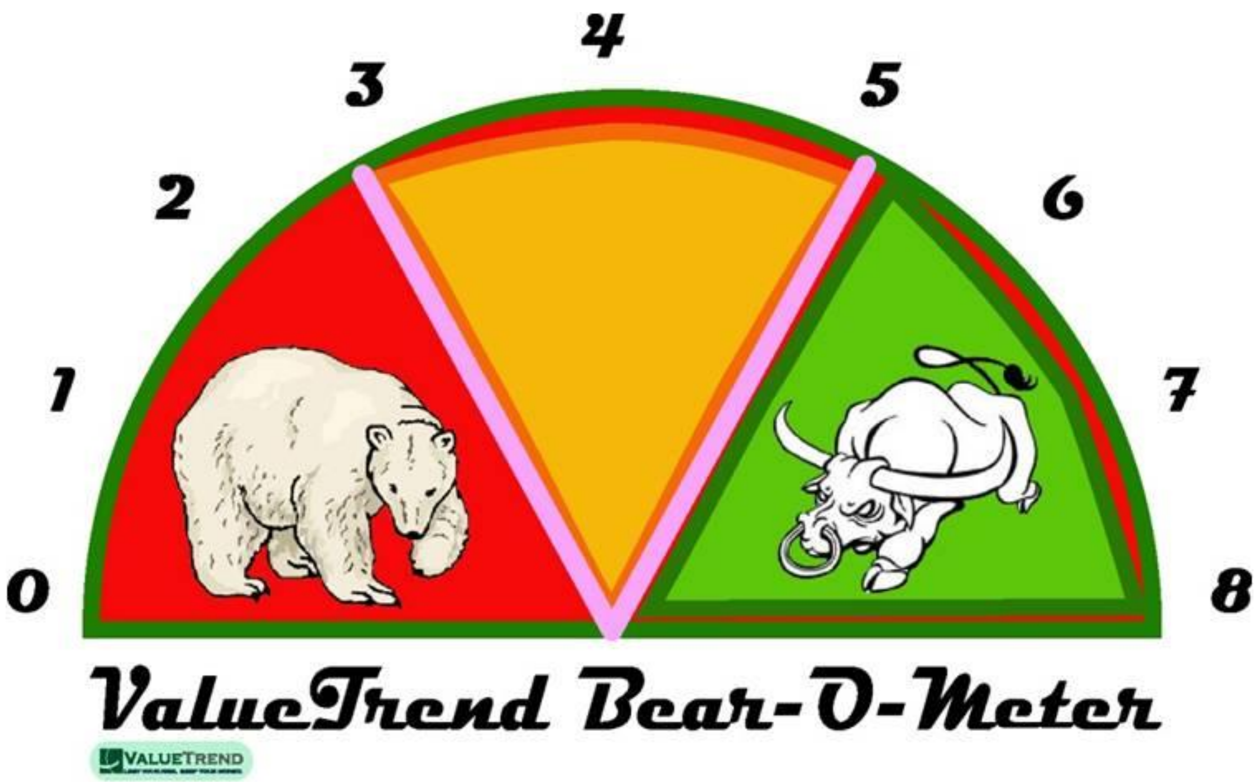
As y'all know, I post a reading of the Bear-o-meter on this blog at the start of each month. The Bear-o-meter is a relative risk/reward reading of the market. Some interesting changes happened this month, despite the net-net reading of the meter remaining the same over last month. Today, I'd like to break down the components of the Bear-o-meter to give you a better understanding of the market's health under the categories that make up this indicator. BTW– if you'd like to construct the Bear-o-meter yourself, refer to my book "Smart Money Dumb Money" for the instructions on how to do so.



OK – to get started – this month's reading was "4" – which, as the diagram above indicates, is smack-dab in the middle of the risk/reward range. LAst month the meter also read "4". And yet, some factors have changed. Lets take a look:

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Breadth: I use the Advance Decline line and the Dow INDU/TRAN confirmation rule in the meter to measure market breadth. This month, market breadth remained at the same healthy level as was seen in October. No change to the points

Value: The training PE ratio for the SPX is measured as a basic measurement of market value. This month, it dropped from 34 to 29 which keeps it neutral. Still, its not a cheap market. No change to the points.

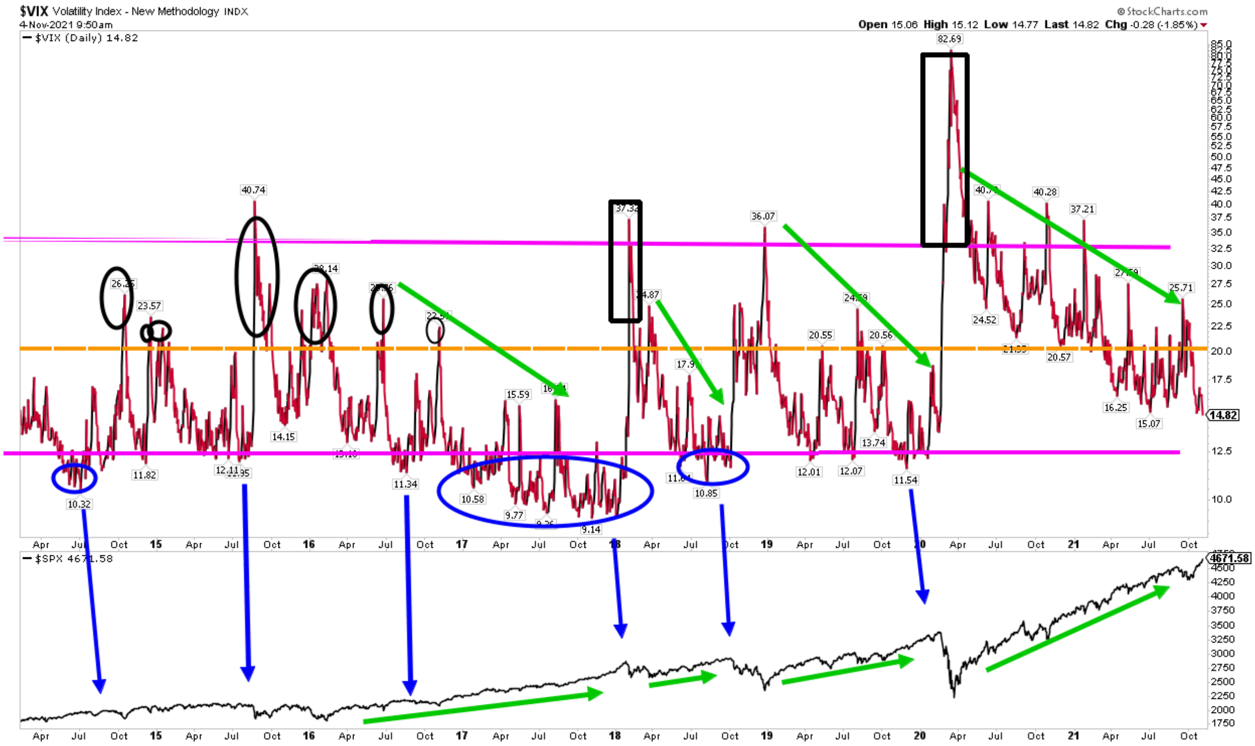
Trend: The trend remains bullish for the SPX, as indicated by the 50 and 200 day SMA's. Of note, the market was below its 50 day average in October, so a point was awarded this month when it moved back over that indicator.

Seasonality: Market Seasonality moves from neutral to bullish in November. The Bear-o-meter added 2 full points for the change in the calendar.

Breadth-momentum: I look at the % of stocks over their 50 day SMA's and the NYSE New high/new low indicators for an indication of market balance. if there are "too many" SPX stocks moving ahead of their 50-day average and if there are "too many" stocks on the broader NYSE making new highs, this can be a sign of an overheated market. Both read neutral this month, as they did last month. No change to the points.

Sentiment: Sentiment is a contrarian way of looking at the market. Too many bulls is a bad thing – especially if the bulls reside amongst retail investors. This month, the Smart/Dumb Money spread (Sentimentrader.com) went into bearish territory. Two points were subtracted from the meter. Meanwhile, the VIX moved lower, although not below its "trigger point. This is something to keep an eye on.

Typically, when the VIX moves below 12, its a sign of irrational exuberance. Its at 15 now. That's low. For perspective, a month ago, it was around 25, and a year ago, it was playing with 40. Please also note the trend (green arrows) on the chart below. You will note that if this trend persists, and leads the VIX into the 12-or-lower zone, we have historical evidence to suggest that the market will correct on that event. At this time, it is not there.



Conclusion

Despite growing risk from a sentiment point of view, the market is indicating good breadth and a sustainable trend. Sentiment is not a coincidental indicator for the market. It is a leading indicator. If market sentiment grows too much more optimistic, the market could be in for a sharp correction. For now, its best to stay invested with an eye on the ball for changing conditions.

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