Bear-o-meter pulls a “180”

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In the military, if you are instructed to turn and face the opposite direction, its called an “about face”. In non-military terms, we sometimes call changing our minds, or moving in the opposite direction “pulling a 180” – meaning to turn 180 degrees and move in the opposite direction. For the first time since April 7th of 2022 – the ValueTrend Bear-o-meter has pulled a 180. It’s moved firmly into the “bullish” zone. We’ll discuss that today, including how we anticipate trading in the near future.

When I issued the “High Risk Alert” back in April 2022, the SPX sat around 4600. This after retreating from its all time high of 4800 in January. Typically, points-based collection of indicators like the Bear-o-meter will lead or lag market tops and bottoms by a few months. After all, it incorporates numerous indictors under 5 broad categories of trend, sentiment, breadth, valuation, seasonality into one reading. All of these factors operate within different time frames (leading, coincidental, and lagging market performance). The Bear-o-meter provides a general risk/reward reading of the market within a multi-factor view – its very nature is not that of precision – but its still been a darned good tool when combined with trend analysis. Readers who paid attention to that warning, along with the trend alert (lower-low on the SPX) profited by moving into cash, value, and low beta as I discussed at the time. The SPX moved to 3500 within 6 months of the warning.

Today, I read the Bear-o-meter for my monthly update. In early January, the Bear-o-meter was firmly entrenched in its High-Risk zone. As noted, this compilation is NOT a coincident indicator designed to pick peaks and troughs. Its designed to view relative risk, and won’t move into a new zone until the weighting of ALL 5 factors are, in balance, leaning in a new direction. That takes a little time. Now, its pulled a 180. The Bear-o-meter has moved from “0” last month (where its hovered since April 2022) to 6! The illustration below shows you that its gone from High Risk to the first level within the Bullish category. Quite a move! Like a fast car – doing zero to 60 in record time…I’ll cover the reasons for the change below.

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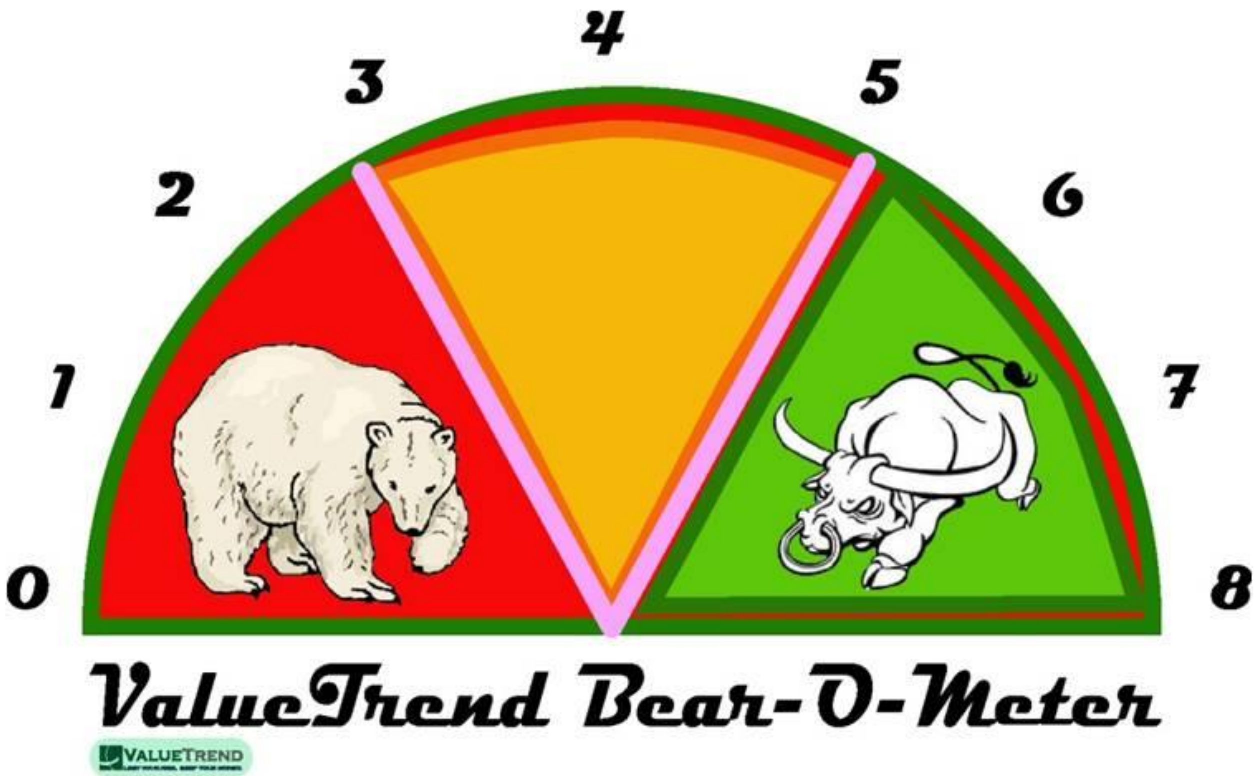
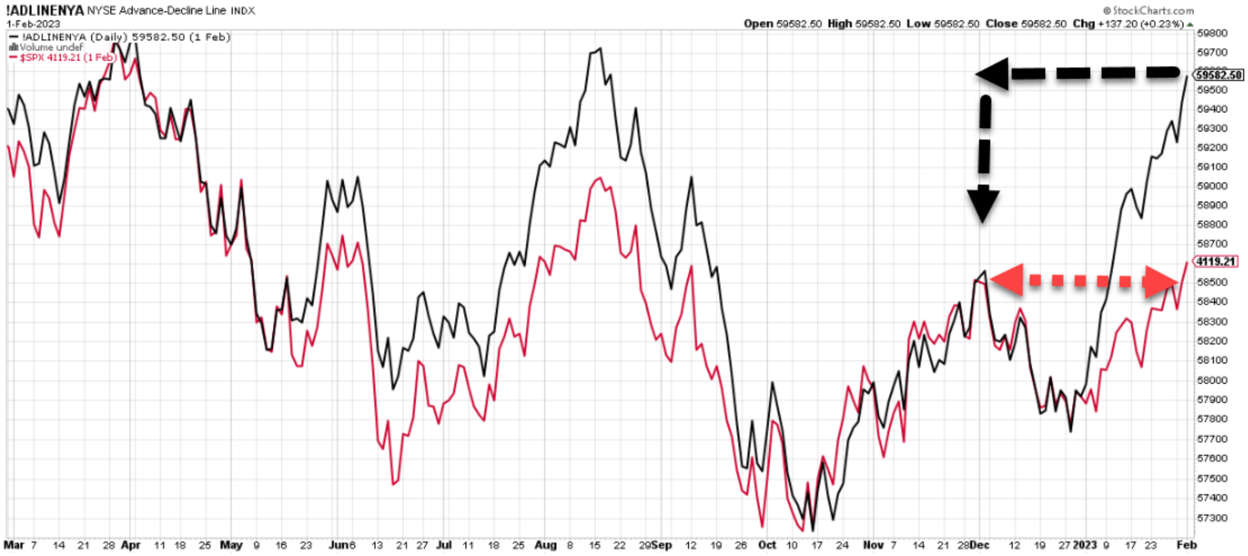
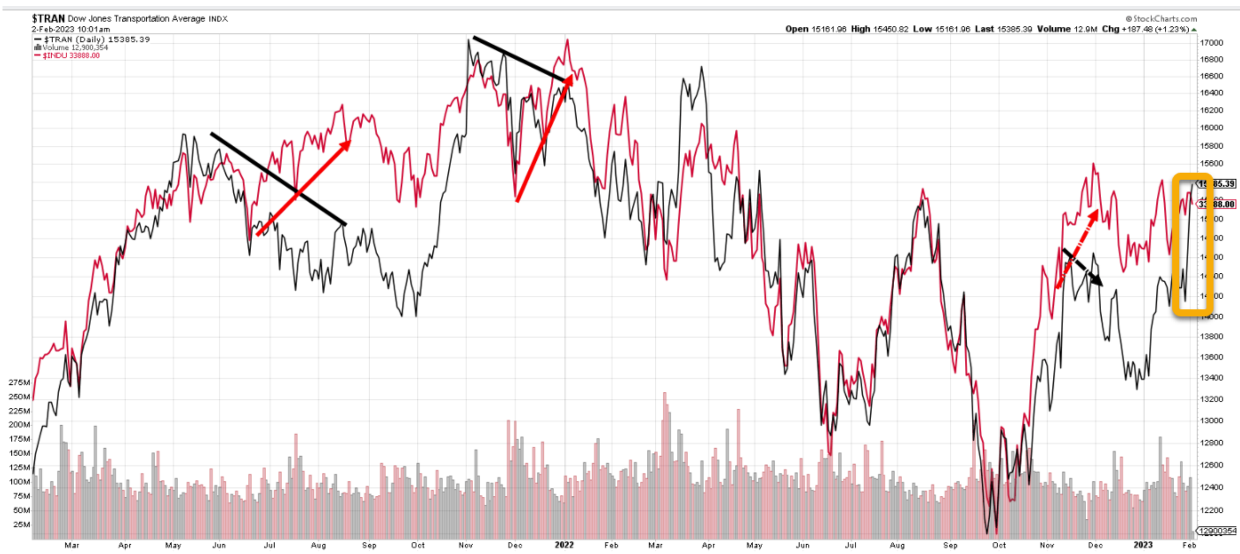


Breadth

A major contributor to the higher reading in the Bear-o-meter was market breadth. Breadth means broad participation. I look at many indicators which include % of stocks over their SMA's, New High/Lows, cumulative breadth and comparative sector breadth. Most of the breadth momentum indicators like New High/Lows, and % over SMA's were flat vs last month. But new positive points were scored in the A/D line (cumulative breadth) and the Dow Industrials vs. Transports pickup. Check the massive jump on the NYSE A/D line (black) vs the SPX (red). Positive divergence.



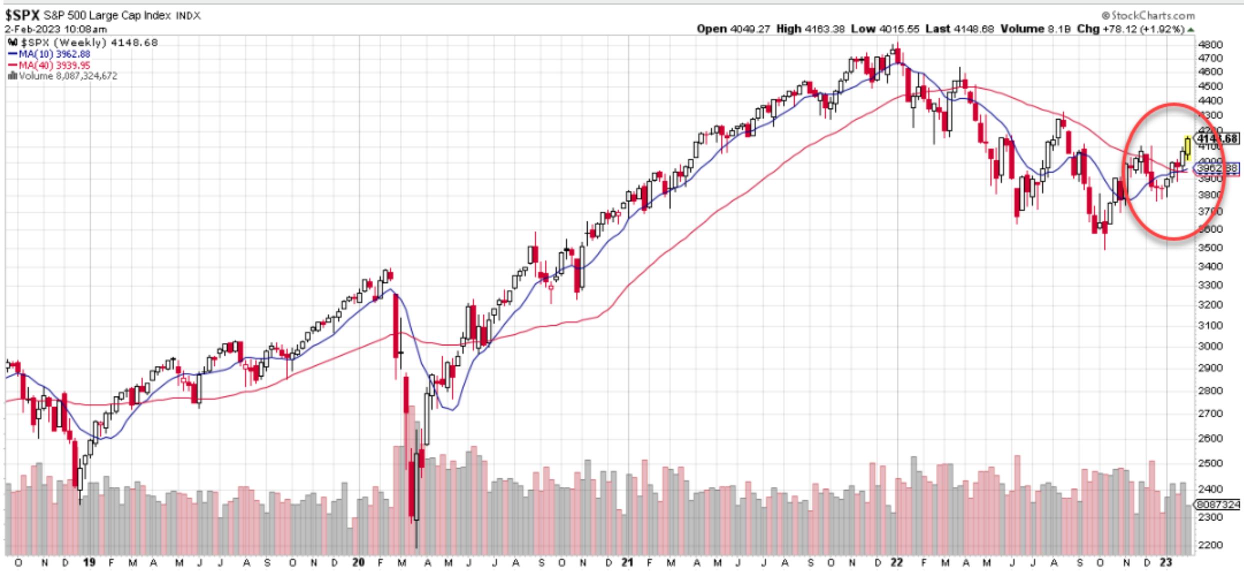
Check the massive move by the transports (black line) vs the Industrials (red line). Positive divergence.



Trend

To start – please note that yesterday's bullish breakout of the SPX resistance point of 4100 is VERY encouraging. Having said that, we still need a bit of time for that level to hold. I need to adhere to my absolute minimum of 3 days before starting to leg back into the market. That has yet to prove true. Still – good news for the bulls, so far.

Adding to the good news are positive signals given by the 200 day (40 week) SMA and the 50 day (10 week) SMA. The SPX has broken through both of these averages, adding 2 positive points to the Bear-o-meter.



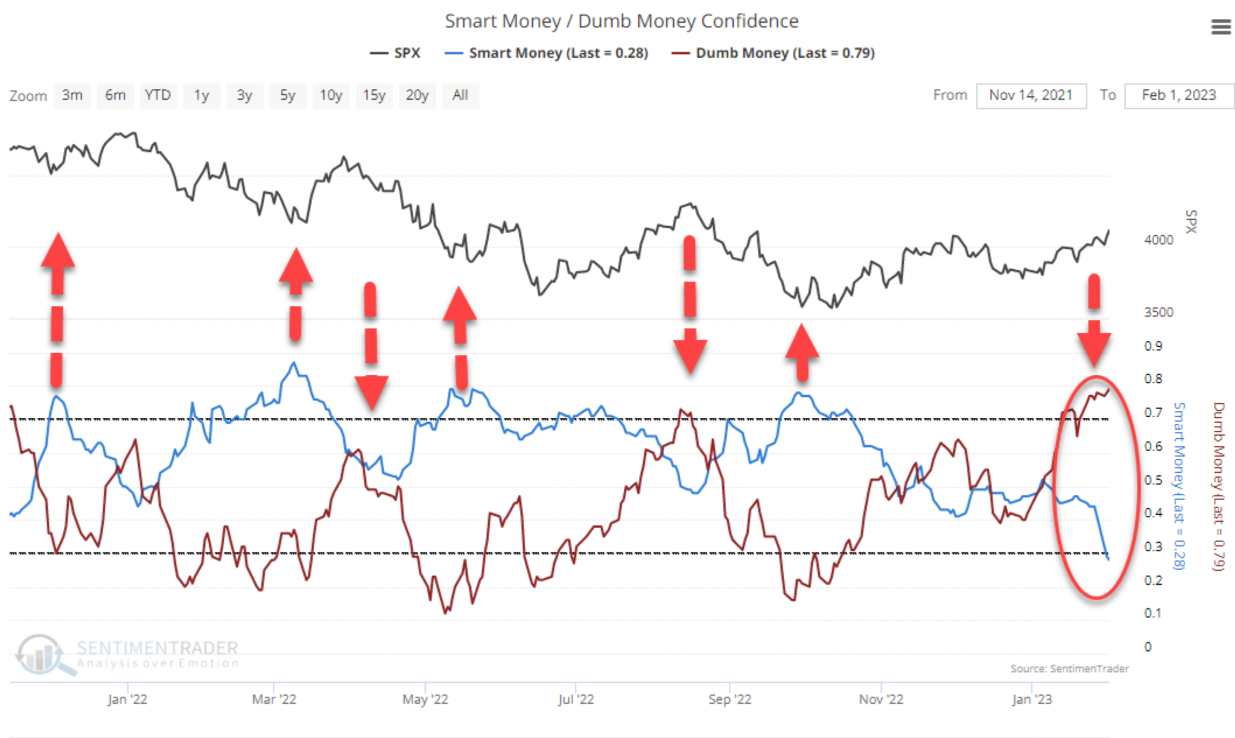
Sentiment

Investor optimism – as quantified by the various sentiment indicators I follow – is largely high. The crux with these indicators is – are investors "too" optimistic? Well, so far, the enthusiasm is certainly approaching the high end of the spectrum. For example, the VIX, sitting near 18, is low. But not "too low/ too optimistic". Same with the Put/Call ratio. Both show a certain level of investor complacency – but its not extreme.

However, one sentiment indictor, which admittedly can be a mid-termed leading indicator (aka the signals are not likely going to spell an imediate move for the market) is bearish. That's the Smart Money/Dumb Money spread. Its well into the "Dumb Money happy, Smart Money Worried" zone. Historically, if the Dummies (retail investors) keep buying and the Smarties (commercial hedgers, pension managers, pro traders, etc) keep selling, you are setting up for a correction. Again, though, this condition can last a while before anything actually happens.

The Smart/Dumb chart is below for January 2022 to current. Note that since the bear began, the Smarties (blue line) have called the market troughs – noted by the "up" arrows. When they got bullish it coincided with opportunistic trades. Note that the Dummies fell in love with the market in August – you will recall my comments noting this head-fake. When the Dummies were buying the Smarties were selling – note the "down" arrows.

The big deal now is that we have not had a big move DOWN in Smart Money confidence since the bear began. Meanwhile, the Dumb Money confidence is the highest its been. I think this is an important factor to consider when determining just how bullish we should be at this time.



Conclusion

If you get the ValueTrend Update newsletter, you will have read our latest edition entitled "Rules are rules". Subscribe here if you don't already.

ValueTrend adheres to rules. They enabled us to perform well in this and past bear markets. The tradeoff with such rules is that you cannot sell at the top, nor buy at the bottom. Systematic rules are not tools of clairvoyance, enabling you to identify precise timing opportunities. They are designed to help us discover the least risk opportunities, and avoid the highest risk scenarios. I encourage you to take the Online Technical Analysis Course to learn my system. For less than $400 it can help you make more profitable decisions, and save many thousands of dollars in mistakes. Cheap insurance.

Anyhow – our rules say that we must start to leg into the market if the SPX continues to hold its 4100 breakout for 3 + days. Assuming it does, the Bear-o-meter backs that decision with a positive risk/reward profile. Yet, sentiment is signaling a potential correction. So we won't be jumping in with our cash all at once – again, assuming SPX 4100 holds into next week. But - rules are rules! And as I always like to say…"A system will save you from yourself"

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