BALDINI INVESTMENT STRATEGIES

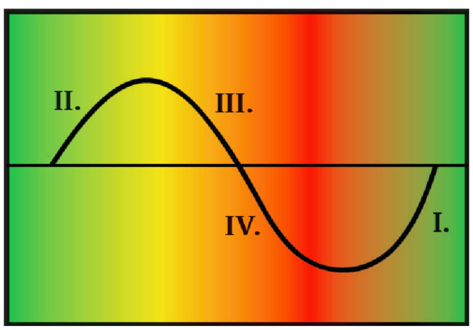
September 2020

# Month in Review

The S&P 500 gained 7% in August as frenetic call buying in big technology stocks created a positive feedback loop driving prices higher. Call buying is a speculative bet on rising stock prices and a contrarian sell signal at extremes. Corporate executives took the other side of the trade and sold the largest amount of their own company's stock since November 2015. The economic fundamentals underpinning the rally remain strong but with the election fast approaching and the market priced for perfection it may take a breather. It's time to check our indicators to see how this spurt to new highs has affected them. I have also provided a brief summary of my thoughts on the market going forward.

## I. CREDIT CYCLE

### PHASE I: EARLY EXPANSION




The credit bull market marches on but a negative divergence seems to be developing between the credit markets and the stock market. A negative divergence occurs when two or more indicators or indexes fail to show confirming trends. In this case, the S&P 500 Index has exceeded the June high but the Corporate High Yield Bond Index has not. The same thing occurred at the top in February and could be a sign that stocks are pricing in an increasingly rosy scenario that the credit markets aren't seeing. What is different today is that trillions of dollars in global liquidity have been created since March and continue to support asset markets. With a new credit cycle firmly in place, any short-term bouts of volatility are likely to be short-lived.

## II. RISK MANAGEMENT MODEL (RMM) RISK LEVEL

*LOW* *GUARDED* *ELEVATED* *HIGH* *SEVERE*

### US STOCKS: LOW

The Risk Level for **US STOCKS** is **LOW** for large company stocks and **GUARDED** for small and mid-sized ones. The outperformance of multinational, mega-cap corporations is an ongoing theme that has been playing out for years. Small and mid-cap companies need pricing power to grow and struggle in a low- growth, disinflationary environment. Their day in the sun may yet come, however, as Fed Chairman Jerome Powell just announced a new strategy to allow inflation to run above their 2% target to "make up" for periods when inflation has run below it. If the Fed gets its wish for higher inflation, this could be the beginning of a "regime shift" away from the disinflationary forces that have dominated the markets for the last 40 years.