Investing *Risk-O-Meter* Style

As promised, this week, I am putting forth an investable version of the *Risk-O-Meter*. Please refer to last week's issue for details on the methodology.

Because this version trades monthly (there's no edge in weekly trading except overtrading and lower returns), there could be differences between the weekly version, which I'll call *Risk-O-Meter* Version 1.0

While both versions measure the same things, there's a difference in expressing the trades in an actual portfolio.

There are four components to both *Risk-O-Meters*: market trend, credit risk, sentiment, and volatility. However, the investable version uses exchange-traded funds (ETFs) to make investments, not individual stocks. Therefore, some adjustments in the secret sauce needed to be made to express the trades with ETFs.

The beauty of ETFs is that they are easy to trade, often trade with no commission, tight bid / ask spreads, and the ones in the *Risk-O-Meter* represent huge asset classes. Therefore, no one can manipulate the market.

I've created a new graphic for the investable *Risk-O-Meter*. You can think of each component as either in "risk-on" or "risk-off" mode. If all of the components are on "risk-on, " the meter will point to dark green. If all components are in "risk-off" mode, the meter will point to dark red. If there is a mixture among the components, the meter will reflect that by pointing in-between.

In my opinion, the advantage of this is you can see collectively how much the components are in "risk-on" or "risk-off" mode.

You can see it in a nanosecond.

I will also show where each component is invested. That gives you many ways to use the *Risk-O-Meter*.

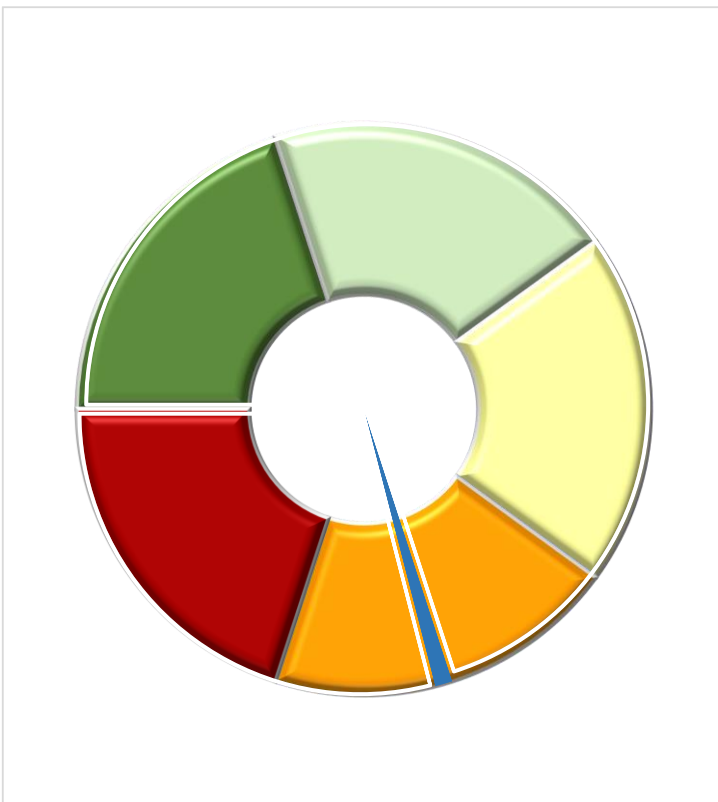
For example, you might think I'm a moron and bet against what my research suggests are profitable systems. I've been called worse! I'm sure you'll lose big over time, but you might have some good short-term runs.

Or, you might invest only in stocks or stock indexes. If the meter were pointed on dark green, that might give you the confidence to invest aggressively. If the meter points somewhere in the middle, you might pick your spots or scale back buying. If the meter points to red, you might sit on your hands and wait for a better environment.

You might also want to invest in one or two of the components. So, it will be easy to see that as well.

For the time being, I will include both versions in this newsletter. As always, I welcome your feedback in making this newsletter more beneficial to you.

Without further ado, here's the current month's meter!



Here are the four components and their positions.

Component	Position	Position Size	Risk ON or OFF
Market Trend	Cash	25%	OFF
Sentiment	Cash	25%	OFF
Volatilty	IEF	22.50%	OFF
Levered Volatility	UST	2.50%	OFF
Credit Risk	SPY	22.50%	ON
Levered Credit Risk	QLD	2.50%	ON

Three of the four components are in "risk-off" mode. For both the Market Trend and Sentiment systems, the position is to hold cash.

Volatility is in "risk-off" mode, and the position is the iShares 7-10 Year Treasury Bond ETF (Nasdaq: IEF), while the levered position is the ProShares Ultra 7-10 Year Treasury ETF (ARCX: UST).

Lastly, the Credit Risk indicator is in "risk-on" mode. The position is long the SPDR S&P 500 Trust (ARCX: SPY), and the levered position is the ProShares Ultra QQQ (ARCX: QQQ).

I use the Schwab US Broad Market ETF (ARCX: SCHB) instead of the S&P 500. In testing, I used SPY because it has a long history. However, my accounts are at Schwab, SCHB has a very low fee, and over time there's a slight edge to owning the broad market versus the S&P 500. However, it's not worth making a big deal over the differences.

Levered ETFs are very volatile and not suitable for many, if not most, people. I keep the position size small at 2.5% because I have found an excellent risk/reward relationship by including the positions in the portfolio.

<u>This portfolio represents my version of an investable Risk-O-Meter.</u> You can make adjustments that suit your purposes (like I did with SCHB instead of SPY), such as not using levered ETFs if you wish.

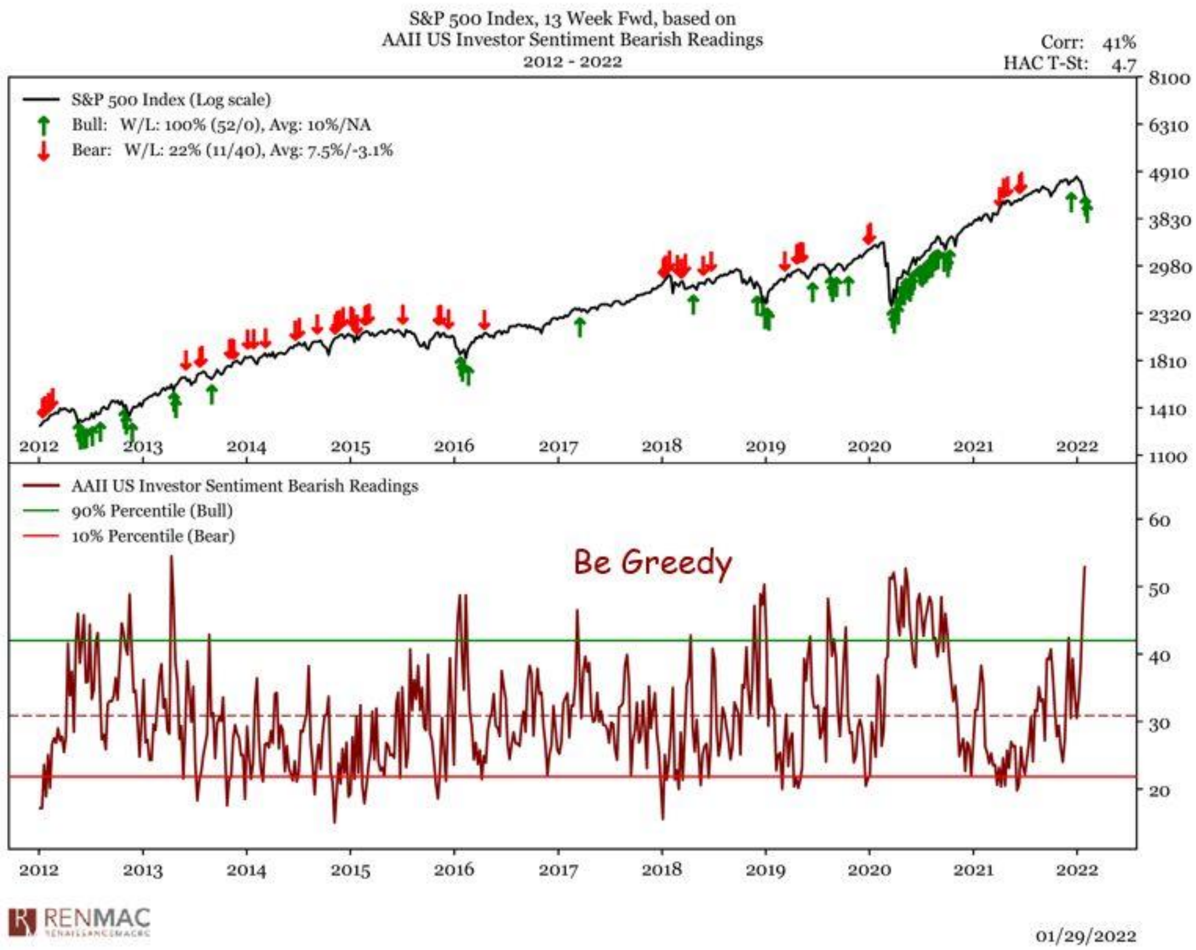
While risks did ease up a bit this week, the *Risk-O-Meter* is still on a sell signal. The rally I suspected would occur and noted in this space has occurred. Absent the complete implosion of Facebook's stock, which sent indexes down big time on Thursday; the market has mostly gone straight up.

The market is no longer oversold.

However, a couple of factors in play may be favorable to stocks.

First, there's way too much bearishness out there. Take a look at this chart, which looks at trends in the levels of bullishness and bearishness in individual investors.

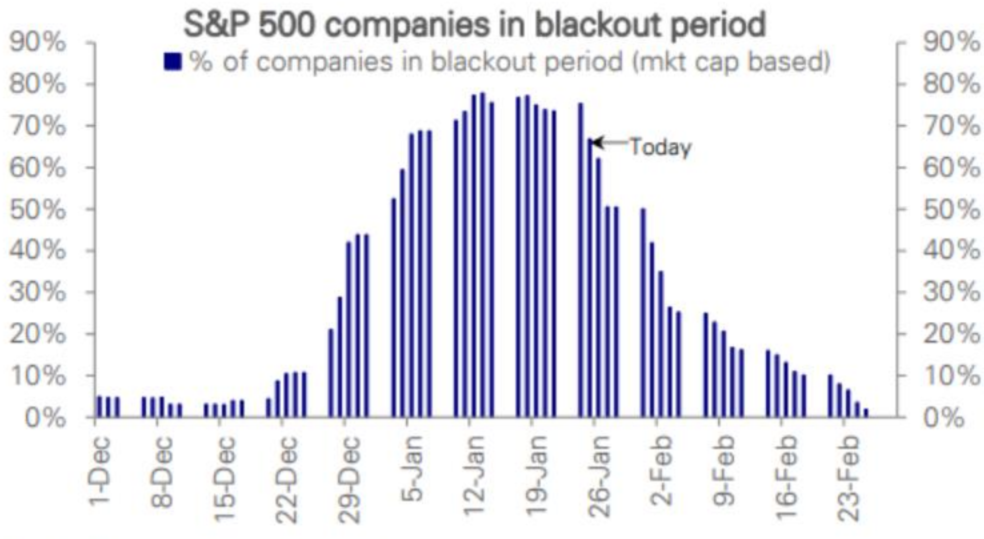
The level of bearishness is right up there with the initial COVID market panic and among the highest levels in the last decade. Historically, that has been very positive for stocks.



The other factor is that companies are increasingly coming out of quiet periods and can begin buying back stock.

Corporate buybacks have been one of the biggest drivers of stock market performance since the financial crisis bottom in early 2009. We are now about three-quarters of the way through the quiet periods, and the numbers drop off sharply from here.

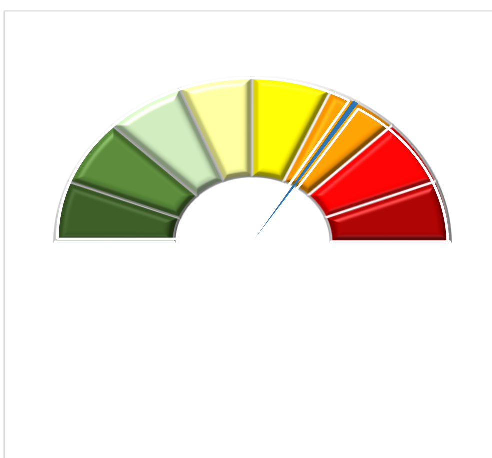
Figure 13: Buybacks will return to strength as companies report earnings and move out of blackout periods



Source : Bloomberg Finance LP, Deutsche Bank Asset Allocation

Note, where the chart says "today" is not today but a couple of weeks ago. Today, only about 10-15% of companies are still in a quiet period. It remains to be seen how aggressive buybacks could be in the near future. Everyone is freaked out about supply chains, inflation, and the labor market.

Now that the oversold condition is worked off, there is no edge either way (the market is not overbought either). Nonetheless, the *Risk-O-Meter* is urging caution.



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