Weekly Market Notes

September 14, 2020

Dow Industrials 27665
S&P 500 3341

BAIRD

Please refer to Appendix – Important Disclosures

Thoughts On The Recent Sell-Off In The Market

Last week the Dow Jones Industrial Average was down 1.7% adding to a loss of 1.8% the previous week and the S&P 500 lost 2.5% on top of the 2.3% loss the previous week. The tech-heavy NASDAQ lost 4.1% adding to its 3.3% loss the previous week.

There have been warning signs of a pullback in the market. The high tech large capitalized stocks had experienced a very quick move up over a short time. Since the mega-cap stocks -- Amazon, Microsoft, Apple, Facebook and Google -- comprise roughly 25% of the market capitalization of the S&P 500, a pullback in these stocks will inevitably pull the rest of the market down. Additionally, as the market was rising, breadth was deteriorating with fewer stocks trading above their 200-day moving average. Technical indicators were pointing to fully invested mutual funds and record call volume at the Chicago Board Options Exchange suggesting too much optimism in the market, which often signals a pullback. The correction in the markets over the past two weeks has helped relieve the excessive optimism in the market. Individual investors as well as active money managers have become more cautious. However, in spite of the recent sell-off, speculation in the options market is still alive and well and will likely contribute to ongoing market volatility.

Technology companies will continue to offer growth prospects due to work-from-home trends in business, education, entertainment, medicine and shopping. But expectations for the mega cap tech sector are tempered by soaring valuations in terms of price-to-earnings ratios and stronger antitrust regulations from the federal government likely coming soon. The past two weeks have seen a shift into the economically sensitive cyclical sectors as well as the cheaper valuation areas such as the small- and mid-capitalized stocks. These stocks were hit particularly hard in March and April of this year as smaller caps generally struggle in an economic downturn. As the economic data continues to point to a gradual recovery, investors should consider small- and mid-cap stocks in the strongest sectors of the market which are consumer discretionary, information technology, materials, communication services and industrials.

A significant decline in the market would likely be triggered by a setback in our progress in overcoming the COVID-19 virus and/or higher inflation or rising interest rates. There is continued progress in testing and treatments for the virus. The Federal Reserve is committed to keeping U.S. interest rates lower for longer and monetary policy accommodative. The Senate failed to pass a much-needed COVID-19 relief package for individuals and small businesses. They are back at the drawing board and we will hopefully see a relief package from Congress by the end of September. Going forward, the possibility of a too close to call unresolved presidential election and indecision on the federal stimulus package will likely weigh on stocks. If we get the additional aid package from Congress and with over $3 trillion parked in money market funds and with low interest rates and a vaccine on the way I expect to see consumer and business confidence improve which translates to a growing economy and a strong stock market.

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	RS Ranking Current		RS Ranking Previous	RS Trend	Sub-Industry Detail	
Consumer Discretionary	1	**	2		*Leaders:*	Homebuilding; Household Appliances; Footwear; Internet Retail; General Merchandise Stores; Computers & Electronic Retail
					Laggards:	Specialized Consumer Services; Department Stores
Information Technology	2	**	1		*Leaders:*	Application Software; Technology Hardware, Storage & Peripherals; Semiconductors
					Laggards:	Communications Equipment; Electronic Equipment & Instruments
Materials	3	**	4		*Leaders:*	Metal & Glass Containers; Gold
					Laggards:	
Communication Services	4	**	3		*Leaders:*	Publishing
					Laggards:	Advertising
Industrials	5	**	5		*Leaders:*	Construction & Engineering; Construction Machinery & Heavy Trucks; Agricultural & Farm Machinery; Diversified Support Services; Air Freight & Logistics; Railroads; Trucking
					Laggards:	Aerospace & Defense
Consumer Staples	6		6	+	*Leaders:*	
					Laggards:	Drug Retail; Brewers
Health Care	7		7		*Leaders:*	Health Care Supplies
					Laggards:	Health Care Services
Real Estate	8		9		*Leaders:*	
					Laggards:	Office REITs; Residential REITs; Retail REITs
Financials	9		8		*Leaders:*	
					Laggards:	Diversified Banks; Multi-line Insurance
Utilities	10		10		*Leaders:*	
					Laggards:	
Energy	11		11		*Leaders:*	
					Laggards:	Oil & Gas Equipment & Services; Integrated Oil & Gas; Oil & Gas Exploration & Production; Oil & Gas Refining & Marketing; Oil & Gas Storage & Transportation

*** Denotes Current Relative Strength-Based Overweight Sectors*

Sentiment Indicators

	Current		Previous			Indication (from contrarian perspective)
CBOE 10-Day Put/Call Ratio *Below 70% is bearish; Above 90% is bullish*	84%		82%			Neutral
CBOE 3-Day Equity Put/Call Ratio *Below 45% is bearish; Above 60%is bullish*	61%		55%			Bullish
VIX Volatility Index *Below 20 is bullish; Above is 45 is bearish*	27		31			Neutral
American Association of Individual Investors *Twice as many bulls as bears is bearish; 2X more bears than bulls is bullish*	Bulls: Bears:	24% 49%	Bulls: Bears:	31% 42%		Bullish
Investors Intelligence (Advisory Services) *55% bulls considered bearish/more than 35% bears is bullish*	Bulls: Bears:	59% 16%	Bulls: Bears:	61% 16%		Bearish
National Assoc. of Active Investment Mgrs. (NAAIM) *Below 30% is bullish; Above 80% is bearish*	53%		107%			Neutral
Ned Davis Research Crowd Sentiment Poll	Optimism Extreme		Optimism Extreme			Bearish
Ned Davis Research Daily Trading Sentiment Composite	Optimism Fading		Optimism Excessive			Neutral

Appendix – Important Disclosures and Analyst Certification

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