Disciplined Wealth Management

12/31/2023 Quarterly Newsletter

Discipline is the key to success

With every approach to the stock market, bear in mind that there will always be periods of over-performance and periods of under-performance. Here at Disciplined Wealth Management (DWM), our goal is to concentrate your portfolio in the leading asset classes while avoiding the performance-sapping lagging asset classes; over the long term, our approach strives to provide you with better performance compared to the overall stock market average (the S&P 500) and with less risk. In summary – stay disciplined during times of under-performance; don't become emotional and abandon a proven long-term strategy during a usually short period of under-performance, but stick with it and let the strategy work for you. If someone says they are never wrong, they have just proven themselves otherwise.

Forecast —

74% Probability of Double-Digit Gains in 2024

2024 should come in with double-digit gains! How did we get 74%, by following the data. We looked at all the annual S&P 500 returns starting in 1926, separating annual returns between secular bull or secular bear markets (Definition of secular market activities that unfold over long time horizons, or that aren't influenced by short-term factors.) Which is what we consider ourselves to be currently involved in. The results are just short of amazing! Fifty-three of the years fell into secular bulls, and here are the probabilities of outcomes:

- 0% Probability of 20% loss or greater,
- 5.7% possibility of a decline between -10% to -20%,
- 7.5% chance of 0% to 10% loss,
- 13.2% of years posted single-digit gains.
- 28.3% of the time the market will rise between 10%-to-20%*
- 45.3% of the time, the S&P 500 gains over 20%.

*As of 12/5/23 S&P 500 fell into 10%-to-20%

What always amazes me, knowing the data, which is easily accessible, are the annual Outlooks by leading strategists, that most of the estimates are typically single digit. A safe bet, as the average S&P 500 return over both secular bulls and bears, does fall into the high-single digits. But single digits gains in secular bulls only occur 13% of the time, a losing bet. One exception is Ed Yardeni, who often breaks from the herd in making more realistic Outlooks.

At DWM, all our analysis is quantitative, based on historical data. Starting with the 74% probability of a double-digit gain, we then drill down to see what quantitative data is available to refute or reinforce that outlook. Also, what data may provide a clue to the scale of the advance.

Odds of an annual decline in a secular bull are slim, 13.2%. Only seven negative years out of 53 cases, and all down years were separated by a minimum of three years of gains.

The rate of inflation has been falling, the Fed's battler is working. The consensus and Fed comments tend to argue that the last hike was on 7/26/23. Looking at seven prior cases of rising rates, the market has done well once the last hike is in place.

Breaking the seven cases between secular bulls and bears, the average gain we could expect is 25%. With the S&P 500 at 4565 on 7/26/23, that provides a goal of 5700 by late July 2024.

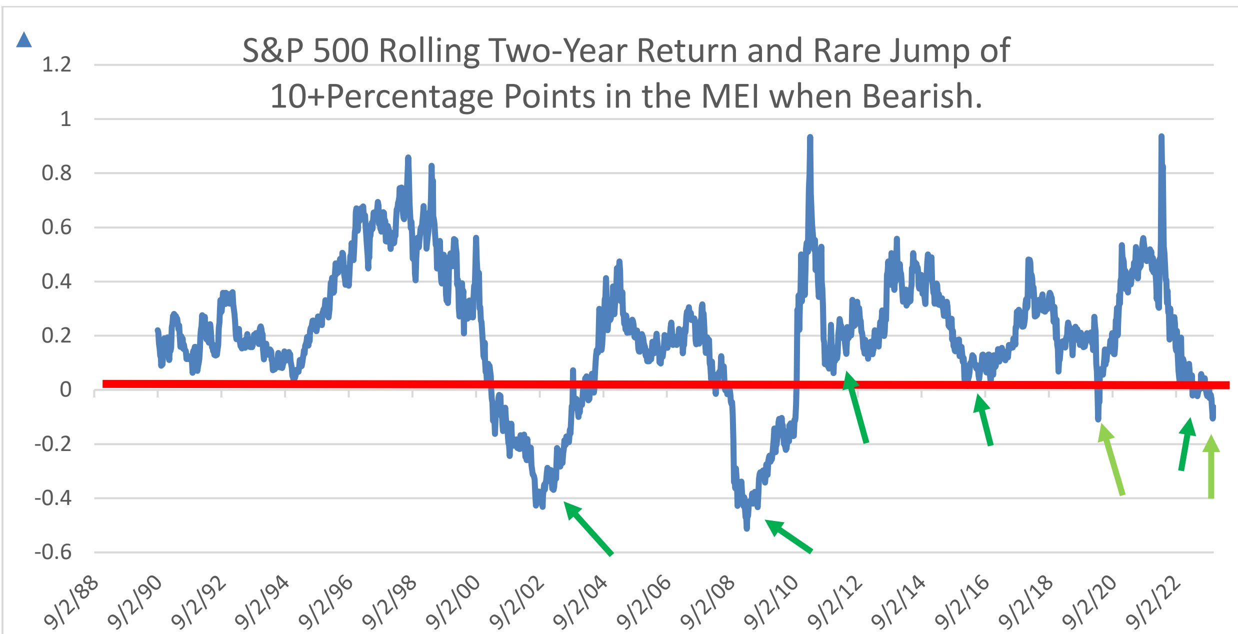
S&P 500 Change after Fed Pause

	6 Months Later	12 Months Later
Secular Bears (4 cases)	2.1%	2.0%
Secular Bulls (3 cases)	19.6%	25.3%

The current bull, starting on 10/12/23, had the weakest 1st year gain when compared to the prior seven bull markets. The average 1st year gain was an impressive 40.5%, while todays only managed a 21.6% move. But what happens the 2nd year, all cases were positive with an average 12 month gain of 15.3%. That provides a glimpse at the S&P 500 trading above 5,000 by mid-October in 2024.

It is very rare when the rolling two-year return for the S&P 500 shows losses. Less than a handful of cases since the secular bear market during the 1970's. But just being in negative territory does not provide a good buy signal. What does, is when a momentum or breath-thrust to the upside occurs, signaling that the trend has reversed.

Within DWM we have an intermediate-term market signal, MEI, that measures momentum and trend of 100+ sub-industry groups that make up the broader S&P 500. Being so broad, weekly moves tend to be narrow based on a scale from 0 to 100. Therefore, a jump over 10 points in a single week is rare. Since 1987 only on 6 prior occasions has a momentum thrust (10+ point gain) occurred when the MEI is in bearish territory. A 7th just occurred on 11/6/23.



A couple of observations: Six of the seven signals came after the two-year rolling return began to turn up, a valid reinforcement that the upward trend is for real. Second, the median 12-month gain following a jump of 10+ points when Bearish is a median 21.4%. That would indicate the S&P 500 should be trading above 5300 by early November 2024. Third, once the trend reversed, it was often followed by multiply years of significant returns. Not a case of one-and-done.

Rare Zweig Breadth Thrust Buy Signal:

"The market just triggered a rare signal that has meant higher returns a year later 100% of the time." This was a recent CNBC Pro headline following the big market gains of 10/27-11/3/23.

The Zweig Breadth Thrust Indicator flashed a buy signal for only the 18th time since 1945. In the 17 prior cases, the S&P 500 has posted gains 3 to 4 times greater than average 6 and 12 months later. Half of the Zweig Indicator signals, highlighted in yellow in the table below, came within days if not weeks of major market turning points.

Rarity and accuracy makes this one piece of data that carries with it a lot of confidence. Eighty years of history tells us that when this is triggered the average gain is over 23%, giving us an objective of 5373 by early November.

Zweig Breadth Thrust Indicator				Description of Indicator signal relative to S&P 500 Bull Markets
Date	3 Months	6 Months	12 Months	
2/3/1945	9.8%	8.2%	32.2%	Occurred in the middle of Bull Market run of 158%
3/8/1949	-7.1%	2.6%	15.0%	3 Months before 97% Market Advance
7/21/1950	13.5%	20.9%	26.9%	1 Year into 97% Bull run
7/11/1962	-0.9%	12.1%	20.8%	2 weeks after of start of new Bull Run of 80%
11/5/1962	13.8%	20.0%	24.8%	Four months after start of 80% market gain
12/3/1971	11.3%	13.2%	21.1%	1 week after start of new 33% market run
10/10/1974	4.0%	20.6%	26.6%	1 week off bear market low, 73% bull market followed.
1/3/1975	14.4%	33.4%	28.6%	2nd confirmation of bull market
8/20/1982	22.4%	30.5%	44.7%	1 week into new 69% Bull market run
8/13/1984	3.2%	10.0%	17.9%	3 weeks off low, bull market runs 128%
5/25/2004	-0.7%	5.7%	6.9%	1 1/2 years into bull market gain of 102%
3/18/2009	14.6%	34.5%	46.8%	1 week after 2007-09 bear market low, S&P gains 102%
10/14/2011	5.6%	13.6%	17.6%	11 days off low, 94% bull market gain for S&P
10/18/2013	5.7%	7.7%	9.1%	right in middle of 4 year bull run of 94%
10/8/2015	-4.5%	1.4%	7.0%	Early signal, 94% bull market run starts 4 months later
1/7/2019	13.6%	16.9%	27.0%	Two weeks after 20% Dec. 2018 decline, 44% gain followed
3/31/2023	8.4%	4.4%	?	Five months after October 2022 low. Modest gains so far
11/3/2023	?	?	?	2nd confirmation. One week after 10% correction
Average	**7.5%**	**15.0%**	**23.3%**	
S&P 500 Average	2.0%	4.1%	8.4%	

Other observations:

What about a recession? A recession has been in the forecast for much of 2023. First, it never occurred, and Q3 GDP is coming in above 5%. Something no one was predicting. With employment strong, and the ratio of job openings to unemployment remaining high, the probabilities of a recession are overrated. But recession fears could be a positive for the market.

Fearful investors may remain initially on the sidelines, but as the market rises and so does the economy, those cautious and defensive prone ’investors, capitulate and turn into buyers.

The earnings recession is behind us! S&P 500 earnings are expected to rise over double-digits in 2024 and hit record highs.

While the Magnificent Seven (consisting of the following stocks: Apple, Alphabet, Amazon, Meta Platforms, Microsoft, Nvidia, and Tesla) have been leading the market and the S&P 500 higher, forever it seems, it is hard to imagine but the Equally Weighted S&P 500 (RSP) or the Russell 2000 (IWM) have delivered equivalent or higher returns, when measured in decades. But after 2023’s run, the Russell 2000’s 12-month return is running at the 2nd biggest negative rate since 2001, and the Equally Weighted S&P 500 is a trailing the 12-month performance of the cap-weighted S&P 500 by a full 12 percentage points, 1.4% versus 13.7% as of 11/30/23. The significance, a reversion to the mean. In the past such large divergences have been followed by a year of catch-up.

DWM’s Outlook: The data points to double-digit gains for the S&P 500 in 2024! DWM’s outlook is for the S&P 500 to finish between 5300 and 5500. But bigger gains will be in the Russell 2000 and the Equally Weighted S&P 500, both over 20%.

Will this be the case? No one knows for sure and only time will tell. DWM, for one, will continue to rely upon its tactical tools to stay in line with the market’s fluctuations. Always remember: the key to investment success is to stay disciplined and flexible in an ever-changing market environment. The moment you start to second-guess your decisions is usually when you shouldn’t.

As we go to press, the overall Market Environment Indicator (MEI) remains bullish, along with the Individual Fund Signals (IFS). We will continue to monitor these indicators and make the necessary adjustments. For an individual performance review, please call 303-471-5189. Please note that, in the following pages, the performance charts for certain asset classes showing year-to-date returns, are for illustration purposes only and do not reflect our Relative Strength Analysis (RSA) system.

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Sources: Style box data = i-Shares Russell Indexes. Source: Investors FastTrack.Sector data = DJ US Sector Indexes via I-Shares. Source: Investors FastTrack. International data = i-Shares for Emerging Markets, Europe, pan, S&P 500 Index for U.S.A. Source: Investors FastTrack.
Bond data = various bond exchange traded funds (ETF). Source: Investors FastTrack.