Market Update – Toews Rolls Leap Higher in Managed Risk

- Markets are Vulnerable – Cost to Protect is Low
- Fixed Income may be set up for surprise….gains?
- Toews Launches its First 351 Seeded ETF – HRSK

At Low Vix Levels – Toews Rolls up LEAP put strike at Mid-Year

In my book The Behavioral Portfolio, I distilled all the factors that determine stock prices down to one just word: ***Optimism***. Optimism reigns over all of the underlying market noise to ultimately determine our mutual prosperity. As fast as perceptions change from optimism to pessimism, our fates change. At positive extremes each dollar of company earnings is worth $40 (collective stock prices). Devoid of optimism, we say that same dollar is worth $5 (a startling 87.5% difference). Your life, and that of your clients, all hinges on that one word.

Understanding that, it is a natural logical extension that when optimism is super high, markets are super vulnerable. And here's where we are presented with a gift, because at optimistic market extremes, the cost to buy protection against losses *is near its lowest*. If life insurance companies operated like stock options pricing, they'd offer the lowest cost policies to those closest to death. At times of extreme optimism, investors assume that there is no need for stock protection.

The blessing is realized by managers that execute options overlays on stock portfolios. At the end of June, we rolled our LEAP higher in our Managed Risk strategies, as we were just north by a rabbit's whisker of 10% above the LEAP strike. That nudge locks in a good chunk of this year's gains, and because we handle the roll under the hood, advisors are spared the tax headache that comes from rolling buffers themselves at the end of an outcome period. The takeaway for advisors utilizing our strategies is this:

> *Our Entire Options Overlay is dynamically managed to adjust for market moves, so that you can make an allocation to hedged equity, and let it run without intervention, regardless of market moves.*

Fiscal Depravity and the Future Path for Bonds – ***Are bonds over the short-term setting up for surprise….gains?***

As I ramp up research for my new book about the potential of currency debasement (*Heading into de Basement),* my thoughts again coalesce into a single word: ***Confidence***. Here's the problem. We all are operating as if there is no level of fiscal depravity that will destroy confidence in the all might dollar and the invincibility of the US treasury to defend it. If, however, confidence is lost, then the difference could be more dramatic than the stock valuation reality cited above. The U.S. dollar becomes the Monopoly dollar, with implications for every aspect of our financial lives.

The history of fiscal excesses tends to lead to negative outcomes for inflation which translates into a potential brutal landscape for bonds, and the transition from calm to disorderly can be abrupt. The play out for this could be many years hence. However, it's impossible for me to think about the fixed income landscape without addressing contingencies around this issue.

That said, over the short term, bonds may be set up for a short term bounce, based on several factors:

1. The "end" of the Iran war has already reduced energy prices, which will likely translate into a reduction in inflation over the coming months[i]
2. Tariffs are actually lower over the last quarter relative to 6 months ago[ii]
3. The pace of job growth is slowing[iii]
4. Real estate inventories across many parts of the country have driven higher, including rentals, causing median rental prices to decline over the past 12 months, which will be reflected in shelter costs on coming CPI reports.[iv]

Considering that the futures markets are pricing in one rate increase this year, a decline in inflation expectations could have a positive effect on bond prices. The question then becomes what part of the bond market optimizes the current environment? This depends on many factors. Yet, should stocks continue their ascent, and interest rates move favorably, taking advantage of the yields provided by high yield bonds may provide a boost to bond market returns to make up for the lackluster gains in fixed income this year. Currently, our models are allocated to High Yield Bonds, but have a close trigger that would move us defensive. Our takeaway for bond portfolios is:

- Current expectations for a rate increase and longer term pressures create a strong incentive for advisors to address fixed income contingencies, yet;
- Bonds, including High Yield Bonds, may rally if inflation pressures subside.

Commented [YK1]: Explain this. Lower energy prices reducing GDP runs backwards from how this normally works. Cheaper energy is usually a tailwind for growth, not a drag, since it lowers input costs for businesses and frees up consumer spending. Please clarify what you meant.

Factors 2-4 support the short term bonds bounce so I concur.

Commented [YK2R1]: Updated to inflation

Happy week ahead!

Felipe

All statements other than statements of historical fact are forward-looking statements (including words such as "believe," "estimate," "anticipate," "may," "will," "should," and "expect"). Although we believe that the expectations reflected in such forward-looking statements are reasonable, we can give no assurance that such expectations will prove to be correct. Various factors could cause actual results or performance to differ materially from those discussed in such forward-looking statements.

This market update is intended to provide general information only and should not be construed as an offer of specifically tailored individualized advice, and no representation is being made as to whether the information provided herein would be beneficial for any or for a specific Employer Benefit Plan or investor.

For additional information about Toews Asset Management, please visit our website, www.toewscorp.com.

---

[i] Source: https://www.bloomberg.com/quote/CO1:COM
[ii] Source: https://am.jpmorgan.com/us/en/asset-management/adv/insights/market-insights/guide-to-the-markets/ - Page 26
[iii] Source: https://am.jpmorgan.com/us/en/asset-management/adv/insights/market-insights/guide-to-the-markets/ Page 19
[iv] https://www.apartmentlist.com/research/national-rent-data