

Monthly Intelligence Report

ZenInvestor®

Invest Smarter

April 2025

Executive Summary

- The S&P 500 entered a correction on March 13.
- Earnings estimates are coming down due to policy uncertainty and weakening consumer sentiment.
- Global GDP growth will slow from 3.2% in 2024 to 2.8% in 2025.
- US GDP growth will slow from 2.8% in 2024 to 1.7% in 2025.
- The Bear Market Probability Gauge moved higher this month.
- The Recession Probability Gauge also ticked higher.
- My December 2025 S&P 500 target is 6381, down slightly from last month.
- I made no changes to the asset allocation models this month.

The US Economy

US economic data releases have been weakening of late. Consumer Confidence is down, as is business sentiment. Retail sales are down, corporate earnings estimates are coming down, and tariffs are here, with more to come on April 2. Companies are postponing CAPEX plans as they await more clarity on the tariff front. Meanwhile, consumers and investors alike are drifting towards a bunker mentality. These are the kinds of effects that uncertainty causes. And we have an abundance of uncertainty right now.

The expected growth rate of the US economy was 2.3% earlier this year but is now revised down to just 1.7% growth. That's not bad enough to start predicting a 2025 recession, but the odds have certainly increased over the last two months. My model puts the odds at 22% that we will have a recession sometime over the next 4-6 months.

Inflation has come down, but consumers are still stretched and this is one of the main reasons for consumer confidence to be as low as it is. As the popular narrative goes, tariffs are inherently inflationary, since businesses who import from other countries are likely to pass all or most of their increased costs to consumers. Although I don't expect it, a spike in the CPI after the tariffs are fully implemented will knock another leg out of the stock market's stool.

The U.S. Stock Market

The S&P 500 has been in a correction since it reached its all-time high on February 19. There is a counter-trend rally going on now, and it's anybody's guess as to whether or not we have hit the bottom of this selloff. The odds of a bear market (down 20% or more from a recent high) happening sometime in the next 4-6 months moved higher this month, from 20% to 22%. Is that cause for alarm? Not yet, but the large institutional investors have been raising cash lately.

I have lowered my forecast for the year 2025 to 6381, which would work out to a yearly gain of 8.5%. As more economic data comes in, this forecast will change, but not by much. The big changes in forecasts come from Wall Street strategists and economists who use judgement and instinct to forecast the outcome. I, on the other hand, use data and only data. If the incoming data continues to weaken, my model will adjust the forecast lower.

Consensus forecasts for 2025

The table below shows the consensus forecasts from strategists, asset managers, and economists at the major Wall Street firms. The individual forecasts are widely dispersed but the average has historically been close to the actual closing price.

According to these forecasts, 2025 will end at **6388**, which would represent a 10% gain for the year. With the bull market intact but currently in correction mode, these forecasters have been lowering their targets. As these forecasts change throughout the year, I will update this table accordingly.

FIRM	2025 S&P	% Change
Oppenheimer	7100	20.7%
Wells Fargo	7007	19.1%
Deutsche Bank	7000	19.0%
Evercore ISI	6800	15.6%
SocGen	6750	14.8%
HSBC	6700	13.9%
BMO Capital Markets	6700	13.9%
FactSet	6678	13.5%
Bank Of America	6666	13.3%
Fundstrat	6600	12.2%
Ned Davis Research	6600	12.2%
CFRA	6586	12.0%
Citigroup	6500	10.5%
Morgan Stanley	6500	10.5%
JPMorgan	6500	10.5%
Yardeni Research	6400	8.8%
UBS	6400	8.8%
Raymond James	6350	8.0%
LPL Financial	6325	7.5%
RBC Capital Markets	6200	5.4%
Goldman Sachs	6200	5.4%
Barclays	5900	0.3%
Stifel	5500	-6.5%
T Rowe Price	5300	-9.9%
BCA Research	4450	-24.3%
AVERAGE	6388	10.0%

As of 3/25/25

Sector preferences.

My top sectors right now are Technology, Healthcare, and Industrials. Technology will benefit from the ongoing buildout of AI infrastructure. Industrials will benefit from providing the tools and materials needed for the buildout. Healthcare will benefit from relatively modest valuations and the ageing U.S. population.

Least favored are the sectors that are the most vulnerable during an economic slowdown – Energy and Real Estate will likely lag as their upside is limited by receding demand from consumers and businesses. Bear in mind that these earnings estimates will change as we move through 2025, and the attractiveness rankings will change accordingly.

These leading and lagging sector forecasts are consistent with an economy that is still expanding but at a slow pace. If we have a recession, which appears less likely, these over- and underweights will become even more valuable from an asset allocation standpoint.

Sector	2025 Earnings Growth (Estimate)	2024 Total Return (Actual)	2025 Total Return (Estimate)
Info Tech	19.6%	29.3%	19.6%
Health Care	18.3%	2.7%	16.9%
Industrials	12.6%	16.9%	16.1%
Comm. Svc.	12.1%	33.1%	14.2%
Utilities	7.1%	23.1%	12.5%
Financials	7.8%	30.5%	11.7%
Materials	9.0%	0.5%	10.6%
Cons. Discr.	6.2%	24.3%	9.4%
Cons. Staples	12.1%	13.3%	8.7%
Real Estate	2.2%	4.8%	7.9%
Energy	-0.2%	6.8%	5.8%

Source: S&P Global; Factset; Zacks Investment Research

Earnings

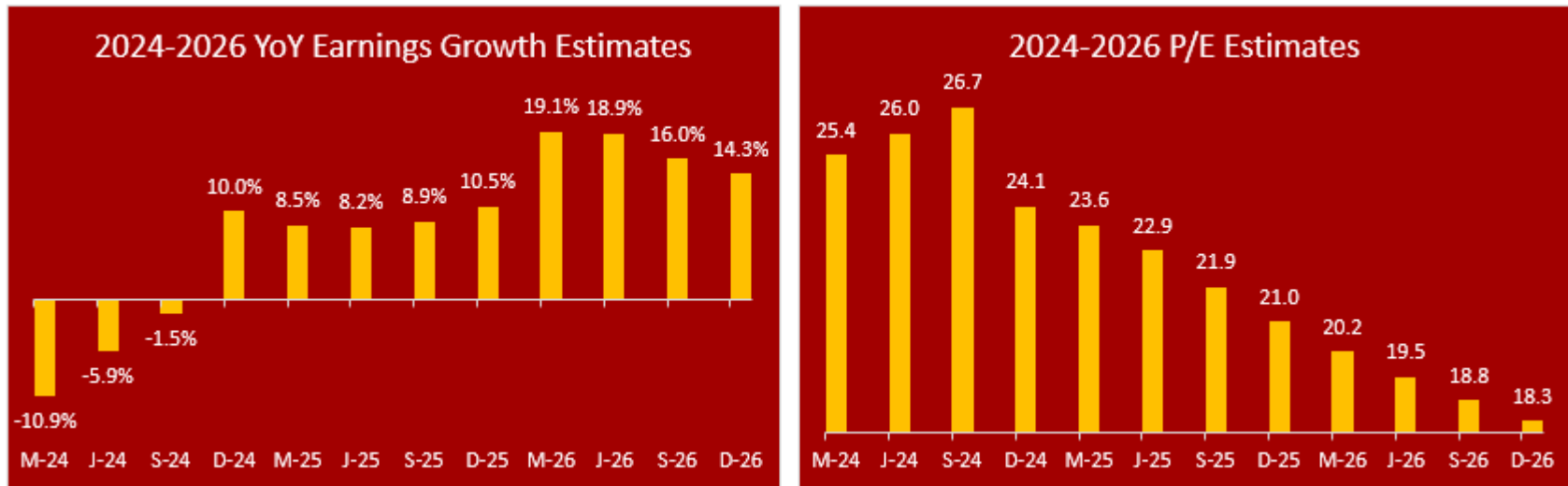
Turning to the earnings outlook for 2025-2026, analyst consensus forecasts have been moving lower for the past few months. Several companies have reported moderate earnings beats for the December quarter but they are also trimming forward guidance. Lowered guidance indicates a more cautious but not necessarily bearish outlook among analysts and the companies they follow.

The S&P 500 (the blue line on the chart below) is well above earnings estimates for the March quarter. As a result, valuations are still stretched, even after a 10% correction. In order to bring valuations down to a level closer to the historical trend, either earnings estimates must rise or the market must slow down. I think the market will keep rising but at a slower pace than we've become accustomed to.



Looking at the picture from a different angle reveals three quarters of negative earnings growth, followed by reasonably healthy growth through 2026. According to S&P Global, year-over-year earnings growth (operating) is projected to be up by 10.0% in

2024, up 10.5% in 2025, and up 14.3% in 2026 (left chart). My view is that Wall Street analysts are still too optimistic about the prospects for future earnings. If these optimistic earnings estimates are met or exceeded, and the market trades sideways, the market P/E (on “operating” earnings) will come down from the September 2024 high of 26.7 to 21.0 by the end of 2025 and 18.3% by the end of 2026 (right chart). This assumes a sideways-trending market that neither gains nor loses more than 5%.



What is more likely to happen is that the market will rise along with earnings, which will keep the P/E ratio close to where it is today. If consensus earnings estimates continue to come down modestly, as I expect, the market P/E will expand. The long-term median P/E based on “operating” earnings is 18.4.

If, on the other hand, earnings estimates should come down more sharply, it would signal an increased risk of a recession. That is not my base case, however. I believe that we will have a soft landing, and that the Fed will accelerate its easing if the market declines sharply from here.

The Models

Key Market Indicators (KMI)

The KMI traffic lights are designed to give readers a visual sense of how healthy the market is. They cover 4 groups of indicators – Fundamental ones, like revenue and earnings growth; Technical, such as relative strength and on-balance volume; Valuation, like P/E, Price-to-book; and Risk, such as recession threat and volatility. Today we have one green, one red and two yellows. This configuration means that the market is healthy but there are above-average risks. Valuations are stretched to the 3rd highest reading since 1950.



The **Fundamental** group light is green, reflecting still solid earnings growth and expanding profit margins. Analysts expect Q4 earnings to come in 10.0% above the same quarter one year ago, which is very respectable. The ongoing rollout of AI applications are starting to show up in a wide range of businesses. If this trend continues, the fundamental light will likely stay green.

The **Technical** group light is yellow this month, mainly due to the recent bout of volatility and market weakness. On the plus side, the spread between the 50 day and 200 day moving averages is still moderately positive but contracting. Fewer stocks are above their respective 200 day moving averages compared to last month.

Valuation is red, reflecting above trend P/E and P/B ratios. Analysts are reducing their earnings estimates for 2025 and 2026, and there have been some pockets of weakness in sectors like Technology and Construction.

Risk is yellow after being green for the last several months. Despite last year's long string of new record highs, there are some concerns investors are dealing with. Has the Fed being too timid with its rate reduction program? Is the AI trade losing steam? Will the Russia-Ukraine conflict turn into a wider campaign? And, will the new administration's policies regarding tariffs and immigration cause a resurgence of inflation? Only time will tell.

Bear Market Probability Gauge

This gauge calculates the likelihood that a new bear market will arrive sometime in the next 4-6 months. It is built on Bayesian inference, where we start with the assumption that the 2025 will see the market rise by 10.6%, which is the long-term average of all years back to 1928. The model then adjusts that assumption based on current data like valuation, projected earnings growth, and market behavior during similar periods.

The probability gauge takes all the measures of market health and assigns a probability to each, based on similar conditions that were present during past bear markets.

As of today, the probability of a bear market arriving in the next 4-6 months is **26%**. This is higher than last month. The reading is based on solid (but slowing) economic data, a slowing but still robust jobs market, and healthy consumer spending. Personal income has been rising at a faster clip lately as compared to the historical trend. However, there has been a downtick in consumer sentiment and an uptick in inflation expectations lately.

The gauge is sending a clear signal that this bull market will last for at least the next 4-6 months. However, if inflation begins to move substantially higher, or the economy slips into a mild recession, and the reading on this gauge starts to move higher, I will increase the cash allocation in the asset allocation models shown later in this report.



Probability of market outcomes for Year End 2025.

In this section of the report I estimate the probabilities of various market outcomes looking out to December 2025. Each market outcome shown in the table on the right has its own Bayesian probability of occurring. This table shows the weighted probability of all the possible outcomes.

The model forecasts a **gain of 8.5%** from the Decembber 31, 2024 closing price of **5881** to the December 2025 estimate of **6381** for the S&P 500. Here are the probabilities for each of the estimated market outcomes:

There is a **19%** chance that the market will be up by **20%** or more by December 2025.

There is a **28%** chance that the market will be up by **10% - 20%**.

There is an **34%** chance that the market will be up by **0% - 10%**.

There is a **10%** chance that the market will be down by **0%-10%**.

There is a **6%** chance that the market will be down by **10% - 20%**.

The most bearish outcome (**3%** probability) is a decline of **20%** or more in 2025.

The table above, when used in conjunction with the stock market traffic lights and the bear market speedometer (both shown above), offers a reasonable, data-driven expectation of where we will end on 12/31/2025. Bear in mind that these forecasts will change as more data comes in and the stock market model makes the necessary adjustments.

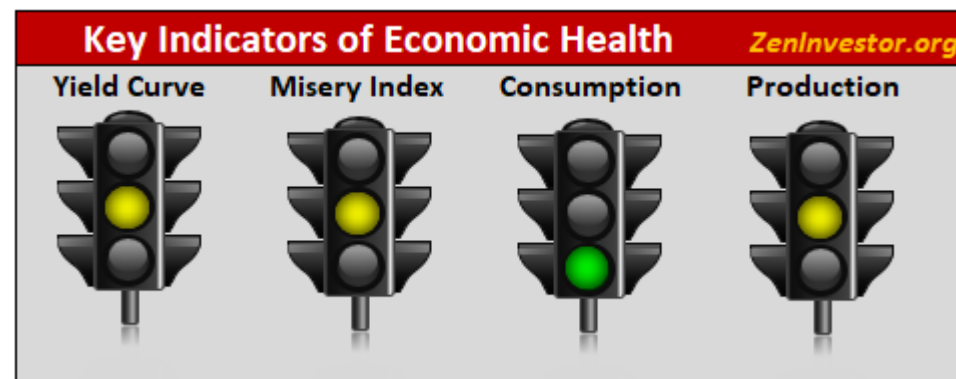
Outcome for the S&P 500 tthis year	Dec 2025 Level	Outcome Likelihood
up 20% or more	7,351	19%
up 10%-20%	6,763	28%
up 0%-10%	6,175	34%
down 0%-10%	5,587	10%
down 10%-20%	4,999	6%
down 20% or more	4,411	3%
As of 3/25/2025		100%

12/31/2024	5,881
12/31/2025 est	6,381
Est. Chg for 2025	8.5%

Key Recession Indicators (KRI)

The recession warning lights look at four economic indicators to gauge the health of the economy. Of the four indicators, the Yield Curve is the most prominent, since it has a good track record of predicting recessions.

After spending several quarters in the red (reflecting the inverted yield curve), this light has turned yellow (reflecting the slightly positive curve.) With three yellow and one green light, the model indicates caution but it does not yet give a clear warning that a recession is coming.



The **Yield Curve** index flipped from red to yellow in December 2024, reflecting the positive Treasury yield curve. The longer the 10yr rate stays above the Fed Funds rate, the lower the risk of recession. There isn't much room for error at this time.

The **Misery Index** is yellow. The index is at the current level of **6.90**, down from **7.00** last month and up from **6.84** one year ago. The index adds together the inflation rate and the unemployment rate. With creeping inflation, this indicator is becoming less bullish. Consumers are still getting squeezed by inflation, and real wages have been growing but have not been keeping up. This has forced many consumers to tap into credit cards and home equity lines of credit in order to cover the high and rising cost of living.

The **Consumption** Index is green, driven by strong demand for travel and leisure services. Consumers may also be pulling future purchases forward in order to avoid paying even higher prices due to excessive tariffs, or getting hit with higher interest rates if inflation moves up at a faster pace.

The **Production** Index is yellow. This indicator tanked during the COVID lockdown, then bounced right back to pre-COVID levels. It has since been trending sideways. U.S. factories are building up excess capacity as the demand for manufactured goods has softened. Some businesses are working off excess inventory.

Recession Probability Gauge

The probability of the US economy slipping into a recession sometime in the next 4-6 months is **22%**. Recent economic data has been softer than expected and there is concern about the trend of unemployment. Retail sales were down in February, but not by enough to signal a significant drop in overall consumer spending.

Some key leading indicators are also trending lower, including consumer confidence and the ISM manufacturing index. My base case is a soft landing for the economy, i.e., inflation moving closer to the Fed's target without a Fed-induced recession. The inflation picture should continue to improve in the coming months, but the ride will be a little bumpy.

The stock and bond markets are trading with above average volatility as investors struggle to formulate their expectations for the economy during 2025. Investors are anticipating lower taxes and loosening regulation on businesses. If implemented, companies – especially small and mid-caps – will benefit. More of their revenue will flow to the bottom line, thus raising earnings per share and creating headroom for price increases.

The Fed is fully focused on its mission to bring inflation under control, regardless of the pain it may cause for consumers, employees, and investors. The risk of a policy error (not cutting rates fast enough) has the potential to send the economy into a recession. If large tariffs are widely imposed, economists think there will be an uptick in inflation and the interruption of some of our supply chains. On the whole, however, economists are guardedly optimistic about the next 2 years. They say that any tariff-related uptick in inflation is likely to be short lived. As far as supply chain interruption goes, the thinking is that we will adapt quickly and avoid the mess we experienced during the pandemic.

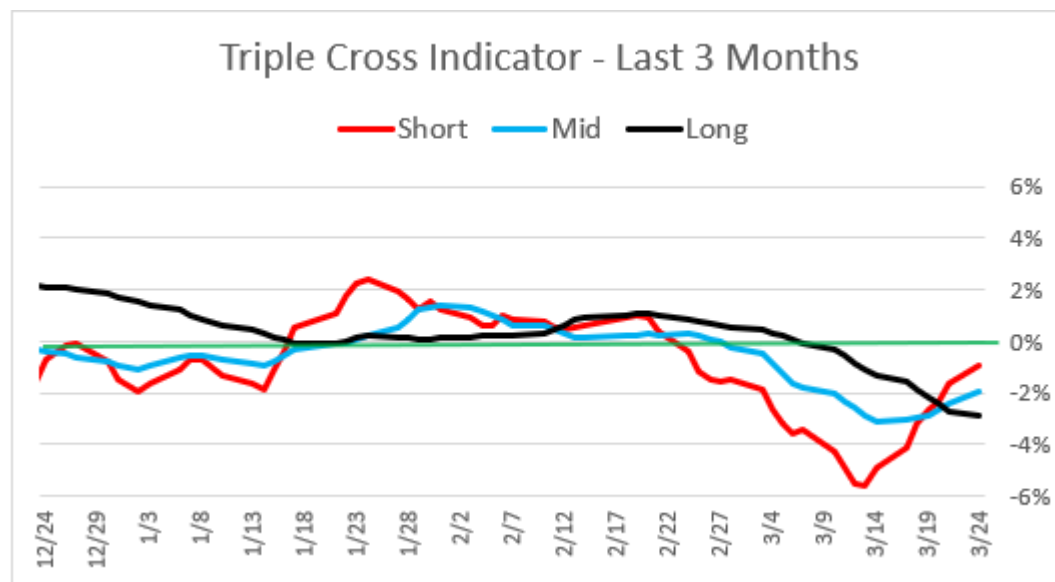


The Zen Triple Cross Moving Average Indicator

This Moving Average Indicator is best utilized as part of a Plan B defensive strategy. As each of the three individual lines cross above or below the Zero line, active investors can increase or reduce risk exposure accordingly. Long term investors should look at this indicator but not be in a rush to make portfolio allocation changes.

A simple example would be a two-asset portfolio that switches between equities (risk) and cash (riskless) as the model indicates. For example, if your normal asset allocation calls for 80% equities and 20% bonds, active investors can use this indicator to adjust that mix. When this indicator begins to turn negative, you might reduce your equity exposure from 80% to 70%. If it continues to become even more negative, you might reduce your equity exposure to 60%, and so on.

Here is a chart of the last 3 months. All three lines are in negative territory, indicating a derisking of asset allocations. The Triple Cross Indicator presents a narrow view of the market, as it is a technical indicator based solely on price movement. It is designed to give the reader a sense of where the market may be headed in the near term. We are currently headed south.



Market Dashboard

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S&P 500 Drawdowns 2024-2025



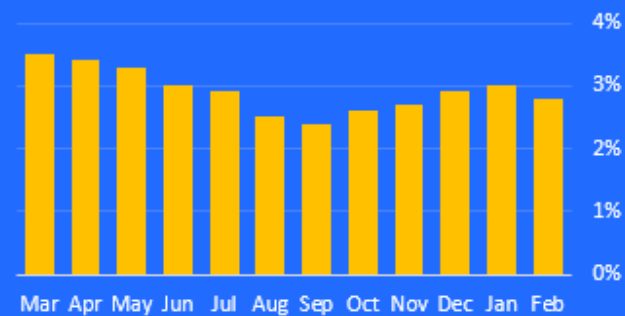
Up Days out of Last 15 Days



Treasury Yield Curve Last 12 Months



YOY Inflation 2023 - 2024



SP500 Moving Averages Last 12 mo.



Junk - Treasury Spread



The dashboard has six individual charts, each offering a different perspective on the capital markets. It's designed to give the reader a quick recap of the recent trends for each view of the market.

Drawdowns. The current drawdown from the February 19 high water mark is **6.7%**. We crossed the -10% threshold on March 13 and the market has bounced higher from there. We may revisit the -10% level if investors can't shake off their funk.

Net Up days out of the last 15 is a measure of momentum. This indicator has a tendency to bounce between 6 and 10, with a long-term average of 8 up days out of the most recent 15 trading days. Today it has a reading of **9**. This indicates that short term momentum is positive and the market is trying to recover from its correction.

Treasury Yield Curve. This chart shows the difference between the rate on the 10-yr Treasury bond and the Fed Funds rate. When this indicator turns negative, (the rate on the 10-yr is lower than the Fed Funds rate) it usually signals a recession. The current reading of **-0.2%** means that we have reverted back to a negative curve shape.

YOY Inflation rate. The **2.8%** CPI print for February was not good enough to pacify the Fed. Chair Powell telegraphed this when he said that the Fed doesn't have to be in a hurry to cut rates. The Fed has adopted a more cautious stand since the November CPI came out in December.

Moving Averages are in a positive configuration, where the 50 day moving average is above the 200 day. It takes several weeks if not months of market action to move the needle on this indicator. The spread between these two lines has been narrowing for the last few weeks. The current spread of **2.7%** is below the median of **3.1%**. This indicates that the market is now vulnerable to a deeper pullback.

Junk-Treasury Spread measures how confident bond investors are about the future. This month we see a widening of the spread, from **2.66%** last month to **3.17%** today. (The long-term median spread is **4.0%**.) Today's reading is an indication that yield-seeking investors are not very concerned about taking the risks associated with holding junk bonds.

My Top Stock & ETF picks

In this part of the report, I share the stocks and ETFs that I am either watching closely or already own. What sets these picks apart from my trading strategies and model portfolios is that I do not use an algorithm or an asset allocation scheme. These are just individual picks that I have watched for months, and sometimes years, and I have a pretty good idea of what the upside/downside probability is for each of them.

The best way to use these picks is to consider them as ideas that you can investigate further, using your own methodology and criteria. My watch list has between 50 and 100 names at any given time, and what you see here are the ones I have the most confidence in.

My top 10 stock picks from last year

I publish this list at the end of each year and hold all 10 names for the next 12 months. Mergers, takeovers, or delisting would be the only reasons for me to change this list mid-year. The Zen Ten performed very well in 2024.

2024 Zen Ten stock picks		12/29/23	12/27/24	Gain
ACGL	ARCH CAPITAL GROUP LTD	74.61	92.67	24.2%
AMZN	AMAZON	151.54	229.05	51.1%
CTVA	CORTEVA INC	47.83	57.48	20.2%
HRMY	HARMONY BIOSCIENCES HOLDINGS INC.	31.10	34.06	9.5%
KNSL	KINSALE CAPITTAL GROUP	334.10	470.95	41.0%
MELI	MERCADOLIBRE INC.	1,562.61	1,743.29	11.6%
META	META PLATFORMS INC.	351.32	607.75	73.0%
MHO	M/I HOMES	135.40	136.11	0.5%
MSFT	MICROSOFT	373.86	439.33	17.5%
NVDA	NVIDIA CORPORATION	49.24	140.22	184.7%
Zen Top 10				43.3%
Vanguard Ttl Stock Mkt		237.33	297.12	25.2%

If you are a long-term investor who does not have time to play around in the market, the Zen Ten might be the right model portfolio for you. But if you are more active in the market, there are some decent bargains out there that cannot be ignored. The following two models – one for stocks and one for ETFs – are not subject to the one-year minimum holding period.

Top Picks for April 2025

This list differs from the previous one in the fact that I have the flexibility to make changes to the lineup at the end of each month. Some months there may not be any changes, and other months the complete list could change, although that would be very rare. The suggested holding period for these picks is 12 months or longer. It's not a short-term trading list. If you want trading ideas, follow [this link](#).

This month's top stock picks

Name	Ticker	3/24/25	VQG*
 CELESTICA INC. (XNYS:CLS)	CLS	\$ 99.94	84.8
 InterDigital, Inc. (XNAS:IDCC)	IDCC	\$ 221.60	84.6
 ARES MANAGEMENT CORPORATION (XNYS:ARES)	ARES	\$ 153.75	82.4
 Qifu Technology, Inc. (XNAS:QFIN)	QFIN	\$ 44.45	81.7
 ARTHUR J. GALLAGHER & CO. (XNYS:AJG)	AJG	\$ 337.67	82.2
 S&P 500 INDEX	INX	5767.57	

*VQG is the combined scores for Value, Quality, and Growth. 100 is the max score.

This Month's Top ETF picks

Name	Ticker	3/24/25	Rating*
 ETC 6 Mrdn Mega Cap Eqty (ARCX:SIXA)	SIXA	\$ 46.62	92.7
 iShares:Gold Trust (ARCX:IAU)	IAU	\$ 56.71	93.1
 FT:US Equity Opptys (ARCX:FPX)	FPX	\$ 120.95	87.8
 Invesco Dorsey W SC Mo (XNAS:DWAS)	DWAS	\$ 82.47	88.6
 iShares:MSCI USA Qu GARP (BATS:GARP)	GARP	\$ 53.90	84.6
 S&P 500 INDEX	SPX	5767.57	

*Rating is based on momentum and money flow. 100 is the max score.

Asset allocation

Our Current Asset Allocations as of 3/25/25

I made no changes to the models this month. Last month I made two changes. Cash increased to 7% from 5% the prior month. Stocks went from 55% down to 53%. The model portfolios are tactical in the sense that they reflect changes in my bullish/bearish posture towards various asset classes and the stock market as a whole. They are designed to minimize short term trading and are meant for long term investors.

The cash allocation of 7% is slightly above average for a bull market like we're in now. I want to have cash on hand to take advantage of opportunities as they present themselves. The recent data on earnings expectations, the economy, and the stock market are coming in weaker than anticipated.

Asset Class - Taxable	Percent Allocation
Summary	
Stocks	53.0
Bonds	30.0
Commodities	7.0
Cash	7.0
Non-traditional assets	3.0
	100.0
Details	
US Large Cap Stocks	8.0
US Mid Cap Stocks	12.0
US Small Cap Stocks	12.0
US Stocks Total	32.0
Intl Developed Mkt Stocks	9.0
Intl Emerging Mkt Stocks	12.0
Non-US Stocks Total	21.0
US Core 1-5 yr Treasury Bonds	8.0
US Muni Bonds	3.0
US IG Corporate Bonds	7.0
US High Yield Bonds	3.0
US Bonds Total	21.0
Intl Developed Mkt Bonds	5.0
Intl Emerging Mkt Bonds	4.0
Non-US Bonds Total	9.0
Cash Total	7.0
Energy	2.0
Precious Metals	5.0
Commodities Total	7.0
Hedging Vehicles	1.0
Private Equity	2.0
Non-traditional assets Total	3.0
	100.0

Asset Class - Deferred	Percent Allocation
Summary	
Stocks	52.0
Bonds	28.0
Commodities	8.0
Cash	7.0
Non-traditional assets	5.0
	100.0
Details	
US Large Cap Stocks	7.0
US Mid Cap Stocks	11.0
US Small Cap Stocks	12.0
US Stocks Total	30.0
Intl Developed Mkt Stocks	9.0
Intl Emerging Mkt Stocks	13.0
Non-US Stocks Total	22.0
US Core 1-5 yr Treasury Bonds	8.0
US Muni Bonds	0.0
US Corporate Bonds	8.0
US High Yield Bonds	4.0
US Bonds Total	20.0
Intl Developed Mkt Bonds	4.0
Intl Emerging Mkt Bonds	4.0
Non-US Bonds Total	8.0
Cash Total	7.0
Energy	2.0
Precious Metals	6.0
Commodities Total	8.0
Hedging Vehicles	2.0
Private Equity	3.0
Non-traditional assets Total	5.0
	100.0

As of 2/25/2025

Asset Class Weighting

	Under	Neutral	Over
Cash			↑
Equities		↔	
US large cap growth		↔	
US large cap value		↔	
US mid cap			↑
US small cap			↑
Intl developed markets		↔	
Emerging markets		↔	
Bonds			↑
US Treasuries			↑
US TIPS		↔	
US Munis		↔	
US IG corporate			↑
US high yield		↔	
EM US currency		↔	
EM local currency		↔	
Alternatives		↔	
Precious metals			↑
Energy			↑
Private Equity		↔	
Hedging vehicles	↓		

As of 2/25/2025

Final Thoughts

My analysis indicates a strategy that buys stocks after a 10% drawdown would deliver higher returns than those waiting for 15% or 20% declines. Historical performance is no guarantee of future results, but waiting for larger drawdowns risks being out of the market should it bounce back quickly. My back-testing analysis since 1975 showed that a strategy that increases equity exposure after a 10% correction delivered the highest return and Sharpe ratio (which measures the risk-adjusted returns of a portfolio) compared to those that wait for 15% or 20% drop. Even though losses can be significant at a -10% entry, they have historically been more than offset by other periods when equities rebound quickly.

My view, therefore, is that investors should buy the dip, if and when the S&P 500 reaches -10% again. (The -10% level is 5530.)

Until next time,

Erik

Appendix

The Data Driving the Equity Market Traffic Lights

Fundamentals are green. Revenues, earnings, and profit margins are improving. Credit conditions are tight but loosening of late.

Technical are yellow, indicating near term caution while still supporting a healthy longer term outlook. Bear in mind that these technical readings are prone to quick reversals during counter-trend rallies and corrections.

Valuation remains stuck on red as it continues to be the biggest threat to the market. High valuations alone can't trigger a bear market. They need help from the other factors.

Risk is yellow. While the threat of recession is low, it remains a possibility, especially if the Fed makes a serious policy error.

Fundamental

Revenue & Earnings

Profit Margins

Credit Conditions

Oct	Nov	Dec	Jan	Feb	Mar est
3	2	2	2	3	3
3	2	2	2	3	3
4	4	4	3	2	2

Technical

Momentum

Breadth

Leadership

Oct	Nov	Dec	Jan	Feb	Mar est
3	3	3	3	4	6
4	4	4	4	3	3
3	3	4	5	4	4

Valuation

Price Ratios

Risk Premium

Return Ratios

Oct	Nov	Dec	Jan	Feb	Mar est
7	8	8	8	7	7
7	8	8	8	7	7
6	7	7	7	6	6

Risk

Recession Threat

Bear Mkt Threat

Volatility

Oct	Nov	Dec	Jan	Feb	Mar est
3	3	4	4	4	4
2	2	2	3	3	3
4	4	4	5	5	6

The Data Driving the Recession Warning Traffic Lights

Where do the traffic lights get their signals? From a set of coincident indicators shown in this table. The numbers range from 1-10, with 1 being the best possible condition for each indicator. The benefit of showing this board is that it tracks the trend of each indicator over the last 6 months.

Readings higher than 7 will be highlighted in red.

When the board begins to turn from green to

yellow, it's time to adopt a more defensive posture. But for now, stay fully invested, with perhaps 5% cash.

Recession Watch

Indicator	Oct	Nov	Dec	Jan	Feb	Mar est
R-Score	3	3	3	3	3	4
Employment	4	3	3	3	3	3
Ind Production	4	4	4	4	3	4
Credit & Debt	5	5	6	5	6	6
Market Trend	3	3	3	3	4	5
Market Stress	4	4	4	5	6	6
Earnings Trend	2	2	3	2	3	3

R-Score. This indicator combines the treasury yield curve, inflation, and unemployment. It's listed first because it has the strongest predictive value of all the indicators on this board.

Employment. Year-over-Year % Change in private non-farm employment.

Ind Production. Year-over-Year % Change in industrial production.

Credit & Debt. Difference between Junk bond and Treasury bond yields.

Market Trend. Year-over-Year % Change in the S&P 500 index.

Market Stress. Combination of stock market price change and the Year-over-Year % change in the unemployment rate.

Earnings Trend. Year-over-Year % change; Beats; Revisions; Analyst rating upgrades.

How to use the data tables

The numbers in the data tables may look a little simplistic but rest assured that quite a lot of thought and effort went into translating the raw data coming out of government and industry sources and putting them in a format that is simple and intuitive to grasp. Each of the numbers is an expression of the percentile rank (deciles) for the category.

I could have, for instance, just reported the raw numbers as published, but that would assume that readers could gauge the significance of the raw numbers. If you happen to have an advanced degree in macroeconomics, it might work for you. But for the rest of us, I think simple is better.

The way I recommend using the data is to scan each line and look at the changes in trend. If you notice that an indicator has recently changed direction, you might want to find out why. And whether it's significant in the larger picture.

I went a step further and created a traffic light metaphor to summarize what all of the individual indicators were saying. The probability speedometers do something similar, by taking lots of raw data points and converting them into a single number that represents the likelihood that an event – a bear market or a recession – might arrive within the next 4-6 months.

All of this work is in the service of one thing – managing the asset allocation and risk profile of your portfolio. As the risks increase, so should your cash and hedging positions. When risks are low, you can be as aggressive as your investment plan allows.

As always, comments and questions are encouraged.