Strategy Update—Uncertainty Reigns Supreme

Cullen O. Roche
Founder
Orcam Financial Group, LLC
cullenroche@orcamgroup.com

Markets are trading again in the USA after a brief hiatus following the storms on the east coast. But the story hasn't changed much in our opinion. Uncertainty is still the story of the day.

3 Uncertainties Reign Supreme

It's been our opinion for many weeks now that the market was vulnerable to downside as uncertainty crept into some of the major catalysts occurring currently and in the coming months. Specifically, we're seeing increasing uncertainty around corporate earnings in real-time. In addition, we believe the uncertainty around the fiscal cliff and the US Presidential election are leaving investors wary about positioning themselves.

On the earnings front we're seeing mild weakness. Revenues are down –3.2% year over year while operating earnings are up just 2.6%. This is a big change from the profit boom we've seen since 2009. And the risk to corporate profits is increasing as the fiscal cliff looms.

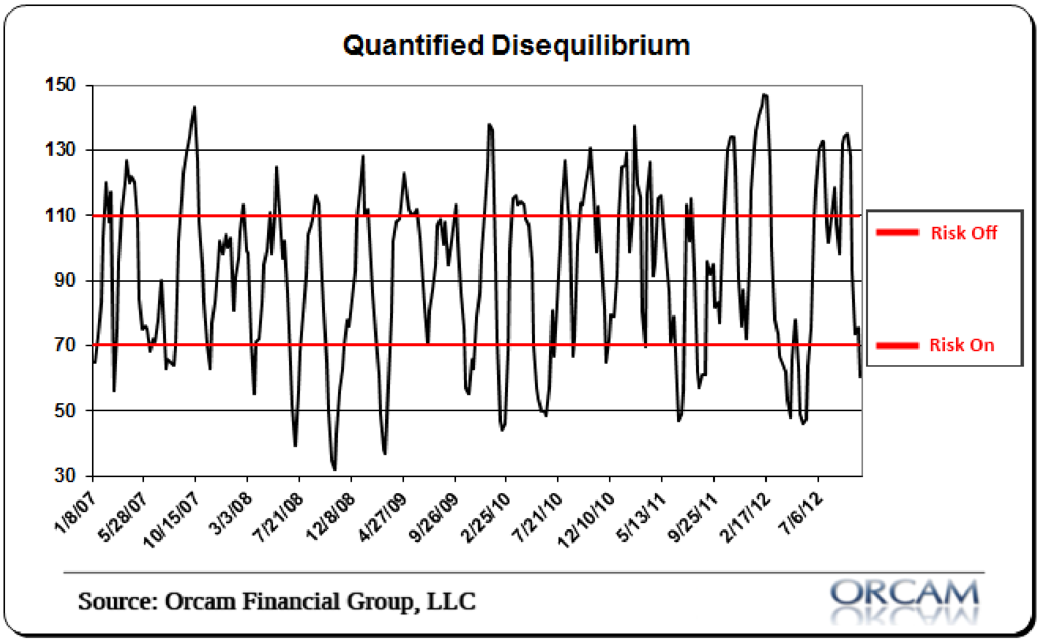
For now, it is looking like the election is swinging back in favor of Obama. His odds are back to 65% at Intrade, but we don't think the markets will feel secure about this until the results are tallied. And then the attention will turn to the fiscal cliff. The timeframe for the cliff resolution is less certain. Congress is unlikely to get anything done before the Thanksgiving holiday so we're likely looking at early December to mid-December at the earliest.

(continued…)

Long story short—Uncertainty will reign supreme for several more weeks….

The Equity Model—More Constructive

Our primary equity trading model has turned considerably more constructive in recent weeks, but has not yet offered a buy signal. We use this model for several different purposes. For short-term strategies we use it as a risk management tool designed to help us stay out of the market when the market appears excessively risky and to buy when the market's risk/reward appears more favorable.



In longer-term strategies we use the QD model for what we call "efficient dollar cost averaging" by staying patient and reinvesting/contributing to long-term strategies when the market's risk/reward becomes more favorable.

As mentioned, the current readings are considerably more constructive, but still not consistent with a buying environment. We have found that the model is most predictive when momentum in the indicators becomes positive. For now, the model is still consistent with our uncertain outlook and potential for further downside. We would not be shocked to see the markets turn in the coming weeks and end the year with their traditional slow crawl higher….

Of course, the QD model is not a holy grail and should never be viewed as such, but rather helps us round out our overall macro view of the markets and more general investing perspective. As we've stated in previous notes, we remain mildly constructive on the US economy and do not yet see recession so the downside in the economy is unlikely to be sizable here (assuming our estimates for the fiscal cliff are correct).

We'll keep you updated.

If you ever have questions or comments on research or Orcam's services please contact us directly.

Orcam Financial Group, LLC

Orcam Financial Group, LLC is a fee only financial services firm offering macro research, personal advisory, institutional consulting and educational services.

Important Disclaimer

ORCAM