During April, the stock market continued its upward trend with both the S&P 500 Index and the NASDAQ Composite Index setting new all-time highs during the third week of the month. While not all of the major averages set new highs, most of them were near their highs—with small cap stocks being one of the exceptions. The market was buoyed by good company earnings reports and the Federal Reserve's more dovish stance on monetary policy.

Interest rates edged upward in April but still remained well below levels at the beginning of the year. The 10-year U.S. Treasury Note rose from its late March low of 2.37% to 2.51% at the end of April but was still below its 2.78% level at the beginning of the year.[1] Credit spreads have once again narrowed, which is a positive. In addition, the percentage of S&P 500 stocks that have a higher dividend yield than the 10-year U.S. Treasury Note rose to 45%, the highest level in almost two years[2] and attributable to lower interest rates.

One negative factor in our work was that investor sentiment got more optimistic as the market climbed (which is negative from a contrary point of view) and bullish sentiment has now reached its highest level of the year. While this could indicate that the market is subject to a correction of 2% to 4% at any time, valuation and monetary/credit conditions are still neutral to positive and the strategy's momentum models are still trending higher. Thus, we held our market exposure steady in April in order to take advantage of the market's strength.

Our assessment of the four pillars of our investment process is as follows:

1. **Valuation:** Valuations have crept up as the market rallied earlier in the year. The S&P 500 median price-earnings ratio now stands at 22.2, higher than its low point in the fourth quarter of 2018 but still below its 15-year high of 26.8 reached in January 2018. In addition, the percentage of stocks in the S&P 500 that have a dividend yield higher than the 10-year U.S. Treasury Note rose to 45%, the highest level in almost two years.[3] When adjusted for the recent decline in interest rates, valuations now appear to be more reasonable.

2. **Monetary factors and credit conditions**: Interest rates ticked upward in April after declining during the first quarter. The 10-year U.S. Treasury Note rose to 2.51% from its March low of 2.37%. Nonetheless, the 10-year still remains below its early January 2.78% high and well below the 3.24% level reached in the fourth quarter of 2018.[1]

   Another positive on the monetary and credit front is that credit spreads have once again begun to narrow. Future economic weakness and a subsequent adjustment in stocks will likely be signaled by rising credit spreads and we have not seen that happen yet.[3] Nonetheless, we will be watching credit spreads closely in coming months.

3. **Sentiment:** Bullish investor sentiment has increased since the beginning of the year (which is a negative development from a contrary point of view) and has now risen to the highest levels of 2019. These levels often indicate elevated downside risk.[3] However, we would note that our models show that it is the professional traders and investors who have gotten more bullish. The retail and public sentiment measures may have to reach a level similar to that of the professionals before the next market correction would occur.

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4. **Momentum:** Our longer-term volume and breadth momentum measures continued to be positive during April.[3] So far, our momentum models have shown good up volume and breadth on the early 2019 rally. Coupled with declining interest rates and lower valuations, this is a favorable backdrop for the stock market.

   One potential negative, however, is lagging participation as measured by the Russell 2000 Index. The Russell 2000 is stuck at its recent highs and as has not set a new high, which points to a potential divergence. The Russell 2000 would need to break out above these levels to give more life to the overall market. A continued rally in large cap stocks without broader participation by the rest of the market would be a concern.

[1] *Source: U.S. Department of Treasury. April 30, 2019*
[2] *Source: Ned Davis Research. March 31, 2019*
[3] *Source: Ned Davis Research. April 30, 2019*