Market Strategy Weekly

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Senior Technical Strategist Todd Sohn breaks down recent stock market weakness and a mixed investor sentiment picture, highlighting an unloved sector that is starting to outperform.

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MARKET SELLOFF | SENTIMENT CHECK | A SECTOR TO BUY

ROSS MAYFIELD: How are you assessing the current market volatility that we've seen in recent weeks?

TODD SOHN: We've had a real speed bump in the markets, and I think it's more rotational than anything. Some areas like small caps, high beta, and high-flying momentum-type names have traded down, but not enough to hit the overall market too badly. So, not really "oversold" yet, leaving us in a bit of an uncomfortable tactical position. Normally, when you have a selloff, you like to see the put/call ratio spike (investors buying protection), you want to see the VIX curve invert (near-term VIX futures contracts becoming pricier than longer-term contracts, indicating a high level of immediate-term anxiety), and you want to see 20-day lows spike (a large number of stocks trading down, indicating broad-based selling). Those conditions usually present a buying opportunity in a global bull market like this one. We just want to stay patient and look for those oversold conditions to start adding to equities into the first quarter of the next year. The one thing to keep an eye on is the credit market. The private capital stocks have been weaker, and I wonder if that starts to leak into broader credit markets. If credit spreads start to widen out with stocks rallying, that's a little bit more concerning. But for now, I think you want to stay the course.

ROSS: How does sentiment play into that calculus? What are you seeing in terms of bullish vs. bearish sentiment out there?

TODD: Well, we've definitely seen some air come out of the leveraged corners of the market. Leverage has been rampant lately, which raised some red flags for us. But now you are seeing these high flyers sell off, so that's good. If there's one risk that's out there in terms of sentiment, we do see acceleration in the money flowing into stock market ETFs recently. We're seeing about $5 to $5.5 billion dollars per day—meaningfully higher than any of the last few years. So, flows are hot, but I do like seeing these levered corners compress…it's almost a necessary condition to get that overall sentiment temperature lower going forward.

Equity ETF flows are heating up

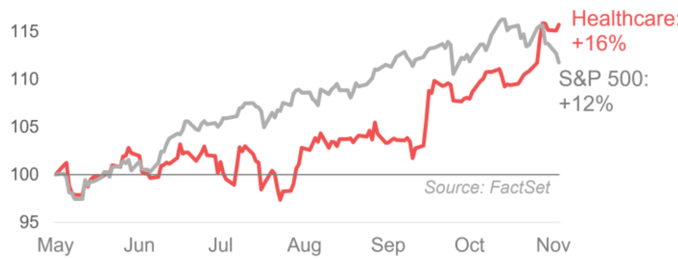
Year of Bull Market	Average Daily Inflow
Year 1	$1.3 billion
Year 2	$2.6 billion
Year 3	$3.4 billion
Year 4 (so far)	**$5.6 billion**

Source: Strategas, Bloomberg

ROSS: If this is a rotational market, where do you see opportunity?

TODD: We love Healthcare right now. It's been ice cold on the sentiment front—Healthcare sector ETFs have seen major outflows over the last year. It's a sector that has frankly not worked for quite some time. But we think there's a lot of runway here, especially if you're looking to play a little bit of a defensive tilt. Healthcare can carry those types of characteristics, especially in the pharma and equipment space. So, we're very opportunistic in Healthcare, especially as a way to water down Tech and Growth exposure. We think there's meaningful runway before the sector becomes too overcrowded, and there's a lot of negativity to reverse. It's also a significant weight in the S&P 500 which might help offset any sort of weakness you might see from the top of the index.

Healthcare is now outperforming over the last six months



This conversation is lightly edited and consolidated from an interview located at www.youtube.com/@BairdTV.

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