Morgan Stanley Issues Rare "Sell" Signal, Are You Prepared?

By Brad Lamensdorf, Co-Portfolio Manager, AdvisorShares Ranger Equity Bear ETF (HDGE)

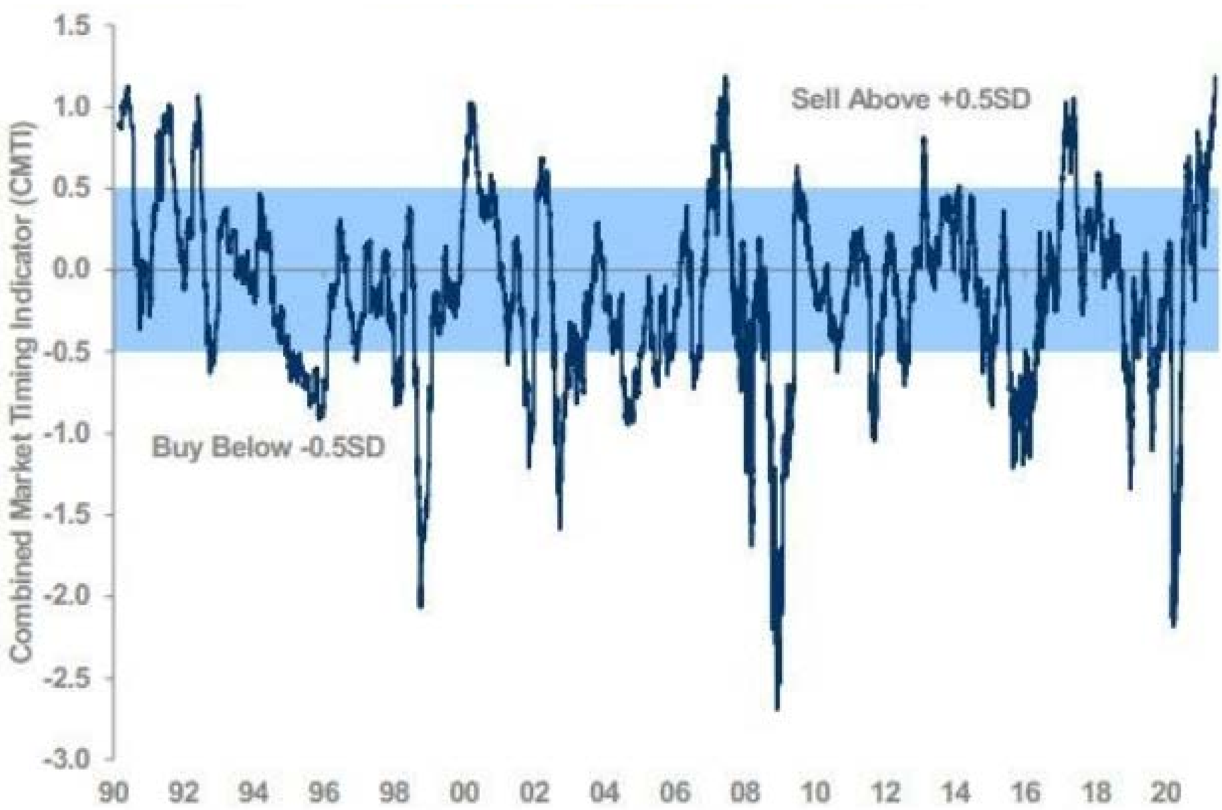
In June of 2021, Morgan Stanley Research issued a rare "sell" signal on the U.S. market: "*For only the fifth time in over 30 years, each of Morgan Stanley's five market timing indicators are giving a sell signal at the same time.*"

Additionally, on September 21, 2021, Morgan Stanley's Chief Investment Officer, Mike Wilson, appeared on CNBC discussing how a 20% market correction seems likely.

Are you prepared?

As the chart below shows, Morgan Stanley's composite market timing indicator has reached new highs, which is bearish for the markets. Previous major signals include 1990, 2000, and 2007, which all preceded dramatic declines in equity indexes.

Exhibit 1: Morgan Stanley's Combined Market Timing Indicator is in-line with its all-time high…

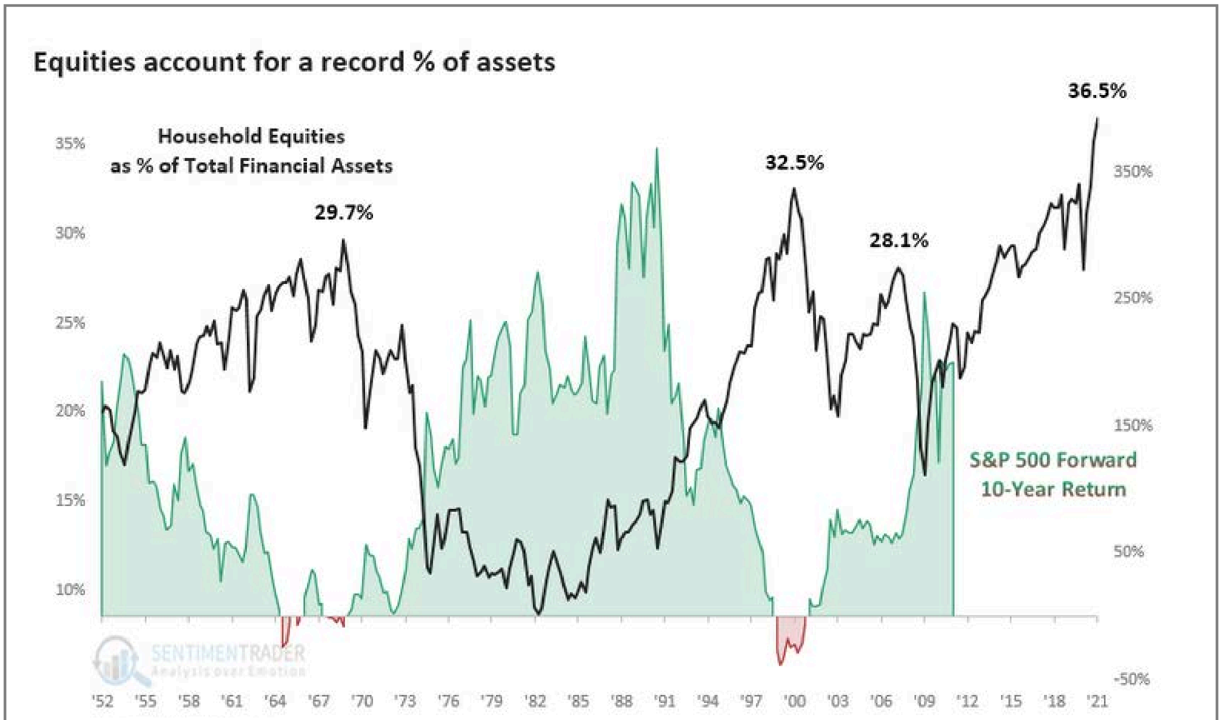


Source: MSCI, Morgan Stanley Research.
SD = standard deviation

While the historical track record of this signal is impressive, current conditions in the market suggest that the next decline could be fierce.

Consider that U.S. households are fully invested in equities, and margin debt is exploding. Both are contrary indicators.

As the following chart illustrates, household equities as a percent of total financial assets have hit a new high of 36.5%.



Source: SentimentTrader, Federal Reserve.

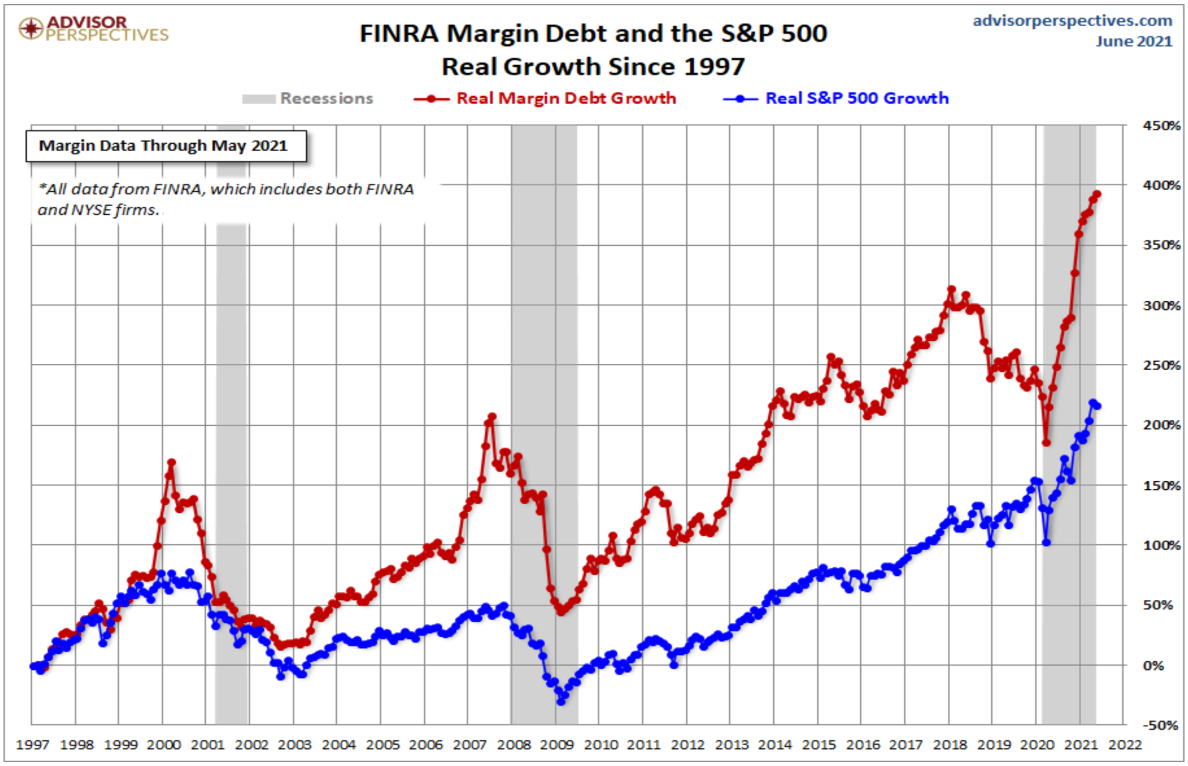
This tops the previous highs of 29.7% in the late 1960s and 32.5% near the turn of this century that preceded negative 10-year annualized returns in the market.

Quite simply, households are loaded to the gills in equities. Their holdings are more than double that of 2009, which represented a generational buying opportunity in stocks. That cycle may be coming to an end.

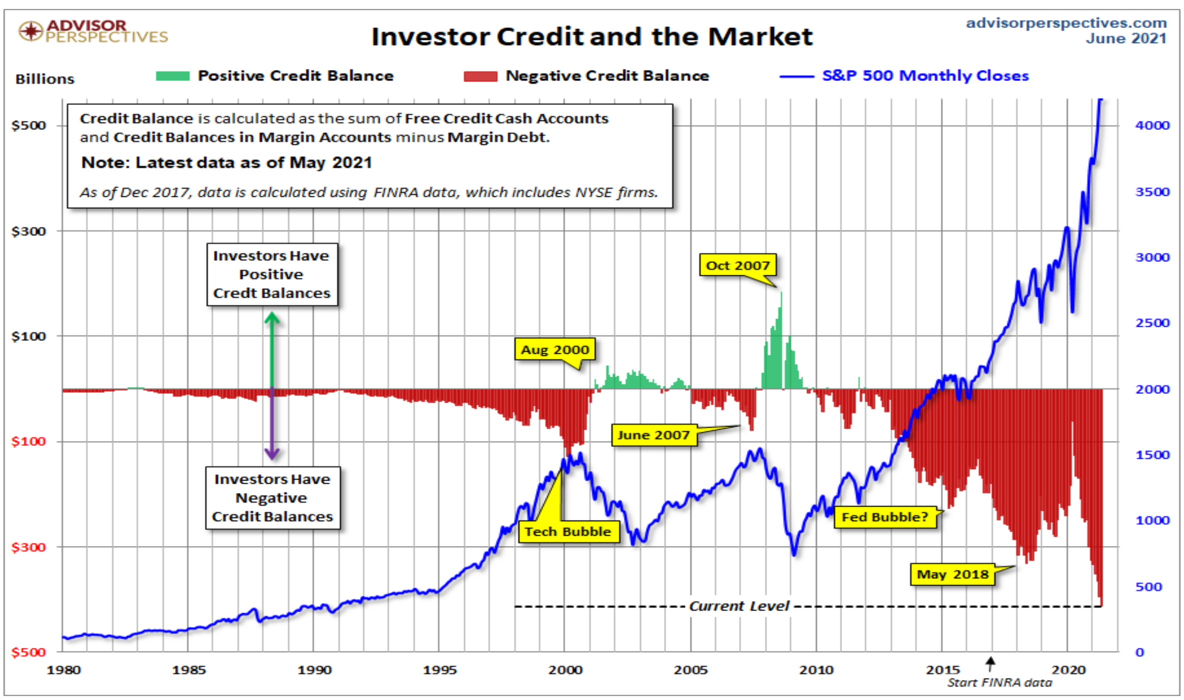
Should the cycle be coming to an end, leverage will only add fuel to the fire. The amount of margin debt has exploded and in real dollars is outside the norm of historical ranges.

Real growth in margin debt is literally off the charts. The following charts, courtesy of Advisor Perspectives, show that real growth in margin debt has dramatically outpaced the rally in U.S. stocks over the past 12 years.

The trend has accelerated since the COVID lows were hit last year.



Lastly, negative credit balances far exceed previously known bubbles.



The unwind is likely to happen swiftly and with tremendous damage. Morgan Stanley is making a rare bearish call on the market. ***Are you prepared?***

***Standard deviation** measures the dispersion of a set of data from its mean and is calculated as the square root of variance.*

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