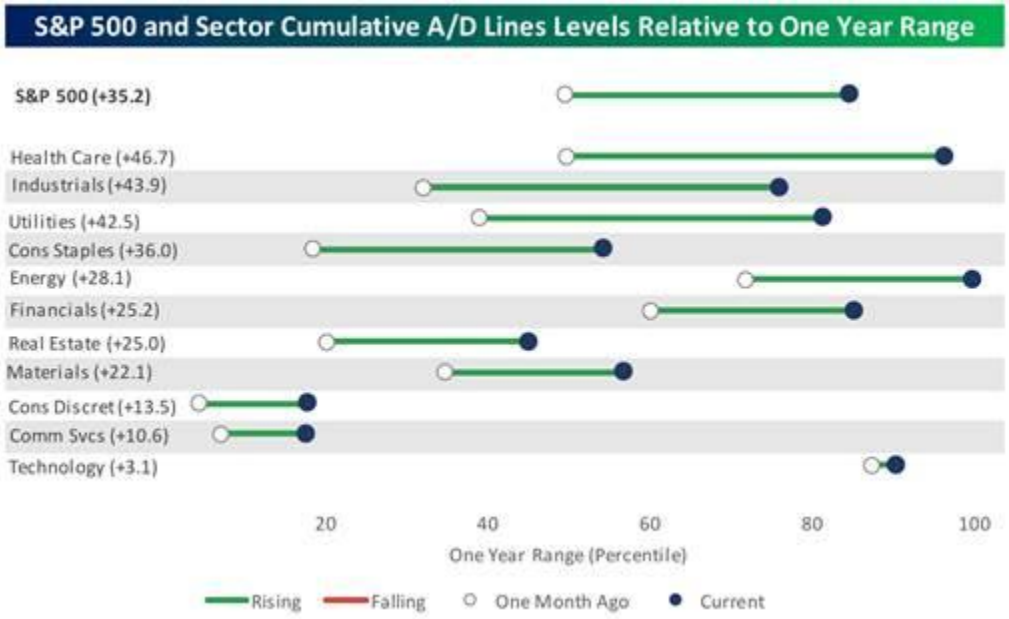
# CJ's Weekly Market Memo

**All That For A Penny?**

October 31, 2026

I have spent decades as a professional investor, and the most useful distinction I have learned is between the stock market and the market of stocks. October demonstrated that distinction about as well as any month I can remember. In their latest report, Bespoke writes that the S&P 500 closed the last trading day of May at 7,580.06 and the last trading day of October at 7,580.07. Five months of record highs, one-day disasters and anxious headlines produced a change of one penny. While the index stood still, the average S&P 500 stock rose nearly 5% in October as technology and communication services fell sharply. Many investors now ask whether the bull market has been slain. I vote no. The money leaving the AI leaders has rotated into the rest of the market, and a market in rotation rather than liquidation is exactly how an index can churn in place for five months. As the chart below shows, that rotation has reached every sector.




*S&P 500 and sector cumulative advance-decline lines relative to their one-year range, end of September versus today. Source: Bespoke Investment Group.*

## Market Technicals

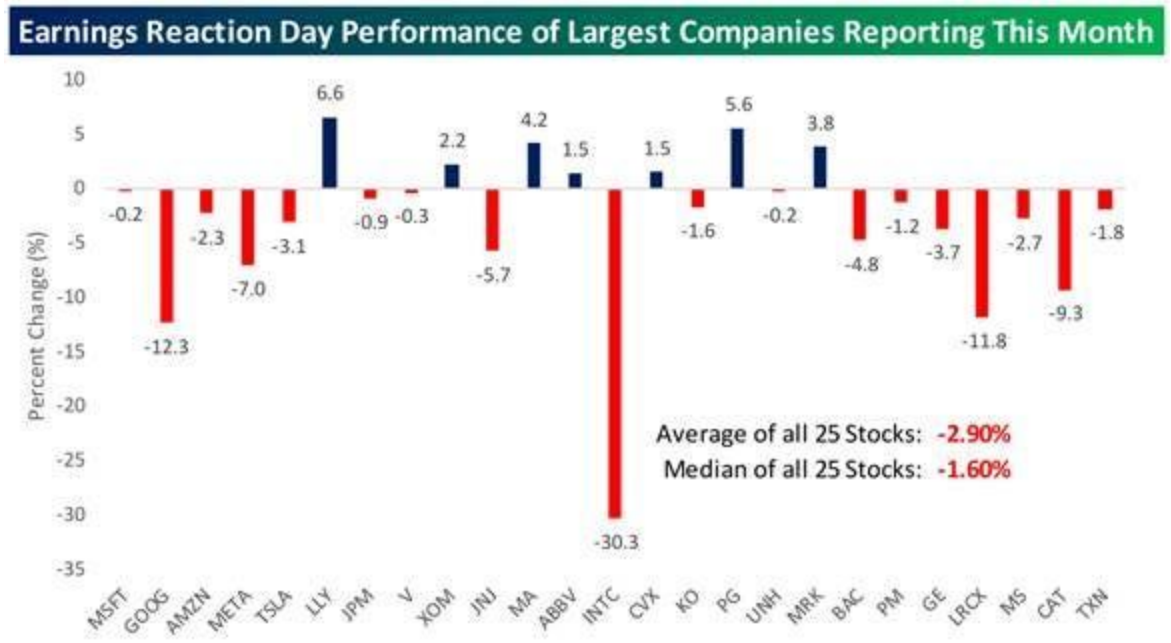
With the major indices seemingly churning in place all summer, the market of stocks continued under accumulation. Bespoke shows the cumulative advance-decline line improved during October for the S&P 500 and for every one of its eleven sectors. And the percentage of S&P 500 members above their 200-day moving average held above 50% last week, confirming the turn higher in the cumulative advance-decline line I noted in my last letter. I have constructed a variety of research and tracking models to help with stock selection. In one of those models, built on Stan Weinstein's stage analysis, I follow 139 stocks of interest to me. As the rotation out of technology into other sectors continued last week, the model cut the names it rates in Stage 2, the advancing phase, from 87 of 139 to 58. Nearly all the demotions were in semiconductors, semiconductor equipment, mega-cap growth and momentum funds. Healthcare, consumer staples, energy and travel companies held their ground. According to Weinstein, that is distribution in the leaders and accumulation in the rest.

Some of my other models that govern my exposure to the S&P 500 itself say something different, and the difference matters. The stage work mentioned above tells me which stocks to own. My combination allocator, which weighs the bond market, a five-indicator model of the S&P 500 and investor sentiment, tells me how much cash to hold in the total portfolio. The week finished at Caution, indicating a continuing high level of cash. My version of William O'Neil's market gate counts the distribution days, those that betray institutional selling, and it has both the S&P 500 and the Nasdaq 100 in a correction. Neither index has seen the panic that usually marks a final low. My breadth gate, based on Paul Desmond's work at Lowry Research, has recorded no 90% down day, the selling climax Desmond found at major lows. Nor did new yearly lows on the New York Stock Exchange approach the level I treat as capitulation. Beyond last week's decline, Bespoke singles out semiconductors and memory as the groups that will decide the direction of the major indices. They point out that the Philadelphia Semiconductor Index finished the week sitting on its 200-day moving average. A break of that line would probably mean the final bottom in technology still lies ahead. A follow-through day on the O'Neil gate or a 90% up day on the breadth gate would tell me the leaders have finished their corrective phase.

I have traded through this kind of market before. From 2000 through 2002 the dot-com leaders declined for nearly three years while a great many companies left for dead during the boom recovered and advanced. Had I remained long those leaders, I would have missed the rally in everything else. The situation is similar enough today, and late last week I began to act on that similarity. I bought a few stocks and added to positions in the stronger areas, particularly healthcare and consumer discretionary companies tied to travel. My stage work shows both groups firmly in Stage 2. Additions of ETFs representing the indices themselves can wait for my allocation models to fire an all clear or buy signal.

**Market Fundamentals**

My call for a mid-October low was wrong. It took a recent conversation with a colleague about market psychology to make me realize my analysis had not been careful enough. I depended too heavily on the seasonal calendar when I should have studied the earnings calendar. The companies with the greatest influence on index prices did not report until the end of the month. The reports from the largest AI companies at month end, Alphabet in particular, were the obvious catalyst for a washout in the major indices. Alphabet suffered its worst session since its IPO in 2004. Of the 25 largest companies reporting in October, Bespoke counts only seven that rose in price on their earnings results. The expected decline came, not in the middle of the month but two weeks later, and it confined itself to the leaders. It was not yet the panic in breadth my index models look for at a final low.




*Earnings reaction day performance of the 25 largest S&P 500 companies reporting in October. Source: Bespoke Investment Group.*

Some of the people I discuss the market with insist the market is wrong. The economy is strong, they argue, and the AI earnings are sure to come. I believe they miss the point. The market is discounting a heightened level of uncertainty concerning those expected future earnings. That uncertainty arrived through the rising cost of credit for the weaker AI borrowers, raising the level of future return needed to offset the higher cost. The largest companies can fund their building from free cash flow. The riskier AI businesses cannot. They now need new debt to keep building, and the interest on that debt is a growing burden. Companies such as CoreWeave and Nebius depend on a steady flow of credit to finance their data centers. The market is pricing this new risk by marking down the companies most exposed to it. The adjustment has been severe, and Bespoke's basket of these neoclouds has lost more than half its value since June. Last week I named that debt one of my two legitimate worries. It has now tainted the outlook for the entire sector. Although stronger AI stocks do not deserve this taint, most AI stocks were priced for perfection. Investors had begun to demand impossible outcomes. In hindsight, given unexpected, potentially unsupportable debt and extreme pricing, the current selloff in the sector was inevitable. The final selloff may still lie ahead. Should it come, it should be short and sharp, leaving conditions clear for a resumption of the rally in the indices and the market of stocks.

So far the damage is confined to the investment markets. The economy is sound. Companies beyond the largest names have touted strong results this season, with far more raising guidance than lowering it. This bodes well for future economic growth. And currently new claims for unemployment remain very low. With earnings expectations rising and the S&P 500 flat since May, my valuation work will soon rate the index below fair value. Even the bond market is cooperating. My bond model shows bond prices rising and long-term yields falling. Bespoke attributes the decline in the 10-year Treasury yield to concern that the AI boom is peaking, which would ease the industry's heavy demand for capital. All of that is good news for the market of stocks. It does little for the second-tier AI companies, whose problem is the price of their own credit. Inflation is the exception, still running hotter than the Warsh Fed would like, with futures market pricing still anticipating another rate increase in December.

**Prognostication**

All of this leads me to the following conclusions. My two confirmations, fundamental and technical, agree about the market of stocks. The technicals show accumulation, and the economy beneath it is sound. They agree less about the S&P 500 and the Nasdaq. My index models say the decline in the leaders may not be complete. The fundamentals say the AI sector must still digest higher financing costs and expectations have run well ahead of results. So, I am confident about the direction of the market of stocks and less certain about the timing of a bottom in the largest names. I may yet be proven wrong about the leaders, they may find their footing at support this week. Should the semiconductors instead break down and drag everything else with them, I will have been early in my buying and my optimism premature. For that reason I have kept early buys small, leaving plenty of cash in the portfolio.

This seems an appropriate week for a reminder I need as much as anyone. Traders like to say the market is never wrong. Benjamin Graham saw it differently. His Mr. Market is moody, swinging from mania to depression. After the mania that priced the AI leaders for perfection, he now suffers the depression that inevitably follows. Graham meant that Mr. Market's moods are merely offers, which an investor is free to accept or decline. Graham lets an investor decline the price. He does not let him deny it. So as an investor I need to decide whether to buy or sell based on the current price. If I as an investor let my ego interfere with my judgment, I may decide the market is mistaken and wait for it to come around to my view. That judgment may prove expensive. The most important part of any market outlook is to leave ego out of it entirely. The market is going to do what it is going to do. The outcome of my investment decisions is determined by how I react to the market's movement, not by how the market acts.

**S&P 500 Years Most Similar to 2026**

| | Correlation | S&P 500 YTD Gain | S&P 500 Performance From 10/30 | | |
|---|---|---|---|---|---|
| Year | Coefficient | Through 10/30 | Rest of Year | Max Gain | Max Loss |
| 1935 | 0.91 | 30.1 | 8.7 | 8.9 | 0.0 |
| 1989 | 0.91 | 20.7 | 5.5 | 5.5 | -0.7 |
| 2003 | 0.90 | 19.0 | 6.2 | 6.2 | -1.3 |
| 1978 | 0.89 | 0.0 | 1.1 | 2.6 | -2.7 |
| 1954 | 0.89 | 27.7 | 13.6 | 13.6 | 0.0 |
| 1933 | 0.89 | 30.6 | 10.3 | 14.0 | -0.9 |
| 1997 | 0.88 | 22.0 | 7.4 | 8.9 | 0.0 |
| 1995 | 0.86 | 27.0 | 5.6 | 6.6 | -0.3 |
| 2021 | 0.86 | 22.6 | 3.5 | 4.1 | -2.0 |
| 1968 | 0.86 | 7.1 | 0.5 | 4.9 | -0.2 |
| 2026 | | 11.1 | | | |
| **Average** | | **20.7** | **6.2** | **7.5** | **-0.8** |
| **Median** | | **22.3** | **5.9** | **6.4** | **-0.5** |
| **Percent of Time Positive** | | | **100%** | | |
| **Average (All Years)** | | **5.9** | **2.4** | **5.3** | **-2.9** |
| **Median (All Years)** | | | **3.4** | **4.8** | **-1.4** |
| **Percent of Time Positive** | | | **68%** | | |

*S&P 500 years most similar to 2026 and their performance from October 30 through year end. Source: Bespoke Investment Group.*

In closing, please note the calendar now favors the investor. In my experience the period from mid-October to mid-April is usually the stock market's strongest, and Bespoke notes that the ten years whose path most closely resembles 2026 all advanced from here into year end. I believe longer term investors should probably remain invested. The elections are this Tuesday, November 3. I have learned to divorce politics from my investment decisions, and with the elections looming that discipline matters. Brazil's presidential election in October, where the betting favorite lost both rounds, is a fair warning against investing on a forecast of political outcomes. My book Investing in the Second Wave is due out on election day and can be found on Amazon and at

investinginthesecondwave.com. If you want to learn more about the methods that have sustained my investing over the last five decades, pick up a copy.

**CJ Brott**
*Chairman Emeritus, Capital Ideas*

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