**Jared Dillian: Trading Sentiment**

Jared makes a living trading human emotions in the market.

Technical analysis matters a little because it relates to emotion. Fundamental analysis doesn’t matter at all…

Jared went to a Coast Guard University and had to spend two years at sea. Shortly after that, he married an archeologist. Soon he wound up in San Francisco and got a job at a San Francisco options exchange. This was 1999, an incredible time to learn the markets.

Jared saw speculation in its purest form. That’s where Jared built his ideas on sentiment.

He was there for the end of the tech bubble, and soon applied for a Wall Street banking job. He wound up at Lehman Brothers. He did index arbitrage, which was a dying trade at the time. It was going electronic, but Jared was doing it by hand.

Jared was profitable because he had a sixth sense of when trades would reverse.

Soon he wound up day-trading S&P 500 futures. His process was extremely involved. He was making $10,000 a day, and his job survived through layoffs.

Next, he was at the ETF trading desk. Being an ETF trader in the 2000’s, Jared says, was Wall Street’s most stressful job.

Jared noticed sell orders came in at the lows and buy orders came in at the highs. This was an expression of sentiment.

Jared got a diagnosis of bipolar disorder while at Lehman’s. He has since been on a quest to be as emotionally healthy as possible. And this introspection has led to his understanding of sentiment.

Lehman’s went bankrupt in 2008 and Jared started his newsletter.

Millions of traders make the worst possible decisions at the worst possible times because of emotions. It’s a predictable cycle. And folks underperform the broad index.

Most financial education has focused on making investors “rational” but that’s an impossible ask. You can’t divorce from your feelings. You must instead profit on the irrationality of others.

Investors should do the opposite of what everyone else is… but it’s not that simple.

It takes years of practice and resisting your instincts.

The average investor has underperformed significantly since 1999 to 2019. This is because of emotion. Bull markets make people overcommit. And bear markets make people sell at lows. That’s the opposite of what you should do.

Sentiment investing addresses these problems. You can be objective but accepting of your own emotions about the market.

It puts emphasis on qualitative data, anecdotes, headlines, and magazine covers. It lets you be in the ballpark of market shifts, and you can subtly change allocations to get better returns.

You need to take in all sensory inputs – tv, radio, social media, offhand discussions with people at conventions. Keep your eyes peeled at all times.

Jared looks for enthusiasm, hubris. He looks for people who make money disproportionate to effort. He looks for a lack of critical thinking, and extreme happiness and sadness.

Sentiment trading is not taken seriously by Wall Street, because it is unquantifiable. But the answer is not in the numbers. Numbers give you a sense of false confidence.

If you stud sentiment methodically you can catch big turning points. And you won’t make as many errors, you’ll be bearish at the highs and bullish at the lows. Jared has never blown himself up in 23 years.

Other indicators: newspapers. Wall Street Journal’s front page. Think of how fast German Electricity prices left the news. It was going to cause a depression… now it’s gone.

Cure yourself of reading newspapers by reading newspapers from two weeks ago. The news tells you what has already happened, not what’s coming. It’s noise. But if the noise gets louder and louder, we know it will not last long.

If a moral panic surrounds something, the trend is likely to reverse.

Look to pop culture for cues. In 1994, the social climate was extremely negative. The top musical act was Nine Inch Nails. The top movie was serial killer horror Seven. Pop culture was dark. And that year the inflation adjusted Dow bottomed and went on a massive bull run.

In 2000, there was happiness. The music was Brittney Spears and Backstreet Boys. And that was the top.

Positioning is another component of sentiment. When people are all out of a trade, there’s no one else to sell. And vice versa.

The Federal Reserve is another sentiment engine. You can always predict the Fed will follow the past of least embarrassment. It’s a system of saving face. No one wants to be in the news for screwing something up. Screwing something up quietly is how the government operates.

Inflation got out of hand and disgraced the government… so now they’re making the other mistake. They will hike rates until the pain of recession exceeds the pain of inflation. Jared thinks we’re there.

Jared has other predictions. He thinks a bear market in energy will continue. It’s down 20 percent from highs, but energy bulls are still doing a victory lap. But it’s crowded and no one is left to buy.

Cannabis interests him. It’s down a lot, forming a base, and advocates are keeping quiet. Sentiment is bombed to hell… so it’s a good time to form a position.

We just had a bubble in tech. Another is unlikely this soon. But Jared thinks the low is in.

It’s tough for the market to go down when everyone is short. In options last week, there were three put options for every call. That is unprecedented. AAII shows more bearishness than we had in the great financial crisis. World War III and depression are in the cultural conversation. Sentiment is far too bearish.

Jared thinks we should be long stocks and bonds. An average bear market lasts 20 months. If this market started with the blowoff top of GameStop exuberance in January 2020… that puts us at 22 months. People are as bearish today as they were bullish in 2020.

People say we need to feel more pain first. Jared says the pain is enough. Stocks are down. It’s the worst year ever in bonds. The wealth destruction this year is equal to the great financial crisis. And at that time, you could hide in gold and bonds… this time there’s nowhere to hide.

This is a plain, vanilla bear market based on rate hikes.

The bear case is always most compelling on the lows. And the most successful pundits reflect the mood on the market today. They sound smart at the time but have little predictive power.

Sentiment trading is a dark art, so Jared gets that people are skeptical. But you have to be willing to do the trade that is insane to be a successful investor. The best time to invest is when there is no evidence to support your position… you have to invest with faith.