Bills Asset Management

BAM MARKET NOTE

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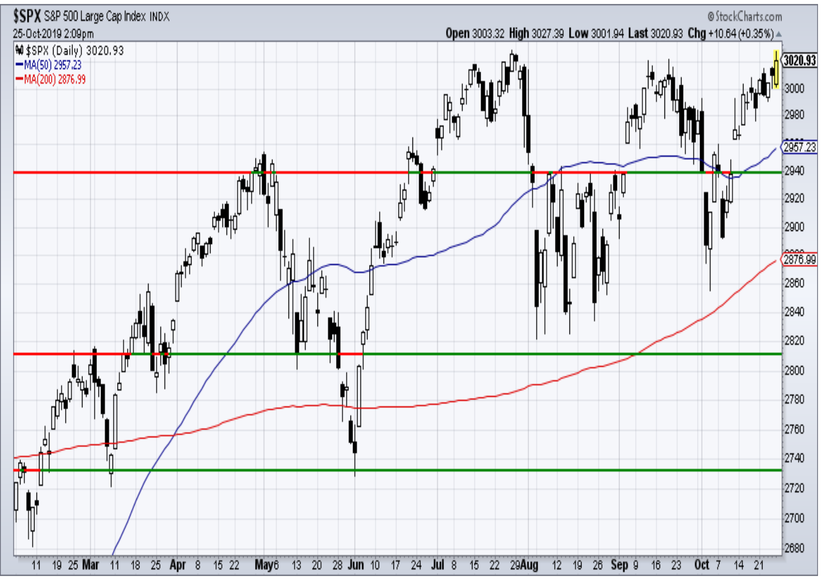
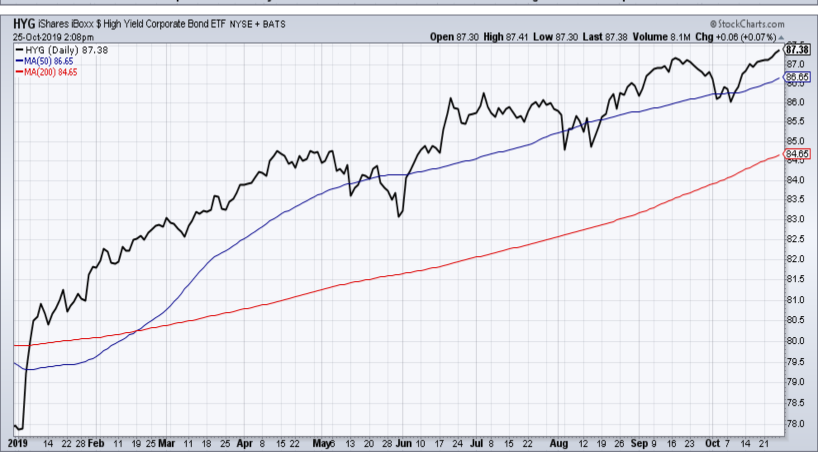


The S&P continued to ease upward this week. It marks the third straight week of modest gains. On an intra-day basis, the S&P touched its highs for the year before turning back a little. The important index remains a mere 5 points from those highs on a closing basis. Market bulls will point to the recent uptrend, seasonal strength, positive earnings, accommodative Fed, etc. for reasons for optimism and the eventual upside break-out. However, market bears will argue just as vehemently that the market's inability to already make new highs despite all the "good" news is reason to be very cautious. Regardless, the market is at an important juncture. A break-out here would set the stage for a significant 4th quarter rally while a failure would send the market back down to the multi-month trading range.



The behavior of high-yield bonds certainly favor the bulls. HYG, a widely traded high-yield ETF, is in a short-term low volatility uptrend. The ETF remains well above its 50 day moving average and shows little weakness currently. High yield bonds are among the first market groups to turn down when signs of a weakening economy emerge. The recent behavior of HYG indicates that, at this point, the market has little concern about the economy.

Our Point

There is a little bit for both the bulls and the bears in the current market. However, until the current short-term uptrend in the major indices fails, the bulls have the upper hand; the current market is going up until proven otherwise. The Fed is widely expected to lower rates again next week. What they say along with the rate announcement will be even more important as many are also beginning to expect the Fed to announce that the current rate cut cycle has come to an end. We have our doubts. Behind the scenes, the Fed is quietly pumping large amounts of liquidity into the short-term repo market. In fact, the amounts being injected surpass those needed during the financial crisis of 2008. It begs the question – what does the Fed know that we don't? The question will likely be asked when the Fed convenes next week so the market will be listening intently. We don't pretend to know the answer and the Fed's liquidity injections through lower rates and direct intervention may well prove to drive the markets higher. However, something does seem amiss and at some point Fed intervention will not cure all ills (see Europe over the last several years). In any event, you cannot argue against price and prices are moving up. If the highs are taken out, we will shift to a more aggressive posture heading into year-end. We made no portfolio adjustments this week as we await confirmation of the next leg-up. If the market fails here, we are positioned to weather any storm. The Vols found out they still have a ways to go to catch up to the Tide but did make us proud as they went toe to toe with the red elephant for the better part of 3 quarters. Absent a late (inexplicable) fumble and a few questionable calls it could have been an orange market note this week. Enjoy a wet weekend and get your indoor chores done.

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