BILLS ASSET MANAGEMENT

BAM MARKET NOTE

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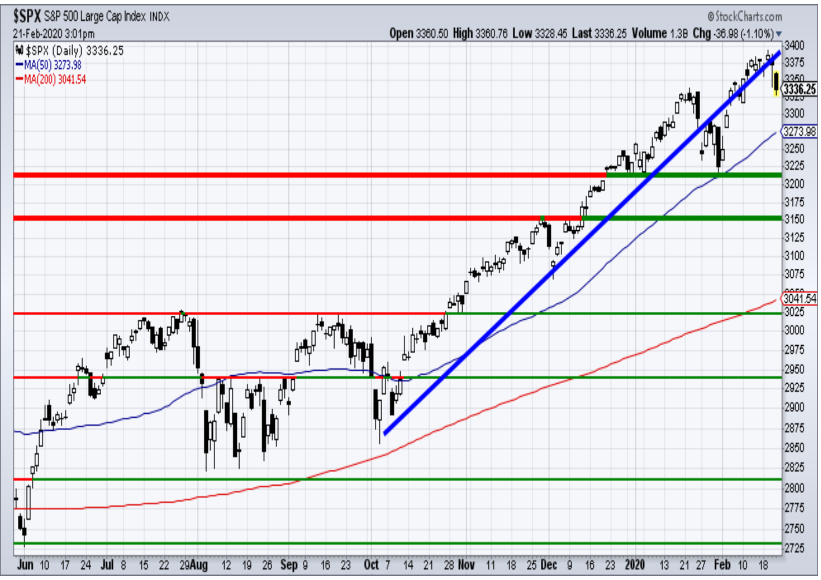
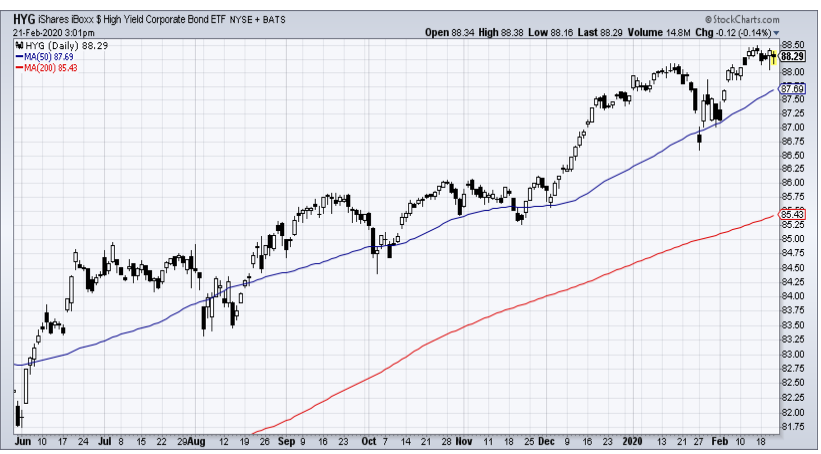


After 3 weeks of up moves, the S&P took a breather this week and looks to finish the week down around 1.5%. In the grand scheme of things, the pull back has been very modest to this point. Goldman Sachs warned earlier this week that the risks of a correction "is looking much more probable." Their view of a 10% or more correction in the near-term is not unreasonable and something we agree with. Investors have become complacent but market risks are present. As we have stated here a number of times in prior notes, a correction of some significance would prove to be healthy for the market in the long run. When the market gets stretched (as it is now), the risks of a violent correction becomes greater. The greater the stretch, the more violent the correction. An orderly selloff would work off the excess without creating panic.



While the market is ripe for a correction, high yields continue to show little to no alarm. A reading of high yield bonds indicates that bond traders are not the least bit worried about the state of the US economy. While the coronavirus has not spread like many had feared, it does continue to disrupt the world economy. It would be naïve to think that it would have no effect on the US but the effects have been muted so far. Apple's warning earlier this week about slowing sales due to China's slowdown is concerning. The rollover effect to other companies and industries is something to watch. High yield bonds will be among the first warning signs.

Our Point

The current market weakness feels worse than it has been. The market rally since October of last year has been a low volatility rise for much of that time. We did feel the "sting" of a 3% pause a few weeks ago but those losses were quickly recovered. While the market is only 1.5% off its highs, the market is overdue for something more significant. Whether or not this is the start of the overdue correction is anyone's guess, but the weakness is enough to start paying attention. The sales warning issued by Apple may well be the first of several warnings to come due to economic weakness throughout the world. While high yields show no worries, there has been a definite flight to safety as gold has rallied significantly and interest rates are falling. The 30 year treasury hit an all time low and is currently trading at 1.97% while the 10 year notes are back to September 2019 levels and a further fall would challenge all time lows. The divergence between the defensive sectors and the rest of the market has our attention and we are watching for more signs of a flight to safety. We made no changes to our portfolios but have tightened our stops should the weakness continue. The bull market remains alive and well (even with a 10% correction) but, at some point, a 10% correction will turn into something much more concerning and much more destructive to portfolios that are not being managed with risk in mind. If further weakness develops, investors should consider taking some profits and building up cash for the next good buying opportunity. We aren't there yet, but savvy investors should start looking for the exit door and finding their path off of the dance floor. Hoping the market continues up is not an investment strategy. Planning your next move if certain conditions are met is one. Speaking of hope, I am hoping that this is the last of the cold weather and that spring springs soon! Enjoy your weekend wherever it finds you.