BILLS ASSET MANAGEMENT

BAM MARKET NOTE

JULY 10, 2020

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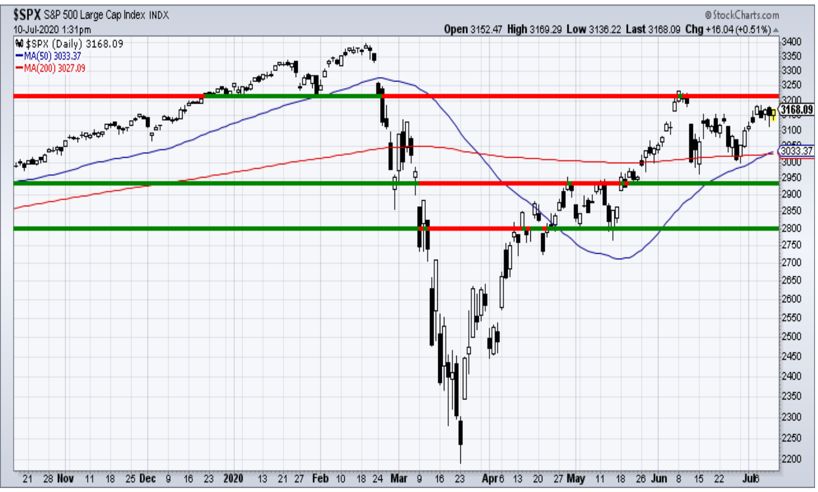
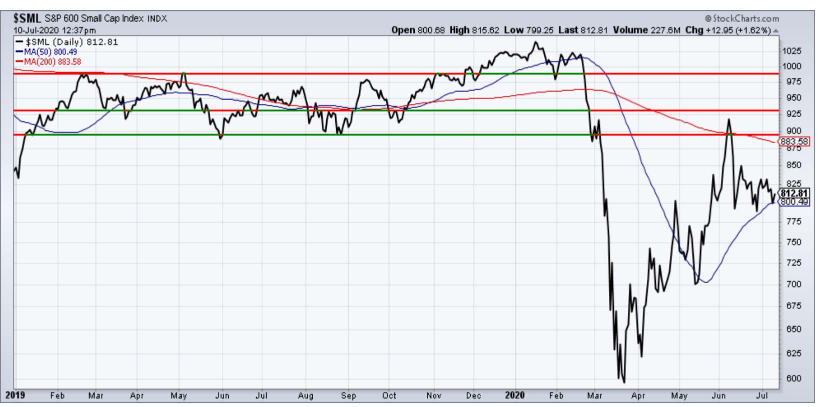


The market was in a short-term downtrend when we last posted this note 2 weeks ago. Since then the S&P has surged upward and is now back near the top of the recent trading range. With the index at the top end of the range a move downward from current levels (back down to support) would not be surprising. However, we suspect support will hold and we will remain in this wide trading range (around 8% from support to resistance) for some time. Volatility has increased markedly so unexpected good news or bad news could lead to an outsized move in either direction. With earnings season starting next week, continued volatility is a surety. Remain vigilant and cautious in the current environment.



While large caps have been surging over the last 2 weeks, small caps have continued to lag significantly. The chart of the S&P Small Cap 600 is troublesome. The recent performance divergence in small caps increases the likelihood of near-term weakness in the broader market. It would be difficult for the broad market to continue its advance without participation of the risk on assets in the small cap universe.

Our Point

Large caps, and specifically large cap tech companies, are driving this market higher. Facebook, Microsoft, Amazon, Apple, and Netflix are all at record highs and continue to increase their shares of the cap weighted S&P 500 and Nasdaq. Their leadership is what is currently driving the market's recovery. All are at frothy levels so weakness from one or more of these stalwarts could lead to a sharp sell-off in the broader market. Financials (as represented by the exchange traded fund IYF) have been one of the few weak spots in the market. Over the last 3 weeks, they are down over 5% while the S&P is up over 1% during that time frame. Tuesday will be a monster day as JP Morgan, CitiGroup, and Wells Fargo all release earnings in what could be a tone-setter for the upcoming earnings parade. Goldman, Morgan Stanley and a host of regional financials follow suit the rest of the week. Earnings will be bad but analysts will be looking for reasons for optimism. With financials already weak, earnings that are unexpectedly more bad would bring down the rest of the market. Next week is a key week to determine the veracity and sustainability of the recent advance. Earnings could be one of those unexpected things (good or bad) that could take us out of the current trading range. Other potential market movers are the Fed and its ever expanding balance sheet, the resurgence of the coronavirus and its impact on re-openings across the country, daily news on advancements of virus treatments and potential vaccines, talk out of Washington of yet another stimulus package, etc. You get the picture – there are myriad unknowns and unknowables that will drive this market over the course of the next several weeks. With so many cross currents, there is no way to know which way it will break and betting one way or the other would just be a guess and a fools errand. In our view, there remains more downside risk than upside potential. That said, we remain invested with the over-riding upward trend – watching things closely and preparing for a quick exit should things turn south. We made no changes to our portfolios this week and remain invested in a number of low volatility bond and income funds with some exposure to equities and gold. It continues to perform exceptionally well – don't fix what is working. We enjoyed a fabulous socially distanced 4th of July celebration with Kelly's family replete with games for the little and big ones alike, fried catfish, and a fireworks show that was the envy of the neighbors. It was a fun day. We hope you were able to likewise enjoy your family. Have a great weekend and mask up.