BILLS ASSET MANAGEMENT

BAM MARKET NOTE

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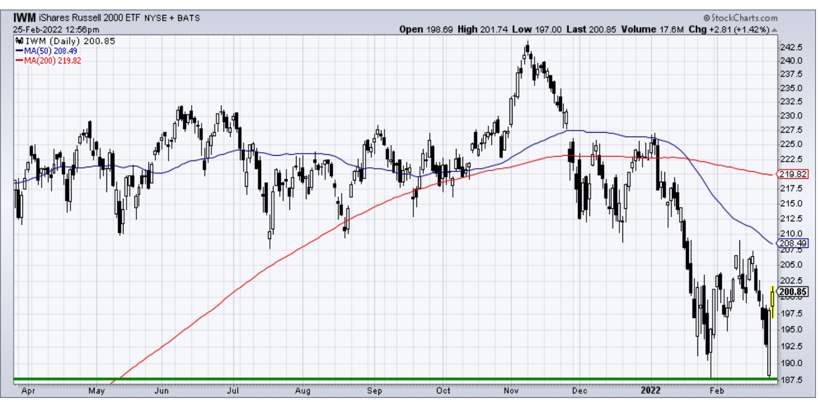
Yesterday's market was astounding. All of the major indices fell precipitously at the market open as shots were fired and Russia began its invasion of Ukraine in earnest. There is an old adage to buy when bullets begin to fly. That seemed to work yesterday as all of the major indices reversed course during the trading day. When the markets closed, all market losses were erased, and stout gains were posted by all the indices. What had been a very bad week for the S&P has now turned into a positive week (assuming today's gains hold). The markets remain nervous and another sell-off could quickly come. However, there is a case to be made that a short-term bottom has formed. On a closing basis, the lows of late January held. We don't believe that we have seen the lows, but we may have a reprieve for a few weeks.



We wrote about the relative strength of small-caps last week and noted that it might be coming to an end. Like the S&P, the Russell 2000 (IWM) had a big drop on the open yesterday but battled back and finished with strong gains. As noted in the chart, small-caps bounced right at the support of the late January lows. The key for this index will be to get back above the prior highs and hold above the 209 level. Should that happen, we would be much more comfortable in waving the all clear for this bout of weakness. We don't believe that will happen, but we will just follow the charts.

Our Point

While the situation in Ukraine is tragic and the humanitarian crisis could be devastating, we don't believe the actions of Russia will have long-lasting effect on the US markets. While some of the direct consequences of the invasion will hit the US economy in the form of rising energy prices, at this point, there doesn't look to be any longer-term direct effects. Of course, that calculus changes should the current conflict spread to other countries or if it serves to embolden China and/or Iran. Strangely enough, the effects of the invasion have been positive for US markets conditioned on the need for government liquidity. The probability of the Fed raising rates by 50 basis points (as many expected) at their next meeting has dropped significantly; with most economists now predicting that the Fed only raises interest rates by 25 basis points. Additionally, the number of 2022 interest rate hikes expected by the Fed has also dropped with the situation in Eastern Europe. We fear the reprieve will only be temporary as inflation continues to rage and promises to get worse (especially in the energy sector). The Federal Reserve continues to be the driver of this market and they remain trapped by geopolitical and inflation concerns. The mid-March meeting of the Fed will be one of the most important meetings in recent memory. With the stark reversal yesterday and the possibility of a short-term bottom forming, we moved some assets back in the market with our aggressive and moderate portfolios. We believe that we are in the midst of a tradeable rally that could extend for a week or two. We do not believe that the market is set to resume the bull market we have enjoyed for the last few years and significant technical damage has been done to the market over the last few weeks. That damage will need to be repaired and will take some time. We will keep a short leash on our recent purchases but could add more positions next week if the markets cooperate! Risk remains elevated and only nimble traders should try to participate. Oversold rallies can look strong but often fail at resistance. We are watching carefully. Have a great weekend and enjoy the dry weather for a change.