Rochester Financial Services

Fee-Only® Financial Management Services

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Dow Jones	S&P 500	NASDAQ	Russell 2000	10 yr Treas	Bitcoin	Gold	Crude Oil
33,615	4,329	13,313	2,001	1.72%	39,443	$1,975	$115.00

Investment Strategy Report

Tragic War in Ukraine Keeps Stock Market Volatility High

All eyes now are on Ukraine, and although the Ukrainians are putting up a terrific fight against the Russians, the loss of life there increases every day. We unfortunately need to assess the effect that the conflict will have on our investments. Stocks were already under pressure for weeks leading up to the onset of hostilities, as the dual concerns about inflation and the Russian build up outside of Ukraine spooked the markets. Many investors sold ahead of the actual invasion, fearing the worst for their investments. But if you had done that, you would have missed the big stock rebound the day the fighting started on February 24th. It was a case of sell the rumor, buy the news, as stocks rebounded for 3 days. However, stocks seemed to have run out of juice on Thursday and Friday of last week, as investor fears seemed to take hold again, and stock prices again are approaching the lows of January.

We once again are in an environment in which most investors want nothing to do with the stock market. This emotional roller coaster ride that we are on is what the stock market tends to do in order to kick investors off the "ride". This environment is reminiscent of the beginning of the pandemic, when if we had only sold before things got bad, we could have avoided the losses. However, our current environment is totally opposite to that of March 2020. Back then, the economy was about shut down, on the verge of collapse. Now, it appears that we may finally be done with Covid, and the economy is about to surge ahead. After 2 years of pent-up demand, all sectors of the economy are set to rebound strongly. This past Friday's jobs report was very positive, with unemployment dropping to 3.8%. While the war in Ukraine is a human tragedy, aside from higher oil prices, it will probably have little effect on our economy.

As I've often mentioned in these letters, one reason to get defensive in your equity exposure is if a recession is anticipated. Bob Brinker addresses that in his March newsletter. He states that "we view the probability of recession this year as minimal". He bases this on the facts that 1) "the slope of the yield curve remains positive (as opposed to inverted), and 2) "the favorable overall trend in the leading economic indicators index". Based on S&P 500 earnings, he is forecasting that the index can reach the 5,000 level within the next year (15% higher from here). He expects that the Fed, while beginning to withdraw monetary stimulus, will not become overly restrictive. Louis Navellier believes that the Fed will only need to raise rates 2 or 3 times this year, as opposed to the 5-7 times that many are predicting. He is very positive on the stock market and advises investors to use any stock pull backs as buying opportunities. He also feels that the US is an oasis of the world markets, with our strong growth emerging from the pandemic and our reduced dependence on imported energy. Conversely, he feels that Europe, because of their substantial dependence on imported energy, could fall into a recession.

The analysts at Sentimentrader.com have published several studies over the past few weeks indicating that stocks prices should be higher during the next few months. The theme here is similar to what I've mentioned in my last letter: when sentiment gets overly pessimistic, stocks tend to rally. On 3/3, they showed that put volume (betting that stocks will fall) increased vs. call volume (betting that stocks will rise), which is predictive of a 2-week win rate of 77%, with any drawdowns being benign. The same day, they noted that the Investor's Intelligence survey has shifted to being pessimistic for the first time in 2 years. After other such shifts from being optimistic to pessimistic, "stocks had a strong tendency to rally in the months ahead". A third study from March 1st showed that their Smart Money/ Dumb Money Confidence Spread recently reached a minimum bullish level. Their historical analysis points to a future 80% win rates for stocks. However, they do warn that an 80% win rate should not be confused with a 100% win rate. "The latest signal should not be interpreted as an "all clear" signal but rather as a wake-up call to overly fearful investors that the market *could* do what it does best and surprise investors in the months ahead".

It appears that volatility will be with us for a while, so we should prepare accordingly. Hopefully, some of the volatility will be to the upside. *Jeff Feldman*

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