Goldman SMALL CAP RESEARCH

The Goldman Guide

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INSIDE THIS ISSUE:

KEY TAKEAWAYS

- ⇒ *A lousy market brings us a modified roundtable discussion on the market and future buys*
- ⇒ *Sector performances will surprise you*
- ⇒ *Small cap value and stocks above their 20-day averages may be the way to go*
- ⇒ *High yield bond ETFs could be the best short term play*
- ⇒ *Golf: All good things must come to an end*

KEY STATISTICS

Index	Close	2014
DJIA	16027	-3.4%
S&P 500	1816	-1.8%
NASDAQ	4000	-4.4%
Russell 2000	1111	-4.8%

(figures are rounded)

Round Table: What To Do From Here

As I feared last week, after a dead cat bounce early in the week, we hit a real corrective phase with one of the worst performing weeks for NASDAQ and the Russell 2000 in years. We originally thought that the correction might not yet occur until May, but the selling appears to be in full swing. Given the present volatile situation the GSCR team felt it would be an opportune time to provide background, projected market moves and recommendations. With the start of the Passover holiday Monday evening, our modified roundtable featuring Rob Goldman and Steve Hercenberg is dubbed:

"The Seder Table."

Moderator: What really happened that caused the stock market to turn on a dime?

RG: As we alluded to last week, we believe that the market for some reason had a delayed reaction to events. Normally the big winners in the previous year are sold off and other sectors come under accumulation. This year, the trend did not shift, until recently. Plus, it seems as if the weather impact on Q1 results will prove to be worse than originally expected. Considering the sell-off has been led by higher than average volume, it has been broad based and fear based.

SH: Consensus heading into 2014 was that technology was still the place to be and the stocks outperformed early on. However, now that the first quarter earnings may largely disappoint, the valuations have become unsustainable.

(cont'd)

The Seder Table (cont'd)

Many explanations have been given for what transpired. Maybe the Market simply lacked any catalyst to continue propelling it upward. This harsh winter has been lowering expectations about upcoming earnings reports this quarter. The Fed has announced no plans for another QE; rather Fed Chairman Yellin plans on further tapering and plans to let long-term interest rates rise as the economy increasingly demonstrates that it is establishing a solid footing. Our military leaders are considering plans to cut back our armed forces to pre-World War II levels. And additional fiscal policy cuts appear likely. In other words, neither US Government monetary nor fiscal policies are in any stimulus mode.

Moderator: Steve, please explain what has happened with the key sectors.

SH: Last year, only four sectors outperformed the S&P 500 (up 29.8%):

> Consumer Discretionary (up 41.9%) led, followed by
> Health Care (up 39.7%),
> Industrials (up 39%), and
> Financials (up 32.1%).

By contrast, the two worst performing sectors last year were Telecommunications (up 6.8%) and Utilities (up 10.6%). Who has had the best performance year-to-date? As of April 4th when the S&P 500 hit a new high (up only 0.90%), Utilities have been leading (up 8.5%) followed by Health Care (up 4.1%), and Materials (up 3%). As of April 11th, however, the S&P took a swan dive resulting in year-to-date change of -1.8% and dragging all but two sectors into negative territory. The Utilities sector actually advanced further, up 8.8%, while Materials fell flat to 0.0%.

We might be confused by the recent performance of utilities stocks with so much concern about the impact of increased tapering by Fed intentions this year. Interestingly, the last time that US Small Cap stocks outperformed all other asset classes was in 2010 and Bonds—US 20 Year Government Bonds and US TIPS Bonds outperformed all asset classes the following year. Will history repeat itself?

The Seder Table (cont'd)

Annual Returns Of Benchmark Asset Class ETFs

2007	2008	2009	2010	2011	2012	2013	Risk
Emerging Mkts 36.89%	US 20Yr+ Govt. Bond 29.06%	Emerging Mkts 62.02%	US Small Cap 27.64%	US 20Yr+ Govt. Bond 30.93%	Int'l Real Estate 30.53%	US Small Cap 32.93%	10.56%
Gold 27.45%	Gold 8.90%	Int'l Small Cap 38.51%	US Real Estate 27.07%	US TIPS Bond 12.62%	Int'l Large Cap 14.01%	US S&P 500 28.66%	8.58%
Commodities 15.84%	US 1-3Yr Govt. Bond 2.38%	Int'l Real Estate 36.25%	Gold 26.49%	Gold 12.44%	Int'l Small Cap 12.52%	Int'l Large Cap 20.53%	11.96%
US 20Yr+ Govt. Bond 11.72%	US Short Govt. Bond 1.78%	US Small Cap 35.79%	Int'l Small Cap 25.75%	US Real Estate 10.61%	US S&P 500 11.79%	Int'l Small Cap 16.04%	11.50%
US TIPS Bond 11.66%	US TIPS Bond (1.31%)	US Real Estate 35.31%	Int'l Real Estate 22.21%	US S&P 500 3.01%	US Small Cap 11.63%	Int'l Real Estate 3.58%	16.60%
Int'l Large Cap 10.78%	US Real Estate (34.30%)	Int'l Large Cap 28.51%	Emerging Mkts 20.31%	US 1-3Yr Govt. Bond 1.43%	US Real Estate 11.57%	US Real Estate 3.37%	15.42%
US 1-3Yr Govt. Bond 7.23%	Commodities (40.35%)	US S&P 500 25.93%	Commodities 16.97%	US Short Govt. Bond 0.06%	Emerging Mkts 9.44%	US 1-3Yr Govt. Bond 0.21%	0.42%
Int'l Small Cap 3.72%	US Small Cap (42.21%)	Gold 23.70%	US S&P 500 15.36%	US Small Cap (0.41%)	US TIPS Bond 4.11%	US Short Govt. Bond 0.00%	0.06%
US S&P 500 4.30%	US S&P 500 (42.87%)	Commodities 19.74%	Int'l Large Cap 10.83%	Int'l Large Cap (11.17%)	US 20Yr+ Govt. Bond 3.82%	Emerging Mkts (4.32%)	12.75%
US Short Govt. Bond 3.82%	Int'l Large Cap (47.33%)	US TIPS Bond 7.53%	US 20Yr+ Govt. Bond 9.58%	Commodities (12.87%)	US 1-3Yr Govt. Bond 0.18%	US TIPS Bond (8.65%)	6.39%
Int'l Real Estate 1.38%	Int'l Small Cap (51.93%)	US Short Govt. Bond 0.11%	US TIPS Bond 6.09%	Int'l Real Estate (16.16%)	US Short Govt. Bond 0.06%	Commodities (11.30%)	9.77%
US Small Cap (0.50)%	Int'l Real Estate (64.48)%	US 1-3Yr Govt. Bond 0.09%	US 1-3Yr Govt. Bond 2.26%	Emerging Mkts (16.83%)	Commodities (2.99%)	US 20Yr+ Govt. Bond (13.81%)	10.15%
US Real Estate (26.91%)	Emerging Mkts (65.88%)	US 20Yr+ Govt. Bond (23.60%)	US Short Govt. Bond 0.13%	Int'l Small Cap (19.43%)	Gold (4.15%)	Gold (31.26%)	18.50%

Source: Koch Capital, Quantext Portfolio Planner

Moderator: Rob, if you were managing money again, what would you do?

RG: The worst thing one can do is this environment is nothing. I would be a seller of the former momentum plays as I think they will still come under pressure. Frankly, trying to justify valuation is too difficult to make them buys right now because there is no discernable floor. I would also make sure that I have sold calls on most of my long positions. In terms of buys, there really are slim pickings because small cap growth valuations are still pretty high on relative basis.. Therefore, I would buy stodgy blue chips and small names that might represent more value than growth. If I can time things right, engaging in the quick trading of stocks that are above their 20-day moving averages could be profitable.

Keep in mind that stocks won't appear to be too risky in perpetuity. Second quarter results will be better than the first which will help , even though it is odd that stocks tend to underperform when the economy is strong and outperform ahead of a good economic performance.

The Seder Table (cont'd)

Moderator: Steve, you have a different take on what will work in the short term.

SH: To Wall Street's surprise, long-term government rates have been in a falling channel since the beginning of the year. The CBOE 30-Year Treasury Bond Yield Index ($TYX) has declined from 3.975% on December 31, 2013, to 3.475% on April 11, 2014. Since the Fed plans to taper long-term interest rate risk appears to be a major downside risk this year at some point in time, but likely further down the road.

High yield bonds exchange traded funds (ETFs) appear to be an investment that benefits from both a stronger economy and you get paid while you wait. Morningstar rates **AdvisorShares Peritus High Yield ETF (NYSE – HYLD - $52.71)**, with 5 stars overall and for the last three years. For a short-term speculative move, consider going short Brazil with **Direxion Daily Brazil Bear 3X Shares (NYSE – BRZS - $37.57)**.

Goldman Small Cap Research analysts are neither long nor short these shares but may elect to purchase these ETF within the next 48 hours.

All Good Things Must Come to an End

For those of you that believe that the long bull market has ended, than this piece from our mystery contributor to *The Uncensored Sensibility* is for you.

author It has been a generation since Tiger and Phil were both absent from the weekend's play at The Masters. The baton is being passed, albeit slowly, in golf, and soon golf's majors without Tiger and Phil, Woods and Mickelson for the few of you who need the full identity, will be the norm instead of the exception. Obviously these giants will not go down quietly, proof of which was Phil's victory in the British Open last year, but father time and mother injuries are colluding to bring about their exit from the grand stage.

Last year, only four players older than Tiger Woods won PGA Tour events, and one of them was Phil. This year is the first time since before Tiger turned professional and won The Masters by twelve strokes in 1997 that neither of them have a victory on tour heading into the event. It has now been twenty years since Tiger won his first of three consecutive US Amateur titles, and twenty five years since Phil won his first PGA Tour event, which he did most unusually while still an amateur golfer at Arizona State!

The Uncensored Sensibility (cont'd)

Certainly this week has forced PGA Tour Commissioner Tim Finchem, CBS Sports, NBC Sports, and Golf Channel executives to start focusing on how to handle this inevitable shift change in the sport. These two men, especially TIger, moved the television ratings more than the rest of the tour's players combined. They must face the new reality.

This is not a prediction that Tiger and Phil will never win again because they will win again, but those wins will be more noteworthy for their triumphs over age and injury than for their dominance of the sport.

The tradition unlike any other this weekend was not The Masters. Sorry Jim Nantz, it was not. The tradition unlike any other was that it is impossible to beat father time, and that tradition will remain undefeated this weekend, and every weekend.

Have a great week! Remember the market is closed on Friday.

The Goldman Guide

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