Goldman SMALL CAP RESEARCH

The Goldman Guide

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INSIDE THIS ISSUE:

KEY TAKEAWAYS

- ⇒ *Investor sentiment incredibly bearish which bodes well down the road.*
- ⇒ *Our take is that there is more pain before the gain*
- ⇒ *Recent sharp declines are seasonal to a degree thanks to institutional window dressing*
- ⇒ *Uncertainty regarding the Fed, economy, Q3 earnings are all near term overhangs*
- ⇒ *While we wait for signals hedge funds are engaging in these strategies right now*

THE MAJOR INDICES

Index	Close	2015
DJIA	16315	-8.2%
S&P 500	1931	-6.2%
NASDAQ	4687	-1.0%
Russell 2000	1123	-6.8%

(figures are rounded)

A Popularity Contest

It's a good thing that Pope Francis is not a U.S. citizen because he would screw up all the polls. While Donald Trump and Hillary Clinton remain at the top of their political party polls, and typically attract a nice crowd, nothing tops the Pontiff. After all, after major pontificating events in Washington D.C. and New York, he led Mass and prayers for hundreds of thousands in Philadelphia, the city of brotherly love.

It's fitting that just after His Holiness addressed Congress by slamming many of our nation's policies and societal ideals, Congressional chaos now looms on the horizon, with the announced resignation of the Speaker of the House John Boehner, and calls for the ousting of Senate Majority Leader Mitch McConnell as well.

What does that mean for stocks?

Investors sometimes forget that public and governmental policy are the real early catalysts for the market and specific sectors. That is why the inaction of the Fed 10 days ago has had such a detrimental effect on the market and why Hillary Clinton, the presumptive Democratic Presidential favorite, killed health care stocks for a spell by merely commenting about the sorry state of pricing of health care on Americans.

As to the GOP leadership, most policy wonks anticipate some gridlock for a while regardless of who mans the rudder. However, it is a reminder that we must be wary of the policies and comments of leading political figures and that stocks may be vulnerable at times as we get through the primary season and pick our Presidential candidates.

The Stock Market Today

U.S. Stock Market Index Performance
as of 9/25/15

Index	Close	52-Wk Hi	52-Wk Low	Hi Date	Low Date	% off High	% from Low	Bounce*	% Below 200-DMA
DJIA	16,315	18,351	15,370	5/19/15	8/24/15	11.1%	6.1%	16.2%	-7.6%
S&P 500	1,931	2,135	1,821	5/20/15	10/15/14	9.6%	6.0%	12.6%	-6.5%
NASDAQ	4,687	5,232	4,118	7/20/15	10/15/14	10.4%	13.8%	18.0%	-4.7%
Russell 2000	1,123	1,296	1,040	6/23/15	10/15/14	13.3%	8.0%	14.8%	-8.0%
Average						11.1%	8.5%	15.4%	-7.0%

* denotes the percentage index is up from recent low

Source: www.StockCharts.com, Goldman Small Cap Research

The past ten days have been brutal haven't they? If it feels like your portfolio has been smack around but the DJIA hasn't, you are partially correct. There has been a sharp selloff in high growth consumer stocks but especially health care and biotech shares, prompted to some degree by the Clinton comments alluded to above. The damage has been pretty bad, with both the NASDAQ Composite and the Russell 2000 Index down by over 6% at their low points over the past 10 days.

Watching the trading of the past week or so one thing has become apparent in the groups and stocks that have sold off sharply, such as the small cap space and biotechs. I believe that we have seen significant, seasonal window dressing by institutions amid the profit-taking in these well-performing equities. In most cases, much of this activity would have occurred in weeks two and three of September, since we are nearing the end of the quarter. Due to investors waiting on the Fed, the profit-taking and portfolio shifts occurred a bit later and with more fury, exacerbating the past 10-day decline.

So what does this all mean?

First, the window dressing means that institutions have reduced or eliminated holdings that appear out of favor so when they produce quarterly reports, the "bad" stocks are not there, or do not dominate top holdings. They also are likely sitting on cash, waiting to see what the Q3 earnings season will bring, along with a potential October move by the Fed. Don't mistake these moves for inactivity. They will be active. More on that later.

Say What?

There are some real must-reads this week, ranging from investor sentiment, potential Fed and market signals and a story that could have a huge impact on the mutual fund and ETF industries, and your investments.

Marketwatch

http://www.marketwatch.com/story/stock-investors-havent-been-this-bearish-in-15-years-2015-09-25

This news bodes well and should be read, but is just one component of the whole picture, as readers of the Guide are aware.

Zero Hedge

http://www.zerohedge.com/news/2015-09-27/what-recovery-94-million-more-americans-below-poverty-line-pre-crisis

It's a headline like this that gives the Fed pause…

CNBC

http://www.cnbc.com/2015/09/25/fed-jobs-could-drop-more-rate-clues-in-week-ahead.html

The market is desperate for signals and we can finally get it—maybe.

The New York Times

http://www.nytimes.com/2015/09/27/business/sec-turns-its-eye-to-hidden-fees-in-mutual-funds.html?ref=business&_r=0

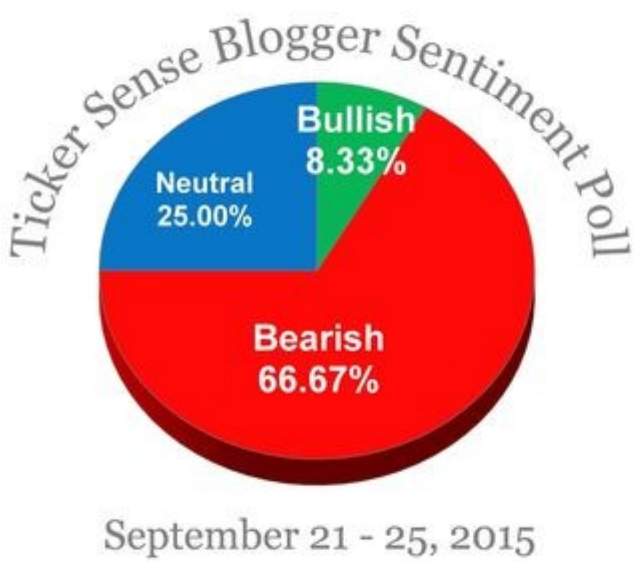
If you own mutual funds, this is a must read. This is a long time coming and could have a huge impact on funds and ETFs.

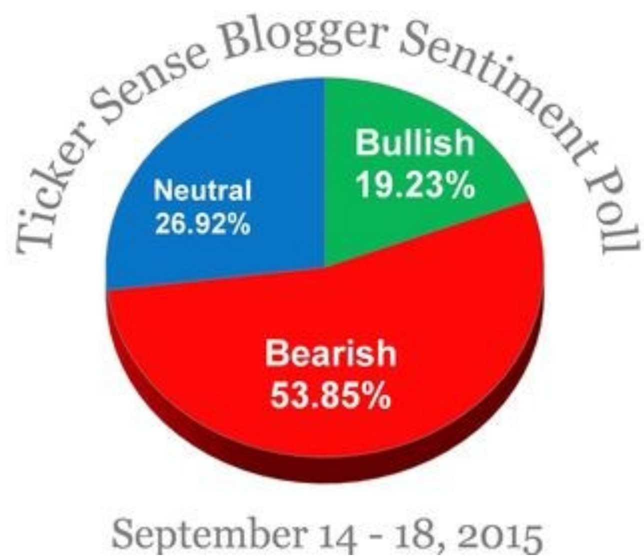
Just the Stats

AAII Sentiment Survey (figures rounded)

	Current	Last Week	*Long Term Avg*
Bullish	32%	33%	*39%*
Neutral	39%	38%	*31%*
Bearish	29%	29%	*30%*

Talk about a non-story. The figures in last week's survey were practically unchanged which translates into no news or shifts to modify sentiment. However, I bet any material moves in either direction for stocks this week will impact next week's survey. The Marketwatch story we referenced in the Say What? Section may onto something. The Tickersense poll has reached a scary low "Bullish" and crazy high "Bearish" sentiment, with no change in the "Neutral" category. This signals to us that it these pros believe it will get worse before it gets better.





Top 5 Moves Hedge Funds Are Making Right Now

If you are a contrarian and you read about he Hulbert Composite showing the greatest bearish sentiment in 15 years, or that only 8% of all bloggers polled in the Tickersense poll were bullish that we are in the catbird seat.

Unfortunately, it may get worse before it gets better. And, it will get better. A month ago we warned that there could be 10-12 weeks of pain. We are I the middle innings, in our view. Between the Fed, the economy, a tepid Q3 earnings seasons with little revenue growth and potential downward revisions for multinationals, the next month could be much like the past 10 days.

Individual investors may fear October, but actually from the historical perspective it is a pretty good month for stocks, with equities rising 0.68% on average since 1950 and 1.49% for the past 20 years, which includes the 17% decline in 2008. Investors should pay attention to 52-week lows right now because the calendar will change some things.

Many stocks, especially small caps, achieved their 52-week lows around mid-October 2014. So, it will be interesting to see how/when/if new lows are achieved and how these new lows will impact the indices and stocks when/if they achieve new lows during October. We had a big move in stocks the last 10 weeks of the year and we think that November will be a big month for equities, once the madness subsides.

So what are the top 5 things hedge funds are doing right now?

Sales: Trimming winning positions in high growth, high valuation consumer and heath care stocks

Cash: Sitting on cash to go back into these positions, domestic-centric businesses, oversold stocks with exposure to China

Old School Energy: Coal stocks and others are staging a comeback

GARP & Value: Buying GARP and value tech trading at low valuations

IPOs: The slate of IPOs should do well which could help reverse negative market sentiment

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