The Goldman Guide

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INSIDE THIS ISSUE:

KEY TAKEAWAYS

- ⇒ *All signs point to short term trading patterns, especially in light of drops due to geopolitical concerns*
- ⇒ *Small caps look terrible and the long term strength seems to have reached its end….but….*
- ⇒ *Given seasonality, reasonable valuations and recent trading patterns, Q4 could see a nice bounce*
- ⇒ *Focus on big caps for now, and review our Stock Market Survival Guide for guidance*

KEY STATISTICS

Index	Close	2014
DJIA	17108	3.2%
S&P 500	1979	7.1%
NASDAQ	4466	6.9%
Russell 2000	1110	-4.6%

(figures are rounded)

Stock and Index Patterns

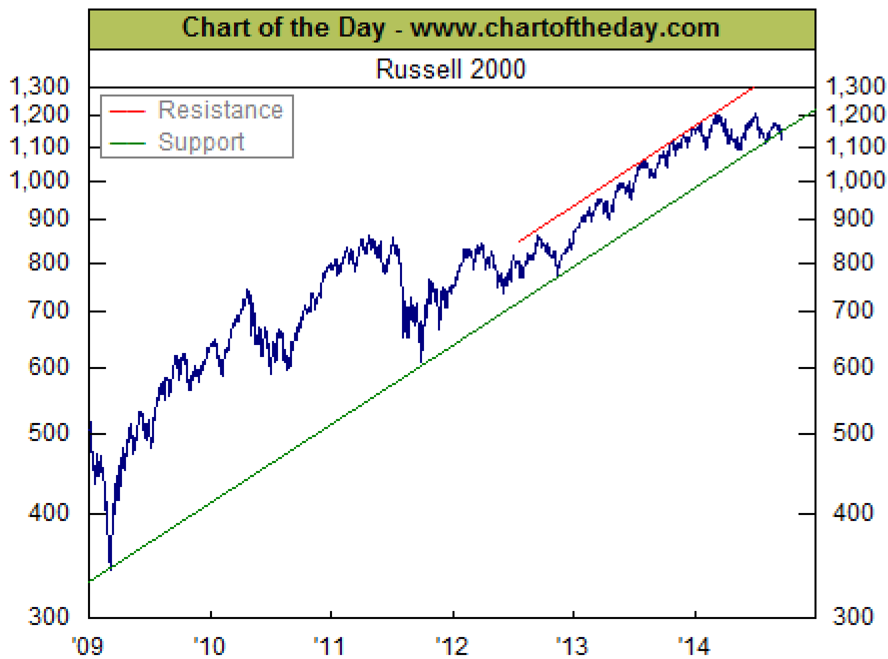
Well, this is a first. We saw global markets getting pummeled overnight and our own market getting clobbered this morning so we trashed the original version of the Guide and instead have drafted this abridged, new one, which is why it is being released a few hours later than usual.

Panic has really hit the market. It is no joke. To make matters worse, the media is really stepping up its game to stoke the fires by manufacturing new reasons why stocks will collapse, since the tried and true issues have become tired and ineffective.

I may not know much, but I do know this. Our failed foreign policies are having an effect on the market, but not in a sustained way. For months, when stocks have tanked due to political or economic issues abroad, they bounce right back. We are seeing it again today. All of you short term traders out there can take advantage of these moves by using short term trading vehicles (like NYSE—TVIX). I suspect that this scenario will continue, unless we break below technical support levels on the S&P 500.

Speaking of support levels, 2 weeks ago, our Guide headline was “Small Caps Screwed in September”. The death cross (50 and 200 DMA crossings) were obvious triggers and the Russell 2000 is down over 6% from its intra-month high. The chart below confirms the fact that despite the declines experienced in recent months, real support did not truly fall apart until recently, after a strong 5+ year run. This narrow channel range between resistance and support is not exactly comforting in the long run, but may not yet signal the commencement of a long term bearish trend.

Stock Resurgence?



The chart to the left certainly is not pretty. But, the recent trading stats may make you feel better.

Right now, we are in the middle of the 52-week range of the Russell. Importantly, each time we have reached the 1200 mark (about 85 points higher from here) the index has collapsed only to rise later. This happened twice in March and once in July and occurred again this month after hitting the 1180 mark. Granted, support on a technical basis is gone and fundamentals are not the best. But, with volume declines and waning interest comes opportunity.

We have broken down below the 10% bear market level for small caps multiple times this year and if that is achieved again (around the 1090 mark), we would begin to dip our toes back in. The bottom line is that for all of the longer term talk, reasonable 2015 P/E valuations and seasonality could play a role in a meaningful bounce in small caps in the next 1-3 months. It just requires a little patience and perhaps a greater focus on big caps until the near term declines are largely complete. The current narrow channel in big caps seems to confirm this tactic.

Looking Ahead

As noted above, in the short term, the broader market S&P 500 is in a narrow rising channel, denoting likely less volatility which means that TVIX holding periods, as referenced earlier, are getting even shorter. Still nervous? the core-satellite approach of simply holding a large cap index appears to be the best fit right now. Also, make sure you read our "Stock Market Survival Guide", published 2 months ago in response to our generally negative short term bias.

1498 Reisterstown Road, Suite 286 Baltimore Maryland 21208 Phone: 410.609.7100
info@goldmanresearch.com www.goldmanresearch.com

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