Lindisfarne Investments, LLC

An island of safety in a sea of risk

Market Update
October 10, 2014

It has been another volatile October so far with the market down 2.1% for the month. As the table below shows, the market can't seem to make up its mind with big up days and big down days.

S&P 500 October Action

October	% Change
1	0.0
2	+1.1
3	-0.2
6	-1.5
7	+1.7
8	-2.1
9	-1.1
Net	-2.1

When a market decides to sell off, it does not do so in a monolithic action. Instead, one stock, one mutual fund, one bond fund at a time rolls over and in a period of several weeks or so, begin to individually move down. This is exactly what our models are designed to catch. Since we have an individual model for each fund we are invested in, these have been taking us out of the market one by one. Thus, as the market gets riskier, we become less and less invested. Of course, we (or no one else either) catches the exact tops or bottoms or a market move. But if it becomes a major move in either direction, we have phased into the appropriate portfolio for that move and are positioned to capture the less risky part of the move.

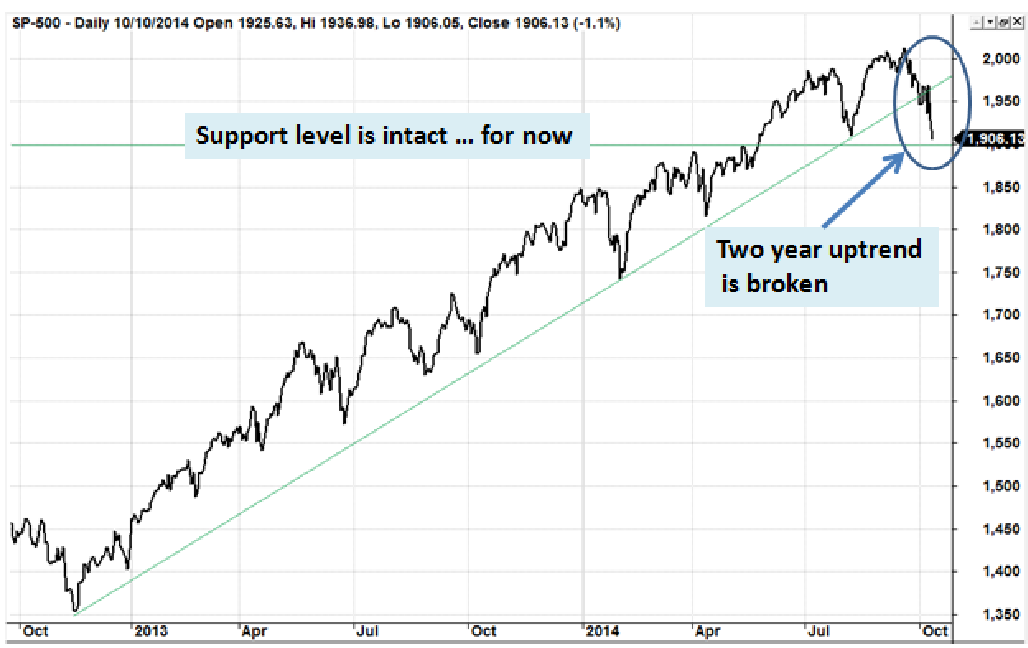
At the beginning of last week, we were only 16% in the market in our traditional brokerage accounts (401k and annuity accounts usually behave a bit differently). At the end of this week, we are 100% in cash in those accounts. So don't worry about what the market does next week.

Our 401k and annuity accounts have also had individual moves to cash, but most of the holdings in them have moved more slowly and been hovering above their respective sell points. More of these have now triggered their sell points and will be sold on Monday.

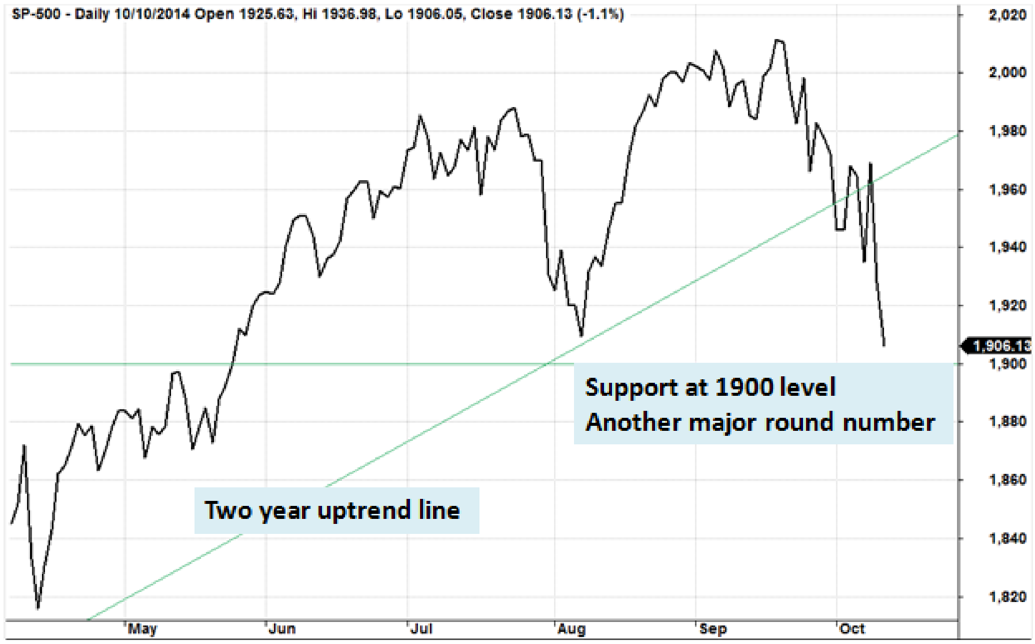
But what will the market do from here? No one knows for sure, but let's look at the charts and see if there is a clear picture of what is going on.

First, the S&P 500 (large companies) have broken their two year uptrend line which is a negative. It is currently just above its support at 1900. If it breaks that level, it could easily go to 1850 (-3%) or 1800 (-6%). If the 1900 level holds, it may take a while for the market to digest this current 5% pullback before re-establishing an uptrend.

S&P 500 Two Year Chart

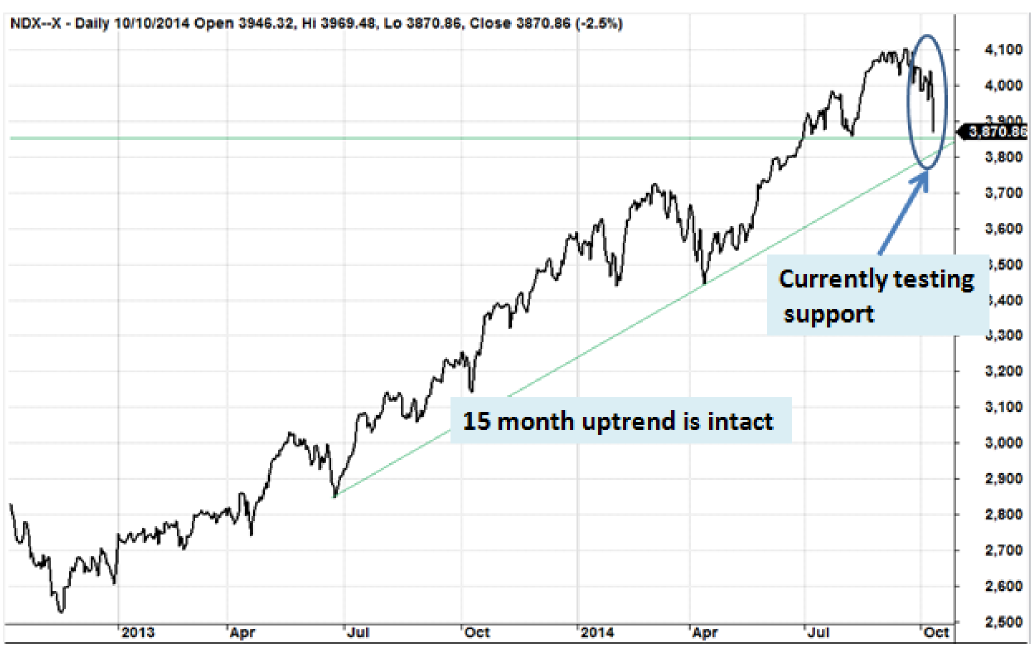


S&P 500 6 Month Chart



The NASDAQ 100 technology stocks have fared a little better. They are currently above both their 15 month uptrend line and support at 3850.

NASDAQ 100 Two Year Chart



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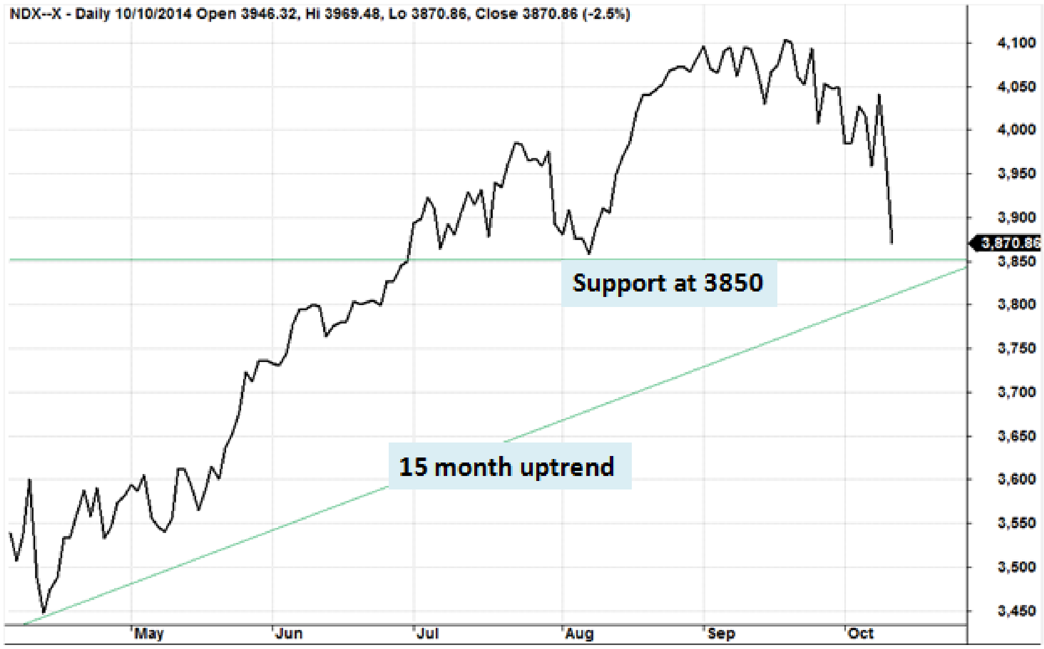
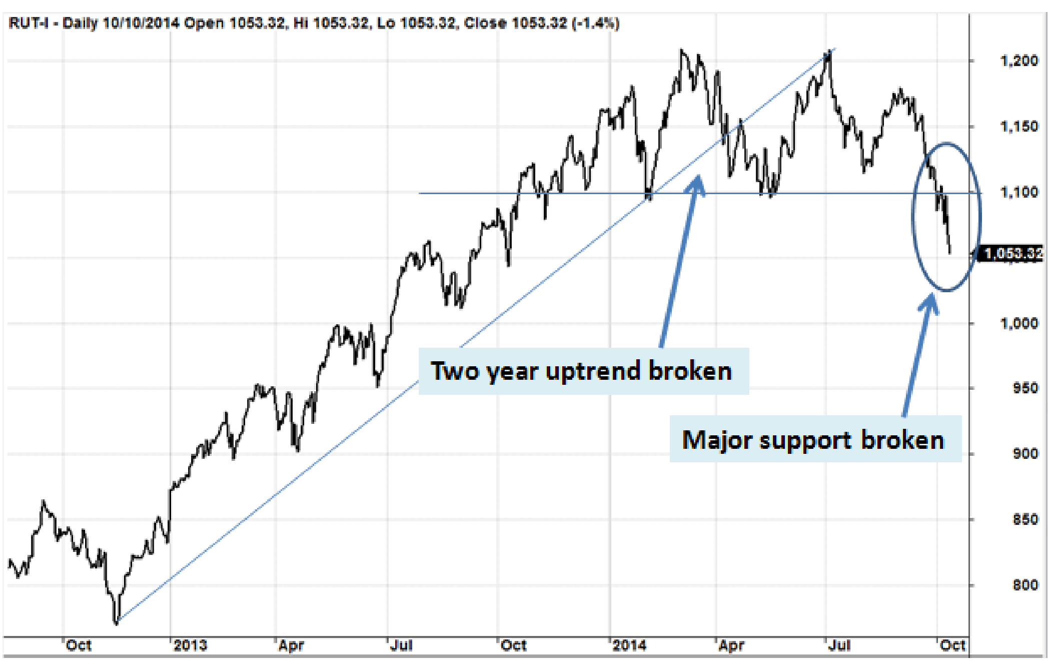
NASDAQ 100 6 Month Chart



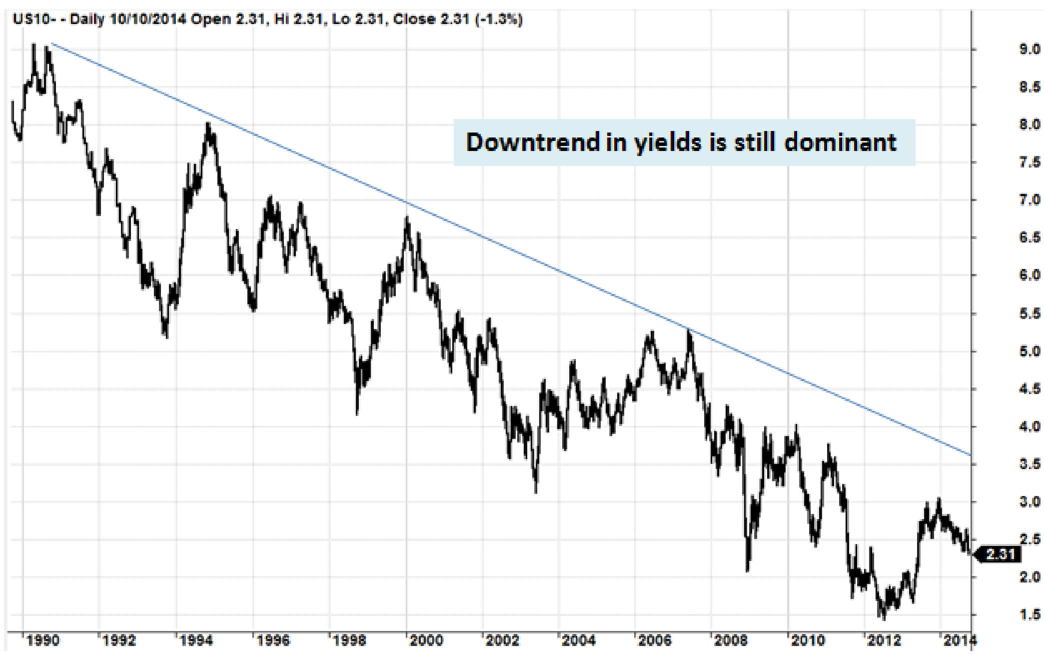
The small company stocks are represented by the Russell 2000 index. As the charts below show, the Russell 2000 has both broken its major uptrend line and is at its lows of the year. Negative.

Russell 2000 Small Caps



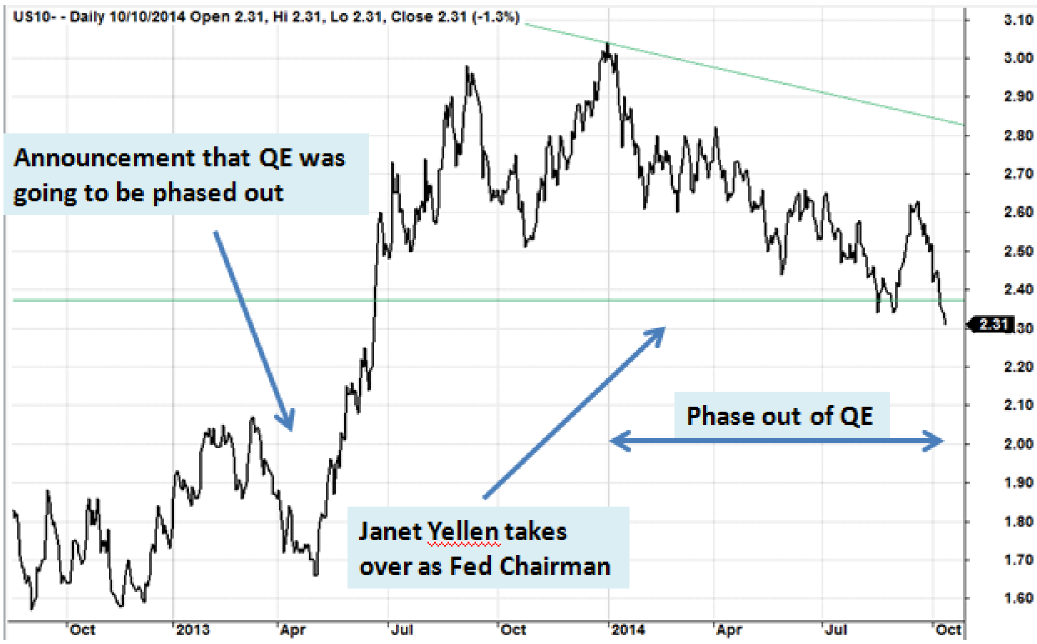
Now that QE is over this month, what are bonds signalling they will do. The talking heads on TV and in the press are argueing over when the Fed will initiate the first rate hike in Treasury yields. As the next chart shows, the 10 year Treasury yield is still obeying its 24 year downtrend line. It is saying no rate hikes soon.

10 Year Treasury Yield … 24 Years



As a matter of fact, the announcement of the coming end of QE has caused a bigger move in rates than the actual implementation of the phasing out of QE. Rates have actually dropped during this latter period.

10 Year Treasury Yield ... 2 Years



So, what does the weight of the evidence tell us?

First, the risk of the market has increased. Large cap stocks are sending both sell and hold signals. Small cap stocks are clearly sending sell signals. Technology stocks are still in a hold. Bonds are showing lower interest rates, even though QE purchases end this month.

It is exactly this type of mixed bag of signals that make it prudent to reduce market exposure and seek the safety of cash. As the police sergeant on the Hill Street Blues TV show used to say, "Be careful out there."

Please feel free to pass this update on to anyone that you think might be interested in it. If they wish to be on the mailing list or would like more information about the services of Lindisfarne Investments, we can be contacted by phone at (440) 623-0775 or by email at bill@lindisfarneinvestments.com .

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