Lindisfarne Investments, LLC
An island of safety in a sea of risk

Market Update
August 1, 2014

What is going on here? Last week saw major technical damage inflicted on the market. What could have caused this? The Federal Reserve on Wednesday once again declared that the economy was recovering and the 2nd quarter GDP was an amazing +4% (even though they changed some parts of the calculation from a cash basis to an accrual basis which let the bookkeepers claim cash inflows earlier). And the markets response was to immediately start moving down that afternoon and followed through with a 2% drop across the board on Thursday. Friday's job numbers came in at 208,000 jobs created, close to expectations, and the market recovered from a nearly 1% intraday loss to finish down only 0.3%. All in all, it wasn't the most reassuring market action.

S&P 500 Long Term Trends

As you can see on the first chart, there a five different trend lines drawn. The longest one, labeled "A" marks the over five year recovery from the lows of 2009. We are still comfortably above the trendline, meaning the recovery uptrend is still intact. The market would have to drop to 1560 or almost 20% from current levels to break this trendline. Such a drop would also put us into bear market territory.

The next trendline, marked "B" is 9% below current levels. This can also be considered a long term trend and its violation would not signal an end to the recovery, but rather a typical 10% pullback which is a common break taken in most uptrends.

The next chart shows trendline "C" which is about one and a half years in the making. We are a mere 20 points above it on the S&P 500 or about 1%. This is our next support for the market.

S&P 500 Intermediate Term Trends

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Looking at the third chart which is less than one year in length, we can see that trendline “C” and the support formed by the recent highs are at similar price levels. This confluence of support areas leads me to believe that here is where we will stop this recent down move. If not, then the 10% correction to trendline “B” is certainly an enhanced possibility.

Shorter term trendlines, “D” and “E” have already been broken.

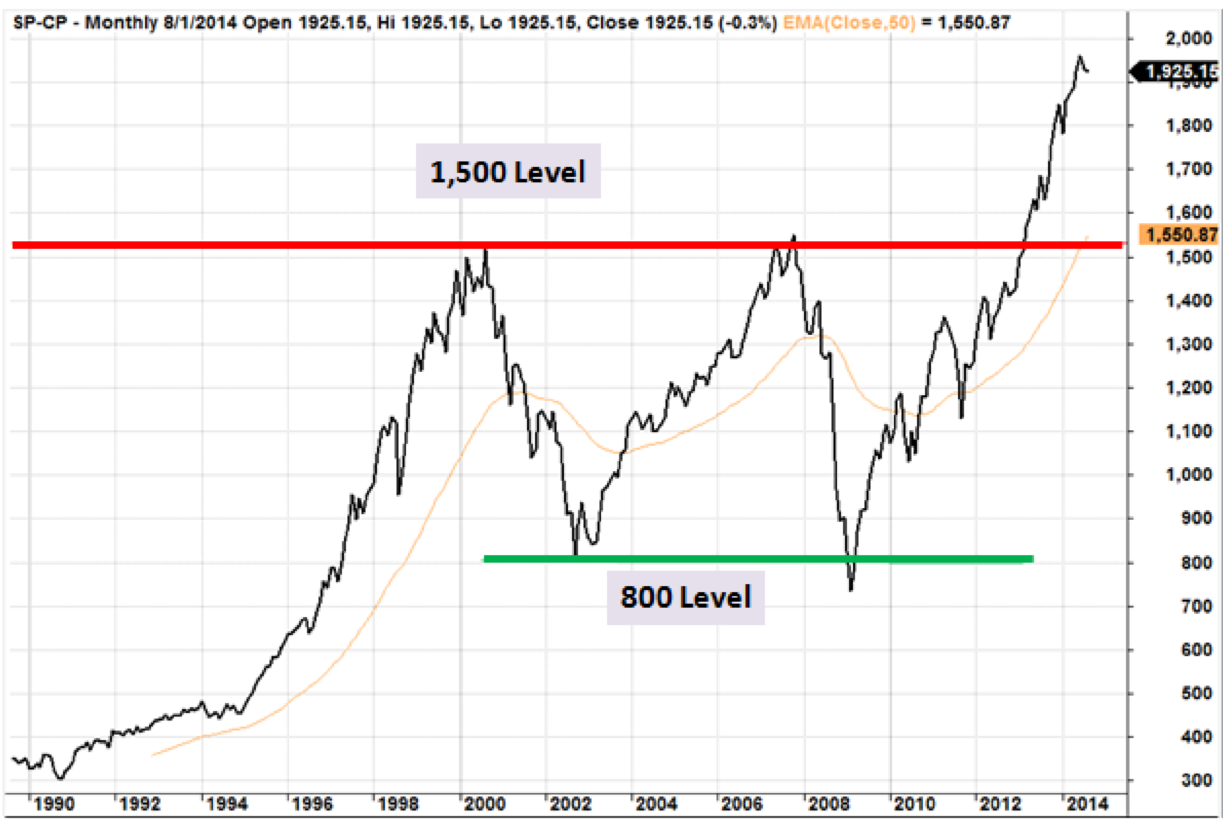
In summary, both long and intermediated term trends are still intact and remain bullish. But short term, the trends are bearish. I would expect us to visit the level around 1,900 sometime within the next week or so. It could be an excellent buying opportunity if the market bounces from this level by forming a higher daily high. But if you buy, chose issues that have reasonable, close supports that can be your stops in case the market resumes its downward moves.

S&P 500 Short Term Trends

Traders often speak of a resistance or support that occurs at major round numbers. This has nothing to do with price trends but is more of a psychological price barrier. What is a round number? It is any one that ends with a zero. The more zeros at the end, the more likely to be a resistance/support. For example, the following monthly price chart on the S&P 500 shows that when the market hit the 15,000 level in 2000, it retreated, revisited 15,000 seven years later and didn't surpass that level until 12 years later. Likewise, it found support around 800 and revisited that level three years later.

Why 15,000 instead of 14,000 or 16,000 (or 800 instead of 900)? No one knows. But the growing belief that, in this case, the dot com frenzy was a bubble apparently reached a bursting point at 15,000. Psychology is psychology and is mostly mysterious to many of us mere mortals.

S&P 500 Monthly Chart



Why am I talking about this? The next four charts illustrate a bunching of these round number levels across different markets in a grouping that I haven't seen before. The Dow Jones is fighting the 17,000 level; the S&P 500 is struggling with 2,000. Meantime, the Nasdaq 100 is bumping into 4,000 and the Russell 2000 small cap index can't break through 1,200. Everything seems to be bumping into and bouncing off of a "psychological" resistance. We will see if this signals trouble ahead, unfortunately seeing it will be in hindsight.

Dow Jones Industrials

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S&P 500

NASDAQ 100

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Russell 2000

Meantime, the current pullback seems to be hitting securities across the board. As such, we have seen a deterioration in most of our holdings. We have already sold several and put the funds into money markets as they have hit our stops. Others are close to their stop levels and could hit them if there is more weakness in the markets. If so, we will sell them as indicated. That is the important thing about having and honoring your stops. As the market deteriorates, you are successively taken to the safety of the sidelines. If there is a silver lining in this, it is that every downturn is the precursor to the next major upmove and therefore is setting up the next buying opportunity.

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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