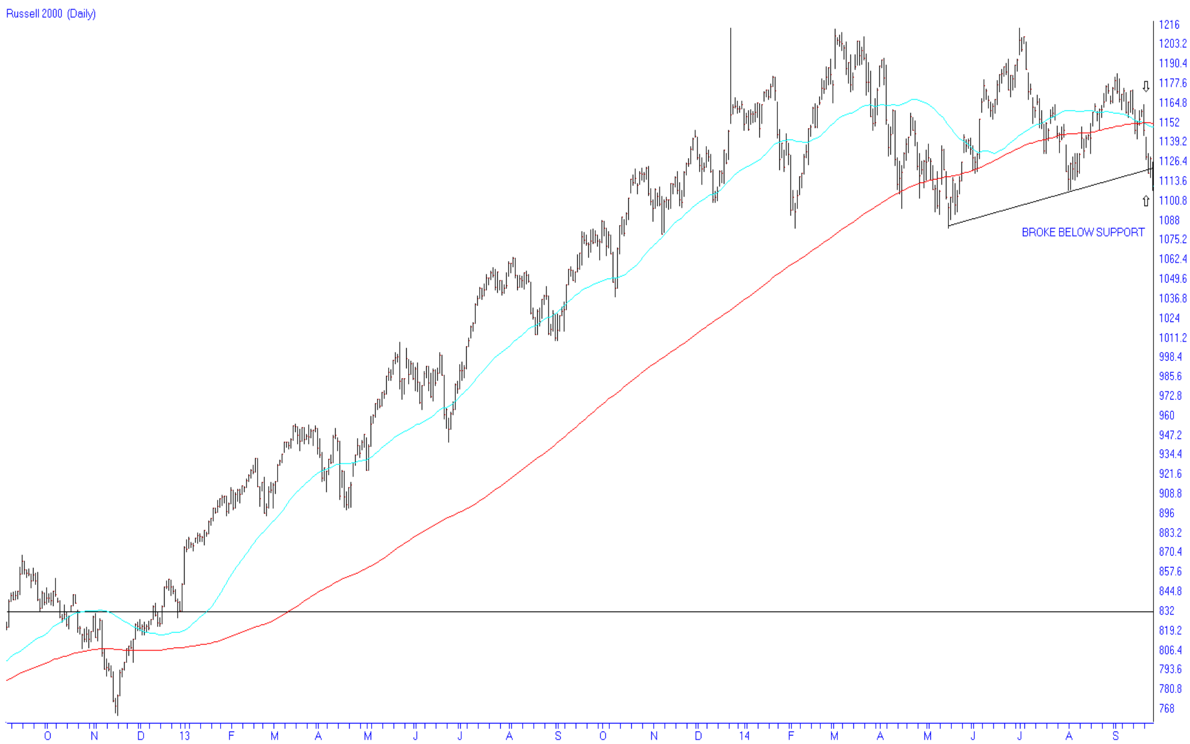
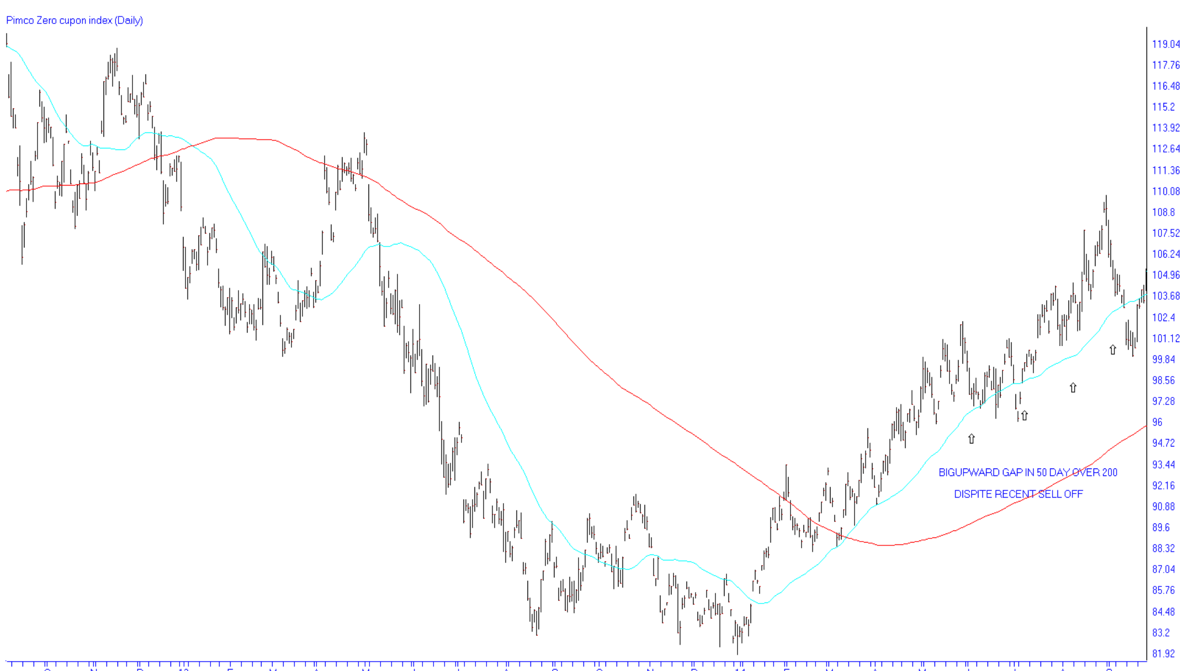
The Starboard Side Report

The week ending September 26, 2014

Charts of the Week



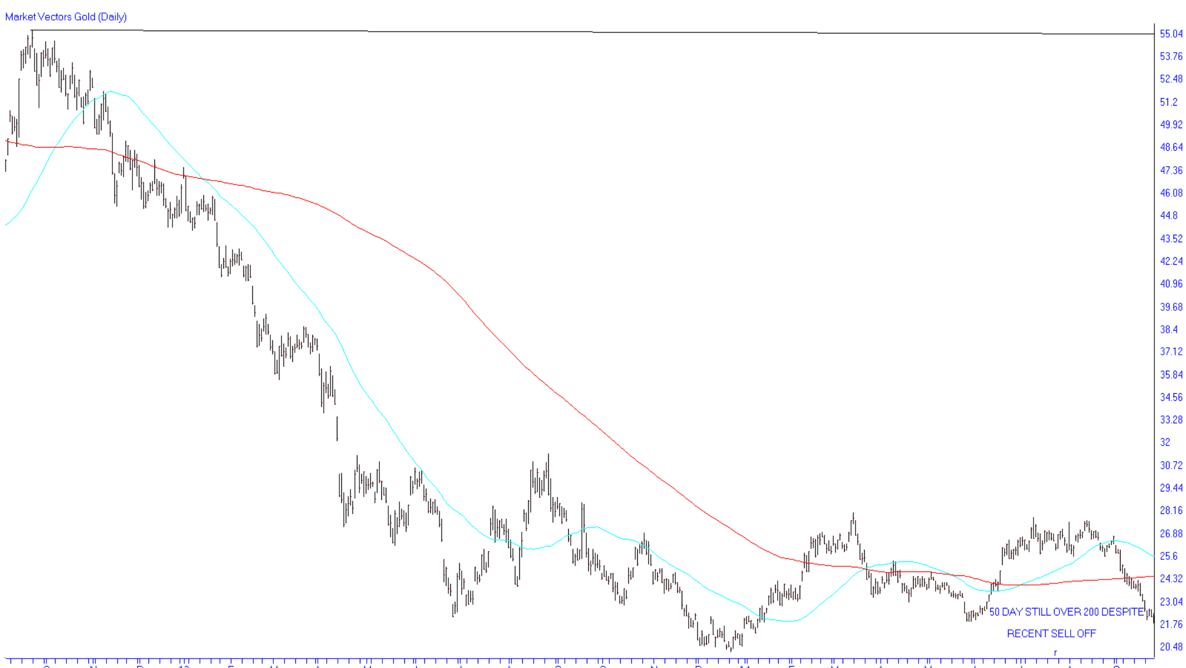


With this week's market decline and what now looks like a continued selloff of the market, I thought it would be helpful to look at how our major holdings have performed. We have a three-legged stool approach to defending against further declines; the Russell 2000 hedge, long-term zero coupon government bonds and gold. All three have held value and moved higher when the market has declined. And all three of these investments are uncorrelated to the market; thus, they should rise as the market sinks further.

TECHNICAL COMMENTS:

Today's first chart is the ProShares Short Russell 2000 (RMW) and it is the basis for our primary market hedge. The final break of the 50-day moving average below the 200 is very significant to our assertion calling for a market decline. This week's selloff has broken below a support line drawn from two previous drops. The Russell 2000 was the strongest index in the market rise. It was up 102% from the market bottom in 2009 and 37% in 2013. It was the leader of the rally and in my opinion will take the same place in the decline.

The second chart (at the bottom of the first page) is the PIMCO 25-year Zero Coupon US Treasury Fund ETF (ZROZ). It has proven to be strong the entire year despite selloffs like the one that took place recently. The big technical take away from this chart is the continued gap between the 50-day and 200-day averages.



The third chart (above) is the Market Vectors Gold Miners ETF (GDX). This is not as convincing as the first two legs of our stool, especially based on its recent negative trading action. The 50-day remains above the 200-day and this week, as the market sold off, the GDX rallied. Gold is usually uncorrelated to stocks, so the best impetus for a breakout to the upside will be our anticipated further decline in the market.

FUNDAMENTAL COMMENTS:

The markets function on a "risk on, risk off basis" driven by the availability of money in the economic system. Soon the FED will end its quantitative easing (QE). The last two times that they ended QE, the markets had a big correction. The higher risk holdings are usually the first to react to money changes in the economy; thus, the selloff in small-cap equities. Another area of high risk that has also broken down is High Yield Bonds. In my view, these breakdowns are a clear beginning of a major reversal, which should be followed by the Dow and the S&P collapse.

The Zero Coupon strength is reflective of a continued decline in interest rates. There is a lot of talk about rising interest rates; however, there is not enough economic growth to create higher rates. That, combined with the enormous debt on the developed world balance sheets, will drive rates lower. Low growth, along with high debt, is a recipe for a stagnant, deflationary economy, and that makes bonds attractive.

Gold can do well in a deflationary economy because it becomes an asset to hold due to the uncertainty surrounding the ownership of equities. When economic confidence is broken due to sovereign debt, it can affect the value of currencies for which gold becomes a substitute.

ASIDE:

Major market changes are created during times of large volatility swings. Recent market action in all of the areas of our three-legged stool has been volatile. An old Wall Street Saw states that "the trend is your friend". Focus on the trend (50 over or under 200 day) and when the price gyrations end, then price will follow the trend. The three charts in this report indicate that we are going with the trend.

<u>Please note</u>: It is the Client's responsibility to notify us of *any* changes that would influence their financial needs.