Starfox Financial Services, LLC

Market Update

October 2014

MARKET SNAPSHOT

DJIA	**17071**
Nasdaq	**4505**
S&P 500	**1977**
Comex GOLD	**$1217**

(closing values September 29, 2014)

Over the years our experience has shown us that risks and opportunities associated with the various assets classes change constantly as a result of changes in market and economic conditions. We believe tactically adjusting exposure to the various asset classes is a vital risk management technique. Because of our tactical approach to risk management, we tend to recommend our clients to be overweight areas of increased value and opportunity and underweight in areas of excess expense or risk.

Our in-house team of analysts monitor more than 60 market and economic indicators for signs of increasing risk and areas of developing opportunities. Over the past two years we have observed a significant (and growing) number of indicators that seem to signal, in some cases very strongly, growing stock AND bond market instability and growing levels of risk. Many of the indicators, taken by themselves, may appear to be just noise or even indicate possible strength in the markets, but when viewed together with other indicators in the context of a still recovering economy, signal what we believe to be an optimism that is not yet warranted.

Of particular concern to us has been the high levels of investor optimism based on what we feel are questionable earnings projections and the sharply decreased breadth of the stock market rally. While the headlines tell a story of seeming endless new market highs being set, a closer look reveals that these new highs have been the result a very few stocks doing very well; The majority of S&P 500 companies are trading below their 50 day moving averages, a trend that usually indicates valuations are too high. Despite the glacially slow growth of the economy, the wind down of QE and a stock market rally that has gone nearly three years without a correction even close to 10%, euphoric investors continue to express optimism for even higher highs. A similar optimism exists in the bond markets, with investors seemingly unwilling to accept that an eventual return to normal interest rates may have a significantly negative effect on portfolio values.

In order to mitigate the mounting risk in equities, we have lowered our stock exposure to 20-40% and focused on owning a diversified mix of quality dividend paying stocks. We have identified an opportunity in international equities and are prepared to increase our international exposure at or near current price levels. We also expect a significant correction in the domestic stock markets to provide an opportunity to increase overall equity exposure at an acceptable value. If, following a correction, the markets appear properly valued we may increase our equity exposure to normal levels.

With the ‘great recession’ several years behind us and a prolonged period of record low interest rates caused by round after round of QE, the major risk in the bond market is rising interest rates. As the economy improves and the Fed winds down QE measures, interest rates will eventually begin to normalize. With interest rates so far below normal, the return to normal can be a traumatic one for bond investors, especially if the return to normal occurs too quickly. In our view, the risks associated with investing in medium and long term bonds is simply too great and have limited our exposure to very short term bonds, floating rate funds and cash-like instruments.

Current Recommendations

Given the continued potential for a market correction of 10+% we recommend maintaining a reduced exposure (30-50%) to equities pending an 10% or greater correction.

We see an opportunity to begin increasing international exposure at current price levels with a target of 5-10% total exposure. Recommend rebalancing equities to include 5% broad international exposure and dollar cost average to a maximum exposure of 10%.

Given the current near zero rate environment, expected future actions by the Federal Reserve and because a return to ‘normal’ interest rate will put price pressure on longer duration bond holding, we recommend owning quality low duration fixed income and floating rate funds. Target total portfolio duration should be 4yrs or less.

***Risks to our recommendations include loss of growth potential due to limited exposure to stocks and potential credit risk when utilizing floating rate funds. Lower duration investments may not provide sufficient income from current interest to meet income needs.**

***Please contact us if you would like to discuss how our recommendations may apply to your specific situation.**
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