

# Interim Report

## Investment Commentary

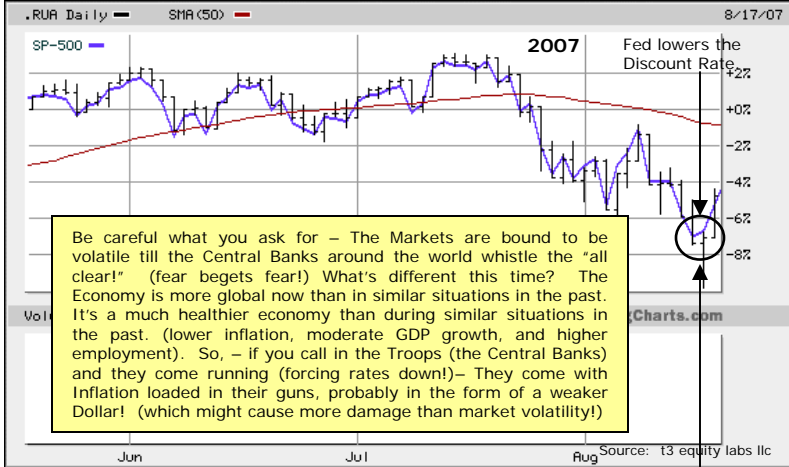
*Allowing for the Unexpected!*

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*thinking outside the box*

### Aberration, Over-reaction or Trend Change?



**The past is not predictive, but it can be instructive!**

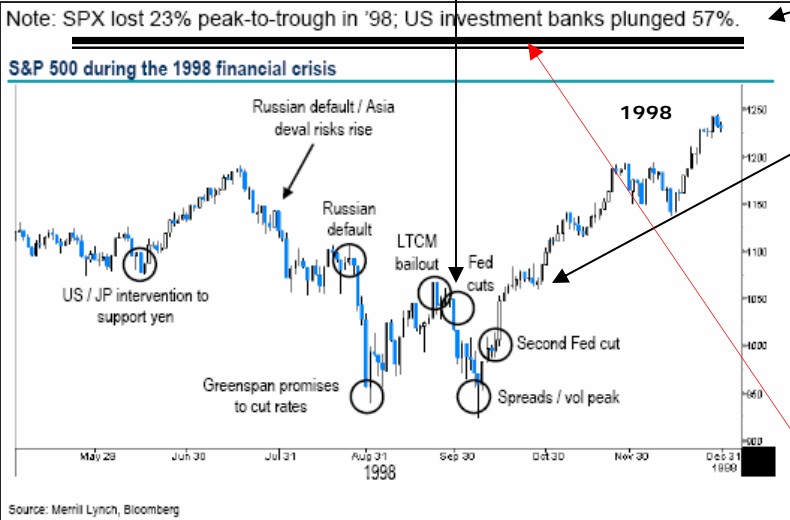
- Probably at least one more test of the lows.
- Probably at least one more headline failure.
- Probably another set of Interest rate cuts of some sort.
- More Sector volatility.
- More Oil volatility.
- More underperformance by most active equity managers.
- Plenty of liquidity around.
- More Global volatility.
- Dollar sets more lows vs. most foreign currencies.
- Hedge Funds continue to under perform as they take risk off of the table.
- Short & Intermediate Term fixed income (incl. munis) outperform.
- Small-Cap's will surprise as rates come down.

### Waiting for Capitulation!

"Markets have the ability to stay irrational longer than most have the ability to stay liquid".  
 John Maynard Keynes

(... from mortgage lending to hedge funds - Keynes might be more relevant than ever ...)

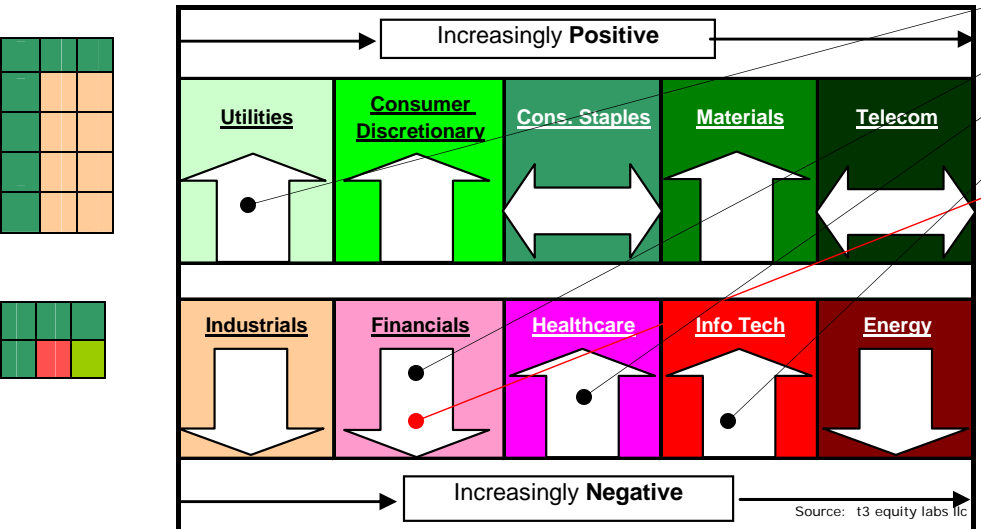
- In the mean time - what should I do?**
- Be cautious and patient..
  - Keep some powder dry!
  - Continue to look forward.
  - Focus on your Process!
  - Remember the only thing you can control is process and not outcome.
  - Interest Rates and Earnings are the best predictors of future market moves - both look good for the market.
  - Use Rally's to reduce risk!
  - Continue to upgrade the quality of your holdings.
  - Asset Allocation is the best way to manage market volatility vs. managing the manager risk in your portfolio.
  - Don't add risk or leverage even though both are cheaper!
  - Start reading a new book.
  - Find a new musician
  - Enjoy the end of summer!!!



This is the most sensible hypothesis of what's ahead I've read in the past couple of weeks. It comes from Michael Hartnett at Merrill Lynch. Lining up both charts suggests there's more volatility in front of us! Remember - the past is not predictive (regardless of trend!)

Notice how the rankings of the predicted earnings surprise model for the S&P 500 Sectors have changed in the past 30 days!

- Curiously, the best performing Sectors during the past 3 weeks have been Financials, Information Technology, Utilities, and Healthcare.



**Financials?**  
**Classic Value Trap? -**  
**Tread Cautiously!**  
*Bottom fish at your own peril!*  
 (Might be the Bermuda Triangle)



Michael C. Jackson  
 President/CEO  
[mike@t3equity.com](mailto:mike@t3equity.com)  
 1700 Broadway #430 Denver, Co 80290  
 303.860.7386 (office) 303.832.3044 (fax)

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