Ellumination
November 3, 2006

Two bull markets

The S&P 500 ($SPX) is charted below. As of the close tonight it remains within the upward trend channel that started in July. You can see that it has moved back to the bottom of its rising channel. We'll have to wait until Monday to see if it starts to slip below the channel or starts the next leg up in its zigzag rising journey. You can also see, at the top of the chart, that relative strength (RSI) is moving downward from the much overbought condition of a few days ago.

Pundits are split on what is next. For every one that is predicting the rising trend will hold, I can find you one who is expecting further declines. If it does continue to decline then the next big support for the $SPX would be down around the 1340 level, or the 50 day moving average. See the blue arrow that is placed below the "bottom of rising channel" comment. That would be a further correction of about 1.75 percent. Longer term support is down at 1294, or the 200 day moving average. That point is 5.13 percent below the current close of 1364. There is nothing in the current technical picture of the market that would indicate a correction of that magnitude is at hand. Until that rising channel actually breaks down it represents the current trend which is upward.

One small cautionary note comes from our VE quantitative model which shows the $SPX "model price level" to be 1329, or about 2.87 percent below the current closing price. That means that according to our model the stock market is slightly overvalued. So we are not expecting a dramatic sell off. In fact, the most likely case is for the U.S. stock market to get stuck in a narrow trading range for the next several days or weeks. (Assuming oil prices do not climb above $62.)

On the other hand, our old friend GOLD seems to have gotten a breath of new life and is breaking out to the upside. We told you a few weeks ago that if the December gold futures broke above $610 we would be a buyer again. Well it did, and we are. We are buying back the street TRACKS Gold Trust Shares (GLD).

GLD recently completed a normally bullish chart pattern called a "reverse head and shoulder". See the three blue arrows near the bottom of the GLD daily chart.

Once the "reverse head and shoulder" was complete you can see the breakout above the 50 day MA (squiggly blue line) and the 200 day MA (the red line rising just above the reverse head-and shoulder) and finally a clean break above the straight declining blue trend line. OK, got it?

You can also see the upward trend of relative strength (RSI) (look at the top section of the chart) and the rising trend of the histograms (look at the bottom part of the chart labeled MACD).

Don't be surprised if GLD pulls back and touches the top of that straight declining blue line, before proceeding upward again. That line now represents "support". But if that test is successful by virtue of the GLD price bouncing off the line and heading back upward; or if the test never happens and GLD just keeps marching upward from here, it looks like we have a gold bull move on our hands again.

If you have received your October statement yet, we hope you are enjoying it. It was a good month for all four of K&A's major model portfolio groups; and it is turning out to have been a good year so far.

Model Group or Index	Hatteras	Mendocino	S&P 500	Halifax	Bonavista	Lehman Aggregate Bond
Time Weighted Return (TWR)	12.27	12.11	10.39	9.39	6.98	3.94

Here are the returns for our four main model groups from January 1-October 31, 2006. While all four models vary significantly in their specific investments, they are all "balanced" portfolios featuring stocks, bonds and cash. We think the returns are pretty darned good for balanced accounts in 2006, particularly when the low volatility that accompanies these returns is taken into consideration.

Returns illustrated are net of management fees, custodial fees and trading costs, underlying mutual fund management fees, and other fund expenses such as short term redemption fees. All dividends and capital gains were reinvested. The performance numbers presented here represent the composite performance of all client accounts managed by K&A that are included in each of the four model groups. Individual account results may vary from the blended performance for a variety of reasons, including the cash flow requirements of individual account holders. No adjustment has been made for income tax liability.

We continue to work on (incubate as we call it) the new model which has been dubbed Fresnel. It is a much more focused portfolio model that tends to feature fewer positions and much higher concentration per position. It too has been “balanced” this year in that it has held stocks, bonds and cash. We have tended to limit the number of holdings between 10 and 15 positions. The return from January 1-October 31, 2006 has been 18.89, using the same criteria as in the box above, and using the K&A 2006 fee schedule. We will be doing a “roll out” of Fresnel to interested parties in January 2007.

We’ll be back on Monday to make the most of a new week for you. Have a wonderful weekend. Rob and Linda, have a good trip to China along with 170+ other people from St. Helena. It should be a lot of fun.

All the best,

Paul Krsek
For K&A Asset Management, LLC

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During 2005 Paul Krsek was appointed Chief Investment Officer of K&A, and as such is responsible to make all trading and management decisions for all client accounts which are being managed according to a specific portfolio model. A description of each of our models can be found on our website at http://www.kaassets.com/choices.htm.

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Paul Krsek and Rob Andreae frequently discuss investment ideas, model portfolio strategies and the investment policies of K&A. But when it comes to the implementation of those polices Krsek is primarily responsible to manage the accounts that fit into each model portfolio description. He makes all final investment and trading decisions relative to those accounts that are considered to be “modeled.”

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No securities that are 'requested by the client' will be held in modeled portfolio accounts.

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Sincerely,
Paul Krsek
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