

# THE NAVIGATOR<sup>®</sup> REPORT



CLARK  
CAPITAL  
MANAGEMENT  
GROUP INC.

FIRST QUARTER 2003

## Cross Currents

What a way to start the year! Talk about confusing. Just when everyone thought the market decline of 2000-2002 had ended in October of last year, the bear makes a last stand, scares investors to death, and almost establishes a new low in March. Just goes to show that the market cannot stand uncertainty and the possibility of war or no war was certainly the major uncertainty for most of the first quarter.

**“this is still the last,  
best buying opportunity  
of the decade”**

DONALD H. ROWE  
*Wall Street Digest*

The quarter began with a wonderful rally that lasted all of six days. Short but powerful as the Dow Jones rose 5.70% on those six days. But, alas, it didn't last long as the market peaked on January 6 at 8,775 and proceeded to plunge 9% to 7,990 by January 27. It was an ugly way to begin the year. Fortunately, we had allocated to cash at the close on January 6 and avoided the decline. All Navigator Asset Allocation accounts were allocated to money

markets, at their assigned weighting of 30% or 100%, on January 6 thereby avoiding the nasty decline. Those accounts were then reallocated to their invested positions at the close of the market on January 27. Navigator Asset Management accounts include the Master Program, Premier Equity, Premier Tax-Free, and Premier Balanced. The Master Program assets are protected by the Navigator Sentry protection strategy utilizing derivatives

while the Premier Equity and Balanced accounts are partially hedged with an option writing overlay if chosen.

Over the next several weeks the market wandered in a four-hundred point range between 7,800 and 8,200 on the Dow Jones Industrial Average while awaiting the U.N. to resolve the diplomatic problems caused by the French, Germans and Russians opposition to the

U.S. and British desire to topple the regime of Saddam Hussein. Among all this infighting (by supposedly U.N. allies) the market began to plunge and reached a low of 7,525 on the day before the war began. That was below the low of last July 23rd, but above the October 9th low of 7,286 on the Dow Jones. So at least for now the low for the three-year bear market is still October 16th.

When the war began the uncertainty was finally lifted, as were investors spirits. The market took off for one of its' best gains in years. The week following the beginning of the war produced the best one-week gain since October 1982. The Dow Jones gained 8.4% for the week and 13.2% from the day before the war began to the end of that week. Of course, nothing that good can last for long these days and the market has been either brooding or celebrating depending on how the press portrays the war progress. As of this date, April 10, the market has settled to about 8200. It remains to be seen whether the MOAR (mother of all rallies) will begin when victory is declared.



## Then vs. Now!

While there are similarities between Iraq I and Iraq II there are also some disturbing differences. Ned Davis Research points out several valuation parameters that are, at the least, slightly disturbing.

	1991	NOW
S&P 500 P/E	15.5	27.7
S&P 500 Div Yield	3.75%	1.91%
Mutual Fund Cash	11.4%	4.4%
Bullish Sentiment	33.6%	46.6%
Stock % Financial		
Assets: Individuals	17.7%	29.7%
Institutions	24.4%	34.6%
Credit Market Debt	13.8B	31.7B

Looking at the figures above must make one wonder if we really have had three years of down market. One could say that the figures for NOW could just as easily be those seen at a market top and not after a three year decline. Iraq I was the kickoff for one of the best decades this country has ever seen. Will Iraq II have the same effect?

Another difference now is that in 1991 the market actually bottomed when the war began while here the bottom (at least for now) was last October 9th. We have already had a rally from that low of about 14% based on the Wilshire 5000 index which measures the approximate value of all stocks traded in the U.S. Now a rally of 14% would not bring the numbers above, comparing 1991 to Now, into line but would make the comparisons more realistic.

An old adage says, "war is bullish." There is every reason to believe that this war will have the same effect. Just think of the possibilities for world order if the U.S. achieves the goal of a democratic republic in the very heart of the Middle East. If the war is over in two to three months and there are no major terror attacks in the U.S. then I think that there is every reason to believe that this war will have the same effect on the market as prior conflicts. That is the market should move higher by 25% to 30% over the months following the beginning of war. Since the S&P 500 is already up about 10% from the day before the war began, we can look for another 15% to 20% move in the months ahead.

In the "history repeats" category, I came across an interesting comparison of the events that lead up to Iraq II and the period around the Cuban missile crisis. In those days the Soviet Union was try-

ing to block a U.S. British resolution condemning Iraq for a 1963 terrorist attack on Israel. North Korea established an atomic energy center and threatened to join the elite nations with nuclear capability and Canada proposed that the U.N. make on-site weapon inspections in Cuba. Things never change!

## Smart Money

There is an interesting way to determine what the so-called "smart money" is doing in the market. The Hayes Advisory Group tracks this theory and the charts shown are theirs. The theory goes that smart money acts at the end of the day after evaluating that day's news. The opposite of smart money is emotional (not so smart) money. These investors usually act first thing in the morning after hearing the overnight news and watching CNBC for their morning fix. Historically, the smart money is a good predictor of future market direction while the emotional money is usually wrong. The first chart shows the "smart" vs. "emotional" buyers while the second shows the "smart" buyers compared to the Dow Jones Index. Notice that the "smart" buyer index is making new highs while the emotional buyers (or sellers) are making new lows.

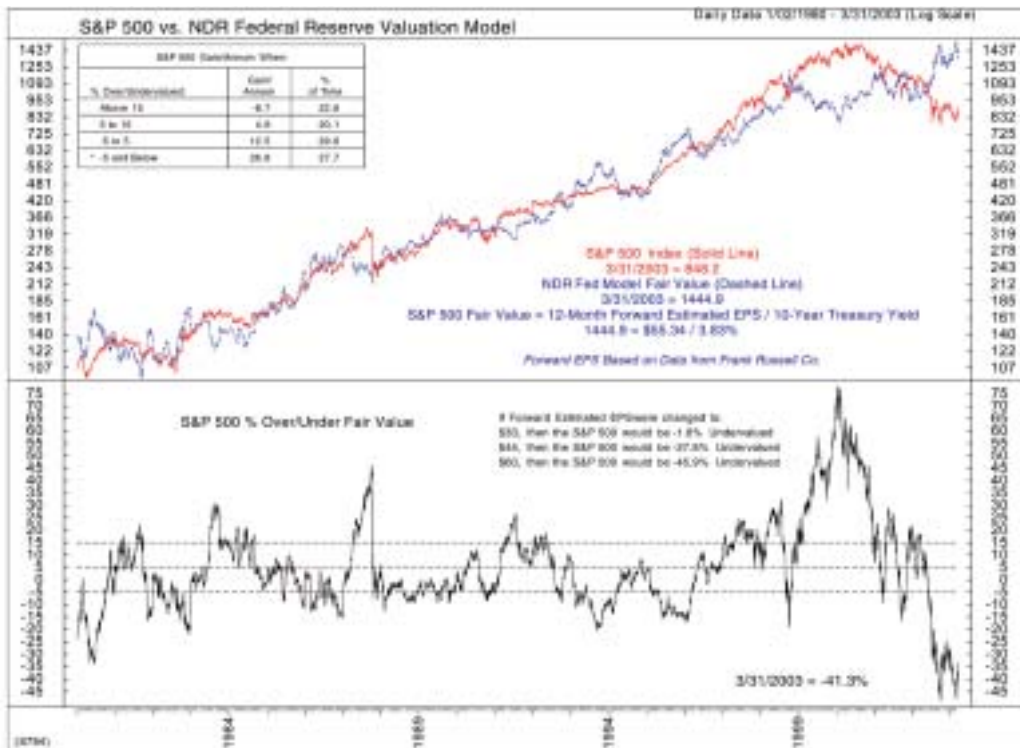


In addition Steve Leuthold, from the Leuthold Group, who I consider to be a “smart buyer” says “We’ll emerge victorious, and then I think we’ll have an explosion on the upside, a rally of at least 1,000 points on the Dow over a couple of weeks. This is the time when people should be building positions, unless they think we’re going to lose this war.” And from the Wall Street Digest “this is still the last, best buying opportunity of the decade, and I believe the market will experience an impressive rally between now and at least mid-June.”

## SALE PRICES

The Federal Reserve Valuation Model chart, from Ned Davis Research, has been shown here before. I am showing it again because it is important to keep the current situation in proper perspective. The American public loves sales. They will buy almost anything if it is on sale. The U.S. is on sale in terms of some of the best companies in the world. Yet, the American investing public is looking the other way even though U.S. stocks are having their biggest sale in several decades!

Source: Ned Davis Research



The valuation is based on forward earnings of about \$55/share. Some say that this is too optimistic. Even if you haircut the earnings by 20%, the under valuation is still over 25%. According to Ned Davis Research, the market has been undervalued by 5% or more 27% of the time. The annual gain on these occasions has been over 26%. The fair market value of the S&P 500 with earnings of \$55 is 1,436. The present S&P 500 value is 868, which means that it is undervalued by

39.5%. If earnings dropped to \$40/share, the fair value would be 1,044. Still a 17% under valuation! If history is any guide, it seems to me that the sale is still here and, as usual, the investing public will be left behind.

Mutual Fund shareholders have been liquidating shares at record levels; \$10.6 billion in February alone. Meanwhile they have been buying bond funds like there is no tomorrow; \$18.6 billion in February. Where do you think the next bubble might develop. Could it be a bond market bubble? It would take a very slight increase in interest rates to cause a decline in the bond market. Today's low yields do not offer much protection to a decline in bond prices. Once again the public will get fleeced. Large equity fund liquidation has always been a sign of a good market bottom; this will be no exception.

## ETFs

You are probably saying what does ETF mean and why is this here? ETF stands for Exchange Traded Fund. These are mutual funds that trade as securities on listed stock exchanges and

they are the fastest growing investment vehicle on the financial landscape. Assets have grown from \$1.1 billion in 1995 to \$102 billion today. Someone once called them ExTraterrestrial Funds because of all the advantages they offer. You have probably already heard of these securities as i-shares or webs. Names such as Diamonds, Spiders, Vipers, and QQQs are but a few of the possibilities. There are presently 113 ETF's trading with more being added regularly. These funds track broad stock market indexes, sectors, countries, regions, and fixed income groups.

### Advantages include:

**Low management expense ratios:** The fee or management expense ratio for the average

actively traded mutual fund is about 1.5%. ETFs range from 0.12% to 0.85%.

**No style drift:** ETF holdings are transparent since they are indexed based. You know what you are getting.

**Exchange traded all day:** Same advantages of mutual funds with trading flexibility.

*Index based:* You may buy one ETF and get the benefit of an entire index of stocks.

*Tax efficient:* Low turnover minimizes taxes.

Several Navigator programs utilize ETFs. There is an ETF STAR allocation program, Strategic World allocation program, ETF option writing program, and ETFs are used as satellite managers around our core Master managers in the Navigator Master Program. Please ask your financial professional if ETFs can benefit your investment program.

## Conclusion

It seems as though the war in Iraq is going to be a huge success. Investors will once again look to underlying fundamentals of the economy going forward. There is an absolutely huge cash hoard sitting on the sidelines. Returns from money markets, CD's etc. are anemic to say the least. Any good looking rally will likely tempt those waiting back into the equity market. We have many appropriate investment programs which will capture the rallies to come. The fact that the market is almost 14% above the low point of 2002 is very encouraging given the world situation and the economy today. This market is telling us that better times are ahead.

## Quarterly Statements On-Line

As many of our clients know, we now provide quarterly statements via the Internet. This is because many of our referring financial professionals as well as many clients, are trying to become paper free. They wish to access their accounts when and from where they wish so we have arranged for Internet access.

Accessing your account on-line is a very easy process. The web site address is **www.CCMG.com**. Next go to the heading "Your Account". The user ID is your CCMG account number and the password is the last four numbers of your social security number.

Any client who wants to receive paper statements only has to call the office at **800-766-2264** and make that request. The statement will be in the mail that day and will continue to be sent every quarter thereafter.

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**All CCMG performance figures in this Report are net of fees and expenses. Past performance is not a guarantee of comparable results in the future. The sited data have been prepared utilizing a methodology consistent with industry standards.**

\*CCMG accounts are managed through the use of tactical and strategic asset allocation methods and utilize the buy and sell indications produced by these methods to determine when clients should be invested in equity securities. When a buy signal is generated clients' accounts are invested in equity securities, and, conversely, when a sell signal is generated their accounts' equity positions are liquidated and invested in money market accounts and other cash equivalents. The performance data cited above reflects the effects such buy and sell signals would have had on an investment in the market indices and mutual funds discussed for the time periods indicated for all CCMG clients invested in the Navigator Classic Program. The buy and sell signals used in such information are actual signals generated by CCMG's methods during the periods portrayed. Client accounts may or may not have been invested in the referenced indices or funds during the periods portrayed. The cited performance data assumes the reinvestment of all dividends and capital gains distributions, and reflects the deduction of the maximum management fee charged by CCMG for the referenced program and actual mutual fund expenses. Historical performance is available upon request.