



CLARK CAPITAL
MANAGEMENT GROUP, INC.

Third Quarter 2009

THE navigator™ REPORT

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WOW!



Just for fun, let's go back to February of this year and remember what things were like then. Unemployment was soaring with 800,000 jobs being lost per month, Lehman Brothers went bust, Bear Stearns barely survived, AIG and CitiBank were national embarrassments, Merrill Lynch had to be rescued by Bank of America as did Countrywide Mortgage, people were afraid to look at their 401K accounts let alone their brokerage accounts, brokers were hiding under their desks, consumers would not part with a dime, houses were being foreclosed on in record numbers, money was impossible to borrow, we were in the midst of a market decline that was following the 1929-1930 decline to a fault and in boardrooms across the country you could hear a pin drop. All this does not come close to describing all of the nasty things that were happening in this country and in the rest of the world at that time. Of course, with all of this going on, the big D word was on everyone's lips.

With all of that in place, on the CNBC program "Closing Bell," on March 3rd, I said that *"the market bottom was a few days away."* The S&P 500 was at 696 that day and, as we know, the bottom was four market days later on March 9th at 676. The bottom was confirmed on March 10th with a tremendous breadth thrust (when advancing stocks and the volume of advancing stocks totally overwhelm declining stocks). On a CNBC "Special Report" on March 19th, the week following the bottom, I said *"We are convinced that the market bottomed last Monday,"* and on March 24th, on "Squawk on the Street," I said that *"we have seen a 'generational low' whose level would never be seen again."* **Market bottoms are like that. They happen when no one is looking, everyone is disinterested, and no one believes it is even possible.**

So what has happened? **We have just completed the best two quarters since 1975!** The S&P 500 gained 15.9%

in the second quarter of this year and 15.3% in the third. What is remarkable here is that prior to these great positive quarters, the S&P 500 was coming off six negative quarters from the last quarter of 2007 through the first quarter of 2009.

We have just had seven positive months in a row! This is only the sixteenth time in the 80 years since 1928 that stocks (S&P 500) have advanced for seven months in a row. Since WWII, there has rarely been a time when stocks kept advancing for more than a month or two following seven months of gain. Does that mean that we are in for a healthy correction? Maybe! This possibility will be covered further on so keep reading!

We have had the best single quarter since 1998! The Dow and the S&P 500 both surged over 15% in the third quarter.

WOW!! Who would have guessed that our near economic death experience would turn out this way?

Another milestone was crossed recently when the S&P 500 advanced over 20% **above** its 200 day moving average. This highlights the remarkable turnaround from the bottom of early March when the S&P 500 was over 20% **below** its moving average. If you are wondering if this has ever happened before, the answer is Yes! It has happened three times before, in 1932, 1938, and 1975. Each time the market suffered a correction averaging 12.2% before moving higher. Seems that this could be concrete proof that the market will have a fairly good correction, or does it? Again, more on a correction later.

For a wrap up of the year and third quarter I will use some items from Don Hays work. Results are as of September 30, 2009.

The total return for the Dow Jones total market index is +15.8% for the year. The S&P 500 total return is +15.3% for the quarter and +19.0% for the year. Financial stocks led for the second and third quarters and are +19.2% for

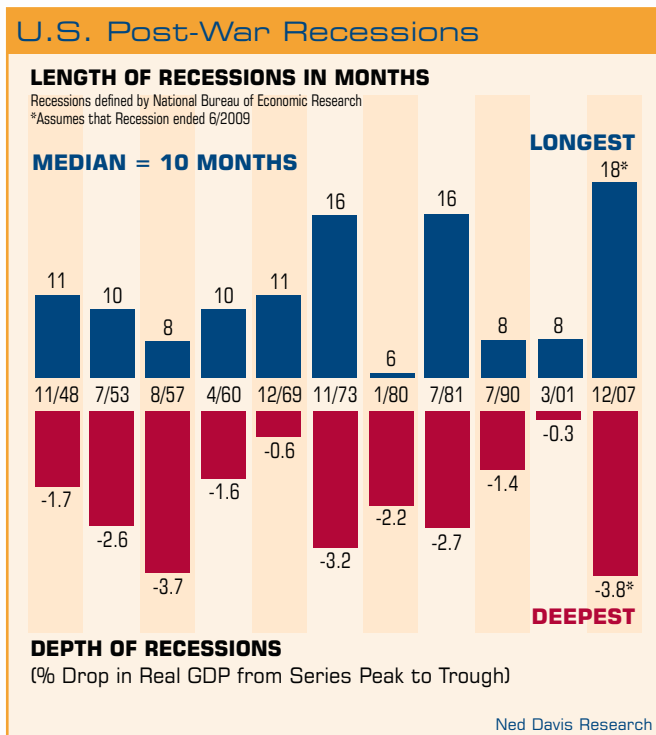
the year. Technology and basic materials are the best performers for the year and are +44% and 36% respectively. Growth stocks led for the year and mid- and small-cap stocks have been best. Latin America leads all international regions for the year at +76.2% and the Emerging Markets are second with +60.7%. During the third quarter, Europe was the surprise and was in second place overall.

In terms of holdings in these areas in our International Explore sleeve, we have been heavily invested in Latin America, specifically México and Brazil for a good part of the year, were heavily invested in the Emerging Markets early in the year, and have been moving into Europe for the past two months. So, in short we believe, our Relative Strength studies are keeping us in the proper areas of the world markets.

THE INDIVIDUAL INVESTOR

As usual, individual investors seem to be the wrong way Corrigans of the investing world. Yes, many were very hurt in the last bear market and have suffered, or seen others suffer, in the recession. The chart below, from Ned Davis Research, gives an excellent pictorial view of recessions in the post-war era and clearly shows how devastating the most recent one was.

While we believe that the recession ended in June, it is still unclear how the recovery will take shape. In my



opinion, unemployment will not reach a peak for ten to twelve months after the recession ended. This does weigh on peoples' minds as they see the numbers rising steadily. Overall, in the recessions shown above, the average time to peak unemployment was seven months after the recession ended. The worst case was following the 1990-1991 recession where unemployment rose for 21 months!! We believe this time will be longer than average but nowhere near the 1990-1991 experience.

So while individual investors have been shunning the market, they have not been sitting still. They are, in my opinion, moving the wrong way and into the wrong investment vehicle, bonds. The charts on the next page show how mutual fund investors are shunning equity funds and moving into bond funds in a very big way.

The Investment Company Institute reports that in the month of August there was an outflow of over \$2 billion from equity funds and that has continued in September. Inflow to taxable bond funds, typically a safe haven, rose to \$29 billion in August. **This is the largest inflow since records became available in 1997.** We know that interest rates are very, almost historically, low on bonds and that means that bond prices are almost at historic highs. What do these investors think will happen when rates begin to rise, as they inevitably will? Bill Gross of PIMCO, an acknowledged guru on the bond market says, "The New Normal may be to avoid bonds." Bond prices will fall! Did I mention wrong way Corrigan above?

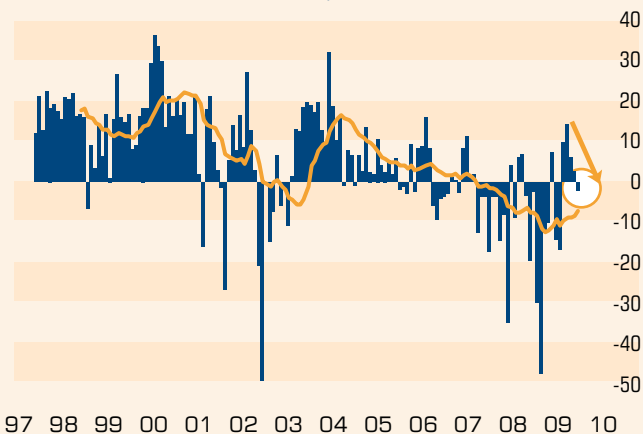
What this does mean is that there will be plenty of money around to support further gains in stocks. When the assets in bond funds are added to other assets in "safe havens" on the sidelines, there is approximately **\$3.5 trillion that could potentially enter the equity markets.** This is about 35% of the entire equity market. In addition, we know that a great many individual investors will eventually throw money at the equity markets when they can no longer stand the pain of missing out on gains. This has always been the picture at major, and minor, market junctions and it will be the same this time.

OCTOBER ???

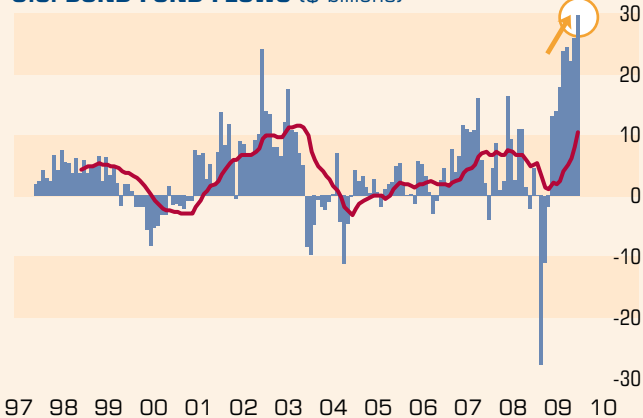
Of all the months during the year, October has the worst reputation for being a bad month. That reputation is not quite accurate but there has been enough nastiness during October to justify that opinion. October 2008, of course, contained the 11th waterfall decline of the last century when the equity markets had a ten day meltdown of

Investors Are Moving Out of Equity Funds and into Bond Funds

U.S. EQUITY FUND FLOWS (\$ billions)



U.S. BOND FUND FLOWS (\$ billions)



Source: Investment Company Institute & Brown Brothers Harriman

over 24%. Other occurrences were October 1987 (-23.22%), October 1929 (-20.36%), and the Ruble/Long Term Capital Management debacle in 1998. In actual fact, October is the 6th best month of the year and the month that has seen more bear market bottoms than any other. Bear markets of 1946, 1957, 1960, 1962, 1966, 1974, 1987, 1990, 1998, and 2002 all ended during October. September and February are the two worst months of the year and the **coming months of November, December, and January are the three best.**

WHERE DO WE GO FROM HERE?

The S&P 500 has gained 19% so far this year (to 9/30). While this is a remarkable feat following the havoc of last year, the 19% gain pales when compared to the gain for the bottom of the market during the dark days of March as described above. **The gain from the S&P 500 closing low of 676 on March 9th to the end of the third quarter at 1057 is 56.4%.** Now that is some gain! The gain had been a little higher several days ago at 1071.6 but there was a small pullback during the last two days of the quarter.

While this gain of 56.4% seems too good to be true, it actually is a bit shy of the average gain following the type of devastation that we had seen earlier, especially during the “waterfall decline” of October 2008 which actually was the internal bottom of the bear market when 88% of all stocks hit new 52-week lows. That decline was the eleventh decline of its type since the depression and the average recovery for those declines was 65% over the following seven or eight months. So it appears that we may have more to go.

Although if history is a guide, as it usually is, there are some disturbing statistics that tell us that if the present administration in Washington remains in place, and Congress maintains its status as the same party affiliation as the executive branch, our gains might be for naught. History tells us that when opposite parties control the White House and Congress, the market seems to perform the best. When the President and Congress are from the same party, as today, the stock market seems to make little headway. This can be referred to as Gridlock compared to Single Party Monopoly. The statistics:

In the 12 years (1980-1992) when the Republicans (Reagan and Bush) were in the White House and the Democrats controlled Congress, the S&P 500 gained 227%.

From 1992-94, the Democrats controlled everything and the market rose just 9.5%.

From 1994-2000 under a Democratic President (Clinton) and a Republican Congress, the market rose 209%.

From 2000-06 Republicans controlled everything and the market rose just 3.6%.

IN THE NEWS



Harry Clark, CEO of Clark Capital Management Group, appeared on CNBC's "Closing Bell" on September 29, 2009.



Sean Clark, CIO of Clark Capital Management Group, appeared on CNBC's "Squawk on the Street" on September 10, 2009.

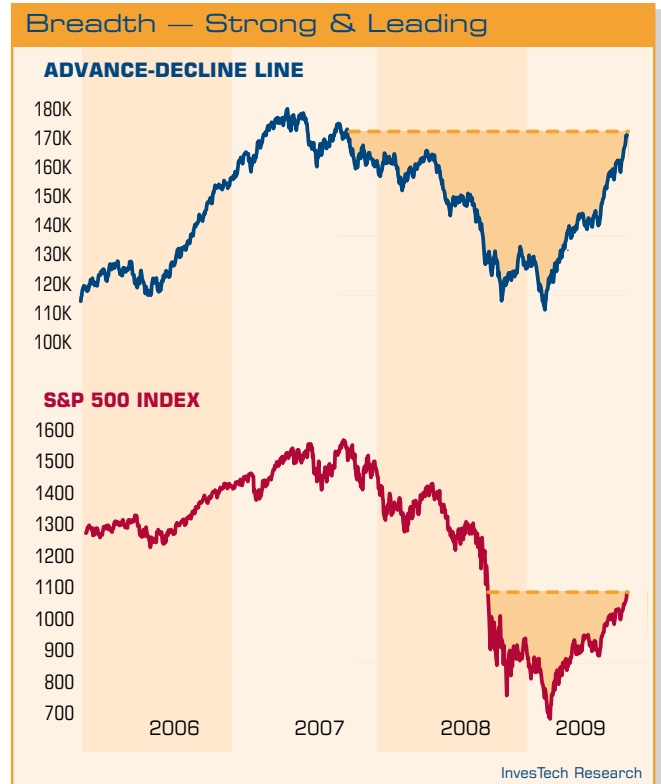
CONCLUSION

Earnings season will soon be upon us. A better than expected earnings season should give the current rally some additional staying power while a disappointing season will likely cause the rally to stall. We do, however, expect a positive bent to current earnings. Since 1936, when the trend in earnings has been negative over the prior twelve months at -15% or greater (as it was), earnings growth over the next twelve months has been up an average of 27.7%. In addition, there has never been an instance where the year-over-year growth in earnings over the next twelve months has been negative.

We have discussed market breadth (advancing vs. declining stock prices) several times in the past. The line formed by market breadth is an extremely good predictor of the path the market will take. The chart below shows that market breadth is almost back to its high of 2008 while the S&P 500 is nowhere near its 2008 high. During the 2007-09 bear market, every time market breadth fell the market followed. Just as now every time breadth advances, the market follows and moves higher. This should be a very positive sign that further gains are in store.

More hopeful signs! When, on average, twice as many stocks rise as fall on the NYSE over a 10-day period. History shows that the S&P 500 will gain 15% over the next six months. This blast-off signal is rare but has occurred three times during this rally: late March, late July, and during September!

So how far do we expect this rally to extend? **A logical target, and one that quite often will cause a rally to pause and correct, is when the recovery hits the 50% retracement level of the entire prior decline.** That level is 1120 on the S&P 500, so, I believe, that this could be a very logical point for the long awaited correction of the rally from March 9th to begin. The quarter ended at 1057 so a move to 1120 would be about a 6%



gain. This does not seem unreasonable and would just make this rally from the bottom, an average rally of 65.6% following the “waterfall” decline theory from above.

But be aware! Corrections can, and will occur, in any market recovery. And they can be sharp and violent. It would be logical to expect a correction from the 1120 level of, in my opinion, 8% to 12% before the market moves higher into yearend.

So enjoy your statement that is enclosed with this publication. Things do feel so much better in the markets and the economy than they did just several months ago. Let us all hope that the recovery continues, the market recovers more lost ground, unemployment finally stops rising, and, God willing, peace comes to those parts of the world in turmoil.

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