



CLARK CAPITAL
MANAGEMENT GROUP, INC.

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THE *navigator*TM REPORT

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THE "FEAR FACTOR"



The quarter that just ended was, no doubt, the worst since the depths of the last bear market during 2008 and into 2009. If you listen to most commentators on the major investment shows, not only is the sky falling, the recession is back and the economy is sinking toward another depression, the Dow Jones will drop to 3000 and our way of life is on the verge of extinction. Well, I guess that is stretching it a bit but almost everything you see or hear these days about the economy, the stock markets and our country is doom and gloom. Some recent headlines:

"Scared Consumers Raise Fears of Double Dip Recession"

Fox Business

"Don't Rule Out a Double Dip Recession"

Wall Street Journal

Even though Double Dip Recessions are rare, there only being one in the past 82 years, it still is the major worry among investors. Goodness knows that fear is a common commodity these days with talk of a weak housing sector, high unemployment, record national debt levels, tax increases, out of control government spending, the sovereign debt crises in Europe, and, of course, the Gulf oil spill. No wonder the Fear Factor is so high.

All the rhetoric has taken a toll on the investing public and has caused investor sentiment to plummet to depths last seen at the major stock market bottom of March 2009. The implications of this doom and gloom are really quite positive as I demonstrate later in this piece.

For the second quarter, the S&P 500 declined 11.41%, the Dow Jones lost 9.91% (and is below 10,000 again), and the NASDAQ Composite declined 11.82%.

What really got the "Fear Factor" going was the 15% decline on the S&P 500 over the last ten weeks from its high of 1217.28 on April 23rd to the low of 1030.71 on June 30th.

This decline includes the "Flash Crash" when the Dow Jones declined 1000 points in a matter of minutes (in a flash) before recovering part of the loss. That decline has been dubbed the "Immaculate Crash" because no one has yet determined the reason for the rapid decline. This all brings back memories of the "Waterfall Decline" of about 30% during 2008 which led to the internal bottom of that bear market. The market had risen 83% from the final bottom on March 9, 2008 to the high on April 23rd and was in need of a correction. In the first quarter Navigator Report, I asked the question, **"Will the bull market continue or should we sell in May and go away?"** I also said, "So it seems that we will see a 10% or larger correction before we get to the top of this bull market." You might recall that I made that statement because during the past 80 years, no bull market has made its final high before experiencing at least one 10% or greater correction.

So now we have our correction, next we need the new high to reflect the past 80 years of history. The bull market that began on March 9, 2009 is not over, just taking a breather. The economy has not ceased growing, it is just taking a breather!

HOW DID WE DO?

The age old question asked every Investment Advisor at the end of every quarter is "How did you do?" Our answer is "very well!" While I would like to show every one of our programs and results for the quarter I can not because of disclosure regulations. Instead I will refer you to your quarterly statement where your performance is detailed and compared against several major indices.

There have been some significant changes in the quarterly statements. We show “Household” performance which combines all accounts of related persons residing at the same address. For example, an investor might have a UMA account, an ETF Explore account, and possibly a separate bond account. There could also be separate accounts for a husband or a wife at the same location. We then show what percentage of the total each account contributes as well as an asset class pie chart showing what type of equity or bond investments make up the total Household. Also shown is cumulative Household value and cumulative Household performance. This performance is then compared to several indices. Next shown is the performance, asset allocation, and sector allocation of each separate account that makes up the total Household.

Of particular importance are the “standard deviation” and “beta” of each individual account as shown in your statement. Standard deviation is used to assess the degree of risk of a given investment or account. An investment with a higher risk is more volatile and has a higher standard deviation. A less risky investment has a lower standard deviation. Standard deviation for the S&P 500 will vary based on the age of each account. Compare your account to the standard deviation to see if we are taking more or less risk in managing your accounts.

Beta is a measure of the volatility, or systemic risk, of a portfolio compared to a market benchmark. The beta for the S&P 500 is 1.00. Compare your account beta to 1.00 to see if we are assuming more or less risk in the way we manage your accounts.

THE BLACK SWAN

In olden days it was thought that only white swans existed. However, in 1697 black swans were discovered in Australia. In the book, “The Black Swan,” Nassim Nicholas Taleb postulates that any “highly improbable” event should be called a “Black Swan.” He was one of those stressing that banks were relying far too much on traditional risk analysis and were not taking into account that a “highly improbable,” or “Black Swan,” event could happen. Of course he was proven correct as our banking system teetered on the edge of a precipice and had to be rescued by the government.

So how does this impact us. In the book Mr. Taleb says to “Insure it (if possible) against losses, of more than, say, 15 percent.” That describes our Sentry program which attempts to provide a downside hedge against a “Black

Swan” event. That is why the standard deviation and beta of those portfolios with Sentry are so far below the benchmarks, indicating less risk is being taken.

WHERE DO WE GO FROM HERE?

This is the primary question on every investor’s mind. Will we, or have we, entered another bear market? Will the market just go flat from here for an extended period? Or does the bull, that began on March 9, 2009, still have legs?

In the fourth quarter Navigator Report, I mentioned that the current bull had experienced several corrections — all within 4% to 7.6%. There had not been a 10% correction since the bull market began in March of 2009. As mentioned above, no bull market since 1929 has ended before experiencing at least one correction of 10% or more. Investors who sold during the first 10% or greater correction passed up, on average, 61% further gain after the correction. In addition, there has not been a bull market that lasted less than 24 months since 1947. By these measures it seems that our current bull still has life left in him.

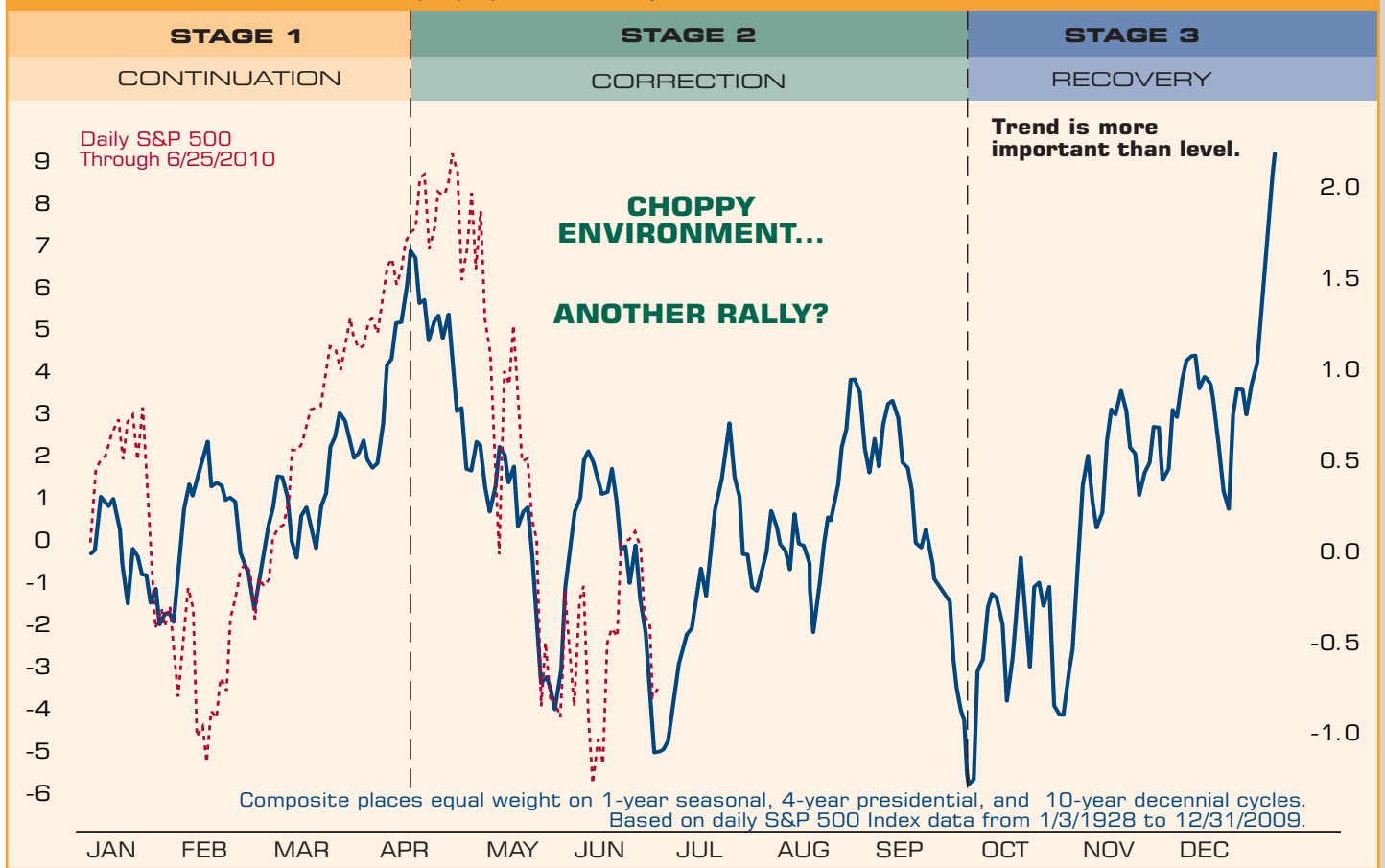
I had also mentioned that this year is a mid-term election year and showed the typical historic market pattern. I said that I expected a temporary market top in late April to early May. The top occurred on April 23rd. I also mentioned that the top would be between 1220 and 1250 and would most likely be at about 1228 which was a Fibonacci retracement of the entire decline. The top was at 1217.28. It is unbelievable how much information you can gather by just looking at what has happened in the past. Investors’ emotions don’t change very much and emotion is what drives the stock market.

The chart on the next page is prepared for us by Ned Davis Research and shows the 2010 Market Roadmap in more detail than was shown in the first quarter Navigator report. The red line is actual market action as of a few days before the quarter ended. It shows the wide swings mentioned above and also shows that the market should make a good bottom in late September before beginning the mid-term election rally. September tends to be the weakest month of the year and it would be fitting to see a market bottom after a September swoon.

MID-TERM ELECTION BIAS

The Presidential Election Cycle is probably the most

2010 Market Roadmap (prepared exclusively for K. Sean Clark)



Source: Ned Davis Research

important cycle to effect the stock markets over an extended period. And the most important part of that cycle involves mid-term elections. This also shows the effect of investor emotion and sentiment.

The market typically rallies when it senses that the party out of favor might garner enough votes to shift the center of power in Congress. As discussed before, we know that the markets wildly favor gridlock over non-gridlock when it comes to Washington. Gridlock is when neither party has a clear majority to pass legislation. Hence gridlock is linked with compromise. Every mid-term election since 1914 has sparked a rally. However, when it seems

that a party with the majority in Congress is about to lose its majority, the rally is much stronger. The table on the next page shows every mid-term election since 1914 and ensuing rallies. As shown, the average gain has been 49.3%.

The consistency is also quite amazing. Notice that only two of the rallies were in the teen or twenty percent range. All others are in the 30s, 40s, 50s and higher range. What makes these results even more interesting is that in four of the more recent elections, the rally was preceded by severe declines: 1974 -26%, 1990 -21.2%, 1998 -22.4%, and 2002 -22.5%. Four of the past nine mid-term elections saw a pretty severe pre-election decline. So it does not

IN THE NEWS



Sean Clark, CIO of Clark Capital Management Group, appeared on CNBC's "Squawk on the Street" on April 6, 2010.



Harry Clark, CEO of Clark Capital Management Group, appeared on CNBC's "Closing Bell" on May 17, 2010.

Mid-term Election Low to Highs

Mid-term Low to High	Dow Jones Point Gain*
1914-15	+89.6%
1918-19	+63.0
1922-23	+34.1
1926-27	+49.7
1930-31	+23.4
1934-35	+73.6
1938-39	+57.6
1942-43	+56.9
1946-47	+14.5
1950-51	+40.4
1954-55	+74.5
1958-59	+55.5
1962-63	+43.2
1966-67	+26.7
1970-71	+50.6
1974-75	+52.7
1978-79	+21.0
1982-83	+65.7
1986-87	+81.2
1990-91	+34.0
1994-95	+45.2
1998-99	+52.5
2002-03	+43.5
2006-07	+33.0
Average:	+49.3%

*From mid-term election year low to following year's high, using the Dow index.

Source: The Almanac Investor

seem to matter what the prior market action was, the mid-term election has always seemed to spark a significant rally.

If we use the June 30th level of 1030 as a bottom, an average mid-term election rally would place the S&P 500 at 1537 and the Dow Jones at 14,500. I admit this seems a little far fetched, but it is history. Perhaps we will get a sub par rally of only 30%. That still would place the S&P 500 at 1340 which would not be hard to take.

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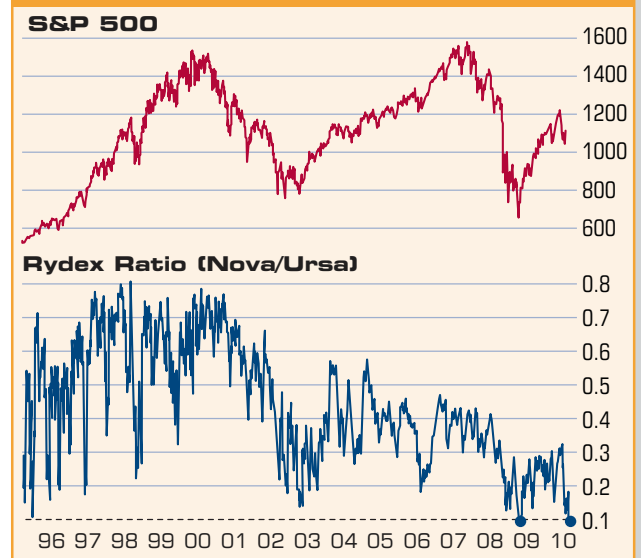
INVESTOR PESSIMISM

As I mentioned earlier, investor sentiment has reached a point of dismay that just about equals that reached at the very bottom of the bear market on March 9, 2009.

One way to show this is to look at the Rydex mutual funds which are very retail investor oriented. Rydex provides S&P 500 funds that follow the market in both directions, upward and downward. The upward fund is referred to as "long" while the downward fund is referred to as an inverse, or "short" fund.

The long fund profits when the market goes up and the inverse fund profits from a decline. There are currently 10 times more assets in the inverse fund, expecting the market to decline, than in the long fund. In fact the ratio is a bit lower than at the absolute market bottom in 2009. This is only the second time in the past 15 years when the ratio reached this level of pessimism. These levels of pessimism usually lead to quite powerful rallies which we expect to get underway in the fall if not sooner.

Rydex Traders Are as Bearish as Ever



Source: www.sentimenTrader.com, Rydex

comparable results in the future. The cited data has been prepared utilizing a methodology consistent with industry standards. 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 Clark Capital for the referenced program. Historical performance is available upon request.