



K E R N S

CAPITAL MANAGEMENT, INC.

**Kerns Capital Management
Market Report**

October 1, 2009

Clients and Friends,

Stocks logged impressive gains for September! The S&P 500 booked its second best quarterly performance in this decade.

What's causing this fantastic rally? Will it continue? Would a correction be a good thing at this point? Why would anyone want a correction?

We will answer these questions and give our best estimate of where the market will end the year.

Our client portfolios had a great September with Aggressive and Moderate and Conservative all outperforming the S&P 500 and the Dow!



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Is Less Bad, Good Enough?

It would be hard to find anyone who is not aware that the economy, the markets and most people's personal finances have been affected over the last two years. As Americans, we just want someone to "Fix It". Unfortunately, problems that have taken decades to build up do not go away in weeks or months and perhaps not ever.

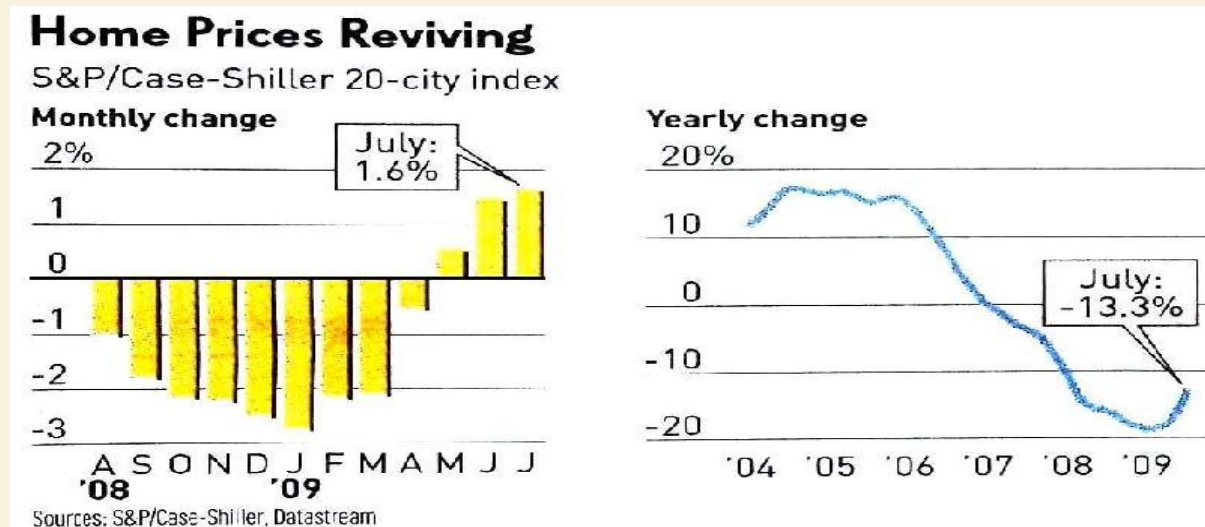
There are plenty of news reports of politicians blaming each other and conducting "Witch Hunts" to blame things on someone. At Kerns Capital we try to look past the news headlines and focus on the facts.

The facts are that we still have problems in the economy. Unemployment, for example, may not fully recover for five to ten years. There are signs, however, that things are beginning to turn ... and the

markets are noticing.

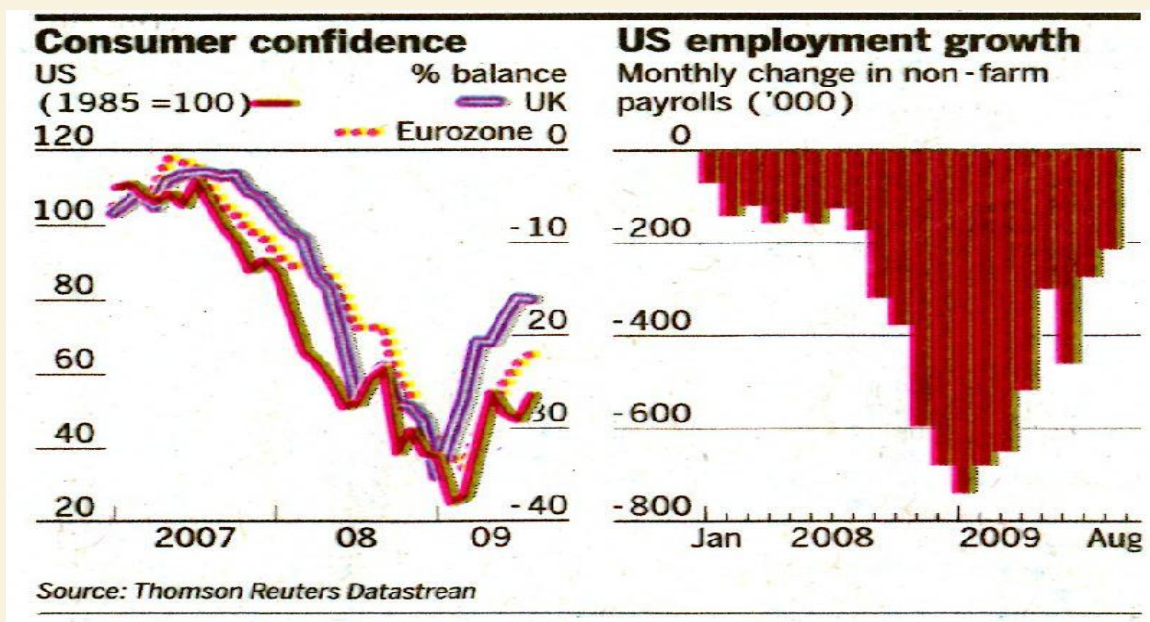
The following chart shows that home prices are down 13.3% over the last year! It would be hard to say that is good for the average homeowner. When home prices were declining, the market was also declining. But now home prices are rising, and while still down from a year ago, they are less down than they were three months ago. In fact, they rose 1.6% in July, and the market has risen with them!

Less bad has been good enough to give your portfolio a boost.



The first panel in the next chart shows Consumer Confidence in the US, the United Kingdom and the Eurozone. All show that consumers are feeling better over the last few months. There is a sense that the worst is behind us.

The second panel shows what is perhaps the most painful statistic, unemployment growth in the US. Unemployment is still growing - not a good thing! But job losses have grown smaller in all but one of the last eight months - a very good thing! Again, the fact that things are less bad correlates with improving consumer confidence which goes hand-in-hand toward improving stock markets.



The point of this is that everything is relative. Are things better or are they worse? The market is like a good old Tennessee Coon Hound. That hound can smell and track a raccoon long before we see the coon. If the economy is about to improve, the market will react to the improvement. If there is a feeling that things are getting worse, like the hound smelling a skunk, the market will go the other way. Right now we are hot on the trail of that raccoon.

A Correction Is Due

I said a correction, not a bear market. Since March 9th, the market has been in a nice uptrend with only a small 3% dip in mid August and a 3.3% dip in early September before resuming its climb. For a market up trend to stay healthy and avoid a large correction it needs regular pullbacks. Pullbacks of more than 3%.

We are now having a third dip. Notice that I am calling it a dip, not a market top. We feel that the market will be higher by the end of the year.

A dip (correction) of 6-10% would be a very healthy thing for the market right now. It would give people who have missed the rally since March an opportunity to get on the band wagon (buy) at lower prices and shake out those who think the market has gone too far - too fast. This would set the market up for a stronger rally into the new year.

We do not believe this dip will go below 990 on the S&P 500. That would be a drawdown of about 8% from its high of the year which was last week. There is fairly strong support at the 990 level. If it does go below 990, we will start hedging to protect our portfolios.

I know this sounds strange but we would like to see a high volume sell-off for another 2-5%. The reason is that high volume sell offs are a sign of capitulation - investors with low confidence throwing in the towel. A high volume sell off creates a situation like a compressed spring. As the selling pressure abates, the market will spring back. When all the selling pressure is gone, only buying pressure remains.

I have followed Price/Volume relationships for years. We check it every day and the following is from our personal investing bible:

"Price Down with Volume Up" usually indicates the following:

Panic - Urgent Selling.

Hint of a warning that a possible oversold condition is building. Often indicates an oversold condition. Near possible bottoming area.

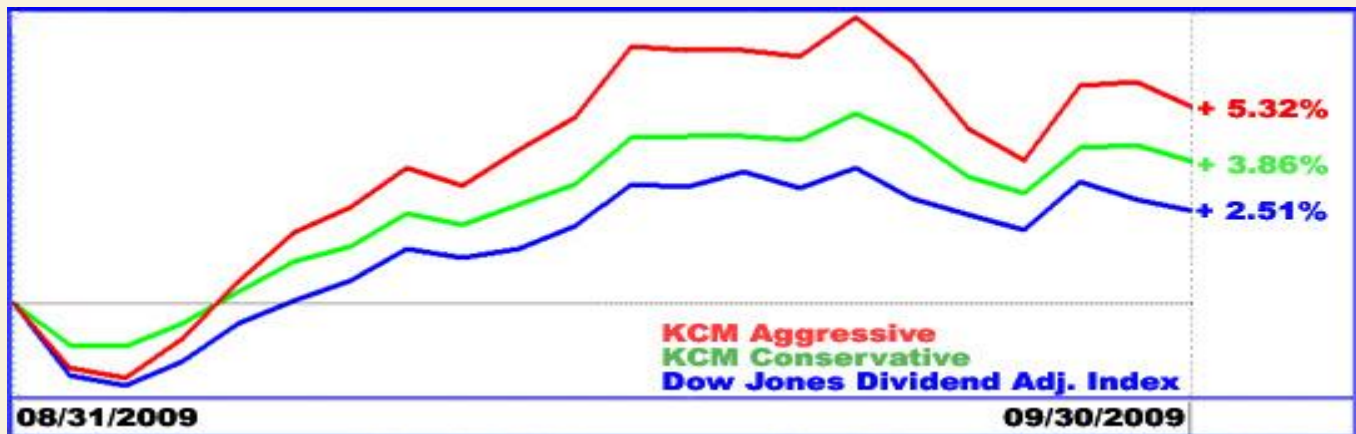
Usually Bullish. As a bottom is neared volume tends to rise until a "Selling Climax" or "Capitulation" is reached. It takes more than one day of a new PD/VU swing to be considered oversold. Over 1,000 stocks in this category suggests such a climax may be approaching.

Yesterday we had 1166 stocks, or 36% of the total stocks traded on the New York Stock Exchange, fall in higher volume. A 40% reading is convincing! I think if we get another day or two of this action it will be over and we may be set up for a great run into the end of the year. If not, we will take defensive action.

How Are We Doing?

We had a great month in September with our Aggressive model more than doubling the Dow performance.

ONE MONTH - September 2009



Note: For 401(k) plans without self-directed brokerage accounts, please see your Plan's Investment Performance Summary for actual performance.

KCM Macro Trends Fund

Our **KCM Macro Trends Fund** (KCMTX) continues to grow in assets!

For more information about the Fund, including its objectives, strategies and performance, please visit our website at www.KernsCapital.com; or click on the following direct links: [Fund Fact Sheet](#) (FINRA reviewed) or [KCM Macro Trends Fund](#).

The Fund is open exclusively to our Clients and Investment Advisors (for their clients) via Fidelity, Charles Schwab, TD Ameritrade, Pershing, Southwest Securities and Trust Company of America.

The KCM Aggressive Portfolio is invested 100% in KCMTX.

In Closing

While those who are unemployed need a job and some help, all of them and us, want to make sure we are financially secure. We want to know that we have a financial plan that will create or maintain our financial independence; conserve or build our wealth and let us sleep well at night.

We at Kerns Capital Management are not financial planners, but we feel that we provide the main building block to financial security - solid investment growth over the long-term.

I am always amazed that retail stores start the Christmas season before Thanksgiving. This year they have topped that by starting before Halloween. I would like to see the American tradition of spending and giving change a bit this year. How about giving family members a new savings or investment account?

Lane Kerns

Important Notice & Disclosures

Performance data is historical. Past performance does not guarantee future results. Current performance may be lower or higher than the performance data quoted.

Kerns Capital Management, Inc. ("KCM") performance figures represent a composite of all individual portfolios managed in accordance with the investment category, are after the deduction of KCM's actual management fee, and include reinvestment of dividends and earnings. The composites contain accounts structured with mutual funds that are managed with a view toward capital appreciation. Standard Deviation and Alpha are calculated monthly and then annualized to be consistent with Morningstar®.

Mutual Fund investing involves risk including possible loss of principal. Investors should carefully consider the investment objectives, risks, charges and expenses of the **KCM Macro Trends Fund**. The Fund may invest in small, less well-known companies, which may be subject to more erratic market movements than large-cap stocks; foreign securities, which are subject to currency fluctuations and political uncertainty; and derivative securities, which may carry market, credit, and liquidity risks. The Fund may also engage in short selling activities, which are more risky than "long" positions because the potential loss on a short sell is unlimited. These risks may result in greater share price volatility. This and other important information about the Fund is contained in the prospectus, which can be obtained by calling 1-877-275-5599. The [Prospectus](#) should be read carefully before investing. The KCM Macro Trends Fund is distributed by Northern Lights Distributors, LLC member FINRA/SIPC.

The S&P 500 Index is an unmanaged composite of 500 common stocks. This index is widely used by professional investors as a performance benchmark. You cannot invest directly in an index. **The Dow Jones Industrial Average** is a price-weighted average of 30 of the largest and most widely held stocks traded on the New York Stock Exchange and the Nasdaq.