



K E R N S

CAPITAL MANAGEMENT, INC.

**Kerns Capital Management
Market Report**

December 1, 2009

Clients and Friends,

As we highlighted in our last letter, it appears that most of the world's major economies have exited from their recessions - global growth has resumed and the stock market is anticipating earnings growth and profits.

The risks to global growth are still there, but the worst appears behind us. This letter will give more details on both earnings growth (which is what drives your stocks up) and economic recovery.

We are not going to get into any deep economic detail. Just a few more facts to build the case.



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Why Global Recovery Will Bring Rising Markets

I received a very thoughtful e-mail from an astute client of ours on Wall Street who raised concerns that I might have an overly optimistic view of the economy and the market's outlook. I always try to write the newsletter answering questions we feel our clients should be asking, so when I get a response indicating that a client thinks I may be "off the mark", it makes good subject material for a follow-up newsletter. His inquiry and my response to him follow.

Client Inquiry

"Three queries on the downside amid your strong upside view:

- (i) Beating market expectations is market spin, which works to a point, but absolute [return] is what matters in the end, yes? You address this to some extent in your Advice;

- (ii) When Bernanke reduces government bailout props, will the market react negatively, perhaps overreact?
- (iii) Will the banks eventually have to own up to big write-downs in commercial real estate investments, again spooking the market ...?"

My Response

"I agree with you about absolute returns as opposed to relative returns. We have not tried to be an absolute return fund because long-term returns are too low compared to accepting a little more risk in exchange for the opportunity to benefit from the market upside. Since the fund started last August, we are 15%+ ahead of the S&P and have an absolute return of a little over 8% during a period of some difficulty.

I like to use relative returns in the newsletter to remind people that our way is better than being a "buy & hope" investor.

I also agree with you that the transition from government support to none will be a very tenuous and fragile affair. The fact that they started slowing (actually almost stopping) the repurchase of debt in the market without a major setback has demonstrated that the Fed and the markets can probably work through it without severe damage. Volatility yes - market top - not yet.

As far as the banks are concerned, I do think there will be some damage from commercial real estate but they seem to be rebuilding their reserves fairly rapidly - time will tell. We lightened our exposure to US banks 3-4 weeks ago.

There are still a lot of negatives in the economy and the market, but on balance, I have more items listed in the positive column as far as the market is concerned." (emphasis added)

I've highlighted several items in the bullet points below that should continue to propel the market and your portfolio higher, so the balance of this section will look like an additional chapter to our last letter.

All of these came from either Bloomberg's market commentary today or the Financial Times.

Copper hits 2009 high

LME three - month price
(\$ per tonne)



Source: Thomson Reuters Datastream

Metal peaks on latest China prospects

- "Stocks rallied from Shanghai to New York and the dollar slid." ***(The falling dollar has been good for the markets - makes US goods cheaper relative to their international competitors - and especially good for our portfolio which is overweight with stocks of sectors such as commodities, which tend to do well when the dollar is falling.)***

The chart to the left shows the price of copper since the first of the year. Notice that the price has more than doubled. This can't be possible without a global recovery creating increasing demand for copper. Of course, the falling dollar is helping

force the price up.

- "Chinese manufacturing grew at the fastest pace in five years."
- "The dollar weakened against 14 of 16 most-traded currencies." (***Again - a good thing for US exports and our portfolio.***)
- "The Institute of Supply Management said US manufacturing expanded in November for a fourth consecutive month."
- "Contracts to buy previously owned US homes unexpectedly rose 3.7% in October, according to the National Association of Realtors."
- "Baoshan Iron & Steel Co. surged 7.8% in Shanghai on speculation steel demand in China will increase." (***This followed yesterday's upgrade of the steel sector by Goldman Sachs.***)
- Treasury bonds declined as money flowed back into stocks.
- "Gold rose for the 11th time in 12 sessions, jumping to a record above \$1,200 an ounce as declines in the dollar spurred investor demand for an inflation hedge."
- "A variety of leading indicators in the economy are painting a much rosier picture. The economic data indicating a recovery, combined with meaningfully improving corporate earnings, keeps us relatively optimistic about the market." (***Schwab's Chief Investment Officer's comments - not mine.***)

The point of all this is that improving global growth means rising corporate profits! With rising corporate profits and demand for goods, employment will rise. With rising employment, demand for more goods, houses and cars will be created.

The market remains in the uptrend that started in March. We remain bullish.

How Are We Doing?

We had a great November!

Conservative, Moderate and Aggressive are up 2.88% to 4.96%, respectively, for the month. Today, the first day of December, Aggressive closed up 1.64%. A good start for the last month of the year.

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

KCM Macro Trends Fund

The **KCM Macro Trend Fund (KCMTX)** is an out-growth of the model portfolios we have been successfully managing for our clients for more than 15 years. It is a proprietary fund open only to our clients and Investment Advisors (for their clients) via Fidelity, Charles Schwab, TD Ameritrade, Pershing, Southwest Securities and Trust Company of America.

For more information about the Fund, including its objectives, strategies and performance, please give us a call at (800) 945-2125, or click on the following direct links: [KCM Macro Trends Fund](#) or [2009 3Q Fund Fact Sheet](#) (FINRA reviewed).

In Closing

Billie and I had a wonderful anniversary trip on Waikiki Beach at the Royal Hawaiian Hotel in Honolulu. Our balcony overlooked the beach and we were not only able to watch the sunsets but also the moonsets! It was very relaxing and our first real vacation in several years. It is nice to have Marty and staff back at the office keeping things going as well without us (perhaps better) than if we were there.

The month has started well from a performance standpoint. I still feel that December will be an up month. This would be icing on the cake as we have had a great year so far.

As we visited the Pearl Harbor Memorial I was reminded that while there are many pressures in the world, we are fortunate to live in a country where we can enjoy the holiday season in relative safety. Please remember those - both past and present who have made it possible for us to enjoy this luxury.

Lane Kerns

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