

The Messenger

Cutting Through the Fog of Today's Investment World

Bank Failures and the FDIC... Then and Now

By Matthew A. DiFilippo, Senior Portfolio Manager and Director of Research

Bank failures from the current crisis have yet to surpass those related to the savings and loan crisis of the late 80s/early 90s.

According to FDIC.gov, there were over 1,800 bank failures during the S&L crisis, covering \$700 billion in assets; adjusted for inflation the value approaches \$1.2 trillion. Since the beginning of 2008, 126 banks have failed with total assets of \$500 billion; reflecting the larger size of banks. At the end of the S&L crisis, the

FDIC borrowed \$15 billion from the Treasury and repaid it with interest. Because there is little appetite for a taxpayer funded loan in the current environment, the FDIC is exploring all alternatives.

From the end of first quarter 2009 to the end of the second quarter 2009, the FDIC troubled bank list increased by 111 to 416. The insurance fund balance was \$10.4 billion, the lowest since 1993 (it was negative at the end of the third quarter). Liquid assets include \$21.6 billion in cash (which will run out by

early 2010) and \$43.2 billion in seized bank assets. Their liabilities include \$22.4 billion in liabilities from failures, which already occurred (these could be paid out over as much as 10 years; more on that later) and \$32 billion in liabilities for failures they expect in the next 12 months. Subtracting liabilities from assets yields the reserve balance of \$10.4 billion.

The FDIC is using three new techniques to raise funds and has proposed a fourth. It is collecting fees to insure bank debt, using loss-share agreements and improving the terms to entice private equity investors to purchase troubled banks.

Insuring newly issued bank debt allows troubled banks to access the capital market at unnaturally low rates.

This is a win-win for the FDIC; it collects more fees (\$7 billion so far) and also prevents, if not delays, bank failures. The result is higher fees and lower overall losses.

Another new method is loss-share agreements, which were used briefly in the S&L crisis. The FDIC

offers these agreements to entice prospective bank buyers. The buyer places the failed bank's assets onto its balance sheet, but only takes a small portion of future losses. Basically, buyers have a call option on the troubled bank's assets. Some of these assets have been marked down well below the value they will

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Economic Commentary

By Helena Rados Derr, Portfolio Manager

US Economy Needs the Extension of Government Programs

During the latter part of 2008, financial markets experienced a liquidity freeze, which resulted in lending institutions losing funding sources. Our government decided to try to increase credit availability by creating different temporary programs. These programs including, the Term Auction Facility (TAF), Term Securities Lending Facility (TSLF) and Term Asset-Backed Securities Loan Facility (TALF), aided in creating liquidity for different parts of our economy. The goal of the Fed was to discontinue using these programs as our economy regained its strength. The extension of these programs beyond 2009 indicates that our economy is not yet able to operate independently.

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Items of interest and
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and encouraged, as are
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Outspoken Investor



**Outspoken Investor,
Malcolm Polley, rants about
the unhappy investor,
regardless of the outcome.**

Investing Psychology

spillover from the
decimation of last
year's financial
markets that is
causing people
to ignore the good
that may be currently
happening within their
portfolio.

On a similar note, there are
those that are always looking
for something better. Some
simply will not be happy
that the Composite is up
more than 30% year-to-
date. Rather, they point to
an investment in a friend's
portfolio that is up 100%
and ask, "Why can't you get
returns like that?"

As I have said in the past, fear
and greed usually dominate
investing and the markets.
Our job as investors and
analysts is to try to block
out the emotional responses
to situations and look at

things in their entirety and
within the proper context
or framework. For example:
If your friend's investments
are up 30% and yours are up
only 10%, you should ask if
they are invested differently.
We believe that, in the
investing world there is only
one truth: The way to get a
higher (long-term) return is
to accept a higher degree of
risk. If your friend's portfolio
is getting a higher rate of
return than you are, chances
are very good that they are
invested more aggressively.
(Or you are looking at a very
short time period, where
differences in returns can
be significant.)

One difficulty of managing
investments is that it is hard
for many people to accept
investments that do not
turn out as expected.

As I have told the other
portfolio managers at
Stewart Capital, "Not to
sound flip, but get over
it." If you make enough
investment decisions,
some of the investments
you make will go bad.
Some of the stocks you
buy will drop like a stone.
Even the best investors
(Warren Buffett, Bill Miller,
Bill Gross, etc.) make bad
investment decisions.
Mistakes are sometimes
inevitable, even for good
investors. Our hope is
that if we do the work,
the good decisions will
outweigh the bad. ■

"The Stewart Capital Mid Cap Composite invests exclusively in mid-cap securities as defined by their market capitalization according to the S&P MidCap 400 Index. The Composite returned 34.31% for the year-to-date period ended September 30, 2009 as compared to the S&P MidCap 400 Index, which returned 30.14% for the same period. This Index is unmanaged and represents a more diversified list of securities than that reflected in the Composite. In addition, the Composite may invest in securities outside of those represented in the S&P MidCap 400 Index. Results are based on fully discretionary accounts under management and returns are calculated in US dollars. Past performance is not indicative of future results. These returns have not been verified by an independent third party and reflect the deduction of the highest fee charged for the specific investment strategy during the period. Fees may vary among clients with the same investment strategy. Results include the reinvestment of dividends and other earnings. Additional information regarding the S&P MidCap 400 Index, the firm's composites, and policies for calculating and reporting returns is available upon request by contacting Stewart Capital Advisors, LLC at 800.446.0246.

The Stewart Capital Mid Cap Composite represents separately managed accounts and is distinct from the Stewart Capital Mid Cap Fund.

Company Report:

Akamai Technologies, Inc. (NASDAQ: AKAM)

By Malcolm E. Polley, CFA, President & Chief Investment Officer

Akamai Technologies, Inc. provides global delivery services for Internet content, streaming media, and applications and global Internet traffic management. The company uses technology and software based on mathematical formulas and algorithms to monitor Internet traffic patterns.

Akamai is Hawaiian for intelligent or cool. The same could be said of the company as it allows web surfing to happen intelligently, and the process behind what they do is definitely cool. One can think of Akamai as a massively distributed computer platform that overlays the Internet. According to the company's website as of October, it has more than 48,000 secure servers across more than 1,000 networks in 70 countries.

Its servers operate in real time to monitor the Internet, gathering information about traffic, congestion and trouble spots, and using the information gathered to optimize routes and replicate data dynamically to deliver content and applications more quickly, reliably and securely. Akamai aims to accomplish its goals by:

- Eliminating long routes when possible. It does this by replicating (caching) and delivering content and applications from servers close to end users around the world instead of from centralized servers. The company refers to this as delivering from the "edge of the Internet."
- Optimizing routes by mapping paths across the Internet to avoid trouble spots, compressing content and replicating packets to ensure fast, complete delivery.

Because Akamai's servers reside at the edge of the Internet, content moving over its servers

moves much more readily and helps increase content usage.

Earnings visibility. One can think of Akamai's revenue stream much as one would look at a cell phone bill. The customer contracts for a specific amount of usage for which the customer pays a specific fee. If the customer stays within the usage band, their billing is equal to the contract amount, and any overages (or added services/products) are charged extra. The result is that approximately 70% of the company's revenue is known in any one quarter.

Issues. Akamai's earnings are not fully taxed, currently. Thanks

to significant net operating loss (NOL) carry forwards, the company's earnings have been sheltered since the dot com bust. The company has stated that it expects that those NOLs will expire in 2010, with the result that earnings will be, at least, partially taxed in 2010, and fully taxed in 2011. That will cause a bit of an earnings headwind for that one year. However, because more of its business mix is shifting to value added services (which should continue to allow margins to expand) these headwinds may be (somewhat) muted.

The company's content delivery network (CDN) business is facing increasing competition

and is becoming commoditized. This increased competition has resulted in their churn rate among CDN customers increasing to slightly above 5%. In their defense, part of this increased churn was the result of the bankruptcies of some of their smaller companies.

Conclusion. We believe that Akamai is an attractive way to invest in continued growth of the Internet, and feel the current stock price more than discounts future opportunities. ■

As of June 30, 2009, the Stewart Capital Mid Cap Fund did not hold a position in Akamai Technologies, Inc. Portfolio holdings will change due to ongoing management of the Fund. References to specific securities should not be construed as recommendations by the Fund, the Advisor or the Distributor.

Selected Rates & Indices

As of 9/30/09



EQUITY MARKETS

	Value	YTD Return
DJIA	9712.28	13.49%
S&P 500	1057.08	19.26%
NASDAQ Composite	2146.30	25.59%
Russell 2000	604.28	22.43%
Nikkei 225	10133.23	16.11%
Hang Seng	20955.25	49.66%
FTSE 100	5133.90	20.40%
DAX	5675.16	17.98%

CURRENCIES

	Per US \$
Japanese Yen	89.77
Australian Dollar	1.133
Swiss Franc	1.036
Canadian Dollar	1.070
British Pound	0.626
EURO	0.683



US Economy Needs the Extension of Government Programs

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TAF is used to auction collateralized (Treasury, agencies, mortgage backed securities, etc.) short-term funds (from 28 to 70 days) to depository institutions (eligible domestic and foreign banks). In other words, this is a credit facility, which enables depository institutions to apply for an advance from the local Fed in order to provide inter-bank liquidity. The Fed initially offered \$150 billion per auction, lowered it to \$75 billion, and will be further reducing it to \$50 billion in October

and \$25 billion in November and December. The goal is to make depository institutions independent by January 2010.

TSLF is a 28 day short-term lending facility extended to Federal Reserve investment banks. This facility offers Treasury general collateral (GC) to the investment banks and it is intended to provide liquidity in the financial markets for Treasury and other collateral. The banks have the option to enter cash-for-bonds agreements or security-for-security

agreements. As is the case with TAF, TSLF also lowered availability from \$150 billion until January 2010, when this program is scheduled to end.

TALF allows any US company (including US branch or agency of a foreign bank, investment fund, etc.) and US citizen owning eligible collateral (US dollar-denominated) to borrow funds from the Fed for three to five years. This program was intended to help thaw the asset backed securities market

(auto, mortgage, student loan, etc.). According to Fed Chairman, Ben Bernanke, this program has indirectly financed nearly three million loans to households and 400,000 loans to small businesses. It is scheduled to end on June 30, 2010.

The above-mentioned programs were established at the height of our economic crisis in order to inject liquidity into different sectors of our economy. Originally, these programs would have expired at the end of 2009. However, the Federal Reserve decided to continue with the programs until 2010. The main reason behind continuation is that the Fed believes our economy is not ready to stand on its own. Regardless of how relatively good the current economic news has been, solid economic growth is not expected to materialize until well into 2010. ■

TREASURY YIELD CURVE COMPARISON



YIELD CURVE

Current
(as of 9/30/09)

Previous
(as of 7/31/09)

Current
(as of 9/30/09)

Previous
(as of 7/31/09)

Fed Funds
3 Month
6 Month
2 Year
5 Year
10 Year
30 Year

0.25%
0.11%
0.17%
0.95%
2.31%
3.31%
4.05%

0.25%
0.17%
0.26%
1.17%
2.66%
3.63%
4.41%

Source: Bloomberg Professional



You should consider the Stewart Capital Mid Cap Fund's investment objectives, risks, charges and expenses carefully before investing. For a prospectus, that contains this and other information about the Fund, call 877.420.4440 or visit stewartcap.com. Please read the prospectus carefully before investing.

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NO BANK GUARANTEE
MAY LOSE VALUE

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What's Hot: Year-end Tax Considerations

By Jonathan Pavlik, Portfolio Manager

As we move toward year end, it is not too early to begin thinking about your taxes as they relate to your investments. There is a fine

line between trying to manage your taxes and letting tax consequences dictate your investment decisions. We believe that

investment decisions should be based on the price value relationship for each security and that tax consequences are a secondary concern.

However, when there are opportunities to manage taxes within the confines of your ultimate investment goals then take advantage.

term capital gains tax is 15%. This rate was reduced in 2003 and extended in 2008, but it is due to revert back to a higher rate in 2011. However, there is not any guarantee that the lower rate will even last that long. In the budget released this year, there are calls for the capital gains tax to be increased before 2011. Considering the large increase in government spending this year, higher tax rates are not a matter of if but when, so why take the chance and wait until next year to realize long-term gains.

Once again, it may not be wise to let taxes drive investment decisions, but the current 15% long-term capital gains tax shouldn't be viewed as prohibitive and time is running out. Don't let the fear of paying Uncle Sam some taxes on your long-term gains prevent you from taking advantage of a low rate that will soon expire. Remember, if you are particularly fond of the security you are selling, you can always buy it back after 30 days to comply with the IRS's wash sale rule. ■

For many individuals, 2009 investment related taxes will not be a concern after last year's losses. For instance, most mutual funds realized enough losses in 2008 to last them well into the future. Fund managers were forced to sell holdings at a loss when investors started pulling their money out of mutual funds during the market decline. As a consequence, investors in mutual fund models may not feel the need to do much but stay with the status quo. However, even though an investor may not have investment gains to offset, if there is a security that they want to exit at a loss, up to \$3,000 of those losses can be used to reduce taxes on income and interest earned each year.

On the flip side, individuals who have long-term positions with large embedded gains could think about trimming if not outright selling these securities. The current long-

HAVE YOU SEEN US LATELY?



Stewart Capital Advisors has become a sought-after source for financial commentary, and are regularly featured in national news.

Malcolm Polley – on Bloomberg News (9/16/09) – “Clearly, the latest reports show that the economy is not getting worse. That gets investors waiting for an inflection point where the improvement in corporate earnings is going to come less from cost cuts and more from top-line growth.”

Malcolm Polley – on Bloomberg News (9/23/09) – “There’s concern we’ve moved too far, too fast without any meaningful correction. I do think any correction will be muted because the latest figures point to modest economic recovery. But we still need to see top-line corporate growth.”

Matthew DiFilippo – on Bloomberg News (10/1/09) – “With the substantial run-up we’ve seen since March, it is more difficult to find companies that are substantially undervalued. But we still do find values out there, particularly in industrial, materials and health care companies.”

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ultimately realize; the buyer realizes the upside with limited downside. It's clear this is a good deal for acquirers, but how does this benefit the FDIC? The acquiring bank assumes the failed bank assets, preserving the FDIC's limited liquidity and spreading short falls to the future, when they are likely to be smaller.

The FDIC is enticing private equity investors to buy

distressed bank assets.

It has set tier one capital requirements at 10%. Most banks have their own problems, making acquisitions difficult. Now, another group of investors can bid on troubled banks and improve the position of the FDIC's insurance fund.

The insurance fund still needs more capital. A recent proposal for banks to prepay FDIC premiums from 2010 through 2012 by year-end

has promise. This would raise \$54 billion and take care of liquidity issues. The banking industry likes this proposal because bank earnings are not impacted by the prepayment. They pay cash out to the FDIC and record this payment as a prepaid asset on the balance sheet. At the time the payment would normally be due; banks will lower the prepaid asset and expense the same amount. Has the FDIC averted the need to tap their line of

credit at Treasury? This proposal is politically popular as it avoids the dirty term, taxpayer bailout. Still, many banks will probably borrow from the Federal Reserve or the Federal Home Loan Banks, which are backed by the Treasury. Whatever happens, it is most important to remember that insured deposits are safe regardless of how the insurance fund is replenished. ■