



My Top-10 List for 2010

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12/28/2009 4:07 PM EST

URL: <http://www.thestreet.com/p/rmoney/investing/10653220.html>

Get ready for year two of a once-in-a-lifetime bull market. On the heels of the nastiest bear market in 80 years, why shouldn't the bull cycle that follows be just as extraordinary? And it is: Never before has it been so easy to outperform the indices, and not just by a few percent but by leaps and bounds.

To capture the gain to be had, all you have to do is recognize this single, salient fact: The price damage incurred during the mega-bear market was brutally uneven -- some stocks got nicked while others were crushed.

Like a rubber band that gets stretched, as prices recover -- as they "snap back" -- you'll get the biggest snap from stocks whose prices were pulled down the most. That's why I filled my Top 10 list for 2009 with stocks that were unfairly smashed during the bear market: On average, 2009's list was composed of stocks that were down 75% from pre-bear market levels. The resulting outperformance has been dramatic. The Top 10 list for 2009 is up by 104% since it was posted on this site one year ago, vs. an **S&P 500** return of 28%.

Here's what is really interesting -- and potentially very profitable for investors: Even though the market rallied nicely in 2009, scores of stocks have yet to stage a meaningful recovery from the carnage suffered during the last cycle. In compiling my Top 10 list for 2010, it was easy to find 10 amazing bargains among crushed stocks. As you can see below, the stocks on 2010's list are down 71%, on average, from pre-bear-market levels.

| <u>Name</u> | <u>Initial Price</u> | <u>2007 High</u> | <u>% off of high</u> |
|------------------|----------------------|------------------|----------------------|
| Metro Bank | \$10.59 | \$33.11 | -68.0% |
| Liz Claiborne | \$4.64 | \$46.80 | -90.0% |
| SmartBalance | \$5.60 | \$13.50 | -59.0% |
| Huntsman | \$10.75 | \$28.40 | -62.0% |
| Leucadia | \$22.67 | \$52.67 | -57.0% |
| NCR | \$10.40 | \$31.42 | -67.0% |
| MEMC Electronics | \$12.88 | \$96.10 | -87.0% |
| Manitowoc | \$10.18 | \$51.50 | -80.0% |
| Humboldt Wedag | \$13.72 | \$45.74 | -70.0% |
| Legg Mason | \$29.30 | \$110.20 | -73.0% |
| AVERAGE | | | -71% |

While each stock on 2010's Top 10 list is a smashed stock with the potential to provide outsized returns as prices recover, it's far from a homogeneous group. Depending on your financial situation and risk temperament, certain names will meet your needs better than others. With that in mind, I'll parse the list for different types of investors.

Conservative investors: If you're an investor whose priority is minimizing risk, I'd recommend **KHD Humboldt Wedag** (KHD) , **NCR** (NCR) and **Legg Mason** (LM) from the list above. There is no such thing as certainty when investing in stocks, so let's just say that the odds that you'll permanently lose capital buying Humboldt Wedag, NCR and Legg Mason are very low -- but not zero.

Note also that risk assessment goes well beyond the obvious, such as a detailed review of the balance sheet. Humboldt Wedag, NCR and Legg Mason are labeled as being appropriate for conservative investors on the

basis of other factors such as the durability of the franchise, their ability to generate free cash flow in trough conditions and, of course, the spread between stock price and intrinsic value.

Aggressive investors: The stocks with the most pop potential are **MEMC Electronic Materials** (WFR) and **Liz Claiborne** (LIZ) . It should come as no surprise that their "price rubber bands" have been stretched the most -- they're down by 87% and 90%, respectively, from their 2007 highs. Needless to say, a stock that's trading at 10 or 11 cents on the dollar compared with 2007 levels doesn't need to snap back much to provide investors with a hefty rate of return, or even a multi-bagger.

Investors seeking inflation protection: **Leucadia National** (LUK) is probably the best hedge from the list of stocks above. It's heavily invested in a wide array of inflation-sensitive assets, including mining and metals and other commodities.

Buy-and-hold investors: After a decade of poor returns from the stock market, buy-and-hold investing is no longer popular. A sluggish economy makes it even less appealing. That's because the ideal buy-and-hold stock is a company that generates organic growth, something that's a rarity nowadays. On the list above are two such rarities: **Smart Balance** (SMBL) and **Metro Bancorp** (METR) . Each has the ability to generate organic growth of 15% or more for the next several years. Combine that with the fact that their stocks are quite undervalued, and you have all of the makings of a superb long-term investment.

Do-it-yourself investors: For investors who enjoy doing their own research, it's a trying time. Messy, convoluted financials are an inevitable consequence of an economy goes from peak to trough in only a few quarters. Of the companies on the Top 10 list, Legg Mason and NCR are the easiest to research and understand. As with most companies, the falloff in the economy caused a revenue/expense mismatch at Legg Mason and NCR. Adjusting their data is a relatively straightforward process; do it and you'll see what I see - stocks with 50%-100% upside potential over the next year or two.

A Final Note on 2009's List

Before I permanently close the books on the 2009's Top 10 list, a final comment. None of the outperformers was seriously considered for inclusion -- eight of the 10 were up by 50% or more, and five by at least 120%. Price is everything, after all. Of the two underperformers, **Brinks** (BCO) , which was down 2%, and **Mueller Water** (MWA) , down 23%, both were logical candidates for inclusion. They're excellent buys, and I'll probably regret not including them when we look back in a year's time. In any event, I can blame their exclusion on the once-in-a-lifetime bull market: an amazing abundance of bargains and just 10 slots to fill.

At time of publication, Alsin and/or ACM was long MWA, BCO, METR, LIZ, SMBL, HUN, LUK, NCR, WFR, MTW, KHD and LM, although holdings can change at any time.

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