Weekly Market Commentary

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Third Quarter Earnings Preview

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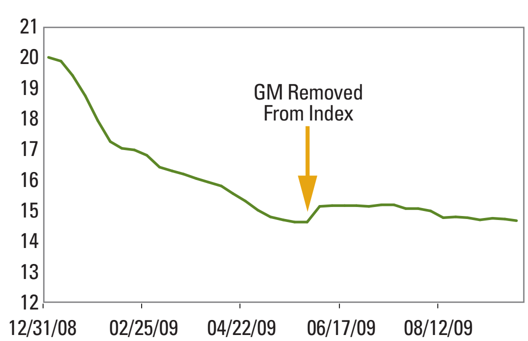
Highlights

We will be tracking four trends during the earnings season:

- The pace of revenue growth from the prior quarter. The rebound in GDP in the third quarter is likely to have helped drive results.
- How the third quarter results for the companies in the S&P 500 Index compare to expectations—we hope to see most companies exceed expectations by a similar margin to the second quarter.
- How the expectations for the fourth quarter change—we hope to see the median expectation for all companies rise.
- How the range between high and low estimates for 2010 change—we hope to see them narrow, reflecting improving confidence as uncertainty surrounding the economic outlook fades.

1 Earnings Expectations Have Not Tracked Rebounding Economic Data
Third Quarter 2008 Analyst Consensus Earnings per Share Estimate

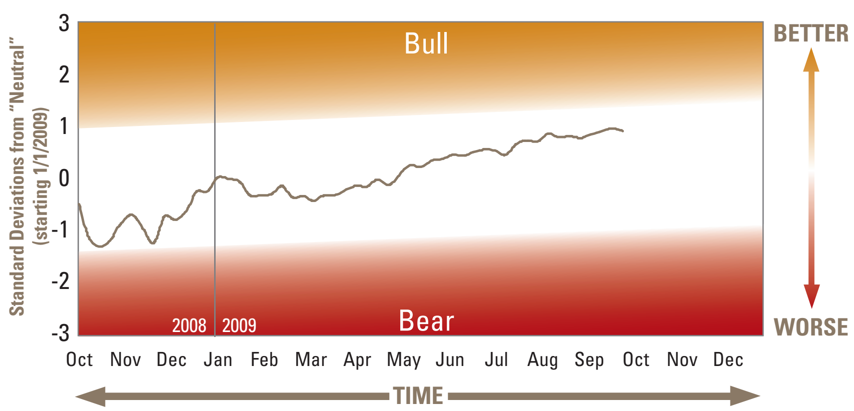


Source: LPL Financial, FactSet

Four times a year investors focus on the most fundamental driver of investment performance: earnings. The third quarter earnings season gets underway this week. However, the companies that report early in the season are most often not the bellwethers they are commonly thought to be. We will not really know how results are shaping up until the end of the month, when about half of the companies will have reported.

The analyst consensus estimates for the earnings of S&P 500 companies in the third quarter fell sharply in the first five months of the year. Then, they stayed relatively flat despite a steady improvement in leading indicators of profit growth that we have highlighted in prior weekly commentaries, such as the ISM index and even our own Current Conditions Index.

LPL Research Current Conditions Index



Source: LPL Financial

During the past two quarters, the stock market moved sideways in the two weeks prior to the start of the earnings season and then rallied as the reports came in. During the first quarter we did not expect good earnings guidance, but instead noted that in that environment a boost to the dividend payment might signal more confidence in a recovery by business leaders than any guidance they were likely to give on the earnings outlook. During the first quarter and first quarter earnings season, we were pleased to see more companies increase their dividend, outnumbering or at least matching those that had decreased their dividend in every sector but Financials, where most of the cuts were concentrated. In the second quarter, we expected

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better than expected results given the turnaround in economic data and the credit markets. Companies followed through, with the second quarter setting the record for the percent of companies exceeding analyst estimates. We expect stocks may rally as third quarter results are reported. Again this quarter, stocks have been relatively flat during the past couple of weeks leading up to the earnings reporting season.

Specifically, we will be tracking four trends during the earnings season:

- The pace of revenue growth from the second quarter. Last quarter, GDP was negative with little revenue growth to go around and the earnings results were boosted in large part by cost cutting. But in the third quarter GDP is likely to have been positive, and we expect to see better top-line growth helping to drive results.
- How the third quarter results for the companies in the S&P 500 Index compare to expectations—we hope to see most companies exceed expectations by a similar margin to the second quarter, when over 72% of companies exceeded the average consensus estimate. The estimate for second quarter earnings as the quarter ended was $13.67; however, the actual earnings came in at a much higher $16.07.
- How the expectations for the fourth quarter change—we hope to see the median expectation for all companies rise. Currently, the consensus estimate for fourth quarter earnings is $16.27.
- How the range between high and low estimates for 2010 changes—we hope to see it narrow, reflecting improving confidence as uncertainty surrounding the economic outlook fades.

While the consensus expectation is for about $75 in earnings per share for S&P 500 companies in 2010, the range of the best and worst cases—as seen by Wall Street analysts—for the profits of the companies in the S&P 500 is also worth watching. To collect this data, we have taken the highest and lowest analyst estimate for each company to derive the bull and bear earnings outlook for the S&P 500 in 2010.

- The bull case, using the highest estimate for each company, forecasts $89.76.
- The bear case, using the lowest estimate for each company, forecasts $56.57.

Market participants will be reacting to how these numbers change over the course of the earnings season.

We expect guidance from business leaders to confirm or boost analysts' expectations. Investor confidence is likely to increase in the current analyst consensus estimate of $75 for S&P 500 companies in 2010, which should support the forward price-to-earnings ratio of about 15 (the long-term average). A forward price-to-earnings ratio of 15 on $75 in expected earnings would result in the S&P 500 ending the year at about 1125, leaving room for additional upside for stocks in the coming months.

IMPORTANT DISCLOSURES

The opinions voiced in this material are for general information only and are not intended to provide specific advice or recommendations for any individual. To determine which investment(s) may be appropriate for you, consult your financial advisor prior to investing. All performance reference is historical and is no guarantee of future results. All indices are unmanaged and cannot be invested into directly.

Investing in international and emerging markets may entail additional risks such as currency fluctuation and political instability. Investing in small-cap stocks includes specific risks such as greater volatility and potentially less liquidity.

Stock investing involves risk including loss of principal Past performance is not a guarantee of future results.

Small-cap stocks may be subject to higher degree of risk than more established companies' securities. The illiquidity of the small-cap market may adversely affect the value of these investments.

Bonds are subject to market and interest rate risk if sold prior to maturity. Bond values will decline as interest rate rise and are subject to availability and change in price.

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