LPL Financial

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Dear Valued Investor:

With a big down day on Thursday, the stock market has returned to the 2008 market lows hit in mid-March. It is important to maintain perspective in troubled times. The market is down lately, we have a large problem with energy prices, but there are plenty of really solid fundamentals. I do not think that now is the time to exit the market.

Catalysts for the decline are a continued march higher in oil prices, more bad news from the big banks, a view that the Federal Reserve is not doing the right thing (I think they are doing fine), some downward pressure on the dollar exchange rate, election outcome concerns and what I view as overreactions to minor earnings misses on otherwise substantial earnings gains by some technology companies.

Oil prices have been unmoored from the real market by financial investors and by geopolitical concerns. And in my judgment, because it takes time for consumers and producers to adjust, prices could remain out of line with fundamentals for quite some time. The move up to $142 a barrel has been very fast – crude oil was selling for $96 a barrel at the end of 2007 and $61 at the end of 2006. I still hope and expect that the move down in prices will come before tipping us into recession.

It's not all bad news. Today we got the report on personal income and spending for May. Bolstered by the Treasury rebate checks, after-tax personal income rose 5.3% in real terms - the second largest one month increase on record. And real consumer spending continued to chug along, rising 0.4%. Consumer spending is not shooting up like income, because we all know it is a one-time gain. But it is still "money in the bank".

And, despite the surge in food and energy prices, consumer inflation remained relatively stable, with total consumer prices rising 3.2%. Also it looks like housing is bottoming, with small upturns in existing home sales and prices in May. Next Thursday we get the employment report for June. I do not expect a rise in employment, rather I expect another small decline consistent with a sluggish economy.

It is unlikely we are headed for another big bear market; rather, the market will likely remain range bound and volatile. This is not 1999! While the S&P 500 stock price index is still about 10% below the 2000 high, S&P 500 operating earnings are about 60% higher. And, while problems remain in the housing sector and banking, LPL Financial

other parts of the economy are doing pretty well. It looks as though real GDP will grow about 2% in the second quarter, not fall as many were saying. No question continued big increases in oil prices could cause a further decline in equity markets, however a fall in oil prices could cause a move higher in stock prices. So I remain “on the cheese grater”.

It is tempting in such times to reduce market exposure. But given that the negative factors, like oil, appear stretched, the positives are still in place, and it is possible that the Federal Reserve and the Treasury could further shift policy to stabilize banking and the dollar, I think now is not the time to exit the market. As always, please call your financial advisor with any questions or concerns.

Sincerely,

Lincoln Anderson
Managing Director, Chief Investment Officer