

September 5, 2008

Dear Valued Investor:

Along with the end of this summer, the markets also are poised to enter a new season. The three months ended August 31 were pretty tough for financial markets, driven by continuing effects from the meltdown in the Financial sector, high energy prices and fears of recession. So far in September it has been more of the same, with the stock market down and economic indicators mixed—employment down, consumers cutting back, but factory orders and shipments strong.

Stocks were down over the summer, with the S&P 500 losing 7.9% over the last three months. Top U.S. equity performers over the last few years—the Energy and Materials sectors—got clobbered as crude oil and other commodity prices fell sharply, while some of the poor performers over the last few years like Healthcare, Consumer Staples and Consumer Discretionary, did better than the overall market. International equities underperformed U.S. equities as the dollar exchange rate rallied. The Financial sector got pounded again as the write-downs of bad loans continued, but I think we are nearing the end of the financial meltdown. Home prices are showing some signs of stabilization, but the outlook remains uncertain. And a certain end to home price declines is necessary for the banking system to finally stabilize.

Some other parts of the economy are doing better. U.S. net exports are booming as the rising, but still very low, dollar exchange rate makes U.S. exports extremely competitive in global markets. And business capital spending on plant and equipment is picking up again. I think we are in for slow growth, or at worst a mild recession, over the remainder of the year. If energy prices continue to fall, I think we can avoid recession and return to more robust growth in 2009. If the fall in the dollar exchange rate really is over, then foreign demand for U.S. financial assets may accelerate. This would help put a floor on U.S. stock prices.

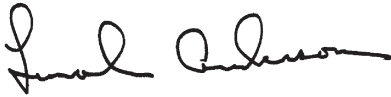
The fall in energy and commodity prices should do wonders for inflation over the coming months. I believe we will see a very sharp drop in CPI inflation if the energy price declines stick. Lower inflation would likely mean the Federal Reserve could stand pat and keep interest rates low well into next year. I think the dire predictions of deep recession and rising inflation are off the beam.

That said, we have gone through a lot this summer and a lot more over the last three years. Bad hurricanes, a housing crash, a banking sector crisis, a huge rise in energy and other commodity prices, a major decline in the dollar exchange rate and the negative effects from dire predictions of all sorts. I come away from this period even more impressed by the resilience of American workers and companies and by our economic system's ability to handle these adversities and keep on ticking. While a shallow recession is possible over the

second half of this year, I continue to believe that by working our way through these adversities, we are setting the stage for better financial market performance later this year and into next. Remember that while the stock market has stalled and fallen back below the 2000 peak, U.S. corporate profits are more than double what they were at the previous peak. Outside of banking, the aggregate non-financial corporate balance sheet is very strong and the ratio of the market value to the net worth of non-financial corporations is well below one (about 0.7), indicating to me very low valuation risk.

Finally, with the end of summer we are now into the thick of the Presidential and Congressional election campaigns. Brace yourself for one heck of a lot of political ads and media coverage for the next two months! The good news is that with only one exception (Q4, 2000), since WWII the S&P 500 has always had a positive return in the fourth quarter of Presidential election years! As always, please call your financial advisor with any questions or concerns.

Sincerely,



Lincoln Anderson  
Managing Director, Chief Investment Officer

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