

September 15, 2008

Dear Valued Investor:

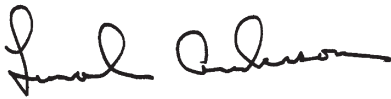
The events of this last weekend represent a major step towards resolution of the financial market crisis. Another big investment bank, Lehman Brothers, failed. Also, Merrill Lynch agreed to be acquired by Bank of America. This comes on the heels of the failures of Fannie Mae and Freddie Mac. And it is by no means clear that the bad news and instability of financial institutions is over. In my view the problems are not due to widespread instability in the credit market. Broad bond market indices are mostly in positive territory. The problems are twofold: 1) high leverage at these financial institutions that have failed and 2) heavy exposure to subsections of the credit market are not doing well (subprime mortgage backed securities and the like). So I think these problems are not due to broad securities markets difficulties but rather, due to very high leverage investments in risky debt at some very prominent financial institutions that should have known better.

What does this mean for financial markets and the economy going forward? Well, in the short run it creates problems. Banks are scrambling to de-lever and that means tighter lending standards and lower loan growth. Bank lending has slowed to a 6.3% growth rate over the last 52 weeks from peak growth of about 12%. But this is not the complete halt in loans that some claim is underway. Tighter credit market conditions will likely add to various other conditions slowing the economy down. On the other hand, stopping this crazy risk taking and allowing the market to discipline the offenders will likely help the economy regain a solid foundation for future growth. While we do need housing investment, I think we were wasting resources on speculative housing and second homes based on ridiculously easy mortgage lending standards. Diverting those resources to other more productive activities is a painful process but, in my opinion, both necessary and a good thing longer term. We need more energy, technology, education, infrastructure as well as traditional plant and equipment investment to stay competitive in the global economy.

How are we being affected by all this toil and trouble in financial markets? Well, first and foremost, it has pulled down prices in financial markets, mainly equities, due to the uncertainty over further bank failures and the downstream consequences. While I cannot rule out a recession, I think we can avoid recession if the fall in oil prices continues. I do not think a bunch of paper losses at some larger financial institutions is enough to break the back of the economy. If I am wrong that would be a shame, American workers and companies have worked very hard to build a strong economy. On a brighter note, I am happy to report that LPL Financial (LPL) has been largely unaffected by these issues. LPL Financial does not carry a levered portfolio of securities of any type. LPL Financial has stuck to its core mission – recommending a wide range of products, unbiased research and services to support your advisor – whose primary mission is providing investment guidance and support to you without the conflicts and distractions associated with proprietary products, investment banking activity, or levered securities portfolios.

I continue to think that we will come out of this at some point and return to a rising equity market. Interest rates are low. The Federal Reserve and the Treasury appear to be competent. Oil is down and the dollar exchange rate is up. Inflation is falling again. Outside of financials, valuations look pretty good. Corporate profits are about double the previous peak in 1999, while stock prices (using the S&P 500) are now below the previous peak. And, while some financial companies have levered up their balance sheets, in aggregate U.S. nonfinancial companies have decreased balance sheet leverage to record low levels with a shift from about minus \$1 trillion in net financial assets (net borrowing) to plus \$1.2 trillion currently (net lending) over the last 12 years. To me, this \$2 trillion swing in the balance sheet represents a dramatic reduction in risk. I just wish some financial institutions had been equally careful. As always, please call your financial advisor with any questions or concerns.

Sincerely,



Lincoln Anderson  
Managing Director, Chief Investment Officer

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