



Weekly Market Commentary



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Europe's Problems Are Manageable, but They Need to Be Managed

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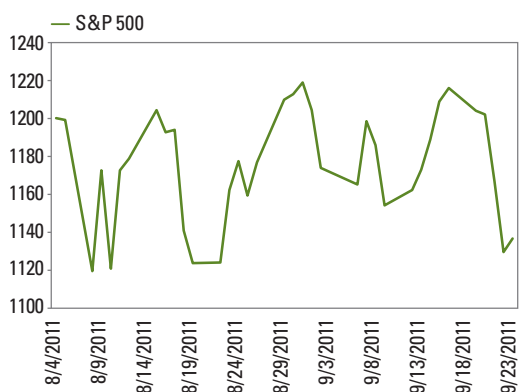
Highlights

Stock markets around the world lost over \$3 trillion last week and entered a bear market as fear of default among some troubled European nations increased once again.

The S&P 500 Index has remained range bound for the past seven weeks. This is most likely due to the fact that a sharp downturn in earnings is already priced in combined with the prospect for earnings growth if a crisis is averted.

Europe's problems are manageable, but they require management. The market moves seen last week push policymakers closer to the tough decisions needed to regain the confidence of investors.

1 S&P 500 Moves from Top to Bottom of Range in Latest Week



Source: LPL Financial, Bloomberg data 09/25/11

The S&P 500 is an unmanaged index, which cannot be invested into directly. Past performance is no guarantee of future results

Last week, the S&P 500 Index dropped 6.5% to 1,136. The Index gave back the 5.4% gain achieved in the prior week, the third-biggest weekly gain since 2009, which had lifted the Index to the top end of the range at 1216. The volatility continues within the range of about 1120 to 1220 on the S&P 500, a range that has prevailed since early August as you can see in [Chart 1](#).

The declines were not restricted to the U.S. markets as the concerns remain focused on the European debt problems. Based on the MSCI All-Country World Index, stock markets around the world lost over \$3 trillion last week (by comparison, all of Greece's government debt totals about \$200 billion) and entered a bear market as fear of default among some troubled European nations increased once again. This was the third largest weekly decline since the global recovery began in March 2009.

It is no surprise that the market appears to be demanding a policy response to the debt problems in Europe. All of the major European stock markets are in a bear market, having declined by about 30% from the peak in early May. However, many of the world's largest markets have avoided a 20% or more decline defined as a bear market, such as those of the United States, United Kingdom, Canada, Singapore and New Zealand. The losses in Europe have been, in general, twice as large as those in non-European nations. They are more severe than even the 21% decline from the peak in Japan which suffered a devastating earthquake and tsunami earlier this year.

While stock values have been affected by the negative sentiment, analyst earnings estimates, in contrast, have remained resilient. In fact, there is not a single nation among the largest 24 whose companies are expected by analysts to produce a loss in aggregate during the coming fiscal year. For example, in the United States, the estimated earnings growth rates for the S&P 500 for the coming four quarters are in the double-digits: 14%, 15%, 11% and 15%. Even in Europe any losses are expected to be temporary and give way to double-digit earnings growth in the coming fiscal year, as you can see in [Chart 2](#).

While U.S. stocks have fallen 15%, analysts' earnings estimates have only been trimmed by about 2%. While we continue to believe, as we have all year, that earnings estimates are a bit too high, we do not believe the major decline priced in by the market is likely. The earnings outlook remains supported by company guidance and world industrial output that remains close to all-time highs. In Europe, earnings growth also remains positive. Market participants have priced in an expectation that earnings will suffer



2 Analysts' Expected Earnings Growth Rates By Country

Companies by Country	Current Fiscal Year	Next Fiscal Year
United States	22.4	16.4
Canada	38.8	18.8
France	7.7	9.8
Germany	2.5	13.1
Italy	20.8	18.6
Japan	19.6	21.6
United Kingdom	16.0	13.1
Austria	11.5	15.8
Belgium	-29.5	76.9
Denmark	15.1	23.2
Finland	-8.6	20.0
Netherlands	19.3	7.6
Spain	-3.9	11.6
Sweden	0.5	12.5
Switzerland	-3.0	14.6
Australia	15.2	15.1
Hong Kong	16.5	4.1
China	23.8	21.3
India	13.3	18.5
Singapore	10.3	3.1
Taiwan	-4.0	20.2
Argentina	16.6	25.0
Brazil	3.8	11.8
Mexico	28.5	16.6

Source: LPL Financial, Thomson Financial data 09/23/11

double-digit declines as a recession and financial crisis erupts, rather than double-digit gains in the coming year as a crisis is averted.

Despite all the negative news, the S&P 500 Index has remained range bound for the past seven weeks. This is most likely due to the fact that a sharp downturn in earnings is already priced in combined with the prospect for earnings growth if a crisis is averted.

There are several ways a crisis may be averted. While euro-zone members have yet to ratify the changes proposed to the European Financial Stability Facility (EFSF) this summer, we believe they will do so with votes scheduled in the coming weeks. Once ratified, a concern market participants have with the EFSF is its limited size of about 440 billion euros. A plan championed by U.S. Treasury Secretary Geithner to address the size of the facility that is winning some support in Europe is to allow the EFSF to borrow from the European Central Bank (ECB), multiplying the funds at its disposal and the impact it can have. The leveraged EFSF funds could be used to buy substantial amounts of troubled European nation debt, making the debt a collective obligation of the euro zone and essentially providing a bridge to eurobond issuance down the road. This form of rescue plan also has the added benefit of acting as stimulus in the form of quantitative easing for the euro zone. These assets can also be used to recapitalize banks that may suffer losses from a partial default by Greece. This is just one of several plans being discussed in Europe to avert a crisis.

Europe's problems are manageable, but they need to be managed. The market moves seen last week push policymakers closer to the tough decisions needed to take decisive action and regain the confidence of investors.



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.

The economic forecasts set forth in the presentation may not develop as predicted and there can be no guarantee that strategies promoted will be successful.

Debt-to-GDP is a measure of a country's federal debt in relation to its gross domestic product (GDP). By comparing what a country owes and what it produces, the debt-to-GDP ratio indicates the country's ability to pay back its debt. The ratio is a coverage ratio on a national level.

Quantitative Easing is a government monetary policy occasionally used to increase the money supply by buying government securities or other securities from the market. Quantitative easing increases the money supply by flooding financial institutions with capital in an effort to promote increased lending and liquidity.

International and emerging markets investing involves special risks such as currency fluctuation and political instability and may not be suitable for all investors.

The Standard & Poor's 500 Index is a capitalization-weighted index of 500 stocks designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries.

The MSCI World Index is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of developed markets. As of June 2007 the MSCI World Index consisted of the following 23 developed market country indices: Australia, Austria, Belgium, Canada, Denmark, Finland, France, Germany, Greece, Hong Kong, Ireland, Italy, Japan, Netherlands, New Zealand, Norway, Portugal, Singapore, Spain, Sweden, Switzerland, the United Kingdom, and the United States.

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