

Economic Perspectives

January 5, 2010



2010 Outlook: Gradual recovery continues amid improving fundamentals.

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- **Optimistic:** Recent economic trends portray an ongoing recovery and we are optimistic of economic prospects in the year ahead. Our optimism, however, must be viewed relative to the severe recession we just endured. The approximate 3% average Real GDP growth we envision over the next few quarters is still below historical recovery standards and significant economic imbalances remain.
- **Jobs, jobs, jobs:** Jobs represent THE most important component of our outlook. We currently expect the U.S. economy to resume generating net positive employment growth within the next few months, with employment gains aiding a consumer spending recovery in the second half of the year. The recovery could still falter should this scenario fail to materialize.
- **Modestly higher interest rates and contained inflation:** We expect market based interest rates to rise moderately as we progress through the new year. Core inflation metrics, meanwhile should remain relatively well contained in our view.
- **Corporate sector still a source of strength in the economy:** Corporate profits for companies of the S&P 500 are currently estimated to rise by a strong 29% in 2010. Strong corporate balance sheets in many sectors could also foster a rebound in merger and acquisition (M&A) activity.
- **Global growth estimates also rising:** Recent improvements in economic fundamentals are not just a U.S. story. Most major economic zones across the globe are also seeing tangible improvements.

KEY ECONOMIC DATA:

	<u>2002</u>	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006</u>	<u>2007</u>	<u>2008</u>	<i>Estimates</i>	
								<u>2009</u>	<u>2010</u>
U.S. Real GDP Growth	1.6%	2.5%	3.6%	3.1%	2.9%	2.2%	-0.8%	-0.3%	3.0%
Real Disposable Personal Income Growth	3.1%	2.2%	3.6%	1.2%	2.7%	3.1%	1.3%	1.2%*	NA
Real Consumer Spending Growth	3.1%	3.3%	3.8%	3.6%	3.2%	2.9%	0.2%	-0.8%*	NA
Unemployment Rate	5.7%	5.6%	5.5%	5.1%	4.5%	4.6%	7.2%	10.0%**	NA
M2 Money Supply Growth	7.5%	7.0%	4.7%	4.4%	4.8%	5.9%	6.8%	5.1%**	NA
S&P 500 Operating Earnings / share	\$48.14	\$55.55	\$66.99	\$76.29	\$88.17	\$86.20	\$68.63	\$62.96	\$78.54
(yr/yr change)	6.6%	15.4%	20.6%	13.9%	15.6%	-2.2%	-20.4%	-8.3%	24.7%

Economic estimates are consensus estimates as surveyed by the most recent Wall Street Journal survey.

** = Number based on average through Nov. ** = Number based on most recent rate*

Historical data and First Call consensus estimates for the S&P 500 sourced from Baseline

2010 Outlook: The (bumpy) road to recovery.

Following six consecutive quarters of economic contraction, which amounted to the deepest and longest period of decline since The Great Depression, the U.S. economy should enter 2010 with two quarters of fairly solid growth under its belt. Clearly we are not out of the economic woods as of yet, but we are optimistic of the economic path ahead.

Economic fundamentals in the U.S. and most other major economic regions across the globe have stabilized, and in most cases are experiencing tentative recovery. In the year ahead, we expect the global recovery should make further progress as economic fundamentals strengthen. Higher interest rates, ongoing consumer deleveraging, and what will likely be rising tax rates across much of the developed world, are detriments to this process, but these issues are more likely to be headwinds rather than recovery busters. Regionally, we expect business activity in the U.S. to outpace that of Europe or Japan, yet trail that of developing regions such as China, India, Brazil and most of emerging Asia. Inflation and interest rates should remain low relative to historical standards, yet we anticipate market based interest rates to rise over the course of the year as economic conditions improve.

While we are optimistic of the outlook, economic fundamentals are far from optimal. Exceptionally high government debt loads remain a very adverse legacy of our recent crisis, and the uncertain impact of pending health care reform legislation could make the public finance situation worse. The outlook could also dim considerably should businesses lack the confidence needed to resume job creation in the first half of the year; and the robustness of any employment rebound could also be tempered by a continuation of credit availability hurdles in the small business sector. Certainly jobs will be a dominant theme over the intermediate-term. Fortunately, we feel that recent employment indicators have been on a positive trend and within the next few months we look for the unemployment rate to peak, and nonfarm payrolls to turn positive on a sustainable basis.

In sum, 2010 is likely to be a transition year on the path toward a full economic recovery. As we go through this process, there are bound to be some discouraging economic reports that cause people to question the legitimacy or robustness of the recovery, and investors should not expect economic measures to show improvement on a purely linear or consistent basis. As we have noted in past reports, it is trends, not singular reports that are important in determining the most likely path forward. In this month's *Economic Perspectives* report we take a look at what recent trends suggest about economic conditions in the year ahead.

Key components of our 2010 forecast:

Economic growth: In 2010, the U.S. economy should see its first full-year of positive economic expansion in two years, and it could register its strongest pace of growth in five years (it's a low bar). This pace, however, is likely to be weaker than that of past recovery periods. We are currently forecasting U.S. economic growth in the first half of 2010 of approximately 3.0% on average, with the general pace of expansion picking-up modestly in the second half of the year. Inventory replenishment should be the most significant contributor to growth in the first half of the year. We expect stronger consumer spending, aided by a return to employment growth, to fuel expansion in the second half of the year. Improved business spending and slightly stronger export growth should also offer some support. Furthermore, we note that recent economic trends have been broadly better than expected, and we presently believe our forecast could ultimately prove conservative. (see page 7 for greater detail on our near-term economic forecast)

From a global perspective, economic growth in the developing world should again outpace that of developed nations in 2010, as the global economy improves materially versus a weak 2009. There are still significant risk factors prevalent across the world, evidenced by the serious fiscal issues in such countries as Greece, Spain, Ireland, Japan and the U.K. to name a few. A broad economic recovery will aid the situation in many of these markets, but will certainly not be a cure-all. Amongst the major industrialized world, we believe growth in the U.S. provides the most attractive prospects relative to risk, which is consistent with the recommended equity allocations as suggested by our Senior Market Strategist, Marc Zabicki, CFA. We expect the rebound to be comparatively less robust in Europe, and growth in Japan is likely to struggle under the weight of weak domestic consumer spending and a strong Yen.

Employment: Job growth should return in the first quarter of the year, and strengthen as the year progresses. For the average American, employment prospects are likely THE most important component of any economic outlook and jobs are also the most important variable in our economic forecast as well. Fortunately, we believe employment indicators currently portend a fairly solid rebound in the job market over the next year. November's unemployment report was the best we have seen in almost two years with net job losses very close to break-even. New claims for unemployment insurance have also been declining at a fairly rapid pace and the recent spike in labor productivity bodes well for forward employment prospects. Further, employment indicators, especially in the first half of the year, should benefit materially as the Federal government begins hiring the more than one-million temporary workers needed to conduct the 2010 Census. These developments give us confidence that the U.S economy should shortly begin generating net positive job growth on a sustained basis. We expect the unemployment rate should peak at about 10.5% around March or April, and we expect the unemployment rate to end 2010 between 9.0% and 9.5%.

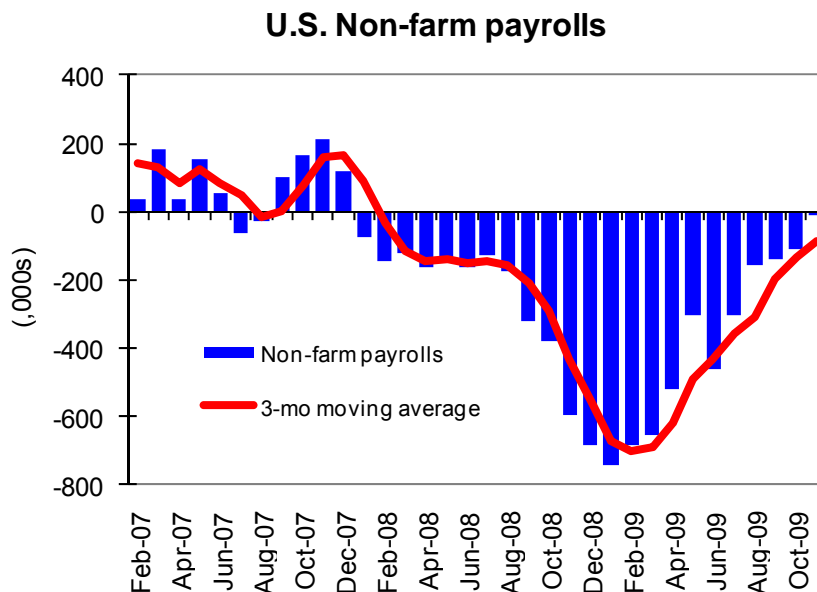


Chart Source: Labor Dept., Ameriprise Financial.

Inflation: Inflation pressures remain benign as we enter the new year given what remains a relatively weak demand environment and slack resource utilization. Our baseline outlook calls for core inflation rates (which exclude volatile food and energy costs) to remain fairly well contained for several more months at least, with rates over the first half of 2010 of between 1.8% and 2.0%. Pricing pressures, however, could percolate in the second half of the year should the economy rebound more strongly than we currently project, and headline inflation numbers (which include food and energy) could heat-up depending on the perceived crude oil supply / demand outlook (see "Energy Costs" below). Many commodity costs have already risen in anticipation of improving global economic fundamentals. These costs may filter through into core product prices sooner, rather than the later, that many forecasters seem to presently expect. As such, we are currently forecasting core inflation pressures in the second half of 2010 to rise modestly, to annualized rates of between 1.9% and 2.3% - higher than today's levels, but not high enough, in our view, to cause significant concern at the Fed.

Energy Costs: Crude oil prices have shown remarkable resiliency over the last nine months despite weak global demand and flush inventory levels. Dollar weakness over this period offered some upside bias to commodity costs but prices are still higher even after adjusting for the dollar's influence. This gives us pause to believe that prices could moderate should global demand levels rise amid a rebounding economic environment. As such, we believe energy prices have more upside than downside risk over the intermediate-term. Despite significant technological advancements there simply remains no true alternative to oil in its primary applications. Improving demand amid a strengthening global recovery, combined with ongoing geopolitical issues especially in oil producing regions, should lift prices. We do not expect a return of \$150 /barrel crude oil over the intermediate-term, but we expect prices are likely to trade closer to an average \$80 to \$90 range than they are \$60 to \$70. On a positive note, higher energy prices over the intermediate-term should further fuel the race for long-term viable alternatives.

Interest rates: Higher. Interest rates start the year at or near historical lows. Some of these rates however, currently benefit from temporary government or Federal Reserve programs that will be wound down this year. The Federal Reserve for instance has already announced that its program to purchase \$1.25 trillion in mortgage backed securities is coming to an end and should reach its conclusion by the end of March. The curtailment of this artificial market support is likely to modestly lift mortgage borrowing costs, thus acting as a modest de facto tightening of monetary policy. Risk aversion should also subside this year as economic conditions stabilize, thus the migration to the safety of Treasury securities that occurred at the heart of the crisis should gradually reverse as confidence recovers. These issues, combined with the U.S. Treasury's need to issue heavy amounts of debt and what we anticipate to be a moderate rise in global credit demand, should result in a steady rise in interest rates through the year. In our outlook, we expect the yield on the Ten-year Treasury security (a common benchmark for other borrowing costs) to end the year between 4.5% and 5%, versus its current 3.8%. We expect average 30-year fixed mortgage rates to end the year near 6% versus a current 5.3%.

At the very low-end of the interest rate maturity spectrum, we currently expect Federal Reserve officials to maintain the Fed Funds Rate at its current historical low target range of 0% to 0.25%, deep into the year. The rate could even be maintained into early 2011 should inflation pressures remain muted, as it is better to err on the side of growth support than it is to follow the Japanese experience and stifling economic recovery too soon.

How Federal Reserve officials currently view the U.S. economic outlook:

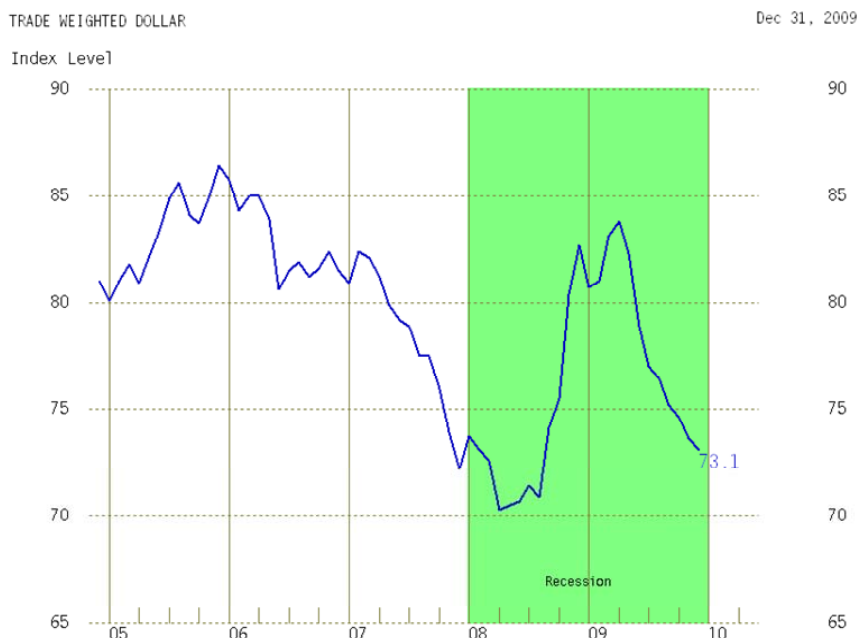
U.S. Federal Reserve "central tendency" forecast estimates:

	<u>2010</u>	<u>2011</u>	<u>2012</u>
U.S. Real GDP Growth	+2.5% to +3.5%	+3.4% to +4.5%	+3.5% to +4.8%
Unemployment Rate	9.3% to 9.7%	8.2% to 8.6%	6.8% to 7.5%
Core Inflation	+1.0% to +1.5%	+1.0% to +1.6%	+1.0% to +1.7%

Source: U.S. Federal Reserve. Estimates as of November 4, 2009

The dollar: The U.S. dollar has been on a rollercoaster ride over the last few years (see chart below). What will be the driver of the greenback's value in 2010? Interest rate differentials? Inflation prospects? Investor risk appetite? Trade measures? As always, the answer is likely to be combination of all of the above, with volatility remaining a key element of the dollar trade.

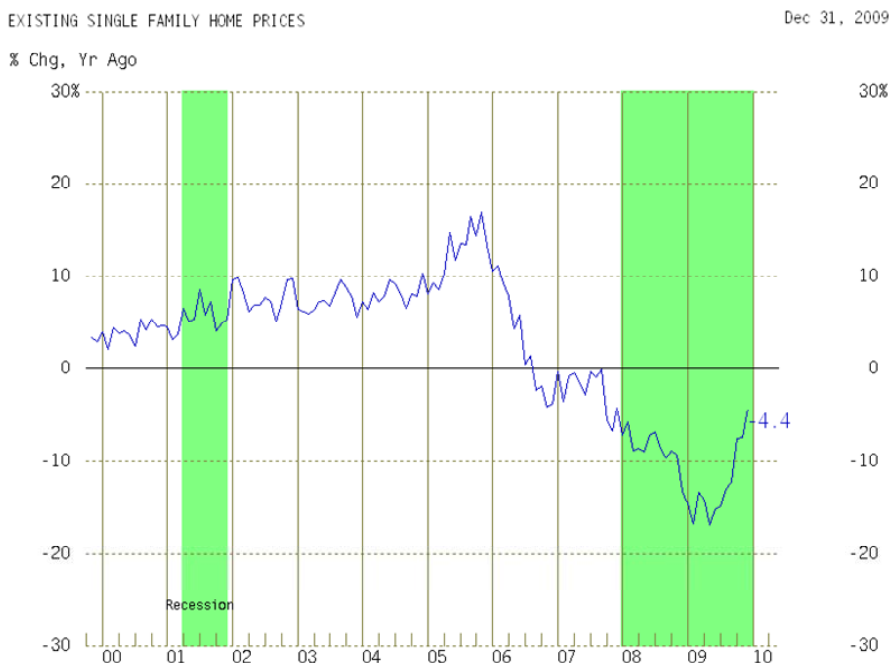
Net / net, we believe the U.S. dollar on trade-weighted basis is likely to end 2010 with a flat to slightly weaker performance (i.e., plus or minus 5%). A flat performance would be contrary to the dollar's pre-crisis downward trend. But our view is fueled by our belief that the U.S. economy, despite its ongoing troubles and rising public sector debt burden, is still in better fiscal shape than that of many other developed economic regions, and with better intermediate-term growth prospects.



Source: Baseline

This backdrop should eventually attract greater foreign demand for U.S. based assets. Weighing on the greenback however, we believe the dollar could lose some ground to some faster growing developing countries and many of the globe's major commodity oriented economies (Australia, Canada, or Brazil for example) as well. Major exchange rates are further likely to be influenced by the timing of any central bank interest rate hikes. Presently we believe the odds favor the European Central Bank to raise its short-term borrowing benchmarks before the somewhat less hawkish U.S. Federal Reserve.

Housing: Conditions in the U.S. housing market improved significantly in 2009. "Improvement" is certainly a relative term in this case but the relative stabilization we have seen is clearly better than the rapid pace of decline we experienced from 2005 through 2008. After what we believe could be a fairly solid 2010 spring selling season, housing sector gains could slow as mortgage borrowing costs are likely to rise and Federal Government incentives for both new and existing home buyers expire by the second quarter. Foreclosures, meanwhile should remain at very elevated levels throughout the year, and likely into 2011 as well; but recent months have seen the percentage of outstanding mortgages entering the delinquency pipeline as declining. Although the sector will take more time to fully heal, current trends do not seem to suggest a "second leg down" for the sector, especially if broader economic conditions improve as we expect. Over time, the housing market should benefit from improving economic conditions, near record affordability, inventory levels that have been pared significantly, and, though higher, still relatively low borrowing costs. Clearly there will be regional differences in the pace of recovery but each month and each quarter we are beginning to see more and more regions stabilizing and prices turning higher.



Source: Baseline

Corporate profits: Overall, we believe the economic outlook is supportive of corporate profit prospects, while the corporate sector itself remains a strong source of support for the U.S. economy and equity markets in general. Corporate profits for companies of the S&P 500 are currently forecast via Thomson First Call consensus estimates to grow by a very strong 29% in 2010. Corporate America also enters the new year with strong balance sheets in most sectors with the exception of the financials, and the deep cyclicals such as autos or steel. These conditions appear poised to foster a general improvement in merger & acquisition (M&A) activity which should also aid overall equity market sentiment. (see page 8 of this report for more on the corporate profit outlook)

What are the growth drivers?

Over the first half of 2010, we expect the economy to receive its strongest growth contribution from reduced inventory reduction efforts. Business inventories have been falling at a very rapid pace and are on track to hit a new all-time low within the next few months in terms of days supply. As inventories become too low, production will have to ramp-up rapidly just to catch-up with demand. Such a scenario bodes well for future economic growth, as the longer this situation continues the more the production equation is slowly being spring loaded. By the second half of 2010, however, the recovery will begin to look to the consumer to sustain its growth, whether the consumer is ready is not.

Contribution to change in GDP	2009				2010			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
	Actual	Actual	Actual	Estimate	Estimate	Estimate	Estimate	Estimate
PERSONAL CONSUMPTION	0.4	-0.6	2.0	1.2	1.3	0.9	1.3	1.4
FIXED INVESTMENT	-6.6	-1.7	-0.2	-0.4	0.1	0.9	0.5	1.3
CHANGE IN INVENTORIES	-2.3	-1.4	0.7	2.5	1.2	1.2	0.3	0.3
NET EXPORTS	2.6	1.7	-0.8	0.2	0.0	-0.3	0.2	0.0
GOVERNMENT	-0.5	1.3	0.6	0.6	0.3	0.3	0.5	0.4
TOTAL GDP	-6.4	-0.7	2.2	4.1	2.8	3.1	2.9	3.3

Numbers may not add-up due to rounding

Source: Actuals via Commerce Department, Estimates via Ameriprise Financial

Global views also improving:

Signs of improving economic fundamentals have not been a U.S. based story alone. Across the globe signs of recovery are emerging in the form of stronger Chinese retail sales, manufacturing expansion in Europe, rising home prices in the United Kingdom and stabilizing unemployment rates in places such as Australia and Japan. Of course these citations are a small fraction of the available data, but the growth trends are starting to emerge on a broad base in our view, thus spurring global growth expectations to rise.

OECD Global Economic Projections:

	2009	2010	2011
United States	-2.5	2.5	2.8
Euro Region (13 OECD members)	-4.0	0.9	1.7
Germany	-4.9	1.4	1.9
France	-2.3	1.4	1.7
United Kingdom	-4.7	1.2	2.2
Japan	-5.3	1.8	2.0
Korea	0.1	4.4	4.2
China	8.3	10.2	9.3
India	6.1	7.3	7.6
Russia	-8.7	4.9	4.2
Brazil	0.0	4.8	4.5

Source: Organization for Economic Cooperation and Development (OECD)
Economic Outlook No. 86, November 2009

Economic Outlook:

The Commerce Department recently revised its estimate of U.S. third quarter GDP growth notably lower to +2.2% from +2.8%. Initially, Commerce had reported growth for the period at a much more robust +3.5%. There were a number of factors contributing to the downward adjustments, including weaker than originally measured consumer spending, lower business investment in new facilities and larger inventory cuts.

The third quarter's loss is the fourth quarter's gain in many respects, however, as estimates of fourth quarter growth have been steadily improving. Consumer spending, the trade balance, and business inventories have each been trending in a better than expected manner through the first half of the quarter and we now see the U.S. economy as having expanded at a 4.1% annualized pace in the fourth quarter as compared to our prior forecast for a 3.3% gain. Our outlook for 2010 has also improved and we now expect quarterly GDP growth in 2010 to average approximately 3.0%, as compared to our view last month for average growth of about 2.75% (and +2.55% in October).

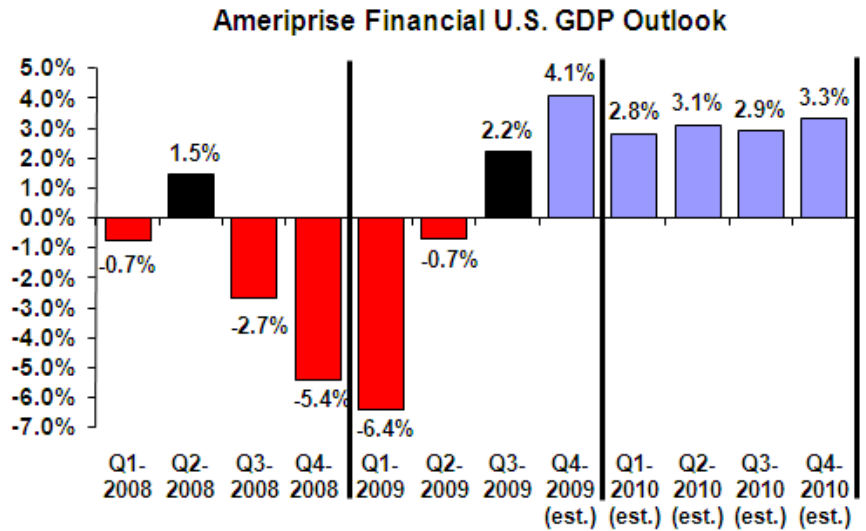


Chart Source: Ameriprise Financial Services, Inc. and the U.S. Commerce Dept.

One of the economic highlights of the last month was the much smaller than expected number of net job losses in November. The Labor Department reported net job losses for the month of just 11,000 - the smallest number of cuts in nearly a year and a much smaller drop than the 114,000 job losses forecast. The improving jobs picture may have led some Americans to hit the malls a bit harder this holiday season as initial reports indicate a modest yr/yr improvement in overall sales for the period. Therefore, December sales activity should build on the slow yet steady improvement consumer outlays have shown over the last several months.

New claims for unemployment insurance also broke below the 500,000 level in the month of November and have been trending steadily lower in recent weeks. The pace of improvement in this measure has been notably better than that of either of the prior two recessions but we are somewhat skeptical of recent numbers due to the potential influence of seasonal adjustment factors.

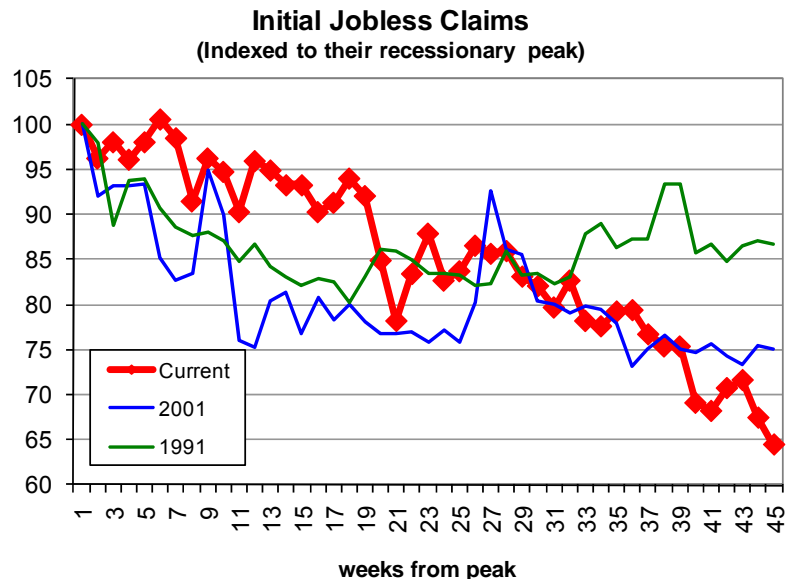


Chart Source: Ameriprise Financial Services, Inc. and the U.S. Labor Dept.

Corporate profits: The lynchpin between the economy and stock prices.

Corporate profits for companies of the S&P 500 exceeded estimates by a wide margin in the third quarter. A final tally of the results show profits for the group were down just 5% versus year-ago levels as compared to expectations for a 17% decline. An exceptionally strong 79% of S&P 500 companies reported better than expected profits according to Thomson, while just 14% came in below estimates.

Analyst estimates for the fourth quarter of 2009 currently look for a strong 29% yr/yr increase. This, however, is down considerably from the +42% yr/yr gain sought just a few weeks ago. Almost all of this recent negative adjustment comes from the financial sector where earnings estimates are being diluted by TARP repayment efforts (i.e. more shares outstanding). We also note that the strength of the Q4 estimate is largely a function of very easy year-ago comparisons. Estimates for Q1-2010 meanwhile are currently looking for a yr/yr gain of 35% (versus +33% a few weeks ago). For all of 2010, S&P 500 earnings are currently forecast via the First Call consensus to be 29% higher yr/yr – four ticks higher than last month’s consensus estimate.

Corporate revenues are also starting to show modest improvements. Total revenues for the S&P 500 were down 14% yr/yr in the third quarter but were 2% higher on a quarter-over-quarter basis for the second consecutive quarter. We expect revenue growth should slowly gain momentum in the quarters ahead, thus allowing companies to further leverage prior cost cuts via margin expansion. As we have noted in past commentaries, this is very much the typical pattern at this point in the economic cycle. Early in an economic recovery, companies slash costs aggressively and these cuts fuel early sequential earnings improvements. As the economy stabilizes and begins to grow, revenue gains can be leveraged off of the prior cost reductions to provide further profit margin improvements.

Current estimates for the S&P 500 and its components:

Year-over-year Operating EPS growth: Actuals and Estimates:

	Q1-2008	Q2-2008	Q3-2008	Q4-2008	Q1-2009	Q2-2009	Q3-2009	Q4-2009	Calendar 2008	Calendar 2009	Calendar 2010	Forward
	ACTUAL	ACTUAL	ACTUAL	ACTUAL	ACTUAL	ACTUAL	ACTUAL	Estimates	ACTUAL	Estimates	Estimates	P/E
Consumer Cyclical	-21%	-55%	-47%	-92%	-101%	64%	139%	1070%	-55%	62%	48%	16.9
Consumer Staples	14%	14%	15%	6%	-2%	2%	6%	12%	12%	5%	8%	14.3
Energy	30%	21%	58%	-25%	-61%	-67%	-63%	-27%	19%	-57%	44%	14.0
Financials	-85%	-91%	-124%	-61%	40%	319%	256%	123%	-108%	531%	47%	19.6
Health Care	7%	11%	7%	10%	2%	4%	5%	1%	9%	3%	11%	12.3
Industrials	12%	9%	3%	-16%	-38%	-34%	-40%	-22%	1%	-34%	8%	17.0
Materials	10%	13%	8%	-62%	-75%	-65%	-47%	38%	-5%	-55%	72%	19.1
Technology	13%	17%	6%	-23%	-30%	-17%	-3%	29%	1%	-6%	22%	17.3
Telecom	4%	0%	-13%	-14%	-12%	-19%	-20%	-24%	-6%	-27%	6%	15.7
Utilities	7%	6%	-4%	2%	-1%	-6%	0%	-8%	2%	-4%	7%	12.8
S&P 500 Total	-17%	-21%	-17%	-28%	-31%	-13%	-5%	29%	-20%	-12%	29%	15.5

S&P 500 Trailing

12-month Operating EPS	\$82.38	\$77.39	\$73.56	\$68.63	\$62.85	\$60.31	\$59.37	\$62.96	\$68.63	\$62.96	\$78.54
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Source: First Call via Baseline Financial; data as of 01/04/2010

Stocks typically bottom long before the economy:

We have highlighted the following data in the table below for the last few months. We believe this historical view of stock performance during economic turning points offers valuable insights for investors at this stage so we intend to re-publish it for a few more months as well.

Our research, as reflected in the table below, shows that in almost every recession since 1960 stock prices have hit bottom about **9 months** prior to the eventual bottom in corporate profits. The lone exception to this was the recession of 2001 when stocks had much more to “give-back” from a valuation perspective.

Recessions and stock performance: A historical perspective.

	Change in: <u>Real GDP</u>		Change in: <u>Corp. profits (TTM)</u>		Change in: <u>S&P 500</u>		<u>Months that the stock market bottomed ahead of profits</u>	Change in: <u>unemployment</u>		<u>Months that the stock market bottomed ahead of unemployment rate</u>
	peak to trough	time (qtrs)	peak to trough	time (mos)	peak to trough	time (mos)		peak to trough	lowest rate / highest rate	
*1929-'33	-26.5%		na		na		na			
*1937-'38	-3.4%		na		na		na			
1948-'49	-1.8%	2	na		-16.9%	12	na			5
1953-'54	-2.7%	3	na		-11.1%	8	na	3.6	2.5 to 6.1	13
1957-'58	-3.7%	2	na		-16.9%	5	na	3.8	3.7 to 7.5	8
1960	-1.6%	3	na		-10.1%	15	3	2.3	4.8 to 7.1	8
1969-'70	-0.6%	2	-15.5%	15	-29.0%	18	10	2.7	3.4 to 6.1	7
1973-'75	-3.1%	5	-17.1%	12	-43.4%	23	14	4.4	4.6 to 9.0	6
1981-'82	-2.9%	3	-18.7%	14	-19.4%	20	12	5.2	5.6 to 10.8	5
1990-'91	-1.3%	2	-37.5%	37	-14.8%	4	24	2.6	5.2 to 7.8	21
2001	-0.4%	1	-54.4%	19	-44.6%	30	-7	2.4	3.9 to 6.3	5
Averages:		2.9		19.4		15.0	9.3	3.4		8.7
2008-'09 so far			-38.0%**	27**	-56.8%	17	?	5.8**	4.4 to 10.2**	

Data as of 08/28/2009

* Prior to 1947 U.S. Real GDP available only on a yearly basis.

** Ameriprise Financial estimate

TTM: Trailing Twelve Month basis

Source: Ameriprise Financial Services, BEA, Baseline, economy.com, National Bureau of Economic Research (NBER)

How to read the above table: Taking the recession of 1990-1991 as an example: from peak to trough Real GDP in the recession of 1990-'91 declined by 1.3% and there were two quarters between said peak and trough. Corporate profits meanwhile fell 37.5% from their peak to trough during this period and there were 37 months between these highs and lows. The S&P 500 declined a total of 14.8% from its high point to its low point during the period (based on month-ending values) and there were 4 months between these occurrences. The stock market hit its low 24 months before corporate profits saw their low for the period and the unemployment rose by 2.6 percentage points, from a low of 5.2% to a high of 7.8%. Stock prices also bottomed 21 months ahead of the eventual peak in the unemployment rate.

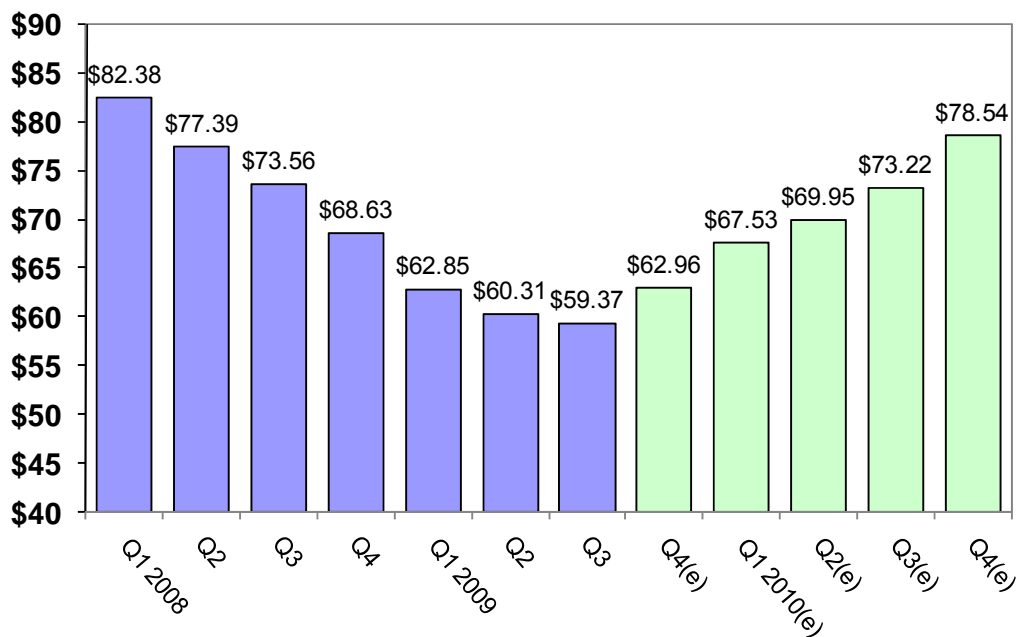
Putting this data to work:

As investors, how can we use this information and apply it to the current cycle? We also went back and looked at how valuation multiples performed during prior cycles. Given that our research (as outlined in the chart above) indicated that stock prices typically begin to move higher 9.3 months ahead of the eventual bottom in corporate profitability, it equated that valuation multiples have historically also hit their low at the time of the stock market low. In other words, if this past February's month-ending close for the S&P 500 of 735.09 was indeed the low for this cycle, then we would expect the P/E ratio at that time to have also been the low for this cycle (i.e. because the denominator, earnings, are still falling). The P/E ratio at the end of February was 10.7. Historically, we found that by the time corporate

earnings did reach their lows (9.3 months later), P/E multiples were 68% higher on average. Excluding the 2001 recession when valuation multiples were still well above their historical norms, the average cycle low for the P/E metric was 11.3 with P/E ratios rising to an average of 18.3 by the time corporate profits hit their low. Thus, from these historical averages we can get a sense of where stocks prices could be headed...if we assume that the third quarter of this year indeed marked the low in the current corporate profit cycle, and that current forward estimates are close to correct, we can follow the resulting math: $\$59.37 * (10.7 * 168\% = 18.0) = 1069$. These numbers thus suggested a possible value for the S&P 500 of 1069 at third quarter's end (very close to the third quarter's actual ending value of 1057). Using the same formula to calculate a potential Q4 ending value provided us with a value of 1133 (as compared to the ACTUAL 2009 year-ending value for the S&P 500 of 1115). We use a similar formula, again based on our historical evaluation, to come up with the data below. Historically, however, the PE multiplier declines over time and in our table below we use a 16.5x metric for our 2010 calculation. Our Senior Market Strategist, Marc Zabicki, CFA, currently forecasts a 2010 year-ending level for the S&P 500 of 1262 - equating to an estimated year-ending P/E of 16.1 assuming First Call full-year S&P 500 earnings estimates are correct. Also, we note that the graph and table below are for illustrative purposes only and implied S&P 500 Index levels may not match our official targets.

In graphical form....

S&P 500 Trailing Twelve Month Earnings (TTM)
(actuals and estimates via Thomson First Call)



	Q3 2009	Q4 2009	Q1 2010	Q2 2010	Q3 2010	Q4 2010
TTM S&P 500 Earnings Estimates*	ACTUAL \$59.37	\$62.96	\$67.53	\$69.95	\$73.22	\$78.54
Estimated P/E Ratio**	18.0	18.0	18.0	17.5	17.0	16.5
Potential S&P 500 Implied Value	1069	1133	1216	1224	1245	1296

TTM= Trailing Twelve Month

* via First Call

** Ameriprise Estimates

Summary:

Our confidence in the global economic recovery continues to build. However, the path is not going to be the linear, predictable recovery with steadily growing momentum that we would all like to see; but then again few if any recovery periods ever are.

Beyond 2010, we believe the American economy should do well. We believe we should enter the next phase of the economic cycle with rising employment levels, very affordable housing costs, and interest and inflation rates near historical norms. Consumers should also enter the next phase with much improved balance sheets, a position much of corporate America already enjoys outside of the financial sector. Of course we always face risks as well, and the recovery could stall if the employment picture were to falter in its recent pace of improvement. The rapidly rising U.S. Federal budget deficit is also a serious source of concern as this imbalance needs to be addressed given the significant risk it poses to future growth prospects. Unfortunately, higher tax rates and fiscal spending constraints are likely to be the prescribed solution to the deficit situation. We believe these measures should emerge as a headwind for the economy over the next few years rather than become a recovery killer, however.

Finally, one only need look at a very long-term chart of our growth as a nation to determine that it pays to be an optimist. We do occasionally run into problems, and we will again in the future, but these difficult periods tend to show up as bumps along the road rather than long-term detours. Have a very good year.

RISKS: Significant economic challenges remain, but we believe many of the economy's imbalances enter the final quarter of 2009 in much healthier condition and still making progress. Clearly however, some issues remain, and a rising Federal government debt position poses longer-term challenges. These issues are likely to weigh on growth prospects over the intermediate-term rather than send us back into recession, in our opinion. Additionally, without a robust improvement in employment and a coincident improvement in consumer spending, by the second half of 2010 (at the latest), the recovery could stall. This could be a dangerous scenario given that there is very little more that can be safely done to aid the economy under traditional measures of monetary or fiscal policy.

While we have confidence in our economic outlook, we recognize that serious economic and financial market challenges remain. Recent credit market turmoil has widely been seen as the greatest risk to the global financial system in a generation. Despite what we believe are signs of improvement in this space, notable risks remain evident and the improvements could unexpectedly reverse due to any number of unforeseen circumstances. The ongoing correction in the U.S. housing market also raises the risk of a prolonged or deeper than expected economic contraction, especially if consumer access to credit remains constrained. Commercial mortgage default rates are also rising and could pose yet another hit to the financial system in the quarters ahead. Legislative changes, along with potentially higher personal and corporate tax rates, also seem to be strong likelihood in the quarters and years ahead and these measures could hamper the economy's growth potential. Given these uncertainties, stock prices are likely to remain volatile over the intermediate-term. Terrorism and geopolitical turmoil are also significant factors capable of producing negative economic shocks.

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