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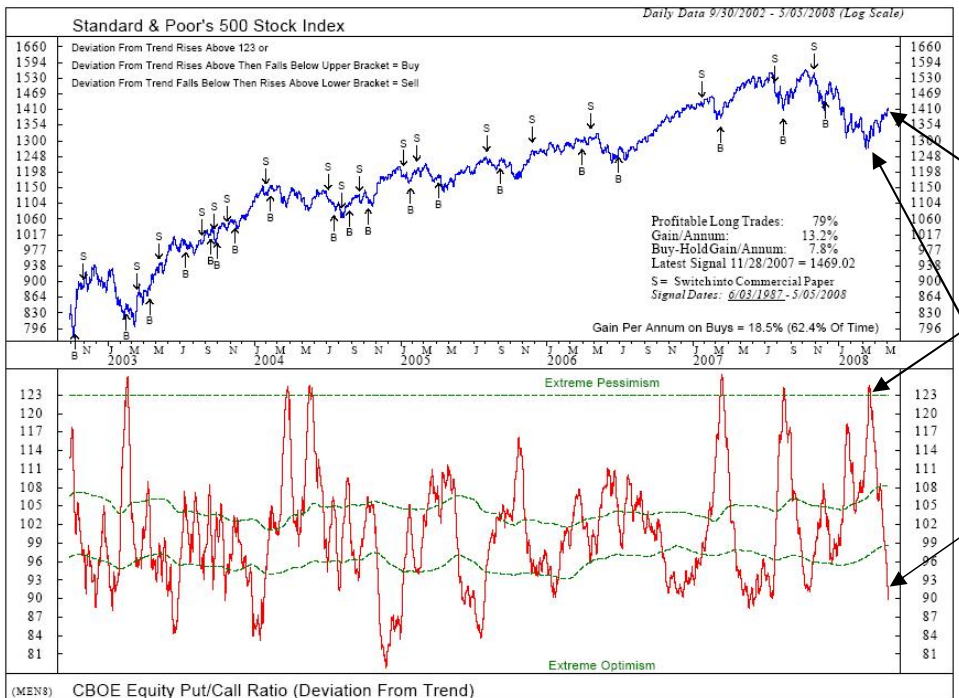
Earnings Season Ending..... Reality Returns

Truth is! The market fared far better during first quarter earnings season than we would have expected. It was not that earnings were that great, but rather expectations were extremely low. As earnings season winds down we worry about the market from five perspectives:

- 1. Catalysts for euphoria dissipate:** Going into earnings season, investors were on the ledge and looking for a reason to jump. Although many companies delivered poor earnings and guidance was guarded the news was not out of alignment with prior pre-announcements or news reports. Without the transparency earnings season offers, we worry that fear will return and investors will once again ponder worst case scenarios.
- 2. Optimism has returned:** The extreme pessimism that had gripped the market coming into earnings season has disappeared and been replaced by a growing sense of optimism. (See Chart 1) You don't have to look far to find the talking heads telling us that the worst is behind us and the fiscal and monetary stimulus thrown at the market are beginning to work. We have yet to see enough evidence to support that outlook and prefer to take a wait and see approach. See the *Weekly View* for more: http://www.riverfrontig.com/commentaries/documents/weekly_view_050508.pdf
- 3. Entering Seasonally Weak period:** There is truth to the adage "Sell in May and go away"
- 4. Market approaching important resistance levels:** Since mid-March, the S&P 500 has rallied from 1288 to over 1400. With the S&P 500 at 1407, key levels of resistance are not far away. We see important resistance levels for the market between 1425 and 1440 and believe the market will need some strong catalysts to break above these levels.
- 5. Commodity Prices keep rising:** The weather is hampering the planting season, tensions are rising in the Middle East and Africa and oil and agricultural commodities keep rising. Today, non-discretionary spending (medical, food & energy, financial obligations) represents a record 57% of income, which is likely to crimp discretionary spending.

What to do? We continue to position our portfolios anticipating that a new period of economic expansion is not yet on the horizon. We are watching signs that we may be wrong, but have not yet seen compelling evidence to necessitate dramatic repositioning. We believe investors should continue to overweight defensive sectors like Consumer Staples, that provide an important ballast to portfolios should fear return and favor high quality companies with a history of delivering growth in all economic environments. A few of our favorite ideas include: Powershares Large-Cap Growth ETF (PWB-O-\$17.6), CVS (CVS-N-\$41.81), Express Scripts (ESRX-O-\$69.53), United Technologies (UTX-N-\$74.62), BJ Services (BJS-N-\$28.36), First Trust Revere Natural Gas (FCG-A-\$27.13).

Chart 1:



S&P 500 at Low and Pessimism at extremes going into Q1 Earnings Season.

S&P 500 now 10% higher and Optimism at extremes coming out of Q1 Earnings Season.

Charts Courtesy Ned Davis Research

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