RIVERFRONT INVESTMENT GROUP

Riverfront Investment Group, LLC
9011 Arboretum Parkway, Ste. 110
Richmond, VA 23236

TEL 804.549.4800
FAX 804.549.4819
TOLL FREE 866.583.0744

www.riverfrontig.com

Daily Thought for April 2nd 2008

Prepared by;
Rod Smyth, Chief Investment Strategist
Doug Sandler, CFA, Chief Equity Officer

Market View:

Powerful rally driven by depressed sentiment and short covering on some good news for the banking industry. We still believe this is a multi month rally in the bear market.
Crowd sentiment poll (shown below) is sufficiently depressed to allow rally to continue. The S&P 500 hit the first critical test at 1370 yesterday. We think it can go higher. The next resistance is 1400 and the 200 day moving average around 1440. If we are right about this being a bear market rally, then it should fail below 1440.

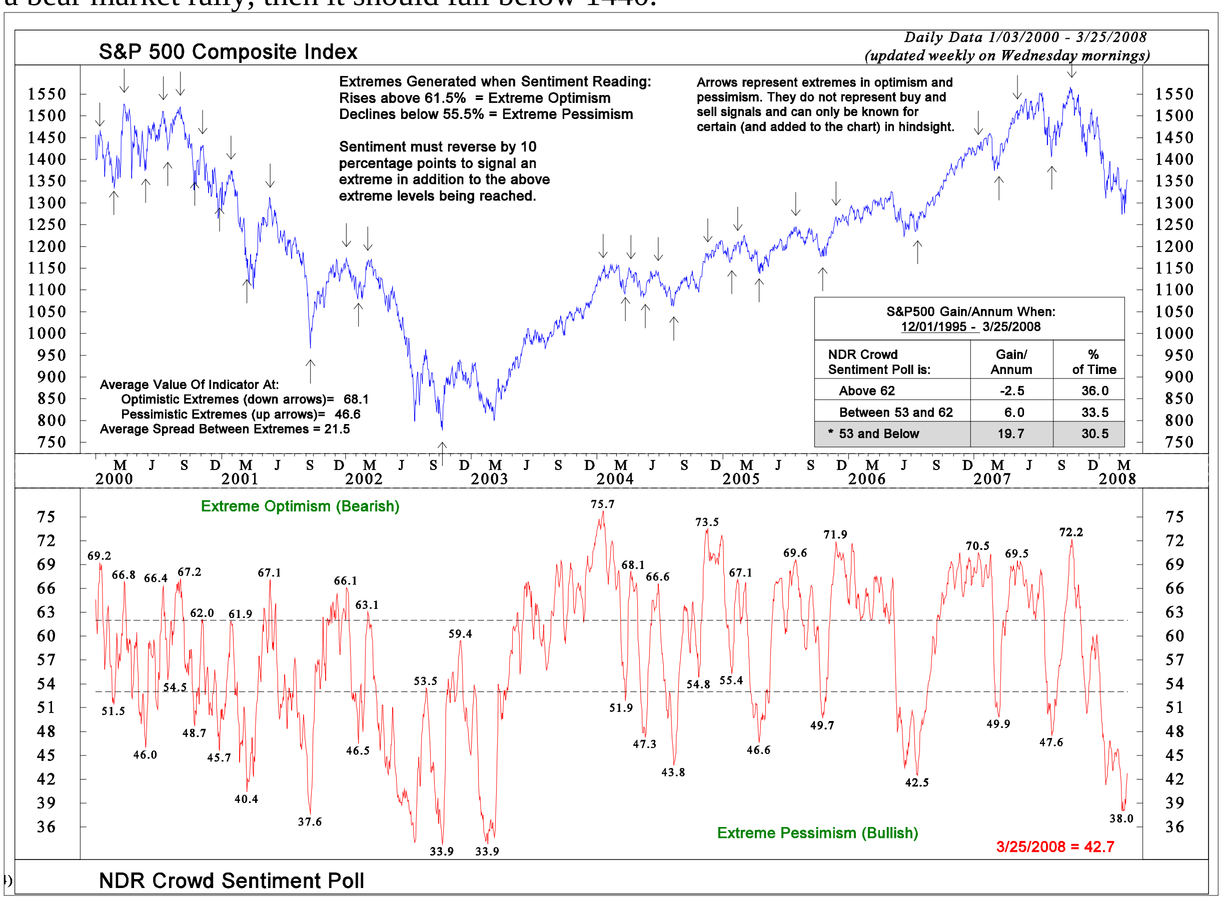

*Chart Courtesy NDR Research

Equity View:

If I had a nickel for every time someone reminds me of the wonderful buying opportunity they had in Citigroup (C-N-$23.84) in the early 90's when they bought the shares below $5 I would be a rich man. We think the memory of that event may be what is driving a large amount of the flows into bank stocks currently. In our opinion, it will take time for the banks to bottom and the opportunity to buy the group cheaply will not run away. From a fundamental perspective we anticipate a second shoe dropping before the final bottom has been made in the financials. The first shoe has already dropped… that shoe was the ramifications of stupid underwriting. Banks that allowed underwriting standards to slip, lending money to sub-prime borrowers or requiring little or no documentation, have paid the price for their mistakes. The second shoe to drop, in our opinion, will not occur for several weeks or months, and will be a result of a recession. In past recessions, banks have had to aggressively build loan-loss reserves to offset default spikes on mortgages, home equity lines and commercial lending. The required reserve building may be above past cycles because many banks have not been able to build their 'rainy day funds' as aggressively this cycle as they have in the past due to new accounting requirements that place limitations on reserves for fear of income smoothing. We believe this second shoe will keep a ceiling on the banks for some time.

The current bounce in bank stocks and other correlated financials may still have some legs and investors underweight the group will need to 'grit their teeth and bear it' a few more weeks. In our opinion, the bounce is likely to stall at the point where the group broke down in February 2008. For the average bank, this might be an additional 5-10% upside, which is a move that only traders can play, in our view.

Our portfolio positioning in the financial group is a slight underweight with a quality bias. We have been wary of the largest financial institutions and have preferred smaller franchises that have been able to operate outside the spreading contagion. Companies like Cullen Frost (CFR-N-$55.11), Northern Trust (NTRS-O-$71.19), US Bancorp (USB-N-$34.01) and Aflac (AFL-N-$66.82) represent the largest financial positions in our portfolios.