STANDARD & POOR'S

# The Outlook

*Intelligence for the Individual Investor*

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## Looking Ahead

In recessionary times, investors tend to move money into "defensive" stocks — companies with products that enjoy a steady, if unspectacular, stream of demand and that consumers are unlikely to forgo when paring their spending. Consumer staples and, to a lesser extent, the packaging companies that supply them are typical defensive plays. Learn more in the March 25 issue of *The Outlook*.

Please see page 3 for required research analyst certification disclosures.

For important regulatory information, please go to: www.standardandpoors.com and click on "Regulatory Disclosures."

# Synchronized Sinking

*Standard & Poor's provides a global economic overview.*

**Beth Ann Bovino**
Senior Economist

A year ago, we thought most economies around the world were better positioned to withstand a U.S. recession than is now the case.

But with a few exceptions, the recession in the United States spread to its global neighbors. Although the rise of Asia and an improving picture elsewhere reduced overall dependence on the United States as the leader for global growth, the United States remains a key part of the global economic equation. More importantly, the financial system problems that led to the U.S. recession were far more widespread than what we calculated a year ago. Therefore, we believe growth in most emerging and developing economies will decelerate sharply as the developed world slides further into recession.

The question for 2009 no longer concerns whether the world can escape a deep U.S. recession. What everyone wants to know now is: With so many countries sinking into recession at the same time, how severe will this global downturn become and how long will it last?

Domestic demand and regional strength largely determine how other economies fare during a U.S. slump. In particular, many industrialized countries have yet to get a boost from government stimulus programs. And a drop in commodities prices hurts the countries that rely on natural-resource exports. The decline in oil prices helps consumers but hurts OPEC and other oil-exporting countries.

This recession is the most synchronized in history and seems likely to turn into the deepest downturn in the industrial countries since the Great Depression of the 1930s. It comes after an unprecedented period of world economic growth, making the contrast even more severe. We expect the recession to be long and deep. The United States, which entered into recession slightly ahead of its peers, is also likely to emerge first, but we think not until late in 2009.

The European downturn will

(Continued on page 9)

REAL ANNUAL GDP GROWTH

| *(% change from a year earlier)* | 2008 | 2009E | 2010E | 2011E |
|---|---|---|---|---|
| World | 2.3 | -1.2 | 2.3 | 3.8 |
| U.S. | 1.1 | -3.0 | 1.8 | 3.1 |
| Canada | 0.5 | -1.5 | 2.0 | 3.0 |
| U.K. | 0.7 | -3.1 | 0.9 | 1.9 |
| Emerging Europe | 4.4 | -0.9 | 2.1 | 3.5 |
| Eurozone | 0.8 | -2.7 | 0.8 | 1.6 |
| Australia | 2.3 | -0.1 | 1.9 | 3.5 |
| China | 9.0 | 6.5 | 7.0 | 8.5 |
| India | 7.4 | 6.0 | 7.3 | 8.0 |
| Japan | -0.7 | -4.0 | 1.5 | 2.2 |
| Asia-Pacific (excluding Japan) | 5.9 | 3.5 | 6.1 | 7.5 |
| Latin America (weighted by GDP share) | 4.6 | 0.7 | 2.5 | 3.5 |

E-Estimated. Sources: S&P Economics, Global Insight.

# Intelligencer

*Headlines, Highlights, and What's on Our Minds*

**RECESSION VS. DEPRESSION:** While most economists continue to tiptoe around the word "depression," especially in describing the world today, Efraim Levy, a Standard & Poor's equity analyst, is more forthright in describing the automotive industry. "We are in an automotive depression that is being exacerbated by 'The Great Recession,' as shell-shocked consumers, fearful for their jobs, the value of their homes, and stock market assets, are wary of making sizable discretionary investments in buying new vehicles," he opines. "We don't foresee an uptick in industry demand before the fourth quarter at the earliest." Sure enough, February light vehicle volumes at General Motors (GM 2 ★★) fell a precipitous 53% (51% adjusted for one less day). Is there a bright spot on the horizon? Levy expects the government stimulus to have a positive impact on automotive sales in 2010. / Beth Piskora

**HOLDING PATTERN:** Flight delays at JFK, La Guardia, and Newark airports are projected to cost the New York tri-state region's economy $79 billion between 2008 and 2025, says a report by the Partnership for New York City. Airline industry losses in fuel and staffing costs were estimated at $834 million in 2008 and a total of $25 billion over the next 18 years. Shipping companies that use passenger and freight aircraft lost about $136 million in 2008, and are expected to lose about $4 billion between 2008 and 2025. This could have negative implications for companies like Forward Air (FWRD 10 ★), Pinnacle Airlines (PNCL 1 ★★★), and SkyWest (SKYW 10 ★★). / Arthur Epstein

**AN UNUSUAL TREND:** Gold and the dollar have been moving in lockstep for a while now, surprising S&P's short-term technical analyst, Chris Burba. "This is unprecedented and looks unsustainable," Burba says. Gold, historically, has been used as a hedge against a falling dollar, making the current pattern of gold and the dollar moving higher together extremely unusual. "Something's gotta give," says Burba, "and one of them has to turn down. My bet would be the dollar goes down." Readers who agree may consider investing in PowerShares DB U.S Dollar Index Bearish ETF (UDN). / Beth Piskora

## MARKET MEASURES

| INDEX | CLOSE WED. 3/11/2009 | % CHG. YEAR TO DATE | % CHG. PAST 52 WKS. | ‡OPERATING —EARNINGS— E2008 | E2009 | †P/E RATIO | INDICATED ANNUAL DIVIDEND | % YIELD |
|---|---|---|---|---|---|---|---|---|
| S&P 500 Composite | 721.36 | -20.1 | -45.9 | 49.50 | 63.74 | 11.32 | 24.24 | 3.36 |
| S&P MidCap 400 | 434.27 | -19.3 | -45.0 | 30.38 | 37.34 | 11.63 | 10.96 | 2.52 |
| S&P SmallCap 600 | 194.09 | -27.8 | -46.5 | 10.09 | 13.90 | 13.96 | 4.22 | 2.17 |
| S&P SuperComposite 1500 | 163.21 | -20.4 | -45.9 | 11.12 | 14.30 | 11.41 | 5.32 | 3.26 |
| Dow Jones Industrials | 6930.40 | -21.0 | -43.4 | 462.49 | 479.85 | 14.44 | 279.95 | 4.04 |
| Nasdaq Composite | 1371.64 | -13.0 | -39.7 | ... | ... | ... | ... | ... |
| S&P Global 1200 | 816.10 | -20.6 | -49.3 | ... | ... | ... | ... | ... |
| BBB Indus. Bond Yield (10-yr.) | 9.33 | 0.20 ◊ | 2.51 ◊ | | | ... | ... | ... |

Data through March 11. E-Estimated. †Based on estimated 2009 earnings. ‡Before special factors. ◊Actual change in yield (not percentage change).

**For even more market intelligence, visit www.outlook.standardandpoors.com.**

Standard & Poor's The Outlook

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The McGraw-Hill Companies

## S&P EVALUATION SYMBOLS

### STARS Rankings*

Our evaluation of the 12-month potential of stocks is indicated by STARS:

- ★★★★★ **Strong Buy**—Total return is expected to outperform the total return of a relevant benchmark by a wide margin over the coming 12 months, with shares rising in price on an absolute basis.
- ★★★★ **Buy**—Total return is expected to outperform the total return of a relevant benchmark over the coming 12 months, with shares rising in price on an absolute basis.
- ★★★ **Hold**—Total return is expected to closely approximate the total return of a relevant benchmark over the coming 12 months, with shares generally rising in price on an absolute basis.
- ★★ **Sell**—Total return is expected to underperform the total return of a relevant benchmark over the coming 12 months, and the share price is not anticipated to show a gain.
- ★ **Strong Sell**—Total return is expected to underperform the total return of a relevant benchmark by a wide margin over the coming 12 months, with shares falling in price on an absolute basis.
- **NR Not ranked.**

*The fund and ETF STARS rankings come from S&P's mutual fund reports.

### Quality Rankings (QR)

Our appraisals of the growth and stability of earnings and dividends over the past 10 years for STARS and other companies are indicated by Quality Rankings:

| | | | | | |
|---|---|---|---|---|---|
| **A+** | Highest | **B+** | Average | **C** | Lowest |
| **A** | High | **B** | Below Avg. | **D** | In reorganization |
| **A-** | Above Avg. | **B-** | Lower | **NR** | Not Ranked |

Quality Rankings are not intended to predict stock price movements.

# The Observatory

*Selected actions for March 6 through March 13.*

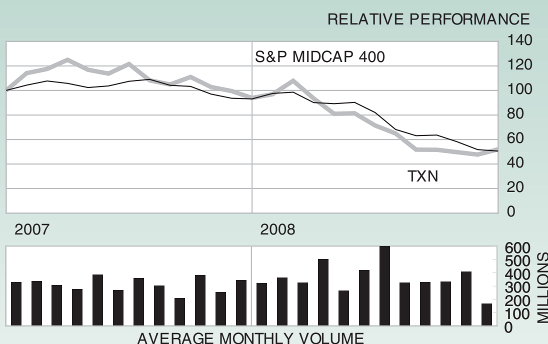
## One to Watch

**Texas Instruments** TXN 16

To ★★★ From ★★

Texas Instruments narrowed its first-quarter earnings forecast, and now expects sales of $1.79 billion to $2.05 billion and a loss per share of $0.08 to breakeven. The new estimates reflect healthy China 3G-related sales. We widened our first-quarter loss estimate by $0.01 to $0.06 on a larger-than-expected restructuring charge estimate of $80 million. But with sales above our view, and the company cutting costs at an aggressive pace, we pared our 2009 loss estimate by $0.05 to a $0.01 loss on higher margin assumptions. Consequently, we raised our 12-month target price by $2 to $15, and now view these shares as fairly priced. ■

**TEXAS INSTRUMENTS** (TXN)




## RISING STARS

**Oracle** ORCL 15

To ★★★★★ From ★★★★

We expect sales growth to weaken in the second half of fiscal 2009 (ending May), given the weakening global economy and negative foreign exchange translations. We expect licenses to be weak, but we think Oracle's wide-margin maintenance streams are more resilient in this environment. We expect tight discipline on costs and expect operating margins to widen in fiscal 2009 and fiscal 2010. We trimmed our fiscal 2009 operating earnings estimate by $0.04 to $1.35 a share and the fiscal 2010 forecast by $0.08 to $1.42. We also cut our target price by $1 to $18, using relative and intrinsic measures. But after a recent decline, we find the shares' valuation compelling.

## FALLING STARS

**Charles Schwab** SCHW 13

To ★★ From ★★★★

Our downgrade reflects fundamentals and valuation. We expect trading volumes to decline through 2009, as we think retail investors will become more risk-averse in the market. Also, with interest rates likely to remain close to zero, we think Schwab's money market-fee income will decline. Lastly, we think asset-based fees could decline should the overall market not recover this year. We lowered our 2009 earnings estimate by $0.25 to $0.70 a share, and we halved our target price to $9, 13 times our 2009 estimate, a below-historical premium to peers.

**Forest Labs** FRX 20

To ★★★ From ★★★★

After consulting with the FDA, Forest Labs expects additional clinical studies will be needed for aclidinium bromide treatment for COPD. The company also expects to delay the launch of recently approved Savella for fibromyalgia to mid-year to obtain approval for a minor formulation change. While we still see promise for these pipeline products, the delays tempered our enthusiasm. Also, the Justice Department charged Forest with marketing drugs for unapproved uses. To reflect revisions in our discounted cash-flow model, we cut our 12-month target price by $9 to $24.

## MASTER LIST CHANGES

Standard & Poor's Portfolio Committee made two changes to its High-Quality Capital Appreciation Portfolio, effective after the market close on March 16. Hudson City Bancorp (HCBK 10 ★★★★★) replaces General Dynamics (GD 36 ★★★), and Church & Dwight (CHD 47 ★★★★) replaces Molson Coors Brewing (TAP 33 ★★★★). In the Small/Mid-Cap Growth Portfolio, Hot Topic (HOTT 9 ★★★★★) replaces Swift Energy (SFY 5 ★★★). ■

**For more STARS, visit www.outlook.standardandpoors.com and for daily STARS changes, call our hotline at 800-618-7827, access #73251.**

S&P Observatory provides a selection of analytical actions and commentary — upgrades, downgrades, initiations — from S&P Equity Research. Stocks featured in S&P Observatory are selected by *The Outlook* according to factors including, but not limited to, newsworthiness, capitalization, and inclusion in a portfolio published by *The Outlook*. Please note that all investments carry risks. Specific risks to each stock recommendation and target price can be found in each company's individual stock report. For a rolling eight-day list of STARS changes, additions, and deletions by S&P Equity Research, please visit our website.

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# Canadian Bank Stocks Suffer

*As the economy goes, so goes the banking sector.*

**Justin Menza**
S&P Editorial
**Erik Oja**
S&P Equity Analyst

Although Standard & Poor's considers the Canadian banking system as one of the soundest in the world, given the banks' fairly high capital ratios and their ability to maintain profitability, investors took money out of the country's bank stocks in recent months as the near-term outlook for the domestic economy deteriorated.

Nearly 80% of all goods exported from Canada head to the United States, making the Canadian economy highly sensitive to changes in the health of the U.S. economy and the U.S. dollar/Canadian dollar exchange rate. Over the past several years, the Canadian dollar appreciated about 50%, which undermined the country's export competitiveness. The Canadian dollar pulled back from its November 2007 peak over the course of 2008 as commodity prices retreated.

S&P Economics forecasts the U.S. economy will contract 3.0% in 2009, and expects a 1.5% contraction in Canadian gross domestic product (GDP) this year following a 0.5% increase in 2008. However, S&P Economics predicts 2.0% growth in 2010 and a 3.0% expansion in 2011, provided the U.S. economy revives.

Part of the current economic weakness in Canada can likely be attributed to the sharp drop in the price of oil from its July 2008 peak and weaker demand from the United States. Energy makes up about 7.1% of Canada's GDP, according to Global Insight, with about two-thirds of crude oil production heading to the United States.

Another factor weighing on the Canadian economy is the country's heavy dependence on the timber industry (about 3.5% of GDP), which is tightly linked to the U.S. housing market. U.S. housing starts dropped 16.8% in January to a record-low annual rate of 466,000. Canadian housing starts also got off to a bad start in 2009, falling to an annual rate of 153,500 in January from 172,200 in December.

The auto industry represents another risk for the Canadian economy. Canada is the seventh-largest auto producer in the world, and its auto industry is highly dependent on the big three U.S. auto manufacturers. The auto industry also accounts for a greater part of the Canadian economy than it does in the United States. Both the United States and Canadian governments provided bailout funds for General Motors (GM 2 ★★) and Chrysler, which are suffering from weak demand for new vehicles during the recession in the United States and elsewhere.

Although the economic outlook is deteriorating, S&P International Equity Strategist Alec Young is more positive on the broader equity markets.

"We believe commodity-sensitive markets like Canada, where earnings per share have seen some of the biggest negative revisions, are beginning to look appealing on a relative basis," he says. "As a result of a 60% weighting in the combined energy and materials sectors, the market's profits and performance are highly leveraged to raw material prices."

Young notes that the global recession's toll on raw material demand has been well-chronicled in the media, which increased "the odds, in our view, that (any concerns about raw material demand) is now largely discounted in extremely depressed commodity prices."

Young adds that while a further drop in commodity prices could occur, he does expect raw material prices to be a positive contributor to earnings "before long."

"Our conviction is due in part to the much larger drop in commodity prices than equities in reaction to the global recession," Young says.

Based on expectations for reduced global oil supply additions, combined with a sharper than expected drop in December and January oil prices, we think there will be a rebound in prices. On March 12, S&P Equity Research trimmed its average 2009 West Texas Intermediate oil price forecast by $0.37 to $39.94 per barrel and 2010's by $1.95 to $50.86.

As mentioned, the fallout from the global credit crisis has taken its toll on Canadian bank stocks. The global credit crisis froze the Canadian wholesale funding markets, which undermined the orderly functioning of the domestic financial system. In response, the Bank of Canada, the country's equivalent to the U.S. Federal Reserve, expanded its liquidity arrangements with the financial industry.

To date, the Canadian banking industry hasn't required government capital due to the banks'

## S&P RECOMMENDATIONS

| COMPANY | TICKER | ‡QUALITY RANKING |
|---|---|---|
| **POSITIVE POTENTIAL IMPLICATIONS** | | |
| Royal Bank of Canada | RY | A |
| **NEGATIVE POTENTIAL IMPLICATIONS** | | |
| Bank of Montreal | BMO | B+ |
| Canadian Imperial Bank of Commerce | CM | B |
| *National Bank of Canada | NA.C | A- |
| Bank of Nova Scotia | BNS | A |
| Toronto-Dominion Bank | TD | B |

*Trades on the Toronto Stock Exchange. ‡See definitions on page 2.
Source: S&P Equity Research.

stringent capital requirements, lower exposure to asset-backed securities, and more conservative lending practices.

Fiscal first-quarter (ending January) results at the six Canadian banks S&P covers were better than expected. Generally steady results in Canadian banking, wealth management, and insurance were enough to offset the losses most of the firms incurred in their international banking divisions. All six banks remained solidly profitable for the quarter, including Canadian Imperial Bank of Commerce (CIBC), which, in the first and second fiscal quarters of 2008, reported large losses on securities and trading.

Canadian banking results for four of the six banks were solid. In the fiscal first quarter, the Canadian retail banking divisions at Bank of Nova Scotia (BNS), Bank of Montreal (BMO), National Bank of Canada, and Royal Bank of Canada (RBC) reported net interest income growth of 15.6%, 7.0%, 4.1%, and 1.8%, respectively, compared with the year-ago quarter.

Despite increased provisions for credit losses, net income in BNS's, BMO's, National Bank of Canada's, and RBC's Canadian divisions grew 17.4%, 12.0%, 5.3%, and 3.4%, respectively.

However, Toronto-Dominion's Canadian division reported a 2.0% decline in net income from a year ago on higher loan loss provisions. In addition, CIBC's retail division, which includes both Canadian and U.S. operations, reported a decline of 14.8% in net income on flat revenues combined with a large increase in loan loss provisions.

We have a buy recommendation on RBC shares. We think RBC's ability to generate non-interest income will help carry it through the current economic slowdown. In the last fiscal year ended October 31, RBC generated nearly $12.2 billion of fee income, including insurance premiums, totaling 56.3% of revenues, and these figures tower over RBC's Canadian peers. ■

# Leaner Times Ahead

**Loran Braverman**
S&P Equity Analyst

*Obesity is a growing problem around the world.*

At a recent investor meeting, the CEO of Weight Watchers International (WTW 18 ★★★★) said, "Obesity is the evil twin of affluence."

We know that he was referring to the tendency, in general, for people to eat more (and get less exercise) as their financial situation improves. To this end, Weight Watchers entered into a joint-venture in China to set up weight-loss centers, as the growing middle class in that country begins to obsess about their growing waistlines.

In western countries, obesity is an ever-worsening problem. The incidence rose to 52% from 37% in Australia, to 58% from 40% in the United Kingdom, and to 42% from 35% in France. In the United States, it rose to 66% from 56%.

We got to wondering if the corollary might be true: Is healthy weight the good twin of hard economic times? While we have no scientific studies to cite that specifically address this issue, there are many studies that show the difficulty people have in losing pounds and then, even more so, in maintaining the weight loss. Although the recession led to weak restaurant industry sales and to trading down in purchases at supermarkets, in the United States, much of the lower-priced foods or restaurant selections are calorie-packed, or energy-dense to use the new terminology. We speculate that the number of people who lose weight when they're stressed is much smaller than the number who overeat when stressed.

Investors pummeled shares of both Weight Watchers and Herbalife (HLF 13 ★★★★) in 2009. Through March 5, 2009, Weight Watchers fell 34% and Herbalife 41% compared with a decline of 24% for the S&P 500. While we have certainly seen some impact from the recession in the United States and many major international markets on the underlying growth of these companies, most of our recent downward earnings revisions came from changes to our foreign currency translation assumptions.

Weight Watchers derives most of its revenues from North America, but the United Kingdom is its second-largest market and the U.K. currency was particularly weak versus the dollar. We estimate that foreign currency translation will negatively affect Weight Watchers by about $0.18 a share in 2009, on our full-year, per-share profit estimate of $2.58.

Herbalife derives about 80% of its segment operating profits from outside the United States. We estimate the negative foreign currency effect on Herbalife's profits in 2009 will be greater than $1.00 a share compared with our full-year, per-share earnings estimate of $2.81. Approximately 63% of Herbalife's 2008 sales were categorized as weight-management products. ■

# Bright STARS

*These stocks have a high IQ.*

**Beth Piskora**
Managing Editor
S&P Editorial

What is your portfolio's IQ?

That's not "Intelligence Quotient," as some may think, but "Investability Quotient." Specifically, the IQ is a proprietary Standard & Poor's measure of investment desirability. The IQ serves as an indicator of potential medium- to long-term return and as a caution against downside risk. It takes into account variables such as technical indicators, earnings estimates, and liquidity. For stocks, the IQ can range from 0 to 250.

This week's screen identifies all recommended stocks — those with four- or five-STARS rankings — that also have an IQ of 200 or higher (see table).

Two of the stocks — International Business Machines and Johnson & Johnson — are repeats from the last time *The Outlook* published this screen on February 13, 2008. Although Quality Ranking was not a parameter in this screen, we note that all the stocks listed in the table have an above-average Quality Ranking of A- or better, another indication of protection against downside risk. An above-average Quality Ranking is awarded only to stocks that showed above-average growth and stability in earnings and dividends over the past 10 years. ■

## STOCK SCREEN OF THE WEEK

| COMPANY / TICKER | ‡STARS | ‡QUALITY RANKING | *RISK | STYLE | CURRENT PRICE | **12-MONTH TARGET PRICE | †P/E RATIO | YIELD (%) | IQ NUMBER |
|---|---|---|---|---|---|---|---|---|---|
| Archer-Daniels-Midland / ADM | 4 | A+ | Medium | Blend | 27 | 34 | 6.6 | 2.1 | 218 |
| ● Becton, Dickinson / BDX | 4 | A | Medium | Growth | 62 | 82 | 12.7 | 2.1 | 214 |
| ● Bard (C.R.) / BCR | 5 | A | Medium | Growth | 71 | 96 | 14.1 | 0.9 | 212 |
| ● Chevron / CVX | 5 | A- | Low | Blend | 61 | 95 | 8.3 | 4.3 | 205 |
| ● Church & Dwight / CHD | 4 | A+ | Low | Growth | 47 | 60 | 14.6 | 0.8 | 200 |
| Colgate-Palmolive / CL | 5 | A+ | Low | Growth | 56 | 76 | 13.2 | 3.1 | 216 |
| Ecolab / ECL | 4 | A+ | Low | Growth | 31 | 40 | 15.5 | 1.8 | 204 |
| ● Int'l Business Machines / IBM | 5 | A | Medium | Growth | 89 | 120 | 9.6 | 2.2 | 205 |
| ● Johnson & Johnson / JNJ | 4 | A+ | Low | Growth | 48 | 65 | 10.7 | 3.8 | 221 |
| Northern Trust / NTRS | 4 | A- | Low | Growth | 55 | 63 | 14.0 | 2.0 | 208 |
| 3M / MMM | 4 | A+ | Low | Growth | 47 | 62 | 10.5 | 4.3 | 214 |
| ● United Technologies / UTX | 4 | A+ | Low | Growth | 41 | 55 | 9.6 | 3.8 | 203 |
| ● Wal-Mart Stores / WMT | 5 | A+ | Low | Blend | 47 | 59 | 13.1 | 2.3 | 214 |

●Master List issue. *Based on our analysts' assessment of qualitative factors, including financial strength, potential share volatility, competitive position, industry cyclicality, regulatory/legal issues, and other factors. **Please note that all investments carry risks. Specific risks to each stock recommendation and target price can be found in each company's individual stock report. ‡See definitions on page 2. †Based on S&P estimated fiscal 2009 earnings. Source: S&P Equity Research.

# Apartment REITs under Pressure

*We changed our view on this industry.*

**Royal Shepard**
S&P Equity Analyst

Until recently, the general market consensus was that apartment operators could benefit from the nation's housing slump. The U.S. Census Bureau puts the nation's fourth-quarter homeownership rate at 67.5%, the lowest level since early 2001. That statistic doesn't tell the whole story, however, and we have changed our outlook to negative from neutral in light of recent data.

An excess supply of new construction in recent years pushed housing inventories to record levels. And, as existing home sales slow, many of these houses went up for rent. In our opinion, it has become readily apparent that an excess supply of housing inventories is hurting the apartment sector. The impact is more severe, in our view, in overbuilt markets and particularly in Sunbelt metropolitan regions such as Phoenix and South Florida.

A review of apartment real estate investment trusts (REITs) shows average fourth-quarter occupancy still high at about 94.7%, but down about 20 basis points from a year ago and a steeper 60 basis points from the third-quarter 2008 average. Rental rates increased a meager 1.3%, on average, during the final period last year as landlords struggled for pricing power. We foresee average rental rate declines on new leases of about 3% to 5%.

We have a strong sell recommendation on Post Properties (PPS 11 ★) and sell recommendations on Avalon Bay Communities (AVB 47 ★★), BRE Properties (BRE 21 ★★), Camden Property Trust (CPT 21 ★★), and Equity Residential (EQR 20 ★★). ■

J.D. Powers & Associates

# Identity Theft

*The $60 billion heist.*

According to U.S. Department of Justice statistics, identity theft will soon replace drug trafficking as the Number One crime in the nation.

In fact, every 60 seconds, more than 28 people become a victim of identity theft, costing companies an estimated $56.6 billion annually. Many consumers, in fact, aren't even aware that they've been a victim of identity theft. For some, it's a phone call from a collection agency trying to collect a delinquent debt. For others, it's being denied credit or even being approved for credit that wasn't applied for. But no matter the cause or how it is discovered, for the victim, identity theft typically leads to many lost hours of work and sleep dealing with creditors to clean up the mess and restore accounts.

While the Internet and cell phones have evolved and made it easier for many consumers to communicate, conduct business, and handle personal finances online or over the airwaves, these same technologies provide even greater opportunities for identity theft.

The traditional methods of identity theft are still practiced — stolen wallets, bank account numbers, and health insurance information; dumpster diving; and mail fraud — but are quickly being replaced by online threats such as e-mail scams and "phishing," which is the process of attempting to acquire sensitive information such as user names, passwords, and credit card numbers by pretending to be a reputable entity to solicit and steal data. Also, as more consumers use their cell phones to store personal information, check e-mail, and even pay bills, a lost or stolen cell phone can be a major headache instead of a minor inconvenience.

To learn more about this growing threat, J.D. Power's Web Intelligence Division has researched the subject to discover that there is much to learn about consumer attitudes and behaviors pertaining to identity theft. According to the J.D. Power Web Intelligence Identity Theft Report, younger consumers — in particular people considered to be part of Generation Y— tend to be at a higher risk for identity theft but are less concerned with the threat than consumers in the Generation X and Baby Boomer demographic groups.

Carter Truong, senior manager at J.D. Power Web Intelligence, explains: "Younger consumers tend to be more tech-savvy than older consumers, which gives them several benefits in protecting against identity theft. For example, their personal computers tend to be better protected and they're more likely to recognize — and avoid — phishing scams than older generations. However, younger consumers also tend to have more of a presence online, leaving them open to more chances for identity theft."

To help protect against identity theft, here are some things consumers can do:

**Face your Facebook**. As social networking sites like LinkedIn, Facebook, and MySpace increase in popularity, the Identity Theft Report identifies these sites as a hot spot for ID theft, as many online posters are unwilling to sacrifice self-expression to stay safe. For your own safety, ensure that social networking pages don't contain more information than you feel comfortable with someone easily accessing, and utilize any available privacy settings provided by the site.

**Don't dread it, shred it.** Dumpster diving, while not nearly as sophisticated as online phishing scams, is still a commonly used tactic among identity thieves. To help protect against this, you should minimize putting sensitive information in volatile situations by buying and using a paper shredder. Also, don't keep important documents, account or PIN numbers in your wallet or purse in case it gets lost or stolen.

**Be smart with your smartphone.** As cell phones, MP3 players, and portable gaming devices become increasingly multi-functional, consumers need to ensure that these devices are equipped with security functions to protect sensitive information. This is especially important with smartphones, which consumers frequently use to conduct mobile banking transactions and for browsing the Internet.

**Know your own finances.** Consumers should check their credit report regularly. The three major credit reporting agencies — Equifax, Experian, and TransUnion — when requested by consumers, are required by law to provide a free credit report once each year. And, rest assured that checking your own credit report will not negatively affect your credit, or FICO, score. Also, regularly check bank and credit card transactions for fraudulent charges.

**Don't be afraid to ask for help.** For those who don't have the time or knowledge to thoroughly protect themselves from identity theft, companies such as LifeLock, Equifax, and Debix can monitor a consumer's financial activity for a minimal monthly fee.

For more information, visit *www.jdpower.com*. J.D. Powers & Associates is part of the McGraw-Hill family of companies, as is Standard & Poor's. The two businesses operate independently of each other. ■

# Crushing Correlation

**Alec Young**
International Equity Strategist

*Rising equity correlation undermines portfolio diversification.*

Amid the worldwide stock market plunge, already historically elevated global equity correlations moved even higher, as all markets converged aggressively to the downside.

As a result, the benefits of equity portfolio diversification have all but evaporated, magnifying investor losses. There has been nowhere to hide within any geographic, size, or style category. Through March 10, the vast majority of worldwide equity asset classes fell at least 50% from their peak (with most down more than 60%).

Given the global nature of the current economic and earnings contraction, the broad-based equity fallout is understandable, in our view. In terms of a silver lining, while rising global equity correlation has amplified losses, we believe it is also likely to boost gains since we think markets will recover in unison. Over time, this should provide investors with some relief, by our analysis.

60-MONTH CORRELATIONS

| | S&P 500 | MC 400 | SC 600 | EAFE | EM | FRONTIER | WORLD SMID EX U.S. |
|---|---|---|---|---|---|---|---|
| S&P 500 | 1.00 | 0.95 | 0.89 | 0.89 | 0.79 | 0.85 | 0.87 |
| MC 400 | 0.95 | 1.00 | 0.92 | 0.89 | 0.81 | 0.60 | 0.87 |
| SC 600 | 0.89 | 0.92 | 1.00 | 0.80 | 0.70 | 0.44 | 0.79 |
| EAFE | 0.89 | 0.89 | 0.80 | 1.00 | 0.91 | 0.57 | 0.95 |
| EM | 0.79 | 0.81 | 0.70 | 0.91 | 1.00 | 0.55 | 0.91 |
| Frontier | 0.85 | 0.60 | 0.44 | 0.57 | 0.55 | 1.00 | 0.81 |
| World ex-U.S. SMID | 0.87 | 0.87 | 0.79 | 0.95 | 0.91 | 0.81 | 1.00 |

Sources: Standard & Poor's, MSCI (through 2/27).

The MSCI EAFE index, a developed international equity benchmark, is now moving in unison with the S&P 500 index 89% of the time vs. 80% in August 2008. Similarly, the MSCI Emerging Markets index's correlation to the 500 jumped to 79% in February from 68% last August. Worse yet, the MSCI Frontier Market index, long touted for its ability to "zig" when the S&P 500 "zags," has seen its 500 correlation soar to 85% from a mere 9% in August.

Smaller-cap stocks offer no refuge. The S&P MidCap 400 index is now moving in lockstep with the 500 95% of the time up from 89% last August. Likewise, the S&P SmallCap 600 index's correlation to the "500" shot up to 89% in February from 83% in August. Looking overseas, the correlation between the MSCI World ex-U.S. Small & Mid Cap index and the 500 rose to 87% from 74% over the same period. ■

# Frugality is the New Chic

**Beth Piskora**
Managing Editor
S&P Editorial

*Some stocks are benefiting from the trend.*

Look at the top performers since Barack Obama was elected president (about four months), and you'll notice an interesting trend.

American Italian Pasta (AIPC 30 NR) rose 34% through March 11 and Netflix (NFLX 37 NR) gained 24 %.

"People are staying home: They are eating at home and they are watching movies at home," explains Richard Peterson, a research director in Standard & Poor's Market, Credit, and Risk Strategies Group, which operates independently from S&P Equity Research.

Stephen Biggar, head of S&P's global equity research, agrees, pointing out that many American households are searching for ways to be more frugal without feeling like they are being deprived.

To this end, the Biggar-led S&P Portfolio Committee positioned the Top Ten Portfolio for this new parsimony. The committee most recently added Advanced Auto Parts (AAP 39 ★★★★★) on the belief that many consumers will repair their existing cars rather than buy new ones.

Family Dollar Stores (FDO 31 ★★★★★) is another Top Ten component based on the fact that consumers are seeking better bargains when they shop. McDonald's (MCD 51 ★★★★★) benefited in recent months from an uptick in sales, as consumers traded down from pricier restaurants. And General Mills (GIS 49 ★★★★★), like American Italian Pasta, is benefiting from eat-at-home trends. ■

## Synchronized Sinking *(Continued from cover)*

be similar to the U.S. recession in depth but will likely be more protracted, in part because European economies are not fully synchronized. We think Japan's recession will be the deepest of the major industrial countries and possibly the longest because of its dependence on exports as an engine of growth.

Emerging Asia is in the best shape of the major regions. China is suffering because of the reduced demand for its goods in the industrial world, particularly in the United States, but by increasing infrastructure spending and spurring domestic consumption, it should be able to rely on domestic demand.

India is less export-sensitive than China but also has less room for fiscal stimulus because of the continuing budget problems it faces. Both countries are less dependent on external finance than in the past, which should keep them relatively immune from the financial problems.

Latin America, Africa, and the Middle East were immune from the recession through mid-2008 because of strong commodity prices. However, the recent plunge in these prices, particularly for crude oil, is now extending the recession to these regions as well. They might suffer the most because they have less room to substitute domestically generated growth for exports. These were the last regions to enter recession and are likely to be the last to emerge from it.

### Where is the United States heading?

Standard & Poor's expects that gross domestic product (GDP) will fall for four consecutive quarters, starting with the third quarter of 2008 through the second quarter of 2009. We now expect a peak-to-trough drop in real GDP of about 3.9%.

We expect GDP to fall 3.0% this year, much worse than the 1.1% increase in 2008. GDP will likely improve by a modest 1.8% in 2010. Housing will likely keep pressure on expansion through early 2010. Housing starts and sales are expected to hit bottom this spring — but improve very little through 2009. Home prices aren't likely to hit a trough until early 2010.

Business conditions could continue to erode, which would likely translate into a larger contraction than what we currently expect for 2009 and result in increased weakness abroad. However, our longer-term outlook remains upbeat, with growth possibly returning to more than 3% by 2011.

We've said that we think credit markets must thaw for the U.S. economy to recover. Unfortunately, they remain relatively frozen. However, some encouraging signs materialized recently, with the Treasury-to-Eurodollar (TED) spread, a measure of banks' willingness to lend, at 98 basis points (bps) and well below the 214-bp spread seen three months ago. However, quality spreads remain wide and lending tight.

To stimulate the market and economy, the Federal Reserve slashed rates and intervened in other markets. The Fed began dealing in Agency securities and intends to continue to do so. It is also buying commercial paper. The early results have been good; mortgage rates dropped to their lowest level of the year.

The Fed made clear that it would employ its balance sheet aggressively to try to free up credit markets and that "all available tools would be employed to promote the resumption of sustainable economic growth and to preserve price stability."

We expect to see more Fed purchases of non-Treasury securities, including, but not limited to, mortgage-backed securities and commercial paper. The programs do seem to be working. Mortgage rates dropped to a record low of 5.1% (30-year conventional), and commercial paper markets have opened up. The London Interbank Offering Rate fell back to 1.4% (three-month), still very high relative to the federal funds rate but far below the 6% it hit three months ago.

However, we are worried about the parallels between the United States today and Japan at the beginning of the 1990s. In both cases, heavy capital losses resulting from property loans constrained the banking system. In Japan, that led to a decade of stagnation, with annual growth averaging 0.8% from 1992 through 2002. Home prices remain 25% below their peak, and the Nikkei stock index is still trading at one-third its level of 20 years ago. Although there are differences, the risk of the United States falling into a Japan-like scenario is frighteningly real.

The U.S. reliance on foreign capital adds more risk. America's current account deficit reached a record of 6.4% of GDP in third-quarter 2006, but it was at a still-high 4.7% in 2008. Private money was almost entirely financing it — at very low interest rates.

Now, foreign investors have lost confidence in most U.S. securities, and money is not so easy to come by. With markets likely to remain tight, we expect the current account deficit to narrow to 2.1% of GDP in 2009. However, for now at least, increased risks abroad have investors sending money into the United States and into the safe haven of Treasuries, strengthening the U.S. dollar and bringing 10-year Treasury yields to 2.91% on March 11, up from the 54-year low of 2.08% on Dec. 18. A rising dollar cuts into U.S. exports and supports the trade surpluses of other U.S. trading partners. But shrinking trade flows also add the risk of protectionist action, which would hurt global growth. ■

# Small/Mid-Cap Growth Portfolio

**12/31/2008— 3/6/2009**
**Base Currency: US Dollar**

The Small/Mid-Cap Growth Portfolio outperformed its benchmark year-to-date in 2009, losing 21.7% vs. a 24.2% loss in the S&P MidCap 400 through March 6. The data we have provided shows which stocks and sectors contributed to, or detracted from, the portfolio's performance through March 6. For information on individual stocks in the portfolio, please visit www.outlook.standardandpoors.com for Standard & Poor's reports on the companies. ■

## TOP CONTRIBUTORS BY HOLDING

| COMPANY NAME | AVERAGE WEIGHT | RETURN | CONTRIBUTION |
|---|---|---|---|
| Family Dollar Stores | 9.67 | 16.46 | 1.44 |
| SBA Communications | 6.48 | 22.49 | 1.06 |
| Icon | 5.00 | -1.42 | -0.20 |
| Superior Energy* | 1.23 | -8.10 | -0.30 |
| PetSmart | 5.71 | -8.53 | -0.51 |

*Replaced on January 20.

## TOP DETRACTORS BY HOLDING

| COMPANY NAME | AVERAGE WEIGHT | RETURN | CONTRIBUTION |
|---|---|---|---|
| Delta Air Lines | 8.81 | -64.57 | -7.27 |
| Titanium Metals* | 3.03 | -24.18 | -2.30 |
| Astec Industries | 6.17 | -33.55 | -2.17 |
| Itron | 4.82 | -27.74 | -1.88 |
| Swift Energy | 2.21 | -69.96 | -1.75 |

*Replaced on January 20.

## TOP CONTRIBUTORS BY SECTOR

| SECTOR | AVERAGE WEIGHT | RETURN | CONTRIBUTION |
|---|---|---|---|
| Telecom Services | 6.48 | 22.49 | 1.06 |
| Consumer Discretionary | 15.38 | 7.05 | 0.93 |
| Consumer Staples | 7.40 | -11.47 | -0.72 |
| Health Care | 15.62 | -19.21 | -2.87 |

## TOP DETRACTORS BY SECTOR

| SECTOR | AVERAGE WEIGHT | RETURN | CONTRIBUTION |
|---|---|---|---|
| Industrials | 14.99 | -52.85 | -9.44 |
| Materials | 11.86 | -28.58 | -4.02 |
| Energy | 7.65 | -47.12 | -3.38 |
| Information Technology | 20.61 | -16.20 | -3.36 |

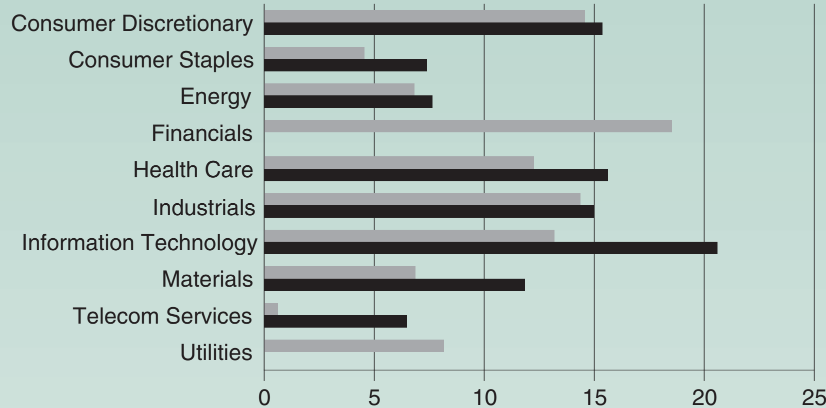
## SMALL/MID-CAP GROWTH PORTFOLIO

| COMPANY / TICKER | ‡STARS | ‡QUALITY RANKING | *RISK | STYLE | CURRENT PRICE | **12-MONTH TARGET PRICE | †P/E RATIO | YIELD (%) |
|---|---|---|---|---|---|---|---|---|
| Amdocs / DOX | 4 | B | Medium | NA | 17 | 23 | 8.9 | Nil |
| Astec Industries / ASTE | 5 | B- | Medium | Blend | 23 | 29 | 9.0 | Nil |
| BJ's Wholesale / BJ | 4 | B | Medium | Blend | 28 | 34 | 12.1 | Nil |
| Covance / CVD | 4 | B+ | Medium | Growth | 35 | 48 | 11.4 | Nil |
| Delta Air Lines / DAL | 4 | NR | High | NA | 5 | 7 | 4.0 | Nil |
| Family Dollar Stores / FDO | 5 | A+ | Medium | Blend | 31 | 35 | 16.1 | 1.7 |
| FMC / FMC | 4 | B- | Medium | Value | 39 | 57 | 8.2 | 1.3 |
| GulfMark Offshore / GLF | 5 | B | Medium | Growth | 17 | 34 | 2.8 | Nil |
| Icon / ICLR | 5 | NR | Medium | NA | 16 | 27 | 10.7 | Nil |
| Itron / ITRI | 5 | B- | Medium | Growth | 47 | 58 | 13.2 | Nil |
| NICE-Systems / NICE | 5 | NR | High | NA | 24 | 27 | 13.7 | Nil |
| Owens & Minor / OMI | 4 | A | Medium | Blend | 31 | 44 | 11.7 | 3.0 |
| PetSmart / PETM | 4 | B | Medium | Growth | 18 | 22 | 12.0 | 0.7 |
| SBA Communications / SBAC | 4 | C | High | Blend | 23 | 27 | NM | Nil |
| Swift Energy / SFY | 3 | C | High | Blend | 5 | 7 | NM | Nil |

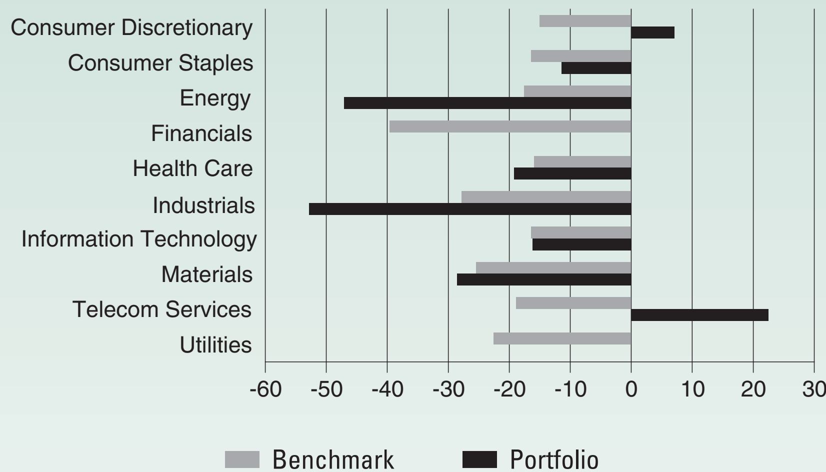
*Based on our analysts' assessment of qualitative factors, including financial strength, potential share volatility, competitive position, industry cyclicality, regulatory/legal issues, and other factors. **Please note that all investments carry risks. Specific risks to each stock recommendation and target price can be found in each company's individual stock report. †Price/earnings ratios are based on Standard & Poor's estimated fiscal 2009 per-share earnings. ‡See definitions on page 2. Past performance is not a valid indicator of future results. Source: S&P Equity Research.

# Small/Mid-Cap Growth Portfolio vs. S&P Mid-Cap 400

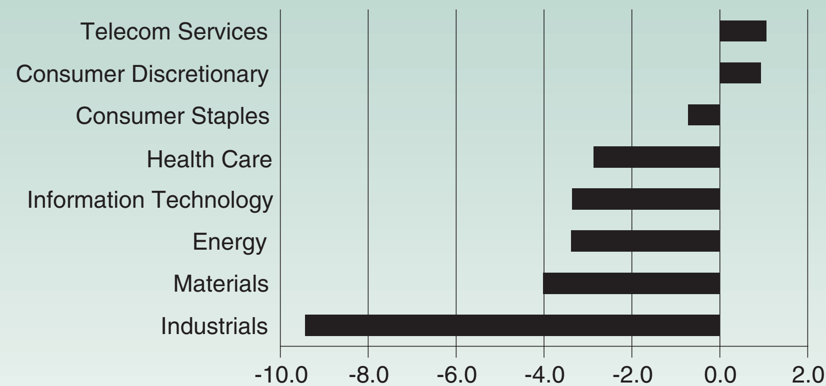
## SECTOR ALLOCATION (%)




## SECTOR RETURNS (%)




## CONTRIBUTION BY SECTOR (%)




Source: S&P Equity Research.

## LARGEST HOLDINGS

| COMPANY NAME | AVERAGE WEIGHT | RETURN |
|---|---|---|
| Family Dollar Stores | 9.67 | 16.46 |
| FMC | 8.83 | -19.67 |
| Delta Air Lines | 8.81 | -64.57 |
| Amdocs | 7.94 | -11.43 |
| NICE-Systems | 7.85 | -7.65 |

## BEST PERFORMERS

| COMPANY NAME | AVERAGE WEIGHT | RETURN |
|---|---|---|
| SBA Communications | 6.48 | 22.49 |
| Family Dollar Stores | 9.67 | 16.46 |
| Icon | 5.00 | -1.42 |
| NICE-Systems | 7.85 | -7.65 |
| Superior Energy* | 1.23 | -8.10 |

*Replaced on January 20.

## WORST PERFORMERS

| COMPANY NAME | AVERAGE WEIGHT | RETURN |
|---|---|---|
| Swift Energy | 2.21 | -69.96 |
| Delta Air Lines | 8.81 | -64.57 |
| Astec Industries | 6.17 | -33.55 |
| GulfMark Offshore | 4.22 | -31.36 |
| Itron | 4.82 | -27.74 |

For more information

on individual stocks in the portfolio,

visit our website

**www.outlook.standardandpoors.com.**

# S&P's Platinum Portfolio

*This portfolio potentially offers the best of both worlds: S&P's STARS ranking system, based on fundamental analysis, and Fair Value, S&P's proprietary quantitative model.*

Each Platinum stock initially carries the highest possible investment ranking from Standard & Poor's equity analysts and our Fair Value system.

S&P's STARS rankings are based on expected total return potential. Stocks with the five-STARS ranking are expected to outperform the total return of the S&P 500 index by a wide margin over the coming 12 months.

S&P's Fair Value model employs a proprietary algorithm to calculate the price at which a stock should be trading at current market levels. Fair Value ranks stocks in five tiers; those with the "5" designation are considered to be the most undervalued and to have the greatest price appreciation potential.

Year-to-date through March 6, the portfolio lost 14.2% vs. a loss of 24.3% for the S&P 500.

Stocks are removed only if they lose the top ranking in both systems. Portfolio changes are available in real time at *www.outlook.standardandpoors.com*. ■

## PLATINUM PORTFOLIO

| | | RANKINGS | | | |
|---|---|---|---|---|---|
| | TICKER | FAIR-VALUE | ‡STARS | ‡QUALITY | CURRENT PRICE |
| Accenture | ACN | 4 | 5 | NR | 29 |
| Aeropostale | ARO | 4 | 5 | NR | 24 |
| ● CVS Caremark | CVS | 4 | 5 | A+ | 25 |
| ● Chevron | CVX | 2 | 5 | A- | 61 |
| ● Chubb | CB | 3 | 5 | A- | 36 |
| Coach | COH | 5 | 5 | NR | 14 |
| Computer Sciences | CSC | 5 | 3 | B+ | 33 |
| ConocoPhillips | COP | 1 | 5 | B | 38 |
| Corning | GLW | 5 | 2 | B | 11 |
| eBay | EBAY | 5 | 4 | B | 12 |
| Express Scripts | ESRX | 5 | 5 | B+ | 45 |
| Fiserv | FISV | 5 | 5 | B+ | 32 |
| Flextronics Int'l | FLEX | 5 | 3 | NR | 2 |
| Google | GOOG | 5 | 5 | NR | 318 |
| ● GulfMark Offshore | GLF | 5 | 5 | B | 17 |
| Harris | HRS | 4 | 5 | B+ | 31 |
| Hewlett-Packard | HPQ | 4 | 5 | B+ | 29 |
| ● Icon | ICLR | 3 | 5 | NR | 16 |
| ● Int'l Business Machines | IBM | 3 | 5 | A | 89 |
| ● NICE-Systems | NICE | 4 | 5 | NR | 24 |
| Noble | NE | 5 | 5 | B | 23 |
| Oracle | ORCL | 5 | 5 | B | 15 |
| St. Jude Medical | STJ | 4 | 5 | B+ | 34 |
| Teva Pharmaceutical | TEVA | 3 | 5 | NR | 43 |
| Thermo Fisher Scientific | TMO | 3 | 5 | B- | 34 |
| Transocean | RIG | 4 | 5 | NR | 53 |
| Viacom | VIA.B | 5 | 2 | NR | 15 |

● Master List issue. ‡See definitions on page 2.

Performance calculations do not take into account reinvestment of dividends, capital gains taxes, or brokerage commissions and fees. If the foregoing had been factored into the portfolio's investment performance, it would have been lower. This performance calculation also does not take into account timing differences between the portfolio selections and purchases made based on those selections by actual investors. Over certain periods, the portfolio incurred losses and over time the portfolio is expected to continue to pose a risk of negative investment returns. Because the portfolio has a high turnover rate, we believe it is best suited for tax-deferred accounts such as IRAs and is less suited for other accounts. Investors should seek financial advice before investing based on the portfolio. This portfolio does not address the specific investment objectives, financial situation, and particular needs of any person. Stocks in the portfolio will not be suitable for all investors. Past performance is not a valid indicator of future results.