STANDARD & POOR'S

The Outlook

Intelligence for the Individual Investor

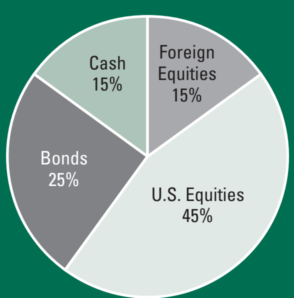
COME VISIT US ONLINE! www.outlook.standardandpoors.com

June 3, 2009
Volume 81
Number 21

What's Inside

Intelligencer	2
Observatory	3
Red Carpet Rollout	4
Drilling for Dólares	6
QR Upgrades	7
ETFs for Cash	8
Master List	10
Neural Fair Value	12

Asset Allocation



Vulnerable Valuations

Too-rich valuations may impede further gains in the cyclical sectors.

Sam Stovall
Chief Investment Strategist

The first-quarter 2009 earnings reporting season is pretty much over. Operating earnings for the S&P 500 dropped 39% year over year, led by a 104% decline for the S&P 500 consumer staples sector, an 83% slide in the consumer discretionary group, and a 75% drop in materials. Through the quarter, however, the S&P 500 index advanced 11.2%.

So what is the reason for the discrepancy? Maybe there wasn't one, when you compare the 39% first-quarter decline with the small operating loss in the fourth quarter of 2008 and the S&P 500's, which was its first loss in history on either an operating or a GAAP basis. Plus, the S&P 500 recorded a 25% decline through March 9 as investors anticipated the worst from first-quarter earnings reports and became convinced the U.S. government would nationalize the U.S. banking system. Neither worry materialized, thus allowing share prices to experience at least a sharp rally within a bear market.

Historically, valuations are low at bear market bottoms, thus allowing for P/E expansion as share prices advance. Since 1937, the median P/E for the S&P 500 at bull market highs was a shade below 19.0 on trailing 12-month GAAP earnings, with only 1980 sporting a peak P/E in the high single-digits and six of the remaining 12 observations recording valuations of 20.0 or higher. At bear market bottoms, however, the median P/E was 12.6 with five of the 13 observations below 10.0 and six more between 11.6 and 15.1. On March 9, the S&P 500's P/E on trailing 12-month GAAP earnings was a whopping

P/E RATIO PEAKS AND TROUGHS

Trailing 12-Month GAAP EPS

END OF BULL	P/E RATIO	END OF BEAR	P/E RATIO
03/06/37	16.8	03/31/38	8.8
11/09/38	21.5	04/28/42	7.6
05/29/46	22.9	06/13/49	5.6
08/02/56	14.4	10/22/57	11.6
12/12/61	22.8	06/27/62	15.1
02/09/66	17.6	10/07/66	13.2
11/29/68	18.8	05/26/70	12.6
01/11/73	17.7	10/03/74	7.0
11/28/80	9.5	08/12/82	7.6
08/25/87	21.2	12/04/87	12.8
07/16/90	17.0	10/11/90	13.8
03/24/00	30.0	10/09/02	28.2
10/09/07	23.6	03/09/09	97.9
Average	18.8	Average	12.6

Past performance is no guarantee of future results. Source: S&P Equity Research.

(Continued on page 8)

Intelligencer

Headlines, Highlights, and What's on Our Minds

PAPER OR PLASTIC — OR GLASS? Quick, what's the most eco-friendly form of packaging? A majority of consumers said glass in one recent survey, citing its 100% reusability. But glass is impractical for many uses. And it's not even the most eco-friendly packaging anyway, despite consumer beliefs.

According to a study conducted by the Institute for Energy and Environmental Research, cardboard cartons are the most environmentally friendly form of packaging. They cut carbon dioxide emissions and fossil fuel consumption by as much as 60% compared with other forms of packaging. The study compared the resource requirement and ecological impact of various packaging materials including cardboard cartons, metal cans, glass jars, and plastic pouches.

It also considered the emissions associated with each form of packaging including carbon dioxide output and its impact on climate, particulate matter emission, eutrophication (or nutrient enrichment), and acidification of soil and natural bodies of water. The researchers studied all aspects of packaging from extraction and processing of raw materials to manufacturing, transport, distribution, and recovery or disposal.

Makers of cardboard containers include Bemis (BMS 24 ★★★), Packaging Corp. of America (PKG 15 ★★★), Rock-Tenn (RKT 38 NR), and Temple-Inland (TIN 12 ★★★★). / Beth Piskora

AIRLINES SEE GREEN: Lacking their own version of the hybrid car or wind turbine, the world's airlines have been mostly left out of the current mania for everything green, organic, and carbon-neutral. JetBlue (JBLU 4 ★★★★★), for example, is asking pilots to use just one engine when taxiing on runways, and it installed energy efficient LED lights on its planes — nice enough but hard to get excited about.

For the past two years, however, the commercial aviation industry has been carefully testing fuel blends that incorporate jet fuel made from coconut oil, jatropha (vegetable oil made from the seeds of a jatropha plant), and even algae. Subsequent reports indicate the renewable biofuels performed as well or sometimes better than petroleum jet fuels, clearing the way for wider use. So, don't be surprised if you find yourself flying on an algae-powered jet a few years from now.

Boeing (BA 44 ★★★) says renewable biofuels could be in widespread use by 2012, when Europe's aviation industry becomes subject to new emissions limits. Air New Zealand, for its part, has a goal of using 10% renewable fuels by 2013, while Virgin Atlantic is targeting 5% by 2015. / Vaughan Scully ■

MARKET MEASURES

INDEX	CLOSE WED. 5/27/2009	% CHG. YEAR TO DATE	% CHG. PAST 52 WKS.	‡OPERATING —EARNINGS— 2008	E2009	†P/E RATIO	INDICATED ANNUAL DIVIDEND	% YIELD
S&P 500 Composite	893.06	-1.1	-35.8	49.51	54.15	16.49	22.68	2.54
S&P MidCap 400	561.90	4.4	-35.1	30.03	28.48	19.73	10.03	1.79
S&P SmallCap 600	259.69	-3.4	-32.5	10.22	14.35	18.10	3.82	1.47
S&P SuperComposite 1500	203.30	-0.8	-35.6	11.12	12.13	16.76	4.97	2.44
Dow Jones Industrials	8300.02	-5.4	-34.1	462.49	357.27	23.23	274.86	3.31
Nasdaq Composite	1731.08	9.8	-29.3	...	...	...	...	...
S&P Global 1200	1061.60	3.2	-38.1	...	...	...	...	...
BBB Indus. Bond Yield (10-yr.)	8.64	-0.49 ◊	1.85 ◊			...	...	...

Data through May 27, 2009. E-Estimated. †Based on estimated 2009 earnings. ‡Before special factors. ◊Actual change in yield (not percentage change).

Standard & Poor's The Outlook

EDITORIAL

Managing Editor, U.S. Editorial Beth Piskora

Managing Editor, The Outlook Lisa Sanders

Statistician Chris Peng

OPERATIONS

Managing Director, Product and Business Development Robert Barriera

Managing Director, Product Development and Marketing Andrea Remyn

Vice President, Global Operations Peter Fiore

Vice President, Data Operations Frank LoVaglio

For customer service, please call **1-800-852-1641** between 9am and 4pm Eastern Time, Monday through Friday.

The Outlook (USPS 415-780, ISSN 0030-7246) is published weekly except for April 15, July 8, September 16, and December 30, 2009 by Standard & Poor's, 55 Water St., New York, NY 10041.

Annual subscription: $298. Periodicals postage paid at New York, NY, and additional mailing offices. Ride along included in all editions. POSTMASTER: Send address changes to *The Outlook*, Standard & Poor's, 55 Water St., New York, NY 10041.

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 May 22 through May 29.

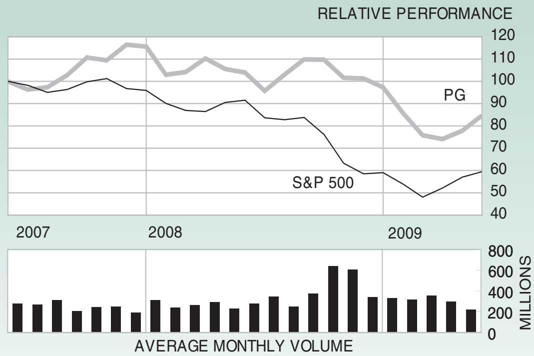
One to Watch

Procter & Gamble PG 52

To ★★★★ From ★★★★★

Long term, we expect Procter & Gamble to benefit from its increasing exposure to developing markets and its emphasis on new products. But based on our growing concerns about worsening economic conditions in Western Europe, and on further inroads in the United States by value brands and private-label goods, we lowered our fiscal 2009 (ending June) earnings estimate on this Master List company by $0.04 to $3.57 a share (excluding a $0.63 gain from the Folgers divestiture) and fiscal 2010's by $0.11 to $3.86 a share. While we expect the foreign-exchange pressure to moderate late in 2009, we also cut our blended discounted cash flow- and P/E-based target price by $5 to $63. ■

PROCTER & GAMBLE (PG)



RISING STARS

Polycom PLCM 17

To ★★★★ From ★★★

We expect Polycom's product demand to benefit from widespread travel-cutting measures at businesses that are trying to lower costs in the weak economic climate. Moreover, we believe the recent swine flu outbreak and its related impact on business travel will spur increased interest in video communication solutions. We also continue to view Polycom as an attractive takeover candidate. On our revised relative analysis, to reflect an improved outlook and a recent expansion in peer multiples, we raised our target price by $5 to $21, which is 17.5 times our 2009 earnings estimate of $1.20 a share.

FALLING STARS

ATC Technology ATAC 15

To ★★★ From ★★★★★

We are concerned about ATC's impending loss of its Honda (7267 Tokyo ★★) automatic transmission remanufacturing business. Assuming a contribution pretax margin of about 7% on annual Honda sales, and taxes at 37.8%, we estimate about a $0.12 annualized earnings per share hit from the lost business starting in 2010. We also expect the company to write down some related assets. We see the operational impact in 2009 as minimal, but with greater uncertainty, we reduced our target P/E to 9.0 times our $1.97 earnings estimate and our target price by $6 to $18. We expect continued stock price volatility.

Staples SPLS 20

To ★★★ From ★★★★

Excluding one-time items, April-quarter earnings of $0.22 a share vs. $0.30 a year ago matched our estimate. While North American retail segment same-store sales declined 8%, better than our projection of a 12% decline, the gross margin in Staples' contract business narrowed modestly on a shift in the product mix. We continue to expect weak business conditions in the near-term, and we maintained our fiscal 2010 (ending January) and fiscal 2011 operating earnings estimates of $1.12 and $1.27 a share. However, factoring in anticipated market share gains over the long term and an improved cost structure, we raised our discounted cash flow-based target price by $2 to $21.

Triumph Group TGI 38

To ★★★ From ★★★★

Following Boeing's (BA 44 ★★★) investor meeting on May 26, we downgraded our opinion, given Triumph's large exposure to the airplane maker. We believe that some of Boeing's customers will have difficulty finding financing in 2010, and we see the risk of production cuts affecting Triumph, whose top two programs currently are Boeing's 777 and 737. We maintained our fiscal 2010 (ending March) earnings estimate of $5.10 a share, but we lowered fiscal 2011's by $0.85 to $5.30. We also reduced our target price by $10 to $42. Nevertheless, we continue to see good prospects for Triumph with military helicopters and the 787. ■

For a rolling eight-day list of STARS changes, additions, and deletions by S&P Equity Research, please visit our website.

Rolling Out the Red Carpet

Hotels try to lure vacationers this summer.

Mark Basham, S&P Equity Analyst

Even as the market's rally and talk of "green shoots" raise hopes that the worst of the recession is behind us, our forecast is that room revenue for domestic hotels will decline 15% from the 2008 summer vacation season.

Hotels are likely to continue to focus on cutting costs, including workforce reductions, to minimize the pressure from lower room demand this summer. Even so, unlike airlines that cut capacity to offset expected declines in travel, hotels do not have the option to mothball rooms like jets parked in the desert. Our sell recommendations on hotel stocks reflect our view that valuations, after the recent rally in certain hotel shares, are not supported by the fundamentals.

From a broad economic perspective, rising unemployment and a weak housing market should undermine hotel room demand this summer travel season. Even though most people still have their jobs and haven't lost their homes, they most likely read or hear about people who have, or even know someone who was laid off or faces foreclosure. And despite the spring rally in the market, most investors were hurt by the market's swoon since last summer.

Moreover, job losses affected nearly every sector of the economy (with the exception of health care and government), and home prices fell in nearly every market across the country. With the primary store of wealth for most Americans declining in value, the housing ATM is largely closed. Coupled with the decline in equities, which most had counted on as the base of their nest egg for retirement, we conclude that many if not most Americans are borrowing less and saving more, and, therefore, will spend less on vacations this summer.

An additional factor we considered in our outlook is that, while the Obama stimulus package is giving a boost to take-home pay, we think the stimulus' effect on summer travel is likely to be less pronounced than the $1,200 rebates per family that many households received as a lump sum heading into last summer. Standard & Poor's Equity Research believes that the stimulus last year may have boosted leisure spending by about 2%, but we expect a significantly smaller impact from the tax stimulus this year.

We expect many of those directly affected by the loss of a job or foreclosure will not vacation this year. For others directly affected who still plan to travel, as well as for everyone else, we generally expect vacations will be spent closer to home, will be slightly shorter, and will be more likely spent with family or friends. For those staying in hotels and other types of lodging, we expect significant trading down to occur.

In our outlook, we divide vacationers into three groups: those traveling by car, those traveling by domestic air, and international tourists from overseas (not counting vacationers from Mexico or Canada). Our outlook for vacationers traveling by car this season is for a 2% to 4% increase over 2008. With gasoline much cheaper this year, we expect more Americans to hit the road. The American Automobile Association (AAA) projected that over the Memorial Day holiday weekend alone, some 27 million travelers took a significant trip by car, up 2.7% from 2008. Inferring a similar rise for the whole season, our forecast appears to be about right, judging by the AAA.

For travelers taking a domestic vacation by air, we look to the Air Transport Association (ATA), the industry trade organization for leading U.S. airlines. The ATA works with most leading airlines to identify volume of booked travel. This allows it to collect data on about two-thirds of volume, from which it derives an industry-wide estimate. The ATA is projecting 7% fewer domestic air passengers this year — or approximately 171 million versus 183 million in 2008. Also, the ATA expects fewer Americans, or 24 million compared to 26 million last year, will travel internationally by air this summer. Our outlook here concerns solely the domestic hotel industry, and we assume that any shift from international to domestic travel is already reflected in the ATA data.

For inbound international travel, we turn to the Office of Travel and Tourism Industries (OTTI) of the U.S. Department of Commerce. The OTTI, while not providing a specific forecast just for the summer season, does expect international visitors for all of 2009 to decline 8% from 2008. An 8% drop over the summer, as well, would result in about 600,000 fewer international tourists than the 7.4 million who visited during June, July, and August last year.

We then looked at the ratio of room nights sold last year to the number of travelers. We refined this by making some assumptions, such as there are an average of two persons per room, that the average number of nights per couple are about three for domestic trips (we factored in that some domestic trips do not include a hotel stay to derive an average of three nights), while we assumed overseas tourists spent 10 nights on average in hotels.

With these inputs, we project that domestic hotels would sell approximately 292 million room nights this season, running from Memorial Day to Labor Day. Adjusting for additional days this season due to Memorial Day being earlier and Labor Day later, we also project that there will be some 475 million room nights available, or a 4.4% increase from 2008.

Having these two numbers, we then forecast occupancy this season of 61%, down from approximately 68% in 2008. With a reasonable idea of how room rates trended so far in 2009, we assumed an average daily rate (ADR) of about $97 versus just under $107 last year. As Revenue Per Available Room, or RevPAR, is the product of occupancy rate multiplied by ADR, we get our RevPAR forecast of slightly more than $59, down 19% from $73 in 2008. We also can project that room revenues, or rooms sold times ADR, are likely to decline. Our forecast is for room revenue for the summer season to decline approximately 15% to $28 billion from $33 billion.

While it remains to be seen how our forecast for this season proves out, we note that we were fairly accurate in 2008 when we projected room demand of 306 million to 320 million nights, with occupancy between 67% and 68%.

With operations looking this weak, most hotel chains significantly stepped up promotional efforts and expanded discounted rate offers. A typical offer for this season might entail a stay of two nights and a night free with the next stay. While effectively a 33% discount to published rates, these deals encourage brand loyalty. Moreover, guests might stay more than one night upon their return for their free night, so these promotions also serve to generate future demand.

Nevertheless, we'll be surprised to see any "no vacancy" signs greeting travelers this summer. ■

NEGATIVE POTENTIAL IMPLICATIONS

COMPANY / TICKER	‡STARS	‡QUALITY RANKING	*RISK	STYLE	CURRENT PRICE	**12-MONTH TARGET PRICE	†P/E RATIO	YIELD (%)
Choice Hotels / CHH	2	B+	High	Growth	27	24	18.0	2.7
Gaylord Entertainment / GET	1	C	High	Blend	14	9	NM	Nil
Marriott International / MAR	1	A	High	Growth	22	13	33.8	1.6
Orient-Express Hotels / OEH	2	NR	High	NA	7	4.5	NM	Nil
Starwood Hotels / HOT	1	NR	High	Blend	22	14	73.3	4.1
Wyndham Worldwide / WYN	1	NR	High	Blend	11	7	9.6	1.5

*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. NA-Not available. NM-Not meaningful. Source: S&P Equity Research.

Stewart Glickman
S&P Equity Analyst

Drilling for Dólares

Energy services companies see prospects in Mexico.

While Mexico faces challenges from swine flu and security fears, we believe that if such risks can be handled, the country offers U.S. energy services companies bright prospects for the future.

Unlike other oil & gas basins around the world, such as the U.S. Gulf Coast, the U.S. Lower 48, and in the North Sea (where exploration and production customers are scaling back on capital spending to stay within their operating cash flows), the same isn't true of Mexico, where investment in energy services — bringing in offshore drillers to find and exploit new fields, and oilfield services companies with high technology capabilities to handle difficult terrain — is on the upswing.

Why is this happening now? One explanation is the production problems at Mexico's nationalized oil company, PEMEX, and its prized field, Cantarell. The world's third-largest oilfield when it was discovered in 1972, Cantarell commenced production in 1979. Over the last 30 years, PEMEX pumped about 13 billion barrels from Cantarell, which accounts for about 33% of PEMEX's total output. Recently, however, Cantarell's production began to decelerate. In January 2009, Cantarell production was a mere 772,000 barrels of oil per day, down 38% from January 2008, and PEMEX's total production in 2008 declined for the fifth-straight year, which we attribute mainly to the problems at Cantarell.

We believe such production woes spell good opportunities for the energy services companies — those that own the drilling rigs that can help access new reservoirs and the services companies that help exploit more output from existing reservoirs. Indeed, in addition to doing what it can to forestall the accelerating decline rate at Cantarell (such as enhanced oil recovery methods), PEMEX is investing in new shallow production, new deepwater production, and in new production from onshore fields. For the latter two categories, PEMEX budgeted $29.1 billion in spending through 2012, *Bloomberg* reported.

In offshore waters, based on data from ODS-Petrodata, Mexico currently hosts 39 actively marketed offshore drilling rigs (excluding one that is owned by PEMEX). Of these 39 rigs, an impressive 35, or 90%, are under contract. This compares very favorably with the situation in the nearby U.S. Gulf of Mexico, where of the 88 actively marketed offshore drilling rigs, only 56 (64%) were under contract, which we attribute in part to weak natural gas prices. Despite being physically adjacent markets for offshore drilling rigs, there is vast disparity in prospects, in our view, and a number of offshore drilling contractors recently moved otherwise idle rigs (from the U.S.

(Continued on page 7)

POSITIVE POTENTIAL IMPLICATIONS

COMPANY / TICKER	‡STARS	‡QUALITY RANKING	*RISK	STYLE	CURRENT PRICE	**12-MONTH TARGET PRICE	†P/E RATIO	YIELD (%)
Diamond Offshore / DO	4	B	Medium	Blend	78	82	7.3	0.6
Ensco / ESV	3	B+	High	Growth	36	32	5.6	0.3
Noble / NE	5	B	Medium	Growth	31	36	4.9	0.5
Pride International / PDE	3	B-	High	Blend	23	24	7.9	Nil
Schlumberger / SLB	3	NR	Medium	Blend	53	52	18.7	1.6
Transocean / RIG	5	NR	Medium	Blend	74	88	5.4	Nil
Weatherford International WFT	4	NR	Medium	Growth	19	21	19.0	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. ‡See definitions on page 2. †Based on S&P estimated fiscal 2009 earnings. Source: S&P Equity Research.

ETFs

NAME / TICKER	TOTAL RETURN* 1-YEAR	TOTAL RETURN* 3-YEAR	EXPENSE RATIO
iShares Dow Jones US Oil Equipment Index / IEZ	-55.0	-9.9	0.50
PowerShares Dynamic Oil & Gas Services / PXJ	-56.0	-10.3	0.60
SPDR Oil & Gas Equipment & Services / XES	-53.4	NA	0.40

*Annualized total returns are through 5/22/09. NA-Not available. Source: Standard & Poor's ETF Reports.

Quality Ranking Upgrades

A select list of high-quality stocks.

Beth Piskora
Managing Editor
S&P Editorial

Standard & Poor's has provided Quality Rankings for stocks since 1956. Quality Rankings represent S&P's quantitative appraisal of the growth and stability of earnings and dividends over the past 10 years. (See complete definition on page 2.)

S&P considers any stock with a Quality Ranking of A- or better to be high quality. The table (right) contains stocks with a STARS ranking of four or five (suggesting our analysts believe they will outperform in the next 12 months), and that had a Quality Ranking upgrade to at least A- this year.

Although Quality Rankings (QR) are not intended to predict stock price movements, a study of high-quality vs. low-quality stocks shows that over long periods of time, high-quality stocks outperform. Of course, that's no guarantee they will continue to behave that way in the future.

"High QR stocks outperformed strongly during the second half of 2008," says Richard Tortoriello, an S&P equity analyst. "However, so far in 2009, it has been a distinctly Low QR market. Low QR stocks tend to rally strongly after a bear market, on initial signs of economic stabilization/improvement. The reason is that they are severely beaten down in the bear market, on worries they may go out of business, etc., and when positive economic signs emerge, these stocks are then repriced." ■

STOCK SCREEN OF THE WEEK

COMPANY / TICKER	‡STARS	‡QUALITY RANKING	*RISK	CURRENT PRICE	*12-MONTH TARGET PRICE	†P/E RATIO	YIELD (%)	QUALITY —RANKING— OLD	NEW
● Bard (C.R.) / BCR	5	Medium	Growth	72	88	14.3	0.9	A-	A
Baxter International / BAX	4	Medium	Growth	50	60	13.3	2.1	B+	A-
● Church & Dwight / CHD	5	Low	Growth	50	65	14.7	0.7	A	A+
● CVS Caremark / CVS	5	Medium	Blend	29	39	11.2	1.0	A	A+
Ecolab / ECL	4	Low	Growth	37	45	18.5	1.5	A	A+
● Entergy / ETR	4	Medium	Blend	72	82	10.6	4.2	A-	A
● EOG Resources / EOG	5	High	Growth	68	87	37.2	0.9	B+	A-
FPL Group / FPL	5	Low	Blend	54	64	12.6	3.5	A-	A
ITT / ITT	4	Medium	Growth	41	50	11.4	2.1	B+	A-
Norfolk Southern / NSC	4	Medium	Blend	35	45	9.6	3.9	B+	A-

●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.

Drilling for Dólares *(Continued from page 6)*

Gulf, and from some overseas basins) to Mexico, to take advantage of Mexico's relatively stronger demand.

Major suppliers of drilling rigs to the offshore Mexico market include Noble Corp. with 13 rigs under contract; Pride International with six rigs under contract; and Diamond Offshore with four rigs under contract. Of the 39 rigs working in Mexico today, 35 are jackups drilling in shallow waters so we see strong expansion potential in PEMEX's midwater and deepwater exploration activity. This would likely benefit Noble, Pride, Diamond Offshore, Transocean, and Ensco International. In Ensco's case, its capacity to handle deepwater work is largely by virtue of newbuild rigs expected to be delivered over the next several years.

Onshore Mexico, PEMEX is taking steps to enhance overall production as well. Despite some extremely challenging geology, PEMEX is undertaking significant investment in its Chicontepec oilfield and awarded contracts to oilfield services companies Weatherford International and Schlumberger. Given the difficult drilling conditions found in this oilfield, we believe that technologically advanced energy services companies, such as Weatherford and Schlumberger, offer a compelling value proposition to PEMEX.

Risk factors to services growth prospects in Mexico include a worsening national security situation, which could drain coffers and constrain PEMEX's ability to finance its planned growth initiatives. ■

Vulnerable Valuations *(Continued from cover)*

97.9, as it included the $23.25 per-share loss in 2008's fourth quarter.

But if some believe this is a perfect example of why operating earnings tell a better story, don't get too optimistic. The S&P 500's operating P/E was trading at nearly 16.0 times earnings on March 9, slightly below the median of 18.0 since 1988. As of May 22, however, the S&P 500 was trading at more than 22.0 times trailing, 12-month operating results, 16.4 times 2009 estimates, and nearly 12 times 2010 estimates.

In other words, even though the S&P 500 bounced nicely off of its early March lows, it may not sustain its upward trajectory for too much longer, as valuations become increasingly stretched. S&P equity analysts are looking for the S&P 500 to earn $54.14 a share in 2009, up 9% from the $49.51 recorded in 2008. Early 2010 estimates point to a more than 39% advance to $74.99, which may in the end prove to be a bit too optimistic.

Rich valuations may also hold back further sharp advances for cyclical sectors in the S&P 500, such as consumer discretionary, financials, and materials even if you overlook 2009 estimated multiples of 48.0, 51.0, and 33.0, respectively, and focus on the more palatable 2010 multiples. Valuations begin to look more plausible, in our opinion, the further out you go. Of course, the confidence in these earnings projections wanes as well. ■

S&P 500 P/E RATIOS ON TRAILING 12-MONTHS OPERATING EPS

Equity Analysts' S&P 500 Bottom-up estimates	OPERATING P/E RATIOS 2008A	2009E	2010E
Consumer Discretionary	32.1	50.1	14.3
Consumer Staples	14.4	13.6	12.4
Energy	7.6	22.4	11.9
Financials	NM	52.2	26.9
Health Care	12.6	11.2	10.1
Industrials	9.8	13.5	12.6
Information Technology	14.4	18.5	13.9
Materials	17.0	34.1	15.8
Telecommunications Services	13.6	12.2	12.0
Utilities	12.1	11.1	10.1
S&P 500	18.2	16.8	12.1

A-Actual. E-Estimated. Source: S&P Equity Research.

ETFs for Cash

Vaughan Scully
S&P Editorial

With the ongoing creation of ETFs, investors have more options and are beginning to use them for the cash portion of their portfolio allocation.

With investor interest in exchange traded funds (ETFs) seemingly endless, fund sponsors are busy exploring every nook and cranny for new ideas. Over the past year, ETFs holding money market securities — Treasury, municipal, and corporate bonds that mature in less than a year — sprung up to give investors a "cash-equivalent" ETF option.

Money market ETFs are attractive for several reasons: they tend to offer higher yields than bank CDs and have lower expense ratios than most money market mutual funds. Like mutual funds, they pay interest once a month, and give investors access to a portfolio of bonds that would be nearly impossible for an individual investor to assemble. Unlike money market mutual funds, there's no minimum investment. For those who prize liquidity most — in September 2008, the $23 billion Primary Fund set off a panic among investors when it halted redemptions for seven days after sustaining losses — shares in money market ETFs can be sold instantly.

There are some downsides to money market ETFs, however. While the ability to sell shares in an ETF more quickly than a mutual fund may be attractive to some, it's really most valuable to investors looking to dabble in highly volatile securities rather than relatively stable short-term paper. True, expense ratios may be low, but expense ratios don't take into account the commissions money market ETF investors have to pay when buying or selling ETF shares, fees that add up quickly for those making regular deposits and withdrawals as is typical of money market funds.

Several money market ETFs are now trading in the United States, and there are several others in Europe and Canada as well. Most seek to replicate an index. The iShares Barclays Short Treasury Bond ETF (SHU) is by far the largest, with $2 billion in assets, while the PowerShares VRDO Tax-Free Weekly Portfolio (PVI) and the SPDR Barclays Capital Short Term Municipal Bond ETF (SHM) have about $450 million in assets. ■

Global Asset Allocation Update

S&P's Investment Policy Committee left all three portfolios intact.

The S&P growth ETF asset allocation is geared towards risk-tolerant investors with longer time horizons. It dedicates 37% to these asset classes: 19% in developed overseas markets (EFA), 6% in emerging markets (EEM), 7% in U.S. mid-caps (MDY), and 5% in U.S. small-caps (IJR). In addition, this allocation dedicates 43% to large-cap U.S. stocks (SPY), 5% to intermediate-term bonds (AGG), 5% to short-term bonds (SHY), and 10% to cash.

The conservative risk profile is designed for investors who primarily seek capital appreciation, but have some income requirements. In general, the time horizon for this model is five to seven years. The moderate risk profile is designed for investors with a primary objective of capital appreciation. In general, the time horizon for this allocation is 10 to 15 years.

The growth risk profile, with a time horizon of 20 to 25 years, is designed for investors who seek capital appreciation and are willing to tolerate the higher risk levels associated with greater exposure to domestic and international equity markets.

These time horizons are often tied to retirement dates or projected life expectancy, but not always. For example, a 70-year-old individual with substantial income may have a long investment time horizon since the funds may eventually be spent on the college education of a grandchild or great-grandchild yet to be born. Conversely, a 50-year-old planning to retire in five years may choose to be more conservative than his age would ordinarily indicate. ■

MODERATE PORTFOLIO

ALLOCATION	ASSET CLASS/ INVESTMENT STYLE	ETF/TICKER	*ANNUALIZED TOTAL RETURN (%)	EXPENSE RATIO (%)
45%	**U.S. STOCKS**			
37	Large-Cap Blend	SPDR S&P 500 / SPY	-35.2	0.09
5	Mid-Cap Blend	S&P MidCap 400 SPDR / MDY	-32.4	0.25
3	Small-Cap Blend	iShares S&P SmallCap 600 / IJR	-30.0	0.20
15%	**FOREIGN STOCKS**			
12	International	iShares MSCI EAFE / EFA	-42.6	0.34
3	Emerging Markets	iShares MSCI Emerging Markets / EEM	-39.8	0.72
25%	**BONDS**			
20	U.S. Debt	iShares Barclays U.S. Aggregate / AGG	3.8	0.23
5	U.S. Short-Term Debt	iShares Barclays 1-3 Year Treasury / SHY	4.2	0.15
15%	**CASH**	U.S. 6-Month Treasury Bills		
Total=100%				

*Data as of 4/30/2009. Sources: Standard & Poor's ETF Reports and iShares. *The Outlook's* Moderate ETF Portfolio gained 0.4% year to date through May 22 vs. a gain of 1.6% for its custom benchmark, which is composed of 45% S&P 1500, 30% Barclays U.S. Aggregate, 15% MSCI EAFE, and 10% Barclays 1-3 month T-bill. Does not include transaction costs. Past performance is no guarantee of future results.

DETAILED GROWTH

ALLOCATION	ASSET CLASS/ INVESTMENT STYLE	ETF/TICKER	*ANNUALIZED TOTAL RETURN (%)	EXPENSE RATIO (%)
55%	**U.S. STOCKS**			
43	Large-Cap Blend	SPDR S&P 500 / SPY	-35.2	0.09
7	Mid-Cap Blend	S&P MidCap 400 SPDR / MDY	-32.4	0.25
5	Small-Cap Blend	iShares S&P SmallCap 600 / IJR	-30.0	0.20
25%	**FOREIGN STOCKS**			
19	International	iShares MSCI EAFE / EFA	-42.6	0.34
6	Emerging Markets	iShares MSCI Emerging Markets / EEM	-39.8	0.72
10%	**BONDS**			
5	U.S. Debt	iShares Barclays U.S. Aggregate / AGG	3.8	0.23
5	U.S. Short-Term Debt	iShares Barclays 1-3 Year Treasury / SHY	4.2	0.15
10%	**CASH**	U.S. 6-Month Treasury Bills		
Total=100%				

*Data as of 4/30/2009. Sources: Standard & Poor's ETF Reports and iShares. *The Outlook's* Growth ETF Portfolio gained 1.4% year to date through May 22 vs. a gain of 1.9% for its custom benchmark, which is composed of 55% S&P 1500, 15% Barclays U.S. Aggregate, 25% MSCI EAFE, and 5% Barclays 1-3 month T-bill. Does not include transaction costs. Past performance is no guarantee of future results.

DETAILED CONSERVATIVE

ALLOCATION	ASSET CLASS/ INVESTMENT STYLE	ETF/TICKER	*ANNUALIZED TOTAL RETURN (%)	EXPENSE RATIO (%)
30%	**U.S. STOCKS**			
23	Large-Cap Blend	SPDR S&P 500 / SPY	-35.2	0.09
4	Mid-Cap Blend	S&P MidCap 400 SPDR / MDY	-32.4	0.25
3	Small-Cap Blend	iShares S&P SmallCap 600 / IJR	-30.0	0.20
10%	**FOREIGN STOCKS**			
10	International	iShares MSCI EAFE / EFA	-42.6	0.34
45%	**BONDS**			
35	U.S. Debt	iShares Barclays U.S. Aggregate / AGG	3.8	0.23
10	U.S. Short-Term Debt	iShares Barclays 1-3 Year Treasury / SHY	4.2	0.15
15%	**CASH**	U.S. 6-Month Treasury Bills		
Total=100%				

*Data as of 4/30/2009. Sources: Standard & Poor's ETF Reports and iShares. *The Outlook's* Conservative ETF Portfolio lost 0.4% year to date through May 22 vs. a gain of 1.5% for its custom benchmark, which is composed of 30% S&P 1500, 50% Barclays U.S. Aggregate, 10% MSCI EAFE, and 10% Barclays 1-3 Month T-bill. Does not include transaction costs. Past performance is no guarantee of future results.

High-Quality Capital Appreciation Portfolio

12/31/2008 — 5/22/2009
Base Currency: US Dollar

The High-Quality Capital Appreciation Portfolio underperformed its benchmark from the beginning of the year through May 22, declining 7.3% vs. a 1.8% decrease in the S&P 500. The data we have provided show which stocks and sectors contributed to, or detracted from, the portfolio's performance year-to-date through May 22. 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
Int'l Business Machines	7.11	22.34	1.38
Hudson City Bancorp	3.34	13.79	0.87
Sigma-Aldrich*	9.03	8.57	0.79
Nike	7.26	3.41	0.31
CVS Caremark	6.36	3.32	0.23

*Replaced on May 26.

TOP DETRACTORS BY HOLDING

COMPANY NAME	AVERAGE WEIGHT	RETURN	CONTRIBUTION
Molson Coors*	3.28	-35.37	-2.61
General Dynamics*	2.75	-31.76	-1.88
Bard (C.R.)	3.92	-17.52	-1.19
Procter & Gamble	6.36	-12.86	-0.99
General Mills	6.15	-11.96	-0.83

*Replaced on March 16.

TOP CONTRIBUTORS BY SECTOR

SECTOR	AVERAGE WEIGHT	RETURN	CONTRIBUTION
Information Technology	9.07	13.73	0.95
Financials	3.34	13.79	0.87
Materials	9.03	8.57	0.79

TOP DETRACTORS BY SECTOR

SECTOR	AVERAGE WEIGHT	RETURN	CONTRIBUTION
Consumer Staples	39.05	-11.61	-4.81
Industrials	14.69	-8.81	-2.51
Health Care	17.56	-9.68	-1.97

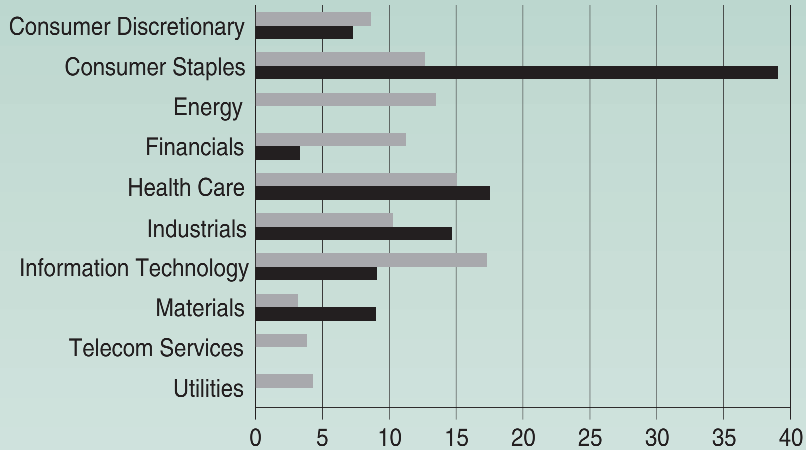
CURRENT HIGH-QUALITY CAPITAL APPRECIATION PORTFOLIO

COMPANY / TICKER	‡STARS	‡QUALITY RANKING	*RISK	STYLE	CURRENT PRICE	**12-MONTH TARGET PRICE	†P/E RATIO	YIELD (%)
Bard (C.R.) / BCR	5	A	Medium	Growth	70	88	14.1	0.9
Church & Dwight / CHD	5	A+	Low	Growth	50	65	15.0	0.7
CVS Caremark / CVS	5	A	Medium	Blend	29	39	11.6	1.0
EOG Resources / EOG	5	A-	High	Growth	68	87	11.6	1.0
Fastenal / FAST	5	A	Medium	Growth	33	45	20.6	2.1
General Mills / GIS	5	A-	Low	Blend	51	65	13.4	3.3
Hudson City Bancorp / HCBK	5	A	Low	Blend	12	15	11.7	5.0
Int'l Business Machines / IBM	5	A	Medium	Growth	103	139	11.2	2.1
Johnson & Johnson / JNJ	4	A+	Low	Growth	54	65	12.4	3.5
Myland / MYL	5	A-	Medium	Growth	13	17	12.4	1.0
Nike / NKE	4	A+	Medium	Growth	54	65	13.4	2.0
PepsiCo / PEP	4	A+	Low	Growth	50	57	13.9	3.5
Procter & Gamble / PG	4	A+	Low	Growth	52	63	15.0	3.3
United Technologies / UTX	4	A+	Low	Growth	51	55	12.8	3.0
Wal-Mart Stores / WMT	5	A+	Low	Blend	49	59	13.6	2.2

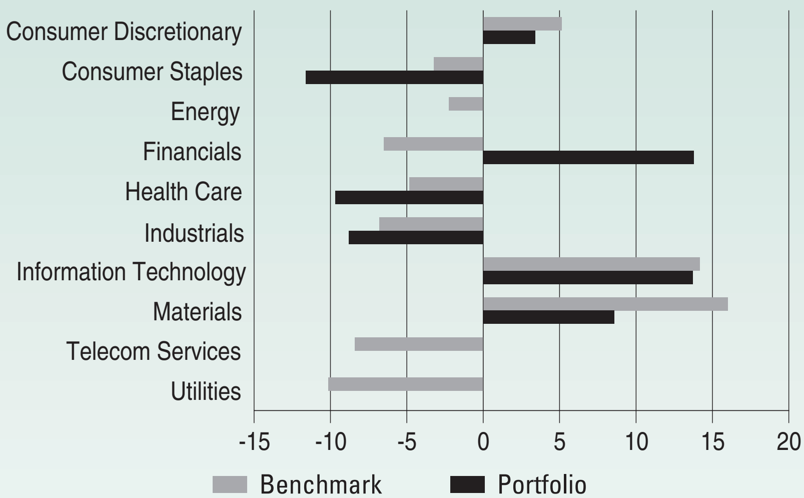
*Based on our analysts' assessment of qualitative factors, including financial strength, potential share volatility, competitive position, industry cyclicality, regulatory/legal issues, and other factors.
**Please note that all investments carry risks. Specific risks to each stock recommendation and 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.

High-Quality Capital Appreciation Portfolio vs. S&P 500

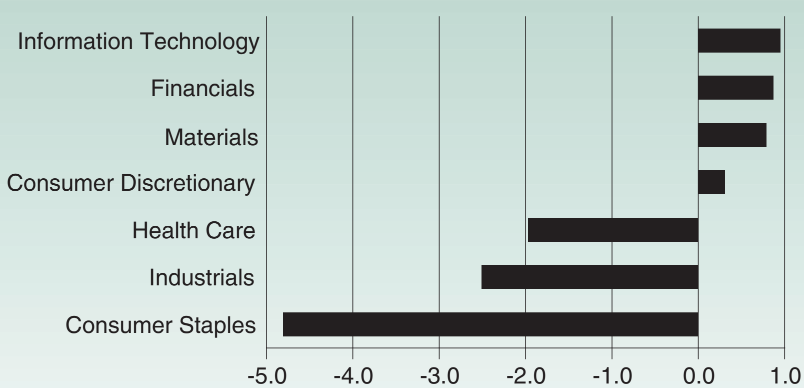
SECTOR ALLOCATION (%)



SECTOR RETURNS (%)



PORTFOLIO CONTRIBUTION BY SECTOR (%)



Source: S&P Equity Research.

LARGEST HOLDINGS

COMPANY NAME	AVERAGE WEIGHT	RETURN
Sigma-Aldrich*	9.03	8.57
Nike	7.26	3.41
Int'l Business Machines	7.11	22.34
Becton, Dickinson*	7.00	-3.15
PepsiCo	6.94	-5.00

*Replaced on May 26.

BEST PERFORMERS

COMPANY NAME	AVERAGE WEIGHT	RETURN
Int'l Business Machines	7.11	22.34
Hudson City Bancorp	3.34	13.79
Sigma-Aldrich*	9.03	8.57
Nike	7.26	3.41
CVS Caremark	6.36	3.32

*Replaced on May 26.

WORST PERFORMERS

COMPANY NAME	AVERAGE WEIGHT	RETURN
Molson Coors*	3.28	-35.37
General Dynamics*	2.75	-31.76
Bard (C.R.)	3.92	-17.52
Procter & Gamble	6.36	-12.86
General Mills	6.15	-11.96

*Replaced on March 16.

For more information

on individual stocks in the portfolio,

visit our website

www.outlook.standardandpoors.com.

Harness Our Quant Power

Standard & Poor's Neural Fair Value 25 Portfolio buys what are deemed undervalued issues with superior return potential.

Neural fair value rankings are derived from two quantitative stock selection systems proprietary to S&P: the neural model and the fair value model.

The neural rank is based on "neural networks," an artificial intelligence system that replicates the brain's ability to learn from mistakes. The neural model identifies the factors that led to outperformance over the most recent six-month period and determines which stocks should benefit from those factors in the future. Stocks are ranked in five tiers, from most attractive (5) to least (1).

The fair value model calculates the price at which a stock should trade, based on fundamental data.

Neural fair value rankings also include the earnings surprise indicator, which tags those issues most likely to beat earnings estimates, and the timing index, which tells investors whether or not a stock meets certain trend requirements that have proved favorable to long-term capital appreciation.

Year-to-date through May 22, the portfolio gained 3.4% vs. a 1.8% loss for the S&P 500. ■

NEURAL FAIR VALUE 25 PORTFOLIO

COMPANY / TICKER	NEURAL	FAIR VALUE	TIMING	***EARNINGS SURPRISE	*S&P INDEX	**RISK	STYLE	CURRENT PRICE
Accenture / ACN	3	5	+	C	...	Medium	Growth	30
ADC Telecommunications / ADCT	2	1	+	C	Mid	High	Blend	7
Allergan / AGN	3	4	N	C	500	Medium	Growth	44
BMC Software / BMC	2	4	+	B	500	Medium	Blend	33
Capella Education / CPLA	3	5	N	A	Small	NA	Growth	52
Check Point Software / CHKP	4	5	+	B	...	High	Growth	23
General Dynamics / GD	3	5	+	A	500	Low	Growth	56
Hanesbrands / HBI	1	5	N	B	Mid	NA	Blend	17
Hanover Insurance / THG	3	3	N	A	Mid	Medium	Value	33
Herbalife / HLF	3	5	+	A	...	Medium	Growth	29
Hologic / HOLX	4	3	N	B	Mid	High	Growth	12
Immucor / BLUD	4	4	N	B	Mid	NA	Growth	14
Integrys Energy / TEG	3	4	N	B	500	Medium	Blend	27
● Int'l Business Machines / IBM	4	5	+	C	500	Medium	Growth	103
Lockheed Martin / LMT	2	4	+	C	500	Medium	Growth	82
Macy's / M	1	1	N	B	500	High	Blend	12
NCR / NCR	3	2	+	E	Mid	Medium	Growth	11
NetApp / NTAP	3	4	+	A	500	High	Growth	19
Occidental Petroleum / OXY	2	2	+	B	500	Medium	Blend	63
Polycom / PLCM	3	5	+	B	Mid	High	Growth	17
QLogic / QLGC	3	5	+	D	500	Medium	Growth	14
Symantec / SYMC	2	1	+	A	500	High	Blend	15
Tempur-Pedic Int'l / TPX	5	5	N	B	...	High	Growth	11
Tidewater / TDW	3	5	+	B	Mid	Medium	Value	46
Tyco Int'l / TYC	3	4	+	A	500	Medium	Blend	27

●Master List issue. *500-S&P 500; Mid-S&P MidCap 400; Small-S&P SmallCap 600. **Based on our analysts' assessment of quantitative factors, including financial strength, potential share volatility, competitive position, industry cyclicality, regulatory/legal issues, and other factors. ***This indicator divides stocks into five tiers, designated by the letters A through E, based upon their ability to beat earnings estimates. "A" ranked stocks are most likely to show future positive earnings surprises, while "E"-ranked stocks are most likely to report negative earnings surprises. "N" indicates data was not available to determine the indicator. N-Neutral. NA-Not available. Source: S&P Equity Research.