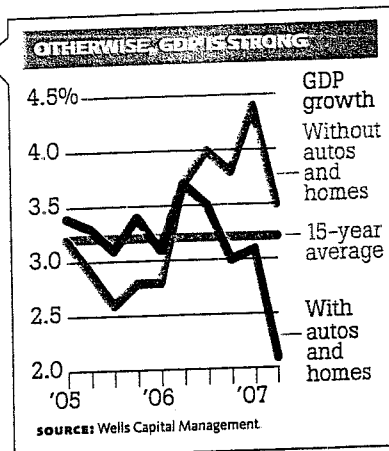


## ■ THE ECONOMY IS DOING WELL, EXCEPT FOR HOUSING AND AUTOS

### Real estate's woes haven't been spreading

Bears are focused on big-picture data that show the pace of economic growth slowing. But excluding homes and autos, the economy looks pretty good, says James Paulsen, chief investment strategist of Wells Capital Management. While problems in the housing sector could still spread to the rest of the economy, it's been almost a year since the real estate bubble began to burst. Federal Reserve chairman Ben Bernanke recently said he didn't think housing posed a danger.



### Profits exceed expectations

Corporate profits, which climbed swiftly for the past three years, are not rising as fast as in 2007. Still, earnings have far exceeded expectations this year, and profit growth is expected to rebound into the double digits in 2008. That's good news for stock prices, which usually follow the bottom line.

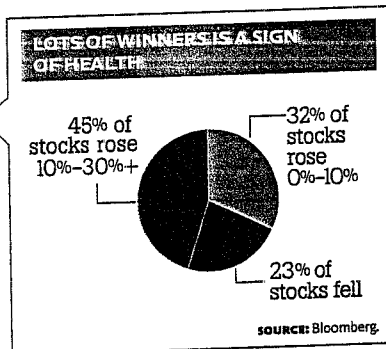
### Deals, deals and more deals

Acquisitions typically buoy the market because they drive up stock prices. And 2007 looks to be the year of the buyout,

## ■ DESPITE THE BIG RUN-UP, THE STOCK MARKET LOOKS UNDERVALUED

### Everyone's a winner (well, nearly everyone)

When a bull market consists of relatively few stocks rising rapidly—think Internet companies in the late 1990s—that's usually a bad sign. Happily, the recent run of good luck on Wall Street has been spread around the entire market. The shares of more than three-quarters of the companies in Standard & Poor's 500 are up in 2007. "People are interested in stocks



again," says David Poiesz, who manages the Oppenheimer Growth Fund.

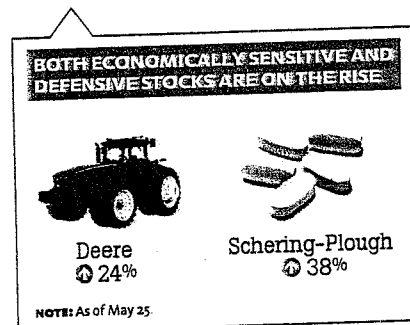
### Stocks are still cheap

Five years into the bull market, the price-to-earnings multiple of the S&P 500 stands at 17, below its 25-year average of 20. For it to return to just average, stocks would have to rise another 18%. Some strategists, like Tobias Levkovich at Citigroup Wealth Management, believe

## ■ THE OUTLOOK IS STRONGEST FOR LARGE-CAP GROWTH STOCKS

### Defensive stocks are on the rise

One worrisome sign: Defensive stocks like health care and consumer staples, which generally hold up well when the economy dips, have been strong lately. For example, pharmaceutical stocks

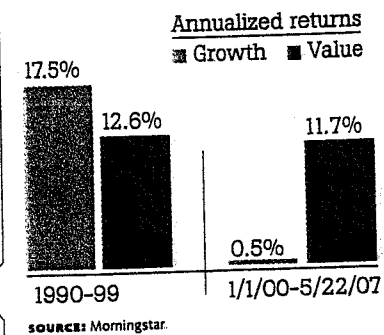


Schering-Plough and Merck are up 38% and 15%, respectively. That's a sign investors don't believe the bull market will continue. On the other hand, commodities and economically sensitive stocks like Alcoa and tractor maker Deere, which soared during the booming economy of the past few years, have continued to do well so far in 2007.

### Time for growth to take a turn

The performance of mutual funds that invest in value stocks—that is, those trading at a low price compared with their earnings—has vastly trumped the performance of growth funds for five of the past seven years. It's one of the lon-

### VALUE FUNDS HAVE BEEN ON TOP SINCE 2000. GROWTH'S TURN SOON?



gest stretches of outperformance for the value group, which suggests that growth investors' turn may be coming soon.

