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For Important Disclosures, see pages 3-4.

Weekly Market Monitor

For the first time in weeks, the stock market had the feel of the ordinary rather than the extraordinary. It resembled the good ol' dog days of summer rather than the highly volatile, back-and-forth action market participants have become accustomed to experiencing.

As earnings reports continued to drift in and economic data were released, the major indices spent much of the week consolidating recent gains. The S&P 500 Index rallied 6.9% in July, following a 5.4% decline in June. July's performance was the biggest monthly gain since July 2009. It is among the top 10% of all monthly performances since 1930. Following the big move, the S&P 500 is down 1.2% year to date.

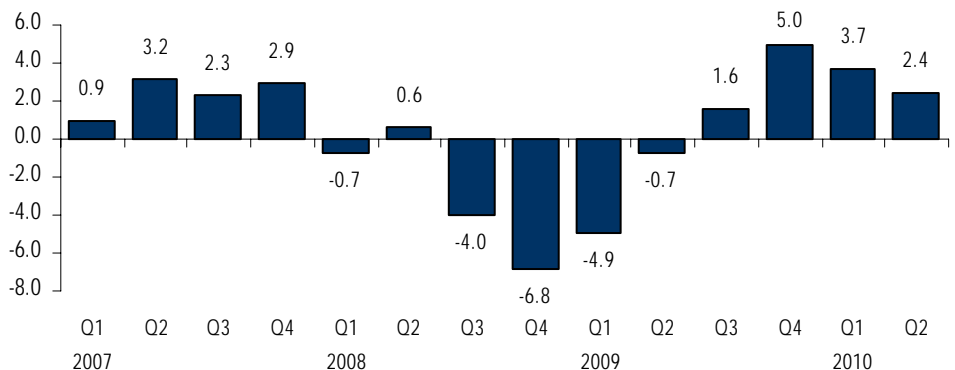
This week, the major indices were mixed. The S&P 500 fell 0.1% and the Dow Jones Industrial Average rose 0.4%. Financials outperformed as a number of regional banks reported earnings. Conglomerates also performed well. The S&P Retail Index underperformed on concerns about consumer confidence and spending trends.

The Long, Tough Climb

While this may not seem or feel like a recovery to many Americans, preliminary data indicated the economy grew 2.4% in the second quarter. Business spending expanded at a reasonable pace, and equipment and software spending surged.

But consumer spending (historically roughly 70% of economic activity) was anemic, and government spending represented much of the activity during the quarter. Also, overall economic momentum has slowed, as the graph below illustrates.

Gross Domestic Product Growth (%)



Source: Bloomberg, Bureau of Economic Analysis; Growth rates reported as annualized rates, quarter-over-quarter

The stock market initially sold off on the news early Friday. The 2.4% growth rate was less than Wall Street economists forecasted, and activity in previous quarters was revised much lower, especially for consumer spending. So the Great Recession was even worse than initially reported. However, the market bounced off the lows following the release of other less troublesome data.

Growth is at risk of decelerating further in the second half of 2010 and will continue to face challenges in 2011, in our view. While the economy has *statistically* rebounded from the severe recession, it's not making much progress in repairing the extreme damage to employment and confidence, or in narrowing the output gap.

The economy is attempting to climb out of a big hole, but it is carrying too much weight to generate the momentum experienced in previous, more robust recovery cycles. The weights include high household debt, high unemployment, excess capacity, a broken tax code, an unsustainable entitlement system, and high government deficits and debt.

Currently no RBC economist is forecasting a near-term recession, but they acknowledge the possibility. Key data next week should shed light about the economy’s progress—the ISM Manufacturing Index and employment report.

Earnings Round-Up

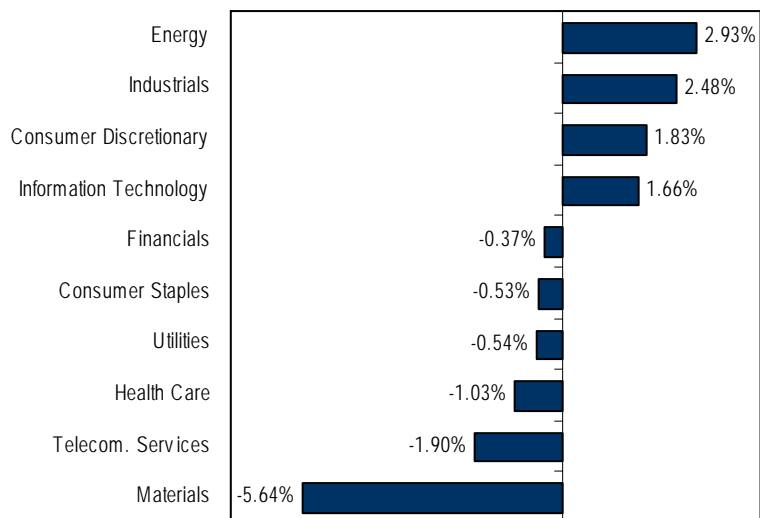
Here’s a look behind the headlines at the roughly 67% of S&P 500 companies that have reported second-quarter earnings thus far:

- 75.6% of companies beat earnings expectations compared to the 59% average since 2003.
- Second-quarter revenue growth stands at 11.7% versus 12.5% in the first quarter, excluding financial companies.
- Third-quarter S&P 500 estimates were nearly unchanged during the past four weeks (-0.01%).
- Analysts have raised estimates for four sectors. Energy and Industrials have experienced the largest upward third-quarter revisions. The Materials sector has suffered the deepest cut, as the chart below on the left illustrates.
- Within the sectors, the following industries have seen the greatest third-quarter estimate increases during the past four weeks: Automobile & Components (30.38%), Semiconductors & Semiconductor Equipment (8.74%), and Transportation (7.16%).
- Wall Street analysts currently forecast S&P 500 earnings per share of \$79.37 in 2010, as illustrated in the chart below on the right. RBC Capital Markets’ institutional strategist Myles Zyblock believes that’s too high of a hurdle. He’s forecasting \$76.00.
- Ditto for 2011. Wall Street analysts are at \$92.62 per share (16.7% growth versus their 2010 estimate). Zyblock is currently at \$90.00.

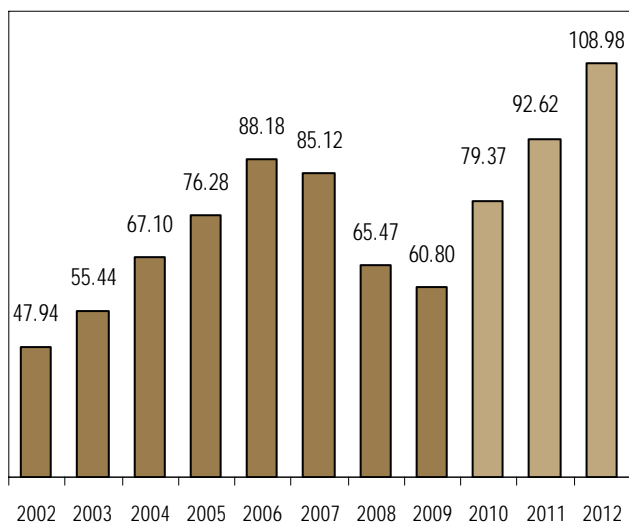
Regardless, 2011 is a long way away. Earnings that year and in 2012 will be highly dependent on whether the U.S. economy eventually morphs into a self-sustaining recovery or whether it withers from the weight it’s carrying.

Corporate Earnings Trends

S&P 500 Third Quarter Estimate Revisions in Last Four Weeks



S&P 500 Annual Earnings – Actual and Estimated



Source left chart: Bloomberg

Source right chart: FactSet; Annual S&P 500 earnings data for 2010, 2011, and 2012 represent the consensus bottom-up estimate among Wall Street analysts

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|------------|-------|-------|--------------------|-------|
| | | | Count | % |
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