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A New Normal for Stock Investors?

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LOOMIS | SAYLES

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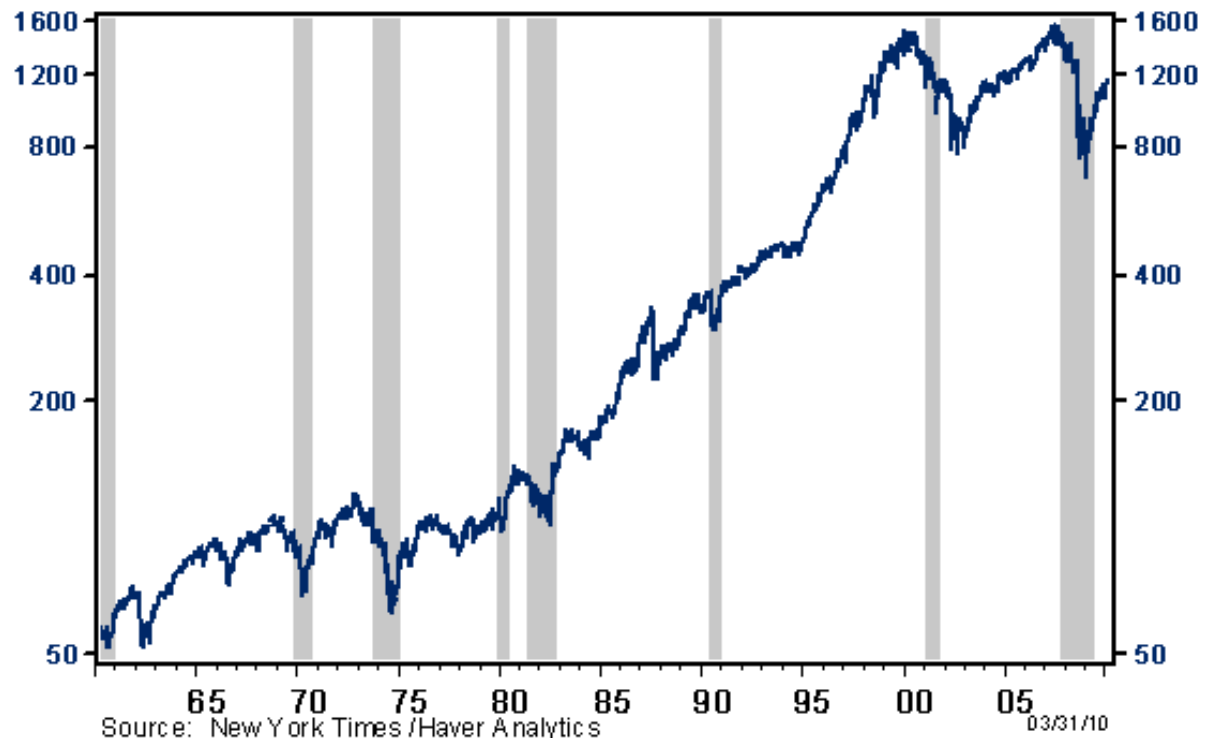
a new normal for stocks

S&P 500 Compound Annualized Total Return

1926 - 2009	+11.0%
1970 - 2009	+9.9%
1970 - 1999	+13.7%
2000 - 2008	-3.6%
2009	+26.5%

Standard & Poor's 500 Stock Price Index

1941-43=10



Data source: 2010 Ibbotson Yearbook, Bloomberg. Indexes are unmanaged and do not incur fees. You cannot invest directly in an index.



dissecting causes of a lost decade for stocks

1. Excessive Valuation

- Price-to-Earnings (P/E) Contraction
- March, 2000 the S&P 500 P/E peaked at 30.7x and P/B peaked at 5.0x

2. Mean Reversion

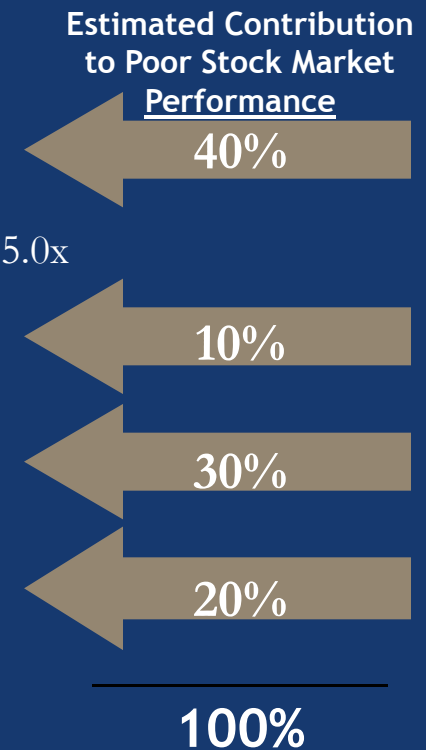
- From 1995 – 1999 the S&P 500 annualized return was +28.5%

3. Excessive Leverage and Failure to Understand Risk

- Financial Sector and Consumers

4. Policy Mistakes

- Mortgage markets
- Fed monetary policy



Source: Bloomberg

Past performance is no guarantee of future results.

Outlook as presented reflects subjective judgments and assumptions of the portfolio manager as of April 2010, and unexpected events may occur. There can be no assurance that developments will transpire as stated. Opinions expressed will evolve as future events unfold.



understanding the stock market: rules of the road

- Return and Risk (a.k.a. greed and fear) may be easily understood in a textbook but much harder to master in the trenches
- Inflation and taxes are among the biggest enemies of long-term stock returns because of their impact on real purchasing power
- Earnings and cash flow are a lifeblood of long-term stock performance
- Dangerous phrases to a trustee:
 - “It’s different this time.”
 - “I have this market all figured out.”

Source: Loomis, Sayles

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stock market gauges over intermediate term

Valuation: Neutral for stocks

The average trailing earnings yield (E/P) of the S&P 500 is now 5.7% versus a 3.6% yield on the 10-Year U.S. Treasury.

Sentiment: Neutral for stocks

From a contrarians view, the percent of individual investors who are bullish are approximately equal to their 5 and 10 year averages (*American Association of Individual Investors*).

Technical: Positive for stocks

Market breadth has improved. Major stock markets have risen above their 150 day moving averages.

Macro Business Environment: Positive for stocks

Corporate profits and margins have continued to expand. Corporate free cash flow has remained robust.

Relative Performance Stocks vs. Bonds: Positive for Stocks

Trailing 3-year annualized returns

Stocks -5.7%

Bonds +5.8%

30-year average

Stocks +11.8%

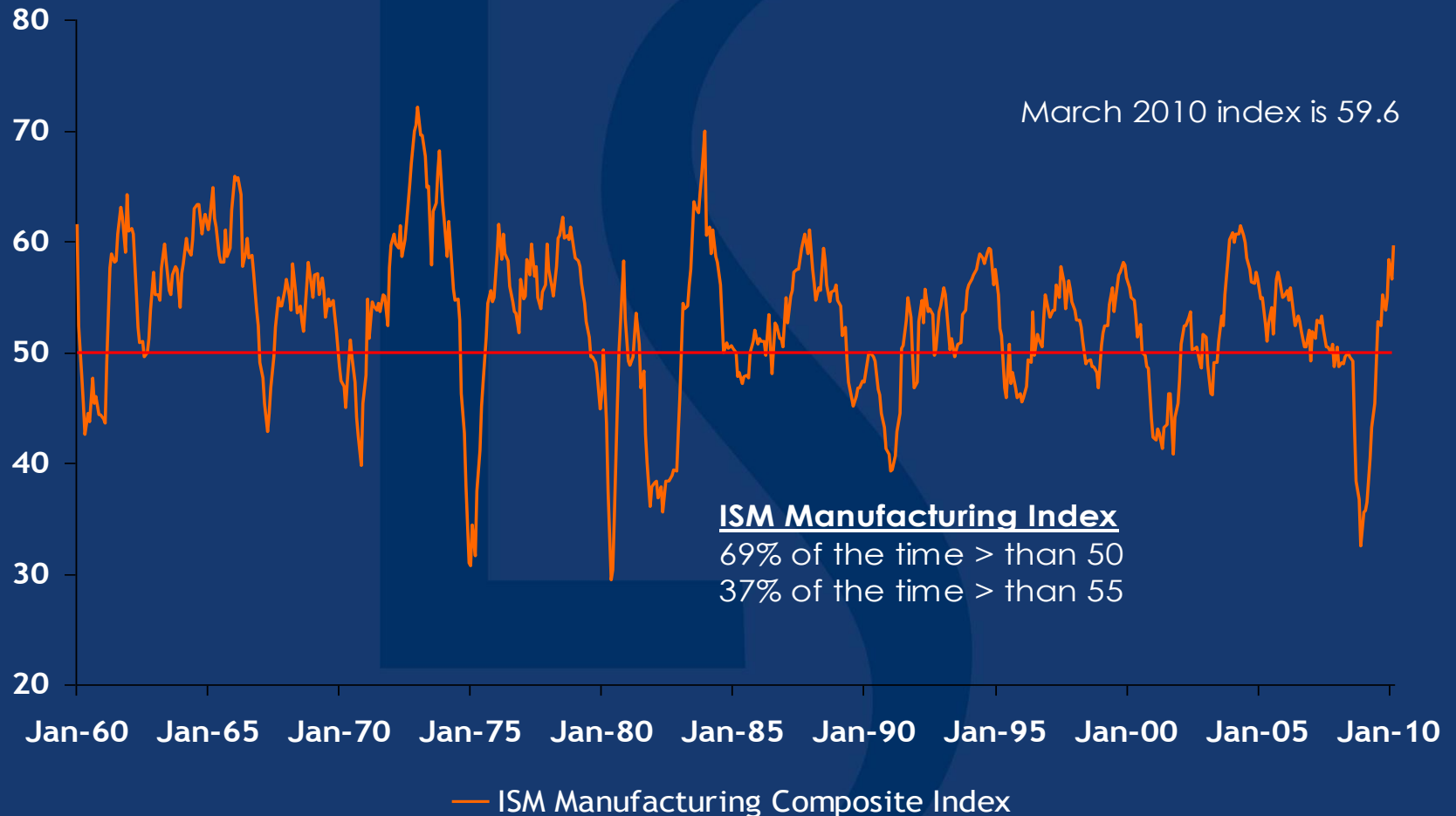
Bonds +8.6%

Source: Bloomberg, Factset, Federal Reserve Bank of St. Louis. Data is updated through 2/28/2010

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ism manufacturing composite index a reliable business measure



capital market risks

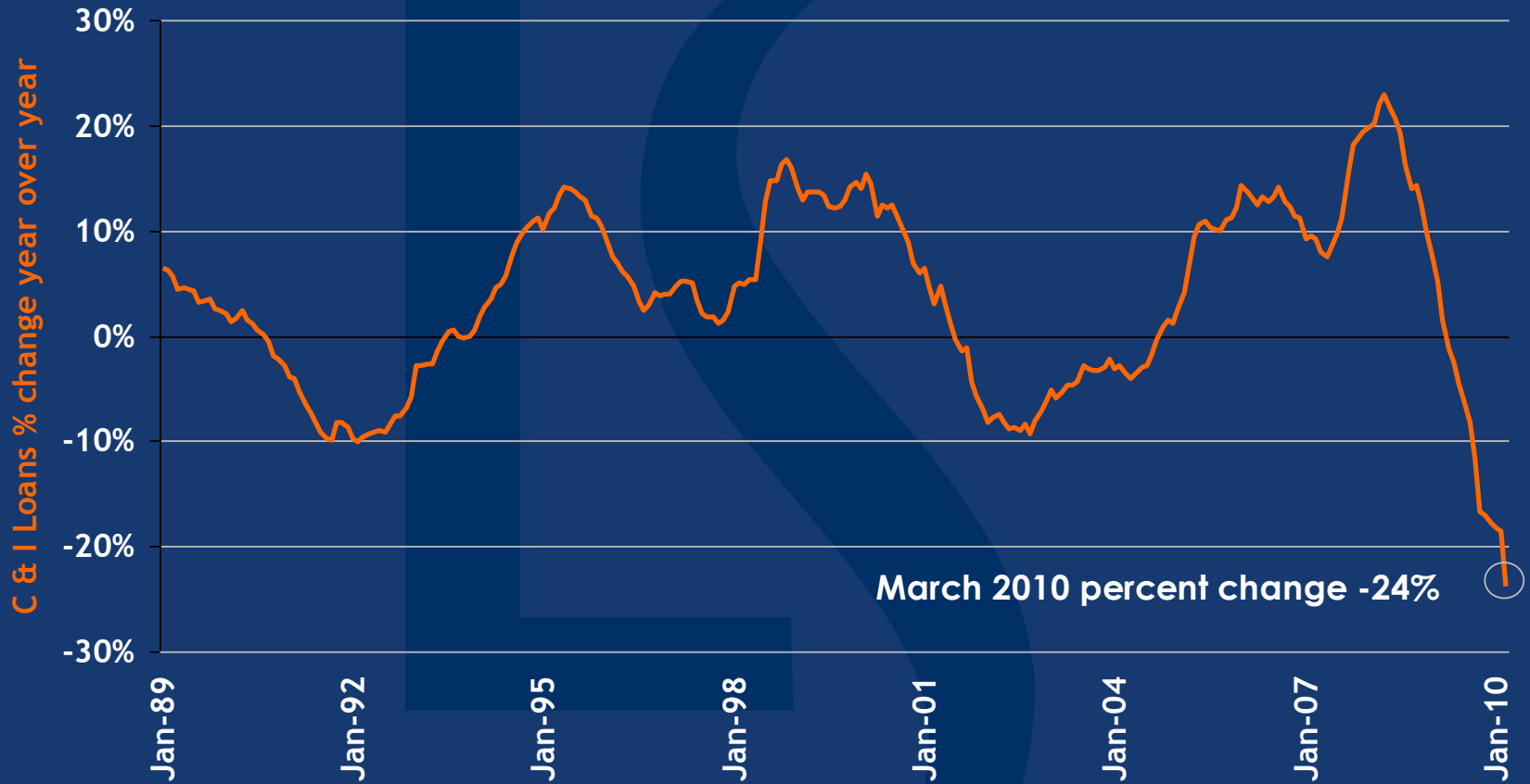
1. C & I loan growth fails to improve, rendering aggressive monetary stimulation less robust to the economy.
2. Federal monetization and federal debt burden prompts higher inflation expectations.
3. Savings rates continue to rise from current 4% to over 8%, as consumer deleveraging continues more than estimated.
4. Investor sentiment becomes overly bullish, setting up a contrarian double-digit stock market decline.
5. Low quality stock rally persists.

Source: Loomis, Sayles

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Large, domestic commercial bank loans – year over year % change



March 2010 percent change -24%

lower quality stocks have led the recent stock rally

S&P 500 Price Returns December 31, 2009 through March 30, 2010

	Median Total Return	Median Net Profit Margin	Median Return on Equity (ROE)	Median Debt to Equity Ratio
Characteristics of the Top 50 Performing Stocks in the S&P 500	34%	4.6%	9.3%	92%
Characteristics of the Remaining 450 Stocks in the S&P 500	6%	8.4%	16.9%	55%

Russell 2500 Price Returns December 31, 2009 through March 30, 2010

	Median Total Return	Median Net Profit Margin	Median Return on Equity (ROE)	Median Debt to Equity Ratio
Characteristics of the Top 250 Performing Stocks in the Russell 2500	46%	2.6%	3.7%	74%
Characteristics of the Remaining Stocks in the Russell 2500	6%	4.9%	9.3%	44%



key indicators at market troughs

Stock Market Perspective at Bear Market Bottoms

	10/3/1974	8/12/1982	12/4/1987	10/9/2002	3/9/2009
S&P 500 % change from Peak to Trough ¹	-48.2%	-27.1%	-33.5%	-49.1%	-55.2%
S&P 500 Trailing P/E Ratio	7.7x	7.2x	14.7x	17.2x	10.0x
Inflation Rate ²	9.5%	6.3%	2.9%	1.6%	2.0%
10 Year Treasury Yield	8.0%	13.6%	9.0%	3.6%	2.5%
Money Supply 6-month % change (Monetary Base)	8.7%	6.8%	7.3%	6.7%	158.0%
Excess Return Value Style vs. Growth ³ Style Stocks Two Year Period Following Bear Market Bottom (cumulative return)	30.8%	9.0%	-4.8%	20.5%	7.7%
Excess Return Small Cap vs. Large Cap ⁴ Style Stocks Two Year Period Following Bear Market Bottom (cumulative return)	31.0%	2.3%	-3.3%	28.1%	26.5%

1-Year Anniversary of
Market Trough
(3/9/2009 - 3/9/2010)

¹ S&P 500 stock index

² GDP Price Deflator

³ Russell 1000 Value/Russell 1000 Growth stock indexes

⁴ Russell 2000 and S&P 500 stock indexes

Data Source: FactSet

You cannot invest directly in an index. Indexes are unmanaged and do not incur fees.



long-term stock returns are determined by:

I. Very Formula Driven:

1. Starting Dividend Yield on Stocks
2. Expected Growth Rate of Earnings, Dividends and Cash Flow
3. Expected Change (up or down) in Price/Earnings Ratio

II. Example:



Source: Bloomberg, Loomis Sayles.

The example is provided for illustrative purposes only and is not meant to convey any prediction or expectation of performance for any investment product.



however, estimating future stock returns is not so simple

FACTORS THAT ALSO MATTER INCLUDE:

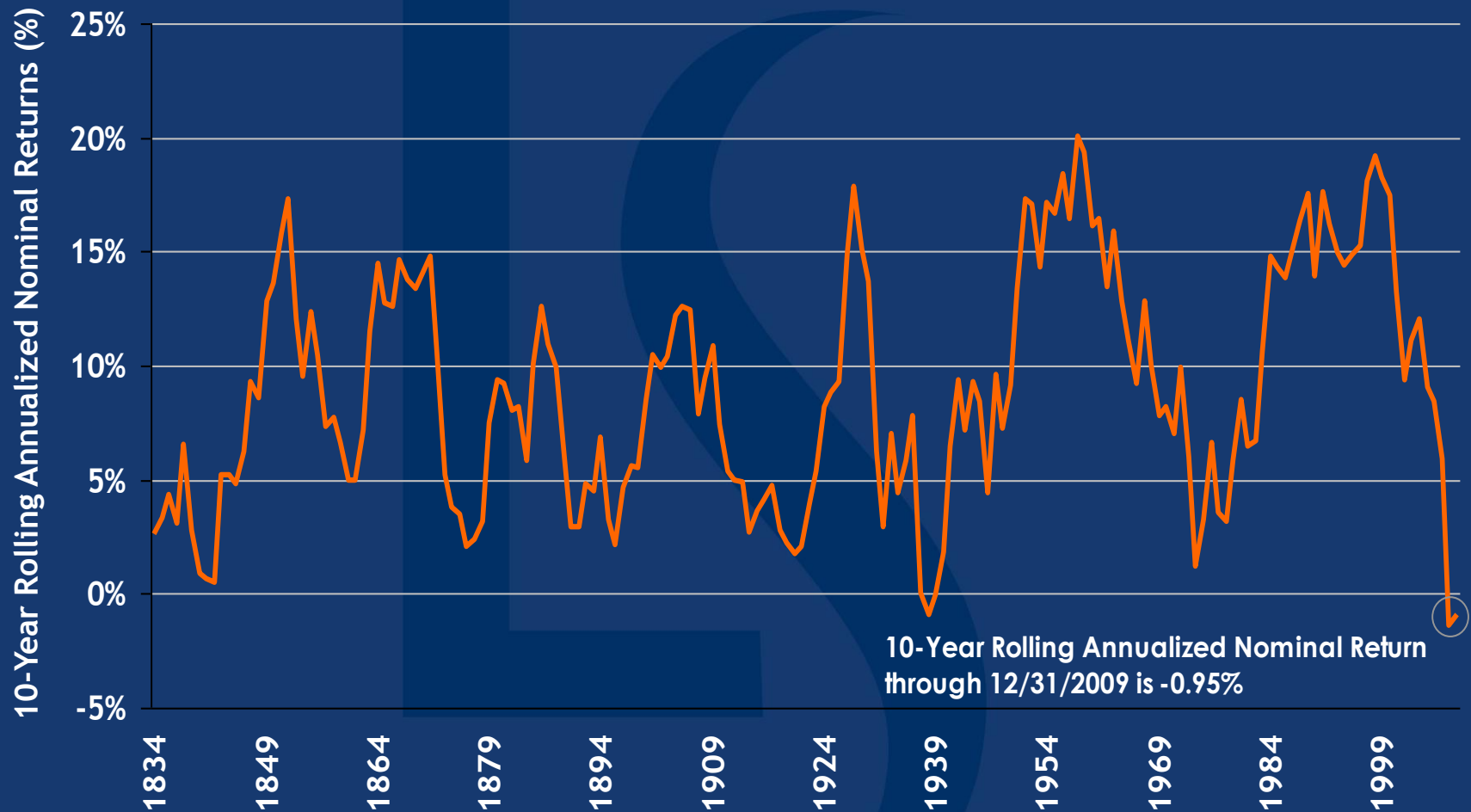
1. Mean Reversion of Long-Term Stock Returns
2. US Productivity
3. Inflation and Federal Reserve Monetary Policy
4. Government Tax, Spending and Regulatory Policy
5. Bond Yields and Assumptions on Equity Risk Premium
6. Corporate Capital Discipline and Free Cash Flow

Source: Loomis Sayles

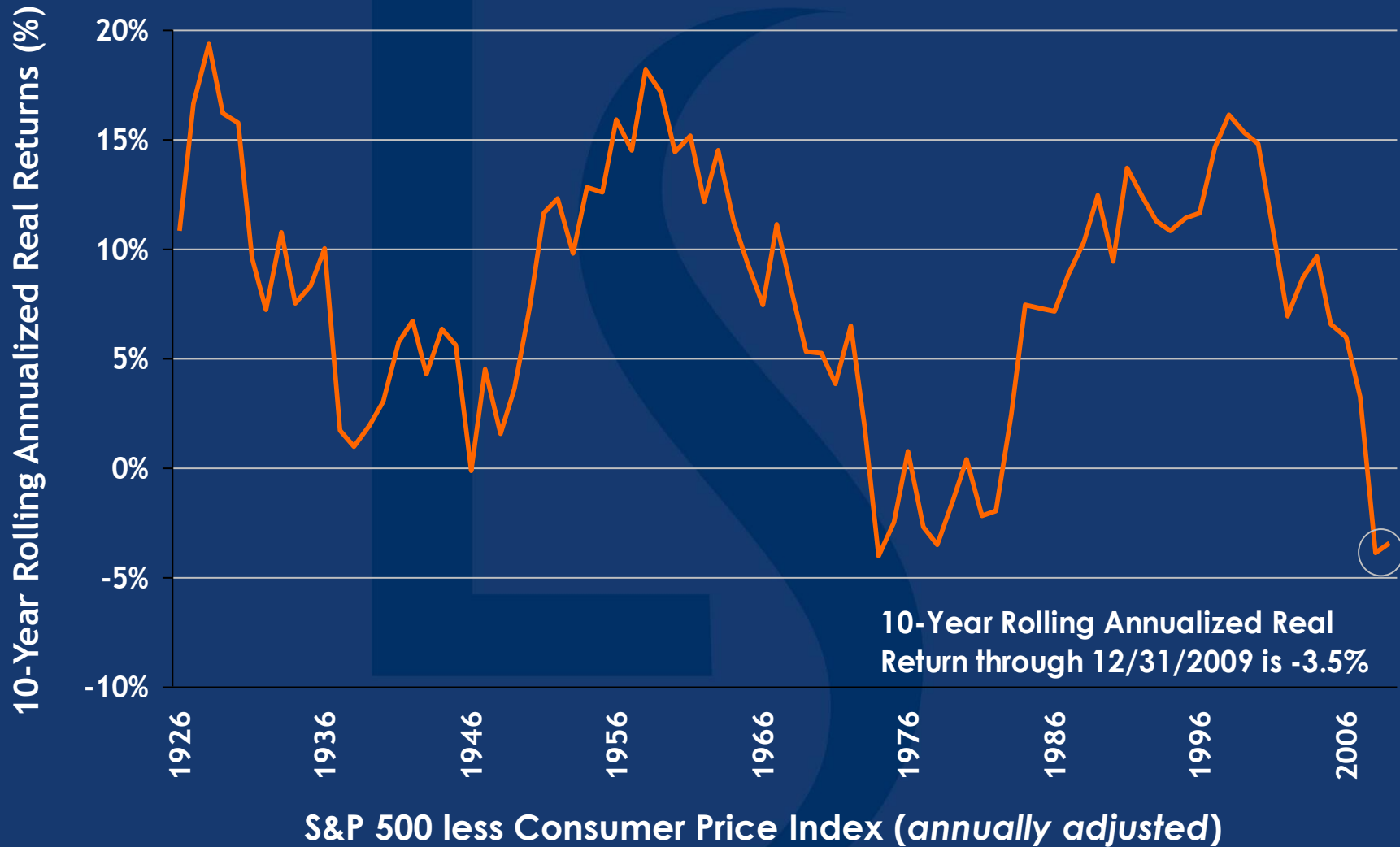
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10-year annualized nominal returns of s&p 500 large cap stocks 1834-2009



10-year rolling annualized real returns of large cap stocks 1926-2009



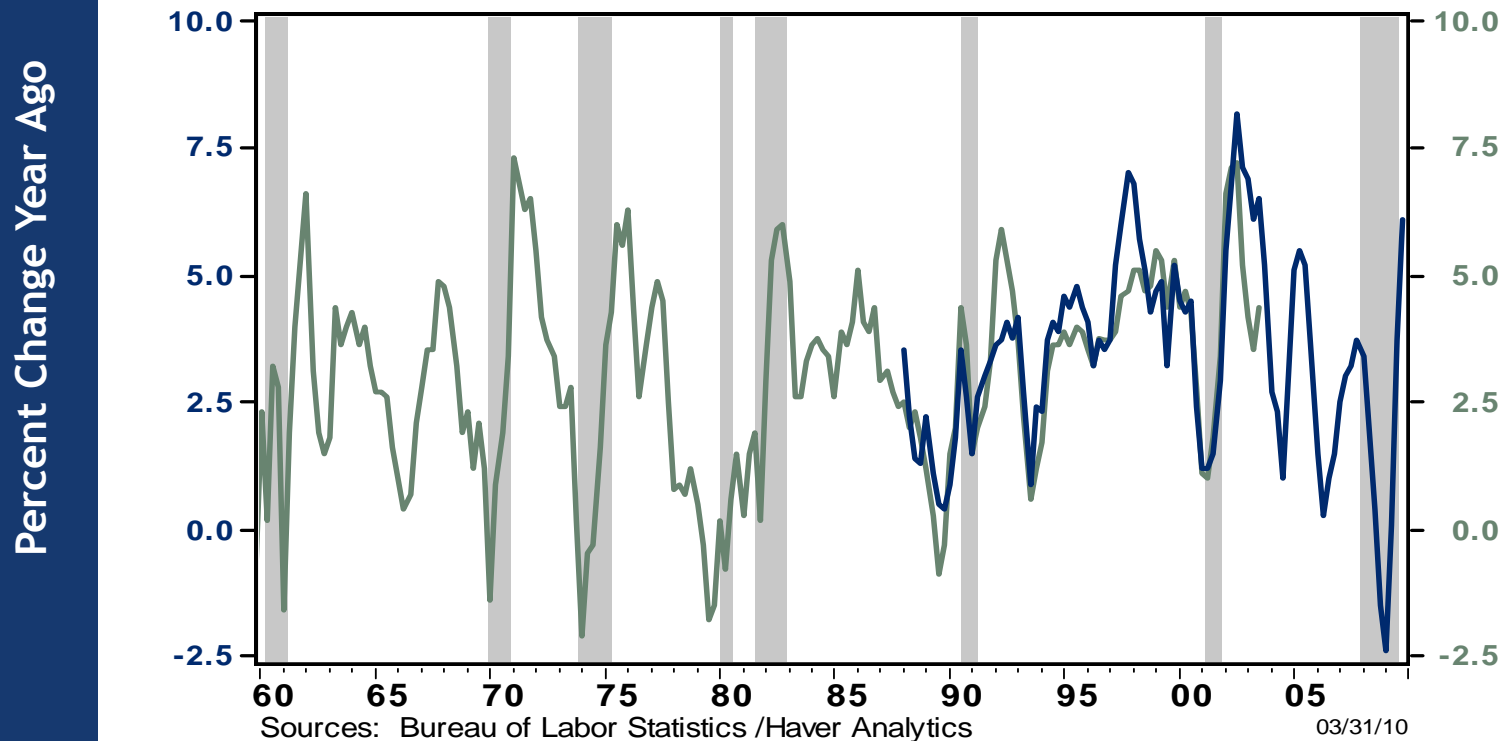
s&p 500 returns worst ten year periods . . . and the next five and ten year returns

<u>S&P 500 Worst Ten Year Periods</u>	<u>10 Year Annual Compound Return</u>	<u>Next Five Years</u>	<u>Next 5 Year Annual Compound Return</u>	<u>Next Ten Years</u>	<u>Next 10 Year Annual Compound Return</u>	
Q2 1929 to Q2 1939	-3.65%	Q2 1939 to Q2 1944	10.25%	Q2 1939 to Q2 1949	8.62%	
Q1 1999 to Q1 2009	-2.99%	Q1 2009 to Q1 2014	?	Q1 2009 to Q1 2019	?	
Q1 1929 to Q1 1939	-2.79%	Q1 1939 to Q1 1944	8.38%	Q1 1939 to Q1 1949	9.12%	
Q3 1929 to Q3 1939	-2.74%	Q3 1939 to Q3 1944	5.99%	Q3 1939 to Q3 1949	7.74%	
Q1 1928 to Q1 1938	-2.54%	Q1 1938 to Q1 1943	13.03%	Q1 1938 to Q1 1948	11.76%	
Q1 1930 to Q1 1940	-1.42%	Q1 1940 to Q1 1945	8.65%	Q1 1940 to Q1 1950	9.65%	
Q2 1930 to Q2 1940	-1.42%	Q2 1940 to Q2 1945	15.14%	Q2 1940 to Q2 1950	12.19%	
Q4 1928 to Q4 1938	-0.65%	Q4 1938 to Q4 1943	3.78%	Q4 1938 to Q4 1948	7.21%	Worst
Q3 1928 to Q3 1938	-0.10%	Q3 1938 to Q3 1948	5.97%	Q3 1938 to Q3 1948	8.12%	
Q3 1930 to Q3 1940	0.18%	Q3 1940 to Q3 1945	15.29%	Q3 1940 to Q3 1950	12.57%	
Q4 1927 to Q4 1937	0.20%	Q4 1937 to Q4 1942	4.61%	Q4 1937 to Q4 1947	9.61%	
Q4 1929 to Q4 1939	0.23%	Q4 1939 to Q4 1944	7.67%	Q4 1939 to Q4 1949	9.09%	
Q2 1928 to Q2 1938	0.44%	Q2 1938 to Q2 1943	7.60%	Q2 1938 to Q2 1948	9.52%	
Q3 1964 to Q3 1974	0.49%	Q3 1974 to Q3 1979	16.86%	Q3 1974 to Q3 1984	15.58%	Best
Q1 1931 to Q1 1941	0.71%	Q1 1941 to Q1 1946	19.22%	Q1 1941 to Q1 1951	14.47%	
Q4 1964 to Q4 1974	1.24%	Q4 1974 to Q4 1984	14.82%	Q4 1974 to Q4 1984	14.76%	
		Average	10.48%	Average	10.67%	



US productivity manufacturing sector & non-farm business sector

OUTPUT PER HOUR OF ALL PERSONS



large-capitalization stocks¹ free cash flow yields 1952 through march 2010



Source: Corporate Reports, Empirical Research Partners Analysis. Data is through 3/31/2010.
¹ Excludes Financial and Utilities; Capitalization-weighted data.



tax cuts, tax hikes & stock market returns: 1965-2009

	RUSSELL 2000	S&P 500
Average Annual Total Return from 1965 - 2009	15.3%	10.8%
Average Return One Year After Tax Cut	20.7%	13.5%
Average Return One Year After Tax Increase	12.5%	10.2%

Source: Tax Foundation, Bloomberg, Ibbotso. All indexes are unmanaged and do not incur fees. You cannot invest directly in an index.



factor influence on long-term stock returns

I. Starting Point

8.0% Stock Return Example

(2.0% Dividend Yield +6.5% Nominal Earnings Growth -0.5% Decline P/E Ratio)

II. Add/Subtract Factors

- | | |
|---|----------|
| 1. Mean Reversion of Long-Term Stock Prices | Positive |
| 2. US Productivity Growth | Positive |
| 3. Bond Yields & Equity Risk Premium | Positive |
| 4. Corporate Capital Discipline | Positive |
| 5. Government Tax & Regulatory Policy | Negative |
| 6. Inflation Rates | Negative |

III. Calculate Net Impact

Positive

Source: Bloomberg, Loomis Sayles.

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