Once Again, as in June - The Wildebeests are Running . . . When there is panic in the herd, there is lunch for the Lions and money to be made . . . Be a Lion!

"Most people get interested in stocks when everyone else is. The time to get interested is when no one else is . . ." – Warren Buffett

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Caution: It's a risky world we live in. My opinions are based on information believed to be reliable but hey, I could be wrong. When investing, try to use good judgment and don't hesitate to seek professional assistance. Remember to set limits and have a plan. . . Good Luck!

ABERDEEN

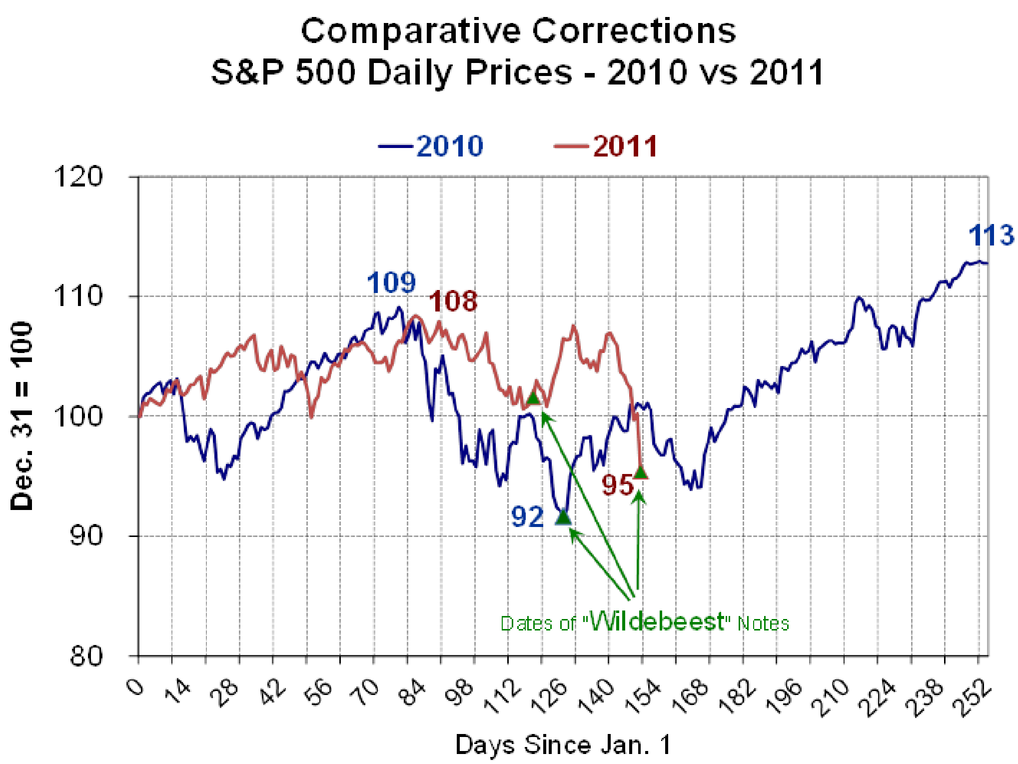
ABERDEEN INVESTMENT MANAGEMENT

This report is part of a series of reports we have periodically issued at times when we believe the market presents compelling value. Prior dates when we have made these calls include:

June 2011
July 2010
February 2009
December 2008

The report last year proved to be timely as it was sent on the day that marked the low closing price for the S&P 500 completing a 16% correction that started in late April. Our other prior reports have tended to be at least near market lows albeit some proved to be short term lows.

We are presently down 11.3% from the April 29, 2011 high. We are down 4.6% YTD. By the reaction in the market yesterday you would think we were on the precipice of another 2008/2009 free fall. The correction this year may turn out like last year's correction and precede a very strong year end rally.



My objective is to provide the reader with a refresh of several data series that will show that conditions are currently similar to other bottoms in the market. While there can be many different opinions I believe that we can all benefit from a review of the facts.

Executive Summary

We have a confluence of indicators in support of an approaching market bottom and prospects for a rally.

- An extended number of consecutive down days in the stock market. The Dow dropped 8 days in a row and is down in 9 of the last 10 days. As I have written in the past, these events are unusual and tend to occur near the end of a corrective phase.
- The market sustained a severe "90/90" panic day yesterday where 99% of the volume on the NYSE and the NASDAQ was down volume and 93% of the issues traded were down for the day. This kind of fear driven, indiscriminant selling is common at or near market bottoms.
- Oversold market conditions. The S&P500 is the most oversold since late 2008. It is more oversold than at the bear market low in March 2009.
- There has not been a sustained decline in the market when there is strong earnings growth such as seen in the market up to now. Earnings for the S&P 500 are estimated to end the Q2 earnings season up 23.9% over 2010 on a trailing 12 month ("LTM") basis. The median LTM earnings growth since 1980 has been 8.6%.
- The earnings yield has not been as strong as now since June 1989. More importantly, the spread between the earnings yield and the 10 year Treasury rate is the widest since 1979 when the S&P 500 gained 12.3% for the year. Spikes in the spread such as now have been coincident with market bottoms.
- The combination of low Treasury rates and a high earnings yield results in a record low undervaluation since 1970. The tool we use says the S&P 500 is 68.7% undervalued. For a frame of reference, the same tool calculated the market was 59% undervalued at December 2008 and 58% at the low in March 2009.
- We have not entered a recession or a bear market when the yield curve is steep, like now, when earnings are rising, like now, and when leading indicators are rising, like now.

As has been the case previously, the recent sell off appears to be an overreaction. Investors are clearly spooked by the hyperbole of the recent debt ceiling debate and the continuing Euro debt crisis. I am unable to predict the outcome in Europe.

March 2009, with similar conditions as now, marked the start of a greater than 90% move from the low to the April 2010 high close for the NASDAQ, where all of our stocks are listed. July 2010, a time when there had also been persistent selling pressure, marked the start of a similar move that lead to gains in the NASDAQ of 12.3% in Q3 of 2010, 27% by year end 2010 and 33% by the April 2011 high**.** That said, it is logical to expect the Street to cut estimates for GDP growth and earnings growth in light of recent developments. **Though the technicals indicate that we are at or near a bottom, the market is trading on pure emotion. We call this FUD (fear, uncertainty and doubt). We can't predict the exhaustion of such emotional selling, but the buyers in this area will be rewarded in time**.

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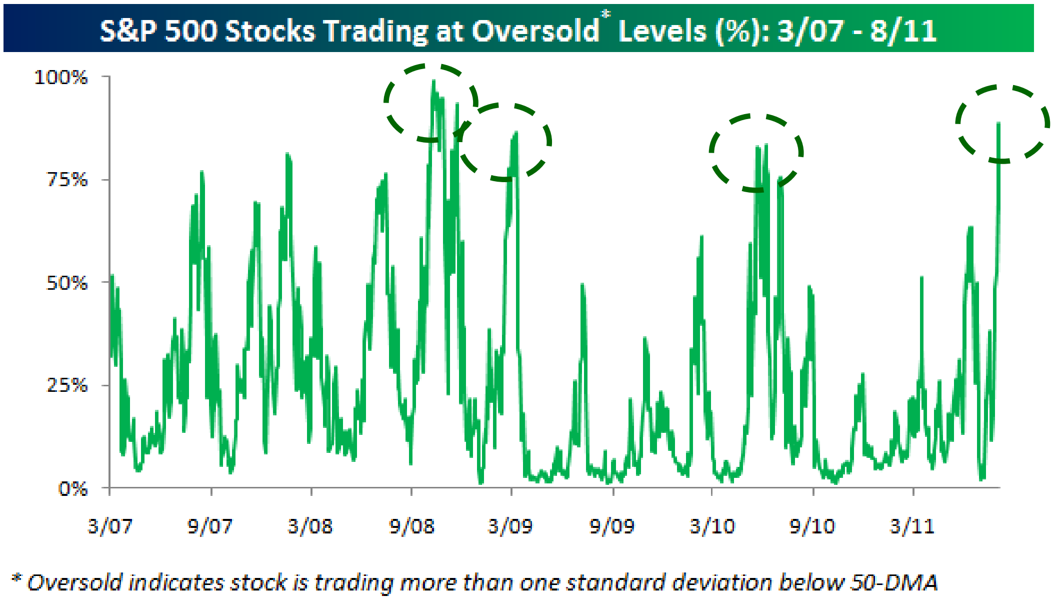
Panic in the Streets!

The extent of the sell off yesterday was breathtaking. 99% of the volume on the NYSE and NASDAQ was down volume! This does not occur at "tops" or "middles" of corrections. This occurs near bottoms.

8/4/2011	NYSE Data	NASDAQ Data
Volume (k)	7,504,992	3,272,996
Up Volume (k)	85,215	37,803
Down Volume (k)	7,417,609	3,231,476
Advancers	138	204
Decliners	2,971	2,445
New Highs	10	14
New Lows	445	305
% Down -Volume	*99%*	*99%*
% Down -Decliners	*95%*	*91%*

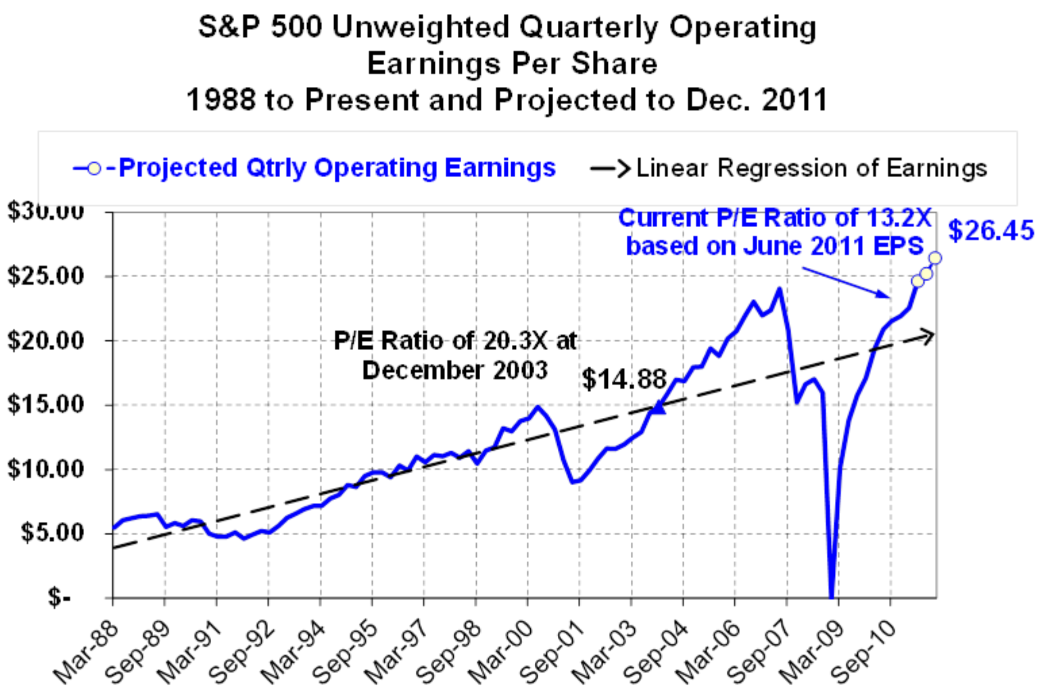
Extreme Oversold Condition

The following chart from Bespoke Investment Group displays that 89% of S&P 500 companies now trade below 1 std. deviation from their 50 day moving average share price. This condition happens at bottoms – not middles



Earnings Remain on the Rise

There has not been a sustained decline in the market when there is earnings growth such as seen in the market up to now and expected the remainder of 2011.

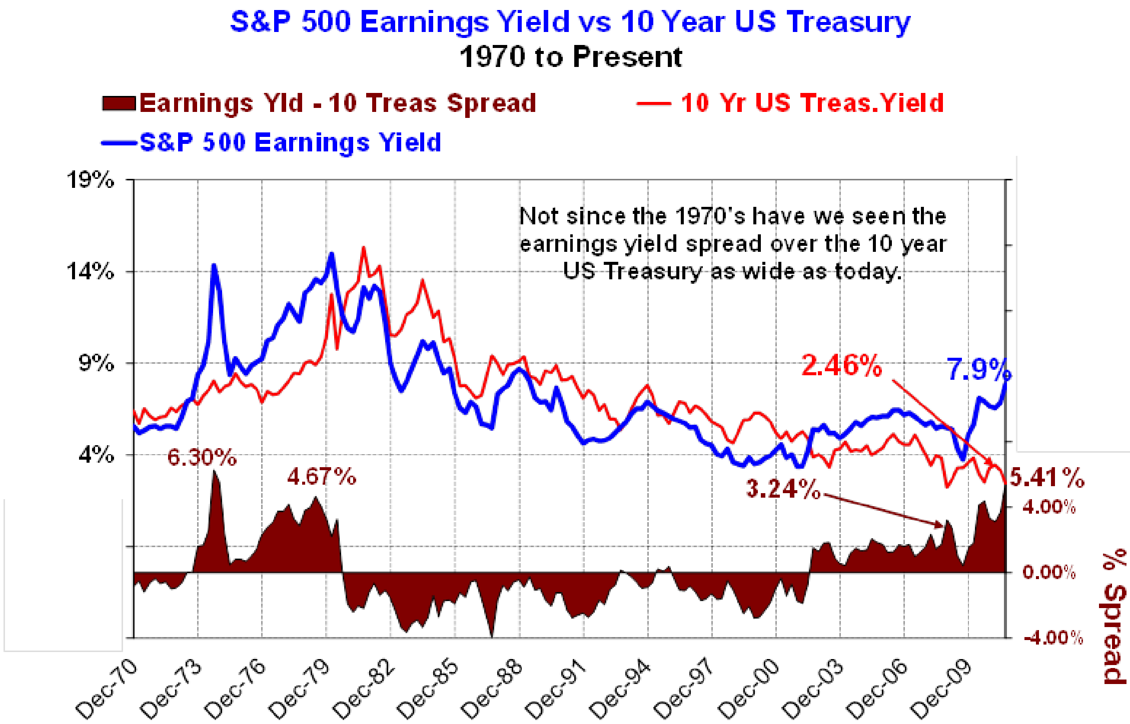


Recessions and bear markets don't happen until corporate profits roll over . . . that hasn't happened and is unlikely to happen soon.

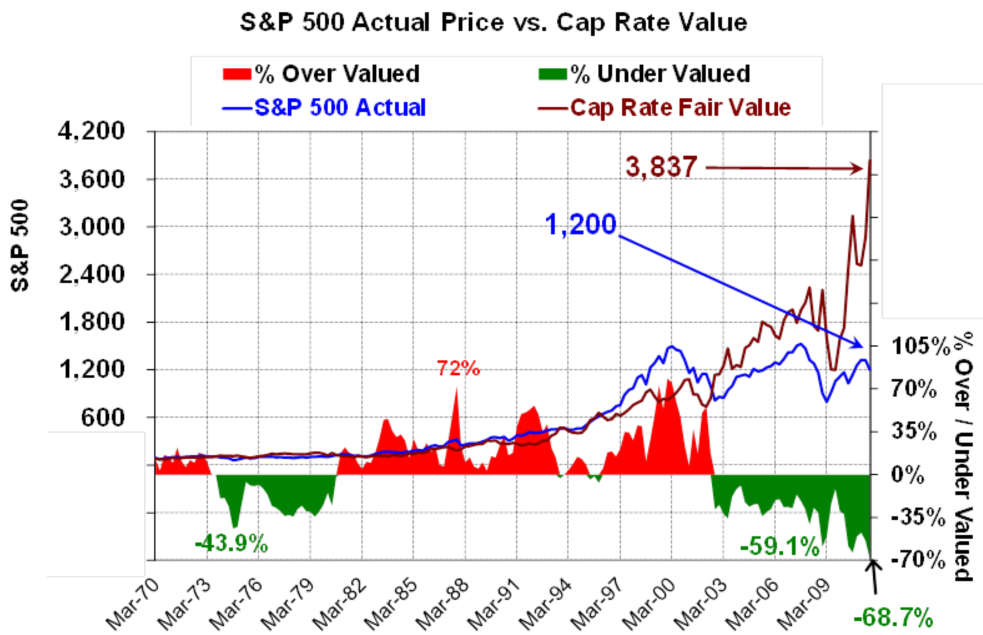
Rising Earnings, Dropping Interest Rates = Cheap Stocks

The spread between the earnings yield (the reciprocal of the P/E ratio, i.e. earnings divided by price) and the 10 year Treasury rate is **the widest since**

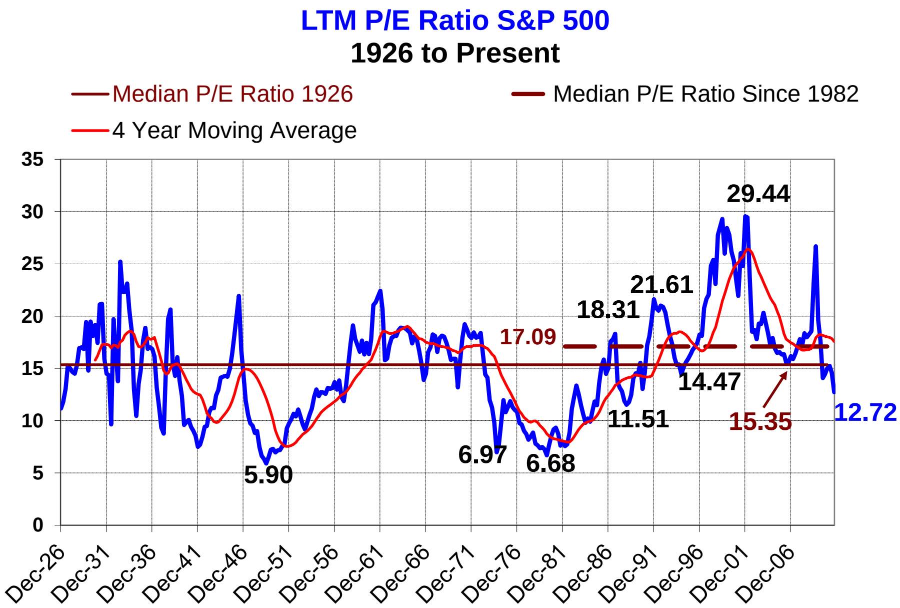
1979 when the S&P 500 gained 12.3% for the year. As I have stated before, **spikes in the spread have been coincident with market bottoms**.



The combination of low Treasury rates and a high earnings yield results in <u>the most extreme undervaluation of the S&P 500 in my data set going back over 40 years</u> to 1970. This market behavior mimics that observed at the panic lows of the last bear market in December 2008 and March 2009 as well as in last year's Q2 correction.



In addition to being undervalued relative to interest rates and the earnings yield, the market is very attractive on a straight forward P/E ratio basis. The P/E ratio on the S&P 500 based on LTM earnings (includes estimated earnings for Q3 11) is now well below the median P/E ratios from 1926 and 1982.



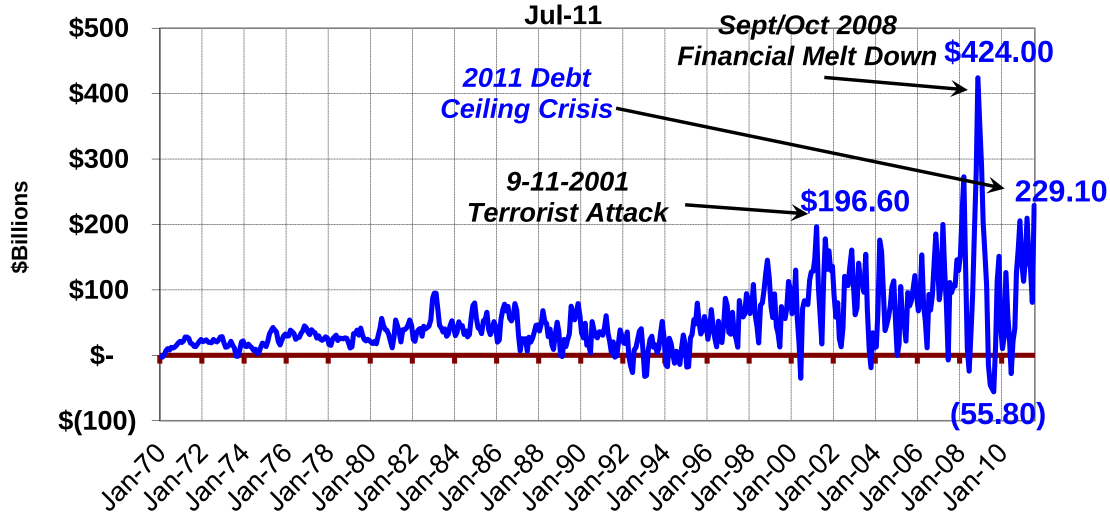
A Pile of Cash, Rising Leading Indicators

The American public has sucked $229 billion out of the economy since the end of April. This rate of cash hoarding is the third highest for any three month period going back to 1970 exceeded only by the panic driven hoarding of 2008. It is no mystery that the leading economic indicators would show some slowing down in Q2 and Q3 in light of the pull back by consumers. Their actions can be understood given the fear mongering that accompanied the debt ceiling debate. Their sentiment has not been helped by the prevailing coverage of the Euro sovereign debt crisis. The good news is that this hoarding process does unwind eventually. There may be a better than expected Q4 economic growth if the American public can regain confidence and restore spending levels in the holiday season.

PANIC WAS RETURNING - PILE OF CASH SUCKED OUT OF ECONOMY IN RECENT MONTHS

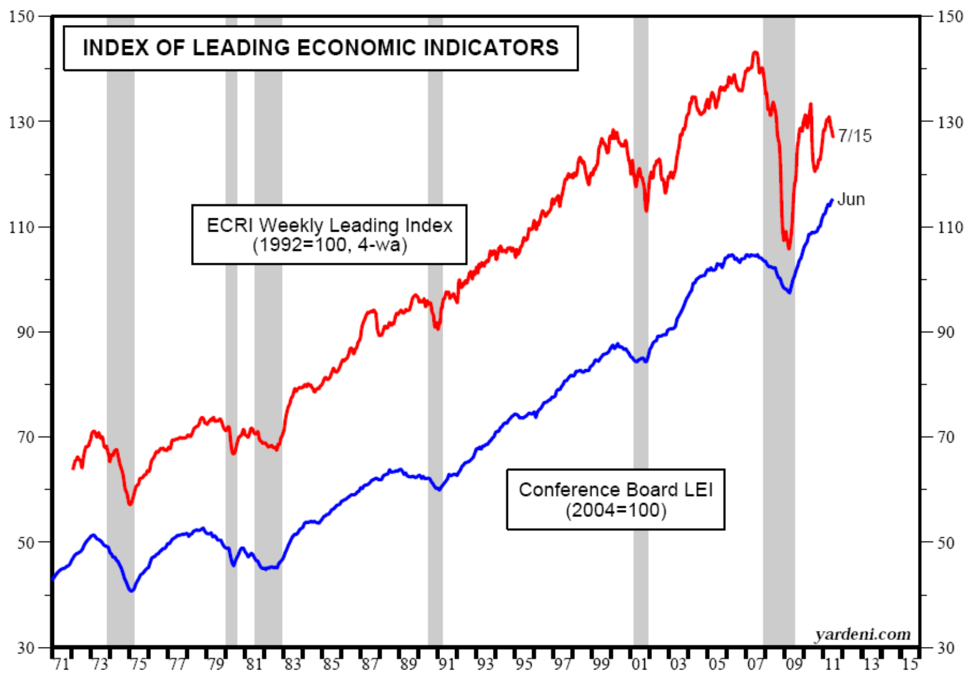
M2 SINCE 1970

Trailing 3 Month $ Change



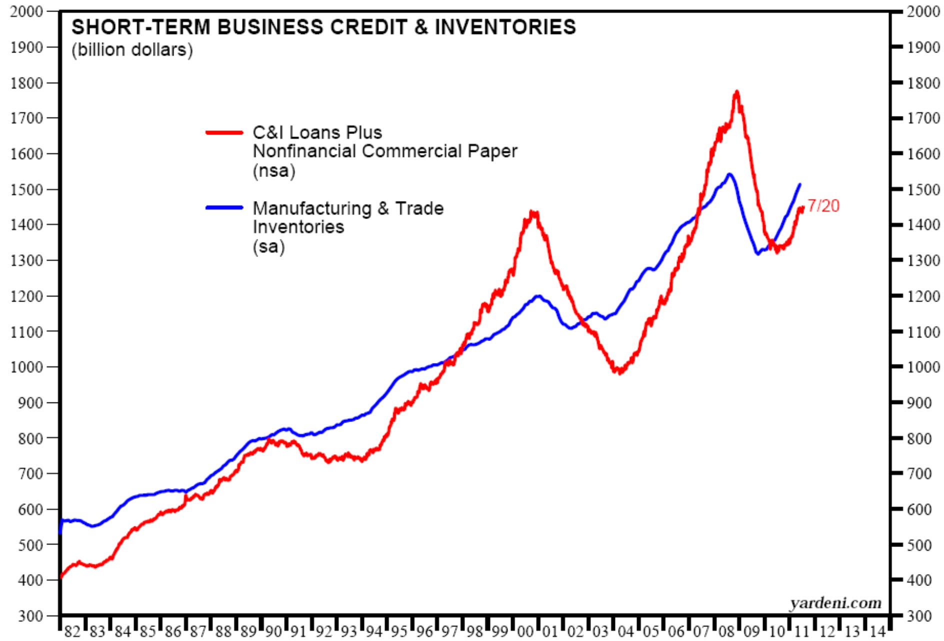
Source: Federal Reserve, not seasonally adjusted

Despite the cash hoarding, the leading indicators are still biased upward.



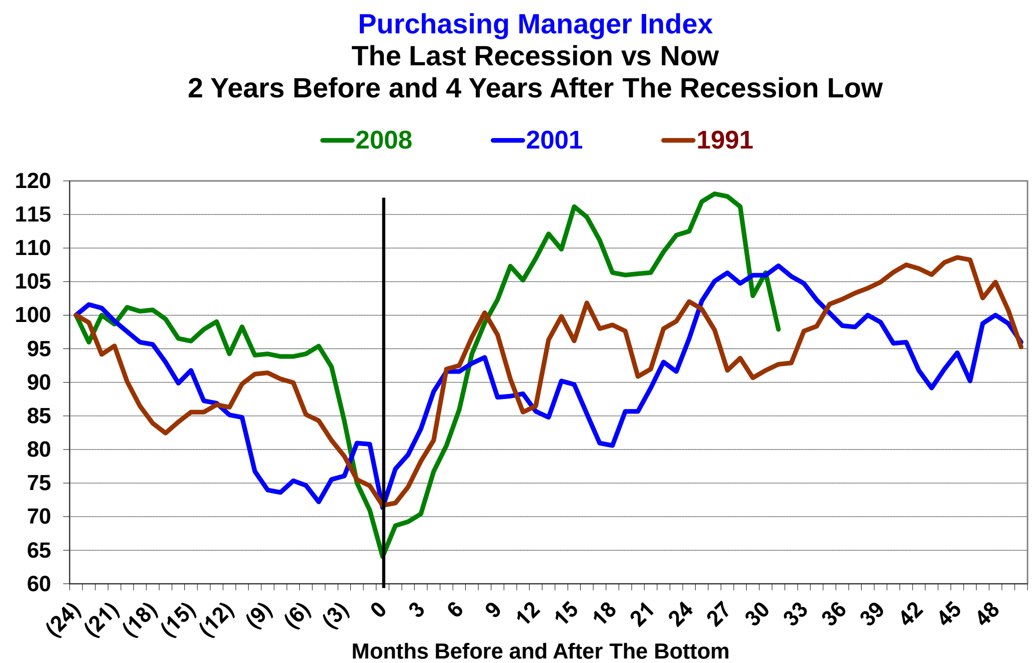
Note: Shaded areas denote recessions according to the National Bureau of Economic Research.
Source: Conference Board and Economic Cycle Research Institute (ECRI).

The gradual recovery in bank lending and inventories suggest we are still in the early – not late – stages of economic recovery.



Source: Board of Governors of the Federal Reserve System and US Department of Commerce, Bureau of the Census.

The market took a dive this week following the release of the PMI on Monday. In a word, people freaked. They overreacted to a somewhat volatile data set that is still performing well compared to prior economic recoveries.



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We are big fans of Warren Buffet. I opened this note with one of his quotes suggesting people should invest when no one else is interested. Given the foregoing information, it is safe to say that we are in a time when few people are interested in investing in equities. I use wildebeests as a metaphor for the "crowd" of normal investors.

As I said in June, it's time to be the lion, not the wildebeest.