



AMERICAN FINANCIAL ADVISORS, LLC

It is unimaginable that there is a person on the planet unaware of the ongoing global recession and bear market. Rather than regurgitate the economic events and government reactions which have been covered ad nauseum (at least that's our feeling), we will focus on current conditions and our expectations. In short, we are cautiously optimistic but believe that this is not the time to be either a raging bull or a raging bear.

While the S&P 500 fell over 11% in the first quarter, it has risen over twenty percent since its low in early March. Is this a new bull market? Is the worst over? The answer to those questions are respectively; no one knows and probably. The markets suffered because there was both a recession and the specter that our financial system would fail (i.e., bank after bank failing in a domino effect). A good part, if not all, of the recent market rally can be attributed to the realization that the risk of systemic financial collapse has receded and thus the worst is over.

Even though the worst is over, the bad news will continue. We expect unemployment to breach the 10% mark, but this expectation is widely shared and priced into the market. As we write this we are in the midst of first quarter earnings releases. While it appears that the economy may stop contracting sooner than had been expected, we remain concerned that the recovery may take a long time.

Volatility remains elevated. This is due to the market sharing our view that the future is even more difficult to predict than usual and a lack of liquidity. The major point is that risk remains.

According to recent news reports, the swine flu outbreak has likely killed more than 100 people in Mexico. On Sunday, the United States declared a health emergency amid signs the disease was spreading. The first case of an infection in Europe has been confirmed in Spain. It looks like the virus can be transferred from human to human, not just from animals to humans. The fear of Swine flu spreading across the globe has put some pressure on stock markets this week. In the 20th century, three influenza pandemics killed over 40 million people ("Spanish influenza" in 1918, "Asian influenza" in 1957, and "Hong Kong influenza" in 1968). This fresh outbreak could easily be contained (like many before) and not be an issue for more than a few days; however, many experts agree that a new pandemic may occur at any time. The Severe Acute Respiratory Syndrome (SARS) outbreak in 2003 clearly demonstrated the vulnerability of the interconnected world to the spread of infectious diseases.

The point we want to make is that any prognostication about where the markets are going, no matter how intelligent and experienced the source, is subject to events that are unpredictable in their timing and magnitude. We pray that this flu is not a pandemic.

While on the subject of predicting the future, we should mention that not all news is bad news, although psychologically we are wired so that bad news has more impact and it is more easily recalled. On a positive note, not all news is bad. For example, technology innovations such as the computer and internet have greatly increased productivity even though their arrival may have caused the demise of other businesses.

Diversification is the best investment strategy for an uncertain future. And since the future is always uncertain, portfolios should always be diversified. In light of the continuing volatility and concerns about a sideways market, we are tilting our allocation to corporate bonds. We think they offer much of the return historically expected from stocks with less risk than stocks. Of course, stocks may outperform bonds. This move is about managing risk rather than reaching for return.

Please feel free to call us or e-mail any questions about your portfolio or other financial matters. As always, we sincerely appreciate your business and value the relationship with our clients. Given the current state of affairs, we all look forward to better, more prosperous times ahead.

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