AMM

AMERICAN MONEY MANAGEMENT, LLC

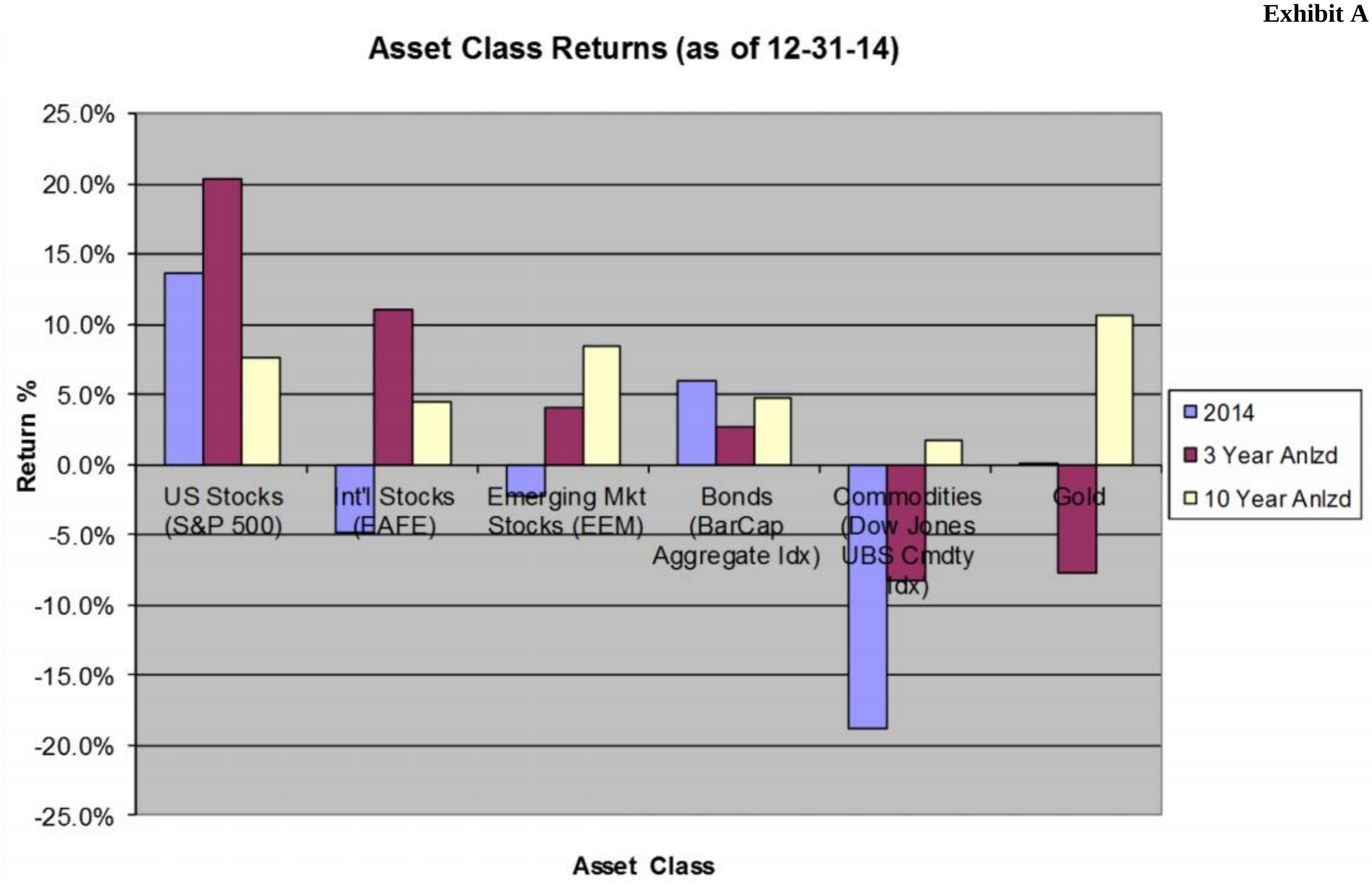
SEC Registered Investment Advisor

PO Box 675203, Rancho Santa Fe, CA 92067 | Tel 888-999-1395 | Fax 866-364-1084 | info@amminvest.com | www.amminvest.com

HAPPY NEW YEAR ~ 2014 IN REVIEW

Through 12/31/14, domestic stocks (S&P 500) increased 13.7%, developed market international stocks (EAFE) declined -4.9%, and emerging market stocks (EM) declined -2.2%. Bonds (Bar Cap Agg Idx) were up 6%, commodities were down -18.8%, and gold was roughly flat for the year. We have updated our asset class return chart (Exhibit A) to reflect Calendar Year 2014 along with three and ten year annualized returns for the aforementioned asset classes.

Exhibit A



The weak performance from non-domestic stocks and diversifying assets meant that broad diversification worked against portfolio returns in 2014 (i.e. if you were broadly diversified away from US stocks, your return was lower than the S&P 500). Some may even go as far as to question the need for broad diversification in their portfolio strategy in a year where simply being in the S&P 500 would have yielded very satisfactory results. Of course, it was only a few short years ago that investors sought shelter *away* from US Stocks in many of the same diversifying assets that have underperformed in recent years.

Rather than try to predict which way the wind will blow in any given year, our investment approach is grounded in our 5 core investment principles. We believe following these principals give all of our clients, whether aggressive, conservative or somewhere in between, the best odds of managing risk and achieving their investment objectives.

(OVER)

AMM's 5 Core Investment Principles

1. Asset Allocation is the most important decision: What percentage of your portfolio should be in stocks, bonds, cash, etc., in light of your financial condition, risk tolerance and goals? While the asset allocation decision varies across investor type (i.e. more aggressive investors tilting more towards stocks, while more conservative investors will lean towards bonds), some degree of prudent diversification is a helpful guard against an unexpected shock to one part of the portfolio. Even an aggressive pure stock portfolio should invest in a basket of stocks as opposed to investing solely in one or two stocks. Like insurance, you don't really want it until you need it, but by then it's too late.

2. Volatility is not risk: We view volatility as the proverbial red herring in investing. When volatility spikes and prices decline, it can trigger otherwise rational and prudent investors to abandon their well-conceived investment plan in the name of reducing risk. At AMM, we have collectively been managing money professionally for several decades and can attest to the fact that appropriately dealing with market volatility is one of the hardest and, at the same time, most important attributes of the successful investor.

We define real risk as the likelihood of a permanent loss of capital. We assess this risk before making an investment and reassess throughout the life of the investment. Unless you are a highly leveraged investor, *volatility is not the cause of permanent capital loss*. However, selling an otherwise sound investment simply *because* of volatility can cause a permanent loss of capital. We do not suggest that you should never sell at a loss; however, this decision should be made for fundamental reasons, not simply because of a price decline.

3. The price you pay determines your potential return: The lower the price paid for an investment, the higher the return potential. As simple as this sounds, it becomes more difficult to do in practice as investments are generally "low priced" when there is significant uncertainty and/or fear surrounding the investment. For example, many oil stocks have come down significantly in price over the last quarter. All else being equal, they are now priced for more attractive long-term returns than they were 3 months ago. The "crash" in the price of oil mixed with fear and uncertainty has provided an opportunity for long-term value and dividend oriented investors. In our firm's Dividend Strategy, we have been investing in large integrated oil companies for some time and have used the recent selloff to add to positions that we believe remain fundamentally sound regardless of the recent decline in the price of oil.

4. Time is your ally, but returns are not linear: Investment success is not about timing the market but the time you put in as an investor. Long run investing allows you the ability to follow core principals 2 and 3 since it buys the precious time to ride through volatility and let your attractively priced (but out of favor) investment selections work. Since 1980, the stock market (S&P 500) has an annualized price return of 8.7%; however, over this time frame, the average intra-year decline was -14.2% with 7 of the 35 years posting negative calendar year returns. Market declines and negative years are quite common and, in hindsight, have provided opportunity for the unemotional investor.

5. You can't predict the future: All too often, investors focus on trying to predict short-term economic and market outcomes and do not focus enough on long-term fundamentals and valuations. The financial media does not generally help in this regard as the "long-term investing" story doesn't get the ratings. Instead, intelligent market prognosticators who can make a persuasive case about the market's next move instill a sense of urgency in the reader, listener and viewer. Rather than trying to predict the future, we attempt to understand the present investment environment and invest according to principles 1 through 4.

The key takeaway from our core principles is that investing is a long-term venture. Do your best to develop an asset allocation strategy appropriate to your risk tolerance and time horizon and adjust as your circumstances change; focus on paying a fair or discount price for investments; manage real risk but don't fret volatility; and avoid trying to predict the market's next big move. As your investment advisor and money manager, we will continue to follow these principles to help you meet your goals and objectives in 2015 and beyond.

Where We Are Investing Capital Now*

<u>Fixed Income (Bonds):</u> For many years now, the low level of interest rates has concerned us as an eventual rise in rates will negatively affect bond portfolios (bond prices generally move inverse to interest rates). Longer maturity bonds will be hurt more than shorter maturity bonds from a rise in interest rates. For example, a 1% rise in interest rates will cause a decline of around -2% in the value of a 2 year treasury bond and a decline of -17% in the value of a 30 year treasury bond. Though the bond holder is fairly certain to get their principal back at maturity, 30 years is a long time to wait to get paid off.

The fundamental question for bond investors in today's low rate environment is whether or not they should 1) take significant interest rate risk in exchange for slightly higher yields or 2) live with lower returns in shorter-term maturities which have much lower interest rate risk. For those clients with bonds, we have mostly chosen the latter option. We think accepting lower shorter-term bond returns makes more sense than exposing our clients to the possibility of potentially large losses in the event that rates rise quickly and unexpectedly. In 2014, this worked to our detriment as long-term bonds rallied strongly and long-term bond rates declined even further. Currently, we do not plan to make any significant changes to our fixed income portfolio strategy.

<u>Stocks:</u> Referring to Sir John Templeton's famous phrase -- "Bull markets are born on pessimism, grow on skepticism, mature on optimism, and die on euphoria" -- it appears from our vantage point that we are in the third mature phase of the bull market in US stocks that began in 2009. The irrational euphoria that seems to signal bull market tops *("it's the new economy, companies don't need earnings", "housing never declines")* doesn't appear to have taken hold. Still, domestic stocks are not nearly as attractively valued as they were a few short years ago and at best, investors today are paying a fair price for domestic stocks on average.

Some market participants have worried that the Fed's expected rate tightening cycle which is forecast to begin in 2015 could be the catalyst for halting the current bull run. However, history (Exhibit B) suggests that the action of stocks in the 6 months following the first Fed rate hike was actually positive.

Exhibit B

Based on Fed tightening cycles since 1962. Discount rate used prior to 1984; fed funds rate used since 1984. S&P 500 price only performance. Source: Birinyi Associates, Inc.

We continue to tilt domestic stock exposure towards large cap dividend paying holdings and growth oriented positions, where applicable. Our selection of dividend stocks remains focused more on a company's ability to grow their dividend, which we feel provides both an inflation hedge and growing income stream in the future, as opposed to the absolute value of the dividend yield.

(OVER)

(Where We Are Investing Now cont.)

Relative to US stocks, we continue to see better overall value in International and Emerging Market (EM) stocks. As you can see from Exhibit A, both markets have lagged the US in recent years. Referring again to the Templeton quote, International and Emerging Market stocks appear to us to be trapped in the pessimism and skepticism phase of a bull market. There are, no doubt, a myriad of issues facing the Eurozone including high overall unemployment, a deflationary environment in the periphery countries like Greece, and negative credit growth from both households and non-financial corporations. However, as we describe in core principle #3, the price you pay determines your return, and for long-term investors who can see through the short term woes, these markets appear to provide better value investment opportunities than the more fairly valued US market.

Diversifying Assets: These assets, by definition, do not have a strong correlation to stocks or bonds and, therefore, increase portfolio diversification. Depending on a client's particular investment strategy, we have included exposure to these assets (including most recently gold and commodities) at varying weights overtime. In 2014, both commodities and gold suffered declines. The continued strength in the dollar meant that the demand for gold as an inflation hedge was limited.

Additionally, the steep and rapid decline in the price of oil (a large weighting in DJ UBS Commodity Index) in the fourth quarter caused a broad basket of commodities to decline. So far, the market action seems to have emphasized the negative aspects of a decline in oil, notably that Gross Domestic Product (GDP) growth will suffer as oil/energy industry capital spending declines. However, oil/energy capex (companies purchasing equipment, etc.) represents roughly 1.2% of GDP, while 68% of the US economy is driven by consumer spending. The decline in energy prices is a big benefit to the global consumer. But if oil remains low, we believe demand both domestically and abroad will expand and ultimately drive prices higher.

**Individual accounts will vary based on the client's stated objectives, risk tolerance, and time frame. We manage several different portfolio strategies, so not every client has exposure to the securities or asset classes listed above. In addition to growth and/or income oriented asset allocation strategies, we also manage more concentrated equity portfolios that generally carry a higher degree of risk and volatility. Please contact us if you want to discuss your portfolio strategy in greater detail.*

Enclosed is a copy of our Privacy Notice. We can also provide you with a current copy of our SEC Form ADV Part II, at your request. Should you have any questions regarding your investment account(s) or, if there have been any recent changes to your investment and/or retirement objectives, please do not hesitate to contact our office.

As always, we thank you for entrusting AMM to help you achieve your investment and retirement objectives.

Your Portfolio Management Team

Gabriel Wisdom — *Managing Director*
Michael Moore — *Chief Investment Officer*
Glenn Busch — *Portfolio Manager*
Vicki Ohara — *Operations Manager*
Jim Rhodes, CFA — *Executive Director*
Mike Green — *Portfolio Manager*
Adele Canetti — *Portfolio Manager*
Robert Frazier — *Investment Advisor*
John Nyaradi — *Investment Advisor*
Bryan Case — *Investment Advisor*

AMERICAN MONEY MANAGEMENT, LLC

14249 Rancho Santa Fe Farms Road
PO Box 675203
Rancho Santa Fe, CA 92067

Tel: (888) 999-1395 Fax: (866) 364-1084 E-mail: info@amminvest.com www.amminvest.com