

Investment & Market Commentary

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Following is the performance of our American Hero models, BEFORE fees and expenses. The S&P total return figures are figured for year-to-date and cumulative as of 12/31/09.

	Year to Date Jan - Dec 08	Inception to date	Inception date
Equity	-33.63%	+6.98%	4/30/04
Equity Plus	-33.75%	+8.29%	4/30/04
Balanced	-27.00%	+9.28%	4/30/04
Conservative	-19.72%	-19.72%	12/31/07
Defensive	-12.49%	-12.49%	12/31/07
S&P 500	-38.50%	-18.43%	04/30/04

We are pleased with the good relative performance in 2008. However, we are disappointed to have managed portfolios that declined so sharply. Following is our **market commentary** (including our market outlook), our recent **business decision** about asset allocated portfolios and **investment management** highlights.

Market Commentary

Past. The fourth quarter decline in stock prices culminated five quarters of weakness following the market peak in October 2007. Fundamentals weakened during 2008 as three speculative bubbles deflated - home prices, oil prices and debt.

In September, credit markets froze. Credit default swap problems forced the largest investment banks out of business. Major commercial banks required special help from the federal government to continue. The election-oriented media amplified the problems.

Panic struck in the fourth quarter as the stock price volatility increased and stock prices fell sharply in October and further in November. Major Indices were 40-50% below October 2007 peaks.

In December, economic and political news worsened. Unemployment rose, the economy contracted and deflation occurred despite the inflationary impact of the Federal Reserve's sharp increase in money supply. However, the market rose, perhaps anticipating improvements in 3-6 months. This rise continued in 2009, before weakness reappeared in mid-January.

Outlook. Bulls and bears make compelling cases for the market outlook.

Bulls cite **possibilities**: large cash on the sidelines ready to buy stocks; many healthy companies; relatively low stock valuations; many oversold stocks; and improvement in investor sentiment. A spark of good news could ignite further gains.

Bears cite **unknowns**: impact of sharply increased role of government in the economy, such as the increased the tax and spend bail-

outs; the negative impact of unwinding excessive consumer debt; and ongoing concerns about soft consumer spending (about 70% of the US economy). More bad news in 2009 could cause a retest of November lows and delay the economic / stock market recovery.

We join Warren Buffett in the bullish category – better to have faith when others fear. However, the timing of the upturn is not accurately predictable. Was November the bottom? Will there be new lows in early 2009? We think the market will be higher by yearend, but interim lows are quite possible, perhaps a 30% probability ... sizable, but not most likely.

Business Decisions

American Values is changing its investment approach slightly. Our thinking in making the change follows. We considered the American Values strengths, which include: **Values Research** – we lead in positive values research; our comprehensive 500-point, positive-values scoring system is uniquely good; **Performance** – The benchmark trend performance of our, multi-cap blend portfolios exceeds the averages; and **Team** – a qualified American Values leadership team is in place for almost six years. Based on these strengths, we think American Values is uniquely positioned to serve the values-oriented investors in the individual and institutional markets.

To meet the needs of these two markets, we are adjusting our asset allocation to the following five portfolios.

	<u>Stocks</u>	<u>Bonds</u>
American Hero 100	96%	4%
American Hero 75	75%	25%
American Hero 50	50%	50%
American Hero 25	25%	75%
All Bonds	0%	100%

Institutions will probably focus on the all-stock, All American Heroes. It utilizes both our pace-setting positive values research and our tested portfolio management expertise.

Individuals (and their advisors) will probably select the asset-allocated portfolio that best fits the risk profile of each investor.

All American Heroes replaces both Equity and Equity Plus. (Most view REITs, about 20% of Equity Plus, as financial stocks, rather than a separate asset class.) American Hero 75 is similar to Balanced. The less risky American Hero 50 and 25 provide asset allocations for lower risk investors. All Bonds contains the two bond ETFs and the Capstone Church Bond fund - we currently use all three.

These new portfolios have 24 stocks, small enough for the benefits of concentration, but large enough to be diversified. This implies a 4% average stock holding. These five new asset allocations reflect our decision to emphasize our two main strengths - values research and investment management.

Please contact your advisor with questions about the portfolio that is best for you.

Investment Management

The dramatic, fourth-quarter stock price decline and these changes in asset allocation led to an acceleration of our annual, in-depth review of investment strategy, tactics and fundamentals. We recently completed this review. The portfolios were adjusted to reflect both this review and these asset allocation changes.

Our weightings continue to be within the 50% minimum and 200% maximum range of the 7 largest S&P sectors. We favor sectors with better near / intermediate term prospects.

To implement these changes, we retained 18 American Hero stocks. Only 6 new Heroes were added to create our 24-stock, diversified model portfolio. We like to find and own good companies for the long term. We use a mix of stocks with good exposure to the expected 2009 market gain (70% probability) plus resistance to an interim market decline (30% possibility).

Modern portfolio theory statistics are of less certain value because of the recently increased stock price volatility and sharp market declines. Yet, we monitor them. They continue to show: above average **alphas** (good stock selection), below average **betas** (less volatility than the market) and above average **Sharpe ratios** (good risk-adjusted return).

We appreciate serving you in these difficult times. We view the disappointments of 2008 as God's appointments. They are consistent with God's eternal will and glory and for our good. We continue to seek the best risk-adjusted, long-term return that is consistent with our "Values-First" investment strategy.

On behalf of George Parks (Committee Chairman) and Carter LeCraw (American Values President), we welcome your comments, questions and prayers that God will provide sound judgment for all of us on The Investment Committee.

As noted earlier, please contact your advisor with questions about the new asset allocation.

Note: Please contact your advisor if there are any changes in your financial situation or investment objectives, or if you wish to impose, add or modify any reasonable restrictions to the management of your account. Our current disclosure statement is set forth on Part II of Form ADV and is available for your review upon request.

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