American Financial Advisors, Inc.

Quarterly Portfolio Review

September 30 2014

Quarter in Review

As we enter the final quarter of the year, let's take a look back at the 3rd quarter:

- The third quarter marked a return to earth for funds that specialize in stocks of smaller companies. Funds investing in a mix of small-cap growth and value stocks fell an average 6.8 percent. Last year, those same funds were stars, returning an average 37.4 percent. At the time, investors were snapping up smaller companies on expectations that their earnings would grow faster than those of big companies.

- The mutual funds that form the core of most investors' bond portfolios, intermediate-term bond funds, were essentially flat last quarter. They lost an average 0.1 percent. It's a letdown from the first half of the year, when intermediate-term bond funds returned 4.1 percent. All of the other 31 categories of bond funds tracked by Morningstar also registered gains in the year's first six months, benefiting from an unexpected drop in interest rates. When rates are falling, it causes the price of existing bonds to go up as their yields suddenly look more attractive.

- Gold-related funds were the quarter's biggest losers. All 10 mutual funds with the worst returns focus on gold stocks. Low inflation and expectations for rising interest rates usually mean investors sell gold, and its price fell to its lowest level since Jan. 2.

A leaf touches down

Rippling the flames of autumn

Burning on the lake

BENCHMARK CENTRAL 2014

Index	Return
Barclay's Aggregate Bond Index	4.09%
MSCI EAFE (International Stock index)	-3.52%
Russell 1000 Value (US Large Cap Value index)	6.21%
Russell 2000 (US Small Cap index)	-5.32%
S&P 500 (US Large Cap index)	6.70%
Wilshire 5000 (US Total Market index)	5.35%

To Our Valued Clients...

One of the most overlooked responsibilities of the AFA Investment Committee is reviewing the changes we have made to our portfolios in the past. While most of our time is spent managing the current portfolios, it is essential that we review the decisions we made previously to determine whether they worked out or not. The most recent change was made was to eliminate Commodities from our portfolios and replace them with Inflation Protected Securities (IPS).

Commodities, such as gold, oil or corn, offer a hedge against inflation. Because commodities prices usually rise when inflation is accelerating, they offer protection from the effects of inflation. Few assets benefit from rising inflation, particularly unexpected inflation, but commodities usually do. One other security that DOES offer the same hedge is Inflation Protected Securities.

Back in March, 2010, or just over 4.5 years ago, we sold DBC (a commodity Exchange-Traded Fund or ETF) and replaced it with DIPSX (a mutual fund focused on inflation protected securities or IPS). The reason we made this change was that as inflation hedges, the IPS provided the same hedge with much less volatility than the commodities did. Since I can't go back exactly 4.5 years, we present the five-year figures below:

- DIPSX 5 year average return +4.76% with 5.72 standard deviation
- DBC 5 year average return +1.03% with a 16.72 standard deviation

In this case, our committee made the right call. The IPS offer more than four times the return with roughly 1/3 the risk...the exact scenario we were looking for. Let's hope future changes yield equally encouraging results!

Quarterly Client Webinar

Starting date: Thursday, October 16th, 2014 Starting time: 12:30 pm, Eastern

Meeting Number: 193 720 149

Website link: https://signin.webex.com/collabs/#/meetings/joinbynumber?TrackID=&hbxref=&goid=attend-meeting

To join the teleconference only: US TOLL: +1-415-655-0001 Access code: 193 720 149

If you cannot join us for this important webinar, we will post a recording of the entire presentation on our website at www.afadvisors.com.

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