Sound Investments Inc.

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Summary

The recent uptick in price could be a sign that some of the fear gripping investors around the world is abating. Worldwide investors are no longer selling shares indiscriminately, but selecting based on prospects for economic recovery even if earnings for the year remain scant.

As I write this in late Apr stocks have appreciated over 30%, but there are clear signs that stocks are overdue for at least a pause. A whopping 84% of stocks are above their 50-day moving averages. To buy here implies a degree of confidence in a share recovery that does not jibe with the available evidence. However I am studying 3 areas that I am using as a buy list outlined as follows: 1. well known companies like Heinz, Eaton, AT&T, 3M, Unilever etc. all pay dividends of over 5%. These stocks are down almost 50% and while it may take some time for the earnings to recovery, you are paid to wait. These are great yields. 2. There are a number of high growth companies that growing by over 20% a year for instance, The best way to play this is through growth-orientated mutual funds. 3. There are some opportunities in the less developed countries particular in China and India.

The Investment Letter is mailed quarterly to our clients and friends. The intent of this publication is to share some of our more interesting views and research.

Signs of Life

Although stocks posted their sixth consecutive losing quarter last month the S & P gained 8.9%. Stocks surged from the Mar 9th lows and enjoyed the steepest rally since 1938. However, in the context of the preceding free fall, it feels anything but normal. After what we have been through, and amidst such volatility, it is a challenge to be confident. People become irrationally pessimistic during downturns.

Yet, we know the economy will not contract indefinitely and already there are signs of hope that it is bottoming. Positive news is starting to appear. Six out of Ten leading indicators were up in Feb. Other economic news were also positive with retail and construction reports better than expected. Let us not ignore the negative affect that our current surging unemployment rate is having on consumer spending and confidence.

Historically, the stock market has been a leading indicator of the economy. Over the past 60 years recessions normally end four of five months after a new bull market begins. It is interesting to note the S & P 500 index has correctly anticipated the end of the recession nine out of ten times

Buyers Appear

The recent uptick in price could be a sign that some of the fear gripping investors around the world is abating. Worldwide investors are no longer selling shares indiscriminately, but selecting based on prospects for economic recovery even if, earnings for the year remain scant.

There is no question that this recession will be the largest in the post World War II. We would not be surprised to see a peak to trough real GNP decline in the range of 5% to 6% when the final numbers are tabulated. For comparison, the 1973-1975 and 1982- 1982 recessions peak to trough declines were 3.18% and 2.9%. This recession has also shown higher unemployment currently at 8% and expected to peak at 9.0% in the 4th quarter of 2009.

Any ensuing business recovery will most likely be slow and uneven. The damaged suffered over the past year and a half – most notably from the stock market and home prices - has been so extensive that the kind of consumer spending and industrial expansion needed to generate strong levels of economic growth may well be slow to evolve. The forecasters are looking at a flat 3rd and 4th quarter of 2009 and do not expect the recovery to really get underway until 2010.

Any economic recovery should be kept in perspective. For example, while housing has lifted off its recent lows, it is still off 80% from the levels of several years ago. Multi lows are still in sight for consumer confidence and manufacturing while troubles continue to mount in the auto industry. Finally, earnings are falling noticeably for many companies with some cutting dividends in order to prop up their balance sheets.

Keep your Eye on the Prize

Sometimes, especially when news is dire and markets move against us, we tend to forget our long-term goals and become preoccupied with short-term volatility. Declines in the stock market have scared some investors away from stocks and most are wondering if it is a good time to get back in.

Realistically regardless of whether the market is at bottom, if you need to grow your portfolio you need to be in stocks. With cash and bonds the yields are so low most of us most of us have to take some risk, in order to make a return on our investments.

So What Should We Be Looking at Now

As I write this in late Apr, stocks have appreciated over 30% but there are clear signs that stocks are overdue for at least a pause. A whopping 84% of stocks are above their 50-day moving averages. To buy here implies a degree of confidence in a share recovery that does not jibe with the available evidence. However I am studying 3 areas that I am using as a buy list outlined as follows: 1. well known companies like Heinz, Eaton, AT&T, 3M, Unilever etc. all pay dividends of over 5%. These stocks are down almost 50% and while it may take some time for the earnings to recovery, you are paid to wait. These are great yields. 2. There are a number of high growth companies that growing by over 20% a year for instance, The best way to play this is through growth-orientated mutual funds. 3. There are some opportunities in the less developed countries particular in China and India.

Conclusion

We continue to think the markets tug of war will be eventually be won by the bulls, assuming steps to counter the recession are effective and efforts to calm a more jittery world bears fruit. Now, however volatility in the stock market is likely to remain high as the recession traverses a painful path and gradually works its way out.

I attached an interesting newspaper article on the differences between Registered Investment Advisor and a stockbroker / advisor at a company like Merrill Lynch, Smith Barney or Edward Jones. I became a Registered Investment Advisor to put my client's needs first. When I was a stockbroker in the 1980's, I was forced to sell new issues I did not believe in and could only sell mutual funds with high expense ratios and it does not look like too much has changed. I put my client's interest first and disclose any conflicts of interest.

Sound Investments Inc.
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THE INTELLIGENT INVESTOR

The Fight Over Who Will Guard Your Nest Egg

A power struggle in Washington will shape how investors get the advice they need.

On one side are stockbrokers and other securities salespeople who work for Wall Street firms, banks and insurance companies. On the other are financial planners or investment advisers who often work for themselves or smaller firms.

By Jason Zweig

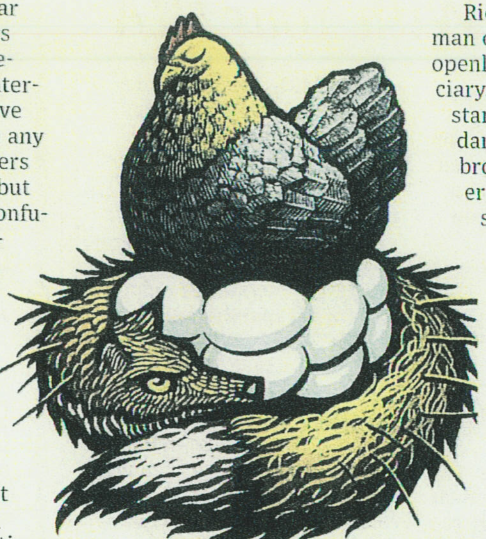
Brokers are largely regulated by the Financial Industry Regulatory Authority, which is funded by the brokerage business itself and inspects firms every one or two years. Under Finra's rules, brokers must recommend only investments that are "suitable" for clients.

Advisers are regulated by the states or the Securities and Exchange Commission, which examines firms every six to 10 years on average. Advisers act out of "fiduciary duty," or the obligation to put their clients' interests first.

Most investors don't understand this key distinction. A report by Rand Corp. last year found that 63% of investors think brokers are legally required to act in the best interest of the client; 70% believe that brokers must disclose any conflicts of interest. Advisers always have those duties, but brokers often don't. The confusion is understandable, because a lot of stock brokers these days call themselves financial planners.

Brokers can sell you any investment they have "reasonable grounds for believing" is suitable for you. Only since 1990 have they been required to base that suitability judgment on your risk tolerance, investing objectives, tax status and financial position.

A key factor still is missing from Finra's suitability requirements: cost. Let's say you tell your broker that you want to simplify your stock portfolio into an index fund. He then tells you that his firm manages an S&P-500 Index fund that is "suitable' for you. He is under no obligation to tell you that the annual expenses that his firm charges on the fund are 10 times higher than an essentially identical fund from Vanguard. An adviser acting under fiduciary duty would have to disclose the conflict of interest and tell you that cheaper alternatives are available.



Heath Hinegardner

If brokers had to take cost and conflicts of interest into account in order to honor a fiduciary duty to their clients, their firms might hesitate before producing the kind of garbage that has blighted the portfolios of investors over the years.

Richard G. Ketchum, chairman of Finra, has begun openly using the F-word: fiduciary. "It's time to get to one standard, a fiduciary standard that works for both broker-dealers and advisers," he told me. "Both should have a fundamental first responsibility to their customers."

When I asked whether Finra should be that single regulator, Mr. Ketchum replied: "Do we have the infrastructure and would we do a good job? We think yes."

Others disagree. "It would be lethal if Finra becomes the only regulator," retorts Tamar Frankel, a professor of securities law at Boston University. "Finra has an inherent conflict of interest, because it's the same people regulating themselves."

In testimony to the Senate in the past week, SEC Chairwoman Mary Schapiro said the agency is considering "whether to recommend legislation to break down the statutory barriers" that impose different regulations on brokers and advisers.

Ms. Schapiro stepped down earlier this year as head of Finra to lead the SEC. In 2005, when she was vice chairwoman of Finra's predecessor, Ms. Schapiro wrote a scathing letter to the SEC calling "this much-vaunted fiduciary duty ... imprecise and indeterminate."

When I asked her now if she still held that view, Ms. Schapiro replied: "I wear a new hat now. I completely get that I work for America's investors, so my perspective has changed. I think investors would rationally say that they prefer fiduciary duty as the standard of care. And they are entitled to have their interests come first, always."

Ms. Schapiro said it is too early to say who should be the lead regulator if brokers and advisers are brought under the same set of rules.

Ms. Schapiro sounds sincere, and they say there is no zeal like that of the convert. Here is hoping she means what she now is saying, and that Congress—and the investing public—will hold her to it. It is high time for everyone who says "Trust me" to be held to the highest standard.

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