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**Subject:** **April Market Turmoil**
**Date:** May 6, 2010 5:16:07 PM EDT
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MIP McKee Investment Planning

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Dear Clients,

The markets had a wild day today with the Dow Jones Average actually went down by almost 1000 points for a few moments, closing down about 350 points.

So what happened? There are a few answers and how much each contributed is subject to debate.

However, before we go into it, I need to reiterate my overall analysis on where we are in the global economic situation. I will keep it short and high level. While the US is in a "rebound" mode right now, I believe it to be short-lived and primarily based upon excess government stimulus that did not solve the underlying fundamental problems. The US dollar has been propped-up for 3 decades by its use as the customary monetary unit for use in the global trade of oil. A side effect of that fact was the US dollar's adoption by most foreign countries as the "reserve currency" which further stoked demand for the US dollar and has kept its value above equilibrium and continues to do so. That will come to an end and the evidence that it will happen continues to mount. In addition, we haven't even scratched the surface of our debt, both government and personal. In trying to "restart" the US economy, the government actually increased the debt and further hampered the near-term future of our country. The balance of global economic power is moving towards Asia and the areas of the world that have solid balance sheets. Asia went through a financial crisis in the 90s and they appear to have learned that a strong balance sheet will trump stimulus spending. So, all in all, I believe that the US will lose ground to Asia in the intermediate term.

Now onto the day's events: I would cite a few sparks that possibly ignited today's selloff.

1. Greece - Uncertainty in the outcome of Greece's debt plan and the media stoking the fire by speculating that if Greece defaults on its bonds, then Portugal and Spain will follow and the whole European Union will follow suit. Credit ratings companies recently noted that they are considering a lowering of the credit rating of Portugal. Keep in mind that these are the same credit reporting agencies that rated all the Lehman Brother's bonds at "investment grade" just prior to Lehman disappeared. We have to remember that Argentina and much of Latin America went through a rash of debt defaults in the 80's and we lived through it. Japan and much of Asia went through it in the 90s. Even if Greece defaults, it would create a very small void which would be seen as a buying opportunity for Asian companies to gain power and presence in Europe. There would be some short-term fallout, but it wouldn't be the end of the world.

2. Natural Cycles - No market can move in a straight line forever, no matter what the direction. The media and worldwide communication networks exacerbate the ups and downs by 24/7 coverage of every move. Looking forward, I anticipate stronger movement in each leg of the cycle, both up and down, due to the media "herding the masses" into thinking one way or another. Volatility will only increase moving forward.

3. Program Trading - There are computer models that use quantitative methods to determine when to sell and when to buy based upon the movement of the market. These models first came to light during the market crash of 1987 and are used today to an exponentially greater extent. They sell when stocks are going down and buy when they are moving up (that is overly simplistic, but you get the idea.) There was even multiple reports today that there was a mistake at one of the trading desks where an order to sell 16 million dollars worth of stock was entered as 16 billion. That is yet to be confirmed as a concrete fact, but shows the extent of the confusion around the volatility today.

4. Fear - Need I say more? If we are controlled by our fears, we have already lost.

In summary, I would not take this as a selling opportunity. To the extent that we have some liquidity in the portfolio, we have to look for bargains in the market that are created by fear and panic. Our investments have a strong gearing towards Asian markets which WILL go down due to this fear. However, when we can continue to reallocate assets at a favorable price, I will look to do so. As always, it will be at a measured pace, not all at once, and will be allocated to the parts of the world which will fill the voids left by debt-ridden countries.

Apple:
For those of you with Apple stock, consider this. When we were heavy buyers of Apple, fear was gripping the markets. At that time, I thought Apple should have been priced at about $200 but the market had it at less than $100. Since then, Apple has reported record sales, earnings, and cash flow for 7 straight quarters and have doubled their earnings and cash flow. Based upon their current financial statements, I would now estimate Apple stock to be worth slightly more than $300. That is roughly 30 times their last year's earnings and 25 times their "free cash flow". Historically, the market has priced Apple stock at an average of 30 times earnings and has priced it as high as 50 times earnings. Currently, it is at 21 times earnings. The company has continued to keep its strategy in place, still has no debt, has cash in the bank to the tune of $41 Billion, and is gaining market share in all product lines. Since we captured our cost in the stock last year, I am not inclined to sell under $300. If the market priced it at $310 in the near future, then you would expect me to sell it. We would then wait and buy it back when the market had another bout of fear-driven selling and pushed the price back to $150.

Best Regards,

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