Tarheel Advisors Newsletter

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The Health Care Bill and Me

I think it's safe to say that everyone has heard their fair share of commentary on the Health Care and Education Reconciliation Act of 2010 (H.R. 4872). Regardless of your personal feelings about this landmark legislation, it certainly has become a complex and polarizing force in the business community. Rather than focus on individual health consequences, or the overall impact on the budget deficit, I thought it would be far more relevant to our readers to discuss how the bill will impact your portfolio and personal finances. I apologize in advance for leaving out certain details, as it would be impossible to synopsize a 2000 page document in 500 words!

Roughly a week after the bill was signed into law, the S&P 500 was up a little over 1% -- hardly the major move that many pundits expected. In the short-term, I think this conveys the efficiency of the Stock Market as a forward-looking mechanism, meaning that the inevitability of the bill's passing was already priced in. Where does that leave us now? Moving forward, I believe the truly complex nature of this bill has not been totally digested by the Market. For instance, we are now seeing companies such as AT&T take write-downs of $1 billion to comply with financial accounting rules that require corporations to immediately restate their earnings to reflect the present value of their long-term health liabilities. According to a recent estimate, the cost to corporate America for retiree drug benefits will total $14 billion this year. Whether these corporations were previously operating under a "loophole" or not, these write-downs will greatly affect the 1st quarter earnings season that begins in mid-April. Lower earnings typically translate to a lower share price, so buyers beware.

On the personal finance front, a lot of the provisions of H.R. 4872 will be phased in over the next few years. Perhaps the biggest impact to your personal income statement will start in tax year 2013 in the form of a new surtax on unearned income. This surtax of an additional 3.8% on interest, dividends, etc. will be assessed to taxpayers making anywhere from $150,000 to $250,000 and up depending on marital filing status. As a result, you can expect a premium to be placed on investments like municipal bonds that continue to pay a tax-free stream of income.

For those individuals that are currently covered or soon will be by Medicare, rest easy knowing that the "donut hole" will be completely closed by 2020. In addition, any seniors that reach the "donut hole" in 2010 will receive a $250 rebate. Beginning in 2011, seniors in the gap that prefer branded drugs will receive a 50% discount.

Perhaps the biggest change to the current health system will be thrust on small business owners. There are a lot of vagaries and situational rules, but the basics state that employers with 50 full-time employees or more must provide health insurance to employees or face a fine of $2000 per worker. Helping to offset this new cost to owners will be a tax credit that can range from 35-50% of the cost depending on the timing and several other factors.

As I mentioned earlier, there is definitely not enough space to cover all the ramifications of H.R. 4872 in a one page column. So, if you would like to learn more about how your individual situation will be affected, please visit our website and peruse an 8-page summary of the key provisions via our "Resource" tab.

-Walter Hinson, CFP®

2010 Market Update

S&P 500	**+4.9%**
DOW	**+4.1%**
NASDAQ	**+5.7%**
MSCI World	**+2.7%**

Mortgage Rates

15-Year	**4.48%**
30-Year	**5.23%**
5/1 ARM	**3.97%**

Did You Know?

Starting after July 1st, 2010 there will be an additional 10% excise tax levied on all tanning salon services.

The $6,500 move-up and $8,000 new home buyer tax credit will soon come to an end! All eligible purchases must be under contract by April 30th and close by June 30, 2010.

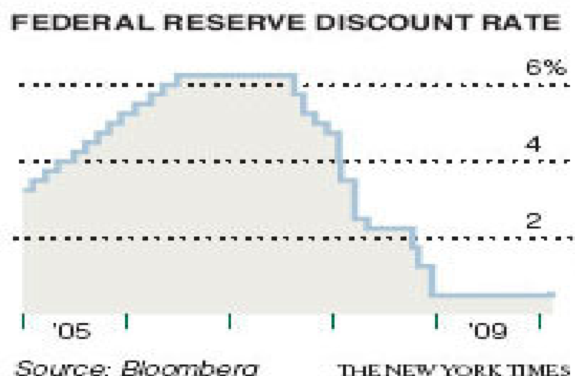
The S&P 500 is up close to 80% from its lows in March 2009!

Interest Rates—Where are They Going?

Up.

I considered taking the easy route on this quarter's article and ending it on the sentence above. After all, with the Fed Funds rate currently sitting at an all time low of 0.25% there is little room to move except up. Probably a better question is *how* will interest rates move and how will this move affect your portfolio? To start lets remember that much of the impetus for us reaching these mega low rates has been artificial in nature. At the end of 2008, the Fed moved their target rate from an already accommodating point of 2% to where we stand today. We applaud this move because within 3 months most asset classes around the world bottomed out and we found ourselves in recovery mode. By making cash so painful to own at the average money market rate (it will take around 10,000 years to double your money), investors have had no choice but to buy riskier asset classes.

The scenario that continues to play out fits well with our underlying thesis that huge rallies like the one we are currently experiencing are to be "rented" and not "owned" over the next several years. If the free hand of capitalism was controlling interest rates then we would no longer be sitting around 0% rates after experiencing a nearly 100% market rally in a little over 12 months.



However, there is one thorn that continues to stick in the side of the Federal Reserve. The one asset class that hasn't soared in value the last year has been the sluggish real estate market that continues to tie the hands of the Fed. To start raising rates at this point would only make home ownership that more expensive causing home values to soften again and potentially thrust us into the dreaded "double-dip recession".

This leaves the Fed with their only real option going forward to be a slow and steady increase of their funds rate. We look for these rates to be increased 1 to 2% over the next 12 to 18 months with a pause in rate hikes to follow. This will allow both the private and public sector the opportunity to shore up their balance sheets further with accommodating rates and also allow us to start returning to a more normal interest rate environment controlled by free market forces. While we are confident in our interest rate predictions for the next 2 years, rate moves going forward will be much tougher to predict and be heavily dictated by the underlying strength of the world economy and also the ability of the US to pay off an ever expanding debt load. For these reasons, we would be cautious in purchasing fixed income securities of any type with maturities greater than 5 to 10 years.

In conclusion, continue to ride the low interest rates wave that is propelling the market higher, but beware the impending bubble that artificially cheap money is nearly certain to create within the next few years.

-Ryan Glover, CFP®

Options Education

Many of you may have noticed a change in the way some of your option positions show in your account. Don't worry, this is not a mistake, but rather an industry-wide initiative that became effective on February 12th.

Moving forward, all option symbols will migrate from the old 3-5 letter symbols to a new, more descriptive 8-21 character symbol. I know you are probably thinking that more digits doesn't sound simpler, but the new symbology with its added length will be more descriptive and hopefully make determining the option symbols more of a formula than the old guessing game.

The new formula for option symbols incorporates the root (underlying stock ticker); then the expiration date (mm/dd/yyyy); the strike price (dollar amount with 2 decimals); and finally whether it is a call or put (C or P).

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