



INVESTING INSIGHTS

Timely Insights for Your Financial Future

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San Antonio Capital Management Make its Debut

San Antonio Capital Management, LLC officially opened its doors on January 1, 2010 after a successful private placement offering of over \$27 Million, which closed on December 23, 2009. As of March 31st of this year, we are proud to say that our firm has nearly doubled in size with just over \$50 MM in assets under management. We would like to thank our partners and clients for their continued trust and support, and for giving us such a successful start.

Our Advisory Investment Committee, headed up by Mr. Richard "Dick" Schlosberg and Vice Chaired by Mr. John C. Kerr, has been extremely active throughout the quarter; helping to guide the investment views and thesis of The Partners Flagship Core Portfolio, our primary asset allocation model. Throughout the course of the past few months, we have implemented several changes to our model portfolios based on the committee's overall views of macroeconomic trends and outlook for the global economy.

We have slowly reduced our cash position, strategically legging into equities, with a slight overweight to growth within the US space. We have held an overweight to energy, industrials, and technology believing these sectors should perform well coming out of a recession. In addition, we have recently added an overweight to Healthcare given its attractive valuation, and our view that the legislation passed through Washington should have a substantial affect on the dollars flowing into the Healthcare space. Most recently we have instituted a small overweight to Financials based on our expectation that larger banks should post good profits over the coming months.

On the fixed income front, we have shortened the duration of our fixed income positions slightly from an average of roughly 6 years, to 4.5 years in order to reduce the potential effects of a rise in interest rates. In addition we have added some floating rate bank note exposure to our high yield position, in order capitalize on and hedge against any probable increases in interest rates. Finally, we have instituted a position in local sovereign emerging market debt. This asset class should provide us with additional yield, as well as non-dollar exposure, since we expect emerging market currencies to appreciate versus the dollar over time.

In other news, San Antonio Capital Management was featured in the Business section of the Express News on Friday, April 2nd, highlighting our unique focus on alignment of interests. Finally, we are very close to having our website finalized, which will allow clients to access their account information from our home page.

No tightening by the Fed is likely until the unemployment rate comes down for a few months in a row, and we don't expect that to happen until the summer at the earliest.

Standard & Poor's Economic Report: Heating Up

By David Wyss, Chief Economist

MARCH 2010 -- We found signs that the economy is taking a turn for the better. Household debt has now dropped for five consecutive quarters -- to 126% of disposable income from the record 136% at the start of 2008. The saving rate is holding at 4.6%, still only half the pre-1990 average but well up from the record low of 1.7% in 2007.

Construction remains a problem for the economy, but it's more a problem now for commercial construction than residential. Home sales dropped off in December but still seem to be holding well above their early-2009 lows. Prices remained off their lows, though we continue to expect a drop over the winter.

Government spending should continue to boost the economy. The Obama Administration's new budget calls for a \$1.6 trillion deficit for fiscal 2010, up from last year's record \$1.4 trillion. The government hopes to reduce the deficit to \$727 billion by fiscal 2013, but that depends on a sharply divided Congress.

The Federal Reserve has terminated its new purchases under the various quantitative easing plans. So far, the markets have taken this move well, and we expect spreads to remain stable over the coming months. No tightening is likely until the unemployment rate comes down for a few months in a row, and we don't expect that to happen until the summer at the earliest.

Housing Slips

As expected, home sales dropped in December. This decline followed a surge in November that stemmed from buyers cashing in on the \$8,000 first-time homebuyer tax credit. The government extended the credit through June (with contracts signed by April), but buyers didn't know this in November. We expect sales to rise again in the spring as buyers try to purchase ahead of the next cut-off date.

We expect the tax credit to be renewed in some form through the end of 2010. The credit seems popular with voters, especially now that it is available to trade-up buyers as well as new homeowners. With Congressional control hinging on the November election, we doubt Congress will allow the credit to expire, though it could be altered. The problem, however, is that the buyers who were most susceptible to the lure of the tax credit have already been caught, so the effectiveness of the credit will likely diminish.

Consumers Hit the Brakes

Consumer spending is expected to slow in the first quarter after a better-than-expected holiday season. Although consumer confidence is continuing to improve and the labor market is getting better, car sales dropped to 10.8 million units from 11.2 million in December. However, we believe the car sales drop was temporary, due to the brake problems at Toyota. Once Toyota restarts full production, we expect sales to rise to 11.7 million in 2010.

Non-auto retail spending will depend on employment. Though the household measure of employment rose 541,000 in January, payrolls dropped another 20,000. Although some of this might stem from seasonal adjustment problems, we saw this same pattern at the beginning of the last recovery. When companies begin to see more sales, they are reluctant to add permanent staff, instead hiring temporary and contract employees. Employment of temp workers rose 52,000 in January, more than accounting for the rise in private services.

We still expect the unemployment rate to climb during the spring, probably reaching a peak above 10% in June, but the October 10.2% rate might be the peak for this recession, remaining well short of the 10.8% peak reached in 1982, which will remain the postwar record.

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ETFs: A Flexible Vehicle for a Variety of Strategies

ETFs can help many investors achieve a level of diversification that otherwise would be too expensive or time-consuming to attain.

ETFs -- or exchange-traded funds -- provide liquidity, flexibility, and cost-efficient exposure to a broad range of asset classes. If you are considering adding one or more ETFs to your investment mix, take a careful look at your investment style, level of knowledge, and time horizon to determine whether this type of investment fits in with your overall strategy.

Who Should Invest?

Although it is widely understood that one of the key attractions of ETFs is low cost, keep in mind that every time you buy or sell shares of an ETF, you must pay a sales charge, or commission. For investors who trade frequently, these sales charges could easily erase any cost advantage associated with ETFs. Similarly, if you are likely to be dollar cost averaging with periodic payroll deductions, or tend to invest sporadically with small amounts of money, you may be better off with a regular mutual fund.

However, if you don't fit any of these "frequent transaction" profiles, ETFs can be an effective and flexible choice in a number of situations.

- **Investing a substantial lump sum using a buy-and-hold strategy.** If you have received an inheritance or some other windfall, or have transferred assets from a former employer's retirement plan to a rollover IRA, ETFs' low expense ratios will offset the one-time brokerage commission if you follow a long-term strategy.
- **Investing outside of a tax-sheltered plan.** When investing in a regular taxable account, ETFs could save you money at tax time. Since ETFs sell on an exchange, most trading takes place between shareholders. Individuals cannot redeem their shares for cash directly from the fund company. As such, the fund manager doesn't have to meet redemptions, so he or she won't be forced to sell shares to raise cash. This helps ETFs keep their potential capital gains exposure much lower than it would be otherwise.
- **For active, knowledgeable investors.** If you enjoy focusing on specific industries or on particular regions of the world, ETFs may offer the most cost-efficient way, when compared with single stocks or sector mutual funds, to pursue these segmented market opportunities.

Some investors use ETFs as core holdings, whereas others use them as effective portfolio-hedging tools. ETFs can help many investors achieve a level of diversification that otherwise would be too expensive or time-consuming to attain. Your financial advisor can help you determine whether ETFs are an appropriate strategic fit with your long-term goals.

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Diversification Can Help Bring Balance to Your Portfolio

During the 20-year period ending December 31, 2008, the correlation between stocks and bonds has been close to zero.

There are many areas in life where people look for balance -- work and play, saving and spending, to name two. Balance also applies to investing, where diversification, the practice of holding a mix of investments, may help to balance risk and return.¹

Understanding how diversification works may provide insight on the best ways to put it into practice. Financial professionals often look at a statistic known as correlation, which measures the historical tendency of two investments to move in tandem in response to market and economic developments. The closer the correlation of two investments is to 1.00, the more closely they have moved up or down together. A correlation of zero means that returns have not been related, and a negative number indicates they have moved in opposite "directions."

Lesson From the Past

The long-term behavior of stocks and bonds provides an example of how paying attention to correlation may help reduce risk.² During the 20-year period ending December 31, 2008, the correlation between stocks and bonds has been close to zero.³

What does that mean in practice? There may be times when stocks zig and bonds zag. For example, stock investors who maintained an allocation to bond funds potentially could have limited losses during the market downturn of 2000 to 2002, when bonds performed well. Just remember, past performance is no guarantee of future results.

When discussing diversification strategies, you may want to review the correlation table below with your financial advisor. A look at the numbers may reveal strategies for building a portfolio that does not fall too far out of balance.

Correlation With Large-Cap Stocks, 1989-2008⁴	
Foreign Equity	0.59
Real Estate Investment Trusts	0.58
Municipal Bonds	0.22
Cash	0.12
Government Bonds	(0.04)

¹There is no guarantee that a diversified portfolio will enhance overall returns or outperform a nondiversified portfolio. Diversification does not ensure against market risk.

²Investing in stocks involves risks, including loss of principal. Bonds are subject to market and interest rate risk if sold prior to maturity. Bond values will decline as interest rates rise and are subject to availability and change in price.

³Source: Standard & Poor's. Past performance does not guarantee future results.

⁴Source: Standard & Poor's. For the period from January 1, 1989, to December 31, 2008. Large-cap stocks are represented by the S&P 500 Index; foreign equity by the Morgan Stanley Capital International Europe, Australasia, Far East (EAFE[®]) Index; real estate investment trusts by the NAREIT Equity Index of all publicly traded REITs; municipal bonds by the Barclays Municipal Bond Index; cash by the Barclays 3-Month Treasury Bill Index; and government bonds by the Barclays Long-Term Government Bond Index. Foreign investments involve greater risk than U.S. investments, including political and economic risks and the risk of currency fluctuations, and may not be suitable for all investors. Municipal bonds are subject to availability and change in price. They are also subject to market and interest rate risk if sold prior to maturity. Interest income may be subject to the alternative minimum tax. Municipal bonds are federally tax free, but other state and local taxes may apply. Government bonds and Treasury bills are guaranteed by the U.S. government as to the timely payment of principal and interest, and, if held to maturity, offer a fixed rate of return and fixed principal value. Past performance does not guarantee future results.

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Estate Planning Alert: New Rules for 2010

For 2010, the tax basis of assets within an estate will not be adjusted to the fair market value as of the date of the decedent's death.

Given the number of recent media reports, it's hard for a watchful observer to miss the one-year repeal of the estate tax for 2010. But even though the tax has been repealed for this year, taxpayers still need to plan carefully for the remainder of 2010 and beyond. The following are areas that require close attention:

Federal Estate Taxes

Before the end of 2009, many observers wondered whether Congress would pass legislation changing estate tax rules for 2010 and subsequent years. Since Congress did not take action, a prior law eliminating the estate tax for 2010 only remains in effect. Beginning in 2011, the estate tax exemption will be \$1 million. Amounts inherited in excess of this threshold will be subject to federal estate taxes up to a maximum of 55% depending on the value of the estate. Taxpayers may want to monitor events in Washington, or stay in contact with their tax advisor or estate planning attorney, to determine whether there are any changes in the law that could affect them.

Tax Treatment of Inherited Assets

For 2010, the tax basis of assets within an estate will not be adjusted to the fair market value as of the date of the decedent's death. Instead, many beneficiaries will receive so-called "carryover" basis equivalent to the decedent's adjusted basis as of the date of his or her death. There are two important exceptions to this rule. Assets that are bequeathed to a surviving spouse, and that have appreciated up to \$3 million in excess of the decedent's adjusted basis, will be "stepped up" to the value as of the date of the deceased's death. Nonspousal beneficiaries with up to \$1.3 million of appreciated assets will receive a "step up" to the value of the assets as of the decedent's death. If the decedent had unrecognized losses as of his or her death, the basis step-up could potentially increase.

Because many assets increase in value over time, it is likely that beneficiaries receiving carryover basis will have a lower inherited basis and ultimately a higher tax bill should they ultimately sell assets that they inherit. This change puts the onus on taxpayers to maintain careful records on the cost basis of their assets, which could be helpful for executors and beneficiaries who outlive them.

Generation-Skipping Transfer Tax

For 2009, transfers of assets to a grandchild or a more remote descendant worth in excess of \$3.5 million were subject to a generation-skipping transfer tax of 45%. This tax is repealed for 2010 only. For 2011 and future years, transfers in excess of \$1.1 million (the equivalent of the lifetime gift tax exemption) will be taxed at a rate of 55%.

Gift Tax Rate

For 2010, the top gift tax rate drops from 45% to 35%. This tax applies to the value of annual gifts worth \$13,000 or more (\$26,000 when a couple makes the gift) to the same nonspousal recipient during a calendar year and also to cumulative gifts in excess of the \$1 million lifetime gift tax exclusion. According to current law, for 2011 and future years, the gift tax rate is scheduled to revert to a maximum of 50% and the lifetime exclusion will increase to \$1.1 million. Examples of gifts that are not subject to the gift tax include gifts of any amount to a spouse, gifts to a political organization, and payment of tuition or medical expenses.

Interpreting estate tax rules can be complicated, especially for estates with significant assets bequeathed to multiple beneficiaries. This communication is not intended to be tax advice and should not be treated as such. Each individual's tax situation will vary. Please contact an estate tax professional who can provide guidance about how federal and state rules apply to your situation.

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