

Fagan Financial Report

VOLUME 10 ISSUE 2

SECOND QUARTER 2007

| Inside this Issue | |
|-----------------------------------|---|
| A Disciplined Approach | 1 |
| Mutual Funds | 3 |
| Sector Weights | 4 |
| New Brochure and Client Referrals | 4 |
| Common Stock Portfolio Holdings | 5 |
| Retirement and Estate Planning | 6 |

Fagan Associates, Inc.
Registered Investment Adviser

The Independent Financial Voice of the Capital Region

Locally owned and managed since 1989

No proprietary products

Individually managed portfolios

No outsourcing to institutional money managers

INVESTMENTS * FINANCIAL PLANNING * RETIREMENT PLANNING

Current assets under management exceed \$100 million.

www.faganasset.com

767 Hoosick Road, Troy, NY 12180

518-279-1044 * 800-273-6026

A Disciplined Approach

Many factors influence the price of a stock. Before we decide to sell, we analyze the impact of the following warning signs on the value of a company.

Company Specific Warning Signs

The revenue and per share earnings of the company fail to live up to Wall Street estimates for a given quarter. Ours is an industry of expectations and should a company fail to live up to these expectations, chances are that for some time, until it re-establishes its credibility, the stock will have a difficult time making headway.

A shake-up in upper management. Reorganizations quite often precede bad news and such a shake-up could be a telltale sign that some bad news is coming. The accompanying press release usually states that "so-and-so is retiring to spend more time with his/her family." Once again, watch

how the price of the stock reacts to the news of a change in management. Be observant, quite often, this could be a time to buy.

The reddest of flags pertains to undefined or defined accounting issues. Should a company (see Enron, Worldcom or Tyco) announce that

Reasons to sell...

Company specific

Fundamental/Technical

Economic

Personal

they are conducting an internal investigation or, more worrisome, that the Securities and Exchange Commission is conducting either an informal or formal investigation into the ac-

counting practices of the company, run for the door. Remember, when you sell a stock, you are **not saying "no to the investment forever," but rather, "this doesn't make sense right now."**

The final company issue reason pertains to the company changing its strategic direction. Quite often, when a company embarks in a new direction it is because the old direction was not working and that this new direction should be the panacea. However, this "new direction" is often laden with pot holes as the company finds its way. Better for an investor to step aside and take a wait and see approach rather than to continue on the same course.

Technical Warning Signs

Investors generally tend to fall into one of two camps when evaluating

Continued on page 2

Fagan Financial Report

Published by: Fagan Associates Inc., 767 Hoosick Road Troy, NY 12180, 800-273-6026, 518-279-1044

stocks. Either they are fundamental investors or technical investors. Fundamental investors are those that examine the underlying financial and competitive strength of a particular company and take painstaking measures in order to determine whether or not this potential investment will grow its revenue and earnings enough to satisfy Wall Street. Technical investors evaluate, among other items, the direction and volume of the price of a particular security hoping that this will provide insight to the future movement of the stock. At Fagan Associates we employ both fundamental and technical analysis. However, for the purpose of this column we will examine the technical warning signs that may indicate that it's time to sell.

The first technical warning sign is when the price of a stock falls below either its 50- or 200-day moving average. A moving average analyzes the price action of a stock over a specified time frame. As the price of a stock declines, it eventually will meet its moving average. Generally speaking, once a stock pierces its 50-day moving average, we would consider this a "yellow light" and should it pierce its 200-day moving average, we would consider this a "red light" and the time to get out. Remember, discipline wins out when investing.

A second technical warning sign is when the price of a stock rises in a parabolic fashion. Think of an airplane rising in a parabolic or straight up fashion. At some point in time the wind is going to catch the nose of the plane, flip it over and send it into a tailspin. Stocks work in the same fashion. They can only go straight up for so long and then, at some point in time, they begin to decline. Most often if they have risen in a parabolic manner, they will also decline rapidly. Our discipline to counter this decline is to raise our trailing stop/loss order (the price at which we want to sell the stock below the current price) as the stock rises. We may also place this stop/loss order relatively close to the price at which the security is currently trading for added protection.

Should a stock rise sharply on an extraordinary amount of volume (more than three times average daily volume), this could be a signal to sell. When a stock experiences such rapid moves on heavy

volume this, it is a sign that all of the buyers are in with no remaining buyers on the sidelines.

The final technical warning is when the preset amount of time you are willing to hold a security has expired. If you buy a stock and it doesn't do anything for a period of time that is beyond your typical holding period, look to sell. There are always other opportunities.

Political and Economic Warning Signs

The federal government, through the legislative process, can have a profound impact, either positively or negatively, on the appeal of a specific industry or even on the entire stock market. One of the primary functions of our federal government is the raising of revenue through identifying and implementing a tax structure that raises this needed revenue on a basis that they would deem fair and equitable. *Given this objective, changes in the tax structure can impact your investment strategy.* A few years back the Federal Government reduced the maximum tax on long-term capital gains (those investments held more than twelve months) to fifteen percent from twenty-eight percent. The impact was an increased demand for dividend paying securities as well as an increase in the average holding period for stocks. Changes in the structure of the Internal Revenue Code will impact the attractiveness of selling a primary or secondary residence; the creation of limited partnerships or the risks of Real Estate Investment Trusts. The bottom line is that it pays to pay attention to changes in the tax code.

When government acts to protect its citizenry, the results can dramatically affect portfolio value. For example, defense spending rose sharply after 9-11. Tobacco stocks dropped like rocks after proposed legislation was enacted raised cigarette prices. The stock prices of tobacco companies as well as pharmaceutical companies rise and fall with wrongful death lawsuits. Recently, we have witnessed this with Vioxx, Merck's popular arthritis drug. Therefore it is imperative to pay close attention to pending legislation and judicial procedures.

Finally, the branch of the Federal Government that determines monetary policy

or the direction of interest rates is the Federal Reserve. *Generally speaking, a rising interest rate environment acts as a headwind to the stock market while a falling interest rate environment acts as a tailwind.* Usually, there are many other factors that act in conjunction with rising or falling interest rates so it is important to recognize what is causing the change in interest rates. We do not buy or sell stocks simply due to changes in interest rates. We also monitor other economic data points as they are released.

Individual Reasons to Sell a Stock

Depending on our client's individual circumstances, stocks might be sold to upgrade or rebalance a portfolio. We are constantly trolling the investment waters for portfolio upgrades. For example, let's assume that in 2003 75% of your portfolio was allocated to stocks and 25% to bonds. Now, due to the bull market, the allocation has changed to 80% stocks and 20% bonds. When this occurs, we sell enough stock to bring the portfolio back to the original allocations.

At different life stages, our clients may need to become more conservative in their cash requirements. Stocks and equity based mutual funds are investments for investors with a time horizon or more than three to five years. A larger percentage of bonds and cash are used for shorter time horizons. When our clients inform us of an anticipated cash requirement, we begin to scale back stock weightings over time in order to use strength in the security to sell. The last thing we want to do is to sell during a weak period. This is one reason why long term planning is so important.

Finally, we may sell a stock to harvest an unrealized capital loss for tax planning purposes. Historically, we use the last quarter of the year to review our clients' non-qualified or taxable accounts to minimize the impact of taxes.

Discipline trumps all when investing especially on the sell side of the equation.

If you have any questions about the activity in your portfolio, please give us a call.



Read the Fagan Financial Report every week in *The Sunday Record*.

PURE NO-LOAD MUTUAL FUNDS
 NO SALES LOADS IN
 NO DEFERRED SALES LOADS OUT
 MANY WITH LOW INTERNAL EXPENSE RATIOS

| <i>Fagan Associates, Inc. Largest Mutual Fund Holdings as of June 30th, 2007</i> | | |
|---|------------------------------------|----------------------------------|
| <i>Domestic Equity Funds</i> | <i>International Equity Funds</i> | <i>Hybrid/Fixed Income Funds</i> |
| Schwab 1000 Select Fund | William Blair International Growth | Loomis Sayles Bond |
| AF Capital Income Builder | Tweedy Browne Global Value | Income Fund of America |
| Baron Asset Fund | Oakmark Global Select | WF Short-Term High Yield |
| TR Price Growth Stock Fund | Vanguard International Growth | Franklin Income Fund |
| Marsico Focused Equity Fund | Janus Overseas | Northeast Investors Trust |

The New York Times

Stocks vs. Bonds

Average returns, by mutual fund category, for the second quarter of 2007 and the past 12 months.



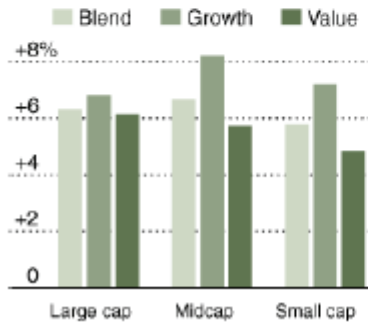
Sector by Sector

Natural resources funds led other sectors this quarter.



Growth vs. Value

Growth stock funds had the biggest gains in the first quarter.



Source: Morningstar Inc.



Fagan Associates, Inc.
 Underwrites
 Locally Produced WMHT Business Series
 Monday evenings at 7:30 p.m.
 Rebroadcast Sunday at 1:30 p.m.



FAGAN FINANCIAL REPORT

Fagan Associates, Inc., Sector Weighting
Master Portfolio Group, Combined Account Statement
June 30, 2007

| Sector | Total Cost | Market Value | Sector Weight | S&P1500 Index Fund as of 6/30/07 | Weighting |
|------------------------|--------------|--------------|---------------|----------------------------------|-----------|
| Financials | \$13,326,503 | \$16,352,812 | 28.69% | 20.31% | Over |
| Industrials | \$ 6,222,354 | \$ 7,894,536 | 13.85% | 11.99% | Over |
| Technology | \$ 6,619,571 | \$ 7,631,142 | 13.39% | 15.53% | Under |
| Energy | \$ 4,868,518 | \$ 7,361,830 | 12.91% | 10.36% | Over |
| Health Care | \$ 4,862,755 | \$ 5,979,350 | 10.49% | 11.68% | Under |
| Consumer Discretionary | \$ 3,298,274 | \$ 3,926,705 | 6.89% | 10.74% | Under |
| Telecommunications | \$ 2,079,218 | \$ 2,430,545 | 4.26% | 3.35% | Over |
| Consumer Staples | \$ 1,237,631 | \$ 1,754,520 | 3.08% | 8.54% | Under |
| Basic Materials | \$ 1,287,364 | \$ 1,590,461 | 2.79% | 3.46% | Under |
| Index Investments | \$ 1,097,828 | \$ 1,288,698 | 2.26% | | |
| Utilities | \$ 750,406 | \$ 795,714 | 1.40% | 3.81% | Under |
| Common Stock | \$45,650,421 | \$57,006,313 | 100.00% | | |

Sector Changes, July 15, 2007 Update

- Strong Sectors: Oil and Gas; Basic Materials; Industrial
- Weak Sectors: Telecom; Consumer Services; Financials

Please pass along our new brochure to family and friends.

During the last several months, we have seen an increase in the number of referrals from our existing clients. This is extremely gratifying because when this happens, we know that you value our services and hold our relationship in high regard.

Recent upgrades in our office technology and trading disciplines have made it possible for us to accept a limited number of new clients. If you know of anyone who might benefit from our services, please tell them to give us a call. We are pleased to offer a free consultation with no obligation. In fact, we encourage prospective clients to interview several advisory professionals before making the decision as to who will manage their hard-earned money.

Thank you for allowing us to assist you in achieving your financial goals.

The radio show ...

810WGY's
Fagan Financial Report at a **new time,**
Sundays, 10:00 a.m. - 11:00 a.m.
following the Joe Gallagher Weekend Morning Show

And, don't miss Dennis Fagan's weekly visit with Joe, Sun-
days, 8:30 a.m. - 9:00 a.m.



- A Recap of the past week's financial markets, including company specific and economic news.
- "The Record Review" – an outline of our column that appears in the Troy Record every Sunday.
- "Widely Helds" – a look at the price action and news releases from the most widely held stocks.
- A spotlight on one or some of our **mutual fund holdings or ETF holdings.**
- A look at the upcoming week, economic data and earnings reports.
- Monthly notable changes to our investment portfolios after the close of the prior month.

If possible, include your IRA beneficiaries in the planning process

According to Boston College's Center on Wealth and Philanthropy, baby boomers alone are positioned to inherit more than \$7.2 trillion from assets in retirement accounts. Getting assets transferred after the death of the original IRA owner involves several issues that could affect the beneficiary's tax liability. Therefore, it is wise to involve your beneficiaries in the planning process.

When you inherit an IRA, choices on how to handle the transfer are based on the type of IRA (Traditional or Roth), the relationship of the beneficiary to the deceased (spouse, non-spouse, trust, estate, charity), and the age of the original account holder at the time of death.

For example, a traditional IRA with a spouse designated as sole beneficiary, can transfer assets into the spouse's own existing or new IRA after taking the required minimum distribution for the year of death, if the original account holder was over age 70 ½ at the

time of death and did not previously take the distribution. In the case of multiple primary beneficiaries, assets must be transferred into separate Inherited IRAs.

Non-spouse beneficiaries have fewer options. Most significantly, they are not allowed to transfer the assets into their own IRA account. Non-spouse beneficiaries are required to transfer assets into an Inherited (five years or life expectancy) IRA and taxable distributions must begin within a certain amount of time. Check with your financial advisor for details.

When a trust is the beneficiary, it must meet be irrevocable; it must name identifiable beneficiaries; it must be valid under state law; and the custodian must have a certified copy of the trust. When an estate is the beneficiary, the executor can take a taxable lump sum distribution or open Inherited IRAs, five year of life expectancy depending on the age of the original account holder.

Any beneficiary may also elect to take a lump sum distribution. However, while there is no 10% early with-

drawal penalty, the beneficiary will need to pay income taxes on the distribution.

New wealth presents new opportunities and with any inheritance, it is likely that a beneficiary will want to reassess their total investment strategy. A meeting between the account holder, beneficiary, and financial adviser can avoid costly mistakes. Discuss what options are available to the beneficiary for taking the proceeds of the assets when the account holder dies as well as the tax and investment implications of each. Also consider naming contingent beneficiaries in case the primary beneficiary is no longer alive when the account holder dies. These assets go to the beneficiary automatically instead of through the probate process. The beneficiary designation forms typically override a will therefore it is very important to keep beneficiary information up to date.

These are only some of the issues involved in beneficiary designations. Please give us a call with any retirement or estate planning questions.

Retirement Savings Facts

- 2007 401(k) limits are \$15,500 for individuals under fifty years of age.
- 2007 401(k) limits for over age fifty are an additional \$5,000 as a catch-up provision.
- 2007 IRA limits are \$4,000 for individuals under fifty years of age.
- 2007 IRA limits are \$5,000 for individuals over fifty years of age.
- 2007 Roth IRA contributions phased out for Joint Filers w/ AGI between \$156,000 and \$166,000.
- 2007 Roth IRA contributions phased out for Individual Filers w/ AGI between \$99,000 and \$114,000.

Estate Tax Exclusion Limits

- 2007 & 2008 Federal Estate Tax Exclusion will remain at \$2 million.
- 2009 Federal Estate Tax Exclusion increases to \$3.5 million.
- 2010 Federal Estate Tax Exclusion decreases to \$0.
- 2011 Federal Estate Tax Exclusion increases to \$1 million.

Social Security Data (www.ssa.gov/)

| | |
|--|-----------|
| Average Monthly Benefit | \$1,052. |
| 2007 Social Security Wage Base | \$97,500. |
| Social Security Recipients | |
| Under Age 65 in 2007 Can Earn | \$12,960. |
| Social Security Recipients At Full S.S. Retirement Age | Unlimited |

Please note that the opinions of the authors are not a recommendation to buy or sell the stock, bond market or any security contained therein. Securities contain risks and fluctuations in principal will occur. Please research any investment thoroughly prior to committing money or consult with your financial advisor. Fagan Associates, Inc. services are offered only to United States citizens and residents. The information on this site is intended solely for such persons. Copyright 2006, Fagan Financial Report. All rights reserved. Broadcast, publication, or storage is strictly prohibited. Information in this document is provided "as is," without warranty of any kind, either expressed or implied, including but not limited to the implied warranties of merchantability, fitness for a particular purpose and freedom from infringement. The user assumes the entire risk as to the accuracy and the use of this document. We will not be liable for any damages of any kind arising from the use of this information, including, but not limited to direct, indirect, incidental, punitive, and consequential damages.