

Ω THE OMEGA FINANCIAL GROUP

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MEMBER NASD & SIPC INSURANCE AGENCY DONOR ADVISED CHARITABLE ORGANIZATION

Opinions & Facts...

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Quote of the Month

“You make money in Bear Markets – Unfortunately you don’t realize it at the time.”

Unknown

We’ve written in these pages a number of times our comments and feelings about Equity-Indexed Annuities. Thus far we’ve never seen any reason to offer them to our clients here at Omega. Equity-Indexed Annuities introduced in the mid 1990’s are generally viewed as a hybrid of fixed annuities, which pay a set rate, and variable annuities, in which the return is dependant upon the performance of investment accounts. Equity-Indexed Annuities guarantee an investor’s principal and a minimum return, but may pay more based on the performance of a stock or bond market index. In the past the contracts have been considered insurance products and regulated by state insurance regulators.

Now however, the Securities and Exchange Commission has made a proposal to put these Equity-Indexed Annuities under the purview of securities regulators (FINRA formally NASD).

Since most of the indexed annuities are sold through independent insurance agents many of these people do not hold a license to sell securities. Spokespersons from the insurance industry say that adopting this oversight rule would destroy the distribution channel provided now by the insurance agent.

“Now, why should I tell him the whole story?”

According to the SEC, complaints about abusive sales practices have increased along with the sales volume of these indexed annuities. The SEC further claims that the annuities’ complex features aren’t adequately disclosed, that commissions on the products are out-sized and that some carry high surrender charges imposed over long periods which can make them particularly unsuitable for seniors and others who may need their money right away.

Omega’s experience with these Equity-Indexed Annuities sold to our clients by others has not been good; however, we can understand why some organizations want to battle the SEC and try to keep further regulation out of their business. We understand because we’ve been offered many deals to market these rather mysterious investments. We are very

much aware of the high commissions paid by the insurance companies as well as the almost impossibility of “complete disclosure”. Our answer to companies wanting us to sell them:

“Thanks but no thanks”.

“WHAT ELSE WILL THEY DRAG OUT OF THE LEFT WING CLOSET?”

It’s difficult to believe we’re actually hearing in this free market society the words, “windfall profits tax”. We’ve asked a number of times, “What is a windfall profit and what is the difference between it and just a regular profit?” The reason we ask this question is that Senator Barack Obama, the assumed candidate for President in the Democratic Party, announced a proposal recently to pay “stimulus” checks for \$1,000 for families, and \$500 for individuals. *In order to fund this, Senator Obama says that the government would take “a reasonable share” of oil company profits.* That’s another question, “What does *reasonable* mean?”

Another Senate Democrat, Dick Durbin stated, “*The oil companies need to know that there is a limit on how much profit they can take in this economy.*” I wonder if Mr. Durbin has figured out a way he can convince the oil companies that they should “cut their profits”.

What we have here is a redefinition of business success...

Maybe we should consider a “Windfall Profits Tax” on others like jazz musicians, rap stars, rock bands and Presidential campaign “War Chests”. And while we’re at it, how about technology companies, hedge fund managers, and brain surgeons?

Besides the corporate tax of 35% (the highest corporate rate in the free world) now the Presidential candidate for the Democrats is suggesting ways to get more.

“...And the beat goes on...”

The *Wall Street Journal* reports that recently no fewer than 51 Senators voted to impose a 25% “windfall profits tax” on US-based oil companies whose profits grew by more than 10% in a single year and wasn’t investing “enough” in “renewable energy”. Ah, so that’s what it means, “growth of profits”! The Journal goes on to say, “If Senator Obama is as exercised about “outrageous” profits as he says he is, he might also have to turn on a few liberal darlings. Oh, say,

Berkshire Hathaway. Warren Buffett's outfit pulled in \$11 billion last year, up 29% from 2006. Its profit margin – if that's the relevant figure – was 11.47%, which beats out the major American oil companies."

Well, we could go on and on. What politicians will do just to get votes! Appealing to the voting public in an attempt to disable the American free market system is biting the very hand that feeds the insatiable appetite of the federal government. Will they ever learn?

Go figure.

"IS THIS THE WAY FREE MARKETS OPERATE?"

Well the bailout continues. The President has signed a \$300 billion + housing bill. A recent story in the *Fort Worth Star Telegram* pointed out that this \$300 billion represents the cost of \$1,000 for every man, woman and child in America. There go the miraculous stimulus payments.

"This is how the arithmetic works..."

According to the July 31 story, \$300 billion in spending authority will help forestall foreclosure on 400,000 homes. We figure this allows \$750,000 for each household. Since there are 2.8 million "at risk" mortgages it means that more than \$100,000 is available for each "at risk" mortgage. According to the article, to qualify for these new FHA mortgages, lending institutions must first write down the existing mortgage to current market value (whatever that means) and the new FHA loan must be for not more than 90% of that.

According to a letter to the editor on this subject from Mr. Kenneth Sap of Richland Hills, Texas: "*This gets the lending institution out of the risk of future default and puts it on the taxpayer. Do you suppose it would make sense that the lending institutions might be able to write down the mortgages to current value and rewrite the mortgage without government assistance?*" We don't think that would work because then the lenders who broke every ethical rule in the book would have to be responsible for the mistakes they made over the last several years. The interesting part is that taxpayers are mutely standing by willing to assume the loss.

Mr. Sap continues with a tongue in cheek ending: "With benefits like this, I don't see why the program isn't extended to *everyone* with a mortgage. For only \$400 billion more we all could get in on this program."

Now, that is a stimulus package!

"AND NOW FROM THE FREE LUNCH DEPARTMENT..."

A few issues back we discussed the first stimulus package announced by the White House when we especially targeted tax rebates which gave the consumer a temporary spending

lift. However, the checks do nothing to change incentives to work or invest, thus their impact is as fleeting as one of the schemes we mentioned in a past *Opinions and Facts*: dropping \$50 bills from helicopters. What happened with the current giveaway stimulus is that consumers have had to spend much of their discretionary income on \$4 gasoline and other necessities.

This of course, didn't have to happen. A year ago the price of oil was \$70 and as the Federal Reserve slashed interest rates by listening to Wall Street instead of the American middle class we see now that while the price of oil has fallen to under \$120 per barrel as of this writing, it rocketed to \$150 on the wings of the Fed's easy money plan. Too many "Free Lunches" come back to give you a bloated and upset stomach.

"Read all about it...the sky has fallen!!"

We have a very resilient economy in the United States and although the sounds we hear from the media and election campaigns continually tell us how bad things are. In spite of this the market has remained in a pretty much level stance during the last few weeks, while experiencing short term volatility. Our free market economy is so strong it will be a monumental task to take it down provided that we, the electorate demand sensible actions by our elected officials.

MANAGEMENT ADAPTATION

Recently a friend of ours forwarded an excerpt from a speech made by Mr. Herb Meyer at a Davos, Switzerland conference attended by most of the CEO's of major international corporations.

Mr. Meyer served in the Reagan administration as special assistant to the director of the CIA and was Vice Chairmen of the CIA's National Intelligence Council. Among other credits, he was the first senior government official to forecast the Soviet Union's collapse.

Here is a short summary of his speech. His observation of American business is worth repeating.

Mr. Meyer stated that the trend for large business to out-source has brought about two new words in business, **intergrator** and **complimentor**. As an example, IBM is the *intergrator* and as you go down the line, Microsoft, Intel and other companies that support IBM are *complimentors*.

He notes that each complimentor itself is an intergrator for the complimentors underneath it.

This explains why unemployment numbers may mean nothing. As an example: many people who used to be employees are now independent contractors launching their own businesses; generally they call themselves consultants, which mean their work is not listed as a job.

Out-sourcing also confuses the numbers. Let's say General Motors, who out-sourced cafeteria functions to Marriott, lays off hundreds of cafeteria workers who then get hired right back by Marriott. Now they work for Marriott rather than GM. And then (for some reason) newspapers and the media will scream that America lost more manufacturing jobs. According to Mr. Meyer all that really happened is that these workers are now classified as service workers. So the old way of counting jobs contributes to false economic readings. Mr. Meyer continues: "As yet, we haven't figured out how to make the numbers catch up with the change of realities of the business world." Now the same employees who were formally a part of the *integrator* are now part of the company that is the *complimentor*.

"Slimming down!"

Mr. Meyer summarizes by indicating that another implication of this massive restructuring is that because companies are getting rid of units and people that used to work for them, the entity is smaller. As these companies get smaller and more efficient, the revenues are going down but profits are going up. He points to the fact that companies are getting smaller but are becoming more efficient and profitable in the process. And we know that the money managers and analysts who cover these smaller entities must do their research in a different atmosphere.

If there is one thing we can be certain of in business, it's that we have changes constantly. Here at Omega we spend a great deal of time making sure that our business plan is consistent, well executed by our associates and flexible in its application. We must also be aware that our cliental does not remain static. Demographics and income as well as attitude and risk profiles also change.

Thanks for your co-operation and your continued business in this changing world.

"Hey, Barack. Here's another piece of bad, Good news!"

A recent editorial in the *Wall Street Journal* made a concise suggestion: "What the economy needs is financial and regulatory discipline for wayward banks; stable money; lower taxes, and policies to reduce energy prices by encouraging more supply." In case you didn't get it, this means more drilling in the US. In our judgment, what we don't need is more government guarantees for the mistakes made by Wall Street investment banks. What we also don't need is the biggest tax increase in history in 2009. We should give thanks that the economy is growing at all. This, of course, has a great deal to do with the low tax rates still in place and the entrepreneurial spirit of the American people.

OPINION

"Well here we go again!"

Time once again to make you feel happy or depressed, whichever tax bracket you're in.

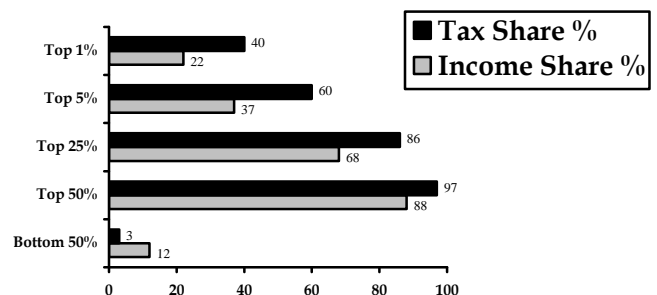
When it comes to recognizing who pays most of the taxes, let's take a glimpse of the current scorecard, circa 2006. Close by is a chart that shows income taxes paid by income earners in the U.S. The numbers you'll see are percentages of adjusted gross income reported and taxes paid by various income groups in 2006, according to the IRS. (Now, don't ask if producing a high income makes you "rich" or whether trust funds or rich fathers make you "rich".) As you look at it remember this: in the year 2005 the "richest" (I guess I have to use that word) 1% of income earners paid about 39% of all income taxes that year; by 2006 they paid 40% of the taxes. That same year, 2006, the 5% highest paid contributed a little less than 60% of the taxes and the highest paid 10% of income earners paid 70%.

The interesting part is if you peruse the chart you'll see that in 2006 the top 1% or the people who earn above \$388,806 paid 40% of the income taxes. By the way, that's the highest share of this group in the last 40 years. Those of us who earn more than \$108,904, or the top 10%, paid 71% of the total in 2006. **The top 50% of income earners paid 97.1%. The bottom 50% of income earners earned 12% of the income and paid less than 3% of all income taxes.**

The most interesting statistic that came from the IRS in July of this year is the increase in the number of Americans who declared an adjusted gross income of more than \$1 million. **From 2003 to 2006 the ranks of U.S. millionaires nearly doubled to 354,000 from 181,000 in a mere 3 years after the Bush tax cuts.**

Taxes and the Rich

Shares of adjusted gross income reported and taxes paid by income group in 2006



And no matter what you hear from Presidential candidates, the supply-siders were right. They predicted that with lower tax rates on capital gains, dividends and income, the economy and earnings would grow faster, *which they did*; investors would declare more capital gains and companies would pay out more dividends, *which they did*; the wealthy would invest less in tax shelters with lower tax rates applied, tax payments would rise, *which has happened*.

To quote the *Wall Street Journal* on this subject: "The idea that this has been a giveaway to the rich has been a figment of the left's imaginations. With a cut in marginal tax rates by President Bush in 2003 we find that no President has pulled more money from the wealthy than George W. Bush did with his tax cuts. Incidentally, the budget deficit dropped to 1.9% of gross domestic product in 2006 from 3.5% in 2003.

Of course, we all have read and heard that if Mr. Obama is elected President he promises to raise taxes. However, he promises to raise the taxes only on those making \$250,000 or more, which means that the above percentages will increase. Additionally, he says he is going to cut taxes for those at the bottom, but that's also going to be a challenge; because Americans with income below the median paid a record low of 2.9% of all income taxes while the top 50% paid 97.1%. Is this saying that he believes that half the country should pay all the taxes to support the other half?

Make no mistake, no matter what Warren Buffett or Ben Stein (in a recent Sunday column in the *New York Times*) say about the importance of the "rich", or high income people needing to pay more taxes, history has proven that high taxes do not create growth, they create chaos. Taking money from the producers gives no incentive to those productive citizens to invest and grow the economy. It's time we take a hard look at what we expect in a Presidential candidate and vote accordingly. However, the low tax approach works only when spending is under control. In the past, when Republicans controlled Congress they showed their ability to mimic the Democrats by increasing government spending rather than shrinking it. Let's hope things change with the next election.

Sometimes you just don't know where to turn.

Editor's Note: On August 14th Senator Obama's economic policy director Jason Furman and Austan Goolsbee, his economic advisor, wrote in an Op Ed piece in the *Wall Street Journal* that the Senator had been misunderstood and incorrectly quoted regarding his economic policies and proceeded to attempt to explain what he really meant. Stay tuned. While *Opinions and Facts* is not a daily publication, there may be more changes. Meanwhile, check out the cartoons nearby. It's as close as we can come to getting a hint as to what the definition of "change" is. Thanks to the *New Yorker* for the cartoons and the cut line from *Somewhere Right of Center*.

That's our take, yours is welcome.

Joseph E. Haulgrove John Dickers

Tom Haulgrove Sammy Bryant



"AND NOW ACCORDING TO THE RULES, THE CURRENT VERSION OF SENATOR OBAMA WILL HAVE TWO MINUTES TO REBUT THE STATEMENTS MADE BY THE PREVIOUS VERSION OF SENATOR OBAMA..."



"AND NOW IF YOU DON'T MIND, I WOULD LIKE TO REASSESS MY POSITION ON THE FIRM STAND I TOOK IN MY PREVIOUS REASSESSMENT."