

ParsecFinancial

Third Quarter 2007

Newsletter

Financial Advice and Planning

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Special Points of Interest

- ◆ US Economy Stumbling Along
- ◆ Parsec welcomes Mark Lewis
- ◆ Third quarter Parsec Prize awarded to North Carolina Center for Health and Wellness at UNCA

Charitable giving is a priority for many of our clients. As fall approaches, with the holiday season and end of the tax year not far behind, giving charitably may be on your mind. Planning for this now will give you more time to consider your options.

People give for altruistic purposes, but in doing so you can maximize the benefit to yourself as well. Qualified donations are tax deductible up to 20-50% of your adjusted gross income, depending on the donation. Timing a gift to a year when you are expecting higher taxes makes the deduction especially valuable, and in many cases you can roll over the excess contribution to future years. Calculating how much of your gift is deductible can be complex, particularly when making a major donation. It is important to consult your accountant on such matters.

Donating a gift of stock from a taxable portfolio is simple, and has an advantage over a gift of cash. You may donate directly to your charity of choice highly appreciated stock, held longer than one year, that you might otherwise sell and subsequently trigger a taxable gain. You would use the fair market value of the stock on the date of the gift to determine the deductible amount.

A qualified charitable distribution from an IRA is a preferred method of donating for those who are qualified. This type of distribution is a temporary allowance of the IRS, as this is only the second year, and also the last year, it is available. The charitable distribution is only available for

IRA account holders who are 70.5 and older, and it satisfies required minimum distribution rules. The total contributions for the year cannot exceed \$100,000. Qualified donations are non-taxable and hence cannot be claimed as a charitable deduction. However, the non-taxable treatment of the distribution is more favorable than a tax deduction. It is important to take action by year-end if you are interested.

Setting up an account specifically for charitable purposes is an alternative for those looking for more long-term charitable solutions. One example of this is a donor advised fund. Here you make an irrevocable contribution to your account and are then eligible to deduct up to your allowable limit in the year the contribution is made. These assets are then invested and may grow tax-free. You may direct that donations be made to any public charity at your discretion. Other accounts in this arena are charitable trusts and gift annuities. Rules for each type of account vary.

The assortment of options for how you may donate your assets are varied, many of which are done in a manner that will benefit you financially as well. Tax consequences and the deductibility of donations can be intricate at times and it is important that your decision best suits your charitable intentions and financial situation. As with any plan we recommend that you consult your financial advisor to find the best option for you.

Dr. Jim Smith's Economic Commentary

THE U.S. ECONOMY KEEPS STUMBLING ALONG

On August 30 the Bureau of Economic Analysis (BEA) of the U.S. Department of Commerce told us that real GDP growth in the second quarter was revised upward to 4.0 percent at a seasonally adjusted annual rate. Their previous estimate was 3.4 percent. This was a huge increase from the paltry 0.6 percent of the first quarter. It was 2.7 percent above a year earlier. The total for GDP was \$13.8 trillion in nominal (current dollar) terms and \$11.5 trillion when adjusted for inflation.

While personal consumption expenditures (PCE) account for a little over 70 percent of real GDP, they do not always account for the lion's share of growth. For example, in the first quarter real PCE rose at a seasonally adjusted annual rate of 3.7 percent, which contributed 2.6 percentage points to the 0.6 percent total real GDP growth rate. Clearly, many other things (most notably housing, business fixed investment and inventory changes) subtracted a lot from the growth rate in the first quarter.

In the second quarter, real PCE grew at a 1.4 percent rate and contributed only 1.0 percentage points to the 4.0 percent growth rate. Increases in net exports (1.42 percentage points), nonresidential investment (1.12 percentage points) and government spending at all levels (0.8 percentage points) were the major contributors to the sharp increase in the growth rate in the second quarter.

Unfortunately (at least for net exports and nonresidential investment), these changes are not sustainable. Thus, a significant slowdown in economic activity this quarter (July through September) seems quite likely.

It appears that we have "dodged the bullet" of a 2007 recession. However, there is a lot of weakness out there.

Housing demand has fallen dramatically with the result that inventories of new (7.5 months) and existing (9.2 months) single-family homes were at extremely high levels in July. Reflecting the activity of speculators who bought several units expecting a quick profit from reselling them, the inventory of condominiums for sale was at 11.9 months. No wonder condominium prices are falling in many areas, though not in Asheville.

The Office of Federal Housing Enterprise Oversight (OFHEO) provided some good news for housing market analysts on August 30. They reported that their index, which covers repeat transactions on all houses that qualify for a mortgage of \$417,000 or less (except in Alaska and Hawaii where the limit is 50 percent higher or \$608,000) was 3.2 percent higher in the second quarter of 2007 than in 2006. This suggests that a lot of the stories we keep hearing about falling house prices are wildly overblown.

The OFHEO data showed that house prices in five states were lower in the second quarter of 2007 than a year earlier. Those states and their rates of decline were: Rhode Island, -0.97 percent; Massachusetts, -0.99 percent; California, -1.38 percent; Michigan, -1.42 percent; Nevada, -1.45 percent.

Before becoming unduly alarmed by those declines, remember that prices in the 45 other states and the District of Columbia rose from a year earlier. Also, the five-year and since-1980 price changes for the same states were quite positive as shown in Table 1.

State	Price Appreciation (in percent)	
	Over last 5 years	Since 1980
Rhode Island	64.96	495.82
Massachusetts	36.61	617.18
California	90.15	536.32
Michigan	10.91	214.90
Nevada	89.47	302.60
U.S. Average	50.76	309.40

North Carolina prices rose 7.10 percent in the second quarter of 2007. This was the eighth fastest rate of increase among all states. Our 5-year appreciation has been 32.72 percent and since-1980 the increase has been 239.43 percent. Both of these rates of increase are well below the national average, which helps explain why people keep moving to North Carolina.

Among metropolitan areas in North Carolina, Asheville

has had the most price appreciation in the year ended June 30, 2007. That increase was 10.9 percent, which was the tenth fastest in the entire U.S. Over five years the Asheville area increase was 55.5 percent.

The Charlotte-Gastonia-Concord metropolitan area ranked 26th in the U.S. with an annual increase of 8.61 percent and a five-year rise of 27.75 percent. The Raleigh-Cary area ranked 44th with a one-year increase of 7.08 percent. Their growth over five years was 25.52 percent. The Durham area was 80th nationally with a one-year increase of 5.38 percent and a five-year pace of 25.63 percent.

The Federal Open Market Committee began what is widely hoped to be a sustained program of reducing the target for the Federal Funds rate (what banks charge each other for overnight loans) on September 18 with a 50 basis point reduction. We hope to see two more such reductions this year. If this feeds through to mortgage markets, stability will return to housing markets soon. Otherwise, housing-related problems could be a drag on the economy well into 2009. No one wants that to happen, so keep hoping that the “magic” of lower interest rates will work one more time.

Stock Market Outlook

The equities markets have been marked by increased volatility and a heightened paranoia led by a slowdown in the real estate economy. In the past we have commented about the extended valuation in the real estate market so we are not surprised to see the correction. However, we are amazed by loose lending standards and the extent of unconventional financing. Historically, residential real estate has both inflation beating returns and tax advantages, so it is a worthwhile investment. When combined with favorable leverage the returns can easily equal or exceed 7 – 11%. However, every equity investment has risk and uncertainty. Past real estate slowdowns have seen declines of 5 – 10% over the intermediate term.

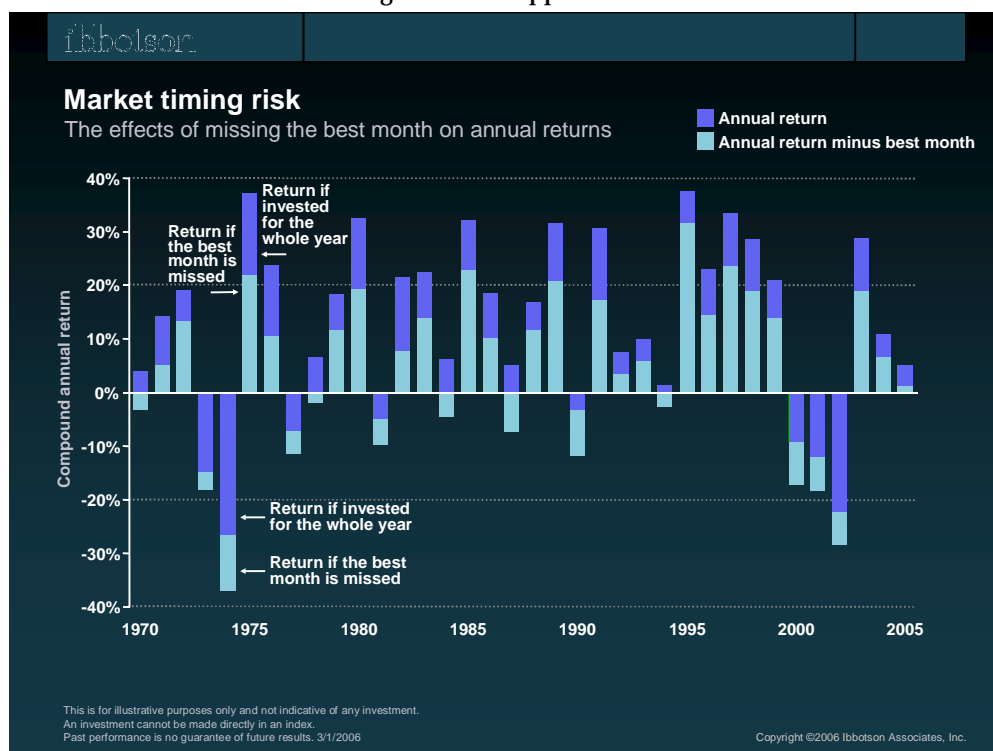
The financial sector of the S&P 500 Index has the most direct exposure to the mortgage, real estate and interest rate sensitive stocks. The widening of the credit risk spread has brought the cost of debt higher, especially in the lower credit quality areas. The hedge fund industry is sure to have some dismal results. Their high degree of leverage can transform a fender bender into a fatal crash.

However, a slowdown in GDP is very likely as concern about a recession have grown. If the disappointments are contained to the financial stocks, and the broader trend in corporate profits are higher, this may be considered a nice opportunity by

those investors with a long term oriented time frame.

As we have made clear, Parsec Financial does not believe in market timing. Instead, we advocate equity markets when they are most reliable, and that is over the long term. Please work with your advisor to plan out your short and intermediate cash flow requirements. This will help to ensure that you can hold your stocks during periods of uncertainty and stock price declines. The long term position of your portfolio should be allocated towards stocks.

Below you will see a table that depicts how important it is to have a long term and consistent perspective. Market timing is a failed approach.



Sign Up for Paperless Delivery

Many of our clients have asked us how they can avoid receiving annual reports, statements and other paper mailings from their custodian. Custodians are obligated by law to send you these communication pieces. However, Fidelity, Schwab and T.D. Ameritrade offer electronic versions in lieu of paper. You can sign up for electronic delivery of such items on the custodians' web sites. For further help,

feel free to contact the client service specialist that works with your advisor for step-by-step instructions.

To get started, visit the appropriate site for your custodian:

Schwab: www.schwaballiance.com
 Fidelity: www.fidelityaccountview.com
 T.D. Ameritrade: www.advisorclient.com

Parsec Welcomes New Staff Members

Mark Lewis, a native of Asheville, joined Parsec in 2007. He holds a bachelors degree in economics from the University of North Carolina at Wilmington and has completed the educational courses that prepare individuals for the CFP certification. Mark has worked in the fields of yacht management, banking and investments where for the last

10 years he was the head trader at Boys, Arnold & Company. With Parsec, Mark will continue to use his experience as a trader of stocks, bonds, and mutual funds as well as broadening his role to serve as a research analyst for the Parsec Investment Policy Committee.

New Website

You may be aware of the many changes happening at Parsec, but did you know that we also gave our web site a face lift? The new site incorporated a completely new design

and other enhancements. The next time you are online, check us out at:

www.parsecfinancial.com

Parsec Prize

Parsec recently awarded the third quarter "Parsec Prize" of \$14,000 to the North Carolina Center for Health and Wellness (NCCHW) at University of North Carolina at Asheville. The NCCHW was created to address a growing health crisis in our state. Nearly all of our population faces diseases and health conditions caused, at least in part, by

unhealthy habits. The center's goal is to alleviate and eventually prevent these conditions through its mission of educating health and wellness professionals, studying critical health and wellness issues, developing effective health and wellness programs, and sharing its research for the benefit of all North Carolinians and the nation.

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