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Bring Back the Uptick Rule!

Eight months in, this year already feels like a lifetime. We are experiencing one of the most tumultuous and bizarre periods in stock market history.

A bipolar stock market produced so many wild daily price gyrations as to make 250 point up and down moves in the Dow Jones Industrial Average (the Dow) appear commonplace. 17 of the 25 trading days in August resulted in 100+ point changes including the only four day streak of 400+ point swings in Dow history.

Look at the week of August 8th. A 635 point Dow plummet on Monday; on Tuesday the Dow rose dramatically by 430 points; it nosedived 520 points on Wednesday; recovered 426 points on Thursday and gained another 126 points on Friday. For the week, this roller-coaster ride produced a "whopping" -1.5% drop; in context, hardly newsworthy.

Why the wild ride?

The recent volatility echoes the 2008 financial crisis, but the fundamentals now are very different. In 2008 we witnessed an unprecedented absence of financial liquidity (money movement was virtually frozen due to fear of a banking collapse). Today the market is literally flush with cash (corporations are reporting record profits and their balance sheets alone hold over $1 trillion in cash).

In my professional opinion, the causal factor for this inordinate volatility can be traced directly to July 06, 2007. For it was on this day that the S.E.C. rescinded its Rule 17 CFR 240.10a-1., otherwise known as the "uptick rule", first adopted way back in 1938.

The purpose of the uptick rule was re-emphasized by the S.E.C. in 1978 when it stated: "To correct inequities that occurred on the Stock Exchanges prior to 1934, the S.E.C. adopted this rule". It was not unusual in those days to discover groups of speculators pooling their capital (money) and selling short (selling a stock one does not own and then hoping to buy it for a lower price; sell high, buy low) for the sole purpose of driving down the stock price of a particular security to a level where the stockholders would panic and unload their fully owned shares. This in turn would cause even greater declines in value. Think of this as something akin to shouting "Fire!" in a crowded theater in order to get a great seat for free.

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Advisor Corner

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Government Health-Care Spending: Medicare

You should plan for possible changes to Medicare. Let me know if you would like to review your options.

It is a well-known fact that the United States spends much more than other developed countries on health care, both in absolute dollars and as a percentage of GDP. Two enormous, complicated programs, Medicare and Medicaid, account for the majority of government health-care spending in the U.S. Both programs have been growing rapidly, which is expected to continue in the coming years.

Medicare and Medicaid were both created in the mid-1960's as part of Lyndon Johnson's Great Society agenda. As of 1970, 62% of total healthcare spending was still private, with out-of-pocket spending the single most significant source. During the subsequent forty years, however, Medicare and Medicaid each expanded by more than 11% annually due to benefit expansions and demographic change, pushing public-sector spending up to nearly 50% of total health-care expenditures. During the same time, private sector spending also grew at a robust 8.7% annually, as employer-sponsored insurance became the predominant conduit of health-care spending.

Looking forward, the Centers for Medicare & Medicaid Services (CMS) project 6.5% annual health-care spending growth over the next decade. Public sector growth is again expected to outpace private spending growth, with a 6.9% growth rate compared to 6% for the private sector. Combined, Medicare and Medicaid are expected to account for 39% of U.S. health-care spending in 2019, up from 37% in 2010 and 17% in 1970. Medicare is a federal government program that provides health insurance to people over age 65, and people with certain disabilities. In 2009, more than 43 million people received health insurance benefits through Medicare at a total cost of approximately $510 billion. Medicare benefits are divided into three parts: Part A Hospital Insurance, Part B Medical Insurance, and Part D Prescription Drug Insurance. Part C created a private version of Medicare, now called Medicare Advantage. More details about these benefits can be found in the attached table.

Original Medicare's relatively high cost-sharing provisions and lack of a limit on out-of-pocket spending can leave beneficiaries exposed to potentially devastating expenses in the case of a serious adverse health event. For this reason, most Medicare beneficiaries also carry supplemental insurance. Employer-sponsored retiree health plans, though becoming less common, still cover approximately 30% of the Medicare population. 20% of Medicare beneficiaries purchase individual supplemental policies, also called Medigap policies. Medicaid helps pay Medicare's premiums and cost-sharing for another 20% of the Medicare population. Only about 10% of Medicare beneficiaries are estimated to be completely without supplemental coverage.

Medicare Benefits Breakdown

Benefit	Approx. % of Spending	What Does It Cover?	What Does It Cost Beneficiaries?
Part A	39	Inpatient hospital care, skilled nursing facilities, and in some cases hospice or home care.	Generally no monthly premium as long as the beneficiary paid sufficient payroll taxes while working. Deductible and co-insurance for hospital stays exceeding 60 days.
Part B	26	Physician services, outpatient care, and in some cases physical or occupational therapy and home health care.	Monthly premium, deductible, and 20% co-insurance after the deductible is met.
Part C	23	Same benefits as Part A, Part B, and often Part D. Medicare Advantage plans are offered by private insurance companies as an alternative to original government-run Medicare.	Monthly premium, deductibles, co-pays, and co-insurance.
Part D	11	Prescription drugs.	Part D benefits are only offered through private insurance companies, which charge a premium in addition to deductibles, co-pays, and co-insurance.

Source: Kaiser Family Foundation and Medicare.gov

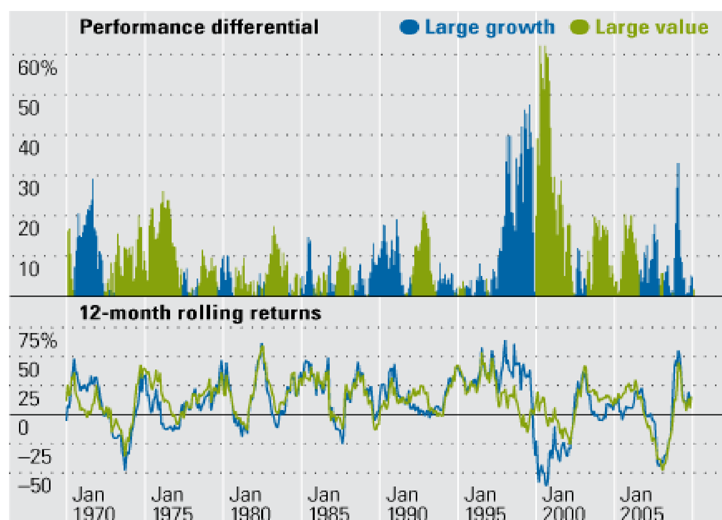
Head to Head Competition: Large Growth versus Large Value

The battle between large-cap growth and value investing has been going on for years, with each style trying to seize the spotlight. Although there is an annual frontrunner, history shows that leadership shifts with market conditions. In the bull market of the late 90s, growth stocks offered superior returns. But, since that bubble burst in 2000, value went on quite an impressive run. Growth seems to have captured the spotlight recently and many wonder if the tables have turned yet again.

Determining your allocation between growth and value can be difficult. Which style is more stable, or which will provide higher returns?

Unfortunately, there is no definite answer. Focus on finding the option that offers the most upside for your situation: perhaps it's growth, maybe value, or possibly a blend of both.

One-Year Growth and Value Cycles: 1970–2010



Performance differential measures the outperformance of one asset class over the other using 12-month rolling returns. This is for illustrative purposes only and not indicative of any investment. An investment cannot be made directly in an index. Past performance is no guarantee of future results. Returns and principal invested in stocks are not guaranteed.

Source: Large growth and value stocks in this example are represented by the Ibbotson Associates Growth and Value Indexes for 1970–1997 and the Morningstar Style Indexes thereafter. Ibbotson Associates Growth and Value Indexes are calculated based on data from CRSP US Stock Database and CRSP US Indices Database, Center for Research in Security Prices (CRSP®), The University of Chicago Booth School of Business. Used with permission.

A Quick Guide to Home Equity Loans

If you as a consumer need an additional line of credit, a home equity loan, also known as a second mortgage where your home serves as collateral, is one of several options that you can choose from. There are two major advantages of home equity loans. First, the interest rate on home equity loans is usually lower than credit cards and other consumer loans. Second, you can usually deduct the interest on home equity loans, unlike other loans. There are two types of home equity loans—fixed rate loans and lines of credit.

A fixed-rate loan provides a single, lump-sum payment to the borrower, and is repaid over a fixed period of time at a pre-determined interest rate. This is useful if you know how much you would need and when you would be able to pay off the loan.

A home equity line of credit (HELOC) is a variable rate loan that works like a credit card. Borrowers are preapproved for a specific spending limit and can withdraw money when needed via a credit card or special checks. Similar to a fixed-rate loan, the outstanding loan amount must be repaid in full at the end of the term. However, unlike a fixed-rate loan, HELOC interest rates float up or down, generally adjusted based on the current prime rate. A HELOC is a convenient way to cover short-term, recurring costs, such as quarterly tuition for a four-year college degree.

Although home equity loans do provide attractive rates of financing, we caution consumers to think twice about the reasons why one would need an additional line of credit. If you are thinking about using a home equity loan for day-to-day expenses, one should examine whether you are overspending and possibly sinking deeper into debt. If you end up taking out more money than your house is worth, the interest paid on the loan above the value of the home is not tax deductible.

Bring Back the Uptick Rule
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Please call or email our office if you would like contact information for the S.E.C.

You can also contact the Congressional (House & Senate) chairs for Financial Oversight. We have their information as well..

In essence, the uptick rule said that if a person pursued a strategy of selling a stock short, the short sale would not execute until the price of the particular stock moved up. For almost 70 years, the rule worked remarkably well.

On August 27, 2007, barely one month after its repeal, Muriel Siebert, (former state banking superintendent of New York, and in 1967, the first woman ever to become a NY Stock Exchange member) expressed severe concerns about the sudden increase in market volatility. "We've never seen volatility like this. We're watching history being made. The S.E.C. took away the uptick rule and now individual investors are getting pounded!"

In early September, 2008, then Presidential Candidate Republican Senator John McCain, blasted the S.E.C. saying that the removal of the uptick rule encouraged speculative short selling and turned "our markets into a casino".

To make matters even worse, the absence of the uptick rule spawned a surge of High Frequency Traders (HFTs). When the Dow crashed 635 points on Monday August 8, 2011, HFTs were responsible for 50% of the price movement (which resulted in a staggering market loss of $850 billion in capitalization!)

HFTs employ algorithmic trading. Many HFTs co-locate their computer mainframes with Exchange members computers (physically in the same or adjacent room). This gives HFTs a head start on the rest of us. Much of the trading sees HF traders battling each other, placing large "out of the market orders" with no intention of execution, simply to drive the stock price down. Then, once the price craters, they swoop-in and buy (low). The next day, they sell (high). Needless to say; if you or I tried any of these shenanigans, the S.E.C. would lock us up so fast it would make your head spin.

If this practice is not bad enough, the S.E.C. itself allows its members to reap sizeable custody fees for HF traders. And, these same Exchange members rent co-location space for hundreds-of-thousands-of-dollars per HFT!

What can you do?

Experience has taught us that when the market comes undone, the best course is to recognize what you cannot control, and to focus on what you can control. You and I must become ever more vigilant about market operations, relentless in demanding fairness, transparency and integrity.

So, call and write to your Senators and Congressional representatives. Demand the full reinstatement of the original 1938 "uptick rule"; (Rule 10a-1 of the S.E.C.). Talk to your friends and neighbors and encourage them to follow your lead.

Let's restore sanity to the financial markets. It's time to stop the destructive rollercoaster ride. Bring back the Uptick Rule!

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