

PORTFOLIO UPDATE

The RCM portfolio is having a good year, despite the tumultuous investment environment. Last year, we moved to emphasize yield and broader diversification, rather than stock picking. This strategy is producing results. During the first six months of 2009, the RCM portfolio is *up* 10.1% (net of all fees) compared to a 3.2% rise for market index.

As for risk, general market volatility has cooled off somewhat since last winter. The RCM portfolio has settled down even more. The risk index for the portfolio measures 75, well below the market (which is defined as 100). The annual yield of the portfolio is about 6%. This yield is slightly lower than previously, largely because the underlying security prices have risen.

COMMENTARY

The government's stimulus activities of recent months appear to have rescued the economy. The worst of the financial crisis is over. However, patient may be out of the ICU, but still remains in critical condition. Industrial output is significantly below capacity, unemployment remains high and continues to rise, housing prices are still depressed, and the credit markets remain in turmoil. The economy has had a quick fix, but not a complete cure. We still face a period of slow and prolonged economic recovery.

Since early March, the S&P 500 index has risen significantly from a devilish low of 666 to a high around 950 in June. Since then it has receded to around 920. This rally has been driven not so much by good news as less bad news than expected. This is not a recipe for a sustained bull market. Eventually, I expect economic reality to seep in and the realization that we're not out of the woods yet. The index should eventually retest prior lows, probably not a deep decline to 666, but the range of 800 is certainly probable. On the other hand, it is entirely possible that, after the current weakening, the rally will resume upward for a while before ultimately retesting lows. In short, anything could happen near term. The next 100 points on the market could be up or down.

In the long term, the bills will have to be paid for the economic rescue. The stimulus package has saddled the federal government with a huge deficit. What's more, plans for expanded federal programs proposed by the administration and Congress signify even more deficits in coming years. Managing the deficit will be the investment theme of the next decade.

The government has basically two options: raise taxes or monetize the debt (which is Fed-speak for "print dollars"). Most likely, they will use both. Neither option presents enticing prospects for investors. This situation will ultimately lead to inflation, rising interest rates, rising tax rates and a sluggish economy. It will likely spell a prolonged period of low investment returns for simple straight-equity investments. Better returns will likely be found only in the bluest of blue chip/dividend-paying stocks, yield plays, commodities, and overseas markets. These are the places I expect to concentrate investments in the future.

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Dr. Rollins has earned both the Chartered Financial Analyst® designation and Certified Financial Planner™ credential. He was awarded the CFA® designation in 2004. The CFA charter is the only credential for investment analysis and management recognized worldwide. Recipients of the CFA charter have successfully completed a graduate-level educational curriculum, and have passed a series of three sequential annual examinations. Pass rates average about 50 percent at each examination level. In 2005, he also successfully completed financial planning coursework and passed the qualifying examination for the CFP® credential.

Company Profile

ROLLINS CAPITAL MANAGEMENT is a fee-only financial advisory firm serving individuals. Using a consistent, patient investment strategy, our focus is long-term, high-quality, personalized investments. Clients have their own individualized accounts. ROLLINS CAPITAL MANAGEMENT handles all the daily investment decisions.

Presentation Disclosures

1. Portfolio composite returns are actual total annual returns, including stock price appreciation, dividends, corporate spin-offs and divestitures, and other occasional cash and non-cash distributions. Individual results may vary from the composite due to variations in portfolio size, and timing of deposits/ and/or withdrawals.
2. Portfolio composite returns represent an asset-weighted combination of fee-paying client accounts under management during the period specified, reported net of all withheld fees.
3. Annual portfolio composite returns and benchmark annual returns use a time-weighted calculation over the period specified.
4. Annualized portfolio composite returns and benchmark returns are calculated as the geometric mean of annual returns.
5. Portfolio and benchmark risk measures calculated using methodology provided by RiskGrades®.
6. Detailed disclosures available on request.

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