Caprin Asset Management, L.L.C.

7100 FOREST AVENUE, SUITE 303, RICHMOND, VA 23226
804.648.3333
WWW.CAPRINBONDS.COM

April 2009

Signs of Improvement: Temporary or Meaningful?

The Federal Reserve on March 18th unveiled an aggressive purchasing program dedicated to buying $300 million of long-term U.S. Treasuries and $750 million of mortgage-backed securities as part of a broader program to jump-start the economy. Meanwhile, after a unanimous vote, the Federal Open Market Committee left its Fed Funds target rate at the 0-0.25% range. Bernanke followed up the rate announcement by forecasting that the target rate would remain unchanged for an "extended period." The FOMC showed little immediate concern for inflation, labeling the risk of prices rising as relatively low due to the struggling global economy. Looking further ahead, at least *some* inflation seems inevitable as the Fed continues running the printing presses at full speed to produce the money supply necessary to fund the stimulus programs.

The proactive, and some say, extreme initiatives by the Obama administration and the Federal Reserve have generated some newfound optimism in consumers and the global markets. During the last full week of March, Treasury Secretary Timothy Geithner conveyed additional details about the bank bailout plan, helping to address some of the questions about the removal of toxic assets plaguing bank balance sheets. He also outlined the creation of a stricter regulatory system to serve as a watchdog for America's fundamental financial markets. These actions have contributed to restoring order and to reversing the equity market's slide which reached a 12-year low on March 9th. Since then, the Dow Jones Industrial Average Index has rallied around 20% on the faith of these initiatives and the release of better-than-expected economic data, including new and existing home sales with meaningful improvements for February, and durable goods orders unexpectedly jumping 3.4%.

Although it is possible that the worst of the financial crisis is behind us, the road to

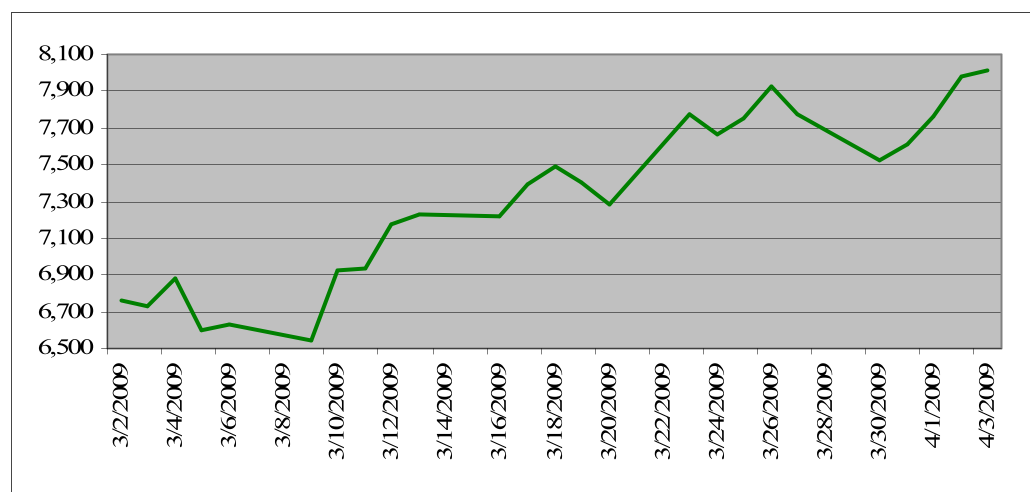

Figure 1. *Dow Jones Industrial Average Index since March 1st, 2009* *Source: Bloomberg*

Highlights:

- Economy showing slight signs of traction, but unemployment continues to rise
- New municipal bond issuance coming in waves, generating buying opportunities
- Caprin maintaining target duration close to 5 years, neutral to target index
- Relative value exists in select sectors and in high-quality issues in the 10– to 15– year range

"The details surrounding the bank bailout plans coming out of Washington are helpful and encouraging, but their execution and ultimate success will be essential to preventing a deeper, longer recession."

recovery remains long. The details surrounding the bank bailout plans coming out of Washington are helpful and encouraging, but their execution and ultimate success will be essential to preventing a deeper, longer recession. Additionally, the timing of a housing upturn remains unclear, and recent news from the auto industry suggests a major overhaul and additional hardships are part of the rehabilitation process.

Caprin Strategy

Although recent headlines have given glimmers of hope, volatility in our financial markets will not disappear overnight. Equity prices have been moving steadily upward in recent weeks and bond yields have been fluctuating in response to positive legislative news and to less favorable financial headlines. Municipal yields have not been immune but yield changes have been much less dramatic and have been driven primarily by issuer supply and investor demand. Recent large volume issuance of new bonds has caused yields to rise in order to attract more buyers. When that supply exits the market, buyers scramble to find attractive bonds and drive prices higher as demand outstrips availability. Regardless of these short term dynamics, municipal bond investors have experienced the benefits of owning a lower volatility, income-oriented portfolio as an offset to the larger price swings of other investment allocations.

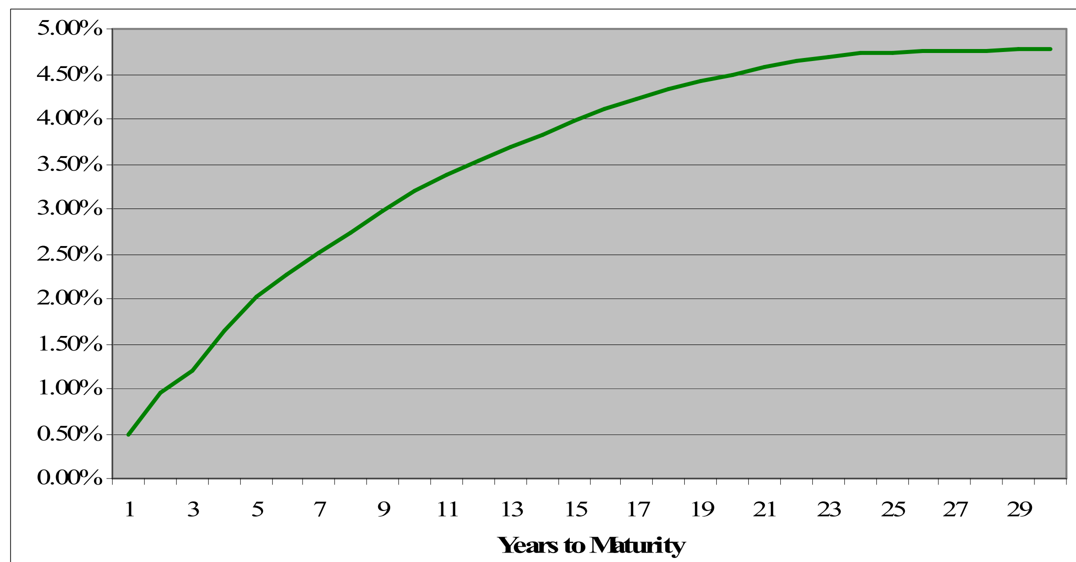

Figure 2. Municipal Bond Yields from 1- to 30-Year Maturities as of April 3, 2009 *Source: MMD*

Caprin's strategy continues to position portfolios relatively neutral to our benchmark (with maturities invested at all points on the yield curve) and maintaining a 5-year duration target. Current market conditions favor seeking yield from bonds in the less than 3-year maturity range while taking advantage of opportunities in the 10- to 15-year maturity range as the new issue surges occur. Interestingly, the recent increase in new issuance has been at such a high level that even the highest quality bonds are being discounted to keep potential investors engaged. We are using this environment to acquire higher yielding general obligation bonds and strong, essential purpose revenue bonds that will provide our clients' portfolios with stability, value and liquidity. Through careful bond selection and a focus on maintaining flexibility in our portfolios, we have been able to keep portfolios positioned to take advantage of evolving market conditions.

Please remember that past performance may not be indicative of future results. Different types of investments involve varying degrees of risk, and there can be no assurance that the future performance of any specific investment, investment strategy, or product made reference to directly or indirectly in this piece, will be profitable, equal any corresponding indicated historical performance level(s), or be suitable for your portfolio. Due to various factors, including changing market conditions, the content may no longer be reflective of current opinions or positions. Moreover, you should not assume that any discussion of information contained in this piece serves as the receipt of, or as a substitute for, personalized advice from Caprin Asset Management. To the extent that a reader has any questions regarding the applicability to their situation of any specific issue discussed above, they are encouraged to consult with the professional advisor of their choosing. A copy of our current written disclosure statement discussing our advisory services and fees is available for review upon request.