



'AAA and Short' is Mr. Magoo Investing: Short-Sighted and an Accident Waiting to Happen

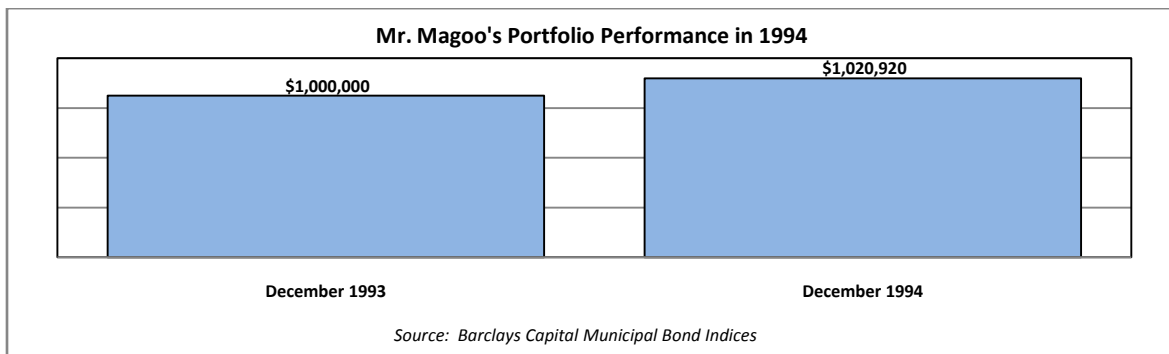
Summary: 'AAA and Short' may seem the best fixed income strategy to avoid risk during uncertain times but, compared to investing for the long-term, it could prove short-sighted, potentially exposing a bond portfolio to market risk and underperformance—exactly what it was supposed to avoid.

Imagine what kind of investor the bumbling but lovable cartoon character Mr. Magoo would be—whose near-sightedness always had him a step away from some major disaster. Risk averse, conservative, and a little lucky? Driving his financial adviser crazy although his portfolio holds only very high grade municipal bonds with very short maturities? Seems to fit the character.

Mr. Magoo's portfolio is probably where a lot of investors wished their portfolios had been in 2008, but weren't. However, with the Federal Reserve reporting over \$8.5 trillion in short-term assets held by individuals—\$500 billion in tax-exempt money market alone—this is where a lot of investors are now. It's understandable; looking at an economy showing signs of potentially further weakness, high net worth investors want the safety of "AAA and short" until these economic worries sort themselves out. Where better than short-maturity, high-grade municipal bonds? Low volatility and federal tax exemption—it seems the perfect strategy.

Unfortunately it also has another Magoo quality—short-sighted and an accident waiting to happen. What if Mr. Magoo pursued that strategy the last year the municipal bond market suffered a big loss, back in 1994? At the start of that year, there was uncertainty a-plenty for the fixed income investor. Although the nation was barely out of a recession, the Federal Reserve seemed on the verge of starting a round of rate tightening, the first time in over 14 months.

Given the unclear future and his propensity for safety, imagine Magoo invested his \$1 million portfolio in bonds on the shortest end of the yield curve to avoid risk. That year, he would have been right: the municipal bond market slumped lower as the Fed increased rates 5 times. As 1994 drew to a close, the municipal bond market was down -5.16%. Magoo was up 2.09%.



Compare Mr. Magoo to another investor, Tycoon Magoo, Mr. Magoo's rich uncle. Tycoon Magoo didn't worry about market movements and he wasn't short-sighted. He invested with a long-term, 3 to 5 year horizon. He took to heart financier J.P. Morgan's adage that "markets will fluctuate." He didn't market time, worry about the Federal Reserve, the economy, or interest rates. History showed that after each down market, there was a strong rally. He had an investment discipline and he stuck to it. If anything, he loved when markets went down; a true investor, he found value by buying low.

At the start of 1994, Tycoon had the same \$1 million to invest as Magoo did and he too had all of it in short-term bonds. But every month, regardless of what the market was doing, Tycoon Magoo moved a fixed amount from his short-term investments into long-term municipal bonds, assuring he would be fully invested by year end. Every time the market dropped in 1994, Tycoon was happy—he was buying more for less. While the municipal bond market took a loss in 1994, Tycoon Magoo outperformed his nephew by \$1,068. By the start of 1995, his portfolio was positioned for a rally.

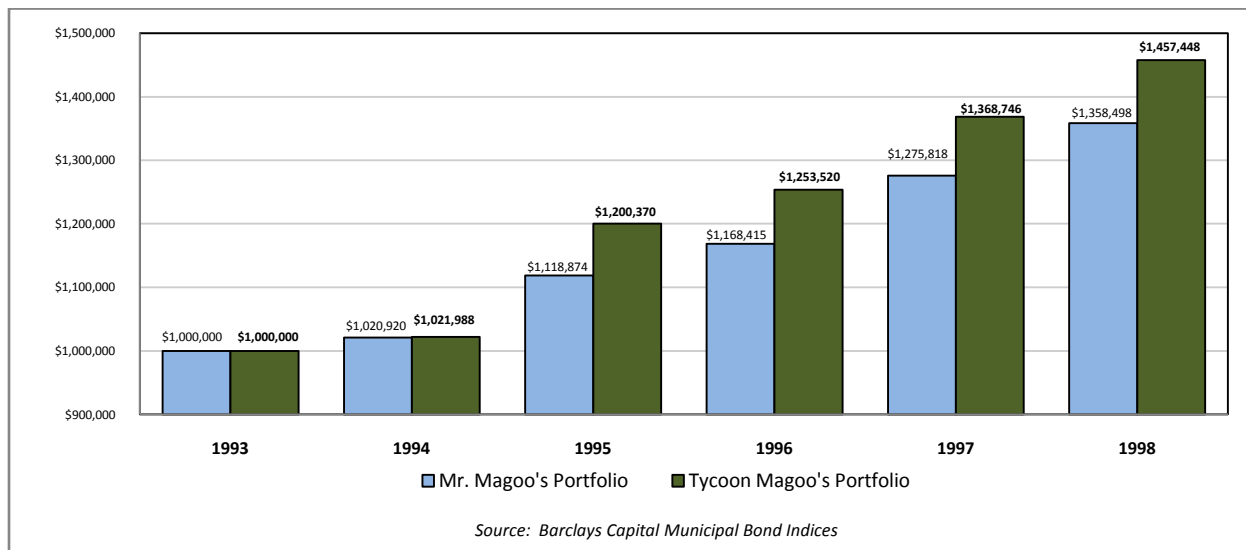
Mr. Magoo faced the start of 1995 with uncertainty: would the municipal bond market rally, or would the past year's slide continue? Would the Federal Reserve keep rates steady or tighten further? Magoo had a decision to make: get out of his low-yielding but still performing short-term investments to buy longer maturity bonds or wait until market trends seemed clearer. So Magoo did what many investors do: he waited until things seemed clearer.

It seemed like the safe decision. But with his short sightedness, Mr. Magoo could not see the longer-term financial accident this decision was about to cause him—**one that would cost him tens of thousands of dollars.**

Unfortunately for investors, no one rings a bell to signal the start of a rally. The municipal bond market started 1995 with a gain and never looked back. By May, it was up 10.61%, posting gains for 5 straight months. It was clear the rally was real, the market on track to end the year in very positive territory. So in June 1995, Mr. Magoo abandoned his "AAA and short" strategy and invested in longer maturity bonds, enjoying a nice 9.18% return for the year, 11.89% over the past two years. He thought he did pretty well.

But compared to Tycoon Magoo's disciplined long-term strategy, he didn't really do all that well. In 1995, the municipal bond market was up 17.45%, fattening Tycoon Magoo's wallet by \$178,382. Mr. Magoo, by initially staying short and waiting for a 'clear trend' to emerge, missed most of the rally. At year end, Magoo's wallet held only a \$97,954 gain, barely half of his uncle's largesse.

The municipal bond market continued to post gains for the next three years. Poor Mr. Magoo. He never caught up to his rich uncle.



And that is exactly the accident-waiting-to-happen quality of Mr. Magoo's short-term and short-sighted investment strategy: in his effort to be safe and cautious, he inadvertently exposed himself to considerable market risk. In the end it cost him close to \$100,000.

As he might have said, "Oh Magoo, you've done it again."

In 2008, the municipal bond market posted a -2.47% decline. For the first two months of 2009, the market posted back-to-back gains, rallying over 5.00%. While past performance may not be an indicator of future returns, following a good investment discipline never goes out of style.

Are you investing like Mr. Magoo—or a Tycoon?



Braintree Capital Partners

The Principals of Braintree Capital Partners are Arthur J. Wunder, Managing Partner and Barnet Sherman, Managing Partner. Ms. Gayl Mileszko is a Partner and COO. With a combined experience of over 60 years in municipal bond investment management, sales, and trading, Messrs. Wunder and Sherman have extensive experience in analyzing, investing in, underwriting, trading, and managing tax-exempt assets.

Barnet Sherman. Mr. Barnet Sherman most recently was a Vice President and Portfolio Manager with Morgan Stanley Investment Management. Mr. Sherman concentrated on making investment recommendations and developing market strategy for the then \$4.6 billion Van Kampen Tax-Exempt High Yield Fund. Managing the non-rated high yield primary market investment process, Mr. Sherman evaluated over 1,000 financings, personally analyzing, negotiating, and closing over \$1 billion public, limited, and private placement offerings. The Fund enjoys a 4-Star rating from Morningstar, who also recognized it as a “Fund of the Decade: 1990-2000”. Mr. Sherman is published in his field, contributing to *The Handbook of Municipal Bonds* and the *Morgan Stanley Investment Management Journal*. Smith’s Ratings and Research has recognized Mr. Sherman as a First Team All-Star and he has been noted in both Who’s Who in America and Who’s Who in Business and Finance.

Mr. Sherman holds an undergraduate degree in honors from Syracuse University (BA 1980). He earned his Master’s in Public Administration from Columbia University (MPA 1982) where he concentrated in public finance. He holds the Series 7, Series 63, and Series 65 licenses.

Arthur J. Wunder. Mr. Arthur J. Wunder has held senior management positions at Dillon Read, Tucker Anthony, Axa Financial, The Advest Group, and RBC Dain Rauscher. Mr. Wunder’s first senior position was at Dillon Read, where he rose to the Head of Institutional Sales and Manager of the Municipal Bond Department during his 19 years with the firm. When Dillon Read was sold to UBS, Mr. Wunder joined Tucker Anthony as Head of the Municipal Bond Department and was instrumental in changing their focus from traditional High-Grade bonds to one of High-Yield. He was subsequently asked to assume the role of Head of Fixed Income where he served until the firm was acquired by RBC, Dain Rauscher. Mr. Wunder remained as Sales Manager at RBC for its High-Yield Muni products, interacting daily with investment bankers and sales personnel in the creation, structuring and distribution of municipal bond products. He was also asked to serve on the firm’s underwriting committee. Mr. Wunder was recruited by the Chairman of The Advest Group Inc, a subsidiary of Axa Financial, to head their Fixed Income Division.

Mr. Wunder is a graduate of St. John’s University in New York where he earned a Bachelor of Science Degree in Business Administration and Marketing. He holds Series 7, Series 63, Series 53 Municipal Principal and Series 24 Securities Principal licenses.

Ms. Gayl Mileszko. Gayl Mileszko is the former Director of the Massachusetts Department of Labor and a former officer and member of the board of the Massachusetts Health and Educational Facilities Authority. She was appointed by the Massachusetts Governor after two years in the executive office on his senior staff. Ms. Mileszko was previously associated with the regional investment bank Tucker Anthony in Boston and New York from 1990 to 2002. She was a vice president in public finance handling more than \$2 billion of originations for tax-exempt issuers in the Northeast. Later, she was named senior vice president in the fixed income capital markets division, where she was the chief of staff to four successive managers supervising bond trading, sales, research and investment banking staff in 60 profit centers. Ms. Mileszko was a member of the staff of the Committee on Appropriations for the U.S. House of Representatives from 1983 to 1988, serving as minority staff counsel for three Subcommittees. She began her career as a staff assistant to U.S. Representative Silvio O. Conte (Massachusetts First District) and in the White House Liaison Office of the Republican National Committee. She holds a B.A. from Yale College.

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