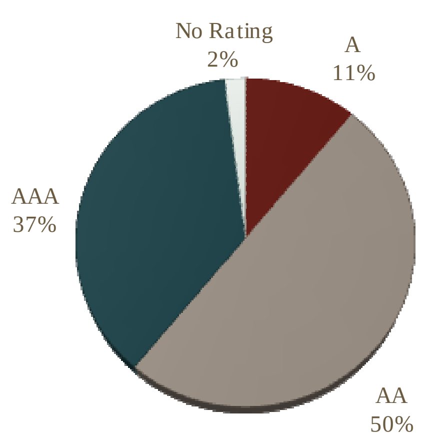
COMMON SENSE MUNICIPAL BOND INVESTING PART II

Crawford Investment Counsel is a high quality municipal bond manager. We focus on an issuer's underlying credit strength and never rely on bond insurance as a sole criterion for purchase. We invest in intermediate maturity bonds, primarily in the 3 to 12 year range. All of our portfolios are separately managed and customized for the individual client.

Our previous piece pointed out that utilizing high quality bonds and a common sense approach to municipal bond investing will help achieve the goals of capital preservation and income generation. We further noted the difficulty many managers experienced in 2008, primarily from their exposure to lower quality bonds which emerged after the AAA insurance backing was deemed almost worthless. We believe our superior performance relative to our peers was greatly influenced by our high quality bias and the underlying credit quality of our portfolios. The chart below illustrates the underlying ratings of all bonds in our National Intermediate Municipal Bond Composite.

Underlying Ratings Analysis



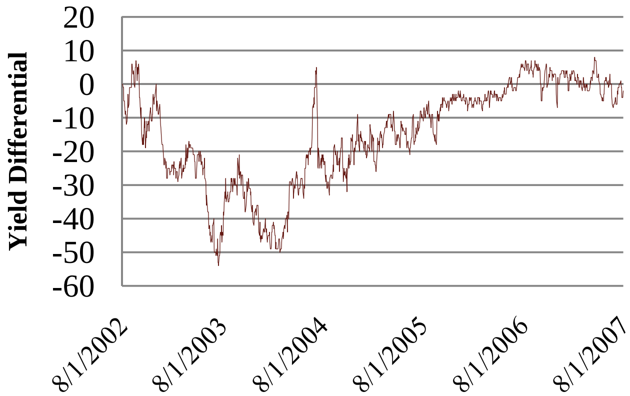
Over 50 percent of the three trillion dollar municipal bond market is insured. We are not suggesting that all insured bonds are of poor quality. Our point is, as the published ratings of insured bonds were downgraded, our portfolio's quality ratings remained strong due to the quality of the underlying bonds we employ.

Quality is the primary determinant of a municipal bond portfolio that is designed for preservation of capital, and the foundation of our common sense approach.

Over the past year we have been asked many times for an analysis of an existing municipal bond portfolio. We have noticed several common themes with many of these individually managed portfolios that seem to violate our common sense approach. For instance, why would a client own California municipals in a portfolio managed for a non-California resident? We also noticed a propensity to own New York bonds as well. Granted, these two states are among the largest issuers of bonds in the national market, but where is the common sense? On further examination, we looked at the largest (ranked by assets) National Intermediate municipal bond funds. Three of the top four funds each held approximately 13% of the portfolio value in California municipal bonds. The same three funds also held approximately 7% in New York municipalities. We wonder if the investors realize that approximately 20% of their holdings are invested in two states that are not faring well in the current economic environment. We have rarely found value in either state for a national portfolio. In fact, we have not purchased California issues for our portfolios, and our New York holdings are for the most part limited to issues that are backed by U.S. Treasury securities.

How did we foresee the troubles that lay ahead for these two states? The reality is we did not. However, our common sense approach led us to the correct conclusion. High quality bonds in California and New York have rarely made sense from a yield perspective relative to the market in general. Both states have relatively high state tax rates, and there is a large incentive for an instate buyer to purchase instate bonds to avoid the state income tax on the coupon income received. This has tended to make the bonds trade artificially expensive in the marketplace. Since we are an income and value focused manager, this would have eliminated most of these issues from our investable universe.

10 Year California G.O. Yield Minus 10 Year Texas G.O. Yield



Source: Bloomberg

To illustrate this, the chart above tracks the yield differential for a 10 year maturity bond in two states, California and Texas. The yields represent only the general obligation debt issued for the two states. We have chosen Texas as an excellent general market surrogate due to the large issuance and absence of a state income tax that would create artificial demand for instate Texas bonds. The time period chosen illustrates a "normal" market environment that existed for the five year period ending in August of 2007. Data for the period after August of 2007 would be affected by the credit crisis and subsequent well documented problems for the State of California. During this five year period, the State of California G.O. debt was rated as low as Baa1/BBB+ and as high as A1/A+. The State of Texas debt was rated Aa1/AA for the entire time period.

From a ratings standpoint, Texas was a more superior credit than California over the 5 year period. Based on the credit quality, common sense would suggest a scenario where California G.O. bonds would yield more than Texas G.O. bonds of the same structure and maturity. In reality, the yield relationship illustrated in the chart shows the exact opposite. The California paper actually traded as much as 50 basis points **lower** in yield than the Texas bond.

Today, due to the state's challenging economic environment, the yield for a California G.O. has risen significantly. If you owned California paper, the resulting price decline had a meaningful impact on your portfolio performance.

We hope this helps illustrate the common sense approach we take to investing in municipal bonds. We believe the ability to create separately managed portfolios tailored for the individual client gives us a significant advantage in meeting the needs of the client. As always, we would be happy to answer any questions you may have on the municipal bond market.

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