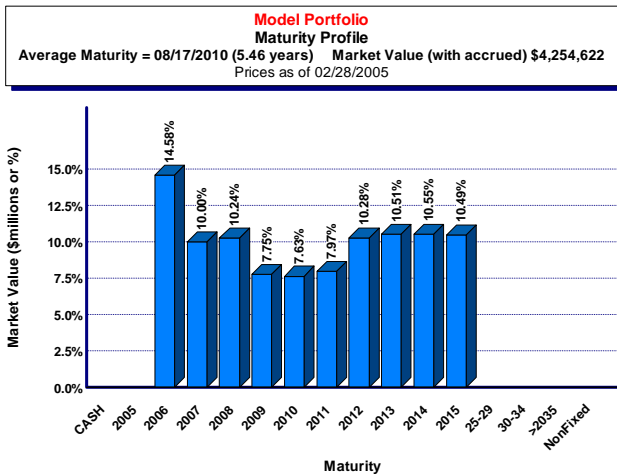


February 2005

The fixed income markets reversed strongly in February. The 10-year Treasury note rallied through the middle of the month from 4.13% to 3.99%. From this peak in the market, sentiment changed and the yield rose to 4.38% by the end of the month. Municipal issuance was very strong with volume of \$35.3 billion, up 16% over last year. The volume of new municipal issues will probably remain strong during March, but continued rising rates would cut the supply of refunding issues. The 10-year municipal bond yield bounced during February from 3.48% to 3.22% midmonth to 3.68% at month-end.

The yield curve has stabilized somewhat as the slope approaches longer term averages. We changed our model portfolio to reflect a more balanced investment strategy. We are still slightly barbelled, expecting the short-term yield to continue to rise, but have raised our allocations to intermediate bonds. The model portfolio reflects our investment of a new cash portfolio. We will change allocations of invested portfolios over time in a tax-efficient manner.



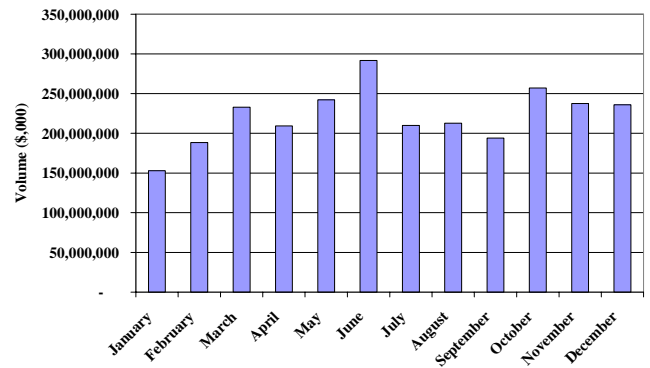
With solid supply, many smaller new issues are priced very attractively. Our overall average duration remains short of benchmarks by about one quarter year. Selectively, we have purchased new issues to replace maturities and to move specialty state portfolios in state. We have had success finding smaller deals and buying full maturities. Our trading desk sorts through many deals to find the best spread. For example, a \$630MM Maryland State GOs (Aaa/AAA) were sold at a spread of +3 to the MMD AAA scale. We did not participate in the deal and it was sold to institutional investors. We participated in \$17.8MM Central Montcalm Public Schools, MI (Aaa/AAA insured, AA2/AA+ underlying) at a spread of +29 spread to the MMD AAA scale. The extra yield comes from not competing directly with other large institutions to find value in the new issue market.

“Beware the Ides of March”

March is the only month that the intermediate municipal market has averaged a negative total return over the last fifteen years. The combination of tax sales and heavy new issue volume tends to drive municipal rates up prior to April 15. It is noteworthy that in 2001 (the last year reported by the IRS), 83% of tax exempt interest was reported on returns with an Adjusted Gross Income over \$100,000. This same group of taxpayers paid 94% of the taxes due on April 15. The liquidation to pay taxes is part of the reason the municipal market tends to under perform in March.

Seasonal supply is another problem in March as issuers ramp up refunding and new issuance after spring elections. We witness other seasonal spikes in June as municipalities end their fiscal year and in the fourth quarter as they try to avoid upcoming Federal tax law changes.

Total Municipal Issuance by Month



We will extend maturities during this period if the market sells off and there is an opportunity to lock in higher rates. At the same time, advisors whose clients may need liquidity for taxes are encouraged to give us plenty of advance notice. March is often a challenging month in the municipal market and we look forward to the opportunities it may present.

Average Total Return by Month for Merrill Lynch 3-7 Year Index for 1990 to 2004

