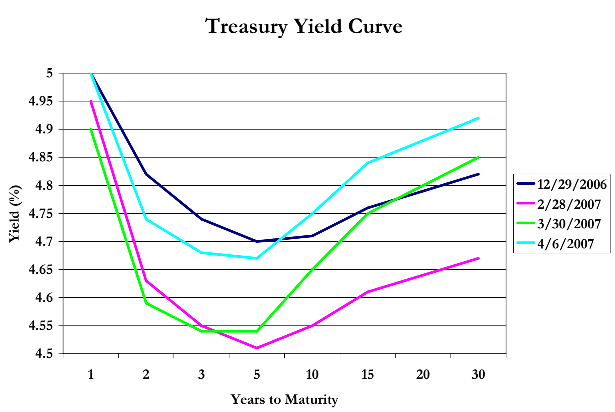
Market Commentary

March 2007

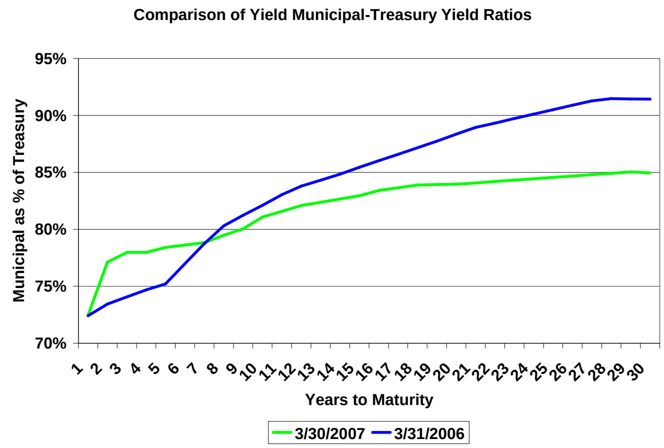
The first quarter saw slowing growth and rising commodity prices. Investor sentiment was torn between fears of further Fed tightening due to the uncomfortably high level of inflation, and fears of Fed easing due to a sub prime mortgage spillover effect on the economy. By the end of the quarter the Fed clearly articulated their view that they would neither raise nor lower rates in the near future, as they took a “wait and see” approach to future economic data. After a solid fourth quarter (GDP at 3.5%), the impact of the weakness in the housing and auto sectors began to weigh on the economy and by the end of March, economists’ estimates for first quarter growth were revised down to roughly 2.0%. Most of the significant events of the quarter seemed to occur in the month of March. As negative headlines regarding the collapse of sub prime mortgage lenders increased, and fears of contagion to the prime mortgage market grew, both the stock and bond markets experienced a period of risk aversion. The treasury market benefited from a flight to quality. Treasury yields declined sharply, particularly in the intermediate sector. Lower quality and higher risk bonds (such as high yield and emerging markets) sharply underperformed in a rapid move away from risk, and investment grade corporate bond spreads widened in sympathy with the declines in the S&P 500. Municipal bond yields from 2-5 years were unchanged over the quarter. The municipal change was a steeper yield curve beyond 5 years.

One of the most significant events of the month was the change in the shape of the treasury yield curve as short and intermediate rates declined and long yields increased. The inversion from two years to ten years that had been in place since last summer ended, and investor expectations for a Fed ease moved to as early as June. This steepening proved to be premature in early April when the March employment data revealed a strong labor market. The subsequent sell off in the treasury market resulted in a move back to a flat yield curve, and a repricing of Fed rate cut expectations to the third quarter of 2007. Despite the strong employment data and re-flattening of the yield curve, we expect that the next major change in the shape of the yield curve will be a steepening with short and intermediate rates moving down. We continue to believe that the economy is in a slowing trend and that we will see lower intermediate yields in the second half of the year.



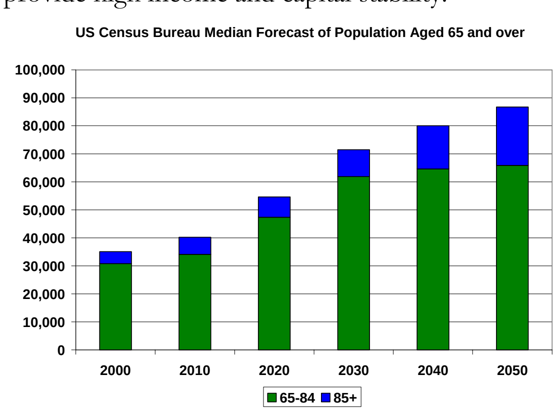
Relative Value of Intermediate Municipal Bonds

The municipal market has seen significant demand from non-traditional buyers due to the persistent upward slope of the yield curve. It has been one of the few liquid markets with a positive carry trade. However, as other yield curves begin to get steeper the relative value of the carry trade will be less. The chart below shows the impact of these buyers on the ratio of municipal yields to Treasury yields. Over the last year the intermediate municipal market is significantly cheaper and the long end of the municipal yield curve is significantly richer. For traditional municipal buyers, the greatest value is an intermediate municipal bond portfolio focused in the 6-9 year maturity range. BCA is concentrating purchases in this range in anticipation of a steeper yield curve in early 2008.



Increasing Muni Demand from Aging Population

Improvements in health care and the coming retirement of the Baby Boom generation will tend to increase the number of retirees and more importantly increase the amount of time retirees will depend on income from portfolios. Intermediate bonds should complement a continued growth strategy portfolio through a long retirement. Demand for intermediate bonds should increase to provide income and provide a stable capital value to offset variations in other portfolio holdings. Breckinridge is focused on managing intermediate bond portfolios for individuals using institutional strategies to provide high income and capital stability.



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