Dissecting the Bond Market

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AAII

Silicon Valley

Massive and Significant Changes

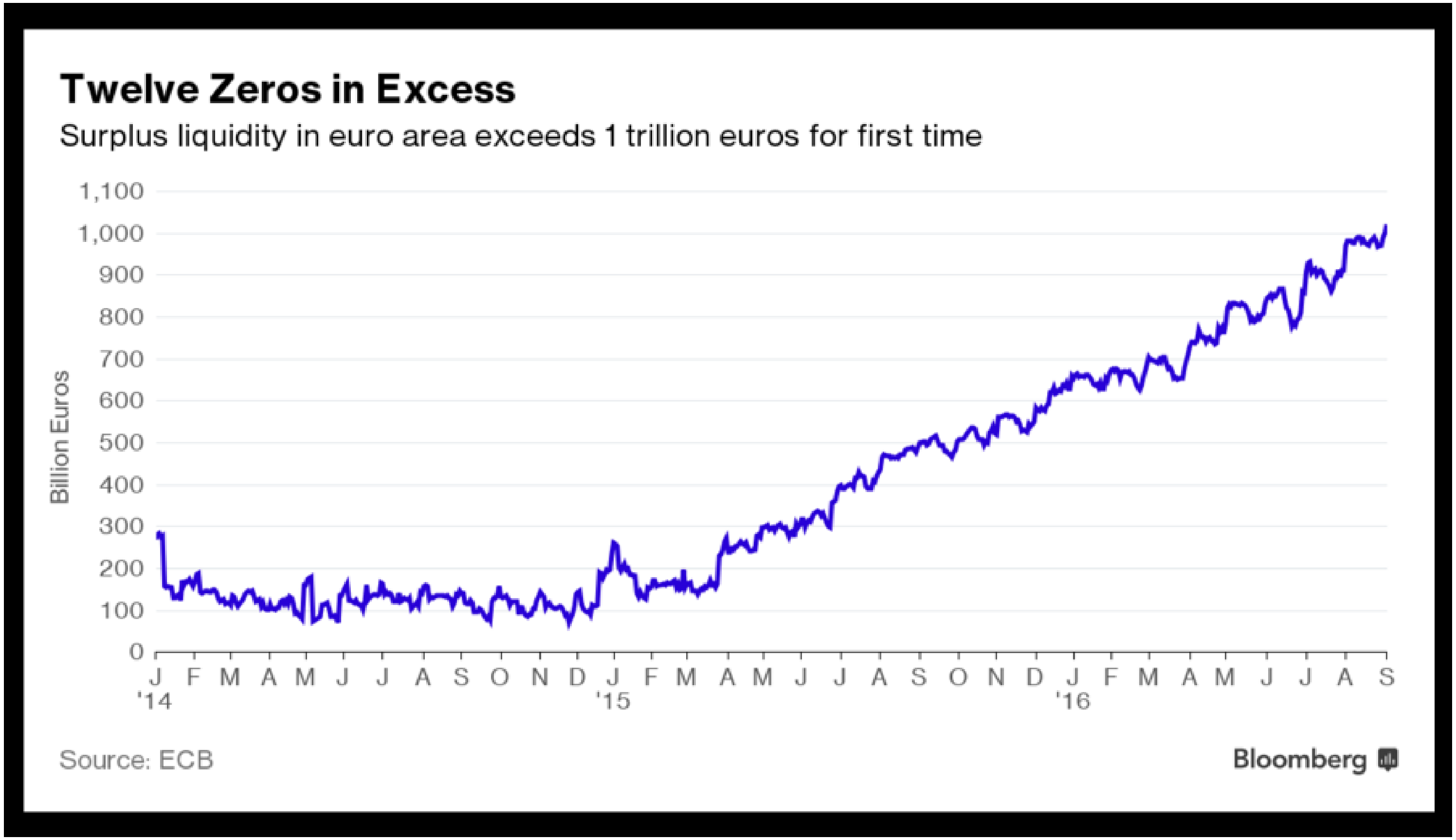
In the Entire Fixed Income Complex are upon us.

Negative Yields

Between $13-16 Trillion Sovereign Debt where the borrower is being paid

$1,000,000,000,000

European Central Bank has $1 Trillion euros sloshing around the financial system

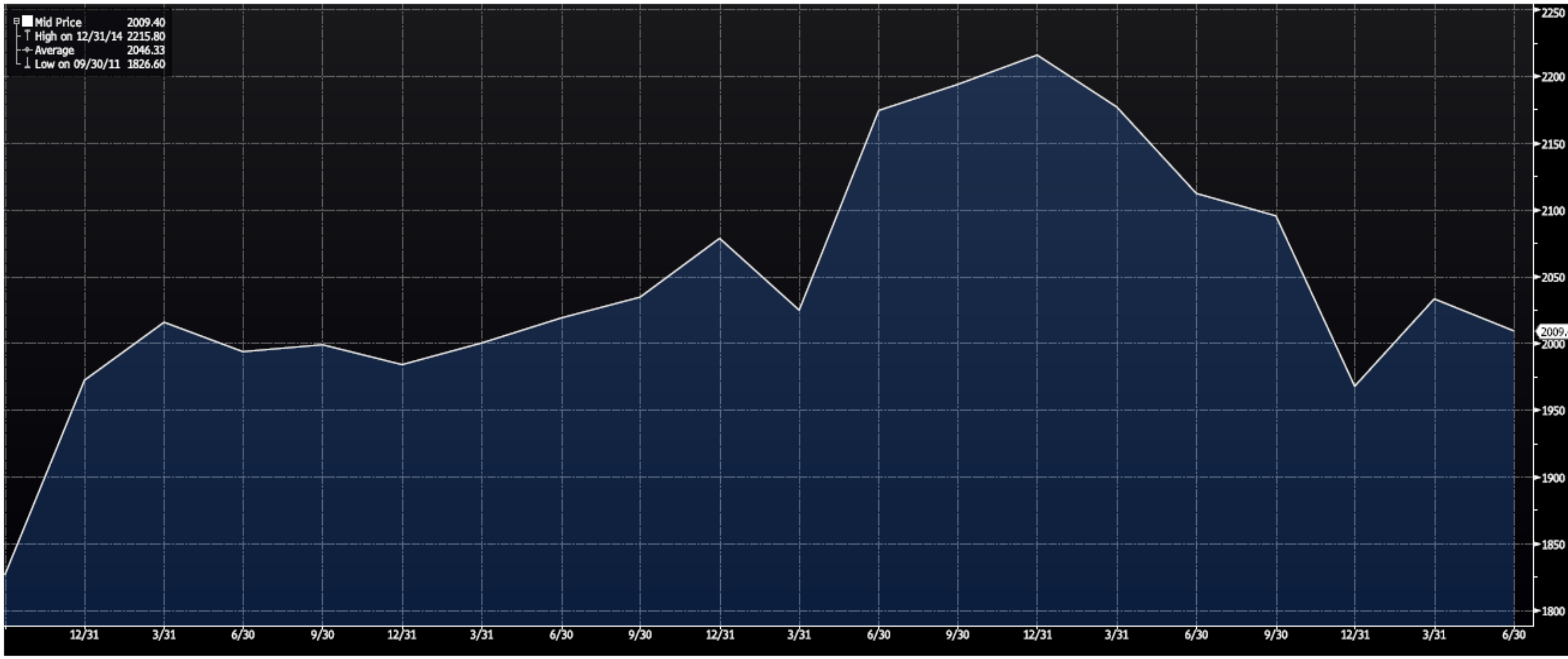


Denial Is Not A Strategy

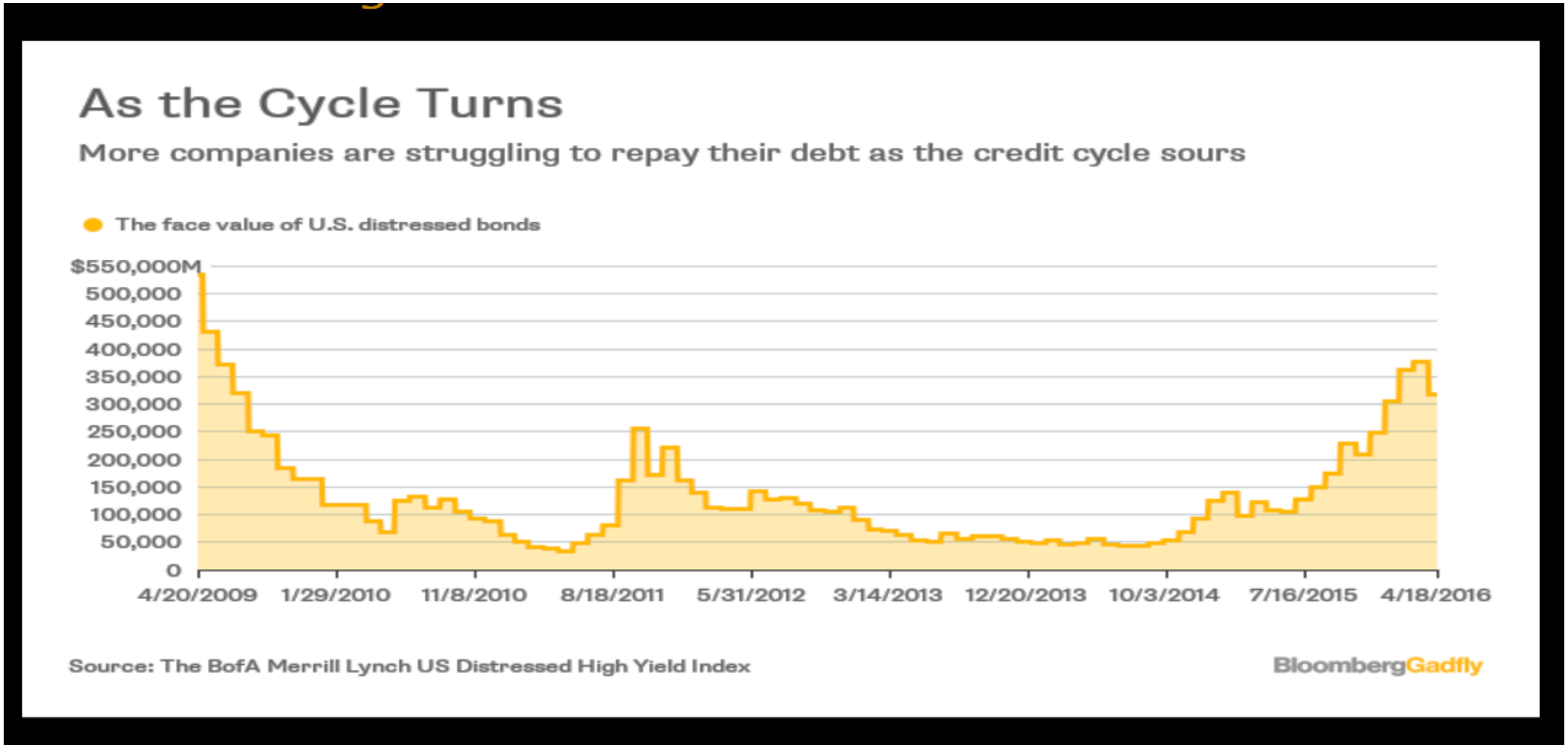
Post Credit Crisis:

- Lower interest rates are not stimulating
- growth
- Consumers are saving
- Central Banks are conducting desperate monetary policies
- These policies are creating asset bubbles
- Companies are using cheap capital to lavish shareholders
- Profits: 6 Negative quarters

Corporate Profits Cloud US Investment & the Hiring Outlook



If this chart represented a stock's price would you buy it?



Two years ago the recovery rates for bond investors was 44 cents on the dollar…now it's 29 cents.

Average Ratings Have Fallen to BB: 15 Year Lows

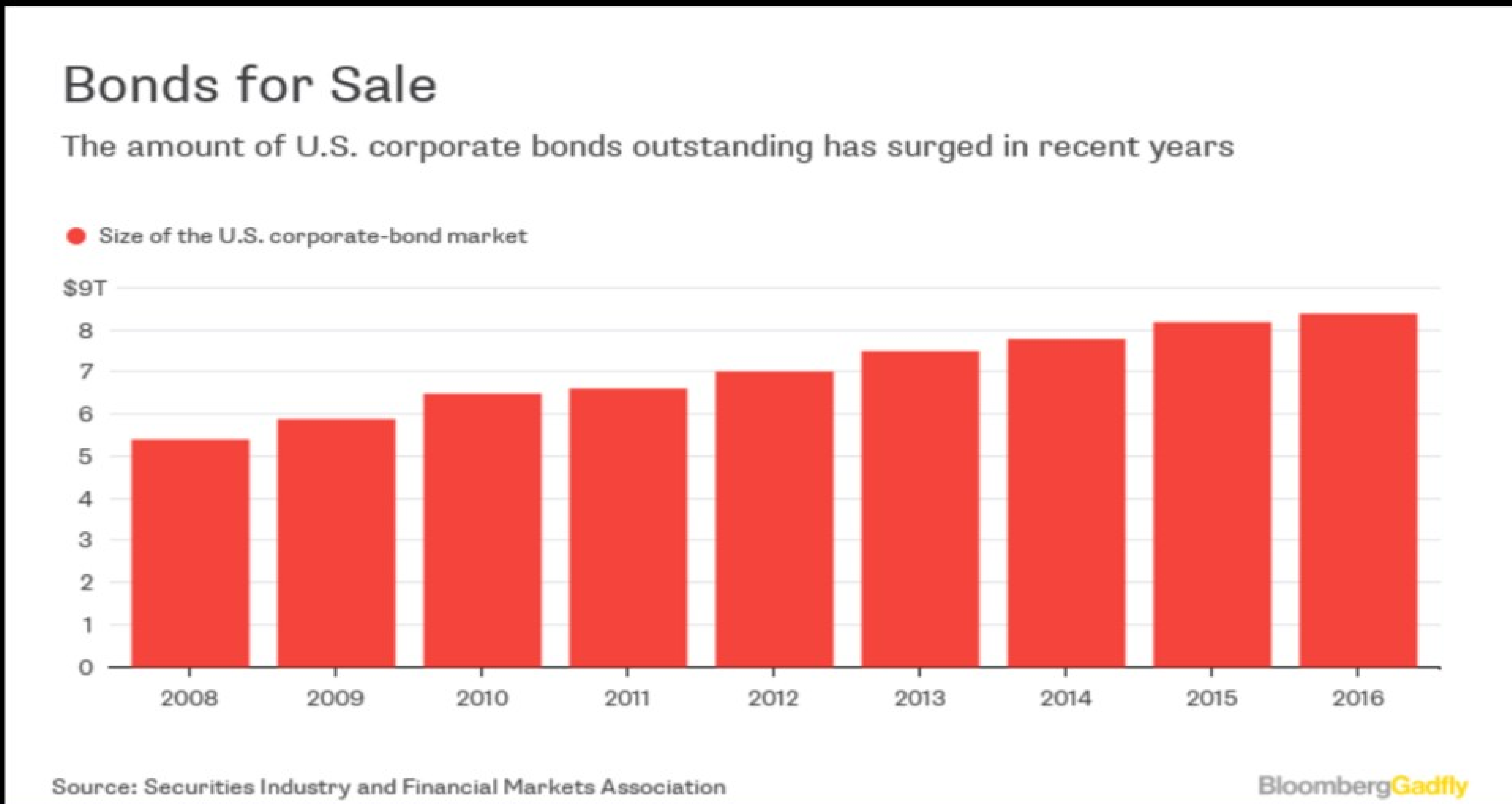
Credit Bubbles End Painfully

Sooooo...

- Stick with Investment Grade and Quasi Investment Grade Bonds
- When the credit bubble bursts you'll lose less with individual bonds than with mutual funds or ETFs
- Those individual issues have finite maturities you can wait out—not so with funds.

Bonds For Sale

The Amount Of US Corporate Bonds Outstanding



Echoes of 2009

Since the credit crisis we haven't seen so many companies with such huge debt problems

Bed Bath & Beyond Inc.

3.749% due August 1, 2024 Callable 5/1/2024

Amount Outstanding $300 million

Rated: Baa1, BBB+

CUSIP: 075896AA8

Yield to Maturity: 3.10%

Change of Control

Corporate Bond Investment Ideas

Under Armour

3.25% due June 15, 2026 Callable

Amount Outstanding $600 million

Rated: Baa2, BBB-

CUSIP: 904311AA5

Yield to Maturity: 3.125%

Change of Control

Corporate Bond Investment Ideas

WP Carey Inc.

4.00% due Feb. 1, 2025 Callable

Amount Outstanding $450 million

Rated: Baa2, BBB

CUSIP: 92936UAC3

Yield to Maturity: 3.80%

Look For REIT Bonds

		REIT	Bond
EPR	EPR Properties	4.74%	4.25% due 2025
HST	Host Hotels & Resorts Inc.	4.60%	3.58% due 2025
HIW	Highwood Properties Inc.	3.18%	2.80% due 2023
OHI	Omega Healthcare	6.31%	4.20% due 2025

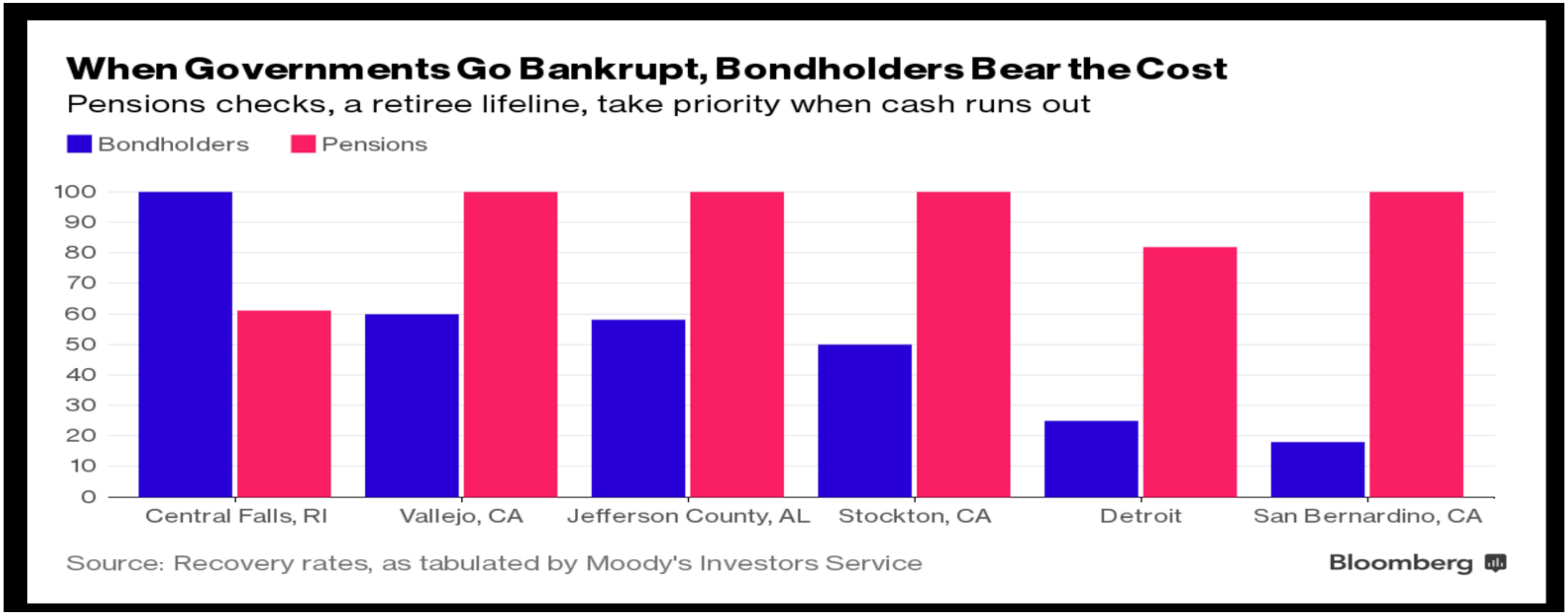
Don’t Overdo It!

The Screw Has Turned In Muniland

Pension Fund Assumptions:

- Unrealistic
- Underfunded
- Bankruptcies? More are coming
- Winners = Pensioners
- Losers = Pension Obligation & General Obligation Bondholders

Retirees Were Victorious Over Bondholders



Why should you care?

Because the money is coming out of our wallets

The "Bad Boys" of Municipal Bondland:

- Illinois
- Chicago
- Kentucky
- New Jersey
- Atlantic City
- Chicago Public Schools

Reconsider Your Definition Of Municipal Default

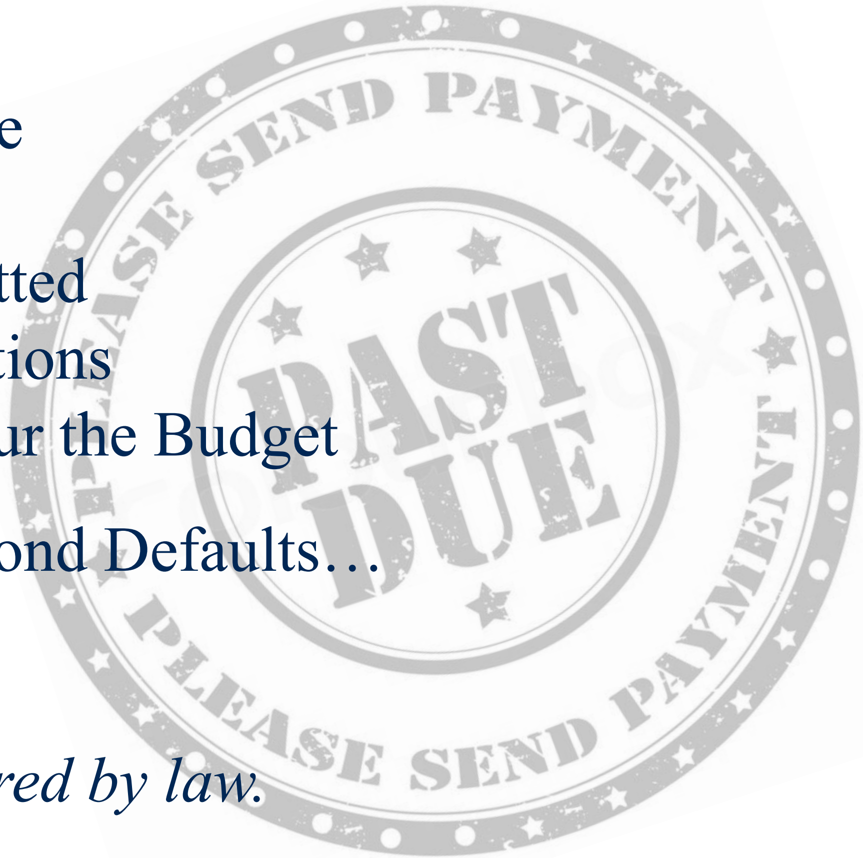
NON-MONETARY DEFAULTS:

- No Budget → Broken Governance
- Bills are Horrifically Past Due
- Essential Services Have Been Gutted
- Not Living Up to Pension Obligations
- When Unfunded Liabilities Devour the Budget

All the Above Are Precursors to Bond Defaults…

New Definition of Default:

Failure to do what is required by law.



Reconsider What Is Essential

• Fire stations	**No**
• Stadiums	**No**
• Court Houses	**No**
• Prisons	**No**
• Libraries	**No**
• Lighting Districts	**No**
• Museums	**No**
• Nursing Homes	**No**
• Small Hospitals	**No**
• Parking Garages	**No**
• Pension Obligation Bonds	**No**

Phrases To Look For

When reading Municipal Bond Official Statements look for:

- Large and diverse tax base
- Limited ability to issue more debt
- No interest rate swaps
- Debt service coverage in excess of 1.5 times
- Sources and uses of funds

All of the above points to Revenue Bonds, NOT General Obligations

THE ABILITY TO TAX THE POPULUS HAS NOTHING TO DO WITH THEIR CAPACITY TO PAY—THINK DETROIT

Which Municipal Revenue Bonds?

Airport Revenues:	San Francisco, LAX, San Diego, Orange County John Wayne, San Jose
Hospitals:	Stanford, Kaiser, Cedars, Scripps, Torrance Memorial, Huntington Memorial, Sutter Health, Dignity Health
RDA’s, TIF’s	Mature areas, little or no new financing, Northern and Southern CA only

Envision Capital Management, Inc.

Fixed Income Money Managers

Minimum account size $500,000

Fees:

- **Municipals .43%**
- **Investment Grade Corporates .60%**
- **Split-Rated Corporates .75%**
- **High yield 1%**

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