ALTMAN INVESTMENT MANAGEMENT

FIXED INCOME STRATEGY HIGHLIGHTS

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THE ECONOMIC OUTLOOK

Recent economic data has indeed been unsettling with ramifications for the U.S. economy and financial markets during the recent quarter. Investor dismay was reflected in the recent quarter's stock market performance and may persist for a while longer until the pace of the recovery improves. With government debt already at inflated levels, another round of government stimulus will most likely be met with some resistance.

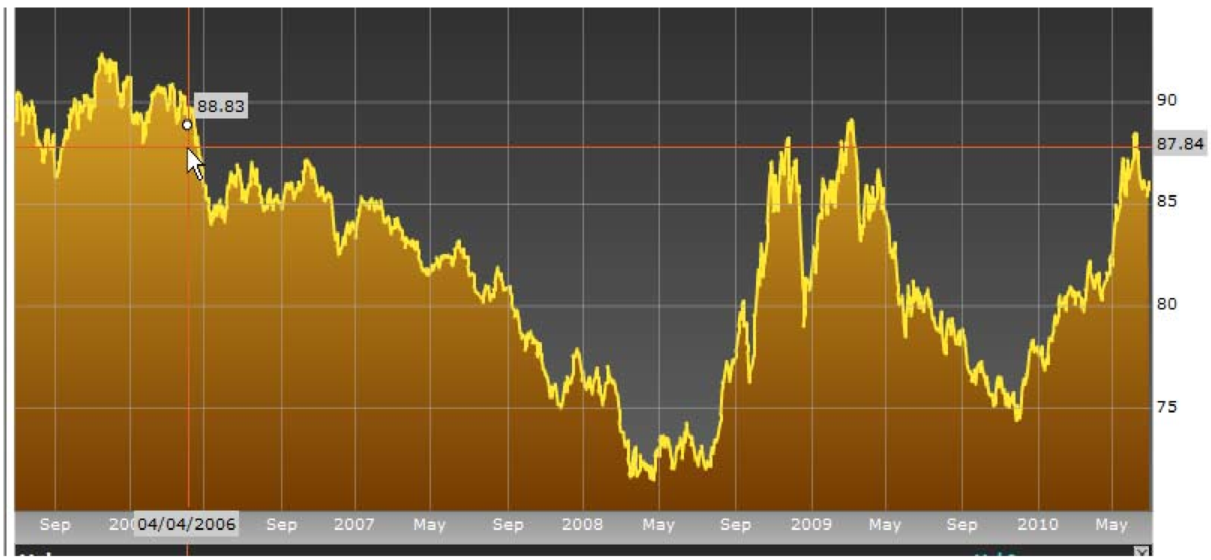
The Federal Reserve once again left rates unchanged at 0-.25 at its last meeting, keeping the language "for an extended period". High unemployment, lack of inflation and a weak housing market were some of the reasons why the Federal Reserve reiterated its interest rate policy at the June meeting. The Federal Reserve prematurely propped up its GDP forecast for 2010 to a range of 3.2 to 3.7 percent annual rate in the fourth quarter, up from a range of 2.8 to 3.5 percent due primarily to strengthening private demand. We believe that the growth rate in GDP will be modestly lower in the second half and have revised our forecast to 2.5% annualized rate. However, in anticipation of subdued inflation, the Fed lowered their inflation targets to 1.2 to 1.5 percent by the fourth quarter, down from 1.4 to 1.7 percent and consistent with our own outlook.

The CPI in May declined .2% after a .1% dip in April. The drop was mostly attributed to falling gasoline prices which declined 5.2%. Deflationary fears are once again resurfacing as European policy makers narrowed their focus on deficit reductions. This reversal in sentiment was reflected in the yield on the 10 year treasury now at 2.93%, down over 1% in the past several months. It now has become evident that these rate cuts initiated by the Federal Reserve have not been enough to stimulate private sector demand growth against a backdrop of high unemployment. There is a large body of opinion that believes that the combination of high taxation and government regulation provides a disincentive for corporations to begin the post recession hiring process.

However, we believe the current concern over deflation will be short lived in the midst of recovering corporate profits in the second quarter and continued strengthening global demand in China and other emerging economies. Since the financial crisis began in 2008, the Federal Reserve has made over $1 trillion dollars available to the U.S. banking system. Tightened lending policies coupled with high unemployment have kept inflation at bay. The Fed is now centered on the ballooning ratio of U.S. deficit to GDP, which now stands at close to 10-11%. Some economists fear this level of U.S. borrowing could cause foreign investors to lose their appetite for U.S. bonds and send our interest rates higher, sparking inflation.

The consumer sector appeared to be holding its own in May with the data reporting an uptick in consumer purchasing power and modest upticks in wages/ salaries and consumer spending. The U.S. savings rate peaked in Q2 2009, demonstrating the resiliency of consumption that with time should take the reigns and steer the economy forward along its recovery path. The recent figures reflected in the Consumer Confidence Index didn't confirm the coincident spending patterns when the index fell 3.9 points to 50.4 in July, the lowest reading since February. This drop is consistent with our expectations for slower economic growth in the second half.

EXHIBIT I
The Euro/US Dollar Index



Source: Altman Investment Management Research and Bloomberg

The U.S. dollar index has strengthened considerably since bottoming in 2008, as the U.S. economy slowly improves. More recent strength in the first half of this year has been a direct result of the weakening Euro amid the Greek sovereign debt crisis and worries over a possible contagion effect. Greece could choose or be forced to abandon the euro within the next several years, but the rest of the single currency zone should hold together.

On May 5th, the European Commission released its forecast for a slow but continuing economic recovery. Global GDP is estimated at 1% and 1.5% for 2010 and 2011 respectively. Typically GDP growth in Europe is led by a pick-up in exports, followed by employment growth which in turn stimulates internal consumption by the private sector. A key element to watch will be the effect that proposed austerity measures across European countries will have on future growth.

Despite the U.S. 10 and 30 year treasury rates trading at 2.98 and 3.93 respectively, the U.S. continues to be viewed as still one of the safest places to invest. The belief is apparent not only in domestic mutual fund and pension trading activity but also by foreign investors. Major foreign holders of treasury securities have increased by over 21%, since the market bottomed in March of 2009. It is argued that a higher interest rate environment within the U.S. is necessary to continue to attract foreign investment in order to maintain dollar strength. However, the underlying fundamentals for most of the major currency zones look poor, but the U.S. is the best of the bunch. This suggests that the dollar will remain firm over the next year.

There is much debate over the natural U.S. unemployment rate which is defined as an unemployment rate that is neither deflationary nor inflationary. For over a decade the rate is estimated to have been 5%. But the concern that the Fed remains on the side lines too long, with respect to interest rate policy as the former FOMC did, will thwart any efforts to stave off inflation. There was talk in the April Fed Meeting by some participants that the real rate is now around 6%. Some economists argue that a range of 6-8% is more appropriate given today's environment.

The June unemployment rate came in at 9.5%. Like past recoveries, we expect job growth to be somewhat subdued rather than a persistent upward slope. We are encouraged by the moderate gains in private sector employment and the gradual renewal of non-farm payrolls growth from trough levels in early 2009. We would expect the path to be uneven despite recent evidence that consumer sentiment continues to improve. The basic premise that the weak initial jobless claims are the result of special factors rather than an indication of a deteriorating employment situation is yet to unfold. Concern over jobs and income growth are more evident in the latest consumer confidence figures which fell almost 10 points last month. Consumer confidence will most likely continue to fluctuate in reaction to economic releases. Recovering industrial production coupled with an ISM composite index level holding above 50 support future job creation and should help bolster consumer confidence going forward.

The Federal Reserve Policy Revisited

There has been no shift in tone from Fed Chairman Bernanke. In a speech at the annual meeting of the Southern Legislative Conference of the Council of State Governments in early August, Bernanke struck a cautious tone on the current economic recovery, in line with that of his recent semi-annual testimony. He said that rising demand from households and businesses should help sustain growth as the boost from the rebound in inventories fades, and that the economy should continue to expand at a "moderate pace." He also cited notable headwinds in the near term, including the housing market, given the large foreclosure pipeline, and the commercial real estate sector. Furthermore, he noted that the recovery in the labor market has been sluggish and that "significant time" will be needed to restore the 8.5 million jobs lost over the recession. He again highlighted the high level of long-term unemployed, and the possible lasting ramifications on employment and earnings prospects. There was no change in language around financial markets either - Bernanke noted that domestic financial conditions have improved substantially since the recession, although were "somewhat less supportive of growth in recent months." The bulk of the speech focused on state and local government, the bottom line being that "dealing with the fiscal challenges at all levels...will be essential to ensuring that our...economy delivers rising living standards."

Once again in July during his Humphrey-Hawkins testimony, the Federal Reserve Chairman indicated that he would consider further policy actions to support a faltering recovery - including a strengthening of the "extended period" language and the purchase of additional assets. James Bullard, president of the Federal Reserve Bank of St. Louis, reiterated that additional Fed stimulus should take the form of Treasury purchases, rather than a hardening of the FOMC's commitment language.

In our attempt to quantify the effects of the Fed's unconventional policies on the ten-year Treasury rate to date, although the results are subject to considerable uncertainty, we found that (1) the Fed's purchase programs has lowered long-term yields by around 45 basis points, and (2) the FOMC's "extended period" language has had an additional effect of similar magnitude. While we believe that both commitment language and the asset purchase program have been effective in supporting the recovery, purchases of Treasuries may well be preferable course for providing additional stimulus. We arrive at this conclusion since the Fed has already picked the "low-hanging fruit" of the extended period language and will probably need to enter into a much more iron-clad commitment to keep rates low to achieve a further easing. However, we conclude that the Fed took the right first steps by reinvesting maturing mortgage receipts back into the markets instead of withdrawing the capital.

A Closer look at the Numbers to Arrive at Our Revised 2.5% GDP Forecast for 2010

First, we considered the impact of the Fed's entire asset purchase program on long-term Treasury rates. Considering the effect of the whole $1.75tr purchase program rather than Treasuries alone is helpful because the announcements were spread over two dates: (1) the November 25, 2008 announcement to buy $600bn of assets ($500bn of mortgage-backed securities (MBS) and $100bn of agency debt), and (2) the March 18, 2010 announcement to buy an additional $750bn MBS and $100bn of agency debt and to start the purchase of $300bn in Treasury securities. The underlying idea of considering the entire program is that purchases of different asset classes have a high degree of substitutability as they all reduce the supply of long-duration government-guaranteed or quasi-government-guaranteed assets.

Second, we looked at past periods in which the Fed attempted to boost the economy through a commitment to low rates. We identify three periods in which the FOMC signaled its intention to leave its policy rate on hold: (1) between August 2003 and January 2004 the FOMC intended to keep rates low for a "considerable period", (2) in December 2008 it announced to keep the funds rate unchanged "for some time" and (3) in March 2009 it adopted the "extended period" language. We combine these observations as a period that denotes when the FOMC announced to stay `on hold'. While this is clearly a simplification we view this language a very different than the period from January 2004 to December 2005 during which the Fed signaled its intention of `gradual tightening' through a "patient" and then a "measured" withdrawal of policy accommodation.

We also took into account a number of economic variables that affect Treasury yields, including changes in private payrolls, the ISM manufacturing index and long-term inflation expectations (as published by the University of Michigan/Reuters). We incorporated the corporate Baa yield to reflect changes in overall attitudes to risk that may or may not be related to the Fed's policies.

It is important to mention that an exercise in successfully predicting the economic outcomes of Fed policy is an extremely difficult process encumbered by multiple variables, many of which change at the same time. For example, the size of any effects are sensitive to how we adjust for risk appetite in the market—i.e. whether we include credit spreads or stock market indicators instead of the BAA yield. Still, we believe that the above results provide a useful benchmark for disentangling the effects of any Fed's unconventional policies.

Our results suggest that both the Fed's commitment language and its asset purchase program have been effective in reducing long-term rates and thus supporting the recovery. However, we believe that in order to achieve a further easing, the committee would probably need to adopt a defined time period for a rate hike or an economic condition (presumably one that seems relatively distant at present). The committee may well regard such a commitment as more constraining—and hence more dangerous from a risk management perspective—than a renewed asset purchase program. Hence, another Treasury purchase program may well be the preferred avenue for providing additional monetary stimulus. The first step in this direction was implemented last week at the proposed reinvestment of maturing mortgage backed securities receipts—a step that was already discussed at the June FOMC meeting.

The Federal Open Market Committee as we expected, decided to reinvest principal repayments of agency and mortgage-backed securities in Treasury securities. With this change in policy the Committee reacted to a downgrade in its assessment of the economic outlook, recognizing that "the pace of recovery … has slowed in recent months." Kansas City Federal Reserve President Thomas Hoenig continued his dissent. The reinvestment decision marks a step towards a more expansionary monetary stance in that it removes a slight bias toward tightening of the monetary policy stance.

By announcing to keep the balance sheet fixed—rather than letting it shrink over time—the Fed thus raised the expected future stock of asset holdings and thereby eased monetary conditions. Estimates from Goldman Sachs indicate that this shrinkage would be in the neighborhood of $200bn from that time through the end of 2011 (roughly a 21-month period, so just short of $10bn per month), though of course this figure may have risen as lower interest rates would have instigated more mortgage refinancing. Our best guess at identifying the effect of past Fed purchase announcements suggests that the ten-year Treasury rate might fall by 2½ basis points for every $100bn of expected purchases. The markets reaction on the announcement—a 6-basis-point drop in ten-year Treasury rate— suggests that the market had been expecting the balance sheet of the Fed to shrink at least $250bn over the next few years. It appeared that the markets were not completely surprised by this decision.

The decision was taken in response to a downgrade of the FOMC's economic outlook. The Committee demoted its previous assessment—that "the economic recovery is proceeding and that the labor market is improving gradually"—to "the pace of recovery in output and employment has slowed in recent months." Household spending is now seen to be increasing only "gradually" and the description of business spending on equipment and software was changed from "has risen significantly" to "is rising." The one upgrade was the Committee's removal of the observation that "financial conditions have become less supportive of economic growth." Overall, the statement concluded that the pace of economic recovery is likely to be "more modest in the near term than had been anticipated," instead of "moderate for a time."

Changes in the inflation paragraph were inconsequential, removing references to declines in prices of energy and other commodities, but continuing to note that "measures of underlying inflation have trended lower." In our view, it is noteworthy that the Committee chose to keep this phrase in the statement despite upward revisions to the core PCE index. Those revisions preserve the sense of disinflation, but from a slightly higher position than had previously been reported.

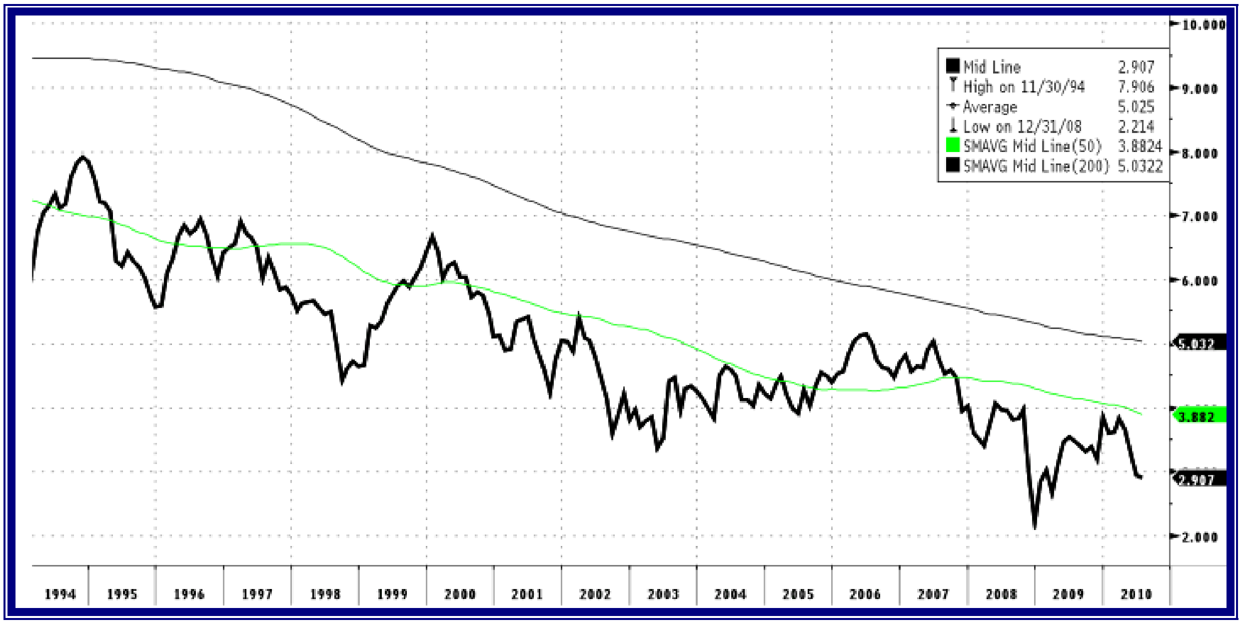
The Trade Deficit widened more than expected to $49.9bn in June, from a slightly downward revised May level (revised from $42.3bn to $42bn). The sharp widening is driven by a decline in exports (down $2bn, or a nominal 1.3% decline) and an increase in imports (up $6bn, or a 3% nominal increase). The decline in exports is mainly due to a fall in goods exports (driven by declines in capital goods exports, in particular) while exports of services rise slightly (by 0.8%). The surge in imports is also mainly due to goods (and consumer goods in part-ticular), although services imports rise too. As a result, the real trade deficit in goods widens by $8billion (of which only $0.5bn is due to petroleum).

This is a much larger deterioration in the trade balance than Commerce assumed in its preliminary estimate of second-quarter GDP, which showed 2.4% annualized growth. The report therefore adds to other indications (from previous data on construction outlays and inventories) of a downward revision to this figure. Absent significant upside surprises in upcoming reports on retail sales and inventories, we would put this revision somewhere in the 1% to 1½% range.

THE U. S. FIXED INCOME MARKETS

In our view, heightened uncertainties are bound to persist, led by sovereign developments in Europe and U.S. financial regulatory reform. The extraordinary challenges associated with the former, and the highly politicized nature of the latter, suggest headline risk could potential surface over the ensuing quarters. Unfortunately government fiscal tightening and more constraints on U.S. financial institutions are hardly the most constructive backdrop to ensure a robust global recovery and renewed employment growth. Slower potential growth suggests that government bond yields – which typically rise at this stage of the cycle as risk appetites improve – are likely to remain anchored near current levels. That is, except for the periphery nations in Europe, where rates should stay elevated relative to core AAA issuers for some time.

EXHIBIT II
Ten Year Generic Treasury Yield



Source: Bloomberg and Altman Investment Management, LLC

Importantly, the substantial threat to financial market stability and renewed economic growth should keep major central banks on the sidelines until 2011. Benign inflation pressures provide policymakers with the additional latitude to delay normalizing overnight rates. Liquidity premiums have also risen across spread sectors and in inflation-linked debt (though these instruments are direct government obligations, they do not typically benefit from safe haven flows). The dearth of expedient solutions in Europe and the summer season has done little to boost liquidity prospects near term. Thus, fragile market conditions and elevated volatility are more likely to prevail in coming months than market rallies. While credit spreads are likely to grind wider near term, we do not recommend reducing risk exposures. Indeed, current valuations are trading at recessionary levels even though fundamentals are still quite favorable. Investors with a longer view should leg into this pullback during the coming months by opportunistically adding solid high beta credits and quality issuers.

GOVERNMENT RELATED DEBT

Although spreads currently trade near long-term norms, even modest widening is likely to generate out performance compared to risk-free debt. U.S. government-sponsored enterprise (GSE) step-up coupon structures currently offer the best value. These structures diversify portfolios and are a defensive hedge against rising interest rates. Short callable GSE debt also is attractive relative to certificates of deposit. In non-callable (bullets), supranational debt (e.g., KFW, EIB) provide yield pick-up relative to U.S. agency debt.

Spreads on current coupon agency pass-through MBS are near historic lows. Although spreads should be well-supported in the near term, current valuations are not compelling, in our view. As opposed to pass-throughs, Ginnie Mae CMOs are attractive since investors can purchase this government-backed debt with higher yields and protection against extension risks, in some structures. In ABS, investors should focus on lower quality to identify relative value, particularly amongst the BBB-rated credit card and retail auto issues, which compare favorably to unsecured corporate debt.

EXHIBIT III

10-year U.S. Government Agency Yield minus 10-year Treasury Yield

Source: Bloomberg and Altman Investment Management, LLC

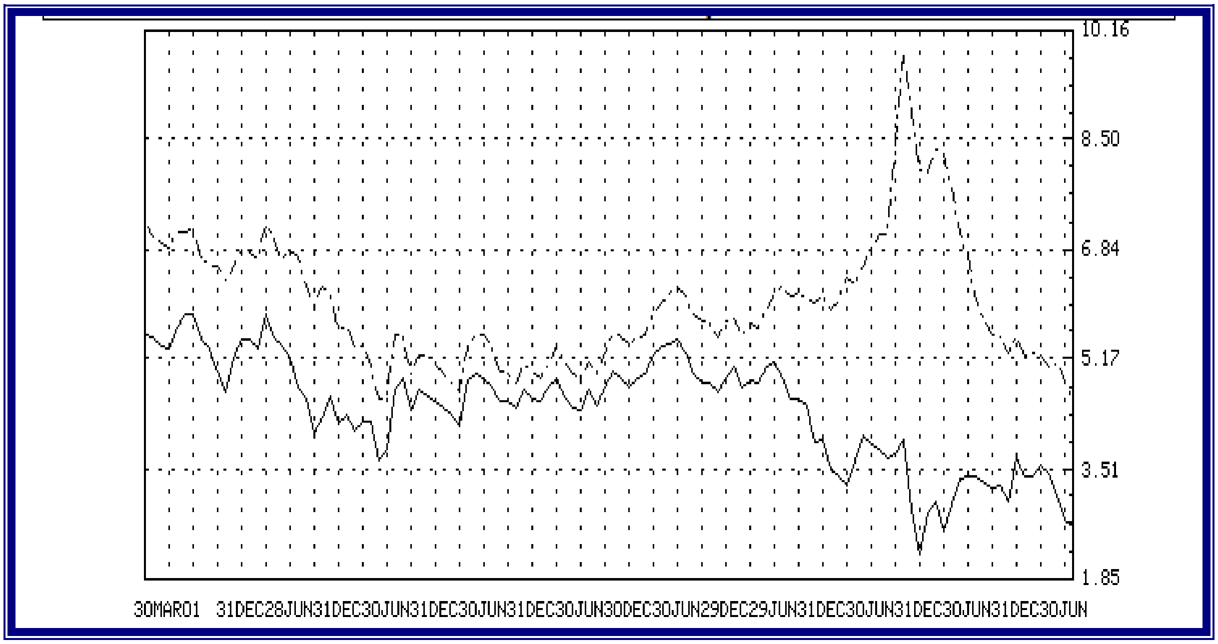
HIGH GRADE CORPORATES AND PREFERREDS

Although risk aversion triggered by the European crisis has overshadowed spread compression for now, the fundamental backdrop for U.S. corporate bonds remains positive. That said, we expect cash spreads to continue grinding wider in the near term (primarily in financials) until a resolution on the European situation becomes more apparent. Keep in mind that the same factors which led us to favor corporate bond performance compared to other fixed income sectors remain intact.

We do not advise investors to reduce overall credit exposures. Instead, we recommend taking advantage of the recent spread widening to look for attractive opportunities in high quality U.S. corporate debt. We continue to recommend paring exposure to European banks, given the challenges associated with periphery debt, slowing growth prospects, higher capital requirements, and liquidity constraints. There hasn't been new issuance of bank debt in Europe since the beginning of May. We favor the Life Insurance, Metals & Mining, and U.S. REIT sectors. Moreover, relatively steep credit curves offer better opportunities to slightly extend duration.

EXHIBIT IV

U.S. Corporate 7-10 year (dotted line) versus U.S. Treasuries 7-10 year (solid line)



Source: Bloomberg and Altman Investment Management Research, LLC Data: ML Global Bond Indices:

Value still exists in the capital trust preferred arena, consistent with our positive conviction on subordinated bank debt. We favor preferred issues with high liquidity amongst the largest bank/finance/insurance names. We recommend capital trust preferreds of U.S.-based issuers compared to the UK and other Euro-area financial institutions. The best opportunities continue to be reflected in the primary market, which currently trade cheap compared to secondary issues.

EXHIBIT V

		12/31/2009	3/31/2010	06/31/2010
10 Year Muni *		3.96%	3.96%	3.71%
10 Year Treasury		3.83%	3.83%	2.95%
Ratio		103%	103%	125%

Source: Bloomberg and Altman Investment Management, LLC
** Merrill Lynch Global Index- Investment Grade*

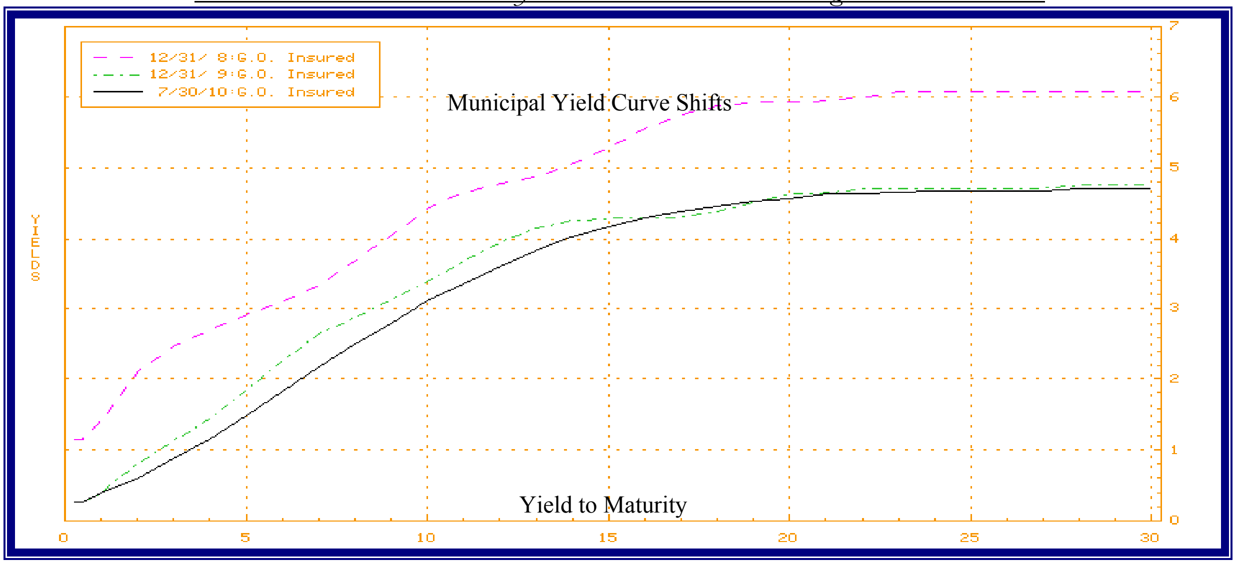
* The impact of an upward shift in the yield curve on long duration instruments suggests that positive performance will likely be led by return on the cost of borrowing, not the price of the issue.

MUNICIPAL BONDS

While municipal spreads relative to Treasuries have risen and ratios reflect improved valuations, absolute yields are anemic. Headlines related to municipal budget strains (e.g.; Central Falls, RI) and the European crises have been the root cause. We expect this trend to continue as geopolitical risks persist, budget gaps are addressed, federal funding diminishes and 2011 solvency issues resurface. Additionally, recent developments about IRS audits to ensure that BABs were sold at the initial offering price (where at least 10% of the bonds are sold to the public) may have negative credit implications, driving spreads wider. Investors should focus on high quality issuers. We recommend AA GO spreads with a focus on 5-10 years to maturity.

EXHIBIT VI

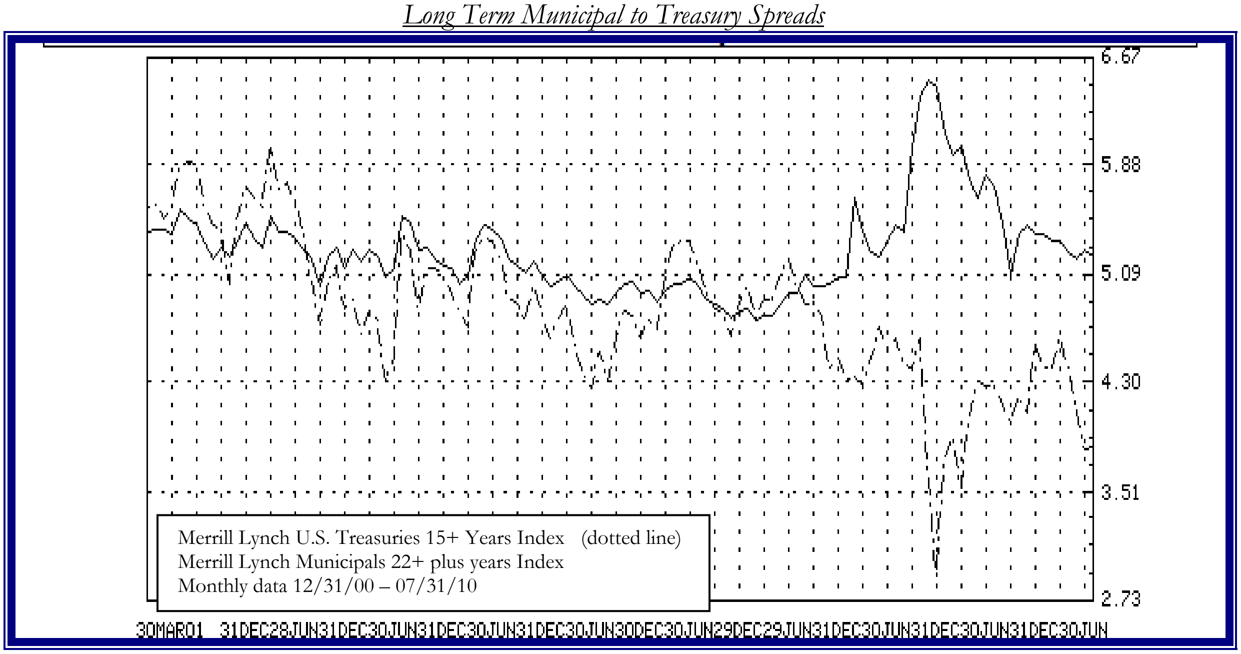
Fair Market Yield Curve History: Generic Muni - General Obligation Insured Curves



Source: Bloomberg and Altman Investment Management Research, LLC

EXHIBIT VII

Long Term Municipal to Treasury Spreads

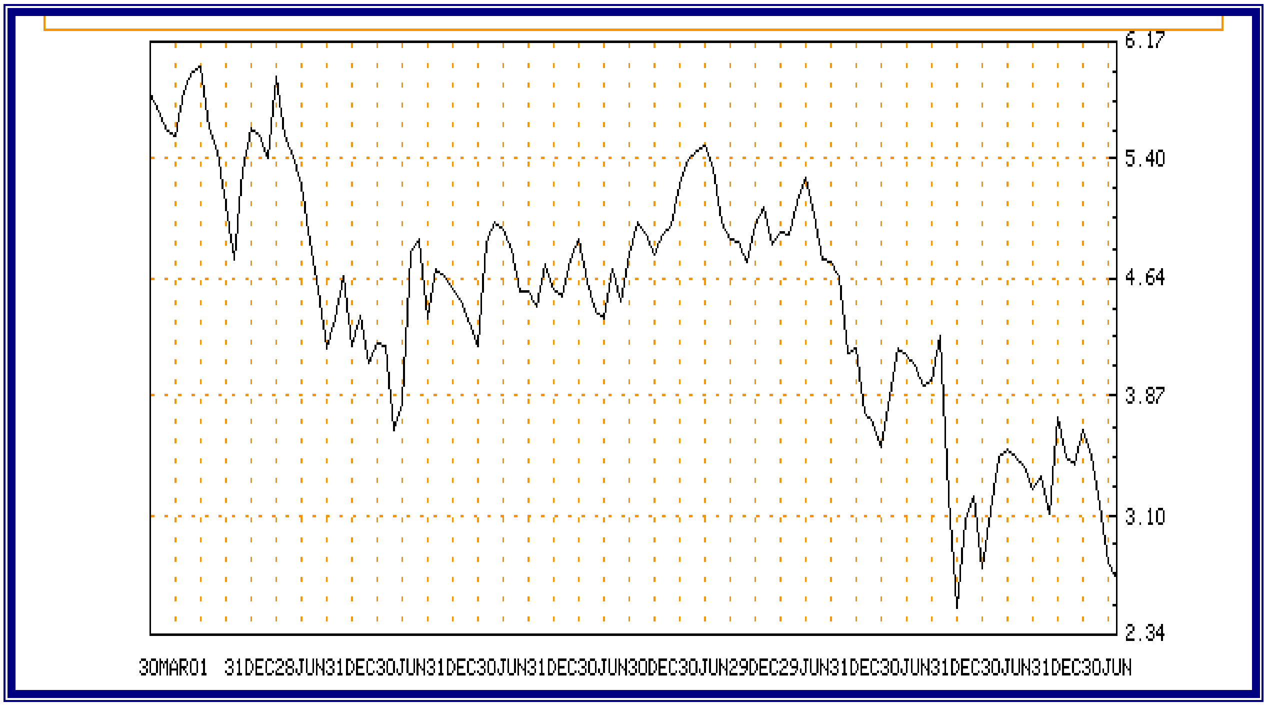


Source: Bloomberg and Altman Investment Management Research, LLC

Long term Municipal to Treasury spreads widened significantly in the second half of 2008 illustrating the massive move into the safe haven of U.S. Treasuries. While municipals have rallied through 2009 with yields leveling out in 2010 closer to its mean, long term U.S. Treasuries remain well below mean levels.

EXHIBIT VIII

Long Term U.S. Treasuries



Source: ISM, Haver Analytics