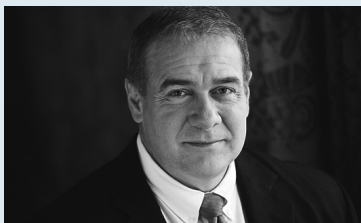


QUARTERLY INVESTMENT FOCUS: 4Q 2010

Opportunities in Municipal Finance

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Opportunities in Municipal Finance



BY SCOTT MINERD

Chief Investment Officer,
Guggenheim Partners, LLC

Each quarter Guggenheim Partners selects an investment theme, asset class, or sector to highlight. In this inaugural edition of our Quarterly Investment Focus, we offer our perspective on the municipal finance market, a key vehicle for investors to access attractive risk-adjusted returns relative to other fixed income asset classes.

While challenges remain for many state and local municipalities, the blanket misperception of credit deterioration across the asset class has led to wider spreads for even the most credit-worthy municipal debt issuers.

Through careful security selection and credit analysis, we believe the municipal market presents an opportunity for fixed income investors to access attractive risk-adjusted returns while increasing credit quality and diversification.

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Municipal finance is a \$2.8 trillion fixed income marketplace that is the primary source of capital for U.S. state and local governments. Through careful credit analysis and security selection, we believe the municipal bond market currently presents an attractive opportunity for investors relative to other fixed income investments for the following reasons:

Headline credit concerns based on a handful of issuers have led to higher yields for even the strongest municipal credits. By deciphering the true strength of underlying credits in the municipal market investors can benefit from historically wide spreads.

- ▶ The spread to Treasuries for AA-rated taxable municipal bonds is 114 basis points wider than its historic average, 71 basis points wider than an AA-rated diversified credit index, and 29 basis points wider than an A-rated corporate bond index, as of 3Q 2010.
- ▶ Relative to Treasuries, AAA-rated tax-exempt municipal bond yields are 16 percentage points higher than historic averages. As of 3Q 2010, this would equate to an additional 39 basis points of yield for investors.
- ▶ Mean reversion to historic municipal market spreads would result in outperformance relative to virtually every asset class in fixed income, with the potential exceptions of high yield corporate bonds and asset backed securities.

In addition, for many municipal credits the road to recovery is underway as the most recent data on state revenues showed the second consecutive quarter of gains. However, due to the diversity of issuers in the municipal market, in-depth credit work and careful security selection remain paramount to maximizing risk-adjusted returns.

Given the attractive yields, as well as the opportunity to increase diversification and credit quality, a reasonable allocation to taxable municipal bonds would be 20 percent of a fixed income portfolio. In the current low yield environment, municipal bonds represent an attractive investment opportunity, but we emphasize the need for careful security selection and ongoing credit analysis.

The Municipal Market at a Glance

TYPES OF MUNICIPAL BONDS

The municipal finance market is dominated by two types of securities – general obligation bonds (“GOs”) and revenue bonds. In 2009, GOs represented 38 percent of total new issuance (\$155 billion) while revenue bonds accounted for 62 percent (\$254 billion).

GENERAL OBLIGATION BONDS

General obligation bonds are debt instruments secured by the pledge of the issuer’s full faith, credit, and, in many cases, taxing power. The primary source of repayment for GO bonds is property taxes at the local level and a combination of income tax and sales tax at the state level. From an investor’s standpoint, GO bonds are attractive because they are secured by the ability to raise taxes to meet obligations. However, certain GOs – called limited GOs – have an inherent tax cap associated with the security.

REVENUE BONDS

Unlike GO bonds, revenue bonds are secured by claims on non-tax revenues derived from tolls or fees associated with the project or facility being financed by the bond issue. Projects financed by revenue bonds generally include water/sewer facilities, public power/utilities, airports, and toll roads.

APPROPRIATION BONDS

Another popular financing vehicle for state and local governments is appropriation bonds. These debt instruments are secured by a “promise to pay” with legislatively approved appropriations. Typically, appropriation bonds carry a rating one notch lower than an issuer’s GO bonds due to the fact that the sources of interest and principle payment can be directly, and possibly adversely, impacted by legislation.

Municipal finance is a \$2.8 trillion fixed income marketplace that allows a diverse group of issuers such as states, local governments, public universities, hospitals, and other related entities to finance capital projects and fund services. Investors in municipal debt can purchase bonds on a taxable or tax-exempt basis. Traditionally, the market for tax-exempt bonds has accounted for 94 percent of municipal debt issuance. During the recent financial crisis, however, the market for taxable bonds increased dramatically. The most notable change was the introduction of Build America Bonds (“BABs”), a federal program that expanded the amount of taxable debt issued by state and local governments by 250 percent from 2008 to 2009. Other important trends in municipal finance include:

► **EXPANSION OF THE MUNICIPAL BOND INVESTOR BASE:** Traditionally, the primary investors in municipal bonds were U.S. banks, households, property and casualty (“P&C”) insurance companies, and other taxable investors that benefited from tax-exempt coupon payments. With the advent of the Build America Bonds program, state and local governments were able to increasingly issue taxable bonds to investors. From April 2009 to September 2010, approximately \$135 billion of taxable BABs were issued. As of the end of the third quarter, nearly 32 percent of municipal securities issued in 2010 were taxable bonds – a significant change considering that from 1988 to 2008 only 6 percent of the market on average was taxable. The advent of the BAB program has expanded the investor base, opening up the municipal market to pension funds, tax-exempt organizations, and foreign investors. For example, life insurance industry holdings of municipal bonds increased 73 percent from 1Q 2008 to 1Q 2010, and foreign investor holdings increased 49 percent over the same period.

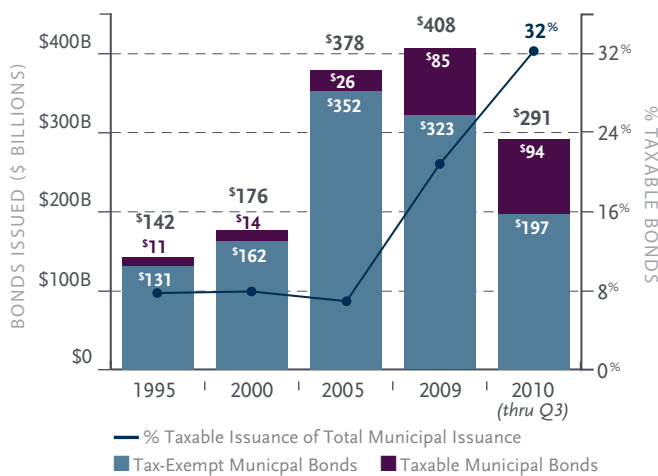
► **MISCONCEPTIONS OF MUNICIPAL CREDIT QUALITY:** The credit history of municipal bonds is exceptionally strong, especially with regards to general obligation bonds (“GOs”), which are debt instruments secured by the pledge of the municipality’s full faith, credit, and (most importantly) taxing power. While investment grade municipal defaults are historically much lower than their corporate bond counterparts, the Great Recession led to defaults on a host of unrated municipal bonds generally associated with real estate developments and long-term healthcare facilities. The blanket misperception of credit deterioration across the entire asset class has led to wider spreads for even the most credit-worthy issuers. We believe this presents an opportunity for investors who understand municipal credit to benefit from attractive spreads on securities that can withstand even “double-dip” scenario stress testing.

► **HISTORICALLY WIDE SPREADS = ATTRACTIVE ENTRY POINT:** As of the end of 3Q 2010, municipal bond indices offered higher yields compared with other fixed income indices of similar duration and credit quality. The onslaught of negative news and the sporadic defaults among unrated municipal bond issuers have led to higher yields across the taxable and tax-exempt municipal markets. This, in addition to improved corporate earnings that have compressed corporate spreads, has flipped the credit matrix – currently, municipal bonds of higher credit quality are trading at spreads wider than corporate bonds or sovereign debt with lower ratings.

As of the end of 3Q 2010, investment grade taxable municipal bonds were trading at spreads wider than corporate bonds or sovereign debt with lower credit ratings. We believe the municipal market presents an opportunity for fixed income investors to access attractive risk-adjusted returns while increasing credit quality and portfolio diversification.

GROWTH OF THE MUNICIPAL BOND MARKET

The municipal bond market reached a record \$408 billion in new issuance in 2009, thanks in large part to the Build America Bond program, which expanded the taxable municipal market by 250 percent over 2008 levels.



Source: Bond Buyer

HISTORIC CREDIT QUALITY COMPARISON

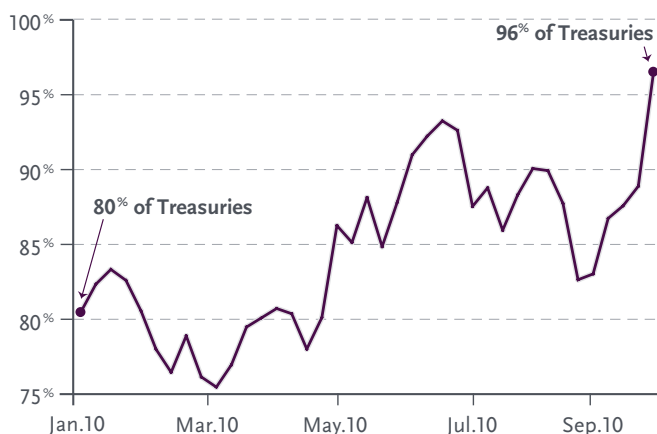
Based on cumulative data from major rating agencies, municipal bonds have registered significantly lower default rates than similarly rated corporate bonds over an extended period of time.

Rating	MOODY'S (1970-2009)		S&P (1981-2009)	
	Municipal Bonds	Corporate Bonds	Municipal Bonds	Corporate Bonds
Aaa, AAA	0.00%	0.05%	0.00%	0.82%
Aa, AA	0.03%	0.54%	0.03%	0.74%
A	0.03%	2.05%	0.06%	1.97%
Bbb, BBB	0.16%	4.85%	0.28%	5.60%
Bb, BB	2.80%	19.96%	1.63%	17.45%
B	12.40%	44.38%	7.05%	30.82%
Ccc, CCC	11.60%	71.39%	36.59%	53.41%

Source: Standard & Poor's, Moody's Investor Services

RATIO OF TAX-EXEMPT MUNICIPAL BOND YIELDS TO TREASURIES RATES

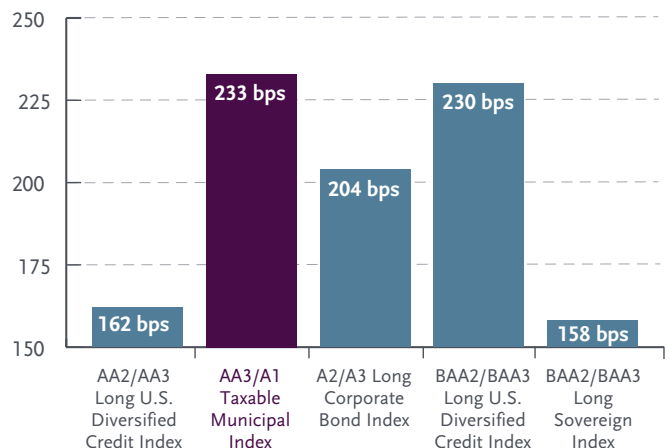
As of the end of the third quarter, tax-exempt municipal bond yields were approximately 96.4 percent of 10-year U.S. Treasury rates, an increase of 16 percentage points from January 2010.



Source: Thomson Reuters

TAXABLE MUNICIPAL BONDS: WIDER SPREADS THAN SIMILAR CORPORATE BONDS AND SOVEREIGN DEBT

As of September 30, 2010, taxable municipal bonds had an average option adjusted spread to Treasuries ("OAS") greater than corporate bonds or sovereign debt of similar or lower credit ratings.



Source: Barclays Capital

Performance and Relative Value

VALUE IN THE TAX-EXEMPT MUNICIPAL MARKET

AAA general obligation tax-exempt municipal bonds generally trade at a discount to taxable U.S. Treasuries of similar duration due to the tax-exempt status of the municipal bond's coupon payments. To measure value in the tax-exempt municipal bond market, investors typically look at trends in the ratio between tax-exempt municipal bond yields and U.S. Treasury rates.

Dating back to 1981, the average yield on a 10-year AAA GO tax-exempt municipal bond was approximately 80.75 percent of the yield on a 10-year U.S. Treasury bond. As of September 30, 2010, however, tax-exempt municipal bond yields were approximately 96.4 percent of Treasury rates. This is an increase of nearly 16 percentage points from January 2010.

To look it another way, applying the historic average of 80.75 percent to a recent 10-year Treasury rate of 2.51 percent from September 30, 2010, the result would be a tax-exempt municipal bond yield of 2.03 percent. However, as of September 30, 2010, the yield on a 10-year AAA GO tax-exempt municipal bond was 2.42 percent, or 39 basis points higher than its historic average. This is similar to the widening of spreads exhibited in the taxable municipal market. Municipal bonds, whether taxable or tax-exempt, are offering investors extra yield compared with historical levels.

The most recent data on taxable municipal bond yields demonstrate what we believe to be a compelling value proposition relative to corporate bonds and sovereign debt of comparable credit quality and duration. Amidst the current low-yield landscape of investment grade fixed income assets, here are some eye-opening data points on the returns available in the municipal bond market as of the end of the third quarter of 2010:

- ▶ The Barclays index of taxable municipal bonds was trading at an option adjusted spread ("OAS") to U.S. Treasuries that is 111 basis points above its historic average.
- ▶ The OAS of a taxable municipal bond index rated Aa3/A1 was 30 basis points higher than the OAS of corporate bonds rated A2/A3 of longer duration.
- ▶ The spread between the OAS of Aa3/A1 taxable municipal bonds and Baa2/Baa3 sovereign debt was 65 basis points, or 105 basis points wider than the historical relationship between the two indices.
- ▶ AAA, 10-year GO tax-exempt municipal bond yields were 96 percent of 10-year U.S. Treasuries rates, which equates to a yield 29 basis point higher than historic standards (see the call out box to the left for more information on tax-exempt yields).

The aforementioned data on taxable municipal bond spreads represent the first time in the post-Depression era that municipal bonds are substantively cheaper than similarly rated corporate bonds or sovereign debt. Reversion to historical spread relationships would imply price appreciation (spread reduction) in the range of 25 to 50 percent for a portfolio of taxable municipal bonds.

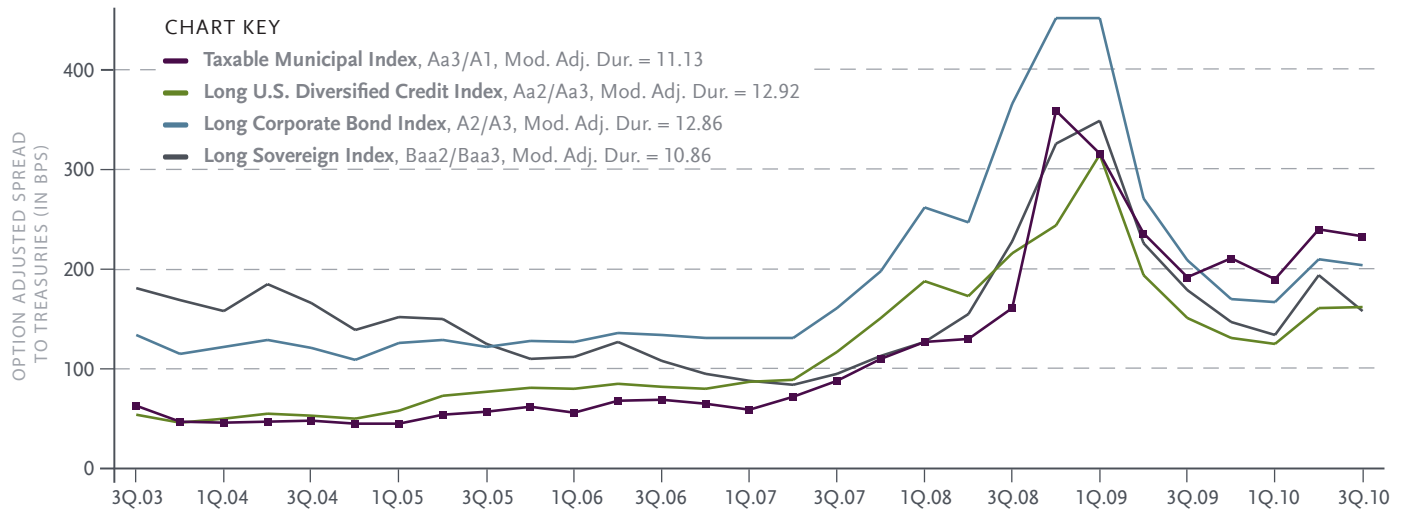
Market pricing like this generally signals either a secular change in the *perception of risk* (justified or unjustified) or a dislocation in supply and demand. It is our belief that both of these factors are at work simultaneously in the municipal bond market and are leading to the current spread widening. We believe these factors have created an attractive entry point for fixed income investors who are able to understand municipal credits.

First, there is the perception of structural credit deterioration in the municipal market. The widening of spreads across the municipal market seems to have more to do with a change in the *perception of risk* rather than any observable, structural change in risk across the asset class.

As of the end of the third quarter 2010, there were 246 municipal bonds, valued at \$7.5 billion, in payment default or experiencing credit impairments, according to data from Municipal Market Advisors. Of the 246 troubled bonds, nearly 75 percent were real estate backed projects. Only 53 of the 246 were initially rated, none of which were issued by a state or a large municipality. Out of a universe of approximately 29,000 municipal bonds currently rated by Moody's, the 53 initially rated bonds experiencing a default or impairment equates to less than one quarter of one percent of the rated market (0.18 percent). The total universe of outstanding municipal debt is approximately \$2.8 trillion, which means by dollar value the \$7.5 billion of total debt in default or experiencing impairment is 0.26 percent of the total municipal market.

TAXABLE MUNICIPAL BOND YIELDS VS. OTHER FIXED INCOME SECURITIES

The graph below shows how the credit matrix has "flipped." Currently, taxable municipal bonds of higher credit quality are yielding anywhere from 29 to 75 basis points more than corporate bonds or sovereign debt of similar duration but lower credit ratings.



Source: Barclays Capital

Decades worth of data from Moody's and S&P shows that for Bbb and BBB-rated municipal bonds the historical default rate is 0.16 to 0.28 percent, which is in line with the default rates currently exhibited in the market. Therefore, any blanket assumption that the quality of the entire municipal finance asset class has eroded is not supported by the data thus far. With regard to the future, credit agency ratings were recently re-calibrated in 2010 and have not reflected a cause for industry-wide spread widening.

In addition to a change in the perception of market risk, we believe the second factor for spread widening is market dislocation, or a supply and demand imbalance. This stems from the rapid evolution of the taxable municipal market during the Great Recession, and the fact that when the Build America Bond program was first introduced as a part of the American Reinvestment and Recovery Act of 2009 it was announced with an expiration, or "sunset," date.

In the past two years, the supply of taxable municipal debt has expanded at a rate dramatically faster than investor demand. In 2009 and 2010 (through August), taxable municipal bond issuance was \$164 billion, which is nearly 210 percent more than all of 2007 and 2008 combined. Few investors or government officials realized back in mid-2009 what a successful program BABs would become, or that the legislation could possibly be extended beyond its initial sunset deadline of December 31, 2010.

As a result, life insurance and annuity companies, pension funds and endowments, international investors, and other large buyers of taxable fixed income assets were slow to enter the market for taxable municipal bonds such as BABs. Over time, the risk-adjusted returns in the taxable municipal market began to draw in

new investors. However, large segments of the traditional taxable fixed income investor base were slow to build out the expertise required for municipal bond credit analysis. The increase in supply of taxable bonds, without a subsequent and proportional increase in the investor base (i.e., demand), has helped support higher yields. The dislocation will ultimately be resolved whether the BAB program is extended or not.

If the BAB program is allowed to sunset, then the supply of taxable municipal bonds will decrease significantly year-over-year. Under this scenario, investors who own the limited supply of issued BABs are likely to benefit from price appreciation based on scarcity value.

If the BAB program is extended and it becomes clear that taxable bonds will become a more permanent part of the municipal market, price appreciation is also likely to take place as more investors will enter the market seeking to capture the excess spread and diversification benefits offered by BABs. Under this scenario, foreign and institutional buyers that were previously hesitant will likely begin to develop the necessary credit teams to focus on the taxable municipal market. As investor demand expands, prices are likely to rise and spreads will retreat back to historic norms.

Therefore, either as a result of scarcity value or a permanent increase in demand to match supply, we believe a carefully selected portfolio of taxable municipal bonds will experience price appreciation as the dislocation corrects itself. Price appreciation, combined with currently wide spreads, would cause this sector to outperform relative to virtually every asset class in fixed income, with the potential exceptions of high yield corporate bonds and asset backed securities.

The Bottom of the Credit Cycle

MUNICIPAL REVENUE CASE STUDY: A LOOK AT CALIFORNIA

In fiscal year 2009, the state of California collected \$174.4 billion – far and away the most revenue of any state or municipality. Of the \$174 billion in receipts, 26 percent was generated by personal income taxes, including capital gains taxes, and 18 percent was derived from sales tax receipts.

While the headlines may be grim, the good news for California is that in the second quarter of 2010, year-over-year personal income tax receipts rose 11.5 percent and sales tax revenues rose 10.1 percent. In addition, California's personal tax receipts are highly correlated to stock market returns. Over the past 10 years, the correlation between CA's personal tax receipts and Dow Jones Industrial Average returns is nearly 0.90. As the worst in the equity markets appears to be over, CA tax receipts should benefit further.

Despite these trends, in September 2010, state finance officials deferred paying \$2.9 billion of subsidies to schools and counties in order to pay bondholders. If necessary, the state said it will issue I.O.U.s or delay payments to further ensure that bondholders are kept in the highest priority.

So while the headlines will likely declare California to be the next black hole among municipalities, the story for bondholders is actually one of increasing tax revenue, declining expenses, and supreme dedication to its bondholders.

It is generally understood that severe downturns do not end by the economy suddenly springing to life overnight. The first step is always for things to stop deteriorating. The next step is to start to see improvement, however modest it might be at first.

Likewise, from an investor's standpoint looking at the municipal market, it is less important to predict when state and local government revenues (which are overwhelmingly driven by tax receipts) will once again reach 2006 and 2007 levels. Undoubtedly, obtaining those peaks once again will take a number of years. Nonetheless, timing the bottom of the credit cycle and the beginning of recovery in the municipal market represents a significant opportunity for investors. Based on the most recent data on state tax collections, we believe certain states have already begun to turn the corner, especially when one combines the recent revenue recovery with newly enacted fiscal discipline.

Beginning in the fourth quarter of 2008, total state tax revenues declined for five consecutive quarters. The worst of this period came in the first and second quarters of 2009, when total state tax revenues declined 11.5 and 16.5 percent, respectively. It wasn't until the first quarter of 2010 that state revenues witnessed their first period of positive year-over-year growth. According to early reporting from the Rockefeller Institute, the data from 2Q 2010 has been positive for the second consecutive quarter. While the gains are modest and the recovery is uneven, the fact that state tax collections have risen, in aggregate, by 2.5 and 2.2 percent year-over-year for the past two reporting periods is a positive sign for the municipal market. Just as federal revenues for calendar year 2010 are expected to exceed revenues from 2009, state tax collections should also post annual gains in 2010, which is a movement in the right direction after the severe troughs in 2009.

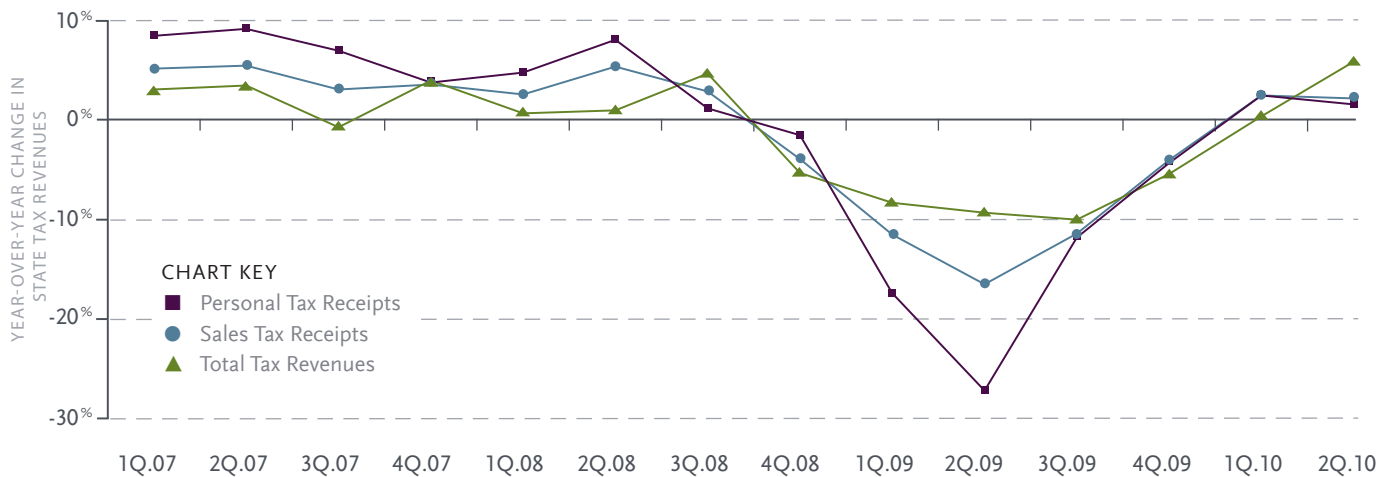
Municipalities address cyclical deficits by raising taxes and cutting spending. What generally happens during economic recovery is that state revenues often start rebounding just as spending cuts are being enacted. This helps municipal finances turn more quickly than one would anticipate. We believe credit quality is at its nadir right now. As the recovery continues to take hold, security prices in the municipal market should generally appreciate.

Markets discount asset prices based on the information that's available – mostly news and events. In the case of municipal bonds, there appears to be a preoccupation that state budgets will turn into the next black hole – U.S. states are often associated with troubled European sovereign credits. This is what has in part driven the historically high yields across the municipal bond market. The reality is that 30 of 47 reporting states experienced revenue growth in the second quarter of 2010. We believe this is the underpinning of improvement for state and local finances. However, it is also important to note that the recovery in tax receipts is taking place at disparate rates. At the risk of sounding like a broken record, the uneven recovery of state revenues is yet another reason why we believe opportunity in the municipal market exists for investors who are able to ignore headline risk and perform in-depth credit analysis on a security-by-security basis.

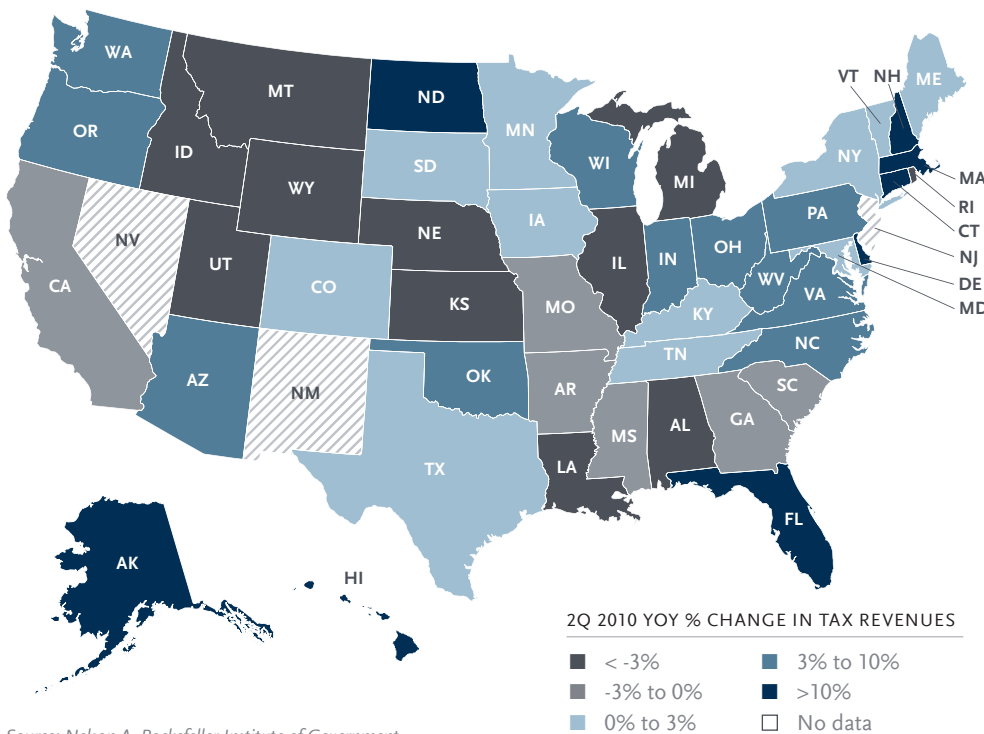
The change in the direction of state revenues is a strong signal for the beginning of a turnaround in credit quality. Security prices discount the future. We believe credit quality is at its nadir right now. As the recovery continues to take hold, security prices in the municipal market should generally appreciate.

TURNING THE CORNER – 2ND CONSECUTIVE QUARTER OF YEAR-OVER-YEAR GROWTH IN STATE TAX REVENUES

The revenue picture in 2010 has finally been turning positive for many states. After five consecutive quarters of year-over-year declines, the first two quarters of 2010 witnessed overall growth in total state tax collections.



Source: Nelson A. Rockefeller Institute of Government



TAX RECEIPTS ROSE IN 30 STATES IN THE SECOND QUARTER OF 2010

Although federal transfers have provided fiscal relief to states, growth in tax receipts is the first step on the road to sustained revenue recovery and financial health. After five consecutive quarters of revenue declines, preliminary reporting from the second quarter of 2010 showed consecutive quarters of revenue growth; however, the recovery is taking place at varying paces, with 30 of 47 states reporting revenue growth in the second quarter. In the end, the decline of state revenues highlights an operating crisis, not a debt crisis, as the majority of tax-supported municipal debt has a priority position to nearly all other expenses.

Source: Nelson A. Rockefeller Institute of Government

Security Selection and Credit Analysis

UNDERSTANDING THE REAL RISK IN UNFUNDED PENSION LIABILITIES

One of the largest looming problems for state governments in particular is unfunded pension liabilities. The numbers are staggering, especially if one adds in Other Post Employment Benefits (“OPEBs”), which typically include promised healthcare and life insurance costs.

The real impact of unfunded pension liabilities once again highlights the difference between the municipal market and corporate credit. In the world of corporate pensions, because a company can declare bankruptcy and go out of business, it makes sense that corporations should fund their pension liabilities 100 percent. However, a state cannot go out of business, so state pension funds could be viewed as existing to generate revenues to pay current retirees. Unfunded municipal pension liabilities therefore require less immediate contributions than in the corporate world.

For example, a restructuring to a state pension plan that is currently 80 to 85 percent funded (which would include quite a few states) could be worked out in 10 or 15 years with little impact to the state economy.

With that said, there are some states, such as Illinois, Massachusetts, and New Jersey, where the state pensions are more dramatically underfunded. In these instances, demographic analyses and political influences play a more prominent role in assessing the real impact of long-term pension liabilities on current credit evaluations.

The scenarios where investors have run into trouble in the municipal market are generally well-documented by the national media and include headline credits such as Vallejo and Harrisburg. The first and worst risk in municipal bond investing is the failure to perform thorough credit analysis. A lack of solid understanding of municipal market credit is a leading reason why spreads today are historically wide compared with corporate and sovereign debt securities.

While in-depth analysis is a prerequisite for all investment decisions, municipal finance poses a host of unconventional and complicated credit risks that are unique among fixed income opportunities. Many of these risks are difficult to quantify and are not readily reflected in credit ratings. This makes original credit work and careful security selection all the more paramount.

According to data from Moody’s Investor Services, nearly 85 percent of municipal securities hold an A rating or higher, compared with just 37 percent for the global corporate credit market. Despite the relative homogeneity of municipal bond ratings, the municipal market, like any other market, has a diverse spectrum of relative credit qualities. Similarly rated investment grade municipal bonds can face dissimilar risk profiles that are not always obvious. The municipal market inherently involves many unconventional measurements of risk, including demographic shifts, microeconomics, political risk, liquidity risk, and/or project risk, among other factors. In addition, the varying speeds of revenue recovery and disparate political outlooks among municipalities of similar credit ratings further underscores the need for an in-depth understanding of revenue stability, the regulatory environment, and tax policies.

Another layer of unique credit analysis that takes place in the municipal market is the differentiation between a municipality’s *willingness* and *ability* to pay its debt obligations under stressful circumstances. In the municipal market, the borrower often has the ability to increase its revenues to service its debt regardless of economic status. This is not true of corporations, where revenues generally decline during a severe recession regardless of the action taken by the company. In the case of municipalities, however, there is greater flexibility to increase revenue to make debt payments regardless of economic conditions. Determining both the willingness and the ability of a municipality to meet its debt obligations under various circumstances requires an understanding of social and political factors that are often as nebulous as they are market specific.

Reinforcing the need for credit work in the “new world” of investing is the fact that the market for municipal bond insurance essentially collapsed during the financial crisis. As much as 57 percent (or \$232 billion) of the municipal debt issued in 2007, was covered by insurance that provided investors with additional assurance of repayment. In 2010 through August, just 7 percent of new municipal debt issuances were insured to protect against default. Ironically, the losses at monoline insurance companies had virtually nothing to do with credit problems in the municipal bond market. The losses

were nearly entirely associated with insurers diversifying into structured credit products prior to the economic downturn – an area where they had limited underwriting experience relative to their core business of insuring municipal bonds.

Absent the insurance wraps, more emphasis now falls on the credit rating agencies and, of course, primary credit research. It should also be noted that, unlike structured products such as RMBS, CMBS, ABS, etc., the credit ratings for the municipal and corporate debt markets hold more water due to the size and scope of their historical track records. Municipal debt has a much longer credit history to draw upon than asset backed securities, for example. As the table on page 5 clearly shows, over the past 30 to 40 years of data, historical default rates are substantially lower for municipal bonds than corporate bonds. Still, ratings alone are not sufficient for analyzing opportunities in the municipal market.

We believe that for fixed income investors who can apply sound credit analysis to security selection and ongoing credit

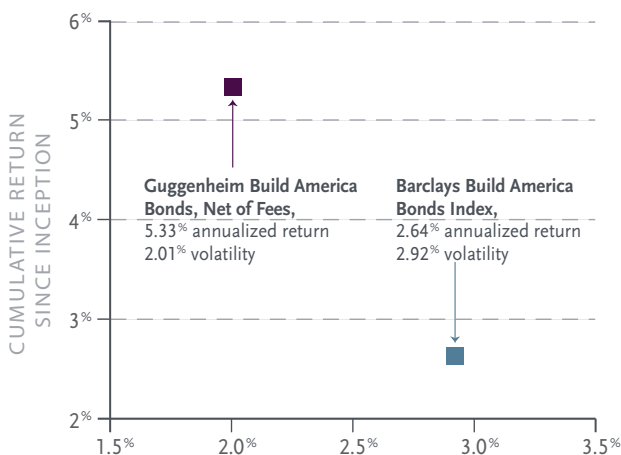
monitoring, the municipal market presents an opportunity to access attractive risk-adjusted returns while increasing credit quality and diversification.

In conclusion, here is a final thought on relative value: given the breadth of the historical data on defaults in both the municipal and corporate bond markets, and the fact that at each rating level the yields on municipal bonds are materially higher than those for corporate debt, investors can draw an important conclusion about relative value between municipal bonds and corporate debt. Even if default rates on municipal bonds were to rise appreciably to levels *equal* to similarly rated corporate bonds (which we do not believe will happen), the risk-adjusted returns would still be more attractive in the municipal market due to the wider spreads. This does not take into account the fact that recovery rates are significantly higher for municipal credits than for corporate bonds, which makes the opportunities in municipal finance even more attractive. □

IN-DEPTH CREDIT RESEARCH CAN UNLOCK VALUE FOR MUNICIPAL INVESTORS

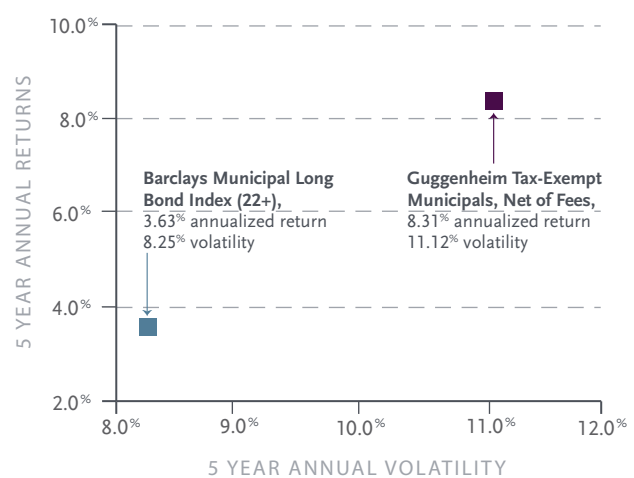
At Guggenheim Partners Asset Management, our Municipal Finance team understands that all municipal bonds are not created equal. We seek to identify issuers with strong management, prudent debt management policies, adequate debt capacity and demonstrated debt service coverage, and potential growth/price appreciation opportunity. Our team targets issuers with strong “hard asset” protection and evaluates assets and legal conditions under hypothetical recessionary conditions to determine credit quality and even potential recovery scenarios. An indication of the impact of careful security selection and ongoing credit analysis can be inferred from the historic performance data shown below.

BUILD AMERICA BONDS



Source: Guggenheim Partners Asset Management (“GPAM”), Barclays Capital; Performance for Build America Bonds excludes Qualified School Construction Bonds. Returns are shown net of advisory fees modeled at 1.00% annually. Return vs. Volatility is calculated from GPAM’s Municipal Build America Bonds historical return data since inception of the Barclays BABs Index (Oct 2009 – June 2010). Sector returns consist of securities purchased under a Build America Bond (taxable municipals) strategy and related derivatives, and such information is supplemental to the GIPS compliant presentation.

TAX-EXEMPT MUNICIPAL BONDS



Source: Guggenheim Partners Asset Management (“GPAM”), Barclays Capital; Returns are shown net of advisory fees modeled at 1.00 percent annually. Return vs. Volatility is calculated from 5 years of GPAM historical returns (July 2005 – June 2010). Sector returns consist of securities purchased under a tax-exempt municipal strategy and related derivatives, and such information is supplemental to the GIPS compliant presentation. This index is the Long Bond (22+) component of the Barclays Capital Municipal Bond Index – a rules-based, market-value-weighted index engineered for the long-term tax-exempt bond market.

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The illustrations are intended solely as tool to assist in consideration of various potential asset allocations for a client's account. Past performance of indices of asset classes does not represent actual returns or volatility of actual accounts or investment managers, and should not be viewed as indicative of future results.

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GUGGENHEIM PARTNERS ASSET MANAGEMENT, GP – FIXED INCOME COMPOSITE, ANNUAL DISCLOSURE PRESENTATION

Year End	Total Firm Assets (\$mm)	Composite Assets		Annual Performance Results			
		USD (\$mm)	No. of Accounts	Composite Gross	Composite Net	Citigroup LFP	Composite Dispersion
2009	39,131	32,354	8	11.90%	11.73%	3.22%	N.A.
2008	29,488	26,200	5	-3.37%	-3.51%	9.18%	N.A.
2007	26,844	25,762	5	5.81%	5.65%	7.32%	N.A.
2006	23,113	22,230	<5	5.52%	5.37%	3.69%	N.A.
2005	22,075	21,203	<5	4.45%	4.29%	3.80%	N.A.
2004	19,129	18,244	<5	7.50%	7.34%	6.60%	N.A.
2003	16,157	15,293	<5	7.10%	6.94%	5.06%	N.A.
2002	10,781	10,311	<5	11.27%	11.10%	12.52%	N.A.
2001	7,393	6,981	<5	7.22%	7.06%	8.17%	N.A.
2000	5,736	5,561	<5	10.79%	10.63%	13.67%	N.A.
1999	4,674	4,214	<5	0.11%	-0.04%	-3.97%	N.A.

N.A. - Information is not statistically meaningful due to an insufficient number of portfolios in the composite for the entire year.

The GIPS firm is defined as Guggenheim Partners Asset Management, which represents all the assets under Guggenheim Partners Advisory Company and Guggenheim Partners Asset Management, LLC (formerly Guggenheim Partners Asset Management, Inc.), wholly owned subsidiaries of Guggenheim Partners, LLC. In presentations prior to October 2007, the firm was comprised solely of Guggenheim Partners Advisory Company assets. The firm maintains a complete list and description of composites, which is available upon request.

Results are based on fully discretionary accounts under management, including those accounts no longer with the firm. Derivatives are used to hedge various risk components of the composite and may make up a material part of the composite strategy. Interest rate derivatives are used to hedge interest rate risk and credit default derivatives are used to hedge underlying credit risk. The use of leverage may be employed when appropriate market conditions exist, generally in the form of reverse repurchase agreements and securities lending. Inherent in any investment is the possibility of loss. Past performance is not indicative of future results.

The U.S. Dollar is the currency used to express performance. Returns are presented gross of management fees and include the reinvestment of all income. Actual returns will be reduced by investment advisory fees and other expenses that may be incurred in the management of the account. Returns are also presented net of management fees and reinvestment of dividends. Net of fees performance is calculated by deducting the highest fee of 0.15% from the monthly gross composite return. The collection of fees produces a compounding effect on the total rate of return net of management fees. As an example, the effect of investment management fees on the total value of a client's portfolio assuming (a) quarterly fee assessment, (b) \$1,000,000 investment, (c) portfolio return of 8% a year, and (d) 1.00% annual investment advisory fee would be \$10,416 in the first year, and cumulative effects of \$59,816 over five years and \$143,430 over ten years. Please refer to Guggenheim Partners Asset Management, LLC's Form ADV Part II for a complete description of its management fees. Additional information regarding policies for calculating and reporting returns is available upon request.

Investment management fees vary by client. The standard fee schedule for clients in the Guggenheim Partners – Fixed Income Composite is .15% on all assets.

The GP – Fixed Income Composite was created July 1, 2005. Guggenheim Partners Asset Management's compliance with the GIPS standards has been verified for the period January 1, 1999 through March 31, 2009 by Ashland Partners & Company LLP. In addition, a performance examination was conducted on the GP – Fixed Income Composite beginning January 1, 1999. A copy of the verification report is available upon request.