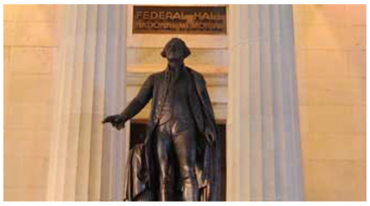
"Municipal Bonds For Individual Investors Since 1964"

Stoever Glass & Co

30 Wall Street, New York, NY10005

THE STOEVER GLASS MUNICIPAL BOND PORTFOLIO PLANNING KIT



The figures accurately reflect those available on the most recent date the Kit was constructed (March 11, 2011). Of course, the figures change daily, and certainly from month to month, however, the relationship between the figures remains relatively constant, as do the principles they represent. (You may or may not achieve the same results as those in the model portfolios).

AN INTRODUCTION TO THE PORTFOLIO PLANNING KIT

For over 50 years in the municipal bond business we have been convinced that buying bonds that best suit your investment goals is the most important thing to know. That's the only way professional buyers invest so we created the "Municipal Bond Portfolio Planning Kit" to show you how to establish your goals and what type of bonds best suit your goals. We think that what Garland Morse, retired CEO of GTE Sylvania said about the kit is exactly right, "In one hour, I learned more about municipals than I knew after ten years of buying them".

To be a successful investor you must preserve your wealth as well as enhance it. So what you should want is not just the highest yield but rather the best combination of yield, safety and liquidity - considering your personal circumstances. And to get that you must learn to establish investment goals that suit your personal profile and buy the bonds that best serve those goals. That's the only way professional investors buy bonds, and that is also the best way for you to invest.

We designed our portfolio planning kit specifically to teach investors how to buy bonds that are right for them. But in the process it has done even more. It's packed with valuable information, so read it carefully.

IDENTIFY YOUR GOALS

If there were one perfect tax-free investment, everyone would buy it. You could sit back and relax, knowing that your investment was producing the highest return, growing at the fastest rate, with instant liquidity and that both your principal and return were absolutely guaranteed. But these elements - current income, growth, liquidity and safety - work against each other with municipals, so there is no such thing as the tax-free investment that is all things to all people. In the real world the key to successful investing is finding the municipal bonds that give you the best combination of these elements - based upon your personal circumstances (age, income, future plans, your other assets, etc.).

BOND PRICING IS BASED ON STRENGTHS AND WEAKNESSES

A municipal bond does not exist in a vacuum, so each municipal bond must be priced competitively in relation to all of the others. Every bond has strong points and weak points but they must balance eachother out. If they didn't, some bonds would never sell. For example, if a bond has a low coupon, the yield to maturity will have to be higher to make it saleable. Bonds with higher coupons are saleable at higherprices. Longer bonds need higher returns to compensate for their increased vulnerability to market fluctuation. Short term bonds protect your principal much better against market risk, so investors are willing to take lower yields to get them.

What you want to do is learn how to select the mixture of coupon, maturity and yield that will produce the best results for you as an individual. And the model portfolios in this kit are designed to show you how to do that - clearly and efficiently. Take a look at the various model portfolios. There is a good chance that you will recognize among them a situation similar to your own. That is the one to study most carefully. The model may suit you perfectly just as it is. However, if you think certain changes may be preferable, turn to "How to Modify the Model Portfolios". That section shows you how to make adjustments and modifications to each of the model portfolios. You should finish our kit with a much better idea of the type of municipal bonds you should buy. And why.

But first of all, to learn how to choose from the many possible combinations of coupons, current yields, net yields and maturities available, it is essential that you begin by understanding the advantages and disadvantages of premium bonds, discount bonds, long term bonds and short term bonds.

MATURITY

It's very important to realize that with municipals, safety of principal can be as dependent upon maturity (market risk) as it is upon the bond's inherent quality. This is due to the fact that long term bonds are generally subject to greater fluctuations due to the uncertainty that longer maturities involve. And liquidity, when described to mean the opportunity that you will be able to sell at or near the price you paid, is also a function of maturity.

Longer bonds and unit trusts have higher returns than shorter bonds but they also usually fluctuate more in the market. Shorter bonds give you lower returns but more protection against market fluctuations than longer bonds.

Remember all long term municipals and long term bond funds have similar market risk - regardless of quality. So keep in mind that if you think you may want your money in five or ten years, you're taking a risk with the market whenever you buy long term bonds or long term bond funds.

That is not to say that no one should buy long term bonds or bond funds. They are right for some, but be sure you know why you want to buy them. We assure you that the highest yields aren't reason enough. They are right only when maximum current return is more important to you than preservation of principal and liquidity at or near the price you paid. Think it over. Is that what you really want?

DISCOUNT BONDS

Discount bonds are best if your regular income is high and you want your municipal bond portfolio to act as a savings/growth portfolio.

They can be what are commonly known in the business as zeros, which pay no periodic interest but grow from a deeply discounted price to par (100) at maturity or they may be coupon bonds selling at discounts.

The return on discount bonds is a combination of the semi-annual coupons over the life of the bond plus the annualized appreciation of the bond from its discounted price to face value or par at maturity.

In some cases, you will pay a capital gains tax on the appreciation of your principal when the bond comes due, but don't let that discourage you from buying this type of bond because they are usually priced to give higher annual yields than other bonds of the same maturity, even after you subtract the maximum capital gains tax.

The capital gains tax computation for municipal bonds is unique, because it is essentially based on your marginal tax rate. However, the computation includes a "De Minimus Rule" or safe harbor provision, which means that ¼ of 1% of your gain per year, is treated as capital gains. The result is a blended rate somewhere between your tax bracket and the capital gains rate. Taxes on the gains are not payable annually as they are for many other investments. With municipals you pay the gain only when it is realized. Many discount municipals are not subject to any gains taxes because they were originally issued at a discount and others may have greatly reduced levels of taxation for the same reason. Your Stoever Glass representative can help you identify the bonds that are subject to the capital gains taxes, and which discount bonds are totally or partially exempt from capital gains taxes.

One further point, with all discount bonds, the formula used to calculate the appreciation automatically compounds your interest at the rate of whatever the yield to maturity was on the date of purchase. So you do not lose the time value of your money. Visit our website for our free educational article: "Bond Arithmetic And The Theory Behind It."

The disadvantage with discounts is that they give less current return than par or premium bonds, but keep in mind that it is sometimes advantageous to sacrifice some current yield in return for a higher annualized yield at maturity.

PREMIUM BONDS

If you want your bond portfolio to serve as a source of additional spendable income, buy premium bonds. Don't be reluctant to pay above par for a bond. Remember when buying bonds you're buying a yield not a dollar price. Even though you're paying more than par, you are also receiving a higher coupon rate than the yield you bought. So in essence the premium is returned to you in coupon form. And a premium bond will almost always yield more to maturity than an identical par bond. That's because the word premium or the fact that you pay more than the bond's par value creates reluctance on the part of many investors. So to help overcome that resistance, premiums usually offer more yield than identical par bonds. And that creates an opportunity for the investor who takes the time to fully understand premiums.

The disadvantage with higher coupon bonds is that they are more likely to be called than other bonds if interest rates drop, forcing you to reinvest at the prevailing lower returns. When buying premium bonds always ask if the bonds are callable.

And if they are, what is the yield to the first call. Also find out if there are hidden calls from sinking funds or special redemptions. Stoever Glass always prices its bonds to the call that generates the lowest dollar price. Visit our website for our free educational article **"Calling The Calls On Municipal Bonds And How To Use Calls To Seek Higher Yields".**

QUALITY

For us, sound portfolio construction begins with good quality bonds. We have always preached that even among various "A" rated bonds, it is the type of bond you buy more than the rating that will determine the true quality of your portfolio.

We usually recommend the general obligations of states, counties and municipalities. These investments are secured by the taxing power of the issuer. We also recommend established revenue bonds, which are secured by stable revenues, derived from essential utilities such as water, sewer, and electric.

Recently created utilities do not have the same degree of security as those with an established history of earnings. And other revenue bonds such as those issued for housing developments, hospital and nursing home construction or industrial development usually do not have the uniform quality or marketability of general obligations and established utility revenue bonds, so we recommend them to individuals only on a highly selective basis.

We also feel that municipal bond insurance for general obligations or essential service revenues is over rated. That's because the security behind most general obligations or essential service bonds is actually stronger than the insurance companies. Even at the height of the great depression of the 1930s, very few general obligations were late on payments and almost 100% of that tiny figure, soon paid off in full. During those dire times many insurance companies went bankrupt and many more have gone bankrupt since. However, we agree that the extra layer of security might be comforting.

HOW MUCH IS TAX EXEMPT INCOME WORTH TO YOU?

It's often surprising to see just how much of an advantage you can get with tax-exempt bonds. Even for those in the 28% income tax bracket, tax-exempt bonds give you a very valuable yield advantage. The chart below compares tax-free yields with taxable returns for various tax brackets.

The exact taxable equivalent yield for any tax bracket can be found by subtracting your marginal tax bracket percentage from 100% and dividing it into the tax-free yield. Assuming an income tax bracket of 28%, let's compare a taxable yield of 7 % to a tax-free yield of 5 ½%. To see what 5½% is really worth, subtract 28% from 100% and divide (72%) into 5 ½%. The result (7.64%) proves the tax-free yield to be a better choice for individuals in the 28% income tax bracket and higher. Obviously, the higher your tax bracket, the more a tax-free yield is worth to you. The following chart shows the taxable equivalent yields for the various tax brackets.

FEDERAL TAX BRACKET	28%	31%	35%
TAX-EXAMPT YIELD (%)	TAXABLE EQUIVALENT YIELD (%)		
3.00%	4.17%	4.35%	4.62%
3.50%	4.86%	5.07%	5.38%
4.00%	5.50%	5.79%	6.15%
4.50%	6.25%	6.52%	6.92%
5.00%	6.94%	7.24%	7.69%
5.50%	7.64%	7.97%	8.46%
5.75%	7.99%	8.33%	8.85%
6.00%	8.33%	8.69%	9.23%

This chart does not show the additional benefits of exemption from local income and/or personal property taxes. And in most cases, in-state municipals are exempt from these taxes, too. These exemptions can be worth as much as an additional 1.3% to an individual in the 31% bracket, even after you deduct the local taxes from the Federal taxes.

Legal Caveat. There were the applicable tax brackets on March 11, 2011 when this kit was constructed. Since tax rates and tax brackets are always subject to change, be sure to consult your accountant and/or tax advisor with any questions you may have.

TAX RELATED TIPS FOR INCREASING NET YIELDS

It is important to note that the Tax Reform Act of 1986 created a category of "private purpose municipals" whose interest income must be added into the Alternative Minimum Tax computations. All municipals of this type must be specifically designated AMT bonds and none of the other municipals figure in the computation. In fact, relatively few municipals fall into this category.

Qualification for the AMT usually means you have a large amount of preferential deductions such as depreciation or that you live in a high tax state such as California, Massachusetts, Minnesota, or New York. Buying AMT municipals can be advantageous because municipals subject to the AMT usually add additional yield. Alternative Minimum Tax bonds might present an opportunity for some, but be careful because more people are affected by the AMT every year. So consult your accountant and/or tax adviser for more complete information about your personal tax circumstances.

Also keep in mind that out-of-state bonds can sometimes yield more than in-state bonds, even after paying state income taxes, especially if your state's taxes are relatively low. Occasionally, because of high supply, identically rated bonds from another state may out yield bonds of your state. So it's worth remembering that out-of-state bonds may outperform in-state bonds for many investors even after the state taxes.

Any Stoever Glass representative can assist you in determining the additional effects of state and local taxes, tell you which bonds are exempt from these taxes, and/or show you out-of-state bonds that may net you more tax-exempt income than bonds of your own state.

MUNICIPAL BOND INDEXING

To properly dissect the municipal market in terms of being able to get a meaningful understanding of the value and benefits of one type of municipal as opposed to another, it is necessary to have valid reference points from which to make comparisons. Fortunately there are such industry-wide reference points, which are used every day in the municipal bond business.

Most of the indexing in the municipal bond industry is compiled and published weekly by an independent professional publication: The Bond Buyer. The weekly averages are a composite average of the yields on "A" rated municipal bonds of various maturities issued during the week. These averages are the standard industry-wide guidelines used by dealers and professional buyers every day.

Using these averages is the best way to judge the value of the various types of municipal bonds, so we think they should be used by individual investors as well as by professionals.

To learn how to use the averages, keep tabs on this section on Municipal Bond indexing so you'll have it readily available as you study the dollars and cents results for each of the model portfolios. You'll be referring to the averages quite often as you review the portfolios.

The 10 and 20 year Bond Buyer Averages shown below are those published for the week the kit was constructed. The 5 and 15 year unweighted averages of new issues were published in the Bond Buyer during the same week. As you can see, allowing for maturity differences, they progress in sequence quite accurately.

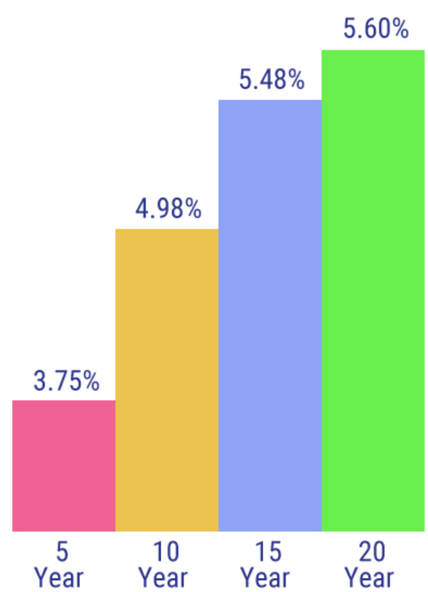
We selected the averages for the week the model portfolios in this kit were assembled. The prices of the bonds used in the various portfolios accurately reflect those of that week, and since all the bonds used in our portfolios are "A" rated or better by Moody's (the same or better than those used in the Bond Buyer's averages) they provide you with an easy way to make valid comparisons for yourself, exactly the way the professionals do.

The averages will vary from week to week and of course from year to year, but the relationship between maturity and yield remain approximately the same and so do the principals involved in the pricing of new issues as compared to the pricing of the older premium and/or discount bonds.

For the week these portfolios were constructed the averages were as follows:

WEEKLY MUNICIPAL YIELD AVERAGES

("A" RATED, NEW ISSUES)



(Source: The Bond Buyer)

PORTFOLIO # 1

A New York City vice president of a company that publishes school textbooks plans to retire next month when he reaches his 65nd birthday, but he will be retained by the company as a special consultant at $100,000 a year for the next ten years.This will give him a nice retirement income but to supplement this income he would like to invest the $500,000 he expects to receive from the sale of company stock in someincome producing securities.

Since the consultant's salary and other income will keep him in the 28% tax bracket, he and his wife decided to invest the $500,000 in tax-exempt securities.

They told us, however, that they were still undecided between bonds and shares in a bond fund. They were considering shares in both the "no-load" open-end funds and the older, more established municipal unit investment trusts, as possible alternatives to buying their municipal bonds separately. So they asked us to help them decide.

We agreed that people in their situation were possible candidates for one of the funds. Because they planned to use the $500,000 to produce the maximum spendable retirement income. And since they planned to leave the principal in their estate, they were not concerned with possible future market fluctuations, so they were in a position to benefit from the advantage of long term securities - higher current yield.

The advantage of long term bonds, or long term bond funds which are entirely made up of 25 to 30 year bonds, is that they give you a higher current return than shorter bonds. The disadvantage is that all long term securities fluctuate more widely in value when the market goes up or down, and that could cost you dearly if you have to sell when the market is off.

But they planned to leave the bonds in their estate. They don't plan to sell and whenever maximum current income is more important than possible negative fluctuation in your portfolio's value, long term securities are better for you.

But before you buy be sure that the higher yields of long term bonds are important enough to you to offset the increased market vulnerability to your principal. Be sure you know why you want long term bond funds. The people who don't take the time to sufficiently educate themselves seem to huddle to the funds as the easiest and seemingly most secure compromise solution. Not surprisingly, these are the people who take some of the biggest losses when rates go up and the market goes against them.

Some of the bonds we used in this portfolio were selling at premiums. But keep in mind that the very long term "A" rated bonds were yielding about 5.60% when this portfolio was constructed. (See Municipal Bond Indexing.) And none of the Lowensteins' bonds yield less than 5.60% to maturity, while the current yield of spendable dollars averages 5.75%. Don't be afraid to pay a premium, because while you pay a higher price than par, you also receive a higher coupon than the yield you bought. So in essence the premium is returned to you in the coupon.

Our chief concern in selecting a portfolio for these people was to provide them with a combination of quality and as much tax-free income as possible - income that they will be able to spend in their lifetimes. They worked hard all their lives, and now they want as much income as possible to enjoy. And long term, high coupon bonds will give them the maximum spendable tax-free dollars in their lifetime. Remember, however, that they didn't plan to spend the principal in their lifetime. The bonds will be left in their estate, so future market fluctuations that might affect their principal were not as important to them as getting the maximum current return on their money during their lifetime.

Be sure that maximum current return is more important to you than liquidity at or near what you paid before you buy long term bonds or long term bond funds.

PORTFOLIO # 2

A Texas doctor, has been practicing medicine for almost 25 years. He is 56 years old and has a reputation as one of the foremost specialists in his field. His income is very high, and with his reputation and ability he will be in a high tax bracket as long as he is working. But a man like this doctor must endure tremendous strain and constant pressure. So he has decided that nine more years will be enough, and he's doing some financial planning now. For years he has been investing through his retirement account, but that is able to absorb only a small portion of his income. He owns stocks and mutual funds, but for someone in his bracket, tax-exempt municipal bonds should definitely comprise a good portion of his portfolio. He decided to invest about $500,000 and asked us to help him decide what type of municipal bonds were best suited to his situation.

We gave him an investment plan that called for sacrificing some current income while he is still working, in order to obtain a higher annual yield at maturity, with growth of principal and maturities shortly after his planned retirement.

We recommended a discount bond portfolio because as long as he is working, his income will be very high, so he doesn't need the extra spending money now. For him a savings/growth type portfolio was more suitable. So we suggested that he forego the higher current income a premium or par bond would provide and buy the discount bonds which will give him a higher annual tax-free yield at maturity - mostly through tax free growth of principal. We arranged to have him realize that growth in a few lump sum payments soon after his retirement.

At the time this portfolio was constructed the Bond Buyers' Weekly Average for 10 year "A" rated bonds was 4.98%.This means that the available alternative, assuming bonds of similar maturities, was a portfolio of par bonds yielding about 4.98%.(See The Bond Buyer Index on page 7) So if he had purchased $500,000 worth of par bonds due in 10 years averaging 4.98% return, his total income at the end of ten years would have been $249,000. Add this income to his original investment of $500,000 and that totals $749,000 at retirement. With our plan, his original investment of $499,778.85 grew to $574,944,71 (even after deducting the gains tax) which when added to total coupon income of $189,945.00 (Avg. Coup. of 3.15% x Par Amt. $600,000.00 x Avg Life 10.05 years) totals $764,889.71 at retirement.

By using discount bonds in this plan, he ended up with $15,889.71 ($764,889.71 - $749,000.00) more tax free dollars than he would have had if he purchased par bonds similar maturities.

Of equal importance to the doctor is the fact that by purchasing bonds that mature at the time he plans to retire, he knows that market fluctuations will not affect his portfolio value when he actually needs the money.

In other words, he won't be put in the position of having to sell some longer term bonds when the market might be off.

Compare the average net annual yield on this portfolio to the 20 year The Bond Buyer Index. This portfolio is only 10.05 years long, but the net yield (5.17%) is fairly close to the 20 year averages (5.60%).Do you think the difference (.43%) is worth venturing 10 years longer? We certainly do not think it's worth the extra risk in market vulnerability, especially for someone like Dr. Pinella who knows exactly when he will want the money.

When constructing this portfolio, we put some zero coupon bonds into the mix. Zeros are the ultimate discount bond because they do not pay any periodic interest. The entire return is realized in the appreciation of your principal from the discounted price at the time of purchase to the bond's face value at maturity.

The big advantages of zeros are that they require the lowest possible initial investment, and they usually have a higher annualized yield than identical current coupon par bonds. And since zeros are originally issued at a discounted price, the appreciation is not subject to capital gains tax.

The formula used for computing the return also automatically compounds your return. Incidentally that is true for all discount bonds. The portion of return you receive in the form of appreciation of principal is always locked in and compounded at the original yield to maturity rate.

Discount bonds don't offer maximum current yields, but as you can see, they are priced to more than compensate you for that. They do so by giving you the highest annual return - mostly in the form of growth to your principal, and that makes them much more beneficial than higher coupon bonds if a savings/growth type portfolio suits you best - as it will for high income earners with circumstances similar to this example.

Remember, no tax exempt bond or bond fund offers an abundance of every element - yield to maturity, current return, safety (primarily a market risk and therefore a function of maturity), and liquidity at or near the price you paid (also a function of maturity). But they are priced in a free and competitive market to compete with one another -each by offering an abundance of some of those elements and less of the others. Pick out the elements most important to you, because finding a bargain in the market means finding a bond that will give you the most for your money - a bond with more of the elements that best help you accomplish your investment goals.

Know what your goals are and buy the right bonds for them.
(This was a Texas resident, where there is no state income tax, therefore we were free to select bonds from the entire country to obtain the highest yields. If you are a resident of one of the higher tax states, you will probably find it more advantageous to buy bonds within your state to get the double exemption.)

PORTFOLIO # 3

A Floridian entrepreneur is the president and the majority owner of a metal ore refining company.Recently, he decided to expand and diversify into related fields that would complement his refining business and help reduce risk. So he acquired a metal casting business and then a manufacturer of metal garden furniture. Later, he and two other businessmen invested in the development of a shopping center. He still owns his original 40% of the shopping center so he earns a good rental income and thedepreciation is deductible from income taxes. He is also a partner with his brother-in-law in a thriving restaurant business located in the shopping center. He owns stocks, bonds and real estate. He takes real estate depreciation off his taxes, but his tax bracket is still so high that any investment income he earns is taxed at the rate of 39.6% by the Federal Government.

He has a knack for business. He anticipates, he adapts and he can evaluate a business opportunity when it comes along. Who knows what he'll be doing next? He doesn't know himself, but he does know that he won't be able to resist a good deal if he sees one. Still he doesn't want any more of his excess money sitting around in tax-free money market funds while he waits for a good opportunity to turn up. So he wanted to hedge a little --- go a little longer to get more yield but still have a portfolio that could act as a contingency or back-up reserve in the event that an unusual business opportunity required more money than he kept in the money market funds.

He asked us to help him achieve his goal as effectively as possible, we suggested short term, pre-refunded municipal bonds. These are bonds that were originally issued as much longer term bonds but have since been called in advance (pre-refunded) and now have both a much shorter maturity and the full faith and credit of the United States Government solidly behind them. All of these pre-refunded bonds that ask to be re-rated by the rating agencies automatically receive a Aaa rating from Moody's. (Many issuers do not ask to have these older bonds re-rated because of the expense involved, but the security is still the same - the ability of the United States Government to meet its obligations.) These bonds give him a second tier of highly liquid reserves right behind his money market funds. But the reason for using pre-refunded bonds goes deeper. These bonds are an exceptional value considering the benefits they confer. These pre-refunded municipals are 100% backed by the U.S. Government, they have short term maturities and they are relatively well priced, often offering the highest short term tax-free yields considering the quality.

There are two reasons why pre-refunded municipals are such bargains. First, most investors don't take the time to understand them, and second, they usually sell at high premiums. But don't let that scare you off, because a premium bond will almost always yield more than an identical par bond. That's because the word premium or the fact that you pay more than the bond's par value often creates the wrong impression and therefore a reluctance on the part of many investors. To help overcome that resistance, premiums offer more yield than the no-fuss-no-muss par bonds. And that creates an opportunity for the investor who takes the time to fully understand premiums.

Using Aaa quality pre-refunded bonds we were able to get him a return of 3.27% tax free with an average maturity of only 2.26 years. And by using high grade pre-refunded bonds and staggering maturities, we were able to maintain a degree of liquidity that was certainly more than adequate for his second-tier of reserves.

Had he known exactly when he would need his money we would have sold him bonds to mature on that date. But the key factor in his case is that he's not sure when he will need his funds. He's not sure how much of his money he might need. He's not even sure he'll need it at all.Because of this and because he already has liquidity with his money market account, we thought it advisable to stagger his maturities and stretch them out a little to increase his tax-free return and give him what amounts to a revolving fund. If he doesn't need the funds, all he has to do is take the money from the shortest bond when it comes due and reinvest in a similar pre-refunded bond which matures in two or three years.

His portfolio never changes in quality, approximate maturity, or liquidity and the average yield is usually higher than other current short term tax-exempt bonds.

We were careful to get bonds for him in preference to short term municipal notes. Bonds are more secure, because they must be funded in the budget. Notes are payable from anticipated sources, not funded in the budget.

Remember well the difference in the treatment of New York City notes and New York City bonds in the mid 1970's. A moratorium was declared and payment on notes was held up for over a year, while market values dropped to the low 60's. Yet in spite of all the publicity, not one New York City bond was ever one day overdue in the payment of interest or principal. In essence the treatment of Cleveland notes and bonds was almost identical. The notes were in default for almost two years, while the bonds were never a day late in payments. More recently, when Orange Co., California experienced its highly publicized, self-inflicted financial woes, the problem was solved by extending the notes while all of its bonds were paid on time.

And for someone as sophisticated as him, buying long term open-end funds thinking he would sell them just before interest rates go up was never a consideration. He knows that even the professionals can't predict exactly when rates will go up.

He knew he wanted short term bonds because only they give him both maximum liquidity and the most assurance of keeping his original principal intact if he suddenly needs his money for something else.

HOW TO MODIFY THE PORTFOLIOS

Each of the portfolios can be adjusted or modified to suit your preferences. To see what we mean, look them over and select the model that offers the type of portfolio that appears to come closest to matching your financial goals.

Your circumstances may be different, but if your primary concern is maximum current income, then look closely at Portfolio # 1. We pointed out that they did not care if their principal came due in their lifetime. They will be leaving the bonds to their heirs, so they are interested in maximizing their current tax-free income more than anything else.

If you want high current income but, unlike them, you would ultimately like to spend your principal, buy bonds that mature when you expect to need your principal.

The yield to maturity will be lower if the bonds are shorter, but if you buy bonds that mature when you know you'll want the money, you will reduce the problem of market fluctuation, and that could be well worth the lower yields.

Example A:

Moody's Rating	Par Amount	Security	Coupon Rate	Maturity	Yield to Maturity	Current Yield	Cost
Aa1	$25,000	Lincoln, MI S/D	7.00%	6 yrs 9 mos	4.75%	6.20%	$28,197.00
Aa3	$25,000	Edwardsburg, MI FSA Ins	6.750%	7 yrs	4.80%	6.04%	$27,933.00
Aaa	$25,000	Oakland Co., MI	7.00%	7 yrs 5 mos	4.80%	6.16%	$28,381.00
Aa3	$25,000	Breitung, MI FSA Ins	6.750%	7 yrs 8 mos	4.80%	6.01%	$28,081.00
					4.77%	6.10%	

Average Current Yield – 6.10% | Average Yield to Maturity – 4.77% | Average Life – 7 yrs. 2 mo.

Notice that with the 7 year, 2 month portfolio used in Example A, the current yield of 6.10% is much higher than the Bond Buyers' unweighted index for ten year "A" rated bonds which was at 4.98% at the time. And your overall yield to maturity of 4.77% is right in line with the new issue averages for bonds in the seven-year range. The point being that when shortening up maturities it is possible to maintain a high current yield - even higher than that which is available from longer par bonds but the yield to maturity keeps decreasing as you buy shorter and shorter bonds.

Nonetheless, when you buy a bond that you will hold until maturity you know exactly what your yield will be.If you buy longer bonds or one of the long term bond funds, knowing that you will probably want to spend your principal before maturity, who knows what the market price for your holdings will be when you want to sell?

For investors who want the high current income that premium bonds give you, there is a fairly common type of bond that provides some extra yield for investors who find them suitable. They're callable premium bonds, which are priced to give a yield to the "call date" which is higher than comparable bonds maturing on that date. And since callable bonds are always priced to the call date that produces the cheapest dollar price to the buyer, the yield to maturity is always much higher if the bond isn't called. They're commonly referred to as "kicker bonds" because the yield to the call kicks up to a much higher yield to maturity.The disadvantage is that the bonds can be called on you, and although they still yield more than they would if they matured on that date, they are not suitable for people who want their bonds to mature on specific dates. However, for investors who are satisfied with a maturity range rather than specific maturities, kicker bonds represent some of the best values in the bond market. Because it is possible to find bonds which have the call date and the maturity fairly close together - five or six years apart for example. So they're ideal for investors who like current income bonds in the short to intermediate maturity range - the five to fifteen year range or so.

If some of your bonds are called you still have a better yield than you could have purchased with the same maturities as your call date. But it is unlikely that all of the bonds in a portfolio of this type will be called, and whenever that happens your yield automatically kicks up. The net result will be a portfolio of higher yields - slightly higher than comparable maturities for those that are called and a much higher yield to maturity than non-callable bonds of the same maturity.

The following is a perfect example of a kicker bond:

Example B:

Moody's Rating	Par Amount	Security	Coupon Rate	Maturity and Call	Yield to Call	Yield to Maturity	Cost
Aa	$10,000	Phoenix,AZ	6.750%	Mat-12 yrs Call- 5 yrs	5.00%	5.68%	$10,916.00

When buying long term bonds it is also possible to get a fairly high current return with a discount bond. Because the coupon is a fixed percentage of face value and if you pay less than face value, that fixed coupon becomes a greater percentage of the amount invested. Usually the longer the bond, the deeper the discount, and the deeper the discount the more that fixed coupon is worth in current return.

Example C shows a case in point.

Example C:

Moody's Rating	Par Amount	Security	Coupon Rate	Maturity	Yield to Maturity	Current Yield	Cost
Aa2	$100,000	Seattle, WA. Water Rev.	5.00%	27 yrs 2 mos	5.80%	5.61%	$89,124.00

Long term discount bonds of this type are very useful for matched tax-loss trading if the market has dropped since you purchased some of your bond holdings.Because they are perfect vehicles for establishing paper losses that can be deducted from regular income and/or capital gains.

For more about "tax trading", visit our website for our free educational article: "How to Reduce Your Taxes By Trading Municipals". It will point out the advantages of tax trading, warn you of potential mistakes, give examples of different types of beneficial trades, and fairly present the transaction costs involved.

If you can afford to forego some current income in return for a higher annual yield at maturity you are like Portfolio #2.

Like the doctor, many buyers are primarily concerned with appreciation of capital and a higher annual return at maturity. But maybe you prefer a little higher current return. To get it, all you have to do is buy discount bonds with higher coupons. Remember though, if you keep buying discount bonds with higher and higher coupons, the ultimate net yield at maturity will drop. Compare the two discount bonds in example D to see the effect that the coupon rate has on the yield to maturity, net annual yield, and the current yield.

Example D:

Moody's Rating	Par Amount	Security	Coupon Rate	Maturity	Yield to Maturity	Net Yield After Gains Tax	Current Yield	Cost
A	$10,000	Portsmouth,Ohio	3 ¼%	8 yrs 1 mos	5.00%	4.68%	3.67%	$8,849.30
A	$10,000	Portsmouth,Ohio	4 ½%	8 yrs 1 mos	4.50%	4.58%	4.53%	$9,933.00

On the first bond, the current yield, payable every six months, is 3.67% and on the second it is 4.53%. But the net yield or the total annual tax-free return on your investment is 4.68% with the 3¼% coupon bond compared to 4.58% with the 4 ½% coupon bond. We can help you decide upon the right balance.

With the discount type bonds, longer maturities will lower the cost of the bond, and increase both the current yield and the net yield.

Example E shows the same bond but first with an 8 year maturity and then with an 18 year maturity.

Example E:

Moody's Rating	Par Amount	Security	Coupon Rate	Maturity	Yield to Maturity	Net Yield After Gains Tax	Current Yield	Cost
Aaa	$25,000	Evanston,Illinois	4 ¼%	8 yrs	5.00%	4.86%	4.46%	$23,820.00
Aaa	$25,000	Evanston,Illinois	4 ¼%	18 yrs	5.75%	5.59%	5.09%	$20,875.00

With longer bonds you can get higher returns but remember that longer bonds will be more vulnerable to market fluctuation.

For someone whose main concern is liquidity, Portfolio #3 is the one to review. This investor didn't know exactly when he would need his money, or whether he would need it at all. If you know when you will need your money, you can eliminate the question of liquidity entirely by purchasing bonds that mature on that date.

For short term bonds we often recommend discount bonds because they can give you a higher return at maturity, and with short maturities you don't wait long to realize the gain.

Refer to Example F which compares two bonds identical in all respects except that one is a discount and one is selling at par.

Example F:

Moody's Rating	Par Amount	Security	Coupon Rate	Maturity	Yield to Maturity	Net Yield After Gains Tax	Cost
A	$50,000	Shreveport,La.	3.40%	1 yrs 9 mos	3.40%	3.40%	$50,000.00
A	$50,000	Shreveport,La.	3.00%	1 yrs 9 mos	4.00%	3.70%	$49,190.00

With the discount bond the net tax-exempt return was 3.70% compared to 3.40% on the par bond.

We used the applicable De Minimus Rule to compute the net yield after the gains tax. However, it is important to note that if you have equivalent capital losses or capital loss carry forwards, deep discount bonds that mature in the years your capital losses impact you, will be totally tax free. In example F the net tax-free yield on the 3% bond would then become 4.00%.

There is another type of discount bond, the ultimate discount bond - the zero coupon bond. Zeros are issued at very deep discounts, so the original discount is not subject to capital gains tax. They pay no current income, but your return is automatically locked in and compounded at the rate of the original yield to maturity.

Investors use them to finance college educations and other anticipated future expenditures because they require relatively little initial outlay and provide rapid growth.

Example G is a zero coupon offering.

Example G:

Moody's Rating	Par Amount	Security	Coupon Rate	Maturity	Yield to Maturity	Net Yield	Cost
Aa	$100,000	Shelby Co.,Tenn	0%	17 yrs	5.80%	5.80%	$37,900.00

There is a small sector of the municipal bond market that when coupled with the proper strategy and sufficient expertise can often net you much higher tax-free returns. They're called "sinking fund bonds."

Common to many long term revenue bonds, sinking funds require that the issuer begin to retire bonds prior to maturity. In this way sinkers are a little like call features, except that calls are at the option of the issuer, while sinkers follow a mandatory retirement schedule. The amount of bonds to be sunk each year is specified at the time the bond is issued and must be carefully adhered to. These bonds must be sunk at par (100).

And since we know the final maturity, the number of bonds originally issued and the mandatory sinking fund schedule, we can also determine the average life of the issue. So bonds of this type can be priced to a predictable average life and since relatively few dealers specialize in sinker bonds, they always yield much more to the average life than any other bonds in the same maturity range.

There is one catch, however. Investors who buy bonds priced to the average life must invest in a quantity that is large enough to make the "average life" valid. Because sinking funds are done by random lot, so if you have ten or twenty bonds out of a $300,000,000 issue you could be unlucky and have the majority of your bonds sunk early.

That could result in a loss of principal because sinking fund bonds which are priced to the average life, usually have negative yields to the first few sinking fund dates. So the larger the amount of a sinking fund bond you can buy, the more assurance you have of approximating the average life, and with it 50 to 100 extra basis points in yield.

A look at Example H should help clarify this investment strategy:

Example H:

Moody's Rating	Par Amount	Security	Coupon Rate	Maturity	Next Sinker	Ave Life	Yield to Ave Life
Aaa	$200,000	CT Hlth & Ed (ETM)	7.00%	11 yrs 11 mos	11 mos	6 yrs 5 mos	5.38%

If you have a combination of goals, you might want to divide your investment into various combinations of Portfolios 1, 2 and 3. An investor in a high tax bracket with $500,000 to invest might decide to place $100,000 in short bonds (Portfolio # 3) to give themselves maximum liquidity, $200,000 in discount bonds (Portfolio # 2) to help finance the college education of two children, and $200,000 in longer term high current income bonds (Portfolio # 1) to establish a flow of good regular income. Choose bonds and combinations that suit your objectives. That's how the professionals do it.

(Please visit www.stoeverglass.com for Risk Factors.)