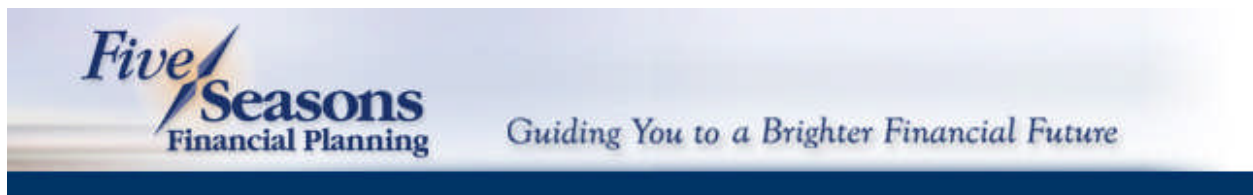


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Seasonal Musings

November 2007

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Hi Paul,

Welcome to another issue of "Seasonal Musings", the online newsletter from Five Seasons Financial Planning LLC (FSFP). In this issue, we'll be discussing developments in the Municipal bond market and tax planning ideas for year-end. As usual, if there are financial planning or investment topics you'd like us to cover in future issues, please drop us a line.

Municipal Mediocrity

Recent Underperformance in the Muni Bond Market

The municipal bond market has been an unexpectedly poor performer so far this year (unexpected to me, anyway). In the flight to quality that we have been experiencing in the past few months, we would expect higher credit quality bonds to outperform those of lesser quality.

This is a sweeping statement, but the average municipal bond fund tends to contain higher credit quality issues than the average taxable bond fund. As an indication of this, the Vanguard Intermediate-Term Tax-Exempt Fund is 90% AA and AAA credits, whereas almost half of the taxable Vanguard Intermediate-Term Investment-Grade Fund is rated below AA.

Meanwhile, the Vanguard taxable fund has generated year-to date returns more than double those of its tax-free counterpart. (Funds specializing in Treasury and

Inflation-protected securities have led the charge this year.) So why have muni funds been laggards this year despite their high credit quality?

A large part of the answer has to do with the way in which many municipal bond issues attain such high credit ratings. Essentially, the issuers of these bonds pay third-party bond insurers to bless the bonds with their credit ratings. Unfortunately, some of these third-party bond insurers also insure some of the nastier subprime mortgage-related debt. Consequently, the credit ratings of these bond insurers themselves, and to some extent the concept of third party insurance in the muni market, have been called into question.

To make matters worse, the municipal bond market tends to be a market more influenced by the average Joe and Jane on the street than the taxable market, which tends to be dominated by institutions. Issue sizes are smaller in the muni market, and with less liquidity, prices can be swayed by emotion more easily, especially in the short-term.

One way to get a sense of the relative attraction of the municipal bond market is to compare the yield on a basket of AAA-rated munis to a Treasury bond with the same maturity. As of Friday's close, you could find 10- year AAA-rated municipal bonds with yields well over 90% of the yield on the 10-year Treasury bond. For longer-term investors in higher tax brackets, this seems like Christmas come early to me.

Mutual Fund Moves

Year-End Tax Planning

Investors in actively managed stock funds may well find a lump of coal in their Christmas stockings this year. Taxable capital gains distributions to fundholders are expected to be near record levels thanks to the 5-year bull market and recent volatility. Distributions in excess of 10% of a stock fund's net asset value will be common.



What to do? Many mutual fund companies publish preliminary estimates of their year-end distributions on their websites or otherwise make them available to shareholders. If you sell your shares before the "ex- dividend" date, you avoid the distribution. However, this should not be the only consideration in determining whether you should pursue this strategy.

Nonetheless, you may also be able to simultaneously

harvest capital losses on mutual fund shares bought earlier this year for example. Please be sure to: (1) identify the tax lot you want sold if you've made a number of purchases through the years, and (2) abide by the wash-sale rules. And be sure to consult a tax professional for additional input. If done right, you may be able to use this market weakness to turn that lump of coal into a lower tax bill.

Happy Thanksgiving !!!

Five Seasons Financial Planning LLC is a Fee-Only financial planning and investment advisory firm registered with the state of Utah. Five Seasons offers financial planning services on an hourly basis, as well as discretionary investment management. To view past issues of "Seasonal Musings", click [here](#).

One of the benefits of working with a Fee-Only investment advisory firm is full disclosure. To receive a copy of our Form ADV, which details a variety of information about Five Seasons, or our Privacy Policy, please use the contact information below.

Best wishes,

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