

MUNICIPAL BOND MARKET NOTE

JANNEY FIXED INCOME STRATEGY

August 12, 2011



State tax revenues continued to improve in 1Q2011 but other indicators have remained stagnant.

We believe the last three years have illustrated that state governments are very resilient credits and possess a high degree of financial flexibility and autonomy.

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State Fiscal Health Scorecard Update

- Concerns about recent rating agency alerts and effects from the Budget Control Act (BCA) of 2011 are alleviated by states' financial flexibility and sovereign power to cut spending and increase revenues, in our opinion.
- We do not expect the BCA to negatively affect state credit quality in the near term based on what the market knows to date, but there is some medium to long term uncertainty. We are taking recent rating agency notices with a "grain of salt."
- If the last three years have illustrated anything it is that state governments are very resilient credits and possess a high degree of financial flexibility and autonomy.
- We recommend a prudent course of action and urge investors to patiently monitor the outcome of deficit reduction negotiations and to not overreact to rating agency assumptions.
- State tax revenues were 9.3% higher in 1Q2011 (YoY), a fifth straight quarter of positive results. Tax supported debt is slightly higher while mortgage and unemployment indicators remain near unchanged since our April 2011 update.

Unprecedented Economic and Political Times

In recent years the market has witnessed an unprecedented number of negative rating actions, some warranted, against state credits. Depleted reserves, a reliance on one-time budget measures, lower revenues, and rising pension liabilities have, and to some degree, still stress state credits. Over the last month rating agencies have been focusing on states' exposure to the federal government because of scheduled and anticipated adjustments to the federal budget. Much has also been made about recent rating agencies' evaluations. While ratings are often good general indicators we have not agreed with some of the rating agencies' recent opinions and actions.

This is uncharted territory from an economic stand-point for the world financial system and politically for the country's constitutional republic. Unfortunately, the near term economic and political climate is likely to become even more unpredictable. We recommend investors monitor deficit reduction negotiations and not overreact to rating agency assumptions. State governments' ability and willingness to pay debt service remains strong and we believe they will be able to adjust as needed.

Potential Credit Consequences from the Budget Control Act of 2011 are Uncertain

Recent rating agency and investor responses have varied in response to the Aug 2 debt ceiling compromise and BCA. Known deficit reductions will take the form of discretionary spending caps and the first phase amounts to about \$917 billion between 2012 and 2021. The greatest savings is back-loaded, minimizing near term effects. In addition, a proposal of at least \$1.2 trillion of additional adjustments is due from the BCA's Joint Select Committee on Deficit Reduction at the end of November. In the near term we do not think these budget alterations will be significant enough to negatively affect state credit profiles. However, we still need more information about where adjustments will be made to have a clearer picture about what effect they might have on municipals in general and to states specifically.

First Phase of BCA Deficit Reductions

2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	Total
-\$21	-\$42	-\$59	-\$75	-\$87	-\$99	-\$112	-\$126	-\$141	-\$156	-\$917

Source: Congressional Budget Office Aug. 2011 and Janney FIS. \$ in bill.

Recent History Shows States are Very Resilient Credits

We believe the last three years have illustrated that state governments are very resilient credits. While some states are statistically more exposed to the federal government we believe ultimately states possess levers, in the form of controls over their budgets, and credits will not significantly deteriorate.

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Janney State Fiscal Health Scorecard

State	Bond Ratings	Federal Aid as a % of Total Revenues	Medicaid as % of Total Expenditures	% Change in Tax Collections	Net Tax-Supported Debt as % of GSDP	State Pension Funding %	Mort Forec. "Seriously Delinquent"	Unemploy. Rate
Total/Average		29%	21%	9.3%	4.48%	78%	8.1%	9.2%
Alabama	Aa1AA/AA+	33%	20%	0.0%	4.76%	74%	5.7%	9.9%
Alaska	Aaa/AA+/AA+	14%	12%	16.7%	8.88%	61%	2.2%	7.5%
Arizona	Aa3/AA-/NR	32%	28%	14.0%	1.96%	78%	9.0%	9.3%
Arkansas	Aa1/AA/NR	31%	21%	7.2%	3.95%	78%	5.1%	8.1%
California	A1/A-/A-	25%	22%	5.7%	5.08%	81%	8.8%	11.8%
Colorado	NR/AA/NR	25%	16%	13.4%	4.03%	69%	4.5%	8.5%
Connecticut	Aa2/AA/AA	20%	19%	11.2%	10.80%	62%	7.7%	9.1%
Delaware	Aaa/AAA/AAA	20%	14%	4.8%	6.35%	94%	7.2%	8.0%
Florida	Aa1/AAA/AAA	29%	28%	4.2%	3.93%	84%	19.0%	10.6%
Georgia	Aaa/AAA/AAA	35%	20%	7.5%	2.79%	87%	8.1%	9.9%
Hawaii	Aa2/AA/AA+	22%	13%	-10.1%	10.30%	69%	7.2%	6.0%
Idaho	Aa1/AA+/AA	29%	21%	22.7%	3.03%	74%	5.7%	9.4%
Illinois	A1/A+/A	26%	33%	13.7%	3.97%	51%	10.5%	9.2%
Indiana	Aaa/AAA/AA+	28%	23%	9.9%	1.92%	67%	8.3%	8.3%
Iowa	Aaa/AAA/AAA	29%	18%	8.7%	2.24%	81%	4.8%	6.0%
Kansas	Aa1/AA+/NR	26%	17%	7.1%	2.78%	64%	4.8%	6.6%
Kentucky	Aa2/AA-/AA	32%	22%	5.1%	4.64%	58%	6.6%	9.6%
Louisiana	Aa2/AA/AA	47%	22%	9.8%	3.77%	60%	7.2%	7.8%
Maine	Aa2/AA/AA+	32%	29%	9.7%	10.14%	73%	8.3%	7.8%
Maryland	Aaa/AAA/AAA	25%	20%	8.0%	3.20%	65%	8.3%	7.0%
Massachusetts	Aa1/AA/AA+	23%	18%	6.7%	8.65%	68%	6.9%	7.6%
Michigan	Aa2/AA-/AA-	27%	25%	20.9%	6.03%	79%	7.9%	10.5%
Minnesota	Aa1/AAA/AAA	24%	22%	10.4%	6.87%	77%	5.0%	6.7%
Mississippi	Aa2/AA/AA+	46%	22%	7.3%	4.55%	67%	8.0%	10.3%
Missouri	Aaa/AAA/AAA	34%	33%	7.2%	1.98%	79%	4.9%	8.8%
Montana	Aa1/AA/AA+	35%	15%	5.5%	1.55%	74%	3.5%	7.5%
Nebraska	Aa2/AA+/NR	30%	17%	9.5%	0.05%	88%	3.3%	4.1%
Nevada	Aa2/AA/AA+	18%	17%	4.1%	2.44%	72%	16.0%	12.4%
New Hampshire	Aa1/AA/AA+	28%	25%	1.7%	3.75%	58%	5.2%	4.9%
New Jersey	Aa3/AA-/AA	21%	21%	8.1%	7.81%	66%	11.2%	9.5%
New Mexico	Aaa/AA+/NR	31%	23%	14.9%	5.37%	76%	5.9%	6.8%
New York	Aa2/AA/AA	30%	28%	12.3%	5.61%	101%	9.1%	8.0%
North Carolina	Aaa/AAA/AAA	30%	37%	2.7%	1.80%	97%	5.9%	9.9%
North Dakota	Aa1/AA+/NR	26%	14%	46.0%	4.26%	81%	1.8%	3.2%
Ohio	Aa1/AA+/AA+	30%	22%	21.0%	3.44%	66%	8.7%	8.8%
Oklahoma	Aa2/AA+/AA+	31%	20%	10.5%	1.38%	57%	5.8%	5.3%
Oregon	Aa1/AA+/AA+	29%	14%	16.2%	9.28%	86%	6.0%	9.4%
Pennsylvania	Aa1/AA/AA+	26%	28%	11.6%	3.11%	81%	6.3%	7.6%
Rhode Island	Aa2/AA/AA	30%	24%	4.3%	7.09%	59%	8.5%	10.8%
South Carolina	Aaa/AA+/AAA	32%	22%	2.2%	2.75%	69%	7.2%	10.5%
South Dakota	A1/AA+/AA	36%	23%	10.3%	1.30%	92%	2.9%	4.8%
Tennessee	Aaa/AA+/AAA	33%	26%	7.4%	2.26%	90%	6.4%	9.8%
Texas	Aaa/AA+/AAA	30%	8%	8.8%	1.66%	84%	4.7%	8.2%
Utah	Aaa/AAA/AAA	25%	14%	8.8%	6.86%	86%	6.0%	7.4%
Vermont	Aaa/AA+/AAA	29%	21%	13.7%	5.32%	73%	5.1%	5.5%
Virginia	Aaa/AAA/AAA	19%	16%	14.7%	2.70%	80%	4.4%	6.0%
Washington	Aa1/AA+/AA+	25%	23%	5.9%	6.82%	99%	6.4%	9.2%
West Virginia	Aa1/AA/AA	30%	13%	13.7%	6.15%	56%	4.7%	8.5%
Wisconsin	Aa2/AA/AA	24%	16%	10.1%	4.60%	100%	6.1%	7.6%
Wyoming	NR/AAA/NR	36%	7%	14.6%	0.11%	89%	2.9%	5.9%

Source: Janney FIS. Federal Aid as a % of Revenue is per the U.S. Census Bureau. Medicaid % of Total Expenditures per National Association of State Budget Officers Fall 2010 Expenditure Report. % Change in Tax Revenue is 1Q2010 to 1Q 2011 and per the Rockefeller Institute July 2011. NTSD to state GDP is per Moody's May 2011 State Debt Medians Report. State pension data from Pew 2011 report (data from 2009). A plan 80% funded is considered healthy by the GAO. Includes Mortgage foreclosures & those 90 days past due data (non-SA) from the Mortgage Bankers Association 1Q 2011. Unemployment rate (SA) per the Bureau of Labor Statistics as of June 2011.

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