

COLLATERALIZED MORTGAGE OBLIGATIONS (CMOs)

Collateralized Mortgage Obligations (CMOs) are securities that are created from a pool of mortgage pass-through securities. CMO investors receive interest and/or principal payments from the mortgage securities in a predetermined manner. There is a range of time frames, payment frequencies and structures available to help meet investors' needs.

PRODUCT HIGHLIGHTS

CMOs offer a number of benefits that fixed income investors can consider, including:

- Monthly cash flow of principal and interest, or interest only
- Access to investments, such as Ginnie Mae (GNMA) securities, backed by the full faith and credit of the U.S. government
- Yields which can be higher than those of Treasuries and other fixed income securities
- Varying time horizons, from one month to 30 year possibilities
- A historically liquid secondary market
- Availability in denominations of \$1,000 and higher

How Does a CMO Work?

A CMO is a security that pools together mortgage investments and separates them into short-, medium-, and long-term classes (called tranches). Each class (tranche) has its own attributes, such as coupon, yield, average life and expected cash flow. Classes can pay different rates of interest depending upon their maturity. Interest payments are usually made on a monthly basis. Your Financial Advisor can help you to determine what type of CMO may be appropriate to consider given your specific investment objectives.

The Mortgage Securities Market

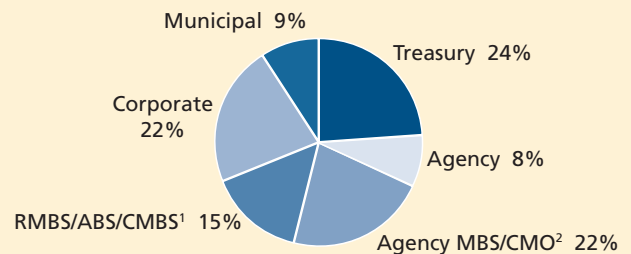
As shown in Chart A, mortgage pass-through securities and CMOs comprise over 20% of the U.S. fixed income market. There are several types of mortgage securities that investors can consider. Provided below is a description of agency mortgage securities:

Ginnie Mae Securities: The Government National Mortgage Association (GNMA) is a U.S. government agency which guarantees the timely payment of both principal and interest for mortgage securities. Its guarantee is backed by the "full faith and credit" of the U.S. government.

Fannie Mae and Freddie Mac Securities: The Federal National Mortgage Association (FNMA) and the Federal Home Loan Mortgage Association (FHLMC) are government-sponsored enterprises (GSEs), currently operating under conservatorship of the Federal Housing Finance Agency. FNMA and FHLMC guarantee the timely payment of principal and interest, but neither carries the "full faith and credit" guarantee available on Ginnie Mae securities.

Chart A: U.S. Dollar Fixed Income Market Composition

(\$32 Trillion as of December 2009)



¹ RMBS/ABS/CMBS: Residential Mortgage-Backed Securities, Asset-Backed Securities and Commercial Mortgage-Backed Securities.

² Agency MBS/CMO: Agency Mortgage-Backed Securities and Collateralized Mortgage Obligations.

(Source: Janney Fixed Income Strategy; SIFMA)

CMO Structure

Unlike corporate, Treasury or municipal bonds, CMOs have an “average life.” The average life is the average number of years each dollar of principal is anticipated to be outstanding, based on mortgage prepayment assumptions.

Average lives can vary as a result of changes in the rate of mortgage prepayments, resulting mainly from refinancing and turnover rates (e.g. home sales). As a result, mortgage securities are discussed in terms of *estimated* average life, rather than their maturity date.

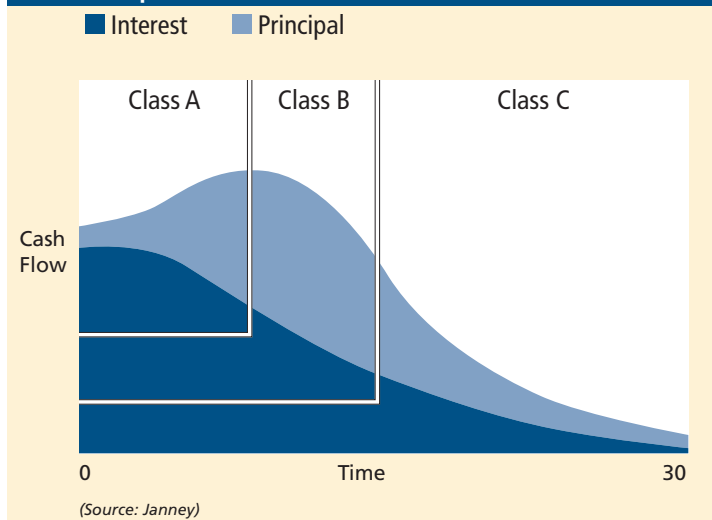
CMOs have the potential to meet a number of individual investment objectives by providing structures offering income as well as choices between characteristics such as average life stability, higher yields or lower prices. For example, certain CMO support structures with increased exposure to average life sensitivity, or variability, offer higher coupons and yields, and/or lower prices than certain Sequential and other CMO structures created to provide average life stability and carrying either a lower coupon and yield or a higher price.

Profile of a Sequential CMO

A Sequential Pay CMO is the most basic type of CMO. It pays cash flow in a specific sequence, which can provide interest and principal payments in a more predictable manner. Each class receives regular interest payments, but principal payments received by the CMO are made only to the first class until that class is completely retired, then to the next class until it is retired and so on until the last class is retired. The first class may have an average life of 3–4 years, the second class 5–6 years, and the third class 8–9 years (and so on). CMOs can have a number of classes, and each can have characteristics that differ from the others.

The information herein has been prepared for informational purposes only. In no event should it be construed as a solicitation or offer to purchase or sell a security. Collateralized Mortgage Obligations (CMOs) are complex securities and are not suitable for all investors. The information presented herein is taken from sources believed to be reliable, but not guaranteed by Janney as to accuracy or completeness. The yield and average life of CMOs may fluctuate significantly depending on the actual prepayment experience of the underlying mortgage and changes in current interest rates. Prospectuses for any new issues mentioned are available upon request. Further information describing the basics of investing in CMOs can be discussed with your Janney Financial Advisor. For investment advice specific to your individual situation, please contact your tax or legal advisor and/or your Janney Financial Advisor.

Chart B: Sequential CMO



CMO Risks

CMOs, like most fixed income investments, have exposure to certain risks, including:

- **Prepayment or Call Risk** – Prepayment assumptions are built into CMO pricing. For example, when rates fall and homeowners prepay mortgages faster than expected, investors may find their investment term is shorter than anticipated, potentially resulting in reinvestment at lower rates.
- **Extension Risk** – CMOs have the potential to extend beyond original average life assumptions as a result of rising interest rates and/or slower prepayment speeds.
- **Market or Interest Rate Risk** – As with most fixed income investments, changes in the direction of interest rates can impact the market value of CMOs, which, if sold prior to maturity, may result in a gain or loss in market value.

For More Information

Your Janney Financial Advisor can provide you with more information on CMOs as a potential fixed income investment for your portfolio.