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IdahoTrust

WealthManagement

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Market Insights

A periodic newsletter from Idaho Trust

The Federal Reserve continues its unprecedented accommodative monetary policy by recently announcing another round of open-ended quantitative easing. Also, state and local governments are finding timely ways to save money by refinancing existing bonds with new cheaper bond issues.

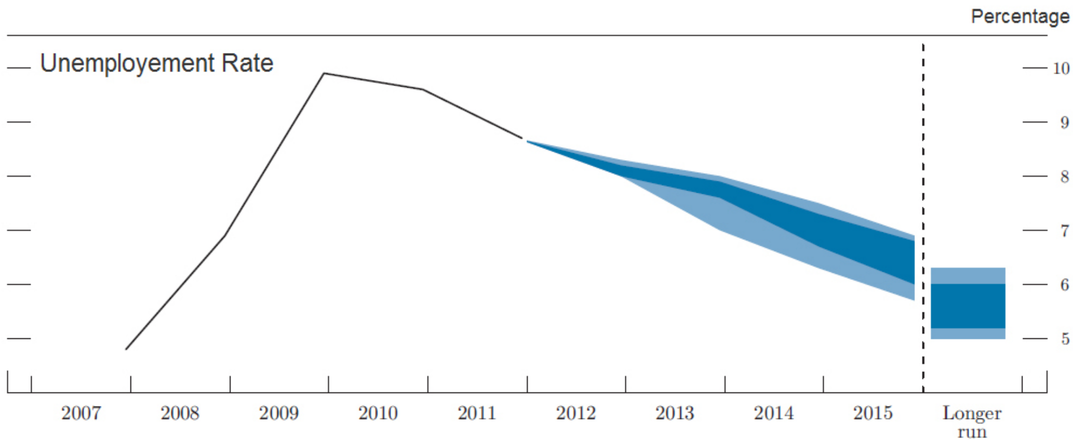
The Federal Reserve

On Thursday, September the 13th the Federal Reserve (Fed) announced that it will be providing additional easing through an open-ended quantitative easing program. This round of easing has been dubbed QE3; however, it could be more aptly named “QE Forever” because the Fed did not outline a specific timeline for the program. The program will consist of 40 billion dollars of agency mortgage backed security purchases each month with newly created money. QE1 ran for 16 months and consisted of roughly 1.7 trillion dollars targeting mortgage backed securities. QE2 ran for 7 months and consisted roughly of 600 billion dollars of treasury security purchases. Policy makers did give guidance as to when the new program will terminate, stating *“highly accommodative stance of monetary policy will remain appropriate for a considerable time after the economic recovery strengthens.”* This language serves two purposes, it reinforces the Fed’s commitment to spurring a stronger recovery and it also signals to the market that the Fed will not tighten their monetary policy at the first sign of economic acceleration but will wait until a stronger recovery is verified. This type of language has been consistent with Chairman Bernanke’s pledge to bring more transparency to the Fed’s operations.

Idaho Trust Bank offers total wealth solutions including its LifeNeeds™ investing process. Idaho Trust's LifeNeeds™ investment process utilizes proven strategies and techniques delivered by a highly trained staff of wealth management professionals.

LifeNeeds™ wealth management accounts feature optimized asset allocations, robust security screening and Idaho Trust's unique TacticLogic™ investment process. All of which are tailored to our client's unique financial needs.

It is important to note that this program is not a replacement of the Fed's current Operation Twist program, which is currently being carried out and will continue until the end of the year. The Fed also lengthened their pledge to keep rates low until sometime in 2014 now to the middle of 2015. In conjunction with the Fed's policy making meeting in September, the Fed released new economic projections. The new Fed projections now show another downward revision to projected 2012 GDP. Currently, the Fed is predicting 2012 GDP will be 1.7% to 2.0% down from their April projection of 2.4% to 2.9%. These recent projections also show an expected slow decline in the unemployment rate over time (see below).

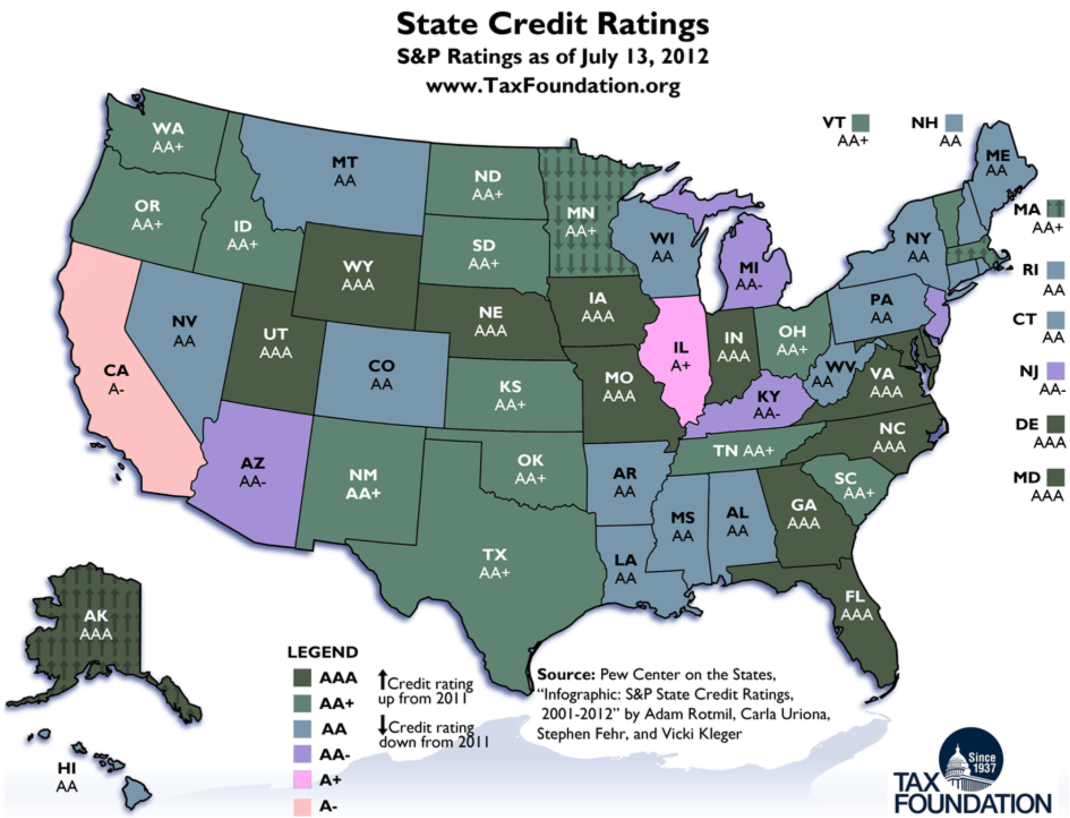


Source: The Federal Reserve

The Municipal Bond Market

In 2011, municipal bonds rallied and reported fewer defaults than in typical years. In 2011, municipal bond performance was outstanding. The Barclays Municipal Index, a broad measure of the municipal bond market, returned 10.70% in 2011, compared against the Barclays US aggregate bond index, a broad measure of taxable bonds, which returned 7.84% in the same period.

Currently, municipal bonds are making headlines. Several large municipal bond issuers have declared bankruptcy including Jefferson County Alabama, Stockton California, San Bernardino California and Central Falls Rhode Island. Although total municipal bond defaults have risen this year as compared to last, it has been within projected levels. Overall in the municipal market, State and local governments are taking advantage of the record low interest rates prevalent in the market by refunding existing bonds. Municipal bond issuers are capitalizing on the low rates by refinancing their existing bonds into lower, cheaper market rate bonds. These rates are now close to a 45 year low. By refunding outstanding bonds, municipalities that are still struggling to recover tax revenues are making up ground by retiring their outstanding expensive bonds and replacing them with new cheaper bonds. In fact, of the roughly $250 billion dollars of municipal bonds issued this year about 62% have been to refinance existing bonds. The refinancing activity comes at a time when the demand for longer-dated municipal bonds is high and supply is low because the bonds that are being refunded are typically longer-dated bonds. This dichotomy of supply and demand has caused the yields on 30-year municipal bonds to drop about 10 times more than similarly dated treasury bonds this year.



Possible Alternative Minimum Tax Changes

One of the issues at the forefront of the upcoming fiscal debate is a possible expansion of the Alternative Minimum Tax (AMT). An expansion of the AMT appears to have the most bipartisan support and could be used to propel Congress to a deal. AMT is a parallel income tax designed to tax a flat rate above a certain threshold of adjusted gross income. It was imposed in 1969 when it was discovered a number of individuals were making over $200,000 and legally not paying any taxes. The idea is simple, to ensure that high-income people would be paying at least some taxes. In application, the idea has proven to be not so simple.

Some municipal bonds, bonds issued by a state and local governments for use of private entities, are issued with an AMT provision that make the interest that these bonds pay taxable under AMT. Because of the potentially higher tax liability, AMT bond issuers have to offer their bonds at higher yields to attract potential buyers. AMT bonds can be attractive for individuals who do not have AMT liability because of the higher yields that they offer. If an expansion of the AMT occurs, then more individuals will qualify for AMT and demand for AMT bonds could dramatically decrease hurting AMT bond issuers by increasing their cost of funding projects or hindering their access to capital markets altogether.

Fed officials are optimistic that QE3 will help the economy and are showing their determination to lower the stubbornly high unemployment rate. Already, stock markets have reacted positively creating great stock returns thus far in 2012.

S&P 500 Index

3 Month	6.35%
Year-to-Date	16.44%
1 Year	30.18%
3 Year	13.21%
5 Year	1.05%

Barclays Municipal Bond Index

3 Month	2.32%
Year-to-Date	6.06%
1 Year	8.32%
3 Year	5.99%
5 Year	6.05%

Barclays Aggregate Bond Index

3 Month	1.59%
Year-to-Date	3.99%
1 Year	5.16%
3 Year	6.19%
5 Year	6.52%

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