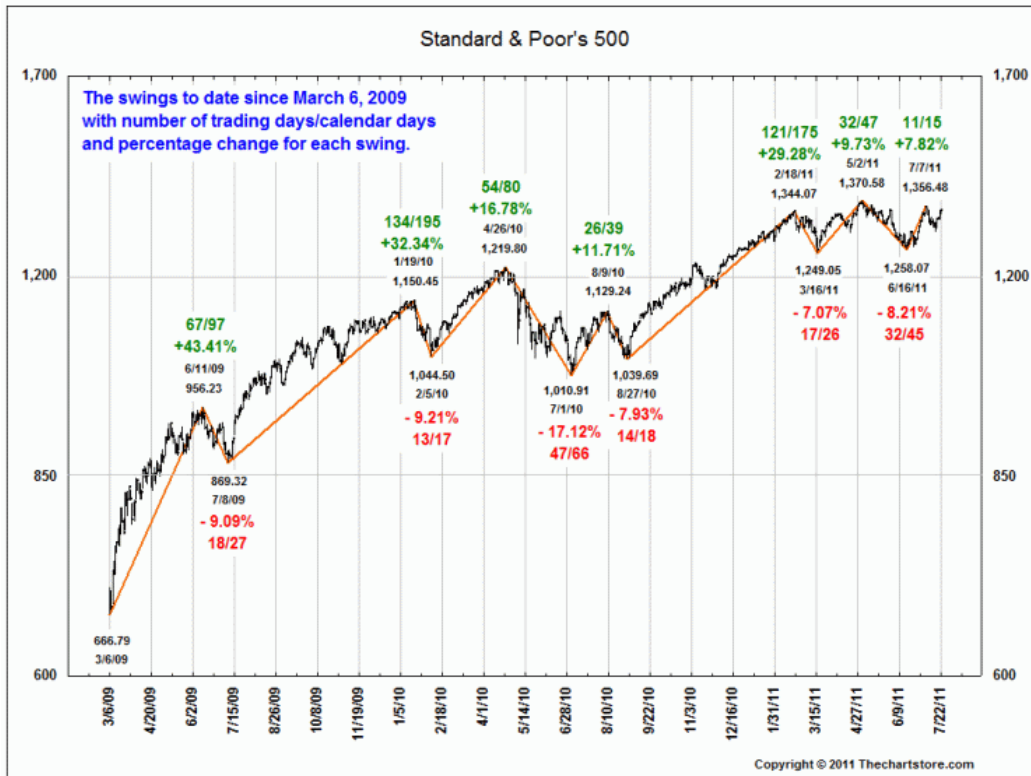


AUGUST 2011

Investment Thoughts: Light and Shadow

Risk on. Risk off. Offense. Defense. With the rapidly changing picture for global growth and various sovereign debt scares, one is left with the idea that the future will have a binary path; all is well, or, all is lost. This has led to short run bouts of optimism and dread in the stock market. In the chart below we can see the swings back and forth in 2011 as investors try to discern the path of the economy.

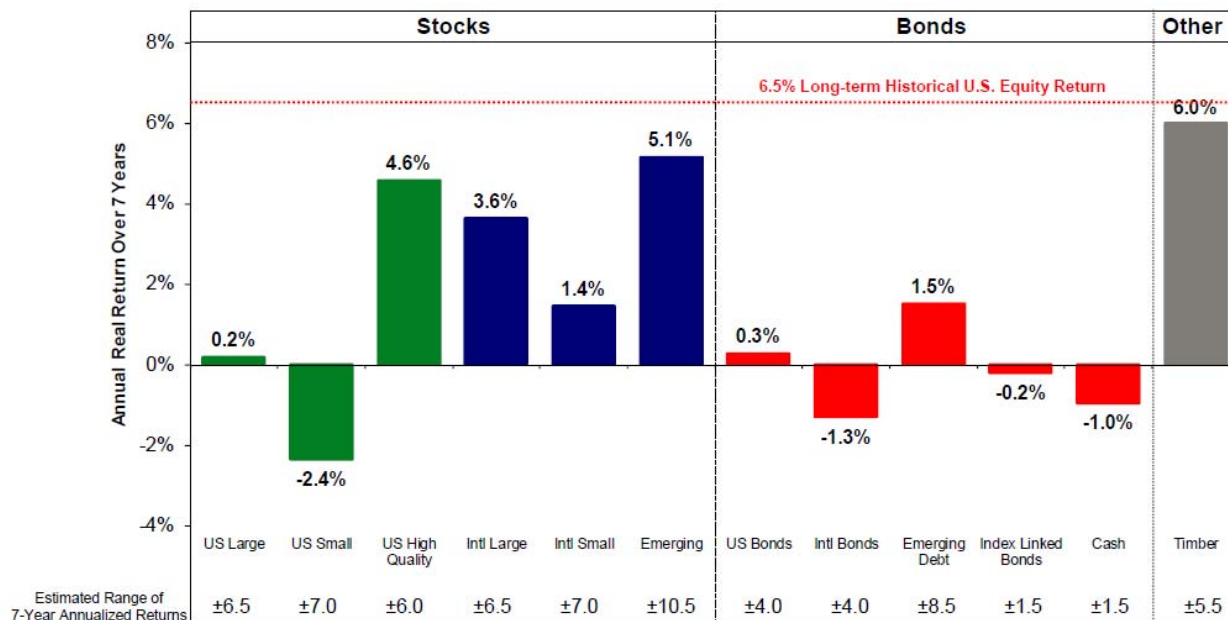


We have noted before that excessive debt at all levels of our economy will hold future growth at a below trend rate, perhaps 5% profit growth for U.S. corporations compared to the 7% historical average. GDP growth for the years 2011 and 2012 looks like 1.5%-2.5%. We think the stock market has begun to see the extent to which our fiscal and monetary policies could not improve matters. The conclusion is that the lasting effects of the debt crisis will lower the growth trend for the next five years or more.

If profit growth trends about 5% and we receive a 2% dividend from the market, it implies a 7% return expectation. Endowments and other long-term investors aspire to a 5% *real* return from stocks. Inflation might be estimated at 3% for this exercise, or at 2.5% as used in the forecast below from Jeremy Grantham of GMO, LLC, a Boston asset manager since 1977. His forecast is in the range of our estimates.

GMO 7-Year Asset Class Return Forecasts*

As of June 30, 2011

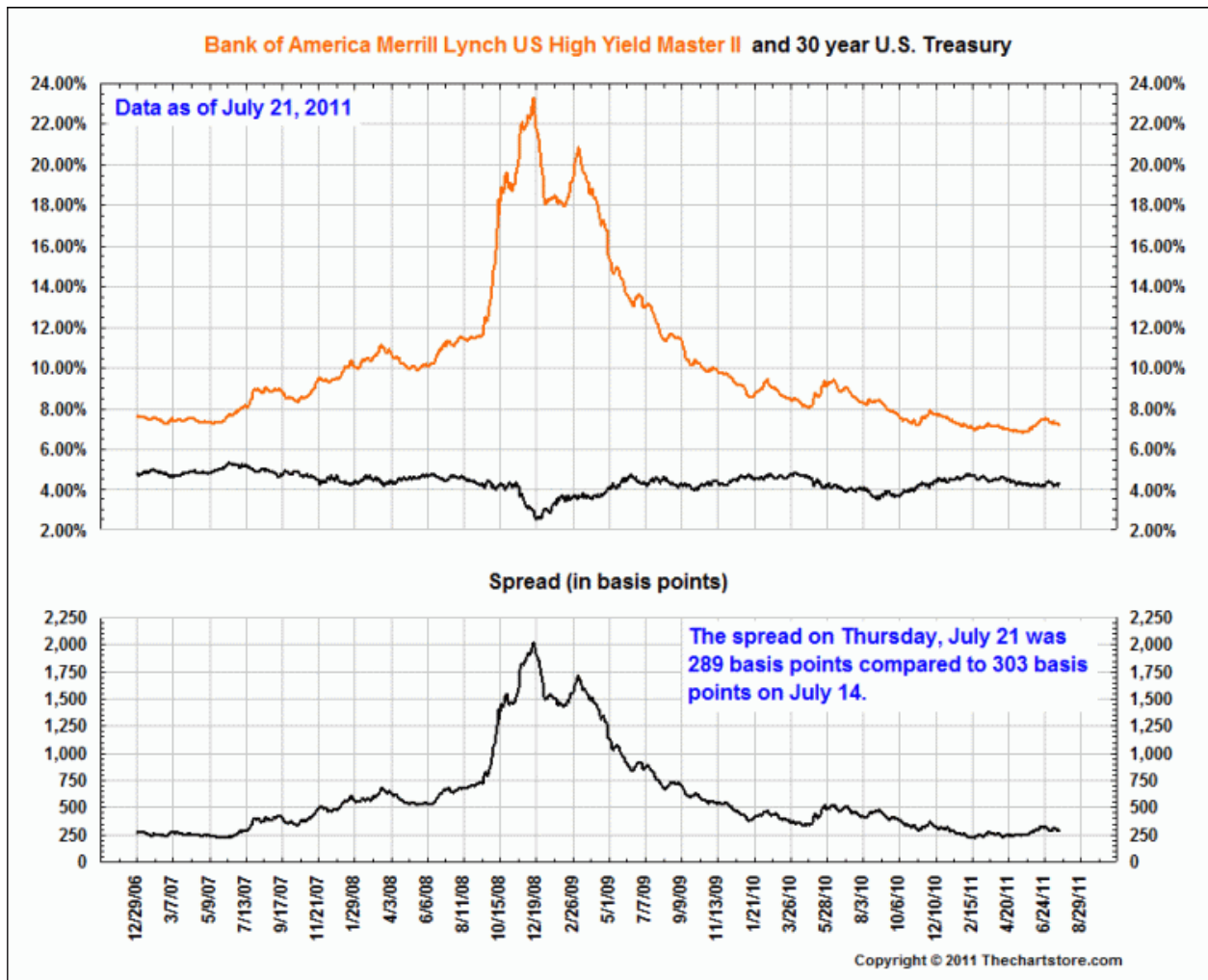


*The chart represents real return forecasts¹ for several asset classes. These forecasts are forward-looking statements based upon the reasonable beliefs of GMO and are not a guarantee of future performance. Actual results may differ materially from the forecasts above.

¹ Long-term inflation assumption: 2.5% per year.

At Ledyard Financial Advisors we have sought out strategies that could replicate stock returns, but with less volatility than we could incorporate into a stock portfolio. High yield corporate bonds offer today an equity-like return (about 7-8%) from interest. Due to their lower credit quality than high grade corporate debt, it is suitable to buy them only in the context of a diversified portfolio of bonds from a specialist in this sector of the bond market. High yield bonds in a portfolio of various maturities have had less volatility in price than stocks, yet have paid in cash an equity-level return. An investor who might own 85% stocks could substitute 10% high yield bonds and reduce volatility for the portfolio without giving up all the returns expected from stocks.

In the chart below we see the current yield differential to be earned on high yield bonds compared to that on a U.S. Treasury Bond. This chart follows the broad universe of high yield bonds. In our portfolios we own a select area of the market characterized by the highest quality tiers and shorter maturity bonds. Each bond in the fund's portfolio is monitored for its ongoing ability to pay and credit analysts track underlying corporate earnings closely. With high yield bonds we accept some credit risk in exchange for current high cash returns and less price volatility than the market.



Even in the credit crisis of 2008 when all assets, stocks and bonds declined, high yield bonds declined less and recovered about equally to stocks. Our fund, Metropolitan West (MWHIX) has outpaced the market since 2007. Some of this performance was a result of falling yields brought about by the Fed that made high yield bonds appreciate in price along with earning a high interest rate. A falling rate climate will not be part of the near future, as rates will be held low by the Fed to help out the economy. Therefore, we have only the expectation of earning the interest alone on our fund going forward. Nevertheless, 7-8% is attractive “rent” for our client’s money in the current environment.

COMPARATIVE RETURNS

Range 7/23/07 - 7/19/11 Period D Daily 1457 Day Period

Securities	Crncy	Prc Appr	Total Ret	Difference	Annual Eq
1 MWHIX US Equity	USD	-.47 %	46.34 %	52.42 %	10.01 %
2 SPX Index	USD	-13.94 %	-6.08 %		-1.56 %
3					

(* = No dividends or coupons)



As a young analyst I was exhorted to look at light and shadow, if you will; meaning values are often discovered outside of what is being most focused on. I believe high yield bonds will perform well as we exit our recession and while nothing is risk-free; they offer a good tool for current returns and diversification.

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