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The HIGH-NET-WORTH INVESTOR'S GUIDE *To* TAX-FREE INCOME

The DRL Group

Fixed Income Specialists

YOUR MUNICIPAL & CORPORATE BOND SPECIALIST

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THE DRL GROUP-

"We specialize in helping high-net-worth investors maximize tax-free returns by proactively maintaining their custom bond portfolios through all market conditions."

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The DRL Group has been consistently recognized as one of Houston's top wealth managers. The National Association of Board Certified Advisory Practices (NABCAP) name us among the top wealth managers two years running, and the Houston Business Journal featured us in both 2012 and 2013. We've been showcased as one of the best businesses of Katy, Texas for 2013, 2014, 2015, and 2016.

ARTICLES FROM DRL GROUP

DIRECTORY

WHY BUY MUNI BONDS IN A TAXABLE WORLD?

HOUSTON BUSINESS JOURNAL LEADERSHIP TRUST
BY DAVID LOESCH, OWNER AT THE DRL GROUP

In this low-interest-rate environment, investing in bonds generates little excitement — especially when returns on a 10-year, tax-free muni yield around 1.08% while the 10-year taxable treasury yield pays around 1.62%. Attention seems focused on the stock market, which keeps reaching record highs.

With the current administration, there are plenty of reasons to consider tax-free income. While the governmental stimulus is being distributed to support the U.S. through the COVID crisis, we will eventually have to pay down all that debt.

Rumblings of higher income tax rates, a 2% wealth tax, elimination of the "step-up" basis (in the transfer of wealth), lowering the estate tax cap and changes to the tax-free status of retirement plans should, in my view, be cause for concern. Considering these possible negative tax consequences, protecting your income with tax-free returns (and added liquidity) is paramount.

In light of these potential taxation changes, I recommend doing the math to understand the difference between muni bonds, treasury bonds and the equity markets.

We'll use the following yields as of close of business on March 24, 2021.

- **Muni yield:**

10 year: 1.08%

30 year: 1.82%

- Treasury yields:

10 year: 1.62%

30 year: 2.31%

If you live in a state with an income tax, add that percentage to the federal rate when you calculate.

Here's an example for the state of New York: 37% federal tax + 4.4% state tax + any city income tax = 41.4% total tax. This gives a tax basis (TB) percentage of 58.6%.

Using this example, here is how you would determine the after-tax yield on a 30-year treasury bond: Multiply the taxable yield (TY) of the bond (2.31%) by the TB% (58.6%) to get the tax-free equivalent (TFE). That gives you 1.35%.

In this case, an investor with a 41.4% income tax rate would only earn a 1.35% after-tax return on investment when purchasing a treasury bond. That means that a tax-free muni yielding 1.82% would be a considerably better investment.

That same calculation with a 10-year treasury paying 1.62% gives you a TFE of 0.95%. That means that a tax-free muni with a 1.08% return rate would be a better investment than a treasury.

Now, let's compare the above to a few popular, actively traded stocks. We'll use closing prices as of March 24, 2021.

- Johnson & Johnson (JNJ)

Closed at 161.91; 2.52%

Multiplying 2.52% by 58.6%, you get a 1.47% after-tax yield.

- JP Morgan Chase (JPM)
Closed at 150.62; 2.39%

Multiplying 2.39% by 58.6%, you get a 1.40% after-tax yield.

- Home Depot (HD)
Closed at 292.75; 2.28%

Multiplying 58.6% by 2.28%, you get a 1.34% after-tax yield.

In these three examples, a 30-year muni yielding a 1.82% return beats the after-tax return of these stocks as a long-term investment. To equal that return in this same tax bracket, you'd need a 3.10% taxable yield. The muni also allows you to gain liquidity, insurance and a high loan-to-value ratio in a margin account.

If you've been loading up on high-yield securities, keep in mind that all it takes is a downgrade or default to cause a significant decline in the value of your investment portfolio. I believe the risk does not justify the reward. This is why I believe purchasing muni bonds makes sense, even in a taxable world.

The information provided here is not investment, tax or financial advice. You should consult a licensed professional for advice concerning your specific situation.

HOW TO DECIDE BETWEEN BONDS: TAX-FREE MUNICIPAL OR TAXABLE CORPORATE?

HOUSTON BUSINESS JOURNAL LEADERSHIP TRUST
BY DAVID LOESCH, OWNER AT THE DRL GROUP

While the answer to whether you should invest in tax-free municipal bonds or taxable corporate bonds seems obvious – whatever pays the highest return – many other essential factors must be considered when making risk versus reward investment choices, and yield should only be one of them.

When investing in fixed-income securities, here are some essential questions to ask and preliminary information you will need to make wise decisions:

YOUR RISK PROFILE

- How much risk are you willing to take?
- How much liquidity do you need?
- How long can you wait to receive your principal back?

SECURITY RISK

- What is the source of funds (securitization) used to pay back principal and interest?
- What is the security's rating, and what do each of these ratings mean (relative to risk)?
- Is there insurance to protect the investment?

YOUR TAX BRACKET

- Does your state have an income tax?
- Are you subject to a city or local income tax?
- Are there any reciprocal agreements between your state and any other regarding buying bonds?
- If you have residency in multiple states, how does that affect what bonds you should buy?

YIELD

- What return can I get on my investment in the current marketplace?
- How do I compare tax-free securities to taxable ones?

THE DIFFERENCE BETWEEN MUNICIPAL AND CORPORATE BONDS

All these questions might have your head spinning. For the sake of simplicity, let's define the differences between a tax-free municipal bond and a corporate bond and then look at how compare their yields.

A tax-free municipal bond is a fixed-rate loan to a municipality such as a city, state or school district for an infrastucture-type project (building, water, sewer, electric, road, etc.) Interest on municipal bonds

("munis) is not subject to federal income tax in most cases. However, these bonds may be subject to state income taxes as well as city or local income taxes, depending on where you live. Munis are considered a safe investment and usually carry a fixed rate of return lower than a corporate bond.

Corporate bonds are fixed-rate loans to corporations for various business operations. They are subject to federal, state and local income taxes. They also generally carry a higher fixed rate of return because they rely on the corporate bonds' success and ability to repay the loan, which may potentially subject the bondholder to more risk.

HOW TO COMPARE A TAX-FREE MUNICIPAL YIELD TO A TAXABLE CORPORATE YIELD

If you already know the tax-free yield and want to know the taxable equivalent, you must know your tax bracket and if your state has an income tax. Assuming you live in a state with no state income tax, **the calculations goes like this:**

1 minus your tax bracket (assume 28%) = tax bracket percentage (TB%)

(1 - 28% = 72%)

The tax-free yield is divided by TB%. Let's assue that there are 3% tax-free muni yield.

(3% ÷ 72% = 4.17%, which is your taxable equivalent yield (TEY))

This calculation means that for a taxable corporate bond to be equal to a 3% tax-free municipal, the corporate yield would need to be 4.17%. In this case, the corporate would need to have a higher yield that 4.17% to be better than the 3% tax-free yield.

If you already know the taxable yield and want to know the tax-free equivalent yield (TFEY), **here's the calculation:**

Multiply the taxable yield by the TB% (in this case, 72%) = TFEY

(4.17% x 72% = 3.00%)

If you live in a state with an income tax, add that percentage to the federal percentage when you calculate.

Example: 28% federal tax + 6% state tax + 1% city income tax = 35% total tax.

(1 - 35% = 65% TB%)

Using the same comparisons as above:

(3.00% ÷ 65% = 4.61%)

In this case, a person with a higher tax bracket would need better than a 4.61% return to beat the 3% tax-free return.

Now that you know how to compare yields, it is best to consult a fixed-income advisor to understand and navigate the other factors mentioned above when assessing risk. While we all want to make the best return on our investments, sometimes a higher rate translates into more significant risk, and that uncertainty may not justify the reward.

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David Loesch, Pricipal/Co-owner, Fixed-Income Money Manager The DRL Group, specialist in Municipal & Corporate Securities.

HOW TO BUY MUNICIPAL BONDS

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BY DAVID LOESCH, OWNER AT THE DRL GROUP

With all the chatter about the prospect of rising taxes, my firm has seen more investors flock to the municipal bond market for tax-free investing. Purchasing municipal bonds is an investment alternative and a proactive measure to protect your income from taxation.

While most investors are accustomed to buying public equities (i.e., stocks), municipal bond investing is more complex and requires a higher initial investment (i.e., $10,000). Once investors understand the basics, municipal tax-free bonds can be a path to a steady timeline of tax-free income.

Municipal bonds are investment loans to various municipalities to improve or develop water and sewer systems, transportation systems and different capital improvement needs. Here's an example of a typical bond description: "10 Austin TX Water & Sewer System Rev 4.50% 06/01/2030."

The language above describes a municipal bond issued by the City of Austin to build or improve the city water and sewer system. This bond was issued with a fixed-rate coupon of 4.50% interest and matures (i.e., the loan principal is returned) on June 1, 2030. Bondholders of this issue would receive tax-free interest payments based on the number of bonds they purchased. In this case, the owner would receive $450 per year of tax-free earnings, split between two payments every six months. Austin's water and sewer revenues, derived from billing their customers each month, are used to pay off this loan.

When Austin initially came to market with this issue, the loan amount was likely large, and the schedule to repay the loan might have been from one to 30-plus years. A repayment schedule such as this gives Austin a chance to pay back the bonds on a predictable plan. As an investor, if you liked this credit, you may have an option to purchase an Austin, Texas Water & Sewer System bond anywhere in that 30-year range, but at varied returns based on current interest rates and market pricing for that maturity.

When purchasing any investment, it is essential to know the exact rate of return so you can compare one bond to another as the value can change daily, as with any investment. In this case, however, the bond's interest payment will remain the same every year.

The inverse relationship between municipal bond prices and yields demystified

Bond investors should understand "the higher the yield, the lower the dollar price," and similarly, "the lower the yield, the higher the dollar price." If yields are up, the market is down; if yields are down, the market is up. To explain this further, investors should remember that a coupon

rate is fixed, but the value of a bond changes daily.

Let's look at an example. If you own a 4.50% coupon bond and interest rates drop to 2%, your 4.50% bond will rise in dollar value. Put another way, someone wanting to buy your bond today will need to pay a higher price to do so. That current 2% yield will equate to less than a 4.50% yield-to-maturity for the new owner, and yet, they will still earn the same fixed rate return of $450 per year. The new owner's price at a 2% yield equates to a premium (i.e., higher than face value) dollar price for this fixed-rate security. The premium, in this case, would be amortized over the life of the bond, giving the new buyer a 2% yield at maturity — not a 4.5% return.

Conversely, if a buyer purchased these at a 4.75% yield, they would pay a discount (i.e., less than face value) for this bond, and thus receive a greater return on investment than the fixed 4.5% coupon. If this were the market value today for these bonds, the original owner would get a lower price than the original face value paid. The term for face value is "par" (i.e., $1,000 per bond). At maturity, a bondholder will get par, no matter how much it was purchased for. If you sell before a bond's maturity, you could end up with a capital gain or loss.

The most common question new bond investors ask is, "Why would I pay more now than I will get at maturity?" The best answer here is that you are buying a rate of return or a flow of funds. If a 2% tax-free yield is where the market is in a low-interest-rate environment, that is the market. The benefit of owning this bond is its high-interest payment of $450 per year, which is of value, especially if you are setting up retirement planning and want to know how much you will earn each month. The investment may only yield a net 2% in the long run, but year after year, your interest payments will reflect 4.5% of the bond's face value. This investor is essentially paying a higher price now for higher income later.

OTHER IMPORTANT FACTORS WHEN PURCHASING MUNICIPAL BONDS

- **TAXES:** Most municipal bonds are federally tax-exempt. Depending on where you live, returns may be subject to your state's income tax. Most states do not tax municipal bond interest if the investor buys and holds municipals issued from the home state of residence.

- **RATINGS:** Another consideration when purchasing bonds is knowing the rating by either Moody's or Standard & Poor's. These rating companies evaluate various factors and assign a rating based on a bond's risk parameters.

- **CALLABLE VERSUS NON-CALLABLE:** If a bond is non-callable, the issuer cannot redeem it before maturity. If it is callable, however, the issuer can redeem the bond on the stated date and at the specific price. The primary reason an issuer would call a bond before maturity is because interest rates have dropped and the debt can be refinanced— similar to why you would refinance your home loan.

- **DAILY SUPPLY:** The number of available bonds to purchase depends on the number of new issues coming to market and the number of sellers in this $4 trillion over-the-counter marketplace.

While all of these factors must be considered when investing in municipal bonds, always consult your municipal bond specialist to guide you in building an optimum bond portfolio.

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David Loesch, Principal/Co-owner, Fixed-Income Money Manager The DRL Group, specialists in Municipal & Corporate Securities.

THE HIDDEN MARKETPLACE: A MUNICIPAL BOND 'BROKER'S BROKER' EXCHANGE

HOUSTON BUSINESS JOURNAL LEADERSHIP TRUST
BY DAVID LOESCH, OWNER AT THE DRL GROUP

While it is common to hear about daily fluctuations in the various market exchanges, such as NASDAQ or DOW, few investors are aware of a fluid exchange taking place daily between fixed-income broker-dealer trading desks and their competitors. This exchange is an over-the-counter marketplace where bond dealers come together via the "broker's broker platform" to buy and sell securities with one another.

The broker's broker (BB) is an intermediary/negotiator for buyers and sellers of municipal (muni) bonds in the secondary marketplace. Like a real estate broker, the BB does not own any securitites but acts as an agent, representing buyers and sellers of muni bonds. These agents help facilitate the trading flow in the $4 trillion municipal bond market.

This platform consist of firms that compete for bonds and clients, and the BB acts as a facilitator between the firms so dealers can buy what they do not have or sell what they do not want. The parties involved in the trades remain anonymous, but each must be a registered broker-dealer to participate.

So, why should your financial advisor's Broker Dealer use a BB? And how does using a BB affect the individual investor?

To answer these questions, you must understand that the buying and selling of municipal bonds is done in an over-the-counter marketplace.

In the past, players would wait for the morning delivery of a publication called "The Blue List." This publication listed municipal offerings by state and included the selling firm's name. Because anonymity is a valuable negotiating tool, a dealer would enlist a BB to entertain a bid for the bond of their liking. Thus, the negotiating began, and if all parties agreed, a trade occurred. Neither buyer nor seller knew who was on the other side of the transaction, and the BB worked with each firm to facilitate the transaction.

These firms across the U.S. would interact with the BB by phone numerous times a day, trading bonds. Today, dealers work with more sophisticated electronic trading platforms called electronic communication networks (ECNs). These systems allow dealers to advertise offerings, execute trades, and buy and sell on the auction platform - all without ever picking up the phone. This method has added greater visibility to muni products advertised in the marketplace while saving valuable time.

An attempt had been made to move municipal trading to a more generic valuing system, but that hasn't proven easy because of the unique differences among municipalities and their financial circumstances. Nevertheless, the electronic trading network (ETN) has come a long way and offers a considerable efficiency level.

The advantage of having your financial advisor's Broker Dealer firm work through a BB can be beneficial in multiple ways. First, if your financial advisor (FA) is looking for a specific type of bond for you and does not have it in inventory, they must go into the marketplace to source it. In this instance, enlisting a BB to find that specific bond is advantageous to the dealer. Dealers always seek to give their clients as close to what they request as possible, and the BB can show you bonds that might fit your clients' requirements.

This situation can also work in reverse. If a client has a bond their FA firm would not usually purchase, this dealer can go to a BB and get a bid for these bonds from another dealer who traffics in that type of paper. In these cases, the dealer satisfies the investment objectives. Using a BB can also assure you that when you sell bonds, the price you are quoted represents what the marketplace pays that day, not just the in-house bid from your FA.

When selling your securities, the BB provides auction-like services by asking marketplace participants to bid on your bonds. This format assures the seller that their bonds are shown to dealer all over the U.S. If the price is right, a trade ensues. An attractive block of bonds can receive upwards of 10 bids, which would save your from calling more than 10 firms yourself to ask for a value on your securities. BBs provide an assurance that the bid price you receive is not just representative of your FA firm's price level but that of the entire marketplace on that day.

Dealers who actively participate in daily bond auctions have an opportunity to bring value to their clients by purchasing bonds on the "bid side" of the market instead of the "offering side."

This method is beneficial to the individual investor because it ensures the best execution – and higher returns.

As with all investing, knowledge is power. Knowing more about the functioning of the muni marketplace is not only advantageous but essential to achieving your investment objectives. Discussing these issues with your fixed-income advisor is always time well spent.

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HOW DO MUNICIPAL BONDS COME TO MARKET? A LOOK INTO THE WORLD OF UNDERWRITING MUNI BONDS

HOUSTON BUSINESS JOURNAL LEADERSHIP TRUST
BY DAVID LOESCH, OWNER AT THE DRL GROUP

In the $4 trillion municipal bond market, few investors know how these securities come to be issued. We often hear of new public company stocks launching via initial public offerings (IPOs) in the marketplace, but the issuance of municipal bonds ("munis") does not get much attention.

The process starts with a municipality. An example would be a school district needing funds to improve its aging school buildings. Instead of approaching a bank, the district might instead issue municipal debt for likely a lower interest rate than a traditional bank would offer. The school district would also have the ability to set a repayment schedule designed to coincide with their ability to repay the debt.

Financial advisory firms (FAs), also referred to as underwriting firms (UFs), will consult with the municipality to advise on bringing their new issue to market. These firms also enlist a bond attorney to provide a legal opinion. This opinion is designed to protect both investors and the FA, ensuring the issue is legal and all regulations for issuance and purpose have been followed.

Depending on the loan amount, the municipality will either work exclusively with one FA firm or request competitive bids to underwrite the issue. Under $25 million deals are commonly negotiated with one firm. More significant issues are usually bid competitively.

When a UF firm brings a muni deal to market, they put up the entire loan amount in exchange for the exclusive rights to sell the bond issue. So, that UF firm essentially takes on the entire liability for the debt until they can sell these bonds to their clients.

In a negotiated situation, a selected firm works exclusively with the municipality to structure the deal to suit their repayment objectives and facilitate the process for their retail clients to purchase these muni bond securities.

In a competitive sale, each UF firm desiring to underwrite the offering submits a bid (i.e., schedule of repayment and pricing) to the municipality on a specific date and time. Typically, the firm that offers the loan at the lowest net interest cost to the municipality wins the deal.

Competitive bids are often submitted for larger issues by "selling groups," which are various UF broker-dealer firms willing to share liability for both the payment and reselling of the securities they purchase it from the municipality. Under this arrangement, all members of the selling group have the exclusive right to offer the bonds to their clients.

Once an underwriting firm acquires an issue, what is called an order period commences. The order period is a designated block of time wherein the

underwriter attempts to resell the securities to their clients. This firm is restricted to offering these securities at a fixed price, previously agreed upon between the municipality and the underwriter and reflected in the original bid. The underwriter's commission on these trades is built into the original loan agreement for each loan's maturity.

The reselling process explained above is termed "the primary market." After the order period has expired, if there is a balance of unsold securities, the underwriter can lift price restrictions and move the bonds into the secondary market, often referred to as "freeing the issue to trade." In the secondary market, bonds can trade to any dealer outside the underwriting firm, and the price of each maturity is no longer restricted. If the market has improved since the underwriting process began, it is not uncommon for the bonds to be marked up, making them now more costly for new buyers. Conversely, if the market has softened (i.e., bond prices have fallen), the underwriter might cut the bond price to expedite the sale of their position and protect themselves from further market deterioration.

In the secondary market, competing dealers can now purchase new-issue bonds they did not underwrite at prices that reflect the current market conditions.

The secondary marketplace is where a significant percentage of new and previously issued securities will change hands. Dealers use a variety of electronic trading platforms managed by "broker's brokers" (BBs). Broker's brokers are middlemen traders who interact daily with broker-dealer trading desks. They act as a dealer-to-dealer go-between for buyers and sellers in the secondary marketplace, and they do not own securities. These BBs work in a similar capacity as real estate brokers. The participation of BBs is critical to the daily trading flow in the over-the-counter municipal trading markets for bond buyers and sellers alike.

Once an issue is released to trade in the secondary marketplace, the underwriting process is complete. Firms that had a selling group arrangement will settle finances amongst one another, and the issue will be delivered to ultimate bondholders on a set date — typically one to two weeks after the sale.

While the process to bring a municipal bond deal to market can take months, the issue itself usually gets sold quickly to retail and institutional accounts. Unless an unsold balance exists, the bonds in question will not resurface in the marketplace unless an investor wishes to sell their position.

For more information on municipal bonds and which ones are most suitable for your investment goals, speak with an experienced fixed-income specialist.

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WHERE DOES THE MUNICIPAL BOND SUPPLY COME FROM?

HOUSTON BUSINESS JOURNAL LEADERSHIP TRUST
BY DAVID LOESCH, OWNER AT THE DRL GROUP

Amidst the $4 trillion municipal bond market, very few investors stop to think about where all these bonds come from and how investment advisors find the right bonds to suit their investment objectives.

The best place to unravel an answer to the first question is to look at the primary marketplace — this is where underwriting municipal bonds begin. First, a municipality that wants to borrow money to build or improve a facility (such as school, airport, roads, water and sewer system) enlists a financial advisory/underwriting firm to guide them in the borrowing process and facilitate bringing the bond issue to market. Once this is done, and the loan is complete, these bonds are available to marketplace participants, thus increasing the supply available to bond investors.

For example, let's say Nassau County, NY, wants to improve its roads and needs $500 million for the project. Once they complete the process mentioned above, there would be $500 million in bonds available for investors. But when a brokerage firm underwrites an issue, their clients, both retail (i.e., individuals) and institutional (i.e., banks, insurance companies, pension funds, etc.), have the option of buying these bonds first, before they are available to the rest of the marketplace.

If half of this bond issue goes to their clients, only $250 million will filter into the market for other investors. Once the rest of these bonds sell, this original $500 million bond issue is gone and is not available again until one of the original investors decides to sell their position.

If this Nassau County deal was priced too high and not attractive to investors, these bonds might remain in the marketplace until they are repriced or the market improves. With that said, supply, in this case, depends on "perfect pricing," demand, interest rates and market fluctuations.

In addition to the new-issue market, the rest of the supply comes from sellers of older, previously-issued bond deals, and these bonds make up a significant portion of the muni bond supply. Every day, registered dealers post offerings, bonds "for the bid/auction" or offerings wanted on various electronic trading platforms where they can buy and sell inventory or their customer's bonds.

Dealers will have access to municipal bonds from every state on these platforms, with every type of coupon, maturity, call structure and rating. Fixed-income firms like ours can bid bonds on the auction platform in hopes of buying munis on "the bid side."

The other option is to purchase bonds offered at specific prices and buy on the "offering side." It is usually advantageous to buy from a dealer who buys bonds for inventory or their client's portfolios on the bid side.

This method can provide an extra yield to the end buyer if the dealer firm does not have multiple layers of internal mark-ups before the bonds are offered to their customers. In addition, some firms like ours will use advanced technology to post live markets for securities. Using these programs to automate bidding for bonds "out for the bid or auction" that meet specific criteria is also possible.

Above all else, the best way to source products and help with the supply issue is to do business with an experienced fixed-income trading firm. While technology is highly effective, nothing beats the knowledge and experience that a seasoned, professional bond trader can bring to the table. This type of advisor will know different credits, understand structuring, payment source differences, insurance and how the market news and rate fluctuations affect your bonds.

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MUNICIPAL BOND INSURANCE: WHAT YOU NEED TO KNOW BEFORE BUYING

HOUSTON BUSINESS JOURNAL LEADERSHIP TRUST
BY DAVID LOESCH, OWNER AT THE DRL GROUP

Insurance coverage has an important place in daily life: Americans insure homes, cars, lives and businesses against unforeseen accidents or distruptions, yet many are unaware it is possible to have similar protection for specific investments.

Such is the case for investing in municipal bonds. Municipal bond insurance protects a bondholder against unexpected principal and interest delinquencies or defaults. While defaults on investment-grade municipal bonds are not commonplace, insurance provides added security and peace of mind regarding principal and interest protection.

When an issuer (municipality) wants to borrow money in the financial markets, the goal is to get that loan at the lowest interest cost possible. At the time of the initial underwriting, if an issuer decides to purchase municipal bond insurance, it enhances the security's marketability. It also helps the issuer keep that loan rate low. The insured rating is often higher than the underlying rating of the municipality, thus resulting in a lower net interest cost to the issuer.

So how does the insurance work?

If a municipality is unable to pay principal and interest because of a specific event and all covenants between the insurer and the municipality are met, the insurance will cover timely principal and interest payment until the issuer's financial matter is rectified.

What do I need to know about buying muni bonds with insurance?

- Not all bond insurance companies are the same. Each insurance company has its own risk-assessment model and claims-paying ability (CPA). For example, some will only insure essential service projects such as utilities, airports and schools.
- Each insurance company carries a rating based on S&P Global Rating Service evaluations of CPA risk and how extended the insurance company is in its portfolio of like-insured obligations.
- Muni bonds come to market with and without bond insurance. Not all munis are insurable.
- You cannot purchase bond insurance on a muni if it is not already insured in the primary marketplace at issuance. There are exceptions to this point if you are trying to insure a very sizeable block of bonds.
- Bonds insurance went through a restructuring period following the 2008-2009 financial crisis when legacy insurance companies overextended their coverage into riskier investments.

- New bond insurance companies in today's market (BAM, AGM, AGC) are monoline insurers with ratings of AA from Standard and Poor's.
- Municipal bond insurance has no association with FDIC or SIPC.

As you can see, there are some complexities regarding municipal bond insurance and how to know which insurance-wrapped bonds are better than others. In my experience, municipal investors want 45% of their investable assets in this asset class; therefore, it is an important topic to cover with an experienced investment advisor.

In general, municipal bond insurance can offer added protection and peace of mind if you're investing in municipal bonds. As always, and for any investment, it is best to consult your fixed income advisor for a more detailed understanding and risk assessment.

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David Loesch is Principal/Co-owner, Fixed-Income Money Manager at the DRL Group, specialists in Municipal & Corporate Securities.

OUR TRADING PHILOSOPHY

The DRL Group maintains a performance-oriented culture, always adhering to clear and consistent investment practices. The group is committed to rigorous fundamental research, with a focus on constant awareness of current fixed-income market trends, pricing structures, and credit enhancements. We maintain sound relationships with other Broker Dealers, which result in best execution for our clients—the cornerstone of The DRL Group's investment philosophy.

While our clients ultimately make the final decisions for their individual portfolios, they work closely with The DRL Group's team, which includes sales and operations professionals as well as fixed income traders. We engage in a dynamic process of conveying and debating various investment strategies that meet our clients' objectives.

This investment process prizes intellectual rigor, while leveraging the knowledge and skills of the DRL Group, and of course, the client. Our entire staff works as a group to provide fast, efficient and personalized service to each and every client. We strive to make every transaction a positive and profitable experience for our clients, while always maintaining regulatory and compliance standards.

Our team approach recognizes that individual accountability of each DRL Group associate combined with close client collaboration, is the foundation of success. The DRL Group believes that to meet our clients' financial needs consistently, we must:

- Understand each client's investment objectives, risk tolerance, and time horizon
- Draw on our broad-based market research and experience to deliver results
- Invest with specialization at every level (meaning focusing on the "bid" side of the markets to deliver better execution, resulting in a higher rate of return)

The DRL Group
Fixed Income Specialists

LADDERING MUNICIPAL BONDS:

PROTECTING PRINCIPAL AND GAINING PREDICTABLE TAX FREE INCOME

HOUSTON BUSINESS JOURNAL LEADERSHIP TRUST
BY DAVID LOESCH, OWNER AT THE DRL GROUP

This year's market volatility in most asset classes has stunned many investors and caused significant indecision regarding where to place investable funds safely. Both the stock and bond markets have been hard hit. With economic and geopolitical issues impacting the supply chain, interest rates, housing prices and cost of goods, it can be daunting to figure out what's next and how to invest safely.

Most investors are concerned with finding the best return on investment and, more importantly, protecting their principal. With these factors in mind, laddering municipal bonds is something many investors should consider seriously.

Laddering bonds is an investment strategy that staggers bond maturities at regular intervals across a specific time range. Laddering high-grade municipal bonds offers a considerable level of assurance that your principal will be secure while also providing tax-free returns. Laddering also allows investors the flexibility to respond to changing market conditions and interest rate fluctuations while minimizing risks associated with investing in more significant positions.

Before diving into laddering, let me familiarize you with the municipal bond structure. Bonds are issued with a purpose for the loan, a fixed rate of return and a preset maturity. Some bonds are callable, meaning the issuer can redeem them before maturity on specific dates. Municipals are issued in $5,000 denominations, but it is generally cost prohibited to do a ladder with such small amounts.

A typical bond description would look like this:

$25,000 State Utilities 4.50% 5/01/2035
Callable 5/01/2030 @100

In this example, $25,000 is the face value of the bond, 4.50% is the fixed rate of return on the investment, the bond will reach maturity on May 1, 2035, but there is a possible early redemption date beginning May 1, 2030, where the redemption price is par, or $1,000 per bond.

In order to simplify laddering, we will not go into bond pricing. In addition, while most bonds are callable, it is best to buy shorter non-callable maturities if you are doing a shorter-term ladder. When doing a longer-range ladder — a retirement account, for example — if bonds were called, you would reinvest those funds, keeping you on a steady pace of roll-offs.

Laddering bonds can be done very specifically depending on your investment goals. If you want funds to be constantly available, you might try a ladder with bonds that mature within two to five years. Within that investing range, you can set up your ladder to include bonds maturing annually or every six months.

For example, with a $100,000 investment and an annual roll-off of maturities, your ladder might look like this:

$20,000 City Transit - 3.00 - 1/01/24

$20,000 Regional Airport - 3.10 - 1/01/25

$20,000 State Highway - 3.20 - 1/01/26

$20,000 Interstate Highway - 3.30 1/01/27

$20,000 International Airport 3.40 1/01/28

Using the example above, once the City Transit bonds mature in January 2024, those funds, plus interest, could be reinvested in a new bond maturing in 2029. This rotation continues until the investor decides to use the funds or finds another asset class for the money. It is unnecessary to have specifics on the coupon rate, but it is not uncommon to see a progression of rising fixed rates as you go farther out in maturities.

For investors who want to align their ladder with retirement, the first bond should mature in that first year of retirement. For example, if you're planning to retire when you turn 67 in five years, your first bond would mature in 2027, and you would space out your funds for 10-20 years from that point, depending on your long-term investing comfort zone. Another strategy that works equally well is aligning your retirement accounts to coincide with Required Minimum Distributions (RMD). The first bond would reach maturity the first year of your RMD and roll off each year until the funds are fully dispersed. In this case, you know that the fund's principal will never be lower than the initial investment if you wait until maturity.

The only disadvantage of laddering might be when interest rates are falling. In this case, as your higher-rate bonds mature, you might have to reinvest in a lower fixed rate bond. But even in this scenario, you never have to worry about your principal — just your return on investment.

Municipal bond laddering allows investors constant liquidity because a portion of your assets is only a year away from maturity. It offers principal safety and tax-free returns and gives you the ability to reinvest as rates increase and options for changing investment strategy as maturities roll off. Best of all, laddering gives peace of mind that you will have a stable, predictable income stream and your initial principal investment is secure.

The information provided here is not investment, tax or financial advice. You should consult with a licensed professional for advice concerning your specific situation.

WHAT MAKES US DIFFERENT

MASTERS OF ONE:

Most financial professionals are "jack-of-all-trades, master of none." The DRL Group has taken a different approach to financial services. "We are Masters of One", having spent decades doing one thing well: fixed-income investing. We specialize in the bond market, helping provide fixed-income solutions for our clients. You can expect this singular focus from the DRL Group.

PRICE-EFFICIENT TRADE EXECUTION:

Thanks to our state-of-the-art technology. DRL Group clients have access to both the primary and secondary bond markets. This provides you with efficient pricing because we can execute trades on both the buy and sell side of the transaction, which in most case, results in the higher returns.

MUNICIPAL AND CORPORATE BOND SPECIALIST:

Our team of professionals is focused on providing fixed-income solutions to produce a stable income stream and help protect principal value. We create customized bond portfolios and preserve capital and minimize risk, while maximizing client returns in unpredictalbe market environments.

TAX FREE INVESTMENT SOLUTIONS:

Our Clients are interested in shielding their investment income from taxes. For investors who want tax-exempt investment solutions, we can purchase at dealer level pricing, with a nominal mark up on attractive tax-free bonds. This results in higher yields for our clientele.

WELL VERSED WITH MAJOR MARKET FLUCTUATIONS:

With over 35 years of collective industry expertise, we have been through significant ups and downs of the economy and the market. We have extensive experience adapting our clients' portfolios to ever changing market conditions. We will do the same for you.

PERSONALIZED PROCESS:

All clients receive the personal attention they deserve. We take the time to understand each client's needs based on their tax bracket, age, goal, and financial situation. We continuously analyze and update strategies to meet our clients' evolving individual onjectives for income, growth, and asset protection. And, our clients deal directly with the owners of the firm-not junior advisors or a call center. We know our clients' time is extremely valuable, so when a client calls, we pick up the phone. You can always expect good, old-fashioned service.

AWARD RECOGNITION:

The DRL Group has been consistently recognized as one of Houston's Top Wealth Managers. The National Association of Board Certified Advisory Practices (NABCAP) named us among the Top Wealth Managers two years running, and the Houston Business Journal featured us in both 2012 and 2013. We have also been showcased as one of the Best Businesses of Katy, Texas of 2013, 2014, 2015, and 2016. You'll be taken care of by an award-winning team.

INDEPENDENT:

Since we are not owned by a bank or an insurance company, we sell no proprietary products. Instead, the financial products we do offer are dependent on what's in the best interest of our clients. All of our operations are highly regulated, your investment funds are held at our custodian, National Financial Services, a 100% subsidiary of Fidelity Investments.

NEXT STEPS:

If you are a high-net-worth investor, we want to help you maximize your tax-free returns by maintaining your custom bond portfolio. Call us now to set an appointment with one of our specialists at 281-398-8600.

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