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# MBIA Capital/Claymore Managed Duration Investment Grade Municipal Fund Portfolio Manager Commentary

Q3 2009

 CLOSED-END FUNDS

NYSE: MZF

The National Bureau of Economic Research announced that the beginning of this current and deep recession started in December 2007. Since then, Gross Domestic Product contracted by 5.4% and 6.4% for the fourth quarter of 2008 and first quarter of 2009, respectively. Monthly non-farm payrolls contracted for 21 consecutive months beginning January 2008 with losses peaking in January 2009 at 741,000 jobs lost. Throughout the third quarter of 2009 it became apparent to most market watchers that the harshest economic contraction since the great depression was running out of steam. Important consumer and manufacturing indicators have indicated bottoming trends. Retail sales and durable goods orders ex-transportation may be indicating a bottoming in “real” consumer demand. Government aided programs, like Cash for Clunkers, have provided a much needed jump start to this demand. Job losses are also showing signs of improvement as are inventories of unsold homes, which have declined to eight months of supply from a peak of eleven. Signals of stabilization and nascent recovery are being delivered to the marketplace from most corners of the global economy. The S&P 500 Index<sup>1</sup> has rebounded by 58% from March 2009 lows as fear of a systemic failure of the global financial system faded.

Strong technical factors within the municipal bond market paved the way for robust tax-exempt bond returns during the 3rd quarter of 2009. The recent success of the “Build America Bond” program, scheduled to expire in December 2010, has shifted a large amount of new issue supply from the tax-exempt to the taxable market. As long as this program continues to remain a more attractive form of financing for municipal issuers we expect its use to continue. Investors with large cash balances looking for tax-exempt income have been increasingly forced into longer maturity bonds at higher prices. With taxes on the rise, retail investors continue to demonstrate a strong preference for tax-exempt income leading to record tax-exempt mutual fund inflows. Institutional investors have begun to reenter the market as corporations make a return to profitability and take advantage of the “cheap” ratios of tax-exempt to taxable bonds. Historically low yields in the front-end of the curve have pressured investors to extend maturities out of near zero percent paying money market mutual funds into longer maturity bonds. The decrease in long-dated supply and subsequent increase in demand has led to a flattening of the tax-exempt yield curve coupled with a significant compression in credit spreads. The market’s strong returns come on the heels of a deteriorating fundamental credit picture amongst many issuers. Combined state budget deficits are projected to exceed \$350 billion over the next two years with an unexpected fall in tax receipts already forcing some states to revise their 2009 budgets. This may boost supply estimates for 2010, however, municipal issuers who only had the option of issuing to a tax-exempt investor base can now tap into deeper taxable pockets of cash, and at attractive financing rates. The diminished tax-exempt supply may provide improved stability to the tax-exempt yields and anchor tax-exempt to taxable ratios inline with historical averages.

The Barclay’s Municipal Bond Index<sup>1</sup> returned 7.12% in the third quarter, according to Barclay’s Capital. The municipal yield curve (from 1-30 years) dramatically flattened during the period from 426 basis points (“bps”) to 350 bps, led by a rally in long-maturity bonds. The yield on 30-year AAA-General Obligation Bonds<sup>2</sup> declined by an astonishing 79 bps during the period, while 10-yr yields decreased by an impressive 66 bps. Tax-exempt bonds outperformed US treasuries pushing the ratio of 30-year tax-exempt yields to 30-year treasury yields from 106.9% at the start of the quarter down to 95.6% at quarter-end.

Credit spreads staged an impressive rally in the third quarter of 2009 and are approaching pre-credit crisis levels. Lower rated credits outperformed high-grade credits by a wide margin during the quarter. Return data also showed that investors favored longer maturity securities over short maturities, possibly in an effort to take advantage of the steepness of the yield curve in an environment where long-dated supply was scarce. According to Barclays Capital, single-A and BBB rated bonds outperformed the Barclay’s Municipal Bond Index by 228 and 519 basis points in the quarter, respectively. High-yield tax-exempt spreads also improved throughout the quarter evidenced by the Barclay’s Municipal Non-Investment Grade Index<sup>3</sup> outperforming the Barclay’s Investment Grade Index by 652 basis points in the third quarter.



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***For illustrative purposes only. Performance data quoted represents past performance, which is no guarantee of future results, and current performance may be lower or higher than the figures shown.***

***The forecasts and opinions are those of MBIA Capital Management as of September 30, 2009 and are subject to change at any time due to changes in market or economic conditions. The comments should not be construed as a recommendation of individual holdings or market sectors, but as an illustration of broader themes. Such forward-looking statements are subject to significant business, economic and competitive uncertainties and actual results could be materially different. There are no guarantees associated with any forecast.***

***There can be no assurance that any closed-end fund will achieve its investment objective(s). The value of any closed-end fund will fluctuate with the value of the underlying securities. Until the original listing of a closed-end fund on an exchange, no closed-end fund's shares will have a history of public trading and, historically closed-end funds often trade at a discount to their net asset value.***

<sup>1</sup>The Standard and Poor's 500 Index is a capitalization-weighted index of 500 stocks. The index is designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries. The index is unmanaged and it is not possible to invest directly in an index.

<sup>2</sup>The Barclay's Municipal Bond Index is a rules-based, market-value-weighted index engineered for the long-term tax-exempt bond market. To be included in the index, bonds must be rated investment-grade (Baa3/BBB- or higher) by at least two of the following ratings agencies: Moody's, S&P, Fitch. The index is unmanaged and it is not possible to invest directly in an index.

<sup>3</sup>General Obligation ("GO")- A municipal bond backed by the credit and "taxing power" of the issuers' jurisdiction rather than the revenue from a specific project.

<sup>4</sup>The Barclay's municipal non-investment grade index is a rules-based, market-value-weighted index engineered for the long-term tax-exempt bond market. To be included in the index, bonds must be non-rated or be rated non-investment grade (Ba1 or below) by at least two of the following ratings agencies: Moody's, S&P, Fitch. The index is unmanaged and it is not possible to invest directly in an index.

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