Plumb Funds

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Thomas G. Plumb, CFA
Lead Portfolio Manager
President, CEO, Chairman

Can You Compensate for Credit Risk?

Have you noticed that interest rates are very low and bond prices volatile?

Of course you have. The question is how to meet your clients' needs in this environment.

With interest rates at or near historic lows, you have probably found it very difficult to implement a strategy to provide clients with income. Many financial planning software programs assume over 4% returns for fixed income assets while the 10-year Treasury Note has consistently stayed below 3% all year and hasn't seen 2% since the end of July.

Additionally, the 44-basis point increase in yields from 1.46% to 1.90% over ten days in early September 2019 gave investors a taste of the potential loss in principal that bond exposure can bring.

The 10-year Treasury Note price declined 4% in less than two weeks!

Historically not only is it a challenge to provide your clients a reasonable retirement income, but you may be exposing your clients to a principal loss that they might not understand or be very unwilling to accept.

Before the extended 35-year secular bull market in bonds as rates declined from mid-teens to under 1.5%, we used to say one thing could go well with bond investing "You get your money back," while two things could go bad: "one, you don't get your money back (credit risk) or two, the bond is worth much less than you paid for it (interest rate risk)."

So how can you invest for your clients now?

In the Plumb Balanced Fund, we believe we can be compensated for credit risk while moderating effective duration by focusing our fixed income investments on the following investment-grade securities:

- **Variable rate preferred stocks:** Many high-quality banks issued these securities during the financial crisis. The dividend rate is reset quarterly, so you don't "lock in" low rates as they will float upward if rates rise.
- **High coupon short-term corporate bonds:** You may pick up the potential for net yield while reducing the duration from similar maturities.

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Blue Chip consumer staple, energy or health care stocks: If you don't need to invade principal, why not consider dividend achievers that have not been exploited by the record high stock market. We seek stocks that are trading at prices at or below where they were five years ago, have good dividend coverage ratios, yield 1-2%over Treasuries and have potentially favorable tax treatment as dividends when compared to interest-paying instruments.

In our opinion, what should you avoid?

- **Long duration bonds or bond funds:** You are not being compensated for interest rate risk and the math is compelling. The damage even a modest increase in ten-year rates can do to your principal is scary. And remember, if the Fed is successful in stimulating the economy by lowering short-term rates, we will have a positive sloping yield curve. Long-term rates could rise as short-term rates decline.
- Avoid exotics and funds that include credit or loan products. In our view, this trade is very crowded and if world economics lead to recessions, these products may not have the liquidity that might be necessary in adverse times.

Thomas G. Plumb, CFA
Lead Fund Portfolio Manager

Thomas G. Plumb is the founding principal of Wisconsin Capital Management, LLC (formerly Thompson Plumb & Associates), which began in 1984.

Tom formerly was the lead portfolio manager of Dreyfus Premier Balanced Opportunity Fund. He earned a bachelor of business administration from the University of Wisconsin-Madison in 1975, is a member of the Madison Investment Management Society and holds the Chartered Financial Analyst designation.

IMPORTANT INFORMATION

The Fund's investment objectives, risks, charges and expenses must be considered carefully before investing. The prospectus contains this and other important information about the investment company, and it may be obtained on www.plumbfunds.com or by calling 866-987-7888. Read it carefully before investing.

Any tax or legal information provided isn't an exhaustive interpretation of some of the current income tax regulations. Investors must consult their tax advisor or legal counsel for advice and information concerning their particular situation. Neither the Fund nor any of its representatives may give legal or tax advice.

Opinions expressed are those of the speaker as of September 19, 2019, and are subject to change, are not intended to be a forecast of future events, a guarantee of future results, nor investment advice.

Past performance does not guarantee future results.

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Basis point (BP) refers to a common unit of measure for interest rates and other percentages in finance. One basis point equals 1/100 of a percentage point. 1 bp = 0.01%, 100 bps = 1%.

Dividend Coverage Ratio is a financial metric that measures the number of times that a company can pay dividends to its shareholders. The dividend coverage ratio is the ratio of the company's net income divided by the dividend paid to shareholders.

Fund holdings are subject to change at any time and should not be considered a recommendation to buy or sell any security. References to other mutual fund products should not be interpreted as offers of those securities.

Mutual fund investing involves risk. Principal loss is possible. The fund may invest in small and mid sized companies which involve additional risks such as limited liquidity and greater volatility. The funds invest in foreign securities which involve greater volatility and political, economic and currency risks and differences in accounting methods. Because the funds may invest in ETFs, they are subject to additional risks that do not apply to conventional mutual funds, including the risks that the market price of an ETF's shares may trade at a discount to its net asset value ("NAV"), an active secondary trading market may not develop or be maintained, or trading may be halted by the exchange in which they trade, which may impact a fund's ability to sell its shares. The fund may also use options and future contracts, which have the risks of unlimited losses of the underlying holdings due to unanticipated market movements and failure to correctly predict the direction of securities prices, interest rates and currency exchange rates. The investment in options is not suitable for all investors. The Plumb Balanced Fund will invest in debt securities, which typically decrease in value when interest rates rise. This risk is usually greater for longer-term debt securities.

Diversification does not assure a profit nor protect against loss in a declining market.

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