MARYLAND CAPITAL ADVISORS INC.
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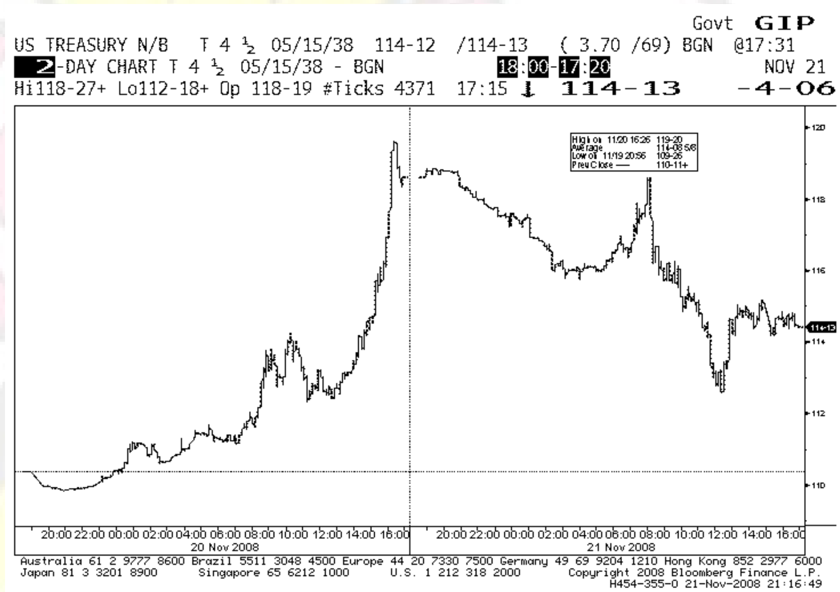
INVESTMENT COMMENT — November 23, 2008
Weekend Update

This past week was another one for the history books. The crisis du jour served each day this week was renewed fears of a failure of a large financial institution. Citigroup was the center of this concern as their common stock was -60.4% just this week, but other major banks were also hit hard (see table). Thursday was the climax of fear as measured by the price movement of the US Treasury 30-year bond. In my 20+ years of experience, I have never seen (and I do not believe it has ever happened) the price of the "long bond" trade in such a wide range. The chart below shows Thursday and Friday intraday prices. At the low price of 109.81 Thursday morning, its yield was 3.94%. Shortly after 4pm that day the bond had moved almost 10 percentage points higher to a low yield of 3.44% – that unprecedented move indicates the level of fear in the financial system.

Bank & Finance Stocks Total Return	Latest Week	2008 YTD
Citicorp	**-60.4%**	-86.5%
Principal Financial Group	-40.6%	-85.1%
KeyCorp	-34.7%	-71.9%
MetLife	-34.3%	-69.3%
JP Morgan Chase	-34.1%	-46.1%
SunTrust Banks	-33.0%	-62.4%
Prudential Financial	-32.7%	-81.7%
National City Corp	-31.3%	-90.0%
Bank of America	-30.2%	-70.6%
PNC Financial	-29.9%	-30.6%

Source: Bloomberg

So what caused this latest market crisis? It is normally difficult to attribute specific market moves to a causal factor. This week there was negative news from ongoing rescue discussions for Detroit-based auto manufacturers, and worse-than-expected economic news regarding inflation and consumer confidence data. However, ***the news item that seems most directly-related is the US Treasury's decision to abandon the asset purchase plan aspect of the Troubled Asset Relief Program (TARP) one week ago.*** As explained in this past Monday's Investment Comment[1], Treasury Secretary Paulson surprised many of us by stating that the plan was now to inject capital into banks with Treasury purchases of preferred stock, rather than negotiated purchases of "troubled assets". Financial institutions with such assets, under the revised plan, must now retain these investments of uncertain value, but will receive additional capital from the sale of preferred stock. The markets appear to have been expecting a process that would determine a price, potentially purchase these assets, and leave an otherwise cleaner (but smaller) bank balance sheet. After Treasury's abandonment of asset purchases, markets were left with renewed



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uncertainty and fear about the value of bank balance sheets. As we said previously, "No one, not the Fed, Treasury, Wall Street analysts, or anyone else knows what the asset-side of the GSE – or almost any other financial firm – balance sheets are worth"[2].

Some good news. Late Friday, markets rebounded on news of the imminent naming of NY Fed President Geithner as US Treasury secretary. That is certainly a good choice, but another important news item was an FDIC announcement finalizing their Temporary Liquidity Guarantee Program (TLGP). This program allows banks to issue unsecured debt with an FDIC guarantee through June 2012. How does this help? We have previously explained how the US Treasury was uniquely capable of profiting from the purchase of "troubled assets" at distressed prices by issuing bonds at sub-4% interest-rates. ***The TLGP program essentially provides an opportunity for banks to achieve low "treasury-like" interest-rates (with FDIC's guarantee) for the next 3 ½ years.*** Is this enough support? The amount of debt that could be issued under this program's limits is estimated to be about $1.4 Trillion[3] – not insignificant. Goldman Sachs and Citigroup were reported to be ready to issue FDIC-Insured bonds as early as this coming week. As I write this note, however, Bloomberg is reporting that Citigroup, Treasury, and the Fed have spent the weekend discussing the Citi crisis and an announcement may be made before US markets open tomorrow. ***Some reports[4] indicate that they may announce a "Good Bank, Bad Bank" plan where distressed assets would be transferred to a government-supported investment vehicle thereby leaving a "good bank" without such assets. If this happens, it is clearly recognition that the original TARP strategy of asset purchases is necessary because markets want to know that banks are solvent, not just flush with liquidity.***

As long-term asset allocating investors, our investment decisions are based on investment horizons of 10 to 20 years or more. However, since many of us monitor global capital markets in real-time, it is not always easy to keep that perspective. As we mentioned in our September 24 client email, "If we have properly assessed the amount of overall equity risk appropriate for your situation, then current conditions do not warrant any particular transactional activity." We humans tend to over-weigh recent history as a projection of the future. As such, ***investor assessment of appropriate risk-taking two to three years ago may now appear over-stated in light of the 2007-2008 "bear market". In reality, this period serves as a reminder that we should weigh all available historical data when evaluating risk – not just the last 5, 10 or 15 years. Consistent with that history, we must also remember that equity markets have always recovered and appreciated significantly after periods of decline. The rebalancing process inherent with asset allocation is the prudent means of "buying low" and "selling high" over the long-term.***

[1] "Perspective, Policy Responses, and Investment Implications", November 17, 2008 (website)
[2] "Lessons from Freddie Mac and Fannie Mae Conservatorship", September 14, 2008 (website)
[3] "Technical Briefing on the Temporary Liquidity Guarantee Program" teleconference, October 14 2008, see http://www.fdic.gov/regulations/resources/tlgp/101408_am.html
[4] "Citi considers 'bad bank' plan", Financial Times, www.ft.com, November 23, 2008 8:37pm