

## **Fixed Income Carries Risk**

*By Jeffrey Kruske*

Historically, stocks have made lots of money for lots of people; they have also helped many investors lose their shirts. Risk-averse investors, especially those that felt the sting of the 2000-2003 bear market, sought refuge in fixed-income investments, such as bonds and money market funds. In recent months, however, those who consider those investments a safe harbor for their money have been unpleasantly surprised.

Most investors who are retired or nearing retirement should have a good portion of their assets in fixed-income investments. Many investors in this demographic invested in bonds and cash alternatives under the assumption that those investments would be conservative enough to preserve their retirement nest egg.

As some bond funds have demonstrated, however, fixed-income can be increasingly risky, especially when the true nature of the investments is not disclosed to the investor. For example, Morgan Keegan, a brokerage firm located in Jefferson City, sold its own bond funds to investors as conservative and safe investments.

However, Morgan Keegan began increasing its holdings in risky subprime mortgage-backed securities, and failed to inform investors of that important fact. Sadly, Morgan Keegan investors learned the hard way by watching many of their “safe” bond funds decline in value by more than 50 percent.

Other examples include investors who parked their money in what they were told were “cash equivalent” investments, such as Auction Rate Securities. Many Kansas City-area investors put large sums of cash in these investments, which were sold as liquid, safe, higher-yielding alternatives to money market funds.

One investor put the proceeds of the sale of a business in ARS; another deposited money earmarked for the purchase of a house. In February, these funds became illiquid because the auctions that supported these investments began to fail. In essence the market for these little-known securities collapsed, leaving local investors with no access to cash they needed.

One local brokerage firm involved in the ARS collapse, UBS Financial Services, offered its investors the opportunity to take out interest-bearing loans against their holdings to meet short-term investment needs. Those investors are now effectively forced to spend money to access their own cash.

What many investors were not told is that UBS and other firms may have known that the ARS auctions were failing, and chose not to notify their customers. In fact, UBS decided not to support any more auctions – another reason why these auctions failed and have not reopened.

Investors who purchased fixed-income investments based on the premise of safety and liquidity may have an unpleasant year ahead of them. The current credit crisis is now being felt by investors who relied on their advisors' recommendations. Unfortunately, many local investors, many of whom do not have a mortgage or a home, now own a share of the subprime debacle or, worse yet, have no access to their money.

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