From: Hines Courtney [Courtney.Hines@morgankeegan.com]
Sent: Wednesday, March 14, 2007 3:51 AM
To: Braden, Dixon; Metcalf, Barbara
Subject: RE: Could you comment on this?

We do hold 13% in sub-prime, HOWEVER…less than 1% (of the 13%) is unrated. Her statement is completely misleading and wrong. Now, we do hold non-rated securities, but in other sectors.

We do hold two line items from New Century, approximately a $3.4 million position. And this is the 2006 collateral that has caused problems in sub-prime. With that being said, New Century is one of the three largest issuers of sub-prime mortgages. For example, if we buy a pool of mortgages from Deutsche…there will be some New Century paper in there somewhere. And not to mention, a $3.4 million position in a portfolio that is 1.2 billion….I think the NAV will survive!!

Also, this time last year we held 30% in sub-prime mortgages. Jim foresaw this blowup and greatly cut our exposure to sub-prime.

Let me know if you have any questions.

Courtney Hines
Director of Marketing
Morgan Asset Management
901-374-7810

From: Braden, Dixon
Sent: Wednesday, March 14, 2007 7:06 AM
To: Hines, Courtney; Kelsoe, Jim
Subject: Could you comment on this?

I am sure we will get some calls on the RMK line regarding an article in the NYTimes talking about Mutual Funds and exposure to SubPrime loans. It specifically mentions your funds:

The Regions Morgan Keegan Select High Income Fund, for example, a $1.2 billion portfolio run by Morgan Keegan, a regional brokerage firm based in Memphis, held $159 million, or 13 percent of its portfolio, in unrated mortgage-backed securities, or those below investment grade. Among the issues in its portfolio at the end of the year: a $3.4 million holding in home equity loans underwritten by New Century in 2006.

Do we still have this type of exposure? What are your general feelings on this topic?

Thank you,
Dixon
Dixon Braden First Vice President
Morgan Keegan Equity Strategy Group
50 North Front Street 12th Floor
Memphis, TN 38103
901-529-5331
Fax: 901-579-4493
dixon.braden@morgankeegan.com

FULL ARTICLE---

March 14, 2007

Mutual Funds at Some Risk on Mortgages

By GRETCHEN MORGENSON

Mutual funds held mortgage-related debt securities issued by the subprime lenders New Century Financial, NovaStar Financial and others at the end of last year, indicating that everyday investors are among those who will probably be hurt by the turmoil that is tearing through the residential mortgage market.

As delinquencies among risky borrowers have risen, the stocks of companies that specialized in these loans have collapsed. The value of the residential mortgages they issued, which Wall Street packaged and sold to investors, has also dropped.

While it is relatively easy to identify those who owned shares in New Century — it closed at around 85 cents yesterday after the New York Stock Exchange suspended its listing — figuring out who holds the mortgage-related debt of such issuers is more difficult.

Regulatory filings show that mutual funds that specialize in generating high income have bought subprime mortgage securities as the market ballooned.

To be sure, with their holdings spread out among hundreds of issuing companies, mutual funds are considerably safer than more concentrated holdings. And some mutual funds may have limited their purchases of debt issued by subprime lenders to securities rated highly by credit rating agencies like Moody's Investors Service, Standard & Poor's and Fitch Ratings.

But the ills in the mortgage securities market are infecting even issues that carry higher ratings from those agencies. These securities have declined along with the broad market in recent days, although they have not fallen as far as lower-quality issues.

As prevailing interest rates have remained low, portfolio managers seeking income from their investments have had difficulties generating attractive yields. Pension funds with significant financial obligations to retirees took on more and more risk to generate income.

During the housing market boom, mortgages became a favored investment vehicle among these managers.

The Regions Morgan Keegan Select High Income Fund, for example, a $1.2 billion portfolio run by Morgan Keegan, a regional brokerage firm based in Memphis, held $159 million, or 13 percent of its portfolio, in unrated mortgage-backed securities, or those below investment grade. Among the issues in its portfolio at the end of the year: a $3.4 million holding in home equity loans underwritten by New Century in 2006.

The fund also held five securities worth $30.4 million issued by First Franklin, a subprime lender that was bought by Merrill Lynch for $1.3 billion last year.

Some 4.4 percent of the Regions Morgan Keegan Short Term Bond Fund, an $80 million fund, was in investment-grade-rated home equity loans — a $2.9 million stake — and another 11.3 percent of the portfolio, or $8.8 million, consisted of investment-grade mortgage securities.

Kathy Ridley, a Morgan Keegan spokeswoman, declined to comment on the funds' holdings, saying that it was the firm's policy not to discuss the stakes.

Legg Mason Partners Capital and Income Fund, a $3.4 billion fund, also owns home equity loans issued by subprime lenders. Some 1.1 percent of the portfolio consists of home equity loans, with $2.25 million issued by New Century; $3.6 million issued by NovaStar; and $2.7 million issued by Fremont General, the parent company of a lender who consented to a cease-and-desist order from the Federal Deposit Insurance Corporation a week ago. That order called for the company to stop "operating with a large volume of poor quality loans" and "engaging in unsatisfactory lending practices."

Mary Athridge, a Legg Mason spokeswoman, confirmed that its funds own some of the trusts issued by troubled lenders. But the firm is comfortable with the holdings, she said, because they are overcollateralized and very little of the loans are left outstanding.

Funds that are part of the American Skandia Trust also own mortgage securities issued by troubled lenders. The trust's American Century Strategic Balanced portfolio held mortgage securities issued by NovaStar and Accredited Home Lenders that were rated Aaa at the time and valued at just over $500 million. Of the fund's $175 million under management at the end of the year, 2.3 percent of it was in asset-backed securities including mortgages.

Officials at American Century could not be reached for comment last night.

Several American Skandia Trust portfolios managed by T. Rowe Price — a global bond fund and asset allocation fund — also showed stakes in New Century home equity loans at the end of 2006.

A T. Rowe Price spokesman said that managers with knowledge of these portfolios were not available last night.

A spokesman for Prudential Financial, which acquired American Skandia, was not able to confirm last night whether the funds still held the securities.

The Builders Fixed Income Fund, a mutual fund with $248 million under management that is overseen by Capital Mortgage Management in Manchester, Mo., has substantial mortgage stakes. Asset-backed securities, including those issued by mortgage lenders, made up 28.4 percent of the fund’s portfolio at year-end. It held two stakes worth $1.14 million in home equity loans underwritten by New Century.

Mike Stewart, chief compliance officer at the fund, said he was “not at liberty to say” if the New Century stake was still in the portfolio.