CHANDLER ASSET MANAGEMENT

April 2011

BOND MARKET REVIEW

A MONTHLY REVIEW OF FIXED INCOME MARKETS

WHAT'S INSIDE

Since 1988, Chandler Asset Management has specialized in the management of fixed income portfolios. Chandler's mission is to provide fully customizable, client-centered portfolio management that preserves principal, manages risk and generates income in our clients' portfolios.

MARKET SUMMARY

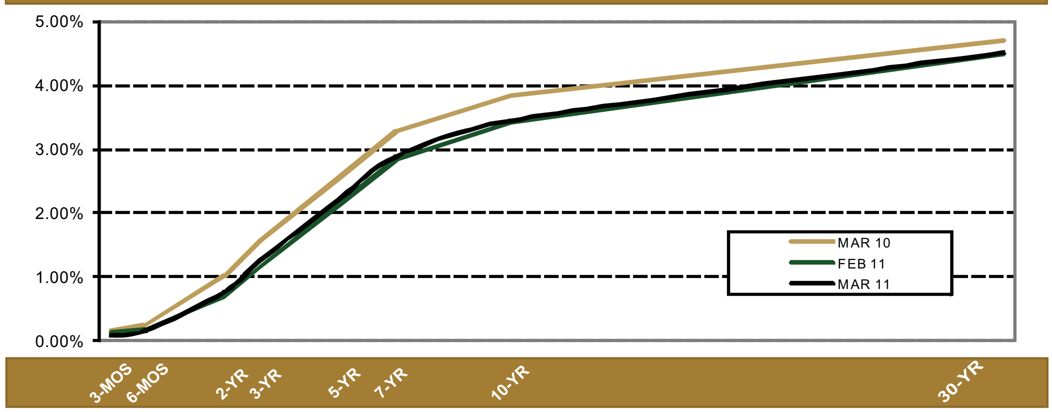
Treasury yields were modestly higher in March as market participants debated the impact of unrest in North Africa and the Middle East, higher oil prices, the Japanese disaster, and an eventual end to ultra-easy monetary policy.

Economic growth remains moderate, and employment has slowly begun to improve. The unemployment rate declined to 8.8% in March, and the economy added 216,000 new jobs. Measures of manufacturing activity have also been relatively robust. On the negative side of the ledger, the housing market remains stagnant, and inflation readings have begun to tick higher. The impact of higher oil prices and various geopolitical events on the US economy remains to be determined.

The Federal Reserve maintains its exceptionally easy monetary policy, and continues to purchase longer-dated Treasury securities in an effort to promote economic growth. The next Fed meeting is April 27, and market participants will be watching closely for signs of what the Fed will do following the completion of its asset purchase program (QE2) in June.

The Fed has also announced that they will begin holding press conferences four times each year immediately following the FOMC meeting. These press conferences are intended to provide greater clarity into the FOMC's assessment of economic conditions and are similar to those already held by many central banks around the world. The first press conference will follow the April 27 meeting.

TREASURY YIELDS MODESTLY HIGHER IN MARCH



Treasury yields ended the month slightly higher. The yield curve flattened slightly but remains steep.

YIELDS	3/31/11	2/28/11	CHANGE
3 Month	0.09	0.14	(0.05)
2 Year	0.78	0.69	0.09
3 Year	1.26	1.16	0.10
5 Year	2.22	2.14	0.08
7 Year	2.89	2.83	0.06
10 Year	3.45	3.41	0.04
30 Year	4.51	4.49	0.02

Consumer Prices

In February, the CPI showed that consumer prices increased 2.1% on a year-over-year basis. The year-over-year Core CPI (CPI less food and energy) increased at a 1.1% rate. Although some producer prices have begun to increase, prices on consumer goods are not expected to increase sharply in the months ahead. The Federal Reserve has noted that it is monitoring commodity price increases, but does not believe that they will flow through to higher consumer prices.

Retail Sales

In February, Retail Sales rose 8.9% on a year-over-year basis. Consumer spending has rebounded from the depths of the recession, and recent activity has been promising; however, activity is still far short of the heights of the previous economic expansion.

Labor Markets

The March employment report showed that the economy added 216,000 jobs, which was higher than expected. Meanwhile, the unemployment rate dropped to 8.8%. The only negative aspect of the report was that changes in average hourly earnings were slightly weaker than anticipated. Overall, this was a good employment report, which demonstrates that the labor market is slowly improving.

Housing Starts

Single-family housing declined 11.8% in February to 375,000, the lowest level since March 2009. Permits for new housing starts also declined. This report indicates that the housing market remains relatively weak.

Credit Spreads Mixed

CREDIT SPREADS	Spread to Treasuries (%)	One Month Ago (%)	Change
3-month top-rated commercial paper	0.12	0.12	0.00
2-year AA corporate note	0.33	0.31	0.02
5-year AA corporate note	0.54	0.52	0.02
5-year Agency note	0.34	0.32	0.02

Source: Bloomberg

Data as of 3/31/2011

Mixed Economic Data

ECONOMIC INDICATOR	Current Release	Prior Release	One Year Ago
Trade Balance	(46.3) $Bln JAN 11	(40.2) $Bln DEC 10	(34.6) $Bln JAN 10
GDP	3.1% DEC 10	2.6% SEP 10	5.0% DEC 09
Unemployment Rate	8.8% MAR 11	8.9% FEB 11	9.7% MAR 10
Prime Rate	3.25% MAR 11	3.25% FEB 11	3.25% MAR 10
CRB Index	359.43 MAR 11	352.58 FEB 11	273.34 MAR 10
Oil (West Texas Int.)	$106.72 MAR 11	$96.97 FEB 11	$83.76 MAR 10
Consumer Price Index (y/o/y)	2.1% FEB 11	1.6% JAN 11	2.1% FEB 10
Producer Price Index (y/o/y)	5.6% FEB 11	3.6% JAN 11	4.2% FEB 10
Dollar / EURO	1.42 MAR 11	1.38 FEB 11	1.35 MAR 10

Source: Bloomberg

New Portfolio Manager Joins Chandler

I am very pleased to announce that William Dennehy II has recently joined Chandler Asset Management as Vice President and Portfolio Manager. Bill brings nearly 20 years of finance industry experience to our firm, including most recently, over ten years as a portfolio manager and quantitative analyst at Northern Trust in Chicago. At Northern, he managed investment grade fixed income portfolios, including trade execution, and he maintained frequent contact with that firm's clients. He also served as a voting member of the Committee that established Northern's long-term credit outlook. Bill received his B.S. in business administration, with a concentration in finance, from California State University at Chico. He holds a Series 3 Securities License, has earned the designation of Chartered Financial Analyst, and is a member of the CFA Institute.

Mr Dennehy's duties at Chandler will include investing our clients' portfolios as a member of the portfolio management team, as well as quantitative and qualitative research and client contact. I hope that many of you will have a chance to meet Bill within the upcoming weeks.

If you would like to know more about Bill, or if you have any questions or comments, please feel free to call me directly.

Kay Chandler

Kay Chandler
President

An Update on Recent International Events

Although the first quarter has just ended, 2011 has already seen a number of important developments across the international landscape. The recent Japanese earthquake, regime change in several Arab countries, continued sovereign debt concerns in Europe, and UN military action in Libya, have dominated recent headlines. Here is a look at recent developments, and attempt to analyze their impact on the economy and financial markets.

Japan

The recent earthquake, tsunami, and nuclear crisis in Japan is an incredible tragedy, and our thoughts and prayers go out to the victims and survivors. Rebuilding the affected areas will take many years. From a purely economic perspective though, the impact in the United States and around the globe is likely to be muted, as long as the nuclear situation does not meaningfully deteriorate. While the Japanese economy is likely to contract in the short term, natural disasters generally do not cause prolonged recessions; Japan's economy is likely to spring back relatively quickly. Furthermore, Japan has been a relatively small contributor to global growth in recent years, and even if the country falls into a mild recession, events elsewhere are likely to play a larger role in determining US and global economic growth.

From a financial market perspective, Japan is the second largest foreign holder of US Treasury securities, which has prompted some concern that they might sell these in order to use the funds to rebuild the country. Such fears are likely unfounded; following the 1995 Kobe earthquake in Japan, large scale sales of US assets did not occur, and given the strength of the Yen, Japanese institutions are likely to view the sale of US dollar assets as a relatively unattractive option (this is because after selling the US $ assets, the Japanese would have to convert the proceeds back into Yen, which is unappealing given recent Yen strength.) Even if the Japanese do ultimately liquidate some of their holdings of US Treasuries, that market is large enough, and liquid enough, to withstand this without too much of an effect.

Europe

The European sovereign debt concerns that began in the spring of 2010 remain a concern for the marketplace. Very high budget deficits and unmanageable debt levels have created a dangerous situation for some European countries, particularly Greece, Ireland, and Portugal. Furthermore, political disagreement among European nations has given financial market participants doubt as to the ability of the European Union to deal with the problems in an effective manner. On the positive side, Greece, Ireland, and Portugal are all relatively small countries, and are unlikely to have a large impact on the global economy. Italy and Spain, both much larger countries, have also been a source of concern. However, market participants have recently begun to differentiate these two countries from the other three. If either Italy or Spain truly experiences a debt crisis, the impact on the US and global economy could be significant.

From a financial market perspective, the most likely effect of the European situation is that each time concerns flare up it is likely that US Treasury prices will rally in a "flight to quality." As such, the situation in Europe might help to contribute to an environment in which US interest rates stay low for a long period of time.

> Events to date should have a relatively muted impact on global economic growth, as long as the turmoil does not spread to Saudi Arabia, Iran, or other large oil producing countries.

The Middle East & North Africa (MENA)

Recent popular uprisings in the Middle East and North Africa (MENA) region have prompted a sharp rise in the price of oil. These events continue to unfold, and depending on their ultimate resolution, are likely to have a more significant impact on the economy and financial markets than events in either Japan or Europe.

Despite their important geopolitical implications, events to date should have a relatively muted impact on global economic growth, as long as the turmoil does not spread to Saudi Arabia, Iran, or other large oil producing countries. If this were to occur, all bets are off, and the likely resulting oil price spike could very well tip the US (and the world) back into recession. If this were to occur, Treasuries would likely rally, with yields falling, and stocks and other risky assets would likely decline.

Further turmoil in MENA is not a base-case scenario, but the possibility exists and should remain on every investor's radar.

Conclusion

In an increasingly interconnected world, global events can have a profound impact on the US economy and financial markets. While the US economy appears to have gained some momentum, the recovery remains fragile and international events still have the power to derail the recovery. Investors would do well to monitor events closely, paying particular attention to the unrest in the Arab world and the price of oil.

Brian Perry, CFA
Portfolio Manager & Investment Strategist