CHANDLER ASSET MANAGEMENT

May 2015

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.

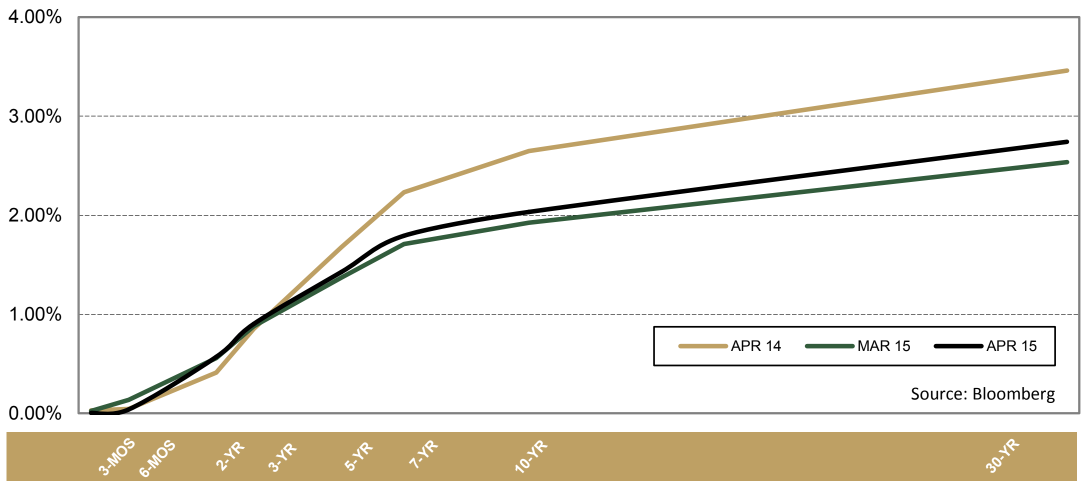
Market Summary

Nonfarm payrolls rose by 223,000 in April, in line with expectations. March and February payrolls were revised down by a net 39,000, bringing the trailing three month moving average to a somewhat lackluster pace of just 191,300. The six month moving average in April was 254,500. The unemployment rate declined to 5.4% in April from 5.5% in March. The labor participation rate edged up slightly to 62.8% in April from 62.7% in March, but it remains near its historical low. Wages rose just 0.1% in April. Overall, the pace of job growth has recently waned and there is still excess slack in the labor market. Meanwhile, manufacturing trends remain sluggish, housing data has been uneven, and consumer spending trends have underwhelmed. On the whole, economic data has been soft, but we believe some of the factors that held back growth in recent months (such as weather and West Coast port delays) may be temporary and that growth is likely to pick up modestly in the second half of this year.

The Federal Open Market Committee (FOMC) left policy rates unchanged at its April 28-29 meeting, without any dissenting votes. The Committee noted that economic growth slowed during the winter months, but attributed part of the weakness to "transitory factors." The policy statement pointed to ongoing slack in the labor market, lower growth in household spending, a recent decline in business fixed investment spending, a slow housing sector recovery, and a decline in exports. Meanwhile, inflation measures remain low. The FOMC expects to see further improvement in the labor market and needs to be confident inflation will move back toward its 2% target, before they raise rates. The Committee isn't providing specific calendar guidance about the timing of the first rate hike, and continues to emphasize that monetary policy changes will be data-dependent. Though a June rate hike is still a possibility, we believe it is unlikely. Instead, we believe the first rate hike will be later in the second half of this year. In the meantime, ongoing uncertainty about the timing of the first fed funds rate hike will likely continue to fuel financial market volatility.

The yield on the two-year Treasury note rose slightly in April. The longer end of the yield curve steepened during the month while shorter rates declined.

THE YIELD CURVE STEEPENED IN APRIL



The yield curve steepened in April. The 'flight to quality' fueled by concerns of a potential sovereign bond default in Greece has recently abated (to a degree), removing some of the downward pressure on long-term U.S. Treasury rates. Meanwhile, domestic economic data has softened, and the timing of the first fed funds rate hike remains unclear. The European Central Bank continues to execute its bond-buying program and other global central banks are pursuing highly accommodative monetary policies.

TREASURY YIELDS	4/30/2015	3/31/2015	CHANGE
3 Month	0.00	0.02	(0.02)
2 Year	0.57	0.56	0.01
3 Year	0.90	0.88	0.02
5 Year	1.43	1.37	0.06
7 Year	1.79	1.71	0.08
10 Year	2.03	1.92	0.11
30 Year	2.74	2.54	0.20

Source: Bloomberg

Economic Roundup

Consumer Prices

In March, overall Consumer Price Index (CPI) inflation was -0.1% on a year-over-year basis after being flat in February. Headline inflation has fallen sharply in recent months due to a precipitous decline in energy prices. The year-over-year Core CPI (CPI less food and energy) increased slightly to 1.8% in March from 1.7% in February.

Retail Sales

In March, retail sales rose 1.3% on a year-over-year basis, following a 1.9% gain in February. On a month-over-month basis, retail sales rose just 0.9% in March (below the consensus forecast of 1.1%). Retail sales have been weaker than expected over the past few months. Unfavorable weather may be a contributing factor.

Labor Market

Nonfarm payrolls rose by 223,000 in April, in line with the consensus forecast. Private payrolls rose by 213,000 and government jobs increased by 10,000. March and February payrolls were revised down by a net 39,000, bringing the trailing three month moving average to a somewhat lackluster pace of just 191,300. The six month moving average in April was 254,500. The unemployment rate declined to 5.4% in April from 5.5% in March. A broader measure of unemployment, the U-6, which includes those whom are marginally attached to the labor force and employed part time for economic reasons, declined to 10.8% from 10.9%. The labor participation rate edged up slightly to 62.8% in April from 62.7% in March, but it remains near its historical low. Wages rose 0.1% in April (slightly below expectations), and were up 2.2% in a year-over-year basis.

Housing Starts

Overall, housing starts rose just 2.0% in March after falling 15.3% in February (the consensus forecast called for a more substantial rebound in March). Housing starts in the Northeast and Midwest experienced healthy gains in March (likely a weather-related rebound) but starts in the South and West declined. Permits were also weaker than expected in March, falling 5.7%. Single-family housing starts rose 4.4% in March, while multi-family using starts fell 7.1%.

Credit Spreads Tightened in April

CREDIT SPREADS	Spread to Treasuries (%)	One Month Ago (%)	Change
3-month top-rated commercial paper	0.22	0.16	0.06
2-year A corporate note	0.47	0.50	(0.03)
5-year A corporate note	0.68	0.64	0.04
5-year Agency note	0.18	0.08	0.10

Source: Bloomberg *Data as of 4/30/2015*

Economic Data Has Softened But Remains Indicative of Modest Growth

ECONOMIC INDICATOR	Current Release	Prior Release	One Year Ago
Trade Balance	(51.4) $Bln MAR 15	(35.9) $Bln FEB 15	(42.8) $Bln MAR 14
GDP	0.2% MAR 15	2.2% DEC 14	(2.1)% MAR 14
Unemployment Rate	5.4% APR 15	5.5% MAR 15	6.2% APR 14
Prime Rate	3.25% APR 15	3.25% MAR 15	3.25% APR 14
CRB Index	229.49 APR 15	211.86 MAR 15	309.53 APR 14
Oil (West Texas Int.)	$59.63 APR 15	$47.60 MAR 15	$99.74 FEB 14
Consumer Price Index (y/o/y)	(0.1)% MAR 15	0.0% FEB 15	1.5% MAR 14
Producer Price Index (y/o/y)	(3.2)% MAR 15	(3.4)% FEB 15	1.8% MAR 14
Dollar/EURO	1.12 APR 15	1.07 MAR 15	1.39 APR 14

Source: Bloomberg