

BOND MARKET REVIEW

A MONTHLY REVIEW OF
FIXED INCOME MARKETS



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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.

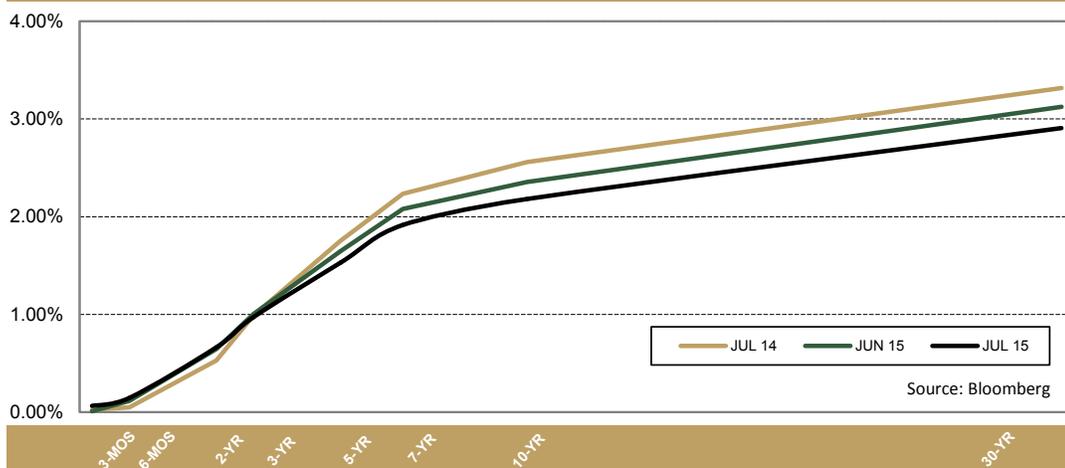
Market Summary

Momentum is building toward a potential fed funds rate hike at the September 16-17 Federal Open Market Committee (FOMC) meeting. Inflation is still running below target, but labor market conditions are likely at or near a level consistent with monetary policy normalization. Over the past three months, payrolls have increased by an average of 235,000 per month, compared to the trailing six-month average of 213,000. In July, the unemployment rate was 5.3%. The PCE price index was up just 0.3% on a year-over-year basis in June, while the Core PCE price index was up just 1.3%. Though inflation remains below the Fed's 2.0% target, multiple Fed Presidents have recently made public comments indicating they are moving closer toward the lift-off date for monetary policy normalization. We believe the first fed funds rate hike will occur before the end of this year. There are three remaining FOMC meetings scheduled this year (September 16-17, October 27-28, and December 15-16).

The financial markets continue to experience volatility, fueled largely by the uncertain outlook for Fed monetary policy and mixed economic data. While employment trends have generally been favorable, consumer spending trends have been lackluster and manufacturing data remains soft. Housing data has been somewhat volatile but the outlook remains constructive. Overall, we believe the economy continues to grow at a slow pace. According to the advance estimate, real annualized GDP growth was 2.3% in the second quarter of 2015, following growth of 0.6% in the first quarter. We are expecting GDP growth of about 2.5%-3.0% in the second half of 2015.

Interest rate volatility remains elevated as global sovereign debt markets continue to be influenced by divergent central bank policies. The Treasury yield curve flattened modestly in July, with short-term rates up slightly and longer-term rates down about 20 basis points. We believe this flattening trend reflects market participants' expectations for a fed funds rate hike before the end of the year.

THE YIELD CURVE FLATTENED IN JULY



The yield curve flattened in July. Market participants are anticipating a potential fed funds rate hike before the end of this year, putting upward pressure on shorter-term rates. Concerns about Greece and China, as well as technical supply factors have also influenced global interest rates. Meanwhile, divergent global central bank monetary policies have been a source of market volatility as the Federal Reserve remains the only major central bank contemplating a tightening of monetary policy over an intermediate time horizon. The European Central Bank continues to execute its bond-buying program and other global central banks are pursuing highly accommodative monetary policies.

TREASURY YIELDS	7/31/2015	6/30/2015	CHANGE
3 Month	0.06	0.01	0.05
2 Year	0.66	0.65	0.01
3 Year	0.97	1.01	(0.04)
5 Year	1.53	1.65	(0.12)
7 Year	1.92	2.08	(0.16)
10 Year	2.18	2.35	(0.17)
30 Year	2.91	3.12	(0.21)

Source: Bloomberg

Economic Roundup

Consumer Prices

In June, overall Consumer Price Index (CPI) inflation was up 0.1% on a year-over-year basis after being flat in May. Headline inflation remains low, following a precipitous decline in energy prices at the end of last year. The year-over-year Core CPI (CPI less food and energy) rose slightly to 1.8% in June from 1.7% in May. Pricing pressures (excluding food and energy) at the consumer and producer levels have firmed slightly, but inflation remains below the Fed's target.

Retail Sales

Retail sales were stronger than expected in July, up 0.6% on a month-over-month basis. On a year-over-year basis, retail sales rose 2.4% in the month, following a 1.8% year-over-year gain in June. Ongoing improvement in the labor market, along with low gas prices, should have a positive influence on consumer discretionary spending. In recent months consumer spending trends have been somewhat lackluster but the July gain may signal an improving trend.

Labor Market

Nonfarm payrolls rose by 215,000 in July, slightly below the consensus forecast of 225,000. However, May and June payrolls were revised upward by a total of 14,000. The unemployment rate was unchanged at 5.3%, and the participation rate held steady at a low level of 62.6%. A broader measure of unemployment called the U-6, which includes those whom are marginally attached to the labor force and employed part time for economic reasons, declined to 10.4% from 10.5%. Wages rose 0.2% on a month-over-month basis in July, and rose to 2.1% from 2.0% in June on a year-over-year basis. Over the past three months, payrolls have increased by an average of 235,000 per month, compared to the trailing six-month average of 213,000.

Housing Starts

Housing starts rose 9.8% in June following a 10.2% decline in May. The strength in June was driven by a 29.4% increase in multi-family starts. Single-family housing starts fell 0.9% in June. Permits were much stronger than expected in June, up 7.4%, following a 9.6% increase in May. Overall, activity in the housing sector has recently picked up.

Credit Spreads Widened in July

CREDIT SPREADS	Spread to Treasuries (%)	One Month Ago (%)	Change
3-month top-rated commercial paper	0.17	0.15	0.02
2-year A corporate note	0.64	0.63	0.01
5-year A corporate note	0.90	0.82	0.08
5-year Agency note	0.21	0.17	0.04

Source: Bloomberg

Data as of 7/31/2015

Economic Data Is Mixed

ECONOMIC INDICATOR	Current Release	Prior Release	One Year Ago
Trade Balance	(43.8) \$Bln JUN 15	(40.9) \$Bln MAY 15	(42.4) \$Bln JUN 14
GDP	2.3% JUN 15	0.6% MAR 15	4.6% JUN 14
Unemployment Rate	5.3% JUL 15	5.3% JUN 15	6.2% JUL 14
Prime Rate	3.25% JUL 15	3.25% JUN 15	3.25% JUL 14
CRB Index	202.57 JUL 15	227.17 JUN 15	294.43 JUL 14
Oil (West Texas Int.)	\$47.12 JUL 15	\$59.47 JUN 15	\$98.17 JUL 14
Consumer Price Index (y/o/y)	0.1% JUN 15	0.0% MAY 15	2.1% JUN 14
Producer Price Index (y/o/y)	(2.6)% JUN 15	(3.0)% MAY 15	2.8% JUN 14
Dollar/EURO	1.10 JUL 15	1.11 JUN 15	1.34 JUL 14

Source: Bloomberg

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