CHANDLER ASSET MANAGEMENT

April 2009

Bond Market Review

A monthly review of fixed income markets

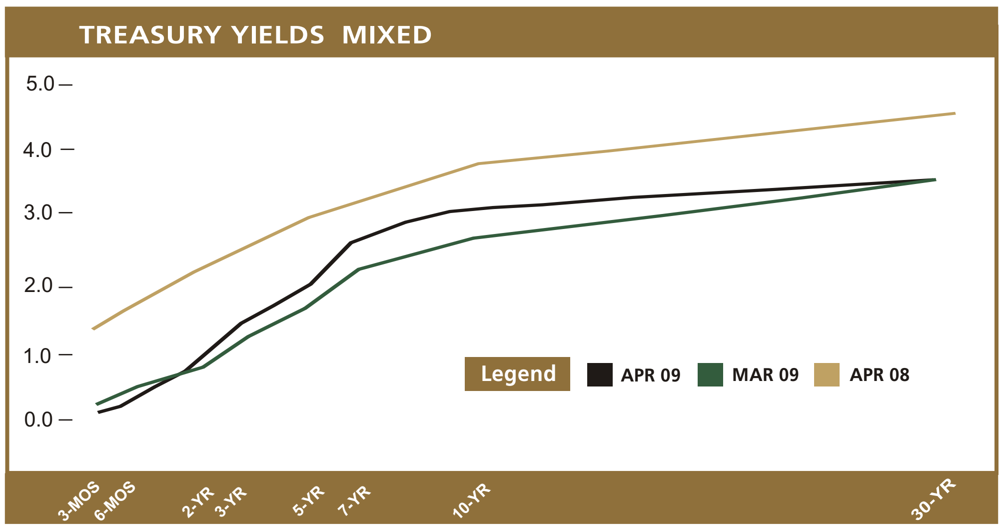
What's Inside

Market Summary

The US economy has been in recession since December 2007 and the economic decline has accelerated following the financial market turmoil that began in September 2008. The economy has now lost 5.7 million jobs since the start of the recession. The April Non-Farm Payroll number showed a decrease of 539,000 jobs and the unemployment rate increased to 8.9%. There were continued tentative signs of stabilization in consumer spending, housing, and manufacturing, although any stabilization is occurring at very low levels. First Quarter 2009 GDP declined at an annualized pace of -6.1%. Forecasts call for continued declines in economic activity, but there is hope that the first quarter of 2009 will ultimately represent the low point of the economic cycle.

Longer-term Treasury bond yields were much higher in April as investors questioned the Federal Reserve's ability to keep longer-term rates at low levels for an extended period of time. Investors also sold Treasuries in reaction to signs of economic stabilization, reduced financial market volatility, very strong equity market performance, and increasing hope that the health of the banking system is improving.

The next scheduled FOMC meeting is on June 24th.



Short-term Treasury yields were slightly lower in April but longer rates rose sharply as market participants debated the impact of increased levels of Treasury bond issuance and the ongoing global recession. The yield curve retained its normal shape as long-term interest rates are higher than short-term rates.

YIELDS	4/30/09	3/31/09	Change
3 Month	0.12	0.20	(0.08)
2 Year	0.92	0.80	0.12
3 Year	1.36	1.13	0.23
5 Year	2.02	1.68	0.34
7 Year	2.69	2.27	0.42
10 Year	3.12	2.69	0.43
30 Year	4.04	3.56	0.48

YIELD SPREADS	4/30/09	3/31/09	Change
5yr - 2yr T-Note	1.10	0.88	0.22
10yr - 2yr T-Note	2.20	1.89	0.31

Source: Bloomberg

Total Return vs. Yield Measures

There are two measures that investors commonly employ in order to track portfolio performance. These two measures are portfolio yield and total return. While yield might seem simpler and is easier to understand, in most circumstances total return is a more accurate measure of a portfolio's performance.

Generally speaking, portfolio yield measurement attempts to project the cash flow that a given portfolio will generate during a specific period of time, usually one year. For instance, imagine that an investor holds a portfolio of bonds that they have purchased for ten million dollars. If this portfolio generates five hundred thousand dollars of revenue each year, it can be said that the portfolio's yield is five percent. If an investor is attempting to generate budget projections, yield is a useful measure of portfolio return. By focusing upon the income that will be generated by the portfolio, the investor can ascertain whether or not the portfolio will generate sufficient revenue to satisfy any liabilities that are coming due.

Total return includes the portfolio's yield but goes further. In addition to yield, total return measures the gains or losses in the value of the portfolio over a given time period. Total return incorporates all cash flows from investment activities and asks the question: what was the value of the portfolio at the beginning of the measurement period and what is the value of the account at the end of the period? The difference between these two measures is the portfolio performance or total return for the period. In order to normalize these figures, portfolio return is often converted into a percentage and then annualized.

There are several reasons why total return is often a superior measure of portfolio performance than portfolio yield. The prices of most securities do not remain constant at the investor's purchase price but instead fluctuate on an ongoing basis. Yield measurement does not take these price fluctuations into account in its return calculations. If the investor needs to liquidate some or all of the portfolio, whether for reasons expected or unforeseen, the market may no longer value those securities at the same price that the investor paid for them. The price may have increased, but it just as easily could have decreased, leaving the investor with an unexpected loss.

Additionally, yields in the market place move up and down on a regular basis due to a variety of factors such as supply and demand or economic growth. An investor measuring their portfolio return based solely upon yield may find that when their securities mature and they need to reinvest the money, market yields may have declined, forcing them to reinvest at lower yields. In a worst case scenario, the new yield may not be sufficient to meet future obligations.

Another benefit of using total return measurement is that it provides for a better method of evaluating a portfolio's performance. When measuring yield it is often difficult to determine whether or not portfolio performance was "good." Is a 4% yield "good?" What about 8%? What should these yields be compared to in order to determine relative performance?

In contrast to yield, total return is generally measured against a benchmark. A benchmark represents an index whose risk characteristics match the investor's risk tolerance and return requirements. On a regular basis, the performance of the portfolio can be compared to the performance of the benchmark thereby providing a reasonable manner in which to evaluate the portfolio's overall performance. Since this benchmark fits the investor's risk tolerance profile, performance versus a benchmark also provides a good measure of how a portfolio is performing on a risk adjusted basis. Total return provides a useful quantitative evaluation of how well the investment program is meeting the investor's objectives, and serves as a basis for understanding steps that could be taken to improve investment decision-making.

One final problem with using yield measurements is that many investors that do so tend to neglect capital appreciation possibilities. In other words, by focusing upon yield, an investor may neglect to conduct portfolio transactions that could benefit the overall portfolio and increase its total value.

This opportunity cost can be confusing to many people. They might respond that yield is "real" and that they "can't spend total return." While it is true that paper profits in a portfolio can not be spent in the same way that portfolio income can, that does not mean that price appreciation can not be harvested. Generating a greater total rate of return will either facilitate greater income by harvesting portfolio gains or allow for the same level of income while increasing the size of the overall portfolio. When considering portfolio returns, an investor should ask themselves how many retirees' pensions could the portfolio fund, how many capital projects could the portfolio finance, how many wonderful vacations could an investor take with the portfolio's proceeds? Thinking about the tangible benefits that portfolio growth can confer should help an investor to move beyond an abstract view of total return and instead begin to consider the added benefits that they can receive if they are able to increase the compound rate of growth on their account.

Brian Perry, Vice President, Investment Strategist

Consumer Prices

In March, the CPI showed that consumer prices decreased 0.4% on a year over year basis. The year-over-year Core CPI (CPI less food and energy) was unchanged at a 1.8% y-o-y rate. Inflation has significantly moderated in recent months as lower energy prices and slowing economic growth have resulted in a slower pace of price increases.

Labor Markets

The April non-farm payroll employment report showed a decrease of 539,000 jobs and the unemployment rate increased to 8.9%. The payroll data reflected the seventeenth consecutive month of negative job growth. Since the start of the recession, the economy has lost more than 5.7 million jobs. April's employment report showed that the rate of deterioration in the labor markets is slowing as the labor markets remain weak.

Retail Sales

In March, Retail Sales declined at a year-over-year rate of -9.6%, worse than February's -8.0% annual rate of decline. Recently, consumers have broadly slowed their spending in reaction to financial market turmoil, a general tightening of credit standards, job loss worries, and the housing market contraction. Retail spending is expected to remain weak in the months ahead.

Housing starts

Single-family housing starts were unchanged in March at a 358,000 annual pace. Single-family housing starts seem to have stopped their most recent decline over the last few months.

Credit Spreads Wider

CREDIT SPREADS	Spread to Treasuries (%)	One Month Ago (%)	Change
3-month top-rated commercial paper	0.41	0.54	(0.13)
2-year AA corporate note	1.33	1.74	(0.41)
5-year AA corporate note	1.54	1.91	(0.37)
5-year Agency note	0.60	0.85	(0.25)

Source: Bloomberg *Data as of 4/30/09*

Mixed Economic Data

ECONOMIC INDICATOR	Current Release	Prior Release	One Year Ago
Trade Balance	(25.97) $Bln FEB 09	(36.20) $Bln JAN 09	(61.88) $Bln FEB 08
GDP	(6.10%) MAR 09	(6.3%) DEC 08	0.90% MAR 08
Unemployment Rate	8.90% APR 09	8.50% MAR 09	5.00% APR 08
Prime Rate	3.25% APR 09	3.25% MAR 09	5.00% APR 08
CRB Index	222.39 APR 09	220.40 MAR 09	409.27 APR 08
Oil (West Texas Int.)	$51.12 APR 09	$49.66 MAR 09	$113.46 APR 08
Consumer Price Index (y/o/y)	(0.4%) MAR 09	0.2% FEB 09	4.0% MAR 08
Producer Price Index (y/o/y)	(3.5%) MAR 09	(1.3%) FEB 09	6.7% MAR 08
Dollar / EURO	1.32 APR 09	1.33 MAR 09	1.56 APR 08

Source: Bloomberg

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