INVESTMENT COMMENTARY

2015 started with a spectacular, though not unexpected, nearly 12% decline of the Euro. Apparently, Mario Draghi decided that he needed to outdo both Chairman Berkanke and Yellen combined, as he announced a massive stimulus of over 1 trillion of purchases of Euro denominated assets. What seemed obvious to many, now became evident to all when the Euro joined the elite of currencies with banana republic policies, where a country issues debt that is promptly purchased by the central bank of that same country. In this way, modern central bankers have succeeded where the medieval alchemists seeking the philosopher's stone had failed. Instead of promoting societal wealth and economic growth via productivity increases and technological advances, the modern day alchemists believe that they have found their Magnum Opus. Their simple recipe for economic growth is based on how many trillions of their assets central banks will purchase and on how long interest rates will be kept at zero percent. In this theory, growth will be created out of thin air and capital will not be misallocated, which sounds wonderful, because markets clearly enjoy quick and easy outsized returns! Just look at the 18% local return of the Euro STOXX 50 in the 1st quarter of 2015.

Traditional economic theory teaches that healthy competition for limited amounts of capital promotes innovation and long-term economic growth. However, today's global economic strategy has become a game of "just blindly follow the central banker" and modern finance has morphed into the equivalent of the "all you can eat buffet" form of investing. Transforming our economic system from selective capitalism to an all-you-can-eat form of investing can only be unhealthy in the long term; however, it's still too early to fully know the long-term effects on prosperity created by this "buffet-style" economic metabolic system hosted by our central bankers.

First quarter events included a modest stabilization of oil prices, fourth quarter GDP was revised down to 2.2%, the official reading of unemployment came down to 5.5%, durable goods and retail sales lagged expectations, Greece vacillated day-to-day between exiting the Euro and remaining a solid member of the Union, and, of course, the Federal Reserve will be patient in their efforts to raise rates! When countries attempt to devalue their currency, each country is caught in a vicious circle of easing and there is no other option but to be patient until events dictate another course of action. The doomsday scenario that never came to be, not only discredited a lot of their authors, but, more importantly, gave their opponents a greater sense of security in pursuing the policies the Cassandras were denouncing. And as always, when vigilance runs low, it is then that the unexpected happens. And after it happens, it then appears so obvious that many wonder how it was missed. The financial crisis of 2008 is a prime example. But, as always, this time is different…until it is not.

For the second quarter of 2015 our strategy remains similar to the first quarter's strategy. Until we move away from Fed rhetoric and promises of Fed actions, which we believe is not close to happening yet, we believe that our current positioning will continue to add value to our portfolios, while maintaining the risk of our portfolios at acceptable levels.

The duration of our portfolios remains close to their respective benchmarks, and our yield curve positioning has a more barbelled structure. Global uncertainties will provide support to the long end of the yield curve, and valuations on a relative basis strongly favor longer maturity US treasuries relative to other foreign government bonds.

Very selective credit overweight continues to be the primary theme of adding value during the 2nd quarter. We maintain our significant overweight in industrial bonds, which provide our portfolios with additional yield. We have a neutral allocation to financials, as we believe that the spreads offered by the sector barely compensate for the sector volatility. Following our recent increased allocation to agency MBS, the sector outperformed, and valuations are now in a fairly valued range.

We continue to maintain our energy sector holdings. Our emphasis within the energy sector has been on companies that can not only withstand years of reduced oil prices, but that have also shown the commitment to maintain their ratings and the willingness to reduce leverage, and as such we are comfortable holding them longer term and we believe they will add value to our portfolios.

Evangelos Karagiannis
Managing Director,
Senior Portfolio Manager

KEY RATES

	3/31/15	12/31/14	3/31/14
Fed Funds Target Rate	**0-0.25%**	**0-0.25%**	**0-0.25%**
3 Month LIBOR	**0.27**	**0.26**	**0.23**
On-the-run Treasuries:			
3 Months	**0.02**	**0.04**	**0.03**
6 Months	**0.14**	**0.12**	**0.06**
2 Years	**0.56**	**0.67**	**0.42**
5 Years	**1.37**	**1.65**	**1.72**
10 Years	**1.92**	**2.17**	**2.72**
30 Years	**2.54**	**2.75**	**3.56**

Source: Bloomberg

KEY ECONOMIC INDICATORS

as of	3/31/15	3/31/14
U.S. $ (DXY)	**98.36**	**80.10**
Oil	**47.60**	**101.58**
Gold	**1183.68**	**1284.01**
CRB	**211.86**	**304.67**
GDP	**2.2**	**2.6**
CPI	**0.0**	**1.1**
Core (Ex - Food & Energy)	**1.4**	**1.1**
Unemployment Rate	**5.5**	**6.7**
Consumer Confidence	**101.30**	**82.30**
S&P/Case-Shiller – Comp-20	**4.56**	**13.24**

Source: Bloomberg

INDEX RETURNS

	1Q'15	YTD	1-Year
Barclays –			
Universal	**1.73%**	**1.73%**	**5.33%**
Aggregate	**1.61**	**1.61**	**5.72**
Aggregate ex-credit	**1.38**	**1.38**	**5.30**
Gov-Credit	**1.84**	**1.84**	**5.86**
Int. Gov-Credit	**1.45**	**1.45**	**3.58**
Corporate	**2.32**	**2.32**	**6.81**
Treasury only	**1.64**	**1.64**	**5.36**
1-3 year Gov	**0.54**	**0.54**	**1.04**
BofA Merrill – 1-yr T-Note	**0.11**	**0.11**	**0.21**
High Yield	**2.52**	**2.52**	**2.00**
International Debt	**-4.63**	**-4.63**	**-10.08**
Emerging Markets Debt	**2.30**	**2.30**	**4.23**
S&P 500	**0.95**	**0.95**	**12.72**
DJIA	**0.33**	**0.33**	**10.57**
NASDAQ	**2.63**	**2.63**	**22.03**
EAFE AWI	**5.04**	**5.04**	**-0.30**

Source: Bloomberg & Barclays

SECTOR RETURNS

1Q'15	Total Return	Excess Return
U.S. Treasuries	**1.64%**	**0.00%**
Government-related U.S. Agency	**1.44**	**-0.11**
Government-related Credit	**1.59**	**-0.21**
Corporate	**2.32**	**0.27**
Corporate Financials	**1.99**	**0.30**
Corporate Industrials	**2.47**	**0.30**
Corporate Utilities	**2.50**	**-0.04**
Corporate AAA-rated	**2.18**	**-0.20**
Corporate AA-rated	**2.03**	**0.09**
Corporate A-rated	**2.21**	**0.23**
Corporate BBB-rated	**2.49**	**0.36**
Corporate High-Yield	**2.52**	**1.09**
Mortgage-backed Securities-FR	**1.06**	**-0.51**
Mortgage-backed Securities-Hybrid	**0.85**	**0.13**
CMBS	**1.77**	**0.37**
ABS	**0.90**	**0.14**

Source: Barclays

Pacific Income Advisers, Inc. (PIA) is an autonomous investment management firm registered under the Investment Advisers Act of 1940. PIA manages a variety of fixed income, equity, and balanced assets for primarily United States clients.

BENCHMARK DESCRIPTION

Barclays U.S. Universal Index represents the union of the U.S. Aggregate Index, U.S. Corporate High-Yield Index, Investment-Grade 144A Index, Eurodollar Index, U.S. Emerging Markets Index, and the non-ERISA eligible portion of the CMBS Index. The index covers USD-denominated, taxable bonds that are rated either investment-grade or below investment-grade. Some U.S. Universal Index constituents may be eligible for one or more of its contributing subcomponents that are not mutually exclusive. These securities are not double-counted in the index. You can not invest directly in an index.

Barclays U.S. Aggregate Bond Index is an unmanaged index that covers the investment grade fixed rate bond market with index components for government and corporate securities, mortgage pass-through securities, and asset-backed securities. The issues must be rated investment grade, be publicly traded, and meet certain maturity and issue size requirements. You can not invest directly in an index.

Barclays U.S. Aggregate Ex-Credit Index (LB Agg (Ex-Credit)) The index covers the U.S. investment grade fixed rate bond market, with index components for government, mortgage pass-through securities, and asset-backed securities. These major sectors are subdivided into more specific indices that are calculated and reported on a regular basis. You can not invest directly in an index.

Barclays U.S. Government/Credit Bond Index includes securities in the Government and Credit Indices. The Government Index includes treasuries (i.e., public obligations of the U.S. Treasury that have remaining maturities of more than one year) and agencies (i.e., publicly issued debt of U.S. Government agencies, quasi-federal corporations, and corporate or foreign debt guaranteed by the U.S. Government). The Credit Index includes publicly issued U.S. corporate and foreign debentures and secured notes that meet specified maturity, liquidity, and quality requirements. You can not invest directly in an index.

Barclays U.S. Intermediate Government/Credit Bond Index is the Intermediate component of the U.S. Government/Credit index. The Government/Credit Index includes securities in the Government and Credit Indices. The Government Index includes treasuries (i.e., public obligations of the U.S. Treasury that have remaining maturities of more than one year) and agencies (i.e., publicly issued debt of U.S. Government agencies, quasi-federal corporations, and corporate or foreign debt guaranteed by the U.S. Government). The Credit Index includes publicly issued U.S. corporate and foreign debentures and secured notes that meet specified maturity, liquidity, and quality requirements. You can not invest directly in an index.

Barclays U.S. 1-3 Year Government Bond Index consist of securities in the U.S. Government Index with a maturity from 1 up to (but not including) 3 years. Securities issued by the U.S. Government (i.e., securities in the Treasury and Agency Indices). Inclusions: Public obligations of the U.S. Treasury with a remaining maturity of one year or more. Publicly issued debt of U.S. Government agencies, quasi-federal corporations, and corporate or foreign debt guaranteed by the U.S. Government. You can not invest directly in an index.

Barclays U.S. Treasury Index includes public obligations of the U.S. Treasury. Treasury bills are excluded by the maturity constraint but are part of a separate Short Treasury Index. In addition, certain special issues, such as state and local government series bonds (SLGs), as well as U.S. Treasury TIPS, are excluded. STRIPS are excluded from the index because their inclusion would result in double-counting. Securities in the Index roll up to the U.S. Aggregate, U.S. Universal, and Global Aggregate Indices. You can not invest directly in an index.

Barclays U.S. Corporate Bond Index covers USD-denominated, investment-grade, fixed-rate, taxable securities sold by industrial, utility, and financial issuers. It includes publicly issued U.S. corporate debentures and secured notes that meet specific maturity, liquidity, and quality requirements. Securities in the index roll up to the U.S. Credit and U.S. Aggregate indices. The U.S. Corporate Index was launched on January 1, 1973. You can not invest directly in an index.

BofA Merrill Lynch 1-Year US Treasury Note Index is comprised of a single issue purchased at the beginning of the month and held for a full month. At the end of the month that issue is sold and rolled into a newly selected issue. The issue selected at each month-end rebalancing is the outstanding Treasury note that matures closest to, but not beyond, one year from the rebalancing date. To qualify for selection, an issue must have settled on or before the month-end rebalancing date. You can not invest directly in an index.

Barclays Corporate U.S. High Yield Index - covers the universe of fixed rate, non-investment grade debt. Eurobonds and debt issues from countries designated as emerging markets (e.g., Argentina, Brazil, Venezuela, etc.) are excluded, but Canadian and global bonds (SEC registered) of issuers in non-EMG countries are included. Original issue zeroes, step-up coupon structures, 144-As and pay-in-kind bonds (PIKs, as of October 1, 2009) are also included. The index includes both corporate and non-corporate sectors. The corporate sectors are Industrial, Utility, and Finance, which include both U.S. and non-U.S. corporations. The Yankee sector has been discontinued as of 7/1/00. The bonds in the former Yankee sector have not been removed from the index, but have been reclassified into other sectors. You cannot invest directly in an index.

Barclays Global Aggregate Index provides a broad-based measure of the global investment-grade fixed-rate debt markets. The Global Aggregate Index contains three major components: the U.S. Aggregate Index (USD 300 million), the Pan-European Aggregate Index (EUR 300 million), and the Asian-Pacific Aggregate Index (JPY 35 billion). In addition to securities from these three benchmarks (94.4% of the overall Global Aggregate market value), the Global Aggregate Index includes Global Treasury, Eurodollar (USD 300 million), Euro-Yen (JPY 35 billion), Canadian (CAD 300 million), and Investment-Grade 144A (USD 300 million) index-eligible securities not already in the three regional aggregate indices. The Global Aggregate Index family includes a wide range of standard and customized subindices by liquidity constraint, sector, quality, and maturity. The Global Aggregate Index is a component of the Multiverse Index. You can not invest directly in an index.

Barclays Global Emerging Markets Index consists of the fixed and floating-rate USD-denominated U.S. Emerging Markets Index and the primarily EUR and GBP-denominated fixed-rate Pan-European Emerging Markets Index and includes emerging markets debt from the following regions: Americas, Europe, Asia, Middle East, and Africa. For the index, an emerging market is defined as any country that has a long term foreign currency debt sovereign rating of Baa1/BBB+/BBB+ or below using the middle rating of Moody's, S&P, and Fitch. The index does not overlap with the U.S. Corporate High-Yield Index or the Pan Euro Corporate High-Yield Index, but may overlap with other investment-grade Aggregate Indices if the securities meet their index eligibility rules. You can not invest directly in an index.

S&P 500 Index – The S&P 500 index includes 500 leading companies in leading industries of the U.S. economy. The S&P 500 is designed to be a leading indicator of U.S. equities and is meant to reflect the risk/return characteristics of the large cap universe. You can not invest directly in an index.

The NASDAQ-100 Index is a modified capitalization-weighted index of the 100 largest and most active non-financial domestic and international issues listed on the NASDAQ. No security can have more than a 24% weighting. The index was developed with a base value of 125 as of February1, 1985. Prior to December 21, 1998 the Nasdaq 100 was a cap-weighted index. You can not invest directly in an index.

The Dow Jones Industrial Average (DJIA) is an index used to measure the performance of the U.S. financial markets. Introduced on May 26, 1896 by Charles H. Dow, it is the oldest stock price measure in continuous use. Over the past century "the Dow" has become the most widely recognized stock market indication in the U.S. and probably in the entire world. Most of the stocks included in the index are listed on the New York Stock Exchange, and are all large blue-chip companies that reflect the health of the U.S. economy. All but a handful of these have major business operations throughout the world, thus providing some insight into the economic well-being of the global economy. You can not invest directly in an index.

MSCI EAFE Index is a capitalization weighted index that monitors the performance of stocks from Europe, Australiasia, and the Far East. You can not invest directly in an index.

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