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High Yield Bonds: A high paying bond with a lower credit rating than investment-grade corporate bonds, Treasury bonds and municipal bonds. Because of the higher risk of default, these bonds pay a higher yield than investment grade bonds. High yield bonds carry a rating below 'BBB-' from S&P, and below 'Baa3' from Moody's.

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EXECUTIVE SUMMARY

Our Outlook for High Yield Remains Favorable

- **Spreads** continue to offer an attractive value and provide a cushion against rising interest rates.
- **Accommodative monetary policy and strong corporate fundamentals** support a constructive view of downside risks, as companies continue to take advantage of the Fed's quantitative easing to reduce interest expense and extend maturities.
- **Default rates are and should remain low.** Financial policies among high yield issuers are broadly respectful of bondholders.
- **High yield offers an attractive alternative to Treasuries and investment grade bonds** in the event that short- or intermediate-term rates were to rise, given the sector's comparatively higher coupon and shorter duration.
- **Relative to equities,** high yield's senior placement in the capital structure and high coupons can reduce volatility and mitigate its exposure to weak economic data and exogenous shocks.
- For investors with an appropriate risk and time horizon profile, high yield can offer **income, diversification, and strong risk-adjusted returns.**

GW&K's outlook for the high yield market remains favorable, as we believe spreads continue to offer an attractive value and provide a cushion against rising interest rates. Accommodative monetary policy and strong corporate fundamentals support a constructive view of downside risks, as companies continue to take advantage of the Fed's quantitative easing to reduce interest expense and extend maturities. With few near-term catalysts for a rise in the default rate, financial policies among high yield issuers that are broadly respectful of bondholders, and continued investor demand for yield and protection against rising rates, high yield continues to offer attractive carry and the potential for spread compression at current levels.

...high yield is not only attractive on a stand-alone basis, but also as an allocation within a broad portfolio, as it has the potential to enhance the portfolio's expected return and improve its risk profile.

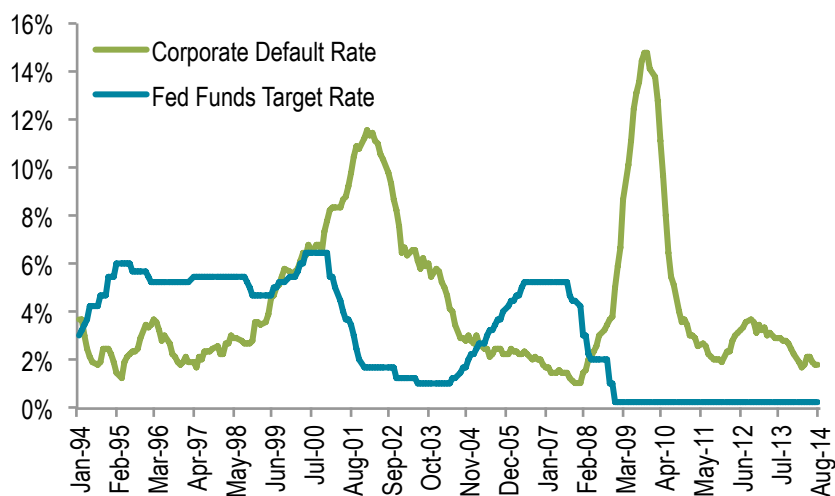
Relative to Treasuries and investment grade bonds, we believe the greater carry that high yield offers more than compensates for its additional risk of default. Relative to equities, its senior placement in the capital structure reduces volatility and mitigates its exposure to weak economic data and exogenous shocks. Consequently, high yield is not only attractive on a stand-alone basis, but also as a component of a broad portfolio, as it has the potential to enhance the portfolio's expected return and improve its risk profile.

FUNDAMENTALS

High yield offers a spread above Treasuries to compensate investors for the risk of default. But with the Federal Reserve expected to hold short-term rates near zero until mid-2015 and corporate balance sheets in good condition following years of refinancing and earnings growth, we believe that defaults will remain at low levels for the next few years. As a result, high yield offers an attractive return relative to the risk investors are assuming in the current environment.

There is typically a two to four year lag between when the Fed starts raising rates and when the default rate begins to pick up. In light of the market's expectation that the Fed will remain on hold until mid-2015, we think that a meaningful increase in defaults is unlikely for at least two to three years.

Fed Funds Target Rate and Corporate Default Rate

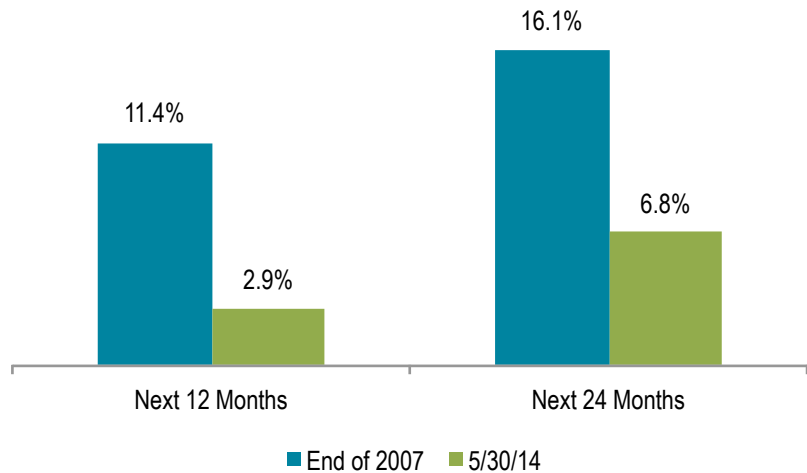


Source: Moody's; Bloomberg

Given that failure to repay principal at maturity is the most common catalyst for corporate default, our view is that the comparatively small number of impending maturities today relative to 2007 bodes well for a benign default environment.

Using the end of 2007 as a proxy for a worst case scenario for credit markets prior to a crisis, the following compares the number of bonds that were scheduled to mature within 12 and 24 months in 2007 to the number that are scheduled to do so today. Given that failure to repay principal at maturity is the most common catalyst for corporate default, our view is that the comparatively small number of impending maturities today relative to 2007 bodes well for a benign default environment.

Single B and Lower Debt Maturities Bonds Scheduled to Mature

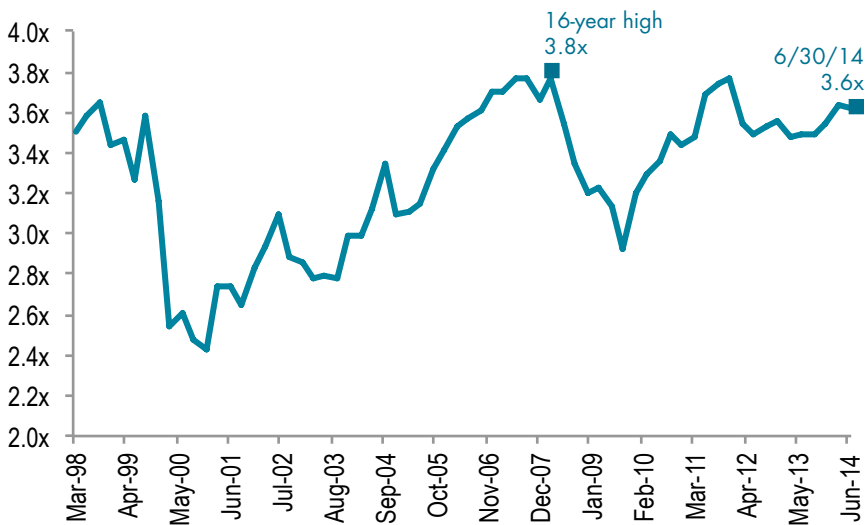


Source: J.P. Morgan Research

Our expectation of a low default rate is further supported by the strong credit metrics we currently see among high yield issuers. Following years of refinancings that have lowered the average high yield coupon from a crisis high of 8.46% to 7.06% as of 8/31/14, companies' ability to service their debt, as measured by the ratio of cash flow to interest expense, is near a 16-year high. This, in combination with the small number of near-term maturities, means that companies not only have a relatively small number of contractual obligations over the next 12 to 24 months, but are also particularly well positioned to meet them—both of which are supportive of a benign default environment.

Interest Coverage Ratio: A ratio used to determine how easily a company can pay interest on outstanding debt. The interest coverage ratio is calculated by dividing a company's earnings (EBITDA: earnings before interest, taxes, depreciation and amortization) of one period by the company's interest expenses of the same period.

High Yield Interest Coverage Ratio



Data as of 6/30/14
Source: BofA Merrill Lynch Global Research

VALUATION

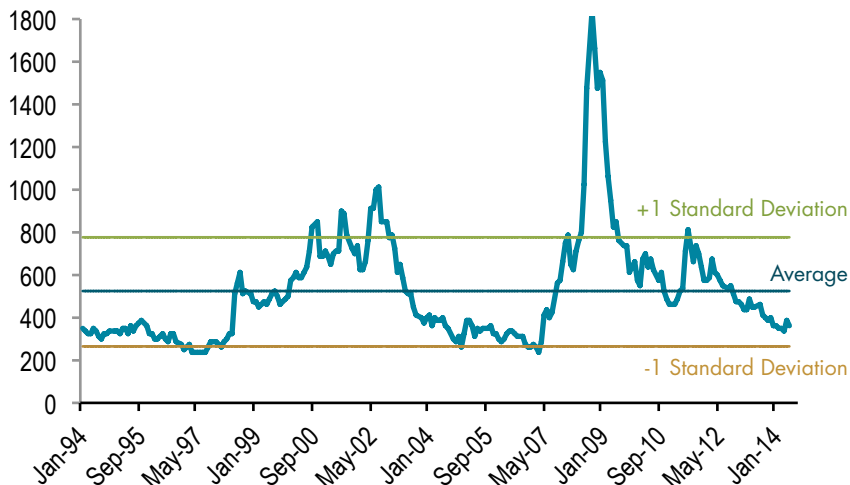
We believe that high yield spreads offer attractive carry at current levels in addition to the potential to compress and thereby drive price appreciation. We examine where spreads are today relative to their historical tight, where they are likely to go given the impending Fed tightening cycle, and what they offer relative to investment grade bonds. Despite offering yields that are near record lows, we find high yield offers an attractive risk/reward relative to other areas of the fixed income market where returns are comparatively paltry and exposure to rising rates is greater.

While we acknowledge that there are valid arguments in favor of being cautious on high yield, we remain constructive on the space and believe that both the carry and potential for spread compression support our bullish stance.

Though high yield spreads at 158 basis points below their long-term average seem slightly rich, they are nevertheless more than 128 basis points above their all-time tight, only 0.62 standard deviations below their long-term average, and at a level below where they have historically traded 35% of the time. While we acknowledge that there are valid arguments in favor of being cautious on high yield, we remain constructive on the space and believe that both the carry and potential for spread compression support our bullish stance. Furthermore, spreads at these levels will allow high yield to absorb a significant portion of any increase in Treasury yields and help the sector outperform in a rising rate environment.

Option Adjusted Spread (OAS): A measurement of the spread of a fixed-income security rate and the Treasury rate of a similar maturity, which is adjusted to take into account an embedded option. OAS can be viewed as the compensation an investor receives for assuming a variety of risks net of the cost of any embedded options.

High Yield OAS



Source: Barclays

Using history to gain insight into what we might expect over the next 24 months, as we approach the beginning of the Fed tightening cycle in the middle of next year, we examined the period beginning 12 months before the Fed last began raising rates in 2004 and ending 12 months after. Though spreads started higher than where they are today, they did not achieve their lows until eight months after the Fed began raising rates, suggesting there may be a long runway for spreads to move even tighter from here.

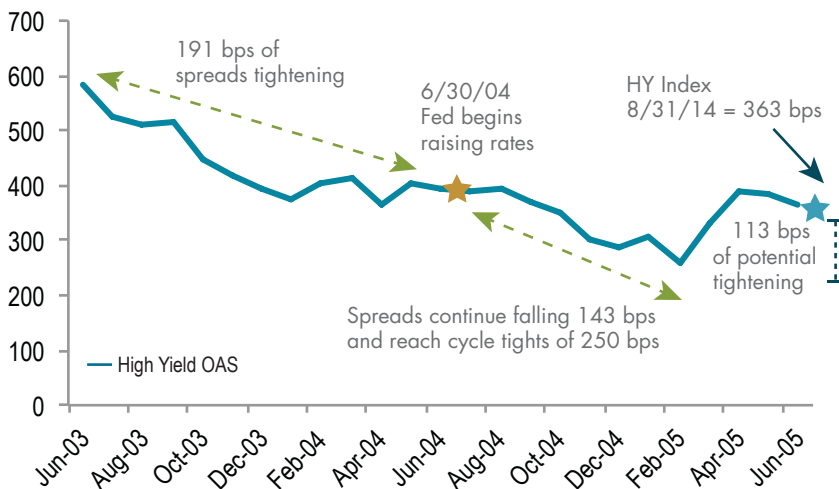
High Yield Statistics

Option Adjusted Spread (OAS)

| | |
|-------------------------|------|
| 8/31/14 | 363 |
| Average | 521 |
| Median | 462 |
| Max | 1833 |
| Min | 235 |
| Standard Deviation | 256 |
| Distance from Max | 1470 |
| Distance from Min | -128 |
| Distance from Average | -158 |
| % of Time Below Current | 35 |
| % of Time Below Average | 59 |

Source: Barclays

2004 Fed Rate Increase: Effect on Spreads (OAS) 12 Months Before & 12 Months After

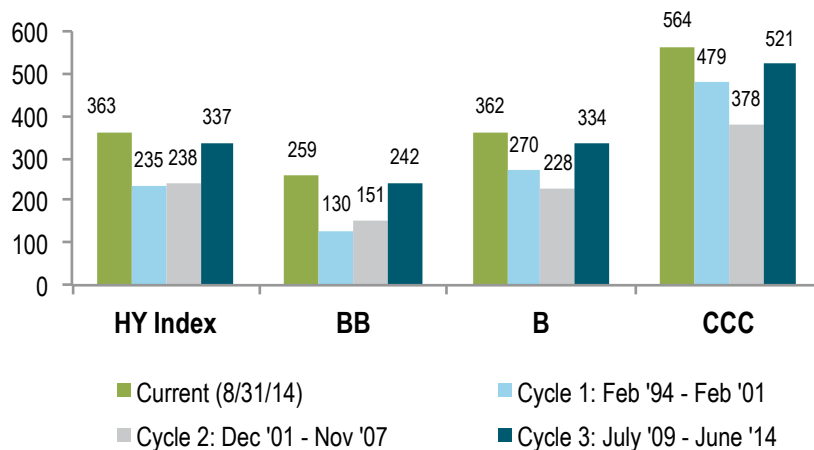


Source: Barclays

Drawdown: The peak-to-trough decline during a specific record period of an investment, fund or commodity. A drawdown is usually quoted as the percentage between the peak and the trough.

At 363 OAS as of 8/31/14, high yield spreads are significantly wider than tights achieved during the two most recent cycles, suggesting that more than 100 basis points of spread compression from current levels is achievable.

High Yield OAS Historical Cycle Tights

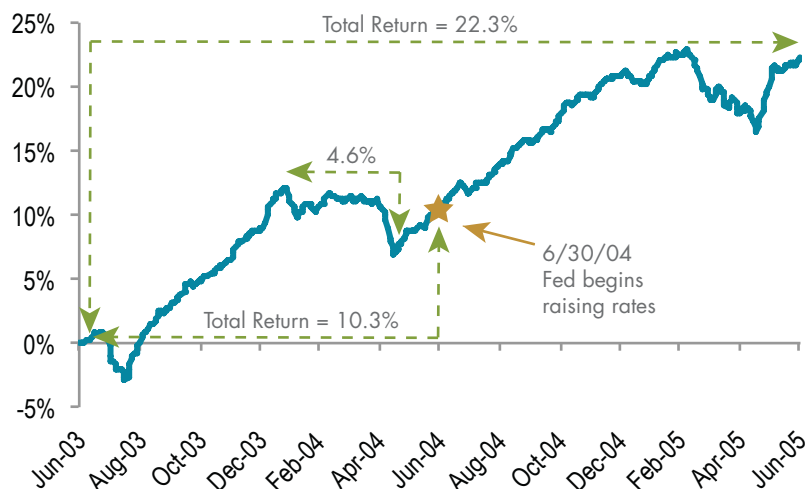


Source: Barclays

Analyzing total returns over the same period, we see in the graph on the next page that high yield gained 10.33% in the 12 months leading up to the first rate hike and an additional 10.86% over the following 12 months. Volatility rose around the first rate hike, but the maximum drawdown was only 4.61% and the index fully recovered in fewer than six months. Although yields are lower today than they were in 2004, the last tightening cycle suggests that positive total returns are possible as the favorable economic conditions that would compel the Fed to begin raising rates (low unemployment, rising asset prices, and strong consumer and business spending) are the same conditions that drive demand for riskier asset classes such as high yield.

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2004 Fed Rate Increase: Effect on Total Return



Source: Barclays

We believe that high yield offers an attractive alternative to Treasuries and investment grade bonds in the event that short or intermediate-term rates were to rise, given the sector's comparatively high coupon and short duration.

We believe high yield offers an attractive alternative to Treasuries and investment grade bonds in the event that short- or intermediate-term rates were to rise, given the sector's comparatively high coupon and short duration. The following examines the expected total returns for high yield under a base case scenario, in which Treasury rates are unchanged and high yield spreads compress modestly, and a rising-rate scenario, in which Treasury rates rise 1% over 12 months and high yield spreads absorb only 25% of this rise. Note that even under the rising-rate scenario, high yield returns are positive due to the high return from income and the modest price return from spread compression.

Scenario Analysis

| | | HIGH YIELD CORPORATE BONDS | |
|---|---------|--|--------------|
| | | Current Rate Assumption 5.20% ¹ | |
| | | Rates Unchanged | Rates Rise |
| Rate Change | Rates | 0.00% | 1.00% |
| Price Change from Rate Change | | 0.00% | -4.00% |
| Assumed Spread Compression | Spreads | 25 bps | 25 bps |
| Price Change from Spread Change | | 1.00% | 1.00% |
| Return — from Income ² | Returns | 5.08% | 5.58% |
| Return — from Spread and/or Rate Change | | 1.00% | -3.00% |
| TOTAL RETURN | | 6.11% | 2.61% |

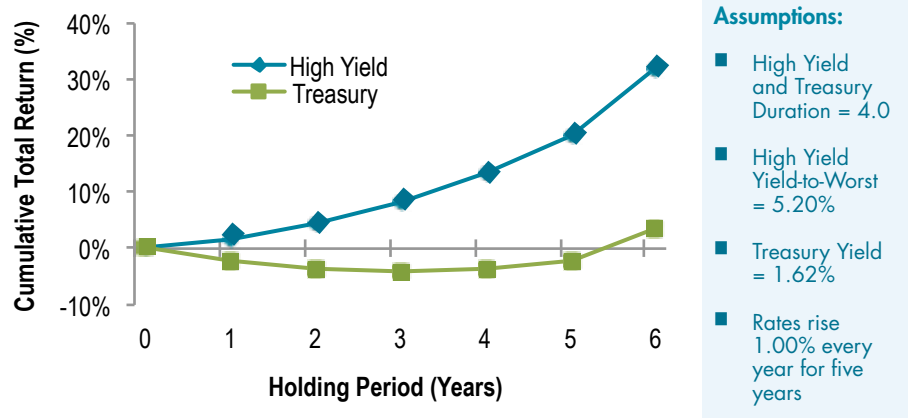
¹Barclays HY Index YTW at 8/31/14;

²Expected Average Income Return Over 1 Year. Duration assumption is 4 years.

The following scenario analysis illustrates the greater returns that high yield offers relative to comparable duration Treasuries in a multi-year rising rate environment. Given that duration is the same in both cases, the 3.52% difference in yield accounts for all of high yield's outperformance.

Note that it is not until the middle of the fifth year that Treasuries begin to generate a positive *cumulative* return, whereas in high yield's worst year (year one), a positive return is still generated. Furthermore, by the end of the sixth year, high yield has outperformed Treasuries by 25.30% on a cumulative basis.

Cumulative Total Return During a Period of Rising Rates



Source: GW&K Investment Management

Looking at annual high yield total returns over the last 30 years, the long-term trend has been favorable. The reason we believe high yield offers such an attractive proposition is that during the calendar years shown, only five saw negative returns, and in every case but one, returns in the following year more than recovered what was lost (in the one case where they did not, the second year fell short by just 0.89%).

High Yield Calendar Year Total Returns

| Date | 1 Year | Date | 1 Year | Date | 1 Year |
|----------|----------|----------|---------|----------|---------|
| 12/31/13 | 7.44% | 12/31/03 | 28.97% | 12/31/93 | 17.12% |
| 12/31/12 | 15.81% | 12/31/02 | (1.41%) | 12/31/92 | 15.75% |
| 12/30/11 | 4.98% | 12/31/01 | 5.28% | 12/31/91 | 46.18% |
| 12/31/10 | 15.12% | 12/29/00 | (5.86%) | 12/31/90 | (9.59%) |
| 12/31/09 | 58.21% | 12/31/99 | 2.39% | 12/29/89 | 0.83% |
| 12/31/08 | (26.16%) | 12/31/98 | 1.87% | 12/30/88 | 12.53% |
| 12/31/07 | 1.87% | 12/31/97 | 12.76% | 12/31/87 | 4.99% |
| 12/29/06 | 11.85% | 12/31/96 | 11.35% | 12/31/86 | 17.45% |
| 12/30/05 | 2.74% | 12/29/95 | 19.17% | 12/31/85 | 25.64% |
| 12/31/04 | 11.13% | 12/30/94 | (1.03%) | 12/31/84 | 9.70% |

Source: Barclays

Looking at annual high yield total returns over the last 30 years, the long-term trend has been favorable.

...high yield offers appealing risk-adjusted returns.

Sharpe Ratio: A ratio developed by Nobel laureate William F. Sharpe to measure risk-adjusted performance. The Sharpe ratio is calculated by subtracting the risk-free rate - such as that of the 10-year U.S. Treasury bond - from the rate of return for a portfolio and dividing the result by the standard deviation of the portfolio returns.

Leveraged Buyouts (LBOs): The acquisition of another company using a significant amount of borrowed money (bonds or loans) to meet the cost of acquisition. Often, the assets of the company being acquired are used as collateral for the loans in addition to the assets of the acquiring company. The purpose of leveraged buyouts is to allow companies to make large acquisitions without having to commit a lot of capital.

Mergers & Acquisitions (M&A): A general term used to refer to the consolidation of companies. A merger is a combination of two companies to form a new company, while an acquisition is the purchase of one company by another in which no new company is formed.

When compared to other asset classes such as stocks and Treasuries, high yield offers appealing risk-adjusted returns.

Sharpe Ratios (as of 8/31/14)

| | 1 Yr | 3 Yr | 5 Yr | 10 Yr | 15 Yr | 20 Yr | 30 Yr |
|---|------|------|------|-------|-------|-------|-------|
| Barclays U.S. Corporate High Yield Index | 3.04 | 1.75 | 1.81 | 0.70 | 0.59 | 0.60 | 0.66 |
| S&P 500 Index | 2.75 | 1.68 | 1.25 | 0.52 | 0.25 | 0.49 | 0.53 |
| Barclays Treasury Index | 1.50 | 0.61 | 0.95 | 0.66 | 0.72 | 0.65 | 0.71 |

Source: Morningstar

The difference in credit risk between the highest quality speculative grade bonds (BBs) and the lowest quality investment grade bonds (BBBs) is generally small. Since 1993 the average default rate for these ratings categories was less than 1% (according to Moody's). However, BBs currently offer a spread above Treasuries that is almost twice that of BBBs (1.93x is higher than the long-term average of 1.89x) and well above recent lows of 1.46x. As a result, we believe that BBs continue to offer a superior risk/return profile at current levels and investors are being more than adequately compensated for the additional risk they are assuming.

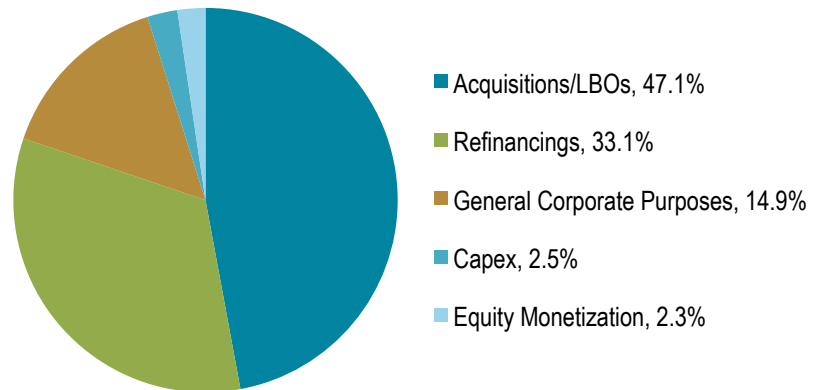
FINANCIAL POLICY

Disciplined financial policies and positive commentary from the ratings agencies support the view that corporations are taking advantage of current market conditions to strengthen their balance sheets rather than pursue LBOs or aggressively return cash to shareholders. Furthermore, far from signs of "frothiness" in the high yield bond market, we continue to see corporations issuing new debt to lower their coupons, push out their maturities, and add cash to their balance sheets. Therefore, consistent with our earlier discussion of anticipated low default rates, we believe recent actions by companies' management teams and boards are supportive of a benign credit environment.

In contrast to 2007, when the largest single use of proceeds was to finance acquisitions and LBOs, so far in 2014, refinancings have been the largest use, with M&A representing only a quarter of total issuance. This is significant because acquisitions and LBOs typically use aggressive levels of debt and optimistic estimates of synergies in order to show profitability, thereby exposing bondholders to significant risk of default in the event that forward-looking assumptions prove incorrect. Refinancings, on the other hand, limit the chance of default by enabling companies to replace debt with lower coupons and longer maturities while adding cash to the balance sheet to service existing debt. We do not expect a significant change in this trend. We expect M&A to be relatively muted due to high stock prices and cost

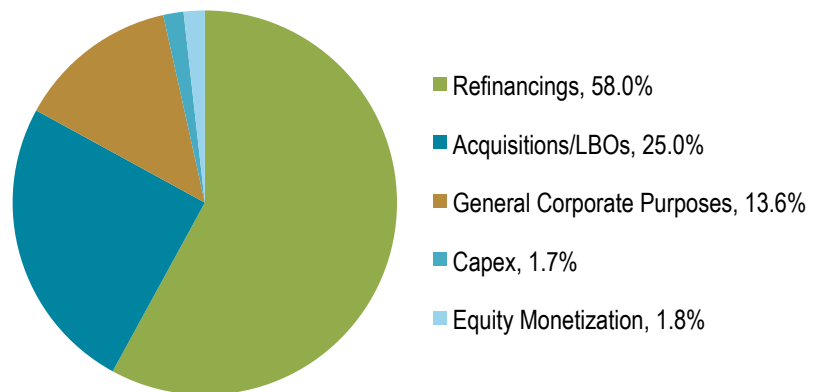
cuts in recent years (which leave little room for further cost reduction and synergy realization), and we expect corporations to continue to refinance, given the large amount of higher cost debt becoming callable in the next few years.

2007: Use of High Yield Bond Proceeds



Source: BofA Merrill Lynch Global Research

YTD 2014: Use of High Yield Bond Proceeds (8/31/14)



Source: BofA Merrill Lynch Global Research

Since the beginning of the year, the ratings agencies have been increasingly positive on U.S. corporations, as upgrades have consistently outnumbered downgrades.

Since the beginning of the year, the ratings agencies have been increasingly positive on U.S. corporations, as upgrades have consistently outnumbered downgrades. Given that these opinions consider not only the probability of default, but also assess company fundamentals from a business, credit, and industry perspective, a broadly favorable view from both agencies suggests that U.S. companies have generally positive outlooks over the next 12 to 24 months.

CONCLUSION

- *We remain constructive on the high yield market due to a variety of factors.*
- *Compared to other fixed income asset classes and forecasts for an eventual rise in rates, high yield is attractive on a relative basis.*
- *For appropriate investors, high yield can offer income, diversification, and strong risk-adjusted returns.*

ABOUT GW&K

GW&K was founded in 1974 to offer innovative investment solutions consistent with our clients' objectives. Our company has grown from a local provider of investment management services to a nationally recognized manager with broad investment capabilities. We first gained attention for our municipal bond expertise, and it remains one of the cornerstones of our investment offerings. Through the years we introduced a range of equity and taxable bond strategies that stay true to our core principles of active management, independent research and an eye toward quality. Today we serve a diverse client base of individuals and institutions.

Our firm has been under continuous senior management since our founding, and now we have the benefit and support of our partner firm, Affiliated Managers Group. Through this partnership we continue to operate independently, maintain our client oriented culture and focus on delivering personalized investment management services.

This represents the views and opinions of GW&K Investment Management. It does not constitute investment advice or an offer or solicitation to purchase or sell any security and is subject to change at any time due to changes in market or economic conditions. The comments should not be construed as a recommendation of individual holdings or market sectors, but as an illustration of broader themes.

Fixed income investments are subject to interest, credit, and market risk. Interest rate risk: the value of fixed income investments will decline as interest rates rise. Credit risk: the possibility that the borrower may not be able to repay interest and principal. Low rated bonds generally have to pay higher interest rates to attract investors willing to take on greater risk. Market risk: the bond market in general could decline due to economic conditions, especially during periods of rising interest rates.

Higher yielding, lower rated securities involve greater price volatility and present greater risks than higher rated fixed income securities.

GW&K assumes no responsibility for the accuracy of the data provided by outside sources. Sources for indexes and other external data include Barclays, Bloomberg, Moody's, JP Morgan Research, BofA Merrill Lynch Global Research, and Morningstar.

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