GW&K® INVESTMENT MANAGEMENT

QUARTERLY INVESTMENT REVIEW 1Q 2015

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ECONOMIC COMMENTARY

By Harold G. Kotler, CFA

People of all ages have come to embrace the changes that technology has brought to our everyday lives. The arrival of smart phones and the birth of firms such as Amazon, Google, and Netflix to name a few, have caused a dramatic shift in behavior patterns and lifestyle. People have come to expect immediate answers and instant gratification. Patience seems to be a thing of the past.

The transformation ushered in by these technologies has also helped to create a culture of sound bites, simple yes or no answers, and reduced perspective. It is amazing that with so much information at our fingertips, so much is also slipping away. What used to be black or white has turned

Continued on inside

INDEX PERFORMANCE	CURRENT QUARTER	ONE YEAR 3/31/15
Barclays 10-Year Municipal Bond Index	1.26%	6.75%
Barclays Aggregate Bond Index	1.61%	5.72%
Barclays High Yield Index	2.52%	2.00%
Dow Jones Industrial Average	0.33%	10.57%
S&P 500 Index	0.95%	12.73%
Russell 2000 Index	4.32%	8.21%
NASDAQ Composite	3.79%	18.12%

FIRST QUARTER 2015

ECONOMY

- After recording post-recession highs in the second and third quarters of 2014, GDP slowed to 2.2% in Q4, below its long-run average of 3.3%.
- Economic indicators were mixed during the quarter. Nonfarm payrolls expanded by over 200K in January and February but disappointed in March with only 126K added jobs. The unemployment rate dropped to 5.5%, the lowest level since 2008, but a multi-decade low in the labor force participation rate and scant increases in wages tempered the data.
- Oil prices continue to decline in the first quarter; however, an elevated savings rate indicates that consumers are not spending increases to disposable income from lower energy prices.
- Inflation appears contained, continuing to run below the Fed's target of 2%.

FED ACTION

- The federal funds target rate remains unchanged at 0–0.25%. In its March meeting, the FOMC removed the term "patient" from its statement, signaling that the ultimate timing of rate hikes would be "data dependent."
- The sentiment overall was viewed as "dovish" because the Fed revised down its forecasts for growth, inflation and the future path of the federal funds rate.
- Market participants are anticipating the first rate hike around September 2015. Even after Fed forecasts for rates were revised lower, the market is still pricing in an easier rate hike path and a lower neutral fed funds rate compared to FOMC members.

BOND MARKETS

- Fixed income markets saw positive performance in the first quarter, driven by negative yields abroad, dovish commentary from the Fed, and lackluster economic data. The 10-year and 30-year Treasury rates dropped 25 bps and 21 bps, respectively.
- Investment grade corporates added to their recent strong performance, up 2.32% for the quarter, benefitting from the rally in Treasuries and their superior incremental income. High yield performance was better at 2.52%.
- Municipals posted respectable returns this quarter amid a flood of tax-exempt supply and extreme volatility in the broader markets.
- Demand proved surprisingly robust as fund flows were consistently positive throughout the quarter amidst substantial fluctuations in rates.

EQUITY MARKETS

- The equity market finished the quarter with modest gains despite facing pressure in March as concerns around the strong dollar, mixed economic data, and above-average valuations weighed on sentiment. Small cap stocks, with a larger percent of domestic revenue and solid earnings growth, led the move higher and outperformed large caps.
- The Health Care and Consumer Discretionary sectors posted the strongest quarterly returns. Utilities was the worst performing sector, retreating after last year's run. Energy also lagged as oil prices hovered at five-year lows.
- Growth stocks generally outpaced value in all market segments. This trend was particularly striking in the small cap market where Biotechnology continued to soar.
- While volatility ticked higher, low interest rates, continued low inflation, and global easing moves all supported the equity market. Merger and acquisition activity also accelerated as U.S. companies put their healthy balance sheets to work.

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into shades of gray. In years past, the geopolitical theater was scary, but more definable. We had East versus West, Communism versus Democracy, us versus them. Now we are at war with culture, chaos, and anarchy. Political parties that used to align along two definitive positions have morphed into an almost parliamentary system.

The investing world has also morphed. Long gone are the days of a conservative portfolio producing a reasonable income stream. It is no longer possible to just sit back and "clip coupons." Today income is a rare commodity. Many workers retired too early or have spent down their assets. Without a strategic approach, the living standards of many retirees could be in jeopardy. Investing, always a challenge, used to have a fallback position of income generated by assets. Now with a dependence on asset growth alongside income growth, investing is far from black or white.

The majority of GW&K's assets have always been in bonds. We created an active bond management approach when the method of the day was passive. We understood that a bond was only a reflection of the time value of money and, as times changed, so did the value of the bond. We counseled clients to focus not so much on the income, but on the time component of the bond's contract. We stressed that *all* bonds needed to be sold before maturity, and our job was to determine when to sell and what to buy.

We of course still follow this approach, staying true to our lineage. But times have changed. We can look back fondly at the 5%–7%–10% days of CDs and bonds, but those days are long gone and not likely to return soon. Tomorrow is here and we plan on doing our best to help all of our clients prosper. So while the technology revolution has simplified so many parts of our lives, we recognize that much has also gone in the opposite direction. Predictability is a comforting attribute, but it has largely slipped away in the investment world. Even so, as global economies continue to develop, the free market system will continue to grow and to create opportunities.

So how do we invest for the future with any level of comfort? Holding cash is not an alternative to investing. An entrepreneur's attitude is needed in this complicated environment because there are no sustainable answers. Those who want an answer as to how to invest capital today without first recognizing the depth of the question and the difficulty of answering it correctly may very well be disappointed in the investment results.

As a firm historically steeped in the bond market, we understood (and always guarded against) the destructive power of declining income. With no guarantees that trend would eventually reverse, we needed to diversify away from a bonds-only portfolio, increase our strategy offerings and offer clients greater choice. Through the years we have added a range of equity options. Our small capitalization strategies have allowed our clients to participate in a dynamic and ever-changing component of the U.S. economy. As bond prices moved higher and interest rates declined, we created an equity dividend strategy, generating income equal to or greater than bonds without the duration risk, accepting greater volatility but also greater returns. We wanted to offer our clients more protection from the risk of re-investing in lower interest rate bonds. Last year we created an international small cap strategy, recognizing that there are great, small public companies outside the U.S. that will provide further growth opportunities in this global economy.

The broadening of our investment expertise was crucial in this changing world. We always knew there was no one investment approach that would meet our clients' needs, but it has become ever more critical to have professional managers and analysts in many different parts of the bond and stock markets to help our clients diversify and to produce more sustainable returns. The days of stable cash or near cash returns are behind us. The need to accept greater volatility is here, but volatility is not a risk if one is disciplined and diversified.

Harold G. Kotler, CFA
CEO, Chief Investment Officer

GW&K UPDATE	*3/31/15*
TOTAL ASSETS UNDER MANAGEMENT	$24.9 Billion
TOTAL EMPLOYEES	108
TOTAL INVESTMENT PROFESSIONALS	36

EQUITY TEAM EXPANDS

We are pleased to announce that **Aaron C. Clark, CFA,** has joined GW&K as a portfolio manager. Aaron will work with Dan Miller to oversee GW&K's larger cap equity strategies. Aaron's career focus on larger-cap and dividend oriented investing and depth of research experience will be a great asset to our equity investment team and to our clients. Prior to joining GW&K, Aaron was a principal and portfolio manager at Tetrem Capital Management. He also served as a portfolio manager at Pioneer Investments as part of their value equities team, and at Morgan Stanley Investment Company, where he co-managed a Dividend Growth Fund.

GW&K PROMOTIONS

We are pleased to announce that **Jeff Whitney** (Equity Research Analyst and Portfolio Manager), **Sheila May** (Director of Municipal Bond Research), **John DelVecchio** (National Sales Manager) and **Steve Sutter** (Director of Information Technology) have been named Principals of the firm. This recognition reflects the important contributions each has made to GW&K, and underscores our commitment to build and maintain a strong team dedicated to excellence in investment management and client service.

Visit **www.gwkinvest.com** for more information.

MUNICIPAL BOND STRATEGIES

INVESTMENT TEAM

Nancy G. Angell, CFA	Partner, Co-Director of Fixed Income
John B. Fox, CFA	Partner, Co-Director of Fixed Income
Martin R. Tourigny, CFA	Partner, Portfolio Manager
Brian T. Moreland, CFA	Principal, Portfolio Manager

14 Municipal Investment Professionals	**18** Average Years Experience	**12** Average Years with Firm

"Municipals posted respectable returns in the first quarter amid a flood of tax-exempt supply and extreme volatility in the broader markets. Momentum swung from furious rallies to orderly retreats to cautious advances."

GW&K MUNICIPAL BOND STRATEGIES

SHORT-TERM MUNICIPAL BOND	Seeks to earn higher after-tax returns than money market funds while managing risk
FIVE-YEAR MUNICIPAL BOND	High-quality active approach aims to preserve and enhance capital and targets an average maturity of five years
MUNICIPAL BOND	High-quality intermediate approach with goal to preserve and enhance capital emphasizes research and active management
MUNICIPAL ENHANCED YIELD	Long-term approach that includes an allocation to higher yielding bonds with a goal to produce high after-tax income

Municipals posted respectable returns in the first quarter amid a flood of tax-exempt supply and extreme volatility in the broader markets. Momentum swung from furious rallies to orderly retreats to cautious advances. The yield on the 10-year municipal bond traded as low as 1.72% and as high as 2.18% before closing March at 1.96%, down 9 basis points for the quarter. In some pockets of the municipal curve, rates finished higher by as much as 10 basis points, though coupon income was enough to keep returns universally positive. Demand proved surprisingly robust even in the face of first quarter volume that topped $100 billion for only the third time ever. Mutual funds saw net inflows of $11 billion for the quarter, about half of what they collected for all of 2014. Even during the February selloff, weekly flows never turned negative. But the heavy supply still weighed on municipal bonds and ensured that returns, though positive, would not match the more impressive results seen in the Treasury market.

The sharp drop in interest rates that began the year caught most investors off guard. After all, the domestic economy was expanding at a healthy clip, unemployment was declining rapidly and overseas central banks were waging an all-out assault on deflation. In January, the Fed removed the "considerable time" language from its policy statement, suggesting a mid-year liftoff in rates was possible. It seemed an unlikely setting for a massive bond rally. But the market instead focused on the continued free fall in crude prices, the rock-bottom yields on foreign sovereign debt and political instability in Russia and Greece. By the end of January, the yields on 10- and 30-year Treasuries had plunged more than 50 basis points and the Long Bond had established a record low level of 2.22%. Soon, however, the volatility that ultimately defined the quarter emerged. In early February, a strong jobs report had the market immediately second guessing itself, and over the ensuing weeks, with oil prices stabilizing, payrolls expanding further and tensions abroad easing, interest rates fully retraced their January run. But even that change in sentiment would prove short lived. In the final weeks of the quarter, bonds rallied back after the Fed reduced forecasts for growth and inflation, dovish signals that seemed confirmed by weaker economic readings. By quarter end, Treasury yields from 5 to 30 years were all down more than 20 basis points from the beginning of the year.

As we head into the second quarter, municipal credit fundamentals remain in good shape. Tax revenues continue to expand while expenses have stayed reined in. Even the surge in issuance has been driven by refinancing existing bonds, not adding new debt. This reflects the states' disciplined approach to repair their finances and also allows them more flexibility to address legacy issues like pension funding. The technical environment has also improved. The selling pressure that normally precedes tax day should be manageable and the market continues to work through excess dealer inventory accumulated over recent weeks. Supply may remain elevated, but fund flows reflect healthy demand. Rate volatility is likely to persist going forward, keeping a premium on nimble trading capabilities. We took advantage of such opportunities in the first quarter and will look for more of the same in the months ahead.

Toward the end of January, we felt the bond market had moved too far too fast and we responded by selling aggressively into the rally. At that time, the yield on 10-year municipals had fallen to 1.72%, the positive technical environment was coming to an end and tax season was fast approaching. We sold bonds with 10-year maturities which brought our duration down to roughly 5.35 from 5.65 and built up our cash allocation to about 7.5%.

By mid-March, the yield on 10-year municipals had backed up to 2.18%, nearly 50 basis points above the January lows. In addition, the Treasury market had stabilized and even begun to rebound a bit while municipals stayed sloppy due to the supply overload. We were handed an opportunity to reinvest cash harvested during a much richer environment into a cheap market that was offering a huge selection of bonds. We concentrated our purchases in maturities between 10 and 12 years and, by the end of the quarter, brought cash down below 3% and are more or less fully invested heading into the second quarter.

TAXABLE BOND STRATEGIES

INVESTMENT TEAM

Mary F. Kane, CFA	Partner, Lead Portfolio Manager
Nancy G. Angell, CFA	Partner, Co-Director of Fixed Income
John B. Fox, CFA	Partner, Co-Director of Fixed Income

10 Taxable Investment Professionals	**18** Average Years Experience	**9** Average Years with Firm

GW&K TAXABLE BOND STRATEGIES

SHORT-TERM TAXABLE BOND	Through research and diversification, seeks to outperform money market funds while managing portfolio volatility
CORE BOND	A core multi-sector bond strategy that offers a more conservative profile by selecting only investment grade securities
ENHANCED CORE BOND	Offers broad market exposure across multiple bond sectors, including high yield bonds, while seeking to provide strong income
TOTAL RETURN BOND	This multi-sector approach takes advantage of relative valuation among distinct bond sectors and seeks to generate high income and capital gain
CORPORATE BOND OPPORTUNITIES	Seeks to maximize current income and longer-term capital appreciation by focusing on both high grade and high yield corporate bonds

Fixed income markets saw strong performance in the first quarter, generating positive returns at every point on the yield curve and across the quality spectrum. Negative yields abroad, dovish Fed commentary, and lackluster economic data drove a rally in interest rates, while stabilization in energy prices, positive corporate earnings, and easing geopolitical tensions provided support for spread product. Despite posting positive returns, the bond market experienced significant volatility, as the 1-year Treasury bill hit its highest yield in almost four years, the 30-year yield reached an all-time low, and investment grade corporate spreads saw their widest level in over twelve months. Yields bounced modestly off the bottom exiting the quarter but are still not far from historic lows, and volatility remains elevated amid concerns about a strong U.S. dollar, low energy prices, and quantitative easing around the world.

The Treasury curve experienced a bull flattening during the quarter, reaching its flattest level in more than six years. Short rates fell by 11 basis points in response to language from the Fed intimating a possible third quarter rate hike and a slow pace of additional hikes thereafter. At the same time, monetary easing around the world and the deflationary impact of falling energy prices drove a rally in the long end, where rates touched an all-time low of 2.22% before rebounding and closing the quarter down 21 basis points. The Treasury sector returned 1.64%, slightly outperforming the 1.61% of the Barclays Aggregate Bond Index. Taxable municipals benefited from their long duration, returning 2.23%, while the comparatively short duration of mortgages drove the relatively weak 1.06% return.

Investment grade corporates returned 2.32%, benefiting from the rally in Treasuries and their incremental income. Within the investment grade sector, lower quality bonds modestly outperformed. The high yield sector was the performance leader this quarter, gaining 2.52%. The best performing sectors in high yield were those which benefited from falling energy prices and those which had the least exposure to a strong dollar.

We expect volatility to persist for the foreseeable future. Uncertainty surrounding monetary policy will continue to dominate fixed income markets as the Fed works to reconcile several conflicting narratives: its attempt to normalize monetary policy at home must contend with easing abroad; its success in lowering unemployment has been stubbornly free of wage growth; and its efforts to stoke higher inflation have been stymied by falling energy prices. Regardless of the exact timing of the first hike or pace of increases thereafter, we ultimately expect the relative attractiveness of U.S. yields to limit upside in rates. We also believe spread product will benefit from strong corporate fundamentals and the scarcity of yield available elsewhere.

All of our strategies remain essentially neutral-weight with respect to duration and curve positioning. We expect any upward pressure on rates from strong economic growth domestically to be tempered by low rates abroad. We also expect the curve to continue flattening in advance of the impending rate hike amid subdued inflation expectations, though we acknowledge that much of this move has already been priced in. We currently see the most compelling value in intermediate maturities, which offer attractive carry and roll for the interest rate risk being assumed.

We continue to believe corporate bonds offer an attractive value relative to Treasuries at current spreads, given a favorable growth outlook for U.S. corporations, near-peak profit margins, and strong balance sheets. Corporates also offer a defensive cash flow profile that protects against the risk of rising rates. Within investment grade, we still have a bias toward lower quality credits, preferring BBBs for their incremental spread over A-rated bonds for acceptable levels of additional risk.

Our outlook for high yield is favorable as well, and we remain overweight in all eligible strategies. Weakness in the Energy sector notwithstanding, credit fundamentals are strong and we expect defaults ex-Energy to remain below their long-term average. Within high yield, our largest overweight is Energy, where we see opportunity among the higher quality credits with strong hedge books, solid balance sheets, and low cost assets. We remain neutral on mortgages, despite limited room for spread compression, because they have relatively low sensitivity to rising interest rates while offering a defensive alternative to credit markets. Within the mortgage space, we continue to target seasoned pools with high coupons.

"Negative yields abroad, dovish Fed commentary, and lackluster economic data drove a rally in interest rates, while stabilization in energy prices, positive corporate earnings, and easing geopolitical tensions provided support for spread product."

EQUITY STRATEGIES

INVESTMENT TEAM

Daniel L. Miller, CFA	Partner, Director of Equities
Jeffrey W. Thibault, CFA	Partner, Portfolio Manager
Aaron C. Clark, CFA	Vice President, Portfolio Manager
Joseph C. Craigen, CFA	Vice President, Portfolio Manager

11	17	7
Equity Investment Professionals	Average Years Experience	Average Years with Firm

GW&K EQUITY STRATEGIES

EQUITY DIVIDEND PLUS	Income oriented strategy that invests in companies paying above-average dividends and with the required balance sheet strength needed to sustain dividend payouts
DIVERSIFIED EQUITY	Combines growth & value disciplines and diversifies across large, mid, and small capitalization stocks
SMALL/MID CAP CORE	A core strategy that invests in both small and medium sized companies that offer sustainable earnings growth
SMALL CAP CORE	Focuses on small companies with sustainable earnings growth in niche markets with lasting growth potential
SMALL CAP GROWTH	Utilizes fundamental research and quantitative screening to identify small companies with sustainable, above-average earnings growth in niche markets

"Overall, we see the continuation of low inflation, low interest rates and slow but steady economic growth despite our being in the seventh year of economic expansion."

The market began the year in a downward drift, as fear over declining oil prices, deflation, and geopolitical tensions in Russia, Greece and the Middle East held sway. But by February, encouraging economic/jobs data, a stabilization in oil prices, and some diminishing of global political tensions seemed to put these fears to rest. The market put together a sustained rally culminating in a record high close for the S&P 500 Index in early March. From there, the market had difficulty holding its gains as the negative impact of the strong dollar on international sales and on corporate profits became more evident. By quarter's end, the market had posted a modest gain of under 1%.

Large cap stocks, as measured by the S&P 500 Index posted a rather anemic yet still positive return of 0.95%. The best sectors, posting mid-single-digit returns, were Health Care and Consumer Discretionary. Weak sectors, posting declines between 2%–5% included interest sensitive Utilities and Financials, as well as Energy names.

The Russell 2000 Index of smaller cap stocks, less impacted by the dollar and less exposed to international markets, posted a more respectable gain of 4.32%. This was the second consecutive quarter of smaller cap outperformance versus large caps. The Health Care sector put up huge gains of more than 12%, with the Biotech and Pharma industries leading the way with 15% gains. Consumer Discretionary and Information Technology sectors also posted solid gains of over 5%. All other sectors posted rather flat returns for the quarter.

The market's roller coaster ride in the first quarter is indicative of its many cross-currents. On the positive side, we still have a continuation of our low inflation, low interest rate environment. Europe's adoption of quantitative easing (QE) should benefit economic growth in that region and should extend the period in which low rates will continue. While the Fed has clearly reduced its QE measures, their commentary suggest they are still in no hurry for rates to go up. Economic growth remains positive, albeit not as robust as initial expectations this year. The strong dollar and the drop in oil prices are expected to be a boon to consumers, yet the data has not been as consistently positive as we would hope. While the Consumer Confidence Index, housing statistics and big ticket retail have been strong, smaller ticket retail sales have been weaker. However, the terrible winter weather in the Northeast and the shortage of some goods due to the West Coast port strike is most likely to blame. We would expect growth to improve now that these issues are behind us. Labor data continues to be the most resilient, with the unemployment rate down to 5.5%, unemployment claims falling and job creation solid. Overall, we see the continuation of low inflation, low interest rates and slow but steady economic growth despite our being in the seventh year of economic expansion.

Corporate profitability remains good, although the factors listed previously have clearly taken down the rate of growth expected by most market strategists and economists. Growth will resume once we cycle through these events in the second half.

The health of corporate balance sheets also supports our view of a positive market outlook. M&A activity remains very strong, dividend payments continue to increase at rates above earnings growth, suggesting companies are paying out a larger share of their earnings in the form of dividends, and share repurchases remain robust. While the volatile market caused investors to pull money out of domestic mutual funds and ETFs in the quarter, it was more than offset by the aggressive corporate share repurchase activity.

While we are maintaining our positive stock market bias, we remain diligent in looking for signs the economy may slow. So far, our concerns are primarily overseas. China's growth rate remains positive but below expectations. Emerging markets continue to feel the pressure of weak oil and commodity prices. Europe's growth remains slow, although we have confidence its QE program should accelerate the continent's growth. But while we maintain a keen awareness of the macro outlook, our primary goal is to identify, buy, and hold on to leading companies whose management teams possess the skill to lead them to success regardless of the market or economic environment.

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