# Sentinel Short Maturity Government Fund

A SSIGX 817270853 S SSSGX 817270499 Manager Insights

as of 9/30/2013

## **Fund Management**

David Brownlee, CFA

Portfolio Manager Industry: 1981 Sentinel: 1993

Jason Doiron, FRM, PRM

Portfolio Manager Industry: 2000 Sentinel: 2008

### **Performance Highlights**

- The Sentinel Short Maturity Government Fund produced a total return of -0.73%\* for the third quarter of 2013. This compares to a return of +0.29% for the Barclays 1-3 Year US Government Index, +1.03% for the Barclays US MBS Index and +0.10% for the Morningstar Short Government category during the same period.
- On a year-to-date basis, the Fund returned -1.44%\*. This compares to a return of +0.30% for the Barclays 1-3 Year US Government Index, -1.00% for the Barclays US MBS Index, and -0.87% for the Morningstar Short Government category during the same period.

#### **Bond Market Review**

The volatility experienced during the second quarter spilled into the third quarter of 2013, as markets continued to debate the timing and amount of the scale back of the Federal Reserve's bond purchase program. Interest rates continued to steadily rise throughout the quarter before easing at the end of September following Federal Reserve Chairman Ben Bernanke's decision to continue buying bonds at the same pace. Yields on the US Treasury 10-year Note traded from a low of 2.48% at

the beginning of the third quarter, to a closing high of 3.00% on September 5th. Yields steadily came back in after that point, with the US Treasury 10-Year finishing the quarter at 2.61%.

Spreads in both the MBS and Corporate bonds narrowed during the quarter even though redemptions remained high in bond mutual funds and ETFs. Within the MBS sector, Fed-sensitive coupons, namely 2.5% to 3.5% 30-yr FNMAs, still underperformed those of higher coupons given the market's negative tone with respect to interest rates. Overall, the Barclays MBS Index posted a 1.03% return for the quarter. Current coupon 30-year mortgage spreads traded in a 67-to-95 basis point spread relative to the 10-year US Treasury Note, closing the quarter near the narrow end of the range, well below their 10-year averages. However, spreads on Collateralized Mortgage Obligations(CMOs), widened sharply due to slowing prepayment speeds, duration extension, and lack of participation by the Federal Reserve. CMO spreads closed the quarter at their 10-year averages relative to comparable duration US Treasury securities according to Barclays data.

### **Performance Attribution**

Against this backdrop, the Fund underperformed the Barclays US MBS Index in the third quarter of 2013 by 176 basis points. However, performance relative to the Barclays 1-3 Year US Government Index proved less challenging given the Fund's lower duration profile. The Fund underperformed primarily due to sector selection, as it was positioned heavily in short duration CMOs which widened significantly in spreads relative to US Treasury securities. Projected prepayment speeds in the MBS market declined sharply in the rising interest rate environment by as much as 3050%. This elongated cash flow streams within the sector, making both mortgage pools and CMOs slightly longer on an effective duration basis. The duration of the Barclays US MBS Index started the year at a 3.18 year duration, peaked at 5.90 years over the summer, and closed the quarter at 5.40 years. However, even with the Federal Reserve's decision not to cutback on their bond purchases in September, projected prepayment speeds in the MBS sector have been slow to react to the recent decline in interest rates. Hence, MBS cash flows are still exhibiting longer effective durations.

#### **Portfolio Positioning and Outlook**

At the end of the third quarter, the Fund's portfolio positioning consists of 97% exposure to Agency MBS, with 90% in CMOs, and 3% cash. While CMO spreads widened during the quarter, the Fund's effective duration decreased to 2.14 years, down from 2.20 years as of June 30th.

It is unclear to us when commencement of Federal Reserve tapering of asset purchases may take place, but lackluster economic data points may result in a delay of any taper. However, this does not preclude interest rates from rising further given the market's tendency to overshoot. We continue to evaluate economic conditions and any subsequent fallout on interest rates, and currently maintain a neutral stance on the bond market in terms of duration.

Data shown is historical performance for each share class and reflects reinvested distributions. Investment return and principal value will vary so that you may have a gain or loss when you sell shares. Past performance does not guarantee future results; current performance may be higher or lower than data quoted. For performance current to the most recent month-end, visit www.sentinelinvestments.com.

The Fund may use derivatives, which are financial contracts whose value depends upon or is derived from the value of an underlying asset, reference rate, or index. The Fund may use derivatives as part of a strategy designed to reduce exposure to certain risks, such as risks associated with changes in interest rates, or currency or credit risk ("hedging"). The use of derivatives may reduce the Fund's return and increase the volatility in movements in the Fund's net asset value. For additional information regarding the use of derivatives, please see the Fund's current prospectus.

The Fund is subject to interest rate risk. Bond values will generally decrease when interest rates rise and will generally increase when interest rates fall. Mortgage-backed securities (MBS) are subject to pre-payment risk. These risks may result in greater share price volatility. Fund shares are not insured or guaranteed by the US government or its agencies. \* Performance for Class A shares only at net asset value. Performance data shown does not include the effects of any sales charge. If it did, returns would be lower.

Effective duration is a measure of the sensitivity of a bond's price to changes in interest rates. The shorter (longer) the duration, the lower (higher) the interest rate risk and price volatility.

The Barclays 1-3 Year US Government Bond Index is an unmanaged index comprising US government and government agency securities with maturities between one and three

years. An investment cannot be made directly in an index.

The Barclays US Mortgage Backed Securities (MBS) Index is an unmanaged index of agency mortgage-backed pass-through securities issued by Government National Mortgage Association (GNMA), Federal National Mortgage Association (FNMA), and Federal Home Loan Mortgage Corporation (FHLMC). An investment cannot be made directly in an

The return for the Morningstar category is an average of funds within the particular category as determined by Morningstar based on investment styles as measured by their underlying portfolio holdings.

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Sentinel Short Maturity Government Fund Performance (as of 9/30/2013)			Cumulative Return YTD (%)	Average Annual Total Returns (%)				
				1 Year	3 Years	5 Years	10 Years	Since s Inception
Class A <sup>1</sup>	SSIGX	Without Sales Charge	-1.44	-1.55	0.04	1.93	2.63	4.10
		With 1% Sales Charge	-2.41	-2.51	-0.28	1.72	2.53	4.04
Class S <sup>2</sup>	SSSGX	Without Sales Charge	-1.64	-1.84	-0.30	1.55	2.21	3.59
Barclays 1-3 Year US Govt Bond Index			0.30	0.37	0.75	1.84	2.68	4.32
Barclays US MBS Index			-1.00	-1.20	2.65	4.66	4.75	6.01
Fund inc	eption date	is 3/27/1995. Total annual o	perating expe	ense rati	o A: 0.869	%, S: 1.25	%.*	

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The Fund is subject to interest rate risk. Bond values will generally decrease when interest rates rise and will generally increase when interest rates fall. Mortgage-backed securities (MBS) are subject to pre-payment risk. These risks may result in greater share price volatility. Fund shares are not insured or guaranteed by the US government or its agencies.

- 1. Performance of the Class A shares prior to June 1, 2006, has not been adjusted to reflect the decrease in the maximum 12b-1 fee from 0.35% to 0.25%. If it had, those returns would be higher. The Class A returns are based on the 1% maximum sales charge and are not adjusted to reflect a maximum sales charge of 3% in effect from June 1, 2006 to December 31, 2008. If they were, the returns would be lower.
- 2. Performance of the Class S' shares prior to their inception on March 4, 2005 is based on the performance of the Fund's Class A shares, adjusted to reflect that Class S shares do not charge a front-end sales charge and adjusted for Class S's higher expenses. The "since inception" performance data for Class S shares is calculated from March 27, 1995, which was the inception date of the Fund.
- The Barclays 1-3 Year US Government Bond Index is an unmanaged index comprising US government and government agency securities with maturities between one and three years. An investment cannot be made directly in an index.
- The Barclays US Mortgage Backed Securities (MBS) Index is an unmanaged index of agency mortgage-backed pass-through securities issued by Government National Mortgage Association (GNMA), Federal National Mortgage Association (FNMA), and Federal Home Loan Mortgage Corporation (FHLMC). An investment cannot be made directly in an index.
- \* Expense ratio data is sourced from the Fund's most recent prospectus.

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