

## MetWest AlphaTrak 500 Fund as of September 30, 2011

Following months of volatility owing to continued economic weakness and apparent intractability to the ongoing European debt problems, all that was needed for a replay of 2010 (and momentum to close out the year) was a signal of commitment from the Federal Reserve at its annual August Jackson Hole retreat that yet another round of quantitative easing was on the way. Either the markets have developed some resistance to Chairman Bernanke's verbal vaccinations or another 12 months of 9% unemployment and irresolute EU central bankers have worn down investors, as the risk markets sold off sharply during the quarter. Equities slumped by nearly 14%, while the "plus" bond sectors of U.S. high yield fell 6% and emerging markets dropped 4%. Although a U.S. Treasury flight-to-safety rally has historically been characteristic of such circumstances, Standard & Poor's early August downgrade to AA+ had the potential for considerable chaos and a spike in yields. Proving not to be the case and highlighting investor disregard for the rating agencies, UST prices climbed as the 5- and 10-Year traded below the 1% and 2% rate milestones. In concluding its scheduled September meeting, the Fed announced the Maturity Extension Program and Reinvestment Policy designed to shift \$400 billion in UST holdings to longer maturities and flatten the yield curve, which it did, bringing the 30-Year UST yield to sub-3% to end the third quarter. So, one month removed from a downgrade that would punish any other debtor with higher borrowing costs, the U.S. enjoyed apparently undiminished sponsorship and reduced interest rates. A developed world in financial turmoil and few alternatives will do that...at least for now.

The rallying UST translated to a robust return quarter for the government bond indexes, also lifting diversified investment grade benchmarks to positive returns. Highlighting the asset class, the Barclays UST Index gained 6.5% in the third quarter, as its Long component jumped nearly 25%. Though lagging the UST market, the Barclays Aggregate returned 3.8%, as each sector experienced a widening in yield spreads that was more than covered by the decline in UST rates, producing positive performance among corporate (+2.9%), mortgage-backed (+2.4%), and asset-backed (+2.4%) securities. Within the corporate sector, financial issuers faced continuing challenges due to (1) perceptions of asset quality on their balance sheets – housing and Europe exposure drawing the most concern – and (2) profit pressure arising from the Fed's "twist" Maturity Extension program, which is likely to reduce income receipts from UST investments by banks. As a consequence, financials slipped 1.4% during the quarter, as yield spreads climbed by nearly 150 basis points, significantly increasing the relative cost of capital. (Investors in financial stocks liked it less, sending shares tumbling by 22% on the quarter.) Among agency mortgages, concerns about the potential for a mass auto-refinance program widened spreads until announcement of the Fed's Reinvestment Policy, which calls for maturing agency debt proceeds and principal and interest payments from agency MBS on its balance sheet to be reinvested in agency mortgages. Not surprisingly, the increase in expected demand reversed the widening caused by fears that a rapid acceleration in prepayments would repay at par (\$100)

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**You should consider the investment objectives, risks, charges, and expenses of the Fund carefully before investing. The Fund's prospectus and summary prospectus contain this and other information about the Fund. You can find the Fund's Prospectus and other information about the Fund online at [www.mwamllc.com/literature.php](http://www.mwamllc.com/literature.php). You can also get this information at no cost by calling (800) 241-4671 or by sending an email request to [metwest-clientservices@tcw.com](mailto:metwest-clientservices@tcw.com). Please read the prospectus carefully before you invest or send money.**

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### Performance

	M Share	Benchmark <sup>1,2</sup>
Latest Quarter (%)	-15.97	-13.87
Year-To-Date (%)	-9.51	-8.68
1 Year (annualized) (%)	2.60	1.15
3 Year (annualized) (%)	3.31	1.23
5 Year (annualized) (%)	-2.95	-1.18
10 Year (annualized) (%)	1.86	2.82
Since Inception (annualized) (%)	1.46	1.75 <sup>3</sup>

For MWATX the total expense ratio is 1.89%, and the net expense ratio is 0.91%. Expenses reflect a contractual agreement by the Adviser to reduce its fees and/or absorb certain expenses until July 31, 2012, unless terminated earlier by the Board of Trustees. For more information about fees and expenses, please read the prospectus. Performance would have been lower if fees had not been waived in various periods. The Fund has experienced relatively high performance due to market conditions which may not be sustained or repeated on an ongoing basis.

<sup>1</sup> S&P 500 Index is a capitalization-weighted index of 500 stocks designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries.

<sup>2</sup> The index is not available for direct investment; therefore its performance does not reflect a reduction for fees or expenses incurred in managing a portfolio. The securities in the index may be substantially different from those in the Fund.

<sup>3</sup> The since inception return for the index reflects the inception date of the MetWest Class M Share Fund. For period 6/29/98 – 9/30/11.

As of September 30, 2011

bonds currently trading at a premium (>\$100). In the non-agency mortgage market, pricing eased as fundamental weakness persisted and appetite from investors remained limited following the government's challenged Maiden Lane II liquidation earlier in 2011.

The Metropolitan West AlphaTrak 500 Fund Class I ("Fund") returned -16.0% versus the S&P 500 Index return of -13.9% for the third quarter. Relative weakness in the spread sectors weighed on performance during the quarter, echoing one of the themes that drove performance in the second quarter. Exposure within corporates continued to favor financials and was a drag on performance as banks and brokers lagged due to potential for contagion from Europe. While the agency MBS sector underperformed overall on fears of a significant government sponsored wave of refinancings, security selection within agency mortgages was marginally additive due to a focus on less prepayment prone issues. In addition, the continued weighting in non-agency mortgage-backed issues comprised of prime, subprime, and Alt-A collateral was a detractor. Given expectations that the economic backdrop would be difficult and external catalysts – European crisis, U.S. debt ceiling debate – would likely arise periodically to trigger volatility, the recent performance pattern has not been especially surprising. Meanwhile, the conditions have afforded an opportunity to continue enhancing the Fund's return-risk profile.

Entering the last part of the year, market indications – particularly UST rates and high yield risk premiums at 800 basis points - suggest an economy at stall speed at best or on the verge of contraction at worst. Consumers are saddled with high unemployment and diminished net worth and businesses, while profitable and somewhat flush with cash, have experienced limited revenue growth and curbed appetite for investment. Meanwhile, the political tide has turned on government stimulus, with further accumulation of Federal debt no longer viewed as productive by a Congressional majority. While recognizing the challenges, a deep 2008-style recession appears unlikely. Significantly, the deleveraging that has occurred over the past three-plus years has limited the buildup of excesses that would presage a considerable pullback. As a result, the degree of decline in UST yields appears far more pronounced than supported by the fundamentals. Nevertheless, generating sufficient growth to bring down stubbornly elevated joblessness will be a central theme of the ongoing partisan rancor and upcoming Presidential campaign. Is it naïve to think any legislatively-sponsored consensus is possible? At least the "independent" Fed, though

largely exhausted of conventional measures, has pursued novel approaches to build confidence, reduce volatility, and sustain momentum. In contrast to the market signals, recent readings indicate that some pickup in activity has been apparent in the leading economic indicators, as well as manufacturing and services, while price indexes have been well removed from deflation. Just a year ago, much of the market chatter referred to potential inflation and how high UST rates might rise after the end of the Fed's second round of quantitative easing. Those fears proved premature in 2011, but can it be long before the market begins imagining a 4% 10-Year UST yield again?

Positioning of the Fund certainly imagines higher UST rates, thus informing duration that remains close to zero. Careful attention will also be paid to Fund liquidity given the potential for additional market volatility, but with lofty prices and stingy yields in the U.S. government markets, the Fund continues to underweight exposure in favor of better risk-adjusted opportunities elsewhere in the fixed income market. The most pronounced overweight is in mortgage-backed securities via a combination of agency and non-agency issues. As the Fed has renewed its commitment as the marginal buyer of MBS, pricing support should remain favorable and subject to further improvement as clarity develops around a refinancing program. Non-agency issues continue to trade at deep discounts (furthered by easing prices over the past six months), representing an attractive risk-adjusted opportunity, captured in a Fund overweight. Within corporates financials continue to represent a significant overweight as yields are suitably compensatory of the risks.

**A Word About Risk** - Fixed income investments entail interest rate risk, the risk of issuer default, issuer credit risk, and price volatility risk. Funds investing in bonds can lose their value as interest rates rise and an investor can lose principal.

Current and future portfolio characteristics and holdings are subject to change and risk. Opinions expressed are current only as of the time made, and are subject to change without notice. While we have gathered this information from sources believed to be reliable, MetWest cannot guarantee the accuracy of the information provided. Source for the statistical and economic data cited in this report is Bloomberg. This commentary contains material that is protected, individually and collectively, by copyright, trademark or other proprietary rights of Metropolitan West Asset Management, LLC, or others as indicated.