

Seix Investment Advisors Perspective

ABOUT THE BOUTIQUE: Seix Investment Advisors LLC



Seix Investment Advisors LLC (Seix) is a fundamental, credit-driven fixed-income boutique specializing in both investment grade and high yield bond management. Seix has applied its bottom-up, research-oriented approach to fixed income management for over 15 years. The firm's success can be attributed to a deep and talented group of veteran investment professionals, a clearly defined investment approach and a performance-oriented culture that is focused on delivering superior, risk-adjusted investment performance for our clients.

The Author:

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Chief Investment Officer and
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Jim is Chief Investment Officer and leads the High Grade division of Seix. Prior to joining the firm in 2008, Jim was Head of Investment Grade Corporate & High

Yield Bond Management for American Century Investments, Chief Investment Officer at Westmoreland Capital Management and Managing Director of High Grade and High Yield Fixed Income at UBS Global Asset Management. Jim's High Grade team sub-advises several of the RidgeWorth Funds, including the RidgeWorth Investment Grade Bond Fund which won a Lipper Performance Award in 2009. He has appeared on CNBC and Bloomberg television, and has been quoted in a range of national publications. Jim received a B.S. degree from St. Francis College and an M.B.A. degree from Fordham University. Jim has more than 25 years of investment management experience.

REVIEW OF FIRST QUARTER 2010

Risk assets continued to outperform in Q1, lifted by a March rally that fed off a robust stock market (S&P500 +6%) and consistent cash inflows into bond funds of all types. As Exhibit 1 below illustrates, the total return for the Barclays Aggregate and various other sectors were solid in the first quarter; this was true on both a total return and excess return basis. All bond market return data refer to Barclays Indices:

Exhibit 1	First Quarter 2010 Total Return	First Quarter 2010 Excess Return	12-Month Total Return
Aggregate	1.78%	0.78%	7.69%
Treasury	1.12%	n/a	-1.18%
Agency	1.19%	0.32%	3.31%
Mortgage-backed (MBS)	1.54%	0.69%	5.21%
Asset-backed (ABS)	2.22%	1.33%	18.53%
Collateralized mortgage-backed (CMBS)	9.10%	7.95%	42.81%
Corporate	2.30%	1.14%	23.80%
High Yield	4.62%	3.50%	56.18%
Ba/B	4.03%	2.91%	41.39%
Ba	4.50%	3.34%	40.04%
B	3.54%	2.46%	43.19%
Caa	5.26%	4.13%	91.53%
Ca-D	12.55%	11.58%	170.20%
Loans	4.81%	n/a	45.96%
S&P 500	5.39%	n/a	49.77%

Sources: Barclays Capital, S&P

Credit in both high grade and high yield performed well; CMBS was the star amongst the securitized sectors. Treasury returns, while lower than most investment grade spread sectors, were still positive as rates managed to edge lower across most of the yield curve.

While equity markets continue to project a "glass half full" approach and rally, global issues like Europe's sovereign debt crisis and domestic issues like record foreclosure filings continue to remind us that the recovery remains fragile at best. Additionally, the Federal Reserve consistently highlights multiple headwinds facing the economy and reaffirms its commitment to exceptionally low rates "for an extended period." While risk levels are down dramatically from a year ago, they remain elevated as we navigate a recovery cycle that is unlikely to resemble anything we've experienced before.

While our focus in this update will be Q1 2010 and the balance of the year, it's worth noting the 12-month return data included in the table above. The trailing returns of some of these sectors are truly amazing; this is illustrative of the incredibly unique period under which we've been investing and perhaps an ominous foreshadowing of the potential volatility that could become the norm in capital markets in the 21st century.

CYCLICAL VS. SECULAR FORCES

Our year end review laid out a simple thesis describing broader secular forces that were going to challenge this recovery and make it unlike the more cyclical recovery the economy typically exhibits after a recession. Without repeating those exhibits we're compelled to remind investors that all these forces remain with us today. The consumer remains over-leveraged; this is an adjustment process that takes years, not quarters. The ability of the economy to generate job growth remains challenged; unemployment remains very high at 9.7% and even the most optimistic of forecasts has the economy spending at least four years replacing the 8.4 million jobs lost during this

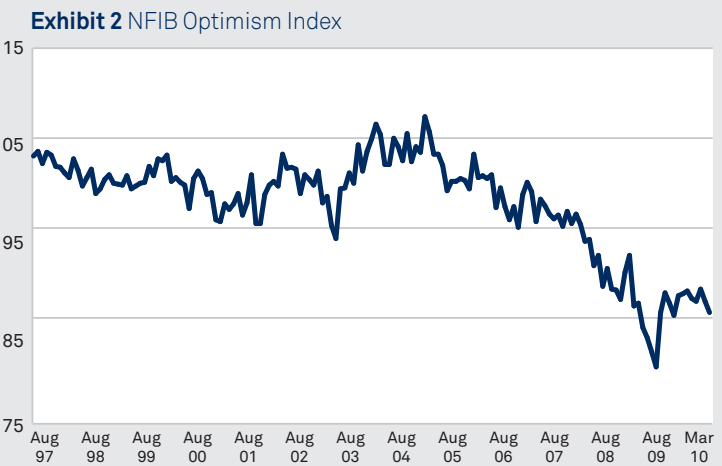
recession. Regulatory reform is upon us, as illustrated by the efforts of Senators Dodd and Shelby, in their effort to craft bipartisan legislation that doesn't garner yet another party line vote. Taxes will surely be rising to pay for the cyclical responses, both fiscal and monetary, that were enacted over the past two years battling this "great recession." These represent a variety of different forces, but they are all headwinds; since the tailwinds of the fiscal and monetary response are diminishing, the second half of 2010 will be very challenged to produce the organic, sustainable economic recovery that is priced into many risk assets right now.

A primary dichotomy in the economy between small business and big business remains front and center and is perplexing to investors and analysts alike. It was a feature of our 2010 outlook and warrants continued emphasis. Small business sentiment remains fairly pessimistic and seemingly isn't participating in the recovery we've witnessed over the last six to nine months. Exhibits 2 and 3 illustrate the difference in this recovery's perception as it's seen by small business – National Federation of Independent Business (NFIB) survey (see *Exhibit 2*) – and big business – Institute for Supply Management (ISM) surveys (see *Exhibit 3*).

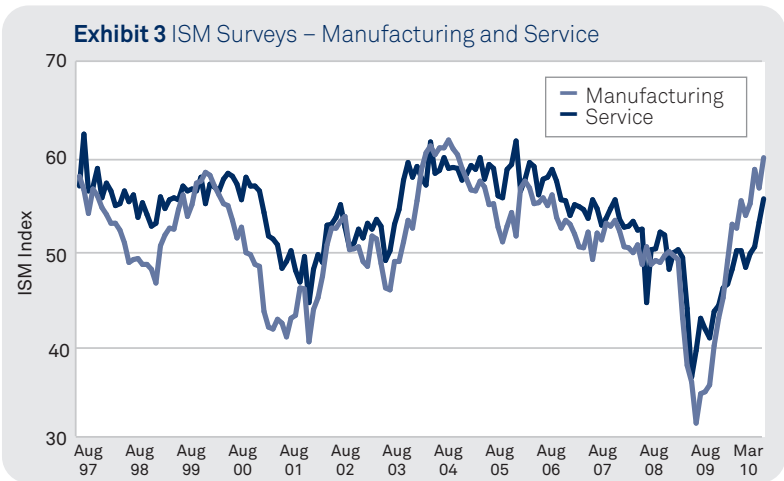
Going back to last March the NFIB optimism index was bottoming (81.0); the April '09 reading saw the index bounce to 86.8. On April 13th of this year we learned that the latest (March) NFIB survey came in at 86.8; essentially unchanged versus 11 months ago. Over the same period, we've seen the ISM surveys gain 19+ points (manufacturing) and 11+ points (services). Bill Dunkelberg, NFIB's chief economist, stated in the March release, "Something isn't sitting well with small business owners. Poor sales and uncertainty continue to overwhelm any other good news about the economy."

The employment situation appears to be at an inflection point as well as we move towards the summer. The establishment survey has produced positive payroll growth in two of the last three months; albeit a fairly tepid +54,000 three-month average that includes temporary census positions. While we've moved out of the period of massive payroll reduction, the road to recovering the jobs lost during this cycle is daunting to say the least. Working with a very optimistic assumption that the economy can suddenly shift to producing 300,000 jobs per month, that would amount to about 175,000 new jobs net of growth in the labor force (the economy requires approximately 125,000 jobs per month to just employ new entrants into the labor force). Hence, to re-capture the 8.4 million jobs lost in this recession requires about four years of uninterrupted 300,000 per month payroll gains. Just how optimistic is that assumption? Well, since 1950 the monthly payroll gain has been 300,000 or better about 16% of the time!

Housing has also seen its share of mixed news of late. New home sales have bounced back to a 411,000 annualized pace in March, up over 16% from the 353,000 pace at year end (see *Exhibit 4*). Despite this modest recovery, new home sales remain well below the 734,000 long-term average witnessed since 1980. Existing home sales have been a bit softer of late, with a March reading of 5.35 million against 5.44 million at year end. This series however remains above the 4.17 million average seen since 1980. This, not surprisingly, has been due to a high percentage of "distressed" transactions taking place over the last few years. Additionally, the tea leaves here remain clouded by the continued influence of the governments' fiscal profligacy. The original home buyer tax credit that was slated to expire last November was extended to April 30th of this year; the program was even expanded beyond just first time home buyers. Hence, as we roll into the traditional peak season for real estate, we're still looking at a market very much under the influence of government policy. We can only speculate what the current underlying turnover rate is in housing and will have to wait until later in the season to see what kind of fallout the market experiences after the incentive program expires.



Source: National Federation of Independent Business



Source: Institute for Supply Management

Exhibit 4 Housing Statistics	March 2010	Long-Term Average
New Home Sales	411,000	743,000
Existing Home Sales	5.35 Million	4.17 Million
Existing Homes for Sale	3 Million	2.3 Million
Supply in Months	7.7 Months	7.1 Months

Source: National Association of Realtors

Other Considerations: Expiring incentives, shadow inventory and strategic defaults

Apart from the pending conclusion of the government's tax incentive, you can't address housing and not talk about some of the additional stresses it faces. The official housing inventory statistics alone are manageable. The current stock of new homes for sale has been coming down for years and is well below its long-term average. The inventory of existing homes for sale has also been coming down for nearly two years, but remains well above its long-term average. Single family homes for sale in March came in at 3 million units; while this is down from its April 2008 peak of 3.9 million, since 1982 (data inception) it has averaged about 2.3 million units. Even at today's elevated sales pace, the current stock represents about 7.7 months of supply against a 7.1 month average since 1982. Unfortunately, this elevated level of official housing stock is only the beginning.

Shadow inventory, which we define as homes that may ultimately come onto the market due to default on the underlying mortgage, is what genuinely clouds the outlook for further housing market gains. The data we have so far indicates there are approximately 8 million housing units that are either delinquent, in foreclosure, or have already been repossessed by banks (REO). This number represents about 15% of all first-lien residential mortgage loans outstanding. Somewhere in the neighborhood of 3 million units are already in the "REO" classification or somewhere in the foreclosure pipeline; this is already part of the shadow inventory. The next concern becomes what percentage of those already delinquent loans eventually default and are put up for sale. Finally, and potentially much more importantly, what happens to the approximate 48 million mortgages that are still current? Distilling these moving parts down to only one number is predicated on a multitude of assumptions regarding delinquency roll rates, home price forecasts, unemployment forecasts, government programs, etc. Additional factors that have to be accounted for include a new concept called "strategic default," whereby a homeowner perfectly capable of servicing a housing debt chooses to walk away from the property when the loan to value ratio moves beyond some acceptable threshold. To the extent that the "social stigma" traditionally associated with default get diminished (moral hazard risk), borrower behavior will become that much more erratic and unpredictable. Many analysts have opined on this shadow inventory issue; a broad range of 5 million to 22 million would round out the best case/worst case expectation. This is not the backdrop for a healthy housing recovery in the short or medium term.

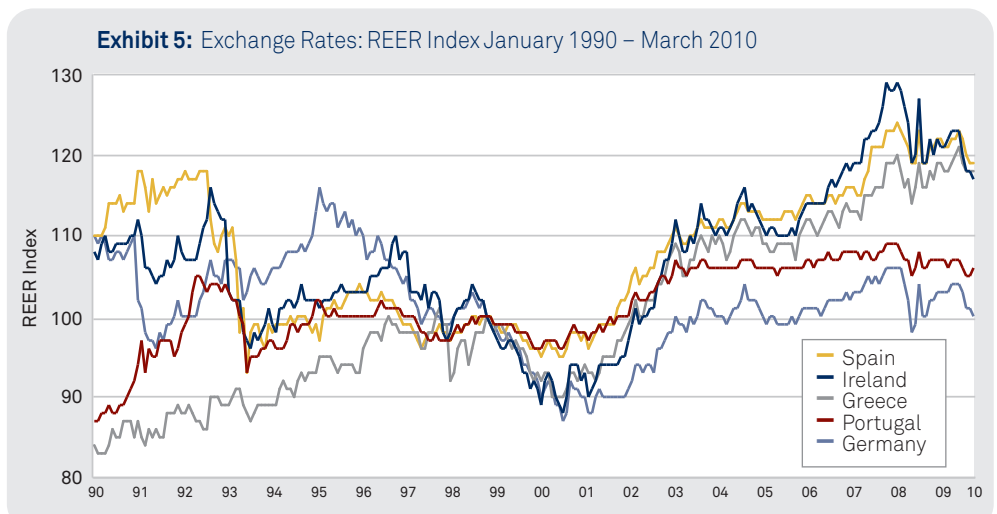
GLOBAL HEADWINDS; EUROPE'S PERIPHERY

If you've read any Wall Street research or watched any business TV recently then the sovereign debt crisis is something you've definitely heard of. It seems as if we've already had 12 rescue packages for Greece, with considerable anxiety remaining as it relates to the rest of the "PIIGS" (Portugal, Ireland, Italy, Greece, and Spain). It may seem like a problem in a faraway place, but with the interconnected nature of capital markets, the ramifications are real for all investors and important to monitor.

Greece's ailments have been blamed on fiscal and debt sustainability concerns. Lax fiscal policy combined with three-digit debt-to-GDP ratios are indeed significant problems. However, we think these are merely the symptoms of the larger problem of a lack of competitiveness emanating from exchange rate overvaluation, which leads to little or no growth. Once Greece and the rest of peripheral Europe decided to surrender monetary and exchange rate flexibility when the Euro was introduced to world financial markets, they linked their growth potential to quickly reducing their cost structure to that of Germany and France. A failure to do so would cause their economies to become uncompetitive, thereby curtailing the growth potential of their respective economies.

In the years following the establishment of the Euro the inflation rates of the periphery outstripped the inflation rates of Germany and France. As a consequence, the private sector suffered and economic growth came from either large public spending as in the cases of Greece and Portugal, or excess spending in the key non-tradable sector of real estate in the cases of Ireland and Spain. Both spending-induced fiscal deficits and real estate bubbles were unsustainable and markets did ultimately bring the excesses to an end. But now that the real estate bubbles in Ireland and Spain have burst and markets will no longer tolerate excessive spending in Greece and Portugal, these four countries are still left with the original conundrum of exchange rate overvaluation and limited prospects for growth.

Exhibit 5 shows Real Effective Exchange Rate (REER) for selected European countries. REER is an indicator used to assess a country's international competitiveness in terms of its foreign exchange rate. Greece, Spain and Ireland REER levels indicate these economies are around 20% less competitive than Germany; Portugal is around 6% less. Furthermore, these REER levels indicate peripheral Europe's competitiveness levels are close to their lowest for the last 20 years.



Source: Seix Investment Advisors LLC

Growth needs to be restored in the periphery while simultaneously implementing austere fiscal programs, a very difficult task. A major fiscal adjustment is likely to deepen the recession in these countries in the months ahead, making it difficult to reduce their fiscal deficits. Failure to show improved fiscal numbers and a grinding recession in coming quarters could lead to persistent upward pressure on bond yields, and continued reluctance on the part of investors to fund the large fiscal needs of these countries (*Exhibit 6*). If markets were to become reluctant to fund Greece, Portugal, Ireland and Spain, the financing needs of these countries would seem even beyond the scope of the International Monetary Fund (IMF) and the more healthy European Union (EU) community. For example, the IMF would be able to lend them a combined amount of around EUR 75 billion (assuming 12 times their IMF quota). This is well short of the combined EUR 670 billion in financing needs over the next three years for these countries beginning in 2010.

The EU and the IMF are advising these four countries to follow the same recipe of large scale fiscal retrenchment and massive wage cuts to restore economic competitiveness. Sounds simple on the surface, but consider a similar dose of austerity right here at home. Had the U.S. been required to impose such austerity measures in the midst of our economic crisis, most economists including Ben Bernanke, Jean-Claude Trichet, and the IMF itself would agree that this would have led us into a second great depression. The difference between these countries and the U.S., apart from the obvious that we remain

Exhibit 6	Financing Needs (EUR bn)				IMF Quota (EUR bn)	Max IMF Potential Lending (EUR bn) 1/
	2010	2011	2012	2010-12		
Greece	38	45	46	129	0.9	11
Spain	152	147	124	423	3.4	41
Ireland	19	21	18	58	0.9	11
Portugal	20	23	17	60	1.0	12
Total	229	236	205	670		75

1/ Assumes lending equal to 1 times quota
Sources: Goldman Sachs, IMF

the world's lone superpower and reserve currency, is that the top priority for the EU is preserving the Euro. All other considerations, like what's in the best interest of each individual country, are secondary and tertiary. With a focus on the preservation of the Euro alone, austerity and economic pain is the only policy option available to the EU authorities. Unfortunately, such a policy mix is likely to spell something akin to a great depression for these countries; this probably leads to difficult social tensions and declining tax revenues. As a result we believe several of these countries may ultimately have to restructure their debt. Sovereign restructurings on this scale will reverberate across the global capital markets unlike any we've experienced in the emerging markets historically.

OUTLOOK AND POSITIONING

Risk assets performed well in the first quarter, lifted by both a fundamental bounce off the recession lows and consistent inflows into bond funds; taxable bond funds have taken in \$399 billion over the past five quarters (ICI data). Credit in both high grade and high yield produced solid excess return while CMBS led the way amongst the securitized sectors. Fortunately, we were positioned to benefit from these trends. Spread tightening is likely to slow/pause and returns will more likely be pure yield versus capital appreciation (additional tightening) over the next few quarters. While risk levels are down dramatically from one year ago, they remain elevated as we navigate a recovery cycle that is unlikely to resemble anything we've experienced before.

We remain overweight investment grade corporate bonds and Ba/B (high quality) high yield, but tilt defensively with an industrial and utility bias versus financials or consumer cyclical. Despite a significant rally, we remain overweight CMBS, as the overall yield level remains wide compared to historical levels. Commercial real estate remains under pressure in many markets, but we are comfortable with our exposure and rely on very careful analysis of deal structure and collateral performance. Security selection is critical in this market as no two deals are alike. Agency MBS valuations remain rich, despite the Federal Reserve's completion of its purchase program; we're underweight this sector and anticipate an eventual re-pricing in the absence of the Fed. Due to similarly rich valuations and loss of Fed support, we are also void any Agency debenture exposure. Finally, the yield curve remains historically steep and we've positioned for flattening as the challenges of this recovery become more apparent in the second half of 2010 and investors reach for yield and capital appreciation further out the yield curve. The benign inflationary environment further supports this yield curve posture.

The recovery to date has been largely an inventory correction and the response to various government stimulus programs; we believe that very little will prove to be organic or sustainable. Consumer spending has proven more resilient than anticipated, but this has come at the expense of savings. The consumer remains over-leveraged and the balance sheet repair process can't rely again on asset appreciation; hence, further gains in spending are unlikely. Capital expenditure plans remain tepid with median guidance across a broad industrial base up only 0.1% versus 2009 and down 7% versus a three-year average. The tailwind from the stimulus plan is also diminishing and won't contribute significantly to growth in the second half of the year; without consumption or capital expenditures filling the void, it's difficult to see what makes this recovery sustainable.

Barclays U.S. Aggregate Bond Index is an unmanaged index of investment grade U.S. bonds, which includes reinvestment of any earnings and is widely used to measure the overall performance of the U.S. bond market. Treasury, Agency, mortgage-backed (MBS), asset-backed (ABS), collateralized mortgage-backed (CMBS) and corporate bonds are subsets of the Barclays U.S. Aggregate Bond Index.

Barclays U.S. Corporate High Yield Bond Index is an unmanaged market value-weighted index that covers the universe of fixed rate, non-investment grade debt. All securities rated below BBB/Baa are considered non-investment grade.

Standard & Poor's 500 Index is an unmanaged index of 500 selected common large capitalization stocks (most of which are listed on the New York Stock Exchange) that is often used as a measure of the U.S. stock market.

Investors cannot invest directly in an index.

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