# Thornburg Multisector Opportunistic Strategy

**Portfolio Manager Commentary**
**31 March 2024**

Thornburg

## Investment Strategy

Designed to be a flexible, alpha-seeking fixed income strategy with the goal to provide investors with attractive risk-adjusted returns by investing in fixed income securities across sector, credit quality, and geography. Over time, we aim to generate returns above that of core fixed income strategies with incrementally higher risk.

## Market Review

Economic data released during the first quarter of 2024 was supportive of the narrative that U.S. growth would not only remain resilient but resume a cyclically upward trend. Both nonfarm payroll releases in January and February exceeded analyst expectations, while the final measure of fourth quarter GDP was revised up from 3.2% to 3.4%. The downward trajectory in inflation remained stalled, with year-over-year CPI down only a tenth of a percentage point to 3.8%. Given this backdrop, Fed communication focused on patience and the need for better inflation data before committing to a rate cut. Markets repriced a higher for longer path, resulting in the 10-year U.S. Treasury yield rising from 3.88% to 4.20% over the quarter. Solid economic data helped keep the broader risk rally going, with spreads tightening across fixed income sectors and lower quality outperforming higher quality on a relative basis.

## Portfolio Managers


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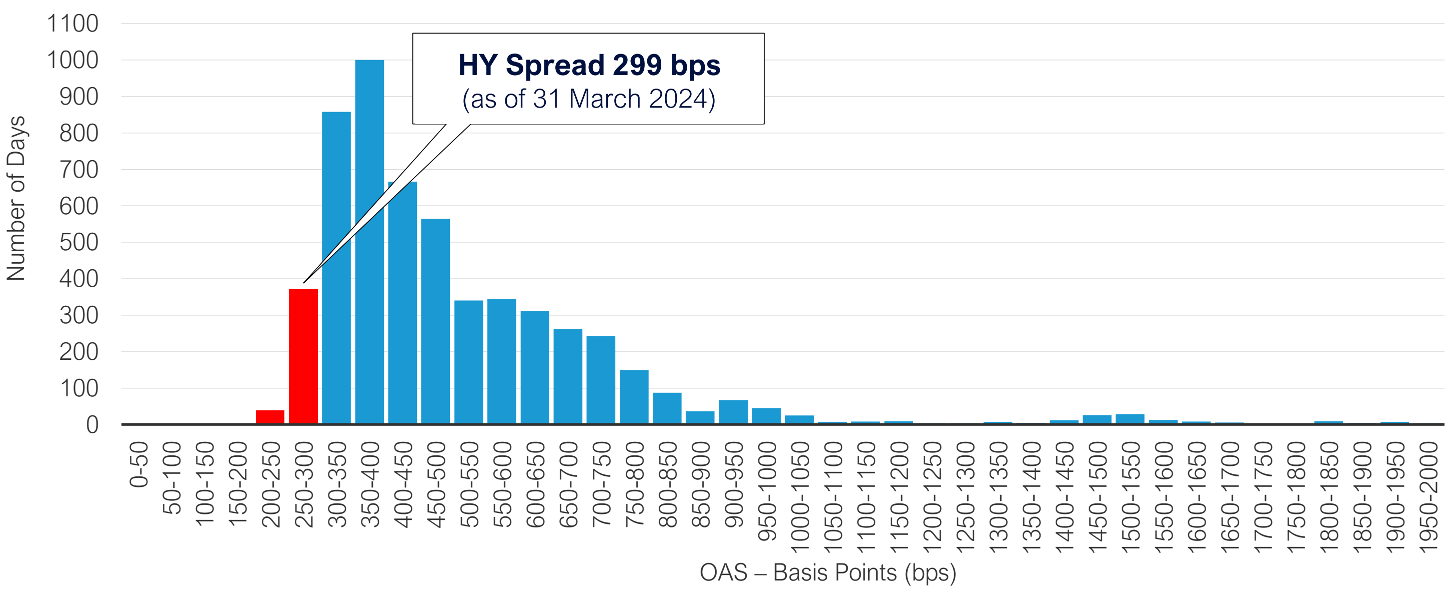
Supported by the entire Thornburg investment team


**Figure 1: Risky Fixed Income Sector Spreads Are at Levels That Do Not Justify Macro Uncertainty**

**High yield corporate spreads are at levels that price in too much optimism**

**HIGH YIELD OAS: DAILY DATA POINTS SINCE 2002**




*The performance data quoted represents past performance; it does not guarantee future results.*

Source: Bloomberg

## First Quarter 2024 Performance Highlights

- In 1Q24 the portfolio (net of fees) returned 0.93%, 140 basis points ahead of the Bloomberg U.S. Universal Index. Year to date the portfolio (net of fees) returned 0.93%, 140 basis points ahead of the Index.
- The portfolio's structural short duration position versus the index was the primary contributor in a quarter marked by rising rates. The portfolio held an average duration of 3.73 years for the first quarter.
- Our allocation to non-agency RMBS (CMO) contributed to relative performance as mortgage credit spreads tightened due to positive investor sentiment and continued robust housing fundamentals.
- Exposure to both investment-grade and high-yield corporates was beneficial, as credit performed well and consistent with the broader risk rally.
- Exposure to low-coupon MBS pass-throughs was a modest contributor to performance. The mortgage basis (i.e. spread between Treasuries and MBS) rallied into the quarter-end after initially widening earlier in the period.
- There were no material detractors from a sector perspective during the first quarter.

## Current Positioning and Outlook

The rally in risk assets over the past few months has contributed to a virtuous circle where household wealth gains have fueled better investor sentiment and could potentially serve as a tailwind for private consumption going forward. Recession is now the bear, not the base case, but firm data flow during the January through March period was also coupled with a few mixed signals. Consumer delinquencies continue a slow but consistent march higher, decoupling from a still tight labor market. Disposable income, on a nominal basis, has increased at a pace faster than pre-COVID trends, but real disposable income gains lag, suggesting the consumer is having difficulty keeping pace with inflation. These mixed signals will need to be monitored given the extent to which fixed income spreads have grinded tighter. Though recession is not a concern for now, it should be noted that over the past 70 years, it has taken an average of ten quarters after an initial Fed hike for a recession to occur. Markets cannot declare victory yet during this particular cycle, as we are currently only eight quarters past the first hike.

During the Fed's March meeting, the average dot for number of Fed cuts by year-end remained at three. The data flow, both on the growth and inflation front, do not support the ability for the FOMC to deliver on this forecast.

**ANNUALIZED RETURNS** (AS OF 31 MARCH 2024)

| THORNBURG MULTISECTOR OPPORTUNISTIC STRATEGY (%) | QTR | YTD | 1-YR | 3-YR | 5-YR | 10-YR | ITD (1 JAN 08) |
|---|---|---|---|---|---|---|---|
| Composite (Gross) | 1.07 | 1.07 | 6.34 | 2.06 | 4.08 | 4.14 | 6.08 |
| Composite (Net) | 0.93 | 0.93 | 5.75 | 1.47 | 3.48 | 3.51 | 5.29 |
| Bloomberg U.S. Universal Index | -0.47 | -0.47 | 2.67 | -2.11 | 0.69 | 1.83 | 3.05 |

**CALENDAR YEAR RETURNS**

| THORNBURG MULTISECTOR OPPORTUNISTIC STRATEGY (%) | 2023 | 2022 | 2021 | 2020 | 2019 | 2018 | 2017 | 2016 | 2015 | 2014 |
|---|---|---|---|---|---|---|---|---|---|---|
| Composite (Gross) | 8.26 | -5.59 | 3.39 | 8.90 | 8.56 | 1.38 | 7.27 | 8.94 | -1.15 | 4.34 |
| Composite (Net) | 7.67 | -6.14 | 2.77 | 8.25 | 7.92 | 0.77 | 6.60 | 8.25 | -1.77 | 3.66 |
| Bloomberg U.S. Universal Index | 6.17 | -12.99 | -1.10 | 7.58 | 9.29 | -0.25 | 4.09 | 3.91 | 0.43 | 5.56 |

In US$ terms. **Returns may increase or decrease as a result of currency fluctuations.**
Periods less than one year are not annualized. ITD is inception to date.

*Performance data for the Multisector Opportunistic Strategy is from the Multisector Opportunistic Composite, inception date of 1 January 2008. The Multisector Opportunistic Composite includes all discretionary accounts invested in the Multisector Opportunistic Strategy. Returns are calculated using a time-weighted and asset-weighted calculation. Returns reflect the reinvestment of income and capital gains. Periods less than one year are not annualized. Individual account performance will vary. The performance data quoted represents past performance; it does not guarantee future results. Gross of fee returns are net of transaction costs. Net of fee returns are net of transaction costs and investment advisory fees. For periods prior to 2011, net returns for some accounts in the composite also reflect the deduction of administrative expenses. Thornburg Investment Management Inc.'s fee schedule is detailed in Part 2A of its ADV brochure. Performance results of the firm's clients will be reduced by the firm's management fees. For example, an account with a compounded annual total return of 10% would have increased by 159% over ten years. Assuming an annual management fee of 0.75%, this increase would be 142%.*

In the absence of recession, one cut appears to be far more appropriate, with inflation no longer showing any material downward momentum. Average hourly earnings growth (year-over-year) has stabilized in the mid 4% level, and the rebound in housing prices tends to be a leading indicator of the direction of core CPI. The fall election also looms over Fed decision making, and the FOMC will want to steer clear from policy decisions that could be interpreted as politically motivated.

Nominal and real yields pushed higher in the first quarter in response to the data and the paring of Fed cut rate expectations. We added rate risk into the sell-off, with duration positioned at 3.9 years as of early April versus 3.5 years to begin 2024. Meanwhile, agency mortgage-backed securities (MBS) continue to demonstrate compelling relative value versus high grade credit, although valuations are somewhat neutral versus non-agency RMBS. Our exposure is in low coupon pass-throughs which have discounted dollar prices and provide both attractive total return potential and fundamental diversification to credit.

Within non-agency RMBS (CMO), fundamentals remain positive given robust underwriting and low housing LTVs, with spreads on senior bonds attractive relative to investment-grade credit. Our exposure has been focused on non-QM, but we see good relative value additions within reperforming loan (RPL) securities. In ABS, our caution on the consumer continues as delinquencies slowly but consistently rise, though senior bonds with shorter weighted average lives are well protected and provide good front end yield. Although CMBS represents a small percentage in the portfolio, there have been select opportunities to take advantage of investor caution in the space to buy attractively priced bonds backed by strong, cash-flowing properties.

Spreads in both investment-grade and high-yield corporates continued their grind tighter in the first quarter. Within the latter, high single digit yields provide good total return potential and protection to wider spreads. However, spread levels do not compensate investors for uncertainty and the potential for higher defaults. On the credit quality stack, we prefer BBB corporates to the BB/B cohort as fundamentals look more appealing on a relative basis. Our investment-grade exposure, however, is focused on defensive, strong cash flow businesses. Spreads are also tight relative to history, but the new issuer calendar remains robust and therefore provides select relative value opportunities going forward.

Within emerging markets, valuations overall in the sovereign and corporate space are tight while interest coverage and leverage have ticked higher. While issuance is running well ahead of previous years, we find the compensation relative to quality to be largely insufficient. We are being highly selective on additions we seek to avoid macro tail risks. Potential opportunities include mispricing which may occur through the busy EM election calendar, as well as in countries where rate cuts may improve the economic outlook and outweigh any inflation or currency depreciation concerns.

## Portfolio Characteristics

| PORTFOLIO STATISTICS | REP. ACCT. |
|---|---|
| Weighted Average Coupon | 4.0% |
| Weighted Average Price | 94.8 |
| Average Credit Quality | A- |
| Average Effective Maturity | 5.2 Years |
| Effective Duration | 3.8 Years |

| ASSET CLASS WEIGHTS (%) | REP. ACCT. |
|---|---|
| Corporate | 42.2 |
| U.S. Treasury | 17.0 |
| ABS | 12.0 |
| CMO | 9.5 |
| Mortgage Pass Through | 7.9 |
| CMBS | 1.9 |
| Bank Loans | 1.0 |
| Non-U.S. Treasury | 0.9 |
| Preferred Stock | 0.2 |
| Municipal Bonds | 0.1 |
| Common Stock | 0.0 |
| Cash | 7.4 |

| CREDIT QUALITY RATINGS (% EX-EQUITY) | REP. ACCT. |
|---|---|
| U.S. Government | 25.6 |
| AAA | 10.0 |
| AA | 2.3 |
| A | 12.4 |
| BBB | 22.2 |
| Below Invest. Grade | 16.4 |
| NR | 3.7 |
| Cash | 7.4 |

| TEN LARGEST COUNTRIES (%) | REP. ACCT. |
|---|---|
| United States | 80.6 |
| Canada | 1.9 |
| Japan | 0.8 |
| Mexico | 0.8 |
| United Kingdom | 0.7 |
| Australia | 0.6 |
| China | 0.6 |
| Brazil | 0.4 |
| United Arab Emirates | 0.4 |
| Nigeria | 0.3 |

Source: FactSet and Thornburg

Cash may include cash equivalents and currency forwards. Holdings are classified by country of risk as determined by MSCI and Bloomberg. Portfolio attributes can and do vary. Weights are percentages of total portfolio, unless otherwise noted. Holdings may change daily. Credit quality ratings use the highest rating available from either S&P Global Ratings or Moody's Investors Service. Where neither rating is available, we have used ratings from other nationally recognized statistical rating organizations (NRSROs). "NR" = Not Rated. Please see disclosure page for other important disclosures and definitions.

## Important Information

*The performance data quoted represents past performance; it does not guarantee future results.*

Unless otherwise noted, the source of all data, charts, tables and graphs is Thornburg Investment Management, Inc., as of 31 March 2024

Investments in the Strategy carry risks, including possible loss of principal. Carefully consider the Strategy's investment objectives, risks, and expenses before investing. There is no guarantee that the portfolio will meet its investment objectives.

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Portfolio holdings and characteristics shown herein are from a representative account managed within the investment composite. The representative account is selected based on account characteristics that Thornburg believes accurately represent the investment strategy as a whole. Should these characteristics change materially, Thornburg may select a different representative account. Holdings may change daily and may vary among accounts, which may contribute to different investment results. The representative account information is supplemental to the strategy's composite and GIPS compliant presentation.

Basis Point (bp) – A unit equal to 1/100th of 1%. 1% = 100 basis points (bps).

OAS (Option Adjusted Spread) - The difference between the yield of a fixed income instrument and the duration-matched Treasury yield assuming the instrument had no embedded options (such as an issuer's option to call a bond at a future date). Option-adjusted spreads enable investors to separate out embedded options and better judge the degree to which an instrument's yield compensates them for credit risk, liquidity risk, or other such factors.

U.S. Treasury securities, such as bills, notes and bonds, are negotiable debt obligations of the U.S. government. These debt obligations are backed by the "full faith and credit" of the government and issued at various schedules and maturities. Income from Treasury securities is exempt from state and local, but not federal, taxes.

Fed Funds Rate - The interest rate at which a depository institution lends immediately available funds (balances at the Federal Reserve) to another depository institution overnight.

Federal Open Market Committee (FOMC) - The branch of the Federal Reserve Board that determines the direction of monetary policy. The FOMC is composed of the board of governors, which has seven members, and five reserve bank presidents. The president of the Federal Reserve Bank of New York serves continuously, while the presidents of the other reserve banks rotate their service of one-year terms.

Consumer Price Index (CPI) - Index that measures prices of a fixed basket of goods bought by a typical consumer, including food, transportation, shelter, utilities, clothing, medical care, entertainment and other items. The CPI, published by the Bureau of Labor Statistics in the Department of Labor, is based at 100 in 1982 and is released monthly. It is widely used as a cost-of-living benchmark to adjust Social Security payments and other payment schedules, union contracts and tax brackets. Also known as the cost-of-living index.

A bond credit rating assesses the financial ability of a debt issuer to make timely payments of principal and interest. Ratings of AAA (the highest), AA, A, and BBB are investment-grade quality. Ratings of BB, B, CCC, CC, C and D (the lowest) are considered below investment grade, speculative grade, or junk bonds.

Credit Spread/Quality Spread - The difference between the yields of securities with different credit qualities.

Duration - A bond's sensitivity to interest rates. Bonds with longer durations experience greater price volatility than bonds with shorter durations.

Yield Curve - A line that plots the interest rates, at a set point in time, of bonds having equal credit quality, but differing maturity dates.

Asset-backed Security (ABS) - A security whose value and income payments are derived from and collateralized (or "backed") by a specified pool of underlying assets. The pool of assets is typically a group of small and illiquid assets that are unable to be sold individually. Pooling the assets into financial instruments allows them to be sold to general investors, a process called securitization, and allows the risk of investing in the underlying assets to be diversified because each security will represent a fraction of the total value of the diverse pool of underlying assets.

Mortgage-backed Security - A type of asset-backed security that is secured by a mortgage or collection of mortgages. These securities must be grouped in one of the top two ratings as determined by a accredited credit rating agency and usually pay periodic payments that are similar to coupon payments. The mortgage must have originated from a regulated and authorized financial institution.

Mortgage Pass-Through - A security consisting of a pool of residential mortgage loans. Payments of principal, interest and prepayments are "passed through" to investors each month.

RMBS (Residential Mortgage Backed Securities) - A type of mortgage-backed debt securities where the cash flows are derived from residential mortgages.

The Bloomberg U.S. Universal Index (BBG US Universal TR Value) represents the union of the U.S. Aggregate Index, U.S. Corporate High-Yield, Investment Grade 144A Index, Eurodollar Index, U.S. Emerging Markets Index, and the non-ERISA eligible portion of the CMBS Index. The index covers USD denominated, taxable bonds that are rated either investment-grade or below investment-grade.

Portfolio construction will have significant differences from that of a benchmark index in terms of security holdings, industry weightings, asset allocations and number of positions held, all of which may contribute to performance, characteristics and volatility differences. The index shown is unmanaged, reflect total returns and assume the reinvestment of all income in U.S. dollars. It does not reflect any management fees or brokerage expenses associated with a portfolio's returns. Returns for an actual portfolio may differ from those of an index due to (among other things) differences in timing and the amount invested and fees and expenses. Investors may not make direct investments into any index.

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*Includes assets under management ($43.2B) and assets under advisement ($1.1B).

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