

# Strategic Income Fund

## FUND FACTS

### OBJECTIVE

Seeks high current income with a secondary objective of capital growth

Share class	Y
Inception	12/1/1999
Ticker	NEZYX
CUSIP	543487250

## Market Conditions

- The global bond markets delivered positive returns in the third quarter, building on their gains in the first half of the year. Bonds were well supported by the combination of slowing economic growth, low inflation worldwide, and the accommodative policies of the US Federal Reserve (Fed) and other major central banks. The Fed cut interest rates by a quarter point on both August 1 and September 19, bringing its benchmark fed funds target rate to a range of 1.75% to 2.00%. In addition, the markets appeared to be pricing in the likelihood of further reductions by mid-2020.
- These circumstances provided a boost to US Treasurys, fueling a rally across the maturity spectrum. Longer-term bonds (those with maturities of ten years and above) generated the best performance and outpaced the two- to five-year segment. The gap between the two- and ten-year yields narrowed as a result, leading to a flattening of the yield curve. The curve in fact inverted for a brief stretch in late August, with the ten-year yield trading below that of the two-year note. Since inversions have often been a leading indicator of recessions, this development contributed to the mounting concerns about the economic outlook.
- Investment grade corporate bonds produced positive returns and exceeded the gains for US Treasurys, continuing a trend that was in place during the first half of the year. At a time of generally uneven market sentiment, investors gravitated to the combination of corporates' above-average quality and yield advantage over government issues.
- High yield bonds, while generating a gain in absolute terms, finished slightly behind investment-grade issues. Returns were dampened by the combined effect of slowing economic growth and shaky performance for both crude oil and global equities. In addition, yield spreads (i.e., the yield advantage over US Treasurys) remained on the low end of the historical range.

## CLASS Y PERFORMANCE (%)

	CUMULATIVE TOTAL RETURN		AVERAGE ANNUALIZED RETURN			
	3 MONTH	YTD	1 YEAR	3 YEAR	5 YEAR	10 YEAR
FUND	0.99	8.03	3.22	4.01	2.74	6.51
BENCHMARK	2.27	8.52	10.30	2.92	3.38	3.75

*Performance data shown represents past performance and is no guarantee of, and not necessarily indicative of, future results. Investment return and value will vary and you may have a gain or loss when shares are sold. Current performance may be lower or higher than quoted. For most recent month-end performance, visit [www.loomissayles.com](http://www.loomissayles.com).*

*Additional share classes may be available for eligible investors. Performance will vary based on the share class. Performance for periods less than one year is cumulative, not annualized. Returns reflect changes in share price and reinvestment of dividends and capital gains, if any. You may not invest directly in an index.*

*Gross expense ratio 0.71% (Class Y). Net expense ratio 0.71%. As of the most recent prospectus, the investment advisor has contractually agreed to waive fees and/or reimburse expenses once the expense cap of the fund has been exceeded. This arrangement is set to expire on 1/31/2020. When an expense cap has not been exceeded, the fund may have similar expense ratios and/or yields.*

*The Class Y inception date is 12/1/1999. Class Y shares are sold to eligible investors without a sales charge; other Classes are available for purchase.*

- Emerging-market bonds finished in positive territory but trailed domestic, investment-grade debt. While the asset class continued to benefit from investor demand for yield, its return was pressured somewhat by concerns about global growth and the ongoing trade dispute between the United States and China.

## Portfolio Review

- The fund underperformed its benchmark, the Bloomberg Barclays US Aggregate Index, primarily due to its stance with respect to duration (and corresponding sensitivity to changes in interest rates).

## Winners

- The fund's allocation to equities positively contributed to performance relative to the benchmark as the asset class generated the greatest returns within the strategy. In particular, holdings within wirelines and pharmaceuticals aided return.
- Exposure to securitized assets generated positive return during the period, led by security selection in local authorities and asset-backed securities (ABS).
- A notable underweight in US Treasuries aided relative performance as higher-yielding holdings outperformed.

## Laggards

- The fund's allocation to high yield credit weighed on performance for the quarter. In particular, holdings within energy lagged due to softening demand and increasing supply.
- Security selection in non-US dollar denominated issues, primarily in Canadian and New Zealand dollar names, limited performance.
- Exposure to convertible securities detracted from relative performance for the period as energy names held hampered returns.
- The exposure to investment grade corporate credit generated positive return on an absolute basis. However, yield curve positioning within the sector weighed on results.

## Outlook

- Recent market volatility and macro developments have confirmed our view that we are in a late cycle environment. We have become more cautious based on the high degree of uncertainty associated with the outlook for trade; we believe there is still potential for a deal but with reduced conviction. Weak global manufacturing demand has persisted longer than expected, and this has the potential to further weaken business and consumer sentiment. We expect the US economy to exit this manufacturing slowdown without recession. However, it is likely that more policy easing will be needed to avoid a near-term downturn with the trade dispute showing the potential for rapid escalation. Our portfolios reflect a cautious view and we expect the above factors will be the primary issues driving risk profiles in the financial markets. As we gain clarity on the macro risk factors, we will seek to invest opportunistically where we feel the market may be mispricing risk in credit, currency or rate markets.
- In our view, it is possible the Federal Reserve overtightened in 2018 while fiscal stimulus

and corporate tax cuts were temporarily boosting economic activity. We don't believe that yield curve inversion is entirely indicative of an imminent recession and the time between inversion and start of a recession can be long. Risk assets can still perform well while yield curves are inverted, which supports continued investment in credit. However, security selection is critical. With the recent policy pivot and acknowledgement of a global slowdown by the Fed and other global central banks, the direction of rates in the near term appears to be more neutral. Additionally, further central bank cuts should support extension of the credit cycle.<sup>1</sup>

- The current shift in US monetary policy has not translated to a materially weaker US dollar. This combined with slower global growth and trade conflict leaves us with a cautious view on markets outside of the US. We are being patient and highly selective within our allocation to emerging market debt.
- We believe there are still opportunities in the credit markets, given the positive technical backdrop including flat to negative net issuance and solid retail inflows driven by negative global yields, along with expectations for slower, but non-recessionary US economic growth. We are finding value in select areas of the market, while maintaining a higher credit quality bias and increased emphasis on sectors with more defensive characteristics and positive secular trends including healthcare, communications, technology and media cable. These are industries that should hold up well even in a downturn. The upside potential for the credit markets, given current valuations, is largely dependent on global profit growth and capital expenditures helping to extend this stage of the cycle. The key risk to markets, in our view, centers around the overhang from macro uncertainty with potential for contagion across sectors.
- Consistent with our process, we use periods of market volatility to invest where there has been significant dislocation at the sector or security level and valuations show a disconnect from the underlying fundamentals. We have maintained sufficient liquidity in our portfolios to be positioned to invest opportunistically as these situations arise.
- During periods in which the US dollar appreciates relative to foreign currencies, funds that hold non-US-dollar-denominated bonds may realize currency losses in connection with the maturity or sale of certain bonds. These losses impact a fund's ordinary income distributions (to the extent that losses are not offset by realized currency gains within the fund's fiscal year). A recognized currency loss, in accordance with federal tax rules, decreases the amount of ordinary income a fund has available to distribute, even though these bonds continue to generate coupon income.

Fund officers have analyzed the fund's current portfolio of investments, realized currency gains and losses, schedule of maturities, and the corresponding amounts of unrealized currency losses that may become realized during the current fiscal year. This analysis is performed regularly to determine how realized currency losses will impact periodic ordinary income distributions for the fund. Based on the most recent quarterly analysis (as of September 30, 2019), fund officers believe that realized currency losses will have an impact on the distributions in the 2020 fiscal year. This analysis is based on certain assumptions including, but not limited to, the level of foreign currency exchange rates, security prices, interest rates, the fund advisers' ability to manage realized currency losses, and the net asset level of the fund. Changes to these assumptions could materially impact the analysis and the amounts of future fund distributions. Fund officers will continue to

monitor these amounts on a regular basis and take the necessary actions required to manage the fund's distributions to address realized currency losses while seeking to avoid a return of capital distribution.

## About Risk

**Fixed-income securities** may carry one or more of the following risks: credit, interest rate (as interest rates rise bond prices usually fall), inflation and liquidity. **Below investment-grade fixed-income securities** may be subject to greater risks (including the risk of default) than other fixed-income securities. **Foreign and emerging market securities** may be subject to greater political, economic, environmental, credit, currency and information risks. Foreign securities may be subject to higher volatility than U.S. securities, due to varying degrees of regulation and limited liquidity. These risks are magnified in emerging markets. **Currency exchange rates** between the U.S. dollar and foreign currencies may cause the value of the fund's investments to decline. **Equity securities** are volatile and can decline significantly in response to broad market and economic conditions.

*The Bloomberg Barclays US Aggregate Index represents securities that are SEC-registered, taxable, and dollar denominated. The Index covers the US investment grade fixed rate bond market, with index components for government and corporate securities, mortgage pass-through securities, and asset-backed securities. These major sectors are subdivided into more specific indices that are calculated and reported on a regular basis. Indexes are unmanaged and do not incur fees. It is not possible to invest directly in an index.*

*Outlook as presented in this material reflects subjective judgments and assumptions of the portfolio team and does not necessarily reflect the views of Loomis, Sayles & Company, L.P. There is no assurance that developments will transpire as stated. Opinions expressed will evolve as future events unfold.*

*These perspectives are as of the date indicated and may change based on market and other conditions. Actual results may vary. Please refer to the Fund prospectus for a comprehensive discussion of risks.*

***Before investing, consider the fund's investment objectives, risks, charges, and expenses. Please visit [www.loomissayles.com](http://www.loomissayles.com) or call 800-225-5478 for a prospectus and a summary prospectus, if available, containing this and other information. Read it carefully.***

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<sup>1</sup>A credit cycle is a cyclical pattern that follows credit availability and corporate health..