Loomis Sayles Investment Grade Bond Fund – Product Changes Q&A

By the Multisector Full Discretion Team: Portfolio Managers Matthew Eagan, Brian Kennedy & Elaine Stokes

On November 1, 2018, Loomis Sayles and Natixis Investment Managers began making guideline changes to the Loomis Sayles Investment Grade Bond Fund (*see "Fund Guidelines - What's Changed?"*)

These changes were largely in response to feedback from our investors as well as client demand for fixed income solutions without the volatility that can accompany currency and equity positions.

The following Q&A explains the portfolio transition since November 1 and gives our latest outlook.

FUND GUIDELINES - WHAT'S CHANGED?

- Non-US dollar and equity allocations eliminated (equity holdings only permitted through restructuring or conversion).
- High yield limit increased to 15% from 10%.
- Increased foreign exposure up to 30% (including Canada and emerging markets) from up to 20% (excluding Canada).

1. How has fund positioning changed since November 1?

- Fund positioning reflects the new guidelines and our view that the credit cycle is in late expansion, but we have not reached the end of this cycle. Our current positioning is[1] :

- **Investment Grade Credit, 52%:** The IG credit sector experienced a notable increase (25.5% at 10/31). The positioning is barbelled, with exposure to front-end maturities (5 years or less) and the intermediate maturity range. We believe this allocation structure currently offers an attractive yield and helps lower interest rate sensitivity. We favor industries that have more defensive characteristics, such as banking, healthcare and cable.

- **Reserves (Cash and US Treasury sector), 23%:** We deployed a notable portion of the fund's US Treasury reserves (45.8% at 10/31), but the portfolio maintains ample flexibility to take advantage of price inefficiencies or other buying opportunities. We prefer to hold cash reserves for opportunistic buys during risk-off market conditions, and we followed this strategy during the fourth quarter of 2018, when investment grade credit spreads widened nearly 50 basis points.

- **Securitized, 14%:** Part of the portfolio reserves were deployed into the securitized space, specifically ABS/RMBS. Most of the allocation is made up of a diversified basket of high-quality ABS positions: receivables from car loans, credit cards and student loans, with some exposure to RMBS via home equity loans. The RMBS sector currently provides opportunity because it sits on the short end of the curve (3-5 year duration) while providing a yield advantage over Treasurys. The portfolio maintains zero exposure to Agency MBS.

[1] *As of 12/31/2018.*

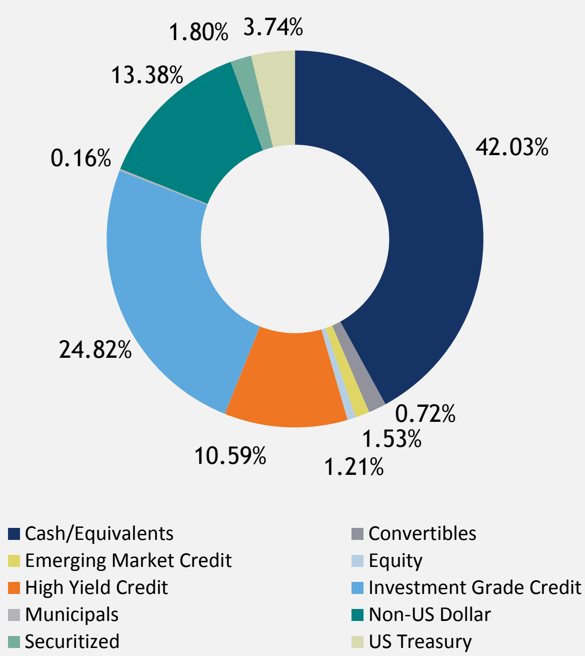
- **High Yield, 7%:** While the allowable limit increased, the fund's actual allocation to this sector decreased as we became more quality-oriented and defensively positioned given the late expansion phase of the credit cycle (11.1% at 10/31). The fund has remained invested in the higher credit quality areas of the high yield sector, for example mid-to-high BB-rated credits.

- **Non-US dollar, 0.2%:** The vast majority of the fund's foreign currency holdings have been removed (13.4% at 10/31).

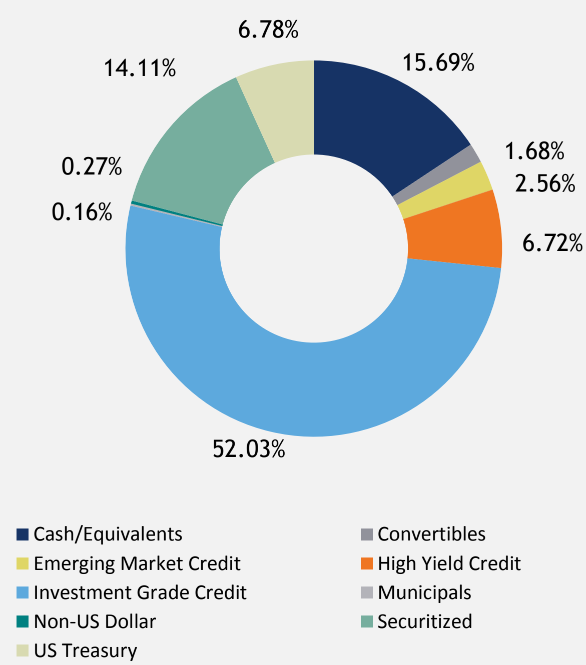
- **Equity, 0%:** All equity positions have been sold in accordance with the new investment guidelines.

- **Duration, 4.23 years:** Fund duration has extended as we transitioned the portfolio and deployed US Treasury reserves into IG credit and ABS/RMBS (2.9 years at 10/31). The portfolio has maintained a duration underweight versus the broader market (6.3 years for the Bloomberg Barclays Government/Credit Index) because we believe risks to global interest rates remain skewed marginally higher as central banks continue to remove liquidity and raise rates.

OCTOBER 31, 2018



DECEMBER 31, 2018[1]



[1] *As of 12/31/2018, foreign currency forwards represented a -0.01% portfolio position.*

2. What is the remaining non-dollar exposure?

We have a small position remaining in the Iceland krona (20 basis points) and we expect to close it out soon.

3. Has the fund retained enough flexibility to generate competitive returns and income?

Yes, the fund maintains its benchmark-agnostic, value-oriented investment approach and flexibility. Exposure to corporate credit is central to our strategy, and the investable limit for high yield was increased to 15%, up from 10%. This, along with the flexibility to allocate across diversified market sectors, should allow us to pursue a yield advantage and alpha potential.

The fund's increased allocation to securitized assets is another important diversifier. While fund guidelines have previously allowed for investments in securitized assets, we believe greater use is warranted at this point in the cycle. This allocation can provide attractive short-duration yield that fits with the fund's income objective, and we believe it positions the fund well going into 2019.

4. What is your outlook?

As we enter 2019, our strategy is to maintain a higher-quality bias within credit markets given the aging credit cycle. We continue to favor sectors that are exhibiting credit improvement, such as banking, and those with defensive characteristics, such as telecommunications and cable. We are limiting our exposure to industries with more challenging business trends, such as retail and home construction.

We believe opportunities in the US high yield market have increased, and long-term value in selected areas has become more attractive since spreads rose significantly during the fourth quarter. Corporate fundamentals appear healthy, and new issuance has declined dramatically, helping support the market. We still do not anticipate a large increase in defaults, and the maturity wall remains pushed out until 2022. However, growth concerns warrant some increase in default risk. The recent market selloff confirms our view that we are nearing the downturn phase of the economic and credit cycles; however, the recovery in spreads and risk assets that has occurred year-to-date supports our position that we have not reached the end of this cycle.

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.

There is no guarantee that the investment objective will be realized or that the strategy will generate positive or excess return.

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.* ***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.* ***Below investment grade fixed income securities*** *may be subject to greater risks (including the risk of default) than other fixed income securities.* ***Mortgage-related and asset-backed securities*** *are subject to the risks of the mortgages and assets underlying the securities. Other related risks include prepayment risk, which is the risk that the securities may be prepaid, potentially resulting in the reinvestment of the prepaid amounts into securities with lower yields.*

Diversification does not ensure a profit or guarantee against a loss.

Before investing, consider the fund's investment objectives, risks, charges, and expenses. Please visit loomissayles.com or call us at 800-633-3330 for a prospectus or a summary of prospectus, if available, containing this and other information. Read it carefully.

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