Understanding Brandywine's unique fixed-income approach

A conversation with Brandywine Global

Q. What is unique about Brandywine's investment philosophy and process?

A. Our investment process is disciplined, active and value-driven. Importantly, our process is responsive, positioning the fund's core of U.S.-centric, investment-grade securities in segments of the yield curve and/or various sectors that may offer the most attractive risk-adjusted return based on our view of the current economic environment. At its core, our investment process combines rigorous top-down macroeconomic research with bottom-up fundamental analysis which seeks to identify the most attractive fixed-income opportunities globally. These two processes continually occur in tandem to position the portfolio in sectors and securities that present the most value for a given economic environment.

Q. What do you mean by "top-down" or macroeconomic focus?

A. Top-down investors generally take a macroeconomic view of the world from the "top"—in other words by examining long-term global economic trends that govern the business cycle. We believe investors can potentially capture excess return by rotating credit quality, sector allocation, and security selection throughout the business cycle. We rely on a robust, internal macroeconomic research platform, which seeks to identify shifts in inflation and real yields (the yield minus the cost of inflation), significant political developments that could alter fiscal and monetary policies, and fundamental credit trends. We also evaluate business and liquidity cycles globally by measuring inflationary pressures, capacity constraints, employment conditions, and fiscal and monetary policies. This is the cornerstone of our process at Brandywine Global's and we believe in its proven ability to help us effectively rotate among sectors, geographies, and currencies in the pursuit of value within fixed income markets.

Q. What is a "bottom-up" or fundamental analysis?

A. We believe that fundamental research, which evaluates creditworthiness of individual security issuers is equally important to the process. Fundamental research is critical to security selection and constructing a portfolio that has the potential to outperform its representative risk benchmark. Through a comprehensive, systematic process, we focus on identifying securities that will provide the opportunity for excess total return given the state of the economy. We analyze: (1) quality of a company's earnings in relation to management's goals and risk tolerance; (2) quality of specific issuer bond covenants; (3) position of an issue within the capital structure; and (4) value and range of a firm's assets across the respective capital structure ("recovery rate"). Our analysts and portfolio managers assess the business risks and issuer prospects through meetings with management, filing reviews, and industry analysis.

Q. Where could this strategy fit within my asset allocation?

A. The 1290 Diversified Bond Fund was designed to fit alongside traditional core plus, total return oriented strategies. The objective of the strategy is to achieve similar risk/return outcomes to typical core plus portfolios, but with a lower level of correlation between excess returns. Our strategy can be differentiated by the relatively higher degree of freedom around what sectors, geographies and currencies the fund may access as compared to traditional core plus portfolios. The fund is designed to be entirely positioned as a U.S.-centric and investment-grade investment.

Q. What is wrong with the traditional core plus approach?

A. Generally speaking, the core plus space is occupied by managers who earn their alpha by effectively managing duration and high-yield credit exposure domestically, to provide a portfolio that has meaningful returns and defensive/diversification benefits. While there is nothing wrong with that objective, the two main levers that core plus managers can pull have increasingly become expensive and subject to price risk. What is potentially worse is that even if returns do not turn negative as interest rates normalize, the positive returns that investors can hope to glean from traditional core/core plus strategies may remain anemic as yields and spreads continue to compress. U.S. bonds have been both a great diversifier and a great source of returns for investors since the 1980s. The path forward, however, looks more challenging given the starting point in yields and valuations.

Q. Why is now a good time to add this strategy?

A. We believe investors need to work a little harder and think more deeply about how to enhance potential returns in their fixed-income allocation without incurring too much additional volatility and capital risk. The 1290 Diversified Bond Fund is designed to deliver an investment-grade, U.S.-centric portfolio in aggregate that has a similar risk and return profile to core plus investments. However, by allowing the "plus" segment of the fund with access to a broader opportunity set, and by allowing Brandywine more latitude in positioning the fund relative to the benchmark, the strategy has the potential to deliver alpha, in a less correlated and more consistent manner over full market cycles. Put more simply, this fund is built to have more levers to pull in the event that the typical balancing act between duration and high yield is not the best way to allocate risk exposures moving forward.

Q. How can currencies be used within the Fund?

A. While the majority of this strategy is likely to be invested in U.S. dollar denominated securities, Brandywine does have the ability to actively invest in foreign currencies within the limits of the fund's guidelines. Some of Brandywine's currency positions may be used to actively hedge all, some, or none of the foreign currency risk associated with non-U.S. bonds denominated in local currency terms. Other applications of Brandywine's currency investments may be for speculative purposes. While foreign currency investments may come with heightened levels of risk, prudent and appropriate long/short allocations among currencies can also provide significant benefits in terms of risk mitigation at a portfolio level. Currency investments also offer the potential to generate enhanced returns through both the direct appreciation/depreciation of a given currency and through the higher yields typically offered for bonds denominated in local currency terms. With the U.S. dollar currently being one of the most expensive currencies in our observed universe, we believe that thoughtful investments in non-dollar denominated securities may be a highly accretive position in this portfolio in the years to come.

Q. Will 1290 Diversified Bond Fund pay a monthly dividend?

A. The Fund may distribute investment income and realized gains as a monthly dividend, although these amounts would be offset by realized losses. In periods of high market volatility, or any time losses exceed income, the Fund may elect not pay a dividend to help mitigate the possibility of a return of capital at the end of the Fund's fiscal year. The Fund may also pay a special distribution at the end of a calendar year.

Q. What is the value of being benchmark aware, but agnostic?

A. Around a U.S. centric core of fixed-income securities, we source ideas from across global fixed-income and currency markets in an effort to deliver lowly correlated sources of excess return over the Bloomberg Barclays U.S. Aggregate Bond Index. Our investments are typically concentrated in market segments where we see value, as opposed to replicating the construction of the index. While our value discipline and focused approach to investing will not change, the strategy's allocation will shift over time in response to changing market conditions.

Q. What are the biggest risks to your process?

A. With a process that originates with a top-down macroeconomic view—clearly, the fund's success depends in great measure on our ability to correctly anticipate major swings in economic activity on a global scale. The fund will also from time to time face headwinds related to rising interest rates or falling credit quality. Nonetheless, it is structured to attempt to take advantage of opportunities that exist anywhere in the world, and even in adverse bond markets we believe its structure will help us seek to mitigate some of these risks. Equally, there is no environment in which the fund's investment process should fall out of favor due to technical factors—however, it is worth noting that a prolonged period of dollar strength would remove one of the important tools by which the fund may gain alpha returns over that of the benchmark. This scenario would make achieving the Fund's objective more difficult.

Note: Brandywine Global became the subadvisor of the 1290 Diversified Bond Fund (formerly 1290 Unconstrained Bond Managers Fund) on June 15, 2018.

For more information, call **(888) 310-0416** or visit **1290funds.com.**

This material must be preceded or accompanied by the prospectus.

Performance may be affected by one or more of the following risks:

Investment Grade Securities Risk: Debt securities are generally considered to be investment grade if they are rated BBB or Higher.

Credit Risk: The fund is subject to the risk that the issuer or the guarantor of a fixed income security is unable or unwilling to make timely principal and/or interest payments.

Foreign Securities Risk: Investments in foreign securities involve risks not associated with investments in U.S. securities. Foreign markets may be less liquid, more volatile and subject to less government supervision and regulation than U.S. markets. Security values, also may be negatively affected by changes in the exchange rates between the U.S. dollar and foreign currencies. There are greater risks involved in investing in emerging market countries and/or their securities markets, and investments in these countries and/or markets are more susceptible to loss than investments in developed countries and/or markets.

Bloomberg Barclays U.S. Aggregate Bond Index covers the U.S. dollar denominated investment-grade, fixed-rate, taxable bond market of securities. The index includes bonds from the Treasury, government-related and corporate securities, agency fixed rate and hybrid adjustable mortgage pass through securities, asset-backed securities and commercial mortgage-backed securities.

Alpha is the excess return of a fund over its benchmark.

Duration is a measure of a fund's interest-rate sensitivity-- the longer a fund's duration, the more sensitive the fund is to shifts in interest rates.

Yield to maturity is the rate of return anticipated on a bond if held until the end of its lifetime.

The 1290 Diversified Bond Fund seeks to maximize total return consisting of income and capital appreciation. There is no guarantee this objective will be met. The fund may not be successful in implementing its investment strategy or may not employ a successful investment strategy, and there can be no assurance that the fund will grow to or maintain an economically viable size, which could result in the fund being liquidated at any time without shareholder approval and at a time that may not be favorable for all shareholders. Until the Fund is fully capitalized it may not be pursuing its investment objective or executing its principal investment strategies.

Diversification does not eliminate the risk of experiencing investment losses.

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