Invesco Active Multi-Sector Credit

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CIO, Multi Sector Credit and High Yield

The song remains the same

We entered the second quarter with risk appetite strongly inspired by dovish central banks globally. The trend continued until mid-quarter as China-US trade talks broke down and global growth showed signs of cracking. A weak payroll number led to a strong rally in US Treasuries, and Europe saw 10-year bunds head back into negative territory following ECB's reaffirmation of doing "whatever it takes" to support growth.

In the quarter, it should come as no surprise that of the four sectors in which we invest, the index for bank loans had the lowest return at 1.68%, followed by high yield at 2.6%. Emerging markets and investment grade performance was largely driven by duration and both returned 3.7%. US 10-year Treasuries rallied 40 bps, ending the quarter near 2%, and German Bunds rallied 26 bps to close the quarter at -0.32%.

Portfolio positioning

The strategy was positioned to take advantage of the rally in credit and rates, maintaining a long duration position for most of the period and favoring fixed rate bonds over Floaters/Bank Loans. For the period, active and passive duration management was a key driver of outperformance. Active duration management took the form of a long duration position, achieved by utilizing an interest rate swaption. Duration was also managed passively through exposure to long dated BBB bonds in the opportunistic sleeve. Although the strategy was underweight the IG sector sleeve relative to the strategic asset allocation, this position was more than offset on an overall strategy level by our BBB exposure in the opportunistic sleeve of the portfolio.

Sector commentary

Investment Grade (IG)

The strategy retains an overweight to Euro credit versus USD credit given our view of:

i. Mid stage fundamentals in the European corporate space versus latter stage for US corporates, and
ii. More attractive hedged yields available within European credit.

This theme has performed well year-to-date. In the European non-financial space, we prefer subordinated hybrid bonds. The dovish tilt from the ECB and the negative yield of German bunds has increased the hunt for yield within European credit, creating strong technical demand for this asset class. Additionally, the low yield environment reduces extension risk of the legacy hybrid bonds. Financials, US and European Banks, and airplane leasing remain a strategic overweight and key driver of performance in the IG space. We favor financial bonds over non-financial equivalents due to the yield pick-up and the continued improvement in balance sheet quality of the banks due to increased regulatory scrutiny post the Global Financial Crisis. Within this theme, the strategy has an overweight to UK exposed banks. While this theme had struggled towards the back end of 2018 on rising 'no-deal' Brexit concerns, we have seen a recovery in UK bank bonds year to date. We are comfortable in the strategy's positioning here and have primarily invested in senior bonds.

Emerging Markets (EM)
Of note in the emerging markets space, the investment grade EM portion of the index outperformed high yield EM by over 175bps in total return. IG spreads tightened while HY spreads were wider. In addition, IG benefited from the large rally in US Treasury rates. In the portfolio, the current IG duration is approximately 2 years longer than HY duration. The strategy was positioned to take advantage of the IG rally through exposures in long maturity Indonesian and Moroccan credits. In the high yield EM space, the strategy's exposure to HY corporates in Mexico (consumer finance), Brazil (banks and protein producer) and Turkey (blue chip corporates and banks) positively contributed to the strategy's performance. Additionally, the strategy's exposure to HY sovereigns, expressed through positions in the Ukraine and Ecuador, and local currency (Brazil, Chile, Indonesia, Russia, and South Africa) also had a positive impact on performance.

Bank Loan (BL)
This quarter, the US loans portion of the portfolio outperformed the bank loan index primarily due to sector allocation. The bank loan sleeve of the strategy was overweight BBs vs the bank loan index, and outperformed the index. The sleeve was also underweight CCCs, and overweight high beta names which outperformed. the index.

European Loan
European loans slightly outperformed the market due primarily to conviction trades. Conviction ideas benefited from strong earnings/management outlooks/events and traded higher. During the first quarter, the team reduced low margin holdings on the expectation of a strong primary pipe with wider spreads. This proved prescient as new issuance in the second quarter provided attractive entry opportunities, by exhibiting higher margins for the same rating. Given the wide AAA spreads, demand for low margin loan names from colletarized loan obligation (CLO) buyers remains muted, whereas high spread names remain in demand. Additionally, we avoided most names exhibiting weak earnings profiles, as they tended to reprice about 2-5 points lower depending on the severity of the earnings miss.

Past performance is not a guarantee of future results.

High Yield (HY)
In high yield, security selection and rates positioning contributed favorably to a slight outperformance during the quarter. Key single name contributors included both credits we owned and credits we avoided in the energy sector, coupled with several high conviction positions. Detracting from performance during the quarter was a cash balance that was only partially offset by credit default swaps, single name securities in the energy sector, and conviction positions that experienced idiosyncratic events.

Opportunistic bucket
Outside the four primary sectors, our high conviction/best ideas positions were driven by our thematic views on technology, media, and commodities. We continued to tactically reduce our exposure to bank loans by allowing our bank loan total return swap (TRS) to mature,. We ended the quarter approximately 10% underweight bank loan exposure relative to the strategic asset allocation. As previously mentioned, banks loans have lagged when compared to other fixed income asset classes this past quarter.

Outlook
Although we believe the market has fully priced the Federal Reserve shifting to an easing of monetary policy, exogenous risks to growth remain the big "known unknown." Markets are likely to be held hostage not by when the Fed eases policy, but by the magnitude of cuts expected over the next twelve months. We believe we could experience a backup in Treasury yields and a steeper yield curve the rest of this year. We will continue to monitor several key economic points, including signs of global growth resurgence and corporate earnings confirming strong credit fundamentals, and we will adjust our overall portfolio duration exposure accordingly. We intend to maintain credit exposure slightly above market weight. Due to our belief that EM credit is both impacted negatively by slower global growth and positively by easing Fed and ECB policy, we are maintaining a neutral EM position, while tactically taking advantage of opportunities as they arise.

Composite perfomance and important disclosures

Period As of 6/30/19	1 month (%)	3 months (%)	YTD (%)	1 year (%)	3 years (%)	5 years (%)	Since inception 10/31/13 (%)
Invesco Active Multi-Sector Credit Composite (Gross)	1.44	3.34	8.71	8.60	5.83	4.43	5.05
Invesco Active Multi-Sector Credit Composite (Net)	1.39	3.21	8.44	8.06	5.31	3.91	4.52
Market Returns*	1.62	2.94	7.84	7.76	5.14	4.27	4.63

Source: Invesco. Performance shown is composite performance. Gross of fees are before deduction of management and custodial fees but after trading commissions. Net returns will be lower. Returns less than one year are cumulative; all other performance figures are annualized. Past performance is not a guarantee of future results.

*The strategy is not managed to any benchmark. We are showing "Market Returns" which consist of a static allocation of 40% Inv Grade/ 15% EM/ 30% Bank Loans/ 15% HY, using representative market indices for returns. Representative market indices for returns are: IG- BBG BARC Global Aggregate Credit Hedged USD; EM- BBG BARC EM Hard Currency Aggregate Hedged USD; HY- BBG BARC Global High Yield Corporate Hedged USD; BL- S&P/LSTA Leveraged Loan.

An investment cannot be made directily into an index.

GIPS® compliant schedule of investment performance, as of December 31, 2018

Year	Gross return (%)	Net return (%)	Benchmark return (%)	Composite 3-year annualized standard deviation	Benchmark 3-year annualized standard deviation	Number of accounts	Composite assets ($ millions)	Total firm assets ($ billions)	Percentage of firm assets (%)
2018	-1.46	-1.95	-0.62	2.97	2.57	2	260.32	578.95	0.04
2017	6.46	5.93	5.79	3.39	2.90	1	310.59	660.32	0.05
2016	9.89	9.35	9.09	3.67	–	1	325.30	599.00	0.05
2015	-0.53	-1.03	-0.28	–	–	1	256.89	575.06	0.04
2014	5.30	4.77	4.71	–	–	1	263.01	584.91	0.04
2013 (2 Months)	0.71	0.63	0.09	–	–	1	101.47	572.83	0.02

Annualized compound rates of return

Period	Gross return (%)	Net return (%)	Benchmark Return (%)
1 Year	-1.46	-1.95	-0.62
2 Years	2.42	1.91	2.53
3 Years	4.85	4.33	4.67
4 Years	3.48	2.96	3.41
5 Years	3.84	3.32	3.67
Composite Inception (10/31/13)	3.86	3.34	3.57

1 Invesco Worldwide claims compliance with the Global Investment Performance Standards (GIPS®) and has prepared and presented this report in compliance with the GIPS standards. Invesco Worldwide has been independently verified for the periods 1st January 2003 through 31st December 2017. The legacy firms that constitute Invesco Worldwide have been verified since 2001 or earlier. The verification reports are available upon request. Verification assesses whether (1) the Firm has complied with all the composite construction requirements of the GIPS standards on a Firm-wide basis and (2) the Firm's policies and procedures are designed to calculate and present performance in compliance with the GIPS standards. Verification does not ensure the accuracy of any specific composite presentation.

2 Invesco Worldwide, the Firm, is defined as follows: Invesco Worldwide ("The Firm") manages a broad array of investment strategies around the world. The Firm comprises U.S.-based Invesco Advisers, Inc. (excluding Unit Investment Trusts) and all wholly owned Invesco firms outside of North America (excluding Invesco India and Source Investment Management Limited). All entities within the Firm are directly or indirectly owned by Invesco Ltd. Invesco Canada Ltd. is also a GIPS-compliant firm whose assets are managed by a subsidiary of Invesco Ltd. Invesco Senior Secured Management, Inc., Invesco Private Capital, Inc., and Invesco Capital Management LLC are affiliates of the Firm. Each is an SEC-registered investment adviser and is marketed as a separate entity. Invesco Great Wall Fund Management Co. Ltd is a fund management company established under China Securities Regulatory Commission's approval, and its assets are excluded from total Firm assets. On May 24, 2019 Invesco acquired Massachusetts Mutual Life Insurance Company's asset management affiliate OppenheimerFunds. As a result of this transaction assets previously part of the OFI Global Asset Management (OFI Global) GIPS® firm will now be part of Invesco Worldwide (IWW) GIPS® firm. Firm assets under management for OFI Global as of December 31, 2018 were $214 billion. IWW historical firm assets have not been restated to reflect the acquisition. OFI Global was independently GIPS® verified through December 31, 2018.

3 The objective of the Invesco Active Multi-Sector Credit strategy is to provide benchmark agnostic credit exposure for return-seeking investors. The strategy seeks to achieve this objective primarily through sector positioning both within and across investments in Sector Funds, including active security selection within the Sector Funds, and up to a 10% opportunistic allocation into other credit related assets. The Sector Funds are managed pools of credit-related assets principally consisting of corporate bonds, emerging market debt, bank loans and high yield bonds. The strategy intends to invest a substantial amount of total assets of the strategy in the Sector Funds. Investment allocations in the Sector Funds will be determined in a manner believed to produce favorable returns across a full credit cycle. The strategy utilizes an affiliate as sub-advisor for one of the Sector Funds.

4 Effective 10/1/2015, the composite is benchmarked to a strategic asset allocation (SAA) comprised of 40% Bloomberg Barclays Global Aggregate Credit Hedged USD Index, 15% Bloomberg Barclays EM Hard Currency Aggregate Hedged USD Index, 30% S&P/LSTA Leveraged Loan Index and 15% Bloomberg Barclays Global High Yield Corporate Hedged USD Index, rebalanced monthly. The prior benchmark was 42% Barclays Global Aggregate Credit Hedged USD Index, 15% Barclays EM Hard Currency Aggregate Hedged USD Index, 29% S&P/LSTA Leveraged Loan Index and 14% Barclays Global High Yield Hedged USD Index. The custom benchmark is a baseline asset allocation derived by applying risk parity principles and is used as a reference for managing portfolios in the composite. The strategic asset allocation is intended to represent a stable, diversified asset allocation over the long term against which the performance of the fund manager's active decision-making in tactical asset allocation and issue selection can be measured. Investments made for the strategy may differ significantly in terms of security holdings, industry weightings, and asset allocation from those of the benchmark. Accordingly, investment results and volatility will differ from those of the benchmark.

5 The minimum size for a separate account is $100 million.

6 The strategy may invest in derivatives for the purpose of hedging against currency, duration and other risk exposures or managing cash balances pending the direct acquisition of an asset or investment in a fund. The strategy may also invest in derivatives in order to obtain exposure for purposes other than hedging, including opportunistic investments. Types of derivatives instruments that may be employed by the strategy are (i) Swap Contracts (including, without limitation, Credit Default Swaps, Credit Default Swap Indices, Total Return Swaps, Interest Rate Swaps, Foreign Currency Swaps and Volatility Swaps), (ii) Futures Contracts (including, without limitation, Interest Rate Futures Contracts), (iii) options (including, without limitation, Credit Default Swap Index options and options on Futures Contracts), (iv) Swaptions, (v) Forward Contracts and (vi) credit-linked notes, and/or other derivative instruments. Derivatives exposure is also permitted with in the Sector Funds. Derivatives held may have the economic effect of financial leverage by creating additional investment exposure, as well as the potential for greater gain or loss.

7 Gross-of-fee performance results are presented before management and custodial fees but after all trading commissions and withholding taxes on dividends, interest and capital gains, when applicable. Net-of-fee performance results are calculated by subtracting the highest tier of our published fee schedule for the product from the monthly returns. The management fee schedule for a separate account is as follows: 50 basis points on first $150 million, 45 basis points on the next $150 million, 40 basis points on the next $200 million, 35 basis point thereafter.

8 Composite dispersion is measured by the standard deviation across asset-weighted portfolio returns represented within the composite for the full year. It is considered not meaningful for composites with fewer than three portfolios during the year. The three-year annualized standard deviation measures the variability of the composite and the benchmark returns over the preceding 36 months. The standard deviation is not presented when there is less than 36 months.

9 Valuations and portfolio total returns are computed and stated in U.S. Dollars. The Firm consistently values all portfolios each day on a trade date basis. Portfolio level returns are calculated as time-weighted total returns on daily basis. Accrual accounting is used for all interest and dividend income. Past performance is not an indication of future results.

10 The composite creation date is October 31, 2013. As of December 31, 2013, 2014, 2015, 2016 and 2017, proprietary and non-fee paying assets were51%, 38%, 36%, 10%, and 9% of the composite, respectively.

11 A complete list of composite descriptions is available upon request. Policies for valuing portfolios, calculating performance, and preparing compliant presentations is available upon request.

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