April was a quiet month due to the absence of any major catalysts. For the most part, attention was given to the direction of U.S. Treasury (UST) rates, growth expectations in the U.S. and any political and fiscal changes.

As we highlighted in last month’s commentary, it was our view that 10-year UST yields would breach 2.20% during the first half of 2017. On April 18th, 10-year UST yields fell to an intraday low of 2.16% as several signals supported the move. Lower yields were supported by several factors including a peak in inflation, as measured by the Consumer Price Index (CPI), seasonally weak first quarter Gross Domestic Product (GDP), and other inflationary measures such as lower U.S. Breakevens, which tend to be correlated to WTI crude oil prices. Additionally, we saw a shift in demand as CFTC Treasury Speculative Positioning unwound from a record short position at the beginning of the year to a net long position by month end. The move appears to have coincided with the move lower in 10-year UST yields, only for investors to end the month in a net long position while yields closed the month higher at 2.30%. Although rates are likely to remain range bound over the near term, attention must be given to the June Federal Reserve (Fed) decision which may be another indication for higher rates.

April also provided the first look at domestic growth as first quarter GDP came in at an annualized rate of 0.7%. Although the figure was the weakest in three years, bright spots in capital expenditure (capex) and residential investment offset the weak Personal Consumption Expenditures (PCE) and volatile change in inventories. We take the figure with a grain of salt as first quarter GDP figure is one of the weaker quarters due to seasonality which may be affected by weather and consumer behavior at the start of the year. We will be keeping a close eye on any updates to first quarter...
Overview

GDP, but more importantly the second quarter GDP which will paint a better picture of growth for 2017. There is certainly some work to do if 2017 GDP is to reach the consistent 3-4% level which President Trump and his administration have called for.

Last but not least, April would not be complete without mentioning the political landscape and any changes to fiscal policy. The French election was front and center as Emmanuel Macron was finally declared President-elect of France after defeating the right-wing nationalist Marine Le Pen. After a closely contested election the results are expected to be supportive of the European Union (EU) which has seen little support following the global populist movement that has occurred over the past year. Outside of the day-to-day headlines in the United States, fiscal policy changes were muted during the month as the world’s largest central banks left their policies unchanged. The Fed left rates unchanged after a weaker first quarter GDP was “likely to be transitory.” The European Central Bank (ECB) kept their policy unchanged with €60 billion in monthly asset purchases and the main refinancing rate and deposit rate at 0.00% and -0.40%, respectively.  


Overall prepayment speeds declined by about 8% month-over-month (MoM) for April. Speeds declined across the coupon stack across all three Agencies and most of the securitized collateral. Most of this is attributed to lower day count, lower seasonal turnover, and mortgage rates being relatively unchanged during this period.

Total gross issuance for the month was approximately $101 billion, only slightly higher than March’s issuance volumes. This brought year-to-date (YTD) volumes to roughly $450 billion which is about 12% higher than the issuance volume for the same period in 2016.

Current coupon spreads against 5/10 Treasury blend spreads have been range bound for most of this year, a trend that continued in April.

Based on the Bloomberg Barclays U.S. Mortgage-Backed Securities (MBS) Index, the Agency Residential MBS (RMBS) sector performed positively with a return of 0.65% with duration shortening from 4.95 years to 4.74 years.

Non-Agency spreads were slightly tighter for April. Spreads across the credit curve, from front-end cash flows to last cash flows (LCF), ground tighter, which was in line with other credit risk assets. However, in the face of recent highs in prices, demand was strong for non-Agency securities throughout the month.

In April, $3.7 billion of legacy non-Agencies traded on bid lists. Trading volume was approximately 40% lower from the previous month, partially due to the absence of any large liquidation during the month. Subprime non-Agencies saw the biggest decline in trading volume, falling 60% from $2.8 billion to $1.1 billion.
Prepayment speeds in all non-Agency sectors were marginally higher in April, with the increases ranging between 1-4 conditional prepayment rate (CPR) for the month. The increase was due primarily to more business days in April versus March. Liquidation speeds were also higher in April, ranging between 4-5 conditional default rate (CDR). Severities were slightly lower for the month, averaging between 60-65%.

April issuance was down 38% MoM with two conduit deals totaling $1.9B and two single-asset single-borrower (SASB) deals totaling $1.8 billion pricing. Commercial MBS issuance YTD remains down 20% compared to the same period in 2016, while commercial real estate (CRE) transaction volumes are down roughly 18% year-over-year (YoY) over the past two consecutive quarters. New issue AAA, AA and BBB’s priced tighter by 5 basis points (bps), 7 bps and 8 bps, respectively, over the last deal priced in March; however, single-A spreads were wider by 2 bps. While 11 conduits have priced YTD, only two deals have utilized a horizontal risk retention structure.

Secondary 2.0/3.0 trading was relatively muted in April as investors were anticipating heavy new issuance in May. 2.0/3.0 spreads tightened for the month, with AAA LCFs tightening by 4 bps in March to Swaps +90 bps and BBB’s tightening by 60 bps to Swaps +380 bps. In April, Single-A and BBB all-in yields tested the lowest levels seen YTD, 3.98% and 6.17%, respectively, alongside the rally seen in broader equity and credit indices. The risk-on sentiment, coupled with limited new issuance, also caused CMBX spreads to tighten across the stack.

The private label CMBS universe fell by $9.6 billion or 2.1% to $447.4 billion in April resulting in a 7.6% decline in net issuance YTD. The conduit universe fell to $341.8 billion, down $9.3 billion MoM, while the legacy universe declined by 62% YoY due to continued payoffs and resolutions. As the CMBS universe continued to pay-down, the overall delinquency rate ticked higher by 15 bps in April to 5.5%. Maturity defaults represented 84% of new delinquencies in April as 10-year loans originated in 2006 & 2007 faced difficulty refinancing.

Three PACE issuers priced over the month with supportive spread levels despite headwinds in the media. Many of the issuers are currently renewing efforts to improve consumer protections and to provide better education programs to their contractor networks.

Investors continue to believe they are able to source attractive risk-adjusted returns relative to other asset classes as both primary and secondary spreads marched tighter in April. The Bloomberg Barclays U.S. ABS Index was up 0.85% YTD, with Utilities being the strongest performer.

According to the Bloomberg Barclays U.S. Treasury (UST) Index, treasuries returned 0.69% in April, its biggest gain since June 2016. This was driven by the weak economic data for March, geopolitical concerns over North Korea and Syria, as well as fading optimism in Trump’s tax reform promises. It also marked a significant retracement to post-election yield levels. Treasury gains were pared during the second half of April as French centrist Macron appeared likely to
defeat nationalist Le Pen, which eased the concerns of another win of populism. The market sold off in relief.

- According to Commodity Futures Trading Commission (CFTC) positioning data, speculators flipped from historic net shorts to heaviest long positions, which prompt us to think the rally in early to mid-April was also supported by short-covering trades.

- Treasury inflation-protected securities (TIPS) underperformed nominals over the month as benchmark breakeven rates fell to YTD lows and 30-year breakevens fell below 2% to the lowest level since Election Day.

- The 5s30s curve steepened to 115 bps.

**Investment Grade Credit**

- The Investment Grade Corporate market was fairly stable in April. Credit spreads varied by 3 bps throughout the month, between a low of 110 bps over UST and a high of 113 bps, ending the month at the low of 110 bps. The Bloomberg Barclays Credit Index posted a total return of 1% driven primarily by a rally in UST. The best performing sectors were in Energy, with refining and midstream up 1.7% and 1.6%, respectively, despite energy prices weakening towards the end of the month.

- Technicals remained positive in April. Weekly flows, as reported by Emerging Portfolio Fund Research (EPFR), initially slowed mid-month to less than $1 billion per week but rebounded in the last week of the month to $3.06 billion, bringing the month to a total of $12 billion of inflows compared to $18 billion in March. New issue supply slowed significantly to $93 billion compared to $148 billion last month and $122 billion in April 2016.

**Collateralized Loan Obligations**

- April was the most active month this year with $10.24 billion in new issuance across 17 deals. Issuance this month was more than half of the total issuance of the first quarter of 2016. This year we have seen $27.63 billion across 30 deals.

- Even with a robust new issuance machine, the refinancing and reset wave remained strong and continued to support CLO demand. A total of 43 deals were refinanced or reset this month.

**Bank Loans**

- The S&P/LSTA Leveraged Loan Index posted a positive return of 0.44% in April. This marked the
14th consecutive month with positive returns and was an improvement from the 0.08% return in March.

- Higher yielding CCC-rated names performed well during the month, rising 1.23%, while B-rated loans returned 0.40% and BB-rated loans returned 0.28%. Second lien loans returned 1.43%. The default rate remained low at 1.43%.

- The best performing sector in the month was Retail, which returned 1.08% after a slightly negative return in March. We remain selective with investments in this sector.

- The technical backdrop remained relatively strong, with over 70% of loans bid above par.

High Yield

- April started out weak for high yield (HY), but rallied in the second half on the back of political optimism, a favorable corporate earnings season and light new issue volumes. The Citi High-Yield Cash-Pay Capped Index returned 1.06% to end the month with a relatively tight spread-to-worst of 397 bps and yield-to-worst (YTW) of 5.62%.

- Unlike most recent months that saw positive returns, lower-rated bonds underperformed higher-rated ones. Most sectors of the Index had positive performance, with Industrials, Food & Beverage and Lodging notably strong. The weakest sectors, and the only ones with negative returns, were Pharmaceuticals, Utilities and Oilfield Services.

- According to J.P. Morgan, the par-weighted U.S. high yield default rate decreased to 1.39% in April, down from 3.57% since the start of 2017. The steep decline thus far this year is due to the removal of $32 billion of debt from the last twelve months (LTM) calculation that defaulted during the first four months of 2016. These were largely Energy and Metals & Mining companies reacting to depressed commodity prices.

- New issue volume was uncharacteristically light for April, with J.P. Morgan showing 44 U.S. Dollar (USD)-denominated bonds pricing for $19.0 billion of proceeds. This compares to a $32.0 billion average for every April since 2010. However, CCC-rated bonds continued to make up a higher percentage of issuance than in 2016.

Commodities

- In April, the broad commodity market decreased by 1.57% and 2.17%, as measured by the Bloomberg Commodity Index (BCOM) and S&P Goldman Sachs Commodity Index (S&P GSCI), respectively.

- The best performing sector during the month was Livestock with a return of 8.50% as live cattle and feeder cattle both rallied with returns of 11.86% and 14.99%, respectively.

- The worst performing sector was Energy, down 3.67%, with five of the six constituents negative on the month.

- Precious Metals increased by 0.51% as gold rallied 1.37% while silver declined 5.83%.

- Industrial Metals declined by 3.14% with the best and worst performers being copper and nickel, with returns of -2.00% and -5.92%, respectively.

- The Agriculture sector declined 1.72% where Kansas wheat was the best performer with a return of 1.05% while cocoa was the worst with a return of -12.92%.

Emerging Markets

- Emerging Market (EM) sovereign and corporate external bonds posted positive performance in April. Despite a backdrop of heightened geopolitical tension, external conditions remained generally favorable for the EM fixed income asset class, and global risk sentiment improved significantly following the market-friendly outcome of the first round of the French presidential elections.

- The J. P. Morgan EMBI Global Diversified’s return during the month was driven primarily by spread performance, with the spread over UST tightening a further seven bps to 303 bps, the lowest spread since late 2014.

- EM sovereign and corporate gross issuance is expected to continue its robust performance, which could provide the opportunity to selec-
add to issuers coming with a new issue premium.

International Sovereign

- Global government bonds posted positive returns in the month of April supported by both declining yields amid a backdrop of heightened geopolitical tensions, as well as foreign currency gains against the U.S. Dollar (USD) as markets awaited more clarity on the Trump administration’s fiscal plans.

- The USD, as indicated by the U.S. Dollar Index (DXY), fell during the month. U.S. economic data was generally subdued, and the initial tax blueprint released by the U.S. administration was short on details. While the Trump administration levied tariffs on Canadian soft lumber, it also signaled a willingness to conduct negotiations on NAFTA with Mexico and Canada.

- The UK Pound was the best performing G10 currency during the month. British Prime Minister Theresa May received parliamentary approval for early elections, with her Conservative party enjoying a significant lead in polls over the Labour party.

- The Euro also rose over the month against a backdrop of continued positive Eurozone economic data, and buoyed by a favorable result from the first round of the French presidential elections. The European Central Bank (ECB) maintained its benchmark interest rate and kept its quantitative easing (QE) program unchanged.

- The Japanese Yen traded in a range this month as the Bank of Japan (BoJ) kept its monetary policy unchanged during the month while lowering its inflation forecast slightly, indicating that it may maintain its accommodative monetary policy for some time.

Infrastructure

- Risk appetite remained strong in April as investors sought to add risk amid a period of brisk new issuance. Infrastructure debt in the U.S. Corporate market generally focused on Utility, Power and Transport assets. International infrastructure-related corporate issues were very diverse with assets representing the sectors of Power, Energy Storage, Electric Transmission/Distribution and Transportation assets. After coming off a quiet first quarter, structured product transactions secured by infrastructure assets saw a sharp increase in new issuance. Transactions involving civil aviation, renewable energy and maritime shipping all had several transactions completed during the month of April.

- Investor demand for infrastructure-related debt transactions steadily rose with many transactions being multiple times oversubscribed and often witnessing meaningful spread tightening post new issue launch.

- Fixed income assets, including infrastructure debt, experienced both rate and spread volatility during the month of April. Geopolitical concerns in Asia and the Middle East caused an increased demand for “safer” assets. With this said, MoM both interest rates and credit spreads in infrastructure

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3. G10 - A grouping of 10 countries identified by the World Trade Organization which are “vulnerable” to imports due to ongoing reform in the agricultural sector. This grouping includes Switzerland, Japan, South Korea, Taiwan, Liechtenstein, Israel, Norway, Iceland, Bulgaria and Mauritius.
debt assets tightened. The most pronounced spread tightening was observed in transactions where infrastructure assets had long-term contracts with strong off-takers.

**U.S. Equities**

- In the month of April, the benchmark S&P 500 Index returned 1.03%, ending the month within a half a percent of its early March all-time high. The three best returning sectors of the market were Technology, Consumer Discretionary and Industrials on the expectation of strong first quarter earnings. Three sectors posted negative returns during the month: Telecom (the only sector of the S&P estimated to post negative earnings growth in the first quarter), Energy and Financials. With the yield curve flattening during the month, Financials continued to lose some of their post-election “Trump bump”.

- By the end of April, approximately 58% of the S&P 500 had reported first quarter earnings. According to FactSet, the results through the end of the month indicate when all reports are done the companies of the S&P 500 will have grown earnings by 12.5% YoY. The last time the S&P 500 recorded double-digit earnings growth in the first quarter was 2011. First quarter revenue growth looks to be approximately 7.5%. For the full year, estimates now call for 10.1% earnings growth on 5.3% revenue growth for the S&P 500.

- The recovery in the Energy sector had a significant impact on the earnings growth for the entire S&P 500 Index: According to FactSet, without the Energy sector the S&P 500 earnings in the first quarter would have grown approximately 8.3% rather than 12.5%. Similarly, revenue growth would have been 5.6% rather than 7.5%. We contrast this with the actual performance of the Energy sector of the S&P 500, as measured by the Energy Select Sector Index -- for the twelve months ended April 28, 2017 the sector underperformed the broader S&P 500 by a full 15 percentage points, and YTD had posted negative returns of over 9%.

- Asian equities were mixed in April with Japanese equities, as measured by the Nikkei, up 1.52%. Chinese equities, as measured by the Shanghai Composite, declined -2.07%. Korean equities, as measured by the KOSPI, returned +2.09%.

- EM equities outperformed developed market equities with the MSCI Emerging Markets Index up 2.21%. Brazil’s Ibovespa was up 0.65%. Indian equities, as measured by the Sensex, rallied up 1.01%. Russian equities, as measured by the MSCI Russia, underperformed with the Index returning -0.20% during the month.

**Global Equities**

- Global equities continued to rally in April with the Morgan Stanley Capital International All Country World Index (MSCI ACWI) up 1.60% during the month. U.S. equities produced positive returns with the S&P 500 and Dow Jones 1.03% and 1.45%, respectively. The Russell 2000 Index and Nasdaq Composite were up 1.10% and 2.35%, respectively.

- In Europe, equities outperformed global equities with the Eurostoxx 50 up 2.05% during the month. Regional equities rallied with the DAX up 1.02% and CAC up 3.15%. In the periphery, the FTSEMIB was up 1.04% and IBEX up 3.03%. UK equities, as measured by the FTSE 100, returned -1.33%. European equities rallied as the probability of a Le Pen victory receded.
Bloomberg Barclays U.S. Credit Index—The US Credit component of the U.S. Government/Credit Index. This index consists of publically-issued U.S. corporate and specified foreign debentures and secured notes that meet the specified maturity, liquidity, and quality requirements. To qualify, bonds must be SEC-registered. The US Credit Index is the same as the former US Corporate Investment Grade Index.

Bloomberg Barclays U.S. MBS Index—An index that measures the performance of investment grade fixed-rate mortgage-backed pass-through securities of the Government-Sponsored Enterprises (GSEs): Ginnie Mae (GNMA), Fannie Mae (FNMA), and Freddie Mac (FHLMC).

Bloomberg Commodity Index (BCOM) - An index calculated on an excess return basis that reflects commodity futures price movements. The index rebalances annually weighted 2/3 by trading volume and 1/3 by world production and weight-caps are applied at the commodity, sector and group level for diversification. Roll period typically occurs from 6th-10th business day based on the roll schedule.

Citi High-Yield Cash-Pay Capped Index -This index represents the cash-pay securities of the Citigroup High-Yield Market Capped Index, which represents a modified version of the High Yield Market Index by delaying the entry of fallen angel issues and capping the par value of individual issuers at $5 billion par amount outstanding.

Cotation Assistee en Continu 40 (CAC) - The CAC 40 Index which is a French stock market index. It tracks 40 of the largest French stocks on the Paris Bourse, or stock exchange.

Consumer Price Index (CPI) - A measure that examines the weighted average of prices of a basket of consumer goods and services, such as transportation, food and medical care. The CPI is calculated by taking price changes for each item in the predetermined basket of goods and averaging them; the goods are weighted according to their importance. Changes in CPI are used to assess price changes associated with the cost of living.

Deutsche Borse AG German Stock Index (DAX) - The German stock index, which represents 30 of the largest and most liquid German companies that trade on the Frankfurt Exchange.

Eurostoxx 50 Index - A stock index of Eurozone stocks designed by STOXX, an index provider owned by Deutsche Borse Group and SIX group, with the goal of providing a blue-chip representation of Supersector leaders in the Eurozone.

Financial Times Stock Exchange 100 (FTSE 100) - A capitalization-weighted index of the 100 most highly capitalized companies traded on the London Stock Exchange.

Financial Times Stock Exchange Milano Italia Borsa (FTSE MIB) - The benchmark stock market index for the Borsa Italiana, the Italian national stock exchange, which superseded the MIB-30 in September 2004. The index consists of the 40 most-traded stock classes on the exchange.

Ibovespa - This accumulation index represents the present value of a portfolio begun on 2 January 1968, with a starting value of 100 and taking into account share price increases plus the reinvestment of all dividends, subscription rights and bonus stocks received.

Indice Bursatil Espanol (IBEX) - The official index of the Spanish Continuous Market. The index is comprised of the 35 most liquid stocks traded on the Continuous market. It is calculated, supervised and published by the Sociedad de Bolsas.

Institute for Supply Management Manufacturing Purchasing Managers Index (ISM PMI) - An index made up of data from 300 manufacturing firms collected by the Institute of Supply Management (ISM). It indicates the economic health of the manufacturing sector.

Institute for Supply Management Non-Manufacturing Purchasing Managers Index (ISM PMI) - An index made up of data from 400 non-manufacturing firms collected by the Institute of Supply Management (ISM).

JP Morgan Corporate Emerging Markets Bond Broad Diversified Index (CEMBI) - This index is a market capitalization weighted index consisting of US-denominated Emerging Market corporate bonds. It is a liquid global corporate benchmark representing Asia, Latin America, Europe and the Middle East/Africa.

JP Morgan Government Bond Emerging Markets Broad Diversified Index (GBI EM) - This index is the first comprehensive, global local Emerging Markets index, and consists of regularly traded, liquid fixed-rate, domestic currency government bonds to which international investors can gain exposure.

JP Morgan Emerging Markets Bond Global Diversified Index (EMBI) - This index is uniquely-weighted version of the EMBI Global. It limits the weights of those index countries with larger debt stocks by only including specified portions of these countries’ eligible current face amounts of debt outstanding. The countries covered in the EMBI Global Diversified are identical to those covered by EMBI Global.

Korea Composite Stock Price Index (Kospi) - A market capitalization weighted index of all common stocks traded on the Stock Market Division—previously, Korea Stock Exchange—of the Korea Exchange. It is the representative stock market index of South Korea, similar to the Dow Jones Industrial Average or S&P 500 in the United States.

Markit CMBX Series 6 Index (CMBX.6) - A synthetic tradable index with 6 subindices referencing a basket of 25 commercial mortgage-backed securities offerings issued in 2012.

Morgan Stanley Capital International All Country World Index (MSCI ACWI) - A market-capitalization-weighted index designed to provide a broad measure of stock performance throughout the world, including both developed and emerging markets.

An investment cannot be made in an index.
MSCI Emerging Markets (MSCI EM) - An index that covers 23 Emerging Market countries and is designed to capture the large and mid-cap representation across those countries.

MSCI Russia Index - A free-float capitalization-weighted index used to track the equity market performance of Russian securities on the MICEX Stock Exchange.

Nikkei 225 Index - A price-weighted index comprised of Japan’s top 225 blue-chip companies on the Tokyo Stock Exchange. The Nikkei is equivalent to the Dow Jones Industrial Average Index in the U.S.

Shanghai Composite Index - A capitalization-weighted index that tracks the daily performance of all A-shares and B-shares listed on the Shanghai Stock Exchange. The index was developed on December 19, 1990 with a base value of 100.

S&P Goldman Sachs Commodity Index (GSCI) - Standard & Poor’s Goldman Sachs Commodity Index, or GSCI, is a composite index of commodity sector returns which represents a broadly diversified, unleveraged, long-only position in commodity futures.

S&P 500 Index - Standard & Poor’s US 500 Index, a capitalized-weighted index of 500 stocks.

S&P/LSTA Leveraged Loan Index - An index designed to track the market-weighted performance of the largest institutional leveraged loans based on the market weightings, spreads and interest payments.

An investment cannot be made in an index.
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