Thornburg Income & U.S. Government Bonds

Portfolio Manager Commentary
30 June 2022

Thornburg

Market Review

- Weighed down by a litany of concerns, the fixed income markets experienced one of the worst quarters on record. The list of investor worries going into the second half of the year is lengthy: rampant inflation, hawkish global central bank policy, rate hikes, quantitative tightening, the war in Ukraine, energy costs, slowing economic growth and a potentially looming recession. Yields across nearly every fixed income asset class were up substantially during the quarter as the U.S. Federal Reserve set the pace for other global central banks by hiking the Fed Funds rate in increasing increments in March (+25bps), May (+50bps) and June (+75bps). Spurred by monthly CPI data in May that was worse than expected, June marked the first 75bps hike since 1994 and served as a confirmation that inflation was become entrenched in the U.S. The same week in June the Swiss National Bank hiked rates (+50bps) for the first time in 15 years, as did Brazil's central bank (+50bps), and the Bank of England (+50bps). The data dependent decision-making process at global central banks, akin to driving by looking in the rearview mirror, has left many behind the curve on interest rate policy which has contributed to inflation rising to 40-year highs. As central banks now play catch-up, investors are faced with the likelihood of a not-so-soft landing, and the realization has set in that the recession many feared at the end of 2019 was not avoided by massive fiscal and monetary stimulus, but instead was only delayed.
- Global rate hikes left fixed income investors with no place to hide as bonds sold off along with what felt like every other financial asset during the quarter. Longer duration bonds bore the brunt of the selloff with some debt markets down double digits on the quarter and many down over 20% on a year-to-date basis. The yield on the 10-year U.S. Treasury, which began the quarter at 2.35%, rose to 3.48%, which marked the highest level since February 2011, but managed to pare its losses in the final weeks of June to finish at 3.01%. Global sovereign debt broadly experienced a similar fate as yields on 10-year government debt rose by as much as 120bps in Brazil or as modestly as 7bps in Japan. Rate hikes also took their toll on investment-grade corporates and securitized debt, which were both down substantially for the quarter and for the year. Credit sectors such as U.S. and global high yield corporates also had to contend with recession concerns, igniting a flight to quality that led credit spreads to widen by a couple of hundred basis points during the quarter thus, further compounding losses created by rate movements. The waning weeks of the quarter were surprisingly unlike the previous two months as yields fell following the Fed's June rate hike. Restored credibility in the Fed's willingness and ability to fight inflation, coupled with a looming economic slowdown, led investors to reignite a bid for Treasuries given the ability to purchase bonds at multi-year high yield levels.

> We are taking advantage of volatility to pursue attractive opportunities within fixed income.

Portfolio Managers

Jason Brady, CFA
President and CEO
Portfolio Manager

Lon Erickson, CFA
Portfolio Manager

Jeff Klingelhofer, CFA
Co-Head of Investments
Portfolio Manager

Supported by the entire Thornburg investment team

Performance Summary

- The Thornburg Limited Term Income Fund (I shares) returned -2.64% during the second quarter, modestly underperforming its benchmark, the Bloomberg Intermediate U.S. Government/Credit Index, which returned -2.37%.
- The fund's structural short duration position versus the index was a contributor to relative performance. The 5-year U.S. Treasury yield moved higher by 58 bps to end the quarter at 3.04%, while the 10-year Treasury yield ended the period 68 bps higher at 3.01%.
- Despite the Fund's defensive posture, the allocation to spread sectors ultimately detracted, with relative performance modestly hampered by the Fund's exposure to asset-backed securities, collateralized mortgage obligations and, to a lesser extent, investment grade corporates.

Limited Term Income Fund Average Annual Returns (%, as of 30 Jun 2022)

	QTR	YTD	1-YR	3-YR	5-YR	10-YR	ITD
A Shares THIFX (Incep: 1 Oct 1992)							
Without Sales Charge	-2.65	-6.44	-6.81	0.29	1.26	1.84	4.37
With Sales Charge	-4.83	-8.57	-8.91	-0.22	0.96	1.69	4.31
I Shares* THIIX (Incep: 5 Jul 1996)	-2.64	-6.31	-6.60	0.57	1.56	2.18	4.69
BBG Int US Govt/Credit TR Value Index	-2.37	-6.77	-7.28	-0.16	1.13	1.45	4.32

Limited Term US Government Fund Average Annual Returns (%, as of 30 Jun 2022)

	QTR	YTD	1-YR	3-YR	5-YR	10-YR	ITD
A Shares LTUSX (Incep: 16 Nov 1987)							
Without Sales Charge	-2.08	-5.64	-6.15	-1.03	0.10	0.37	4.14
With Sales Charge	-4.31	-7.77	-8.25	-1.53	-0.20	0.22	4.10
I Shares* LTUIX (Incep: 5 Jul 1996)	-2.00	-5.49	-5.89	-0.76	0.39	0.68	4.49
BBG US Govt Int TR Value Index	-1.65	-5.77	-6.32	-0.30	0.87	0.97	4.86

Ultra Short Income Fund Average Annual Returns (%, as of 30 Jun 2022)

	QTR	YTD	1-YR	3-YR	5-YR	10-YR	ITD
A Shares TLDAX (Incep: 30 Dec 2013)							
Without Sales Charge	-0.19	-1.19	-1.22	1.02	1.48	–	1.37
With Sales Charge	-2.42	-3.45	-3.47	0.51	1.17	–	1.19
I Shares TLDIX (Incep: 30 Dec 2013)	-0.14	-1.10	-1.03	1.22	1.68	–	1.56
ICE BofA US Treasury Bill Index	0.07	0.05	0.07	0.63	1.11	–	0.75

ITD–Inception to Date

*Prior to inception of class I shares, performance is calculated from actual returns of the class A shares adjusted for the lower Institutional expenses.

Periods less than one year are not annualized.

Performance data shown represents past performance and is no guarantee of future results. Investment return and principal value will fluctuate so shares, when redeemed, may be worth more or less than their original cost. Current performance may be lower or higher than quoted. For performance current to the most recent month end, visit thornburg.com or call 877-215-1330. For all funds listed, the maximum sales charge for A shares is 1.50%. There is no up-front sales charge for class I shares. The total annual operating expenses are as follows: Limited Term Income Fund: A shares, 0.77% and I shares 0.50%; Limited Term US Government Fund: A shares, 0.87% and I shares, 0.61%; Ultra Short Income: A shares, 1.38% and I shares, 0.76%; Thornburg Investment Management and/or Thornburg Securities Corporation have contractually agreed to waive fees and reimburse expenses through at least February 1, 2023, for some share classes, resulting in a net expense ratio of the following: Limited Term Income, I shares, 0.49%; Ultra Short Income, A shares, 0.50% and I shares, 0.30%. For more detailed information on fund expenses and waivers/reimbursements, please see the fund's prospectus.

Positioning and Outlook

With central banks in full inflation fighting mode, the chances of a recession have risen rapidly, with the question becoming not if a recession will occur, but potentially how deep it might be. Central banks have a mixed record at best with soft landings, and the Fed is reluctant to admit that some sort of demand contraction is needed to soften inflation. Given this backdrop, portfolio risk continues to be defensively positioned. We incrementally added duration as rates have risen, believing Treasury yields have reached a level somewhat close to fair value, though tail risks remain elevated on both sides. A Fed unable to control inflation and inflation expectations is a recipe for rapidly rising rates. On the flip side, recession fears may well reignite an interest rate rally as investors once again look to Treasuries as a safe haven in times of stress.

Securitized fixed income remains the best relative value proposition in the portfolio. We are constructive on spread levels and favor a bias toward prime consumer issuance. That said, we believe the portfolio has an appropriate level of securitized risk, mindful that spreads could widen further in a risk-off environment. Though recession and inflation fears will remain an overhang, the consumer is broadly coming into the second half of the year in a position of strength. Delinquencies across prime consumer sectors are modestly higher than in 2020-2021, but remain low overall, and in many cases, still below pre-COVID levels. We continue to be cautious on the subprime consumer, given the challenges this cohort could experience should the economy drastically weaken. Within the residential mortgage space, the headwind of rising mortgage rates is being offset by still favorable supply/demand dynamics. While we expect housing market strength to wane, bondholders have plenty of built in protection from lower LTVs and existing loans underwritten with strong lending standards.

Within U.S. corporates, valuations have improved to a point that, as of quarter-end, spreads are clearly above long-term historical averages. While this makes the opportunity set within corporates more interesting, we remain fairly cautious given the weakening macro backdrop and input cost inflation. We have a bias toward names with less cyclicality and more attractive valuations versus recent history. In emerging markets, weakness persists in sympathy with broader risky assets and the weak growth/high inflation narrative. We believe this environment has created security-level mispricing for which we will look to exploit. The timing, however, will be based on evolving domestic and global trends. We continue to look for opportunities in areas with high real rates, advanced policy cycles, and improving domestic demand.

Thanks for your continued support and investing alongside us in Thornburg's fixed income funds.

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Important Information

Unless otherwise noted, the source of all data, charts, tables and graphs is Thornburg Investment Management, Inc., as of 30 June 2022.

Investments carry risks, including possible loss of principal. Portfolios investing in bonds have the same interest rate, inflation, and credit risks that are associated with the underlying bonds. The value of bonds will fluctuate relative to changes in interest rates, decreasing when interest rates rise. Unlike bonds, bond funds have ongoing fees and expenses. Investments in mortgage-backed securities (MBS) may bear additional risk. Investments in the Fund are not FDIC insured, nor are they bank deposits or guaranteed by a bank or any other entity.

U.S. Treasury securities, such as bills, notes and bonds, are negotiable debt obligations of the U.S. government. These debt obligations are backed by the “full faith and credit” of the government and issued at various schedules and maturities. Income from Treasury securities is exempt from state and local, but not federal, taxes.

A bond credit rating assesses the financial ability of a debt issuer to make timely payments of principal and interest. Ratings of AAA (the highest), AA, A, and BBB are investment-grade quality. Ratings of BB, B, CCC, CC, C and D (the lowest) are considered below investment grade, speculative grade, or junk bonds. Investments in mortgage-backed securities (MBS) may bear additional risk.

Asset-backed Security (ABS) – A security whose value and income payments are derived from and collateralized (or “backed”) by a specified pool of underlying assets. The pool of assets is typically a group of small and illiquid assets that are unable to be sold individually. Pooling the assets into financial instruments allows them to be sold to general investors, a process called securitization, and allows the risk of investing in the underlying assets to be diversified because each security will represent a fraction of the total value of the diverse pool of underlying assets.

Basis Point (bp) – A unit equal to 1/100th of 1%. 1% = 100 basis points (bps).

Credit Spread/Quality Spread – The difference between the yields of securities with different credit qualities.

Duration – A bond’s sensitivity to interest rates. Bonds with longer durations experience greater price volatility than bonds with shorter durations.

Consumer Price Index (CPI) - Index that measures prices of a fixed basket of goods bought by a typical consumer, including food, transportation, shelter, utilities, clothing, medical care, entertainment and other items. The CPI, published by the Bureau of Labor Statistics in the Department of Labor, is based at 100 in 1982 and is released monthly. It is widely used as a cost-of-living benchmark to adjust Social Security payments and other payment schedules, union contracts and tax brackets. Also known as the cost-of-living index.

OAS (Option Adjusted Spread) - The flat spread over the treasury yield curve required to discount a security payment to match its market price.

Yield Curve - A line that plots the interest rates, at a set point in time, of bonds having equal credit quality, but differing maturity dates.

The Bloomberg Intermediate US Government/Credit Total Return Index Value Unhedged is an unmanaged, market-weighted index generally representative of intermediate government and investment-grade corporate debt securities having maturities from one up to ten years.

The performance of any index is not indicative of the performance of any particular investment. Unless otherwise noted, index returns reflect the reinvestment of income dividends and capital gains, if any, but do not reflect fees, brokerage commissions or other expenses of investing. Investors may not make direct investments into any index.

The views expressed are subject to change and do not necessarily reflect the views of Thornburg Investment Management, Inc. This information should not be relied upon as a recommendation or investment advice and is not intended to predict the performance of any investment or market.

There is no guarantee that the Fund will meet its investment objectives.

Before investing, carefully consider the Fund's investment goals, risks, charges, and expenses. For a prospectus or summary prospectus containing this and other information, contact your financial advisor or visit thornburg.com. Read them carefully before investing.