Wellington Global High Yield Bond Fund

WELLINGTON MANAGEMENT®

MARKET REVIEW

Most global sovereign yields increased following the Bank of Japan yield curve control adjustment, anticipated inflationary impact of China reopening, and repricing higher-for-longer Fed policy rates. Fixed income spread sectors posted mixed results amid typical weaker liquidity conditions into year end.

US economic data showed positive momentum, underpinned by improved consumer confidence amid a lower inflation print and solid labor market. Annualized GDP growth in the third quarter beat consensus estimates, personal income rose more than expected, while spending fell short of forecasts. Headline and core inflation eased as price declines for used cars, gas, and airfare more than offset higher services costs. The unemployment rate steadied. Nonfarm payrolls gained more than estimated, led by leisure, hospitality, healthcare, and government sectors. Manufacturing and services PMIs moved deeper into contraction owing to a significant drop in new orders as demand waned. Declines in mining and manufacturing activity dragged down industrial production, while utilities output rose as colder-than-usual weather lifted demand for heating. Housing data largely lagged. High mortgage rates hampered pending sales and refinancing volumes. New home sales got a boost from improved activity across the Midwest and West regions.

Euro area manufacturing PMI remained in contraction, faced with weak domestic and global demand. Germany's IFO business climate index exceeded expectations as fears around the gas crisis and supply chain bottlenecks eased. UK manufacturing slowed more than forecasted as soft demand dampened order growth.

FUND PERFORMANCE AND ATTRIBUTION

- The portfolio underperformed its benchmark during the month.
- Quality positioning had a negligible impact on relative performance during the month.
- Regional allocation had a negative impact on relative returns during the month. We maintain an overweight to North America against an underweight to Emerging Markets.
- In aggregate, sector allocation had a negative impact on relative performance during the month. An underweight to the government & government related sector and underweight to financial institutions detracted from relative results. In contrast, an overweight to the home construction sector and underweight to media and entertainment contributed to relative results.
- In aggregate, security selection had a negative impact on relative performance during the month. From a sector perspective, the largest detractors were security selection within health care and the building materials industries. In contrast, the largest positive contributors were security selection within financial institutions and cable and satellite.
- The largest relative detractor was an overweight to Interior Logic Group and the largest relative contributor was an overweight to Country Garden.
- Country Garden is a real estate development company in China. While volatile, we are maintaining the portfolio's position in Country Garden as we believe their liquidity profile remains strong, allowing them to benefit from the recent policy easing from the state. Interior Logic provides interior finish and design technology solutions for homebuilders. Management has guided towards margin improvement and a strong backlog provides a cushion from falling housing demand.

FUND POSITIONING AND OUTLOOK

We maintain a slightly defensive risk posture but will look to take advantage of any dislocations that arise from tighter global monetary policies. The pace of inflation has decelerated, but it is unclear where it will settle and if central banks will feel compelled to continue tightening. While consumer health has held up better than expectations, buoyed by credit growth, excess savings depletion, labor gains, and housing wealth, there are downside risks to the consumer in 2023. The labor market remains tight, and the stickiness of wages will likely be an important factor in the Fed's decision-making process in 2023. We think there is a reasonable likelihood of a mild recession, with a growing tail risk of a more severe slowdown.

Fundamentals are currently good, but likely to be worse in 6-12 months as lagged policy effects work their way through the bottom-up economy. While our expectation is for default rates to move toward long-term averages (~4-5%) over the next 12 months, we do not see a full-scale default cycle on the horizon. Further, with global high-yield credit spreads now above 500 basis points (bps) and "all-in" yields north of 8.9%, we believe market technicals could turn positive as investors seek to capture spreads and yields that are significantly higher than a year ago.

At the end of the month, our largest overweight was to B-rated issuers, and our largest underweight was to the BB segment of the market. Our largest industry overweights were the technology and health care industries. In particular, within technology, our largest overweights include Entegris and Dun & Bradstreet, and within health care, our largest overweights include Medline and IQVIA Holdings. The largest industry underweights in the portfolio were the financial institutions and wireless industries. During the month, we added to our pharmaceuticals and gaming exposure while trimming our exposure to the cable and satellite and technology industries.

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