PIMCO

# Mortgage-Backed Securities Fund

SHARE CLASS: **INSTITUTIONAL** | AS OF: **30 JUNE 2022** | **Quarterly Commentary**

| Fund information | |
|---|---|
| Fund inception date | 31 July 1997 |
| Strategy | Government |
| Total Net Assets (in millions) | $159.1 |
| Portfolio manager(s) | Michael Cudzil<br>Dan Hyman |
| Effective duration (yrs) | 5.83 |
| Benchmark duration (yrs)* | 5.86 |
| Benchmark duration (yrs)** | 6.42 |
| Effective maturity (yrs) | 10.27 |
| Inst. share 30-day SEC yield | 2.63% |

| Class | CUSIP | Ticker |
|---|---|---|
| Institutional | 693391500 | PTRIX |

* The benchmark duration as provided by Barclays.
** The benchmark duration calculated with the methodology used by the PIMCO Mortgage-Backed Securities Fund. The additional benchmark duration is shown in order to achieve consistency in the methodology used in the duration calculations for the benchmark and the Fund.

| Expenses | |
|---|---|
| Gross Expense Ratio (%) | 0.52 |
| | |
| Adjusted Expense Ratio (%) | 0.50 |

The Adjusted Expense Ratio excludes certain investment expenses, such as interest expense from borrowings and repurchase agreements and dividend expense from investments on short sales, incurred directly by the Fund or indirectly through the Fund's investments in underlying PIMCO Funds (if applicable), none of which are paid to PIMCO.

## Performance summary

The PIMCO Mortgage-Backed Securities Fund returned –2.42% after fees in June versus the Bloomberg U.S. MBS Fixed Rate Index, which returned –1.60% for the month. Year-to-date the Fund has returned –9.93% after fees, while the benchmark returned –8.78%.

In the second quarter, the Bloomberg Fixed Rate MBS Index returned -4.01%, underperforming like-duration Treasuries by 98 bps. Legacy non-Agency residential MBS spreads widened 65 bps alongside the broader credit market, and the Bloomberg Non-Agency Investment Grade CMBS Index returned -3.25%, underperforming like-duration Treasuries by 114 bps.

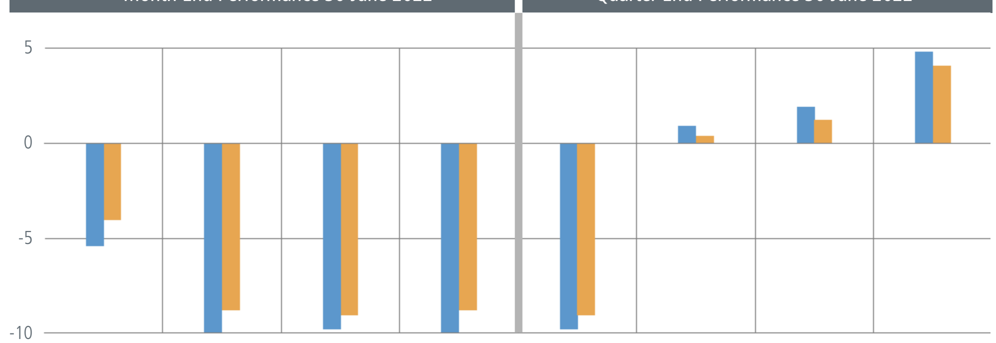
### Contributors

- Structured Agency MBS positions

### Detractors

- U.S. duration positioning
- Exposure to senior non-Agency RMBS
- Agency MBS relative value strategies

Month End Performance 30 June 2022 | Quarter End Performance 30 June 2022




| | 3 Mos. | 6 Mos. | 1 Yr. | YTD | 1 Yr. | 5 Yr. | 10 Yr. | Since Inception |
|---|---|---|---|---|---|---|---|---|
| PIMCO Mortgage-Backed Securities Fund net of fees (%) | -5.41 | -9.93 | -9.76 | -9.93 | -9.76 | 0.90 | 1.87 | 4.78 |
| Bloomberg U.S. MBS Fixed Rate Index (%) | -4.01 | -8.78 | -9.03 | -8.78 | -9.03 | 0.36 | 1.18 | 4.07 |

■ PIMCO Mortgage-Backed Securities Fund net of fees (%) ■ Bloomberg U.S. MBS Fixed Rate Index (%)

*Performance quoted represents past performance. Past performance is not a guarantee or a reliable indicator of future results. Investment return and the principal value of an investment will fluctuate. Shares may be worth more or less than original cost when redeemed. Current performance may be lower or higher than performance shown. For performance current to the most recent month-end, visit PIMCO.com or by calling 888.87.PIMCO.*
For the periods prior to the inception date of a share class, performance information is based on the performance of the Fund's oldest class shares, adjusted to reflect the fees and expenses paid by that class of shares.

Differences in the Fund's performance versus the index and related attribution information with respect to particular categories of securities or individual positions may be attributable, in part, to differences in the pricing methodologies used by the Fund and the index. There is no assurance that any fund, including any fund that has experienced **high or unusual performance** for one or more periods, will experience similar levels of performance in the future. High performance is defined as a significant increase in either 1) a fund's total return in excess of that of the fund's benchmark between reporting periods or 2) a fund's total return in excess of the fund's historical returns between reporting periods. Unusual performance is defined as a significant change in a fund's performance as compared to one or more previous reporting periods.

The minimum initial investment for institutional class shares is $1 million; however, it may be modified for certain financial intermediaries who submit trades on behalf of eligible investors.

**IMPORTANT NOTICE**
Please note that this material contains the opinions of the manager as of the date noted, and may not have been updated to reflect real time market developments. All opinions are subject to change without notice.

**Sector diversification**

| | % Market Value |
|---|---|
| GNMA MBS | 29.6 |
| FNMA, FHLMC and Other Agency MBS | 88.2 |
| Non-Agency MBS | 16.7 |
| Home Equity ABS | 5.5 |
| CMBS | 0.6 |
| Other MBS | 0.0 |
| US Government Related | -31.6 |
| Other [1] | 1.3 |
| Net Other Short Duration Instruments [2] | -10.3 |

Portfolio structure is subject to change without notice and may not be representative of current or future allocations.
MV% may not equal 100 due to rounding.

[1] "Other" may include municipals, convertibles, preferreds, and yankee bonds.

[2] Net Other Short Duration Instruments includes securities and other instruments (except those instruments tied to emerging markets by country of risk) with an effective duration less than one year and rated investment grade or higher or, if unrated, determined by PIMCO to be of comparable quality, commingled liquidity funds, uninvested cash, interest receivables, net unsettled trades, broker money, short duration derivatives and derivatives offsets. With respect to certain categories of short duration securities, the Adviser reserves the discretion to require a minimum credit rating higher than investment grade for inclusion in this category. Derivatives Offsets includes offsets associated with investments in futures, swaps and other derivatives. Such offsets may be taken at the notional value of the derivative position.

## Portfolio positioning

We decreased our relative Agency MBS spread exposure during the quarter but maintained an overweight position relative to the benchmark. We continue to find relative value opportunities between coupons, issuers, and collateral types and view the sector as broadly attractive given its strong liquidity, high quality spread, and diversification benefits versus other risk assets. We have an overweight exposure to Conventional 30-year MBS and GNMA MBS, and an underweight exposure to 15-year MBS. With respect to coupon positioning, we maintain an overweight to higher coupon MBS and an underweight to lower coupon MBS. Within mortgage credit, we continue to favor high quality, senior non-Agency mortgages.

## Quarter in review

Agency MBS[1] returned -4.01% during the quarter, underperforming like duration Treasuries by 98 bps. Volatility in the Agency MBS market persisted during the quarter as rates continued to sell off and the Fed began its balance sheet reductions. Higher coupons outperformed lower coupons, 15 year MBS outperformed 30 year MBS and the FNMA Index outperformed the GNMA Index. During the quarter, the Fed began allowing Agency MBS to run off its balance sheet with a monthly cap of $17.5bn. In June, gross issuance totaled $139bn, decreasing 4% from May and 52% YoY. In May, prepayment speeds decreased by 14% (most recent data). During the quarter, legacy non-Agency residential MBS spreads widened 65 bps alongside the broader credit market, while non-Agency commercial MBS[2] returned -3.25%, underperforming like-duration Treasuries by 114 bps.

The seasonally-adjusted S&P Case-Shiller 20-City Home Price index was up 5.41% over the past 3 months (February to April - latest), while the RCA Commercial Property Price index rose 2.4% from March to May and 18.6% YoY.

Agency MBS sector positioning

| Sector | Portfolio | Benchmark | Difference |
|---|---|---|---|
| 15-year All | 6.0 | 13.2 | -7.2 |
| 30-year GNMA | 27.7 | 20.7 | 7.1 |
| 30-year Conv. | 76.4 | 65.0 | 11.5 |

Agency MBS 30-year coupon stack positioning

| Coupon | Portfolio | Benchmark | Difference |
|---|---|---|---|
| <= 2.0 | 3.5 | 37.4 | -33.9 |
| 2,5 | 0.0 | 24.6 | -24.5 |
| 3,0 | 33.5 | 15.8 | 17.6 |
| 3,5 | 37.5 | 10.7 | 26.8 |
| 4,0 | 20.2 | 6.3 | 13.9 |
| 4,5 | 10.6 | 2.6 | 8.0 |
| 5,0 | 1.8 | 0.9 | 0.9 |
| 5,5 | 0.9 | 0.3 | 0.6 |
| 6,0 | 0.8 | 0.1 | 0.7 |
| 6,5 | 0.5 | 0.0 | 0.5 |
| >= 7.0 | 0.8 | 0.0 | 0.8 |

## Outlook and strategy

Agency MBS markets have seen significant spread widening YTD, but we believe valuations are now more attractive and opportunities for relative value have increased. We have remained underweight in lower coupons given demand pressures and overweight in higher coupons given stronger valuations.

PIMCO remains constructive on senior U.S. securitized credit. Senior Non-Agency MBS stand out as attractive and should benefit from the strong U.S. housing market, which is supported by limited supply and strong borrower fundamentals. Despite increasing rates, we do not believe that affordability will have a material impact on fundamental quality of non-Agency MBS. We believe CMBS remains an attractive opportunity to remain defensive but capture some upside from continued COVID recovery, and we prefer senior CLOs and select ABS among high quality spread assets.

During the quarter, we decreased our relative duration exposure and moved to an underweight duration position versus the benchmark.

**Management profile**

**Michael Cudzil**
Managing Director

**Dan Hyman**
Managing Director

**1997**
**31 JUL**
INCEPTION DATE

**59**
PORTFOLIO MANAGERS

- Average years of experience **15**
- Resources in **4 global offices**

**$159.1MN**
ASSETS UNDER MANAGEMENT

**A high-quality core bond investment**

*Investors should consider the investment objectives, risks, charges and expenses of the funds carefully before investing. This and other information are contained in the fund's prospectus and summary prospectus, if available, which may be obtained by contacting your financial advisor or PIMCO representative or by visiting www.pimco.com. Please read them carefully before you invest or send money.*

Investments made by a Fund and the results achieved by a Fund are not expected to be the same as those made by any other PIMCO-advised Fund, including those with a similar name, investment objective or policies. A new or smaller Fund's performance may not represent how the Fund is expected to or may perform in the long-term. New Funds have limited operating histories for investors to evaluate and new and smaller Funds may not attract sufficient assets to achieve investment and trading efficiencies. A Fund may be forced to sell a comparatively large portion of its portfolio to meet significant shareholder redemptions for cash, or hold a comparatively large portion of its portfolio in cash due to significant share purchases for cash, in each case when the Fund otherwise would not seek to do so, which may adversely affect performance.

**A word about risk:** Investing in the **bond market** is subject to risks, including market, interest rate, issuer, credit, inflation risk, and liquidity risk. The value of most bonds and bond strategies are impacted by **changes in interest rates**. Bonds and bond strategies with longer durations tend to be more sensitive and volatile than those with shorter durations; bond prices generally fall as interest rates rise, and low interest rate environments increase this risk. Reductions in bond counterparty capacity may contribute to decreased market liquidity and increased price volatility. Bond investments may be worth more or less than the original cost when redeemed. Investing in **foreign denominated and/or domiciled securities** may involve heightened risk due to currency fluctuations, and economic and political risks, which may be enhanced in emerging markets. **Mortgage and asset-backed securities** may be sensitive to **changes in interest rates**, subject to early repayment risk, and their value may fluctuate in response to the market's perception of issuer creditworthiness; while generally supported by some form of government or private guarantee there is no assurance that private guarantors will meet their obligations. **Equities** may decline in value due to both real and perceived general market, economic, and industry conditions. **Derivatives** may involve certain costs and risks such as liquidity, interest rate, market, credit, management and the risk that a position could not be closed when most advantageous. Investing in derivatives could lose more than the amount invested. **Diversification** does not ensure against loss.

Morningstar ratings are only shown for those funds that have achieved a 4 or 5 star rating. Ratings for other share classes are either lower or not available.

**Duration** is a measure of a portfolio's price sensitivity expressed in years. Effective duration is the duration for a bond with an embedded option when the value is calculated to include the expected change in cash flow caused by the option as interest rates change.

Bloomberg U.S. MBS Fixed Rate Index covers the mortgage-backed pass-through securities of Ginnie Mae (GNMA), Fannie Mae (FNMA), and Freddie Mac (FHLMC). The MBS Index is formed by grouping the universe of over 600,000 individual fixed rate MBS pools into approximately 3,500 generic aggregates. It is not possible to invest directly in an unmanaged index.



**PIMCO Investments LLC**, distributor, 1633 Broadway, New York, NY, 10019 is a company of PIMCO.

[1]Bloomberg U.S. Agency Fixed Rate Index

[2]Bloomberg Investment Grade Non-Agency CMBS Index

Mortgage-Backed Securities (MBS), Collateralized Loan Obligations (CLO); Commercial Mortgage-Backed Securities (CMBS), Ginnie Mae (GNMA); US Federal Reserve (The Fed); Year over Year (YoY).

The S&P/Case-Shiller Home Price Indices measures the residential housing market, tracking changes in the value of the residential real estate market in 20 metropolitan regions across the United States. In addition, the S&P/Case-Shiller® U.S. National Home Price Index is a broader composite of single-family home price indices for the nine U.S. Census divisions and is calculated quarterly.

The RCA CPPI™ (Commercial Property Price Indices) are a series of transaction-based, repeat-sales regression (RSR) indices developed and published by Real Capital Analytics. RCA CPPI covers a broad range of geographies and property types.

The credit quality of a particular security or group of securities does not ensure the stability or safety of an overall portfolio. The quality ratings of individual issues/issuers are provided to indicate the credit-worthiness of such issues/issuer and generally range from AAA, Aaa, or AAA (highest) to D, C, or D (lowest) for S&P, Moody's, and Fitch respectively.

Like-duration Treasuries are calculated by the index provider by comparing the index return to a hypothetical matched position in Treasuries.

PIMCO