# DoubleLine Asset Allocation Webcast Recap

**Originally aired on October 3, 2017**

## About this Webcast Recap

On October 3, 2017, Deputy Chief Investment Officer (DCIO), Jeffrey Sherman held a webcast discussing the DoubleLine Core Fixed Income Fund (DBLFX/DLFNX) and the DoubleLine Flexible Income Fund (DFLEX/DLINX) titled "Asset Allocation Webcast."

This recap is not intended to represent a complete transcript of the webcast. It is not intended as solicitation to buy or sell securities. If you are interested in hearing more of Mr. Sherman's views, please listen to the full version of this webcast on www.doublelinefunds.com on the **"Webcasts"** tab under **"Latest Webcast"**. You can use the **"Jump To"** feature to navigate to each slide.

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**DoubleLine Core Fixed Income Fund**

| Month-End Returns September 30, 2017 | September | Year-to-Date | Annualized 1-Year | Annualized 3-Year | Annualized 5-Year | Annualized Since Inception (6-1-2010 to 9-30-2017) | Expense Ratio (Gross) |
|---|---|---|---|---|---|---|---|
| I-share (DBLFX) | -0.37% | 4.18% | 1.72% | 3.40% | 3.06% | 5.62% | 0.49% |
| N-share (DLFNX) | -0.39% | 3.99% | 1.47% | 3.12% | 2.80% | 5.36% | 0.74% |
| Bloomberg Barclays U.S. Aggregate Index | -0.48% | 3.14% | 0.07% | 2.71% | 2.06% | 3.38% | |

| Quarter-End Returns September 30, 2017 | 3Q17 | Year-to-Date | Annualized 1-Year | Annualized 3-Year | Annualized 5-Year | Annualized Since Inception (6-1-2010 to 9-30-2017) |
|---|---|---|---|---|---|---|
| I-share (DBLFX) | 1.11% | 4.18% | 1.72% | 3.40% | 3.06% | 5.62% |
| N-share (DLFNX) | 1.05% | 3.99% | 1.47% | 3.12% | 2.80% | 5.36% |
| Bloomberg Barclays U.S. Aggregate Index | 0.85% | 3.14% | 0.07% | 2.71% | 2.06% | 3.38% |

Bloomberg Barclays US Aggregate Index represents securities that are SEC-registered, taxable, and dollar denominated. The index covers the US investment grade fixed rate bond market, with index components for government and corporate securities, mortgage pass-through securities, and asset-backed securities. These major sectors are subdivided into more specific indices that are calculated and reported on a regular basis. It is not possible to invest in an index.

**DoubleLine Flexible Income Fund**

| Month-End Returns September 30, 2017 | September | Year-to-Date | Annualized 1-Year | Annualized 3-Year | Annualized Since Inception (4-7-2014 to 9-30-2017) | Expense Ratio (Gross) |
|---|---|---|---|---|---|---|
| I-share (DFLEX) | 0.04% | 4.53% | 4.79% | 3.59% | 3.68% | 0.85% |
| N-share (DLINX) | 0.02% | 4.35% | 4.44% | 3.30% | 3.40% | 1.10% |
| BAML 1-3 Year Eurodollar Index | -0.03% | 1.65% | 1.33% | 1.53% | 1.44% | |
| LIBOR | 0.11% | 0.88% | 1.11% | 0.66% | 0.61% | |

| Quarter-End Returns September 30, 2017 | 3Q17 | Year-to-Date | Annualized 1-Year | Annualized 3-Year | Annualized Since Inception (4-7-2014 to 9-30-2017) |
|---|---|---|---|---|---|
| I-share (DFLEX) | 1.29% | 4.53% | 4.79% | 3.59% | 3.68% |
| N-share (DLINX) | 1.23% | 4.35% | 4.44% | 3.30% | 3.40% |
| BAML 1-3 Year Eurodollar Index | 0.53% | 1.65% | 1.33% | 1.53% | 1.44% |
| LIBOR | 0.33% | 0.88% | 1.11% | 0.66% | 0.61% |

***Performance data quoted represents past performance; past performance does not guarantee future results. The investment return and principal value of an investment will fluctuate so that an investor's shares, when redeemed, may be worth more or less than the original cost. Current performance of the fund may be lower or higher than the performance quoted. Performance data current to the most recent month-end may be obtained by calling 213-633-8200 or by visiting www.doublelinefunds.com.***

London Interbank Offering Rate (LIBOR) is an indicative average interest rate at which a selection of banks known as the panel banks are prepared to lend one another unsecured funds on the London money market. BAML 1-3 Year Eurodollar Index is a subset of the BAML Eurodollar Index including all securities with a remaining term to final maturity less than 3 years. The BAML Eurodollar Index tracks the performance of US dollar-denominated investment grade quasigovernment, corporate, securitized and collateralized debt publicly issued in the eurobond markets. One cannot invest directly in an index.

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### U.S. Economy

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Gross Domestic Product (GDP)

- U.S. Real GDP has been very stable during the past seven years and continues to hover between 2.0% and 2.3%
  - In the absence of policy changes, DoubleLine does not foresee any alteration to the stability

U.S. Consumer Confidence

- U.S. Consumer Confidence is near cycle highs dating back to 2009
  - This is positive for the economy as consumer spending accounts for roughly 70% of GDP and higher confidence generally leads to more spending
- There is a disconnect between consumer confidence and economic hard data
- Chief Executive Officer (CEO) confidence is also near cycle highs, but will likely be highly correlated to the Trump administration's ability to follow through on prior proposals

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Economic Data

- Soft data, or forward looking sentiment, continued to surprise to the upside since the election
- Hard data, or facts, have disappointed for the most part since election
- This disconnect is worth noting, but it does not imply markets are due for a correction
  - Sentiment, fundamentals and technicals are the 3 main factors that drive markets

### Forward looking indicators in the U.S.

U.S Conference Board Leading Economic Indicators

- Recessions have been preluded by a negative number year-over-year (YOY)
  - We believe it looks like smooth sailing for now as DoubleLine is well above 0 and even in an upward trend

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Institute for Supply Management (ISM) Manufacturing and Services PMI

- U.S. economy is roughly 70% service-based, with the remaining 30% is in manufacturing
- Recessions have been preluded by a ISM manufacturing and Services PMI below 50
  - Currently both are well above 50 and ISM manufacturing PMI is at highest reading seen in this cycle since financial crisis

U.S. Loan Growth

- This chart signifies a bit of trouble
- Historically, the Federal Reserve's (the "Fed") policy is correlated to U.S. loan growth. If loan growth is increasing, Fed will tighten and vice versa. Currently, the opposite is happening. Loan growth YoY is dwindling and approaching 0%, while the Fed continues to raise rates.
- Not overly troubling today, but worth monitoring if loan growth goes to negative year over year.

### Global Macro

Purchasing Managers' Index (PMI) – Eurozone vs. U.S.

- Positive numbers for both U.S. and Eurozone, but significantly more strength in the Eurozone

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German 10-Year Bund yield vs. Consumer Price Index (CPI)

- Big disconnect currently between yields and inflation
- Strangest disconnect is U.S. Treasuries relative to European BB high-yield securities

Inflation

- Despite all the fear and loathing in the marketplace about inflation, U.S. has not reached 2% and the price of inflation is pretty stable globally right now
- The thing for investors to watch as it pertains to inflation is an increase in wages. Right now DoubleLine does not see any rampant inflation around the corner.

Copper/Gold Ratio vs. U.S. Treasury 10-Year yield

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- This is a short term yield indicator for us
- Copper prices have historically gone up in an expansionary market, while higher demand for gold drives ratio down

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- The idea is that the copper/gold ratio will have a push/pull relationship with yield
- As of the time of the podcast the copper gold ratio is showing that the 10-year Treasury is fairly valued
- Clearly, this ratio has nothing to do with fundamental analysis so it is more or less a correlation between two variables that DoubleLine thinks have some economic merit

Interest Rates

- Today's rate environment looks very similar to when rates on the 10-Year U.S. Treasury bottomed in 2016, leading DoubleLine to believe it has seen the bottom in 2017
- While the yield curve has been flattening since 2013, DoubleLine believes it has simply been normalizing and does not portend recession
- London Interbank Offered Rate (LIBOR) rates trending upwards are suggesting the market is pricing in a high probability of a rate hike in December

U.S. Dollar

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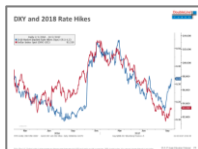


- Based on the Dollar's (DXY) correlation to implied interest rate hikes DoubleLine believes the dollar should continue to rally

Federal Reserve Bank

- Starting this month, the Fed will begin to roll debt off of its balance sheet in the amount of $6 billion (bn) of treasury bonds and $4 bn of Mortgage-Backed Securities (MBS) per month
- Quarterly, the Fed will incrementally increase monthly tightening by $6 bn of treasuries and $4 bn of MBS
- Capping roll off amounts at $30 bn treasuries and $20 bn MBS
- The S&P 500 has been moving in lockstep with the Central Bank's balance sheets, giving DoubleLine reason to be cautious as they begin to unwind

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Fixed Income Index Returns and Valuations

- Year-to-date (YTD) investors have been paid to take risk in the fixed income markets due to dampened volatility and liquidity
- Mortgages relative to Treasuries look fairly valued
- Corporates and High Yield Bonds relative to Treasuries look as expensive as they have ever been since 1985
- Emerging Markets (EM) debt looks slightly rich relative to Treasuries

**DoubleLine Core Fixed Income Fund (DBLFX/DLFNX)**

- Benchmarked to Bloomberg Barclays U.S. Aggregate Index (the "Agg")
- DoubleLine believes now is the time to be more defensive with bond portfolios by investing in high quality bonds and finding relative value amongst fixed income sectors
  - Duration of 4.79- 1.14 years lower than the Agg
  - Average Bond Price is $103.62 vs. the Agg of $104.25

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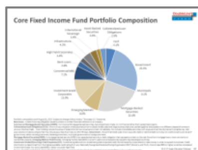


- Composition (as of August 31, 2017)
  - 25.5% U.S. Treasury (UST)
  - 23.4% MBS
  - 13.0% Investment Grade Corporates
  - 8.0% EM
  - 7.1% Commercial MBS
  - 4.3% Infrastructure
  - 3.4% International Sovereign
  - 2.9% Collateralized Loan Obligations

**Slide #** **Recap**

- 2.8% Bank Loans
- 2.4% High Yield Corporates
- 2.0% Asset-Backed Securities
- 0.10% Municipals
- 5.1% Cash

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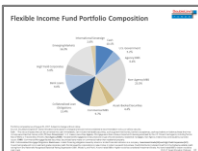


**DoubleLine Flexible Income Fund (DFLEX/DLINX)**

- The fund  is Benchmarked to the Bank of America Merrill Lynch 1-3 Year Eurodollar Index and aims to generate LIBOR-type of returns
- The funds aims to take less duration risk, be more credit sensitive, all while navigating through all interest rate environments
  - Duration of 2.05- 3.88 years lower than the Agg
  - Average Bond Price is $101.47 vs. the Agg of $104.25
- Current composition (as of August 31, 2017)
  - 23.5% Non-Agency MBS
  - 16.2% EM
  - 13.4% Collateralized Loan Obligations
  - 9.7% Commercial MBS
  - 9.0% Bank Loans
  - 5.6% High Yield (HY) Corporates
  - 5.2% UST
  - 4.4% Asset-Backed Securities
  - 2.6% International Sovereign
  - 0.4% Agency MBS
  - 10.1% Cash

**Question & Answer**

CPI is annualized at an extraordinary 1% over six months. What are the odds for mean reversion? Kicks into 3% over the next two quarters?

- I would say they are extremely low, because we haven't seen a three print in a long time, and that's close to pre-crisis levels. You would need to see massive acceleration in commodities. Also consider that 40%-45% of CPI is housing related home prices would need to go up another 15% or so to get to 3%. So I think it's very difficult to get to 3%. I think central tendency right now is about 1.6% unless we change monetary or fiscal policy.

"Are low European Union (EU) rates likely to move up and, therefore, turn to a negative for EU equities over the next year?"

- I think EU rates are likely to move up. They could move up as quickly as an announcement of tapering comes, which would likely put pressure on rates globally. However, I'm not completely sure that would turn negative for EU equities. Rates are very, very low and valuations in the equity market are relatively moderate to below average in the EU. In fact, rising rates could be viewed as signs of strength, as economic data does imply that EU equities should be higher. And so, we remain somewhat positive and optimistic on the EU market.

"If Quantitative Easing (QE) has been disinflationary, will Quantitative Tightening (QT) be inflationary?"

- I don't see QT being inflationary, because we've already borrowed the money. QT is just putting the bonds that are already in existence, out for sale. We are not all of the sudden issuing new bonds. The issuing of the bond is the inflationary moment. This could put some pressure on rates – that's a different question, and the question we should be thinking about. So, unless the tightening encourages people to go on a larger debt binge, we don't see this being an inflationary event.

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## Definitions:

**Consumer Price Index -** 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.

**Duration -** A measure of the sensitivity of the price of a fixed income investment to a change in interest rates, expressed as a number of years.

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

**ISM Manufacturing Index -** 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.

**Purchasing Mangers' Index (PMI) -** Is an indicator of the economic health of the manufacturing sector.

**S&P 500 Index** - S&P 500 Index is based on the market capitalizations of 500 large companies having common stock listed on the NYSE or NASDAQ. The S&P 500 index components and their weightings are determined by S&P Dow Jones Indices.

**U.S. Dollar Index (DXY) -** Is an index (or measure) of the value of the United States dollar relative to a basket of foreign currencies, often referred to as a basket of U.S. trade partners' currencies.

One cannot invest directly in an index.

## Disclaimer

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*Investments in debt securities typically decrease in value when interest rates rise. This risk is usually greater for longer-term debt securities. Investments in lower-rated and non-rated securities present a greater risk of loss to principal and interest than higher-rated securities. Investments in Asset-Backed and Mortgage-Backed Securities include additional risks that investors should be aware of such as credit risk, prepayment risk, possible illiquidity and default, as well as increased susceptibility to adverse economic developments. The Funds may use certain types of investment derivatives. Derivatives involve risks different from, and in certain cases, greater than the risks presented by more traditional investments. Derivatives may involve certain costs and risk 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. The Funds may also invest in securities related to real estate, which may decline in value as a result of factors affecting the real estate industry*

*The Core Fixed Income Fund invests in foreign securities which involve greater volatility and political, economic and currency risks and differences in accounting methods. These risks are greater for investments in emerging markets.*

*The Flexible Income Fund may use leverage which may cause the effect of an increase or decrease in the value of the portfolio securities to be magnified and the fund to be more volatile than if leverage was not used.*

*Credit distributions are determined from the highest available credit rating from any Nationally Recognized Statistical Rating Organization (S&P, Moody's, and Fitch).*

*Diversification does not assure a profit or protect against loss in a declining market.*

Fund holdings and sector allocations are subject to change and are not recommendations to buy or sell any security.

Absolute return funds are not intended to outperform stocks and bonds during strong market rallies, and may underperform during periods of strong positive market performance.

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