PIMCO

Your Global Investment Authority

Call Summary

February 2012

Income Investing in a Low-Yield Environment

On February 15, PIMCO held a conference call for clients, "Seeking Income in a Low-Yield World." Dan Ivascyn, managing director and portfolio manager for PIMCO's Income Strategy, discussed PIMCO's outlook for income investing in 2012, how PIMCO's Income Strategy differs from others, and what sectors of the fixed income market appear attractive.

Daniel J. Ivascyn
Managing Director

PIMCO's outlook: Low yields are likely to remain challenging for income investors

Consistent with the Federal Reserve's current outlook, we think U.S. interest rates will remain on hold until 2014 because global growth is likely to remain low. In our view, the debt crisis in Europe and the lack of new fiscal stimulus in the U.S., among other factors, will keep growth from surprising to the upside.

- Yields are extremely low from an historical perspective: five-year U.S. Treasury bonds yield well below 1% and 10-year Treasuries barely two percentage points more.
- We believe income investors can still find potentially attractive opportunities in high quality sectors, notably mortgage-backed securities, and in global markets, including certain emerging markets where growth is likely to remain strong.

PIMCO's Income Strategy: Focusing on income, total return and high quality

Our Income Strategy focuses first on generating consistently high dividend yield. Unlike many other income strategies, we also emphasize:

- **Total return as an important, secondary objective.** We manage assets with the goal of price appreciation, as well as income generation.
- **High quality.** We attempt to generate dividend income within a relatively low risk investment framework; we tend to avoid illiquid securities and many types of derivatives even though their yields may be attractive.

Because of the high level of uncertainty in the current market, we are focusing on several investment themes as we manage the Income Strategy.

- **Structural seniority.** We target the most senior part of the capital structure in an attempt to minimize the risk of loss. In the corporate sector, we like secured bank loans.
- **Improving fundamentals.** We favor areas of the world where economic fundamentals are improving. Brazil is an example.
- **Diversification.** We seek the best opportunities across the global fixed income sectors and leverage PIMCO's full platform.
- **Being opportunistic.** We try to be aggressive in taking advantage of immediate opportunities as they arise. In the past, we have purchased discounted senior securities during temporary market dislocations.

Portfolio Strategy: Where PIMCO currently sees value

PIMCO's Income Strategy is diversified across all the major fixed income asset classes. We currently favor:

- **Non-agency U.S. ("private label") mortgage-backed securities.** Purchased at significant discounts to par value, they offer high current yields, much more downside protection than high yield corporate bonds, and the potential for price appreciation.
- **U.S. Agency mortgage-backed securities.** Although the potential for refinancing creates some cash flow uncertainty, they can offer 1.5 to 2.0 percentage points more yield than comparable U.S. Treasuries and carry guarantees from the national housing agencies.
- **Corporate credit.** We favor a highly selective corporate credit allocation, of which senior secured bank loans are a part. We are cautious on high yield corporate debt because of our defensive view on the economy.
- **Non-U.S. securities.** We incorporate some opportunistic foreign exposure. We favor quasi-sovereign companies or large established firms that offer attractive yields in emerging markets and specific opportunities in the core of Europe as financial institutions deleverage.
- **Yield curve roll down opportunities.** Where the bond yield curve is steep, we see opportunities to purchase bonds, hold them for a period of time, and sell them when they are closer to maturity, if their market values have increased.

Overall, PIMCO's Income Strategy aims to provide strong dividend yield and an attractive total return for investors. We focus on dividend sustainability because we understand the importance of a consistent income stream.

A word about risk: Past performance is not a guarantee or reliable indicator of future results. Investing in the bond market is subject to certain risks including market, interest-rate, issuer, credit, and inflation risk; 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. High-yield, lower-rated, securities involve greater risk than higher-rated securities; portfolios that invest in them may be subject to greater levels of credit and liquidity risk than portfolios that do not. 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.

Bank loans are often less liquid than other types of debt instruments and general market and financial conditions may affect the prepayment of bank loans, as such the prepayments cannot be predicted with accuracy. There is no assurance that the liquidation of any collateral from a secured bank loan would satisfy the borrower's obligation, or that such collateral could be liquidated.

Statements concerning financial market trends are based on current market conditions, which will fluctuate. There is no guarantee that these investment strategies will work under all market conditions, and each investor should evaluate their ability to invest for the long-term, especially during periods of downturn in the market. Outlook and strategies are subject to change without notice.

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