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PIMCO TRENDS Managed Futures: Seeking Diversification and Returns

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Managed futures strategies have produced positive returns during sustained equity market downturns, but not all funds are designed with the agility to generate "crisis alpha" during periods of sudden volatility. Matt Dorsten, co-portfolio manager of the PIMCO TRENDS Managed Futures Strategy Fund, and Christopher Santore, product strategist, talk with Mike Connor, product strategist, about how funds differ in their objectives and design.

Q: WHAT ARE REASONABLE LONG-TERM OBJECTIVES FOR MANAGED FUTURES STRATEGIES?

Dorsten: Managed futures strategies use systematic trend-following to pursue a valuable set of objectives: **positive returns** over long holding periods, **diversification** through negative equity correlation, and **crisis alpha** through positive returns across periods of sustained market volatility.

Over the long-run, trend-following strategies have delivered returns that are similar to equity markets, with lower volatility and a negative correlation to equities, attracting allocations from investors seeking diversification from equity risk (see Figure 1).

Figure 1: Managed futures have delivered equity like returns over the long run

	Managed futures	Global equities
Jan 2000 - May 2021	SG Trend Index	MSCI World Index
Return (p.a.)	5.36%	5.45%
Volatility (p.a.)	13.61%	15.48%
Correlation	-0.05	

Source: PIMCO and Bloomberg as of date 31 May 2021. The SG Trend Index tracks the 10 largest Commodity Trading Advisors to be representative of the trend followers in the managed futures category.

Q: HOW HAVE INVESTORS USED MANAGED FUTURES?

Santore: After performing well through sustained equity market drawdowns (see Figure 2), trend-following has gained popularity in risk-mitigating allocations alongside traditional defensive investments such as government bonds and equity put options.

We believe that trend-following offers investors a compelling value proposition as a strategy that can capitalize on market volatility. In 2020 for example, trend-followers seized opportunities from both long and short positions across asset classes as portfolios adapted to crisis conditions in the first quarter, followed by a risk asset rally in the second half of the year. Looking forward, we believe trend-followers are well-positioned to continue meeting expectations, and encourage allocators seeking equity diversification to focus on strategies specifically designed to emphasize diversification.

Figure 2: Trend-following returns across major equity market drawdowns

10 worst quarters in MSCI World since 2000		MSCI World	SG Trend	Difference
Q4 2008	Global financial crisis (Lehman)	-22.2%	12.7%	34.8%
Q1 2020	Coronavirus	-21.4%	2.3%	23.7%
Q3 2002	U.S. accounting scandals	-18.7%	18.0%	36.7%
Q3 2011	Taper tantrum, Euro crisis	-17.1%	2.4%	19.5%
Q3 2008	Global financial crisis	-15.7%	-6.9%	8.8%
Q3 2001	9/11	-14.6%	3.9%	18.5%
Q4 2018	Slowing global growth	-13.7%	-5.1%	8.7%
Q2 2010	U.S. 'flash crash'	-13.3%	-3.1%	10.2%
Q1 2001	U.S. recession	-13.1%	10.6%	23.7%
Q1 2009	Global financial crisis (bailouts)	-12.5%	-2.7%	9.8%

Source: PIMCO and Bloomberg as of 31 May 2021

Q: WHAT MARKET ENVIRONMENTS TEND TO BE BEST FOR MANAGED FUTURES?

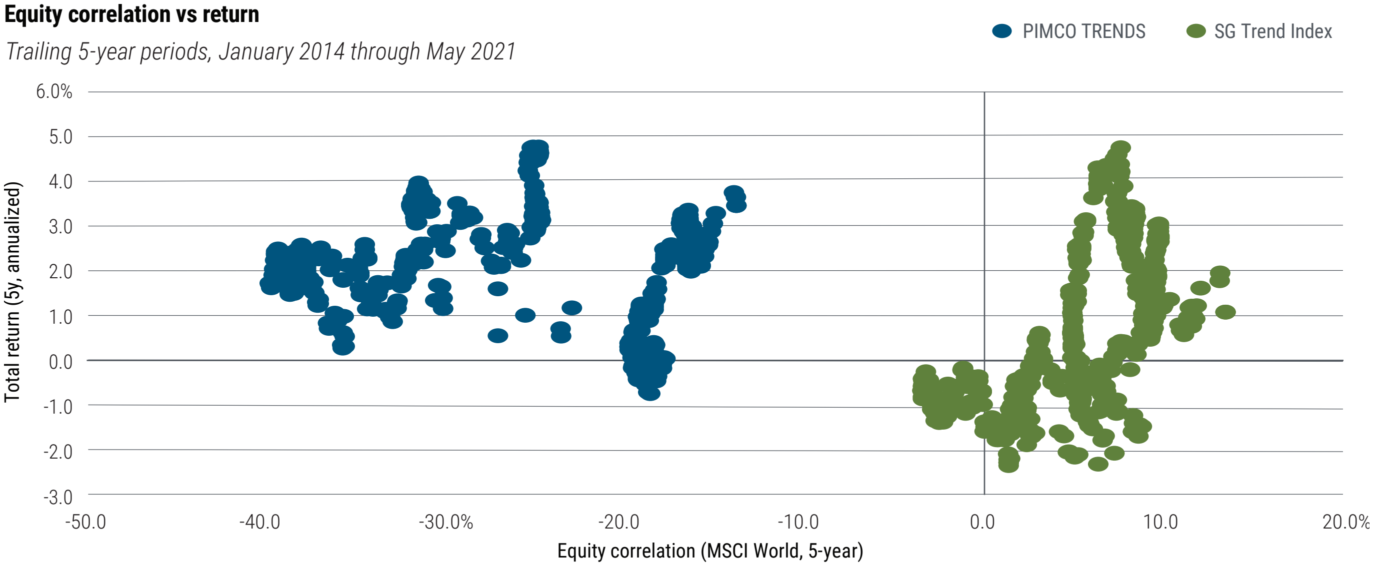
Dorsten: Trend-following portfolios have historically performed best during periods of elevated market volatility, when equities tend to struggle, and when investors value diversifying strategies the most. Trend-following thrives during periods of market volatility by building larger positions as persistent trends develop, producing an inherently diversifying distribution of returns that often performs best in the most volatile market conditions. In particular, equity sell-offs have often been productive environments for trend-following as persistent equity declines drive risk reducing behavior across asset classes, creating more potential trends to follow.

However, not all managed futures strategies have successfully navigated recent bouts of market volatility, such as the fourth quarter of 2018 and the first quarter of 2020, suggesting that some managed futures strategies may either include non-trend strategies that are less consistently defensive, or may allow for more long equity risk that can degrade the equity diversification potential. By contrast, the PIMCO TRENDS Managed Futures Strategy has remained focused on trend-following, with a steadfast commitment to equity diversification as a primary objective.

Figure 3: Not all managed futures strategies have been reliably defensive

Equity correlation vs return

Trailing 5-year periods, January 2014 through May 2021



Source: PIMCO, Bloomberg as of date 31 May 2021. **For illustrative purposes only.**

At PIMCO, our TRENDS Managed Futures Strategy seeks an enhanced return potential in higher-volatility markets through a number of design features, including:

- Emphasizing short- to medium-term trend signals that have historically outperformed across equity drawdowns,
- Imposing a conservative limit on the maximum equity beta, and
- Trading a broad and diverse investment universe selected to enhance return potential rather than maximize capacity.

Our results in Figure 4 demonstrate the value-add of such a disciplined approach, resulting in more consistent diversification and performance over the long-term. Our strategy has consistently generated strong returns across volatile markets – such as in the first quarter of 2020 and in fourth quarter of 2018 – and generated more muted positive returns in low volatility risk-on environments such as 2017.

Q: HOW DOES PIMCO TRENDS TARGET AN ENHANCED DIVERSIFICATION PROFILE?

Santore: At PIMCO, we've enhanced the diversification potential of our strategy by capping equity beta to limit the potential long equity exposure of the portfolio without sacrificing return potential. This is possible because, counterintuitively, there's a surprisingly weak relationship between the equity positioning of trend-following strategies and subsequent returns. In practice, limiting the maximum equity beta of the trend-following portfolio reduces the size of positions with positive equity betas when the portfolio would otherwise exceed the limit. This effectively embeds a dynamic sizing feature by allowing the portfolio to have larger potential positions when it offers more potential diversification benefits. Of course, this can cause the strategy to miss out on some potential returns from long equity positions that an unconstrained portfolio with a higher equity beta would capture. But for allocators seeking equity diversification, our research shows that the short-term trade-offs of limiting long equity exposure are worthwhile over the long-term.

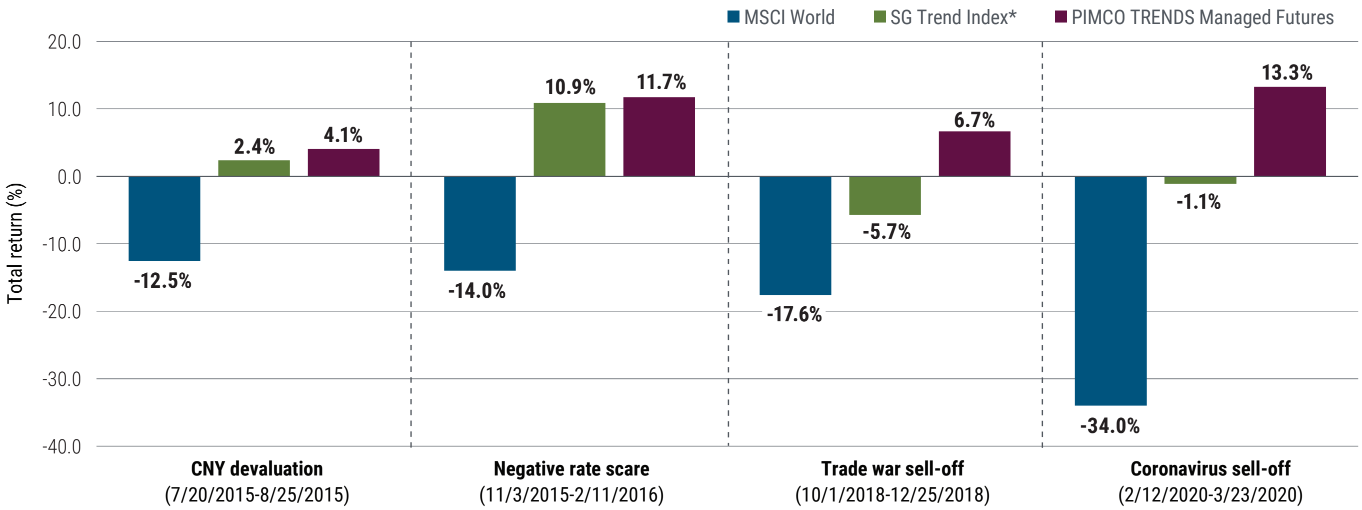
Q: HOW DOES PIMCO TRENDS TARGET CRISIS ALPHA THROUGH POSITIVE RETURNS ACROSS MARKET CRISES?

Dorsten: Negative average equity correlations have historically enabled managed futures to provide strong positive returns during sustained equity market sell-offs. Briefer equity sell-offs, however, have resulted in mixed outcomes across managed futures funds. Yet even during brief and moderate equity declines (exceeding 10%), PIMCO TRENDS Managed Futures Strategy has, since its inception in December 2013, delivered consistently positive returns that have outperformed the SG Trend Index.

Figure 4: Defensive features can enhance potential crisis alpha

PIMCO TRENDS has consistently delivered crisis alpha

All 10%+ MSCI World drawdowns since ('13 December incep.). MSCI World peak-to-trough returns.



Source: PIMCO and Bloomberg as of 31 May 2021. The Covid-19 Crisis is represented by the period 12 February 2020 - 23 March 2020. The Covid-19 Crisis is ongoing and is used for illustration purposes only, and may not be reflective of the current environment.

PIMCO TRENDS Managed Futures Strategy Fund performance results (as of 31 March 2021)

	3-mos	1-year	3-years	5-years	Since inception	Inception date
After fees (%)	3.13	4.90	6.38	3.19	4.45	31 Dec '13
3 Month USD Libor Index (%)	0.06	0.56	1.77	1.49	1.12	

Performance is shown for the institutional class. Performance is net average annual returns, and periods less than one year are cumulative.

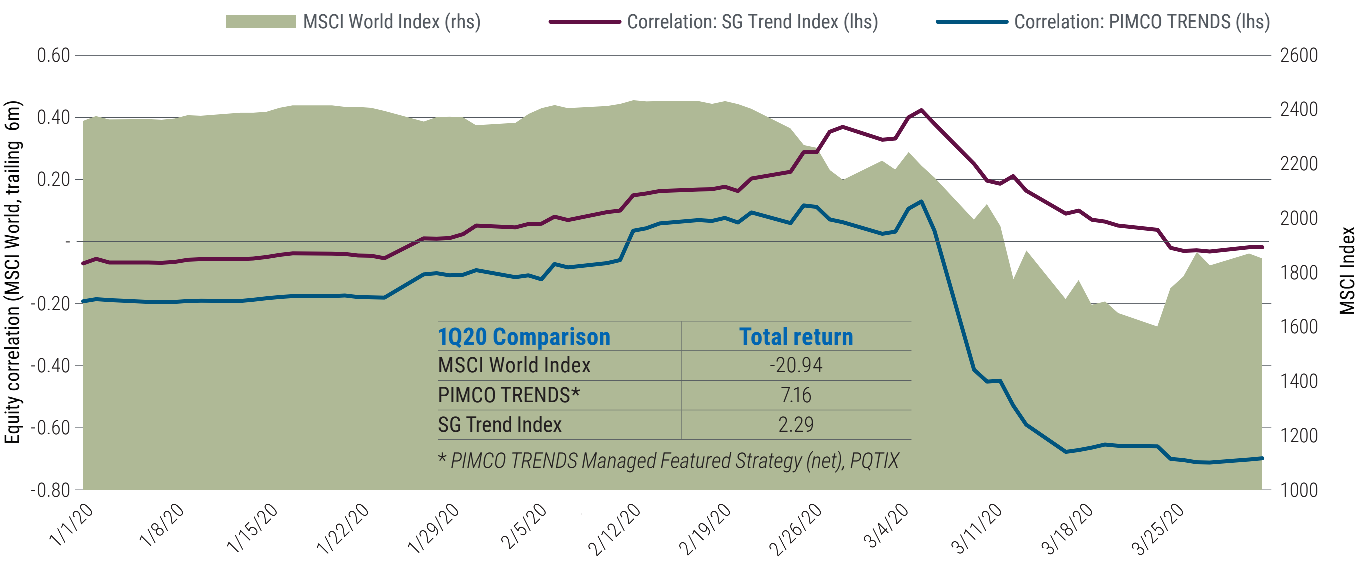
Performance quoted represents past performance. Past performance is not a guarantee or a reliable indicator of future results. Current performance may be lower or higher than performance shown. Investment return and principal value will fluctuate, so that fund shares may be worth more or less than their original cost when redeemed. Performance data current to the most recent month-end is available at www.pimco.com on the fund page, or by calling 888.87.PIMCO.

Gross expense ratio is 1.69%.

PIMCO TRENDS Managed Futures Strategy prioritizes crisis alpha (i.e., generating positive return during periods of high financial stress) partly by emphasizing relatively fast-moving trend signals designed to adapt quickly to changing market conditions. During the March 2020 COVID-19-induced market crash, for example, moving quickly to net short equity exposure was critical in driving positive returns, as slower signals missed out on some of the decline (see Figure 5 below). And while moving quickly introduces higher turnover and potentially more exposure to sudden market reversals, we've calibrated our trend-signal speed to prioritize potential performance in equity sell-offs.

Figure 5: Prioritizing crisis alpha was a clear benefit in March 2020

Moving quickly was critical to capture crisis alpha in 1Q20



Source: PIMCO and Bloomberg as of 31 May 2021

Q: WHAT SHOULD INVESTORS EXPECT FROM THE PIMCO TRENDS MANAGED FUTURES STRATEGY GOING FORWARD?

Santore: Going forward, we expect our defensive-oriented trend-following strategy to continue to seek to deliver on our long-term objectives: **positive returns** over long holding periods, **diversification** through negative equity correlations, and **crisis alpha** through periods of sustained market volatility. Investors must understand that not all managed futures strategies share these objectives and make the same trade-offs in strategy design. Accordingly, we advise allocators to focus on the role managed futures strategies are meant to play in their portfolio. Allocators prioritizing defensive characteristics may choose different strategies than allocators seeking to maximize returns in an equity rally.

At PIMCO, we believe that managed futures allocations can have the most positive impact during volatile market conditions and have designed our strategy with clear objectives in mind.

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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 investment professional or PIMCO representative or by visiting www.pimco.com. Please read them carefully before you invest or send money.

Past performance is not a guarantee or a reliable indicator of future results. The performance figures presented reflect the total return performance, unless otherwise noted, for Institutional Class shares (after fees) and reflect changes in share price and reinvestment of dividend and capital gain distributions. All periods longer than one year are annualized. Periods less than one year are cumulative. The minimum initial investment for Institutional, I-2, I-3 and Administrative class shares is $1 million; however, it may be modified for certain financial intermediaries who submit trades on behalf of eligible investors.

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.

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.

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. **The fund will seek exposure to commodities** through commodity-linked derivatives and through the PIMCO Cayman Commodity Fund VIII Ltd., a wholly-owned subsidiary of the Fund organized under the laws of the Cayman Islands (the "Subsidiary"). The Subsidiary is advised by PIMCO, and has the same investment objective as the Fund. The Subsidiary (unlike the Fund) may invest without limitation in commodity-linked swap agreements and other commodity-linked derivative instruments. **Commodities** contain heightened risk including market, political, regulatory, and natural conditions, and may not be appropriate for all investors. **Derivatives and commodity-linked 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. Commodity-linked derivative instruments may involve additional costs and risks such as changes in commodity index volatility or factors affecting a particular industry or commodity, such as drought, floods, weather, livestock disease, embargoes, tariffs and international economic, political and regulatory developments. Investing in derivatives could lose more than the amount invested. **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. **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. 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. The **models** evaluate securities or securities markets based on certain assumptions concerning the interplay of market factors. Models used may not adequately take into account certain factors, may not perform as intended, and may result in a decline in the value of your investment, which could be substantial. **Diversification** does not ensure against loss.

The correlation of various indexes or securities against one another or against inflation is based upon data over a certain time period. These correlations may vary substantially in the future or over different time periods that can result in greater volatility.

Alpha is a measure of performance on a risk-adjusted basis calculated by comparing the volatility (price risk) of a portfolio vs. its risk-adjusted performance to a benchmark index; the excess return relative to the benchmark is alpha. Beta is a measure of price sensitivity to market movements. Market beta is 1.

The SG Trend Index calculates the net daily rate of return for a group of 10 trend following CTAs selected from the largest managers open to new investment. The SG Trend Index is equal-weighted and reconstituted annually and has become recognized as the key managed futures trend following performance benchmark. The MSCI World Index is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of developed markets. The MSCI World Index consists of 23 developed market country indices. It is not possible to invest directly in an unmanaged index.

There is no guarantee that these investment strategies will work under all market conditions or are appropriate for all investors and each investor should evaluate their ability to invest long-term, especially during periods of downturn in the market

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