# Strategic Credit Fund

3Q 2019 Commentary

## Summary

Corporate credit markets continued their strong 2019 with positive returns in the third quarter as falling interest rates, expectations for additional stimulus from global central banks and steady credit fundamentals boosted investment grade corporate bonds, high yield bonds and bank loans.

## Market Environment

**Corporate credit benefited from increasingly dovish posturing by the Federal Reserve (Fed) and European Central Bank (ECB).**

The rally in risk-free rates was the primary driver of the strong corporate credit returns. Risk-free rates moved lower and flatter during the quarter as global growth and inflation numbers continued to slow, and also as key central banks either cut rates, announced more asset purchases, or expressed a more dovish view. The Fed was active on this front, twice cutting the Fed Funds rate (25 basis points each time) during the quarter. The 10-year yield fell from 2.00% at the end of the second quarter to 1.68% at the end of September, while the 2-year yield fell from 1.75% to 1.63% and the 3-month yield fell from 2.12% to 1.88%. This marks the second quarter in a row where the Treasury yield curve ended the period with the 3-month yield higher than the 10-year yield. While many have historically viewed an inverted yield curve as a reliable predictor of a recession, the Fed and other central banks appear committed to providing the stimulus necessary to support the economy and financial markets if economic data fails to improve.

Corporate credit spreads were flat to marginally better during the quarter, with the exception of distressed issues, which understandably underperformed in the weakening growth environment. While defaults increased in the third quarter, we believe the overall default environment continues to be benign with current default rates well below long-term averages. Additionally, net supply in the high yield market remains low, which should provide support to the corporate credit market.

The inherent interest rate sensitivity of investment grade corporates led to the sector's outperformance of high yield bonds and bank loans as rates declined. Investment grade corporates, as measured by the Bloomberg Barclays U.S. Corporate Investment Grade Index, returned 3.05% in the third quarter; high yield bonds, as measured by the FTSE BB/B Excluding B/CCC Splits Index, returned 1.54%; and bank loans, as measured by the Credit Suisse Leveraged Loan Index, returned 0.92%.

## Performance and Attribution Summary

**The Aristotle Strategic Credit Fund (ARSSX) returned 1.92% at NAV in the third quarter, outperforming the 1.51% return of its blended benchmark of one-third Bloomberg Barclays U.S. High Yield Ba/B 2% Issuer Cap Index, one-third Bloomberg Barclays U.S. Intermediate Corporate Index and one-third Credit Suisse Leveraged Loan Index. Positive performance relative to the Fund's blended benchmark was driven primarily by positive security selection, with industry allocation also adding value.**

Security selection was the largest contributor to relative performance, driven by strong performance of holdings within the Energy and Insurance industries; partially offset by negative security selection within the Finance and Gaming industries.

Industry allocation also added value during the third quarter, as the Fund benefited from an underweight in Energy and an overweight in Gaming; partially offset by underweights in Aerospace & Defense and Media Entertainment, which detracted from relative performance.

Sector rotation was neutral to relative performance as the underweight in bank loans was additive, though offset by the allocation to cash in the strong return environment.

| Top Five Contributors | Top Five Detractors |
|---|---|
| Southern California Edison | Lennar |
| Sprint | Unit |
| Fiserv | Weld North Education |
| AT&T | Meredith |
| Dell | West |

*Performance data quoted here represents past performance. Past performance is no guarantee of future results. Investment return and principal value will fluctuate, so that an investor's shares, when redeemed, may be worth more or less than their original cost. Current performance may be lower or higher than the performance information quoted. To obtain current performance information to the most recent month-end, please call (844) 274-7868.*

## Outlook and Strategy

**We believe accommodative central bank policies, positive credit fundamentals and relatively low supply remain supportive of corporate credit, though we are somewhat cautious on valuations for lower quality credit.**

We believe that sluggish global economic growth, tame inflation, accommodative central bank policies and negative risk-free rates overseas will provide a strong bid to U.S. risk-free assets; and that a still healthy U.S. economy, albeit growing at a more moderate pace, should restrain interest rates from falling much further. Thus, we expect risk-free rates to reside in a range-bound market through year-end.

In our view, higher quality corporate credit will likely see spreads relatively range-bound, also, due to a modestly supportive U.S. economic backdrop, the strong global bid for yield, and fair valuations. In addition, we believe equity and bond investors will continue to favor companies with more modest or declining leverage, providing further support for valuations. In terms of performance, we expect higher quality corporate credit to give investors a "coupon-like" return throughout the remainder of the year. Lastly, we remain cautious on the more speculative and distressed segments of the market.

*Strategic Credit Positioning*

**The Fund remains overweight in high yield bonds and has shifted some exposure from floating-rate bank loans to investment grade corporates.**

As of September 30, 2019, the Fund was composed of 38.1% investment grade corporates, 37.3% high yield bonds and 22.1% bank loans, with the balance in cash. The shift from bank loans to investment grade bonds has been based on the current interest rate environment and concerns regarding deteriorating fundamentals and covenants within the bank loan market.

The Fund's significant active exposures at quarter-end included overweights in the Insurance, REITs and Real Estate Related, Telecommunications and Gaming, Lodging & Leisure industries and underweights in the Banking, Technology, Chemicals and Energy industries.

## Aristotle Strategic Credit Fund (Class I)

Performance Update September 30, 2019

| Total Return | 3Q19 | YTD | 1 Year | 3 Years | Since Inception (12/31/14) | Gross/Net Expense Ratio |
|---|---|---|---|---|---|---|
| ARSSX Class I | 1.92% | 10.31% | 7.07% | 4.62% | 4.40% | 4.03%/0.62% |
| Blended Benchmark* | 1.51% | 9.22% | 6.98% | 4.74% | 4.69% | N/A |
| Bloomberg Barclays U.S. Aggregate Bond Index | 2.27% | 8.52% | 10.30% | 2.92% | 3.17% | N/A |
| Bloomberg Barclays U.S. High Yield Ba/B 2% Issuer Cap Index | 1.85% | 12.35% | 8.30% | 6.03% | 5.82% | N/A |

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***The Fund's advisor has contractually agreed to waive certain fees and/or absorb expenses, through April 30, 2020, to the extent that the total annual operating expenses do not exceed 0.62% of average daily net assets of the Fund. The Fund's advisor may seek reimbursement from the Fund for waived fees and/or expenses paid for three years from the date of the waiver or payment. Without these reductions, the Fund's performance would have been lower. A redemption fee of 1.00% will be imposed on redemptions of shares within 30 days of purchase.***

**The blended benchmark represents a blend of 1/3 Bloomberg Barclays U.S. High Yield Ba/B 2% Issuer Cap Index, 1/3 Bloomberg Barclays* U.S. *Intermediate Corporate Index and 1/3 Credit Suisse Leveraged Loan Index. The Bloomberg Barclays U.S. High Yield Loans Index was retired on September 30, 2016 and was replaced with the Credit Suisse Leveraged Loan Index effective October 1, 2016.*

Important Information:

There can be no guarantee that any strategy (risk management or otherwise) will be successful. All investing involves risk, including potential loss of principal.

The views in this commentary were as of the date stated and may not necessarily reflect the same views on the date this letter is first published or any time thereafter. These views are intended to help shareholders in understanding the Fund's investment methodology and do not constitute investment advice.

Past performance is not indicative of future results. You should not assume that any of the securities transactions, sectors or holdings discussed in this report are or will be profitable, or that recommendations Aristotle Credit makes in the future will be profitable or equal the performance of the securities listed in this report. There is no assurance that any securities, sectors or industries discussed herein will be included in or excluded from the Fund. Fund composition will change due to ongoing management of the Fund. References to specific securities or sectors should not be construed as recommendations by the Fund, its Advisor or Distributor. The opinions expressed are as of the date of publication and are subject to change due to changes in the market or economic conditions and may not necessarily come to pass Aristotle Credit reserves the right to modify its current investment strategies and techniques based on changing market dynamics or client needs. This is not a recommendation to buy or sell a particular security. Holdings are available within the last 12 months.

An investment in the Fund is subject to risks and you could lose money on your investment in the Fund. The principal risks of investing in the Fund include, but are not limited to, investing in fixed income securities, high yield bonds, bank loans, foreign securities and emerging markets.

The prices of fixed income securities respond to economic developments, particularly interest rate changes, as well as to changes in an issuer's credit rating or market perceptions about the creditworthiness of an issuer. High yield bonds are debt securities rated below investment grade (often called "junk bonds"). Junk bonds are speculative, involve greater risks of default, downgrade, or price declines and are more volatile and tend to be less liquid than investment-grade securities. The Strategic Credit Fund's investments in assignments of bank loans may create substantial risk. Although the Strategic Credit Fund expects it will invest in senior and secured bank loans, the Fund may invest in unsecured or subordinated loans. In addition, the Fund may invest in secured and unsecured participations in bank loans. These bank loans will generally be rated below investment grade. Foreign securities have additional risks including currency rate changes, political and economic instability, lack of comprehensive company information, less market liquidity, less efficient trading markets, and differing auditing controls and legal standards. Investments in emerging markets involve even greater risks.

Credit quality ratings are sourced from Standard & Poor's (the "S&P"), Moody's and Fitch's. Ratings values are based on the higher of either S&P, Moody's or Fitch's. If none of the rating agencies have assigned a rating the Fund will assign a rating of NR (non-rated security). The ratings represent their (S&P, Moody's, Fitch's) opinions as to the quality of the securities they rate. The ratings from AAA (S&P, Fitch's) or Aaa (Moody's) (extremely strong capacity to meet its financial commitment) to D (S&P, Fitch's) or C (Moody's) (in default). Ratings are relative and subjective and are not absolute standards of quality. The ratings provided relate to the underlying securities within the fund and not the fund itself.

Definitions:

- The Fund is benchmarked to a blend of three indices: 1/3 Bloomberg Barclays U.S. High Yield Ba/B 2% Issuer Cap Index, 1/3 Bloomberg Barclays U.S. Intermediate Corporate Index and 1/3 Credit Suisse Leveraged Loan Index. The Bloomberg Barclays U.S. High Yield Loans Index was retired on September 30, 2016 and was replaced with the Credit Suisse Leveraged Loan Index effective October 1, 2016.
- The Bloomberg Barclays U.S. High Yield Ba/B 2% Issuer Cap Index is an issuer-constrained version of the U.S. Corporate High-Yield Index that measures the market of U.S. dollar-denominated, non-investment grade, fixed-rate, taxable corporate bonds rated Ba/B. The Index limits the maximum exposure to any one issuer to 2%.
- The Bloomberg Barclays U.S. Intermediate Corporate Index is designed to measure the performance of U.S. corporate bonds that have a maturity of greater than or equal to 1 year and less than 10 years. The Index includes investment grade, fixed-rate, taxable, U.S. dollar denominated debt with $250 million or more par amount outstanding, issued by U.S. and non-U.S. industrial, utility and financial institutions.
- The Credit Suisse Leveraged Loan Index is designed to mirror the investable universe of the U.S. dollar-denominated leveraged loan market.
- The Bloomberg Barclays U.S. Aggregate Bond Index is an unmanaged index of domestic investment grade bonds, including corporate, government and mortgage-backed securities.
- The Bloomberg Barclays U.S. Corporate Investment Grade Index measures the performance of investment grade corporate bonds that are U.S. dollar-denominated and have a remaining maturity of greater than one year.
- The FTSE BB/B Excluding B/CCC Splits Index is a high yield market index, which includes BB-rated and B-rated bonds. This is a sub-index of the U.S. High Yield Market Index excluding bonds rated B/CCC and below.
- Treasuries are negotiable debt obligations of the U.S. government secured by its full faith and credit and issued at various schedules and maturities.

The volatility (beta) of the Fund may be greater or less than the benchmarks. It is not possible to invest directly in these indices.

Fund composition will change due to ongoing management of the Fund. References to specific securities or sectors should not be construed as recommendations by the Fund, its Advisor or Distributor.

As of September 30, 2019, the ten largest holdings in the Fund and their weight as a percent of total net assets were: CSC Holdings, LLC January 2018 Incremental Term Loan, 2.39%; Concentra Inc. Tranche B-1 Term Loan (First Lien), 2.36%; Rackspace Hosting, Inc. Term B Loan (First Lien), 2.36%; USI, Inc. (fka Compass Investors Inc.) 2017 New Term Loan, 2.34%; Penn National Gaming, Inc. Term A Facility Refinancing Loan, 2.24%; Astro AB Borrower, Inc. Tranche B Term Loan (First Lien), 2.16%; Prudential Financial Inc, 1.95%; Anheuser-Busch InBev Worldwide Inc, 1.69%; Southern California Edison Co, 1.54%; Sprint Communications, Inc. Initial Term Loan, 1.50%.

**Please consider the Fund's investment objectives, risks, charges and expenses carefully before investing. The prospectus or summary prospectus that contains this and other information about the Fund is available by calling (844) 274-7868, or by visiting www.aristotlefunds.com, and should be read carefully prior to investing.**

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