

Bonds Be Nimble, Bonds Be Quick

Exploiting inefficiencies with active management

Fixed income investors can exploit a wide variety of pricing inefficiencies—across sectors, geographies, and currencies—by conducting thorough credit research and carefully managing portfolios. These inefficiencies aren't static; they ebb and flow as relative values shift across markets.

We believe inefficiencies persist because of benchmark construction, execution complexities, and market and investor segmentation. Two of Allspring's fixed income teams demonstrate how they have exploited these inefficiencies by remaining nimble for sector allocation opportunities or acting quickly for security selection opportunities.

Be quick: Security selection in core fixed income

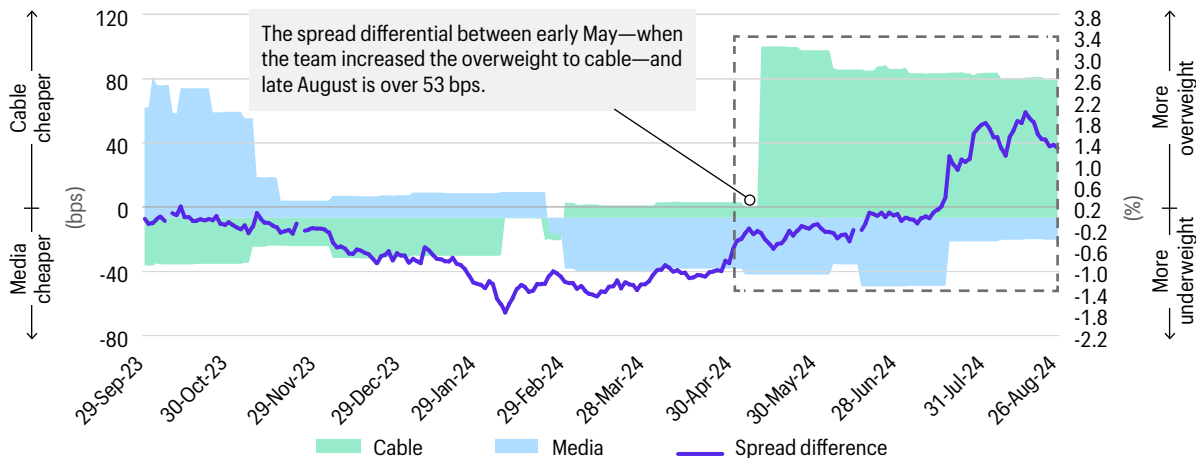
Technology, media, and telecommunications (TMT) bonds have fluctuated in valuation during 2024—offering opportunities for active security selection within these sectors.

Throughout the year, Allspring's Core Fixed Income team assessed the impact that secular changes to the TMT industry would have on various firms' business models and how increased competitive pressures were being reflected in rapid changes to relative value. The team identified bonds issued by two companies within the industry and saw an opportunity to move quickly to exploit these changes in valuation (Exhibit 1).

- The competitive landscape for communications and media companies has shifted quickly over recent quarters, affecting firms in different ways.
- Case in point, these two companies in similar industries have had different challenges and opportunities. An investor's ability to be nimble and exploit shifts in relative value can add meaningful performance.
- By actively rotating positions in these two companies, the Allspring Core Fixed Income team took advantage of market pressures and captured portfolio alpha without adding significant risk.

Featuring Allspring Investment Teams:
CORE FIXED INCOME TEAM
PLUS FIXED INCOME TEAM

EXHIBIT 1: RELATIVE VALUE FLUCTUATED BETWEEN TMT BONDS



Sources: Allspring and Bloomberg Finance L.P. Data as of 27-Aug-24. 100 basis points (bps) = 1.00%



Be nimble: Sector allocation in plus fixed income

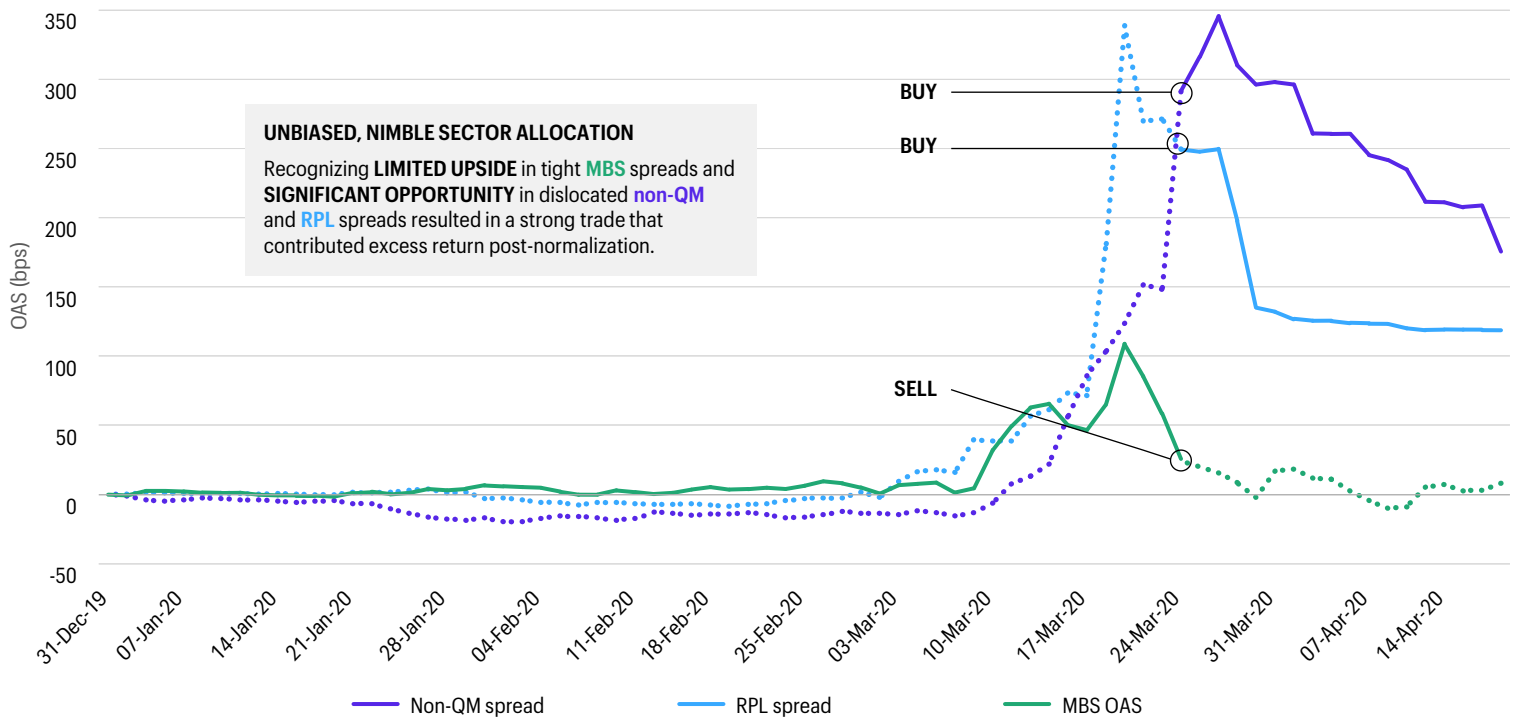
In March 2020, uncertainty over the impact of the COVID-19 pandemic shutdowns on prepayments and delinquencies for securitized assets weighed heavily on markets.

As a liquidity crisis unfolded and spreads increased across securitized sectors, the Allspring Plus Fixed Income team captured opportunities due to these idiosyncrasies in sector valuations (Exhibit 2).

- At the height of the pandemic, the U.S. Federal Reserve (Fed) announced it would support agency mortgage-backed securities (MBS)—which are created by government and quasi-government agencies—prompting the option-adjusted spread (OAS) of the U.S. MBS Index to tighten.

- At the same time, however, residential mortgage-backed securities (RMBS) received no direct Fed support, which added uncertainty on prepayments and delinquencies. The Plus Fixed Income team observed a compelling opportunity on securities with relatively low credit risk in the non-QM (non-qualifying mortgages) RMBS and reperforming loan RMBS sectors.
- Believing agency MBS had the least upside potential, the team trimmed agency MBS positions and added a diversified set of non-agency RMBS with additional spread. The RMBS positions contributed considerable excess return to the Plus team portfolios as spreads quickly normalized thereafter.

EXHIBIT 2: COVID-19 IMPACT ON SECURITIZED SPREADS



Sources: Allspring and J.P. Morgan. Non-QM 19 AAA 25 CPR Base (full extension), average life spread (static), RPL 19.AAA 10 CPR base average life spread (static), MBS OAS (SWP). As of 14-Apr-20.

The solid portion of each line represents the security's OAS when the security was held, and the dotted-line portion represents the security's OAS when it was not.

This was one of many opportunities the team exploited during early 2020 when relative valuations across global markets were changing rapidly. The pandemic, associated recovery, and historic global central bank policy actions taken since have caused market conditions to change dramatically over the past several years, providing additional opportunities. The Plus Fixed Income team believes employing an unbiased approach designed to take advantage of a wide array of opportunities wherever they arise is the optimal strategy for navigating dynamic markets and exploiting the inefficiencies found across the fixed income landscape.

Actively managing for opportunity

Shifting market fundamentals make it more challenging for bond investors to add value. Thorough credit research and rigorous risk management can help add significant alpha when markets fluctuate. As with Jack and the candlestick, the key is to be nimble and quick—to avoid getting burned by market volatility or opportunity cost.



For further information

We're committed to thoughtful investing, purposeful planning, and the desire to deliver outcomes that expand above and beyond financial gains.

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Contact details

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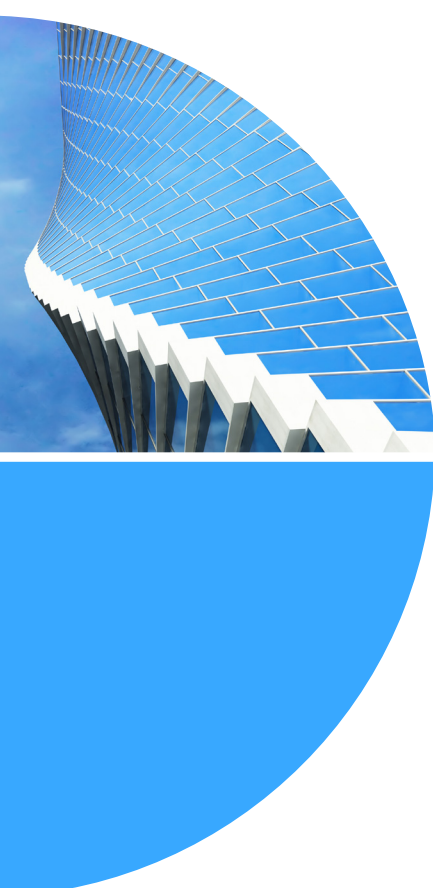
- To reach our U.S.-based intermediary sales professionals, contact your dedicated regional director, or call us at **+1-866-701-2575**.
- To reach our institutional investment professionals, contact your existing client regional director, or email us at **AllspringInstitutional@allspringglobal.com**.
- To reach our retirement professionals, contact your dedicated defined contribution investment only specialist, or call us at **+1-800-368-1370**.

FOR EMEA AND APAC INVESTORS ONLY

To reach our EMEA- and APAC-based investment professionals, contact us at **AllspringInternational@allspringglobal.com**.

FOR SUSTAINABLE INVESTING

To discuss sustainable investing solutions, contact **Henrietta Pacquement**, head of Sustainability, and **Jamie Newton**, deputy head of Sustainability, at **henrietta.pacquement@allspringglobal.com** and **jamie.newton@allspringglobal.com**.



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