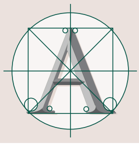


Artisan High Income Fund

QUARTERLY Commentary

Investor Class: ARTFX | Advisor Class: APDFX | Institutional Class: APHFX

As of 30 June 2022

Investment Process

We seek to invest in issuers with high-quality business models that have compelling risk-adjusted return characteristics. Our research process has four primary pillars:

Business Quality

We use a variety of sources to understand an issuer's business model resiliency. We analyze the general health of the industry in which an issuer operates, the issuer's competitive position, the dynamics of industry participants and the decision-making history of the issuer's management.

Financial Strength and Flexibility

We believe that analyzing the history and trend of free cash flow generation is critical to understanding an issuer's financial health. Our financial analysis also considers an issuer's capital structure, refinancing options, financial covenants, amortization schedules and overall financial transparency.

Downside Analysis

We believe that credit instruments by their nature have an asymmetric risk profile. The risk of loss is often greater than the potential for gain, particularly when looking at below investment grade issuers. We seek to manage this risk with what we believe to be conservative financial projections that account for industry position, competitive dynamics and positioning within the capital structure.

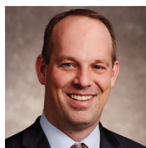
Value Identification

We use multiple metrics to determine the value of an investment opportunity. We look for credit improvement potential, relative value within an issuer's capital structure, catalysts for business improvement and potential value stemming from market or industry dislocations.

Team Overview

Our team brings together a group of experienced credit analysts who are dedicated to a single investment philosophy and process. All team members conduct deep fundamental credit research as generalists with sector tendencies to identify issuers with high quality business models that have compelling risk-adjusted return characteristics.

Portfolio Management



Bryan C. Krug, CFA
Portfolio Manager

Investment Results (%)

			Average Annual Total Returns				
As of 30 June 2022	QTD	YTD	1 Yr	3 Yr	5 Yr	10 Yr	Inception
Investor Class: ARTFX	**-9.46**	**-10.81**	**-9.64**	**2.91**	**3.78**	—	**5.00**
Advisor Class: APDFX	**-9.31**	**-10.72**	**-9.38**	**3.08**	**3.94**	—	**5.17**
Institutional Class: APHFX	**-9.39**	**-10.70**	**-9.41**	**3.14**	**4.03**	—	**5.14**
ICE BofA US High Yield Master II Index	-9.97	-14.04	-12.66	-0.04	1.95	—	3.14

Source: Artisan Partners/ICE BofA. Returns for periods less than one year are not annualized. Class inception: Investor (19 March 2014); Advisor (19 March 2014); Institutional (3 October 2016). For the period prior to inception, Institutional Class performance is the Investor Class's return for that period ("Linked Performance"). Linked Performance has not been restated to reflect expenses of the Institutional Class and the share class's returns during that period would be different if such expenses were reflected.

Expense Ratios	ARTFX	APDFX	APHFX
Semi-Annual Report 31 Mar 2022[1]	0.94	0.78	0.69
Prospectus 30 Sep 2021[2]	0.96	0.80	0.71

[1]Unaudited, annualized for the six-month period. [2]See prospectus for further details.

Past performance does not guarantee and is not a reliable indicator of future results. Investment returns and principal values 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 that shown. Call 800.344.1770 for current to most recent month-end performance. The performance information shown does not reflect the deduction of a 2% redemption fee on shares held by an investor for 90 days or less and, if reflected, the fee would reduce the performance quoted. Unlike the Index, the High Income Fund may hold loans and other security types. At times, this causes material differences in relative performance.

Performance Discussion

Our portfolio outpaced the ICE BofA US High Yield Index in Q2 to extend its lead over the benchmark to more than 300bps YTD. Similar to Q1, our asset allocation decisions had a significant impact on results. The portfolio's strategic allocation to leveraged loans—and resulting shorter-duration bias—helped buoy the portfolio throughout the quarter's volatility, materially outperforming the broader high yield market. Elsewhere, the portfolio's underweight to BBs in favor of lower-rated and idiosyncratic credit opportunities was a modest headwind during the quarter as higher-rated credit risk outperformed on slowing growth concerns. Offsetting this weakness was strong security selection across our CCC-rated holdings. Our lower-rated credits tend to be concentrated in less cyclical industries—particularly insurance and software—and materially outperformed similarly-rated risk. As we look ahead, we remain comfortable with the portfolio's positioning and believe we are well-positioned to navigate the wide range of outcomes that could unfold over the coming quarters.

Investing Environment

Credit markets concluded their worst first half year performance on record in Q2 as building concerns of a slowing economy led to widespread decompression. Credit assets were notably weaker across the board, but the rationale was distinctly different than in Q1. Through the first few months of the year, the drawdown across credit was primarily the function of a selloff in interest rates. But it was credit risk repricing that was the main contributor to high yield's 10% loss in Q2 (as measured by the ICE BofA US High Yield Index). The macro backdrop of tightening financial conditions, sequentially slowing growth and 40-year highs in inflation led to a quick erosion of risk appetites as investors priced in expectations for slowdown. Widespread risk aversion translated into materially wider credit valuations with spreads reaching their widest levels since the pandemic. Decompression was particularly acute among lower-rated and cyclical segments of the market, which all experienced notable underperformance on economic worries.

Leveraged loans, which have been largely immune from the year's volatility, succumbed to risk off price action but held up materially better than both investment grade and high yield bonds. Still, the 4.4% decline in loans in Q2 (as measured by the JPMorgan Leveraged Loan Index) marked the worst quarter of performance since Q1 2020. The weakening economic backdrop accelerated outflows across the loan space as investors' fixation with higher interest rates and surging inflation earlier in the year gave way to broader concerns about the economy later in the quarter. Despite weakness, loans remain one of the best performing segments across both equity and fixed income asset classes.

High yield valuations for the index finished the quarter with spreads just inside 600bps and yields near 9.0%. Even with fears of an impending recession, valuations still sit well inside prior periods of economic contraction. Nonetheless, growing pockets of stress/distress were evident across several capital structures and economically vulnerable industries. At the end of the quarter, nearly half of all CCC-rated bonds trade at distressed levels, implying investors have less confidence in lower-rated issuers' ability to withstand tighter financial conditions and slower growth. For many issuers needing access to capital markets, the difficult environment has required large concessions and significant discounts.

Defaults were only modestly higher from the cyclically low levels at the start of the year. The quarter saw 10 issuers default on $15 billion in bonds and loans, pushing the 12-month default rate 30bps higher to 0.76%. Even with growing distress, the number of bonds trading below $70 is largely in line with where it was pre-pandemic. Of course, defaults are likely to rise from current cyclical lows as markets become dislocated and as financial conditions tighten. Fortunately for investors, borrowers are in a much better position to weather a downturn than past cycles. The last two years of record refinancing have pushed out any near-term maturity wall that would increase the odds of refinancing-driven default activity. At the same time, high yield leverage is at pre-pandemic levels, and interest coverage is at post-crisis highs. This suggests we're unlikely to see a widespread default wave like previous downturns.

Portfolio Positioning

We took several steps throughout the quarter to take advantage of volatility and better position the portfolio for yield and total return. Continuing the trend from Q1, we reduced the portfolio's leveraged loan exposure into relative strength. We entered the year with nearly 40% of the portfolio in floating-rate assets, but trimmed that allocation to just 18% through quarter-end, in favor of deeply discounted bonds. This decision is based on our relative value views and the by-product of our bottom-up, research intensive security selection. While yields of bonds and loans were largely the same, the average high yield bond trades with dollar prices in the low 80s, compared to the average loans in the low 90s. This discount translates into positive convexity and an opportunity to capture returns well in excess of a bond's coupon once volatility stabilizes. It's also important to note, the return differential between bonds and loans has reached the largest margin on record when looking over rolling six-month periods. Most of loan outperformance this year has been a function of limited interest rate sensitivity, but with a meaningful degree of policy tightening already priced into the market, we expect duration to play a smaller role in driving relative performance going forward.

We also came into the quarter with a higher-than-average cash balance and a duration profile two years shorter than the benchmark. Amid volatility, we deployed some cash and swapped some of our shorter-dated exposure into what we believe are uniquely discounted and dislocated opportunities. As a result, our cash balance decreased to 6%, while our duration profile became incrementally longer at 3.3 years. Across sectors, the portfolio has become marginally more defensive. A third of the portfolio is now concentrated in the cable,

telecom and insurance sectors—areas that tend to have high business quality and show resiliency throughout an economic cycle.

The portfolio's top 10 holdings included two new issuers during the quarter: Virgin Media Secured Finance and Altice USA. Exiting the top 10 were Nordstrom Inc and Medline Industries. Our portfolio became incrementally more concentrated with our largest 10 issuers making up 30% of the portfolio, compared to 27% in Q1.

With Virgin Media, we added to existing unsecured exposure on weakness, viewing the company as a high quality, defensive business. Its recent tie up with O2 Limited creates one of the largest cable and telecom operators in the UK by bringing together Virgin Media's solid brand positions with O2's large market share in fixed and mobile services. From a credit perspective, the company has been aggressively investing in its broadband business, which remains a key catalyst to footprint expansion and growth. While cash flow generation has been predictable, overall free cash flow generation has been somewhat constrained due to higher investment related to the new-builds activity. Once the project is complete, Virgin Media should have substantial free cash flow to deleverage. Most of our exposure in Virgin Media is in high quality, BB-rated risk that now trades in the low 80s, resulting in high single-digit yields and attractive total return potential.

We also materially increased our investment in Altice USA's unsecured debt during the quarter. The company is one of the largest cable providers in the US with operations concentrated throughout the New York and South-Central US region. Its credit profile has seen some moderate deterioration as difficult cable and broadband subscriber trends have led management to begin a large multi-year investment cycle focused on broadband asset upgrades. The company is rolling out a fiber network that is expected to reignite subscriber growth and help it better compete with more aggressive peers. The capital spending plan will constrain the company's free cash flow generation and limit its ability to pay down debt in the near term, but it will position the company for healthier and more sustainable growth over the long term. Despite difficult near-term trends, we expect the company's capital structure to tighten materially as investment slows and as subscriber growth shows signs of improvement.

On the other side of the ledger, upscale retailer Nordstrom and health care products manufacturer Medline fell out of the portfolio's top issuers with underperformance. Despite continued progress with its turnaround, our longer-dated exposure in Nordstrom lagged with higher interest rates. It's a similar story for Medline. While the company's operations are largely recession-proof, our exposure's slightly longer duration profile and below average coupon make it more susceptible to changes in interest rates.

Perspective

As we move into the second half of the year, it's undeniable the credit landscape is dramatically different from the one at the start of the year. Soaring inflation and tightening financial conditions now characterize an environment where investors' recession outlook has moved from bear case to base case. While we don't think a recession is inevitable, we can confidently say credit fundamentals are in a much stronger place today to weather a downturn than past cycles. Fortunately for investors, a worsening macro picture has been met with a much better set of valuations. Dispersion is widespread, and pricing between industries and capital structures has become increasingly differentiated. In our view, this has created the most attractive opportunity set for credit selection we've seen since the depths of the pandemic. Of course, we acknowledge credit markets remain vulnerable to shifts in sentiment, and it's possible spreads could continue to widen from here. But for investors with a longer timeframe, current valuations have historically led to compelling forward returns. Ultimately, it's environments like these where the portfolio has built much of its lifetime excess returns. And we expect the continued uptick in dispersion to create attractive opportunities for credit selection and the potential for further outperformance.

ARTISAN CANVAS

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Carefully consider the Fund's investment objective, risks and charges and expenses. This and other important information is contained in the Fund's prospectus and summary prospectus, which can be obtained by calling 800.344.1770. Read carefully before investing.

Current and future portfolio holdings are subject to risk. The value of portfolio securities selected by the investment team may rise or fall in response to company, market, economic, political, regulatory or other news, at times greater than the market or benchmark index. Fixed income securities carry interest rate risk and credit risk for both the issuer and counterparty and investors may lose principal value. In general, when interest rates rise, fixed income values fall. High income securities (junk bonds) are speculative, experience greater price volatility and have a higher degree of credit and liquidity risk than bonds with a higher credit rating. The portfolio typically invests a significant portion of its assets in lower-rated high income securities (e.g., CCC). Loans carry risks including insolvency of the borrower, lending bank or other intermediary. Loans may be secured, unsecured, or not fully collateralized, trade infrequently, experience delayed settlement, and be subject to resale restrictions. Private placement and restricted securities may not be easily sold due to resale restrictions and are more difficult to value. The use of derivatives in a portfolio may create investment leverage and increase the likelihood of volatility and risk of loss in excess of the amount invested. International investments involve special risks, including currency fluctuation, lower liquidity, different accounting methods and economic and political systems, and higher transaction costs. These risks typically are greater in emerging markets.

ICE BofA US High Yield Master II Index measures the performance of below investment grade $US-denominated corporate bonds publicly issued in the US market. J.P. Morgan Leveraged Loan Index is designed to mirror the investable universe of the USD-denominated institutional leveraged loan market. The index(es) are unmanaged; include net reinvested dividends; do not reflect fees or expenses; and are not available for direct investment.

This summary represents the views of the portfolio managers as of 30 Jun 2022. Those views may change, and the Fund disclaims any obligation to advise investors of such changes. For the purpose of determining the Fund's holdings, securities of the same issuer are aggregated to determine the weight in the Fund. These holdings comprise the following percentages of the Fund's total net assets (including all classes of shares) as of 30 Jun 2022: Virgin Media Secured Finance PLC 2.7%, Altice USA Inc 2.4%; Medline Industries Inc 2.4%; Nordstrom Inc 2.3%. Securities named in the Commentary, but not listed here are not held in the Fund as of the date of this report. Portfolio holdings are subject to change without notice and are not intended as recommendations of individual securities. All information in this report, unless otherwise indicated, includes all classes of shares (except performance and expense ratio information) and is as of the date shown in the upper right hand corner. Portfolio statistics include accrued interest unless otherwise stated and may vary from the official books and records of the Fund. This material does not constitute investment advice.

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Credit Quality Ratings typically range from AAA (highest) to D (lowest) and are subject to change. The ratings apply to underlying holdings of the Portfolio and not the Portfolio itself. **Non-Investment Grade** refers to fixed income securities with lower credit quality. **Spread** is the difference in yield between two bonds of similar maturity but different credit quality. **Par-weighted Default Rate** represents the total dollar volume of defaulted securities compared to the total face amount of securities outstanding that could have defaulted. **Free Cash Flow** is a measure of financial performance calculated as operating cash flow minus capital expenditures. **Duration** estimates the sensitivity of underlying fixed income securities to changes in interest rates—the longer the duration, the greater the sensitivity to changes in interest rates. **Coupon** is the annual interest rate paid by a fixed income security, expressed as a percentage of the face value.

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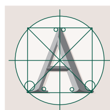
A R T I S A N  P A R T N E R S