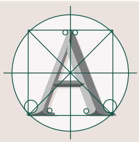


Artisan High Income Strategy

QUARTERLY
Commentary

As of 31 March 2019

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.

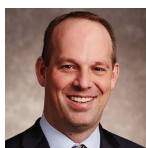
Value Identification

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 (%)

As of 31 March 2019	QTD	YTD	1 Yr	3 Yr	5 Yr	10 Yr	Inception[1]
			Average Annual Total Returns				
Composite — Gross	**6.74**	**6.74**	**5.36**	**9.95**	**7.11**	—	**7.11**
Composite — Net	**6.56**	**6.56**	**4.63**	**9.18**	**6.35**	—	**6.35**
ICE BofAML US High Yield Master II Index	7.40	7.40	5.94	8.69	4.69	—	4.69

Annual Returns (%) 12 months ended 31 March

	2015	2016	2017	2018	2019
Composite — Gross	**5.94**	**0.12**	**17.90**	**7.01**	**5.36**

Source: Artisan Partners/ICE BofA Merrill Lynch. Returns for periods less than one year are not annualized. [1]Composite inception: 1 April 2014.

Past performance does not guarantee and is not a reliable indicator of future results. Current performance may be lower or higher than the performance shown. Unlike the Index, the High Income Composite may hold loans and other security types. At times, this causes material differences in relative performance. Composite performance has been presented in both gross and net of investment management fees.

Investment Risks: Investments will rise and fall with market fluctuations and investor capital is at risk. Investors investing in strategies denominated in non-local currency should be aware of the risk of currency exchange fluctuations that may cause a loss of principal. These risks, among others, are further described on the last page, which should be read in conjunction with this material.

Performance Discussion

Our portfolio participated in the quarter's strong risk-on rally, providing notable absolute returns, but with gains that trailed the ICE BofAML US High Yield Index. Much of our relative underperformance can be attributed to our out-of-benchmark allocation to leveraged loans, which failed to keep pace during the quarter due to their lower-beta return profile. Additionally, the idiosyncratic credit-selection approach we employ is the primary reason for our substantial outperformance since inception but caused us to lag this quarter due in part to a few credit-specific situations in the energy and retail sectors.

April marks the five-year anniversary of the Artisan High Income Strategy, and we are pleased to have outperformed the ICE BofAML US High Yield Index and the eVestment US High Yield Fixed Income Universe. Since its launch on April 1, 2014, the Artisan High Income Strategy is among the best-performing strategies in its peer group, ranking in the 1st percentile out of 181 of its peers within the eVestment US High Yield Fixed Income Universe*.

Importantly, these returns have been generated with an emphasis toward capital protection. Over the last five years, our unwavering focus on risk-adjusted return potential has resulted in a consistently lower standard deviation than the ICE BofAML US High Yield Index. Having remained true to our investment process by creating a high-conviction, bottom-up portfolio, the portfolio has been able to deliver among the best risk-adjusted returns in its peer group based on Sharpe ratio. More notably, our portfolio has captured roughly 67% of drawdowns while participating in 95% of the market's upside, highlighting the team's objective of sidestepping negative credit events and avoiding permanent capital impairment.

Investing Environment

Credit markets rebounded sharply from Q4's sharp sell-off to clock in the strongest quarter of returns in almost a decade. Softening global growth conditions helped foster a more dovish Fed narrative that calmed investor anxieties, sending Treasury yields lower and risk markets higher. High yield bonds (as measured by the ICE BofAML US High Yield Index) were able to recover all of Q4's losses with returns of 7.4%. After touching multi-year wides to start the year, credit spreads rallied almost 150bps before finishing the period at 415bps. Credit spreads have recovered close to 60% of spread widening that has occurred since touching cyclical lows in October 2018.

Leveraged loans (as measured by the JPMorgan Leveraged Loan Index) also posted strong absolute returns, with gains of 3.9%. Despite the strong showing, loans lagged in relation to other high yield and high-grade segments. The Fed's dovish pivot resulted in resetting interest-rate expectations that limited the relative attractiveness of the asset class. As a result, loans have had to contend with 17 consecutive weeks of retail outflows, totaling more than $10 billion. Loan spreads contracted 85bps to finish the quarter at 474bps.

Despite the favorable backdrop for risk assets, there was a notable divergence between overall risk appetite and investors' willingness to reach for yield. Lower-rated segments logically outperformed higher-quality bonds, but the pace of outperformance was underwhelming in the context of high yield's significant recovery. At this point in the cycle, investors were more discerning of riskier, beta-driven credits. In all, BB-rated bonds returned 7.4%, slightly trailing CCC-rated returns of 7.9%. On a spread basis, BB spreads have recovered 75% of Q4 2018's spread widening, whereas CCCs have only recovered 40%.

Across sectors, the risk-on sentiment helped almost every sector finish materially higher. Energy credits led the market higher with returns of 8.4%—helped by a 30% rebound in oil prices—followed closely by consumer products (8.1%) and financials (8.0%). Among the laggards were transportation (2.8%), media (3.2%) and automotive (5.5%).

With the quarter's risk rally, the environment remains broadly supportive of credit fundamentals. Stressed situations in the market remain limited, with less than 2% of the index trading at a price below $70. Nonetheless, there was a small pickup in default activity in the quarter, with nine companies defaulting on a total of $9.3 billion in bonds and loans. Despite the increased volume, the high yield default rate fell below 1% to its lowest level in five years. The favorable environment is expected to continue throughout 2019 and into 2020.

Portfolio Positioning

The portfolio composition between bonds and loans was little changed from Q4 2018—though we used broad strength to make some incremental changes. As always, we look to attach ourselves to the part of the capital structure with the best risk-adjusted potential. As a result, our loan exposure increased incrementally to 22.5% from 20.4%, while our weighting in bonds decreased to 73.2% from 77.6%. From a sector perspective, the biggest changes were increased weightings in telecom and insurance and pared exposure in energy and industrials. With regard to portfolio distribution by credit ratings, we incrementally traded down the ratings spectrum with the broad strength at the higher-end of the credit spectrum, trimming our BB exposure while incrementally adding to CCC-rated risk and a few idiosyncratic opportunities in the IG market. Changes to the top-10 issuers included the addition of Acrisure, NFP Corp, Realogy and VEREIT. All were existing issuers in the portfolio.

The most notable new entrant to the top 10 is Realogy. The company enjoys a leading market position as the world's largest franchisor of residential real estate brokerages. While Realogy has been able to maintain its market share despite disruption from online brokerage solutions, it has seen its credit profile deteriorate over several years as management has levered the company's balance sheets to repurchase equity. More recently, a combination of concerns, including slowing home sales and rising home prices have weighed on the company's capital structure. The residential real estate brokerage market remains cyclical, but we believe there are several

*Source: Artisan Partners/ICE BofAML/eVestment Alliance. As of 31 Mar 2019. **Past performance does not guarantee and is not a reliable indicator of future results. Gross-of-fees performance shown for the Composite.** Current performance may be lower or higher than performance shown. Inception: 1 April 2014. Total return rankings—1-Yr: 63% out of 206 strategies; 3-Yr: 9% out of 194 strategies. Sharpe ratio rankings—1 Yr: 73% out of 206 strategies; 3-Yr: 15% out of 194 strategies; 5-Yr: 6% out of 181 strategies. The universe includes separate/segregated account monthly, gross-of-fees observations. eVestment is a manager-reported database of institutional investment managers and does not independently verify the data.

positive developments that have increased the relative value of Realogy's debt. At a macro level, the backdrop remains supportive as accommodative monetary conditions and low inventory levels should allow current sales trends to continue in the near term. More importantly, the company has pivoted to a more creditor-friendly financial policy, introducing covenants in its most recent debt offering that restrict the company's ability to buy back stock. As a result, we anticipate the company's credit trajectory will improve as free cash flow will be deployed toward debt repayment or strategic M&A. With leverage likely to decrease over the next 12-18 months, we believe our senior unsecured positions offer attractive total return potential.

Other new entrants include insurance brokers Acrisure and NFP Corp. We added to our position in Acrisure with the purchase of its discounted term loan. The company has been aggressively growing its market presence in the US insurance brokerage market through a well-developed acquisition strategy which allows for acquired entities to maintain their existing brands while providing operational autonomy by centralizing critical back-office functions. While leverage has risen in lockstep with its acquisition activity, the company has been able to generate significant organic growth to support its credit profile. Similarly, NFP enjoys a rising position in the employee-benefits marketplace–particularly among mid-sized companies. NFP has experienced strong growth, both organically and through acquisitions, in its property and casualty business and as it increases its efforts to leverage cross-selling opportunities. Recovery in its senior unsecured debt helped it move into the portfolio's top-10 issuers.

VEREIT is another long-time holding that made its way into the portfolio through appreciation as the issuer's higher-grade profile rallied with the help of falling interest rates. The company's credit story remains largely the same since we first meaningfully added the issuer to the portfolio in early 2015. Over the last few years, the company's credit profile has materially improved as management has aggressively deleveraged the balance sheet through strategic divestitures and a series of credit-positive transactions. As a result, the company was able to regain its investment-grade rating in 2017.

On the other side of the ledger, we used the quarter's strength to reallocate to more attractive relative value opportunities. Among issuers falling out of the top 10 was a roofing-materials distributor. After adding to our holdings in late 2018 on acquisition-integration risks and housing-related weakness, we exited a portion of our senior unsecured position based on valuation in Q1. Similarly, we trimmed our position in a Texas-based E&P after talks of an acquisition by a major oil and gas company pushed spreads inside 200bps, limiting our holding's relative value. We also trimmed our position in multi-brand retailer. The company's turnaround has experienced a setback despite positive momentum in its flagship banner and the market's constructive valuation view of its popular women's brand. Operational headwinds limit our position's near-term upside, though opportunity remains on a longer-term basis. Finally, we reduced our long-term holding in an American cable television provider based on valuation.

Perspective

We are proud of our progress over the last five years and believe our approach will be particularly appealing as we look at the investing environment ahead. As career investors in the high yield credit space, we recognize the risk of loss is often greater than the potential for gain—accordingly, we focus intently in our research on what can go wrong. We believe this commitment to downside analysis and margins of safety will serve us well as we enter into the latter stages of the current cycle. While the economic environment remains supportive for credit investors in the near term, swings in sentiment are likely as investors price in risks from decelerating global growth and uncertain monetary conditions. Against this backdrop, our disciplined underwriting process and ability to capitalize on market inefficiencies by way of individual security selection is increasingly critical, and we believe it should serve us well when the cycle turns. As always, we'll continue to manage the portfolio with an eye toward downside risks, believing this disciplined, high-conviction approach will be rewarded over our long-term investment horizon.

For more information: Visit www.artisanpartners.com

Investment Risks: 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. These risks, among others, are further described in Artisan Partners Form ADV, which is available upon request.

Unless otherwise indicated, the Artisan Strategy characteristics relate to that of an investment composite or a representative account managed within a composite. It is intended to provide a general illustration of the investment strategy and considerations used by Artisan Partners in managing that strategy. Individual accounts may differ, at times significantly, from the reference data shown due to varying account restrictions, fees and expenses, and since-inception time periods, among others. Where applicable, this information is supplemental to, and not to be construed with, a current or prospective client's investment account information.

Securities of the same issuer are aggregated to determine a holding's weight in the portfolio. Securities referenced may not represent all of the securities in the portfolio. The following holdings comprise the top 25 largest holdings as a percentage of the portfolios's total net assets as of 31 Mar 2019: General Electric Co 6.0%, Charter Communications Inc 5.2%, Vertafore 3.6%, Ferrellgas LP 2.9%, T-Mobile USA Inc 2.5%, Seven Generations Energy Ltd 2.2%, Acrisure LLC 2.2%, NFP Corp 2.2%, Realogy Group LLC 2.2%, VEREIT Inc 2.2%, Altice USA Inc 2.1%, AssuredPartners Inc 2.1%, TKC Holdings Inc 2.1%, HCA Inc 1.9%, Virgin Media 1.9%, Springleaf Finance Corp 1.8%, Sonic Automotive Inc 1.8%, Uniti Group LP 1.7%, USI Inc 1.7%, Ardonagh Midco 3 PLC 1.6%, Werner FinCo LP 1.6%, Tutor Perini Corp 1.6%, Endeavor Energy Resources LP 1.6%, Beacon Roofing Supply Inc 1.6%, Iron Mountain Inc 1.6%. All information in this report is as of the date shown in the upper right hand corner unless otherwise indicated and is subject to change without notice. Portfolio statistics include accrued interest unless otherwise stated. Totals may not sum due to rounding.

Attribution is used to evaluate the investment management decisions which affected the portfolio's performance when compared to a benchmark index. Attribution is not exact, but should be considered an approximation of the relative contribution of each of the factors considered.

Net-of-fees composite returns were calculated using the highest model investment advisory fees applicable to portfolios within the composite. Fees may be higher for certain pooled vehicles and the composite may include accounts with performance-based fees. All performance results are net of commissions and transaction costs, and have been presented gross and net of investment advisory fees. Dividend income is recorded net of foreign withholding taxes on ex-dividend date or as soon after the ex-dividend date as the information becomes available to Artisan Partners. Interest income is recorded on the accrual basis. Performance results for the Index include reinvested dividends and are presented net of foreign withholding taxes but, unlike the portfolio's returns, do not reflect the payment of sales commissions or other expenses incurred in the purchase or sale of the securities included in the indices.

ICE BofAML 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.

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This summary represents the views of the portfolio manager as of 31 Mar 2019. Those views and portfolio holdings are subject to change and Artisan Partners disclaims any obligation to advise investors of such changes. The discussion of portfolio holdings does not constitute a recommendation of any individual security.

Drawdown figures based on monthly returns of a representative account within the composite beginning April 2014 relative to the ICE BofAML US High Yield Index.

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.

Free Cash Flow is a measure of financial performance calculated as operating cash flow minus capital expenditures. **Spread** is the difference in yield between two bonds of similar maturity but different credit quality. **Three-year takeout** refers to the point at which a current loan is refinanced or otherwise paid off. **Beta** is a measure of the volatility of a security or a portfolio in comparison to the market as a whole. **Investment Grade** indicates above-average credit quality and lower default risk and is defined as a rating of BBB or higher by Standard and Poor's and Fitch rating services and Baa or higher by Moody's ratings service. **Margin of Safety**, a concept developed by Benjamin Graham, is the difference between the market price and the estimated intrinsic value of a business. A large margin of safety may help guard against permanent capital loss and improve the probability of capital appreciation. Margin of safety does not prevent market loss—all investments contain risk and may lose value. **Sharpe Ratio** is a measure of risk-adjusted return—it is the average return earned in excess of the risk-free rate per unit of volatility or total risk.

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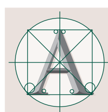
A R T I S A N  P A R T N E R S