

FLASH Memo

Subject: PGIM Global Bond Underperformance and PM Addition

Previous Status: Maintain

Current Status: Watch

Effective Date: August 2022

Overview

Prudential Global Investment Management ("PGIM") announced, effective July 14, 2022, Gregory Peters, Co-Chief Investment Officer ("CIO"), will be added to the Global Total Return strategy as a named portfolio manager. The current team complexion for the global bonds' suite is illustrated in the table below:

Fund Name	Portfolio Managers	Firm Experience	Strategy Experience
Global Dynamic Bond	Robert Tipp	31 yrs	19.8 yrs
Global Total Return	Matthew Angelucci	16.5 yrs	3.7 yrs
Global Total Return Hgd	Brett Bailey	15 yrs	0.8 yrs
International Bond	Gregory Peters	Joined in 2014	Added 7/14/22

PGIM's intent with the addition of Mr. Peters is to promote further dialogue and debate across the global multi-sector team. Mr. Peters can also veto decisions as the most senior member of the team. This team addition comes in wake of severe year-to-date ("YTD") underperformance, dragging trailing periods lower for the Global Total Return strategy, and is the only strategy that Mr. Peters will be added to.

As of 6/30/22	YTD	1 YR	3 YR	5 YR	10 YR
Bloomberg Global Aggregate TR USD	-13.91	-15.25	-3.22	-0.55	0.11
PGIM Global Total Return R6	-20.66	-22.09	-5.30	-0.95	1.40

There are two main drivers of underperformance YTD. The first is security selection within emerging markets, which accounts for -291 basis-points ("bps") of underperformance. This is mainly due to security selection in

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Russia and Ukraine going against the strategy due to geopolitical conflict. The second driver is duration positioning. Coming into the year, the portfolio was structurally long duration at 9.79 years versus the Bloomberg Global Aggregate index at 7.45 years. As of 6/30/22, the portfolio had an active duration position of +0.31 years relative to the index. Overall, duration positioning has cost the strategy -207bps or relative performance YTD.

Whenever strategies relatively underperform to large magnitudes, investment professional compensation is important context. For portfolio managers on the strategy, variable compensation is based on annual trailing 3-year performance relative to their alpha target of 250bps. PGIM estimates that variable compensation is 55-70% of portfolio manager total compensation. Investment professionals at PGIM also receive a Long-Term Incentive Plan ("LTIP") that is paid out based on an AUM weighted average of all portfolio composites meeting their individual alpha targets.

Recommendation

While investing with a long-term view is generally advisable, severe short-term underperformance should still be evaluated carefully. Within the context of the severe relative underperformance of the Global Total Return strategy, the addition of Greg Peters, CIO, gives us pause as it fundamentally changes the decision-making process for the team amid compensation in jeopardy. Because compensation is earned by trailing 3-year relative performance, underperformance YTD and in 2021 will be included in future trailing 3-year numbers. Further, Mr. Peters' seniority as CIO and intention of bringing more debate to the team may dilute the decision making of portfolio manager Robert Tipp, who has been leading the strategy for nearly 20 years. Considering their Russia/Ukraine positions are not able to be traded, and the relatively neutral current duration positioning, the portfolio will likely need to add risk to participate in more upside when the market rallies. However, the dynamic risk budget and ability to position the portfolio tactically are not a competitive advantage for the strategy. Thus, the efficacy of the strategy going forward is uncertain. For these reasons, the strategy is placed on Watch status.