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Active versus Passive Update: Active continues to outperform

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Two years ago, our in-depth study of Morningstar data on global fixed-income fund returns revealed that active global bond fund managers outperformed their passive counterparts after fees, as of 31 December 2020. We have updated this research with the latest data from the past decade (2014-2023), capturing recent inflationary trends. The results?

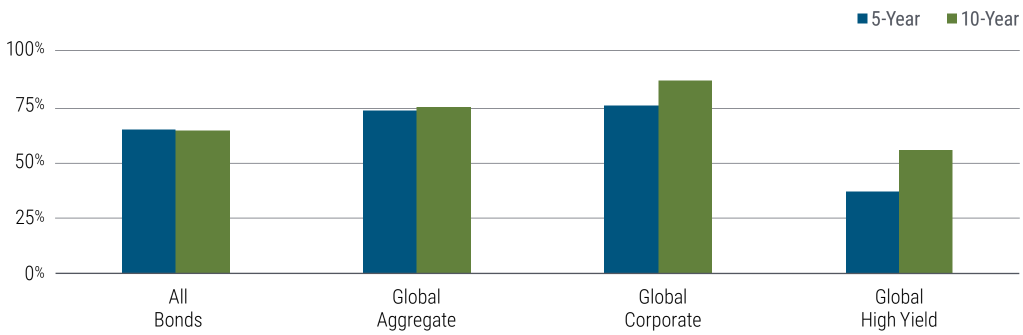
Active management still outperformed passive management.

Below, we drill down into our findings to see whether active bond managers have historically given investors an advantage over their passive peers.

ACTIVE OUTPERFORMS PASSIVE

The chart below reinforces our previous findings: over 60% of active global bond funds outside the U.S.[1] have outperformed their median passive counterparts, net of fees, over the long term. That is to say that, in the past decade, investors choosing active bond solutions had a better than 60% chance of outperforming passive alternatives. Notably, global aggregate and global (investment-grade) corporate managers excelled, with more than 75% of these funds outperforming their median passive peers[2].

Figure 1: Active global bonds continue to outperform their passive counterparts, net of fees



Past performance is not a guarantee or a reliable indicator of future results. Outperformance does not necessarily mean positive performance.

Chart shows percentage of funds that outperformed their median passive counterparts.

As of 31 December 2023; Source: Morningstar Direct, Bloomberg. Based on three Morningstar E.A.A Global Bond Fund categories (institutional shares and ETFs only): Global Bond, Global Corporate Bond, Global High Yield Bond. Global Bond category is divided into Global Aggregate and Global Treasury sub-categories according to benchmark characteristics. Funds without a prospectus benchmark or benchmarked to cash indices are excluded. NOTE: To address the issue of heterogeneous benchmarks within the same categories, we define more granular sub-categories according to benchmark characteristics and compare active and passive funds within each sub-category. **Refer to the important information at the end for additional Morningstar category and risk information.**

1 Funds are selected and grouped from the Morningstar database based on their prospectus benchmarks

2 In a case of multiple share class data for a given fund, the institutional share class with the lowest fee ratio was selected and thereafter the series with the longest history

There is no guarantee that the trends mentioned above will continue. Statements concerning financial market trends are based on current market conditions which will fluctuate.

The global high yield category, however, presents a unique challenge: active high yield funds in general benchmark against qualitatively different indices than passive funds, making direct comparisons unfair. That being the case, we have compared *excess* returns of active high yield funds against the corresponding median excess return of passive peers – both over their respective benchmarks. This approach neutralizes benchmark differences, revealing that median active high yield funds consistently outperformed their passive counterparts, on an excess return basis, across different time horizons.

A deeper dive into our global high yield analysis will be distributed in a forthcoming paper.

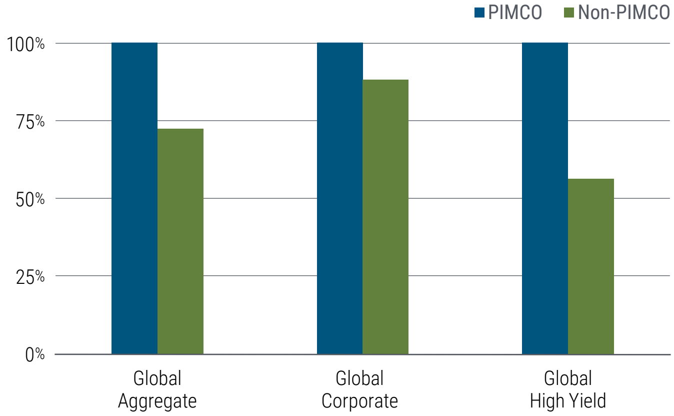
THE ACTIVE ADVANTAGE

The global fixed income market is diverse and complex, with several structural differences from the equity market. Unlike passive peers, whose primary goal is to track the benchmark, active fixed income managers have a large toolbox of strategies to fine-tune positions and express investment views to potentially outperform their respective benchmarks. Additionally, the market includes investors such as central banks and insurance companies, who must balance economic considerations with accounting, capital and other regulatory requirements. These factors combined, create a range of opportunities for skilled active managers to find value in global fixed income markets to potentially deliver returns that exceed any additional fees they may charge.

WHY PIMCO

In a constantly shifting investment landscape, partnering with a leader in fixed income investing can be highly beneficial for investors. With 100% of PIMCO funds having outperformed their Morningstar peer group categories over the past 10 years, we have far exceeded the average competitor success rate.

Figure 2: 100% of PIMCO funds outperformed passive medians over the last 10 years



Past performance does not predict future returns. Share value can go up as well as down and any capital invested in the Funds may be at risk. For more details on each fund's potential risks, please read the Key Investor Information Document/Key Information Document.

Source: Morningstar Direct, as of 31 December 2023.

For PIMCO Funds, the Global Aggregate category is represented by PIMCO GIS Global Bond, PIMCO GIS Global Bond Ex-US, and PIMCO Select Global Bond (liquidated in 2016), the Global Corporate category is represented by PIMCO GIS Global IG Credit and the Global High Yield category is represented by PIMCO GIS Global HY Bond. For non-PIMCO funds, please see list of qualifying Morningstar benchmarks in the appendix. We compare the PIMCO credit fund with the median passive corporate fund, given its lower risk and spread characteristics relative to the average corporate fund. We compare the PIMCO BB-B fund with the median passive all HY fund. **Refer to the important information section at the end for additional performance and fee, chart, index, GIS Funds and risk information.**

APPENDIX

For figures 1 and 2 – the qualifying Morningstar benchmarks are below:

Any base currency, hedged or unhedged

Global Aggregate	Global (IG) Credit	Global HY Bond
Bloomberg Global Aggregate Ex Securitized	Bloomberg Ag Cor (F40%)$/€/£1%$500M	Bloomberg Global HY xCMBS xEMG 2%Cap
Bloomberg Global Aggregate OECD	Bloomberg Global Aggregate Corp 0901	Bloomberg Global HY 2% Is Capped
Bloomberg Global Aggregate ex USD	Bloomberg Global Aggregate Corp 1229	Bloomberg Global High Yield
Bloomberg Global Aggregate	Bloomberg Global Aggregate Corp	BofAML High Yield Master II Const
Bloomberg Global Aggregated Fl Adj&Scal	FTSE WBIG Corp	ICE BofA Dv Mkts HY Constnd
	ICE BofA Global Corporate	ICE BofA Global HY Constrained
		ICE BofA NFincl Dv Mkt HY Constrained
		Markit iBoxx Global Dev Liq HY Cap

Any fund that had a prospectus benchmark in the above columns was categorised in accordance with the column header.

PLEASE ALSO NOTE:

1. Only funds with passive peers were included in the analysis.
2. Where a fund exists in several hedging and base currency combinations, we selected just one based on the following criteria:
    a. First, the one with the lowest fee.
    b. Second, (if two have the same fee level) the one with the longest history.
3. For the 10-year horizon analysis, we insist on a minimum of 12 months of historical data; for other horizons, even one observation is sufficient.

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CHART

Performance results for certain charts and graphs may be limited by date ranges specified on those charts and graphs; different time periods may produce different results.

CORRELATION

The correlation of various indices or securities against one another or against inflation is based upon data over a certain time period. These correlations may vary substantially in the future or over different time periods that can result in greater volatility.

INDEX

It is not possible to invest directly in an unmanaged index.

RISK

High-yield, lower-rated, securities involve greater risk than higher-rated securities; portfolios that invest in them may be subject to greater levels of credit and liquidity risk than portfolios that do not. Investing in the **bond market** is subject to risks, including market, interest rate, issuer, credit, inflation risk, and liquidity risk. The value of most bonds and bond strategies are impacted by changes in interest rates. Bonds and bond strategies with longer durations tend to be more sensitive and volatile than those with shorter durations; bond prices generally fall as interest rates rise, and low interest rate environments increase this risk. Reductions in bond counterparty capacity may contribute to decreased market liquidity and increased price volatility. Bond investments may be worth more or less than the original cost when redeemed. Investing in **foreign denominated and/or domiciled securities** may involve heightened risk due to currency fluctuations, and economic and political risks, which may be enhanced in emerging markets. **Mortgage and asset-backed securities** may be sensitive to changes in interest rates, subject to early repayment risk, and their value may fluctuate in response to the market's perception of issuer creditworthiness; while generally supported by some form of government or private guarantee there is no assurance that private guarantors will meet their obligations. **Equities** may decline in value due to both real and perceived general market, economic, and industry conditions. **Derivatives** may involve certain costs and risks such as liquidity, interest rate, market, credit, management and the risk that a position could not be closed when most advantageous. Investing in derivatives could lose more than the amount invested. **Diversification** does not insure against loss.

MORNINGSTAR

MORNINGSTAR CATEGORIES

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The Morningstar Global Aggregate category encompasses a broad range of fixed-income investments, including government, corporate, and securitized debt from various countries. This category is designed to provide investors with a comprehensive view of the global bond market, reflecting the performance of a diverse set of bonds across different sectors and regions.

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The Morningstar Global (IG) Credit category includes a diverse range of investment-grade credit securities, primarily focusing on corporate bonds and other fixed-income instruments that are rated investment grade by major credit rating agencies. This category aims to provide investors with exposure to high-quality credit markets across various sectors and regions.

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The Morningstar Global High Yield Bond category comprises a variety of high-yield fixed-income securities, primarily focusing on bonds issued by corporations with lower credit ratings. These bonds typically offer higher yields to compensate for the increased risk of default compared to investment-grade bonds. This category provides investors with exposure to the global high-yield bond market, which can be subject to significant price volatility and credit risk.

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