EATON VANCE

How Eaton Vance managers navigate volatile markets March 2020

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March 2020

Eaton Vance

EV Forward

How Eaton Vance managers navigate volatile markets

Summary

- The confluence of the coronavirus pandemic, an oil price war, Fed actions and US election-year politics has sparked a new level of volatility in global equity and fixed income markets, after a prolonged stretch of relative calm.
- Eaton Vance investment managers seek to actively capitalize on opportunities presented by volatile investor sentiment, while ensuring that the portfolio risk profile remains appropriate for the specific strategy.
- Eaton Vance strategies are designed to seek fundamental value that helps build client wealth over the course of many business cycles. In our view, times like these underscore the value of active management. We believe in carefully assessing the dynamics of fluctuations driven by political change or other disruptions, and in taking action that best serves the long-term interests of our clients.

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E|V|M
An Eaton Vance Company

Andrew Sveen
Co-Director of Floating-Rate Loans, Portfolio Manager

Floating-Rate Loans

- **What we are seeing:** Loan prices have corrected sharply, as the technical balance in the asset class has come under pressure. Accelerating retail fund redemptions and the overarching risk-off tone in capital markets are the culprit. Underneath, it's coronavirus, the "emergency Fed cut," plunging oil, and now more Fed cuts likely ahead. The situation is less about loans themselves, rather it's the exogenous macro picture that's weighing on technical conditions. This will all abate at some point but no one can say with confidence when nor at what level.
- **What we are doing:** We've been selling commensurate with our outflows and the market has proven to be liquid and orderly with good two-way flow. At the same time, we've seen prices gap lower. The S&P/LSTA Leveraged Loan Index lost 2.5 points on Monday alone, bringing the Index's average price down to 91.5. Forward returns from these levels have historically been among loans' very best – look at the snapbacks in 2012, 2016 and 2019 – but at times like these volatility can persist before things ultimately improve. Silver lining: While the market awaits better days, the current environment is serving as a great opportunity to optimize portfolios for risk and return.
- **What we are watching:** It's been good to see our funds' performance has held up well, though we're looking ahead much more than behind. We remain focused on our credits and our portfolio mix. Many investors seem worried about energy at present. Rest assured this is a small corner of the loan market (low single-digit percentages) and our portfolios have historically been positioned both underweight and tilted up in quality. More broadly – and much more importantly – a full-blown recession is now "priced in", with the current discount in today's market implying significantly worse credit losses than what was experienced during the global financial crisis. This suggests loans are in severely oversold territory.

Final word: Our best advice: If you are in, stay invested. If you can stomach it, add. Resist the urge to catch the bottom. If you have dry powder, consider putting a third of it in now. If loans dip further, you'll be glad you didn't jump feet first. If loans rally, at least you caught some of it. Meantime, loans offer a high income, a bond diversifier and one of the best values in fixed income today.

Floating Rate Loans– About Risk: The value of investments may increase or decrease in response to economic, and financial events (whether real, expected or perceived) in the US and global markets. Loans are traded in a private, unregulated inter-dealer or inter-bank resale market and are generally subject to contractual restrictions that must be satisfied before a loan can be bought or sold. These restrictions may impede the Strategy's ability to buy or sell loans (thus affecting their liquidity) and may negatively impact the transaction price. It may take longer than seven days for transactions in loans to settle. Due to the possibility of an extended loan settlement process, the strategy may hold cash, sell investments or temporarily borrow from banks or other lenders to meet short- term liquidity needs. Loans may be structured such that they are not securities under securities law, and in the event of fraud or misrepresentation by a borrower, lenders may not have the protection of the anti-fraud provisions of the federal securities laws. Loans are also subject to risks associated with other types of income investments. Investments in debt instruments may be affected by changes in the creditworthiness of the issuer and are subject to the risk of non- payment of principal and interest. The value of income securities also may decline because of real or perceived concerns about the issuer's ability to make principal and interest payments. Investments rated below investment grade (sometimes referred to as "junk") are typically subject to greater price volatility and illiquidity than higher rated investments. As interest rates rise, the value of certain income investments is likely to decline. Investments in foreign instruments or currencies can involve greater risk and volatility than US investments because of adverse market, economic, political, regulatory, geopolitical, currency exchange rates or other conditions. Changes in the value of investments entered for hedging purposes may not match those of the position being hedged.

Atlanta Capital

Joseph B. Hudepohl, CFA
Managing Director and Principal Atlanta Capital Management

- **What we are seeing:** Investors may have been looking for an excuse to sell after the S&P 500 in 2019 posted one of the top five strongest years since 1978 followed by the strongest Jan in 30 years; Coronavirus provided the spark pushing the S&P back to June 2019 levels. Low quality has led in the large cap growth market, however, if history is a guide, investors will seek high quality companies after the initial panic phase of selling liquid stocks.
- **What we are doing:** Although we have not taken any action based on the recent volatility, we are closely watching for opportunities to buy high quality companies. We have always focused on holdings with durable earnings growth, proven management teams, and the ability to succeed over the long-term by weathering any volatility.
- **What we are watching:** Each investment decision we make is based on individual company fundamentals. Therefore, we are stress testing current businesses we own as well as new ideas using prior crisis markets as a starting point for potential outcomes.

Final word: Over time and during markets like these, we remain confident our high-quality philosophy is the best approach. Sticking to our discipline provides the long-term benefits of equity investing if the markets move higher and protect if markets face continued volatility or declines.

Calvert International Equity

Christopher M. Dyer, CFA
Vice President, Director of Global Equity, Eaton Vance Advisers International Ltd.

- **What we are seeing:** Across all geographies of the international equity market we have seen broad-based, indiscriminate selling that has been driven by risk reduction at quantitative and leveraged funds. Coronavirus crisis has moved from a supply side crisis when it was concentrated in China to a demand side crisis as it has spread globally. Additionally, the collapse in the oil price will put incremental pressure on parts of the credit market and commodity / industrials space, at a time when the odds of recession had increased materially in Europe and Japan.
- **What we are doing:** We have been incrementally adding exposure to high quality business models that have sold off but we believe are positioned to be long-term winners (e.g. luxury goods).
- **What we are watching:** We are watching the rate of new infections across all geographies as this will be the ultimate determinant of when the market determines that the worst is behind us. We are also continuously identifying candidates that we believe are compounders with sustainable business models that we can potentially add to the portfolio following price weakness.

Final word: We believe that structuring strategies to provide protection in down markets and exposure to long-term compounders with sustainable business models is the best way to preserve and grow wealth.

Atlanta Capital – About Risk: The value of investments may increase or decrease in response to economic, and financial events (whether real, expected or perceived) in the US and global markets. The value of equity securities is sensitive to stock market volatility. Smaller companies are generally subject to greater price fluctuations, limited liquidity, higher transaction costs and higher investment risk than larger, more established companies. A non-diversified strategy may be subject to greater risk by investing in a smaller number of investments than a diversified fund. Investments in foreign instruments or currencies can involve greater risk and volatility than US investments because of adverse market, economic, political, regulatory, geopolitical, currency exchange rates or other conditions.

Calvert International Equity – About Risk: Investing primarily in responsible investments carries the risk that, under certain market conditions, the strategy may underperform funds that do not utilize a responsible investment strategy.

Aidan Farrell
Vice President,
Eaton Vance Global
Advisors Limited

International Small-Cap/Calvert International Opps

- **What we are seeing:** Headlines are laden with anxiety, "expert" opinions are hitting our smartphones and email inboxes by the minute. There are no comfortable hiding places across investment markets, and all are likely to be experiencing disruption for weeks/months to come. It all feels pretty awful, and in many ways it is. We have seen indiscriminate selling across risk assets broadly with less notable differentiation between higher and lower quality businesses.
- **What we are doing:** We are incrementally adding to positions where we feel near-terms concern have led share prices to valuation points that do not reflect the true medium-to-long-term franchise value of the business.
- **What we are watching:** We are closely watching the pace at which the Coronavirus is spreading in different parts of the world. Investors will likely be most sensitive to the rate of change in the number of cases. In our experience, holding good, quality companies, staying well diversified and taking minimal regional and sector risk has helped to limit our exposure to potential risks like the Coronavirus outbreak, which could force us to take quick counter measures. While the news flow is concerning and stock prices are violently reacting to the uncertainty, we believe it's important not to become distracted by this challenging time for investment markets.

Final word: In times of tumult we often like to emphasize our philosophy across the small-cap franchise. We remain true to our practice of analyzing the long-term business prospects of our investments through the lenses of quality, valuation and time (QVT). Q – The quality of the companies we invest in leave us well positioned to withstand volatile equity markets. V – Sharp downward price movements create short-term pain, but attractive valuation opportunities over a longer-term investment horizon. T – It's an interesting time to re-visit some quality companies which have been on our wish list having been previously considered too expensive.

International Small-Cap/Calvert International Opps – About Risk: The value of investments may increase or decrease in response to economic, and financial events (whether real, expected or perceived) in the US and global markets. The value of equity securities is sensitive to stock market volatility. Investments in foreign instruments or currencies can involve greater risk and volatility than US investments because of adverse market, economic, political, regulatory, geopolitical, currency exchange rates or other conditions. Investing primarily in responsible investments carries the risk that, under certain market conditions, the strategy may underperform strategies that do not utilize a responsible investment strategy.

Focused Value/Large-Cap Value

Edward J. Perkin, CFA
Vice President, Chief Equity Investment Officer Eaton Vance Management

Aaron Dunn, CFA
Co-Director of Value Equity

- **What we are seeing:** Cyclicals were taking the brunt of the selling pressure due to the nature of the virus and its impact on resource intensive economies around the globe. The Russell 1000 Value Index is underperforming The Russell 1000 Growth Index due to the higher mix of cyclical weightings. This has overwhelmed the defensive parts of the value benchmark such as REITs and utilities that have rallied in response to falling interest rates. We invest on a multi-year through-the-cycle basis. So, our team is focused on owning quality companies that are very inexpensive on a normalized earnings basis. We have continued this approach in response to the decline in equities.
- **What we are doing:** Our strategies entered the downturn with expectations that the portfolios were more defensive. The strategies have not been as defensive in the near-term as we might have expected because the market has not rewarded lower balance sheet leverage and better business models, rather it has been more focused on exposures to travel, etc. On that basis, we have owned some travel related stocks that were initially hit harder than one would have expected. We are constantly looking to create the best upside/downside capture across the strategy. Therefore, we are working on positioning around a number of opportunities given the amount of global stimulus we expect to be in the system once the virus and associated fears recede.
- **What we are watching:** We are focusing on the permutation of the Coronavirus in the US, its residual impact on the energy crisis and on employment. In addition, the markets waning faith in the Fed backstop is a key concern moving forward. As global stimulus is expected to be significant, markets should begin to favor stimulus beneficiaries, especially once the eventual peak of Coronavirus appears to be reached globally.

Final word: We continue to follow our investment process, focusing on a multi-year, through-the-cycle investment horizon. To that end, we continue to look for high quality, yet out of favor, companies that exhibit a strong balance sheet, value-add returns on capital, and strong free cash flow to compound value over time.

Focused Value/Large-Cap Value – About Risk: The value of investments may increase or decrease in response to economic, and financial events (whether real, expected or perceived) in the US and global markets. The value of equity securities is sensitive to stock market volatility. Investments in foreign instruments or currencies can involve greater risk and volatility than US investments because of adverse market, economic, political, regulatory, geopolitical, currency exchange rates or other conditions.

Michael D. McLean, CFA
Portfolio Manager, Eaton Vance Management

J. Griffith Noble, CFA
Portfolio Manager, Eaton Vance Management

Calvert Small Cap/US Small Cap

- **What we are seeing:** The Russell 2000 Index reached bear market territory today, falling more than 20% since February 20, and matching its 4Q18 decline. On the heaviest down days, we've seen huge correlation among small-caps, and less opportunity for high quality to outperform, though our downside protection has been strong through the total period.
- **What we are doing:** We eliminated a stock with significant business conference exposure at the onset of the outbreak in Italy. In addition, given the magnitude of the sell-off we are incrementally adding high quality beta as stocks hit our wish list prices, while trimming holdings that have held up extremely well.
- **What we are watching:** While shares of companies with direct exposure to the most extreme developments (travel, energy producers, banks) have understandably performed poorly, we are closely watching US economic indicators (jobless claims, ISM, etc.) and company comments to determine how widespread the impacts will be felt. Signs of further economic damage will limit our aggressiveness.

Final word: The current environment makes the case for active management in small cap, as blindly buying ETFs leaves clients with many highly levered and unprofitable companies most vulnerable to an economic shock like this. Our emphasis on downside protection and disciplined application of (Q)uality, (V)aluation, and (T)ime positions us for strong relative performance in challenging market environments.

Calvert Small Cap/US Small Cap – About Risk: The value of investments may increase or decrease in response to economic, and financial events (whether real, expected or perceived) in the US and global markets. The value of equity securities is sensitive to stock market volatility. Investments in foreign instruments or currencies can involve greater risk and volatility than US investments because of adverse market, economic, political, regulatory, geopolitical, currency exchange rates or other conditions. Investing primarily in responsible investments carries the risk that, under certain market conditions, the strategy may underperform strategies that do not utilize a responsible investment strategy.

Stephen C. Concannon, CFA
Co-Director High Yield Bonds Portfolio Manager

High Yield

- **What we are seeing:** High-yield energy opened up nearly 20% lower on Monday, according to the ICE BofAML US High Yield Index. The average energy issue ended the day with an average spread 330bps wider that where it began the day. This has had a significant impact on the broader high yield market, contributing to the impact of the Coronavirus. The average spread on the ICE BofAML US High Yield Index increased by more than 100bps over the course of the day. The high yield market is functioning in an orderly manner. In particularly higher volatility spaces, such as energy, issues are working through a period of price discovery, given the volatility in the underlying commodity. Issuers that are more exposed to the Coronavirus are also in a price discovery mode. However, bonds are trading across these spaces and across the high yield market broadly. We are seeing an orderly, if volatile, process of price discovery and risk transfer occur. It would appear that cash balances remain ample in the market and we are not seeing signs of forced selling or aggressive liquidations. We continue to see buy interest in higher quality bonds given the move in interest rates.
- **What we are doing:** We are being patient. Our strategies entered this downturn with a modestly conservative posture relative to the Index. It is not our intent to make significant changes to the Fund's risk positioning by rating segment or sector at this time.
- **What we are watching**: The Index closed last week trading with an average spread of 581 bps, just wide of the long-term average. Monday's move moved the average spread to 686bps. The spread of Coronavirus in the US is likely and the pace at which it spreads is important. We think this could provide a short-term headwind to economic growth. As a result we are moving cautiously in terms of adding risk in client portfolios.

Final word: We plan to maintain a slightly conservative positioning while taking advantage of market dislocation and identifying bonds that are trading at levels that we feel are out of synch with their underlying value.

High Yield - About Risk: The value of investments may increase or decrease in response to economic, and financial events (whether real, expected or perceived) in the US and global markets. Investments in debt instruments may be affected by changes in the creditworthiness of the issuer and are subject to the risk of non-payment of principal and interest. The value of income securities also may decline because of real or perceived concerns about the issuer's ability to make principal and interest payments. Investments rated below investment grade (sometimes referred to as "junk") are typically subject to greater price volatility and illiquidity than higher rated investments. As interest rates rise, the value of certain income investments is likely to decline.

Vishal Khanduja, CFA
Director of Investment Grade Fixed Income Portfolio Management & Trading

Calvert Short Duration

- **What we are seeing:** The past week has given us elements of both Q4 2018 and the middle of 2016. We have seen four years' worth of investment-grade corporate spread tightening wiped out in three days. As a result, we believe spreads are attractive again in short duration and value opportunities are increasing. Initially, travel and leisure companies were the ones aggressively bid down. While markets have continued to be orderly, we have seen more indiscriminate selling over the past two business days, which is likely a result of the push to meet redemptions.
- **What we are doing:** Heading into this year, we were underweight investment-grade corporates relative to the Bloomberg Barclays US Corporate Investment Grade Index, as we did not see value, particularly on the short end. Corporate balance sheets were in good shape but carried rich valuations. Now, those same balance sheets are offering more attractive spreads. We are looking to add to corporate names, but only after the dust settles.
- **What we are watching:** We are not extending Treasury duration and we are not taking energy bets. Every balance sheet – government, corporate and consumer – is more strained as a results of this event. However, relative to corporate and government balance sheets, the consumer remains the strongest. And consumer balance sheets could improve further as a result of lower energy costs and mortgage refinancings.

Final word: In the future, yields are going to have a higher percentage of the yield coming from the spread over Treasuries (because Treasury yields are so low and credit risk has increased). We believe this may be an excellent opportunity for investors to reduce duration risk and invest in flexible fixed-income products.

Calvert Short Duration – About Risk: The value of investments may increase or decrease in response to economic, and financial events (whether real, expected or perceived) in the US and global markets. As interest rates rise, the value of certain income investments is likely to decline. Investments in debt instruments may be affected by changes in the creditworthiness of the issuer and are subject to the risk of non-payment of principal and interest. The value of income securities also may decline because of real or perceived concerns about the issuer's ability to make principal and interest payments. Mortgage- and asset-backed securities are subject to credit, interest rate, prepayment and extension risk. US Treasury securities generally have a lower return than other obligations because of their higher credit quality and market liquidity. While certain US Government-sponsored agencies may be chartered or sponsored by acts of Congress, their securities are neither issued nor guaranteed by the US Treasury. Investments rated below investment grade (sometimes referred to as "junk") are typically subject to greater price volatility and illiquidity than higher rated investments. Investing primarily in responsible investments carries the risk that, under certain market conditions, they may underperform funds that do not utilize a responsible investment strategy.

Vishal Khanduja, CFA
Director of Investment Grade Fixed Income Portfolio Management & Trading

EV Core Plus

- **What we are seeing:** Risk assets, which are those not issued or guaranteed by the US Treasury, have sold off substantially and US Treasury duration has become the main driver to core bond strategies. The oil price shock earlier this week was an unexpected and unwelcome addition to already challenged credit market.
- **What we are doing:** We have an active, total return approach, and are continuing to evaluate credit opportunities in the face of increased volatility. Earlier during this volatile period, we moved out of some holdings that were specifically affected by the initial wave of the Coronavirus. We have been conservatively positioned from a risk perspective for quite a while, and our ample liquidity has given us the ability to add risk as we see opportunities, though we remain cautious.
- **What we are watching:** Areas of interest, even in this turbulence, include Credit Risk Transfer bonds, (CRTs), which are mortgage bonds that benefit from prepayments and lower rates. Additionally, we like idiosyncratic tech name risk since not all tech is contracting. We believe this is not a time to own broad market beta, but to be very selective in the credits you do own. Our focus is on deeply-researched individual corporate and securitized credits with strong businesses and improving stories.

Final word: With safe-haven US Treasuries dropping in yield, having some yield from core plus strategies in a close-to-zero interest rate environment will be important. Longer-term, once the economy recovers, who will want to hold a 30-Year US Treasury at 1.00% or less?

Core Plus – About Risk: The value of investments may increase or decrease in response to economic, and financial events (whether real, expected or perceived) in the US and global markets. As interest rates rise, the value of certain income investments is likely to decline. Investments in debt instruments may be affected by changes in the creditworthiness of the issuer and are subject to the risk of non-payment of principal and interest. The value of income securities also may decline because of real or perceived concerns about the issuer's ability to make principal and interest payments. Contractual restrictions may impede the Fund's ability to buy or sell loans and loans may be subject to an extended settlement process. Investments in foreign instruments or currencies can involve greater risk and volatility than US investments because of adverse market, economic, political, regulatory, geopolitical, currency exchange rates or other conditions. In emerging countries, these risks may be more significant. Convertible securities may react to changes in the value of the common stock into which they convert, and are thus subject to the risks of investing in equities, as well as, to the risks of investing in income securities. When interest rates rise, the value of preferred stocks will generally decline. Investments rated below investment grade (sometimes referred to as "junk") are typically subject to greater price volatility and illiquidity than higher rated investments.

Craig R. Brandon, CFA
Vice President, Co-Director of Municipal Investments, Eaton Vance Management

Jon Rocafort, CFA
Managing Director, SMA Portfolio Management

Municipals

- **What we are seeing:** While uncertainty around the Coronavirus has hit risk assets hard, the Bloomberg Barclays Municipal Bond Index continues to produce positive returns in this evolving environment. As US treasury yields have declined sharply, municipal yields have also declined, though less significantly, according to Bloomberg LLC. For example, on March 9, with the 10-year US Treasury 26 bps lower, the benchmark 10yr AAA muni yield declined 8 bps. As a result, on a muni-to-Treasury ratio basis, municipals appear undervalued across the curve.
- **What we are watching:** We are closely watching municipal retail flows as a 60-week positive inflow streak ended on March 4. If the market experiences large retail outflows, it may create technical pressure on municipal valuations and push municipal yields higher. In the high yield municipal space, we are seeing spread widening in some of the riskier names. However, broadly the market reaction has been limited. High yield municipal ETFs have seen some forced selling, but broadly the market remains in price discovery mode.
- **What we are doing:** Being patient and looking for attractive entry points. As mentioned above, since municipals are notoriously a retail-driven market, we see the prospect of municipal mutual fund outflows should appetite for risk assets return following an equity market correction. We are on watch for any investor rebalancing movement, and using any available cash balances to look for opportunities to put money to work.

Final word: As we witnessed during the previous five equity drawdowns since the financial crisis, munis have exhibited low-to-negative correlation to equity risk and equity-like risk in fixed income. Munis should continue to play the role as the ballast of a fixed-income allocation, should the spreading epidemic drag the world economy into the steepest slowdown since the credit crisis.

Municipals – About Risk: The value of investments may increase or decrease in response to economic, and financial events (whether real, expected or perceived) in the US and global markets. There generally is limited public information about municipal issuers. As interest rates rise, the value of certain income investments is likely to decline. Investments in debt instruments may be affected by changes in the creditworthiness of the issuer and are subject to the risk of non-payment of principal and interest. The value of income securities also may decline because of real or perceived concerns about the issuer's ability to make principal and interest payments. Investments rated below investment grade (sometimes referred to as "junk") are typically subject to greater price volatility and illiquidity than higher rated investments.

Eric Stein, CFA
Co-Director of Global Income

Michael A. Cirami, CFA
Co-Director of Global Income

Global Macro

- **What we are seeing:** No “risk” market is being spared around the world. The big fall in safe-haven bond yields was being mimicked in many other rates markets around the world as most investors are pricing in falling inflation on lower for longer oil prices and additional central bank easing. Fed funds futures were pricing in 0% by end of April! Foreign exchange (FX) was mixed, but most EM currencies were weaker vs. the USD while yen and euro are stronger on expectations that the Fed will cut aggressively. The broad credit markets, including corporates and sovereigns, were under a lot more stress than local emerging-markets debt markets. This is not a surprise to us, but oftentimes we hear concerns over the liquidity in local markets and today is further proof that they are, in fact, more liquid given the diverse nature of demand (local banks, insurance companies, central bank, etc). They were down, but generally not as much and trading with better liquidity. While pretty much all risk markets were getting hammered, oil exporters are getting hit worse than importers.
- **What we are doing:** Worth a reminder that Global Macro is a well-balanced strategy of longs and shorts and has been hanging in there reasonably well. That said, on the margin, we had generally already been reducing risk in some of our longs, adding some highly liquid / notably exposed shorts opportunistically, and raising some cash. This is something we’ve been doing over the past week or two as we felt market reaction to the Coronavirus would likely continue to get worse before it gets better.
- **What we are watching:** Market volatility typically equates to opportunity. While we remain cautious, there are a number of spots where attractive value is opening up and we’ll be looking to take advantage in an appropriate way for the global macro strategies.

Final word: We believe our Global Macro strategies are suited for this type of market. The flexibility to invest opportunistically both long and short provides us with the tools needed in this kind of market.

Global Macro - About Risk: The value of investments may increase or decrease in response to economic, and financial events (whether real, expected or perceived) in the US and global markets. The strategy employs an "absolute return" investment approach, benchmarking itself to an index of cash instruments and seeking to achieve returns that are largely independent of broad movements in stocks and bonds. Investments in foreign instruments or currencies can involve greater risk and volatility than US investments because of adverse market, economic, political, regulatory, geopolitical, currency exchange rates or other conditions. In emerging or frontier countries, these risks may be more significant. Investments in debt instruments may be affected by changes in the creditworthiness of the issuer and are subject to the risk of non-payment of principal and interest. The value of income securities also may decline because of real or perceived concerns about the issuer's ability to make principal and interest payments. Exposure to derivatives involves risks different from, or possibly greater than, the risks associated with investing directly in securities and other investments. As interest rates rise, the value of certain income investments is likely to decline. The value of commodities investments will generally be affected by overall market movements and factors specific to a particular industry or commodity, including weather, embargoes, tariffs, or health, political, international and regulatory developments..

Michael A. Cirami, CFA
Co-Director of Global Income

Emerging Markets Debt

- **What we are seeing:** Oil exporters were getting hit worse than importers, as you would imagine. Most EM currencies were weaker vs. the US dollar, with the Russian ruble not surprisingly amongst the worst performers (off ~9%) while some on the opposite end of the spectrum were off just a touch if anything, such as Ukrainian hryvnia, according to Bloomberg, LLC. Hard currency bonds were under a lot more stress than local EMD markets. This is not a surprise to us, but oftentimes we hear concerns specifically over the liquidity in local markets and today is further proof that they are, in fact, more liquid given the diverse nature of demand (local banks, insurance companies, central bank, etc).
- **What we are doing:** We had generally already been culling risk in a prudent fashion over the past week or two. Generally, we have been easing back on positions that are higher beta, highly liquid, and more exposed to the fallout from the collapse in oil prices / the Coronavirus.
- **What we are watching:** Market volatility typically equates to opportunity. While we remain cautious, there are a number of spots where attractive value is opening up and we'll be looking to take advantage.

Final word: It is nearly impossible to predict when this bout of market volatility will end, but it will. And what does seem clear to us is that on the back-end of this, given the huge leg down in core bond yields around the world and the dovish stance of the Fed that is likely to last well-beyond market stabilization, we believe EMD will be even more attractive to investors in search of yield and to take advantage of a flat-to-weaker USD environment.

Emerging Market Debt - About Risk: The value of investments may increase or decrease in response to economic, and financial events (whether real, expected or perceived) in the US and global markets. Investments in foreign instruments or currencies can involve greater risk and volatility than US investments because of adverse market, economic, political, regulatory, geopolitical, currency exchange rates or other conditions. In emerging or frontier countries, these risks may be more significant. Investments in debt instruments may be affected by changes in the creditworthiness of the issuer and are subject to the risk of non-payment of principal and interest. The value of income securities also may decline because of real or perceived concerns about the issuer's ability to make principal and interest payments. Exposure to derivatives involves risks different from, or possibly greater than, the risks associated with investing directly in securities and other investments. As interest rates rise, the value of certain income investments is likely to decline. The value of commodities investments will generally be affected by overall market movements and factors specific to a particular industry or commodity, including weather, embargoes, tariffs, or health, political, international and regulatory developments.

Eric Stein, CFA
Co-Director of Global Income

Andrew Szczurowski, CFA
Portfolio Manager, Eaton Vance Management

Short Duration Strategic Income

- **What we are seeing:** The big fall in safe-haven bond yields was being mimicked in many other rates markets around the world as most investors are pricing in falling inflation on lower for longer oil prices and addition central bank easing. Fed funds futures are pricing in 0% by end of April! Foreign currencies are mixed, but most EM currencies were weaker vs. the USD while yen and euro are stronger on expectations that the Fed will cut aggressively. The broad credit markets, including corporates and sovereigns, were under a lot more stress than local bond markets. This is not a surprise to us, but oftentimes we hear concerns over the liquidity in local markets and today is further proof that they are, in fact, more liquid given the diverse nature of demand (local banks, insurance companies, central bank, etc). While pretty much all risk markets were getting hammered, oil exporters / oil sensitive sectors are getting hit worse than importers.
- **What we are doing:** On the margin, we had generally already been reducing risk over the past week or two as we felt market reaction to the Coronavirus would likely continue to get worse before it gets better.
- **What we are watching:** Market volatility typically equates to opportunity. While we remain cautious, there are a number of spots where attractive value is opening up and we'll be looking to take advantage.

Final word: This is an important episode for managers to have the flexibility to invest opportunistically around the world. As investors come to realize the incredible lack of yield from low volatility / high quality sources, strategies with this global ability to seek more yield are likely to be especially appealing.

Short Duration Strategic Income - About Risk: The value of investments may increase or decrease in response to economic, and financial events (whether real, expected or perceived) in the US and global markets. The Fund invests in other underlying funds in a fund-of-funds structure. Investments in debt instruments may be affected by changes in the creditworthiness of the issuer and are subject to the risk of non-payment of principal and interest. The value of income securities also may decline because of real or perceived concerns about the issuer's ability to make principal and interest payments. Investments rated below investment grade (sometimes referred to as "junk") are typically subject to greater price volatility and illiquidity than higher rated investments. Loans are traded in a private, unregulated inter-dealer or inter-bank resale market and are generally subject to contractual restrictions that must be satisfied before a loan can be bought or sold.. Loans are also subject to risks associated with other types of income investments. As interest rates rise, the value of certain income investments is likely to decline. Mortgage- and asset-backed securities are subject to credit, interest rate, prepayment and extension risk. Investments in foreign instruments or currencies can involve greater risk and volatility than US investments because of adverse market, economic, political, regulatory, geopolitical, currency exchange rates or other conditions. In emerging countries, these risks may be more significant.

Andrew Szczurowski, CFA
Portfolio Manager, Eaton Vance Management

Short Duration Government Income

- **What we are seeing:** The sell-off in risk assets led to a flight-to-quality environment that we haven't seen in years – investors are finally rewarding Agency MBS for their government-guarantee! Prices on Agency MBS moved higher, but spreads were still significantly wider vs. history and are near the widest level since 2013 (triple digit government bond spread), according to Bloomberg, LLC. We think yields will "catch down" to US Treasuries over the next few weeks providing a tailwind to the Agency MBS market.
- **What we are doing:** In an effort to reduce prepayment risk, several months ago we began reducing the average price of our strategy by selling some higher-coupon, premium bonds We also began gradually reducing our floating-rate Agency MBS exposure.
- **What we are watching:** While risk markets have seen a pretty dramatic selloff the last few weeks, investment-grade corporate credit spreads are still trading well inside of early 2016 levels (forget 2008). We believe the economic disruption to come from the Coronavirus will be far greater than those of the early 2016 energy crisis, so there could be a lot more pain to come in investment-grade corporate spreads. We expect the global economic data to see a significant slowdown in the coming weeks/months and for the Fed to unsuccessfully try to calm markets by cutting the federal funds rate back towards the zero lower bound in the very near future. At that point they will be out of rate-cut ammo. We also expect the Fed to stop the $20 billion a month Agency MBS runoff as early as next week, which would be a substantial positive for Agency MBS spreads.

Final word: During periods of stress, this type of strategy can be very appealing to investors, and an attractive place to sit out the current volatility.

Short Duration Government Income - About Risk: The value of investments may increase or decrease in response to economic, and financial events (whether real, expected or perceived) in the US and global markets. Securities with longer durations tend to be more sensitive to interest rate changes than securities with shorter durations. As interest rates rise, the value of certain income investments is likely to decline. Mortgage- and asset-backed securities are subject to credit, interest rate, prepayment and extension risk. Investments in debt instruments may be affected by changes in the creditworthiness of the issuer and are subject to the risk of non-payment of principal and interest. The value of income securities also may decline because of real or perceived concerns about the issuer's ability to make principal and interest payments. US Treasury securities generally have a lower return than other obligations because of their higher credit quality and market liquidity. While certain US Government-sponsored agencies may be chartered or sponsored by acts of Congress, their securities are neither issued nor guaranteed by the US Treasury.

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Bloomberg Barclays Municipal Bond Index is an unmanaged index of municipal bonds traded in the US

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For further information, please contact:

Eaton Vance Management
Two International Place, Boston, MA 02110
800.836.2414 or 617.482.8260 | eatonvance.com

Eaton Vance Management (International) Limited
125 Old Broad Street, London, EC2N 1AR, United Kingdom
+44 (0)203.207.1900 | global.eatonvance.com