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Nominees for Fixed-Income Fund Manager of the Year

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The two big bond stories of 2016 were the sharp reversal in the path of bond yields midyear and an impressive rally in corporates. Against the backdrop of plunging oil prices, concerns about global growth, and Brexit, bond yields shifted down during the first part of 2016. By the third quarter, though, bond yields were edging upward, a trend that accelerated following the election. The Fed hiked rates by 25 basis points in mid-December, and most bond funds were in negative territory for the fourth quarter.

After a rough 2015 and tough start to 2016, meanwhile, credit rallied through much of the rest of the year, with particularly strong performance in energy-related names. Many funds that did poorly in 2015's rocky credit markets performed well in 2016 as risk paid off. The best-performing sector in 2016 was high-yield bonds, with the Bank of America High Yield Master II Index gaining 17.5% for the year, compared with a less than 3% gain for the Bloomberg Barclays U.S. Aggregate Bond Index.

The ebb and flow of the bond market caused some managers and funds to look great in one quarter and not so great the next quarter, highlighting the importance of sound strategy and a longer-term outlook. Although a strong showing in 2016 is an important criterion in selecting our nominees, we also want to recognize managers who have delivered superior long-term returns with sound strategies that continue to earn our analysts' confidence. As a result, all nominees have earned a Morningstar Analyst Rating of Bronze, Silver, or Gold, indicating that our analysts believe the funds will outperform their peers on a risk-adjusted basis over a full market cycle.

This year's nominees for Fixed-Income Fund Manager of the Year are as follows:

Mary Ellen Stanek and Team, Baird Core Plus Bond (BCOIX)
Baird Core Plus Bond's long-tenured team, led by Mary Ellen Stanek, implements a straightforward strategy that has produced strong absolute and risk-adjusted results over time, supporting its Morningstar Analyst Rating of Silver. The fund is managed with a duration that is kept in line with that of its Barclays U.S. Universal benchmark and does not use derivatives or foray into foreign currency. Ultimately, sector allocation decisions and security selection, particularly within the fund's credit holdings, are critical to success, and the team has delivered consistently. Moreover, without substantial allocations to high yield and emerging markets, this fund has kept pace with and often surpassed more-intrepid peers who have a wider variety of levers at their disposal. In 2016, an overweighting to credit and strong security selection, especially in financials, helped it to a 4.8% gain that edged out roughly 85% of its peers. Modest allocations to commercial mortgage-backed securities (5% as of December 2016) and out-of-benchmark nonagency residential mortgage-back securities (8% as of December 2016) also added to returns. That the fund has delivered strong results in a risk-conscious and consistent way, tested by bouts of market stress, makes it a compelling option for this year's top prize.

Fixed-Income Investment Policy Committee, Dodge & Cox Income (DODIX)
Dodge & Cox's seasoned eight-member investment policy committee has earned a nomination for Dodge & Cox Income's agility during 2016's alternatively risk-off/risk-on environment. The fund's 5.6% gain handily beat its Bloomberg Barclays Aggregate U.S. Bond benchmark's 2.7% gain and topped 94% of intermediate-term peers.

A credit-heavy (and concentrated) portfolio requires an experienced team delving deeply into the fundamentals of firms and their bonds. This team works off a three- to five-year investment horizon and has patience with a number of long-term themes, though its managers aren't afraid to make changes when valuations warrant. For example, the team added more than 7 percentage points to its corporate stake between mid-2015 and March 2016, a time when valuations largely dropped and spreads widened. After a quick rebound, the managers reduced corporates by 4 percentage points by September 2016. The

Investors should carefully consider investment objectives, risks, charges and expenses. This and other important information is contained in the fund prospectuses and summary prospectuses, which can be obtained from a financial professional and should be read carefully before investing.

fund's long-standing shorter duration stance also paid off as bond yields increased in the second half of the year. Over longer periods of time, this Gold-rated fund has also drummed up an impressive track record. Its 10-year trailing return through December beat 85% of the intermediate-term bond category, and it has also stood out on a volatility-adjusted basis.

Ford O'Neil and Team, Fidelity Total Bond (FTBFX)
The risk-on markets of 2016 proved a boon for Fidelity Total Bond, a core-plus strategy run by long-tenured manager Ford O'Neil and his team. A team-based approach employs expertise from across Fidelity's mortgage, municipal, and credit specialists, many who run well-rated funds in their own rights. Employing the fund's flexible mandate, O'Neil aggregates this broad information and translates it into positioning at a total portfolio level with an eye to risk management.

The process was firing on all cylinders last year, delivering performance that ranks fourth in the competitive intermediate-term bond category. Not only were sector allocation decisions strong--the fund had an underweighting to richly valued mortgages and an overweighting to credit with an emphasis on financials--but the team's security selection and positioning also added to returns. For example, emerging-markets exposures to Argentina, Brazil, and Venezuela were particularly additive. As oil prices dipped at the start of the year and spreads in lower-rated energy bonds widened, O'Neil and his team (who had an underweighting to energy prior that drop) added to pipeline names. That allocation aided returns as oil prices quickly bounced back. An advantageous allocation to longer-dated Treasury Inflation-Protected Securities in anticipation of inflation also played out well. While the fund's 5.9% return for calendar-year 2016 is a standout relative to peers, its team and process also deliver over longer trailing periods. Since O'Neil took the fund's helm in late 2004 through the end of 2016, the portfolio has generated 4.8% of annualized return and lands in the top quartile of the category.

Ray Kennedy, Mark Hudoff, Patrick Meegan, and Richard Mak, Hotchkis & Wiley High Yield (HWHIX)
In a year when credit risk paid off, Hotchkis & Wiley High Yield distinguished itself with strong security selection and an emphasis on small- and mid-cap issuers. High-yield veterans Ray Kennedy, Mark Hudoff, and their team run a fairly plain-vanilla portfolio, with an approach that's designed to be driven by security selection, rather than big shifts in credit quality or macro positioning. Their long-standing preference for higher-rated (B and BB) junk bonds could have tripped this fund up given that returns were generally stronger by orders of magnitude down the quality ladder--the lowest quality bonds outperformed higher-rated debt fairly significantly--but strong security selection fueled its returns. The fund's 16% gain last year topped 85% of its high-yield bond peers' and was driven largely by security selection, particularly in energy, autos, and capital goods. The fund's overweighting to energy names also added to returns as oil prices bottomed out in early 2016 and rebounded strongly through much of the rest of the year.

Long-term results for this Bronze-rated fund are also impressive, especially given its higher-quality tilt. The fund lands near the top decile of its high-yield bond peers over the trailing five-year period through December.

Michael Hasenstab and Sonal Desai, Templeton Global Bond (TGBAX), Templeton Global Total Return (TTRZX), **and Templeton Global Income** (GIM)
Michael Hasenstab and Sonal Desai earn a nomination for a strong 2016 and top-tier long-term returns for Templeton Global Bond, Templeton Global Total Return, and Templeton Global Income. The funds had a decidedly rough start to 2016, in part because of a short on the yen, which strengthened against the U.S. dollar, and a struggling position in Mexican sovereign debt. During the second half of the year, however, some longtime positions paid off. A long-standing view that inflation would pick up panned out as expectations for inflation started to rise in November, and the funds benefited from extremely short duration positioning (near zero) as rates rose in the second half of the year. Some currency positions also added to returns, including a bet on a strengthening dollar, played through a short position in the euro, which weakened against the dollar in the second half of 2016. Finally, Hasenstab built a midteens stake in Brazil's bonds and currency during the sell-off in the third quarter of 2015. Brazil was the top-performing emerging-markets country in 2016 with a very strong surge in the first half of the year.

Longer-term results remain strong here despite pockets of volatility over the years. Gold-rated Templeton Global Bond's trailing 10-year returns through December landed in the top percentile of its world-bond peers while Silver-rated Templeton Global Total Return bested 95% of peers over the trailing five years. (It does not have a 10-year track record.) Investors should note that these funds are not for the faint of heart, as concentrated and contrarian bets can take time to pay off. Hasenstab and Desai have proved their worth over time.