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Brazil's Strong Economy Make Its Bonds a Buy

Gregg Greenberg – 05/13/10

NEW YORK, NY (TheStreet) — Brazil's strong currency and stable economy make its government bonds good buys for foreign investors, says George Strickland, co-manager of the **Thornburg Strategic Income Fund** (TSIAX).

The \$188 million fund has returned 27% during the past year, better than 82% of its peers, according to **Morningstar** (MORN). U.S. corporate bonds make up 63% of the fund, while foreign corporate bonds account for 24%.

Welcome to *TheStreet's* Fund Manager Five Spot, where America's top mutual fund managers give their best stock picks and views on the market in a five-question format.

What is your view of the economy?

Strickland: The economy is coming back, but still has a long way to go. Housing is, for the most part, the land of the living dead. Commercial real estate is still in the midst of an extended downturn. Consumer spending is picking up a bit, but will not show much strength unless the economy starts producing 300,000 or more new jobs a month. Celebrations around turning merely positive are premature.

Corporations are sitting on mountains of cash and starting to spend some of it. That may turn out to be a bright spot. Exports are another area of relative brightness, and government spending is mixed as state and local governments cut while Washington writes checks. Overall, we should see positive growth this year and next, but nothing to write home about.

Do you have a favorite corporate bond issue?

Strickland: The entire corporate bond asset class has tightened dramatically. We saw a high of around 640 basis points option adjusted spread over U.S. Treasuries at the end of 2008, and now we are about at the average for the past 10 years of approximately 140 basis points. Getting 5% less compensation for risk is a massive market change, and one to which the market is still trying to adapt. Any particular bond that we were excited to own 12 months ago has moved in price such that it is no longer a "favorite", merely a good income producer in the context of the portfolio.

What is your favorite U.S. corporate bond sector?

Strickland: We still like good bond businesses with recurring cash flows, like utilities. There has been much less payment for risk there recently, but the nature of the business is terrific for meeting interest payments. On the other hand, many strategists were very excited about financials, particularly banks, at the beginning of 2010, mostly because of their wider-than-typical spreads. We're not sure that the market has a terrific memory, and the idea that these businesses suffered from cliff risk — the possibility that the business could suddenly fall off a cliff — is not being priced into spreads. With regulatory headwinds and now, with perhaps a criminal case against **Goldman Sachs** (GS), it seems like a place through which we should step carefully.

What about a favorite foreign bond? Do you have one of those?

Strickland: Brazil sovereign debt in local currency is pretty interesting. It pays at least 6% real yield after inflation. Credit metrics are very solid. Net debt to GDP is below 50% and the government typically runs a primary account surplus. They have over \$260 billion of U.S. dollar reserves, and export huge amounts of iron ore, coffee, sugar, ethanol, meat and soybeans. The economy is becoming more consumer-oriented and producing more finished goods.

Inflation has surged to over 5% recently, but the central bank has acted aggressively by raising (its overnight lending) rate 75 basis points and signaling that more tightening may be necessary. Brazil is one of the few places where you can get an attractive yield, good credit dynamics and have some confidence in the value of the currency.

What sector would you avoid?

Strickland: High-yield corporate bonds, particularly of highly levered low margin business such as airlines, steel companies, and homebuilders have probably overshot fair value. If the economy grows robustly over the next couple of years, they could generate enough cash flow to decrease leverage and survive through the next downturn, but if growth is anemic or non-existent, these businesses will have a hard time rolling over debt maturities. Basically we are trying to find places where risk and reward are skewed in our favor. But, with the tremendous gains of the past year in very low quality bonds, we are concerned that some adverse news or events could quickly make those investments unprofitable.

Thornburg Strategic Income Fund, Class A Shares (TSIAX)

Average Annual Total Returns as of 3/31/10

	1-Yr	Since Incep (12/19/2007)
Without sales charge	38.77%	7.74%
With sales charge	32.53%	5.59%
Blended Index*	15.73%	3.27%
Barclays U.S. Universal Bond Index	10.39%	5.86%

Thornburg Strategic Income Fund, class A, ranked in the top 17% of Morningstar's Multisector Bond Category, out of 251 funds, for the one-year period as of 4/30/2010. Ranking is based on total return without sales charge.

Performance data shown represents past performance and is no guarantee of future results. Investment return and principal value will fluctuate so shares, when redeemed, may be worth more or less than their original cost. Current performance may be lower or higher than quoted. For performance current to the most recent month end, visit thornburg.com. The maximum sales charge for the Fund's A shares is 4.50%. The total annual operating expense ratio for class A shares is 1.49%. Thornburg Investment Management and Thornburg Securities Corporation have contractually agreed to waive fees and reimburse expenses through at least February 1, 2011, so that actual expenses do not exceed 1.25%.

Investments in the Fund carry risks, including possible loss of principal. Bond funds have the same interest rate, inflation, and credit risks that are associated with the underlying bonds. The principal value of bonds will fluctuate relative to changes in interest rates, decreasing when interest rates rise. Unlike bonds, bond funds have ongoing fees and expenses. Funds invested in mortgage backed securities may bear additional risk. Investments in lower rated and unrated bonds may be more sensitive to default, downgrades, and market volatility; these investments may also be less liquid than higher rated bonds. Investments in structured finance arrangements and other types of derivatives are subject to the risks associated with the securities or other assets underlying the pool of securities including illiquidity and difficulty in valuation. Investments in equity securities are subject to additional risks, such as greater market fluctuations. Special risks may be associated with investments outside the United States, especially in emerging markets, including currency fluctuations, illiquidity and volatility. Investments in the Fund are not FDIC insured, nor are they deposits of or guaranteed by a bank or any other entity.

Before investing, carefully consider the Fund's investment goals, risks, charges, and expenses. For a prospectus containing this and other information, contact your financial advisor or visit thornburg.com. Read it carefully before investing.

The views expressed by George Strickland reflect his professional opinions and are subject to change. The sectors and securities mentioned are for illustration purposes only. Under no circumstances does the information contained within represent a recommendation to buy or sell any security.

Basis Point – A unit equal to 1/100th of 1%. 1% = 100 basis points (bps).

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The Barclays U.S. Universal Index represents the union of the U.S. Aggregate Index, U.S. Corporate High-Yield Index, Investment-Grade 144A Index, Eurodollar Index, U.S. Emerging Markets Index, and the non-ERISA eligible portion of the CMBS Index. The index covers USD-denominated, taxable bonds that are rated either investment-grade or below investment-grade.

*The Blended Index is composed of 80% Barclays Capital Aggregate Bond Index and 20% MSCI World Index. The Barclays Capital Aggregate Bond Index is composed of approximately 8,000 publicly traded bonds including U.S. government, mortgage-backed, corporate and Yankee bonds. The index is weighted by the market value of the bonds included in the index. The Morgan Stanley Capital International (MSCI) World Index is an unmanaged market-weighted index that consists of over 1,200 securities traded in 23 of the world's most developed countries. Securities are listed on exchanges in the U.S., Europe, Canada, Australia, New Zealand, and the Far East. The index is calculated with net dividends reinvested, in U.S. dollars.

The performance of any index is not indicative of the performance of any particular investment. Unless otherwise noted, index returns reflect the reinvestment of income dividends and capital gains, if any, but do not reflect fees, brokerage commissions or other expenses of investing. Investors may not make direct investments into any index.

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