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The Secrets of a Winning Bond Fund

By Debbie Carlson Jan. 28, 2020 8:00 am ET

Matt Brill is the lead portfolio manager for Invesco Core Plus Bond.
Photograph by Peyton Fulford

Matt Brill knows how bad bond markets can get.

In 2005 he started as a portfolio manager in ING's commercial mortgage-backed securities and investment-grade credit divisions. It was part of the insurer's structured credit group, which included asset-backed securities and collateralized loan obligations. That placed him at ground zero of the global financial crisis, which started in structured credit in 2007 before spreading in 2008.

"I joke that I'm 40 years old, but in terms of bond years, I'm probably 50," says Brill, who has an economics degree from Washington and Lee University.

The crisis also drilled into him that capital preservation is paramount. That don't-lose-money mindset shaped how Brill now actively manages the $4.5 billion Invesco Core Plus Bond fund (ticker: ACPSX).

In 2013, the Atlanta-based Brill—along with his former ING colleague and now co-manager Michael Hyman—joined Invesco. The two have worked together since 2005 and have a "seamless" interaction, Brill says. He's the day-to-day overseer, while Hyman takes a big-picture perspective.

The partnership has served the four-star, Morningstar-bronze medalist fund well. Core Plus Bond's 11.3% total return in 2019 bested 95% of its competitors and beat its benchmark, the Bloomberg Barclays U.S. Aggregate Bond Index. The fund has consistently outperformed its peers and index over the past three, five, and 10 years, too. The fund has an expense ratio of 0.75%—below average for its category—and an SEC yield of 2.39%. Its A shares carry a 4.25% load.

Brill seeks high-quality bonds across asset classes, working with Invesco's fixed income teams to identify opportunities and risks. He has a daily call with global macro teams and a weekly investment strategy team meeting. Twice a year, the teams gather with key investors. These sessions help build camaraderie, making it easier to ask questions and challenge one another, he says.

He uses a three-dimensional approach to picking bonds, considering credit, capital structure, and duration. When looking at credit, he's interested in the nuances of the bond, rather than simply picking a credit level. One holding that illustrates this approach is unsecured bonds from Delta Air Lines (DAL). Delta is a higher-quality credit because of its efforts to reach investment grade, such as cost-cutting and labor negotiation efforts, Brill says. Airlines are the second-largest industry in the fund, which also owns investment-grade secured bonds from American Airlines (AA). These securities are backed by individual planes, which can be sold if necessary.

The "plus" in the fund's name can come from numerous sources, with high-yield debt being the most obvious for additional returns. As much as 20% of the fund can be in high-yield bonds, but currently only 12.5% of its holdings are below investment grade. Brill errs on the side of quality, even for high-yield debt. His position in junk-rated Ford Motor Credit is one example. "We like that Ford has a lot of liquidity, with over $30 billion in cash. We liked the extra yield you get to buy Ford," he says. Most of the bonds mature in three years or less.

The fund is tilted heavily toward corporate bonds, at 44% of holdings, compared with a category average of 27.5%. It is the reason the fund performed so well in 2019, Brill says. (But it's also why the fund had a rough 2018, when its corporate exposure was at 55% and the fund's negative 2.7% return placed it in the bottom 1% of its category.)

The fund made a big push into triple-B corporates starting in the fourth quarter of 2018. At the time, the market was fretting about companies' debt-heavy balance sheets, sending equities prices sliding. But Brill saw an opportunity as several companies started to reduce debt to shore up their stocks. He knew his bet on higher-yielding corporates would work when the Federal Reserve pivoted away from raising interest rates in early 2019—but he didn't expect it to work that well. "It was never intended to be a home run," he says. "We were incentivized because the valuations were so attractive."

One such purchase was AT&T's 30-year bond at a 5.15% yield, a top-10 holding. Brill liked that executive compensation was tied to debt reduction and the telecom was aggressively discussing deleveraging. "We wanted to go and buy the longest possible bond in AT&T to participate in that deleveraging for a number of years," he says.

Invesco Core Plus Bond

	1-Yr	3-Yr	5-Yr
ACPSX	11.5%	4.8%	3.6%
Bloomberg Barclays U.S. Aggregate Bond Index	9.6	4.3	3.0

Top Industries	% Assets
Diversified Banks	7.0
Airlines	3.3
Thrifts and Mortgage Finance	3.3
Wireless Telecommunication Services	2.4
Oil and Gas Storage and Transportation	1.6
Integrated Telecommunication Services	1.5
Automobile Manufacturers	1.5
Electronic Components	1.2
Semiconductors	1.1
Biotechnology	1.1
Total	24.0

Note: Top industries as of Dec. 31. Returns through Jan. 24th; three- and five-year returns are annualized

Sources: Morningstar; Invesco; Bloomberg

According to Brill, people buy bond funds for certain characteristics, such as preservation of capital, income, and to protect from stock market risks. He tries to balance liquidity, credit risk, and duration—a bond's sensitivity to changes in interest rates—to achieve those ends.

The fund's effective duration is 5.98 years, which Brill says helps the fund be a hedge against equities. That means it should gain or lose 5.98% for every one percentage-point move in the opposite direction in yield. When he adds more credit risk to the portfolio, he adds duration to offset it during volatile times. Brill isn't afraid of duration, like some bond buyers. He believes inflation will stay low because of technological advances, and that an aging population will still want fixed income.

That's why Brill is comfortable owning certain long-maturity corporate bonds, such as 60-year investment-grade bonds from Corning (GLW), best-known for specialized glass. That's double the maturity of most long-dated bonds, making Corning's offer of bonds maturing in 2079 "uncharted territory," he says. It is hard to forecast whether companies will be around in five years, let alone 60, but Corning was founded in 1851, Brill says.

Part of what makes Corning and AT&T especially attractive is they are very liquid securities, Brill says, which means they should be easy to trade, even during times of market stress. That is a plus for Brill, who is always looking for opportunities to buy or sell—the fund has a 250% turnover rate. "Everyone focuses on maturity, but if I sell a bond today, it's matured in our portfolio as far as I'm concerned," he says.

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