September 2023 – MBS Mantra/ARAM Strategy Returns and newsletter

	% Net Return	% Gross Return	2023 YTD Net %	Trailing 1 year Net %	2022 YTD Net %	2021 YTD Net %
MBSM Aggregated SMAs	**-0.06%**	**+0.01%**	**+3.2%**	**+4.1%**	-3.8%	+10.0%
ARAM AGG+ Alpha - ETFs	**-0.16%**	**-0.12%**	**+7.1%**	**+8.5%**	-10.0%	-0.45%
BB Barc Agg	-2.59%		-1.0%	+0.5%	-13.0%	-1.8%
BB Barc MBS	-3.02%		-2.1%	0.0%	-11.7%	-1.0%
BB Barc HY	-1.18%		+5.9%	+10.3%	-11.2%	5.3%
S&P 500	-4.74%		+13.0%	+21.6%	-18.2%	28.7%

Sep 2023 MBS Income: +1.36%; Annualized: +17.2% (Aggregated SMAs @ month end marks)
YTD 2023 MBS Income: +10.2%, 15.5% annualized (current portfolio, excluding bonds no longer in portfolio)

Sep 2023 MBS Cashflow: +1.6% (~19% annualized rate, implying a short weighted average life/duration)
Sep 2023 MBS Loss rate: +0.05% (a negative loss rate is a gain from subsequent recoveries)

Hello:

You'll notice a new logo and summary line in the table above – **we are reintroducing our Systematic Portfolio of Fixed Income ETFs under our ARAM brand.** The Fact Sheet for the Baseline Model Portfolio is linked above. The next section has details.

MBS High Income Strategy commentary

Our MBS High Income Strategy returns were almost flat for the month, which is in sharp contrast with fixed income markets, which all sold off significantly. Once again, we are outperforming the AGG, MBB, HY and the S&P for the month. For the year, we have outperformed the MBB ETF by 5.8%!

The marks of our portfolio were not immune to the selloff in bond prices from the increase in yields, albeit less than the marks on MBB and AGG, a result of our shorter duration. However, the High MBS Income of our portfolio offset the price declines in our marks, with a slightly positive Aggregated Gross return. This outperformance is due to the fundamental nature of our strategy: the High Income of our MBS selections buffers price change, and results in positively skewed returns.

This month, the Income of the MBS portfolio was 1.76%, offsetting the negative price changes from marks, which were almost all lower (but less negative) than most bond market proxies, such as MBB and the AGG.

Between the rates volatility and summer doldrums, this month was relatively illiquid, with not much trading in Non-Agency MBS, and a light BWIC calendar.

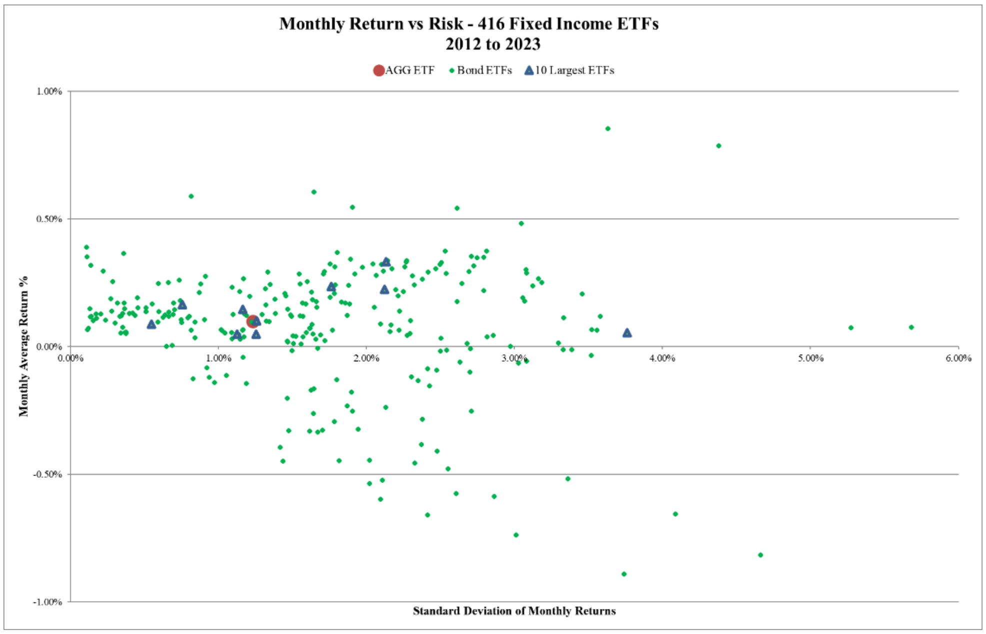
For the year to date, our Income is approximately +11.6% (~15% annualized). This has been offset by mark-price declines in our portfolios, especially for the fixed rate bonds, as rates have risen.

Agg Plus Alpha Systematic Portfolio of ETFs

(Re) Introducing Alpha Research and Management (ARAM's) ***AGG Plus Alpha Systematic Portfolio of ETFs***. Please email me or call if you'd like to see our deck that contains more details.

In 2014, after I founded MBS Mantra, and became a 'competitor' to my former clients, I was curious about their performance. **I discovered a complete inconsistency of risk and return between most of them, even when they purported to have the same benchmark and strategy, and realized that Fixed Income was ripe for optimizing – a portfolio of Fixed Income funds could outperform the benchmark AGG.**

Fixed Income Funds are not homogenous (even within the same sector):



In 2017, I created the AGG Plus Alpha Fund of Fixed Income Fund strategies that systematically identify the funds and weightings for the Model Portfolios. See the initial [Oct 2017 newsletter] for the initial strategy that used Fixed Income Mutual Funds.

I have continued to research and develop this product, incorporating Parameter Targeting to develop Model Portfolios, and using periodic rebalancing to systematically adjust the portfolios. With the reawakening of interest in Fixed Income, it is time to reintroduce this strategy. As ETFs have grown both in number and size, it is now possible to implement this strategy and technology using ETFs.

The parameters used to develop portfolios are: Risk, Liquidity, Diversification, and Sector limitations.

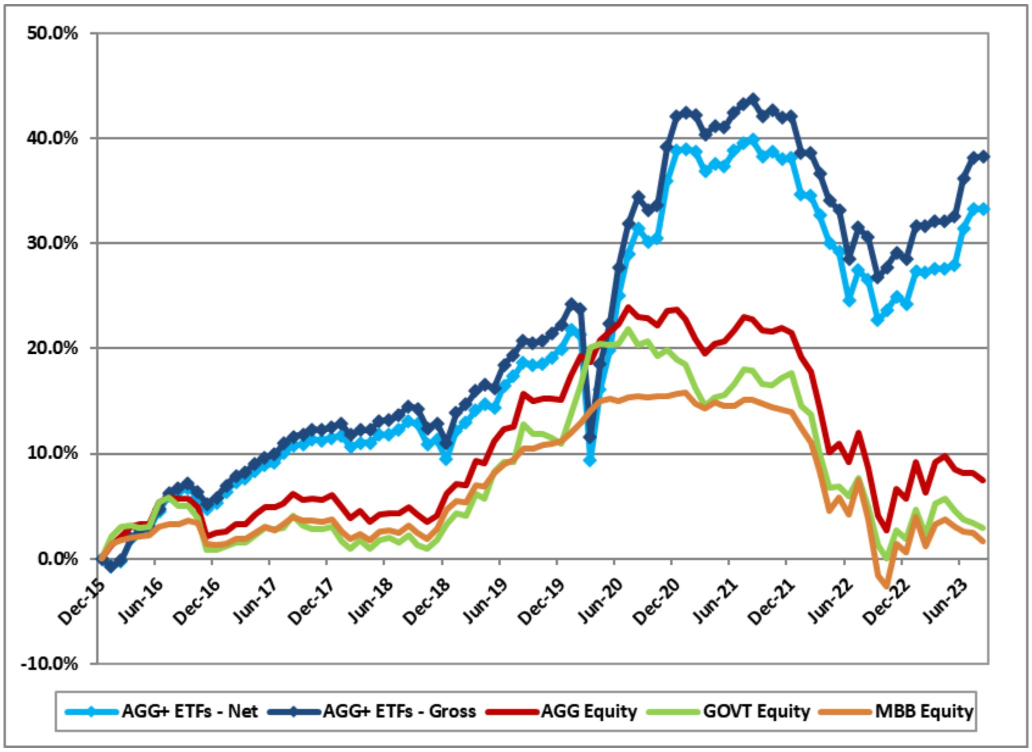
Much research went into rebalancing process to understand the amount of data it took for the system to identify regime changes in Fixed Income. We have developed a collection of model portfolios (>30) to satisfy the risk and liquidity constraints and requirements of potential investors of all sizes. We can customize a portfolio for any investor type.

Our systematic rebalancing process adjusts fund selections and weights (and by implication, sectors) dynamically, creating significant outperformance over the AGG, or any other benchmark.

Our Baseline Model portfolio is a moderate risk portfolio that uses up to 10 ETFs with limits on weights.

This strategy is a superior way to invest in Fixed Income for all investor types, especially compared to the typical investor that treats fixed income as an insurance product instead of as a source of returns, and invests in one Fixed Income fund or manager, or an institutional allocator that might have a portfolio of managers but does not rebalance in response to market and environment changes.

<u>Baseline Model Portfolio Cumulative Returns and Annual Returns (since 2016):</u>

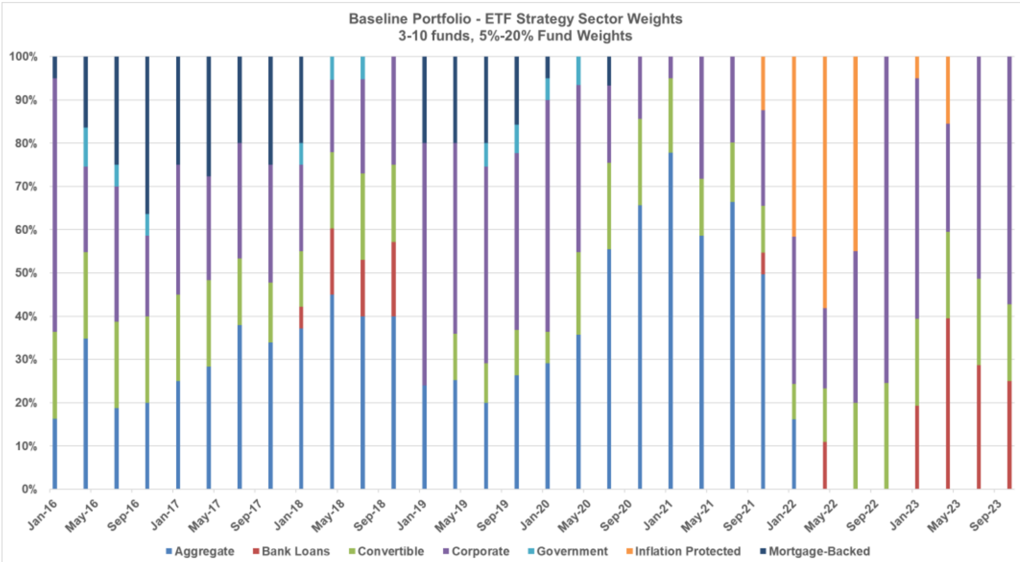


	AGG+α ETFs	AGG	Diff
2023	7.1%	-1.3%	8.4%
2022	-10.0%	-13.4%	3.4%
2021	-0.5%	-1.1%	0.6%
2020	15.7%	7.3%	8.4%
2019	9.6%	7.4%	2.3%
2018	-1.8%	0.3%	-2.1%
2017	5.9%	2.2%	3.7%
2016	5.3%	0.8%	4.4%

One of the key results is more months with positive returns (2016-present): 67% for the model portfolio versus 53% for the AGG, 48% for GOVT, and 56% for MBB.

Note that portfolio construction and re-balancing are only done with historical returns data (starting in 2012), rebalancing's are assumed to happen at month end using closing prices, and returns for the model portfolios from 2016 onwards are all 'out-of-sample' for the following period, until the portfolio is rebalanced again. Real returns might differ due to slippage during rebalancing, which only happens on a few days in the year.

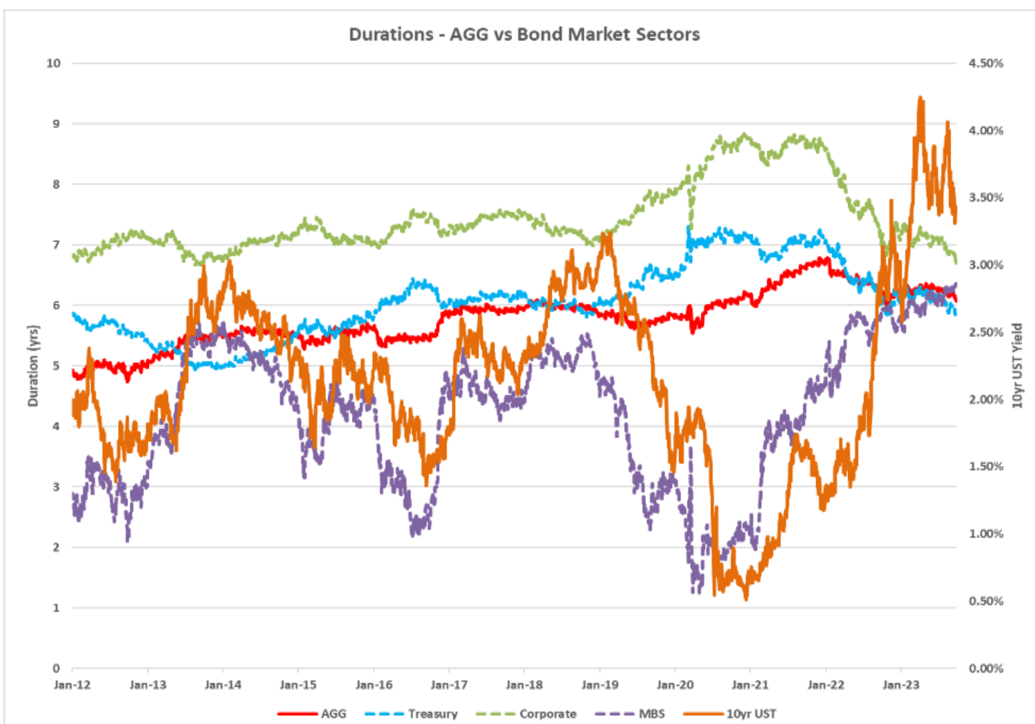
Rebalancing captures Rate and Risk Regime Changes and adjusts portfolio weights:



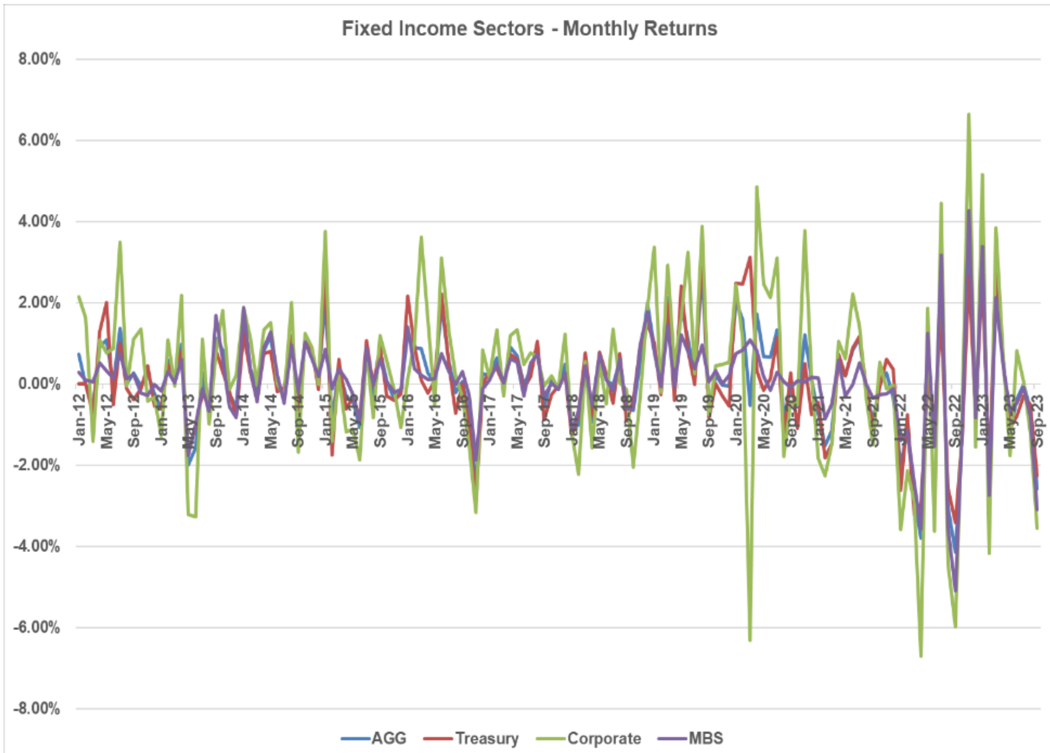
Note: there are multiple funds in each sector in each period. Over the course of the history above, approximately 50 ETFs, out of over 400 currently tracked and analyzed, have been used, varying depending on the Model parameters.

Also note: no AI was used in creating this strategy, just normal finance- and statistics-trained human intelligence. I'll incorporate AI when I am ready to sell MBS Mantra. 😊

Bond Sector Durations are not stable and change with rate regimes:



Income might be Fixed, but Total Returns including Yield/Dividends are not:



Our Agg Plus Alpha Systematic portfolios that recognize regime changes systematically and rebalance the portfolio are the solution for Fixed Income investors.

Please contact me for more information.

Regards, Samir Shah

October 10, 2023

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