FIRST EAGLE
INVESTMENT MANAGEMENT

Commentary March 31, 2020

First Eagle High Income Fund

Market Overview

The emergence of the novel coronavirus and the economic impact of efforts to contain its transmission led to a deep, sharp repricing of risk assets during the first quarter as liquidity concerns emerged across financial markets. The Bloomberg Barclays US Corporate High Yield Index fell nearly 13% during the period;[1] though lower-quality issues suffered the most, the dispersion of performance among credit tiers wasn't as significant as one might expect given the magnitude of the selloff. While the quarter as a whole was bad for high yield bonds, March was historically so, even if a late-month rally took out some of the sting. Driven by five of the six worst single-day moves ever, high yield spreads widened 670 basis points over the first three weeks of March, eclipsing the monthly record of 500 established in October 2008. The market was down 21% for the month at one point, worse than the 2008 record of 17%.[2]

Financial markets appeared to grow squeamish in late February and by March the impulse to de-risk had accelerated across asset classes. In the past, banks and brokerage houses typically acted as countercyclical shock absorbers for bond markets during periods of volatility, taking on risk when investors declined to do so; post-financial crisis regulatory capital requirements have limited their ability and/or willingness to fill this role, however. The absence of banks and brokers was particularly noticeable in the bond Exchange-Traded Fund (ETF) market, where these intermediaries essentially manage the arbitrage between the net asset value of an ETF portfolio and the underlying value of the individual bonds it holds. Their withdrawal during this most recent period of heightened volatility had all but collapsed the ETF market by the third week of March before the Federal Reserve stepped in to provide liquidity.

We believe we are likely in the early stages of the end of the credit cycle; purging the market of the significant excesses built up in recent years—most prominently in the investment grade bond and leveraged loan markets—should take some time to play out, as investors' reach for yield in recent years resulted in a corporate debt market characterized by lower credit quality, higher leverage and weaker investor protections even as spreads remained tight. While backward-looking default rates remain fairly benign, the forward-looking distress ratio suggests to us that much higher default rates lie ahead as credit issues bloom throughout 2020.

In a typical credit cycle, a gradually slowing economy impairs cash flow generation, which translates into deteriorating credit metrics, rising leverage levels and increased defaults for issuers and ultimately liquidity concerns for lenders. While the current cycle began with a liquidity issue rather than a gradually slowing economy, it seems more than likely the end result will be the same from the perspective of the bond market participants: higher credit costs, greater corporate distress and higher defaults.

Meanwhile, we think recovery values are likely to be a lot lower than historical norms. Gross leverage, which typically creeps higher toward the end of a recessionary period as cash flows decline, is elevated across the corporate credit complex at what appears to be the beginning of a recession, leaving borrowers in a more precarious position. We expect to see a lot of restructuring activity, some of which was likely necessary but deferred in 2009–10 as the Federal Reserve flooded the market with liquidity.

The prospect of a large volume of "fallen angels" remains both a concern and a potential opportunity for investors. March alone saw more than $90 million of fallen angels,[3] as ratings agencies have been quick to react to the current crisis after their experience in 2008, but we think there could be much more to come. As we've noted before, BBB rated bonds currently comprise a historically oversized share of the investment grade market, and we'd estimate that around one-third of these issuers have a metric in their credit profile more consistent with that of a high yield issuer. As the economic backdrop weakens and begins to challenge corporate cash flows, the equity cushion for many of these highly leveraged BBB issuers will likely erode. We wouldn't be surprised if 10%–15% of BBB issuers are downgraded to high yield through the current cyclical downturn, an enormous volume of bonds for the market to absorb, especially since many of these fallen angels will have longer durations than the typical high yield

1. Source: FactSet.
2. Source: Credit Suisse.
3. Source: Bloomberg.

First Eagle High Income Fund was known as the First Eagle High Yield Fund prior to March 1, 2020.

investor is accustomed to. This structural mismatch may provide opportunities to acquire the debt of attractive issuers at attractive prices, even after the Fed's early April announcement that it would buy bonds of fallen angels under the condition that they had maintained an investment grade rating as of March 22 and were downgraded to no lower than BB- reduces the likelihood of a broad market dislocation and repricing resulting from the high yield market's inability to absorb the cascade of fallen angels.

As there were in 2008 with the end of the previous cycle, there may be false dawns in the current crisis. The rally in late March, which has extended into early April, may be an example of positivity returning to the market before it is truly warranted. The bottom line, however, is that significant excesses developed over the course of the credit cycle, and these excesses will need to be purged.

We have long thought it better to prepare for a market turn early than late. We entered 2020 with the Fund's portfolio primed for defense—perhaps more so than at any other point in our history—with an emphasis on higher credit quality and short duration. We intend to remain up in quality and to keep plenty of "dry powder," which will enable us to be a liquidity provider to a dysfunctional secondary market and a goal of being an opportunistic buyer of fallen angel paper, while remaining positioned to potentially take advantage of the significant credit deterioration we believe lies ahead.

Portfolio Review

The High Income Fund A Shares (without sales charge*) posted a return of –12.11% in first quarter 2020. All market sectors detracted from performance in what was a very challenging period for risk assets. The Fund's holdings in cash and cash equivalents had a slight positive impact on return, however. The High Income Fund outperformed the Bloomberg Barclays US Corporate High Yield Index in the period.

The quarter's top contributors were HCA, Inc. 5.3875% due 05/01/2023; Southeastern Grocers Inc. common stock USD; Diamond 1 Finance Corp 7.125% due 06/15/2024; HCA Healthcare, Inc. 6.25% due 02/15/2021; and Open Text Corporation 5.625% due 01/15/2023.

The largest for-profit acute care hospital system in the US by revenues, HCA is a high-quality company, in our view. During the quarter, the company announced plans to issue new debt for the purpose of redeeming its 2021 paper. The short tenor of this particular bond issue also appeared to help buoy it in a difficult market, as longer HCA paper was much more volatile during the period.

The common stock of Southeastern Grocers, which owns supermarket chains in the U.S. region for which it is named, entered the Fund's portfolio pursuant to a corporate restructuring. Because it rarely trades, the stock's price tends to swing up and down in response to the valuations of its peers, and supermarket-related stocks held up fairly well relative to the broader equity market. In our view, the company has performed well since emerging from bankruptcy—having shrunk its store base, increased its margins and hit its earnings guidance from quarter to quarter.

Diamond 1 Finance was formed by Dell to facilitate its acquisition of EMC Corporation in 2016. Its issue maturing in 2024, like much of the high yield universe, was quite volatile during the quarter, gaining sharply toward the end of the month as investor risk appetites reawakened.

Canada's OpenText is among the leaders in the enterprise information management space. In February it issued $1.8 billion in senior secured notes, the proceeds of which will go to refinancing its outstanding debt, including the redemption of the 2023 bonds we own.

The principal detractors in the first quarter of 2020 were Enquest Plc 7.0% due 04/15/2022; Antero Resources Corp. 5.625%, due 06/01/2023; Men's Wearhouse, Inc. 7.0% due 07/01/2022; NGL Energy Partners Lp 7.5% due 11/01/2023; and California Resources Corp. 8.0%, due 12/15/2022.

UK-based EnQuest is a North Sea oil producer, and the sharp decline in crude oil prices during the first quarter hit these bonds pretty hard despite executing well of late. Similarly, bonds issued by Antero, a high-quality extractor of natural gas and natural gas liquids in the Marcellus and Utica formations, sold off with the rest of the energy complex. We may have expected diversified midstream players like NGL to fare better than the pack in the selloff, but its bonds were punished like any other energy industry participant. California Resources had been hurt in recent quarters by legislative noise in California, and plummeting energy prices only worsened the pain.

Retailers have struggled through the ongoing coronavirus outbreak, and Men's Wearhouse bonds were particularly vulnerable to negative sentiment, with Moody's having lowered its outlook to negative from stable, citing profitability and cash-flow issues, even before store shutdowns began.

Sincerely,

First Eagle Investment Management, LLC

* Performance for Class A shares without the effect of sales charges and assumes all distributions have been reinvested, and if a sales charge was included values would be lower.

Average Annual Returns as of 03/31/2020 (%)

		YTD	1 Year	5 Years	10 Years	Since Inception	Inception Date	Expense Ratio Gross*	Expense Ratio Net
First Eagle High Income Fund – Class A (without sales charge)	FEHAX	-12.17	-8.30	0.97	--	3.15	01/03/12	1.34	1.24
First Eagle High Income Fund – Class A (with sales charge)		-16.08	-12.43	0.04	--	2.58			
First Eagle High Income Fund – Class I (without sales charge)	FEHIX	-12.11	-8.04	1.26	4.37	6.50	11/19/07	1.05	0.95
Bloomberg Barclays U.S. Corporate High Yield Bond Index		-12.68	-6.94	2.78	5.64	6.31	11/19/07**		

The annual expense ratio is based on expenses incurred by the Fund, as stated in the most recent prospectus.

*These are the actual Fund operating expenses prior to the application of fee waivers and/or expense reimbursements. The Adviser has contractually agreed to waive its management fee at an annual rate in the amount of 0.10% of the average daily value of the Fund's net assets for the period through February 28, 2021. This waiver has the effect of reducing the management fee for the term of the waiver from 0.70% to 0.60%. Had fees not been waived and/or expenses reimbursed, returns would have been lower.

**Inception date shown for the Bloomberg Barclays U.S. Corporate High Yield Bond Index matches the High Income Fund Class I shares, which have the oldest since inception date for the High Income Fund.

Class I Shares require $1 million minimum investment, and are offered without sales charge. Performance information assumes all distributions have been reinvested and does not account for taxes. The Fund commenced operations in its present form on December 30, 2011, and is successor to another mutual fund pursuant to a reorganization December 30, 2011. Information prior to December 30, 2011, is for this predecessor fund. Immediately after the reorganization, changes in net asset value of the Class I shares were partially impacted by differences in how the Fund and the predecessor fund priced portfolio securities.

The performance data quoted herein represents past performance and does not guarantee future results. Market volatility can dramatically impact the Fund's short-term performance. Current performance may be lower or higher than figures shown. The investment return and principal value will fluctuate so that an investor's shares, when redeemed, may be worth more or less than their original cost. The average annual returns for Class A Shares "with sales charge" of the First Eagle High Income Fund gives effect to the deduction of the maximum sales charge of 4.50%. Past performance data through the most recent month-end is available at www.feim.com or by calling 800.334.2143.

Funds that invest in bonds are subject to interest-rate risk and can lose principal value when interest rates rise. Bonds are also subject to credit risk, in which the bond issuer may fail to pay interest and principal in a timely manner, or that negative perception of the issuer's ability to make such payments may cause the price of that bond to decline.

The Fund invests in high yield securities (commonly known as "junk bonds") which are generally considered speculative because they may be subject to greater levels of interest rate, credit (including issuer default) and liquidity risk than investment-grade securities and may be subject to greater volatility. The Fund invests in high yield securities that are non-investment grade. High yield, lower-rated securities involve greater price volatility and present greater risks than higher-rated fixed income securities. High yield securities are rated lower than investment-grade securities because there is a greater possibility that the issuer may be unable to make interest and principal payments on those securities. All investments involve the risk of loss.

Bank loans are often less liquid than other types of debt instruments. There is no assurance that the liquidation of any collateral from a secured bank loan would satisfy the borrower's obligation, or that such collateral could be liquidated.

There are risks associated with investing in securities of foreign countries, such as erratic market conditions, economic and political instability and fluctuations in currency exchange rates. These risks may be more pronounced with respect to investments in emerging markets.

Funds whose investments are concentrated in a specific industry or sector may be subject to a higher degree of risk than funds whose investments are diversified and may not be suitable for all investors.

The holdings mentioned herein represent the following percentages of the total net assets of the First Eagle High Income Fund as of March 31, 2020: HCA Inc. 5.875%, due 05/01/2023—0.79%;Southeastern Grocers Inc Common Stock USD—4.38%; Diamond1 Finance Corp. 7.125%, due 06/15/2024—2.52%; HCA Healthcare, Inc. 6.25%, due 02/15/2021—0.00%; Open Text Corporation 5.625%, due 01/15/2023—0.00%; EnQuest Plc 7.0%, due 04/15/2022—0.67%; Antero Resources Corp. 5.625%, due 06/01/2023—1.60%; Men's Wearhouse, Inc. 7.0%, due 06/01/2022—0.88%; NGL Energy Partners LP 7.5%, due 11/01/2023—1.02%; California Resources Corp. 8.0%, due 12/15/2022—0.48%.

The commentary represents the opinion of the High Yield team portfolio managers as of March 31, 2020, and is subject to change based on market and other conditions. The opinions expressed are not necessarily those of the firm. These materials are provided for informational purposes only. These opinions are not intended to be a forecast of future events, a guarantee of future results, or investment advice. Any statistics contained herein have been obtained from sources believed to be reliable, but the accuracy of this information cannot be guaranteed. The information provided is not to be construed as a recommendation to buy, hold or sell or the solicitation or an offer to buy or sell any fund or security.

A credit rating as represented here is an assessment provided by a nationally recognized statistical rating organization (NRSRO) or credit worthiness of an issuer with respect to debt obligations, including specific securities, money market instruments, or other bonds. Ratings are measured on a scale that generally ranges from AAA (highest) to D (lowest); ratings are subject to change without notice. Not Rated (NR) indicates that the debtor was not rated and should not be interpreted as indicating low quality. For more information on the Standard & Poor's rating methodology, please visit standardandpoors.com and select "Understanding Ratings" under Rating Resources.

The Bloomberg Barclays US Corporate High Yield Bond Index comprises fixed-rate, publicly issued, non-investment grade debt, is unmanaged, with dividends reinvested, and is not available for purchase. The index includes both corporate and non-corporate sectors. The corporate sectors are industrial, utility, and finance, which include both US and non-US corporations. The index is presented here for comparison purposes only. One cannot invest directly in an index. Indices do not incur management fees or other operating expenses.

Investors should consider investment objectives, risks, charges and expenses carefully before investing. The prospectus and summary prospectus contain this and other information about the Fund and may be obtained by asking your financial advisor, visiting our website at www.feim.com or calling us at 800.334.2143. Please read our prospectus carefully before investing. Investments are not FDIC insured or bank guaranteed, and may lose value.

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