

Mohamed El-Erian and Ramin Toloui

Discuss the PIMCO Global Advantage™ Strategy

With the global economy and financial system undergoing profound changes, investors need an investment approach that positions them to thrive in the New Normal. PIMCO's Global Advantage Bond Index (GLADI™) provides investors with an alternative fixed income benchmark designed to better capture the opportunities in the changing world. In this interview, PIMCO's CEO and Co-CIO Mohamed El-Erian and Executive Vice President Ramin Toloui discuss the new index and its application as a benchmark in PIMCO's Global Advantage strategy.

Q: What is PIMCO Global Advantage? Is it a strategy or an index?

El-Erian: Global Advantage is a fixed income approach designed to help investors seize the opportunities created by the dramatic secular shifts taking place in the global economy. The approach consists of an innovative, forward-looking index and an investment strategy built around that index.

The new index – the PIMCO Global Advantage Bond Index (GLADI) – offers investors a wider spectrum of fixed income opportunities and sectors, from developed to emerging markets, nominal to real (inflation-linked) assets, and cash to derivative instruments.

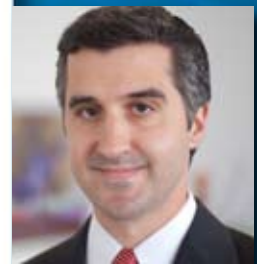
The actively managed Global Advantage strategy combines the “beta” of GLADI with an alpha strategy driven by PIMCO's combination of top-down macro analysis and bottom-up depth of resources across market sectors and geographies. The result is a bond strategy that can potentially enhance returns and reduce volatility, while simultaneously positioning investors for the secular global destination of tomorrow.

Q: Why do investors need another fixed income benchmark?

El-Erian: Dramatic transformations in growth drivers, wealth dynamics and institutional arrangements affect the ability of traditional investment approaches to generate sustainable returns while also managing risks. We have designed the PIMCO Global Advantage Bond Index as a tool designed to better represent the universe of investment opportunities available to investors in this new world. This means less emphasis on government debt of the United States and other industrialized countries, and more emphasis on the full spectrum of global



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opportunities, such as those in inflation-protected securities, emerging-market assets, and other modern fixed income instruments.

Many portfolio managers use such securities already as “off-index” investments in bond portfolios. By incorporating these instruments directly into the index itself, we think GLADI offers investors an improved yardstick and greater transparency for measuring their investments and manager performance.

We believe that GLADI also provides a benchmark for asset allocation that will serve investors well in the coming years. Many investors have embraced global diversification in their equity portfolios but may still be underexposed to global bonds, particularly in some of the world’s most dynamic economies. We believe that the secular forces transforming global capital markets will only increase the need to diversify globally.

Q: How is GLADI different from other fixed income indices?

Toloui: Two main elements set GLADI apart from other global fixed income benchmarks: first, the inclusion of a fuller set of fixed income opportunities, and, second, the use of GDP-weighting as an alternative to traditional market-capitalization weighting.

First, GLADI reflects the full universe of investment-grade, fixed income opportunities. Not only is it diversified across market sectors, geographies, and currencies, but it also incorporates non-traditional instruments such as swaps and inflation-linked bonds, which investment managers commonly utilize in portfolios but that are usually not reflected in indices.

Second, GLADI uses an innovative GDP weighting methodology as a replacement for the traditional weighting based on market capitalization. Market capitalization weights are inherently backward-looking, reflecting past patterns of capital market development. Since rapid economic growth tends to precede the liberalization and deepening of capital markets, GLADI’s GDP weighting is designed to capture the opportunities that exist in the world’s most dynamic economies. This helps investors position their portfolios to seize these opportunities ahead of the herd, reminiscent of hockey great Wayne Gretzky’s famous maxim for success: “I skate to where the puck is going to be, not where it has been.”

Q: What are the advantages of GDP weighting?

Toloui: In addition to embedding a forward-looking orientation in the index construction, GDP weighting can also help avoid some of the crucial pitfalls of traditional market capitalization-weighted indices. The market capitalization approach increases the weight of securities that have recently gone up in price and reduces the weight of securities that have recently declined in price – exactly the opposite of the investment maxim to “buy low, sell high.”

Moreover, market capitalization weighting in a bond index can allocate too heavily to government debt and large bond issuers with debt burdens that might be negative for creditworthiness. The current crisis offers a case in point: With their fiscal deficits on the rise, G-7 governments will be issuing large quantities of bonds over the next few years. This will lead to an increased allocation to G-7 government bonds in traditional market cap-weighted indices. GDP-weighting avoids this adverse tendency, relative to traditional indices.

Finally, GDP weighting tends to lead to counter-cyclical rebalancing, since bond prices tend to move inversely to GDP growth rates. This gives GLADI a structural advantage that can potentially boost long-term performance.

Q: Which investors is Global Advantage designed for? And how might Global Advantage fit into investor portfolios?

El-Erian: We designed Global Advantage to be a core bond strategy that represents an investment solution for a wide range of investors. In a world in which global economic relationships are being re-aligned, the importance of global diversification has never been greater. Global Advantage is designed to be part of a more holistic approach to achieve that.

Global Advantage fits into investors’ portfolios in several different ways. The strategy may be utilized as an all-in-one solution to gain fixed income exposure to different markets and sectors, leaving allocation decisions to experienced managers. Global Advantage also complements existing core allocation (in many cases domestic and/or government bonds) to allow investors to take opportunities in a broader and forward-looking global market. Finally, as an alternative to equities, this strategy represents an effective vehicle for taking international exposure in the portfolio, with a focus on maintaining a low volatility and attractive risk-adjusted returns.

Q: Do investors need to invest in PIMCO's Global Advantage strategy to apply GLADI as benchmark?

El-Erian: No. While as an experienced fixed income manager we think that we are well-positioned to outperform GLADI, the index can be used as benchmark for portfolios managed by any fixed income manager. Performance and detailed index information for GLADI is publicly available on the Internet and through information services such as Bloomberg. GLADI is administered and calculated independently from PIMCO by Markit LLC, an unaffiliated global index provider. Portfolios benchmarked to GLADI managed by other fixed income managers have the potential to benefit from GLADI's improved fixed income beta, though they do not give an investor the advantage of PIMCO's active management capabilities.

For more information:

Additional information and access to GLADI data can be found at: www.pimcoindex.com and www.indexco.com/link/pimco. It is also available on Bloomberg by typing PGLA Index <GO>.

For more information about the PIMCO Global Advantage Strategy, please contact your PIMCO representative.

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Beta is the return generated from a portfolio that can be attributed to overall market returns. Alpha is the portion of a portfolio's return that is independent from market returns.

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