Investment Perspectives

# How Completion Portfolios Can Help Enhance Separately Managed Accounts

**These specialized mutual funds can help SMA portfolios achieve diversification and gain access to a greater range of investable securities.**

*Stephen Hillebrecht, CFA*
*Co-Head of Product Management*

Although Separately Managed Accounts (SMAs) have seen tremendous growth in recent years—and gained greater attention from investors—they have been around since the 1970s. These vehicles were originally developed to bring institutional-quality investment management to the individual investor. Previously, retail investors could gain access to broad diversification and professional management via mutual funds, but separately managed portfolios of individual securities were only available to investors that could meet institutional minimums.

Through an SMA, individual investors can access institutional-style professional management with much lower minimums (typically $100,000, for example, in the case of equity portfolios). Compared to investing through a mutual fund, some of the potential benefits of an SMA that come from individual security ownership include:

- Increased transparency of portfolio holdings.
- Flexibility to customize portfolios.
- Ability to implement security and industry restrictions.
- Greater control over tax planning.

Given these attributes, it may be surprising to some to see the growing trend of certain SMA portfolios including mutual funds as a key element of their strategy. These funds, also known as *completion portfolios*, are designed to serve specific functions within an SMA.

Here, we offer more details about completion portfolios, how they work, and their potential benefits to SMA investors.

## What are completion portfolios?

Completion portfolios are no-fee mutual funds that are designed and managed exclusively to be a component of an SMA portfolio. They are registered with the SEC under the Investment Company Act of 1940 like any other mutual fund but are only available to the manager of the SMA portfolio. Completion portfolios are not available to be purchased or sold by any other investor. These funds can provide portfolio diversification and access to certain securities that are not typically included in SMA strategies, at no additional cost to the investor.

LORD ABBETT®

## Why would an SMA strategy benefit from a completion portfolio?

While pooled investment vehicles like mutual funds can hold hundreds, if not thousands of securities, an individual SMA tends to have a much smaller number of positions. For example, a high-quality municipal bond strategy (investing in bonds rated 'AAA' through 'A') can achieve sufficient diversification with a portfolio of as little as 10 to 15 holdings.

However, history shows there are tremendous opportunities in bonds rated 'BBB' and below, which not only offer higher tax-free income, but have delivered much higher total returns over the long term.[1] In order to achieve prudent diversification when investing in lower-rated credits, the portfolio would need a much larger number of holdings than are typically found in an SMA strategy.

Even among higher-rated securities, SMA portfolios tend to focus on larger, more liquid issues, as they may be required to sell odd-lot positions to meet redemption requests. Completion portfolios allow investors to access high-quality issues with enhanced yield and total return potential that might not have the liquidity profile to be included in an SMA portfolio.

## How are these strategies managed?

SMA portfolios that include completion portfolios are managed in a holistic manner, targeting overall portfolio exposures for yield curve, credit quality, and sector positioning. For example, the Lord Abbett Enhanced Intermediate Municipal Bond SMA strategy includes a portfolio of high-quality individual municipal bonds (rated A- or higher) along with a completion portfolio consisting of a diversified selection of more credit-sensitive municipals. This approach can enable a professional manager to deliver to SMA investors an investment solution more typically found in a mutual fund.

Clients could benefit from the transparency, tax efficiency, and customization options from the individual bond holdings, as well as the higher income, potential total return, and diversification benefits of the completion portfolio.

## Are completion portfolios only beneficial to municipal strategies?

Completion portfolios can be valuable additions to many SMA investment strategies. Within taxable fixed income, for example, individual positions in SMA portfolios are largely limited to U.S. Treasuries, U.S. government-related securities, and certain segments of the high-quality corporate and asset-backed securities (ABS) markets. The addition of high yield exposure could enhance yield and total return in these high-quality portfolios, but as noted earlier, proper diversification in the high yield corporate bond market would require a large number of holdings. Meanwhile, certain segments of the high yield market may have minimum trade sizes or might not have the proper liquidity profile to trade odd-lot sizes in SMA accounts.

In addition, a large and growing part of the taxable bond market (corporate bonds, securitized sectors, and convertible securities) is now issued under the U.S. Securities & Exchange Commission's Rule 144a, meaning that such securities are only available to qualitied institutional investors. While securities covered under this rule are commonly found in mutual funds, they are not registered for sale to individual investors. Completion portfolios can allow access to this broader opportunity set; the enhanced diversification and yield of these sectors can help deliver core-plus or multisector bond strategies within an SMA portfolio.

### Potential Benefits of an SMA Strategy with a Completion Portfolio

| Individual Bond Holdings | Completion Portfolio |
|---|---|
| ▪ Transparency into holdings | ▪ Access to broader opportunity set |
| ▪ Ability to customize portfolios | ▪ Portfolio diversification |
| ▪ Flexibility to restrict securities and industries | ▪ Higher income and total return potential |
| ▪ Greater control over tax planning | ▪ Zero additional expense |

Source: Lord Abbett. For illustrative purposes only.

[1]Based on the performance of ratings-specific segments (i.e., for ratings 'BBB' and below) of the Bloomberg Municipal Bond Index in the 10 years ended December 31, 2023.

Separately managed accounts may not be appropriate for all investors. This information should not be relied upon as investment advice or a recommendation for any particular investment product or strategy and is provided for informational purposes only.

Lord Abbett Separately Managed Accounts - Lord, Abbett & Co. LLC. is the investment advisor for the separately managed accounts (SMA).

The information provided is not directed at any investor or category of investors and is provided solely as general information about Lord Abbett's products and services and to otherwise provide general investment education. None of the information provided should be regarded as a suggestion to engage in or refrain from any investment-related course of action as neither Lord Abbett nor its affiliates are undertaking to provide impartial investment advice, act as an impartial adviser, or give advice in a fiduciary capacity.

A Note about Risk: As interest rates rise, the prices of debt securities tend to fall; as rates fall, prices tend to rise. The value of a portfolio will change as interest rates fluctuate. Municipal securities may include insured municipal securities that are covered by insurance policies that guarantee the timely payment of principal and interest. Insurance does not pertain to yield or market values, which will fluctuate over the life of bonds. Income from municipal bonds may be subject to the alternative minimum tax. Federal, state, and local taxes may apply. Although these are the main risks of investing in bonds, there may be other risks associated with investing in bonds, such as credit, inflation, call, high-yield, and market risks. An investor should consult with his or her investment professional before making an investment decision.

Asset allocation or diversification does not guarantee a profit or protect against loss in declining markets.

No investing strategy can overcome all market volatility or guarantee future results.

The value of investments and any income from them is not guaranteed and may fall as well as rise, and an investor may not get back the amount originally invested. Investment decisions should always be made based on an investor's specific financial needs, objectives, goals, time horizon, and risk tolerance.

Market forecasts and projections are based on current market conditions and are subject to change without notice.

Projections should not be considered a guarantee.

**Fixed-Income Investing Risks**

The value of investments in fixed-income securities will change as interest rates fluctuate and in response to market movements. Generally, when interest rates rise, the prices of debt securities fall, and when interest rates fall, prices generally rise. High yield securities, sometimes called junk bonds, carry increased risks of price volatility, illiquidity, and the possibility of default in the timely payment of interest and principal. Bonds may also be subject to other types of risk, such as call, credit, liquidity, and general market risks. Longer-term debt securities are usually more sensitive to interest-rate changes; the longer the maturity of a security, the greater the effect a change in interest rates is likely to have on its price.

The credit quality of fixed-income securities in a portfolio is assigned by a nationally recognized statistical rating organization (NRSRO), such as Standard & Poor's, Moody's, or Fitch, as an indication of an issuer's creditworthiness. Ratings range from 'AAA' (highest) to 'D' (lowest). Bonds rated 'BBB' or above are considered investment grade. Credit ratings 'BB' and below are lower-rated securities (junk bonds). High-yielding, non-investment-grade bonds (junk bonds) involve higher risks than investment-grade bonds. Adverse conditions may affect the issuer's ability to pay interest and principal on these securities.

This material may contain assumptions that are "forward-looking statements," which are based on certain assumptions of future events. Actual events are difficult to predict and may differ from those assumed. There can be no assurance that forward-looking statements will materialize or that actual returns or results will not be materially different from those described here.

The views and opinions expressed are as of the date of publication, and do not necessarily represent the views of the firm as a whole. Any such views are subject to change at any time based upon market or other conditions, and Lord Abbett disclaims any responsibility to update such views. Lord Abbett cannot be responsible for any direct or incidental loss incurred by applying any of the information offered.

This material is provided for general and educational purposes only. It is not intended as an offer or solicitation for the purchase or sale of any financial instrument, or any Lord Abbett product or strategy. References to specific asset classes and financial markets are for illustrative purposes only and are not intended to be, and should not be interpreted as, recommendations or investment advice.

Please consult your investment professional for additional information concerning your specific situation.

**Glossary & Index Definitions**

**Core bond** portfolios invest primarily in investment-grade, U.S. fixed-income issues including government, corporate, and securitized debt. **Core plus** is an investment management style that permits managers to add instruments with greater risk and greater potential return to a core bond strategy.

An **odd lot** is an order amount for a security that is less than the normal unit of trading for that particular asset.

**Yield** is the income returned on an investment, such as the interest received from holding a security. The yield is usually expressed as an annual percentage rate based on the investment's cost, current market value, or face value. **Yield-to-maturity** (YTM) represents the expected return (expressed as an annualized rate) from the bond's future cash flows, including coupon payments over the life of the bond and the bond's principal value received at maturity. **Yield-to-worst** refers to the lesser of a bond's (a) yield-to-maturity or (b) the lowest yield-to-call calculated on each scheduled call date.

**Yield curve** is a line that plots the interest rates, at a set point in time, of bonds having equal credit quality, but differing maturity dates. One such comparison involves the two-year and 10-year U.S. Treasury debt. This yield curve is used as a benchmark for other debt in the market, such as mortgage rates or bank lending rates. The curve is also used to predict changes in economic output and growth.

The **Bloomberg Municipal Bond Index** is a rules-based, market-value-weighted index engineered for the long-term, tax-exempt bond market. Bonds must be rated investment-grade (Baa3/BBB- or higher) by at least two ratings agencies. They must have an outstanding par value of at least $7 million and be issued as part of a transaction of at least $75 million. The bonds must be fixed rate, have a dated-date after December 31, 1990, and must be at least one year from their maturity date.

LORD ABBETT®

Bloomberg Index Information

Source: Bloomberg Index Services Limited. BLOOMBERG® is a trademark and service mark of Bloomberg Finance L.P. and its affiliates (collectively "Bloomberg"). Bloomberg owns all proprietary rights in the Bloomberg Indices. Bloomberg does not approve or endorse this material or guarantee the accuracy or completeness of any information herein, or make any warranty, express or implied, as to the results to be obtained therefrom and, to the maximum extent allowed by law, shall not have any liability or responsibility for injury or damages arising in connection therewith.

Indexes are unmanaged, do not reflect the deduction of fees or expenses, and are not available for direct investment.

This material is the copyright © 2024 of Lord, Abbett & Co. LLC. All Rights Reserved.

Important Information for U.S. Investors

Lord Abbett mutual funds are distributed by Lord Abbett Distributor LLC.

**FOR MORE INFORMATION ON ANY LORD ABBETT FUNDS, CONTACT YOUR INVESTMENT PROFESSIONAL OR LORD ABBETT DISTRIBUTOR LLC AT 888-522-2388, OR VISIT US AT LORDABBETT.COM FOR A PROSPECTUS, WHICH CONTAINS IMPORTANT INFORMATION ABOUT A FUND'S INVESTMENT GOALS, SALES CHARGES, EXPENSES AND RISKS THAT AN INVESTOR SHOULD CONSIDER AND READ CAREFULLY BEFORE INVESTING.**

The information provided is not directed at any investor or category of investors and is provided solely as general information about Lord Abbett's products and services and to otherwise provide general investment education. None of the information provided should be regarded as a suggestion to engage in or refrain from any investment-related course of action as neither Lord Abbett nor its affiliates are undertaking to provide impartial investment advice, act as an impartial adviser, or give advice in a fiduciary capacity. If you are an individual retirement investor, contact your financial advisor or other fiduciary about whether any given investment idea, strategy, product or service may be appropriate for your circumstances.


Copyright © 2024 by Lord, Abbett & Co. LLC/Lord Abbett Distributor LLC. All rights reserved.


IP-COMPLETION_PORTFOLIO
05-24

NOT FDIC INSURED–NO BANK GUARANTEE–MAY LOSE VALUE