PACIFIC FUNDS

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FLOATING RATE INCOME COMMENTARY

DECEMBER 31, 2022

SUB-ADVISED BY PACIFIC ASSET MANAGEMENT LLC

Class A		Class C		Class I-2	
Ticker	**Fund Number**	**Ticker**	**Fund Number**	**Ticker**	**Fund Number**
PLFLX	110	PLBCX	310	PLFDX	010

Market Overview

2022 dealt a year of challenges not seen in decades. Accelerating inflation in the front end of the year led to aggressive monetary policy responses across global central banks. Domestically, the Federal Reserve raised the target Fed Funds rate by over 400 bps through the year and transitioned from Quantitative Easing to Quantitative Tightening. As monetary policy tightened, domestic and global growth waned, elevating recessionary fears. Most risk assets had the worst calendar year returns since 2008. However, the most notable pain in 2022 was felt in the bond market, where the Bloomberg U.S. Aggregate Index lost over 13%, more than 4X the loss of the worst calendar year return, -2.92% during 1994, in index history. As we transition into 2023, investors remain uncertain on prospects of a hard or soft landing.

While third quarter real gross domestic product (GDP) was revised higher from 2.9% to 3.2%, indications of weakening fundamentals have emerged with greater frequency. After a 29-month period of consistent growth, the ISM Manufacturing Index contracted the last two months of 2022 to 48.4%. The index's report cites easing customer demand, skilled labor shortages, supply-chain issues, and uncertain economic forecasts that are causing delayed commitments for capital purchases. Likewise, December marked the sixth straight month of contraction for the US Services PMI. Additionally, the Conference Board Leading Economic Index (LEI) for the U.S. decreased by 1% in November following a decline October. The LEI is now down 3.7% over the six-month period (May to November 2022), a much steeper rate of decline than its 0.8% contraction over the previous six-month period (Nov. 2021 to May 2022).

The combination of a slowing savings rates, elevated costs of goods and services, increased usage of credit by consumers, declining home values, and lackluster market returns paints the picture of a worried consumer. Elevated cost pressures have been reflected in the personal savings rate (per BEA) moving to 2.4%, down from 4.7% in January 2022 and 20% in January 2021. As of year-end 2022, headline Consumer Price Index (CPI) resided at 7.1%, with the Core Personal Consumption Expenditures (PCE), the Fed's preferred inflation measure, at 4.7%. Both indicators were well above the Fed's targeted 2% inflation rate. A possible offset is that the labor market has remained tight, with unemployment holding at 3.7%. There has not been a formal recession in a century without deteriorating labor dynamics.

Inflation remains a key concern globally and has driven central banks to act strongly in both function and rhetoric. Federal Reserve officials appear unwavering in their fight against inflation. The 50bps rate hike in December ended a streak of four consecutive 75bps rate hikes, taking the target range for the fed funds rate to 4.25%-4.5%--its highest level in 15 years. The most recent FOMC meeting minutes revealed that while Fed Chair Powell indicated that there has been some progress in the battle against inflation, he saw only halting signs and expects rates to hold at higher levels even after the increases cease. The FOMC meeting minutes also stated, "Participants generally observed that a restrictive policy stance would need to be maintained until the incoming data provided confidence that inflation was on a sustained downward path to 2%, which was likely to take some time. … In view of the persistent and unacceptably high level of inflation, several participants commented that historical experience cautioned against prematurely loosening monetary policy." As a result, no FOMC members expect rate cuts in 2023. In conjunction with increasing rates, the Fed has been shrinking its balance sheet by enacting quantitative tightening (QT), allowing up to $95 billion in proceeds from maturing securities to roll off each month rather than be reinvested. In a program started mid-2022, the balance sheet has contracted by $364 billion to $8.6 trillion. As the rate of inflation remains well above the Fed's 2% target, the market has assumed additional rate hikes in early 2023, possibly elevating the fed funds rate north of 5%.

Across the pond, the European Central Bank (ECB) hiked rates again in December to 2% and stressed significant tightening remains ahead as it presented plans to drain cash from the financial system to further combat elevated inflation. Driven

largely by COVID, supply-chain disruption and elevated energy costs, European inflation has risen substantially, although there have been recent signs of peaking amid recessionary fears. Nevertheless, ECB President Christine Lagarde is forecasting, "another 50bps rise at our next meeting and possibly at the one after that, and possibly thereafter."

Despite a strong Q4, 2022 proved difficult for risk-based assets. For the fourth quarter, the S&P 500 returned 7.55%, yet had an overall dismal performance in 2022, returning -18.13%. Uncertainty within the rate market has wrecked havoc within fixed-income asset classes and duration was unfriendly to investors. The return of the investment-grade bond market (represented by the Bloomberg US Credit Index) was markedly positive for the quarter but negative for the year, returning 3.44% and -15.26%, respectively. The high-yield bond market (represented by the Bloomberg US Corporate High Yield 2% Issuer Cap Index) performed positively in the fourth quarter, returning 4.17% but closed -11.18% for the year. The 10-year U.S. Treasury yield moved 21bps higher over the quarter and 236bps over the year, ending at 3.88%.

Asset Class Overview

In a historic year, the floating-rate loan asset class (represented by the Credit Suisse Leveraged Loan Index or CSLL Index) was largely, but not entirely, immune. The CSLL Index returned 2.33% in the fourth quarter, and while outperforming nearly all other fixed-income asset classes on calendar basis, the asset class returned -1.06% over the year. This annual return marked the second worst return of the index since its inception (only 2008 was worst, returning -28.75%). Additionally, 2022 was only the third negative calendar year return of the index since its inception (2008 returned -28.75%, 2015 returned -0.38%, and 2022 returned -1.06%). Needless to say, the floating-rate loan asset class was a shining star in the face of extraordinary rate hikes, persistent inflation, weakening growth, supply-chain disruption, and geopolitical conflict.

As investors weighed concerns of slowing growth and persistent inflation, fund flows weakened over the year. Loan funds experienced significant outflows in 2022 totaling -$11.4 billion. However, this was countered by inflows totaling $46.5 billion in 2021. In 2022, loan outflows were offset by a lack of loan issuance and strong CLO issuance. 2022 institutional loan issuance totaled $252.5 billion ($163.1 billion, excluding refi/repricing), which is 70% lower (60%, excluding refi/repricing) than levels seen in 2021. Meanwhile, 2022 saw 323 U.S. CLOs price totaling $149.6 billion ($127.5 billion, excluding refinancing and $22.2 billion refinancing), marking the second highest year of CLO issuance in history. As measured by the 4-year effective yield, the CSLL Index currently offers investors a yield of 10.69%, with a coupon of over 8%.

The average price of the CSLL Index ended the year at $91.89, down $6.50 from the start of 2022. For the fourth quarter and the year, higher-quality credits outperformed lower quality with BB, B, and CCC rated issuers returning 3.63%, 2.41%, and -2.85% over the quarter and 2.70%, -1.33%, and -13.26% over the year, respectively. Performing loans (over $90) vastly outperformed distressed loans (up to and including $90), returning 3.09% versus -0.98% over the quarter and 0.58% and -19.72% over the year, respectively. According to J.P. Morgan, leveraged-loan default rates (including distressed exchanges) ended the quarter at 1.59%. J.P. Morgan has forecasted a 2023 year-end loan-default rate of 3.5% and a 2024 default rate of 4% on the back of elevated rate concerns, slowing growth, persistent inflation, and concern over corporate fundamental deterioration. For context, the historical longer-term default rate of loans in 3.2%.

Fund Performance

Pacific Funds Floating Rate Income (Class I-2) returned 2.70% versus the Credit Suisse Leveraged Loan Index return of 2.33%.

Past Performance is not indicative of future results. *Returns reflect reinvestment of dividends/distribution. 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. Current performance may be lower or higher than the performance quoted. Performance current to the most recent month end may be found at www.PacificFunds.com/performance or by calling 1-800-722-2333. The investment advisor has contractually agreed to limit certain expenses and reevaluates the annually. Please see the current prospectus for detailed information.*

Ratings are measured on a scale that generally ranges from AAA (highest) to D (lowest).

Portfolio Review

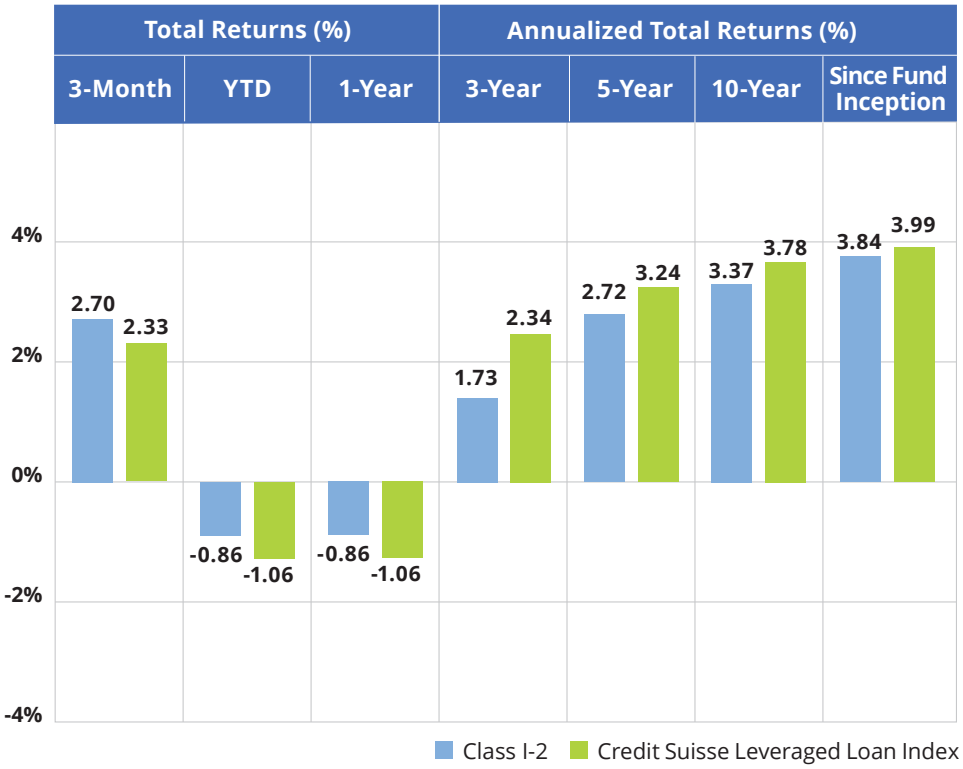
For the fourth quarter of 2022, the fund outperformed the benchmark due to security selection and an underweight to distressed loans (<$80 price). Security selection within information technology, healthcare, gaming and packaging were contributors to performance. Underweights to and security selection within energy, utilities and transportation detracted from performance. Credit-quality allocations were negative, driven by an underweight to loans rated BB and above, but was partially offset by an underweight to distressed (CC, C and default) securities. While the fund was overweight CCC rated issuers, the concentration was in performing second-lien loans, which contributed to performance. Exposure to high-yield bonds contributed to performance. The fund's focus on larger and more liquid issuers, generally greater than $1 billion in facility size, contributed to performance. Facility/issue sizes greater than $1 billion returned 3.05% versus facility/issue sizes less than $300 million returning -0.71%.

Manager Outlook

Floating-rate loans were among the best-performing asset classes in 2022 amid a rising-rate backdrop. The coupon of the asset class (as represented by the Credit Suisse Leveraged Loan Index as of year-end) was over 8% and is expected to climb higher in the first quarter 2023 as the Federal Reserve continues to fight inflation by increasing the federal funds rate. For context, the coupon of the asset class started the year in 2022 at just 4%. The 4-year discount margin of the benchmark ended the year at 592 basis points, representing an effective yield of approximately 10%. Implied annual default rates, using the historical average of excess spread and recoveries, stand at approximately 5%-6%. From an asset-demand perspective, loan retail mutual fund flows experienced outflows of $11 billion during the fourth quarter amid growing recessionary concerns. CLO issuance slowed in the fourth quarter to $23 billion, bringing year-to-date issuance to $128 billion.

We are overweight forest products/containers, information technology, and healthcare, while remaining underweight in media/telecom, food/tobacco, chemicals, and utility. We continue to favor many issuers within financials (insurance brokers) and information technology (software). We believe insurance companies will continue to exhibit an ability to perform well in both good and bad economic environments. We also believe software companies will continue to benefit from the stability of their subscription-based business models. We are underweight distressed CCC rated loans, with our CCC exposure largely concentrated in performing second-lien loans.

Class I-2



Top-10 Holdings	Weight (%)
Hub International Limited	2.09
Sunshine Luxembourg VII SARL	2.05
Epicor Software Corporation	2.02
RealPage, Inc.	1.89
PetVet Care Centers LLC	1.84
Bway Holding Co., Inc.	1.79
Polaris Newco LLC	1.72
Thrive Pet Healthcare	1.59
Sovos Compliance LLC	1.54
CDK Global, Inc.	1.50
Total	**18.03**

Past Performance is not indicative of future results. *Returns reflect reinvestment of dividends/distribution. 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. Current performance may be lower or higher than the performance quoted. Performance current to the most recent month end may be found at www.PacificFunds.com/ performance or by calling 1-800-722-2333. The investment advisor has contractually agreed to limit certain expenses and reevaluates the annually. Please see the current prospectus for detailed information.*

Gross/Net annual operating expenses for Class I-2 are 0.90%/0.77%. Inception date 6/29/12.

Indexes are unmanaged and cannot be invested in directly. Further, they hold no cash and incur no expenses. All share classes may not be available at all firms and not all investors may be eligible for all share classes.

Definitions

One **basis point** equals 0.01%.

The **Bloomberg 1–3 Year US Government/Credit Bond Index** is a performance benchmark of U.S. investment-grade government and corporate bonds with maturities of one to three years.

The **Bloomberg Asset-Backed Securities (ABS) Index** is the ABS component of the Bloomberg Barclays U.S. Aggregate Index that measures the performance of ABS with the following collateral types: credit and charge card, auto and utility loans. All securities have an average life of at least one year.

The **Bloomberg Short Treasury Total Return Index** is a performance benchmark of all U.S. Treasuries that have a remaining maturity between one and twelve months.

The **Bloomberg US Aggregate Bond Index** is composed of investment-grade U.S. government bonds, investment-grade corporate bonds, mortgage pass-through securities, and asset-backed securities, and is commonly used to track the performance of U.S. investment-grade bonds.

The **Bloomberg US Corporate Bond Index** includes publicly issued U.S. corporate and specified foreign debentures and secured notes that meet the specified maturity, liquidity, and quality requirements.

The **Bloomberg US Corporate High Yield Bond Index** measures the USD-denominated, high yield, fixed-rate corporate bond market.

The **Bloomberg US Credit Index** measures the investment grade, US dollar-denominated, fixed-rate, taxable corporate and government-related bond markets. It is composed of the US Corporate Index and a non-corporate component that includes non-US agencies, sovereigns, supranationals and local authorities.

The **Bloomberg US High-Yield 2% Issuer Capped Bond Index** measures the performance of high-yield bonds with a 2% maximum allocation to any one issuer.

The **Credit Suisse Leveraged Loan Index** is designed to mirror the investable universe of the U.S. senior secure-credit (leveraged-loan) market.

Duration is often used to measure a bond's or fund's sensitivity to interest rates. The longer a fund's duration, the more sensitive it is to interest-rate risk. The shorter a fund's duration, the less sensitive it is to interest-rate risk.

The **ISM Non-Manufacturing Purchasing Managers' Index (PMI)** (also known as the **ISM Services PMI**) report on Business, a composite index is calculated as an indicator of the overall economic condition for the non-manufacturing sector.

Option adjusted spread (OAS) is the measurement of the spread of a fixed-income security rate and the risk-free rate of return.

Quantitative Easing (QE) is a monetary policy action whereby a central bank purchases predetermined amounts of government bonds or other financial assets in order to stimulate economic activity.

Quantitative Tightening (QT) (or quantitative hiking) is a contractionary monetary policy applied by a central bank to decrease the amount of liquidity within the economy.

The **S&P 500 index** is a market capitalization-weighted index of 500 widely held stocks often used as a proxy for the U.S. stock market.

Yield to worst is the lowest potential yield that can be received on a bond without the issuer actually defaulting.

Investing involves risk. Principal loss is possible. The Fund is subject to liquidity risk (the risk that an investment may be difficult to purchase, value, and sell particularly during adverse market conditions, because there is a limited market for the investment, or there are restrictions on resale) and credit risk (the risk an issuer may be unable or unwilling to meet its financial obligations, risking default). High-yield/high-risk bonds ("junk bonds") and floating-rate loans (usually rated below investment grade) have greater risk of default than higher-rated securities/higher-quality bonds that may have a lower yield. The Fund is also subject to foreign-markets risk.

This commentary represents the views of the portfolio managers at Pacific Asset Management LLC as of the publication date and are presented for informational purposes only. These views should not be construed as investment advice, an endorsement of any security, mutual fund, sector or index, or to predict performance of any investment. Any forward-looking statements are not guaranteed. All material is compiled from sources believed to be reliable, but accuracy cannot be guaranteed. The opinions expressed herein are subject to change without notice as market and other conditions warrant. Sector names in this commentary are provided by the Fund's portfolio managers and could be different if provided by a third party.

Investors should consider a fund's investment goal, risk, charges, and expenses carefully before investing. The prospectus contains this and other information about the fund and can be obtained at www.PacificFunds.com. It should be read carefully before investing.

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Diversification does not assure a profit, nor does it protect against a loss in a declining market.

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