Touchstone Impact Bond Fund

Sub-Advised by: EARNEST Partners LLC

Income – Investment Grade Bond 3Q/2023

Fund Manager Commentary

As of September 30, 2023

Fund Highlights

- Seeks to maximize total return by investing in market sectors and securities that are considered undervalued for their risk characteristics
- Focus is placed on high-quality securities, many with beneficial structures such as government guarantees or significant tangible collateral support; there is limited exposure to non-investment grade securities
- Prefers to invest in securities of government programs and companies that have sustainable operating models by considering a wide range of factors including, but not limited to, support for economic development, home ownership and job creation
- Utilizes a traditional long-only investment style and invests directly in cash bonds
- Does not invest in futures contracts, options, credit default swaps or derivatives
- Constructs a diversified portfolio across issuer, sector and industry that strives to maximize yield while minimizing the risks inherent in fixed income investing

Market Recap

The third quarter of 2023 was characterized by significant macroeconomic events that influenced the financial landscape. The U.S. Federal Reserve's (Fed) actions, particularly their decisions during and after their September meeting, played a pivotal role in shaping the market's trajectory. Interest rates saw an uptick during this period, largely influenced by the Fed's stance and the market's subsequent adjustments. These rate increases appear to be having the largest effect on the housing market and real estate markets. Home affordability is near an all-time low as the rate on a conventional 30-year mortgage finished the quarter at 7.35%. While housing price data turned up towards the end of the quarter, transactions are down near to levels experienced during the Great Financial Crisis.

Still, the economic data continues to provide an overall healthy environment. GDP growth was last reported at 2.4%, unemployment at 3.8%, and Core PCE at 3.9%. The strength of the economy, in the face of the increases in interest rates over the last year and a half, has surprised many. It pushed the Fed to upgrade their economic projections and espouse more confidence that they will be able to achieve a famed soft landing.

The other major development during the quarter was the downgrade of the U.S. Government debt by Fitch. This decision was primarily driven by the persistent budget deficits the government faced, which are expected to reach 5.7% of GDP in 2023. The recent removal of Speaker of the U.S. House of Representatives Kevin McCarthy is unlikely to help temper the situation.

Interest rates experienced an increase during the quarter, with short Treasury yields rising by less than 20 basis points (bps). More pronounced changes were observed in the 10-year and 30-year Treasury yields, which increased by 84bps and 94bps, respectively. The yield curve underwent a steepening process, particularly evident in the last several weeks of the quarter. This was a reaction to the market's realization of the Fed's commitment to maintaining higher rates for an extended period. These rate moves led to a total return of -3.23% for the Bloomberg U.S. Aggregate Bond Index during the quarter, eliminating the positive total returns produced during the first half of the year.

Spreads were mixed during the period, but on aggregate observed a modest widening during the quarter led by Agency Single-Family Mortgage Backed Securities (SF MBS). In terms of quality differentiation, lower-quality bonds outperformed their higher-quality counterparts in excess returns.

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Performance data quoted represents past performance, which is no guarantee of future results. The investment return and principal value of an investment in the Fund will fluctuate so that an investor's shares, when redeemed, may be worth more or less than their original cost. Current performance may be higher or lower than performance data given. ***For performance information current to the most recent month-end, visit TouchstoneInvestments.com/mutual-funds.***

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Portfolio Review

The Touchstone Impact Bond Fund (Class A Shares Load-Waived) outperformed its benchmark, the Bloomberg U.S. Aggregate Bond Index, for the quarter ended September 30, 2023.

Increases in interest rates had little impact on the relative performance of the fund during the period.

Spread sectors generated mixed excess returns. The weak structure of SF MBS caused the sector to be negatively affected by the surge in interest rates. As a result, the sector underperformed matched duration Treasuries by -85bps. Most other spread sectors delivered positive excess returns, leading the excess returns on the Bloomberg U.S. Aggregate Bond Index to fall to 0.00% during the period. Our underweight to SF MBS, and significant overweight to spread products, was a tailwind for the fund's performance.

Credit spreads tightened during the period. Corporate bond spreads tightened by 2bps, allowing the extra yield to shine and the sector to generate excess returns. Spreads also tightened by 8 bps in Commercial MBS and 1 bps in Asset Backed Securities. Our overweight to the combination of these assets benefited the portfolio during the period. However, our focus on less volatile and higher quality over lower quality credits offset some of this advantage as riskier securities provided the highest excess returns during the period.

The largest contributors during the period were the Fund's positions in higher coupon SF MBS, Regional Banks, and Utilities.

The index is primarily comprised of low coupon SF MBS. Our investments demonstrate a preference for middle and up in the coupon stack coupons. The middle-to-higher coupon SF MBS outperformed their lower coupon siblings meaningfully.

With thorough review, we have maintained our exposure to regional banks throughout the year. After the March scare, the bonds have continued to rebound as investors have better digested that the bank failures were largely due to mismanagement at the individual institutions. While the regional banks face challenges, we feel their exposure to duration remains manageable and within their core competency.

Utilities benefited the Fund's performance in two ways. First, Utilities outperformed their Industrial and Financial peers. We are overweight the Utility sector while underweight the Industrial sector. Additionally, our preference for secured Operating Company (OpCo) Utility debt also benefited the fund as these issues outperformed senior unsecured Holding Company (HoldCo) debt issued by the same parent companies. This seemed to be the one area of the market where investors demonstrated an appetite for owning higher quality corporate debt.

The largest detractors during the period were the Fund's positions in Sierra Pacific, Agency Multi-Family (MF) MBS, and Small Business Association Bonds (SBA).

For Sierra Pacific it was a matter of guilt by association. Sierra Pacific is owned by Berkshire Hathaway Energy, who also owns PacifiCorp. PacifiCorp is involved in a lawsuit related to forest fires in Oregon. A surprise judgement awarded the plaintiff's an outsized award, about 5times the size of the amounts paid to victims in the California wildfire cases. While there are many options open for PacifiCorp, the market has moved quickly against not only them, but all issuers within the Berkshire Hathaway Energy stack. Our Sierra Pacific bonds are senior secured and issued at the OpCo level. This structure exists for exactly this kind of reason, providing us confidence in the securities and issuer.

Along with their SF MBS cousins, Agency MF MBS was one of the only spread sectors to deliver negative excess returns during the period. Compared to SF MBS, these securities performed much better, but still generated -4bps of excess returns. While using them as a complementary position to SF MBS was beneficial, overall the positions generated a negative excess return, acting as a headwind to a Treasury alternative.

While SBA bonds continue to scream value to us, their spreads have not compressed as other high quality and U.S. Agency debt has. On a duration neutral basis, their price performance lags other U.S. Agency debt.

There were no significant changes to the Fund's positioning during the quarter. The largest change to positioning during the quarter was an increased allocation to SF MBS. The fund's allocation to these securities increased, as we continued to incrementally add exposure to the sector as the relative value of the securities has increased throughout the year.

The Fund's effective duration of 5.78 continues to be approximately matched to that of the benchmark, representing 98% of the benchmark's effective duration as of quarter end. The Fund entered the quarter at 97% of the benchmark's duration. Rates rose across the entirety of the yield curve. Changes in interest rates had little relative impact on returns. The portfolio is actively managed to be approximately duration and yield curve neutral, leading to little impact on returns.

Outlook and Conclusion

It is becoming increasingly obvious that the discussions and debate about how to handle the Fed's ongoing budgetary deficits is more than headline news, but a challenge for financial markets. The lack of progress and brinkmanship employed by Congress led to Fitch downgrading the U.S. Government's debt, matching a move taken by S&P in 2011 for similar reasons. This downgrade is not just a symbolic notation but also a reflection of the economic strains and fiscal imbalances, highlighting the government's struggle to maintain financial equilibrium. The budget deficits are expected to reach 5.3% of GDP in fiscal 2023, hit 6.1% in 2025, and grow to nearly 7% by 2033. This (7%) level has only occurred a handful of times in the United States' history, emphasizing the nature of the government's precarious fiscal position.

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Where this becomes a challenge for the market lies in the projections for new Treasury supply. The Treasury increased its net borrowing estimate to $1.0 trillion for third quarter and announced $850B of incremental borrowing for fourth quarter. These types of increases are expected throughout fiscal 2024. Moreover, these increases matched with the fact the Fed is actively allowing Treasuries to run-off means investors will have to absorb roughly $3.4 trillion in additional Treasury supply (from July'23-Sep'24). All else equal, this will push the weight of Treasuries within the Bloomberg U.S. Aggregate Bond Index from 41% to roughly 46%. The change here is profound, with the increased supply acting like a new instrument introduced into the market's symphony, altering its harmony and requiring recalibration.

Unfortunately, the government might not be alone. Consumers are also beginning to demonstrate financial strain. The excess savings accumulated during the COVID years have been eliminated for all but the top 20% of earners. At the same time, credit card balances have swelled. Though consumer spending has sustained itself, creating a pillar of support for the economy, this appears to be fueled by purchases made with debt. This development could add a new layer of economic vulnerability and uncertainty, which has been missing from the market's composition for several years.

Against these economic challenges, the portfolio is strategically positioned. The increase in Treasury supply, which will be reflected in the index and across passive strategies, aligns well with our overweight to spread products. In particular, our preferred high-quality spread bonds, such as those issued by the SBA. These bonds offer attractive spreads, consistent supply, and are equally backed by the U.S. government. Should the depletion of personal excess savings rear an ugly note, the largest vulnerabilities lie in riskier corners of the fixed income market. This includes sectors such as Energy, Leisure, and Retail. Our underweight position in these sectors acts as a protective shield from weaker U.S. households. We expect securities that are less maligned by budget deficits to provide a more stable bedrock of returns for the portfolio over the investment cycle.

For the reasons discussed above, we remain constructive about the relative performance of the fund. We have strong conviction in our SBA bonds and believe that corporate bond spreads have run quite tight. While corporate spreads may register as average, this is not true if you compare them to an alternative such as the yield on a Treasury bill. Should they widen, this will have the largest impact on the riskiest and most volatile issuers that we are underweight. Because of the pricing of SBA securities, we do not believe they would necessarily need to follow suit and widen. The same holds true for other government spread and AAA-rated spread debt. This is the type of debt that we build our overweight to spread products upon.

Fund Facts (As of 09/30/23)

Class	Inception Date	Symbol	CUSIP	Annual Fund Operating Expense Ratio* Total	Net
A Shares	08/16/10	**TCPAX**	89155T102	0.93%	0.76%
C Shares	08/01/11	**TCPCX**	89155T201	2.25%	1.51%
Y Shares	11/15/91	**TCPYX**	89155T409	0.52%	0.51%
INST Shares	08/01/11	**TCPNX**	89155T300	0.49%	0.41%
R6 Shares	11/22/21	**TIMPX**	89155T433	238.46%	0.37%
Total Fund Assets	**$519.6 Million**				

**Expense ratio is annualized. Data as of the current prospectus. Touchstone Advisors has contractually agreed to waive a portion of its fees and/or reimburse certain Fund expenses in order to limit certain annual fund operating expenses (excluding Acquired Fund Fees and Expenses "AFFE," and other expenses, if any) to 0.76% for Class A Shares, 1.51% for Class C Shares, 0.51% for Class Y Shares, 0.41% for Class INST Shares and 0.37% for Class R6 Shares. These expense limitations will remain in effect until at least 01/29/24.*

Share class availability differs by firm.

Annualized Total Returns** (As of 09/30/23)

	3Q23	YTD	1 Year	3 Year	5 Year	10 Year	Inception
Excluding Max Sales Charge							
A Shares	-2.97%	-1.39%	-0.20%	-5.34%	-0.40%	0.82%	4.21%
C Shares	-3.04%	-1.88%	-0.87%	-6.03%	-1.11%	0.23%	3.53%
Y Shares	-2.90%	-1.32%	0.05%	-5.13%	-0.15%	1.08%	4.47%
INST Shares	-2.88%	-1.13%	0.15%	-5.03%	-0.05%	1.19%	4.52%
R6 Shares	-2.87%	-1.21%	0.18%	-5.04%	-0.10%	1.11%	4.48%
Benchmark^	-3.23%	-1.21%	0.64%	-5.21%	0.10%	1.13%	4.57%
Including Max Sales Charge							
A Shares	-6.13%	-4.61%	-3.47%	-6.37%	-0.80%	0.34%	4.05%
C Shares	-4.01%	-2.84%	-1.84%	-6.03%	-1.11%	0.23%	3.53%

Max 3.25% sales charge for Class A Shares and 1% Contingent Deferred Sales Charge for Class C Shares held less than 1 year.

^Benchmark - Bloomberg U.S. Aggregate Bond Index[1]

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*****The performance presented for Class A, C, INST and R6 Shares combines the performance of an older class of shares (Y Shares) from the Fund's inception, 11/15/91, with the performance since the inception date of each share class.***

Please consider the investment objectives, risks, charges and expenses of the Fund carefully before investing. The prospectus and the summary prospectus contain this and other information about the Fund. To obtain a prospectus or a summary prospectus, contact your financial professional or download and/or request one at TouchstoneInvestments.com/resources or call Touchstone at 800.638.8194. Please read the prospectus and/or summary prospectus carefully before investing.

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[1]The Bloomberg U.S. Aggregate Bond Index is an unmanaged index comprised of U.S. investment grade, fixed rate bond market securities, including government, government agency, corporate and mortgage-backed securities between one and ten years.

The indexes mentioned are unmanaged statistical composites of stock market or bond market performance. Investing in an index is not possible. Unmanaged index returns do not reflect any fees, expenses or sales charges.

A Word About Risk

The Fund invests in fixed-income securities which can experience reduced liquidity during certain market events, lose their value as interest rates rise and are subject to credit risk which is the risk of deterioration in the financial condition of an issuer and/or general economic conditions that can cause the issuer to not make timely payments of principal and interest also causing the securities to decline in value and an investor can lose principal. When interest rates rise, the price of debt securities generally falls. Longer term securities are generally more volatile. The Fund invests in mortgage-backed securities and asset-backed securities which are subject to the risks of prepayment, defaults, changing interest rates and at times, the financial condition of the issuer. The Fund invests in investment grade debt securities which may be downgraded by a Nationally Recognized Statistical Rating Organization (NRSRO) to below investment grade status. The Fund invests in non-investment grade debt securities which are considered speculative with respect to the issuers' ability to make timely payments of interest and principal, may lack liquidity and has had more frequent and larger price changes than other debt securities. The Fund invests in U.S. government agency securities which are neither issued nor guaranteed by the U.S. Treasury and are not guaranteed against price movements due to changing interest rates. The sub-adviser considers ESG factors that it deems relevant or additive along with other material factors. The ESG criteria may cause the Fund to forgo opportunities to buy certain securities and/or gain exposure to certain industries, sectors, regions and countries. The Fund may be required to sell a security when it could be disadvantageous to do so. The Adviser engages a sub-adviser to make investment decisions for the Fund's portfolio; it may be unable to identify and retain a sub-adviser who achieves superior investment returns relative to other similar sub-advisers. Events in the U.S. and global financial markets, including actions taken to stimulate or stabilize economic growth may at times result in unusually high market volatility, which could negatively impact Fund performance and cause it to experience illiquidity, shareholder redemptions, or other potentially adverse effects. Banks and financial services companies could suffer losses if interest rates rise or economic conditions deteriorate. The Fund invests in municipal securities which may be affected by uncertainties in the municipal market related to legislation or litigation involving the taxation of municipal securities or the rights of municipal security holders in the event of bankruptcy and may not be able to meet their obligations. The Fund invests in mortgage dollar rolls which involve increased risk and volatility, as the securities the Fund is required to repurchase may be worth less than the securities that the Fund originally held. Current and future portfolio holdings are subject to change.

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