

Quarter highlights

- Security selection among agency mortgage-backed securities (MBS) was a drag on relative returns.
- Sector/industry allocation had a negative impact on relative results. With agency MBS rising strongly over the quarter, out-of-benchmark holdings of Treasuries, asset-backed securities and commercial mortgage-backed securities hindered returns on a relative basis.
- Overall duration and curve positioning also weighed on relative returns.

Market review

The U.S. bond market rebounded in the fourth quarter, boosted by the shift in narrative from the Federal Reserve (Fed) and further reductions in inflation. After several interest rate hikes in the first half of the year, the Fed held rates steady and moved to a more dovish stance. It ended the year indicating three possible rate cuts in 2024. Against this backdrop, all major U.S. fixed income sectors posted strong gains, and the Bloomberg U.S. Aggregate Index returned 6.82%.

Gross domestic product rose 4.9% on an annualized basis in the third quarter, a fifth consecutive quarterly GDP gain and the fastest growth since 2021. Consumer spending – which makes up around two-thirds of the U.S. economy – rose 3.1%. Meanwhile, inflation continued to improve without a significant increase in unemployment. The Consumer Price Index rose an annualized 3.4% in December, down from 6.5% at the end of 2022, while core inflation, which excludes food and energy, fell to a two-and-a-half year low of 3.9% from 5.7% the prior December.

U.S. Treasury yields fell across the curve in the fourth quarter. The 10-year Treasury ended the year at 3.88%, down 69 basis points (bps) over the fourth quarter, while the two-year Treasury fell 80 bps to end the year at 4.25%, slightly softening the inversion of the curve. With these moves, the Bloomberg U.S. Treasury Index rose 5.7% for the quarter, and the Bloomberg U.S. Treasury Inflation-Protected Securities Index returned 4.7%.

Credit markets were an area of strength for U.S. fixed income as markets priced in a soft landing and fundamentals and technicals were largely supportive. The Bloomberg U.S. Corporate Investment Grade Index returned 8.5% while the Bloomberg U.S. Corporate High Yield 2% Issuer Capped Index returned 7.2%. Investment-grade (AAA/Aaa and AA/Aa) and high-yield spreads narrowed by 22 bps and 71 bps, respectively. Issuance was slower than average for recent years in both markets. Elsewhere, municipal bonds and securitized debt also advanced. The Bloomberg U.S. Municipal Bond Index returned 7.9%, and the Bloomberg U.S. Mortgage-Backed Securities Index returned 7.5%.

Portfolio review

Security selection among agency mortgage-backed securities (MBS) was a drag on relative returns. The fund had larger positions in higher coupon bonds and small allocations to lower coupon bonds, which hurt.

Sector/industry allocation had a negative impact on relative results. With agency MBS rising strongly over the quarter, out-of-benchmark (Bloomberg U.S. Mortgage Backed Securities Index) holdings of Treasuries, asset-backed securities and commercial mortgage-backed securities hindered returns on a relative basis.

Overall duration and curve positioning also weighed on relative returns. During a quarter with significant volatility in fixed income markets, curve positioning detracted on a relative basis, although duration positioning had a positive impact. The fund had a longer duration than its benchmark when yields fell sharply in November and December.

Long-term perspective

The fund aims to provide income and preserve capital by investing primarily in mortgage-related securities that are guaranteed or sponsored by the U.S. government. The portfolio managers seek to deliver higher returns than those available on U.S. Treasury bonds, through holding a diversified mix of issuers, maturities and yields. Backed by Capital Group's extensive research, the portfolio managers invest with an eye to both current market yields and future market conditions.

Figures shown are past results and are not predictive of results in future periods.

Investments are not FDIC-insured, nor are they deposits of or guaranteed by a bank or any other entity, so they may lose value.

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Figures shown are past results and are not predictive of results in future periods. Current and future results may be lower or higher than those shown. Prices and returns will vary, so investors may lose money. Investing for short periods makes losses more likely. For current information and month-end results, visit capitalgroup.com.

Class F-2 share returns for periods ended 12/31/23

	Total returns (%)			Average annual total returns (%)			
	QTD	YTD	1 year	3 years	5 years	10 years	Fund lifetime (Since 11/1/10)
American Funds Mortgage Fund	6.76	4.00	4.00	-2.24	0.96	1.68	1.73
Bloomberg U.S. Mortgage-Backed Securities Index	7.48	5.05	5.05	-2.86	0.25	1.38	–

Fund expense ratio: 0.40%†

†The expense ratio is as of the fund's prospectus available at the time of publication.

Investors should carefully consider investment objectives, risks, charges and expenses. This and other important information is contained in the fund prospectuses and summary prospectuses, which can be obtained from a financial professional and should be read carefully before investing.

This content, developed by Capital Group, home of American Funds, should not be used as a primary basis for investment decisions and is not intended to serve as impartial investment or fiduciary advice.

The return of principal for bond funds and for funds with significant underlying bond holdings is not guaranteed. Fund shares are subject to the same interest rate, inflation and credit risks associated with the underlying bond holdings. Investments in mortgage-related securities involve additional risks, such as prepayment risk, as more fully described in the prospectus. The use of derivatives involves a variety of risks, which may be different from, or greater than, the risks associated with investing in traditional securities, such as stocks and bonds.

Portfolios are managed, so holdings will change. Certain fixed income and/or cash and equivalents holdings may be held through mutual funds managed by the investment adviser or its affiliates that are not offered to the public.

Investment results assume all distributions are reinvested and reflect applicable fees and expenses. When applicable, results reflect fee waivers and/or expense reimbursements, without which they would have been lower. Refer to capitalgroup.com for more information.

Class F-2 shares were first offered on August 1, 2008. Class F-2 share results prior to the date of first sale are hypothetical based on the original share class results without a sales charge, adjusted for typical estimated expenses. Refer to capitalgroup.com for more information on specific expense adjustments and the actual dates of first sale.

Bond ratings, which typically range from AAA/Aaa (highest) to D (lowest), are assigned by credit rating agencies such as Standard & Poor's, Moody's and/or Fitch, as an indication of an issuer's creditworthiness.

Bloomberg U.S. Aggregate Index represents the U.S. investment-grade fixed-rate bond market. **Bloomberg U.S. Corporate High Yield 2% Issuer Capped Index** covers the universe of fixed-rate, non-investment-grade debt. The index limits the maximum exposure of any one issuer to 2%.

Bloomberg U.S. Treasury Index includes public obligations of the U.S. Treasury, i.e. U.S. government bonds. Certain Treasury bills are excluded by a maturity constraint. In addition, certain special issues, such as state and local government series bonds (SLGs), as well as U.S. Treasury TIPS, are excluded. **Bloomberg U.S. Treasury Inflation-Protected Securities (TIPS) Index** consists of investment-grade, fixed-rate, publicly placed, dollar-denominated and non-convertible inflation-protected securities issued by the U.S. Treasury that have at least one year remaining to maturity and have at least \$250 million par amount outstanding. **Bloomberg U.S. Mortgage Backed Securities Index** is a market-value-weighted index that covers the mortgage-backed pass-through securities of Ginnie Mae (GNMA), Fannie Mae (FNMA), and Freddie Mac (FHLMC). **Bloomberg U.S. Corporate Investment Grade Index** represents the universe of investment-grade, publicly issued U.S. corporate and specified foreign debentures and secured notes that meet the specified maturity, liquidity and quality requirements.

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Consumer Price Index (CPI) is a measure of the average change over time in the prices paid by urban consumers for a market basket of consumer goods and services. Widely used as a measure of inflation, the CPI is computed by the U.S. Department of Labor, Bureau of Labor Statistics. **Core inflation (Core CPI)** is a measure of price changes faced by urban consumers, excluding food and energy. Core CPI is computerized by the U.S. Department of Labor, Bureau of Labor Statistics. **Bloomberg U.S. Municipal Bond Index** is a market-value-weighted index designed to represent the long-term investment-grade tax-exempt bond market. This index is unmanaged, and its results include reinvested distributions but do not reflect the effect of sales charges, commissions, account fees, expenses or U.S. federal income taxes.

The market index is unmanaged and, therefore, has no expenses. Investors cannot invest directly in an index. There have been periods when the fund has lagged the index.

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