Market Neutral Income Strategy Quarterly Commentary

CALAMOS INVESTMENTS

Market Overview

In the second quarter, a strong labor market, an averted debt ceiling crisis, moderating inflation data, and a pause in the Federal Reserve's interest-rate tightening all supported the convertible and equity market rally. The ICE BofA All US Convertibles Index (VXA0) returned 4.63% in the second quarter and participated in the broader equity market's advance as measured by the 8.74% return of the S&P 500 Index. Market leadership was narrow as evidenced by the S&P 500 Equal Weighted Index return of 3.99% and given that the top 10 S&P 500 names contributed roughly 6.5% of that 8.74% index result. The underlying stocks of the convertible market were up 7.88% in the quarter as reported by ICE BofA.

The US Federal Reserve raised its overnight federal funds rate target by 25 basis points during the quarter with the top federal funds rate rising to 5.25% from 5.00%. Longer-term rates also increased as the yield of the 10-year US Treasury bond increased from 3.48% at the beginning of the quarter to 3.84% by quarter's end. The average global high-yield credit spread narrowed 56 basis points quarter over quarter to 457 basis points over government securities, according to Bloomberg.

Performance Review

The strategy returned 2.96% (gross of fees) and 2.80% (net of fees) in the quarter, strongly outperforming the Bloomberg US Government/Credit Bond Index return of -0.93%.

Hedged Equity Performance Drivers

Equity Performance: As the S&P 500 Index advanced 8.74% during the quarter, the portfolio's equity sleeve increased with the market and supported the quarterly result.

Option Positioning: The current skew in the options market has been conducive to utilizing call and put spreads. Although we are near the top end of our call write range, we have also utilized short-dated long calls to provide an additional upside. In addition, we continue to layer in put spreads over and above our typical minimum level of notional long puts as a means of mitigating the downside. As the S&P 500 Index moved higher, the long calls allowed us to capture a bit more upside without incurring additional risk.

Interest Rates: Higher interest rates benefited the hedged equity strategy given that the portfolio earns a wider spread on calls written versus long puts. Because we generally sell longer-dated calls and buy shorter-dated puts, the portfolio receives a higher premium from the time value differential of selling longer-duration calls and buying shorter-dated puts.

Volatility: The Cboe Volatility Index (VIX) declined to 13.59 from its 18.70 value at the beginning of the quarter. When viewed in isolation, declining volatility means that the portfolio's options contracts decrease in value because they have a lower probability of reaching a strike price. Because the hedged equity strategy is net short options, the declining volatility supported the strategy's quarterly result.

Option Skew: Option skew widened during the quarter. The Credit Suisse Fear Barometer (CSFB) provides a useful statistic for evaluating option skew. Using premium captured by writing 90-day S&P

500 Index call options that are 10% out of the money, the CSFB value is determined by understanding how far out of the money 90-day index puts are purchased to construct a zero-cost collar around the S&P 500. The higher the index value, the more skew is evident in the options market. The CSFB finished the quarter at 27.84, considerably higher than where it started at 19.30 and above its long-term average of 21.35. This widening skew has made the use of call and put spreads more lucrative.

Convertible Arbitrage Performance Drivers

Interest Rate Environment: In a rising-rate environment, convertible arbitrage benefited from higher coupons on new convertible issues and higher overnight money received from the short stock proceeds. Additionally, narrower credit spreads supported the value of the convertibles' bond component.

Convertible Valuations: Convertible valuations cheapened during the quarter. The theoretical value of a convertible can be determined by the sum of its bond and option components. US convertibles began the quarter trading at an average 0.09% discount to this theoretical value and ended at a 0.46% discount according to ICE BofA. Cheapening convertible valuations slightly reduced the long convertibles' bond value.

Volatility: As previously discussed, the market saw declining market volatility during the quarter. Declining volatility is generally a headwind to convertible arbitrage because it can lead to fewer trade rebalance opportunities. The significant drawdown of the equity market in 2022 provided a more bond-like convertible market with fewer gamma opportunities. At the same time, these more bond-like convertibles have provided attractive yield to maturity opportunities.

New Convertible Issuance: Convertible issuance continued to improve with $19.5 billion raised globally in the second quarter. US issuance totaled $14.3 billion, Europe brought $2.0 billion to market, Asia launched $2.5 billion, and Japan introduced $0.8 billion. Moreover, these new convertible issues are being brought to market with terms that include higher coupons and lower conversion premiums, which present attractive arbitrage opportunities in our view.

Positioning and Portfolio Changes

We actively manage allocations to the different strategies based on our view of market conditions and relative opportunities. The portfolio's current allocation to the arbitrage strategy is 53% with 47% in the hedged equity strategy. At the start of the year, the portfolio's allocation to the arbitrage strategy was 51% with 49% allocated to the hedged equity strategy.

Within the arbitrage strategy, we have the flexibility to utilize different strategies, including convertible arbitrage, merger arbitrage and special purpose acquisition company (SPAC) arbitrage. We continue to like the opportunity in convertible arbitrage the most, and the portfolio's allocation to this strategy grew from 39% at the start of the year to 46% by June 30. We expect to continue adding to convertible arbitrage, particularly if we see the attractive new convertible issuance that we anticipate.

We funded the increased allocation to convertible arbitrage primarily through a reduction of our SPAC book. SPACs are now 3% of the portfolio, after peaking at almost 10%. While we have sold a few SPACs, the lower allocation is primarily the result of the natural runoff of SPACs issued in 2021 with terms of two years or less.

A principal driver for our bullishness in convertible arbitrage is our heightened return expectations of the rise in overnight interest rates. Convertible arbitrage returns have historically been correlated with overnight rates, partly because of the direct linkage of the rebate the portfolio receives on its short stock positions, which is directly tied to the fed funds rate. Although returns don't necessarily go up tick-for-tick with rates, we expect a meaningful tailwind in 2023 and beyond.

We would buy new SPACs if we saw terms similar to those we bought in 2021. Then SPACs were profitable for the portfolio due to limited volatility, and our allocation served the portfolio well over the past few years. However, the SPAC new issue market has been quiet since late 2021. The gating factor for SPAC issuance is sponsors' willingness to commit capital in exchange for the opportunity to multiply their investment if they can get a deal across the finish line. This tends to be a bull market trade, and we are not seeing those levels of animal spirits in the small-cap space where most "de-SPAC-ed" equities reside.

The slow grind upward of the S&P 500 Index during the quarter also benefited the hedged equity side of the portfolio. Call volatility has come in a bit recently, but it has generally been higher this year, which has allowed us to generate more income from the options strategy while retaining a significant degree of downside risk mitigation. Higher interest rates also have flowed through to the hedged equity strategy in the form of higher call prices and lower put prices, making our collar strategy more attractive. Also, a relative bid to tail risk has made put spreads an attractive tool for layering in extra downside risk mitigation.

Special Purpose Acquisition Company (SPAC) Arbitrage Positioning

The allocation to Special Purpose Acquisition Company (SPAC) arbitrage has decreased as existing SPACs reach their expiration dates while new SPAC issuance has waned.

During the second quarter, just six SPACs priced IPOs with a market value of $1.0 billion. Recent market volatility and small-cap equity valuations have hindered IPO activity. All told, 51 SPACs have filed registration statements, which represents another $5.7 billion in potential opportunity should these registered issues IPO in the future. (Source: SPACAnalytics.com).

The trend of slowing SPAC issuance, fewer deal announcements and increased redemptions portends a shrinking SPAC market. We are using SPAC arbitrage opportunistically and still see value in a positive yield to expiration in our SPAC arbitrage portfolio. Additionally, as overnight interest rates have moved higher, the SPACs' cash in trust is earning an attractive yield.

- As short interest rates moved higher, the interest earned on the cash in trust in the portfolio increased.
- We purchased the bulk of the MNI SPACs in the portfolio at or below the $10 IPO price.
- The portfolio's SPAC holdings are well diversified with 62 SPACs held (versus 157 SPACs held on 3/31/23).

Merger Arbitrage Positioning

We expect merger arbitrage to provide lower volatility and lower correlation to equity markets, along with a high probability of a positive return over a long time horizon in most market environments. The merger arbitrage holdings provide a complementary risk profile to the portfolio, with a beta to the S&P 500 somewhere between convertible arbitrage and hedged equity strategies. The current merger arbitrage holdings consist of 28 long equities and convertibles (three more than 3/31/22).

Outlook

The market continues to experience volatility stemming from ongoing investor concerns regarding ongoing inflation, changing interest rates, deposit risk in the banking sector, perceptions of the Federal Reserve's ability to execute a soft landing, and the prospects for a recession. Elevated volatility creates opportunities for the portfolio to rebalance its hedges, which may create value for investors.

The strategy demonstrates its value in asset allocation by providing a bond-like return with bond-like standard deviation without completely embracing bond-like risk exposure. While the Calamos Market Neutral Income Strategy has done well in rising interest rate environments, it doesn't need rising rates to provide relative value. Because rising interest rates have increased nominal yields in the bond market and have made bonds more attractive in the eyes of investors, it should be noted that rising interest rates are also supportive of the portfolio's total return. Higher interest rates should provide higher coupons on newly issued convertibles, a higher short-interest rebate, higher potential option premium capture, and a higher yield on the cash-in-trust portion of the SPAC arbitrage strategy.

For additional information please visit the strategy's profile page:
https://www.calamos.com/strategies/market-neutral-income/

CALAMOS MARKET NEUTRAL INCOME STRATEGY RETURNS (%)

	QTR	1-YEAR	3-YEAR	5-YEAR	10-YEAR	SINCE INCEPTION (1/91)
Calamos Market Neutral Income Composite						
Return Gross	2.96	10.00	4.55	4.61	4.83	7.39
Return Net of Fees	2.80	9.29	3.87	3.92	4.13	6.63
Bloomberg US Govt./Credit Bond Index	-0.93	-0.70	-4.11	1.04	1.66	5.06
Bloomberg Short Treasury 1-3 Month Index	1.23	3.73	1.31	1.54	0.96	2.51
S&P 500 Index	8.74	19.59	14.60	12.31	12.86	10.54

Source: Calamos Advisors LLC
Past performance is no guarantee of future results.

Past performance does not guarantee or indicate future results. Current performance may be lower or higher than the performance quoted. Portfolios are managed according to their respective strategies which may differ significantly in terms of security holdings, industry weightings, and asset allocation from those of the benchmark(s). Portfolio performance, characteristics and volatility may differ from the benchmark(s) shown.

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The information portrayed is for the Calamos Market Neutral Income Strategy. Representative holdings and portfolio characteristics are specific only to the portfolio shown at that point in time. Other portfolios will vary in composition, characteristics, and will experience different investment results. The representative portfolio shown has been selected by the advisor based on account characteristics that the advisor feels accurately represents the investment strategy as a whole. The opinions referenced are as of the date of publication and are subject to change due to changes in the market or economic conditions and may not necessarily come to pass. Information contained herein is for informational purposes only and should not be considered investment advice.

The information provided in this report should not be considered a recommendation to purchase or sell any industry, sector or particular security. There is no assurance that any industry, sector or security discussed herein will remain in a client's account at the time of reading this report or that industry, sectors or securities sold have not been repurchased. The industries, sectors, or securities discussed herein do not represent a client's entire account and in the aggregate may represent only a small percentage of an account's holdings.

It should not be assumed that any of the securities transactions or holdings discussed were or will prove to be profitable, or that the investment recommendations or decisions we make in the future will be profitable or will equal the investment performance of the securities discussed herein.

Returns and Risk/Reward statistics presented reflect the **Calamos Market Neutral Income Composite**, which is an actively managed "market neutral" composite that seeks to achieve maximum current income while maintaining a low correlation to the fluctuations of the US equity market as a whole. The Composite was created November 15, 2013, calculated with an inception date of January 1, 1991. The Composite results include all fully discretionary accounts, including those no longer with the Firm.

Alternative Strategy Risks: Alternative investment strategies are speculative and entail substantial risks. The investment practices of these strategies could result in substantial losses. There can be no assurance that the alternative strategies will be profitable or the investment objective will be achieved.

Convertible Securities Risks: The value of a convertible security is influenced by changes in interest rates, with investment value declining as interest rates increase and increasing as interest rates decline. The credit standing of the issuer and other factors also may have an effect on the convertible security's investment value.

Equity Securities Risk: The securities markets are volatile, and the market prices of the securities may decline generally. The price of equity securities fluctuates based on changes in a company's financial condition and overall market and economic conditions. If the market prices of the securities owned fall, the value of your investment will decline.

Short Positions Risks: A short sale of an instrument entails the theoretical risk of an unlimited increase in the market price of that instrument, which can in turn result in significant losses to a client. Purchasing instruments to close out a short position in such instruments can itself cause the price of the instrument to rise further, increasing losses. Furthermore, a client may be forced to close out a short position in a security prematurely if a lender of such security demands the return of the security sold short.

Derivatives Risks: Options, futures and other derivatives involve risks and are not suitable for everyone. Such trading can be speculative in nature and carry substantial risk of loss, including the loss of principal.

Alpha is the extra return of a portfolio due to non-market factors. **Beta** is a historic measure of a portfolio's relative volatility, which is one of the measures of risk; a beta of 0.5 reflects half the market's volatility as represented by the strategy's primary benchmark, while a beta of 2 reflects twice the volatility. **Gamma** is the rate of change of an option's delta with respect to the change in price of an underlying asset. Higher gamma indicates higher price volatility for the option. **Skew** describes asymmetry from the normal distribution in a set of statistical data. Standard deviation is a statistical measure of the historical volatility of a mutual fund or portfolio. The Bloomberg US Government/Credit Index comprises long-term government and investment-grade corporate debt securities and is generally considered representative of the performance of the broad US bond market. Unlike convertible bonds, US Treasury bills are backed by the full faith and credit of the US government and offer a guarantee as to the timely repayment of principal and interest. The ICE BofA All US Convertibles Index (VXA0) measures the return of all US convertibles. Source: ICE Data Indices, LLC, used with permission. ICE permits use of the ICE BofA indices and related data on an 'as is' basis, makes no warranties regarding same, does not guarantee the suitability, quality, accuracy, timeliness, and/or completeness of the ICE BofA Indices or data included in, related to, or derived therefrom, assumes no liability in connection with the use of the foregoing and does not sponsor, endorse or recommend Calamos Advisors LLC or any of its products or services. The **Cboe Volatility Index** or **VIX** (based on its Cboe ticker symbol) shows the market's expectation of 30-day volatility. It is constructed using the implied volatilities of a wide range of S&P 500 Index options. The **Bloomberg Short Treasury 1-3 Month Index** is generally considered representative of the performance of short-term money market investments and is provided to show how the Fund's performance compares to public obligations of the US Treasury with maturities of 1-3 months. The **Credit Suisse Fear Barometer** essentially tracks the willingness of investors to pay up for downside protection with collar trades on the S&P 500 Index. Delta is the ratio of change in price of an option to the change in price of the underlying asset. The **S&P 500 Index** is generally considered representative of the US stock market. **Sharpe ratio** is a measure of the excess return per unit of risk taken by an investment strategy. Unmanaged index returns assume reinvestment of any and all distributions and do not reflect any fees, expenses or sales charges. Investors cannot invest directly in an index.

Fees include the investment advisory fee charged by Calamos Advisors LLC. Returns greater than 12 months are annualized. Sources: Calamos Advisors LLC.

Average annual total return measures net investment income and capital gain or loss from portfolio investments as an annualized average assuming reinvestment of dividends and capital gains distributions.

Calamos Advisors LLC is a federally registered investment advisor. Form ADV Part 2A, which provides background information about the firm and its business practices, is available upon written request to:

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