

Fund Manager Commentary
William Blair Income Fund

Fund Performance

The William Blair Income Fund (Class N shares) outperformed its benchmark, the Bloomberg Barclays Intermediate Government/Credit Index, during the third quarter.

There were some factors that detracted from the Fund's performance during the quarter. The Fund's positioning in agency mortgage-backed securities (MBS) underperformed comparable duration Treasuries during the quarter. The Fund emphasized higher-coupon segments of the market and is actively avoiding the lower-coupon segments that the FOMC targets when purchasing agency MBS. The Fund held a position in corporate bonds issued by Kroger that underperformed comparable-duration Treasuries and hindered results.

A couple of factors contributed to the Fund's performance relative to the Index during the quarter. Sector allocation impacted results favorably, as the Fund was underweight to fixed-rate Treasuries and overweight to corporate bonds on a risk-adjusted basis. Security selection of corporate bonds contributed to results during the quarter, as positions in bonds issued by ConocoPhillips, Synchrony Financial, BRF SA, Fibria Cellulose, and Vale were additive to performance.

Market Review

Investment-grade bonds generated gains during the third quarter of 2017, as interest rates were little changed during the quarter and risk spreads of corporate and agency mortgage-backed securities narrowed. The Bloomberg Barclays U.S. Aggregate Bond Index returned +0.85% during the quarter,

¹ Listed holdings are presented to illustrate examples of the securities that the Fund has bought and do not represent all of the Fund's holdings or future investments. Information about the Fund's holdings should not be considered investment advice. There is no guarantee that the Fund will continue to hold any one particular security or stay invested in any one particular sector. Holdings are subject to change at any time and are as of the date shown above. Top ten holdings are shown as a percentage of total net assets.

Top 10 Holdings¹ as of 9/30/17

Company Name	% of Fund
Fannie Mae Pool, 4.00% due - 2/1/29	9.7%
Fannie Mae Pool, 5.50% due - 12/1/41	6.5%
Fannie Mae Pool, 6.00% due - 11/1/24	6.2%
Freddie Mac Gold Pool, 4.00% due - 11/1/25	3.5%
Fannie Mae Pool, 6.00% due - 1/1/42	2.6%
United States Treasury Inflation Indexed Bonds, 1.13% due - 1/15/21	2.3%
Fannie Mae Pool, 5.50% due - 11/1/33	2.0%
Freddie Mac Gold Pool, 5.50% due - 11/1/38	1.5%
Freddie Mac Gold Pool, 5.00% due - 6/1/41	1.5%
Freddie Mac Gold Pool, 6.00% due - 10/1/39	1.3%
Total Top 10	37.1%

with all major market segments enjoying positive results.

The Federal Open Market Committee (FOMC) met twice during the third quarter, and while the FOMC made no changes to the target range of the federal funds rate, the FOMC communicated its plans to reduce the size of its balance sheet. An important feature of these plans involves a monthly cap on the maximum amount the FOMC will permit the balance sheet to reduce; principal and interest payments in excess of that monthly cap will continue to be reinvested into Treasury and agency mortgage-backed securities. The FOMC released a schedule of the monthly cap of balance sheet reductions. From October 2017 – December 2017, the total is \$10 billion per month: 60% of that amount is the maximum for Treasury securities and 40% of that amount is the maximum for agency securities (agency debt plus agency MBS). This monthly cap rises to \$20 billion per month during January 2018 – March 2018, \$30 billion per month during April 2018 – June 2018, \$40 billion per month during July 2018 –

September 2018, and \$50 billion per month after September 2018, with the cap for Treasury securities and agency securities at 60% and 40%, respectively, of the total cap amount for each time period.

As a result of the FOMC's well-coordinated plans for balance sheet reduction, interest rate volatility has been low. The FOMC will still be purchasing longer-term securities and, perhaps more importantly, will not be selling securities into the market. The fed funds futures market carried an implied probability that the FOMC will increase the federal funds rate target range by 25 basis points at its December 2017 meeting. The FOMC has hiked the target range by 25 basis points twice thus far in 2017, and both instances have been well-absorbed by the market due to the benign volatility conditions and the FOMC's ongoing purchases of longer-term instruments.

Longer-term Treasury rates changed little quarter-over-quarter in spite of the Fed's plans to raise short-term rates and reduce its balance sheet. Longer-term interest rates remained at levels above those that prevailed before the U.S. presidential elections of 2016. Treasury Inflation-Protected Securities (TIPS) outperformed similar-maturity, fixed-rate Treasury notes and bonds as market-implied inflation expectations rose.

Agency mortgage-backed securities generated positive total returns and experienced narrowing risk spreads during the third quarter. The best-performing segments of the market were lower-coupon 30-year pools that the FOMC has targeted in "FedTrade" to suppress mortgage rates, such as 30-year 3.0%, 3.5%, and 4.0%, as the market took comfort in the fact that the FOMC's plans for balance sheet reduction continue to involve purchases of agency MBS, at least for the time being, and no selling of securities.

Corporate bonds have generated strong returns during the quarter, both total returns and duration-adjusted returns. Corporate bonds of all credit qualities, tenors, and sectors produced gains. Risk spreads remain at lower levels, and the new issue market is robust and open for companies to access capital in the bond markets.

Outlook

We believe that the Federal Open Market Committee (FOMC) will continue to raise the federal funds rate at a measured pace over the next 12 months. The U.S. economy is growing; forecasters predict a real GDP growth rate of approximately 2.0%-2.5% during 2017. In addition, the U.S. labor market is adding jobs and the unemployment rate is at 4.3%. However, recent indicators of inflation have revealed slower-than-desired inflation. Wage inflation has tapered after strong readings throughout 2016. Macroeconomic theory predicts that a robust labor market creates wage inflation, which in turn spurs broader inflation. We believe that the FOMC will raise rates so long as inflationary pressures do not deteriorate.

We believe that the FOMC's plans to reduce the size of the Fed's balance sheet will be executed with little disruption to the markets. We believe this is attributable, in part, to strong communication efforts, adequate advance notice, and the absence of security sales to reduce the balance sheet. In addition, remarks by FOMC members indicate that the FOMC will err on the side of conservatism, with the permissible reduction being relatively small in scale and subject to a monthly cap.

However, we believe the lower-coupon MBS that was purchased by the Fed will underperform higher-coupon alternatives when the FOMC ends their campaign of purchasing agency MBS.

U.S. Treasury Inflation-Protected Securities (TIPS) have market-implied breakeven inflation rates that are below the FOMC's stated target range of 2.0%-2.5%. We believe TIPS are an attractive alternative to fixed-rate Treasuries to mitigate the effects of rising rates driven by accelerating inflationary pressures.

We believe that spread sectors are poised to lead the market over the longer term. Corporate risk premiums are at levels near their longer-term averages, and risk premiums of higher-coupon segments of the agency MBS market remain attractive. In addition, we believe Treasuries and lower-coupon MBS are likely to struggle as the FOMC tightens the fed funds rate and embarks on reducing the size of the Fed's balance sheet.

We believe that higher-coupon segments (coupon rates of 5.0% and above for 30-year) of the agency MBS market offer compelling value. These segments of the agency MBS market offer attractive spreads and a defensive duration profile. The key risk of these securities is that the underlying borrowers are in-the-money to refinance their loan. We believe this risk can be mitigated by focusing on pools comprised of borrowers that do not have the economic incentive to refinance their loans: low-loan balance pools.

We believe that opportunities remain in the corporate bond market despite risk spreads near their longer-term averages. We remain concerned about company-specific risks, including shareholder-friendly activities such as leveraged finance mergers and acquisitions, large share repurchases, and special dividends. Importantly, we do not believe the market will enter a period of excessive LBO activity.

INVESTMENT PERFORMANCE % (as of 09/30/17)

	QTR	YTD	1Y	3Y	5Y	10Y
Class I (SI: 10/01/99)	0.59	1.64	0.80	1.87	1.49	3.24
Class N (SI: 10/01/90)	0.64	1.58	0.59	1.63	1.28	3.02
Bloomberg Barclays Intermediate Govt./ Credit Bond Index	0.60	2.34	0.23	2.13	1.61	3.64

EXPENSE RATIOS (%)

	Gross Expense
Class I	0.57
Class N	0.79

Expenses shown are as of the most recent prospectus.

Performance cited represents past performance. Past performance does not guarantee future results and current performance may be lower or higher than the data quoted. Returns shown assume reinvestment of dividends and capital gains. Investment returns and principal will fluctuate with market and economic conditions and you may have a gain or loss when you sell shares. For the most current month-end performance information, please call +1 800 742 7272, or visit our Web site at www.williamblairfunds.com. Class N shares are available to the general public without a sales load. Class I shares are available only to investors who meet certain eligibility requirements.

DISCLOSURE

The Fund's returns will vary, and you could lose money by investing in the Fund. As interest rates rise, bond prices will fall and bond funds become more volatile. The Fund is subject to credit risk. The Fund's net asset value and total return may be adversely affected by the inability of the issuers of the Fund's securities to make interest payments or payment at maturity. The Fund's investments in obligations issued or guaranteed by U.S. Government agencies or instrumentalities may not be backed by the full faith and credit of the United States and may differ in the degree of support provided by the U.S. Government. The Fund is also subject to interest rate and foreign investments risk. Foreign investments often involve additional risks, including political instability, differences in financial reporting standards and less stringent regulation of securities markets. Rule 144A securities are not registered for resale in the general securities market and may be classified as illiquid. It may not be possible to sell or otherwise dispose of illiquid securities both at the price and within a time period deemed desirable by the Fund. Investments with longer maturities, which typically provide higher yields than securities with shorter maturities, may subject the Fund to increased price changes resulting from market yield fluctuations. The Fund's investments in collateralized mortgage obligations are subject to prepayment and extension risk. Prepayment of high interest rate mortgage-backed securities during times of declining interest rates will tend to lower the return of the Fund and may even result in losses to the Fund if the prepaid securities were acquired at a premium. Slower prepayments during periods of rising interest rates may increase the duration of the Fund's mortgage-backed securities and asset-backed securities and reduce their value.

The Bloomberg Barclays Intermediate Government/Credit Bond Index indicates broad intermediate government/corporate bond market performance. The Index is unmanaged, does not incur fees or expenses, and cannot be invested in directly.

This content is for informational and educational purposes only and not intended as investment advice or a recommendation to buy or sell any security. Investment advice and recommendations can be provided only after careful consideration of an investor's objectives, guidelines, and restrictions.

Please carefully consider the Fund's investment objectives, risks, charges, and expenses before investing. This and other information is contained in the Fund's prospectus, which you may obtain by calling 1-800-742-7272. Read it carefully before you invest or send money. Investing involves the risk of loss.

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