Full year 2016 summary

What worked:

- Emerging market exposure
- Bank loan and high yield exposure
- Mortgage-backed securities (MBS) collateralized mortgage obligation (CMO) investment selection.

What did not work:

- Energy exposure
- Investment grade corporate curve exposure.

The following is a detailed review of Delaware Diversified Income Fund's performance for the full year 2016 relative to its benchmark, the Bloomberg Barclays U.S. Aggregate Index.

Delaware Diversified Income Fund Institutional Class shares returned 3.94% and Class A shares at net asset value returned 3.56% for the full year 2016 (4.54% before expenses), outperforming its benchmark, the Bloomberg Barclays U.S. Aggregate Index by 129 and 91 basis points (189 basis points before expenses). The Fund outperformed the average return of the Morningstar Intermediate-Term Bond Fund Category by 71 basis points for the Fund's Institutional Class shares and by 33 basis points for its Class A shares. A bulleted curve position emphasizing the 5- to 10-year part of the curve, a lack of energy exposure, and interest rate sensitivity in investment grade corporate bonds detracted from performance for the year. Investments in emerging market bonds, bank loans, and traditional high yield bonds added to index relative performance. The security selection in MBS investments also helped the portfolio outperform the Bloomberg Barclays U.S. Aggregate Index.

Three important events shaped capital market movements in 2016. Early in the year there was a significant risk-off environment that followed 2015's selloff in energy and commodities. The threat of U.S. Federal Reserve interest rate hikes (the Fed had raised rates by 0.25 percentage points in December 2015) had ignited a strong U.S. dollar move and a commodities bear market. Additionally, credit markets were rattled by strong supply, equity-friendly activity (at the expense of bond investors), and credit issues in the high yield markets. All of this volatility was met with significant monetary easing from the European Central Bank (ECB) (adding the purchase of corporate bonds into its quantitative easing measures). The Fed also decided to postpone interest rate hikes. The Organization of the Petroleum Exporting Countries (OPEC) nations also joined forces to talk about production cuts. These events stopped the early year price declines, and opened up capital markets for challenged entities. Significant rallies in the capital markets, especially in energy- and commodity-related names ensued.

The second important event for 2016 was the Brexit vote in the United Kingdom. The threat of exiting the European Union by such an important member reignited volatility in the capital markets. The actual vote to leave was met with monetary easing by the Bank of England and further reinforced the fact that central banks were sensitive to capital market declines. Risk premiums declined further as capital market participants gained more confidence in their investment selections.

Key votes in two countries dominated market environments in the fourth quarter. Italy held a referendum on a government restructuring. The outcome saw an Italian population cast a "no" vote for the referendum. The vote became more of a "no confidence" opinion on Italian Prime Minister Matteo Renzi than an opinion on government structure. The resulting political uncertainty — Renzi resigned and fringe party influence increased slightly — had a surprisingly small effect on global markets. The U.S. presidential and congressional elections had a far higher effect on markets in the fourth quarter. The win by Donald Trump and Republicans' ability to hang on to majorities in Congress surprised many capital market participants. The initial reaction to this event was a selloff in equity and other risk markets. When investors soon revised their views to encompass a more business-friendly environment and possible fiscal stimulus, equity and credit markets started to rally strongly.

The Fund has an income advantage over the index due to its exposure to the corporate and structured product sectors. At year end this income advantage was 114 basis points (before expenses). Central bank actions to keep rates low and to buy corporate bonds had set a favorable environment for exposure away from U.S. Treasury investments in 2016. We expect to keep this credit exposure and income advantage in the Fund in the near term.

The Fund's emerging market exposure of approximately 7% had strong returns for the full year 2016 (9.75%) and contributed 66 basis points to index-relative returns (return references before expenses). A key decision to add to quasi-sovereign, oil sensitive names aided performance for the year. The Fund's Mexico exposure after the U.S. election took some performance back as the country was a favorite target of Donald Trump's trade promises. The current emerging market exposure consists of 37% in sovereign investments and 63% in corporate and quasi-sovereign entities. Energy, food and beverage, and communications are prominent sector holdings. Local currency exposure (17% of the emerging markets subportfolio) featured the Mexican peso, Polish zloty, Indonesian rupiah, and others. As of this writing, we are currently taking down the Fund's Mexican peso exposure for some risk management. Approximately 40% of the current emerging markets subportfolio consists of below-investment-grade securities.

Investments in the bank loan sector (10% of the Fund at year end) contributed to the Fund's return relative to the Bloomberg Barclays U.S. Aggregate Index for the year. The Fund's investment in bank loans had a return of 8.7% (before expenses), which stood in sharp contrast to the nominal return of the U.S. Aggregate Index (2.65%). Bank loans were responsible for 61 basis points of index-relative gains (before expenses). We increased the Fund's bank loan exposure by 1.5% (on the whole portfolio). Risk premiums declined and many investors are excited that the floating nature of these coupons can restart as the three-month London interbank offered rate (Libor) rises above 1.0%. The Fund's bank loan subportfolio underperformed the S&P/LSTA Leveraged Loan Index return of 10.2%.

Investments in traditional high yield bonds (8.5% of the overall portfolio at year end) returned 7.3% (before expenses). This subportfolio underperformed the BofA Merrill Lynch BB-B U.S. High Yield Index, which had a return of 14.7%. Important sector exposures for the high yield investments were media companies, healthcare companies, technology companies, and the leisure area. The subportfolio had an underweight to both the energy and mining sectors, which saw significant returns in 2016.

We increased the Fund's investment grade corporate exposure in a significant way in 2016 after the early central bank and OPEC measures. Exposure went from 24% at the beginning of the year to 40% at year end. The contribution to duration went from 95% to 161%. The liquidity challenges and volatile capital markets indicators made us proceed with caution. Energy and commodity assets were added slowly and with particular attention to the company's ability to operate over a wide range of oil prices. Investment grade bonds in this sector (ex emerging markets) increased by 1.2% and included integrated energy, independent producers, and midstream or pipeline companies. Banking sector investments increased by 4.4%. We felt confident in banking sector additions as the industry is still under significant regulatory supervision. We ventured down into subordinated bonds due to this environment. Our analysts still avoided many names in Europe due to the slow growth and nonperforming loan issues in a few countries. Large mergers in the food and beverage sector led to significant issuance in 2016. We added selectively here (1.7%) and took advantage of new-issue premiums. The communications sector has been a favorite of our analyst team ever since the global financial crisis (GFC). Assets increased by 1.5% on the whole portfolio. Cable and wireline company bonds were prominent investments. We have also favored utility investments in the volatile years after the GFC. Once again, regulation and investor pressure to keep leverage in check have kept volatility low. The Fund's investments in this sector increased by 1.8%.

A noteworthy drag on 2016 performance was related to investment grade corporate investments and/or positioning. As we said earlier, the rally in the energy sector was fierce after OPEC agreed to talk about limiting production and the ECB decided to buy corporate bonds. Our conservative posture in the sector and the underweight exposure for some of the year led to an 18-basis-point negative contribution relative to the benchmark index (Brinson method, before expenses). A smaller, but similar effect occurred in the commodity space. A late year decline in pharmaceutical company bonds also produced a performance drag. Political pressure against drug price increases, and competition in the generic drug space caused an increase in risk premiums in these companies. Additionally, the significant yield and curve move in the fourth quarter created performance drags. Attractive new-issue corporate and curve placement had led us to concentrate exposure in the 5- through 10-year maturity space. This placement was very sensitive to movements in the fourth quarter. While these factors produced drags on performance, the Fund's investment grade corporate investments are an important part of the Fund's income advantage over the index.

MBS exposure declined throughout the year as the sale of these investments was used to fund purchases of corporate bonds. Our MBS team had correctly predicted that nominal returns in this sector would be muted due to starting yield and risk premium levels. The Fed's continued MBS purchases have also kept the sector from moving to more attractive levels. The Fund's exposure to MBS declined from 24.9% in 2015 to approximately 14.9% at the end of 2016. The fourth quarter nominal yield and yield curve move had a significant effect on MBS performance contribution. The agency pass-through mortgage portfolio's barbell structure — that is, combining long-term bonds and short-term bonds — in 30-year conventional 3%, 4.5%, and 5.5% coupons underperformed the benchmark index during this period of rising rates and a steeper yield curve. Conventional 3% coupons extended and were the most affected by this move. The Fund's exposure to CMOs helped mitigate the agency pass-through performance as both nonagency structures and interest-only investments had attractive relative performance in this period. The credit risk transfer deals also contributed to the CMO performance as these are floating-rate deals with attractive yield premiums above U.S. Treasury investments.

As we enter 2017, we plan to keep the Fund's overweight in credit exposure and to maintain the income advantage into the first quarter. We believe a combination of possible Trump stimulus and a favorable business environment will compete against a higher U.S. rate environment and the relentless rise in the U.S. dollar in 2017. We will watch these competing forces very closely.

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Performance

The performance quoted represents past performance and does not guarantee future results. Investment return and principal value of an investment will fluctuate so that 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 data current to the most recent month end may be obtained by calling 800 523-1918 or visiting delawareinvestments.com/performance.

Total returns may reflect waivers and/or expense reimbursements by the manager and/or distributor for some or all of the periods shown. Performance would have been lower without such waivers and reimbursements.

Average annual total return

as of quarter-end (12/31/2016)

	Current quarter	1 year	3 year	5 year	10 year	Lifetime	Inception date
Institutional Class shares	-2.35%	3.94%	2.73%	2.83%	5.57%	6.48%	10/28/2002
Class A (NAV)	-2.42%	3.56%	2.47%	2.55%	5.31%	6.68%	12/29/1997
Class A (at offer)	-6.82%	-1.06%	0.91%	1.61%	4.83%	6.42%	
Bloomberg Barclays U.S. Aggregate Index	-2.98%	2.65%	3.03%	2.23%	4.34%	n/a	
Morningstar Intermediate-Term Bond Category	-2.54%	3.23%	2.73%	2.61%	4.10%	n/a	

Returns for less than one year are not annualized.

Performance at NAV assumes that no front-end sales charge applied. Performance at max offer price assumes that a front-end sales charge applied.

Class A shares have a maximum upfront sales charge of 4.50% and are subject to an annual distribution fee.

Index performance returns do not reflect any management fees, transaction costs, or expenses. Indices are unmanaged and one cannot invest directly in an index.

Expense ratio

Institutional Class shares (Gross)	0.65%
Institutional Class shares (Net)	0.65%
Class A (Gross)	0.90%
Class A (Net)	0.90%

Institutional Class shares are only available to certain investors. See the prospectus for more information.

Important disclosures and definitions

Investing involves risk, including the possible loss of principal.

Carefully consider the Fund's investment objectives, risk factors, charges, and expenses before investing. This and other information can be found in the Fund's prospectus and its summary prospectus, which may be obtained by visiting delawareinvestments.com/literature or calling 800 523-1918. Investors should read the prospectus and the summary prospectus carefully before investing.

Past performance is no guarantee of future results.

Unless otherwise noted, the source for all data cited in this commentary is Bloomberg.

Fixed income securities can lose value, and investors can lose principal, as interest rates rise. They also may be affected by economic conditions that hinder an issuer's ability to make interest and principal payments on its debt.

Fixed income securities may also be subject to prepayment risk, the risk that the principal of a fixed income security may be prepaid prior to maturity, potentially forcing the investor to reinvest that money at a lower interest rate.

High yielding, non-investment-grade bonds (junk bonds) involve higher risk than investment grade bonds.

International investments entail risks not ordinarily associated with U.S. investments including fluctuation in currency values, differences in accounting principles, or economic or political instability in other nations.

Investing in emerging markets can be riskier than investing in established foreign markets due to increased volatility and lower trading volume.

International fixed income investments are subject to currency risk. Adverse changes in foreign currency exchange rates may reduce or eliminate any gains provided by investments that are denominated in foreign currencies and may increase losses.

If and when the Fund invests in forward foreign currency contracts or uses other investments to hedge against currency risks, the investment portfolio will be subject to special risks, including counterparty risk.

This document may mention bond ratings published by Standard & Poor's, a nationally recognized statistical rating organization. Bonds rated AAA are rated as having the highest quality and are generally considered to have the lowest degree of investment risk. Bonds rated AA are considered to be of high quality, but with a slightly higher degree of risk than bonds rated AAA. Bonds rated A are considered to have many favorable investment qualities, though they are somewhat more susceptible to adverse economic conditions. Bonds rated BBB are believed to be of medium-grade quality and generally riskier over the long term.

This document may mention bond ratings published by Moody's, a nationally recognized statistical rating organization. Bonds rated Aaa are rated as having the highest quality and are generally considered to have the lowest degree of investment risk. Bonds rated Aa2 are considered to be of high quality, but with a slightly higher degree of risk than bonds rated Aaa. Bonds rated A2 are considered to have many favorable investment qualities, though they are somewhat more susceptible to adverse economic conditions. Bonds rated Baa3 are believed to be of medium-grade quality and generally riskier over the long term.

This document may mention bond ratings published by Fitch, a nationally recognized statistical rating organization. Bonds rated AAA are rated as having the highest quality and are generally considered to have the lowest degree of investment risk. Bonds rated AA are considered to be of high quality, but with a slightly higher degree of risk than bonds rated AAA. Bonds rated A are considered to have many favorable investment qualities, though they are somewhat more susceptible to adverse economic conditions. Bonds rated BBB are believed to be of medium-grade quality and generally riskier over the long term.

Diversification may not protect against market risk.

The Fund may experience portfolio turnover in excess of 100%, which could result in higher transaction costs and tax liability.

Because the Fund may invest in bank loans and other direct indebtedness, it is subject to the risk that it will not receive payment of principal, interest, and other amounts due in connection with these investments, which primarily depend on the financial condition of the borrower and the lending institution.

The Fund may invest in derivatives, which may involve additional expenses and are subject to risk, including the risk that an underlying security or securities index moves in the opposite direction from what the portfolio manager anticipated. A derivative transaction depends upon the counterparties' ability to fulfill their contractual obligations.

The Morningstar Intermediate-Term Bond Category compares funds that invest primarily in corporate and other investment grade U.S. fixed income issues and typically have durations of 3.5 to 6.0 years. These funds are less sensitive to interest rates, and therefore less volatile, than funds that have longer durations.

The Bloomberg Barclays U.S. Aggregate Index (formerly known as the Barclays U.S. Aggregate Index) measures the performance of publicly issued investment grade (Baa3/BBB- or better) corporate, U.S. government, mortgage- and asset-backed securities with at least one year to maturity and at least $250 million par amount outstanding.

The BofA Merrill Lynch BB-B U.S. High Yield Index tracks the performance of U.S. dollar–denominated high yield corporate debt rated BB1 through B3 publicly issued in the U.S. domestic market.

The S&P/LSTA (Loan Syndications and Trading Association) Leveraged Loan Index is a broad index designed to reflect the market-value-weighted performance of U.S. dollar-denominated institutional leveraged loans.

Views expressed were current as of Dec. 31, 2016, are subject to change, and may not reflect the manager's current views. Views should not be considered a recommendation to buy, hold, or sell any security and should not be relied on as investment advice.

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