

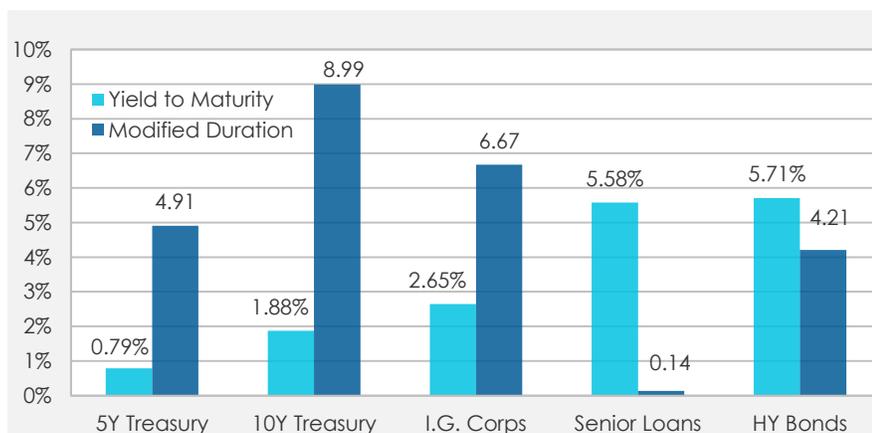
Senior Bank Loans: A chance to diversify within High Yield

Senior Bank Loans offer a very good alternative to diversify High Yield holdings within an investment portfolio.

Bank Loans, commonly referred to as “floating rate loans,” are privately structured debt obligations issued by corporations, often rated below Investment Grade, that seek to raise capital. The most important feature of Bank Loans is their seniority in the capital structure. Loans are primarily composed of first lien and senior-secured debt that takes precedence over other debt claims in the case of default or bankruptcy. Bank Loan coupons in general reset in line with the 1-, 3- or 6-month LIBOR index. This floating rate feature lowers the interest rate risk of Bank Loans compared to other fixed income products. In addition, many Bank Loans contain highly restrictive covenants that prevent companies from issuing additional debt if financial ratios would be pushed over certain predetermined levels.

Table 1. Not all High Yield is equal

	Senior Bank Loan	Fixed High Yield
Coupon	Floating	Fixed
Duration (index)	0.14	4.21
Lien position	1st, 2nd	No
Secured	Yes	No
Recovery Rate (1999-2009)	55	30



Senior Bank Loans rank higher in a company’s capital structure, as the loans are structured in such a way that have priority (traditionally 1st and 2nd lines) in the case of a corporate default, in addition to being secured.

The Thinking Man’s Approach



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High Yield represents a very good compliment to Equity investments in a low yielding world, where risk on investments are in demand.

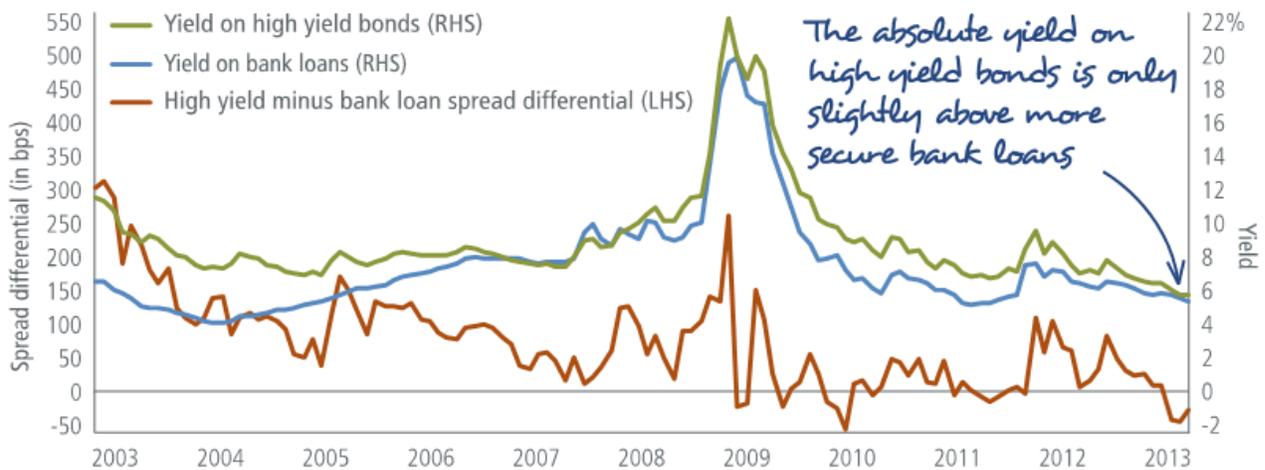
Senior Bank Loans or leveraged loans, are sometimes misunderstood and viewed as a complex investment proposal, but this is a misconception. The Senior Secured Loan market provides a stable current income investment alternative to more traditional fixed income and High Yield Bond allocations. According to S&P the size of the Bank Loan market is now similar in size to that of the High Yield Bond Market.

For more information and details on our investments, or how to invest into the Senior Bank Loan space please contact your Investment Advisor or inquire at: ideas@bigsurpartners.com



Source: Neuberger Berman

The opportunity to invest into Senior Bank Loans is current, as a more secure investment within High Yield trades almost at par to non-secured High Yield traditional investments as the graph below illustrates.



Source: PIMCO

Conclusion

With most fixed income asset classes trading at or inside historical yield levels, the loan market offers investors an attractive relative value. We think that an allocation in floating rate Senior Bank Loans can help reduce duration risk without diluting returns. The effect of this, is that portfolios are hedged against future increases in interest rates. We think that very few fixed income investments offer attractive current income with a low duration and moderate volatility as Senior Bank Loans do.



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