SEIX INVESTMENT ADVISORS LLC®
A VIRTUS INVESTMENT PARTNER

Leveraged Finance

> High yield rebounded strongly in 1Q19, underscoring commentary that the Federal Reserve's (Fed) last rate hike was an ill-timed misread of myriad underlying data, which in turn led spooked investors in passively managed strategies to overreact. With increased liquidity and wider spreads, the U.S. high-yield bond market, as measured by the BofA Merrill Lynch High Yield Cash Pay Index, rose 7.4% during 1Q19.

> Defying its critics, the U.S. leveraged loan market, as measured by the Credit Suisse Leveraged Loan Index, showed returns of 3.78%, marking the strongest first quarter in a decade, according to Credit Suisse.

> While high yield flows during the quarter were positive, the pace of retail outflows in the loan sector slowed.

HIGH YIELD

High yield's performance in the first quarter benefited from a pause by global central banks, improved earnings, resurgent equity markets, and trade optimism. Offsetting that was a slowdown in growth expectations for the U.S. economy as Europe weakened and uncertainty about Chinese trade talks continued.

While the BofA Merrill Lynch High Yield Cash Pay Index had its strongest first quarter since 1992, CCCs only outperformed by 50 basis points. Using the J.P. Morgan US High Yield Index, CCCs actually underperformed the market.

One big area of outperformance was in the metals and mining sector, partially driven by a Canadian metals company that experienced a highly unusual jump in price in one week. Although the company was marked at 64 on March 8, it matured at par on March 15. The other big source of outperformance was the energy sector, as resilient demand growth drove oil prices to four-month highs toward the end of the quarter.

The big area of underperformance was the financial sector, particularly banks and insurance, both of which were hurt by the Fed decision to hold off on further interest rate hikes. We continue to favor the financial sector with a preference for high quality credits.

High yield issuance picked up during the quarter, and high yield funds reported their third monthly inflows in March. In contrast, investors concerned about risk fled floating rate for fixed rate, but collateralized loan obligation (CLO) issuance maintained a deliberate pace.

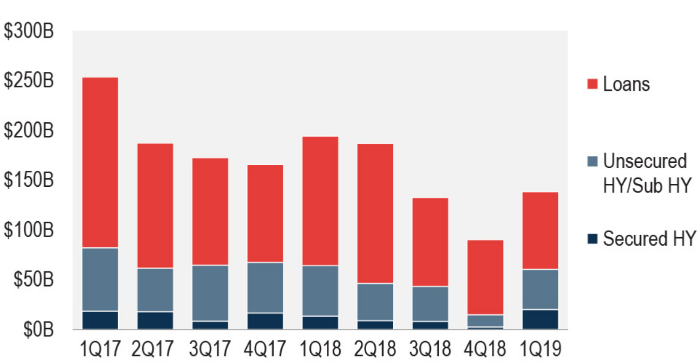
Bellying Up to the Barbell

We continue to follow a barbell approach. On one end of the barbell, we are looking at shorter duration bonds of higher quality companies with a catalyst, and that catalyst tends to be maturity. On the other side of the barbell are CCC credits, which can be more volatile as investors turn defensive, especially in the energy sector. But such volatility can create potential opportunity in oversold credits that appear very cheap. Some of those CCC credits may represent a short-term trading opportunity, but if they stay cheap, we may just hold them and clip the coupon for a while.

We also reduced our energy exposure to shale gas plays during the quarter. While we still believe there are potential opportunities in shale, particularly in the Permian Basin in the southwestern United States (now the world's largest oil producer), some companies in that region have raised concerns about their returns on invested capital.

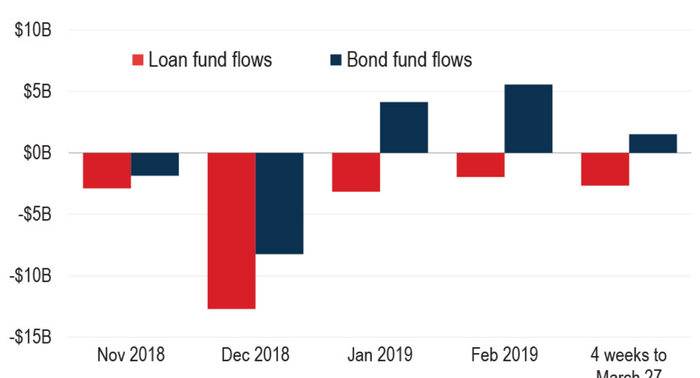
That said, there appears to be a trend toward underweighting CCCs as active managers wait for more attractive buying opportunities to present themselves. Even so, defaults in the high yield space continue to run very low, according to JP Morgan data.

HIGH YIELD ISSUANCE ROSE IN 1Q19



Source: LCD, an offering of S&P Global Market Intelligence

...AS RETAIL INVESTORS FLED FLOATING RATE FOR FIXED RATE



Note: Based on weekly reporters only
Source: Lipper

Our View

Market fundamentals continue to look good. While some investors have reduced their positions in energy, retail, and healthcare, others have added selectively in media, technology (more on the hardware side), broadcasting and gaming.

While we expected the default rate to rise to 2% in 2019, the trend so far has been in the opposite direction. Ultimately, it will probably tick higher, but we believe the overall rate should be very conducive to a healthy year for actively managed high yield strategies. Retail flows turned positive in the first quarter compared to the tumultuous 4Q18, and we expect they will remain stable as investors continue to view the sector as an attractive source of income.

LEVERAGED LOANS

The Credit Suisse Leveraged Loan Index returned 3.78% for the first quarter as yield-starved investors, confident in resilient economic growth, warmed to the asset class and the ability of underlying borrowers to repay their debts. Notable contributors by industry were energy (+5.13%), retail (+5.0%), and broadcasting (+4.68%).

Gross issuance in 1Q19 rebounded from a very slow 4Q18, but came in at $67.4 billion, down 72% over last year's period. On a net basis (excluding repricings and refinancings), issuance was $53.7 billion, down 30% over last year. Two-thirds of the issuance was in M&A, while refinancings accounted for 20%, and the general corporate/dividends/other category amounted to 14%. The majority of issuance (78%) was in middle-tier ratings (BB, B), while the upper tier accounted for 9%, and the lower tier was 13%.

As for demand, retail fund flows continued a negative trend since October 2018, with an outflow of -$10.1 billion—a distinct improvement over the $20.6 billion outflow in 4Q18.

CLO Net Volume Growth Remains Stable in a Low Default Environment

CLOs saw gross volume of $38.5 billion compared to $62.3 billion for the same period last year. Net volume was $29.3 billion compared to $32.1 billion last year.

In stark contrast to recent articles about risk in the financial press, default rates remained low. The loan par-weighted default rate ended February at 1.0%, the lowest level since April 2012, according to Credit Suisse.

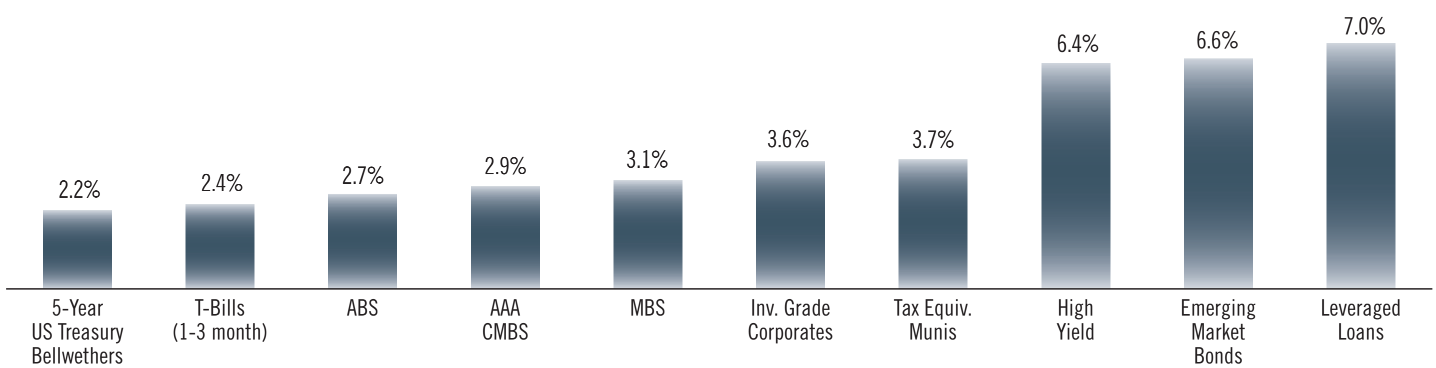
The key points, in our view, are that retail outflows continue, but have decelerated; CLO formation provided continued support; refinancings/repricings were sidelined; Index pricing recovered somewhat with the month-of-March price falling $0.64 after rising $2.90 in January and February; and LIBOR levels remain supportive, with the 3-month LIBOR around 2.6%.

Our View

With leveraged loans still one of the strongest performing asset classes on a risk-adjusted basis since 1992[1], we maintain our constructive outlook given average yields and the average price of loans. Remember, leveraged loans tend to perform well when rates do not rise. The most recent Fed rate hike did not begin until December 2015, and **prior** to that loans outperformed three out of five times and posted positive absolute returns four out of five times.[2] Investors who sold their leveraged loan funds into recent downdrafts (in favor of cash-equivalents or ultra-short duration funds earning far more modest returns) eventually saw those bank loan funds rally.[3]

The bottom line: Our rigorous individual credit research analysis aims to take advantage of attractive risk/reward valuation opportunities created by the recent market volatility. Additionally, we continue to be overweight higher quality loans, consistent with our fundamentally-oriented investment philosophy.

HIGH YIELD BONDS AND LEVERAGED LOANS OFFER COMPELLING YIELDS IN THE CURRENT MARKET ENVIRONMENT



Past performance is not indicative of future results.
Source: Bloomberg Barclays, JPMorgan, Credit Suisse. As of 3/31/19.

[1]"CS Credit Strategy Daily," Credit Suisse, April 3, 2019. [2]Source: "Annual Total Returns 2010-2015," Bloomberg Barclays, Credit Suisse. [3]"High Yield Bond and Leveraged Loan Market Monitor," J.P. Morgan, April 1, 2019.

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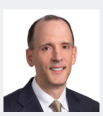
Authored by:

Leveraged Loans



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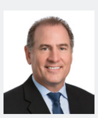

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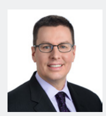
High Yield



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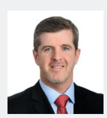

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Seix Investment Advisors is an investment management boutique focused exclusively on managing fixed income securities since 1992. Seix seeks to generate competitive absolute and relative risk-adjusted returns over the full market cycle through a bottom-up focused, top-down aware process. Seix employs multi-dimensional approaches based on strict portfolio construction methodology, sell disciplines, and trading strategies with prudent risk management as a cornerstone.

The **Credit Suisse Leveraged Loan Index** is a market-weighted index that tracks the investable universe of the U.S. dollar denominated leveraged loans. The index is calculated on a total return basis. **ICE BofAML U.S. High Yield Cash Pay Index** is an unmanaged index consisting of all domestic and Yankee high-yield bonds maturing over one year. The quality range is less than BBB-/Baa3 but not in default (DDD1 or less). The **Bloomberg Barclays U.S. Aggregate Bond Index** measures the U.S. investment grade fixed rate bond market. The **J.P. Morgan Domestic High Yield** Index is designed to mirror the investable universe of the U.S. dollar domestic high yield corporate debt market.

The indexes are unmanaged, their returns do not reflect any fees, expenses, or sales charges, and are not available for direct investment.

LIBOR is a benchmark interest rate at which major global lend to one another in the international interbank market for short-term loans. LIBOR, which stands for London Interbank Offered Rate, serves as a globally accepted key benchmark interest rate that indicates borrowing costs between banks.

A **Basis Point (bp)** is equal to 0.01%.

Collateralized Loan Obligations are securities backed by a pool of assets often low-rated corporate loans.