Introducing Leveraged Corporate Bond Portfolios

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Bonds, in particular, are subject to a number of risks, including, but not limited to, market fluctuations. Such fluctuations in value can occur for many reasons, including interest rates, rating upgrades/downgrades, and other economic reasons. You may lose the entire value of your investment in a specific bond if the issuer defaults. Because the strategy involves the use of leverage, you may lose your entire investment as a result of a margin call. You may also realize losses on callable bonds that are valued below your purchase price at the time the issuer calls them away. If you do not understand the risks involved with bonds and in the use of leverage, you should not invest in such a strategy.

The examples provided in this presentation may not reflect the impact of material market or economic factors that might ultimately influence an adviser’s decision making. There are numerous other factors related to the markets in general or to the implementation of any specific trading program that cannot be fully accounted for in the preparation of the examples provided herein. Accordingly, clients should focus on the strategy described rather than the results shown herein.

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In today's environment, fixed income investors face a dilemma…

- Money market rates return at 1.5% or less
- Investors who go farther out the yield curve take on significant interest rate risk when holding periods exceed the immediate term
- The stock market is near all time highs, and is now the longest bull market ever as of 2009

Our solution is to leverage shorter-duration corporate bond portfolios…

- We use speculative-grade corporate bonds from corporate leaders that yield significantly more than government-issued securities
- We take advantage of changes in margin practices to leverage the portfolio
- The portfolio is reviewed monthly and actively managed

We focus on speculative-grade bonds and a five-year or so duration…

- We mitigate credit risk through research and diversification, typically selecting 10-30 different issuers per portfolio, in companies we believe are economically sound and not at great risk of defaulting.
- We focus on BB bonds, known as “fallen angels”. Fallen angels have higher yields because they are one step below BBB investment grade bonds. Many institutions are forced to sell their BBB bonds if they are downgraded from BBB to BB (investment to speculative grade) – and therein lies the opportunity.

Standard and Poor’s Bond Ratings

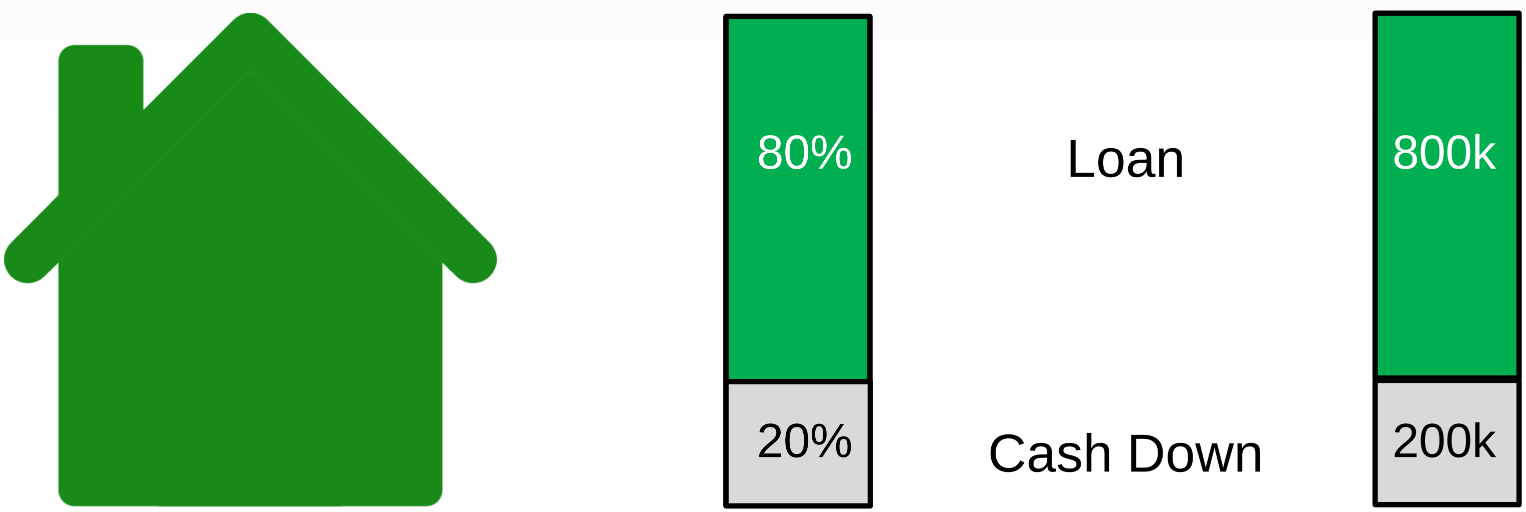
AAA AA A BBB	Investment Grade
BB B	Speculative Grade — Zone of Opportunity
CCC CC C	Junk Grade

Our program uses the maximum amount of leverage available to bonds…

- Reg T limits stock leverage to 1:1
- Unlike Reg T, speculative bonds typically qualify for up to 3:1
- Margin rates vary but can range between 2-4% for those in our trading program
- Leverage allows us to capture the spread between corporate bonds and the broker call rate, and then leverage it several times

Concept of Leverage

- Traditional home purchases are approximately 5 to 1 leverage



Please see Important Disclosures on slide 2 as they are an integral part of this presentation.

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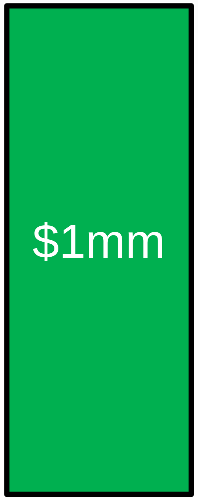
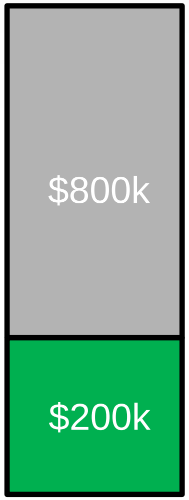
Concept of Leverage Continued: Positive Rate Carry



Rental Home
Base Investment:
$1,000,000
Rent: 6.00%
Annual Rent: $60,000

Leveraged Rental Home
Base Investment:
$800,000
Mortgage Rate: 4.00%
Annual Cost $32,000
$200k Cost: 0%

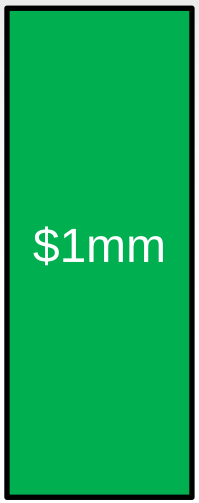


Annual Rent: $60,000

Annual Cost: - $32,000

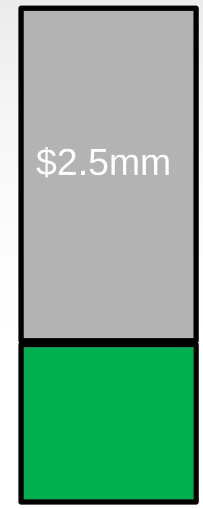
Annual Gain: + $28,000 = Positive carry

Concept of Leverage Continued: Positive Rate Carry



Un-leveraged
Base Investment:
$1,000,000
Yield: 6.83%
Yield less fee 95BPS:
5.88%
Annual Interest:58,800
Margin 0%
Effective yield NET: 5.88%
Total interest $58,800

Leveraged
Base Investment:
$2,500,000
Yield: 6.83%
Yield less fee 95BPS:
5.88%
Annual Interest $147,000
Margin 3.06%
Effective yield NET: 2.82%
Total Interest: $70,500



Yield Less Fee: 5.88%
3:1 Leverage: $3,500,000
Total Interest: $129,300
Effective NET Rate for this example: 12.93%

We use Interactive Brokers for a one-stop custody and trading platform solution...

- Interactive Brokers is a full-service broker dealer capable of custody and clearing for bonds, futures and interest rate swaps
- Interactive Brokers offers portfolio margining, and electronic access to global markets, giving us full integration with their trading, clearing and reporting systems
- An integrated platform allows us to manage margins and balances across asset classes

Margin Explanations

What is margin?

- Borrowing on margin is a similar concept as a home loan but, it is based on the value of your investments as opposed to the value of your home.
- Investing on margin carries risks which have been outlined in the Important Disclosures section in the beginning of this presentation. Please reach out to us with any additional questions you may have.
- There are two main margin definitions:

Securities Margin:

- Securities margin is borrowing money to buy stock

Commodities Margin:

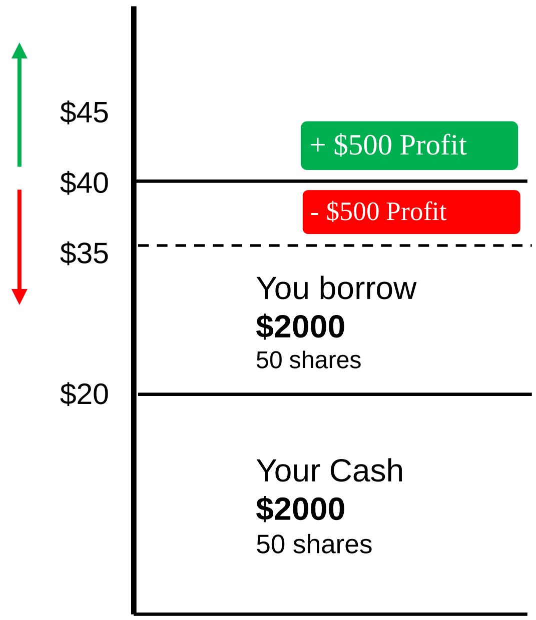
- Trading commodities on margin involves putting in your own cash as collateral for the contract

Margin Requirements

Initial margin:

•How much you must deposit to buy securities on margin

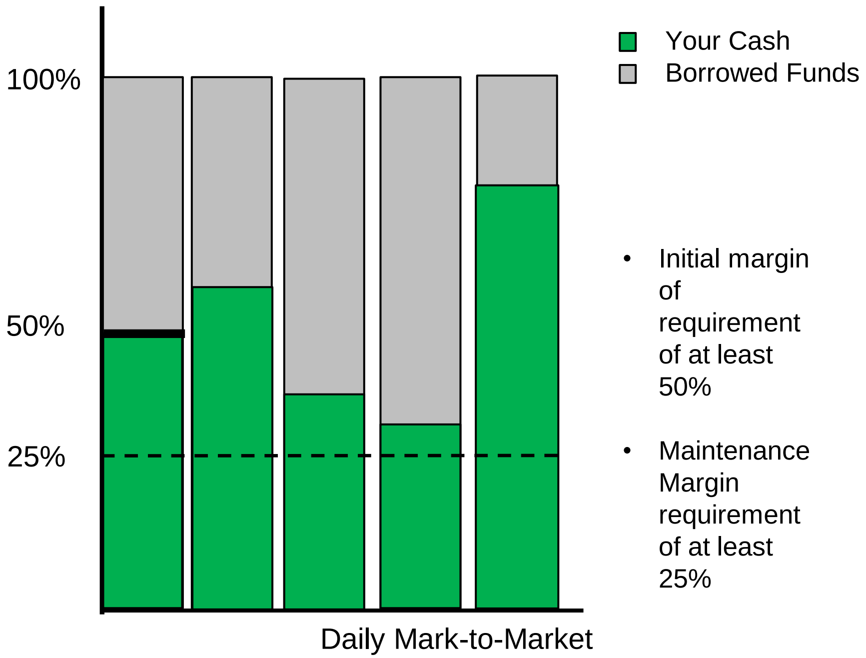
•Example of Trading on Margin:



Maintenance Margin:

•How much equity you must keep in your margin account

•Example of Margin Requirements:



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Interactive Brokers Margin Account Types

Regulation T Margin

•Rules based margin requirements are created from a defined formula and governed by regulation T exchange rules and IBKR house requirements.

Portfolio Margin

•Risk based margin requirements are assessed by profiling the risk of the position in your account in accordance with OCC requirements.

Real-Time Activity Monitoring

- **Monitor Balances**
  - View your margin balances and requirements in the TWS account window in real-time
- **Preview Margin Impact**
  - Shows your projected margin balances before entering an order
- **Margin Alerts**
  - Receive warnings and set alerts that tell you when your margin requirements are at risk

The risks in this program include:

- Interest rates are at historic lows, and could rise during the holding period, which would negatively impact bond values
- If bond is held to maturity and does not default, this risk is eliminated, but bond values fluctuate over time
- Bonds may not reach maturity in the event of a margin call, as they may be liquidated before maturity date
- During the life of the bond, it’s value can fluctuate based on rating downgrades, upgrades, and interest rates
- Short rates could rise, making spread between short and bond narrow, lowering net yield
- Bonds can default
- Leverage creates risks across the entire portfolio

We believe there is a limited window to for accredited investors to capture these preferential spreads...

- Rates are set by the market and are subject to change
- Spreads between 5-year speculative-grade corporates and the broker call rate could tighten at any time

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