Question 1

Paige: The number one question we got was about inflation. Venk, actually, you just wrote a piece on this. I'm going to push this question to you. **Can you tell us your thoughts on inflation?**

Venk Reddy: Sure. I'd be happy to. First of all, thanks to everybody for joining us. For those we've spoken to in the past, nice to see your names again. For those we haven't, we'll look forward to connecting with you soon. Regarding inflation. This is a topic that as you know as fixed-income investors, we think about a lot. I want to be clear, the way we manage our portfolios, typically, we don't express interest rate news in the portfolio in large part because our goal is not to be on the right side of a move in interest rates. Our goal is to have a portfolio that will perform as expected and consistently regardless of what happens.

That said, we definitely have our views and our opinions on what we're seeing. I think the thing that I find most notable and when we think about inflation, is not as much what's happening in the economy, is what's happening at the Fed. For those who read the article that we published, Paige, I think it was published on LinkedIn if I remember correctly and I'm sure you could get a copy from us.

Paige: It’s on our new website.

Venk: Oh, it's on our website. There you go.

One of the things that have been thinking a lot about, if you look at the comments that Fed Chairman Powell has made since the tail end of third quarter and the fourth quarter of last year, you'll see-- Everybody I think is aware of the Fed's dual mandate. Its mandate is to manage inflation, keep inflation at a reasonable level, and to manage what would be determined as a full employment. When you hear Chair Powell speak in his comments, it's often put in as an aside for the most part, but he started talking a lot about employment in under-less-advantaged demographics.

Just putting a fine point on, I'm going to say Black and Brown unemployment. Black unemployment and unemployment in Hispanic communities. I think one thing that we have to really recognize is that, for better or worse, whether we like it or not, our community, our society is still a bit of a trickle-down society when it comes to certainly employment and opportunities in these communities. I believe that a focus there and actually after we wrote our piece, Chair Powell has actually made very explicit comments to this effect. I feel somewhat validated in the point of view.

I believe that the focus on underrepresented demographics with respect to unemployment management is going to result in the Fed leaving rates lower longer. The reason is even when top-line unemployment gets to a level that most Wall Street economists and folks in New York think is a reasonable level, we're still going to need to keep rates low in order to see those employment figures and that job creation appear in less served communities. If this really is a priority of the Fed as it seems to be, as it comes up every single time as a metric that Chair Powell is focusing on, I believe the Fed is going to choose to leave rates lower longer, even

lower than people who think that they're going to leave rates lower longer, even longer than that.

I think the Fed is going to be looking at leaving the rates low for a particularly long period of time. What does this mean? It means that while the Fed can control the short end of rates pretty directly with their monetary policy, their levers for managing the longer end of the yield curve are less direct. I guess, less direct is the wrong choice of words because they can go into the market and buy bonds, but it's certainly not quite as impactful. A lot of times, the longer end of the yield curve and inflation expectations are driven by Wall Street's expectations by exactly this conversation and these questions.

It is my view that it's likely, though not guaranteed, that the market is going to see the risk of an overheating economy even more than what might otherwise be the case with low rates and is going to drive inflation expectations even higher than maybe where they are now. The Fed gave themselves cover to allow this to happen by switching from a 2% inflation target to a 2% average inflation target. For those who aren't familiar with the difference, in the past, the Feds, it was actually stated policy is they would target monetary policy that led to 2% inflation, but they didn't care what happened in the past. You could run it 1% for 10 years and they're still just targeting two.

Now with an average inflation target, they're actually saying, "If you run at 1%, for some period of time, you can run it three for a little while, and we're not worried about it." This gives the Fed cover to let inflation run hot, let the economy run hot, let inflation run high or expectations of inflation run high or even actual inflation run high until they achieve the other side of their mandate, which is the unemployment the way they see that playing out. The last point I want to make on this is-- I'm going to share a screen here. Do I have the right to do the screen? Do you mind enabling me there, Paige? I want you guys to see something real quick. Let's see. Oh, good. Here we go.

I'm going to show you guys have a Bloomberg screen. What you're looking at here, just so you see, this is the yield curve over various points in time. This is today. What is that? 2016, this is 2010. All right, and I'm comparing that to-- this was the end of 2019. Then this one right here is the end of 2006. The reason I'm putting this up there is because really-- the point I'm going to make, I'm going to make the point that I'm going to show you why this graph supports it is, I think one of the Fed's biggest takeaways from the crisis in 2008 is that they want banks to be strong, healthy and profitable.

Banks are profitable, the banking business model is as many analysts will recognize is that you lend long, and you borrow short. When there's an upward sloping yield curve as we see now and then 2010, and in 2016, banks can lend up here-- hopefully, you can see my mouse-- and they can borrow down here or get their deposits down here and they have a nice healthy profit based on the shape of the yield curve. When you end up in a situation like we saw in 2019, and then 2006, it is not a coincidence that those years are right before a market dislocation and the yield curve is flat. Banks aren't profitable unless they use credit spreads in order to increase the steepness of essentially their internal yield curve.

When banks can't make their money using interest rates, they're going to make their money using credit. Once banks start using credit, they use their balance sheet, they use up risk

budget on their balance sheet, just getting the profitability and when the market comes to them for liquidity, for a bid, essentially, on risk assets and they've used up their risk budget on just getting the basic upward sloping profitability that they need, then they are not there to provide liquidity and you end up with what we had in 2008 and in 2020. Not coincidentally, the sell-off, the market dislocation starts, at least, in exactly that sector that the banks have overextended on the credit to begin with, whether it was housing in the 2008 crisis or whether it was corporate lending in 2020-- what happened last year.

The Fed doesn't want this. That's really what I'm getting at. The Fed doesn't like this. They don't love that banks in a flat yield curve environment have to take on and use balance sheet on risks that would then prevent them from providing liquidity. I don't think the Fed will be that upset about a steep upward sloping yield curve and I think we run the risk of having a very steep yield curve over the course of the next few years as the market heats up on their views of the economy, or as the market adjust their views on how overheated the economy can get while the Fed continues to keep rates on the short end very low.

Question 2

Paige: Thanks, Venk. **That actually reminded me, we had a client call last week and they asked specifically how steep it could get for how long.**

Venk: If I knew when and how long it would stay steep, we'd probably have another strategy where we actually express these views in the marketplace. I can be very on point about that. This is 2010 and this is now and you can see the short end of the curve is very similar. You can see the long end of the curve is very not. This is 200 basis points of difference on the 30-year point. It's about 150 basis points of difference on the 10-year point. Being overly simplistic about it, I look at this, and I say, "Okay, even if you ignore the renewed focus on underrepresented demographics on less advantaged demographics, with respect to unemployment, you see that on a in a post-crisis scenario, we could see the curve steeping another 150, 200 basis points."

Could it get steeper than that? Sure. Is it possible that it doesn't get that steep? Yes, that's possible, too. In my view here, I certainly wouldn't be betting against it getting that steeper, steeper. If I was further out on the yield curve, I would be very cautious about what risks I'm taking in my portfolio. Which by the way, just to be clear, we are not taking those risks in our portfolios, so that I was not Zeo that I was a rhetorical investor.

Question 3

Paige: Marcus, with some of the stage that Venk set with inflation, how are our companies preparing? Or do you have concerns about our portfolio companies with a rising inflation environment?

Marcus Moore: Definitely, inflation is a hot-button topic right now but the thing I'm encouraged by is that many of our companies feel that they have the ability to pass on that

inflation through means. There are even companies in our portfolio talking about taking on incremental risk or incremental costs to bring in product because they're seeing such demand in the marketplace that they're willing to incur those incremental costs, those inflationary costs because there's a customer waiting to pay whatever is necessary for them to still be profitable on that transaction. I feel good about obviously, where our company stand now.

I think the question is just going to be how long this lasts. I think throughout most of 2021, a lot of our companies are either headed from a cost perspective or feel so good about the demand that they're taking on incremental cost on top of just the raw materials in and of itself, paying higher freight costs, et cetera, to bring that product in because they know they can sell their product at a cost that's profitable to them.

Question 4

Paige: We had a question come in, and Marcus, I'm going to push this to you and Venk, you can chime in if you like as well. Can you just give us a state of the credit markets, including fundamentals valuations and what you're seeing?

Marcus: Okay, sure. Right now, the high yield index is yielding about 4% on a spread basis here at about 300 basis points, not at the all-time lows for each but relatively close. With that, you're seeing tremendous demand for the high yield asset class. Issuance has set monthly records in March and April of 2021. One cue 2021 is a record for quarterly issuance and most people who thought at the end of 2020 that there was no way 2021 issuance would be higher than 2020 have now really adjusted their forecasts, and we're expecting to see 2021 issuance higher than last year.

The good news is that most of that's going to be significantly refinancings. I think we talked about this on a previous town hall where last year there was a significant amount of new debt brought into the high yield market. Most companies were doing that to help buffer through what was the unknown of how long the pandemic would last, what recovery would look like. Now that companies have seen what recovery is starting to look like, vaccines have rolled out aggressively, now just really saying new debt issuance really being more just for refinancing, which is good for the overall industry.

One interesting data point, Nielsen, a company that we like for various reasons, they do measurement for TV commercials, the ratings, you can get the Nielsen box and all those people. If you want to know what's a rating, it's Nielsen. They track your viewing at your house and so that's a big part of their business. They issued 8-year and 10-year paper in September, October of 2020. The 8-year price, that five and five-eighths, the 10-year price that five and seven-eights. Just this week, Nielsen came back to the capital markets and they issued 8 and 10-year paper. That 8-year paper came in four and a half, and the 10-year paper came in four and seven eighths.

You've seen within the last six, eight months a compression for Nielsen of about 100 basis points. That's tighter than what we've seen overall from a spread perspective, which speaks to the fact that Nielsen is a solid fundamental credit and had been able to, over that six-month

window as concerns around again, what business is going to look like post-pandemic have alleviated. They've taken advantage of one, a tightening credit market, and then two, improve credit fundamentals to drive significant interest savings on new debt issuance this week. Oh, man, I think the market is relatively healthy. That's a good thing for us right now.

Venk: I'm going to chime in on that. First of all, to point out that you mentioned the Nielsen box. I don't know, hopefully, some of the people on this call remember filling out the little booklets. Forget the box, whatever that is. [crosstalk] boxes that's so modern and today. The only other comment I'll make on the current market, and this has implications for how we manage our portfolios is at least in amongst-- When you filter for just those companies that meet our credit standards. That meet our definition of creditworthiness, the yield curve is actually very flat. The credit yield curve is very flat, not spreads or interest rates, but just what you're getting, 4% yields, 5% yield, it's pretty flat.

What that really means is from our perspective, the folks who know us on the call, well know we're not tactical. We don't like say, "Oh, now we want to be here and now we want to be here." We have a duration constrained to short-duration portfolio and then we have a duration unconstrained portfolio. In the case of the short duration portfolio, it's just short duration, period, end of story. For a duration unconstrained portfolio, we're making assessments of opportunity cost. That's how we think. We always think in risk term. I'm sure I'll bring this up later too, when we answer other questions, but we always think in risk terms.

If you're not going to get paid to take on longer risk out five years or eight years as opposed to what you're getting paid to take risk for two to three years, it's really notable right now that that curve is so flat. It's not actually upward sloping as you would expect, as you would imagine, there's more uncertainty, when you're looking at a company 10 years from now. Out 10 years versus out 2 years, you'd expect there to be a risk premium compensating you for that. With respect to what we're seeing in the credit markets right now, because that yield curve is so flat when you select for-- Surely, there's really high yields and really crappy credits all along the curve.

When you select for the types of credits that we're willing to look at and consider, the opportunity cost is not really rewarding you for longer duration. Whether in the portfolio we have where we have that flexibility, or, obviously, in our short duration portfolio, it's constrained either way. I just wanted to toss that point out there.

Question 5

Paige: With the markets being so healthy and thinking about the two strategies that we have Marcus and Venk, are there any risks that you see in the companies that we own because we're right in the middle of earning season? Is anything coming up that's concerning or is particularly exciting?

Marcus: I feel really good about what we've seen in this earning season. For context, our companies on average, which have reported yet-- We probably have a few stragglers out there's and off cycle names, but of companies who've reported so far, we've seen a beat of

our internal estimates by about 35%. We'll grant you that we're not the most aggressive in terms of forecasting out to the future because we always want to be mindful of what the downside risk are to our companies, but I think another data point will help frame it even better. If you think about 1Q21 EBITDA for our companies versus 1Q19, 1Q21 has been up 16%.

The companies in our portfolio are through the worst of the pandemic and are now entering into a secondary phase of growth in line with what you saw pre-pandemic. Given that, and the fact that most of our companies really are thinking about right now, balance sheet repair and focusing on, "If we did take incremental debt throughout 2020, we're now in a position where we can repay that debt, given the fact we've seen stronger earnings and stronger cash flows." Those improvements on a fundamental credit basis that we're seeing throughout the portfolio from earnings is very encouraging. It's something I'm pretty excited about.

Paige: Venk, did you want to add anything there?

Venk: I'll toss this in, which I think is again, I'm king of the philosophical points. I think when we think about earnings, it's important for people to understand if they don't already, that we-- Again, I keep talking about risk. We subscribe to the philosophy. We focus on the risks and scenarios that the most common question, I think, Marcus and I ask each other is, "How can this go wrong?" We want to wrap our arms around those risks and if we get comfortable with those, then the upside takes care of itself. We're not trying to be on the right side of a directional move, but if you buy good things, good things happen.

When I think about it from that standpoint, I think it's important for us that I could not emphasize enough. What we model into our credit analysis are those downside scenarios. It's going to be extremely rare for us to be able to answer a question that says, "Is there anything concerning or anything that scared you or surprised you to the downside," or whatever because we're already factoring those into the scenarios we consider when we're doing our analysis. Whereas you might see the equity in a company that we own sell-off because the market is, "surprised to the downside," that's not equivalent to a surprise to the downside for us, because we're already modeling in those scenarios.

That might be an often is reaffirming to our credit thesis. For us, because of that, we're almost set up to always be pleasantly surprised as opposed to ever being negatively surprised. That is in many ways, the difference between good credit work and good equity work. You're not trying to capture reality in your models, you're trying to capture downside scenarios, and then reality is a bonus.

Question 6

Paige: A question that came in that I think the entire audience would really benefit hearing from Venk is our approach to ESG in the credit space, and what approach we're taking there.

Venk: Yes, I'm happy to talk about this. I actually enjoy talking about this quite a bit. It's for this reason. I'm going to start this by saying something that some may find controversial and

others might take issue with but I believe it extremely strongly, and we factor it into everything we do here. When it comes to ESG in particular, in my opinion, negative screens and overlays are just lazy. They're lazy. They don't actually get to the point and they don't actually support the goal of the portfolios, which are dual. There are two goals of portfolio, performance and progress.

I think at the end of the day, instead of picking-- this is what we do in our portfolios as credit investors always, when you're picking securities, you're proactively selecting what goes into portfolio, the idea that you're going to take a bunch of stuff, and you're just going to throw out some bad guys, and then say, "Here you go," is fine. It sells well. For those who haven't read our most recent quarterly letter, I talked about some academic research that does exactly this, those strategies that deeply incorporate ESG factors into their analysis tend to perform better. But those strategies that take the quick in easy and lazy way, tend to raise the most assets.

At the end of the day, the market is gravitating away from the approaches that tend to deliver the best performance in favor of the ones that deliver the lowest fees and sort of, for lack of a better choice of words, the easiest stuff to explain. It's not that dissimilar attack to credit management in general. Enough of that. I want to get into why we take the deeply integrated ESG approach. It's super simple. Creditworthiness is a function of evaluating credit risks, period. That's noncontroversial. Everybody on this call can understand that. Credit risks in our experience throughout, as long as I've a managing credit fall into basically three main categories.

One is risks related to business factors. Those are going to be things like competitive landscape and management team and that sort of thing. There are risks that fall into the category of financial factors. Those are what you're used to seeing the quantitative metrics, leverage, liquidity, cash flows. Then there are those that fall into what-- I guess, though, term sustainability is a loaded term now, because there's such a trend toward ESG and sustainable investing. But business sustainability. If a business is not behaving in a way that's long-term sustainable for its business, if a management team is acting in a way that creates future liabilities.

Whether it's not cleaning up after themselves, or not respecting a fair business practices or something of the sort, if a management team is behaving in a way that's not long-term sustainable for their business, then that undermines creditworthiness. Now, even for someone who manages a short duration portfolio like we do, just because a bond is going to mature in two or three years doesn't mean that you don't have to pay attention to that long-term sustainability mindset. Because a bond might get paid off in three years, it was paid off, because they're able to refinance with a seven-year bond.

When we do the work, we have to recognize it, "Okay, three years from now, we need people to want to give the money for seven years." You're really doing a 10 year and you're effectively doing a long-term analysis, whether you're buying short or long. I'm not sure all short-duration portfolios, think this way, but certainly, this is how we think and we find that it drives consistency. Because of that, that business sustainability side, those characteristics that one evaluates, are equivalent entirely, to what would be considered material ESG factors,

meaning those ESG factors, characteristics, the founder, environmental, social, and governance issues that are material to that company's business.

There's obviously some things that aren't material. It's not really that valuable for a bank to tell you how they're disposing of their hazardous waste. They don't have hazardous waste in their normal course-- well, that's not true, but they don't have physical hazardous waste as part of their normal business process. Those factors that are material, those actually are necessary characteristics to consider and they always have been, this is not new, this is not something from the last couple of years. I can give you examples from almost a decade ago that fall into these same categories.

Put simply, that is the driver of creditworthiness, and that's how we evaluate it. Getting specific on ESG factor because that was actually the question. We actually do recognize there is one difference, one material difference between ESG factors and financial factors, and that material difference is this. The SEC has mandated that the companies report financial factors quarterly like in Ks and Qs. There is no such mandate or disclosure for some of these other factors that drive true financial performance of a company but aren't necessarily financial in nature. What that means is most companies treat reporting around some of these ESG issues as marketing, not as disclosure.

It takes a lot more work to really understand and dive into the history and the patterns of how a company is behaving in order to determine if they're actually behaving in a way that's long term sustainable for their business. What you're looking at on the screen here is how we do that. We do this per material ESG factor, which I can talk-- For anybody who's curious, I can talk more about how we determine materiality, we start by aligning ourselves with SASB standards, but then we adjust based on our own knowledge of particular company. I was just on a call earlier today, where we talked a lot about that's not an easy thing to do to really line something up to be a fit for a company.

That's something that we can dive into another time. But what you're looking at here, I'm going to give you an example with respect to financial leverage, it's not even an ESG factor. It's what I referred to as a financial factor. When we're looking at a company, we are and especially like, in some sectors such as retail, we're aware, we've been around long enough, we're aware of what a reasonable level of leverage is for a retail company. We are evaluating a company in a management team on whether they're aware of how important that factor is to their business.

Whether they have a strategy around managing their leverage, whether they're executing on that strategy, and whether measuring, reporting and holding themselves accountable. Now, in the case of financial factors, again, they have to report these things, or at least the numbers to allow us to calculate them. As a result, we're really focused on whether they have a strategy and execution and are they holding themselves accountable? If a company makes an acquisition that takes themselves above, what would be a reasonable average level for that particular business?

One of the first things we look for is what has the company said about bringing leverage back in line? What are their priorities? Are their priorities to get back to that point? Every credit factor essentially gets evaluated on this spectrum. We also evaluate all ESG factors along the

same spectrum. We engage with our companies, we look through historical data that we have, and data sources that we've partnered with in order to be able to try to identify that history, that pattern of behavior across each material, ESG factor the same way we dealt with other credit factors. What I'm really getting at is this is deeply, deeply embedded in a reasonable credit process.

It's deeply embedded in our deeply fundamental credit process. Except for the one piece that I mentioned before, it's a lot harder to do, because you don't have the 10Ks and Qs to be able to just spread numbers into a spreadsheet. We actually had to build our own piece of software internally that we call the green slate in order to track ESG factors the way that we can track financial factors in a spreadsheet. The long and short of it, that is how we approach ESG credit, and how we get above and beyond the lazy approach of just negative screening and overlays.

Question 7

Paige: Another philosophical question. We're probably going to start with you Venk and then maybe move into some specifics if Marcus has a follow-up. **What is the advantage to targeting a less trafficked area of the market?**

Venk: It's a good question, look, even with respect to ESG-- In my personal experience, throughout my career, I have found that there is almost a 100% correlation between what is less trafficked and what takes work. I was just describing the true work that has to happen, especially in credit space and high yield space, where with ESG, the services that other managers license, MSCI, Sustainalytics, whatever they do, the coverage and high yield is very poor because most of those services are built on equity indices and equity portfolios and in particular large-cap equity portfolios.

For our subset of the market, where there's a lot of privately held equities and where there are smaller cap companies, you don't get that coverage. You have to do the work. It's by nature, a less traffic area. The reality of it is, in that same way, when I think about the sandbox that we traffic in, which is risk-adjusted return, risk-managed and the duration managed credit, it is-- How should I put it? Our entire business is predicated on being a less-trafficked area. [chuckles] We're not the less trafficked corner of a very, very highly trafficked asset class. We actually are living in that component that it just takes more work to put together a portfolio, but what you get on the other side of it is a risk profile that we can deliver on consistently as best we can in our view.

From our perspective, because of that, it's what we do. I've spent a lot of my career having the opportunity to try to deliver risk profiles. This is what we do by the way, just as a side note. For those who don't know us that well, we deliver risk profiles. Now, where do you find those risk profiles? Well, I've had the opportunity to invest in a lot of different asset classes and to invest in relative value and all strategies, long shorts, and long-onlys and this, that, and the other. I found that, in my experience, the most consistent capital preservation risk profile is in this deeply researched risk-managed risk-adjusted and credit universe.

It can be a long-only portfolio. We're doing fundamental work, it doesn't have to be complicated to be sophisticated, but it does take a lot of work. Marcus will second me on this. It is extremely painful to do a ton of work on a company then have it refinanced out from under you within a month or two, or three months or six months or even a year. It's a lot of work, and that's okay. If what we're getting paid to do is roll up our sleeves and do work, I feel like that's a pretty fine way to make a living. At the end of the day, there's a lot of different ways that people try to come at delivering this type of a risk profile. We found that this particular segment of the market because it's less trafficked and is a place that we can consistently deliver this capital preservation profile that we aim for. The entire business is predicated on being a less traffic area. It's not that we're looking for less-trafficked opportunities in a picked-over sandbox. If that makes sense.

Question 8

Paige: Are there some specific examples as an output of this process that you can share?

Marcus: Yes. We looked at a company sometime last year, AgroFresh it was actually spun out of Dow Chemical. Dow actually still owns 40% of the shares. It's AGFS if you care to look up the equity ticker. The company's main product or their products are designed to enable produce to stay fresh longer. The main application is on apples. In the storage of apples before, after being picked, and before being distributed, you basically treat the product with their licensed technology MCP-1, and that enables for the produce to stay fresher longer. When it gets to us in the retail store, it's still fresh and it can last even from the time we get it home for a period of time, even after that.

Again, the chief fundamental process of the company is to eliminate food waste. From a sustainability standpoint, that's obviously a good thing. I think it's almost half of all produce that is harvested actually goes into waste, and 8% of all GHs greenhouse gas emissions are from food waste. To be able to help eliminate that is something good from a sustainability standpoint, and one of the important parts of that, to some extent, is as they eliminate greenhouse gasses potentially, you can see less weather variability, which is really their biggest risk. They're not exposed to economic cycles, the biggest concern they have is how many apples have been picked in the Northern and Southern hemisphere in any season, because of those apples being picked, about 80% of them are going to be treated with their products. Again, from a business perspective, they have a very strong and dominant market share.

Then another benefit is that they've done tests to actually see how much food waste they eliminate. In Europe, the product eliminates about 22% of food waste. The study they've done in the US says it eliminates about 30%. In 2015, the FDA set a target to reduce food waste by 50% by 2030. AgroFresh's product is the center of the fairway for what the FDA is trying to do as it relates to reducing food waste. From a financial perspective, the company's net leverage is less than four times, generate about a mid-single-digit, free cash flow on an annualized basis over its total debt, and management really is focused on two things, maintaining a very strong balance sheet and growing this product out to incremental application.

They have applications out now for blueberries and avocados, peaches, pears, and other citrus fruits. Again, the goal is to eliminate food waste to the extent, I think they said an apple treatment costs less than one penny per apple treated. At the end of the day, if the farmer is getting significant yield, from that product and its produce being enabled to being fresh longer, it's a no-brainer that the farmers would take that product in. It's really just a matter of getting approval. Again, this is a heavily regulated industry, but they have the leading technology. You already have a core business that has an 80% market share. They're diversifying a way into categories that should see, again, significant benefit, minimal economic risk, as it relates to economic cycles just really more weather variability.

To some extent, their businesses is working to help offset that.

For us, that's a name that not many people would have looked at. It's actually a term loan, but the term loan is the only debt in the structure. That was the only way we could participate. When we saw the business and got comfortable with, again, the business financial sustainability risks, it was something that we definitely found to be attractive.

Question 9

Paige: Marcus, where are you finding attractive opportunities in the market?

Marcus: We try to say this a lot, but I think the opportunity set has been consistent. We're finding opportunities where we always have. I keep track of this just for my own adaptation, but the median size of our issue in our portfolio is about $500 million. It's in a sweet spot where it's large enough to be liquid, but not large enough that the large money managers want to come in and take significant stakes in those positions. That leaves, the little bread crumbs for us, and we take all those crumbs we can. From that perspective, the opportunity set has been good.

More specifically, I think one of the key areas that we've been able to see a decent amount of opportunity is, I talked about the uncertainty around 2020, and so a lot of companies needed to issue that, to make sure they had the liquidity to get through that period. There was a good amount of debt issued by some very solid companies but at relatively high coupons. It also happened to be more likely to be five or six-year notes versus 7, 8, 9, or 10-year notes. We're a year removed, we have much more visibility and clarity. Then again, one of the things that as we've talked about being concerned about duration risk, well, high coupons in a low environment dampen that duration risk. They limit that duration volatility. We've been able to find some opportunities. I think we have coupons north of 9% or 9% or higher in our portfolio which is, that's like traditional high yield. That's the high yield I grew up on.

Venk: Those are getting refied before we even get off this call, probably.

Marcus: To your point just a minute ago, those will be the ones that get refinanced three months away but it's a part of the work. For us, I enjoy the work, we enjoy the work and that's what we're paid to do, is to do that work. It's good to see that there are companies out there

that give you the opportunity to really dig in and get real value. I think I want to make this point because you've made it but I think it's, I'll just say it this way. I'd rather have a 5% yielding piece of paper that has a two-year duration versus a 5% piece of paper right now that has a seven-year duration. To make it simple, those are the opportunities that we've been focused on, is that 5% yield with a much shorter duration profile versus something that has a similar yield but much longer duration.

Question 10

Paige: Venk, this is a risk question so I'm pushing it to you. **Where do you see the most risks in the market?**

Venk: Right now, in our opinion, the best risk to take in the market today is reinvestment risk. I would much rather earn that same 4% or whatever for one or two years and then have to reinvest it in two years, then tie it up for seven years in the same yield. Quite frankly, for many of our clients, that's the thesis of our short duration portfolio and why it's able to deliver lower volatilities in normalized markets and why it's able to deliver consistently because we're just constantly reinvesting as things come up, and we're investing into the current market. We're not taking that surprise duration risk.

Even when you compare to loans, we have a handful of very carefully selected loans in our portfolio but broader loan portfolios, floating-rate portfolios are at risk of long durations. People find that surprising, but it's because what you don't realize in a floating-rate portfolio is you have a short duration with respect to interest rates. We have really long timeframes and durations when it comes to sensitivity of credit spreads. They're asymmetric to the downside because loans can get repaid at basically at par at almost any time.

Let me unpack that real quick. A lot of people have already heard us talk about this, and we've written about it too, and we can point you at the right resources, but quickly simplifying it, a loan is a floating rate plus a spread and it's, call it a five to seven-year weighted average life. The spread component is actually not floating. When credit spreads move, your loan will move on this five to seven-year sensitivity even if it doesn't move as much when interest rates move. You're actually taking on long-duration risk with credit spreads. The problem is when credit spreads go down, you don't get the benefit of that because since the loan can get repaid at par, it's called constrained. You don't get the markup you'd get in a bond, you basically run up against this ceiling. Whereas if credit spreads go wider, then sure as hell, pardon my French, the loan pricing will drop. It's asymmetric to the downside.

What that means is a lot of loan portfolios look really attractive because they look like they're paying you a lot, because you can't get that markup of spread until the loan has been refinanced essentially into a lower spread. You don't get that price appreciation to benefit from the drop in credit spreads. You're essentially getting paid that extra amount for this asymmetry risk until it comes a time where the company just pays you down. It's like mortgages. At the end of the day, there's prepayment risk. It's a very similar concept to mortgage-backed securities with prepayment risk. When rates are low, there's a lot of

refinancing, durations are short. As soon as rates go up, people don't refinance as much and durations step out. By the time that happens, it's too late.

Now we're seeing a ton of issuance in CLOs. One article I read said that it was record levels of issuance, even compared to 2017's record levels because there's all this movement toward floating-rate securities. A quick plug for our short duration portfolio, the re-investment that takes place when you buy shorter-term bonds, you get a similar concept without taking on the really long-term credit risk and our duration unconstrained portfolio because we have the ability to really make decisions based on opportunity costs. It's a similar concept except we obviously then when duration does pay, we have the opportunity to take advantage of that and put that into the portfolio.

Question 11

Paige: Venk, do you have any concluding comments to wrap us up?

Venk: As Marcus mentioned, we are really, really happy with what the portfolio looks like. Generally, right now we have never been more excited about the businesses and the companies that we're invested in. People who've been with us for a while now, we started this firm 12 years ago. The mutual fund is five days away from being 10 years old, which is just crazy. It's not long before it's a teenager and starts rolling its eyes at us. It's particularly noticeable because right now, we're looking at our companies, we're seeing improving economies. We're seeing credits that are performing. We see all sorts of risks in the marketplace.

God, I don't know how to say this. There has never been a market for which what we do was designed for more perfectly. We're super excited about what we're doing and how we do it. Every day we come in and we look at what's in the portfolio and we look at the risks in the market, both rates going up risk. Duration risk, and credit risk because the economy might overheat and the market might get caught with its pants down. There's never been an environment where the fundamental work that we do, and the way we go about it, and the decision to focus on delivering a risk profile, not just an asset class, and not just a yield profile, hasn't felt more appropriate and a better fit for our clients than there is right now. We've loved what we've done for the last 10 years, but sitting right here and looking forward, I have the same excitement that we had when we sat in 2009 and 2000--. when we launched this firm in 2011 in particular, and I just looked forward and said, "My goodness."

I can't tell you when rates are going to go up. I can't tell you when duration is going to stop paying. I can't tell you what expected returns are going to be on in the duration product, but I know that you won't know when it's happened when that risk is accidentally hit you until after it's happened. By golly, I love where we're sitting. We've been very lucky. This market has been even as something in the last six months that I don't think we could have even asked for. It has shown us there's so many irresponsible ways to make money that it's not about missing one trade, or missing another trade, or not having a Bitcoin portfolio, and not owning stacks, or not buying ETFs at the bottom of the market. These things aren't mistakes, they're discipline.

There are so many irresponsible ways to make money, so many ways to make money that make no sense, so many places to make money that you're probably looking at each other going like, "Wow, what is this?" There's an opportunity to do better. There's an opportunity to be intentional, to actually set out to deliver something and deliver it, not because we held our noses and took a risk we didn't want to take, but because we're actually taking only the risks we want to take and still delivering on it. For us, that's what we aim to deliver, is a portfolio that allows our clients to feel that way, to say, "I know what I'm getting, and they told me what I'm getting, and they've been transparent about it, and they've explained it, and probably talked my ear off way too much about it. I know what I'm getting, and they gave it to me, and they told me what they had hoped to deliver from the beginning, even when it deviates from what we thought it was going to look like."

With that, I think I'm just going to leave it at that. There's never been a market that's more appropriate for what we do, in our view. This is why we exist, this is why Zeo was started. This was in post-2008, we had clients who needed income, wanted reasonable returns, and wanted to know what they owned, and wanted to mitigate these very risks. These are the markets that I started this business for. This is the reason we're one of the only firms doing what we do. There's a lot of short duration managers out there, there are a lot of credit managers out there, but delivering it the way we deliver it, there's a reason for that. We look forward to the opportunity to talk to you more about that.

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