

# BAY COUNTY EMPLOYEES' RETIREMENT SYSTEM INVESTMENT REVIEW

OCTOBER 24, 2013

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## Convertible

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**EDWARD SILVERSTEIN, CFA**

Senior Managing Director  
Head of Convertible Division



MACKAYSHIELDS

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# MacKay Shields: A Leader in Income-Oriented Investing

## About Us

### Experience & Quality

With over 40 years of experience, we are committed to partnering with our clients to deliver:

- Tailored income-oriented investment solutions based on their goals and objectives
- The highest levels of client service and consistent investment performance

### Our People

A firm comprised of approximately 145 dedicated employees, including 48 investment professionals

### Our Approach

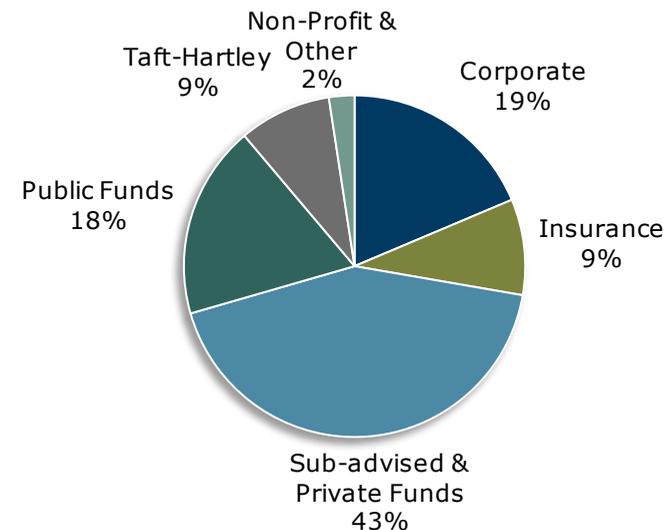
Investment teams recognize and integrate the importance of capital preservation into all of their investment philosophies

### Long-Term Commitment

Similar to our investment approach, we take a long-term perspective toward our clients, their portfolios and our business

Total Assets Under Management: \$77.7B<sup>1</sup>

### By Client Type



<sup>1</sup>AUM shown is as of September 30, 2013. In respect to AUM by client type, due to rounding the sum of the items may not equal 100% or any expressed totals as applicable. Investment goals may not be achieved and past performance is no guarantee of future results.

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## Investment Objectives and Guidelines

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### **Investment Guidelines:**

The investment objective is to seek long term growth of capital together with current income.

### **Benchmark:**

Merrill Lynch Investment Grade Bonds Only plus 1%

### **Peer Group:**

Becker Burke Convertible Portfolio Universe

### **Primary Investment Focus:**

The account will invest primarily in domestic convertible securities such as bonds, debentures, corporate notes, and preferred stocks or other securities, i.e. synthetics that are convertible into common stock or the cash value of stock or a basket or index of equity securities. Any equity security received in the portfolio resulting from a conversion will be liquidated in an orderly and timely fashion as determined by the investment manager. Typically equities will not be purchased out right but would be in the portfolio as a result of another holding.

The account will be limited to invest up to 20% of the portfolio in convertible preferred stocks or other securities.

Rule 144A securities, convertible debt and equity, are permitted.

The account shall have an overall rating of "A" or better from either rating agency. Individual investment grade fixed income securities shall have at a minimum a Moody's rating of "Baa3" or a Standard & Poors rating of "BBB-".

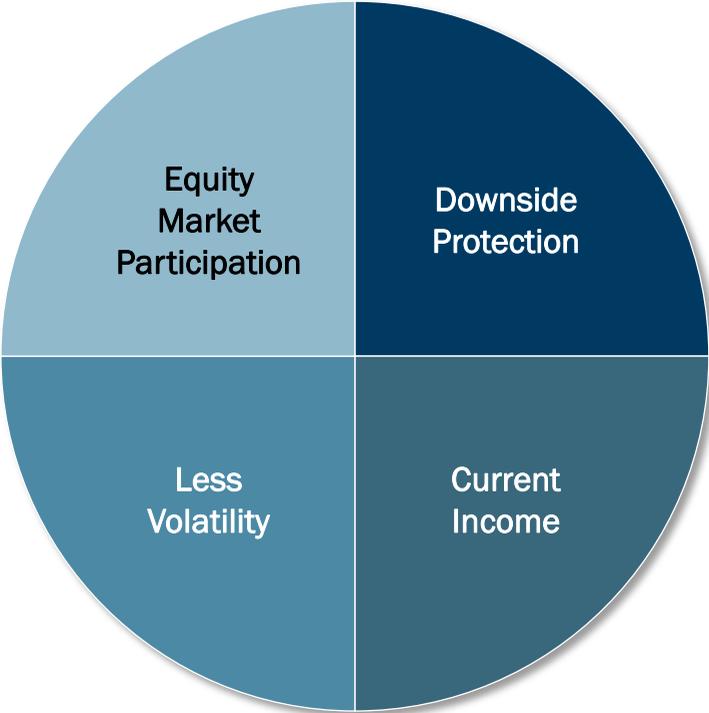
The account is allowed to invest up to 20% of the portfolio in non-investment grade domestic convertible securities as identified above, however individual securities shall have at a minimum a "B" rating as determined by Moody's and Standard & Poors. The lowest of the two ratings shall prevail. The account shall divest itself of all securities rated below "B" from either rating agency within 60 days of the reduction.

If any non-investment grade securities are convertible preferreds they will be applied against both 20% maximums.

### **Performance Objectives:**

To outperform the benchmark net of fees and to rank within the top one-third of the peer group over a 3 - 5 year period as identified above.

# Benefits of Investing in Convertibles



This document is for informational purposes only. Portfolios are actively managed and all expressions of opinion are subject to change without notice and are not intended to be a guarantee of future events.



## Objective

Seek to maximize total return by outperforming the market and our competition while protecting against downside risk

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## Philosophy

- Convertibles provide a means of obtaining exposure to the equity markets while emphasizing the protection of principal
  - Identify securities that offer an asymmetric risk/return profile
  - Target the “total return” instrument
- 



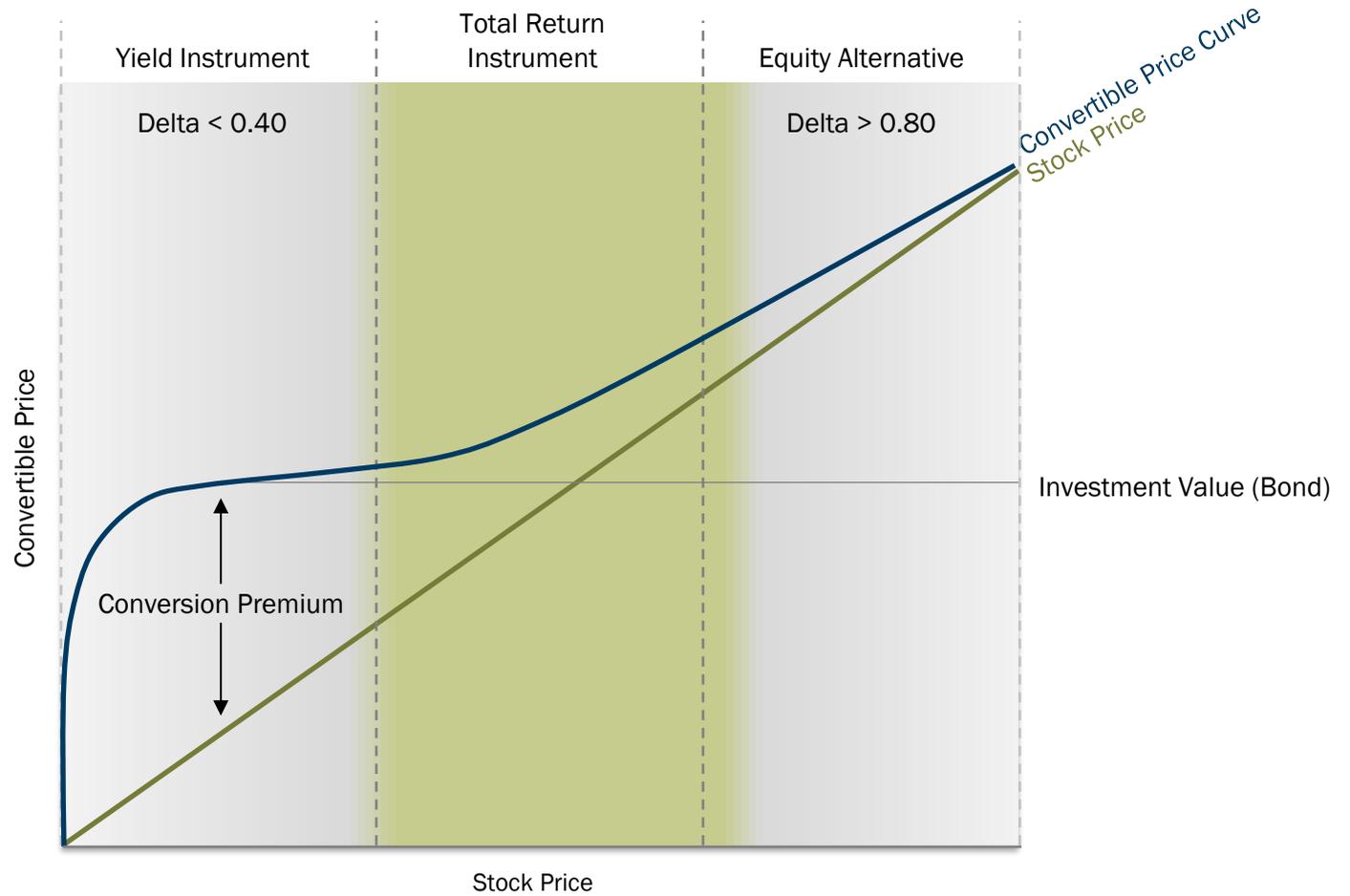
## Discipline

- Fundamental research driven
- Evaluate downside and upside potential
- Invest in convertibles with the best risk/reward profile
- Construct well-diversified portfolio
- Strict sell discipline

## Target the “Total Return” Instrument

*Total Return =  
Yield + Price Appreciation*

*We aim to own convertibles  
which may participate in 60-80%  
of the common stock's upside,  
while limiting downside  
participation to  
30-50% of the stock's decline.*





## Objectives

- Exclude Illiquid Convertibles
- Target Balanced Convertibles
- Reduce Risk
- Stress Test
- Up/Down Market Capture to Identify Asymmetry of Returns
- Determine Timelines of Investments
- Complement Our Quantitative Tests with Fundamental Analysis
- Accumulate Convertibles with the Best Risk/Reward Profile and Favorable Company Fundamentals

## Criteria

- Generally Equity Market Cap Above \$300 Million and at Least \$100 Million of Convertible Bonds Issued
- Equity Sensitivity
- Model 60-80% Upside/30-50% Downside
- Bond Value
- Conversion Premium
- Internal Credit Research
- Valuation
- Positive Earnings Trend
- Free Cash Flow
- Positive Fundamental Change in Industry and/or Company
- In-Depth Analysis
- Company Contact
- Insider Buying/Ownership
- ~50-70 Companies

Screening Objectives with an Emphasis on Risk Management

- Apply fundamental research investment process
- Identify the risk/reward of the convertible relative to the underlying common stock
- Adhere to client guidelines
- Accumulate convertibles with best risk/reward profile
- Diversify among sectors
- Set price target
- Follow proven sell discipline
  - Change in fundamentals
  - Valuation
    - Free cash flow yield or P/E out of line with growth rate
    - Free cash flow yield or P/E out of line with peer group
    - Free cash flow yield or relative P/E outside of historical range

# Convertible Investment Team

| Name   | Years of Investment Experience | Investment Experience                         | Education   |
|--|--------------------------------|---|---|
| <b>Edward Silverstein, CFA</b><br><i>Senior Managing Director</i><br><i>Portfolio Manager/Research Analyst</i> | 18                             | Bank of New York<br>New York Stock Exchange   | Brooklyn Law School, JD<br>Baruch College, MBA<br>University of Vermont, BS |
| <b>Elizabeth Xu</b><br><i>Director</i><br><i>Portfolio Manager/Research Analyst</i>                            | 16                             | Epic Partners<br>Deutsche Bank<br>J.P. Morgan | Harvard Business School, MBA<br>Mount Holyoke College, BA                   |
| <b>Scott Mallek</b><br><i>Director</i><br><i>Trader</i>  | 17                             | Salomon Smith Barney                          | Fairfield University, BA  |
| <b>J. Alex Leites</b><br><i>Associate Director</i><br><i>Trader</i>  | 20                             | Credit Suisse First Boston                    | New York University, BS   |

## Research Efforts Supported by the High Yield Investment Team<sup>1</sup>

|  |  |  |   |   |   |
|--|--|--|---|---|---|
| <b>J. Matthew Philo, CFA</b><br><i>Senior Managing Director</i><br><i>Lead Portfolio Manager</i> | <ul style="list-style-type: none"> <li>▪ Generalist</li> </ul>   | <b>Andrew Susser</b><br><i>Managing Director</i><br><i>Portfolio Manager/Analyst</i> | <ul style="list-style-type: none"> <li>▪ Food</li> <li>▪ Gaming &amp; Leisure</li> <li>▪ Lodging</li> <li>▪ Retail</li> <li>▪ Services</li> </ul> | <b>Won Choi, CFA</b><br><i>Director</i><br><i>Analyst/Portfolio Manager</i> | <ul style="list-style-type: none"> <li>▪ Chemicals</li> <li>▪ Metals</li> <li>▪ Paper &amp; Packaging</li> </ul>                    |
| <b>Nate Hudson, CFA</b><br><i>Managing Director</i><br><i>Portfolio Manager/Analyst</i>          | <ul style="list-style-type: none"> <li>▪ Automotive/Transportation</li> <li>▪ Building Materials</li> <li>▪ Homebuilding</li> </ul>                      | <b>James S. Wolf</b><br><i>Managing Director</i><br><i>Portfolio Manager/Analyst</i> | <ul style="list-style-type: none"> <li>▪ Finance</li> <li>▪ Health Care</li> </ul>  | <b>Eric Gold</b><br><i>Director</i><br><i>Analyst/Portfolio Manager</i>     | <ul style="list-style-type: none"> <li>▪ Media-Cable TV/Broadcasting</li> <li>▪ Technology</li> <li>▪ Telecommunications</li> </ul> |
| <b>Michael A. Snyder</b><br><i>Managing Director</i><br><i>Portfolio Manager/Analyst</i>         | <ul style="list-style-type: none"> <li>▪ Aerospace/Defense</li> <li>▪ Consumer Products</li> <li>▪ Manufacturing</li> <li>▪ Media-Diversified</li> </ul> | <b>Dohyun Cha, CFA</b><br><i>Director</i><br><i>Analyst/Portfolio Manager</i>        | <ul style="list-style-type: none"> <li>▪ Energy</li> <li>▪ Utilities</li> </ul>   | <b>Thomas Metcalf</b><br><i>Associate</i><br><i>Research Analyst</i>        | <ul style="list-style-type: none"> <li>▪ Generalist</li> </ul>  |

<sup>1</sup>As needed.

# Bay County Employees' Retirement System



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**Asset Allocation**  
September 30, 2013  
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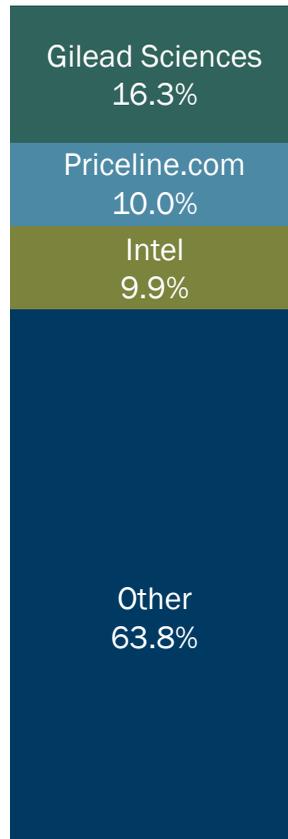
|                   | <b>Market Value</b> | <b>Percent</b> |
|-------------------|---------------------|----------------|
| Convertible Bonds | \$12,207,335        | 72.96%         |
| Preferreds        | \$2,262,619         | 13.52%         |
| Cash              | \$2,262,146         | 13.52%         |
| <b>Total Fund</b> | <b>\$16,732,100</b> | <b>100.00%</b> |

# BofA ML Convertible Investment Grade Bonds Index Composition and Returns

## Gilead Sciences Percent of Index

As of September 30, 2013

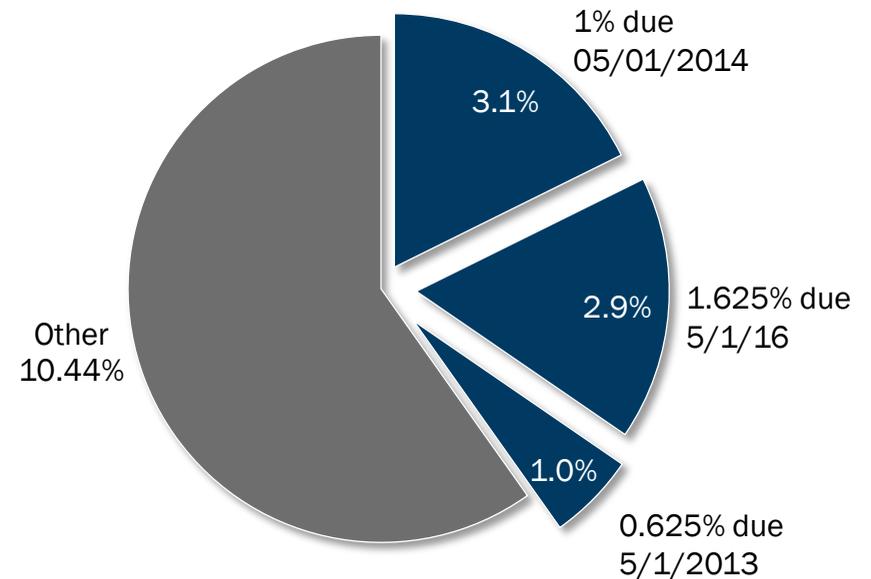
- Gilead represents a disproportionate portion of the Index.
- Several other issuers including Priceline.com and Intel also carry large weights in the index.



## Gilead Sciences Contribution to Index Return

Year to Date Ending September 30, 2013

|                               |        |
|-------------------------------|--------|
| Year to Date Index return     | 17.45% |
| Gilead Contribution to Return | 7.01%  |



# Bay County Employees' Retirement System

## Historical Rates of Return

|                   | Bay County Employees'<br>Retirement System <sup>1</sup> | BofA Merrill Lynch<br>Convertible Investment<br>Grade Bonds Index | BofA Merrill Lynch<br>Convertible Investment<br>Grade Bonds Index +1% | BofA Merrill Lynch Convertible<br>All Investment Grade Index<br>(includes Convertible Preferred<br>Securities) |
|-------------------|---|---|---|--|
| 2012              | 8.0   | 10.0  | 11.0  | 11.9   |
| 2011              | -1.1  | -3.6  | -2.6  | -3.1   |
| 2010              | 9.5   | 7.4   | 8.4   | 7.9  |
| 2009              | 25.5  | 28.6  | 29.6  | 25.5   |
| 2008              | -25.8   | -15.2   | -14.2   | -31.6  |
| 2007              | 15.3  | 7.9   | 8.9   | 5.8  |
| 2006              | 7.5   | 7.3   | 8.3   | 8.6  |
| 2005              | 7.4   | 0.5   | 1.5   | 1.9  |
| 2004              | 4.9   | 4.7   | 5.7   | 7.1  |
| 2003 <sup>2</sup> | 7.2   | 5.2   | n/a   | 5.8  |

| Periods ending<br>September 30, 2013                | Bay County Employees'<br>Retirement System <sup>1</sup> | BofA Merrill Lynch<br>Convertible Investment<br>Grade Bonds Index | BofA Merrill Lynch<br>Convertible Investment<br>Grade Bonds Index +1% | BofA Merrill Lynch Convertible<br>All Investment Grade Index<br>(includes Convertible Preferred<br>Securities) |
|---|---|---|---|--|
| Year to Date  | 12.73   | 17.45   | n/a   | 15.71  |
| Since Inception - Annualized<br>(10/1/03 - 8/31/12) | 6.27  | 6.45  | 7.45  | 4.42   |

<sup>1</sup>Gross of fees

<sup>2</sup>From 10/1/03 - 12/31/03

Past performance is not indicative of future results.

# Bay County Employees' Retirement System

(as of September 30, 2013)

## Portfolio Characteristics

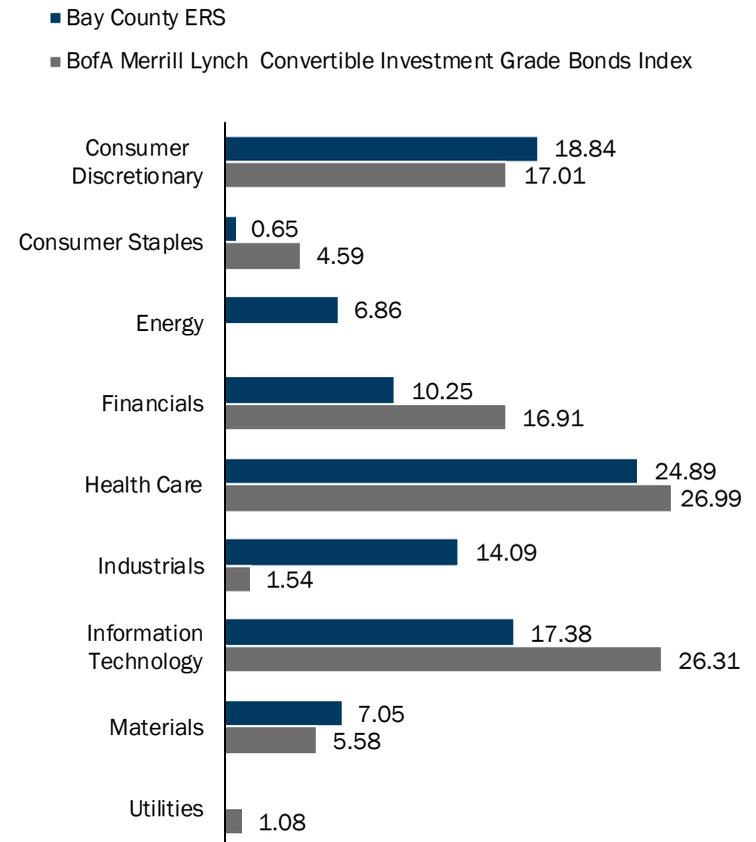
|                             | MacKay Shields      | BofA Merrill Lynch Convertible Grade Bonds Index |
|-----------------------------|---------------------|--|
| Years to Effective Maturity | 5.96                | n/a  |
| Current Yield               | 1.47%               | 1.81%  |
| Yield to Effective Maturity | 1.83%               | n/a  |
| Delta                       | 0.71 <sup>1</sup>   | 0.74   |
| Conversion Premium          | 32.53% <sup>1</sup> | 13.82%   |
| Average Quality             | A-                  | BBB+   |
| Number of Holdings          | 41                  | 56   |

## Credit Concentration

|     | MacKay Shields | BofA Merrill Lynch Convertible Grade Bonds Index |
|-----|----------------|--|
| AAA | 18.46          | 0.50   |
| AA  | 0.00           | 0.00   |
| A   | 33.77          | 43.92  |
| BBB | 33.11          | 55.58  |
| BB  | 8.56           | 0.00   |
| B   | 6.11           | 0.00   |

## Portfolio Sector Breakdown

vs. BofA Merrill Lynch Convertible Grade Bonds Index (% Market Value)



<sup>1</sup>Source: Bloomberg

Index data source: BofA Merrill Lynch Convertible Research

# Bay County Employees' Retirement System

Convertible Portfolio



# Bay County Employees' Retirement System



## Summary Report — Account 1256

September 30, 2013

|                    | Total<br>Cost       | Percent<br>at Cost | Yield<br>at Cost | Market<br>Value     | Percent<br>of Assets | Yield<br>at Market | Annual<br>Income |
|--------------------|---------------------|--------------------|------------------|---------------------|----------------------|--------------------|------------------|
| Bonds              | 10,176,128          | 85.53              | 1.78             | 12,157,710          | 72.66                | 1.49               | 181,110          |
| Stocks             | 1,720,986           | 14.47              | 3.55             | 2,261,077           | 13.51                | 2.70               | 61,157           |
| Cash & Equivalents | 0                   | 0.00               |                  | 2,262,146           | 13.52                | 0.09               | 2,036            |
| Accrued Income     |                     |                    |                  | 51,166              | 0.31                 |                    |                  |
|                    | <b>\$11,897,113</b> | <b>100.00%</b>     | <b>2.04</b>      | <b>\$16,732,100</b> | <b>100.00%</b>       | <b>1.46</b>        | <b>\$244,302</b> |

# Bay County Employees' Retirement System



## Holdings Report — Account 1256

September 30, 2013

| Shares<br>or<br>Par Value | Security                             | Unit<br>Cost | Total<br>Cost | Current<br>Price | Market<br>Value | Percent<br>of Assets | Yield      | Annual<br>Income | S & P |         |      |
|---------------------------|--------------------------------------|--------------|---------------|------------------|-----------------|----------------------|------------|------------------|-------|---------|------|
| <b>Bonds</b>              |                                      |              |               |                  |                 |                      |            |                  |       |         |      |
| 228,000                   | AIRTRAN HOLDINGS INC CONV BOND       | 5.250        | 11/01/2016    | 136.07           | 310,248         | 149.06               | 339,863    | 2.03             | 3.52  | 11,970  | BBB- |
| 37,000                    | ALCOA INC CONV BOND                  | 5.250        | 03/15/2014    | 100.00           | 37,000          | 129.00               | 47,730     | 0.29             | 4.07  | 1,943   | BBB- |
| 451,000                   | ALLEGHENY TECHNOLOGIES CONV BOND REG | 4.250        | 06/01/2014    | 116.52           | 525,524         | 104.13               | 469,604    | 2.81             | 4.08  | 19,168  | BBB- |
| 690,000                   | ALZA CORP CONV BOND 07/28/2020       |              |               | 81.14            | 559,876         | 119.69               | 825,844    | 4.94             | 0.00  | 0       | AAA  |
| 303,000                   | APOLLO INVESTMENT CORP REG CONV BOND | 5.750        | 01/15/2016    | 100.49           | 304,499         | 106.00               | 321,180    | 1.92             | 5.42  | 17,423  | BBB  |
| 292,000                   | ARES CAPITAL CORP REG CONV BOND      | 5.750        | 02/01/2016    | 106.39           | 310,648         | 107.88               | 314,995    | 1.88             | 5.33  | 16,790  | BBB  |
| 68,000                    | BLUCORA INC 144A                     | 4.250        | 04/01/2019    | 100.23           | 68,156          | 125.88               | 85,595     | 0.51             | 3.38  | 2,890   | NR   |
| 169,000                   | CHART INDUSTRIES INC                 | 2.000        | 08/01/2018    | 135.55           | 229,072         | 186.63               | 315,396    | 1.88             | 1.07  | 3,380   | B+   |
| 137,000                   | CUBIST PHARMACEUTICALS 144A          | 1.125        | 09/01/2018    | 100.00           | 137,000         | 108.31               | 148,388    | 0.89             | 1.04  | 1,541   | NR   |
| 177,000                   | CUBIST PHARMACEUTICALS 144A          | 1.875        | 09/01/2020    | 100.00           | 177,000         | 107.88               | 190,939    | 1.14             | 1.74  | 3,319   | NR   |
| 419,000                   | DANAHER CORP CNV BND REG             |              | 01/22/2021    | 101.16           | 423,870         | 201.63               | 844,809    | 5.05             | 0.00  | 0       | A+   |
| 412,000                   | EMC CORP CONV BOND REG               | 1.750        | 12/01/2013    | 139.96           | 576,637         | 159.88               | 658,687    | 3.94             | 1.09  | 7,210   | A    |
| 322,000                   | GILEAD SCIENCES INC CONV BOND REG    | 1.000        | 05/01/2014    | 107.88           | 347,385         | 278.56               | 896,971    | 5.36             | 0.36  | 3,220   | A-   |
| 95,000                    | HELIX ENERGY SOLUTIONS CONV BOND REG | 3.250        | 03/15/2032    | 112.50           | 106,875         | 133.69               | 127,003    | 0.76             | 2.43  | 3,088   | NR   |
| 443,000                   | INTEL CORP CONV BND REG              | 2.950        | 12/15/2035    | 100.57           | 445,514         | 108.50               | 480,655    | 2.87             | 2.72  | 13,069  | A-   |
| 493,000                   | INTEL CORP CONV BOND                 | 3.250        | 08/01/2039    | 125.25           | 617,485         | 124.00               | 611,322    | 3.65             | 2.62  | 16,023  | A-   |
| 359,000                   | INTL GAME TECHNOLOGY REG CONV BND    | 3.250        | 05/01/2014    | 115.44           | 414,421         | 110.75               | 397,593    | 2.38             | 2.93  | 11,668  | BBB  |
| 118,000                   | KB HOME REG                          | 1.375        | 02/01/2019    | 104.79           | 123,655         | 102.06               | 120,434    | 0.72             | 1.35  | 1,623   | B    |
| 126,000                   | MICROCHIP TECHNOLOGY CONV BOND REG   | 2.125        | 12/15/2037    | 125.92           | 158,661         | 157.19               | 198,056    | 1.18             | 1.35  | 2,678   | NR   |
| 120,000                   | MICRON TECHNOLOGY INC CONV BOND 144A | 1.625        | 02/15/2033    | 125.63           | 150,758         | 170.25               | 204,300    | 1.22             | 0.95  | 1,950   | BB-  |
| 291,000                   | NEWMONT MINING CONV BND REG          | 1.625        | 07/15/2017    | 121.45           | 353,418         | 110.50               | 321,555    | 1.92             | 1.47  | 4,729   | BBB+ |
| 48,000                    | NUANCE COMMUNICATIONS CONV BOND REG  | 2.750        | 11/01/2031    | 106.17           | 50,962          | 101.56               | 48,750     | 0.29             | 2.71  | 1,320   | BB-  |
| 493,000                   | OMNICOM GROUP INC                    |              | 07/31/2032    | 111.66           | 550,486         | 120.94               | 596,222    | 3.56             | 0.00  | 0       | BBB+ |
| 553,000                   | PRICELINE.COM INC CONV BOND REG      | 1.000        | 03/15/2018    | 113.18           | 625,877         | 129.00               | 713,370    | 4.26             | 0.78  | 5,530   | BBB  |
| 126,000                   | RTI INTERNATIONAL METALS REG         | 1.625        | 10/15/2019    | 103.06           | 129,850         | 104.00               | 131,040    | 0.78             | 1.56  | 2,048   | NR   |
| 48,000                    | RYLAND GROUP REG                     | 0.250        | 06/01/2019    | 100.00           | 48,000          | 91.75                | 44,040     | 0.26             | 0.27  | 120     | BB-  |
| 556,000                   | SCHLUMBERGER                         |              | 05/05/2015    | 136.47           | 758,773         | 155.52               | 864,691    | 5.17             | 0.00  | 0       | NR   |
| 180,000                   | TELEFLEX INC CONV BOND REG           | 3.875        | 08/01/2017    | 101.42           | 182,550         | 141.31               | 254,363    | 1.52             | 2.74  | 6,975   | BB-  |
| 597,000                   | TEVA PHARMACEUTICALS CONV BOND       | 0.250        | 02/01/2026    | 112.35           | 670,730         | 104.19               | 621,999    | 3.72             | 0.24  | 1,493   | A-   |
| 72,000                    | WABASH NATIONAL CORP CONV BOND       | 3.375        | 05/01/2018    | 121.62           | 87,568          | 131.06               | 94,365     | 0.56             | 2.58  | 2,430   | NR   |
| 511,000                   | WELLPOINT INC 144A                   | 2.750        | 10/15/2042    | 101.68           | 519,573         | 127.81               | 653,122    | 3.90             | 2.15  | 14,053  | A-   |
| 132,000                   | XILINX INC                           | 2.625        | 06/15/2017    | 131.86           | 174,059         | 162.75               | 214,830    | 1.28             | 1.61  | 3,465   | BBB+ |
|                           |                                      |              |               |                  | 10,176,128      |                      | 12,157,710 | 72.66            | 1.49  | 181,110 | BBB- |

# Bay County Employees' Retirement System



## Holdings Report — Account 1256

September 30, 2013

| Shares<br>or<br>Par Value     | Security                                | Unit<br>Cost | Total<br>Cost       | Current<br>Price | Market<br>Value     | Percent<br>of Assets | Yield       | Annual<br>Income | S & P       |
|-------------------------------|---|--------------|---------------------|------------------|---------------------|----------------------|-------------|------------------|-------------|
| <b>Stocks</b>                 |   |              |                     |                  |                     |                      |             |                  |             |
| 99                            | BANK OF AMERICA 7.250%                  | 830.69       | 82,238              | 1,080.00         | 106,920             | 0.64                 | 6.71        | 7,178            | BB+         |
| 2,100                         | CLIFFS NATURAL RESOURCES                | 25.00        | 52,500              | 19.77            | 41,517              | 0.25                 | 0.00        | 0                | NR          |
| 2,100                         | GOODYEAR TIRE & RUBBER                  | 51.28        | 107,691             | 63.68            | 133,728             | 0.80                 | 4.61        | 6,170            | NR          |
| 1,000                         | HEALTH CARE REIT 6.500 CNV PFD          | 50.00        | 50,000              | 57.66            | 57,656              | 0.34                 | 5.64        | 3,250            | BB+         |
| 1,000                         | MAIDEN HOLDINGS CNV PFD                 | 50.00        | 50,000              | 49.62            | 49,620              | 0.30                 | 0.00        | 0                | NR          |
| 900                           | POST HOLDINGS INC 144A                  | 100.00       | 90,000              | 104.13           | 93,717              | 0.56                 | 0.00        | 0                | NR          |
| 5,200                         | STANLEY BLACK & DECKER I CONV PFD UNITS | 108.87       | 566,110             | 137.38           | 714,376             | 4.27                 | 3.90        | 27,872           | NR          |
| 6,700                         | UNITED TECHNOLOGIES CORP CONV PFD       | 56.54        | 378,846             | 65.36            | 437,912             | 2.62                 | 2.87        | 12,563           | BBB+        |
| 550                           | WELLS FARGO & COMPANY 7.500%            | 624.73       | 343,600             | 1,137.51         | 625,631             | 3.74                 | 0.66        | 4,125            | BBB+        |
|                               |   |              | <u>1,720,986</u>    |                  | <u>2,261,077</u>    | <u>13.51</u>         | <u>2.70</u> | <u>61,157</u>    | <u>B-</u>   |
| <b>Cash &amp; Equivalents</b> |   |              |                     |                  |                     |                      |             |                  |             |
|                               | UNITED STATES DOLLAR 0.0900             | 0.00         | 2,262,146           | 1.00             | 2,262,146           | 13.52                | 0.09        | 2,036            | AAA         |
|                               |   |              | <u>2,262,146</u>    |                  | <u>2,262,146</u>    | <u>13.52</u>         | <u>0.09</u> | <u>2,036</u>     | <u>AAA</u>  |
|                               | Accrued Income                          |              |                     |                  | 51,166              | 0.31                 |             |                  |             |
| <b>Total Portfolio</b>        |   |              | <u>\$14,159,260</u> |                  | <u>\$16,732,100</u> | <u>100.00%</u>       | <u>1.46</u> | <u>\$244,302</u> | <u>BBB-</u> |

# Appendix



# Convertible Investment Grade: Performance

## Preliminary Composite Returns (%)

Periods Ending September 30, 2013

|                       | <b>Mackay Shields<br/>Composite<sup>1</sup></b> | <b>BofA Merrill Lynch<br/>Investment Grade<br/>Convertible Index</b> |
|-----------------------|---|--|
| September             | 2.7   | 2.5  |
| Third Quarter 2013    | 6.2   | 6.5  |
| Year-to-Date          | 13.8  | 15.7   |
| 1 Year                | 14.9  | 16.4   |
| 3 Years - Annualized  | 9.1   | 9.3  |
| 5 Years - Annualized  | 8.7   | 9.2  |
| 7 Years - Annualized  | 6.1   | 3.6  |
| 10 Years - Annualized | 6.5   | 4.4  |

<sup>1</sup>Gross of fees, Convertible Investment Grade Composite  
See GIPS-compliant presentation following. The above returns are unaudited and subject to change.

# Convertible Investment Grade: Performance Composite Disclosures

| Period            | MacKay Shields<br>Composite <sup>1</sup><br>(%) | BofA Merrill Lynch<br>Investment Grade<br>Convertible Index<br>(%) | Composite<br>3-Yr St Dev<br>(%) | Benchmark<br>3-Yr St Dev<br>(%) | Firm Assets<br>(\$Mil) |
|-------------------|---|--|---------------------------------|---------------------------------|------------------------|
| 2013 (Thru 6/30)  | 7.2   | 8.6  | 7.9                             | 7.8                             | 75,983                 |
| 2012              | 8.9   | 11.9   | 8.6                             | 8.1                             | 78,371                 |
| 2011              | -2.3  | -3.1   | 9.6                             | 9.5                             | 58,115                 |
| 2010              | 10.9  | 7.9  | 15.7                            | 16.1                            | 54,319                 |
| 2009              | 27.9  | 25.5   | 15.1                            | 15.8                            | 43,197                 |
| 2008              | -26.4   | -31.6  | 14.1                            | 14.1                            | 28,370                 |
| 2007              | 15.3  | 5.8  | 5.3                             | 5.0                             | 38,094                 |
| 2006              | 7.5   | 8.6  | 4.7                             | 4.3                             | 40,074                 |
| 2005              | 6.8   | 1.9  | N/A                             | N/A                             | 38,329                 |
| 2004              | 4.9   | 7.1  | N/A                             | N/A                             | 39,208                 |
| 2003 (Since 10/1) | 7.2   | 5.8  | N/A                             | N/A                             | 37,771                 |

<sup>1</sup>Gross of fees

The Convertible Investment Grade Composite includes all discretionary convertible investment grade accounts managed with similar objectives for a full month, including those accounts no longer with the firm. This strategy primarily consists of convertible securities such as bonds, debentures, corporate notes, and preferred stocks or other securities that are convertible into common stock or the cash value of a stock or a basket or index of equity securities. A majority of the strategy's total assets will be invested in securities that are rated investment grade or, if unrated, that we determine to be of comparable quality. Composite performance reflects reinvestment of income and dividends and is a market-weighted average of the time-weighted return, before advisory fees and related expenses, of each account for the period since inception. Policies for valuing portfolios, calculating performance, and preparing compliant presentations are available upon request. Performance is expressed in US Dollars. The composite inception date is 10/1/03. The composite creation date is 1/1/05. Advisory fees, which are described in the firm's ADV, Part 2A, and related expenses will reduce returns. For example, in flat markets a .50% annual investment advisory fee, our highest fee, applied quarterly, would have the effect of reducing the annual compound return by .50% in the first year and by a cumulative 2.53% in the fifth year. All portfolios in the composite are fee-paying portfolios. There can be no assurance that the rate of return for any account within a composite will be the same as that of the composite presented. Past performance is not indicative of future results.

MacKay Shields LLC, an SEC-registered investment adviser, claims compliance with the Global Investment Performance Standards (GIPS®) and has prepared and presented this report in compliance with the GIPS standards. The firm has been independently verified from January 1, 1988 through December 31, 2012. The verification report is available upon request. Verification assesses whether (1) the firm has complied with all the composite construction requirements of the GIPS standards on a firm-wide basis and (2) the firm's policies and procedures are designed to calculate and present performance in compliance with the GIPS standards. Verification does not ensure the accuracy of any specific composite presentation. A complete list of composite descriptions is available upon request. Indices do not incur management fees, transaction costs or other operating expenses. Investments cannot be made directly into an index. The BofA Merrill Lynch Investment Grade Convertibles Index is referred to for comparative purposes only and is not intended to parallel the risk or investment style of the portfolios in the MacKay Shields Composite. Internal dispersion is calculated using the equal-weighted standard deviation of annual gross returns of those portfolios that were included in the composite for the entire year. The three-year annualized standard deviation measures the variability of the composite and the index returns over the preceding 36-month period. The standard deviation is not presented for periods prior to 2006 because the composite did not have a three-year track record.

June 30, 2013 number of accounts and composite assets (mil) were: 11, \$69. Year-end number of accounts, composite assets (mil) and internal dispersion were: 2012, 16, \$130, 1.0; 2011, 17, \$126, 0.9; 2010, 16, \$126, 0.9; 2009, 13, \$78, 0.8; 2008, 7, \$29, 0.0; 2007, five or fewer, \$22, 0.0; 2006, five or fewer, \$19, 0.0; 2005, five or fewer, \$18, 0.0; 2004, five or fewer, \$15, 0.0; 2003, five or fewer, \$14, N/A.

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## Convertible Team

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### **Edward Silverstein, CFA**

*Senior Managing Director  
Portfolio Manager/Research Analyst  
Head of Convertible*

Edward Silverstein is a Senior Managing Director and Head of Convertibles, where he oversees the management and research of the firm's Convertible strategy. He is a member of the firm's Advisory Committee. Edward joined MacKay Shields as a Research Analyst in 1998, becoming a Portfolio Manager/Research Analyst in 1999. Prior to joining MacKay Shields, he worked as a Portfolio Manager and Law Clerk at the Bank of New York. He also interned at the New York Stock Exchange Enforcement Division.

He has a BS from the University of Vermont, an MBA from the Baruch College and a JD from Brooklyn Law School. He is a CFA charterholder and also a member of the New York State Bar. He authored, *Wise Up!: A Portfolio Manager's Guide to Better Investment Decisions*. He has been working in the investment industry since 1995.

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### **Elizabeth Xu**

*Director  
Portfolio Manager/Research Analyst*

Elizabeth Xu is a Director, Portfolio Manager and Research Analyst for the Convertibles Team, where she follows multiple sectors including telecom, media, technology, industrial and financials (ex REITs). Prior to joining MacKay Shields in 2007, she worked for the private equity firm Epic Partners, where she served as a research investment analyst following multiple sectors. She has also worked at Deutsche Bank and J.P. Morgan Securities.

Elizabeth earned a BA magna cum laude from Mount Holyoke College and an MBA from Harvard Business School. She began working in the investment industry in 1997.

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### **Scott Mallek**

*Director  
Trader*

Scott joined MacKay Shields in 2002 after spending six years with Salomon Smith Barney, where he was an Assistant Vice President involved with IFG High Yield Trading. Scott received a BA in Economics from Fairfield University and has been in the investment management industry since 1996.

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### **J. Alex Leites**

*Associate Director  
Trader*

Alex joined MacKay Shields in 2002 from Credit Suisse First Boston where he was a Settlements Specialist. Alex was previously affiliated with Kinexus, Inc. and Bank of New York. Earlier in his career he was with Lazard Asset Management and Prudential Securities. Alex has a BS in Economics and Business Management from New York University's Stern School of Business and has been in the investment management industry since 1993.

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## Senior Management

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### **Jeffrey Phlegar**

*Chairman & Chief Executive Officer*

Jeffrey Phlegar is Chairman and Chief Executive Officer, responsible for setting the firm's strategy and leading the organization as it implements these goals across its fixed income business. This includes oversight of the portfolio management teams, enterprise risk, sales and new product development. He is a member of the firm's Board of Managers and leads the Advisory Committee. He joined MacKay Shields in December 2011 after 18 years of service at AllianceBernstein, where he served most recently as president of Special Opportunities and Advisory Services, responsible for building a variety of new business initiatives, including the firm's new alternatives platform. From 2004 to 2008, Jeff co-led AllianceBernstein's fixed income division as executive vice president and chief investment officer. In this role, he was responsible for overseeing all aspects of the firm's fixed income business, including oversight of its portfolio management, research and risk management teams, client relationships worldwide, as well as the development and implementation of new products and successful strategies for distribution, servicing and technology/operations.

Jeff's previous roles at AllianceBernstein included serving as Director of U.S. Fixed Income and Insurance, Director of Liquid Markets/MBS and portfolio manager for Taxable Fixed Income & Insurance. Prior to joining AllianceBernstein in 1993, he had portfolio manager responsibilities at Equitable Capital Management and served as a fixed income product specialist at Dreyfus Corporation.

He earned his MBA from Adelphi University and a BBA at Hofstra University. He has been working in the investment industry since 1987.

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### **Lucille Protas**

*President & Chief Operating Officer*

Lucille P. Protas is an Executive Managing Director and President and Chief Operating Officer of MacKay Shields, responsible for managing all aspects of the firm's infrastructure divisions, including finance/accounting, human resources, administration and back-office operations. She is actively involved in shaping the firm's direction through her participation on its Board of Managers and the Advisory Committee. Lucille joined the firm in 1973 as an Investment Research Assistant and later became a Senior Analyst in the accounting and financial division in 1977. She was named Treasurer in 1983, Chief Administrative Officer in 1992 and Chief Operating Officer in 2007.

She attended Fairleigh Dickinson University. She has been working in the investment industry since 1973.

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## Marketing & Client Service

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### **John W. Akkerman, CFA CAIA** *Executive Managing Director* *Global Head of Distribution*

John W. Akkerman is an Executive Managing Director and Global Head of Distribution, responsible for creating and implementing strategies for MacKay Shield's distribution, marketing, consultant relations and client service practices. He is a member of the firm's Advisory Committee. He joined MacKay Shields in September 2012 after 16 years in various leadership roles at AllianceBernstein, where he most recently led the firm's specialist institutional sales and marketing functions focused on alternatives and fixed income. From 2004 to 2010 he was responsible for the expansion and leadership of AllianceBernstein's institutional business in Canada, the United States and Latin America. This followed the launch and development of AllianceBernstein's Canadian business from 1996 to 2004. Prior to joining AllianceBernstein in 1996, John was a shareholder at TAL Investment Counsel, a business development executive at Sun Life and a corporate banking officer with Bank of Montreal.

He earned a BComm from Saint Mary's University and an MBA from the University of Western Ontario. A member of the Toronto Society of Financial Analysts, he is a CFA charterholder and a Chartered Alternative Investment Analyst. He has been working in the investment industry since 1987.

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### **Virginia E. Rose** *Senior Managing Director* *Head of Institutional Client Service*

Virginia is a Senior Managing Director and Head of Institutional Client Service. She is responsible for managing the firm's day-to-day relationships with clients, consultants and private fund investors, as well as all aspects of client reporting and data. She is a member of the firm's Advisory Committee. Prior to joining MacKay Shields in 1990, Virginia was a Marketing Assistant with Glickenhau & Co., Stamford Capital and a Research Analyst at New York Capital Resources specializing in Mergers & Acquisitions.

She attended Northeastern University. She has been working in the investment industry since 1985.

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### **Beth Griper** *Director* *Product Specialist*

Beth joined MacKay Shields in 2007 as a Director in the Institutional Client Service Division. Prior to joining MacKay Shields, she was a Director within the Global Corporate Client Group at NYSE Euronext where she was responsible for soliciting new listings and managing relationships with 120 listed companies. Beth also spent six years with Zurich Financial Services Group as a Business Development Analyst working with institutional and high net worth clients. Prior to that, Beth was with Credit Suisse First Boston and Shearman & Sterling. She received an MBA in Finance and Economics from New York University's Leonard N. Stern School of Business and a BA in International Relations and German from Bucknell University. Beth's career in the financial service industry began in 1996.