

CONVERTIBLE ISSUANCE SUITED TO GROWTH COMPANIES

Ask the PORTFOLIO MANAGER

What kinds of companies issue convertible securities?

Transcript of a video recorded on March 21, 2019

There are many different reasons that a company would issue a convertible.

Any time that a company is looking to finance a capital outlay, they're typically looking at either equity or debt. Convertibles can be a unique part of that capital structure because they are effectively allowing the company to issue equity at a premium, or they're able to issue debt at a lower interest rate than a traditional high yield market. One of the reasons that we've seen companies come to the market in the last couple of years on the convert side has been growth companies seeking growth capital. And in these types of scenarios, they tend to be smaller, more mid-cap companies that have identified a unique growth niche, but they are earlier in their profit cycles, so they are looking for ways to finance that.

For example, one of the areas that has been prevalent in the convert market for the past decade has been software as a service—technology companies. Those companies have a proven business model, but they are yet early in their profit cycle, so they are not generating enough cash to capitalize on all of their growth outlays. Those companies come to the convert market to gain capital, to expand their market share, to expand their product suite, and in that form, they are able to get the capital to grow their business. Those companies don't set up well for traditional high yield or bank loan markets because they don't have the hard assets that a traditional loan officer would want to backstop the loan.

But from a convert investor perspective, we have a call option on the underlying equity. Should those opportunities play out, we will be rewarded as long as the equity participates as well. In that case, those types of companies have been a great part of the convertible market—growth companies that are seeking growth capital.



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Convertible Securities Risk: The value of a convertible security is influenced by changes in interest rates, with investment value declining as interest rates increase and increasing as interest rates decline. The credit standing of the issuer and other factors also, may have an effect on the convertible security's investment value.

Convertible Arbitrage Risk: If the market price of the underlying common stock increases above the conversion price on a convertible security, the price of the convertible security will increase. The fund's increased liability on any outstanding short position would, in whole or in part, reduce this gain.

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