May 13, 2016

Zebra Commentary
By Alan Snyder

Pity the poor zebra that is neither black nor white; it lives in a perpetual world of in-between. The zebra evokes most political, economic, and societal commentaries. Often, they are replete with "on the one hand" yet "on the other hand," mind-numbing blather and self-protecting opinions.

Regardless of any antipathy we may feel toward Donald Trump, he has vanquished 16 accomplished adversaries and captured the public zeitgeist with his blunt comments. He is no zebra. No circumlocutions, no matter how inconsistent, are undertaken. We can learn from the "Donald" about being direct, even in the world of investing but hopefully be more thorough.

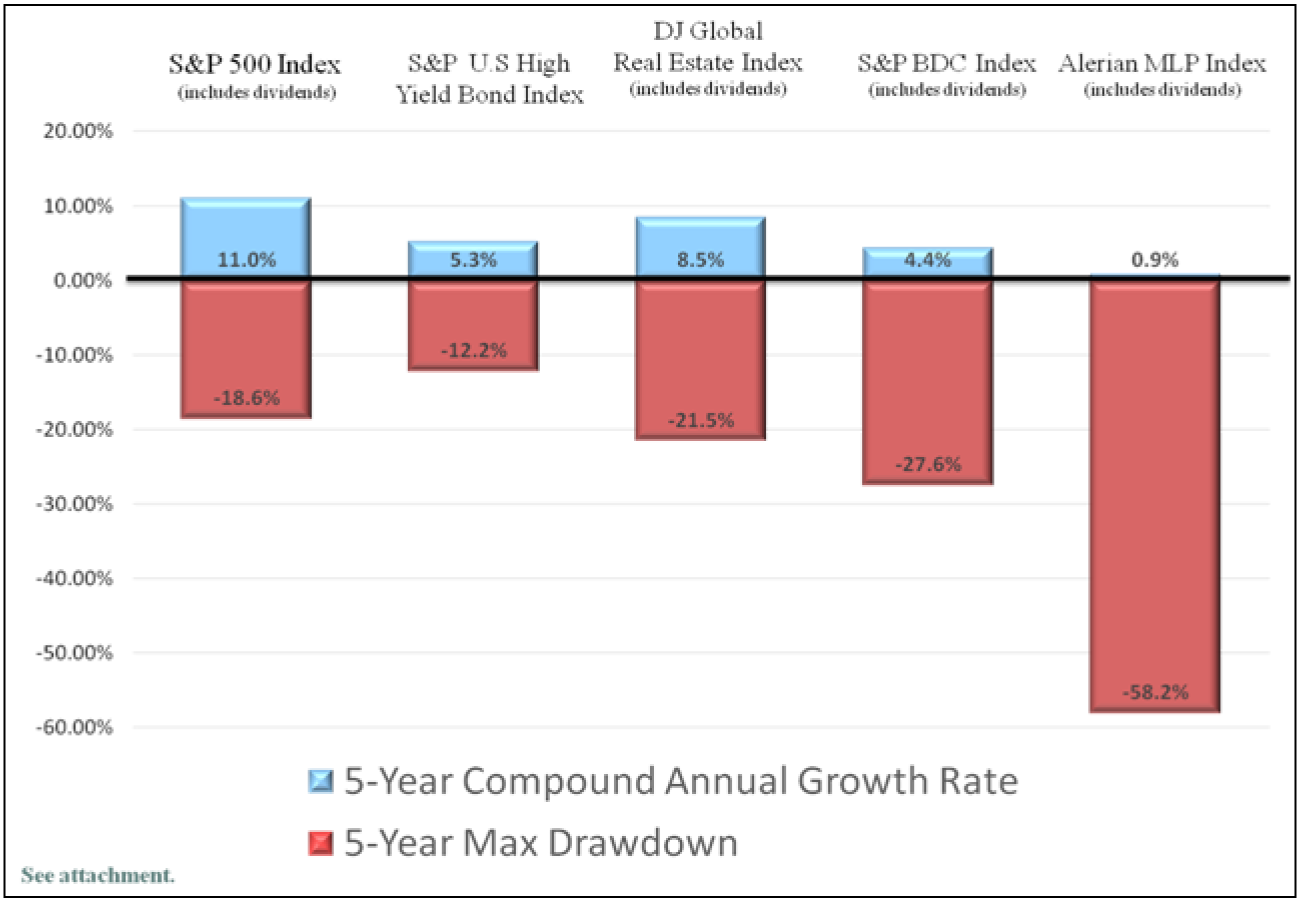
On this note, we aim to marshal some facts and predictions in order to evaluate the benefits or detriments of investing in the alternative lending space. You bet correctly that we have a thoroughbred horse in this race and an axe to grind. Yes, we have also bet our own "highly valued" investment funds on this horse. Versus that standard euphemistic investor bromide of "cautious optimism," we are "all in." Of course, we have not abandoned our core principle of believing in portfolio diversification; to poke fun at ourselves, maybe that's our hedge.

Many of our readers have become more active in responding to these missives. We totally welcome the input and repartee!

Where can we invest to achieve steady returns and compound our funds? Several months ago, we listed some possibilities and our prejudices about them against seven criteria. Each alternative may have a place in one's portfolio depending on how each criterion is weighted. Beauty is in the eye of the beholder but a newer entrant, alternative lending, merits careful consideration and we believe, participation.

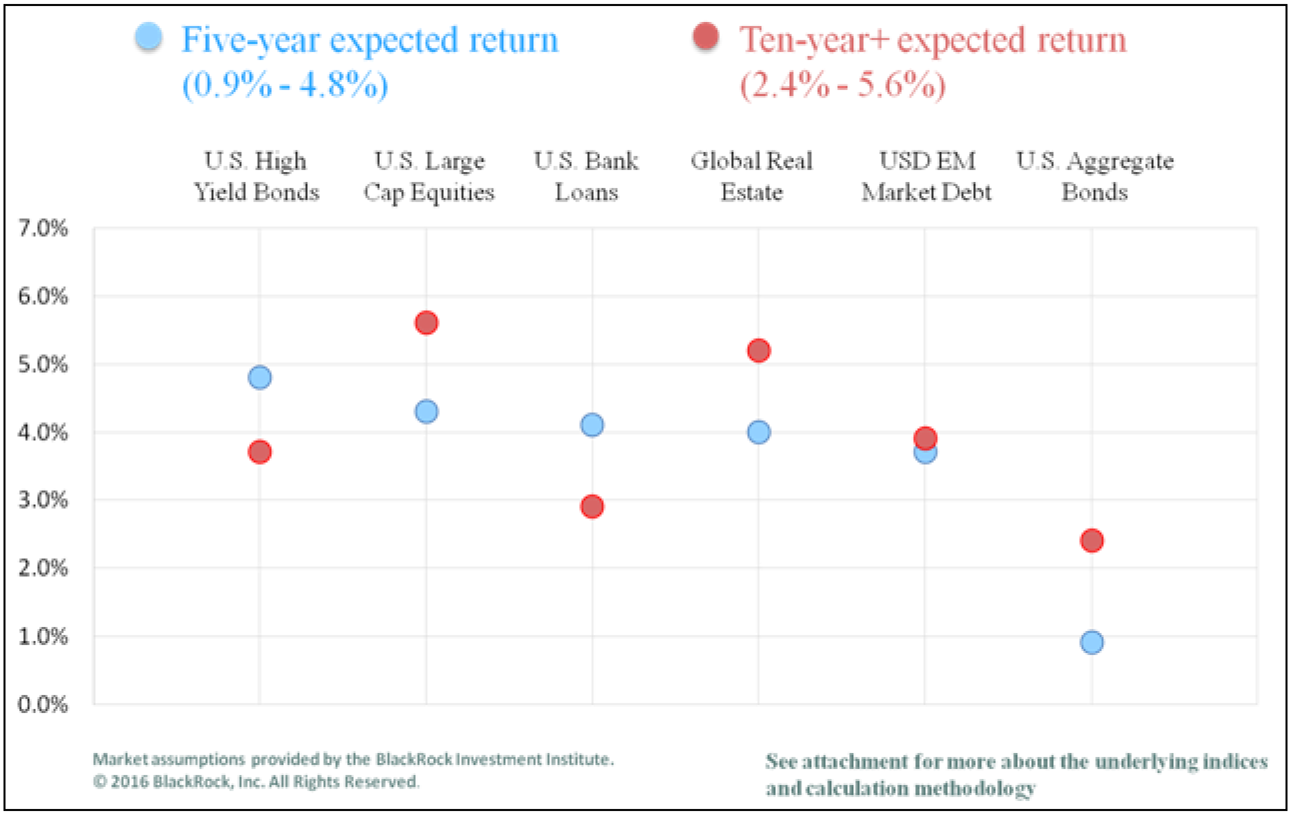
Investment Type	Yield	Rising Rate Protection	Downside Protection	Liquidity	Correlation to Market	Volatility	Transaction Costs
SIF	**High**	**Yes**	**Yes**	**Moderate**	**Low**	**Low**	**Low**
High-Yield Bonds	High	No	Moderate	Moderate	Moderate	Moderate	Moderate
Dividend Stocks	Low	No	Moderate	High	High	Moderate	Low
REITs	Moderate	Maybe	No	High	Moderate	High	Low
MLPs	High	No	No	High	Moderate	High	Low
Closed-end Bond Fund	High	No	No	High	Low	High	Low
BDCs	High	No	No	High	Moderate	High	Low
SBA Loans	High	No	Moderate	Low	Low	Moderate	Moderate
Yield Co's	Moderate	Maybe	No	Moderate	Low	High	Moderate
Income Property	Moderate	Maybe	No	Low	Low	Low	High

To aid in the discovery process, past performance is one data point. We have not listed the data for each of the above alternatives only to avoid excessive complexity:



Some might wonder how that long-term darling, equities, has fared over the past ten years – less good. The S&P 500 with dividends reinvested scored approximately 7% but with a 51% peak to valley decline and an annualized standard deviation of 15%.

"Piffle," snorts the forward looking skeptic, noting that past may not be prologue. Hence we sought out a future prognostication from the largest money manager in the world, BlackRock. Below we have graphically highlighted the table we previously shared, to facilitate review:



Their future is a rude awakening. In BlackRock's voluminous report, they add equally daunting volatility measures.

Against this backdrop, alternative lending looks pretty darn compelling. Adding some fuel to the fire, the IMF has lowered their projected growth rates four times in the past few months. U.S. GDP for the first quarter is estimated at an anemic 0.5% annualized rate. And, the TIPS spread to Treasuries, a forecast of future inflation, rests at approximately 1.65%. U.S. interest rates are close to negative on an inflation adjusted basis.

The Importance of Alternative Lending Diversification

"All in" does not mean all in one. With platform marketplace lenders experiencing challenges from slowing growth, a January shock from rising defaults, securitization markets demanding more, increased regulatory scrutiny and the alleged malfeasance of executives at Lending Club, is it time to abandon this category? "No" is the short answer. Teething pains for sure, but should not be unexpected given its growth. Overinflated stock prices have tumbled but it is clear to us that the need these newcomers fulfill is real; traditional banks move carefully yet have partnerships of varying degrees with the leading marketplace lenders including Lending Club.

This turmoil highlights the risks of a monochromatic investment strategy (e.g., single strategy/manager) in alternative lending at any particular moment in time. Towers Watson presciently noted the critical importance of a multi-strategy/multi-lender (i.e., "many sub-manager") approach. We heartily agree with them. In our "generic" alternative lending portfolio, modest allocations to consumer lending platforms are overshadowed by secured consumer lending, secured small business lending, secured trade finance, secured real estate lending and unlevered life settlements. In fact, the portfolio is 11% unsecured consumer platform lending and 89% secured other lending.

Given the openness of our notes, we can't be specific about our offerings herein but, if we have made a dent in your protective armor against new possibilities and are ready to dig deeper, check out the generic portfolio, shared before but recently updated, at http://www.shinnecock.com/articles/alternative_lending_presentation.pdf.

Best of all, let's talk and compare thoughts.

Please see below for details on the methodology.

Methodology for Historical Performance Comparison

The five-year compound annual growth rates (CAGRs) and five-year maximum drawdowns were calculated using daily pricing data from April 29, 2011 to April 29, 2016. The indices used were as follows: S&P 500 Total Return Index; S&P U.S. Issued High Yield Corporate Bond Index; Dow Jones Global Select Real Estate Securities Total Return Index; S&P Total Return BDC Index; Alerian Total Return MLP Index.

Index Definitions

The S&P U.S. Issued High Yield Corporate Bond Index tracks the performance of U.S. dollar-denominated, below-investment-grade corporate debt publicly issued in the U.S. domestic market by U.S. domiciled issuers. The index is rebalanced monthly and each bond must have a maturity greater than one month from the rebalancing date such that no bonds mature in the index. The minimum par value for a bond to be included in the index $100 million. The bonds in the index are subject to change after the close of every month, based on new issuance, size and maturity. Total return is calculated by aggregating the interest return, reflecting the return due to paid and accrued interest, and price return, reflecting the gains or losses due to changes in the end-of-day price and principal repayments. All cash, including interest payments and principal prepayments, is assumed to be kept in cash until the next rebalancing date.

The Dow Jones Global Select Real Estate Securities Total Return Index is designed to serve as a proxy for direct real estate investment and is comprised of equity real estate investment trusts (REITs) as well as real estate operating companies (REOCs) traded globally. In order to be included in the index a company must be both an equity owner and operator of commercial and/or residential real estate, and at least 75% of the company's total revenue must be derived from the ownership and operation of real estate assets.

The S&P BDC Index is designed to track leading business development companies that trade on major U.S. exchanges. Business development companies (BDC's) are publically traded private equity firms that invest equity and debt capital in small and mid-sized businesses, and make managerial assistance available to portfolio companies.

Alerian MLP Index is designed to track the performance of publically traded energy master limited partnerships (MLP's). Master limited partnerships are publically traded limited partnerships that derive at least 90% of cash flow from real estate, natural resources, and commodities. The constituents of the Alerian MLP Index represent approximately 85% of the total float-adjusted market capitalization of energy related MLP's.

BlackRock Future Projection Comparison Methodology

Return assumptions were published by the BlackRock Investment Institute in April 2016. These assumptions consider two time horizons: the five-year outlook and ten-year plus equilibrium capital markets assumptions. The five-year outlook incorporates valuation signals and macroeconomic scenarios, and is a reflection of how BlackRock analysts think current economic and market conditions will play out in the medium-term. The ten-year plus assumptions reflect 'equilibrium' or 'valuation-neutral' market conditions expected in the long-term, and are based on the capital asset pricing model, which holds that each asset class earns a return equal to the risk-free rate plus a risk premium. For each asset class represented, forward looking returns are based on the following indices : U.S. large cap equities are represented by the MSCI USA Index; global real estate is represented by a proprietary BlackRock proxy for real estate assets; U.S. high yield fixed income is represented by the Barclays U.S. High Yield Index; U.S. bank loans are represented by the S&P/LSTA Leveraged Loan 100 Index, USD emerging market (EM) debt is represented by the JP Morgan EMBI Global Diversified Index; U.S. aggregate bonds are represented by the Barclay's Capital Aggregate Bond Index. Five-year and ten-year plus equilibrium annualized return assumptions are in geometric terms. Return assumptions are total nominal returns.