many investments to choose from, sources to withdraw from and timing issues, we at Wellesley understand your concerns. For questions about your withdrawal strategy, as always please do not hesitate to contact your Wellesley advisor.

The Benefits of 144A Securities

In 1990, the Securities and Exchange Commission introduced Rule 144A as a means for accredited investors to trade securities that were not quoted on an exchange. Since then, adjustments have been made to reduce holding periods and increase liquidity for 144A securities. Today these securities provide many benefits to issuers and investors alike. At Wellesley Asset Management, we provide our investors the opportunity to invest in these securities, even if they aren’t accredited investors.

During the 1990s and early 2000s, many companies opted to register their proposed securities offerings with the SEC so that there were no restrictions on who could participate in an offering. For issuers this took time and also cost more money due to the amount of reports that needed to be filed with the SEC prior to an offering. In addition, there was often a roadshow for each new deal where the issuer would meet with potential investors in major U.S. cities. The reporting time combined with the roadshow took several weeks to complete. This led to uncertainty for the issuer and investors over where the security would be trading and what the market conditions would be when the deal was set to price.

The idea of 144A securities came about as a means of reducing both times to market and the amount of information that needed to be provided by an issuer. In order to purchase a 144A security, a buyer has to be a Qualified Institutional Buyer (QIB). A QIB cannot be an individual and must own and invest at least $100 million on a discretionary basis. The idea being that sophisticated investors do not need as much information or time to research new investment ideas. Rule 144A allowed issuers to bring deals to the market on a timelier basis thereby allowing them to take advantage of favorable prices and market conditions.

However, Rule 144A wasn’t created without its drawbacks. For one, the initial holding period was two years making the securities very illiquid. In 2008, the SEC relaxed this requirement to six months to a year, depending on the level of reporting a company did. In 2009, 144A securities became TRACE eligible, which meant every transaction had to be posted to a central reporting facility adding transparency to the price discovery process. Today there are no holding requirements on 144A securities and they are as liquid as registered securities.

In addition to providing benefits to issuers, 144A securities can be beneficial to investors. Most new convertible deals come to the market as 144A securities for one of three reasons. Many deals come to market quickly; sometimes on an overnight basis. In addition, new deals are sometimes paired with a stock buyback or the buyback of an existing convertible. Finally, derivatives transactions are sometimes added to convertibles to adjust the conversion price for the issuer of a bond. New deals are beneficial to investors because they are often priced “cheap” so that investors will buy them. According to Barclays, new deals on average were priced 1.35% cheap in 2020. Investors who can buy 144A securities may enjoy what we refer to as the “first day pop” because the securities immediately trade higher on day one.

Many Wellesley Asset Management clients cannot buy 144A securities in their separately managed accounts. Most 144A securities are issued with registration rights, which means after a seasoning period (usually one year) the bonds will become registered and anyone can buy them.

Unfortunately, in rising equity markets like we have experienced over the last 12 years, by the time the bonds become registered, they are too highly priced and are trading at a negative yield to worst, defined as the lowest possible yield that can be received on a bond without the issuer actually defaulting. Fortunately, at Wellesley Asset Management, we allow clients to own our mutual funds (which are QIBs) in their separately managed accounts. This gives them access to 144A names which helps diversify their portfolio and gives them access to new deals which may help improve performance.

Greg, Michael and the Wellesley Asset Management team look forward to another successful year and thank you for your continued trust in our services. We extend our sincerest best wishes to you and your family for good health and happiness as we start this New Year.

Important Disclosures:

Past performance is no guarantee of future results.

Investments in convertible securities are subject to the risks associated with both fixed-income securities and common stocks. All fixed-income securities are subject to two types or risk: credit risk and interest rate risk. Lower rated fixed-income securities are subject to greater risk of loss of income and principal than higher-rated securities. When the general level of interest rates goes up, the prices of most fixed-income securities go down. When the general level of interest rates goes down, the prices of most fixed-income securities go up. In general, stock and other equity security values fluctuate, and sometimes widely fluctuate, in response to activities specific to the company as well as general market, economic and political conditions.

No content in this newsletter should be construed as specific investment advice, or replacement for investment advice from Wellesley Asset Management, Inc. (Wellesley), or any other investment professional. This is not an offer to purchase securities. No representation is made that the investor will obtain similar results to those discussed. These articles are meant for broad discussion purposes only, and are not intended as a recommendation to buy or sell any security. Although information has been obtained from and is based on sources Wellesley believes to be reliable, Wellesley does not guarantee the accuracy of the information, and it may be incomplete or condensed.

Pertaining to Why Wellesley's Convertible Bond Strategy Now: Source
https://realinvestmentadvice.com/corporate-profits-are-worse-than-you-think/