



SMH CAPITAL ADVISORS, INC.

A Subsidiary of Sanders Morris Harris Group

In addition to financial analysis, SMH Capital Advisors shares its client's desire to generate solid investment returns and also reflect socially responsible values into its decision making process. We are discovering that many of our customers want their investments to reflect their closely held values. Socially responsible investing does not mean that SMH Capital Advisors will change their investment process and discipline that has remained consistent for over 17 years and 3 high yield 'bear' markets. In our socially responsible strategy, we select bond issues for your client's portfolio strictly based on our investment process, as not every company with strong social values passes our investment analysis.

Our Socially Responsible portfolios are managed in the same way as our High Income portfolios except that we will adhere to a socially responsible investment policy that prohibits owning any companies in the investment portfolio that derive more than 50% of their annual revenue from the following industries:

- Alcohol
- Tobacco
- Weapons Manufacturing
- Gambling
- Pornography

SMHCA High Income Investment Process

Our process consists of three disciplines. The process is a bottom-up value type investment style with a primary focus on the balance sheet of the businesses. We refer to this first discipline as the **Credit Risk Reduction**. Once a security has passed the first discipline, we move to discipline two where we look for **Adequate Return for the Risk**. The goal is to purchase securities that offer adequate yield over a treasury and the best relative value while avoiding overpriced securities and markets. The third discipline has been put in place to help us avoid "being the market". Statistically, most of the diversification of a portfolio has been shown to come from less than the first 20 holdings. By keeping a focused portfolio of generally 35 issuers or less, we believe we can choose our "best picks" and **Reduce the Systematic (or Market) Risk**, while adding alpha.

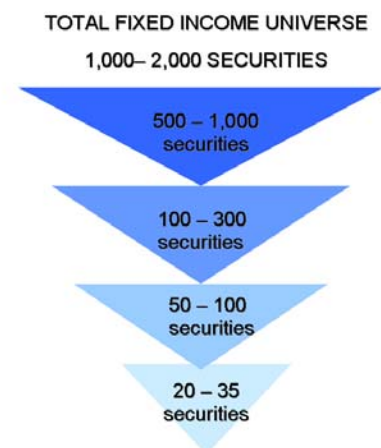
The portfolio, resulting from these three disciplines, consists of generally 20 to 35 positions landing the portfolio in an average BB to B credit range (considered non investment grade and highly speculative by Moody's and S&P) and an average duration between 3 and 6 years. Generally, a single position will not account for more than 5% of an entire portfolio at cost. Solid credit research with a focused portfolio of our 'best picks' has produced a default rate* significantly below the index and higher net returns.

How our Process Breaks Down the Fixed Income Universe

We start our process with the General Fixed Income Universe...

- Discipline 1 Balance Sheet Analysis (Credit Risk Reduction)
Universe is reduced to 500-1000 securities
- Discipline 2 Adequate Return for the Risk
Universe is reduced to 100-300 securities
- Discipline 3 Reduction of Systematic (or Market) Risk
Universe is reduced to 50-100 securities

Our Resulting portfolio (20-35 securities)



*Annual default rate is 0.35% with a net annual loss rate due to defaults of 0.19% (both are since inception of 1/1995). The annual default rate was derived by taking the total number of issuers purchased in client portfolios divided by the total number of issuers that defaulted while bonds were still in the portfolios. The net annual loss rate was calculated by taking the average recovery rate on the default bonds still held in the portfolio as a % of par (45%) and multiplied it by the annual default rate.

Past performance is not indicative of future results. SMH Capital Advisors, Inc., a Registered Investment Adviser, is a wholly owned subsidiary of Sanders Morris Harris Group. Request Form ADV Part II for a complete description of SMH Capital Advisors, Inc.'s management services. Market and economic factors can change rapidly producing materially different returns. No inference should be drawn that managed accounts will be profitable in the future or that the Investment Team will be able to achieve its objectives. Investing involves risk, you may experience a profit or a loss. Please be aware of the specific risks associated with investing high yield bonds, such as the issuer may not be able to meet its principal and interest obligations. As such, your investments may lose value or you may lose the principal investment. High Yield Bond- These funds primarily invest in U.S. high-income fixed-income securities where at least 65% or more of bond assets are not rated or are rated by a major agency such as Standard & Poor's or Moody's at the level of BB (considered speculative for taxable bonds) and below.