DoubleLine FUNDS

DoubleLine News

DoubleLine Floating Rate Fund (DBFRX/DLFRX)

By Robert Cohen, CFA & Matthew Baca

As of June 8, 2016

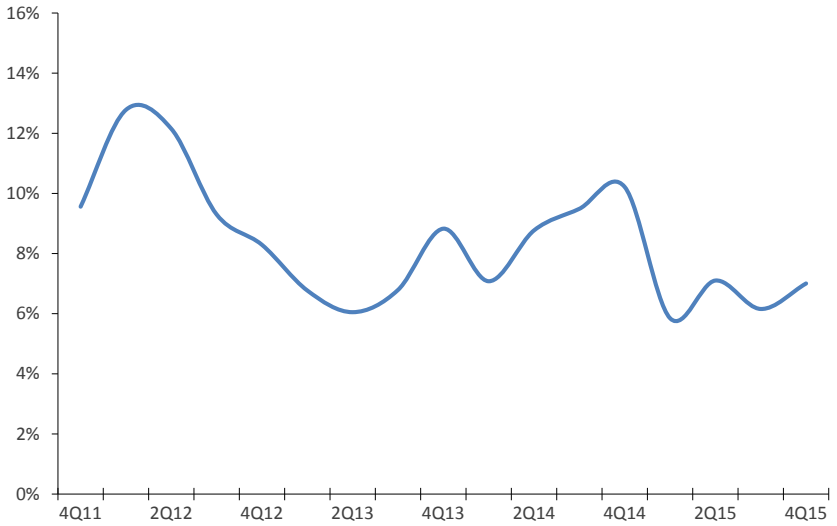
Leveraged loans have been one of the hottest asset classes in recent years as investors seek yield and try to manage exposure to expected rising rates. These investors made large contributions to loan funds following the financial recession. In fact, between 2009 and 2014, total loan fund assets under management (AUM) increased nearly five-fold from $33 billion to a record $158 billion. As investor appetite for the asset class grew, many larger loan funds were the first to receive inflows. As these funds grew, so did their participation in the new issue market with many funds being forced to buy nearly all new issues to get inflows invested. Collateralized loan obligation (CLO) activity also expanded rapidly during this time period, from less than $1 billion in 2009 to a record $124 billion by 2014. The combined interest from loan funds and CLOs drove flows into the asset class as part of an overall search for yield and duration management in financial markets.

It was at this time that DoubleLine saw the opportunity to offer investors an actively-managed bank loan fund. This is achieved through a detailed bottom-up selection process and a selective mandate that allows the team to find individual opportunities outside many of the larger beta names. While this strategy may underperform during periods of extreme optimism, we believe it will outperform over full credit cycles, particularly when conditions deteriorate.

Since the peak in bank loan AUM during 2014, demand has cooled off as we continue to see a combination of retail outflows and a contraction in CLO formation - the two largest demand components for leveraged loans. Fortunately, the weaker demand has been somewhat offset by the lighter new issue calendar as only $41.0 billion in new institutional loans were priced during the first quarter of 2016. The lighter new issue calendar is welcomed from a technical standpoint, as it helps to move the market to a stable equilibrium point.

From a fundamental standpoint, the loan market has also experienced support from positive earnings growth. According to the most recent data from Leveraged Commentary & Data (LCD), earnings before interest, taxation, depreciation and amortization (EBITDA) across the S&P/LSTA Leverage Loan Index increased 7% year-over-year (YoY) through the fourth quarter. We believe this trend bodes well for the loan market, especially when compared against the declining corporate profits in the equity market and negative YoY EBITDA growth across U.S. high yield corporate bonds.

Figure 1: Quarterly EBITDA Growth*
December 31, 2011 through December 31, 2015



Source: Bloomberg

* There is a one-quarter lag in EBITDA Growth Data.

During 2016 thus far, it has been the lower quality CCC and B rated loans that have led to the rebound in credit. Our view at DoubleLine is that now is not the time to be chasing after lower quality loans as defaults are likely to head higher. According to the most recent figure, the S&P/LSTA Leveraged Loan Index

default rate increased to 1.75% during the twelve months ending March 31st.

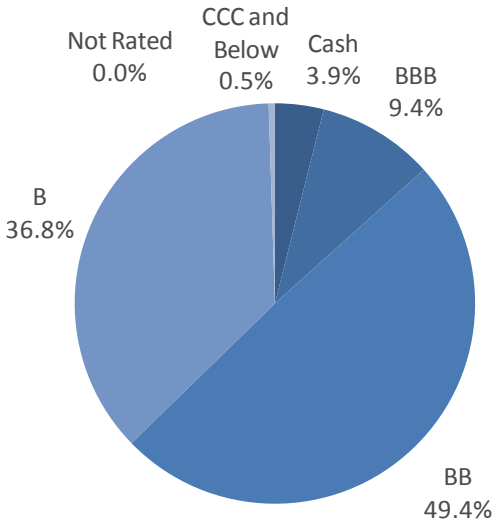
As such, we have been opportunistically selling risk during the most recent countercyclical rally as technicals have superseded fundamentals over the short term. The DoubleLine Floating Rate Fund maintains an underweight position in Energy and all Commodity-related sectors, in favor of more defensive sectors such as Healthcare. Until both technicals and fundamentals improve, the portfolio will remain defensively positioned and ready to change should an opportunity arise.

Figure 2: DoubleLine Floating Rate Fund Top 10 Sectors As of May 31, 2016

Sectors	% Weight
Healthcare	9.32%
Business Equipment & Services	7.76%
Lodging & Casinos	7.32%
Electronics/Electrical	6.50%
Food Products	6.00%
Chemicals & Plastics	5.76%
Leisure Goods/Activities/Movies	5.46%
Retailers (Except Food & Drug)	5.35%
Containers & Glass Products	4.25%
Building & Development	4.16%
Grand Total	**61.89%**

Source: DoubleLine Capital LP

Figure 3: Current Credit Quality Breakdown* As of May 31, 2016



Source: DoubleLine Capital LP

*As of May 31, 2016, the DoubleLine Floating Rate Fund held 0.00% in unrated securities.

Definitions

Beta is the measure of a mutual funds' volatility in relation to the market. By definitions, the market has a beta of 1.0, and individual mutual funds are raked according to how much they deviate from the market. A beta of above 1.0 means the fund swings more than the market. If the fund moves less than the market, the beta is less than 1.0.
Duration is a measure of sensitivity of the price of a fixed-income investment to a change in interest rates.
S&P/LSTA Leveraged Loan Index is a weekly total return index that tracks the current outstanding balance and spread over LIBOR for fully funded term loans.
One cannot invest directly in an index.

Disclosures

The fund's investment objectives, risks, charges and expenses must be considered carefully before investing. The summary and statutory prospectus contains this and other important information about the investment company, and it may be obtained by calling 1(877)354-6311/1(877)DLINE11, or visiting www.doublelinefunds.com. Read it carefully before investing.

Mutual fund investing involves risk; principal loss is possible. Investments in debt securities typically decrease in value when interest rates rise. This risk is usually greater for longer-term debt securities. Investments in floating rate securities include additional risks that investors should be aware of such as credit risk, interest rate risk, possible illiquidity and default, as well as increased susceptibility to adverse economic developments. Investments in lower-rated and non-rated securities present a greater risk of loss to principal and interest than higher-rated securities. Investments in Asset-Backed and Mortgage-Backed Securities include additional risks that investors should be aware of including credit risk, prepayment risk, possible illiquidity and default, as well as increased susceptibility to adverse economic developments. Investments in foreign securities may involve political, economic, and currency risks, greater volatility and differences in accounting methods. These risks are greater for investments in emerging markets. In order to achieve its investment objectives, the Fund may use certain types of exchange traded funds or investment derivatives. Derivatives involve risks different from, and in certain cases, greater than the risks presented by more traditional investments. Derivatives may involve certain costs and risks such as liquidity, interest rate, market, credit, management and the risk that a position could not be closed when more advantageous. Investing in derivatives could lose more than the amount invested. ETF investments involve additional risks such as the market price trading at a discount to its net asset value, an active secondary trading market may not develop or be maintained or trading may be halted by the exchange in which they trade, which may impact the fund's ability to sell its shares. The Fund may use leverage which may cause the effect of an increase or decrease in the value of the portfolio securities to be magnified and the Fund to be more volatile than if leverage was not used.

Diversification does not assure a profit or protect against loss in a declining market.

Fund holdings and sector allocations are subject to change and are not recommendations to buy or sell any security.

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Disclaimers

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Important Information Regarding DoubleLine

To receive a complimentary copy of DoubleLine Capital's current Form ADV (which contains important additional disclosure information, including risk disclosures), a copy of the DoubleLine's proxy voting policies and procedures, or to obtain additional information on DoubleLine's proxy voting decisions, please contact DoubleLine's Client Services.

Important Information Regarding DoubleLine's Investment Style

DoubleLine seeks to maximize investment results consistent with our interpretation of client guidelines and investment mandate. While DoubleLine seeks to maximize returns for our clients consistent with guidelines, DoubleLine cannot guarantee that DoubleLine will outperform a client's specified benchmark or the market or that DoubleLine's risk management techniques will successfully mitigate losses. Additionally, the nature of portfolio diversification implies that certain holdings and sectors in a client's portfolio may be rising in price while others are falling; or, that some issues and sectors are outperforming while others are underperforming. Such out or underperformance can be the result of many factors, such as but not limited to duration/interest rate exposure, yield curve exposure, bond sector exposure, or news or rumors specific to a single name.
DoubleLine is an active manager and will adjust the composition of client's portfolios consistent with our investment team's judgment concerning market conditions and any particular sector or security. The construction of DoubleLine portfolios may differ substantially from the construction of any of a variety of market indices. As such, a DoubleLine portfolio has the potential to underperform or outperform a bond market index. Since markets can remain inefficiently priced for long periods, DoubleLine's performance is properly assessed over a full multi-year market cycle.

Important Information Regarding Client Responsibilities

Clients are requested to carefully review all portfolio holdings and strategies, including by comparing the custodial statement to any statements received from DoubleLine. Clients should promptly inform DoubleLine of any potential or perceived policy or guideline inconsistencies. In particular, DoubleLine understands that guideline enabling language is subject to interpretation and DoubleLine strongly encourages clients to express any contrasting interpretation as soon as practical. Clients are also requested to notify DoubleLine of any updates to Client's organization, such as (but not limited to) adding affiliates (including broker dealer affiliates), issuing additional securities, name changes, mergers or other alterations to Client's legal structure.

DoubleLine Group is not a registered investment adviser with the Securities Exchange Commission (SEC).