

# OAKTREE INSIGHTS

APRIL 2020

SPECIAL EDITION: COMMEMORATING 25  
YEARS OF MASTERING THE MARKET CYCLE



# OAKTREE

CELEBRATING 25 YEARS

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- Starting in the late 1970s, the seeds for Oaktree are sown, as the **soon-to-be founding team and core expertise start to come together**.
- 1978: **Howard Marks**, working for Citibank, meets Michael Milken, a pioneer in issuing and trading **high yield bonds**. Their meeting sets the stage for Howard and his team to build their **high yield bond business**. Shortly thereafter, Howard moves from New York to Los Angeles.



- 1983: **Sheldon Stone** joins Howard at Citi, leaving Prudential Insurance where he was a director of corporate finance and manager of fixed income portfolios. At Citi, Sheldon focuses on credit analysis and manages high yield bonds.
- 1985: Meanwhile, **Bruce Karsh** first comes across **distressed debt** while working for Eli Broad, the chairman of SunAmerica. The same year, Sheldon and Howard move from Citi to TCW and establish the firm's high yield bond department.
- 1986: **Larry Keele** joins Howard and Sheldon to oversee **convertibles** portfolios, bringing his experience as manager of convertible securities and high-yielding equities for NationsBank.
- 1987: Bruce joins Howard, Sheldon and Larry to establish and manage the Special Credits funds for distressed debt investing.
- 1988: **Richard Masson** joins the team – leaving Houlihan, Lokey, Howard and Zukin, where he oversaw the valuation and analysis of securities and businesses – to head the Special Credits Analytical Group.

## 1970s

- Mid-to-late 1970s: **Inflation** accelerates; by the end of the decade, curbing inflation becomes Washington's **primary economic priority**.
- 1979: Paul Volcker starts his tenure as U.S. Fed chairman. Committed to a **disinflationary monetary policy**, he concentrates on restraining the growth of the money supply. The **Iranian Revolution** of 1979 sparks a round of oil price increases (the second major spike in the decade, following the 1973 oil embargo).

## 1980s

- Early 1980s: The U.S. economy slows due to **stagflation** and, along with much of the developed world, experiences a **recession**. The U.S. starts a recovery by 1983 that would lead one of the longest periods of **sustained growth** since WWII.
- Early-to-mid 1980s: In an era of **financial deregulation**, the savings and loan industry embarks on increasingly speculative activities, many involving real estate and high yield bonds. Factors such as overall economic growth, declining interest rates, liberalization of debt issuance and good performance pave the way for **alternative investing to grow** in earnest.
- 1987: In a global stock market crash, U.S. equities suffer the **greatest one-day percentage drop in history**. The severity of the crash is attributed to computerized trading and over-reliance on portfolio insurance, among other factors.
- 1988 marks the peak in **S&L failures**, part of a slow-moving crisis that would see more than 1,000 institutions fail.

- 1990: Howard writes his **first investment memo**, *The Route to Performance*, stating that “if you can avoid the losers (and losing years), the winners will take care of themselves.” This remains the guiding spirit of Oaktree’s investment approach today.
- 1990s: The team at TCW **invests throughout the early-1990s recession** even as some competitors leave the market amid the economic weakness.
- 1995: **Oaktree Capital Management LLC** opens for business in Los Angeles with five founders, two employees and one consultant. Oaktree starts with seven strategies, including **high yield bonds, convertibles, distressed debt, distressed mortgages and distress for control**.
- 1996: Oaktree hosts its **first client conference**.
- 1998: Total **AUM passes \$10 billion and headcount reaches 100**. Oaktree headquarters moves from a sublet office on Hope Street to three floors of permanent space at 333 South Grand Avenue. The same year, Oaktree sets up its first overseas office in **Singapore**, followed shortly by an opening in **Tokyo**. Oaktree begins to expand its product line, adding strategies involving **emerging markets equities and European high yield bonds**.
- 1999: Oaktree continues to extend its global reach, opening its **London** office.
- 2000: In his first memo of the new century, Howard expresses caution regarding **the dot-com bubble**: “To say [tech stocks] have benefited from a boom of colossal proportions and should be examined very skeptically is something I feel I owe you.”
- Starting in late 2004, Oaktree begins to invest in smaller amounts and more cautiously, as its portfolio managers detect “**too much trust and too little worry**” in the markets.
- 2007: Oaktree begins to **gear up for an expanded opportunity for distressed debt investing**.
- Late 2008: In the last 15 weeks of 2008, in the face of widespread fear of a systemic collapse of financial markets, **Oaktree invests ~\$600 million per week** following the bankruptcy of Lehman Brothers.
- 2009: Oaktree provides seed capital for **DoubleLine**, helping support the firm in its start-up period.

## 1990s

- 1990: As **many prominent LBOs of the 1980s default**, the **high yield bond market collapses**. The year marks the start of the end of the Cold War. Reductions in defense spending help close budgetary shortfalls and contribute to the surpluses of the late 1990s.
- A **recession** takes hold from July 1990 to March 1991, after which the U.S. economy and markets enter a “**golden age**.”
- The mid-1990s see the high yield bond market develop on a **path to maturity**.
- Mid-decade marks the liftoff of the digital age. Growth in employment and productivity accelerates in the second half of the decade. This expansionary period lasts until 2001 and becomes the **longest stretch of economic growth** on record when it reaches 10 years.
- 1997: The Taxpayer Relief Act lowers the top marginal capital gains tax rate. Investors become **increasingly eager to make speculative bets**, including in tech and media companies. The same year, the **Asian financial crisis** begins with a currency devaluation in Thailand. Declines spread rapidly throughout East Asian economies. Market drops are also felt in the U.S., Europe and Russia.
- Financial markets continue to be challenged. In particular, they’re rattled once again in 1998 when prominent hedge fund **Long-Term Capital Management melts down**.

## 2000s

- 2000: Fed Chairman Alan Greenspan warns that interest rate hikes are necessary to head off inflationary pressures hovering over the booming economy. **Markets rise past warnings**. Eventually the **tech bubble bursts**, marking the end of the economic expansion and kicking off the first three-year decline of equities since the Great Depression.
- 2001: A brief recession takes hold from March to November. The Al Qaeda terrorist attacks on **September 11** kill thousands in the U.S. and lead to the global War on Terrorism.
- The collapse of tech stocks and the broad market sends investors away from equities and toward alternative investments. Over the mid-2000s, a boom in home prices leads to the creation of **subprime mortgages**. These are packaged into mortgage-backed securities that are invested in by financial institutions. Eventually subprime mortgages and MBS default in large numbers, causing a wave of financial institution collapses.
- 2007: December marks the start of a **recession**.
- 2008: Lehman Brothers files for bankruptcy in September, the stock market crashes, and confidence erodes rapidly as the **Global Financial Crisis** takes hold.
- 2009: The economy bottoms out mid-year and a **recovery begins**, thanks in part to **unprecedented monetary accommodation** by the Fed and swift policy actions that help avoid worsening conditions.

- 2010: Oaktree recognizes the **early resumption of pro-risk behavior in the markets**, even as significant uncertainties remain.
- 2011: Thus Oaktree sets its mantra of “**move forward, but with caution.**”
- 2012: Oaktree debuts on the NYSE.
- 2013: Barron’s names Howard “**Wall Street’s Favorite Guru**” on its cover. Bruce becomes Oaktree’s first **Chief Investment Officer**.
- 2014: Jay Wintrob is hired as Oaktree’s first **Chief Executive Officer**.
- 2015: Oaktree launches **Our Communities Matter**, its philanthropic and community-service initiative.
- 2017: Jay signs the **CEO Action for Diversity & Inclusion**, a statement of commitment to advancing diversity and inclusion in the workplace.
- 2019: Oaktree and **Brookfield** enter into a partnership that gives Brookfield a 61% interest in Oaktree. Oaktree becomes a signatory to the **UN-supported Principles for Responsible Investment** in an affirmation of its commitment to ESG considerations in investing.
- 2020: In response to the coronavirus outbreak and related measures, Oaktree implements business continuity plans and transitions into a temporarily virtual organization. Oaktree **identifies opportunities amid market dislocations** and plans for what it believes will be an expanded distressed credit cycle. Oaktree reaches its **25-year anniversary** in April.



## 2010s

- The decade ushers in **new financial regulations in the aftermath of the financial crisis**.
- The U.S. witnesses a **bull market** throughout the decade, with near-zero yields helping boost investors’ appetite for risk assets. This **economic expansion becomes the longest on record**. Global growth is supported by accommodative central bank actions and quantitative-easing programs that keep interest rates low. “**Synchronized global growth**” is a widely used phrase . . . for a while.
- Late 2010s: Growth slows in major global markets, causing the U.S. to stand out.

## 2020

- The start of 2020 sees U.S. stocks continuing to hit records, but it isn’t without **macro and geopolitical issues**, including trade conflicts, European fragmentation and the start of the **coronavirus outbreak in Asia**. The virus quickly becomes a pandemic and the world’s “biggest story,” affecting millions of lives and leading to nationwide lockdowns and a halt in commercial activities. In March, **global equities plummet** and U.S. stocks make their quickest transition from a bull market to a bear market, driven by uncertainty surrounding the health crisis and the crash in oil prices that amplified fears of escalating damage to the economy. World economies face a **recession** as governments grapple with providing economic stimulus.

## Q&A WITH OAKTREE'S FOUNDERS



**HOWARD MARKS**

*Co-Chairman*



**BRUCE KARSH**

*Co-Chairman and  
Chief Investment Officer*



**SHELDON STONE**

*Principal and  
Portfolio Manager*



**RICHARD MASSON**

*Outside Director*



**LARRY KEELE**

*Advisory Partner*

### WHAT ARE SOME OF THE MOST MEANINGFUL ASPECTS OF OAKTREE'S WORK?

**HM:** We stand strongly for incorporating risk control in our portfolios, even in good times. As a result, that risk control is in place when the bad times roll around. And we have historically done a good job of switching from risk control to risk-bearing when the potential rewards have been greatest.

**BK:** We founded our firm with a well-defined investment philosophy and set of business principles. The adherence to and implementation of both have served our clients well and helped lead to our success as an investment firm. They've also contributed to a working environment that is enjoyable, respectful and community-minded. I think that's quite special.

**SS:** An important part of our work is the fact that we're all investors. Starting from Day One, none of us has been involved in anything other than managing investments as fiduciaries for others. Our greatest priority remains managing money within the construct of

our investment philosophy. And we continue to carry on with the things that helped in the past: our skills, our knowledge of markets, and our focus on controlling risk.

**RM:** We participate in markets that require a high degree of specialization and skill, and we should be proud of our consistent pursuit of strong results. We have focused, and will continue to concentrate, on producing investment returns not for our own sake, but for the benefit of our clients and, ultimately, the people who depend on them for their retirement, education and charitable work.

**LK:** I believe it's important that we think about our work not in terms of investing for a few thousand clients, but in terms of our investments impacting millions of individuals throughout the world. We need to maintain our standards and investment discipline, and continue to manage the firm according to the principles set out 25 years ago.

### WHAT IS YOUR FAVORITE OAKTREE MEMORY?

**HM:** Some of my favorite Oaktree moments have been those (a) when clients told us they understand that our returns may lag benchmarks in bull markets as a result of our emphasis on risk control, and (b) when we have successfully turned to risk-bearing during crises. Each of these has happened often. They are the result of the cohesiveness of our organization and are behind Oaktree's success.

**BK:** I'd point to the last 15 weeks of 2008, when Oaktree invested boldly in challenging times. Although the world felt like it was falling apart and everyone was scared to stick their head out of their shells, we invested an average of more than \$600 million a week during that period, exactly when it mattered most.

**SS:** I have to say the most gratifying events for me were right at the formation of Oaktree. Starting up was like diving into a pool while it was being filled; you didn't know how deep it was. Fortunately it was awfully deep. We all saw risk, but we trusted each other. If you trust your partners, you don't second-guess. I'll also mention that the people of Oaktree have been one of the best parts of working here the past 25 years. My teammates gave me a "Sheldon Stone" bobble-head doll on my 30th anniversary as a portfolio manager. It reminds me that the community and relationships we

get to develop in our workplace are some of the most meaningful memories, and they stay with me. And if we at the leadership level do our job well, the next Oaktree generation will have their own stories like these to tell.

**RM:** One of my favorite Oaktree memories tracks back to the founding of the firm – namely the fact that nearly all of our colleagues at TCW decided to join our new venture. To have our faith in the new company confirmed by the people with whom we had worked so closely was one of the most satisfying moments of my career.

**LK:** Day One (or shortly thereafter) was a favorite for me, too, when basically the entire team came over from TCW to start Oaktree. Another personal favorite is having had the opportunity to engage with clients about our strategies. Earning clients' trust and having a wonderful relationship with them have been some of the most important and memorable aspects of being part of Oaktree.

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