

Investment Manager: **Fixed Income Investors**

## MainStay Floating Rate Fund

### Fund Review

For the quarter, the Fund's performance outpaced its benchmark, the Credit Suisse Leveraged Loan Index. This outperformance was due to the portfolio's underweight to credits rated CCC and lower, as higher rated credits posted stronger relative returns.

We remain focused on generating attractive risk-adjusted returns through a variety of credit cycles. Emphasis is placed on higher quality floating rate loans, both from a credit rating and structure perspective. Issues are added to the portfolio based on a fundamental, credit-specific investment approach.


Industry concentration is generally less than 12% and position sizes average 1% or lower, allowing for broad diversification. The largest industries in the Fund based on market value were health care at 11.3%, diversified media at 8.4%, chemicals at 7.7%, and automotive, cable/wireless video, and forest products at 5.7%. Of the Portfolio's largest industry concentrations, it is significantly over-weighted against its benchmark with respect to chemicals and forest products. The Fund is modestly over-weighted in automotive and cable/wireless video, and it is approximately market-weighted in health care and diversified media.

### Market Review/Outlook

The leveraged loan market lost 1.04%<sup>1</sup> in the second quarter of 2010, snapping a streak of five consecutive quarterly gains as measured by the Credit Suisse Leveraged Loan Index (Index). The Index remains in positive territory for the year, with a return of 3.26%.<sup>1</sup> All ratings classes performed comparably during the quarter, with each category from BB down to distressed credits losing approximately 1%-2%.<sup>1</sup> This differs from the trend of the last few quarters, where lower-rated, distressed, and defaulted credits tended to outperform. The Index continued to be priced well below par, with an average price of 89.41 as of June 30th.<sup>1</sup>

The second quarter of 2010 was defined by a revived primary market, as issuers took advantage of favorable conditions brought on by the market's 15-month advance. Issuers brought \$44 billion of new institutional loans to market during the quarter, as compared to \$31 billion in the first quarter and \$6 billion from the year-ago quarter.<sup>2</sup> This level of volume surpassed loan demand, and the market's decline gained momentum from a heightened sense of risk aversion caused by the Greek economic crisis. Additionally, a slowdown in bond-for-loan takeout activity meant less cash was made available for investment, which reduced demand. Due to these combined pressures, loans issued during the quarter (particularly those in June) came to market with higher spreads, increased LIBOR floors, and larger purchase discounts. The market was given some support, however, by solid increases in GDP over the last few quarters, better liquidity in the capital markets, and a continued reduction in defaults. The trailing 12-month institutional leveraged loan default rate was 4.65% at the end of June 2010.<sup>3</sup> One additional point of interest is that no issuers defaulted in the month of June, which marks the first time in two and half years this has occurred.<sup>3</sup>

The second quarter also witnessed a \$37 billion reduction of loans due to mature in the near to medium term. This so-called "maturity wall," which represents approximately \$350 billion of leveraged loans due through 2014<sup>4</sup>, will continue to experience extensions and repayments as long as capital markets remain liquid. One thing to note, however, is that many of the stronger borrowers have already refinanced into longer-dated paper, which means the remaining "wall" is comprised of relatively weaker credits.



Given the uncertainty in the financial system, particularly with regard to the strength of the global economic recovery, volatility could continue in the leveraged loan market as we move through 2010. Therefore, borrowers may be content to delay issuing new loans until a sense of optimism returns. Sources of demand may remain limited as well, as Collateralized Loan Obligations (CLOs)<sup>5</sup> are holding historically small amounts of cash and a new-issue securitized market has yet to emerge. While uncertainty on both the supply and demand fronts could result in short-term volatility, we will continue to manage our portfolios with a long-term view, while attempting to minimize losses by focusing on credits with strong fundamentals and a proven track record.

*The opinions expressed are those of Fixed Income Investors Group<sup>6</sup> (Fixed Income Investors) as of the date of this report and are subject to change. This is no guarantee that any forecast made will come to pass. This material does not constitute investment advice and is not intended as an endorsement of any specific investment.*

The Credit Suisse Leveraged Loan Index is an unmanaged index that represents tradable, senior-secured, U.S.-dollar-denominated non-investment-grade loans. An investment cannot be made directly into an index.

1. Source: Credit Suisse, "Leveraged Finance Strategy Update", July 2010.
2. Source: Standard & Poor's LCD, Quarterly Review 2Q10.
3. Source: Credit Suisse, "Leveraged Finance Strategy Update", July 2010.
4. Source: Standard & Poor's LCD, Quarterly Review 2Q10.
5. CLOs are securities backed by a pool of leveraged loans structured so that there are several classes of bondholders with varying maturities, called tranches, that have different risk/reward characteristics.
6. Fixed Income Investors Group is a division of New York Life Investment Management LLC.

Floating rate funds are generally considered to have speculative characteristics that involve default risk of principal and interest, collateral impairment, borrower industry concentration, and limited liquidity. The Fund may invest in foreign securities. U.S. dollar-denominated securities of foreign issuers can be subject to different risks than U.S. investments, including less liquid trading markets, greater price volatility, political and economic instability, less publicly available information, and changes in U.S. or foreign tax or currency laws and monetary policy. Funds that invest in bonds are subject to interest-rate risk and can lose principal value when interest rates rise.



For more information about MainStay Funds, call 800-MAINSTAY (624-6782) for a prospectus. Investors are asked to consider the investment objectives, risks, and charges and expenses of the investment carefully before investing. The prospectus contains this and other information about the investment company. Please read the prospectus carefully before investing.

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