

# Webinar Summary

---

## Introduction

The average closed-end fund through Friday is down 40%. Discounts widened; NAVs and market prices both fell. NAV movements reflect a lack of trading in the market, a shortage of bids. Most funds are levered (including 90% of bond funds), and leverage magnifies results on the way up and down. For those who remember the Financial Crisis, discounts were wider than they ever got on a single day in October 2008. If you're in closed-end funds, your brokerage statements look scary, reflecting a sentiment of fear in the market. Volatility is something we talk about with every client, but I can guarantee you that every client we've brought on in my entire 18-year career has not seen the current level of discounts that we have.

Remember that closed-end funds are not one position; they're diversified and actively managed. Closed-end funds have a fixed capitalization, and apart from breaking 40 Act leverage terms, they are essentially never a forced seller of assets (unlike ETFs and open-end mutual funds, which must sell to meet redemptions), which is very useful in periods like this. No closed-end fund has ever gone bankrupt, and no BDC debt has ever gone unpaid.

We never know where the bottoms or tops are, but I see signs that the market is oversold. The market is pricing in an 80% cut in dividends. I don't see that happening. We're modelling 15% cuts for our portfolios; the average closed-end fund may experience a 20% cut in the next year, though there will be sectors and sponsors who are hit worse. As long as you stay diversified, haven't margined positions, and aren't forced sellers, you'll be okay. Remember, the fear you feel in situations such as today's is often positive, because other people feel also that fear and when there's no one left to sell, asset prices can recover. I think that pain is going to build the base where NAVs can stabilize as the market gains more liquidity and discounts can come back towards normal levels. As in '08-09, we will observe a slow narrowing of discounts as time heals wounds.

---

## Investment Perspectives and Strategy

We build multi-sector, multi-manager portfolios, because no one sector or sponsor is perfect. We focus generally on the income side, with some growth component. We look for sustainable dividends, discounts that are more likely to narrow than widen, and net asset value in sectors that we can overweight. We like managers who can wander and be active, since that's the point of active management. In the current turbulent environment, we like munis, senior loans and preferred equity (higher on the capital structure than equity), multi-sector bond fund managers whom we know well, utilities, REITs, and the top 10-15% of BDC managers. Generally, fixed income tends to bounce back much faster than equity funds since there's a floor—all that matters is if the income payments continue coming in.

Munis, for example, I think are very, very attractive now. Muni funds are the most diversified investments, and I don't see any near-term issues for muni bond distributions at the sector level. If interest rates start to rise again, that means the economy is getting healthier. We looked at the correlation of a muni fund's market price to its net asset value over a 90-day rolling period to inform us of how much the current movement is going with or against net asset value. It rarely gets above ninety,

but we are there now. When discounts are wide and correlations are up, it's often the bottom; it doesn't mean it's free of volatility, but it's where a bottom can be formed. There is currently a lack of liquidity in the muni market, but that will at some point be resolved.

Retail-oriented BDCs are the exact place to experience high volatility, the highest levels of fear. Coming into this weekend, BDCs showed an average 19% yield and a 47% discount. In this environment, when some BDCs are trading at ten to twenty cents on the dollar, I may not bottom fish, but I'd definitely look for dislocations that are significant and where liquidity is not going to be an issue. Quality BDCs have one of the best structures to work through the uncertainty, but I would say stick to top tier and high quality.

Last week we refocused parts of portfolios into lower-levered, lower beta, easier dividend policies. A quick and dirty method is to sort by yield: The lower the yield, the safer investors think that dividend is because they're not requiring really high numbers. If you're currently an owner of funds in the bottom tier, the market is telling you it's expecting a dividend cut. But we're seeing discounts of over 35%; dividends can be cut, and you can still get through it. Our models right now are for 80-85% of diversified income through the next two years based on -25% GDP next quarter and

---

a 20-25% unemployment rate. Bear in mind that leverage is very cheap today; there has never been a better time for prudent use of leverage in a closed-end fund structure. If you were going to navigate this storm on your own, I would overweight the sectors I mentioned earlier. Lower beta, lower leverage, lower leverage-to-NAV yield are the types of funds I'd be searching for, and a great way to stay invested and remain comfortable as an investor. On portfolio construction, stay diversified, stay active. If you're an income investor, the yields are immense, and even with 20% haircuts, there's still a lot of cash flow that can survive the future. As an income investor, you don't need to worry about the price movement of the investment; of more concern is the direction of the income. I know the pressure is immense out there; but avoid panic selling. We can get through this; closed-end funds are the right structure to do so. It may not feel like it at this moment, but the rear-view mirror will look a lot better down the road.

There is a chance that, with so much pessimism in the market, any good news could turn this around quickly. In the past, we've solved really hard problems. Markets are pricing as if we can't solve these hard problems, and that we'll live in caves and can never go to the office again. My best guess is that, in a matter of weeks or months, this will bottom out. Clients I have who were buying bond funds in '08 and early '09 are still bragging about the purchases ten years later.

## AICA

We are working on a schedule of webinars through the Active Investment Company Alliance with both our members and participants in the sector. If you would like to be involved, go to [AICAlliance.org](http://AICAlliance.org) and let us know. Whether you're a product manager, a closed-end fund advisor, an analyst, a fund sponsor, or a service provider, we'd be delighted to hear your story or research and for you to have a seat at the table.

Disclosure: The opinions of the speakers / presenters are their own opinions and may not be the opinions of AICA. Listed closed-end funds and business development companies trade on exchanges at prices that may be above or below their NAVs. There is no guarantee that an investor can sell shares at a price greater than or equal to the purchase price, or that a CEF's or BDCs discount will narrow or be eliminated. Non-listed closed-end funds and business development companies do not offer investors daily liquidity but rather on a quarterly or semi-annual basis, often on a small percentage of share. CEFs often use leverage, which can increase a fund's risk or volatility. The actual amount of distributions may vary with fund performance and other conditions. Past performance is no guarantee for future results.