Rob Shaker of Shaker Financial Focuses on Discounts to Get Paid in Closed-End Investing

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In this bonus edition of the NAVigator podcast taped at the AICA Boot Camp and Round Table in New York City on November 6th, Chuck Jaffe interviewed Rob Shaker, portfolio manager at Shaker Financial. Read the Q & A below as Chuck discusses with Rob about why his primary focus in choosing closed-end funds is the discount level, buy why all discounts are not created equal.

Rob Shaker

The podcast can be found on AICA's website by clicking here: https://aicalliance.org/alliance-content/pod-cast/

CHUCK JAFFE: Hi, it's Chuck Jaffe, host of The NAVigator podcast. I attended the Active Investment Company Alliance closed-end fund, business development company, interval fund Boot Camp in New York City on November the 6th. While I was there I did several interviews with closed-end fund experts for Money Life, my radio show and podcast. We're bringing those interviews to you as bonus episodes of The NAVigator, enjoy. Welcome back to Money Life at the Active Investment Company Alliance Conference in New York City. I'm joined right now by Rob Shaker, he is chief investment strategist at Shaker Financial, a firm that puts together portfolios of closed-end funds and uses them for separately managed accounts. And Rob shared a panel with me. Well, he was the panelist, I was the moderator. So he was the important one, I was just the host, as I am again. But he left me with a couple of good questions and a couple of things I think investors can benefit from. First, Rob, thanks for taking the time.

ROB SHAKER: Thank you.

CHUCK JAFFE: So when we were talking, you made it very clear that for you as a closed-end fund investor, it's all about the discount. Most of the time when I talk to closed-end fund investors, they always say, "Well, make sure that the discount's not fool's gold, it's not leading you astray." So when you're saying it's all about the discount, explain what it is that you're looking for, and how do you tell which discounts are real and which ones are those fool's gold?

ROB SHAKER: Well that's an interesting point. I think that one of the problems that most novice closed-end fund investors may have, is thinking of a discount in absolute terms. A discount in absolute terms means nothing. You can have a discount that's a small discount, that's two percent, or fourteen percent, or even a five percent premium. That isn't necessarily a good or a bad thing, or over-valued or under-valued thing. It's the relative discount to where that particular fund trades over time that you're really looking for. So at Shaker Financial, what we're looking for and what our models help us understand, is when is an individual fund's discount artificially wide? In which case we'll accumulate. Or artificially narrow? In which case we'll sell it out.

CHUCK JAFFE: I talked earlier today for the show with Bill Meyers from Nuveen, and he was talking about how he thinks investors should pay less attention to the discount and more be focused on, what are the underlying assets that they're buying? He's like, "Don't worry so much about the discount, worry about how do these assets fit into my portfolio?" How do you respond to his take less focus on the discount, when you say you put more focus on it?

ROB SHAKER: Well, as a firm that is managing closed-end funds, I hope that's exactly how he feels. Because that is what he can control, is how they are managing their fund. As an investor you have more options. Now we stay fully invested at all times in all of our separately managed accounts. When doing so we can have a Nuveen as part of our equity, or we could have a different family of funds. So to us, what's more important is where are we going to be able to generate the alpha from? Sometimes it's with Nuveen. We happen to own a lot of Nuveen's. But that doesn't mean we're going to be tied to that Nuveen in terms of, if we can buy it and sell it and get a two percent alpha discount capture, then we will do that.

CHUCK JAFFE: Explain to my audience, because alpha discount capture is a little much. But there is a plain English term for this.

ROB SHAKER: Well, the easiest way to describe it, I believe, is just you're buying a fund that's undervalued and selling when it's overvalued, right? And so what you're basically doing, is if you're going to buy a fund, instead of investing in SPY to get market movement, you buy a closed-end fund that's going to move with SPY and it's NAV. If you can buy it at a discount that's one under its average and then sell it at one over, then you're going to make whatever SPY made in the holding period plus two percent.

CHUCK JAFFE: In terms of closed-end funds, there's been a lot of changes to the industry, a lot of growth in the industry, but new funds come out typically highly leveraged and can be tricky situations. So for you, how old does a closed-end fund have to be before you can get interested in it?

ROB SHAKER: Well, we will never buy a fund at its IPO. Mathematically it's not in your favor. The first time that we'll look at an IPO is the first tax loss season. Typically depending on what time of year the IPO hit the market, it'll probably get sold off either in that first tax loss cycle, or the second, and that's when we'll start investing in it.

CHUCK JAFFE: And again, it'll be how much it suffers through that tax loss cycle to wind up at a discount that is favorable to you?

ROB SHAKER: Correct. In a good tax loss season, you're really going to get your bottoming out of discounts and your best values somewhere between December 24th and December 30th.

CHUCK JAFFE: In terms of looking for those discounts, you made a point that last December, not quite a year ago when the market was tanking, the discounts were growing, the funds were losing value, and investors were panicking. And that's exactly when they should have been doing the opposite. Is that a fundamental thing? That if you don't understand that when prices fall and discounts get bigger, you want to be in closed-end funds, is that your sign? "Hey, you. Don't invest in closed-end funds."

ROB SHAKER: Right. If you're the type of person that wants to follow the herd and follow the sentiment, closed-end funds are not good for you. Because closed-end funds will be at their most attractive for purchase when sentiment is the worst, and they'll be at the best sale levels when sentiment is overdone.

CHUCK JAFFE: For my audience, which in many cases is learning now about closed-end funds and is going to have one or two as part of a broader portfolio, what are the advantages of getting a portfolio of closed-end funds? Whether it's through a separately managed account, or a mutual fund, or a what have you, versus, "I'll pick one or two individual closed-end funds"?

ROB SHAKER: I think for a normal retail investor, a couple of closed-end funds as part of a balanced portfolio is great. Particularly a fixed-income closed-end fund, they benefit probably the most from the fixed-capital structure because they can take long dated positions and not worry about redemptions. But if you really want to go like we do, all in on closed-end funds, it really is something that's probably left better to those who live and sleep in closed-end fund world.

CHUCK JAFFE: Yeah, and that's been an interesting crowd here. It's been fun to talk with you as part of this. Thanks so much for taking the time to join me.

ROB SHAKER: Oh, thanks. A pleasure to meet you.

CHUCK JAFFE: That's Rob Shaker, he is chief investment strategist at Shaker Financial. You can get more information at ShakerFinancial.com. There's more to come from Money Life at the AICA meeting in New York City, we'll get to it in just a moment.

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