Calamos' Bush: Low Interest Rates Have Helped Create Closed-End Opportunities

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Chuck Jaffe, in The NAVigator podcast, interviewed Robert Bush, senior vice president and director of closed-end fund products at Calamos Investments. Read the Q & A below as Robert says that the benefits of closed-end fund investing have been on display this year in the rebounding stock market coupled with the low rate environment, because that low on borrowing costs has helped funds profit from using leverage. He also discusses convertible securities, where many of the closed-end funds have not kept up with the underlying securities – convertibles are up about 20 percent on average, he says – creating particularly attractive opportunities now.

Robert Bush

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

CHUCK JAFFE: Robert Bush, director of closed-end products at Calamos Investments is here and we're talking convertible securities, the bond market, income opportunities, and more on The NAVigator. Welcome to The NAVigator, where we talk about all-weather active investing and plotting a course to financial success with the help of closed-end funds. The NAVigator is brought to you by the Active Investment Company Alliance, a unique industry organization that represents all facets of the closed-end fund industry, from users and investors to fund sponsors and creators. If you're looking for excellence beyond indexing, The NAVigator's going to point you in the right direction. Joining me today, well, it's Bob Bush, he is director of closed-end fund products at Calamos Investments, senior vice president there, and if you want to learn more about the firm and its closed-end products, well, it's Calamos.com, they're on Twitter @Calamos. If you want to learn more about closed-end fund investing generally, about interval funds, BDCs, and more, go to AICAlliance.org, the website for the Active Investment Company Alliance. Bob Bush, thanks for joining me on The NAVigator.

ROBERT BUSH: Thanks for having me, Chuck.

CHUCK JAFFE: We are living in these times where interest rates are lower for longer, and Lord knows, people not excited by them. And yet, I've read your commentaries and I know that at Calamos you're actually pretty excited right now about the income opportunities that are out there, and particularly so in closed-end funds. Explain why you see things that I think the average person is looking at going, "I don't know what I'm going to do with this income stuff right now."

ROBERT BUSH: The great thing about closed-end funds is that many of them do provide income, as you pointed out, through multiple different investment strategies, whether it be fixed-incomes, whether it be equities, convertibles, U.S. domestic, foreign, there's a whole bunch of different opportunities there. And the use of leverage, which is oftentimes borrowing at short-term rates and reinvesting at longer-term rates or the equity markets has had a positive spread. And what this does is it allows that difference to be kicked back to the shareholder, whether that be an improvement through the net asset value, but more importantly through income distributions. Again, whether it be through capital gains, whether it be through fixed-income. So closed-end funds in an environment where you had a recovery in the equity markets, a recovery in the fixed-income markets since the onset of COVID earlier on, coupled with low borrowing costs has really been a great opportunity in the space.

CHUCK JAFFE: The space of course has been helped by the fact that, yes, you can buy in at great discounts, but those discounts have narrowed. How are the discounts now relating to where we'd expect them to be historically, still good deals to be had?

ROBERT BUSH: It's very interesting, if you look at the macro investment thesis that's taken place sort of at the general index level and then you look at what's gone on in the closed-end fund market, oftentimes a different dynamic. The closed-end fund market is dominated by retail investors, so inherently without a lot of institutions at play there tend to be inefficiencies, and those inefficiencies oftentimes result in what we call discounts or sometimes premiums. What's happened in the closed-end fund space this year, which has been sort of representative of the market in general is a tremendous amount of volatility, and during volatile times, oftentimes retail investors will used closed-end funds as the first source for cash. So we saw discounts widen tremendously with the onset of COVID in the first quarter, somewhere north of 20-25%, those narrowed as the markets recovered. But as the markets continued to recover, it's interesting, you still had a lot of volatility in there. What's happened is it's resulted in situations where you've had NAVs, particularly in the convertible space where convertible bonds have had a great year, upwards of 20% returns year to date, but the closed-end funds, the prices of those have only participated about half of that. So what that's done is it's basically given you in some cases double-digit discounts in many funds where the market has not kept up with what the appreciation and performance on the NAV has been. And I think a large part of that is just there's a concern that many of these funds may not be able to continue to make their distributions, that there's concern about getting back in the closed-end fund space, maybe the retail investor would rather sit in cash, maybe they're going to something that's maybe a little less risky, not leveraged. So I think you're seeing some great dynamics here in the closed-end fund space, where it's unusual in that the discounts are forming because the NAV is outperforming the stock price, typically it's that the NAV is underperforming the stock price. So if the NAVs are declining and the stock price is moving down with it, and many times in excess of that, or a closed-end fund is cutting its distribution rate, or a closed-end fund is having a large portion of its distribution return to capital. None of that, at least in the context of our funds, is the case. It's just that the market for whatever reason is not keeping up, the price is not keeping up with the NAV performance hence a discount, hence where I see tremendous opportunities right now.

CHUCK JAFFE: Let's talk about one area where Calamos particularly specializes, that a lot of other people they don't necessarily understand the opportunities there, and that's convertible securities. It's a big part of a number of Calamos closed-end funds. Convertibles of course are kind of a hybrid, they're not a bond entirely, they're not a stock entirely. Talk about the outlook for them in this market and why they're perhaps particularly well suited.

ROBERT BUSH: That's a great point Chuck, because convertibles have had a phenomenal run this year, upwards of performance of 20% plus. We've had phenomenal issuance both int he U.S. and across the globe. Again, convertibles is access to capital. In fact we've had the best issuance since 2007. Globally year-to-date it's been about $125 billion of $33 billion in the U.S. market, and that's been the best since 2007, so there's plenty of product out there. The other thing that's good is you've seen a cross-section of issuers. You've seen it not just in a financial area, but you've also seen it in consumer discretion area, you've seen it industries, we own Tesla, we own Southwest Air, we own Royal Caribbean, along with a Wells Fargo, which again banks are traditional issuers of convertibles. But my point is that if you believe that you're going to have more of a synchronized recovery in the general markets than what you've seen here, which heretofore has been more isolated with the tech stocks and some of the consumer services stocks. The convertible market, because it's investing now or issuing now in a broader array of sectors, we're going to be able to participate in this reopening up of this economy. Which you've seen a lot today obviously with the announcement of Pfizer with what will hopefully be a vaccine, you're seeing these opening up economic sectors. You're seeing the airlines going up, you're seeing the cruise lines going up, sort of the normalization if you will. And again, because the convertible market is extended into these areas because you've had such a large issuance today, we're able to participate in that across the board, and that's translating into our investments not only in the closed-end fund space but also in the open-end fund space.

CHUCK JAFFE: Do you believe that the things that are creating volatility, even if it's positive volatility, will kick in and create a bunch of volatility for closed-end funds in general?

ROBERT BUSH: Again, you have to sperate what's going on in the portfolio, which reflects in the NAV, versus what the closed-end fund market is doing, which reflects in the price. Now typically as we approach year-end as we're coming into November, a lot of times there'll be some tax-loss selling, investors may get out of closed-end funds to pay taxes. Again, they tend to utilize closed-end funds for sources of cash, so you've got that pressure on the space in general when you come to year-end. But the flip side is this, again leverage is relatively inexpensive if you look at what the borrowing rates are, where LIBOR is. And again, the borrowing rates in many closed-end funds are short-term and they're based off of LIBOR. If you're borrowing off of LIBOR right now, it's less than 1%. And if the general markets are doing well, whether it be high yield, or whether it be convertibles, or the general equity markets, the S&P, the MSCI, you're going to have a nice spread return there between what you're borrowing at and what you're reinvesting at. So what this should do is give some comfort to the closed-end fund market that, look, these funds are doing well, they've improved. More importantly they're earning their distributions as opposed to just paying return of capital because their NAVs are improving, and there's less concern that the decking NAV is going to result in more return of capital. So I think fundamentally hopefully the message to the market is that these are well-positioned. Again, leverage is a friend now as markets go up, that they should continue to do what buyers expected them to do as far as performance. Hopefully that translates into the equity price. Again, it's a different dynamic as we've said, but hopefully the rising NAV and the consistency of distribution and those distributions being earned is not a result of return of capital are all favorable things that hopefully the market will understand. That's why programs like this are so good because you need to get the message out, you need to tell the investors exactly what's going on in this space. Because frankly, the analysts that cover this space are excellent but there just aren't enough of them out there, so it's incumbent upon issuers like Calamos to make sure that the users and the financial advisors really understand what's going on in the space. We do a number of calls, we have a number of information out there, our website, it's all out there and we certainly invite any investors to take advantage of that.

CHUCK JAFFE: Bob, great stuff, thank you so much for joining me on The NAVigator. Please come back and do this with us again down the line.

ROBERT BUSH: My pleasure, Chuck. Thanks so much for having me.

CHUCK JAFFE: The NAVigator is a joint production of the Active Investment Company Alliance and Money Life with Chuck Jaffe. I am Chuck Jaffe and you can find my show on your favorite podcast app or at MoneyLifeShow.com. To learn more about closed-end funds, interval funds, and business-development companies go to AICAlliance.org, the website for the Active Investment Company Alliance. They're on Facebook and LinkedIn @AICAlliance. Thanks to my guest Robert Bush, director of closed-end fund products at Calamos Investments, learn more about him and the firm at Calamos.com and on Twitter @Calamos. The NAVigator podcast is available every Friday, please subscribe on your favorite podcast app, and if you like us leave review and plan to join us again next week to learn more about investing in closed-end funds. Until then, stay safe everybody.

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