



Convertibles Are Acting More Like Stocks Than Bonds

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Chuck Jaffe, in this episode of The NAVigator podcast interviewed Tom Dinsmore, Portfolio Manager at Gabelli Funds, which manages the 50-year-old Bancroft Fund and several other issues that specializes in convertible securities. Read the Q & A below as Tom says that investors looking to increase yields with a 'bond-like equity' will be hard-pressed to create a portfolio of currently available convertible issues that do the job. He notes that many new convertible issues – coming

from health-care and technology companies – require the underlying common stock to do well, and don't carry big coupons, so that investors should use them as a lower-volatility equity alternative.



Tom Dinsmore

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CHUCK JAFFE: The Bancroft Fund just celebrated its 50th anniversary, and today we're talking with manager Tom Dinsmore about the fund and the market for convertible securities. This is 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's 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. And of course if you're looking for more information on investing in closed-end funds, business-development companies, and interval funds, go to AICalliance.org, the website for the Active Investment Company Alliance. Today on The NAVigator I'm joined by Tom Dinsmore, he's Tom Dinsmore, Portfolio Manager at Gabelli Funds, which runs the Bancroft Fund and the Ellsworth Fund, and also Gabelli Convertible Securities; which they're all part of the Gabelli family so you can learn more about them at Gabelli.com. Tom Dinsmore, thanks for joining me on The NAVigator.

TOM DINSMORE: Thank you very much, Chuck.

CHUCK JAFFE: The Bancroft Fund is the oldest of the funds that you're involved with, and as I said it's just celebrated its 50th anniversary. You guys got a little bit of facetime with the stock exchange when you were doing that. You haven't been running it for all of that time, you've been involved with it for about 40 of those years. But just quickly, how has running a closed-end fund changed over the decades? I mean, obviously technology has changed, but the investment object hasn't really changed, so has the job changed?

TOM DINSMORE: The job has changed. I mean, 50 years ago, 40 years ago you could be a small money manager that ran a closed-end fund or a convertible fund and be able to compete with the big boys. Then later on in the 2000s, the regulations changed, so they made it tougher to be a small guy. So that's why we came to merge with Mario Gabelli's firm, which has been a wonderful marriage between Dinsmore and Gabelli, and I think our shareholders are much better off for it.

CHUCK JAFFE: Right now I would imagine that convertibles, well, with everybody looking for additional yield, with the market making it that people are saying, "I want to change what goes into the 40% of my 60-40 allocation in things," I would imagine that convertible securities are seeing enhanced interest. A, am I right about that? And B, what's that doing for the market?

TOM DINSMORE: Well, you're absolutely right about it. And the approach that we take to investing is a total return approach, and we try to make people understand that this is a reasonable replacement for equity exposure. It's not as safe as certain fixed-income exposure might be, it's not as volatile as much of the equity investments might be. We've been able

over long periods of time to provide returns that are directly competitive with the S&P 500 with 70-80% of the volatility.

CHUCK JAFFE: It's important that you immediately gravitated towards the equity comparison and not the bond comparison.

TOM DINSMORE: Absolutely.

CHUCK JAFFE: Because what's happening for so many individual investors is that they are looking for bond-like equities. They want things that maybe act and feel like bonds but they're not buying bonds because the bond market isn't giving them enough total return. Do convertible securities fit that bill? Because they're a hybrid, are they enough of a bond to be a bond-like equity?

TOM DINSMORE: I would say in this particular market the answer is no. I really think that while you can find a few convertible securities that might meet that criteria, it would be very difficult to create a portfolio out of current convertible issues available to investors to put them in a position to have that kind of return.

CHUCK JAFFE: And what is driving that in the market?

TOM DINSMORE: The new issuance. I mean, let's face it, the biggest issues now are technology and healthcare companies, and they're issuing converts that really require the underlying common to do well for you to get the kind of returns you're hoping for. They don't have big coupons, they have fairly sizeable premiums, but that's because you have a volatility of the underlying common stock that makes the embedded option worth substantially more.

CHUCK JAFFE: So ultimately, when we talked about the changes that we're seeing from running the fund, the other change at least right now is the type of things that are coming into the convertible market. Because the classic convertible was basically you're buying a bond that if the stock does well enough it'll convert to an equity and you'll get a bonus. Now it's kind of like, you'll buy a stock with a little bit of a buffer to it.

TOM DINSMORE: I think that's a fair comment. I mean, let's face it, 20 years ago I could tell people that we would have only 60% of the volatility of the stock market and we'd still give very close to equity returns. Now it's much closer to 80% of the volatility, so it's up a little bit more with still the same or very similar returns to the stock market.

CHUCK JAFFE: I mentioned that you run multiple funds. Of course the Bancroft Fund, ticker BCV, the Ellsworth Fund, ECF, Gabelli Convertible, that's GCV, all in the closed-end space, and

then also the TETON Convertible Fund which is WESRX. I'm curious, between them, given the way the market is constructed, how much of your portfolios are the same? You're looking in the same space, how much do you try to differentiate? Because the convertible market is big enough at this point that you could say, "Hey, I want to own technology driven convertibles versus I want to own financial driven convertibles." How much of a distinction is there from one convertible to the next, at least in your stable of funds?

TOM DINSMORE: Well, in our stable of funds, Bancroft is a pure convertible fund portfolio. Mostly US domestic, a little bit of international exposure, but US domestic just pure convertible fund with a very modest amount of leverage. That's the advantage of the closed-end fund. We have a 5% managed dividend distribution policy and we work around that for our shareholders. Ellsworth has a bit of room in it for common stocks that we believe exhibit significant convertible-like features, such as a good yield or occasionally we'll continue to hold a common stock from a convertible that we loved but we were forced to convert for technical reasons, maturity or a call or something like that. So that fund may have 20 or 25% in common stocks. GCV is a bit more of an international exposure to it. The Gabelli team helps us manage a portion of it as well, so we're not the pure management team of GCV. We get a bit more of the influence from the whole Gabelli organization on that. The TETON open-end fund, we're actually the sub-advisor to that, and we've just put in the basic, the best converts we can find. It is obviously unleveraged. BCV, ECF, GCV are leveraged to an extent. GCV has a large managed distribution policy of 8%, ECF is 5%, BCV is 5%, and that's how we differentiate the different funds.

CHUCK JAFFE: And of course leverage being one of those reasons why you might want to own a closed-end fund as opposed to a traditional mutual fund. We're talking all this about convertibles and I haven't really asked you for your market outlook. But as a manager for convertibles given the situation that we're seeing, what is your market outlook?

TOM DINSMORE: Well, we anticipate that interest rates will rise a little bit, and that historically has not bothered convertibles. It does tend to cause the premiums embedded in convertibles to narrow a little bit, but the underlying common stock is much more important to the performance of the convertible. We think that as long as the Fed is being relatively liberal with the monetary policy, we don't anticipate a large decline in the stock market. But hey, I've been in this game long enough to know that what we anticipate and what actually

happens can sometimes be very different. I enjoyed your *Dude You're Not Rich* column, that's a big warning to anybody who wants to make a projection to the future. Because you have a tendency to get used to the way things are going now and not recognize that something is changing. That even just the process of having things move along as they are, you're moving on a road that is going to have to turn off at one point in time or another. We're comfortable with the portfolio as it is. We don't try to anticipate major changes in the market but we try to set up a portfolio that if the market fluctuates significantly we can weather it.

CHUCK JAFFE: Tom, great stuff. Thank you so much for joining me to talk about.

TOM DINSMORE: Very good. Thank you very much, Chuck.

CHUCK JAFFE: The NAVigator is a joint production of the Active Investment Company Alliance and Money Life with Chuck Jaffe. I'm Chuck Jaffe and you can check out my show on your favorite podcast app or you can learn about it, and oh by the way, you can find my column, the *Dude You're Not Rich* column that Tom was talking about, at MoneyLifeShow.com. To learn more about interval funds, closed-end funds, and business-development companies go to AICAlliance.org, the website for the Active Investment Company Alliance. On Facebook and LinkedIn @AICAlliance. Thanks to my guest, Tom Dinsmore, chairman and chief executive at Dinsmore Capital Management, the convertible bond specialist who manage the Bancroft Fund, the Ellsworth Fund, Gabelli Convertible and more. They're all in the Gabelli family, so get more information at Gabelli.com. The NAVigator podcast is available every Friday, follow us on your favorite podcast app and join us again next week to learn more about investing with closed-end funds. Until then, stay safe everybody.

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