John Cole Scott provides welcome remarks to the 2021 AICA Interval Fund Boot Camp & Manager Spotlight along with a presentation on “ABCs of Interval Funds”.

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John Cole Scott, Founder and Executive Chairman of the Active Investment Company Alliance opens the 2021 AICA Interval Fund Boot Camp & Manager Spotlight with opening remarks and with a primer on interval funds. Read the transcript below to hear what Mr. Scott had to say to kick off this event.

John Cole Scott

To view the rest of the conference events and panels go to:
[Interval Fund Boot Camp & Manager Spotlight - AICA (aicalliance.org)]

John Cole Scott: Good morning or good afternoon wherever you may be. My name is John Cole Scott with the Active Investment Company Alliance. I want to thank you and welcome you to the AICA’s Interval Fund Bootcamp and Manager spotlight. AICA was started in the summer of 2019 as a desire to create diverse and high-quality content across the ecosystem of traditional closed-end funds, business-development companies, and interval funds. My firm, Closed-End Fund Advisors, which is 32 years old, is focused on separate accounts in the closed-end fund space. We developed a data business in 2012 after a partnership with Fundamental Data previously, and have had an independent traditional closed-end fund data set since 12/31/2011.

In 2014 we added BDCs to our coverage and focused the firm, and in 2018 we added interval funds and more recently tender-offer funds to our database and focus at Closed-End Fund Advisors.

We felt that a non-profit that was balanced between the creators of funds, so fund sponsors, the user of funds, which could be analysts and institutional investors, financial advisors like yourself, and other family offices would be a useful core part to keep the quality and focused eye. We also recognize in the fund sponsor ecosystem there's tremendous work done by accounting firms, law firms, distribution firms, compliance firms, PR firms. The service providers that actually do the stuff that investment people hate but require to brings products to financial advisors and investors.

We want to thank our sponsors, we have members of AICA speaking, and non-members speaking, that's part of the approach to the non-profit. But sponsors like Northern Trust, which subsidizes AICA to support and create content for interval funds, as well as UMB Fund Services, which is part of this event and a very welcome addition to content that we've created. We want to make sure you know if you're not sure that AICA does a weekly podcast, *The NAVigator*. I've put a shortcut on the right-hand side of the event. We have 85, actually 86 recorded, 85 released so far. It comes out each and every Friday, we transcribe it, post it on our website, and then you can even search for it by keyword or person's name to find those sessions which might be interesting to you. We also put a link to the fund screener on AICA's website, AICAlliance.org, I assume you all found it because that's how you registered for this event, and you can filter and sort any interval or tender-offer fund with limited data off of CEFdata.com.

If you haven't done so yet, please click the right-hand. There's a little circle in the upper right hand corner, you can add a photo, logo, name. You can put a LinkedIn profile if you choose. You can put a link to a scheduling app if you have one. If you have a great conversation between the sessions or after and want to follow-up later, a great way to connect here. We really like this remote platform but we also recognize we miss in-person. We do expect in '22 to offer some sort of combination in-person and virtual content for AICA. We expect that to be by partnering with other organizations and looking for key content and key cities.

Remember during each session, we've actually really focused for each moderator and presenter, that we really want 10 minutes of questions so we can really get that whatever you're thinking or interested in broadly communicated to the entire audience. Please start thinking of them during this session, type them in the Q&A box. There's no questions for this yet because it's not a presentation, but we'll be watching that and making sure we make this event as timely and personalized as possible. There is a survey link in the upper right-hand corner. Before you leave, if your schedule allows and everything's fresh, please go ahead and fill out the survey so we can get your feedback and make this event better going forward.

There is an AICA support table just below the agenda, and that will be staffed by at least one person from our team for any issues you might be having from the event logistics. If it's a tech issue they can be somewhat helpful, but there's also the Remo support link on the lower left-hand corner which should do well. With that, I'm going to start the presentation, the ABCs of Interval Funds, and we'll get started in the day. And the first panel, as you'll see in the agenda, is at 1:25. I'll tell you, it's been really interesting, nobody missed a flight but we definitely had some tech issues we've mostly resolved.

John Cole Scott: So this is a chance to make sure, we have 14 managers or people from funds on four panels, and they're all non-listed closed-end funds. So we want to make sure we cover some of the basics here, and this is a presentation that we'll show or adapt and improve over time. We borrowed this from UMB FUSE report that came out last year, and really as you think about the interval fund structure, our firm Closed-End Fund Advisor was traditionally focused on listed closed-end funds. We liked intra-day trading. We liked that there was a potential discount to net asset value. We liked that liquidity and access to active management. I was born owning traditional closed-end funds because my father was on the board of one.

But if you think about the non-listed structure, it's an inflow daily, you can invest it any day you want, in our experience in the funds we used for our clients at Closed-End Fund Advisors. But you only get these tendering periods. And these tendering periods typically for most of the funds that we use, and we see growing in popularity, are a quarterly tender of around 5%. And then what happens is you're able to, if you want your money back they can offer up to 2% over their offering, and so think 7%. And in that concept it's basically giving you less volatility because there's no market price, and more visibility. All the funds we use pretty much are daily net asset values, a few are weekly for interval funds. And it's that nice balance between a closed-end fund. And really more transparent and more oversight than a private equity or hedge fund, but some of the features, there are funds for accredited investors. You'll learn about one of them today on panel #4. We have to be an accredited investor because you're in a fund of hedge funds. And so that's part of the process.

But where we like it, where it's really been useful as you're see, is really good access to illiquid active management in less traditional equity and fixed-income investments. And you'll see that a lot of the growth there has been maximizing that illiquid bucket for many of the funds and basically not worried about a discount to net asset value because of not understanding the quarterly marks. If you ever looked at the equity BDC sector, there have been and there are some great funds there, but they don't traditionally trade very well off their net asset value and that I think is one of the reasons why the interval fund structure can be so powerful for this type of investing. Not going to spend a lot of time on it. This comes from our quarterly deck for Closed-End Fund Advisors, just to give you a sense of the universe of listed funds that we cover. It's about $300 billion, about 535 ticker symbols. We do a very deep report every quarter, I believe it's April 14th or 15th this next quarter, that you may want to attend if you really like the listed funds.

The main thing we see people trying to avoid is discount downside. Now firms like ours are built to take advantage of recovering discounts, and what can be an attractive discount, and which discounts are permanent versus uncommon. But what the non-listed fund structure really is trying to solve is active management, alternative investing, and you don't have to worry about a two discount or two premium falling to a 15% discount. Now there's no benefit of going up on the way up, but we find that giving up volatility for liquidity is a decision we made at our firm to allocating client portfolios to interval funds. And so we tend to do allocations to a handful at a time in a portfolio, and in all those conversations with clients we're talking about, "Well, this is why we're using this fund." Either there isn't a closed-end fund like, it gets us this feature and benefit, or we want to drop your volatility and discounts are relatively narrow. Which right now discounts are relatively narrow for listed closed-end funds. If you're an advisor traditionally using listed closed-end funds and haven't dug in deeply to interval funds, now is a rather attractive time in my opinion and my guess, is moving some assets from the listed side to non-listed.

Just quickly, I want to talk about there's only five interval funds with a 10-year track record. The oldest is presenting here, very excited. Invesco came out in 1989, right when the regs were brought to fruition to bring out a senior loan fund. A perfect use of illiquid guts, active management, and the use of the wrapper. And there's only 13 funds that have a five or 10-year track record, 15 three to five, 28 have a one to three, and there are five that are under one year old and are reporting data into our data system. Which means we're seeing some assets, some leverage, some holdings, something that's making it an active and I would say looking to grow in the market. That's a huge growth rate and I think it's proving the structure successful. And why if you look at the managers in the space, most of them are here, many of the ones that we like and use for our firm are at this conference, are able to show why they're growing and why they're interesting.

I wanted to make sure we cover that tradeoff liquidity for volatility, and that avoids pervasive discounts like I said. And we have a chart later which talks about the volatility that we experience in the Covid which is the perfect example of this structure. Remember with a 5% quarterly tender, which is the most common use case, you can have 80% illiquid private things. And the more you maximize that bucket generally speaking, the better off you are for using this fund structure when we advise fund sponsors, new and joining the space. Versus you can only have up to 15% those types of investments in an ETF or open-end fund structure, and many people shy. Under 10 and under five is the most common cause of the risk of that redemption drag on the portfolio.

One thing, being a closed-end fund investor on the listed side there are managed and leveled distributions, which can be sustainable, which can be unsustainable in our opinions. But one thing I've noticed from most of the funds is that they only pay out what they're earning because there's no risk of a discount from changing their policy. So we see a little bit more, like they actually pay out for credit funds, we believe we see in the data, most of these firms are paying out the net investment income they have. And so it's much more like a real portfolio. It's not smooth but that's because leverage costs change and dividend income comes in differently every quarter, and most funds pay quarterly because they align themselves quarterly. But I really like that concept, it just really can make you feel more comfortable for this structure.

The minimums for investments can be misleading. We pull those from the prospectuses, and I can tell you how commonly we own under a million dollars, sometimes under $100,000 of an interval fund and we can buy it in $5,000 chunks. So that is a conversation between you, and your custodian, and the fund sponsor about what their actual minimums are, what they allow and what they prefer. And so I just would say sometimes you'll see a large minimum in a share class, definitely worth reaching out to the firm and your sponsor and a custodian to make sure.

Leverage use is less common and usually lower than we see in listed funds and some pure comps. And I find some of these funds are really excited to bring, they believe, above average yield without leverage, and they're choosing not to. And I would argue if you've not choosing leverage in 2021, I just re-fied at 2.5% for a mortgage, that you're probably not going to lever unless something else changes in your investment committee's focus. Now you do need approval by a custodian to use interval funds, the custodians have to onboard these, that's usually in the alternative department. One thing AICA came out to do was to help with that, and pro rata tenders.

Checking the time I know I need to push up a bit because we have a session coming up. This is a chart on the growth rate. These slides will also be available and sent to everyone who attends live or replay. This is some focus on some average yields and average expenses. This is that slide I really, really wanted to cover, it's the last content slide. We looked at four interval funds with similar, they're not exact, listed closed-end fund peers. And we covered this in the podcast back in April, maybe in May of '20, but ran the data April 20th of '20. Essentially we found that the leverage tended to be less leverage, we had generally lower expenses, we had less NAV volatility. Now remember, you don't buy listed closed-end fund NAV volatility, you buy listed fund market price exposure. But we actually, in our opinion with these four funds proved less volatility in the session, and yet, generally better performance. I think that's a decision you need to be thinking about as you consider which funds can make sense in your portfolio.

This is just a list of things we've seen file with some active data in the last two years, year and a half. And of course disclaimers because we all have compliance departments. With that, I'm going to stop sharing my screen and I'm going to end the presentation. And then we're going to have the next session jump on stage and give you your first level of content.

Recorded on March 31, 2021.

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https://AICalliance.org/