Robinson's Browne: How To Overcome Current Fixed-Income Struggles

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Chuck Jaffe, in this bonus episode of The NAVigator podcast interviewed Jonathan Browne, director of research at Robinson Capital. Read the Q & A below as Jonathan talks about how closed-end funds can help investors meet their needs for income in ways that traditional fixed-income strategies are struggling to do given current rate levels. By managing duration and supplying above-market yield - and by focusing on credit risk at a time when it is more worrisome than interest-rate risk - Browne says investors can better achieve income goals.

Jonathan Browne

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, and when I'm not doing The NAVigator I host Money Life, my own one-hour show that's available every weekday. Well, Monday on Money Life we were discussing closed-end funds with Jonathon Browne of Robinson Capital in a segment we call the Market Call. And because it was all about closed-end funds, The NAVigator's favorite subject, we didn't want you to miss it. So here it is as a bonus episode of The NAVigator, enjoy. Jonathan Browne, portfolio manager and director of research at Robinson Capital is here and we're talking closed-end funds now in the Money Life Market Call. It's Market Call time, the part of the show where we talk with experienced money managers and market observers about how they do their job. What determines what they're buying and selling, what they see happening broadly on the market now, and how they are putting it all together. And my guest has been on Money Life before, but in The NAVigator and not in the Market Call. So we were talking more broadly about closed-end funds with him then, today we're going to look at specific issues and more. His name is Jonathan Browne, he is portfolio manager and director of research for Robinson Capital. You can learn more at RobinsonFunds.com. Jonathan Browne, it's great to have you back on Money Life.

JONATHAN BROWNE: Yeah, thanks for having me Chuck. Glad to be here.

CHUCK JAFFE: Now we always start with methodology, and I know that a big part of your methodology, you've said that your clients are looking for maximum yield with minimum levels of risk like losses. That rule number one is avoid losses, rule number two is make sure you're paying attention to rule number one, that is a big thing with your clients. So obviously that impacts the methodology, but explain how it works and how you actually put that into action.

JONATHAN BROWNE: Yeah, sure. So we're an alternative fixed-income shop and we've been investing in closed-end funds for the better part of 10 years now. Given today's low rate environment, it's not apparent that traditional fixed-income strategies are solving the needs for investors anymore. You have lower yields and increased credit or interest rate risk, which isn't ideal for one's portfolio. We believe that closed-end funds solve a lot of those challenges, and so we manage a couple 40 Act mutual funds, one that focuses predominantly on the municipal closed-end fund space and the other is a multi-sector strategy that focuses on the taxable bond space. And so when we're looking at these closed-end funds, what really differentiates us is the fact that utilizing the fund structure, we're able to reduce or manage some of the risks that are inherent in closed-end funds. Sort of said different, with municipal closed-end funds we all know that they have long and levered durations, many well above 10 years. And in an environment where rates are this low and the uncertainty surrounding inflation, we're able to manage that duration down to inside a year while still providing above market yield. And we think that that's extremely attractive in this environment, and something that quite frankly individual advisors or investors are challenged to do on an account by account basis. On the taxable side, it's less of an interest rate risk and more credit risk. And so in a similar fashion we have the ability to easily reduce some of that credit risk within the fund while still maintaining exposure to closed-end funds and the above average income that they provide.

CHUCK JAFFE: Given that you're looking for alternative investments and alternative sources of income, there have been some developments in the closed-end fund structure. In fact, recently on The NAVigator I was talking with someone from Thornburg, which has just entered the closed-end fund space. And what helped to drive them there was the new commonplace pricing structure, which is kind of inside baseball, it's a bit jargony. But for you, as you look at the developments that we've been seeing in the closed-end fund space, some of the evolution here, is that creating other opportunities for you?

JONATHAN BROWNE: You know, it does create opportunities. I guess what I would say, it's always good to see innovation structures that may be more appealing to investors or in the closed-end fund space, structures or innovations that may help to reduce some of that perpetual discount that we see inherent in a lot of the closed-end funds. So any type of new structure, we're absolutely open to. With that said, we do track all taxable and municipal closed-end funds in real time, and so while that's one component of our analysis, we're going to be looking across the spectrum at discount levels, at how each manager has performed over the short term, long term, what are some of their inherent biases in their investment style, etcetera. So I would definitely say that that is a piece of the analysis, yes.

CHUCK JAFFE: In terms of where you're at right now with closed-end funds, closed-end funds have been a fascinating space to watch during the pandemic because oh my goodness, the discounts got enormous. And for anybody who was interested in closed-end funds and discounts are important, huge flashing buy signs. Then of course the discounts narrowed dramatically and it was maybe you need to back away, maybe we're not quite as attractive, and then things eased up. How do you see the space generally right now? And is it reasonably priced, is it bargain priced, is it pick and choose because there are a couple of bargains mixed in? How do you decide?

JONATHAN BROWNE: Obviously going back to right after Covid when discounts were 10-20% plus, any investors who understands closed-end funds could throw a dart at the wall, pick a closed-end fund and they were pretty confident that they were going to make money as discounts narrowed. We've seen those discounts narrow to single digits in many cases, and in the muni space we're seeing quite a few funds at a premium. I would say that how we're viewing the space going forward is we think that there are still absolutely pockets of investments that are attractive within closed-end funds. And part of that reasons is we see the setup right now being very similar to 2010-2013 when almost all closed-end funds traded at significant premiums. You have a Fed that's still accommodative, and you have a Fed that has explicitly said that they're going to keep short rates lower for longer. Which as we all know with the leverage nature of closed-end funds, their borrowing costs are going to stay muted which is ultimately a positive. And with yields being as low as they are, investors are looking for other areas such as closed-end funds to really fill that income void. And so all of those factors combined really lead us to believe that we're in an environment where we should see most if not all closed-end funds trade to premiums. With that being said though, I think this is a perfect environment where you really need to be selective and an active manager. There are many closed-end funds that are no longer attractive in our opinion right now but there are a handful that are. And so we think that utilizing a professional manager such as ourselves who's constantly all day every day looking at the closed-end fund space and really trying to understand where the value is, is going to become critical for the advisor community, for the RIAs, for anyone really who's investing in closed-end funds and may not have the time to consistently analyze each and every fund out there and whether or not it's an attractive opportunity or not. And so there's definitely room for closed-end funds and closed-end fund discounts specifically to narrow, but you do have to be careful which funds you're looking to purchase.

CHUCK JAFFE: So let's look at a fund that is kind of the poster child, the exemplar of what you're looking to purchase at Robinson Capital. What's a fund or two that really stands out to you right now?

JONATHAN BROWNE: One of the names that we like, we'll stay within muni land, is ticker MFM, the MFS Municipal Income Trust, for several reasons. One, compared to the space it's trading at a reasonably wide discount, almost 6% as we speak. But sort of the second level analysis that I think is important to really take a look at is its management's ability to put up solid returns over time, and it does rank well compared to the rest of the muni closed-end fund universe on that metric as well. So we think it has a strong management team and is trading at a wide discount relative to its history and on an absolute basis. So that's a name right now that we feel very comfortable with and like within the muni space.

CHUCK JAFFE: And what makes you sell? When you find a fund like that one, what ultimately winds up making you sell? Because if I buy something at a good discount and the discount narrows, that's not necessarily bad for me, maybe if it's a premium you want to cash out and get that little bonus. But what ultimately normally makes you back away from a good fund that you found over time?

JONATHAN BROWNE: Yeah, a lot of it will have to do with the discount. And so if we're looking at MFM and it goes from a 6% discount and starts trading at a premium over weeks or months, we'll look at it relative to the rest of the options available in the muni closed-end space to see how it ranks on a relative basis. We'll look at where its discount or premium sits relative to its own historical average, and we'll really use that to determine if there's a better investment outcome. Now if it starts to trade at significant premiums, we may decide that there's more risk by owning it and the discount widening than there is sort of return from that discount continuing to narrow further or the premium continuing to get larger. And so if that's the case then we may look to exit that closed-end fund entirely and we may invest in an ETF until that discount level returns to a level that we think it becomes attractive on a risk-return basis.

CHUCK JAFFE: Well, now we're going to get your quick and dirty take on some closed-end funds that my audience is particularly interested in. Well, we hope that Jonathan Browne might make your day, but it's going to depend on what he says if you're one of the lucky enough people to get through here. Jonathan Browne is portfolio manager and director of research at Robinson Capital, the Robinson Funds, RobinsonFunds.com the website, and of course Quick and Dirty is where we put our guest to your test. You can test our guest and see if you feel lucky by sending your name, your hometown, and the ticker symbols you're interested in to Chuck@MoneyLifeShow.com, hopefully it'll make it into an interview soon. And by the way, not just closed-end funds but ETFs, traditional mutual funds, and of course stocks. We start today with a request from Dan in Meadville, Pennsylvania, he wants to know about BKN. That's the BlackRock Investment Quality Muni Fund.

JONATHAN BROWNE: So I'm going to have to go ahead and say sell on BKN. Right now BKN's trading at an 11% premium, which is about 15% above its five-year average discount and almost 14% above its 10-year average discount, so lot of risk in that name if discounts start to widen. I will say it does have a good management track record, but again that discount widening out or getting back to any sort of historical levels could very easily erode a portion if not all of the NAV return to the fund, so I'm selling BKN.

CHUCK JAFFE: Yeah, the good news is it worked up to that big premium, the bad news is you maybe don't want to hang on. That's a sell on BKN, BlackRock Investment Quality Muni Fund. Sticking with munis, Mike in Redwood City, California wants to know about the Invesco Value Muni Income Trust, that's IIM.

JONATHAN BROWNE: I'm going to also have to give that a sell rating. While it's not trading at an 11% premium, it is trading at a 1% premium which is roughly 9% above its five-year average discount. Based on the models that we've built here at Robinson Capital, it shows as one of the most overvalued muni closed-end funds at present, so I think that any profit that may have been made would be better served capitalizing on and moving into a more undervalued muni closed-end fund at this time.

CHUCK JAFFE: So it's a sell on IIM, the Invesco Value Muni Income Trust. We'll stick with one more muni-oriented fund but go pretty local on this one. Andrew in San Jose, California wants to know about Eaton Vance California Municipal Bond Fund, that's EVM.

JONATHAN BROWNE: Yeah, so on EVM I'm saying this is a buy right now. It's trading at almost a 6% discount with a 4+% dividend that looks to be covering. So again, anyone in California, we think it's a great option for a state-specific muni at present, so I would be a buyer here.

CHUCK JAFFE: Finally a muni fund that he can get behind, Jonathan Browne, and in this case it's the good getting behind, not the kind of being left behind like that sound was. Eaton Vance California Municipal Bond Fund, EVM, that was a buy. Let's get away from the munis and get over to high yield. Rich in Orchard Beach, Maryland wants to know about the PGIM Short Duration High-Yield Fund, that's ISD.

JONATHAN BROWNE: Yeah, so on that one I'm also going to put a buy. We know that credit spreads are extremely tight, but with ISD you're trading at a 5% discount, which compared to some of the other high-yield closed-end fund peers is one of the widest discounts. Great management performance over the last three to five years, and given the current environment you have to appreciate the short duration nature that this fund provides so I'm going to put a buy recommendation on ISD.

CHUCK JAFFE: Yup, that's a buy on PGIM Short Duration High Yield, ISD. And last for Andrew in San Jose again, and Rick in York, Pennsylvania, Nuveen Real Estate Income, JRS.

JONATHAN BROWNE: JRS is also going to be a buy by my ratings. Real estate obviously had gotten hit pretty hard with the unknown of how Covid was going to impact the sector, but with JRS you're currently trading at a 6% discount which is over 20% below its 10-year high of a 15% premium. Not saying it's going to get back up there, but I think it does have the ability for significant discount compression. It has solid short and long-term performance, and real estate may perform well in an inflationary environment compared to many fixed-income sectors, so JRS is a buy.

CHUCK JAFFE: So we finish on a solid note, three buys in a row. Yep, this case the third buy was Nuveen Real Estate Income, JRS. And now we've got one more goodbye to talk about, it's the one where we say our goodbye to Jonathan Browne. But Jonathan, this was great, don't be a stranger, come back and do this with us again sometime.

JONATHAN BROWNE: Yeah, thanks for having me. Anytime.

CHUCK JAFFE: Jonathan Browne is portfolio manager and director of research at Robinson Capital, learn more at RobinsonFunds.com.

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To request a particular topic for The NAVigator podcast please send an email to: TheNAVigator@AICalliance.org

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