Pre-Market SPACs Offer Unique Opportunity, Given Current Conditions

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Chuck Jaffe, in this bonus episode of The NAVigator podcast interviewed Jonathan Browne, director of research at Robinson Capital and portfolio manager of the Robinson Funds. Read the Q & A below as Jonathan talks about how balancing closed-end fund investments with pre-market SPACs [special-purpose acquisition companies] creates opportunities for higher yields with diversification that helps to balance out risks.

Jonathan Browne

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

CHUCK JAFFE: Jonathan Browne, director of research at Robinson Capital is here, and we're talking SPACs and closed-end funds now on the Money Life Market Call. Welcome to the Market Call, the part of the show where we talk with experienced money managers about how they do their job, what they look for that determines their buys and sells, what they see happening broadly on the market, and how they put it all together. And my guest is Jonathan Browne, he's portfolio manager and director of research at Robinson Capital. And he's been on the show before and we were always talking about closed-end funds because, well, as he's defined it, their clients are looking to generate maximum yields while incurring minimum levels of risk, and they point towards closed-end funds. But he specifically also wanted to make sure that we were going to talk about SPACs today, specialty-purpose acquisition corporations, which are an interesting investment phenomenon that, oh by the way, some of you are interested in. And I know that because I told you to send in your requests, and you did. But if you want to get more information on what Jonathan does go to RobinsonFunds.com. Jonathan Browne, it's great to have you back on Money Life.

JONATHAN BROWNE: Yeah, thank you Chuck. It's great to be back.

CHUCK JAFFE: The Gainbridge hotline connects Money Life to all guests. Gainbridge believes investment products offering consistent guaranteed returns are the bedrock of a well-funded retirement. Through its platform, Gainbridge offers annuity products that could mesh well with your retirement plan, all purchased and managed by you via Gainbridge's online portal. Visit Gainbridge.life to get started. Jonathan, we always talk about methodology first. Now today we're going to talk about SPACs and closed-end funds. We need to know what goes into your picks, but I also need the audience to pick up on why SPACs are something that you have in your trick bag right alongside closed-end funds.

JONATHAN BROWNE: Yeah, so we look at SPACs, and specifically we look at those pre-merger SPACs or those that have yet to find a merger target. We really love the SPAC space and think that if offers one of the most compelling risk-reward profiles out there of any investment at present. The reason we think that is, is ultimately a SPAC, until it finds a merger target and merges with the security, is essentially just a T-Bill portfolio. So right now we're able to purchase these SPACs at roughly a 3% discount to the trust value that we know we're able to get. Whether a deal is announced or not, we can redeem our shares for that trust value. So similar to closed-end funds, we see an inefficiency in the space or an arbitrage opportunity to take advantage of those discounts.

CHUCK JAFFE: I should point out that you've got the Robinson Alternative Yield Pre-Merger SPAC ETF, ticker symbol SPAX. And is it all pre-merger? The day that they've got that target are you out? How does that transition work for you?

JONATHAN BROWNE: So we're only investing in pre-merger SPACs, and the reason for that is the absolute downside that they afford. So again, a SPAC is really just a pool of capital that's raised, that's ultimately used by the sponsor team or the management team to find a private company to bring public. One of the unique features of SPACs is that the shareholder always has the right to redeem their shares for trust value, which typically is known to be around

$10 a share. So if we're able to buy those for $9.70 or a 3% discount, we know that at the end of the day, whether that management team finds a private company to bring public or not, that we can redeem for that $10 a share or a 3% positive return. And so we love the ability to protect all of our downside by having this redemption feature, but what also is important to understand about SPACs is you really have equity-like optionality. For any SPAC that finds a merger target that the market likes, you can see a significant share price appreciation. And so having that sort of absolute downside protection with the equity-like upside is why we really think that it's one of the most compelling risk-reward profiles out there today.

CHUCK JAFFE: How does that fit in separately with closed-end funds? Because among the other things you do, the Robinson Opportunistic Income Fund is using closed-end funds to generate its income. And so you're used to seeing things trade at a discount, but of course the closed-end space is different, so what exactly are you looking for in the closed-end space?

JONATHAN BROWNE: So in the closed-end fund space we're able to purchase a handful of names, whether it's high-yield, bank loans, etcetera, for around 10% discount. So we've seen discounts in closed-end funds since the beginning of the year really widen out, which isn't surprising given what we've seen in the equity and fixed-income markets year to date. And so we think that closed-end funds are a compelling opportunity right now to invest just given their wide discounts. We use the combination of closed-end funds and SPACs because we're able to get an above average income from the closed-end fund portion. But as I stated prior, with the pre-merger SPAC portion, you're essentially getting the credit and interest rate risk of a T-Bill portfolio with that equity-like upside. And so we think the marriage of the two provides a better mousetrap for a core bond position.

CHUCK JAFFE: And I should point out you use both SPACs and closed-end funds. I said closed-end funds when I was describing Robinson Opportunistic Income, but you use both SPACs and closed-end funds there.

JONATHAN BROWNE: We do.

CHUCK JAFFE: In terms of what that has led you to, give us an example. To me, the example, especially on the SPAC side, is particularly curious because everybody here's about pre-merger deals, hopes to get pre-merger deals, etcetera. Often for very different reasons than what you're talking about, like, hey, the whole SPAC boom was not predicated on the stuff you're talking about. It was, hey, they're going to cut this deal, and look what you're going to get and how it's going to work. But what's an example of a SPAC, a pre-merger SPAC that looks good to you and why?

JONATHAN BROWNE: I guess what I would just say is there's really a handful of SPACs. There's over 590 SPACs that are currently looking for a merger partner. Right now you can look down the list and find a handful that are trading at a discount of 3%+, which is extremely attractive. The second layer of what we look for on the SPAC side is then really digging into the management team and the boards. We look at their record of allocating capital, and that's really where they're able to differentiate themselves from the other 500-some SPACs that are out there. Do they have a record of issuing other SPACs and bringing private companies public, etcetera And so that's what we're going to really look at on a SPAC-by-SPAC basis to see which sponsors we like best, whether that's a Churchill with Michael Klein, whether it's a Gores-backed SPAC, etcetera.

CHUCK JAFFE: In the closed-end fund space discounts have widened but asset classes are changing. I mean, it's been very interesting talking with bond fund managers just about the opportunity set changing in bonds. So where on the closed-end fund space are you looking? What is particularly attractive there for you?

JONATHAN BROWNE: We generally still have a bit of an overweight to high yield. I guess what I would say is the first half of this year thus far, it's really been more of a duration move, we've seen interest rates rise significantly. I think the market's set to face quite a bit of headwind over the next six to 12 months, and I think one needs to start to potentially get a little more cautious on credit. And so what we've been doing is dialing down some of that credit risk, and a name that we've found very interesting for example is BRW, and that's the Saba Capital closed-end fund. And one of the things that's really interesting about that strategy is it's actually right now invested in 80% SPACs and then 20% bank loans, and so they have the ability to fluctuate that weighting based on how they see the market environment shaping up. But for us, that's one way to not only get a closed-end fund that's trading at an 8 or 9% discount, but also get access to a portfolio that's higher credit quality than just a high-yield closed-end fund.

CHUCK JAFFE: We talked about when you're getting out of SPACs, because of course you're looking at them as pre-merger and once they've got the deal you want to be done, etcetera. And then of course if they're not going to get a deal that would get you out as well potentially.

But what gets you out of a closed-end fund? Once you find a closed-end fund that you like, what makes you say it's time to go?

JONATHAN BROWNE: There's two components that we look at. One is from more of a macro standpoint, and so what's our view on the asset classes? What do we think about the high-yield space? What do we think about the bank loan space? The second component is really the discount. And so we look at discounts not only relative to its own history, but versus the rest of the closed-end funds in those same asset classes that really determine if it looks attractive to us or not. And so if we saw discounts start to narrow back to levels that are inside historical averages, we may look to exit that closed-end fund or to rotate into another closed-end fund in the same asset class that may be a little more attractive.

CHUCK JAFFE: Well, now we're going to get your quick and dirty take on some investments that my audience is particularly interested in. Well, we hope you're making your day as we have a discussion about SPACs and closed-end funds with Jonathan Browne, he's director of research at Robinson Capital, they run the Robinson funds which you can learn about at RobinsonFunds.com. Now, Quick & Dirty is our lightning round, it's where we put our guests to your test. And if you want to test our guests you need to send your name, your hometown, and the ticker symbols you're interested in to Chuck@MoneyLifeShow.com. Now of course you can send them about—SPACs are basically stocks, they come under the stock purview. But Jonathan had made it clear he wanted to do this, I sent out a note to you guys. I sort of basically said, "Hey, if you want SPACs, send us some requests." And a few of you did just that. And we're only going to talk about one of them but let's start with the SPACs today, Jonathan. We have a request from Steve in Royal Oak, Michigan who wanted to know about LCID, that's Lucid Group.

JONATHAN BROWNE: Yeah, so Lucid has come off of its highs from late last year quite a bit. What I would say is in the near term I'd be a little cautious. Any sort of speculative stock has seemingly come under pressure lately as rates have risen as the market has deteriorated. But I think longer term it's quite an interesting security. It has great backing by Michael Klein, and then has deep pockets. So near term I'd be cautious, longer term I think it's more of a speculative buy.

CHUCK JAFFE: So yeah, that's a cautious buy, the speculative buy side of things. Yeah, so whether you're going to be cautious or you're going to be speculative, well, you're hoping to become a richer man on Lucid Group, LCID, but be careful there. Now let's move over to closed-end funds. We'll start with a request we got from Barry in Tucson, Arizona. And Barry, it's been a long time since I've heard from you, so let me know if you're still out there listening to us. He wants to know about CIF, that's the MFS Intermediate High Income Fund.

JONATHAN BROWNE: Yeah, I would be selling that right now. Looking at that it's trading at a 7.5% premium which is well above its three, five, 10-year average discount. There's a handful of other high-yield names in the space that I would focus on as a better value proposition or wide discounts at present.

CHUCK JAFFE: Anything that particularly springs to mind?

JONATHAN BROWNE: Yeah, I think you could look at ticker DHY, or if you wanted another high-yield fund that has a shorter duration profile, SDHY.

CHUCK JAFFE: So it's a sell on CIF, the MFS Intermediate High Income Fund. But the tickers you were being pointed to if you want to buy in that space instead would be DHY and SDHY. We'll stay in high income. Dale in London, Ohio wants to know about Western Asset High Income, HIO.

JONATHAN BROWNE: Yeah, that one to me is a buy. It's actually one of my favorite high-yield names right now trading at over a 10% discount. It's an unlevered way to get access to the high-yield space in closed-end funds. So if you're worried about credit risk, this is a little safer way to play it compared to some of the other levered high-yield closed-end funds.

CHUCK JAFFE: That's a buy on HIO, Western Asset High Income Opportunity. Dale had another request, this taking us to the utility space. He wanted to know about Gabelli Utility & Income, which is ticker symbol GLU.

JONATHAN BROWNE: Yeah, at present I have a buy on GLU. It's trading at roughly a 10% discount which is significantly wider than its one, three, five, and 10-year average. So from a discount perspective I think that you're getting a great entry point on this name. And also kind of going back to the markets, if you're concerned about the credit environment, which way markets are going to go, utility fund, that should be much more defensive in nature. So probably a good way to remain a little more defensive.

CHUCK JAFFE: So Gabelli Utility & Income. Yeah, well, all the power that comes not necessarily just from utilities but from that big discount and more, that was a buy on GLU.

And we finish with a request from Javier in Wilmington, North Carolina who wants to know about Principal Real Estate Income, that's PGZ.

JONATHAN BROWNE: Yeah, I have a buy on PGZ as well. You're looking at 11% discount, a nice, healthy 9% yield, and you get access to real estate which can help protect your portfolio from inflation. So I have a buy on PGZ.

CHUCK JAFFE: So we finish on a high note. That is a buy on PGZ, Principal Real Estate Income. Well, we thought about a lot of things beyond just buys. Jonathan, this was great, it's always good to talk with you. Thanks so much for coming on the show.

JONATHAN BROWNE: Yeah, thank you for having me.

CHUCK JAFFE: That's Jonathan Browne, he's portfolio manager and director of research at Robinson Capital. We talked about the Robinson Alternative Yield Pre-Merger SPAC ETF, that's SPAX, and the Robinson Opportunistic Income Fund. You can learn more at RobinsonFunds.com.

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