The NAVigator At Morningstar: Mario Gabelli On His Long Closed-End Fund Career

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Host Chuck Jaffe attended this week's Morningstar Investment Conference in Chicago and took the podcast with him, catching up with 'Super Mario' – investment legend Mario Gabelli, founder of the Gabelli Funds, a long-tenured fan of closed-end funds. Read the Q&A below as Mario and Chuck discuss the pros and cons of the closed-end structure, especially as it relates to the Gabelli Equity Trust and the 10 percent payout he has made a cornerstone of the fund's investment policy.

Mario Gabelli

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

CHUCK JAFFE: Welcome to The NAVigator at Morningstar; so The NAVigator is of course the closed-end fund, business-development company, interval fund conversation that we have each week, but this week with Money Life, my show being on the road at the Morningstar Investment Conference, The NAVigator's on the road too. And we are talking right now with Mario Gabelli, he is the founder of the Gabelli Funds and Gabelli Investment Management, if you want to learn more it's Gabelli.com. And of course generally to learn more about investing in closed-end funds, business-development companies, and interval funds go to AICAlliance.org, the website for the Active Investment Company Alliance which brings you The NAVigator. Mario Gabelli, it's great to chat with you again.

MARIO GABELLI: My privilege, Chuck, to talk about our favorite subject, investing and investing in equities.

CHUCK JAFFE: Well, and specifically I want to talk about closed-end funds, because one of the funny things about hosting The NAVigator is that now I hear from people all the time going, "Oh, I love closed-end funds!" That is not a sentiment that I had ever heard, like going back to the 1980s when I was an early investor, when I started covering mutual funds at *The Boston Globe* and all the other things I did, nobody was sitting and saying, "Let's do more with closed-end funds." And yet, there was Mario Gabelli, and over the years not only did you have your closed-end funds, you were buying up some really interesting other ones from money managers who were retiring and the rest. Why has the closed-end fund structure always appealed to you?

MARIO GABELLI: Well, they actually didn't, Chuck, until about the early 1980s when we started an open-end fund, but we knew that in certain economic times and stock market times people would withdraw money at a time in which they should be investing. Chuck Allmon started a fund and we examined it, it was the first time a closed-end fund had been started since the 1920s. So what we did is we took their prospectus, understood it, individuals that I knew from my days working at my first firm of Loeb, Rhoades came to me and said, "We'll underwrite it." They were now part of Shearson Lehman, and so they started a closed-end fund called the Gabelli Equity Trust, and the benefit of it was that in a down market, if you have the liquidity, you can invest. And so from an investor's point of view, that is very, very beneficial. The first year or two that we were in business however, you had October of 1987; 1987 resulted in the stocks of closed-end funds, all of ours, selling below net asset value. So the ideal world is to take the funds, invest and earn a return, and over time the publicly traded stock cracked the NAV, net asset value. And what we did was we followed a guy in LA who said, "We're going to put a 10% return on the investment, and that will hopefully match at the time a little more than inflation what we can earn, that'll be less than what we can earn," and we adopted that policy. And so our Gabelli Equity Trust, which is the first fund we started, has a 10% payout which we've been religious on for about 35 years. And so as a result of that, our price on an exchange tracks, plus or minus 5% over the last X number of years, the underlying net asset value. That fund over time, as the world changed, for example in the early eighties, while I went to China in 1981, while I went to

Japan in 1971, I would not invest globally. When the Berlin Wall came down, and Tiananmen Square, we said, "We're going global," so we started to spin off segments of that fund. So we started a convertible fund, several others, so over time that spawned segments of different funds to pick up different styles. Again, at times we will buy back the funds, the boards will add to the cash out, sometimes they'll reduce the cash out. Each of these funds have different directors, so unlike Fidelity or T. Rowe Price that might have 12 directors for all of their funds, we have 32 directors for all of our funds.

CHUCK JAFFE: Well, and in terms of putting it together for closed-end funds, it was not a part of the business that attracted folks, and here you were doing really well with your traditional open-end funds. Why did you stick with the business at a time when the business was still--

MARIO GABELLI: No, no, we have more money in our open-end funds than the closed-end funds. Again, the advantage of a closed-end fund world is that it allows investors, the investor, that's me, to make returns, the manager, in volatile markets. For example, today I can buy a stock called XYZ, knowing full well that it may go down 10%, but I want to buy more because I can then go long term and the flowthrough on a K-1, on a 1099 is a long-term gain for the owner. Unlike ETFs, which have a major advantage of taxes, deferring taxes and evading taxes by what they do on a short-term basis, and we can do that in our closed-end funds but there are too many rules to overcome. So there are disadvantages of being a long-only or even a hedged closed-end fund, or even an open-end fund, but Chuck, the big advantage is that in periods of stress in the marketplace you know the money is there and you can invest it.

CHUCK JAFFE: How stressful is this marketplace? Is this a time when closed-end funds should be doing great, or because of what we see with discounts and how they get hammered every time the market picks up?

MARIO GABELLI: All of the above. Independent of that, we like stress. Because good businesses run by good managements will sell at a lower valuation, so your holdings will go down. But your opportunity to have one or two of them taken over, which we are fortunate enough to have a lot of those, like Aerojet being taken over, Public Service of New Mexico being taken over, we take that cash and buy good businesses at a bigger discount which helps our returns longer term. That's the advantage of closed-end funds. The disadvantage, Chuck, is that we do pay out 10% a year at Gabelli Equity Trust, that is $200 million of cash going out, so during certain periods of time I have to build up cash to pay it out. So we hold above average cash, and like right now we're paying out a dividend, just distributed at the end of March, a cash balance. But we do that, we have a team that's been in place for 35 years, we have investor relations people that know closed-end funds and they talk to the clients and the shareholders, and we do our best at it.

CHUCK JAFFE: And the other side of that is that because again it's been consistent for 30 plus years, is there any event that would knock you off the 10%?

MARIO GABELLI: Yeah. No, no, the 10% would remain unchanged but the dollar amount may go down, in part because of the following; if you have a 40% decline in the market for two years in a row, a 30% decline two years in a row, the board will get very concerned about the liquidation of the fund. They would probably keep the 10% payout ratio, which they've done in the past when we've had crises like this, like '01-'02, like '08, '09 or '10 when you had the Lehman crisis and the Bear Stearns crisis, that's the stress factor that I don't anticipate, I think that downturns will be sharper and last not as long.

CHUCK JAFFE: That's a pretty good outlook. I think most people would be pretty happy if they wind up having an investment that can do that, right?

MARIO GABELLI: Well, let's do it another way. We have long-only separately managed accounts, un-levered for the last 45 years we've generated 14.1% net of fees. And we believe over the next 20 years we should be able to do, with the world that we see, very little, we'll make some money in the next two or three years, but over the next 10 years we should be back up to 10-11%. And we're going to miss markets like 2001, where you went and bought companies that were highly levered, cash burn, but new ideas and new innovations. We ignored those, and so last year we were down 9% when everybody else was down 30%. So we lose less and make less, but we'll do extremely well over a long period of time on a compounded basis.

CHUCK JAFFE: Mario, always a pleasure to see you, thanks so much for taking the time.

MARIO GABELLI: Chuck, my privilege to be with you. You ask great questions and I appreciate your insights into the world that we're a part of.

CHUCK JAFFE: The NAVigator is a joint production of the Active Investment Company Alliance and Money Life with Chuck Jaffe. And yes, that's me, and you can learn all about my show, including the three days of wall-to-wall interviews we're doing for Money Life at

Morningstar, including more from Mario Gabelli from the Morningstar Investment Conference, by going to MoneyLifeShow.com or by searching on your favorite podcast app. To learn more about investing in closed-end funds, business-development companies, and interval funds check out AICAlliance.org, the website for the Active Investment Company Alliance. They're on Facebook and LinkedIn @AICAlliance. And thanks to my guest Mario Gabelli, "Super Mario", the founder and chairman of the Gabelli Funds, learn more at Gabelli.com. The NAVigator is here for you every Friday, ensure you don't miss anything by following along on your favorite podcast app. We'll be here next week, I hope you will be too. And until then, happy investing everybody.

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