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NAVigator Bonus: RVP's Fertig On What's Attractive As Rate-Cut Cycle Starts

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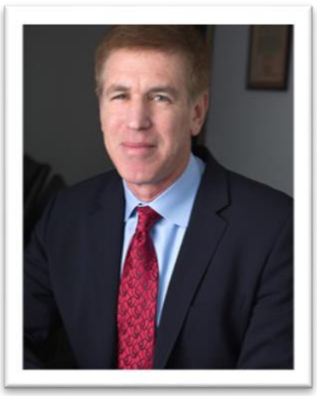

Chuck Jaffe, in this episode of The NAVigator podcast interviewed Maury Fertig, Chief Investment Officer at Relative Value Partners. Read the Q&A below as Maury discusses how the changing interest rate picture is impacting considerations on the closed-end funds he is considering for client portfolios, and which areas of the closed-end fund universe look particularly attractive now. He also talks about how a number of BlackRock funds are performing in the wake of a recent tender offer.

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 from the Active Investment Company Alliance. Every weekday I also host an hour-long interview program called Money Life with Chuck Jaffe, and our show on August the 23rd featured Maury Fertig, co-founder and chief investment officer at Relative Value Partners in Chicago. Because the conversation is all about the way Maury invests in closed-end funds, we wanted to make sure you got a chance to listen in, so here it is as a bonus episode of The NAVigator. Enjoy! Welcome to the Money Life 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 returning to The Market Call today, Maury Fertig, he is co-founder and chief investment officer at Relative Value Partners. If you want to learn more about the firm and what they do, it is RVP for Relative Value Partners, RVPLLC.com. Relative Value Partners and Maury, big investors in closed-end funds, so that's where we're going today. Maury Fertig, it's great to have you back on Money Life.

MAURY FERTIG: Great to be here.

CHUCK JAFFE: We always start with methodology, and it's particularly important I think with closed-end funds, because with closed-end funds you get guys who are simply discount capture investors, you get guys who are much more driven by income and a variety of other things, so help us understand what it is that you are looking for that's going to make closed-end funds a buy to you and other ones not so much.

MAURY FERTIG: Yeah, I think that for us, and I think for any investor, the first thing is does the closed-end fund have exposure to an asset class you want to be in? That's where it all starts, so if we're looking for a high-yield fund or a municipal bond fund or a country-specific equity fund or emerging markets, then we have a place to start to look and is there a closed-end fund that meets those investment objectives? But that's the first thing I think any investor needs to understand, it's not just about buying fund XYZ at a big discount and hope and pray that everything works out, the underlying assets in the fund are ultimately going to be the biggest determinant of how you do in that investment, so that's step one. I think for most funds you want to look at does this manager, are they a good manager of either equities or fixed income, do they have good long-term performance, how have they done against their peer group, how have they done against the indices, are they a competent manager? You don't necessarily have to pick the best manager, but are they going to capture, if you're buying a fund that's investing in bank loan fund for instance, has it performed in line with the other bank loan funds, has it performed in line with the underlying ETF, and making sure that you're getting a good manager that is going to fulfill those objectives. I think the other thing you need to look at is what the fees are on the fund, sometimes the fees can be very exorbitant, you can see some fund fees excluding interest expense can approach 2%, so you want to make sure the fund fee is in line with the discount. Sometimes we'll take a fund that has a higher fee if the discount is substantially greater, but that's one of the other things that I think will ultimately drive long-term returns. A couple other things to look at is the historical relationship of the discount, is the discount in line with its long-term average, is it a fund that's been around for 20 years and it usually trades at a 10% discount and now it's at a 15%? That's one reason, that might be one thing to look at. Or is it now trading at a 5% discount and it's richer than its historical average, so whatever you gain from the investment you might lose that in discount if it reverts to its mean. And then finally one other thing to look at, and I don't know that the individual investor has to be so focused on this, particularly if they get the first four things correct, but is there a catalyst for the discount to close? If it's trading at a depressed price, I'll give you a great example of this, as you get into the late fall and around year-end, particularly in a down bond market or down equity market, there'll be a lot of tax-loss harvesting and you'll see a lot of funds trade at substantially wider discounts than their averages. So the catalyst there would just be getting over year-end, tax-loss selling stops, and investors start to find value in these funds, so that's a nice thing we like to look at. Sometimes that can mean shareholder-friendly provisions in the underlying fund which allows for shareholders to potentially vote to liquidate the fund or allow for tenders, things like that which can enhance value over time.

CHUCK JAFFE: But it's interesting in there, because as much as people want discounts to close, when you gave an example of just random numbers, you're like, "Hey, if a fund's got a 20-year history and it's normally trading at a 10% discount, if it's now at 15% we're looking to see if it might close," et cetera. So there are clearly funds out there, and there are more than a few closed-end funds that have very long track records, where you're much more thinking that whatever the discount is, the discount's normal, and let's really function around normal rather than functioning around I'm buying this thinking an activist is coming in or whatever and I'll get all the way back to NAV?

MAURY FERTIG: Yeah, so one of the big reasons for that, particularly if you look at some of the older funds like Adams Express, ADX for instance, these funds have been around a long time, they have a massive amount of embedded capital gains in them, even if that were to happen, somebody's going to get hit with those big tax bills. There are some funds that do have reasons why they should trade at a discount, and embedded tax gains is one of them.

CHUCK JAFFE: In terms of what we've seen with the closed-end fund industry, it's been a very hot space. There have been a lot of new funds issued, there's a lot of examples of not new funds, also BDCs being added to the mix and the rest. For you, once you get past the brand new phase, where sometimes there's some leverage that may be a concern or what have you, how much does new matter to you? Is it a benefit, you're looking at more investment products and that's always good? Or is new, I'm waiting till they're seasoned?

MAURY FERTIG: Waiting till they're seasoned. New closed-end funds are an opportunity for the future at some point. You had a lot of new funds come, and particularly it's been pretty quiet the last year because of the higher rates, leverage is more expensive, and the bond market had up till recently performed quite poorly, so it's been pretty quiet. But there were a lot of funds issued in 2021 for instance, and those got rocked pretty hard when the Fed started raising rates in '22, and that created some nice opportunities to get involved in those new funds. So we do like to see some new supply because ultimately there'll be some kind of crack-up whether it's an equity market selloff, a crash, a hiccup in the bond market, something will trigger a little bit of panic. And if none of that triggers it, ultimately there'll be some tax-loss selling at some point and that may be a nice opportunity to enter these funds.

CHUCK JAFFE: And for you, given what you do and how you run portfolios for investors, does the interval structure, do you like it, hate it, you use it, you're worried about it? How do you factor in interval funds where liquidity may or may not be an issue?

MAURY FERTIG: Well, we don't use 'em generally speaking. We just decided as a rule we're not, we're concerned about that, we're concerned about too many people heading for the exit at the wrong time, so we've stayed away from them.

CHUCK JAFFE: Well, let's talk about what you head into. What's an example or two of a closed-end fund that stands out to you right now?

MAURY FERTIG: Well, right now things are pretty fairly valued for the most part. The Fed stopped raising rates over a year ago, it was a rough period for closed-end funds 2022, first half of '23, now we're looking at a Fed cut in September, and that I think will bode well for closed-end funds and I think a lot of funds are setting up for that. There's a few thing in the fixed-income area we like, one is in the high-yield space, which we're a little concerned about economic downturn so I want to be cautious, we're not really bullish on high yield, but there's these term trusts which basically are self-liquidating on a date certain. So there's one ticker, SDHY, it's the PGIM Short Duration High Yield Fund, it will liquidate in 2029, it owns five-year and under high-yield, a majority of which are BB or higher, so it's a reasonably good credit quality for a high-yield fund, yields about 10%, and is trading at about a 10% discount, so we're going to capture that discount over the next five years provided the underlying assets perform well. So we like something like that with a little bit of certainty to it in terms of how we're going to exit the fund.

CHUCK JAFFE: What's something else that stands out to you right now?

MAURY FERTIG: Sure. In the equity world there's a fund, BDJ, it's the BlackRock Enhanced Dividend Achievers Fund, so it owns dividend equities and overlays with a covered-call strategy, and it's yielding about, I think it's yielding about 8%, but it has a 10-11% discount right now. Well, there is an active tender going on in that fund, so we think that's pretty cool as well. It's a nice benefit.

CHUCK JAFFE: And in fact, I want to talk to you about that active tender.

MAURY FERTIG: Yeah.

CHUCK JAFFE: I just want to point out, and I will have you confirm this, you and I did not talk in advance about the fact that BDJ was going to be a fund you mentioned, did we?

MAURY FERTIG: No. No, not at all.

CHUCK JAFFE: Well, it happens to be a closed-end fund that I own, and on our August 22nd show, so we're recording this on the 22nd, shortly after that show went out--

MAURY FERTIG: Yeah.

CHUCK JAFFE: I answered a listener's question which was about that tender offer because I also was facing that tender offer. Their question was more directly about, do you accept the tender offer whenever one is out there? And my response was, "Yes." But in this case, it was a tender offer where it was oversubscribed, so although I tendered my shares, only 20% of them will have the nice little bump up to 98% of NAV. So I am curious, because I want to ask you the question that basically my audience member asked, which is if you own a fund and there's suddenly a tender offer, will you always accept it even if it's only a partial sale of your shares?

MAURY FERTIG: Absolutely, because if you recall that particularly BDJ tender, they're only tendering for 2.5% of the outstanding stock, and you're getting filled on 20%. That's a pretty big win, and with the prospect of more tenders to come if the discount remains in place. So unless the fund's trading at a premium, or NAV for some reason, there may not be a reason to tender, but at a discount, the only reason, the only possible reason I wouldn't tender is if you're in a taxable situation where you would prefer to keep the security rather than sell it. That would be the only situation.

CHUCK JAFFE: Okay, so let's then add a follow-up question. Again because I assumed that my listener was getting something from one of the BlackRock, because BDJ was not the only one, that's what I assumed was motivating their question.

MAURY FERTIG: Yeah.

CHUCK JAFFE: But again, as somebody who's there in this one myself, so now here you are talking about BDJ as a buy. The tender offer is being completed, et cetera, it's now going to be back on sale at its standard price which is about a 10% discount or close to it, et cetera. So here it is, as much as you like the tender offer, you would be buying more of it? That's why you mentioned it?

MAURY FERTIG: I would buy it at this level because should the discount persist there will be other tender offers, and they will be lightly subscribed as this one was, the fact you're getting a 20% fill on a 2.5% tender. So that's a prospect in the future that either we'll see the discount compress or we'll see more of your shares will be able to liquid at 98% of NAV.

CHUCK JAFFE: Well, again, I tell my audience all the time, we don't plan this out necessarily, sometimes it just works out that way, but glad that we got extra opinion on that particular issue. And now we're going to get your quick and dirty take on some closed-end funds that my audience is particularly interested in. "Always account for variable change." Well, you've just heard that as the variables change, my guest Maury Fertig is accounting for them. He is co-founder and chief investment officer at Relative Value Partners, it is RVPLLC.com if you are looking for more information. And of course, Quick and Dirty is our lightning round, if you want to get involved, send your name, your hometown, and the ticker symbols you're interested in, closed-end funds, ETFs, traditional funds, and of course stocks to Chuck@MoneyLifeShow.com. We're going to start with a request from Danny in Falls Church, Virginia, who I think has only ever written us about closed-end funds. You were talking about liking certainty to some extent, well, he's interested in ETX, that's the Eaton Vance Municipal Income 2028 Term Trust.

MAURY FERTIG: Yeah, so as I mentioned earlier, I do like term trusts, but this term trust is trading very close to NAV, around a 1% discount, it has a reasonably high fee and you still have bond risk associated with it. I would be a seller of this fund at this very tiny discount given that, and I'd look to something like, if I want to get municipal exposure I'd look to something like the Nuveen Municipal Value Fund, the ticker's NUV, trading at a 6% discount, has a very low fee, very liquid fund that historically has traded at a 2%, and it's one of my favorite municipal funds from a risk-reward standpoint.

CHUCK JAFFE: So ETX, the Eaton Vance Municipal Income 2028 Term Trust, "Whoa, dumber than advertised." But in there instead in that space you could go with NUV, the Nuveen Fund, "Come on, let's buy." Rick, in York, Pennsylvania wants to know about Tortoise Power and Energy Infrastructure, TPZ.

MAURY FERTIG: Well, I want to hand it to him for owning this because this has been a very great success story in the closed-end fund arena. TPZ this next quarter, most likely in November, will be converting into an ETF, and that means that the fund can be liquidated at or very near NAV at the time and they're merging it with several other funds. This fund had been trading at a double-digit discount up until a few weeks ago. It's still at a discount, I would own it, keep it until the conversion into an ETF happens and look to sell it at that time if I'm looking to get down on my energy exposure.

CHUCK JAFFE: And if you could buy it right now knowing that that's coming, grab a couple extra points?

MAURY FERTIG: You know, yes, if you specifically want MLP and energy exposure at this point in time there's another 3% to pick up, but short of that I would not play for 3%. It's a volatile asset class and there's leverage in the fund as well.

CHUCK JAFFE: So the fund itself, Tortoise Power and Energy Infrastructure, TPZ, "Winner, winner, chicken dinner!" Yes, you've been a winner in it, as for whether or not you'd buy it now, that's a cautious buy there based on that very specific limited upside.

MAURY FERTIG: Yes.

CHUCK JAFFE: Our next request comes from Morris in Bradenton, Florida, he wants to know about BGT, the BlackRock Floating Rate Income Trust.

MAURY FERTIG: Well, BGT has performed very well. This whole space, the loan fund area has been a great performer the last couple years, and now this fund's trading at a slight premium. Historically this has traded at around a 7% discount and we used to own in meaningful size earlier in this economic cycle, but I would be a seller here given where we are in terms of rates and given the fact that if we do have an economic slowdown in Q4 next year, the discount will widen and the underlying NAV [inaudible 0:16:34].

CHUCK JAFFE: "I say we sell now." That's a sell on BGT, the BlackRock Floating Rate Income Trust. We'll stay with income funds, Dale in London, Ohio and David in Escondido, California both wanted to know about DSL, that's DoubleLine Income Solutions.

MAURY FERTIG: Yeah, so this is a bond fund that about half of it's high-yield, it's managed by Jeff Gundlach who has a great reputation. I will say that it's trading at a premium right now, has a pretty high management fee of over, I believe it's about 1.25%, which is a lot for a bond fund. Last fall when we had little hiccups in the equity market this fund traded at a 5% discount, so I would say if you like Jeff Gundlach and you want to own him, there's other mutual funds that are available that may have lower fees and no chance of a discount happening, but I'd be a seller of DSL at these prices.

CHUCK JAFFE: "And now for the profit taking." Yeah, it got to a premium, so if you bought it at some point when it was at a discount, you are definitely taking profits on DSL, DoubleLine Income Solutions. And last for Steve in Royal Oak, Michigan, it's EMF, Templeton Emerging Markets.

MAURY FERTIG: Well, for somebody that likes, wants emerging markets exposure, I think this is a great fund. It's trading at a 14% discount, but more importantly the managers had good long-term performance versus its peer group in the EM space, so I'd be a buyer of EMF at this point.

CHUCK JAFFE: We finish on a high note, that is a buy on Templeton Emerging Markets, ticker symbol EMF. "Sounds like the opportunity of a lifetime." Well, whether it's the opportunity of a lifetime or not, one of the things we love is the opportunity to talk closed-end funds with Maury Fertig. Maury, the time flies when we do this, I hope we'll get a chance to do it again in the not too distant future.

MAURY FERTIG: Absolutely.

CHUCK JAFFE: Maury Fertig is co-founder and chief investment officer at Relative Value Partners, it is RVPLLC.com if you want to learn more about the firm and Maury and what they do.

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