Interval Funds

Providing investors exposure to private assets

The trade-off between risk and reward is an age-old conundrum for investors, the outcome of which often depends on how long an investor is willing and able to commit their money. That's because many private investments require a long-term commitment, sometimes tying up an investor's capital for multiple years. For many investors that can prove (and has proved) an insurmountable stumbling block in their search for alpha. An interval fund may provide investors with enhanced risk-adjusted returns with exposure to less liquid investments, without completely giving up access to their money.

An Interval Fund explained

An interval fund is a type of closed-end fund that can provide investors with exposure to less liquid investment opportunities, while repurchasing a percentage of investor shares at regular intervals (typically quarterly). As a result, the fund can give investors access to alternative sources of return and/or income … enhancing their portfolio's risk-adjusted return potential … while still giving them periodic access to a portion of their capital (should they need it).

Interval Funds are not a completely new concept. They originally emerged in the 1990s, but have attracted growing interest in recent years, with assets increasing by over 40% to $27.5 billion in 2018 alone.[1] As investors continue to search for new and uncorrelated sources of alpha, including a growing array of alternative assets, the growth of interest in interval funds is not surprising, and likely to continue, especially in light of increased market volatility.

What are the benefits?

While classified as a closed-end fund, interval funds offer investors a number of the benefits of open-end funds—including a continuous share offering and potential for liquidity. (Liquidity is not offered daily, but at prescribed intervals, and limited by the percentage of shares that the fund has agreed to redeem in a given repurchase offer.) However, what really sets an interval fund apart from a traditional open-end fund is its ability to invest more than 15% of its assets in private assets. Broader exposure to private assets can generate important benefits for both the investors in and managers of an interval fund:

› **The investor:** Interval funds can provide individual investors with exposure to a diversified portfolio of publicly listed securities and private, non-listed investments — a strategy that has been successfully deployed by institutional investors for many years. This more diverse portfolio can enhance return potential, but it can also help:

- Reduce portfolio volatility
- Potentially increase income
- Lower the portfolio's correlation to public markets
- Mitigation against unexpected inflation (depending on interval fund primary investment strategy and objective)
- Potential of lower minimum investments than private funds (which can typically be $10 million or more)
- Regulated and transparent reporting requirements typically experienced by investors in professionally - managed registered funds

[1] Source: Interval Fund Tracker

The manager: An interval fund does not offer daily redemption of its shares. This gives the portfolio manager greater flexibility (when compared to an open-end fund manager) to invest in private, non-listed assets — such as commercial real estate debt and equity, infrastructure, timber, agriculture, natural resources, private equity, or structured credit — which generally lend themselves to a longer-term investment horizon. Not having to provide daily redemptions and liquidity can alleviate managers from being forced sellers at potentially distressed prices shielding investors from the daily fluctuations of public markets.

How interval funds compare with other fund structures?

While interval funds are similar in many ways to traditional mutual funds and traditional (exchange listed) closed-end funds, there are a few key differences to note, some of which were previously highlighted.

- Interval fund shares are offered continuously, unlike listed closed-end funds (where a fixed number of shares is offered by IPO with shares typically traded at a premium or discount to NAV).
- Interval fund shares are not listed on any secondary market. Instead the fund offers to repurchase a certain amount of its outstanding shares (minimum 5%, maximum 25%), at NAV, at periodic intervals (typically three, six or twelve month intervals).
- If shareholders apply to redeem more shares than the amount offered for redemption by the fund, then the fund must repurchase shares on a pro-rata basis.
- Interval funds tend to invest in income-producing assets and offer investors periodic distributions from the fund, which may be a combination of income, capital gains, and/or return of capital.

At a glance: **Interval funds versus other major fund types**

	Open-end mutual fund	Close-end fund (listed)	ETF	Interval fund
Maximum investment in private assets	15%	No limit	15%	No limit[2]
’40 Act registered product	Yes	Yes	Yes	Yes
Shares offered	Continuously	One time via an IPO	Continuously	Continuously
Exchange traded	No	Yes	Yes	No
Share redemptions	Daily redemptions	Exchange traded	Daily redemptions for authorized participants. Exchange traded of other shareholders.	Periodic redemptions[3]
Share pricing, frequency	NAV, daily	Market pricing, daily	Market pricing, daily	NAV, daily
Taxation	Form 1099	Form 1099	Form 1099	Form 1099
Investment Risks[4]	Varies	Varies	Varies	Varies
Fees and Expenses[5]	Varies	Varies	Varies	Varies

[2] Interval funds must maintain liquid assets sufficient to meet repurchase offers during time between notice of repurchase offer to shareholders and repurchase pricing date.

[3] Redemptions are limited by the percentage of shares that the fund has agreed to redeem in a given repurchase offer (minimum 5%, maximum 25% of outstanding shares).

[4] Investment risks will vary from fund to fund depending on the investment strategy, asset classes, and underlying investments selected by the manager. See the applicable prospectus for more information.

[5] The level of fees and expenses vary from fund to fund. See the applicable prospectus for more information.

Who might invest?

While interval funds offer to periodically repurchase a portion of their shares, they still remain best suited to the investor with a longer-term investment horizon. That does not mean that interval funds are not suitable for an investor seeking regular income, as a significant number of interval fund strategies focus on delivering a high current yield. In addition, investors seeking long-term capital growth, interval funds are well positioned if the investor is unlikely to need access to their original capital for an extended period of time.

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Before investing in an interval fund, investors should carefully consider the risks associated with the offering. An investment in an interval fund is not suitable for all investors. Adding real asset components may not be appropriate for all investors. The additional risks associated with investment in these sectors should be considered prior to investment. Past performance does not guarantee future results. Asset allocation and diversification do not ensure a profit or protect against a loss.

Real estate investment options are subject to risks associated with credit, liquidity, interest rate fluctuation, adverse general and local economic conditions, and decreases in real estate values and occupancy rates. Investments in companies involved in agriculture, infrastructure, natural resources and energy can be significantly affected by government policies, regulations, interest costs, surplus capacity, weather conditions, and natural disasters. Investing in derivatives entails specific risks relating to liquidity, leverage, and credit, which may reduce returns and/or increase volatility. Fixed-income investments are subject to interest rate risk; as interest rates rise their value will decline.

Due to the inherent uncertainty and subjectivity of determining the fair value of investments that do not have a readily available market value, the fair value of private investments may differ significantly from the values that would have been used had a readily available market value existed and may differ materially from the amounts that investors may realize on any disposition of such investments.

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Investors should consider an interval fund to be illiquid, since the ability of investors to sell shares to access their invested capital is very limited. Interval funds tend to use leverage, which increases investment exposure and has the potential to magnify losses.

Investors should be aware that closed end interval funds are subject to annual expenses which may include management fees, distribution and/or service (12b-1) fees, interest payments on borrowed funds, acquired funds fees, and other expenses. In addition, a sales load may be charged in some cases, depending on the share class selected. See the applicable prospectus for additional information regarding fees and expenses.

Alpha - The difference between an investment's actual returns and its expected performance, given its level of risk.

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