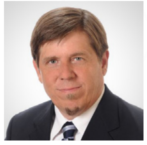
Lipper's December Closed-End Fund Market Review

Tom Roseen, Head of Research Services with Refinitiv Lipper and author of the Fund Market Insight Report which provides in depth monthly commentary on the closed-end fund market and the Closed-End Fund Association discuss Tom's insights on December's closed-end fund market action. The podcast audio can be heard here.



Tom Roseen

CEFA: **Welcome to CEF Insights, your source for closed-end fund information and education, brought to you by the Closed-End Fund Association. My name is Diane Merritt.**

Before we start our discussion, I would like to note the Closed-End Fund Association is holding an educational conference for registered investment advisors on March 10th in Fort Lauderdale, Florida. For more information and registration, please go to www.cefadvisorsummit.com.

Today we are joined again by Tom Roseen, Head of Research Services with Refinitiv Lipper, and author of The Fund Market Insight Report, which provides in depth monthly commentary on the closed-end fund market. We're happy to have you with us today, Tom.

TR: Hi, Diane. Good to be with you.

CEFA: **Tom, you recently published your report covering December 2019. You look closely at performance, premiums and discounts, corporate activity. What overall trends are you seeing in the closed-end fund space, and how did those trends play out in December?**

TR: Well, I think a lot of investors, whether you are on closed-end fund side or open-end side of the equation, I think everybody was looking to an agreement. Whether it be a phase one agreement or not, between China and the U.S. And I think people were hearing from both the Chinese side, and also from the U.S. side, that we were getting closer and closer. And I think that propped up the markets fairly well for us.

We had a very strong non-farm payroll report for November that came in, 266,000 versus 180,000, so I think investors were really thrilled to see that as well. It appears that the economy is firing on all cylinders, contrary to what a lot of other people said. 3.5% unemployment rate tied a 50 year low. So, overall investors were very sanguine on the market.

We saw that equity funds rose 3.36% on an av basis for December. It was the fourth month of plus side performance. And for the second consecutive month we saw fixed income funds post plus side returns, gaining 1.7% for December. And one thing that people haven't been paying attention too much to was really the increase we saw in oil, and it'll pan out here later in our conversation. The near term oil futures basically had a 10.68% return in December, a monster, after learning that OPEC reduced its output by 500,000 barrels per day actually starting in January. So, it was a real big boon for the closed-end fund space for investors investing in that area.

CEFA: **Now your data breaks out closed-end funds into over 20 classifications. What classifications were the best performing for the month, and which sectors struggled?**

TR: Well, we basically saw world equity and world fixed income funds rise to the top for the first time in couple of months on the fixed income side, but for the fourth consecutive month, on the world equity side. Basically, what we saw was the world equity funds post a 3.71% return. Again, that's the fourth consecutive month they've seen plus side performance. And then if we take a look at the world fixed income side, for the third month in four, we saw a 2.59% return this month.

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Let's go back though. Energy master limited partnerships were actually the highest and best performer. Recall that I said that oil had one of its best returns in a while, a 10.68% return. Well, that passed through to the energy MLP group, for the first month in nine they rose to the top, returning 10.30%. Another related classification here at Lipper, natural resources funds was the next best performing classification, 7.52%. And emerging markets actually saw a very strong return. They were the third top performer as far as macro groups go or classifications go, 5.44%. These are all one month returns that I just gave you, so phenomenal returns on that.

And let me quickly tell you about the fixed income. Emerging market debt, 3.82% for the month. High yield leverage, 2.25%. And high yield unleveraged was 2.24%. So, really the story on this area was people willing to put risk on the portfolio. They were paying attention to what was happening between the global markets. And finally, they were thrilled by the non-farm payroll report showing a lot better economic activity.

CEFA: **Is this a change in what you have seen in the previous months? Was there any impact from year end tax-loss selling?**

TR: When we take a look at NAV based, and basically what happened on Friday is NAV based returns. If we take a look at the market returns that are out there, so market prices, those are the most influenced by premium and discount behavior. And we did see that the average equity fund actually had a widening of its discounts by 80 basis points, which we would expect from a little bit of that tax-loss selling at year end. So, we did see that.

Interesting enough on the fixed income side that did not occur. We saw a 54 basis increase, or improvement I should say, or a narrowing of discounts to 5.63 for the average fixed income fund. So yes, we did see some impact from tax-loss selling, but it was predominantly only on it. And we'd expect that with one of the biggest equity performance years that we've had in a while. We'd expect that at the year end when people were probably looking for some safety, taking some of those hard won profits off the table, and also thinking about Uncle Sam.

CEFA: **Now, closed-end funds can trade at a premium or a discount net asset value. What were the trends in premium discount behavior?**

TR: Again, so we saw equity funds widen about 80 basis points. They actually increased their median discount to 7%. And then we saw the fixed income funds go to 54 basis points improvement, and the median discount for fixed income funds was 5.63%. And if we take a look at some of these, we see that the worst case scenario was, or actually, the worst thing was it actually occurred in December 2018, we saw an average discount for all closed-end funds, whether it was fixed income or equity, at 11.97%.

CEFA: And how do premiums and discounts compare to their historical averages?

TR: And we've seen a decline. We've seen actually improvement, and it's generally at a discount. We saw that the average fund, again, whether it was equity or fixed income, had a median discount of 5.78% today. But it's still much better than the 6.97 median average discount that we saw for the group over the last 13 months.

CEFA: Which sector saw the greatest improvement and the most downdraft?

TR: So, single-state munis actually saw the largest narrowing of discounts, 120 basis points to 7.59. And then the largest increase was in the world income funds was still in the taxable bond fund side, they saw the largest widening of their discounts, 130 basis points, but actually to a very reasonable 6.02% discount on average.

CEFA: Tom, there was quite a bit of corporate activity in 2019, and notably there has been an uptick in initial public offerings. Do you expect this to continue into 2020, and what is the impact of the closed-end fund market?

TR: So, I do think that we're going to start seeing this. One of the things that we saw in the prior year, in 2018, we saw a lot of consolidation. We saw, actually, the number of mergers and liquidations exceed the number of new funds being created. But this year we saw a new trend of not only more interval funds coming out, there was 26. There was 33, by the way, created in 2018. In 2019, we saw 26, so the trend continued. But instead of three in 2018 from the conventional closed-end fund point of view, we saw 10 new conventional closed-end funds being created in 2019.

I think that's where we're going to see more of the trend. We saw the consolidations. The muni bond fund categories that particularly where we saw New York, let's say, aggressive or a New York general, we see that fund families actually consolidated a lot of those general muni bond funds into each other trying to get economies of scale. But what we're seeing now is an embracing of other types of income producing funds, and I think that's where some of the trend is going to come from is new creation. So, I do believe this will continue on.

CEFA: Interval funds differ somewhat from traditional closed-end funds, and they have been gaining interest among investors and fund sponsors. What activity are you seeing among interval funds?

TR: Okay, so the activity that I'm seeing around interval funds is that the interval funds, first of all, are double edged sword. When we're taking a look at them as we have discussed in the past. Basically, they are a continual offering, just like any open-end fund, however, they only have quarterly refundings. But the trick here is that the fund families are able to raise money on a continual offering basis. But there is a little bit of drag on performance that we would need to be concerned about, because they have to have some money around to meet those quarterly redemptions. But one of the trends that we're seeing is the fund family sponsors are actually coming out and coming out with more income related type of funds.

CEFA: **Do you expect to see new interval funds continue to be brought to market in 2020? And if so, what type of funds?**

TR: I do. Really the fund sponsors are trying to meet the need of the Baby Boomers. Baby Boomers have a need for income. Right now, I think many investors think that the equity market's a little long in the tooth. The treasury rates are flat. We heard, basically, the Federal Reserve Board come out and say, "Hey, they're okay waiting." They're going to wait for economic data to show whether they should be either increasing interest rates, decrease interest rates. So, interest rates are very low.

So, investors are struggling to find a instrument that they can use to meet their income needs in retirement. And so, I think what we're going to see is more offerings of income related funds. So, we'll see real estate funds, covered-call funds. Any of those income, preferred stock, anything that can get them a little bit extra yield in there. And I think they'll be using the interval fund to meet those needs.

CEFA: **Tom, thank you so much for taking the time to join us today.**

TR: My pleasure. Thanks for having me, Diane.

CEFA: **And we want to thank you for tuning into another CEF Insights podcast. For more educational content, please visit our website at www.cefa.com.**

Disclosure

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