

# HIGHLIGHTS FROM CAPITAL LINK'S 11TH ANNUAL CLOSED-END FUNDS & GLOBAL ETFs FORUM

CONFERENCE NOTES  
WEDNESDAY, APRIL 25, 2012

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*The below Conference Notes are provided by Lewis Aaron, Founder and Director of Fund Consultants LLC, who served as Conference Chairman over the plenary sessions of the 11th Annual Closed-End Funds & Global ETFs Forum on Wednesday, April 25, 2012, at the Metropolitan Club in New York City. For more information, please contact Capital Link at (212) 661-7566 or [forum@capitallink.com](mailto:forum@capitallink.com).*

## **MORNING SESSIONS**

### **1. OPENING ADDRESSES**

#### ***Session 1.1 - CLOSED VERSUS OPEN-END FUNDS – WHO WAS THE BETTER PERFORMER IN 2011?***

*Mr. Lewis Aaron, Founder and Director – Fund Consultants LLC – Conference Chairman*

##### **Key points:**

- Over both 1 year and 5 years, both equity and bond CEFs performed better than their open-ended counterparts.
- This outperformance was evidenced in the majority of closed-end fund sectors mapped against their equivalent open-ended sectors.
- Outperformance was due in part to CEF lower expense ratios, but also due in part to leverage and better management of the investment of fund cash flows.

#### ***Session 1.2 - THE STATE OF THE CLOSED-END FUND INDUSTRY IN 2012***

*Mr. Jeff Margolin, Senior Vice President and Closed-End Fund Analyst – First Trust Advisors*

##### **Key points**

- CEFs have endured big challenges, especially with the collapse of the auction rate preferred market.
- CEFs have not only survived, but have strongly

rebounded. The overall discount is only 1.3% in equity funds and fixed interest on a 0.7% premium.

- Demand is strong as interest rates at historical lows, and more and more people are approaching retirement age.
- Of the CEF sectors, First Trust likes domestic equities and the senior loan side of the fixed interest market.
- The challenge will be how to guide investors through rising interest rates when this happens.

#### ***Session 1.3 - THE STATE OF THE ETF INDUSTRY IN 2012***

*Mr. Martin Kremenstein, Head of North America ETP Management – db-X Group*

##### **Key points**

- ETFs had a strong year with AUM up 14% at \$1.6



*Jeff Margolin*



*Martin Kremenstein*



From left to right: Kenny Feng, Yigal Jhirad



Donald Amstad



Dan Spears



William Housey

trillion since the end of the year, and up 20% since 2010. The number of products is up 37%.

- Despite this fast growth, they are still small when compared to mutual funds.
- The investor base is growing with private investors as well as institutional investors.
- Interesting new launches include \$1.5 billion S&P volatility fund, and a \$500 million active management fund.
- He sees active management as a growth trend in ETFs.

## 2. REAL ASSETS FOR REAL RETURNS

### **Session 2.1 - THE ELEMENTS OF INVESTING IN REAL ASSETS**

*Mr. Yigal Jhirad, Senior Vice President & Portfolio Manager – Cohen & Steers*

#### **Key points**

- Real assets are being driven by low interest rates and growth in demand from emerging markets whilst supplies remain relatively constant.
- Real assets can be effective hedges against inflation, have stable returns, and can complement (diversify) a portfolio of financial assets.
- He recommends a core portfolio of commodity futures, global natural resources, and real estate.
- A supplementary portfolio of diversifiers, such as gold and currencies, is also recommended.

### **Session 2.2 - OPPORTUNITIES IN THE MLP MARKET**

*Mr. Kenny Feng, President and Chief Executive Officer – Alerian*

#### **Key points**

- Why MLP's are so attractive:
  - Energy infrastructure is growing (\$240 billion needs to be spent).
  - Stable cash flow that grows 6%, while growing at about 3.5% pa.
  - There is no entity level tax for the time being.

- There are many ways to invest in MLPs—CEFs, ETFs, or direct.

## 3. OUTLOOK AND OPPORTUNITY IN THE ASIA PACIFIC REGION

### **Session 3.1 - OUTLOOK FOR ASIAN ECONOMIES**

*Mr. Donald Amstad, Director – Aberdeen Asset Management Asia*

#### **Key points**

- Asian governments are solvent as opposed to the bankrupt Western economies, and currencies are cheap and set to appreciate.
- Asia is growing and is just too important to ignore in your allocations.

## 4. FIXED INCOME INVESTING

### **Session 4.1 - ROYALTY TRUST**

*Mr. Dan Spears, Partner & Portfolio Manager – Swank Capital / Cushing MLP Asset Management*

#### **Key points**

- MLPs are very attractive with a 6% yield and growing distributions.
- Any additional risk has been more than offset with additional returns.
- Energy independence is a big theme in the future, and the U.S. could become a net exporter of oil.
- Many different types of MLPs are available, investing in Upstream, Midstream, or combinations of the two.

### **Session 4.2 - SENIOR LOAN MARKET UPDATE AND OUTLOOK**

*Mr. William Housey, Senior Vice President & Senior Portfolio Manager, Leveraged Finance Investment Team – First Trust Advisors*

#### **Key points**

- Why senior loans?



- Senior loan market remains attractive despite uncertainty surrounding interest rates.
- Defaults remain well below trend.
- Spreads remain very attractive (LIBOR +625bp).
- U.S. corporate health is quite strong.

### **Session 4.3 - FIXED INCOME ETF PORTFOLIO MANAGEMENT**

*Mr. Don Suskind, CFA, Senior Vice President & Head of ETF Product Management – PIMCO*

#### **Key points**

- Government bond prices are high and there may be downside risk so he recommends underweight.
- Agency mortgages look very attractive so overweight, but focus on the lower coupon, which is more defensive.
- There are many investor choices in fixed interest management, ranging from direct investment in more than 4,200 direct bonds to active CEFs and active ETFs or indexed ETFs.

## **5. EQUITY & TOTAL RETURN INVESTING**

### **Session 5.1 - FACTOR INVESTING: MEASURING AND MANAGING FACTOR EXPOSURES**

*Mr. David Koenig, Director, Investment Strategy – Russell ETFs*

#### **Key points**

- Understanding a portfolio's return factors gives rise to a whole host of ways to control risk and returns.
- The recent introduction of ETFs based on individual portfolio factors gives investors a cost effective way of managing return factors for the first time.
- The use of low volatility ETFs can actually help manage the overall volatility of a portfolio.

### **Session 5.2 - CURRENCY EFFECTS ON INTERNATIONAL EQUITY INVESTMENTS**

*Mr. Alex Depetris, Vice President – db-X Group*

#### **Key points**

- Diversification abroad can bring with it much higher growth potential, but there are risks of political instability.
- It is important to note that currency fluctuations can severely affect returns to USD investors so it is important to have an fx strategy.

## **6. INVESTING INTERNATIONALLY**

### **Session 6.1 - THE THIRD COMING OF EMERGING MARKETS**

*Mr. James Upton, Executive Director – Morgan Stanley Investment Management*

#### **Key points**

- Breakout Nations: In Pursuit of the Next Economic Miracles—the new book by Morgan Stanley's Head of Emerging Markets Ruchir Sharma—provides the thesis for this presentation.
- The third wave of growth in emerging markets equities is about to start.
- Underweight China as growth will disappoint.
- Currencies in Brazil and Russia are vulnerable so be careful.
- Korea and Taiwan are cheap.

### **Session 6.2 - THE MEXICO FUND: MEXICAN ECONOMIC CLIMATE, PERSPECTIVES & INVESTMENT OPPORTUNITIES**

*Mr. Eduardo Solano, Investor Relations Vice President – The Mexico Fund, Inc.*

*Mr. Alberto Osorio, Senior Vice President, Treasurer & CFO – The Mexico Fund Inc.*



*Don Suskind*



*David Koenig*



*From left to right: Bruno del Ama, Alberto Osorio, Eduardo Solano, James Upton*



*From left to right: Robert Shaker, Robert Ionescu, Paul Williams, Robert Bush, Michael Taggart*

#### **Key points**

- Since Mexico GDP is closely linked to the U.S., it was affected by the financial crisis.
- Expect 3% growth this year, fuelled mainly from domestic consumption.
- Inflation is under control and running at around 3.7%.
- Concern about Mexican financial institutions is overdone and non-performing loans only 35 (similar to the US).
- Both presenters believe prospects are good for 2012.

### **Session 6.3 - TACTICAL OPPORTUNITIES IN GLOBAL MARKETS**

*Mr. Bruno del Ama, Chief Executive Officer –Global X Funds*

#### **Key points**

- He believes in the long term secular trends in emerging markets on a 10-year investment horizon.
- Emerging markets will see increased commodity consumption as a result of rising wealth.
- In Brazil & China, households are getting wealthier and will be demanding more and more consumer goods and luxury goods.
- Also, like Colombia, Greece, and Norway.

## **AFTERNOON SESSIONS**

### **7. CEF INDUSTRY ROUNDTABLE**

#### **CURRENT TRENDS, OPPORTUNITIES & OUTLOOK IN CEFS**

**Moderated by:** Mr. Mike Taggart, Director of U.S. Closed- End Fund Research – Morningstar

#### **Panelists:**

- Mr. Robert Bush, Director, Closed-End Fund Products – Calamos Investments
- Mr. Paul Williams, Managing Director, Product Development – Nuveen Investments, Global Structured Products Group



*From left to right: Deborah Fuhr, Erik Liik, Edward Rosenberg, Alex Depetris, Paul Justice*

- Mr. Robert Ionescu, Director and Senior Closed-End Fund Product Specialist – Legg Mason
- Mr. Robert Shaker, Portfolio Manager – Shaker Financial Services

#### **Key points**

- Current trends discussed by Robert Bush include continued emphasis on yield products as well as the rising importance of the asset manager direct sales force in order to better inform investors and analysts, keeping the secondary market strong. Better informed means less discount.
- Robert Shaker talked about tactical swapping or discount capture as a strategy to increase returns if you get your timing right. Be careful of Z-scores over defined periods.
- Bob Ionescu discussed what factors he looks for in choosing a closed-end fund—including yield, UNI or income cover, discount, and performance.
- Paul Williams discussed leverage.

### **8. ETF INDUSTRY ROUNDTABLE**

#### **CURRENT TRENDS, OPPORTUNITIES & OUTLOOK IN ETFs**

**Moderated by:** Mr. Paul Justice, Director of North American ETF Research – Morningstar

#### **Panelists:**

- Mr. Alex Depetris, Vice President – db-X Group
- Mr. Edward Rosenberg, Director, Head of ETF Capital Markets & Analytics – Russell ETFs
- Mr. Erik Liik, President & CEO – FocusShares
- Ms. Deborah Fuhr, Partner & Co-founder – ETF Global Insight

#### **Key points**

- Paul Justice felt that active ETFs are one of the most prominent trends in the marketplace.
- Edward Rosenberg mentioned that factor ETFs provide a new way to adjust portfolio factors such as volatility or to diversify.
- Erik Liik discussed the exciting potential to use ETFs in 401k and smaller retirement plans.





*From left to right: Florian Fischer, Mark Absy*

- Deborah Fuhr mentioned the great usefulness of ETFs in providing tactical asset allocation for both institutional and private individuals.

## 9. INDICES ROUNDTABLE

### 9.1 - INDICES SESSION 1

*Mr. Mark Absy, Senior Index & ETF Manager – International Securities Exchange (ISE)*

#### Key points

- Mark Absy explained using the SPY bear call options and the bull put options from both a buyers and sellers perspective.
- He also discussed using vertical spreads, which are self financing.

### 9.2 - INDICES SESSION 2

*Mr. Florian Fischer, Global Product Manager – Thomson Reuters Indices*

#### Key points

- Florian Fischer discussed the interesting things that Thomson Reuters is doing in the indices area, including the use of consensus forecasts (IBES estimates) in indices.
- He also discussed the trends that he saw with respect to new indexing products.

## 10. COMMODITIES

### 10.1 - COMMODITY OPPORTUNITIES – A TOTAL RETURN STRATEGY

*Mr. Jonathan Spencer, President – Gresham Investment Management*

#### Key points

- Commodities markets are large and now available to private investors. Nuveen Diversified Commodities (CFD) is an easy way for private investors to play the commodities markets.
- Production cycles of commodities and their interaction with the economy make them an effective hedge against inflation.
- Gresham Investment Management, with Nuveen, has incorporated TAP PLUS into CFD.
- CFD offers active management in exchange traded futures with no leverage and a regular monthly distribution.

### 10.2 - COMMODITY ETF ROUNDTABLE

**Moderated by:** *Ms. Mariana Bush, Closed-End Fund & Exchange-Traded Tracking Products – Wells Fargo Advisors, LLC*

#### **Panelists:**

- *Mr. John T. Hyland, CFA, CIO – United States Commodity Funds, LLC (USCF)*
- *Mr. Ashmead Pringle, President – GreenHaven LLC*
- *Mr. Jonathan Spencer, President – Gresham Investment Management LLC*

#### Key points

- Ashmead Pringle and the panel discussed the case for holding commodities as an inflation hedge, dollar hedge, and as an absolute return asset class.
- The physical holding of commodities is expensive, so the use of exchange futures is the best or only way to achieve exposure on a cost effective basis.
- The futures market is technical and best left to experts like the panel who run both ETFs and CEFs. The panel explained concepts such as roll, roll yield, collateral yield, and pricing anomalies such as backwardations and contangos.
- Jonathan Spencer mentioned active ETFs that



*From left to right: Mariana Bush, John Hyland, Ashmead Pringle, Jonathan Spencer*



*William Rhind*



*Matthew Moran*

provide a systematic approach with an active element, such as their proprietary TAP.

## 11. PRECIOUS METALS

### 11.1 - OUTLOOK FOR PRECIOUS METALS AND ETFS IN 2012

*Mr. William Rhind, Managing Director – ETF Securities (US) LLC*

#### Key points

- Precious metals have outperformed equity and bond benchmarks over the past 10 years.
- They achieved this outperformance with volatility similar to the S&P 500.
- Precious metals have a low correlation to equities and bonds, providing real diversification benefits.
- Q1 was a strong one for platinum and palladium ETFs. The reason is the recovery optimism.

## 12. EQUITY VOLATILITY MANAGEMENT

### 12.1 - EQUITY VOLATILITY MANAGEMENT

*Mr. Matthew Moran, Vice President – Chicago Board Options Exchange (CBOE)*

#### Key points

- Matthew explained that writing index options against stock held (covered call funds) can provide portfolios with higher income and lower volatility than they could achieve without them.
- He also explained the relationships between implied and actual volatility, and that sellers of volatility often do better because the market perception of volatility (implied) is often higher than the actual.

## 13. ANALYST PANEL

**Moderated by:** *Mr. Michael Jabara, Vice President, Head of Exchange-Traded Fund (ETF) and Closed-End Funds Research – Morgan Stanley Smith Barney*

**Panelists:**

- *Mr. Jon Maier, Global Macro Research, Closed-End Fund Analyst and ETF Strategist – Bank of America Securities - Merrill Lynch*
- *Ms. Mariana Bush, Closed-End Fund & Exchange-Traded Tracking Products – Wells Fargo Advisors, LLC*
- *Mr. Alex Reiss, Vice President, Closed-End Fund Research – Stifel Nicolaus*



*From left to right: Alex Reiss, Michael Jabara, Mariana Bush, Jon Maier*

#### Key points

- Jon Maier explained that CEF stock recommendations are never at odds with his firm's view of markets and currencies. He overlaid the firm's macro view with his individual stock recommendations, but of course there are good and bad within each sector.
- Mariana Bush explained what she termed the bad return of capital, or destructive capital, as contrasted to the good. Destructive erodes the NAV over time whereas with the good, or constructive return, the NAV still increases despite the capital loss distribution.
- John Maier was asked his views on index optimization versus replication. He thought that with fixed income indices, optimization might prove better whereas with equities indices. Then, exact replication was probably best.
- Mariana Bush also mentioned how passively managed fixed income funds could still add alpha through securities lending.

#### CONTACT:

Jessica Cho

Capital Link, Inc.

230 Park Avenue, Suite 1536, New York, NY 10169

T: (212) 661-7566 | [forum@capitallink.com](mailto:forum@capitallink.com)

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