

Convertible and High Income Fund (CHY) 2Q17 Commentary

CALAMOS[®]

INVESTMENTS

FUND

- » CHY is an enhanced fixed income offering that seeks to provide an attractive monthly distribution, with a secondary objective of capital appreciation.
- » Invests in: high yield and convertible securities, issued primarily by U.S. companies.

Current Annualized Distribution Rate¹ 10.14%

ASSET ALLOCATION

Convertible Bonds	45.1%
Corporate Bonds	38.3
Convertible Preferred Stock	12.8
Common Stock	1.1
Preferred Stock	0.5
Cash and Receivables/Payables	2.2

The portfolio is actively managed. Holdings and weightings are subject to change at any time without notice. Asset Allocation Weightings are calculated as a percentage of Managed Assets.

¹ Current Annualized Distribution Rate is the Fund's most recent distribution, expressed as an annualized percentage of the Fund's current market price per share. The Fund's most recent distribution was \$0.1000 per share. Based on our current estimates, we anticipate that approximately \$0.0553 is paid from ordinary income or capital gains and \$0.0447 of the distribution represents a return of capital. Estimates are calculated on a tax basis rather than on a generally accepted accounting principles (GAAP) basis, but should not be used for tax reporting purposes. Distributions are subject to re-characterization for tax purposes after the end of the fiscal year. This information is not legal or tax advice. Consult a professional regarding your specific legal or tax matters. Under the Fund's level rate distribution policy, distributions paid to common shareholders may include net investment income, net realized short-term capital gains and return of capital. When the net investment income and net realized short-term capital gains are not sufficient, a portion of the level rate distribution will be a return of capital. In addition, a limited number of distributions per calendar year may include net realized long-term capital gains. Distribution rate may vary.

There is no assurance that the Fund will achieve or maintain its investment objective.

Overview

During the quarter, the convertible and equity markets tacked on to their strong first quarter performance. Despite waning enthusiasm on the political front as Congress struggled to find common ground, investors continued to be bullish regarding the prospects of tax reform, regulatory easing and increased infrastructure spending. A low unemployment rate, rising consumer confidence, and rising personal income stemming from lower gasoline prices were among the items that encouraged investors.

Investors also continued to focus on the prospects of rising interest rates after the Federal Reserve increased the Fed Funds rate by 25 basis points as expected in June. The Fed also stated that it would begin reducing its balance sheet "relatively soon" and it pointed towards further interest rate increases in the event of rising inflation. The U.S. Treasury yield curve flattened during the quarter as three-month yields increased from 0.76% to 1.03%, while 30-year yields declined from 3.02% to 2.84%. Three and five-year Treasuries saw little change as they increased 5 and 4 basis points to 1.55% and 1.89% respectively.

Convertibles posted a 2.46% return in the quarter, as measured by the BofA Merrill Lynch All U.S. Convertibles Index (VXA0), and participated in the upside move of the broader equity market as represented by the 3.09% return of the S&P 500 index. Convertibles also outpaced the high yield market based on the 2.24% return of the BofA Merrill Lynch High Yield Master II Index. Convertibles continued to benefit from narrowing credit spreads, richening valuations, and the strong performance of their underlying stocks, up 7.30% during the quarter. BofA Merrill Lynch reported average convertibles trading at a 1.58% average discount to their fair theoretical value at the end of the quarter, which reflected an improvement from the 1.71%

ANNUALIZED TOTAL RETURN AS OF 6/30/17

	QTD	1-YEAR	3-YEAR	5-YEAR	10-YEAR	SHARE INCEPTION (05/28/03)
On Market Value	6.67%	24.26%	2.80%	8.48%	6.59%	8.07%
On NAV	3.32	17.02	2.78	8.04	6.96	8.38

Source: State Street Corporation

Returns of less than 12 months are cumulative returns. Returns for periods greater than 12 months are annualized returns. Total return measures net investment income and capital gain or loss from portfolio investments as an annualized average. In calculating net investment income, all applicable fees and expenses are deducted from the returns.

Performance data quoted represents past performance, which is no guarantee of future results. Current performance may be lower or higher than the performance quoted. Portfolios are managed according to their respective strategies which may differ significantly in terms of security holdings, industry weightings, and asset allocation from those of the benchmark(s). Portfolio performance, characteristics and volatility may differ from the benchmark(s) shown.

You can purchase or sell common shares daily. Like any other stock, market price will fluctuate with the market. Upon sale, your shares may have a market price that is above or below net asset value and may be worth more or less than your original investment. Shares of closed-end funds frequently trade at a market price that is below their net asset value.

Please refer to back page for important notes.

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discount witnessed at the beginning of the quarter and 2.94% discount in June 2016. Additionally, high yield credit spreads narrowed 15 basis points to 441 basis points over Treasuries, according to J.P. Morgan.

Convertibles with the strongest economic sector results included consumer discretionary (+11.10%), health care (+4.83%) and financials (+4.28%). Convertibles that most lagged the benchmark result included energy (-10.53%), materials (-3.79%) and telecommunications (-3.35%). Investment-grade convertibles (+4.02%) outperformed speculative-grade issues (+1.44%). Convertibles with the most equity sensitivity (+2.84%) strongly outperformed convertibles with more balanced risk/reward attributes (+2.13%) and credit sensitivity (+2.47%).

The U.S. high yield bond market, as represented by the BofA Merrill Lynch High Yield Master II Index, returned 2.24% in the second quarter. Option-adjusted spreads tightened by 15 basis points, ending at 377 basis points while trading in a tight range over the course of the quarter. With two-year yields closing at 1.38% (up from 1.25%), and ten-year yields closing at 2.31% (down from 2.39%), the curve flattened 22 basis points during the second quarter.

The best-performing sectors in the BofA Merrill Lynch High Yield Master II Index were banks (+4.4%), leisure (+3.7) and healthcare (+3.6%), while energy (-1.1%), broadcasting (+1.0%), and environmental (+1.2) represented the worst laggards. The up-in-credit trade led the way as BB-rated credits (+2.7%) outperformed their B/CCC counterparts (+1.8%). According to J.P. Morgan, the U.S. high yield default rate ended June at 2.02%, which represented a 13 basis point increase from May's 1.89% figure, but a 2.25% reduction from the year-end 2016 rate of 4.27%.

Despite higher Treasury rates across some of the curve, the yield-to-worst declined 20 basis points during the quarter to close at 5.68%. The average dollar price increased from \$100.6 to \$101.3. New issue activity slowed from a brisk first quarter pace, but finished at a reasonable \$72.9 billion.

Distributions Remained Competitive. The fund maintained a monthly distribution of \$0.100 throughout the quarter. The fund's current annualized distribution rate was 10.14% of market price as of June 30, 2017. We believe that the fund's monthly distributions are competitive, given that very low interest rates and yields remain the norm throughout much of the global marketplace. For example, as of June 30, 2017, the 10-year U.S. Treasury bond yield was 2.31% and the BofA Merrill Lynch U.S. High Yield Master II Index was 3.77%.

Performance Review

For the quarter ending June 30, 2017, the fund returned 6.67% on price and 3.32% on NAV. This outperformed on stock price, and on NAV relative to the Credit Suisse U.S. High Yield Index, which returned 1.97% for the same period.

Contributing Factors. This past quarter, the fund benefitted from selection in consumer discretionary, particularly from our allocation and selections in automobile manufacturers relative to the Credit Suisse U.S. High Yield Index. The fund also benefitted from an overweight and selection in the pharmaceuticals industry within the health care sector.

Detracting Factors. Our selections in energy—notably in oil and gas exploration and production relative to the Credit Suisse U.S. High Yield Index—detracted from the quarterly return. Likewise, our holdings in information technology—notably in the semiconductors industry—impeded performance relative to the index during the period.

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Positioning

We continue to hold our highest allocations (27%) in the “BB” credit tier, as we believe this exposure will offer investors a better risk/return dynamic over time while providing regular income. We continue to take a very selective approach to CCC rated credits, in spite of the fact that they have seen continued improvement over the past quarter. We are cognizant of the fact that rising interest rates and volatility can impact longer-term fixed income securities. Accordingly, as of June 30, 2017, the weighted average bond duration of our portfolio was only 4.3 years. From an economic sector perspective, our heaviest exposures are in the information technology, consumer discretionary and health care sectors, which collectively make up approximately 60% of our holdings. Our lightest weights are in utilities, real estate and consumer staples. Approximately 91% of our holdings are in the U.S.

Leverage

We believe this environment is conducive to the prudent use of leverage as a means of enhancing total return and supporting the fund’s distribution rate. In spite of a slight cost increase due to rising interest rates over the quarter, our use of leverage enjoyed a favorable spread over its cost. We borrowed at what we trust were attractive rates, and invested the proceeds at levels in excess of the cost of leverage. We think our recent leverage reallocation has benefitted the fund and believe this enhancement will continue to provide diversity and increased capacity to our borrowing capabilities, while presenting the opportunity to reduce interest related costs. As of June 30, 2017, our total percent of assets leveraged was approximately 29%.

Conclusion

We have a particularly favorable outlook on the convertible market given the downside protection the structure provides in case the markets experience an increase in volatility after a relatively non-volatile first half of 2017. We believe there will be continued healthy new convertible issuance given strong equity market performance and an increased appetite from issuers looking to raise capital for growth projects. We continue to view convertibles as a favorable asset class given their historical performance in rising rate environments and their ability to dampen the volatility of a pure-equity exposure.

Regarding high yield, barring an unforeseen breakout event, our expectation is for the default environment to continue to trend along its recent benign path, though we remain cautiously positioned from a credit perspective given the asymmetric risk/reward profile of CCC issuers. Given the range bound environment for both interest rates and spreads over the first half of 2017, coupled with spreads trading well through long-run averages, we anticipate limited upside from price return over the next six to 12 months. As such, the asset class overall should provide a coupon-like return. We believe that our active portfolio management with its rigorous bottom-up security selection process should enable us to generate better-than-coupon returns in this environment.

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Important Fund Information

The goal of the level-rate distribution policy is to provide investors a predictable, though not assured, level of cash flow. Monthly distributions paid may include net investment income, net realized short-term capital gains and, if necessary, return of capital. Maintenance of this policy may increase transaction and tax costs associated with the fund.

A credit rating is a relative and subjective measure of a bond issuer's credit risk, including the possibility of default. Credit ratings are assigned to companies by third-party groups, such as Standard & Poor's. Assets with the highest ratings are referred to as "investment grade" while those in the lower tiers are referred to as "noninvestment grade" or "high yield." Ratings are measured using a scale that typically ranges from AAA (highest) to D (lowest).

Leverage creates risks which may adversely affect return, including the likelihood of greater volatility of net asset value and market price of common shares; and fluctuations in the variable rates of the leverage financing. The ratio is the percent of total managed assets.

The fund may invest up to 25% of its assets in foreign securities and invest in an array of security types and market-cap sizes, each of which has a unique risk profile. As a result of political or economic instability in foreign countries, there can be special risks associated with investing in foreign securities. These include fluctuations in currency exchange rates, increased price volatility, and difficulty obtaining information.

There are certain risks associated with an investment in a convertible bond such as default risk—that the company issuing a convertible security may be unable to repay principal and interest, and interest rate risk—that the convertible may decrease in value if interest rates increase.

Investments by the fund in lower-rated securities involve substantial risk of loss and present greater risks than investments in higher-rated securities, including less liquidity and increased price sensitivity to changing interest rates and to a deteriorating economic environment.

Fixed income securities are subject to interest rate risk; as interest rates go up, the value of debt securities in the fund's portfolio generally will decline.

Owning a bond fund is not the same as directly owning fixed income securities. If the market moves, losses will occur instantaneously, and there will be no ability to hold a bond to maturity.

The fund may invest in derivative securities, including options. The use of derivatives presents risks different from, and possibly greater than, the risks associated with investing directly in traditional securities. There is no assurance that any derivative strategy used by the fund will succeed. One of the risks associated with purchasing an option is that the fund pays a premium whether or not the option is exercised.

The fund may seek to purchase index put options to help reduce downside exposure however, the effectiveness of the fund's index option-based risk management strategy may be reduced if the fund's equity portfolio does not correlate to the performance of the underlying option positions. The fund also risks losing all or part of the cash paid for purchasing index options. Unusual market conditions or lack of a ready market of any particular option at a specific time may reduce the effectiveness of the fund's option strategies, and for these and other reasons the fund's option strategies may not reduce the fund's volatility to the extent desired. From time to time, the fund may reduce its holdings of put options, resulting in an increased exposure to a market decline. Please refer to the fund's prospectus for a full description of risks.

Parties entering an interest rate swap take on exposure to a given interest rate; the exposure can be long or short depending on whether a counterparty is paying or receiving the fixed rate. At the same time, each party takes on the risk—known as counterparty credit risk—that the other party will default at some time during the life of the contract.

The BofA Merrill Lynch All U.S. Convertibles Index (VXA0) is comprised of approximately 700 issues of only convertible bonds and preferreds of all qualities. BofA Merrill Lynch High Yield Master II Index consists of below investment grade U.S. dollar denominated corporate bonds that are publicly issued in the U.S. domestic and yankee bonds. Issues included in the index have maturities of one year or more and have a credit rating lower than BBB-/Baa3, but are not in default. The index includes domestic high-yield bonds, including deferred interest bonds and payment-in-kind securities. The Credit Suisse U.S. High Yield Index consists of U.S.-

denominated high yield issues of developed countries. Issues must be publicly registered in the U.S. or issued under Rule 144A with registration rights, must be rated "BB" or lower, and the minimum amount outstanding (par value) must be at least \$75 million. The S&P 500 Index is generally considered representative of the U.S. stock market.

Unmanaged index returns assume reinvestment of any and all distributions and, unlike fund returns, do not reflect fees, expenses or sales charges. Investors cannot invest directly in an index.

The information contained herein is based on internal research derived from various sources and does not purport to be statements of all material facts relating to the sectors, securities and markets mentioned. The information contained herein, while not guaranteed as to the accuracy or completeness, has been obtained from sources we believe to be reliable. Opinions expressed herein are as of the date of publication and are subject to change without notice due to various factors and may not necessarily come to pass. Information contained herein is for informational purposes only and should not be considered investment advice.

Terms

A Level Rate Distribution Policy is an investment company's commitment to common shareholders to provide a predictable, but not assured, level of cash flow. **Market Price** refers to the price at which shares of the fund trade in the market. **NAV or Net Asset Value** refers to the net value of all the assets held in the fund. **IPO Price** refers to the initial public offering price for shares of the fund.

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