CALAMOS INVESTMENTS

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Convertible Securities Offer Many Benefits–Including as a Hedge against Higher Interest Rates and Inflation

KEY POINTS

Convertible securities can provide a hedge against rising long-term interest rates and inflation while also providing lower-volatility stock market participation.

Capitalizing on the unique structural features of convertibles requires active management.

Calamos has provided innovative convertible investment solutions since the 1970s, including strategies to enhance fixed income allocations.

The Calamos US Convertible Strategy may help investors resist the temptation to make interest rate or market timing calls.

Since the 1970s, we have used convertible securities to help investors successfully navigate a variety of market and economic risks. Stock market volatility is one of the most pervasive risks investors face, and it can be especially frustrating because of its many causes, including fiscal policy unknowns, increased taxes and regulations, geopolitical pressures, changes to monetary policy, event shocks, and company-specific news. Given the many crosscurrents buffeting the economy today, we expect the stock market to remain choppy and rotational as economic recovery continues.

Meanwhile, new risks are rising in the markets: inflation and the potential for higher interest rates. For many years, investors have grown accustomed to abnormally low inflation, and the shuttering of the economy in 2020 went so far as to raise fears of *deflation*.

However, inflation is now definitely on investors' radars. To some extent, inflation isn't unexpected. Inflation pressures increase when the economy grows at a faster rate. Wage growth, rising commodity prices, and supply-demand imbalances have tended to be powerful drivers of inflation. As the economy is emerging from pandemic lockdown, all of these forces are emerging as well.

The Federal Reserve also can play a part in inflation, either by pumping money into the economy as it has been doing for many years, which leads to a run-up in asset prices, or by not hiking short-term rates quickly enough to cool the economy and markets. Since 2020, the Fed has indicated its willingness to let inflation run hotter without stepping in. Although the Fed has begun to dial back its accommodative policy, it has indicated that short-term rate hikes aren't likely before mid-2022, at the soonest.

Earlier this year, expectations were that inflation would be a short-lived burst driven by pent-up consumer demand as the threat of Covid-19 receded, but inflation is proving less "transitory" and more sticky than many originally anticipated. Adding to investor anxiety, recent data showed a monthly inflation spike the likes of which hasn't been seen in 30 years.

Traditional fixed-income investments, such as Treasury bonds, are vulnerable to inflation to the extent that inflation contributes to a rise in interest rates. This creates challenges for many investors, especially those who are also concerned about equity market volatility. However, investors can take steps to help mitigate the impact of inflation, without rushing headlong into equities.

Convertible securities can enhance a fixed-income allocation by providing a hedge against a rising interest rate environment. Bonds tend to lose value in an environment of rising interest rates. However, convertible returns have tended to more closely reflect equity returns than bond returns when long-term interest rates rise. As we show in the following pages, **our active approach has consistently capitalized on this opportunity.**

Convertibles can provide a hedge against changing interest rates because of their unique structural features, which combine attributes of stocks and bonds. Like stocks, convertibles typically offer upside appreciation in rising equity markets. Like fixed-income securities, they provide income and can mitigate exposure to downside in the stock market. **Although convertibles are influenced to a degree by interest rate fluctuations, they also are affected by the price movements of their underlying stocks; historically, this "equity sensitivity" has helped soften the negative effects of rising interest rates.**

CONVERTIBLES: AN OVERVIEW

Convertible securities are less well known than stocks and bonds, but they are a global asset class with a history that traces back to the mid-1800s.

A convertible bond can be exchanged—or converted— into a specific number of shares of common stock of the issuer's company. Convertible bonds are technically classified as debt instruments because they pay interest and have a maturity date.

To learn more about convertibles, **read our guide, *"Convertible Securities: Structures Valuation, Market Environment and Asset Allocation."***

With Active Management, Convertible Securities Can Address Specific Goals

Convertible securities are complex, and the characteristics of an individual convertible security can change over time. At certain points, a convertible may behave more like a stock; at other points, it may behave more like a bond. For example, the more a convertible's price is determined by the value of its underlying equity, the less likely it is to be influenced by changing interest rates. However, too much equity sensitivity may expose a convertible security to drawdowns in the stock market.

It is not simply the inclusion of the convertible that positions us to achieve a client's specific investment objective. Convertibles must be actively managed to ensure that a portfolio reflects the desired level of interest rate sensitivity or exposure to the stock market. With active management, convertible securities can be used to support a variety of investment goals and risk tolerances.

Convertibles are an attractive part of an enhanced fixed-income allocation, but reduced interest-rate sensitivity is not the only potential benefit convertibles offer. Convertibles also can be used to provide lower-volatility stock market participation. Because a convertible is linked to its underlying stock through its conversion feature, it tends to rise when its underlying stock does. However, the convertible's bond characteristics—its bond value "floor" and coupon—can help mitigate downside during periods of stock market volatility.

Because convertible securities can be actively managed to adjust to different market and interest rate conditions, they are an attractive choice for the core of an asset allocation. History shows that long-term rates can move suddenly and with little warning, and stocks can also experience unexpected downturns. **An actively managed convertible strategy allows investors to position their portfolios ahead of changes in interest rates and market turns.**

A Historical Perspective on Actively Managed Convertibles

Calamos Investments began investing in convertible securities during the difficult financial markets of the 1970s. Our proprietary investment approach has been tested over multiple market and economic cycles, including a variety of inflationary environments. We found that convertible securities could offer benefits that stocks and bonds could not, providing a powerful tool for enhancing returns and managing risk for our clients.

We established our first institutional convertible strategy in the late 1970s. Today, we use convertibles in a range of strategies, with tailored risk/reward profiles for client goals (e.g., enhanced fixed income or lower volatility). One of our flagship strategies is the Calamos US Convertible Strategy.

The Calamos US Convertible Strategy delivered significant outperformance when long-term interest rates rose. In Figure 1, we show the strategy's performance during periods when the 10-year Treasury yield increased more than 1 percentage point. In each period, the Calamos US Convertible Strategy (blue) posted positive performance, whereas traditional fixed-income indexes (green and orange) lost value more often than not. Additionally, the strategy often outperformed by a very wide margin.

The Calamos US Convertible Strategy also has provided equity-like performance over the long term (Figure 2) with a historically attractive asymmetrical risk profile. Through active management, the strategy has captured more of the stock market's upside and less of its downside, including through the Covid-19 market meltdown and subsequent rebound (Figure 3). By preserving capital on the downside, the strategy can stairstep its way up over a full market cycle.

FIGURE 1. CALAMOS US CONVERTIBLE STRATEGY: OUTPERFORMANCE WHEN INTEREST RATES RISE

CUMULATIVE RETURNS

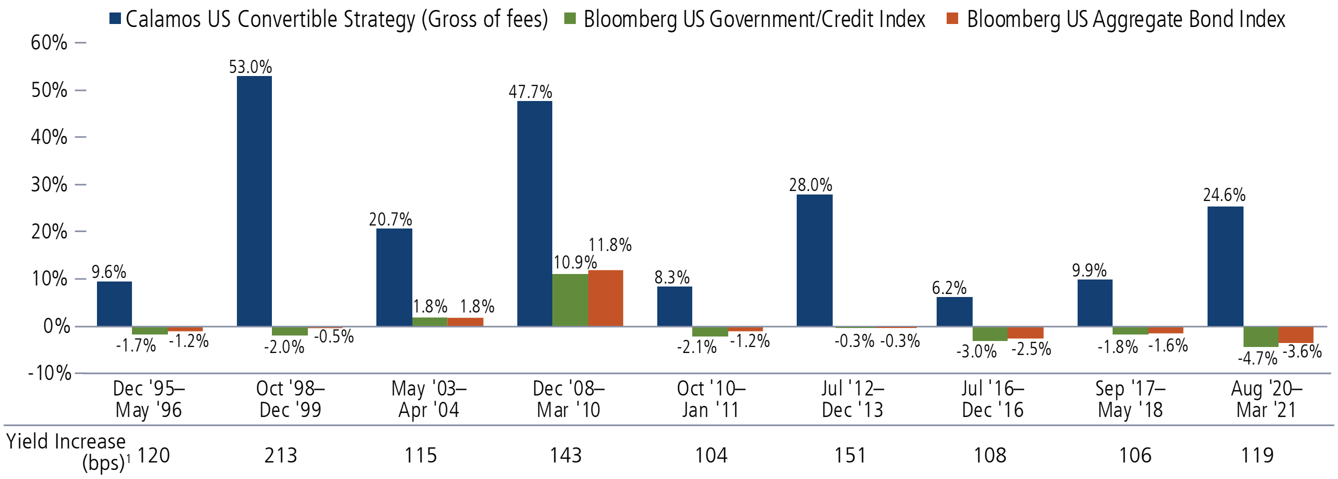


FIGURE 2. CALAMOS US CONVERTIBLE STRATEGY HAS DELIVERED EQUITY-LIKE RETURNS WITH LESS VOLATILITY

GROWTH OF $10 MILLION, 20 YEARS

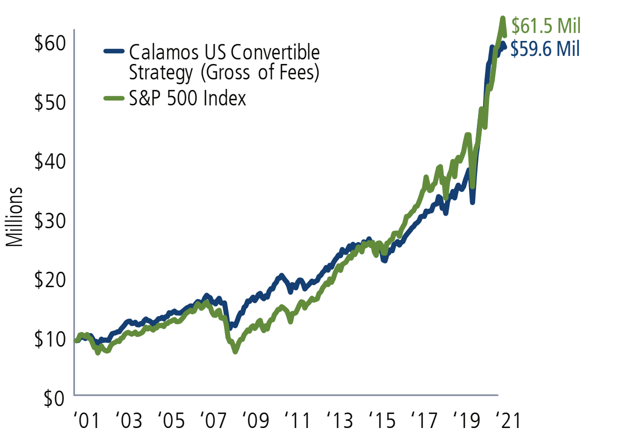
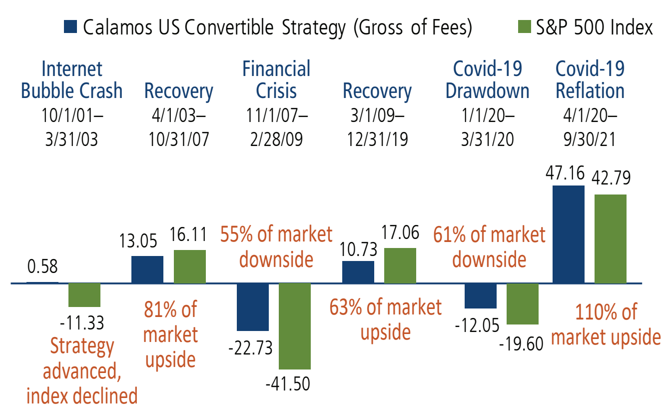


FIGURE 3. A HISTORY OF CAPTURING MORE MARKET UPSIDE THAN DOWNSIDE

RETURN (%)[2]



Past performance is no guarantee of future results. Current performance may be lower or higher than the performance quoted. For performance current to the most recent calendar quarter end, please see page 4.

Sources: Morningstar and Federal Reserve Bank of St. Louis. Indexes do not include fees or expenses and are not available for direct investment.

[1]Yield increase is represented by the 10-year Treasury yield. Rising-rate environment periods for full monthly periods from troughs to peaks from October 1993 to March 2021, based on the most recent data available as of September 30, 2021. [2]Net of fees returns: Internet bubble crash, -0.01%; 2003–2007 recovery, 12.38%; financial crisis, -23.18%; 2009–2019 recovery, 9.98%; Covid-19 drawdown, -12.22%; Covid-19 reflation, 46.12%. Returns for periods longer than 12 months are annualized.

Conclusion

Economic and market conditions can change quickly. Inflation and long-term rates can ramp up suddenly and with little warning, and the stock market can experience sudden downturns in the midst of rapid gains. **Actively managed convertible securities provide a proactive approach for addressing the challenges of inflation, rising rates and market volatility. The Calamos US Convertible Strategy exemplifies the opportunity of actively managed convertible securities over the long term.**

ABOUT THE AUTHOR

John P. Calamos, Sr.
Founder, Chairman and Global Chief Investment Officer

John P. Calamos, Sr. founded Calamos Investments in 1977. With origins as an institutional convertible bond manager, the firm has grown into a global asset management firm with major institutional and individual clients around the world. With more than 50 years of investment industry experience, John has established research and investment processes centered around a team-based approach designed to deliver superior risk-adjusted performance over full market cycles. John is recognized as a pioneer in using convertible securities to pursue a range of asset allocation goals.

John is often quoted as an authority on risk-managed investment strategies, markets and the economy, and he has authored two books on convertible securities. He is a frequent speaker at investment seminars and conferences around the world and appears regularly on leading news networks.

Prior to entering the investment industry, he served in the United States Air Force. During the Vietnam War, he served as a Forward Air Controller and was awarded the Distinguished Flying Cross. His Air Force career included five years of active duty flying B-52 bombers and twelve years in the Reserves flying A-37 jet fighters. He retired as a Major. He holds a B.A. in Economics and an M.B.A. in Finance, both from Illinois Tech.

ANNUALIZED TOTAL RETURNS (%), CALAMOS US CONVERTIBLE STRATEGY, AS OF 9/30/21

	1-YEAR	3-YEAR	5-YEAR	10-YEAR	15-YEAR	SINCE INCEPTION (1/91)
Gross of fees	23.77%	20.40%	17.37%	12.60%	9.59%	10.79%
Net of fees	22.89	19.55	16.55	11.82	8.86	10.10

Past performance does not guarantee or indicate 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.

The results portrayed on the preceding pages are for the Calamos Institutional Convertible Strategy. The inception dates and performance results shown are for the composite. Representative holdings and portfolio characteristics are specific only to the portfolio shown at that point in time. Other portfolios will vary in composition, characteristics, and will experience different investment results. The representative portfolio shown has been selected by the advisor based on account characteristics that the advisor feels accurately represents the investment strategy as a whole. Supplemental information has been provided for the Institutional Convertible Composite.

Returns and Risk/Reward statistics presented reflect the Calamos Institutional Convertible Composite, which is an actively managed convertible bond composite that invests primarily in high-quality US convertible bonds. The Composite was created March 1, 2014, calculated with an inception date of January 1, 1991. The Composite results include all fully discretionary Accounts, including those no longer with the Firm. Fees include the investment advisory fee charge by Calamos Advisors LLC. Returns greater than 12 months are annualized. Data Sources: Evestment Alliance and Calamos Advisors LLC. Average annual total return measures net investment income and capital gain or loss from portfolio investments as an annualized average assuming reinvestment of dividends and capital gains distributions.

The **S&P 500 Index** is a market-value weighted index consisting of 500 stocks chosen for market size, liquidity, and industry group representation. It is widely regarded as the standard for measuring U.S. stock-market performance. The **Bloomberg US Aggregate Bond Index** is a broad-based benchmark that measures the investment-grade, US dollar-denominated, fixed-rate taxable bond market of SEC registered securities. The **Bloomberg US Government/Credit Index** comprises long-term government and investment grade corporate debt securities and is generally considered representative of the performance of the broad US bond market. Unmanaged index returns assume reinvestment of any and all distributions and do not reflect any fees, expenses or sales charges. Investors cannot invest directly in an index.

Unlike convertible bonds, US Treasury bills are backed by the full faith and credit of the U.S. government and offer a guarantee as to the timely repayment of principal and interest.

The information in this report should not be considered a recommendation to purchase or sell any particular security. There is no assurance that any securities discussed herein will remain in an account's portfolio at the time you receive this report or that securities sold have not been repurchased. The securities discussed do not represent the account's entire portfolio and in the aggregate may represent only a small percentage of an account's portfolio holdings.

Calamos Advisors LLC is a federally registered investment advisor. Form ADV Part 2A, which provides background information about the firm and its business practices, is available upon written request to: Calamos Advisors LLC, 2020 Calamos Court, Naperville, IL 60563-2787 Attn: Compliance Officer.

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