

ACTIVE MANAGEMENT REACTS TO CHANGING RISK PROFILE

Ask  PORTFOLIO
MANAGER

Why is active management critical when investing in convertible securities?

Transcript of a video recorded on March 21, 2019

In the simplest form, a convertible is a traditional bond with an embedded call option on the equity.

Now, that's great, because you get the best of both worlds, in that you get principal protection on the downside, plus a stream of income, as well as you have an equity option on the equity, so you can get capital appreciation should the equity perform well. In theory, that sounds great, but in reality, what happens is the markets are dynamic, and the profile of that convertible changes daily, weekly, quarterly, depending on how the equity and credit markets change. We think that it's very important to actively monitor and manage those risks throughout the life of the convertible bond.

For example, when you have a strong equity market, it is not uncommon for the convertibles to participate with the equity market and have a high degree of participation. But that does leave one exposed to significant downside risks that you may not have with a balanced convertible. What we think is the true benefit to the asset class over full market cycles is to be able to monitor the risks, actively manage those risks, and create a portfolio that has the optimal risk/reward throughout the full market cycles.



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Video recorded 3/21/19.

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Convertible Securities Risk: The value of a convertible security is influenced by changes in interest rates, with investment value declining as interest rates increase and increasing as interest rates decline. The credit standing of the issuer and other factors also, may have an effect on the convertible security's investment value.

Convertible Arbitrage Risk: If the market price of the underlying common stock increases above the conversion price on a convertible security, the price of the convertible security will increase. The fund's increased liability on any outstanding short position would, in whole or in part, reduce this gain.

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