Five Things to Know About Interval Funds

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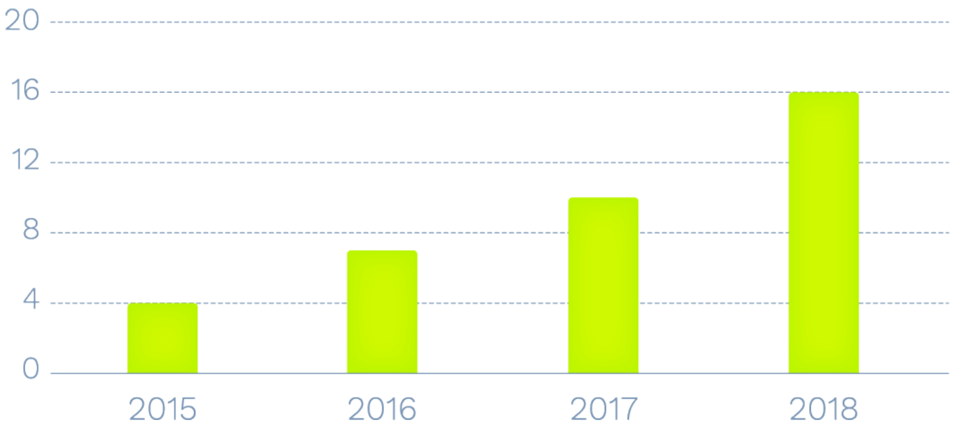
Interval Funds have been proliferating as the number of launches scales up and assets under management grow. While these funds are very attractive to their traditional investors – sophisticated institutions and pension funds– growth is also being driven by individual retail investors who are attracted by the features of these funds.

WHAT ARE THEY?

Interval funds aren't a strategy – they're a structure. It's just a way to describe a type of closed-end fund that continuously offers new shares for sale, but buys back existing shares only during specified periods, or intervals. Why is that important? Because by limiting liquidity, a manager may be able to deploy strategies that require long-term investments. Because the structures are registered 1940 act funds, they can be offered to individual investors without the burden of high minimums and net worth requirements.

Growth in Interval Fund Launches, 2015-2018



Source: Interval Funds Tracker, based on SEC data

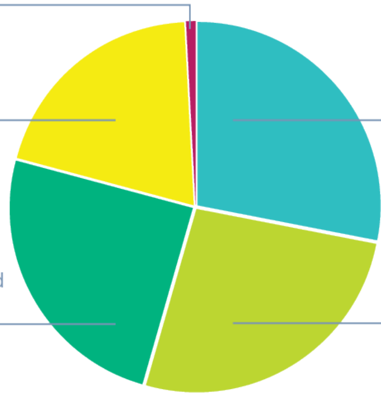
WHY DO INVESTORS WANT THEM?

The short answer – because liquidity is one of the levers of yield, like duration or credit quality. If you are willing to accept illiquid strategies as a trade-off, you can potentially accrue an illiquidity premium[1] – greater yield.

The long answer is that macro conditions have been combining to create a democratization of investing similar to the growth of mutual funds in the 1980s. Coming out of the Global Financial Crisis and over the last 10 years, keeping borrowing rates very low has resulted in low bond yields, leaving investors searching for yield. At the same time, banks went through a period of consolidation that left a funding gap for middle market businesses and real estate developers.

These two situations resulted in the growth of highly specialized credit and real estate investors that dedicate their strategies to private credits and direct real estate investments, both of which require long-term investments, but also both of which potentially can reward the illiquidity with additional yield.

Incentive Fee Split Above Hurdle Rate



Source: Interval Funds Tracker, based on SEC data

Institutional investors who have long-term time horizons have been aggressive investors in these types of alternative investments. By employing the interval fund structure, individual retail investors are now able to invest in the same illiquid strategies as institutional investors.

DO THEY OFFER ANYTHING ELSE?

Yes! Because interval funds are not traded on any exchanges, they are less correlated to most other stock and bond investments. This can help smooth volatility in a portfolio. Also, they can be an effective portfolio diversifier, as managers may seek underlying assets across credit qualities and geographies to place in the fund.

There are structural features as well. As noted above, investment minimums are low and accessible to individual investors – and on the other side, tax reporting on distributions is simple and done by 1099.

ARE THERE OTHER CONSIDERATIONS?

Because interval funds offer only periodic liquidity – usually at 3, 6, 9 or 12 months – investors must be mindful that their investment dollars will not be available to them in the way an exchange traded stock or bond investment may be.

WHAT ARE THOSE RISKS YOU MENTIONED?

In general, the risk specific to the structure of interval funds is that they lack daily liquidity and can expose investors to liquidity risk. Each fund will also have specific strategy risks, depending on what they invest in. These risks are outlined in the prospectus and should be read carefully.

To learn more about interval funds, please contact your financial professional.

[1] The Wall Street Journal. Simon Constable, What is 'Illiquidity Premium?' 10/7/16