

Five Things to Know About Interval Funds

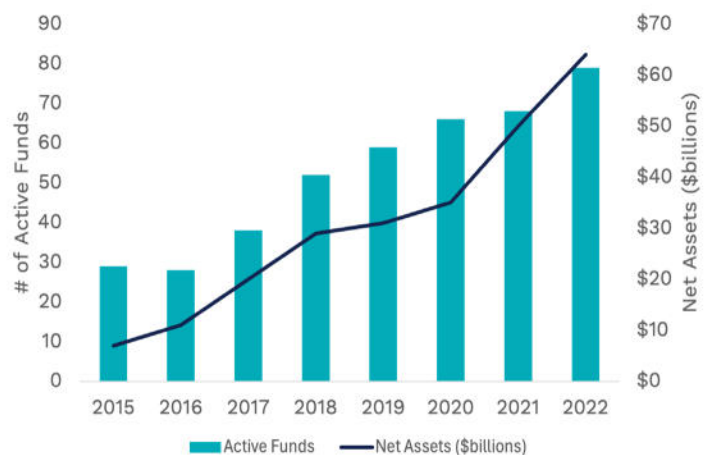


Interval Funds have been proliferating as the number of launches scales up and assets under management grow. While these funds are attractive to their traditional investors – sophisticated institutions and pension funds – growth is also being driven by individual retail investors who are attracted by the features of these funds. We break down what you need to know into five easy pieces.

What Are Interval Funds?

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, 2015-2022



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 premium¹ – or potentially 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. Investors are seeking portfolio diversification to help lower portfolio volatility, as well as income. At the same time, alternative investment strategies that have long been used by institutions, such as private credit, have seen growth as bank consolidation has resulted in a funding gap for middle market companies.

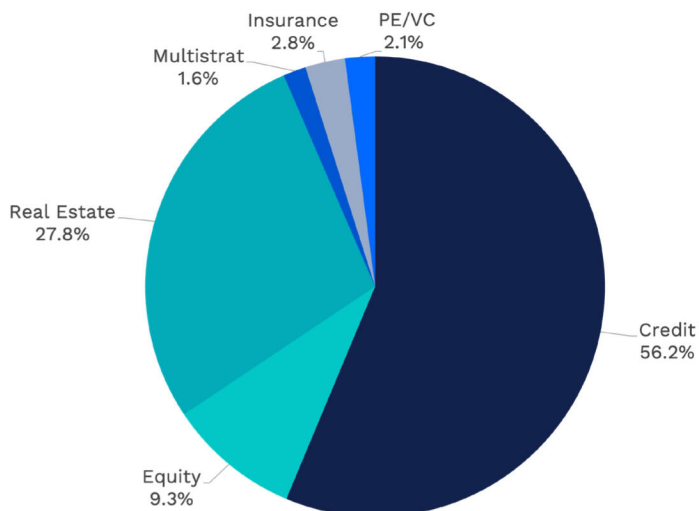
These two situations resulted in the growth of highly specialized credit and real estate investors that dedicate their strategies to private credit and direct real estate investments, both of which typically require longer-term holding periods, but which potentially can reward the illiquidity with additional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

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 can be relatively low and accessible to individual investors – and on the other side, tax reporting on distributions is simple and done by 1099.

Interval Fund Net Assets by Category



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.

Are There Other Considerations?

Because interval funds offer limited 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 same way an exchange traded stock or bond investment may be.

Interval funds can be purchased like open-ended mutual funds. They do not trade on the secondary market and only allow investors to redeem shares periodically in limited quantities, which means that they are mostly illiquid and have restricted selling opportunities.

¹The Economist. What is the illiquidity premium? 11/9/2019

What Are Those Risks You Mentioned?

One of the risks 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 capital, market and strategy risks, depending on the underlying fund assets. They can be affected by economic downturns, interest rate changes, credit quality, and other factors that can reduce their value and performance.

They can also have higher fees than traditional mutual funds, which can erode their returns and reduce net asset value (NAV) of the fund and the amount of money available for repurchase. Therefore, interval funds are best suited for investors who have a long-term horizon, a high risk tolerance, and a diversified portfolio. These risks are outlined in the prospectus and should be read carefully.

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

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