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CLOSED END FUNDS (CEFs)

DISCLAIMER - I am not a Financial Advisor and do not work for any Brokerage Firm. The opinions given are my own and are not to be used as professional advice. These are my findings and can hopefully help you make informed investing decisions. Consult a Broker or Lawyer before making any investment.

I want to discuss a type of investment that many are unfamiliar with in the investing industry. These are called CEFs or Closed-End Funds.

Closed end funds are mutual funds that have a set amount of shares. The amount is set at the funds IPO and can only be changed by a management decision. Normal mutual funds can sell more shares, but not CEFs.

Closed-end Funds are basically like a mutual fund but they can not sell additional shares. Since these funds are fixed, they sell initially at Net Asset Value. (NAV) So in the market, these sell for more or less of their value. If the price is more than NAV, they are selling at a Premium. (like +2.1%) Since these are managed, when selling at a Premium it may be due to the excellent management. You have to pay for quality funds. A quality fund that normally is above premium of NAV is PIMCO Dynamic Income fund (PCI). I own shares of this CEF.

Where the most money can be made is when they are selling at a discount to NAV. I purchased one today which is a healthcare REIT that is selling at -8.45 to NAV with an annualized return of 6.71%. The one mentioned is THQ - Tekla Healthcare Opportunities Fund. Prices fluctuate all the time, so sometimes some really good prices are there for the taking. It should be noted that CEFs many times do not perform well in periods of fluctuating interest rates like we experienced in 2022.

Here is a complete rundown from the Fidelity website that does a good job in explaining CEFs.

[What is a closed-end fund?](#)

A closed-end fund holds an IPO at launch and the money raised from that IPO is used by portfolio managers to buy securities.



Even though they have been traded in the US for over a century, closed-end funds (CEFs) are not well understood. A common misunderstanding is that a CEF is a type of traditional mutual fund or an exchange-traded fund (ETF). **A closed-end fund is *not* a traditional mutual fund that is closed to new investors.**

At its most fundamental level, a CEF is an investment structure (not an asset class), organized under the regulations of the Investment Company Act of 1940. A CEF is a type of investment company whose shares are traded on the open market, like a stock or an ETF.

Why are they called "closed-end" funds?

Like a traditional mutual fund, a CEF invests in a portfolio of securities and is managed, typically, by an investment management firm. But unlike mutual funds, CEFs are closed in the sense that capital does not regularly flow into them when investors buy shares, and it does not flow out when investors sell shares. After the initial public offering (IPO), shares are not traded directly with the sponsoring fund family, as is the case with open-end mutual funds.

Instead, shares are traded on an exchange, typically, and other market participants act as the corresponding buyers or sellers. The fund itself does not issue or redeem shares daily. Like stocks, CEFs hold an initial public offering at their launch. With the capital raised during this IPO, the portfolio managers then buy securities befitting the fund's investment strategy.

After the IPO, there are only 5 ways to increase capital within the portfolio

1. Making sound investment choices that appreciate and thus increase the net asset value
2. Issuing debt, thereby leveraging the fund
3. Issuing preferred shares, thereby leveraging the fund
4. Conducting a secondary share offering (selling new shares to the public)

5. Conducting a rights offering (giving existing shareholders the right to invest more capital into the fund in proportion to their existing ownership)

Similarly, there are only 5 ways capital can flow out of a CEF

1. Distributions to shareholders
2. Poor investment decisions
3. A tender offer to repurchase shares, which is a method to control discounts
4. For leveraged funds only, forced sales to remain in compliance of leverage limits
5. The liquidation of the fund

So, because capital does not flow freely into and out of CEFs, they are referred to as "closed-end" funds.

The "closed-end" structure gives rise to discounts and premiums. After the IPO, a CEF's shares trade on the open market, typically on an exchange, and the market itself determines the share price. The result is that the share price typically does not match the net asset value of the fund's underlying holdings. (Net asset value = (fund assets - fund liabilities)/shares outstanding)

If the share price is higher than the net asset value, shares are said to be trading at a "premium." This is typically portrayed as a "positive discount," although mathematically that is counterintuitive. For instance, a fund trading at a 2% premium would be shown as "+2%." If the share price is less than the net asset value, the shares are said to be trading at a "discount." This is typically portrayed with a minus sign, "-2%."

The closed-end structure also has other implications

- Unlike with open-end mutual funds, a closed-end fund manager does not face reinvestment risk from daily share issuance.

- A closed-end fund manager does not have to hold excess cash to meet redemptions.
- Because there is no need to raise cash quickly to meet unexpected redemptions, the capital is considered to be more stable than in open-end funds. It is a stable capital base.

The relatively stable capital base, in turn, gives rise to 2 other attributes: First, it makes CEFs a good structure for investing in illiquid securities, such as emerging-markets stocks, municipal bonds, etc. The higher risk involved with investing in illiquid securities could translate into higher returns to shareholders.

Second, regulators allow the funds to issue debt and preferred shares, with strict limits on leverage. The fund can issue debt in an amount up to 50% of its net assets. Another way to look at this is that for every \$1 of debt, the fund must have \$3 of assets (including the assets from the debt). This is commonly referred to as a 33% leverage limit.

The fund can issue preferred shares in an amount up to 100% of its net assets. Another way to look at this is that for every \$1 of preferred shares issued, the fund must have \$2 of assets (including the assets from the preferred shares). This is commonly referred to as a 50% leverage limit.

The point is that CEFs are not highly leveraged, though any amount of leverage magnifies the volatility of the fund's net asset value.

Key takeaways

- Closed-end funds are a type of investment company whose shares are traded in the open market like a stock or ETF
- Capital does not flow into or out of the funds when shareholders buy or sell shares
- Like stocks, shares are traded on the open market
- A CEF's share price is almost always different from its net asset value
- Investors need to be aware of the resulting premium or discount
- Because of the stable asset base, CEFs can invest in illiquid securities and can issue debt and/or preferred shares

[Link to Fidelity Research on CEFs.](#)

Here is an example of CEF Screener using a discount of -8 or less to NAV for one month and -7 for the year and up at least .5 for today. This list is for example only, each investment has to be analyzed on all merits, not just the discount to NAV.

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Closed End Fund* Screener

[Saved Screens](#) | [Quick Screens](#) | [Expert Screens](#) | [Print](#) | [How to use Screener](#) | [Criteria Definitions](#)

Important information you should know about investing in closed end funds.

[Screening Criteria: Unsaved Screen](#) | [Save Screen](#) | [Rerun Last Screen](#) | [Enable Score Weighting](#) | [Clear Criteria](#)

Criteria	Value	Benchmark	Results	Delete
Premium/Discount (1 Month Average)	Is less than or equal to -8	Market median is -7.35%	197	
Premium/Discount (1 Year Average)	Is less than or equal to -7	Market median is -6.47%	206	
Market Price Performance (Today)	Is greater than or equal to .5	Market median is 0.88%	43	

Type Criteria Here or: [Select Criteria](#) | Select a Value

Total Results: 16

Total results meeting all criteria : 16 AS OF 3:48 pm ET 01/05/23

Default View (criteria) | [Edit View](#) | [Save View](#) | [Download](#)

Quotes delayed at least 15 minutes

[Don't see a security you expected?](#)

Action	Score [†]	CEF Name	Symbol	Leveraged	Premium/Discount (1 Month Average)	Premium/Discount (1 Year Average)	Market Price Performance (Today)
<input type="checkbox"/>	100	FIRST TRUST ENERGY INFRASTRUCTURE FUND	FIF	No	-15.00%	-13.88%	+2.95%
<input type="checkbox"/>	100	MORGAN STANLEY CHINA A SHARE FUND	CAF	No	-15.12%	-14.55%	+2.02%
<input type="checkbox"/>	100	RIVERNORTH MANAGED DURATION MUNICIPAL INCOME FUND II, INC	RMMZ	No	-10.84%	-7.00%	+1.42%
<input type="checkbox"/>	99	ARROWMARK FINANCIAL CORP	BANX	No	-17.23%	-7.82%	+1.31%
<input type="checkbox"/>	98	ADAMS NATURAL RESOURCES FUND	PEO	Yes	-15.44%	-13.70%	+1.30%
<input type="checkbox"/>	97	MASSMUTUAL PARTICIPATION INVESTORS	MPV	No	-14.54%	-14.32%	+1.05%
<input type="checkbox"/>	96	CHINA FUND, INC.	CHN	No	-13.57%	-11.97%	+0.93%
<input type="checkbox"/>	95	PIMCO ENERGY & TACTICAL CREDIT OPPS	NRGX	No	-18.14%	-16.21%	+0.82%
<input type="checkbox"/>	95	NEUBERGER BERMAN NEW YORK MUNICIPAL FUND	NBO	No	-10.71%	-11.77%	+0.79%
<input type="checkbox"/>	95	MEXICO EQUITY & INCOME FUND	MXE	No	-24.86%	-22.88%	+0.79%
<input type="checkbox"/>	94	BLACKROCK ENERGY & RESOURCES TRUST	BGR	No	-10.42%	-11.32%	+0.75%
<input type="checkbox"/>	93	PIONEER MUNICIPAL HIGH INCOME OPPORTUNITIES FUND INC.	MIO	No	-9.33%	-10.66%	+0.65%

So in summary, I believe that Closed-End Funds are great for income and some experience growth in value based on their underlying investments, particularly those tied to REITs.

They typically will move back to their NAV over time which means you can make some good money by buying them when they are at a discount to NAV. Be sure to analyze the fund before purchasing. No one thing such as a discount to NAV means it is a super investment.

List of All Investment Articles <https://lifecanbesimple.net/investments.html>

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