Seeking Alpha α

Interview With Phil Goldstein And Andrew Dakos Of Bulldog Investors, Part 1

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by: Mark Gottlieb

Summary

- Bulldog Investors has enjoyed equity like returns with lower risk over the past quarter century. They averaged a return of 11.2% per year and absent are drops during market swoons.
- How do these transactional activists achieve this? Read on to find out.
- And learn all about SPACs from the masters of the SPAC universe in part 2. SPACs are low risk and for income with an equity kicker.

Phil Goldstein

Andrew Dakos

Yesterday I ventured 15 minutes from my home to Saddle Brook, NJ to meet with Phil Goldstein, Bulldog Investors Principal, Co-Founder, and Portfolio Manager and Andrew Dakos, Bulldog Investors Principal and Portfolio Manager. They were generous with their time speaking with me for 2 hours. Phil has coined the phrase ‘transactional activist’ to describe what he does. It seemed like a great time to meet with this dynamic duo considering U.S. stocks have had a historic run in terms of price and duration. Also, missteps from the Trump Administration on the trade front which thus far have been supportive to the U.S. dollar and U.S. equities vs. their foreign counterparts, could ultimately could lead to much lower U.S. stock prices which in turn could lead foreign stock prices even lower. iShares MSCI Emerging Markets ETF (EEM) is already off nearly

11% YTD while the S&P 500 is up nearly 8% thanks largely to tech and FANG stocks. Bonds could also remain on the defensive if inflation rears its ugly head thanks to trade front issues and further tightening by the Fed.

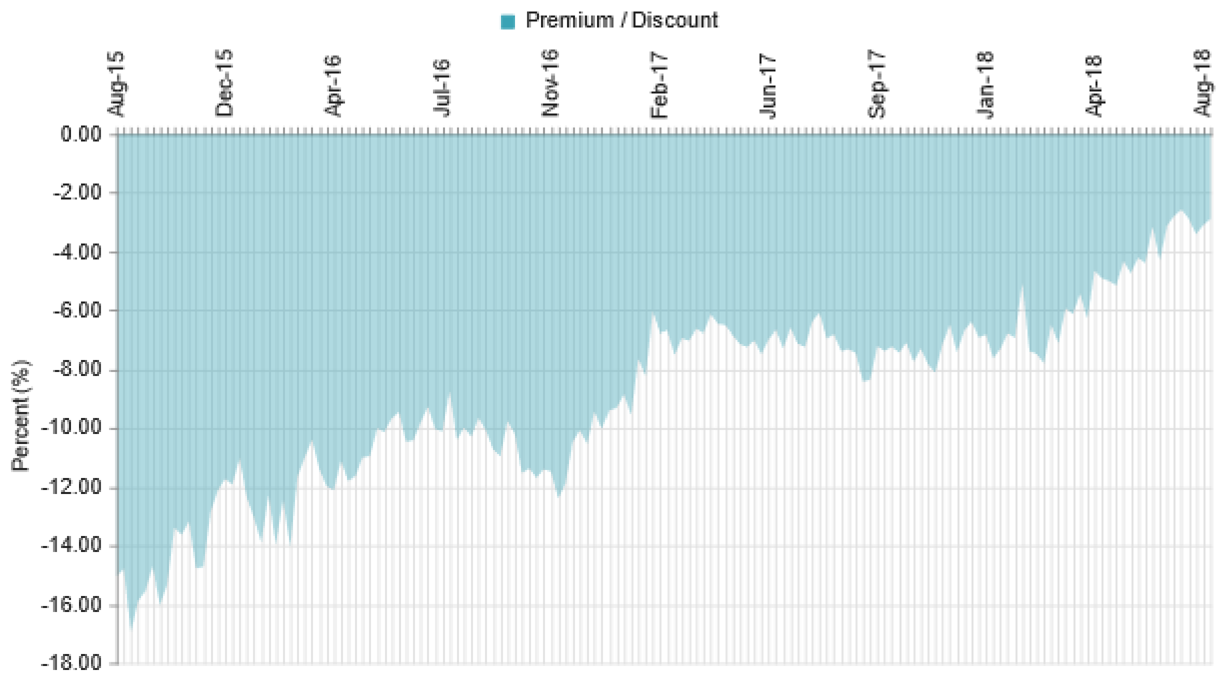
While the rest of the world often panics during market meltdowns and turbulence, Bulldog Investors scoops up investments from bargain bins such as SPACS even the most seasoned investors are often unaware of. Whatever they are doing must be working. They now have approximately $490 million under management with top holdings in diverse often hated areas of the markets (e.g. China equities). Their niche is to buy closed-end funds on the cheap (large discount to net asset value) and use their transactional activism to reduce or eliminate the discount to net asset value on closed-end funds.

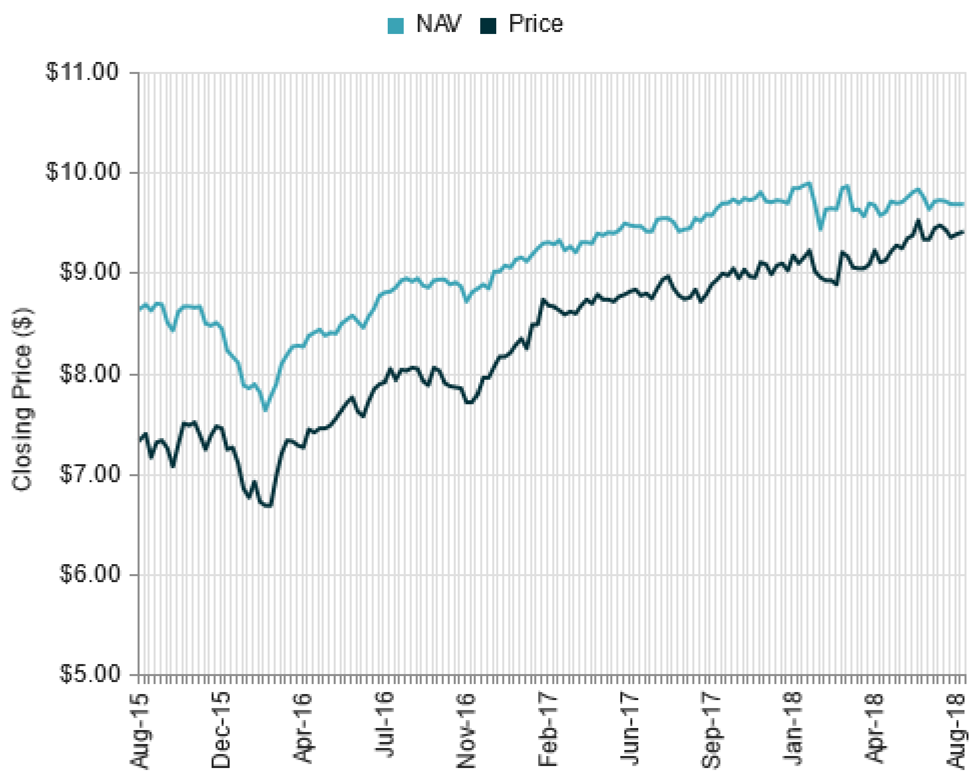
Since inception of the Bulldog Investors original hedge fund 25 years ago, investors have enjoyed equity like returns with lower risk. Phil said they have averaged a return of 11.2% vs. 9.5% for the S&P 500 during this timeframe. Most importantly, from 2000-2002 they had their best market outperformance (+5% vs. -22% for the S&P 500) and in 2008 they had what was likely the only long only equity fund that was positive (by 2%) – it was invested solely in SPACs -- while the S&P 500 was down 37%. They typically lag performance wise when growth is in favor such as now and leading up to the 2000 market debacle, but they more than make up for it during major market swoons.

Phil wasn't always a market maven. He started off as a civil engineer, a civil servant for the city of New York. The work came easy to him but he wasn't passionate about it; there was no incentive to do better. Back in 1974, he read his first financial book, The Money Game by Adam Smith, and became interested in closed-end funds. He did well with his private investing largely in closed-end funds and went to a closed-end fund conference in 1989. Phil was an activist them as now; back then he would write letters to the editor to major newspapers on political and legal topics. Phil had a letter to the editor published in Barron's back in 1992 which led him to Steve Samuels, an entrepreneurial money manager back then and ultimately a Bulldog Investors Principal and Co-Founder. Steve asked Phil if he ever considered managing money. Steve was the rainmaker and began to get Phil clients and Phil kept his civil service job while working on investment management out of his Brooklyn home basement until late at night. Steve said let's start a hedge fund in 12/92 which Phil knew nothing about. They started with $700,000 in assets (1/2 family money) and grew to $3 million under management by the end of 1993. They did mostly closed-end funds and some risk arbitrage with rights offerings.

Bulldog Investors targets high net worth investors. They offer hedge funds and SMAs focused on SPACs and income-oriented closed-end funds. While many SMAs often have minimums of $500,000 to $1 million, theirs is just $100,000 for SPAC SMAs ($200,000 on their other SMA strategies) and they take a modest 1% for all their knowledge and hard work of finding the best investment options that meet their risk tolerance of clients looking for income. They have a $250,000 minimum for investments in their private funds. They also manage the Special Opportunities Fund (SPE) which is up a modest 1% at NAV in 2018 but is up about 6% per annum at NAV over the past 5 years. I like to consider it a hedge fund for the little guy investor. Back in 2009, Bulldog Investors ended up ousting the board of the Insured Municipal Income Fund and replacing it with its own team. It changed the name of the fund to Special Opportunities Fund (SPE). While it is not a clone of the main hedge fund, it does hold many of the same positions. SPE uses leverage while managed accounts do not. The separately managed account assets are held by Charles Schwab and Co. (SCHW) which was instrumental in getting the minimum down to $100,000 for SPAC SMAs. Bulldog Investors invests a lot in SPACS which are low risk and for income with an equity kicker. I will focus on them in part two of this article.

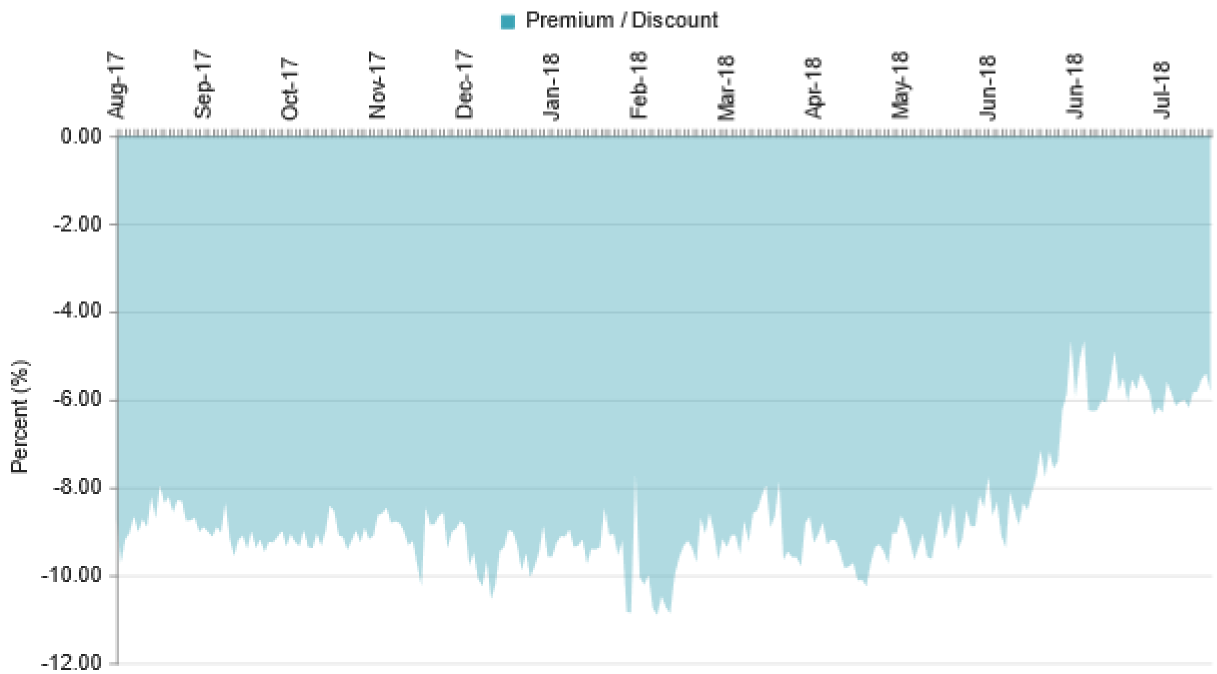
I asked Phil for some recent examples where his transactional activism paid off. High Income Securities Fund (PCF) was trading at a discount as high as 16%+ back in 2015. It is currently at a 2% discount and has been very profitable for investors of this closed-end fund who bought at a deep discount, especially Bulldog Investors/Special Opportunities Fund investors. Bulldog gained control of the board of this closed-end fund a few months ago and Putnam resigned as manager. The portfolio was liquidated all in cash with at least 55% of the shares to receive 99% of net asset value on a self-tender and what is left is run as a holding company. Last year Bulldog Investors lost a proxy fight against this closed-end fund but like a Pitbull (or bulldog) with a bone they persevered, bought more shares and eventually won the proxy contest.





Above charts from cefconnect.com

Swiss Helvetia Fund (SWZ) is another recent example where the transactional activism of Bulldog Investors is paying off. Bulldog Investors won two SWZ seats last year and two more this year. The discount to net asset value pre-proxy fight was 9-10%, today it is under 6%. I wouldn't be surprised to see the discount drop further or get eliminated thanks to the transactional activism of Bulldog Investors.



Above chart from cefconnect.com

I asked Phil what does an activist look for? He said Bulldog Investors considers themselves value investors and they look for opportunities where they can narrow the discount gap. He told me a story about Blair Corporation, one of the largest direct marketing mail order retailers. Bulldog once went after them because the team uncovered assets not valued in the stock. They issued their own credit to customers instead of taking credit card transactions. The value of the receivables from the credit alone equaled the stock price. Phil and Andy met with Blair's managers and convinced them to sell the receivables from the credit facility to a credit card company which was done at over their value. The stock went up as a result and there was a self-tender offer which was very profitable.

Bulldog Investors looks for solid companies that are hard to blow up. He has great trust in the closed-end fund valuations of the Blackrocks, Nuveens, and Putnams of this world and Bulldog Investors does what it takes to narrow the gap in closed-end funds trading at a wide discount. He considers some BDCs overvalued at this time but thinks others are undervalued. The hard part is getting comfortable with the valuations.

We discussed Bulldog's influence over management. If management resists Bulldog Investors activism, they may seek to win a proxy fight. Before they decide on a discounted closed-end fund to take position in that could benefit from their transactional activism, they look at the shareholder base. They have good rapport with other value investors such as Saba Capital who generally support each other and with large non-activist investors. This can lead to shareholders voting for a closed-end fund to go open-end. Closed end fund managers often will negotiate a deal since closed-end fund management can see the writing on the wall and headline risk with Bulldog Investors activism.

I asked if other closed-end fund groups such as Blackrock (BLK) would follow in the footsteps of Eaton Vance whose Eaton Vance NJ Municipal Income Fund (EVJ) I own rose about 5% since the announcement on 7/26 that shares of EVJ would be exchanged for shares of the Eaton Vance Municipal Income Fund (EVN) at the then discount to NAV of EVN. EVJ prior to this announcement was trading at a discount to NAV of almost 17%. EVN is trading at a discount to NAV of 8.97% which if it holds steady when the deal is done would mean an 8% smaller discount for EVJ shareholders. I brought up BlackRock Muni Holdings NJ Quality Fund (MUJ) and Blackrock Muni Yield New Jersey Fund (MYJ) holdings which I own and are selling at a historically high 13 and 15% discount to net asset value. He said Blackrock cares about its reputation, talks good governance, and Bulldog Investors may get involved with Blackrock in the future. He said the managers of closed-end funds often do nothing if shareholders don't nag them. The Chairman of the Board of Blackrock closed-end funds is to get back to me shortly regarding my suggestions for narrowing the discount to net asset value on MYJ, MUJ, etc. Read all about my SeekingAlpha article on Suggestions For Blackrock After Discussion With Chairman Back to the subject of Eaton Vance, they are continuing with their shareholder friendly actions with their closed end funds, see here and here. All in all, since June 1, they have announced the proposed merger or tender offer of 28% of their 40 closed-end funds and 40% of their 20 municipal bond closed-end funds. They also authorized the redemption of all 16 outstanding institutional MuniFund Term Preferred (IMTP) Shares during the same timeframe. Blackrock had 0 shareholder friendly actions with their closed-end funds during the same timeframe.

We discussed if closed-end fund managers should take responsibility for large discounts to net asset value. Some, such as the manager of Central Securities Corp. (CET) have publicly said they should not, the manager's belief is investors should invest for the long-term so the discount does not matter much. The manager's belief is it only matters if you have to sell it. I wondered why isn't CET an even larger position for Bulldog Investors/Special Opportunities Fund with a 17+% discount I figured they could get narrowed quite a bit. Phil and Andy said Plymouth Rock is its largest position which according to Morningstar is 19% of assets. According to George Spritzer in SeekingAlpha in a June 2018 article, its Plymouth Rock assets could be worth far more and privately owned Plymouth Rock is like a mini Berkshire Hathaway (BRK.B). Andy spoke about CET selling back shares of Plymouth Rock to the company in the past consistent with fair value. He said Plymouth Rock is a great business and it owns valuable real estate including Boston real estate that is likely on the books below its true value. CET invested $700,000 in Plymouth Rock in 1980 and the shares they still hold are conservatively valued at $159 Million. With such a small cost basis, if Plymouth Rock shares are sold they would have to distribute virtually all the gains as a special or year-end dividend. If enough is sold, it would be very profitable for shareholders. Hopefully it will all be sold one day. A charitable trust controlled by CET's manager's wife owns over 30% of its shares so you can't get board control to maximize the value of CET shares. It sounds as if the charitable trust donates shares of CET to colleges, etc. who likely sell the shares to fund programs and thus, contrary to the manager's belief, would not be long-term shareholders. The CET discount is partially due to the illiquidity of CET shares but mostly to the large position owned by the charitable trust.

I asked Phil which investment managers does he admire the most? He mentioned Jeff Smith and Carl Icahn. He said investors pay management fees for good decisions and he is pleased with his good risk adjusted returns.

A lesson Phil learned was when he sold 6,000 shares of a closed-end fund short before he became a professional investor. The closed-end fund shot up like a rocket one day while the NAV barely budged. His account was upside down and he lost more money that day than he earned in a year at that time. One of his favorite business quotes is from John Maynard Keynes is "The Market Can Remain Irrational Longer Than You Can Remain Solvent." His lesson was living proof of this and so are the PIMCO closed end funds that have sometimes reached premiums of 100% or more.

Phil said he has had a good run in his 23 years of activism but he modestly said he still can't keep up with the return of the Amazons of this world. Then again, when Amazon (AMZN) stock dropped from about $63 a share in 6/99 to $5.97 a share in 9/01, Bulldog Investors was enjoying its best period of outperformance while tech stocks were being thrown to the curb. Will history repeat? They say it does not repeat itself but it rhymes. Will Bulldog Investors ever convert some of the tremendously undervalued municipal closed-end funds if they gain control of them into something such as a Special Opportunities Fund II like the way Special Opportunities Fund began? One never knows but I believe Bulldog Investors expertise is like money in a rock sold FDIC insured U.S.A. bank.

Disclosure: I am/we are long EVJ, MUJ, AND MYJ.

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