



## The Case for Convertible Opportunity and a V-Shaped Recovery

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As anxiety about the coronavirus has pummeled the global markets and economy, we've been having many conversations with our clients about what is likely to happen next—and the investment strategies that make the most sense. **What we're seeing now reminds me of the 1987 crash, and I believe conditions point to a V-shaped recovery**, supported by monetary and fiscal policy. Many securities have been oversold, which creates opportunities for long-term investors.

**Because the tide could turn quickly and suddenly, trying to time the markets is exceedingly ill-advised.** However, given the uncertainty of the Covid-19 pandemic—as well as the U.S. election cycle—risk management is crucial. This is an environment where convertible securities are extremely compelling.

### Why a V-shaped recovery?

Let's take a closer look at the case for a V-shaped recovery, starting with the similarities between now and 1987. Back then, the economy was doing well, boosted by Reaganomics, and this stronger economic backdrop helped the market regain its footing in relatively short order. In other words, conditions were far different than what we saw in 2008, where we had a deep financial crisis. Right now, we have a health crisis creating headwinds for an economy that has been very strong up until just a few weeks ago. **I believe the massive fiscal stimulus package making its way through Congress, combined with Fed actions, will be instrumental in helping the U.S. economy withstand the health crisis of Covid-19.**

The U.S. economy's trajectory can be sped along by biotechnology innovations (which will support coronavirus containment efforts) and technology innovations (which have allowed many businesses to maintain operations amid shelter-in-place and social distancing orders). I'm also encouraged by how the private sector is stepping in—for example, auto companies switching their manufacturing operations to produce health care equipment.

### Why convertible securities?

Convertible securities combine attributes of stocks and bonds. With active management, these hybrid attributes can provide the opportunity for upside equity participation and the potential for risk mitigation during periods of volatility.

My appreciation for the convertible security dates back to the founding of the firm. When I first got into the business in the early 1970s, it wasn't long before the equity market corrected substantially. Then, it seemed like every 18 months or so, we had an up and down cycle. It was clear that these were markets that required more than good luck. The other thing that was very apparent was that trying to time these markets would be very difficult, even impossible. So, we developed strategies that didn't rely on luck. We focused on making sure we were managing risk over market cycles, which is what led us to convertibles.

Through the years, we've developed many strategies that exploit this versatile asset class. For example, we use them in stand-alone convertible strategies, in strategies that blend stocks and convertibles, as well as in liquid alternative strategies, such as our market neutral income approach.

## Conditions in the Convertible Market Signal Opportunity

The convertible market continues to provide access to many attractive secular growth opportunities in technology, health care and consumer companies with healthy balance sheets, including manageable debt levels.

Right now, our teams see a backdrop that signals significant long-term opportunities. A combination of wide credit spreads, oversold equities, and a wide convertible valuation gap is unlikely to last. When one or more of these conditions reverse, many convertibles are likely to benefit.

Importantly, while convertible securities have sold off in recent weeks alongside other risk assets, the market has remained orderly. We are not seeing the same conditions as we did in the more chaotic environment of 2008, when liquidity seized up much more dramatically.

## Conclusion

Volatility creates opportunities for long-term investors, which means that now is not the time to move to the sidelines. With active management, convertibles provide a compelling way to invest through full market cycles. The selloff in risk assets has pushed the valuations of many convertibles to very attractive levels, especially given our belief that the markets and economy may see brighter days before many expect.

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