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1Q25 RiverNorth/DoubleLine Strategic Income Fund & RiverNorth DoubleLine Strategic Opportunity Fund, Inc. Audio Review Transcript

Chris Lakumb

All right. Well, Corey, let's start with you, if you'd like to provide an overview of what DoubleLine's seeing in the market and then also how your fixed income asset allocation committee is responding as such.

Corey Clermont

Yeah, of course. Thanks, Chris. Thanks for having me. So, I mean, really, in the second half of the first quarter, I mean, you think last week of February through today, April 17th, I mean, volatility began to pick up in both rates in the risk asset markets, equity markets, right? They sold off, credit spreads started to widen, led by high-yield corporates. And high-yield corporates, actually, through last Friday, spreads have widened 132 basis points year-to-date. Rates rallied into quarter end, which really kind of benefited those longer duration assets. And we talk about traditional fixed income a lot - think of things like Treasury, agency, mortgage-backed securities, and investment-grade corporate bond - these sectors all finished the quarter positive and really the best performers. And actually, if you zoom out a little bit, all sectors of the global public fixed income market finished the first quarter with positive performance. Now, just given where we stand today, hit or miss, we didn't discuss the first few weeks of April, right? As you know, volatility really ramped up around that Liberation Day, April 2nd. Credit spreads unsurprisingly widened, moved further out from there with the overall risk sentiment that we saw in the market. But parts of securitized market and particularly high-quality agency mortgage-backed securities appear to be a relative safe haven when compared to some of the uncertainty around corporate credit. And just with the current situation around tariff policy, it remains an extremely fluid and unpredictable situation from our standpoint. I mean, Chairman Powell alluded to it yesterday at a press conference, and he said that the policy could be at odds moving forward with inflation being on one end, potentially moving higher because of the tariffs, and then on the other end, maintaining maximum unemployment. And with the weakening economy, you could see some potential upticks in employment.

So, all in all, we're staying very vigilant, paying attention to the upcoming data and the ever-changing policy that seems to be coming down the pipeline every other week. So how we position portfolios within our fixed income asset allocation committee, we actually did make a top-down change in February. We decided to reduce our overall credit risk. Within the RiverNorth core sleeve, we allocated an additional 2% to both Treasuries and then another 2% to agency mortgage-backed securities. And that came out of our securitized credit sectors really across the board. And those were two main reasons. One, they're relatively expensive looking at the option-adjusted spread compared to the trailing 10 years. And secondly, it was just slowing economic data, and we thought it would be prudent to reduce some of our credit risk. And the timing worked out pretty well, as we started to see some of that weakness really materialize in the first week of March there. For the RiverNorth opportunistic income sleeve, similar move, similar reasons. We took down securitized really across the board, and we allocated 5% in total to agency mortgage-backed securities. So, with that, I will pass it back to you, Chris.

Chris Lakumb

Thanks, Corey. That's a good, succinct update around the markets as well as what your fixed income asset allocation committee is seeing. So, appreciate that. Steve, why don't we turn over to you if you'd like to provide an update on the closed-end fund space?

Sure. Thanks, Chris. Yeah. I mean, in the taxable closed-end fund space, similar to Corey's point about risk spreads, risk was a bid up for the first couple of months of the year, and you saw that playthrough in the closed-end fund market. I mean, interestingly, taxable closed-end funds had basically traded at NAV during the month of March. And so, it was about as rich as we've seen it in quite some time. Naturally, we had reduced exposure meaningfully across both RNSIX and OPP. And so, kind of going into the sell-off that began in April, we started off in a really good place. I'd say close-end fund investors that were discount-focused certainly would be underweight, again, at the end of March. And so, when the sell-off began, it presented opportunity. And I think quite a number of funds had two down 5 to 10 percent days back-to-back. It was a Friday and a Monday. That creates trading opportunities for us. I think the average discount basically gapped out from 0 to 7, bounced back a couple hundred basis points. And we're right around 3 or 4 percent discounts today. But that 3 or 4 percent probably shouldn't excite very many people. I mean, it's interesting in the velocity and the magnitude of the move. But from an absolute discount perspective, taxable bonds are still fairly narrow. I think the explanation for that is that investors are looking for high absolute yields, high yield and more credit-sensitive parts of the fixed income market, outside of closed-end funds, offer high absolute yields even with albeit narrow spreads. And then within the closed-end fund wrapper, you lever that and give investors more yield. That's kept demand pretty high. I mean, there is a lot of demand still for closed-end funds with kind of 9-plus percent yields.

Again, I think that that is an asset allocation call for investors. But from a discount perspective, not all that interesting even with the recent volatility. In contrast to the taxable closed-end fund side, municipals have remained out of favor. We also own municipal closed-end funds, specifically in RNSIX. And that market really hasn't recovered from the bear market that began in 2022. There was certainly a nice recovery for muni closed-end funds over the past 18 months. But muni sold off with other classic classes here in April, and it created, I'd say, a technical opportunity in the market where tax-exempt muni bonds were yielding more than Treasuries and comparable corporates in some cases. That was interesting from an asset class perspective. Again, that created volatility for munis. And again, unlike taxable closed-end funds that started off rich, I'd say munis started off April pretty cheap, and got exceptionally cheap, and remains so to this date. So again, sorry for popping around there. But two markets, taxable closed-end funds and munis, varying levels of attractiveness across the space.

Chris Lakumb: Thanks, Steve. That's helpful. Just one follow-up there. Maybe just as a recap or refresh, how you're thinking about allocating to muni closed-end funds within both OPP or RNSIX, knowing it's not necessarily a core holding, if you will.

Steve O'Neill: Sure. Well, let me touch on OPP first. Within the OPP portfolio, DoubleLine's managing the majority of the capital, and then within the RiverNorth sleeve, we've preferred to invest in Square small business loans and business development company debt, both short-duration, higher-income securities. What we haven't had in OPP is much closed-end fund exposure. So, we've had about less than 1% of the portfolio invested in closed-end funds. And so, in that portfolio, we don't own any munis. On the RNSIX portfolio, again, DoubleLine is managing about 70% of the portfolio. RiverNorth's managing about 30. We have had about half of our capital invested in closed-end funds. And then, again, about half of that or about 7 or 8 percent of our portfolio invested in muni closed-end funds. Certainly, that is not part of the, I would say, core or strategic asset allocation. That being said, when munis offer relative value compared to other parts of the high-quality, fixed income market, and then we also think that there's discount opportunities, we make investments there. And so, I'd say if you look back to RNSIX over the past 10 years, it's certainly atypical for us to own munis. But again, when we have a house view that the closed-end fund space looks attractive, and then specifically, if we have kind of the duration risk budget to take those trades within RNSIX, we like to do it.

Chris Lakumb: Thanks, Steve. That's helpful. Corey, back over to you. Any other top-down or bottom-up information you'd like to provide relative to the core or opportunistic income sleeves?

Corey Clermont: Yeah. I mean, I think it's just helpful to review performance quickly for the first quarter. I mean, obviously, things have kind of changed here over the first 12 trading days of the second quarter. But generally speaking, I mean, when looking at the RiverNorth core sleeve, slightly underperformed its bench with really all of that coming in March. And if you think about what unfolded in March, credit spreads started to widen, right? And the Ag, the index only owns about 20, 25 percent worth of credit, whereas the core sleeve owns a little bit more than that. And so, credit spreads widened is really regardless of credit quality or the asset class, and it was in line with the overall risk-off sentiment. But despite that, you had positive returns across all of the sectors within the core sleeve. Now, two things I do want to note that really helped out, things that we had been talking about is, first, our positioning from our Treasury exposure. We've had a steepener on for really about the last 12 months. We put it on back in February. And so, we've been overweight our duration exposure from the two-year part of the Treasury curve and pretty significantly underweight our exposure to the 30-year part of the curve. And the yield curve, it did steepen pretty significantly. And really, since we put on this trade, the difference between the 2-year and 30-year, which was negative 20 when we put on the trade, has flipped all the way to positive 90 here. So that Treasury positioning and where we're taking that duration exposure has definitely benefited.

And then lastly, kind of a theme that, again, we talked about for maybe almost going on 18 months now is just upgrading the underlying credit quality across all of our sleeves, which has benefited relative performance, right, as lower credit quality has seen larger spread widening. And then lastly, just a quick thought on the RiverNorth opportunistic income sleeve. It actually outperformed the Ag by roughly 50 basis points, although it does take on a little bit more credit risk there. And part of the reason it outperformed was due to our agency mortgage-backed security positioning, which really shined. It had a return, about 6% in the first quarter, nearly doubling the Bloomberg MBS index return. So, agency MBS was a big positive for the first quarter within the opportunistic income sleeve. And then, really, all sectors had positive performance outside of bank loans, which had some spread widening. So, I will stop there on the update of the two sleeves and pass back to you, Chris.

Chris Lakumb: Thanks, Corey. That's helpful. Steve, any other comments you'd like to make on our sleeves within the Funds or any top-down asset or sleeve allocation, if you will, across the funds?

Steve O'Neill: Yeah. Let's try to wrap it up a bit. Yeah. I mean, as we think about RNSIX, as Corey mentioned, the op-income portfolio outperformed the Barclays Ag. That was a positive. That's the largest part of the RNSIX portfolio. That's about 40%. Within the RiverNorth sleeve, we've had minimal exposure to closed-end funds, which has been positive, certainly, in light of recent volatility. We preferred to own BDC debt in RNSIX that has performed fairly well, even with a little bit of spread widening recently. And then the balance of the portfolio is within the core sleeve. I'll make note that year to date, we've had a little bit of redemption activity, certainly in April, and we've used the core sleeve to meet that. And so, as we think about positioning, we continue to like op-income, maintain that overweight. Within our sleeve, we've tried to be on offense, using this opportunity and the sell-off for closed-end funds to increase our exposure. There's been some really interesting tactical trading opportunities, and those continued today. Within the OPP portfolio or op-income, closed-end fund, that op-income by a DoubleLine is really unchanged. I would say there are no meaningful changes within our part of that portfolio. Again, we continue to reinvest in square loans and have looked at the weakness in BDC debt as an opportunity to add.

Chris Lakumb: Thanks, Steve. Corey, any final thoughts or outlook from your side?

Corey Clermont: Yeah. I guess I would just point to really kind of the first week of April and some of the trading that we saw there in rates. It's interesting to see what's been going on in the long end of the curve. It's something that Jeffrey and team have been talking about for quite a while now, which is some of the pressures on the long end that you don't necessarily see on the front end, one being the budget deficit and kind of the fiscal risk premium that we think is really underappreciated on that long end. And what you saw unfold in that first week when risk-- it seemed like the equity markets are down 5% every day. Treasuries are typically that safe haven asset where investors flock into, and you get a rate rally, and they have that negative correlation to the risk market. So, you have your price appreciation there in long-end Treasuries. And we saw that. It was a knee-jerk reaction. It lasted about a day or two. And then yields started to sell off pretty aggressively on the long end of the curve. And that's just an idea that we have been talking about internally in terms of how you're taking that interest rate risk and some of the potential problems that could arise in the long end of the curve if we do tip over into a recession. And if you do, you potentially get another knee-jerk reaction. But ultimately, in a recessionary type of environment, we know the playbook, fiscal spending goes up, the budget deficit gets even more out of whack than it currently is, and we're going to need to finance that debt. So, it's just an idea that we've been talking about. I think you saw a microcosm of that in the first week of April, and I just think it's something to keep an eye on. And it's ultimately reflected in how we're positioned within our Treasury sleeve, having a curve steepener on.

Chris Lakumb: Thanks, Corey. Steve, any final thoughts on your side?

Steve O'Neill: Yeah. I guess we would expect volatility to continue in the closed-end fund space. It's easy to say that. Most closed-end funds are meaningfully below their year-to-date high, and they're meaningfully above recent lows in April. It's interesting volatility. We're trading around kind of a narrower discount range. And so don't expect us to meaningfully increase closed-end fund exposure from here. But it is the type of opportunity where you can put capital to work quickly. There have been some exceptional opportunities. There continue to be a handful of those. But our hope would be that closed-end fund volatility continues in both the DoubleLine portfolios. We've got cash to put to work. We can rotate into closed-end funds. And I'd say kind of our risk budget to add closed-end funds would be very large if the opportunity presented itself.

Chris Lakumb: Thanks, Steve.

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