

LGI: One Of The Most Durable Machines In Our Income Factory

Jul. 12, 2021 10:55 PM ET | **Lazard Global Total Return&Income Fund (LGI)** | 20 Comments | 29 Likes

Summary

- LGI is one of the "workhorse" funds in our Inside the Income Factory model portfolios, generating 52% total return over the past year, and over 18% year-to-date.
- With a distribution policy of 7% of year-end NAV, we can already project another 8% increase in 6 months if it maintains its existing NAV.
- Anyone confident the fund won't backslide on its NAV over the remaining year can lock in a future yield of 7.3% by buying at current price levels.
- Obviously nothing is assured, but I would guess LGI is more likely to grow further this year than slip back.

- So I will probably pick up more of it myself this week.
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Andrii Yalanskyi/iStock via Getty Images

Lazard Global Total Return & Income Fund ([LGI](#)) is one of my favorite equity closed-end funds. I bought it as one of the 15 funds in our *Inside the Income Factory* "Hunker Down" portfolio that we launched a year ago, whose purpose was to be as solid and conservative as possible while still generating a serious income for those of us who couldn't afford the "safety" of riding out last year's uncertainty in low-yield/no-yield bonds and other low-return assets.

Since then, that portfolio has earned a total return of 44% for the 12 months, and LGI has contributed more than its fair share, with a total return on its market price of 52%, and a total return measured on its net asset value ("NAV") of just under 38%. The fact that its market value return has exceeded its NAV return means its price has gone up relative to its NAV; in other words, its discount has shrunk, from around -15% to the current -4%.

When I [last wrote about LGI](#) in December 2020, it was just about to review its distribution for the upcoming year, and based on its formula of paying out 7% of its year-end net asset value ("NAV"), it appeared pretty obvious that shareholders were about to get a raise. I projected at the time (in mid-December) that the increase would be just under 6%, but fortunately I under-estimated the year-end boost in its NAV, and LGI ended up increasing its distribution by over 8%.

Now we're halfway through this year, and while we wouldn't expect LGI to be reviewing its distribution policy until December, it's not too early for us to consider what might be in the cards in the future.

If we assume LGI's management keeps the same distribution formula of paying out 7% of its year-end NAV, then the question comes down to how confident are we that the fund's NAV will at least maintain its current level, or better yet, continue to rise between now and the end of the year.

LGI's NAV on 12/31/2020 was \$19.74. A distribution of 7% of that is \$1.38, which divided by 12 gives us the current monthly distribution of \$0.1151.

LGI's current NAV is \$21.34, an increase of \$1.60, or 8% from year-end 2020. If LGI's NAV merely holds its present value (i.e. rises no more) from now until the end of the year, and LGI keeps the same distribution formula of 7% of its current NAV, the new distribution would be 7% times \$21.34, or \$1.494 per annum (i.e. a monthly distribution of \$0.1245 or 8% higher than the current distribution.)

This projected end of year distribution boost, already "baked in" as long as LGI maintains its current net asset value, would bring LGI's yield up to 7.3%, compared to its current 6.8%, at today's market price of \$20.47. The increase of 8% would represent the same percentage increase as last January.

Investors' Choices

LGI investors have several choices to make, depending on their outlook:

- Current investors can sit tight and enjoy their 6.8% current distribution yield, knowing that's pretty generous for a fund that has also provided a solid additional growth component to its total return over the years, in addition to its distribution yield; bringing LGI's average annual total return up to almost 12% over the past 10 years, and 8.7% since its inception in 2004.

- More optimistic investors can buy LGI now, hoping that it will hold its current NAV until the end of the year (or even increase it) and that they will then have locked in the new, higher distribution rate at today's price, giving them the higher 7.3% yield (or more) on their current cost.
- Others can wait and see if the current NAV holds or increases as we approach year-end, and just wait to try to buy in on "down days."

LGI - the Fund Itself

Managed by one of the world's most respected money managers, LGI has generated average total returns of:

- 19.7% for the past 5 years, and 11.6% for the past 10 years, on a market price basis, and
- 17% and 11%, for the past 5 and 10 years respectively, on a net asset value (NAV) basis.

Meanwhile, it sells at a current discount of -4%, not as big a discount as past periods, but still attractive for a fund with this sort of record, and not bad given how closed-end fund prices have gone up across the board, bringing discounts down and prices into premium territory for so many funds.

Here is LGI's investment strategy, according to its website:

The Fund's investment objective is total return, consisting of capital appreciation and current income. The Fund's net assets are invested in a portfolio of approximately 60 to 80 US and non-US equity securities, including American Depository Receipts, generally of companies with market capitalizations greater than \$2 billion, and may include investments in emerging markets. The Fund also invests in emerging market currencies (primarily by entry into forward currency contracts), or instruments whose value is derived from the performance of an underlying emerging market currency, and also may invest in debt obligations, including government, government agency and corporate obligations and structured notes denominated in emerging market currencies."

LGI reports its holdings in two "sleeves," one a developed country segment and the other an emerging market one. Currently the developed country segment accounts for 74% of the fund's assets, and the emerging market segment represents 26%. Within the developed country segment, the distribution is:

- North America - 49%
- Europe ex UK - 24%
- UK - 9%
- Asia ex Japan - 13%
- Japan - 4%

- Latin America - 1%

Within the emerging market segment, the breakdown is:

- Asia - 37%
- Eastern Europe - 30%
- Latin America - 26%
- Africa/Middle East - 7%

Here are its top ten holdings:

Top Holdings (%)	
Alphabet Inc.	3.5%
Microsoft Corp.	3.2%
IQVIA, Inc.	3.0%
Thermo Fisher Scientific, Inc.	2.9%
Aon plc	2.5%
Wolters Kluwer N.V.	2.5%
Zoetis, Inc.	2.2%
Accenture plc	2.1%
Taiwan Semiconductor Manufacturing Co., Ltd.	2.0%
Tencent Holdings Ltd.	2.0%
Top 10 Holdings	23.52%
# Portfolio Holdings	72

Distribution Coverage

As an equity fund, LGI generates most of its total return through capital appreciation, i.e. making good investment decisions and having its portfolio rise in value over time. For example in 2020, its Investment Income, which is dividends and interest received on its investments, was about 2% of its investment portfolio. In other words, the yield on its portfolio was 2%. When you deduct expenses to get Net Investment Income, it was lower, about 0.5%. That means if LGI had to pay its distribution totally out of its NII, its distribution would only be about 8% of the distribution rate it currently is.

Fortunately there is a good explanation for this. Equity funds, unlike fixed income funds, are expected to earn most of their total return from capital appreciation. That's what we expect from well managed equity funds, whether they pay relatively high dividends like many utility funds, REITs or BDCs, or whether they pay no dividends, like Berkshire Hathaway ([BRK.A](#)) ([BRK.B](#)) where you have to create your own income stream by routinely selling off shares of the fund.

LGI delivers in this regard, and in 2020 their distribution coverage, when you consider their entire total return (including appreciation) and not just their NII, was 217%. In other words, the fund's total return was \$2.78 per share, covering its distribution of \$1.28 by over 2 times. This comes as a surprise to many investors, who have come to believe that it is normal for closed end fund distributions to be covered solely by Net Investment Income. While that is not unusual for fixed income funds that collect all their income from interest or dividends (and do not expect to earn much from trading their portfolios), it would be highly unusual for an equity fund that generated most of its income from market appreciation. See our [recent article](#) on Reaves Utility Income Fund ([UTG](#)) for a discussion of this.

So when we buy a fund like LGI, we are counting on fund management to make good investment decisions and generate capital gains. They may not be steady or consistent, with some years' higher-than-usual gains offsetting other years' mediocre results or even losses. But over time, the gains have to offset the losses by a considerable margin if total returns are to meet a long-term, "equity return" level of 8-10%, and of course, exceed the fund's distributions.

Fortunately, LGI's record shows that its management has done that. The best way I know of to determine whether they will keep doing it is to (1) review their website and see if their "bench strength" of professional portfolio managers looks adequate and impressive, and (2) read their reports and research materials and decide whether what they say about their strategy and the markets they operate in makes sense.

Some funds do a better job of presenting this than others, and LGI does a pretty good one. As one of the oldest and largest money managers in the world I would expect this of them, and I am pleased to see that their website does not disappoint. Check out their research and outlook on [global markets here](#). LGI's recent [piece on inflation](#) and its likely impact on value stocks as opposed to growth stocks, as well as fixed income markets, is worth a read, not necessarily because they have all the answers (they don't), but because it and the other research articles suggest that management has its head on straight and is thoughtful and well-informed about the key global trends that will determine the fund's success or failure. That - "having its head on straight and being thoughtful" - is not the same as having a crystal ball. But it's about all I can reasonably expect from any fund management and I think LGI delivers.

Don't just take my word for it...

Besides its great management team and exemplary record, I'm also [happy to see](#) that LGI has 24% of its ownership in the hands of other institutional money managers and fund companies. So as an investor I am in good company. I plan to pick up some more LGI for my own personal account this week.



I launched **Inside the Income Factory** because many of my 11,500 followers and readers of my book **The Income Factory**® (McGraw-Hill, 2020) said they wanted more interactive dialogue than I could provide through public articles.

I answer questions, provide model portfolios, and present short, pithy articles loaded with ideas for spicing up your own Income Factories.

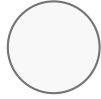
Since starting Inside the Income Factory a year ago, we've climbed to #26 of 186 services in numbers of subscribers.

We must be doing something right. Why not give it a shot: [click here](#) to learn more.

Thanks,

Steve Bavaria

This article was written by



Steven Bavaria

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Author of [Inside the Income Factory](#)

Real-time insights and alerts on all our Income Factory™ model portfolios

Disclosure: I/we have a beneficial long position in the shares of LGI, UTG either through stock ownership, options, or other derivatives. I wrote this article myself, and it expresses my own opinions. I am not receiving compensation for it (other than from Seeking Alpha). I have no business relationship with any company whose stock is mentioned in this article.

29 Likes

20 Comments

Comments (20)

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alphabettr

Yesterday, 11:30 AM



Comments (154) | + Follow

Looks like a good long-term hold. Just wish there were some attractively priced options in the market - I hate buying at the possible crest of a breaking wave. If the feds ever bump rates, we are all going to be holding on for dear life wondering when it will stop.

Reply Like (4)



Greektex

Yesterday, 9:06 AM



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With ROC wouldn't this be best held in a IRA account ?

↪ Reply 👍 Like



7865671

Yesterday, 11:28 AM



Comments (763) | + Follow

[@Greektex](#) From a tax perspective, any fund with high ROC is best held outside of an IRA since gains from ROC induced basis reduction are taxed as LT cap gains when the fund is sold. In an IRA, all withdrawals are taxed as ordinary income. (If held in a ROTH, of course, it doesn't matter.)

↪ Reply 👍 Like (1)



Greektex

Yesterday, 11:58 AM



Comments (2) | + Follow

[@7865671](#) Thanks !

↪ Reply 👍 Like



chris.strickland

Yesterday, 8:41 AM



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It'd be nice to get a large special dividend at the end of the year.

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jasonjones

Yesterday, 6:29 AM



Comments (6.03K) | + Follow

I like articles that tell me positive and negatives about buying CEFs now, this article is the total package. Review of management company, stocks in the fund and analysis. Many global funds have the FAANG stocks in the top five and over 50 % USA stocks. That's not global. LGI is a real global fund.

↪ Reply 👍 Like (1)



toromi

Yesterday, 3:14 AM



Premium

Comments (1.08K) | + Follow

Thanks for this article. I've held a position in LGI since last May, and it's a fund I hope I never sell (the only reason I would consider selling is if the fund gets too expensive relative to its NAV). A fund this successful should get more coverage, but I'm happy that for now it's a diamond in the rough.

↪ Reply 👍 Like (1)



SleepyInSeattle

Yesterday, 2:14 AM



Comments (5.69K) | + Follow

Purchased full position a while back upon your recommendation. Very pleased.

↪ Reply 👍 Like (2)



Eileen Dover

Yesterday, 12:24 AM



Comments (2.45K) | + Follow

[@Steven Bavaria](#) If I keep this on my watch list I may never see it drop back even to 19 again? Now is better than never to get it? I do love the portfolio.

↪ Reply 👍 Like (1)



welcometothemachine

Yesterday, 12:14 AM



Premium

Marketplace

Comments (262) | + Follow

Glad you brought this to my attention awhile ago. Been very happy with its performance and its one of the few CEFs I've been adding to on drops lately. I don't own a large amount of global funds and this is a good one. Cheers

↪ Reply 👍 Like (1)



User 13175852

Yesterday, 12:00 AM



Marketplace

Comments (21) | + Follow

Hi-- What are the fixed income & commodity components? Are they earning the distribution (or some part of it)?

↪ Reply 👍 Like



gman1253

Yesterday, 6:17 AM



Comments (1.08K) | + Follow

[@User 13175852](#) look up LGI on Morningstar (free) click on Portfolio tab & CEF CONNECT to give you the Holdings & grouping breakdowns.

as of 6/30 - around 8.62% Bond according to cefconnect.

↪ Reply 👍 Like



Steven Bavaria

Yesterday, 9:59 AM



Marketplace Contributor

Premium

Comments (3.25K) | + Follow

Author's Reply [@User 13175852](#) I discuss distribution coverage in the article. Over 2 to 1.

↪ Reply 👍 Like



idahojoe

12 Jul. 2021, 11:46 PM



Comments (48) | + Follow

I purchased LGI last fall and have a 20% appreciation so far. The distribution was increased in January. It is a monthly payor and I have been dripping. M* shows that of the \$0.1151 distribution, \$0.0955 is return on capital, the remainder income. M* doesn't show any ST or LT CG so far. I assume that this is an estimate and we will know more at the end of the year. I hold in an IRA and may transfer to my individual account as part of my RMD.

↪ Reply 👍 Like



movetohawaii

12 Jul. 2021, 11:35 PM



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Thank you for the article. I'm holding a full position. Can't complain about its performance. *(edited)*

↪ Reply 👍 Like (1)



thebellsareringing

12 Jul. 2021, 11:28 PM



Marketplace

Comments (2.08K) | + Follow

Thanks for an interesting pick. I like your analysis and will consider the opportunity.

↪ Reply 👍 Like



BuckingTrends

12 Jul. 2021, 11:13 PM



Premium

Comments (232) | + Follow

What type of year end tax form does this generate for shareholders?

Thank you.

↪ Reply 👍 Like



Steven Bavaria

12 Jul. 2021, 11:23 PM



Marketplace Contributor

Premium

Comments (3.25K) | + Follow

Author's Reply @BuckingTrends

I own in an IRA, but if you own in a taxable account I assume it would show up on your brokerage account's 1099, just like other investments.

↪ Reply 👍 Like (4)



NV_GARY

Yesterday, 7:31 PM



Comments (14.95K) | + Follow

@BuckingTrends

The ROC portion would defer tax until sold (cost basis decreases on the 1099)-- do your own DD- it's a bit more complicated than that (in taxable accts)

↪ Reply 👍 Like



jegreen4684

12 Jul. 2021, 11:09 PM



Comments (57) | + Follow

Thanks!!

↪ Reply 👍 Like