

Quarterly Commentary—Q4 2020

# Advent Convertible and Income Fund

Closed-End Fund

## Market Review

Convertible securities rose again in the fourth quarter with their ties to outperforming equity sectors. The asset class closed a banner 2020, with further gains led both by growth sectors and rebounding cyclical and value sectors benefitting from vaccine development and an optimistic outlook on 2021. Approval of two vaccines and more on the way, passage of a second stimulus package, discussion of a larger third package, and resolution of the U.S. elections all played key roles in advancing the equity markets and compressing corporate credit spreads. At the same time, uncertainty over the slope of recovery and the process of advancement of these catalysts has kept volatility higher, aiding the pricing of convertibles. All of these led to strong performance for the convertible market, with the ICE BofA U.S. Convertible Index (VXAO) up 19.67 percent in fourth quarter, compared with 12.15 percent for the S&P 500 and 14.68 percent for the Russell 3000 Index.

In early 2021, there is a healthy marketplace debate over inflation and the potential for the U.S. Federal Reserve to taper its bond purchases again. Investors are reminded that convertibles have a history of strong performance in a time of rising interest rates, as the signals of a strong economy benefit the underlying equities. An example of another example of this was during the “taper tantrum” from May 2013–September 2013 when the convertible index rose 7.71 percent while the 10-yr Treasury yield rose from 1.67 percent to 2.61 percent.

## Convertibles Market

Key sectors contributing to the appreciation of convertible securities in the fourth quarter included semiconductors, software, internet, airlines, retail, restaurants, cruise lines, and capital equipment manufacturers. With strong ties to export sectors such as technology, health care, and industrials, convertible issuers are also poised to benefit from the recent trend of the U.S. dollar falling.

## High-Yield Market

For the high-yield market, the back-up in spreads at the end of the previous quarter quickly reversed as the fourth quarter began and, despite some additional volatility heading into the U.S. election, the spread tightening accelerated following the election outcome and the positive news regarding vaccine development. The ICE BofA US High Yield Index (HOAO) returned 6.48 percent for the fourth quarter, and 6.17 percent for the full year.

The CCC & lower segment of the market outperformed significantly, posting a 12.19 percent return, while single-Bs and double-Bs returned 5.72 percent and 5.74 percent, respectively. All industry sectors posted positive returns led by energy, transportation, and banking, while the worst performing sectors were technology, telecommunications, and utilities.



### Fund Overview

NYSE Ticker	AVK
NAV Ticker	XAVKX
CUSIP	00764C109
Inception	4.29.2003

### Convertible Market Characteristics

Q4 2020 Return	19.7%
Average Delta	68
Current Yield <sup>1</sup>	1.8%
Average Conversion Premium	24%
Effective Duration	1.6 years

Represents characteristics of the ICE® BofA® All U.S. Convertible Index as of 12.31.2020.

### High Yield Market Characteristics

Yield to Worst <sup>2</sup>	4.24%
Option-Adjusted Spread <sup>3</sup>	386 bps
Effective Duration	3.7 years

Represents characteristics of the ICE® BofA® U.S. High Yield Index as of 12.31.2020.

Source: ICE® Data Services, Advent Capital Management, LLC. Characteristics for indexes are calculated by Advent using the holdings and weightings reported by the index provider as of the referenced date.

- 1 Current yield is the annual coupon divided by the current price as of 12.31.2020. For an index, it is the average of the constituent security current yields, weighted by full market value.
- 2 For bonds with embedded options, yield to worst is the yield to the redemption date that produces the lowest result for bonds with call features or the highest result for bonds with put features. For U.S. mortgage-backed securities, asset-backed securities, commercial mortgage-backed securities, and collateralized mortgage obligation securities, yield to worst is equal to effective yield. For an index, it is the average of the yield to worst of its constituent securities weighted by full market value.
- 3 Option-adjusted spread is the number of basis points that the fair value government spot curve is shifted in order to match the present value of discounted cash flows to the bond's price.

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After a large tightening move in the fourth quarter, high-yield spreads are now through their historical averages but still remain wide of pre-pandemic levels. Although valuations are not as

compelling as they were a few months ago and significant additional spread tightening will be more difficult, we believe spreads can continue to grind tighter over the course of 2021.

### Average Annualized Total Returns (12.31.2020)

	YTD 2020	1 Year	3 Years	5 Years	10 Years	Since Inception 4.29.2003
AVK Market Price	17.66%	17.66%	11.62%	13.92%	7.34%	6.54%
AVK NAV	22.91%	22.91%	12.38%	12.03%	7.31%	6.98%
ICE BofA US Convertible Index (VXA0) (USD)	46.22%	46.22%	21.72%	17.76%	12.59%	—

Performance data quoted represents past performance, which is no guarantee of future results, and current performance may be lower or higher than the figures shown.

Source: Advent Capital Management, LLC. Since Inception returns assume a purchase of common shares at each fund's initial offering price for market price returns or the fund's initial net asset value (NAV) for NAV returns. Returns for periods of less than one year are not annualized. All distributions are assumed to be reinvested either in accordance with the dividend reinvestment plan (DRIP) for market price returns or NAV for NAV returns. Until the DRIP price is available from the Plan Agent, the market price returns reflect the reinvestment at the closing market price on the last business day of the month. Once the DRIP is available around mid-month, the market price returns are updated to reflect reinvestment at the DRIP price. All returns include the deduction of management fees, operating expenses and all other fund expenses, and do not reflect the deduction of brokerage commissions or taxes that investors may pay on distributions or the sale of shares.

All data as of 12.31.2020 or otherwise noted. Data is subject to change on a daily basis. The securities mentioned are provided for informational purposes only and should not be deemed as a recommendation to buy or sell. Net asset value (NAV) is the value of all fund assets (less liabilities) divided by the number of common shares outstanding. Market price is the price at which a fund trades on an exchange. Shareholders purchase and sell closed-end funds at the market price, not NAV. A closed-end fund's premium/discount valuation is calculated as market price minus NAV, divided by NAV.

#### GUGGENHEIM FUNDS DISTRIBUTORS, LLC

Guggenheim Investments represents the investment management businesses of Guggenheim Partners, LLC ("Guggenheim"), which includes Guggenheim Funds Investment Advisors, LLC ("GFIA") and Guggenheim Funds Distributors, LLC, the serving agent for the referenced fund. Collectively Guggenheim Investments has a long, distinguished history of serving institutional investors, ultra-high-net worth individuals, family offices and financial intermediaries. Guggenheim Investments offers clients a wide range of differentiated capabilities built on a proven commitment to investment excellence.

#### ADVENT CAPITAL MANAGEMENT, LLC

Advent Capital Management, LLC serves as the Fund's Investment Manager. Based in New York, New York, Advent is a credit-oriented firm specializing in the management of convertible, high-yield and equity securities and the implementation of covered call and hedge fund strategies. The firm manages assets for several FORTUNE 500 companies, foundations, endowments, public pension plans and insurance companies.

#### RISK CONSIDERATIONS

There can be no assurance that the Fund will achieve its investment objective. The value of the Fund will fluctuate with the value of the underlying securities. Historically, closed-end funds often trade at a discount to their net asset value. The Fund is subject to investment risk, including the possible loss of the entire amount that you invest. **Convertible Securities.** The Fund is not limited in the percentage of its assets that may be invested in convertible securities. Convertible securities generally offer lower interest or dividend yields than non-convertible securities of similar quality. The market values of convertible securities tend to decline as interest rates increase and, conversely, to increase as interest rates decline. However, the convertible security's market value tends to reflect the market price of the common stock of the issuing company when that stock price is greater than the convertible's "conversion price," which is the predetermined price at which the convertible security could be exchanged for the associated stock. **Synthetic Convertible Securities.** The value of a synthetic convertible security will respond differently to market fluctuations than a convertible security because a synthetic convertible security is composed of two or more separate securities, each with its own market value. In addition, if the value of the underlying common stock or the level of the index involved in the convertible component falls below the exercise price of the warrant or option, the warrant or option may lose all value. **Lower Grade Securities.** Investing in lower grade securities (commonly known as "junk bonds") involves additional risks, including credit risk. Credit risk is the risk that one or more securities in the Fund's portfolio will decline in price, or fail to pay interest or principal when due, because the issuer of the security experiences a decline in its financial status. **Leverage Risk.** Certain risks are associated with the leveraging of common stock. Both the net asset value and the market value of shares of common stock may be subject to higher volatility and a decline in value. In addition to the risks described above, the Fund is also subject to: Interest Rate Risk, Illiquid Investments, Foreign Securities, Management Risk, Strategic Transactions, Market Disruption Risk, and Anti-Takeover Provisions.

#### DEFINITIONS

**Basis Point** One basis point is equal to 0.01%. **Conversion Premium** The excess of a convertible security's price above parity, expressed as a percentage (Conversion Premium = (Price - Parity) / Parity). For an index, it is the harmonic mean of the constituent security conversion premiums, weighted by full market value. Advent's calculation of Conversion Premium excludes index holdings that have a conversion premium greater than 500, and re-weights the remaining holdings proportionately. **Delta** A measure of equity sensitivity, showing the relationship between a percentage change in the underlying equity and the corresponding expected percent change in convertible price. For an index, average delta is calculated with the average of each constituent security delta, weighted by full market value. Advent corrects erroneous Delta values reported by the index provider (e.g., a Delta reported as less than zero is set at zero, and a Delta reported as greater than 100 is set at 100). **Effective Duration** The percentage change in the price of a bond given a parallel shift in the semi-annual par coupon government yield curve while keeping option-adjusted spread constant. **Yield to Worst** For bonds with embedded options, yield to worst is the yield to the redemption date that produces the lowest result for bonds with call features or the highest result for bonds with put features. If the initially calculated yield to worst is negative, the calculated workout date is within 30 days and the bond is continuously callable, the yield to worst is recalculated using a workout date 60 days from the current date. When yield to worst is stated in conventional terms, the bond cash flows to the workout date are discounted using a yield based on the same coupon frequency of the bond. When stated in semi-annual terms, the bond cash flows to the workout date are discounted using a semi-annual yield. For US MBS, ABS, CMB and CMO securities, yield to worst is equal to effective yield. For an index, it is the average of the yield to worst of its constituent securities weighted by full market value. All bond yields are limited to a +100%/-10% range.

The **S&P 500® Index** is a broad based unmanaged index of 500 stocks, which is widely recognized as representative of the equity market in general. The **ICE® BofA® U.S. High Yield Index** tracks the performance of below investment grade, but not in default, U.S. dollar-denominated corporate bonds publicly issued in the US domestic market, and includes issues with a credit rating of BBB or below, as rated by Moody's and S&P. The **ICE® BofA® All U.S. Convertibles Index** is a market-cap weighted index of domestic U.S. corporate convertible securities including mandatory convertible preferreds. The **ICE® BofA® US Convertible Excluding Mandatory Index** tracks the performance of publicly issued US dollar denominated non-mandatory convertible securities of US companies. The **Russell 3000® Index** is a market-capitalization-weighted index of the 3,000 largest U.S.-traded stocks, representing about 98% of all U.S incorporated equity securities.

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