July 2018

Investment perspectives

Wiley Angell
Senior Portfolio Manager,
Ziegler Capital Management, LLC

Key highlights:

- The goal of the **First Investors Premium Income Fund** is to provide stable returns via in-the-money equity call options to help diversify a traditional stock and bond portfolio allocation.
- Through selling covered call options, the Premium Income Fund is essentially selling away the upside of a stock in exchange for the upfront premium and downside protection generated by the sold call option.
- While there are similarities between this Fund and the **First Investors Covered Call Strategy Fund**, the deep in-the-money sold calls is what differentiates the Premium Income Fund and creates the bond complement characteristics in an investor's overall portfolio. The Fund will likely have a low or negative correlation to traditional fixed income indexes.
- We are not aware of another mutual fund available to retail investors that currently uses an actively managed, in-the-money covered call strategy based on individual stocks.

Concerned about rising rates and maintaining your income?

The latest equity fund launched by Foresters Investment Management Company, Inc. is the **First Investors Premium Income Fund.** We recently sat down with Wiley Angell, Senior Portfolio Manager, Ziegler Capital Management, LLC (the Fund's subadviser), to hear more about the Fund and why investors concerned about inherent fixed income risks may consider this fund in today's rising rate environment.

First, can you share your team's background?

Our team has been managing covered call strategies for over 20 years. Given our approach to risk management, we tend to have a bias towards large-cap, value stocks. Our core strategy has been to buy individual stocks and then sell call options against those same stocks, with the objective of reducing volatility for our clients, while producing competitive returns.

What was the inspiration for this new Fund?

We had an institutional client with an investment grade corporate bond portfolio, with short- to intermediate-range maturities. They were concerned about the potential for rising interest rates and the accompanying duration risk. Also, the yields on their bonds were so low that the client wasn't achieving the same return that they'd received in the past, so they were looking for a new complement to their existing fixed income portfolio. As a result of those conversations, we developed an in-the-money covered call strategy for them, which we are now offering to retail clients as the First Investors Premium Income Fund. The goal of the Premium Income Fund is to provide stable returns via in-the-money equity call options to help diversify a traditional stock and bond portfolio allocation.

How does the Fund work?

The strategy buys individual stocks and then sells calls against those same stocks that are at least 10% or more (also known as being "deep") in the money. This means that the strike price is 10% below the current stock price, so for ABC stock trading at $100, we would sell a call with a strike price of $90. We are selling away all of the upside of ABC stock for the upfront income and the downside protection generated by the call option. The amount in-the-money, in this case, $10, equates to the downside protection (10% downside protection in this example).

So this is an equity product, not a fixed income one?

I do want to be clear on this topic. Although we consider the Fund to be a solid proxy in terms of providing returns for fixed income products, it does buy individual stocks. While the Fund seeks to produce stable returns over the long-term, there are stock-specific and systemic equity market risks, which may impact returns. The downside protection provided by the deep in-the-money calls should help mitigate the majority of this risk, but not all of it. The upside is that the fund does not share fixed income's relationship with interest rate risk. As interest rates rise, bond prices go down, but call premiums go up. So the Fund should continue to benefit from the monetary path of higher rates that the Federal Reserve is currently taking.

Foresters Financial

Exhibit 1 illustrates the mechanics of the Fund. The price of a call option includes a time value component. Longer duration call options have more time value. This time value decays over time. The time value is the income that call option sellers earn over time, as compensation for selling away potential stock upside. In-the-money call options also have intrinsic value, which is the downside protection. Call options that are deeper in-the-money have more intrinsic value, hence, more downside protection.

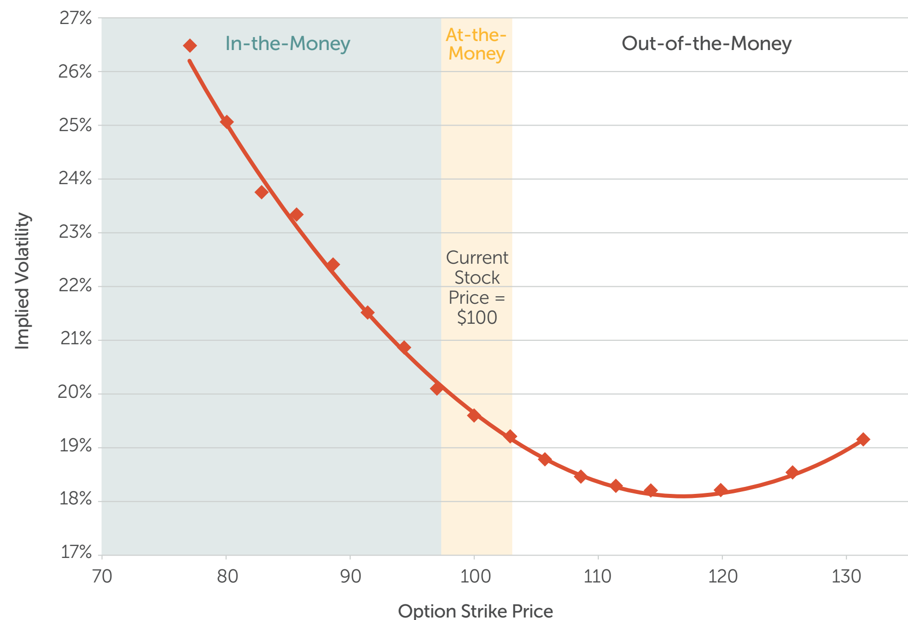
Exhibit 1: How the First Investors Premium Income Fund works

Duration of the call is one year and assumes the stock price is flat at call expiration. For illustrative purposes only. This data is not actual or based on any specific security. This is not a representation or guarantee that a security will achieve similar performance or pay dividends as to those shown.

Can you walk us through the three types of call options?

Exhibit 2 illustrates this concept by using three colored zones plotted against a range of strike prices. The stock is at $100 in this example. Strike prices in the yellow-shaded area near $100 indicate the option is at-the-money, meaning the strike price is close to the current stock price ($100). Looking to the right, the white area shows out-of-the-money calls, meaning the strike price is above the actual market price of the stock. Finally, the blue area on the left side reflects in-the-money calls, whereby the strike price is below the current stock price. The y-axis reflects the implied volatility of the call options. When an investor is selling call options, they would want to sell call options that have the highest implied volatility because that suggests that your premiums are higher.

Exhibit 2: The implied volatility smile



For illustrative purposes only. Actual results may vary.

How unique is the Fund?

At this time, we are not aware of another open-end mutual fund available to retail investors that uses an actively managed, in-the-money covered call approach based on individual stocks, in the way this Fund does. There may be a few investment managers that offer something similar to their institutional clients, but as far as the fund space is concerned, we think it is unique in terms of its investment process as well as how long we have been managing a related strategy. We also believe that the Fund, based on our past experience, is likely to be negatively correlated to the Barclays U.S. Aggregate Bond Index, which would indicate that it should be a good diversifier for fixed income portfolios.

Your team manages a similar Fund?

That is correct. We also manage the First Investors Covered Call Strategy Fund, which is an out-of-the money approach and offers four key benefits to investors. First, by having exposure to large-cap equities, the Fund helps them participate in stock market growth to increase their wealth over the long-term. Second, in attempting to provide more consistent equity market returns, with lower volatility, the Fund aims to help investors stay on track with their financial goals. Third, downside protection from active investment selection and call premiums help to smooth out performance relative to equities alone. Finally, the First Investors Covered Call Strategy Fund hopes to increase client confidence from professional management and downside protection, helping them rest easier and stay invested in the stock market across market cycles.

Are there any similarities between the two Funds?

That's a good question. Both funds buy stocks and sell call options on those stocks. But there's a very substantial difference between the call options in the two funds. In the Premium Income Fund, the call options are written deep in the money. Writing the options in the money provides significantly more downside protection than out-of-the money call options. In the case of the First Investors Premium Income Fund, we are trying to produce a bond substitute in the return stream. As you can see, the two Funds are designed to do two entirely different things. The goal of the Premium Income Fund is to provide stable returns via in-the-money equity call options to help diversify a traditional stock and bond portfolio allocation. In contrast, the goal of the First Investors Covered Call Strategy Fund is to provide equity-like returns with less risk than the S&P 500 Index.

In the First Investors Premium Income Fund, we are selling away the upside in a given stock in exchange for a large amount of downside protection, so the growth potential of the stock is not really a focus as we won't be able to participate in the price appreciation. In contrast, for the First Investors Covered Call Strategy Fund, we prefer to buy stocks that potentially go up in price, because we participate in that upside momentum as the calls are written out-of-the-money.

We would anticipate there to be some overlap of issuers between the two Funds, especially among consumer staples and industrial companies. The First Investors Premium Income Fund buys individual stocks similar to the type found in First Investors Covered Call Strategy Fund, meaning large-cap and high-quality equities. However, in the Premium Income Fund, while still continuing to select stocks based on their ability to avoid downside risk, we approach call options in a slightly different way. For the First Investors Premium Income Fund, we sell (or write) call options at a level of 10% or more in-the-money for the downside protection provided to the Fund. This deep, in-the-money component is what additionally allows the Fund to serve as a bond complement to an investor's overall portfolio as we expect it to have a low correlation to traditional fixed income indexes.

	First Investors Premium Income Fund	First Investors Covered Call Strategy Fund
Underlying strategy	**FAMCO In-The-Money Strategy**	**FAMCO Covered Call Strategy**
Investment objective	Seeks to generate income	Seeks long-term capital appreciation
Best use in the portfolio & objective	**Bond alternative**, bond complement/diversifier	Core equity, **equity alternative**, lower volatility equity
Who should use this strategy?	Investors concerned about rising interest rates and low bond yields	Investors concerned about high equity valuation and more conservative investors
Long-term risk/return expectations	Bond-like return with less risk than broad equity market; does not participate in equity market appreciation; more downside protection in comparison to out-of-the-money (OTM) Covered Call Strategy	Equity market participation with less risk; limited downside protection, capped upside
When this strategy works best?	During flat and slightly positive or slightly negative equity markets	During single digit positive or slightly negative equity market returns
Equity beta[1]	~0.3	~0.7
Stock portfolio	Active to protect downside, Alpha is not a goal. Typically, 30-50 stocks	Actively seek Alpha; typicaly 30-50 stocks
Call options on stocks	Sell 10-15% in-the-money (ITM) calls; generally uses longer-dated options (6-12 mos)	Sell OTM calls, more flexible to roll options to adapt to changing market conditions

[1] Source: Ziegler Capital Management, LLC., 12/31/17. Data is based on historical FAMCO figures. FAMCO is the designated investment team within Zeigler Capital Management, LLC that serves as a subadviser to Foresters Investment Management Company, Inc. for several of its First Investors Funds.

Glossary

Call: an option contract that gives the holder the right to buy the underlying security at a specified price for a certain, fixed period of time.

Covered call: an option strategy in which a call option is written against long stock on a share-for-share basis.

Covered call option writing: a strategy in which one sells call options while simultaneously owning an equivalent position in the underlying security or strategy in which one sells put options and simultaneously is short an equivalent position in the underlying security.

In-the-money: a term describing any option that has intrinsic value. A call option is in-the-money if the underlying security is higher than the striking price of the call. A put option is in-the-money if the security is below the striking price.

Intrinsic value: the value of an option if it were to expire immediately with the underlying stock at its current price; the amount by which an option is in-the-money. For call options, this is the difference between the stock price and the striking price, if that difference is a positive number, or zero otherwise. For put options it is the difference between the striking price and the stock price, if that difference is positive, and zero otherwise.

Option premium: the income received by an investor who sells or "writes" an option contract to another party. An option premium may also refer to the current price of any specific option contract that has yet to expire.

Strike price: the stated price per share for which the underlying security may be purchased (in the case of a call) or sold (in the case of a put) by the option holder upon exercise of the option contract.

Time value: the portion of the option premium that is attributable to the amount of time remaining until the expiration of the option contract. Time value is whatever value the option has in addition to its intrinsic value.

These views represent the opinions of the Portfolio Manager and are not intended as investment advice or to predict or depict the performance of any investment. These views are as of the close of business on April 10, 2018, based on the information available at the time and are subject to change at any time based on market or other conditions. We disclaim any responsibility to update such views.

The **Barclays U.S. Aggregate Bond Index** is a broad-based flagship benchmark that measures the investment grade, U.S. dollar-denominated, fixed-rate taxable bond market. The index includes U.S. Treasurys, government-related and corporate securities, MBS (agency fixed-rate and hybrid ARM pass-throughs), ABS and CMBS (agency and non-agency).

The **Standard & Poor's 500 Index (S&P 500)** is a capitalization-weighted index of 500 stocks. The Index is designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries.

All investing involves risk, including possible loss of principal. You can lose money by investing in a fund. There is no guarantee that the Fund's investment objective will be achieved. The principal risks of investing in the Premium Income Fund are:

American Depositary Receipts Risk. ADRs may involve many of the same risks as direct investments in foreign securities, including currency exchange fluctuations, less liquidity and more volatility, governmental regulations, and the potential for political and economic instability.

Call Options Risk. Writing call options involves risks, such as potential losses if equity markets or an individual equity security do not move as expected and the potential for greater losses than if these techniques had not been used. By writing covered call options, the Fund will lose money if the exercise price of an option is below the market price of the asset on which the option was written and will give up the opportunity to benefit from potential increases in the value of a Fund asset above the exercise price. The difference between the exercise price of an option and the market price of the security on which the option is written may be more than the premium the Fund received for writing the covered call option. Nevertheless, the Fund will continue to bear the risk of declines in the value of the covered assets. Writing call options may expose the Fund to significant additional costs. Derivatives may be difficult to sell, unwind or value.

Dividend Risk. At times, the Fund may not be able to identify attractive dividend-paying stocks. The income received by the Fund will fluctuate due to the amount of dividends that companies elect to pay.

Exchange-Traded Funds Risk. The risks of investing in an ETF typically reflect the risks of the types of instruments in which the ETF invests. In addition, because ETFs are investment companies, the Fund will bear its proportionate share of the fees and expenses of an investment in an ETF. As a result, the Fund's expenses may be higher and performance may be lower.

High Portfolio Turnover Risk. High portfolio turnover could increase the Fund's transaction costs, result in taxable distributions to shareholders and negatively impact performance.

Market Risk. Stock prices may decline over short or even extended periods not only because of company-specific developments, but also due to general economic and market conditions, adverse political or regulatory developments or a change in interest rates. Adverse market events may lead to increased redemptions, which could cause the Fund to experience a loss or difficulty in selling investments to meet redemptions.

Mid-Size and Small-Size Company Risk. The market risk associated with stocks of mid- and small-size companies is generally greater than that associated with stocks of larger, more established companies because stocks of mid- and small-size companies tend to experience sharper price fluctuations. At times, it may be difficult to sell mid- to small-size company stocks at reasonable prices.

Security Selection Risk. Securities selected by the portfolio manager may perform differently than the overall market or may not meet expectations. Declines in certain stocks could detract from the Fund's returns even when the broad market is flat or increasing and the Fund's call option writing strategy may make it difficult for the Fund to dispose of underperforming securities.

Tax Risk. Writing call options may significantly reduce or eliminate the amount of dividends that generally are taxable to non-corporate shareholders at a lower rate. Covered calls also are subject to federal tax rules that: (1) limit the allowance of certain losses or deductions by the Fund; (2) convert the Fund's long-term capital gains into higher taxed short-term capital gains or ordinary income; (3) convert the Fund's ordinary losses or deductions to capital losses, the deductibility of which are more limited; and/or (4) cause the Fund to recognize income or gains without a corresponding receipt of cash.

First Investors Funds are managed by Foresters Investment Management Company, Inc., underwritten and distributed by Foresters Financial Services, Inc.; each is a wholly owned subsidiary of Foresters Financial Holding Company, Inc.

For more information about First Investors Funds from Foresters Financial Services, Inc., you may obtain a free prospectus by calling 800 423 4026 or visiting foresters.com. You should consider the investment objectives, risks, charges and expenses of the funds carefully before investing. The prospectus contains this and other information about the funds, and should be read carefully before you invest or send money. This is general information about the fund. It is not intended to be a recommendation to buy or sell a security product. An investment in these funds is not a bank deposit and is not insured or guaranteed by the Federal Deposit Insurance Corporation (FDIC) or any other government agency.

Foresters Financial

Foresters Financial™ and Foresters™ are the trade names and trademarks of The Independent Order of Foresters, a fraternal benefit society, 789 Don Mills Road, Toronto, Canada M3C 1T9 and its subsidiaries, including Foresters Financial Services, Inc. Foresters Financial Services, Inc. is a member of the Securities Investor Protection Corporation (SIPC).

Foresters Financial Services, Inc. | 40 Wall Street | New York, NY 10005 | 800 423 4026 | foresters.com

18-00286