Investopedia
LIVE

What Is an Interval Fund? Definition, Buying & Selling, Risks

By JIM PROBASCO Updated July 14, 2022
Reviewed by CHARLES POTTERS
Fact checked by ARIEL COURAGE

An interval fund is a type of closed-end fund with shares that do not trade on the secondary market. Instead, the fund periodically offers to buy back a percentage of outstanding shares at net asset value (NAV).

The rules for interval funds, along with the types of assets they hold, make this investment largely illiquid compared with other funds. High yields are the main reason investors are attracted to interval funds. Here is a closer look at these investments.

KEY TAKEAWAYS

- An interval fund is a type of closed-end fund with shares that do not trade on the secondary market.
- These funds periodically offer to buy back a percentage of

- Repurchase is done on a pro-rata basis; there is no guarantee you can redeem the number of shares you want during a given redemption.
- Interval fund shares are usually offered for sale daily by the fund at the current net asset value.
- The minimum investment of an interval fund is typically between $10,000 and $25,000 and they have expense ratios as high as 3%.
- Interval funds tend to provide higher returns than open-end funds and their ability to invest in alternative types of assets also helps increase interval fund yields.
- Because of the restricted selling opportunities, an interval fund should be considered a long-term, mostly illiquid investment.

Buying Is Easy But Expensive

Interval fund shares are usually offered for sale daily by the fund at the current net asset value. Depending on the fund and its guidelines, shares may be restricted to accredited investors but most interval funds are available to anyone.

Minimum investments are often between $10,000 and $25,000 and have expense ratios as high as 3%.

at the stated NAV. The repurchase period can be every three, six, or 12 months. Most funds offer to repurchase quarterly. [1]

The repurchase announcement will specify a date by which you must accept the repurchase offer and the percentage of all outstanding shares the fund will buy; usually 5% and sometimes up to 25%. Since repurchase is done on a pro-rata basis, there is no guarantee you can redeem the number of shares you want during a given redemption.

Because of these restricted selling opportunities, an interval fund should be considered a long-term, mostly illiquid investment.

Yields Are High...

Thanks to a largely illiquid structure, which allows fund managers to invest without the pressure of ongoing redemptions, interval funds tend to provide higher returns than open-end funds.

The ability to invest in alternative types of assets, such as commercial real estate, consumer loans, debt, and other illiquid assets, also helps increase interval fund yields.

...And So Are Fees

Overall fees for interval funds tend to be much higher than those for

Investopedia

LIVE

0.75% in operating expenses.

Not counting the sales charge, annual expenses for this fund could be as much as 3.45%. Annual returns can and do exceed fees, but investors need to know that the bar is often high.

Commercial Real Estate Funds

One alternative investment class made available through interval funds, commercial real estate, deserves special mention. As opposed to REITs, which invest in property pools and trade like stocks, interval funds invest directly in the properties themselves.

> **Important:** Interval funds are registered under the Investment Company Act of 1940 and regulated under the Securities Act of 1933 and the Securities Exchange Act of 1934.

Interval funds tend to be less volatile than REITs, which are sensitive to interest rate changes and subject to the whims of the market. That's partly because real estate-based interval funds rely more on steady rental income than on capital appreciation.

Pros and Cons of Interval Funds

In deciding whether these investments belong in your portfolio, you may consider this list of pros and cons.

Pros

- Returns on interval funds are significantly higher than those of open-end mutual funds.
- The illiquid, long-term structure of interval funds helps restrict normal investor “buy high/sell low” behavior.
- Interval funds provide retail investors with access to institutional-grade alternative investments with relatively low minimums.
- Funds are often less volatile and market reactive since investments are not tied to equities.

Cons

- Interval funds are essentially illiquid, especially compared to open-end mutual funds.
- Since repurchase is done on a pro-rata basis, there is no guarantee you can redeem all of your shares during a redemption window.
- Although yields are higher, so are fees; much more so than with open-end mutual funds.
- The minimum investment, which is low by private equity standards, is still high when compared to the minimum for open-end mutual funds.
- There is both a transparency and conflict-of-interest issue if the portfolio manager is allowed to invest in other funds of the fund sponsor.

specific investor. Interval funds do have higher yields than standard mutual funds; however, they also come with higher fees and are illiquid. If an investor does not need the liquidity and the returns are higher than the fees, particularly when compared to a standard fund, interval funds can be a good investment.

Do Interval Funds Pay Dividends?

Interval funds can pay dividends as they receive them passively, depending on the stocks they hold. If an interval fund's portfolio holds stocks that pay dividends, these dividends are passed onto the shareholder of the fund.

Are Interval Funds Risky?

Interval funds can be considered riskier than standard mutual funds. This is so because they are illiquid and the illiquidity may be a risk to certain investors. Additionally, interval funds can invest in alternative assets, which are inherently riskier than traditional stocks and bonds.

The Bottom Line

The main advantage of interval funds is that they offer higher yields than most other mutual fund options. The two main disadvantages are higher fees and illiquidity. As noted above, illiquidity can be a positive if it forces you to keep an investment long-term.

your portfolio could tolerate the long-term commitment required for this type of vehicle. You should also carefully research any interval funds that interest you to make sure the fees are not likely to eat up any yield advantage.

Finally, you should consult with a trusted financial advisor to make sure you have not overlooked potential traps and that an interval fund makes sense for you.

ARTICLE SOURCES ▼

Related Articles

GUIDE TO MUTUAL FUNDS

Interval Fund: What It Is, How It Works, Example

GUIDE TO MUTUAL FUNDS

How to Invest in Mutual Funds