Market Review

The convertible market closed a strong 2019 with notable returns in the fourth quarter, as global equity markets advanced on improving economic momentum and as fears of a global recession subsided due to easing trade tensions. The ICE BofA U.S. Convertible Index gained 7.38 percent in the quarter, compared with 9.06 percent for the S&P 500 and 9.09 percent for the Russell 3000 Equity Index. Volatility fell as economic angst faded, with the CBOE Volatility Index (VIX) declining from 16.2 at the end of September to 13.8 closing the year, although it ended above the mid-quarter trough of 11.5 as Middle East tensions flared again as the year ended.

While risk-free interest rates rose in the fourth quarter as the Federal Reserve ceased signaling further monetary easing, convertibles have fairly short duration at 2.5 years and are, therefore, somewhat insulated from price risk on rising rates. In fact, the bond element of convertibles benefited from the spread of the high-yield corporate bond index, falling from 402 basis points to 360 during the fourth quarter. For the full year, the convertible market had a notable return of 23.15 percent, compared with the 31.47 percent return of the S&P 500 and the 31.01% gain in the Russell 3000.

Growth sectors resumed outperforming value sectors after a respite in the month of September, with positive sentiment on U.S. GDP growth and falling U.S.-China trade tensions helping export sectors. Optimism regarding global growth helped equity markets rebound, due to their exposures to cyclical sectors. Lower capital spending in 2019 limited supply growth, which led to gains in key commodity prices such as oil and copper at the start of 2020. The potential inflation pickup led to steepening yield curves in most developed sovereign bond markets during the fourth quarter. A forecast of rebounding growth and rising interest rates have historically been correlated with positive returns in the convertible market because they typically help mitigate bond price risk due to convertibles’ low duration, as well as the participation in rising equity markets.

Convertibles Market

Issuance of convertibles remained brisk, as corporates took advantage of higher equity valuation and thinner corporate bond spreads. The largest issuers in the domestic convertible markets were DTE Energy, Sea Limited, and Lumentum Holdings. In the foreign markets, issuers included Atos (convertible into Worldline), Ocado Group, and Rohm. For 2019, the total issuance of convertible securities was nearly $110 billion, the highest level in 10 years.

1 Current yield is the annual coupon divided by the current price as of 12.31.2019. 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.
Global GDP growth is rebounding, but there is substantial uncertainty in the face of the upcoming U.S. elections, British exit from the European Union, and geopolitical tensions. This makes convertible bonds an interesting investment choice to offset the duration risks of fixed-income portfolios while participating in a potential continued appreciation of the equity markets and possible increased volatility.

**High-Yield Market**

The high-yield market, as defined by the ICE BofA U.S. High Yield Index (H0A0), returned 2.61 percent for the fourth quarter. High-yield returns in the first two months of the quarter were about in line with the coupon and continued the 2019 pattern of double-B credits outperforming and triple-C credits underperforming. In December, a confluence of favorable economic and geopolitical developments led investors to add risk aggressively across all quality buckets. Unlike the first eleven months of the year, however, lower quality credits, most notably in the Energy sector, led the way. The strong finish propelled gains in the ICE BofA US High Yield Index, bringing its returns to 14.41 percent for 2019.

Despite the strong outperformance of the lower quality CCC segment in December, it was notable that 2019 was the only year in history that a double-digit return in high-yield was not led by this segment. The high-yield sleeve of AVK also delivered strong absolute returns.

Our outlook is for the expansion to continue near its current pace through at least mid-year. We think about the outlook for high-yield credit spreads in terms of three separate quality bands. The BB-rated band is trading near its all-time tight spreads versus both treasuries and BBB’s, so we see little upside for that segment as a whole. The B-rated segment is relatively tight, with a slightly asymmetrical tilt toward widening. However, if the economic backdrop remains supportive, this sector’s historical range indicates that it could tighten by as much as 50 basis points on a credit-by-credit basis as issuers report better results. The CCC- and-below sector is idiosyncratic, with pockets of value where spreads can tighten if the economy continues growing through year-end. But if growth falters, these low-quality bonds can widen in spread considerably. Putting all of that together and looking at the High-Yield Index as a whole, we see flat Treasury yields and a slight downward bias in high yield spreads combining to produce a constructive outlook for high-yield in 2020.

Given our outlook, we are transitioning our portfolio closer to the benchmark in terms of duration and ratings while still reflecting long-term concerns about an economic slowdown and our asymmetric outlook for Treasury rates. We continue to maintain our duration below the benchmark and remain well underweight in the lowest quality tiers. Our outlook reflects stable economic conditions and could change substantially if we see signs of deterioration. In that case, we would increase our quality bias and reduce duration. As always, our entire team will seek alpha in every corner of the high-yield market, and we strive to outperform through those efforts.

### Average Annualized Total Returns (12.31.2019)

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<thead>
<tr>
<th></th>
<th>1 Year</th>
<th>3 Years</th>
<th>5 Years</th>
<th>10 Years</th>
<th>Since Inception 4.29.2003</th>
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<tbody>
<tr>
<td>AVK Market Price</td>
<td>36.34%</td>
<td>11.47%</td>
<td>7.71%</td>
<td>8.17%</td>
<td>5.91%</td>
</tr>
<tr>
<td>AVK NAV</td>
<td>25.63%</td>
<td>9.16%</td>
<td>6.35%</td>
<td>6.95%</td>
<td>6.09%</td>
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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 12.31.2019 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 Investments

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, delta is calculated with the average of each constituent security delta, weighted by full market value. Advent calculates an index’s delta 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 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 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, CMBS 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 issuers with a credit rating of BB 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. The CBOT Volatility Index (VIX) is a calculation designed to produce a measure of constant, 30-day expected volatility of the U.S. stock market, derived from real-time, mid-quote prices of S&P 500® Index (SPXSM) call and put options. This material is not intended as a recommendation or as investment advice of any kind, including in connection with rollovers, transfers, and distributions. Such material is not provided in a fiduciary capacity, may not be relied upon for or in connection with the making of investment decisions, and does not constitute a solicitation of an offer to buy or sell securities. All content has been provided for informational or educational purposes only and is not intended to be and should not be construed as legal or tax advice and/or a legal opinion. Always consult a financial, tax and/or legal professional regarding your specific situation.

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