



John Cole Scott On Discounts Vs. Dollars, The Recovery And What's Next

Friday, July 2, 2021

Chuck Jaffe, in the 100th episode of The NAVigator podcast interviewed John Cole Scott, chief investment officer at Closed-End Fund Advisors and the executive chairman of the Active Investment Company Alliance. Read the Q & A below as John returns to discuss narrowing



discounts and why investors shouldn't wait for them to widen before investing, developments in the closed-end business, the state of closed-end funds now, and a few funds worth considering for the second half of 2021.

John Cole Scott

The podcast can be found on AICA's website by clicking here: <https://aicalliance.org/alliance-content/pod-cast/>

CHUCK JAFFE: John Cole Scott, founder of the Active Investment Company Alliance is here and we're talking about the difference between discount and dollars, and also about the closed-end fund industry in recovery, welcome to The NAVigator. This is The NAVigator, where we talk about all-weather active investing and plotting a course to financial success with the help of closed-end funds. The NAVigator's brought to you by the Active Investment Company Alliance, a unique industry organization that represents all facets of the closed-end fund industry from users and investors to fund sponsors and creators. If you're looking for excellence beyond indexing, The NAVigator's going to point you in the right direction. And

joining me today, it's John Cole Scott, who not only runs the Active investment Company Alliance but who is the chief investment officer at Closed-End Fund Advisors in Richmond, Virginia which has really good research tools online that you can use at CEFdata.com, and you can learn more about the firm at CEFadvisors.com. You can also learn about the Alliance at AICAlliance.org. And I should point out, this is the 100th episode of The NAVigator. Now that's not that we've been around 100 weeks because we've had some bonus episodes, but it's episode 100 and I'm very happy to say John Cole Scott, great to have you back on The NAVigator.

JOHN COLE SCOTT: It is always good to be here with you, Chuck.

CHUCK JAFFE: These have been fascinating times. When we said we're going to do The NAVigator I was excited anyway because I love closed-end funds, but man, have we tapped into what an interesting time for the closed-end fund industry. And of course the pandemic made things silly and goofy, and now we're watching a recovery that is really interesting because you've got people anxious, desperate almost to get yield. Closed-end funds is a place to get it, but once you get that interest we're also seeing discounts narrow. So help us understand first where we are today.

JOHN COLE SCOTT: Absolutely. So when we think about total returns from before Covid looking back to mid-February of 2020, the average net asset value for a diversified portfolio was about 17% and market prices up about 20%, and that's over a percent a month which is above average for the closed-end fund universe. If we go a little deeper, we kind of do a three and five-year look, and there's some rather favorable numbers, because three years ago, 12% annualized returns, five years ago, 11%. So it's interesting, the discount narrowing in those two periods is only one and change percent, it's not ridiculous narrowing because we were kind of wide three and five years ago. Because you can forget, every three to six years something happens, discounts blow out, markets go down, there's opportunity. But you also can't forget that when you're waiting for the opportunity it doesn't always make sense to wait, if you're an income investor, you need to spend your money every month. So there's interesting data we've found with dividend yields. And so we looked at our index as of the end of second quarter 2021, average yields are 7%, but in dollar terms that's \$113. You go back about four years when we launched our index business with granularity, 7.8% indicated yields but only \$86 in dollar terms. If you might remember, closed-end funds really picked

up after Halloween and the election, indicated yields were 9%, but in dollar terms was only \$104 or 8% lower than today. So yes, discounts are important, Rob covered it last week in great granularity, but you also need to be thinking about the dividends in dollar terms. Because we spend our money in dollar terms and invest for our clients in dollar terms.

CHUCK JAFFE: Because you can't eat discounts.

JOHN COLE SCOTT: You can't, and you need to buy groceries pretty much every other week at least if you're a retired adult.

CHUCK JAFFE: Yeah. So that said, as the closed-end fund industry has seen great growth, tremendous interest, everything else going on with yields, how do you believe we're looking from a longer-term perspective? Because the focus since March of last year has been on the pandemic and it's been on returning to normal, but now 18 months later and having seen everything we've seen, what does normal look like compared to what we have now? Because I'm not sure any of us remember what normal was.

JOHN COLE SCOTT: Well I remember, my undergrad degree is in psychology and in abnormal psychology they say abnormal is just absence of normal, and if you read that textbook you'd think you have almost every disorder in the textbook. So I can definitely say that I've been doing this 21 years as you know, and things always change. I always look at what I can control, and a couple of things we've done value for client is making sure in their taxable accounts, if they have a reasonable tax issue, they're using the right dividend structure of investments, so more return to capital, more long-term gains, more qualified dividends, more munis where appropriate. And then their IRAs, we can definitely do short-term gains and things like BDCs and regular bond funds, because you only get to keep the money you earn after you pay the government and any investment fees. So you can't forget about taxes, and that's for the simple place we've worked really hard for the last couple of years to really help our clients. If you think about what else is normal, I think it's really important to be willing to change your mind. To go down to asset allocation and make decisions about equity and bond, US-foreign, and to really make decisions about where you want your portfolio to sit over the rails of and be willing to make those changes. And I know some people don't change their portfolio regularly, we tend to change the relatively often, Rob Shaker trades three to five million a day each way, but when discounts move there's micro movements that are worth trading which I know he's covered well. So closed-end

funds have that benefit of there's active management, where I need to understand the governance of an Aberdeen versus a Franklin Templeton. I need to understand the quality of the actual manager, the NAV, and then pick the dividend sustainability and the discount level.

CHUCK JAFFE: What is next for closed-end funds? And I'm not talking about the discounts and the performance, I'm talking about with all of the interest and so many people looking to create a difference, is there something on the horizon that you're waiting to see? Because as you point out, you've been doing this for 20 plus years and we're already getting fund types that 20 years ago you really didn't expect them, whether it's structure, interval funds, tender funds, all those other sorts of things, or whether it's content. So as I'm curious, as you're looking forward, watching us get back to normal, with all this interest and potential for growth, what cool thing or different thing or worrisome thing is on the horizon in terms of closed-end funds and products?

JOHN COLE SCOTT: One of my favorite things is we have these new entrants to the structure, whether it be Lord Abbett for interval funds, or Thornburg IPOing a fund this month, but because they're an open-end shop, they actually hired a closed-end fund person from Nuveen that retired to be a lead independent board member to make sure they don't forget how to be a closed-end fund. So what I love, we have funds every month that are coming out with over a billion dollars, sometimes four or five billion dollars in IPO assets, these are serious funds that can last permanently for a long time. But with that new structure as we've talked about over the last two years, it makes the manager pay the load, so entry-day NAV for everyone, and they have a 12-year term usually, which means they have to design a support system for the fund so that investors feel comfortable year three, year five, year 10, and year 12. It's a great structure, new managers, new sectors, we saw the first ESG fund this year. So what I love is you go back to my dad's book in 1990, that was the tail end of the country fund era, and so it's amazing how much the sector changed in the 90s and 2000s, and up to the 20s. I think the next 10 years are going to be an amazing amount of growth for active portfolios that solve specific problems where the ETF wrapper and mutual funds just don't do it well.

CHUCK JAFFE: Well, we want to also solve some problems for our audience, and I know that one of the ways you do that is by advising on funds. So have you got anything that looks

particularly good to you right now that as we get into the second half of 2021, this is on your radar and should be on our audiences' radar?

JOHN COLE SCOTT: Absolutely. So I'll give you an equity fund first, and we're leaning international because we feel that while we're not out of the US market, it's had a heck of a run and I'm okay to be more conservative, I'm not a trend-following investor. So Aberdeen Total Dynamic Dividend Fund is symbol AOD, it's around an eight and change discount, that's relatively wide for what's possible. It's about a billion dollar fund and it yields just around 6.8%, which is a solid yield for an equity fund but you're getting a lot of developed market exposure, it's a fund company that supports its funds really well in the secondary market, and looks to maintain relationships with activists, and institutional investors, and analysts all over. You go to another fund on the debt side, I think emerging markets there's the Templeton Emerging Markets Income Fund, TEI, I know we've talked about it in the past on your show. But again, it's about a half billion dollar fund, it's at about a 5.5% discount, and it yields just under nine, and that's after it reduce its yield, it's doing a managed distribution policy. What I find outstanding, because I have a lot of faith in Templeton managers, you're getting in the top half of the assets, Indonesia, Egypt, Colombia, Ecuador, and Argentina. And I'll tell you, I would not want to do an ETF version of those markets, I definitely want to do a human, boots on the ground version. Such a historic fund that I believe you can even get some extra benefits from the currency differences between countries. So those are ideas we have to maintain monthly dividends without aggressively high yields with a good thesis behind it.

CHUCK JAFFE: John, fabulous stuff as always. We've done 100 issues with the Active Investment Company Alliance on The NAVigator, looking forward to the next 100 and beyond.

JOHN COLE SCOTT: Thank you, Sir. Me as well.

CHUCK JAFFE: The NAVigator is a joint production of the Active Investment Company Alliance and Money Life with Chuck Jaffe. I am Chuck Jaffe and you can learn more about my work and my hour-long weekday podcast at MoneyLifeShow.com. To learn more about closed-end funds, business-development companies, and interval funds go to AICAlliance.org, the website for the Active Investment Company Alliance. They're on Facebook and LinkedIn @AICAlliance. And if you have questions about closed-end funds, send them to TheNAVigator@AICAlliance.org. Thanks to my guest, John Cole Scott, chief

investment officer at Closed-End Fund Advisors in Richmond, Virginia, the founder and executive chairman of the AICA. His firm is online at CEFadvisors.com and CEFdata.com, and he's on Twitter @JohnColeScott. The NAVigator podcast is available every Friday, please subscribe on your favorite podcast app and join us again next week for more closed-end funds. Until then, happy holidays and happy investing.

Recorded on July 1st, 2021

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