CEF Advisors' Scott On The Start Of The 2025 Tax-Loss Harvesting Season

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Chuck Jaffe, in this episode of The NAVigator podcast interviews John Cole Scott, President of CEF Advisors. John looks at tax-loss selling season and whether it has started yet, noting that a few asset classes have largely been able to avoid situations where there will be widespread harvesting this year, while others (most notably business-development companies) may be poised for a lot of tax-driven reshuffling before year's end. Scott, who is the chairman of the Active Investment Company Alliance, also answers some questions on the value of tax-loss harvesting if it means selling a fund you like, and how he recognizes yield traps and spots big discounts that are poor buying opportunities.

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

CHUCK JAFFE: We're talking tax-loss selling with John Cole Scott, president of CEF Advisors, this is The NAVigator. Welcome to 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, which is a unique industry organization because it 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 will point you in the right direction. Returning to The NAVigator today, John Cole Scott, president of CEF Advisors in Richmond, Virginia, and you can dig into their data and everything they do by going to CEFData.com. Beyond CEF Advisors, John is chairman of the Active Investment Company Alliance, which you can learn about and you can get a lot more information generally on closed-end funds at AICAlliance.org. John Cole Scott, great to have you back on The NAVigator.

JOHN COLE SCOTT: Always good to be here, Chuck.

CHUCK JAFFE: Before the Thanksgiving holiday, or as we got to Thanksgiving, we were talking about discount shopping for the holiday season, but the holiday season in the closed-end fund world is also tax-loss selling season. So has the tax-loss selling started as we get to the first week of December?

JOHN COLE SCOTT: Yeah, that's a great question, and so we dug into CEF Data for perspective on the three major credit funds, the taxable bond funds, muni bond funds, and debt-focused BDCs. The taxable bond funds, as recently as July were at about a 40 basis point discount, we think about tax-loss selling season generally after Halloween, so on Halloween that group had widened to 3.7%. They recently bottomed out November 20th at a 5.8%, so over a 2% move, which we would say is tax-loss selling, and they bounced only 90 basis points to 4.7% as of 12/3/25, and we think that's a great example of that sector showing real tax-loss selling. The next group would be the muni funds, muni funds were near-term discount highs as recently as October 1st at only 4.5% discount, then by Halloween a 5% discount, marginally wider, they then widened to 5.9%, so a muted 90 basis point widening as there so much more interest in munis based on where interest rates are going, but they've bounced about 1.2% from that bottom to 4.7%, so not as much but a bigger overall move because of the overriding interest rate factor for munis. Then we go and look at debt BDCs, debt BDCs were at 2% discount way back in mid-July, we already talked about that previously on the podcast, October 10th they widened in that private credit panic that we talked about, to an 18% and change discount, Halloween almost a 15% discount, and they widened more in November to a 17.3%, and now they've bounced 4% to a -13% discount. So we really feel like all three structures had it, it was mild for munis, medium for taxable bond funds, and like BDCs usually are, twice the volatility of regular funds we look at.

CHUCK JAFFE: Well, now I want to move question in another direction, but only after I ask a question from a listener to my show *Money Life* that came in on closed-end funds and on tax-loss selling. This question sent to me by Morris in Bradenton, I'm not going to read the specific question because there's a lot of extraneous details, but if I have to sum it up, Morris has a small loss in one of the closed-end funds he owns, he doesn't hate the fund but he obviously doesn't love the loss, so what he really wanted to know was if the thing that matters when it comes to tax-loss selling is just entirely the size of the loss. Does it make sense if he's not, I want to make a change and go get a faster horse, or I want to do an asset allocation change, if the only thing that's driving the decision is, yep, this fund is down this year, you can capture that loss, but he doesn't hate the fund, does tax-loss selling make sense? Or does it only make sense if there's enough dollars involved?

JOHN COLE SCOTT: So at a basic level, especially the higher his marginal tax rate, and it's a short-term versus the long-term loss, it is useful and powerful. However, like most investing, especially closed-end fund investing, there's some layers of that onion you should peel back. Is it a fund that has a peer to make it a really almost perfect swap? So think a covered call from Eaton Vance, there's a bunch that are similar there, or a muni bond fund from Nuveen, there's a bunch that are similar there. That is a factor that makes it even more likely to take that loss, because you're really not losing tracking error on the recovery. The two other factors, which I alluded to initially was, is it a short-term or long-term, and this year did he already take short-term or long-term gains? So is he trying to neutralize taxes to be in three weeks or is he just taking a loss because he sees red on his screen and doesn't like it? The last piece, and this is also important because closed-end fund discounts are a mechanism of analysis, if you're swapping to another fund, is it to a reasonably peer-attractive discount relatively absolute, relatively relative or comparable? Are you basically paying too much for that swapping peers? Where his taxes live is important, what he's coming from, and where he's going to would drive that answer in my opinion.

CHUCK JAFFE: And in that "Where he's going to" side of that equation, does that change if he's changing asset classes? In other words, you're still looking at the discount prospects and the rest, but his thing was, "I'm positioned where I want to be, I don't mind the fund, if I'm going to take the loss, I'm going to take it and basically put something in that same sleeve in the portfolio, so I'm just going to rotate over to a competitor." Does it make a difference if he was to say, "Well, okay, I'm going to get rid of this, and I'm moving from fund type A to fund type B"?

JOHN COLE SCOTT: That's a good question, because you're right, we find good reasons to review asset allocation are when there's tax losses or money to be raised or to be invested where you're rethinking your overall asset allocation. So if you thought that maybe you're too overweight covered call funds and you'd rather be more in senior loan funds as a random example because of valuations of the NAV and your opinions about next year, this would be a reason to say, "Oh, I can sell this covered call loss," I doubt it's a loss this year, it's probably reversed if he owns those two sectors, that would be a great opportunity. So I think every time you make a decision to trade, it's a great time to rethink where you want to put the money, even if it's not a homogeneous peer.

CHUCK JAFFE: Let's take a moment to talk about where people are putting the money right now, because we've got closed-end funds that are yielding nine and 10% today, and if all I do is look at the income, which is what a lot of people do, they're appealing. And in fact, every time I talk to folks about closed-end funds who haven't invested in them before, it's the income that's drawing them in, but I don't have to explain to you how those payouts, they've got to be supported by the portfolio.

JOHN COLE SCOTT: Yep.

CHUCK JAFFE: You don't want 'em driven by borrowing, you want them supported by the portfolio. So what are the warning signs that you would tell somebody who's looking at a high-yield to be like, "Uh, if this is there, maybe this is not the fund for you"?

JOHN COLE SCOTT: So one of the first data points we added to CEF Data back in 2012 was leveraged-adjusted NAV yield, and I've had some very interesting conversations with some really smart investors that still don't really get that concept, but it's really, I think, basic. It's taking the distribution policy set by the board of directors, in most cases, and line it with what the manager has to do economically with his assets to fuel that policy, and decide is it reasonable and rational? Historically there's more rational distribution policies, there's less rational, there's ones we saw upside that never happen, there were some that were just so large and they never came down, just eroding that principal. That's the leverage adjusted NAV yield and then taking that sector, so imagine preferred equity, and you go, "Okay, leverage-adjusted NAV yield, preferred equity, and let's just say it's 6%, I'm making it up, and go, "Well, that's actually a reasonable return profile for preferred equity, this is a reasonable distribution policy." Then you're taking out the impact of gross assets through leverage and discounts or premiums changing the math required to fuel the distribution.

CHUCK JAFFE: But the other side that's in that answer is you're going to have to look at some statistics that frankly you're going to find at CEF Data, you're not necessarily going to find them everywhere.

JOHN COLE SCOTT: You won't find them at Seeking Alpha, Yahoo! Finance, Morningstar, or I believe even CEF Connect, correct.

CHUCK JAFFE: So if that's going to be our sign, let's talk about other signs that people might want to look for, because you're looking at discounts in some cases that have gotten into the double digits, 15% and potentially more below net asset value. We talked bargain hunting the last time you were on, how does somebody decide that this is real, as opposed to, they're this cheap because they've got a problem?

JOHN COLE SCOTT: Great question. So the problems that we've seen historically come from as simple as just a relatively high expense ratio for what you're getting in the NAV, like there are managers you pay more for because they do stuff that you can't do in your own portfolio, there are some closed-end funds that have expense ratios that surprise me that they're still surviving the market they've been in, you also have funds that just have generally better treatment of shareholders. Now most closed-end fund sponsors are very good to their shareholders, there are a couple that we deem to be less friendly, it doesn't mean we never own them, but we have to say, "You don't like us, we don't trust you, and we'll still buy you." There's also funds that just, whether they're on the OTC market or not really the same governance of a regular closed-end fund, just don't have that same future upside, or so much inside ownership an activist can never bite into it, and so that's going to keep discounts, all else equal, actively wide. So discounts are very useful, they're free leverage if they go your direction, they're not free leverage if they go against you, discounts generally ebb and flow through market cycles between equity, taxable, muni, but real ones, the discount volatility data we show on CEF Data helps you understand one-year, three-year, five-year, how much that discount moves. We love telling retail clients one fund to get excited about, if you like the manager and the sector, relatively low net asset value volatility, relatively wide absolute discount, and relatively high discount volatility, because if you're patient and again like the sector and like the manager, not just those other metrics, there's maybe a tailwind if you're patient, and a lot of retail clients love to be patient with closed-end fund discounts.

CHUCK JAFFE: You can see how that works. If there are anybody who doesn't necessarily break that down, the net asset value is the value of the assets, et cetera, but if it's holding steady but the discount has that, you're seeing how sentiment's doing it, find that spot where sentiment has gotten off kilter, that's the classic, oh, I'm buying something at clearance prices that shouldn't be this much on sale.

JOHN COLE SCOTT: Yeah, like preferreds and senior loans for example, different asset classes but they're relatively low volatility, and there are times when they each have a lot of volatility around their discounts which we find very useful for our separate account clients at CEF Advisors.

CHUCK JAFFE: You know, you mentioned the ownership stake in there and will activist investors be able to get involved, things along those lines. Previously we were talking about when you see high yields, how much further do you have to look beyond that? Well, here, if you've got activist investors, or you've got tender offers, you've got any of those other things that closed-end funds are kind of known for that investors are not always on the lookout for, do you just go, "Okay, let's look at the discount and see if those other things even exist"? And if they do then, "Okay, what's going on?" Do you have to put a check in on there to make sure that that's one other thing on that discount that you're not being led astray?

JOHN COLE SCOTT: Yes, if you have the time to go through 13 filings and see who actually owns the fund, and if it's those three or four names that are generally doing Ds, or the three or four names that are more pro-structure, conversation behind closed doors with closed-end fund management to make decisions good for all shareholders, that's very, very useful. If you don't see them in there and the discount's over 10%, then there's probably not likely to see people jump in at a 15%, maybe a 20% discount. So yes, look at the 13 filers, and also, some like a Nuveen, a BlackRock, they're really committed to the closed-end fund structure, they defend like it's their child, good or bad, and there are some fund sponsors that it's one thing they did, they have one or two or three funds, and if things get hard and complicated, they're far more likely to throw in the towel so they can focus on the rest of their business than just these few closed-end funds that you and I may love for our portfolio but may not be a big focus at the firm.

CHUCK JAFFE: It's one of these things that we're always talking about people to closed-end funds, like anything else, you want to make sure you're making that right investment, getting the right things, it's going to work out for you. John, great stuff, thanks as always for joining me on The NAVigator.

JOHN COLE SCOTT: Happy to be here, and happy holiday season.

CHUCK JAFFE: The NAVigator is a joint production of the Active Investment Company Alliance and Money Life with Chuck Jaffe, and yes, that's me, and I've got an hour-long weekday podcast and you can learn more about it by going to your favorite podcast app and searching for Money Life or just by going to MoneyLifeShow.com. Now to learn more about closed-end funds, interval funds, and business-development companies, go to AICAlliance.org, the website for the Active Investment Company Alliance, and if you have questions for us, well, send them to TheNAVigator@AICAlliance.org. Thanks to my guest John Cole Scott, president of CEF Advisors in Richmond, Virginia, the chairman of the Active Investment Company Alliance, his firm is online at CEFAdvisors.com and CEFData.com, and John's on X @JohnColeScott. The NAVigator podcast is available every Friday, make sure you don't miss any of our episodes by following or subscribing on your favorite podcast app, and if you like us, leave a review or a comment because those things really help. We'll be back next week with more closed-end fund talk, until then, happy investing, everybody.

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