

## CEF Leaders Back CLO BB Debt Amid ‘Cockroach’ Clamor

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Amid lingering concerns about the health and stability of private credit markets, closed-end fund (CEF) industry leaders are soothing their worries by turning to a once-niche solution for income-seeking investors: Collateralized Loan Obligation (CLO) BB-rated debt.

CEF followers say the “structural resilience” of the asset class<sup>1</sup> has allowed it to mature and attract investor interest despite several recent, high-profile red flags, namely the late-2025 collapse of subprime auto loan provider Tricolor Holdings and bankruptcy of First Brands. In response to those developments, JPMorgan Chase CEO Jamie Dimon famously warned the private lending sector may contain more such poor-performing “cockroaches.”

CEF industry speakers at the Active Investment Company Alliance’s 2025 Fall Roundtable in New York City in November

largely brushed aside those concerns as “market blips” that come with investing in equity and debt<sup>2</sup>

“It’s really an overheating of the loan market, a lot of spread compression,” said Connor Dugan, CFA, Principal at Octagon Credit Investors. “The CLO portfolios, they’re investing in below-investment-grade credit, impairments happen all the time,” he added. “With [First Brands] ... it’s definitely our view that it’s a one-off idiosyncratic loss. If you think about what happened there, it’s a variety of factors, a very aggressive M&A spree from the borrower, very aggressive off-balance sheet financing, and ... alleged fraud,” Dugan said.

“At the end of the day on the CLO market, [First Brands] didn’t really impact it as much as you would think given the noise that it’s created,” said Kristofer Pritchett, Partner and Portfolio Manager with Ares Credit Group. He noted that not all CEFs, including the [Ares Dynamic Credit Allocation Fund \(ARDC\)](#), were exposed to First Brands.

The downfall of First Brands underscores the importance of active management in the CEF space, speakers said. “In the CLO universe there’s roughly 130 unique CLO managers, and I’d say 20 of those managers are probably 95% of our underlying portfolio,” noted Dugan. “We feel very confident in this small list of managers,” he added.

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Many industry analysts and asset managers at the November 19, 2025, event bemoaned the recent poor performance of CLO equity, but remained bullish on CLO debt, specifically CLO BB debt, which the speakers all seemed to coalesce around.

“My call on best relative value is CLO BB tranches,” said Dugan, noting that his firm recently launched the [Octagon XAI CLO Income Fund](#), an interval fund with a core CLO BB strategy.

## Evolution of an Asset Class

A new [white paper](#) by Chicago-based XA Investments says a new wave of institutional and private wealth investors have begun taking a more strategic approach to CLO BB debt, resulting in greater market transparency and liquidity.

Characterized by floating-rate income, built-in structural protections, and diversified exposure to leveraged loans, CLOs potentially offer attractive yields compared to similarly rated corporate debt and high-yield bonds.

According to CEF Advisors’ CLO Index, a grouping of funds with net assets over \$100 million and that gives equal weight to each fund, CLOs as of December 29, 2025, had a weighted average market yield of 23.9% and after-tax yield of 18.8% (based on marginal tax rates of 25% and long-term capital gains

rates of 15%). The sector’s predominant allocation is in CLO equity (72.1%).

As an asset class, CLO BB debt weathered the initial “turmoil” of President Trump’s Liberation Day tariff event well, declining by less than 5% and rebounding swiftly — “an outcome that diverged from past episodes of market stress,” the XA white paper states.

The asset class has also benefited from a “global investor education campaign” around CLOs more broadly amid recent scrutiny of so-called risk retention funds, the paper adds. “In this new era, CLO BB debt is no longer just growing – it has grown up.”

## References

<sup>1</sup> XA Investments, [Evolution of an Asset Class: The Case for CLO BB Debt Today](#), Dec. 2025

<sup>2</sup> AICA 2025 Fall Roundtable, Panel Two, [“Credit Alchemy: Turning CLOs and High Yield into Income Opportunity”](#), November 2025.

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