



## John Cole Scott On How Headline Risks Are Impacting Closed-End Funds

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Chuck Jaffe, in this episode of The NAVigator podcast interviews John Cole Scott, President of CEF Advisors. John says that closed-end funds are being buffeted in two directions due to current headlines, with war in Iran impacting net asset values and anchored interest rates impacting levered closed-end funds and discounts shifting to reflect both situations. Scott, who also serves as the Chairman of the Active Investment Company Alliance, says sectors that have

benefitted from the chaos have been MPL and energy funds, while business-development companies and CLO equity funds have suffered. Scott also put his firm's "Trifecta analysis" to work with four funds to consider now: ticker symbols AFB, ARDC, CSQ and MEGI.

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

If you own closed-end funds or business-development companies, you may be overlooking discount shifts, leverage changes, sector rotations, earnings resets and more. A focused portfolio review from CEF Advisors will review positioning and help identify risks while uncovering potential opportunities across your holdings, schedule a conversation at [CEFData.com/contact](https://CEFData.com/contact). Results will vary.

**CHUCK JAFFE:** We're talking about how current events are impacting the closed-end fund world and which closed-end funds might worth a look now, and we're doing it with John Cole Scott, president of CEF Advisors, this is The NAVigator. Welcome to The NAVigator, where we discuss all-weather active investing and plotting a course to financial success using closed-end funds. The NAVigator is brought to you by the Active Investment Company Alliance, which is a unique industry organization that represents the entire closed-end fund industry, from users and investors to fund sponsors and creators. If you're searching for excellence beyond indexing, The NAVigator will point you in the right direction. Today we're talking about navigating through the rough seas of current event headline risk with John Cole Scott, president of CEF Advisors, where they produce really intriguing data that covers closed-end funds, business-development companies, and interval funds. And while John's going to discuss the data, you can dig into it for yourself and learn about the firm at [CEFData.com](http://CEFData.com). John is also the chairman of the Active Investment Company Alliance, which you can learn about at [AICAlliance.org](http://AICAlliance.org). John Cole Scott, it's great to have you back on The NAVigator.

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

**CHUCK JAFFE:** There are a few headlines and they affect various areas of closed-end funds differently, but closed-end funds trade on a few things, not the least of which is sentiment, not the most of which is what's the reality of the underlying investments? So let's talk a little bit about the market backdrop we've got right now, and which is the bigger story for closed-end funds? Is it war in Iran and all of the tentacles coming out from that, or is the Fed and interest rates not doing anything here? What are the stories and how are they impacting?

**JOHN COLE SCOTT:** Yeah, so with interest rates basically, in our opinion, being anchored with no Fed pivot expected, don't really see up or down, that will affect pretty much every levered closed-end fund as that's a piece of the outcome. Going with the war and the other headlines, that's going to affect the NAVs of these funds, the other part of the analysis, and where you might want to be more defensive versus aggressive in the current environment. And then the one thing that's very closed-end funded-ness is where is the discount, where are there some good discounts? Because if given some time, discounts can do the work for you, as long as you've been thoughtful on the entry point.

**CHUCK JAFFE:** Well, speaking of that entry point, have we wound up already seeing discounts move a little bit? Has there been some movement in either direction? In other words, the things where it's a little more risk on, discounts widening, things where it's a little more risk off, let me go for safety, discounts narrowing?

**JOHN COLE SCOTT:** Well, focusing on closed-end funds, there has been some movements in either direction, where I think is actually a bigger story is where the total returns, those discounts on top of NAVs, have been. Looking at our indices for example, at CEF Data, we've talked about it earlier this quarter, but MLP funds up 19%, good call going into the current situation we're in with the war, but utilities are still up 8%, international equity still trending well at 5%, the same as REIT real asset funds, and even international bond funds, +3% and low change, convertibles up 3%, and even the average muni, a very different animal than those, is up 2%, which is a positive, positive side. And then going on the other side, where we see some pullbacks on a total return basis, it's been the US equity and covered-call funds, down 3.5% year to date, the preferred equity funds are basically flat year to date total return, CLO funds, one we thankfully have underweighted dramatically for a while are down 29% year to date, make the BDCs look great this year, Chuck, US bond funds off 6.5%, and senior loan funds off 5.75%, so that's really where a portfolio has done. But the average portfolio is actually up this year a couple percent, depends on your weightings.

**CHUCK JAFFE:** Is there something driving the CLOs, collateralized loan obligation equity funds? Is there something specific that is driving that decline that we've seen?

**JOHN COLE SCOTT:** Massive dividend cuts and terrible NAV performance. We've been using CLOs mostly through the debt side or through multi-sector funds, as we've talked about on this show before in the last couple years. We really historically have only stepped into CLO equity funds, the most volatile part of that, when it's a 2020-like experience or end of '18. Here's the thing I'm telling my clients, markets have been kind of annoying, they've been maybe a little bit frustrating, they've not been ugly, except for CLOs. For closed-end funds and general markets, we're [inaudible 0:04:57] the S&P, things are down, but down a lot is 15, 20, 25, 30%, and we're not there.

**CHUCK JAFFE:** Yeah, and again, CLOs would put you there, and that's why you're not doing too much of it.

**JOHN COLE SCOTT:** Absolutely, so thankfully it's an underweight, we do our best every year to make opinions about where to be and where to avoid, and that has been good so far.

**CHUCK JAFFE:** Are there specific areas where you're going, "Here's a good entry point right now"?

**JOHN COLE SCOTT:** We're building diversified portfolios for taxable and qualified clients, we always like to give a look at examples of our trifecta process at CEF Advisors, your audience can do some more research on it if they'd like, but they pass at least our initial mustard. And looking first, the largest bucket, the one that was still prevalent when I was a baby, Chuck, the muni bond funds which have been around for a long time, and the one that I picked this time to consider is AFB, it's the AllianceBernstein National Muni Income Fund, it's sporting just around a 10% discount, it yields about five and mid-change, it does have modestly high leverage, 42.5%, though relatively normal for its peer group. Duration, not too high for closed-end funds, but 11.8, so definitely banking that interest rates won't go higher in the near term if you buy this fund, or any muni fund in my space, 88% investment grade, it's almost a \$600 million fund, and so it's rather liquid, I don't worry about your listeners if they choose to buy it, have trading issues. And here's one of our favorite puts, both Saba and Allspring, well-known 13 filers, both have just under 5%, which tells me they're keeping an eye on that discount, we'll see what happens down the road for these funds because of that. And another important thing, harder to find in this sector right now, 0% return on capital the last three years, basically it's a high-quality muni opportunity and rare discount, and so it's a great way, we think, to put some money to work when you are tax-driven for your taxable assets.

**CHUCK JAFFE:** So that's AFB, AllianceBernstein National Municipal Income, but I know you didn't come here with just one.

**JOHN COLE SCOTT:** No, sometimes we pull funds we've spoken about before, but we like them again, that happens with our universe. A taxable fund we think's really useful right now is ARDC, the Ares Dynamic Credit Allocation Fund, it's basically a nine and mid-change discount, the yield's around 11%, and in my experience that board works very hard to make sure that dividend is supported and not fake, which sometimes happens in closed-end funds. Leverage, relatively modest for this universe at 39%, duration, the other end of the spectrum, 1.3, and again, it's a broad exposure of roughly one third corporate bonds, one third loans,

one sixth CLO equity, and one sixth CLO debt, again, a multi-sector manager choosing where to be versus stuck in any of those buckets.

**CHUCK JAFFE:** But let's push back and try to explain a little bit to folks who maybe are hearing some of this and hear the jargon and don't get it, because there's a couple things. You talked about the duration being very short, 1.3 years, you also talked about one sixth of the exposure being to CLOs, which we have already said in this conversation, they suck this year, that's as nice as we could be. So you've got short duration exposure to the worst possible sector, that's not a, I'm going to wait for this to get better, I'm going to play a turnaround, that's it sucks and I might have to suck it as a result. Really, that fund now?

**JOHN COLE SCOTT:** The way I would put it is this way, that fund is not a CLO equity fund, where they have to be there no matter what the weather is or the interest rate environment or the recession, that is a fund where Ares is choosing to be and chooses to rotate that portfolio actively. The fluctuation in those buckets are strategic, and again, if I'm going to put a position to portfolio, I want the manager to be choosing that sector right now because he doesn't have to be there. And again, one sixth is material, but is not the driver of the train.

**CHUCK JAFFE:** That ticker symbol, ARDC, for Ares Dynamic Credit Allocation. What else have you got for us?

**JOHN COLE SCOTT:** Well, we're looking at an equity income fund, and again, you know we've been cautiously optimistic for the last couple of years, even though the average closed-end fund has done very well in the last three calendar years. Looking at an equity income fund that is CSQ, that's the Calamos Strategic Total Return Fund, sporting a similar 9.5% discount, a yield of 8.26%, and a leverage of 30%. And this again is a balanced fund, it's not a pure play equity, it's about two thirds equity exposure, very traditional for Calamos, 16% convertibles, and then the balance of what's left is a mix of preferreds and bonds. It's a huge fund by closed-end fund standards, \$4.7 billion, there's not many billion dollar closed-end funds, and no return on capital reported in their tax filings in '22, '23 or '24, and so I think that's a great way to have a balance [inaudible 0:09:50] for the equity side of your bucket to get cash flow. And again, we're also always looking for reasonable discounts, and these dividend policies are all very sustainable, nothing looks too aggressive, where you're getting back your money even at a deep discount.

**CHUCK JAFFE:** And again, that is ticker CSQ for Calamos Strategic Total Return Fund. John, I've never known you to do an odd number, so I'm thinking there's one more.

**JOHN COLE SCOTT:** I can be an odd person but not an odd number. Yeah, we thought it'd be fun to focus on a sector, round out where the themes are we think we'd like to be overweighted, and overweighting is still a nudge in our world, it's not taking over the whole portfolio. But there's a closed-end fund out there, it's the MEGI, the MainStay CBRE Global Infrastructure Megatrends Fund, and it's sporting an 11 and mid-change discount, yield's right at 10%, modest leverage at 25%, and this is one of the things that I like about it, it is 49% US equity and 20% non-US equity, and the balance in a mix of other assets, but it's not a pure play US, the global markets have supported it. It has had return on capital, about 25%, we define it at CEF Data as not destructive by the math of the net asset value performance and the way we look at that, but more of a byproduct of the investments and nothing to be too worried about. And again, this is another thing, it's not the only reason to own a closed-end fund, but Saba owns just under 9% of the shares, so it's a great way, I think, to get a sector that we think could do well this year at a discount that's above average, with a reasonable distribution rate and some tailwinds that I think are going to be useful.

**CHUCK JAFFE:** It's MEGI, that's the MainStay CBRE Global Infrastructure Megatrends Fund. No worry there as we talk megatrends, about just how disrupted things are, because they're megatrends, you don't worry about it at all because things like war in Iran are short duration events relative to megatrends?

**JOHN COLE SCOTT:** I would say that, and also the manager is active management and they've picked their positions, they react during all trends, not just war trends, and like I said, we think those trends will do better. It's kind of at an infrastructure end of the spectrum, which we think is more positive than other areas, and valuations aren't too high.

**CHUCK JAFFE:** One other thing everybody should note, in our show notes for today, we're not going to just have links to [CEFData.com](http://CEFData.com), we're going to put links to the individual funds, the [CEFData.com](http://CEFData.com) pages of the individual funds we've talked about. So there's four, if you want to check 'em out, just go to the show notes, you'll have the links there for the four funds. John, ultimately in times like this it's not, let's lean in and find the best buy, it's build the best portfolio. So since you are an active manager in closed-end funds and you're always trying

to be reasonably well positioned while having a base case as well, how active have you been with investors' portfolios as we've watched war break out and the rest of this stuff?

**JOHN COLE SCOTT:** Yeah, no, we still remain rather active, I've taken some positions down that have run longer than we like, we've seen some of our year-end 13 filings grow by almost 2x and some almost disappear. Again, we're not high turnover, Dan Silver and I are basically nudging our client portfolios actively through the cycles. I did another round of tax-loss selling since I last talked to you, Chuck, so if you do it right, you don't want to tax-loss sell, but if it's there, you use it because it's a tailwind for the future.

**CHUCK JAFFE:** So it's about being opportunistic, and even in times that the headlines make you crazy, the opportunities make you wealthy.

**JOHN COLE SCOTT:** Yeah, and the closed-end funds are stable capital, the discounts are far more important to analyze than just the NAV or just the yield, you really need to bring it all together in a balanced approach. Again, we don't know what's going to happen, Chuck, that may surprise you, and so we try to blend this analysis and diversify, more like baseball than doing brain surgery.

**CHUCK JAFFE:** Great stuff, John. I'm sure we'll talk again soon, thanks so much.

**JOHN COLE SCOTT:** Always good to be here, man.

**CHUCK JAFFE:** The NAVigator is a joint production of the Active Investment Company Alliance and Money Life with Chuck Jaffe, and I'm Chuck Jaffe, you can learn more about me and my show by going to [MoneyLifeShow.com](http://MoneyLifeShow.com) or you can search for it on your favorite podcast app. Now if you want to search for more information on your favorite closed-end fund, interval fund, or business-development company, go to [CEFData.com](http://CEFData.com), that's the website for CEF Advisors. John Cole Scott, my guest, he's president there, and you can get more information to dig into the funds directly, like I said, they're in our show notes as well, by going to CEF Data. To learn more generally about closed-end funds and the whole closed-end fund industry, go to [AICAlliance.org](http://AICAlliance.org), the website for the Active Investment Company Alliance. The NAVigator podcast is available for you every Friday, and we'd love it if you'd made sure you're not going to miss us by following along or subscribing on your favorite podcast app. We'll be back next week with more closed-end fund fun, until then, happy investing, everybody.

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