



XA's Flynn On How The Private Credit Market Is Challenging BDCs, Interval Funds

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Chuck Jaffe, in this episode of The NAVigator podcast interviews Kim Flynn, president at XA Investments, a firm that specializes in alternative investments. Kim says recent private-credit bad news events have widened discounts and raised concerns over business-development companies and interval funds, but have likely created a buy-the-dip moment in the industry. She discusses how fund sponsors and advisers must do a better job educating investors on how these products get through worrisome times, but says she does not think the headlines or their attendant challenges on direct lenders will

discourage yield-hungry private-credit investors in the long run.

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CHUCK JAFFE: We're talking about the private credit markets, direct lending, and interval funds with Kimberly Flynn, president of XA Investments, 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 is brought to you by the

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Active Investment Company Alliance, an industry organization that represents the entirety of the closed-end fund business from investors and users up to fund managers, sponsors, and creators. If you're looking for excellence beyond indexing, The NAVigator will point you in the right direction. And today we're looking in the direction of the credit markets and more with Kimberly Flynn, president at XA Investments, which is an investment management company that gives investors access to alternative investments, you can learn more about the firm and what it does at XAInvestments.com. And if you want to learn more generally about closed-end funds, interval funds, and business-development companies, you can get more at AICAlliance.org, the website for the Active Investment Company Alliance. Kim Flynn, great to have you back on The NAVigator.

KIM FLYNN: Thanks, Chuck. Good to be back, it's timely that we're talking today.

CHUCK JAFFE: It is, because we have seen a number of things happening in credit markets and direct lending, BDCs, direct lending interval funds, there have been some issues. So let's start there because, yes, there have been some headlines, they've gotten some attention, but have they had much impact on the closed-end fund market and the BDC market yet, or is it more our red flags are up and we're watching?

KIM FLYNN: I think for BDCs the answer is slightly different, so let's start with BDCs. It was really in the fall, subsequent to the news around First Brands and Tricolor, which we now know to be largely fraud, but the question that investors are asking in private market, or direct lending specifically, is how much of the loans that have been issued to these small and medium sized businesses are going to go bad? How widespread is something like fraud? And the BDC market, starting with listed BDCs, started trading at fairly large discounts, so 10-15% discounts, and then we started to see headlines regarding Blue Owl trying to merge a non-traded BDC with a listed BDC, and because there was a valuation question regarding that merger, it actually didn't happen because the listed BDCs had gone to fairly large discounts. BDCs will do this from time to time in terms of how close they trade to par, sometimes at premiums, sometimes at discounts. So I think there's a lot of questions it started, and then we started to see concerns about direct lending interval funds in Q1 of 2026, and so more recently the question is liquidity and how shareholders should think about liquidity in an interval fund. When you're investing in small and medium businesses, the loans can vary in terms of liquidity, and so we want to structure these investments the

right way. A BDC wrapper or an interval fund wrapper, these are appropriate in terms of structuring these types of loans, right? You wouldn't be able to put these loans into a mutual fund or an ETF given the lack of liquidity. So at the heart of this issue, Chuck, I think is concerns about valuation, and concerns about shareholder access to liquidity.

CHUCK JAFFE: Credit has really been the biggest category of the interval fund marketplace, it got the bulk of the inflows last year. Has that trend continued or have the headlines basically stopped the flow? How has it impacted the market? Or has it not, it's just a backdrop?

KIM FLYNN: Well, I think what a lot of the media is not reporting, especially in regard to some of the market leaders like Cliffwater, which is that they actually have a very robust sales and marketing effort. So even though we've started to see more demand for liquidity, in the case of Cliffwater's latest redemption on their corporate lending fund, they had a 14% demand for liquidity, but an interval fund is designed to provide partial liquidity or a limited amount of liquidity, if you will. Most interval funds are designed to offer, on a quarterly basis, 5% of the portfolio for exiting shareholders or people who want to trim positions. So in this case, we have seen an uptick in demand for liquidity in that higher amount of redemptions, the 14% that I noted. But it's important for investors who are starting to invest in interval funds to understand the proration mechanism, because this is built into an interval fund at the start and it's meant to protect shareholders. So in light of the fact that these types of loans in the direct lending category are less liquid than what you might find in a mutual fund or an ETF, proration is necessary to protect all shareholders. And so at the outset, when you make an investment in an interval fund, you need to understand the terms and conditions of an interval fund. An interval fund, it can from time to time prorate, oftentimes these funds continue and you don't hear about proration. Proration, we see it as the normal functioning of an interval fund, and I think the media is focused on this aspect of, do investors know that there's a proration risk? Do they understand that they may have limited liquidity? So I think there's some industry growing pains as both investors learn about these aspects and understand some of the limitations on liquidity, but also I think there's growing pains on behalf of the interval fund sponsor community in terms of what are best practices and what can we do to improve the experience for shareholders?

CHUCK JAFFE: Yeah, you'd like to make sure that the shareholders are aware of what they're getting, and while you'd like to believe that the shareholders understand it, fund companies can do a little bit more when it comes to education, can't they?

KIM FLYNN: Yeah, I think they do a terrific job, especially Cliffwater and other market leaders, in terms of education at the point of sale, but as we know, Chuck, investor memory three years later, they may not remember exactly what was said. So I think that there are things that we can do on our website or on our fact sheets to make the liquidity provisions more prominent and serve as a reminder, right? I think that we're at a point where interval fund adoption is growing and there's a larger base of investors coming into the market, so a lot of advisors and investors are new to this, and so it's a helpful reminder because you're dealing with clients that have been in your portfolio for maybe a longer time, maybe they're used to the quarterly redemption cycle. But to the extent that we want this marketplace to grow and we want to broaden out the potential investors, there's been talk about putting interval funds into retirement accounts, so naturally as that buyer base potentially grows, it raises more questions about appropriateness, suitability, and I think most of the interval funds are sold through the financial advisor community, it's not a direct-to-consumer type investment. Chuck, we've talked in the past about listed closed-end funds, which are like ETFs in the sense that anybody can buy it, you don't have to have a financial advisor, but here the financial advisor has a role to play, in addition to the interval fund sponsors, in making sure that shareholders understand liquidity and are comfortable, especially in times like this when they're seeing headlines and they may have more questions about these topics.

CHUCK JAFFE: One of the things you said in the early part of this conversation about BDCs was that sometimes you have conditions come up and BDCs wind up trading at a bigger discount, et cetera. Interval funds are built to withstand this, this is not an abnormal thing, if it was an abnormal thing, it wouldn't be built this way to deal with this. As we expand and people are getting their first exposure, and suddenly it happens and something happens in the market, they may not recognize this. But is there a lesson here as well, that we see this happen and it may not be part of the standard business cycle, but it's not so unusual? Can we get to a spot where somebody understands, if your interval fund has gated the exit, it's kind of like hanging on through the dips? It may not be buying the dips, but it's kind of like you're going to be hanging on through the dips. Is there a point where the public will get

that? Or do they not get that because these things never show us that real cycle, here's the bounce back?

KIM FLYNN: Well. I think we're all learning, but part of what we've seen in the non-traded REIT and the non-traded BDC space, those are investment structures that you can stop liquidity, meaning you can gate. When you stop liquidity, you effectively are throwing up a gate, and as we know, shareholders don't like that, right? Especially because there's a question about when you will have liquidity to the extent that the fund continues to be gated. So I think the media has picked up the topic of gating, but what interval fund investors need to know is that interval funds, they legally cannot gate, they prorate. And I appreciate that this is a subtle difference, and proration is by design because these assets, the underlying assets, are fairly illiquid, and so to structure something like this you need to have this mechanism. People want liquidity, we have to provide it, but it is a redemption cycle, and so you're right about, we haven't really lived through enough cycles so that people get accustomed to it. And I think a lot of the reporters are conflating the different structures, the non-traded REITs, the non-traded BDCs, which do and legally are able to stop providing liquidity and gate. Private funds can also gate, it depends on their terms and provisions. But an interval fund, from day one, it has a liquidity plan, it's communicated in the prospectus, and so we actually think that the interval fund will continue to be a preferred structure because you can't stop liquidity. You at least have to provide whatever is stated in your prospectus, typically that's 5% per quarter, and I think some advisors take comfort in that. But you're right that we just as an industry haven't lived through too many cycles, and there were interval funds around in 2020 during the Covid cycle, but as we know, that was a very quick recovery given what the federal government stepped in and did. And so if an event like that happens in between two quarterly redemption windows, which is precisely what happened in March and April of 2020, the market was unphased and there was really no experience with this. So I think the question is, we've actually seen continued sales into credit interval funds, and one of the opportunities for credit interval fund sponsors, if you have an asset-backed strategy, if you have a multi-strat, the noise of late actually gives you an opportunity to talk with advisors about why there are some other alternatives to direct lending. Frankly, a lot of advisors are probably overexposed to BDCs because they've been so popular over the last five years, so we say that the interval fund market is large, diverse,

a lot of different asset classes, a lot of sub-categories. And as you know, Chuck, yield is always in demand, people are going to look for yield, and maybe right now you're going to back away from some of your corporate credit exposure and look for other sources of yield, so we do see a lot of people, at least in terms of the new fund formations, there's been a ton of activity on the asset-backed side for that very reason.

CHUCK JAFFE: And is there something particularly interesting to you that's coming, because of course you're involved in the development of new funds? Or the problems that we've seen, is that going to slow down development for a little while as everybody watches that play out and doesn't want to be doing the marketing while this other stuff's happening?

KIM FLYNN: I think you're right, Chuck. I think some of the fund formation and rollout of new credit funds will probably slow down a little bit, only because of the practical reality of sending your sales team out at a moment in time when people are concerned about credit. I think it's actually a great moment in time because there are these other attractive alternatives. But for that very reason, I think we're going to see more private equity, but specifically we're seeing momentum around sector-specific, so we think we're going to see more in the way of sports focused private equity, healthcare, tech, and even an energy fund. There's 313 interval and tender funds in the market as of the end of February, and it's kind of shocking given how large the energy sector in the United States is, that there's not a single dedicated energy fund, so I think there is a lot of white space away from credit and we will see more new entrants in those areas.

CHUCK JAFFE: We'll turn to you as we watch it all play out, I'm sure we'll have you back. Kim, thanks so much for the time today.

KIM FLYNN: Thanks, Chuck. Great to be with you as always.

CHUCK JAFFE: The NAVigator is a joint production of the Active Investment Company Alliance and Money Life with Chuck Jaffe, and yes, I'm Chuck Jaffe, you can check out my show on your favorite podcast app or at MoneyLifeShow.com. Now to learn more about interval funds, closed-end funds, and business-development companies, go to AICAlliance.org, that's the website for the Active Investment Company Alliance. Thanks to my guest Kim Flynn, she's president at XA Investments, an investment management company that gives investors access to alternatives, learn more at XAInvestments.com. The NAVigator podcast has

something new for you every Friday, so make plans to join us again next week for some more closed-end fund fun, and until then, happy investing, everybody.

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