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Jaffe and Aberdeen's Taggart on Changing the Future for Closed-End Funds

"Words Definitely Matter": Mike Taggart on What It Would Take to Make Closed-End Funds Mainstream



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Chuck Jaffe, in this special edition of The NAVigator podcast, interviewed Mike Taggart, Head of Closed-End Fund Investor Relations at Aberdeen Investments, at the Active Investment Company Alliance's Fall Roundtable in New York City. Jaffe goes through ideas from his roundtable keynote on making closed-end funds more mainstream, from a new name to embracing the discount, and Taggart weighs in on each. "Words definitely matter," Taggart says. He argues that if closed-end funds were rated alongside mutual funds and ETFs on risk-adjusted returns, "most closed-end funds would be five star rated."

TOPICS DISCUSSED

- Why the name "closed-end fund" makes eyes glaze over, and whether calling them "sentiment" or "permanent capital" exchange-traded funds could catch on the way defined-outcome and buffer ETFs have
- Why RIAs are good candidates for closed-end funds, while wirehouse advisors can only pitch what's approved on their platforms, and why CEFs were scarce at Schwab Impact
- How managed distribution policies work, either a set amount per month or a percentage of NAV, and the trade-off between a predictable check and payouts that move with NAV
- Why a blowup in a private credit, private markets, or IPO fund could tar all closed-end funds, and why funds should disclose whether they hold a company like Anthropic directly or through a special purpose vehicle
- Why the industry avoids marketing its discounts for fear of drawing activists, and how Taggart separates fund-specific discounts from sentiment-driven ones that can be a selling point
- Why rating agencies mostly skip closed-end funds, and Taggart's experiment showing most would be five-star rated on risk-adjusted returns if rated alongside mutual funds and ETFs

The discussion is educational in nature and intended to help investors and advisors better understand the tools, trade-offs, and data points involved in evaluating income-focused strategies.

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- Free CEF & BDC profile pages: cefdata.com
- 40+ CEF & BDC indexes: cefdata.com/index
- Listen to the full episode: AICAlliance.org

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THE CONVERSATION

CHUCK JAFFE

We're talking with Mike Taggart, head of CEF Investor Relations at Aberdeen Investments, and the subject matter? Well, it's actually some of the things that I was saying at the Active Investment Company Alliance Fall Roundtable. This is a special edition of The Navigator.

Welcome to The Navigator, which is all about following a course to financial success using closed-end funds, and it's brought to you by the Active Investment Company Alliance, which this week is holding its Fall Roundtable event in New York City. I attended it, but I didn't just come as an attendee or the media guy. I also gave a keynote, and in that keynote, well, I threw out some ideas that I think would make closed-end funds more popular and more mainstream. And while I threw them out to the broad audience, the guy I really wanted to hear from about it is my guest, because Mike Taggart is a longtime observer of the closed-end fund industry. He is head of closed-end fund investor relations at Aberdeen Investments, online at AberdeenInvestments.com. And if you want to learn more about closed-end funds generally, check out AICAlliance.org, the website for the Active Investment Company Alliance. Mike Taggart, thanks for joining me.

MIKE TAGGART

Yeah, thanks for having me, Chuck. Always good to chat with you.

CHUCK JAFFE

So, like I said, I gave a keynote speech here where nobody really asked me to say, like, what could happen to make the closed-end fund industry better, but I've got opinions and I'm not afraid to

share them. So I did, and I want to run over points that I made, and then you can say, like, "Chuck, you're crazy. This shouldn't have happened," or "This is a great idea, and maybe somebody should take this up." So the first thing I said, as I was again pointing out what has to happen to make closed-end funds more accepted: we've got to call them something else. I mean, closed-end funds. The eyes glaze over just at the mention of the words, and they are, especially listed ones, exchange-traded funds. They are a mutual fund vehicle. Can we get something else to call them?

MIKE TAGGART

Yeah, I mean, I think you make an interesting point. When I first started looking at closed-end funds in 2010, I had friends who knew what closed-end funds were, but they would joke with me, you know, "Why are you covering those? They're closed, right?" As if they were a closed mutual fund. And years ago, people tried to say, well, you know, exchange-traded products, and that would be ETFs and closed-end funds. You know, you threw out some ideas, perhaps the sentiment exchange-traded fund or that sort of thing. I mean, words definitely matter. It's just finding a way to describe them that a retail investor would understand, I think, is the primary thing that you're looking for and suggesting. And I don't know what the answer is, but yeah, I mean, if they called them something other than closed-end funds, would it change anything? I don't know.

CHUCK JAFFE

But that's part of the interesting thing behind that discussion, because we now have, like, defined outcome ETFs or buffer ETFs. Well, they're getting traction, and autocallable ETFs, which I know people don't understand. They understand them even less than closed-end funds. And the idea behind calling it a sentiment fund is that ETFs trade basically at net asset value. Closed-end funds don't, based on sentiment.

MIKE TAGGART

Largely due to sentiment. I mean, there's some funds. I mean, we talked about this on an earlier panel. Some funds seem to get stuck at a wide discount. It has nothing to do with sentiment. But for the most part, yeah. I mean, I think the discounts are sentiment-driven. The valuations are sentiment-driven.

CHUCK JAFFE

And a suggestion was made literally between the time when I finished the talk and when we came down here for permanent capital funds. I like that better, even if I don't believe the audience necessarily understands it. But if they've come up to understand defined outcome funds, everything's possible.

MIKE TAGGART

> Yeah, I mean, I brought up the term permanent capital on our panel earlier, and one of the large activists took me to task for calling it permanent capital. But I mean, really, it is permanent capital. That's what's being implied with the closed-end name to begin with. So yeah, permanent capital exchange-traded funds sounds stable, but, you know, again, words matter. And maybe if you change the label of these funds, it could gain more investor interest. "Hey, what are these things?" Right.

CHUCK JAFFE

> Another thing that I said in my talk would help was if there was more resonance for closed-end funds within the advisory community. After spending the time at Schwab Impact, I saw very little closed-end fund representation. You were there. I got to just see you, and I'm sure you walked around and saw the same thing. It wasn't your closed-end fund competitors who were filling that exhibit hall, but that's where they should be, because investors are not coming to closed-end funds naturally.

MIKE TAGGART

> One thing, you know, Schwab Impact had a lot of RIAs there, right? Advisors. And just speaking with them over the years, different kinds of independent advisors, you know, they're focused on building their practice. At the end of the day, it kind of goes back to what we were saying earlier: that advisors, whether they're wirehouse, whether they're independent, they need to be able to explain to their clients what they're invested in, right? And they have to do it simply. RIAs, especially depending on what their end client wants, are good candidates to be involved with closed-end funds. You know, wirehouse advisors, to a large degree, they can only solicit what's been approved on their platform. And so, you know, it's really kind of understanding how you get things approved on their platform to see if they can actually get their clients invested in the product.

CHUCK JAFFE

> Third thing I made as a point is that closed-end funds need to just provide consistent, day in, day out. Be the kind of alternative to an annuity: I buy it, I know what I'm going to get, I know what it's going to pay me. And that's what a lot of closed-end funds want to do and try to do. Do we mess that up because we encourage the tax-loss selling and some of those things, or do we mess it up just because investors can't really sort of look at the income and go, "That's what I want," at a time when they're maybe watching a discount get wider?

MIKE TAGGART

> I think most investors in closed-end funds kind of hold on to them for a very long time. We see this a lot on my team. My team answers the 800 lines at Aberdeen, and the people calling in there are

smaller advisors or retail investors. And those questions, you know, I mean, we'll get people calling in saying, "I've owned this fund for 20 years," right? And they have just some vague question about the fund. One of the things that closes a discount, and one of the things you can do to manage a discount, is a distribution, a managed distribution policy. Different firms call them different things. There's two types of policies, really. One is where you say, okay, I'm going to pay out X cents a month, and just set it. Another one is, I'm going to pay out a percentage of the NAV every month. And if you do the percentage-of-NAV approach, you are going to have some fluctuation. As the NAV changes, you know, the amount that's being paid out changes. And I mean, there's different schools of thought within the industry as to which is preferred by investors, right? Because on the one hand, if it's "I'm paying out X cents a month," then they know what's coming in, right? Every single month they're getting a check for X amount. Whereas the managed distribution policy, if the NAV goes up, you can actually see an increase, but if the NAV goes down, you're going to see a little bit of a decrease, right? The idea is that over time, hopefully, on a percentage-based policy, it kind of evens out, but there would be some fluctuation in the amount that the person's receiving every month.

CHUCK JAFFE

In the effort to keep us on our time frame, I'm not going to do all seven points that we had. I'm going to jump ahead to one that I think is particularly important, which is we're seeing a lot of things happen in the closed-end fund industry. A lot of new products being created. There's also a lot of, like, "Hey, let's get access to this asset class or that asset class." And I've talked to plenty of experts outside the closed-end fund industry who believe we're going to see some sort of private credit fund, a private markets fund or IPO fund have a blowup, and it is really important for the future of the closed-end fund industry that if that blowup occurs, it not be in a closed-end fund. Right?

MIKE TAGGART

We've had different sectors, just since 2010, since I've been following closed-end funds, that have kind of blown up, right? And then there's, you know, the shareholders in those funds are negatively affected, but then kind of the survivors that are still in that have kind of done things with the product, I think, to improve them, and to maybe diversify more broadly within the broader segment that the fund invests in, right? So I think what you're talking about is private credit, private equity type of stuff. And, you know, I think the important thing is, yeah, to a degree, if something bad happens to the closed-end fund industry, it puts a bad light on all closed-end funds until you get the messaging out that, "Hey, we don't do that, right? We're not invested in that segment," that sort of thing. I do think that the funds that are out there now investing heavily in private equity have a, I think, I mean, I think they have a fiduciary duty to explain to their shareholders exactly what they're investing in, right? So you can go out there all day and say, "Oh, well, this fund's invested in Anthropic." Is it, or is it invested in a special purpose vehicle that's invested in Anthropic, right? And I was at another conference earlier this week, and that was a big

discussion, kind of in the hallways and that sort of thing. So hopefully we don't see a blowup. But if we do, hopefully the shareholders in those funds actually understand what they're invested in. And that's a big thing for all closed-end funds. I mean, investors should know what they're invested in, whether it's a closed-end fund, an ETF, mutual fund, whatever, right? They should just know what they're invested in.

CHUCK JAFFE

But the problem with having this unusual name that, again, we started with, "let's change the name," or what people see as, is that they're just going to remember there was a blowup in a closed-end fund. The same way, by the way, that when you had early blowups in exchange-traded notes, you basically killed the ETN market, even as the ETF market was going gangbusters.

MIKE TAGGART

Right. I mean, I think that there was just a general misunderstanding. Maybe we could look back to closed-end funds with the ARPS crisis, almost 20 years ago now, where they were being sold as money market funds, right? And they certainly weren't money market funds. So, you know, that took a lot of explaining by the closed-end fund industry and the funds that use auction rate preferred securities to explain to their investors what was actually going on.

CHUCK JAFFE

Another point that I made in my talk was that closed-end funds need to really embrace the discount, like make the discount a selling point, which they don't really want to do in their marketing materials, because it's like, "Hey, our fund is not performing all that well," or "Our fund is below its net asset value." But investors love a good sale, and it's not a terrible thing. Like, you can buy assets at a discount. Oh, by the way, if we can't narrow the discount, maybe an activist will come in, and you'll wind up getting it narrowed that way. I frequently feel that the closed-end fund industry kind of doesn't embrace the fact that this is a benefit, or a potential benefit, as opposed to it's a negative.

MIKE TAGGART

So I mean, I think there's different types of discounts, right? There's a type of discount where a fund trades at a wide discount for a fund-specific reason. There's a fund-specific reason that investors stay away from the fund, right? And then there's another type of discount that reflects sentiment, market sentiment about what the fund actually invests in, right? And any other type of consumer product, if you can get it at a discount, you want to get it. I mean, look, that was how Amazon got its start, right? Selling everything cheaper than what you could get at a store. But to your point, like, there's a hesitancy necessarily to do that, because if you start broadcasting the fact that your fund's trading at a wide discount, you're basically asking institutional investors who get involved in activism involving your fund. So that's why the industry as a whole kind of shies away

from doing that. But certainly, like, when I'm speaking with investors, if a fund's trading at a discount that I don't believe is fund-related, then that's definitely, to me, a selling point for me to throw out there during the conversation.

CHUCK JAFFE

I do understand, because I talk to managers all the time, that, like, "Yeah, I don't really want to talk about that discount. I haven't figured out how I'm going to narrow it, and I don't want to alert the entire world that, like, wow, it's oversized right now. Come in and create problems."

MIKE TAGGART

Right? Yep.

CHUCK JAFFE

And then finally, and this one, I actually called you out in my talk because you have a background at Morningstar, and I don't want you to talk necessarily about Morningstar, but I do want you to talk about the idea that closed-end funds are generally not included with fund ratings. Not just Morningstar's, but Lipper will assign numerical values, but CFRA Research, which does extensive fund research, does nothing on closed-end funds. Morningstar gives them a star rating, but hasn't done any analyst reports or anything else analytical on them since 2022, when they formally stopped. When you then put closed-end funds in other categories, like they're their own category, so they don't get measured alongside a traditional fund or an ETF, I think it makes it that the consumer gets an incomplete picture, and, oh, by the way, goes with what is more mainstream. So how do we get the rating agencies to do what would be intellectually honest? To just say, "Hey, we're going to rate all funds, put them all in the same pool, and then do the analysis that says, 'Hey, this is a better value because it's on sale, or because whatever. This is a worse value because it's got a higher cost structure.'"

MIKE TAGGART

Yeah, I mean, I completely agree that it would be beneficial to consumers to have ratings on closed-end funds. The issue you have is leverage. Most closed-end funds use leverage, and leverage increases risk, increases volatility, both on the NAV of the fund and on the price. So I think a rating, when you're rating them, you have to say, well, look, do we rate it based on the NAV, which is the underlying thing, right? Or do we rate it based on the price, which is what the client and end investor actually gets? So you have to make that determination, and then once you make that determination, and frankly, for me, I would use price, then you have to say, okay, well, then how do we lump these all together with open-end mutual funds, exchange-traded funds? And do we include interval and tender offer funds? I would not include interval and tender offer funds.

CHUCK JAFFE

I would agree with that.

MIKE TAGGART

And then you have to create proper categories, right? But, like, if we just were to use Morningstar for an example, they all have the categorizations already. But Morningstar doesn't lump closed-end funds in with open-end mutual funds or exchange-traded funds. They just rate them separately, closed-end fund against closed-end fund. So if you have, I think it's five closed-end funds in a category with three years of history, then you can get a star rating. But that's kind of intellectually dishonest, because you're rating five funds against each other. And I believe that they also are now including interval funds and tender offer funds in with closed-end funds in a category, which doesn't make any sense. But if you were to do that, I did this experiment before: if you were to lump all open-end funds, ETFs, and closed-end funds together, and look at them on their volatility-adjusted, risk-adjusted returns, which the risk-adjusted returns would take into account the leverage, most closed-end funds would be five-star rated. But they aren't, right? They aren't rated that way, so unfortunately, clients can't see. So you could have a very lowly rated fund that outperforms a very highly rated fund. So whatever rating agency would eventually, hopefully, take this on would have to take all of that into consideration, right?

CHUCK JAFFE

Yeah, but it's all doable. That's the thing. And again, if you put it together, and you have done the research to say, "Wait, the closed-end funds would be the five-star funds," that changes the conversation, and there's got to be a way to do it. I don't know which comes first, the demand for it, or what's driving the demand.

MIKE TAGGART

You know, I mean, there's a couple of things, right? So one of the things that closed-end funds benefit from is the permanent capital, right? They're not taking in fresh cash at the top of a market when everybody's excited about this segment of the market, and then having to put it to work. And they're also not forced to sell at the bottom of the market, when everybody's, like, upset about the performance and they're selling, and then the fund has to sell, right? So it's permanent capital. They can just stay invested through the highs and the lows. So that's one of the things. And then the second thing is, like, from a business perspective, right? I mean, closed-end funds are such a small and a niche area of the market. Like, you're probably not going to make a lot of money by including closed-end funds in your ratings. But it would be a nice thing if somebody were to do it, because I do think it would help out the closed-end fund industry tremendously.

CHUCK JAFFE

Well, and again, it would be intellectually honest as we're looking at funds, and we're looking at them all, and we're including them all. Mike, great stuff. Thanks for joining me.

MIKE TAGGART

Yeah, thanks for having me, Chuck. It's always a pleasure to talk to you.

That's Mike Taggart. He is head of closed-end fund investor relations at Aberdeen Investments. AberdeenInvestments.com to learn more about the firm and its funds. The Navigator is a joint production of the Active Investment Company Alliance and MoneyLife with Chuck Jaffe. And yeah, that's me. And if you want to learn more about my show, go to MoneyLifeShow.com or search for it on your favorite podcast app. To learn more about the Active Investment Company Alliance, to make sure you don't miss their next events, go to AICAlliance.org. That's their website. The Navigator's here for you every Friday. Follow along on your favorite podcast app so that you get in on all of the closed-end fund fun. We'll be back again next week. Until then, happy investing, everybody.

Mike Taggart is head of closed-end fund investor relations at Aberdeen Investments. Learn more about the firm and its funds at AberdeenInvestments.com. Visit AICAlliance.org for more on BDCs, closed-end funds, and interval funds.

Click the link below to go to the home page of Active Investment Company Alliance to learn more: https://AICalliance.org/

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