Digging Into Lesser-Known Interval Fund Picks With John Cole Scott

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Chuck Jaffe, in this episode of The NAVigator podcast interviewed John Cole Scott, President of Closed-End Fund Advisors and the Chairman of the Active Investment Company Alliance. Read the Q&A below as John discusses interval funds and digs into the data on four funds that use the structure to create promising investment opportunities for investors. Plus, learn about the NAVigator Podcast's first-ever contest, in celebration of its fifth anniversary!

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

Dig into current investment strategies, the latest trends, and new developments in the closed-end fund industry at the Active Investment Company Alliance's Annual Roundtable. The event now in its sixth year is Wednesday, November 13th in New York City and will combine informative panels, engaging speakers, and valuable networking opportunities with leaders in closed-end funds, interval funds, and business-development companies. AICA events are known for their high-quality advisor-centric content and for enabling meaningful discussion and interaction with the top minds in closed-end funds. Advisors can get seven CE credits for attending. Go to AICAlliance.org/events to get complete details and to see the full schedule, and through Halloween night use the code NAVIGATOR30 for a 30% discount on registration costs.

CHUCK JAFFE: John Cole Scott of Closed-End Fund Advisors is here, we're digging into interval funds and some lesser-known strategies you can tap into using them, 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 Active Investment Company Alliance, a unique industry organization representing 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. And returning to The NAVigator today, John Cole Scott, he is president at Closed-End Fund Advisors in Richmond, Virginia, which is online at CEFAdvisors.com. We are about to dig into interval funds using the firm's research, you can do that yourself, not just about the funds we talk about but about any funds, at CEFData.com. John is also chairman of the Active Investment Company Alliance, which you can learn about at AICAlliance.org. John Cole Scott, great to chat with you again.

JOHN COLE SCOTT: Always good to be here.

CHUCK JAFFE: Now before we dig into interval funds, well, you and I, or you, me, and the Active Investment Company Alliance are kind of celebrating an anniversary, as The NAVigator just passed its fifth birthday.

JOHN COLE SCOTT: Yes, it's been a great five years, it's been a lot more fun than I ever imagined.

CHUCK JAFFE: To celebrate, we're going to have a contest, and the prize is a classic that is near and dear to your heart.

JOHN COLE SCOTT: It is, it's my father's 1991 book on closed-end funds he co-authored called *Closed-End Funds: Finding Value and Building Wealth*, and there's not many copies left and we thought it'd be fun to share it with some of our passionate audience.

CHUCK JAFFE: And I'm going to point out, John's father, the late George Cole Scott was a legend, an absolute legend in the closed-end fund world. You could not have done my job as a journalist without talking to him if you were going to do anything in the closed-end fund space, and his book, though now more than 30 years old, the fundamentals are all still there. So to be entered in a drawing to win the book, you need to answer a simple question; in what year did closed-end funds trade on the New York Stock Exchange for the first time? Send your answer along with your name and address to Chuck@MoneyLifeShow.com by noon

Eastern time on October 22nd to be entered for the book. We'll announce winners on the October 25th edition of The NAVigator. John, now let's get to the business at hand, which is looking at interval funds. It's funny because I think most people hear about interval funds and they think it's all about the structure, they don't think that it's all about the holdings, but there are a lot of ways that interval funds are being used these days, some of which are pretty appealing to you, aren't they?

JOHN COLE SCOTT: There are, and we recently just surpassed 110 interval funds in CEF Data and just over $103 billion in assets, and really thought it'd be fun to look at three very different interval funds and how they're using the wrapper and giving products that to my opinion really couldn't live in an ETF or traditional closed-end fund wrapper and could be compelling for different investors.

CHUCK JAFFE: Well, let's dig into what you found. You've picked out four very different funds to talk about today, help us understand what you're looking at and what makes them particularly interesting to you.

JOHN COLE SCOTT: Happy to. So the first one is the First Eagle Credit Opportunities Fund, it's FECRX, its inception date is back in September of 2020, it's getting close to $900 million in assets, it's giving you basically about a 10% yield with only about 9% leverage. The management fee, which is not the only part of the expense ratio but the one we focus on a lot here, is only 1.25%, and just giving a benchmark through the first three quarters of 2024, it's up about 6%. When you look into the style of the portfolio, it's high current income based on that yield, it's a US alternative credit fund and it really focuses on first-lien senior secured holdings, kind of like a BDC but not using the BDC wrapper, and there's 225 issuers with over 400 holdings. As you might imagine for that style of investment, the duration profile is under 0.35.

CHUCK JAFFE: Because you mentioned, it's kind of like the BDC structure, what is the benefit of holding an interval fund for those kinds of assets rather than using a BDC? Is there a specific benefit to the interval style?

JOHN COLE SCOTT: Really for those investors that are comfortable with not necessarily having daily or possibly even quarterly liquidity, you drop a lot of the volatility associated with it, and so the fee structure's a lot lower than you would get in the BDC, even a non-traded or private BDC, but you don't have to worry as much about discount direction. But again, we love closed-end funds because of liquidity, but this is a great way to get those types of interesting credit exposure and not have to worry about as much volatility should you be a volatility thoughtful investor.

CHUCK JAFFE: So again, First Eagle Credit Opportunities, FECRX the ticker symbol there. What's next?

JOHN COLE SCOTT: Next one is the Cantor Fitzgerald Infrastructure Fund, CFIIX, it was incepted in July of '22, it's getting close to $200 million in assets. It's more of an equity style fund, the yield's only 4%, the management fee is about 1.5%. Year to date though it's been a very good year for that sector as your audience may be aware, it's up 18% year to date, and you look at the portfolio, it's 70% roughly private infrastructure focused and 30% public securities. Now remember, interval funds need to maintain about 20% in relatively liquid securities for that 5% a quarter typical redemption process, and that's a great use of the same manager, the manager's in the same sector but in the listed and the private structure and it's 90% US-focused. There are 48 public or listed positions, there's seven private funds, but those seven private funds give exposure to around 5,000 underlying private holdings, and the thesis of the management team there is the digital transformation, the energy transition, and enhancement of aging current infrastructure.

CHUCK JAFFE: On my show *Money Life* we recently were talking with some folks who were infrastructure investors. Is there a benefit to owning infrastructure plays in an interval structure as opposed to traditional open-ended mutual funds?

JOHN COLE SCOTT: The main thing here is if you were looking to go beyond the listed infrastructure components of a sizeable level you will not be able to find 70% private infrastructure unless you go to a private equity fund or other hedge fund structure where the fees are higher and liquidity is even less traditionally than the interval fund wrapper. Now for example, there's a listed closed-end fund ASGI, it's got 15% private exposure as a goal for the management team and 85% public, because you could not trade well in our experience to have so much private even in a listed closed-end fund.

CHUCK JAFFE: Again, CFIIX, Cantor Fitzgerald Infrastructure Fund. We're halfway there, who's next?

JOHN COLE SCOTT: Well, you know, we talked about an emerging market fund recently on The NAVigator, well, there's a PIMCO Flexible Emerging Markets Income Fund, an interval fund structure, it was launched back in March of 2022, it is newer but it's like the third or fourth PIMCO interval fund, they've had a lot of success growing that platform. It's only $15 million, but I imagine it will gain traction well, the yield is very durable at 6.3%. Common with interval credit funds, the leverage is down around 20%, lower than typical, the management fee is also very accessible, 1.3%. It's up the first three quarters of the year about 12%, and as a focused portfolio the top 10 holdings are just under 20% exposure, and it's 80% emerging markets by focus, and a big focus as usual for interval funds in the private access to emerging markets and not worrying as much about frontier exposure in all the markets that could make the net asset value tougher to evaluate and discounts possibly large. And the management team really talks about the interval fund wrapper allowing flexibility to structure lending in a way that can insulate against some of the historical risks that are observed in emerging market countries which include defaults, capital controls, and currency depreciation. It's a great use that's not yield-hungry to use the interval fund wrapper for more of a total return, active management approach.

CHUCK JAFFE: Since you mentioned that we covered an emerging markets fund in The NAVigator recently, how should somebody compare an interval fund in that space with a closed-end fund in the space? I mean, obviously there's the discount and all the rest, and it's a bit of an apples and oranges comparison, but is an asset allocation and our portfolio is a bit of fruit salad.

JOHN COLE SCOTT: It is, and so I would say at CEF Advisors we use interval funds, zero for some clients, five to 10 for a middle amount, and the higher volatility focused clients, it can be 20-30% of the portfolio. You would be looking to put that in that portfolio, and if you want it again, as I said before, the other funds, more private or less liquid exposure. The fund that we talked about previously was a large discount because it was maybe an out of favor sector, it's not been the strongest market in the recent times, and so there's discount upside with that fund. This one doesn't have discount upside, but don't worry as an investor, there's also no discount downside either, and so it's a complementary fund based on the volatility and the underlying assets, and I think it's been a good way to complement and to add in a more balanced approach to what typically drives listed closed-end funds which is yield, yield, yield. If a listed closed-end fund only yielding 6% in the sector, it'd be a terrible discount and would not trade well, you typically need a much higher yield to trade better in a listed fund. This is a more real, durable, actual yield of the underlying holdings.

CHUCK JAFFE: So again, that was EMFLX, PIMCO Flexible Emerging Market Income Fund. Flex is in the next one too because your next one I know is VFLEX, the First Trust Alternative Opportunities Fund, tell us about that.

JOHN COLE SCOTT: First Trust acquired it I believe about three years ago, maybe four. It goes back inception date to June of 2017, and with their backing they've really built it up to about $1.5 billion dollars, and their yield of about 7% really feels more like a managed distribution that kind of targets that level in the dividend file, it's not moving around a lot. The management fee is sitting around 1%, which I suspect is based on the legacy fee structure in the original prospectus, so a benefit for all shareholders. Year to date, because it's really a fund of funds, it's not one sector, it's only up just under 8%, and it can go roughly a third into all these categories but right now it's 10% private equity, kind of a natural underweight in this market, it's 12% real estate, it's 18% alternative credit, it's 20% hedge strategies, and it's almost 40%, the largest share, direct co-investment, an area that you don't easily see in other regular funds. The top 10 holdings, it's relatively diversified, about 28%, funds are 87% of the holdings and then real estate exposure or buildings are 13% of the holdings. And what's additionally fascinating, as I dug into the strategy, they have the liquid strategies, the biggest bucket shouldn't be surprising potentially, it's CEF arbitrage to maintain that liquid bucket for redemptions, a chance to use listed closed-end funds in the portfolio for probable performance relative to ETFs to create alpha potentially and keeping a liquidity profile there while a really durable diversified multi-sector manager fund.

CHUCK JAFFE: Again, a huge part of the advantage, interval fund to traditional fund here is the strategies you're going to get into, alternatives mean a lot of things and there's a lot of alternative funds, but you can go more alternative, if you will, by going the interval route.

JOHN COLE SCOTT: Yes, you can go more alternative with interval funds than traditionally in listed closed-end funds, and we use both at the firm though we have a lot of interest in the listed funds. We recognize the volatility can scare some investors, and we think the growth of interval funds, adding complementing strategies, traditional ETFs both active and passive has been really wonderful and beautiful for our universe of funds at CEFData and CEF Advisors.

CHUCK JAFFE: John, great stuff as always, looking forward to doing the next five years with you, but I'm sure I'll talk to you well before that. Thanks again for joining me on The NAVigator.

JOHN COLE SCOTT: Yes, it's been a pleasure.

CHUCK JAFFE: The NAVigator is a joint production of the Active Investment Company Alliance and Money Life with Chuck Jaffe. I am Chuck Jaffe and you can learn more about my work and my show on your favorite podcast app or by going to MoneyLifeShow.com. To learn more about closed-end funds, business-development companies, and interval funds go to AICAlliance.org, it's the website for the Active Investment Company Alliance, on Facebook and LinkedIn @AICAlliance. Thanks to my guest John Cole Scott, he's president of Closed-End Fund Advisors in Richmond, Virginia, and he's the chairman of the Active Investment Company Alliance. His firm is online at CEFAdvisors.com and you can dig into their data for yourself by going to CEFData.com, and John is on X or Twitter @JohnColeScott. Remember, we've got a contest going, tell us when the first closed-end funds started trading on the New York Stock Exchange and send that to Chuck@MoneyLifeShow.com. The NAVigator's available for you every Friday and we'll be back next week. We can't wait to see you then, and until then, happy investing, everybody.

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TheNAVigator@AICalliance.org

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