CLOSED-END FUND REVIEW

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FOURTH QUARTER 2024 OVERVIEW

Following three straight positive quarters for closed-end funds (CEFs) in 2024, the average CEF was lower by -1.68% during the fourth quarter of the year. The fourth quarter was a mixed one with equity CEFs up on average +1.18%, while taxable fixed-income CEFs were lower by -1.58% and municipal CEFs were lower by -5.48%. Despite the negative average return for the fourth quarter of the year, 2024 ended up being a very positive one for many CEFs. For the year, the average CEF returned a robust +15.30%. This represented the second consecutive year CEFs returned double digits as the average CEF was up +10.55% in 2023.

It was a broad rally in 2024 with the average equity CEF returning +21.23%, taxable fixed-income CEF returning +15.16% and municipal CEF returning +6.62%. (Source: Morningstar. All data is share price total return.) During 2024, equity CEFs benefitted from the +25.00% return in the S&P 500 Index and the +6.09% gain in the MSCI ACWI ex USA Index. Taxable fixed-income CEFs benefitted from positive returns in several key fixed income indices. For 2024, the ICE BofA US High Yield Constrained Index gained +8.22%, the Morningstar® LSTA® Leveraged Loan Index returned +9.01%, the ICE BofA Fixed Rate Preferred Securities Index gained +7.06% and the Bloomberg US Aggregate Bond Index returned +1.25%. For the year, municipal CEFs benefited from the +0.40% return in the ICE BofA 7-12 Year US Municipal Securities Index and the +6.32% gain in the Bloomberg Municipal High Yield Index. (Source: Bloomberg)

Average Discounts to Net Asset Value Widen Slightly During the Fourth Quarter but Narrowed in 2024

Average discounts to net asset value (NAV) widened slightly during the fourth quarter to -5.99% from the -4.44% level they ended on 9/30/2024. While average discounts widened slightly during the quarter, they did narrow significantly during 2024. The -5.99% average discount on 12/31/2024 was noticeably narrower than the -9.63% level they ended on 12/29/2023. Average discounts to NAV are slightly wider than the 10-year average discount to NAV of -5.84%. It was encouraging to see average discounts to NAV narrow during 2024. CEF investors who were disciplined and dollar cost averaged during the challenging periods of 2022 and part of 2023 are seeing the positive benefit of having purchased CEFs when average discounts to NAV were high single and low double digit levels.

Average discounts to NAV for equity CEFs widened during the fourth quarter to -7.76% from the -7.19% level they ended the 3Q. However, for the year they narrowed from the -10.86% level they ended on 12/29/23. Average discounts to NAV for equity CEFs are slightly wider than the 10-year average discount of -7.24%. Taxable bond CEFs ended the fourth quarter at an average discount of -1.10%. This was slightly wider than the +0.14% premium they ended the third quarter, but meaningfully narrower than the -5.57% level they ended on 12/29/23. The 10-year average discount to NAV for taxable bond CEFs is -4.55%.

Among these broad categories, the widest discrepancy between current discounts to NAV relative to the long-term average remains in the municipal CEF category where average discounts to NAV ended the fourth quarter at -8.97%. This is wider than the -5.60% level they ended on 9/30/24 but narrower than the -12.39% they ended on 12/29/23. While average discounts for municipal CEFs did narrow during the year, they remain far wider than the 10-year average discount of -5.24%. (Source: CEFData.com) If the Fed continues to lower short-term interest rates in 2025, I expect average discounts for municipal CEFs to narrow and potentially trade at discounts which are narrower than the long-term average.

Outlook for 2025

As 2025 commences, my outlook for the CEF structure has not changed meaningfully from my prior commentary piece in October of 2024. I believe the backdrop for the CEF structure remains solid. The Federal Reserve (the "Fed") began the process of reducing short-term interest rates in 2024 and will likely continue to lower short-term rates in 2025. This helps to create a solid backdrop for many CEFs as many funds employ the use of leverage. As the Fed reduces short-term interest rates, borrowing cost for levered CEFs trend lower which is expected to lead to improved earnings rates and could potentially lead to distribution increases or lead CEFs to payout less return of capital in their current distributions. In my view, both of these potential outcomes are positive. Furthermore, while average discounts to NAV narrowed in 2024 from 2023 levels, many CEFs are still trading at discounts to NAV which are wider than their historical average.

In addition to the Fed potentially further reducing short-term rates and attractive valuations for many CEFs, another potential positive for the CEF structure for 2025 relates to the increase in demand and improved sentiment we could see if overall interest rates decline and yields on competing income-oriented investments including CDs, money market funds, U.S. Treasuries etc. decline. If competing and alternative rates decline this year, investors may be more likely to consider the CEF structure given the very high and attractive distribution rates that exist in the secondary market for CEFs. As of 12/31/24, the average CEF had a distribution rate of 8.92%, according to Morningstar.

In summary, I believe the backdrop for many CEFs- particularly leveraged fixed income CEFs including municipal and preferred CEFs- is solid and will likely continue to improve throughout the year and discounts will likely continue to narrow. I advocate for CEF investors to remain disciplined and dollar cost average across many categories including but not limited to diversified equity CEFs, municipal CEFs, preferred CEFs, and high yield CEFs.