

Closed-End Fund Review

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Second Quarter 2026 Overview

Following a quarter in which the average closed-end fund (CEF) was lower by -0.96%, many CEFs rebounded strongly in the second quarter. The average CEF gained +7.24% for the quarter and is now up +6.23% year-to-date (YTD) through June 30, 2026. It was a broad rally with equity CEFs gaining on average +10.64%, taxable fixed-income CEFs rising +4.66% and municipal CEFs adding an average of +5.48%. (Source: Morningstar. All data is share price total return)

Equity CEFs benefitted during the second quarter from the +15.20% gain in the S&P 500 Index as well as the 14.49% gain in the MSCI ACWI ex USA Index. Taxable fixed-income CEFs got a boost from positive total returns in several key fixed-income indices. For the second quarter, the ICE BofA US High Yield Constrained Index was up +2.45%, the Morningstar® LSTA® US Leveraged Loan Index gained +1.88%, the ICE BofA Fixed Rate Preferred Securities Index added +1.58% and the ICE BofA Global Corporate Index increased +1.49%. (Source: Bloomberg) Municipal CEFs benefitted from the second quarter gain of +2.26% in the S&P National AMT-Free Muni Bond Index. (Source: S&P Dow Jones Indices)

Average Discounts to Net Asset Value (NAV) Narrow Slightly During the Second Quarter

Average discounts to NAV for all CEFs narrowed slightly during the second quarter to -5.99% from the -6.49% level they ended on 3/31/2026. Average discounts to NAV ended the second quarter wider than the 10-year average discount to NAV of -5.52%. Average discounts to NAV for equity CEFs narrowed slightly during the second quarter to -7.18% from the -7.55% level they ended on 3/31/2026 and are wider than the 10-year average discount to NAV of -6.64%. Average discounts to NAV for taxable fixed-income CEFs narrowed slightly during the second quarter to -6.70% from the -6.82% level they ended on 3/31/2026 and are meaningfully wider than the 10-year average discount to NAV of -4.08%. Municipal CEFs are the only broad category of CEFs where average discounts to NAV are narrower than the long-term average. Average discounts to NAV for municipal CEFs narrowed during the second quarter to -2.35% from the -3.72% level they ended on 3/31/2026 and are narrower than the 10-year average discounts to NAV of -5.45%.

I continue to believe that if the Federal Reserve were to lower short-term interest rates during the second half of 2026 or in early 2027, we could see average discounts to NAV narrow further, particularly for fixed-income CEFs, as they potentially benefit from lower leverage costs and increased demand from investors.

Historical Importance of CEF Distributions; Outlook for Second Half of 2026

Albert Einstein once said, "Compound interest is the eighth wonder of the world. He who understands it, earns it. . . he who doesn't. . . pays it." Long-term investors in the CEF structure are very much aware of this principle as historically, a significant percentage of the total return generated by CEFs has come from the compounding of distributions. I have written about this topic before, but I think it is important to reexamine the data periodically, as I firmly believe the compounding of CEF distributions illustrates the benefits of long-term, diversified investing in CEFs.

The First Trust Composite Closed-End Fund Index is composed of the municipal, taxable fixed-income and equity indexes and is intended to provide a capitalization-weighted representation of the entire U.S. closed-end fund universe. There are two versions of this index. The First Trust Closed-End Fund Composite Total Return Index (UPCEFT) which includes distributions and the First Trust Closed-End Fund Composite Index (UPCEF) which excludes distributions. The difference in returns for these two indexes over the past 17 years is dramatic. From 12/31/2008 to 12/31/2025, UPCEF only had an average annualized return of 0.84%. Not terribly impressive. However, when we include distributions and use UPCEFT, the average annualized return jumps to a much more impressive 9.13%. (Source: Bloomberg) This data point clearly illustrates the historical importance of CEF distributions and shows how the majority of the total return that CEFs have earned over the past 17 years has come from the compounding of the distributions. In short: CEF distributions matter and this is why I believe it is critical to think in terms of total return when analyzing the performance of an individual CEF or a portfolio of CEFs.

As the second half of the year gets underway, I believe the backdrop for diversified CEF investors remains a good one. Valuations for many CEFs are compelling as they are trading at discounts to NAV that are more inexpensive (wider) than their long-term average (see above), the U.S. economy continues to grow at a modest pace and CEFs that employ the use of leverage have seen a gradual decline in borrowing cost following the three consecutive cuts in short-term interest rates at the end of 2025. As I have written in prior CEF commentary pieces, I favor equity, municipal and preferred CEFs.

Source for CEF performance: Morningstar. All performance is based on share price total return.

Past performance is not a guarantee of future results. All data as of 6/30/26, unless indicated otherwise.

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