

NYSE INTERVIEW · MONDAY, JUNE 8, 2026

## How John Cole Scott Is Reading the BDC Sell-Off

*A Conversation on Private Credit, AI Risk, and Where Listed BDCs Go From Here*



**John Cole Scott**  
President & CIO  
CEF Advisors

In this interview from the New York Stock Exchange, John Cole Scott, President & CIO of CEF Advisors, breaks down the sharp sell-off in business development companies (BDCs) amid AI fears, renewed scrutiny of private credit, and broad market volatility. The conversation explores what the data actually shows beneath the headlines — from non-accrual trends in software-heavy portfolios to a new AI risk score across the listed BDC universe — and where relative value may exist today.

### TOPICS DISCUSSED

- The peak-to-trough pullback in listed BDCs and what's driving it
- Floating-rate dynamics as interest rates decline
- AI as both a tailwind and a headwind for portfolio companies
- A new AI risk score across ~5,000 listed BDC holdings
- Manager quality, loan structure, and covenants vs. headline AI risk
- Historical forward returns from comparable discount levels
- Discounts, dividend sustainability, and after-discount yields

### HOW CEF ADVISORS POSITIONS BDC EXPOSURE

1. Tactical, more premium names (often internally managed)
2. Median-level BDCs trading relatively well
3. Cautiously strategic, deeper-discount opportunities

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.

**EXPLORE THE DATA REFERENCED IN THIS INTERVIEW:**

- Free CEF & BDC profile pages: [cefddata.com](https://cefddata.com)
- 40+ CEF & BDC indexes: [cefddata.com/index](https://cefddata.com/index)

*Powered by CEFDData, offering transparent data on U.S. listed closed-end funds, BDCs, interval funds, and ETFs.*

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## THE CONVERSATION

### JANE KING

John Cole Scott is a 25-year industry veteran and second-generation leader in the closed-end fund, business development company, and interval fund landscape. As President and CIO of CEF Advisors, he manages customized, income-focused portfolios for high-net-worth investors, specializing in risk mitigation and tax optimization. So, John, great to have you back in New York and at the Stock Exchange.

### JOHN COLE SCOTT

Always great to be here with you, Jane.

### JANE KING

Well, we've seen a sell-off in a lot of things, but BDCs are one of them. There have been AI fears, private credit is under attack again, and there are a lot of worries in the markets. So how do you see it? How bad is it really?

### JOHN COLE SCOTT

Yes. When we look at the market, the peak-to-trough pullback in listed BDCs is about 23% from back in February of 2025, and we really see a couple of factors there. There's been a reduction in interest rates, which has brought some of the yields down, because that's the nature of a floating-rate investment product like a business development company.

### JOHN COLE SCOTT

We've also seen the software sector — which historically has been about 30% of the net asset value of BDC portfolio holdings — go from almost a zero non-accrual, or non-performing loan, bucket to now about 50 basis points. There's now actual risk in software, since AI is adding value and tailwinds to some companies but creating challenges and headwinds for others. And because BDCs are generally retail-owned, they're hard for many institutions to own because of the tax issues, the AFPE (acquired fund fees and expenses), and other concerns.

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**JOHN COLE SCOTT**

It's really just been a matter of looking into the portfolios and, through our research, realizing that we don't see as much risk as the market suggests — with discounts down to about 18% for our CEF Advisors equal-weight BDC index. We're really modeling what's been happening at the structure level and the holdings level and comparing it to back in 2015–2016 and that energy pullback.

**JANE KING**

So, software — there's some debate about how much it's impacted by AI. Some call it a “SaaS-pocalypse,” others say it's overdone. What do you think?

**JOHN COLE SCOTT**

It is a debate. And honestly, the fact that we're a nimble firm means we're diversified in how we use BDCs for our client portfolios. I think I've shared this with you before, Jane: we're doing roughly a 1% allocation, maybe 2%, and two-and-a-half to 3% if we're very convicted. So these are not taking over the portfolio, but they're a significant sector for income clients.

**JOHN COLE SCOTT**

Really digging in, we thought it would be interesting — earnings season wrapped up about three weeks ago for the first quarter — so we dug into the portfolios. We asked: okay, how are the better-performing names doing versus the worst? We use return on equity, ROE, as that measurement — the 18 best and the 18 worst. And we have a new data point since I last saw you, Jane: an AI risk score for every portfolio holding, about 5,000 across the listed BDC universe. We rate them from one to 10 through a matrix of durability.

**JOHN COLE SCOTT**

We found that the best ROE portfolios versus the worst had almost the same AI risk score, which led us to believe that, while AI is a risk, there's a risk in every investment a BDC makes. It's much more important how the manager structured the loan — what the covenants on the loan were, and whether, if there's a problem, their team can assist these portfolio companies. You may not remember this, but one of the caveats Congress built into the BDC structure back in 1980 was for these managers to be an assistant and a partner to these companies — hopefully to help them thrive and grow through problems. So we found that it's far less about AI risk, in our opinion, and far more about a good manager who can usually get paid back — which, as we've always said, is what's important for a BDC.

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JANE KING

Okay, very interesting how much you dug into that data. That's your breaking news — it's the first time I've heard that. That's amazing. So where does it go from here? What do you think?

JOHN COLE SCOTT

Yeah, so we try to figure out what's next. In the past — and this isn't an exact mirror of what happened in 2015–2016 — we saw recoveries after the net asset value bottom. Looking forward historically — and this is not guaranteed — from the trough, which we think we've hit, though we'll know more in six months, we've seen 40% median forward returns the three times BDCs went from this level.

JOHN COLE SCOTT

So, if you were to go back to August of 2021, the listed BDC universe was at a 12% premium with an 8.3% yield. Today we're seeing an 18% discount — significant, about 30% lower — and a 13% yield. However, we recognize there are some credit issues. Credit losses will probably be higher in the next six to 12 months than in the last three years, but we still see dividends staying above 11% in current dollar terms.

JOHN COLE SCOTT

We expect recoveries to happen — probably getting their footing at the end of the next earnings season, but possibly the one after. We really need the market to prove that these good managers are actually holding conviction and supporting their companies in a powerful way, which then gives the market a chance to breathe. At the same time, BDCs are down 20% in price over the last 12 months, while the S&P equal-weight is up, I think, 17%, and the regular S&P is up 23% — and all of them have software in them. I'm much more comfortable over allocating to things that are down a lot versus things that are up a lot, for our income clients.

JANE KING

Well, an 11% dividend is still very nice.

JOHN COLE SCOTT

It is, and some of them could be higher. But we also consistently recommend that you don't just sit on the deepest discount and the highest yield. That's usually the market telling you something about the dividend. There are 20% dividends out there, or 18% dividends are probably not. And there are discounts wider than 30% that are rarely easily recoverable.

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**JOHN COLE SCOTT**

So, we really do three things for our clients at CEF Advisors. We buy some tactical, more premium names — sometimes internally managed BDCs; versions of that would be Capital Southwest or Trinity Capital, which we may not own right now, but they're good managers, and we try to position at the right time. Then there are the median-level BDCs that are trading relatively well, like an Ares or a Blackstone. And then there are some I'd call cautiously strategic, deeper discounts — names like that that we use for our clients. So, it's not just the deep ones, and it's not just the best ones. We try to sift through the data every quarter and pick our spots — plan for earnings season, react to an earnings season, and then plan and review for the next earnings season.

**JANE KING**

Okay, John, thank you so much for your insight. Always great to hear it.

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