AUGUST 31, 2013

The Month in Closed-End Funds: August 2013

PERFORMANCE

At the beginning of August some investors breathed a sigh of relief after the jobs report fell short of forecasts, coming in at just 162,000 for July compared to the analyst consensus of 180,000. The Dow Jones Industrial Average (DJIA) and the S&P 500 actually rallied on the news, recording their thirtieth and twenty-fifth record closes, respectively, as investors interpreted the employment results as being too soft for the Federal Reserve to reduce its asset purchases in September. To many investors' chagrin, however, economic news released later in the month was stronger than expected, spooking investors and causing Treasury yields at maturities greater than one year to rise for the month. Increased tensions in the Middle East and saber-rattling by the U.S. concerning the reported chemical weapons attack by the Syrian government on its own people pushed commodity prices higher and stocks lower as the world waited to see President Obama's response to the attacks. Low volume in the last weeks of summer, tapering fears, a three-hour NASDAQ trading glitch, spikes in Treasury yields, and late talks about the looming debt ceiling brought about the worst monthly equity fund returns in 16 months. Lipper's equity CEF macro-group posted its first set of negative returns since June, losing 2.33% on a NAV basis and 3.28% on a market basis. And, pulled down by continued rising-interest-rate fears and a hangover from the Detroit bankruptcy filing, it wasn't surprising to see fixed income CEFs post their fourth consecutive month of negative returns, losing 2.05% on a NAV basis and 2.03% on a market basis for August.

Despite the DJIA and the S&P 500 reaching record closes early in the month, they both posted their worst monthly returns since May 2012, with the DJIA returning minus 4.45%, while the S&P 500 lost 3.13% for the month. Both indices remained solidly in the black for the year-to–date period, returning 13.02% and 14.50%, respectively.

In the middle of the month speculation that the Fed would begin tapering its bond purchases as early as September sent Treasury prices spiraling, and yields approached their highest levels since 2011. The ten-year Treasury yield rose to 2.90% on August 22, before falling back to close at 2.78% on August 30, 18 basis points above the July closing value. The 135-bp increase in yield since its low on July 26, 2012 (+1.43%) represented an amazing 94% increase in yield in just over a year. At maturities of one year or greater the Treasury yield curve shifted upward, with the five- and seven-year yields rising the most—24 bps each to 1.62% and 2.24%, respectively, on August 30. Much as in July, the selloff in Treasuries also led to a significant selloff in municipal debt funds as investors contemplated the Fed's next move, future tax reforms, and the credit risk of municipalities.

For August the dollar weakened against the pound (-1.89%) and the yen (-0.18%), but it gained against the euro (+0.64%). Once again, commodities prices were on the rise for the month, with the near-month crude oil price gaining 2.49% to close the month at $107.65/barrel. Gold prices continued to strengthen, gaining 6.38% to end the month at $1,396.10/ounce.

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- For August only 12% of all closed-end funds (CEFs) traded at a premium, with 13% of equity funds and 12% of fixed income funds trading in premium territory to their NAVs. Both the taxable bond funds and municipal bond funds macro-groups witnessed a narrowing of discounts for August.
- For the second month in three all of Lipper's equity CEF and fixed income CEF classifications were in the red.
- For the fourth consecutive month all of the municipal bond fund groups posted returns in the red, with single-state municipal bond funds (-2.97%) mitigating losses slightly better than their national municipal debt fund brethren (-3.10%).
- Equity funds tied to interest rate-sensitive issues (such as mortgages) and India Region plays lagged the other equity classifications, pushing Real Estate Funds (-5.51%), Emerging Markets Funds (-4.47%), and Value Funds (-2.78%) to the bottom of the pack.

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CLOSED-END FUNDS LAB

For August only 8% of all CEFs posted NAV-basis returns in the black, with 10% of equity CEFs and only 7% of fixed income CEFs chalking up returns in the plus column. For just about the entire month hand wringing over the timing of the Fed's future tapering cast a pall over the markets. And late-month worries over Syria, the U.S. approaching its debt limit in mid-October, the NASDAQ glitch, and the rise in the Chicago Board Options Exchange Volatility Index (VIX) kept investors on the sideline and ducking for cover. Despite hearing upbeat news concerning German and U.K. GDP data, investors generally focused on how the Fed tapering might impact the global economy. The concerns pushed the World Equity CEFs macro-group to the bottom of the barrel (-2.61%), underperforming both the domestic equity CEFs macro-group (-2.27%) and the mixed-asset CEFs macro-group (-2.10%).

For the second month in three all of Lipper's equity CEFs and taxable fixed income CEFs classifications were in the red (something we haven't seen since October 2008). Given the spike in Treasury yields and the impact on spread products, it wasn't surprising to see the municipal bond funds macro-group (-3.04%) pushed to the bottom of the fixed income group, underperforming taxable domestic bond CEFs (-0.59% on a NAV basis) and world bond CEFs (-2.56%).

Only 24 equity CEFs posted returns in the black for August, with 5 of the 10 top funds being housed in Lipper's Sector Equity Funds macro-group. In a late month flight to safety investors bid up the prices of gold (to a three-month high) and oil (rising to over $109 per barrel for the first time this year), while they pushed the yield on the benchmark ten-year Treasury note to 2.72% (down 7 bps in a day). Developed Markets Funds (-1.18%), Convertible Securities Funds (-1.37%, July's leader), and Sector Equity Funds (-1.64%) mitigated losses for August better than the other classifications in the universe. Equities tied to interest rate-sensitive issues (such as mortgages) and India Region plays lagged the other equity classifications, pushing Real Estate Funds (-5.51%), Emerging Markets Funds (-4.47%), and Value Funds (-2.78%) to the bottom of the pack. For the remaining equity classifications returns ranged from negative 2.39% (Income & Preferred Stock Funds) to negative 1.80% (Option Arbitrage/Option Strategies Funds).

Again, five of the ten top-performing individual funds were housed in Lipper's Sector Equity CEFs classification, with the two top-performers being precious metals-related funds. At the top of the chart was **Central Fund of Canada Limited (AMEX: CEF)**, gaining 11.05% on a NAV basis and traded at a 3.50% discount at month-end. Following CEF were **ASA Gold & Precious Metals Limited (NYSE: ASA**, one of July's leaders**)**, posting a 6.81% return and traded at a 6.70%

TABLE 1 CURRENT-MONTH PERFORMANCE, P&D, P&D SHIFTS (% OF UNIVERSE)

	NAV RETURNS POSITIVE	PREMIUM/DISCOUNT		NOW TRADING AT	
		BETTER	WORSE	PREMIUM	DISCOUNT
Equity Funds	10	29	69	13	86
Bond Funds	7	49	49	12	88
ALL CEFS	**8**	**42**	**56**	**12**	**87**

TABLE 2 AVERAGE NAV RETURNS, SELECTED PERIODS (%)

	AUGUST	YTD	3-MONTH	CALENDAR-2012
Equity Funds	-2.33	6.58	-1.93	15.42
Bond Funds	-2.05	-5.50	-7.17	15.04
ALL CEFS	**-2.16**	**-0.81**	**-5.14**	**15.18**

TABLE 3 NUMBER OF IPOs, SELECTED 12-MONTH PERIODS

	AUGUST 2013	CALENDAR-2012
ALL CEFS	**32**	**31**

TABLE 4 AVERAGE SIZE OF IPOs, SELECTED PERIODS, $MIL

3 MONTHS THROUGH 7/31/2013	434
COMPARABLE YEAR-EARLIER 3 MONTHS	528
CALENDAR 2012 AVERAGE	506

Source: Lipper, a Thomson Reuters company discount on August 30; **Morgan Stanley China A Share Fund, Inc. (NYSE: CAF**, housed in Lipper's Pacific ex-Japan Funds classification**)**, rising 6.44% on a NAV basis and traded at an 8.29% discount at month-end; **Central GoldTrust (AMEX: GTU)**, chalking up a 6.00% return and traded at a 4.99% discount at month-end; and **RENN Global Entrepreneurs Fund, Inc. (NYSE: RCG**, housed in Lipper's Global Funds classification**)**, rising 3.50% and traded at a 44.36% discount on August 30.

For the month the dispersion of performance in individual equity CEFs—ranging from minus 12.20% to positive 11.05%—was wider than August's spread and more negatively skewed. The 20 top-performing equity funds posted returns in excess of 0.25%, while the 20 lagging funds were at or below minus 5.51%.

Given the concerns about the Middle East, emerging markets, and the global economy, it wasn't surprising to see **Turkish Investment Fund, Inc. (NYSE: TKF)**, housed in Lipper's Emerging Markets Funds classification, at the bottom of the equity CEF group. TKF shed 12.20% of its July month-end value and traded at a 13.57% discount on August 30. The next poorest performing equity fund was warehoused in Lipper's Pacific ex-Japan Funds classification: **Thai Fund, Inc. (NYSE: TTF)** declined 11.64% and traded at a 10.94% discount at month-end.

For the fourth consecutive month all of Lipper's municipal debt CEF classifications posted negative NAV-based returns, with—since investors are still reeling from Detroit's bankruptcy—Michigan Municipal Debt Funds (-3.93%) and General & Insured Municipal Debt Funds (Leveraged) (-3.32%) once again taking the worst of the beatings. For the second consecutive month the Intermediate Municipal Debt Funds (-2.04%) classification mitigated losses better than the other classifications in the group. The municipal debt funds macro-group (-3.04%) significantly underperformed by 245 bps its taxable domestic CEFs counterpart (-0.59%). Single-state municipal debt funds (-2.97%) mitigated losses slightly better than their national municipal debt fund counterparts (-3.10%).

As conditions deteriorated for the world markets, the two classifications making up Lipper's World Income Funds macro-group (-2.56%) took it on the chin, with Emerging Markets Debt Funds (-3.86%) taking the worst beating and Global Income Funds (-1.75%) faring a little better. With investors anticipating rising interest rates, the adjustable-rate Loan Participation Funds (-0.12%), Flexible Income Funds (-0.26%), and High Yield Funds (-0.52%) classifications mitigated losses better than the other classifications in the domestic bond funds group. Corporate BBB-Rated Debt Funds (Leveraged) and Corporate BBB-Rated Debt Funds (-0.86% each) were the laggards of the group. Mixed comments by Fed officials at the Jackson Hole retreat during the month didn't help calm the "taper tantrum" investors were having. The two-/ten-year Treasury spread widened 10 bps from July's month-end 229 bps. The yield on the ten-year Treasury note finished the month 18 bps higher at 2.78%.

In the domestic taxable fixed income CEFs universe (-0.59%) the remaining classification returns ranged from minus 0.66% (U.S. Mortgage Funds) to minus 0.79% (General Bond Funds). Only 28 fixed income CEFs posted plus-side returns for August.

Two of the three CEFs at the head of the fixed income CEFs universe were housed in Lipper's U.S. Mortgage Funds classification. **Capstone Church Capital Fund (NASDAQ: XCBFX**, an interval hybrid CEF housed in Lipper's General Bond Fund classification**)** rose 2.76% to the top of the heap. Following XCBFX were **First Trust Mortgage Income Fund (NYSE: FMY)**, tacking 1.30% onto its July month-end value and traded at a 12.62 discount at month-end, and **Western Asset Mortgage Defined Opportunity Fund Inc. (NYSE: DMO)**, posting a 0.76% return and traded at a 7.34% discount on August 30.

For the remaining funds in the fixed income CEFs universe monthly NAV-basis performance ranged from minus 7.43% (**Dreyfus Municipal Bond Infrastructure Fund, Inc. [NYSE: DMB]**, housed in Lipper's General & Insured Municipal Debt Funds (Leveraged) classification and traded at a 7.89% discount), to 0.75% for **Guggenheim Credit Allocation Fund (NYSE: GGM)**, housed in Lipper's General Bond Funds classification and traded at a 0.33% premium on August 30. The 20 top-performing fixed income CEFs posted returns at or above 0.11%, while the 20 lagging funds were at or below negative 4.07%.

PREMIUM AND DISCOUNT BEHAVIOR

For August the median discount of all CEFs narrowed 15 bps to 7.91%—considerably lower than the 12-month moving average discount (2.92%). Equity CEFs' median discount widened 115 bps to 9.57%, while fixed income CEFs' median discount narrowed 72 bps to 7.15%. Municipal bond funds' median discount narrowed 107 bps to 6.78%. Single-state municipal debt funds witnessed the largest narrowing of discounts for the month, narrowing 113 basis points to 6.77%, while Domestic Equity Funds' median discount witnessed the largest widening—153 bps to 8.66%.

For the month 42% of all funds' discounts or premiums improved, while 56% worsened. In particular, 29% of equity funds and 49% of fixed income funds saw their individual discounts narrow, premiums widen, or premiums replace discounts. The number of funds traded at premiums on August 30 (72) was 22 less than on July 31.

CEF EVENTS AND CORPORATE ACTIONS

IPOs

KKR & Company launched its first listed CEF, **KKR Income Opportunities Fund (NYSE: KIO)**. The fund raised $305 million in its common-share offering, which could go to $352 million if the underwriters exercise their options in full.

RIGHTS, REPURCHASES, TENDER OFFERS

Preliminary results of the tender offers for up to 5% of each of **The Central Europe, Russia and Turkey Fund (NYSE: CEE)** and **The New Germany Fund (NYSE: GF)** were oversubscribed. Approximately 72% of CEE's common shares and 62% of GF's common shares were tendered; on a *pro rata* basis just 7% and 8% of the tendered shares were accepted for payment.

Liberty All-Star Equity Fund (NYSE: USA) has commenced a tender offer for up to 7.5% of its outstanding shares at 96% of NAV. The offer expires September 23. The fund's discount held steady in August to end at 9.9%.

The semiannual repurchase offer of **The India Fund (NYSE: IFN)** will end September 13, 2013; tendered shares will be subject to a repurchase fee of 2% of NAV. At the end of August the fund's discount was 13.3%.

MERGERS AND REORGANIZATIONS

Trustees approved the merger of **Nuveen New York Performance Plus Municipal Fund (NYSE: NNP)** and **Nuveen New York Dividend Advantage Municipal Fund 2 (NYSE MKT: NXK)** into **Nuveen New York Dividend Advantage Municipal Fund (NYSE: NAN).** Shareholder approval is still required at the annual shareholder meetings scheduled for early 2014.

OTHER

Trustees of **The Gabelli Dividend & Income Trust (NYSE: GDV)** approved creation of a new CEF that would be a spinoff of Dividend & Income Trust. GDV would contribute approximately $100 million of its cash and/or securities and would then distribute all the shares of the new fund to the common shareholders of GDV. The fund's discount was 10.3% at the end of August.

Trustees of **BlackRock S&P Quality Rankings Global Equity Managed Trust (NYSE: BQY)** approved a name change to **BlackRock Dividend Income Trust.** The name of **Massachusetts Health & Education Tax-Exempt Trust (NYSE: MHE)** will change to **BlackRock Massachusetts Tax-Exempt Trust.** Neither ticker symbol will change.

Rocky Mountain Advisers launched a new website for Boulder Funds. Boulder Funds consists of four CEFs: **Boulder Growth & Income Fund (NYSE: BIF), Boulder Total Return Fund (NYSE: BTF), The Denali Fund (NYSE: DNY),** and **First Opportunity Fund (OTC: FOFI).**

Thai Capital Fund (NYSE: TF) paid an initial liquidating distribution of $10.93 per share to all shareholders of record as of August 16, 2013; that amount was approximately 90% of the proceeds of the fund's portfolio liquidation per share. The final liquidating distribution is expected to be made no later than September.

Duff & Phelps Utility and Corporate Bond Trust (NYSE: DUC) will reduce the amount of leverage used by $65 million (to approximately 29% of total assets) through a combination of reducing its outstanding credit and redeeming its auction rate preferred shares. The reduction in the amount of leverage is intended to lessen the potential volatility of the fund. At the end of August the fund's discount was 7.8%.

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