INITIAL PUBLIC OFFERINGS SHATTER RECORD
The number was down but the dollars raised were well up! A total of 49 closed-end fund initial public offerings (IPOs) came to market in 2003, down from a count of 78 in the prior year and well below the all-time record of 121 established in 1993. However, the average new 2003 offering raised a stunning $550 million, for a total of $27.0 billion (vs. the old record of $18.5 billion). The final dollar total may expand mildly when supplementary data are received on the "green shoe" overallotments in the weeks just ahead. While the offerings were almost evenly divided between equity and bond universes (26 and 23, respectively), the income-oriented theme of 2001-2002 remained very much in force, as all but three funds and all but $300 million of the 2003 IPOs fit that mold.

Preferred-stock funds were tops in number at seven, while convertible securities, municipal bonds, and loan participation portfolios each saw six more entries in 2003. High Yield, Real Estate, and Equity Income each saw five deals, with the latter raising second most dollars at $4.03 billion. The most dollars raised ($6.08 billion) came in convertibles funds, which offered buyers a comforting mix of current income, upside potential, and some downside protection. The largest individual new fund of the year, and so far in CEFs history, was Eaton Vance Limited Duration Income Fund (ticker EVV), a loan-participation portfolio that raised over $1.94 billion after expenses and load in late May. It was almost exceeded four weeks later by Nuveen Preferred and Convertible Income 2 (JQC), raising $1.93 billion. A bit of innovation was seen, as the first closed-end balanced fund (Partners Balanced) came, but because it was not aftermarket traded it raised under $40 million. First Trust also brought two niche funds, and its Value Line-based portfolio was popular, raising $217 million. Other notable trends were in the creation of products with combination rather than rifle-shot portfolio strategies: real estate and preferreds; straight and convertible preferreds in a single package; and some bond and equity combinations.

All of the bond and all but four of the equity funds launched in 2003 allow for the use of leverage. In a research report in the summer (http://www.research.lipper.wallst.com/fundIndustryOverview.asp), we expressed concern about the possible downsides for investors, advisors, and brokerages if interest rates should rise significantly. A handful of municipal bond funds created in 2002-2003 do now focus on intermediate-term securities. Giving up maximum yield did not seem to inhibit sales of still-leveraged products, and the reduction in risk to all involved was a positive development in our view.

TOTAL NET ASSETS (TNA) AND FUND COUNT ALSO HIT NEW HIGHS
The combined TNA of closed-end funds finally burst through to a new all-time high in 2003. IPOs (described above) were the largest driving force, and bullish equity and lower-quality bond market trends helped as well. TNA at the end of November (December data are not yet available) stood at a record $177.3 billion, up about 28.9% from the $137.5 billion recorded at year-end 2002. The count of closed-end funds has now also finally exceeded the old record of 563 established in 1993. At year-end there were 604 portfolios, not including additional classes where multi-class structures exist (in some of the Loan Participation funds). Some 580 of the funds are traded in the aftermarket.

RIGHTS OFFERINGS CONTINUE AT SUBDUED PACE
A total of eight rights offering occurred in 2003, two more than in 2002. The count in 2003 was the largest since an equal number in 1999, but the dollars raised ($257 million) were the smallest since the $115 million of 2000. As is the prevailing historical pattern, many of the 2003 events seemed focused on investment themes that were 'hot' at the time. This included four issuances by bond funds, which traditionally have not had much success with rights offerings. Two others were by a value fund and a utilities fund. Some highlights from throughout the year follow:

The Aberdeen Global Income Fund, Inc. (FCO) and the Aberdeen Asia-Pacific Income Fund, Inc. (FAX) cancelled plans for a rights offering initially announced in October of 2002. A committee of the Board, fund managers, and third-party advisors decided to postpone the
offering citing “unfavorable market conditions.” Not coincidentally, on November 5 a complaint was filed against the advisor to block the rights offerings. The board indicated it was not influenced by the complaint.

**The Royce Value Trust, Inc. (RVT)** raised $54.5 million in a non-transferable 1-for-10 deal in March. It had previously conducted seven non-transferable rights offerings, all in ratios of 1:15 to 1:25, between 1989 and 1995.

**The Liberty All-Star Growth Fund, Inc. (ASG)** conducted a 1-for-8 non-transferable rights offering in August. The filing came in the wake of recent strong equity performance and when shares were trading at a 5% premium.

**The New America High Income Fund (HYB)** conducted a 1-for-3 transferable rights offering, the fund’s fourth since 1994, during July. Since its inception in 1988 the fund had posted a 4.09% annualized market return.

**The Ellsworth Convertible Growth and Income Fund, Inc. (ECF)** and the Bancroft Convertible Fund, Inc. (BCV) made 1-for-6 transferable rights offerings in November, raising $13.2 and $14.2 million, respectively.

**Boulder Total Return Fund, Inc. (BTF)** conducted a 1-for-3 transferable offering in July, raising $38.5 million. An interesting aspect was that pricing was based on the volume-weighted average sales price on the expiration date and four trading days after.

**The Gabelli Utility Trust (GUT)** did a 1-for-3 transferable rights offering, raising $52.5 million in August and September. The fixed-price feature used is somewhat unusual as it exposes a fund to risk if the market price drops significantly.

**The 1838 Bond-Debenture Fund (BDF)** concluded in November a transferable 1-for-3 rights offering at 87% of net asset value. It raised $23.2 million.

**Z-Sevent Fund (ZSEV)** has announced its intention to convert to open-end status is early 2004.

In one of the more unusual developments this year among closed-end funds, **NAIC Growth Fund (Chicago:GRF)** began on July 9 via prospectus a secondary offering. The text indicates the fund's intention to perhaps continue the offering for as long as two years. The fund at various times had traded at premiums to NAV during its life (IPO was in July 1990) and was at an 18% premium in January 2003 and more than 14% just before the filing. Its year-end discount was about 9%. A continuous offering at NAV (+5% load in this case) drives purchasers to the fund itself for shares, eliminating the chance for existing holders to enjoy occasional aftermarket premiums. Discussions of the priorities of existing shareholders vs the management company must have been quite involved.

**Funds leaving the closed-end universe**

A total of thirteen funds left the closed-ends fold in the past year. One of these was a term trusts so scheduled, and a few more of that type will follow in 2004-2005. The other main clusters were world equity and particularly single-country funds as well as very small funds suffering from profitability woes as seen by their advisors. We remain of the opinion that the proliferation of ETFs covering country and region and world markets has been a significant factor in weeding out some parallel closed-end funds. A list of disappearances and some highlights from the year follows:

**Other news**

- **The India Fund (IFN)** adopted interval-fund status in the spring of 2003.
The 35-year-old Bergstorm Capital Corporation (BEM) fund has closed its doors. On January 29 the roughly $125-million fund was holding 100% of its portfolio in cash and proceeded after a vote at the April 2003 meeting. The decision followed several months of analyzing alternative courses of action. Potentials for merger were explored but to no avail. Bergstorm had the best life-of-fund return of all then-existing closed-ends.

February 13 was the last day of NYSE trading prior to liquidation for the Italy Fund Inc. (ITA). At the January meeting, shareholders approved ending the 17-year-old fund. Ultimately, the maturation of the Italian securities market, a discount that often hovered around 10%, and the relatively low-risk benefits to shareholders achieved by liquidating led to the decision. An ETF has competed for investor attention since its creation in March 1996.

The India Growth Fund, Inc. (IGF) has liquidated. Based on a plan approved by shareholders in December 2002 the fund distributed approximately $9.9388 per share on about May 30.

The $8 million, MorganFunShares (MFUN), has notified shareholders of its intent to liquidate by year-end. The fund’s unique (contrary) spin on socially responsible investing did not experience much success. Though millions enjoy smoking, drinking, and gambling, investors were not eager to adopt the indulgences as an investment strategy. Contributing to the decision to liquidate was the passing of founder Burton Morgan last March.

**NET ASSET VALUE PERFORMANCE**

Average NAV-based performance for closed-end funds in 2003 jumped by 18.86%—the best year since 1995 (+20.04%)! Every one of the closed-end classifications—both bond and equity—landed in the black in 2003. Closed-end equity funds, which represent approximately one-third of all closed-end assets, had their best year on record! An astounding 40.62% in gains topped the previous mark of 38.44% set in 1979. Once again, world markets were a major driver.

Closed-end bond funds (+12.15%) also managed to string four more quarters of gains together. Their streak of quarterly gains now sits at 16—resulting in four years of gains in a row! Classifications within World Income were top performers in the bond universe, as was high yield. Municipals and domestic government bonds, meanwhile, achieved only mild gains.

The closed-end funds universe was not without its doubts in 2003. Geopolitical uncertainty gripped markets during the first quarter, and thoughts of a recovery were still mere fantasy. At the break of the first quarter, bonds were up 2.32% while equities had slumped 2.04%.

In April, corporate earnings results from domestic corporations began to feed optimism that a recovery could be on the way. The concern remained that profits were mainly a result of job and cost cuts. The term “jobless
recovery” began to float into reports and news stories. The effect on closed-end funds was nearly as strong as on open-ends. Closed-end equity saw the second quarter 2003 as the strongest quarter since fourth quarter 1999, gaining 17.69%. Closed-end bond funds jumped 5.22%—it’s best quarterly performance since fourth quarter 1995! The good economic news continued as data on domestic jobs continued to improve during the quarters that followed as did consumer sentiment. In response, overseas markets also became robust.

To that fact, the top performer in the closed-end universe was the Miscellaneous Country/Region Funds classification, climbing 73.51%. Amazingly, that amounts to little more than half of the classification’s 132.6% gains in 1999. Still, the performance was impressive when compared to all other closed-end classifications (Actually, it beat out all open-end classifications as well!). Keeping this in perspective, there are only 6 funds in the classification. Of those six, the funds invested in South Africa and Turkey performed the best with returns over 100%.

Other classifications within World Equity also outperformed. Latin American Funds (+66.37%), Eastern European Region Funds (+62.61%), and Pacific Ex-Japan Funds (+61.47%) all responded to positive economic news both in the U.S. and locally. All told, the top seven closed-end equity classifications were in World Equity.

Looking at diversified equity, an interesting phenomenon was uncovered. Unlike the open-ended universe, value funds were the top dog for 2003, beating growth funds in an up market. Value Funds returned 38.66%, while Growth Funds managed only 24.55%—just one step away from the worst performing closed-end equity classification Global Funds (+20.87%).

In closed-end bond, the strength was also found in World Income, as well as in Below Investment Grade holdings. The seven classifications within the two groups were all top performers. Corporate bond investments followed the lead of a recovering equity market, handing Below Investment Grade classifications such as High Yield Leveraged Funds (+41.99%) its best mark since 1991 (+45.15%). Unleveraged High Yield Funds (+30.00%), meanwhile, recorded its best performance since the classification was first created back in 1994.

The macro-classification also received continued support from General Bond Funds (+17.16%)—up 9 years in a row and counting. Loan Participation Funds (+13.25%) also have offered continued support, have not experienced a down year since Lipper has been tracking it as a separate classification (since 1989).

Closed-end funds investing in government bonds fell flat in 2003. Although Leveraged U.S. Government Funds (+18.02%) managed to pull in returns near the top of the closed-end bond funds pack, all others were flat to down. The falling dollar undoubtedly helped to keep investors wary as did concerns about possible rises in domestic long-term rates. U.S. Government Funds (+5.24%) and U.S. Mortgage Term Trust Funds (+1.43%) disappointed. Municipals were at the bottom of the barrel in terms of performance.

**PREMIUM/DISCOUNT TRENDS**

The median discount on all closed-end funds narrowed 200 basis points in 2003 to 3.1%. This brought the universe back to pre-1999 levels. The median discount for all closed-end funds at year’s end 1998 was -2.4%. 1999 had seen discounts increase more than 500%—ending with a 13.4% median discount.

Equity discounts dropped from 10.1% to 4.1%—an incredible 600 basis-point move! Obviously, this was partly due to the recovery within the equity markets in 2003. Another factor, of course, was the introduction of 23 new income-oriented equity funds via IPO, so the population shifted somewhat away from risk. Bond discounts meanwhile narrowed only slightly from 4.5% at the end of 2002 to 2.9% currently. Municipal Bond Funds also saw their discounts narrow from 5.0% to 3.5%.

As stated in the performance section, two of the strongest performing macro-classifications in closed-end bonds were World Income and Below Investment Grade. That said, it’s not surprising that the only two groups trading at a premium were high yield funds and world income funds. The average high yield premium jumped 220 basis points to 5.9%. World Income, meanwhile, reversed position from a 1.2% discount to a 1.7% premium. News of recovering economies and upgraded foreign debt were behind the move. In addition, since “yield sells” and investors were starved for current income, these fund groups attracted attention.