Capital Link's
CEF & ETF Monthly Newsletter

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Capital Link

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The Month in Closed-End Funds: June 2013

PERFORMANCE

On the heels of 15 100-point days (both up and down) for the Dow Jones Industrial Average in June and on fears of imminent Federal Reserve "tapering," Lipper's equity and fixed income CEF macro-groups posted negative returns on a NAV basis for the second consecutive month, losing 2.55% and 4.60%, respectively, for June. On a market-price basis both groups were also in the red, posting negative returns of 2.74% and 3.42%, respectively.

With the Fed signaling its intention to begin removing some of its easy-money provisions, both stock and bond investors have been put into a tailspin. Rising interest rates already have begun hammering spread products and dividend payers, while some pundits in stocks think that pulling the plug on quantitative easing is a signal for the end of the equity rally. This dependency has led many investors to take a twisted, contrarian approach to investing, battering the markets after reports of good economic news and raising the markets on bad news. In June the Fed indicated that purchases of mortgage-backed securities could be reduced as early as this year, with Federal Reserve Governor Jeremy Stein suggesting the first tapering move could occur as early as September. While Stein may have spooked investors, the simple fact is the Fed has begun to see improvement in the U.S. economy. In fact, much of the recent economic news has indicated slow but steady improvement on many U.S. economic fronts. At the beginning of June the May nonfarm payrolls rose 175,000, beating the consensus 163,000; the May ISM nonmanufacturing index beat expectations; and May retail sales rose 0.6%, outpacing the expected gain of 0.4%. Some disappointing economic news kept investors on defense in June, with the May ISM manufacturing index coming in at 49.0—its lowest level since June 2009, and later in the month first quarter GDP growth was revised down to 1.8% from the consensus 2.4%. Nonetheless, the May housing market showed strength, while personal income and consumption rose in May.

Despite the continued selloff in equities toward June month-end, investors continued to push Treasury prices lower on concerns the Fed is closer to ending its easy-money regime than previously thought, which sent benchmark ten-year Treasury yields to their highest close since August 3, 2011. After hitting a closing high of 2.60% late in the month, Treasury yields generally eased slightly, ending the month up 36 basis points (bps) at 2.52%. The 109-bp increase in yield since its low on July 26, 2012 (1.43%) represents an astounding 76% increase in yields in less than 12 months. The Treasury yield curve shifted up at all maturities over three months, with the seven-year yield rising the most, 41 bps to 1.96% on June 28. The selloff in Treasuries also led to a significant selloff in municipal debt funds as investors pondered the Fed's next move, future tax reforms, and the credit risk of municipalities.

For June the dollar weakened against the euro (-0.22%), the pound (-0.19%), and the yen (-1.65%). Commodities prices were mixed for the month, with near-month crude oil prices gaining 4.99% to close the month at $96.56/barrel and gold prices continuing to plunge, dropping 12.12% to end the month at $1,223.80/ounce.

The Month in Closed-End Funds: June 2013

- For June only 22% of all closed-end funds (CEFs) traded at a premium, with 21% of equity funds and 24% of fixed income funds trading in premium territory to their NAVs. Many of the Lipper CEF macro-groups witnessed a narrowing of discounts in June.
- For the first month since October 2008, all classifications in both the fixed income and equity universe were in the red for the month of June, with equity and fixed income CEFs losing on average 2.55% and 4.60%, respectively, on a NAV basis.
- For the second consecutive month all of Lipper's municipal bond fund groups posted returns in the red, with single-state municipal bond funds (-5.88%) mitigating losses slightly better than their national municipal debt fund (-6.05%) brethren.
- With the emerging markets showing signs of weakness and the European Union still mired in recession, the world equity CEFs (-4.33%) macro-group for the second consecutive month was the cellar dweller of the equity universe.

THOMSON REUTERS

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For June only 6% of all CEFs posted NAV-basis returns in the black, with 13% of equity CEFs and a measly 1% of fixed income CEFs chalking up returns in the plus column. Investors ran for cover after Fed Governor Stein suggested the first tapering move could occur as early as September, since many economic numbers point toward an improving U.S. economy. Better-than- expected May new home sales, durable goods orders, and personal consumption outweighed the downward revision in first quarter GDP growth. During the month there were very few places to hide. Even for open-end funds, positive returns were hard to come by, with Dedicated Short-Bias Funds (+3.73%), Japanese Funds (+2.28%), Commodities Specialty Funds (+1.06%), Telecommunication Funds (+0.87%), and Small-Cap Growth Funds (+0.27%) providing the only plus-side returns for June. With the emerging markets showing signs of weakness and the European Union still mired in recession, the world equity CEFs macro-group (-4.33%) for the second consecutive month was the cellar dweller—lagging its domestic equity CEFs (-1.65%) and mixed-asset CEFs (-2.62%) counterparts for the month.

For the first month since October 2008 all classifications in both the fixed income and equity CEFs universe were in the red for June. Given the spike in Treasury yields and the impact on spread products, it wasn't surprising to see the municipal bond funds macro-group (-5.97%) pushed to the bottom of the fixed income group, underperforming taxable domestic bond CEFs (-2.68% on a NAV basis) and world bond CEFs (-4.54%).

Only 34 equity CEFs posted returns in the black for June, helping Sector Equity Funds (-1.08%) and Growth Funds (-1.61%) mitigate losses better than some of the other equity classifications. As a result of the continued concerns in the global market and on reports of a rotation out of dividend plays, investors kept Pacific ex-Japan Funds (-7.22%), Emerging Markets Funds (-6.56%), and Real Estate Funds (-2.76%) at the bottom of the pack. For the remaining equity classifications returns ranged from negative 2.74% (Convertible Securities Funds) to negative 1.71% (Value Funds).

All of the ten top-performing individual funds were housed in Lipper's Sector Equity CEFs classification, and all were energy master limited partnership (MLP)- related funds. At the top of the chart was Tortoise MLP Fund, Inc. (NYSE: NTG), gaining 5.13% on a NAV basis and traded at a 2.52% premium at month-end. Following NTG were Tortoise Energy Capital Corporation (NYSE: TYY), posting a 4.97% return and traded at a 6.36% premium on June 28; Tortoise Energy Infrastructure Corporation (NYSE: TYG), rising

CLOSED-END FUNDS LAB

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	13	42	56	21	79
Bond Funds	1	67	32	24	75
ALL CEFS	**6**	**57**	**41**	**22**	**77**

TABLE 2 AVERAGE NAV RETURNS, SELECTED PERIODS (%)

	June	YTD	3-MONTH	CALENDAR-2012
Equity Funds	-2.55	5.95	-1.35	15.42
Bond Funds	-4.60	-2.92	-4.38	15.04
ALL CEFS	**-3.80**	**0.54**	**-3.20**	**15.18**

TABLE 3 NUMBER OF IPOs, SELECTED 12-MONTH PERIODS

	June 2013	CALENDAR-2012
ALL CEFS	**36**	**31**

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

3 MONTHS THROUGH 5/31/2013	711
COMPARABLE YEAR-EARLIER 3 MONTHS	457
CALENDAR 2012 AVERAGE	506

Source: Lipper, a Thomson Reuters company

4.95% on a NAV basis and traded at an 8.11% premium at month-end; **Nuveen Energy MLP Total Return Fund (NYSE: JMF)**, chalking up a 4.62% return and traded at a 7.99% premium at month-end; and **ClearBridge Energy MLP Fund Inc. (NYSE: CEM)**, rising 4.17% and traded at a 5.43% premium on June 28.

For the month the dispersion of performance in individual equity CEFs—ranging from minus 16.66% to positive 5.13%—was wider than May's spread and more negatively skewed. The 20 top-performing equity funds posted returns in excess of 1.25%, while the 20 lagging funds were at or below minus 7.30%. For the month only 31 equity funds posted positive NAV-based returns.

Given the meltdown in gold prices, it wasn't surprising to see **ASA Gold & Precious Metals Limited (NYSE: ASA)**, housed in Lipper's Sector Equity Funds classification, at the bottom of the equity CEF group. ASA shed 16.66% of its May month-end value and traded at a 2.76% discount on June 28. The next poorest performing equity fund was also warehoused in Lipper's Sector Equity Funds classification: **Central Fund of Canada Limited (AMEX: CEF)** declined 15.18% and traded at a 1.45% discount at month-end.

For the second consecutive month all of Lipper's municipal debt CEF classifications posted negative NAV-based returns, with General & Insured Municipal Debt Funds (Leveraged) (-6.52%) and Michigan Municipal Debt Funds (-6.23%) taking the worst of the beatings. However, one of May's leaders once again mitigated losses better than the other classifications in June as General & Insured Municipal Debt Funds (Unleveraged) (-3.71%) remained at the top. The municipal debt funds macro-group (-5.97%) significantly underperformed its taxable domestic CEFs counterpart (-2.68%) by 329 basis points. Single-state municipal debt funds (-5.88%) mitigated losses slightly better than their national municipal debt fund counterparts (-6.05%).

As the pall continued to hang over the world markets, the two classifications making up Lipper's World Income Funds macro-group (-4.54%) weighed on fixed income returns: Emerging Markets Debt Funds (-5.73%) and Global Income Funds (-3.80%). Loan Participation Funds (-1.00%, May's leader) mitigated losses better than the other classifications in the domestic bond funds group; General Bond Funds (-3.64%) and U.S. Mortgage Funds (-3.56%) dragged down the group. With investors becoming generally more sure toward month-end that the Fed would start removing its quantitative easing, the two-/ten-year Treasury spread widened a whopping 30 bps from May's month-end 186 bps. The yield on the ten-year Treasury note finished the month 36 bps higher at 2.52%.

In the domestic taxable fixed income CEFs universe (-2.68%) the remaining classification returns rangedfrom minus 3.29% (Corporate BBB-Rated Debt Funds [Leveraged]) to minus 2.03% (Flexible Income Funds).

In the whole fixed income universe only four individual CEFs posted positive NAV-basis returns for the month. At the head of the fixed income CEFs class was **GL Beyond Income Fund (NASDQ: GLBFX)**, a hybrid interval fund housed in Lipper's General Bond Funds classification, rising 0.83%. Following GLBFX were **Vertical Capital Income Fund (NASDAQ: VCAPX)** (also a hybrid interval fund housed in Lipper's U.S. Mortgage Funds classification), tacking 0.57% onto its May month-end value; **NexPoint Credit Strategies Fund (NYSE: NHF**, housed in Lipper's High Yield Funds [Leveraged] classification**)**, posting a 0.47% return and traded at an 8.59% discount on June 28; and **Pioneer Floating Rate Trust (NYSE: PHD**, warehoused in Lipper's Loan Participation classification**)**, gaining 0.11% on a NAV basis and traded at a 0.30% premium at month-end.

For the remaining funds in the fixed income CEFs universe monthly NAV-basis performance ranged from minus 12.45% (**BlackRock Municipal Target Term Trust [NYSE: BTT]**) housed in Lipper's General & Insured Municipal Debt Funds (Leveraged) classification and traded at a 1.86% discount) to negative 0.15% for **Capstone Church Capital Fund (NASDAQ: XCBFX)**, a hybrid interval fund housed in Lipper's General Bond Funds classification. The 20 top-performing fixed income CEFs posted returns at or above negative 0.97%, while the 20 lagging funds were at or below negative 7.41%.

PREMIUM AND DISCOUNT BEHAVIOR

For June the median discount of all CEFs narrowed 137 bps to 4.87%—much lower than the 12-month moving average discount (1.80%). Equity CEFs' median discount widened 28 bps to 7.44%, while fixed income CEFs' median discount narrowed 164 bps to 4.02%. Municipal bond funds' median discount narrowed 220 bps to 4.06%. Single-state municipal debt funds witnessed the largest narrowing of discounts for the month, narrowing 255 basis points to 4.45%. World Income Funds' median discount suffered the largest widening—110 bps to 7.59%. Domestic equity funds' discount narrowed 68 bps to 5.77%, while their world equity CEF counterparts' discount narrowed only 14 bps to 10.15%.

For the month 57% of all funds' discounts or premiums improved, while 41% worsened. In particular, 42% of equity funds and 67% of fixed income funds saw their individual discounts narrow, premiums widen, or premiums replace discounts. The number of funds traded at premiums on June 28 (134) was 21 more than May 31.

IPOs

The initial public offering of **ClearBridge American Energy MLP Fund (NYSE: CBA)** raised gross proceeds of approximately $1.05 billion; if underwriters fully exercise their overallotment options, the fund could raise up to $1.20 billion.

The initial public offering of **Eaton Vance Floating-Rate Income Plus Fund (NYSE: EFF)** sold 6.75 million shares and raised gross proceeds of $135 million. Another 1 million shares may be issued if underwriters exercise their overallotment options.

RIGHTS, REPURCHASES, TENDER OFFERS

The semiannual repurchase offer for The Asia Tigers Fund (NYSE: GRR) will end July 12. Directors authorized the fund's repurchase offer for up to 5% of its outstanding common shares, with a repurchase fee of 2% of NAV. The discount on GRR was 10.5% at the end of June.

Gabelli Global Utility & Income Trust (NYSE: GLU) completed its recent transferable rights offering of one million common and preferred shares, with gross proceeds of over $70 million. The fund received total subscriptions for approximately $130 million and retained approximately $70 million, with the balance returned to investors who submitted oversubscription requests. At the end of June the fund's discount was 8.4%.

MERGERS AND REORGANIZATIONS

Western Asset High Income Opportunity Fund (NYSE: HIO) completed its merger with **Western Asset High Income Fund (previously NYSE: HIF).** Effective immediately, HIF shareholders become HIO shareholders.

Shareholders of **Nuveen Municipal High Income Opportunity Fund (NYSE: NMZ)** approved the merger of their fund into **Nuveen Municipal High Income Opportunity Fund 2 (NYSE: NMD).**

Trustees of **BlackRock High Yield Trust (NYSE: BHY), BlackRock Corporate High Yield Fund (NYSE: COY), BlackRock Corporate High Yield Fund III (NYSE: CYE), BlackRock High Income Shares (NYSE: HIS),** and **BlackRock Corporate High Yield Fund V (NYSE: HYV)** have approved their reorganizations into **BlackRock Corporate High Yield Fund VI (NYSE: HYT).** The reorganizations are each separately subject to shareholder approval and are expected to be completed in late 2013.

OTHER

Trustees of **First Trust Active Dividend Income Fund (NYSE: FAV)** replaced the fund's investment advisor— Aviance Capital Management—with Chartwell Investment Partners, effective July 1. The fund's discount was 11.7% at the end of June.

BlackRock S&P Quality Rankings Global Equity Managed Trust (NYSE: BQY) will no longer use S&P's Earnings and Dividend Quality Ranking System or its International Quality Rankings System as the underlying universe for investment. Instead, BQY will broaden its horizon to invest across the globe for dividend-paying equities. In addition, BQY's name will be changed to reflect this change in investment strategy; the ticker symbol will not change. The fund's discount was 8.8% at the end of June.

Trustees of **BlackRock MuniVest Fund (NYSE: MVF), BlackRock MuniYield California Fund (NYSE: MYC), BlackRock MuniYield New Jersey Fund (NYSE: MYJ)**, and **BlackRock MuniYield Investment Fund (NYSE: MYF)** approved changes to no longer restrict investments to investment-grade long-term municipal debt. Instead, each fund may invest up to 20% of its total assets in securities rated below investment grade.

The portfolio management team of **Invesco Bond Fund (NYSE: VBF)** has changed, with the exception of Chuck Burge, who has managed the fund since 2010. Four other managers are also responsible for portfolio management. At the end of June the discount on VBF was 8.1%.

Shareholders of **The Thai Fund (NYSE: TTF)** approved a plan to restructure the fund. Officers of the fund will take the necessary steps to effect the restructuring, including seeking any necessary approvals from the Thai Securities and Exchange Commission. The restructuring is expected to be completed around the end of Q3 2013. At the end of the month the fund had a discount of 12.9%.

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CEF Performance Statistics

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Category	Average of 1MO NAV Change	Average of 1MO Mkt Change	Average P/D 5/31/2013	Average P/D 6/30/2013	Average of 1 MO P/D Change	Average of YTD NAV Change	Average of YTD Mkt Change	Average of YTD P/D Change
Growth Funds	-0.10	-0.06	-3.85	-1.71	2.14	0.08	0.46	10.27
High Yield Municipal Debt Funds	-0.61	-0.40	-2.04	-0.5	1.54	-0.69	-0.88	-2.17
Flexible Income Funds	-0.35	-0.55	-6.33	-7.67	-1.34	-0.28	-0.75	-3.55
High Yield Funds (Leveraged)	-0.43	-0.47	-1.36	-1.5	-0.14	0.29	0.17	-1.29
Convertible Securities Funds	-0.44	-0.39	-6.1	-5.68	0.42	0.51	0.64	1.81
Loan Participation Funds	0.01	0.08	2.29	2.47	0.18	0.29	0.5	1.37
Options Arbitrage/Opt Strategies Funds	-0.41	-0.39	-5.06	-5.05	0.01	0.25	0.64	3.21
Developed Market Funds	-0.34	-0.37	-8.74	-9.03	-0.29	0.71	0.71	1.36
Global Funds	-0.46	-0.49	-8.13	-8.77	-0.64	0.24	0.38	0.84
Real Estate Funds	-0.12	0.37	-5.86	-3.69	2.17	0.25	1.26	3.7
New York Municipal Debt Funds	-0.90	-0.47	-4.8	-1.91	2.89	-1.22	-1.67	-3.09
Value Funds	-0.34	-0.33	-11.22	-10.56	0.66	1.29	1.73	2.7
Corporate BBB-Rated Debt Funds(Leveraged	-0.57	-0.42	-4	-3.24	0.76	-0.54	-0.91	-2.87
California Municipal Debt Funds	-0.94	-0.43	-5.5	-2.14	3.36	-1.18	-1.52	-2.37
Intermediate Municipal Debt Funds	-0.75	-0.33	-4.71	-2.06	2.65	-1.07	-1.37	-2.3
General & Insured Muni Debt Funds (Lever	-1.05	-0.58	-5.58	-2.95	2.63	-1.33	-1.71	-2.79
Michigan Municipal Debt Funds	-1.00	-0.72	-8.43	-7.87	0.56	-1.37	-1.57	-2.78
Other States Municipal Debt Funds	-0.91	-0.69	-3.15	-1.73	1.42	-1.22	-1.63	-2.72
Income & Preferred Stock Funds	0.15	-0.29	-3.06	-2.37	0.69	1.31	0.8	0.18
Pennsylvania Municipal Debt Funds	-0.96	-0.55	-8.35	-6.12	2.23	-1.3	-1.93	-4.71
New Jersey Municipal Debt Funds	-0.98	-0.53	-7.47	-4.87	2.6	-1.32	-2.32	-6.77
General & Insured Muni Fds (Unleveraged)	-0.65	-0.58	-4.8	-4.77	0.03	-0.77	-1.24	-3.22
Core Funds	-0.39	0.17	-7.62	-6.26	1.36	1.79	2.02	6.46
U.S. Mortgage Funds	-0.81	-0.91	-6.04	-6.46	-0.42	-0.01	-0.55	-2.96
Corporate Debt Funds BBB-Rated	-0.58	-0.72	-7.76	-8.75	-0.99	-0.91	-1.62	-4.65
Emerging Markets Debt Funds	-1.14	-1.18	-5.7	-6.11	-0.41	-2.1	-2.37	-2.29
Global Income Funds	-0.79	-0.77	-4.61	-5.1	-0.49	-0.42	-1.06	-4.38
Pacific Ex Japan Funds	-1.47	-1.59	-9.68	-10.78	-1.1	-0.86	-1.48	-3.65
Emerging Markets Funds	-1.55	-1.45	-7.81	-8.18	-0.37	-1.84	-1.63	0.44
Sector Equity Funds	-16.13	-0.43	-0.27	-1.14	-0.87	-11.81	1.46	1.46
General Bond Funds	-4.50	-0.15	-3.22	-2.11	1.11	-4.25	-0.66	-3.83
High Yield Funds	-5.70	-0.33	-2.77	-3.02	-0.25	-1.54	-0.32	-2.54

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Top 5 Performing CEFs

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Fund Name	Category	Ticker Symbol	1-Month NAV Change	Rank
Tortoise Energy Inf Corp	Sector Equity Funds	TYG	2.03	1
Tortoise Energy Cap Corp	Sector Equity Funds	TYY	1.54	2
Tortoise MLP	Sector Equity Funds	NTG	1.39	3
ClearBridge Energy MLP	Sector Equity Funds	CEM	1.07	4
Tortoise NA Energy Corp	Sector Equity Funds	TYN	1.04	5

Fund Name	Category	Ticker Symbol	Year-to-Date NAV Change	Rank
Tortoise Energy Inf Corp	Sector Equity Funds	TYG	8.17	1
Kayne Anderson MLP	Sector Equity Funds	KYN	6.89	2
Source Capital	Core Funds	SOR	6.53	3
Tortoise Energy Cap Corp	Sector Equity Funds	TYY	6.13	4
Salient MLP&Energy Infra	Sector Equity Funds	SMF	5.3	5

Fund Name	Category	Ticker Symbol	1-Month Market Change	Rank
Tortoise Energy Inf Corp	Sector Equity Funds	TYG	2.07	1
Tortoise Energy Cap Corp	Sector Equity Funds	TYY	1.72	2
Kayne Anderson MLP	Sector Equity Funds	KYN	1.68	3
Fiduciary/Clay MLP Opp	Sector Equity Funds	FMO	1.56	4
Nuveen Engy MLP Tot Rtn	Sector Equity Funds	JMF	1.46	5

Fund Name	Category	Ticker Symbol	Year-to-Date Market Change	Rank
Source Capital	Core Funds	SOR	9.49	1
Kayne Anderson MLP	Sector Equity Funds	KYN	9.42	2
Tortoise Energy Inf Corp	Sector Equity Funds	TYG	8.6	3
Tortoise NA Energy Corp	Sector Equity Funds	TYN	6.22	4
Tortoise Energy Cap Corp	Sector Equity Funds	TYY	6.13	5

Fund Name	Category	Ticker Symbol	1-Month P/D Change	Rank
Nuveen MA Div Adv Muni	Other States Municipal Debt Funds	NMB	14.59	1
PIMCO Corp & Inc Oppty	Corporate BBB-Rated Debt Funds(Leveraged)	PTY	12.81	2
PIMCO Gl StksPLUS & Inc	Options Arbitrage/Opt Strategies Funds	PGP	10.72	3
Cornerstone Total Return	Core Funds	CRF	10.24	4
PIMCO Corp & Inc Strat	General Bond Funds	PCN	9.22	5

Fund Name	Category	Ticker Symbol	Year-to-Date P/D Change	Rank
Cornerstone Total Return	Core Funds	CRF	35.43	1
Cornerstone Prog Return	Growth Funds	CFP	28.78	2
Cornerstone Strat Value	Core Funds	CLM	28.25	3
PIMCO Gl StksPLUS & Inc	Options Arbitrage/Opt Strategies Funds	PGP	23.98	4
PIMCO High Income	High Yield Funds (Leveraged)	PHK	17.87	5

Global ETP Monthly Overview

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Highlights (US$):[1]

Global ETP outflows in June totaled ($8.2bn). It was the first month of outflows since November 2011 when redemptions were ($0.1bn), which was then followed by three consecutive months of inflows averaging $21bn. The record for monthly outflows was January 2010, when we saw ($13.4bn) of outflows.

- June represents a reversal from May when flows reached $25.6bn. Key themes in May were the acceleration of flows into Japanese Equity ETPs, shifting investor preference within Sector Equities for more economically sensitive categories, and more robust flows into Intermediate-Maturity Fixed Income funds.
- **Japanese Equity ETPs followed up last month's record inflows of $10.3bn with additional asset gathering in June of $2.8bn** despite a 1% drop in Japanese Equity markets. The Bank of Japan's ETP purchases totaled $1.6bn during the month.
- **Short-Maturity Fixed Income flows accelerated to $5.5bn from May's level of $2.6bn,** this despite total Fixed Income outflows in June of ($8.1bn). Short-Maturity Treasury and Investment Grade led flows in June as investors reacted to recent FOMC comments regarding an upcoming slowdown of bond purchases. Investor appetite for intermediate-maturity funds waned in June as investors pulled out ($2.3bn) as compared to May which saw inflows of 4.2bn.
- **US Sector Equity flows slowed to $1.1bn** this month as compared to May when these funds gathered $5.1bn.
- **Gold ETP redemptions were ($4.1bn)** in June compared to ($5.9bn) in May, bringing YTD outflows to ($28.2bn).

JUNE RESULTS AT A GLANCE[1]

(US $billions)

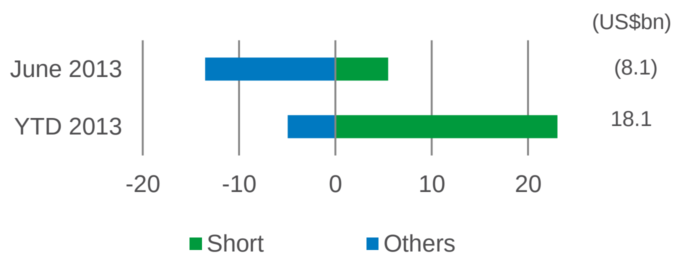
	June 2013	May 2013*	December 2012	June 2012
Monthly Flows	(8.2)	25.6	38.7	20.3
Assets	2,036	2,123	1,944	1,677
# of ETPs	4,868	4,871	4,759	4,723

*May - 2013 restated with additional Asia Pacific data

GLOBAL 13-MONTH ROLLING NET FLOWS[1]

2013 YTD Net Flows: $96.3bn

FIXED INCOME FLOWS BY MATURITY[1,2]



Source: BlackRock

Global ETP Year-To-Date Overview

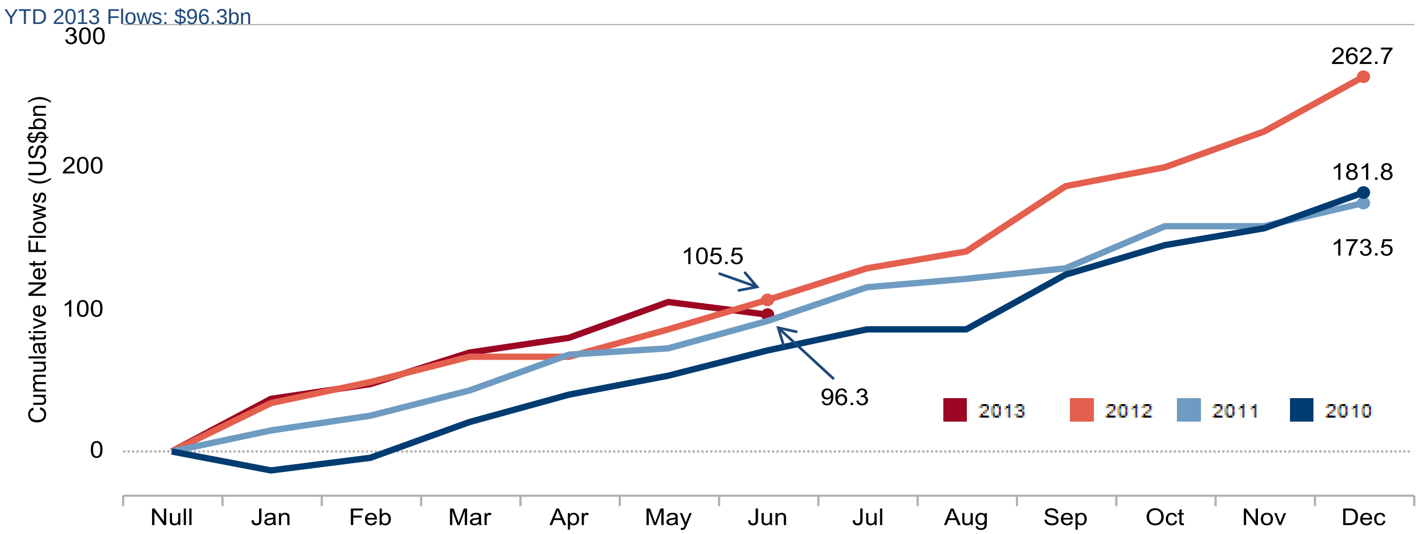
BlackRock

Highlights (US$):[1]

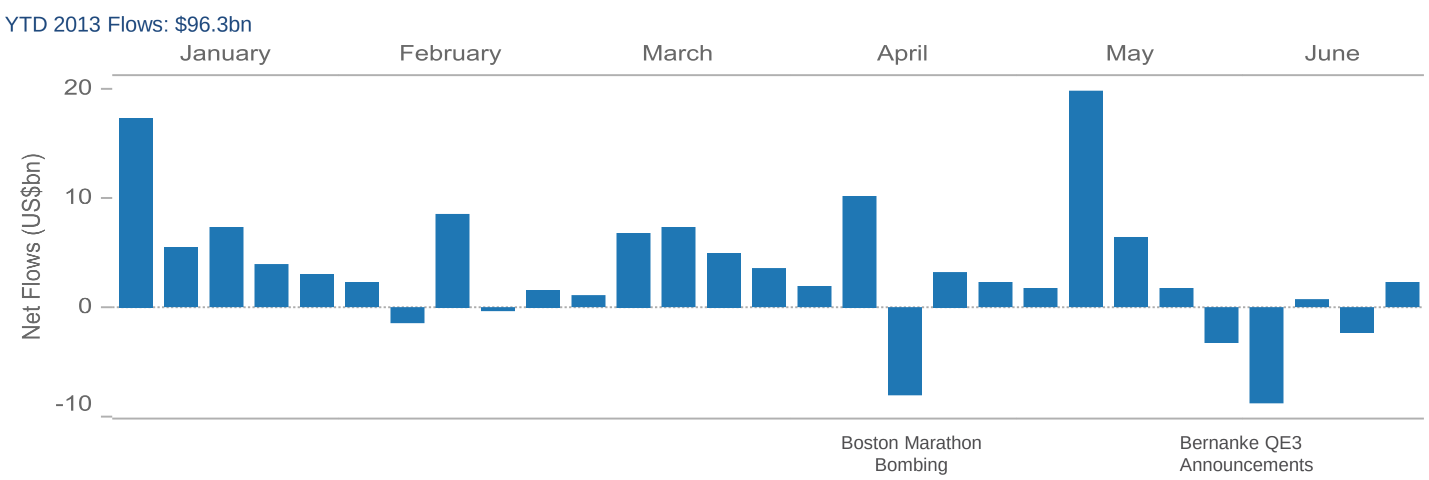
Year-to-date global ETP inflows dropped below the $100bn mark in June

- YTD net flows of $96.3bn are below last year's record-setting pace due to June outflows. In the first half of 2012, ETP industry gathered $105.5bn of inflows.
- **Equity funds led with more than $105 billion** of YTD inflows which is more than 80% above last year's pace of $56bn.
- **US and Japanese Equity exposures account for the bulk of the year-over-year Equity flow growth.** Both equity markets have been bolstered by accommodative Central Bank monetary policies.
- The growth in year over year Equity flows was mitigated **by EM Equity outflows** of ($10.4bn) YTD. The category had seen strong inflows in January of $10.9bn and then shifted to outflows from February through June.
- **Short Maturity funds (Floating Rate, Ultra-Short-Term and Short-Term) have been the engine for Fixed Income flows this year,** accumulating $23.1bn. Last June, the duration picture was completely different with YTD inflows of $3.5bn for Short Maturity funds.[2]
- **Gold** and **Fixed Income funds** are driving the year-over-year decline in flows.

GLOBAL ETP CUMULATIVE NET FLOWS[1]



GLOBAL ETP WEEKLY NET FLOWS[1]



Source: BlackRock

Largest Asset Gathering ETPs Launched in 2013

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Highlights (US$):[1]

- 210 new ETPs and 20 individual share class listings debuted around the globe so far this year and have accumulated $11.4bn in assets.
- 103 products and 9 individual share class listing were delisted this year with combined assets of less than $980mn.

Product Name (US$mn)[1]	Bloomberg Ticker	Exposure	Listing Region	Launch Date	Assets as of June 2013
ChinaAMC CSI 300 Index ETF	510330 CH	Emerging Markets Equity	Asia Pacific	January	3,244
FI Enhanced Global High Yield ETN	FIGY US	Other Developed/ Global	US	May	1,059
Guotai SSE 5-Year China Treasury Note ETF	511010 CH	Fixed Income	Asia Pacific	March	395
SPDR Blackstone/GSO Senior Loan ETF	SRLN US	Fixed Income	US	April	328
BMO Mid-Term US IG Corporate Bond Index ETF	ZIC CN	Fixed Income	Canada	March	291
FI Enhanced Europe 50 ETN	FEEU US	Other Developed/ Global	US	May	279
SPDR MSCI EMU UCITS	ZPRE GY	Other Developed/ Global	Europe	January	262
China Southern Kaiyuan CSI 300 Index ETF	159925 CH	Emerging Markets Equity	Asia Pacific	April	251
Harvest MSCI China A 50 Index ETF	83136 HK	Emerging Markets Equity	Asia Pacific	June	207
ChinaAMC SSE Health Care ETF Index Sponsor Fund	510660 CH	Emerging Markets Equity	Asia Pacific	May	201
Lyxor MTS Spain Gov Bond All-Maturity	ES10 FP	Fixed Income	Europe	February	197
ChinaAMC SSE Financials ETF Index Sponsor Fund	510650 CH	Emerging Markets Equity	Asia Pacific	May	180
Samsung KODEX FTSE China A50 ETF	169950 KS	Emerging Markets Equity	Asia Pacific	January	161
BMO Mid-Term US IG Corporate Bond Hedged to CAD Index ETF	ZMU CN	Fixed Income	Canada	March	155
KyoboAXA POWER KTB ETF(Bond)	176710 KS	Fixed Income	Asia Pacific	May	150
Others					4,067
Total - 210 Primary ETPs + 20 Share Classes					11,429

Source: BlackRock

Largest Year-to-Date Fund Inflows and Outflows

BLACKROCK®

ETPs as of June (US$mn)[1]	Bloomberg Ticker	2013 YTD Inflows	Jun-13 Assets
WisdomTree Japan Hedged Equity Fund	DXJ US	8,170	9,936
iShares MSCI Japan	EWJ US	4,956	10,938
Daiwa ETF TOPIX	1305 JP	4,467	8,984
Financial Select SPDR	XLF US	3,428	14,446
iShares Core S&P 500	IVV US	3,300	42,944
Vanguard Short-Term Bond	BSV US	3,249	12,404
Vanguard Total Stock Market	VTI US	3,245	30,796
PowerShares Senior Loan Portfolio	BKLN US	3,083	4,526
ChinaAMC CSI 300 Index ETF	510330 CH	2,726	3,244
iShares Russell 2000	IWM US	2,704	21,852
Grand Total		39,325	160,070

ETPs as of June (US$mn)[1]	Bloomberg Ticker	2013 YTD Inflows	Jun-13 Assets
SPDR Gold	GLD US	(18,175)	37,138
iShares MSCI Emerging Markets	EEM US	(8,414)	34,848
iShares Barclays TIPS Bond	TIP US	(4,722)	16,012
SPDR S&P 500	SPY US	(4,551)	133,336
iShares iBoxx $ Investment Grade Corporate Bond	LQD US	(4,416)	19,463
Vanguard FTSE Emerging Markets	VWO US	(3,169)	49,356
SPDR Barclays Capital High Yield Bond	JNK US	(2,868)	9,379
iShares FTSE China 25	FXI US	(2,005)	5,208
iShares MSCI Brazil	EWZ US	(1,885)	6,052
iShares J.P. Morgan USD Emerging Markets Bond	EMB US	(1,862)	4,385
Grand Total		(52,068)	315,176

Source: BlackRock

Global ETP Flows by Exposure – Developed Equity

BLACKROCK®

Exposure (US$mn)[1]		June 2013 Net Flows	2013 YTD Net Flows	% of YTD Flows	Assets	% of Assets	# ETPs
US Size and Style	Large Cap	3,050	18,801	19.5	384,182	18.9	225
	Mid Cap	716	3,428	3.6	64,442	3.2	50
	Small Cap	2,357	8,863	9.2	68,486	3.4	64
	Micro Cap	73	202	0.2	852	0.0	4
	Total Market	1,066	8,566	8.9	54,475	2.7	60
	Extended Market	99	671	0.7	2,983	0.1	2
	Preferred Stock	(1,190)	871	0.9	15,667	0.8	5
	US Size and Style Total	6,170	41,402	43.0	591,088	29.0	410
US Sector	Basic Materials	100	10	0.0	5,035	0.2	14
	Consumer Cyclicals	251	2,534	2.6	13,972	0.7	18
	Consumer Non-cyclicals	325	999	1.0	9,813	0.5	12
	Energy	495	2,955	3.1	29,168	1.4	41
	Financials	1,308	5,533	5.7	27,008	1.3	37
	Health Care	414	2,227	2.3	18,014	0.9	28
	Industrials	87	944	1.0	8,122	0.4	17
	Real Estate	(1,353)	2,755	2.9	30,561	1.5	22
	Technology	(179)	2,772	2.9	18,169	0.9	27
	Telecommunications	(105)	(56)	(0.1)	982	0.0	5
	Utilities	(264)	(35)	(0.0)	8,360	0.4	12
	Theme	(18)	273	0.3	1,124	0.1	9
	US Sector Total	1,062	20,913	21.7	170,329	8.4	242
US Strategy		550	8,706	9.0	59,147	2.9	54
US Total		7,782	71,021	73.8	820,564	40.3	706
Canada Equity		824	(37)	(0.0)	30,925	1.5	83
North America Regional Equity		(63)	564	0.6	6,865	0.3	18
North America Total		8,543	71,549	74.3	858,354	42.2	807
Pan European Size and Style	Large Cap	574	75	0.1	29,583	1.5	76
	Mid Cap	(9)	(29)	(0.0)	661	0.0	8
	Small Cap	(58)	93	0.1	1,400	0.1	13
	Total Market	(63)	(87)	(0.1)	24,913	1.2	68
	Pan European Size and Style Total	444	36	0.0	56,513	2.8	164
Pan European Sector		(309)	(680)	(0.7)	10,455	0.5	158
Pan European Strategy		(27)	176	0.2	2,491	0.1	19
Pan European Total		108	(451)	(0.5)	69,503	3.4	342
Country	Germany	1,592	(193)	(0.2)	37,907	1.9	60
	U.K.	858	1,110	1.2	15,177	0.7	50
	Switzerland	89	187	0.2	8,952	0.4	23
	France	155	(574)	(0.6)	5,049	0.2	19
	Others	(228)	547	0.6	7,388	0.4	67
	Europe Single Country Total	2,467	1,076	1.1	74,472	3.7	219
Europe Total		2,575	625	0.6	143,975	7.1	561
Asia-Pacific	Regional	(1,184)	565	0.6	14,788	0.7	57
	Country	2,017	25,539	26.5	118,632	5.8	223
Asia Pacific Total		833	26,105	27.1	133,420	6.6	280
Broad-Based Global /Global ex-US		(162)	17,430	18.1	154,355	7.6	444
Developed Equity Total		11,789	115,709	120.2	1,290,104	63.4	2,092

Source: BlackRock

Endnotes

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Endnotes: BlackRock's ETP Landscape: Monthly Highlights report

"ETP" (or exchange traded product) as referred to above means any portfolio exposure security that trades intraday on a US exchange. ETPs include exchange traded funds (ETFs) registered with the SEC under the Investment Company Act of 1940 (open-end funds and unit investment trusts or UITs) and certain trusts, commodity pools and exchange traded notes (ETNs) registered with the SEC under the Securities Act of 1933.

The data for this report are captured from a number of sources by the BlackRock Investment Institute including provider websites, fund prospectuses, provider press releases, provider surveys, Bloomberg, the National Stock Exchange, Strategic Insight Simfund, Wind and the Bank of Israel. All amounts are reported in US dollars. Net flows are derived using daily net asset values and shares outstanding using the most recent data we can capture at month-end. For products with cross-listings, we attribute net flows and assets to the primary listings. Where price is not available, we use an approximation.

1. Data is as of June 27, 2013 for Europe and June 30, 2013 for the US, Canada, Latin America, Israel, and some Asia ETPs. Some Asia ETP data is as of May 31, 2013. Global ETP flows and assets are sourced using shares outstanding and net asset values from Bloomberg for the US, Canada, Europe, Latin America and some ETPs in Asia. Middle East ETP assets are sourced from the Bank of Israel. ETP flows and assets in China are sourced from Wind. Inflows for years prior to 2010 are sourced from Strategic Insights Simfund. Asset classifications are assigned by the BlackRock based on product definitions from provider websites and product prospectuses. Other static product information is obtained from provider websites , product prospectuses, provider press releases, and provider surveys. Market returns are source from Bloomberg.
2. We classify maturity buckets of a Fixed Income ETP if the fund invests at least 70% of its assets in the corresponding maturity/exposure range: Short maturity includes: underlying security maturities < 3 years and floating rate where the fund holds floating rate securities and/or bank loans. Intermediate includes: 3 years < underlying security maturities < 10 years. The "other" category includes Long-Term: underlying security maturities > 10 years; Broad Maturities: The fund invests in more than two maturity buckets without emphasizing one; Selected Maturities: The fund holds securities with multiple selected range of maturity buckets, i.e. barbell strategy which focus on the specific short-term and long-term buckets with even weights; and Fixed Maturity: The fund itself has a target maturity date and arranged holdings correspondingly

Disclosures:

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John P. Calamos from Calamos Investments on CNBC

June 11, 2013
Mike Taggart from Morningstar on CEF News: *Choices abound in the Investment Universe*

Exchange-Traded Tracking Products

July 02, 2013

Liquidity of Exchange-Traded Tracking Products vs. Their Underlying Assets

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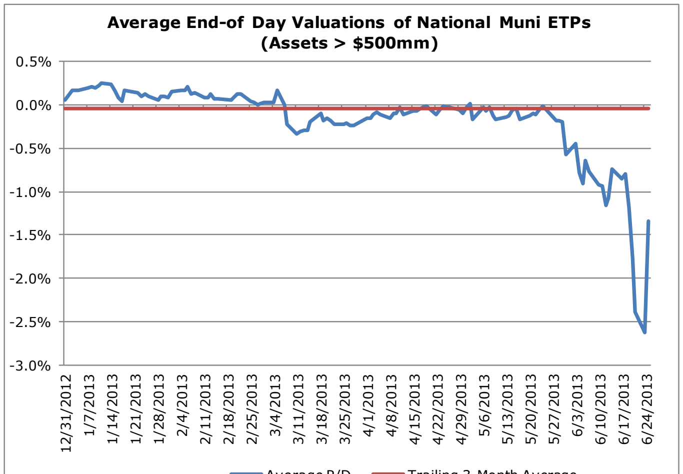
In the month of June there was a sizeable disparity between the market prices, net asset values (NAVs) and indicative NAVs (iNAVs) of a group of ETPs (primarily municipal bond ETPs), which was the result of a significant reduction in the liquidity of their underlying assets.

Exchange-traded tracking products (ETPs) are popular among retail investors because, by holding these products, they are provided cost-effective exposure to a variety of asset classes that, in some cases, could be relatively inaccessible to non-institutional investors. In most cases, the pricing and performance of ETPs are fairly close to their NAVs (the value of the underlying assets) and indices because of, in part, the liquidity of the underlying assets. Even if the ETP itself displays light trading volume, if its underlying assets are liquid (actively traded in their respective markets), and orders are entered appropriately, the market makers (often referred to as authorized participants [APs]) are able to use the natural price discovery of actively trading markets to determine the appropriate value for the shares. This minimizes the impact of larger-than-normal trades on the ETP's price relative to its NAV. However, if the underlying assets of the ETP are (or become) relatively illiquid, resulting in a weaker price-discovery mechanism, there is a potential for significant disparities between the price of the ETP, its NAV and its index which, may lead to a difference in performance.

Unfortunately, one of the reactions to these periods of disparate performance is the concern by investors that "ETPs are not effective instruments to gain access to certain markets." However, it is our opinion that the ETP market price most likely provides the more accurate valuation for the underlying assets. We believe a good example to demonstrate this risk is with municipal bond ETPs as, over the past few weeks, this fixed-income sector faced significant downward pressure, like other fixed-income sectors, in reaction to a concern for a possible sooner-than-expected tapering of the Federal Reserve's stimulus plan.

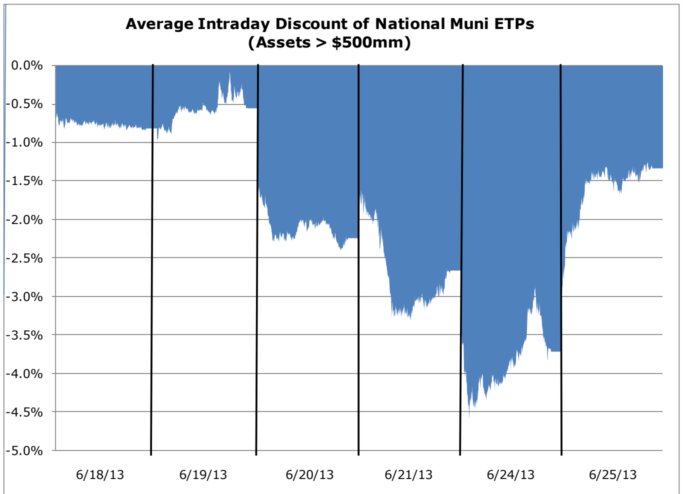
Another issue with the municipal bond market, which prompted our team to highlight this sector, was the significant decline in liquidity as competitive bids almost disappeared.



Source: Bloomberg L.P.

Pricing of the NAV, iNAV and Index

The absence of sufficient liquidity in an asset class hinders the process to price those assets. Unlike US-listed stocks, which typically have relatively active market-driven price discovery during market hours, bonds are usually less liquid. While the liquidity of the US Treasury market is abundant, the liquidity begins to deteriorate in other fixed- income markets such as that for high-yield corporate bonds and municipal bonds since a centralized exchange matching buyers and sellers is non-existent. Not only is it more difficult to find a counterparty, which usually is dependent on the size of the trade, it is also difficult to find a consistent and accurate price given that some bonds may not trade for days at a time (the last reported price for a bond may not be indicative of its true, current value) and the spread between bid and offer prices could potentially be much wider than that of stocks.



Source: Bloomberg L.P.

We believe that the recent illiquidity among municipal bonds was evident in the magnitude of the premiums and discounts (both end-of-day and intraday) experienced by ETPs that track a municipal bond index, which are displayed in the two charts below. The three-month average end-of-day discount (as of May 24, 2013) for national muni ETPs with at least $500 million in assets (seven ETPs) prior to the selloff was 0.04%. During the heart of the selloff, in late June, the average end-of-day discount reached as wide as 2.6%, ranging from 0.7% to 5.6% among the individual ETPs. In addition, the average intraday discount to iNAV, which is the estimate of the NAV during the trading hours, reached as wide as 4.6% during the trading day of June 24, 2013, with the discounts of the individual ETPs ranging from 1.7% to 8.9%.

We believe that the primary culprit for the premiums and discounts, which is the result of the illiquidity, is the pricing methodology of both the NAVs and iNAVs. The majority of ETP sponsors use third parties to provide prices for both their NAVs, which are calculated at the end of the day, and the iNAVs, which are usually calculated every 15 seconds throughout the trading session. To calculate the NAV, third parties typically simply average quote sheets provided by broker/dealers (B/Ds) on the Trade Reporting and Compliance Engine™ (TRACE™), weighted by the size of the trade. While this potentially poses a risk of stale pricing, all B/Ds that are members of FINRA are required to report transactions on TRACE™, resulting in significantly more quote sources and a decreased likelihood of stale pricing. One could argue that the NAV calculations are fairly accurate, yet such accuracy would weaken naturally during periods of illiquidity as the inconsistency of reported prices could increase significantly.

The methodology for iNAV pricing is fairly different than that of the NAV. Instead of using TRACE™ to price the bonds throughout the trading day, third parties typically apply a quantitative model, based on swap spreads on US Treasuries[1], against the previous-day's closing price to estimate the iNAV every 15 seconds. However, since the quantitative model uses only U.S. Treasury swap curves, the estimated prices would not necessarily reflect the intraday impact of unique events or intraday liquidity reductions, potentially not fully representing the current market value (or absence of a market value) of the bonds. One can thus easily imagine that during stressful periods, the NAVs and iNAVs would probably not accurately reflect existing market conditions.

Another factor that should be considered is the overlap of the trading hours as the closing time of a fixed-income ETP and its underlying assets is different. Fixed-income trading concludes at 3 pm Eastern Time, while trading of fixed-income ETPs concludes at 4 pm Eastern Time — one hour later. Therefore, during highly volatile markets, prices of the ETPs have the potential of moving substantially away from the value of the bonds at the close because of, in part, any news that is released during that hour. Investors are more familiar with this effect among ETPs that track international indices, particularly Asian market indices. However, ETPs tracking other asset classes such as fixed-income and commodities are also subject to this time dislocation, albeit typically to a lesser degree.

Finally, index providers often have different pricing methodologies. The most-basic methodology for identifying the prices of bonds is by simply consolidating price quotes from a group of B/Ds based on their last available trade. The benefit of this methodology is that it uses the actual prices determined by the market. However, the Achilles' heel of this methodology surfaces during extremely illiquid markets when none of the contributors trade a number of the bonds in the index. In that case, the prices of certain individual bonds would remain constant, potentially resulting in a stale price. The other commonly-used pricing methodology is "matrix" pricing, in which the index providers use multiple sources to price the bonds within the index. In addition to direct price quotes, quantitative models can also be used to extrapolate estimated prices for bonds without readily available quotes. While the resulting bond prices may not be based off of market quotes, they provide estimates which attempt to more-closely reflect current market activity.

Another noteworthy factor is that the prices of municipal bond ETPs, similar to the majority of fixed-income ETPs, tend to approximate the median of the bid/offer prices of the underlying portfolio of bonds. Instead, only the bid is typically used in the calculation of the NAV which results in the ETPs naturally trading at premiums most of the time. Accordingly, when the liquidity in the credit markets declines, prompting bid/offer spreads of bonds to widen, the deviations between the ETP's price and its NAV and iNAV widen as well.

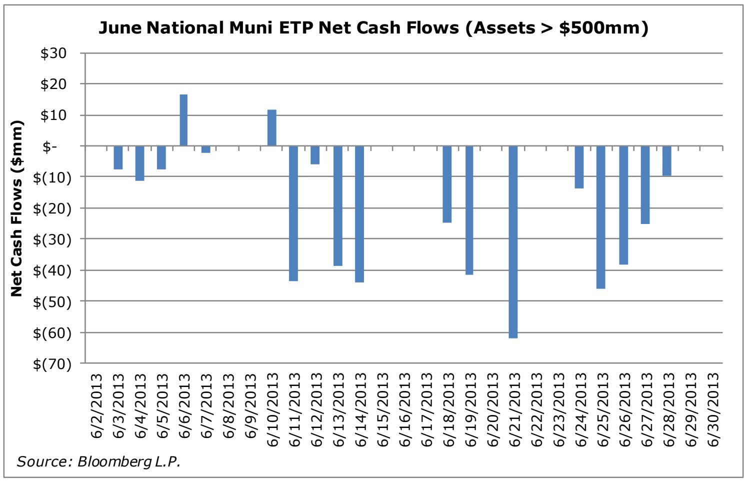
Share creation and redemption procedures during illiquidity may also impact price deviations

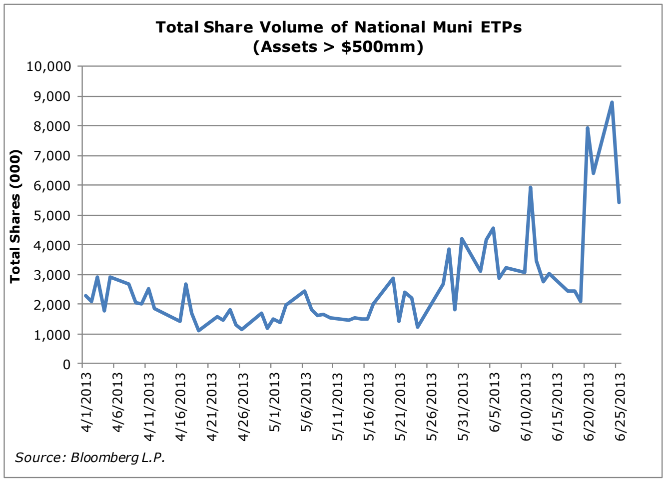
Illiquidity also exacerbates the impact on the cost of creating and redeeming shares as wider spreads are passed through to shareholders. This, in turn, results in wider premiums and discounts.

There are two methods by which new shares of ETPs are created and old shares redeemed — "in-kind" and "cash". In the "in-kind" process a basket of the underlying portfolio with appropriate weights is exchanged between an AP and the ETP provider. In the "cash" creation/redemption process, instead of exchanging the underlying assets and ETP shares, the APs and ETP providers simply exchange cash.

The degree of liquidity of an ETP's underlying assets can significantly impact the costs of creating and redeeming new shares in both procedures. The main cost of a security transaction is typically considered to be the spread between the bid/ask prices of stocks and the bid/offer prices of bonds. In periods of relatively high liquidity, the spreads between the two prices are often very tight, resulting in fairly insignificant trading costs, as a percentage of the price. However, as discussed earlier, in periods of low and even minimal liquidity, spreads may widen considerably. As the spreads widen, the costs of share creations and redemptions increase, which may magnify the deviations between the ETP price and its iNAV and NAV.

In addition, as the liquidity of certain markets dries up, it becomes increasingly challenging for either the APs or ETP providers to





purchase and/or sell sufficient assets for ETP share creations and redemptions. This escalating "execution risk" may also contribute to an increase in the cost of creating and redeeming ETP shares, which would typically result in a widening of the bid/ask spreads provided by market makers. We believe this increase in execution risk impacted the widening of discounts as there was a net $390 million pulled from seven ETPs with more than $500 million in assets, which is displayed in the chart below.

ETPs — The More Accurate Price?

In the event of illiquidity in an ETP's underlying asset class while at the same time the shares of the ETP remain liquid, we think the price of the ETP is the ultimate price discovery mechanism for the asset class (i.e., it is more indicative of the "true value" of the underlying asset class). Such was the recent environment for national muni ETPs — the liquidity of muni bonds dried up, which triggered a number of challenges to price an ETP's NAV, iNAV and underlying index, but the seven muni ETPs remained quite liquid. In fact, their liquidity increased as displayed in the chart on the following page. Perhaps one day, bonds will trade on an exchange, similar to how stocks trade, providing greater transparency and liquidity. When that day comes, there will be fewer challenges in pricing a fixed-income ETP's NAV, iNAV, and underlying index even during stressful markets when liquidity declines.

End Notes

[1] A swap spread is defined as the spread paid by the fixed-rate payer of an interest rate swap contract over the rate of the on the run treasury with the same maturity as the swap. For example, if the fixed-rate of a 5-year swap is 2.3% and the 5-year Treasury is yielding at 1.8%, the swap spread is 2.3% - 1.8% = 50 basis points (100 basis points = 1%).

Disclaimers

The investments discussed are not suitable for all investors. Investors must make their own decisions based on their specific investment objectives and financial circumstances.

Exchange-Traded Tracking Products are subject to risks similar to those of stocks. Investment returns may fluctuate and are subject to volatility, so that an investor's share, when redeemed or sold, may be worth more or less than the original cost.

Shares of ETPs are bought and sold at market price which may differ significantly from the ETP's net asset value and are not individually redeemed from the fund. Only "authorized participants" can purchase and redeem directly in the funds creation units, typically consisting of a block of 50,000 shares.

Investing in fixed income securities involves certain risks such as market risk if sold prior to maturity and credit risk especially if investing in high yield bonds, which have lower ratings and are subject to greater volatility. Income from municipal securities is generally free from federal taxes and state taxes for residents of the issuing state. While the interest income is tax-free, capital gains, if any, will be subject to taxes. Income for some investors may be subject to the federal Alternative Minimum Tax (AMT).

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What's next in 2013?

The Critical Answers

Russ Koesterich
Managing Director, Global Chief Investment Strategist, BlackRock

Jeff Rosenberg
Chief Investment Strategist for Fixed Income, BlackRock

Peter Hayes
Head of BlackRock's Municipal Bonds Group

Highlights

Stocks Surprise and the Fed Shifts. The surprising rally in equities continued but the shift in Federal Reserve policy pushed up interest rates. Slow growth and low inflation are likely but uncertainty and volatility will remain high. In this report, we offer some perspective on the critical questions investors are asking:

- What surprised you about the first half and what played out as expected? Surprises were several: the shift in Federal Reserve policy stance that pushed up interest rates, the strong equity market rally and poor performance by emerging markets. As expected? The US economy: slow growth and low inflation.
- Will stocks go higher or is this a correction? Will volatility stay high? Stocks should make further gains, though more slowly and with more volatility. Uncertainty from policy and economic questions will remain high.
- When will the Fed begin changing policy and what impact will that have? Policy and markets are already shifting. The market will likely overshoot. These forces bring our forecast for the 10-year US Treasury up to 2.50% for the year end.
- What is the state of the global economy? Are risks from Europe receding? The global economy remains in slower growth mode, with less risk of widespread recession. Japan is a bright spot. But Europe remains a source of risk.
- Where are the best opportunities in stocks from geographic and sector perspectives? US stocks are not as cheap as last year, but energy and tech sectors are attractive. Lower valuations from underperforming emerging markets may offer value.
- Will emerging markets underperformance continue? We would not be surprised to see continued challenges for emerging markets. However, we believe the longer-term secular investment story remains attractive.
- Given volatility, where are opportunities in fixed income? The potential tapering of Fed policy means underweight Treasuries and MBS. We would avoid TIPS as well. High yield is more attractive, and flexible portfolios offer adaptable approaches that can be opportunistic across maturity, sector, quality and geography.
- Will the recent weakness in municipal bonds persist? While municipal bonds have not been spared from the recent bond market selloff, the correction has created value that should reignite demand for owning the asset class.
- What is the outlook for gold prices? Gold should remain a strategic part of portfolios. However, we would reduce holdings amid rising real interest rates.

1 What surprised you about the first half and what played out as expected?

"The shifting interest rate outlook—both in nominal and real, after inflation rates—changes the game."

Surprises were several: the shift in Federal reserve policy stance that pushed up interest rates, the strong equity market rally and poor performance by emerging markets. as expected? The US economy: slow growth and low inflation.

There are always surprises, and the biggest one in the first half—and the one with greatest impact—was the apparent shift in the Fed's policy stance that emerged after the June FoMc statement. Even before this shift in communications which, intentional or not, sent Treasury rates markedly higher, real rates—the yields on inflation protected Treasuries—had been going up, providing an important clue for capital markets.

The shifting interest rate outlook—both in nominal and real, after inflation rates—changes the game: In a world accustomed to a global excess of dollars available at zero interest cost to borrow, the Fed's policy shift has an even greater impact on global investing. While we had anticipated that the Fed's shift would lift the dollar and weigh on gold, the knock-on effect on emerging markets have been most surprising. While we had a neutral stance on emerging market debt, investors' shift toward perceived safety closer to home was surprising for its speed. With china policy also impacting markets, emerging market stocks suffered as well. We still believe emerging market stocks offer a compelling long-term story, but headwinds will remain for the near term.

In the US, while we began the year with a positive view on stocks, the magnitude and composition of the equity rally were surprising. Normally, when markets rally it is the higher-risk, more cyclical sectors that outperform. For most of the year, however, the defensive sectors were the winners, helping to lift the overall market 15% by May.

Overall, however, the US economy progressed as we thought it would. During the first six months of the year, real growth in the United States was close to the 2% level, around the same rate we have seen since the recession ended in 2009. Inflation has remained well contained. Economic performance in Europe and Japan—sluggish growth in the former and a monetary-policy-induced pickup in the latter—was broadly as expected.

DESPITE RISE IN REAL RATES, TREASURIES REMAIN OVERVALUED

Round Trip: US 10–Year Real Interest Rate

Source: Bloomberg, 7/8/13. TIPS=Treasury Inflation-Protected Securities

2 Will stocks go higher or is this a correction? Will volatility stay high?

"Stock prices can make further gains from here, but they will likely do so at a slower pace and with increased volatility."

Stocks should make further gains, though more slowly and with more volatility. uncertainty from policy and economic questions will remain high.

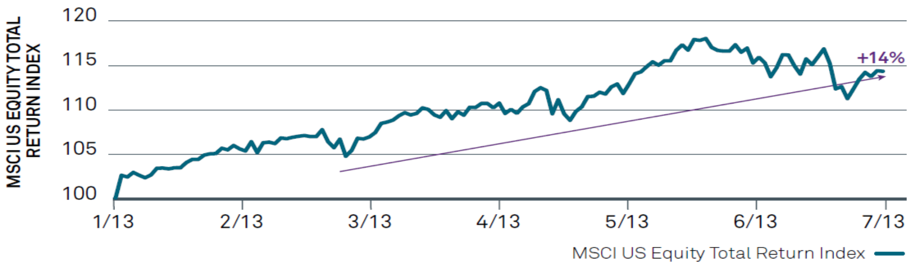
In short, yes. We believe stock prices can make further gains from here, but they will likely do so at a slower pace and with increased volatility. Stocks are still supported by reasonable valuations (particularly when compared to bonds). This is especially true outside of the United States, where most markets are trading at significant discounts. Additionally, corporations remain in strong shape and profit

That said, the higher volatility we have seen over the past month is likely to continue. First, we expect to see continued sluggish growth in the second and third quarters (probably close to 2%, near the 1.8% pace seen in the first quarter). Some of this slowdown will result from the delayed impact of the "sequester" (the automatic spending cuts that are going into effect), and some is coming about due to weakening consumer spending. All else being equal, slower growth tends to be associated with higher levels of volatility.

Secondly, and perhaps more importantly, the angst over central bank policy will help keep market volatility high. To the extent there continues to be uncertainty over the future direction of Fed policy—and the Bank of Japan—we are likely to see higher levels of stock market volatility.

US EQUITIES HAVE RALLIED, BUT HAVE ROOM TO RUN

Equity Total Return



Source: Thomson Reuters Datastream, 6/26/13.

Policy is already shifting with communications and markets are shifting away from riskier assets. It will be bumpy and the market will likely overshoot. These forces bring our forecast for the 10-year US Treasury up to 2.50% for the year end.

3 When will the Fed begin changing policy and what impact will that have?

The recent communication efforts by the Fed's policy makers have effectively marked the beginning of the end of quantitative easing. But the Fed may have inadvertently exacerbated market uncertainty in its efforts to communicate its exit strategy. The market reaction demonstrates investors' shift in assumptions toward the reality that central bank accommodative policies will not continue indefinitely. Indeed, markets now estimate the start of tapering later in 2013 and actual tightening (a rise in the Fed Funds rate) to take place year-end 2014. What was once a matter of forecasting the Fed's interpretation of the economy now means investors must interpret the Fed path based on their own overly-

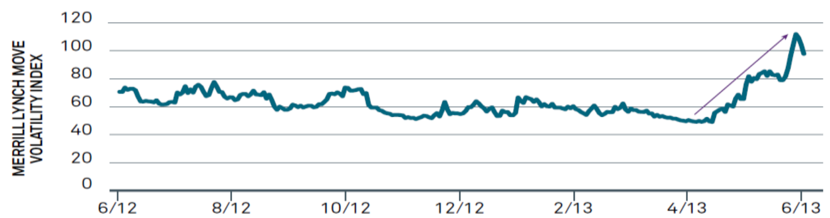
> “Competing forces bring our forecast for the 10-year Treasury to 2.50%, up from 2.25%.”

optimistic forecasts, as well as the potential bond market overreaction and Fed counter- reaction. How does the Fed proceed if labor markets do not show sufficient progress as needed for tapering to take place? Furthermore, internal dissention within the FoMc over more or less accommodative policy has contributed to market uncertainty.

For all practical purposes, the impact of potential tapering is already being felt, since those remarks helped trigger the recent downturn in stock prices, the spike in yields and rising volatility. Looking at the remainder of the year, the bumpy feedback cycle will continue: Fed communication leads to market overreaction leads to Fed clarification leads to market normalization. Ultimately, these competing forces bring our forecast for the 10-year Treasury to 2.50%, up from 2.25%.

So what does all of this mean for investors? We would continue to advocate underweight positions in Treasuries. Volatility in Treasuries is up as shown in the chart, and we believe will remain elevated. Even with the recent increase in real interest rates, we still believe Treasuries are overvalued and expect that yields are likely to rise over the long term. In any case, however, bond market yields are likely to trade unevenly, and investors should not be surprised if they see some sort of near-term drop in yields as markets overreact one way or the other.

US TREASURY VOLATILITY WILL REMAIN HIGH



Sources: Thomson Reuters Datastream, Merrill Lynch, BlackRock Investment Institute, 6/25/13. The Merrill Option Volatility Expectations Index (MOVE) reflects a market estimate of future Treasury bond yield volatility.

4 What is the state of the global economy? Are risks from Europe receding?

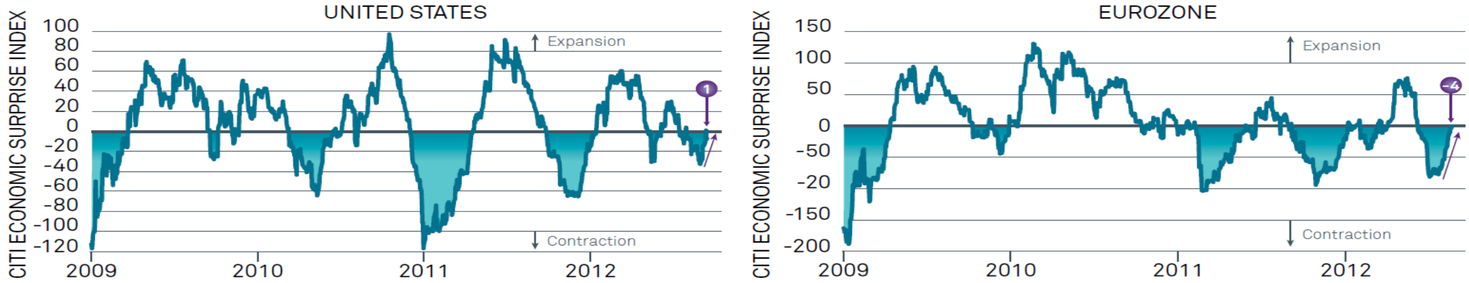
The global economy remains in slower growth mode, with less risk of widespread recession. Japan is a bright spot. But Europe remains a source of risk.

> “There is less risk now of a widespread global recession than there was one year ago.”
> .

The global economy is still mired in a slower growth mode. Indeed, in the second quarter, many areas of the world appeared to be decelerating further—particularly many emerging markets. There is less risk now of a widespread global recession than there was one year ago (thanks in large part to an avoidance of the worst of the “fiscal cliff” and to some more aggressive action from the European central Bank), but overall global growth is still hovering around a relatively slow 3.3% to 3.5%. one surprising bright spot has been Japan. Following decades of economic stagnation, that country’s economy grew at an astounding 4.1% in the first quarter.

In terms of Europe, the near-term threat of an outright breakup of the eurozone has definitely receded. There remain, however, ongoing threats. The banking system is fragile and undercapitalized and remains a source of risk (as we saw in the Cyprus debacle earlier in the year). Real reform will require more political will than we have seen in Europe, and given the German elections in September, we don’t expect much progress until a new German government is formed.

EUROZONE: UPSIDE ECONOMIC SURPRISE TO COME?



Sources: Thomson Reuters Datastream, Citigroup, BlackRock Investment Institute, 6/25/13.

5 Where are the best opportunities in stocks from geographic and sector perspectives?

> "We would suggest a focus on cyclical sectors of the market (although not those that have excessive exposure to the US consumer)."

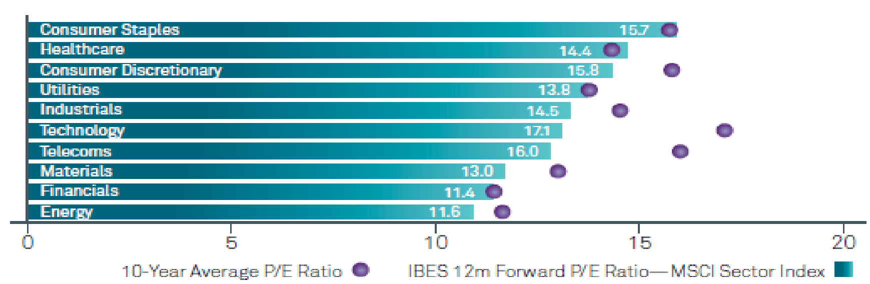
US stocks are not as cheap as last year, but energy and technology sectors are attractive. Lower valuations from underperforming emerging markets may offer value.

US corporate earnings have not been keeping pace with stock price gains, which means that US stocks are not nearly as cheap as they were last fall. Nevertheless, we expect the market can continue to perform well (although, as we stated earlier, investors should expect slower gains and more volatility). In particular, we would suggest a focus on large and mega-cap US stocks as opposed to their smaller-cap counterparts.

From a sector perspective, most of the defensive sectors, particularly Real Estate Investment Trusts (REITS) and utilities appear overvalued and tend to perform poorly in rising interest rate environments. Instead, we would suggest a focus on cyclical sectors of the market (although not those that have excessive exposure to the US consumer). As such, we have a particularly favorable view toward the energy and technology sectors, both of which look inexpensive.

Outside of the United States, we are seeing some good values in international stocks. While we would back away from US yield plays, dividend stocks look cheaper outside the United States. Additionally, emerging markets have underperformed so far this year and are trading at a significant discount compared to developed markets. We believe valuations have reached depressed levels and this may present some attractive entry points. In particular, we are seeing good long-term value in parts of Asia and Latin America.

FOCUS ON CYCLICAL SECTORS LIKE TECHNOLOGY



Source: Thomson Reuters Datastream, BlackRock Investment Institute, 7/5/13. P/E=Price/Earnings.

6 Will emerging markets underperformance continue?

"Together, stronger macroeconomic conditions and attractive valuations make for a compelling long-term argument for emerging markets equities."

We would not be surprised to see continued challenges for emerging markets. However, we believe the longer-term secular investment story remains attractive.
In the short term, we would not be surprised to see additional performance challenges for emerging markets. Slowing growth, concerns over the Chinese banking system and a general preference among investors for US stocks have been hurting performance and these trends are not going away any time soon. Finally, a less accommodative monetary regime and a stronger dollar will represent additional headwinds for many EM countries.

Over the longer term–say, three to five years—however, we believe emerging market stocks represent good value, given that they are trading at more than a 30% discount to developed markets, the largest gap since the end of 2008. Although the stellar economic growth we saw in china and India in 2010 is not likely to be repeated, emerging markets growth as a whole should continue to outpace that of developed markets. In addition, while emerging markets face numerous headwinds, by many measures EM countries are more stable than many developed markets, with lower sovereign debt, significant currency reserves and (with some notable exceptions) relatively stable current account balances. Together, stronger macroeconomic conditions and attractive valuations make for a compelling long-term argument for emerging markets equities.

7 Given volatility, where are opportunities in fixed income?

"We would advocate scaling back in loans in favor of high yield bonds."

The potential tapering of Fed policy means underweight Treasuries and MBS. We would avoid TIPS as well. High yield is more attractive. Incorporate flexible portfolios that offer adaptable approaches that can be opportunistic across maturity, sector, quality and geography.

First, we would point out the obvious: The potential for a tapering of Federal Reserve asset purchases would cause the most pain to those segments of the market that the central bank is buying—namely Treasuries and agency mortgage-backed securities. Given this backdrop, and our belief that better value can be found elsewhere, we would continue to recommend underweight positions in these areas of the market. At the same time, while restoring a positive real (inflation-adjusted) interest rate environment improves the outlook for TIPS, more volatility remains a risk and we would look to avoid this area of the market.

With real (inflation-adjusted) interest rates–and bond market volatility–rising, investors should be mindful of their bonds' duration. For some time we have advocated the benefits of bank loans as a lower risk alternative for higher yielding fixed income because of their better valuations, higher position in the capital structure, and from a longer-term point of view, the benefits of the floating rate reset to protect from a turn in the interest rate cycle. While loan performance held up much better than bonds in May and June that was more due to perception than reality - strong inflows into the sector bolstered demand and supported prices. However, they have not protected investors from the rise in longer maturity yields. We would advocate scaling back in loans in favor of high yield bonds for the higher risk income segment of fixed income portfolios.

In addition, investors may want to consider a more flexible and opportunistic approach in their fixed income portfolio, particularly funds which employ an adaptable investment approach across fixed income sectors without constraints on maturity, sector, quality or geography.

8 Will the recent weakness in municipal bonds persist?

> "We advocate a tactical approach in municipal bond portfolios."

While municipal bonds have not been spared from the recent bond market selloff, the correction has created value that should reignite demand for the advantages of owning the asset class.

Muni markets were not able to avoid the broad selloff in bonds that occurred as a result of uncertainty over Fed positioning. Waning demand and lower-than-expected supply exacerbated the situation. After two years of very strong inflows, demand patterns have recently grown much more sporadic.

The biggest headline maker over the past quarter centered on Detroit, MI. After decades of fiscal struggle (including declining population, employment and tax receipts), Detroit appears to be inching toward bankruptcy. While a chapter 9 filing by Detroit would be the largest ever in the municipal market, the city's distress has been long in the making and well telegraphed and, as such, we do not anticipate significant market risk, as clarity will be long in coming.

We advocate a tactical approach in municipal bond portfolios, as the higher volatility and more muted demand than we had anticipated at the start of the year comes to bear. The recent market correction, although painful, was healthy in that it created value — and value begets demand. Further bolstering the case for munis is a strong reinvestment period in July and August, as some $75 billion in coupons, calls and maturities will be looking to find its way back into the market. As we pointed out at the start of the year, the frothy returns of 2012 and 2011 are unlikely to be repeated in 2013, and muni investors should adjust their expectations accordingly. overall, tax-exempt munis remain an attractive choice for income-oriented investors, particularly in an environment of higher tax rates.

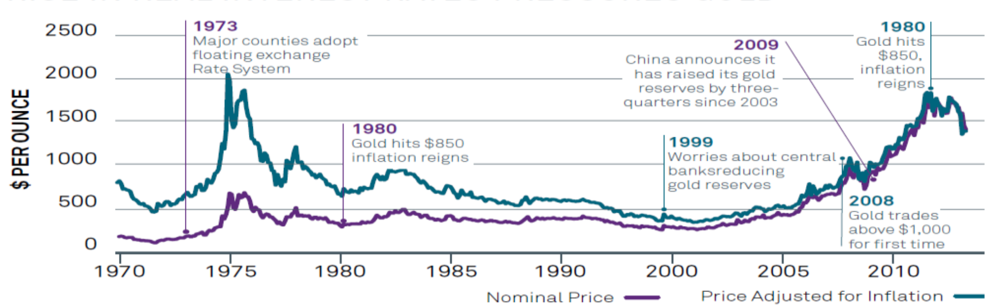
9 What is the outlook for gold prices?

> "We do, however, expect gold prices to remain volatile, and expect a general downward bias in the price of the precious metal."

Gold should remain a strategic part of portfolios. However, we would advocate reducing holdings of gold amid a rising real interest rate environment.

We think investors should hold gold as a long-term, strategic part of their portfolios. However, we expect gold prices to remain volatile, and expect a general downward bias in the price. Sentiment has clearly changed in the gold market and we would now advocate reducing holdings in this asset class. Gold prices are facing the headwind of rising real interest rates (adjusted for inflation) for the first time in years. Many investors focus on inflation and the US dollar when thinking about gold prices, but real interest rates actually tend to have a more significant effect. All else being equal, higher real interest rates should create a less supportive environment for gold.

RISE IN REAL INTEREST RATES PRESSURES GOLD



Source: Thomson Reuters Datastream, BlackRock Investment Institute, 7/5/13.

Turning Answers Into Investment Actions

The second quarter presented a number of surprises to investors, from the recent bond selloff to the continuation of the rally in equities. In this context, we highlight the risks investors may be exposed to in traditional core bond portfolios and suggest investors take a more flexible, risk-aware approach that can better respond to market changes.

Investment Actions to Consider:

1 BROADEN YOUR BOND APPROACH

2 FIND NEW SOURCES OF INCOME

3 SEEK WEALTH IN UNPREDICTABLE MARKETS

Allocate To Flexible Core Bond Alternatives — Flexible core bond strategies are not tethered to benchmarks, and can thus seek to diversify risks in response to market changes to increase yield, reduce duration and properly manage downside risks.

Increase Exposure To Credit Sectors — Credit sectors of the fixed income market provide an attractive risk/reward opportunity, especially as companies have materially improved their credit profiles.

Implement Long/ Short Strategies — Implementing long/short strategies can help mitigate interest rate risk, smooth volatility and increase diversification, although diversification does not ensure a profit or protect against a loss in declining markets.

For additional analysis, the BlackRock Investment Institute published its *Entry, Exit and Overshoot* report, which discusses the fork in the road for monetary policy and financial markets and details emerging market and rate rise risks.

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Investment involves risks. Stock and bond values fluctuate in price so that the value of an investment can go down depending on market conditions. International investing involves additional risks, including risks related to foreign currency, limited liquidity, less government regulation and the possibility of substantial volatility due to adverse political, economic or other developments. These risks are typically heightened for investments in emerging markets. Typically, when interest rates rise, there is a corresponding decline in the market value of bonds. Credit risk refers to the possibility that the issuer of the bond will not be able to make principal and interest payments. There may be less information available on the financial condition of issuers of municipal securities than for public corporations. The market for municipal bonds may be less liquid than for taxable bonds. A portion of the income from municipal securities may be taxable.

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Fitch: Leveraged CEFs Lose as Rates Inch Higher

July 03, 2013

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Fitch Comments on Leveraged Closed-End Fund Performance Through Recent Market Turbulence

The recent rise in U.S. Treasury yields and speculation surrounding possible changes in the Fed's buying program led to leverage ratio increases and discounts widening for leveraged CEFs, according to Fitch. Market turbulence and increasing interest rates challenged CEF portfolio managers (PMs), but also presented buying opportunities for PMs conservatively positioned before May.

Click here for complete reading

Sources: Fitch, public financial statements.

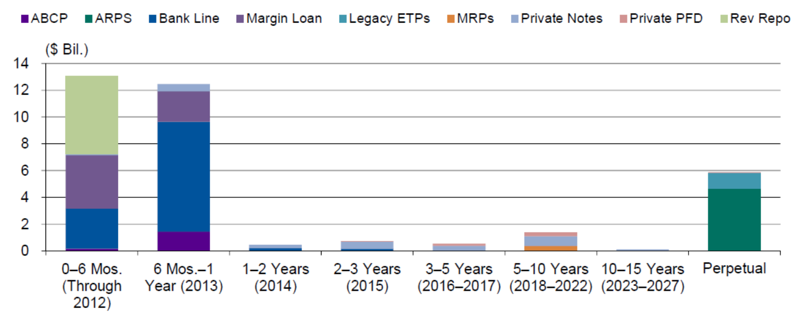
Basel III to Affect Taxable Closed-End Funds

June 18, 2013

Basel III Expected to Increase Borrowing Costs: Basel III banking capital requirements are expected to result in increased borrowing costs and, potentially, diminished availability of bank provided credit with migration of lending toward less regulated segments of the financial system (e.g. shadow banking). Regulation of the repo market is also impacting availability of repo funding nontraditional collateral. This has implications for closed-end funds (CEFs), especially taxable CEFs, as they are heavily reliant on repos and bank lines of credit as providers of leverage.

CEF Credit Quality to Mute Cost Increases: The high credit quality of CEFs borrowers will serve to mute the impact of Basel III relative to other borrowers. Basel III applies relatively higher capital requirements to riskier lending activities, which could cause banks to focus on reducing their exposure to lower rated and more volatile sectors. By contrast, CEFs are generally viewed as having low credit risk, with Fitch Ratings generally assigning ratings of 'AAA' to the senior borrowings of CEFs,

Taxable Closed-End Funds — Debt Maturity Schedule



Notes: Data cover 200 taxable closed-end funds with approximately $34.6 billion of the above leverage types outstanding as reported in latest financial statements available as of Sept. 15, 2012. The data exclude the use of derivative leverage and $2.5 billion in leverage of the to-be-announced securities, securities sold short,and securities lent.

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Click here for complete reading

Sources: Fitch, public financial statements.

Click here for complete CEF Rating Actions

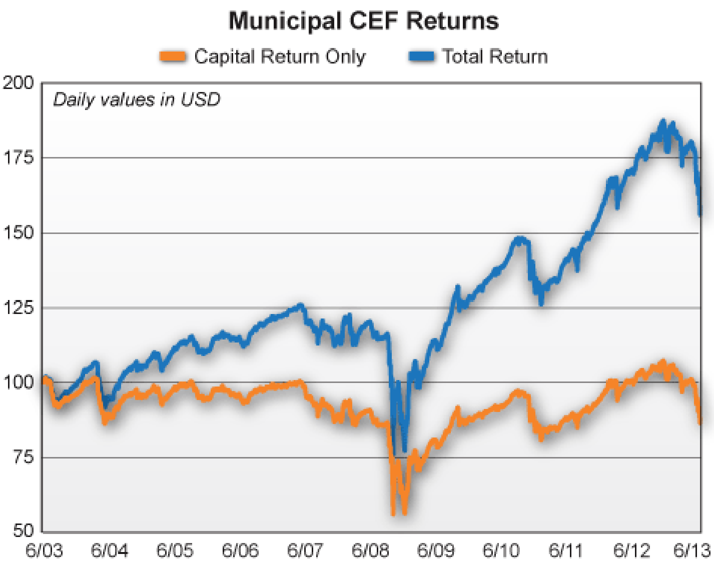
Update on Municipal Closed-End Funds

July 05, 2013

Authored by:
Jeff Margolin
Senior Vice President
Closed-End Fund Strategist
First Trust Advisors, LP.

Despite a wider than historical current average discount to NAV of 4.91% (as of June 24, 2013 according to Morningstar); attractive average yields of 6.63% (Morningstar) for national leveraged funds; and the fact that within the past couple of weeks the Fed clearly stated it is not raising short-term interest rates anytime soon, the market has yet to see meaningful buying in the municipal CEF category. One of the main reasons we continue to see volatility among municipal CEFs, in my opinion, is related to the factors currently negatively impacting the underlying municipal bond market.

Right now both open-end municipal bond mutual funds and municipal ETFs are dealing with significant outflows from investors. While the municipal bond market is an enormous market—with over one million bonds outstanding—many of these bonds don't trade every day. Nevertheless, open-end mutual funds are forced to sell meaningful amounts of individual bonds to meet redemptions. As there are not a lot of muni bond buyers in the market currently, fund managers are forced to mark down the price of the bonds, thereby making them more attractive for investors to purchase. The result of some of this illiquidity in the underlying municipal bond market is that municipal bond prices have declined—even more than U.S. Treasuries—on some days (as on 6-24-13).



Source: Morningstar. Data 6/2/03 through 6/24/03.

While there continues to be redemptions in the municipal bond market, historically when yields in individual bonds get to these levels (relative to Treasuries and even corporates), it has attracted interest from retail and/or institutional "cross-over" buyers, which in turn has historically firmed up the market. (The definition of an institutional "cross-over" buyer is an institutional manager who generally only buys taxable bonds because they usually yield more than tax-exempt municipal bonds. However, at times, the institutional managers will "cross-over" to the tax-exempt municipal bond market when yields on municipal bonds rise above taxable bonds and credit quality is comparable, or even better.)

Lastly, during these periods of increased volatility in municipal closed-end funds, it is important to remember the significant and compelling distributions funds continue to make. Indeed, as the chart below clearly shows, the compounding impact of distributions adding up over time is a significant contributor to the historical total return of municipal closed-end funds. "Capital Return Only" shows the price performance of municipal CEFs over the past 10-years ended 6-24-13 and "Total Return" shows municipal CEFs including distributions over the same period.

The chart is for illustrative purposes only and not indicative of any investment. Past performance is no guarantee of future results. An index cannot be purchased directly by investors. Closed-end funds are subject to various risks, including management's ability to meet the fund's investment objective, and to manage the fund's portfolio when the underlying securities are redeemed or sold, during periods of market turmoil and as investors' perceptions regarding the funds or their underlying investments change. Unlike open-end funds, which trade at prices based on a current determination of the fund's net asset value, closed-end funds frequently trade at a discount to their net asset value in the secondary market. Certain closed-end funds may employ the use of leverage which increases the volatility of such funds.

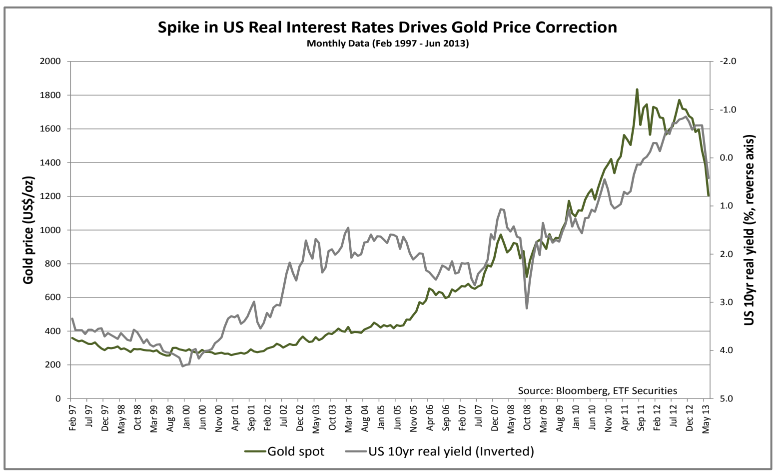
Precious Metals Return to Attractive Value

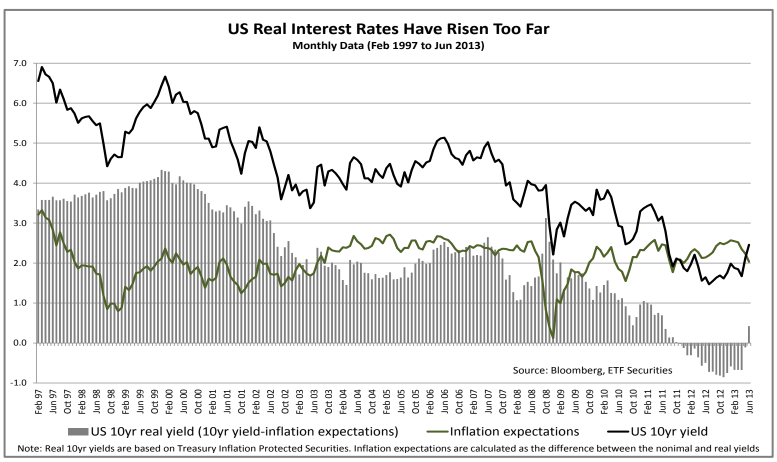
July 01, 2013

Authored by:
Nicolas Brooks
Head of Research and Investment Strategy, ETF Securities

- **The recent correction of the gold price to below $1,200/oz. has been driven by a sharp rise in US real interest rates on back of fears the Fed will reduce its bond buying program sooner than anticipated.**
- **We believe the reaction of bond markets to Fed comments has been overdone, and ultimately real rates will fall from current levels, driving a rally in the gold price.**
- **On our estimates, gold, silver and platinum (with implications for palladium) are now trading around 20%, 10% and 25% below their respective average marginal costs of production. Prices will have to move above these levels to support long-term supply growth.**
- **Short gold futures positioning on COMEX is at an all-time high and silver shorts are now at over 10-year highs, indicating scope for powerful short covering rallies once fundamentals improve.**
- **Physical gold buyers, notably in China, have increased purchases as the price has dropped.**
- **While precious metals prices will be driven primarily by macro and technical factors in the near-term, we believe that at current levels they provide attractive value for long-term investors.**

All good bull markets need a correction. After a twelve year run, the gold price was well overdue a major correction and this is now taking place, albeit at a much higher velocity than its increase – as is usually the case. The silver price has been dragged down with gold, and platinum and palladium prices have been affected by China growth concerns as domestic liquidity has been squeezed. We believe the price corrections have been excessive and have returned precious metals prices to attractive long-term accumulation levels.

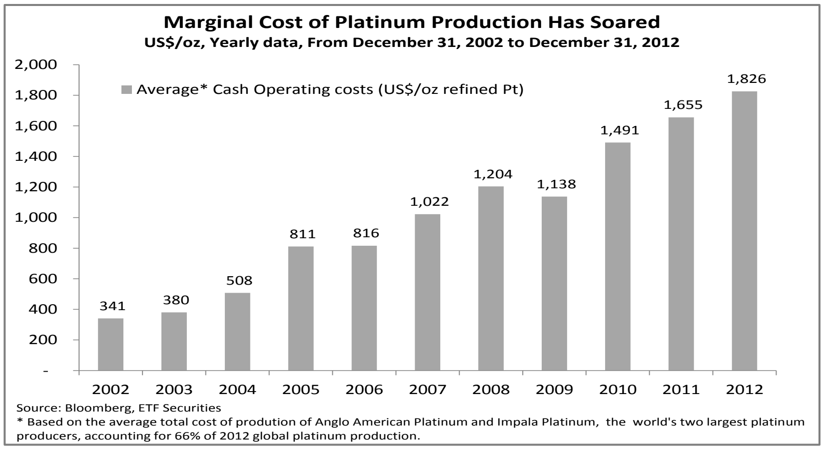


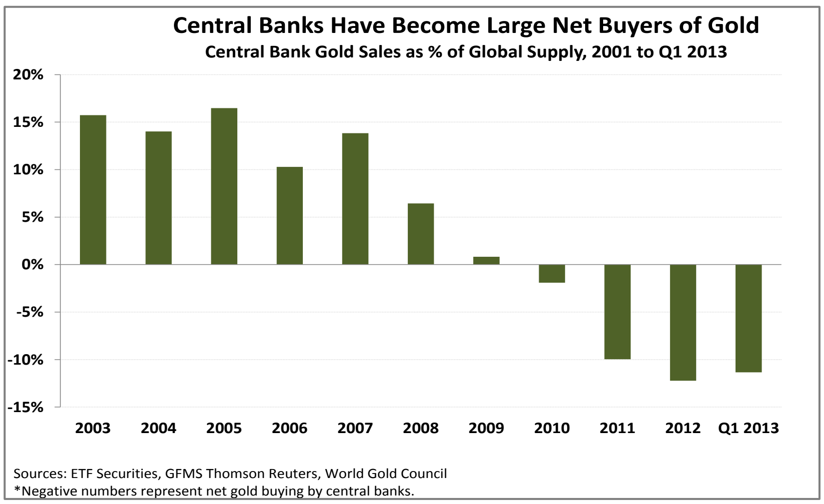


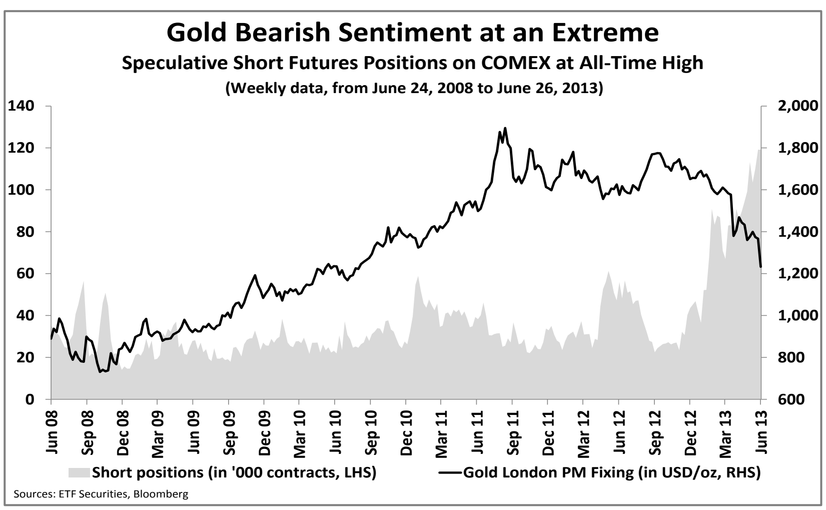
Prices now below marginal production costs

On our estimates, all of the precious metals are now trading below their all-in marginal costs of production (cash costs plus capital and exploration costs) – and in some cases quite significantly below them. The costs of finding and extracting precious metals have surged in recent years. Gold cash costs have increased nearly five-fold over the past ten years and platinum costs have soared even more. The average marginal cost of production of gold for the largest gold miners is somewhere around $1,500/oz. on our calculations, with a number of mines with all-in costs well above $2,000/oz. In recent comments by Gold Fields CEO Nick Holland, he highlights that in his view the industry needs a gold price of at least $1,500/oz. to sustain the industry in “any reasonable form”. The average all-in marginal cost of platinum production in South Africa on our estimates is around $1,800/oz. This is directly relevant for palladium as it is a by-product of platinum production. The average marginal cost of silver is estimated to be around $20/oz.

Therefore, on our estimates, gold, silver and platinum (relevant for palladium too) are now trading around 20%, 10% and 25% below their respective average marginal costs of production. While prices can remain below marginal production costs for a while, ultimately, as mines are closed and supply begins to dry up, prices are forced back up again. This is already occurring, with Anglo American Platinum shutting a number of South African platinum shafts earlier this year, and gold miners now slashing costs across-the-board. If prices do not rebound quickly, closures are likely to accelerate, reducing anticipated supply, leading to a self-fulfilling increase in prices.







Important Risks

• Commodities generally are volatile and are not suitable for all investors.

• The statements and opinions expressed are those of the authors and are as of the date of this report. All information is historical and not indicative of future results and subject to change. Reader should not assume that an investment in any securities and/or precious metals mentioned was or would be profitable in the future. This information is not a recommendation to buy or sell. Past performance does not guarantee future results.

Where to from here?

Despite the near unanimous negative sentiment towards the gold price and most of the other precious metals, we believe that longer term fundamentals remain price supportive and ultimately will re-assert themselves once cyclical and technical factors move again in their favour.

The weak and fragile nature of the US recovery, continued recession in Europe, and large sovereign debt burdens in the major developed economies are likely to keep central banks firmly in stimulus mode. On the other hand, the growth of precious metals supply, as highlighted above, is being hit by substantially higher costs of production and increasingly scarce new finds. The increase in gold supply has been less than 10% over the past decade compared to a near tripling of US dollar money supply. It should be no surprise that the price of gold has risen so much in US dollar terms!

Emerging market central banks are a new major source of gold demand. Central banks as a group have been large net buyers of gold since 2010. They are now buying the equivalent of over 10% of annual gold supply, reversing years of net selling equivalent to 10-15% of annual supply. Chinese physical demand for gold has exploded, with Chinese imports of gold through Hong Kong now equivalent to just under 20% of total global gold demand, up from levels of under 3% 10 years ago. Increases in China's gold import quotas this year have led to a renewed surge of China physical gold buying, with accelerated buying since the April price correction. While India has moved to curb gold imports by increasing tariffs on gold imports and forbidding gold import financing, cash purchases and smuggling are likely to at least partially offset the restrictions.

Outlook

Given the technical nature of the recent sell-off, short term moves in the gold price are difficult to predict. Further declines can't be ruled out. However, at these levels, strategic buyers – central banks, Chinese and Indian consumers, long-term investors – are likely to see value. In addition, with short-term interest rates expected to stay low for the foreseeable future, the opportunity cost of holding store-of-value assets such as gold should remain low. Of course, in the near-term, gold needs a positive impetus – a reduction in US real yields, a weaker US dollar, renewed sovereign crisis in Europe – to sustainably resume its bull market climb. However, with COMEX speculative short positions at an all-time high, physical demand re-emerging, and the gold price now trading well below the average marginal cost of production, we believe gold provides substantial potential upside, as well as continued tail risk insurance, for long-term investors. Silver will likely continue to trade as a higher beta version of gold. Platinum and palladium offer particularly attractive longer-term value at current levels in our view, with prices now substantially below their marginal costs and supply cuts already underway.

When the Going Gets Tough, the Tough Use ETFs

July 03 ,2013

Authored by:
Dodd Kiittsley, CFA
Director, Global Head of ETP Research, BlackRock

Investors talked and ETFs sure listened in June.

While we've written about market rollercoasters and nail biters here on the blog before, this past month was a doozy, and we saw investors turn to ETFs to express their rapidly shifting market views.

Heading into June, global ETF flows were following a record-setting pace, breaking through the $100 billion mark. But market sentiment shifted toward the end of May when Fed Chairman Ben Bernanke signaled that the Fed could slow its bond-buying program. After Bernanke said on June 19 that the Fed could begin tapering its monetary stimulus before the end of 2013, yields on the 10-year Treasury jumped and global investors –who have become hypersensitive to central bank comments – reacted quickly, selling emerging markets equity, gold and fixed income ETFs.

June marked the first time global fixed income ETFs saw monthly outflows since December of 2010. Investors moved into shorter duration ETFs (which are generally less sensitive to interest rates and will lose less when rates rise), and the category attracted $5.5 billion of flows globally. But other fixed income maturity categories saw outflows of $13.5 billion globally.

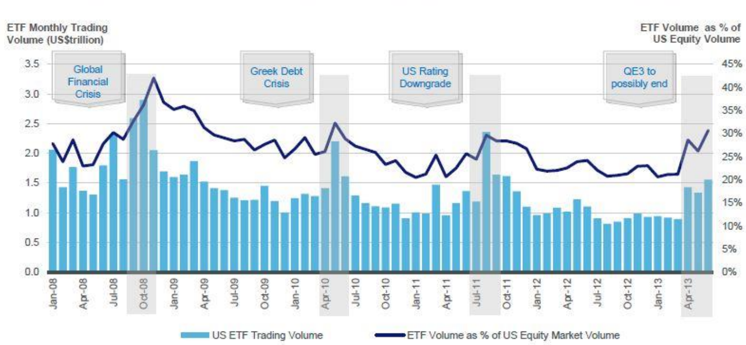
In total, global ETF outflows for June totalled $8.2 billion, and it was the first month of outflows since November of 2011.

Simultaneously with these flows, US ETF volumes spiked in June (see below), once again illustrating how investors are using ETFs to express market sentiment – even when that sentiment changes dramatically.

This is a trend we've seen before. When headline-making news triggers a sudden shift in investor sentiment and market volatility jumps, it has been followed by elevated ETF trading volumes in absolute dollar terms and also in proportion to total US equity market trading volumes. In June, ETFs accounted for 31% of the dollar value of all trading volume in US equity markets, up from 20-25% in recent months.

It's important to note that June saw orderly trading of ETFs and, as designed, ETFs delivered liquidity under stressed market conditions.[2] Investors were able move quickly and efficiently in and out of investment exposures, and this is a trend we expect will continue as more investors turn to ETFs to execute precise market views.

US LISTED ETF MONTHLY TRADING VOLUME AS A PERCENTAGE OF EQUITY MARKET VOLUME[1]



1. Data source BlackRock ETP Research and Bloomberg. Data is as of June 30, 2013
2. Source: Bloomberg as of June 2013. Market volatility was sourced from Bloomberg as measured by elevated levels in the VIX and MOVE indexes. The MOVE index is up 125% in May-June 2013 (110.98 on June 24th 2013 vs. 49.24 at end of April).

Source: BlackRock ETP Research and Bloomberg

Some Top-Ranked ETFs in Newly Favored Sector

June 21, 2013

Authored by:
Todd Rosenbluth
Senior Director,
S&P Capital IQ Equity Research
@TRosen_SPCAPIQ

Earlier today, S&P Capital IQ's Equity Strategy Group upgraded its view on the Financials sector to Overweight, from Marketweight. The group cited the strong fundamentals and favorable trading patterns of the sector on an absolute and relative basis. We think one way to potentially benefit from these trends is through ETFs.

S&P Capital IQ Chief Equity Strategist Sam Stovall believes that the S&P 500 Financials Sector will outperform the S&P 500 in the months ahead as the bull market undergoes a shift from being liquidity driven to fundamentally driven. Stovall noted that consensus estimates from Capital IQ project Financials sector operating EPS to rise 11.0% in 2013 versus the 6.8% gain seen for the S&P 500. He also referenced that the anticipated acceleration of the Fed's tapering timetable has steepened the yield curve, which could add a tailwind to Financials' profit growth.

On Wednesday, the Federal Reserve stated that it was maintaining its $85 billion monthly bond purchases and its exceptionally low range" for the federal funds rate tied to whether the unemployment rate remains above 6.5%. It said that "inflation has been running below the Committee's longer-run objective," and that it is "partly reflecting transitory influences." In addition, it said that "the Committee sees the downside risks to the outlook for the economy and the labor market as having diminished since the fall." To S&P Capital IQ, these statements increase the chances that the start date for a reduction in QE bond purchases will be this year, depending on the data. The Equity Strategy Group believes when a move is made, it is likely to be at a meeting with a press conference, such as September.

S&P Capital IQ has rankings and reports on 84 different ETFs tied to the Financials sector, but only 12 of them receive our top ranking of Overweight, based on a combination of performance, risk and cost factors, including the relative appeal of the ETF's holdings and its expense ratio. The ETF rankings are not directly connected to the Equity Strategy Group's views and as such there are also Financials ETFs that are viewed negatively.

The largest of the top-ranked ETFs is Financial Select Sector SPDR (XLF 19 Overweight), which has over $13 billion in assets. This ETF holds the stocks in the S&P 500 Financials sector, with JPMorgan (JPM 52 ****) the ETF's largest holding and its top-10 holdings representing 51% of assets as of May 31. The highest sub-industry representation in the ETF are Other Diversified Financial Services (21% of assets) and Property & Casualty Insurance (14%). Erik Oja, an S&P Capital IQ equity analyst who covers the Other Diversified Financials sub-industry, projects strong profit growth for this group in 2013 helped by housing price increases and capital markets growth. XLF ranks favorably for positive S&P Capital IQ Fair Value and S&P Capital IQ Technical inputs as well as a relatively low expense ratio and tight bid/ask spread.

Oja, who also follows the Regional Banks sub-industry for S&P Capital IQ, noted that these banks are generally well capitalized and managed and he expects that loan growth for them should pick up in 2013. He believes the interest margins of regional banks in particular should be a beneficiary of the rising interest rate environment as the 10-year Treasury has climbed approximately 80 basis points since the beginning of May to 2.45%. Oja thinks it might lead to faster loan originations and higher mortgage banking income now, as buyers rush ahead of possibly higher interest rates.

For investors who want higher exposure to Regional Banks than XLF or VFH offer, there are some additional highly ranked ETFs. One in particular, SPDR S&P Regional Banking ETF (KRE 33 Overweight), is concentrated solely in this sub-industry, while another, SPDR S&P Bank ETF (KBE 28 Overweight), has 70% of assets in the sub-industry and holds Thrifts & Mortgage and Other Diversified Services stocks as well. KRE holds 76 stocks including Regions Financial (RF 9 ****) and we think it is diversified at the holdings level with just 19% of assets in its top-10 positions. Helping the ETF's overall Overweight ranking is a favorable S&P Capital IQ Technical input, a tight bid/ask spread and a low expense ratio.

To learn more about these ETFs or to see the others that rank favorably within the recently upgraded Financials sector, visit the ETF tab of MarketScope Advisor.

Key Takeaways

With S&P Capital IQ's upgraded Financials sector view, we highlight several favorably ranked names in this area..

POSITIVE IMPLICATIONS

FINANCIAL SELECT SECTOR SPDR FUND	OVERWEIGHT	[XLF]
JPMORGAN CHASE & CO	★★★★	[JPM]
REGIONS FINANCIAL	★★★★	[RF]
SPDR S&P BANK ETF	OVERWEIGHT	[KBE]
SPDR S&P REGIONAL BANKING ETF	OVERWEIGHT	[KRE]
VANGUARD FINANCIALS INDEX FUND; ETF SHARES	OVERWEIGHT	[VFH]

The recommendations contained in this Takeaway box are current, and may have changed since the original story was published.

S&P CAPITAL IQ
McGRAW HILL FINANCIAL

Laddering Your Portfolio Through Bond ETFs

June 19, 2013

History is not a good way to judge future returns, so there's no point waiting three years for performance-based bond-fund rankings.

Authored by:
Isabelle Sender
S&P Capital IQ Editorial

S&P Capital IQ ranks newer exchange-traded funds (ETF) based on risks and costs because investors need to know now what fixed-income securities they should diversify amongst as the threat of rising interest rates loom large.

"In the case of the iShares 2016 Investment Grade Corporate Bond ETF (IBCB 100 Overweight), which matures in 2016, waiting three years for performance-based research means you would miss out on the whole point of the product," says Todd Rosenbluth, director of ETF and mutual fund research. IBCB launched in mid-April of this year, along with three other iShares taxable bond ETFs and already has an S&P Capital IQ ETF ranking and report.

S&P Capital IQ knows a three-year track record is less important for assessing ETFs, when risks at the holdings level and costs are known. For example, duration in this investing climate - in which the market is skittish about the end of central-bank accommodation -- is a risk that can be a negative reveal.

A defined-maturity bond fund, IBCB receives an overall overweight S&P Capital IQ ranking not based on its track record. S&P Capital IQ's ETF ranking methodology considers IBCB's risk considerations, such as credit quality, rated credit coverage, liquidity, and duration, favorably compared to other ETFs in its asset class. For cost factors, such as expense ratio, price to NAV, and bid/ask spread, S&P Capital IQ has an overall favorable ranking.

IBCB is not only an example of a newly launched ETF, it is also a useful tool for building a laddered bond portfolio - with potential benefits over the old way of laddering with individual bonds: "ETFs provide more diversification across issuers, enhanced liquidity, and lower costs," Rosenbluth points out.

Instead of purchasing multiple bonds to ladder, investors can ladder each defined-maturity ETF with different maturity dates, in order to maintain steady investor cash flows, decrease interest-rate risk, or decrease re-investment risk. As one ETF in the ladder matures, the cash is re-invested, and as rates rise and ETFs mature the funds can be re-invested into higher yielding ETFs.

Key Takeaways

TS&P Capital IQ ranks "young bond ETFs, which should help investors ladder their holdings.

POSITIVE IMPLICATIONS

GUGGENHEIM BULLETSHARES 2013 CORPORATE BOND ETF	OVERWEIGHT	[BSCD]
GUGGENHEIM BULLETSHARES 2013 HIGH YIELD CORPORATE BOND ETF	MARKETWEIGHT	[BSJD]
GUGGENHEIM BULLETSHARES 2014 CORPORATE BOND ETF	MARKETWEIGHT	[BSCE]
GUGGENHEIM BULLETSHARES 2014 HIGH YIELD CORPORATE BOND ETF	MARKETWEIGHT	[BSJE]
GUGGENHEIM BULLETSHARES 2015 CORPORATE BOND ETF	MARKETWEIGHT	[BSCF]
GUGGENHEIM BULLETSHARES 2015 HIGH YIELD CORPORATE BOND ETF	MARKETWEIGHT	[BSJF]
GUGGENHEIM BULLETSHARES 2016 CORPORATE BOND ETF	MARKETWEIGHT	[BSCG]
GUGGENHEIM BULLETSHARES 2016 HIGH YIELD CORPORATE BOND ETF	MARKETWEIGHT	[BSJG]
GUGGENHEIM BULLETSHARES 2017 CORPORATE BOND ETF	MARKETWEIGHT	[BSCH]
GUGGENHEIM BULLETSHARES 2017 HIGH YIELD CORPORATE BOND ETF	OVERWEIGHT	[BSJH]
GUGGENHEIM BULLETSHARES 2018 CORPORATE BOND ETF	OVERWEIGHT	[BSCI]

The recommendations contained in this Takeaway box are current, and may have changed since the original story was published.
Continued on next page.

In terms of choice, defined-maturity date fixed- income ETFs allow investors to tilt their portfolios in the preferred risk direction. For instance, they can concentrate on either high-yield or investment-grade bonds, while keeping the maturity target intact.

Other iShares defined maturity date fixed-income ETFs holding investment-grade bonds include iShares 2018 Investment Grade Corporate Bond ETF (IBCC 99 Overweight), iShares 2020 Investment Grade Corporate Bond ETF (IBCD 97 Overweight), and iShares 2023 Investment Grade Corporate Bond ETF (IBCE 95 Overweight).

Guggenheim Investments offers a family of defined-maturity bond ETFs called “BulletShares” with either an investment-grade corporate focus or junk-bond view. The following Guggenheim BulletShares corporate-bond ETFs hold more than 50% of assets in high-quality, A-rated bonds with the following maturities: 2013 (BSCD 21 Marketweight), which recently yielded 1.2%; 2014 (BSCE 21 Marketweight), which recently yielded 1.5%; 2015 (BSCF 22 Marketweight), which recently yielded 1.8%; 2016 (BSCG 22 Marketweight), which recently yielded 2.1%; 2017 (BSCH 23 Marketweight), which recently yielded 2.3%; and 2018 (BSCI 21 Marketweight), which recently yielded 1.9%. Ratings info comes from agencies including Standard & Poor’s Ratings Services, which operates independently of S&P Capital IQ.

Among its high-yield offerings, Guggenheim BulletShares holds lower-quality, higher yielding portfolios with the following maturities:2013 (BSJD 26 Marketweight), which recently yielded 4%; 2014 (BSJE 27 Marketweight), which recently yielded 4.3%; 2015 (BSJF 27 Marketweight), which recently yielded 5.1%; 2016 (BSJG 26 Marketweight) recently yielded 4.1%; 2017 (BSJH 27 Overweight), which recently yielded 4.4%; and 2018 (BSJI 27 Overweight), which recently yielded 5%. Not surprisingly, these high-yield ETFs incur greater credit risk than investment-grade corporate focused offerings, with most holdings rated BB or below.

Choosing duration is probably the most important benefit Rosenbluth sees among defined-maturity date fixed-income ETFs. “They allow investors concerned about higher interest- rates to focus on lower-duration ETFs, which have a fixed maturity date,” he adds. After all, since beginning of May, the yield on the 10-year Treasury increased 60 basis points, recently trading at 2.21%.

The expansion of the fixed income ETF universe in the last three year to include these defined maturity bond ETFs has given investors and advisors a lot more freedom to tailor their portfolios. To see reports on these ETFs, visit the ETF on MarketScope Advisor.

Key Takeaways

S&P Capital IQ ranks “young bond ETFs, which should help investors ladder their holdings.

POSITIVE IMPLICATIONS		
GUGGENHEIM BULLETSHARES 2018 HIGH YIELD CORPORATE BOND ETF	OVERWEIGHT	[BSJI]
ISHARES 2016 INVESTMENT GRADE CORPORATE BOND ETF	OVERWEIGHT	[IBCB]
ISHARES 2018 INVESTMENT GRADE CORPORATE BOND ETF	OVERWEIGHT	[IBCC]
ISHARES 2020 INVESTMENT GRADE CORPORATE BOND ETF	OVERWEIGHT	[IBCD]
ISHARES 2023 INVESTMENT GRADE CORPORATE BOND ETF	MARKETWEIGHT	[IBCE]

The recommendations contained in this Takeaway box are current, and may have changed since the original story was published.

Why Oil has Proven Resilient

July 05, 2013

Authored by:
Russ Koesterich
Managing Director, Global Chief Investment Strategist, BlackRock

This year has been rough for commodities. Gold is down roughly 25% in 2013, as is corn, while silver is off an astounding 35% through the end of June. But there has been one exception to this trend: energy, particularly oil.

Crude oil has proven more resilient and less volatile this year (depending on which benchmark you use, it is either up or down in the single digits) than most other commodities. There are three main factors behind this:

1. **Higher interest rates hit precious metals hard.** While the rate regime impacts all commodities, it typically has a more pronounced impact on precious metals. The big losses in gold and silver can largely be attributed to rising real rates. To the extent rates rise in the context of a normalizing economy, the impact is likely to be more muted for energy commodities.

2. **Fears about slower Chinese growth have hit industrial metals.** Losses in industrial metals – like copper, down 12% year-to-date – have been driven by fears over Chinese growth. As infrastructure building in that economy has accounted for much of the marginal demand for industrial metals, these commodities are hyper-sensitive to any perceived change in China's appetite for raw materials. However, the demand for oil tends to be tied to the global economy, rather than a single country. In addition, a Chinese rebalancing toward consumption may actually benefit oil as more middle-income consumers purchase cars.

3. **A drop in supply.** While surging North American production has captured investor imagination, what has gone largely unnoticed is the drop in supply from other sources. Heightened unrest in the Middle East and Africa, coupled with increasing sanctions against Iran, has resulted in big drops in production and exports. For example, sanctions on Iranian crude have caused exports to drop from over two million barrels per day to approximately 700,000 bpd, basically negating the surge in North American production. We've seen similar, though less dramatic drops from other OPEC producers, including Nigeria and Libya, both of whom are struggling with their own geopolitical issues.

With violence escalating in Syria and renewed unrest in Egypt, investors are increasingly worried about more supply disruptions, a fear reflected in risk metrics such as The Alliant Oil & Gas Country Risk Index. This is important as rising levels of geopolitical risk in oil producing countries have historically correlated with higher crude prices.

Going forward, my view is that oil remains what traders like to call "range bound," not moving particularly higher or lower. But, if it were to break out of its current range, I believe it is more likely to move higher given rising geopolitical tension. Assuming oil continues to hold at or near current levels, I would continue to advocate that investors take advantage of current prices in large-cap, global energy companies, which can be accessed through the iShares Global Energy ETF (IXC).

Source: Bloomberg data as of 6/30/2013

Stocks Stabilize But Risks Rise

July 08, 2013

Authored by:
Russ Koesterich
Managing Director, Global Chief Investment Strategist, BlackRock

Better Economic Data Stabilizes Stocks

With economic data coming in generally better than expected, equity markets stabilized and rallied last week. the Dow Jones industrial average gained 1.5% to close at 15,136, the s&P 500 index rose 1.6% to 1,632 and the nasdaq composite advanced 2.2% to 3,479. in bond markets, good news has meant bad news lately, and yields continued to rise (as prices correspondingly fell). For the week, the yield on the 10-year treasury climbed 0.23% to 2.72%.

Odds Rise That Fed Tapering Begins This Fall

The recent better-than-expected economic data has come from modest firming in the manufacturing sector, as seen in the uptick in the ism manufacturing survey, and a solid jobs report. while June's non-farm payrolls report of 195,000 new jobs was by no means the long hoped for breakout in the labor market, it was consistent with the 190,000 average for the past year and strong enough to indicate the recovery is making progress. although we see little evidence of the economy taking off, we continue to believe we should see slow improvement into year's end.

However, there is a flip side to continuing progress in the recovery: eventually, the Fed will have to pull back on its extremely accommodative monetary policy. at this time in the economic cycle, it means a tapering and eventual cessation of the Fed's quantitative easing bond-buying program. with a solid if uninspiring June payroll report, the odds rise that the Fed will begin to taper the rate of asset purchases sometime this fall. as a result, investors are still looking to lower their exposure to the bonds the Fed has been buying, and Friday witnessed yet another bond market selloff (although we believe the magnitude of Friday's selling was exacerbated by thin volume due to the holiday).

Although we see little evidence of the economy taking off, we continue to believe we should see slow improvement into year's end.

Risks Increase With Higher Rates

While markets can withstand a small rise in interest rates without derailing the rally, the risks going forward have risen. we saw on Friday that markets can weather a modest rate increase, as stocks rallied despite the selloff in bonds. and there is further evidence that investors are growing accustomed to somewhat higher rates: Despite the yield on the 10-year treasury note remaining at or above 2.5%, $6 billion flowed into equity funds last week. at some point, however, higher rates will create a more significant headwind for stocks. while there is no magic level, a prolonged and substantial move over 3% in the 10-year Us treasury yield would represent a risk to equities for several reasons. Higher rates would hurt corporate margins, slow the housing recovery and create more of an alternative for yield-hungry investors

Global Risks Escalate

While the first six months of the year were mostly free of market-rattling headlines, the number of global risks that investors should watch closely has risen. with the exception of a brief scare over cyprus banks, the political issues in both europe and the United states have at least temporarily faded. Going into the second half of the year, we see a number of potential issues. two in particular surfaced last week: fatigue with austerity measures in europe and rising tensions throughout the middle east.

The Portuguese government is the latest to show cracks. while Prime minister coelho's government avoided collapse, the country is clearly struggling with divisions regarding its austerity approach. elsewhere, the recent departure of the Democratic left, one of the smaller political parties in Greece, puts the Grecian political coalition at risk. with europe still mired in a recession and its banking system fragmented, we continue to view the region as a major risk factor.

Our other major concern continues to be the middle east. with the recent collapse of the egyptian government, and syria still embroiled in a civil war, there is the potential for more unrest. in addition, political and terrorism risks have already impacted oil production in several countries, including nigeria, iran and iraq. Fortunately, rising Us production has offset these losses, but oil prices are creeping higher and any further disruption in production would likely send them higher still. while a stronger jobs market is helping the Us consumer, higher gasoline prices would represent a painful headwind at a time when many consumers are still getting back on their feet.

While there is no magic level, a prolonged and substantial move over 3% in the 10-year US Treasury yield would represent a risk to equities for several reasons

Preferreds React to Potential Tapering

Background and Market Review

Financial markets have come under pressure following the May 22nd congressional testimony of Federal Reserve Chairman Ben Bernanke, who indicated that further bond purchases associated with quantitative easing could be "tapered" in the next few months, depending on the pace of employment growth. Given the general improvement in recent U.S. economic data, the market began to price in an earlier-than- expected removal of its exceptionally accommodative policy. In response, Treasury yields moved sharply higher—with the benchmark 10-year Treasury rising from 1.7% to 2.2% as of mid-June. This pressured income-related securities, such as higher income equities and most fixed income classes, including preferreds. It also sparked significant swings in currency markets and a general downward pressure on many risk assets.

Absolute yields are still low

The rise in yields may not be as dramatic when absolute levels are considered; Treasury yields were near historic lows at the start of May, pushed down in part by news of Japan's launch of further and substantial unconventional monetary easing policies in April. Notably, inflation concerns did not appear to be a driver of higher rates, as the data remained largely benign and well below historic levels. Nevertheless, investors priced in a new path for the Fed, with futures recently showing a potential first 25-basis-point rate hike by October 2014, bringing this expectation forward from mid-2015 projections one month ago.

Preferred securities held up somewhat better than many fixed income asset classes in May, with their above-average yield spreads to Treasurys and corporate bonds providing a cushion as interest rates rose along the length of the yield curve. Preferreds traded in the institutional over-the-counter (OTC) market outperformed exchange-traded retail preferred issues, reflecting in part the overall shorter-duration (lower interest rate risk) profile of OTC issues.

In the month, the index returns for the BofA Merrill Lynch Fixed Rate Preferred (exchange-traded market), Capital Securities (OTC preferred market) and Corporate Bond Master (investment-grade corporate bonds) indexes were -0.84%, -0.29% and -2.28%, respectively. Another wide-spread market, high yield, also held up better in May, with the BofA Merrill Lynch High Yield Master Index returning -0.54%. Our strategy invests in both exchange-listed and OTC issues, with a preference for the lower-duration fixed-to- float issues that dominate the OTC market. Adjustable-rate preferreds, which are found in both markets, had a modestly positive total return in the month.

Yields stabilized in June, yet volatility intensified

Pressures intensified in early June as equity and other risk markets wobbled—despite Treasury yields stabilizing near 2.1%. Exchange-traded preferred issues came under the most pressure since the Europe breakup scares of 2011, with many lower-coupon issues falling several points in price. Prices of OTC securities, while also lower, again held up somewhat better. Notably, so far in June the higher credit spread markets of high yield and preferreds have both underperformed high grade markets that are more directly correlated with Treasury yields. In a sign of the selling being less related to interest rate risk per se, even the least interest-rate-sensitive issues—floating-rate preferreds—felt the downdraft.

The performance of preferred securities in early June has differed from prior periods of rising Treasury yields seen since the financial crisis of 2008-09. In previous periods, the historically wide yield spreads of preferreds cushioned them against rising Treasury yields. For example, when Treasury yields rose from December 2012 through early March 2013 (from 1.6% to 2.0%, roughly equivalent to May's numbers), the BofA Fixed Rate Preferreds Index had a total return of about 2.0%, and preferreds' yield spreads tightened against Treasury yields. During that period, investors viewed rising rates as a sign of an improving economy, which is typically good for credit. By contrast, in recent trading sessions spreads have been widening on many fixed income securities, including preferreds, but also investment-grade and high-yield corporate debt.

What to Make of This?

The market reaction leaves many questions. For instance, if a stronger economy (good job growth) is needed for Federal Reserve policy "tapering," then why have risk assets performed so poorly? Such markets normally respond favorably to growth. And, specifically, why have credit spreads not tightened in response to growth? If market fears circle around interest-rate risk alone, then why would even floating rate preferreds come under pressure?

We believe the world is adjusting not simply to rising Treasury yields, which are typically accompanied by growth, but also to expectations for less accommodative Fed policy following several years of exceptional accommodation. Monetary policy has greatly supported financial markets by ushering in cheap and abundant liquidity. Now the Fed has signaled that markets must prepare to wean themselves of this support. This raises the level of market uncertainty, hence the credit-spread widening and pressures on risk assets, like stocks. As part and parcel of the changes associated with less accommodative policy, leveraged investors tend to unwind investment positions, which can be a bumpy process.

Investors sold fixed income in a self-fulfilling prophecy

A direct consequence of investor expectations for a change in the Fed cycle has been a material change in preference for financial investments. In recent weeks there have been heavy sales of fixed income assets following several years of strong investor preference for such assets. This is evident in fund flow data, which show very sizable outflows from fixed income funds and ETFs in recent weeks. In this way, investor fears fulfilled their own prophecy, as selling begat more selling. Another factor to consider: although somewhat similar in magnitude and level to the bond yield backup earlier in the year, this Treasury yield backup happened more quickly, contributing to the somewhat disorderly state of markets. As well, liquidity has been generally poor as the summer has approached and because market makers have committed less capital with the onset of new regulations stemming from the financial crisis.

Outlook

The Fed has clearly rattled markets by showing a greater-than-expected inclination to remove some of its highly accommodative monetary policy. This has resulted in a quick downdraft in fixed income markets, including the preferred securities market.

An attractive entry point?

This downdraft has been somewhat rational, as prospects for lower Fed accommodation increase uncertainty. However, we believe the extent of repricing of many preferreds has led to a value entry point. With yield spreads already well wide of historical levels before the selloff and even wider now, we believe many securities look quite compelling, even if we assume that Treasury yields will rise further. Today, all-in yields on many quality investment grade issues are in the 6 to 7 percent area, offering spreads of 400 basis points or more relative to 10-year Treasurys. Historically, such issues have offered spreads of 300 basis points or less. Also, looking just at the exchange-traded preferred index, the weighted-average premium as of this publication is over 5 points lower than it was on May 1st (102.0 versus 107.6), and that market is now rife with discount issues.

Our outlook on yields

We expect Treasury yields to rise over time, but to levels that would not threaten many of the current values. We expect the 10-year Treasury to hover in the mid-2% area by year end as U.S. growth continues to improve modestly; and 3% is a possibility in 2014. However, we believe it is unlikely to be much higher given declining inflation globally as well as moderating economic growth in Asia and a very tepid outlook for European economies. In our view, growth in the U.S. could be a bit stronger, but GDP is unlikely to be strong enough to elicit materially higher rates that could affect the 6%–7% yields currently offered by many preferreds.

An important caveat is that our investment thesis depends on normal credit spread tightening, which had been occurring since the financial crisis, but which was clearly lacking in early June. We see scope for more periods of dislocation along the way similar to this one. However, we believe the high income rates, together with the quality and improving fundamentals prevalent in the financials-heavy preferred market will show through over time as bank metrics continue to reflect much higher levels of capital and lower risk taking than in the past. We expect ratings agency upgrades to follow from this over time, and spreads to tighten again.

A prudent, active approach

While we see value, we are approaching investing cautiously. As mentioned, we expect to see more short-term dislocations over time. We continue to position the portfolio to protect against a further increase in bond yields. As in prior months, we view this as the best risk-adjusted course of action, whether yields rise or not. We are employing various tools to manage this risk, including buying securities that have wide credit spreads, and we are favoring high-coupon, fixed-to-float and floating rate structures over lower-coupon securities. We may also take other hedging measures.

A total-return perspective

As a final note, investors should consider the total-return protection that the high income rate of preferreds affords over time. With income generally over 6% today, price swings have a more muted effect on total returns for term holders. The Fed's removal of its highly accommodative monetary policy will affect many markets, but few offer the stabilization effect of income that is this high and regular.

For a more complete discussion of how interest rates can affect preferred securities, please visit the Cohen & Steers website at cohenandsteers.com. In particular, our recent Viewpoint, *"When Interest Rates Rise: Opportunities and Risk Management Strategies in Today's Preferreds Market,"* provides in-depth historical perspective and insights from our investment team.

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Topic: Alternative Strategies using ETPs
Date: Tuesday, July 23rd, 2013
Time: 11 AM EST
Speaker: Michael Akins, *Portfolio Manager* - ALPS ETF Trust

Topic: TBD
Date: Tuesday, August 6th, 2013
Time: 11 AM EST
Speaker: ETF Securities

Topic: TBD
Date: Tuesday, August 20th, 2013
Time: 11 AM EST
Speaker: Cohen & Steers

Dear Readers,

We are pleased to launch the second issue of our CEF & ETF Newsletter, which aims to provide a review of developments in the CEF & ETF space as well as commentaries and editorial from leading industry participants. We hope you will find it helpful and useful.

Due to the huge success of our CEF & ETF webinars, we will continue to host these webinars twice a month.

Please check out our newly revamped Closed-End Funds internet portals (www.cef.capitallink.com), dedicated to providing free news and data as well as the latest in fund commentary and analysis on CEFs.

Thanking for your interest and support,

Sincerely,
Nicolas Bornozis
President

SAVE THE DATE:

CAPITAL LINK'S
13th Annual
Closed-End Funds &
Global ETFs Forum
Thursday, April 24, 2014
New York City

13th ANNUAL CAPITAL LINK CLOSED-END FUNDS & GLOBAL ETFs FORUM
Thursday, April 24th, 2014
Metropolitan Club, New York City

For participation opportunities, contact Nicolas Bornozis at funds@capitallink.com

Transcript: Closed-End Funds Analyst Roundtable

Thursday, June 13, 2013 | 11:00 AM ET

Robert F Bush, Jr - Great, thank you Nicolas, thank you very much, and again on behalf of the panel, you know, putting something like this together to help disseminate information to the users and shareholders and advisors on the street with respect to closed-end funds, I think anything that we can do to get information out there on a product is helpful for all those involved and again I think the panel who is a very solid representation of the folks that cover this business so I'm very interested to hear what comes from this.

Just as sort of a backdrop, those of us who are involved in the closed-end fund business and [unclear] the closed-end fund business, clearly the last year or two have been very dynamic in the business. this year-to-date we raised on IPO assets over $11 billion in new money and that's a run rate to approximate really what the record was back in 2007 which broke 26 billion so that's quite a demand for this in the primary and that's shown by how the secondary market has reacted. You've seen quite a bit of tightening of discounts across the board. That's widened a little bit over late and we're going to get into that in a bit, but again the backdrop has been primarily in last year so you've had quite a bit of issuance with respect to credit, high yield, bond funds, that's approximately about 60% of the issuance balanced by preferreds about 17%, and then basically the only equity new issuance we've seen has been relative to the energy infrastructure and [NLP] markets, so I think that hopefully serves as a backdrop as to where we are and perhaps where we're going.

I think this is, as I mentioned earlier before the call, this is a great time to talk about volatility because we've seen it in the market and the closed-end fund market has reacted to that as of late and so I will pass the first question over to Dave Perlman at Morgan Stanley. Given the recent volatility, Dave, in current valuations in the market, how do closed-end funds compare to their historical averages?

David Perlman - Thank you Bob and thank you Nicolas for having me and for organising this webinar. The demand for income and the strong performance on an absolute and relative basis, but the full valuations for many parts of the closed-end fund market especially within the fixed income universe, over the past year both taxable fixed income and municipal closed-end fund average valuations reached 10 year highs, trading at up to over 3% premiums to net asset values.

Two areas that were in high demand within the taxable closed-end market were funds focusing on floating rate loans and high yield bonds. Both of these areas came close to their 10 year highs over the past year with loans trading to over a 5% premium on average and high yield funds trading up to a 9% premium. However with the current rise in interest rates and the supply/demand balance has shifted as market prices have sharply underperformed net asset values. The average valuation on taxable fixed income closed-end fund is now 4.4% discount which is wider than its 10 year average discount at 3%. We note that the widening in valuations has been widespread, even impacting shorter duration and floating rate funds which should be less impacted by rising rates. The average valuation on municipal closed-end funds is now at 5.2% discount which is also cheaper this 10 year average discount of 2.7%. In our opinion, our cheaper valuations are a reflection of the higher interest rate volatility and concern over the impact on the Fed begins to slow the pace of its asset purchases and ultimately ends its unconventional monetary policy. Equity closed-end funds did not experience the same level of demand and valuation extremes that we witnessed with

Participants

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the fixed income closed-end funds. In fact the current valuations on equity closed-end funds is 5.4% discount and that's consistent with its longer-term average. However, if you look within the equity universe there is a wide range of valuations, traditional and non-income focused equity funds generally trade at wider discounts, [covered core] funds, despite their attractive distribution levels, are also trading at wider discounts for this space and we believe that the cheaper valuations are a result of sizeable dividend reductions since the financial crises. Many of the funds tried to maintain high distribution pay-outs despite lower asset levels and declining volatility. On the opposite end of the spectrum NLP closed-end funds have traded at sizeable premiums over the past five years. Part of this attributed to the impact of their [unclear] structure, but these funds have also been in high demand for the attractive distribution rates and potential for dividend growth and higher total returns. We did see valuations on the NLP funds cheapen with the recent increase in rates.

I know I mentioned a lot of numbers so just to summarise. Both taxable fixed income and municipal closed-end funds are now trading cheaper than the longer-term averages. [Equity] closed-end funds are trading in line. The potential for higher interest rate volatility going forward will likely result in more volatility in closed-end fund valuations, which can present opportunities for more tactical investors.

I'll pass it back to you Bob.

Robert F Bush, Jr - Great, is there anything anybody wants to add on that? I mean one thing I might throw out, Dave, if you don't mind, just as a thought, I mean in the high yield space particularly and many of the funds that have come out over the course of the year and a half have been, oh, hybrids, they have had high yield in them, [unclear] credit, maybe some floating rate in there as well, to the tune of maybe certainly over $10 billion in new issuance [unclear] over the course of the last 18 months. Do you see the amount of supply having an impact? We talked sort of about the macroeconomic effects but do you see the amount of supply coming into the closed-end fund space to address those particular asset classes having an impact on valuations?

David Perlman - Generally [with the universe] trading at premiums, it's pretty easy to bring out new funds in the offering and [unclear] had them in, so I think that definitely can have an impact on the weakness we've see, you know, many of the new funds that hadn't yet built up the track record performance or there's more limited information available, and some of those funds have been hit pretty hard, so I think just the number of options of in the space now where investors can [occupy], they definitely could have an impact on the wider discounts that we…or the discount widening that we did see.

Robert F Bush, Jr - Sure, well, that's a natural reaction absolutely. I will turn the next question over to Dan Brown at Wells Fargo. Dan, given what we've experienced with respect to the closed-end fund market activity of late, what lessons can be learned from that, what are your thoughts on that?

Dan Brown - There are a couple of lessons that we can think of really just right from the start about the recent market activity especially on the fixed income side like Dave said. I mean on the fixed income side we're seeing valuations at levels in general that we haven't seen since back in 2011, so a couple of the important lessons that I and our team can think of here, is that first and foremost investors, clients, advisors should keep in mind that this really isn't anything unique. I mean we have seen issues like this within the closed-end fund market definitely over the past two years and even further back where we will be in fairly stable trending environment at least with evaluations and then something occurs and then the volatility in the market price will pick up, especially relative to the NAV and then we see these kind of drastic movements in evaluations, so for example another event that we've actually seen recently was back in March with the municipal bond closed-end funds where we saw the traditional seasonal patterns with the underlying market, which when we start getting to the tax season when people are selling out of their municipal bond, individual municipal bonds to cover some of those potential required tax payments. We saw that downtrend in the underlying market in the NAVs, which moved in line, however we saw even more drastic decline in the market prices, but the market prices of the closed-end funds causing significant tightening of the premiums, widening of the discounts so again this isn't really anything unique and honestly we would expect, like Dave said, in the near term is we're dealing with potential increases in interest rates, still seeing volatility in the valuations especially in the fixed income side, but definitely going forward in the future seeing issues like this and where there are short-term quick swings in the valuation. First and foremost again this really isn't a unique event we would say.

Now second I would say this is also just another reminder of the general liquidity of closed-end funds, I guess you could say the illiquidity in general, because when you look at kind of the average volume from a…we typically look at the three-month average trailing volume, the majority are pretty much…on average they're as…they have the same liquidity profile as micro capped stocks. I mean we see some funds that have some decent amount of liquidity or where you have 10 million, 11/12 million in average daily volume, however

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Transcript: ETFs Outlook & Minimum Volatility

Tuesday, July 2, 2013 | 11:00 AM ET

Raman Subramanian: Thank you Nicolas, and good morning to all of you. As Nicolas said, the topic for today is Volatility, Minimum Volatility, and people can manage it and utilise different kind of products and tools which are available in the market, to mitigate the risk which arises from the equity market volatility. So I will refer to the presentation called MSCI Minimum Volatility Indices Track Broad Market Returns with Lower Risk. The way…if you go to the first slide of this deck, the outline of today's presentation that I'm going to follow has three main components. The first component is that I will, before I go into the methodology and construction of MSCI Minimum Volatility Indices, I will spend some time explaining the research background on what is low volatility effect.

After that, I will spend a few minutes explaining how MSCI construct its minimum volatility indices in a rules-based and transparent mechanics, to capture this low volatility effect. And finally, I will summarise some of the key benefits that we have put in place within the construction methodology, and that investors can look and see, by using MSCI Minimum Volatility Indices. So if you look at…refer to the third slide of this presentation, what is low volatility or minimum volatility effect? Now, if you look at the financial theory; you know, we are all finance professionals, we have been taught in the Finance 101 classes that if you are looking to capture a higher return, then potentially you are looking for stock or asset classes which are a little bit more riskier compared to stocks and asset classes which are less riskier.

So if you take higher risk, potentially, you will be rewarded for that by taking…getting a higher return. But in reality, what has been observed in the marketplace is that stocks or asset classes, or mostly equity markets, stocks which have been less volatile have outperformed the stocks which are more riskier, so that the price volatility is higher in the long term, on a risk adjusted basis. Now, clearly, this is an anomaly, because, you know, if finance taught us that you take more risk and you get more rewarded, but in reality, what we see is that you have…if you have created a portfolio of stocks which are less riskier, and it has outperformed compared to stocks which are more riskier, then clearly, this is an anomaly.

Now, immediately, the questions comes, is that, why this is happening, and whether the classical theory, which previously we have listened to, like the value and growth and small cap, but if that is the effect which is explaining this anomaly or performance of the stocks which are less volatile outperforming the stocks which are more volatile. So what the academic researchers have done is that they have negated the effect of all other different factors, like the value growth, and the resulting tiled portfolio, which is just on the lower volatility, after negating all this effect, still retains the characteristic of outperforming, related to the stocks which are more, you know, more volatile. Now, the explanation given to that, you know, by the academic professionals is that, in reality, when people are investing, sometimes they build in this irrational behaviour, or behaviour (unclear).

So they are tending to bias their decision towards stocks which have a potential…upswing potential, but you know, they also realise that sometimes, even on the stock which is more volatile, can go upside and downside, so you know, they can also have a negative return on the downside. So since they're biasing towards stocks which are more volatile, they are neglecting the stocks which are less volatile, and that, itself, creates a potential premier, and that results in the outperformance in the long run. The immediate question then comes is that, okay, we have seen that happening in the long run; how do you actually capture that in a portfolio or index sense?

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\So if you go to slide four of this deck, where we talk about MSCI Minimum Volatility Index Methodology, what we have done is that in construction of the methodology, there are two main features. One is, you still want to retain the broad, underlying features of the equity market, because you don't want to lose out the benefit of staying within the equity market, and get the broad market exposure. And then second thing which we want to do is that we want to tilt your portfolio towards stocks which are less volatile, and negate any of the other effects that I talked about, like, you know, which can come because if you are not creating those…you want to control the unintended biases which can come in the construction process.

So if you look at the picture on the top right, the way this is done is that we start with MSCI Parent Index, and these are quite familiar to all of you, like the MSCI All Country World Index, which is a…which combines both developed and emerging markets, MSCI Emerging Market Index, which is…which shows the performance of the MSCI emerging market universe, then you have the MSCI USA Index, which gives a broad exposure to the US equity market. That is our starting reference point. Then what we do is that we apply a process of constraining on sectors and countries and styles, (unclear) to negate any of the biases which can come in the index construction process. And finally, we tilt that portfolio towards lower volatility or minimum volatility stocks.

So it's a very transparent process. Start with the universe of any index that you want to start with, constrain them on that biases that can come if you don't control the construction process. Once you have put the constraint, you tilt your portfolio towards minimum volatility stocks. And the resulting index is [called] as Minimum Volatility Index. And the question is that, okay. The index was constructed, and we saw that the objective here was to tilt towards stocks which are less volatile, and maintaining the broadest exposure to the equity market. And if that is done, whether the performance characteristic of that, how it looks like, and more importantly, how is the risk of that stock, the resulting index will look like?

So let's see those things in the subsequent slides. So if we look at slide five, the MSCI Minimum Volatility Indices were launched in 2008. Right before that, the whole financial sub-prime crisis that was observed in the marketplace. So we, technically, have an index which was live during the market crisis that was, you know, one of the biggest crisis that we have seen in the recent decade. And we can clearly see that if the index had characteristic which prevented…provided a downside protection, during even that financial crisis, then it reflected the objective that we intended to carry forward, so that means to protect us from the excess volatility in the marketplace.

So let's see what happened, and look at the performance of the…from the risk perspective, so on slide six; so here we are showing a little bit more longer period of the risk reduction, so on slide six, if we look, there are two charts here. The top chart shows the ratio of the volatility of the MSCI Minimum Volatility Index, to that of the MSCI World Index. So the World Index, as you know, is the developed market index. So this ratio showed that across time, the MSCI Minimum Volatility Index has always had a lower volatility compared to the parent index. So the bottom chart is much more clearer, so if you look at, on average, MSCI World Index had a volatility which is ranging between about 15%, or on downside, we have close to about 11 to 12%, during the market crisis in 2008, 2009, it spikes up to close to 25%, and much more recently, we are seeing that it's close to around 20% or so.

And this is a rolling 36 month volatility, with a standard deviation of the returns, so it is simply the…you take the standard deviation and calculate the 36 month volatility. Now, if you look at the blue line, which is the one below the green line, which is for the MSCI World, you clearly see that the volatility of that is always lower than that of the MSCI World Index. And more importantly, when the whole financial crisis was happening, you can see that the index volatility, the spread was even wider. So whenever the markets have been turbulent, the MSCI Minimum Volatility Index has provided a lower volatility and a better downside protection, compared to the broader market exposure itself.

The next questions comes is, okay, if that is the case, what is the performance characteristic of this; vendors index will outperform…vendors index will underperform compared to the broader market index. So let's refer to slide number seven, and here we show a…the performance characteristic, and for reasoning that since this is a live index from 08, and we want to avoid any kind of a back-calculated, we just tried to show here, we are keeping with the results, what is seen in the live index performance, when the index was actually live in the market. So clearly, you can see that, if you look at the related performance shot, which is, the line goes up, the MSCI Minimum Volatility Index outperformed compared to the MSCI World Index, and then the line goes down, the index underperformed on a related basis.

So clearly, whenever there was a…the market crisis, whether it's a sub-prime crisis or a Eurozone crisis, you see that minimum volatility index outperform compared to the MSCI broader index. And in normal markets, if you see from 08 to April of 2009, to maybe, like, end of 2010, you can see that the

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