# Capital Link's
# CEF & ETF Monthly Newsletter

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# The Month in Closed-End Funds: June 2017

## PERFORMANCE

For the eighth consecutive month equity CEFs on average witnessed a plus-side return on a NAV basis and—for the seventh month in a row—on a market basis (+0.84% and +0.70%, respectively). However, for the first month in seven their fixed income CEF counterparts, declining just 0.01%, were in the red on a NAV basis, but for the third consecutive month they posted a plus-side return on a market basis, returning 0.24%. Most of the U.S. broad-based indices managed to finish the month on the plus-side, despite a mini meltdown in large technology issues. The Russell 2000 Price Only Index posted the strongest return (+0.80%), and the NASDAQ Composite Price Only Index posted the only negative return (-0.49%).

Equity mutual funds witnessed a slight increase in volatility in June on a lower-than-expected May nonfarm-payrolls report, a reported glut in crude-oil stockpiles, and uncertainty ahead of the Federal Reserve Board's policy-setting meeting. But, equity funds—despite a rough patch in big tech issues in mid-June—managed to stay in the black.

After pushing the market indices to new highs at the beginning of June, investors began to take a wait-and-see approach ahead of what many in the mainstream media were calling "Super Thursday," when ex-FBI director James Comey was scheduled to testify before Congress, the European Central Bank was to hold its policy meeting, and the U.K. general elections were scheduled. The Labor Department reported that the U.S. had created 138,000 new jobs for May (coming in below analyst expectations of 182,000), but the unemployment rate still ticked down to 4.3%. Notwithstanding the lower-than-expected jobs creation, most pundits still believed the Fed would raise its short-term interest rate on June 14.

In the following week the NASDAQ Composite Price Only Index notched another record close. Investors appeared to breath a collective sigh of relief after Comey's testimony to the Senate Intelligence Committee produced no new surprises in the ongoing investigation into Russian meddling in the U.S. presidential election and as the European Central Bank kept its monetary policy unchanged. Nonetheless, later in the week a mini meltdown in tech stocks and an unexpected outcome in Britain's snap parliamentary election kept many investors on edge.

Technology issues continued their slide, but small-cap and financial issues appeared to fill the void. As was expected, the Fed raised its key lending rate 25 bps to between 1.00% and 1.25% and announced that it would start reducing its $4.5-trillion balance sheet this year; however, it was vague on details. Further dampening market sentiment, American Petroleum Institute data showed an increase in U.S. oil and gasoline stockpiles, pressuring near-month crude oil prices.

Later in the month investors scooped up battered energy and technology stocks after the Commerce Department reported new-home sales ran at a 610,000 seasonally adjusted annual rate, surpassing analyst forecasts. However, investors remained cautious at month-end, despite learning of the increase in May consumer spending and the better-than-expected Chicago PMI and June consumer sentiment reports.

**The Month in Closed-End Funds: June 2017**

- For the eighth month in a row equity closed-end funds (CEFs) witnessed a plus-side return on average, rising 0.84% on a net-asset-value (NAV) basis for June, while for the first month in seven their fixed income CEF cohorts posted a return in the red, declining however only 0.01%.
- For June 22% of all CEFs traded at a premium to their NAV, with 20% of equity CEFs and 23% of fixed income CEFs trading in premium territory. Thomson Reuters Lipper's municipal debt CEFs macro-group witnessed the largest narrowing of discounts for the month—49 basis points (bps) to 4.20%.
- Utility CEFs (-1.35%) and Natural Resources CEFs (-1.01%) posted the lowest returns in the equity universe and weighed on the domestic equity CEFs macro-group (+0.67%).
- Despite the meltdown in big tech stocks, investors focused on growth opportunities during the month, pushing Growth CEFs to the top of the charts (+8.08%) for the third month in four.
- For the first month in seven none of Lipper's municipal debt CEF classifications posted returns in the black; High Yield Municipal Debt CEFs (-0.01%) mitigated losses better than the other classifications in the group.

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THOMSON REUTERS

For the month of June Treasury yields rose at all maturities of the curve—except the one-month and thirty-year, which declined by 2 bps and 3 bps, respectively—as investors responded to the mid-month rate hike. Treasury yields of less than two years witnessed increases for the month ranging between 1 bp and 7 bps, while longer-dated yields rose, with the five-year yield rising the most—14 bps to 1.89%.

For June the dollar weakened against the euro (-1.63%) and the pound (-0.53%) but gained against the yen (+2.57%). Commodities prices declined for the month, with near-month gold prices declining 2.46% to close June at $1,240.70/ounce and with front-month crude oil prices falling 4.72% to close the month at $46.04/barrel.

For the month 53% of all CEFs posted NAV-based returns in the black, with 73% of equity CEFs and only 37% of fixed income CEFs chalking up returns in the plus column. For the first month in four Lipper's mixed-asset CEFs macro-group (+1.10%) outpaced its two equity-based brethren: world equity CEFs (+1.06%) and domestic equity CEFs (+0.67%).

As a result of the strong preference for out-of-favor growth and healthcare issues, the Growth CEFs classification (+8.08%) jumped to the top of the equity charts for the third month in four. It was followed by Sector Equity CEFs (+2.50%) and Emerging Markets CEFs (+1.93%). Domestic equity CEFs (+0.67%) were dragged down by Utility CEFs (-1.35%), Natural Resources CEFs (-1.01%), and Energy MLP CEFs (-0.78%) as oil prices and energy stocks were hurt by data showing an increase in U.S. oil and gasoline stockpiles. For the remaining equity classifications returns ranged from 0.15% (Developed Markets CEFs) to 1.46% (Real Estate CEFs).

Three of the five top-performing individual equity CEFs were housed in Lipper's domestic equity CEFs macro-group. At the top of the charts was **Engex, Inc. (EXGI,** housed in the Growth CEFs classification), rising 14.06% on a NAV basis. (The fund did not trade on June 30, so neither a discount nor a premium was recorded). EXGI was followed by **Morgan Stanley China A Share Fund, Inc. (CAF,** warehoused in the Emerging Markets CEFs classification), gaining 6.85% and traded at a 13.23% discount at month-end; **Tekla Life Sciences Investors (HQL,** housed in the Sector Equity CEFs classification), rising 6.61% and traded at a 0.24% premium on June 30; **Tekla Healthcare Opportunities Fund (THQ),** gaining 6.47% and traded at a 7.75% discount at month-end; and **Gabelli Convertible & Income Securities Fund, Inc. (GCV,** housed in Lipper's Convertible Securities CEFs classification), posting a 6.27% return and traded at a 6.01% discount on June 30.

# CLOSED-END FUNDS LAB

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

| | NAV RETURNS POSITIVE | PREMIUM/DISCOUNT BETTER | PREMIUM/DISCOUNT WORSE | NOW TRADING AT PREMIUM | NOW TRADING AT DISCOUNT |
|---|---|---|---|---|---|
| Equity Funds | 73 | 53 | 42 | 20 | 78 |
| Bond Funds | 37 | 59 | 35 | 23 | 76 |
| **ALL CEFs** | **53** | **56** | **38** | **22** | **77** |

**TABLE 2** AVERAGE NAV RETURNS, SELECTED PERIODS (%)

| | JUNE | YTD | 3-MONTH | CALENDAR-2016 |
|---|---|---|---|---|
| Equity Funds | 0.84 | 8.06 | 2.12 | 11.72 |
| Bond Funds | -0.01 | 5.06 | 2.38 | 6.66 |
| **ALL CEFs** | **0.36** | **6.37** | **2.27** | **8.90** |

**TABLE 3** NUMBER OF IPOs, SELECTED 12-MONTH PERIODS

| | JUNE 2017 | CALENDAR-2016 |
|---|---|---|
| **ALL CEFs** | **25** | **18** |

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

| | |
|---|---|
| 3 MONTHS THROUGH 5/31/2017 | 251 |
| COMPARABLE YEAR-EARLIER 3 MONTHS | 241 |
| CALENDAR 2016 AVERAGE | 348 |

**Source:** Thomson Reuters Lipper

For the month the dispersion of performance in individual equity CEFs—ranging from minus 5.50% to positive 14.06%—was wider than May's spread and more skewed to the plus side. The 20 top-performing equity CEFs posted returns at or above 3.31%, while the 20 lagging equity CEFs were at or below minus 1.35%.

For the month 70 CEFs in the equity universe posted negative returns. Three of the five worst performing funds were housed in either the Natural Resources CEFs or Sector Equity CEFs classifications, with **Tortoise Energy Independence Fund, Inc. (NDP,** housed in the Natural Resources CEFs classification) at the bottom of the pile, shedding 5.50% of its May-closing NAV price and traded at a 3.34% premium on June 30. **Columbia Seligman Premium Technology Growth, Inc. (STK,** housed in the Options Arbitrage/Options Strategies CEFs classification) posted the next poorest return in the equity universe, declining 4.43%. STK traded at a 7.39% premium at month-end.

As a result of the lower-than-expected nonfarm-payrolls report and some soft economic data, the ten-year Treasury yield bounced from 2.21% at May month-end to an intra-month closing low of 2.14% on June 6 and June 26. It rose again after investors learned that the ECB would soon be less accommodative in its monetary policy and closed the month at 2.31% as the hawkish tone was echoed by Canadian and U.K. central bankers. For the seventh month in a row domestic taxable bond CEFs (+0.15%) posted a plus-side return on average. They were bettered by world income CEFs (+0.63%), which benefitted from strong performance from Global Income CEFs (+0.95%), while Emerging Markets Debt CEFs (-0.03%) weighed on the subgroup. However, for the first month in seven municipal bond CEFs (-0.23%) posted a return in the red on average.

Investors continued their search for yield, bidding up developed-markets issues after hearing encouraging election results from France and on improving micro-and macro-economic conditions. The domestic fixed income CEFs macro-group was dragged down by Loan Participation CEFs (-0.12%) and High Yield CEFs (Leveraged) (-0.08%). At the top of the domestic taxable bond CEFs universe were General Bond CEFs (+0.53%), U.S Mortgage CEFs (+0.47%), and Corporate Debt BBBRated CEFs (+0.32%).

Breaking a six-month winning streak in which all Lipper municipal debt CEF classifications posted returns in the black, none of the municipal debt CEF classifications posted plus-side returns for June. High Yield Municipal Debt CEFs (-0.01%) and California Municipal Debt CEFs (-0.21%) mitigated losses better than the other classifications in the group, while General & Insured Municipal Debt CEFs (Unleveraged) (-0.32%) was the group laggard. National municipal debt CEFs (-0.22%) mitigated losses slightly better than their single-state municipal debt CEF counterparts (-0.25%).

The three top-performing individual CEFs in the fixed income universe were housed in Lipper's Global Income CEFs classification. At the top of the charts were **PIMCO Dynamic Income Fund (PDI),** returning 2.90% and traded at a 6.57% premium on June 30; **PIMCO Income Opportunity Fund (PKO),** returning 2.23% and traded at a 6.67% premium at month-end; and **PIMCO Dynamic Credit and Mortgage Income Fund (PCI),** posting a 2.16% return and traded at a 2.36% discount on June 30. Following those three were **Nuveen Build America Bond Opportunity Fund (NBD,** warehoused in the General Bond CEFs classification), tacking 2.13% onto its May month-end value and traded at a 5.49% discount on June 30, and **Western Asset Mortgage Defined Opportunity Fund Inc. (DMO,** warehoused in Lipper's U.S. Mortgage CEFs classification), returning 1.75% and traded at a 22.18% premium at month-end.

For the remaining funds in the fixed income CEFs universe monthly NAV-basis performance ranged from minus 1.49% for **Avenue Income Credit Strategies Fund (ACP,** housed in Lipper's High Yield CEFs [Leveraged] classification and traded at an 8.37% discount on June 30), to 1.53% for **BlackRock Taxable Municipal Bond Trust (BBN,** housed in Lipper's General Bond CEFs classification and traded at a 1.76% discount at month-end). The 20 top-performing fixed income CEFs posted returns at or above 0.83%, while the 20 lagging CEFs were at or below minus 0.55%. A total of 203 fixed income CEFs witnessed negative NAV-based performance for June.

### PREMIUM AND DISCOUNT BEHAVIOR

For June the median discount of all CEFs narrowed just 9 bps to 5.27%—better than the 12-month moving average discount (6.10%). Equity CEFs' median discount narrowed 7 bps to 6.29%, while fixed income CEFs' median discount narrowed 10 bps to 4.73%. Municipal debt CEFs' median discount witnessed the largest narrowing of discounts in the CEFs universe, 49 bps to 4.20%, while the high yield bond CEFs macro-group witnessed the largest widening of discounts—59 bps to 6.99%.

For the month 56% of all funds' discounts or premiums improved, while 38% worsened. In particular, 53% of equity funds and 59% of fixed income funds saw their individual discounts narrow, premiums widen, or premiums replace discounts. The number of funds traded at premiums on June 30 (114) was identical to the number on May 31.

## CEF EVENTS AND CORPORATE ACTIONS

### IPOs

Medley Management Inc., an alternative asset management firm, announced that **Sierra Total Return Fund (NASDAQ:SRNTX)** is now available to individual investors through Class T shares. The fund seeks to provide total return through a combination of current income and long-term capital appreciation by investing in a portfolio of debt securities and fixed income-related equity securities. The fund expects to achieve these investment objectives through a disciplined and balanced allocation among four distinct asset strategies, including public and private credit, public investment opportunities, private investment opportunities, and pooled credit.

The fund is a non-diversified, closed-end investment management company that is operated as an interval fund that continuously offers its shares on a daily basis. The fund requires a minimum initial investment of $2,500. To provide liquidity to shareholders the fund intends to make quarterly offers to repurchase its outstanding shares at NAV.

### RIGHTS, REPURCHASES, TENDER OFFERS

**First Trust/Aberdeen Global Opportunity Income Fund (FAM)** announced the final results of the tender offer it conducted. The fund conducted a tender offer for up to 25% of its outstanding common shares for cash at a price per share equal to 98% of the NAV per share determined on the expiration date. The fund's tender offer, which expired on June 23, 2017, was oversubscribed. Because the number of shares tendered exceeded the number of shares the fund offered to purchase, the fund will purchase 25% of its outstanding common shares on a pro-rata basis in accordance with the number of shares duly tendered by each shareholder and the terms of the offer to purchase. Based on final results, a total of 8,693,400 shares were tendered.

**Virtus Global Dividend & Income Fund Inc. (ZTR)** announced that, in accordance with its tender offer for up to 5% of its issued and outstanding common shares (which expired on June 23, 2017), the fund accepted 1,283,635.68 shares, representing 5% of its outstanding shares, for payment on or about June 30, 2017. A total of 1,563,521.82 shares were properly tendered and not withdrawn by June 23, 2017, the final date for withdrawals. Therefore, on a pro-rated basis approximately 82.108% of the shares so tendered by each tendering shareholder were accepted for payment. The purchase price of properly tendered shares was 98% of the NAV per share determined as of the close of the regular trading session of the New York Stock Exchange (NYSE) on June 23, 2017, which was equal to $12.6714 per share.

**The Virtus Total Return Fund Inc. (ZF)** announced that in accordance with its tender offer for up to 5% of its issued and outstanding common shares, which expired on June 23, 2017, the fund accepted 1,133,020.45 shares, representing 5% of its outstanding shares, for payment on or about June 30, 2017. A total of 6,104,415.82 shares were properly tendered and not withdrawn by June 23, 2017, the final date for withdrawals. Therefore, on a pro-rated basis approximately 18.568% of the shares so tendered by each tendering shareholder were accepted for payment. The purchase price of properly tendered shares was 98% of the NAV per share determined as of the close of the regular trading session of the NYSE on June 23, 2017, which was equal to $13.1908 per share.

**Advent/Claymore Enhanced Growth & Income Fund (LCM)** announced that the tender offer to purchase for cash up to 32.5% of the fund's outstanding common shares of beneficial interest at a price per share equal to 98% of the fund's NAV as of the business day immediately following the expiration of the tender offer would commence on June 12, 2017 and expire, unless otherwise extended, on July 11, 2017.

**The Taiwan Fund, Inc. (TWN)** announced that on June 12, 19, 26, and 29, 2017, the fund repurchased 998, 1,025, 731, and 900 shares, respectively, under the fund's discount management policy.

**First Trust High Income Long/Short Fund (NYSE:FSD)** commenced a tender offer. The fund will purchase up to 15% of its outstanding common shares for cash at a price per share equal to 98% of the NAV per share as determined as of the close of the regular trading session of the NYSE on July 14, 2017, or if the offer is extended, as determined by the close of the regular trading session of the NYSE on the next trading day after the day to which the offer is extended. The tender offer will expire on July 13, 2017, or on such later date to which the offer is extended.

**Reaves Utility Income Fund (UTG)** announced that it filed a preliminary registration statement with the Securities and Exchange Commission (SEC) relating to the offering of additional common shares of the fund pursuant to a rights offering. The fund is issuing transferable subscription rights to its common shareholders on a record date to be set by the fund's board of trustees, and such shareholders will be allowed to subscribe for new common shares of the fund. Record-date shareholders will receive one right for each common share held on the record date. For every three rights held a holder of rights may buy one new common share of the fund. Record-date shareholders who fully exercise all rights initially issued to them in the primary subscription will be entitled to buy those common shares that are not purchased by other record-date shareholders. In addition, the fund in its sole discretion may elect to issue additional common shares in an amount of up to 25% of the common shares issued in the primary subscription.

**Neuberger Berman Real Estate Securities Income Fund Inc. (NRO)** announced the second measurement period under its tender offer program that was previously announced in July 2016 in connection with other discount mitigation measures. Under the tender offer program the fund will conduct two separate 12-week measurement periods during 2017. If the fund's common shares trade at an average daily discount to NAV per share of greater than 10% during a 12-week measurement period, the fund will conduct a tender offer for at least 8% of its outstanding common shares at a price equal to 98% of the fund's NAV determined on the day the tender offer expires. The fund's board of directors determined that the second of the two measurement periods under the tender offer program will commence on Monday, July 10, 2017, and end on Monday, October 2, 2017.

### MERGERS AND REORGANIZATIONS

**JPMorgan China Region Fund, Inc. (JFC)** confirmed that its entire investment portfolio was liquidated and the fund's assets are now fully in cash. The fund also sought to transfer these assets into U.S. dollars where possible.

Nuveen successfully completed the merger of **Nuveen Flexible Investment Income Fund (JPW) into Nuveen Preferred Income Opportunities Fund (JPC)** prior to the open of the NYSE on June 12, 2017. In the merger JPC acquired substantially all the assets and liabilities of JPW in a tax-free transaction in exchange for an equal aggregate NAV of newly issued common shares. The exchange took place based upon the funds' closing NAVs on June 9, 2017. The exchange ratio at which common shares of JPW were exchanged for common shares of JPC was 1.73985578.

Federated Investment Management Company, the investment advisor to **Federated Premier Intermediate Municipal Income Fund (FPT)** and **Federated Premier Municipal Income Fund (FMN),** announced that it recommended to the boards of trustees of FPT and FMN and the boards of trustees approved that FPT reorganize into FMN, with FMN being the surviving fund. The reorganization, which requires shareholder approval, was expected to be a tax-free transaction completed during fourth quarter 2017.

Federated Investment Management Company also recommended to the board of trustees of FPT and the board of trustees approved FPT's conducting a tender offer for up to 20% of its outstanding common shares at a price equal to 98% of NAV at the close of trading on the date the tender offer expires. This tender offer would be completed prior to the reorganization of FPT into FMN.

The specific dates for FPT's tender offer will be announced separately, but it was anticipated that the tender offer will commence in July 2017 and end in August 2017. Additional terms and conditions of FPT's tender offer will be set forth in its offering materials, which will be distributed to its common shareholders. Should the number of common shares tendered and not withdrawn exceed 20% of FPT's outstanding common shares, FPT will purchase common shares from tendering common shareholders on a pro rata basis. Accordingly, common shareholders cannot be assured that FPT will purchase all of its tendered common shares. Following the tender offer, if shareholders approve the reorganization, FPT will reorganize into FMN. It was anticipated that if the tender offer is completed by the end of August 2017, the reorganization may be completed by the end of November 2017.

### OTHER

BlackRock Advisors, LLC announced that **BlackRock International Growth & Income Trust (BGY)** will be renamed "BlackRock Enhanced International Dividend Trust" and **BlackRock Global Opportunities Equity Trust (BOE)** will be renamed "BlackRock Enhanced Global Dividend Trust." BGY and BOE will continue to trade on the NYSE under their current ticker symbols. These changes were made in accordance with changes to the funds' nonfundamental investment policies and portfolio management terms previously announced on March 28, 2017.

**The New Ireland Fund, Inc. (IRL)** announced a change to its managed distribution policy. Under the revised distribution policy the fund pays quarterly distributions at an annual rate (set once a year) that is a percentage of the fund's NAV on May 31. The board determined that the annual rate will be 8% per annum, payable in quarterly installments. The revision was made by the board in connection with the smaller asset size of the fund resulting from the fund's recent tender offer. The distribution policy seeks to provide investors a stable quarterly distribution from current income, supplemented by realized capital gains and—to the extent necessary—paid-in capital.

The board of directors of **Credit Suisse Asset Management Income Fund, Inc. (CIK)** approved the fund's entry into a credit facility that will allow the fund to borrow up to one-third of its NAV, including the proceeds borrowed, for investment purposes. The fund anticipates it will pay interest on the loan at short-term rates and that the net return on the fund's portfolio, including the proceeds of the borrowing, will exceed the interest rate on the loan. Through leverage with bank borrowing the fund seeks to obtain a higher return for holders of its common shares than if the fund did not use leverage.

# CEF Performance Statistics

LIPPER

| Lipper Category | Average of 1Mo Nav | Average of 1 Mo Mkt | Average of Jul P/D | Average of Jun P/D | Average of 1 Mo P/D chg | Average of YTD NAV Change | Average of YTD Mkt Change | Average of YTD P/D Change (%) |
|---|---|---|---|---|---|---|---|---|
| California Municipal Debt Funds | -0.59% | 0.16% | 0.09% | -0.69% | 0.78% | 2.26% | 4.34% | 2.12% |
| Convertible Securities Funds | 0.10% | 0.54% | -3.66% | -4.52% | 0.41% | 3.51% | 9.67% | 5.44% |
| Core Funds | 0.10% | -0.43% | -6.46% | -7.15% | -0.54% | 4.80% | 9.02% | 3.24% |
| Corporate BBB-Rated Debt Funds(Leveraged) | -0.41% | 0.29% | -7.31% | -7.97% | 0.66% | 2.50% | 3.02% | 0.47% |
| Corporate Debt Funds BBB-Rated | -0.07% | 1.67% | -3.26% | -4.93% | 1.67% | 1.67% | 2.48% | 1.18% |
| Developed Market Funds | 0.14% | 0.19% | -9.54% | -9.57% | 0.04% | 15.77% | 20.41% | 3.54% |
| Emerging Markets Funds | 1.73% | 1.66% | -10.54% | -10.49% | -0.05% | 17.31% | 21.85% | 2.89% |
| Emerging Mrkts Hard Currency Debt Funds | -1.01% | -2.75% | -3.93% | -2.03% | -1.90% | 4.41% | 7.71% | 2.77% |
| Energy MLP Funds | -1.07% | -1.17% | -1.57% | -1.35% | -0.22% | -9.58% | -3.91% | 6.06% |
| General & Insured Muni Debt Funds (Leveraged) | -0.69% | -0.15% | -2.59% | -3.12% | 0.53% | 2.19% | 3.72% | 1.41% |
| General & Insured Muni Fds (Unleveraged) | -0.63% | -0.70% | -1.97% | -1.84% | -0.13% | 1.74% | 3.61% | 1.79% |
| General Bond Funds | -0.27% | -0.11% | -0.82% | -0.91% | 0.10% | 2.95% | 4.89% | 2.40% |
| Global Funds | -0.21% | 0.65% | -5.82% | -6.60% | 0.78% | 8.22% | 14.22% | 4.81% |
| Global Income Funds | 0.31% | 0.17% | -1.74% | -1.62% | -0.11% | 4.67% | 8.46% | 3.62% |
| Growth Funds | 8.07% | 3.80% | -8.60% | -10.10% | 1.50% | 30.25% | 17.70% | 4.30% |
| High Yield Funds | -0.25% | 0.21% | -3.49% | -4.07% | 0.59% | 2.04% | 5.74% | 3.60% |
| High Yield Funds (Leveraged) | -0.55% | -0.77% | -5.71% | -5.55% | -0.16% | 2.11% | 3.22% | 0.93% |
| High Yield Municipal Debt Funds | -0.45% | -0.35% | -1.85% | -1.90% | 0.05% | 2.56% | 5.13% | 2.36% |
| Income & Preferred Stock Funds | 0.34% | 0.69% | -2.01% | -2.47% | 0.20% | 4.70% | 8.21% | 2.33% |
| Intermediate Municipal Debt Funds | -0.60% | 0.05% | -4.07% | -4.69% | 0.62% | 2.28% | 1.89% | -0.47% |
| Loan Participation Funds | -1.30% | -2.52% | -3.68% | -2.10% | -0.95% | -1.03% | -1.13% | -0.75% |
| Natural Resources Funds | -1.27% | -2.57% | -5.18% | -3.86% | -1.32% | -10.32% | -6.18% | 4.17% |
| New Jersey Municipal Debt Funds | -0.60% | -0.13% | -6.18% | -6.65% | 0.48% | 2.21% | 1.85% | -0.53% |
| New York Municipal Debt Funds | -0.62% | 0.43% | -3.82% | -4.85% | 1.03% | 2.35% | 3.10% | 0.61% |
| Options Arbitrage/Opt Strategies Funds | -0.38% | -0.61% | -1.04% | -0.69% | -0.35% | 5.31% | 10.58% | 4.75% |
| Other States Municipal Debt Funds | -0.65% | -0.37% | -3.84% | -4.30% | 0.29% | 2.01% | 3.68% | 1.58% |
| Pacific Ex Japan Funds | -4.75% | -5.21% | -7.72% | -7.38% | -0.34% | 13.19% | 19.65% | 4.92% |
| Pennsylvania Municipal Debt Funds | -0.57% | 0.17% | -8.47% | -9.20% | 0.73% | 1.77% | 0.16% | -1.77% |
| Real Estate Funds | 0.43% | 1.45% | -5.95% | -6.56% | 0.61% | 1.71% | 6.60% | 3.48% |
| Sector Equity Funds | 1.62% | 1.31% | -4.20% | -3.93% | -0.27% | 6.95% | 11.68% | 3.45% |
| U.S. Mortgage Funds | -0.03% | 1.05% | -1.03% | -2.15% | 1.12% | 2.79% | 5.35% | 2.63% |
| Utility Funds | -2.06% | -0.86% | -0.02% | -1.22% | 1.20% | 6.34% | 13.45% | 6.24% |
| Value Funds | 0.53% | 0.77% | -6.68% | -6.70% | 0.02% | 3.10% | 9.76% | 3.70% |

# Top 5 Performing CEFs
## LIPPER

| Fund Name | Category | Ticker Symbol | 1-Month NAV Change | Rank |
|---|---|---|---|---|
| Engex Inc | Growth Funds | | 14.1% | 1 |
| Morg Stan China A | Emerging Markets Funds | XCAFX | 6.7% | 2 |
| Tekla Life Sciences Inv | Sector Equity Funds | XHQLX | 6.6% | 3 |
| Tekla Healthcare Invest | Sector Equity Funds | XHQHX | 6.1% | 4 |
| Tekla Healthcare Opps | Sector Equity Funds | XTHQX | 5.9% | 5 |

| Fund Name | Category | Ticker Symbol | Year-to-Date NAV Change | Rank |
|---|---|---|---|---|
| Engex Inc | Growth Funds | | 48.4% | 1 |
| Turkish Investment Fund | Emerging Markets Funds | XTKFX | 25.4% | 2 |
| India Fund | Emerging Markets Funds | XIFNX | 24.2% | 3 |
| Morg Stan India Inv | Emerging Markets Funds | XIIFX | 24.1% | 4 |
| Morg Stan China A | Emerging Markets Funds | XCAFX | 24.1% | 5 |

| Fund Name | Category | Ticker Symbol | 1-Month Market Change | Rank |
|---|---|---|---|---|
| BlackRock VA Muni Bd Tr | Other States Municipal Debt Funds | XBHVX | 8.9% | 1 |
| Morg Stan China A | Emerging Markets Funds | XCAFX | 8.4% | 2 |
| J Hancock Finl Opptys | Sector Equity Funds | XBTOX | 7.2% | 3 |
| RENN Fund | Global Funds | | 6.7% | 4 |
| Tekla Healthcare Opps | Sector Equity Funds | XTHQX | 6.3% | 5 |

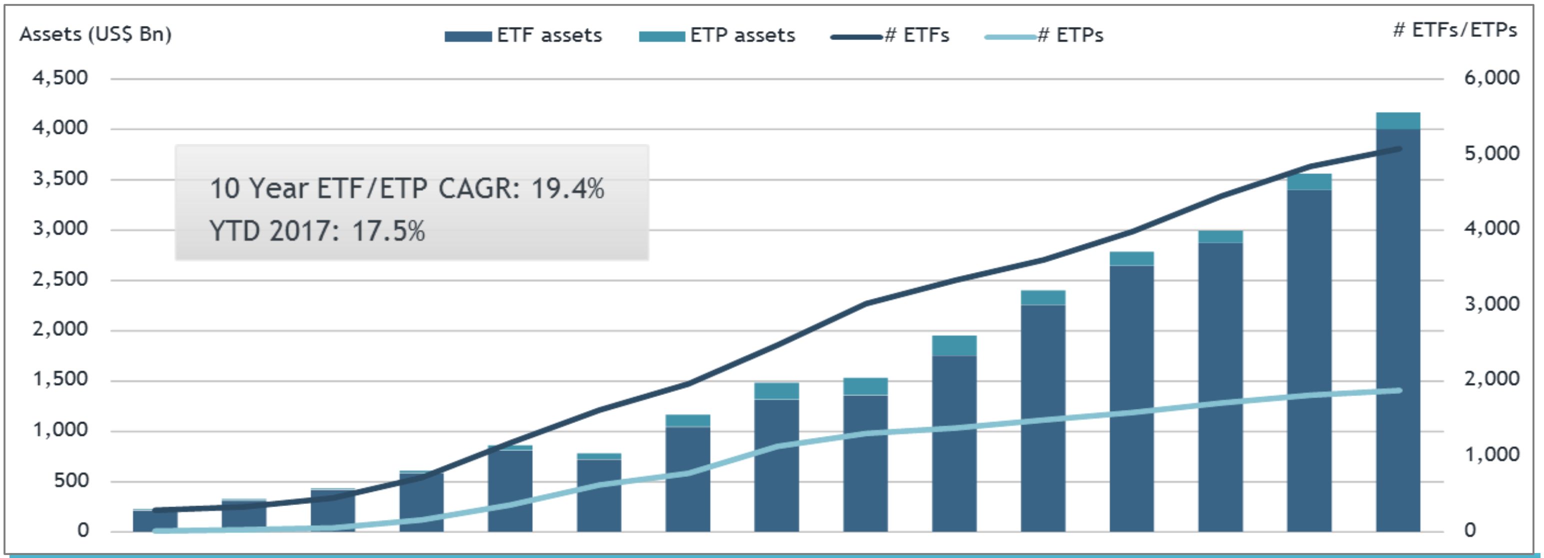
| Fund Name | Category | Ticker Symbol | Year-to-Date Market Change | Rank |
|---|---|---|---|---|
| Turkish Investment Fund | Emerging Markets Funds | XTKFX | 42.2% | 1 |
| Asia Pacific Fund | Pacific Ex Japan Funds | XAPBX | 33.7% | 2 |
| Aberdeen Greater China | Emerging Markets Funds | XGCHX | 32.0% | 3 |
| Morg Stan China A | Emerging Markets Funds | XCAFX | 31.7% | 4 |
| PIMCO Gl StksPLUS & Inc | Options Arbitrage/Opt Strategies Funds | XPGPX | 30.8% | 5 |

| Fund Name | Category | Ticker Symbol | 1-Month P/D Change | Rank |
|---|---|---|---|---|
| BlackRock VA Muni Bd Tr | Other States Municipal Debt Funds | XBHVX | 10.8% | 1 |
| Westn Asst IG Def Opp Tr | Corporate Debt Funds BBB-Rated | XIGIX | 5.6% | 2 |
| Putnam Premier Income | General Bond Funds | XPPTX | 5.4% | 3 |
| MFS Special Value Trust | High Yield Funds | XMFVX | 5.3% | 4 |
| Nuveen CA Muni Value 2 | California Municipal Debt Funds | XNCBX | 5.1% | 5 |

| Fund Name | Category | Ticker Symbol | Year-to-Date P/D Change | Rank |
|---|---|---|---|---|
| PIMCO Gl StksPLUS & Inc | Options Arbitrage/Opt Strategies Funds | XPGPX | 25.4% | 1 |
| BlackRock VA Muni Bd Tr | Other States Municipal Debt Funds | XBHVX | 24.7% | 2 |
| PIMCO Strat Income | Global Income Funds | XRCSX | 16.7% | 3 |
| Calamos Glbl Tot Rtn | Global Funds | XCGOX | 14.7% | 4 |
| MFS Special Value Trust | High Yield Funds | XMFVX | 13.2% | 5 |

## Global ETF and ETP asset growth as at end of June 2017

At the end of June 2017, the Global ETF industry had 5,083 ETFs, with 10,540 listings, assets of US$4,002 Bn, from 293 providers on 68 exchanges. At the end of June 2017, the Global ETF/ETP industry had 6,965 ETFs/ETPs, with 13,125 listings, assets of US$4,168 Bn, from 328 providers on 70 exchanges.




| Year | 2003 | 2004 | 2005 | 2006 | 2007 | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | Jun-17 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| # ETFs | 291 | 337 | 453 | 727 | 1,187 | 1,619 | 1,968 | 2,479 | 3,030 | 3,339 | 3,612 | 3,987 | 4,457 | 4,848 | 5,083 |
| # ETFs/ETPs | 306 | 367 | 509 | 890 | 1,548 | 2,244 | 2,747 | 3,619 | 4,342 | 4,721 | 5,100 | 5,576 | 6,174 | 6,667 | 6,965 |
| ETF assets | 212 | 310 | 417 | 580 | 807 | 716 | 1,041 | 1,313 | 1,355 | 1,754 | 2,254 | 2,643 | 2,870 | 3,397 | 4,002 |
| ETF/ETP assets | 218 | 319 | 426 | 603 | 857 | 774 | 1,158 | 1,478 | 1,526 | 1,949 | 2,398 | 2,784 | 2,993 | 3,548 | 4,168 |

## Summary for ETFs/ETPs: Global

ETFGI, a leading independent research and consultancy firm on trends in the global ETF/ETP ecosystem, reported today that assets invested in ETFs/ETPs listed globally reached a new record of US$4.167 trillion at the end of first half of 2017, according to ETFGI's June 2017 global ETF and ETP industry insights report an annual paid for research subscription service (click here to view the ETFGI ETFs/ETPs listed globally asset growth chart).

The Global ETF/ETP industry had 6,965 ETFs/ETPs, with 13,125 listings, assets of US$4.167 trillion, from 329 providers listed on 70 exchanges in 56 countries.

"Equity markets have performed well in the first half of 2017: the S&P 500 gained 9.34%, international equity markets outside the US were up 14.27% and emerging markets were up 16.69%. Political risks remain a focus for investors - the ability of the Trump administration to move forward on policy goals and hearings on Capitol Hill, Brexit negotiations, and North Korea is still an area of concern." According to Deborah Fuhr, managing partner at ETFGI.

ETFs and ETPs listed globally gathered a record amount of $63.57 Bn in net inflows in June and a record level of $347.70 Bn in year to date net inflows. At this point last year there were net inflows of just $123.55 Bn.

Equity ETFs/ETPs gathered a record level of $41.15 Bn in net inflows in June, bringing year to date net inflows to a level of $242.69 Bn, which is much greater than the net inflows of $15.81 Bn over the same period last year.

Fixed income ETFs and ETPs have gathered a record level of $17.17 Bn in net inflows in June, growing year to date net inflows to a record level of $80.96 Bn, which is greater than the same period last year which saw net inflows of $67.98 Bn.

Commodity ETFs/ETPs accumulated net inflows of $1.34 Bn in June. Year to date, net inflows are at $7.29 Bn, which is significantly less than the net inflows of $26.31 Bn gathered over the same period last year.

iShares gathered the largest net ETF/ETP inflows in June with US$28.83 Bn, followed by Vanguard with US$13.38 Bn and SPDR ETFs with US$6.68 Bn net inflows.

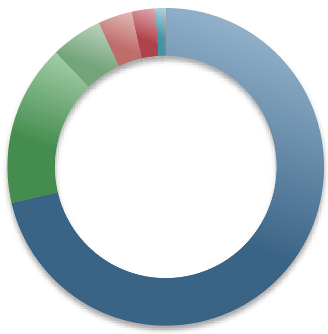
YTD, iShares gathered the largest net ETF/ETP inflows with US$140.84 Bn which is above the US$137.90 Bn gathered in all of 2016, followed by Vanguard with US$82.31 Bn and Schwab ETFs with US$13.39 Bn net inflows.

*Source: ETFGI data sourced from ETF/ETP sponsors, exchanges, regulatory filings, Thomson Reuters/Lipper, Bloomberg, publicly available sources, and data generated by our in-house team.*
*Note: "ETFs" are typically open-end index funds that provide daily portfolio transparency, are listed and traded on exchanges like stocks on a secondary basis as well as utilising a unique creation and redemption process for primary transactions. "ETPs" refers to other products that have similarities to ETFs in the way they trade and settle but they do not use a mutual fund structure. The use of other structures including grantor trusts, partnerships, notes and depositary receipts by ETPs can create different tax and regulatory implications for investors when compared to ETFs which are funds.*

# Global ETF/ETP Assets Summary

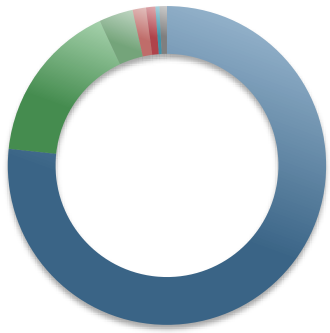
etfgi.com

### ETF/ETP assets by region listed



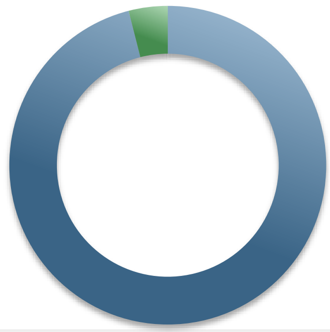
| Region | # ETFs/ ETPs | Assets (US$ Bn) | % total |
|---|---|---|---|
| US | 2,041 | $2,972.8 | 71.3% |
| Europe | 2,286 | $686.3 | 16.5% |
| Japan | 188 | $219.6 | 5.3% |
| Asia Pacific (ex-Japan) | 1,082 | $144.9 | 3.5% |
| Canada | 515 | $100.9 | 2.4% |
| Middle East and Africa | 806 | $37.1 | 0.9% |
| Latin America | 47 | $6.1 | 0.1% |
| **Total** | **6,965** | **$4,167.7** | **100.0%** |

### ETF/ETP assets by asset class



| Asset class | # ETFs/ ETPs | Assets (US$ Bn) | % total |
|---|---|---|---|
| Equity | 3,780 | $3,195.4 | 76.7% |
| Fixed Income | 984 | $683.4 | 16.4% |
| Commodities | 717 | $144.1 | 3.5% |
| Active | 364 | $56.7 | 1.4% |
| Leveraged | 412 | $39.8 | 1.0% |
| Leveraged Inverse | 190 | $16.8 | 0.4% |
| Others | 518 | $31.5 | 0.8% |
| **Total** | **6,965** | **$4,167.7** | **100.0%** |

### ETF/ETP assets by product structure

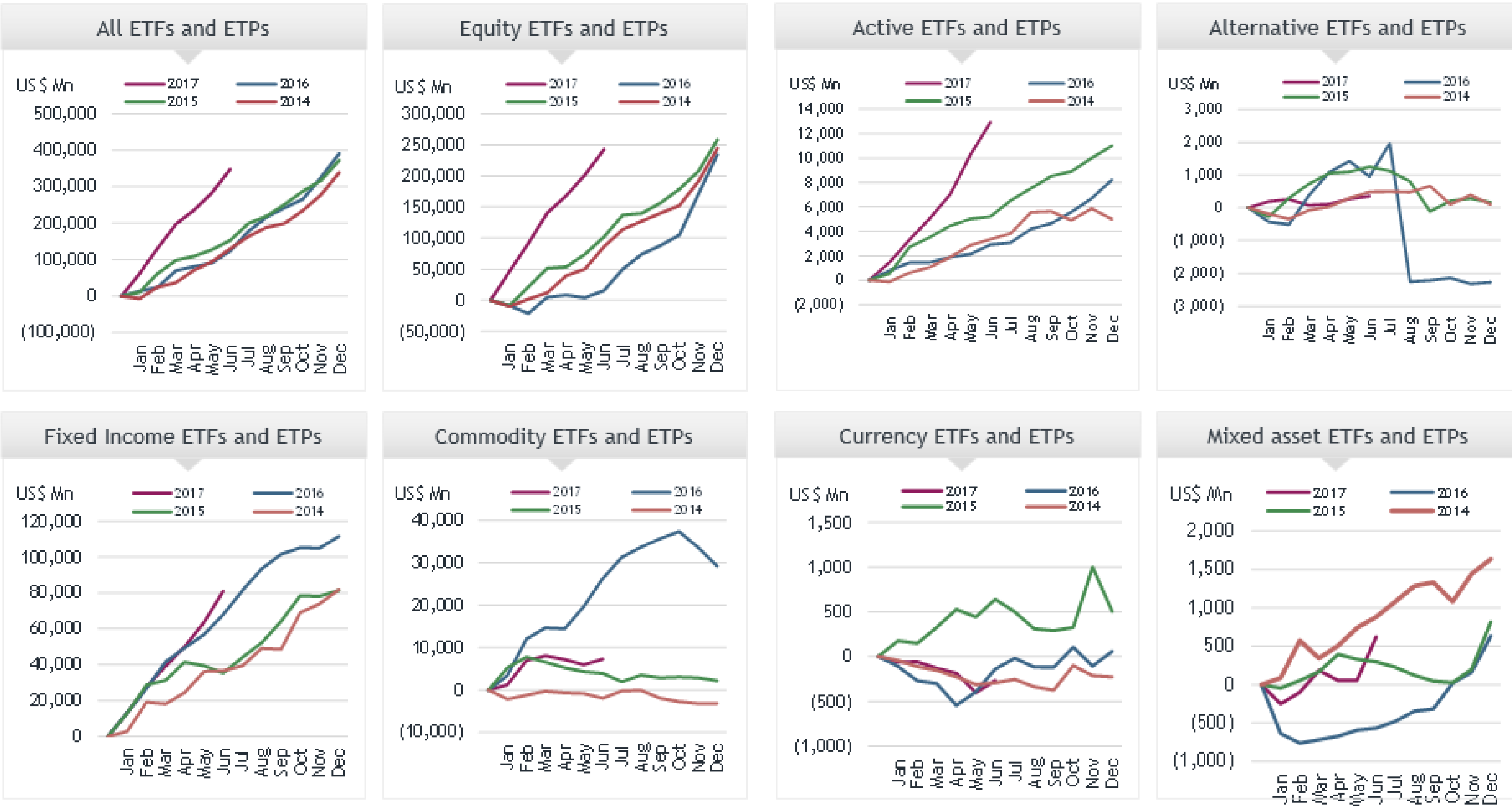


| Asset class | # ETFs/ ETPs | Assets (US$ Bn) | % total |
|---|---|---|---|
| ETF | 5,083 | $4,002.1 | 96.0% |
| ETP | 1,882 | $165.6 | 4.0% |
| **Total** | **6,965** | **$4,167.7** | **100.0%** |

*Source: ETFGI data sourced from ETF/ETP sponsors, exchanges, regulatory filings, Thomson Reuters/Lipper, Bloomberg, publicly available sources, and data generated by our in-house team.*

*Source: ETFGI data sourced from ETF/ETP sponsors, exchanges, regulatory filings, Thomson Reuters/Lipper, Bloomberg, publicly available sources, and data generated by our in-house team. Note: This report is based on the most recent data available at the time of publication. Asset and flow data may change slightly as additional month-end data becomes available.*

## YTD 2017 vs 2016, 2015, 2014 ETF and ETP net new assets by asset class: Global




ETFs and ETPs listed globally gathered net inflows of $63,567 Mn in June. Year to date, net inflows stand at $347,699 Mn. At this point last year there were net inflows of $123,550 Mn.

Equity ETFs/ETPs saw net inflows of $41,149 Mn in June, bringing year to date net inflows to $242,689 Mn, which is greater than the net inflows of $15,807 Mn over the same period last year.

Fixed income ETFs and ETPs experienced net inflows of $17,171 Mn in June, growing year to date net inflows to $80,965 Mn, which is greater than the same period last year which saw net inflows of $67,980 Mn.

Commodity ETFs/ETPs accumulated net inflows of $1,339 Mn in June. Year to date, net inflows are at $7,292 Mn, compared to net inflows of $26,308 Mn over the same period last year.

Actively managed products saw net inflows of $2,681 Mn in June, bringing year to date net inflows to $12,930 Mn, which is greater than the net inflows of $2,915 Mn over the same period last year.

Products tracking alternative indices experienced net inflows of $81 Mn in June, growing year to date net inflows to $350 Mn, which is less than the same period last year which saw net inflows of $952 Mn.

Currency products accumulated net inflows of $135 Mn in June. Year to date, net outflows are at $269 Mn, compared to net outflows of $138 Mn over the same period last year.

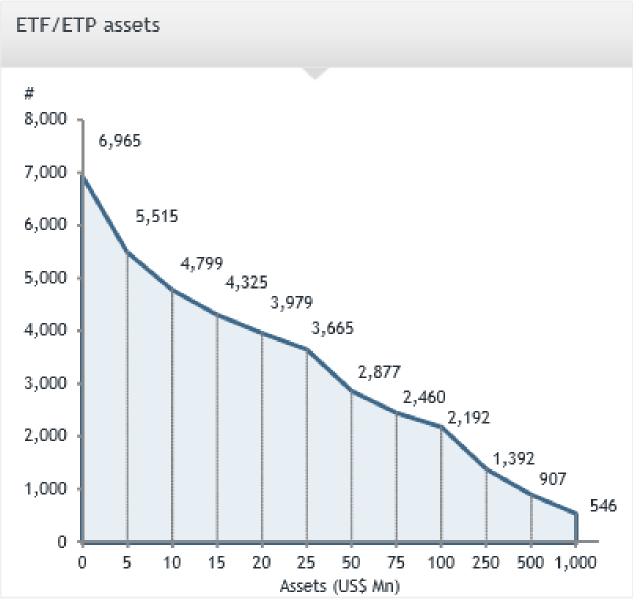
Products holding more than one asset class saw net inflows of $565 Mn in June, bringing year to date net inflows to $621 Mn, which is greater than the net outflows of $569 Mn over the same period last year.

*Source: ETFGI data sourced from ETF/ETP sponsors, exchanges, regulatory filings, Thomson Reuters/Lipper, Bloomberg, publicly available sources, and data generated by our in-house team.*
*Note: This report is based on the most recent data available at the time of publication. Asset and flow data may change slightly as additional month-end data becomes available.*

# ETF/ ETP Distribution and Benchmarks

etfgi.com

## Distribution of ETFs/ETPs by size




| Assets greater than (US$ Mn) | # ETFs/ ETPs | % total | Total assets (US$ Bn) | % total |
|---|---|---|---|---|
| 0 | 6,965 | 100.0% | 4,161 | 100.0% |
| 5 | 5,515 | 79.2% | 4,158 | 99.9% |
| 10 | 4,799 | 68.9% | 4,153 | 99.8% |
| 15 | 4,325 | 62.1% | 4,147 | 99.7% |
| 20 | 3,979 | 57.1% | 4,141 | 99.5% |
| 25 | 3,665 | 52.6% | 4,134 | 99.4% |
| 50 | 2,877 | 41.3% | 4,105 | 98.7% |
| 75 | 2,460 | 35.3% | 4,080 | 98.1% |
| 100 | 2,192 | 31.5% | 4,057 | 97.5% |
| 250 | 1,392 | 20.0% | 3,929 | 94.4% |
| 500 | 907 | 13.0% | 3,755 | 90.3% |
| 1,000 | 546 | 7.8% | 3,493 | 84.0% |

546 ETFs/ETPs have greater than US$1 Bn in assets, while 2,192 have greater than US$100 Mn in assets and 2,877 have greater than US$50 Mn in assets. The 546 ETFs/ETPs with greater than US$1 Bn in assets hold a combined total of US$3,493 Bn, or 84.0%, of Global ETF/ETP assets.

## ETF/ETP underlying benchmarks: developed equity

Top 20 by assets

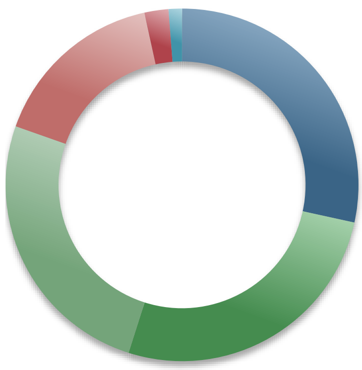
| Name | Assets (US$ Mn) Jun-17 | NNA (US$ Mn) Jun-17 | NNA (US$ Mn) YTD 2017 |
|---|---|---|---|
| MSCI EAFE Index | 92,325 | 2,221 | 10,901 |
| CRSP US Total Market Index | 79,832 | 355 | 4,712 |
| FTSE Developed All Cap ex US Transition Index | 55,615 | 2,224 | 9,841 |
| EURO STOXX 50 NR Index | 40,574 | (316) | 1,726 |
| MSCI US REIT Index | 33,993 | (169) | 1,097 |
| MSCI Japan Index | 32,396 | 1,505 | 803 |
| CRSP US Large Cap Value Index | 31,340 | 123 | 3,179 |
| MSCI EAFE IMI Index USD | 29,270 | 2,987 | 11,072 |
| CRSP US Large Cap Growth Index | 27,068 | (44) | 777 |
| MSCI EMU index | 22,702 | 1,005 | 7,109 |
| DAX Index | 20,224 | (670) | (1,435) |
| CRSP US Mid Cap Index | 19,662 | 136 | 1,597 |
| Hang Seng Index | 18,994 | 303 | (714) |
| CRSP US Small Cap Index | 18,675 | (19) | 1,527 |
| FTSE High Dividend Yield Index | 18,153 | 41 | 19 |
| Dow Jones Industrial Average Index | 17,671 | 836 | 363 |
| Dow Jones US Select Dividend Index | 17,605 | (20) | (592) |
| FTSE Developed Europe Index | 17,573 | 2,025 | 4,342 |
| MSCI Europe index | 15,555 | 142 | (397) |
| MSCI USA Minimum Volatility Index | 13,689 | 505 | 311 |

Top 20 by monthly net inflows

| Name | Assets (US$ Mn) Jun-17 | NNA (US$ Mn) Jun-17 | NNA (US$ Mn) YTD 2017 |
|---|---|---|---|
| MSCI EAFE IMI Index USD | 29,270 | 2,987 | 11,072 |
| FTSE Developed All Cap ex US Transition Index | 55,615 | 2,224 | 9,841 |
| MSCI EAFE Index | 92,325 | 2,221 | 10,901 |
| FTSE Developed Europe Index | 17,573 | 2,025 | 4,342 |
| MSCI Japan Index | 32,396 | 1,505 | 803 |
| MSCI EMU index | 22,702 | 1,005 | 7,109 |
| Dow Jones Industrial Average Index | 17,671 | 836 | 363 |
| EURO STOXX 50 Index | 4,145 | 507 | 1,506 |
| MSCI USA Minimum Volatility Index | 13,689 | 505 | 311 |
| FTSE All World Developed ex US Index | 10,359 | 492 | 2,301 |
| MSCI USA Momentum Index | 3,121 | 439 | 871 |
| Dow Jones US Real Estate Index | 4,733 | 399 | 471 |
| MSCI Europe IMI Index | 2,834 | 388 | 1,426 |
| CRSP US Total Market Index | 79,832 | 355 | 4,712 |
| MSCI EAFE Minimum Volatility Index | 7,235 | 335 | 428 |
| MSCI Australia Index | 2,735 | 306 | (359) |
| FTSE EPRA/NAREIT US Dividend+ Index | 956 | 303 | 344 |
| Hang Seng Index | 18,994 | 303 | (714) |
| MSCI Canada Index | 4,544 | 294 | (551) |
| FTSE Developed Asia Pacific Net Tax US RIC TR Index USD | 4,304 | 272 | 680 |

## 2017 ETF/ETP product launches

# ETFs/ETPs by region listed



# ETFs/ETPs by asset class

# ETFs/ETPs by product structure

| Region | # ETFs/ETPs | % total |
|---|---|---|
| Asia Pacific (ex-Japan) | 116 | 28.4% |
| US | 108 | 26.5% |
| Europe | 104 | 25.5% |
| Canada | 66 | 16.2% |
| Japan | 9 | 2.2% |
| Middle East and Africa | 5 | 1.2% |
| **Total** | **408** | **100.0%** |

| Asset class | # ETFs/ETPs | % total |
|---|---|---|
| Equity | 142 | 34.8% |
| Active | 76 | 18.6% |
| Fixed income | 56 | 13.7% |
| Commodities | 43 | 10.5% |
| Leveraged | 32 | 7.8% |
| Mixed | 26 | 6.4% |
| Others | 33 | 8.1% |
| **Total** | **408** | **100.0%** |

| Structure | # ETFs/ETPs | % total |
|---|---|---|
| ETF | 330 | 80.9% |
| ETP | 78 | 19.1% |
| **Total** | **408** | **100.0%** |

*Source: ETFGI, Bloomberg, ETF/ETP providers.*

Please visit www. Etfgi.com and contact deborah.fuhr@etfgi.com if you would like to subscribe to ETFGI's full monthly Global ETF and ETP industry insights reports containing over 300 pages of charts and analysis, ETFGI's Institutional Users of ETFs and ETPs report or a custom analysis.

# Rating Actions

**To access the complete rating action, please click on the links below.**

- **Fitch Rates TPS Shares Issued by Nuveen Closed-End Fund 'AA'** – May 19
- **Fitch Affirms Madison Arbor Senior Notes at 'AAA'** – May 19
- **Fitch Affirms VMTP Shares Issued by 9 Invesco Closed-End Funds** – June 1
- **Fitch Affirms Gabelli Fund Auction Preferred Ratings at 'AA'** – June 15
- **Fitch Affirms Notes and Preferred Shares Issued by Duff & Phelps Closed-End Funds** – June 15
- **Fitch Affirms MRPS Issued by Blackstone / GSO Closed-End Funds** – June 15
- **Fitch Upgrades Astrea III's Class A-1 Notes; Affirms Classes A-2 and B** – July 10
- **Fitch Rates VMTPs Issued by Managed Duration Investment Grade Municipal Fund** – July 12
- **Fitch Affirms and Withdraws Ratings on VRTP Shares of Two Invesco Funds** – July 17

# Closed-End Fund review – Second Quarter 2017

July 20, 2017

Authored by:
**Jeff Margolin**
*Senior Vice President, CEF Analyst*
First Trust Advisors

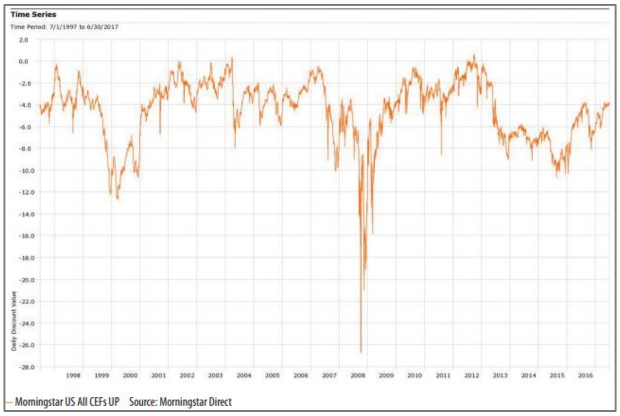
### Second Quarter 2017 Overview

The second quarter of 2017 was another solid one for diversified closed-end fund (CEF) investors. The average fund was up 3.50% for the quarter and is now up 8.82% year-to-date (YTD). It was a broad based rally again this quarter with equity funds up on average 2.91%, taxable fixed-income funds up 4.10% and municipal funds up 3.60%. Equity CEFs are now up on average 11.42% YTD, taxable fixed-income funds are up on average 8.93% YTD and municipal funds are up 6.02% YTD (Source: Morningstar. All data is share price total return).

Similar to the first quarter of the year, several factors contributed to the solid performance many categories posted during the second quarter. From my viewpoint, those factors included rising global equity prices, still solid fundamentals for credit-sensitive asset classes (i.e., defaults below historical averages), demand for income-oriented investments, a quiet CEF Initial Public Offering (IPO) market (which helps create demand for the secondary market of CEFs) and discount narrowing all helped contribute to the broad-based positive total returns many categories earned during the second quarter.

### Average Discounts to Net Asset Value (NAV) Continue to Narrow

As you can clearly see in the chart below, average discounts to NAV continue to narrow for the Morningstar universe of all CEFs.




Indeed, the average discount to NAV for all CEFs at the end of the second quarter was 3.74%. They ended the first quarter at 5.12% and ended 2016 at 6.34%. The trend of discounts narrowing has been a very rewarding one for shareholders (particularly those who took advantage of double-digit discounts in 2015 and early 2016) as in many cases share prices are outperforming rising NAVs--causing discounts to narrow. For example, using Morningstar total return data, the average CEF share price total return is up 8.82% YTD which is outperforming the average CEF NAV total return (which is up 5.91% YTD).

As discounts to NAV have narrowed considerably the past two years, I believe it means CEF investors need to pick their spots carefully and continue to focus on categories where the fundamentals, valuations and outlook remain compelling. From my standpoint, equity income-oriented CEFs (both domestic and global), as well as shorter duration fixed-income categories, continue to stand out as being compelling total return investments.

### No Changes to My Three Favored Categories

I am making no change to my belief that the most compelling categories of the CEF marketplace remain U.S. Equity, Senior Loan and Global Equity. My thesis for continuing to want to have overweight exposure to these three categories remains the same and is the following:
1) These three categories continue to have strong fundamentals and valuations within their respective underlying asset classes.
2) All three remain poised to benefit from the macro view our Economics Team continues to forecast for the remaining half of 2017 including more “Plow Horse” U.S. GDP growth, as they phrase it, higher U.S. equity prices (their year-end forecast for the S&P 500 Index remains 2700), at least one more federal funds rate hike this year and a steady rise in the interest rate on the 10-year U.S. Treasury. This macro view continues to give my focus to equity income-oriented CEFs and shorter duration fixed-income funds, while focusing less on longer-duration levered fixed-income funds.

Click here for complete reading

# Closed-end Funds - Shorter-Term Trusts

May 30, 2017

Authored by:
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*Head of CEF/ETP Research*
Wells Fargo Advisors

Authored by:
Adam Shah
*CEF/ETP Analyst*
Wells Fargo Advisors

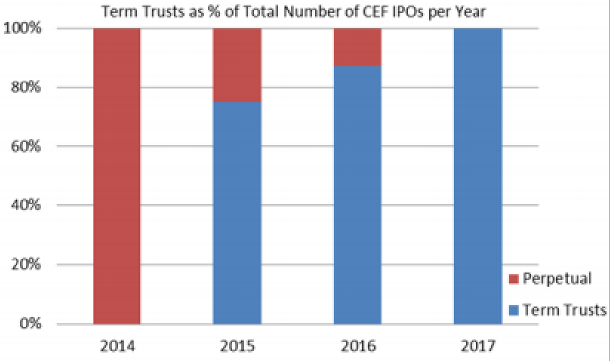
**Summary**
>> A closed-end fund (CEF) structure with a shorter termination of three to seven years after its initial public offering (IPO) has been a recent innovation that has dominated the primary market in the past few years.
>> Shorter-term trusts have commanded better valuations — tighter discounts and even smaller premiums — after their IPO than longer term trusts and perpetual funds.
>> As the termination date approaches, investors should expect declining distributions.

In the current environment of increasingly disruptive market forces, the CEF structure has also undergone drastic innovation relative to the past few decades. One such innovation has been the term trust with a shorter life.

**Innovations in the Primary Market**

The CEF IPO market ebbs and flows with market cycles, and the volume of CEF IPOs had diminished substantially after the Taper Tantrum1 in the spring of 2013. As investors perceived that the accommodative environment was finally coming to an end and a market environment of higher interest rates was probably approaching, discounts among existing CEFs widened and valuations remained lower for over two years until the Federal Reserve started raising rates in December 2015. When discounts are generally wide, it is difficult to issue new CEFs — a new CEF IPO is not as compelling when similar existing CEFs are already trading at wide discounts.

Term Trust Trend
Term Trusts as % of Total Number of CEF IPOs per Year




*Source: Bloomberg, Wells Fargo Advisors (data as of March 31, 2017)*
*"Term Trusts" in 2015 and 2016 includes CEFs that are not a term trust, but have a shareholder vote to liquidate or convert to a mutual fund.*

Thus, it is not surprising that the primary market for CEFs was subdued following the Taper Tantrum — on average, barely one launch per month.

In order to resuscitate the CEF IPO market, a number of innovations were introduced and tested, but only two have provided good results and therefore persisted: (1) lower offering fees, and (2) shorter terms. First, declines in expenses are ubiquitous these days among all sorts of investment vehicles such as exchange-traded products (ETPs), mutual funds, unit investment trusts (UIT), etc. In the case of CEF IPOs, the offering expenses declined on average from 4.5% to 1.5%, which allowed the IPO premium to start at a much narrower level2. (Decades ago when markets were less competitive, the offering expenses were in the double-digits.) Second, perpetual structures gave rise to term trusts with much shorter terms than ever before. In the past, terms were normally as long as 10 to 20 years, but the recent terms range between three and seven years with most having 5-year terms3.

**Characteristics**

*Underlying exposure.* So far, the underlying asset classes of all the recent shorter-term trusts have been fixed-income such as municipal bonds, high yield corporate bonds, corporate loans, preferred securities and income-focused convertibles. Yet, one could speculate that sponsors of future CEF IPOs may attempt to launch equity-based term trusts.

*Term.* Most of the recent term trusts have a 5-year term, except two that have a 3-year term and two others that have 7-year terms. One may speculate that sponsors may try to extend the length of the term in future IPOs in order to make it a more viable proposition.

*Option to Extend.* Most have an option to extend the term date for one 6-month period without shareholder approval, which provides the portfolio managers the flexibility to wait for an opportune time to unwind the portfolio instead of liquidating securities in the middle of severe market turmoil. Any further extensions would require a shareholder vote.

*Target Payout.* The typical target at termination is to pay out the initial NAV and in other cases a floating NAV. Absent are the cases where the objective is to pay out the IPO market price as was the case of the original longer-term trusts.

Some may remember that a few of those original term trusts a few decades ago were not able to achieve their objective of returning the IPO price at termination. In some of those worst cases, the term trusts returned less than 80% of the IPO price at term (as well as suffering severe reductions in distributions). In other cases, some of the original term trusts barely managed to return the IPO price, but at the expense of withholding most — or all — distributions toward the end of their lives in order to build up the NAV.

### Distributions near the Term: Beware!

As a term trust approaches its termination date, it is possible that it will reduce its distribution. A term is usually designed so that most of the portfolio securities will mature within a few months of the term date. However, securities that mature or are called before the fund's term will be reinvested in shorter maturities and probably at a lower yield than the original purchase yield of the previous security being replaced. This will likely reduce the earnings power of the term trust, which may eventually result in a reduction in its distribution. One can imagine that some holders may rotate into another CEF with a higher-yield at that point thereby exerting pressure on the valuation — the discount may widen or a premium may narrow. However, we do not expect wide discounts to persist because the reality of receiving NAV will be approaching.

### Conclusion

Investors seem to favor the innovative shorter-term trust structure; however, they should be prepared to experience potential reductions in distributions as the termination nears.

**List of All Shorter-term Trusts**

| Name | Ticker | Inception Date | Target Payout | IPO Price | Target Termination Price | Termination Date | Term Period (years) | Remaining Time to Termination (years) |
|---|---|---|---|---|---|---|---|---|
| BlackRock Defined Opportunity Credit Trust | BHL | 1/28/2008 | Floating NAV | $15 | | 12/29/2017 | 9 | 0.6 |
| Nuveen High Income December 2018 Target Term Fund | JHA | 11/13/2015 | IPO NAV | $10 | $9.86 | 12/1/2018 | 3 | 1.5 |
| BlackRock California Municipal 2018 Term Trust | BJZ | 10/26/2001 | IPO Price | $15 | $15.00 | 12/31/2018 | 17 | 1.6 |
| BlackRock Municipal 2018 Term Trust | BPK | 10/26/2001 | IPO Price | $15 | $15.00 | 12/31/2018 | 17 | 1.6 |
| BlackRock New York Municipal 2018 Term Trust | BLH | 10/26/2001 | IPO Price | $15 | $15.00 | 12/31/2018 | 17 | 1.6 |
| Nuveen Mortgage Opportunity Term Fund | JLS | 11/24/2009 | Floating NAV | $25 | | 11/28/2019 | 10 | 2.5 |
| Nuveen High Income December 2019 Target Term Fund | JHD | 5/11/2016 | IPO NAV | $10 | $9.86 | 12/1/2019 | 3 | 2.5 |
| Nuveen Mortgage Opportunity Term Fund 2 | JMT | 2/24/2010 | Floating NAV | $25 | | 2/28/2020 | 10 | 2.8 |
| Blackstone / GSO Senior Floating Rate Term Fund | BSL | 5/28/2010 | Floating NAV | $20 | | 5/28/2020 | 10 | 3.0 |
| Nuveen Build America Bond Fund | NBB | 4/28/2010 | Floating NAV | $20 | | 6/30/2020 | 10 | 3.1 |
| Nuveen High Income 2020 Target Term Fund | JHY | 7/28/2015 | IPO NAV | $10 | $9.85 | 11/1/2020 | 5 | 3.5 |
| BlackRock Florida Municipal 2020 Term Trust | BFO | 9/30/2003 | IPO Price | $15 | $15.00 | 12/31/2020 | 17 | 3.6 |
| BlackRock Municipal 2020 Term Trust | BKK | 9/30/2003 | IPO Price | $15 | $15.00 | 12/31/2020 | 17 | 3.6 |
| Nuveen Build America Bond Opportunity Fund | NBD | 11/24/2010 | Floating NAV | $20 | | 12/31/2020 | 10 | 3.6 |
| Nuveen Municipal 2021 Target Term Fund | NHA | 1/26/2016 | IPO NAV | $10 | $9.85 | 3/1/2021 | 5 | 3.8 |
| Western Asset Municipal Defined Opportunity Trust Inc | MTT | 3/26/2009 | Floating NAV | $20 | | 4/30/2021 | 12 | 3.9 |
| Eaton Vance High Income 2021 Target Term Trust | EHT | 5/25/2016 | IPO NAV | $10 | $9.85 | 7/1/2021 | 5 | 4.1 |
| Nuveen High Income November 2021 Target Term Fund | JHB | 8/24/2016 | IPO NAV | $10 | $9.85 | 11/1/2021 | 5 | 4.5 |
| First Trust Senior Floating Rate 2022 Target Term Fund | FIV | 12/20/2016 | IPO NAV | $10 | $9.85 | 2/1/2022 | 5 | 4.7 |
| BlackRock 2022 Global Income Opportunity Trust | BGIO | 2/24/2017 | Floating NAV | $10 | | 2/28/2022 | 5 | 4.8 |
| Western Asset Mortgage Defined Opportunity Fund Inc | DMO | 2/23/2010 | Floating NAV | $20 | | 3/1/2022 | 12 | 4.8 |
| Nuveen Preferred and Income 2022 Term Fund | JPT | 1/26/2017 | Floating NAV | $25 | | 3/1/2022 | 5 | 4.8 |
| Nuveen Intermediate Duration Municipal Term Fund | NID | 12/6/2012 | Floating NAV | $15 | | 3/31/2023 | 10 | 5.9 |
| Nuveen Intermediate Duration Quality Municipal Term Fund | NIQ | 2/7/2013 | Floating NAV | $15 | | 6/30/2023 | 10 | 6.1 |
| Invesco High Income 2023 Target Term Fund | IHIT | 11/23/2016 | IPO NAV | $10 | $9.84 | 12/1/2023 | 7 | 6.5 |
| Nuveen Preferred & Income Term Fund | JPI | 7/26/2012 | Floating NAV | $25 | | 8/31/2024 | 12 | 7.3 |
| Miller/Howard High Dividend Fund | HIE | 11/24/2014 | Floating NAV | $20 | | 11/25/2024 | 10 | 7.5 |
| Western Asset Global Corporate Defined Opportunity Fund Inc | GDO | 11/24/2009 | Floating NAV | $20 | | 12/2/2024 | 15 | 7.5 |
| Western Asset Investment Grade Defined Opportunity Trust Inc | IGI | 6/26/2009 | Floating NAV | $20 | | 12/2/2024 | 15 | 7.5 |
| MainStay DefinedTerm Municipal Opportunities Fund | MMD | 6/27/2012 | Floating NAV | $20 | | 12/31/2024 | 12 | 7.6 |
| Western Asset High Yield Defined Opportunity Fund Inc | HYI | 10/27/2010 | Floating NAV | $20 | | 9/30/2025 | 14 | 8.4 |
| Eagle Growth & Income Opportunities Fund | EGIF | 6/19/2015 | Floating NAV | $20 | | 5/14/2027 | 11 | 10.0 |
| Blackstone / GSO Strategic Credit Fund | BGB | 9/26/2012 | Floating NAV | $20 | | 9/15/2027 | 14 | 10.3 |
| Eaton Vance Municipal Income 2028 Term Trust | ETX | 3/28/2013 | Floating NAV | $20 | | 6/30/2028 | 15 | 11.1 |
| Calamos Dynamic Convertible & Income Fund | CCD | 3/27/2015 | Floating NAV | $25 | | 3/26/2030 | 14 | 12.9 |
| AllianzGI Diversified Income & Convertible Fund | ACV | 5/21/2015 | Floating NAV | $25 | | 5/22/2030 | 15 | 13.0 |
| BlackRock Municipal 2030 Target Term Trust | BTT | 8/28/2012 | IPO Price | $25 | $25.00 | 12/31/2030 | 18 | 13.6 |
| ***Contingent Conversions:*** | | | | | | | | |
| RiverNorth/DoubleLine Strategic Opportunity Fund Inc | OPP | 9/27/2016 | Floating NAV | $20 | | 2021 | 5 | 4.6 |
| RiverNorth Opportunities Fund Inc | RIV | 12/23/2015 | Floating NAV | $20 | | 2021 | 6 | 4.6 |

*Source: fund documents, Bloomberg, Wells Fargo Advisors*

*Not all funds may be available for purchase at Wells Fargo Advisors*

** Shareholder vote on contingent conversion to an open-end fund during calendar year 2021. If approved, fund will convert within 12 months of such approval. If not approved, fund will continue to operate as a CEF.*

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# Aberdeen Japan Equity Fund, Inc. (JEQ)

July 2017

Authored by:
**Kwok Chern Yeh**
*Head of Investment Management, Japan*
Aberdeen Asset Management

**Has Japan's economy turned a corner?**
Japan has been buoyed by five consecutive quarters of rising gross domestic product (GDP) growth. Depressed oil prices and a revival in global growth have helped drive Japan's current account balance to its highest level for years (see Chart 1). But we remain cautious. There are signs that the U.S. recovery is not improving. This dampens the outlook for Japanese exports further. The threat of trade protectionism lingers. And domestic consumption, which contributes 50-60% of Japan's GDP, is relatively stagnant and wage growth weak. Inflation is thus absent. Labor reforms are needed to drive productivity and counter population decline. Even if recoveries in Europe, China and regional demand continue to support Japan's exports, its economy will be stuck until firms can pass on cost increases to consumers.

**How have companies performed?**
Actually year-end financial results were largely positive. Driven by yen weakness on the back of U.S. reflation expectations and dollar strength, earnings have accelerated and triggered a rise in profitability. Cuts to corporate tax rates combined with domestic labor shortages and a pick-up in global growth have fostered an environment for companies to reinvest in their businesses. We expect this to continue. Retail companies are also investing in IT and logistics. However, this willingness to spend has yet to translate into faster wage growth. What about your other holdings? Broadly, earnings have been resilient. We invest in businesses based on their fundamentals such as sustainable earnings and cash flows, not in those overly reliant on tailwinds.

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# Managing Volatility-Aided Strategies in a Low Volatility Environment

June 26, 2017

Authored by:
**David O'Donohue**
*Vice President, Co-Portfolio Manager*
Calamos Investments

**There has been much publicity lately related to the low volatility market environment. For many investors, a lack of volatility is a comforting feeling. For some of our hedged strategies though, volatility plays an important role in how we manage portfolios and generate returns. This leads to the question "How do we manage volatility-aided strategies in periods of low volatility?"**

First, it is important to separate index volatility from individual stock volatility. Often, when investors think about their investments and the markets, they ask a simple question. "Was the market up or down today?" While people tend to think of "the market" in monolithic terms, it is important to remember that investors are usually thinking of an index (e.g., the S&P 500) that is composed of a number of individual companies—each with unique opportunities and challenges.

Many times, the market will move largely in lockstep based on changing investor sentiment. Sentiment shifts could be led by economic data, political events, or even a presidential tweet. Recently, however, correlation has declined both among sectors and individual equities. This has dampened index volatility, even as some stocks and sectors have continued to experience large moves.

To put it very simply, let's say that on a given day, half the stocks are up and half are down. These moves could cancel each other out and leave "the market" relatively unchanged. Even so, we could have a number of individual stocks with large moves, which could provide many potential gamma trades for our convertible arbitrage strategy. (For more on convertible arbitrage and an overview on gamma trading, read our blog.) An observer reading the paper the next morning may see the unchanged levels in various indices and think that not much has happened. Owners of individual stocks may see things quite differently, however.

Because our convertible arbitrage strategy relies on individual stock volatility rather than index volatility to provide gamma trading opportunities and price dislocations, the reduction in market volatility has had less of an impact on this strategy than it has on our covered call strategy, which relies more on index volatility. In general, we think of our covered call (collared) strategy as short volatility. We generally take in more premium from the calls we sell than we spend on our put protection, and the strategy performs best in a slow-grinding upward market that often coincides with low volatility periods. Therefore, the strategy has tended to work well during the transition phase from a normal volatility environment to a low volatility environment. (Our calls decrease in value while our equities might slowly rise.) However, if low volatility persists once we get past the transition phase, we often adjust our focus.

One of the guiding principles of our market neutral income and hedged equity income strategies is to take advantage of the opportunities the market presents, not the ones we hoped it would present. In normal markets, we are able to generate income from our option hedge as the money we take in selling calls can exceed the money we spend on puts. This becomes challenging or impossible with index volatility at historic lows. That said, any time we find ourselves talking about "historic" levels, there are often opportunities as well.

For strategies like ours that rely on providing downside protection, the opportunity presented in environments like these is clear. Just as the price of the calls we sell is lower, the price of the puts we need to buy is lower too. This allows us to add more hedge through puts than we would normally be able to purchase. Similar to a shopper at a store, with the price of downside protection low, we can afford to stock up. We need to manage the cost of that in conjunction with the decreased income we discussed earlier, but the lower cost can allow us to be more hedged should this period of complacency end with a downside move.

If environments like this persist, we will continue to focus on capturing individual equity volatility in our convertible arbitrage strategy, while aggressively monitoring our option income/spend. Also, as always, we are working to identify and take advantage of opportunities the market presents. Although it may limit our income, a reduced call overwrite combined with increased put protection can leave us positioned favorably whether this current low volatility environment is just a pause before the next leg of a continued bull market or simply the calm before the equity storm.

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# 5 Reasons to Consider Convertible Securities

July 10, 2017

We see a strong case for convertible securities at this point of the market cycle.

1. **Convertible securities have tended to perform well during periods of rising interest rates.** Against a backdrop of improving economic activity, the Federal Reserve has stated its intentions to raise short-term interest rates further. While we do not expect long-term rates to soar over these next quarters, due to overall U.S. economic conditions and accommodative monetary policy globally, we do believe investors should be prepared for a higher interest-rate environment. Because convertible securities have equity characteristics as well as fixed income attributes, they have proven more resilient than non-convertible fixed income securities when interest rates rise.

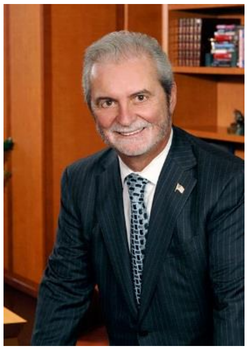
2. **Convertible securities can provide benefits in a period of uncertainty.** In the U.S., partisan tension remains high, calling into question how quickly and to what extent fiscal policy reforms will be enacted. Further, global geopolitical tensions (including those related to Russia and North Korea) may unsettle market participants in the coming months. In turbulent equity markets, convertible securities can provide potential downside protection through their bond characteristics.

3. **Convertible securities can benefit in an environment of longer-term economic growth.** We believe the U.S. is positioned for continued expansion, framed by a larger synchronized global growth story. Fiscal policy implementation has encountered hurdles, but tax reform and less burdensome regulation are not out of reach, which could provide a powerful catalyst to bolster business activity and economic growth.

4. **Convertible securities can provide risk-managed access to growth opportunities.** While we see continued upside in equities, valuations in some areas of the market are elevated. Convertibles offer a way to invest in some of the fastest-growing companies, with downside protection.

5. **We expect a breadth of new opportunities to emerge.** Convertible issuance is about capital market access, which in turn is supported by economic growth. Issuance has been solid through the first half of the year, led by the U.S. We expect continued healthy issuance as companies seek to raise capital for growth projects.

**Active management remains essential for capturing the favorable tailwinds we see for the asset class.** We are drawing on our extensive experience to identify securities that offer not only attractive opportunities for upside equity participation but also an appropriate level of potential downside protection.



Authored by:
**John P. Calamos, Sr.**
*Founder, Chairman and Global CIO*
Calamos Investments

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## Market Videos

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**July 10, 2017**
Bob Carey of First Trust: *Let's Get Back to the Fundamentals*

**July 4, 2017**
Alex Bryan of Morningstar: *2 Favorite ETFs for Foreign Diversification*


**July 6, 2017**
Gemma Acton of CNBC: *Active managers having best year since bull market began*


**June 22, 2017**
Ben Johnson of Morningstar: *MSCI News Has Meaningful, Long-Term Implications*


**July 5, 2017**
Ben Johnson of Morningstar: *News From ETF Land: Record Flows and Quincy Jones*


**June 19, 2017**
Gemma Acton of CNBC: *Activity in the fund management space*

# Energy's Shifting Return Drivers

May 2017

Authored by:
**Maxwell Gold**
*Director – Investment Strategy*
ETF Securities

**Summary**

- Changes in the global oil supply dynamic may likely continue to weigh on the drivers for oil and energy prices.
- The traditional negative relationship between the US Dollar and oil prices has broken down and is currently positive.
- Roll and collateral yields may see further prominence.

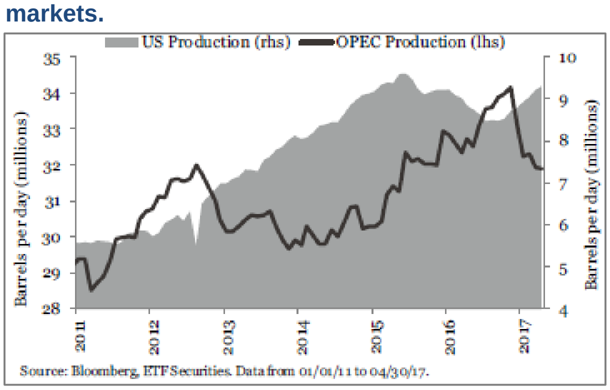
The expected global economic backdrop remains broadly supportive for the energy sector in coming years. Demand for oil remains robust driven by further recovery of global growth accompanied with building inflationary pressures, while efforts to reduce the global supply glut are underway. These changes in supply side fundamentals are beginning to unravel and impact some of the traditional drivers of energy returns including the US dollar (USD), interest rates, and curve structure.

## Fundamentals in Focus

On May 25th the Organization of the Petroleum Exporting Countries (OPEC) agreed to extend production cuts that it initially implemented in November 2016. This 9-month extension, ending March 2018, is a direct response of the changing landscape of global oil supply dynamics.

Since enacting these cuts, OPEC production has dropped from 34 to 32 million barrels per day. OPEC's strategy, however, has resulted in a loss of market share without the commensurate rise in price. The rise of North American shale oil and gas production in recent years has made this region the current swing producer to the global oil market - a trend likely to persist (see Exhibit 1).

**Exhibit 1: The role of US production and supply continues to grow in importance for global energy markets.**

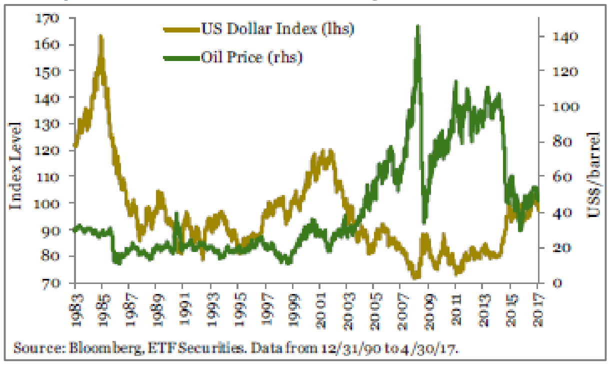



Source: Bloomberg, ETF Securities. Data from 01/01/11 to 04/30/17.

## Changing Dollar Dynamic

The rule of thumb known to many investors is that the US dollar has an inverse relationship with oil and energy prices. This negative relationship was most prominent from 2003 to 2014 (see Exhibit 2). During this period the US current account deficit rose driven by oil imports which boosted oil prices. Concurrently, this led to a large build-up of current account surpluses (held in USD) in oil exporting economies increasing supply of USD reducing its value

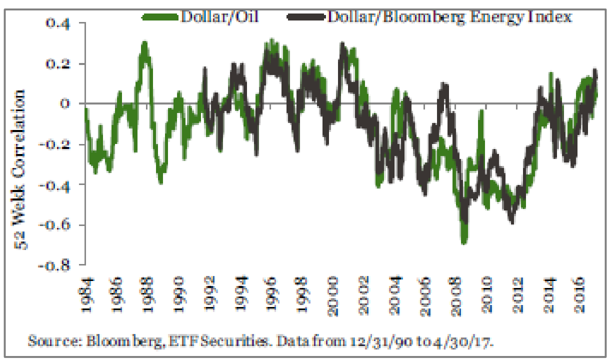
**Exhibit 2: Oil's inverse relationship to the dollar was most prominent from 2003 through 2014**




Source: Bloomberg, ETF Securities. Data from 12/31/90 to 4/30/17.

While oil and USD have a -0.11 correlation since 1983, this traditional relationship has broken down in recent years and is currently positive (see Exhibit 3). This low and positive correlation with USD may likely continue with the dollar's significance as a driver of oil and energy prices becoming more muted in markets.

**Exhibit 3: Oil and USD correlation currently positive.**



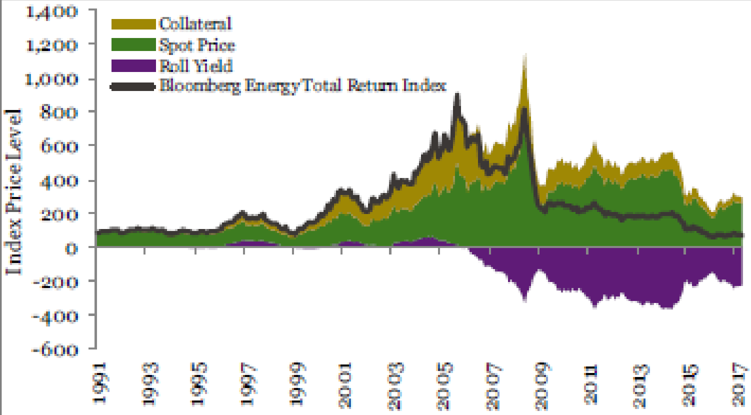

Source: Bloomberg, ETF Securities. Data from 12/31/90 to 4/30/17.

As the US has ramped up its domestic production since 2010, this has increased its energy self-sufficiency. This changing supply dynamic has simultaneously aligned US growth much closer to global energy markets, leading the USD to behave more like traditional commodity currencies. Unlike recent decades, as the US's role as the global swing producer continues, markets will likely see oil markets continue to be driven more by fundamentals.

## A return to backwardation?

Among the three components of total return when investing in futures contracts (price return, roll yield, and collateral yield), the roll yield for the energy sector has been a continuous performance drag over the last decade (see Exhibit 4).

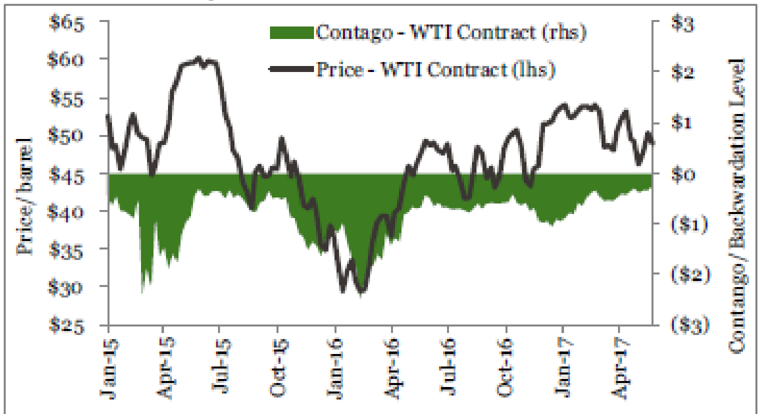
**Exhibit 4: Drag on performance.**




Source: Bloomberg, ETF Securities. Data from 12/31/90 to 4/30/17.

Oil futures markets are most often in a state of contango, whereby the futures price is greater than the spot price. When inventors roll into new contracts at expiration there is an implied cost of buying a more expensive contract, resulting in a negative roll yield component to total return.

**Exhibit 5: Contango in oil markets continues to fall.**




Source: Bloomberg, ETF Securities. Data from 01/01/15 to 05/26/17. WTI = West Texas Intermediate.

Since oil prices bottomed out in early 2016, the degree of contango in futures markets has been reduced. Year to date, the oil market has become even closer to backwardation (see Exhibit 5). If global supply is reduced at a higher rate and oil inventories continue to experience drawdowns, this may push the market towards backwardation thereby bringing roll yield back into focus as a key contributor for oil and energy total returns.

Another component for total returns that has diminished over the last decade is collateral yield. In the current low interest rate, the yield garnered from holding collateral against futures contracts has been minimal. This may see a bit of a reprieve against expectations of further tightening by the Federal Reserve this year. Additionally nominal interest rates are a key driver for energy commodity prices and a rising rate environment may be met with higher prices. Crude oil and gasoline perform positively on average in rising rate environments while natural gas tends to benefit from falling market interest rates (see Exhibit 6).

**Exhibit 6: Rising rates may boost oil and energy prices.**

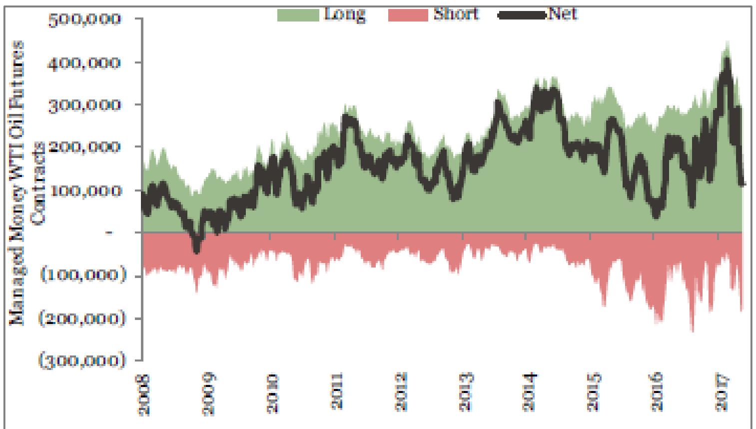
| Monthly Price Returns (01/31/91 to 4/30/17) | Rising Interest Rates | Falling Interest Rates | Average |
|---|---|---|---|
| Energy Sector | 0.7% | 0.7% | 0.7% |
| WTI Crude | 1.4% | -0.1% | 0.7% |
| Brent Crude | 1.6% | -0.3% | 0.7% |
| Gasoline | 3.5% | -2.5% | 0.6% |
| Natural Gas | -1.2% | 4.0% | 1.4% |
| Heating Oil | 1.0% | 0.4% | 0.7% |

Source: Bloomberg, ETF Securities. Data from 01/31/91 to 04/30/17. Energy sector is represented by the Bloomberg Energy Spot Subindex.

## Outlook: Crude Oil

OPEC's decision to extend its production cuts through March 2018 was met with disappointment in markets. While this is a positive sign for the global crude market which continues to rebalance from a multi-year supply glut, expectations of continued US productions will remain in focus. There have been encouraging signs in recent weeks of US inventory drawdowns which if sustained could support current price levels. Additionally, OPEC has had a poor track record in keeping compliance to its stated quotas. Lack of follow through on this extended deal by OPEC members may weigh negatively on prices.With continued tightening fundamentals and reduced investor sentiment (see Exhibit 7), we expect prices to range from $40-55/barrel this year.

**Exhibit 7: Oil positioning has unwound recent highs.**




Source: Bloomberg, ETF Securities. Chart data from 1/1/08 to 5/16/17.

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# Which Market Shocks Matter for Metals?

June 2017

Authored by:
**Maxwell Gold**
*Director – Investment Strategy*
ETF Securities

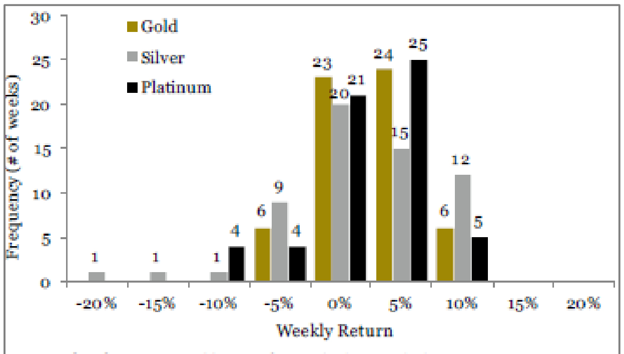

## Summary

• Heightened equity volatility historically benefits gold and platinum, while equity drawdowns favor gold and silver.
• Positive oil shocks tend to boost all precious metals while platinum has had the least sensitivity to extreme price drops.
• Shifts in reserve currencies may drag on precious metals, but shocks from emerging market currencies may be limited.


## Equity shocks

On June 2nd, the Chicago Board Options Exchange Volatility Index (VIX) closed at 9.75, hitting a 23 year low. This low volatility environment has raised concern among investors about a potential mean reversion leading to a spike in volatility. Given precious metals' low correlation to equities historically, many support the view that they should serve as significant hedges against a spike in equity volatility. Based on the data, however, this may not be the proper way of gauging their relationship to equities, particularly during very short-term equity movements (see Exhibit 1).

**Exhibit 1: Extreme VIX levels benefit gold and platinum**




Source: Bloomberg, ETF Securities. Data from 03/30/90 to 06/16/17.

When evaluating the VIX Index, there have been 59 trading weeks since its inception in 1990 where it experienced elevated levels (weekly moves exceeding 2 standard deviations). These periods of elevated volatility on average have favored gold and platinum, with median weekly returns of 0.5% and 0.2% respectively and broadly even performance distributions. Silver's track record to extreme VIX moves, on the other hand appears to be negatively skewed. Silver has also suffered significant pullbacks of 10% or more, albeit infrequently. This makes sense given silver's high sensitivity to industrial demand as well as it historically higher volatility (27%) compared to gold (16%) and platinum (21%).

**Exhibit 2: Equity drawdowns tend to favor gold and silver**

| Total Return | Gold | Silver | Platinum | S&P 500 |
|---|---|---|---|---|
| 8/28/08 - 03/09/09 | 10.5% | -5.0% | -28.2% | -47.1% |
| 8/25/87 - 12/04/87* | 8.4% | -11.8% | -14.5% | -33.5% |
| 3/19/02 - 07/23/02 | 6.8% | 7.0% | 0.3% | -31.5% |
| 9/29/00 - 04/04/01 | -5.8% | -10.5% | 1.3% | -22.7% |
| 7/16/90 - 10/11/90 | 6.8% | -10.8% | -6.4% | -19.2% |
| 7/17/98 - 08/31/98 | -6.4% | -12.7% | -10.1% | -19.2% |
| 7/07/11 - 10/03/11 | 8.2% | -16.6% | -13.5% | -18.4% |
| 10/09/07 - 03/10/08 | 31.8% | 45.8% | 48.0% | -17.9% |
| 8/24/01 - 09/21/01 | 6.8% | 9.4% | 5.9% | -18.4% |
| 4/23/10 - 07/02/10 | 4.7% | -2.6% | -13.8% | -15.6% |
| Average | 7.2% | -0.8% | -3.1% | -24.4% |

Source: Bloomberg, ETF Securities. Data: 8/25/87 to 10/3/11. * S&P 500 price return.

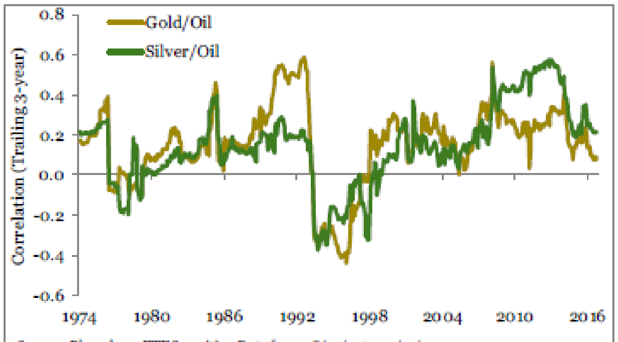
The effectiveness of precious metals during equity swings becomes more clear when evaluating sustained sell offs in equity markets as opposed to individual trading weeks of extreme volatility.

When the S&P 500 suffered a peak to trough drawdown of 15% or more since 1987, precious metals helped limit the downside capture. Gold is the clear benefactor averaging a return of +7.2% and posting positive returns in 8 of the 10 events. Silver, on average, acted as source of downside protection better than platinum, while both outperformed the average S&P 500 return of negative 24.4% (see Exhibit 2).

## Oil shocks

Over time, precious metals have exhibited a positive relationship to oil prices (see Exhibit 3). When evaluating shorter term periods, this relationship still holds, but with varying results depending on the specific metal and size of the oil price shock.

**Exhibit 3: On average metals correlate positively with oil**

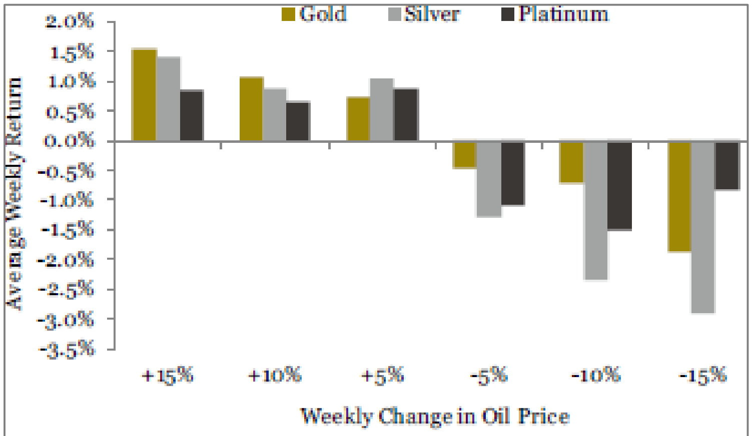



Source: Bloomberg, ETF Securities. Data from 08/31/74 to 05/31/17.

In evaluating weekly oil price swings, there have been 69 weeks since 1987 that exhibited at least 2 standard deviation move from the average move. As shown in

Exhibit 4, gold tends to be the top performer for larger increases of oil prices of 10% or more followed by silver and then platinum. However, for more moderate positive oil shocks (+5%), silver outpaced gold and platinum.

**Exhibit 4: Platinum shines for largest oil shocks.**




Source: Bloomberg, ETF Securities. Data from 01/09/87 to 06/16/17.

Additionally for weekly oil returns of 5% or 10%, gold offers an asymmetrical capture to oil price moves. This means that gold's upside movement for positive oil shocks is greater than its downside movement for negative oil shocks of a similar degree.

When the oil price drops rapidly, gold and platinum have provided a better hedge to oil price volatility than silver. Platinum, however, significantly outperforms both gold and silver during the largest weekly oil price drops on average. This may stem from the fact that a large part of platinum demand is tied to auto sales and with a fall of 15% or more in oil prices, this may boost market expectations of future auto sales spurred by a lower oil price environment.

### Currency shocks

Another source of short term market shocks is driven by currency volatility. By evaluating long term correlations between precious metals and currencies, investors may gain some insight into how shocks to these currencies may impact each metal. Turning to major reserve currencies, the behavior of the precious metals complex is fairly uniform. The US Dollar, Swiss Franc, and Japanese Yen (which are often in demand during periods of flight to quality amid market turmoil) exhibit negative correlations. Conversely the Euro and British Pound tend to exhibit positive correlations to precious metals (see Exhibit 5).

**Exhibit 5: Shocks to reserve assets may impact metals.**

| Correlation | Gold | Silver | Platinum | Palladium |
|---|---|---|---|---|
| US Dollar | (0.43) | (0.39) | (0.28) | (0.18) |
| Swiss Franc | (0.39) | (0.33) | (0.21) | (0.11) |
| Japanese Yen | (0.26) | (0.15) | (0.12) | (0.02) |
| Euro | 0.40 | 0.35 | 0.25 | 0.16 |
| British Pound | 0.30 | 0.29 | 0.19 | 0.13 |

Source: Bloomberg, ETF Securities. Data from 11/5/93 to 6/16/17.

For emerging market (EM) currencies, the sensitivity is broadly negatively correlated but more limited compared to reserve currencies. Therefore shocks to these currencies may be more limited to metals prices. Free floating EM currencies that are highly levered to the precious metal markets (such as India for jewelry demand and South Africa for mine supply), however, appear to be exceptions with higher negative correlations (see Exhibit 6).

**Exhibit 6: Metals are less sensitive to EM currency moves.**

| Correlation | Gold | Silver | Platinum | Palladium |
|---|---|---|---|---|
| Brazilian Real | (0.12) | (0.19) | (0.15) | (0.14) |
| Russian Ruble | (0.10) | (0.12) | (0.12) | (0.10) |
| Indian Rupee | (0.20) | (0.28) | (0.26) | (0.22) |
| Chinese Yuan | (0.03) | (0.03) | (0.03) | (0.00) |
| S. African Rand | (0.28) | (0.32) | (0.22) | (0.19) |

Source: Bloomberg, ETF Securities. Data from 11/5/93 to 6/16/17.

### Portfolio Strategy

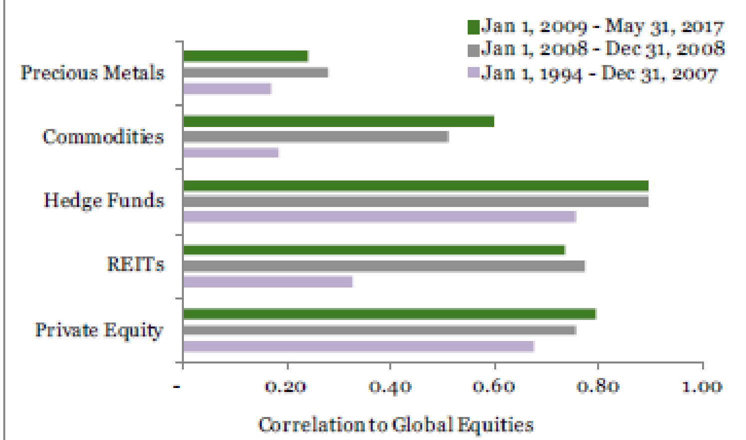
A key benefit from investing in precious metals lies within its distinct role as a core risk management tool. Precious metals wear many hats on the risk management front and thereby may serve as a dynamic and multi-faceted hedge against many forms of risk.

This role as a risk management tool may be useful particularly for long term investors seeking to continually hedge against a broad spectrum of both known and unknown risks.

Precious metals have historically shown low correlations with most asset classes, particularly equities. Over the past two decades, precious metals have carried lower correlations to both US and global equities than other alternative investments (see Exhibit 7).

**Exhibit 7: Precious metals remain a true alternative.**

Exhibit 7: Precious metals remain a true alternative.



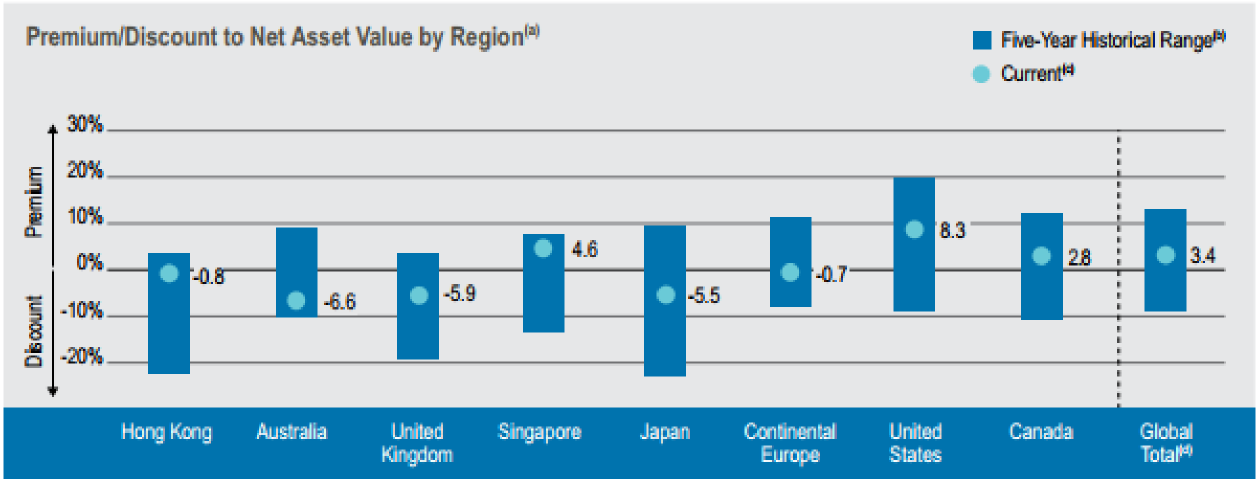

Source: Bloomberg, ETF Securities. Precious metals = ETFS Physical Precious Metals Basket Index, Global equities = MSCI World Index, US equities = S&P 500, commodities = Bloomberg Commodity Index, hedge funds = HFRI Fund Weighted Index, REITs (Real Estate Investment Trusts) = FTSE NAREIT All Equity REITs Total Return Index, Private Equity = LPX50 Index. Chart data from 12/31/93 – 05/31/17. See disclosures for further details.

Click here for complete reading

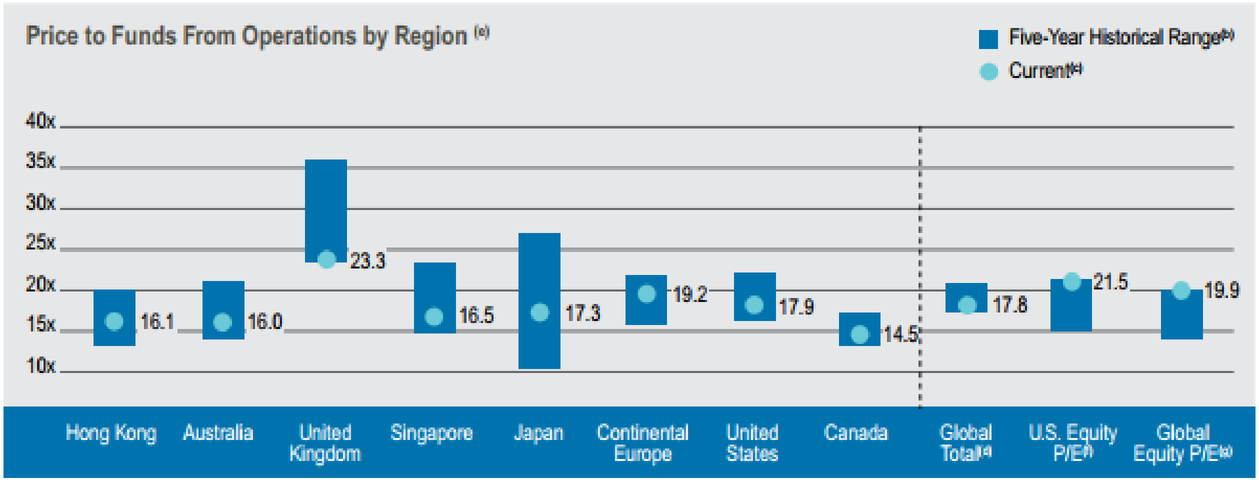
# Global Real Estate Securities Valuations Present Potential Opportunity

May 2017

**Global real estate securities are trading towards the middle of their five-year historical range relative to their underlying property assets (upper chart) and towards the bottom relative to cash flows (lower chart). We believe this is appropriate considering the steady growth of the global economy, modest new supply and still historically low financing costs. When compared to broad equities—which are trading at the top of their five-year P/E range in the U.S. and globally—we believe global real estate securities represent an attractive opportunity.**




Net asset value (NAV) is the real estate security equivalent of book value, representing the estimated market value of a company's property assets, less any liabilities. On average, global real estate companies are trading at premiums to NAV representing the ability of management to add value over and above a property's income.




Price-to-funds from operations (P/FFO) is the global real estate security equivalent of the price-to-earnings (P/E) ratio—essentially measuring a real estate company's valuation in terms of its recurring income and any appreciation in property values. The P/FFO ratio roughly indicates the market's expectations for real estate security cash flow growth.

**At June 30, 2017.** Source: Cohen & Steers estimates based on proprietary qualitative and quantitative metrics. Only major REIT sectors are shown individually.

**Data quoted represents past performance, which is no guarantee of future results.** The information presented above does not reflect the performance of any fund or account managed or serviced by Cohen & Steers, and there is no guarantee that investors will experience the type of performance reflected above. There is no guarantee that any historical trend illustrated above will be repeated in the future, and there is no way to predict precisely when such a trend might begin. An investor cannot invest directly in an index and index performance does not reflect the deduction of any fees, expenses or taxes.

(a) NAV (Net Asset Value) seeks to calculate the net market value of all of a company's assets after subtracting liabilities. (b) The 5-Year Historical Range begins on 7/31/2012 and ends on 6/30/2017. The range was calculated using Cohen & Steers' valuation metrics and is based on the FTSE EPRA/NAREIT Developed Real Estate Index—net at the end of each month. (c) Current numbers were calculated using Cohen & Steers' valuation metrics and are based on securities that are in Cohen & Steers' coverage universe which represents a 97% overlap with securities included in the FTSE EPRA/NAREIT Developed Real Estate Index. Certain companies in sectors, such as infrastructure, are covered by Cohen & Steers but are not in the FTSE EPRA/NAREIT Developed Real Estate Index - net. The FTSE EPRA/NAREIT Developed Real Estate Index is an unmanaged market-weighted total return index which consists of many companies from developed markets who derive more than half of their revenue from property-related activities. (d) Global Total represents the weighted average of all REIT sectors. (e) (FFO) Funds from operations is the REIT industry's key earnings metric. It is calculated as GAAP net income, plus real estate gains (minus real estate losses), plus GAAP real estate depreciation and amortization. (f) U.S. Equity represents the weighted harmonic average P/E multiple based on the S&P 500 Index. The S&P 500 Index is an unmanaged index of 500 large-capitalization stocks that is frequently used as a general measure of U.S. stock market performance. (g) Global Equity represents the weighted harmonic average P/E multiple based on the MSCI World Index. The MSCI World Index - net is a free-float-adjusted index that measures performance of large- and mid-capitalization companies representing developed market countries and is net of dividend withholding taxes.

### The Added Value of Active Portfolio Management

We believe that investing in global real estate securities with an experienced active manager offers several important advantages over passively managed investments such as exchange-traded funds (ETFs). Here are a few reasons why:

**Different real estate securities are better suited for different phases of an economic cycle.** Certain real estate securities may be more or less cyclical than others, depending largely on the duration of their leases, which can range from a single day (hotels) to a decade or more (hospitals). An active manager can adjust a portfolio's allocation depending on their economic outlook in an effort to enhance absolute returns over full market cycles.

**Differences in country valuations provide opportunities for global investors.** Some global real estate companies trade at discounts to the estimated net asset value (NAV) of their underlying holdings, while others trade at a premium to NAV. Finding value is the foundation of active portfolio management, which we believe is the best way to invest in real estate markets worldwide.

**Flexibility among market capitalizations.** ETFs are typically weighted by market cap, meaning that large-cap REITs will dominate the portfolio's holdings. By contrast, an active manager can increase allocations to select small-cap real estate securities that may offer greater growth potential.

**The importance of fundamental analysis.** Returns often vary widely among regions, sectors and individual companies. As a global active manager, Cohen & Steers conducts extensive research on each company, evaluating its management team, its acquisition and development strategy, the quality of its properties, and the strength of its balance sheet, using these inputs to assess the stock's value relative to its peers.

**Cohen & Steers' actively managed real estate securities solutions**

| Open-End Mutual Funds | | |
|---|---|---|
| Cohen & Steers Global Realty Shares | CSFAX—Class A<br>CSFCX—Class C<br>CSSPX—Class I<br>GRSRX—Class R<br>CSFZX—Class Z | Global |
| Cohen & Steers Institutional Global Realty Shares | GRSIX—Institutional | Global |
| Cohen & Steers International Realty Fund | IRFAX—Class A<br>IRFCX—Class C<br>IRFIX—Class I<br>IRFRX—Class R<br>IRFZX—Class Z | Global (ex. U.S.) |
| Cohen & Steers Realty Shares | CSRSX—no load | U.S. |
| Cohen & Steers Real Estate Securities Fund | CSEIX—Class A<br>CSCIX—Class C<br>CREFX—Class F<br>CSDIX—Class I<br>CIRRX—Class R<br>CSZIX—Class Z | U.S. |
| Cohen & Steers Institutional Realty Shares | CSRIX—Institutional | U.S. |

Cohen & Steers open-end funds are distributed by Cohen & Steers Securities, LLC.

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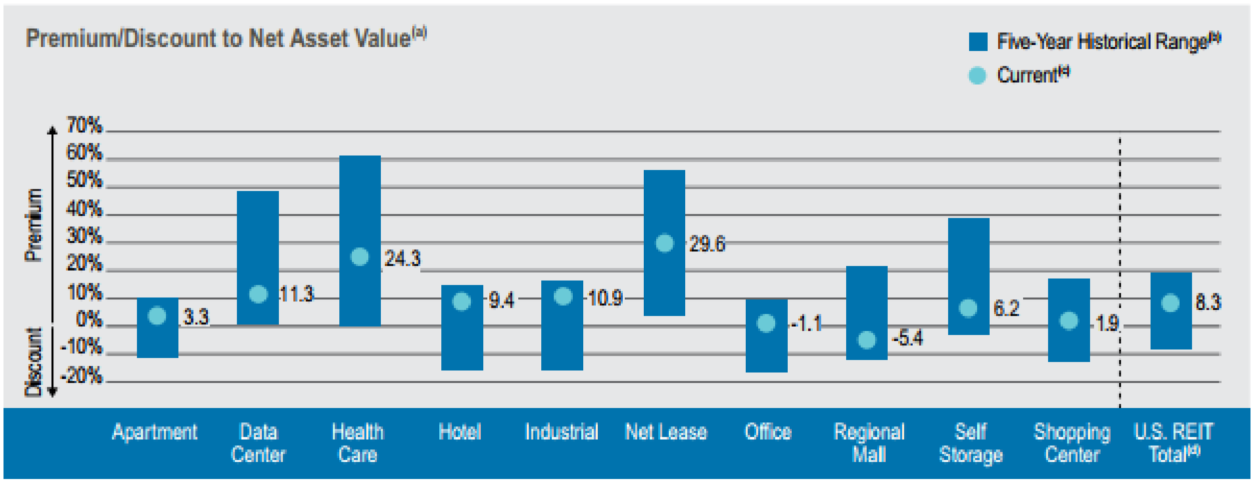
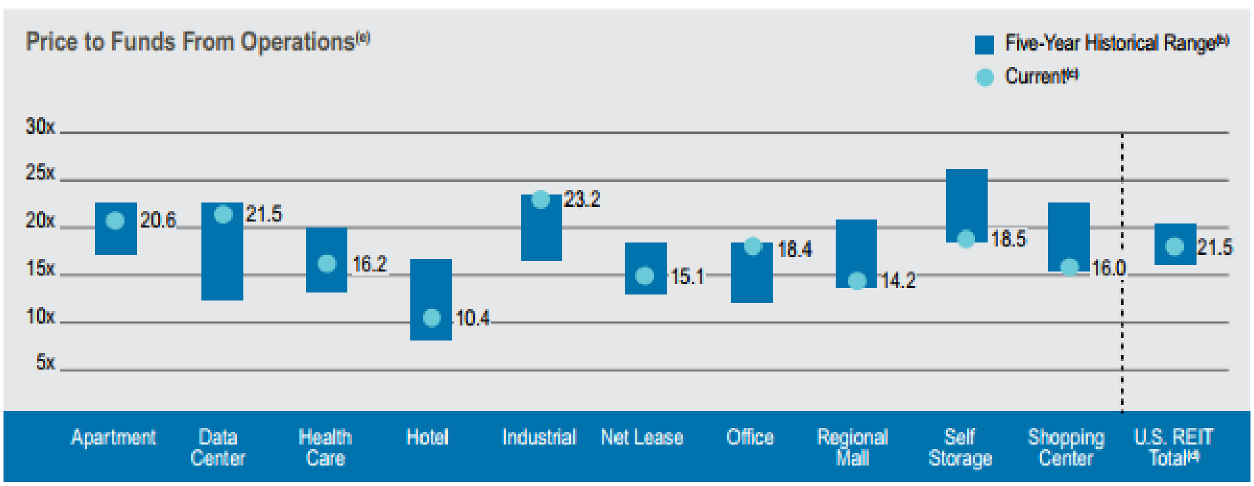
# U.S. REITs Valuations Reflect Prospective Growth

June 2017

**U.S. REITs are trading towards the middle of their five-year historical range relative to their underlying property assets (upper chart) and to cash flows (lower chart). We believe this is appropriate considering the steady growth of the U.S. economy, modest new supply and still historically low financing costs. For investors looking to boost their income and broaden their diversification, we believe REITs represent an attractive opportunity.**




Net asset value (NAV) is the REIT equivalent of book value, representing the estimated market value of a company's property assets, less any liabilities. U.S. REITs have historically traded at premiums to NAV due to the ability of management to add value over and above a property's income.




Price-to-funds from operations (P/FFO) is the REIT equivalent of the price-to-earnings (P/E) ratio—essentially measuring a REIT's valuation in terms of its recurring income and any appreciation in property values. The P/FFO ratio roughly indicates the market's expectations for REIT cash flow growth.

**At June 30, 2017.** Source: Cohen & Steers estimates based on proprietary qualitative and quantitative metrics. Only major REIT sectors are shown individually.

**Data quoted represents past performance, which is no guarantee of future results.** The information presented above does not reflect the performance of any fund or account managed or serviced by Cohen & Steers, and there is no guarantee that investors will experience the type of performance reflected above. There is no guarantee that any historical trend illustrated above will be repeated in the future, and there is no way to predict precisely when such a trend might begin.

(a) NAV (net asset value) seeks to calculate the net market value of all of a company's assets after subtracting liabilities. (b) The five-year range begins on 7/31/12 and ends on 6/30/17, calculated using Cohen & Steers' valuation metrics and is based on the FTSE NAREIT Equity REIT Index at the end of each month. (c) Current numbers were calculated using Cohen & Steers' valuation metrics and are based on securities that are in Cohen & Steers' coverage universe which represents a 98% overlap with securities included in the FTSE NAREIT Equity REIT Index. Certain companies in sectors, such as infrastructure, are covered by Cohen & Steers but are not in the FTSE NAREIT Equity REIT Index. The FTSE NAREIT Equity REIT Index contains all tax-qualified REITs except timber and infrastructure REITs with more than 50% of total assets in qualifying real estate assets other than mortgages secured by real property that also meet minimum size and liquidity criteria. An investor cannot invest directly in an index and index performance does not reflect the deduction of any fees, expenses or taxes. (d) U.S. REIT Total represents the weighted average of all REIT sectors. (e) Funds from operations is the REIT industry's key earnings metric, calculated as GAAP net income, plus real estate gains (minus real estate losses), plus GAAP real estate depreciation and amortization.

### The Added Value of Active Portfolio Management

We believe that investing in U.S. REITs with an experienced active manager offers several important advantages over passively managed investments such as exchange-traded funds (ETFs). Here are a few reasons why:

**Different REITs are better suited for different phases of an economic cycle.** Certain REITs may be more or less cyclical than others, depending largely on the duration of their leases, which can range from a single day (hotels) to a decade or more (hospitals). An active manager can adjust a portfolio's allocation depending on their economic outlook in an effort to enhance absolute returns over full market cycles.

**Flexibility among market capitalizations.** ETFs are typically weighted by market cap, meaning that large-cap REITs will dominate the portfolio's holdings. By contrast, an active manager can increase allocations to select small-cap REITs that may offer greater growth potential.

**Finding opportunities through fundamental company analysis.** An active manager may conduct extensive research of each company, evaluating its management team, its acquisition and development strategy, the quality of its properties, and the strength of its balance sheet, using these inputs to assess the stock's value relative to its peers.

**Cohen & Steers' actively managed U.S. REIT solutions**

| Open-End Mutual Funds | | |
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| Cohen & Steers Institutional Realty Shares | CSRIX—Institutional | |

Cohen & Steers open-end funds are distributed by Cohen & Steers Securities, LLC.

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# Alternatives Update - 2nd Quarter 2017

July 20, 2017

The capital markets continually offer up uncertainty and confusion. A "Chekov's gun" mindset to market analysis will likely result in terabytes of data mining, great mental anguish, but perhaps little else. Rarely do any markets follow the careful sequencing of a well-crafted spy novel or a tightly written screenplay. In fact, it might be said that the incoherent jumbled mess of a Michael Bay directed movie is logical and cohesive by comparison. As a tangent, the current administration and both political parties seem to be giving Michael Bay a serious run for his money. Fortunately for investors, the markets appear to be ignoring both domestic and global political dysfunction. Despite all the noise, a couple of clear themes emerged in the second quarter: For risk assets, any news was good news, and there has been a shift in messaging from the Federal Open Market Committee (FOMC).

Second quarter returns for traditional assets were strong across the board with global equity markets continuing to dominate (see Figure 1). Carrying on the theme that has been in place since the start of quantitative easing, equity or credit of most varieties proved to be rewarding. Despite the FOMC raising rates and signaling more to come, long dated treasuries rallied strongly, outpacing the S&P 500.Two of the more popular explanations for the flattening are: The bond market is telling the FOMC that they should not be raising rates at this juncture and the talk of several more rate moves and balance sheet unwinding is just that,talk.

Alternative Investment ("Alternatives") returns were modest by comparison to traditional long only risk assets. For the quarter, 7 of the 11 alternative categories had positive returns. Real estate was the best performing category and Commodities the worst (see Figure 2). As in the recent past, exposure to equity beta seems to have been a major driver of returns. As was the case for most of 2016 and the first quarter of 2017, returns mostly aligned with the rank order correlation to the S&P 500 (see Figure 3). Real assets (commodities, real estate, gold), struggled in the second quarter realizing an average return of -0.34%, with only real estate ending in the black. Given that first quarter returns for real estate and gold were nearly equal to or greater than their total returns for all of 2016, it is not clear if this is a manifestation of lower inflation expectations or simply a pause following outsized returns. Commodities, after a strong 2016, posted another negative return quarter, -3.0% (see Figure 4).

Managed Futures, commodities, and macro strategies have historically shown low correlations and beta to stocks and bonds, thus they serve as potentially strong portfolio diversifiers. Strategies such as credit, event driven, hedge equity, et al., which have higher correlations with equities and bonds, provide attractive risk/return profiles through lower volatility. These characteristics may allow investors to broaden their investment choices and create more efficient portfolios.

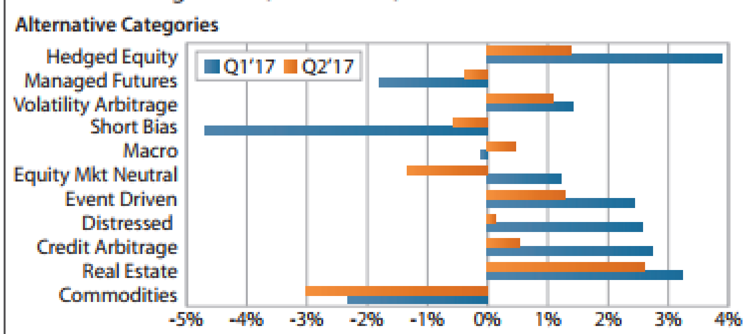
The U.S. political dynamics continue to provide fodder for late night talk shows, but for the average American, the waning prospect of meaningful healthcare reform, tax reform, and regulatory curtailment is no laughing matter. While those central tenets of the Trump platform gave hope to the markets after last year's election, their dimming prospects do not appear to be impacting capital markets in a symmetric fashion to the downside. Second quarter earnings growth for U.S. stocks and U.S. employment data were bright spots, while global growth and inflation/deflation concerns remain sizable question marks. Most markets seemed willing to ignore the negatives and seize firmly on the positives.

**Figure 1: Asset Class Returns**

| | 2Q17 |
|---|---|
| S&P 500 | 3.09% |
| MSCI EAFE | 6.12% |
| MSCI Emerging | 6.27% |
| U.S. Treasury | 4.18% |
| Real Estate | 2.59% |
| Commodities | -3.00% |
| Bloomberg Barclays High Yield | 2.20% |
| Bloomberg Barclays Aggregate | 1.45% |

*Source: Bloomberg, 6/30/17. Past performance is no guarantee of future results. An investor cannot invest directly in an index.*

**Figure 2: Q1'17 and Q2'17 Performance**




*Source: Bloomberg, 6/30/17. Past performance is no guarantee of future results. An investor cannot invest directly in an index.*

**Figure 3: Correlations (2-Year) & Returns**

| | S&P 500 | 2Q17 |
|---|---|---|
| Hedged Equity | 0.88 | 1.39% |
| Event Driven | 0.78 | 1.27% |
| Real Estate | 0.74 | 2.59% |
| Distressed | 0.61 | 0.13% |
| Credit Arbitrage | 0.58 | 0.53% |
| Equity Market Neutral | 0.56 | 1.10% |
| Volatility Arbitrage | 0.5 | -1.32% |
| Macro | 0.18 | 0.45% |
| Commodities | 0.09 | -3.00% |
| Managed Futures | -0.06 | -0.36% |
| Short Bias | -0.7 | -0.56% |

*Source: Bloomberg, 6/30/17. Past performance is no guarantee of future results. An investor cannot invest directly in an index.*

U.S. equity volatility (as measured by the VIX Index) remained suppressed,
touching a low of 9.75 before ending the quarter at 11.18 (see Figure 5). In our 2017 first quarter commentary, we noted that "The average

daily VIX level in the first quarter (11.69) was the second lowest reading since the creation of the VIX Index." That is no longer true, as the average daily VIX level in the most recent quarter is now the second lowest reading since the creation of the VIX index (see Figure 6). To further gain perspective on just how low equity volatility was in the second quarter, it is instructive to look at the extreme percentiles. Sorting all daily VIX closing levels since inception and then examining the lowest 1%, one will find the greatest number (27) occurred in 2017 (and the year is only half over). All 27 instances were in the second quarter. The next largest cluster of readings in the lowest 1% tallied 17. Of some concern is that all 17 of those instances occurred in the first two months of 2007, right before the collapse in the Shanghai composite and the onset of the subprime crisis (see Figure 7). Credit spreads tightened slightly 16 basis points (bps) as money continued to seek out yield, though with rates at extremely low absolute levels, further tightening may be limited (see Figure 8).

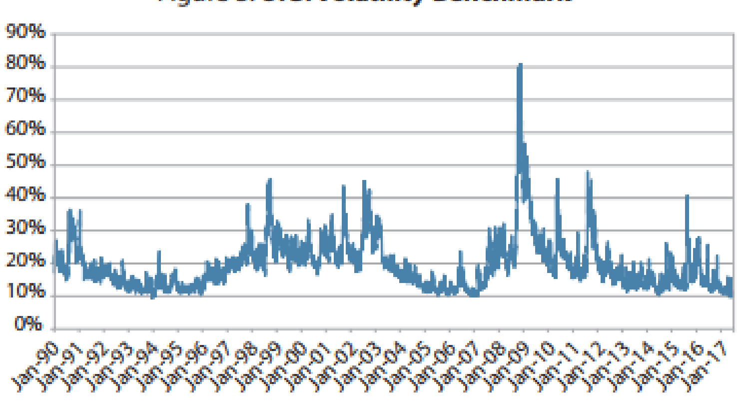
Figure 4: **Real Assets**

| | 2Q17 | 1Q17 | 2016 |
|---|---|---|---|
| Real Estate | 2.59% | 7.56% | 5.89% |
| Commodities | -3.00% | -2.33% | 11.77% |
| Gold | -0.62% | 8.43% | 8.56% |
| ***Average*** | ***-0.34%*** | ***4.55%*** | ***8.74%*** |

*Source: Bloomberg, 6/30/17. Past performance is no guarantee of future results. An investor cannot invest directly in an index.*

The ratio of New Highs to New Lows for the NYSE and for the NASDAQ ticked down in the quarter continuing a medium-term trend begun in late 2016, possibly reflecting the narrowing of leadership (see Figure 9). Comparing absolute levels across a lengthier history does not indicate sentiment being a concern at the moment (see Figure 10).

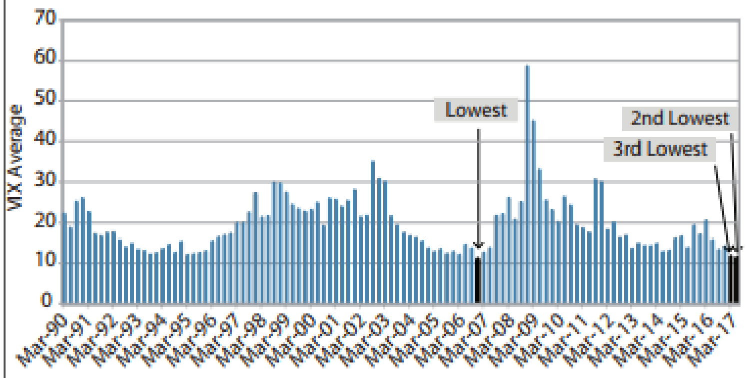
Figure 5: **U. S. Volatility Benchmark**



*Source: Bloomberg, 6/30/17.*

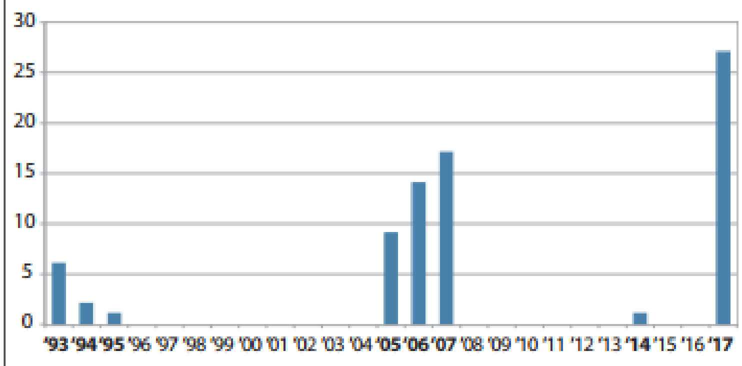
The FOMC raised rates 25bps at the June 14, 2017 meeting citing positive labor markets, recent inflation readings near the target level of 2% but potentially climbing, and monetary policy as continuing to be accommodative. Previously, language from the FOMC had implied that balance sheet reduction was far in the future. The June meeting initiated a departure from this narrative. A plan to start shrinking the balance sheet was not only mentioned, but the FOMC issued a reasonably detailed map in its "Addendum to Policy Normalization Principles and Plans." While the Addendum made it clear that balance sheet downsizing would be measured and possibly modified at the first sign of disturbance to the economy, the change in tone from "dovish at all costs" was clear.

Figure 6: **Daily VIX Level - Quarterly Average**



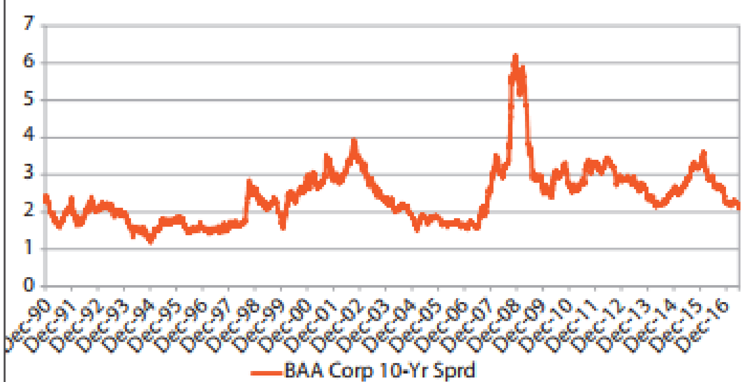

*Source: Bloomberg, 6/30/17*

Figure 7: **# of Daily VIX Closings in Lowest 1%**



*Source: Bloomberg, 6/30/17.*

Figure 8: **Credit Spread vs. 10-Year U.S. Treasury**

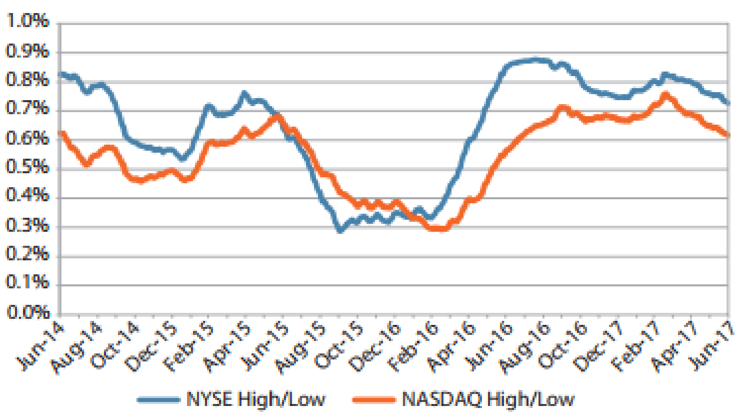



*Source: Bloomberg, 6/30/17.*

The long end of the Treasury yield curve, which had been mostly unchanged starting the second quarter, rose slightly in the first week of May before turning sharply lower.A yield of 2.70% was reached on June 26, before drifting higher and ending at 2.835% as of June 30, 2017, 17.5bps below yields at the start of the quarter (see Figure 11). Since December of 2015,the Treasury curve hasflattened just over 105bps,with the bulk of the movement coming on the short end.

It was a good quarter for "Risk On" (+2.35%) and passable for "Risk Off" assets (+1.78%), with Gold and the Japanese Yen being exceptions, (see Figure 12). There was no clear rotation to one side or the other but more a reshuffling of allocations. We continue to emphasize that Alternatives have historically provided significant diversification benefits when paired with a portfolio of traditional assets, in addition to both competitive absolute returns and attractive risk-adjusted returns.

Figure 9: **New Highs/New Lows** *(90-Day Rolling Average)*

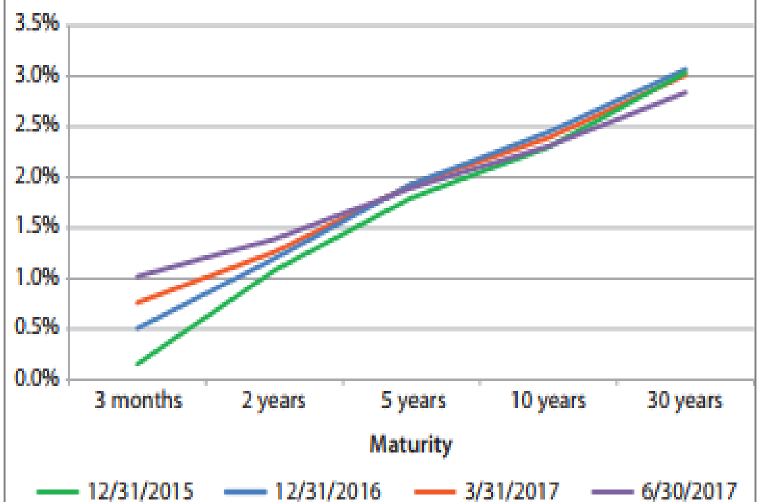



*Source: Bloomberg, 6/30/17.*

Figure 10: **U.S. 30-Yr. Treasury Yield**

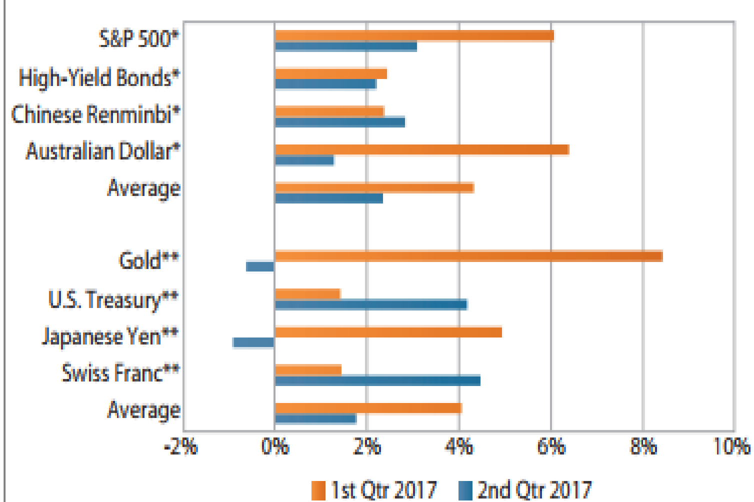

*Source: Bloomberg, 6/30/17.*

Figure 11: **U.S. Treasury Yield Curve**




*Source: Bloomberg, 6/30/17.*

Figure 12: **Risk Off vs. Risk On Asset Returns**




*Source: Bloomberg, 6/30/17.*
**Considered to be "Risk On" asset class. **Considered to be "Risk Off" asset class.*

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# Senior Loan & High Yield Review – 2nd Quarter 2017

July 18, 2017

Authored by:
**William Housey, CFA**
*Senior Vice President, Senior Portfolio Manager*
First Trust Advisors

### Macro Overview

Equities posted a strong second quarter of 2017, with the S&P 500 Index up 3.09%. Equity market volatility remained subdued, despite weaker oil prices, while interest rates declined for much of the quarter. Crude oil fell from an intra-quarter high of $53.40 to $42.53 near the end of the quarter while the 10-year U.S. Treasury yield touched 2.414% in May and drifted to 2.126% by mid-June, eventually finishing the quarter at 2.304%. Declining yields were a boon to fixed-income, with investment grade corporate bonds up 2.42% and high-yield bonds up 2.14% for the quarter. Moreover,the yield-curve flattened significantly in the quarter, with the difference between 2-year U.S. Treasuries and 10-year U.S. Treasuries falling to a mere 79 basis points (bps) in mid-June from 113 bps on March 31, 2017. In our opinion, the primary catalyst for lower rates and a flattening yield curve was a building narrative around weaker inflation data in the U.S. and a view that the Trump Administration's pro-growth policies may be far more difficult to implement than previously anticipated.

*Exhibit 1* – U.S. High-Yield Bond Performance: 1997 – 2Q 2017

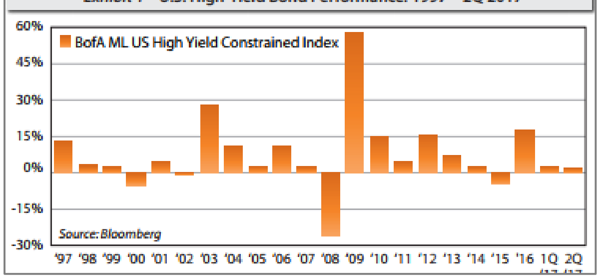
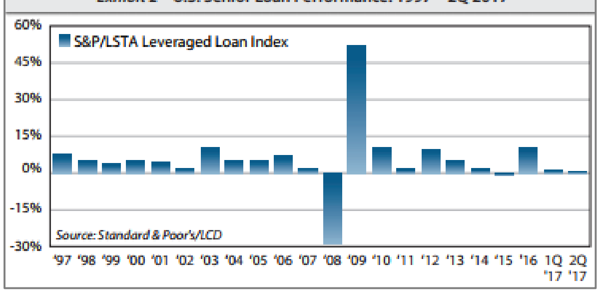
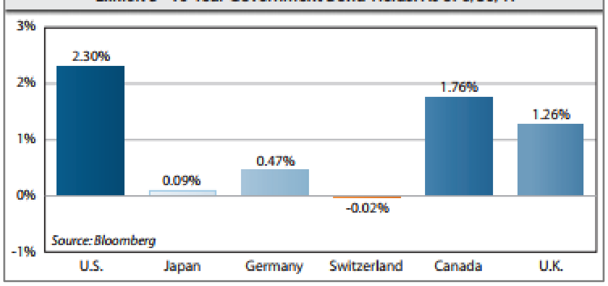



*Exhibit 2* – U.S. Senior Loan Performance: 1997 – 2Q 2017




We believe there are a number of potential interest rate catalysts on the horizon. First, the narrative from the Federal Reserve (Fed) has been that short-term rates will continue to increase while we're likely to see a formal decision to begin slowing the reinvestment on the Fed balance sheet before year-end. Taken in isolation, we believe that the gradual reduction in the Fed's balance sheet should send interest rates higher, or, at the very least, introduce greater volatility into the bond market. Second, while wage growth has been slow to materialize, despite incredibly healthy jobless rates, we may finally be entering the phase of the expansion where commodity prices begin to increase. In the wake of the recent weakness in the dollar, we believe commodity prices may begin to improve in the second half of 2017, which would ultimately flow through to inflation data. Many agricultural commodity prices bottomed toward the later half of June and already began to move higher by quarter-end. Finally, we believe that we are likely to see tapering of the Quantitative Easing (QE) program underway via the European Central Bank (ECB) in the second half of 2017. In December, Mario Draghi, President of the ECB, announced a covert tapering whereby he trimmed monthly bond purchases from 80 billion euros to 60 billion euros, but extended the length of time in which QE would be in force. The market interpreted this as additional stimulus, however, we believe this sets the table for an additional cut to the ECB's QE program later this year. Moreover, Draghi commented in June that signs are pointing to a strengthening and broadening recovery in the euro area. While he also suggested that the continued stimulus remains needed, we believe the recognition of the improved trends suggests that the ECB is contemplating how and when to begin pulling back their stimulus. We believe that when the ECB does in fact begin to taper its QE, that it will lead to higher interest rates in Europe and such a move would likely carry through to the U.S. given the high correlation between German Bunds and U.S. Treasury yields (Exhibit 3: 10-year yields as of 6/30/2017).

*Exhibit 3* –10-Year Government Bond Yields: As of 6/30/17




### High-Yield and Senior Loan Market Overview

High-yield bond spreads over U.S. Treasuries tightened modestly at the end of the second quarter, by 16 bps from the end of the first quarter. While spreads are in fact tight to the historic average (the long-term average high-yield bond spread over U.S. Treasuries is T+588, December 1997 – June 2017), we believe there is room for further tightening given that spreads remain wide of the tight spreads experienced in May 2007 of T+245 (Exhibit 4). Moreover, defaults in the commodity sensitive sectors of the high-yield bond market drove the high yield default rate up to a peak at 3.82% in May 2016,but the rate has since fallen to 1.50% at the end of June 2017.This is well inside the long-term average highyield bond default rate of 3.29% (March 1999 – June 2017; Exhibit 6).We believe the low default rate is reflective of the relatively sound financial condition of most companies in the JPM High-Yield Bond Universe and the strong backdrop of a healthy macroeconomic environment.

default rate for senior loans remains low, at 1.54% at the end of the second quarter, and we believe it is likely to remain low given the overall health of the U.S. economy. This is below the long-term average senior loan default rate of 3.06% (March 1999 – June 2017; Exhibit 6).

*Exhibit 4* – U.S. High-Yield Bond Spread (OAS)*: December 1997 - June 2017

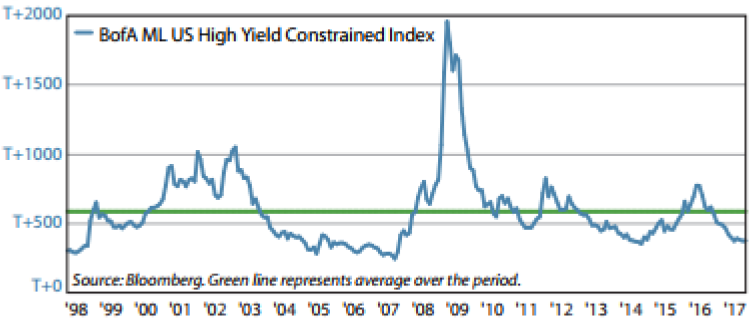
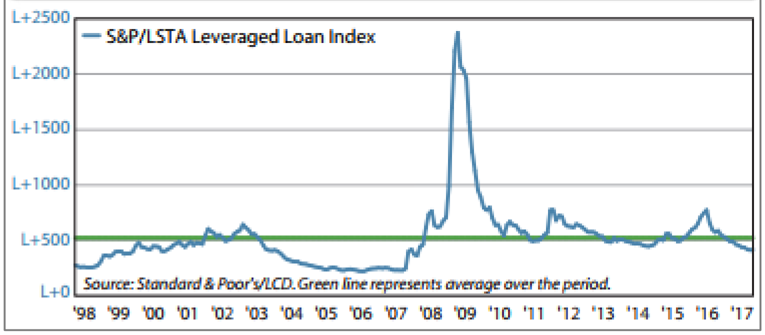



*Exhibit 5* – U.S. Senior Loan Spread over LIBOR[2]: December 1997 - June 2017

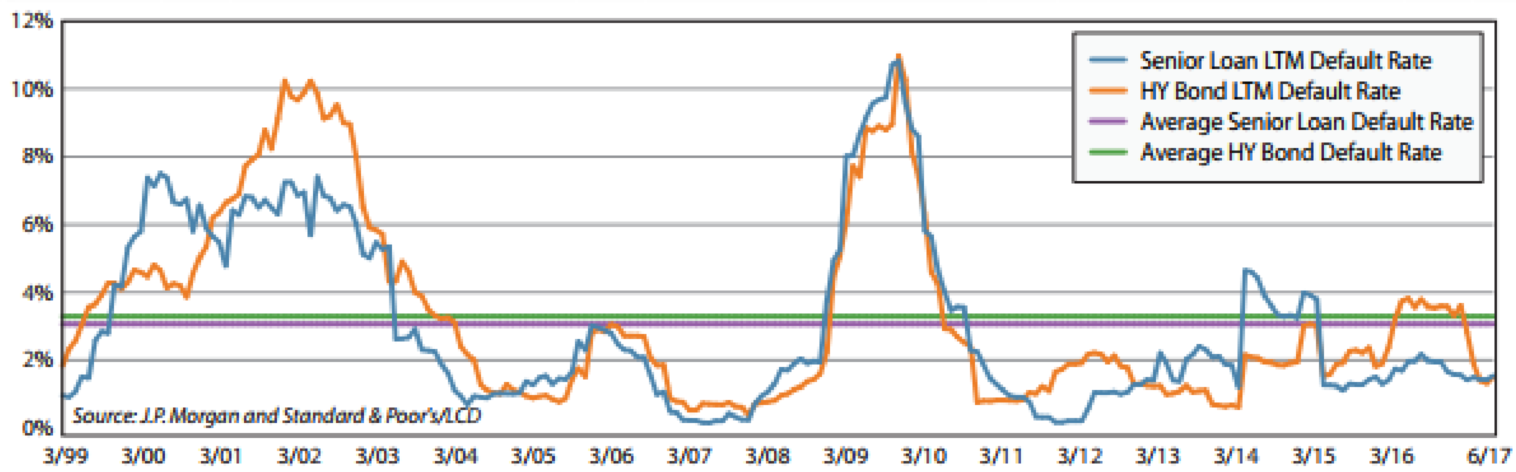



Senior loan spreads over 3-month LIBOR2 declined 21 bps during the second quarter to L+417 bps at quarter-end. This compares favorably to the pre-credit crisis average spread of L+372 (December 1997 – June 2007) and is inside the long-term average spread of L+523 (December 1997 – June 2017; Exhibit 5). According to JP Morgan, the senior loan asset class benefitted from $3.2 billion of inflows into retail mutual funds and exchange traded funds in the second quarter. While this is down from the $12.7 billion of inflows in the first quarter, the trend was still quite strong. The robust demand from investors for senior loans has led to additional refinancing's on the part of senior loan issuers. The refinancing rate has reduced the yield to investors given that the LIBOR1 increases haven't been enough to offset the spread decline from the refinancing's. We believe that with the potential for additional interest rate hikes on the horizon, LIBOR1 should continue to migrate higher throughout 2017. Importantly, the

## Conclusion

We remain confident that the favorable backdrop for the macro economy will persist for the near to intermediate term and that we are in a healthy part of the economic cycle to own high-yield bonds and senior loans. We also believe that the current cycle still has a long runway. Specifically, we believe senior loans, given their senior secured position in the capital structure, floating interest rate, attractive income and low default rate are well positioned as we move through 2017. We also believe that high-yield bonds should continue to perform well given their mid-cycle valuations and declining default rate. As we evaluate new investment opportunities, decisions will continue to be rooted in our rigorous bottom-up credit analysis and focus on the opportunities that we believe offer the best risk and reward balance.

*Exhibit 6* – Senior Loan and High-Yield Bond Historical Default Rates[3]: March 1999 - June 2017

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