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THE SCOTT LETTER is intended to educate global investors about closed-end funds. Closed-end funds can be a valuable and profitable investment tool. To learn about closed-end funds, visit our web site, www.CEFAdvisors.com, and in particular, read our article, *What Are Closed-End Funds*. Feel free to forward this newsletter to anyone who you believe could benefit from information on closed-end funds or global portfolios.

– George Cole Scott
Editor-in-Chief

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Financial Analysts Meet in Zurich

Your editor was among a group of 1,200 attending the 59th CFA Institute 2006 Annual Conference, its first overseas annual meeting, in Zurich, Switzerland. Participants at this high-powered meeting came from 50 countries and territories. It was the biggest meeting the city of Zurich has hosted this year.

The CFA Institute is the global, non-profit professional association that administers the Chartered Financial Analyst curriculum and examination program worldwide. It also publishes research, conducts professional development programs and sets ethics-based professional and performance reporting standards for the investment industry.

Located in Charlottesville, Virginia, the CFA Institute has more than 81,000 members in 126 countries and territories. It includes the world's 68,000 CFA charter holders and 132 affiliated professional societies. The CFA Institute also tries to reach out to other members who do not want to take the rigorous examinations for the CFA designation but desire to learn more about investments.

Topics covered at the four-day seminar included The State of the Wealth Management Industry, Looking Globally for Growth, The Virtues of Flexible Financial Markets and such regional lectures as China's Economy: Structural Strength, Cyclical Weakness. There were seminars on both the equity and the fixed income markets, with a strong emphasis on cross-border investing.

In the mornings, sessions were held for the entire group, while the afternoons were divided into workshops to include such topics as Global Diversification Opportunities: Portfolios Without Borders, The Benefits of Value Investing and The New Frontier: Venture Capital Investing in China. There were also some references to emerging markets investing as the wave of the future.

Zurich is the banking center for Switzerland, a country where services are the most important part of the economy. We learned that there are more assets in Zurich than anywhere else in the world, with banking and money management being the most important business in Switzerland. Exports are important, but Switzerland suffers a lot because of the expensive Swiss franc. Switzerland does not belong to the European Union which slows down exports. Switzerland's three most important trade partners are Germany, Italy and France.

The city of Zurich sits at the head of Lake Zurich, where one can see snow-capped mountains in the distance. Most of Switzerland has low air and water pollution, although it is increasing from vehicle emissions, acid rain and water pollution due to more use of agricultural fertilizers and a loss of biodiversity. ■

Emerging Markets Bear the Brunt of Sell-Off: The World Bank Lifts 2006 Outlook

Global financial markets in late May suffered one of their most turbulent weeks of recent years. By June 6, the Dow Jones Industrial Average was selling below the 11,000 level that it had traded above for most of the year. The reason was fear that interest rates will continue to rise in the U.S. and a slowdown will occur. The emerging markets were hit the hardest, despite many posting positive corporate news. These markets, which have produced outsized returns over the past three years, have struggled lately because they are tightly tied to U.S. economic health and concerns that Federal Reserve decisions will chill growth, hitting developing markets hard. Many investors have had to evaluate their holdings and consider switching into less volatile investments. Closed-End Fund Advisors has made moves for its clients in this direction.

In spite of this, a recent report from the World Bank said that it had raised its forecast for economic growth this year, arguing that sound policy frameworks have made many countries – especially developing nations – more resilient to high oil prices. The development leader expects the global economy to expand 3.7% this year, up from its November forecast of 3.2%.

Mark Mobius, head of emerging markets at Franklin Templeton, is optimistic as he sees the sell-off as a buying opportunity, citing strong macro-economic fundamentals, increased domestic buying and good valuations.

"In terms of valuation, emerging markets are looking quite attractive at the moment," said Jonathan Garner, analyst at Credit Suisse Bank. Garner said that valuations for emerging markets fell as low as 11 times forecast 2006 earnings on May 24, the day that markets seemed to reach bottom. He added that emerging markets rallied strongly after three previous sell-offs in April/May 2004, March 2005 and October 2006.

The Organization for Economic Cooperation and Development (OECD) said that economic prospects remain strong and have forecasted economic growth of 3.1% this year for its 30 member countries and 2.9% in 2007. Jean-Philippe Cotis, OECD chief economist, points out that much of the turmoil was a welcome reappearance of more normal pricing for risks, saying that the economic consequences would be limited. The OECD attributed strong growth in its area to buoyant trade spurred by Asia and recovery in Japan's economy but warned that deflation (in Japan) was waning only gradually. The organization said that China's expansion is expected to continue, forecasting economic growth of 9.7% in 2006 and 9.5% in 2007. He also warned that risks to the global economy from trade imbalances and lax fiscal policies remained. ■

The EU and Emerging Europe

Fueled by a surge of inward investment and growing international demand for new opportunities, the economies in Central and Eastern Europe are enjoying a period of unprecedented growth. Recent entrants to the EU, including Hungary and Poland, are improving productivity at a rate double that of their western European neighbors. Many countries in the region are seeing decreasing budget shortfalls and a stronger balance of payments, while at the same time exports to western Europe are growing. Poland, where foreign investment is critical to further development, is a country facing stiff competition for such investment from its neighbors. Its 40 million people are now in a period where the economy is able to grow in the 4%-5% range, and it has a low inflation rate. Poland has also established itself as a center for excellence for consumer electronics manufacturing. Despite some political uncertainties, investors in Poland are still bullish; further interest rate cuts will bring more inflows into this market. Making Poland more attractive for domestic companies will also make it a good place for investors. While some eastern European countries are prospering, the picture across the region is far from uniform. With its unwieldy mix of cultures, languages and politics, and a geographic area that stretches from Estonia along the Baltic Sea in the north to Bulgaria in the south, the region remains economically diverse even as it forges closer ties with the West. In May, eight countries in this vast territory – the Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Slovakia and Slovenia – were marking their two-year anniversary as the European Union's newest members, along with Cypress and Malta. Romania and Bulgaria may join this coveted Western club of 25 democratic nations in January 2007. Analysts agree that it is each country's degree of past psychic alignment with the West – even when the country was under the influence of the former Soviet Union or, in the case of Slovenia, part of the former communist state of Yugoslavia – that makes the difference in its economic and political progress and subsequent ability to lure investment dollars. ■

Source: *Global Finance,* May, 2006

Editor's Note: Closed-End Fund Advisor's clients hold investments in Central European Equity Fund. Templeton Russia Fund and Morgan Stanley Eastern Europe Fund are also in this region.

Franklin/Templeton Aims to Tap BRIC Fever

The recent fall in world stock markets hasn't stopped Franklin/Templeton Investments from launching a new mutual fund on June 1, 2006. The fund is the first so-called BRIC fund (which invests in Brazil, Russia, India and China) in the U.S and will invest at least 80% of its assets in securities of BRIC companies. Dr. Mark Mobius, the portfolio manager, said, "We believe BRIC companies have enormous earnings potential … and are attractive because of the dynamism of the BRIC economies and the historically low correlation among their stock markets over the last few years."

The new fund follows 10 BRIC funds which have been launched abroad. CEFA regrets that it will be a mutual fund rather than a closed-end fund, which has so many advantages over the newer, more marketable mutual funds.

Mark Mobius puts it this way: "For our sales guys, it's a terrible time to launch. But for investors, it is a great time." According to Dr. Mobius, a value investor, this is a great time to launch because the recent meltdown has knocked these stocks down to more attractive valuations while their countries growth prospects remain solid. Some analysts are skeptical of the narrow focus of the BRIC funds; they suggest that investors may be better served with a broadly diversified emerging markets fund. Indeed, Dr. Mobius agrees that a BRIC fund should be considered a supplement to a broader emerging markets fund, not a substitute. For investors seeking added exposure to some of the largest and fastest-growing developing countries, BRIC funds fit the bill. The existing BRIC funds, already available in Europe, Asia and Latin America, have most of their assets in Brazilian and Chinese stocks, with India representing the smallest portion of the four countries.

Goldman Sachs Group popularized the term "BRIC" in a 2003 report that suggested these four economies might one day surpass the U.S., Japan and western Europe as the most important in the world.

The Dow Jones BRIC 50 index was launched on June 7, 2006. It measures the performance of the 50 largest and most easy to trade companies in the four emerging markets, including Russia's Gazprom and Lukoil Holdings and India's Reliance Industries. It will be an underlying index for mutual funds, exchange-traded funds and other products. The number of components in the index is fixed at 15 each for Brazil, India and China and five for Russia. ■

Emergence and Growth of Global REITs

Hong Kong and China are among the areas where initial public offerings of new REIT shares are oversubscribed. REITs – which enable companies to avoid corporate taxation by distributing their profits in the form of dividends – have gained tremendous popularity in the U.S. over the past 20 years. Still, the U.S. REIT market may only represent the tip of the iceberg for investors seeking these characteristics. In Europe and Asia/Pacific, for example, many real estate securities markets are already in the early stages of development, potentially creating attractive opportunities for investors. Thirteen countries have introduced structures similar to U.S. REITs, and several more are considering REIT legislation. The growth of REIT-like structures around the world provides new ways to invest in the global real estate markets. Currently, the universe of real estate securities, as represented by the S&P/Citigroup World Property Broad Market Index, is more than twice the size of the U.S. market alone. The countries that have REIT-like structures now include Australia, Belgium, Canada, France, Hong Kong, Japan, Malaysia, New Zealand, Netherlands, Singapore, South Korea and Taiwan. Countries considering REIT-like structures are Finland, Germany, Italy, Philippines, Spain, Thailand and the United Kingdom.

Cohen & Steers, the most experienced REIT-fund investor, believes an allocation to global real estate may help reduce volatility in an investor's overall portfolio, while potentially enhancing a portfolio's return over time. With low correlations to U.S. markets, international real estate securities can help balance a portfolio that may be heavily weighted in U.S. REITs, while offering investment opportunities in rapidly growing/restructuring economies.

International real estate securities can also provide an additional level of diversification to an overall portfolio. The strongest REIT segments in 2006, in percentage gains through May, have been those invested in factory outlets (35.4%), apartments (34.6%), office (26.1%) self-storage (25.4%) and hotels (23.0%). REIT stocks as a group have risen 27.2% during the same period. Cohen & Steers, which has both mutual and closed-end funds holding REITs, has not only long experience in real estate (since 1986) but is also a pioneer of REIT investment around the globe. The Cohen & Steers Global Realty Fund (RWF:NYSE) was launched in 2005. More information on this and other Cohen & Steers funds can be found at www.cohenandsteers.com or call 800-330-7348. ■

Editor's Note: Clients of Closed-End Fund Advisors and your editor hold shares in RWF.

Templeton Global Income Fund Has Solid Growth

Templeton Global Income Fund (GIM:NYSE) posted cumulative total returns of +3.05% based on market price and +4.05% based on net asset value for the period ending February 28, 2006. While higher oil prices negatively impacted the deficit, the underlying trade balance (not including oil) deteriorated. Furthermore, the U.S. current account deficit widened to 7.0% of gross domestic product in the fourth quarter vs. 6.3% a year earlier. Overall, aggregate demands among Asian economies such as China, Singapore, Japan and South Korea, continued to accelerate in the fourth quarter of 2005. Correspondingly, regional interest rates tightened as economic activity accelerated. Economic activity also accelerated in the 12 country euro zone as growth slowed and inflation remained stable.

Franklin/Templeton also manages the Templeton Emerging Markets Income Fund (TEI:NYSE), which has a higher yield, but more volatility and risk. ■

Editor's Note: Clients of Closed-End Fund Advisors and your editor hold shares in GIM and TEI.

Low Returns for Mutual Fund Investors

The average mutual fund investor returns have received only a fraction of the impressive returns reported by the main stock and bond market indices over the past 20 years, and this is almost entirely their own fault. Their average annualized returns in equity funds has only been 3.9% for the 20 years through December 31, 2005, compared to an annual return of 11.9% for the S&P 500 Index, according to a study published in *The Financial Times*. The difference was almost entirely due to investors moving their money into and out of funds at precisely the wrong moment. "As markets rise, investors pour cash into mutual funds, and a selling frenzy begins after a decline," the study said. It found that investors were most likely to make the right decision in rising markets, and the most mistakes during downturns. "Investors are driven by fear that the market will not recover, but as the broad indices show, the market does recover," the study stated. This should be educational for closed-end fund investors, who generally take a longer-term view, as their funds are not subject to sudden redemptions in the down markets of recent days. The discount that closed-end funds sell at to their net asset value also is a defense against down markets. ■

Investment Manager Planning Dividend ETFs

New York-based Wisdom Tree Investments, Inc. has filed with the Securities and Exchange Commission to sell 20 exchange traded funds (ETFs) that will invest in six indexes of dividend-paying domestic equities and 14 that will invest in dividend-paying international equities. The proportion of the securities in each index will be based on either the amount of cash dividends that companies pay or the dividend yield of the companies in each index. The weighting of each security will depend on the amount of dividend yield per company.

Other issuers that have an ETF dividend focus are Barclays Global Investors, PowerShares Capital Management, State Street Global Advisors and the Vanguard Group. Out of more than 200 total ETFs, however, there are only about a half dozen ETFs with a dividend focus.

ETF providers are also moving forward with more commodity-related products. New issues are in registration by Barclays Global Investors (the largest ETF sponsor), Deutshe Bank and others, but the trend for more commodity-related ETFs is reviving as a diversification tool and to hedge geopolitical risk.

The next step will be the appearance of a move-away from indexed approaches to more active strategies. AMEX also wants to list options on commodity ETFs. The list is expanding. In April, the first ETF allowing investors to put money directly on the price of crude oil (U.S. Oil Fund) launched on the AMEX. It uses energy futures contracts, cash-settled options and other instruments to achieve oil exposure. A dividend yield is used to offset management fees. Research analysts at Deutsche Bank AG have said that as commodities gain more credibility, it will have the status of the emerging markets in the mid-1980s.The benefits of commodity diversification are real; the sector tends not to have much relationship to traditional asset classes such as stocks and bonds. Strong global growth, rising interest rates and higher inflation are seen as bullish for commodities, and ETFs are seen as a good way to play this sector. ■

Portfolio Manager's Review

In May, we took advantage of market weakness to add to holdings in Adams Express, Central European & Russia Fund and some of the Cohen & Steers real estate closed-end funds. We have reduced our mutual fund holdings to less than 10% to expand our closed–end fund exposure. We added to our REIT, Diamondrock Hospitality Co. Due to recent market volatility, we have also added to the Swiss Helvetia Fund because of its stability. For risk reduction, we reduced the Templeton Emerging Markets Income Fund and some shares of the Templeton Developing Markets Trust, a mutual fund, to lower emerging market exposure. ■

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