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THE SCOTT LETTER: CLOSED-END FUND REPORT

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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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World Economic Growth Unaffected by Stock Market Turbulence

"In the parlance of Thomas Friedman, the world never looked flatter than it did this week," says Business Week on March 12. The China February 27, 2007 9% stock market sell-off prompted sharp drops around the globe. Suddenly, money managers and traders, lulled into a trance by seven months of steadily rising share prices, felt like they'd been hit over the head with a best-selling hardcover. They were reminded that stocks are risky and emerging markets are riskier.

However, this market turbulence may not blow global growth off course as world economic growth is unlikely to be affected much, according to Jean-Claude Trichet, the European Central Bank President. Mr. Trichet saw it a "useful reminder" of the risks faced by investors. His remarks were aimed to calm market jitters. He pointed out that economic conditions, particularly in Europe, continue to be positive. Mr. Trichet is firmly allied with the relatively upbeat outlook of Ben Bernanke, chairman of the U.S. Federal Reserve, rather than Alan Greenspan, the former chairman, who has speculated about a possible recession.

Adding to this optimism, International Monetary Fund director, Rodrigo Rato said on April 9 that the risks to the world economy are less today than they were six months ago ... actually they were a little lower. He also urged political leaders to take the tough steps needed to make progress on global economic imbalances and financial market stability.

Mark Mobius, the founder of emerging markets investing and well-known to Scott Letter readers, said just after the February sell-off that he is "cautiously optimistic." He also said that short-term investors have to be cautious and be ready for a down-turn. "These (emerging) markets, on a price-earnings basis, are not highly expensive, and there's no good reason for a massive correction." Dr. Mobius views the Chinese market as a buying opportunity. "The global economy is dynamic," he added. ■

Sources: *Financial Times, Market Watch* (Dow Jones)

Emerging Markets Roundup: A Report on the BRIC Countries

The BRIC countries – Brazil, Russia, India and China – are the world economies building blocks. They are countries with large populations hungry for growth that are reshaping global commerce and have the potential to change it even more. The fortunes of the world economy over the next decade depend on what happens in these countries.

Brazil: Lula Unveils Growth Plan

Having vowed to make economic growth the focus of his second term, Brazilian president Luiz Inacio Lula da Silva unveiled a long-awaited plan to boost the nation's economy. The federal government will invest $234 billion over the next four years to improve infrastructure, increase access to credit, reduce bureaucracy and encourage private investment. He promised to accelerate growth to 5% in 2007, up from an average of 2.7% during his first administration.

Increased investment and lower interest rates should support the President's growth strategy. The Institute of International Finance predicts that net direct investment in Brazil will rise to $13 billion this year compared to a $6 billion decline in 2006. Portfolio equity investment will also rise to a record $12 billion, according to the organization, which expects almost 50% of the $52 billion in net equity investment predicted for Latin America to go to Brazil.

Brazil's central bank cut the benchmark Selic rate by a quarter-point to 13% in January, slowing the pace of its rate cuts. The IPCA inflation index (broad consumer price index) ended 2006 at 3.14%, its lowest level in nearly a decade and below the 4.5% official target. As a result, further cuts are expected.

The Petrobras state-owned oil company was granted an investment-grade rating by Standards and Poors ("S&P"). With a BBB- long-term rating, it is two notches above the sovereign. Meanwhile, investor appetite for sovereign paper remains high. A $500 million reopening of the government's 7.125% bonds due 2037, led by Merrill Lynch, saw demands for $950 million. The bonds were priced to yield 6.635%.

[**Editor's Note:** Clients of Closed-End Fund Advisors hold shares in Latin America Discovery Fund and Latin America Equity Fund, both of which have major holdings in Brazil.]

Russia: Investors Stay Away From IPOs

Prosecutors brought fresh charges against former Yukos oil company head Mikhail Khodorkovsky and an associate, which could add another 15 years behind bars. Khodorkovsky would otherwise have been eligible for parole later this year. He labeled the charges a "shameful farce" and contended that they were intended to prevent him from being free during the 2008 presidential elections. Norilsk Nickel CEO Mikhail Prokhorov announced he will sell his largest platinum and palladium producers to partner Vladimir Potanin, which may be a step toward the Kremlin, eager to continue to expand its presence in the natural resources sector, taking control of the company.

Meanwhile, in early February, Russian president Vladimir Putin urged big business to diversify out of commodities and to instead focus on more value-added products. Investors are clearly becoming more selective about Russian offerings. Three planned Russian company IPOs were anticipated in early February 2007: the metals company Polymetal and tech equipment supplier Sitronics closed the first day of trading below their offering price despite pricing at the bottom of the range and one offering, GV Gold, was postponed, suggesting that state banks Sberbank and Vneshtorgbank, which hope to raise a total of around $15 billion in offerings later in the first half of 2007, may face an uphill battle.

Another $15 billion in fresh stock is in the pipeline for 2007, although there is an anemic appetite for Russian IPOs. Defense minister Sergei Ivanov announced a $189 billion overhaul of Russia's military, a move interpreted as evidence that Russia intends to expand its military influence.

A few days later, President Putin said that U.S. military policy had the impact of encouraging other countries to seek nuclear technology, as recent downswings in U.S.–Russian relations continued.

[**Editor's Note:** CEFA clients hold small positions in Central European Equity Fund, which has as much as 50% of its assets invested in Russia.]

India: Rating Upgrade Boosts the Rise of India

In a move that will drive substantial foreign investment to India, S&P became the third major ratings agency to raise India's sovereign rating to investment grade. The rating now stands at BBB-/A-3. S&P cited a strong national balance sheet, foreign exchange accumulation, strong capital flows and prudent debt management. Though this is a sovereign rating upgrade, it does not affect the Indian government much since it does not borrow from foreign markets. The rating upgrade will have a very significant effect on corporate India's activities. Indian companies raised $30 billion in debt, largely through convertible securities, between April 2004 and March 2006. Even before the upgrade, Indian dollar-denominated debt was priced at 57 basis points above six-month LIBOR. (The LIBOR benchmark is among the most common of interest rate indexes used to make adjustments to adjustable rate mortgages.) The spread over LIBOR (rates) is expected to fall further while the rupee is expected to strengthen.

The rating upgrade reflects strong growth in India's economy. According to Central Statistical Organization (CSO), Indian GDP growth is expected to be 9.2% for the fiscal year April 2006-March 2007, topping the blistering 9% growth of 2005-2006. Estimates for 2006-2007 show manufacturing growth at 11.3% against 9% last year, while construction grew at 9.4% against 14.2%. Agriculture grew by only 2.7% against 7% in 2005-2006.

Within the services sector, banking and finance has expanded by 11.1%, while trade, hotels, transport and telecommunications have grown by 13%.

The premier Indian stock exchanges are sitting pretty, as overseas stock exchanges and private equity funds line up for a stake. Deutsche Borse, NASDAQ, the London Stock Exchange and the Singapore Stock Exchange are all in the fray for a 5% stake in the Bombay Stock Exchange (BSE) prior to its IPO this May.

Late reports said that a surge in capital inflows, due to the recent interest rate rise, has pushed the rupee to a near 8-year high against the U.S. dollar and boosted foreign exchange reserves to $200,000 billion USD. This will prompt India's conservative central bank to delay further moves the currency. There are concerns that the increase in reserves could make India vulnerable to a heard-like exit of foreign investors, triggering sharp falls in asset prices.

[**Editor's Note:** A few CEFA clients have small positions, including your editor, in one of the two Indian closed-end funds. We are now considering whether to increase our holdings in this dynamic economy, despite the rate rise.]

China: Restraints Fail to Cool Sizzling Economy

China's economy continued to sizzle in 2006 despite government efforts to slow the country's growth to a more moderate pace. GDP grew more quickly in 2006 than it has in a decade, leaping 10.7% to $2.7 trillion. The rapid growth brings China closer to overtaking Germany, which has a total GDP of $3 trillion and a much slower growth rate, to become the world's third largest economy.

The government in 2006 raised interest and reserve rates, and limited investment in some overheated sectors. Such measures have yet to slow the economy significantly; further tightening is likely. Fear of tightening measures and concerns over market speculation contributed to domestic stock market volatility earlier this year.

The Shanghai Composites index, which more than doubled in value last year, dropped significantly in late January and early February following comments from government officials suggesting that speculation had played a significant role in recent gains. The market has rebounded, but fears of a market bubble remain. To reduce speculation, the government has ordered the country's banks to block loans for stock market investments.

China-U.S. relations have been shaken on the trade front, as the United States brought a new WTO case against China, charging that China gives export subsidies to companies producing steel, wood, paper and other manufactured products. Such export subsidies benefit companies that may produce up to 60% of China's exports, according to U.S. trade officials. Chinese president Hu Jintao visited eight African nations in early February, offering financial aid and negotiating various trade agreements. China is increasingly looking to African countries for support within international organizations and for the natural resources needed to sustain China's rapid growth. While African leaders have responded positively to Hu's visit, worries that China may be exploiting some of its trade relationships there are growing. ■

Source: *Global Finance,* March, 2007

Editor's Note: Clients of CEFA, as well as George Cole Scott, hold the Asia Pacific Fund and Templeton Dragon Funds which invest in China.

Dividend-Paying Stocks Take Center Stage: Cohen & Steers Leads the Way

Many dividend-paying stocks are experiencing a renaissance with investors, thanks in large part to the 15% tax rate on qualified dividends and baby boomer's desire for investments that offer the potential for income and growth as they ready for retirement, according to Cohen & Steers latest "Investor Focus" report.

Although past performance is no guarantee of future results, history supports the potential benefits of a dividend-focused strategy. Since 1972, stocks that pay dividends have performed more than four times better than those that don't. What's more, stocks that grow their dividends have surpassed all dividend-paying stocks by another 0.7% per year.

"A company needs a healthy balance sheet and solid cash flows to grow a dividend," a Cohen & Steers spokesman said. The firm points out that there has been a dramatic increase in the number of companies paying or raising dividends.

"We believe that any management willing to return cash to shareholders by raising their dividend is signaling confidence in the company's future prospects."

Cohen & Steers anticipates continued growth in the number of companies that will initiate, reinstate or raise their dividends in 2007.

"As all equity investments fluctuate in response to internal and external circumstances, we believe that dividends will be viewed as an increasingly important part of a company's performance and an investment's total return."

It's a welcome state of affairs, one that engenders new opportunities for value and potential income. ■

Editor's Note: CEFA clients, as well as George Cole Scott, hold major positions in Cohen & Steers closed-end funds to fulfill the real estate asset allocation.

U.S. Property Funds Feel Sub-Prime Sting

The implosion of some parts of the mortgage market is starting to hit mutual (and closed-end) funds. The latest casualty might seem to be the most obvious: real estate funds. When HSBC announced that it will take a "higher than expected" charge on bad debts for 2006 as a result of the growing bankruptcy rates in the U.S. sub-prime mortgage market, it sent a shockwave through stock markets.

The $10.5 billion write-off was interpreted as a signal of worse to come from banks and financial institutions growing fat from the booming U.S. housing market, particularly those that are waist-deep in sub-prime loans. Until recently, these funds have been surprisingly resilient, because their investments tend to be concentrated in commercial properties, not residential.

These funds invest in real estate investment trusts ("REITs") which acquire and manage commercial properties such as offices, malls and apartment buildings. However, they have relatively little exposure to home loans to borrowers with weak credit. Many banks and mortgage firms have focused significant resources on the sub-prime market over the past two years. The question is not whether they will impact balance sheets and share prices, but how much impact they will have (on share prices). In the past two years, the U.S. housing market has seen remarkable growth in alternative mortgage products with a sharp rise in interest-only loans. As a result, a number of sub-prime lenders have closed over the past few months.

Some financial advisors say that the current downturn could be an early sign of a slowdown in the real estate market. The hardest hit were some mortgage REITs that had either loaned money to owners of property or bought existing mortgages to profit on the interest earned. Investors are trying to see which of these have exposure to sub-prime borrowers.

There is some good news. The apartment sector could benefit as low credit borrowers who may have defaulted, may be renting apartments, which will be good for apartment REITs. Investors should be warned, however, that they shouldn't expect the +30% annual returns they have seen in the past. ■

Source: *Wall Street Journal, Global Finance*

Cohen & Steers Closed-End Opportunity Fund

The Cohen & Steers Closed-End Opportunity Fund is the first-ever fund of closed-end funds. It raised $541 million in November 2006, invests in closed-end management investment companies that invest significantly in equity or income-producing securities. The fund's common shares are listed on the New York Stock Exchange under the symbol FOF. The Fund seeks total return by investing in common stock of closed-end funds that invest significantly in equity or income-producing securities.

"The rational for launching the fund is the potential investment opportunity we see in publicly traded closed-end mutual funds. Many funds offer investors the potential for high current income – 107 closed-end funds yield more than 7%, and some are selling at discounts to net asset value," portfolio manager Doug Bond said recently.

"As we [Cohen & Steers] manage high income equity portfolios, we see closed-end funds as offering an attractive total return opportunity.

Asked whether he sees closed-end funds as offering value, Mr. Bond replied that closed-end funds are not widely followed by research analysts, and the market's growth in newly listed funds over the past five years has only widened the long-term coverage gap.

"A lack of coverage within a relatively illiquid market can create compelling values, especially when certain factors periodically spark indiscriminate selling. We believe we have the resources and expertise to monitor these funds and determine which ones offer the best values."

"We see the potential for attractive total returns across most categories, but the strength of the 2006 rally is unlikely to repeat itself. In our view, the chief positive catalyst going into 2007 is a better interest rate environment.

"In 2005 and the first half of 2006, the Federal Reserve gradually raised rates from 2.25% to 5.25%. We believe that in 2007 the Fed will be more likely to keep rates on hold or even reduce them, as long as inflation stays contained.

"If we are correct, closed-end fund share prices should benefit for two reasons. First, the earnings power of leveraged closed-end funds should improve as borrowing costs either remain stable or decline. Second, investor sentiment should improve as investors shift from fear of dividend cuts to a focus on which closed-end funds are likely to increase their dividends. In addition, a benign interest rate policy should allow closed-end funds to maintain their above-average yields compared with many other investment options. This would help demand.

"Fund of funds ("FOFs") has been favoring funds focused on equity strategies, and we expect that bias to continue. Our portfolio will have a meaningful allocation to funds with fixed income strategies. Our investment process starts by seeking funds with strong fundamentals, including dividend coverage, high current income and attractive relative discount to net asset value. While we are focused primarily on funds with market capitalization in excess of $200 million, we expect to invest in and capitalize on the value we find in funds with smaller capitalizations as well. As of December 31, 2006, we had made investments in 60 different funds and 15 distinct closed-end fund sectors."

For more information on Cohen & Steers funds, please call 800-330-7348 or visit www.cohenandsteers.com. ■

The Latin America Discovery Fund: Letter to Stockholders

"For the year ended December 31, 2006, The Latin America Discovery Fund, Inc. had total returns, based on net asset value and market price per share, of 50.27% net of fees and 64.51%, respectively, compared to 43.15% for the Morgan Stanley Capital International ("MSCI") Emerging Markets Free Latin America Index.

"The closing price of the Fund's shares at year-end on the New York Stock Exchange was $26.70, representing a 4.2% discount to the Fund's net asset value per share. Past performance is no guarantee of future results.

"In the 12 months ended December 31, 2006, the Latin America markets as measured by the MSCI gained 37.3% in local terms and 43.2% in U.S. dollar terms. The region began the year surging over 15.5% in the first quarter, outperforming major developed markets. Favorable valuations relative to the developed world, rising corporate profitability and stronger underlying economics enticed investors.

"Overall appetite for emerging markets equities reached record highs in April with year-to-date inflows surpassing those of the whole of 2005. The period in review, however, did not end without some renewed volatility.

"After reaching new heights, Latin American markets, along with other global markets, sold off in May as global risk aversion spike due to concerns of slowing global growth, rising inflation and interest rates in the U.S.-Latin American markets were down an average of 13% during the global sell-off.

"Nevertheless, as concerns subsided over global growth and U.S. interest rates, the asset class, as in past corrections, rebounded strongly and ended the year above its previously 2006 high.

"We attribute the resilience of the asset class in each period to the fact that economies have become more resilient to external shocks thanks to the adoption of better macro-economic fundamentals, stronger fiscal performance and de-leveraging of corporate balance sheets.

"The Fund's outperformance was driven by both stock selection and country decisions. Stock selection, however, was the majority contributor. Country allocations to Mexico and Brazil were key contributors to relative returns as both country and stock decisions added value. Stock selection was strong within telecommunication services, industrials, financials and materials. Stock selection in Argentina (energy) and Chile (materials) was also positive.

"Overall, the Fund's strategy of overweighting domestic and consumer-oriented stocks while maintaining a large underweight in cyclical stocks within materials and energy related names proved to be a strong driver this year and a key reason for the strong relative performance.

"We continued to focus on countries where gross domestic product (GDP) growth and fiscal policy remain strong, and on companies with strong management and earnings visibility. With limited systemic risk, particularly among the larger countries, we continue to see stock selection as a key driver of performance in 2007.

"We are seeing in Latin America a similar story to what we have seen take place in other emerging market regions over the last couple of years: rising currency and domestic consumption. Over the year, we continued to consolidate positions within domestic oriented sectors with strong secular growth prospects as we believe that these stocks will preserve their value in an environment of lower domestic rates, peaking commodity prices and slowing global growth.

"We remain positive on both Brazil and Mexico, due to our still positive view on each country's domestic sectors and select Brazilian cyclical stocks. The remainder of our allocations are spread across Chile, Peru and Columbia with a focus again on domestic sectors, particularly banks.

Sincerely,
Ronald E. Robison
President/Principal Executive Officer

This is a condensed version of the Shareholder Letter. More information is available on their web site at www.morganstanley.com. ■

[Editor's Note: CEFA clients hold an increasing number of shares of Latin America Discovery Fund. We look forward to interviewing the Fund's portfolio manager in the near future.]

Berkshire Hathaway, Inc.: A Synopsis of the Letter from the Chairman, Warren E. Buffett

"Our gain in net worth during 2006 was $16.9 billion, which increased the per share book value of both our Class A and Class B stocks by 18.4%.

"Over the last 42 years (that is, since the present management took over), book value has grown from $19 to $70,281, a rate of 21.4% compounded annually.

"The 1965-2006 compound growth rate for Berkshire Hathaway was +17.9% and +31.7%. for the period 1995-2006.

"We believe that $16.9 billon is a record for a one-year gain in net worth – more than has ever been booked by any American business, leaving aside boosts that have occurred because of mergers, e.g., AOL's purchase by Time Warner. Of course, Exxon Mobil and other companies earn far more than Berkshire, but their earnings largely go to dividends and/or purchases, rather than building net worth.

"Our most important business, insurance, benefited from a large dose of luck. Mother Nature, bless her heart, went on vacation. After hammering us with hurricanes in 2004 and 2005 – storms that caused us to lose a bundle on super-cat insurance – she just vanished. Last year, the red ink from this activity turned black – very black.

"In addition, the great majority of our 73 businesses did outstandingly well in 2006. Let me focus for a moment on on eof our largest operations, GEICO. What management accomplished there was simply extraordinary. Between year-end 2003 and year-end 2006, the number of GEICO policies increased from 5.7 million to 8.1 million, a jump of 42%. Yet during the same period, the number of company employees fell 3.5%. So productivity grew 47%. That remarkable gain has allowed GEICO to maintain its all-important position as a low cost producer, even though it has dramatically increased its advertising expenditures from $631 million in 2006, up from $238 million in 2003.

"Last year we had a good increase in non-insurance earnings: 38%. Large gains will continue here only if we are able to make major and sensible acquisitions. That will not be easy.

"We began 2006 by completing three acquisitions pending at year-end. All are performing very well. We spent about $6 billion for PacifiCorp, Business Wire and Applied Underwriters.

"The highlight of the year, however, was our July 5th acquisition of ISCAR, an Israeli company. Our conclusion is that Berkshire Hathaway would be the ideal home for ISCAR, a maker of cutting tools.

Mr. Buffett lists 18 of his largest investments. The five largest are American Express Company, Anheuser-Busch Cos., the Coca-Cola Company, Conoco Phillips, and Johnson & Johnson.

"We are delighted by the 2006 business performance of virtually all of our investees. Last year, we told you that our expectation was that these companies, in aggregate, would increase their earnings by 6% to 8% annually, a rate that would double their earnings every 10 years or so. In 2006, American Express, Coca-Cola, Procter & Gamble and Wells Fargo increased per-share earnings by 18%, 9%, 8% and 11%, respectively. These are stellar results, and we thank their CEOs.

Berkshire Hathaway also realized about $186 million in pre-tax profits in

2006 in foreign exchange positions. Mr. Buffett sees the U.S. dollar as continuing to weaken over time.

"Overall, Berkshire's business performance will determine the price of the stock, and most of the time it will sell in a zone of reasonableness.

Mr. Buffett, 76, stated "Last year I arranged for the bulk of my Berkshire holdings to go to five charitable foundations, thus carrying out my lifelong plan to eventually use all of my shares for philanthropic purposes. Details of the commitments I have made, as well as the rationale for them, are posted on our web site, www.berkshirehathaway.com."

"In my will, I've stipulated that the proceeds from all Berkshire shares that I still own at death are to be used for philanthropic purposes within 10 years after my estate has closed. Adding this 13-year period to my lifespan of about 12 years (though naturally I'm expecting more) means that the proceeds from all of my Berkshire shares will likely be distributed for societal purposes over the next 25 years or so.

"A few shareholders have expressed concern that sales of Berkshire by the foundations receiving them will depress the stock. These fears are unwarranted. The annual trading volume of many stocks exceeds 100% of the outstanding shares, but nevertheless the stocks usually sell at prices approximating their intrinsic vlaue. Berkshire intends to sell at an appropriate price, but the annual volume is only 15% of shares outstanding. [This will] leave Berkshire with a turnover that the lowest around.

Mr. Buffet concludes his report with a description of his long-time friend, Walter Schloss, who last year turned 90. From 1956 to 2002, Walter managed a remarkably successful investment partnership, from which he took not a dime unless his investors made money. Walter and his son, Edwin, never used inside information; indeed they used "outside" information only sparingly, generally selecting securities using simple statistical methods, learned by working for Ben Graham.

When asked about his approach, he replied, "we try to buy stocks cheap." So much for Modern Portfolio theory, technical analysis, macroeconomic thoughts and complex algorithms. ■

Editor's Note: Many clients of Closed-End Fund Advisors hold Class B shares of Berkshire Hathaway. They appreciate the lack of volatility as well as the steady increase in value.

Portfolio Manager's Review

We used much of the cash we had raised in the previous month and weakness in our covered markets to increase holdings in many of our best performing funds. These include Adams Express, Asia Pacific Fund, Berkshire Hathaway (Class B shares), Central Securities, Cohen & Steers Quality Income Realty and Diamondrock Hospitality, a hotel-finance REIT.

We found lower prices, due to market weakness, in real estate funds such as ING Clarion Global Real Estate Income Fund and some of the Cohen & Steers closed-end funds. Other opportunities were found in Latin American Discovery Fund, Templeton Emerging Income Fund and Templeton Dragon Fund.

We reduced Allied Capital, Calamos Global Total Return Fund, Central European & Russia Fund and Templeton Emerging Markets Fund. Templeton Global Income is being eliminated because of its high premium.

Going forward, we are now nearly fully invested in funds which we see as being better able to outperform our benchmarks, as we did in 2006.

New clients are being invested in many of these funds, according to their asset allocation models dictated by their individual investment objectives. ■

George Cole Scott

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