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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

IN THIS ISSUE:

Adams Express Company Continues to Generate Solid Returns

Dissidents Try to Force ADX into a Tender Offer, Conversion to a Mutual Fund or Liquidation

Management Prevails, but Issues Remain for the Industry

BALTIMORE – (March 22, 2011) The Adams Express Company (NYSE:ADX) announced that a stockholder proposal for the Board of Directors to consider causing the Company to conduct a self-tender offer was soundly defeated by stockholders at its annual meeting in Baltimore. Of the 56% of the outstanding shares of the Company's stock that were cast on the proposal, 72% of the shares voted against it, and 25% of the shares (representing only 14% of the Company's outstanding shares) voted for it. Three percent (3%) of the shares abstained. For the proposal to pass, the affirmative vote of a majority of the votes cast on the proposal was required.

Douglas G. Ober

Douglas G. Ober, Chairman and CEO stated: "I am very pleased that our shareholders carefully considered the merits of the proposal, which was submitted by an activist hedge fund and the reasons articulated by the Board for recommending that the stockholders vote against it. They resoundingly voted against the proposal."

For the 12 months ended December 31, 2010, the total return on Adams Express' net asset value, with dividends and capital gains reinvested, was 11.2%. Comparable figures for the S&P 500 Composite Stock Index ("S&P 500") and the Lipper Large-Cap Core Mutual Fund Average ("Lipper Peer Group") were 15.1% and 12.9%, respectively. The total return on Adams Express' market value was 11.5%. ADX has outperformed both the S&P 500 and the Lipper Peer Group on a total return basis for the three and five year periods ended December 31, 2010. As of that date, ADX's net assets were $1,124,671,966, an increase from $1,045,027,339 in December 31, 2009.

Doug Ober is the chief portfolio manager and has been a Director of ADX and Petroleum & Resources Fund (NYSE:PEO) since 1989 and Chairman of the Board since 1991. He is also chief portfolio manager of PEO. Doug is supported by a team of research analysts who look for investments offering long-term earnings growth at a reasonable price.

Closed-End Fund Advisors wants to note that contrary to what activists think, the Investment Company Act of 1940 specifically allowed discounts in closed-end funds. Secondly, it is possible that Congress may restrict hedge fund activity and require SEC registration, although we are not optimistic that will happen any time soon.

The Interview

We interviewed Doug by telephone on February 25, 2011:

SL: This interview is being published ten years after we resumed publication of *The Scott Letter* in electronic format in May 2001. When our son, John Cole Scott, graduated from William & Mary, he joined us in January 2001.

John convinced us that it would be best to publish *The Scott Letter* on-line. As a result, this bi-monthly newsletter is now distributed free in electronic format and has been mailed to our clients since May 2001. We now have more than 2,500 subscribers to *The Scott Letter* which is distributed to every part of the world.

Do you remember when The Closed-End Fund Association met at the New York Stock Exchange?

Ober: Yes, and I think that you and John are doing a great job keeping the interest alive.

SL: We are concerned about the future of the industry because of the activity of hedge funds and other activists who are only interested in short-term gains. This is a vibrant industry that has excelled and achieved excellence in long-term performance for investors over many years.

I am going to attend the CFA annual conference in Edinburgh in May. Will you be attending?

Ober: Not this year, but I will attend the ICI [Investment Company Institute] general meeting in May and The Closed-End Fund Association meeting in New York on April 5.

SL: We voted our proxy on the internet.

Ober: Internet voting makes a lot of sense and saves paper. We urge all of our shareholders to get their quarterly and annual reports electronically as we think that it is the wave of the future.

SL: What is the present focus of ADX?

Ober: We want to focus more on the industrial side – Caterpillar, Federal Express, General Electric – assuming that we don't see a substantial price hike in oil from the $100 level. We started emphasizing the industrials in early 2009. However, there were market concerns about a double-dip recession, so the industrials subsequently underperformed and hurt our performance in 2010.

We think that we have a good, broad exposure in Adams to the energy sector, including our Petroleum & Resources holdings. The strong performance from Exxon and Chevron also helped, but we are still underweight in energy.

Natural gas has been out of favor for the better part of a year now, but we think it will turn around. There are some good opportunities, as many of these companies have been beaten down excessively.

SL: What market segments have performed the best for the Fund?

Ober: Three segments have done particularly well: Financials, Materials and Healthcare. We have been underweighted in Financials, but the Bank of America, JP Morgan Chase and Morgan Stanley are up over double-digits so far in 2011, after being a drag for a few years. They got hit first with the meltdown and then with new, tighter regulations, but the new regulations weren't as tough as expected.

[**Editor's Note:** Doug is referring to the Dodd-Frank Wall Street Reform and Consumer Protection Act, enacted in July 2010, which addressed the increasing propensity of the financial sector to put the entire system at risk by bailing companies out at taxpayer expense.]

SL: Do you think that the financial sector will continue to improve and why?

Ober: The proposed $20 billion mortgage settlement could be a setback for banks such as Wells Fargo and Bank of America, but the banking group in general has come back strong with increased lending in the past six months. The group is much more cognizant of the amount of risk they are taking on, which is being reflected in the stock prices.

SL: We don't pay a lot of attention to how geopolitical events affect stock markets because we know from experience that economic fundamentals drive markets. For example, during the Egyptian crisis, the stock markets were up nearly every day because good U.S. economic numbers came out at the same time. Stock markets have seen many years of crises but have always recovered. In fact, lower stock prices have usually been bargain hunting times. This is an important issue that *The Scott Letter* will follow-up on periodically.

Ober: I think a realistic area of concern for the markets is that we have consistently gone into recession with spikes in higher oil prices. If they go up to $130 or $140 a barrel, I suspect that we will fall back into a recession. The revised fourth quarter GDP numbers were 50 basis points weaker than expected, largely as a result of government cutbacks in the fourth quarter, but we believe that we are on the right track. The economy should continue to expand.

I had the pleasure last night of being able to listen to the former president of South Africa, Mr. de Klerk, who said that these countries – Libya, Tunisia, Egypt – need to realize that changes have to be made peacefully as in South Africa. There is no question that Libya is a place of concern because they are a significant oil producer, mostly supplying Europe.

SL: I also notice that you added four new names in the fourth quarter, including Caterpillar, FedEx, Apple and Google.

Ober: Caterpillar has done particularly well as a result of the worldwide focus on basic materials. They have done business around the world with mining companies like BHP Billiton Ltd., Rio Tinto and others. They will buy Bucyrus Erie (presently Bucyrus Corp.) which will increase their exposure to the mining industry.

Federal Express is worldwide and has been successful in keeping their costs down by taking marketshare from smaller companies. With a general pick-up in worldwide economic activity, FedEx will also benefit from the stronger growth.

Regarding Apple and Google, we have seen tremendous success with Apple's iPhone, iPod and iPad. Apple is really penetrating the corporate world on the iPad side, as laptops and notebooks have lagged.

Google has surpassed the other search engine companies with their very strong software as well as their entry into the communications arena with the Android Smartphone operating system - the first company to penetrate that arena successfully. There are now more Android phones out there than Apple phones.

SL: Do you have an iPad yet?

Ober: I am waiting for the next version.

SL: Do you think that Microsoft will use the $31.55 billion they have in cash to acquire someone or increase their dividend?

Ober: I suspect that they might pay out another special dividend. Microsoft is selling at ten times earnings, and investors see it as an old line company. We question their direction and Steve Ballmer's ability to drive that company. They are still way behind the Google search engine.

[**Editor's Note:** On February 11, 2011, Nokia outlined a broad strategic partnership with Microsoft to build a new global mobile ecosystem. However, there are risks facing this Finnish company as it battles to preserve leadership in the mobile phone market. More details on this are available at press.nokia.com.]

SL: One of our clients holds a large position in one of your top holdings, General Electric (GE). He thinks the stock could double from its present price of around $21.50. Do you agree?

Ober: Their P/E (price to earnings) is probably similar to that of Microsoft, but GE is a strong company that recently bought Dresser and other companies that are doing well. They have built a sizeable oil service business with close to $9 billion in revenue coming from that sector. I think GE can go to $42, but it will take a couple of years. The most recent quarter was very strong; it is the first time that revenues and earnings were both up significantly. The stock price is up about 13% in 2011, reflecting that potential.

SL: The recent weakness in GE presents an opportunity that fits our philosophy of buying when everyone else is selling. How much cash do you have in the ADX portfolio now?

Ober: At year-end, we held 3.6% in cash and money markets or $41.15 million.

SL: That should be sufficient for share repurchases. Do you have price targets for each position you hold?

Ober: Our analysts establish price targets when we first purchase a stock. As with most analysts, either on the buy or the sell side, they have opportunities to raise or lower those target prices as things change.

SL: Please tell us about your distribution policies and their flexibility. We note that the total distributions on Adams Express for 2010 were $0.51 or a 13% increase over the amount paid in 2009. Do you have a set formula by which you pay out distributions? What do you think about funds that pay what is known as "managed distributions" by paying out a set amount of the net asset value, usually each quarter?

Ober: In 2007, the distribution was $1.03, in 2008 it was $0.64, and $0.45 in 2009. It was back up to $0.51 in 2010. We take capital gains, which constitute a big chunk of the total distributions, when individual stock valuations are full or nearly so. We took profits in 2010 in stocks that did very well in 2009 and were thus able to pay out a larger distribution. While there are certainly attractive aspects to managed distributions, they do require a different portfolio strategy.

SL: That is the philosophy of the older funds. The smaller funds often want to have a managed distribution plan in place because they think it will solve the so-called "discount problem". However, some funds just take capital gains to reach this mandate which, as you well know, may be the wrong reason to sell a position. Some of them have found that they are unable to find any profits and may have to take losses.

You sent out a survey to shareholders last year and found that both your ADX and PEO shareholders were "very content". Do you think this has changed with the recent events?

Ober: When the responses to the last survey were received, the discount was between 15.5% and 16.4%. I think that if shareholders considered the discount a problem, they certainly would have let us know at the time. Such a survey is expensive, but, if there is sufficient support from the shareholder proposal, I suspect the Board will, if there is a solid basis for it, require another survey.

SL: As we go to press, the discount was -13.7% (as of March 25, 2011), and the 52-week total market return was +12.70%. Are you ready to start a regular share repurchase program immediately?

Ober: When we first instituted the repurchase program in 1999, we began buying but not aggressively as daily trading was running only about 40,000 shares a day, so we couldn't buy a huge number of shares. We are limited by the SEC in the number of shares that we can buy daily. At first, we could only buy about 10,000 shares a day, and we saw a real response in the narrowing of the discount to the share repurchases for maybe four years.

Subsequent to those years, the discount widened almost every year from 2004 out to 2010, with the exception of 2007. <u>This occurred despite regular share repurchases every year through 2009</u>.

In the past 18 months, our Board's desire was to build up the assets of ADX after the losses in 2008. The assets are now at a satisfactory level, so I expect that we will begin repurchasing shares again as long as there is cash available (meaning the management believes there are no better investments) and the discount is above 10%.

SL: We have confidence that you will continue to do what is best for your shareholders. Do you normally use a proxy solicitor to be sure that shareholders vote?

Ober: Over the years, we have used The Altman Group to be sure that we get enough votes for a quorum so Directors can be elected and the auditors can be ratified by the shareholders. Regarding the tender offer proposal, it really isn't a tender offer because it can be turned down by the Board.

SL: As a result of all of these events, the smaller funds must be shaking in their boots. We will continue to follow this for the industry which, as you know, has continued to expand for nearly 200 years. What other advantages do you see for regular repurchases?

Ober: We think it important to have a share repurchase program, but we don't want to force our shareholders to re-invest their distributions if they don't want to. If we don't buy-in enough shares to offset the bulk of that distribution, then we are modestly diluting our shareholders, which is something we would rather avoid. That was one of the principal reasons the share repurchase programs were first instituted. But, when you had a 20% return on your shares as we did on PEO in 2010, this is better than buying shares at a 14% discount. In 2009, we had a 26% market return on PEO.

We believe in the value of the share repurchase program over the practice of many funds to have periodic tender offers. This reduces or eliminates dilution, increases liquidity and puts an effective floor under the stock price, but I remain unconvinced that it has any impact on the discount. I expect that we will begin to again repurchase shares in the open market as long as the discount is 10% or greater and there is sufficient cash in the Fund. It will provide a competitive return to our shareholders.

SL: Last year you told us that you had repurchased shares of PEO but not enough to offset pay-out in distributions.

Ober: Since we beat our benchmark, we picked stocks better then the index. We believe that, in the case of PEO, we can periodically do better for our shareholders by staying more fully invested in energy and basic materials. We had a better return for the shareholders of PEO than if we had bought in more shares.

ADX's 52-week total return through February 25, 2011 was +20.3% so we are doing a good job for shareholders by investing in stocks other than our own.

SL: That is commendable. What is your philosophy behind your option writing, and has it changed any this year?

Ober: We more than tripled our activity in 2010 in PEO with option writing, to over 24,000 contracts. In ADX, we wrote only 3,000 calls and 4,000 puts, about half as many as in 2009, because there was not much volatility, hence lower premiums. It really is a function of what's going on in the market. That is what we have done for over 20 years, but on less than 10% of the portfolio.

Performance* as of December 31, 2010

Market Price (USD) Return Net of Fees	1 Year	3 Year Annualized	5 Years Annualized
Adams Express Company			
ADX – NAV	11.2%	-1.6%	3.1%
ADX – Market	11.5%	-3.5%	3.0%
Petroleum & Resources Corporation			
PEO – NAV	20.8%	-2.7%	6.9%
PEO – Market	19.6%	-3.4%	6.0%

*Investment involves risk, and past performance figures shown above are not indicative of future performance.

Update On Petroleum & Resources

Petroleum & Resources Corporation began trading on the New York Stock Exchange in January 1929 with a focus on investing primarily in energy and natural resources. It is designed for investors who seek a broadly diversified exposure to the sector in a conservatively managed fund. Investments are made with an eye towards protecting shareholders' original investment and generating dividends and capital gains that could be used as a source of income or reinvested to increase their holdings in the Fund.

PEO held 55.4% of its assets in integrated oil and exploration and production companies, including Exxon Mobil, Chevron, Occidental Petroleum, Apache Corp. and Noble Energy, with 16.4% in chemicals, metals, and mining companies, including Freeport-McMoRan Copper & Gold, according to PEO's 2010 annual report.

SL: You have a strong component in exploration and production companies and are also interested in alternate energy as expressed to us for the April 2010 *Scott Letter.* Would you update us on this important issue facing our country in the coming years?

Ober: Alternate energy will, over time, supplant oil and natural gas as the primary source of energy for transportation and generation of power. In the U.S., we are still generating about 50% of our power by burning coal, which is a very dirty source of energy.

There is an issue of water quality everywhere, including the Appalachia area where surface mining is permitted. The same thing is going on in the Marcellus shale region in Pennsylvania and New York where fracturing is a problem affecting water supplies. These are things that companies must pay attention to. We think that some companies are doing that better than others and that the regulatory environment is having a significant impact on what companies are doing. In eastern New York, anywhere near the reservoirs that service New York City, no drilling will be permitted.

SL: What are your thoughts on increasing nuclear power generation?

Ober: I think that, depending on how much the U.S. government is willing to ease the regulation of the nuclear power industry, you will see significant growth in nuclear power over the next 5-10 years.

The miniature nuclear plants that General Atomic is building have some real potential. They could get going faster. In the long term, until our government is willing to make a decision on where waste materials are going to be stored, companies are going to be reluctant to spend money on new plants. There are huge stock piles of nuclear waste at the operating nuclear plants that the utilities don't know how to handle, since there is no safe repository.

[**Editor's Note:** The massive earthquake that forced the closure of four nuclear power plants in Japan has highlighted the grave risks of nuclear power.

"The financial crisis created by crises in Japan and Europe highlight a growing problem. The rich world is getting close to the point where it won't be able to bear the costs of another disaster," writes Mark Whitehouse of *The Wall Street Journal.*

Despite all of the concerns about this earthquake disaster that could easily occur again, Japan appears to have handled this emergency well so far. All countries that have nuclear plants, including the U.S., are having their nuclear specialists review their safety systems now. This is likely to lead to greater scrutiny in nuclear energy plants in the future.

Two kinds of nuclear plants are most likely to be affected by the accident: those that are of similar reactor types to those in Japan and those that are also located on coastal areas around earthquake faults such as those in earthquake-prone California.

Virginia's Dominion Power and Georgia's Southern Company are continuing to develop new plants, despite calls for a slowdown.]

SL: We agree that nuclear power still has a future because it is clean power. When the new plants are on-line, it will be a tremendous improvement in lowering the huge amount of carbon emissions from dirty coal and oil spills.

You must have read the recent *New York Times* report that said natural gas is seen as a way to wean the United States from its dependency on other countries for oil, but it also has environmental dangers in the way it is extracted. This "carries significant environmental risks as it involves injecting huge amounts of water, mixed with sand and chemicals at high pressures to break up rock formations and release the gas." The newspaper also reported that the dangers to the environment are greater than previously understood. Waste water is hauled to sewage plants not designed to treat it and then discharged into rivers that supply drinking water which then contain more pollutants than were previously known.

Ober: George, I read the article with great interest. There is no question that there are companies acting irresponsibly when it comes to the handling of wastewater from drilling. Other companies are recycling 100% of their wastewater and reusing it in their operations. I think the article you cite is very one-sided and quoted scientists with dramatic effect. I also think that there were facts left out, that the attribution to many problems was inaccurate, but it made news. That's what sells newspapers.

SL: This is a continuing and changing problem, as the development of renewable energy remains a key issue of our times.

We hope this will help to make our readers better informed about ADX, PEO and the closed-end fund industry. They have served long-term investors well.

Ober: I'd like to thank you and John for your continued support of the closed-end fund industry. We strongly believe there is a place for closed-end funds with their particular characteristics in individual investment portfolios.

SL: Thanks, Doug. ■

Disclosure: George Cole Scott and his family own shares of ADX and PEO.

Exchange Traded Funds Are Hot News, but It Isn't Always Good News

Investors have poured some $4.5 billion into domestic exchange traded funds (ETFs) lately, nearly 10 times the amount they put into foreign stock ETFs, according to fund-tracker Lipper in a *Wall Street Journal* report.

Recently, more and more investors have taken a shine to ETFs that focus on specific sectors, but the holdings, weightings and costs of these ETFs can vary greatly, boosting or hurting performance. In fact, some analysts argue that the growth of ETFs makes them look like they are actively managed mutual funds or individual stocks. They are neither but are unique beta instruments. Beta is the exposure that an investor gets to, say, the S&P 500 index or to financial stocks.

An ETF is designed to trade more or less in lockstep with its underlying index, hence the beta exposure. These "funds" get a letter grade based on three criteria: efficiency, tradability and fit.

Despite these advantages, some executives are calling for regulations to address the suitability requirements for the sale of sophisticated versions, such as commodities and leveraged fund ETFs. They have good reason to be championing greater control over investments in these funds.

ETFs have been growing rapidly, surpassing $1 trillion in assets at the end of 2010, and a chunk of that is from retail investors. Sector ETFs, with the most assets in materials, are aimed more at financial advisors. They are growing even more quickly, up 22% for the year ending December 31, 2010 and had $205 billion in assets.

Sector ETFs are generally used for tactical investing in a portfolio where you are trying to overweight parts of the market because you are bullish on tech, energy or whatever. Tradability essentially measures liquidity, crucial for hedge funds, which move in and out of an ETF frequently.

Efficiency measures how well an ETF tracks its benchmark. For example, one ETF gets a high mark because of its low expense ratio. However, just because a mutual or closed-end fund has a higher expense ratio doesn't mean that it will trail in performance.

A recent report in the *Financial Times* notes that the SEC is investigating whether ETFs are being used to hide large bets based on inside information.

Why are we writing about ETFs? We firmly believe that closed-end funds continue to be one of the best ways to invest and, unlike hedge funds, are strictly regulated by the Investment Company Act of 1940.

Closed-end funds have the advantages of being able to trade at discounts to net asset values that are not available to ETFs. They also give investment protection to investors. The discounts leverage their returns.

What is really happening is that more and more traders are targeting closed-end funds just for short-term profits. We are hoping that the SEC will enact new restrictions on the growing menace of hedge funds and their continuing threat to our industry.

It is interesting to also note that some hedge funds are now liquidating, largely because of poor performance.

Primarily because Adams Express was attacked by a hedge fund and a group of associates, we have continuing concerns about the closed-end fund industry and will again report on this issue in the future.

Closed-end funds have served investors well for nearly 200 years when they were first founded in Brussels, Belgium in 1822 by King William I of the Netherlands. Enough said. ■

Sources: *Barron's, Investment News*

Portfolio Manager's Review

Equity closed-end funds strung together their third consecutive month of positive returns in February, adding 2.49% on a NAV basis and 2.49% on a market basis. Resurging geopolitical risks and buying opportunities gave fixed income funds their first positive returns in four months. CEFs rose 1.98% on a NAV basis and 1.57% on a market basis, respectively, with the pariahs of late – municipal bond funds – leading the charge. (Source: Lipper)

Economic numbers have improved lately, and investors remain bullish. Even after the events in Egypt, Libya and other Middle East nations, the economy was cheered by a jump in new housing starts and durable goods orders, encouraging earnings reports and a rise in personal income that is expected to continue.

In this interview, Doug Ober shows that he remains a clear-thinking spokesman for the closed-end fund industry. He was the first president of the Closed-End Fund Association and continues today to speak to investment groups around the country about the long-term values of investing in in closed-end funds.

Doug continues to inspire others in showing that closed-end funds are the best way to achieve consistent returns, and can provide steady flows of income to investors.

CEFA will attend the annual meeting of the Closed-End Fund Association in New York on April 5 and expects the hot topic to be the threat to our industry from increasing numbers of activists, led by hedge funds.

Some of these funds have been able to force smaller CEFs to hold tender offers which can substantially reduce fund assets and raise their expense ratios. Adams Express was able to deter these destructive actions, but the smaller funds are much more vulnerable.

The Board and shareholders of Adams Express realized that it was in shareholders' best interests to vote against this kind of action. Despite threats, our industry remains strong, and new funds continue to come to market. All of us are becoming increasingly aware of this threat to the industry and are taking action to deter it.

CEFA continues its mission to educate all investors on the virtues of closed-end funds. We occasionally will use mutual funds but only when we cannot find a closed-end in the same area, such as the Winslow Green Growth Fund, that has no counterpart in our industry.

We also try to make a clear case that investors should not to be deterred by geopolitical events such as the turmoil in the Middle East and pay more attention to the continued global economic recovery as this has been proven to be what drives stock markets.

These events can upset stock markets in the short-term, but history shows that economic fundamentals always overshadow these concerns. ■

George Cole Scott

Letter to the Editor

George, in reading your interview with Mark Mobius, I believe you are correct on Brazil. It already has had some major expansion, and the upcoming sporting events in the next few years are sure to spawn more growth. I did not know about the dam projects there. It is disturbing. My firm belief is that all humans, everywhere, need to figure out how to have a fruitful and exciting life, without consuming so much energy and resources.

Kindest regards,
Adam J. Haller, CFA, Richmond, VA

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We encourage readers to send us their thoughts on any aspect of *The Scott Letter* or their views about what is happening in the closed-end fund industry. Please direct your e-mails to our editor-in-chief, George Cole Scott, gscott@cefadvisors.com.

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