Closed-End Fund Review

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First Trust

THIRD QUARTER 2008

Third Quarter 2008 Overview

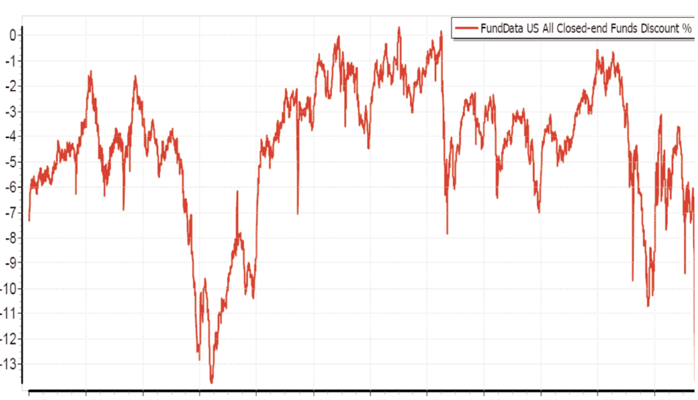
Over the past few weeks, I have spent a good percentage of my time talking to advisors from all over the country about the extreme volatility we have seen in closed-end funds during the third quarter. The two most common questions I receive during these calls are as follows:

1. What do I believe has caused this unprecedented weakness in closed-end funds?
2. What do I think it will take to turn things around for closed-end funds?

I want to address both of these questions in my commentary, but first I want to provide a brief overview of the performance of closed-end funds during the third quarter.

In short, the third quarter was one of the most challenging three month time periods I have ever observed for closed-end funds during my 14-year career in the financial services industry. All 20 of the categories I monitor were lower on a total return net asset value (NAV) basis. As usual, the share prices of closed-end funds tended to overreact relative to NAV performance on both the up and downside, and this quarter was no different with every category lower on a share price total return basis as well. Indeed, every category posted worse share price performance relative to its respective NAV performance. This helped to widen discounts to an average of 16% (according to Lipper) as of the end of the third quarter. In fact, according to *etfconnect.com,* over 100 funds (or nearly 20% of all closed-end funds) traded at a discount of 20% or more. Reflecting the extreme negative sentiment of closed-end fund investors, as well as the elevated state of anxiety in the global financial markets, closed-end funds now trade at their widest discounts in a decade (see chart below) and significantly wider than the 10-year average discounts of between 4-5%.

Average Premium/Discount of all U.S. Traded CEFs



Source: FundData.com

Think Opportunity

Despite these wide discounts and very challenging environment during the third quarter (and much of the past year for that matter), I have not lost my confidence in the closed-end fund structure whatsoever. I strongly believe these discounts represent an excellent long-term buying opportunity for investors who believe that over the coming months and years the equity and credit markets will stabilize and perform better. Ultimately, I believe the most successful closed-end fund investors are the ones who take advantage of these wide discounts and inefficiencies in the marketplace and buy funds for the long-term. I do not know precisely when we will see stability in the global equity and credit markets, but I do firmly believe that when we do, many closed-end funds are poised to outperform because they have been beaten down so dramatically relative to their underlying NAVs.

Below is the three-month share price and NAV performance of all 20 categories I monitor. Please note all numbers are total return. **I believe one of the takeaways from looking at the data below is that due to the global weakness in both the equity and credit markets during the third quarter, NAVs of all 20 categories had meaningful weakness; however, share prices did overreact significantly, and I believe therein lies the opportunity for investors as the financial markets stabilize.**

Category	Share Price	NAV
Convertibles (hybrid)	-26.70%	-16.81%
Investment-Grade (debt)	-14.17%	-8.66%
Multi-Sector (debt)	-24.49%	-11.88%
Domestic Equity (equity)	-18.12%	-12.79%
Sector Specific (equity)	-16.47%	-8.13%
Global Income (debt)	-12.58%	-5.47%
General Mortgage (debt)	-11.62%	-4.10%
Growth & Income (hybrid)	-25.27%	-9.43%
Government (debt)	-9.45%	-4.02%
Covered Call (equity)	-21.22%	-10.11%
High Yield (debt)	-26.98%	-13.72%
International Equity (equity)	-26.38%	-22.20%
Senior Loan (debt)	-24.82%	-12.16%
National Municipal (debt)	-15.85%	-8.36%
California Municipal (debt)	-13.52%	-8.52%
New York Municipal (debt)	-14.23%	-8.08%
Other State Municipal (debt)	-12.11%	-8.31%
Emerging Market Debt (debt)	-18.14%	-7.93%
REITs (equity)	-23.83%	-11.42%
Preferreds (hybrid)	-40.26%	-32.29%

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(Cont'd)

Why The Extreme Volatility in Closed-End Funds?

I believe the main reason closed-end funds were hit so hard was due to the very weak and volatile quarter the global equity and credit markets had. This directly impacted the NAVs of closed-end funds and explains why NAVs were down anywhere from 4% to 32% for the quarter. However, as I stated above, share prices of most closed-end funds were hit much harder than underlying NAVs for the quarter, which I believe is more a reflection of the state of panic many investors are in and the extreme negative sentiment which exists in closed-end funds (and many other investments, for that matter.) Furthermore, the low liquidity of many funds also tends to create wide swings in the share price of closed-end funds.

A good way to illustrate the panic and extreme negative sentiment which exists in the marketplace is to cite what happened in ultra-safe investments during the quarter. At one point in September, over $100 billion was withdrawn from money market funds in one week. The one-month U.S. Treasury Bill was yielding 0% as investors flocked to the safety of U.S. Treasury Bills amid an extreme flight to quality. I mention this extreme flight to quality because I think it explains just how significant the rush to safety has been recently. If investors were willing to take 0% just to get their money back from the U.S. Treasury and investors were withdrawing money from money market funds, it details how nervous investors were during the quarter. If they were redeeming their money market funds then they were clearly selling their closed-end funds too, thus leading to historically wide discounts for many funds.

I also believe some of the selling we saw in the third quarter was tax-loss related as investors try to harvest losses in funds they have purchased and have losses in. Furthermore, some of the selling could have been due to margin calls which have forced investors to sell securities to raise cash to meet the calls.

What Will Turn Performance Around?

I believe the most important factor which could lead to better performance for closed-end funds is stability in the global equity and credit markets. I believe that if the equity and credit markets were to stabilize over the coming couple of quarters we would see more investors interested in the attractive yields and discounts available in closed-end funds. As investors become comfortable with taking on more risk as the financial markets stabilize, I believe we will see closed-end funds perform better. Meanwhile, until the global financial markets stabilize, I expect more volatility in closed-end funds. But I also expect most funds to continue to pay out very attractive distributions to shareholders, which are an important contributor to total return performance over time.

Fourth Quarter Outlook

As I stated above, I believe the most important factor impacting the performance of closed-end funds will be if we see stability in the global financial markets in the next quarter. I believe that if the credit markets were to begin to act more normally and the equity markets were to improve, then closed-end funds would perform much better even in the face of the potential for tax-loss selling which typically accelerates as the fourth quarter progresses. While tax-loss selling is usually worse in years when investors have gains to offset or when there have been a lot of initial public offerings (IPOs), I still do expect more tax-loss selling later in the fourth quarter. However, assuming that we see stability in the equity and credit markets by the first quarter of 2009, I believe a further widening of discounts at the end of the fourth quarter would represent a buying opportunity. Historically, discounts narrow the most in the first quarter of the year and funds tend to perform best during the quarter as investors take advantage of the wide discounts and opportunities which have been created due to tax-loss selling.

Recently I have noticed a significant amount of insider buying in closed-end funds. I believe this is very encouraging as it illustrates how many insiders believe the recent weakness has created excellent long-term opportunities. As always, due to the fact that closed-end funds can exhibit periods of high volatility, investors are encouraged to maintain a long-term time horizon and exposure to different types of funds.