

Cohen & Steers Closed-End Fund Strategy

We would like to share with you our review and outlook for the closed-end fund market as of December 31, 2011. For the fourth quarter, the market price total return of the Morningstar U.S. All Taxable ex-Foreign Equity Closed-End Fund Index was +6.2%, while its return on net asset value (NAV) was +7.0%. For the year, the index had a market price total return of +0.7% and a NAV return of +2.0%. By comparison, the S&P 500 Index and the Barclays Capital U.S. Aggregate Bond Index had total returns of +11.8% and +1.1% for the quarter, and +2.1% and +7.8% for the year, respectively.

Investment Review

Closed-end funds had a slightly positive return based on market price in 2011, although this belied a high degree of volatility seen in financial markets during the year. The group made gains through July, but encountered turbulence when it appeared that the global economic recovery was on a weaker trajectory than previously expected. Investor confidence was further eroded by the growing risk of a Greek default, sparking fears of heavy bank losses and fiscal contagion. In addition, the debate over raising the U.S. debt ceiling was followed quickly by a downgrade of the U.S. credit rating by Standard & Poor's.

In the fourth quarter, however, closed-end funds rallied along with equities broadly as late-year U.S. economic data stabilized and demonstrated moderate improvement. Investors also took relief as Europe's fiscal and monetary authorities seemed to get a temporary handle on the region's formidable debt problems.

Fixed income funds outperformed equity funds

Funds that employ fixed income strategies generated a collective gain for the year, while equity-oriented funds had a modest decline. Fixed income funds also outperformed the equity group on a NAV basis, which drove a divergence in valuations. Both categories began the period trading at an approximate 2% discount to their underlying NAVs, but by year end, fixed income funds were valued at a 1% premium, whereas equity funds' discount widened to 6%. This partly reflected the market's greater confidence in fixed income funds' ability to maintain their distribution rates amid market volatility and economic uncertainty. Equity funds are more reliant on capital appreciation in their holdings to sustain payout levels.

Most fixed income sectors advanced in the period, led by taxable municipal funds (+28.3%⁽¹⁾ within the index), which were a strong beneficiary of a flight to quality. Funds focused on preferred securities (+16.8%) were another standout, aided by improvements in the underlying issuers' credit

Closed-End Fund Sector Returns⁽¹⁾

	Q4 2011		YTD	
	Market	NAV	Market	NAV
Taxable Municipal	7.3%	0.3%	28.3%	27.3%
CA State Municipal	6.7%	3.1%	22.4%	18.4%
Municipal High	7.4%	1.8%	20.3%	14.8%
National Municipal	5.8%	3.0%	20.2%	17.1%
NY State Municipal	7.1%	2.7%	19.6%	15.1%
State Municipal-Other	7.2%	2.9%	19.1%	15.4%
Preferreds	7.9%	4.2%	16.8%	7.2%
Health-Biotech	10.7%	10.5%	13.2%	10.3%
Investment Grade	8.6%	3.1%	12.9%	2.0%
U.S. Hybrid (Growth & Income)	8.7%	10.1%	12.4%	10.5%
Utilities	7.0%	9.9%	11.7%	7.5%
High Yield	8.2%	5.6%	9.9%	1.8%
Government	2.8%	2.2%	6.9%	9.6%
Global Income	6.5%	4.1%	6.6%	2.7%
MLP	14.6%	14.9%	6.1%	8.9%
Emerging Market Income	7.0%	3.6%	4.2%	1.9%
Limited Duration	5.2%	3.8%	3.8%	4.0%
Equity Tax-Advantaged	9.8%	12.9%	2.5%	3.9%
General Mortgage	2.3%	0.2%	2.4%	1.5%
Multi-Sector	6.5%	4.8%	2.2%	1.4%
Commodities	-4.9%	-4.4%	0.4%	5.0%
Real Estate	9.1%	11.4%	-0.8%	1.2%
U.S. Equity Dividend	7.1%	11.2%	-2.9%	3.5%
U.S. General Equity	9.0%	12.2%	-3.0%	-2.2%
Senior Loan	4.4%	4.6%	-3.9%	1.6%
Global Hybrid (Growth & Income)	4.6%	7.6%	-6.1%	-4.5%
Covered Call	5.6%	9.7%	-8.2%	-0.4%
Global Equity	4.6%	8.2%	-10.3%	-7.3%
Finance	10.8%	14.7%	-14.2%	-10.0%
Convertibles	4.3%	4.9%	-14.2%	-10.7%
Global Equity Dividend	0.5%	6.0%	-14.4%	-12.0%
Energy-Resources	6.1%	11.0%	-14.9%	-8.9%
International Equity	0.6%	0.5%	-21.4%	-19.3%

Source: Bloomberg.

This information is not representative of any Cohen & Steers account and no such account will seek to replicate an index. You cannot invest directly in an index.

(1) Sector constituents as per the Morningstar U.S. All Taxable Ex-Foreign Equity Index; constituent returns as per Bloomberg L.P.

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profiles. Investment grade funds (+12.9%) also performed well. A notable underperformer was the convertible bond group (-14.2%), which tends to have a greater sensitivity to conditions in equity markets. The senior loan funds sector (-3.9%) also declined, hindered by delayed expectations for a return to interest-rate increases by the Federal Reserve (senior loans have short durations).

The equity funds category had mixed results. Utilities (+11.7%) and health care (+13.2%) funds were among the winners, favored for their more stable cash flows in an uncertain environment. Concerns over slowing global growth weighed on the global equity (-10.3%), global equity dividend (-14.4%) and energy/resources (-14.9%) groups.

Closed-end fund IPOs were steady

New issuance of closed-end funds occurred at a modest but steady pace through the year, with an increasing shift in favor of equity strategies. The total issuance from new funds in 2011 was \$5.9 billion, about 20% lower than the amount raised in 2010.

Investment Outlook

The U.S. economic picture has brightened modestly in recent weeks, a positive for equities and credit markets, and we expect slow but sustained growth. However, Europe remains a market risk. While recent fiscal, political and central bank initiatives to address the sovereign credit crisis in Europe are somewhat encouraging, the political landscape remains very uncertain, and economic austerity measures will weigh on growth.

With interest rates likely to remain near historical lows for an extended period, we believe that attractive spreads should continue to benefit the income-generating potential of leveraged closed-end funds. As for new closed-end fund issuances, we believe the IPO window will remain open, but not to the degree that could pressure pricing in the secondary market or impede discount narrowing (or premium expansion) as investors bid for above-average income.

In terms of sector allocation, one noteworthy move was our recently increased position in senior loan funds. In addition to offering good income, these funds have become more attractive for their total-return potential based on relative value. Within the commodities group, we have made a shift from pure metals funds in favor of those that own operating companies, which underperformed metals funds in 2011 and appear attractively valued in our view.

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