

# The Closed-End Fund Market in 2005

## KEY FINDINGS

- **Assets in closed-end funds increased for the fourth consecutive year:** At year-end 2005, assets in closed-end funds totaled \$276.3 billion. Closed-end fund assets have increased 93 percent since year-end 2000.
- **Equity funds continue to increase their share of total closed-end fund assets:** While bond funds accounted for nearly two-thirds of closed-end fund assets at year-end 2005, closed-end equity fund assets have grown at a faster rate during the past four years.
- **Closed-end fund owners tend to be experienced investors:** An estimated 2.0 million U.S. households owned closed-end funds in 2005. The typical closed-end fund owner is older, has accumulated more household financial assets, and owns a broader array of investments than the typical U.S. household financial decisionmaker.

## WHAT IS A CLOSED-END FUND?

A closed-end fund is a type of investment company that generally issues a fixed amount of shares which are listed on a stock exchange or traded in the over-the-counter market. The assets of a closed-end fund are professionally managed in accordance with the fund's investment objectives and policies, and may be invested in stocks, bonds, and other securities.

Closed-end funds offer a fixed number of shares to investors during an initial public offering. At some point, a closed-end fund may make additional public offerings of its shares in order to raise additional capital. Once issued, the shares of a closed-end fund are not typically purchased or redeemed directly by the

fund, but rather, investors buy and sell shares in the open market.

Because a closed-end fund does not need to maintain cash reserves or sell securities to meet redemptions, the fund has the flexibility to invest in less liquid portfolio securities. For example, a closed-end fund may invest in securities of very small companies, municipal bonds that are not widely traded, or securities traded in countries that do not have fully developed securities markets. Closed-end funds also have considerable flexibility to borrow against their assets, allowing them to use leverage as part of their investment strategy.

## CLOSED-END FUND ASSETS INCREASE

Assets in closed-end funds grew in 2005, marking the fourth consecutive year of increasing assets. At year-end 2005, assets in closed-end funds reached \$276.3 billion (Figure 1).<sup>1</sup> Closed-end fund assets have grown 93 percent during the last five years. In 2005, closed-end fund assets increased 9 percent.

Bond funds have accounted for the vast majority of assets in closed-end funds for the past decade (Figure 2). At the end of 2005, bond funds held \$171.7 billion, or 62 percent of closed-end fund assets. Equity funds totaled \$104.6 billion, or 38 percent of closed-end fund assets.

FIGURE 1

### CLOSED-END FUND ASSETS INCREASE FOR FOURTH CONSECUTIVE YEAR

Closed-end fund assets at year-end, billions of dollars, 1995–2005

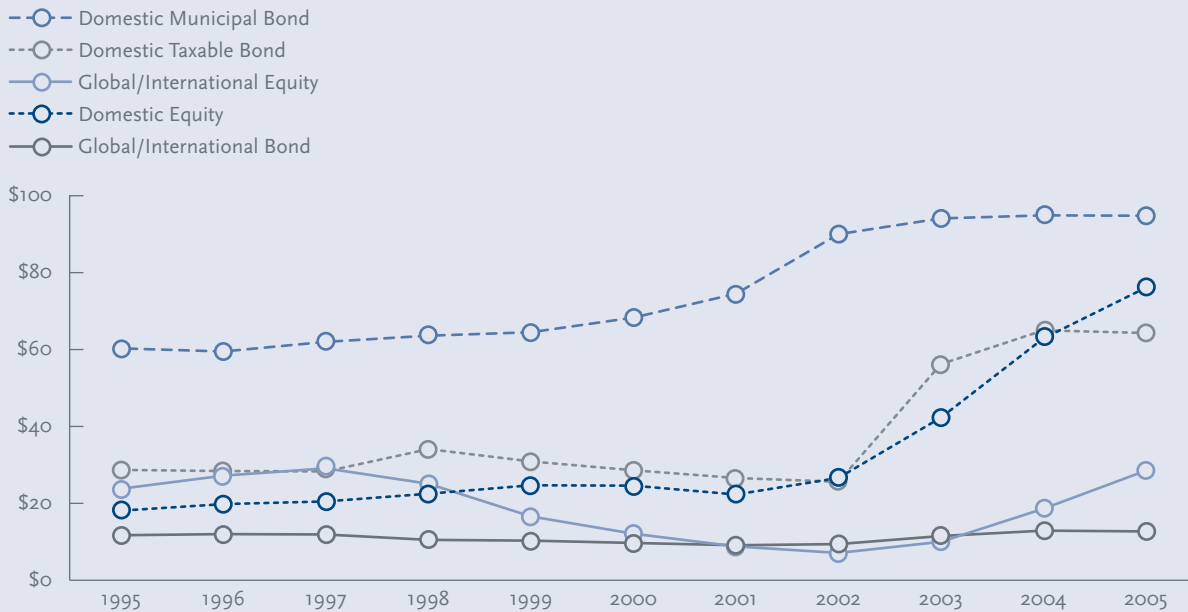


source: Investment Company Institute

FIGURE 2

### BOND FUNDS ARE LARGEST SEGMENT OF CLOSED-END FUND MARKET

Closed-end fund assets at year-end by investment objective, billions of dollars, 1995–2005



source: Investment Company Institute

Equity funds, however, have fueled about half of the recent growth in closed-end fund assets. From year-end 2000 through 2005, assets in closed-end equity funds increased by \$68.0 billion, or 186 percent, while assets in closed-end bond funds rose by \$65.2 billion, or 61 percent.

The role of equity funds in the recent growth of closed-end fund assets is also evident when proceeds from initial and additional public offerings of equity and bond funds are compared. In 2004 and 2005, proceeds from initial and additional public offerings of equity funds greatly exceeded those of bond funds; the reverse was true in 2002 and 2003 (Figure 3).

## NUMBER OF CLOSED-END FUNDS INCREASES

The number of closed-end funds available to investors has also increased over the past several years. At the end of 2005, there were 634 closed-end funds, up from 482 at the end of 2000 (Figure 4). As with closed-end fund assets, equity funds accounted for about half of the increase in the number of closed-end funds during this five-year period. While the majority of these equity funds invest in a broad mix of U.S. companies, many of the closed-end equity funds introduced since 2002 have been real estate and energy sector funds.

**FIGURE 3**

### CLOSED-END EQUITY FUND SHARE ISSUANCE SURGES IN 2004 AND 2005

*Proceeds from the issuance of initial and additional public offerings of closed-end fund shares, year-end, millions of dollars, 2002–2005<sup>1</sup>*

	2002	2003	2004	2005
<b>Total Proceeds From Closed-End Fund Share Issuance</b>	24.9	41.0	27.9	21.2
Equity fund share issuance	9.2	10.8	21.2	19.2
Bond fund share issuance	15.7	30.2	6.6	2.1

<sup>1</sup>Data is not available for years prior to 2002.

note: Components may not add to total because of rounding.

source: Investment Company Institute

**FIGURE 4**

### NUMBER OF CLOSED-END EQUITY FUNDS ACCELERATES AFTER 2000–2002 STOCK MARKET CONTRACTION

*Number of closed-end funds, 1995–2005, selected years*

	1995	2000	2001	2002	2003	2004	2005
<b>All Closed-End Funds</b>	500	482	493	545	586	619	634
<b>Equity Closed-End Funds</b>	141	123	116	123	130	157	191
Domestic	49	53	51	63	74	95	119
Global/International	92	70	65	60	56	62	72
<b>Bond Closed-End Funds</b>	359	359	377	422	456	462	443
Domestic	326	329	349	397	429	432	412
Taxable	119	109	109	105	131	137	131
Municipal	207	220	240	292	298	295	281
Global/International	33	30	28	25	27	30	31

source: Investment Company Institute

## CLOSED-END FUND OWNERS ARE EXPERIENCED INVESTORS WITH DIVERSIFIED PORTFOLIOS

An estimated 2.0 million U.S. households held closed-end funds in 2005 as part of their investment portfolios.<sup>2</sup> These households tend to include affluent, experienced investors who own a range of equity and fixed-income investments. In 2005, 95 percent of closed-end fund investors also owned individual stock either directly or through mutual funds (Figure 5). Seventy percent owned individual bonds, bond mutual

funds, or fixed annuities. In addition, nearly half of these investors owned investment real estate.

Because a large number of closed-end fund investors also own individual stock and mutual funds, closed-end fund investors are similar in many respects to the individuals who own these investments. For instance, closed-end fund investors, like individual stock and mutual fund investors, tend to be college-educated and have household incomes above the national average (Figure 6).

**FIGURE 5**

### CLOSED-END FUND INVESTORS OWN A BROAD RANGE OF INVESTMENTS

*Percent of closed-end fund investors owning each type of investment,<sup>1</sup> 2005*

<b>Stock Mutual Funds or Individual Stock</b>	95
<b>Bond Mutual Funds, Individual Bonds, or Fixed Annuities</b>	70
<b>Mutual Funds (total)</b>	89
Stock mutual funds	69
Bond mutual funds	54
Hybrid mutual funds	57
Money market mutual funds	57
<b>Individual Stock (total)</b>	86
Individual stock other than company stock	81
Company stock through employer	30
<b>Individual Bonds</b>	33
<b>Annuities (total)</b>	44
Variable annuities	39
Fixed annuities	19
<b>Investment Real Estate</b>	46

<sup>1</sup>Multiple responses are included.

source: Investment Company Institute

Nonetheless, closed-end fund investors exhibit certain characteristics that distinguish them from individual stock and mutual fund investors. For example, closed-end fund investors tend to have much greater household financial assets than either individual stock or mutual fund investors.

Closed-end fund investors are also more likely to be self-employed or retired from their lifetime occupations than either individual stock or mutual fund investors.

Ownership of bond investments traditionally has been greatest among older individuals and households in the highest income and wealth groups.<sup>3</sup> Because bond funds account for a large portion of closed-end fund assets, investors in these funds tend to have demographic characteristics similar to those of bond investors in general.

**FIGURE 6**  
**CLOSED-END FUND INVESTORS HAVE ABOVE-AVERAGE HOUSEHOLD INCOMES, FINANCIAL ASSETS**

	All U.S. Households <sup>1</sup>	Households Owning Closed-End Funds <sup>1</sup>	Households Owning Mutual Funds <sup>2</sup>	Households Owning Individual Stock <sup>3</sup>
<b>Median</b>				
Age of head of household	47	50	48	53
Household income	\$45,000	\$75,000	\$68,700	\$74,000
Household financial assets <sup>4</sup>	\$60,000	\$370,400	\$125,000	\$205,000
<b>Percent</b>				
Household primary or co-decisionmaker for investing:				
Married	53	52	71	74
Widowed	11	19	5	8
Four-year college degree or more	38	59	56	64
Employed (full- or part-time)	66	60	77	64
Self-employed <sup>5</sup>	18	36	16	24
Retired from lifetime occupation	26	46	21	35
Household owns:				
IRA	41	64	69	73
Defined contribution retirement plan account	53	57	64	62

<sup>1</sup>Investment Company Institute Annual Mutual Fund Tracking Survey, 2005  
<sup>2</sup>Investment Company Institute, Profile of Mutual Fund Shareholders, Fall 2004  
<sup>3</sup>Investment Company Institute and Securities Industry Association, Equity Ownership in America, 2005  
<sup>4</sup>Household financial assets excludes primary residence, but includes assets in employer-sponsored retirement plans.  
<sup>5</sup>among those who are employed  
note: Number of respondents varies.  
sources: Investment Company Institute and Securities Industry Association

## NOTES

<sup>1</sup> See the Investment Company Institute's (ICI) Closed-End Fund Survey. The survey was conducted annually from 1988 through 2001, and quarterly since 2002.

<sup>2</sup> Based on a June 2005 ICI survey of 3,000 randomly selected U.S. households. The survey's standard error for the sample of 3,000 households is +/- 1.8 percentage points at the 95 percent confidence level. The sample is weighted to match the age distribution of the U.S. population. The number of U.S. households owning closed-end funds is based on the U.S. Census Bureau's estimate of 113.1 million total U.S. households as of March 2005 (see U.S. Census Bureau, Current Population Reports, Series P60-229, *Income, Poverty, and Health Insurance Coverage in the United States: 2004*, August 2005 ([www.census.gov/prod/2005pubs/p60-229.pdf](http://www.census.gov/prod/2005pubs/p60-229.pdf))).

<sup>3</sup> See Brian K. Bucks, Arthur B. Kennickell, and Kevin B. Moore, "Recent Changes in U.S. Family Finances: Evidence from the 2001 and 2004 Survey of Consumer Finances," *Federal Reserve Bulletin* (2006), p. A14 ([www.federalreserve.gov/pubs/bulletin/2006/financesurvey.pdf](http://www.federalreserve.gov/pubs/bulletin/2006/financesurvey.pdf)).

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