ROYCE VALUE TRUST INC
Form 497H2
October 07, 2003

PROSPECTUS

8,800,000 SHARES

ROYCE VALUE TRUST, INC.
5.90% CUMULATIVE PREFERRED STOCK
LIQUIDATION PREFERENCE $25.00 PER SHARE

The 5.90% Cumulative Preferred Stock, initial liquidation preference $25.00 per share (the "Cumulative Preferred Stock") is being offered by Royce Value Trust, Inc. (the "Fund"). The Fund is a closed-end diversified management investment company. The Fund's primary investment goal is long-term capital growth. The Fund normally invests at least 75% of its assets in the equity securities of small- and micro-cap companies. The Fund's address is 1414 Avenue of the Americas, New York, New York 10019, and its telephone number is (212) 355-7311. Royce & Associates, LLC ("Royce") is the Fund's investment adviser.

Dividends on the Cumulative Preferred Stock offered hereby, at the annual rate of 5.90% of the initial liquidation preference of $25.00 per share, are cumulative from the Date of Original Issue thereof and are payable quarterly on March 23, June 23, September 23 and December 23, commencing on December 23, 2003.

(Continued on following page)

INVESTING IN THE CUMULATIVE PREFERRED STOCK INVOLVES RISKS. SEE "PROSPECTUS SUMMARY -- SPECIAL CONSIDERATIONS AND RISK FACTORS" BEGINNING ON PAGE 9 AND "INVESTMENT GOAL, POLICIES AND RISKS" BEGINNING ON PAGE 22.

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved these securities or passed upon the adequacy of this prospectus. Any representation to the contrary is a criminal offense.

	Per Share
Public Offering Price (1)	$ 25.00
Underwriting Discount (2)	$ .7875
Proceeds to the Fund (before expenses)(3)	$24.2125

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(1) Plus accumulated dividends, if any, from October 9, 2003.

(2) The Fund and Royce have agreed to indemnify the Underwriters against certain liabilities, including liabilities under the Securities Act of 1933, as amended.
(3) Offering expenses payable by the Fund are estimated at $281,800.

The Underwriters are offering the Cumulative Preferred Stock subject to various conditions. It is expected that delivery of the Cumulative Preferred Stock will be made in book-entry form through the facilities of The Depository Trust Company ("DTC") on or about October 9, 2003.

Joint Book-Running Managers

Citigroup   UBS Investment Bank

Merrill Lynch & Co.   Wachovia Securities

Legg Mason Wood Walker
Incorporated

October 6, 2003

(Continued from cover page)

Application will be made to list the Cumulative Preferred Stock on the New York Stock Exchange (the "NYSE"). If offered, trading of the Cumulative Preferred Stock on the NYSE is expected to commence within 30 days of the date of this Prospectus. Prior to this offering, there has been no public market for the Cumulative Preferred Stock. See "Underwriting".

Distributions paid on the Cumulative Preferred Stock will consist of: (i) long-term capital gains, (ii) qualified dividend income, (iii) other ordinary income and/or (iv) returns of capital. The Jobs and Growth Tax Relief Reconciliation Act of 2003 (the "2003 Tax Act") reduced the individual Federal income tax rate on long-term capital gains and qualified dividend income to a maximum of 15%. Under the 2003 Tax Act, the maximum individual Federal income tax rate on other ordinary income is 35%. These tax rates are scheduled to apply through 2008. Assuming the 2003 Tax Act had been in effect during the past one, three and five years ended December 31, 2002, approximately 100%, 86% and 88% of the distributions paid by the Fund would have consisted of less highly taxed long-term capital gains and qualified dividend income. It is currently expected that dividends paid on the Cumulative Preferred Stock will consist primarily of such long-term capital gains and qualified dividend income, which are taxed at lower rates for individuals than other ordinary income. See "Tax Attributes of Preferred Stock Dividends" and "Taxation". No assurance can be given, however, as to what percentage, if any, of the dividends paid on the Cumulative Preferred Stock will consist of long-term capital gains and qualified dividend income.

It is a condition to the issuance of the Cumulative Preferred Stock that it be rated Aaa by Moody's Investors Service, Inc. ("Moody's"). In connection with the receipt of such rating, the Fund will be required to maintain a discounted asset coverage with respect to the Cumulative Preferred

Stock reflecting guidelines established by Moody's. See "Rating Agency Guidelines".

The Cumulative Preferred Stock is subject to mandatory redemption, in whole or in part, by the Fund for cash at a price equal to $25.00 per share plus accumulated but unpaid dividends (whether or not earned or declared) through the date of redemption (the "Redemption Price") if the Fund fails to maintain a quarterly asset coverage of at least 200% or fails to maintain the discounted asset coverage required by Moody's. Commencing October 9, 2008 and thereafter, the Fund at its option may redeem the Cumulative Preferred Stock, in whole or in part, for cash at a price equal to the Redemption Price. Prior to October 9, 2008, the Cumulative Preferred Stock will be redeemable, at the option of the Fund, for cash at a price equal to the Redemption Price, only to the extent necessary for the Fund to continue to qualify for tax treatment as a regulated investment company. See "Description of Cumulative Preferred Stock -- Redemption".

If the Fund voluntarily terminates compliance with the Moody's guidelines, the Fund will no longer be required to maintain the discounted asset coverage required by Moody's. However, at the time of such termination, the Cumulative Preferred Stock must have received a rating from at least one nationally recognized statistical rating organization that is at least comparable to the then current rating from Moody's. The Fund will then be required to comply with the guidelines established by such successor rating organization. See "Rating Agency Guidelines" and "Description of Cumulative Preferred Stock -- Termination of Rating Agency Guidelines".

This Prospectus concisely sets forth certain information an investor should know before investing and should be retained for future reference.

A Statement of Additional Information dated October 6, 2003 has been filed with the Securities and Exchange Commission and is incorporated by reference in this Prospectus. The table of contents of the Statement of Additional Information appears on page 47 of this Prospectus. A copy of the Statement of Additional Information may be obtained without charge by writing to the Fund at its address at 1414 Avenue of the Americas, New York, New York 10019, or by calling the Fund toll-free at (800) 221-4268.

IN CONNECTION WITH THIS OFFERING, THE UNDERWRITERS MAY OVER-ALLOT OR EFFECT TRANSACTIONS WHICH STABILIZE, MAINTAIN OR OTHERWISE AFFECT THE MARKET PRICE OF THE CUMULATIVE PREFERRED STOCK, INCLUDING THE ENTRY OF STABILIZING BIDS, SYNDICATE COVERING TRANSACTIONS OR THE IMPOSITION OF PENALTY BIDS. FOR A DESCRIPTION OF THESE ACTIVITIES, SEE "UNDERWRITING".

YOU SHOULD RELY ON THE INFORMATION CONTAINED IN OR INCORPORATED BY REFERENCE INTO THIS PROSPECTUS. NEITHER THE FUND NOR THE UNDERWRITERS HAVE AUTHORIZED ANY OTHER PERSON TO PROVIDE YOU WITH DIFFERENT INFORMATION. IF ANYONE PROVIDES YOU WITH DIFFERENT OR INCONSISTENT INFORMATION, YOU SHOULD NOT RELY ON IT. NEITHER THE FUND NOR THE UNDERWRITERS ARE MAKING AN OFFER TO SELL THESE SECURITIES IN ANY JURISDICTION WHERE THE OFFER OR SALE IS NOT PERMITTED. YOU SHOULD ASSUME THAT THE INFORMATION APPEARING IN THIS PROSPECTUS IS ACCURATE AS OF THE DATE ON THE FRONT COVER OF THIS PROSPECTUS ONLY.

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PROSPECTUS SUMMARY

This is only a summary. You should review the more detailed information included elsewhere in this Prospectus and the Statement of Additional Information. Capitalized terms not otherwise defined in this Summary are defined in the Glossary that appears at the end of this Prospectus.

THE FUND.......... Royce Value Trust, Inc. (the "Fund") has been engaged in business as a closed-end diversified management investment company since its initial offering in November 1986. The Fund's primary investment goal is long-term capital growth. Royce & Associates, LLC ("Royce"), the Fund's investment adviser, normally invests at least 75% of the Fund's assets in the equity securities of small- and micro-cap companies, generally with stock market capitalizations ranging from $100 million to $2 billion, that Royce believes are trading significantly below its estimate of their current worth. The Fund may also invest up to 25% of its assets in non-convertible fixed income securities. See "Investment Goal, Policies and Risks".

THE OFFERING....... The Fund is offering 8,800,000 shares of 5.90% Cumulative Preferred Stock, par value $.001 per share, initial liquidation preference $25.00 per share (the "Cumulative Preferred Stock"), at a purchase price of $25.00 per share.

USE OF PROCEEDS.... The Fund will use a substantial portion of the net proceeds from the offering of the Cumulative Preferred Stock to redeem the issued and outstanding shares of 7.80% Cumulative Preferred Stock, par value $.001 per share, of the Fund (the "7.80% Preferred"), and the issued and outstanding shares of 7.30% Tax-Advantaged Cumulative Preferred Stock, par value

$.001 per share, of the Fund (the "7.30% Preferred"). In order for the Fund to redeem the 7.80% Preferred and the 7.30% Preferred, the Fund must pay the 7.80% Preferred's aggregate initial liquidation preference of $60,000,000 and the 7.30% Preferred's aggregate initial liquidation preference of $100,000,000, plus an amount equal to accumulated and unpaid dividends (whether or not earned or declared) on the 7.80% Preferred and the 7.30% Preferred through the applicable redemption date. Royce expects to use any proceeds remaining after the redemption of the 7.80% Preferred and the 7.30% Preferred to purchase additional

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portfolio securities in accordance with the Fund's investment goal and policies. See "Use of Proceeds".

DIVIDENDS.......... Dividends on the Cumulative Preferred Stock, at the annual rate of 5.90% of the initial liquidation preference of $25.00 per share, are cumulative from the Date of Original Issue and are payable, when, as and if authorized by the Board of Directors and declared by the Fund, out of funds legally available therefor, quarterly on March 23, June 23, September 23, and December 23, commencing on December 23, 2003, to the holders of record on the preceding March 6, June 6, September 6 and December 6, respectively. See "Description of Cumulative Preferred Stock-- Dividends".

LONG-TERM CAPITAL GAINS AND QUALIFIED DIVIDEND INCOME ... The Jobs and Growth Tax Relief Reconciliation Act of 2003 (the "2003 Tax Act") reduced the individual Federal income tax rate on long-term capital gains and qualified dividend income to a maximum of 15%. Long-term capital gains and qualified dividend income included in distributions of a regulated investment company (such as the Fund) to its stockholders are generally passed through to such stockholders, including preferred stockholders, and taxed at the related rates. See "Tax Attributes of Preferred Stock Dividends" and "Taxation".

The 15% income tax rate applicable to capital gains and qualified dividend income is scheduled to expire after December 31, 2008. After this date, absent extension or modification of the relevant legislative provisions, long-term capital gains distributions paid by the Fund generally will be taxable at the previously applicable maximum 20% rate, and distributions attributable to qualified dividend income will be taxed to the stockholder at his or her marginal Federal income tax rate (which generally will be higher than 15%).

TAX ATTRIBUTES OF PREFERRED STOCK DIVIDENDS.......... The distributions paid on the Cumulative Preferred Stock will, for Federal income tax purposes, consist of varying proportions of long-term capital gains, qualified dividend income, other ordinary income (including short-term capital gain and interest income and non-qualified dividend income), and/or returns of capital. Ordinary

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income, other than qualified dividend income but including short-term capital gains, interest income and non-qualified dividend income, is referred to in this Prospectus as "Other Ordinary Income". The Fund is required to allocate long-term capital gains, qualified dividend income and/or Other Ordinary Income proportionately among holders of shares of its Common Stock and the Cumulative Preferred Stock offered hereby. Assuming the 2003 Tax Act had been in effect during the past one, three and five years ended December 31, 2002, the distributions of taxable income by the Fund would have consisted of approximately 100%, 86% and 88% long-term capital gains and qualified dividend income and approximately 0%, 14% and 12% Other Ordinary Income. Certain investors in the Cumulative Preferred Stock may realize a tax benefit to the extent that Fund distributions are composed of long-term capital gains and qualified dividend income rather than more highly taxed Other Ordinary Income. See "Tax Attributes of Preferred Stock Dividends". No assurance can be given, however, as to what percentage, if any, of the distributions to be paid on the Cumulative Preferred Stock will consist of long-term capital gains and/or qualified dividend income. To the extent that such distributions do not consist of long-term capital gains and qualified dividend income, they will be paid from Other Ordinary Income taxable at higher Federal income tax rates, or will represent a return of capital.

Subject to statutory limitations, investors may also be entitled to offset the long-term capital gains portion of a Cumulative Preferred Stock dividend with capital losses incurred by such investors. See "Taxation".

RATING............. It is a condition to its issuance that the Cumulative Preferred Stock be issued with a rating of Aaa from Moody's Investors Service, Inc. ("Moody's"). The Articles Supplementary creating and fixing the rights and preferences of the Cumulative Preferred Stock (the "Articles Supplementary") contain certain provisions which reflect guidelines established by Moody's (the "Rating Agency Guidelines") in order to obtain such rating on the Cumulative Preferred Stock on the Date of Original Issue. Although it is the Fund's present intention to continue to comply with the Rating Agency Guidelines, the Board of Directors of the Fund may

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determine that it is not in the best interest of the Fund to continue to comply with the Rating Agency Guidelines. If the Fund voluntarily terminates compliance with the Rating Agency Guidelines, the Fund will no longer be required to maintain the discounted asset coverage required by Moody's. However, at the time of such termination, the Cumulative Preferred Stock must have received a rating from at least one nationally recognized statistical rating organization ("NRSRO") that is at least comparable to the then current rating from Moody's. The Fund will then be required to comply with the guidelines established by such successor NRSRO. See "Description of Cumulative Preferred Stock -- Termination of Rating Agency Guidelines".

ASSET MAINTENANCE.. The Fund will be required to maintain, as of the last Business Day of March, June, September and December of each year, Asset Coverage of at least 200% with respect to the Cumulative Preferred Stock. Assuming the Fund had issued and sold the Cumulative Preferred Stock and redeemed the 7.80% Preferred and the 7.30% Preferred as of June 30, 2003, the Asset Coverage would have been 415%. See "Description of Cumulative Preferred Stock -- Asset Maintenance -- Asset Coverage".

Also, pursuant to the Rating Agency Guidelines, the Fund will be required to maintain, as of each Valuation Date, a Portfolio Calculation for Moody's at least equal to the Basic Maintenance Amount. The discount factors and guidelines for determining the Portfolio Calculation have been established by Moody's in connection with the Fund's receipt from Moody's of a rating on the Cumulative Preferred Stock on the Date of Original Issue of Aaa. See "Description of Cumulative Preferred Stock -- Asset Maintenance -- Basic Maintenance Amount" and "Rating Agency Guidelines".

VOTING RIGHTS...... At all times, holders of shares of Cumulative Preferred Stock and any other Preferred Stock will elect two members of the Fund's Board of Directors, and holders of shares of Cumulative Preferred Stock, any other Preferred Stock and Common Stock, voting as a single class, will elect the remaining directors. However, upon a failure by the Fund to pay dividends on the Cumulative Preferred Stock and/or any other Preferred Stock in an

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amount equal to two full years' dividends, holders of Cumulative Preferred Stock, voting as a separate class together with the holders of any other Preferred Stock, will have the right to elect the smallest number of directors that would constitute a majority of the directors until cumulative dividends have been paid or provided for. Holders of Cumulative Preferred Stock and any other Preferred Stock will vote separately as a class on certain other matters, as required under the Articles Supplementary and the Investment Company Act of 1940, as amended (the "1940 Act").

Except as otherwise indicated in this Prospectus and as otherwise required by applicable law, holders of Cumulative Preferred Stock will be entitled to one vote per share on each matter submitted to a vote of stockholders and will vote together with holders of shares of Common Stock and any other Preferred Stock as a single class. See "Description of Cumulative Preferred Stock -- Voting Rights".

MANDATORY REDEMPTION......... The Cumulative Preferred Stock is subject to mandatory redemption, in whole or in part, by the Fund in the event that the Fund fails to: (i) maintain the quarterly Asset Coverage, or (ii) maintain a Portfolio Calculation at least equal to the Basic Maintenance Amount required by Moody's and does not cure such failure by the applicable cure date. Any such redemption will be made for cash at a price equal to $25.00 per share plus accumulated and unpaid dividends (whether or not earned or declared) through the redemption date (the "Redemption Price"). In the event that shares of Cumulative Preferred Stock are redeemed due to a failure to maintain the quarterly Asset Coverage, the Fund may redeem a sufficient number of shares of Cumulative Preferred Stock so that the asset coverage, as defined in the 1940 Act, of the remaining outstanding shares of Cumulative Preferred Stock and any other Preferred Stock after such redemption is up to 275%. In the event that shares of Cumulative Preferred Stock are redeemed due to a failure to maintain a Portfolio Calculation at least equal to the Basic Maintenance Amount, the Fund may redeem a sufficient number of shares of Cumulative Preferred Stock and any other Preferred Stock so that the Portfolio Calculation exceeds the Basic Maintenance Amount of the remaining outstanding shares of Cumulative Preferred

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Stock and any other Preferred Stock by up to 10%. See "Description of Cumulative Preferred Stock-- Redemption-- Mandatory Redemption".

OPTIONAL REDEMPTION......... Commencing October 9, 2008 and thereafter, the Fund at its option may redeem the Cumulative Preferred Stock, in whole or in part, for cash at a price equal to the Redemption Price. Prior to October 9, 2008, the Cumulative Preferred Stock will be redeemable at the option of the Fund at the Redemption Price, only to the extent necessary for the Fund to continue to qualify for tax treatment as a regulated investment company. See "Description of Cumulative Preferred Stock -- Redemption -- Optional Redemption".

LIQUIDATION PREFERENCE......... The liquidation preference of each share of Cumulative Preferred Stock is $25.00 plus an amount equal to all unpaid dividends accumulated to and including the date fixed for such distribution or payment (whether or not earned or declared but excluding interest thereon). The initial liquidation preference is $25.00 per share. See "Description of Cumulative Preferred Stock -- Liquidation Rights".

LISTING...........	Prior to this offering, there has been no public market for the Cumulative Preferred Stock. Application will be made to list the shares of Cumulative Preferred Stock on the New York Stock Exchange (the "NYSE"). However, during an initial period, which is not expected to exceed 30 days from the date of this Prospectus, the Cumulative Preferred Stock will not be listed on any securities exchange. During such period, the Underwriters intend to make a market in the Cumulative Preferred Stock; however, they have no obligation to do so. Consequently, an investment in the Cumulative Preferred Stock may be illiquid during such period.
SPECIAL CONSIDERATIONS AND RISK FACTORS...	General. The market price for the Cumulative Preferred Stock will be influenced by changes in interest rates, the perceived credit quality of the Cumulative Preferred Stock and other factors. Liquidity. During an initial period which is not expected to exceed 30 days after the date of issuance, the Cumulative Preferred Stock will not be listed on any

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securities exchange. During such period, the Underwriters intend to make a market in the Cumulative Preferred Stock; however, they have no obligation to do so. Consequently, the Cumulative Preferred Stock may be illiquid during such period. No assurance can be provided that listing on any securities exchange or market making by the Underwriters will result in the market for Cumulative Preferred Stock being liquid at any time.

Credit Rating. The credit rating on the Cumulative Preferred Stock could be reduced or withdrawn by Moody's or a successor NRSRO, if any, while an investor holds shares of Cumulative Preferred Stock, either as a result of the Fund's termination of compliance with the Rating Agency Guidelines or otherwise. The credit rating does not eliminate or mitigate the risks of investing in the Cumulative Preferred Stock. A reduction or withdrawal of the credit rating by Moody's or a successor NRSRO, if any, may have an adverse effect on the liquidity and market value of the Cumulative Preferred Stock. See "Description of Cumulative Preferred Stock -- Termination of Rating Agency Guidelines".

Market, Selection and Style Risk. As with any investment company that invests in common stocks, the value of the Fund's portfolio may decline. For example, if an issuer of a common stock in which the Fund invests experiences financial difficulties, defaults on its senior securities, has the credit rating on its senior securities reduced or withdrawn, or otherwise is affected by adverse market factors, the Fund's portfolio will be negatively impacted. In particular, the prices of small- and micro-cap companies are generally more volatile and their markets are generally less liquid relative to larger-cap companies. Therefore, an investment in the Fund may involve more risk of loss than funds investing in larger-cap companies or other asset classes. See "Investment Goal, Policies and Risks -- Risk Factors -- Investing in Small- and Micro-Cap Companies". In addition, different types of investment styles tend to shift into and out of favor with stock market investors, depending on market and economic conditions. The performance of funds that invest in value-style stocks may at times be better or worse than the performance of stock funds that focus on other types of stocks or have a broader investment style.

Declines in the value of the Fund's portfolio may reduce the asset coverage for the Cumulative Preferred Stock or the Fund's income. As indicated above, the Cumulative Preferred Stock is subject to redemption under specified circumstances. To the extent that the Fund experiences a substantial decline in the value of its net assets, it may be required to redeem Cumulative Preferred Stock to restore compliance with the applicable asset maintenance requirements. See "Description of Cumulative Preferred Stock -- Redemption -- Mandatory Redemption". Sufficiently sharp declines in the value of the Fund's assets could leave the Fund with insufficient assets to redeem all of the Cumulative Preferred Stock for the full redemption price.

Indebtedness and Other Preferred Stock. Payments to the holders of Cumulative Preferred Stock of dividends or upon redemption or in liquidation will be subject to the prior payments of interest and repayment of principal then due on any outstanding indebtedness of the Fund and the contemporaneous payment to holders of any other outstanding Preferred Stock of dividends, upon redemption or in liquidation. Assuming the Fund had issued and sold the Cumulative Preferred Stock and redeemed the 7.80% Preferred and the 7.30% Preferred as of June 30, 2003, the Fund would have had no outstanding indebtedness and no Preferred Stock ranking on parity with the Cumulative Preferred Stock offered hereby as to dividends and payment upon liquidation. See "Investment Goal, Policies and Risks -- Borrowing Money and Issuing Senior Securities". The Fund may issue additional Preferred Stock under the circumstances set forth under "Description of Cumulative Preferred Stock -- Limitations on Issuance of Additional Preferred Stock".

Leverage and Borrowing. The Fund is authorized to borrow money. So long as the Cumulative Preferred Stock is rated by Moody's, however, the Fund cannot borrow for investment leverage purposes. Borrowings create an opportunity for greater capital appreciation with respect to the Fund's investment portfolio, but at the same time such borrowing is speculative in that it will increase the Fund's exposure to capital risk. In addition, borrowed funds are subject to interest costs that may offset or exceed the return earned on the borrowed funds.

Restrictions on Dividends and Other Distributions. The Fund has qualified, and intends to remain qualified for Federal income tax purposes, as a regulated investment company. Qualification requires, among other things, compliance by the Fund with certain distribution requirements. If the Fund does not meet the asset coverage requirements set forth in the 1940 Act or the Articles Supplementary, the Fund will be required to suspend distributions to holders of its Common Stock until such asset coverage is restored. See "Description of Cumulative Preferred Stock -- Dividends". Such a limitation on distributions could jeopardize the Fund's ability to meet the above-referenced distribution requirements. Although the Fund presently intends, to the extent possible, to purchase or redeem Cumulative Preferred Stock and/or any other Preferred Stock to maintain its qualification as a regulated investment company, no assurance can be given that such actions can be effected in time to meet the above-referenced distribution requirements.

Redemption. As set forth above, the Cumulative Preferred Stock is subject to both mandatory and optional redemption under specified circumstances at a redemption price equal to $25.00 per share plus accumulated and unpaid dividends (whether or not earned or declared) through the redemption date. Upon redemption, stockholders may not be able to reinvest the proceeds received from the redemption in an investment providing the same or a better rate than that of the Cumulative Preferred Stock.

Certain Corporate Governance Provisions. Certain provisions of the Fund's Charter and Bylaws may have the effect of maintaining the continuity of management and may make it more difficult for the Fund's stockholders to change the majority of the Board of Directors. See "Description of Capital Stock -- Certain Corporate Governance Provisions".

FEDERAL INCOME TAX CONSIDERATIONS..... As set forth above, the Fund has qualified, and intends to remain qualified for Federal income tax purposes, as a regulated investment company. Qualification requires, among other things, compliance by the Fund with certain distribution requirements. Limitations on distributions if the Fund failed to satisfy the Asset Coverage or Portfolio Calculation requirements could jeopardize the Fund's

ability to meet tax-related distribution requirements. The Fund presently intends, however, to the extent possible, to purchase or redeem Cumulative Preferred Stock and/or any other Preferred Stock if necessary in order to maintain compliance with such distribution requirements. See "Taxation" for a more complete discussion of these and other Federal income tax considerations.

INVESTMENT ADVISER............ Royce has served as the investment adviser to the Fund since its inception. Royce also serves as investment adviser to other registered management investment companies, privately offered funds and institutional accounts. As of September 30, 2003, Royce managed approximately $12.6 billion in assets for the Fund and other client accounts.

Charles M. Royce, Royce's President and Chief Investment Officer, is primarily responsible for managing the Fund's portfolio. He is assisted by Royce's investment staff, including W. Whitney George, Senior Portfolio Manager, Managing Director and Vice President, Boniface A. Zaino, Senior Portfolio Manager and Managing Director, and Charles R. Dreifus, Senior Portfolio Manager and Principal, and by Jack E. Fockler, Jr., Managing Director and Vice President. See "Investment Advisory and Other Services-- Portfolio Management" herein and "Directors and Officers" in the Statement of Additional Information.

As compensation for its services under the Investment Advisory Agreement, Royce receives a fee at a rate ranging from 0.5% up to 1.5% per annum of the Fund's average net assets (including assets obtained from the sale of Preferred Stock) for the applicable performance period, depending upon the investment performance of the Fund relative to the investment record of the Standard & Poor's SmallCap 600 Index (the "S&P 600"), determined by comparisons made over rolling periods of 60 months. However, Royce will not receive any fee for any month when the Fund's investment performance, rounded to the nearest whole point, is negative on an absolute basis for the 36-month period then ended. For a more detailed description of the methods by which the advisory fee is determined, see "Investment Advisory and Other Services -- Advisory Fee".

Royce has volunteered to waive the portion of its investment advisory fee attributable to the liquidation preference of the 7.80% Preferred, the 7.30% Preferred and the Cumulative Preferred Stock (net of the liquidation preference of the 7.80% Preferred and the 7.30% Preferred) for any month when the Fund's net asset value average annual total return since the initial issuance of the 7.80% Preferred, the 7.30% Preferred or the Cumulative Preferred Stock fails to exceed the blended dividend rate on those assets.

CUSTODIAN, DIVIDEND-PAYING AGENT, TRANSFER

AGENT AND REGISTRAR.........	State Street Bank and Trust Company, acts as custodian of the cash and other assets of the Fund. Equiserve Trust Company, N.A. acts as transfer agent, dividend-paying agent and registrar for the Fund's shares and as agent to provide notice of redemption and certain voting rights for the Cumulative Preferred Stock. See "Custodian, Dividend-Paying Agent, Transfer Agent and Registrar".

FINANCIAL HIGHLIGHTS

The financial highlights table is intended to help you understand the Fund's financial performance for the periods presented and reflects financial results for a single share of the Fund's Common Stock. The total returns in the table represent the rate that an investor would have earned on an investment in the Fund's Common Stock (assuming reinvestment of all dividends and distributions). The information for the six months ended June 30, 2003 has not been audited and is included in the Statement of Additional Information, which is available upon request. The information for each of the five years in the period ended December 31, 2002 has been audited by Tait, Weller & Baker, whose report, along with the Fund's financial statements, is included in the Statement of Additional Information, which is available upon request.

	Six months ended June 30, 2003 (unaudited)	Years ended December					
		2002	2001	2000	1999	1998	19
NET ASSET VALUE, BEGINNING OF PERIOD..................	$13.22	$17.31	$16.56	$15.77	$15.72	$16.91	$14.
INVESTMENT OPERATIONS(a):							
Net investment income (loss)..................	(0.02)	(0.02)	0.05	0.18	0.26	0.17	0.
Net realized and unrealized gain (loss) on investments..........	1.97	(2.25)	2.58	2.58	1.65	0.67	3.
Total investment operations............	1.95	(2.27)	2.63	2.76	1.91	0.84	4.
DISTRIBUTIONS TO PREFERRED STOCKHOLDERS:							
Net investment income...	-	(0.01)	(0.01)	(0.03)	(0.04)	(0.03)	(0.
Net realized gain on investments..........	-	(0.28)	(0.30)	(0.30)	(0.32)	(0.26)	(0.
Quarterly distributions*	(0.13)	-	-	-	-	-	-

Total distributions to Preferred Stockholders..........	(0.13)	(0.29)	(0.31)	(0.33)	(0.36)	(0.29)	(0.
NET INCREASE (DECREASE) IN NET ASSETS APPLICABLE TO COMMON STOCKHOLDERS RESULTING FROM INVESTMENT OPERATIONS................	1.82	(2.56)	2.32	2.43	1.55	0.55	3.
DISTRIBUTIONS TO COMMON STOCKHOLDERS:							
Net investment income...	-	(0.07)	(0.05)	(0.13)	(0.15)	(0.16)	(0.
Net realized gain on investments............	-	(1.44)	(1.44)	(1.35)	(1.22)	(1.38)	(1.
Quarterly distributions*	(0.65)	-	-	-	-	-	-
Total distributions to Common Stockholders....	(0.65)	(1.51)	(1.49)	(1.48)	(1.37)	(1.54)	(1.
CAPITAL STOCK TRANSACTIONS:							
Effect of reinvestment of distributions by Common Stockholders.....	(0.00)	(0.02)	(0.08)	(0.16)	(0.13)	(0.09)	(0.
Effect of Common Stock Rights offering or Preferred Stock offering	(0.07)	-	-	-	-	(0.11)	-
Total capital stock transactions..........	(0.07)	(0.02)	(0.08)	(0.16)	(0.13)	(0.20)	(0.
NET ASSET VALUE, END OF PERIOD(a)	$14.32	$13.22	$17.31	$16.56	$15.77	$15.72	$16.
MARKET VALUE, END OF PERIOD	$14.94	$13.25	$15.72	$14.438	$13.063	$13.75	$15.0
TOTAL RETURN(b):							
Market Value..............	18.4%***	(6.9)%	20.0%	22.7%	5.7%	1.5%	28
Net Asset Value(a).........	13.8%***	(15.6)%	15.2%	16.6%	11.7%	3.3%	27
RATIOS BASED ON AVERAGE NET ASSETS APPLICABLE TO COMMON STOCKHOLDERS:							
Total expenses (c, d)......	1.47%**	1.72%	1.61%	1.43%	1.39%	1.31%	1.
Management fee expense..	1.30%**	1.56%	1.45%	1.25%	1.18%	1.10%	0.
Interest expense........	-	-	-	-	-	-	0.
Other operating expenses	0.17%**	0.16%	0.16%	0.18%	0.21%	0.21%	0.
Net investment income (loss)	(0.30)%**	(0.09)%	0.35%	1.18%	1.47%	1.11%	1.
SUPPLEMENTAL DATA:							
Net Assets Applicable to Common Stockholders; End of Period (in thousands)......	$699,221	$560,776	$689,141	$623,262	$552,928	$516,963	$494,2
Liquidation Value of Preferred Stock; End of Period (in thousands)................	$160,000	$160,000	$160,000	$160,000	$160,000	$160,000	$60,0
Portfolio Turnover Rate....	12%	35%	30%	36%	41%	43%	
Average Commission Rate Paid (e).................	.0447	.0473	.0515	.0590	.0610	.0632	.06
PREFERRED STOCK:							
Total shares outstanding...	6,400,000	6,400,000	6,400,000	6,400,000	6,400,000	6,400,000	2,400,0
Asset coverage per share...	$134.25	$112.62	$132.68	$122.38	$111.40	$105.78	$165.

Liquidation preference per share.....................	$25.00	$25.00	$25.00	$25.00	$25.00	$25.00	$25.
Average market value per share:							
7.80% Cumulative Preferred Stock (f).....	$26.09	$26.37	$25.70	$23.44	$24.98	$25.91	$25.
7.30% Tax-Advantaged Cumulative Preferred Stock(f)...............	$25.60	$25.82	$25.37	$22.35	$24.24	$25.43	-
NOTES:							
Total amount outstanding (in thousands)............	-	-	-	-	-	-	$27,8
Asset coverage per note....	-	-	-	-	-	-	$2,090.
Average market value per note (f)..................	-	-	-	-	-	-	$107.

	Years ended December 31,	
	1994	1993
NET ASSET VALUE, BEGINNING OF PERIOD.................	$13.47	$12.50
INVESTMENT OPERATIONS(a):		
Net investment income (loss).................	0.04	0.09
Net realized and unrealized gain (loss) on investments............	0.09	2.12
Total investment operations............	0.13	2.21
DISTRIBUTIONS TO PREFERRED STOCKHOLDERS:		
Net investment income...	-	-
Net realized gain (loss) on investments..........	-	-
Quarterly distributions*	-	-
Total distributions to Preferred Stockholders...........	-	-
NET INCREASE (DECREASE) IN NET ASSETS APPLICABLE TO COMMON STOCKHOLDERS RESULTING FROM INVESTMENT OPERATIONS................	0.13	2.21
DISTRIBUTIONS TO COMMON STOCKHOLDERS:		
Net investment income...	(0.01)	(0.09)
Net realized gain on investments............	(1.04)	(1.06)
Quarterly distributions*	-	-

Total distributions to Common Stockholders....	(1.05)	(1.15)
CAPITAL STOCK TRANSACTIONS:		
Effect of reinvestment of distributions by Common Stockholders.....	(0.07)+	(0.01)
Effect of Common Stock Rights offering or Preferred Stock offering	(0.14)	(0.08)
Total capital stock transactions...........	(0.21)	(0.09)
NET ASSET VALUE, END OF PERIOD(a)	$12.34	$13.47
MARKET VALUE, END OF PERIOD	$11.00	$12.875
TOTAL RETURN(b):		
Market Value...............	(6.7)%	14.9%
Net Asset Value(a).........	0.1%	17.3%
RATIOS BASED ON AVERAGE NET ASSETS APPLICABLE TO COMMON STOCKHOLDERS:		
Total expenses (c, d)......	2.01%	1.33%
Management fee expense..	1.21%	1.09%
Interest expense........	0.46%	-
Other operating expenses	0.34%	0.24%
Net investment income (loss)	0.31%	0.74%
SUPPLEMENTAL DATA:		
Net Assets Applicable to Common Stockholders; End of Period (in thousands)......	$269,032	$246,558
Liquidation Value of Preferred Stock; End of Period (in thousands)................	-	-
Portfolio Turnover Rate....	35%	33%
Average Commission Rate Paid (e)..................		
PREFERRED STOCK:		
Total shares outstanding...	-	-
Asset coverage per share...	-	-
Liquidation preference per share.....................	-	-
Average market value per share		
7.80% Cumulative Preferred Stock (f).....	-	-
7.30% Tax-Advantaged Cumulative Preferred Stock(f)...............	-	-
NOTES:		
Total amount outstanding (in thousands)............	$40,000	-
Asset coverage per note....	$768.67	-
Average market value per note (f)..................	$95.62	-

(a) Commencing June 21, 1995 through December 31, 1997, Net Asset Value per share, Net Asset Value Total Returns and Income from Investment Operations were calculated assuming that the then outstanding convertible notes had been fully converted, except when the effect of doing so resulted in a higher Net Asset Value per share than would have been calculated without such assumption. If it were not assumed the Notes had been converted, the Net Asset Value per share would have been increased by $0.31 at December 31, 1997, $0.17 at December 31, 1996 and $0.09 at December 31, 1995.

(b) The Market Value Total Return is calculated assuming a purchase of Common Stock on the opening of the first business day and a sale on the closing of the last business day of each period reported. Dividends and distributions, if any, are assumed for the purposes of this calculation to be reinvested at prices obtained under the Fund's Distribution Reinvestment and Cash Purchase Plan. Net Asset Value Total Return is calculated on the same basis, except that the Fund's net asset value is used on the purchase and sale dates instead of market value. Net Asset Value and Market Value Total Return, assuming a continuous stockholder who fully participated in the primary rights offerings, were 14.22% and 18.90%, 22.42% and 19.55%, 0.94% and -6.53%, and 17.82% and 14.60%, for the six months ended June 30, 2003 and the years ended December 31, 1995, 1994, and 1993, respectively. These returns include the positive impact to a stockholder from participation in the primary subscription of these rights offerings resulting from the purchase of shares in each such offering at a discount to the market price and net asset value of the Fund.

(c) Expense ratios based on total average net assets including liquidation value of Preferred Stock were 1.16%, 1.38%, 1.30%, 1.12%, 1.06%, 1.06%, 0.99%, 1.20%, 2.01%, 2.01% and 1.33% for the six months ended June 30, 2003 and the years ended December 31, 2002, 2001, 2000, 1999, 1998, 1997, 1996, 1995, 1994, and 1993, respectively.

(d) Expense ratios based on average net assets applicable to Common Stockholders before waiver of fees by Royce would have been 1.67%, 1.82%, 1.65%, 1.51%, 1.48%, 1.34%, 1.14%, 1.31%, 2.04% and 2.02% for the six months ended June 30, 2003 and the years ended December 31, 2002, 2001, 2000, 1999, 1998, 1997, 1996, 1995 and 1994, respectively.

(e) For fiscal years beginning after October 1, 1995, the Fund is required to disclose its average commission rate paid per share for purchases and sales of investments.

(f) The average of month-end market values during the period.

* To be allocated to net investment income and capital gains at year-end.

** Annualized.

*** Not annualized.

+ Includes distributions paid January 31, 1994 and December 30, 1994.

TAX ATTRIBUTES OF PREFERRED STOCK DIVIDENDS

The Fund intends to distribute to its stockholders substantially all of its long-term capital gains, qualified dividend income, and Other Ordinary Income. The Fund is a regulated investment company ("RIC"), and a RIC's distributions generally retain their character as long-term capital gains, qualified dividend income, or Other Ordinary Income when received by its preferred and common stockholders. Thus, distributions paid by the Fund to holders of the Cumulative Preferred Stock will, for Federal income tax purposes, consist of varying proportions of long-term capital gains, qualified dividend income, described below, Other Ordinary Income, and/or returns of capital.

The 2003 Tax Act reduced the individual Federal income tax rate on long-term capital gains and qualified dividend income to a maximum of 15%. Qualified dividend income consists of dividends paid by domestic corporations and certain foreign corporations. Under the 2003 Tax Act, the maximum individual Federal income tax rate on Other Ordinary Income is 35%. These tax rates are scheduled to apply through 2008. Assuming the 2003 Tax Act had been in effect during the past one, three and five years ended December 31, 2002, the distributions of taxable income by the Fund would have consisted of approximately 100%, 86% and 88% long-term capital gains and qualified dividend income and approximately 0%, 14% and 12% Other Ordinary Income. No assurance can be given, however, as to what percentage, if any, of the dividends paid on the Cumulative Preferred Stock will consist of long-term capital gains and qualified dividend income, which are taxed at lower rates for individuals than Other Ordinary Income.

Although the Fund is not managed utilizing a tax-focused investment strategy and does not seek to achieve any particular distribution composition, its primary investment goal is long-term capital growth. Accordingly, certain individual investors in the Cumulative Preferred Stock would, under current Federal income tax law, also realize a tax advantage on their investment to the extent that Fund distributions continue to consist primarily of long-term capital gains and qualified dividend income rather than more highly taxed Other Ordinary Income. The Federal income tax characteristics of the Fund and the taxation of its stockholders are described more fully under "Taxation".

ASSUMPTIONS

The following table shows examples of the pure Other Ordinary Income equivalent yield that would be generated by the dividend rate on the Cumulative Preferred Stock, assuming distributions consisting of three different proportions of long-term capital gains, qualified dividend income and Other Ordinary Income for an individual investor in the 35% Federal marginal income tax bracket. In reading these tables, prospective investors should understand that a number of factors could affect the actual composition for Federal income tax purposes of the Fund's distributions each year. Such factors include (i) the Fund's investment performance for any particular year, which may result in varying proportions of long-term capital gains, qualified dividend income, Other Ordinary Income and/or return of capital in the year's distribution and (ii) the timing of the realization of gains and losses during the Fund's taxable year.

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THESE TABLES ARE FOR ILLUSTRATIVE PURPOSES ONLY AND CANNOT BE TAKEN AS AN INDICATION OF THE ACTUAL COMPOSITION FOR FEDERAL INCOME TAX PURPOSES OF THE FUND'S FUTURE DISTRIBUTIONS.

PERCENTAGE OF CUMULATIVE PREFERRED STOCK A CUMULATIVE PREFERRED STOCK

ANNUAL DIVIDEND COMPOSED OF		ANNUAL DIVIDEND RATE OF
		5.90%
LONG-TERM CAPITAL GAINS AND QUALIFIED DIVIDEND INCOME**	OTHER ORDINARY INCOME	IS EQUIVALENT TO AN OTHER ORDINARY INCO
90%	10%	7.53%
75%	25%	7.26%
50%	50%	6.81%

Assuming that long-term capital gains and qualified dividend income comprise 90% of the Cumulative Preferred Stock dividend and that Other Ordinary Income comprises the remaining 10% of that Cumulative Preferred Stock dividend, the following table shows the pure Other Ordinary Income equivalent yields that would be generated at the dividend rate for taxpayers in the indicated tax brackets.

	A CUMULATIVE PREFERRED ANNUAL DIVIDEND RATE
	5.90%
2003 FEDERAL MARGINAL INCOME TAX BRACKET*	IS EQUIVALENT TO AN OTHER ORDINAR
35.0%..	7.53%
33.0%..	7.33%
28.0%..	6.86%
25.0%**..	6.61%

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* Annual taxable income levels corresponding to the 2003 Federal marginal tax brackets are as follows: 35.0% -- over $311,950 for both single and joint returns; 33.0% -- $143,501 - $311,950 for single returns, $174,701 - $311,950 for joint returns; 28.0% -- $68,801 - $143,500 for single returns, $114,651 - $174,700 for joint returns; and 25.0% -- $28,401 - $68,800 for single returns, $56,801 - $114,650 for joint returns. An investor's Federal marginal income tax rates may exceed the rates shown in the above table due to the reduction, or possible elimination, of the personal exemption deduction for high-income taxpayers and an overall limit on itemized deductions. Income also may be subject to certain state, local and foreign taxes. For investors who pay alternative minimum tax, equivalent yields may be lower than those shown above. The tax rates shown above do not apply to corporate taxpayers.

** Assumes that such individuals are taxed at a 15% rate on long-term capital gains and qualified dividend income received from the Fund.

THE FUND

The Fund is a closed-end diversified management investment company, incorporated under the laws of the State of Maryland on July 1, 1986 and registered under the 1940 Act. The Fund commenced operations in November 1986. Assuming the Fund had issued and sold the Cumulative Preferred Stock and redeemed the 7.80% Preferred and the 7.30% Preferred as of June 30, 2003, the Fund would have had 48,820,755 shares of Common Stock issued and outstanding, with an aggregate net asset value of $692,009,396, and 8,800,000 shares of Cumulative Preferred Stock issued and outstanding, with an aggregate initial liquidation preference of $220,000,000. The Fund's principal office is located at 1414 Avenue of the Americas, New York, New York 10019, and its telephone number is (800) 221-4268.

The Fund's primary investment goal is long-term capital growth. Royce normally invests at least 75% of the Fund's assets in the equity securities of small- and micro-cap companies, generally with stock market capitalizations ranging from $100 million to $2 billion, that Royce believes are trading significantly below its estimate of their current worth. The Fund may also invest up to 25% of its assets in non-convertible fixed income securities. An investment in the Fund is not appropriate for all investors. No assurance can be given that the Fund's investment goal will be realized. See "Investment Goal, Policies and Risks".

USE OF PROCEEDS

The net proceeds from the offering of the Cumulative Preferred Stock are estimated at $212,788,200, after deduction of the underwriting discounts and estimated offering expenses payable by the Fund. The Fund will use a substantial portion of the net proceeds from the offering of the Cumulative Preferred Stock to redeem the 7.80% Preferred and the 7.30% Preferred. In order for the Fund to redeem the 7.80% Preferred and the 7.30% Preferred, the Fund must pay the 7.80% Preferred's aggregate initial liquidation preference of $60,000,000 and the 7.30% Preferred's aggregate initial liquidation preference of $100,000,000, plus an amount equal to accumulated and unpaid dividends (whether or not earned or declared) on the 7.80% Preferred and the 7.30% Preferred through the applicable redemption date. Royce expects to invest any proceeds remaining after the redemption of the 7.80% Preferred and the 7.30% Preferred in accordance with the Fund's investment goal and policies within approximately six months from the completion of the offering, depending on market conditions for the types of securities in which the Fund principally invests. Pending any such investment, the proceeds will be held in high quality short-term debt securities and instruments and money market mutual funds. Any delay by Royce in investing such remaining proceeds may hinder the Fund's ability to achieve its investment goal.

CAPITALIZATION

The following table sets forth the capitalization of the Fund as of June 30, 2003, and as adjusted to give effect to the issuance of the Cumulative Preferred Stock and the redemption of the 7.80% Preferred and the 7.30% Preferred.

	OUTSTANDING
Preferred stock, $.001 par value per share, authorized 50,000,000 shares of which the following series have been classified and designated:	
7.80% Cumulative Preferred Stock, authorized 10,000,000 shares, issued and outstanding 2,400,000 shares..........................	$ 60,000,00
7.30% Tax-Advantaged Cumulative Preferred Stock, authorized 10,000,000 shares, issued and outstanding 4,000,000 shares........	100,000,00
5.90% Cumulative Preferred Stock, as adjusted, authorized 8,800,000 shares, issued and outstanding 8,800,000 shares.........	-
	$160,000,00
Common stock, $.001 par value per share:	
Authorized 150,000,000 shares, issued and outstanding 48,820,755 shares..	$ 48,82
Additional paid-in capital....................................	566,557,50
Accumulated net investment loss...............................	(895,29
Accumulated net realized gain on investments..................	15,009,71
Net unrealized appreciation on investments....................	154,131,80
Quarterly and accrued distributions...........................	(35,631,3
Net assets applicable to outstanding common stock..............	$699,221,19

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(1) After deducting underwriting discounts and estimated costs of this offering of $7,211,800.

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PORTFOLIO COMPOSITION

The following tables set forth certain information with respect to the Fund's investment portfolio as of June 30, 2003.

	VALUE
Common stocks..	$ 783,631,54
Preferred stocks...	533,86
Corporate bonds..	1,403,78
U.S. Treasury obligations..	27,649,42
Repurchase agreement...	46,399,00
Total investments..	$ 859,617,61

SECTOR WEIGHTINGS IN COMMON STOCK PORTFOLIO

Technology...	$173,613,75
Industrial Products..	115,236,15
Industrial Services..	115,056,76
Financial Intermediaries...	80,390,76
Health...	70,104,98

Consumer Products	60,162,24
Natural Resources	56,991,87
Financial Services	53,549,51
Consumer Services	44,174,13
Miscellaneous	14,181,95
Utilities	169,40
Total common stocks	$783,631,54

OTHER INFORMATION REGARDING COMMON STOCK INVESTMENTS
Number of issuers....................................
Median market capitalization....................................

INVESTMENT GOAL, POLICIES AND RISKS

INVESTMENT GOAL

The Fund's primary investment goal and one of its fundamental policies is long-term capital growth. Royce normally invests at least 75% of the Fund's assets in the equity securities of small- and micro-cap companies, with stock market capitalizations ranging from $100 million to $2 billion. Stock market capitalization is calculated by multiplying the total number of common shares issued and outstanding by the per share market price of the common stock. See "--Changes in Investment Goal and Policies" below. There are market risks inherent in any investment, and no assurance can be given that the Fund's primary investment goal will be achieved. Although the Fund may seek current income by investing in dividend-paying equity securities of small- and micro-cap companies, this is not the Fund's primary investment goal.

INVESTMENT POLICIES

Royce uses a value method in managing the Fund's assets. In selecting securities for the Fund, Royce evaluates the quality of a company's balance sheet, the level of its cash flows and various measures of a company's profitability. Royce then uses these factors to assess the

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company's current worth, basing this assessment on either what it believes a knowledgeable buyer might pay to acquire the entire company or what it thinks the value of the company should be in the stock market. This analysis takes a number of factors into consideration, including the company's future growth prospects and current financial condition.

Royce invests in securities of companies that are trading significantly below its estimate of the company's "current worth" in an attempt to reduce the risk of overpaying for such companies. Royce's value approach strives to reduce some of the other risks of investing in small- and micro-cap companies (for the Fund's portfolio taken as a whole) by evaluating various other risk factors. Royce attempts to lessen financial risk by buying companies that combine strong balance sheets with low leverage. While no assurance can be given that this risk-averse value approach will be successful, Royce believes that it can reduce some of the risks of investing in the securities of small- and micro-cap companies, which are inherently fragile in nature and whose securities have substantially greater market price volatility. Although Royce's approach to security selection seeks to reduce downside risk to the Fund's portfolio, especially during periods of broad small-cap market declines, it may also potentially have the effect of limiting gains in strong small-cap up markets.

Foreign Investments. The Fund may invest up to 10% of its assets in securities of foreign issuers. Foreign investments involve certain additional risks, such as political or economic instability of the issuer or of the country of issue, fluctuating exchange rates, less government regulation of foreign securities markets and the possibility of imposition of exchange controls, nationalization or expropriation of assets and more difficulty obtaining information on the foreign companies.

Fixed Income Securities. The Fund may invest up to 25% of its assets in direct obligations of the Government of the United States or its agencies and/or in non-convertible preferred stocks and non-convertible debt securities of various issuers, including up to 5% of its net assets in below investment-grade debt securities, also known as high-yield fixed income securities. There are no limits on the maturity or duration of the fixed income securities in which the Fund may invest.

Two of the main risks of investing in fixed income securities are credit risk and interest rate risk. Below investment-grade debt securities may be in the lowest-grade categories of recognized ratings agencies (C in the case of Moody's or D in the case of Standard & Poor's) or may be unrated. High-yield/high-risk investments are primarily speculative and may entail substantial risk of loss of principal and non-payment of interest, but may also produce above-average returns for the Fund. Debt securities rated C or D may be in default as to the payment of interest or repayment of principal. As of the date of this Prospectus, interest rates are near historical lows which makes it more likely that they will increase in the future which could, in turn, result in a decline in the market value of the fixed income securities held by the Fund.

Warrants, Rights or Options. The Fund may invest up to 5% of its assets in warrants, rights or options. A warrant, right or call option entitles the holder to purchase a given security within a specified period for a specified price and does not represent an ownership interest in the underlying security. A put option gives the holder the right to sell a particular security at a specified price during the term of the option. These securities have no voting rights, pay no dividends and have no liquidation rights. In addition, market prices of warrants, rights or call

options do not necessarily move parallel to the market prices of the underlying securities; market prices of put options tend to move inversely to the market prices of the underlying securities.

Securities Lending. The Fund may lend up to 25% of its assets to brokers, dealers and other financial institutions. However, under the Rating Agency Guidelines, the Fund may not lend portfolio securities in excess of 15% of its total assets. The Rating Agency Guidelines may in the future be amended to permit the Fund to lend a greater percentage of its total assets. Securities lending allows the Fund to retain ownership of the securities loaned and, at the same time, to earn additional income. Since there may be delays in the recovery of loaned securities or even a loss of rights in collateral supplied should the borrower fail financially, loans will be made only to parties that participate in a global securities lending program organized and monitored by the Fund's custodian and who are deemed by it to be of good standing. Furthermore, such loans will be made only if, in Royce's judgment, the consideration to be earned from such loans would justify the risk.

The current view of the staff of the Securities and Exchange Commission (the "Commission") is that a fund may engage in such loan transactions only under the following conditions: (i) the fund must receive 100% collateral in the form of cash or cash equivalents (e.g., U.S. Treasury bills or notes) from the borrower; (ii) the borrower must increase the collateral whenever the market value of the securities loaned (determined on a daily basis at the close of regular trading) rises above the value of the collateral; (iii) after giving notice, the fund must be able to terminate the loan at any time; (iv) the fund must receive reasonable interest on the loan or a flat fee from the borrower, as well as amounts equivalent to any dividends, interest or other distributions on the securities loaned; (v) the fund may pay only reasonable custodian fees in connection with the loan; and (vi) the fund must be able to vote proxies on the securities loaned, either by terminating the loan or by entering into an alternative arrangement with the borrower.

Temporary Investments. The assets of the Fund are normally invested in the equity securities of small- and micro-cap companies. However, for temporary defensive purposes (i.e., when Royce determines that market conditions warrant) or when it has uncommitted cash balances, the Fund may also invest in U.S. Treasury bills, domestic bank certificates of deposit, repurchase agreements with its custodian bank covering U.S. Treasury and agency obligations having a term of not more than one week, high-quality commercial paper and money market funds registered under the 1940 Act, or retain all or part of its assets in cash. Accordingly, the composition of the Fund's portfolio may vary from time to time.

Repurchase agreements are in effect loans by the Fund to its custodian, and the agreements for such transactions require the custodian to maintain securities having a value at least equal to the amount loaned as collateral. Repurchase agreements could involve certain risks if the custodian defaults or becomes insolvent, including possible delays or restrictions upon the Fund's ability to dispose of collateral.

CHANGES IN INVESTMENT GOAL AND POLICIES

The Fund's primary investment goal of long-term capital growth is a fundamental policy of the Fund and may not be changed without approvals of the holders of a majority of the Fund's outstanding shares of Common Stock and Cumulative Preferred Stock and any other Preferred Stock, voting together as a single class, and a majority of the Cumulative Preferred Stock and any other Preferred Stock, voting as a separate class (which for this purpose and under the 1940 Act means the lesser of (i) 67% or more of the relevant shares of capital stock of the Fund present or represented at a meeting of stockholders, at which the holders of more than 50% of the outstanding relevant shares of capital stock are present or represented, or (ii) more than 50% of the outstanding relevant shares of capital stock of the Fund). Except as indicated under "Investment Restrictions" in the Statement of Additional Information, the Fund does not consider its other policies, such as seeking current income, to be fundamental, and such policies may be changed by the Board of Directors without stockholder approval or prior notice to stockholders.

The Fund's investment policies are subject to certain restrictions. See "Investment Restrictions" in the Statement of Additional Information.

RISK FACTORS - INVESTING IN SMALL- AND MICRO-CAP COMPANIES

Royce views the large and diverse universe of small-cap companies as having two investment segments or tiers. Royce defines small-cap as those companies with market capitalizations between $400 million and $2 billion; it refers to the segment with market capitalizations less than $400 million as micro-cap.

The securities of small- and micro-cap companies offer investment opportunities and additional risks. They may not be well known to the investing public, may not be significantly owned by institutional investors, and may not have steady earnings growth. In addition, the securities of such companies may be more volatile in price, have wider spreads between their bid and ask prices and have significantly lower trading volumes than larger capitalization stocks. As a result, the purchase or sale of more than a limited number of shares of a small- or micro-cap security may affect its market price. Royce may need a considerable amount of time to purchase or sell its positions in these securities, particularly when other accounts managed by Royce or other investors are also seeking to purchase or sell them. Accordingly, Royce's investment focus on small- and micro-cap companies generally requires it to have a long-term (at least three years) investment outlook for a portfolio security.

The micro-cap segment consists of more than 5,900 companies. These companies are followed by relatively few, if any, securities analysts, and there tends to be less publicly available information about them. Their securities generally have even more limited trading volumes and are subject to even more abrupt or erratic market price movements than are the securities in the upper tier, and Royce may be able to deal with only a few market-makers when purchasing and selling these securities. Such companies may also have limited markets, financial resources or product lines, may lack management depth and may be more vulnerable to adverse business or market developments. These conditions, which create greater opportunities to find securities trading well below Royce's estimate of the company's current worth, also involve increased risk. This leads Royce to more broadly diversify most of the Fund's assets invested in micro-cap stocks by holding proportionately smaller positions in more companies.

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The upper tier of the small-cap universe of securities consists of approximately 1,500 companies. In this segment, there is a relatively higher level of ownership by institutional investors and more research coverage by securities analysts than generally exists for micro-cap companies. This greater attention makes the market for these securities more efficient than that of micro-cap companies because they have somewhat greater trading volumes and narrower bid/ask spreads. As a result, Royce normally employs a more concentrated approach when investing in the upper tier of small-caps, holding proportionately larger positions in a relatively limited number of securities.

RISK FACTORS - LIQUIDITY RISK

During an initial period which is not expected to exceed 30 days after the date of issuance, the Cumulative Preferred Stock will not be listed on any securities exchange. During such period, the Underwriters intend to make a market in the Cumulative Preferred Stock; however, they have no obligation to do so. Consequently, the Cumulative Preferred Stock may be illiquid during such period. No assurance can be provided that listing on any securities exchange or market making by the Underwriters will result in the market for Cumulative Preferred Stock being liquid at any time.

RISK FACTORS - CREDIT RATING RISK

The credit rating on the Cumulative Preferred Stock could be reduced or withdrawn by Moody's or a successor NRSRO, if any, while an investor holds shares of Cumulative Preferred Stock, either as a result of the Fund's termination of compliance with the Rating Agency Guidelines or otherwise. The credit rating does not eliminate or mitigate the risks of investing in the Cumulative Preferred Stock. A reduction or withdrawal of the credit rating by Moody's or a successor NRSRO, if any, may have an adverse effect on the liquidity and market value of the Cumulative Preferred Stock. See "Description of Cumulative Preferred Stock -- Termination of Rating Agency Guidelines".

RISK FACTORS - LEVERAGE AND BORROWING

The Fund is authorized to borrow money. So long as the Cumulative Preferred Stock is rated by Moody's, however, the Fund cannot borrow for investment leverage purposes. Borrowings create an opportunity for greater capital appreciation with respect to the Fund's investment portfolio, but at the same time such borrowing is speculative in that it will increase the Fund's exposure to capital risk. In addition, borrowed funds are subject to interest costs that may offset or exceed the return earned on the borrowed funds.

RISK FACTORS - RESTRICTIONS ON DIVIDENDS AND OTHER DISTRIBUTIONS

The Fund has qualified, and intends to remain qualified for Federal income tax purposes, as a regulated investment company. Qualification requires, among other things, compliance by the Fund with certain distribution requirements. If the Fund does not meet the asset coverage requirements set forth in the 1940 Act or the Articles Supplementary, the Fund will be required to suspend distributions to holders of its Common Stock until such asset coverage is restored. See "Description of Cumulative Preferred Stock -- Dividends". Such a limitation on distributions could jeopardize the Fund's ability to meet the above-referenced distribution requirements. Although the Fund presently intends, to the extent possible, to purchase or redeem

Cumulative Preferred Stock and/or any other Preferred Stock to maintain its qualification as a regulated investment company, no assurance can be given that such actions can be effected in time to meet the above-referenced distribution requirements. See "Taxation" in this Prospectus and the Statement of Additional Information.

RISK FACTORS - REDEMPTION

The Cumulative Preferred Stock is subject to both mandatory and optional redemption under specified circumstances at a redemption price equal to $25.00 per share plus accumulated and unpaid dividends (whether or not earned or declared) through the redemption date. Upon redemption, stockholders may not be able to reinvest the proceeds received from the redemption in an investment providing the same or a better rate than that of the Cumulative Preferred Stock. For a description of the circumstances in which shares of Cumulative Preferred Stock may be redeemed, see "Description of Cumulative Preferred Stock -- Redemption" in this Prospectus.

BORROWING MONEY AND ISSUING SENIOR SECURITIES

The 1940 Act and the Fund's fundamental investment policies and restrictions (see "Investment Restrictions" in the Statement of Additional Information) permit the Fund to borrow money from banks and certain other lenders and to issue and sell senior securities (as defined by the 1940 Act) representing other forms of indebtedness or consisting of Preferred Stock if various requirements are met. Such requirements include initial asset coverage tests of 300% for indebtedness and 200% for Preferred Stock and restrictive provisions concerning Common Stock dividend payments and other distributions, Preferred Stock dividend payments and other distributions (if indebtedness is incurred), stock repurchases and maintenance of asset coverage and giving senior securityholders the right to elect directors in the event specified asset coverage tests are not met or dividends are not paid. While the issuance and sale of senior securities allows the Fund to raise additional cash for investments, it is a speculative investment technique, involving the risk considerations of leverage, potential dilution and increased share price volatility for the Fund's Common Stock. In addition, the Fund may be required to sell investments in order to make required payments to senior securityholders when it may be disadvantageous to do so.

The Cumulative Preferred Stock offered hereby is a senior security, as defined by the 1940 Act, of the Fund, which means, among other things, it is senior in priority to the Fund's Common Stock; however, it will rank junior to any future indebtedness of the Fund. See "Description of Cumulative Preferred Stock". Payments to the holders of Cumulative Preferred Stock of dividends or upon redemption or in liquidation will be subject to the prior payment of interest and repayment of principal then due on any outstanding indebtedness of the Fund.

Assuming the Fund had issued and sold the Cumulative Preferred Stock and redeemed the 7.80% Preferred and the 7.30% Preferred as of June 30, 2003, the Fund would have had 48,820,755 shares of Common Stock issued and outstanding, with an aggregate net asset value of $692,009,396, and 8,800,000 shares of Cumulative Preferred Stock, par value $.001 per share, with an aggregate initial liquidation preference of $220,000,000, issued and outstanding, and no outstanding indebtedness. Accordingly, assuming the Fund had issued and sold the Cumulative Preferred Stock and redeemed the 7.80% Preferred and the 7.30% Preferred as of such date, the Fund could have, under its investment policies and restrictions, issued and sold senior securities

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representing indebtedness of up to approximately $456 million or additional shares of Preferred Stock having an aggregate involuntary liquidation preference of up to approximately $472 million or various combinations of lesser amounts of both securities representing indebtedness and Preferred Stock.

RATINGS AGENCY GUIDELINES

Certain of the capitalized terms used herein are defined in the Glossary that appears at the end of this Prospectus.

Moody's has established guidelines in connection with the Fund's receipt from Moody's of a rating of Aaa for the Cumulative Preferred Stock on the Date of Original Issue. Moody's, an NRSRO, issues ratings for various securities reflecting the perceived creditworthiness of such securities. The guidelines have been developed by Moody's in connection with issuances of asset-backed and similar securities, including debt obligations and various auction rate preferred stocks, generally on a case-by-case basis through discussions with the issuers of these securities. The guidelines are designed to ensure that assets underlying outstanding debt or preferred stock will be sufficiently varied and will be of sufficient quality and amount to justify investment-grade ratings. The guidelines do not have the force of law, but are being adopted by the Fund in order to satisfy current requirements necessary for Moody's to issue the above-described rating for the Cumulative Preferred Stock. The guidelines provide a set of tests for portfolio composition and discounted asset coverage that supplement (and in some cases are more restrictive than) the applicable requirements of Section 18 of the 1940 Act. The Moody's guidelines are included in the Articles Supplementary and are referred to in this Prospectus as the "Rating Agency Guidelines".

The Fund intends to maintain a Portfolio Calculation at least equal to the Basic Maintenance Amount. If the Fund fails to meet such requirement and such failure is not cured by the applicable cure date, the Fund will be required to redeem some or all of the Cumulative Preferred Stock. See "Description of Cumulative Preferred Stock -- Redemption -- Mandatory Redemption". The Rating Agency Guidelines also: (i) exclude certain types of securities in which the Fund may invest from Moody's Eligible Assets and, therefore, from the Portfolio Calculation, (ii) prohibit the Fund's acquisition of futures contracts or options on futures contracts, (iii) prohibit reverse repurchase agreements, (iv) limit the writing of options on portfolio securities and (v) limit the lending of portfolio securities to 15% of the Fund's total assets. Royce does not believe that compliance with the Rating Agency Guidelines will have an adverse effect on its management of the Fund's portfolio or on the achievement of the Fund's investment goal. For a further discussion of the Rating Agency Guidelines, see "Description of Cumulative Preferred Stock".

The Fund may, but is not required to, adopt any modifications to the Rating Agency Guidelines that may hereafter be established by Moody's. Failure to adopt such modifications, however, may result in a change in the Moody's rating or a withdrawal of a rating altogether. In addition, Moody's may, at any time, change or withdraw such rating. The terms of the Cumulative Preferred Stock provide that the interpretation or applicability of any or all of the Rating Agency Guidelines may from time to time be modified by the Board of Directors of the Fund in its sole discretion based on a determination by the Board of Directors that such action is necessary or appropriate with respect to the Cumulative Preferred Stock; provided, however, that

the Board of Directors receives written confirmation from Moody's that any such modification would not impair the then current rating assigned to the Cumulative Preferred Stock by Moody's. Furthermore, under certain circumstances, the Board of Directors of the Fund may determine that it is not in the best interests of the Fund to continue to comply with the Rating Agency Guidelines. If the Fund terminates compliance with the Rating Agency Guidelines, it is likely that Moody's will change its rating on the Cumulative Preferred Stock or withdraw its rating altogether. However, at the time of such termination, the Cumulative Preferred Stock must have received a rating from at least one NRSRO that is at least comparable to the then current rating from Moody's. The Fund will then be required to comply with the guidelines established by such successor NRSRO. It is the Fund's present intention to continue to comply with the Rating Agency Guidelines.

As recently described by Moody's, a preferred stock rating is an assessment of the capacity and willingness of an issuer to pay preferred stock obligations. The rating on the Cumulative Preferred Stock is not a recommendation to purchase, hold or sell such shares, inasmuch as the rating does not comment as to market price or suitability for a particular investor. Moreover, the Rating Agency Guidelines do not address the likelihood that a holder of Cumulative Preferred Stock will be able to sell such shares. The rating is based on current information furnished to Moody's by the Fund and Royce and information obtained from other sources. The rating may be changed, suspended or withdrawn as a result of changes in, or the unavailability of, such information.

INVESTMENT ADVISORY AND OTHER SERVICES

Royce & Associates, LLC (which term as used in this Prospectus includes its corporate predecessor) ("Royce"), a Delaware limited liability company, is an investment advisory firm whose predecessor was organized in February 1967. Royce is registered as an investment adviser under the Investment Advisers Act of 1940, as amended. Royce became investment adviser of the Fund in November 1986, when the Fund commenced operations. Royce also serves as investment adviser to other management investment companies and institutional accounts. As of September 30, 2003, Royce managed approximately $12.6 billion in assets for the Fund and other client accounts. Royce's principal business address is 1414 Avenue of the Americas, New York, New York 10019.

On October 1, 2001, Royce became an indirect wholly-owned subsidiary of Legg Mason, Inc. ("Legg Mason"). On March 31, 2002, Royce's corporate predecessor was merged into Royce Holdings, LLC (a wholly-owned subsidiary of Legg Mason), which then changed its name to Royce & Associates, LLC. As a result of this merger, Royce & Associates, LLC became the Fund's investment adviser and a direct wholly-owned subsidiary of Legg Mason. Founded in 1899, Legg Mason is a publicly-held financial services company primarily engaged in providing asset management, securities brokerage, investment banking and related financial services through its subsidiaries. As of June 30, 2003, Legg Mason's asset management subsidiaries had aggregate assets under management of approximately $215.4 billion.

Under the Fund's Articles of Incorporation, as amended and supplemented (the "Charter"), and Maryland law, the Fund's business and affairs are managed under the direction of its Board of Directors. Investment decisions for the Fund are made by Royce, subject to any

direction it may receive from the Fund's Board of Directors, which periodically reviews the Fund's investment performance.

PORTFOLIO MANAGEMENT

Royce is responsible for the management of the Fund's assets. Royce has been investing in small-cap companies with a value approach for more than 25 years. Its offices are located at 1414 Avenue of the Americas, New York, NY 10019. Charles M. Royce has been the firm's President and Chief Investment Officer during this period. He is also the primary portfolio manager of the Fund.

Royce's investment staff also includes three other Senior Portfolio Managers: W. Whitney George, Managing Director and Vice President; Boniface A. Zaino, Managing Director; and Charles R. Dreifus, Principal. Royce's investment staff is assisted by Jack E. Fockler, Jr., Managing Director and Vice President. Mr. George has been a Portfolio Manager at Royce since 2000, and prior thereto was a Senior Analyst. He has been employed by Royce since 1991. Mr. Zaino joined Royce in April 1998 as a Senior Portfolio Manager and previously was a Portfolio Manager and Group Managing Director at Trust Company of the West (since 1984). Mr. Dreifus joined Royce in February 1998 as a Senior Portfolio Manager and previously was a Portfolio Manager and Managing Director (since June 1995) and

General Partner (from 1983 until June 1995) of Lazard Freres & Co. LLC. Mr. Fockler has been employed by Royce since 1989 as its Director of Marketing.

INVESTMENT ADVISORY AGREEMENT

Under the Investment Advisory Agreement between the Fund and Royce dated October 1, 2001 (the "Investment Advisory Agreement"), Royce determines the composition of the Fund's portfolio, the nature and timing of the changes in it and the manner of implementing such changes; provides the Fund with investment advisory, research and related services for the investment of its assets; and pays all expenses incurred in performing its investment advisory duties under the Investment Advisory Agreement.

The Fund pays all of its own administrative and other costs and expenses attributable to its operations and transactions (except those set forth above), including, without limitation, registrar, transfer agent and custodian fees; legal, administrative and clerical services; rent for its office space and facilities; auditing; preparation, printing and distribution of its proxy statements, stockholder reports and notices; Federal and state registration fees; listing fees and expenses; Federal, state and local taxes; non-affiliated Directors fees; interest on its borrowings; brokerage commissions; and the cost of issue, sale and repurchase of its shares. Thus, unlike most other investment companies, the Fund is required to pay substantially all of its expenses, and Royce does not incur substantial fixed expenses.

ADVISORY FEE

As compensation for its services under the Investment Advisory Agreement, Royce is entitled to receive a fee comprised of a Basic Fee (the "Basic Fee") at the rate of 1% per annum of the Fund's average net assets (including assets obtained from the sale of Preferred Stock) and an adjustment to the Basic Fee based on the investment performance of the Fund in relation to

the investment record of the S&P 600. A rolling period of 60 months ending with the most recent calendar month is utilized for measuring performance and average net assets, as described below.

The Basic Fee for each such month will be increased or decreased at the rate of 1/12 of .05% per percentage point, depending on the extent, if any, by which the investment performance of the Fund exceeds by more than two percentage points, or is exceeded by more than two percentage points by, the percentage change in the investment record of the S&P 600 for the performance period. The maximum increase or decrease in the Basic Fee for any month is 1/12 of 0.5%. Accordingly, for each month the maximum monthly fee rate as adjusted for performance will be 1/12 of 1.5% and will be payable if the investment performance of the Fund exceeds the percentage change in the investment record of the S&P 600 by 12 or more percentage points for the performance period, and the minimum monthly fee rate as adjusted for performance will be 1/12 of 0.5% and will be payable if the percentage change in the investment record of the S&P 600 exceeds the investment performance of the Fund by 12 or more percentage points for the performance period. As a result, the actual investment advisory fee rate may at times be greater than the fee rate paid by many other funds.

Because the Basic Fee is a function of the Fund's net assets and not of its total assets, Royce will not receive any fee in respect of those assets of the Fund equal to the aggregate unpaid principal amount of any indebtedness of the Fund. Royce will receive a fee in respect of any assets of the Fund equal to the liquidation preference of the outstanding Cumulative Preferred Stock and for any other Preferred Stock that may be issued and sold by the Fund.

The following table illustrates, on an annualized basis, the full range of permitted increases or decreases to the Basic Fee.

DIFFERENCE BETWEEN PERFORMANCE OF FUND AND % CHANGE IN S&P 600 RECORD	ADJUSTMENT TO 1% BASIC FEE
+12 or more	+0.50%
+11	+0.45%
+10	+0.40%
+9	+0.35%
+8	+0.30%
+7	+0.25%
+6	+0.20%
+5	+0.15%
+4	+0.10%
+3	+0.05%
+/-2	0.00%
-3	-0.05%
-4	-0.10%
-5	-0.15%
-6	-0.20%
-7	-0.25%
-8	-0.30%
-9	-0.35%
-10	-0.40%
-11	-0.45%
-12 or less	-0.50%

In calculating the investment performance of the Fund and the percentage change in the investment record of the S&P 600, all dividends and other distributions during the performance period are treated as having been reinvested at net asset value on the record date, and no effect is given to gain or loss resulting from capital share transactions of the Fund. Fractions of a percentage point are rounded to the nearest whole point (to the higher whole point if exactly one-half).

Notwithstanding the foregoing, Royce will not be entitled to receive any fee for any month when the investment performance of the Fund for the rolling 36-month period ending with such month is negative on an absolute basis. In the event that the Fund's investment performance for such a performance period is less than zero, Royce will not be required to refund to the Fund any fee earned in respect of any prior performance period.

Royce has volunteered to waive the portion of its investment advisory fee attributable to the liquidation preference of the 7.80% Preferred, the 7.30% Preferred and the Cumulative Preferred Stock (net of the liquidation preference of the 7.80% Preferred and the 7.30% Preferred) for any month when the Fund's net asset value average annual total return since the initial issuance of the 7.80% Preferred, the 7.30% Preferred or the Cumulative Preferred Stock fails to exceed the blended dividend rate on those assets.

Because Royce's fee is partially based on the average net assets of the Fund (including assets obtained from the sale of the Cumulative Preferred Stock and other Preferred Stock), Royce has generally benefited from the Fund's issuance of Preferred Stock.

CODE OF ETHICS

The Fund's Board of Directors approved a Code of Ethics under Rule 17j-1 of the 1940 Act that covers the Fund and Royce. The Code of Ethics establishes procedures for personal investing and restricts certain transactions. Employees subject to the Code of Ethics may invest in securities for their personal investment accounts, including, in certain cases, securities that may be purchased or held by the Fund. See "Code of Ethics and Related Matters" in the Statement of Additional Information.

DESCRIPTION OF CUMULATIVE PREFERRED STOCK

The following is a brief description of the terms of the Cumulative Preferred Stock. This description does not purport to be complete and is qualified by reference to the Charter, including the Articles Supplementary, the form of which is filed as an exhibit to the Fund's Registration Statement, and the Bylaws. Certain of the capitalized terms used herein are defined in the Glossary that appears at the end of this Prospectus.

GENERAL

The Cumulative Preferred Stock offered hereby is a senior security, as defined by the 1940 Act, of the Fund, which means, among other things, it is senior in priority to the Fund's Common Stock; however, it will rank junior to any future indebtedness of the Fund. Under the terms of the Cumulative Preferred Stock, the Fund is initially authorized to issue up to 8,800,000 shares of Cumulative Preferred Stock. No fractional shares of Cumulative Preferred Stock will be issued. The Board of Directors reserves the right to issue additional shares of Cumulative

Preferred Stock or other Preferred Stock from time to time, subject to the restrictions in the Charter and the 1940 Act. The shares of Cumulative Preferred Stock will, upon issuance, be fully paid and nonassessable and will have no appraisal, preemptive, exchange or conversion rights. Any shares of Cumulative Preferred Stock repurchased or redeemed by the Fund will be returned to the status of authorized but unissued shares of Preferred Stock, without designation as to series. The Board of Directors may by resolution classify or reclassify any authorized but unissued Preferred Stock from time to time by setting or changing the preferences, rights, voting powers, restrictions, limitations as to dividends or other distributions, qualifications or terms or conditions of redemption. The Fund will not issue any class of stock senior to the shares of Cumulative Preferred Stock.

DIVIDENDS

Holders of shares of Cumulative Preferred Stock will be entitled to receive, when, as and if authorized by the Board of Directors and declared by the Fund out of funds legally available therefor, cumulative cash dividends at the annual rate of 5.90% per share (computed on the basis of a 360-day year consisting of twelve 30-day months) of the initial liquidation preference of $25.00 per share, payable quarterly on March 23, June 23, September 23 and December 23 (each, a "Dividend Payment Date"), commencing on December 23, 2003 (or, if any such day is not a Business Day, then on the next succeeding Business Day), to the persons in whose names the shares of Cumulative Preferred Stock are registered at the close of business on the preceding March 6, June 6, September 6 and December 6 (or, if any such day is not a Business Day, then on the next succeeding Business Day), respectively.

Dividends on the shares of Cumulative Preferred Stock will accumulate from the date on which such shares are originally issued (the "Date of Original Issue").

No dividends will be declared or paid or set apart for payment on shares of Cumulative Preferred Stock for any dividend period or part thereof unless full cumulative dividends have been or contemporaneously are declared and paid on all outstanding shares of Cumulative Preferred Stock through the most recent Dividend Payment Date thereof. If full cumulative dividends are not paid on the Cumulative Preferred Stock, all dividends on the shares of Cumulative Preferred Stock will be paid pro rata to the holders of the shares of Cumulative Preferred Stock. Holders of Cumulative Preferred Stock will not be entitled to any dividends, whether payable in cash, property or stock, in excess of full cumulative dividends. No interest, or sum of money in lieu of interest, will be payable in respect of any dividend payment that may be in arrears.

For so long as any shares of Cumulative Preferred Stock are outstanding, the Fund will not declare, pay or set apart for payment any dividend or other distribution (other than a dividend or distribution paid in shares of, or options, warrants or rights to subscribe for or purchase shares of, Common Stock or other stock, if any, ranking junior to the Cumulative Preferred Stock as to dividends or payment upon liquidation) in respect of the Common Stock or any other stock of the Fund ranking junior to or on a parity with the Cumulative Preferred Stock as to dividends or payment upon liquidation, or call for redemption, redeem, purchase or otherwise acquire for consideration any shares of its Common Stock or any other junior stock (except by conversion into or exchange for stock of the Fund ranking junior to or on a parity with the Cumulative Preferred Stock as to dividends or payment upon liquidation), unless, in each case, (i) immediately after such transaction, the Fund will have a Portfolio Calculation for Moody's at

least equal to the Basic Maintenance Amount and the Fund will maintain the Asset Coverage (see "-- Asset Maintenance" and "-- Redemption" below), (ii) full cumulative dividends on shares of Cumulative Preferred Stock due on or prior to the date of the transaction have been declared and paid (or sufficient Deposit Securities to cover such payment have been deposited with the Paying Agent) and (iii) the Fund has redeemed the full number of shares of Cumulative Preferred Stock required to be redeemed by any provision for mandatory redemption contained in the Charter.

If the Fund fails to pay dividends for two years or more, holders of the Cumulative Preferred Stock will acquire certain additional voting rights. See "-- Voting Rights" below. Such rights will be their exclusive remedy for any such failure.

ASSET MAINTENANCE

The Fund will be required to satisfy two separate asset maintenance requirements under the terms of the Cumulative Preferred Stock. These requirements are summarized below.

Asset Coverage. For so long as any shares of Cumulative Preferred Stock are outstanding, the Fund will be required to maintain as of the last Business Day of each March, June, September and December of each year, an "asset coverage" (as defined by the 1940 Act) of at least 200% (or such higher percentage as may be required under the 1940 Act) with respect to all outstanding senior securities of the Fund which are stock, including the Cumulative Preferred Stock (the "Asset Coverage"). If the Fund fails to maintain the Asset Coverage on such dates and such failure is not cured in 60 days, the Fund will be required under certain circumstances to redeem certain of the shares of Cumulative Preferred Stock. See "-- Redemption -- Mandatory Redemption" below.

Assuming the Fund had issued and sold the Cumulative Preferred Stock and redeemed the 7.80% Preferred and the 7.30% Preferred as of June 30, 2003, the Asset Coverage immediately following such issuance and sale of the Cumulative Preferred Stock and such redemption of the 7.80% Preferred and the 7.30% Preferred (after giving effect to the deduction of the underwriting discounts and estimated offering expenses for such shares) would have been computed as follows:

Value of Fund assets less liabilities not constituting senior securities	=	$912,009,396	=	415%
Senior securities representing indebtedness plus aggregate liquidation preference of the Cumulative Preferred Stock		$220,000,000		

Basic Maintenance Amount. For so long as any shares of Cumulative Preferred Stock are outstanding, the Fund will be required to maintain, as of each Valuation Date, portfolio holdings meeting specified guidelines of Moody's, as described under "Rating Agency Guidelines", having an aggregate discounted value (a "Portfolio Calculation") at least equal to the Basic Maintenance Amount, which is in general the sum of the aggregate liquidation preferences of the Cumulative Preferred Stock and any other Preferred Stock, any indebtedness for borrowed money and current liabilities and dividends. If the Fund fails to meet such requirement as to any Valuation Date and such failure is not cured within 14 days after such Valuation Date, the Fund will be required to redeem certain of the shares of Cumulative Preferred Stock. See "-- Redemption -- Mandatory Redemption" below.

Any security not in compliance with the Rating Agency Guidelines will be excluded from the Portfolio Calculation.

The Moody's Discount Factors and guidelines for determining the market value of the Fund's portfolio holdings have been based on criteria established in connection with the rating of the Cumulative Preferred Stock. These factors include, but are not limited to, the sensitivity of the market value of the relevant asset to changes in interest rates, the liquidity and depth of the market for the relevant asset, the credit quality of the relevant asset (for example, the lower the rating of a corporate debt obligation, the higher the related discount factor) and the frequency with which the relevant asset is marked to market. The Moody's Discount Factor relating to any asset of the Fund and the Basic Maintenance Amount, the assets eligible for inclusion in the calculation of the discounted value of the Fund's portfolio and certain definitions and methods of calculation relating thereto may be changed from time to time by the Board of Directors, provided that, among other things, such changes will not impair the rating then assigned to the Cumulative Preferred Stock by Moody's.

On or before the third Business Day after each Quarterly Valuation Date, the Fund is required to deliver to Moody's a Basic Maintenance Report ("Basic Maintenance Report"). Within ten Business Days after delivery of such report relating to the last Quarterly Valuation Date of the Fund's fiscal year, the Fund will deliver a letter prepared by the Fund's independent accountants regarding the accuracy of the calculations made by the Fund in such a Basic Maintenance Report. If any such letter prepared by the Fund's independent accountants shows that an error was made in the most recent Basic Maintenance Report, the calculation or determination made by the Fund's independent accountants will be conclusive and binding on the Fund.

REDEMPTION

Mandatory Redemption. The Fund will be required to redeem, at a redemption price equal to $25.00 per share plus accumulated and unpaid dividends through the date of redemption (whether or not earned or declared) (the "Redemption Price"), certain of the shares of Cumulative Preferred Stock (to the extent permitted under the 1940 Act, Maryland law and any agreement in respect of indebtedness of the Fund to which it may be a party or by which it may be bound) in the event that:

(i) the Fund fails to maintain the quarterly Asset Coverage and such failure is not cured on or before 60 days following such failure (a "Cure Date"); or

(ii) for so long as the Fund is complying with the Rating Agency Guidelines, the Fund fails to maintain a Portfolio Calculation at least equal to the Basic Maintenance Amount as of any Valuation Date, and such failure is not cured on or before the 14th day after such Valuation Date (also, a "Cure Date").

The amount of such mandatory redemption will equal the minimum number of outstanding shares of Cumulative Preferred Stock and/or any other Preferred Stock the redemption of which, if such redemption had occurred immediately prior to the opening of business on a Cure Date, would have resulted in the Asset Coverage having been satisfied or the Fund having a Portfolio Calculation for Moody's equal to or greater than the Basic Maintenance Amount on such Cure Date or, if the Asset Coverage or a Portfolio Calculation for Moody's

equal to or greater than the Basic Maintenance Amount, as the case may be, cannot be so restored, all of the shares of Cumulative Preferred Stock, at the Redemption Price. In the event that shares of Cumulative Preferred Stock are redeemed due to the occurrence of (i) above, the Fund may, but is not required to, redeem a sufficient number of shares of Cumulative Preferred Stock in order to increase the "asset coverage" (as defined in the 1940 Act) of the remaining outstanding shares of Cumulative Preferred Stock and any other Preferred Stock after redemption up to 275%. In the event that shares of Cumulative Preferred Stock and/or any other Preferred Stock are redeemed due to the occurrence of (ii) above, the Fund may, but is not required to, redeem a sufficient number of shares of Cumulative Preferred Stock so that the Portfolio Calculation exceeds the Basic Maintenance Amount of the remaining outstanding shares of Cumulative Preferred Stock and any other Preferred Stock remaining after redemption by up to 10%.

If the Fund does not have funds legally available for the redemption of, or is otherwise unable to redeem, all the shares of Cumulative Preferred Stock to be redeemed on any redemption date, the Fund is required to redeem on such redemption date that number of shares for which it has legally available funds and is otherwise able to redeem, pro rata from each holder whose shares are to be redeemed, and the remainder of the shares required to be redeemed will be redeemed on the earliest practicable date on which the Fund will have funds legally available for the redemption of, or is otherwise able to redeem, such shares upon written notice of redemption ("Notice of Redemption").

If fewer than all shares of Cumulative Preferred Stock are to be redeemed, such redemption will be made pro rata from each holder of shares in accordance with the respective number of shares held by each such holder on the record date for such redemption. If fewer than all shares of Cumulative Preferred Stock held by any holder are to be redeemed, the Notice of Redemption mailed to such holder will specify the number of shares to be redeemed from such holder. Unless all accumulated and unpaid dividends for all past dividend periods will have been or are contemporaneously paid or declared and Deposit Securities for the payment thereof deposited with the Paying Agent, no redemptions of Cumulative Preferred Stock or any other Preferred Stock may be made.

Optional Redemption. Prior to October 9, 2008, the shares of Cumulative Preferred Stock are not subject to any optional redemption by the Fund unless such redemption is necessary, in the judgment of the Board of Directors of the Fund, to maintain the Fund's status as a RIC under the Code. Commencing October 9, 2008 and thereafter, the Fund may at its option redeem shares of Cumulative Preferred Stock at any time in whole or in part at the Redemption Price. Such redemptions are subject to the limitations of the 1940 Act, Maryland law and any agreement in respect of indebtedness of the Fund to which it may be a party or by which it may be bound.

Redemption Procedures. A Notice of Redemption will be given to the holders of record of Cumulative Preferred Stock to be redeemed not less than 30 or more than 45 days prior to the date fixed for the redemption. Each Notice of Redemption will state: (i) the redemption date, (ii) the number of shares of Cumulative Preferred Stock to be redeemed, (iii) the CUSIP number(s) of such shares, (iv) the Redemption Price, (v) that dividends on the shares to be redeemed will cease to accumulate on such redemption date and (vi) the provision of the Charter under which the