Stone Harbor Emerging Markets Total Income Fund
Form N-CSR
August 08, 2014

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM N-CSR

CERTIFIED SHAREHOLDER REPORT OF REGISTERED

MANAGEMENT INVESTMENT COMPANIES

Investment Company Act file number: 811-22716

Stone Harbor Emerging Markets Total Income Fund

(Exact name of registrant as specified in charter)

1290 Broadway, Suite 1100

Denver, CO 80203

(Address of principal executive offices) (Zip code)

Adam J. Shapiro, Esq.

c/o Stone Harbor Investment Partners LP

31 West 52nd Street, 16th Floor

New York, NY 10019

(Name and address of agent for service)

With copies To:

Michael G. Doherty, Esq.

Ropes & Gray LLP

1211 Avenue of the Americas

New York, NY 10036

Registrant s telephone number, including area code: (303) 623-2577

Date of fiscal year end: May 31

Date of reporting period: June 1, 2013 May 31, 2014

Item 1. **Reports to Stockholders.**

Distribution Policy

May 31, 2014

Stone Harbor Emerging Markets Total Income Fund (the Fund), acting pursuant to a Securities and Exchange Commission exemptive order and with the approval of the Fund s Board of Trustees (the Board), has adopted a plan, consistent with its investment objectives and policies to support a level distribution of income, capital gains and/or return of capital (the Plan). In accordance with the Plan, the Fund began distributing $0.1511 per share on a monthly basis in December 2012.

The fixed amount distributed per share is subject to change at the discretion of the Fund s Board. Under the Plan, the Fund will typically distribute most or all of its available investment income to its shareholders, consistent with its primary investment objectives and as required by the Internal Revenue Code of 1986, as amended (the Code). The Fund may also distribute long term capital gains and short term capital gains and return capital to shareholders in order to maintain a level distribution. Please refer to Note 3 on page 25 for a description of this period s distribution. Each monthly distribution to shareholders is expected to be at the fixed amount established by the Board, except for extraordinary distributions and potential distribution rate increases or decreases to enable the Fund to comply with the distribution requirements imposed by the Code.

Shareholders should not draw any conclusions about the Fund s investment performance from the amount of these distributions or from the terms of the Plan. The Fund s total return performance on net asset value is presented in its financial highlights table. The Board may amend, suspend or terminate the Fund s Plan without prior notice if it deems such action to be in the best interest of the Fund or its shareholders. The suspension or termination of the Plan could have the effect of creating a trading discount (if the Fund s stock is trading at or above net asset value) or widening an existing trading discount. The Fund is subject to risks that could have an adverse impact on its ability to maintain level distributions. Examples of potential risks include, but are not limited to, economic downturns impacting the markets, investments in foreign securities, foreign currency fluctuations and changes in the Code. Please refer to the Fund s prospectus for a more complete description of its risks.

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May 31, 2014
(Unaudited)

Dear Investor,

The Stone Harbor Emerging Markets Total Income Fund (EDI or Fund) seeks to maximize total return, which consists of income on its investments and capital appreciation. The Fund invests in fixed income securities and related instruments that are economically tied to emerging markets (EM) countries, including sovereign external debt, local currency debt (non-U.S. dollar), and corporate debt from EM issuers. Additionally, the Fund may invest up to 20% of its assets in emerging equity markets.

Our investment thesis is straightforward despite significant recent market volatility, we believe EM debt markets continue to offer attractive investment opportunities for total return investors. EM countries generate the majority of global growth today and their share of global economic output has nearly doubled in the past decade. Furthermore, inflation in EM countries has fallen substantially and remains subdued, particularly in comparison to the hyperinflationary periods of the 1990s. And unlike many advanced economies, most EM countries maintain prudent debt levels and substantially lower fiscal deficits, in our opinion. In addition, EM debt still offers higher yields than advanced economy debt, even though EMs have better relative fundamentals in most cases, based on our analysis.

Macroeconomic developments in advanced economies are important inputs into our assessment of the outlook for EM debt returns. The impact of developments outside the emerging markets on emerging market valuations has been a critical variable in the performance of emerging market assets since the end of the 2008 financial crisis. These factors, including weaker than expected economic growth and uncertainty about the future direction of developed market central bank policies weighed heavily on the Fund s performance during the first eight months of this fiscal year, in our view. During the next four months of the fiscal year (February-May 2014) these same factors drove strong performance as investor confidence in continued economic expansion has combined with greater clarity on future central bank steps, particularly at the US Federal Reserve.

We believe that a key advantage we have in managing EDI is the latitude to seek to adjust the risk in the portfolio based on fundamental economic and credit views, as well as our assessment of the macroeconomic environment. We can seek to adjust risk and potential return opportunities by allocating to three distinct sectors of EM debt as well as the EM equity markets, each of which tend to behave differently in various macroeconomic environments.

In addition, we can vary the amount of leverage used by the Fund depending on our confidence in our return expectations. In general, we employ leverage to seek higher returns. However, when uncertainty rises, and with it greater perceived risks, we can also reduce leverage so that the Fund has less exposure to EM debt.

Performance Review

The total return on net asset value (NAV) of EDI for the 12 months ending May 31, 2014 was 0.28%, (net of expenses). For the same period, the Fund maintained an average discount to its NAV of 4.51%[1]. Market tracking indices for the three sectors of EM debt[2] external sovereign debt, local currency debt and corporate debt delivered total returns of 5.77%, -1.37% and 4.78%, respectively, during the reporting period. The relatively poor performance of local currency debt was driven by negative returns from foreign exchange. As we discussed, asset allocation is an important factor in our management of the Fund. Our allocation to local currency sovereign debt ranged from approximately 20% to 38% of the total portfolio during the fiscal year. Given the disparity in returns between local currency sovereigns and other segments of EM, our local currency allocation detracted from our overall fund returns.

In the Fund s exposure to sovereign debt, our holdings in U.S. dollar-denominated debt of Venezuela had a large impact on returns, negatively for the first eight months of the fiscal year, then positively for the last four months. The positive performance outweighed the earlier sell-off. We invested in Venezuela based on our assessment of the country s ability and willingness to repay debt from U.S. dollar cash flows generated from oil exports. We also believed that Venezuela s government had strong incentives to prioritize oil export cash flows for servicing external debt in order to maintain relationships with integrated global oil companies that invest in Venezuela s Orinoco oil belt, which contains some of the world s largest proven oil reserves. Venezuela s political situation has been quite chaotic in the aftermath of President Chavez s death. In addition, economic growth has slowed and inflation is rising. This political volatility overwhelmed the country s solid debt fundamentals as the market sold off during the second half of 2013. As political volatility faded in early 2014, investors reassessed Venezuela s prospects and valuation. As of the date of this report, Venezuela offered the highest yields in the sovereign hard currency universe. This attractive valuation combined with its structural incentives to continue servicing its debt helped Venezuela generate the best returns for the Fund during the February to May period.

Throughout the reporting period, leverage consisted primarily of short-term reverse repurchase agreements through which the Fund borrowed funds by selling securities under the obligation to repurchase them at a later date at a fixed price. The implied borrowing costs of the repurchase agreements averaged approximately 0.55% per annum. The level of gross leverage reached a maximum of approximately 33.3% of total assets on January 31, 2014 and a minimum of approximately 23.8% on June 6, 2013. By the end of the reporting period, leverage was approximately 28.7%. Net leverage (gross leverage less cash held) remained lower than gross leverage throughout the period. The Fund s management team varied borrowing levels to reflect the team s outlook on EM debt, increasing borrowings when it felt opportunities had improved and reducing borrowings when, in the team s judgment, macroeconomic risks had risen.

May 31, 2014

Market Review and Outlook

In our view, the total returns for EM indices[2] for the reporting period reflected a combination of events in developed markets and emerging markets overlayed by valuations in emerging markets. Market tracking indices for the three sectors of EM debt[2] external sovereign debt, local currency debt and corporate debt delivered total returns of 5.77%, -1.37% and 4.78%, respectively, during the reporting period. As mentioned previously, the pattern of returns during the Fund s fiscal year changed in February 2014. During the eight month period ending in January each emerging markets debt sector generated negative returns. Beginning in February 2014, volatility decreased and valuations attracted significant investor interest. Returns in the four month period of February through May 2014 turned strongly positive in each sector leading to the overall returns listed above. The factors that impacted returns during these two segments of the reporting period are discussed below.

Several factors, both fundamental and technical, contributed to the market volatility of EM assets in the second half of 2013. From a macroeconomic perspective, rising concerns over the timing of the U.S. Federal Reserve s reduction in the pace of its bond purchase program led to a rapid increase in U.S. Treasury yields and a broad-based sell off of fixed income assets. Fears of less accommodative monetary policy in the U.S. contributed to growing concerns about the attractiveness of EM assets that had benefited from large investor inflows since the end of the global financial crisis. Fundamental factors also played a role in the EM debt decline, in our opinion, as growth in many large emerging markets, including China, remained lower than expected and growth expectations fell. At the same time, popular uprisings in Argentina, Brazil, Thailand, Turkey and Ukraine produced headlines about political risks in EMs. These factors imposed a significant influence over investor sentiment across all EM sectors, in our view.

By the end of January 2014 investors developed greater clarity on the likely course of policy moves by the U.S. Fed. This increased clarity combined with evidence of continued economic recovery in the developed world and reduced political volatility in the emerging world created a better environment for risk-taking on the part of investors, in our opinion. The weak performance of EM during 2013 provided compelling valuations and started the rally that continued throughout the remainder of the review period.

Despite these influences from advanced economies, our fundamental views on emerging markets have not changed. We continue to forecast that China should maintain a growth rate above 7% over the next year and that many EM country growth rates should improve in the next 12-18 months. In our view, expectations for improved U.S. growth, together with recent depreciation of emerging market currencies and prior monetary easing by EM central banks, will support EM growth in the months ahead. But we believe this process will take time. Government deficits in most EM countries remain at healthy levels, particularly compared to the U.S., Japan and many developed European countries. We believe markets are again focusing on the relative strengths of EM fundamentals.

In the past, we have detailed some of the key risks to our constructive outlook for emerging markets debt. Today, those risks seem to emanate from both developed and emerging countries. The possibility of rising U.S. interest rates, the ongoing political and religious strife in the Middle East, weak growth in Europe and the potential for China s growth rate to fall short of expectations are all potential risks. However, our base case return scenarios for EM debt over the coming year remain positive. Our view derives from a disciplined investment process in which we review the ability and willingness of borrowers to repay their debts. We also assess whether current prices of bonds reflect adequate compensation for risk within the current macroeconomic environment. Based on this process, we continue to believe that EM debt will generate the highest returns in the fixed income markets.

Other general risks of the Fund relate to our use of leverage and also to the longer-term prospects for a rise in global interest rates. Stone Harbor attempts to mitigate the risk of loss of principal due to the possibility of a general rise in global interest rates through our investment processes that determine sector and country allocations, as well as security selection. We seek to reduce interest rate sensitivity during periods of rising interest rates. Notwithstanding these efforts, rising interest rates would increase the Fund s cost of leverage and could also decrease the value of its portfolio securities, adversely affecting Fund performance.

We continue to believe that investing in EDI may offer an attractive means of capitalizing on further improvements in credit quality in EM. We thank you for your confidence in our ability to invest in these challenging markets and look forward to reporting on EDI in six months.

Sincerely,

Thomas K. Flanagan

Chairman of the Board of Trustees

May 31, 2014
(Unaudited)

1 *Performance on a market value basis, or at market price, will differ from its results at NAV. Although market price returns typically reflect investment results overtime, during shorter periods, returns at market price can also be influenced by factors such as changing views about the Fund, market conditions, supply and demand for the Fund s shares, or changes in Fund dividends.*

2 *J.P. Morgan emerging markets debt benchmarks are used throughout as being representative of market returns. The J.P. Morgan EMBI Global Index (EMBIG) tracks total returns for U.S. dollar-denominated debt instruments issued by emerging markets sovereign and quasi-sovereign entities: Brady bonds, loans, and Eurobonds. The changes in the benchmark more accurately reflect the investment strategy. The J.P. Morgan EMBI Global Diversified (EMBI Global Diversified) limits the weights of those index countries with larger debt stocks by only including specified portions of these countries eligible current face amounts outstanding. The countries covered in the EMBI Global Diversified are identical to those covered by the EMBI Global. The J.P. Morgan GBI-EM Global Diversified consists of regularly traded, liquid fixed-rate, domestic currency government bonds to which international investors can gain exposure. The weightings among the countries are more evenly distributed within this index. Return from FX is the difference between the JP Morgan GBI EM Global Diversified index total return Bloomberg ticker JGENVUUG) and the GBI EM Global Diversified index in local currency terms (Bloomberg ticker JGENVLLG). Return from Rates equals the total return of the GBI EM Global Diversified index in local currency terms (Bloomberg ticker JGENVLLG). The J.P. Morgan CEMBI Broad Diversified tracks total returns of U.S. dollar-denominated debt instruments issued by corporate entities in emerging market countries and consists of an investable universe of corporate bonds. The minimum amount outstanding required is $350 mm for the CEMBI Broad Diversified. Broad-based securities indices are unmanaged and are not subject to fees and expenses typically associated with managed accounts or investment funds. Investments cannot be made directly in a broad-based securities index. The CEMBI Broad Diversified limits the weights of those index countries with larger corporate debt stocks by only including a specified portion of these countries eligible current face amounts of debt outstanding.*

Stone Harbor Emerging Markets Total Income Fund

Summary of Portfolio Holdings

May 31, 2014
(Unaudited)

Security Type Allocation[2]

Fund Details

Market Price	$19.95
Net Asset Value (NAV)	$21.18
Premium/(Discount)	(5.81)%
Current Distribution Rate[1]	9.09%
Net Assets ($ in millions)	$204

Country Allocation

(as a % of total net assets)

Country Breakdown	**% of TNA**
Venezuela	22.03%
Brazil (Includes 2.03% ETF)	18.87%
Argentina	11.38%
Mexico	10.06%
South Africa	8.96%
Turkey (Includes 1.38% ETF)	7.71%
Indonesia	6.66%
Iraq	5.80%
Colombia	5.38%
Dominican Republic	4.02%
Ivory Coast	3.50%
Russia	3.40%
Kazakhstan	3.19%
Nigeria	2.89%
Mozambique	2.63%
Ukraine	2.60%
Peru	2.53%
China	1.48%
Croatia	1.41%
India	1.20%
Chile	1.10%
El Salvador	0.98%
United Arab Emirates	0.87%
Luxembourg	0.82%
Trinidad	0.63%
Guatemala	0.52%

Panama	0.45%
Ghana	0.44%
Israel	0.41%
Honduras	0.21%
Hungary	0.21%
Costa Rica	0.14%
Vanguard® FTSE Emerging Markets ETF	2.07%
Total	**134.55%**
Short Term Security	**1.92%**
Other Liabilities in Excess	**-36.47%**
Total Net Assets	**100.00%**

Sector Allocation(2)

Sovereign Local	37.2%
Sovereign External	42.5%
Corporate	14.0%
Equity	3.9%
Cash & Equivalents/ U.S. Treasuries	2.4%

Regional Breakdowns(2)

Latin America	56.8%
Africa	14.1%
Europe	13.4%
Asia	6.7%
Middle East	5.1%
Multi	1.5%
Cash & Equivalents/ U.S. Treasuries	2.4%

Sovereign Local

Currency Breakdown(2)

Brazilian Real	11.5%
Colombian Peso	3.7%
Indonesian Rupiah	3.4%
Mexican Peso	6.5%
Nigerian Naira	0.9%
Turkish New Lira	4.6%
South African Rand	6.6%
Total	**37.2%**

(1) *Current Distribution Rate is based on the Fund s current annualized monthly distribution divided by the Fund s current market price. The Fund s monthly distributions to its shareholders may be comprised of ordinary income,*

net realized capital gains and return of capital in order to maintain a level distribution.

(2) *Based on managed assets and investment manager s sector classifications including derivative exposure. For purposes of this example, managed assets include total net assets plus any borrowings attributed to the use of reverse repurchase agreements as described on page 13.*

Stone Harbor Emerging Markets Total Income Fund

Growth of
$10,000 Investment

May 31, 2014 (Unaudited)

Comparison of Change in Value of $10,000 Investment in Stone Harbor Emerging Markets Total Income Fund and the J.P. Morgan Emerging Markets Bond Indices: EMBI Global Diversified, CEMBI Broad Diversified, and GBI-EM Global Diversified (please refer to page 36 for detailed benchmark descriptions).

Total Returns as of May 31, 2014 (Inception, October 25, 2012)

	3 Months	**6 Months**	**1 Year**	**Since Inception (Annualized)**
Stone Harbor Emerging Markets Total Income Fund NAV	12.24%	10.86%	0.28%	0.88%
Stone Harbor Emerging Markets Total Income Fund Market Price	12.29%	12.86%	-8.58%	-5.58%
J.P. Morgan CEMBI Broad Diversified	3.49%	5.84%	4.78%	4.11%
J.P. Morgan EMBI Global Diversified	5.81%	8.83%	5.77%	2.53%
J.P. Morgan GBI-EM Global Diversified	5.88%	4.37%	-1.37%	-0.70%

Past performance is no guarantee of future results. Current performance may be lower or higher than the performance shown. Total return is calculated by determining the percentage change in NAV or market price (as applicable) in the specified period. The calculation assumes that all income dividends, capital gain and return of capital distributions, if any, have been reinvested and includes all fee waivers and expense reimbursements. Total return does not reflect the deduction of taxes that a shareholder would pay on Fund distributions or broker commissions or sales charges in connection with the purchase or sale of Fund shares. Investment return and principal value will vary, and shares, when sold, may be worth more or less than their original cost. Total returns for a period of less than one year are not annualized. Index returns do not include the effects of sales charges or management fees. It is not possible to invest directly in an index.

Performance at market price will differ from its results at NAV. Although market price returns typically reflect investment results over time, during shorter periods returns at market price can also be influenced by factors such as changing views about the Fund, market conditions, supply and demand for the Fund s shares, or changes in Fund dividends.

An investment in the Fund involves risk, including the loss of principal. Total return, market price, market price yield and NAV will fluctuate with changes in market conditions. This data is provided for information purposes only and is not intended for trading purposes. Closed-end funds, unlike open-end funds, are not continuously offered. There is a onetime public offering and once issued, shares of closed-end funds are traded in the open market through a stock exchange. NAV is equal to total assets attributable to common shareholders less total liabilities divided by the number of common shares outstanding. Holdings are subject to change daily.

Stone Harbor Emerging Markets Total Income Fund

Report of Independent Registered Public Accounting Firm

To the Shareholders and Board of Trustees of Stone Harbor Emerging Markets Total Income Fund:

We have audited the accompanying statement of assets and liabilities of Stone Harbor Emerging Markets Total Income Fund (the Fund), including the statement of investments, as of May 31, 2014, and the related statements of operations and cash flows for the year then ended, and the statements of changes in net assets and the financial highlights for the year then ended and for the period from October 25, 2012 (commencement of operations) to May 31, 2013. These financial statements and financial highlights are the responsibility of the Fund s management. Our responsibility is to express an opinion on these financial statements and financial highlights based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements and financial highlights are free of material misstatement. The Fund is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Fund s internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. Our procedures included confirmation of securities owned as of May 31, 2014, by correspondence with the custodian and brokers; where replies were not received from brokers, we performed other auditing procedures. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements and financial highlights referred to above present fairly, in all material respects, the financial position of Stone Harbor Emerging Markets Total Income Fund as of May 31, 2014, the results of its operations and its cash flows for the year then ended, and the changes in its net assets and the financial highlights for the year then ended and for the period from October 25, 2012 (commencement of operations) to May 31, 2013, in conformity with accounting principles generally accepted in the United States of America.

DELOITTE & TOUCHE LLP

Denver, Colorado

July 28, 2014

May 31, 2014

	Currency	Rate	Maturity Date	Principal Amount*	Market Value (Expressed in U.S. $)
SOVEREIGN DEBT OBLIGATIONS - 84.85%					
Argentina - 10.87%					
Republic of Argentina:					
	USD	7.000%	10/03/2015	10,900,000	$ 10,443,714(1)
	USD	7.000%	04/17/2017	11,157,323	10,201,822(1)
	USD	8.750%	06/02/2017	1,600,000	1,482,440
					22,127,976
Brazil - 15.42%					
Nota Do Tesouro Nacional:					
	BRL	10.000%	01/01/2017	20,260,000	8,722,557
	BRL	10.000%	01/01/2021	30,000,000	12,292,825
	BRL	10.000%	01/01/2023	25,830,000	10,381,103
					31,396,485
Colombia - 0.37%					
Bogota Distrio Capital	COP	9.750%	07/26/2028	1,130,000,000	761,646(2)
Costa Rica - 0.14%					
Republic of Costa Rica	USD	7.000%	04/04/2044		