

Salient Midstream & MLP Fund
Form N-CSR
February 08, 2013

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

FORM N-CSR

CERTIFIED SHAREHOLDER REPORT OF REGISTERED
MANAGEMENT INVESTMENT COMPANY

Investment Company Act file number 811-22626

Salient Midstream & MLP Fund

(Exact name of registrant as specified in charter)

4265 SAN FELIPE, SUITE 800, HOUSTON, TX 77027

(Address of principal executive offices) (Zip code)

Gregory A. Reid

With a copy to:
George J. Zornada

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Salient Midstream & MLP Fund
4265 San Felipe, Suite 800
Houston, TX 77027
(Name and address of agent for service)

K & L Gates LLP
State Street Financial Center
One Lincoln St.
Boston, MA 02111-2950
(617) 261-3231

Registrant's telephone number, including area code: 713-993-4675

Date of fiscal year end: 11/30/12

Date of reporting period: 11/30/12

Item 1. Reports to Stockholders.

Salient Midstream & MLP Fund

Annual Report to Shareholders

For the Period May 24, 2012 (commencement of operations) through November 30, 2012

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Management Discussion of Fund Performance (Unaudited)

Letter to Shareholders

January 17, 2013

Dear Fellow Shareholders:¹

It has been an exciting six months since our initial public offering (IPO) on May 24, 2012 and we are pleased to provide you with our annual investor letter to update you on the Fund's investments and performance since inception. As a reminder, the Salient Midstream & MLP Fund priced its IPO on May 24, 2012 at \$20.00 per share and received net proceeds of \$171.5 million from the IPO, which includes the net proceeds from the sale of nine million shares, and an additional 459,100 shares for net proceeds of \$8.8 million that were exercised as part of the over allotment option.

As of November 30, 2012, the Fund had total investments of approximately \$262.3 million, which includes the \$171.5 million net proceeds from the IPO as well as \$75.2 million that was funded with borrowings under our revolving credit facility. Immediately following the IPO, the Fund's net asset value (NAV) totaled \$19.06 per share, which represents the offering price less underwriting discounts and other offering expenses. As of November 30, 2012, the Fund's net assets were \$183.7 million and the NAV per share was \$19.40. The Fund's investments are shown in the pie chart below:

¹ **Certain statements in this letter are forward-looking statements.** The forward-looking statements and other views expressed herein are those of the portfolio managers and the Fund as of the date of this letter. Actual future results or occurrences may differ significantly from those anticipated in any forward-looking statements, and there is no guarantee that any predictions will come to pass. The views expressed herein are subject to change at any time, due to numerous market and other factors. The Fund disclaims any obligation to update publicly or revise any forward-looking statements or views expressed herein. There can be no assurance that the Fund will achieve its investment objectives. The value of the Fund will fluctuate with the value of the underlying securities. Historically, closed-end funds often trade at a discount to their net asset value.

² Past performance is not predictive of future results. Current performance may be higher or lower than the data shown. The data shown are unaudited. Returns do not reflect the deduction of taxes that shareholders may have to pay on Fund distributions or upon the sale of Fund shares.

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The Fund's Top 10 holdings are shown below, as of November 30, 2012:

Company Name	Sector	% of Gross Assets
Kinder Morgan Management, LLC	MLP Affiliate	8.7%
Enterprise Products Partners, L.P. **	MLP	8.5%
Plains All American Pipeline, L.P. *	MLP	6.5%
El Paso Pipeline Partners, L.P. *	MLP	5.3%
Kinder Morgan, Inc.	Midstream Company	5.0%
Linn Co., LLC	MLP Affiliate	4.7%
Teekay Offshore Partners, L.P.	Marine Midstream	4.6%
Williams Companies, Inc.	Midstream Company	4.5%
Enbridge Energy Management, LLC	MLP Affiliate	4.3%
Energy Transfer Equity, L.P. *	MLP	4.2%
Total		56.2%

* Held indirectly through the wholly owned C-Corporation, Salient Midstream & MLP Fund, Inc.

** A portion of the shares are held indirectly through the C-Corporationx

Note: These holdings include restricted and unrestricted shares

Source: Salient Capital Advisors, LLC, November 2012

Since the IPO, the top five contributors to the Fund's performance include Plains All American Pipeline (PAA), Energy Transfer Equity (ETE), Rose Rock Midstream (RRMS), Kinder Morgan Management (KMR), and Magellan Midstream Partners (MMP). The five largest detractors to the Fund's performance include Crosstex Energy, Inc. (XTXI), Crosstex Energy L.P. (XTEX), Golar LNG Partners (GMLP), Whiting USA Trust II (WHZ), and Centerpoint Energy (CNP). For the period ended November 30, 2012, the Fund's derivative transactions detracted approximately \$5.8 million from the Fund's performance.

The Fund paid its first distribution of \$0.325 per share in late August and its second distribution of \$0.33 per share in early December, all of which is return of capital for tax purposes, which represents a 6.6% yield on the Fund's \$20.00 initial public offering price.

2012 Review

In 2012, the Alerian MLP Index lagged the S&P 500 for the first time in 12 years. The AMZ generated a total return of 4.8% which was more than 11% behind the SPX total return of 16.0%. Distribution growth in 2012 came in above our expectations (7.7% actual vs. 6.5% expected) but MLP prices fell, driving the yield on the index from 6.1% at the end of 2011 to 6.6% at the end of 2012.

MLPs lagged the S&P 500 all year long, but almost half of the relative underperformance for 2012 occurred over the last two months. In fact, the AMZ was down 3.9% while the S&P 500 was up 1.5% during the November-December time frame. We believe a major culprit of the recent weakness was the expected change in long-term capital gains tax rates, which moved from 15% in 2012 to 20% plus the 3.8% Medicare surcharge on January 1 (for a total tax rate of 23.8%) for those with income above a certain threshold. Since MLPs have been up cumulatively over 100% on a price basis since the end of 2008, we believe that some investors may have locked in the 15% tax rate before year-end. Not surprisingly, MLPs have had a significant bounce thus far in January as the tax selling abated.

2013 Outlook

Due to the relative weakness in 2012, we believe that total returns in 2013 could potentially be strong. The yield of the AMZ was ~6.6% on December 31 and many analysts currently anticipate 6.5% to 7.0% distribution growth in 2013.

Below is a table showing the range of potential returns in 2013 for MLPs based on different yield and distribution growth assumptions.

The risk factors that may impact MLP and midstream company volumes, cash flow, and valuations this year include (but are not limited to) potential economic weakness, questions regarding the tax status of MLPs, a decline in crude oil, natural gas, and natural gas liquids (NGL) prices, and widening credit spreads.

Summary

We believe the Fund's first six months of operations have gone well, and we remain optimistic about the outlook in 2013. We believe valuations for MLPs and Midstream Companies remain attractive and we look forward to providing regular updates in the future on our progress in executing the Fund's business plan. Please visit our website at www.salientfunds.com for the latest updates and sign up to receive email alerts on future press releases by the Fund.

Please note that this letter, including the financial information herein, is made available to shareholders of the Fund for their information. It is not a prospectus, circular or representation intended for use in the purchase or sale of shares of the Fund or of any securities mentioned in this letter.

Sincerely,

Gregory A. Reid

President and Chief Executive Officer

MLP Business, Salient Capital Advisors, LLC

SALIENT MIDSTREAM & MLP FUND

Report of Independent Registered Public Accounting Firm

The Shareholders and Board of Trustees of

Salient Midstream & MLP Fund:

We have audited the accompanying consolidated statement of assets, liabilities and shareholders' equity of Salient Midstream & MLP Fund and Subsidiary (the Fund), including the consolidated schedule of investments, as of November 30, 2012, and the related consolidated statements of operations, changes in net assets and cash flows, and the consolidated financial highlights for the period May 24, 2012 (commencement of operations) through November 30, 2012. These consolidated financial statements and consolidated financial highlights are the responsibility of the Fund's management. Our responsibility is to express an opinion on these consolidated financial statements and consolidated financial highlights based on our audit.

We conducted our audit 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 consolidated financial statements and consolidated financial highlights are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. Our procedures included confirmation of securities owned as of November 30, 2012, by correspondence with the custodian and brokers or by other appropriate auditing procedures where replies from brokers were not received. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the consolidated financial statements and consolidated financial highlights referred to above present fairly, in all material respects, the financial position of Salient Midstream & MLP Fund and Subsidiary as of November 30, 2012, the results of their operations, changes in their net assets, their cash flows and the financial highlights for the period May 24, 2012 through November 30, 2012 in conformity with U.S. generally accepted accounting principles.

KPMG LLP

Columbus, Ohio

January 29, 2013

SALIENT MIDSTREAM & MLP FUND

Consolidated Schedule of Investments

November 30, 2012

	Shares/Units	Fair Value
Master Limited Partnerships and Related Companies 141.1%		
Coal 3.0%		
United States 3.0%		
Alliance Holdings GP, L.P. ⁽¹⁾⁽²⁾⁽⁴⁾	118,771	\$ 5,450,401
		5,450,401
Crude/Refined Products Pipelines 43.7%		
United States 43.7%		
Enbridge Energy Management, LLC ⁽²⁾⁽³⁾⁽⁴⁾	387,399	11,428,284
Kinder Morgan Management, LLC ⁽²⁾⁽³⁾⁽⁴⁾	306,829	23,288,346
Kinder Morgan, Inc. ⁽²⁾	392,078	13,256,157
Magellan Midstream Partners, L.P. ⁽¹⁾⁽²⁾⁽⁴⁾	114,000	5,070,720
MPLX, L.P. ⁽⁴⁾	51,100	1,474,746
Plains All American Pipeline, L.P. ⁽¹⁾⁽²⁾⁽⁴⁾	370,000	17,234,601
Rose Rock Midstream, L.P. ⁽²⁾	183,123	5,982,628
Summit Midstream Partners, L.P. ⁽²⁾⁽⁴⁾	128,566	2,540,464
		80,275,946
Diversified Pipelines 3.2%		
Canada 3.2%		
TransCanada Corp. ⁽²⁾	127,000	5,840,730
		5,840,730
Natural Gas Gathering/Processing 38.7%		
United States 38.7%		
Crosstex Energy, Inc. ⁽²⁾	733,805	9,429,394
Crosstex Energy, L.P. ⁽²⁾⁽⁴⁾	416,451	6,280,081
DCP Midstream Partners, L.P.	154,712	6,479,339
Linn Co., LLC ⁽²⁾	328,000	12,670,639
MarkWest Energy Partners, L.P. ⁽²⁾⁽⁴⁾	157,500	8,139,600
Off-Gas Partners QP, L.P. ⁽¹⁾⁽⁵⁾⁽⁶⁾⁽⁴⁾		700,000
PVR Partners, L.P. ⁽²⁾⁽⁴⁾	212,074	5,108,863
Targa Resources Corp.	68,633	3,437,827
Targa Resources Partners, L.P. ⁽²⁾⁽⁴⁾	155,979	5,875,729
Whiting USA Trust II	62,500	1,017,500
Williams Companies, Inc. ⁽²⁾	362,000	11,888,080
		71,027,052
Natural Gas/Natural Gas Liquids Pipelines 34.6%		
United States 34.6%		
El Paso Pipeline Partners, L.P. ⁽¹⁾⁽⁴⁾	375,767	14,027,382
Energy Transfer Equity, L.P. ⁽¹⁾⁽²⁾⁽⁴⁾	247,000	11,231,090
Enterprise Products Partners, L.P. ⁽¹⁾⁽²⁾⁽⁴⁾	436,882	22,643,595
EQT Midstream Partners, L.P. ⁽²⁾	82,734	2,541,588
Regency Energy Partners, L.P. ⁽⁴⁾	127,200	2,845,464

See accompanying Notes to Consolidated Financial Statements.

SALIENT MIDSTREAM & MLP FUND

Consolidated Schedule of Investments, continued

November 30, 2012

	Shares/Units	Fair Value
Spectra Energy Corp. ⁽¹⁾	180,877	\$ 5,055,512
Spectra Energy Partners, L.P. ⁽⁴⁾	172,796	5,147,593
		63,492,224
Power/Utility 2.8%		
United States 2.8%		
CenterPoint Energy, Inc. ⁽²⁾	264,000	5,208,720
		5,208,720
Shipping 14.7%		
Bermuda 2.7%		
Golar LNG Partners, L.P. ⁽²⁾	167,500	5,008,250
Republic of the Marshall Islands 9.0%		
Navios Maritime Partners, L.P.	322,062	4,312,410
Teekay Offshore Partners, L.P. ⁽²⁾	458,252	12,203,251
United States 3.0%		
Capital Product Partners, L.P. ⁽⁵⁾⁽⁶⁾⁽⁴⁾	622,222	5,423,038
		26,946,949
Specialty 0.4%		
United States 0.4%		
Hi-Crush Partners, L.P. ⁽²⁾	53,000	819,380
		819,380
Total Master Limited Partnerships and Related Companies ⁽⁴⁾ (Cost \$242,101,131)		\$ 259,061,402
Money Market Fund 1.7%		
United States 1.7%		
JPMorgan U.S. Government Money Market Fund ⁽¹⁾	3,231,520	\$ 3,231,520
Total Money Market Fund ⁽⁴⁾ (Cost \$3,231,520)		\$ 3,231,520
Total Investments 142.8% (Cost \$245,332,651)		262,292,922
Credit Facility (40.9%)		(75,200,000)
Other Assets and Liabilities (1.9%)		(3,408,123)
Total Net Assets Applicable to Common Shareholders 100.0%		\$ 183,684,799

All percentages disclosed are calculated by dividing the indicated amounts by net assets applicable to common shareholders.

(1) All or a portion of these securities are held by Salient Midstream & MLP Fund, Inc. (the "Subsidiary").

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- (2) All or a portion of these securities are held as collateral for the line of credit agreement. As of November 30, 2012 the total fair value of securities held as collateral for the line of credit agreement is \$184,921,482.
- (3) Distributions are paid-in-kind.
- (4) Non-income producing security.

See accompanying Notes to Consolidated Financial Statements.

SALIENT MIDSTREAM & MLP FUND

Consolidated Schedule of Investments, continued

November 30, 2012

- (5) Security is exempt from registration under the Securities Act of 1933. The security may be resold in transactions exempt from registration, normally to qualified institutional buyers.
- (6) Restricted securities have been fair valued in good faith using fair value procedures approved by the Board of Trustees and represent 3.3% of net assets. See Notes to Consolidated Financial Statements for further information.

Futures Contracts Sold:

Description	Expiration Date	Number of Contracts	Notional Amount at Value	Unrealized Appreciation (Depreciation)
30-Year U.S. Treasury Bond	March 2013	46	\$ (6,902,875)	\$ (476)
E-Mini S&P 500	December 2012	276	(19,518,720)	187,309
WTI Crude ⁽¹⁾	January 2013	32	(2,845,120)	(94,465)
			\$ (29,266,715)	\$ 92,368

Credit Default Swap Agreements Buy Protection⁽²⁾

Underlying Instrument	Fixed Deal Pay Rate	Maturity Date	Implied Credit Spread at November 30, 2012 ⁽³⁾	Notional Amount ⁽⁴⁾
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