

DELAWARE INVESTMENTS MINNESOTA MUNICIPAL INCOME FUND II, INC
Form N-CSR
June 03, 2011

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: 811-07420

Exact name of registrant as specified in charter:

Delaware Investments® Minnesota Municipal Income Fund II, Inc.

Address of principal executive offices:

2005 Market Street
Philadelphia, PA 19103

Name and address of agent for service:

David F. Connor, Esq.
2005 Market Street
Philadelphia, PA 19103

Registrant's telephone number, including area code: (800) 523-1918

Date of fiscal year end: March 31

Date of reporting period: March 31, 2011

Item 1. Reports to Stockholders

Annual Report

Delaware
Investments
Closed-End
Municipal Bond
Funds

March 31, 2011

The figures in the annual report for Delaware Investments Closed-End Municipal Bond Funds represent past results, which are not a guarantee of future results. A rise or fall in interest rates can have a significant impact on bond prices. Funds that invest in bonds can lose their value as interest rates rise.

Closed-end funds

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Portfolio management review

Delaware Investments Closed-End Municipal Bond Funds

April 12, 2011

Performance preview

The fiscal year ended March 31, 2011 was generally volatile for the Funds (and for investors in tax-exempt debt in general). Municipal bonds were under considerable selling pressure during the later parts of the fiscal year, driven primarily by fears about the credit worthiness of the municipal bond market, as well as technical developments that affected bond supply. Despite a fiscal year that ended in a flurry of headwinds, municipal bonds posted a cumulative gain of slightly more than 1.5% for the period (as measured by the Barclays Capital Municipal Bond Index).

National economic environment

During the fiscal year, the U.S. economy continued to emerge from its biggest downturn in seven decades, albeit relatively slowly. As the Funds' fiscal year got under way, U.S. economic growth softened, with gross domestic product (a measure of the economy's production of goods and services) slipping from an annualized rate of 3.7% in the first quarter of 2010 to just 1.7% in the second quarter. The grim economic situation was reflected in the national unemployment rate, which stood at 9.7% at the start of the fiscal year.

Several factors contributed to sluggish economic performance, among them:

- Many investors focused their attention on the high levels of sovereign debt across the developed world (and particularly in Greece), fearing that reductions in government spending could exacerbate declining economic growth.
- The U.S. housing market's glut of supply continued to weigh on home prices in many parts of the country.
- State and local governments, whose spending makes up a sizeable component of GDP, largely cut back expenditures to meet big budget shortfalls.

GDP data moderately improved as the fiscal year went on, with the economy growing at an annual rate of 2.6% in the third quarter of 2010 and 2.8% in the final three months of that year. The employment picture, while still generally challenging, began to improve as well, finishing the Funds' fiscal year at 8.9%.

Data: Bloomberg, Lipper, U.S. Department of Commerce

Municipal market trends

For the first two quarters of the Funds' fiscal year, the municipal bond market enjoyed relatively strong performance, echoing the positive trends of 2009. The municipal bond market benefited from several factors, including:

- Low inflation and declining interest rates provided a generally favorable climate for fixed-income securities.
- The popular Build America Bond (BAB) program continued to divert supply away from the traditional tax-exempt bond market and toward the taxable bond market.
- In this environment of reduced supply of tax-exempt securities, demand remained strong, especially for lower-rated, higher-yielding issues.

In November 2010, conditions in the tax-exempt bond market deteriorated suddenly, as many investors became increasingly concerned about the potential for inflation to put downward pressure on bond prices. Concerns were heightened by several developments, including the Federal Reserve's announcement that it would engage in another round of quantitative easing, in which it plans to purchase \$600 billion of Treasury securities, in order to further spur economic growth.

Meanwhile, several other events inhibited the municipal bond market:

- With the BAB program facing expiration at the end of 2010, many investors realized that supply of tax-exempt bonds could potentially increase markedly.
- Negative sentiment grew about the fiscal health of state and local governments.

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Portfolio management review

Delaware Investments Closed-End Municipal Bond Funds

- Significant gains in the number of Republican seats in Congress led many investors to envision a less friendly environment for federal aid to help states manage their budget challenges.
- An extension of Bush-era tax cuts led some investors to view the tax advantage of municipal bonds less favorably.

This confluence of factors precipitated dramatic investment outflows from municipal bond funds in the final months of 2010 and early 2011, reversing the tremendous inflows seen during the market's run-up in much of 2010. In turn, these outflows put downward pressure on municipal bond prices.

Fund positioning

When the Funds' fiscal year began, we maintained a modest emphasis on lower-rated, longer-dated securities, using our research capabilities to help identify those securities we believed offered good value relative to their risk. This approach generally worked well; within each of the Funds, these types of securities generally added to performance.

Unfortunately, this approach hampered the Funds' returns relative to their benchmark index when market conditions deteriorated in the final months of the fiscal year. As investors' confidence in the tax-exempt bond market generally waned, securities with heightened credit risk (such as lower-rated bonds) or interest-rate risk (namely, bonds with longer maturity dates) underperformed their higher-rated, shorter-dated counterparts.

As the Funds' fiscal year came to a close, we faced the need to make a decision about current market conditions — whether to treat them as a passing storm or as a fundamental change that warranted a shift in approach. We concluded that the increased volatility in the municipal bond environment at least required us to position the Funds somewhat more conservatively. This resulted in an increased focus on intermediate-maturity bonds with higher credit ratings, and a reduction of exposure to longer-dated, lower-rated bonds where appropriate.

Performance effects

Our conservative positioning was consistent with our overall philosophy of managing the Funds with an emphasis on preserving principal. We were willing to be somewhat more conservative than some other municipal bond managers (perhaps sacrificing a bit of performance potential) in an attempt to avoid greater losses during particularly difficult market downturns.

On an individual security basis, the Funds often saw good results from the types of bonds that outperformed for the fiscal year; namely, bonds with shorter maturities and relatively higher credit ratings. Within Delaware Investments Arizona Municipal Income Fund, Inc., for instance, bonds with relatively shorter maturities led the way, including bonds issued by the University of Arizona (maturing in 2018) as well as housing bonds issued by the City of Phoenix (maturing in 2020).

Leading contributors also included prerefunded bonds, which are very high-quality, short-duration bonds. (When a bond is prerefunded, the issuer has secured the bond's principal value by holding some type of risk-free asset — typically Treasuries — in an escrow account). Within Delaware Investments Colorado Municipal Income Fund, Inc., prerefunded bonds issued by the University of Denver and by the Denver Convention Center Hotel Authority were among the Fund's leading contributors.

Similar to the Colorado Fund, Delaware Investments Minnesota Municipal Income Fund II, Inc. benefited from holdings in prerefunded bonds that raised money for civic projects, as bonds for the St. Paul civic center were among its strongest contributors.

Leading contributors within Delaware Investments National Municipal Income Fund included bonds issued in New York that were backed by American Airlines (in an arrangement commonly known as an industrial development revenue bond) and an energy bond issued in Iowa by the state's Authority for Interstate Power. Both bonds advanced by more than 5%.

Across all four Funds, the weakest contributors to overall return included bonds issued by the Commonwealth of Puerto Rico. These bonds, which are widely held and are highly liquid, came under tremendous selling pressure during the last half of the Funds' fiscal year. In a sense, the characteristics that make Puerto Rico bonds desirable were the very characteristics that worked against them: They became the instrument of choice for municipal bond investors seeking to raise cash. (This was particularly true for mutual fund managers who needed to satisfy investor redemptions.) The resulting decline in bond prices was widespread and difficult to control, and it was a good example of the dislocation that municipal markets were suffering through.

As in prior reporting periods, we continued to follow our basic investment philosophy and management approach. We believe successful municipal bond investing requires rigorous credit analysis. In our opinion, there is no substitute for thorough credit research. On a bond-by-bond basis, we scrutinize each security we include in the Funds to help ensure our comfort level with its financial position and to feel confident that, in our view, any risks are more than offset by the potential income provided by the bond.

Fund basics

Delaware Investments
Arizona Municipal Income Fund, Inc.

As of March 31, 2011

Fund objective

The Fund seeks to provide current income exempt from both regular federal income tax and from Arizona state personal income tax, consistent with the preservation of capital.

Total Fund net assets

\$40 million

Number of holdings

60

Fund start date

Feb. 26, 1993

CUSIP number

246100101

Delaware Investments
Colorado Municipal Income Fund, Inc.

As of March 31, 2011

Fund objective

The Fund seeks to provide current income exempt from both regular federal income tax and Colorado state personal income tax, consistent with the preservation of capital.

Total Fund net assets

\$65 million

Number of holdings

62

Fund start date

July 29, 1993

CUSIP number

246101109

Delaware Investments
Minnesota Municipal Income Fund II, Inc.

As of March 31, 2011

Fund objective

The Fund seeks to provide current income exempt from both regular federal income tax and Minnesota state personal income tax, consistent with the preservation of capital.

Total Fund net assets

\$158 million

Number of holdings

103

Fund start date

Feb. 26, 1993

CUSIP number

24610V103

Delaware Investments
National Municipal Income Fund

As of March 31, 2011

Fund objective

The Fund seeks to provide current income exempt from regular federal income tax, consistent with the preservation of capital.

Total Fund net assets

\$31 million

Number of holdings

80

Fund start date

Feb. 26, 1993

CUSIP number

24610T108

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Sector/State allocations

As of March 31, 2011

Sector designations may be different than the sector designations presented in other Fund materials.

Delaware Investments

Arizona Municipal Income Fund, Inc.

Sector	Percentage of Net Assets
Municipal Bonds	93.71%
Corporate-Backed Revenue Bonds	6.13%
Education Revenue Bonds	11.93%
Electric Revenue Bonds	11.00%
Healthcare Revenue Bonds	17.28%
Housing Revenue Bond	0.48%
Lease Revenue Bonds	6.50%
Local General Obligation Bonds	5.71%
Pre-Refunded Bonds	3.28%
Special Tax Revenue Bonds	15.34%
State General Obligation Bond	0.81%
Transportation Revenue Bonds	6.17%
Water & Sewer Revenue Bonds	9.08%
Short-Term Investments	4.52%
Total Value of Securities	98.23%
Receivables and Other Assets Net of Liabilities	1.77%
Total Net Assets	100.00%

Delaware Investments

Minnesota Municipal Income Fund II, Inc.

Sector	Percentage of Net Assets
Municipal Bonds	98.57%
Corporate-Backed Revenue Bonds	5.78%
Education Revenue Bonds	9.68%
Electric Revenue Bonds	8.55%
Healthcare Revenue Bonds	18.84%
Housing Revenue Bonds	7.96%
Lease Revenue Bonds	6.33%
Local General Obligation Bonds	10.13%
Pre-Refunded/Escrowed to Maturity Bonds	20.51%
Special Tax Revenue Bonds	4.08%
State General Obligation Bond	0.70%
Transportation Revenue Bonds	5.09%
Water & Sewer Revenue Bond	0.92%

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Short-Term Investments	0.57%
Total Value of Securities	99.14%
Receivables and Other Assets Net of Liabilities	0.86%
Total Net Assets	100.00%

Delaware Investments
Colorado Municipal Income Fund, Inc.

Sector	Percentage of Net Assets
Municipal Bonds	94.95%
Corporate-Backed Revenue Bond	1.17%
Education Revenue Bonds	20.05%
Electric Revenue Bonds	7.00%
Healthcare Revenue Bonds	10.18%
Housing Revenue Bonds	2.69%
Lease Revenue Bonds	5.14%
Local General Obligation Bonds	8.41%
Pre-Refunded Bonds	15.76%
Special Tax Revenue Bonds	11.34%
State General Obligation Bonds	5.54%
Transportation Revenue Bonds	2.50%
Water & Sewer Revenue Bonds	5.17%
Short-Term Investments	3.56%
Total Value of Securities	98.51%
Receivables and Other Assets Net of Liabilities	1.49%
Total Net Assets	100.00%

(continues) 5

Sector/State allocations

Sector designations may be different than the sector designations presented in other Fund materials.

Delaware Investments

National Municipal Income Fund

Sector	Percentage of Net Assets
Municipal Bonds	94.07%
Corporate-Backed Revenue Bonds	10.56%
Education Revenue Bonds	14.08%
Healthcare Revenue Bonds	15.72%
Housing Revenue Bonds	6.39%
Lease Revenue Bonds	2.41%
Local General Obligation Bonds	3.73%
Special Tax Revenue Bonds	20.08%
State General Obligation Bonds	5.74%
Transportation Revenue Bonds	11.45%
Water & Sewer Revenue Bonds	3.91%
Short-Term Investments	4.58%
Total Value of Securities	98.65%
Receivables and Other Assets Net of Liabilities	1.35%
Total Net Assets	100.00%

State	(as a % of fixed income investments)
Arizona	1.93%
California	8.78%
Colorado	0.90%
Florida	22.89%
Georgia	2.36%
Hawaii	0.87%
Illinois	2.65%
Iowa	1.79%
Kansas	0.47%
Louisiana	0.85%
Maryland	3.11%
Massachusetts	7.50%
Missouri	2.42%
New Hampshire	1.04%
New Jersey	2.75%
New Mexico	1.49%
New York	13.72%
Ohio	3.72%
Oregon	0.44%
Pennsylvania	9.94%
Puerto Rico	4.73%
Texas	2.85%
Virginia	2.04%

Washington D.C.	0.76%
Total	100.00%

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Statements of net assets

Delaware Investments Arizona Municipal Income Fund, Inc.

March 31, 2011

	Principal Amount	Value
Municipal Bonds – 93.71%		
Corporate-Backed Revenue Bonds – 6.13%		
Maricopa County Pollution Control Revenue (Public Service - Palo Verde Project) Series B 5.20% 6/1/43	\$ 500,000	\$ 491,035
Navajo County Pollution Control Revenue (Public Service - Cholla Project) Series D 5.75% 6/1/34	500,000	544,660
Pima County Industrial Development Authority Pollution Control Revenue (Tucson Electric Power) 5.75% 9/1/29 Series A 4.95% 10/1/20 5.25% 10/1/40	250,000 500,000 400,000	247,718 481,255 346,416
Salt Verde Financial Senior Gas Revenue 5.00% 12/1/37	400,000	327,896
		2,438,980
Education Revenue Bonds – 11.93%		
Arizona Board of Regents System Revenue (University of Arizona) Series A 5.00% 6/1/39 Series 2008A 5.00% 6/1/18	500,000 150,000	487,790 168,881
Arizona Health Facilities Authority Education Facilities Revenue (Kirksville College) 5.125% 1/1/30	500,000	468,195
Glendale Industrial Development		