

WESTERN ASSET MUNICIPAL HIGH INCOME FUND INC.

Form N-CSRS

June 29, 2018

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 811-05497

Western Asset Municipal High Income Fund Inc.

(Exact name of registrant as specified in charter)

620 Eighth Avenue, 49th Floor, New York, NY 10018

(Address of principal executive offices) (Zip code)

Robert I. Frenkel, Esq.

Legg Mason & Co., LLC

100 First Stamford Place

Stamford, CT 06902

(Name and address of agent for service)

Registrant's telephone number, including area code: (888) 777-0102

Date of fiscal year end: October 31

Date of reporting period: April 30, 2018

ITEM 1. REPORT TO STOCKHOLDERS.

The **Semi-Annual** Report to Stockholders is filed herewith.

Semi-Annual Report

April 30, 2018

WESTERN ASSET
MUNICIPAL HIGH
INCOME FUND INC.
(MHF)

INVESTMENT PRODUCTS: NOT FDIC INSURED NO BANK GUARANTEE MAY LOSE VALUE

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Fund objective

The Fund seeks high current income exempt from federal income taxes.

The Fund invests primarily in intermediate- and long-term municipal debt securities issued by state and local governments. However, the Fund may invest in municipal obligations of any maturity.

Letter from the chairman

Dear Shareholder,

We are pleased to provide the semi-annual report of Western Asset Municipal High Income Fund Inc. for the six-month reporting period ended April 30, 2018. Please read on for Fund performance information and a detailed look at prevailing economic and market conditions during the Fund's reporting period.

As always, we remain committed to providing you with excellent service and a full spectrum of investment choices. We also remain committed to supplementing the support you receive from your financial advisor. One way we accomplish this is through our website, www.lmcef.com. Here you can gain immediate access to market and investment information, including:

Fund prices and performance,

Market insights and commentaries from our portfolio managers, and

A host of educational resources.

We look forward to helping you meet your financial goals.

Sincerely,

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Jane Trust, CFA

Chairman, President and Chief Executive Officer

May 31, 2018

II Western Asset Municipal High Income Fund Inc.

Investment commentary

Economic review

Economic activity in the U.S. was somewhat mixed during the six months ended April 30, 2018 (the reporting period). Looking back, the U.S. Department of Commerce reported that third and fourth quarter 2017 U.S. gross domestic product (GDP) growth was 3.2% and 2.9%, respectively. Finally, the U.S. Department of Commerce's second reading for first quarter 2018 GDP growth released after the reporting period ended was 2.2%. The deceleration in GDP growth in the first quarter reflected decelerations in personal consumption expenditures (PCE), exports, state and local government spending, and federal government spending and a downturn in residential fixed investment. These movements were partly offset by an upturn in private inventory investment and a larger increase in nonresidential fixed investment.

Job growth in the U.S. was solid overall and supported the economy during the reporting period. When the reporting period ended on April 30, 2018, the unemployment rate was 3.9%, as reported by the U.S. Department of Labor. This was the lowest unemployment rate since December 2000. The percentage of longer-term unemployed declined during the reporting period. In April 2018, 20.0% of Americans looking for a job had been out of work for more than six months, versus 23.8% when the period began.

Investment commentary (cont d)

Market review

Q. How did the Federal Reserve Board (the Fed) respond to the economic environment?

A. The Fed increased the federal funds rateⁱⁱⁱ twice during the reporting period. Looking back, at its meeting that concluded on September 20, 2017 before the reporting period began the Fed kept rates on hold, but reiterated its intention to begin reducing its balance sheet, saying, "In October, the Committee will initiate the balance sheet normalization program." At its meeting that ended on December 13, 2017, the Fed raised rates to a range between 1.25% and 1.50%. As expected, the Fed kept rates on hold at its meeting that concluded on January 31, 2018. However, at its meeting that ended on March 21, 2018, the Fed again raised the federal funds rate, moving it to a range between 1.50% and 1.75%.

Q. Did Treasury yields trend higher or lower during the reporting period?

A. Both short-term and longer-term Treasury yields moved higher during the six-month reporting period ended April 30, 2018. The yield for the two-year Treasury note began the reporting period at 1.60% its low for the period and ended the period at 2.49% equaling its peak for the period. The yield for the ten-year Treasury began the reporting period at 2.38% and ended the period at 2.95%. The low for the period of 2.32% occurred several times in November 2017 and the high for the period of 3.03% took place on April 25, 2018.

Q. How did the municipal bond market perform versus the taxable bond market over the reporting period?

A. The municipal bond market outperformed its taxable bond counterpart on a relative basis during the reporting period. For the six months ended April 30, 2018, the Bloomberg Barclays Municipal Bond Index^{iv} and the Bloomberg Barclays U.S. Aggregate Index^v returned -0.97% and -1.87%, respectively. Both municipal and taxable bonds were negatively impacted by the rising interest rate environment. The municipal market's relative outperformance was partially due to overall solid fundamentals and periods of positive investor demand.

Performance review

For the six months ended April 30, 2018, Western Asset Municipal High Income Fund Inc. returned -0.22% based on its net asset value (NAVⁱ) and -1.56% based on its New York Stock Exchange (NYSE) market price per share. The Fund's unmanaged benchmark, the Bloomberg Barclays Municipal Bond Index, returned -0.97% for the same period. The Lipper High Yield Municipal Debt Closed-End Funds Category Average^{vii} returned 0.38% over the same time frame. Please note that Lipper performance returns are based on each fund's NAV.

Certain investors may be subject to the federal alternative minimum tax, and state and local taxes will apply. Capital gains, if any, are fully taxable. Please consult your personal tax or legal adviser.

During this six-month period, the Fund made distributions to shareholders totaling \$0.15 per share. As of April 30, 2018, the Fund estimates that all of the distributions were

sourced from net investment income.* The performance table shows the Fund's six-month total return based on its NAV and market price as of April 30, 2018. **Past performance is no guarantee of future results.**

Performance Snapshot as of April 30, 2018
(unaudited)

	6-Month Total Return**
Price Per Share	
\$7.76 (NAV)	-0.22%
\$7.22 (Market Price)	-1.56%

All figures represent past performance and are not a guarantee of future results. Performance figures for periods shorter than one year represent cumulative figures and are not annualized.

**** Total returns are based on changes in NAV or market price, respectively. Returns reflect the deduction of all Fund expenses, including management fees, operating expenses, and other Fund expenses. Returns do not reflect the deduction of brokerage commissions or taxes that investors may pay on distributions or the sale of shares.**

Total return assumes the reinvestment of all distributions, including returns of capital, if any, at NAV.

Total return assumes the reinvestment of all distributions, including returns of capital, if any, in additional shares in accordance with the Fund's Dividend Reinvestment Plan.

Looking for additional information?

The Fund is traded under the symbol **MHF** and its closing market price is available in most newspapers under the NYSE listings. The daily NAV is available on-line under the symbol **XMHF** on most financial websites. *Barron's* and the *Wall Street Journal's* Monday edition both carry closed-end fund tables that provide additional information. In addition, the Fund issues a quarterly press release that can be found on most major financial websites as well as www.lmcef.com (click on the name of the Fund).

In a continuing effort to provide information concerning the Fund, shareholders may call 1-888-777-0102 (toll free), Monday through Friday from 8:00 a.m. to 5:30 p.m. Eastern Time, for the Fund's current NAV, market price and other information.

Thank you for your investment in Western Asset Municipal High Income Fund Inc. As always, we appreciate that you have chosen us to manage your assets and we remain focused on achieving the Fund's investment goals.

Sincerely,

Jane Trust, CFA

Chairman, President and Chief Executive Officer

May 31, 2018

RISKS: The Fund is a diversified closed-end management investment company designed

*These estimates are not for tax purposes. The Fund will issue a Form 1099 with final composition of the distributions for tax purposes after year-end. A return of capital is not taxable and results in a reduction in the tax basis of a shareholder's investment. For more information about a distribution's composition, please refer to the Fund's distribution press release or, if applicable, the Section 19 notice located in the press release section of our website, www.lmcef.com (click on the name of the Fund).

Investment commentary (cont d)

primarily as a long-term investment and not as a trading vehicle. The Fund is not intended to be a complete investment program and, due to the uncertainty inherent in all investments, there can be no assurance that the Fund will achieve its investment objective. The Fund's common stock is traded on the New York Stock Exchange. Similar to stocks, the Fund's share price will fluctuate with market conditions and, at the time of sale, may be worth more or less than the original investment. Shares of closed-end funds often trade at a discount to their net asset value. Diversification does not assure against market loss. The Fund's investments are subject to a number of risks, such as credit risk, inflation risk and interest rate risk. High-yield bonds, known as junk bonds, involve greater credit and liquidity risks than investment grade bonds. As interest rates rise, bond prices fall, reducing the value of the Fund's holdings. Municipal securities purchased by the Fund may be adversely affected by changes in the financial condition of municipal issuers and insurers, regulatory and political developments, uncertainties and public perceptions, and other factors. The Fund may invest in securities of other investment companies. To the extent it does, Fund stock holders will indirectly pay a portion of the operating costs of such companies, in addition to the expenses that the Fund bears directly in connection with its own operation. Investing in securities issued by other investment companies, including exchange-traded funds (ETFs) that invest primarily in municipal securities, involves risks similar to those of investing directly in the securities in which those investment companies invest. The Fund may use derivatives, such as options and futures, which can be illiquid, may disproportionately increase losses, and have a potentially large impact on Fund performance.

All investments are subject to risk including the possible loss of principal. Past performance is no guarantee of future results. All index performance reflects no deduction for fees, expenses or taxes. Please note that an investor cannot invest directly in an index.

The information provided is not intended to be a forecast of future events, a guarantee of future results or investment advice. Views expressed may differ from those of the firm as a whole.

ⁱ Gross domestic product (GDP) is the market value of all final goods and services produced within a country in a given period of time.

ⁱⁱ The Federal Reserve Board (the Fed) is responsible for the formulation of U.S. policies designed to promote economic growth, full employment, stable prices and a sustainable pattern of international trade and payments.

ⁱⁱⁱ The federal funds rate is the rate charged by one depository institution on an overnight sale of immediately available funds (balances at the Federal Reserve) to another depository institution; the rate may vary from depository institution to depository institution and from day to day.

^{iv} The Bloomberg Barclays Municipal Bond Index is a market value weighted index of investment grade municipal bonds with maturities of one year or more.

^v The Bloomberg Barclays U.S. Aggregate Index is a broad-based bond index comprised of government, corporate, mortgage- and asset-backed issues, rated investment grade or higher, and having at least one year to maturity.

^{vi} Net asset value (NAV) is calculated by subtracting total liabilities, including liabilities associated with financial leverage (if any), from the closing value of all securities held by the Fund (plus all other assets) and dividing the result (total net assets) by the total number of the common shares outstanding. The NAV fluctuates with changes in the market prices of securities in which the Fund has invested. However, the price at which an investor may buy or sell shares of the Fund is the Fund's market price as determined by supply of and demand for the Fund's shares.

^{vii} Lipper, Inc., a wholly-owned subsidiary of Reuters, provides independent insight on global collective investments. Returns are based on the six-month period ended April 30, 2018, including the reinvestment of all distributions, including returns of capital, if any, calculated among the 11 funds in the Fund's Lipper category.

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Fund at a glance (unaudited)

Investment breakdown (%) as a percent of total investments

The bar graph above represents the composition of the Fund's investments as of April 30, 2018 and October 31, 2017 and does not include derivatives. The Fund is actively managed. As a result, the composition of the Fund's investments is subject to change at any time.

Spread duration (unaudited)

Economic exposure April 30, 2018

Total Spread Duration

MHF 6.12 years

Benchmark 5.94 years

Spread duration measures the sensitivity to changes in spreads. The spread over Treasuries is the annual risk-premium demanded by investors to hold non-Treasury securities. Spread duration is quantified as the % change in price resulting from a 100 basis points change in spreads. For a security with positive spread duration, an increase in spreads would result in a price decline and a decline in spreads would result in a price increase. This chart highlights the market sector exposure of the Fund's sectors relative to the selected benchmark sectors as of the end of the reporting period.

Benchmark Bloomberg Barclays Municipal Bond Index
MHF Western Asset Municipal High Income Fund Inc.

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Effective duration (unaudited)

Interest rate exposure April 30, 2018

Total Effective Duration

MHF 6.16 years

Benchmark 6.00 years

Effective duration measures the sensitivity to changes in relevant interest rates. Effective duration is quantified as the % change in price resulting from a 100 basis points change in interest rates. For a security with positive effective duration, an increase in interest rates would result in a price decline and a decline in interest rates would result in a price increase. This chart highlights the interest rate exposure of the Fund's sectors relative to the selected benchmark sectors as of the end of the reporting period.

Benchmark Bloomberg Barclays Municipal Bond Index
MHF Western Asset Municipal High Income Fund Inc.

Schedule of investments (unaudited)

April 30, 2018

Western Asset Municipal High Income Fund Inc.

	Rate	Maturity Date	Face Amount	Value
Security				
Municipal Bonds 98.6%				
<i>Alabama 5.8%</i>				
Jefferson County, AL, Sewer Revenue:				
AGM	5.500%	10/1/53	\$ 400,000	\$ 444,084
Convertible CAB, Subordinated Lien, Step bond, 0.000% until 10/1/23; 7.900%	0.000%	10/1/50	3,020,000	2,511,976
Subordinated Lien Warrants	6.000%	10/1/42	1,120,000	1,289,400
Subordinated Lien Warrants	6.500%	10/1/53	3,000,000	3,526,650
Lower Alabama Gas District, Gas Project Revenue	5.000%	9/1/46	1,700,000	2,015,605
<i>Total Alabama</i>				<i>9,787,715</i>
<i>Arizona 3.5%</i>				
La Paz County, AZ, IDA, Educational Facility Lease Revenue, Charter School Solutions, Harmony Public School Project	5.000%	2/15/36	1,000,000	1,038,460 (a)
Navajo Nation, AZ, Revenue	5.500%	12/1/30	190,000	209,777 (a)
Phoenix, AZ, IDA, Education Revenue:				
Basis School Inc.	5.000%	7/1/35	1,000,000	1,027,190 (a)
Great Hearts Academies	5.000%	7/1/41	1,200,000	1,280,436
Salt Verde, AZ, Financial Corp. Senior Gas Revenue	5.000%	12/1/37	1,500,000	1,756,095
University Medical Center Corp., AZ, Hospital Revenue	6.250%	7/1/29	500,000	524,905 (b)
<i>Total Arizona</i>				<i>5,836,863</i>
<i>California 10.2%</i>				
Alameda, CA, Corridor Transportation Authority Revenue, Second Subordinated Lien	5.000%	10/1/34	500,000	556,935
Anaheim, CA, Public Financing Authority Lease Revenue	5.000%	5/1/46	2,000,000	2,218,060
California State PCFA, Water Furnishing Revenue	5.000%	11/21/45	2,960,000	3,014,582 (a)
California State Public Works Board, Lease Revenue, Various Capital Project	5.125%	10/1/31	1,500,000	1,639,890
California Statewide CDA, Student Housing Revenue:				
Provident Group-Pomona Properties LLC	5.600%	1/15/36	500,000	533,290 (a)
Provident Group-Pomona Properties LLC	5.750%	1/15/45	360,000	384,152 (a)
Inland Valley, CA, Development Agency, Successor Agency Tax Allocation Revenue	5.000%	9/1/44	500,000	538,675
M-S-R Energy Authority, CA, Gas Revenue	7.000%	11/1/34	2,000,000	2,794,260
M-S-R Energy Authority, CA, Gas Revenue	6.500%	11/1/39	3,000,000	4,155,270
Redding, CA, RDA, Tax Allocation, Shastec Redevelopment Project	5.000%	9/1/29	600,000	600,738