Investment Trust Newsletter
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STOCKMARKET INTELLIGENCE

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Andrew McHattie
Publisher

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Investment Trust Newsletter

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This month we have coverage of a number of manager interviews, an in-depth look at the Downing Strategic Micro-Cap new issue, stockbrokers research, and news of some interesting corporate developments relating to redemptions, dividends, management arrangements, rollovers, requisitions, name changes, debt issues, and a merger. Let's dive straight in.

Major Price Changes Over One Month

Globalworth Real Estate Investments	+14.23%
Macau Property Opportunities	+13.00%
India Capital Growth Fund	+12.39%
Dunedin Enterprise	+12.04%
Schroder Real Estate	+9.70%
Fidelity Asian Values	+8.79%
Jupiter European Opportunities	+7.88%
Aberdeen New India	+7.57%
Standard Life Invs Property Income	+7.29%
Chelverton Small Cos Dividend	+7.17%
Prospect Japan Fund	-11.80%
Better Capital PCC 2012	-9.76%
Symphony International	-9.56%
LXB Retail Properties	-8.64%
Adamas Finance Asia	-6.14%

Major Price Changes Over One Year

Baker Steel Resources Trust	+133.85%
EPE Special Opportunities	+113.15%
Industrial Multi Property Trust	+102.33%
3i Group	+75.80%
BlackRock World Mining Trust	+66.55%
Tiso Blackstar Group	+65.50%
Livermore Investments Group	+63.73%
India Capital Growth	+62.61%
Riverstone Energy	+60.76%
Crystal Amber Fund	+60.28%
Infrastructure India	-63.33%
LXB Retail Properties	-37.69%
LMS Capital	-35.61%
Marwyn Value Investors	-19.67%
Candover Investments	-17.09%

£25m market capitalisation filter applied. Source: Morningstar.

LMS Capital (LMS, 43p) is not well-known, but it has been a regular in the list of fallers over the last twelve months, down by more than 35% over this period. As of last summer, the company has a new manager in Gresham House and a new private equity mandate, but it has been struggling with its legacy assets which have proved disappointing. In January the company reported on some deteriorating valuations and estimated its NAV at 69.5p, down from 88p at the end of June 2016. After some better news this month on the disposal of its holding in an IT services business called 365IT, JPMorgan Cazenove reckoned the NAV may have ticked back up to 72.7p, implying a very wide discount of just over 40%. There is clearly a lot of uncertainty over the realisable value in the portfolio though, so that may not be the bargain it first appears.

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It's a slightly similar story at **Better Capital PCC 2012** (BC12, 27.75p), where the fund has been suffering write-downs. You may have read in the press that the fashion chain Jaeger – owned by Better Capital - has fallen into administration. BC12 just managed to sell its debt instruments in BECAP (Jaeger) Ltd before this news, but at a heavy loss.

Staying with the fallers, **Prospect Japan Fund** (PJF, US$1.1075), which announced in January that it was in discussions with the parent company of the managers, Prospect, about a takeover, has slipped back. Prospect has not clarified its intentions by the statutory deadline date, which has now been extended. Discussions are "ongoing."

TR PROPERTY INVESTMENT TRUST PLC (TRY, 317.4p)

Investors nervous about valuations in equity markets might be thinking about squirrelling some money away into property instead, and TR Property is in many ways an obvious choice. This multi award-winning pan-European indirect property trust is one of the largest in its sector, has a fine track record that tops the five-year performance tables of its peers, offers a yield of 2.9%, and is available on a discount of 12.3%.

Manager Marcus Phayre-Mudge has a slick turn of phrase and describes property as "an income stream with a capital kicker." At the moment he says that total returns are strong with yields in excess of 3%, rental growth, and capital values moving in the right direction. Amongst property shares – where the trust invests most of its money, there are discounts on mainstream property companies such as British Land and Land Securities that seem to be pricing in lots of bad news. Marcus thinks such pessimism may be misplaced and points to the lack of new supply in many markets because banks have stopped speculative lending. He says that no bank money has gone anywhere near any of the recent landmark developments in the City of London. The fall in the pound has also driven up construction costs, meaning new buildings cost more to erect. "This is an exciting moment", he says, adding "it is rare that I've seen the market have such a disconnect", offering much higher yields on property than on bonds even though earnings and dividends are growing.

The trust has 31% in UK shares at present, and 8% in direct UK property, and 61% in continental Europe. The UK exposure has dropped, following the currency effect through the benchmark. In Austria and Germany, which accounts for 20%, much of the exposure is residential in the form of buy-to-let property companies that offer earnings yields of 5% and dividend yields of 4%. Marcus also favours logistics (warehouses), Paris, Stockholm and Madrid offices, and UK student housing, where he owns Unite. While risks are plentiful, Marcus clearly has a positive outlook, and thinks the sector offers value, particularly for 'bond refugees' seeking non-equity income. He thinks the trust's shares offer decent value too, saying the long-term average discount is around 6%-8% and that the shares were on a premium 16 months ago. We agree and rate these shares a buy along with some others in the sector. Last month we recommended **Kennedy Wilson Europe Real Estate** (KWE, 978p), which has edged higher but still sticks out with a discount of 19.2%.

HENDERSON ALTERNATIVE STRATEGIES TRUST PLC (HAST, 279.5p)

Managed by Henderson since 2013, when they took over the old SVM Global trust that had run into difficulties, we think Ian Barrass and James de Bunsen took their time to refresh the portfolio and to really put their own stamp on this £125m trust. Now that about 85% of the inherited portfolio has been switched, we think this trust, in the 'flexible investment' sector, can argue for a place in portfolios that need some diversification, or something different.

Ian puts it nicely when he says the trust is "providing investors with access to funds they wouldn't normally invest in themselves." This is a one-stop shop for those esoteric specialist and alternative trusts that sometimes crop up in our lists of risers and fallers on the front page, or get mentions elsewhere. The trust's largest holdings include **Riverstone Energy,** Majedie Tortoise Fund, **Blackstone/GSO Loan Financing,** and **Polar Capital Global Financials.** It also invests in hedge funds and private equity funds that are less well-known. The portfolio will generally be 30-40 holdings focused on five investment categories, namely (i) specialist sectors, such as credit funds, biotech, renewable energy; (ii) specialist geographies, particularly in emerging markets; (iii) private equity; (iv) hedge funds; and (v) property. There are limitations on exposures to each segment, a target of 50%-70% listed (meaning 30%-50% unlisted), and a total return target of 8%pa over three years. The broad range of categories means there is enough work for two managers. Ian has been at Henderson for 12 years and has real multi-asset experience spanning 32 years in total, and James is a specialist in hedge funds, derivative strategies, commodities and risk management.

The trust had a very decent 2016 and currently ranks third of 14 trusts in its sector over the last twelve months. It also paid a modest dividend, yielding 1.4%, and shareholder returns have been boosted

further by a narrowing of the discount from 19.8% at the September year end to 13.9% now. Looking ahead, Ian sees some valuation opportunities in private equity (he mentioned **Princess Private Equity, HarbourVest Private Equity** and **Standard Life European Private Equity**) and also in hedge funds, where he says that some skilled managers are able to deliver equity-like returns at a lower risk. Ian also highlighted CEIBA Investments, which invests in Cuban real estate assets. He is fairly cautious on broader equity markets, where he notes that when interest rates start to rise, market multiples tend to contract.

For exposure to smaller closed-end funds on wide discounts we think Nick Greenwood's Miton Global Opportunities (MIGO, 236.75p) does a good job, but if you want to spread your wings a little wider and include more alternative assets, with more of an emphasis on quality rather than discounts, then HAST also seems worth considering.

SCHRODER ASIAPACIFIC FUND PLC (SDP, 384.125p) SCHRODER ORIENTAL INCOME FUND LTD (SOI, 247.375p)

We were pleased to have an update on this pair of Asian trusts managed by Matthew Dobbs of Schroders. The £700m Schroder AsiaPacific Fund is the top performer in its sector over the last year, while Schroder Oriental Income couples Asian investments with a 3.5% yield.

"These countries are in good shape" Matthew reassures us at the outset, while examining how nearly all emerging markets were hit by Trump's surprise election in November and his protectionist rhetoric. They have since recovered, and most are up quite strongly in 2017 to date. Matthew says as well that historically, Asia does not do too badly when America raises interest rates, so he is not fearful about that. Except for Malaysia, all Asian countries have decent external debt positions and Asia Pacific economic data is generally surprising on the upside. After a couple of disappointing years, earnings expectations look much more robust for 2017. Worries about China have receded too. Matthew says "China as an issue is kind of parked, allowing other things to work in Asia."

Valuations in aggregate still look cheap too. Matthew says "OK, they are not as cheap as they were, but there is still a bit of value." The average price to book ratio since 1991 is around 1.9 times and currently stands closer to 1.5 times; the historic P/E average over the same period is about 17.5x and is now more like 15x. That may understate the region's attractions, as Matthew says "balance sheets are stronger than I can ever remember them being", and he also says that the opportunity set expands once you look beyond the mega-caps. He says the region has a lot of good entrepreneurs and open consumers who respond well to disruptors. The Chinese, for example, are much more keen on the idea of driverless cars than more traditional American consumers. Matthew says it is important to look for dynamic small and mid cap stocks.

Schroder AsiaPacific has 68 holdings in total, and the largest four are all technology companies, namely Taiwan Semiconductor, Samsung Electronics, Tencent Holdings, and Alibaba Group. IT is the biggest sector overweight, but the trust is not sticking its neck out too far though – we have commented before about how we regard this trust as a solid, professionally-run trust that has delivered decent returns over the long run and probably has some very satisfied shareholders. You could join them by buying on a 12.1% discount, which we think offers some value against a sector average of 8.1%, particularly as we have seen some sharp tightening of individual ratings (**Fidelity Asian Values,** for example, in to a 1.8% discount).

Schroder Oriental Income is, as the name suggests, more income-focused, and here Matthew reckons Asia punches above its weight, with many more stocks now yielding more than 4% and paying good dividends with comfortable payout ratios. This trust is skewed towards dividend payers, which means it is overweight Hong Kong and underweight China, and is overweight in telecoms and real estate. Against SDP it is more conservative and has a lower beta, as we would expect. You do have to pay up for the income though – the shares trade on a 1% premium to NAV, which looks fully valued to us. We prefer Schroder AsiaPacific as an investment proposition at present.

MAJEDIE INVESTMENTS PLC (MAJE, 286.875p)

Majedie was last covered in detail in the newsletter in September 2015 when the shares were 260p. At the time we acknowledged its improved performance since changing investment policy in 2014, but we did not want to buy it on a premium. That seems a sound call as the shares have dropped to a 9.1% discount. In mid-March we met the trust's chief executive, William Barlow, for an update.

Classified as a global trust, Majedie does not make individual investments itself, but holds its exposure indirectly, through six Majedie Asset Management (MAM) funds. It also has a significant holding in the management company, like **Lindsell Train Investment Trust** (LTI, 777.5p). Two of the fund holdings are quite small allocations – 3.4% in the MAM Global Focus Fund at the turn of the year and

3.8% in the MAM US Equity Fund. Another 9.4% is in the MAM Global Equity Fund and 9.7% in the MAM UK Income Fund. That leaves the 'big two' – MAM Tortoise Fund (15.8%) and MAM UK Equity (31.2%).

The MAM UK Equity Fund has outperformed the FTSE All-Share Index in eight out of the last ten years, with 2016 being a strong year, producing a return of 22.6% against 16.8% from the index. Undoubtedly the currency would have helped, with international blue-chips such as Royal Dutch Shell, HSBC, BP, Barclays, and Anglo American prominent. William said that since the year-end, some money has been taken out of the UK fund and allocated instead to the Tortoise Fund, which is a global long/short equity fund that aims for positive absolute returns. This was really about "taking some equity risk off the table." William says the trust is intended to have an "all-weather" investment style that is very much about the returns over the cycle, hence the multi-manager approach.

Perhaps the other really key driver for the share price, apart from these fund allocations, is the holding in the management company, which accounted for 25.4% of the assets at 31st December. This is a real unique selling point (USP) for the trust. MAM had a total of £13.6bn of assets under management at the turn of the year, and that is "a little bit higher now", William says. The Tortoise Fund has been re-opened and has a little over a billion pounds of assets. It is likely to be closed again at £1.5bn. MAM is a growing fund management house, and William talked about the style of teamwork that ensures a rich debate, without a 'star manager' culture. New managers have been brought in from outside to bring new perspectives and to challenge existing methods, and of course the trust has a very deep understanding of exactly how they work, having such a close relationship. In terms of the value of the trust's stake, William reiterated there is a formula for this, based on a rolling three-year metric that tends to lag when AUM is rising, as it has been. This augurs well.

There are a couple of other special factors here that need highlighting. One is the trust's debt – it has two expensive debentures that run to 2020 and 2025. The first of these, accounting for £13.5m of the £34m debt, rolls off in three years' time, which will be a relief. William says he sees the trust having debt going forward, but perhaps not quite as much. The remaining debt may be diluted somewhat as well if the trust is able to grow a little through tap issues that have been used when the shares have been trading closer to asset value.

The second point is about a 13% holding owned by Aviva. It is well known that Aviva has been selling its legacy stakes in investment trusts, but this one is still remaining. William was phlegmatic about it, saying it "will get sorted out" and that the Aviva investors were very sensible and realistic about how this might be achieved. The trust will not want to buy the shares back because that would bolster the debt as a percentage of assets. If, in the meantime, there is some perceived 'overhang' that casts a shadow over the shares and their rating, that could of course create an opening for opportunistic buyers.

Majedie seems set on a steady course, investing through the MAM funds. The current allocations give it a higher UK weighting than some of its peers, but of course the FTSE 100 Index is highly international in any case. The UK weight also allows Majedie to yield a little more and to pay a progressive dividend. The trust's yield is currently 3% against a sector average of only 1.4%. It might become a little more global over time, particularly as the management company stake pays a good dividend, but there is no reason to expect any major changes here.

Majedie seems a reasonable performer in its peer group, ranked highly (5/24) over three years, though less strong over one year (18/24), and we think the shares are worth considering at the right price. The management company stake is a big differential here that could turbo-charge the returns for years to come. We might hope the Aviva stake causes the discount to drift out to double-figures to enable a good entry point.

NEW ISSUE

Downing Strategic Micro-Cap Investment Trust plc

We gave this new issue a brief mention on the back page last month, but we have since had the opportunity to meet the manager Judith MacKenzie and to learn more about her approach and how it differs from the other UK micro-cap trusts from River & Mercantile and Miton. Research from Professors Paul Marsh and Elroy Dimson of London Business School, which has been widely reported, shows that the smallest UK companies have outperformed substantially over the very long-term, so we think it makes sense to consider a spot for them in portfolios. This trust is targeting a compound return of 15%pa over the long term.

Describing herself as a "roving" investment manager, Judith MacKenzie spends a lot of time on the road, visiting companies, meeting management, and making sure she has a deep first-hand understanding of (potential) portfolio constituents. She has plenty of experience, with 20 years work in this realm, advising and investing in micro-cap companies. She already manages an OEIC with a similar mandate that has delivered strong returns, up 133% over five years, outperforming its peer group over one, three, and five years. Over three years it is ranked 6th out of 45 funds, and over five years it is ranked

11th out of 45. Downing is possibly best known for its VCTs, which are focused on even smaller companies, and Judith shares some of that heritage with her public equity team of six, applying techniques that are more common in private equity. This means extensive due diligence and engaging with management, working with them to achieve the best outcome.

This new investment trust, which is seeking to raise up to £100m (more probably £50m-£60m), plans to take 12-18 strategic investments in companies capitalised at less than £150m. This is not quite the same as the open-ended fund, which is more diversified with 25-30 holdings. By taking larger, focused stakes, Judith says the idea is that the new investment trust will focus on what has been the best section of the OEIC. Being an open-ended fund and therefore in need of some liquidity, the OEIC also invests in some value stocks, whereas this new trust can be more pure. It's not easy to take these positions in illiquid stocks though: Judith says "you have to engineer your way in and engineer your way out." It can take eight to ten months of work and due diligence to make an investment decision. The universe extends to around 1000 micro-cap companies, of which around 100 are on an active list and perhaps eight are in the due diligence process. Patience is sometimes needed to find an entry point, which might often be through a placing. Once in, Judith says their investment horizon is typically between three and seven years, and the team will engage actively with executives. Downing believe a proactive investment approach can help smaller companies realise their potential. Downing sometimes has the power to appoint people to boards, although in general it prefers to discuss board appointments. It also provides access to capital to fund acquisitions, restructure debt or improve the operating structure. It can also advise on management incentive plans, where options are structured to incentivize executives to realise value over a fixed time period, and to be rewarded based on shareholder returns.

"We find value down where we hunt", Judith says, and she showed us statistics from Thomson Reuters showing that sub-£50m companies have an average of 0.5 investment analysts following them, compared to 7.8 at the top end of companies over £500m. Many are simply ignored. The median yield is higher at 3.4% against 2.7% for the larger companies, and the median forward P/E ratio is much lower at 10.6 times against 16.5 times. Judith is expecting a 'natural yield' of around 1.8% from the portfolio once it is established, but the trust is not expecting to pay out any income as dividends.

Judith does not expect to invest in any IPOs, nor in any 'blue-sky' operations that have listed with a great idea but no profits. Mining and exploration is off the agenda too. "We like things we can see, touch, kick", Judith says. She likes to visit companies on site and to talk to operational staff as well as management. As well as good products, she is looking for a quality management team, efficient capital management, good free cash flow, a value catalyst strategy, and a discounted entry value. Judith ran through several companies that the team has invested in, to give a flavour of the style. You may recognise a couple of names from Pennant International, Accumuli, Office2Office, Science in Sport, and Universe.

We like the fact that the Downing One VCT will put £10m into this investment trust, Downing Group is adding about £1m and the board is putting in £240,000 between them. Just as Downing aims to align its interests with the management of its investee companies, the same applies here with the trust.

Of course the risks of a highly-focused micro-cap trust investing where liquidity is poor are fairly obvious, and it is likely this trust may have periods of underperformance. We expect its future performance to have little correlation with market indices or with other trusts. It's not a short-term speculation, and we do not recommend it for investors looking to make a quick turn. We do think though that it looks an attractive prospect for long-term investors, which raises the question of whether it makes sense to invest at the launch (where an offer for subscription should enable you to do so). One key factor here is discount control, since no-one wants to pay a small premium for initial access, only to find the trust on a double-digit discount in a year or two. There has been no savage de-rating so far for **Miton UK Microcap** (MINI, 59.125p), on a 5.9% discount, or **River & Mercantile UK Micro** (RMMC, 148.5p) on a 6.4% discount, but they are both on moderate discount ratings now, making it much harder to swallow the 100p asking price for the new Downing trust which will have an initial NAV of around 98p. Like Miton, Downing will be building in a 'liquidity event' – the opportunity to redeem shares after three years and then every two years thereafter – to make sure the discount is limited. This quasi open-ending does not sit too easily with the management claims that the investment trust will be so much more 'pure' than the OEIC, particularly when coupled with a 15%pa buyback capability, but that is a fairly small niggle. Of greater significance is that it may take a while to get the money invested – perhaps eight to ten months - and then some patience may be required for performance to come through. Judith told us that they have been working on the pipeline for two years and that some of the target companies are already in the process of change, but we nevertheless have our doubts about whether these shares can get off to a flying start. **We were impressed by the manager and her detailed approach, and we believe this trust could become a really popular core holding in future years, but we would still prefer to wait six months before making a move.**

STOCKBROKERS RESEARCH

Cenkos issued an update note on **F&C UK Real Estate Investments*** (FCRE, 103p) on 6th April, pointing to its "robust income-focused returns." The trust has a diversified portfolio that includes offices, industrial and retail property, with 61% by value located in the South East of England, including 15% in London. Cenkos say the portfolio's void rate has fallen to just 3% and the weighted average lease to expiry is relatively high at 7.1 years. The covenant strength is robust with the top 10 tenants major nationals accounting for 44% of the rent roll. Rental income security and covenant strength are at the heart of the company's long term business model, and the portfolio benefits from a yield premium in all sub-sectors. Debt is sourced at an average of 3.3%, with 4.5x interest cover, and the note says "the portfolio has continued to outperform the IPD Index in rental and capital terms with an ungeared total return of 3.8% in H1/2016-17. In the three financial years to June 2016 the average ungeared total return was 12.8%." The broker concludes "the shares have performed well relative to the UK REIT sector, with far less share price volatility. This reflects, in our view, the high quality of the investment portfolio and its strong income profile and covenants. The shares are trading at a small premium to NAV with the support of a 5% dividend yield – with quarterly dividends now fully covered by rental profits." They rate the trust a long-term buy.

Numis has made a couple of changes to its recommendations list, with one addition and one removal. The addition is **Murray International** (MYI, 1212.5p) as a core buy now that it is trading on a discount, albeit modest at 1%. The broker says the share price return of 4.6% in 2017 so far has lagged significantly behind the NAV return of 10.7%, presenting an opportunity. The note says the trust, managed by Bruce Stout, "has an excellent long term record and pays an attractive quarterly yield of 3.9%pa." On the way out is **Picton Property** (PCTN, 84.75p), previously a trading buy. Its strong share price performance, up by 14% in the year to date, means it is back trading on a premium of 5%.

Stockdale Securities spent four days in March on the road in India with the managers of **India Capital Growth Fund*** (IGC, 92.5p), meeting companies, brokers, media, and government officials. They say that while the issue of non-performing loans within the banking sector is expected to restrain growth from re-accelerating significantly from c.7% figure it stands at, in the short-term the policies being implemented by the BJP government lay the foundation for an acceleration in growth in the future. The note concludes "we continue to recommend that investors buy India Capital Growth Fund to capture India's accelerating growth."

A note from Panmure Gordon on 11th April on **Baillie Gifford Shin Nippon*** (BGS, 640p) notes that Japanese equities have returned around 95% in sterling terms since the start of Abenomics in December 2012, stimulated by yen denominated earnings growth over this period. The markets have simultaneously re-rated as valuations responded to earnings growth. Panmure suggest that while sentiment remains positive, Japanese market valuations allow some upside, and the trust will continue to add value. BGS offers an opportunity to invest in a portfolio of companies with superior earnings growth (10%-15% pa compounding), applying innovative and disruptive business models. The trust continues to focus on asymmetric returns that have driven outperformance since launch to date. Over the past twelve months BGS has traded at a premium to NAV 68% of the time. Panmure believe "superior performance justifies the premium."

JPMorgan Cazenove has reiterated its 'overweight' stance on **Riverstone Energy** (RSE, 1311.5p) after a management meeting. This fund has 15 companies in its portfolio, although the top five represented 78% of the asset value at the turn of the year. The largest two, Centennial (27%) and CIOC (25%), represented over half of the total value. A significant majority of the portfolio is focused on the Texas Permian & Eagle Ford basins (Centennial, Three Rivers) and Western Canada (CIOC) where there is a significant proportion of acreage from which it is economic to produce oil and gas from at current prices. Centennial is a publicly traded exploration and production company that plans to grow production. It currently produces 10,700 barrels of oil per day (boepd) and wants to ramp this up to 50,000 with the aid of its cash pile in excess of US$100m. CIOC is further down the line and has already grown production five-fold to 16,000 boepd since Riverstone first invested in 2015. A larger firm operating on land nearby has achieved substantial production growth and illustrates the potential, Riverstone says, both for improvements in size and in valuation. Three Rivers III, another holding, is different in that it bought cheap land that it has been focused on improving by proving potential using test wells. Riverstone says its acreage multiples have increased significantly, making it a likely sale candidate.

You have probably read about the two-way pull on oil prices, with OPEC trying to cut production as fast as new North American operators are ramping up. Riverstone say that 2016 saw continued substantial reductions to drilling and completion costs that have fallen between 50% and two-thirds compared to three years ago. These cost reductions have come with significant efficiency gains and the implementation of new technologies such as pad drilling (essentially drilling multiple wells at once from one location), extended laterals (which increases the potential amount recoverable from a single well), and

increased well pressure in laterals. These cost reductions have meant oil production across North America has become economic in an increasing number of locations despite the fall in oil prices since 2014, although the effect is most pronounced among the highest quality basins, where the strata are that much deeper and in more layers. As rig counts increase, some of these cost reductions may partially reverse as service companies and their equipment come under greater demand, so higher oil prices may lead to lower margins, but are still a positive. Riverstone sees upside to the oil price from current levels, principally due to the substantial capex cuts among the major oil companies which they believe are yet to fully take effect in terms of supply reductions.

JPMorgan Cazenove says "Riverstone has a focused portfolio with the key assets located in some of the most attractive areas of North America in terms of potential well economics. We like Riverstone's build-up approach and capital discipline which means only those commitments that are most economic actually draw down capital. There are clear value drivers for the key assets in the portfolio with a range of strategies in place." At the time of this note the shares stood on a 16.6% discount against the broker's NAV estimate of 1581p per share. The note concluded "this looks wide relative to an average of 12.4% for the UK Listed Direct Private Equity sector (ex 3i). RSE offers a unique investment exposure in both the investment companies universe and the London market as a whole. We think RSE represents one of the best potential growth opportunities and we reiterate our overweight recommendation."

Winterflood published a note on **Scottish American*** (SCAM, 338.625p) on 6th April. The trust, known commonly as SAINTS, is a global equity trust managed by Baillie Gifford with the objective to deliver real dividend growth by increasing capital and growing income. Dominic Neary has been responsible for the management of SAINTS since February 2014 and he is supported by James Dow and Toby Ross, who were appointed as deputy managers last year. The team is focused on three key areas: growth, income and dependability. As at the end of February, SAINTS' equity portfolio accounted for 99% of net assets, with the remainder of invested assets allocated to bonds (7%), direct property (18%) and net liquid assets (1%). SAINTS' direct property portfolio is managed by OLIM Property, a specialist property manager run by Matthew Oakeshott. The portfolio consisted of 22 properties across the UK at the end of last year and was valued at £61m, with a yield of 6.8%. SAINTS has a long history of paying a progressive dividend, achieving dividend increases in each year for over 36 consecutive years. Dividends are paid quarterly. The fund has grown its dividend from 7.40p per share to 10.83p over the last ten years, equivalent to a compound annual growth rate of 3.9%, ahead of consumer price inflation (2.4% pa).

Winterflood say "the global income growth strategy is an important area for Baillie Gifford and we believe that SAINTS' investment team benefits from the best ideas across the firm. The strategy has evolved over the last few years and the emphasis is very much on income growth. In our opinion this should ensure that the fund is well-placed to continue to grow its dividend. SAINTS has tended to trade on a premium to its NAV over the last five years (with debt at fair value). While a market setback could result in discount volatility, we believe that the rating is underpinned by SAINTS' long-term dividend growth record, its yield of 3.3% and the strength of Baillie Gifford's stock picking ability."

NEWS ROUND-UP

Full year results from our ISA recommendation **BlackRock Emerging Europe** (BEEP, 322.375p) were very strong, revealing asset growth of 55.8% for the year to 31st January, ahead of the benchmark return of +48.6%. We note the discount has narrowed slightly to 9.1%, perhaps helped by an upgrade by the stockbrokers JPMorgan Cazenove from neutral to overweight. The shares are still a buy in our view, as are the other three trusts we tipped for your ISAs.

Dunedin Enterprise (DNE, 370p), which announced a little over a year ago that it would start a managed wind-down of its assets, has taken a next step. Subject to shareholders approval the trust plans to make a pro rata bonus issue of 'B' shares that may be redeemed at the option of the company. Effectively this will be a way of returning cash, when the trust has paid off its bank borrowings and has cash in excess of its capital requirements. The shares have responded well to this development, rising by 12% over the month, and on a discount of 25.9% we might expect more appreciation in due course if the trust is able to negotiate some good exits.

In the same sector, **SVG Capital** (SVI, 740.75p) has completed its third and final tender offer. Some 41.76m shares were repurchased at 715p, returning £298.6m, and the board still expects to propose a winding up resolution to shareholders on or after 31st May this year.

Martin Currie Asia Unconstrained (MCP, 375.375p) has changed its dividend policy so that it will in the future pay dividends partly out of capital. The plan is to set the capital distribution at 2% of the prior year-end ex-income NAV, boosting the total yield now to around 4.5%. This is intended to narrow the discount to NAV, but to us this is simple sleight-of-hand, and we cannot fathom why a simple of return of capital would encourage investors to pay more for the same assets. We do not like this policy, which to us smacks of financial engineering and does not sit well with the industry virtues of simplicity and transparency.

P2P Global Investments (P2P, 832.25p) issued a short and terse-sounding statement on 4th April saying "following discussions with MW Eaglewood Europe LLP (the investment manager) and significant shareholders of the company, the board has resolved to initiate a review of the company's investment management arrangements. The board will update shareholders as to the outcome of the review in due course." The trust's returns have been below projections to date (although positive for 33 consecutive months) but this was nevertheless a surprising announcement, suggesting a change may be imminent. We have no particular insight into what might happen next, but it seems likely to us that any material change could be better news for shareholders and may help the currently wide discount of 16.8% to narrow further (it has already moved in from 20%-plus). On that basis we think these shares have some speculative attractions now.

It may be relevant to note that for reasons relating to its corporate structure and potential conflicts, the **SME Loan Fund** (SMEF, 97.5p) is withdrawing from the loan origination platform sector. It has appointed SQN Capital Management as its new manager, and is proposing to amend its investing policy to concentrate on wholesale lending, trade and receivable finance and collateralised lending opportunities as either debt or structured notes including equity or equity participations. The fund is also changing its name to SQN Secured Income Fund plc so that its ticker will become SSIF from 2nd May. It is not all doom-and-gloom for the platform loan sector though, with **Funding Circle SME Income** (FCIF, 103.25p) raising a further £142m from a 'C' share issue. It expects to invest the extra funds within nine months.

Polar Capital Global Healthcare Growth & Income Trust (PCGH, 204.375p), which was always designed with a fixed time-frame to January 2018, has made some proposals for its future. The trust is offering a cash exit at NAV less costs, through a tender offer, but assuming it can retain at least £200m of assets (out of about £250m currently, plus a new placing and offer) the trust will continue in a slightly different format. The plan is to change the name to the simpler Polar Capital Global Healthcare Trust and to become more focused on growth. The trust still expects to pay a dividend in the future, but at a lower level. This will enable it to compete head-to-head with **Worldwide Healthcare Trust** (WWH, 2320.5p) and also (less directly) with the specialist biotech trusts, all of which are focused mainly on growth.

Changes may also be afoot at the smaller companies trust **Strategic Equity Capital** (SEC, 205.875p), where you may remember the manager Stuart Widdowson resigned from the managers, GVQ Investment Management. He has moved to Harwood Capital Management, which is chaired by Ian Armitage and owns a company called Growth Financial Services (GFS). That's relevant because Mr Armitage and GFS own just over 5% of SEC, and recently tried to make a requisition request to the board, which was rebuffed. It seems likely they will try again and ultimately there is a chance that this trust will move its mandate to Harwood and back to Stuart Widdowson. That could be good news for the shares and for the rating, currently a discount of 14%.

Scottish Mortgage Trust (SMT, 371.75p) has taken advantage of its size and prominence to issue long-term debt at attractive rates. The trust is replacing some existing bank borrowing with three fixed rate notes and a refinancing of a debenture, totalling £125m in aggregate, at a weighted average annual coupon of 3.22%. That is cheap in historical context, and as the trust is a keen proponent of the use of gearing, locking in the debt at such a low interest rate seems very sensible.

The £47m **Threadneedle UK Select Trust** (UKT, 209.25p) has announced it is planning to merge into the larger **Henderson High Income Trust** (HHI, 188.625p), capitalised at £211m. Shareholders of UKT will also be offered a cash exit, but we think the merger makes good sense for all parties so we would be inclined to accept the rollover option.

Our sister newsletter *Warrants Alert* points out there has been a de-rating of the small market in investment trust subscription shares that has left many at bargain levels. One it highlighted is **Utilico Emerging Markets** subscription shares (UEMS, 28.75p), which are exercisable at 183p and run until 28th February 2018. With the ordinary shares at 216.75p that implies 33.75p of intrinsic value, yet the subscription shares, which offer high gearing of 7.5 times, trade 5p lower at a mid-price of 28.75p (dealing spread 27.5p-30p). The risk is high, of course, but for active speculators these may be of interest and subscription shares (unlike warrants) can be included in ISAs and SIPPs.

The next issue of Investment Trust Newsletter is published on Saturday 13th May.

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The FTSE 350 Equity Investment Instruments Index is up 34.33 points (+0.38%) to 9019.40 since the last newsletter.