Investment Trust Newsletter
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STOCKMARKET INTELLIGENCE

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With my best wishes for your investment trust holdings.

Andrew McHattie
Publisher

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Investment Trust Newsletter

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After the calm of the summer, we suddenly have plenty of action. A Brexit timetable from the government has caused sterling to fall further and the FTSE 100 Index to smash through the 7000 barrier; the private equity trust SVG Capital has received a takeover bid; Henderson Global Investors is to merge with Janus Capital to form a larger fund management group; and we have been busily catching up with lots of leading managers, giving us their first-hand views on markets and sectors. We'll press straight on.

Major Price Changes Over One Month

Livermore Investments Group	+31.44%
EPE Special Opportunities	+22.30%
US Traded Life Interests Fund	+19.40%
SVG Capital	+17.83%
UIL Limited	+17.68%
Pantheon International Participations	+13.49%
VinaCapital Vietnam Opportunity Fund	+12.42%
HgCapital Trust	+12.21%
Standard Life European Private Equity	+12.03%
Baillie Gifford Shin Nippon	+11.87%
Baker Steel Resources Trust	-12.70%
Infrastructure India	-7.84%
Tritax Big Box REIT	-6.35%
Doric Nimrod Air Three	-4.86%
Establishment Investment Trust	-3.96%

Major Price Changes Over One Year

Golden Prospect Precious Metals	+137.42%
UIL Limited	+87.08%
Lindsell Train Investment Trust	+79.39%
JPMorgan Brazil	+73.91%
EPE Special Opportunities	+71.89%
VinaLand	+64.58%
BlackRock World Mining Trust	+63.25%
VinaCapital Vietnam Opportunity Fund	+61.16%
Aberdeen Latin American Income	+60.67%
JPMorgan Russian Securities	+57.76%
Dolphin Capital Investors	-60.34%
Candover Investments	-50.91%
Better Capital PCC 2012	-45.31%
Menhaden Capital	-42.43%
Infrastructure India	-39.74%

£20m market capitalisation filter applied. Source: Morningstar.

We have been highlighting the big discounts to net asset value in the private equity sector for some time, so it was not a complete surprise to see an opportunistic offer for **SVG Capital** (SVI, 654.25p). In the second week of September the trust received an unsolicited cash offer of 650p per share from Harbourvest Structured Solutions III. The trust's board responded with a recommendation that shareholders reject the offer, saying that it was at a 16.5% discount to the value of the investment portfolio at 31st July 2016 and undervalued the shares. The board has subsequently announced that it proposes to wind down the company to maximise cash returns to shareholders. It has agreed in principle to sell half the portfolio to Pomona Capital and Pantheon Ventures for £379m against an asset value of £401m as at 31st

Warning. Investment Trusts may use or propose to use the borrowing of money to increase holdings of investments or invest in other securities with a similar strategy and as a result movements in the price of the securities may be more volatile than the movements in the price of underlying investments. Your investment may be subject to sudden and large falls in value and you may get back nothing at all. You should not buy equity securities with money you cannot afford to lose. You run an extra risk of losing money when you buy shares in certain smaller companies including 'penny shares'. There is a big difference between the buying price and the selling price of these shares. If you have to sell them immediately, you may get back much less than you paid for them. The price may change quickly, it may go down as well as up, and you may not get back the full amount invested. Changes in rates of exchange may have an adverse effect on the value or price of the investment in sterling terms. As with other investments, transactions in investment trust securities may also have tax consequences and on these you should consult your tax adviser. This warning notice draws your attention to some of the high risks associated with warrants and subscription shares. The risks attaching to instruments and transactions of this kind are usually different from, and can be much greater than, those attached to securities such as shares, loan stock and bonds, such transactions often having the characteristics of speculation as opposed to investment. Warrants may involve a high degree of 'gearing' or 'leverage'. This means that a small movement in the price of the underlying asset may have a disproportionately dramatic effect on your investment. A relatively small adverse movement in the price of the underlying asset can result in the loss of the whole of your original investment. Moreover, because of the limited life of warrants, they may expire worthless. A warrant is a right to subscribe for shares, debentures, loan stock or government securities, usually exercisable against the original issuer of the securities. Because of the high degree of gearing which they may involve, the prices of warrants can be volatile. Accordingly, you should not buy warrants with money you cannot afford to lose. In certain circumstances it may be difficult to sell or realise the investment. Because of the volatile nature of the investment, a fall in its value could result in your recovering nothing at all. We have taken all reasonable care to ensure that all statements of fact and opinion contained in this publication are fair and accurate in all material respects. Figures for net asset values and historical track records supplied by DigitalLook, Thomson Reuters Datastream, Morningstar, the AIC, JPMorgan Cazenove, or by the trusts themselves. Investors should seek appropriate professional advice if any points are unclear. This newsletter is intended to give general advice only, and the investments mentioned are not necessarily suitable for any individual. It is possible that the officers of the McHattie Group may have a beneficial holding in any of the shares or warrants mentioned in this newsletter. Andrew McHattie, the editor of this newsletter, is responsible for the preparation of the research recommendations contained within. Published by The McHattie Group, St Brandon's House, 29 Great George Street, Bristol, BS1 5QT. Tel: 01179 200 070. E-Mail: enquiries@mchattie.co.uk. Web Site: http://www.tipsheets.co.uk. All rights reserved. No part of this publication may be reproduced, stored in a retrieval system, or transmitted in any form by any means, electronic, mechanical, photographic, or otherwise without the prior permission of the copyright holder. ©2016. The McHattie Group offers restricted advice on certain types of investment only. Authorised and regulated by the Financial Conduct Authority.

July, a 7.8% discount. To return the cash it plans a £450m tender offer before the year end at 700p per share and a further £300m tender offer at NAV early in 2017, making further tender offers thereafter as investments are sold. Shareholders face a classic choice now between a bird in the hand at 650p, or two in the bush where the sale of half of the portfolio by SVG can achieve a better price, but there is risk over the value and timing of the other half. Our preference would probably be to ignore the offer and to back the company's plan, which we believe has a strong chance of achieving a better exit price during a reasonable timeframe (more so because SVG is a fund-of-funds investor rather than holding individual companies). We do think as well that this offer can act as a catalyst to close up the discounts elsewhere in the sector. That has already happened to a degree – hence the appearance of **Pantheon International Participations** (PIN, 1634p), **HgCapital Trust** (HGT, 1486p), and **Standard Life European Private Equity** (SEP, 274.5p) in the list of monthly risers above, but it could have further to go. To us, the ratings given to private equity trusts have looked anomalous against the rest of the sector, so it is about time these shares rose in value. You can still buy **Aberdeen Private Equity Fund** (APEF, 104.875p) on a discount of 25.8% or **Harbourvest Global Private Equity** (HVPE, 1066p) on a discount of 22.6%, which we consider GOOD VALUE.

WINTERFLOOD EDINBURGH CONFERENCE

The North American Income Trust plc (NAIT, 1086.5p)

In the small North American trust sector, Aberdeen's North American Income Trust (NAIT, 1086.5p) has been through a few changes. This was the old Edinburgh US Tracker trust until 2012, then in June 2015 there was a change of portfolio manager when Paul Atkinson decided to leave and was replaced by Fran Radano and Ralph Bassett. Working from Philadelphia, the managers are aiming to deliver a steadily growing income from a portfolio of high quality, cash-generating US companies.

Addressing the elephant in the room straight away, Fran spoke about the forthcoming US Presidential election and was sanguine about the outcome. He said that in reality, whoever wins will be constrained to a large degree by Congress, so he dismissed some of the more outrageous policy statements that have been made as electioneering bluster. He said there is a "pretty good backdrop" for US equities now, economically. Against that background he seemed comfortable with the trust's 13% gearing (really 10% after netting out some deposits required for option trades), which he described as "fairly structural." The gearing is not being used to time the market, but rather to boost the income account, which is central to how this trust works. Fran said they are looking for consistent dividend growth "alongside a total return philosophy overall." The dividends – both received and paid out – are clearly important. The trust has paid out dividends per share of 27p, 30p and 33p over the last three years, at the same time adding roughly 3p per share to reserves each year. These now amount to just over 16p per share, or a little over two quarterly payments.

The trust's portfolio comprises 40-45 equities, currently yielding around 3.1% compared to the 2% yield from the S&P 500 Index. The trust also has some corporate bonds and option positions where these make sense, but there is a clear focus here on high-yielding equities. Only one of the trust's holdings has a yield less than the market, and that is Molson Coors, the brewer whose strong share price performance accounts for that lower yield now. Some of the trust's largest holdings will be well known to many investors – names such as Wells Fargo, Dow Chemical, Pfizer, and Microsoft. It is fairly well known that some of these US blue-chips are commanding relatively high ratings now, which Fran acknowledged, but he said while valuations are high, they are well supported. Profits are growing, and "there's a decent backdrop from inflation and interest rates", he suggests. "Overall, we feel reasonably comfortable with valuations", he says, adding "US corporations are in a pretty healthy spot."

This strikes us as a decent trust that has outpaced its opposition, ranking top in its peer group over the last year. On a 9.2% discount the shares offer a yield of 3.1%, which is decent if you are seeking North American exposure. The preference for high-quality, high-yielding companies does give the portfolio a particular skew though, so we could also foresee periods of underperformance in the future. We feel slightly nervous about US equities, on these valuations and at this point in the monetary and political cycle.

Henderson European Focus Trust (HEFT, 1061.5p)

We last reported on HEFT manager John Bennett's views after he spoke at Winterflood's London conference in early 2014. Since then the shares have moved up from 902p to 1061.5p, a decent return that reflects the trust's standing as a solid performer. Now that the shares have moved from a rating close to NAV to a 9.9% discount, an update was very welcome.

John says his management approach blends sector themes with stock specifics, and some of his themes are much the same as before. He has favoured healthcare since 2010 and smart cars since 2013. Now though he is tilting the portfolio more towards value rather than growth, and he also feels it is necessary to be much more stock specific in markets that may not generally

be helpful. Earlier in the year he suggested that 2016 would likely be a 'down year' for European equities, and so it has proved so far. The Eurostoxx 50 Index is down by 8% in the year to date.

Looking at each of these four themes in turn, we'll start with healthcare, very much an issue in the news ahead of the US Presidential election, with Hillary Clinton making much political capital from her desire to cut high drug prices. John points out that prescription drugs are actually only 10% of US healthcare expenditure, dwarfed by hospital care. He admits that "price pressure is for real", but quickly adds "the headlines are a bit hysterical and have caused the sector to have a poor 2016, but I think it will come out of that. I think the sector has had its derating." On a PEG (P/E ratio to growth) basis, healthcare stocks look much more attractive than consumer staples now. In the portfolio, HEFT has exposure to Roche, Novartis, and Fresenius. Another long-term theme for HEFT is 'smart cars', where John is less interested in investing in car makers but in the parts manufacturers for things such as telematics, electronics, and sensors. He likes Autoliv, a Swedish company that specializes in automotive safety systems, and Continental, a German firm known for its tyres but actually a big player in innovative engine technology.

That distinction between value and growth multiples leads us on to John's third theme – that he has been shifting some assets towards more value stocks as "the air is getting thin" for some growth stocks that have risen sharply. He says "I'm quite mean: I don't like to pay up for growth." He reckons that European quality stocks are on a 30% premium to the wider market, saying "at these prices I'm just not sure." Quality stocks have performed very well in Europe especially, and they are now expensive relative to other stocks and to their own history. Moving away from quality, he has bought some banks at bombed-out prices, being careful to stress these are domestic retail banks, not global operators. He has also been looking for what he describes as 'self-help' businesses that are benefiting from cost-cutting and other measures.

In terms of what really distinguishes HEFT from other European trusts though, John pointed towards the mid cap area which he described as "very fertile." He says "this is the key differentiator of what we do" – the trust has 35% of assets in companies capitalised at less than EU5bn. It's an 'all cap' portfolio, and that has really added value, John says. This year has been tough though, and John is not particularly bullish on markets generally. He says that trying to extract value this year has been a battle, like 12 rounds in a boxing ring. He notes that European stockmarkets have actually been quietly correcting this year, although there is a money illusion for sterling investors because of the devaluation against the euro.

Even so, he did not want to give the impression of being negative. The trust remains 9% geared (it can go up to 20%) and John concluded by saying "I'm not that gloomy" because he does not think in one-year timeframes. Partly for that reason he topped up his personal stake in the trust when the discount hit 15% at one point in the summer. He genuinely seems to like the trust and its structure – he said that investment trusts are "wonderful to manage" and that this is the "single best structure" for collective investment. He said that HEFT is beating all of his open-ended funds.

It is difficult to construct too much of a case for buying from what John said, but equally we think holders could find his medium-term view and emphasis on finding alpha quite reassuring. We like his pragmatic approach to investment that we think is likely to pay off over the long-term.

SQN Asset Finance Income Fund (SQN, 113.75p)

We have actually heard Jeremiah Silkowski, the chief executive of the managers of this specialist trust, speak twice this year – once at the Numis Annual Investment Companies Conference in June, and again at this conference. We didn't provide a write-up last time because the trust seemed unlikely to appeal too much to a broad readership, but we have been nudged into action this time.

This US-managed trust was launched in July 2014 to provide regular income for investors from equipment leasing and asset finance operations, paying monthly dividends with a target yield on the assets of 7.25%. The high demand for income and for non-correlated assets, as we have seen in the infrastructure sector, has since allowed the trust to undertake two successful expansions, most recently raising £180m through an oversubscribed 'C' share offer last November. Those 'C' shares are about to merge with the ordinary shares, and the trust has said it is planning a further issue of new shares later this year, subject to demand. Jeremiah says he is hoping the trust will grow to more than £500m this time. As the ordinary shares are currently trading on a 11.5% premium to net asset value, we imagine the demand could again be substantial.

In the past we have mentioned trusts such as the **Doric Nimrod Air** trusts (DNA, DNA2, DNA3**)** that own and lease aircraft, and the troubled **Nimrod Sea Assets** (NSA, US$0.065) that does the same with marine vessels. This trust is a more diversified operator that buys and leases all kinds of business-essential equipment, within very carefully-specified boundaries. Jeremiah says it is a "very distinctive, but tried and true investment strategy." He also says "what we do is very predictable and very stable."

When you think of leasing you may well think of consumer items such as cars, or massive capital

items such as aircraft, but SQN generally operates somewhere in the middle, leasing equipment to companies and government organisations. While it does not lease aircraft, SQN does lease the ground support equipment at airports. Typically, leases may be over three to five years, or a bit longer. Jeremiah explained that leasing is attractive to corporations that are run on a divisional and a quarter-by-quarter basis, meaning it is simpler to budget for a leasing payment off the balance sheet than to tap a capital budget. SQN is most interested in providing assets that are business-essential and revenue producing (or cost saving), meaning there is less likely to be any problem with payments. It wants them to have a relatively long economic life, with an active secondary market for used equipment, which makes it easier if there are multiple industry applications. In practice this means it has a widely diversified portfolio of assets from modular buildings to wind turbines, from paper mills to plant hire. About half of the portfolio is in the UK, with the rest in the US, France, the Netherlands, and a very small amount of business in Brazil and Australia. All of the exposure is hedged back to sterling, so there is no currency risk, and no gearing either.

To give more of a flavour of the actual assets owned, Jeremiah ran through some in detail. His favourite example is Rolls Royce energy generation plants that run on natural gas and produce both energy and heat. One client is the UK's largest tomato farm on the Isle of Wight. The ten-year term here has a target yield of 9.4%. He also spoke about hotel internet access kit, anaerobic digestion plants, and about the IT infrastructure for the Swedish Nasdaq OMX stock exchange. He stressed "we are very selective about the assets we own. It's a robust market, we occupy a very important space that is generally underserved."

In some ways this feels like an esoteric, specialised trust, generating returns in a less familiar way, but actually the management seems to be founded on a great deal of common sense that aims for steady, unspectacular returns. The yield of 6.6% on the shares looks attractive, and if there is any dip in the rating when the new fund-raising is announced, we would consider taking advantage of any opportunity to buy in more cheaply. We prefer this trust to the more specialist asset finance trusts that appear to carry more specific risk.

Schroder UK Mid Cap Fund plc (SCP, 445.5p)

Since Rosemary Banyard retired from Schroders in March, this trust has been managed solely by the experienced Andy Brough, who points out that he is in his 111th quarter of fund management. This month the trust announced he is to be joined by Jean Roche as co-manager, refreshing the management team.

We had an update from Andy, who explained more about how he looks for earnings and dividend growth from the FTSE 250 Index. That is very much this trust's universe – it sells when a company is promoted to the FTSE 100. Apart from the greater sector concentration in the F100, Andy also highlighted a concern that the large cap index has diverged significantly from the earnings of the underlying companies, pressing on to 7000 in spite of falling earnings per share. This has not happened with the mid cap index.

Part of Andy's management process is to break down where inflation is in the system, to see which companies might have pricing power. This is a key attribute he looks for, along with strong business franchises, quality of management, strong balance sheets, and areas of secular growth. He tries to avoid areas of industry overcapacity that may be experiencing long-term decline. As favoured stocks, he gave the examples of Dechra Pharmaceuticals, the pet pharma business, and Redrow, the housebuilder, also naming TalkTalk as one to avoid. By sector, the trust is overweight in support services, software and healthcare, and underweight in consumer services and financials.

For us, the key message from Andy's presentation was that he is sticking with his proven process and trying to keep things simple in a complex world. This trust has a strong long-term performance record and seems to us to offer some value on a discount of 19.2%, as long as you are not too frightened by the shadow of Brexit over this domestically-focused sector.

Templeton Emerging Markets Investment Trust plc (TEM, 593.5p)

Following Dr Mark Mobius, one of the highest profile of all investment trust managers, Carlos Hardenberg had big shoes to fill when he took over as manager of TEMIT a year ago. He has definitely put his own stamp on the trust since that time though, and the performance has been superb so far under his stewardship. TEMIT is comfortably the best performer in the emerging markets sector over the last year with a net asset value return of almost 50%. Yet the shares are still available on a double-digit discount of 13.9%, wider than the sector average of 11.7%. We were glad to hear from Carlos himself, who ran through his current views.

Templeton reckon that emerging markets have outperformed developed markets in 17 of the last 28 years, and that has certainly been the case in 2016 to date as well. Carlos acknowledges that it is a high risk area though, and that although emerging markets have grown a lot, there will always be certain problems and issues. Over the last three to five years he says there was "kind of a perfect storm" for emerging markets, which were hit by concerns of a slowdown in China, a correction in commodity prices, and heightened

political trouble in countries such as South Africa, Brazil and Turkey. This toxic combination led to a period of underperformance, leading to what Carlos believes is still "a very good opportunity right now to look at these markets." Importantly, he notes, both the equity markets and currency markets have corrected. This last point is crucial – there is little point in making gains in local equity markets if those are immediately eroded by weak currencies.

Carlos believes that emerging markets have come out of this perfect storm now, with Brazil and Russia coming out of particularly deep holes. He points to exports stabilising after a long period of decline, to purchasing managers' indices improving, and to GDP growth indicating some degree of mean reversion and returning to more normal levels closer to 5.5% for 2017 and 2018. Against this background he views emerging markets as offering a "fairly unique value proposition" on a big discount to developed markets like the US and UK, close to their all-time highs. There are just a few signs that investors might be starting to agree with this view, as net flows into emerging markets have turned positive after some large underweight positions in 2013, 2014 and 2015.

On a number of different measures, emerging markets still look relatively cheap against developed markets. Their forward P/E ratio is 12.4 times, against 16.2 for developed markets; the price to book value is 1.5 against 2.2; whilst earnings per share growth is faster at 11.7% against 9.3%. and net margins are higher, at 9.9% against 8.5%.

One area where Carlos has made his mark is in raising the trust's technology exposure. He notes that China is the world's biggest internet user with about 21% of usage, and India has a share of 14% as well. Emerging markets now account for around 70% of global smartphone sales, compared to 39% in 2010. Consumers are "embracing technology much faster" now, Carlos says. Wechat, the Chinese equivalent of the instant messaging service WhatsApp, took only a year to reach 150m users (now about 700m), whereas the television took 38 years to reach that same adoption. Technology is becoming a more important component of the index – actually more for the MSCI Emerging Markets Index than for others – and that is why information technology is now the single largest sector in TEMIT's portfolio at 26.2%, up from 12.1% a year earlier. Financials and energy have been reduced.

After a bear market that took the MSCI Emerging Markets Index down by 35% in 17 months over 2015/16, Carlos expects this to be followed by a long recovery, as has generally been the case in the past. To position the trust for growth he has increased the number of portfolio holdings from 50 to 90, selectively increasing small and mid cap holdings and also some frontier market exposure. The percentage of assets in China/Hong Kong has come down from 26.6% to 18.4%, and Thailand has also been cut, whereas the trust has more money now in South Korea, Taiwan, and Russia. Carlos suggests the trust is "well positioned to benefit from a two to three year recovery in markets." The trust is not currently geared, but that question is apparently "on the agenda."

Carlos made an interesting point about increasing mid cap exposure, that this area does not become distorted by the cash flowing in and out of the large caps as a result of passive funds such as ETFs and other index trackers that have become more important. He said there are "big flows" when countries move in and out of specific indices.

We think holders must be hugely encouraged by the initial performance under Carlos's management. Of course he arrived at an opportune moment in the emerging markets cycle, but he has made more significant changes to the portfolio than you might have expected, and shifted it meaningfully towards technology stocks. On a double-digit discount, with what appears to be a very positive outlook, we rate the shares a BUY. It is better to arrive at a party late than not at all.

MORE FIRST-HAND VIEWS

Henderson International Income Trust (HINT, 145.625p)

We were pleased to catch up again with Ben Lofthouse, the manager of HINT, whom we have met a couple of times before. We have never really had a very strong opinion about the trust, which is a fairly middle-of-the-road international trust, but we certainly don't mean that in a disparaging way. The trust is "designed as an equity income diversification tool", in Ben's words, and we think it fulfils that role rather well.

The idea of the trust is that it will not overlap with things people already hold, so there's no HSBC or Royal Dutch Shell or BT Group in this portfolio, which is completely ex-UK. Ben chooses overseas stocks from a wide universe, but it is still difficult on occasions. He says that most of the recent equity returns from global markets have come from a re-rating of stocks rather than growing earnings, so the global equity price-earnings ratio has risen to historically high levels. Ben says that these high valuations "are the nub of equity fund managers' problems at the moment." Stockmarkets have rallied due to QE and cheap money, but they have forced the prospective P/E up to 16 times earnings.

Ben has reduced the gearing for HINT, which peaked at 16% at the time of Mario Draghi's famous speech. Now the trust has a small amount of net cash, but Ben says

"it is not as obvious what to buy now." He does see some pockets of value though – he mentioned GM on a P/E of 5.5 and Apple on a P/E of 10. He does not yet own Apple, but says he is closer to owning it than ever before. The trust has done well from Microsoft, and Ben says the technology sector has lots of cash and low multiples. More generally, he says there is a wide dispersion of valuations in the market. At one end of the spectrum people are paying up for quality, making those stocks expensive. Ben has been selling some of the trust's strong performers as a result. On the other hand, he says lots of Chinese stocks are cheap, and that in the value arena there is "a lot of cheap stuff, but it is very cyclical, so we don't really want that."

The answer for this trust is to reduce dividend risks and focus on value, prioritising cash flow and skewing towards areas with well supported dividends such as technology, healthcare and industrials, away from those with uncovered dividends such as utilities and energy. Buying higher yielding stocks is possible, but Ben says it "requires a leap of faith that cashflow will catch up", and that is not his style at all. HINT's portfolio yields 3.9% from stocks that are growing their dividends, such as ING, Panasonic, AXA, and Cisco Systems. Ben says the trust is "not having any problem with yield" and of course as an overseas investor without any sterling assets the trust has benefited quite significantly from the Brexit-associated currency shift that has boosted its dividend income in sterling.

Ben is not expecting global growth to take off any time soon, and clearly has reservations about the valuations being placed on many global equities at present. His management has been focused on securing dividend income, hunting for growth and stability, and trying not to overpay for yield. The trust is maintaining its value bias to maximize long-term total returns, which it has done well so far, ranking second out of ten trusts in its peer group (ahead of Murray International). To us, the shares are no bargain on a small discount to net assets of 1.3%, yielding 3.2%, but we like Ben Lofthouse as a solid manager in charge of what looks like a solid trust.

F&C UK Real Estate Investments Limited (FCRE, 97.5p)

Of course property funds hit the headlines after the Brexit vote in June, for the wrong reasons, as investors tried to pull out of open-ended funds that had to slam the door shut pretty quickly to prevent massive outflows they could not finance as holders of illiquid assets. Investment trust managers and investors may have had to fight a brief temptation to feel smug, but as discounts widened for UK property investment trusts as well, they also endured a sharp sell-off. Prices have recovered part of the way, but we are not sure they will move much higher from here. Peter Lowe, the manager of FCRE, gave us a realistic assessment.

The general case for property trusts, first of all, is that they are amongst the most readily understandable and long-established of the alternative asset trusts, along with private equity. They can provide non-correlated returns that are primarily composed of consistent, contractually-backed rental income. Peter says this "dependable income" is at the core of the returns, as capital growth has been subdued during this post financial crisis period, and UK property capital values remain some way below their 2007 peaks, with the exception of central London.

Peter says he "was quite looking forward to buying a couple of bits" in the wake of the Brexit sell-off, but actually found there were a limited number of sellers. He was unable to invest the trust's £14m of surplus cash at that point. There has been no panic. Capital values did fall in July and August though, across all sub-sectors, meaning that trusts on discounts now – 3.3% for this trust – may represent "fair value", Peter reckons. Forecasters are generally expecting modest total returns going forward for the market as a whole, but at this point in the cycle Peter's strategic view is that it makes most sense to focus on income.

The trust pays a quarterly dividend of 1.25p per share, equating to a 5.2% yield on the current share price. That dividend is not quite covered, although it is forecast to be covered this year. In our guide to alternative assets trusts published last year we reckoned property yields tended to be between 4% and 6%, so this is roughly where we might expect to find it. The sector average yield is 4.9%. At present, most of the trust's returns are coming from its income. In the year to 30th June, total returns from the portfolio were 7.1%, driven by an income return of 5.6%.

Part of the trust's yield advantage comes from its underweight positioning in London, where rental yields are lower (due to the high capital values), but this is a well diversified portfolio across different types of properties in different areas. It does have nearly half of its assets in the south-east though, so that's one concentration. Pater says that in this market, where income is weakening and the capital growth cycle is coming to and end, looking for a yield premium is key. Getting the income in is the priority, rather than using "tactical voids" to look for income growth through refurbishments, which is why the trust's portfolio has a very low void rate of 4%.

This trust – formed in 2013 by the merger of the old ISIS Property Trust and IRP Property Investments – sits mainly in the middle of the pack for the generalist UK direct property trusts. It does have a yield advantage that may become more important as the property market weakens, but we don't think the case for buying is very strong at this point in the cycle. We might, if anything, be looking to reduce UK property exposure.

Polar Capital Technology Trust plc (PCT, 802p)

When picking five stocks for a long-term growth portfolio in August of last year, Polar Capital Technology was one of our selections. It was fairly obvious that we might want some technology exposure, but we also noted that PCT was neck-and-neck in performance terms with Allianz Technology Trust (ATT, 767p) at that time. Over the last year though, the Polar trust has proved the better call, which manager Ben Rogoff assigns to more aggressive positioning during what has been a good spell for the sector (and even better for sterling investors). PCT shares are up by 35% since that time.

We met Ben a couple of weeks ago, when he was just back from a visit to the US. He said the tone there was very positive and that the companies he saw did not complain of any macroeconomic problems. It's business as usual, which for Ben means "looking for themes, trying to avoid rubbish, that's what leads to good performance." Much of what he does involves understanding product cycles and where companies are on the curve of innovation. Sometimes this means being quite patient, as is the case for example with Tesla, the electric car maker that is arguably at the very early point in its development. Ben says he has had two tours of the Tesla factory in the last three months, but owns only a "tiny bit" at present. Importantly, Ben also tries to avoid last generation winners – it has been a recurring theme in Ben's talks over the years that he is wary of large incumbents and highly conscious that established markets can be destroyed quickly by disruptive new innovation. Ben says that technology companies are like empires, "either rising or falling."

The trust's portfolio is diversified, with around 120 holdings, necessary because in this sector "there are lots of upsets", Ben says. He is bullish at present though, saying that in the absence of much global growth, this sector is delivering – indeed he says that recent earnings growth means "the promise of the late 1990s is finally being delivered" as shares revisit their boom-time highs, but this time with the earnings to back those valuations. He says he doubled his personal holding in the trust recently when it hit a new all-time high.

Ben ran through several slides showing the colossal growth of data, of smartphone adoption, and the falling cost of bandwidth. He argues the shift to ubiquitous computing together with the mass production of IT in the cloud means "the risk of trying new things has collapsed" and could usher in a wonderful new period of innovation. Smartphone usage is not all about watching cute videos of cats playing pianos – not for everybody, anyway. Ben says that as a society we are asking more questions than ever before, with huge numbers of Google searches, empowering individuals like never before. Behaviour is changing as a result, with adoption rates accelerating rapidly and the largest technology companies becoming natural monopolies in some instances. Ben points out that in 2001 the five largest publicly traded companies in the world were GE, Microsoft, Exxon, Citi, and Walmart, so one technology company. Now all five of the top spots are technology, namely Apple, Alphabet (that's Google), Microsoft, Amazon, and Facebook. That's a handy reminder that we probably should have some technology in our portfolios and that we might prefer to achieve that through a London Stock Exchange listed trust rather than buying US stocks directly.

Returning to one of his favourite themes, the diminished value of incumbency, Ben says this can lead to greater M&A activity as older companies scramble to redefine themselves and to catch up with newer products and services. He says the trust has had seven or eight holdings bought this year – the most ever – and that this could be the start of something. Ben does not go hunting specifically for M&A targets though, rather that happens by being in attractive companies in the right sectors. Ben sees opportunities in areas such as software-as-a-service, cyber security, internet advertising, eCommerce, payments, and videogames.

Valuations look reasonable too. The technology sector is nowhere near bubble territory – Ben says absolute sector valuations are compelling against their history and about the same as the wider market in relative terms, but with superior balance sheets. In terms of stock selection, Ben says he is "looking for more than benchmark growth, without paying too much." When asked about Apple, which forms around 11% of the trust's benchmark index but accounts for around 6% of assets, Ben said the iPhone 7 was "very disappointing" but that US mobile carriers were giving away very generous upgrades, good news for Apple.

This was a very upbeat presentation – as it always is from Ben – but we think there was plenty to be encouraged about in terms of technology company profitability and stocks on reasonable ratings. It is worth remembering that two-thirds of the portfolio is in the US and only 2% in the UK, so the trust has been a net beneficiary of Brexit risk so far, with the fall in sterling providing a bonus. We consider this trust a core long-term growth holding, especially suitable for younger investors who can afford to ride out future dips – we think the fund manager has real insight into a complex industry and feel content to reiterate our LONG-TERM BUY recommendation.

Henderson Global Investors, the fifth largest manager in the industry, is merging with the US firm Janus Capital. We can't see that this has any implications for the firm's investment trust business though, except perhaps to make more expertise available in the US and Japan.

STOCKBROKERS' RESEARCH

We only have space for a very brief summary this month. JPMorgan Cazenove has downgraded **Witan Pacific Investment Trust*** (WPC, 290.75p) from overweight to neutral, saying "performance has not been sufficient to justify an overweight recommendation" and the differential of the discount between peers in the ex-Japan sector has narrowed. In a review of the Japanese sector, Winterflood says "our recommendation in the Japan sector is **JPMorgan Japanese** (JFJ, 342.875p), which we believe offers value at its current discount of 15%. This fund has seen a significant improvement in its performance over recent years and benefits from an experienced and well-resourced management team." Canaccord Genuity, the trust's broker, also rates it a buy. Stifel rates **Target Healthcare REIT*** (THRL, 111p) a buy, saying the prospective yield of 5.7% is attractive, whilst Numis highlights **TwentyFour Select Monthly Income Fund*** (SMIF, 92p) as an "opportunity to buy 7% yield at a discount to NAV." Cantor Fitzgerald issued a note on **Aberdeen New Dawn*** (ABD, 191p) on 21st September, saying that while the trust has underperformed in recent years "this is not surprising, as markets have been driven mainly by sentiment and monetary interventions, while the Aberdeen investment style is strictly long-term, fundamentals-driven and quality-focused. The bigger picture is however more compelling. The trust has outperformed greatly over the last two bull markets and absolute returns have been strong (+13.1% pa over 15 years and +10.1% pa over 10 years), while also providing the added comfort of the quality portfolio and very low risk of a drift in style." On 5th October Panmure Gordon downgraded **Pantheon International Participations** (PIN, 1634p) to 'hold, saying this reflected "solid rather than stellar return expectations" and the strong recent share price performance.

** asterisks in this section indicate that the trust is a client of the stockbroking firm providing the research*

NEWS ROUND-UP

Asian Total Return Investment Company has changed its name to **Schroder Asian Total Return Investment Company** (ATR, 262.5p). **BlackRock Greater Europe** (BRGE, 281.5p) has announced a tender offer for up to 20% of its shares as part of its discount control policy. Shareholders should receive a circular in early November about the offer at 98% of NAV. In view of the 9.1% discount to NAV in the market, we think holders should TAKE UP the offer to the maximum extent. **BlackRock Income Strategies** (BIST, 112p) has announced a strategic review and is inviting fund management groups (including BlackRock) with experience of closed-end funds and "established multi-asset management credentials" to present proposals to the board. We can expect a further announcement later this year. The trust has been a poor performer, ranking bottom of the Flexible Investment peer group over one and three years, so shareholders might welcome a change of emphasis or manager. As we indicated was likely in our write-up in June, **Harbourvest Global Private Equity** (HVPE, 1066p) has applied to delist from Euronext Amsterdam, which makes sense to clean up the structure and cut costs. This should be finalised this month, leaving the shares traded exclusively in London. The demand for infrastructure investment continues unabated. Both **HICL Infrastructure** (HICL, 173.55p) and **The Renewables Infrastructure Group** (TRIG, 107.85p) found their additional share offerings were materially oversubscribed, so HICL raised £113.4m instead of the £76m it was seeking and TRIG raised £62.6m instead of £25m. **International Biotechnology Trust** (IBT, 557.75p) is to seek shareholder permission to introduce an annual dividend, equivalent to 4% of the trust's NAV, payable through two equal distributions each year, which it is expected will be paid out of capital reserves. The trust may argue this is what shareholders want, and that it may help to sustain a higher rating, but we dislike this sort of artificial dividend that bears no relation at all to the companies in which the trust is investing. To us, it smacks of financial engineering, and we find it off-putting. Mark Barnett is relinquishing some of his investment trust management duties, passing the baton for the UK equity portfolio of **Invesco Perpetual Select** (IVPU, 173p) to James Goldstone. The board of **Schroder UK Growth** (SDU, 163.75p) has decided to abandon its 'hard' discount control target of 5%, adopting instead a more nuanced and soft policy. The discount is much wider now at 14.3%, which we think represents GOOD VALUE for big-stock exposure, if that is what you want. The trust's largest holdings are Royal Dutch Shell, GlaxoSmithKline, AstraZeneca, BP, and Lloyds Banking Group. **Tritax Big Box REIT** (BBOX, 136.35p) is raising more cash, looking for £150m from an offer of new shares priced at 132p, between the current share price and the net asset value. We quite like the trust's specialist field, large logistics facilities in the UK, but this pricing does not attract us hugely.

The next issue of Investment Trust Newsletter is published on Saturday 12th November.

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The FTSE 350 Equity Investment Instruments Index is up 209.60 points (+2.57%) to 8355.64 since the last newsletter.