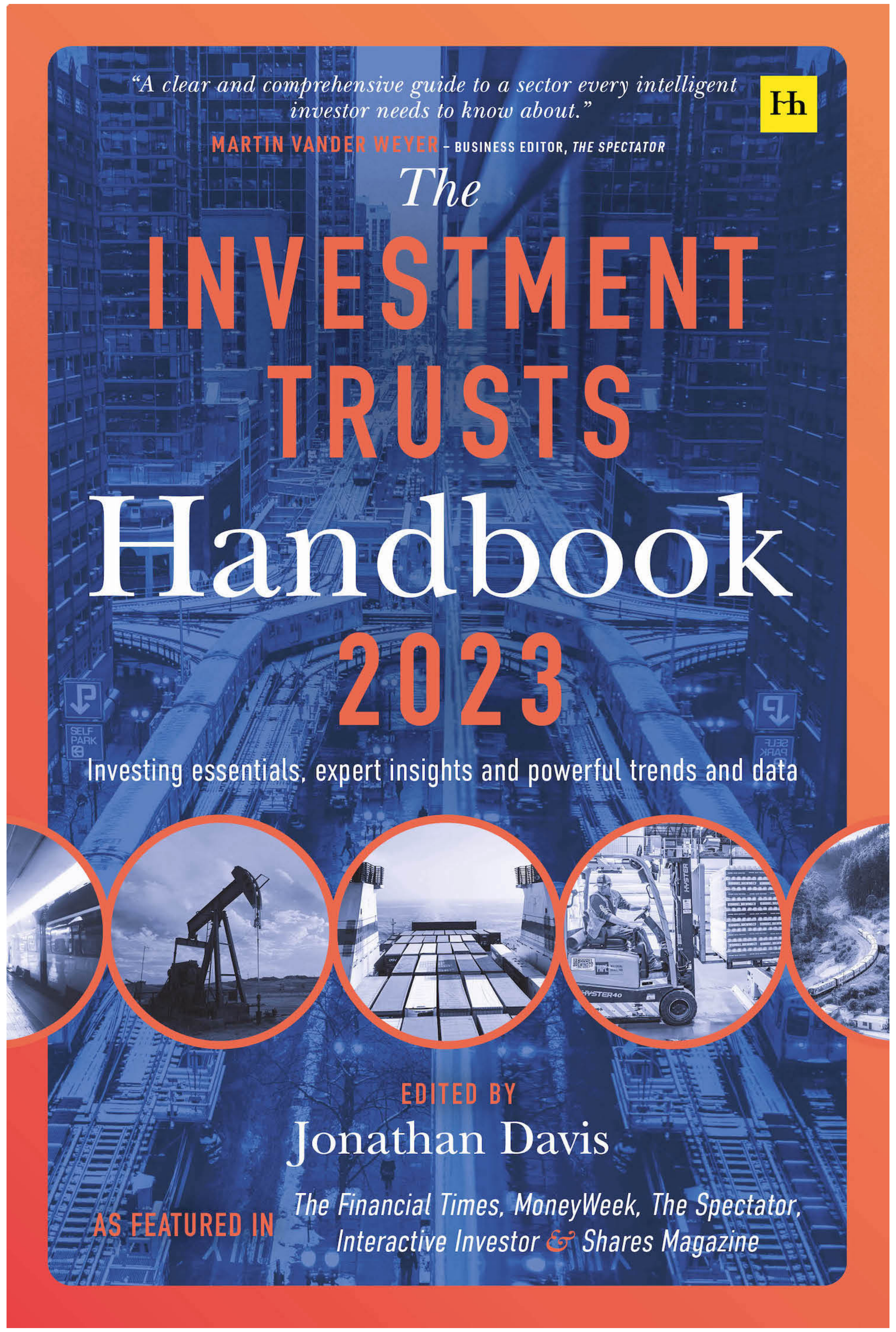
# Investment trusts: stick or twist?

## Facing the discount challenge

*Jonathan Davis*

Editor, *the Investment Trusts Handbook*

*April 15th 2023*



# The Money Makers podcast: all about investment trusts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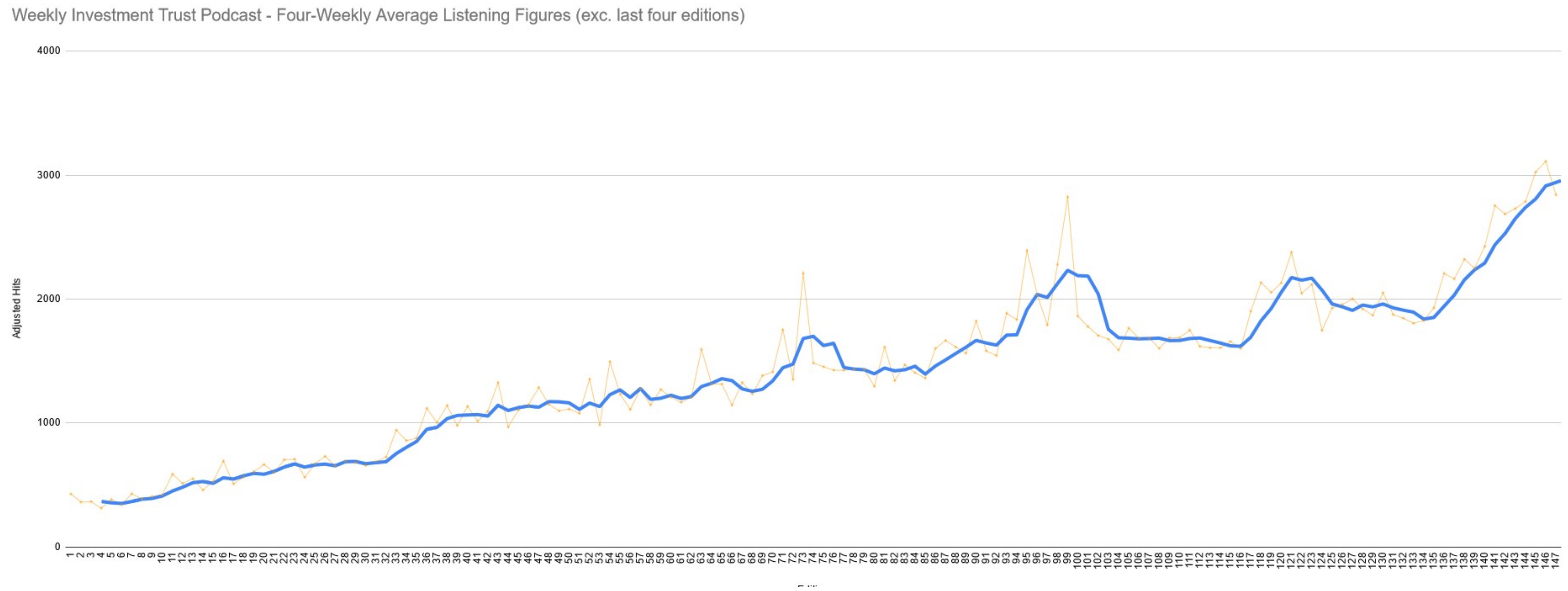


- Launched in March 2020
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- FREE on multiple channels
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- 60 mins of trust news + chat

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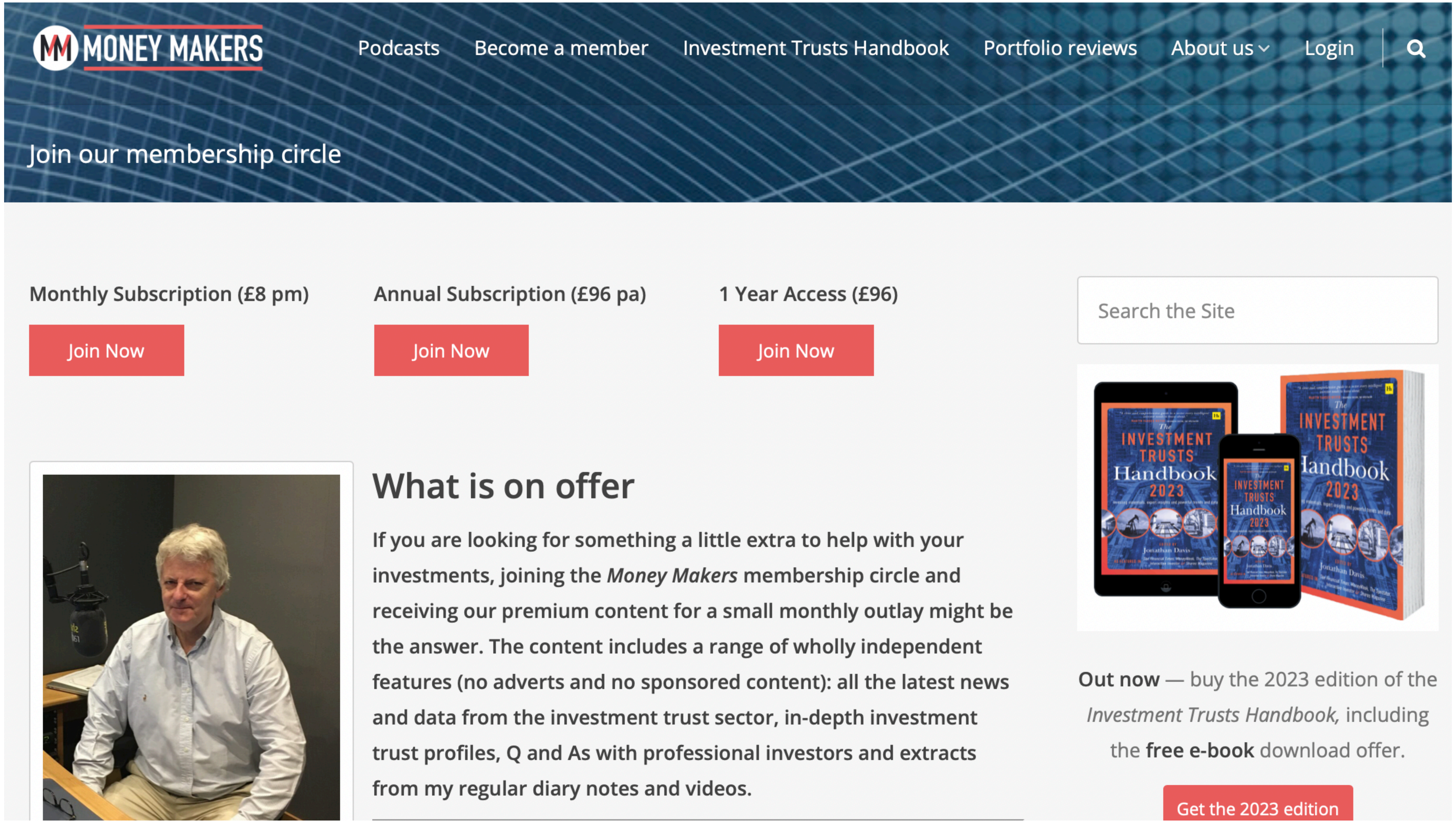



## Subscriber content

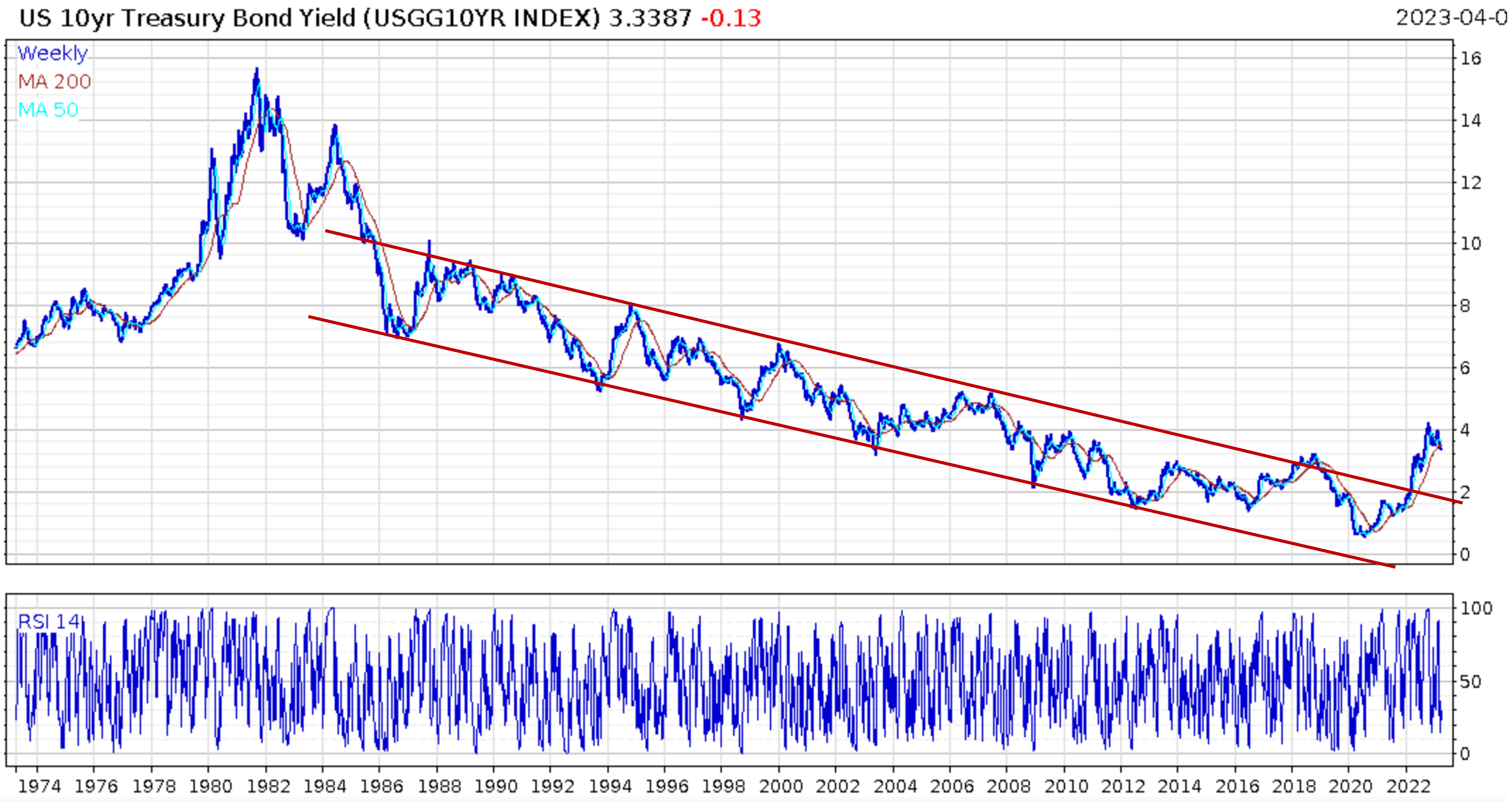
- Launched in Jan 2021
- In-depth trust profiles
- Trust news (with links)
- NAV, share price and discount movements
- Model portfolios
- Independent editorial
- Editor's thoughts

*Website: www.money-makers.co*

# The single most important question (March 2022)?


Q. Is this a prelude to an enduring change in the investment climate?

# The single most important answer (April 2023)?




**A: Yes, this does appear to be a game changer in the investment climate**

# What has changed?

- For the first time in years there is income potential in bonds, money markets and cash
- Higher bond yields also drive down valuations of long duration assets
- Alternatives such as property, private equity, ventures also face higher debt costs
- In the short term though inflation and recession are the critical variables
- Fiscal and monetary policy are pushing in opposite directions
- The challenge for central banks - 2% inflation target versus stability worries
- So-called “soft landing” is possible in theory, quite rare in practice

**Nobody knows for sure which way this two-way pull is going to settle short term….**

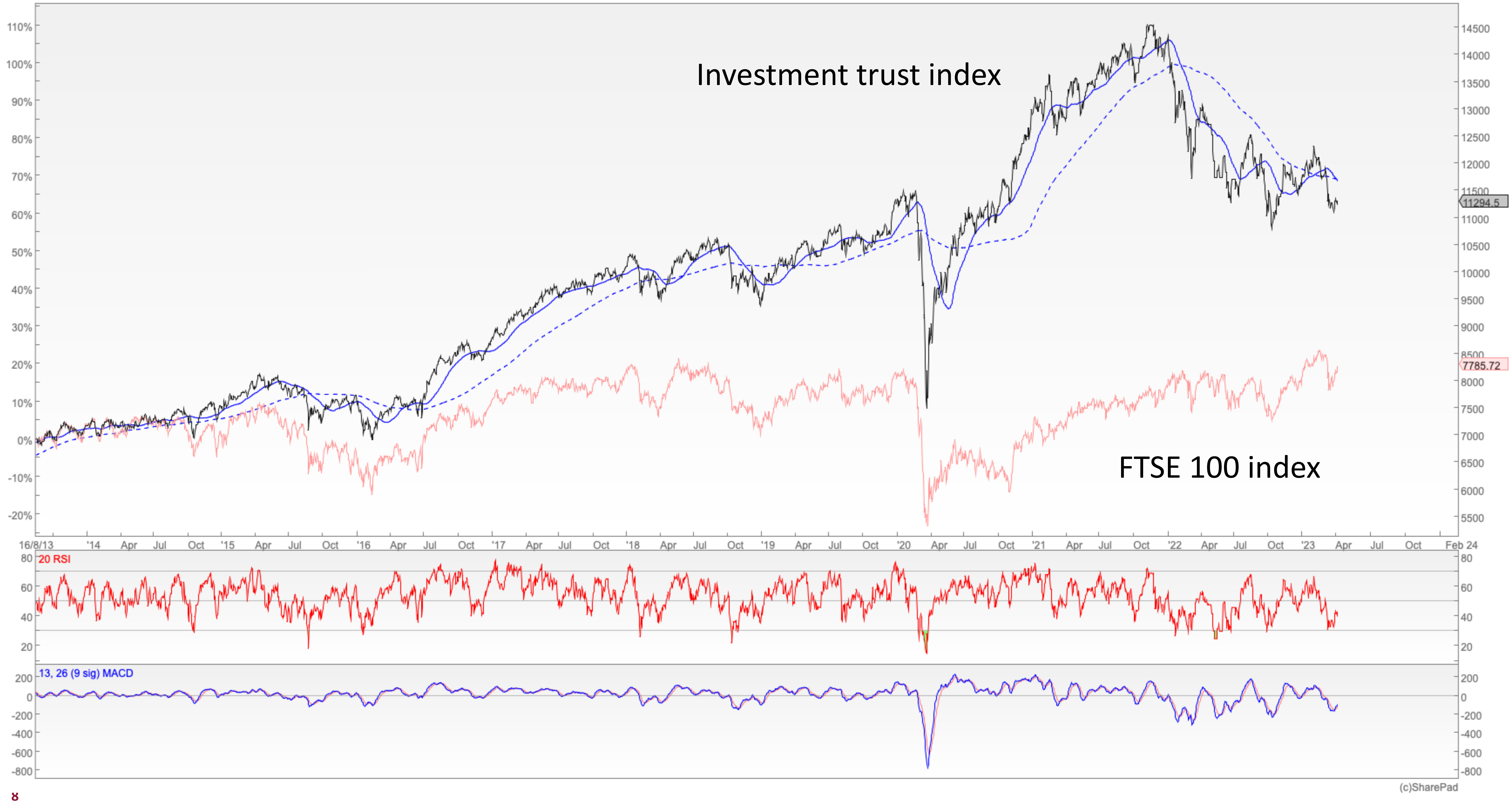
**But longer term unlikely that what worked until now will work as well from here**

# Investment trust impact

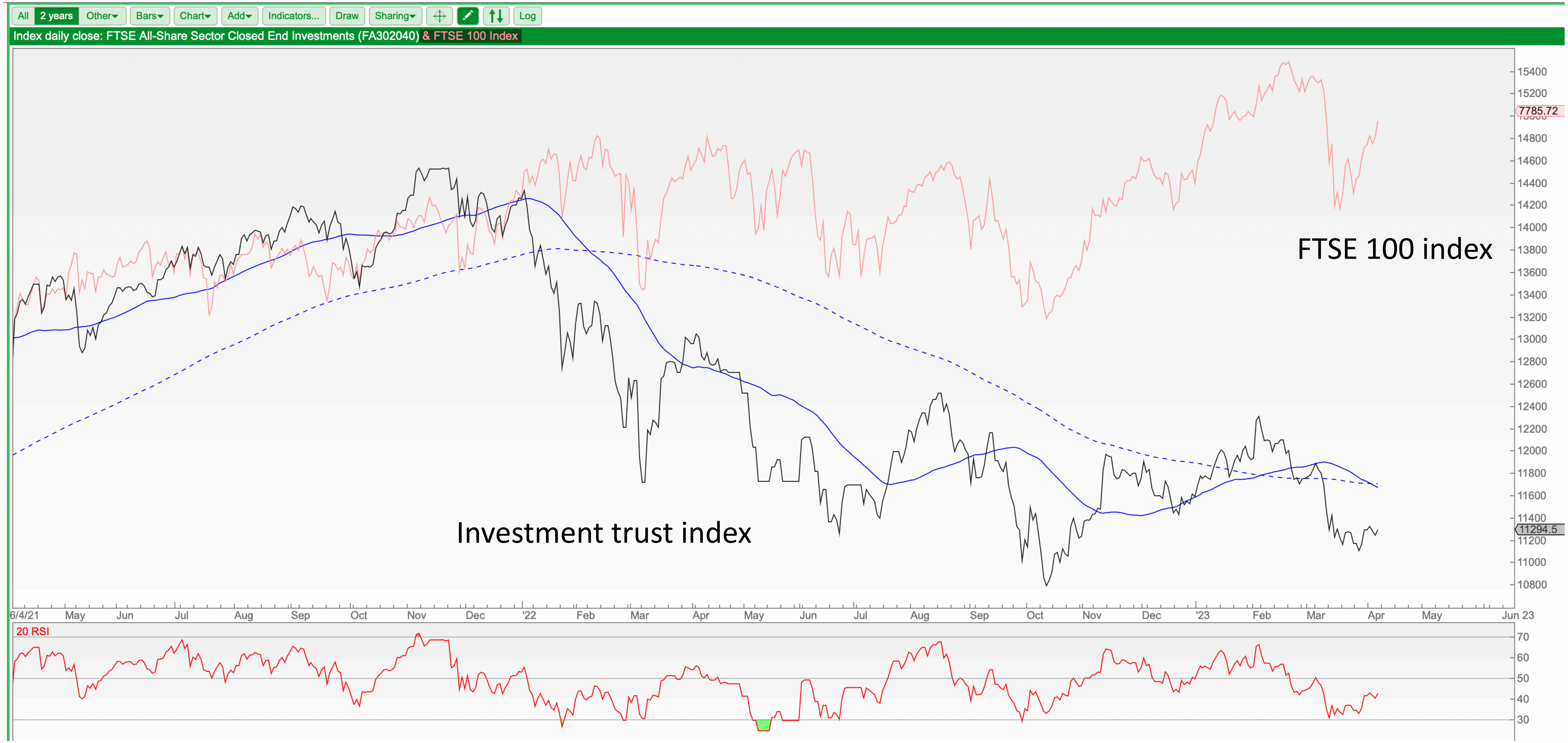
- 2022 brought to an end decade of strong relative + absolute performance
- Macro/market cycles drive discounts in both directions
- Short term prepare for more volatility until inflation/growth outlook clarifies
- Discounts also create opportunities - but not all discounts are bargains
- NAVs may be out of date - so look at discounts to what?
- Majority of alternatives have yet to be tested by a real bear market
- Trusts not totally immune from the bezzle or poor governance (HOME REIT)
- Liquidity is a growing issue for a number of smaller trusts
- We will see more mergers, wind downs, consolidation

**But be patient: investment trusts have survived much worse than this**

# Strong performance over ten years

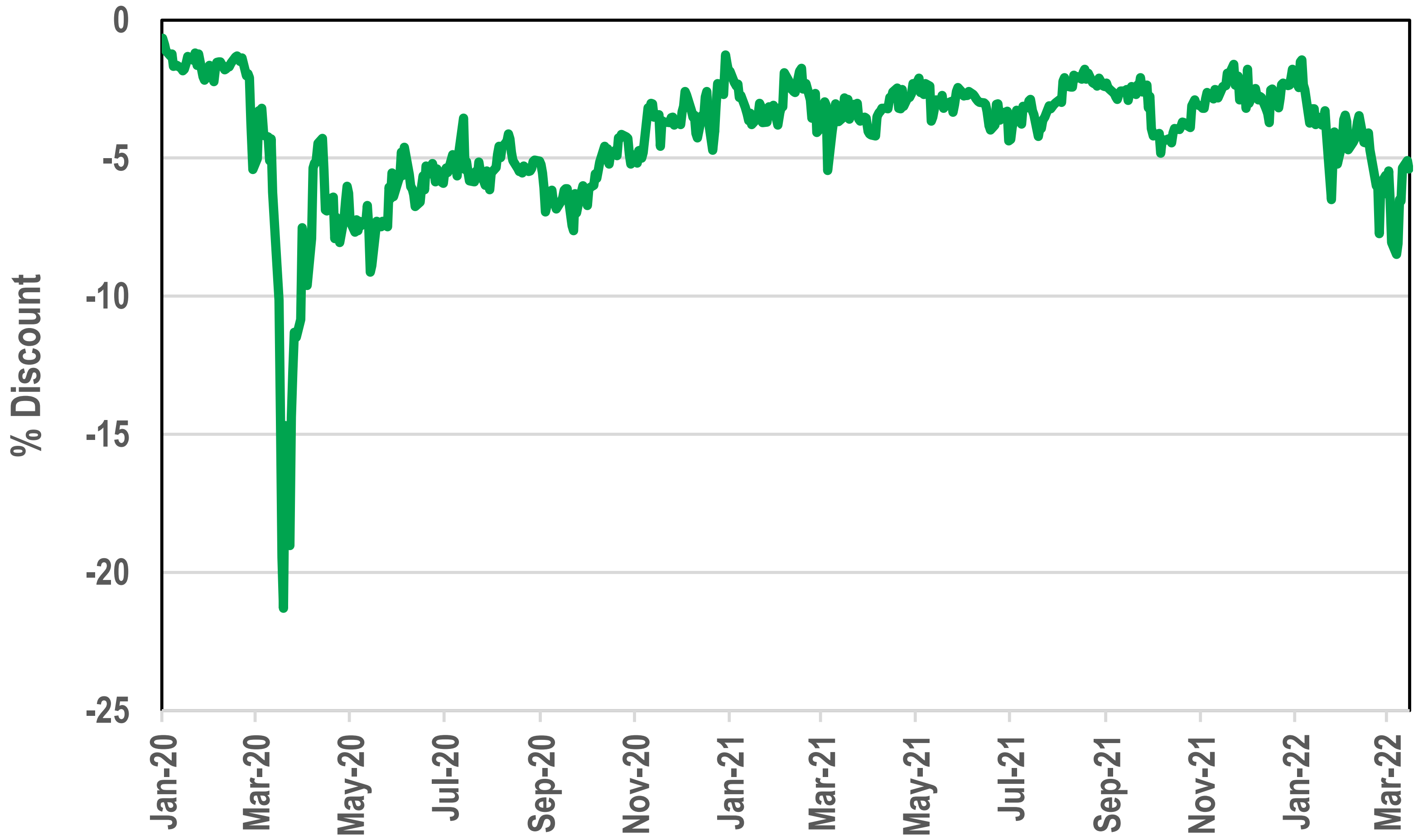


# Weak performance over two years

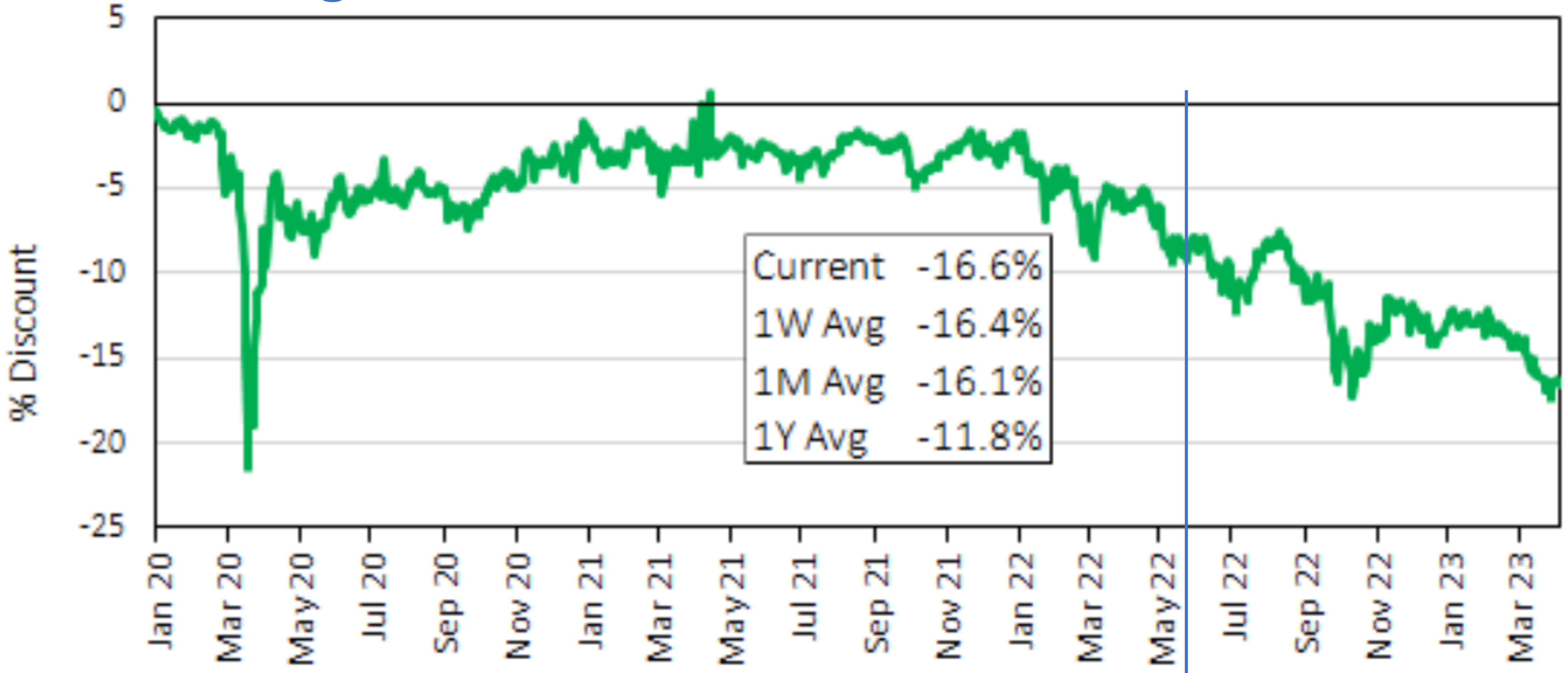


# Investment trust discounts have taken the strain

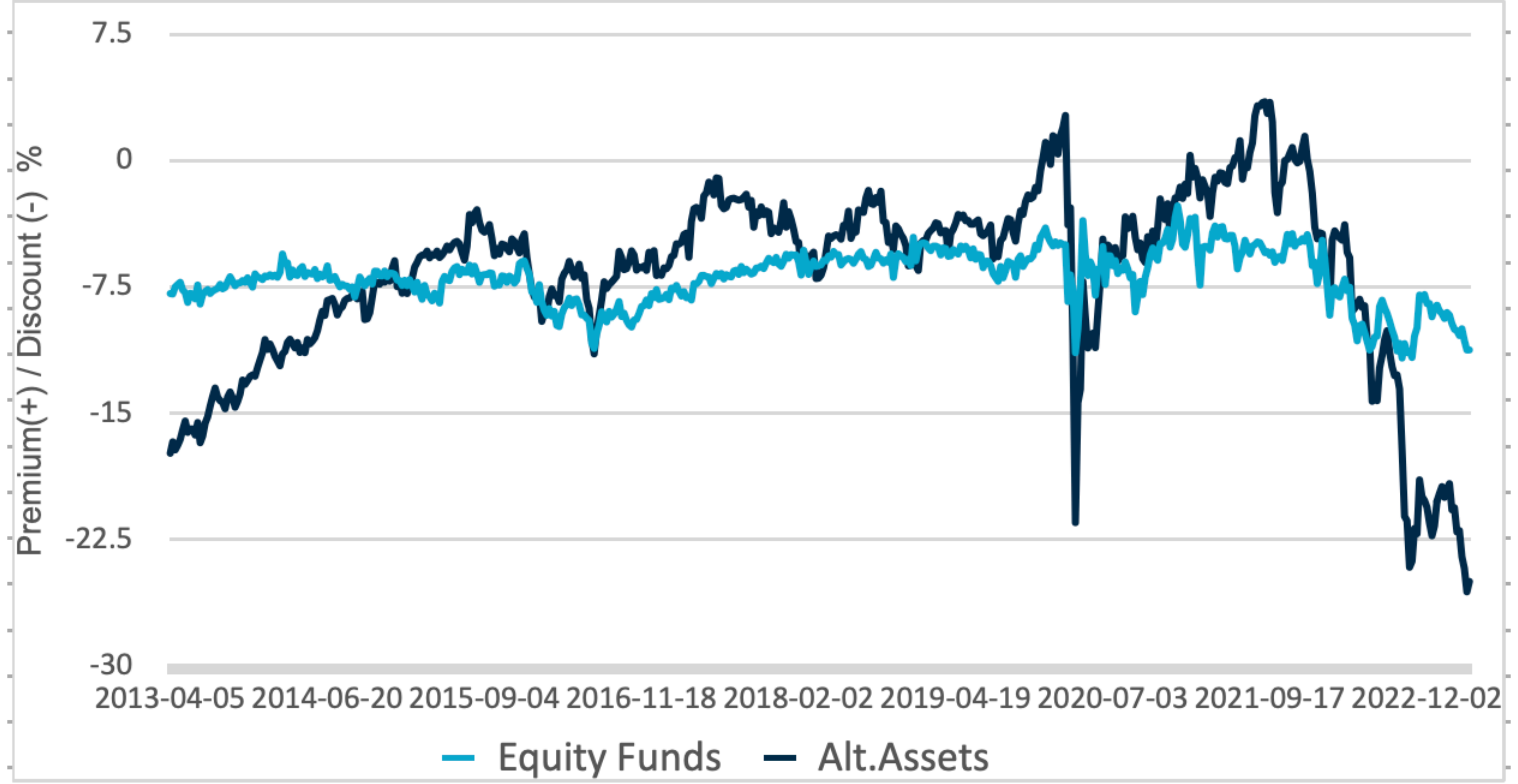
## Average discount last year




## Average discount now




| Share prices | YTD | Since 2/22 | 5 years |
|---|---|---|---|
| *Risers* | 141 | 60 | 161 |
| *Fallers* | 235 | 323 | 166 |
| | | | |
| **NAV Total Return** | | | |
| *Positive* | 178 | 104 | 250 |
| *Negative* | 205 | 280 | 77 |
| | | | |
| **Source** | Sharepad | 390 trusts | >£50m Market cap |




Equity trusts

Alternatives trusts

# Since April 2022: winners and losers

## Share Price

### Top 15

| Fund | Ticker | Now | Previous | Change |
|---|---|---|---|---|
| DP Aircraft | DPA | 0.05 | 0.02 | **122.2%** |
| JZ Capital Partners | JZCP | 165.00 | 100.00 | **65.0%** |
| Trian Investors 1 | TI1 | 184.50 | 126.50 | **45.8%** |
| Amedeo Air Four Plus | AA4 | 43.20 | 30.40 | **42.1%** |
| Doric Nimrod Air Two | DNA2 | 101.50 | 72.50 | **40.0%** |
| Literacy Capital | BOOK | 402.00 | 295.00 | **36.3%** |
| Rockwood Strategic | RKW | 1820.00 | 1420.00 | **28.2%** |
| Georgia Capital | CGEO | 785.00 | 650.00 | **20.8%** |
| Doric Nimrod Air Three | DNA3 | 50.50 | 42.00 | **20.2%** |
| 3i Group | III | 1685.00 | 1402.50 | **20.1%** |
| SME Credit Realisation | SCRF | 104.50 | 90.00 | **16.1%** |
| India Capital Growth | IGC | 121.00 | 106.50 | **13.6%** |
| Nippon Active Value | NAVF | 138.00 | 121.50 | **13.6%** |
| Sherborne Investors (Guernsey) C | SIGC | 52.50 | 46.60 | **12.7%** |
| Tetragon Financial | TFG | 10.35 | 9.20 | **12.5%** |

### Bottom 15

| Fund | Ticker | Now | Previous | Change |
|---|---|---|---|---|
| Global Resources | GRIT | 1.63 | 11.25 | **-85.6%** |
| Jade Road Investments | JADE | 1.25 | 7.75 | **-83.9%** |
| Home REIT - SUSPENDED | HOME | 38.05 | 126.00 | **-69.8%** |
| Schiehallion Fund C | MNTC | 0.40 | 1.29 | **-69.0%** |
| Chrysalis Investments | CHRY | 58.70 | 177.00 | **-66.8%** |
| Molten Ventures | GROW | 273.60 | 800.00 | **-65.8%** |
| Seraphim Space | SSIT | 37.55 | 103.80 | **-63.8%** |
| Schiehallion Fund | MNTN | 0.68 | 1.84 | **-63.0%** |
| Seed Innovations | SEED | 1.93 | 4.75 | **-59.5%** |
| Triple Point Social Housing REIT | SOHO | 42.70 | 95.50 | **-55.3%** |
| HydrogenOne Capital Growth | HGEN | 47.23 | 103.60 | **-54.4%** |
| Phoenix Spree Deutschland | PSDL | 185.50 | 376.00 | **-50.7%** |
| Schroder UK Public Private | SUPP | 12.62 | 24.10 | **-47.6%** |
| Digital 9 Infrastructure | DGI9 | 61.10 | 111.60 | **-45.3%** |
| Baillie Gifford US Growth | USA | 142.00 | 251.50 | **-43.5%** |

## NAV

### Top 15

| Fund | Ticker | Now | Previous | Change |
|---|---|---|---|---|
| Amedeo Air Four Plus | AA4 | 117.66 | 74.05 | **58.9%** |
| Georgia Capital | CGEO | 2090.00 | 1445.05 | **44.6%** |
| Gresham House Energy Storage | GRID | 160.66 | 112.02 | **43.4%** |
| Literacy Capital | BOOK | 345.70 | 245.30 | **40.9%** |
| 3i Group | III | 1639.77 | 1237.27 | **32.5%** |
| Taylor Maritime Investments £ | TMIP | 138.21 | 106.12 | **30.2%** |
| Trian Investors 1 | TI1 | 215.65 | 171.36 | **25.8%** |
| Harmony Energy Income | HEIT | 125.59 | 100.05 | **25.5%** |
| Petershill Partners | PHLL | 357.00 | 286.00 | **24.8%** |
| Oakley Capital Investments | OCI | 659.61 | 530.08 | **24.4%** |
| Greencoat UK Wind | UKW | 171.24 | 138.65 | **23.5%** |
| JLEN Environmental Assets | JLEN | 125.63 | 102.68 | **22.3%** |
| SME Credit Realisation | SCRF | 117.24 | 96.29 | **21.8%** |
| Rockwood Strategic | RKW | 1903.01 | 1599.70 | **19.0%** |
| Nippon Active Value | NAVF | 151.03 | 127.64 | **18.3%** |

### Bottom 15

| Fund | Ticker | Now | Previous | Change |
|---|---|---|---|---|
| Chrysalis Investments | CHRY | 127.13 | 229.08 | **-44.5%** |
| TR Property | TRY | 301.64 | 493.09 | **-38.8%** |
| Golden Prospect Precious Metals | GPM | 37.96 | 61.07 | **-37.8%** |
| ICG Longbow Senior Secured UK Pro | LBOW | 61.32 | 92.76 | **-33.9%** |
| Vietnam Enterprise Investments | VEIL | 669.33 | 962.21 | **-30.4%** |
| Miton UK Microcap | MINI | 62.35 | 89.22 | **-30.1%** |
| Warehouse REIT | WHR | 108.79 | 152.48 | **-28.7%** |
| Seed Innovations | SEED | 7.84 | 10.98 | **-28.6%** |
| Geiger Counter | GCL | 41.41 | 57.98 | **-28.6%** |
| Schroder UK Public Private | SUPP | 28.26 | 39.52 | **-28.5%** |
| Baillie Gifford US Growth | USA | 184.63 | 255.97 | **-27.9%** |
| River & Mercantile UK Micro Cap | RMMC | 180.27 | 249.36 | **-27.7%** |
| abrdn UK Smaller Companies Growth | AUSC | 494.71 | 681.02 | **-27.4%** |
| Crystal Amber | CRS | 115.80 | 159.11 | **-27.2%** |
| Edinburgh Worldwide | EWI | 190.97 | 259.21 | **-26.3%** |

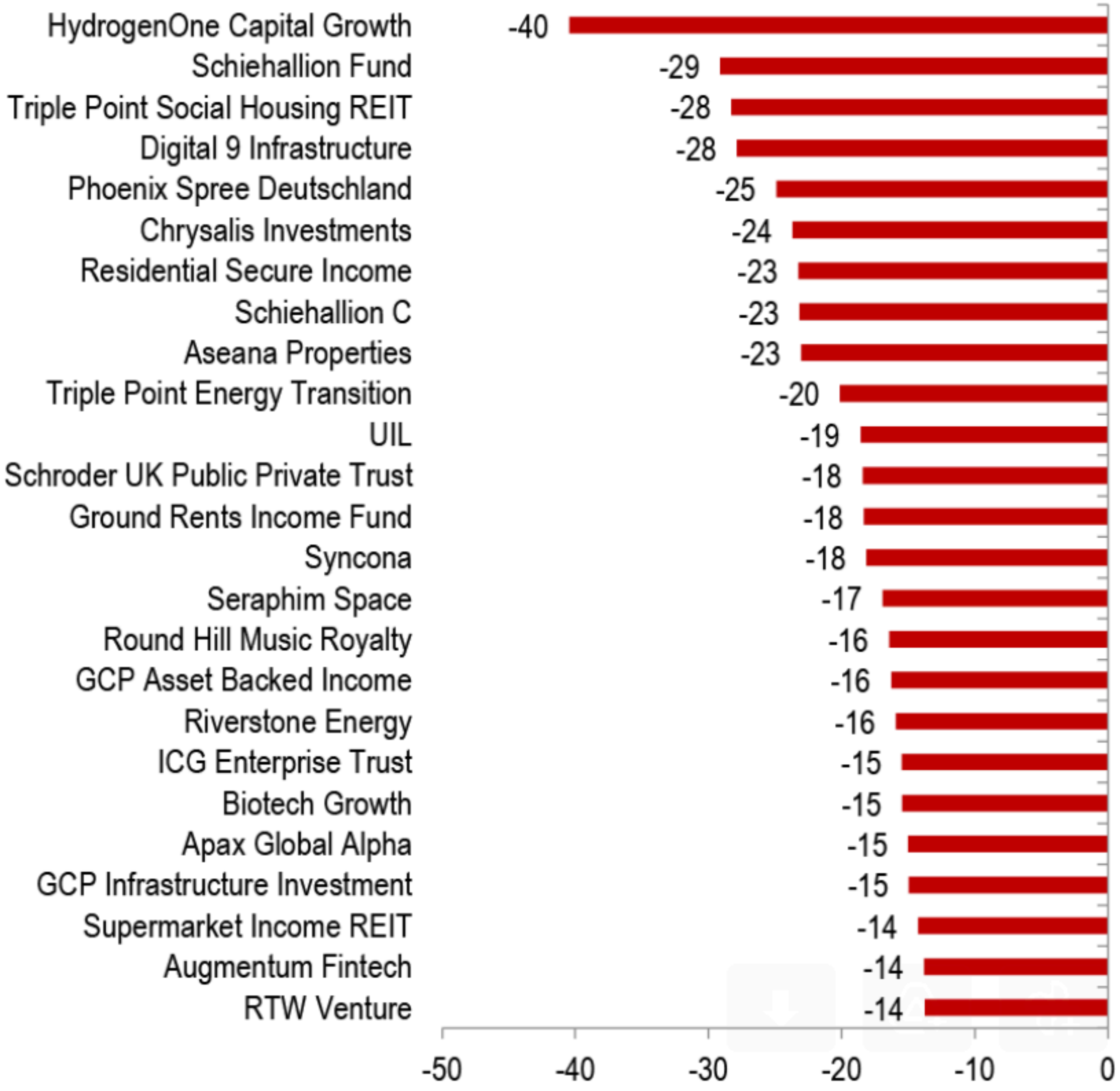
*Source: Numis Securities*

## Discount

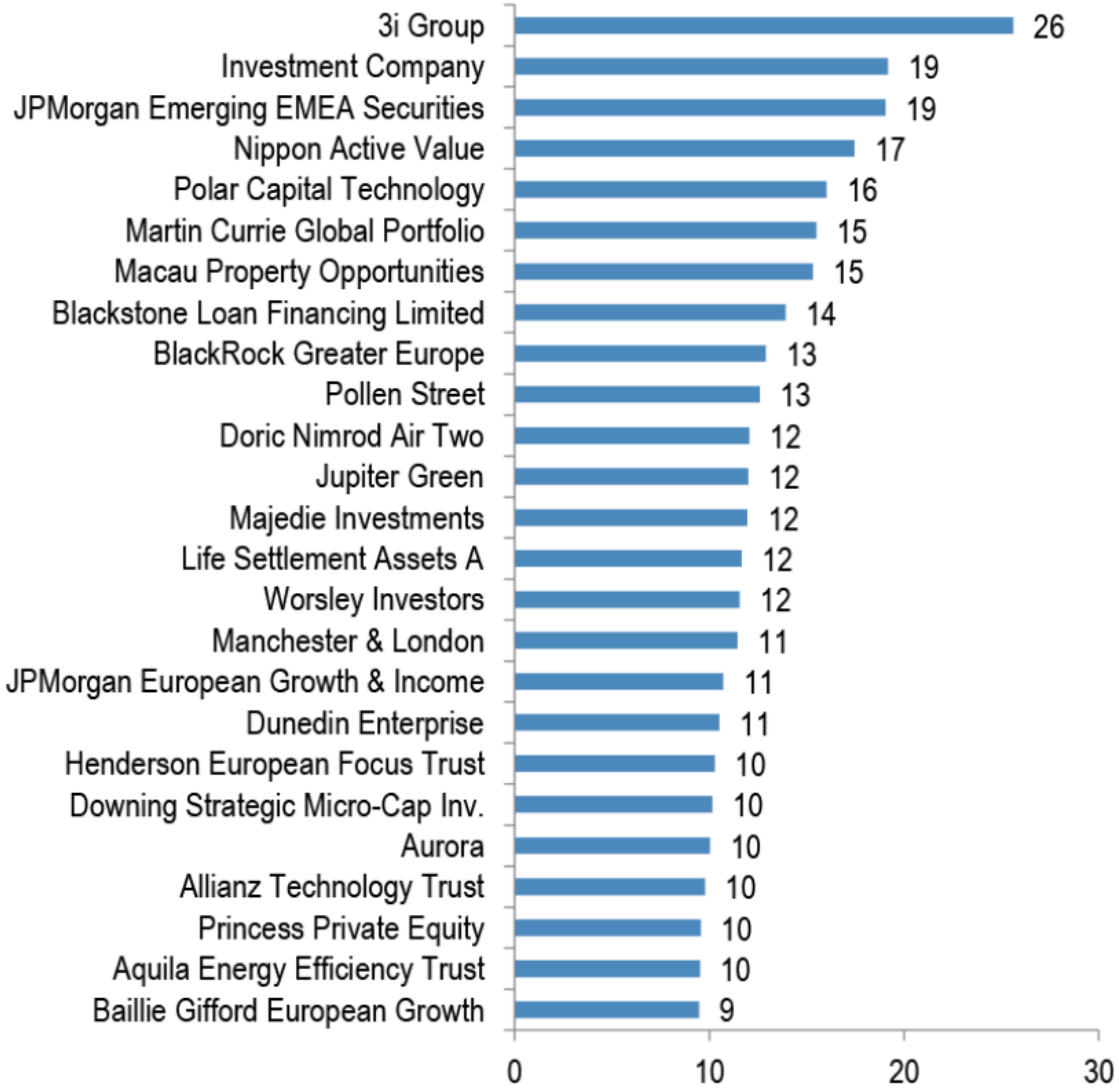
| Fund | Ticker | Now | Previous | Change |
|---|---|---|---|---|
| Doric Nimrod Air Three | DNA3 | 107.0% | 34.2% | **72.8%** |
| Doric Nimrod Air Two | DNA2 | 7.5% | -31.2% | **38.7%** |
| JZ Capital Partners | JZCP | -51.5% | -68.3% | **16.8%** |
| DP Aircraft | DPA | -73.4% | -86.2% | **12.8%** |
| Trian Investors 1 | TI1 | -14.4% | -26.2% | **11.7%** |
| Athelney Trust | ATY | -4.3% | -15.2% | **11.0%** |
| Chelverton UK Dividend | SDV | 6.5% | -4.2% | **10.7%** |
| India Capital Growth | IGC | -7.1% | -16.5% | **9.4%** |
| NB Distressed Debt Investment | NBDD | -2.8% | -12.1% | **9.3%** |
| Empiric Student Property | ESP | -15.4% | -22.9% | **7.5%** |
| Aberdeen Latin American Income | ALAI | -9.7% | -17.1% | **7.4%** |
| Aberdeen Smaller Companies Income | ASCI | -10.3% | -17.8% | **7.4%** |
| Vietnam Enterprise Investments | VEIL | -14.1% | -21.2% | **7.1%** |
| Golden Prospect Precious Metals | GPM | -13.5% | -20.4% | **7.0%** |
| Rockwood Strategic | RKW | -4.4% | -11.2% | **6.9%** |

| Fund | Ticker | Now | Previous | Change |
|---|---|---|---|---|
| JPMorgan Emerging Europe, Middle E | JEMA | 127.5% | 248.1% | **-120.7%** |
| Global Resources | GRIT | -83.1% | 17.2% | **-100.3%** |
| Schiehallion Fund C | MNTC | -48.1% | 36.1% | **-84.2%** |
| Home REIT - SUSPENDED | HOME | -66.3% | 17.9% | **-84.1%** |
| Schiehallion Fund | MNTN | -40.4% | 22.3% | **-62.7%** |
| HydrogenOne Capital Growth | HGEN | -51.5% | 9.2% | **-60.6%** |
| Molten Ventures | GROW | -67.3% | -9.6% | **-57.7%** |
| Seraphim Space | SSIT | -58.1% | -0.8% | **-57.2%** |
| Digital 9 Infrastructure | DGI9 | -44.2% | 6.6% | **-50.8%** |
| Triple Point Social Housing REIT | SOHO | -60.8% | -11.9% | **-48.9%** |
| Tritax Eurobox | EBOX | -50.1% | -5.2% | **-44.9%** |
| Petershill Partners | PHLL | -52.6% | -8.2% | **-44.4%** |
| Round Hill Music Royalty | RHM | -48.8% | -5.6% | **-43.3%** |
| Phoenix Spree Deutschland | PSDL | -63.1% | -20.4% | **-42.7%** |
| Hipgnosis Songs | SONG | -44.0% | -2.7% | **-41.4%** |

# Q1 2023: winners and losers



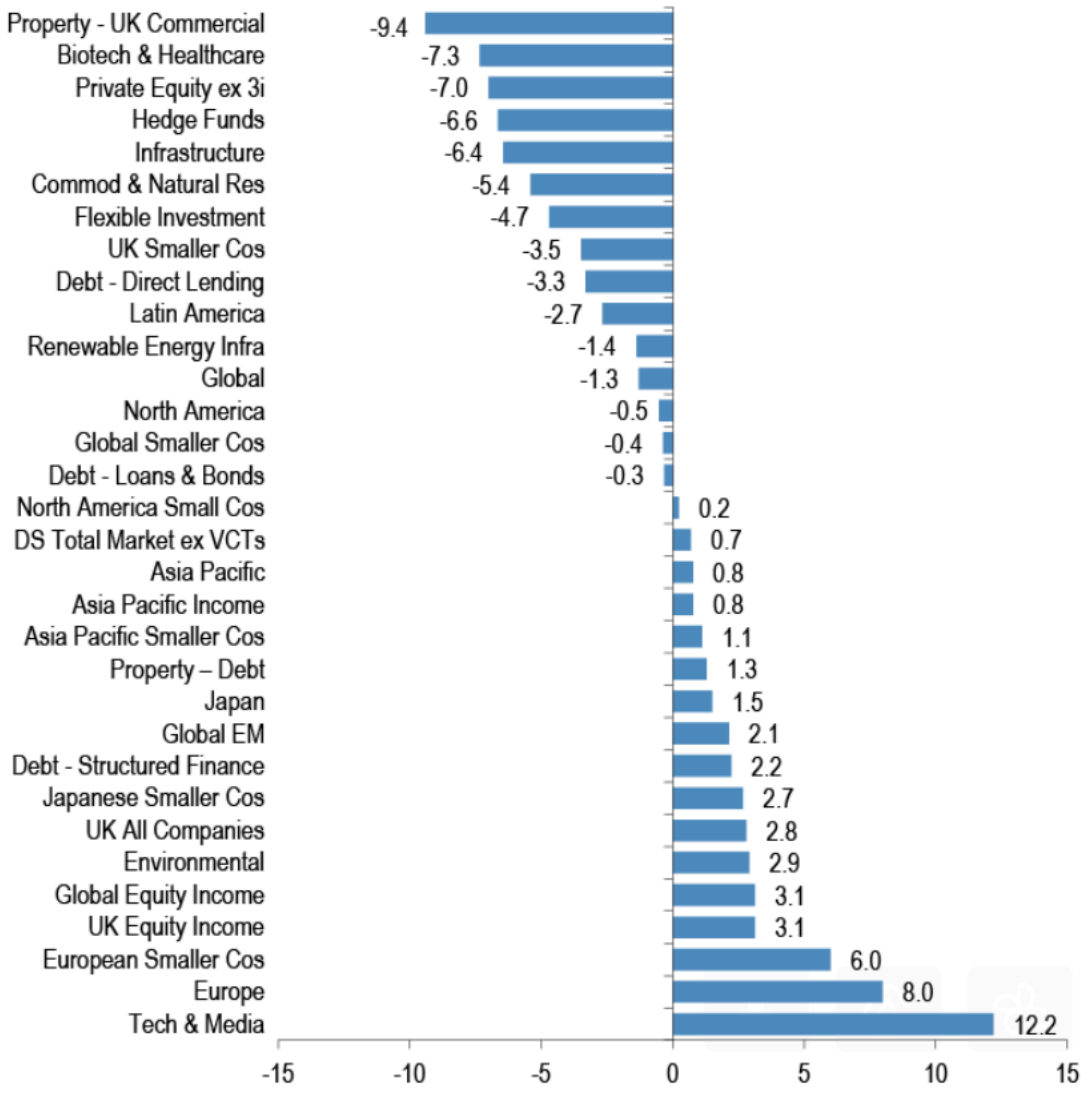

Source : Refinitiv Datastream




Source : Refinitiv Datastream

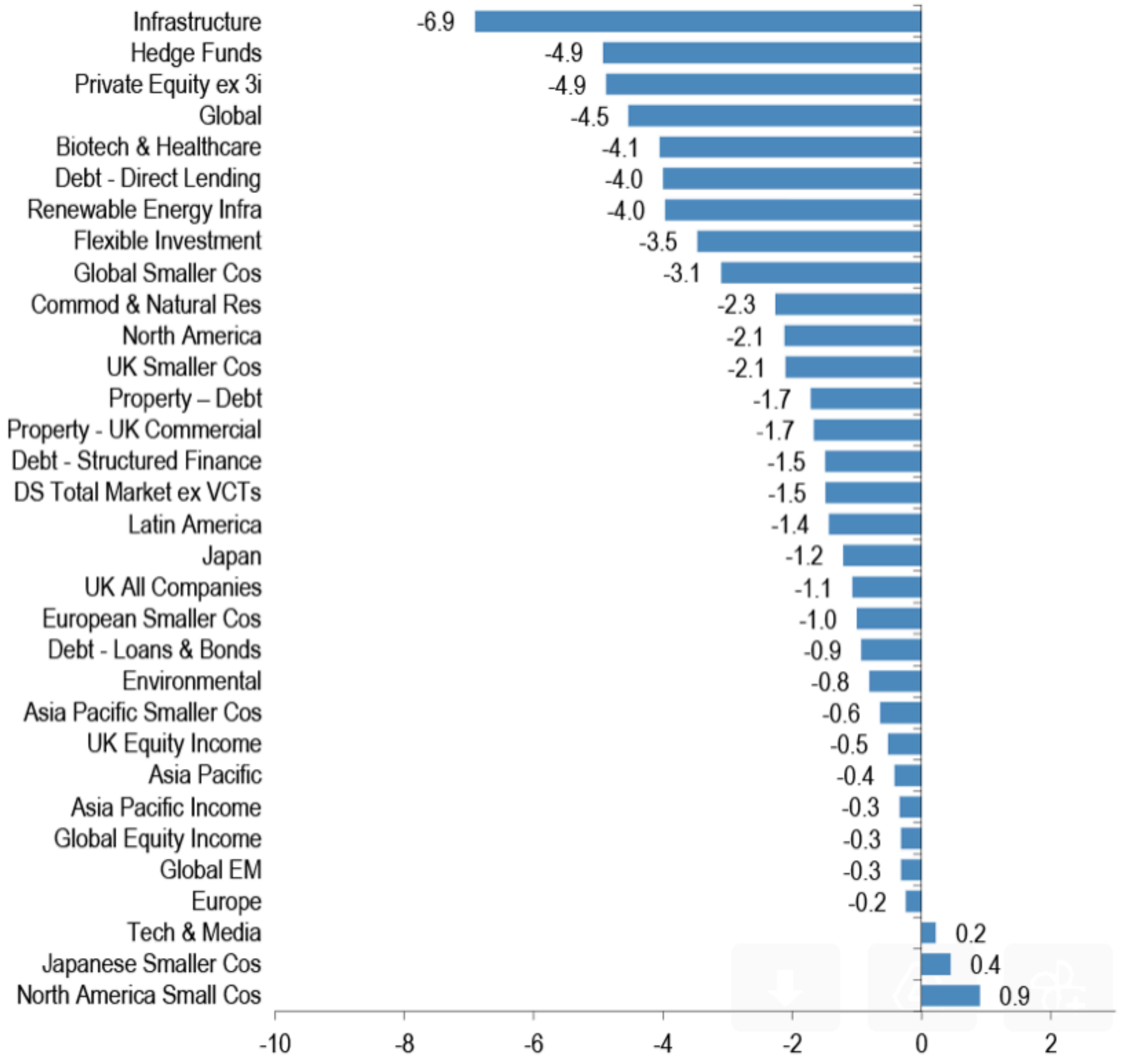
# Q1 2023: winners and losers

Share price performance




Source : Refinitiv Datastream

Discount movement




Source : Refinitiv Datastream

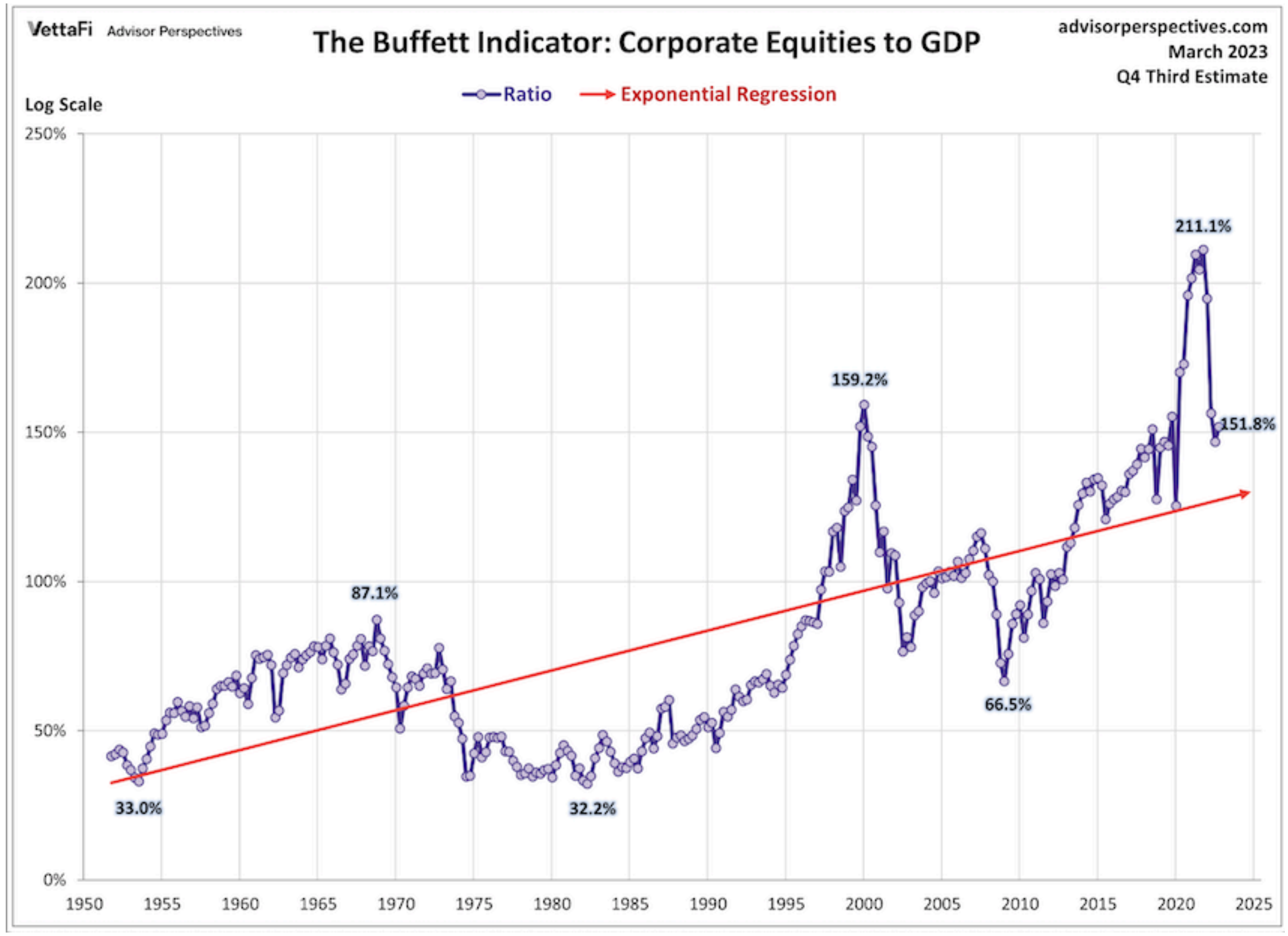
# Q1 2023: most and least popular

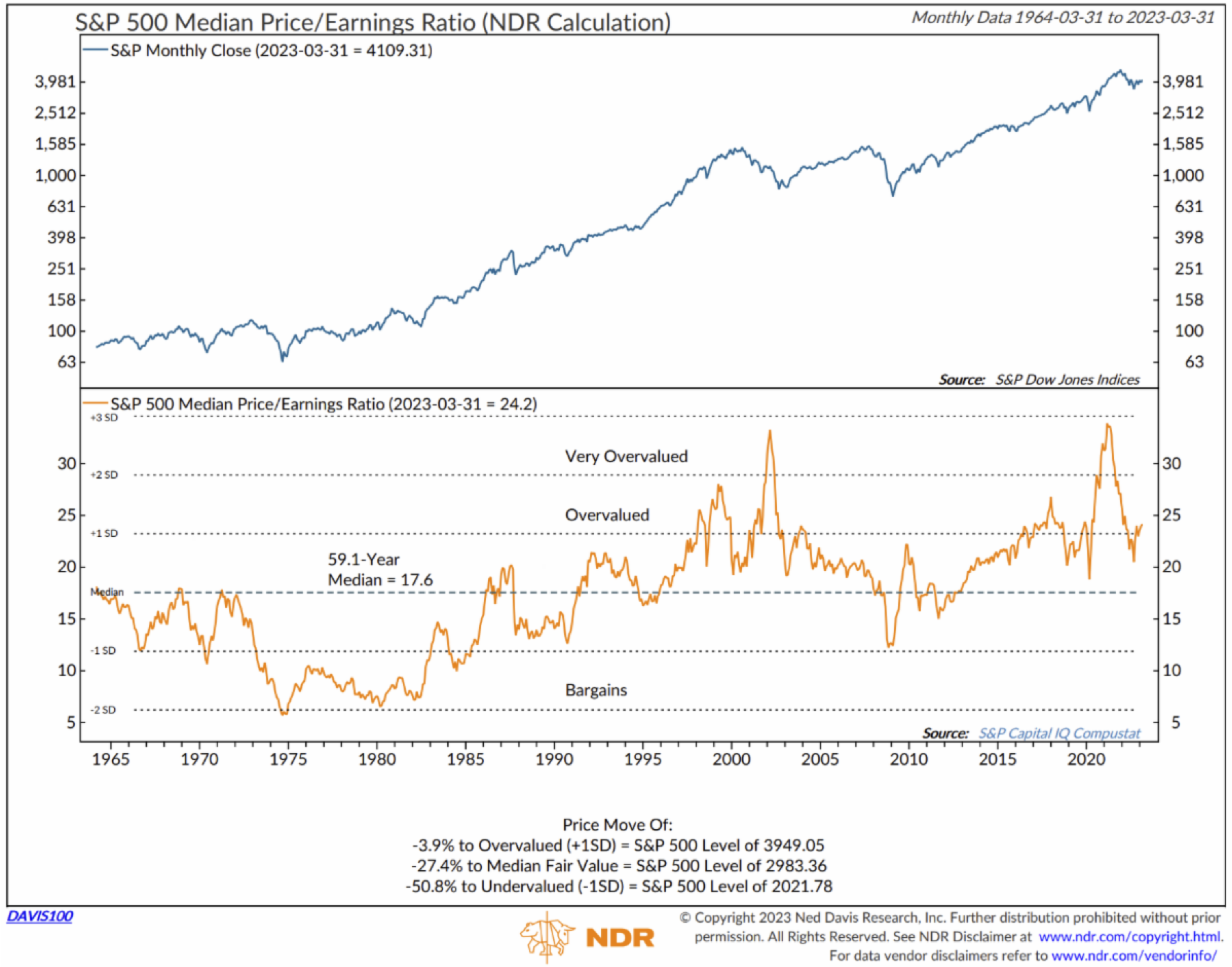
## Figure 15: AJ Bell – Most bought/sold investment companies

| Buys | | Sells | |
|---|---|---|---|
| **Fund** | **% of deals** | **Fund** | **% of deals** |
| Scottish Mortgage | 14.4% | Scottish Mortgage | 20.5% |
| City of London | 3.9% | RIT Capital Partners | 4.5% |
| Merchants | 3.9% | Capital Gearing | 3.6% |
| Renewables Infrastucture Group | 3.7% | JPM Global Growth & Inc | 3.4% |
| Alliance Trust | 3.6% | Smithson | 3.3% |
| BlackRock Throgmorton | 3.1% | BlackRock World Mining | 3.2% |
| Witan | 3.0% | Edinburgh Worldwide | 2.5% |
| Tritax Big Box | 3.9% | Greencoat UK Wind | 2.3% |
| Impax Environmental | 2.8% | Ruffer IC | 2.3% |
| F&C IT | 3.8% | City of London | 2.2% |

*Based on number of deals placed from 06 March to 06 April Source: AJ Bell*

# US equity market valuations still high

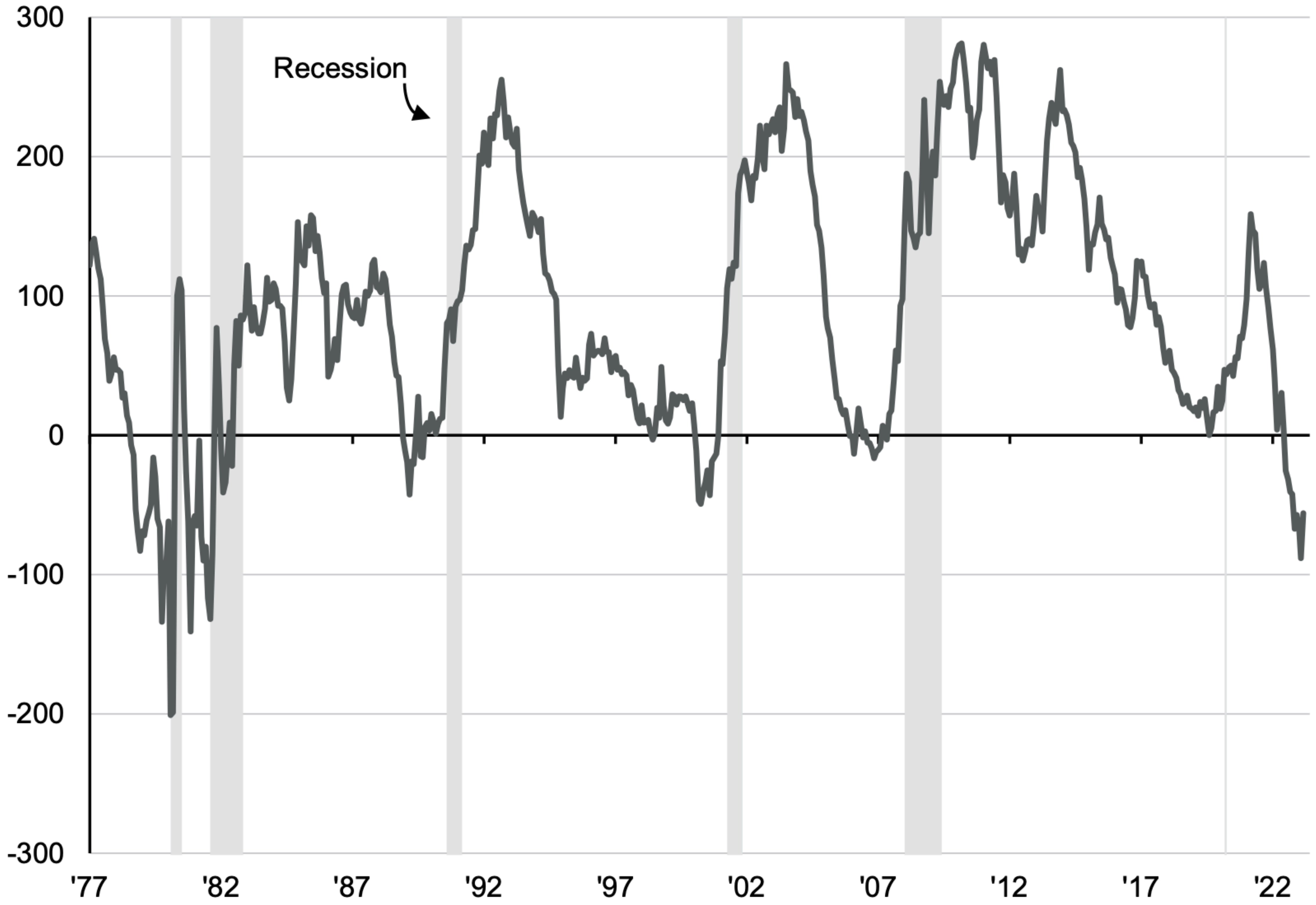


# Recession indicators flashing red

### US yield curve

Basis points, 10-year Treasury yield minus 2-year Treasury yield




### Yield curve inversion and recessions

Number of months from

| Yield curve inversion date | Curve inversion to S&P 500 peak before recession | S&P 500 peak to start of recession | Curve inversion to recession |
|---|---|---|---|
| Aug ’78 | 18 | 0 | 18 |
| Sep ’80 | 3 | 8 | 11 |
| Dec ’88 | 19 | 1 | 20 |
| May ’98 | 22 | 12 | 34 |
| Dec ’05 | 22 | 3 | 25 |
| **Median** | **19** | **3** | **20** |
| **Average** | **17** | **5** | **22** |

Source: (Left) Refinitiv Datastream, J.P. Morgan Asset Management. (Right) Refinitiv Datastream, S&P Global, J.P. Morgan Asset Management. Periods of “recession” are defined using US National Bureau of Economic Research (NBER) business cycle dates. Past performance is not a reliable indicator of current and future results. *Guide to the Markets - UK*. Data as of 31 March 2023.

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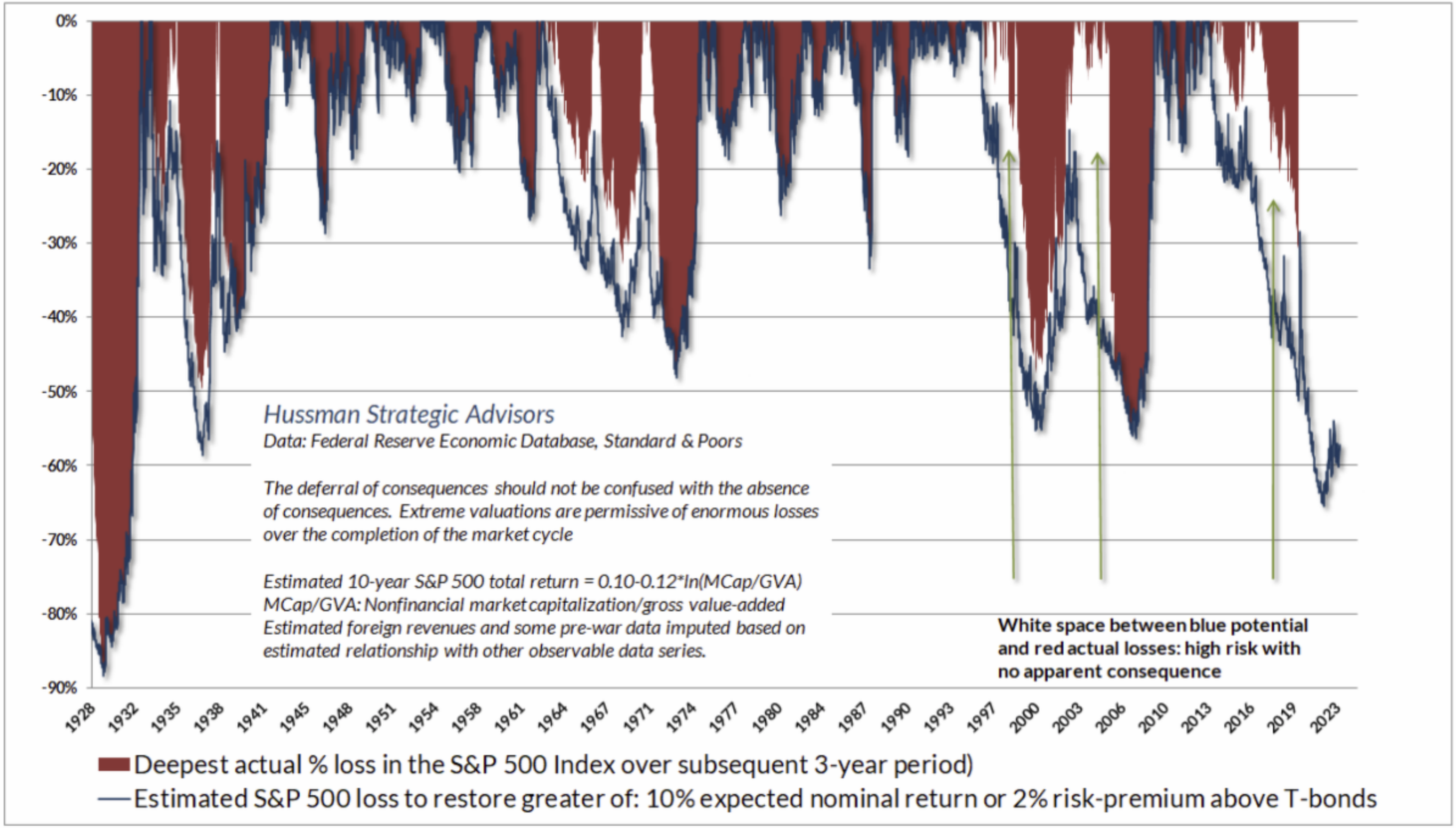
ASSET MANAGEMENT

# How far could the US stock market fall?




Based on historical experience and current valuations, to achieve a 10% annualised return over next 10 years, on some estimates the equity market could need to fall by 50%+ from peak to trough.

But NB it doesn't have to all happen in one go - more a case of adjusting your expectations to a higher interest rate world.

# Market leadership over the next few years

If the premise of a new environment is right, market leadership will change

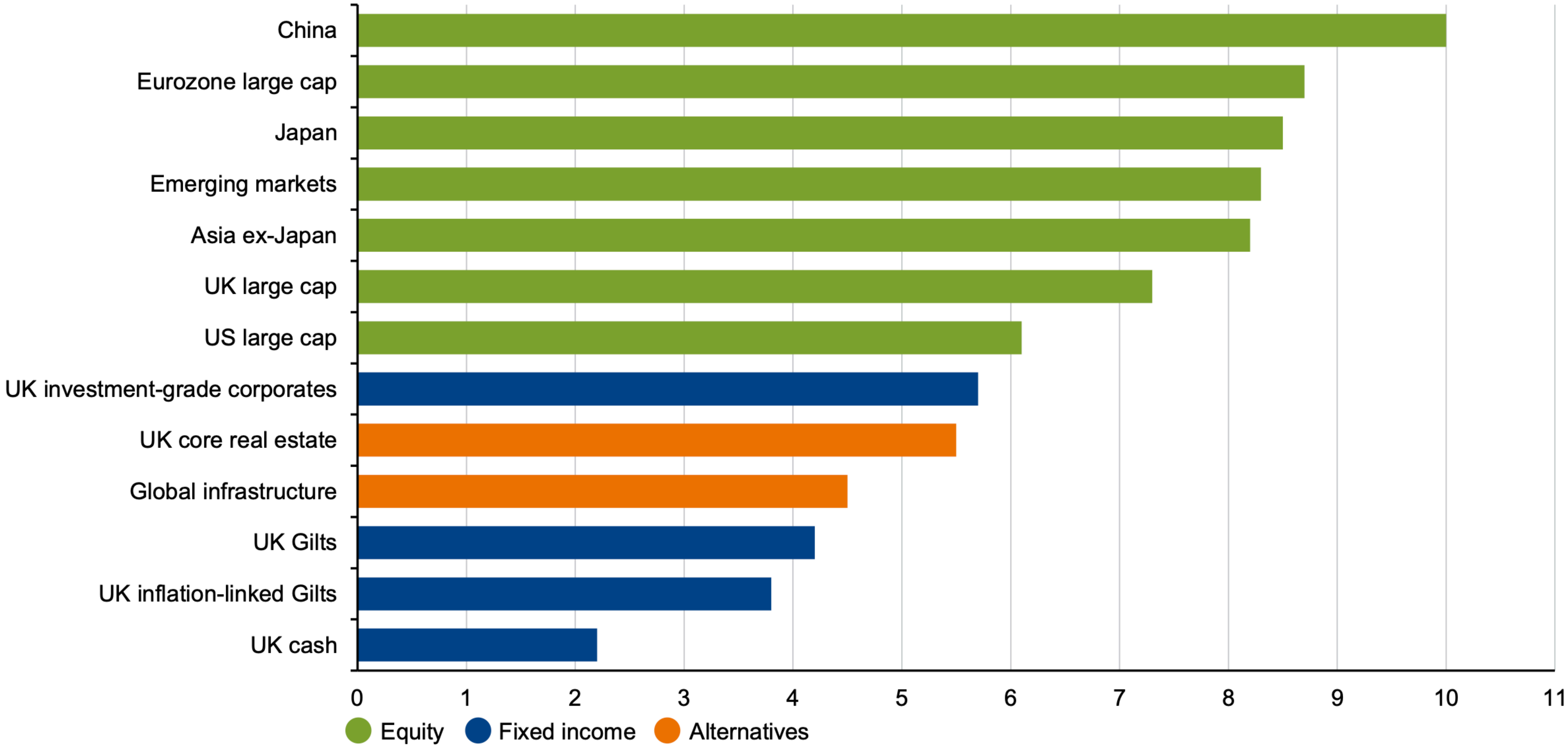
That suggests <u>**tilting**</u> towards

- Value/dividends rather than long duration/capital growth
- Rest of World versus US equities (UK, Japan look particularly cheap)
- Commodities/equity income rather than tech/growth
- Non-US currencies versus the dollar
- Public versus private equities
- Strong balance sheets versus smaller/riskier geared structures

**Your time horizon, risk tolerance, experience should drive your choices**

# Looking further ahead

**2023 Long-Term Capital Market Assumptions expected returns in coming 10-15 years**
%, annualised return in GBP




Risk and starting valuations drive long term returns but don't tell you how bumpy the journey will be.

From where we are positive but sub-10% annualised returns are the implied path = lower than in the post GFC zero-interest rate world.

Source: 2023 Long-Term Capital Market Assumptions, J.P. Morgan Asset Management. Returns are nominal and in GBP. The projections in the chart above are based on J.P. Morgan Asset Management's proprietary long-term capital market assumptions (10-15 years) for returns of major asset classes. The resulting projections include only the benchmark return associated with the portfolio and do not include alpha from the underlying product strategies within each asset class. The assumptions are presented for illustrative purposes only. Past performance and forecasts are not reliable indicators of current and future results.
*Guide to the Markets - UK.* Data as of 31 March 2023.

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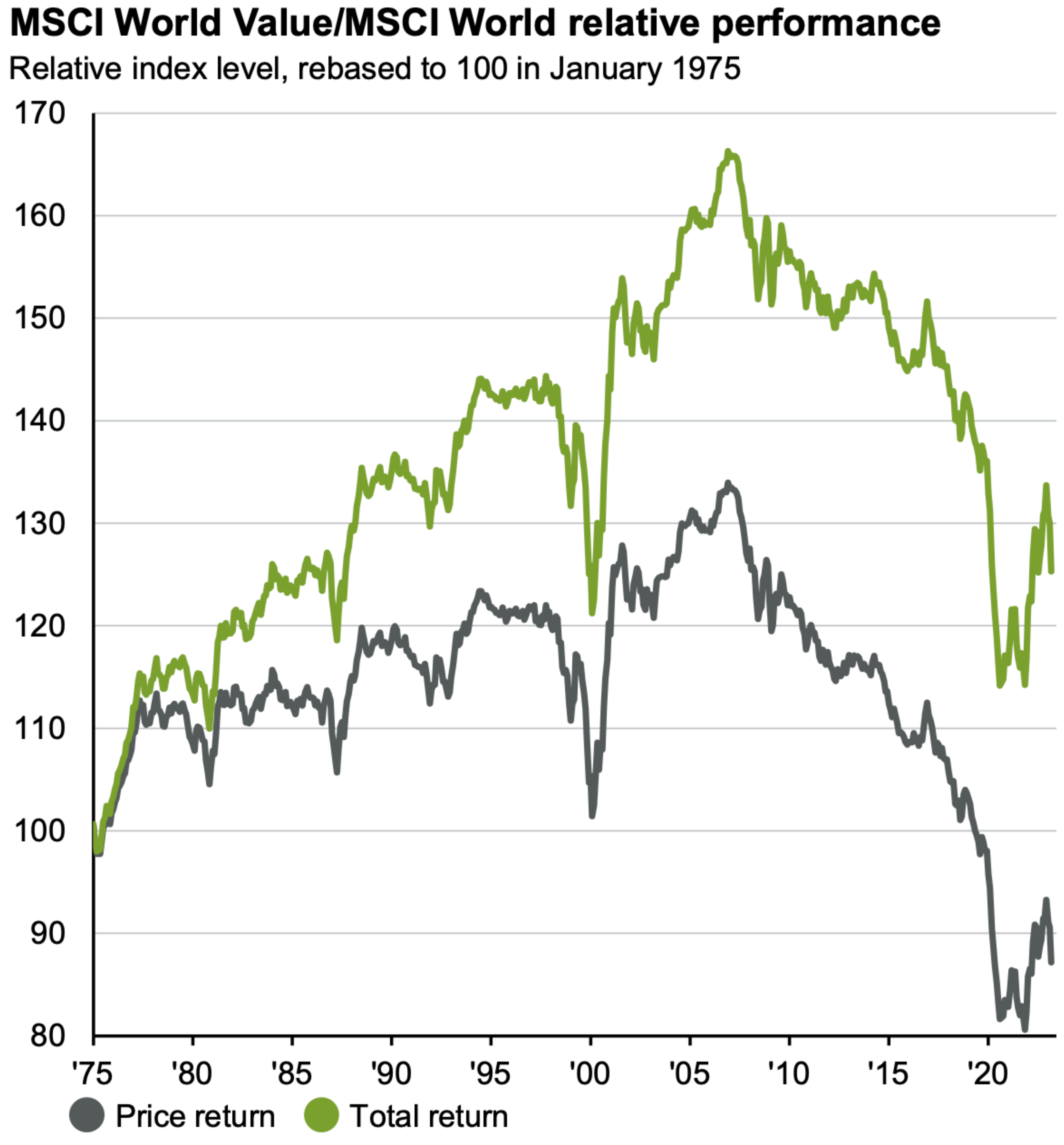
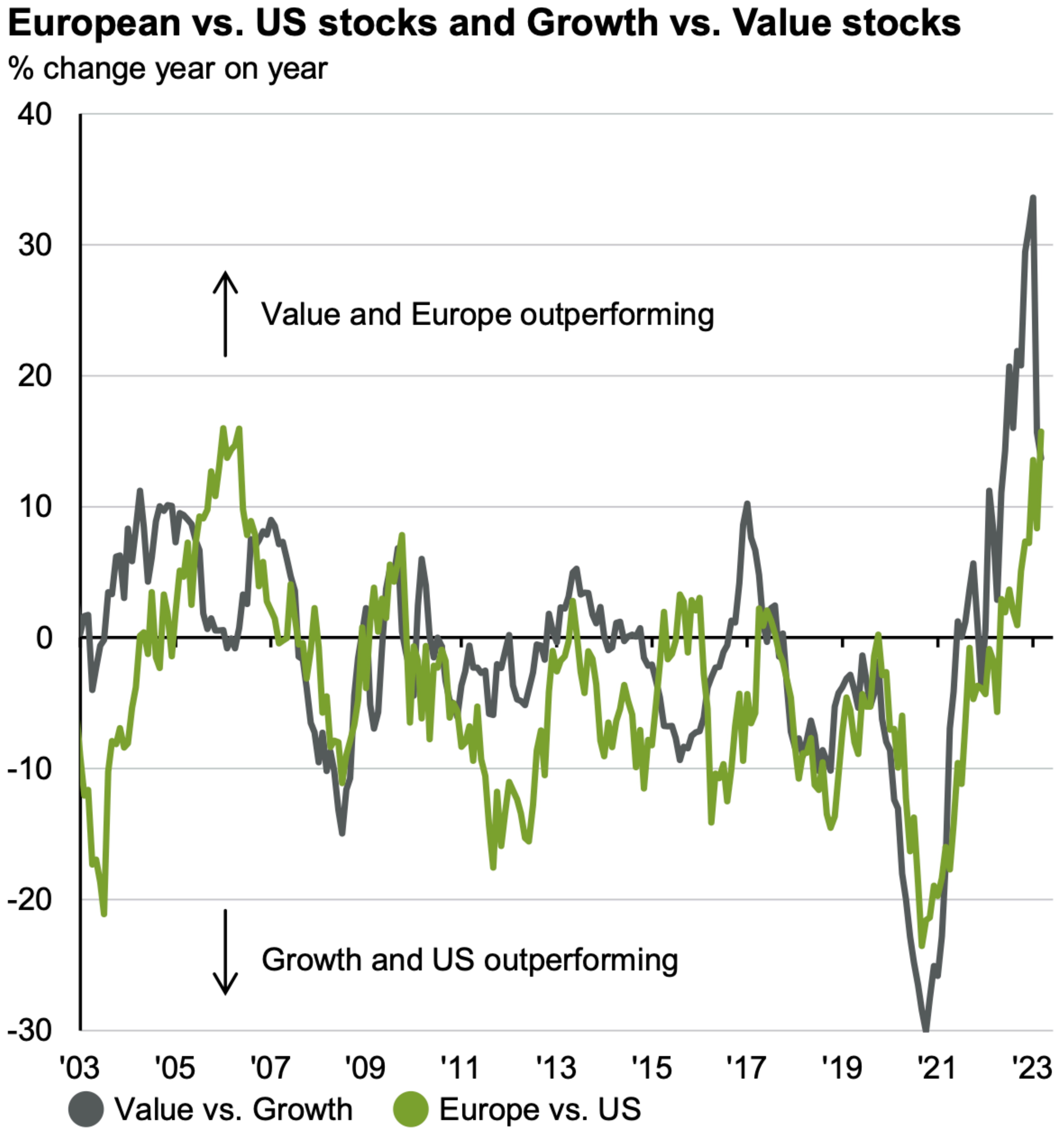
# Style and regional leadership




We are seeing some early signs that value is coming back into favour after a long period of under-performing - it is easy to forget that value historically has produced better returns than growth.

Europe is also outperforming the US market for the first time for a while which is consistent with the trend towards value. It may take time to see if this trend consolidates.

Source: (Left) MSCI, Refinitiv Datastream, J.P. Morgan Asset Management. Returns are in USD. (Right) MSCI, Refinitiv Datastream, J.P. Morgan Asset Management. Returns are in local currency. Past performance is not a reliable indicator of current and future results. *Guide to the Markets - UK.*
Data as of 31 March 2023.

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# Investment trust opportunities 1

Steady proven performers with experienced managers

- Murray International (MYI)/Scottish American (SAIN)
- J.P.Morgan Global Growth and Income (JGGI)
- Fidelity European (FEV)/Fidelity Asian Values (FAV)
- Temple Bar (TMPL)/Finsbury Growth and Income (FGI)/Merchants (MRCH)
- BioPharma Credit (BCPR) - specialist debt
- Bluefield Solar (BSF)/Greencoat UK Wind (UKW)
- Asset Value Investors (AVI)
- Blackrock World Mining (BRWM)/Blackrock Energy and Resources (BERI)
- Defensives - RICA/PNL/CGT/BH Macro (tho NB disappointing last few months)

**“There are old pilots and bold pilots, but no old bold pilots” - experience is important**

# Investment trust opportunities 2

Investable discount opportunities that are worth a look

- Pershing Square Holdings (PSH)
- Global Opportunities Trust (GOT)/maybe RIT (RCP)
- Henderson Smaller Companies (HSL)/Aberforth Smaller Companies (ASL)
- Odyssean (OIT)/Rockwood Strategic (RKW)
- Oakley Capital (OCI)/Literacy Capital (BOOK)/HG Capital (HGT)
- TR Property (TRY)/LXI REIT (LXI)
- AVI Japan Opportunity (AJOT)/Nippon Active Value (NAVF)

**Look for the opportunities to buy trusts that you know already you want to own**

# Investment trust opportunities 3

Special situations and much riskier discount opportunities

- Biotech sector looks oversold on many measures
- Civitas Social Housing (CSH)/smaller property companies
- Hipgnosis (SONG)/Round Hill Music Royalty (RHM)
- Continuation vote/consolidation candidates could go to par on exit
- M&A eg recent Blackstone agreed bid for Industrials REIT at 30% premium
- Chrysalis (CHRY)/microcap trusts - not for me, but…..
- Interest rate outlook is critical for many growth trusts

**Don’t be a hero - keep high risk bets to a manageable % of your portfolio**

*The stock market “transfers wealth from the impatient to the patient” (Warren Buffett)*

# Investment trust straws in the wind?

- Troubles surfacing - social housing, HOME REIT, Scottish Mortgage
- Sector will shrink - Darwinian process at work - liquidations/wind ups
- Consolidation - eg abrdn Smaller Companies Income, Ediston Property
- IPOs nearly at a standstill; 2022 inflows down 90%
- Buybacks accelerating - boards' commitment being tested
- Extreme discounts in private equity/property/specialists suggest sector risks
- Liquidity not improving for smaller trusts but discounts appealing
- More important than ever to be discerning - quality will out

**These trends are likely to continue - but structural advantages will win out over time**

# Conclusions: is your portfolio fit for purpose?

- More important than ever to be discerning - value quality and experience
- Be patient - this cycle will play itself out, though it could take 12-18 months
- Don’t be fooled by big discounts - always look behind the numbers
- Equally remember that premiums rarely last - it is okay to top slice
- Keep a list of trusts you really want to buy - track the discounts, pounce
- Keep the faith - investment trusts strengths will come through again

**Investment trust universe is reshaping itself and has survived much worse**

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# Investment trusts: stick or twist?

## Facing the discount challenge

*Request today's slides?*

*Email: editormm124*

*@gmail.com*

*April 15th 2023*