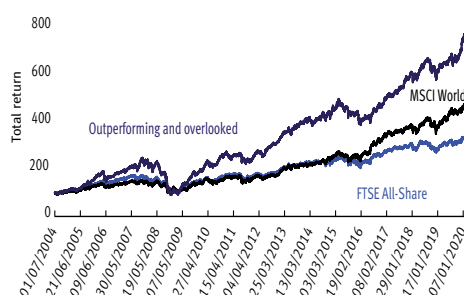




## Alpha Investment Trusts: Highlighting sector plays

*The investment trust sector is wonderfully diverse. Our screen compares the best value closed-end funds, whatever their investment mandate, and identifies those with the best growth prospects. We screen for our top 25 trusts and select an automated portfolio of 10*

### Outperforming and overlooked trusts



### Screen methodology:

To fairly compare investment trusts with different remits and capital structures, we assess funds' value relative to their historic mean premium/discount. Three-month share price momentum indicates market sentiment towards the funds. Next, a composite value-momentum ranking is arrived at using hedge fund manager Joel Greenblatt's 'Magic Formula' two-factor model. Our tables show the top 25 investment trusts and a portfolio of 10 investment trusts subject to additional selection criteria.

■ Investors are often told that it's good to buy on the dips, but when the stock market plunges like it has in the past two weeks, it's important to accept that things can get worse before they get better. Dripping money in gradually may be a better way to play emerging value opportunities.

■ Buyers of investment trusts might have the comfort that at least the underlying portfolio is falling less rapidly than the shares of the company itself. This has the effect of widening the discount, although it must be stressed that you could still be trying to catch a falling knife.

■ Investing, however, is a long-term game and some of the trusts our screen signals are in value territory represent an attractive entry point to access the strategies of proven investment companies. Most strikingly, the £8.9bn market-cap **Scottish Mortgage Trust (SMT)** ranks highly.

■ Other niche trusts represent powerful ways to play long-term growth trends, with **Biotech Growth Trust (BIOG)** and **Allianz Technology (ATT)** ranking in our top 10.

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### **Making fair comparison in the richly diverse investment trust sector**

Valuation metrics for trusts are very limited relative to those for other equities, with the key measure of value being the discount or premium a trust's shares trade at, compared with its net asset value (NAV) per share. However, the average historic discount of individual trusts is strongly influenced by the assets they invest in and past performance, along with multiple other factors such as the trust's structure and the level of 'gearing' it employs to enhance returns. So, while one trust trading at a 10 per cent discount to NAV may look achingly cheap against its history, another trust trading at the same discount may be considered eye-wateringly expensive.

Meanwhile, an assessment of the underlying quality of an investment trust also depends on many factors that are often unique to the trust concerned. Screens are ill-suited to providing a nuanced analysis and direct comparisons between trusts with different characteristics can be misleading.

However, we have found that a useful screen can be created by focusing on two 'high-level' factors that researchers have shown to be predictive of future share price performance: 'value' and 'momentum'. Based on 14-year back-testing of the screen (the period over which we have been able to source reliable historic data), this strategy has produced a 619 per cent cumulative total return or 482 per cent if an annual dealing charge is included for the presumed yearly reshuffles of the portfolio. Over the same period, a 50:50 split between the FTSE All-Share and the MSCI World indices has produced a 250 per cent total return (see graph on page 1). This data is based on annual reshuffles of 10-stock portfolios like the one on page 5, which applies the rules listed on page 4.

### How the screen works

The screen uses the following two criteria:

**Value:** To hunt for value, this screen looks at a trust's premium or discount compared with its own one-year historic average. A statistical measure known as the Z-score is used to do this which produces a standardised score based on where the premium or discount sits compared with its historic range (the score measures how many standard deviations the current valuation is from the mean average). A negative Z-score suggests a trust is cheap relative to its own historic standards (the larger the negative score the cheaper). A positive score suggests a trust is expensive. Because each trust has its current valuation compared with its own valuation history rather than that of other trusts, the Z-score can be used to make comparisons between trusts with very disparate valuation characteristics.

**Momentum:** The other factor the screen looks at is recent share price performance. There is a huge body of research that has found rising share prices tend to beget more of the same. Specifically, the screen wants to see strong share price performance over three months. The fact that the screen looks at price and not NAV performance means some credence is given to the wider market view of a trust's prospects. For example, if sentiment has been improving towards a trust, thereby narrowing its discount over the three months, this will create stronger momentum which means a more favourable ranking from the screen. Scepticism implied by a widening discount will, by contrast, act as a headwind to price performance. That said, the overall objective when combining momentum with value is to find promising performance trends that the market has not yet fully priced in.

### Bringing it all together

To assess both factors together, the screen uses the ranking method employed by hedge fund manager Joel Greenblatt in his two-factor 'magic formula' (the magic formula uses different inputs). The method simply ranks both factors and then adds the rankings together to find the trusts with the most attractive combined ranking.

The top 25 ranking trusts are presented in the table on page 5, while a portfolio of 10 trusts is published in the table on page 5 based on the following rules:

### The 10-stock portfolio rules

- Market capitalisation must be more than £100m.
- No tracker or hedge funds.
- No more than half the portfolio (five out of 10 shares) should be in funds with a niche theme. Trusts defined as niche are those focused on non-mainstream asset classes or sub-sectors such as private equity, debt, technology and biotechnology, and those focused on single countries (excluding the UK and US) or high-risk economic regions such as emerging markets. I also regard Asian smaller companies trusts as niche, but not Asian generalists.
- No more than half the portfolio (five out of 10 shares) should be mainstream funds of the same type. This rule does not apply to global funds, but it does to other mainstream themes such as trusts investing in the UK (large and small companies), Europe, the US or Asia.
- All trusts must trade at a discount to NAV.

## 10-trust portfolio

Rank	Name	TIDM	Market cap	Price	DY	Z-score	Now	Discount to NAV			1m	3m	6m	Share price performance		
								Avg	Low	High				1y	3y	5y
1	Biotech Growth Trust	BIOG	£386m	978p	–	-1.6	-10.1%	-8.0%	-4.8%	-11.6%	1.5%	16.2%	29.7%	31.8%	25.7%	30.2%
2	JPM American	JAM	£970m	466p	1.4%	-4.5	-7.2%	-4.1%	-2.1%	-8.1%	-7.7%	0.5%	-1.7%	10.1%	24.7%	76.0%
3	Allianz Technology	ATT	£628m	1,760p	–	-1.1	-2.0%	-0.1%	3.8%	-8.9%	-5.8%	9.6%	4.1%	19.3%	94.0%	201.9%
4	JPM China Growth & Income	JCGI	£258m	355p	0.7%	-0.8	-13.0%	-11.0%	-3.0%	-17.3%	1.0%	14.2%	14.3%	29.1%	70.0%	101.6%
6	Pacific Horizon	PHI	£195m	330p	–	-1.3	-9.3%	-4.2%	5.5%	-10.7%	-3.9%	4.1%	4.3%	1.4%	45.1%	72.7%
7	Scottish Mortgage	SMT	£8,865m	610p	0.5%	-0.7	-2.0%	-0.4%	3.8%	-6.8%	-1.9%	17.7%	17.7%	24.1%	78.5%	150.0%
10	Fidelity China Special Situations	FCSS	£1,280m	236p	1.6%	-0.6	-8.3%	-7.8%	-3.5%	-11.4%	1.3%	12.1%	7.8%	4.4%	31.1%	89.3%
13	European Opportunities	JEO	£927m	821p	0.7%	-1.6	-6.4%	-3.0%	2.6%	-6.9%	-9.1%	0.5%	-2.5%	15.8%	42.4%	67.9%
19	Alliance Trust	ATST	£2,557m	777p	1.8%	-3.2	-7.9%	-5.8%	-3.7%	-9.1%	-8.4%	-3.5%	-3.4%	6.3%	18.7%	73.9%
21	Independent Inv. Trust	IIT	£294m	538p	1.5%	-0.4	-5.0%	-4.0%	4.6%	-10.0%	-7.7%	4.5%	9.8%	-1.6%	27.6%	97.2%

Winterflood Investment Trusts, as at: 5 March 2020

## Top 25

Rank	Name	TIDM	Market cap	Price	DY	Z-score	Now	Discount to NAV			1m	3m	6m	Share price performance		
								Avg	Low	High				1y	3y	5y
1	Biotech Growth Trust	BIOG	£386m	978p	–	-1.6	-10.1%	-8.0%	-4.8%	-11.6%	1.5%	16.2%	29.7%	31.8%	25.7%	30.2%
2	JPM American	JAM	£970m	466p	1.4%	-4.5	-7.2%	-4.1%	-2.1%	-8.1%	-7.7%	0.5%	-1.7%	10.1%	24.7%	76.0%
3	Allianz Technology	ATT	£628m	1,760p	–	-1.1	-2.0%	-0.1%	3.8%	-8.9%	-5.8%	9.6%	4.1%	19.3%	94.0%	201.9%
4	Fair Oaks Income #	FAIR	£243m	1p	12.2%	-1.8	-10.3%	-4.2%	1.2%	-12.3%	-1.8%	1.8%	-8.9%	-0.1%	11.6%	49.5%
4	JPM China Growth & Income	JCGI	£258m	355p	0.7%	-0.8	-13.0%	-11.0%	-3.0%	-17.3%	1.0%	14.2%	14.3%	29.1%	70.0%	101.6%
6	Pacific Horizon	PHI	£195m	330p	–	-1.3	-9.3%	-4.2%	5.5%	-10.7%	-3.9%	4.1%	4.3%	1.4%	45.1%	72.7%
7	Scottish Mortgage	SMT	£8,865m	610p	0.5%	-0.7	-2.0%	-0.4%	3.8%	-6.8%	-1.9%	17.7%	17.7%	24.1%	78.5%	150.0%
8	CVC Credit Partners Euro Opps	CCPG	£250m	101p	5.5%	-1.9	-6.6%	-2.6%	2.6%	-7.9%	-3.6%	1.2%	-1.2%	-0.1%	7.1%	25.4%
9	VPC Specialty Lending #	VSL	£249m	81p	9.9%	-0.8	-16.3%	-13.6%	-4.2%	-20.9%	-0.5%	6.1%	6.1%	16.2%	38.7%	19.5%
10	Fidelity China Special Situations	FCSS	£1,280m	236p	1.6%	-0.6	-8.3%	-7.8%	-3.5%	-11.4%	1.3%	12.1%	7.8%	4.4%	31.1%	89.3%
11	Asia Dragon	DGN	£514m	402p	1.2%	-1.2	-11.5%	-10.7%	-8.0%	-13.6%	-1.6%	3.1%	-0.5%	9.1%	26.3%	50.6%
12	JPEL Private Equity - US\$	JPEL	£190m	1p	–	-1.4	-24.1%	-19.7%	-15.1%	-24.4%	0.7%	1.5%	-11.8%	17.1%	149.2%	274.1%
13	European Opportunities	JEO	£927m	821p	0.7%	-1.6	-6.4%	-3.0%	2.6%	-6.9%	-9.1%	0.5%	-2.5%	15.8%	42.4%	67.9%
14	BioPharma Credit - US\$	BPCR	£1,068m	1p	8.3%	-1.5	-2.5%	0.4%	4.3%	-3.5%	-0.2%	0.8%	-2.6%	4.4%	–	–
15	Schroder AsiaPacific	SDP	£744m	444p	2.2%	-1.5	-10.4%	-8.8%	-5.7%	-12.0%	-2.7%	0.5%	1.1%	4.9%	27.8%	65.8%
15	Standard Life Private Equity	SLPE	£543m	353p	3.6%	-0.7	-20.0%	-16.5%	-5.9%	-25.2%	-9.3%	3.5%	-1.9%	4.3%	31.8%	103.1%
15	Starwood Euro Real Estate Fin.	SWEF	£419m	102p	6.4%	-1.9	-2.1%	1.1%	5.9%	-3.2%	-1.0%	-1.0%	-1.0%	2.9%	12.1%	31.9%
18	Ecofin Global Utilities & Infrastructure	EGL	£155m	169p	3.8%	-0.1	-10.0%	-9.5%	0.1%	-17.0%	-3.9%	9.8%	12.9%	34.5%	69.3%	–
19	Alliance Trust	ATST	£2,557m	777p	1.8%	-3.2	-7.9%	-5.8%	-3.7%	-9.1%	-8.4%	-3.5%	-3.4%	6.3%	18.7%	73.9%
19	Electra Private Equity	ELTA	£127m	333p	–	-0.4	-35.6%	-33.4%	-17.3%	-50.9%	-8.4%	5.1%	-3.3%	10.1%	-8.1%	55.7%
21	Independent Inv. Trust	IIT	£294m	538p	1.5%	-0.4	-5.0%	-4.0%	4.6%	-10.0%	-7.7%	4.5%	9.8%	-1.6%	27.6%	97.2%
22	ICG-Longbow Snr Sec Prop Debt	LBOW	£116m	96p	6.3%	-1.2	-1.1%	0.6%	3.0%	-3.5%	-3.3%	0.8%	-3.1%	2.4%	13.8%	24.2%
23	Schroder Asian Total Return	ATR	£341m	348p	1.8%	-2.0	-0.6%	2.2%	5.6%	-3.1%	-5.2%	-2.5%	-3.9%	0.3%	30.9%	78.6%
23	PRS REIT	PRSR	£416m	84p	6.0%	-1.8	-10.6%	-2.0%	7.0%	-11.7%	-7.7%	-1.8%	-4.6%	-12.6%	–	–
25	Aberdeen Asian Income	AAIF	£350m	198p	4.7%	-2.0	-8.8%	-7.1%	-4.5%	-9.2%	-4.6%	-2.7%	-7.7%	-0.4%	8.6%	26.2%

Winterflood Investment Trusts, as at 5 March 2020

*(Methodology and screens by Algy Hall)*

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