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In Changing of the Seasons We (Investment) Trust...

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It is the time of year when we, in the northern hemisphere, emerge from winter, welcome new life, and even start a new UK tax year. Our gardens sprout new growth and rediscover colourful displays, it is in many ways an optimistic time of year. Investors might be tempted to have similar feelings towards the investment trust market.

To recap, recent years have seen what feels like an unprecedented period of "issuance" where new investment trusts were formed to invest in a variety of assets such as property, infrastructure and even esoteric things such as music royalties, that have typically been out of reach of many investors. The shares of such vehicles typically traded at premiums to Net Asset Value (NAV) which afforded them to issue further equity and expand their portfolios of assets. With the odd exception, returns were good, dividend income was earned, investors diversified their portfolios beyond simply holding equities and bonds, and UK plc benefitted from a new source of financial capital to help address the almost overwhelming need for investment in its physical capital. All was going well and then the season changed...

It started with the Autumn "fiscal event" which set bond yields reaching for the stars, with a resultant negative impact on NAVs which take some of their reference point from the plunging value of "risk free" government debt. Even though some normality returned to gilts under Jeremy Hunt, the damage was done; it has been an embarrassing lesson for enthusiasts of backward looking "risk" models.

The situation was made worse by what can only be assumed were unintended consequences of the application of cost disclosure regulation for investors in Europe. The problems raised by these rules are too expansive to cover here but have been commented elsewhere in the investment press. However, in simple terms they have created an uneven playing field that has unfairly penalised holders of these specialist investment trusts versus ordinary equities. By making funds that hold investment trusts such as Greencoat UK Wind optically (but crucially not economically) more expensive than other investors that hold listed equities such as SSE plc, the rules on cost disclosure have removed a key "marginal buyer" of investment trusts.

The price of anything that is traded is set by the marginal buyer and marginal seller, that is where the last available seller will supply an asset and the last available buyer is prepared to buy an asset at a given price. Once you remove one of those market participants, the price resets to find the next marginal buyer/seller. The motivation to buy or sell is driven by a multitude of factors, only one of which is the price.

In the case of investment trusts, investors who were buying in the years leading up to mid-2022 will have been drawn to income paying credentials, diversification benefits, ESG attractions, their own investment inflows and outflows to name a few; the premiums to NAV implied there was more buying demand than any need to sell investment trusts. However, in the last six to nine months those marginal buyers have either walked away or even become sellers; possibly spooked by falling NAVs, needing to finance outflows from their own investor base, or reluctant to have to report their optically (but not economically) higher cost of holding investment trusts.

The result of this descent into winter has resulted in discounts to NAV opening up of 10-20% in some infrastructure names; up to 30% in property REITs (despite solid evidence of rental growth in many sectors), whilst private equity is suffering discounts of over 50% in some names.

It is true that the sector has not helped itself with scandals such as HOME REIT shaking investor confidence, and private equity allowing itself to get carried away with some deals in the period of low interest rates. Greed also resulted in an excessive number of trusts being launched that has resulted in too many being sub-scale. Self-help is required with Boards instigating consolidation; yes, an ironic test for a quality Board is its preparedness to put itself out of a job.

With valuations being where they are, it is hard to believe that marginal buyers will not return, particularly if catalysts for value discovery occur. Furthermore, common sense could be restored as a result of the packaged retail investment and insurance products and UK Retail Disclosure consultation papers from the Government and Financial Conduct Authority in March. Selling investment trusts at this time does not feel economically rational.

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Market Focus - 17 April 2023

- **Global equities returned 1.3% last week**
- **The International Monetary Fund (IMF) revised down their global growth prediction for both 2023 and 2024 by a tenth relative to their January predictions in their April economic outlook. They now see global growth at +2.8% in 2023 and +3.0% in 2024**
- **Brent crude rose by 1.4% to $86.31 per barrel**
- **Gold fell by 0.2% to $2004.17 per ounce**

US

- US equities rose 0.8% last week
- The year-on-year Consumer Price Index (CPI) rate was down to +5.0% (vs. +5.1% expected), which is the lowest since May 2021
- The stickier core CPI reading was more resilient, coming in as expected at +4.7% on an annualised basis
- The labour market remained tight as the unemployment rate fell back a tenth to 3.5% (vs. 3.6% expected) and the participation rate hit a post-COVID-19 high of 62.6% (vs. 62.5% expected)
- The effects of the banking crisis continue to be felt, a net of 9% of small business owners who borrow frequently said that financing was more difficult to obtain compared to three months earlier

UK

- UK equities returned 1.7% last week
- The IMF's economic outlook projected UK Gross Domestic Product (GDP) to contract by -0.3% (vs. -0.6% in January) despite a revision down of global growth prospects
- Monthly GDP growth in February was flat (vs. +0.1% expected), although the overall picture was a bit better than that implied since the January figure was revised up a tenth to +0.4%

Europe

- European equities returned 2.0% last week
- Despite difficulties in the banking sector, European Central Bank members still expect the next rate hike to be between 25 and 50bps. Austria's Holzmann said in an interview that they should hike by another 50bps in May and that the "danger of currently doing too little and to fan inflation is bigger than the risk of doing too much"
- Euro Area retail sales contracted by -0.8% in February, as expected

Rest of the World/Asia

- Global emerging market equities returned 1.4% last week
- Japanese equities rose by 2.7% last week
- The Yen fell sharply on comments from new Bank of Japan Governor Ueda, who said that "given the current economic, price and financial conditions, I think it's appropriate to keep up the current yield curve control"
- Chinese exports grew by 14.8% year-on-year, far exceeding the expected decline of -4.1% as the country continued to emerge from lockdown
- Chinese year-on-year loan figures also rose by 11.8%

Market Summary

Asset Class / Region	Currency	Week ending 14 April	Month to date	YTD 2023	12 months
		Cumulative returns			
Developed Markets Equities					
United States	USD	0.8%	0.7%	8.1%	-4.7%
United Kingdom	GBP	1.7%	3.5%	6.9%	7.5%
Continental Europe	EUR	2.0%	2.0%	12.2%	6.3%
Japan	JPY	2.7%	0.8%	8.0%	8.8%
Asia Pacific (ex Japan)	USD	1.1%	0.9%	5.0%	-6.2%
Australia	AUD	2.0%	2.6%	6.1%	2.3%
Global	USD	1.3%	1.3%	9.1%	-2.9%
Emerging Markets Equities					
Emerging Europe	USD	4.5%	6.7%	8.3%	9.6%
Emerging Asia	USD	0.9%	0.5%	5.3%	-6.9%
Emerging Latin America	USD	5.6%	4.4%	8.5%	-4.5%
BRICs	USD	0.8%	0.4%	1.3%	-6.7%
China	USD	-0.3%	-1.4%	3.3%	-4.1%
MENA countries	USD	0.6%	2.6%	0.7%	-21.0%
South Africa	USD	1.9%	1.6%	1.0%	-15.0%
India	USD	1.5%	3.3%	-0.2%	-3.9%
Global emerging markets	USD	1.4%	1.1%	5.1%	-7.9%
Bonds					
US Treasuries	USD	-0.6%	-0.1%	3.1%	-2.0%
US Treasuries (inflation protected)	USD	-0.1%	0.3%	3.7%	-4.1%
US Corporate (investment grade)	USD	-0.9%	0.2%	3.6%	-1.6%
US High Yield	USD	0.8%	0.7%	4.5%	-1.0%
UK Gilts	GBP	-2.1%	-1.1%	1.1%	-15.2%
UK Corporate (investment grade)	GBP	-1.0%	-0.1%	2.3%	-9.9%
Euro Government Bonds	EUR	-1.7%	-0.9%	1.7%	-10.2%
Euro Corporate (investment grade)	EUR	-0.8%	0.0%	1.6%	-6.4%
Euro High Yield	EUR	0.3%	0.4%	3.1%	-3.0%
Japanese Government	JPY	0.0%	-0.5%	1.9%	-2.0%
Australian Government	AUD	-0.7%	0.0%	5.1%	0.9%
Global Government Bonds	USD	-0.9%	-0.1%	3.1%	-5.7%
Global Bonds	USD	-0.6%	0.2%	3.5%	-4.7%
Global Convertible Bonds	USD	0.9%	1.0%	3.5%	-7.5%
Emerging Market Bonds	USD	0.0%	0.6%	2.5%	-4.2%

Asset Class / Region	Currency	Week ending 14 April	Month to date	YTD 2023	12 months
		Cumulative returns			
Property					
US Property Securities	USD	-2.0%	-2.9%	-0.5%	-22.5%
Australian Property Securities	AUD	1.5%	2.3%	2.1%	-14.7%
Asia Property Securities	USD	1.6%	2.4%	-0.8%	-10.0%
Global Property Securities	USD	0.1%	0.0%	0.3%	-19.9%
Currencies					
Euro	USD	0.6%	1.0%	2.5%	1.5%
UK Pound Sterling	USD	-0.1%	0.5%	2.5%	-5.0%
Japanese Yen	USD	-1.2%	-0.8%	-2.1%	-5.9%
Australian Dollar	USD	0.5%	0.0%	-1.8%	-9.6%
South African Rand	USD	0.8%	-2.0%	-5.8%	-18.9%
Swiss Franc	USD	1.1%	2.1%	3.0%	5.3%
Chinese Yuan	USD	0.0%	0.0%	0.4%	-7.2%
Commodities & Alternatives					
Commodities	USD	1.6%	2.8%	-2.0%	-13.2%
Agricultural Commodities	USD	0.9%	0.2%	-0.2%	-12.2%
Oil	USD	1.4%	8.2%	0.5%	-22.7%
Gold	USD	-0.2%	1.8%	9.9%	1.7%
Hedge funds	USD	0.4%*	0.4%	0.4%	-2.9%

**as at 05/04/2023.*

Source: Bloomberg Finance L.P. Past performance is not indicative of future returns.

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