INVESTMENT TRUST NEWSLETTER

HISTORICAL REVIEW PART ONE 1996-2006

NOVEMBER 2016

We are delighted to be celebrating our 20th anniversary of publication for Investment Trust Newsletter and have decided to look back over some of the details of the journey so far. It shows us that the investment trust sector is a constantly shifting landscape, able to adapt and change as conditions and demands shift.

This is part one of a two-part review, covering the decade from our first issue in November 1996 to the end of 2006.

From the election of a new Labour government, to the launch of the 'its' marketing campaign, the activities of arbitrageurs, the split capital crisis, and the technology bubble, there is plenty to remember. Perhaps we can learn from the past as well, from previous cycles, fads, winners and losers.

1996 – The Very Beginning

Investment Trust Newsletter launched in November 1996, aiming to provide well-researched advice and to uncover much of the useful information not made easily accessible to investors. The first issue looked in detail at **Electric & General Investment Company** and **Electra Investment Trust,** both of which we recommended. The stockbrokers' research section contained research from Merrill Lynch, SBC Warburg, Credit Lyonnais Laing, James Capel, BZW, and NatWest Securities, none of which exist in the same form now. In December we met Brian Ashford-Russell, the manager of the new **Henderson Technology Trust** that was just being launched, and we also talked to Colin McLean of **Undervalued Assets Trust** and Andy Steel of **Ivory & Sime Enterprise Capital.**

1997 – Arbitrageurs and Vultures: Lots of Corporate Activity

In January we tried to pick some trusts reasonably immune from worries over the forthcoming UK general election. We looked at **British Empire Securities & General Trust,** emerging markets trusts, **Kleinwort Development Fund, Abtrust Scotland, TR Property,** and **East German Investment Trust.**

Investment trusts started the year well and we noted good gains from several of our early recommendations. Using director buying as a signal we examined the attractions of **Latin American Investment Trust, Glasgow Income Trust,** and **Brunner Investment Trust,** amongst others. We also looked at the specialist trust **Voyageur European Smaller Companies. Kleinwort Second Endowment Policy Trust's** 'S' share issue was oversubscribed.

In the early part of the year there was a burst of corporate activity with a bid for **Pilot Investment Trust,** a proposed merger between two Henderson income trusts, and US arbitrageurs buying into UK trusts sitting on wide discounts. There were also rumours of the imminent launch of two 'vulture' funds to target trusts, although they actually failed to arrive until closer to the end of the year. We made our first recommendation of the capital shares of a split capital trust, **Fleming Income & Growth.**

The UK stockmarket was unfazed by the new Labour government, elected in May, and there were some strong performances from emerging markets trusts. These helped the newsletter to get off to a strong start, with 26 of our first 30 recommendations in profit as at June 1997, with an average gain of 9.95%. We were making a lot of recommendations at this point, in tune with the prevailing bull market mentality that was also manifest in other ways. **Edinburgh Investment Trust** was one of several trusts to issue debentures to boost its gearing. The trustnet website indicated a lot of interest in the **First Russian Frontiers** trust. The launch of **Mercury Retirement Investment Trust** flopped and was scrapped though, and several trusts left the sector, including **Paribas French, Govett Global Smaller Companies,** and **Matheson Lloyd's Investment Trust.**

In September we revealed details of our *Meet The Managers* conference, to be held in November. The **Cairngorm Demutualisation Investment Trust** was launched with the aim of profiting from the change in status of building societies, although it did not raise as much capital as it had hoped. Harvard College built stakes in a number of emerging markets trusts. In the second half of the year there was a further flurry of corporate activity, with liquidations, changes of manager, buybacks and strategic stakes all in the news. **TR European Growth** took an 8.6% stake in **Continental Assets.** The Liverpool Partnership, a US arbitrageur, bought a 3.2% holding in **Healthcare Reform Trust** and Regent Fund Management bought 6.5% of **Gartmore Emerging Pacific. Mercury European Privatisation** bought back more shares; **Voyageur European** and **Kleinwort Overseas** restructured. **European Smaller Companies, BZW Convertible,** and **Saracen Value Trust** decided to wind-up. **Scottish National** issued rollover proposals.

In October 1997 stockmarkets had a sell-off and Asian trusts tumbled in value. We looked at some income trusts, **Fleming Income & Capital** income shares, and **Shires Income.** The new vulture fund **Advance UK** took its first declared stake in **British & American** and we felt there would be pressure for corporate action at **Govett Oriental,** where US arbitrageurs took their holdings up to 12.4%.

1998 – Some Volatility; Plenty of Action from Split Capital Trust Shares

In the newsletter at this point we regularly covered directors' dealings, and pointed out at the start of the year there was some good buying. As a speculation we recommended the capital shares of **Finsbury Income & Growth** at 15.75p, and we also recommended **Scottish Mortgage Trust,** noting it "typically trades on a discount of around 14%." Both HSBC James Capel and NatWest Securities were bullish on the investment trust sector, feeling there was value waiting to be unlocked.

In February we noted the very strong performance of capital shares in split capital investment trusts, saying we had recommended eight over the previous eleven months, with all showing double-digit percentage gains. The **Fleming Income & Growth** capital shares had jumped from 155p to 287p. We reiterated our recommendation of **Archimedes Investment Trust** capital shares at 642.5p, having first tipped them at 537p.

In March we were able again to report on strong performances from the capital shares of split capital trusts, with the **Finsbury Income & Growth** capital shares up nearly 50% already from our January recommendation. Both **Fleming Income & Growth** capital shares and **Danae** capital shares had doubled since recommendation. We recommended another capital share, this time in **Rights & Issues Investment Trust.**

Henderson Greenfriar announced plans to unitise, sending its shares up by 10%. We rated **Aberdeen European** a good 'each-way bet' at 136.5p to perform or restructure. Around the turn of the tax year there was a surge in directors' dealings and also in trust buybacks. Stockbrokers said that Budget changes to tax and to PEPs and ISAs should be good for the sector.

In May we produced a table of all of our recommendations to date, showing nearly five out of six in profit (of a total of 65) and an overall average gain of 25.6%. Three capital shares led the way with triple-digit gains. In June we interviewed Ian Rushbrook of **Personal Assets Trust,** Colin McLean of **Undervalued Assets Trust,** and Stephen White of **Foreign & Colonial Eurotrust.** We also wrote about the new **Drescner RCM Income Growth** split capital trust. Advance UK took a stake of 3.65% in **Martin Currie Moorgate** that we thought might be a prelude to some corporate action. **Healthcare Reform** announced its liquidation and **Govett Oriental** a restructuring.

The new vulture fund **Advance Developing Markets** took stakes in **Murray Emerging Economies, Morgan Grenfell Latin American, Taiwan Investment Trust** and **Edinburgh Inca.** There was a great deal more corporate activity too, with **Murray Ventures, Murray Split,** and **Exmoor Dual** all restructuring and **Govett American Smaller Companies** winding up. We suggested taking profits on a number of the capital shares that had performed so well. Nick Train left **GT Income Growth** following the takeover of the management group. Several Lloyd's insurance vehicles gave up their investment trust status.

In the first half of 1998, **TR European Growth** was the top performer, up by 52.3%. The trust was managed by Stephen Peak, who spoke at our Meet the Managers conference in November 1997. We would host the conference again in London this year.

In August we spoke to Max Ward, the manager of **Scottish Mortgage,** and in September, Peter Webb of **Eaglet Investment Trust,** where the shares were 118p. We launched a new website called trustnews, featuring a discussion group, but this was later abandoned. We looked at UK smaller companies trusts trading on wide discounts to net asset value of around 20%, and private equity trusts, which we called venture capital trusts back then.

It was a tough summer. In the three months to the start of October, the investment trust sector dropped by 23.6%, not helped by a widening of discounts as prices fell. The average discount was 15%, with many emerging markets trusts on 30% and UK smaller companies on an average discount of 22%. Even **Scottish Mortgage** went out to a 20% discount and **Henderson Technology Trust** to 23%. Capital shares of split capital trusts were hammered.

Sentiment recovered quite quickly in the autumn, as did activity. **Gartmore European** bid for **Aberdeen European,** the Liverpool Partnership arbitrageur increased its stake in **Foreign & Colonial US Smaller Companies** to 7%, and the £1bn-plus trust **Scottish Eastern** was targeted by Advance UK. We covered new split capital issues from Commercial Union and Jupiter, offering attractive potential returns.

1999 – Strong Performances and Discount Narrowing as the "its" Campaign Launches; But We Warn Repeatedly on Split Capital Trusts

We started the year with a few suggestions for self-select PEPs (that's personal equity plans in case you have forgotten). For beginners we suggested **Alliance Trust.** We interviewed Anthony Bolton, the manager of **Fidelity Special Values.** In February we wrote about the new **BGI Endowment Fund III,** investing in second-hand endowment policies. We liked its projected returns of 11.1% a year. Another split capital trust was also launched – **Govett Enhanced Income.** Picking out some discount and valuation anomalies, we alighted upon **Henderson Technology Trust** on a 16.1% discount, **Dresdner**

RCM Smaller Companies on a 36% headline discount (27% with debt at fair value), **Aberforth Split Trust** package on a 14.7% discount; and **Mercury European Privatisation** on a 17.7% discount. The annual review from the stockbrokers BT Alex Brown was somewhat sombre, saying that capital outflows from the sector had accelerated in 1998. **Henderson American Capital & Income** was the latest to wind up. **3i** made an unsolicited approach to **Electra Investment Trust.**

Our performance review in March noted an average gain since launch of 16%, ranging from a 134% gain on **Danae** capital shares to a thumping 60% loss on **East German,** which we had at least labelled as a gamble. We did particularly well from the split capital recommendations, nearly all of which we had since advised selling. Of eight new issues we liked, six were in positive territory, the best being **Henderson Technology Trust.** We suggested investors avoid the new split capital **Edinburgh Income & Value Trust.**

In April 1999 we reported on the AITC's big "its" initiative to launch a national advertising campaign, due to start in September. We hoped it might help to generate extra demand and reduce discounts. At the same time we noted that investment trusts were now able to buy in their shares without suffering advance corporation tax. Expecting more buybacks in the international generalist sector, we repeated our buy recommendation for **Foreign & Colonial** on a 14.5% discount to net asset value (with debt at fair market value). We also reiterated our buy recommendation for **Schroder Ventures International Trust.**

Schroder UK Growth changed its manager; **Mercury European Privatisation** decided to drop the privatisation part of its remit (and its name), and we rated it a buy. We noted several positions where arbitrageurs had built up stakes. In our review of the new split capital trust **Premier High Income** we said we had steadfastly declined to recommend the ordinary income shares of any splits, and we said "the incestuous nature of the split capital market worries us. In particular we do not like to see in any of these split capital trusts a statement that they will invest in the ordinary income shares of other split capital trusts." We also said "if the UK stockmarket falls … we think that this trust, and many other of the new split capital trusts, will struggle to return 100p for every 100p you have paid for your ordinary income shares." Those words would later prove prescient.

There were changes of manager for **Fleming Geared Growth, Fleming Claverhouse, Fleming Indian,** and **Fleming Asian.** Corporate activity continued, with **Dartmoor** making a hostile bid for **Pictet British Investment Company.** In July we recommended the new split capital **Close FTSE 100 Trust,** basically a split capital tracker, but reiterated our warning for both **Govett European Enhanced** and **Framlington Second Dual,** which said they would invest in the shares of other split capital trusts. We interviewed Dr Mark Mobius of **Templeton Emerging Markets.**

Markets were strong during this period, helping **Eaglet Investment Trust** shares to rise to 176.25p. Manager Peter Webb was still bullish. Share buybacks gathered pace, and about 50 trusts had started the process, the most enthusiastic proponents being **Fleming Overseas, Mercury European,** and **RIT Capital Partners.** The discount on **Mercury European** narrowed to 8%. Arbitrageurs increased their stake in **Foreign & Colonial US Smaller Companies** to 16.2%. **Martin Currie Japan** took over **Edinburgh Japan.**

In August the newsletter opened with the statement "we are nervous of the markets right now, and indeed as we write the FTSE 100 Index has fallen by more than 140 points to below the 6000 level. We fear for the capital entitlement of some of the highly geared ordinary income shares which we have not recommended, and suggest you avoid them." We focused on special situations, looking at **British Assets Trust** and **Acorn Income Fund.** We also sought out what we believed to be the safest and cheapest zero dividend share on the market – on **JZ Equity**. We suggested holders who might have doubled their money since launch in **Henderson Technology Trust** "could be forgiven for wanting to take some profit." We were not keen on the new split capital technology trust from Aberdeen, feeling it had high gearing and that its timing might be poor. **Martin Currie Moorgate** decided to wind up, as did **St Andrew Trust.** HSBC Securities recommended **Jupiter European** under its new manager Alex Darwall. Nils Taube retired as the principal investment adviser for the quoted element of **RIT Capital Partners.**

The "its" campaign to promote the industry got underway in the autumn, with high hopes that it might boost money flows into the large international generalists such as **Witan** and **Foreign & Colonial** in particular. Average discounts had already narrowed to 10.4%.

One of George Soros's Quantum Funds invested in **Foreign & Colonial Special Utilities** 'S' shares. **AIM Trust** and **Beacon Investment Trust,** two of our recommendations, soared in value, the former doubling in six months. **Henderson Technology Trust** moved to a 9% premium to net asset value amid much excitement in the sector. **Finsbury Technology** shares leapt 39% in two months; **Technology and Income Trust** announced its NAV was up by 42% in the first three months since launch. As the year drew to a close, so the bullish activity intensified, with trusts jumping by 9% in November, **3i** moving to a 48.9% premium and **Henderson Technology Trust** to a 20.8% premium. **Beacon Investment Trust** converted to open-ended status. **Gartmore Fledgling Index** succeeded in its bid for **Themis FTSE Fledgling Index.** Jupiter raised £400m for the launch of its **Dividend & Growth** investment trust – the largest ever split capital trust issue. 1999 was a dramatic year in which the FTSE Investment Trusts Index rose by 47.6%.

2000 – Arbitrageur Activity and More Technology

We felt the start of the new millennium seemed a decent time to recycle some money from the big winners of 1999 to some cheaper quality vehicles, or to carefully continue with monthly savings plans to build longer-term positions. Tom Walker took over as manager of **Martin Currie Portfolio Trust.** We noted director selling at the private equity trust **Thompson Clive.** In February we reported on the new **Amerindo Internet Fund,** which was initially hoping to raise £300m, later raised to £400m. Research from Deutsche Bank Benchmarking confirmed the outstanding performance of technology trusts in 1999. It also singled out **Fidelity Japanese Values, Fleming European Fledgling, Scottish Value Trust, Abtrust Scotland, Mercury European,** and **Electra** for praise.

The US arbitrageur Sierra Trading increased its stake in **Bankers Investment Trust** to 5%. The AITC's "Its" marketing campaign said it attracted 75,000 requests for information from consumers in its first two months, and revealed its intentions to continue the campaign for a second year. The excitement over technology stocks continued to build. The **Invesco**

Enterprise small cap trust announced plans to convert into a technology trust, **Invesco techMARK Enterprise; Fleming Geared Growth** planned to convert into the **Fleming Applied Science & Technology Investment Trust;** and **Hambros Smaller Asian Companies** into **The Asian Technology Trust.** Framlington launched the **Framlington NetNet.Inc** fund and 3i launched the **3i European Technology Trust.**

In March the backlash against technology stocks began, with the FTSE techMARK 100 Index falling by 29% in less than a month. There were some sharp price falls and some discount widening across the sector as well, encouraging more reconstructions and arbitrageur activity. **US Smaller Companies** decided to convert into an open-ended fund and **First Ireland** proposed a reconstruction. We wrote about the launch of another 'vulture' fund, **Value Catalyst Fund,** and on more aggressive moves from trust agitators. Shareholders requisitioned an EGM at **Govett Emerging Markets** to consider realisation options; Advance Developing Markets raised its stake in **Murray Emerging Economies** to 14.5% and also took stakes in **Morgan Grenfell Latin American** and **Dresdner RCM Emerging Markets.** Amongst the large international generalists, both **Bankers** and **Monks** found Sierra Trading on their share registers. There were calls for a reconstruction at **International Biotechnology Trust,** and the arbitrageur Millennium Offshore Partners also took a stake of 5.1% in **Montanaro UK Smaller Companies.**

An upheaval at the fund management group Jupiter, triggered by the departure of the boss, John Duffield, cast a shadow over some of its trusts, with **Jupiter Primadona** losing its premium and both **Jupiter Split** and **Jupiter Dividend & Growth** serving 'protective notice' on their management contracts. **Merrill Lynch Japan Enhanced Performance** launched, using derivatives in its structure. The managers of **Henderson Technology Trust** chalked up an impressive £43.1m performance fee for the year.

We met Robert Knapp of Millennium Partners to discuss its investment trust forays, which now included **Scudder Latin America.** Sierra Trading, meanwhile, topped up its holding in **GT Japan.** The technology sector showed it still had some life in it with the launch of **Close Finsbury Eurotech Trust.** The annual Credit Lyonnais Securities Europe yearbook argued that trusts should be more actively embracing share buyback programmes, which reduce discount volatility and can place a floor under discounts. Repurchases became viable after the abolition of Advance Corporation Tax in 1997.

In September 2000 we invited subscribers to switch to delivery by e-mail if they wished, taking delivery in the form of a PDF instead of a printed copy in the post. The colourful manager John Johnston resigned from fund managers Murray Johnstone, and as a result the discounts widened on **Murray Enterprise** and **Murray TMT,** two aggressively-positioned technology growth trusts. A vibrant new issue market saw new offerings from **Henderson European Micro Trust, Merrill Lynch New Energy Technology,** and **LeggMason American Assets.** In the autumn, global markets shuddered again, driven lower by Nasdaq in the US. Aberdeen raised £300m for a new split capital trust, **American Monthly Income Trust,** with its US equity element being managed by Katherine Garrett-Cox. **Independent Investment Trust** was also launched, while the shareholders of **Scudder Latin America** voted to wind up the trust. **Mercury European** rebranded as **Merrill Lynch European Investment Trust.**

At the end of the year we wrote about some more new issues being cued up for the start of 2001, including **Lindsell Train Investment Trust.** Research from Merrill Lynch showed that 129 trusts had bought in shares since the start of 1999, contributing to narrower discounts, averaging 10% (ex-private equity). Repurchases in 2000 were dominated by **Edinburgh Investment Trust, Scottish Mortgage,** and **Monks.** Credit Lyonnais Securities Europe advised holders to reduce exposure to battered technology trusts where they felt the premium ratings would erode.

2001 – Heavy Price Falls and The Split Capital Crisis

At the start of the year we noted that it had become harder to find discount bargains in the sector. Deutsche Bank data showed the average discount for all conventional trusts had narrowed to 5%, with some technology trusts including **Amerindo Internet Fund** still sporting large premium ratings. We fretted a little as well about the chase for income, wondering whether fund structures and hurdle rates could be stretched to provide tasty headline yields.

In our start of year round-up we noted the strong performance of Anthony Bolton's **Fidelity Special Values** trust. We also picked out **Eaglet Investment Trust** in the smaller companies sector, the **AIM Trust,** and **Murray Enterprise,** now reunited with its manager John Johnston at LeggMason Investors. Nick Train became the investment adviser to **Finsbury Growth Trust,** and **Capital Gearing Trust** manager Peter Spiller decided to leave Cazenove and set up his own boutique firm – the board signalled they intended to follow him.

The US arbitrageur ST Partners tried to force tender offers at some big international generalist trusts, **Scottish Investment Trust, Murray International,** and **Foreign & Colonial Investment Trust.** Separately, **Beta Global Emerging Markets** decided to wind up. **GT Japan's** board switched the management contract from Invesco to Sloane Robinson.

In February we reiterated our recommendation of **North Atlantic Smaller Companies Investment Trust** as a long-term buy at 662p. The furious pace of reconstructions and winding-ups continued, particularly in the emerging markets sector that had earned the unfortunate nickname of 'submerging' markets. A review of the private equity sector by UBS Warburg rated three trusts as strong buys, **Candover, F&C Private Equity,** and **Mercury Grosvenor.** The **Framlington NetNet.Inc** split capital trust paid back £40m of borrowings, leaving it with just £7.8m of assets, just a year after launching with £100m. We said it was vying with **Amerindo Internet Fund** for the title of highest-profile technology disaster.

We shared the key points of an article by Dr Andy Adams and Robin Angus in *Professional Investor* magazine that warned of the risks of 'barbell' investment trusts in the split capital sector. Problems had already arisen due to high gearing levels in falling markets, but this article warned of higher than realised costs, questioned whether distress calls would continue to be met, and also criticised the 'magic circle' of managers investing in each others' trusts. We spoke to some bankers who lend money to investment trusts and found they preferred traditional trusts too. None of this stopped BFS Investments from launching a barbell split capital trust called **BFS US Special Opportunities Trust.** Not all trusts were finding fund-raising easy at this time – there were stumbles for **3PC Investment Trust** and the **First Housing Investment Trust** – but the volume of new issuance remained strong.

For investors wishing to obtain data on split capital shares we highlighted a new website, www.splitsonline.co.uk, run by Aberdeen Asset Management and Fundamental Data. Research at this time indicated that 40% of Britons had access to the internet. In July we reported on the premature end for the AITC's "its" marketing campaign, which had limited success in attracting large numbers of new private investors to the sector. The following month we noticed that Credit Lyonnais Securities Europe had changed its tune about buybacks, arguing they had contributed to falling liquidity in the sector, leading to the withdrawal of Merrill Lynch from investment trust market-making.

The FSA warned fund managers to strengthen the risk warnings attached to split capital trusts as Aberdeen's **European Technology & Income Company** saw its asset value slump after sharp falls in both its technology portfolio and its high yield bond portfolio, exacerbated by high gearing. The stockbroker Cazenove warned of the possibility of a systemic collapse in the 'barbell' part of the split capital sector. Other trusts, such as **Govett High Income** and **LeggMason Investors Income & Growth** had to issue new equity to reduce the risk of breaching loan covenants, yet in the same month the new **BFS Managed Properties** split capital trust raised £200m from a new launch and Britannic Asset Management launched a new split offering high headline yields. Splits had grown from 8.8% of the investment trust sector in 1994 to 19.9% by August 2001, accounting for £14.3bn out of £71.9bn of assets.

UBS Warburg noted that technology funds had reverted to trading on discounts. **GT Japan** decided to reconstruct and **Aberdeen Emerging Economies** received a winding-up requisition. Trust prices fell heavily over the summer and then tumbled again after the September 11th terrorist attacks in the US. Split capital and technology trusts both took a pounding. The first nine months of 2001 saw investment trusts fall on average by nearly 29% before a fourth quarter rally restored some value.

Peter Webb of Unicorn Asset Management had built a strong reputation with this top-performing **Eaglet Investment Trust** and launched another trust called **Falcon Investment Trust** to invest in mid-cap stocks. More split capital trusts raised capital to improve their asset cover. Ben Rogoff took over as manager of **Murray TMT.** Aberdeen closed its Fund of Investment Trusts unit trust after its assets dropped from £90m to £8.1m. Its **European Technology & Income** split was taken over by the **Technology & Income Trust.**

2002 – A Year of Change in Tough Market Conditions

The year started with some licking of wounds after a terrible 2001, and the FSA issued a discussion paper on the failings of split capital trusts, followed by a series of visits to fund managers. We hosted our third 'Meet the Managers' conference in London. **Henderson Eurotrust** bid for **Charter European Trust,** which rebuffed its proposals and ultimately fended it off successfully with its own reconstruction plan. The board of **Britannic Smaller**

Companies introduced a symmetrical performance fee that penalised poor performance as well as rewarding good. The performance of **Eaglet Investment Trust** started to dip. Stockbrokers began to trawl through the wreckage of the split capital sector – sometimes dubbed the spilt capital sector – to hunt for bargains from better quality trusts. We recommended shares in **Aberforth Split Level Trust** which we felt was being unfairly punished for its structure. Collins Stewart launched a **Zero Dividend Recovery Fund.**

Michael Moule, the manager of **Bankers** and the industry's longest-serving manager, announced he would retire and hand over to Alex Crooke. The £1.4bn **Edinburgh Investment Trust** put its management contract out to tender, a blow for Edinburgh Fund Managers. It chose Fidelity as its new manager. Prices fell again in the summer, pushing some split capital trusts to their final sad conclusions. Some trusts such as **Aberdeen High Income** called in the receivers, the fourth Aberdeen split capital trust to do so. A House of Commons select committee quizzed the AITC head Daniel Godfrey, three executives from Aberdeen Asset Management, and John Tiner of the FSA.

By October the average discount had widened out to 15% in a sector battered by weak equity markets and the split capital crisis. Technology trusts and UK smaller companies trusts were particularly sharp fallers, including **AIM Trust, Eaglet Investment Trust,** and **Polar Capital Technology.** Neil Hermon took over as manager of **Henderson Smaller Companies** and John Pennink took over from John Walton at **British Empire Securities & General Trust.** A number of trusts decided to reconstruct, including **Baring Emerging Europe, Fleming Technology Trust, Investec Extra Income,** and **Invesco Tokyo Trust.** Arbitrageurs targeted **Amerindo Internet Fund.** At the end of the year the **Standard Life Investments Property Income Fund** launched with a target yield of 6.5%, but was unable to reach its minimum funding target in depressed conditions.

2003 – More Corporate and Regulatory Activity as Markets Start to Recover

The FSA proposed new rules for investment companies in the wake of the split capital crisis, with limits on cross-holdings and stricter requirements about the independence of directors. Markets continued to fall as sentiment was hurt by the impending Iraq war, with UK smaller companies trusts suffering badly, and an AITC survey found that 51% of investors were not planning to use their ISA allowances. **Witan Investment Trust** addressed the benefits of staying invested in its marketing literature, quoting David Brent, the fictional star of the television series 'The Office', who said "quitters never win."

Mark Barnett became manager of **Keystone Investment Trust,** which moved from Merrill Lynch to Invesco Perpetual. **Jupiter Dividend & Growth** purchased a two-year FTSE 100 put option aimed at protecting downside capital protection. **LeggMason Investors Enterprise,** a popular trust at the height of the technology boom, shifted to Schroders with a new UK mid and small cap mandate. **Mercury Grosvenor Trust** renamed as **HgCapital Trust.** Markets rallied in the spring and Anthony Bolton, the manager of **Fidelity Special Values,** proclaimed the start of a new bull market, but Ian Rushbrook of **Personal Assets Trust** remained resolutely bearish. Discounts narrowed as investors started to buy again, and there was a rash of corporate activity with a whole group of tenders, reconstructions and offers. Trusts affected included **Aberdeen Latin**

American, AIM Trust, 3PC, Henderson Absolute Return Portfolio, Liontrust Winners, New Opportunities Investment Trust, Jubilee Investment Trust, Piccadilly Growth Trust, Smaller Companies Investment Trust, Special Utilities Investment Trust, and **Schroder Emerging Countries.** Newspaper reports suggested that **Edinburgh Small Companies** was preparing for a change of management company. We recommended **Acorn Income Fund** at 77p and also took a look at geared trusts well positioned to motor in a recovery.

After **Edinburgh Small Companies** moved its management contract to Standard Life Investments and **Edinburgh Worldwide** moved to Baillie Gifford, Edinburgh Fund Managers was taken over by Aberdeen Asset Management. Govett, the manager of six trusts, sold its management contracts to Gartmore. We reiterated our recommendation of **Acorn Income Fund** at 95.5p. A clash erupted at **Caledonia Investments** between the board and activist shareholders seeking a realisation of the portfolio.

From December 2003 trusts could start to hold their own shares in 'treasury' for later re-sale. **ISIS Property Trust** was launched to great demand with an initial yield target of 7% and was later joined by **Standard Life Investments Property Income Trust**. The Times newspaper recommended **Amerindo Internet Fund** shares at 14.75p. Both **Martin Currie European** and **Henderson European Micro** received 'perform or else' ultimatums from their boards. **Witan Investment Trust** said it planned to appoint a chief executive and to allocate assets to specialist managers. **Scottish American Investment Trust,** known as SAINTS, moved from First State Investment Management to Baillie Gifford. We reported on **JPMorgan Indian,** whose shares had nearly doubled in six months.

2004 – Japanese and UK Smaller Companies Trusts Sprint Ahead and new Property Income Trusts Arrive

The year began with an air of optimism after a decent 2003 and a sense that more orderly markets were giving some trusts a breathing space to reconsider their positions. A number of individual manager changes were followed by some corporate manoeuvres, with the arbitrageur Millennium Partners instigating wind-up proposals for **Amerindo Internet Fund, Merrill Lynch World Mining** making a bonus issue of warrants, **Caledonia Investments** creating an exit for its disgruntled minority, and **Merrill Lynch European** deciding to reconstruct. Credit Lyonnais exited from the investment trust sector.

Japan performed very strongly in the first quarter, pushing some Japanese smaller companies trusts up sharply. By the time of the May newsletter, **Atlantis Japan Growth, Invesco Japan Discovery,** and **Fidelity Japanese Values** had all doubled their assets over twelve months. Geared smaller companies trusts in the UK were also performing well, with **Active Capital Trust, Eaglet Investment Trust, Gartmore Fledgling** and **Invesco English & International** all growing their assets by at least 70% over twelve months. We suggested some caution might be prudent at these levels. Chris Turner and Marcus Phayre-Mudge, the managers of **TR Property,** resigned from Henderson Global Investors, triggering the board to give notice to terminate its management contract and undertake a selection process for a new manager. The FSA was close to concluding its enforcement against firms involved in the split capital crisis, but the mediation process stumbled over the £350m it was seeking in compensation payments.

Ruffer Investment Company launched, along with **Insight Foundation Property Trust.** The fund management companies ISIS and F&C announced a merger to create the fourth largest asset manager in the UK. Never ones to miss out on a topical link, the AITC conducted an 'Investment Trust Olympic Games.' In the ten year consistency decathlon, **Fidelity European Values** beat off **Aberforth Smaller Companies** and **Candover Investments** to take the gold. In the sprints, Japanese trusts swept the board, with **Invesco Japan Discovery** on top of the podium. We recommended **Law Debenture Corporation** shares. **Scottish Investment Trust** and **JPMorgan Fleming Claverhouse** decided to pay back expensive debt, and the management contract for **TR Property** was awarded to Thames River Capital, where the previous management duo had relocated.

More property income trusts arrived, promising yields of around 6%. We arranged access to the placing for **Invesco UK Property Income Trust**. **Henderson Electric & General** gave the international generalists sector a shock wake-up call by announcing a change of management company to Taube Hodson Stonex, dropping the 'Henderson' part of its name at the same time. A series of presentations by international generalists trusts, hosted by UBS, suggested guarded optimism for the outlook.

The whirl of reconstructions and switches in management mandates kept on spinning. 3i decided to seek an exit from its management contracts for **3i Smaller Quoted Companies Trust** and **3i European Technology,** and plans to move both trusts to DWS – the investment trust management arm of Deutsche Asset Management – were abandoned when DWS announced its own strategic review. **3i Bioscience** moved to Schroders. **Aberdeen Convertible Income** became **New City High Yield Trust.** A formal performance target was imposed on the managers of **Charter Pan European,** with the threat of a wind-up if the target was not met, and the board effectively issued a similar ultimatum to **F&C Emerging Markets Investment Trust. Alliance Trust** and **Second Alliance Trust** rejoined the AITC after a three-year absence. The Treasury issued a consultation paper seeking views on whether there was a need to introduce additional regulation for investment trust companies. At the very end of the year, the FSA and 18 firms involved with split capital trusts agreed a compensation package of £194m for investors.

2005 – Rising Markets Attract More New Issues

F&C Commercial Property Trust was launched to swell the assets of an already popular sector. In contrast, the large shareholders of **3i Bioscience** wanted to exit and the trust announced reconstruction proposals. **3i Smaller Quoted Companies** moved to Merrill Lynch, and **F&C Income Growth** and **F&C Capital & Income** entered into merger discussions. **Gartmore Global Opportunities** came under siege from arbitrageurs. The early part of the year saw plenty of personnel changes at a number of trusts. Dresdner Kleinwort Wasserstein's annual review noted that board initiatives had helped discounts to narrow towards the 9% 'glass ceiling' that had been in place since the mid-1990s. The broker thought markets might struggle this year after two years of good gains.

After a few periods of lacklustre performance, **Foreign & Colonial Investment Trust** made a partial shift towards a multi-manager approach. **F&C Pacific Investment Trust** replaced F&C Management with Aberdeen Asset Managers and Nomura Asset Management and planned to change the name to **Witan Pacific.** **Perpetual Income & Growth** bid for **Securities Trust of Scotland,** a rare hostile takeover bid in the sector, but did not ultimately succeed. **AXA Property Trust** became the latest addition to a burgeoning sector. **Finsbury Life Sciences** appointed OrbiMed Advisors as its new investment adviser. **Jupiter Global Green** just survived a liquidation vote. We met the managers of **Polar Capital Technology Trust** when the shares were 185.5p – their message was "get ready to buy." UBS suggested caution on private equity trusts, as they saw a less buoyant outlook and some relatively expensive valuations.

The founders of Amerindo Investment Advisers were arrested in New York on alleged fraud charges, so the board of **Amerindo Internet Fund** served notice on the managers and the trust was liquidated when it became clear there was insufficient support from shareholders for it to continue. **Deutsche Equity income** also served protective notice on its managers, DWS. F&C purchased Martin Currie's private equity fund of funds business and changed the name of **Martin Currie Capital Return Trust** to **F&C Private Equity Trust.** **Taverners Trust** became **Midas Income & Growth Trust.**

By mid-year the FTSE 100 Index was rising, up and away from the 5000-mark that had been something of a magnet. The rash of property funds spread to Bulgaria, although we had reservations about the **Lewis Charles Sofia Property Fund.** Over in Japan, **Atlantis Japan Growth Fund,** managed by Ed Merner, was a strong performer, trading on a premium to NAV. **City Merchants High Yield** agreed a merger with **Exeter Selective Assets Investment Trust.** At the start of October The Times newspaper reported that Fidelity was preparing to launch its first new investment trust in ten years, aiming to raise £80m-£100m for an emerging markets trust for launch in the first half of 2006. **ING UK Real Estate Income Trust** was the latest big launch in the property sector, targeting a 6.25% dividend yield. The fourth quarter saw a real flurry of new issues in specialist fields, including **Aberdeen Asian Income Fund, Merrill Lynch Commodities Income Investment Trust, The Ukraine Opportunity Trust, Morant Wright Japan Income Trust, India Capital Growth Fund, and AcenciA Debt Strategies.**

Presentations from several well-known UK managers, including Anthony Bolton, Mark Barnett and Job Curtis, indicated that while British shares were some way into the bull market, they could have further to go. **Lowland** won the award for best UK trust at the annual Investment Week awards in London, with **British Empire Securities** winning the award for best global trust and Baillie Gifford picking up the prize for best group. **Baillie Gifford Japan** snatched the Japan title from **Atlantis Japan Growth,** which had won for the previous four years. The Nikkei 225 Index moved ahead strongly to round off a good year.

2006 – The Sector Diversifies Into Alternative Assets

Rounding up some fund managers views for the year ahead, in the January 2006 newsletter, we quoted Bruce Stout, the manager of **Murray International.** He said "unprecedented credit-fuelled consumer spending and irresponsible fiscal policies have enabled the US and UK economies to grow only by living well beyond their means. Such debt-dependency has produced unsustainable deficits that history tells us are exceedingly painful to correct. We believe the post credit-binge hangover is rapidly approaching for such 'Debtor Nations.'" How prescient his words would become, though not just yet. Most fund managers expected a good year ahead.

The JPMorgan trusts started to drop the word 'Fleming' from their titles. Ben Rogoff took over from Brian Ashford-Russell as manager of **Polar Capital Technology Trust.** Investment trusts seemed to be moving into previously unchartered waters, including infrastructure with the launch of **HSBC Infrastructure Company,** targeting a 5.75% yield. WINS Investment Trusts said the largest fund facing a high probability of corporate action in 2006 was **JPMorgan Fleming Continental European,** in which the arbitrageur Carrousel Capital held a 13% stake. The broker had a long list of trusts with large arbitrageur stakes on their shareholder registers.

A number of smaller investment companies listed on the AIM, including **Eastern European Property Fund**, **Aurora Russia,** and **Puma Brandenburg.** Hedge funds were also in vogue, with new listings from companies such as **Dexion Alpha Strategies** and **PSolve Alternatives.** **Alliance Trust** and **Second Alliance Trust** finally decided to do the obvious thing and merge, forming the largest generalist investment company on the London Stock Exchange. Simon Gergel took over from Nigel Lanning as manager of **Allianz Dresdner Income Growth.** Noting the rise of AIM-listed and Guernsey-domiciled investment companies, the Association of Investment Trust Companies (AITC) announced plans to change its name to the Association of Investment Companies (AIC). The new issue market continued full steam ahead, including **ING Global Real Estate Securities, RCM Technology Trust, Jupiter Green Investment Trust, the Close AllBlue Fund, Canadian Income Trusts Investment Company, VietNam Holdings,** and **Macau Property Opportunities Fund.**

In May, markets fell sharply, with UK and Japanese equities suffering badly. It felt like a correction after three years of fairly solid gains. In March The Financial Times had pointed out that "not since the 1950s has the London stock market enjoyed a longer uninterrupted bull run." **JPMorgan Fleming Continental European** announced restructuring proposals. **Acorn Income Fund** scraped through a continuation vote.

We noted in September that the sector was strong, with average discounts standing at just 2.2% (or 8% excluding private equity). New managers were coming into the sector, with new AIM listings helping the industry to grow. It was a busy time for two-way capital flows. In the year to the end of August, new inflows amounted to £6.7bn from fund launches, extra gearing, 'C' share issues and warrant exercise, with £4.1bn leaving the sector through capital distributions, winding-ups and liquidations, tender offers, redemptions, and share repurchases.

Standard Life Investments Property Income Trust was trading on a large premium of 8.4%, and we questioned its sustainability. There were warnings of slower future returns from UK property. **Edinburgh UK Smaller Companies Tracker** and **Resources Investment Trust** both decided to wind-up. **Gartmore Asia Pacific** switched its management mandate to Aberdeen. More alternative assets trust arrived, including **Babcock & Brown Public Partnerships, Prospect Epicure J-REIT Value Fund,** and **CQS Rig Finance Fund.** At the annual end-of-year awards sponsored by Investment Week, **British Empire Securities & General** won in the global category again, making it four years out of five.

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