QuotedData

Quarterly report | Investment Companies

20 April 2015

First Quarter of 2015

QuotedData news

This is the first quarterly report we have published – we hope it is useful and you like the format. The information and layout is based on our regular monthly updates on the investment companies sector.

New research

This quarter we published research on Strategic Equity Capital (Different in a good way), Altin (An alternative investment), Premier Energy & Water (Value in emerging markets) and Japanese investment companies (is Japan on the road to recovery?). You can find all these reports and more on the website.

Income

We have been gradually expanding the information we provide on income – low interest rates have depressed returns on many assets yet demand for income is high and may increase now that pensioners can opt to invest their pension pot in something other than an annuity. We have added a section on our website that will build to a database of dividend announcements by investment companies. This is available on an excel spreadsheet which is updated daily – useful if you are trying to keep track of the income your portfolio is generating. We will publishing a special report on funds designed to pay income to investors shortly.

Roadshows

We have started a programme of talking to advisers about investment companies to help broaden and deepen their knowledge of the sector (if you are an IFA we may be coming to a town near you soon – CPD points are available – contact us for more details). We are also taking some of our clients to meet professional investors around the country and we plan to be helping some funds raise fresh capital from investors in Q2 2015.

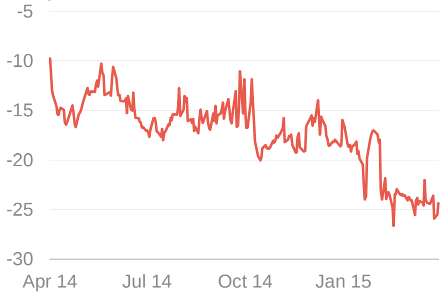
Sector average discount

Time period 01/04/2014 to 31/03/2014

Over the 12 months to the end of March 2015, the average discount across the whole of the investment company sector moved within a range of c9% to c12% - narrowing over Q2 2014 and gradually widening thereafter.

Natural resources discount

Time period 01/04/2014 to 31/03/2014



The area of the market where discounts widened the most on average was the Commodities and Natural Resources sector as a hoped for rally in commodity prices did not materialise and then the oil price fell sharply.

More information about the funds mentioned in this report is available on our website. If you are reading this online, there are links embedded in the document that will take you through to the relevant webpage.

Performance Data

A few themes stand out from the performance data. On the positive side of the tables in figures 1 and 2, it looks as though investors are starting to believe that, one year on after the events of Maidan Square, the situation in Ukraine is on the mend. This is most pronounced in the recovery of Dragon Ukrainian's share price but Russian funds also did well over the first three months of 2015. There is some way to go however. JPMorgan Russian's share price, for instance, is still 30% below where it was at the end of 2013.

Japanese and Biotech related investments also did well. We published an extensive note on Japan during the quarter in which many of the investment managers running Japanese investment companies talked about the successes and failures of government efforts to stimulate the economy. Most argued that many Japanese companies can thrive regardless of the sluggish economic environment. With regards to the Biotech sector, its success also seems to be a reflection of investors favouring companies that they believe can grow their earnings without much help from the global economy. The sector has also benefited from a bout of merger and takeover activity.

Looking at a few of the other investment companies that did well in Q1, Tejoori is a tiny, Shari'a compliant, investment company. There wasn't much news in Q1 that could have justified the share price move. Sticking with very small investment companies, SVM UK Emerging's share price rise seems to be largely the consequence of an improvement in its rating, it still trades on a 21% discount however. CATCo provides reinsurance covering the very worst disasters – things like the Japanese earthquake or Hurrican Sandy. Not much happened that triggered losses in the contracts it wrote for 2014 and, during the quarter, it reported good results. Riverstone Energy is investing in a variety of oil and gas projects. Its share price had suffered as investors worried about the effect of falling energy prices on its business but its results, published half way through the quarter, showed a rising net asset value.

Figure 1: Best performing funds in price terms in Q1

	%
Dragon Ukrainian Properties	+39.5
Tejoori	+33.0
Aurora Russia	+28.6
JPMorgan Russian	+28.1
SVM UK Emerging	+25.5
JPMorgan Japanese	+23.2
Riverstone Energy	+22.8
International Biotechnology	+21.8
Schroder Japan Growth	+20.9
TR European Growth	+20.8

Source: Morningstar

Figure 2: Best performing funds in NAV terms in Q1

	%
JPMorgan Russian	+31.6
CATCo Reinsurance Opportunities	+23.7
Biotech Growth	+22.8
Elephant Capital	+22.1
International Biotechnology	+22.1
JPMorgan Japanese	+21.8
Baillie Gifford Shin Nippon	+21.6
Baillie Gifford Japan	+20.7
Aberdeen Japan	+18.5
Worldwide Healthcare	+17.2

Source: Morningstar

On the negative side, looking at figures 3 and 4, a number of very small funds that are close to the end of their life show up in the tables. Dealing with some of these:

- Black Sea Property returned just about all its capital to its shareholders after selling off the last of its portfolio. It has just received a new lease of life however. A new set of shareholders have been recruited and the fund intends to rebuild a portfolio of Bulgarian property.

- Ottoman Fund was hit by a fraud within a Turkish subsidiary. They think they have identified the person responsible and are trying to retrieve their cash.
- International Oil & Gas Technology is now suspended pending the sale of its largest asset.
- Invista European has been selling off property to cut its mountain of debt but the prices it has been achieving are well below valuation
- Cambria Africa threatened to delist its shares and then changed its mind as it brought in a new investor.
- The board of ARC Capital was replaced in a shareholder vote, the broker resigned. To date the new Board has not announced its plans for the company.
- Trading Emissions is embroiled in a number of arbitration proceedings and is racking up legal fees.

Funds invested in the commodities and natural resources sector had a trying time as hopes of a recovery in the sector's fortunes were dashed. The weak oil price also took its toll. Brazil is one country whose economy is heavily exposed to the resources sector. Its problems have been compounded by a corruption scandal circling the government.

Figure 3:Worst performing funds in price terms in Q1

	%
Black Sea Property	-66.6
Ottoman Fund	-61.9
International Oil & Gas Technology	-53.3
St. Peter Port Capital	-42.0
Cambria Africa	-38.9
Avanti Capital	-37.0
Praetorian Resources	-36.4
Global Resources	-35.4
ARC Capital	-35.4
Trading Emissions	-29.6

Source: Morningstar

Figure 4: Worst performing funds in NAV terms in Q1

	%
Ottoman Fund	-33.9
New City Energy	-17.2
Cambium Global Timberland	-15.5
Invista European Real Estate	-14.6
JPMorgan Brazil	-11.0
Tiger Resource Finance	-9.0
Taliesin Property	-8.8
Terra Catalyst	-6.9
Globalworth Real Estate	-6.8
Treveria	-6.8

Source: Morningstar

Significant rating changes

The list of funds that got significantly more expensive in figure 1 is dominated by property companies. Investors in search of yields have been piling into property and this is driving up asset values. The published net asset values can be quite out of date and so, today, may be underestimating the true asset value which could in turn mean that the premiums aren't as high as they look.

It does seem as though demand for shares in many property investment companies and REITs has far outstripped supply however. New issues of stocks from some of these funds could put pressure on these ratings in the future.

The search for income has also benefited the aircraft leasing companies, including the two Doric Nimrod funds featured in figure 5. Investors in Riverstone Energy, who had been unnerved by the falling oil price, seem to have been reassured by that company's results. Russian and Ukrainian investment companies have been recovering as tensions between the two have eased a little.

The list of funds getting cheaper in figure 6 includes a number of resources companies. The general malaise in that sector has also affected sentiment toward

Canada, which is a big producer of natural resources, and this has had an impact on Middlefield Canadian. The private equity company, Candover, is another casualty of falling natural resource prices – one of its largest investments is oil services company, Expro international.

St Peter Port Capital has been hit by the bankruptcy of one of its investments, Gourmet Express. Globalworth is one of the largest investors in the Romanian office market. It is not particularly well known however and this might account for its widening discount. Investors have been deserting Better Capital 2012 since the collapse of City Link at Christmas 2014. It is not clear to us why investors seem to be losing faith in NB Distressed Debt however.

Figure 5: More expensive relative to NAV - notable changes to discount (-ve) or premium (+ve)

	31/03/15 %	31/12/14 %
Green REIT	+34.4	+6.2
Taliesin Property	+37.3	+10.3
Redefine International	+58.8	+43.9
Riverstone Energy	+14.0	-3.0
Standard Life Inv. Property Inc	+17.4	+3.7
Doric Nimrod Air 2	+25.8	+13.3
F&C UK Real Estate Invest	+15.1	+3.5
Picton Property Income	+9.5	-1.5
Doric Nimrod Air 3	+25.3	+14.8
Aurora Russia	-42.0	-52.1

Source: Morningstar

Figure 6: Less expensive relative to NAV - notable changes to discount (-ve) or premium (+ve)

	31/03/15 %	31/12/14 %
St Peter Port Capital	-68.5	-45.8
Praetorian Resources	-60.6	-38.7
Globalworth Real Estate	-25.5	-4.4
Global Resources	-67.9	-52.1
Candover	-39.7	-27.0
Better Capital 2012	-35.9	-25.9
Middlefield Canadian	-11.4	-1.7
NB Distressed Debt	-12.2	-2.4
Macau Property Opportunities	-31.6	-22.0
Geiger Counter	-24.4	-14.9

Source: Morningstar

Money in and out of the sector

Coming in:

We reckon the sector expanded by more than £1bn over the course of Q1 2015. The largest amount of money, £250m, was raised by P2P Global Investments via a “C” share issue. This fund is investing in the fast growing peer to peer lending sector. We saw one competitor to P2P launched during the quarter; VPC Specialty Lending Investments raised £200m. Another fund, Ranger Capital is raising money now and GLI Finance has said that it also intends to launch a fund. The bulk of money raised by these funds is being lent, through a variety of on-line debt marketplaces, at fairly high interest rates and the funds are forecast to pay high levels of dividend.

The two other new issues during the quarter were Sequoia Economic Infrastructure, which is lending money against infrastructure projects and Gabelli Value Plus+ which is being invested in a portfolio of smaller US companies. These two funds raised £150m and £101m respectively.

We should also mention Tritax Big Box REIT which raked in £175m, Empiric Student Property £85m, Picton Property Income £42m and a clutch of solar energy companies – Renewables Infrastructure, NextEnergy Solar and Foresight Solar – that, collectively, brought in £200m as they rushed to get money invested in solar projects before government subsidies fell on 31 March.

Going out:

The funds that we lost during the quarter were CQS Diversified, Lyxor Focus Fund, BlackRock Hedge Selector and PXP Vietnam. The first three of these were hedge funds, which speaks to the unpopularity of this part of the market. This is underscored by the presence of funds such as Acencia Debt Strategies, BH Marco, BH Global and BlueCrest All Blue on the list of fastest shrinking funds in Q1 2015. We wondered, in note we wrote on Altin during the quarter, whether this trend has gone too far.

The fund handing back the most money was SVG Capital, which gave back around £90m to its shareholders, largely funded by the sale of its investment in Hugo Boss. The funds that bought back the most shares, in an effort to control their discounts, were Monks and Mercantile. Monks ended up replacing its investment manager.

Figure 7: Funds raising capital in Q1

	£m
P2P Global Investments	250
VPC Speciality Lending Investments	200
Tritax Big Box REIT	175
Sequoia Economic Infrastructure	150
Renewables Infrastructure	102
Gabelli Value Plus+	101
Empiric Student Property	85
NextEnergy Solar	61
Picton Property Income	42
Foresight Solar	36

Source: Morningstar, QuotedData

Figure 8: Funds returning capital in Q1

	£m
SVG Capital	90
Acencia Debt Strategies	65
Monks	36
Mercantile	31
BlackRock North American Income	25
Ashmore Global Opportunities	25
Northern Investors	19
British Empire Securities	18
Qatar Investment Fund	15
Templeton Emerging Markets	15

Source: Morningstar, QuotedData

Major news stories

Portfolio developments

- **International Biotechnology** sold an unquoted investment, Convergence Pharmaceuticals, for 15x what they'd paid for it
- **3i Infrastructure** sold its stake in Eversholt rail for £358m and reinvested some of the proceeds in oiltanking operations in Belgium and the Netherlands
- **Marwyn** began the process of rebuilding its portfolio in earnest as one new vehicle, Haversham,, was linked to a bid for British Car Auctions and they invested in Zegona Communications
- **GLI Finance** sold its stake in Fair Oaks Income, finally severing the connection with its original CLO loans business

Corporate News

- Brooks MacDonald's proposals for **Origo Partners** were rejected by other shareholders
- **Baker Steel Resources** unveiled its expansion plans and grew through a series of stock swaps
- **JZ Capital Partners** proposed changes to its investment policy and followed this up by growing its new property portfolio
- **ARC Capital**'s Board was ousted

- The UK Government sold their stake in **Greencoat UK Wind,** concluding a successful effort to get the renewables infrastructure sector off the ground in the UK
- Sherborne threatened to call another EGM on **Electra** and raised £100m to fund further investment in the fund despite having hads its previous proposals comprehensively rejected. **Electra** cut its fees as part of its review of its structure implemented in response to Sherborne
- **JPMorgan Claverhouse** appointed a Board apprentice – this is a scheme designed to help broaden the diversity of the boards of UK companies
- **Alliance Trust** was requisitioned by Elliott Advisers who asked for three new directors to be appointed. As we go to press, the EGM is scheduled for 29 April and the outcome is getting harder to predict

Managers

- **Scottish Mortgage** appointed Tom Slater as joint manager of the fund
- **North American Income Trust** appointed new joint managers after Paul Atkinson returned to the UK
- **Origo Partners** externalised its investment management
- Dik Blewitt is the new portfolio advisor for **Carador Income**
- Alisdair McKinnon is **Scottish Investment Trust**'s new manager
- James Hart is moving from **The Cayenne Trus**t to **Witan** – Cayenne will start to wind down in coming months
- **NB Distressed Debt** got two new co-portfolio managers, replacing Patrick Flynn
- **BlackRock Throgmorton** said Ralph Cox was stepping down as co-manager
- Nitin Bajaj is replacing John Lon as manager of **Fidelity Asian Values**
- Charles Plowden is replacing Gerald Smith as manager of **Monks**

Income

There are a number of investment companies that pay out quite high levels of income relative to other investments. Appearances can be deceptive however as some of these are, in one way or another boosting the dividend by paying out more than they receive in revenues after expenses – in effect distributing capital. Figure 9 shows the list of highest yielding funds at the end of March 2015. We have tried to exclude from this list funds that are shrinking deliberately by handing back capital to shareholders.

Figure 9: Highest yielding investment companies

	Yield %
Jupiter Dividend & Growth	24.7
Carador Income Fund	9.9
DP Aircraft One	9.5
British & American	9.3
Doric Nimrod Air Two	9.1
Doric Nimrod Air Three	8.7
Doric Nimrod Air One	8.7
MedicX	8.6
Premier Energy & Water	7.3
CQS High Yield	7.3

	Yield %
GCP Infrastructure	7.2
BlackRock Commodities Inc	7.2
HICL Infrastructure	6.9
Dragon Ukrainian	6.8
Real Estate Credit	6.7
Invesco Perpetual Enhanced	6.7
Chenavari Capital Solutions	6.7
Duet Real Estate Finance	6.7
BlackRock World Mining	6.4
Target Healthcare REIT	6.3

Source: Morningstar, QuotedData

Jupiter Dividend & Growth is a split capital company that will wind up in November 2017. The way its structure works (it has a combination of ordinary income shares, common shares and zero dividend preference shares), its ordinary income shares have almost no net asset value right now but are entitled to a disproportionate share of the income generated by the company.

Carador Income invests in the lower tranches of CLOs (see our website for a detailed explanation). Its investment style leads it to earn quite a bit of income but this is often offset by capital losses, reducing the overall return that investors earn.

DP Aircraft One and the three Doric Nimrod funds are leasing planes. It is hard to tell what the resale value of these planes will be when the leases come to the end of their life. This resale value will have a big impact on their final net asset values and will determine whether these funds generate capital growth or losses.

British American's ordinary shareholders benefit from the presence of a convertible security in its capital structure which boosts the dividend but makes its net asset value more volatile.

MedicX's dividend was only covered 54% by its income last year so, at the moment, it is one of the funds boosting its income through capital distributions.

Premier Energy & Water is a split capital trust with ordinary shares and zero dividend preference shares. The zeros have the effect of increasing the amount of income available to ordinary shareholders. This fund has been paying regular special dividends in an effort to reduce its revenue reserves and this will not continue indefinitely. However, if we stripped out the special dividend, it would still be on around a 5.4% yield today.

QuotedData

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