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By Fiona Hamilton

Which investment trusts make it into the brokers' 2019 model portfolios?

Diversity rules with a mix of equity and alternative trusts in all the leading investment trust brokers' portfolios – but there are some names that keep cropping up, reports Fiona Hamilton.

Around 80% of fund managers surveyed by the Association of Investment Companies (AIC) started 2019 predicting that stockmarkets would rise this year. More than a third forecast gains of more than 11.5%, with the US and UK stockmarkets expected to be the most rewarding.

The AIC findings would be more encouraging if the fund managers had not been far too optimistic about 2018, with 69% expecting stockmarkets to rise and almost 80% predicting that the FTSE 100 would finish above 7,500, whereas in practice it fell to 6,728.

Most leading investment trust brokers are more circumspect than the AIC's cohort of fund managers, and have been adjusting their recommendations to allow for more difficult times.

Canaccord Genuity

Alan Brierley of Canaccord Genuity has been the most cautious, having started de-risking his flexible model portfolio in 2014 by gradually reducing its exposure to equity trusts in favour of a variety of alternative investment companies.

Scottish Mortgage was dropped in 2014, followed by Impax Environmental and Polar Capital Technology in 2016. In their place he added Ruffer Investment Company and Highbridge Multi Strategy(hedge) fund in 2014, followed by BH Global hedge fund and Schroder Asian Total Return in 2017.

In April 2018, he further diversified the portfolio by backing two funds offering an attractive yield and well-managed exposure to new sectors, namely BioPharma Credit and Sequoia Economic Infrastructure.

In March 2009, equity trusts accounted for all but two of the 19 holdings in the Canaccord flexible model portfolio. The 2019 version includes stakes in just seven, including long-standing holdings in Edinburgh Investment Trust, Worldwide Healthcare, British Empire Trust, Monks and Edinburgh Dragon.

In addition to the alternatives mentioned earlier, the balance includes two private equity trusts, HarbourVest and Pantheon*, HICL Infrastructure*, property specialist The MedicX Fund*, and capital preservation-oriented RIT Capital.

With equity exposure at its lowest since the financial crisis, total returns on the Canaccord portfolio in 2018 were almost in the black at minus 0.7%, which compares well with the 9.5% fall in the FTSE All-Share index.

This was the portfolio's best relative performance since 2014, as although it outperformed the All-Share in each of the past 10 years bar 2011, the margin was progressively narrower through 2015 to 2017.

Brierley is counting on its highly diversified approach and focus on trusts with strong fundamentals to serve followers well through difficult times.

"Our cautious approach to portfolio construction is a function of concerns over the maturity of both the economic and credit cycles, elevated valuations driven by a 10-year bull market and escalating geopolitical worries," he explains.

However, he warns that the portfolio is liable to lag if stockmarkets rally, as in January 2019.

JP Morgan Cazenove

JP Morgan Cazenove's Christopher Brown and Adam Kelly launched their model portfolio of closed-ended companies in 2016. It has done well so far, beating the All-Share index in its first two years with gains of 28 and 20%, and again in 2018 with a 2.9% fall.

Like Canaccord, Brown and Kelly have been including a growing range of alternative investment companies and had only 40% in equity trusts at the start of 2019.

Stakes in Jupiter US Smaller Companies and North American IncomeTrust account for a third of that equity exposure, Asia ex Japan for 18%, and the sole 'UK' equity trust is technology specialist Herald*.

Around 15% is in infrastructure, notably 3i Infrastructure* and HICL, 21% in private equity including 3i Group, Hg Capital Trust and NB Private Equity, and 24% in fixed income/hedge, including BH Global*, BioPharma Credit*, Riverstone Energy*, Real Estate Credit Investments* and ultra defensive Capital Gearing*.

The latter was added at the start of 2019, with the Cazenove team including its zero discount policy among its attractions. This tunes in with their general preference for trusts seeking to defend or improve their ratings.

Winterflood Securities

Simon Elliott and his team at Winterflood have a different approach to the model portfolio they have been running for the past three years.

Their prime aim is to identify trusts that will outperform their peers on an 18- to 24-month view through discount narrowing or outperformance of the underlying portfolio.

In order to avoid making significant asset allocation calls, they have opted for an asset allocation broadly in line with the FTSE UK Private Investors Balanced Index (UKPIBI), which they use as a benchmark.

As a result, more than 60% of the Winterflood portfolio was in equity trusts at the start of 2018. Despite this, its total return last year was only 2.9% down, roughly in line with the UKPIBI.

Winterflood's 2019 portfolio includes 35 trusts, of which 12 are replacements for previous holdings and 15 are broking clients. They include 30% split evenly between six UK equity trusts, including contrarian stakes in Woodford Patient Capital* and Perpetual Income and Growth*, and a new stake in Troy Income and Growth because its conservative approach and zero discount policy bolster the model's defensive characteristics.

Seventeen overseas equity trusts account for 29%, and range from 3% stakes in each of Scottish Mortgage, Mid Wynd and Bankers to smaller stakes in Worldwide Healthcare*, BlackRock World Mining* and Allianz Technology*.

On the alternatives front, widening discounts prompted an increase to 6% in private equity exposure, evenly split between Hg Capital Trust, Pantheon International and Standard Life Private Equity*. Debt trusts account for 15%, including new stakes in Real Estate Credit Investments (also held by JPM Cazenove) and high-yielding Fair Oaks Income.

Property accounts for 4.9% of which a third is in TR Property. Ten per cent is in other alternatives including 3i Infrastructure and John Laing Environmental Assets*, Personal Assets and BH Macro £ share.

Numis Securities

Charles Cade and his team at Numis Securities offer a list of 25 core equity trust recommendations, of which six are broking clients, and a separate list of 19 core alternatives including 11 broking clients.

Rather than offer a model portfolio, Numis aims to highlight opportunities within the listed funds sector. The returns on its recommendations confirm that alternatives tended to be more rewarding last year.

Only five of Numis's core equity recommendations achieved positive share price total returns (SPTRs) in 2018, including Capital Gearingand Caledonia Investments, and only two more outperformed the 3.9% fall in the MSCI AC World Index against which Numis judges its success.

Another 10 outperformed the All-Share, but 12 failed to do so. In contrast, all but five on the alternatives list outperformed the MSCI AC World index, and 13 of the 18 on the list throughout the year ended it in positive territory.

SPTRs ranged from low single figure gains for HgCapital Trust* and ICG Enterprise* to 22% for BioPharma Credit and 33% for Syncona*. Seven alternative recommendations were withdrawn while still in the black.

Numis started 2019 guardedly optimistic, on the basis that corporate earnings growth is expected to remain positive albeit slowing, equity valuations were more appealing than a year ago, especially in the UK and emerging markets, and “there is no clear catalyst for a bear market”.

“For investors willing to ride out the cycle, we favour backing experienced managers who may be more willing to take a long-term view, as well as more defensive managers who seek to protect capital in a downturn. We also favour funds where the risk of discount widening or premium erosion appears limited,” Cade says.

Numis’s core equity recommendations include seven UK equity trusts, 13 overseas equity trusts and three sector specialists, plus TR Property, Capital Gearing, RIT Capital Partners* and Aberdeen Diversified Income & Growth. Its core alternative recommendations include four private equity trusts, four property, four debt, and BH Macro £ shares (also recommended by Wins, whereas Canaccord and JPMC prefer BH Global).

Multiple choices

Investment companies recommended by Numis, JPMC and Wins include Fidelity European Values, BlackRock World Mining and Hg Capital Trust.

Numis’ overlaps with both JPMC and Canaccord are HICL Infrastructure and Biopharma Credit.

Canaccord and Numis both like Monks, Edinburgh IT, Edinburgh Dragon, RIT Capital Partners and HarbourVest Global Private Equity.

Winterflood and Canaccord both like Pantheon International and Schroder Asian Total Return.

Canaccord and JPMC both favour BioPharma Credit.

Winterflood and JPMC both favour North American Income, and Winterflood and Numis both favour JPM Emerging Markets.

With investment trusts’ wide choice of equity funds now complemented by an equally varied choice of alternative investment companies, investors are much better placed to assemble portfolios suited to most scenarios.

** Denotes that the portfolio managers are brokers to the trust.*