

INVESTMENT TRUST DIVIDEND SNAPSHOT



AUGUST 2021

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THE GLOBAL DIVIDEND CONTEXT

In the first full year of the pandemic, our UK Dividend Monitor, the sister publication to the Investment Trust Monitor, has shown how severely the pandemic impacted the amount of capital UK plc distributed to its shareholders by way of dividends. Two thirds of the UK's listed companies cut payouts between April 2020 and March 2021, bringing the total down 41.6%.

Of course, one of the real advantages of investment trusts is that they are not restricted only to buying UK shares. Depending on the trust's mandate, they might invest globally, in particular countries or regions, look at large or small companies, or have a particular sector focus. UK dividends alone are therefore only part of the picture. Around the world, dividends fell much less than those in the UK in the first twelve months of the pandemic. Janus Henderson's Global Dividend Index showed that payouts dropped 14%, with the greatest resilience in North America, Japan and Asia, but the greatest weakness in Europe, the UK and Australia.

In the second quarter, our most recent UK Dividend Monitor showed that the rebound has begun in earnest, with payouts 43.8% higher on an underlying basis and set to rise 13.4% for the full year². By the end of 2021, UK dividends will still be three tenths lower than their pre-crisis peak and are only likely to catch up fully in 2025. Global dividend growth will be slower than the UK because there is less lost ground to make up, but the global recovery is underway too.

It is important to remember that dividends are usually a lagging indicator of economic growth and company performance, since they are paid retrospectively out of company profits. 2020 was unusual because dividend cuts came pre-emptively, in many cases even before the pandemic hit profits. The dividend recovery we are seeing now therefore reflects the low base created by this precautionary action, meaning that the lag we might normally expect in a rebound is not present this time. It's all happening simultaneously.

Over the course of the pandemic investment trusts have outperformed the broader market, both in the UK and globally



UK Plc dividends

DOWN 34.6%



Global dividends

DOWN 5.9%



If investment trusts had followed wider market trends, dividends would have fallen by

almost a fifth



BUT actually, investment trust dividends

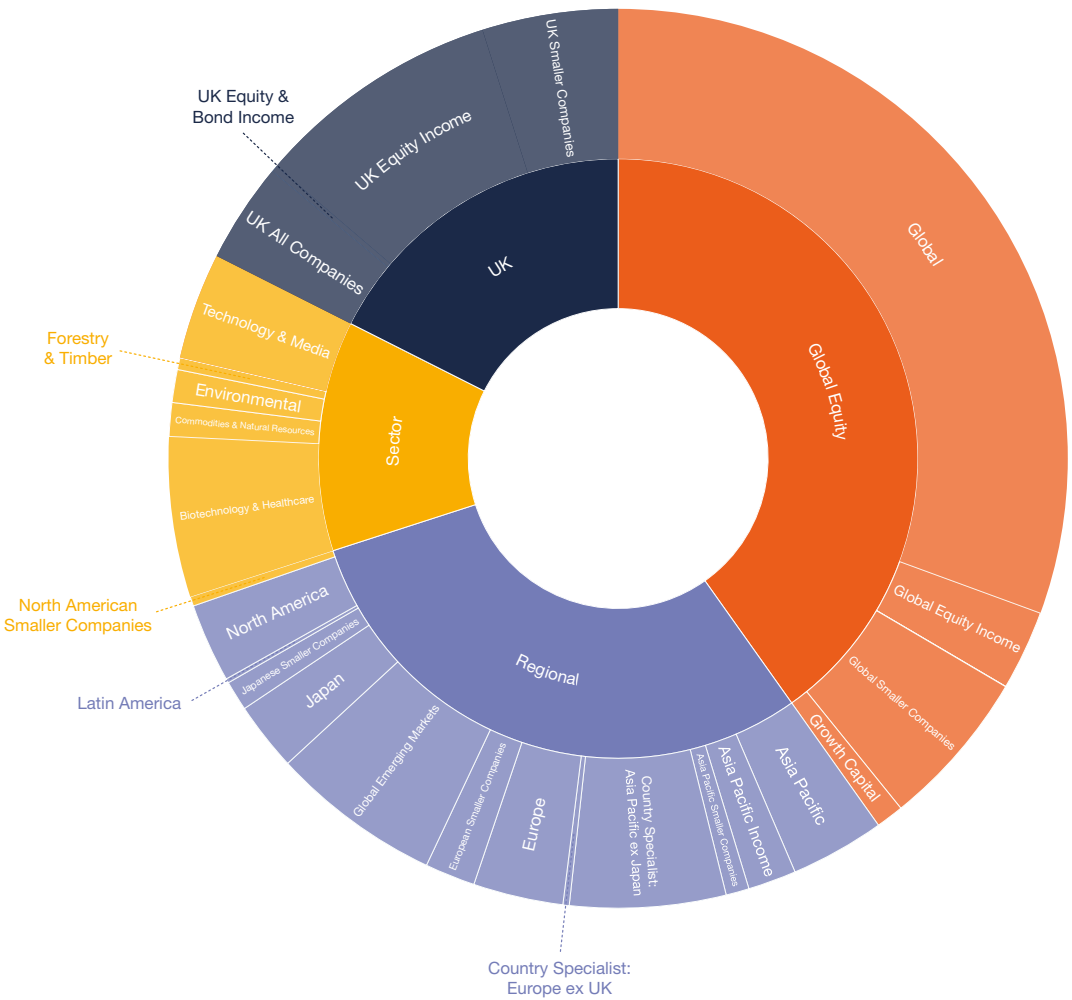
ROSE 2.0%

1 In USD, source JHGDGI Edition 30, May 2021

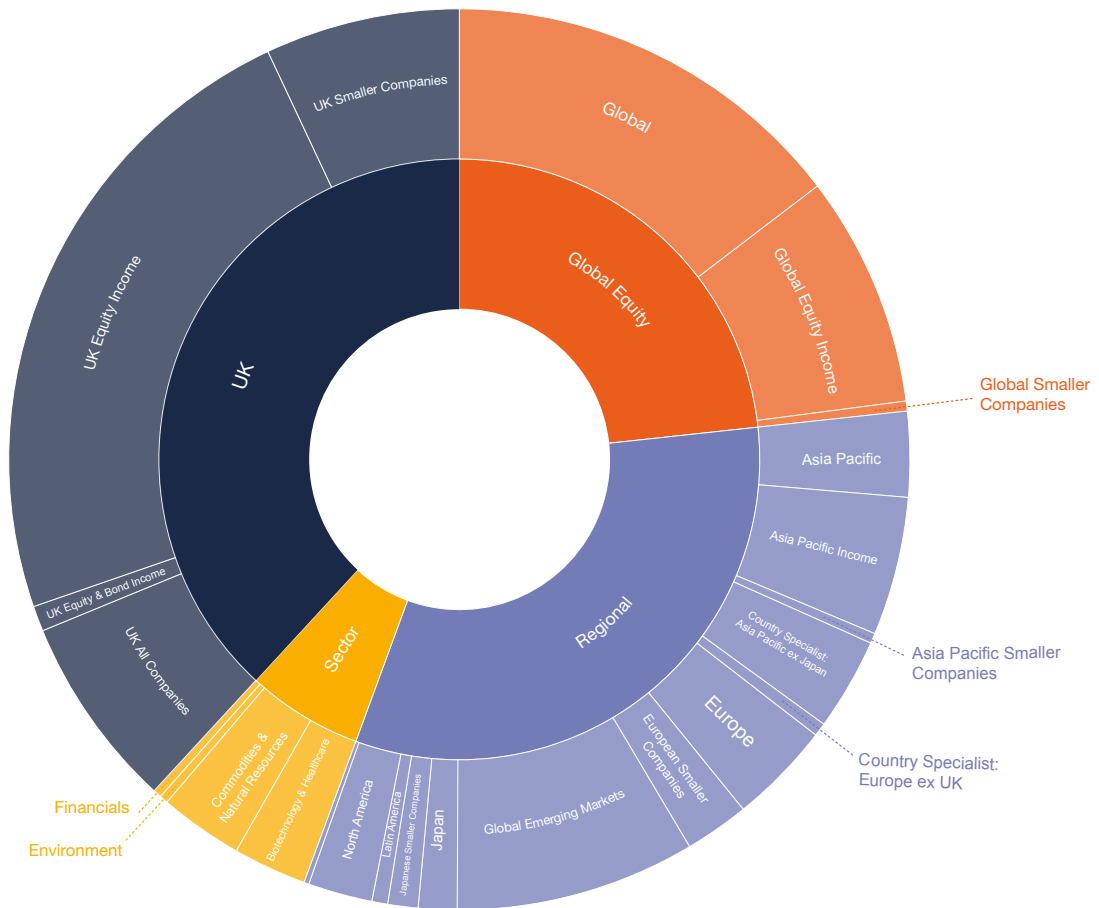
2 Link Group UK Dividend Monitor, Edition 46, July 2021; underlying growth excludes special dividends

INVESTMENT TRUSTS DIVIDENDS

Market capitalisation of investment trusts



H1 dividends of investment trusts



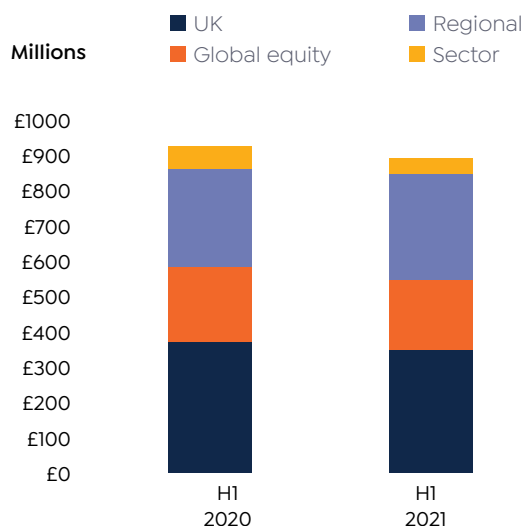
Investment trusts sailed through the pandemic with their income-generating power almost undiminished, despite their greater exposure to hard-hit UK dividends than to the more modest decline in the wider world. This greater exposure reflects the long pedigree of many funds focused on UK equities, as well as the largely domestic shareholder base which has historically had a greater appetite for UK assets. Despite the large weighting of UK shares in the collective portfolio of investment trusts, dividends rose 3.6% in 2020 to a total of £1.85bn, hugely better than the showing in the wider stock market either in the UK or elsewhere in the world.

If we look from before the pandemic began to now, we get a fair perspective of investment trusts versus the wider markets. Between January 2020 and June 2021, Link Group's index of UK dividends fell by 34.6%³ on an underlying basis. Global dividends were down just 5.9%⁴. If this were replicated across the investment trust sector, we calculate that investment trust pay-outs would have fallen by almost a fifth over the same period. But in fact, our index of investment trust dividends rose 2%.

Investment trust dividends do lag a bit behind other listed companies because they are mainly distributed from dividends the trusts themselves receive on their underlying investments. We can see this lag in the growth rates over the last few half-year periods. The rate of increase slowed steadily from 14% in the first half of 2019 to 1% in the second half of 2020, before turning negative in the first six months of 2021.

The first half of 2021 therefore reflects the much lower income the trusts themselves were receiving from their investments in the months before. Moreover, it is set against a record six months for investment trust dividends in the first half of 2020, so the year-on-year comparison is very unfavourable. Between January 2021 and June 2021, payouts fell 3.1% to £891.9m, £29m less than in the first six months of 2020. A decline, certainly, but barely a blip compared to 2020's dividend wipeout in the wider stock markets. Moreover, more than seven trusts in ten raised their dividends or held them steady in H1 2021 compared to H1 2020. Among those that cut, the average reduction was 23%.

Investment trust dividends - first half



3 Source: Link Group UK Dividend Monitor, GBP

4 Source: Janus Henderson Global Dividend Index, USD

More than seven trusts in ten raised their dividends or held them steady in H1 2021 compared to H1 2020.

The biggest impact came from the UK Equity Income sector, but mainly because it is the largest income-paying sector, contributing a quarter of dividends from equity investment trusts. Payouts here fell by 9% year-on-year in the first half of 2021, a drop of £20.3m. A 10% decline in dividends from the Global sector also made a significant impact. The largest percentage decline among the major categories was from mainstream European funds. Regional sectors focused on Asia, Japan, and North America almost all paid out more in dividends, reflecting the very limited effect of 2020s cuts among companies in those parts of the world.

Top payers

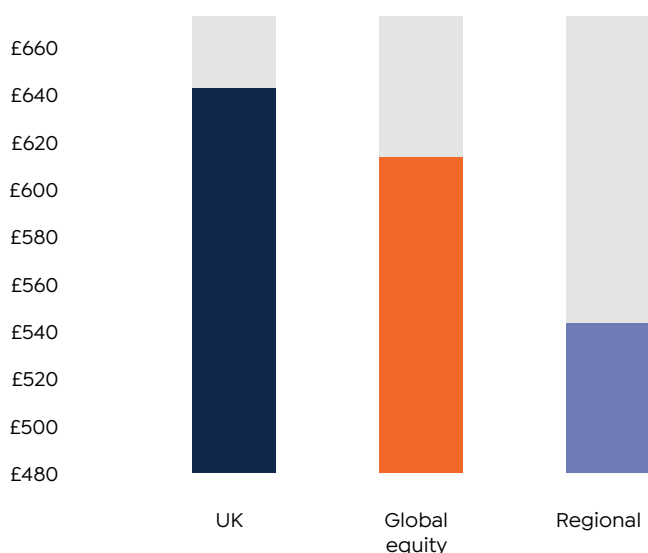
Sector	Company	H1 2021 £m
UK Equity Income	City of London Investment Trust	£41.4
Global Equity Income	Murray International Trust plc	£39.2
Global Emerging Markets	Templeton Emerging Markets Investment Trust plc	£35.5
Global	F&C Investment Trust plc	£33.7
UK All Companies	The Mercantile Investment Trust plc	£31.7
Global	Alliance Trust plc	£23.1
Commodities & Natural Resources	Blackrock World Mining Trust plc	£23.0
Global	Witan Investment Trust plc	£21.9
UK Equity Income	Edinburgh Investment Trust plc	£20.7
UK Smaller Companies	Aberforth Smaller Companies Trust plc	£20.3
UK Equity Income	Finsbury Growth & Income Trust plc	£17.9
UK All Companies	Fidelity Special Values plc	£17.4
UK Equity Income	Law Debenture Corp plc	£17.3
Asia Pacific Income	Henderson Far East Income Ltd.	£16.9
UK Equity Income	Merchants Trust plc	£16.7
Europe	Fidelity European Trust plc	£16.0
European Smaller Companies	European Assets Trust plc	£14.4
UK Equity Income	Murray Income Trust plc	£14.3
Global	Bankers Investment Trust plc	£14.1
Asia Pacific	Schroder Asia Pacific Fund	£13.3

THE REVENUE RESERVE

The Revenue reserve has protected investment trust payouts

Revenue reserves (latest annual report)

Millions

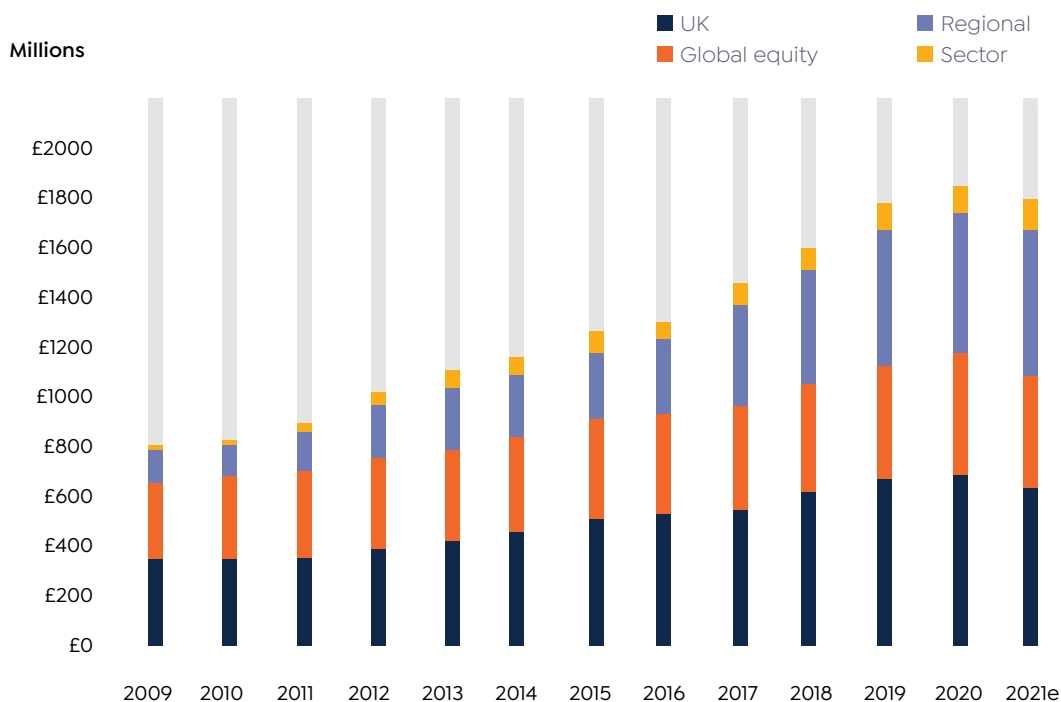


Pre-pandemic, investment trusts had accumulated reserves of £2.13bn from past dividends they have received from companies but which they are permitted to tuck away for a rainy day. The rules allow up to 15% of dividends received to be saved in this way.

The pandemic has been the rainiest of days. By mid-July, the collective revenue reserve had fallen by £360m to £1.77bn, meaning that £22 in every £100 of dividends distributed by investment trusts over the last 12 months has been funded from reserves. More than half of trusts (56%) have dipped into their back pocket in this way. Rainy-day funds are likely to be depleted further in the next three to six months, but we are optimistic that the total drawn down will come in below the £700m upper limit we considered possible in our March annual report. Dividend cuts have reduced the burden on the revenue reserve somewhat, but there is another reason. Given how high equity markets have soared in the last twelve months, trusts have taken advantage of the rules that permit them to distribute some of their capital gains as dividends and that this has enabled them to protect their reserves more than would have otherwise been possible.

OUTLOOK

Investment trust dividends



Dividends are recovering strongly across the wider stock market both in the UK and abroad. We at Link Group expect underlying growth of 13.4% for 2021, with the headline figure growing significantly faster owing to generous special dividends this year. The ‘run-rate’ of growth is actually better than this, because dividends in Q1 2021 were still suppressed by the pandemic, so we have only three rebound quarters this year. The recovery is really encouraging, but we do not expect to equal the 2019 high point again until 2025, because the giant oil sector, once the biggest paying by a long chalk, has permanently reset its dividends at a lower level. More widely around the world, Janus Henderson’s global dividend index suggests that payouts should reach the 2019 level again some time in 2022.

For investment trusts, the global funds can continue dividends without too much difficulty. Revenue reserves comfortably exceed dividend payments and there is not long to wait until cash distributed from the underlying companies in funds tops pre-pandemic highs. For UK-focused trusts, the picture is more difficult. Fund managers with a clear income mandate have rejigged portfolios to focus more on those companies that are today’s bigger dividend payers and revenue reserves are certainly healthy. But they are now 4% below the level of a single year’s

payments from the sector, having gone into the pandemic more than 10% bigger. Managers will use the discretion they derive from the revenue reserve and to distribute capital gains, but we should expect lower dividends to wash through for another few months and caution that significant growth is unlikely until the wider stock market has caught up a bit on the ground lost in 2020. The same applies in European funds, which have depleted their revenue reserves more than other categories over the last year, but other regionally focused funds should do fine.

Overall therefore, the next six months are likely to see a further small drop in dividends from investment trusts even as the wider market is funnelling significantly more cash to shareholders. If this drop does not happen it is because boards have relied more heavily on reserves than we expect. We estimate 2021 will see £1.79bn in dividends from the sector, a decline of 3.2% year-on-year. This is not something to worry about. It is one of the most reassuring features of investment trusts that they can smooth out the peaks and troughs in dividend income caused by the economic cycle or big one-off shocks. For investors, this regular, predictable income is very welcome indeed.

APPENDIX

EQUITY FUNDS - Dividends Paid £m

Group	AIC Sector	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	H1 2020	H1 2021
UK	UK All Companies	£75.8	£70.7	£69.5	£70.8	£83.5	£88.1	£92.4	£93.9	£82.4	£92.4	£101.3	£112.0	£70.8	£62.5
	UK Equity & Bond Income	£71	£72	£7.4	£7.7	£8.3	£9.0	£10.2	£10.1	£13.7	£15.4	£15.0	£16.4	£8.2	£8.2
	UK Equity Income	£237.2	£244.2	£257.8	£269.3	£290.1	£315.9	£344.2	£358.5	£377.3	£406.4	£443.6	£452.1	£229.9	£209.6
	UK Smaller Companies	£41.6	£35.9	£37.0	£42.7	£45.2	£50.3	£66.8	£73.1	£85.6	£113.2	£120.7	£118.0	£63.2	£62.8
Global Equity	Global	£252.5	£263.7	£268.7	£291.0	£285.3	£291.0	£301.3	£292.2	£285.0	£297.9	£304.4	£330.2	£146.7	£131.5
	Global Equity Income	£50.0	£59.2	£63.2	£76.5	£83.7	£89.0	£93.9	£103.0	£117.8	£118.8	£126.4	£132.2	£72.1	£74.7
	Global High Income	£0.5	£0.0	£0.0	£0.0	£0.7	£1.1	£1.4	£1.5	£2.3	£2.4	£1.2	£1.1	£0.0	£0.0
	Global Smaller Companies	£10.5	£6.0	£5.9	£7.1	£7.9	£8.3	£9.6	£11.9	£13.9	£11.6	£14.2	£14.4	£3.3	£3.2
	Growth Capital	£0.0	£0.0	£0.0	£0.0	£0.0	£0.0	£0.0	£1.3	£0.0	£0.0	£0.0	£0.0	£0.0	£0.0
Regional	Japan	£5.2	£8.2	£5.0	£6.0	£8.8	£7.4	£7.4	£9.4	£13.7	£18.0	£23.9	£26.4	£12.2	£12.5
	Japanese Smaller Companies	£0.0	£0.0	£0.0	£0.1	£0.0	£0.0	£0.0	£0.0	£0.0	£5.3	£10.4	£16.1	£7.8	£9.8
	Latin America	£3.5	£5.1	£7.0	£10.6	£13.0	£9.9	£10.6	£5.8	£6.8	£8.9	£12.5	£9.6	£5.2	£5.1
	North America	£8.7	£7.4	£7.7	£11.5	£18.0	£19.8	£23.9	£26.2	£27.2	£29.8	£32.6	£34.7	£20.3	£20.8
	North American Smaller Companies	£0.0	£0.0	£0.0	£0.0	£0.0	£4.0	£0.0	£0.0	£0.0	£1.4	£1.4	£1.5	£1.5	£1.6
	Asia Pacific	£17.9	£18.4	£23.4	£25.1	£22.6	£23.0	£24.0	£26.5	£28.8	£32.8	£42.6	£44.0	£26.1	£27.5
	Asia Pacific Income	£15.0	£26.9	£31.3	£40.3	£50.5	£54.3	£58.7	£61.6	£84.6	£82.1	£86.6	£91.3	£41.6	£44.7
	Asia Pacific Smaller Companies	£3.7	£5.3	£7.1	£7.8	£9.0	£9.3	£10.6	£10.4	£12.4	£13.2	£16.2	£15.7	£3.4	£3.3
	Country Specialist: Asia Pacific ex Japan	£3.6	£2.1	£5.6	£10.4	£11.8	£12.4	£13.3	£16.0	£37.5	£53.3	£50.3	£59.4	£17.5	£22.4
	Country Specialist: Europe ex UK	£0.0	£0.0	£0.0	£0.0	£0.0	£8.0	£6.8	£12.0	£12.0	£13.0	£14.6	£15.5	£4.6	£4.3
	Europe	£33.9	£37.1	£42.0	£40.9	£45.2	£29.9	£48.1	£50.3	£66.1	£68.0	£85.1	£66.5	£41.2	£33.0
	European Smaller Companies	£4.8	£4.2	£4.7	£10.3	£10.6	£10.4	£11.1	£12.1	£12.5	£21.7	£45.0	£48.5	£18.8	£20.8
	Global Emerging Markets	£24.2	£16.0	£24.8	£39.0	£50.5	£49.8	£58.1	£66.1	£88.4	£105.9	£118.7	£133.4	£66.1	£77.5
	Sector	Biotechnology & Healthcare	£2.0	£4.0	£9.2	£11.1	£13.1	£18.8	£18.4	£21.2	£40.6	£46.6	£59.5	£48.4	£20.2
Commodities & Natural Resources		£15.9	£16.7	£18.7	£46.0	£46.6	£47.0	£47.6	£42.0	£40.3	£36.2	£45.4	£46.5	£28.3	£27.0
Environmental		£0.0	£2.4	£2.5	£2.7	£2.6	£3.0	£3.2	£3.0	£3.8	£4.8	£6.5	£10.8	£7.4	£2.7
Financials		£0.0	£0.0	£0.0	£0.0	£0.0	£4.3	£5.6	£5.8	£6.4	£8.2	£8.7	£7.0	£4.1	£2.7
EQUITY FUNDS - TOTAL		£813.4	£841.0	£898.4	£1,027.0	£1,106.9	£1,164.0	£1,267.1	£1,313.9	£1,459.1	£1,607.4	£1,786.7	£1,851.5	£920.5	£891.9

OTHER ASSET CLASSES - Dividends Paid £M

Group	AIC Sector	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	H1 2020	H1 2021
Property	Property	£1.4	£4.5	£6.1	£13.9	£19.9	£34.6	£57.8	£53.0	£425.4	£427.6	£441.8	£366.8	£194.7	£0.0
	Property - Debt	£0.0	£0.0	£0.0	£0.0	£0.0	£5.1	£6.5	£6.5	£18.6	£23.5	£28.4	£34.3	£16.8	£30.4
	Property - Europe	£0.0	£0.0	£0.0	£0.0	£0.0	£0.0	£0.0	£0.0	£5.5	£11.5	£18.2	£19.1	£10.2	£24.8
	Property - Rest of World	£0.0	£0.0	£0.0	£0.0	£0.0	£0.0	£0.0	£0.0	£0.0	£0.0	£0.0	£0.0	£0.0	£0.0
	Property - UK Commercial	£0.0	£0.0	£0.0	£0.0	£0.0	£0.0	£0.0	£1.4	£11.9	£11.5	£11.5	£6.9	£4.1	£104.6
	Property - UK Healthcare	£0.0	£0.0	£0.0	£0.0	£0.0	£0.0	£0.0	£0.0	£0.0	£0.0	£6.1	£25.9	£12.2	£21.5
	Property - UK Residential	£0.0	£0.0	£0.0	£0.0	£0.0	£0.0	£0.7	£0.0	£0.0	£0.0	£2.3	£1.6	£1.6	£42.3
	Property Securities	£0.0	£8.9	£15.4	£16.9	£22.2	£23.7	£24.4	£26.5	£33.3	£38.7	£42.8	£44.4	£16.5	£16.5
Debt	Liquidity Funds	£0.0	£0.0	£0.1	£0.1	£0.0	£0.0	£0.0	£0.0	£0.0	£0.0	£0.1	£0.0	£0.0	£0.0
	Debt - Direct Lending	£0.0	£0.0	£0.0	£0.0	£0.0	£1.2	£16.8	£49.5	£76.5	£108.1	£123.3	£131.5	£64.4	£46.2
	Debt - Loans & Bonds	£2.8	£14.5	£15.4	£29.1	£35.6	£56.7	£75.8	£80.2	£80.4	£73.2	£94.7	£90.8	£48.7	£39.9
	Debt - Structured Finance	£0.0	£0.0	£0.0	£0.0	£5.1	£18.4	£18.9	£39.0	£50.8	£99.1	£92.9	£123.3	£39.6	£52.3
Other	Private Equity	£16.8	£11.4	£16.2	£29.9	£48.5	£52.7	£71.0	£144.6	£1,848.0	£307.7	£174.2	£169.6	£81.3	£276.6
	Renewable Energy Infrastructure	£0.0	£0.0	£0.0	£0.0	£3.9	£60.4	£135.6	£171.5	£199.1	£263.1	£331.8	£387.8	£186.6	£258.3
	Hedge Funds	£0.0	£0.0	£0.0	£0.0	£0.0	£0.0	£0.0	£0.0	£0.0	£0.0	£32.7	£65.8	£34.0	£30.2
	Infrastructure	£15.7	£94.2	£68.9	£213.4	£252.8	£286.8	£460.9	£364.3	£454.1	£459.1	£461.2	£529.5	£256.7	£267.6
	Infrastructure Securities	£0.0	£0.7	£1.4	£1.6	£1.9	£2.3	£2.4	£3.4	£7.6	£8.0	£7.7	£8.0	£4.0	£4.1
	Insurance & Reinsurance Strategies	£0.0	£0.0	£0.0	£0.0	£0.0	£0.0	£0.0	£0.0	£0.0	£0.0	£0.0	£0.0	£0.0	£0.0
	Leasing	£0.0	£0.0	£0.0	£0.0	£0.0	£0.6	£10.9	£26.0	£25.9	£30.9	£36.7	£9.0	£9.0	£0.0
	Flexible Investment	£56.4	£54.0	£54.7	£96.7	£100.1	£103.7	£107.2	£116.5	£84.6	£90.9	£97.2	£109.0	£51.3	£53.3
	Other	£24.9	£27.6	£27.2	£20.7	£21.7	£23.0	£28.1	£38.2	£32.6	£37.8	£34.0	£30.4	£12.6	£0.2
	Royalties	£0.0	£0.0	£0.0	£0.0	£0.0	£0.0	£0.0	£0.0	£0.0	£1.0	£14.4	£30.7	£12.6	£27.5
OTHER ASSET CLASSES - TOTAL		£118.0	£215.7	£205.4	£422.3	£511.6	£669.1	£1,016.9	£1,120.6	£3,354.3	£1,991.9	£2,052.1	£2,184.5	£1,056.7	£1,296.3

THE BACKGROUND

What is an investment trust?

Quite simply, an investment trust is a 'pot' of assets in which you can buy shares on the stock exchange. These assets may be listed or unlisted equity or may be alternative assets such as unlisted real estate, infrastructure or commodities. Legally they are self-contained companies in their own right and some are among the oldest financial institutions in the UK – the F&C Investment Trust is 152 years old.

Investment trusts have an independent board of directors that set out the investment objective and are responsible for the governance of the trust, but they employ an investment manager to make all the investment decisions. Crucially the trusts are closed-ended, which means they have a defined number of shares in issue and do not experience daily inflows and outflows of capital. This provides valuable stability, especially in volatile markets as the trust need never be a forced seller or buyer.

This is especially important if the trust itself invests in illiquid assets. The share price will typically track the value of the underlying assets in the trust, but, because the number of shares issued by the trust is fixed, the share price can exceed the net asset value (NAV) when demand for the trust is high and performance expectations are positive. Equally it can trade below the net asset value when investors are less keen and performance expectations are negative (the so-called "premium" or "discount" respectively).

Investment trusts are ideal vehicles for private investors as they offer an easily accessible route for investing in a diversified but targeted pool of assets. Importantly, investment trusts may be allowed limited borrowing or leverage, using borrowed funds to buy more assets. At present, those that use this freedom have borrowings equal to 8% of their net asset value. This brings the advantages of modest gearing of returns. Since interest rates are below dividend yields in most major markets, borrowed capital should also finance itself.

Most investment trusts pay regular dividends to their shareholders, although different investment styles will focus on income (return in the form of dividends), capital (return in the form of share price increases) or total returns (a combination of both).dividend per share. Those that have bought back shares will see their total dividend paid grow more slowly than their dividend per share.



We estimate 2021 will see

£1.79bn in dividends

from the investment trust sector, a decline of

3.2% year-on-year

Statistical Methodology

Link Group extracted investment trust data from its quarterly UK Dividend Monitor database for each quarter between 2009 and 2021 (the regular UK Dividend Monitor excludes investment trusts). All main-market UK listed trusts are included, though the analysis focuses on equity funds unless otherwise stated. Revenue reserve data was sourced from Factset. Dividends are included on the pay date. Link Group has categorised the trusts according to AIC investment trust sectors. VCTs are excluded. Link Group's series includes any investment trust in operation during each period, so it captures a full market picture at any point in time, rather than only those investment trusts that survive to this day.

The analysis looks at the total dividend paid. Trusts that have issued shares will therefore have seen their total dividend paid expand faster than their dividend per share. Those that have bought back shares will see their total dividend paid grow more slowly than their dividend per share.

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