EDISON

Finsbury Growth & Income Trust

A measure of optimism (and one of cognac)

Investment trusts

Finsbury Growth & Income Trust (FGT) is a focused portfolio of 25-30 stocks, mainly large cap and focused on the UK, although up to 20% at the time of acquisition (currently c 18%) may be held in overseas companies. Manager Nick Train is known for his long-term, low-turnover approach; the last complete exit from the portfolio was in 2013 and until the recent purchase of Rémy Cointreau, no new stocks had been bought since 2011. Long-term performance has been strong, with NAV and share price total returns in excess of 10% a year over 10 years, and the trust is ranked in the top quartile of its peer group over one, three, five and 10 years.

12 months ending	FGT share price (%)	FGT NAV (%)	FTSE All-Share Index (%)	FTSE 350 Index (%)	MSCI World Index (%)
30/09/11	6.5	5.9	(4.4)	(4.4)	(2.7)
30/09/12	23.6	21.2	17.2	17.2	18.0
30/09/13	30.5	31.9	18.9	18.6	20.6
30/09/14	8.6	9.0	6.1	6.1	12.7
30/09/15	11.8	12.0	(2.3)	(2.6)	2.1

Source: Thomson Datastream. Note: Total return basis.

Investment strategy: Long term, short list

Portfolio manager Nick Train aims to ‘buy great companies and hold them forever’, taking advantage of the long-term compounding of returns from market-leading companies bought at sensible valuations. The manager conducts fundamental analysis to identify stocks that are undervalued relative to their growth prospects, focusing on quality companies with strong brands and enduring intellectual property. The investment style is highly concentrated, with a portfolio of 25-30 stocks drawn from just four industry sectors, and gearing is modest and used for investment flexibility rather than as a means of expressing a market view.

Market outlook: Can good news allay investor fears?

After something of a recovery from the sharp global market sell-off in late August, the FTSE All-Share index is flat year-to-date (total return of +0.7% to 5 October). Markets remain volatile, with investors focusing on fears over slowing growth in China and the potential impact around the world of rising interest rates in the US and UK. However, the UK was one of the few developed countries not to have its 2015 GDP growth estimate downgraded by the IMF in its latest report, with further good news evident in recent rises in household disposable income, as inflation remains subdued and the low oil price pays dividends for consumers.

Valuation: Still in strong demand

Demand for FGT's shares has remained robust and at 7 October the shares were trading at a 0.3% premium to cum-income net asset value, compared with an average premium of between 0.4% and 0.6% over one, three and five years. The trust has a defined process for managing supply and demand and will tend to buy back shares if the discount exceeds 5% (which it has not in the past five years) and issue new shares if there are unfulfilled buy orders in the market. So far in 2015, 17.7m shares have been issued, raising a little over £100m.

9 October 2015

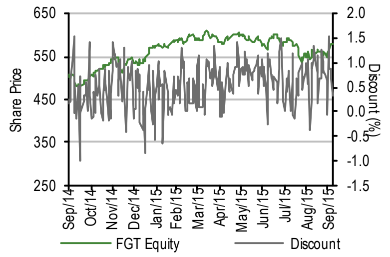
Price	**567.0p**
Market cap*	**£687.7m**
AUM	**£706.6m**

NAV*	568.8p
Premium to NAV	1.6%
NAV**	576.2p
Premium to NAV	0.3%
Yield	2.1%

*Excluding income. **Including income. Data at 7 October 2015.

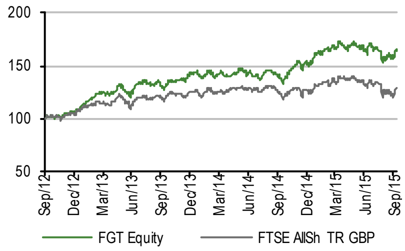
Ordinary shares in issue	121.3m
Code	FGT
Primary exchange	LSE
AIC sector	UK Equity Income

Share price/premium performance*



*Including income. Positive values indicate a premium; negative values indicate a discount.

Three-year cumulative perf. graph



52-week high/low	609.0p	470.3p
NAV* high/low	606.4p	474.6p

*Adjusted for debt at market value, including income.

Gearing

Gross	3.0%
Net	3.0%

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Edison profile page

Finsbury Growth & Income Trust is a research client of Edison Investment Research Limited

Exhibit 1: Finsbury Growth & Income Trust at a glance

Investment objective and fund background

FGT's investment objective is to achieve capital and income growth and provide shareholders with a total return above that of the FTSE All-Share Index. It invests principally in the securities of UK-quoted companies, but up to a maximum of 20% at the time of acquisition can be invested in non-UK-quoted companies. FTSE 100 companies normally represent 50-100% of the portfolio, with at least 70% usually invested in FTSE 350 companies.

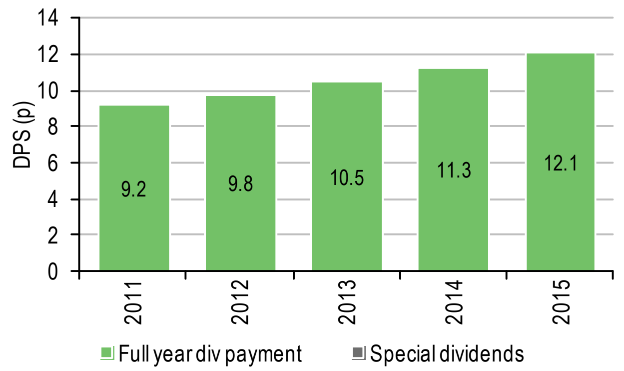
Recent developments

- 23 September 2015: second interim dividend of 6.6p declared, bringing the total dividend to 12.1p for the year ending 30 September .
- 17 July 2015: block listing application for 10m new shares, to be issued according to market demand.
- 29 June 2015: Simon Hayes, chief executive of Peel Hunt, appointed as a non-executive director.

Forthcoming		Capital structure		Fund details	
AGM	February 2016	Ongoing charges	0.8%	AIFM	Frostrow Capital
Annual results	December 2015	Net gearing	3.0%	Portfolio manager	Lindsell Train
Year end	30 September	Annual mgmt fee	£70k + 0.6% market cap	Address	25 Southampton Buildings, London, WC2A 1AL, UK
Dividend paid	May, October	Performance fee	None (see page 7)		
Launch date	January 1926	Trust life	Indefinite	Phone	+44 (0)20 3008 4910
Continuation vote	None	Loan facilities	£50m revolving	Website	www.finsburygt.com

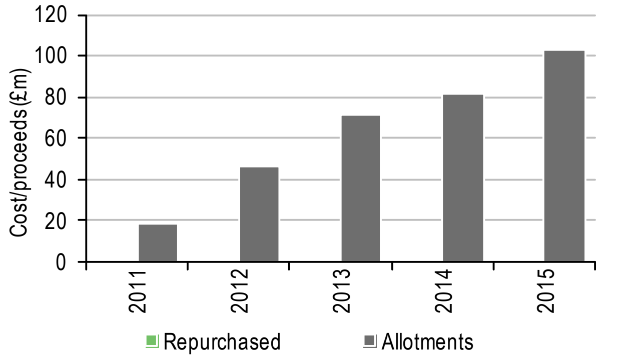
Dividend policy and history

Two dividends annually, paid in May and October. The dividend is expected to rise over the longer term.

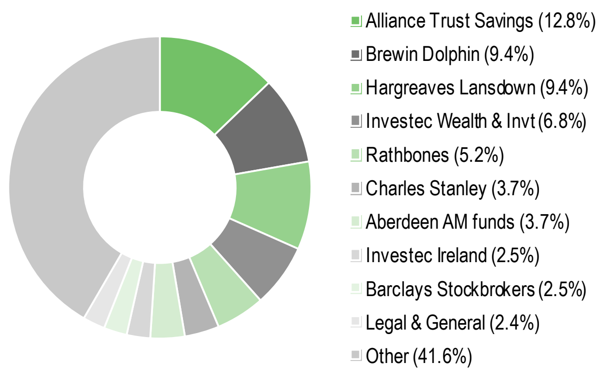


Share buyback policy and history

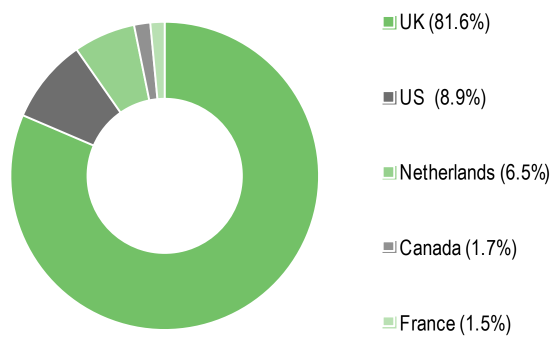
Renewed annually, the trust has authority to purchase up to 14.99% and allot up to 10% of issued share capital.



Shareholder base (as at 30 September 2015)



Distribution of portfolio (as at 30 September 2015)



Top 10 holdings (as at 30 September 2015)

			Portfolio weight %	
Company	Country	Sector	30 Sept 2015	31 March 2015
Unilever	UK	Consumer goods	9.3	8.8
Relx*	UK	Consumer services	8.8	7.7
Diageo	UK	Consumer goods	8.4	7.7
Heineken	Netherlands	Consumer goods	6.5	6.6
Hargreaves Lansdown	UK	Financials	6.4	5.9
Sage Group	UK	Technology	6.2	5.4
London Stock Exchange	UK	Financials	5.9	6.3
Pearson	UK	Consumer services	5.4	7.2
Schroders	UK	Financials	5.0	5.5
Burberry Group	UK	Consumer goods	5.0	5.4
Top 10 (% of portfolio)			**66.9**	**66.5**

Source: Finsbury Growth & Income Trust, Edison Investment Research, Morningstar, Bloomberg. Note: *Formerly Reed Elsevier.

Market outlook: Bright spots emerging for UK?

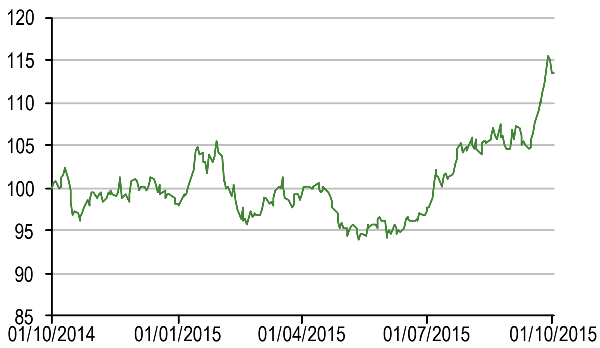
Following a broadly positive first half to the year, global stock markets sold off sharply in late August and remain volatile into the autumn. Having recovered somewhat from the 25 August low point, the MSCI World index has produced a total return of just 0.4% year-to-date (to 5 October). New growth forecasts from the International Monetary Fund included some encouraging news for the UK in early October, with a small upgrade to the 2015 GDP forecast published in July. However, the latest numbers for world growth in both 2015 and 2016 are below those forecast by the IMF in April and July. The prospect of continued recovery in the UK and US once again raises the question of when, and by how much, the Bank of England and the Federal Reserve will begin raising interest rates, a vexed question as the 'good news' – evidence of a recovery strong enough to support normalisation of rates – risks being outweighed by the 'bad news' (effects on indebted consumers and weakening emerging market economies with large volumes of dollar-denominated debt and falling currencies).

The high level of market uncertainty can be observed in the recent relationship of cyclical and defensive stocks (Exhibit 2, left-hand chart). Defensives sold off more than cyclicals in August as investors focused on their emerging markets exposure and interest rate sensitivity (many are seen as 'bond proxies', and could see selling activity should rates rise on cash and bonds), but bounced back sharply in September. Warnings from global economic bodies such as the IMF and World Bank on the negative effects of hasty interest rate rises in the West may have driven some of this rerating, as well perhaps, as a renewed appreciation of the benefits of 'defensiveness' in volatile markets.

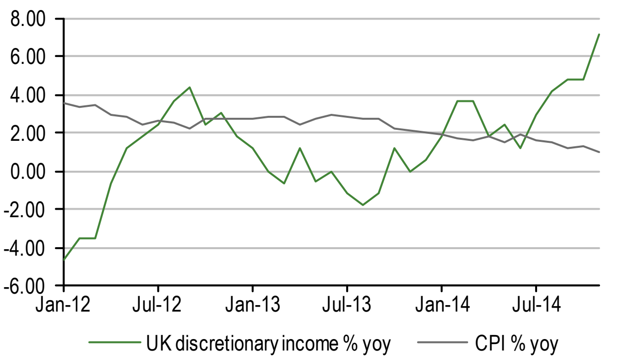
What happens next in global markets will depend on multiple factors – can the oil price remain at its current low level, benefiting consumers globally; is the slowdown in China as bad as feared, and how will geopolitical worries play out over the coming months? However, for UK consumers – and the companies that serve them – rising disposable incomes in the face of flat to falling inflation (Exhibit 2, right-hand chart) could provide a little good news among the general uncertainty.

Exhibit 2: FTSE Defensive vs FTSE Cyclical indices and UK household income vs inflation

FTSE Defensive vs FTSE Cyclical TR, one year to 1 October 2015



UK household disposable income and CPI inflation, % change year-on-year



Source: Bloomberg, Asda income tracker, Office for National Statistics, Edison Investment Research

Fund profile: Focus on market leaders

Finsbury Growth & Income Trust (FGT) was launched in 1926. Since December 2000 its portfolio has been managed by Nick Train, a founding partner of Lindsell Train Investment Management. Previously known as Finsbury Growth Trust, the trust took on its current name in 2004 to reflect its total return focus. The manager takes a very long-term approach to investing in mainly UK companies with market-leading brands and strong intellectual property; turnover is extremely low although significant issuance in response to investor demand has seen the trust grow by c £100m in 2015 to date. Frostrow Capital acts as the alternative investment fund manager (AIFM) under the AIFM Directive (AIFMD) and also provides company secretarial, administration and marketing services.

The fund manager: Nick Train

The manager's view: First new position since 2011

The FGT portfolio is very stable, in line with manager Nick Train's long-term investment approach, so the purchase of a new stock is a major event. The last new position taken was in Heineken, in 2011, and the recent purchase of a small stake (c 1.5% of the portfolio at the time of writing) in Rémy Cointreau adds another overseas-listed global drinks brand.

Train draws parallels between the purchases of Heineken and Rémy: both have a stable of market-leading drinks brands, both stocks were added during a period of market dislocation, and both are long-established companies (Heineken was founded in 1864 and Rémy in 1724), which retain a controlling family shareholding. The manager says family-owned companies sit well with FGT's long-term approach, as they tend to be run with the aim of ensuring wealth is passed from one generation to the next, rather than in response to short-term management incentive schemes. Rémy – whose brands include Cointreau, Mount Gay rum and Bruichladdich single malt whisky, as well as its portfolio of high-end cognacs – has seen its earnings and share price suffer because of exposure to China (c 35% of 2013/14 operating profit), where worries over economic growth have added to the headwinds already faced by luxury brands because of the government's anti-bribery drive. The shares were purchased at a P/E of c 27x, having fallen in price by c 30% over the summer.

The new position was largely funded by a special capital dividend paid out earlier in the summer by Kraft Heinz under the terms of its merger, providing an unanticipated block of liquidity. It takes FGT's portfolio towards the 20% limit for overseas-listed stocks; Train says that while he is generally uncomfortable taking the trust too far off-benchmark, he is willing to compromise in the case of truly exceptional franchises, where there is an opportunity in terms of valuation.

In terms of the macro environment, Train says he is hopeful that the wider market will begin to share his view that lower oil and commodity prices are a positive economic signal – leading to higher disposable incomes and boosting consumer stocks – rather than a signal of a global slowdown or recession. The behaviour of supposedly 'defensive' stocks such as consumer staples in the late August sell-off suggested the market was more focused on downside risks from higher US interest rates affecting emerging economies, although defensives have since bounced back strongly versus cyclicals (see Exhibit 2). However, difficulties for emerging markets and their currencies may put downward pressure on dividend growth for companies such as Diageo, Heineken and Unilever in the short to medium term.

Asset allocation

Investment process: High conviction with low turnover

Manager Nick Train has described his investment approach – influenced by long-term value investors Sir John Templeton and Warren Buffett – as 'buy great companies and hold them forever'. Rather than taking tactical or macro views, Train seeks to own quality stocks that can grow and compound over time. Fundamental analysis is used to assess whether a company is undervalued relative to its long-term prospects, and Train is prepared to wait for attractive companies to reach equally attractive valuations. The concentrated nature of the portfolio (25-30 stocks) allows each holding to make a meaningful contribution, and positions are broadly sized according to the market capitalisation and liquidity of the companies held, with FTSE 100 stocks making up the majority of the top 10 holdings, and FTSE 250 (or equivalent-sized) stocks the bulk of the next 10. Of the six non-UK companies held, only the two newest holdings – Rémy Cointreau and Heineken – were actively bought for the portfolio; the remainder are former UK stocks that have been acquired by overseas companies.

Train says the kind of companies he likes to own are those with strong brands and enduring intellectual property. The manager has a total return rather than a purely income or growth focus, and favours firms that have predictable cash flows and are not excessively levered. In keeping with the ultra long-term approach, turnover is extremely low, with the last full exit from a stock taking place in 2013. Gearing is used to provide flexibility rather than as a bet on market direction or a way of increasing conviction in individual positions: the portfolio is already 'high conviction' owing to its level of concentration.

Current portfolio positioning

At 30 September 2015 FGT had 28 holdings: 25 mainstream equities plus small positions in the Lindsell Train Investment Trust, the unlisted Frostrow Capital (the trust's alternative investment fund manager, or AIFM) and cumulative convertible preference shares of Celtic FC. The stock list has increased from 27 as a result of the new position in French-listed Rémy Cointreau, FGT's first new holding since 2011.

The addition of the new stock takes the non-UK exposure from c 16.5% to c 18%, close to the 20% limit. (Aggregate exposure can go above 20% as a result of rising share prices but a further purchase could not be made that would breach the 20% barrier.) The last new purchase – Heineken, in 2011 – was also a non-UK stock: evidence, says Train, that he has been unable to find a sufficiently attractive UK-based candidate for the portfolio for some time. Geographically the trust now has six non-UK holdings, three of which (Kraft Heinz, Mondelēz and Dr Pepper-Snapple) are the products of a holding in Cadbury-Schweppes, while Canadian media company Thomson Reuters has been held since before Thomson's takeover of London-listed Reuters.

Exhibit 3: Sector allocations as at 31 August 2015

	Portfolio weight (%)	Change since 28 Feb (%)	FTSE All-Share weight (%)	Trust active weight (%)
Consumer goods	41.9	1.1	15.2	26.8
Consumer services	26.2	-0.8	12.6	13.7
Technology	9.7	0.0	1.6	8.1
Utilities	0.0	0.0	3.7	-3.7
Financials	22.2	-0.3	26.3	-4.1
Telecommunications	0.0	0.0	5.2	-5.2
Basic materials	0.0	0.0	5.5	-5.5
Healthcare	0.0	0.0	8.6	-8.6
Industrials	0.0	0.0	10.4	-10.4
Oil & gas	0.0	0.0	11.0	-11.0
	100.0	**0.0**	**100.0**	**0.0**

Source: Finsbury Growth & Income Trust, FTSE, Edison Investment Research. Note: Ranked by active weight.

The portfolio is concentrated into just a few sectors: consumer goods and services, financials and technology. This level of specialisation results in significant divergences from the benchmark FTSE All-Share index weightings (Exhibit 3). The exposures reflect a number of broad themes but all are predicated on holding companies with market-leading franchises. Consumer goods holdings are mainly focused on staples (the diversified Unilever and a selection of food and drinks companies), along with consumer discretionary stock Burberry, held not just because of its strong brand position but also its innovative use of technology, a theme that runs throughout the portfolio.

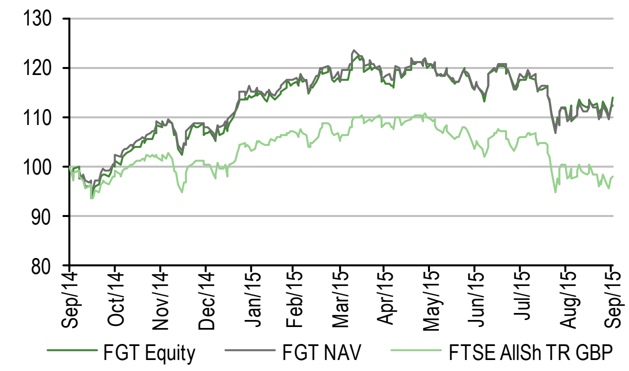
Consumer services stocks are principally in media (22.8% out of 26.2%, and another area where the use of technology is fundamental to the investment case) and leisure (pub and brewery companies as well as a small holding in Celtic FC). The financials weighting is concentrated in what the manager views as proxies for the stock market, namely asset and wealth managers, as well as the London Stock Exchange; the technology exposure is made up of business software firm Sage, and Fidessa, a developer of trading and investment software for the financial services industry.

Recent portfolio activity has seen Train top up holdings in the majority of the top 10 stocks with the exception of Pearson, funded partly by the £100m-plus of new share issuance in 2015 to date, and partly by a special capital distribution paid by Kraft under the terms of its merger with Heinz.

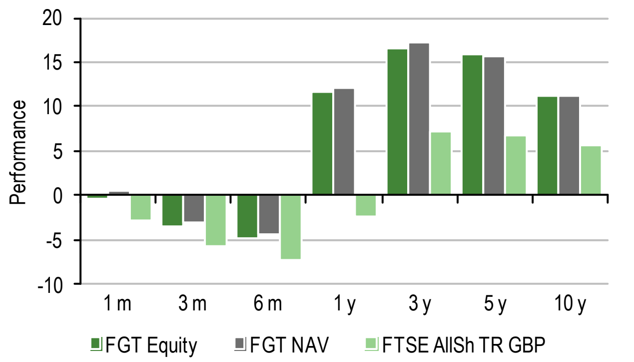
Performance: Outperforming over all periods

Exhibit 4: Investment trust performance to 30 September 2015

Price, NAV and benchmark total return perf, one year rebased



Price, NAV and benchmark total return performance (%)*



Source: Thomson Datastream, Edison Investment Research. Note: *Three, five and 10 years annualised.

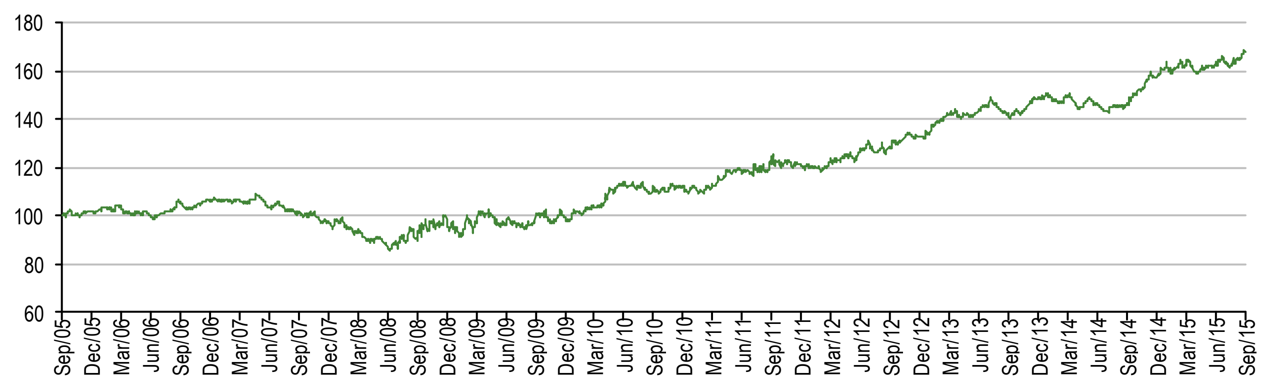
FGT has a very strong long-term performance record, both in absolute terms and relative to the FTSE All-Share index (Exhibit 4), producing annualised returns in excess of 10% over 10 years. In terms of more recent performance, the trust's portfolio is biased towards large caps and defensive sectors such as consumer staples, both areas that suffered in late summer market volatility. Some 60% of the portfolio is in FTSE 100 companies; this is below the 79% weighting of blue-chip stocks in the All-Share, however, and may have helped FGT to outperform the benchmark (even though absolute performance has been flat to negative) over recent periods. Train notes that stocks such as Unilever and Diageo – FGT's two largest holdings, accounting for 17.5% of the portfolio – did not prove altogether defensive in the recent sell-off, as fears of slowing growth in China affected stocks with emerging markets (EM) exposure, exacerbated by falls in EM currencies. While these factors may have contributed to slightly negative NAV performance versus comparator indices in August, outperformance persists over all other periods, relative both to the FTSE All-Share benchmark and other UK and global comparators (Exhibits 5 and 6).

Exhibit 5: Share price and NAV total return performance relative to benchmarks (%) to 30 September 2015

	One month	Three months	Six months	One year	Three years	Five years	10 years
Price relative to FTSE All Share	2.4	2.5	2.6	14.4	28.5	50.9	66.7
NAV relative to FTSE All Share	3.2	2.8	2.9	14.7	30.7	49.6	68.2
Price relative to FTSE 350	2.5	2.6	2.8	14.7	29.3	51.8	66.8
NAV relative to FTSE 350	3.3	2.9	3.2	15.0	31.4	50.5	68.3
Price relative to MSCI World index	1.8	1.5	5.5	9.4	14.2	31.0	46.6
NAV relative to MSCI World index	2.6	1.9	5.8	9.7	16.1	29.8	47.9

Source: Thomson Datastream, Edison Investment Research. Note: Geometric calculation.

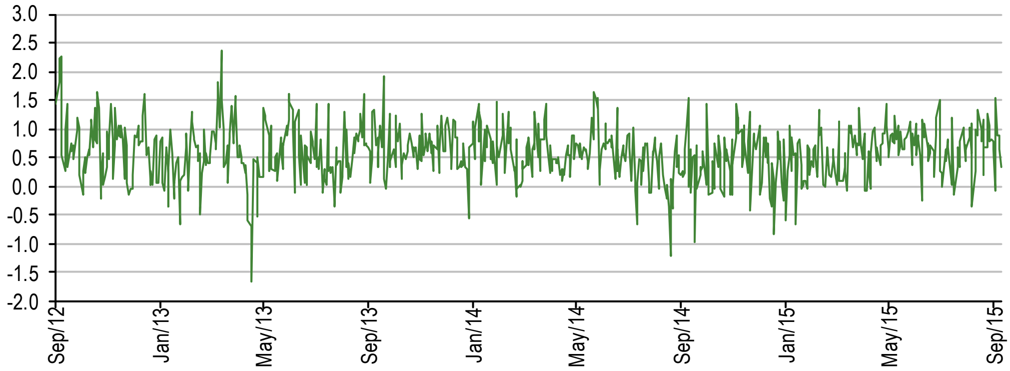
Exhibit 6: FGT NAV total return vs FTSE All-Share total return, over 10 years, rebased to 100



Source: Thomson Datastream, Edison Investment Research

Discount: Active issuance keeps shares close to par

Exhibit 7: Discount/premium to cum-income NAV over three years



Source: Thomson Datastream, Edison Investment Research. Note: NAV with debt at fair value, including income.

FGT's discount control policy (see Capital structure, below), combined with strong demand for the shares, has seen it trade in a narrow band from a 1% discount to a 2% premium to cum-income NAV in recent years (Exhibit 7). The recent market volatility has had little noticeable effect on demand, and at 7 October the shares were trading at a 0.3% premium to net asset value, compared with average premiums over one, three and five years of 0.6%, 0.6% and 0.4% respectively.

Capital structure and fees

A conventional investment trust with one class of share, FGT had 121.2m ordinary shares in issue as of 5 October. Under its discount control policy the board will buy back shares if the discount exceeds 5% and will issue shares if there are unfulfilled buy orders in the market. Demand for the trust has remained strong even through the recent market volatility and FGT has issued 17.6m new shares so far in 2015, raising just over £100m.

The trust has a £50m revolving loan facility with Scotiabank, currently in its second of three years. At the 31 March half-year end £26.4m of this was drawn down, representing net gearing of 3.7%; at 31 August gearing was 3.0%. The trust may gear up to a maximum of 25% of its net assets although in practice the manager says gearing is unlikely to rise substantially above 5%.

Lindsell Train is paid an annual fee of 0.45% of market capitalisation for providing portfolio management services, while Frostrow Capital, which acts as the alternative investment fund manager (AIFM) under the AIFM Directive, as well as providing company secretarial, administration and marketing services, receives a fee of 0.15% of market cap plus £70,000. Ongoing charges for the year ended 30 September 2014 were 0.8%.

Dividend policy and record

FGT pays two dividends a year, in May and October. It has a progressive dividend policy and has raised its payout in each of the last five years. The second interim dividend of 6.6p announced on 23 September in respect of FY15 (year ending 30 September) brings the total dividend for the year to 12.1p per share, a 7.1% increase on the 11.3p per share paid for FY14. Dividends have grown at a compound annual rate of 5.6% over five years, compared with CPI inflation at a compound 2.9% pa over the same period. Based on the FY15 dividend and the 7 October share price of 578p, FGT currently yields 2.1%, which is low for the UK equity income sector, but should be seen in the context of the trust's mandate to achieve capital growth as well as income: over five years FGT has produced an NAV total return of 112.9% compared with the peer group average of 79.9%.

Peer group comparison

There are 25 funds in the AIC's UK Equity Income sector, encompassing a broad range of investment approaches; Exhibit 8 below shows the 11 largest. In spite of recent market volatility, almost all the peer group have produced a positive return over 12 months, with FGT ranked second of the large trusts and fifth overall. Over three and five years it is fifth and second overall, or third and first of the large trusts. Risk-adjusted performance as measured by the Sharpe ratio is top quartile over one and three years. FGT's yield is the lowest in the sector at 2.1%, understandable given its total return rather than specifically income mandate. Ongoing charges are broadly average, while gearing is below average. Issuance has helped keep a lid on FGT's premium to NAV; eight of the peers are on a larger premium, though the average is a 0.9% discount.

Exhibit 8: UK Equity Income investment trusts

% unless stated	Market cap (£m)	TR one year	TR three years	TR five years	Ongoing charge	Perf. fee	Discount (-) /premium	Net gearing	Yield	Sharpe NAV 1 yr	Sharpe NAV 3 yrs
Finsbury Growth & Income	**681.8**	**17.1**	**59.7**	**112.9**	**0.8**	**No**	**0.5**	**103.0**	**2.1**	**0.9**	**1.3**
City of London	1227.0	9.8	39.6	73.6	0.4	No	2.1	109.0	3.9	0.4	1.0
Diverse Income Trust	356.6	22.3	85.3		1.3	No	2.1	99.0	2.7	2.9	2.8
Dunedin Income Growth	352.6	-1.6	19.5	43.3	0.6	No	-7.2	109.0	4.9	-0.5	0.4
Edinburgh Investment	1383.4	16.2	54.4	100.0	0.6	No	2.3	114.0	3.4	0.9	1.2
JPMorgan Claverhouse	319.3	7.1	44.9	58.3	0.7	Yes	-6.5	117.0	3.7	0.2	1.0
Lowland	359.0	5.5	44.9	102.7	0.6	Yes	-1.4	117.0	3.1	0.0	1.0
Merchants Trust	474.3	2.3	24.5	52.3	0.6	No	-4.9	120.0	5.6	-0.2	0.6
Murray Income Trust	468.1	0.7	23.0	48.7	0.7	No	-6.2	107.0	4.7	-0.5	0.6
Perpetual Income & Growth	981.5	13.0	62.3	104.0	0.7	Yes	1.0	118.0	3.4	0.8	1.6
Temple Bar	718.2	-1.0	28.0	62.8	0.5	No	-3.2	100.0	3.7	-0.6	0.7
Weighted average (25 fds)		**9.9**	**45.1**	**79.9**	**0.7**	**0.0**	**-0.9**	**110.3**	**3.8**	**0.5**	**1.1**
FGT rank out of 25	**5**	**5**	**5**	**2**	**14**		**9**	**17**	**25**	**6**	**5**

Source: Morningstar, 5 October 2015, Edison Investment Research. Note: Excludes trusts with less than £300m market cap. TR = NAV total return. The Sharpe ratio is a measure of risk-adjusted return. The ratios we show are calculated by Morningstar for the past 12- and 36-month periods by dividing a fund's annualised excess returns over the risk-free rate by its annualised standard deviation. Net gearing is shown here as total assets less cash/cash equivalents as a percentage of shareholders' funds. 100 = ungeared.

The board

FGT has six directors, all non-executive and independent of the manager. Anthony Townsend, the chairman since 2008, joined the board in 2005. John Allard and Vanessa Renwick were both appointed in 2000. David Hunt became a director in 2006 and Neil Collins joined the board in 2008. In May 2015, Simon Hayes was appointed as a director, bringing the number of board members back up to six for the first time since the unexpected death of Giles Warman in 2013.

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