Finsbury Growth & Income Trust

Investment trusts review

Edison investment research

Continued strong performance

Investment trusts

Finsbury Growth & Income Trust's (FGT) good performance has continued during the last year with FGT outperforming its benchmark, the FTSE All-Share Index, by 7.6% and 6.9% in terms of price total return and NAV total return respectively. The fund has an experienced investment management team and uses a bottom-up strategy to invest in quality companies that are then held for the long term. There is a strong focus on businesses with strong franchises that are well managed, which are held for the long term. FGT maintains a focused portfolio of 25-30 stocks with low turnover (c 6% per annum), which is moderately geared and aims to have an above-average dividend yield. During the last 10 years, FGT has outperformed the FTSE All-Share by 178.0% and 117.5% in terms of price and NAV total return respectively.

12 months ending	Total share price return* (%)	Total NAV return* (%)	Total return FTSE All-Share * (%)	Total return FTSE 350 Index* (%)	Total return MSCI UK Index* (%)
22/10/2009	40.5	43.0	36.9	36.8	35.2
22/10/2010	27.6	27.1	14.7	14.8	13.7
22/10/2011	12.9	8.5	(1.5)	(1.4)	(0.9)
22/10/2012	20.4	19.6	12.8	12.6	11.6

Note: *Twelve-month rolling discrete performance.

Investment strategy: Undervalued quality UK-listed companies

FGT invests in large and medium-sized companies listed primarily on the UK equity markets. The manager subscribes to the Buffet doctrine and looks for long-term winners able to withstand economic down cycles. Typically these will have strong business franchises and sound management, will be acquired with patience when deemed to be underpriced and held with great conviction over the longer term (average annual portfolio turnover is just over 6%). The portfolio currently consists of 26 holdings. Between 50% and 100% of the portfolio is invested in FTSE 100 stocks and at least 70% invested in FTSE 350 stocks. FGT's portfolio is not strongly correlated with any benchmark. FGT is mandated to be permanently geared. Net gearing is currently 5.2%, but can range between 5% and 20% of net assets.

Sector outlook: Insulated from economic headwinds

The stock picking approach of Lindsell Train, the investment manager, looks to provide FGT with a portfolio of quality companies to be held over the long term. The current economic environment remains a headwind to business but, by design, FGT's portfolio should be relatively resilient to harsh economic conditions.

Valuation: FGT remains on premium rating

FGT's discount management policy (repurchasing shares at discounts above 5% and issuing new shares at a 0.5% premium) continues to be effective and offers investors confidence that they will be able to enter and exit at valuations around this level. FGT's current premium of 1.2% reflects a stronger rating than its three- and five-year discount averages of 0.5% and 1.9% respectively, but remains comparable. As such, we believe FGT may be of interest to investors looking for long-term value plays on the UK.

1 November 2012

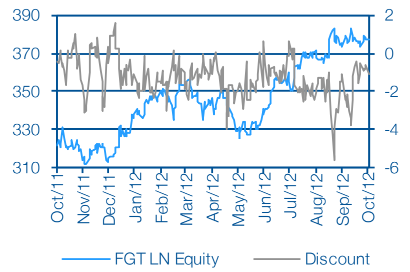
Price	372.8p
Market cap	£258m
AUM	£273m
NAV*	368.36p
Premium to NAV	1.2%
NAV**	368.96p
Premium to NAV	1.0%
Yield	2.5%

** Adjusted for debt at par value and excluding income, as at 24 October 2012.*

*** Adjusted for debt at market value, excluding income, as at 24 October 2012.*

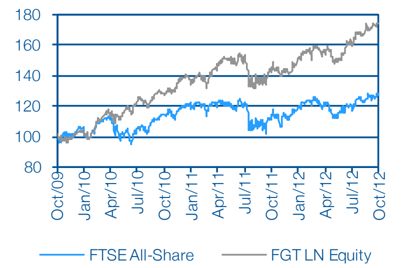
Ordinary shares in issue	63.0m
Code	FGT
Primary exchange	LSE
AIC Sector	UK Growth & Income

Share price/discount performance



** Positive values indicate a discount; negative values indicate a premium*

Three-year cumulative performance



52-week high/low	383p	312p
NAV* high/low	376.26p	302.99p

** Adjusted for debt at market value, excluding income.*

Gearing

Gross	6.1%
Net	5.2%

Analysts

Matthew Read +44 (0)20 3077 5758
Martyn King +44 (0)20 3077 5745
investmenttrusts@edisoninvestmentresearch.co.uk
Edison profile page

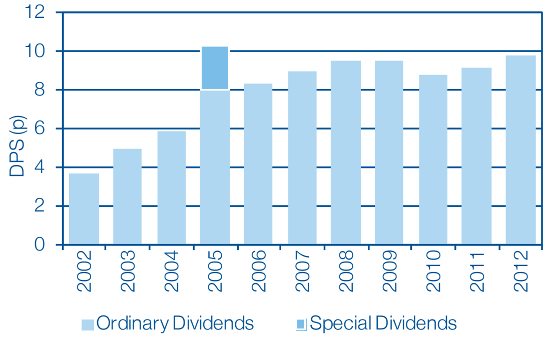
Finsbury Growth & Income Trust is a research client of Edison Investment Research Limited

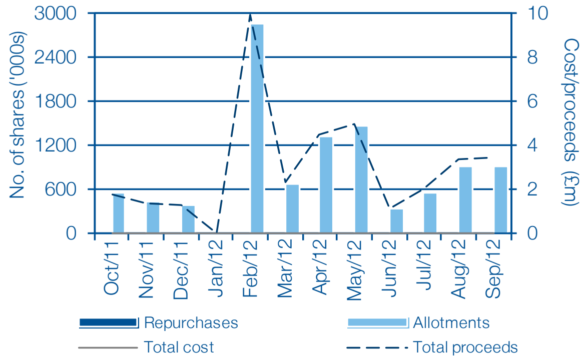
Exhibit 1: Trust at a glance

Investment objective and fund background	Developments last quarter
FGT's investment objective is to achieve capital and income growth and provide shareholders with a total return over that of the FTSE All-Share Index. It invests principally in the securities of UK-quoted companies, but up to a maximum of 20% can be invested in non-UK quoted companies at acquisition. FTSE 100 companies normally represent 50-100% of the portfolio, with at least 70% usually invested in FTSE 350 companies.	3 October 2012: Second interim dividend of 5.2p, for the year ended 30 September 2012, went xd. To be paid 2 November 2012 30 August 2012: Mrs C Townsend (wife of the chairman) purchased 7,300 shares.

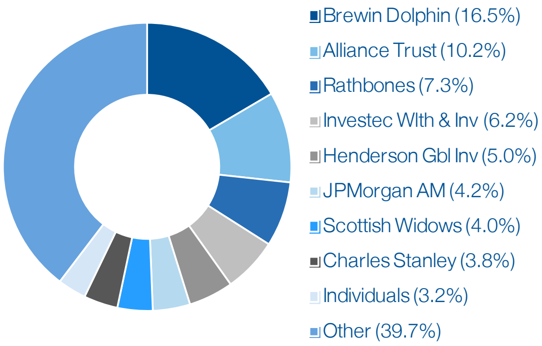
Forthcoming		Capital structure		Fund details	
AGM	January 2013	Total expense ratio	1.0%	Group	Frostrow Capital LLP
Preliminary results	December 2012	Net gearing	5.2%	Invest. mgr.	Lindsell Train
Year end	30 September	Annual mgmt fee	£70k+0.6% mkt cap	Address	25 Southampton Buildings, London WC2A 1AL
Dividend paid	May, October	Performance fee	15% above RPI + 6%		
Launch date	January 1926	Trust life	Indefinite	Phone	+44 (0)20 3008 4910
Wind-up date	None	Loan facilities	£20m revolving	Website	www.finsburygt.com

Dividend policy and history	Share buy-back policy and history
Two dividends annually, paid in May and October. The dividend is expected to rise over the longer term.	Renewed annually, the trust has authority to purchase up to 14.99% and allot up to 10% of issued share capital.

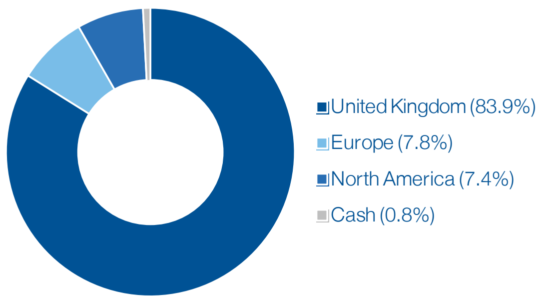




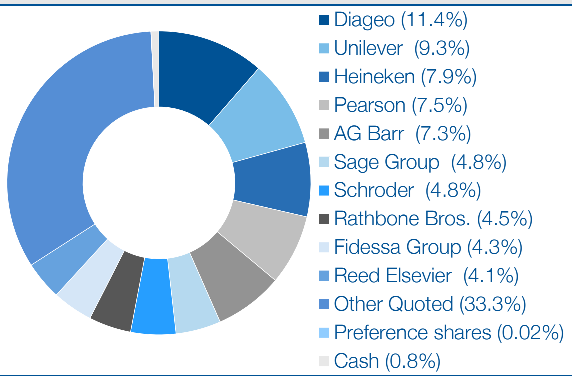
Shareholder base (as at 30 September 2012)



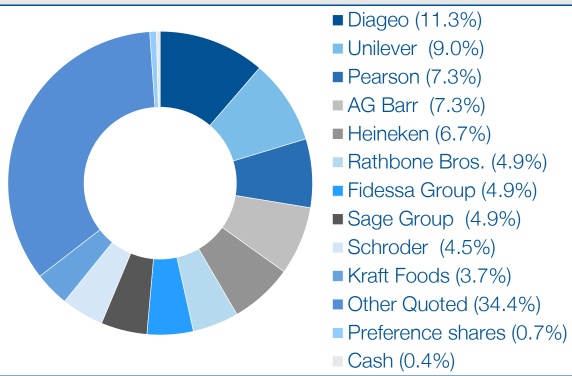
Geographic distribution of portfolio (as at 30 September 2012)



Portfolio composition (as at 30 September 2012)



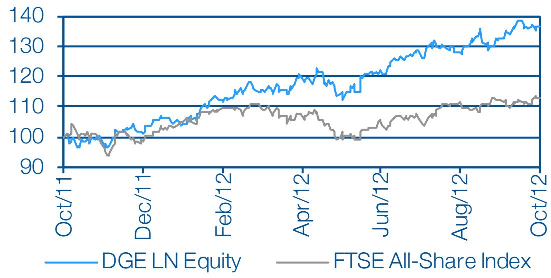
Portfolio composition (as at 31 March 2012)



Source: Finsbury Growth & Income Trust, Edison Investment Research

Exhibit 2: Top five holdings at a glance

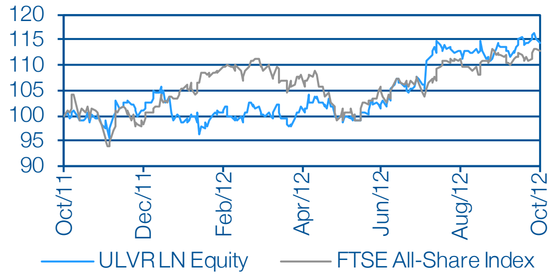
Diageo	Code: DGE LN	Market cap: £44,451m



Div yield (trail. 12 months)	2.45%
Industry/Sector	Beverages – wine/spirits
Listing	LSE – Premium listing
Website	www.diageo.com

The manager considers Diageo is a unique collection of global drinks businesses, with excellent franchises, that offer good inflation protection. Its brands include Johnnie Walker, Crown Royal, J&B, Buchanan's, Bushmills, Smirnoff, Ciroc, Baileys, Tanqueray and Guinness. The manager considers Diageo has been undervalued allowing FGT to build a position at dividend yields that are between 10% and 15% above the market average.

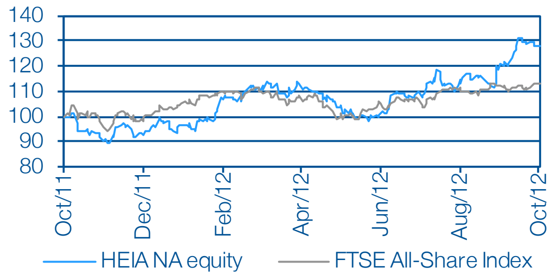
Unilever	Code: ULVR LN	Market cap: £68,282m



Div yield (trail. 12 months)	3.34%
Industry/Sector	Food – misc/diversified
Listing	LSE – Main market
Website	www.unilever.com

Unilever (ULVR) is a British-Dutch consumer goods company. The manager considers that Unilever provides exposure to a very extensive range of durable global consumer brands. Its food brands include Flora, Bertolli, Blue Band, Rama, Heartbrand, Hellman's, Knorr, Lipton and Slim Fast. Home care includes Omo, Surf, Comfort and Cif. Personal care includes Axe, Dove, Lux, Pond's, Rexona and Sunsilk. Unilever has operations in over 100 countries and sales in 180 countries.

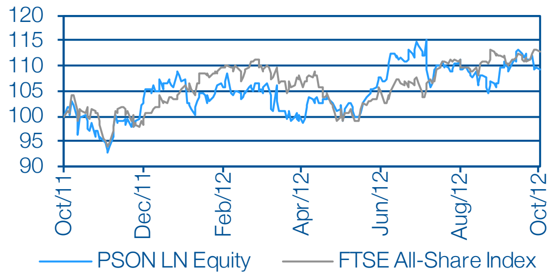
Heineken	Code: HEIA. NA	Market cap: €27,562m (£22,468m)



Div yield (trail. 12 months)	1.80%
Industry/Sector	Beverages/brewery
Listing	Euronext Amsterdam
Website	www.heinekeninternational.com

Heineken NV is an international brewer with a very extensive portfolio of global beer brands. The group sells over 200 beers and ciders, which include international premium, regional, local and speciality brands. The manager considers that Heineken is highly profitable, very cash generative and that the purchase of Asia Pacific Breweries in September is a very positive development. FGT began building its position, at very attractive prices, following market falls in August 2011.

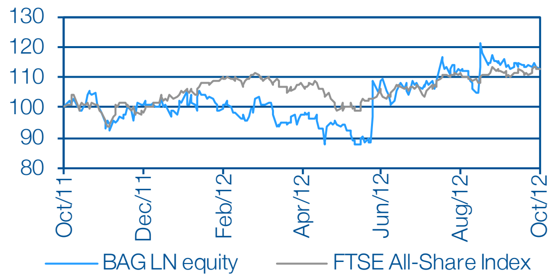
Pearson	Code: PSON LN	Market cap: £9,902m



Div yield (trail. 12 months)	3.55%
Industry/Sector	Multimedia
Listing	LSE – Premium listing
Website	www.pearson.com

The manager considers Pearson, which is structured around three key lines (education, Penguin Books and financial publishing), has a collection of media brands with excellent long-term durability. Education includes Longman, a mainstay of education text books in the UK, which the manager considers has strong brand recognition and financial publishing includes the Financial Times Group and a 50% stake in The Economist.

A G Barr	Code: BAG LN	Market cap: £518m



Div yield (trail. 12 months)	2.14%
Industry/Sector	Beverages – non-alcoholic
Listing	LSE – Premium listing
Website	www.agbarr.co.uk

A G Barr (BAG) is engaged in the manufacture, distribution and retailing of soft drinks. Organised around two business segments, Carbonates and 'still drinks and water', its brands include IRN-BRU, Rubicon, Strathmore, Tizer, Simply, KA, D'N'B, St. Clement's, Findlays, Abbott's, Barr Brands, Vitsmart and Taut. The manager considers that BAG has been a fantastic investment for FGT, which has quintupled in value since 2001, against a backdrop of a challenging decade.

Source: Finsbury Growth & Income Trust, Thomson Datastream, Edison Investment Research

Fund profile: Low turnover, long-term value play

FGT was launched in 1926 and Nick Train, co-founder of Lindsell Train, has managed the portfolio since December 2000. The manager takes a value-oriented investment approach with a long time horizon and low portfolio turnover (turnover has averaged just over 6% per year since December 2001 when the manager finished rebalancing the portfolio). During the 10 years to 19 March 2012, FGT has outperformed its benchmark, the FTSE All-Share, by 117.5% in terms of NAV total return and 178.0% in terms of share price total return.

Equity outlook

Edison's strategist, Alastair George, points out that equities appear good long-term value as risk-free rates of return have declined to historic lows across the yield curve. Unusually, there is now a significant yield advantage in favour of quality blue-chip non-financial equities compared to 10-year government bonds. If current dividend levels are maintained, it is difficult to see how such stocks will underperform bonds over the next 10 years, but the risk clearly lies in the dividend level, which in turn relies on corporate profitability.

The fund manager: Nick Train

The manager's view: Portfolio resilient to economic headwinds

The manager believes he is best able to exploit the opportunity in equity investment by seeking to identify companies that have the strength of franchise and strength of management to be able to benefit from secular growth trends and technological advance. Economic and market circumstances will ebb and flow, but the same attributes that allow these companies to prosper in good times also provide support, to profitability, cash flow and dividends in harsher times. Such stocks clearly exist; the challenge for any investor is to identify and stick with them. It is this process that the manager is very clearly focused on as a route to creating long-term portfolio returns.

Asset allocation

Investment process: Bottom-up fundamental analysis

FGT is managed using bottom-up fundamental analysis. The manager's approach to investing has been heavily influenced by the investment approach of Berkshire Hathaway. There are four key tenets to Lindsell Train's investment philosophy for managing FGT:

- The manager attempts to invest only in businesses that are deemed to be really exceptional. A key filter question is, "How likely is a business to be very profitable in 20 years' time?" To pass, a business must have something that truly differentiates it: either fantastic brands or exceptionally durable market franchises. As a result, FGT's portfolio has a bias towards the consumer sectors, which historically have had some very durable brands.
- FGT runs a concentrated portfolio. This is a reflection of the first tenet as well as the requirement that, as a long-term investor, the manager looks for particularly attractive entry points in terms of valuations. However, the manager considers that when such opportunities arise, the logical conclusion is to build solid positions.
- The manager takes a long-term strategic view of trust holdings and considers FGT's stakes as semi-permanent ownership positions in companies. The manager then expects returns to feed through as

multiple gains on the original investment. The manager is not looking for the next 20% to 30% price shift. Instead, he looks for businesses that have the potential to double, treble, quadruple or more in price. The manager recognises that this will take time. Low turnover and thus low transaction costs are the positive side effects of this policy.

- The manager is very interested in capturing dividends and growth in dividends. As such, the manager looks for companies with strong cash generation, defensive earnings and strong franchises that will allow companies to increase dividends over the long term.

As a result, the asset allocation is a relatively simple process. When adding a new FTSE 100 stock, the manager would look to build a minimum position of between 4% and 6% of FGT's NAV. Mid-cap stocks (ie sub-£1bn market cap) receive an initial allocation of between 2% and 4% of FGT's NAV. Although rare, the manager will also consider small-cap stocks but, recognising liquidity constraints, the starting allocation would be limited to 1% of FGT's NAV. As a result, while FGT is benchmarked against the FTSE All-Share, it has a portfolio that is radically different in its composition.

Overview: Highly-focused UK equity portfolio

FGT has 24 equity investments and, following the sale of its Lloyds Group preference shares, has one preference share holding in the portfolio, in Celtic, which represents 0.02% of total assets. The top 10 equity holdings account for 65.9% of the portfolio, cash 0.8%, with the remaining 14 equity investments accounting for 33.3%. As displayed in Exhibit 3, FGT's asset allocations can vary significantly from those of the benchmark index, reflecting the actively-managed nature of the trust.

FGT has a zero allocation to oil and gas, basic materials, industrials, healthcare, telecommunications and utilities sectors that collectively represent c 58% of the index. It retains its substantial overweights in consumer goods, consumer services and technology, with allocations c 3.1x, 3.2x and 7.4x those of the benchmark. FGT is also marginally overweight financials. As Exhibit 3 illustrates, FGT's portfolio has a radically different allocation to that of its benchmark, the FTSE All-Share. In addition, the manager has given FGT's portfolio a growth-oriented bias, relative to the benchmark, by underweighting defensive and overweighting cyclical sectors.

Exhibit 3: Sector allocations as at 30 September 2012

	Trust weight (%)	Benchmark weight (%)	Trust active weight (%)	Trust weight/ benchmark weight
Consumer goods	43.4	14.2	29.2	3.05
Consumer services	29.5	9.3	20.2	3.17
Technology	8.9	1.2	7.7	7.44
Financials	17.5	17.3	0.2	1.01
Utilities	0.0	3.2	(3.2)	0.00
Telecommunications	0.0	5.3	(5.3)	0.00
Healthcare	0.0	6.1	(6.1)	0.00
Industrials	0.0	7.5	(7.5)	0.00
Basic materials	0.0	15.1	(15.1)	0.00
Oil and gas	0.0	20.8	(20.8)	0.00
Cash	0.8	0.0	0.8	N/A
Total	**100.0**	**100.0**	**0.0**	

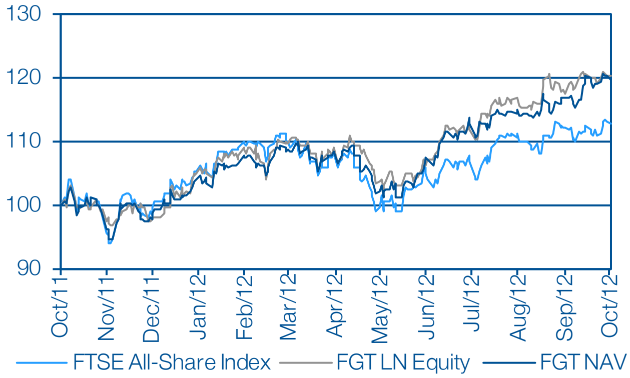
Source: Finsbury Growth & Income Trust, Edison Investment Research

Recent performance: Consistent outperformance

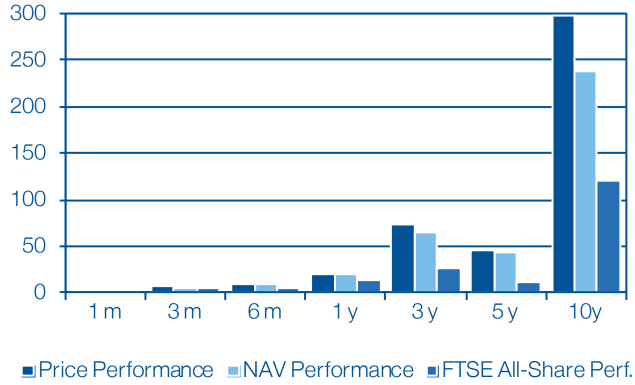
As Exhibits 4 and 5 illustrate, FGT has given a consistent long-term performance, outperforming its benchmark, the FTSE All-Share index, in terms of both price and NAV over all the time periods provided. In reality, the concentrated nature of FGT's portfolio, in terms of both number of stocks and sectoral allocation, means that performance can suffer in the short term because of stock-specific or sectoral-specific events. However, the performance figures in Exhibit 5 clearly illustrate the effectiveness of the strategy over the long-term time horizons, which we consider to be more relevant in evaluating FGT's performance.

Exhibit 4: Investment trust performance

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



Price, NAV and benchmark total return performance (%)



Source: Finsbury Growth & Income Trust, Thomson Datastream, Edison Investment Research

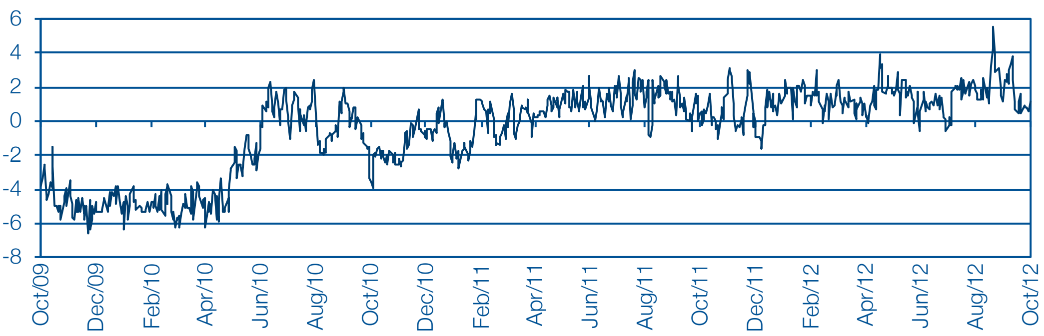
Exhibit 5: Share price and NAV (with debt valued at par) total return performance (sterling adjusted), relative to benchmarks

	One month	Three months	Six months	One year	Three years	Five years	10 years
Price relative to FTSE All-Share	1.7	2.1	5.9	7.6	46.1	33.9	178.0
NAV relative to FTSE All-Share	1.7	0.3	5.9	6.9	37.6	31.9	117.5
Price relative to FTSE 350 High Yield	1.7	2.2	6.0	7.8	46.0	33.5	178.2
NAV relative to FTSE 350 High Yield	1.8	0.4	5.9	7.0	37.4	31.4	117.7
Price relative to MSCI UK Index	1.8	2.8	6.2	8.8	47.8	35.3	193.3
NAV relative to MSCI UK Index	1.9	1.0	6.2	8.1	39.2	33.2	132.8

Source: Finsbury Growth & Income Trust, Thomson Datastream, Edison Investment Research

Discount: Effective discount management policy

Exhibit 6: Discount/premium through three years



Source: Finsbury Growth & Income Trust, Thomson Datastream, Edison Investment Research. Note: Positive values indicate a premium; negative values indicate a discount.

FGT has an active discount-management policy aimed at protecting shareholders from discount volatility. FGT actively repurchases shares into treasury when they are offered at a discount greater than 5.0%. It reissues shares from treasury at a discount of less than 5.0% and issues new shares at a 0.5% premium. Exhibit 6, which shows the discount of the trust over the last three years, illustrates that this policy has been effective. FGT's discount volatility increased after the financial crisis, but the increase was comparatively mild and short lived when compared to many trusts and was not accompanied by the general widening seen elsewhere in the sector. FGT's average discount over the last three years is 1.5%. With FGT trading at a premium for most of the period, there have been no share repurchases since April 2010. This has given FGT the opportunity to issue stock and, as illustrated in Exhibit 1, FGT has continued with its programme of allotments, issuing 10.5m shares and raising £36.4m during the last 12 months. The current premium of 1.2% reflects a higher rating than its three-year and five-year discount averages of 0.5% and 1.9% respectively.

Capital structure: Conventional, moderate gearing

FGT is a conventional trust, having only one class of share in issue – 25p ords. It can gear up to 25% of net assets and has a £20m revolving credit facility with Scotiabank Europe for this purpose. The board considers that, over the long term, moderate gearing is value enhancing and has mandated that FGT should be permanently geared. If the gearing falls below 5% or rises above 20% of net assets, the manager must provide an explanation to the board. This band gives FGT sufficient flexibility in choosing its gearing policy and, to date, has remained within these boundaries. As at 30 September 2012, we calculate that FGT had gross gearing of 6.1% and net gearing of 5.2% of net assets.

The annual management fee is split between Frostrow (responsible for administration, secretarial and marketing services) and Lindsell Train, the investment manager. Frostrow receives a fixed amount of £70,000 per year plus 0.15% of the company's market capitalisation per year, calculated monthly and payable monthly in arrears. Lindsell Train receives a management fee of 0.45% of the company's market capitalisation per year, also calculated monthly and payable monthly in arrears. The trust also pays a performance fee amounting to 15% of the annual increase in the company's adjusted market capitalisation per share, subject to an absolute return hurdle, which is the sum of the increase in the Retail Price Index (RPI) in the year, plus a fixed return of 6%. Where a performance fee is payable, the investment manager (Lindsell Train) receives 85.0% and the manager (Frostrow Capital) receives 15.0% of the performance fee. The total performance fee payable in any one year is capped at 1.25% of FGT's market capitalisation, with any surplus carried forward into the calculation of future years' fees. Similarly, any underperformance must be recovered before a performance fee can be accrued. For the year ended 30 September 2011, the RPI rose by 5.59%, providing an increase in the market capitalisation performance hurdle for the year of 11.59% above the 2010 performance hurdle. The 2011 performance hurdle was 507.78p per share versus FGT's actual market capitalisation of 311.61p per share. No performance fee was accrued for the years ended 30 September 2009-11. The total expense ratio (TER) was 1.0% for the year ended 30 September 2011 (1.0% for the year ended 30 September 2010). The management contract can be terminated at one year's notice by either party. FGT does not have a fixed life and there is no specific mechanism to wind up the company.

Dividend policy and record

The company seeks to provide shareholders with long-term growth in dividends and two dividend payments are made each year. A first interim dividend is paid in May (2012 = 4.6p) and a second interim, in lieu of a final, is paid in October (2012 = 5.2p). For the year ending 30 September 2012, FGT paid a total dividend for the year of 9.8p (2011 = 9.2p), which represents a 6.5% rise year-on-year in total dividends. As Exhibit 1 illustrates, FGT has a progressive dividend policy. The dividend, which has risen by 161% during the last 10 years, has been maintained or increased every year with the exception of a 7.4% fall between 2009 and 2010 (9.5p to 8.8p) caused primarily by a substantial reduction in the level of income received from FGT's Lloyds preference. Payment of dividends for the years ended 30 September 2009 and 2010 required FGT to dip into its revenue reserves to the tune of £187k and £170k respectively, but the 2011 payment was fully covered (FGT earned 9.7p per share, paid out 9.2p and retained 0.5p, thus increasing revenue reserves by £160k). As at 30 September 2011, FGT had revenue reserves equal to 8.6p per share. Dividend growth has been strong during the last 12 months and the manager expects good, although not as strong, growth over the next year. We believe that FGT is well positioned to maintain the dividend at 9.8p and that a dividend increase for 2013 is not unlikely. In terms of expense allocation, transaction costs relating to the purchase and sale of investments and exchange gains/losses are charged to the capital account. Management fees and interest payable are charged one-third and two-thirds to the revenue and capital accounts, respectively. Performance fees are charged 100% to capital. While this offers capital less protection than if management fees and interest were charged predominantly, or exclusively, to the revenue account, it gives FGT greater flexibility to smooth dividends.

Peer group comparison

As Exhibit 7 illustrates, the AIC sector UK Growth and Income is a comprehensive peer group with 20 constituents (a sample is given below). Within this group, FGT ranks sixth over one year, second over three and five years when considering share price total return.

Exhibit 7: Global growth sector, as at 24 October 2012

Company	Share price total return on £100			Ongoing charges (%)	(Disc)/ prem.	Net gearing (100=no gearing)	Five-year dividend growth (%)	Div. yield
	One year	Three years	Five years					
Sector average	**112.5**	**149.3**	**125.7**	**0.77**	**0.5**	**112**	**1.5**	**4.2**
Finsbury Growth & Income	**118.0**	**169.2**	**142.6**	**0.98**	**1.1**	**105**	**0.6**	**2.6**
Dunedin Income Growth	108.0	144.8	112.5	0.65	(2.9)	109	(12.9)	2.2
Edinburgh Investment	110.7	163.8	138.4	0.72	5.6	121	2.0	4.4
F&C Capital & Income	111.9	128.2	115.8	0.81	0.7	103	1.9	3.9
Invesco Income Growth	118.6	153.3	115.8	0.99	(3.1)	110	2.6	4.2
Lowland	127.2	175.3	111.0	0.62	(0.3)	112	3.4	3.2
Merchants	103.1	133.5	102.9	0.64	(3.9)	124	1.6	6.3
Murray Income	109.8	145.7	119.7	0.79	0.8	106	2.0	4.5
Perpetual Income & Growth	114.1	154.2	136.0	1.00	0.1	116	6.8	3.9
Standard Life Equity Income	111.4	128.8	120.2	0.96	(6.2)	109	4.0	4.5
Troy Income & Growth	109.7	148.2	82.0	1.40	1.3	95	(17.5)	3.6
Value & Income	104.3	132.7	102.6	1.35	(21.6)	129	1.7	4.4

Source: The Association of Investment Companies

The board

All directors are non-executive and independent of the investment manager. They are: Anthony Townsend (chairman), John Allard, Neil Collins, David Hunt, Vanessa Renwick and Giles Warman. The average length of director service is 9.0 years.

Registered in England, number 4794244. Edison Investment Research is authorised and regulated by the Financial Services Authority.
www.edisoninvestmentresearch.co.uk

London +44 (0)20 3077 5700
Lincoln House, 296-302 High Holborn
London, WC1V 7JH, UK

New York +1 646 653 7026
245 Park Avenue, 24th Floor
NY 10167, New York, US

Sydney +61 (0)2 9258 1162
Level 33, Australia Square, 264 George St,
Sydney, NSW 2000, Australia