EDISON

Henderson International Income Trust

Dividends and growth from all-overseas portfolio

Investment trusts

16 December 2015

Henderson International Income Trust (HINT) is the only investment trust specifically targeting income by investing in companies outside the UK. Launched in 2011, it has provided year-on-year dividend growth and is also building a revenue reserve. While a structural underweight to the US and Japan (because these markets are low yielding) has dented relative performance in the period since launch, the trust has achieved its objective of providing capital and income returns at least equivalent to those available from the FTSE All Share. Manager Ben Lofthouse describes the trust as a "global best ideas" portfolio, with a flexible allocation between three main geographical areas of the Americas, Europe and Asia.

12 months ending	Share price (%)	Total NAV return (%)	MSCI World ex-UK (%)	FTSE All-Share (%)	MSCI World (%)
30/11/12	21.7	15.5	11.9	12.1	12.2
30/11/13	20.2	20.3	21.8	19.8	24.3
30/11/14	4.4	11.3	14.3	4.7	14.5
30/11/15	4.8	0.8	2.3	0.6	3.9

Note: Twelve-month rolling discrete £-adjusted total return performance.

Investment strategy: Seeking dividends and growth

Manager Ben Lofthouse, a member of Henderson's global equity income team, seeks to construct a portfolio of c 60 stocks, in three regional sub-portfolios (Americas, Europe and Asia), with a focus on finding undervalued companies that may contribute to capital growth, and well-managed, sustainably financed dividend payers with strong free cash flow yields. The portfolio aims to provide diversification for UK investors seeking overseas exposure, and targets a dividend yield at least equivalent to that available on UK equities.

Market outlook: Cast net wider for income

Alongside worries about growth in China, military action in the Middle East and how quickly the US Federal Reserve will act to normalise interest rates, concerns are emerging about the sustainability of dividends from larger UK companies. The level of dividend cover for the FTSE 100 has declined to less than 1.5x (the long-term median since 1970 is 2x), with specific areas of pressure such as oil companies, which have been boosted by a stronger dollar but are vulnerable to sustained oil price falls. Although earnings growth remains subdued in aggregate, some areas outside the UK (particularly in Asia and Japan) have seen strong annualised dividend increases, suggesting a broader geographical focus could be beneficial for income-seeking investors.

Valuation: Close to par after supply-driven widening

At 14 December HINT's shares traded at a 0.5% premium to cum-income net asset value. On average the trust has enjoyed a premium rating since launch, although a temporary supply glut in September 2014 caused by the final exercise of subscription shares saw it move to a discount of c 8% before settling back at around par. The board actively issues shares to manage the premium, and may also use buybacks should a persistent discount arise.

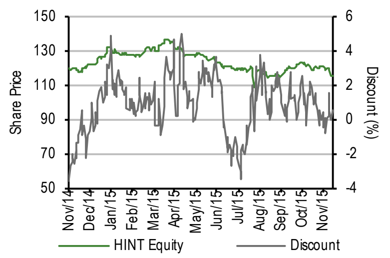
Price	**115.9p**
Market cap	**£93.0m**
AUM	**£97.6m**

NAV*	114.1p
Premium to NAV	1.6%
NAV**	115.3p
Premium to NAV	0.5%

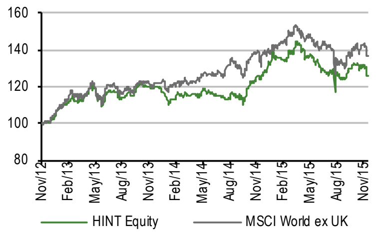
*Excluding income. **Including income. Data at 14 December.

Yield	3.9%
Ordinary shares in issue	80.25m
Code	HINT
Primary exchange	LSE
AIC sector	Global Equity Income

Share price/discount performance



Three-year cumulative perf. graph



52-week high/low	136.9p	108.6p
NAV** high/low	135.2p	109.3p

**Including income.

Gearing

Gross*	4.0%
Net*	4.0%

*As at 31 October 2015.

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Edison profile page

Henderson International Income Trust is a research client of Edison Investment Research Limited

Exhibit 1: Trust at a glance

Investment objective and fund background

Henderson International Income Trust aims to provide a high and rising level of dividends, as well as capital appreciation over the long term from a focused and internationally diversified portfolio of securities (predominantly listed equities and fixed income) outside the UK. It is benchmarked against the MSCI World ex-UK index.

Recent developments

- 20 November 2015: All resolutions passed at AGM.
- 19 October 2015: Annual report for the year ended 31 August. NAV TR +2.1% compared with +5.0% for the MSCI World ex-UK index. Share price TR +12.2%.
- 12 October 2015: Fourth interim dividend of 1.15p declared, payable 27 Nov.

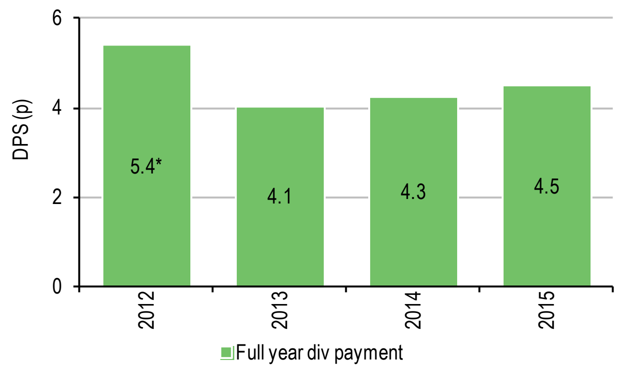
Forthcoming		Capital structure		Fund details	
AGM	November 2016	Ongoing charges	1.11%	Group	Henderson Global Investors
Interim results	April 2016	Net gearing	4.0%	Manager	Ben Lofthouse
Year end	31 August	Annual mgmt fee	0.75%	Address	201 Bishopsgate, London, EC2M 3AE
Dividend paid	Feb, May, Aug, Nov	Performance fee	No		
Launch date	28 April 2011	Trust life	Indefinite	Phone	+44 (0) 20 7818 6825
Continuation vote	Three-yearly, next 2017	Loan facilities	£20m overdraft facility	Website	www.hendersoninternationalincometrust.com

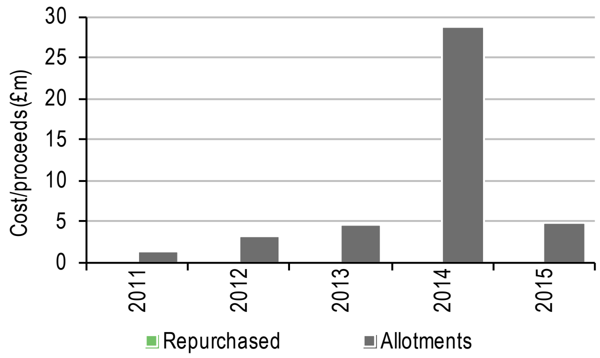
Dividend policy and history

Dividends paid quarterly in February, May, August and November. Note: *Six dividends were paid in respect of the period from launch in April 2011 and the first full year-end at 31 August 2012. The annualised dividend for this period was 4.05p.

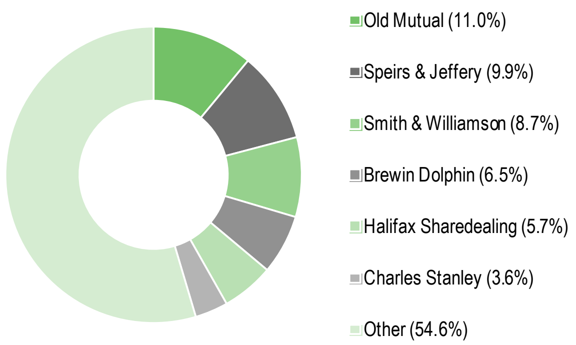
Share buyback policy and history

HINT has authority to buy back up to 14.99% of shares and will also issue shares to manage a premium. 2014 issuance includes the conversion of C shares issued in November 2013 and the final exercise of subscription shares issued at launch.

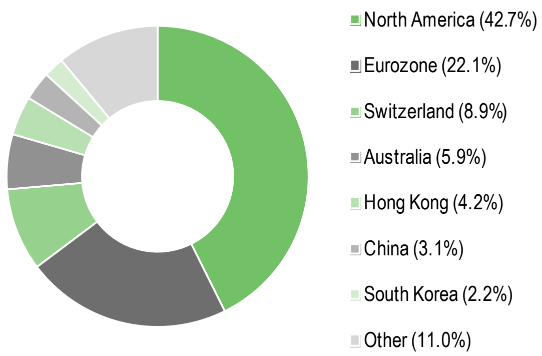




Shareholder base (as at 31 August 2015)



Regional breakdown of portfolio exposure (as at 31 October 2015)



Top 10 holdings (as at 31 October 2015)

			Portfolio weight %	
Company	**Country of listing**	**Sector**	**31 Oct 2015**	**30 April 2015***
Microsoft	US	Computing	3.1	2.6
Lockheed Martin	US	Aerospace & defence	2.8	2.2
General Electric	US	Conglomerate	2.7	N/A
Novartis	Switzerland	Pharmaceuticals	2.7	2.6
Roche	Switzerland	Pharmaceuticals	2.6	2.4
Six Flags Entertainment	US	Leisure	2.4	2.1
Verizon Communications	US	Telecommunications	2.4	N/A
Chevron	US	Oil & gas	2.3	N/A
SK Telecom	Korea	Telecommunications	2.2	2.6
Eurocommercial Properties	Netherlands	Commercial property	2.2	N/A
Top 10 (% of portfolio)			**25.4**	**24.9**

Source: Henderson International Income Trust, Edison Investment Research, Morningstar, Bloomberg, Thomson Datastream. Note: *N/A where not in April 2015 top 10.

Market outlook: Time to look further afield for income?

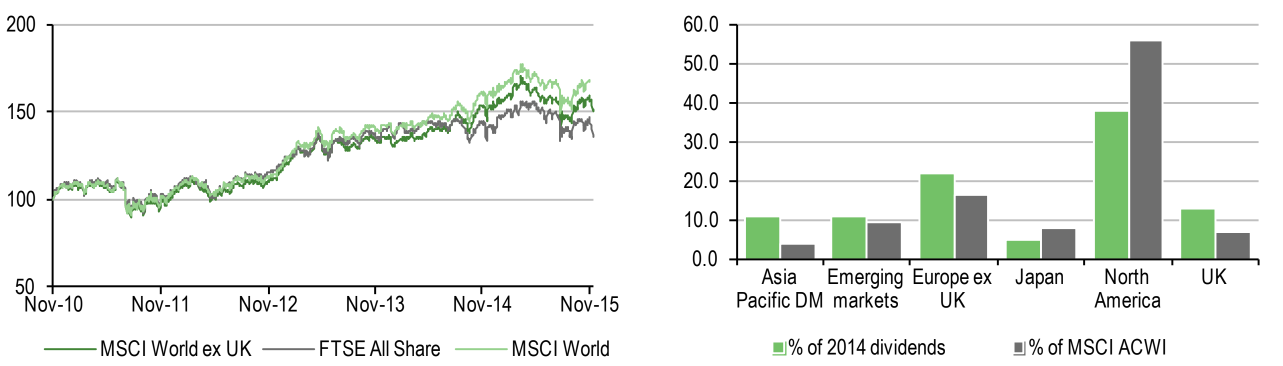
Investors are becoming increasingly concerned about the prospects for dividends from the largest companies in the FTSE 100. According to the Capita Dividend Monitor, for Q315 the UK's top five dividend payers accounted for 31% of total dividends, and the presence of BP and Shell in this number could see dividends come under pressure if oil prices remain lower for longer. (The UK is not alone in its high level of dividend concentration, however: according to the Henderson Global Dividend Index, c 90% of Swiss dividends come from the country's top 20 payers, compared with c 70% for the UK.) Meanwhile, the level of dividend cover for the FTSE 100 (ie the relationship of company earnings to dividends paid) was less than 1.5x in late November, suggesting wider growth/sustainability issues in an environment where earnings growth continues to be subdued.

One solution for UK investors concerned about dividend income could be to look overseas. Although the UK punches above its weight in terms of its share of global dividends, generating 13% of 2014 dividends compared with a 7% weighting in the MSCI AC World index (Exhibit 2), that still leaves 87% of global income coming from elsewhere. Europe ex-UK and developed Asia Pacific also contribute a greater proportion of dividends than their index weighting would suggest and, while the US and Japan are lower yielding in aggregate, stock-specific higher yield opportunities may be found.

In an environment where risk awareness may be higher, given fears over growth in China, war in the Middle East and the future path of US and UK interest rates, investors may also wish to consider the importance of sustainable dividends in producing positive total returns in periods of volatility.

Exhibit 2: Market performance and dividend contribution

5yr total returns from MSCI World ex-UK, MSCI World and FTSE All-Share | **Contribution to global dividends versus global index weighting**



Source: Thomson Datastream, Edison Investment Research, MSCI, Henderson Global Dividend Index

Fund profile: Income diversifier with growth potential

Henderson International Investment Trust (HINT) seeks to provide a high and rising income from dividends, as well as long-term capital growth, by investing outside the UK. It was launched in April 2011, in part as a rollover vehicle for investors in Henderson Global Property Companies. The manager since launch, Ben Lofthouse, is assisted by a team of global equity income specialists and draws on Henderson's wider regional investment teams.

A relatively focused portfolio of c 60 stocks, HINT is diversified by geography and industrial sector. Its benchmark is the MSCI World ex-UK index – a large universe of c 1,500 stocks – although the portfolio is built from the bottom up with little reference to index weightings. HINT is unusual among its global equity income peers in that it explicitly excludes the UK; the idea of the trust is to provide diversification (particularly in terms of income) for investors who may already have sufficient UK exposure. Dividends are paid quarterly and have grown ahead of inflation since launch.

The fund manager: Ben Lofthouse

The manager's view: Cautiously positioned for recovery

Dividend growth is key for an equity income fund, and Lofthouse points to a surprising figure for the sector with the best growth record: from Q409 to Q215 technology stocks globally saw annualised dividend growth of 19% in dollar terms, with further surprises possible from US tech stocks sitting on large cash piles. In spite of a more challenging backdrop, with fears emerging for UK investors in particular over sustainability of dividends, HINT saw only one cut in FY15, from Italian oil stock ENI.

Lofthouse says the HINT portfolio is broadly but not aggressively positioned for economic recovery. In a normalising interest rate environment cyclical sectors such as technology tend to outperform, while defensive areas like consumer staples may struggle. However, with QE still ongoing in areas such as Japan and Europe, the manager is keeping a balance in the portfolio, with sensibly valued stocks in areas such as healthcare and telecoms alongside more cyclical financials and industrials.

Valuation is a key focus, although Lofthouse warns that the 'deep value' end of the market has a more cyclical tilt than usual, as banks and oil companies are currently out of favour and hence trade on cheap valuations. The manager is instead focusing on areas such as pharmaceuticals that have defensive qualities but are less expensive than consumer staples stocks, which have been driven to high valuations by investors looking for bond-like reliability of income in a world of low bond yields. "Drug companies are trading more cheaply than Kellogg's and they are very cash-generative," says Lofthouse, although he acknowledges risks from political pressure on pricing and the regulatory environment, and remains underweight healthcare versus the index as a result.

While bond proxies have performed well, the manager says 'hopeful growth' stocks such as biotech and internet companies like Uber have also been driving the market in recent years, meaning that value and income have been left behind somewhat. Overall, however, equity returns in 2015 have been disappointing, with emerging markets the worst performers but defensive assets such as bonds and property doing well. While the future path of emerging markets is far from certain, Lofthouse says the declines could lead to opportunities in fundamentally undervalued companies in these areas, which could see an uptick in gearing from the current low level of c 4%.

Asset allocation

Investment process: Dividend-seeking, valuation-focused

HINT manager Ben Lofthouse is a member of Henderson's global equity income team, headed by Alex Crooke, which has grown substantially in recent years and now has nine portfolio managers and analysts. The team takes a bottom-up approach to investing, defining its universe as stocks in the MSCI World index that have dividend yields of 2%+, attractive free cash flow yields and strong free cash flow growth. HINT aims to achieve a yield at least equivalent to that of UK equities.

Stocks in the global equity income universe are assessed on their business fundamentals, with the manager seeking companies with defensible competitive positions, affordable investment requirements, management whose interests are aligned with those of shareholders, and sustainability of returns. Such companies should contribute sustainable profits, cash flow and dividends to the portfolio. In addition, the manager targets capital growth from unloved and undervalued companies whose earnings are underappreciated by the market.

Lofthouse manages the allocation between HINT's three regional portfolios, North and South America, Europe ex-UK (including the Middle East and North Africa) and Asia Pacific (including Australasia). He is able to draw on the expertise of fund managers outside the global equity income team, such as Henderson Far East Income fund manager Mike Kerley, who contributes Asian stock ideas. The manager also sets the level of gearing (up to 25%) in response to available opportunities. The end result is a portfolio of c 60 companies, roughly one-third from each region. While the number of stocks is broadly equal across regions, weightings may vary. Stocks may be sold if valuation targets are reached or if there is a fundamental change in the investment case.

HINT's mandate includes the flexibility to hold bonds as well as equities. Lofthouse has not yet used this power and says he would only do so if he were extremely cautious on the outlook for equities. Currency hedging may be employed, although this tends only to be used when the portfolio is significantly overweight in a given currency, rather than as a view on the likely direction of interest rates. The manager may also make limited use of option writing to enhance income.

Current portfolio positioning

At 31 October HINT had 67 holdings, slightly above the target range of 40-60 and higher than six months ago. This is a shorter stock list than the peer group average of 93.5, although with 25.4% of assets invested in the top 10 stocks, HINT is less concentrated than the sector average of 30.8%.

The largest allocation is to financials; the 31.9% shown in Exhibit 3 includes 12.1% in real estate, including Netherlands-listed shopping centre operator Eurocommercial and French stocks Icade, a commercial property REIT, and Nexity, a mass-market housebuilder. Lofthouse says European property stocks are undervalued (all three stocks were bought below book value) and offer good yields. There is also a large overweight to telecoms, with eight stocks diversified by geography. Favourable fundamentals for the sector include increasing customer spend on 4G data services, and a regulatory environment generally more inclined to allow consolidation, leading to greater pricing power for the remaining operators in each market. Companies held include SK Telecom in Korea and Bezeq in Israel, bought at 12x P/E and with a dividend yield of 8%.

Exhibit 3: Portfolio sector exposure vs benchmark (% unless stated)

	Portfolio end Oct 2015	Portfolio end April 2015	Change (% pts)	MSCI World ex-UK weight	Active weight vs index (% pts)	Trust weight/ index weight (x)
Financials*	31.9	36.0	-4.1	20.4	11.6	1.6
Telecommunications	13.4	12.5	0.9	3.2	10.3	4.3
Industrials	16.1	16.0	0.1	11.1	5.1	1.5
Oil & Gas	4.7	3.0	1.7	6.2	-1.5	0.8
Technology	12.6	10.0	2.6	15.2	-2.6	0.8
Utilities	0.0	1.5	-1.5	3.0	-3.0	0.0
Basic Materials	1.0	0.0	1.0	4.5	-3.5	0.2
Healthcare	9.3	7.0	2.3	13.4	-4.1	0.7
Consumer Services	9.1	9.0	0.1	13.7	-4.6	0.7
Consumer Goods	1.9	5.0	-3.1	9.6	-7.7	0.2
	100.0	**100.0**		**100.0**		

Source: Henderson International Income Trust, Edison Investment Research. Note: Ranked by active weight. 30 April sector weightings are approximate. *Financials includes real estate, 12.1% at 31 October 2015.

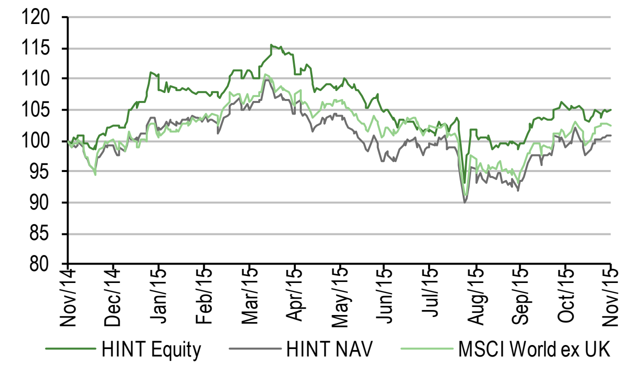
Oil and gas exposure was reduced before the worst of the oil price falls, with sales of oil services companies predicated on greater supply and demand equilibrium in the sector. More recently Lofthouse has bought US oil major Chevron (now a top 10 holding). Consumer goods weightings have been trimmed as 'bond proxy' stocks in the sector become increasingly expensive. Some of the proceeds have been deployed in an increased allocation to healthcare, where a new holding in Johnson & Johnson has provided consumer staple-type exposure at a more favourable valuation.

Geographically, HINT is structurally underweight the US (by 20.5 percentage points versus the index) and Japan (by 8.2 percentage points) because these markets are on average low-yielding. All regions must contribute to the overall portfolio yield. At 31 October 44% of the portfolio was in North American stocks, on an average P/E of 15.9x and with a dividend yield of 3.6%. European stocks (35% of assets) had an average P/E of 16.0x and a dividend yield of 4.5%, while Asia Pacific including Japan (24%, with Japan at 1.3%) had both the cheapest stocks and the highest yield, with an average P/E of 13.5x and a dividend yield of 4.8%.

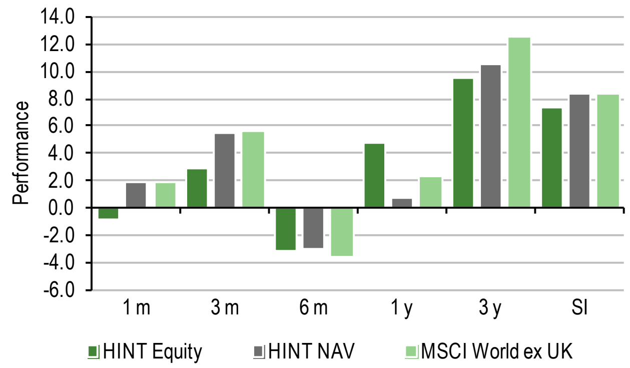
Performance: Overcoming currency headwinds

Exhibit 4: Investment trust performance to 30 November 2015

Price, NAV and benchmark total return performance, one-year rebased



Price, NAV and benchmark total return performance (%)



Source: Thomson Datastream, Edison Investment Research. Note: Three-year and since inception (SI) performance figures annualised. Inception date is 28 April 2011.

Exhibit 5: Share price and NAV total return performance, relative to indices (%)

	One month	Three months	Six months	One year	Three years	SI
Price relative to MSCI World ex-UK	(2.7)	(2.7)	0.5	2.4	(7.7)	(4.2)
NAV relative to MSCI World ex-UK	(0.0)	(0.2)	0.6	(1.5)	(5.4)	(0.3)
Price relative to FTSE All-Share	(1.4)	0.4	3.6	4.2	4.2	6.7
NAV relative to FTSE All-Share	1.3	3.0	3.6	0.1	6.8	11.0
Price relative to MSCI World	(2.9)	(2.8)	(0.7)	0.9	(11.1)	(9.2)
NAV relative to MSCI World	(0.2)	(0.3)	(0.6)	(3.0)	(8.8)	(5.6)

Source: Thomson Datastream, Edison Investment Research. Note: Data to end-November 2015. Geometric calculation.

Over 12 months to 30 November HINT's share price total return is ahead of the MSCI World ex-UK index, although over most other periods both share price and NAV returns are in line with or somewhat behind the benchmark (Exhibit 4). The manager points out that because of its focus on dividends, the trust tends to be structurally underweight the lower-yielding markets of the US and Japan, which are the two largest constituents of the benchmark and have also produced some of the strongest capital performance in the period since HINT's launch. Returns in FY15 were also hit by the strength of sterling. The importance of dividends in total returns is underlined by the fact that HINT's positive NAV performance for FY15 was made possible by income (even allowing for unfavourable currency moves) outweighing a small capital loss.

As seen in Exhibit 5, HINT has since launch fulfilled its aim of rewarding investors who venture overseas with better returns than they could have achieved from the UK index: both NAV and share price total returns have beaten the FTSE All-Share over almost all periods since inception.

In FY15 the top five contributors to performance versus the benchmark were tobacco giant Reynolds American, theme park operator Six Flags Entertainment (a longstanding holding), defence company Lockheed Martin, Chinese online games stock NetEase and German stock exchange operator Deutsche Börse. Lofthouse describes these as a mix of growth stocks and more stable defensive names. The most significant detractors (relative to the index) were Korean companies SK Telecom and Hyundai Motor, oil stocks ENI and Petrochina (although oil exposure was cut substantially during the year) and mid-cap Canadian loyalty card operator Aimia, which has a 10% free cash flow yield and an 8% dividend yield, but has struggled to achieve earnings forecasts following a new airline loyalty card contract agreed in 2013. Lofthouse comments that investors are wary of companies with narrow end-markets, so these tend to get punished more by falling share prices in the event of any wobbles.

Discount: Back at a premium despite market wobbles

At 14 December HINT's shares traded at a 0.5% premium to cum-income net asset value. On average the shares have traded at a premium of 1.3% since launch. The final exercise of subscription shares in September 2014 may have caused temporary oversupply of HINT's shares; the discount hit an all-time widest of 8.3% on 3 September that year, but has since closed back up and has traded at an average premium of 1.0% over the past 12 months. HINT may buy back up to 14.99% of shares to manage a discount (a power not used to date) and uses tap issue to meet demand. So far in 2015, 3.9m shares have been issued, raising £4.9m.

Exhibit 6: Share price premium/discount to NAV (including income) over three years (%)

Source: Thomson Datastream, Edison Investment Research

Capital structure and fees

HINT is a conventional investment trust with one class of share. At 14 December 2015 there were 80.25m ordinary shares in issue, an increase of 5% on 12 months previously as new shares have been issued to meet demand. At the beginning of FY15 the final exercise of subscription shares also added 8.3m shares to the total in issue.

At its 31 August 2015 year end, HINT had gearing of 6.3% through a £20m overdraft facility with HSBC; £6.0m was drawn at FY15 (FY14: £6.7m). Net gearing had fallen to 4% at 31 October.

Henderson Global Investors is paid an annual management fee of 0.75% of net assets (this was reduced from 0.8% in November 2013, when a performance fee structure was also removed). Ongoing charges for FY15 were 1.11%, a small increase on the 1.09% for FY14, reflecting costs associated with the final exercise of subscription shares.

Dividend policy and record

HINT pays dividends quarterly, in February, May, August and November. The total dividend for the year ended 31 August 2015 of 4.5p per share was 5.9% higher than for FY14, a significantly above inflation increase, in spite of pressure on the income stream (which all comes from overseas) from the strength of sterling. While historically the board has raised the dividend at the fourth interim, setting the bar for the first three dividends of the following year, in FY15 the first two dividends were 1.1p each and the third and fourth were 1.15p. Since launch the dividend has grown at a compound annual rate of 2.7% (using the annualised dividend for the first financial period). The FY15 dividend was fully covered by income of 5.14p per share and the trust added to its revenue reserve, which now stands at £2.4m, sufficient to cover 70% of the dividend.

Peer group comparison

HINT is a member of the AIC's Global Equity Income sector, although it is the only fund in the group to focus exclusively outside the UK. There are 10 funds in the sector and HINT's NAV total return performance has been well above average over both one and three years (it does not yet have a five-year track record). Risk-adjusted performance as measured by the Sharpe ratio is above average over one and three years. Half of the peer group currently trades at a premium to NAV; HINT's premium was among the smallest in this group at 14 December. The trust has the joint lowest dividend yield in the group; this may be a reflection of its lack of exposure to the UK, though the 3.9% yield is broadly in line with the FTSE All-Share (ex-ICs). Ongoing charges are somewhat above average, while gearing is towards the lower end of the peer group range.

Exhibit 7: Global Equity Income peer group as at 14 December

% unless stated	Market Cap £m	TR 1 Year	TR 3 Year	TR 5 Year	Ongoing Charge	Perf. fee	Discount (-)/prem	Net Gearing	Yield (%)	Sharpe 1y (NAV)	Sharpe 3y (NAV)
Henderson International Income	**92.5**	**0.2**	**27.8**	**--**	**1.2**	**No**	**0.5**	**105.0**	**3.9**	**0.1**	**1.0**
BlackRock Income Strategies	368.0	4.1	16.3	23.4	0.7	No	1.1	91.0	5.1	0.0	0.7
Blue Planet Investment Trust	16.4	-3.8	25.7	--	3.8	No	-29.7	152.0	8.2	0.0	0.7
F&C Managed Portfolio Income	40.6	3.2	26.8	43.8	1.2	Yes	0.5	99.0	4.4	0.2	1.1
Invesco Perp Select Glo Eq Inc	49.4	3.9	38.9	46.5	1.0	Yes	2.1	110.0	3.9	0.4	1.2
London & St Lawrence	100.3	2.4	28.4	50.4	0.9	Yes	-4.1	99.0	4.1	0.4	1.1
Murray International	1022.2	-10.2	-7.2	9.2	0.7	Yes	-0.7	118.0	5.9	-0.9	0.0
Scottish American	333.3	3.8	18.7	25.1	0.9	No	4.7	124.0	4.3	0.4	0.8
Securities Trust of Scotland	145.8	-1.8	18.6	38.2	0.6	No	-6.3	109.0	4.0	-0.2	0.7
Seneca Global Income & Growth	57.4	6.0	26.9	42.0	1.5	No	0.3	110.0	4.1	0.8	1.2
Sector weighted average		**-3.2**	**8.1**	**20.5**	**0.8**		**-0.1**	**112.0**	**5.1**	**-0.3**	**0.5**
HINT rank in sector	**6**	**7**	**3**	**N/A**	**3**		**6**	**7**	**9**	**6**	**5**

Source: Morningstar, Edison Investment Research. Note: TR = total return. Sharpe ratio is a measure of risk-adjusted return. The ratios shown 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 total assets less cash and equivalents as a percentage of net assets (100 = ungeared).

The board

HINT's four non-executive directors have all been in post since the trust's launch in 2011. Chairman Christopher Jonas was also chairman of the predecessor vehicle, Henderson Global Property Companies (HGPC), and has a background in property. Peregrine Banbury – another former HGPC board member – and Bill Eason formerly worked in investment management, while Simon Jeffreys' professional background is as an accountant and business manager.

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