

# Henderson International Income Trust

## Ex-UK income specialist boosted by rollover

Henderson International Income Trust (HINT) seeks a high and growing income as well as capital growth potential; it is unusual in that it invests exclusively outside the UK. The trust has produced annualised total returns (NAV and share price) of 8-9% since launch in 2011 and is comfortably ahead of most peers over one, three and five years. Following the rollover of stablemate Henderson Global Trust (HGL) in April 2016, HINT has doubled its asset base, which should widen its appeal to some investor groups, as well as reducing the impact of fixed costs. Manager Ben Lofthouse currently favours European companies over those in the Americas and Asia, with continental stocks making up almost half the portfolio at 31 May.

12 months ending	Share price (%)	NAV (%)	MSCI World ex-UK (%)	FTSE All-Share (%)	MSCI World (%)
31/05/12	(3.1)	(3.1)	(5.5)	(8.0)	(4.3)
31/05/13	32.1	31.5	28.7	30.1	30.5
31/05/14	(1.0)	5.9	6.3	8.9	8.0
31/05/15	15.1	12.9	17.0	7.5	16.8
31/05/16	1.3	3.2	0.3	(6.3)	1.3

Source: Thomson Datastream. Note: Total returns in sterling.

## Investment strategy: Seeking value and income

HINT's manager, Ben Lofthouse – a member of Henderson's well-resourced global equity income team – selects a portfolio of c 60 stocks, split into three regional portfolios (Americas, Europe ex-UK and Asia Pacific). He seeks to blend well-managed, sensibly financed companies with strong free cash flow generation and sustainable dividends, with unloved and undervalued stocks that have the potential to provide superior capital growth while still contributing to income. The rationale for the trust is to provide income diversification for investors who may otherwise be over-reliant on the UK as a source of dividends.

## Market outlook: Volatility set to continue in near term

Global market volatility is likely to continue in the near term, with lower summer trading volumes combining with macro worries including slower economic growth, the US presidential election and the British referendum on EU membership. With dividends providing an even more important element of total returns when capital values are under pressure, a strategy that invests for income as well as growth could help investors ride out short-term bumps in the road.

## Valuation: Back at a premium after short-lived dip

HINT's shares are trading at a 2.7% premium to cum-income NAV. This could be seen as a resumption of 'normal service' (the average premium since launch is 0.8%) following a period earlier in 2016 when the discount widened to an all-time high of 9.2% (at 1 March). This should be seen in the context of generally wider discounts on investment trusts in Q116, reflecting investor risk aversion amid market volatility. Since the completion of the HGL rollover on 26 April, the discount to cum-income NAV has averaged 1.7% (ex-income average of 0.5%).

## Investment trusts

21 June 2016

**Price** 127.5p  
**Market cap** £198.9m  
**AUM** £194.9m

NAV\* 121.8p  
 Premium to NAV 4.7%  
 NAV\*\* 124.1p  
 Premium to NAV 2.7%

\*Excluding income. \*\*Including income. Data at 17 June 2016

Yield 3.6%

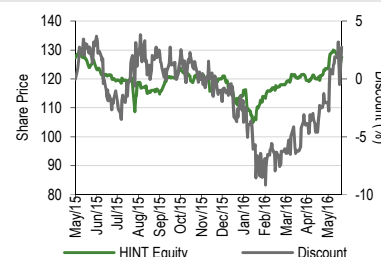
Ordinary shares in issue 156.0m

Code HINT

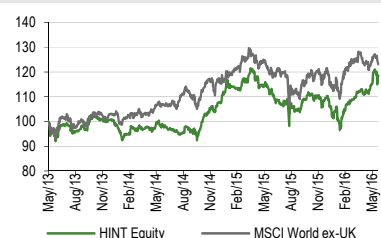
Primary exchange LSE

AIC sector Global Equity Income

## Share price/discount performance



## Three-year cumulative perf. graph



52-week high/low 130.0p 104.8p

NAV\*\* high/low 129.0p 109.3p

\*\*Including income.

## Gearing

Gross\* 3.0%

Net\* 3.0%

\*As at 31 May 2016.

## Analyst

Sarah Godfrey +44 (0)20 3681 2519

[investmenttrusts@edisongroup.com](mailto:investmenttrusts@edisongroup.com)

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**Henderson International  
 Income Trust is a research  
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**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 equities and fixed income) outside the UK. It is benchmarked against the MSCI World ex-UK index.

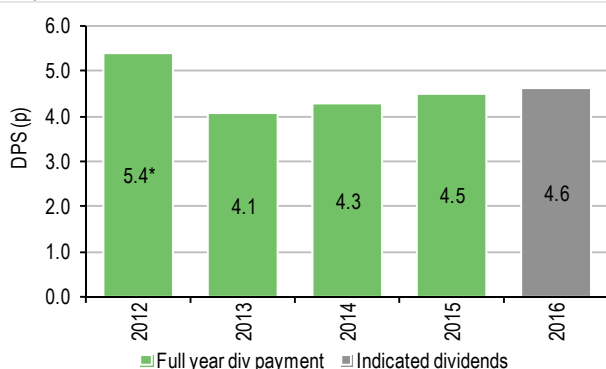
**Recent developments**

- 26 April 2016: Half-year results for the period to 29 February. NAV TR +7.8% versus +5.4% for MSCI World ex-UK benchmark. Share price TR -2.3%.
- 25 April 2016: Appointment of Richard Hills and Aidan Lisser to the board of HINT following the rollover of Henderson Global Trust.
- 25 April 2016: 75.2m new HINT shares issued as a result of the rollover of HGL; HINT acquires £95m of assets from HGL.

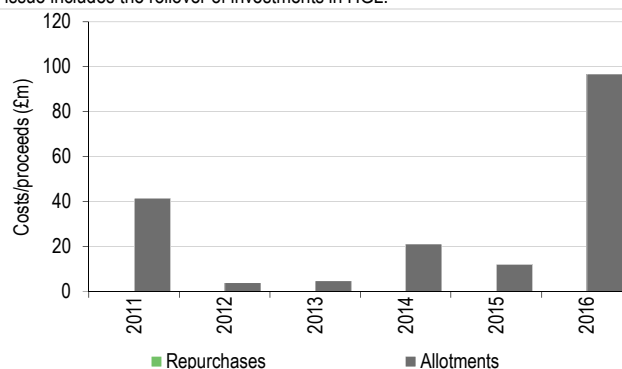
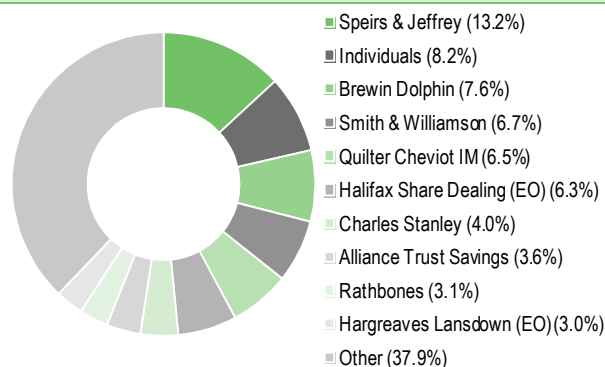
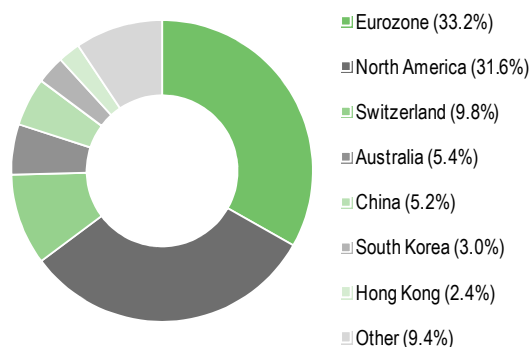
Forthcoming		Capital structure		Fund details	
AGM	November 2016	Ongoing charges	1.1% (31 Aug 2015)	Group	Henderson Global Investors
Annual results	October 2016	Gearing	0.0%	Manager	Ben Lofthouse
Year end	31 August	Annual mgmt fee	0.65% of NAV (see page 7)	Address	201 Bishopsgate, London, EC2M 3AE
Dividend paid	Feb, May, Aug, Nov	Performance fee	None	Phone	+44 (0) 20 7818 1818
Launch date	28 April 2011	Trust life	Indefinite	Website	<a href="http://www.hendersoninternationalincome.com">www.hendersoninternationalincome.com</a>
Continuation vote	Three-yearly, next 2017	Loan facilities	£50m overdraft facility		

**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 to 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 the authority to buy back up to 14.99% of shares and will issue shares to manage a premium. 2014 issue includes conversion of C shares issued in November 2013 and the exercise of subscription shares issued at launch. 2016 issue includes the rollover of investments in HGL.


**Shareholder base (as at 2 June 2016)**

**Portfolio exposure by geography (as at 31 May 2016)**

**Top 10 holdings (as at 31 May 2016)**

Company	Country of listing	Sector	Portfolio weight %	
			31 May 2016	31 May 2015*
Roche	Switzerland	Pharmaceuticals & biotechnology	3.5	2.5
Novartis	Switzerland	Pharmaceuticals & biotechnology	3.5	2.6
Microsoft	US	Software & computer services	3.0	2.5
Orange	UK	Mobile Telecommunications	2.4	N/A
Deutsche Telekom	Germany	Mobile Telecommunications	2.4	N/A
Deutsche Post	Germany	Industrial Transportation	2.3	N/A
Cisco Systems	US	Technology hardware & equipment	2.2	N/A
AXA	France	Insurance	2.1	N/A
JPMorgan Chase	US	Banks	2.1	N/A
Lockheed Martin	US	Aerospace & defence	2.1	2.3
<b>Top 10 (% of portfolio)</b>			<b>25.6</b>	<b>24.1</b>

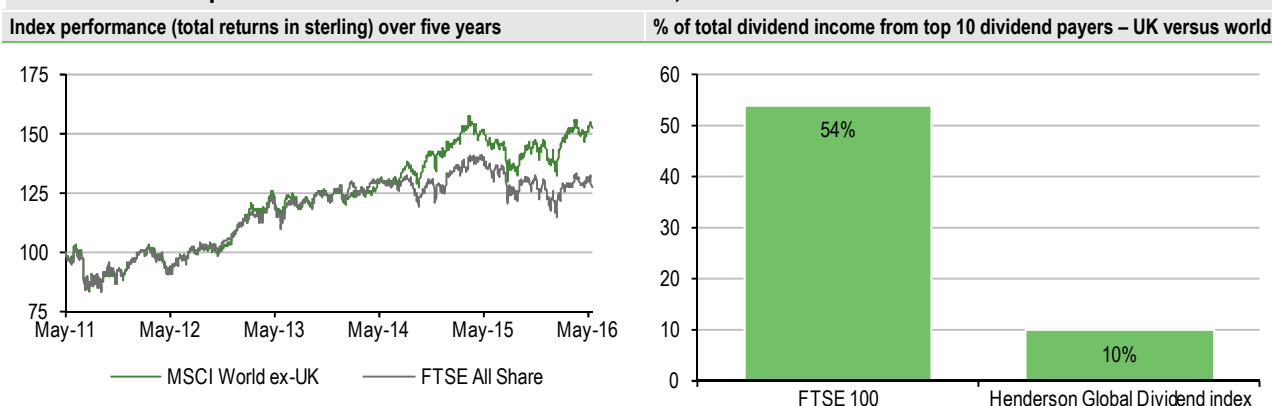
Source: Henderson International Income Trust, Edison Investment Research, Morningstar, Bloomberg. Note: \*N/A where not in May 2015 top 10.

## Market outlook: Focus on total return amid volatility

Global markets have struggled to advance so far in 2016, with investors beset by a range of concerns, from the US presidential election to the UK's EU referendum (where the ramifications of a vote to leave would be felt far beyond Britain), and from worries over growth in China to transatlantic divergences in monetary policy. Added to this, the summer months are often a time of lower trading volumes, which can be a further source of volatility.

When capital returns from shares are under pressure, dividends are a vital contributor to total returns. However, as shown in Exhibit 2 below, as well as having lagged the rest of the world in total return terms, UK stocks are subject to additional dividend risk as a result of high concentration. In 2015, the top 10 dividend paying stocks in the FTSE 100 index (c 80% of the FTSE All-Share) accounted for 54% of total income, compared with a figure of 10% globally. With this in mind, a fund that looks for income beyond UK shores could provide a good source of diversification.

**Exhibit 2: Market performance and dividend concentration, UK versus world**



Source: Thomson Datastream, Henderson Global Investors, Edison Investment Research

## Fund profile: Newly enlarged ex-UK income specialist

Henderson International Income Trust (HINT) was set up in 2011 as a successor vehicle to a closed-ended property fund run by Henderson Global Investors. It seeks to provide a high and rising dividend income, along with capital growth potential, by investing exclusively outside the UK. This makes it unusual among its peers in the Association of Investment Companies' Global Equity Income sector; the rationale for the investment policy was that many investors may already have sufficient UK exposure in their portfolios, and may benefit from diversifying their sources of income. HINT aims to achieve a dividend yield largely equivalent to that of the UK market – at 20 June its yield of 3.6% was close to the FTSE All-Share index yield of 3.9%. The trust has a relatively concentrated portfolio of c 60 stocks chosen on a bottom-up basis with little reference to index weightings. There is a value bias and the manager, Ben Lofthouse, focuses on companies with sustainable dividends and high free cash flow yields.

In April 2016, HINT roughly doubled in size as a result of a rollover scheme for Henderson Global Trust (HGL). HGL investors were given a choice between transferring their investment into HINT or its Henderson stablemate The Bankers Investment Trust, which includes the UK. Some 63% of HGL shareholders chose HINT, and as a result the trust received c £80m in stocks (only those holdings that were common to both portfolios) and c £15m in cash and equivalents from the liquidation of remaining positions. The board and management expect that as a larger trust, HINT will enjoy greater investor demand, as well as benefiting from a bigger pool of assets over which to spread fixed costs. As part of the deal, the management fee has also been reduced from 0.75% to

0.65% of net assets, and two former directors of HGL have joined the HINT board in recognition of the fact that c 50% of HINT's shareholder base is now made up of former HGL investors.

## **The fund manager: Ben Lofthouse**

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### **The manager's view: Finding value in Europe**

Lofthouse is currently overweight Europe, predicated on the assessment that certain areas of the market are currently very cheap and that from a macro perspective, low interest rates (backed by ECB policy intervention), low oil prices and a weaker euro are an important source of support, particularly for consumer-facing sectors. With European banks largely recapitalised and lending starting to pick up, the manager draws parallels with the US in 2011/12, arguing that the lesson from the US recovery is that it was domestic stocks, rather than the big global names, that were the major beneficiaries. An example is the French mass-market housebuilder Nexity, bought on a 7% dividend yield in 2013, since when its share price has more than doubled.

The manager notes that it has been another year of strong performance for bond proxy-type stocks, leading him to exit positions in companies like Reynolds American (the top contributor to HINT's performance in H116) and Nestlé on valuation grounds. The expectation of a rising interest rate environment in the US led to widespread selling of defensive growth stocks, allowing Lofthouse to take positions in companies such as Verizon, Chevron and Johnson & Johnson at more favourable valuations and with attractive yields. The manager has also bought real estate investment trusts in Asia, Europe and the US.

Lofthouse argues that while stable, quality companies (both low-yielding and high-yielding) are relatively expensive in aggregate, this is not true across the board; while he has sold or trimmed holdings in Reynolds, Lockheed Martin and Six Flags Entertainment, he has added to Bayer and ING at more favourable P/E valuations.

Given the value bias and income focus of HINT, Lofthouse says avoiding value traps – stocks that appear cheap but have limited recovery potential – is a key focus, although of equal importance is finding those stocks that are cheap without justification; at present, he argues, Europe is the best source of these companies. However, with an increasing number of riskier, cyclical stocks falling into the value segment, Lofthouse says he is unlikely to increase HINT's gearing substantially in the near term.

## **Asset allocation**

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### **Investment process: Focus on sustainable dividends**

HINT has been enlarged by the HGL rollover, but its investment process is unchanged. Manager Ben Lofthouse, a member of Henderson Global Investors' well-resourced global equity income team, takes a bottom-up approach to investing, narrowing down the MSCI World ex-UK index to those stocks with dividend yields above 2%, attractive free cash flow yields and strong free cash flow growth. While he describes the process as value-biased, Lofthouse says that focusing on free cash flow means he can avoid stocks that are 'cheap for a reason'.

The team assesses stocks in the global equity income universe on their business fundamentals. Lofthouse seeks companies where management interests are aligned with those of shareholders, and that have strong competitive positions, affordable capital requirements, and sustainable profits, cash flow and dividends. The manager cites research by Citigroup showing that a focus on high free cash flow has produced superior returns, even over the past four years, a period in which stocks classified as 'value' on more traditional measures have underperformed. High free cash flow

yield also leads to greater sustainability of dividends, a key focus for HINT. In addition, the manager looks for companies that are unloved and undervalued by the market, seeing their under-appreciated earnings as an important driver of potential capital growth.

Regional exposures, which Lofthouse actively manages, are allocated between North and South America, Europe (excluding the UK but including North Africa and the Middle East) and Asia Pacific (including Australasia). Each region is limited to a maximum of 50% of the portfolio. Sector weightings are subject to a maximum of 20%. The end portfolio is made up of 40-70 stocks, with broadly one-third (in numerical terms) coming from each region. Gearing is deployed in response to available opportunities. (The recent fall in the level of gearing resulted from HINT's receipt of c £15m in cash and equivalents following the HGL rollover, and does not necessarily indicate a more bearish view on the manager's part.)

Lofthouse assigns valuation targets to stocks in the portfolio, and may sell positions when these targets are reached. Holdings will be reviewed if dividend yields fall below 2%, and the manager may also sell positions where fundamental change has had a negative impact on the outlook.

Further portfolio management tools include the ability to hold bonds as well as equities (Lofthouse has not historically done this), the limited use of option writing to enhance income and the ability to hedge currency exposure (historically only used to neutralise a large currency overweight).

## Current portfolio positioning

At 31 May 2016, HINT had 60 holdings, broadly in line with the average for its peer group. The concentration in the top 10 holdings, at 25.6%, was largely unchanged from a year previously, although many of the names in the top 10 had changed.

In geographical terms (see Exhibit 1), HINT is currently close to its maximum 50% weight in Europe (33.2% in the eurozone, with another 9.8% in Switzerland and 2.1% in Norway), with the US at c 32% (a large underweight versus the MSCI World ex-UK index) and the balance in Asia Pacific (figures at 31 May). In sector terms (Exhibit 3) there are large overweights to financials (including property) and telecoms. The manager describes property as offering low beta-like consumer staples (the largest underweight), but without being similarly expensive. Other financials holdings include top 10 stock AXA, which Lofthouse says offers 10% return on equity in spite of the tough trading environment, and new bank holdings ING and Svenska Handelsbanken. The telecoms exposure includes recent purchase Deutsche Telekom, which came up on Henderson's screens early in 2016, offering a good dividend, growth from its US division and good free cash flow.

Most positions come into the portfolio at c 1.5%, with the 2.0-3.5% weightings of the top 10 holdings being largely a result of share price gains. Lofthouse notes that many of the largest positions in the portfolio were deeply out of favour when they were purchased, and that often the challenge is having the conviction to stick with companies such as these to reap the rewards of recovery.

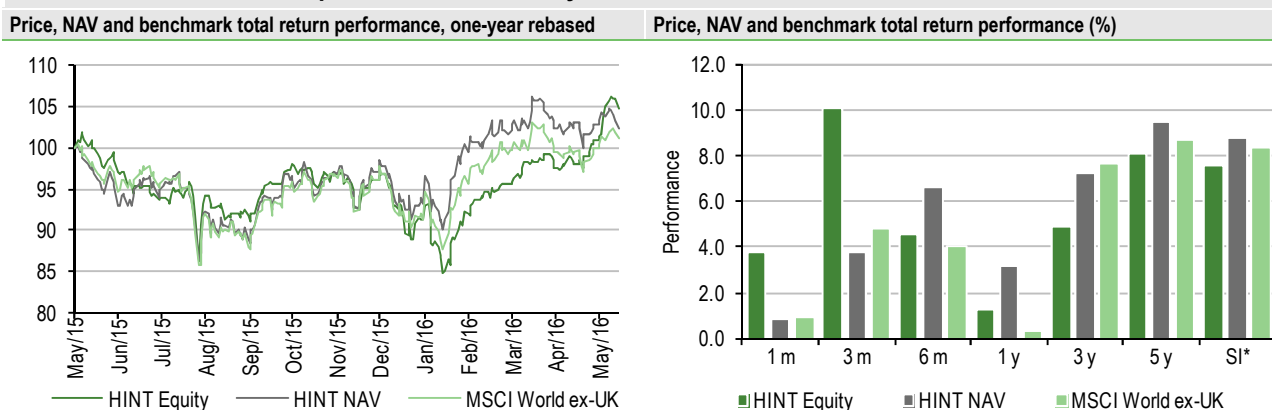
**Exhibit 3: Portfolio sector exposure vs benchmark (% unless stated)**

	Portfolio end-May 2016	MSCI World ex-UK index weight	Active weight vs index (% pts)	Trust weight/index weight (x)
Financials	30.5	19.8	10.7	1.5
Telecommunications	16.2	3.4	12.8	4.8
Industrials	15.9	11.2	4.7	1.4
Healthcare	13.9	13.4	0.5	1.0
Information technology	7.7	15.1	-7.4	0.5
Consumer discretionary	6.7	13.0	-6.3	0.5
Energy	4.0	6.2	-2.2	0.6
Utilities	2.1	3.3	-1.2	0.6
Materials	1.5	4.6	-3.1	0.3
Consumer staples	1.5	10.0	-8.5	0.1
	<b>100.0</b>	<b>100.0</b>		

Source: Henderson International Income Trust, Edison Investment Research

## Performance: Solid record since launch

**Exhibit 4: Investment trust performance to 31 May 2016**



Source: Thomson Datastream, Edison Investment Research. Note: Three- and five-year and since inception (SI\*, 28 April 2011) performance figures annualised. Sterling-adjusted performance.

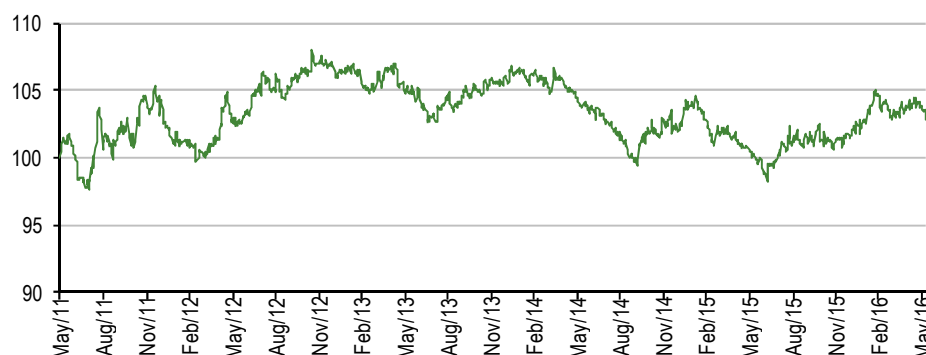
**Exhibit 5: Share price and NAV total return performance, relative to indices (%)**

	One month	Three months	Six months	One year	Three years	Five years	SI*
Price relative to MSCI World ex-UK	2.8	5.0	0.5	1.0	(7.5)	(2.6)	(3.7)
NAV relative to MSCI World ex-UK	(0.1)	(1.0)	2.4	2.8	(1.1)	3.7	1.9
Price relative to FTSE All-Share	3.1	6.0	4.4	8.1	5.3	12.6	11.4
NAV relative to FTSE All-Share	0.2	(0.0)	6.5	10.1	12.6	19.8	17.9
Price relative to MSCI World	2.4	5.1	0.7	0.0	(9.7)	(7.4)	(8.6)
NAV relative to MSCI World	(0.4)	(0.9)	2.7	1.8	(3.5)	(1.5)	(3.2)

Source: Thomson Datastream, Edison Investment Research. Note: Data to end-May 2016. Geometric calculation. Sterling-adjusted.

HINT's NAV total return over 12 months has been well ahead of the benchmark MSCI World ex-UK index (Exhibit 4). Since launch in 2011, NAV total returns have been a little ahead of the benchmark, while share price returns have been a little behind. Strong share price total returns over three months have narrowed the discount that opened up early in 2016 in a difficult period for global equity markets. Given its aim of providing diversification (in both capital and income terms) for UK investors who may already have sufficient domestic exposure, it is encouraging that HINT has outperformed the FTSE All-Share in both share price and NAV terms over almost all the periods shown in Exhibit 5. Differentiation from world index performance (Exhibit 5 shows MSCI World indices both including and excluding the UK; Exhibit 6 charts performance versus the ex-UK benchmark) is attributable to several factors: a large underweight to the US (c 30% of the HINT portfolio compared with 50-60% of world indices), the focus on stocks with attractive dividends, the manager's value bias and the relatively short stock list (62 holdings from a universe of c 1,500).

**Exhibit 6: NAV performance relative to MSCI World ex-UK index over five years**



Source: Thomson Datastream, Edison Investment Research

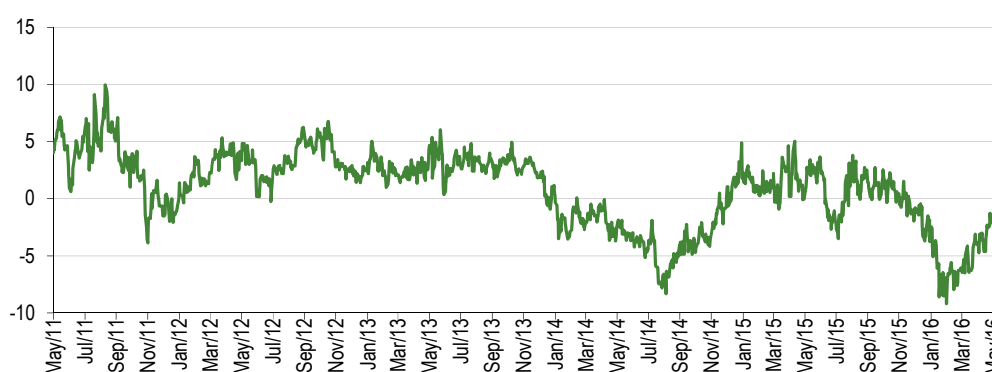


## Discount: At an average premium since launch

HINT has traded at an average premium of 0.8% since launch in 2011, although as shown in Exhibit 7 below, there have been periods of discount widening, including in the early part of 2016, when investment trust discounts widened across the board in a climate of heightened risk aversion.

The trust may allot shares to meet demand and can also buy back up to 14.99% a year to manage a discount. Excluding the effect of the HGL rollover, in the past 12 months HINT has issued 2.2m shares. The terms of the HGL transaction permit a tender offer for up to 20% of the new shares at NAV less costs if HINT's average discount to NAV exceeds 5% in the 90 days from completion. This period lasts until 25 July 2016; from 26 April to 20 June the cum-income discount averaged 1.7% (0.5% ex-income), meaning a significant widening would be required to trigger the tender offer.

**Exhibit 7: Share price premium/discount to NAV (including income) over five years (%)**



Source: Thomson Datastream, Edison Investment Research

## Capital structure and fees

HINT is a conventional investment trust with one class of share. Following the rollover of HGL, the number of shares in issue has increased from c 80m to 156.0m. The trust may gear up to 25% of net assets and has a £50m overdraft facility with HSBC. Given the enlarged asset base, the effective maximum level of gearing is now 10%. Gearing is managed actively and has ranged from 0% to 10% over the past year, averaging 5.25%. At 31 May, HINT had net gearing of 3%.

As part of the HGL scheme, the management fee has fallen from 0.75% to 0.65% of net assets, reducing to 0.6% above £250m. This, along with the benefit of spreading fixed costs over a larger asset base, will have the effect of lowering ongoing charges, although the impact in FY16 is likely to be small because the transaction took place more than halfway through HINT's financial year.

## Dividend policy and record

HINT pays dividends quarterly, in February, May, August and November. For FY15, total dividends of 4.5p per share were paid. So far in FY16, two dividends of 1.15p have been paid and the board has indicated this level is likely to be maintained for the rest of the year, implying a total dividend of 4.6p, 2.2% up on FY15. The ex-dividend date of the second dividend was brought forward to avoid dilution from the HGL scheme. The timing of the scheme was such that the manager expects no adverse impact in terms of revenue, as portfolio holdings' dividends are biased to the middle of the calendar year and so will accrue to the enlarged fund, as well as being paid out to a larger shareholder base. The revenue reserve will reduce in the short to medium term on a per-share basis as a result of the deal, although the board intends to continue adding to it as revenues allow.

## Peer group comparison

HINT is a member of the AIC's Global Equity Income sector, although it is unusual in its peer group because it excludes the UK. Following the rollover of HGL, it is now the third-largest trust in the sector. NAV total return performance is above the peer group average over one, three and five years, ranking second, second and first respectively. It also ranks first for risk-adjusted performance as measured by the Sharpe ratio over one and three years. Ongoing charges are slightly above average, but are set to fall under the new fee structure; like the majority of peers, HINT does not charge a performance fee. The trust is one of three standing at a premium to NAV at 9 June 2016. Gearing is below average and HINT has the second-lowest dividend yield in the sector, possibly as a result of excluding the UK, which is one of the higher-yielding markets globally.

**Exhibit 8: Global Equity Income peer group as at 9 June 2016**

% unless stated	Market cap £m	TR 1 Year	TR 3 Year	TR 5 Year	Ongoing charge	Perf. fee	Discount (ex-par)	Net gearing	Dividend yield (%)	Sharpe 1y (NAV)	Sharpe 3y (NAV)
<b>Henderson International Income</b>	<b>201.7</b>	<b>7.0</b>	<b>28.3</b>	<b>61.3</b>	<b>1.1</b>	<b>No</b>	<b>2.8</b>	<b>103.0</b>	<b>3.5</b>	<b>0.1</b>	<b>0.6</b>
Blue Planet Investment Trust	18.1	(12.2)	18.7	--	3.8	No	(23.5)	140.0	7.7	(0.8)	0.3
F&C Managed Portfolio Income	47.6	(2.7)	15.1	40.4	1.2	Yes	0.0	97.0	4.5	(0.7)	0.2
Invesco Perp Select Global Eq Inc	51.0	3.5	29.9	58.3	1.0	Yes	(2.6)	111.0	3.2	(0.1)	0.6
London & St Lawrence	98.7	(1.5)	19.7	49.2	0.9	Yes	(5.1)	99.0	4.2	(0.5)	0.4
Murray International	1,209.6	7.3	5.0	31.4	0.7	No	0.6	114.0	4.9	(0.1)	(0.1)
Scottish American	361.5	6.3	23.2	37.4	0.9	No	(0.8)	123.0	3.9	0.0	0.5
Securities Trust of Scotland	151.6	3.9	16.0	46.8	0.9	No	(6.6)	107.0	4.1	(0.2)	0.2
Seneca Global Inc & Growth Trust	58.3	0.6	20.7	41.6	1.5	No	0.5	111.0	4.0	(0.3)	0.4
<b>Weighted average</b>		<b>5.8</b>	<b>12.8</b>	<b>38.1</b>	<b>0.9</b>		<b>(0.5)</b>	<b>113.0</b>	<b>4.5</b>	<b>(0.1)</b>	<b>0.1</b>
<b>Rank</b>	<b>3</b>	<b>2</b>	<b>2</b>	<b>1</b>	<b>4</b>		<b>1</b>	<b>7</b>	<b>8</b>	<b>1</b>	<b>1</b>

Source: Morningstar, Edison Investment Research. Note: TR = NAV 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

Following the rollover of HGL, HINT now has six non-executive directors. Richard Hills, the former chairman of HGL, and Aidan Lissner joined the board of HINT in April 2016 on completion of the scheme. HINT chairman Christopher Jonas and Peregrine Banbury were also directors of predecessor company Henderson Global Property Companies and have been on the HINT board since launch in 2011, as have Bill Eason and Simon Jeffreys. The directors have backgrounds in property, investment management, accountancy, business and marketing.

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