

The World Trust Fund

Searching out discounted assets globally

The World Trust Fund (WTR) invests globally in a mix of closed-end funds (35.7% at 31 August), investment trusts (39.2%) and holding companies (27.3%) chosen for their discounted assets and potential for capital appreciation. The managers seek to identify catalysts for re-rating and will also engage actively with holdings to boost long-term shareholder value. Benchmarked against the MSCI AC World Index, the portfolio is heavily underweight the US (which the managers see as broadly overvalued) and overweight emerging markets. Performance over one year has been strong versus the benchmark, but has suffered in the recent global sell-off, and the discount expansion of its underlying investments. A new dividend policy was introduced in FY15 and WTR has a 1.4% yield.

12 months ending	Share price (%)	NAV (%)	MSCI AC World (%)	MSCI World ex US (%)	DS World Inv. Cos (%)
31/08/12	5.0	6.0	9.5	1.0	7.8
31/08/13	17.8	18.8	19.2	16.5	12.8
31/08/14	4.2	6.1	13.3	10.1	7.5
31/08/15	7.6	5.8	1.7	(4.9)	(2.2)

Note: All total returns in £ terms.

Investment strategy: Finding value with catalysts

Kun Deng and the Discounted Assets Strategies team at Lazard Asset Management follow a four-stage investment process, first screening the universe to identify funds and holding companies trading on attractive discounts, then applying macro and fundamental analysis to gauge if assets are unjustly discounted and have catalysts for rerating, before building a portfolio where risks are understood and underlying assets appropriately diversified. There are no top-down sector or country constraints and the portfolio differs markedly from the benchmark MSCI AC World Index, which is heavily weighted towards the US. Short positions may be used for hedging.

Outlook: Volatility could bring opportunity

Discounts on closed-end funds on both sides of the Atlantic have converged at an average of c 6%; this is wider than the 10-year average for the US but narrower in the UK, though in both cases discounts differ widely, giving a large opportunity set for a value-focused investor. Meanwhile, a global market sell-off and fears over contagion from a slowdown in China could spell short-term volatility but the potential for longer-term rewards for those who are prepared to take a contrarian view.

Valuation: Two layers of discount give potential uplift

Over the past three years WTR has traded broadly in a range of 10-14% below cum-income net asset value. At 23 September the discount stood at 12.3%, having narrowed briefly to 7.5% (a three-year low) in late-August volatility. Because WTR's strategy is to invest in discounted assets, it is worth noting that there are effectively two layers of discount. At 30 June the aggregate discount on the underlying portfolio was 22.5% (broadly in line with the five-year average); applying the 23 September discount to this figure gives an overall discount of 32.0% – or, as the managers put it, each £1 invested buys £1.47 of assets.

Investment companies

25 September 2015

Price 238.0p
Market cap £96.3m
AUM £109.4m

NAV* 271.4p
Discount to NAV 12.3%
Yield 1.4%

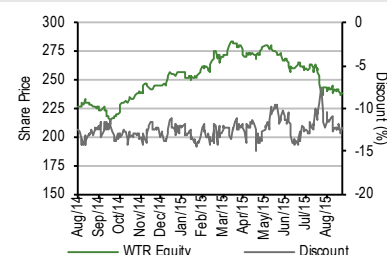
*Including income, at 23 September 2015.

Ordinary shares in issue 40.5m
Code WTR

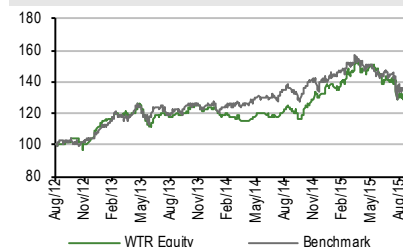
Primary exchange LSE

AIC sector Global

Share price/discount performance*



Three-year cumulative perf. graph



52-week high/low 283.5p 215.3p

NAV* high/low 327.4p 242.5p

*Including income.

Gearing

Gross 2.2%
Net 2.2%

Analysts

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[Edison profile page](#)

Exhibit 1: Fund at a glance

Investment objective and fund background

The World Trust Fund (WTR) seeks to achieve long-term capital appreciation by investing primarily in a diversified portfolio of companies whose shares trade at a discount to the underlying net asset value. The fund measures its performance against the MSCI ACWI World Index.

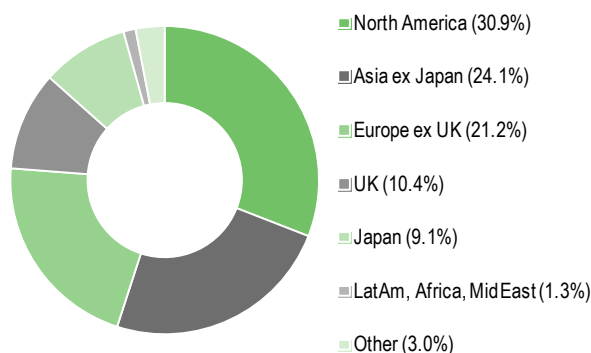
Recent developments

12 August 2015: Interim management statement for the three months ended 30 June. NAV TR +2.6% (US\$) compared with +0.4% for MSCI ACWI. Share price TR (GBP) -1.4%.
17 July 2015: Final dividend of 2.9p per share declared for year-ended 31 March 2015.

Forthcoming		Capital structure		Fund details	
AGM	August 2016	Ongoing charge	1.42% (FY15)	Management	Lazard Asset Management LLC Group
Half year results	November 2015	Net gearing	2.2%	Manager	Kun Deng
Year end	31 March	Annual mgmt fee	0.75% of NAV	Address	30 Rockefeller Plaza, New York, NY 10112 USA
Dividend paid	January, September	Performance fee	See page 7	Phone	+1 212 632 6000
Launch date	1991	Fund life	Indefinite (annual cont. vote)	Website	www.theworldtrustfund.com
Continuation vote	Annual	Loan facilities	Annual facility		

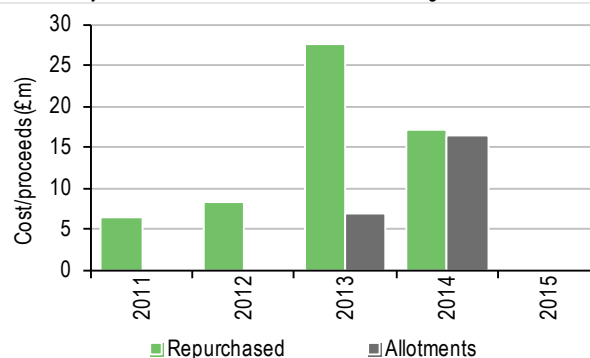
Regional exposure (31 August 2015 – net exposures)

Gross exposures totalled 102.2% - analysed below as a percentage of 100%

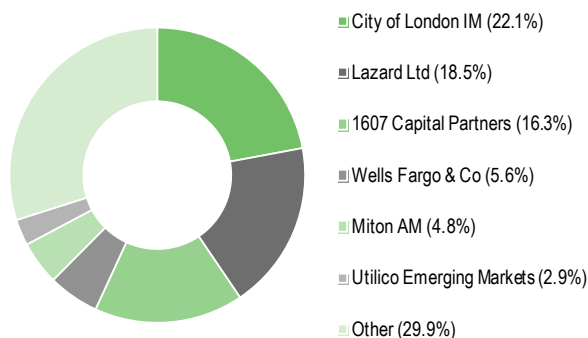


Share buyback policy and history

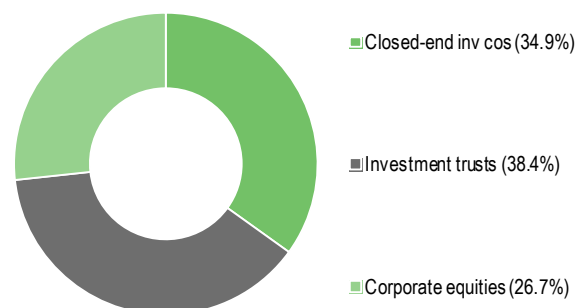
WTR is authorised to repurchase up to 14.99% of its ordinary shares. Chart includes buybacks via tender offers and issuance through exercise of warrants.



Shareholder base (as at 31 July 2015)



Portfolio by company type (as at 31 August 2015, net of gearing)



Top 10 holdings (as at 31 August 2015)

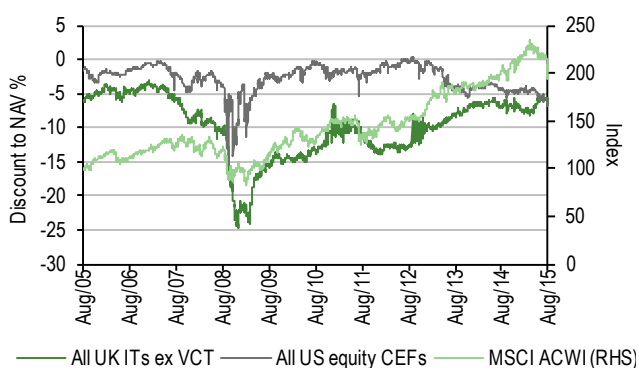
	Country of listing	Portfolio weight 31 Aug 2015 (%)	Discount to NAV 31 Aug 2015 (%)	Portfolio weight 28 Feb 2015 (%)*	Discount to NAV 28 Feb 2015 (%)*
BB Biotech	Switzerland	7.4	19.2	7.6	15.9
JPMorgan European Smaller Cos	UK	6.2	6.7	5.2	11.6
General American Investors	US	5.6	17.1	5.7	13.5
Eurazeo	France	5.6	22.8	5.5	12.4
Investor AB	Sweden	4.7	21.2	4.8	16.4
Adams Diversified Equity	US	4.5	14.7	4.4**	13.7
JPMorgan Japanese	UK	4.4	10.6	N/A	N/A
Harbourvest Global Private Equity	UK	4.3	18.2	N/A	N/A
Tri Continental	US	4.3	15.6	4.3	14.1
International Biotechnology Trust	UK	4.3	6.5	N/A	N/A
Total/average discount		51.3	15.3	55.0	26.6

Source: The World Trust Fund, Thomson Datastream, Edison Investment Research. Note: *N/A where stock not in top 10 at 28 February. **Formerly known as Adams Express. Top 10 total/average discount figures for 28 February 2015 are for the top 10 holdings at that date. Rounding errors may mean that some percentages do not sum to 100%.

Discounted asset outlook: Mixed picture amid volatility

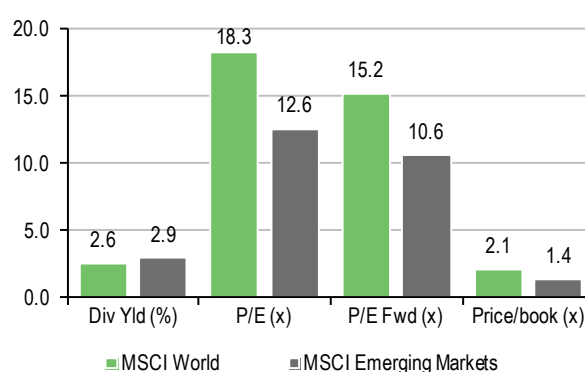
When considering the outlook for a global fund investing in discounted assets, it is worth looking at discount trends for closed-end funds as well as the macroeconomic and market backdrop. Exhibit 2 shows discounts for UK investment trusts (excluding venture capital trusts) and US closed-end funds, as well as total returns for the MSCI AC World Index over 10 years to 31 August. Discounts in the US and UK have converged at c 6%. This is narrower than the 10-year average of 9.7% for the UK but wider than the US average of 2.8%. (Interestingly, the ballooning discounts seen during the financial crisis are barely significant in the context of the long-term average: the five-year figures of 9.3% and 2.7% since 31 August 2010 are almost identical to the 10-year average. However, the US recovered much more quickly from the crisis, leading to the smaller average discount.)

Exhibit 2: Closed-end fund discount history



Source: Morningstar, Edison Investment Research

Exhibit 3: World and emerging market valuations



Source: MSCI at 31 August 2015, Edison Investment Research

Meanwhile, global market turmoil during August has thrown the spotlight on the differing economic prospects of developed and emerging markets, with the US poised to raise interest rates in response to continued recovery while fears grow over a slowing economy in China and its ramifications for the region. Exhibit 3 highlights the more favourable valuation metrics of emerging versus developed markets, although investors must balance these lower valuations against the possibility that returns are likely to be dented by continued uncertainty. In such conditions, an investment strategy that focuses on discounted assets could provide a longer-term foil both to fears of overvaluation in the West and to near-term volatility in Asia.

Fund profile: Discount-focused global growth fund

The World Trust Fund (WTR), launched in 1991, aims for long-term capital growth from a portfolio of investment and holding companies that are assessed to be trading at unwarranted discounts to their underlying asset value, and where the underlying assets are also undervalued. WTR is an investment company incorporated in Luxembourg and listed on the London Stock Exchange. It has been managed since launch by the mainly New York-based Discounted Assets Strategies team of Lazard Asset Management, led by Kun Deng. The fund is a member of the Association of Investment Companies' Global sector and is benchmarked against the MSCI AC World Index (MSCI World Index until April 2009). In the financial year ended 31 March 2015, the fund introduced an additional reference index – the MSCI AC World ex-US Index – and also began paying a dividend for the first time.

As well as identifying undervalued assets that have a catalyst for revaluation, the WTR team may also engage directly with its holdings to put in place measures to unlock value, such as tender offers or partial returns of capital. However, the managers are at pains to stress that they are not arbitrageurs, taking the view that activism should focus on how to generate more future profits for all investors.

The fund manager: Kun Deng

The manager's view: Taking advantage of undervalued assets

Kun Deng summarises WTR's approach as 'buying undervalued assets with catalysts that are backed by macro improvements'. An example of this discount-focused strategy is the recent rebuilding of positions in China, which had been radically reduced earlier in 2015 as valuations began to look stretched, although it remains an overweight and is one of the manager's top long-term picks. "China is undergoing a long-term, multi-generational, secular transformation," says Deng. "We like to take advantage of pessimism as long as there is a discount and we can see the underlying assets are undervalued." The managers also favour Japan – another contrarian view– arguing that Japanese firms are now more profitable and focused on shareholder returns than for many years.

At a regional level the managers see the best P/E valuations in emerging markets, while the US is trading above its historical average and Europe, the UK and Japan are all towards the upper end of long-term ranges. Biotech is an exception – the majority of stocks are US-listed but biotech analysts at Lazard argue there are still significant growth opportunities in the sector. WTR's managers say that with some biotech stocks on inflated valuations, investors should avoid backward-looking ETFs and favour actively managed funds targeting the disruptive drugs and companies that will drive the next leg of growth. Top holding BB Biotech (a Swiss company) trades at a c 20% discount to NAV, unlike some US and UK peers that trade close to NAV or at a premium. WTR is engaging with the company to explore whether a US or UK listing could help to unlock value for investors.

As well as actively engaging with holdings to realise value, WTR can also employ hedging (short) strategies to protect on the downside, or gearing to boost anticipated returns. At present the portfolio is unhedged and gearing is modest at 2.2%, although the managers say either strategy could be employed to a greater extent in the face of continued volatility.

Asset allocation

Investment process: Identifying and unlocking hidden value

WTR is managed by the Discounted Assets Strategies team at Lazard Asset Management, led by Kun Deng. The six-strong team, mainly based in New York, can also draw on the expertise of the Lazard group globally to gain a deeper understanding of markets and industry sectors. WTR's investment process consists of four main steps: screening, macro analysis, fundamental analysis and portfolio construction. The ultimate aim is to build a portfolio of assets that are trading at absolute and relative discounts to their net asset value, with identifiable catalysts for revaluation.

Screening sifts the universe to identify potential investments trading on discounts that are high relative to peers or to a company's history, or where volatility suggests short-term opportunities.

Macro analysis focuses more on whether the market and economic conditions are conducive to a company's discount narrowing, rather than on top-down country or sector allocations.

Fundamental analysis is undertaken on stocks that pass the first two screens. The team aims to assess whether a company's assets are also trading at an unwarranted discount, as well as understanding the competitive landscape, the quality of management and the board, and whether the stock is operating in sectors or countries that the team considers to be attractive.

Catalysts for revaluation must be identified, which may include the potential for tender offers or restructuring. Such catalysts would normally be expected to occur within a year, although many holdings may be in the portfolio for the longer term and the team is willing to engage with investee companies to encourage practices that may help value to be realised for shareholders.

Portfolio construction brings together the previous steps in the process, with the team seeking to reaffirm the value opportunity and downside risks, as well as being satisfied that company management are good stewards of capital and that underlying investments are properly diversified. Investments will only be made in stocks that are a good fit with the rest of the portfolio.

Hedging is used on occasions to reduce market risk, usually through short positions in ETFs. Currency exposure is not usually hedged.

Current portfolio positioning

At 31 August WTR had 34 holdings, although with three in the process of liquidation and one a subscription share on another holding, the number of active positions was 30. This was lower than the 51-stock average for the close peer group (see Exhibit 10). Portfolio concentration was broadly average, with the top 10 stocks making up 51.3% of the total, compared with 45.6% for the peer group. Although the stock list is short, the managers point out that the underlying investments of the portfolio holdings number 1,000-2,000, meaning there is a high degree of diversification.

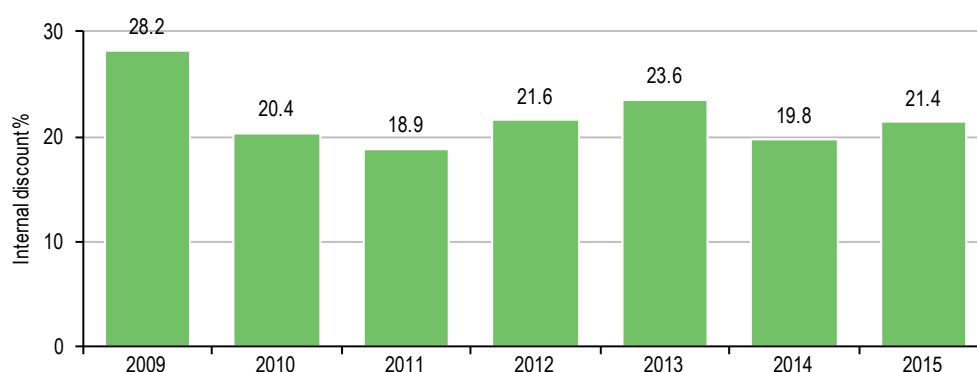
Exhibit 4: Top 10 country exposures

	Portfolio weight end Jul 2015 (%)	Change since 31 Jan 2015 (%)	MSCI AC World Index (%)	Active weight vs index (%)	Trust weight/Index weight
US	29.7	0.9	52.0	-22.3	0.6
UK	9.1	0.9	7.0	2.1	1.3
Japan	9.1	0.2	7.9	1.2	1.2
China	9.0	-8.4	2.3	6.7	3.9
Switzerland	5.7	0.5	3.4	2.3	1.7
France	5.2	0.3	3.5	1.7	1.5
Sweden	3.6	0.8	1.0	2.6	3.6
Philippines	3.1	-1.0	0.1	3.0	31.0
Singapore	2.7	-0.7	0.5	2.2	5.4
India	1.9	N/A	0.8	1.1	N/A
Other	20.9	4.6	21.5	-0.6	1.0
	100.0	100.0	0.0	0.0	100.0

Source: The World Trust Fund, Edison Investment Research

The US is the largest country exposure as well as the biggest underweight versus the MSCI AC World Index. Regionally, Europe (including UK) and North America are the biggest weightings, at 30.9% and 31.6% respectively (net of gearing), while Asia ex Japan is third at 24.1%. Recent changes to the portfolio include a big reduction in exposure to China – Citic Securities, the top holding at 28 February, was sold during March, and other China holdings were trimmed, although some positions have begun to be rebuilt at more favourable discounts during the summer correction. Elsewhere in Asia, positions have been taken in India (India Capital Growth) and Vietnam (Vietnam Opportunity Fund). Proceeds from reductions in China were also used to cut leverage and top up small-cap holdings in Europe (incl. UK). The underlying discount to NAV at FY15 was 21.4%, in line with the five-year average, though discounts are likely to have widened in the recent correction.

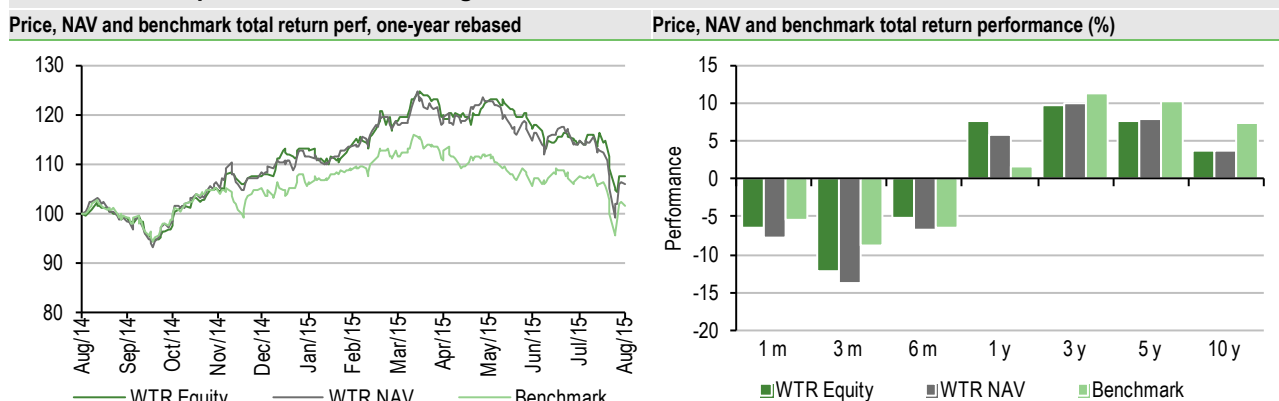
Exhibit 5: Portfolio underlying discount to net asset value (end-March financial years)



Source: The World Trust Fund annual accounts, Edison Investment Research

Performance: Improving trend over one to five years

Exhibit 6: Fund performance to end August 2015



Source: Thomson Datastream, Edison Investment Research. Note: Three- and five-year performance is annualised.

Exhibit 7: Share price and NAV total return performance, relative to benchmarks

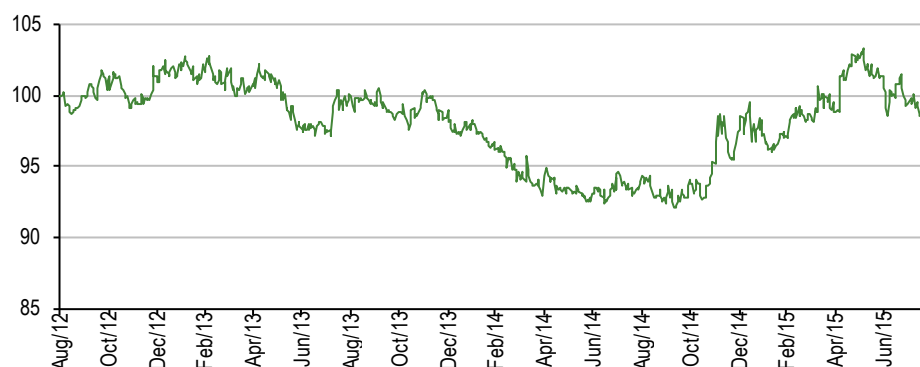
	One month	Three months	Six months	One year	Three years	Five years	10 years
Price relative to Benchmark	(0.9)	(3.5)	1.3	5.7	(3.8)	(11.0)	(29.1)
NAV relative to Benchmark	(2.4)	(5.4)	(0.4)	4.0	(3.0)	(9.9)	(28.7)
Price relative to MSCI World ex US	(0.1)	(1.1)	3.2	13.2	8.3	12.0	(21.5)
NAV relative to MSCI World ex US	(1.5)	(3.0)	1.5	11.3	9.3	13.5	(21.1)
Price relative to DS World Inv Cos	(3.1)	(5.5)	1.9	10.0	11.3	0.3	(20.7)
NAV relative to DS World Inv Cos	(4.5)	(7.3)	0.1	8.2	12.3	1.7	(20.3)

Source: Thomson Datastream, Edison Investment Research. Note: Geometric calculation, data to end-August 2015 and indices sterling adjusted. Benchmark from 1 April 2009 MSCI All Countries World Index, previously MSCI World Index.

WTR has performed strongly versus its benchmark, the MSCI AC World Index, over one year (Exhibit 6). Performance was driven by exposure to China – which was high as the market rose but was trimmed in the second quarter as valuations became stretched – biotechnology, Japan and smaller companies in Europe (including UK). Over three and five years performance is somewhat behind the benchmark (reflecting strong performance from the US, where WTR is underweight), but ahead of the MSCI World ex-US Index and the investment companies universe. Performance has been negative over shorter periods, reflecting summer volatility in world markets (Exhibit 7). Underperformance over 10 years is in part due to the fact that until April 2009 the benchmark was the MSCI World Index, a less appropriate reference index as it excludes emerging markets.

The relative performance chart in Exhibit 8 shows that WTR's NAV total return was behind the MSCI AC World Index for much of 2014 but recovered sharply from November to May. A relative decline over the summer months reflects more negative sentiment towards emerging markets.

Exhibit 8: NAV relative performance over three years



Source: Thomson Datastream. Note: The performance is total return relative to the MSCI AC World Index.

Discount: Back in long-term range after brief spike

During the late August market correction, WTR's discount to net asset value narrowed sharply to a three-year low of 7.5%, before settling back to 12.3% at 23 September, compared with average levels over one and three years of 12.5% and 11.8%. This was a result of sharper moves in the value of underlying holdings, meaning WTR's NAV fell and then recovered by more than its share price. WTR's managers point out that the discount tends to widen when NAV performance improves, as it can take the share price a while to catch up. WTR manages its discount through a programme of tender offers for up to 15% of shares, which occur if the discount has averaged more than 10% during a financial year and the fund has underperformed the benchmark by more than 1% in the same period. The last such tender was in 2014.

Exhibit 9: Discount over three years including income



Source: Thomson Datastream, Edison Investment Research. Note: Negative values indicate a discount.

Capital structure and fees

WTR is structured as a Luxembourg closed-end fund, or SICAF (*société d'investissement à capital fixe*). At 23 September it had 40.5m shares with voting rights in issue and a further 10.2m held in treasury without voting rights. Following the final exercise of warrants at the end of FY14 there are no warrants in issue. The fund has an annual continuation vote which, together with periodic tender offers (see Discount section, above), should help to contain the level of discount to NAV. WTR's manager is authorised to gear up to 15% of net assets, and further gearing may be allowed to a maximum of 25% in consultation with the board. The fund has a \$25m line of credit with Citibank. Based on 23 September exchange rates this equates to £16.4m, or a maximum of 14.6% gearing if the whole facility were drawn. At 31 August WTR was 2.2% geared.

Lazard is paid an annual management fee of 0.75% of NAV (fees on underlying holdings are paid at the portfolio level). A performance fee may be paid on a sliding scale if the total returns over two years (to 31 March) exceed the benchmark total return by more than 5%. No performance fee has been paid in any of the last five years.

Dividend policy and record

WTR's principal aim is to achieve capital appreciation and it has not historically paid a dividend. However, in 2014 it announced it would begin to distribute a significant portion of its investment income (net of fees). For FY15 a total dividend of 3.4p per share was paid (0.5p interim and 2.9p final), representing a dividend yield of 1.4% based on the 23 September share price of 238p. Net income per share for FY15 (based on a 31 March exchange rate of \$1.483/£) was 4.25p, meaning dividends were covered 1.25x.

Peer group comparison

WTR is a member of the AIC's Global sector, but has few direct comparators owing to its portfolio mix of closed-end funds and holding companies. Below we have compared it with a selection of global funds with broadly similar (mainly fund of funds) strategies, some of which take a specifically value or discount-focused approach. WTR's NAV total return performance is above the peer group weighted average over one, three and five years, although the mean is somewhat distorted by the lacklustre performance of the largest fund in the group, British Empire Securities. Risk-adjusted performance as measured by the Sharpe ratio is also above the mean over one and three years. The 1.4% yield is somewhat below average, while ongoing charges are the second highest in the group. The discount is close to the mean. WTR is one of four trusts out of the group of seven to charge a performance fee.

Exhibit 10: Selected Global sector peers

Percentage 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 1y	Sharpe NAV 3y
World Trust Fund	96.3	6.4	30.8	37.4	1.4	Yes	-12.1	100.0	1.4	0.4	0.9
British Empire Securities	615.3	-10.3	10.4	12.5	0.9	No	-12.9	102.0	2.3	-0.8	0.5
Cayenne	37.6	7.5	42.8	39.1	1.9	Yes	-2.0	73.0	2.4	2.8	1.8
F&C Managed Portfolio Growth	43.9	5.3	39.9	57.0	1.2	Yes	1.9	92.0	0.0	0.9	1.4
Henderson Alt. Strategies	95.8	-6.7	-3.5	-11.6	0.9	No	-18.4	95.0	1.4	-1.1	-0.3
JPMorgan Elect Managed Growth	208.2	6.5	48.2	66.1	0.5	No	-1.4	99.0	1.2	0.8	1.5
Mitton Worldwide Growth	39.8	-1.5	21.8	29.0	1.2	Yes	-8.3	108.0	0.0	-0.2	1.1
Weighted average		-4.0	20.5	25.6	0.9		-10.1	99.6	1.9	-0.2	0.8
WTR rank in peer group	3	3	4	4	2		5	3	3	4	5

Source: Morningstar, 23 September 2015, Edison Investment Research. Notes: TR = NAV total return. The Sharpe ratio is a measure of risk-adjusted return. Ratios 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/cash equivalents as a percentage of shareholders' funds (100 = ungeared).

The board

WTR has five non-executive directors. Philip McLoughlin has been on the board since WTR's launch in 1991 and became chairman in 2010. Duncan Budge was appointed in 2006 while James Cave joined the board in 2008. Howard Myles became a director in 2011 and the newest board member, Tony Morrongiello, was appointed in 2014. All the directors have backgrounds in investment management.

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