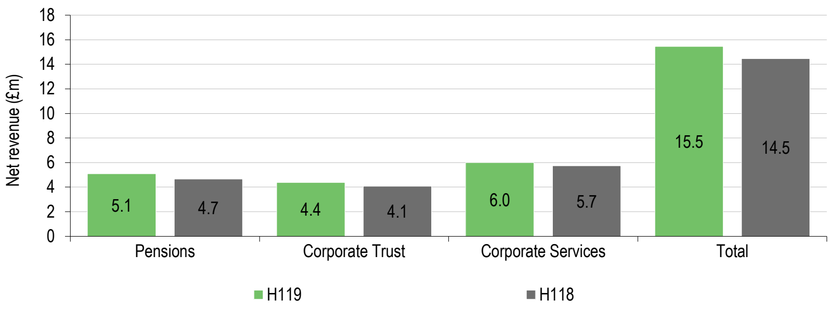
The Law Debenture Corporation

A robust H119 for trust portfolio and IPS

The Law Debenture Corporation (LWDB) has delivered robust NAV and share price gains in the first half 2019, supported by an upward revaluation of its independent professional services (IPS) business, which continues to grow well in spite of a tougher capital markets backdrop. The managers of LWDB's investment portfolio have increased net gearing from c 3% to c 7% in order to take advantage of attractive valuations in selected UK equities. While more than 20% of its diversified portfolio is still invested overseas to gain access to opportunities unavailable in the UK, LWDB has recently moved from the AIC's Global sector to the UK Equity Income sector, where its NAV total returns currently rank it in the top quartile over three, five and 10 years.

Year-on-year revenue growth from all of LWDB's IPS business areas



Source: The Law Debenture Corporation, Edison Investment Research

The market opportunity

Global equity markets have resumed their upward trajectory after a significant sell-off in Q418, despite growing evidence of a worsening economic backdrop, and little concrete progress on geopolitical worries such as Brexit and the US-led trade war. 'Value' stocks have continued to underperform, bucking their longer-term trend (see Exhibit 3), but could hold up better than highly valued growth companies if the current uncertain climate spills over into a further bout of market volatility.

Why consider investing in Law Debenture?

- Unique structure, with IPS division generating significant income as well as providing future growth potential.
- Value-biased equity portfolio could perform well if the current extended cycle of growth stock outperformance turns.
- 44-year record of increasing or maintaining its annual dividend.
- One of the lowest-cost investment trusts in the AIC universe.

Wider-than-average discount; dividend up 10%

At 23 July, LWDB's shares traded at a 10.2% discount to cum-income net asset value (with both debt and the IPS business at fair value). While narrower than the 16.5% five-year high seen last October, this is above both short- and longer-term averages. The H119 dividend of 6.6p has been increased by 10% year-on-year, reflecting a 32% increase in group revenues for the period and building on a 9.3% year-on-year increase in the FY18 final dividend.

Investment trusts
Income and growth

24 July 2019

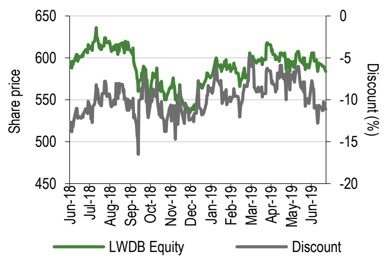
Price	**590.0p**
Market cap	**£691.4m**
AUM	**£913.6m**

NAV*	674.0p
Discount to NAV	12.5%
NAV**	657.2p
Discount to NAV	10.2%

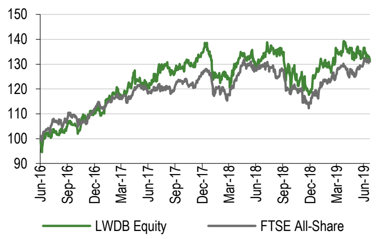
*Excluding income, with debt at par value. **Including income, with debt at fair value. As at 19 July 2019.

Yield (prospective)	3.3%
Ordinary shares in issue	118.2m
Code	LWDB
Primary exchange	LSE
AIC sector	UK Equity Income
Benchmark	FTSE All-Share index

Share price/discount performance



Three-year performance vs index



52-week high/low	636.0p	534.0p
NAV* high/low	697.7p	609.8p

*Including income.

Gearing

Gross (debt at par)*	14.1%
Net*	7.0%

*As at 30 June 2019.

Analysts

Sarah Godfrey	+44 (0)20 3681 2519
Gavin Wood	+44 (0)20 3681 2503

investmenttrusts@edisongroup.com

Edison profile page

The Law Debenture Corporation is a research client of Edison Investment Research Limited

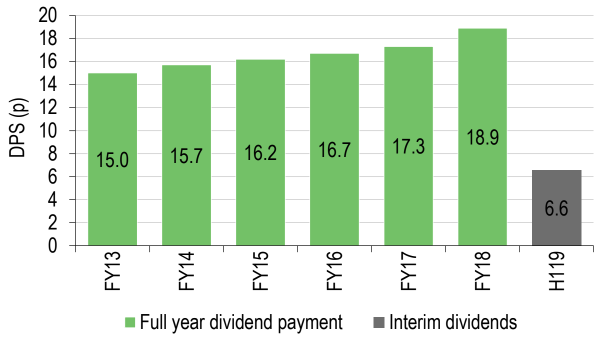
Exhibit 1: Trust at a glance

Investment objective and fund background	Recent developments
LWDB's investment objective is to achieve long-term capital growth in real terms and steadily increasing income. The aim is to achieve a higher rate of total return than the FTSE All-Share Index through investing in a diversified portfolio (mainly UK equities with some international holdings). LWDB's IPS business provides a regular flow of income, which augments the dividend income from the equity portfolio.	■ 24 July 2019: Results for the six months ended 30 June. NAV TR 10.3% versus 13.0% for the FTSE All-Share Index; share price TR 12.1%. Interim dividend of 6.6p declared, a 10.0% increase on H118 (6.0p). ■ 9 May 2019: LWDB reclassified by the Association of Investment Companies into the UK Equity Income sector.

Forthcoming		Capital structure		Fund details	
AGM	April 2020	Ongoing charges	0.43% (FY19)	Group CEO	Denis Jackson
Annual results	February 2020	Net gearing	7.0% (30 June)	Managers	James Henderson and Laura Foll, Janus Henderson Investors
Year end	31 December	Annual mgmt fee	0.30% of portfolio NAV	Address	Fifth floor, 100 Wood Street,
Dividend paid	September, April	Performance fee	None		London, EC2V 7EX
Launch date	1889	Trust life	Indefinite	Phone	+44 (0) 20 7606 5451
Continuation vote	None	Loan facilities	£115m long-term debt	Website	www.lawdebenture.com

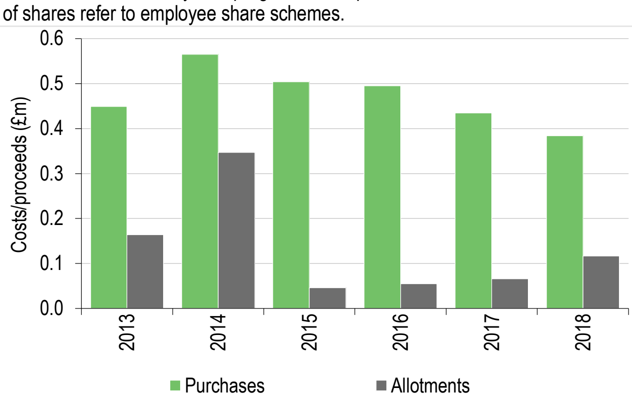
Dividend policy and history (financial years)

LWDB aims to deliver steadily increasing dividends, fully covered by earnings, and has a 44-year record of increasing or maintaining its dividend.

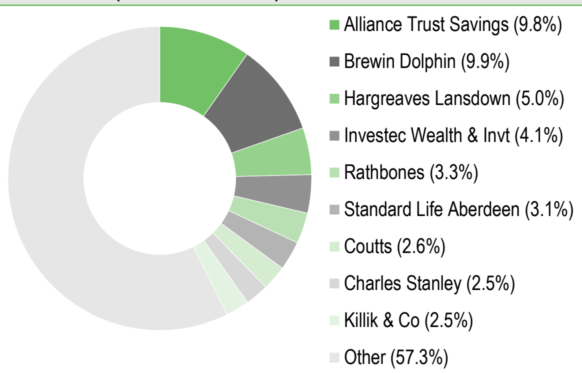


Share buyback policy and history (financial years)

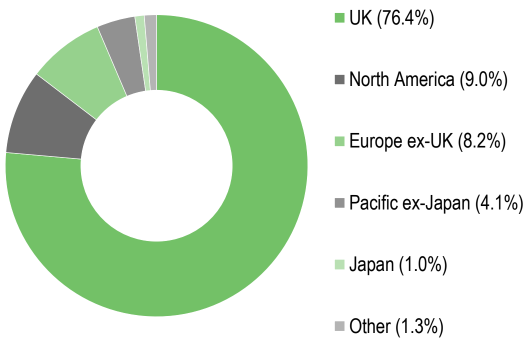
LWDB has no share buyback programme in operation. Purchases and allotment of shares refer to employee share schemes.



Shareholder base (as at 5 March 2019)



Portfolio exposure by geography (as at 30 June 2019)



Top 10 holdings (as at 30 June 2019)

Company	Country	Sector	Portfolio weight %	
			30 June 2019	30 June 2018
Royal Dutch Shell	UK	Oil & gas producers	4.2	4.4
Rio Tinto	UK	Mining	2.4	2.0
GlaxoSmithKline	UK	Pharmaceuticals & biotechnology	2.4	2.1
BP	UK	Oil & gas producers	2.3	2.4
HSBC	UK	Banks	2.3	2.4
Prudential	UK	Life insurance	2.1	1.7
RELX	UK	Media	1.9	1.6
Rolls-Royce	UK	Aerospace & defence	1.8	2.1
Johnson Service	UK	Support services	1.8	1.6
Senior	UK	Aerospace & defence	1.7	2.3
Top 10 (% of holdings)			**22.9**	**22.6**

Source: The Law Debenture Corporation, Edison Investment Research, Bloomberg, Morningstar

Fund profile: UK-biased trust with unique structure

The Law Debenture Corporation (LWDB) began life in 1889 as a vehicle to facilitate the issuance of corporate debentures. This activity still forms a major part of its independent professional services (IPS) business, which also includes pensions and corporate services (see IPS performance and fair value). The company operates in two distinct parts, with a diversified investment portfolio focused on UK equities making up c 85% of its fair value NAV at 30 June 2019 (end-H119), and c 15% of NAV accounted for by the IPS business. Management of the investment portfolio is delegated to Janus Henderson Investors, where fund managers James Henderson and Laura Foll (who also run the Lowland and Henderson Opportunities investment trusts) aim to achieve long-term capital growth and steadily increasing income from a diversified portfolio of c 140 stocks. Because of the significant contribution of the IPS business to LWDB's revenues (25% of the total in H119, a lower percentage than in previous years because of the boost to the revenue account of the investment trust from a change in the allocation of management fees between capital and income), the managers have greater flexibility to invest for capital growth, while remaining confident in the trust's ability to build on its 44-year record of increasing or maintaining its annual dividend.

LWDB has a primarily UK equity portfolio (c 76% of the portfolio at end-H119), with some international exposure to gain access to attractive opportunities that do not have an equivalent in the UK. Because of this, it uses the FTSE All-Share Index as a performance benchmark, and has recently moved from the Association of Investment Companies' (AIC) Global sector to the UK Equity Income sector. Gearing comes via two tranches of long-term debt and is deployed actively within a working range of 10% net cash to 20% geared. At 30 June 2019, net gearing stood at 7%, an increase from 3% at end-FY18 (31 December).

LWDB is led at the corporate level by Chief Executive Officer Denis Jackson and Chief Financial Officer Katie Thorpe, who are both executive members of the board of directors.

IPS performance and fair value

LWDB presents its IPS business in three divisions: pensions, corporate trusts and corporate services. Overall H119 results for the IPS business built on the growth achieved in FY18 under new CEO Denis Jackson (appointed in January 2018), in spite of a tough market backdrop in several of the businesses' areas of operation. Revenues for the IPS business were 6.9% higher in H119 than in H118, while profit after tax was up 8.9% as costs were contained to a 6.1% increase, although LWDB continued to invest for growth. For the pensions business, revenues grew by 9.3% in H119 (compared with H118), the strongest growth of all LWDB's IPS segments and towards the top end of the target of mid- to high single-digit growth. The corporate trusts business saw a 7.4% increase in revenues, while income from corporate services grew by 4.6%.

LWDB's **pensions** business includes its independent trustee services business (established for 50 years and the largest of its kind in the UK), as well as Pegasus, an outsourced pension administration and governance service, launched in 2017. LWDB's pension trustee business provides experienced professional trustees to both defined benefit (DB) and defined contribution (DC) schemes, and Jackson says both this business and Pegasus continue to benefit from a regulatory drive towards consolidation and improvements in the governance of company pension schemes. This was exemplified by a recent report from The Pensions Regulator calling for 'fewer, better-governed schemes'. Thorpe adds that the pensions business has strong recurring revenues as well as potential for future growth, and continues to attract a high calibre of new hires.

The **corporate trusts** business also performed well in H119, despite the low level of corporate debt issuance and merger and acquisition (M&A) activity (for which the division provides escrow agency services) in Europe. The business primarily acts as a bridge between the issuer of a bond or loan and the lender/investor, in order to protect the interests of the investor. Around two-thirds of annual revenues are contracted, with the balance coming from a mixture of acceptance fees from new issuance and special fees from bankruptcy situations, both of which are more dependent on market conditions. Thorpe says the H119 result is partly an increase in ongoing revenues (from new business won in the previous year), as well as some exceptional items. Jackson adds that the focus for corporate trusts remains on winning new ongoing business to facilitate long-term growth as well as replacing what rolls off as a result of maturities.

Corporate services saw the weakest increase in revenues for H119 over H118, but still improved after seven years of broadly flat revenue growth across the IPS business until end-FY17. The main corporate services business is in helping clients to establish and maintain special purpose vehicles (SPVs), by providing governance, administrative, accounting, process agent and company secretarial services. The formation of SPVs is often associated with new issues, and the relatively lacklustre capital markets backdrop so far in 2019 (particularly in Europe) has proved a headwind for the division. Most of the business is international and is concerned with cross-border vehicles. A much smaller part of corporate services – although the biggest contributor to its revenue growth in H119 – is Safecall, a whistleblowing service that has continued to see a strong flow of new corporate clients. Jackson remains confident on Safecall's growth prospects and says the evidence from H119 is that 'it continues to be in the right place at the right time'.

Exhibit 2: Fair valuation of IPS business

£000s unless stated	30 June 2019	31 December 2018	30 June 2018	31 December 2017
IPS valuation				
IPS EBITDA	10,828	10,424	10,440	9,797
EBITDA multiple (x)	9.2	8.4	8.4	7.9
Operational value of IPS	99,618	87,562	87,696	77,396
IPS surplus net assets	15,962	16,844	22,800	17,176
IPS fair value	115,580	104,406	110,496	94,572
IPS fair value per share (p)	97.8	88.3	93.5	80.0
LWDB fair value				
LWDB fair value per share as per IFRS financial statements (p)	619.37	566.27	638.21	633.28
IPS fair value adjustment per share (p)	72.24	66.36	70.08	61.57
Debt fair value adjustment (p)	(27.94)	(18.56)	(20.00)	(25.32)
LWDB fair value NAV per share (p)	663.67	614.07	688.29	669.53
IPS book value (IFRS) as % of total	4.1%	3.9%	3.8%	3.0%
IPS fair value as % total	14.7%	14.4%	13.6%	12.0%

Source: The Law Debenture Corporation, Edison Investment Research

LWDB carries the IPS business at book value in its IFRS financial statements, but also provides an independent assessment of its fair or market value, which is substantially higher. This figure is based on an appropriate multiple of historical EBITDA, and allows investors to make a more accurate assessment of LWDB's fair value. As shown in Exhibit 2, the EBITDA multiple has been raised from 8.4x at end-FY18 to 9.2x at end-H119. The multiple is based on an undisclosed basket of broadly similar companies, adjusted for differences in size, liquidity, margins and growth rates.

The operational value of IPS rose by 13.8% in H119 and the fair value of IPS per share rose by 10.7%. At 97.8p per share, the fair value of IPS accounted for 14.7% of LWDB's NAV per share (with debt at fair value) at end-H119, up from 14.4% at end-FY18. The IFRS book value of IPS rose from 21.8p to 25.5p per share (+17.0%) during H119; the 72.2p IPS business fair value adjustment was an 8.9% increase from 66.4p at end-FY18.

The fund managers: James Henderson and Laura Foll

The managers' view: Maintaining a preference for value

Although they do not follow a 'deep value' investment approach in any of the funds they manage (particularly not LWDB, where portfolio income is supported by IPS business revenues), Henderson and Foll have a strong preference for stocks that are trading at lower-than-average valuations. With this in mind, they admit that their recent trading activity – trimming holdings that have performed well and are trading at higher valuations, and adding to companies (mainly in the UK) that are out-of-favour but have a clear path to earnings growth – could detract from short-term returns. However, they also point to the long-term tendency of stocks with a lower starting valuation to outperform (see Exhibit 3, MSCI World Value versus MSCI World Growth), and argue that after 10 years of strong performance from what are perceived to be high-quality growth stocks, valuations for these companies are now at levels that in many cases look unsustainable. LWDB Chief Financial Officer Thorpe also argues that to have achieved a six-month NAV total return of c 10% is impressive when both value stocks and the UK in general are unloved by the majority of investors.

Exhibit 3: Value has underperformed growth for more than a decade

Source: Janus Henderson Investors, Edison Investment Research

Henderson comments that 'there are some real bargains to be had' currently in the UK stock market, such as Eddie Stobart Logistics, which is trading well and has good prospects for dividend growth, yet 'looks very much the wrong price' on a forward P/E ratio of c 5x. He describes his and Foll's current approach to the UK market – where they have recently invested an extra £50m through increasing LWDB's gearing – as 'opportunistic but not gung-ho'. However, Foll adds: 'If we find value that is not in the UK, we will buy it, such as [recent purchase] Bristol-Myers Squibb'.

While not driven by the change in AIC sector from Global to UK Equity Income, Henderson says most signs currently point to a further increase in LWDB's UK exposure from the current c 76%. 'If it takes five years before the value/growth trade turns, we will have more in the UK [because of buying more attractively valued UK stocks]. If it turns more quickly, the UK will still go up [because value stocks will outperform].'

Many of the recent purchases in the UK have been bought at attractive dividend yields, because share prices have fallen while dividends have not been cut. Henderson adds: 'We are moving more towards yield in the understanding that the wind is in our face. But we are adding to the UK from a [total return] investment perspective, not for yield alone.'

Asset allocation

Investment process: One-stop shop for quality equity exposure

LWDB's portfolio managers aim to hold a diversified portfolio of quality, primarily UK-listed companies. Even before the recent move to the AIC's UK Equity Income sector from the Global sector, more than 70% of LWDB's assets were invested in UK equities, with the overseas portion used to give access to attractive investment areas where there is no compelling UK-listed equivalent (for example, Microsoft in the case of large-cap technology stocks). The only change to the geographical allocation guidelines (see Exhibit 3) as a result of the sector change has been an increase in the maximum UK weighting from 80% to 85%.

Henderson and Foll own a relatively long list of stocks (139 names at 30 June 2019) in order to mitigate company-specific risk and provide a good spread of underlying business areas. They invest across the market capitalisation spectrum on a bottom-up basis, based on their rigorous assessment of company fundamentals, although LWDB has more of a large-cap bias than some of the managers' other funds, with around two-thirds of the portfolio in FTSE 100 names (or overseas equivalents). Henderson and Foll aim to invest in growing businesses whose current share price does not reflect their long-term growth prospects. Although the managers are mainly focused on the UK market, they sit within Janus Henderson's global income team, which gives them access to overseas stock ideas. James Ross is responsible for European stock selection in the LWDB portfolio, while Henderson and Foll oversee the UK and North American stocks, as well as fund selection in Asia and emerging markets, which LWDB rarely invests in directly. The managers tend to build and exit holdings gradually (which also contributes to the length of the stock list); the average starting position is c 0.3% of NAV, although some very large companies may enter the portfolio as a bigger percentage; for example, recent purchase Royal Bank of Scotland is almost 1% of NAV.

The managers' patient approach to investing is reflected in LWDB's relatively low level of portfolio turnover, which stood at 15.4% in FY18 (FY17: 14.0%). The figure for H119 was slightly higher (an annualised rate of 18.6%), driven by greater buying activity as a result of an increase in gearing over the six months. Positions may be reduced and ultimately sold where valuations have become stretched (and future upside is therefore limited) as a result of strong performance, or when there is a deterioration in fundamentals.

Because of the significant contribution (c 25% in H119, but closer to 40% historically, prior to the recent change in the allocation of investment management fees between the revenue and capital accounts) from the IPS business to LWDB's total revenue, Henderson and Foll have the freedom to invest part of the portfolio in lower-yielding stocks while still achieving the trust's objective of providing long-term growth and a steadily growing income. However, when deploying gearing they will tend to target stocks that have yields above the cost of LWDB's borrowing (currently c 4.6%) and can thus provide immediate upside. The portfolio yield is currently c 4.1% on a 12-month forward basis, an increase on six months previously, partly reflecting the use of LWDB's gearing to buy into out-of-favour UK stocks on attractive yields.

Current portfolio positioning

At 30 June 2019, there were 139 stocks in LWDB's portfolio. This included seven collective investment funds, which made up 6.8% of the total (end-FY18: seven funds and 6.9% of the total). The total number of holdings was unchanged compared with six months earlier, although there were some changes at the stock level. The top 10 holdings made up 22.8% of the portfolio, virtually unaltered from 22.6% a year earlier.

Exhibit 4: Portfolio geographic exposure vs allocation guidelines (% unless stated)

	Portfolio end-June 2019	Portfolio end-June 2018	Change (pp)	Allocation guidelines
UK	76.4	73.1	3.3	55-85
North America	9.0	8.7	0.3	0-20
Europe ex-UK	8.2	9.2	(1.0)	0-10
Pacific ex-Japan	4.1	4.8	(0.7)	0-10
Japan	1.0	2.0	(1.0)	0-10
Other	1.3	2.2	(0.9)	0-10
	100.0	**100.0**		**100.0**

Source: The Law Debenture Corporation, Edison Investment Research

In geographical terms (Exhibit 4), the main change compared with 12 months earlier has been a 3.3pp increase in the UK weighting. The managers stress that this is in response to investment opportunities rather than LWDB's move from the AIC Global sector to the UK Equity Income sector. However, the slight increase in the upper bound of the board's allocation guidelines for UK exposure (from 80% to 85%) is largely a result of the sector change. North American exposure has slightly increased compared with 12 months ago but is lower than at end-FY18 (9.4%). All other regions have decreased somewhat over the past 12 months.

Exhibit 5: Portfolio sector exposure vs benchmark (% unless stated)

	Portfolio end-June 2019	Portfolio end-June 2018	Change (pp)	Index weight	Active weight vs index (pp)	Trust weight/ index weight (x)
Industrials	24.1	25.5	(1.4)	11.5	12.7	2.1
Financials	21.6	18.6	3.0	26.1*	(4.5)*	0.8*
Oil & gas	10.4	11.0	(0.6)	14.3	(3.9)	0.7
Consumer services	9.5	8.3	1.2	11.5	(2.0)	0.8
Health care	7.6	8.2	(0.6)	8.5	(0.9)	0.9
Basic materials	7.4	6.9	0.5	8.2	(0.8)	0.9
Pooled equity invts	6.8	10.0	(3.2)	N/A	N/A	N/A
Consumer goods	4.5	3.8	0.7	13.9	(9.4)	0.3
Utilities	3.7	3.3	0.4	2.6	1.1	1.4
Technology	3.1	3.0	0.1	1.2	2.0	2.7
Telecommunications	1.3	1.4	(0.1)	2.4	(1.1)	0.5
	100.0	**100.0**		**100.0**		

Source: The Law Debenture Corporation, Edison Investment Research. Note: *Index weight in financials includes pooled equity investments.

The portfolio remains well diversified by sector (Exhibit 5), with few major changes over the past 12 months. The biggest increase in exposure was to financials (+3.0pp), largely as a result of new positions in Royal Bank of Scotland and Lloyds Banking Group. The largest decrease over 12 months was in pooled equity investments (-3.2pp), with most of the activity occurring in H218, although the position in Stewart Investors Asia Pacific Leaders has been trimmed in H119. The portfolio sector exposure differs markedly from that of the index, with a large overweight in industrials (+12.7pp), where Henderson and Foll continue to find attractively valued opportunities, and a significant underweight in consumer stocks (-11.4pp across consumer goods and consumer services), where many companies are trading at historically high valuations, in spite of the uncertain economic outlook.

The managers have been net buyers of stocks in H119, raising LWDB's gearing from 3% at end-FY18 to 7% at end-H119. They have invested an extra £50m into UK companies, most notably in RBS and Lloyds. Foll says LWDB historically had no exposure to the big UK banks, but both currently look like attractive total return opportunities, trading below book value (giving scope for capital appreciation) and with dividend yields of c 6–7%. The managers have also added to existing holdings in cruise operator Carnival (whose shares had sold off on news of pockets of weak demand in Europe), property company Hammerson (trading at a c 60% discount to the value of its estate) and insurer Direct Line (sustainably yielding more than 9% on the back of stable revenues, despite tough conditions in the motor insurance market). Away from the UK domestic sphere (although still listed in the UK), the managers have also added to Hipgnosis Songs Fund, part of an allocation to high-yielding, less correlated funds that includes Foresight Solar and Urban Logistics REIT.

Henderson and Foll were net sellers of stocks in the US (-£9m), Europe (-£4m) and Asia-Pacific (-£1.5m) over the six months. The position in US healthcare supplies firm Becton Dickinson was sold completely on fears that its valuation had become over-extended, while holdings in US technology stocks such as Microsoft and Lam Research were trimmed. However, a new position was bought in pharmaceutical giant Bristol-Myers Squibb (currently undergoing a merger with biotechnology major Celgene), which is trading on a 12-month forward P/E of less than 8x.

Performance: H119 sees strong absolute returns

Exhibit 6: Five-year discrete performance data

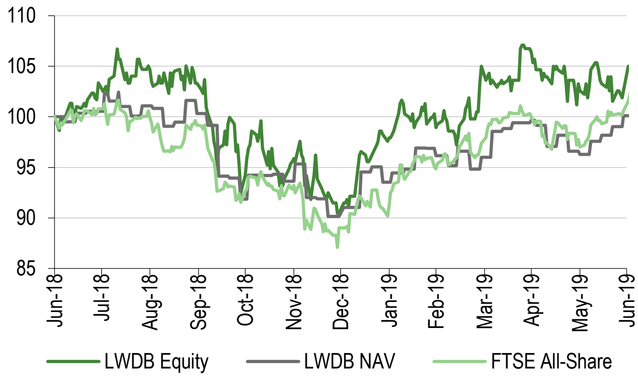
12 months ending	Share price (%)	NAV* (%)	FTSE All-Share (%)	FTSE 250 (%)
30/06/15	1.4	0.9	2.6	14.5
30/06/16	(1.5)	4.0	2.2	(4.6)
30/06/17	21.2	25.9	18.1	22.2
30/06/18	7.3	9.9	9.0	10.6
30/06/19	2.6	0.1	0.6	(3.8)

Source: Refinitiv. Note: All % on a total return basis in pounds sterling. *Cum-income NAV with debt and IPS business at fair value.

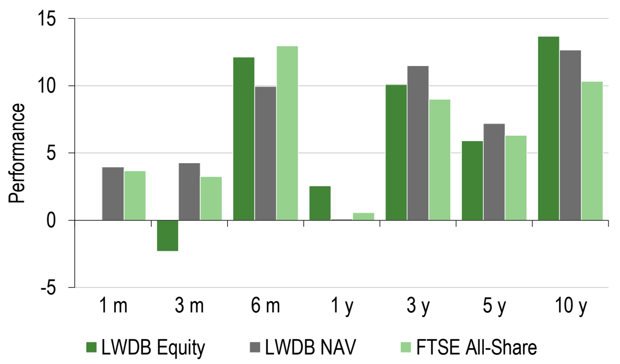
LWDB has performed strongly in absolute terms over H119, with a share price total return of 12.1% and a fair value NAV total return of 10.3%, boosted by an upward revaluation of the IPS business. However, these returns did slightly lag the 13.0% total return from the benchmark FTSE All-Share Index, which may reflect the managers' value bias, as growth stocks continued to perform better on average. In the investment portfolio, the top five positive contributors in H119 were mining company Rio Tinto, homeware store chain Dunelm, US tech giant Microsoft, textile rental firm Johnson Service and paving supplier Marshalls. Together these positions made gains of £18.7m for the portfolio. Henderson and Foll note that, with the exception of Rio Tinto, all these companies are now trading at relatively high valuations versus history, and therefore the managers have been gently reducing some of the positions (notably Marshalls and Microsoft) to realise gains and reinvest in better-value opportunities. The five biggest detractors in H119 were construction and outsourcing firm Kier, sub-prime lender Provident Financial, early-stage technology/healthcare incubator IP Group, International Personal Finance (a peer of Provident Financial with a focus on emerging markets) and International Consolidated Airlines, which owns British Airways. Together these stocks lost £11.2m for the portfolio. Many are now very small positions and the managers have added to some of the names on weakness, where they believe they have been oversold.

Exhibit 7: Investment trust performance to 30 June 2019

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



Price, NAV and benchmark total return performance (%)



Source: Refinitiv, Edison Investment Research. Note: Three-, five- and 10-year performance figures annualised.

While the six-month return has moderately lagged a strongly rising market (the beginning of the period marked a 12-month low for UK and US equities, with a significant bounce back in Q119), over the longer term (Exhibit 7, right-hand chart), LWDB's fair value NAV total return has outperformed the FTSE All-Share Index, with the trust delivering annualised returns of c 7–13% over three, five and 10 years, compared with c 6–10% for the benchmark.

Exhibit 8: Share price and NAV total return performance, relative to indices (%)

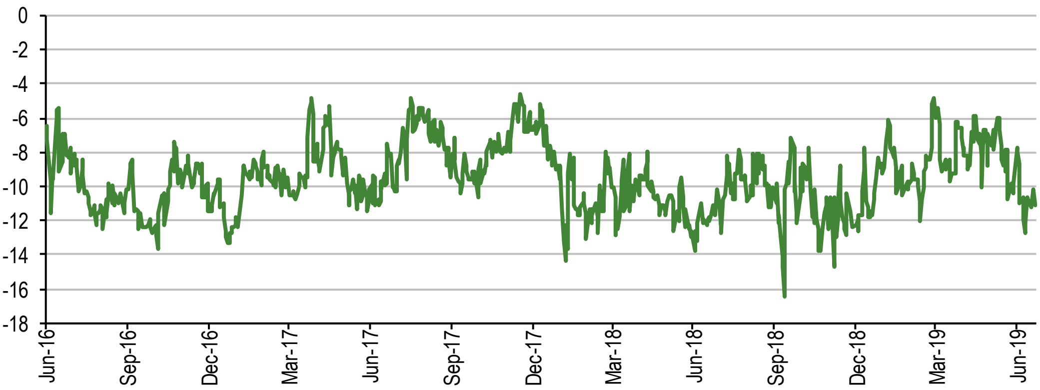
	One month	Three months	Six months	One year	Three years	Five years	10 years
Price relative to FTSE All-Share	(3.5)	(5.4)	(0.7)	2.0	3.0	(1.9)	35.0
NAV relative to FTSE All-Share	0.3	1.0	(2.7)	(0.5)	7.0	4.2	23.3
Price relative to FTSE 250	(2.8)	(5.1)	(0.7)	6.6	2.7	(6.1)	4.5
NAV relative to FTSE 250	1.1	1.3	(2.7)	4.1	6.7	(0.2)	(4.5)

Source: Refinitiv, Edison Investment Research. Note: Data to end-June 2019. Geometric calculation.

Discount: Wider than average and wider than peers

At 23 July 2019, LWDB's shares traded at a 10.2% discount to cum-income NAV (with both the debt and IPS business at fair value). This is higher than both short- and longer-term averages (which range from 7.9% over 10 years to 9.7% over one year), but substantially narrower than the five-year high of 16.5% seen in October 2018. It has widened from a 12-month low of 4.8% in late March (Exhibit 9). Before LWDB began accounting for the fair value of the IPS business in its published NAV (from 1 March 2016), the company's shares had historically traded at a premium, because the share price included an implied fair value of the IPS business that was not included in the NAV, which accounted for the IPS business at cost. However, having moved to reporting fair value NAV, LWDB also provided restated historical NAVs including IPS at fair value, to enable a more meaningful comparison. Based on the restated historical NAVs, LWDB's shares have traded between a c 7% premium and a c 21% discount over the past 10 years. LWDB's discount is currently somewhat wider than the average of its peers in the UK Equity Income sector, possibly reflecting its slightly unorthodox structure, as its performance has been better than average (Exhibit 10). Meanwhile, UK Equity Income funds on average trade at a wider discount than the investment company universe as a whole (at 6.6% versus 4.0% for the industry average excluding VCTs and 3i), suggesting continued investor caution towards UK equities while Brexit uncertainty persists.

Exhibit 9: Share price discount to NAV (including income) over three years (%)



Source: Refinitiv, Edison Investment Research

Capital structure and fees

LWDB is a conventional investment trust, with 118.2m ordinary shares (its only share class) in issue at 23 July 2019. Although the board has the authority to buy back up to 14.99% of shares and to allot shares up to 5% of the issued share capital each year in order to manage a premium or a discount, in practice these powers are used infrequently. Purchases or allotments in recent years have tended to be confined to small numbers of shares in connection with employee share ownership schemes.

Gearing is available to the fund managers via long-term borrowings of £115m (nominal value), made up of £40m of 6.125% secured bonds maturing in 2034, and £75m of 3.77% senior secured notes maturing in 2045. Together this equates to gross gearing (at par value) of c 14.1% of NAV. Because the current low level of interest rates means high-coupon debt is deemed more valuable, the fair or market value of the debt is higher than the par value, standing at £147.2m at 30 June 2019 (end-H119). At fair value, the debt equates to gross gearing of 18.9%, while net gearing was 7.0% at 30 June 2019, compared with a permitted working range of 10% net cash to 20% geared, and a formal limit of 50%. The net gearing is lower than the gross figure because LWDB has significant cash (£86.5m at end-H119) on its balance sheet. Henderson and Foll have steadily increased the net gearing since end-FY18, when it stood at 3.0%.

Janus Henderson Investors is paid an annual management fee of 0.30% of LWDB's net assets (excluding net assets of the IPS business), with no performance fee. While previously all management fees were charged to the revenue account, since the start of FY19, fees have been charged 25% to revenue and 75% to capital, in line with the expected split of future returns. Ongoing charges for FY18 were 0.43%, making LWDB one of the lowest-cost funds in the AIC investment company universe.

Dividend policy and record

LWDB aims to pay a steadily rising income and has a 44-year track record of maintaining or increasing its annual dividend. Dividends are paid twice a year, in September (interim) and April (final). For H119 an interim dividend of 6.6p has been declared, an increase of 10.0% over H118. The revenue from the IPS business supports the payment of a higher level of dividend and means the managers are not constrained to investing only in higher-yielding stocks. While the 25% contribution to total income from IPS was lower in H119 than hitherto (30% in H118, 37% in FY18, and 39% over the long term), this was principally because of higher income from the investment portfolio.

The revenue return for the investment trust portfolio in H119 was 11.76p per share, 42% higher than in H118 and only 12% below the FY18 figure (which covers 12 months rather than six), helped by the reallocation of management fees between capital and income. Normalised IPS earnings per share of 3.92p were 8.9% higher than in H118. The 6.6p interim dividend is c 2.4x covered by group income of 15.68p per share (which was 32% higher than in H118). Based on the current share price and the latest two dividends (H119 interim and FY18 final), LWDB has a prospective yield of 3.3%.

Peer group comparison

Previously a member of the AIC's Global sector, LWDB has recently moved to the UK Equity Income sector. Its FTSE All-Share Index benchmark and primary focus on UK equities means the new sector is a more natural home for the trust, in spite of its continued exposure to overseas stocks. Many of the peers also invest in non-UK companies, and the AIC's guidance is that a UK weighting of c 80% justifies inclusion in the sector.

Of the 24 funds in the UK Equity Income sector with a performance track record of at least one year and a market capitalisation of at least £10m (two funds have been excluded from Exhibit 10 on this basis), LWDB's NAV total returns are above average over one, three, five and 10 years, currently ranking 12th, third, fourth and sixth, respectively, meaning it is in the top half of the peer group over all periods, and in the top quartile over all but one year. Ongoing charges are the third lowest in a very competitively priced group of funds, and, in common with all but one of the peers, there is no performance fee. Gearing is moderately below average. LWDB's dividend yield (based on FY18 dividends) is currently the second-lowest in the sector, in line with its focus on capital appreciation as well as income. However, the 10% year-on-year growth in the H119 dividend builds on a 9.3% increase in the FY18 final dividend versus FY17, suggesting a path to a higher dividend yield for LWDB in the future, supported by the reallocation of management fees between the revenue and capital accounts. In previous years, annual dividend growth has been more in the c 3–5% range. More than one-third of the peer funds currently yield less than the FTSE All-Share dividend yield of 4.1%, possibly reflecting general fund manager concerns over the index's income concentration in a small number of large stocks whose yields may prove unsustainable.

Exhibit 10: AIC UK Equity Income sector as at 22 July 2019*

% unless stated	Market cap £m	NAV TR 1 year	NAV TR 3 year	NAV TR 5 year	NAV TR 10 year	Ongoing charge	Perf. fee	Discount (cum-fair)	Net gearing	Dividend yield
Law Debenture Corporation	**691.4**	**(0.9)**	**31.7**	**43.6**	**228.3**	**0.4**	**No**	**(11.5)**	**107**	**3.2**
Aberdeen Standard Equity Inc Trust	200.1	(6.9)	20.1	29.2	178.7	0.9	No	(5.3)	110	5.0
BlackRock Income and Growth	46.0	(1.2)	22.0	40.0	172.0	1.1	No	(3.4)	101	3.5
BMO Capital & Income	340.2	1.6	37.9	55.1	186.7	0.6	No	0.6	102	3.4
BMO UK High Income Units	119.9	(1.5)	17.7	29.2	144.2	0.3	No	(10.5)	105	4.1
Chelverton UK Dividend Trust	36.2	(12.9)	23.2	40.2	412.3	2.0	No	(13.7)	135	5.2
City of London	1,620.7	2.9	23.1	39.1	210.8	0.4	No	1.7	108	4.4
Diverse Income Trust	335.9	(5.9)	22.8	39.9	--	1.1	No	(6.2)	100	3.9
Dunedin Income Growth	404.6	7.5	28.0	35.0	191.3	0.6	No	(9.4)	108	4.6
Edinburgh Investment Trust	1,144.9	(8.4)	3.2	28.4	196.5	0.6	No	(12.0)	109	4.7
Finsbury Growth & Income	1,839.3	13.6	55.2	105.7	483.1	0.7	No	0.7	101	1.6
Invesco Income Growth	158.4	(0.6)	15.2	30.1	202.4	0.7	No	(15.8)	102	4.2
Investment Company	14.4	1.1	15.2	17.3	344.2	2.7	No	(13.8)	100	5.4
JPMorgan Claverhouse	403.1	(2.8)	30.9	42.0	192.6	0.7	No	(5.1)	109	4.0
JPMorgan Elect Managed Inc	93.1	(1.9)	21.0	30.4	165.7	0.7	No	(2.5)	100	4.3
Lowland	352.6	(9.7)	18.8	22.3	296.9	0.6	Yes	(8.0)	113	4.6
Merchants Trust	532.5	(3.9)	28.3	27.0	183.5	0.6	No	(1.6)	115	5.5
Murray Income Trust	561.9	6.1	29.3	38.0	199.0	0.7	No	(4.5)	103	3.9
Perpetual Income & Growth	741.3	(9.5)	(0.5)	14.4	172.4	0.7	No	(11.5)	116	4.6
Schroder Income Growth	196.4	0.4	27.1	40.6	192.4	0.9	No	(8.6)	112	4.1
Shires Income	80.9	1.1	30.0	39.4	249.7	1.4	No	(1.6)	119	5.0
Temple Bar	838.6	(2.5)	23.4	30.2	198.6	0.5	No	(5.4)	109	4.1
Troy Income & Growth	241.1	7.1	19.4	50.5	219.3	0.9	No	1.4	100	3.3
Value and Income	120.9	(0.2)	15.4	23.5	160.4	1.3	No	(16.2)	129	4.4
Sector average (24 funds)	**463.1**	**(1.1)**	**23.3**	**37.1**	**225.3**	**0.9**		**(6.8)**	**109**	**4.2**
LWDB rank in sector	**6**	**12**	**3**	**4**	**6**	**22**		**18**	**14**	**23**

Source: Morningstar, Edison Investment Research. Note: *Performance to 19 July 2019. TR=total return. Net gearing is total assets less cash and equivalents as a percentage of net assets (100 = ungeared).

The board

LWDB has four independent non-executive directors and two non-independent executive directors. Robert Hingley has been the chairman since April 2018, having joined the board in October 2017 as part of a succession plan. The other non-executive directors and their dates of appointment are Senior Independent Director Robert Laing (April 2012), Audit Committee Chairman Mark Bridgeman (March 2014) and Tim Bond (April 2015). The two executive directors are The Law Debenture Corporation Chief Executive Officer Denis Jackson (appointed to the board in January 2018) and Chief Financial Officer Katie Thorpe (appointed to the board in January 2019). The directors' professional backgrounds include investment management, corporate finance, law and accountancy.

General disclaimer and copyright

This report has been commissioned by The Law Debenture Corporation and prepared and issued by Edison, in consideration of a fee payable by The Law Debenture Corporation. Edison Investment Research standard fees are £49,500 pa for the production and broad dissemination of a detailed note (Outlook) following by regular (typically quarterly) update notes. Fees are paid upfront in cash without recourse. Edison may seek additional fees for the provision of roadshows and related IR services for the client but does not get remunerated for any investment banking services. We never take payment in stock, options or warrants for any of our services.

Accuracy of content: All information used in the publication of this report has been compiled from publicly available sources that are believed to be reliable, however we do not guarantee the accuracy or completeness of this report and have not sought for this information to be independently verified. Opinions contained in this report represent those of the research department of Edison at the time of publication. Forward-looking information or statements in this report contain information that is based on assumptions, forecasts of future results, estimates of amounts not yet determinable, and therefore involve known and unknown risks, uncertainties and other factors which may cause the actual results, performance or achievements of their subject matter to be materially different from current expectations.

Exclusion of Liability: To the fullest extent allowed by law, Edison shall not be liable for any direct, indirect or consequential losses, loss of profits, damages, costs or expenses incurred or suffered by you arising out or in connection with the access to, use of or reliance on any information contained on this note.

No personalised advice: The information that we provide should not be construed in any manner whatsoever as, personalised advice. Also, the information provided by us should not be construed by any subscriber or prospective subscriber as Edison's solicitation to effect, or attempt to effect, any transaction in a security. The securities described in the report may not be eligible for sale in all jurisdictions or to certain categories of investors.

Investment in securities mentioned: Edison has a restrictive policy relating to personal dealing and conflicts of interest. Edison Group does not conduct any investment business and, accordingly, does not itself hold any positions in the securities mentioned in this report. However, the respective directors, officers, employees and contractors of Edison may have a position in any or related securities mentioned in this report, subject to Edison's policies on personal dealing and conflicts of interest.

Australia

Edison Investment Research Pty Ltd (Edison AU) is the Australian subsidiary of Edison. Edison AU is a Corporate Authorised Representative (1252501) of Crown Wealth Group Pty Ltd who holds an Australian Financial Services Licence (Number: 494274). This research is issued in Australia by Edison AU and any access to it, is intended only for "wholesale clients" within the meaning of the Corporations Act 2001 of Australia. Any advice given by Edison AU is general advice only and does not take into account your personal circumstances, needs or objectives. You should, before acting on this advice, consider the appropriateness of the advice, having regard to your objectives, financial situation and needs. If our advice relates to the acquisition, or possible acquisition, of a particular financial product you should read any relevant Product Disclosure Statement or like instrument.

New Zealand

The research in this document is intended for New Zealand resident professional financial advisers or brokers (for use in their roles as financial advisers or brokers) and habitual investors who are "wholesale clients" for the purpose of the Financial Advisers Act 2008 (FAA) (as described in sections 5(c) (1)(a), (b) and (c) of the FAA). This is not a solicitation or inducement to buy, sell, subscribe, or underwrite any securities mentioned or in the topic of this document. For the purpose of the FAA, the content of this report is of a general nature, is intended as a source of general information only and is not intended to constitute a recommendation or opinion in relation to acquiring or disposing (including refraining from acquiring or disposing) of securities. The distribution of this document is not a "personalised service" and, to the extent that it contains any financial advice, is intended only as a "class service" provided by Edison within the meaning of the FAA (i.e. without taking into account the particular financial situation or goals of any person). As such, it should not be relied upon in making an investment decision.

United Kingdom

This document is prepared and provided by Edison for information purposes only and should not be construed as an offer or solicitation for investment in any securities mentioned or in the topic of this document. A marketing communication under FCA Rules, this document has not been prepared in accordance with the legal requirements designed to promote the independence of investment research and is not subject to any prohibition on dealing ahead of the dissemination of investment research.

This Communication is being distributed in the United Kingdom and is directed only at (i) persons having professional experience in matters relating to investments, i.e. investment professionals within the meaning of Article 19(5) of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005, as amended (the "FPO") (ii) high net-worth companies, unincorporated associations or other bodies within the meaning of Article 49 of the FPO and (iii) persons to whom it is otherwise lawful to distribute it. The investment or investment activity to which this document relates is available only to such persons. It is not intended that this document be distributed or passed on, directly or indirectly, to any other class of persons and in any event and under no circumstances should persons of any other description rely on or act upon the contents of this document.

This Communication is being supplied to you solely for your information and may not be reproduced by, further distributed to or published in whole or in part by, any other person.

United States

The Investment Research is a publication distributed in the United States by Edison Investment Research, Inc. Edison Investment Research, Inc. is registered as an investment adviser with the Securities and Exchange Commission. Edison relies upon the "publishers' exclusion" from the definition of investment adviser under Section 202(a)(11) of the Investment Advisers Act of 1940 and corresponding state securities laws. This report is a bona fide publication of general and regular circulation offering impersonal investment-related advice, not tailored to a specific investment portfolio or the needs of current and/or prospective subscribers. As such, Edison does not offer or provide personal advice and the research provided is for informational purposes only. No mention of a particular security in this report constitutes a recommendation to buy, sell or hold that or any security, or that any particular security, portfolio of securities, transaction or investment strategy is suitable for any specific person.