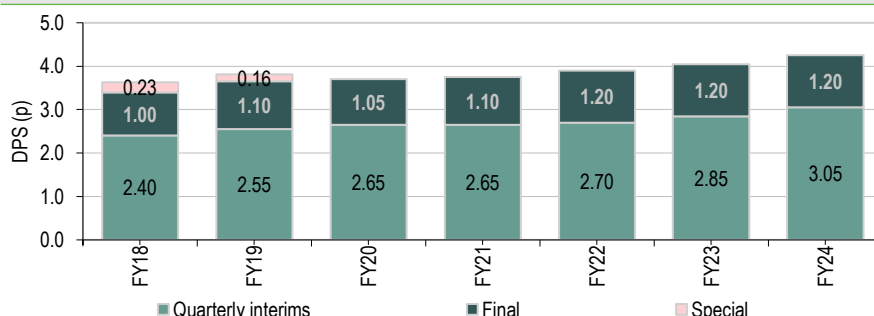


The Diverse Income Trust

An exciting time for UK investors – enjoy the ride

The Diverse Income Trust's (DIVI's) portfolio is broadly diversified by sector and market cap, offering the potential for good upside in rising markets, and unlike the UK market, has consistently grown its ordinary annual dividend since the fund's launch in 2011. The trust's two highly experienced managers, Gervais Williams and Martin Turner at Premier Miton Investors, have become even more bullish on the outlook for UK equities. Their enthusiasm is based on UK companies' inexpensive valuations, and a perception that global investors are now starting to skew their allocations towards firms that are generating surplus cash, such as those in the UK 100 Index. In recent weeks, this large-cap index has started to outperform the S&P 500 and the technology-heavy Nasdaq Composite indices. While the focus is currently on the largest UK companies, if money starts to trickle down the market cap spectrum, it could lead to significant appreciation in mid- and small-cap stocks.

Progressive dividend policy, even during the global pandemic



Source: DIVI, Edison Investment Research

DIVI is truly a multi-cap fund, investing across the spectrum with a broad portfolio split of large-cap (20%), mid-cap (20%), small-cap (55%) and cash (5%), and across all industries. This offers potential outperformance versus funds that are less diversified. Smaller companies tend to outperform over the long term and, as they are generally less well-researched, they can be mispriced.

UK small-cap shares in particular have struggled in recent years as investors have focused on the 'Magnificent 7' large-cap US technology stocks. Taking a longer-term historical perspective, during globalisation, higher-growth names were favoured over more mature dividend-paying companies. However, in the current uncertain economic environment, there is likely to be greater appetite for reasonably priced small-cap and income stocks as the spectrum of returns broadens and investors are more discerning about company valuations.

Since 2019, UK dividend income has declined (partially due to higher share repurchases as a means of returning cash to shareholders). In contrast, DIVI has seen consistent dividend growth, even through the global pandemic. Having a broadly diversified portfolio means that the trust is less reliant on a limited number of companies to generate its income.

Until Brexit, DIVI's shares regularly traded at a premium. If there is a continued increase in demand for UK and particularly UK income strategies, the trust's shares could once again be afforded a higher valuation. Of note, DIVI's discount has been narrowing since October 2024.

Investment companies
UK multi-cap equity income

18 February 2025

Price	94.20p
Market cap	£223m
Total assets	£237m
NAV	100.2p
¹ At 14 February 2025.	
Discount to NAV	6.0%
Current yield	4.6%
Shares in issue	236.4m
Code/ISIN	DIVI/GB00B65TLW28
Primary exchange	LSE
AIC sector	UK Equity Income
Financial year end	31 December
52-week high/low	94.8p 81.6p
NAV high/low	101.5p 86.7p
Net gearing	0.0%

¹At 31 January 2025.

Fund objective

The Diverse Income Trust's investment objective is to provide an attractive and growing level of dividends, coupled with capital growth over the long term. It invests in a diversified portfolio primarily of quoted or traded UK companies across the market cap spectrum, with a bias to high-quality small- and mid-cap stocks. The stock-specific approach means the trust's portfolio does not track a benchmark index.

Bull points

- DIVI's diversified portfolio meant its capital returns fared better during COVID-19 than other funds with narrower stock/sector remits.
- Income diversification enabled DIVI's uninterrupted dividend growth during the global pandemic despite many corporate dividend reductions/suspensions.
- Since launch in 2011, DIVI has built a revenue reserve of over 1x the last annual dividend.

Bear points

- DIVI's strategy harnesses 'the small-cap effect', which can be a major headwind when large-cap stocks are in favour.
- As an equity income strategy, with a low beta portfolio, the trust is likely to underperform during 'risk-on' markets.
- DIVI's intensive research process contributes to its above-average ongoing charge within the AIC UK Equity Income sector.

Analyst

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DIVI: The UK equity income, multi-cap specialist

Williams and Turner aim to deliver good and growing total returns, by investing in a wide range of good and growing companies, which are expected to produce good and growing dividends. Along with the potential for a change in sentiment towards UK stocks, in an environment of heightened geopolitical tensions investors could increasingly turn their attention towards income and away from the capital growth strategies that have been favoured during the multi-decade period of globalisation and abundant market liquidity.

DIVI has a strong long-term record of outperformance (all figures quoted are total returns). Since launch in April 2011, until the end of H125 (ending 30 November 2024), the trust's adjusted NAV increased by 235.5% and its share price rose by 196.2%. These returns compare favourably with the Deutsche Numis All-Share Index (+123.6%), the Deutsche Numis Smaller Companies plus AIM (ex-Investment Companies) Index (+106.1%) and the AIC UK Equity Income peer group (+176.1%).

Overall, low volatility, coupled with the trust's outperformance since inception, implies that DIVI offers investors an attractive mix of high alpha and a below-average beta.

Highlights from DIVI's H125 report

In H125, DIVI delivered a strong performance with NAV and share price total returns of +4.9% and +5.3% respectively. These were ahead of the total returns of the Deutsche Numis All-Share Index (+2.1%), the Deutsche Numis Smaller Companies plus AIM (ex-Investment Companies) Index (-2.3%) and the peer group (+0.9%).

Revenue per share of 2.63p was 10.5% higher than 2.38p in H124. So far in FY25, two dividends have been announced. The first interim payment of 1.00p per share was flat year-on-year, while the second interim dividend is 1.05p per share, which is a 5% increase versus 1.00p per share in H123. The board has said that it expects the total annual dividend will exceed the FY24 total distribution of 4.25p per share. DIVI's ongoing charges ratio in H125 was 1.09%, which was 5bp lower than 1.14% in FY24. This was in part due to a reduction in the investment management fee, which took effect from 1 June 2024.

The trust has an annual redemption facility, which the board considers important as it offers liquidity to shareholders. At the end of May 2024, 25.8% of the share base was tendered. From 2025, the redemption date will move from the end of May to the end of August to separate the redemption administration from the preparation of DIVI's annual results.

Current portfolio breakdown

At the end of December 2024, DIVI's top 10 holdings made up 25.4% of the portfolio, which was a higher concentration compared with 21.5% 12 months earlier; four names were common to both periods.

Exhibit 1: DIVI's top 10 holdings

Company	Sector	Portfolio weight Dec 2024 (%)	Portfolio weight Dec 2023 (%)
Galliford Try Holdings	Industrials	3.4	2.2
TP ICAP Group	Financials	3.1	2.6
Paypoint	Industrials	2.9	2.1
Pan African Resources	Basic materials	2.7	N/A
CMC Markets	Financials	2.7	N/A
XPS Pensions Group	Financials	2.7	3.0
Aviva	Financials	2.1	N/A
BT Group	Telecommunications	2.0	N/A
Concurrent Technologies	Technology	1.9	N/A
Savannah Energy	Energy	1.9	N/A
Total:		25.4	21.5

Source: DIVI, Edison Investment Research. Note: N/A is not in end-December 2023 top 10.

Williams explains that UK companies that have delivered strong results have not seen this fully reflected in their share prices (via a revaluation) due to the ongoing outflows from the UK market. Hence, the managers are holding positions for longer to realise their full value, and the top 10 concentration is rising. The total number of holdings is also declining. At the end of 2024, there were 116 names in the fund versus 122 at the end of 2023. Williams suggests that the number of holdings is likely heading towards 80.

The manager highlights a few of DIVI's largest holdings. He says that two years ago, one could buy Galliford Try for less than the cash on its balance sheet. Its margins have increased, partly due to Galliford Try's management team moving away from riskier contracts, and there is potential for further margin expansion.

TP ICAP, which considers itself to be the world's largest inter-dealer and energy and commodities broker, is planning a partial IPO of its data and analytics business this year, which will release cash that could be returned to shareholders via another higher dividend.

According to Williams, having become oversold in 2023, CMC Markets' share price rallied in 2024 before pulling back. He highlights the risk management skills of CMC's management, while the company's flexible software is a competitive advantage as it rolls out new services and expands its geographic footprint.

Concurrent Technologies is another stock that Williams is very upbeat about. A few years ago, new management replaced the family-based team. The company had a retail share offer in August 2023 at 65p per share; an investment made then would have grown around three times based on the current share price.

Exhibit 2: Market cap breakdown at end H125

(%)	Mainstream stocks	Small-cap stocks	Other/alternative market
DIVI	32.3	36.3	31.4
Deutsche Numis All-Share Index	90.0	8.0	2.0

Source: DIVI, Edison Investment Research. Note: Numbers subject to rounding.

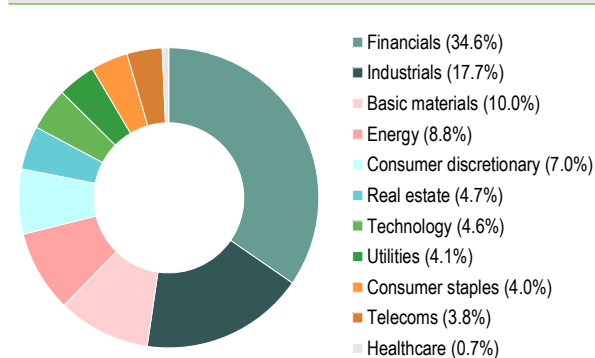
Exhibit 2 shows that DIVI's breakdown by market cap is significantly different to that of the Deutsche Numis All-Share Index. However, Exhibit 3 is more instructive showing a detailed market cap breakdown of DIVI's portfolio, which is broadly split: large-cap (20%), mid-cap (20%), small-cap (55%) and cash (5%). There were minimal changes in the fund's market-cap breakdown between year-end 2024 and year-end 2023.

Exhibit 3: DIVI's detailed market cap breakdown

	End December 2024 (%)	End December 2023 (%)	Change (pp)
AIM	28.6	29.3	(0.7)
Small cap	20.9	22.1	(1.2)
Large cap	20.7	23.3	(2.6)
Mid cap	20.2	16.9	3.3
UK listed non-index	2.7	2.7	0.0
Fledgling	0.4	1.4	(1.0)
Other	0.6	1.0	(0.4)
Cash	5.9	3.3	2.6
	100.0	100.0	

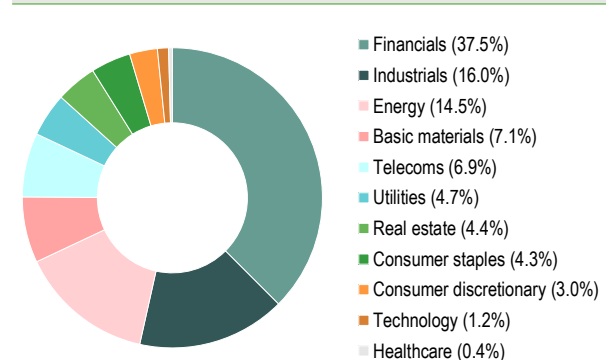
Source: DIVI, Edison Investment Research

Exhibit 4: Breakdown by sector at end H125



Source: DIVI, Edison Investment Research

Exhibit 5: Breakdown by sector income at end H125



Source: DIVI, Edison Investment Research

Financials has been the largest sector exposure since DIVI was launched in 2011. It is one of the higher-yielding sectors representing a 2.9pp higher percentage of the trust's overall income than its portfolio weighting. Other notable differences between the two measures are the higher dividend yields in energy (+5.7pp) and telecom (+3.1pp) with lower yields in consumer discretionary (-4.0pp), IT (-3.4pp) and materials (-2.9pp). DIVI's relatively low exposure to consumer discretionary stocks seems appropriate given these companies tend to be major employers and employee costs are rising.

Recent portfolio activity

Recent additions to the portfolio include Lloyds Banking Group and OSB Group (buy-to-let lending). A higher savings rate has encouraged an increase in consumer deposits. As this is low-cost funding, it has led to an expansion in bank net interest margins. The valuation of B&M European Value has declined under its new CEO. There is concern about increasing staff costs and negative like-for-like sales as B&M undercuts supermarket prices. However, Williams reports that trading is robust and free cash flow generation is strong, while B&M has announced a special dividend.

Holdings exiting the portfolio, primarily due to the managers locking in profits include: Gateley Holdings, Mears Group, Property Franchise Group, Jadestone Energy and property companies Helical and LondonMetric Property.

Williams' perspectives on the UK market

The manager is excited about the performance of UK stocks so far in 2025, noting that the top 100 UK company index is hitting new highs and is outperforming the US market, including the technology-heavy Nasdaq Composite Index (60% technology). He notes that results from the 'Magnificent 7' have not been great, suggesting that their stock prices already reflect their growth opportunities.

While some investors may consider income stocks to be dull, Williams points to Barclays and Lloyds Banking Group, whose shares have rallied by more than 100% in the last 12 months. The manager suggests that income stocks are just starting to move and there is much more to come. He points to the uncertain investment backdrop, where there will be winners and losers from the shift from globalisation to protectionism, while the unpredictability of US President Trump is likely to increase stock market volatility. Also, investors generally have significant weightings in a few stocks and sectors, which they may look to unwind.

Williams expects the performance of small-caps stocks to catch up with that of large-cap companies, as money trickles down from large to mid- and small-cap stocks. He suggests that small-cap stocks in particular look very appealing, and that it is an important time as a relatively small amount of money can really affect the performance of the smaller end of the market.

The UK is still experiencing fund outflows, but this is starting to be outweighed by international investors buying UK stocks. This is despite a lack of UK government support for the domestic market and companies delisting from the UK either as a result of being taken over or moving to an overseas exchange in search of higher valuations.

Williams highlights how attractive UK valuations are, outlining how they were low in April 2011 and rose modestly up to May 2021 as global stock markets appreciated. However, since then, UK stocks have come under pressure from UK open-ended fund redemptions. This is in stark contrast to the US, which has been the go-to area for global investors and has become very expensive compared to other markets and its own history.

The manager explains that if a UK company is trading at an inexpensive valuation, it does not necessarily mean its business prospects are lacklustre. He says that there are several names in DIVI's portfolio that have the potential to be global winners but have seen heavy selling, resulting in a low valuation. These companies include: Beeks Financial Cloud Group (cloud computing, connectivity and analytic services), Gaming Realms (mobile-gaming content), Gulf Marine (offshore support vessels), Raspberry Pi (single-board computers) and Record (currency and derivative management systems).

Performance: Looking brighter – outperformance in H125

DIVI is one of 18 funds in the AIC UK Equity Income sector; while the trust has a differentiated strategy, a peer group comparison provides some context. The trust's NAV total return ranks third since inception in April 2011. DIVI has an above-average total return over the last 12 months ranking fifth, and is broadly in line over the last decade, ranking 12th. At 13 February 2025, the trust's discount was below the peer group average, it has an above-average ongoing charge, no gearing and a dividend yield that was modestly below the mean. As its name implies, DIVI's portfolio is made up of a relatively large number of holdings, meaning the trust is not overly reliant on a few high-yielding companies to fulfil its income requirement. Unusually, DIVI has holdings right across the market cap spectrum from small immature companies up to major multinational operators.

Exhibit 6: AIC Equity Income sector at 13 February 2025

% unless stated	Market cap (£m)	1Y NAV TR	3Y NAV TR	5Y NAV TR	10Y NAV TR	SI NAV TR*	Disc (cum-fair)	Ongoing charge	Net gearing	Dividend yield
Diverse Income Trust	223.2	22.1	(0.6)	24.5	77.8	234.1	(5.6)	1.1	100	4.5
abrdn Equity Income Trust	157.2	25.4	6.6	8.3	30.8	105.6	(3.3)	0.9	114	7.0
BlackRock Income and Growth	39.7	18.7	24.9	32.3	78.5	148.7	(11.9)	1.2	105	2.4
Chelverton UK Dividend Trust	32.1	17.5	(13.6)	2.8	48.0	206.2	(5.7)	2.7	153	9.1
City of London	2,168.8	21.7	26.7	33.8	81.5	185.3	(2.8)	0.4	108	4.8
CT UK Capital and Income	330.9	16.2	18.0	20.9	94.5	161.2	(4.6)	0.7	105	3.8
CT UK High Income	84.3	22.8	24.8	24.1	65.0	130.6	(1.5)	1.1	110	5.6
Dunedin Income Growth	378.9	11.1	16.0	20.7	71.0	139.3	(11.1)	0.6	111	4.9
Edinburgh Investment	1,111.0	29.0	36.4	52.6	81.0	218.2	(10.3)	0.5	105	3.6
Finsbury Growth & Income	1,412.4	14.1	19.3	23.8	117.8	302.5	(6.3)	0.6	102	2.1
JPMorgan Claverhouse	408.2	20.3	17.9	23.0	78.1	157.6	(6.5)	0.7	109	4.8
Law Debenture Corporation	1,210.6	20.4	20.2	55.1	123.9	246.7	1.2	0.5	100	3.5
Lowland	335.9	16.7	9.2	18.0	51.7	158.9	(7.4)	0.7	113	4.8
Merchants Trust	805.9	16.9	10.1	34.4	81.9	164.8	(5.4)	0.5	113	5.2
Murray Income Trust	854.8	15.1	17.0	24.4	84.0	161.7	(11.1)	0.5	111	4.5
Schroder Income Growth	201.1	21.8	22.5	31.0	76.3	178.9	(11.4)	0.8	112	4.9
Shires Income	100.9	21.4	13.2	24.7	78.1	184.4	(9.4)	1.1	116	5.8
Temple Bar	816.8	34.8	30.5	32.9	79.4	173.4	(7.6)	0.5	108	3.7
Simple average	592.9	20.3	16.6	27.1	77.7	181.0	(6.7)	0.8	111	4.7
Rank (out of 18)	12	5	17	9	12	3	7	16	17	11

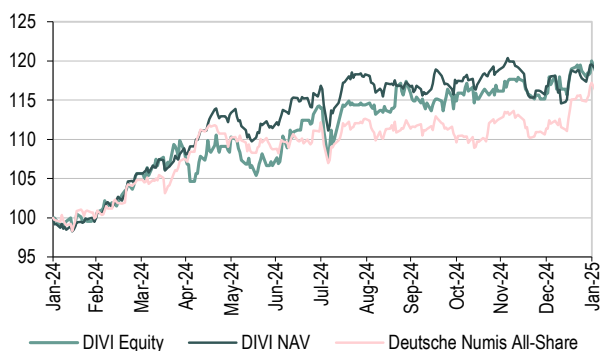
Source: Morningstar, Edison Investment Research. Note: Performance is TR based on ex-par NAV. *Since DIVI's inception on 28 April 2011.

Morningstar data show that, within the sector, there are only two funds classified as small-cap value funds: DIVI and the much smaller Chelverton UK Dividend Trust. DIVI has, by far, the superior performance over all periods shown. Considering the whole sector, at c 55% the trust has a larger-than-average exposure to cyclical sectors (high sensitivity to the business cycle), a 10% exposure to defensive sectors (anticyclical), which is around half of the sector average, and a modestly lower-than-average weighting (c 35%) in sensitive sectors (moderate correlation to the business cycle).

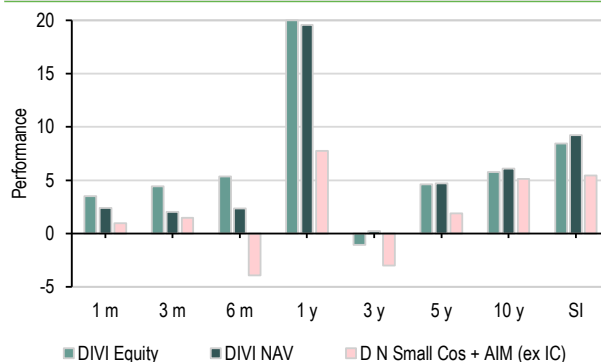
Exhibit 7: Five-year discrete performance data

12 months ending	Share price (%)	NAV (%)	Numis All-Share (%)	Numis Smaller Cos ex ICs (%)	CBOE UK All Cos (%)
31/01/21	10.7	9.7	(5.6)	(0.9)	(8.6)
31/01/22	16.8	13.9	16.5	15.1	19.3
31/01/23	(11.9)	(9.2)	3.3	(7.5)	6.3
31/01/24	(8.4)	(7.3)	1.6	1.8	2.0
31/01/25	20.0	19.6	17.2	13.4	17.6

Source: LSEG Data & Analytics, Edison Investment Research. Note: All figures are total return in pounds sterling.

Exhibit 8: Share price and NAV performance to 31 January 2025 (one year rebased)


Source: DIVI, Edison Investment Research

Exhibit 9: Price, NAV and index total return (%)


Source: DIVI, Edison Investment Research. Note: Three-, five- 10- and SI- (since inception) figures are annualised (£).

Exhibit 9 illustrates how well DIVI has performed against the Deutsche Numis Smaller Companies plus AIM (ex-Investment Companies) index. It has delivered above-index performance over the past one, five and 10 years, and even more so since the trust's inception in April 2011.

As highlighted earlier in the report, in H125, DIVI's NAV and share price total returns outpaced the comparator index's total return. The largest positive contributors to the trust's NAV returns were: XPS Pensions (+1.17pp); Paypoint (+1.14pp); Galliford Try Holdings (+1.09pp); Pan African Resources (+0.87pp); and Just Group (+0.69pp). On the opposite side of the ledger, the largest performance detractors were Zotefoams (-0.53pp); CT Automotive Group

(-0.47pp); Inspired (-0.37pp); Sabre Insurance Group (-0.36pp); and Man Group (-0.35pp).

Exhibit 10: Share price and NAV total return performance, relative to indices (%)

	1 month	3 months	6 months	1 year	3 years	5 years	10 years
Price relative to Numis All Share	(1.6)	(2.3)	0.8	2.4	(21.2)	(7.3)	(4.9)
NAV relative to Numis All Share	(2.7)	(4.6)	(2.1)	2.0	(18.1)	(7.0)	(2.1)
Price relative to Numis Smaller Cos ex ICs	2.0	1.3	7.6	5.9	(9.2)	3.0	(3.4)
NAV relative to Numis Smaller Cos ex ICs	0.9	(1.0)	4.5	5.5	(5.7)	3.3	(0.6)
Price relative to CBOE UK All Companies	(2.2)	(2.4)	0.2	2.0	(24.0)	(9.9)	(6.7)
NAV relative to CBOE UK All Companies	(3.2)	(4.7)	(2.6)	1.7	(21.1)	(9.6)	(3.9)

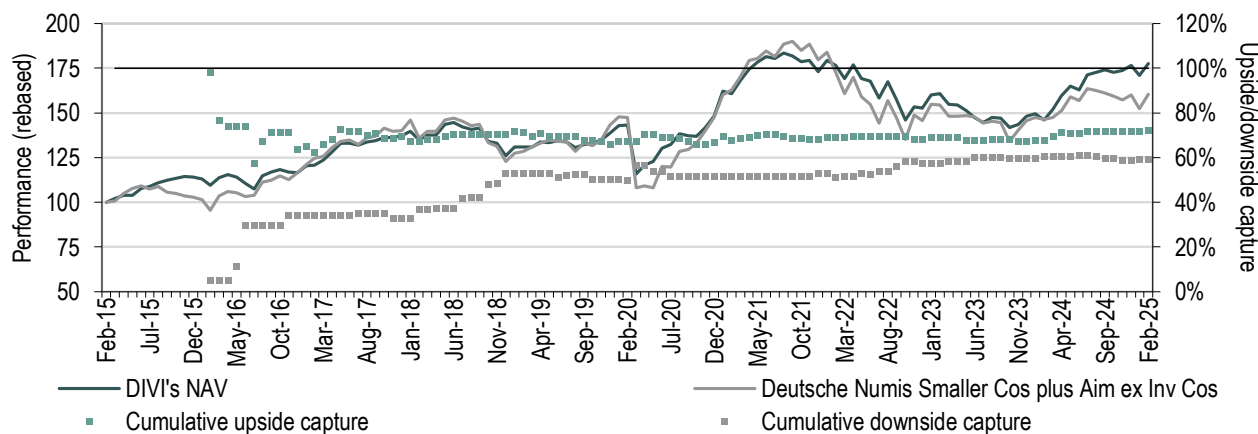
Source: LSEG Data & Analytics, Edison Investment Research. Note: Data to end January 2025. Geometric calculation (%).

Commenting on DIVI's recent performance, Williams said that the trust's relative performance was weak in January 2025 as, although there is now some foreign investor interest in UK stocks, this has initially been focused on large-cap companies. The manager reiterates that he expects the shares in small-cap companies to catch up. In recent months, positive contributors to DIVI's performance include: Covenant Technologies, Galliford Try, Diversified Energy, TP ICAP and gold stocks Pan African Resources and Greatland Gold (due to a higher gold price). Stocks that have detracted include: CMC Markets and Shoe Zone.

Upside/downside capture analysis

Exhibit 11 shows DIVI's upside/downside cumulative capture rates over the last 10 years versus the Deutsche Numis Smaller Companies plus AIM (excluding Investment Companies) Index. The trust's defensive portfolio qualities are shown by capture rates of less than 100%. However, the upside capture of 72% and a downside capture of 59% imply that DIVI will appreciate more in a rising market than it will lose in a falling market.

Exhibit 11: DIVI's upside/downside capture



Source: LSEG Data & Analytics, Edison Investment Research

Cumulative upside/downside capture calculated as the geometric average NAV total return (TR) of the fund during months with positive/negative reference index TRs, divided by the geometric average reference index TR during these months. A 100% upside/downside indicates that the fund's TR was in line with the reference index's during months with positive/negative returns. Data points for the initial 12 months have been omitted in the exhibit due to the limited number of observations used to calculate the cumulative upside/downside capture ratios.

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