EDISON

The Brunner Investment Trust

Managing well through choppy waters

Investment trusts
Global equities

The Brunner Investment Trust's (BUT's) lead manager is Matthew Tillett at Allianz Global Investors. He is 'delighted' by the fund's relative performance so far in 2022, given elevated levels of share price volatility, and points to the balanced investment approach whereby the portfolio is not overexposed to a single factor within the global stock market. He has taken advantage of this volatility to improve the growth profile of BUT's portfolio as he has been able to invest in some high-quality companies whose valuations would normally be considered prohibitive for the fund, including US software developer Adobe. BUT's board has just announced the FY22 first interim dividend, which is 9.6% higher year-on-year despite the challenging market backdrop, and it highlighted the trust's healthy revenue reserves and portfolio income that is comfortably above pre-pandemic levels.

NAV outperformance versus the benchmark over the last three years (Tillett became lead manager on 13 May 2020)

Source: Refinitiv, Edison Investment Research. Note: Total returns in sterling.

The analyst's view

Tillett's measured approach and BUT's diversified portfolio has served investors relatively well during a period of above-average stock market volatility in 2022. The trust offers an active but balanced portfolio of c 65 high-quality global equities across the market cap spectrum, with the prospects of both income and capital growth; BUT has grown its annual dividend in each of the last 50 consecutive years. All stocks are selected on a bottom-up basis and the resulting portfolio currently has meaningful overweight exposures versus the benchmark in industrial and healthcare stocks. The trust's relative performance has improved since the change of lead manager in May 2020 and BUT's NAV is ahead of its benchmark over the last one, three, five and 10 years.

Potential for a narrower discount

BUT is currently trading at an 11.9% discount to cum income NAV, which is wider than the 10.0%, 10.4% and 10.4% average discounts over the last one, three and five years respectively. There is scope for a higher valuation given the trust's commendable relative performance; its NAV total returns rank second over one year and fourth over three years out of the 17 funds in the AIC Global sector.

14 June 2022

Price	**975.0p**
Market cap	**£416m**
AUM	**£481m**
NAV*	1,107.2p
Discount to NAV	11.9%

*Including income. As at 10 June 2022.

Yield		2.1%
Shares in issue		42.7m
Code		BUT
Primary exchange		LSE
AIC sector		Global
52-week high/low	1,130.0p	942.0p
NAV* high/low	1,229.0p	1,058.3p

*Including income.

Gearing

Net gearing*	7.1%

*As at 30 April 2022.

Fund objective

The Brunner Investment Trust aims to provide growth in capital value and dividends over the long term through investing in a portfolio of global equities. Its benchmark is a composite of 70% All-World ex-UK (£) Index and 30% All-Share Index.

Bull points

- Balanced portfolio of global equities, aiming to generate both capital and income growth.
- Long-term record of outperformance versus its benchmark and 50 consecutive years of higher dividends.
- Scope for a higher valuation.

Bear points

- The fund is likely to underperform in a market led by very high growth or deep value stocks.
- Structural gearing of £25m will amplify capital losses in a market sell-off.
- Dividend is modestly below the peer group average.

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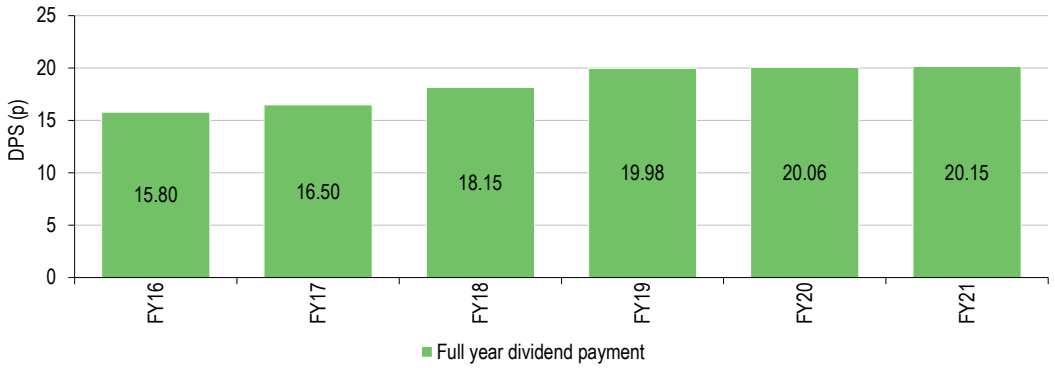
Recent development

On 9 June 2022, BUT's board declared the first interim dividend in respect of FY22 at 5.15p per share, which was a 9.6% increase year-on-year. It anticipates a similar level for the second and third interim payments with an unchanged final dividend of 6.05p per share. The total FY22 distribution of 21.50p per share would equate to a 6.7% increase year-on-year and would be the 51st consecutive year of higher annual dividends.

BUT's board notes that it is impossible to judge the impact that higher interest rates will have on economic growth, but takes comfort from the fact that the manager's revenue forecasts are comfortably above pre-pandemic levels and the trust has revenue reserves of 24.7p per share, which is 1.15x the anticipated FY22 dividend payment. Based on its current share price, BUT offers a 2.1% yield.

Exhibit 1: Dividend history since FY16



Source: Bloomberg, Edison Investment Research

The fund manager: Matthew Tillett

The manager's view: Opportunities from market weakness

Commenting on the investment backdrop, Tillett says it has been a difficult start to 2022. Stocks have repriced in an environment of rising interest rates, due to higher inflation expectations. At the end of 2021, certain parts of the market were highly valued, such as technology stocks; these companies have subsequently derated as interest rate expectations have risen and there has been a rotation in investor preference from growth to value stocks. However, cyclical stocks have been more of a concern for investors since the start of the war in Ukraine as there are higher prospects of a hit to consumer confidence with people already facing unprecedented cost increases: this could put consumer discretionary stocks under further pressure. Unsurprisingly, defensive stocks have performed relatively better this year along with those that are short-term beneficiaries of higher inflation, such as energy and mining stocks.

The manager's opinion is that 'the changing macroeconomic environment does not warrant a major shift in BUT's portfolio construction'. He believes that consumers are not financially stretched, as their personal balance sheets were generally in good shape prior to the pandemic and there have not been the excesses that were in evidence before the global financial crisis. Also, unlike then, the financial sector is not distressed, and banks are now well capitalised. Tillett suggests that 'with the help of pandemic handouts consumers can cope with a certain level of inflation'. Nevertheless, there are signs of a tougher economic environment with major US retailers Target and Walmart both reporting earnings that lagged consensus expectations, due to higher costs. However, despite

some companies starting to see some weakening demand, the manager does not feel that there are huge excesses that will lead to an economic collapse.

'Companies remain investible', according to the manager and he is taking advantage of share price opportunities when they arise. He considers that inflation is the most important economic variable as it is driving central banks' monetary policy. They need to raise interest rates to avoid losing their credibility, but in general, they have been slow to react to higher inflation, which they initially viewed as transitory. The US economy was 'running hot' says Tillett and there have been widespread supply-side bottlenecks and issues related to China's COVID-19 lockdowns. However, he believes these pressures should ease and generally, 'capitalist economies are good at working through supply-side challenges'. Providing more information about China, the manager says there is a political issue to overcome, as President Xi Jinping has staked his reputation on his zero-COVID policy. There is a Chinese party congress in autumn 2022, so Tillett considers that a dramatic change in policy is unlikely until Xi Jinping has established his next term in office. The manager opines that the zero-COVID policy is clearly not working and needs to change towards an improved treatments and more vaccinations approach. He suggests that if demand declines in the West due to the rising cost of living, this could reduce inflationary pressures. In his view, US inflation does not need to go back to 2%, and if the rate of change moderates, that should be sufficient to lead to improved levels of consumer and business confidence. However, he suggests that the timing of any improvement in the inflationary backdrop is uncertain, while the war in Ukraine brings an elevated risk that prices will continue to rise.

While the manager is taking advantage of market weakness, he admits that 'you can never be sure that all the bad news is baked into stock prices', although he suggests that the valuations of most cyclical stocks are 'implying a significant reduction in earnings'. Tillett expects some pressure in the consumer discretionary sector even though so far, earnings reports have 'generally been okay'. He says that there are companies that have fully recovered and are operating at levels above those experienced in 2019. However, Tillett prefers to focus on those firms that are operating below their 2019 levels, such as travel and leisure stocks, and those with a meaningful Chinese exposure. He believes that for these businesses 'the post-pandemic rebound will be powerful, and should help to offset any economic weakness'.

Current portfolio positioning

Looking at BUT's top 10 holdings, at both the end the end of April 2022 and a year earlier, they made up 30.6% of the portfolio; six positions were common to both periods.

Exhibit 2: Top 10 holdings (as at 30 April 2022)

Company	Country	Sector	Portfolio weight %	
			30 April 2022	30 April 2021*
Microsoft	US	Software & computer services	4.9	4.5
UnitedHealth	US	Healthcare equipment & services	4.8	4.0
Visa	US	Financial services	3.6	2.7
Adidas	Germany	Sportswear manufacturer	2.9	N/A
Roche	Switzerland	Pharmaceuticals & biotechnology	2.8	2.6
Taiwan Semiconductor	Taiwan	Technology hardware & equipment	2.5	2.9
Munich Re	Germany	Non-life insurance	2.4	2.6
Novo Nordisk	Denmark	Pharmaceuticals & biotechnology	2.3	N/A
Shell	UK	Oil & gas producers	2.2	N/A
Schneider Electric	France	Energy management & automation	2.2	N/A
Top 10 (% of portfolio)			**30.6**	**30.6**

Source: The Brunner Investment Trust, Edison Investment Research. Note *N/A where not in end-April 2021 top 10.

Over the 12 months to end-April 2022, the largest changes on a geographic basis were a 4.1pp higher UK weighting and a 2.6pp reduction to the trust's North American exposure. The largest

active weights were an overweight allocation to continental Europe and lower weightings to the UK (-6.1pp) and Pacific ex-Japan (-5.4pp).

Exhibit 3: Portfolio geographic exposure versus benchmark (% unless stated)

	Portfolio end-April 2022	Portfolio end-April 2021	Change (pp)	Benchmark weight	Active weight vs b'mark (pp)	Trust weight/ b'mark weight (x)
North America	43.7	46.3	(2.6)	45.3	(1.6)	1.0
Europe ex-UK	25.6	26.7	(1.1)	9.0	16.6	2.8
UK	23.9	19.8	4.1	30.0	(6.1)	0.8
Pacific ex-Japan	4.0	4.6	(0.6)	9.4	(5.4)	0.4
Japan	2.8	2.7	0.1	4.4	(1.6)	0.6
Latin America	0.0	0.0	0.0	0.7	(0.7)	0.0
Middle East & Africa	0.0	0.0	0.0	1.2	(1.2)	0.0
	100.0	**100.0**		**100.0**		

Source: The Brunner Investment Trust, Edison Investment Research. Note: Excludes cash. Numbers subject to rounding.

A year-on-year comparison is unavailable for BUT's sector weightings due to changes in sector classifications during the last 12 months. The largest active exposures versus the benchmark are overweight positions in industrials (+7.6pp) and healthcare (+7.0pp) and an underweight to the consumer staples sector (-5.6pp).

Exhibit 4: Portfolio sector exposure versus benchmark (% unless stated)

	Portfolio end-April 2022	Benchmark weight	Active weight vs benchmark (pp)	Trust weight/ benchmark weight (x)
Industrials	20.3	12.7	7.6	1.6
Financials	19.0	16.6	2.4	1.1
Healthcare	18.7	11.7	7.0	1.6
Technology	13.7	16.3	(2.6)	0.8
Consumer discretionary	13.3	13.0	0.3	1.0
Energy	4.1	6.0	(1.9)	0.7
Basic materials	3.5	5.4	(1.9)	0.7
Consumer staples	3.3	8.9	(5.6)	0.4
Utilities	3.1	3.3	(0.2)	0.9
Real estate	1.0	3.1	(2.1)	0.3
	100.0	**100.0**		

Source: The Brunner Investment Trust, Edison Investment Research. Note: Excludes cash. Numbers subject to rounding.

In April 2022, Tillett added a new position in mid-cap (c £500m) Atalaya Mining to BUT's portfolio; he says that this company plays into the energy transition theme. Atalaya is a copper miner with assets in Spain on the Pyrite mining belt. The manager considers it to be a very well managed company with an established operational facility, which is generating around 55k tons of copper each year. This commodity is a beneficiary of the electrification of economies and the energy transition away from fossil fuels and is used in products including electric vehicles, solar panels and batteries.

Tillett says that within the copper mining industry the supply side is relatively tight with additional resources located in tough geographical or political areas and suggests that it will be difficult to fulfil the anticipated demand growth over the next 10–20 years. The manager finds Atalaya's prospects more attractive than those of a large miner with major development projects, helped by Atalaya's management team's knowledge around geology, reserves and the company's growth potential. Atalaya has other higher-grade deposits that are yet to be developed and Tillett believes that this growth potential is underappreciated by the market, where analysts are only modelling the current mine plan. The manager explains that Proyecto Riotinto, its current operating mine, has an 11-year life with its existing deposit, but production and mine life can be grown significantly once the other deposits are brought on line. Atalaya also has blended production capabilities that can respond to current market conditions; if commodity prices are high, it uses lower-grade ore, while if prices are weak, it can shift production to higher-grade ore. Tillett expects the company's share price to re-rate as investors comes to appreciate its long-term cash flow potential.

The manager explains that Atalaya is listed on AIM and is not a well known company. It had a concentrated share register with three holders each owning around 20%. One sold its position around 12 months ago and then in April 2022, a second holder was a forced seller as it was under financial pressure. As a result, BUT's position was initiated at a double-digit discount to the prevailing share price. Tillett says the company is expected to move to a main-market listing in the next 12 months, which should make it more visible to investors.

Commenting on other portfolio activity, the manager says that he has been taking some profits in the healthcare sector, such as reducing the position in AbbVie. Following the acquisition of Allergan, the company is less reliant on Humira for the treatment of autoimmune conditions. However, Humira still represented 37% of AbbVie's 2021 revenues and is going off patent next year. Tillett believes that the company is 'likely to struggle to grow' its earnings over the next two to three years. The manager has also been adding to some high-quality industrial companies in the fund such as Assa Abloy and Atlas Copco, which he considers to be moderately cyclical businesses with positive structural drivers that are now trading at attractive valuations.

A few months ago, the manager added to BUT's Adidas position. This stock has performed poorly, which Tillett believes is due to its meaningful exposure to China, where its business is very depressed. He suggests that any normalisation of the Chinese economy over the next 12–18 months should be beneficial for Adidas. The manager believes that the post-pandemic kicker is underappreciated and should benefit some of BUT's other holdings, including Booking Holdings, Bright Horizons Family Solutions, Estée Lauder Companies and Yum! Brands. In February 2022, Tillett sold BUT's positions in Fresenius and Merlin Properties, as Tillett identified better opportunities elsewhere in the fund.

The manager highlights the trust's position in Homeserve, citing it as a good example of a smaller cap, good-quality company with a defensive repeatable business. Its UK operations have been weak, but North America is now its largest market and is growing at 10–15% pa; Tillett suggests that this business alone could justify the valuation of the whole company. He added Homeserve to BUT's portfolio in late 2021 and its board has recently recommended a £12 per share takeover bid from Canada-based Brookfield Asset Management. This is a 95% premium to Homeserve's year-to-date low share price point in early February 2022.

Performance: Navigating a volatile stock market

Exhibit 5: Five-year discrete performance data

12 months ending	Share price (%)	NAV* (%)	Benchmark** (%)	CBOE UK All Companies (%)	MSCI All World ex-UK (%)
31/05/18	15.7	10.1	8.6	6.6	9.3
31/05/19	(0.1)	1.5	2.7	(3.4)	5.2
31/05/20	3.2	3.7	2.7	(12.0)	9.2
31/05/21	29.6	27.1	24.2	23.4	24.1
31/05/22	4.0	7.7	6.5	8.5	5.2

Source: Refinitiv. Note: All % on a total return basis in pounds sterling. *NAV with debt at market value.

Exhibit 6: Share price and NAV total return performance, relative to indices (%)

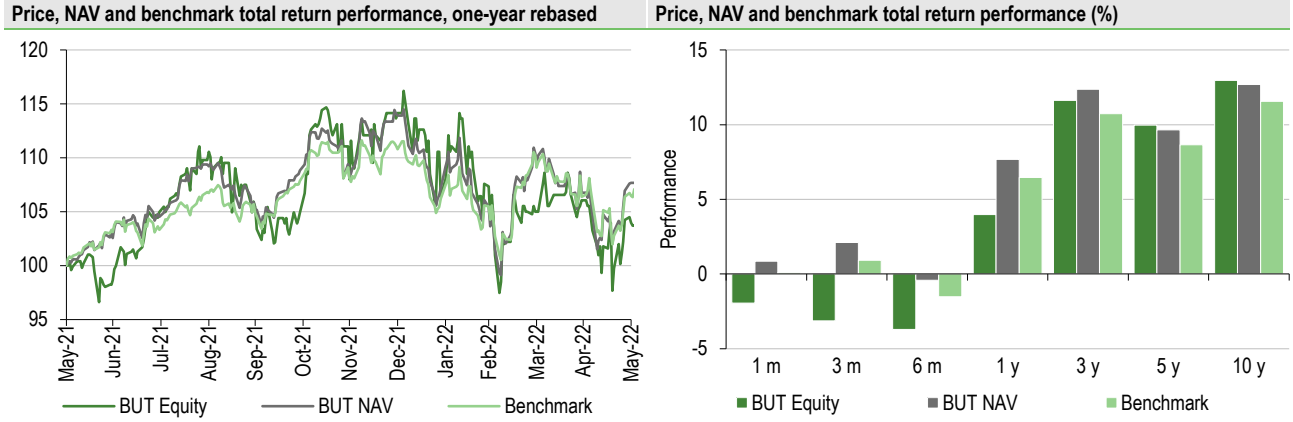
	One month	Three months	Six months	One year	Three years	Five years	10 years
Price relative to benchmark	(2.0)	(4.0)	(2.2)	(2.3)	2.4	6.2	13.4
NAV relative to benchmark	0.8	1.2	1.1	1.1	4.5	4.7	10.7
Price relative to CBOE UK All Companies	(2.7)	(5.4)	(9.9)	(4.1)	18.1	32.7	55.5
NAV relative to CBOE UK All Companies	0.0	(0.2)	(6.8)	(0.7)	20.6	30.8	51.9
Price relative to MSCI All World ex-UK	(1.7)	(3.3)	1.6	(1.2)	(2.5)	(1.9)	(3.9)
NAV relative to MSCI All World ex-UK	1.1	1.9	5.0	2.3	(0.5)	(3.3)	(6.1)

Source: Refinitiv, Edison Investment Research. Note: Data to end-May 2022. Geometric calculation.

Exhibit 6 shows BUT's relative performance, its NAV is ahead of the benchmark over all periods shown, while its share price has outperformed over the last three, five and 10 years. There is also a

notable outperformance versus the broad UK market over the last three, five and 10 years, illustrating the potential benefits of considering stocks that are listed overseas. Tillett is very encouraged by BUT's performance in a tricky market. He highlights that in the 12 months to end-April 2022, the top four best active contributors to the trust's performance were all healthcare stocks: UnitedHealth Group (+117bp); Novo Nordisk (+102bp); AbbVie (+80bp) and Roche Holdings (+51bp). On the negative side the three worst active contributors were Adidas (-105bp) and not holding Apple (-65bp) and AstraZeneca (-52bp).

Exhibit 7: Investment trust performance to 31 May 2022



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

Exhibit 8: NAV performance versus benchmark over five years

Source: Refinitiv, Edison Investment Research

Peer group comparison

There are 17 funds in the AIC Global sector, with the peers following a variety of investment mandates. BUT can be categorised as one of the 'core' funds in the group given its balanced approach of aiming to generate both capital and income growth, straightforward equity portfolio and no exposure to unlisted companies. The trust's relative performance continues to improve with its NAV total returns now ranking a very creditable second over the past 12 months, fourth over the last three years, seventh over five years and ninth (out of 16 funds) over the last decade. BUT's returns are above the peer group averages over the last one, three and five years.

There has been relatively weak performance over the last year at some of BUT's peers with a growth mandate such as Manchester and London Investment Trust, Monks Investment Trust and Scottish Mortgage Investment Trust, which highlights the different approaches within the peer group, that can lead to different results. BUT's proposition is a more stable, 'all-weather fund' that aims to add value across varied market cycles. The manager has a flexible, 'lower-risk' approach and the backing of a well-resourced investment team, and some investors favour BUT's high-

conviction, more concentrated portfolio rather than those of its more diversified 'core' peers such as Bankers Investment Trust, F&C Investment Trust and Witan Investment Trust.

BUT's discount is currently wider than the peer-group average, which one may consider surprising given the trust's improving performance record and balanced investment approach. It has a competitive ongoing charge and a below-average level of gearing. BUT's 2.1% dividend yield is 30bp lower than the sector average.

Exhibit 9: AIC Global sector at 10 June 2022*

% unless stated	Market cap £m	NAV TR 1 year	NAV TR 3 year	NAV TR 5 year	NAV TR 10 year	Discount (cum-fair)	Ongoing charge	Perf. fee	Net gearing	Dividend yield
Brunner Investment Trust	423.1	2.8	33.4	47.6	187.1	(10.6)	0.6	No	107	2.1
Alliance Trust	2,818.2	(2.1)	30.4	45.8	198.2	(5.1)	0.6	No	106	2.5
AVI Global Trust	938.2	0.8	35.8	49.4	184.9	(11.1)	0.8	No	100	1.8
Bankers Investment Trust	1,309.8	(2.8)	26.0	44.0	209.4	(6.8)	0.5	No	108	2.2
Blue Planet Investment Trust	6.2	(57.9)	(66.1)	(66.5)		(6.9)	4.3	No	146	4.2
F&C Investment Trust	4,216.3	1.1	33.4	51.8	224.9	(11.2)	0.5	No	107	1.6
Global Opportunities Trust	84.2	11.4	16.9	18.0	150.7	(16.2)	1.0	No	100	1.7
JPMorgan Elect Managed Growth	260.8	(4.5)	24.4	40.4	202.7	(1.4)	0.5	No	100	1.8
Keystone Positive Change Inv	120.0	(27.1)	(35.3)	(36.7)	21.3	(10.4)	0.5	No	111	5.8
Lindsell Train Investment Trust	218.0	(11.8)	15.2	83.7	459.3	3.0	0.8	Yes	100	4.6
Manchester & London Inv Trust	147.4	(24.8)	1.0	25.2	92.6	(21.0)	0.8	Yes	100	3.8
Martin Currie Global Portfolio	256.2	(15.8)	17.2	42.3	182.5	(2.1)	0.7	No	111	1.4
Mid Wynd International Inv Trust	476.6	(1.6)	38.6	67.7	254.2	2.2	0.6	No	100	1.0
Monks Investment Trust	2,122.0	(21.4)	23.5	48.8	198.2	(9.6)	0.4	No	108	0.2
Scottish Investment Trust	547.9	1.7	8.5	10.5	116.2	(3.5)	0.6	No	102	3.1
Scottish Mortgage Inv Trust	10,753.9	(33.3)	72.4	116.3	532.6	(11.9)	0.3	No	117	0.5
Witan Investment Trust	1,505.0	(7.7)	16.6	24.9	185.5	(9.5)	0.7	Yes	113	2.7
Average (17 funds)	**1,541.4**	**(11.4)**	**17.2**	**36.1**	**212.5**	**(7.8)**	**0.8**		**108**	**2.4**
BUT rank in sector	**10**	**2**	**4**	**7**	**9**	**12**	**10**		**8**	**9**

Source: Morningstar, Edison Investment Research. Note: *Performance to 9 June 2022 based on ex-par NAV. TR = total return. Net gearing is total assets less cash and equivalents as a percentage of net assets.

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