Witan

Highly active multi-manager approach offering a 'one-stop shop' for capital appreciation and income...

Update
03 December 2019

Summary

Witan is a self-managed investment trust which aims to achieve growth in capital and income over the long term, through a portfolio of global equities.

The team follow a highly active multi-manager approach, using a range of third-party managers who run concentrated portfolios of 15 to 60 stocks. Currently there are ten managers in the portfolio, with allocation sizes and mandates being controlled by the board and executive team, led by Andrew Bell. Alongside this, the executive team are directly responsible for up to 12.5% of the portfolio, investing in specialist collective funds and smaller managers that could be larger constituents in the future.

Since adopting the multi-manager approach in 2004, the trust has performed strongly relative to peers and the benchmark. This has also been seen over the short term, although the current exposure to the UK and low exposure to FAANG stocks have been a slight headwind in the short term on a relative basis.

Alongside capital appreciation, the trust offers investors a strong income stream. The trust has an enviable track record of 44 years of dividend increases, and over the past five years the trust has delivered triple the dividend growth of the average peer in the sector.

Over the past few years, the trust has traded on a narrow discount to NAV. The current discount of 3.8% is a little wider than in recent years, and the company is repurchasing shares on a regular basis.

Analyst's View

Witan offers investors an actively managed equity global portfolio which aims to generate both capital appreciation and income. Importantly, the way the portfolio is put together means that there is very little single-manager risk, making it an excellent 'fire and forget' trust for global exposure with little need for maintenance on the part of the investor who holds it.

The trust boasts a strong long-term track record, and the executive team have a proven ability to identify strong managers for the trust's allocations. In addition, the executive team have also added considerable value through the direct holdings portfolio over time.

Over ten years to the end of August 2019, Witan has achieved its goal in outperforming the returns of its composite benchmark. The income the trust offers is also not to be overlooked: Witan has raised the dividend significantly faster than the rate of inflation.

As a result, the trust has the fourth-highest yield in the global sector (2.3%), and one of the most impressive dividend growth records in the investment trust sphere. The company has increased its dividends for 44 consecutive years, and

Key Information:

As at	19/11/19
Price (p)	219.5
Discount (%)	-3.8
OCF (%)	0.79
Yield (%)	2.2
Gearing (%)	13
Ticker	WTAN
Turnover Ratio (%)	41.5
Shares (£)	866,872,377
Market cap (£)	1,902,874,863

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at a compound annual rate of 10.3% over the past five years, this is triple the peer group average. The most recent dividend is covered 1.5x by revenue reserves, giving investors confidence that this already impressive track record of dividend growth should be able to continue going forward.

Analyst's View

BULL	BEAR
A well-defined and simple-to-understand investment approach means that investors can benefit from a diversified array of concentrated portfolios	As a highly active global trust Witan may lack appeal for investors who want to do their own asset allocation
Since the change in strategy in 2004, the trust has delivered strong returns	Due to poor performance in Q4, the trust was unable to outperform the benchmark in 2018
A reliable dividend, progressively growing for the past 44 years	

Portfolio

Witan follows a highly active 'manager of managers' approach, using a range of third-party managers who hold concentrated portfolios of their best ideas. This approach means that shareholders can benefit from active management with relatively concentrated portfolios, but with little key-man or manager risk.

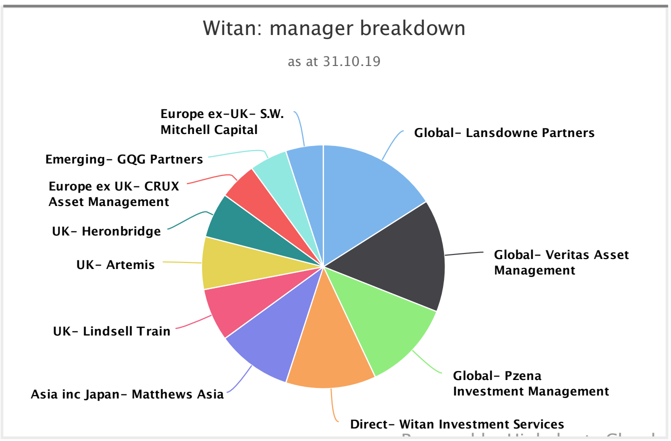
The general activities of the managers are overseen by the executive team, led by Andrew Bell, which sets the specific mandates for the formation of the portfolio. This means that the executive team vary the combination of different investment approaches and geographical exposures, although the board retains ultimate responsibility and the underlying managers ultimately choose their portfolio holdings. The majority of the managers selected are flexible in their approach to portfolio construction, varying between 'value' or 'growth' stocks depending on the market environment and opportunities available to them. Whilst some of the managers might concentrate on one particular style, the range of managers that the team are interested in normally sits between 'opportunistic value' (special situations) and 'growth at a reasonable price'. This tends to produce a portfolio which is fairly neutral on the value–growth spectrum.

Witan's stable is likely to consist of between eight to 12 investment managers at any given time, and the team look to identify those that have the capabilities and track record to outperform their relevant benchmarks. Each manager runs a highly concentrated portfolio, on average around 35 stocks each, with investment decisions being made based on fundamental drivers, as opposed to short-term trends. Alongside this, the managers need to exhibit talented and accountable leadership, high standards of corporate governance (as we discuss in the ESG tab), and generally long-term outlooks. The executive team also takes a long-term view in its allocations. Although monitored closely, no changes have been made to the underlying managers over 2018 or 2019, with the latest additions being the two European managers in October 2017.

Alongside the external managers, up to 12.5% of Witan's portfolio may be invested directly by Witan's executive team. This is a key aspect of differentiating the trust from other multi-manager funds and trusts, and as 2018 showed, can be a key area of returns for Witan. As we discuss in the management section, the team have lengthy experience and can invest up to 10% of the portfolio in specialist collective funds and up to 2.5% in smaller mandates with third-party managers who are newly established or running niche investment strategies. This allows the managers to get to know new managers better and decide if they might be 'one for the future'.

A recent addition to this area of the portfolio is the GMO Climate Change Fund, which looks to take advantage of some of the opportunities climate change will throw up, including mitigating impacts and adapting to outcomes. This investment has been made for its prospective investment returns and the opportunity to profit from addressing climate change. The team believe that a disciplined approach, such as that adopted by GMO, is likely to help avoid some of the hype which accompanies this evolving story. The executive team have also recently invested in the Schroder Real Estate Investment Trust, in the wake of recent uncertainty surrounding Brexit and the UK commercial property sector.

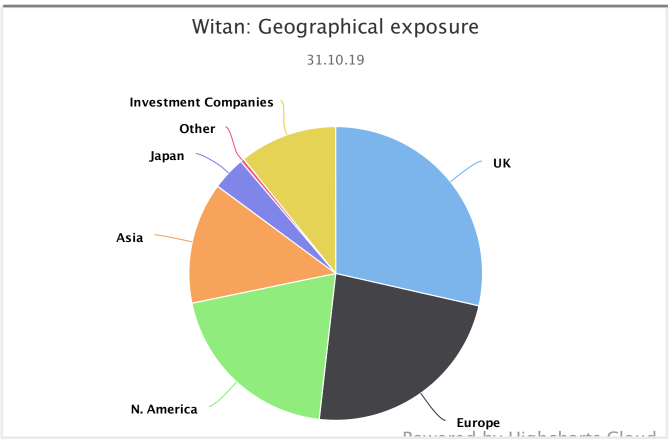
Fig.1: Manager Breakdown As % Of Nav



Source: Witan

As can be seen below, the UK represents the portfolio's largest exposure (28.6%), followed by Europe (23.3%) and North America (20%). The diversity across regions is a key part of the risk management approach and enables the trust to avoid undue concentration of risks arising from local economic and political situations.

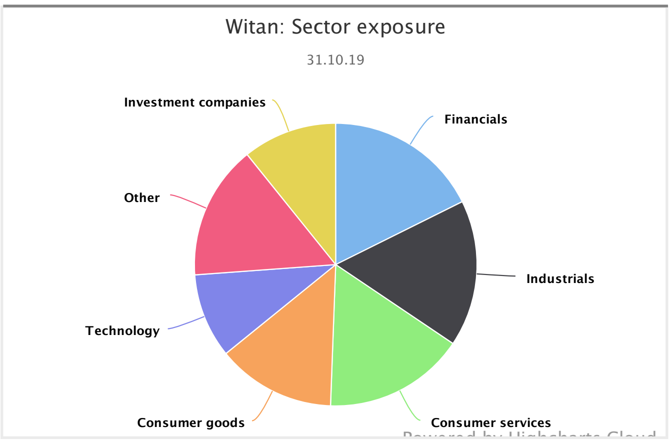
Fig.2: Regional Exposure



Source: Witan

The sector exposure is equally well diversified. As can be seen below, financials (17.7%), industrials (16.8%) and consumer services (16.2%) make up the largest weightings. With this said, it is important to reiterate that the fund managers within the portfolio are active stock pickers, and the biases towards certain industries are the result of finding stock-specific opportunities rather than taking macro/sector bets.

Fig.3: Sector Exposure



Source: Witan

Gearing

Witan employs structural gearing to enhance returns for shareholders, worth around 10% of NAV. It is the board's long-standing policy not to allow gearing to rise to more than 20%, other than temporarily in exceptional circumstances.

As at 31st October 2019, gearing was 11%. However, over 2019 gearing has been slightly higher than this, averaging 12.1% of NAV, and this has positively contributed to performance over the first half of the year. The company has both fixed and flexible rate borrowings. We detail the fixed rate borrowings in the table below, equating to a total of £170m (and 8.6% of NAV).

Fixed Rate Borrowings

BORROWING	AMOUNT
Secured Bonds - 2025 6.125%	£64m
Secured Notes - 2035 3.29%	£21m
Secured Notes - 2045 3.47%	£54m
Secured Notes - 2054 2.74%	£30m

Source: Witan, Annual report

In addition to the above, the company has agreed to issue £50m in new debt on 1 October 2019, at a record low interest rate for the investment trust sector of 2.39%. As such, the average interest rate on fixed debt has fallen to 3.8%. We note that once the 2025 £64m debt expires, the blended interest rate will drop below 3% (assuming no further changes to the debt structure).

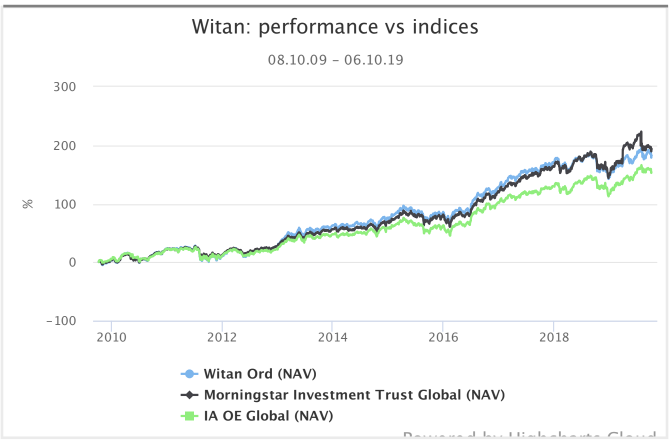
In addition to its fixed rate borrowings, the company also has a £125m short-term multi-currency facility, which it can use on a much more flexible basis.

Performance

Over the ten years to the end of August 2019, Witan has achieved its goal of outperforming the returns of its composite benchmark and raising the dividend significantly faster than the rate of inflation.

Witan uses a composite benchmark because the board states that long-term returns are likely to stem from changing opportunities as economies evolve, as opposed to relative market capitalisation. This evolution was recently illustrated (in September 2019), when the

Fig.4: Ten-Year Nav Performance

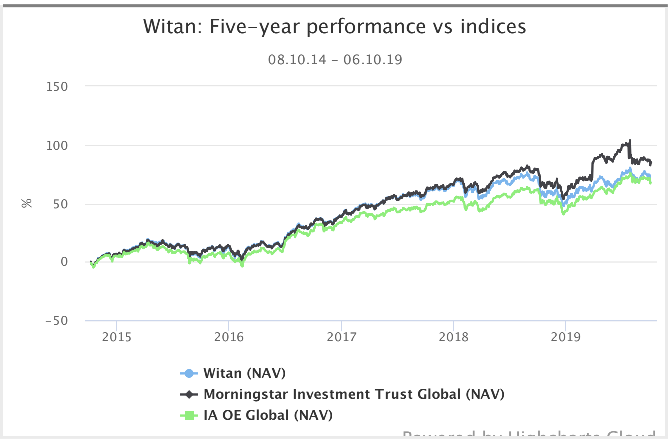


Source: Morningstar

company announced its intention to change the benchmark as of the start of January 2020. Currently, the benchmark consists of 30% UK, 25% North America, 20% Europe ex-UK, 20% Asia Pacific and 5% Emerging Markets. As of 2020, the new benchmark will be 15% UK (FTSE All-Share) and 85% global (FTSE All-World). The effective UK component will be c.19% when accounting for the weight the UK represents within the global index. As Witan has stated, the global component represents a simplification from the current combination of four regional indices into one index, which they believe will be easier for investors to monitor. There is no requirement for the portfolio to mirror the benchmark and any change in asset allocation will be driven by its prospects relative to opportunities globally.

Over the five years to the end of August 2019, Witan has delivered an NAV total return of 66.7%, compared with the benchmark's 59.6% return over the same period, representing another period of good outperformance. Witan has historically been structurally underweight to the US versus its peers. This is the main reason why the trust has underperformed the AIC Global peer group, which has delivered NAV returns of 82.4% over the same period, and marginally underperformed the IA peer group, which has delivered 67.6%.

Fig.5: Five-Year Nav Performance



Source: Morningstar

As an actively managed portfolio, it is likely that the trust will have periods of underperformance as well as outperformance. However, in the past five years Witan has only had one year in which it has materially underperformed its benchmark – a very creditable result – largely thanks to the strong long-term performance from the stable of managers (shown in the table below).

Throughout 2014 and 2015 equities oscillated around the unchanged mark for most of the period. As such, the underlying managers outperformed through active investment selection in response to the opportunities created by the market's volatility. The following year (2016) saw the trust perform in line with the benchmark during 12 months that saw an abundance of political risk, which the managers responded to by spreading the risk across the portfolio. 2017 saw a number of changes made to the underlying managers in the portfolio, and the trust returned to its winning ways by outperforming the benchmark by 4%. Five of the seven managers outperformed their benchmarks, chiefly Lindsell Train (21.8% total return), Lansdowne (19.1%) and Veritas (17.1%), and the average gearing of 10.5% further amplified returns.

Breakdown Of Managers' Long-Term Performance

COMPANY	% IF WITAN'S AUM AT 30/06/19	PERFORMANCE SINCE APPOINTMENT (% PER ANNUM)	BENCHMARK PERFORMANCE SINCE APPOINTMENT (% PER ANNUM)
Artemis	7.1	8.4	6.1
Heronbridge	6.3	9.1	7.1
Lindsell Train	8.4	16.2	8.6
Lansdowne Partners	14.8	17.1	13.8
Pzena	12.4	10.1	12.6
Veritas	15.1	14	11.6
CRUX	4.7	2.6	2.9
S.W. Mitchell	4.7	-0.4	2.9
Matthews Asia	10.3	9.5	8.7
GQG	5.1	11	6.9
Witan Direct Holdings	11.1	10.9	9.1

Source: Witan

Fig.6: Calendar-Year Nav Returns

Source: Morningstar

During what was a challenging 2018, Witan's returns were positive for most of the year – in fact, the portfolio itself actually outperformed the benchmark overall. However, the trust's costs and gearing meant that NAV performance lagged the benchmark by 2.1%. Q4 was a particularly harsh period for the portfolio, hampering what would otherwise have been a strong year.

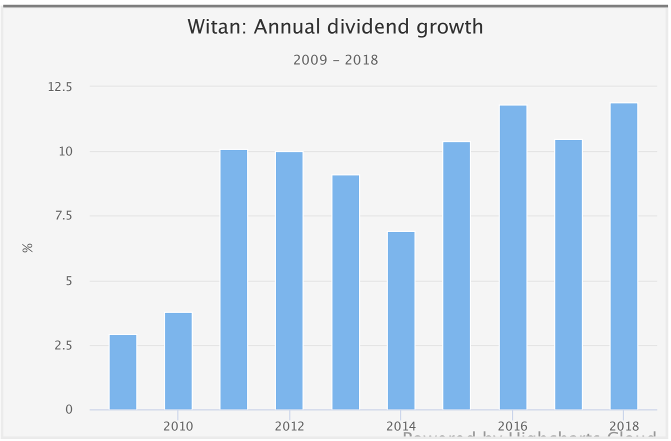
Over the first half of 2019 Witan has delivered NAV total returns of 13.5%, marginally trailing the composite benchmark, which delivered 14.9%. The IA and AIC peers returned 16.9% and 24% respectively. This underperformance was largely due to the underlying managers reducing the overall exposure to FAANG stocks and bond proxies (e.g. consumer staples, branded goods, etc.), both of which have contributed a huge portion of returns to equity markets. Over the period, six of the ten external managers outperformed their relative benchmarks, with S.W. Mitchell and Lindsell Train being the standout performers, both outperforming their respective benchmarks by more than 6%. Witan's direct investments ('Witan Direct Holdings' in the earlier table breaking down the managers' long-term performance) lagged the benchmark, during a period in which they had multiple headwinds. Electra and Syncona are two holdings the executive team highlight, and which, despite stable NAV performances, saw their share prices lag. Witan has made further absolute progress over the second half of 2019, making up the shortfall between its NAV and the benchmark.

Dividend

At the current share price, Witan yields 2.3%. It is the board's policy each year to grow the dividend ahead of inflation. Over the past five years Witan's dividend per share has increased by 10.3% on an annualised basis, more than triple the weighted average for the global sector and considerably more than the 12-month CPI annual rate of 1.7%. The dividend is paid quarterly (in March, June, September and December).

The 2018 dividend of 4.7p was 11.9% greater than the 4.2p paid in 2017, bringing the number of consecutive annual dividend increases to 44. As of the most recent annual report (December 2018), the trust has revenue reserves of c.£65m, which is the equivalent of 1.5x the annual dividend. So far in the current financial year, the trust has announced three dividends, equating to 3.525p per share, up from 3.15p at this stage in 2018. The board has stated it expects a further year of growth in 2019 (in the absence of unforeseen circumstances).

Fig.7: Dividends



Source: Witan

Management

Witan is internally managed by a team headed by Andrew Bell, who became CEO in 2010 and sits on the board of directors. There are multiple benefits to being self-managed, including the alignment of interests: there is no question of an investment decision being influenced by what is better for a management company which may be investing in the same or similar assets elsewhere. Other benefits are that the board is largely independent and employees are wholly focused on Witan's portfolio, which is unlike other investment houses where analysts could be working for multiple clients.

Witan has a multi-manager approach, using a range of third-party managers investing in concentrated portfolios. Changes are expected to be relatively infrequent, and as of October 2019 there are ten managers.

Managers are formally reviewed at least once a year, but are reviewed more frequently than that by the executive team. We understand the intention is that managers are unlikely to be replaced due to short-term performance relative to their benchmarks; rather, this is more likely to happen in cases of unexplainable performance, investment mandate changes or changes at the management company. The breadth of experience represented by Witan's ten board members also facilitates this process, with diverse skills being brought to the table from the likes of Ben Rogoff (current Polar Capital Technology fund manager), Paul Yates (ex-CEO of UBS Global Asset Management UK) and new appointee Gabrielle Boyle (senior fund manager and head of research at Troy Asset Management).

Witan is able to use its large size (total assets of £2.154bn) to negotiate attractive fees with the managers it has selected. Up to 12.5% of the portfolio may be invested directly by the executive team, of which up to 10% may be invested in specialist collective funds. These funds may represent undervalued asset categories or funds viewed as longer-term generators of superior returns. Up to 2.5% may be allocated in smaller mandates to third-party managers with strong potential to add value, which the team view as possible managers for the future.

Investment Managers

MANDATE	MANAGERS
UK	Artemis, Heronbridge, Lindsell Train
Global	Lansdowne, Pzena, Veritas
Europe	CRUX, S.W. Mitchell
Asia/Emerging	Matthews, GQG

Source: Witan, as at 31 October 2019

Artemis

The fund from Artemis is run by Derek Stuart, manager of Artemis's UK Special Situations strategy. Through recovery/special situations-style investing, the manager looks to achieve superior long-term growth by looking for unrecognised growth potential in companies. The strategy has a tilt towards smaller and medium-sized companies, especially those that are out of favour and need new management or refinancing, or that are suffering from investor indifference. The portfolio typically has fewer than 50 holdings.

Heronbridge

The portfolio from Heronbridge is run by two managers, Benoit Bouchaud and Bevis Comer, investing solely in UK equities. Their style is described as 'intrinsic value growth', searching for good companies at fair prices. The result is a contrarian and high-conviction portfolio based on their desired investment qualities, as opposed to a stock's size in a particular market index. The managers aim to outperform both the FTSE All-Share and inflation over time.

Lindsell Train

Lindsell Train, run by Nick Train, is a high-conviction portfolio of around 15 stocks which he likes to describe as "rare and beautiful assets". The manager has a single-minded focus on investment excellence, guided by four beliefs: that investors undervalue durable, cash-generative business franchises; that concentration can reduce risk; that transaction costs are a 'tax' on returns; and that dividends matter even more than you think. The result is a bias towards three sectors: Consumer Brands, Media & Digital Technology and Financial Services. Alongside a unique investment perspective, the utilisation of a long term buy-and-hold strategy is synonymous with Lindsell Train, highlighted by a portfolio turnover rate of less than 10% per annum.

Lansdowne

Although Lansdowne is well known as a hedge fund manager, its long-only Developed Markets strategy, managed by Peter Davies and Jonathon Regis, has gained a large amount of attention since launching in 2012. The managers have a high conviction and unconstrained approach, with the portfolio holding around 20 stocks. Fundamental and well-detailed research is at the core of the investment process, and holdings are subject to detailed company-specific analysis, allied with an investigation of global thematic developments.

Pzena

Pzena is committed to finding deep value opportunities. The managers, John Goetz and Caroline Cai, search for high-quality companies at low valuations, concentrating entirely on companies that are underachieving relative to their demonstrated historical earnings power. This type of value investing means finding companies before the stock price reflects signs of business improvement, and relies on investors avoiding businesses that are experiencing problems. The Global Value Portfolio contains close to 65 stocks across the world.

Veritas

The aim of the company is to generate excellent real returns and minimise the risk of permanent capital loss. The manager, Andy Headley, has a 'fundamental value approach', putting companies through a highly selective and rigorous investment process. The team are extremely disciplined when it comes to valuations in 'quality' mid- to large capitalisation companies, and potential investments are analysed on an absolute basis rather than relative to a benchmark. Typically, the portfolio will be comprised of 30 stocks or fewer, with a clear focus on a handful of investment themes.

CRUX

Established in 2014, CRUX is a UK-based fund management company founded by Richard Pease. Richard, supported by long-term colleague James Milne, has constructed a more concentrated version of their European Special Situations fund for Witan's fund. The manager has a bottom-up and truly active approach to stock picking, centred around finding companies which are high quality, have proven management, are sensibly capitalised and trade at a discount to CRUX's assessment of intrinsic value. Whilst the portfolio of 40 to 50 stocks contains some large- and small-cap businesses, CRUX tends to concentrate on opportunities in the medium-sized range.

S.W. Mitchell

S.W. Mitchell Capital is a specialist European equities investment boutique. Freedom of thought, detailed research and insulation from market distractions are at the heart of the company, which tries to avoid some of the pitfalls of larger investment firms. The portfolio, run by Stuart Mitchell, takes an alternative view on value investing, looking for misunderstood and hence undervalued quality growth businesses. The manager utilises a bottom-up approach, with management engagement at the heart of the investment process. The portfolio is completely unconstrained and benchmark agnostic, and it is also high conviction as it contains only 25 stocks.

Matthews

Matthews is an Asia-only investment specialist based in the USA. The largest of its kind, the 46-person investment team travel extensively across Asia, uncovering investment opportunities. Matthews has an active, long-term investment approach and uses bottom-up, stock-specific research to build a portfolio of companies with strong business models and quality management at reasonable valuations. The Asia Dividend strategy, managed by Yu Zhang, pays particular attention to the payment of dividends and sees them as an important signal for a company's capital allocation, business quality and corporate governance.

GQG

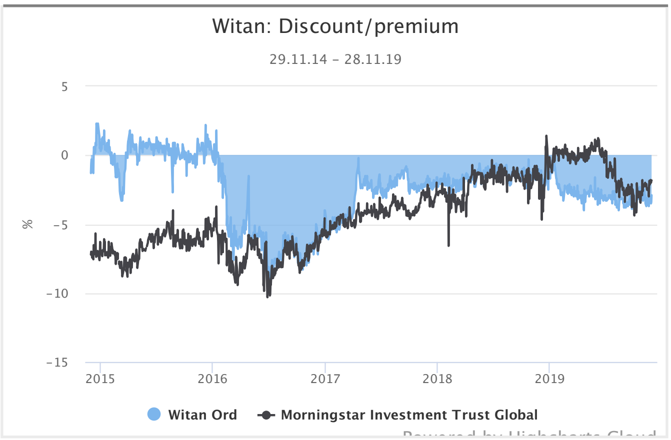
GQG Partners' Emerging Markets Equity strategy aims to participate in the growth of emerging market economies, while mitigating some of the risks through diversifying across countries and stocks within the company's investment universe. Rajiv Jain is at the helm of the portfolio, employing a fundamentals-driven investment process to find high-quality, large-cap companies with attractively priced future growth prospects.

Discount

Over the last five years, Witan has tended to trade at a small discount to NAV. As can be seen in the discount graph below, the only exception was in 2016 following the placing of shares from the large shareholder Aviva, but this was a technical issue rather than one related to performance. Currently the trust trades at a discount of 3.8%, marginally wider than the one-year average of 2.8% and the sector average of 2.2%.

The board places great emphasis on the importance of the liquidity of the shares. As such, it closely watches for discount-related issues and over the past few years has made significant use of share buybacks in order to meet its objective that the shares should trade on a sustainable low discount or premium to NAV. Over the first half of the year, Witan has bought back 1.2% of the shares into treasury. This goal of ensuring the best liquidity for shareholders was further illustrated in May 2019, where there was a five-for-one split of the shares which was done to help broaden the shareholder base and increase liquidity.

Fig.7: Discount



Source: Morningstar

Charges

In 2018 the ongoing charges excluding performance fees were 0.75%, in line with the peer group average of 0.71%. However, we understand that two of the managers in the portfolio (one of which significantly outperformed over 2018) charge a performance fee, so including these costs the OCF rises to 0.83%.

Witan has a KID RIY of 1.9% (including interest and transaction costs), relative to the sector average of 1.34%. It is worth noting that calculation methodologies can vary.

ESG

Witan does not currently have an ESG policy; however, we understand that this is something that the board has in the pipeline. Governance continues to be a key part of the process for assessing managers, as is a long-term focus on the managers themselves. All the underlying external managers have ESG policies, eight of whom are also currently signatories of the UNPRI.

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