

Listed Investment Companies (LICs)

SECTOR REPORT

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Monthly LIC update – top picks

- The following report contains a LIC sector update and performance review of our coverage list for the month of January 2016.
- **Top picks:** Our top picks refer to preferred exposures within each sector based on numerous quantitative and qualitative factors. However, they should not be treated as official stock recommendations but merely as a guide to where we would apportion funds at this particular point in time.
- **Large capitalisation:** Across traditional large cap LICs, trading volumes for FY16 year-to-date (YTD) have been, on average, 12.3% and 15.5% lower than the prior two respective previous corresponding periods (pcp). In our view, volumes have been influenced by two contributing factors: 1) market volatility in FY16, resulting in elevated premium trading levels to NTA; and 2) the increased number of Self-Managed Superfunds (SMSFs) on registries with SMSFs typically holding LICs with a longer term view. Whilst we advocate more favourable conditions for an entry point (i.e. a reversion back to more normalised historical trading levels), in our view, this reversion will be primarily driven by underlying NTA movements. Holding over 34.0% of its portfolio in banks, Milton Corporation (MLT) is trading at an estimated 3.2% premium to NTA. This falls broadly in line with its one year average (2.4%) and is currently a top pick. Diversified United Investment (DUI) remains a value proposition currently trading at an estimated 4.3% discount to NTA.
- **Small capitalisation:** Perpetual Equity Investment Company (PIC) and Future Generation Fund (FGX) are our current top picks. PIC, with a dual objective including providing a growing stream of fully franked dividends, announced its maiden interim dividend (0.8 cents). Holding a concentrated (~20 securities), mid-cap focused portfolio with the capacity for a global allocation (max: 25%), we estimate PIC to be trading at a 4.6% discount to NTA. FGX also announced its maiden interim dividend (full year dividend yield of 3.5%) as well as announcing an expected FY16 donation to charities of \$2.2 million, exceeding the \$1.6m contribution from nine months to FY15. FGX is estimated to be trading in line with its NTA. Elsewhere, for investors seeking exposure within the microcap space, Contango Microcap (CTN) is trading at an attractive estimated discount to NTA of 14.0%.
- **International:** Underlying assets continue to be impacted by global market movements and investor sentiment remains low. On average, YTD TSR decreased 8.3% compared to TSR of the MSCI World Index (AUD) of -5.1%. YTD, Global Value Fund (GVF) has outperformed the market and is a top pick within this space for the following reasons: 1) The underlying portfolio is actively hedged to mitigate exposure; 2) Asset allocation within the portfolio is diversified across a number of asset classes (i.e. fixed interest represents 31% of the portfolio at 31 January 2016) and; 3) GVF has ~50 million options outstanding with a 17 March 2016 expiry date. Post the expiry date of these options, GVF will have no further dilution impact on its NTA and in our view, should move broadly in line with the NTA. PM Capital Global Opportunities Fund (PGF) remains a top value pick, currently trading at an estimated 14.7% discount to NTA.
- **Specialty:** Acorn Capital (ACQ) remains a top pick within the specialty space, currently trading at an estimated 19.2% discount to NTA. Elsewhere, for investors seeking diversification outside of equities, Blue Sky Alternative Access Fund (BAF), with its largest holding (30.8%) invested in a Water Fund is trading at an estimated 8.9% discount to NTA.
- Please refer to page 2 for an updated table on current dividend yields, January NTAs and our current NTA estimates for selected LICs ahead of the upcoming NTA releases for February.

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Disclosure

The author owns no shares in any of the mentioned companies.

Sector snapshot

BAILLIEU HOLST - EQUITY RESEARCH Listed Investment Companies Coverage by Sector

Figures as at: 22 February 2016

Large Capitalisation	Code	Share Price	Market Cap. (\$m)	Dividend (cents)	Dividend Yield	Grossed Up Yield	TSR since Feb 1	Current Est. NTA	Current Estimated Disc/Prem	January NTA	January Disc/Prem	3 Mth Ave Disc/Prem	1 Yr Ave Disc/Prem	3 Yr Ave Disc/Prem
Australian Foundat.	AFI	5.60	6325.8	23.0	4.1%	5.9%	-1.4%	5.25	6.7%	5.31	8.9%	6.2%	3.8%	3.9%
Argo Investments	ARG	7.39	5002.7	29.5	4.0%	5.7%	-0.3%	6.75	9.5%	6.90	9.6%	8.7%	5.8%	2.5%
Australian United In	AUI	7.18	884.8	33.4	4.7%	6.7%	-1.4%	7.35	-2.4%	7.32	-0.5%	-3.7%	-5.1%	-6.1%
BKI Investment Ltd	BKI	1.58	910.9	7.2	4.6%	6.5%	-4.2%	1.48	6.1%	1.53	9.8%	6.7%	2.6%	-0.6%
Djerriwarrh	DJW	3.99	872.2	26.0	6.5%	9.3%	-5.0%	2.90	37.5%	2.89	45.3%	37.9%	31.4%	25.6%
Diversified United	DUI	3.24	670.4	14.0	4.3%	6.2%	-1.5%	3.38	-4.2%	3.38	-2.7%	-4.7%	-5.3%	-7.0%
Milton Corporation	MLT	4.20	2725.8	18.8	4.5%	6.4%	-4.9%	4.07	3.2%	4.24	6.4%	3.1%	2.4%	0.3%

Small Capitalisation	Code	Share Price	Market Cap. (\$m)	Dividend (cents)	Dividend Yield	Grossed Up Yield	TSR since Feb 1	Current Est. NTA	Current Estimated Disc/Prem	January NTA	January Disc/Prem	3 Mth Ave Disc/Prem	1 Yr Ave Disc/Prem	3 Yr Ave Disc/Prem
Australian Leaders	ALF	1.50	401.4	10.0	6.7%	9.6%	2.4%	n/a	n/a	1.36	7.4%	2.8%	1.0%	7.0%
Aberdeen Leaders	ALR	1.00	61.3	5.0	5.0%	7.2%	-0.5%	1.11	-10.0%	1.09	-8.3%	-9.5%	-8.8%	1.7%
AMCIL Limited	AMH	0.87	212.8	4.0	4.6%	6.6%	1.2%	0.90	-3.6%	0.89	-3.9%	-4.7%	-4.1%	-2.2%
Cadence Capital	CDM	1.44	386.5	11.0	7.6%	10.9%	-4.0%	1.23	17.3%	1.27	17.8%	15.6%	4.4%	3.2%
Contango Inc Gen Ltd	CIE	0.95	67.9	n/a	n/a	n/a	-4.9%	0.96	-0.6%	1.00	2.6%	n/a	n/a	n/a
Carlton Investments	CIN	31.50	834.0	108.0	3.4%	4.9%	-1.1%	35.68	-11.7%	36.06	-11.7%	-12.0%	-10.7%	-11.8%
Contango Microcap	CTN	0.91	146.6	7.7	8.5%	10.0%	-1.5%	1.06	-14.0%	1.07	-11.5%	-13.6%	-8.4%	-9.7%
Glennon SML Co Ltd	GC1	0.98	21.3	n/a	n/a	n/a	2.1%	1.02	-4.4%	1.03	-6.5%	n/a	n/a	n/a
Future Gen Ltd	FGX	1.15	219.9	2.0	1.7%	2.5%	-0.4%	n/a	n/a	1.15	0.0%	-2.0%	n/a	n/a
Mirrabooka Invest.	MIR	2.54	394.0	17.0	6.7%	9.6%	0.4%	2.26	12.4%	2.28	11.0%	7.1%	9.4%	11.2%
Naos Emerg Opp	NCC	0.95	44.3	6.3	6.6%	9.4%	-2.1%	n/a	n/a	1.08	-10.6%	-8.0%	-9.1%	-10.0%
Ozgrowth Limited	OZG	0.12	43.3	1.5	12.5%	17.9%	6.6%	0.15	-17.9%	0.15	-22.8%	-19.8%	-12.9%	-15.5%
Perpetual Equity Ltd	PIC	0.94	236.1	0.5	0.5%	0.8%	-1.1%	0.99	-4.7%	1.03	-7.6%	-7.0%	n/a	n/a
Qv Equities Limited	QVE	1.00	204.5	1.5	1.5%	2.1%	-1.0%	n/a	n/a	1.05	-4.1%	-3.9%	-1.1%	n/a
Sandon Capital Ltd	SNC	0.84	37.0	5.0	6.0%	8.6%	-1.8%	n/a	n/a	0.97	-11.9%	-12.3%	-8.1%	n/a
Thorney Opp Ltd	TOP	0.53	89.6	0.5	0.9%	1.3%	-0.9%	n/a	n/a	0.56	-4.1%	-2.8%	-8.6%	-3.6%
Whitefield Ltd	WHF	4.17	334.5	17.0	4.1%	5.8%	-1.9%	4.47	-6.8%	4.49	-5.3%	-7.8%	-6.8%	-6.4%
WAM Capital Limited	WAM	2.17	1015.6	14.0	6.5%	9.2%	0.5%	1.90	14.1%	1.92	12.8%	8.8%	7.1%	5.1%
WAM Research Ltd	WAX	1.39	240.1	8.0	5.8%	8.2%	3.0%	1.17	19.2%	1.19	13.5%	9.6%	6.2%	4.6%
Wealth Def Equ Ltd	WDE	0.78	97.4	n/a	n/a	n/a	2.0%	0.88	-11.6%	0.87	-12.9%	-9.5%	n/a	n/a
Westoz Inv Ltd	WIC	0.73	94.4	9.0	12.3%	17.6%	-7.0%	0.86	-15.2%	0.91	-10.4%	-10.2%	-10.0%	-10.4%
Watermark Fund Ltd	WMK	1.04	90.7	4.5	4.3%	6.2%	-1.4%	n/a	n/a	1.07	-1.9%	-8.1%	-10.4%	n/a
8lp Emerg Co Ltd	8EC	0.90	29.8	0.0	0.0%	0.0%	-6.3%	0.93	-3.3%	0.96	-0.2%	n/a	n/a	n/a

International	Code	Share Price	Market Cap. (\$m)	Dividend (cents)	Dividend Yield	Grossed Up Yield	TSR since Feb 1	Current Est. NTA	Current Estimated Disc/Prem	January NTA	January Disc/Prem	3 Mth Ave Disc/Prem	1 Yr Ave Disc/Prem	3 Yr Ave Disc/Prem
Amp Capital China	AGF	0.80	307.1	33.9	42.6%	42.6%	1.3%	1.03	-23.1%	1.33	-41.0%	-25.4%	-23.3%	-21.5%
Argo Global Ltd	ALI	1.73	246.8	n/a	n/a	n/a	-13.8%	1.93	-10.6%	1.93	-11.1%	-9.0%	n/a	n/a
Ellerston Asian	EAI	0.83	99.0	n/a	n/a	n/a	-1.4%	n/a	n/a	0.90	-5.1%	n/a	n/a	n/a
Ellerston Global Inv	EGL	0.97	73.3	1.0	1.0%	1.5%	2.1%	n/a	n/a	1.07	-11.2%	-6.0%	n/a	n/a
Future Gib Invest Co	FGG	1.11	305.7	n/a	n/a	n/a	-4.3%	n/a	n/a	1.04	11.1%	n/a	n/a	n/a
Global Value Fnd Ltd	GVF	1.02	74.4	2.0	2.0%	2.8%	1.0%	n/a	n/a	1.14	-11.6%	-11.2%	-10.3%	n/a
Hunter Hall Global	HHV	1.12	270.3	12.0	10.8%	10.9%	0.9%	1.33	-16.0%	1.30	-15.3%	-11.5%	-11.5%	-12.9%
Magellan Flagship	MFF	1.84	852.1	2.0	1.1%	1.1%	-2.4%	1.92	-4.3%	2.01	-6.2%	-2.8%	-7.9%	-2.9%
Pm Capital Asian Ops	PAF	0.86	47.4	n/a	n/a	n/a	-0.6%	1.02	-15.3%	1.03	-16.1%	-12.3%	-13.4%	n/a
Platinum Asia Ltd	PAI	0.93	272.6	n/a	n/a	n/a	-3.6%	0.90	3.1%	0.92	5.4%	n/a	n/a	n/a
Pm Capital Fund	PGF	0.87	302.2	n/a	n/a	n/a	-5.9%	1.02	-14.7%	1.07	-13.3%	-11.6%	-12.8%	n/a
Platinum Capital Ltd	PMC	1.65	385.9	11.0	6.7%	9.6%	-5.8%	1.47	11.5%	1.51	17.8%	18.2%	11.0%	7.0%
Templeton Global	TGG	1.08	269.6	4.1	3.8%	5.4%	-3.1%	1.29	-16.5%	1.32	-15.5%	-13.3%	-10.2%	-10.2%

Specialist	Code	Share Price	Market Cap. (\$m)	Dividend (cents)	Dividend Yield	Grossed Up Yield	TSR since Feb 1	Current Est. NTA	Current Estimated Disc/Prem	January NTA	January Disc/Prem	3 Mth Ave Disc/Prem	1 Yr Ave Disc/Prem	3 Yr Ave Disc/Prem
Acorn Cap Inv Fund	ACQ	0.80	39.8	n/a	n/a	n/a	-3.6%	0.99	-19.2%	0.97	-14.7%	-15.6%	-17.7%	n/a
Bailador Tech Inv	BTI	1.00	58.3	n/a	n/a	n/a	4.2%	1.26	-20.3%	1.26	-23.5%	-18.4%	-19.0%	n/a
Blue Sky Alt Access	BAF	0.98	125.4	3.00	3.1%	4.4%	-1.5%	1.08	-8.9%	1.08	-7.5%	-5.7%	-19.0%	n/a
Lion Selection Grp	LSX	0.23	24.6	n/a	n/a	n/a	-1.7%	n/a	n/a	0.28	-28.6%	-39.4%	-37.6%	-37.6%

Source: IRESS, Bloomberg, company reports and Baillieu Holst estimates

Recent News

- Reporting season:** Whilst we analyse LICs on an NTA basis, a number of LICs have released 1HY16 earnings with some evident trends. Within the traditional large cap LICs, AFI, ARG, BKI and MLT all increased their respective interim dividends. Australian Leaders Fund (ALF) and Watermark Fund (WMK) employing a respective long/short and market neutral strategy performed strongly with NPAT up 207.0% and 301.4% respectively. Within the small cap space, Wilson Asset Management's WAM and WAX both performed strongly with NPAT up 224.9% and 92.8% respectively. International LICs were cycling tough comps given currency gains in the pcp and this was reflected in NPAT figures with a number of LICs reporting lower figures to that of the pcp.
- Dividend announcements:** A number of LICs have used 1HY16 results as an opportunity to declare maiden interim dividends with Contango Income Generator (CIE), FGX, GVF, PIC, PGF and Wealth Defender Equities (WDE) all announcing interim dividends.
- Options:** Over the prior three years the LIC market has seen the entrance of over 16 new LICs. When LICs typically list on the ASX the pro forma NTA is often slightly lower than the issue price (i.e. if the issue price is \$1.00 then typically the initial NTA will be between \$0.96-\$0.98), this is due to the costs associated with listing on the ASX. In order to counter this issue and appease investor sentiment, included within the offer is often an attached bonus option (i.e. on a 1:1 basis) essentially giving investors (in total) one dollar worth of value. Often LICs will have 12-24 month duration with exercised options having a dilutive impact on the NTA (depending on the size of the issue and performance of the underlying NTA) as well as placing downwards pressure on LIC share prices.
- March:** In March 2016 three LICs, Global Value Fund (GVF), QV Equities (QVE) and Bailador Technology Investments (BTI) have expiring options. The share prices of GVF, QVE and BTI are all trading around the exercise option price (\$1.00) which creates a dilemma for investors as to whether: 1) sell the options; 2) exercise the options or; 3) let the options expire. With the options expiring in March, coupled with share prices trading around the exercise price, the market value of the options is marginal (i.e. QVEO is trading at \$0.001). The dilemma is essentially whether to exercise the option or allow it to expire. The figures below provide a summary of the dilution impact on the NTA at various numbers of options being exercised.

FIG.2: GVF DILUTION ESTIMATES

Estimated No. of Options exercised (Mn)	Estimated NTA	Dilution impact to Jan 2016 Pretax NTA
5	1.13	-0.8%
10	1.12	-1.4%
20	1.11	-2.6%
30	1.10	-3.5%
40	1.09	-4.3%
Fully Diluted NTA	1.08	-4.9%

Source: IRESS, Baillieu Holst estimates

FIG.3: BTI DILUTION ESTIMATES

Estimated No. of Options exercised (Mn)	Estimated NTA	Dilution impact to Jan 2016 Pretax NTA
5	1.23	-1.6%
10	1.22	-3.0%
20	1.19	-5.2%
30	1.17	-6.9%
40	1.15	-8.3%
Fully Diluted NTA	1.13	-10.2%

Source: IRESS, Baillieu Holst estimates

FIG.4: QVE DILUTION ESTIMATES

Estimated No. of Options exercised (Mn)	Estimated NTA	Dilution impact to Jan 2016 Pretax NTA
25	1.05	-0.5%
50	1.04	-1.0%
75	1.04	-1.4%
100	1.04	-1.7%
125	1.03	-1.9%
150	1.03	-2.1%
Fully Diluted NTA	1.03	-2.2%

Source: IRESS, Baillieu Holst estimates

- We advocate that GVF, QVE and BTI investors exercise their options given the following factors: 1) As shown in the previous figures, with the exception of BTI (trading at a ~25% discount) the proximity of the current share price and NTA decrease the dilution impact (assuming full dilution) on the NTA (<5% for GVF and QVE); 2) Options are initially provided to shareholders as compensation for investing at the IPO (where issue prices are often greater than NTAs). Whilst the initial day one trading level of GVF, QVE and BTI was at a premium to NTA, shareholders now have the opportunity to utilise that option at a (assuming full dilution) 5.0%, 2.2% and 10.2% discount to NTA respectively and; 3) given the closed end structure of a LIC, options provide an injection of capital for management without having to undertake a capital raising which can influence investor sentiment and underlying NTAs. We also note that all outstanding GVF options are entitled to the interim dividend of 3.0 cents.

Monthly performance by sector

FIG.5: LARGE CAP TSR

Top Performers			
January Return		Quarterly Return	
Company	TSR (%)	Company	TSR (%)
DJW	0.0%	MLT	5.1%
BKI	-0.3%	DJW	3.6%
MLT	-1.5%	BKI	0.9%

Bottom Performers			
January Return		Quarterly Return	
Company	TSR (%)	Company	TSR (%)
ARG	-5.5%	DUI	-3.8%
DUI	-3.5%	AUI	-2.4%
AFI	-2.9%	ARG	-2.3%

FIG.6: LARGE CAP NTA PERFORMANCE

Top Performers			
January Return		Quarterly Return	
Company	NTA Growth (%)	Company	NTA Growth (%)
BKI	-5.0%	MLT	-1.6%
ARG	-5.2%	BKI	-3.2%
AFI	-5.7%	ARG	-3.8%

Bottom Performers			
January Return		Quarterly Return	
Company	NTA Growth (%)	Company	NTA Growth (%)
DJW	-6.9%	DJW	-6.9%
AUI	-6.5%	AUI	-6.6%
DUI	-5.8%	DUI	-5.1%

FIG.7: SMALL CAP TSR

Top Performers			
January Return		Quarterly Return	
Company	TSR (%)	Company	TSR (%)
WMK	7.7%	WAX	11.1%
ALF	4.7%	WMK	10.5%
WAX	4.7%	WAM	10.2%
CIE	4.6%	FGX	6.0%
WAM	1.9%	ALF	5.4%

Bottom Performers			
January Return		Quarterly Return	
Company	TSR (%)	Company	TSR (%)
WDE	-7.3%	OZG	-17.9%
TOP	-6.1%	GC1	-5.9%
CIN	-6.1%	PIC	-4.0%
GC1	-5.0%	WIC	-3.6%
AMH	-4.5%	NCC	-3.0%

FIG.8: SMALL CAP NTA PERFORMANCE

Top Performers			
January Return		Quarterly Return	
Company	NTA Growth (%)	Company	NTA Growth (%)
ALF	0.0%	WMK	2.9%
OZG	0.0%	CTN	2.9%
TOP	-0.7%	CIN	2.7%
WMK	-0.9%	WAX	2.6%
WAX	-1.1%	WAM	2.2%

Bottom Performers			
January Return		Quarterly Return	
Company	NTA Growth (%)	Company	NTA Growth (%)
CIN	-6.7%	WIC	-8.5%
WHF	-6.3%	CDM	-8.0%
ALR	-6.0%	GC1	-7.1%
CTN	-5.6%	OZG	-6.9%
CDM	-5.1%	ALR	-5.2%

FIG.9: INTERNATIONAL TSR

Top Performers			
January Return		Quarterly Return	
Company	TSR (%)	Company	TSR (%)
FGG	-0.9%	FGG	5.5%
GVF	-1.5%	MFF	-0.8%
ALI	-2.0%	GVF	-2.4%

Bottom Performers			
January Return		Quarterly Return	
Company	TSR (%)	Company	TSR (%)
AGF	-29.3%	AGF	-26.5%
EAI	-11.5%	EAI	-14.6%
MFF	-10.5%	TGG	-14.2%

FIG.10: INTERNATIONAL NTA PERFORMANCE

Top Performers			
January Return		Quarterly Return	
Company	NTA Growth (%)	Company	NTA Growth (%)
ALI	3.2%	AGF	1.8%
AGF	1.5%	GVF	-3.3%
GVF	-1.0%	EGI	-3.5%

Bottom Performers			
January Return		Quarterly Return	
Company	NTA Growth (%)	Company	NTA Growth (%)
EAI	-7.7%	EAI	-12.1%
PGF	-5.7%	TGG	-11.4%
TGG	-5.4%	PGF	-10.1%

FIG.11: SPECIALIST TSR

Top Performers			
January Return		Quarterly Return	
Company	TSR (%)	Company	TSR (%)
LSX	14.3%	ACQ	7.8%
BAF	-0.5%	BTI	-4.0%

Bottom Performers			
January Return		Quarterly Return	
Company	TSR (%)	Company	TSR (%)
BTI	-3.5%	LSX	-33.3%
ACQ	-2.4%	BAF	-5.2%

FIG.12: SPECIALIST NTA PERFORMANCE

Top Performers			
January Return		Quarterly Return	
Company	NTA Growth (%)	Company	NTA Growth (%)
BAF	0.7%	BTI	14.7%
BTI	0.4%	BAF	2.7%

Bottom Performers			
January Return		Quarterly Return	
Company	NTA Growth (%)	Company	NTA Growth (%)
ACQ	-4.1%	LSX	-3.4%
LSX	-3.4%	ACQ	2.1%

Source: Bloomberg, IRESS, Company Report, Baillieu Holst estimates

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Buy: The stock's total return is expected to increase by at least 10-15 percent from the current share price over the next 12 months.

Hold: The stock's total return is expected to trade within a range of \pm 10-15 percent from the current share price over the next 12 months.

Sell: The stock's total return is expected to decrease by at least 10-15 percent from the current share price over the next 12 months.

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