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Business

This trust has slashed the cost of its debt – and income investors should benefit

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Trust Bargains
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We've already made decent gains on Brunner and now the dividend is expected to receive a 10pc boost

A CAPITAL gain of 15pc over 16 months is pretty respectable, especially when the yield adds another 2pc or so – and when next year's dividend is expected to rise by 10pc.

Brunner, which was recommended in this column in April last year, is the trust in question.

Founded in 1927 to manage the wealth of the eponymous family, whose chemicals firm had merged the previous year with three others to form ICI, the trust now has an unbroken 46-year record of dividend increases.

The reason for its board's expectation that the dividend for 2018 will be a tenth higher is found in the fund's borrowings.

Like many investment trusts, Brunner uses "gearing" in an attempt to boost returns. If you can make more on the borrowed money than it costs to service the loan, shareholders will be better off. Doing this is, of course, much easier at times such as the present when borrowing is so cheap. However, many trusts have remained saddled with debts taken on when rates were much higher. If they can refinance these loans more cheaply, the portfolio's net income will rise, other things being equal, and higher dividends will become possible.

> Brunner
> **Hold**
> **Expensive debt has been repaid and management simplified**

This is what is happening at Brunner. It has already repaid an outstanding "debenture" at a cost of £39m, using existing resources and a newly issued £25m, 30-year "private placement note". This note will cost 2.84pc a year in interest, compared with the previous 7.7pc cost of the trust's long-term debt.

The board has estimated that, in the absence of unforeseen circumstances, total dividends for the year to Nov 30 will be 18.15p a share, a 10pc increase on last year's 16.5p. That in turn was a 4.4pc rise on 2016's figure. A payment of 18.15p would represent a yield of 2.7pc for readers who paid 681.25p at the time of our tip.

There are other attractions. Stifel, the broker, said in a recent note that, in addition to tidying up its debt structure, "over the past two and a half years Brunner has been getting its house in order – it has moved to one lead manager [Lucy Macdonald] from two and adopted a more globally focused benchmark".

The trust now aims for a 70:30 split between global stocks and British ones, compared with 50:50 previously.

The discount of 10.7pc, "wide relative to its global peers", according to Stifel, should also be enough to interest new buyers.

There is, however, one cloud on the horizon. The trust's largest shareholder, Aviva, wants to sell its 19pc stake. This is no reflection on Brunner: it is part of a strategic move by the insurer, which has already disposed of shareholdings in other trusts including Witan, Mercantile and BlackRock Income Strategies.

But the presence of such a large intended seller tends to depress the share price and provides a headache for Brunner. "The board now requires a solution to help Aviva exit its investment without causing too much disruption," Stifel said.

Brunner is a solid, low-cost vehicle for exposure to global stock markets and investors should not see their long-term returns unduly affected by the Aviva question.

Questor says: hold
Ticker: BUT
Share price at close: 718.00

Key numbers

- **Market value: £333.5m**
- **Year of listing: 1927**
- **Discount: 10.7pc**
- **Ave discount over past year: 10.1pc**
- **Yield: 2.1pc**
- **Most recent year's dividend: 16.5p**
- **Gearing: 8pc**
- **Annual charge (Nov 2017): 0.72pc**