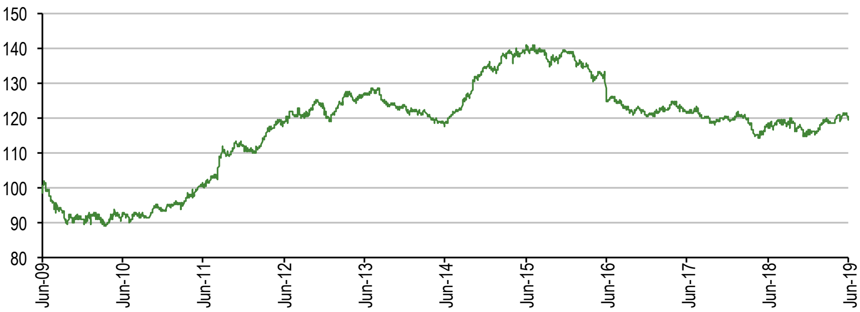
European Assets Trust

Long-term capital growth and high yield

European Assets Trust (EAT) aims to achieve capital growth over the long term through investing in small- and medium-sized companies listed in Europe (ex-UK). Over the past 10 years to end-June 2019, the trust has delivered an annualised NAV total return of 15.1%. EAT also has an attractive 5.6% dividend yield, significantly higher than its peers, reflecting the board's high distribution policy. The trust completed its legal migration to the UK from the Netherlands in March 2019; previously dual-listed in London and Amsterdam, EAT is now solely traded on the London Stock Exchange (LSE) and is a constituent of the FTSE SmallCap and FTSE All-Share indices.

Strong NAV performance relative to benchmark over the past 10 years



Source: Refinitiv, Edison Investment Research

The market opportunity

Economic growth in Europe is stalling, in large part led by its biggest contributor, Germany. This country's exports sectors are facing significant headwinds, including structural challenges for its important autos industry, compounded by weaker global growth, rising US trade protectionism, and uncertain Brexit outcomes. The manager believes a fundamental approach to investing in companies that can achieve growth through economic cycles is the best approach in an uncertain environment.

Why consider investing in EAT?

- Detailed bottom-up approach to building a well-diversified portfolio of c 40 high-quality stocks, with a focus on valuation discipline and capital preservation.
- Good stock selection is typically the main driver for performance. EAT's H119 NAV increase of 20.4% represented a c 4% outperformance vs the benchmark. This was overwhelmingly attributed to stock picking.
- Dividend yield of 5.6%, underpinned by the board's high distribution policy.

Scope for discount to narrow

EAT currently trades on a 8.1% discount to its cum-income NAV, which is significantly wider than its three-year average of 3.6%. Historically, the trust has typically traded close to its NAV, reflecting the board's aim to minimise the volatility of the trust's discount. It hopes EAT's premium London listing and inclusion in the FTSE UK Index series will help attract new investors and improve demand for the trust's shares.

Investment trusts
European smaller companies

10 July 2019

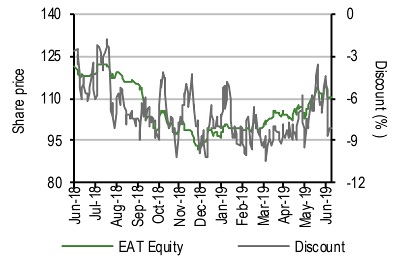
Price	**110.5p**
Market cap	**£397.6m**
AUM	**£430.6m**

NAV*	120.3p
Discount to NAV	8.1%

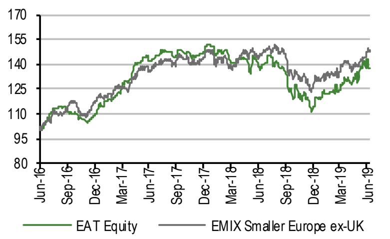
*Including income. As at 8 July 2019.

Yield	5.6%
Ordinary shares in issue	359.8m
Code	EAT
Primary exchange	LSE
AIC sector	European Smaller Companies
Benchmark	EMIX Smaller Europe ex-UK

Share price/discount performance



Three-year performance vs index



52-week high/low	122.5p	91.8p
NAV** high/low	128.3p	100.2p

**Including income.

Gearing

Gross*	0.0%
Net cash*	0.2%

*As at 31 May 2019.

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Edison profile page

European Assets Trust is a research client of Edison Investment Research Limited

Exhibit 1: Trust at a glance

Investment objective and fund background

European Assets Trust was launched as a Dutch company in 1972 and was previously dual listed on the LSE and Euronext Amsterdam exchanges. The trust formally migrated from the Netherlands to the UK on 16 March 2019. It targets capital growth through investment in quoted small- and medium-sized companies in Europe (ex-UK), taking the EMIX Smaller Europe ex-UK index as a benchmark.

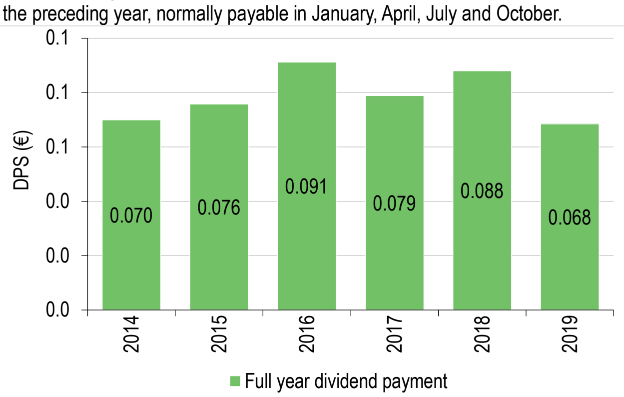
Recent developments

- 18 March 2019: Announced completion of the migration of the company's legal seat and structure from the Netherlands to the UK, and admission to the main market of the LSE effective 16 March 2019.
- 10 January 2019: EGM – shareholders approved the migration of the company from the Netherlands to the UK.
- 8 January 2019: Declaration of 2019 total dividend of €0.0684 per share.

Forthcoming		Capital structure		Fund details	
AGM	May 2020	Ongoing charges	1.1%	Group	BMO Global Asset Mgt (formerly F&C)
Interim results	July 2019	Net cash	0.2% as at end-May 2019	Manager	Sam Cosh
Year end	31 December	Annual mgmt fee	0.8% of gross assets reducing to 0.65% above €500m	Address	Exchange House, Primrose Street, London, EC2A 2NY
Dividend paid	Quarterly	Performance fee	None		
Launch date	1972	Trust life	Indefinite	Phone	+44 (0)800 136420
Continuation vote	None	Loan facilities	€45m with RBSI	Website	www.europeanassets.co.uk and www.europeanassets.eu

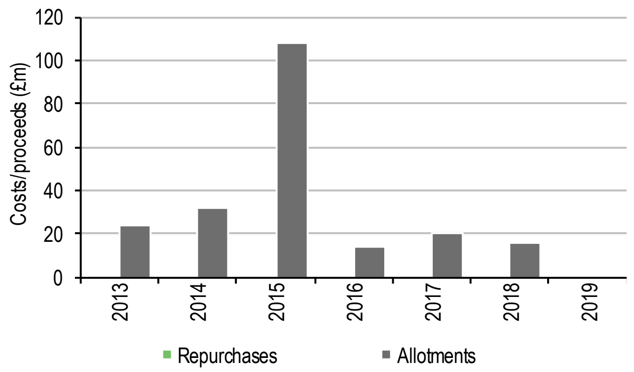
Dividend policy and history

The board targets a distribution of 6% of euro-denominated NAV as at the end of the preceding year, normally payable in January, April, July and October.

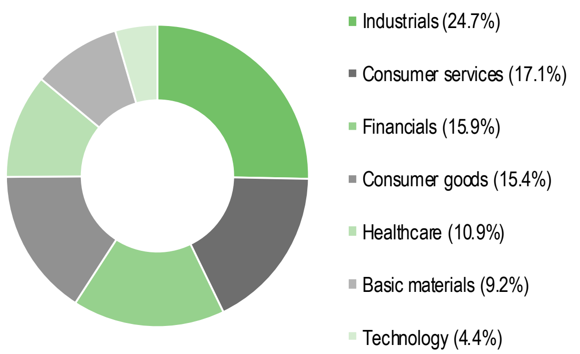


Share buyback policy and history

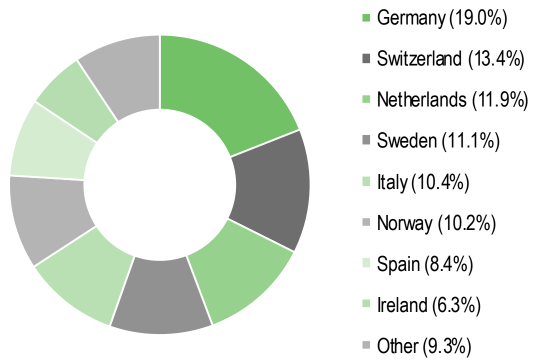
EAT is authorised to both repurchase and allot its ordinary shares. The chart of buybacks and issuance excludes shares issued as scrip dividends.



Portfolio exposure by sector (as at 31 May 2019)



Portfolio exposure by geography (as at 31 May 2019)



Top 10 holdings (as at 31 May 2019)

			Portfolio weight %	
Company	**Country**	**Main area of business**	**31 May 2019**	**31 May 2018***
IMCD Group	Netherlands	Specialty chemicals	4.9	3.1
Gerresheimer	Germany	Glass and plastic containers	4.2	3.8
Forbo Holding	Switzerland	Flooring, adhesives and conveyor belts	4.1	3.5
Vidrala	Spain	Glass bottle manufacturer	3.8	N/A
CTS Eventim	Germany	Concert and ticketing	3.8	4.2
Ringkøbing Landbobank	Denmark	Banking	3.8	3.3
Tecan Group	Switzerland	Healthcare laboratory instruments	3.7	N/A
Coor Service Management	Sweden	Facilities management	3.7	N/A
Cerved Information Solutions	Italy	Data management	3.6	3.3
DiaSorin	Italy	Healthcare diagnostics	3.5	N/A
Top 10 (% of holdings)			**39.1**	**33.9**

Source: EAT, Edison Investment Research, Bloomberg, Morningstar. Note: *N/A where not in May 2018 top 10. Figures subject to rounding.

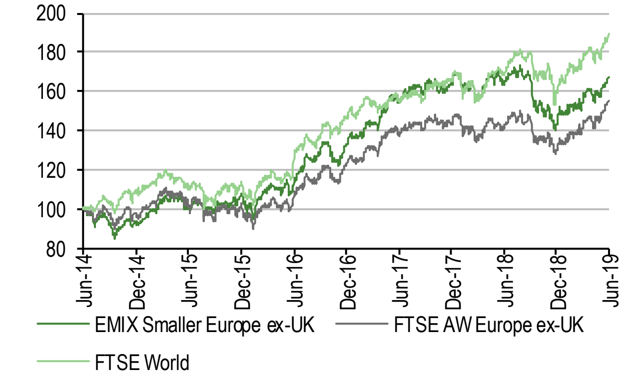
Market outlook: Influenced by geopolitics

Europe's economy has slowed more than expected over the past year, largely led by Germany, which was its engine of recovery in 2017 and early 2018. Growth was mainly powered by German exporters during a period of synchronous global economic expansion, but this sector has since become a source of economic weakness. Expectations for global growth began to moderate in early 2018; however, the escalation of US tariffs against its major trading partners, including China and the EU, have taken a toll on trade as well as investor sentiment. Germany's economy is also being affected by weakness in its autos industry, which accounts for over 16% of its exports. In 2018, the value of German car exports suffered its first decline since 2013, hit by new emissions standards and a significant slowdown in demand from many of its major markets, including the UK and US, but most notably China where German car exports declined by 37%.

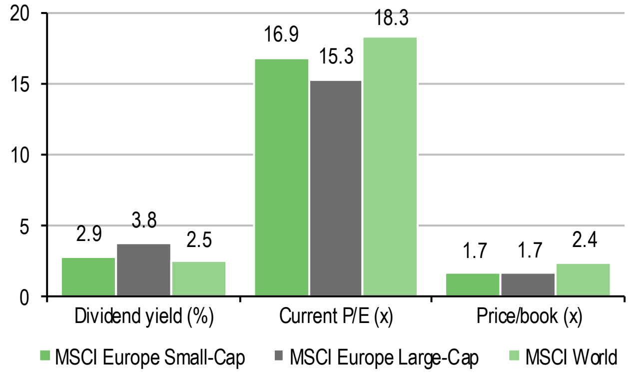
Earnings expectations for European companies have fallen, which is reflected in relatively high P/E ratios (as shown in Exhibit 2, RHS). The European Commission forecasts euro area GDP growth in 2019 to moderate to 1.2% (2018: 1.9%) and accelerate modestly to 1.5% in 2020. These forecasts assume that trade and policy uncertainty recedes or at least does not escalate, highlighting the importance of geopolitical developments to the direction of European equities in the near term.

Exhibit 2: Market performance and valuation

European and world index total returns over five years (£)



Valuation metrics for European small-cap, large-cap and world equities*



Source: Refinitiv, Edison Investment Research, MSCI. Note: *Valuation data as at 28 June 2019.

Fund profile: Bottom-up approach and high yield

EAT aims to achieve capital growth through investing in small- and medium-sized companies listed in Europe (ex-UK). The manager, Sam Cosh, follows a bottom-up and disciplined approach to select c 40 high-conviction stocks that can be held for the long term. The board employs a high distribution policy (see page 8) and EAT's dividend yield of 5.4% is significantly higher than its peers. The trust was launched as a Dutch company in 1972 and migrated its legal seat and structure to the UK on 16 March 2019, where it is listed on the London Stock Exchange and is a member of the FTSE SmallCap and FTSE All-Share indices. The reasons for the migration include:

- an overwhelming majority of the trust's shareholders are UK residents and the investment management and marketing activities are also performed from the UK;
- a simplified corporate structure;
- a single jurisdiction for current and future regulation;
- a potential reduction in ongoing charges; and
- a premium listing on the London Stock Exchange, and inclusion in the FTSE US Index series may increase demand for the trust's shares.

The fund manager: Sam Cosh

The manager's view: Focus on long-term fundamentals

Cosh observes that equity market movements in Europe (and globally) have been driven by an extended period of exceptionally low interest rates and abundant liquidity since the global financial crisis. He notes that investors are very sensitive to geopolitical news and to changes in expectations for the direction of interest rates. Markets were very weak in Q418 when the Federal Reserve was on course to rein in liquidity, and then moved sharply higher in Q119 when it signalled that interest rates are on hold for the time being. The manager believes that exceptionally low interest rates have fuelled growth in global debt levels, which he notes are now higher as a percentage of GDP than before the global financial crisis, and may be storing up problems for the future. However, Cosh is not distracted by macroeconomic or political predictions; he focuses on identifying quality companies with resilient businesses and strong balance sheets that can deliver good earnings growth through economic cycles. The manager notes that, although European growth overall is stalling, there are also areas of strength supported by improving employment levels and stimulative fiscal policies. He also observes that underlying economic performances within the region are not uniform, for example Germany is presenting a drag on Europe's growth, but he thinks Spain has brighter prospects. Cosh believes that EAT's fundamental and disciplined long-term investment approach, with a focus on capital preservation, is particularly relevant in the current uncertain environment.

Asset allocation

Investment process: Patient and disciplined

The manager's investment process is disciplined and bottom-up. Meeting companies is a key element, seeking well-managed, quality companies with sustainable competitive advantages. These may be derived from a company's scale, brand recognition, intellectual property or know-how, or the strength of its business relationships. Valuation discipline is important and the manager looks for companies that trade at a substantial discount to their intrinsic value, which are capable of generating multi-year superior returns and strong cash flows. Cosh is supported by a well-resourced BMO European equities team, comprising 10 members. The team produce detailed, proprietary research for each candidate stock, which includes valuation targets and specific triggers for the sale of a stock. Companies that meet the manager's investment criteria, but are not currently attractively valued, are added to his 'patient fishermen' list of stocks, awaiting a better price entry point.

The portfolio has four broad investment themes:

- **Durable franchise**. This is the core of the portfolio and represents companies with sustainable growth potential, disciplined management and robust business models.
- **Wide moat growth**. These are faster growing companies with an ability to defend market share in a competitive environment.
- **Transformation/recovery**. These firms are undervalued but have a catalyst for change, such as new management or reallocation of capital.
- **Deep value**. These companies are often out of favour, but the manager believes there is recovery potential that is underappreciated by the market.

Current portfolio positioning

Exhibit 3 (LHS) shows EAT's industry exposure and the change over the past year to end-May 2019. During this period, most of the portfolio activity took place in H118 when the manager turned more cautious on the outlook for European equities. At that time, Cosh thought that Europe's economic recovery was maturing, and cyclically exposed companies were at risk of earnings disappointments and share price corrections. He reduced the portfolio's exposure to what he viewed to be relatively expensive stocks with cyclical earnings, in favour of companies with secular growth prospects. This is reflected in the portfolio's shift in sector weights over the past 12 months to end-May 2019, most notably an 8.8pp reduction in industrials, a 4.1pp increase in consumer services and a 3.9pp increase in healthcare. The main sales and purchases were discussed to our recent reports published in January 2019 and July 2018.

Exhibit 3: EAT's industry exposure* and portfolio characteristics (as at end-May 2019)

(% unless stated)	End May 2019	End May 2018	Change (pp)	Benchmark	Active weight vs benchmark		EAT	EMIX Smaller European Companies ex-UK
Industrials	24.7	33.5	(8.8)	24.6	0.1	Forward P/E (x)	16.1	15.5
Consumer services	17.1	13.0	4.1	10.1	7.1	Dividend yield (%)	2.6	2.8
Financials	15.9	15.6	0.3	26.1	(10.2)	Weighted avg market cap (£m)	2,189	2,182
Consumer goods	15.4	17.0	(1.6)	10.8	4.6	ROE (%)	13.7	9.1
Healthcare	10.9	7.0	3.9	8.7	2.2	Net debt/equity (%)	13.2	52.4
Basic materials	9.2	7.4	1.8	4.6	4.7			
Technology	4.4	4.9	(0.5)	7.5	(3.0)			
Oil & gas	2.2	1.6	0.6	2.8	(0.6)			
Total	100.0	100.0						

Source: European Assets Trust, Edison Investment Research. Note: *Figures subject to rounding.

Over the past six months, portfolio activity has been light as the manager believes that the changes made to the portfolio last year continue to be valid, and that the fund should be relatively resilient in the current uncertain environment. As shown in Exhibit 3 (RHS), the EAT portfolio has significantly higher profitability (as measured by ROE) and lower levels of debt compared to the EMIX Smaller European Companies ex-UK index. However, the valuation of EAT companies is only marginally more expensive than the index in forward P/E multiple terms.

EAT has recently purchased a position in food processing company, Marel (Iceland). The company is one of the world's largest manufacturers of food processing machinery with operations in over 30 countries. It has a leading position in the poultry business, which accounts for c 60% of profits, with a global market share of around 20%. The manager believes Marel can benefit from decent organic growth as the industry becomes increasingly automated, which helps raise manufacturers' efficiency as well as reduce contamination risks and improves the traceability of meat through the production process. Cosh also thinks the company's margins can expand over time as there is scope to improve the margins of its meat and fish businesses towards the level achieved by the poultry business. Furthermore, the company plans to be an industry consolidator, which may provide additional upside to growth estimates. The manager participated in Marel's secondary listing on the Amsterdam Euronext exchange in June 2019 at a slight discount to its previous three-month average share price, which the manager believes was an attractive entry point.

In January 2019, EAT disposed of its long-held position in French automotive parts supplier Plastic Omnium. The company has been successful with its exterior body parts products, which are 30% lighter than metal and reduce carbon dioxide emissions. The development and growth of this business was a key part of the manager's investment case in 2013. Looking forward, however, Cosh believes the company faces multiple headwinds, including trade uncertainties (it exports to c 25 countries) and regulatory risk, as governments seek to raise testing standards and reduce the sales of internal combustion engine vehicles.

Over the six months to end-May 2019, the manager has also added and trimmed positions as valuation opportunities presented themselves. Additions included glass bottle manufacturer Vidrala (Spain) and food services company Sligro (the Netherlands). Trims have mostly been to cyclical companies on strong share price performance, including construction and industrial elevator manufacturer Alimak (Sweden), and reverse vending machine manufacturer Tomra (Norway).

Performance: Strong long-term performance

Exhibit 4: Five-year discrete performance data

12 months ending	Share price (%)	NAV (%)	EMIX Smaller European ex-UK (%)	FTSE AW Europe ex-UK (%)	FTSE All-Share (%)
30/06/15	18.2	18.3	(0.3)	0.4	2.6
30/06/16	(4.1)	2.9	14.2	6.3	2.2
30/06/17	41.7	30.9	35.8	28.7	18.1
30/06/18	(0.1)	3.9	6.9	3.0	9.0
30/06/19	(0.2)	1.6	0.6	8.6	0.6

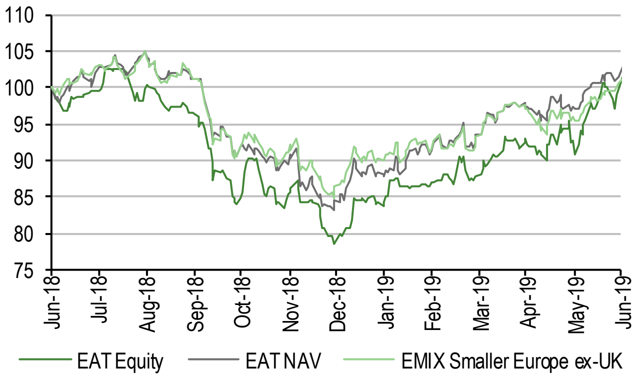
Source: Refinitiv. Note: All % on a total return basis in pounds sterling.

As shown in Exhibits 5 and 6, EAT has delivered strong long-term performance with an annualised 10-year NAV total return of 15.1%. Over five and 10 years, EAT's NAV total return has outperformed the EMIX Smaller Europe ex-UK, FTSE AW Europe ex-UK and FTSE All-Share indices. The three-year numbers are relatively weak and reflect a pronounced underperformance following the result of the UK's European referendum in 2016, for which EAT was poorly positioned. The trust held a number of Ireland-listed companies, which were heavily exposed to the UK domestic economy and sterling.

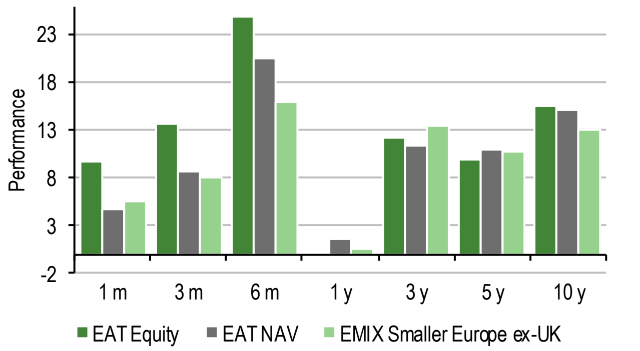
Cosh has a long-term investment horizon and focuses on company fundamentals, without significant regard for political developments. He noted that many of the firms that suffered sharp share price falls following the Brexit vote did recover and make subsequent positive performance contributions to the portfolio. EAT's own attribution analysis shows that positive stock selection is the main contributor to its performance. For H119, the fund outperformed its benchmark by c 4%, which overwhelmingly attributed to stock selection.

Exhibit 5: Investment trust performance to 30 June 2019

Price, NAV and benchmark total return performance, one-year rebased



Price, NAV and benchmark total return performance (%)



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

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 EMIX Smaller Europe ex-UK	4.0	5.2	7.7	(0.8)	(3.2)	(3.6)	24.6
NAV relative to EMIX Smaller Europe ex-UK	(0.7)	0.5	3.8	1.0	(5.4)	1.2	19.8
Price relative to FTSE AW Europe ex-UK	3.1	4.1	5.9	(8.1)	(1.9)	4.1	55.3
NAV relative to FTSE AW Europe ex-UK	(1.6)	(0.5)	2.1	(6.4)	(4.1)	9.3	49.4
Price relative to FTSE All-Share	5.8	10.0	10.5	(0.8)	9.1	17.9	58.3
NAV relative to FTSE All-Share	1.0	5.2	6.6	1.0	6.7	23.8	52.2

Source: Refinitiv, Edison Investment Research. Note: Data to end-June 2019. Geometric calculation.

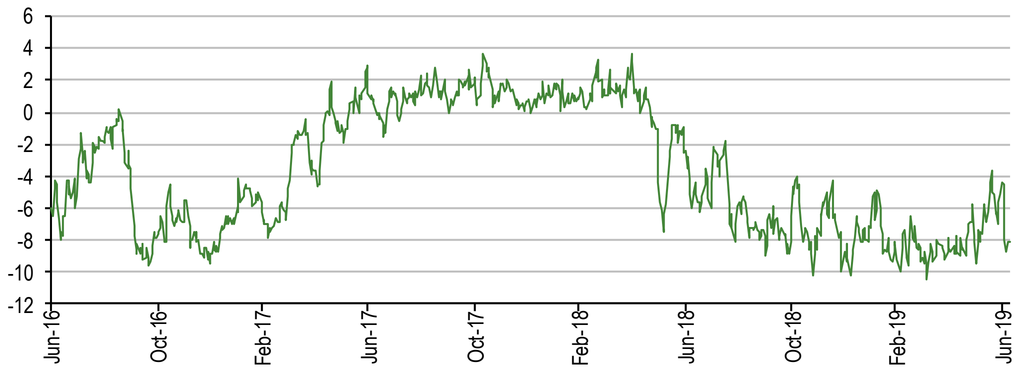
Exhibit 7: NAV total return performance relative to benchmark over five years

Source: Refinitiv, Edison Investment Research

Discount: Demand for shares may improve

EAT is currently trading on a 8.1% discount to cum-income NAV, which is significantly wider than its three-year average of 3.6%. The board actively monitors the trust's share price volatility relative to its NAV and has the ability to manage the demand and supply balance for EAT's shares through share issuance and repurchases. The board anticipates that, following the trust's migration to the UK, demand for EAT's shares may benefit from its premium listing on the LSE and its inclusion in the FTSE SmallCap and FTSE All-Share indices.

Exhibit 8: Share price premium/discount to NAV (including income) over three years (%)



Source: Refinitiv, Edison Investment Research

Capital structure and fees

The migration of EAT NV from the Netherlands to the UK was completed on 16 March 2019 and shareholders of the Netherlands-registered company received one ordinary share of the UK-registered company (EAT). EAT has one class of share and, following a 10-for-one stock split in May 2018, there are 359.8m shares ordinary shares in issue and none held in treasury. Demand for the trust's shares has historically been robust, and the board has issued new shares to meet demand. During FY18, EAT issued 12.1m new shares raising £15.4m (in FY17 the equivalent of 15.3m shares were issued, raising £19.8m).

EAT has a €45m loan facility with RBSI; as at end-May 2019 it was ungeared and had a net cash position of 0.2%.

Dividend policy and record

The board has a distribution policy (barring unforeseen circumstances) to pay an annual dividend equivalent to 6% of the trust's NAV as at the end of the preceding year. Dividends are funded from income and distributable reserves. The board has announced 2019 total dividends of €0.0684 per share (2018: €0.088), reflecting a 16.3% decline in the trust's euro-denominated NAV total return (with dividends reinvested) for the year to end-December 2018. The 2019 distribution will be paid in four instalments in January, March, July and October. Following EAT's migration to the UK, dividends paid in July and October 2019, and thereafter, will no longer be subject to Dutch withholding tax. Dividends for 2019 in sterling terms will be determined by the sterling-euro exchange rate prevailing on the dates and, at the current rate, suggest a prospective dividend yield of 5.4%.

Peer group comparison

Exhibit 9 shows the AIC European Smaller Companies sector, which consists of just four funds. EAT's NAV total return ranks second over one and 10 years, third over three years, and fourth over five years. Its ongoing charge ranks second and there is no performance fee. The trust's discount to its cum-fair NAV ranks third however, the current 8.1% discount to cum-fair NAV is wider than usual. Typically the trust has traded close to its NAV and the average discount over the past three years is 3.6%. It ranks first for dividend yield which, at 5.6%, is significantly higher than its peers.

Exhibit 9: AIC European Smaller Companies peer group as at 9 July 2019*

% 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 (%)
European Assets Trust	397.6	3.5	37.8	71.9	313.3	(8.1)	1.1	No	100	5.6
JPMorgan European Smaller Cos	591.6	(2.5)	36.1	85.6	299.6	(12.8)	1.1	No	100	1.8
Montanaro European Smaller	185.3	14.1	68.2	111.1	330.9	(2.1)	1.2	No	100	0.8
TR European Growth	457.0	(4.3)	44.6	79.3	274.5	(6.9)	0.7	Yes	112	2.4
Simple average in sector	**407.9**	**2.7**	**46.7**	**87.0**	**304.6**	**(7.5)**	**1.0**		**103**	**2.6**
EAT rank in sector	**3**	**2**	**3**	**4**	**2**	**3**	**2**		**2**	**1**

Source: Morningstar, Edison Investment Research. Note: *Performance data to 8 July 2019. TR = total return. Net gearing is total assets less cash and equivalents as a percentage of net assets.

The board

Prior to the migration to the UK, in accordance with Dutch corporate governance requirements, EAT had a two-tiered board comprising a supervisory board and a management board. Following the migration, the management board is no longer required and the trust has a unitary board composed of all five members of the previous Dutch supervisory board. Chairman Jack Perry was appointed in 2014. Deputy chairman professor Robert van der Meer and senior independent director Julia Bond were appointed in 2007 and 2014 respectively. The other directors and the dates of appointment are Laurence Jacquot (2011) and Martin Breuer (2016).

General disclaimer and copyright

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