Miton Global Opportunities

Investing in a diverse array of other trusts, MIGO seeks to build a portfolio with significant embedded value...

Update
17 December 2020

Summary

Miton Global Opportunities (MIGO) offers exposure to a diversified pool of closed-ended investment companies, often operating in highly specialised areas and trading on substantial discounts to their intrinsic value and where MIGO's managers believe there is a catalyst for a re-rating. Aiming to beat cash (three-month SONIA plus 2%), the trust is relatively unconstrained in asset allocation.

MIGO's managers believe we are likely seeing structural changes to the investment trust universe which are opening up opportunities. This includes broader use of the investment trust structure for alternative asset classes, consolidation in the investment trust market in other asset classes (where the persistence discounts are likely in the managers' view to attract merger activity or similar), and greater retail utilisation of investment trusts.

Furthermore, as discussed under **Portfolio**, MIGO's managers believe we may ultimately witness a change in market and economic environment towards a more inflationary backdrop. That could catalyse opportunities to narrow discounts across a broad range of assets, which could be a strong tailwind to MIGO's returns if it were to occur.

As noted under **Performance**, typically MIGO has consistently displayed a lower correlation to global equities than the wider Morningstar Flexible Investment peer group whilst delivering returns over twice those seen by the FTSE All-Share over the previous five years. An inflationary environment (which the managers anticipate materialising) could serve as a tailwind to absolute returns.

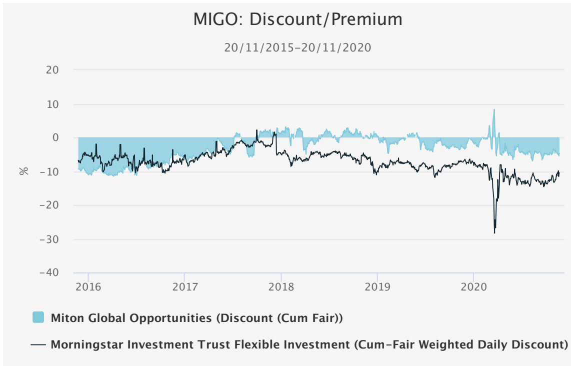
Whilst MIGO trades on a share price discount of c. 4.7% (as at 20/11/2020), the underlying holdings themselves trade at sizeable discounts to what the managers deem to be their fair-value NAVs. There is therefore a greater look-through double discount, as discussed under Discount.

Analysts:

Callum Stokeld
+ 44 (0) 203 795 9719

Key Information:

Price (p)	280
Discount (%)	-4.6
OCF (%)	1.34
Gearing (%)	0
Yield (%)	0.0
Ticker	MIGO
Market cap (£)	76,243,958



Kepler View

MIGO presently tilts towards 'vaccine beneficiaries' on an output basis, yet the managers have also taken care to ensure that the positions they hold are typically operationally and financially robust. As and when economic normalisation occurs, we think there may be broad-based valuation opportunities across swathes of financial markets, perhaps in areas deemed to be illiquid by many investors looking to tactically allocate. We think the trust structure of MIGO and the focus on the trust itself identifying other trusts to invest in should stand it in good stead to identify opportunities which retain 'catch-up' potential.

Given MIGO's focus on identifying poorly researched trusts where share prices do not reflect their potential, such an environment as we have experienced over much of 2020 should have presented a highly attractive hunting ground for the managers. As well as opening up the possibility of initiating positions in high-quality trusts previously deemed too pricey by the managers (such as Tufton Oceanic Assets) at more attractive valuations, the generalised sell-off of Q1 also afforded the managers the chance to top up positions in trusts with tangible routes to value realisation (such as Dunedin Enterprise Investment Trust).

The resultant portfolio looks to us to have some attractive optionality to a higher inflationary environment, whilst retaining fundamental look-through value should this scenario not materialise. Typically low correlations to broader equity markets make this a potentially attractive portfolio diversifier, particularly for investors whose equity exposure is currently tilted towards growth strategies.

BULL
Returns have been lowly correlated to wider equity markets in ordinary market conditions
Any rise in inflationary pressures could prove a tailwind
Exposure to an array of otherwise hard-to-access, relatively illiquid opportunities

BEAR
Illiquid nature of many closed-ended holdings makes discounts vulnerable to market reversals
Gearing can exacerbate downside (as well as amplify upside)
Will not suit investors who want to control their asset allocation

Portfolio

Miton Global Opportunities (MIGO) is a trust of trusts specialising in deep value opportunities and special situations. The management team of Nick Greenwood and Charlotte Cuthbertson seek to identify pricing inefficiencies within the investment trust market, as well as thematic drivers for discount convergence to the share price. In practice, this often means buying trusts on deep discounts where there is a catalyst for a significant narrowing of the discount and/or a cyclical or structural change in operating environment.

Nick and Charlotte primarily seek opportunities on a bottom-up basis. However, there are certain thematic underpinnings running through MIGO's portfolio. These include allocations to specific opportunities based on what they view as attractive asset classes, but also themes relating to industry construction within the broader investment trust universe. As we have previously highlighted, Nick and Charlotte anticipate a general trend of narrowing discounts across the investment trust universe with several drivers. These include a shift towards increasing utilisation of the investment trust structure for illiquid alternatives investments, increasing consolidation amongst existing (more conventional) strategies, and increased inflows by retail investors.

With MIGO having a closed-ended capital structure, the managers are better able to take high-conviction positions in what are often relatively illiquid underlying holdings. Although there are currently c. 54 holdings in MIGO (as at 31/10/2020), there is a sizeable tail of smaller holdings, with over 51% of the portfolio presently held in the top ten holdings and over 94% of the portfolio in the top 30 positions. Some of the smallest positions include holdings in the latter stages of winding up, or holdings which have potentially extremely convex return potential (such as warrants). Nick and Charlotte prefer to initiate holdings with small positions, and build these further as they develop conviction. As such, certain very small holdings may be considered exploratory as they determine whether to pursue the opportunity or not.

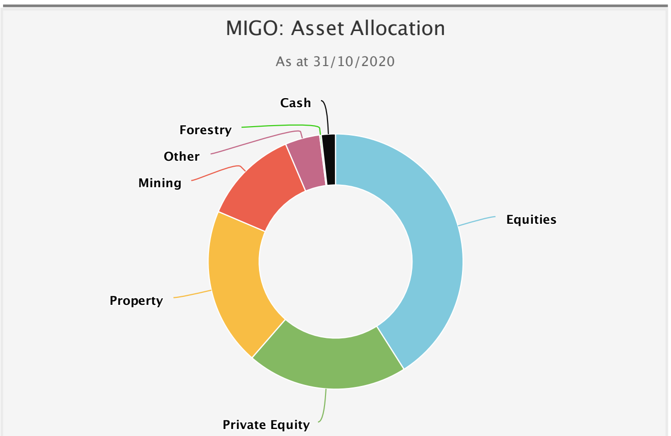
The managers have a long investment horizon and so have the ability to take positions in themes where they see a catalyst for future returns. A recent example of this is in uranium, which has been a theme in the portfolio in recent years. The managers identified that a supply-and-demand crunch would materialise at some point as there was less mining production but increased demand from nuclear power stations. In recent weeks we have seen this develop as the US has announced a strategic stockpiling, and COVID-related mining closures have seen supply curtailed. The uranium market has been quiet in recent years so most investors have been more interested in more mainstream commodities; however, MIGO's management team have been keeping a close eye on this market for the right time to add to the position.

Many of these holdings offer identifiable routes to value realisation, but are often too illiquid for large investment houses to take on significant exposure. As noted above, there is a substantial tail of smaller positions, many of which are in wind-up and returning capital to shareholders and offering high potential IRRs with relatively low equity market correlation.

Positions in trusts undergoing wind-up can also include some of the larger holdings in MIGO too, such as Dunedin Enterprise Investment Trust (DNE). Nick and Charlotte anticipate DNE's wind-up being completed in two to three years, and anticipate not only a narrowing of the discount (currently c. 16.6% at the time of writing) but also NAV uplift. DNE recently saw Visa take a stake in one of its largest holdings (a payments processor) which could potentially materially uplift the reported valuation of DNE. DNE recently conducted a tender offer as part of the planned liquidation strategy, with MIGO participating. On other occasions, sales within MIGO may be more conventional, such as the relatively recent decision to take profits from biotechnology holdings following a strong rise in their share prices (having first purchased them amidst the market turmoil of December 2018).

Whilst a top-down macroeconomic viewpoint is incorporated into the trust, portfolio construction is primarily a function of bottom-up idea conviction, tempered with consideration of the balance of themes within the portfolio. The team are cognisant of ensuring the portfolio is suitably diversified across different themes. Along with diversification considerations, position sizing also accounts for the perceived relative opportunity offered by individual holdings. In line with the thematic considerations noted above, Nick and Charlotte are increasingly identifying opportunities in alternative

Fig.1: MIGO: ASSET CLASS ALLOCATIONS



Source: Premier Miton

asset classes, and these should be reasonably expected (outside of cyclical opportunistic weightings) to account for an increasingly greater proportion of MIGO's assets. The team believe that these non-equity holdings should typically have independent drivers of NAV returns and will often display low to no correlation to wider equity markets (though their share prices may do in moments of more acute market stress or ebullience).

Whilst they identify long-term opportunity sets in alternative asset classes, where the closed-ended nature of the investment trust structure is well suited, Nick and Charlotte will also look at potential opportunities in conventional asset classes. Within the portfolio there remains, for example, a substantial play on UK small- and micro-cap equities, represented by a basket of investment trusts. The managers of MIGO note that there also remains the detritus of the Woodford fallout hanging over UK small and micro caps, which in their view are damned by association. In their view this has poisoned wealth-management risk department sentiment against a considerable proportion of the market, at the same time that wealth-management industry consolidation has often rendered holding meaningful positions in smaller vehicles (increasingly defined as c. sub-£250m in market cap) unviable.

However, Nick and Charlotte view the valuation opportunity within UK smaller companies as extremely heightened, with the potential for easing of political concerns to potentially serve as a catalyst for strong share price returns. They note that they regard current valuations as being so compelling that they would anticipate buyers emerging from sources other than public equity markets if a re-rating does not occur soon. This may be through industry consolidation and merger & acquisition activity, or through private equity buyers (signs of which have started to emerge).

Within the basket of UK equity holdings in the portfolio there are some tactical tilts, including an increase in exposure in recent months to Artemis Alpha Trust (ATS). Nick and Charlotte observe that the greater value tilt of this portfolio should, in their view, leave the trust itself more likely to be exposed to any recovery in the UK market. ATS also offers an exit strategy should the base case of a strong NAV recovery catalysing discount narrowing not materialise, with the trust operating a tender offer in 2021 that will redeem up to 25% of shares at close to NAV. With ATS trading on a discount of c. 13.9% at the time of writing (despite a very sharp share price rally in recent weeks following positive news on potential COVID-19 vaccines), there remains a degree of protection against any NAV headwinds from the uplift that would be realised from the current discount should investors decide to exit via the tender offer at close to NAV.

The positive sensitivity that ATS is expected (and thus far largely has demonstrated) to demonstrate from any global macroeconomic recovery/normalisation is more broadly true of MIGO's portfolio on an aggregated risk analytic output. As we have previously discussed, the managers broadly anticipate the impact of fiscal and monetary policy responses to ultimately prove inflationary, noting that there are already incipient signs that spare capacity is diminishing in many areas (either through destruction in the wake of the COVID-19-induced economic contraction, lack of replacements from low capex spending, or a mixture of both). However, they do not believe this will necessarily materialise until a prolonged and sustained recovery occurs.

Accordingly, MIGO's portfolio does not presently comprise a broad-brush, quantitative approach to value. Many lowly rated companies are, in the managers' view, lowly rated in recognition that they face very real insolvency and obsolescence risks. Instead, they prefer to tilt towards companies with real assets, which should stand as beneficiaries of any ultimate inflationary environment, but which often operationally display significant resilience to ongoing cyclical macroeconomic fluctuations. This can be seen in their holding in Tufton Oceanic Assets (SHIP), a position initiated earlier in 2020 to which they have continued to add to on weakness.

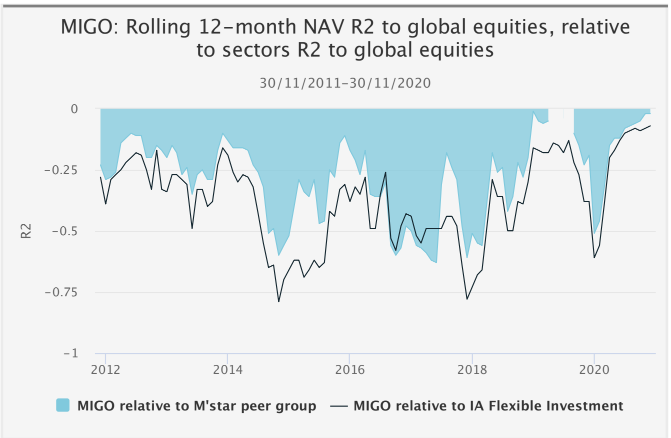
SHIP itself benefits from certain squeezes on supply within the broader industry, as the shipping industry has in recent years failed to add replacement capacity sufficient to offset retired capacity. SHIP is exposed to default risk from the operators who lease its ships, and also from potentially having idle ships should contracts not be renewed. The former is considered a mild risk by Nick and Charlotte (as the counterparties are large multinational companies), whilst the latter is diminished by recent industry trends. Accordingly, despite a market assumption that SHIP is highly cyclically exposed, the cash flows generated should remain resilient in their view, and this should continue to support a generous dividend.

The preference to tilting towards 'real assets' can largely be seen in the top ten holdings, with several of the largest positions holding 'real', hard underlying assets. As we have **previously noted**, the managers believe these are frequently misunderstood or attract little coverage in the wider market, and as such positive operational updates are frequently only recognised in share prices when their results are announced.

Top holding Baker Steel Resources Trust (BSRT) is not, despite the macroeconomic outlook of the managers and the nature of the trust, an explicit play on commodities. Instead, Nick and Charlotte note the very high quality and depth of experience of the management team (who

below. This shows the rolling 12-month R^2 of MIGO's monthly NAV returns to the MSCI ACWI, relative to the R^2 of the sectors in question to the MSCI ACWI. When the line is below zero, MIGO has displayed lower correlation than the sector.

Fig.3: MIGO: ROLLING 12-MONTH NAV R^2 TO GLOBAL EQUITIES, RELATIVE TO SECTORS' R^2 TO GLOBAL EQUITIES



Source: Morningstar

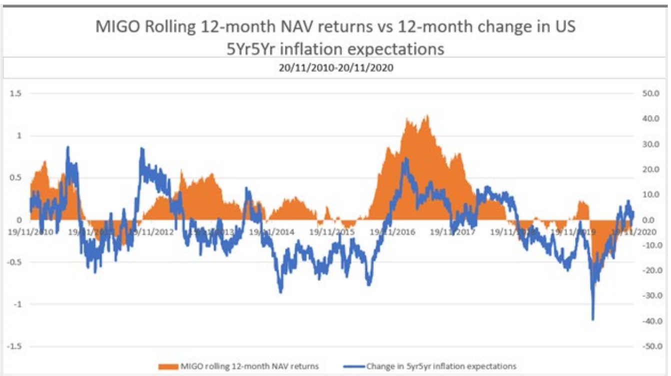
Intra-market correlation was high in the initial sell-off (amidst a general liquidation of assets), and general market direction has remained high: despite a wide bifurcation in performance of the different investment styles, the R^2 of the MSCI World Value to MSCI World Growth, Momentum and Quality indices has been above the ten-year median reading. As **we have previously noted**, such environments have typically made for more challenging performance environments for MIGO, offering as they do less opportunity for idiosyncratic value realisation.

Nonetheless, MIGO has generated positive absolute NAV returns over the last 12 months, with NAV and share price returns of c. 1.7% and 0% respectively (to 20/11/2020). Over the same period, the Xtrackers FTSE All-Share ETF declined by c. 8.5%, whilst the Morningstar Flexible Investment peer group saw NAV gains of c. 2.1% and share price declines of c. 6.8%. We note that many of the holdings with exposure to alternative asset classes proved more resilient in the market drawdown, whilst narrowing discounts and rebounding NAVs in several equity trust holdings have helped returns in recent months.

As we can see in the graph below, MIGO's managers have generally been successful in achieving absolute gains, with rolling 12-month NAV returns positive on c. 70% of occasions over the previous ten years.

With a clear focus on present valuations, it is perhaps unsurprising that the direction and magnitude of MIGO's levels of absolute returns over the previous ten years have seen a degree of correlation to changes in inflation expectations. This association has become stronger in recent years. Rising inflation expectations would generally be accompanied by a market-level association with higher interest rates and, accordingly, the need to apply higher discount rates to valuation multiples. This favours present value over growth strategies, and vice versa. Whilst it is notable that MIGO has generated positive absolute returns in periods where inflation expectations have been falling, we think there is a logical rationale to expect higher inflation rates to help drive stronger absolute levels of NAV returns for MIGO. In fact, as we have discussed under Portfolio, this correlates with the managers' investment thesis: Nick and Charlotte's base case macroeconomic assumption is ultimately for higher inflation rates to materialise as a result of the extraordinary fiscal and monetary stimulus currently being applied by governments and central banks across the world.

Fig.4: MIGO: ROLLING 12-MONTH NAV RETURNS VERSUS 12-MONTH CHANGE IN US 5YR5YR INFLATION EXPECTATIONS



Source: Morningstar, St. Louis Federal Reserve

Dividend

MIGO does not target dividends, and has not paid a dividend in the past 12 months. Whilst dividend streams are generated from the portfolio, the trust is targeting capital growth and the investment management fee is charged directly against the income account (with any shortfall paid out of capital). In the past three reporting years, dividends generated have been sufficient to cover all management costs. Other expenses are also deducted from the income account. Any excess has been used to reduce the deficit in revenue reserves. In the most recent financial year (ending 30/04/2020), net income per share was 1.5p per share, whilst revenue reserves were c. 1.3p per share in deficit.

Management

MIGO is managed by Nick Greenwood and Charlotte Cuthbertson. Nick has over 40 years' experience in the investment trust sector and was a founder member of the Christows stockbroking operation in 1991. He joined Miton following the merger with Exeter Fund Managers in November 2007. He has managed Miton Global Opportunities for 16 years and also runs the OEIC equivalent – Premier Miton Worldwide Opportunities.

Charlotte Cuthbertson works as the assistant manager on the trust, having joined Miton in 2015 and worked on the investment trust team since 2017. Further idea generation is often stimulated by conversations the team have with Miton colleagues and external brokers.

Discount

MIGO presently trades on a discount of c. 4.7% (as at 20/11/2020). This is relatively wide compared to recent history, with MIGO displaying a median discount level of c. 2.9% over the previous five years. We note that, over the previous five years, the headline discount has been tighter to NAV than the present level on c. 65% of occasions.

Whilst the headline discount is at a narrower level than that of the wider peer group, the underlying holdings in the portfolio trade at a significant discount to their NAV. Even having marked down the NAV of several of the holdings to reflect ongoing trading and operational conditions, the managers estimated the top 12 holdings were trading at a weighted average discount of around 26.4% to their NAV at the end of October.

Discount control considerations have become an increasing focus of MIGO's board in recent years, and this, along with a rise in retail shareholders, has seemingly helped to improve liquidity in MIGO shares. As a result, there has been a significant narrowing of MIGO's discount in recent years. Given the relatively small size of the trust, we believe the board is keen to issue stock to grow the trust if and when the shares trade at a premium.

MIGO: NEW ISSUANCE AND BUYBACKS IN CURRENT FINANCIAL YEAR

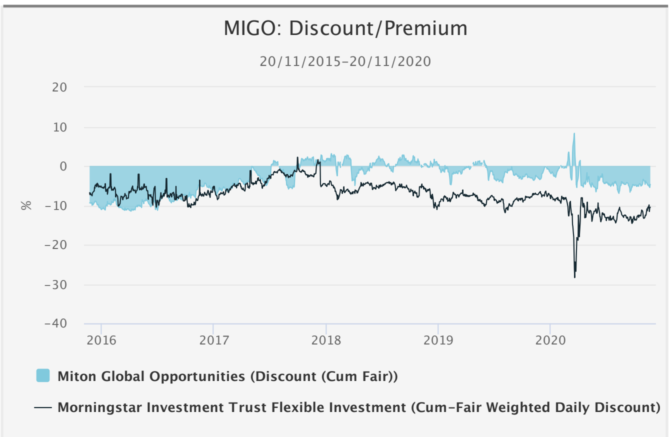
ACTIVITY	TOTAL SHARES DEALT	TOTAL CONSIDERATION PAID (-)/RECEIVED (+) (£)	WEIGHTED AVERAGE PREMIUM/ DISCOUNT
Net issuance	+1,50,000	c. +306k	+1.0%
Buybacks	-5,75,000	c. -1,318k	-4.9%
Net Effect	-4,25,000	c. -1,011k	

Source: London Stock Exchange

The board remains active in the current financial year (commencing 01/05/2020), having repurchased for cancellation a net 425,000 shares (to 20/11/2020). The trust has issued shares whilst shares traded at a premium, and repurchased whilst at a discount. We can see the breakdown of activity in the table below.

MIGO offers a realisation option to shareholders every three years, with the next opportunity arising in 2021. Together with increased retail ownership, these factors appear to have helped to narrow the discount, and while there remains some volatility in the level of the discount, it has consistently traded within a narrower range in recent years.

Fig.5: MIGO: DISCOUNT/PREMIUM



Source: Morningstar

Charges

MIGO currently has an OCF of 1.3%, which compares to an AIC Flexible Investment sector average of 0.84%. The management fee is charged at 0.65%, based on the market capitalisation. Management fees are taken from income, and this was more than covered over the previous financial year by existing income streams. The Key Information Document Reduction in Yield (KID RIY) figure is 1.96%, compared to a sector average of 2.85%, although we caution that calculation methodologies vary.

ESG

Through its management company, MIGO aims to encourage adherence within its holdings to best-practice standards with regards to corporate governance, and to conduct itself (as a trust) responsibly and ethically. This has included a move to giving all shareholders the option of receiving all communications electronically to reduce their carbon footprint.

However, the managers of MIGO itself are not consciously targeting ESG outcomes. Whilst the managers will engage with the boards of constituent holdings to try to ensure good corporate governance is being upheld, the nature of the trust is such that neither the board nor the managers deem it do be in the interests of MIGO shareholders to constrain the range of assets that can be held within the trust.

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