Results analysis: Henderson European Focus Trust

A focused portfolio of European 'Global Champions'

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- **Henderson European Focus's (HEFT's) NAV and share price total return for the year to 30/09/2023 were 24.1% and 27.7% respectively, outperforming the benchmark, the FTSE World Europe ex UK, which produced a total return of 20.5%. The equivalent NAV total return figure for the AIC Europe peer group was 20.0%. The trust has also outperformed its benchmark over three, five, seven and ten years and in the analysis below we highlight the performance since 2010.**

- **Performance in 2023 was driven by semiconductor stocks BE Semiconductor and ASM International, along with long-term holding Holcim and pharmaceutical company Novo Nordisk, which has now become Europe's largest company by market capitalisation. Detractors included insurer ASR Nederland, oil major Shell, AkerBP and Finnish pulp and paper manufacturer UPM Kymmene. The position in banks has been entirely sold, as has the position in utilities.**

- **Total dividends for the year were 4.35 pence per share (2022: 4.35p). At the closing share price on 12/12/2023 of 167p this represents a yield of 2.6%.**

- **HEFT currently trades at a c. 13% discount, starting the financial year at c. 14%. The current discount is slightly wider than the five-year average of c. 11%, and wider than the AIC Europe peer group average of c. 9%. During the year, the board repurchased a small number of shares, highlighting that it is prepared to use buybacks should the discount become excessive, while believing that performance and wider investor sentiment are the primary long-term drivers of the discount.**

- **HEFT's management team made dynamic use of gearing over the year, taking gearing up to 11% in March and, following strong performance, reducing it to a current small net cash position, as noted in the chair's comment below. HEFT's gearing comes from low-cost long-term debt in secured early 2022 with an average interest cost of 1.57%.**

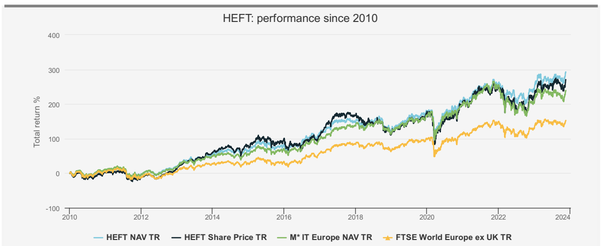
- **During the year, co-manager John Bennett, who has managed HEFT since 2010, announced he would retire in August 2024. Co-manager Tom O'Hara has worked on HEFT since 2020 and the manager and board anticipate no change to the process and philosophy of the trust.**

- **Chair Vicky Hastings said: "With US bond yields not far off the levels last seen in the Global Financial Crisis, geopolitical risks that have continued to rise and the very real threat of recessionary forces, it is not a surprise that your fund managers are erring on the side of caution and, for the first time that I can remember, investing in UK gilts (albeit for the very short term) to de-gear the company. However, for active stockpickers (as opposed to index huggers or passive funds), when markets get volatile and uncertainty increases, opportunities arise, and good investment returns can accrue for the medium to longer term. Indeed, this is the environment we now face and which your fund managers are embracing. Meetings with the underlying company management teams continue and, for some, the future is very bright. Your board remains confident in your fund managers' ability to uncover these opportunities and for the company to continue to prove a good long-term investment for its shareholders."**

Kepler View

As the board notes, manager John Bennett, who took on the role in 2010, has delivered strong outperformance over that time, which is highlighted in the chart below. The same chart illustrates that European equities can be very fertile ground for active management given the large number and diversity of companies to choose from.

Fig.1: Performance Since 2010



Source: Morningstar
Past performance is not a reliable indicator of future results.

The announcement of John's retirement was made in August 2023, and we think giving a full year's notice is an example of best practice, allowing for a proper succession process. John's co-manager Tom O'Hara is an experienced professional. He has been with Janus Henderson since 2018 and has worked as co-manager of HEFT since 2020, so investors can expect a continuation of the same process and philosophy that has delivered the results recorded in the chart above.

Tom very recently appeared in a webinar hosted by Kepler, which can be viewed here, where among other things he made the observation that European equities are, on a forward P/E basis, cheaper than they have ever been compared to US equities. Industry fund flow data shows that during 2023, investors haven't been selling European equity funds in the huge volumes they did in 2022, but neither have they re-embraced them, with a steady drip of selling. So, despite good performance since the lows of September 2022, these low valuations may yet help turn the tide on investor sentiment, which could be very constructive for European equities generally.

While big picture factors such as these do matter, what really shines through in the results is the team's enthusiasm for stock picking, which is done in the context of their strong views about the big trends that will help drive investment returns. Thus, while a lot of investor focus relating to AI has been on US company Nvidia, HEFT's portfolio features leading global semiconductor equipment manufacturers such BE Semiconductor and ASM International, which provide essential equipment to the industry, and are likely beneficiaries no matter which company ends up manufacturing the end product. The team's carefully considered approach to ESG is highlighted by the good performance of long-term holding Holcim. While an energy-intensive industry such as cement might not at first glance be an obvious ESG beneficiary, Holcim is a leader in reducing its reliance on fossil fuels and in utilizing recycled materials in some of its products, and its good performance shows that other investors are beginning to reward something that the HEFT team realized some time ago. This also serves to highlight that whilst a focused portfolio, HEFT provides exposure to a broad set of themes, and the team do not have a fixed investment style, but instead follow the evidence to find the best returns.

In addition to this core proposition, some other features are worthy of mention. HEFT's gearing facility, secured before interest rates began to rise, has an average interest rate of 1.57% over 25-30 years, which today looks like exceptionally good value, and it's hard to imagine when it will next be possible to replicate such terms. HEFT is primarily a capital return vehicle but the yield of 2.6% is generally covered by underlying income, with revenue reserves used to occasionally smooth things. HEFT is currently trading at a 13% discount. With European equities at exceptionally low valuations, and notwithstanding the strong performance of the last year, we think this could be a very good entry point for long-term investors.

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