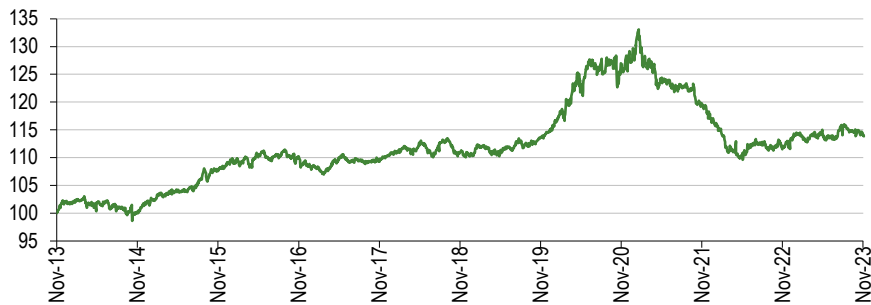


Henderson EuroTrust

Good stock selection outweighing headwinds

Henderson EuroTrust's (HNE's) manager, Jamie Ross, is heartened by the trust's outperformance in FY23 despite investors favouring lower-quality value stocks. This result was achieved through successful stock selection. The manager employs a long-term view, seeking high-quality companies with high or improving returns. He also has a mid- and long-term record of NAV outperformance versus the Europe ex-UK market, although the trust encountered a protracted period of style headwinds between Q121 and Q222. In absolute terms, over the last decade, HNE's NAV total return of 9.4% per year is comfortably ahead of the market's 8.0% annual total return. European stocks are trading at a meaningful discount to global peers and with the trust continuing to be valued at a double-digit discount, now could be an opportune time to consider a portfolio of high-quality companies where the manager has a proven strategy of successful fundamental stock selection.

NAV versus Europe ex-UK index (last 10 years) – getting back on track following a period where value rather than growth stocks led the market



Source: Refinitiv, Edison Investment Research

Why consider HNE?

Ross has been HNE's sole manager since February 2019, having progressed from his role as deputy manager in March 2017. He works in a collegiate environment and can draw on the very wide resources of Janus Henderson Investors when required. The trust has a portfolio of around 45 Europe-listed businesses that is diversified by sector and geography. HNE's well-defined and repeatable investment process incorporates ESG/sustainability analysis as an integral element and the trust is designated as a Light Green fund under Article 8 of the EU Sustainable Finance Disclosure Regulation.

With its focus on generating a superior total return, alongside seeking capital growth, HNE also offers a dividend yield, which ranks highly versus most of its peers in the AIC Europe sector. In FY21, the board announced a change in the company's dividend policy, whereby distributions would be broadly based on the level of income received. At the time, the trust had significant revenue reserves, which were paid out in FY21 and FY23. The board has recently announced that due to the pattern of income receipts, there will now be a single annual dividend payment rather than a modest interim and a larger final dividend.

Investment trusts
European ex-UK equities

13 December 2023

Price 137.5p
Market cap £291m
Total assets £348m

NAV* 159.7p
Discount to NAV 13.9%

*Including income at 11 December 2023.

Yield 2.8%
Shares in issue 211.9m
Code HNE
Primary exchange LSE
AIC sector Europe
Financial year-end 31 July
52-week high/low 140.5p 121.0p
NAV* high/low 164.5p 141.5p

*Including income

Net gearing* 5%

*At 31 October 2023

Fund objective

Henderson EuroTrust aims to achieve a superior total return from a portfolio of European (excluding the UK) investments where the quality of the business is deemed to be high or significantly improving. HNE has an all-cap mandate but tends to have a bias towards large and medium-sized companies. ESG factors are embedded within the investment process.

Bull points

- Long-term record of outperformance.
- Experienced manager and well-resourced collegiate team.
- Competitive fee structure.

Bear points

- HNE's relative performance is likely to struggle in a market led by value stocks.
- The European macroeconomic backdrop remains uncertain.
- Moderate fund size may deter some investors.

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[Edison profile page](#)

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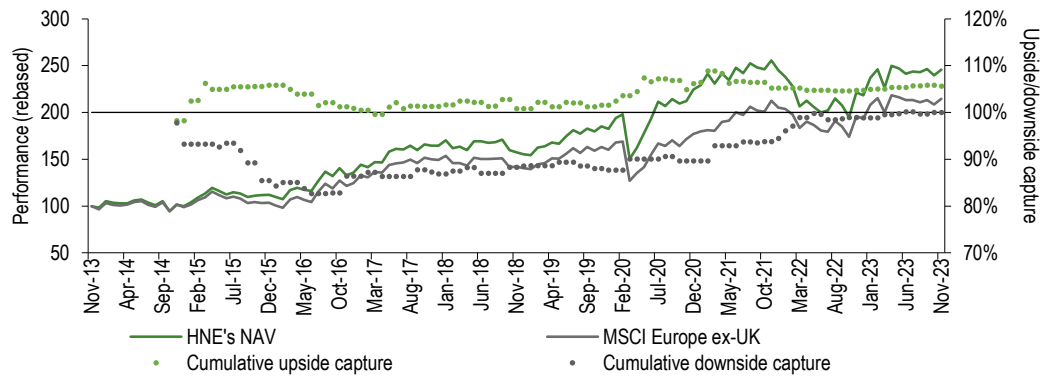
HNE: High-quality European growth exposure

HNE offers investors exposure to the European stock market via a fund of high-quality companies with either high or improving returns. Despite style headwinds, Ross has adhered to his successful investment process, selecting stocks on a bottom-up basis, and has generated a commendable performance record; the trust's NAV is ahead of its benchmark over the last one, five and 10 years.

HNE's upside/downside capture

Exhibit 1 shows HNE's upside/downside capture over the last 10 years. Its upside capture of 106% suggests that in months when European stocks rally, the trust is likely to modestly outperform the European market. However, its 100% downside capture implies that the trust is likely to perform in line with the market during months of share price weakness. The downside capture was below 100% for most of the last decade, suggesting until HNE's performance was negatively affected by style headwinds from Q121 to Q222 the trust would have outperformed during a falling market.

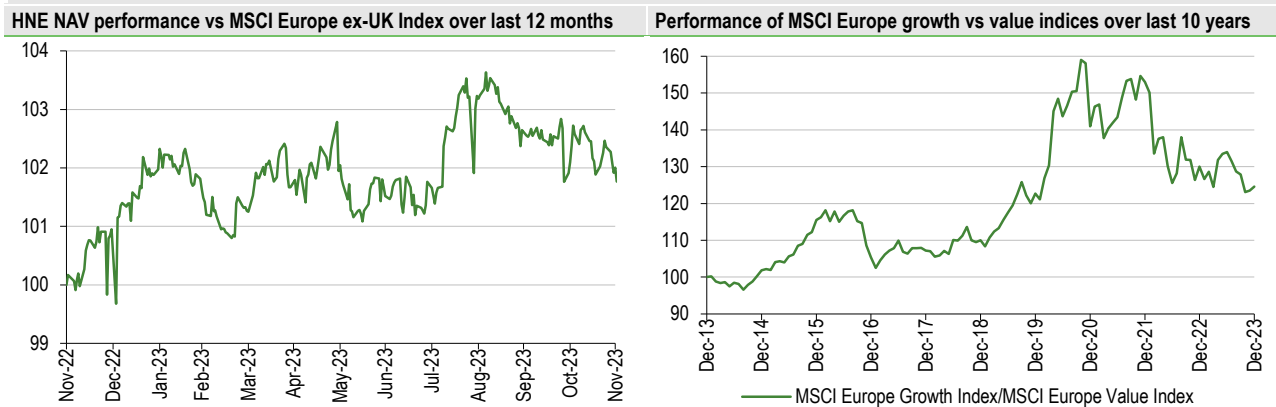
Exhibit 1: HNE's upside/downside capture



Source: Refinitiv, Edison Investment Research. Note: Cumulative upside/downside capture calculated as the geometric average NAV total return (TR) of the fund during months with positive/negative reference index TRs, divided by the geometric average reference index TR during these months. A 100% upside/downside indicates that the fund's TR was in line with the reference index's during months with positive/negative returns. Data points for the initial 12 months have been omitted in the exhibit due to the limited number of observations used to calculate the cumulative upside/downside capture ratios.

HNE's short-term and MSCI European indices' long-term performance

Exhibit 2: Relative performance of HNE's NAV and MSCI European indices



Source: Refinitiv, Edison Investment Research

Over the last 12 months, HNE's NAV has been ahead of the Europe ex-UK market despite a style headwind (Exhibit 2, left-hand side). Higher interest rates, rising inflation and concern about quality

growth companies have seen investors favour cyclical stocks, which generally do not fit the manager's investment criteria. However, successful stock selection has outweighed an unfavourable investment backdrop.

Exhibit 2 (right-hand side) illustrates how growth stocks outperformed in a low interest rate environment. The manager comments that when interest rates moved from 0% to 5%, growth stocks underperformed, and it was 'a terrible place to be'. This is evidenced by HNE's underperformance between Q121 and Q222, which is highlighted on the front-page chart.

The trust's portfolio metrics

HNE's portfolio metrics compared with the benchmark are shown in Exhibit 3. Reflecting the trust's bias to quality growth stocks, its portfolio has a higher valuation in terms of price-to-book and forward P/E multiples and has a lower historical dividend yield. HNE also has a superior earnings growth outlook and generates a higher return on equity and operating margin, while it has less leverage than the benchmark.

Over the last 18 months, the manager has initiated positions in very high-quality stocks, while selling lower-quality businesses. This has increased the quality of the portfolio and raised its overall margins. New positions include Airbus (aerospace and defence), Sartorius (medical equipment and services) and Universal Music Group (media), while sales include BAWAG Group (bank), Kion (industrial engineering) and UniCredit (bank).

Exhibit 3: HNE's portfolio metrics versus the benchmark				
Weighted averages	Compounders	Improvers	HNE	Benchmark
Market cap (£bn)	112.9	43.2	94.0	81.7
Price-to-book (x)	3.6	1.4	2.6	2.0
Trailing dividend yield (%)	2.2	2.6	2.3	3.0
Forward 2024 P/E (x)	17.5	12.9	16.0	12.9
Next 12 months EPS growth (%)	12.7	8.4	11.5	9.4
Return on equity (%)	27.4	5.7	21.5	19.6
Operating margin (%)	25.1	13.5	22.0	18.3
Long-term debt to capital (%)	31.0	33.9	31.8	33.1
Number of securities	32	15	47	577
Weight (adjusted for gearing, %)	73.0	27.0		

Source: HNE. Note: At 31 July 2023.

Current portfolio breakdown

Over the 12 months to the end of October 2023, the largest changes in HNE's sector positions were an increase in healthcare (+4.1pp) with a decrease in financials (-3.9pp). The largest active weights compared with the benchmark were above-index weightings in consumer staples (+5.3pp) and healthcare (+4.2pp) with underweight positions in industrials (-4.3pp) and consumer discretionary stocks (-4.2pp). However, it should be remembered that the trust's relative positioning is a result of bottom-up stock selection.

Within consumer staples there is a new holding in Dutch brewer Heineken. The brewing industry has had to deal with cost inflation, including higher prices for barley, which is a major ingredient. In addition, Heineken has struggled in some of its important markets such as Vietnam and Nigeria, which drove a decline in its share price that allowed the manager to pay 14x earnings for a business he expects to grow at 15% per year.

In the healthcare sector, Ross initiated a position in Denmark-listed Zealand Pharma. It is a pharmaceutical business focused on research and development and licensing, with no commercial operations. The company has a series of products in various stages of development, two of which have the highest potential value – an obesity product and a drug for the treatment of the rare condition short bowel syndrome. Given HNE's long-term holding in Novo Nordisk, the manager has a particular interest Zealand's obesity product. Although it is only in Phase II trials, Ross believes

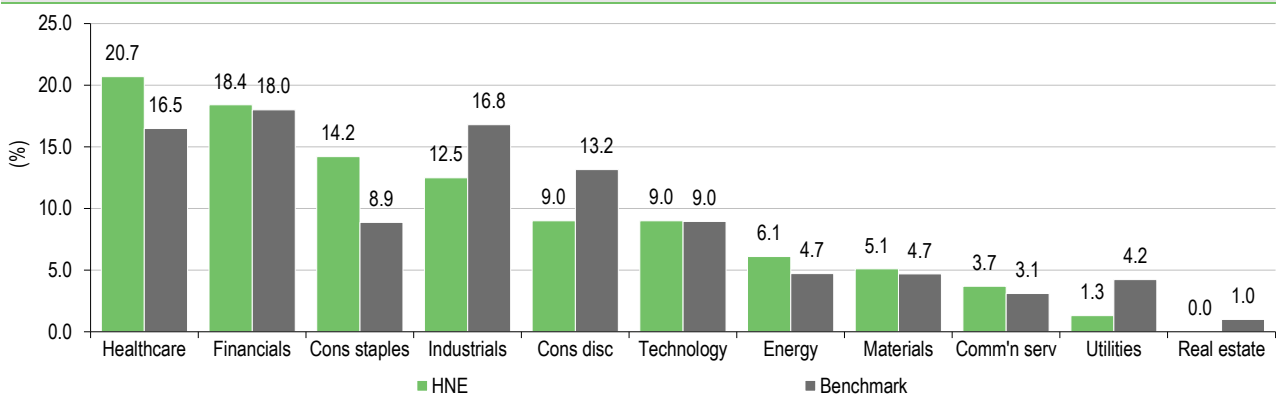
that it could fill a niche within the market for the treatment of non-alcoholic fatty liver disease (commonly known as NASH), which would set the company apart from Novo Nordisk and Eli Lilly, which are currently the market leaders in drugs to combat obesity. He considers that this product is not fully reflected in Zealand's share price.

Exhibit 4: Portfolio sector exposure versus benchmark (% unless stated)

	Portfolio end-October 2023	Portfolio end-October 2022	Change (pp)	Active weight vs index (pp)
Healthcare	20.7	16.6	4.1	4.2
Financials	18.4	22.3	(3.9)	0.4
Consumer staples	14.2	11.8	2.4	5.3
Industrials	12.5	12.4	0.1	(4.3)
Consumer discretionary	9.0	8.4	0.6	(4.2)
Technology	9.0	8.6	0.4	0.0
Energy	6.1	5.8	0.3	1.4
Materials	5.1	6.9	(1.8)	0.4
Communication services	3.7	5.1	(1.4)	0.6
Utilities	1.3	2.0	(0.6)	(2.9)
Real estate	0.0	0.0	0.0	(1.0)
Total	100.0			

Source: HNE, Edison Investment Research. Note: Numbers subject to rounding.

Exhibit 5: HNE's sector exposure versus benchmark (at 31 October 2023)



Source: HNE, Edison Investment Research. Note: Numbers subject to rounding.

Within the underweight consumer discretionary sector, HNE has an overweight exposure to luxury goods companies. The Hermès position has been in the portfolio for around seven years, and Moncler and LVMH for around five and two years, respectively. These companies have strong pricing power and high returns, having built their valuable brands over multiple decades, thereby providing high barriers to entry. However, their businesses have a level of cyclicity and Chinese economic weakness is negatively affecting current trading conditions. Despite this, Ross retains a positive outlook on the long-term prospects for the trust's luxury goods names, so is not inclined to trim these positions.

The manager has reduced HNE's prior overweight position in semiconductors down to a market weight, locking in significant profits. ASML has been in the portfolio for many years but the holdings in ASM International and BE Semiconductor were initiated within the last year to 18 months and have rallied strongly, making their valuations less attractive. Also, semiconductor stocks can move dramatically in a short space of time due to swings in investor sentiment and these companies' fundamentals may come under pressure due to the risk of further US sanctions on the sale of specific semiconductor technology to Chinese firms. Ross will look to increase the trust's semiconductor exposure when he considers it is appropriate.

The manager has been reducing HNE's bank exposure and the trust now has an underweight position versus the benchmark for the first time since the announcement of Pfizer's COVID-19

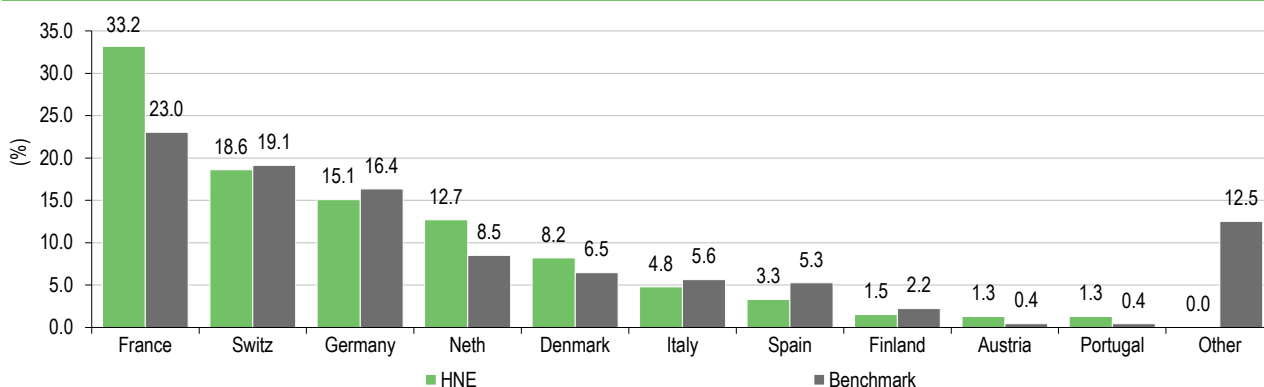
vaccine in November 2020. Ross believes that we are close to the peak in interest rates, so while banks are now benefiting from higher net interest margins, if the economy weakens, they will likely have to increase their loan-loss provisions. The manager is therefore anticipating a move from an interest-rate cycle to a credit cycle.

Exhibit 6: Portfolio geographic exposure versus benchmark (% unless stated)

	Portfolio end-October 2023	Portfolio end-October 2022	Change (pp)	Active weight vs index (pp)
France	33.2	28.8	4.4	10.2
Switzerland	18.6	18.5	0.1	(0.5)
Germany	15.1	16.7	(1.6)	(1.3)
Netherlands	12.7	13.1	(0.4)	4.2
Denmark	8.2	5.2	3.0	1.7
Italy	4.8	5.7	(0.9)	(0.8)
Spain	3.3	3.6	(0.3)	(2.0)
Finland	1.5	2.3	(0.8)	(0.7)
Austria	1.3	4.1	(2.8)	0.9
Portugal	1.3	2.0	(0.7)	0.9
Other	0.0	0.0	0.0	(12.5)
Total	100.0			

Source: HNE, Edison Investment Research. Note: Numbers subject to rounding.

Exhibit 7: HNE's geographic exposure versus benchmark (at 31 October 2023)



Source: HNE, Edison Investment Research. Note: Numbers subject to rounding.

In terms of HNE's geographic exposure, the largest changes in the 12 months to end-October 2023 were higher weightings to France (+4.4pp) and Denmark (+3.0pp) and a lower weighting to Austria (-2.8pp). Versus the benchmark, the trust's largest active weights were a 10.2pp higher weighting to France, with zero exposure to 'other' European countries, which made up 12.5pp of the index.

Exhibit 8: Top 10 holdings (at 31 October 2023)

Company	Country	Sector	Portfolio weight %	
			31 Oct 2023	31 Oct 2022*
Novo Nordisk	Denmark	Pharmaceuticals & biotech	7.1	5.2
TotalEnergies	France	Oil, gas & coal	6.1	5.8
Nestlé	Switzerland	Food producer	5.0	5.5
Roche	Switzerland	Pharmaceuticals & biotech	4.7	5.7
Sanofi	France	Pharmaceuticals & biotech	3.9	4.4
ASML	Netherlands	Technology hardware & equipment	3.2	N/A
SAP	Germany	Software & computer services	3.1	N/A
Safran	France	Aerospace & defence	3.0	N/A
LVMH Moët Hennessy Louis Vuitton	France	Personal goods	3.0	N/A
SGS	Switzerland	Industrial support services	2.9	N/A
Top 10 (% of portfolio)			42.0	46.6

Source: HNE, Edison Investment Research. Note: *N/A where not in end-October 2022 top 10.

At end-October 2023, HNE's top 10 positions made up 42.0% of the fund (Exhibit 8), which was a lower concentration compared with 46.6% a year earlier; five positions were common to both

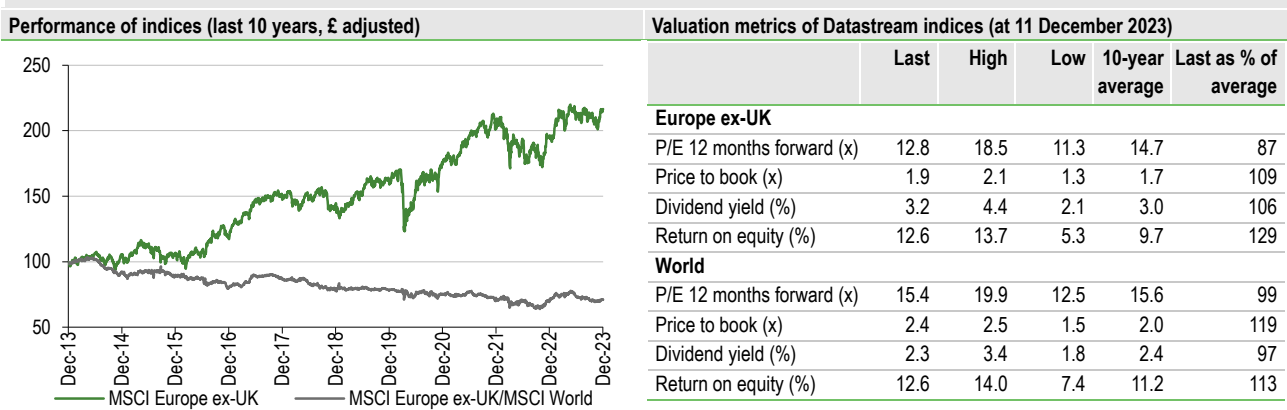
periods. Ross has been taking profits in HNE's largest position, Novo Nordisk, as the stock has performed so well, the holding had become too large from a risk perspective. The company's Wegovy weight-loss product is in very high demand for the treatment of obesity. Also, positive trial data show that the use of Wegovy can reduce adverse cardiovascular outcomes by 20%.

Market overview

According to the manager, it appears that the worst of the interest rate concerns have passed, and inflation is moderating; however, a tight labour market is supporting wage inflation. Higher interest rates are having a negative impact on economic activity. There has been increased commentary about weakening demand, especially in more cyclical areas of the market including industrials and consumer discretionary businesses. Several companies are citing China as an area of weakness, including BASF (chemicals), Siemens (broad industrial exposure) and Pernod Ricard (premium spirits), which has also experienced wholesale destocking in North America following strong post-pandemic demand growth.

European growth outlooks are relatively lacklustre – the International Monetary Fund World Outlook that was updated in October 2023 shows Euro area growth projections of 0.7% for 2023 and 1.2% for 2024. These are lower than 1.5% and 1.4% for advanced economies and 3.0% and 2.9% for world output, respectively. However, lower growth may already be reflected in European valuations. As shown in Exhibit 9 (right-hand side), using Datastream indices, on a forward P/E multiple basis, Europe ex-UK is 16.8% less expensive than the world market. In relative terms, Europe ex-UK is trading at a 13% discount to its 10-year average, which is wider than the world's 1% discount. Europe ex-UK has a more attractive price-to-book valuation and offers a higher dividend yield.

Exhibit 9: Performance of indices and valuations



Source: Refinitiv, Edison Investment Research

Performance: Benefiting from stock selection

There are seven funds in the AIC Europe sector following a range of investment mandates. HNE has the smallest market cap and has a total return mandate, focusing on quality growth companies rather than those at the high growth or value ends of the style spectrum. Stabemate Henderson European Focus Trust also has a total return mandate but is growth/value style agnostic. Fidelity European Trust seeks to generate long-term growth in capital and income. The four other companies have capital growth mandates: Baillie Gifford European Growth can invest in both private and listed companies; BlackRock Greater Europe has a broad remit and can invest in emerging European markets, although currently all the fund is invested in developed markets; European Opportunities Trust invests taking top-down factors into consideration; and JP Morgan European Growth & Income seeks capital growth and a rising share price, but also pays dividends based on its quarterly NAV.

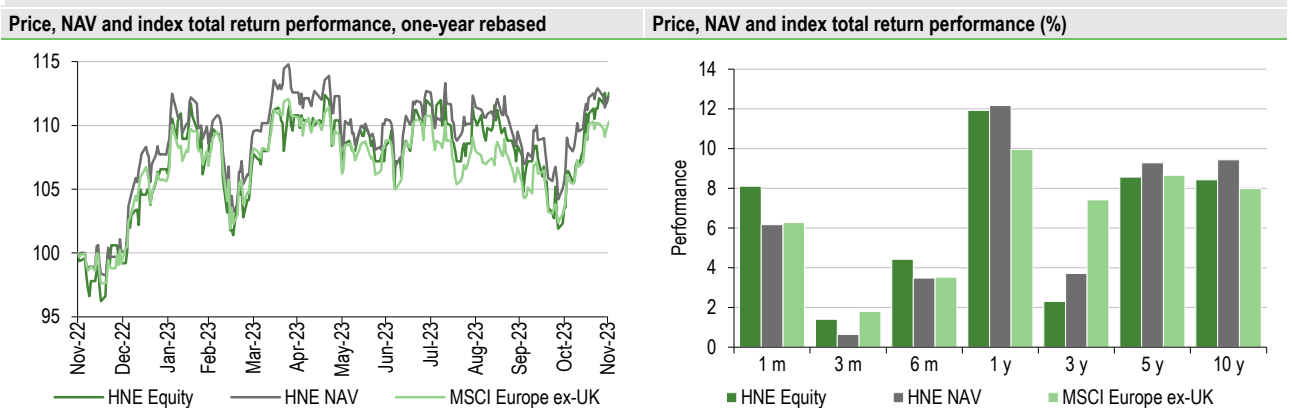
HNE's relative NAV total return performance has improved in recent months as it now ranks third over one year compared with fourth when our last review was published in [July 2023](#). The trust ranks sixth over the last three years and has above-average returns over the last five and 10 years, ranking fifth and fourth respectively. Despite its relative performance HNE has one of the widest discounts in a sector where no funds are trading at a premium. Its ongoing charge is in line with the mean, and along with all its peers, no performance fee is payable. The trust has a lower-than-average level of net gearing, and has an above-average dividend yield, which is 80bp above the mean. HNE ranks second, surpassed only by JPMorgan European Growth & Income with its NAV-based distribution policy.

Exhibit 10: AIC Europe peer group at 11 December 2023*

% 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
Henderson EuroTrust	291.3	14.9	11.3	60.6	152.6	(13.9)	0.8	No	105	2.8
Baillie Gifford European Growth	318.6	5.7	(24.3)	20.9	53.8	(14.5)	0.6	No	113	0.4
BlackRock Greater Europe	540.4	16.3	14.0	81.1	180.3	(7.0)	1.0	No	107	1.3
European Opportunities Trust	817.6	11.7	18.3	28.3	137.0	(8.6)	1.0	No	100	0.4
Fidelity European Trust	1,434.6	14.3	35.2	76.6	185.3	(6.9)	0.8	No	113	2.2
Henderson European Focus Trust	357.5	19.9	30.9	75.3	164.6	(12.3)	0.8	No	104	2.6
JPMorgan European Growth & Inc	409.2	14.0	34.8	63.0	134.1	(11.4)	0.7	No	105	4.4
Simple average	595.6	13.8	17.2	58.0	144.0	(10.7)	0.8		107	2.0
HNE rank in sector (7 funds)	7	3	6	5	4	6	5		5	2

Source: Morningstar, Edison Investment Research. Note: *Performance to 11 December 2023 based on ex-par NAV. TR, total return. Net gearing is total assets less cash and equivalents as a percentage of net assets.

Exhibit 11: HNE performance to 30 November 2023



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

Exhibit 12: Five-year discrete performance data

12 months ending	Share price (%)	NAV (%)	MSCI Europe ex-UK (%)	MSCI World (%)	CBOE UK All Cos (%)
30/11/19	16.8	16.8	14.1	13.6	11.3
30/11/20	20.6	19.6	7.1	11.5	(11.2)
30/11/21	7.0	8.9	15.5	23.4	17.1
30/11/22	(10.6)	(8.7)	(2.4)	(0.5)	7.9
30/11/23	11.9	12.2	10.0	6.8	1.5

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

Despite the difficult performance period between Q121 and Q222, when investors favoured value rather than growth stocks, HNE has a respectable relative performance record (Exhibit 13) as its NAV total returns are now ahead of the European ex-UK market over the last one, five and 10 years. The performance of the world market has been boosted by the dominant US market (70% of the MSCI World Index) that has outperformed for much of the last decade (the US S&P 500 Index has outpaced the MSCI World Index, in US dollar terms, for nine out of the last 10 years). HNE is noticeably ahead of the UK market over the last one, five and 10 years.

Exhibit 13: HNE share price and NAV total return performance, relative to regional and global indices (%)

	One month	Three months	Six months	One year	Three years	Five years	10 years
Price relative to MSCI Europe ex-UK	1.7	(0.4)	0.9	1.8	(13.6)	(0.4)	4.2
NAV relative to MSCI Europe ex-UK	(0.1)	(1.1)	0.0	2.0	(10.0)	2.9	14.2
Price relative to MSCI World	3.1	(0.4)	(2.1)	4.8	(18.4)	(9.3)	(25.9)
NAV relative to MSCI World	1.2	(1.2)	(3.0)	5.0	(15.0)	(6.3)	(18.8)
Price relative to CBOE UK All Companies	5.3	0.9	2.9	10.3	(16.5)	19.0	37.0
NAV relative to CBOE UK All Companies	3.4	0.1	1.9	10.5	(13.0)	23.0	50.2

Source: Refinitiv, Edison Investment Research. Note: Data to end-November 2023. Geometric calculation.

Looking back to the trust's FY23 results (ending 31 July), its NAV and share price total returns of +16.7% and +19.7%, respectively, were ahead of the benchmark's +16.1% and the AIC Europe sector's +14.6% total returns. The largest contributors to the trust's returns were: UniCredit (+2.8pp), Munich Re (+1.5pp) and Hermès (+0.8pp). On the negative side, the largest detractors were: Koninklijke DSM (prior to the merger with Firmenich, -1.6pp), EDP Renováveis (-1.0pp) and Cellnex (-0.9pp).

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