**Unit 9: Investment Trusts**

<https://quizlet.com/gb/892642247/unit-9-investment-trusts-flash-cards/?i=24ef59&x=1qqt>

**How are investment trusts set up?**

PLCs

**Investment trusts: Choice**

400 Trusts.

All with different focus: e.g. UK Equities.

**Risk of close-ended structure**

Increases risk- more uncertainty in value of investment

Even if fund is doing well, may not always be reflected in share price.

**Investment trusts: Finding value**

May be able to find a bargain where share price of trust is less than NAV.

**Investment trusts:**  **Gearing**

Can borrow in same way as normal PLC.

Potentially riskier than Unit Trusts/OEICs.

**Investment trusts: Trading at a Premium**

Share Price > NAV.

Share Price 5.20. NAV £4.90.

**Investment trusts: Trading at a Discount.**

Share Price < NAV.

Share Price. £3.50. NAV £5.00

**Why is there a discrepancy between investment trust price and NAV?**

Market sentiment on trust, its area of focus, MGMT.

**Investment trusts: Narrowing the Discount.**

Share price increases as investors take advantage of discount.

Price discrepancy decreases.

**Calculating the Discount/ Premium as a %.**

Price differential / NAV \* 100.

NAV £5. Share price £4.

1/5 \* 100 = 20%.

**Warrants**

Right to Buy shares at a fixed price at a certain date / within a set time period.

**Warrants: SD/SDRT**

None.

Warrant itself it just an agreement.

**Warrants: Income tax**

None as don’t produce an income.

Just a right to buy in future.

**Warrants: CGT**

Yes if sold warrant for a profit.

**Impact of warrants being exercised**

More money enters investment trust.

Number of shares increases.

**When are warrants typically exercised?**

When fixed price is less than trading price.

**Undiluted NAV**

Ignores warrants.

Normal Calc.

**Diluted NAV**

Includes impact of warrants.

More shares in issue.

**Diluted NAV Formula**

(Fund value + warrant value) / (number of shares + number of warrants)

**How can investment trusts borrow/ gear?**

Loans

Corporate bonds

Preference shares

**Gearing Ratio**

Gross Assets/ Net Assets \* 100

100 = No Gearing

**Two types of Investment Trusts**

Conventional & Split Capital

**Conventional Investment Trust**

No end date.

Fixed number of shares.

**Split Capital Investment Trust**

Set time period – 5/10 years.

Zero Dividend Preference Shares (Zeros) & Ordinary shares

**Zero Dividend Preference Shares (Zeros)**

Pre-determined level of Capital growth but no income.

Ahead in queue of ordinary shares.

Viewed as low risk

**Ordinary Shares**

All income & any capital growth left over when Zeros have been paid.

Viewed as riskier but higher dividend than normal shares as income is only shared amongst this share class.

**Capital only shares**

Rare.

Only pays out if capital left when ordinary shareholders have been paid.

**Hurdle Rate**

Annual rate of growth for ‘zeros’ to meet their capital target and ordinary shares to get their money back.

**Negative Hurdle Rate**

Good news.

More than sufficient assets to meet its obligations.

**Investment Trusts Tax**

Same as normal equities.

Treated as Dividend Income.

Normal CGT.

**Investment Trusts: ISAs**

No Income tax/ CGT

APS applies for IHT.

**REIT: What type of properties?**

Commercial or Residential

Not owner occupied units.

**REIT Sources of Income**

Rent

Property MGMT (Secondary)

**REIT Corporation Tax**

Profits exempt from corporation tax.

**REIT Liquidity**

As Investment trusts are on stock market, fund manager cant suspend trading.

**REIT Gearing**

125% coverage Ratio

**REIT Criteria**

75% of profits & assets from property letting business.

Must distribute 90% taxable income to shareholders.

**REIT Taxation Overview**

Tax is different based on whether the income is from rent (main business) or from secondary business (property MGMT).

**REIT Taxation: Rental Income**

Property Income Distribution ( PID)

Non-savings Income – can’t use DA/PSA.

Paid net of basic tax.

**REIT Taxation: Rental Income – what do pay HMRC?**

Paid net of basic tax.

Basic rate owe no more.

Higher rate owe HMRC an extra 20/25%.

Non-taxpayers can claim back.

**REIT Taxation: Secondary Income**

Normal dividend income.

Paid Gross.

Can use DA etc.

**REIT: CGT**

Normal CGT rules – annual exempt amount etc.

Surcharge on property doesn’t count as don’t directly own property.

**Property Authorised Investment Fund (PAIF)**

Near identical to REIT.

However, legally set up as an OEIC.

**Property Authorised Investment Fund (PAIF): Criteria**

60% of net income and assets must come from property investment.

**Investment Trusts: Pros/ Cons**

Generally lower fees/ costs

But riskier due to closed structure

More Complex.