Investment Trusts should revel in their own distinctiveness
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Some market commentators, and indeed some Wealth Managers and IFAs, try and make investment trusts look like open-ended funds. They are not; their additional characteristics make investment trusts one of the best ways for retail investors to invest in the equity market.

Many investment trusts have long and distinguished histories with the oldest going back as far as 1868. This formula, which has served generations of investors so well, led investment trusts to be called the City's best kept secret. Indeed, I remember the late great Philip Chappell, who was Director of the Association of Investment Trust Companies some 25 years ago, saying that it was an unkind jibe yet true that City experts put their clients into better marketed competing products whilst investing in investment trusts themselves. I believe that this unkind jibe remains true today.

There is good reason for these City experts to put their own money in investment trusts as research produced by the perceptive analyst Alan Brierley at Canaccord Genuity consistently shows that, on average, investment trusts outperform open ended funds in more sectors than vice versa.

Base=100	1 Year		5 Year		10 Year	
Sectors	Investment Companies	OEIC/Unit trust	Investment Companies	OEIC/Unit trust	Investment Companies	OEIC/Unit trust
Global	108.9	108.7	175.6	158.0	261.8	213.3
Global Equity Income	104.8	108.9	196.2	167.7	278.1	219.9
UK Equity Income	106.9	105.5	215.4	170.8	291.8	208.5
UK All Companies	102.0	103.3	180.9	166.1	224.5	211.8
North American	111.8	118.0	197.4	198.7	243.3	226.4
Europe vs. Europe ex UK	108.0	103.0	183.1	145.1	310.6	221.8
Global Emerging	102.6	106.0	126.2	124.7	310.7	294.7
Asia Pacific ex Japan	112.9	109.4	179.7	142.7	395.6	301.3
Japan	107.2	100.8	223.9	143.4	208.1	147.9

Source: Canaccord Genuity; as of February 2015

So what changes are being proposed that might take away that investment trust distinctiveness and make investment trusts more like open ended funds?

The first of these are zero discount control policies. The object of these is to use share issue and share buyback powers to ensure that the Trust's share price trades at or around the net asset value. The key benefit is improved liquidity for both buyers and sellers and the knowledge that the shares will not drift out to a wide discount or premium. This is fine and dandy, but if that is your worry as an investor then buy a single-priced open ended fund and do not seek to undermine one of the key attractions of the investment trust structure.

Being closed-ended enables the portfolio manager to take a longer term view of investment without having to worry about a redemption stream. Portfolio Managers of open-ended funds have to consider holding cash to fund redemption streams or else accept that they will have to sell stock to do so. In a market crash situation, or indeed a simple rapidly falling market, this may prove difficult to do and the Portfolio Manager may be forced to sell those stocks he can, rather than those he wants to sell, in order to satisfy the redemption stream.

Of course zero discount control policies come from a concern about the discount and premiums at which investment trust shares trade to their net asset value. Investment trust investments are medium to long term investments with typical holding periods of five years or more. Over that time period the difference between the buy discount and the sell discount is likely to be a tiny proportion of the return on the investment.

The second way in which investment trusts are being pushed into being open-ended is management fees. The standard fee for the “clean” share class of an equity open-ended fund is 0.75% and some commentators are saying investment trusts should scrap their performance fees and fall into line. Well, some have, and often at base fee levels much lower than 0.75% but the majority are sticking with their performance fee structures. In my view they are right to do so: paying lower management fees when performance is poor and higher fees when performance is good seems to me to be an attractive formula.

There are other distinctive features of investment trusts that fortunately have not yet come under the spotlight, such as oversight by their independent board of directors or investment trusts’ ability to gear the portfolio by borrowing money with the objective of enhancing returns for shareholders. This has proved an invaluable capital and income enhancing strategy for well managed investment trusts.