Client: NewRiver Retail
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Five cheap investment trusts

When sentiment is dire, investment trust discounts can become overly stretched. We screen for the five cheapest investment trusts

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Investment trusts offer many attractions, but for those with an enduring love of the sector it is often the opportunity to buy assets at less than their market value that is most alluring. Discounts have a tendency to widen when markets are volatile, then tighten when things calm down – so there are often bargains to be had during turbulent periods.

There are many explanations for why shares in investment trusts often trade at a discount to net asset value (NAV), which is derived from the value of the underlying investment portfolios. There is even an argument that the added risk that a discount itself represents means investment trusts should be valued at a discount to offset this. Fancy theories aside, though, ultimately the price that a trust trades at relative to its portfolio is an issue of supply and demand.

Such a strategy is risky, of course – a discount is the market's way of saying that it expects the value of the trust's portfolio to fall, and you'd be foolish to ignore that message altogether. However, if you can see beyond the eurozone's woes or the US fiscal impasse, or think that another dose of monetary stimulus is a dead cert, the following list of investment trusts should be of interest.

These are the 15 trusts that broker Numis Securities calculates have the highest Z-score, which is a measure of cheapness based on the discount range they have traded in over the past year, and discount volatility. Below, we take a closer look at the five 'cheapest' at the time of writing (please note we have updated our data prior to publication, so the order of trusts has changed slightly in the table).

With all the worries about the possibility of a hard landing in China, it's not surprising to see an investor in Asia up among the cheapest trusts on the market. And **Pacific Alliance Asia Opportunity**, the master fund to which the investment trust offers exposure, invests in risky assets that the managers have deemed to be valued at less than their true worth. This includes distressed debt, secondary issues of private equity and special situations. The trust, which has a market capitalisation of £87m and gross assets of £122m, is classed as an absolute return fund. While NAV has only dropped 2 per cent in the year to date compared with a near 17 per cent average fall for all Asia Pacific funds, the market seems sceptical about the trust's ability to keep this up, as the shares are down by almost 16 per cent, despite a good NAV performance during the credit crunch (when the discount also widened).

The eurozone is the real crucible of the world's economic concerns at the moment. A Greek default has the potential to trigger a new credit crisis as banks are forced to write off debt and revalue the debt of similarly challenged (and larger) economies. As well as investing in the region, the **Standard Life European Private Equity fund**, which has a market capitalisation of £212m and gross assets of £442m, has the added spectre of private equity exposure. This is a particularly cyclical asset class. Furthermore, the Standard Life trust is a fund of funds, so discounts on its underlying holdings will widen as their underlying NAVs fall, compounding the trust's own discount. However, that also means major upside if a credible fix to the eurozone's problems can be found.

Mithras is a private equity fund of funds in wind-up mode. At the start of 2009 it pledged to make no new commitments to invest in funds and to start selling up and returning cash to shareholders. You could be forgiven for thinking that the discount represents a steal. However, private equity holdings can be difficult to monetise; particularly worrying now as the private equity market has started to slow down. But, if the market turns, the discount could turn out to have been a bargain.

SVG investment trust invests alongside the Primera private equity group by taking stakes

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in its buyout funds. It was one of the most distressed private equity funds during the credit crunch due to the high level of investment commitments made and debt taken on. However, much has been done to put the trust on a more stable footing and its shares have enjoyed a stunning recovery from their lows of 73p in 2009, although the price is still some way off the 2007 high of 944p. But concerns about the economy have inevitably brought back memories of its brush with disaster.

NewRiver Retail was set up to take advantage of faltering UK commercial property prices. Its experienced team has been buying into shopping centres with the aim of pepping them up and increasing their value. However, with real disposable incomes under pressure, the outlook is tough. Management has focused on food and value retailers as tenants, which should help performance during what is expected to be a very tough Christmas and 2012. If the trust can prove itself during these times, the rewards could be good for the brave.

The favourite 15

Fund	TIDM	Price	Discount (%)	Average discount (%)	Z-score	1-yr performance (%)*
Pacific Alliance Asia Opportunity	PAX	100¢	-25.4	-13.9	-3.3	-4.9
NewRiver Retail	NRR	229p	-16.1	-5.2	-3.2	-10.2
Better Capital	BCAP	112p	10.6	16.1	-3.0	0.9
Picton Property Trust	PCTN	41p	-32.0	-17.8	-3.0	-13.3
Standard Life Euro Private Equity	SEP	134p	-43.1	-28.2	-3.0	17.3
Mithras Investment Trust	MTH	99p	-33.4	-25.2	-2.9	-9.6
ARC Capital	ARCH	72¢	-43.0	-21.7	-2.9	-37.0
Pantheon International Participations	PIN	613p	-45.2	-32.2	-2.9	4.8
Dunedin Enterprise	DNE	280p	-46.7	-33.6	-2.9	-3.0
SVG Capital	SVI	207p	-46.7	-28.0	-2.8	22.5
Origo Partners	OPP	31p	-31.7	8.1	-2.7	6.8
Sirius Real Estate	SRE	€0.24	-67.1	-53.2	-2.7	-27.7
PME African Infrastructure	PMEA	25¢	-53.7	-37.6	-2.7	-47.0
Aberdeen Private Equity	APEF	58p	-39.3	-24.8	-2.7	-13.4
Pacific Alliance China Land	PACL	111¢	-42.4	-28.3	-2.6	11.5

*Currency adjusted share price performance. Source: Numis Securities & Thomson Datastream

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