Liontrust Diversified Real Assets Fund – July 2023 review

- **Core property holdings deliver strongest contribution to performance, supported by cyclical real assets and diversifiers**
- **Speciality REITs stage turnaround but renewable and social infrastructure weigh**
- **Investors with a medium- to long-term horizon can benefit from a higher starting income yield and a potential normalisation in discounts**

Over the month to 31 July 2023, the Diversified Real Assets Fund (the 'Fund') returned 0.87%, (Class A accumulation share class, net of fees).[1]

Our core property holdings, which include speciality real estate investment trusts (REITs,) made the strongest contribution to our positive performance over the month, supported by cyclical real assets and diversifiers. Core infrastructure, which is the fourth of the key building blocks in the Fund, weighed on performance, however.

Speciality REITs have been significantly impacted by rising interest rates as central banks expedited aggressive monetary tightening to combat soaring inflation from 2022 onwards. But July saw them stage a turnaround, with Supermarket Income, Assura, Tritax Big Box and LXI REIT making the best contribution to performance of any of our holdings. Global property equity was also a significant contributor through Segro and Digital Realty Trust, and iShares Physical Gold in our diversifiers exposure was also a notable positive.

The renewable and social infrastructure stocks in our core infrastructure exposure delivered the poorest performance, however, including VH Global Sustainable Energy Opportunities, Cordiant Digital Infrastructure, HICL Infrastructure and GCP Infrastructure Investment.

Outlook

Over the last 12 months we have seen some of the widest discounts in the real asset investment trust market since the Global Financial Crisis. The average current discounts of share prices relative to their Net Asset Valuations (NAVs) are in the double-digit territory, while historically these have traded at double-digit premiums to NAVs.

In the absence of fundamental concerns, we believe the magnitude of the discounts may be overdone and an investor with a medium- to long-term horizon can benefit from strong prospective returns through a higher starting income yield and a potential normalisation in discounts. The Fund's dividend yield is 5.7%[2] as of 31 July 2023.

Falling interest rate expectations are one catalyst for a strong re-rating, but we believe even if rates were to stabilise at current levels, the discounts and cheapness of the sector will encourage buyers back into the market, especially as fundamentals remain robust. Using history as our guide, we note periods of high persistent discounts are often followed by very attractive prospective returns from the higher starting yields and the unwinding of the discounts.

Furthermore, discounts also entice external bids for these companies by well capitalised players which can lead to a buy-out price at close to NAV (book value of the portfolio) or at a meaningful premium to current market prices. We have already seen this spur acquisitions of REITs, where deep discounts have enticed bids led by private market participants.

Rapidly rising interest rates have caused a painful re-pricing in our income sensitive names, however, we are beginning to see encouraging signs on slowing inflation, alongside an easing of supply chains and a normalisation in pent up demand via declining savings rates. This makes us confident that most of the pain may be behind us in terms of interest rates. Equally, investors should not disregard the risks of a recession as the full effect of a tight monetary policy feeds into companies, the economy and equity markets, which have so far been resilient.

For real assets, however, a cheap starting valuation point and defensive cashflow profile can act as a good source of diversification and returns for investors over the long-term.

(1) Source: Financial Express, as at 31 July 2023

(2) Source: Liontrust/Bloomberg, as at 31 July 2023

For more insights and views from Liontrust visit: https://www.liontrust.co.uk/insights/ourinsights

For a comprehensive list of common financial words and terms, see our glossary at: https://www.liontrust.co.uk/glossary

Key Risks
Past performance does not predict future returns. You may get back less than you originally invested.

We recommend this fund is held long term (minimum period of 5 years). We recommend that you hold this fund as part of a diversified portfolio of investments.

The Fund invests at least 80% of its net asset value in a diversified portfolio of real assets (including investments in infrastructure, renewables. commodities, inflation linked assets and specialist property).
■ The Fund will gain exposure to these real assets through investment in real estate investment trusts (REITs), investment trusts, equities, debt instruments (bonds), collective investment schemes and exchange traded instruments.
■ The Fund is currently categorised 4 primarily for its balanced exposure to higher and lower risk assets.
■ The SRRI may not fully take into account the following risks:
– that a company may fail thus reducing its value within the Fund;
– overseas investments may carry a higher currency risk. They are valued by reference to their local currency which may move up or down when compared to the currency of the Fund.
– Bonds are affected by changes in interest rates and their value and the income they generate can rise or fall as a result;
– the creditworthiness of a bond issuer may also affect that bond's value. Bonds that produce a higher level of income usually also carry greater risk as such bond issuers may have difficulty in paying their debts. The value of a bond would be significantly affected if the issuer either refused to pay or was unable to pay.
■ This Fund may have a concentrated portfolio, i.e. hold a limited number of investments or have significant sector or factor exposures. If one of these investments or sectors / factors fall in value this can have a greater impact on the Fund's value than if it held a larger number of investments across a more diversified portfolio.
■The Fund may, under certain circumstances, invest in derivatives, but it is not intended that their use will materially affect volatility. Derivatives are used to protect against currencies, credit and interest rate moves or for investment purposes. There is a risk that losses could be made on derivative positions or that the counterparties could fail to complete on transactions. The use of derivatives may create leverage or gearing resulting in potentially greater volatility or fluctuations in the net asset value of the Fund. A relatively small movement in the value of a derivative's underlying investment may have a larger impact, positive or negative,

on the value of a fund than if the underlying investment was held instead. The use of derivative contracts may help us to control Fund volatility in both up and down markets by hedging against the general market.
■ The Fund may encounter liquidity constraints from time to time. The spread between the price you buy and sell shares will reflect the less liquid nature of the underlying holdings.
■ The Fund may have both Hedged and Unhedged share classes available. The Hedged share classes use forward foreign exchange contracts to protect returns in the base currency of the Fund.
■ Outside of normal conditions, the Fund may hold higher levels of cash which may be deposited with several credit counterparties
(e.g.international banks). A credit risk arises should one or more of these counterparties be unable to return the deposited cash.
■ Counterparty Risk: any derivative contract, including FX hedging, may be at risk if the counterparty fails.
■ ESG Risk: there may be limitations to the availability, completeness or accuracy of ESG information from third-party providers, or inconsistencies in the consideration of ESG factors across different third party data providers, given the evolving nature of ESG.

The issue of units/shares in Liontrust Funds may be subject to an initial charge, which will have an impact on the realisable value of the investment, particularly in the short term. Investments should always be considered as long term.