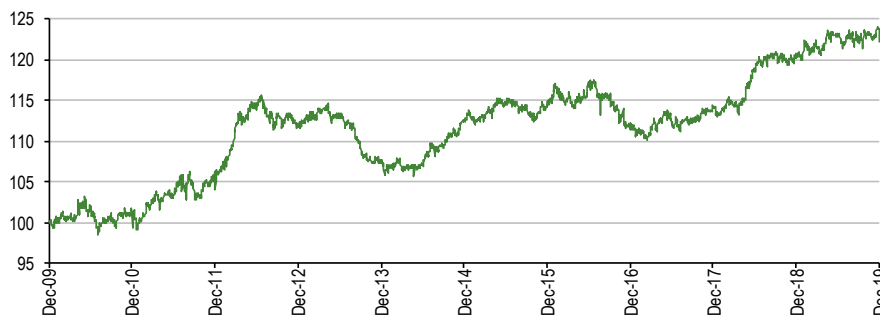


Fidelity European Values

Disciplined process driving outperformance

Fidelity European Values (FEV) is managed by Sam Morse, who selects stocks on a bottom-up basis, focusing on quality companies with strong balance sheets that are able to grow dividends over the long term. He notes that investor concerns that affected the market in 2019 are abating: central banks are very supportive; a resolution to the US-China trade war is looking more likely; and within Europe, there is the prospect of fiscal stimulus to support economic growth. While there is potential for a rotation in market leadership towards cyclical stocks, which could put the fund's relative performance under pressure, the manager is 'sticking to his knitting', and remaining disciplined, rather than shifting his portfolio exposures in an effort to try to 'time the market'.

Long-term NAV outperformance versus the benchmark



Source: Refinitiv, Edison Investment Research

The market opportunity

While improved investor sentiment drove a re-rating of the European market in 2019, central banks remain very accommodative and there is potential for fiscal stimulus to support economic growth. These factors may lead to further upward moves in equity prices in 2020, despite above-average total returns last year.

Why consider investing in FEV?

- Strong performance track record – the trust has outperformed the benchmark over the last one, three, five and 10 years.
- Experienced fund manager, with a disciplined investment approach, who is able to draw on the broad resources of Fidelity's analyst team.
- Long-term record of dividend growth, supported by a focus on well-financed companies that can grow their own dividends.

Discount narrower than historical averages

FEV's shares are currently trading at a 7.1% discount to cum-income NAV, which is narrower than the average discounts of 8.4%, 9.3%, 9.0% and 10.8% over the last one, three, five and 10 years, respectively. The trust pays dividends twice a year in November and May; the annual ordinary payment has increased in each financial year since 2010 and FEV currently offers a 3.3% yield. Gearing of up to 30% of NAV is permitted; net market gearing was 3.8% at end-November 2019.

Investment trusts European equities

16 January 2020

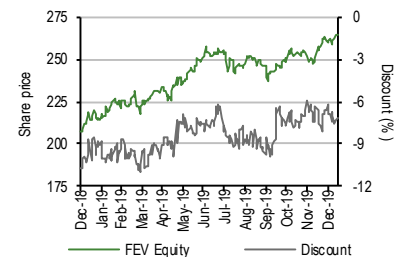
Price 265.0p
Market cap £1,090m
AUM £1,178m

NAV* 285.3p
Discount to NAV 7.1%

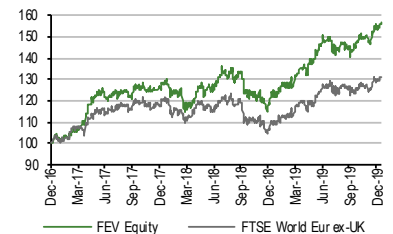
*Including income. As at 14 January 2020.

Yield 3.3%
Ordinary shares in issue 411.5m
Code FEV
Primary exchange LSE
AIC sector Europe
Benchmark FTSE World Europe ex-UK

Share price/discount performance



Three-year performance vs index



52-week high/low 265.0p 214.0p
NAV** high/low 285.3p 235.3p

**Including income.

Gearing

Gross market gearing* 6.5%
Net market gearing* 3.8%

*As at 30 November 2019.

Analysts

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[Edison profile page](#)

Fidelity European Values is a research client of Edison Investment Research Limited

Exhibit 1: Trust at a glance

Investment objective and fund background

Fidelity European Values' investment objective is to achieve long-term growth in both capital and income from a portfolio predominantly comprising continental European securities. Up to 20% exposure to stocks listed outside continental Europe is permitted, to give the manager investment flexibility. FEV's performance benchmark is the FTSE World Europe ex-UK Index.

Recent developments

- 11 November 2019: Appointment of Sir Ivan Rogers as a non-executive director with effect from 1 January 2020.
- 2 August 2019: Interim results to 30 June 2019 – NAV TR +19.9% versus benchmark TR +17.5%; share price TR +24.5%.
- 13 May 2019: Two-yearly continuation vote passed at the AGM.

Forthcoming

AGM	May 2020
Final results	March 2020
Year end	31 December

Capital structure

Ongoing charges	0.88%
Net market gearing*	3.8%
Annual mgmt fee	Tiered: 0.85% up to £400m net assets, then 0.75%.
Performance fee	None
Trust life	Indefinite (subject to vote)
Loan facilities	None – CFDs used

Fund details

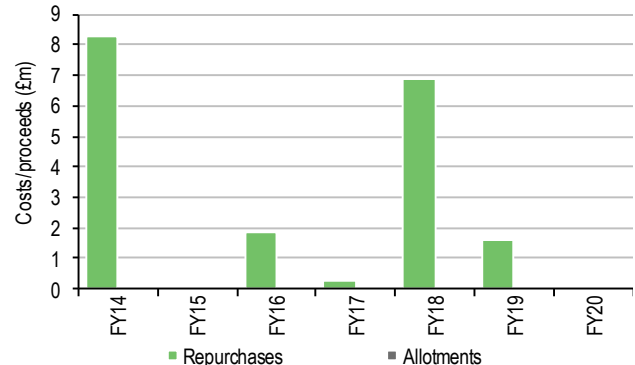
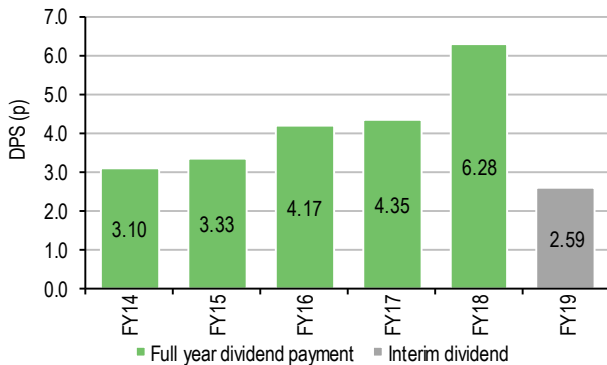
Group	FIL Investments International
Manager	Sam Morse
Address	Beech Gate, Millfield Lane, Lower Kingswood, Tadworth, Surrey KT20 6RP
Phone	+44 (0)800 414110
Website	www.fidelity.co.uk/europeanvalues

Dividend policy and history (financial years)

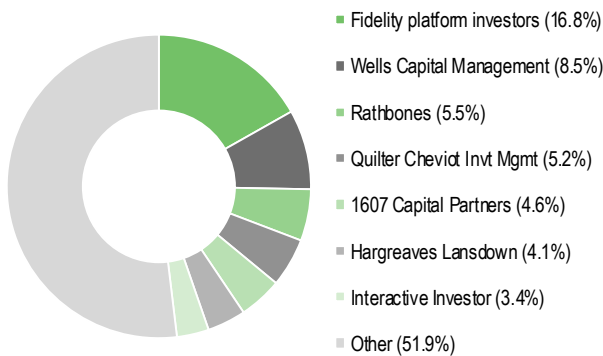
Until FY18, FEV paid an annual dividend in May. From FY19, an interim dividend is also paid in November. FY18 distributable income rose partly due to the shift to a 75:25 allocation of fees and expenses between capital and revenue.

Share buyback policy and history (financial years)

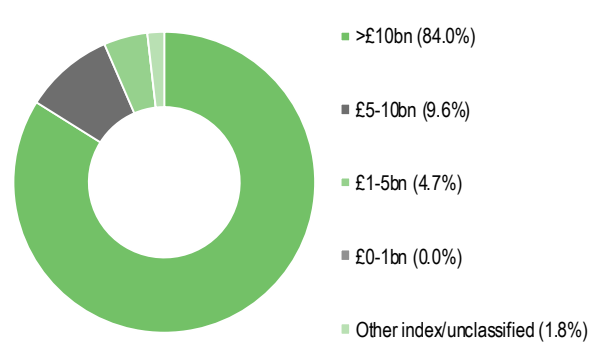
FEV has annually renewed authority to purchase up to 14.99% and allot up to 5% of its issued share capital.



Shareholder base (as at 31 December 2019)



Portfolio exposure by market cap (as at 30 November 2019)



Top 10 holdings (as at 30 November 2019)

Company	Country of listing	Sector	Portfolio weight (%)		Benchmark weight (%)	Active weight (pp)
			30 Nov 2019	30 Nov 2018**	30 Nov 2019	30 Nov 2019
Nestlé	Switzerland	Consumer goods	6.9	7.1	4.4	2.5
Roche Holding	Switzerland	Healthcare	5.3	5.3	3.2	2.1
SAP	Germany	Technology	4.4	3.8	1.9	2.5
LVMH	France	Consumer goods	4.2	N/A	1.6	2.6
Total	France	Oil & gas	4.0	4.3	1.8	2.2
ASML Holding	Netherlands	Technology	3.5	3.2	1.6	1.9
Sanofi	France	Healthcare	3.5	4.3	1.5	2.0
L'Oréal	France	Consumer goods	3.2	3.4	1.0	2.2
EssilorLuxottica	France	Healthcare	3.0	N/A	0.7	2.3
Novo Nordisk	Denmark	Healthcare	2.9	3.1	1.3	1.6
Top 10 (% of holdings)			40.9	40.5		

Source: Fidelity European Values, Edison Investment Research, Bloomberg, Morningstar. Note: *Gearing net of short positions. **N/A where not in end-November 2018 top 10.

The fund manager: Sam Morse

The manager's view: Continued focus on individual companies

Morse comments that despite stock market volatility in 2019, FEV outperformed its benchmark during the year, which is gratifying. However, he says that there were some tricky periods, such as in Q2 and Q3, when there was short-term rotation into value stocks, where the trust is underweight (FEV has a growth bias due to its focus on investing in companies that can consistently grow their dividends). Over 2019 as a whole, the manager enjoyed a stylistic tailwind as good dividend payers outperformed and defensive stocks fared better than cyclical names. At the margin, Morse has been reducing the fund's defensive exposure, taking profits in stocks that have performed relatively well, such as 3i Group, ASML, Dassault Systèmes, Deutsche Börse and EssilorLuxottica. He has been reallocating the proceeds into companies that have done less well, such as in the energy and industrial sectors.

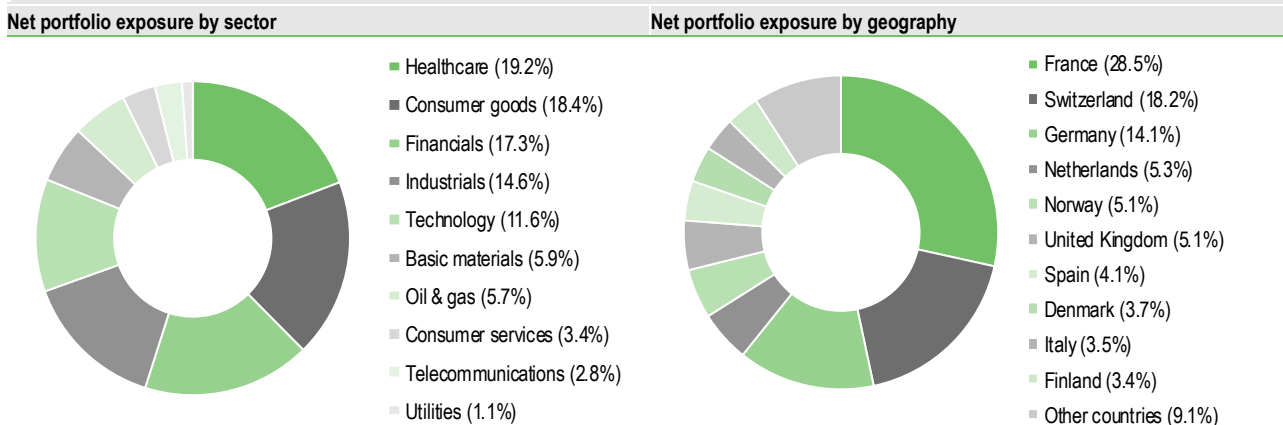
At the beginning of 2019, there was concern about the outlook for European equities given an expected low level of earnings growth. However, sentiment improved as central banks moved to stimulate their respective economies: the US Federal Reserve shifted its stance from raising to reducing interest rates and the European Central Bank (ECB) restarted quantitative easing. This has proved to be a powerful feature for global markets, outweighing concerns about the dispute between the US and its trading partners and the ongoing Brexit negotiations. Improved investor sentiment led to a re-rating of equities and investors enjoyed above-average returns in 2019.

Consensus earnings growth for European equities in 2020 is currently in the mid-single digit range; however, Morse says that this is likely to be dependent on fiscal stimulus, as there is not much more the ECB can do in terms of monetary policy. The bank has been very vocal in encouraging fiscal stimulus at the national level, but the manager suggests that apart from direct tax cuts, it would very difficult to see a rapid positive impact from changing fiscal policies. He is conscious that the current bull run since the global financial crisis is prolonged and he will continue to focus on what individual companies are doing, rather than significantly repositioning FEV's portfolio and trying to 'time the market'.

The portfolio

At end-November 2019, FEV's top 10 holdings made up 40.9% of the portfolio, which was broadly in line with 40.5% a year earlier; eight positions were common to both periods.

Exhibit 2: FEV's net portfolio exposure by sector and geography at end-November 2019



Source: FEV, Edison Investment Research. Note: Exposures are net of short positions, adjusted for gearing and index futures.

The make-up of the fund is broadly similar to end-May 2019, which we covered in our last [note](#) published in June; FEV continues to be diversified by both sector and geography (Exhibit 2).

Portfolio activity has been relatively light, with two new holdings and no complete disposals over the last six months. Morse is not 'super positive' on the outlook for European equities and has not been finding many new attractive investment opportunities. He is mindful about the continued outperformance of steady growth companies, given that they have been in favour with investors, and notes that valuations are stretched, although he does not anticipate an imminent market correction. FEV's portfolio turnover in 2019 was around 10% versus a more typical 20–30% a year. The trust has an active share of 79% (a measure of how a fund differs from an index, with 0% representing full replication and 100% no commonality).

The two new holdings are both private equity firms, operating in a sector that is enjoying positive fundamentals and investor inflows. Partners Group is listed in Switzerland. Its shares dipped in September as the company's margins came under short-term pressure, which provided Morse with an attractive entry point. He is expecting Partners to generate double-digit dividend growth. EQT is a Swedish company that listed last September; its shares were in high demand, so FEV only received a small allocation. As the company has continued to perform well following the initial public offering, the manager will either wait for a pull back to increase the position size, or he may sell the holding as it is currently too small to make a meaningful impact on the fund's performance.

Performance: Long-term record of outperformance

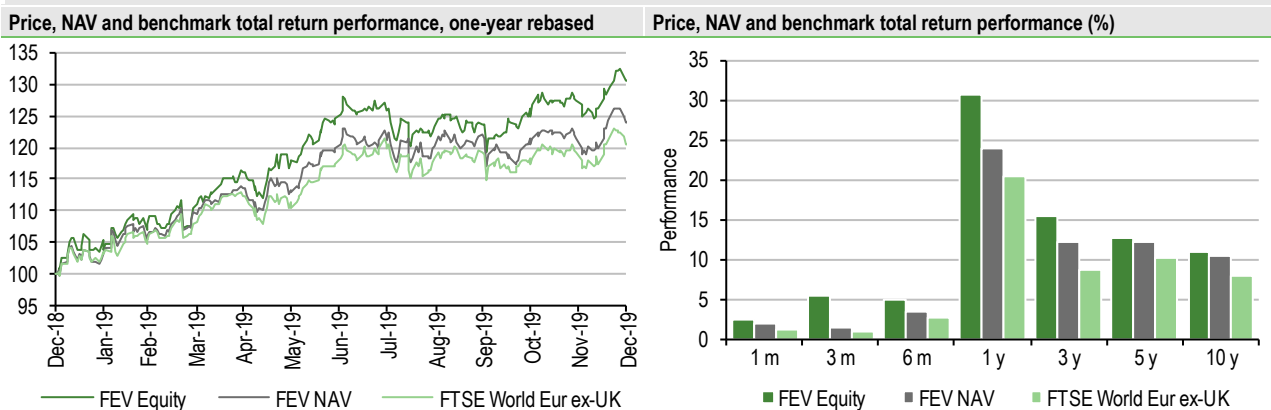
Exhibit 3: Five-year discrete performance data

12 months ending	Share price (%)	NAV (%)	FTSE World Europe ex-UK (%)	MSCI Europe (%)	MSCI World (%)	FTSE All-Share (%)
31/12/15	9.2	6.8	5.3	3.3	5.5	1.0
31/12/16	7.6	17.6	19.7	19.5	29.0	16.8
31/12/17	26.2	20.0	17.5	15.3	12.4	13.1
31/12/18	(6.8)	(4.8)	(9.5)	(9.0)	(2.5)	(9.5)
31/12/19	30.6	23.8	20.4	19.8	23.4	19.2

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

With the exception of 2016, FEV's NAV and share price total returns have surpassed the performance of the benchmark FTSE World Europe ex-UK Index in each of the last five years (Exhibit 3). In absolute terms, the trust has generated double-digit annual returns over the last one, three, five and 10 years, with a particularly strong performance over the last 12 months.

Exhibit 4: Investment trust performance to 31 December 2019



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

FEV's relative returns are shown in Exhibit 5; it has outperformed its benchmark in both NAV and share price terms over all periods shown. The fact that it has also beaten the MSCI World Index

over almost all periods of three years and less is notable given the strong outperformance of the dominant US market in recent years. Morse explains that in recent months, positive contributors to performance include ASML (lithography equipment – company gaining market share); EssilorLuxottica (ophthalmic lenses, frames and sunglasses – now operating more efficiently following its major merger); and LVMH (luxury goods – results have exceeded expectations). Stocks that have performed less well include ABN AMRO (bank – facing a regulatory fine); Andritz (engineering firm – exposure to the auto sector); and Fresenius Medical Care (kidney dialysis – operational issues).

Exhibit 5: Share price and NAV total return performance, relative to indices (%)

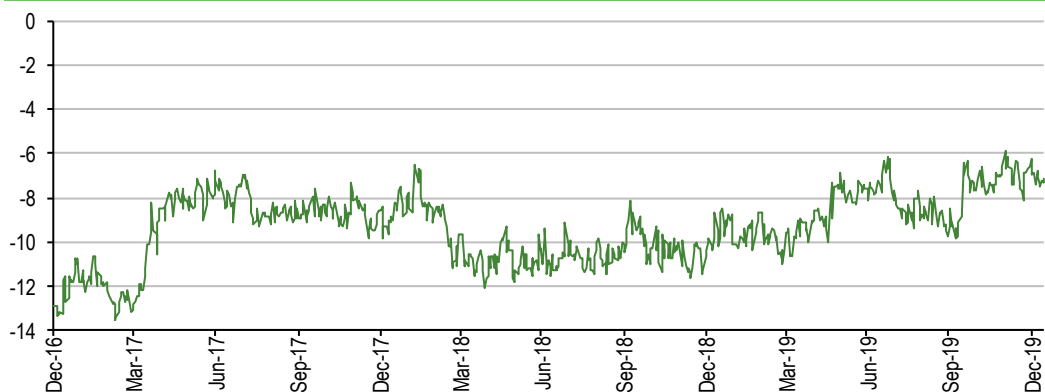
	One month	Three months	Six months	One year	Three years	Five years	10 years
Price relative to FTSE World Europe ex-UK	1.3	4.5	2.3	8.4	19.9	11.8	30.6
NAV relative to FTSE World Europe ex-UK	0.9	0.6	0.8	2.8	10.4	9.9	23.8
Price relative to MSCI Europe	0.9	4.1	2.0	9.0	22.3	16.4	31.3
NAV relative to MSCI Europe	0.5	0.2	0.5	3.4	12.5	14.5	24.5
Price relative to MSCI World	1.7	4.3	(0.2)	5.8	13.6	(1.8)	(11.7)
NAV relative to MSCI World	1.3	0.4	(1.7)	0.3	4.5	(3.5)	(16.3)
Price relative to FTSE All-Share	(0.9)	1.3	(0.6)	9.6	26.0	25.7	28.8
NAV relative to FTSE All-Share	(1.3)	(2.5)	(2.0)	3.9	15.9	23.5	22.1

Source: Refinitiv, Edison Investment Research. Note: Data to end-December 2019. Geometric calculation.

Valuation: Discount at narrower end of three-year range

Having been in a narrowing trend since Q218, FEV's shares are currently trading at a 7.1% discount to cum-income NAV. This is at the narrow end of the 5.9% to 11.0% range of discounts over the last 12 months. Over the last one, three, five and 10 years, the trust has traded at average discounts of 8.4%, 9.3%, 9.0% and 10.8%, respectively. The narrower discount may be as a result of the board's initiatives in recent quarters, such as a more competitive ongoing charge (0.88%) and the 75% allocation of management fees and finance costs to the capital account, supporting a higher dividend, along with the manager's continuing record of outperformance.

Exhibit 6: Share price discount to NAV (including income) over three years (%)



Source: Refinitiv, Edison Investment Research

Peer group comparison

FEV is one of eight funds in the AIC Europe sector. Its NAV total returns are above average over one, three and five years – 2.4pp, 8.7pp and 7.1pp ahead of the mean returns, respectively – while lagging over the last decade. The outperformance over one year, a period of above-average market returns, is particularly notable given Morse's focus on preserving, as well growing, capital. None of the funds in the peer group trade at a premium and the range of discounts is relatively wide; FEV's is currently modestly above average. Its ongoing charge is in line with the mean and, in keeping

with all of its peers, no performance fee is payable. The trust's level of gearing is below average, while courtesy of a significantly higher dividend in FY18, it now offers a yield that is 0.8pp above the peer-group average.

Exhibit 7: AIC Europe sector peer group as at 15 January 2020*

% 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
Fidelity European Values	1,090.4	25.1	40.7	82.6	167.0	(7.5)	0.9	No	104	3.3
Baillie Gifford European Growth	371.1	16.2	13.0	40.6	95.5	(5.1)	0.6	No	100	3.4
BlackRock Greater Europe	348.3	32.0	47.4	96.1	183.1	(3.1)	1.1	No	100	1.2
European Opportunities Trust	966.2	24.2	53.9	97.0	336.4	(4.6)	0.9	No	108	0.6
Henderson European Focus Trust	285.9	24.1	25.2	70.1	177.2	(7.8)	0.8	No	103	2.4
Henderson EuroTrust	261.6	26.6	33.7	87.1	197.9	(8.4)	0.8	No	104	2.5
JPMorgan European Growth Pool	206.9	18.3	19.9	62.4	124.5	(11.7)	1.0	No	113	2.9
JPMorgan European Income Pool	163.4	15.2	22.4	67.9	161.4	(8.3)	1.1	No	112	3.9
Average	461.7	22.7	32.0	75.5	180.4	(7.1)	0.9		106	2.5
Rank in peer group (8 funds)	1	3	3	4	5	4	5		4	3

Source: Morningstar, Edison Investment Research. Note: *Performance to 14 January 2020 based on ex-par NAV. TR = total return. Net gearing is total assets less cash and equivalents as a percentage of net assets (100 = ungeared).

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