The Law Debenture Corporation

Differentiated income and growth

Investment trusts

The Law Debenture Corporation (LWDB) is differentiated by being both an investment trust with a diversified portfolio of global equities and a leading provider of independent professional services through its IPS subsidiaries. The bottom-up managed portfolio is globally diversified with a strong bias towards UK equities. IPS is highly profitable, regularly providing revenue earnings well ahead of its share of NAV, supporting a strong track record of dividend growth and allowing greater flexibility within the portfolio to pursue high-return but lower yield investments. LWDB is benchmarked against the FTSE All-Share index, which it has outperformed over one, three, five and 10 years. Ongoing charges are competitive and the 2.8% yield is one of the highest in the sector.

12 months ending	Share price (%)	NAV* (%)	FTSE All-Share (%)	FTSE 250 (%)	FTSE World (%)
31/08/13	25.4	20.6	18.9	31.7	20.1
31/08/14	12.7	15.7	10.3	11.5	13.3
31/08/15	(6.0)	0.4	(2.3)	10.6	2.3
31/08/16	5.1	7.2	11.7	6.4	26.5
31/08/17	27.7	20.7	14.3	14.9	19.4

Source: Thomson Datastream. Note: All % on a total return basis in GBP. *NAV including income and debt at fair value.

Investment strategy: Flexible with income support

LWDB maintains a diversified, bottom-up managed portfolio of c 130 holdings, typically 70-75% drawn from the UK. The managers seek out growing businesses, trading at valuations that do not reflect their long-term prospects, investing across the market cap spectrum without bias to value or growth. The strong income contribution from the IPS businesses allows investment in a wider range of opportunities than a typical income-focused fund may normally consider. Overseas stock selection (typically 25-30%) is driven by gaining exposure to more attractive investment opportunities than can be found in the UK and 10-15% of the portfolio is held in open- and closed-ended funds to add specialist regional or sector exposure.

Market outlook: Market valuation has increased

Following a year of strong equity returns, valuations are looking less attractive. On a forward P/E basis developed markets such as the UK, Europe, and the US are trading at a c 20% premium to their 10-year averages. As the economic recovery and equity bull market mature, investors may find appeal in a trust such as LWDB with a strong record of dividend growth, underpinned by the income stream from its IPS business, providing flexibility to invest in a wider range of opportunities than many other income-orientated funds.

Valuation: Discount narrower but still above peers

At 7.8%, LWDB's share price discount to fair value cum-income NAV has narrowed since the first time publication of an IPS fair value in early 2016, but remains above the peer group average. A 2.8% dividend yield ranks third highest among the sector's 24 trusts, providing support for a potential discount narrowing.

26 September 2017

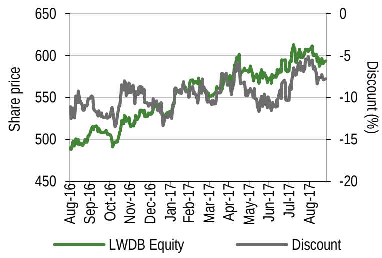
Price	**593.5p**
Market cap	**£701.5m**
AUM	**£903.6m**

NAV*	643.4p
Discount to NAV	7.8%
NAV**	657.9p
Discount to NAV	9.8%

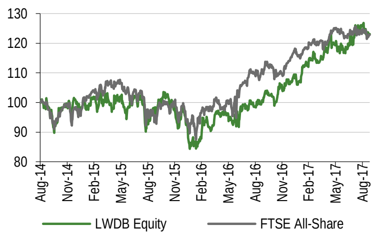
*Including income, debt at fair. **Excluding income, debt at par. Data as at 25 September 2017.

Yield	2.8%
Ordinary shares in issue*	118.2m
*Excludes own shares held	
Code	LWDB
Primary exchange	LSE
AIC sector	Global
Benchmark	FTSE All-Share Index

Share price/discount performance



Three-year performance vs index



52-week high/low	613.0p	491.0p
NAV** high/low	655.7p	553.3p

**Including income.

Gearing

Gross*	14.0%
Net*	2.0%

*As at 31 August 2017.

Analysts

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Edison profile page

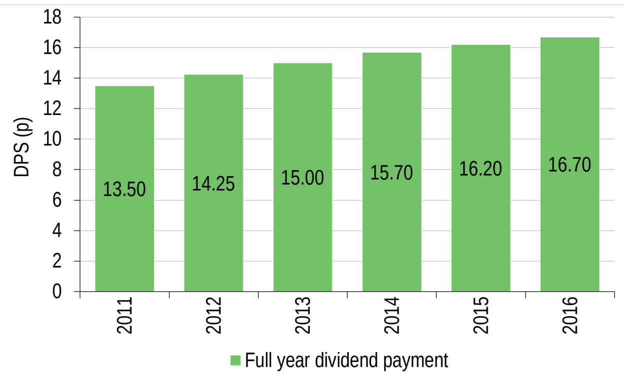
The Law Debenture Corporation is a research client of Edison Investment Research Limited

Exhibit 1: Trust at a glance

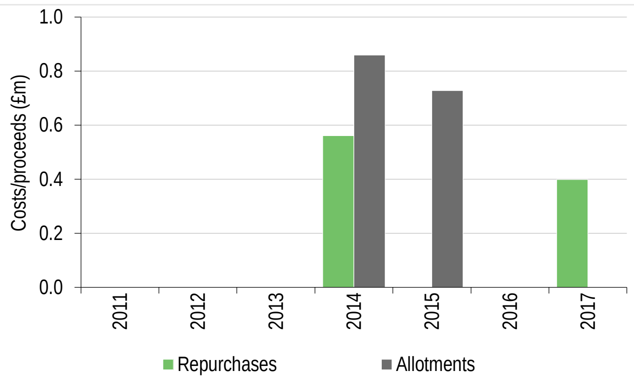
Investment objective and fund background	Recent developments
LWDB's investment objective is to achieve long-term capital growth in real terms and steadily increasing dividend income to shareholders. The aim is to achieve a higher rate of total return than the FTSE All-Share index through investing in a global portfolio diversified both geographically and by industry. LWDB's independent professional services (IPS) business provides a regular flow of income, which enhances the dividend income from the equity portfolio.	■ 1 September 2017: Net asset value and portfolio update. ■ 25 July 2017: Half year results to 30 June 2017. NAV TR +9.3% vs FTSE All-Share +5.5%. Share price TR +10.2%. Interim dividend of 5.5p (paid 8 September 2017). ■ 13 March 2017: Final results to 31 December 2016. NAV TR +16.9% vs FTSE All-Share +16.8%. Annual DPS 16.7p (2015: 16.2p).

Forthcoming		Capital structure		Fund details	
AGM	April 2018	Ongoing charges	0.43%	Group	Michael Adams
Annual results	March 2018	Net gearing	2.0%	Manager	James Henderson & Laura Foll, Janus Henderson Investors
Year end	31 December	Annual mgmt fee	0.30% of portfolio NAV	Address	Fifth Floor, 100 Wood Street,
Dividend paid	September, April	Performance fee	None		London, EC2V 7EX
Launch date	1889	Trust life	Indefinite	Phone	+44 (0)20 7606 5451
Continuation vote	N/A	Loan facilities	£115m long term debt	Website	www.lawdeb.com

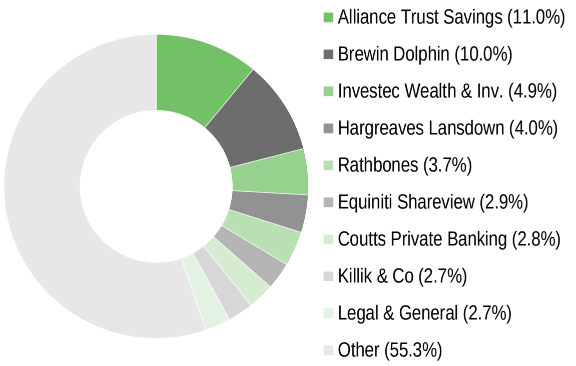
Dividend policy and history



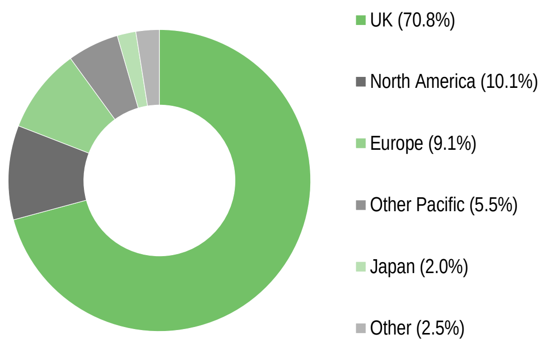
Share buyback policy and history



Shareholder base (as at 5 July 2017)



Portfolio exposure by geography (as at 31 August 2017)



Top 10 holdings (as at 31 August 2017)

			Portfolio weight %	
Company	Country	Sector	31 August 2017	31 August 2016*
Royal Dutch Shell	UK	Oil & gas producers	3.3	2.9
HSBC	UK	Banks	2.8	2.2
Baillie Gifford Pacific	Asia Pacific	Pooled equity investments	2.3	2.2
Senior	UK	Aerospace & defence	2.2	2.1
Stewart Investors Pacific	Asia Pacific	Pooled equity investments	2.2	2.1
Rolls-Royce	UK	Aerospace & defence	2.1	N/A
GKN	UK	Automobiles & parts	2.0	2.1
BP	UK	Oil & gas producers	2.0	2.1
Rio Tinto	UK	Mining	2.0	1.8
Prudential	UK	Life insurance	1.9	N/A
Top 10 (% of holdings)			22.8	21.2

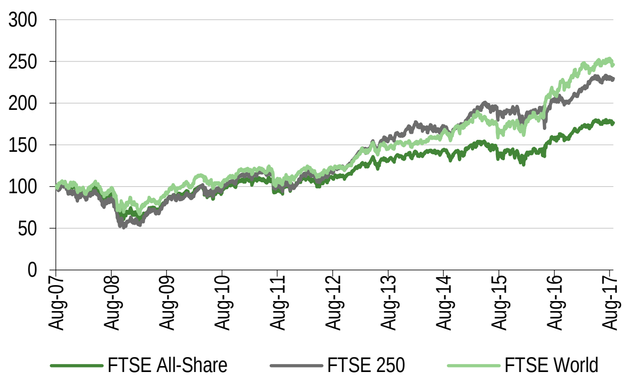
Source: The Law Debenture Corporation, Edison Investment Research, Bloomberg, Morningstar. Note: *N/A where not in August 2016 top 10.

Market outlook: Valuations have lifted

Global equity markets have continued to rise in recent months and remain close to their highs despite a number of economic and geopolitical uncertainties. The FTSE All-Share index, against which LWDB is benchmarked, has also shown positive performance but continues to lag global indices such as the FTSE World index (Exhibit 2), in which UK equities were weighted at 6.4% at the end of August 2017. UK-listed companies with significant overseas earnings have received a material boost from the weakness of sterling since last year's EU referendum vote, but this has only slightly narrowed the performance gap that has built up in recent years between the FTSE All-Share index and the better-performing FTSE 250 index. More recently, the US dollar has lost the gains made in the aftermath of the US presidential election, with a period of weaker economic data raising doubts about the extent of future tightening in US interest rates. The rise of markets has not been fully supported by corporate earnings growth, such that developed market equity valuations have reached a relatively high level when measured in terms of forward P/E multiples, c 20% above their 10-year averages. In terms of yield the comparison with long-term averages is less marked, especially considering the continued low level of bond yields and interest rates. However, as both the economic cycle and equity bull market continue to mature, investors may find appeal in a trust such as LWDB with a strong record of dividend growth, underpinned by the income stream from its IPS business, providing flexibility to invest in a wider range of opportunities than many other income-orientated funds.

Exhibit 2: Market performance and valuation metrics

Market indices total return performance over 10 years



Valuation metrics

	Last	High	Low	10-year average	Last as % of average
UK					
P/E 12 months forward (x)	14.2	15.6	7.4	12.1	118%
Price to book (x)	1.6	2.5	1.2	1.7	93%
Dividend yield (%)	3.7	6.6	2.7	3.5	104%
Return on equity (%)	8.6	21.2	2.5	10.4	82%
World					
P/E months forward (x)	15.7	16.0	8.8	13.1	120%
Price to book	2.1	2.5	1.1	1.8	120%
Dividend yield	2.4	4.6	2.0	2.7	90%
Return on equity	10.8	16.9	4.7	11.0	98%

Source: Thomson Datastream, Edison Investment Research. Note: Data to 25 September 2017.

Fund profile: Differentiated income and growth

LWDB was originally founded in 1889 as a limited company to facilitate the issue of corporate debentures, and it is out of this long history that its current structure, differentiated from other investment trusts, has developed. Today, it divides into two distinct businesses: it is an investment trust listed on the London Stock Exchange with a diversified portfolio of global equities; and a leading provider of independent professional services through a group of subsidiaries collectively referred to as IPS. Much of the commentary in this note refers to the strategy, management and performance of the investment portfolio (c 87% of fair value NAV), but in the following section we provide more detail on IPS (c 13% of fair value NAV), its earnings contribution and the group synergy that it brings, and its valuation. We also provide a detailed description of the IPS businesses in the appendix to this report.

LWDB's objective is to achieve long-term capital growth in real terms and steadily increasing income, aiming to generate a higher rate of total return than the FTSE All-Share index. Janus

Henderson Investors is the appointed manager of the investment portfolio, within broad regional constraints set by the LWDB board (see Exhibit 4). The lead fund manager since 2003 has been James Henderson, assisted since 2011 by Laura Foll from the Janus Henderson equity income team. Janus Henderson's director of European equities, Tim Stevenson, is responsible for the LWDB portfolio's European stock selection.

Although LWDB sits within the AIC Global sector it has a higher than average UK equity exposure, typically in the range of 70-75%, with international equity exposure typically 25-30%. The portfolio is constructed through bottom-up stock selection, primarily from the UK stock market, without reference to index sector allocations. Overseas stock selection targets chosen exposures where suitable opportunities to invest are limited or do not exist within the UK market. Collective investment funds are used to gain diversified exposure to particular regional (eg Asia-focused funds to access regional growth) or sector (eg technology) opportunities.

Independent professional services (IPS)

Through a group of subsidiaries that operate entirely independently from the investment trust, LWDB is a leading provider of independent professional services, comprising corporate trusts (including trustee and escrow banking), pension trusts, corporate services (including agent for service of process), treasury services, whistleblowing services, and governance services to client boards and pension funds. This group of businesses has recently been rebranded Independent Professional Services (IPS), having historically been known as Independent Fiduciary Services (IFS), so as to better capture the breadth of professional services that are offered, as well as management's plans to develop and grow IPS further. The IPS businesses are separately capitalised, and are monitored and overseen by a board whose members include the heads of relevant business areas and two independent non-executive directors. However, although the investment trust and IPS are legally, commercially and operationally separate, their combination within LWDP provides attractive group-level synergies that are not found in a conventional investment trust structure. We discuss the IPS businesses in detail in the appendix to this report. In summary, they are highly profitable, with modest marginal capital needs, and make a substantial contribution to LWDB's overall net revenue per share.

IPS regularly contributes more than 40% of overall LWDB revenue per share, well ahead of its c 3% share of LWDB's H117 IFRS NAV or c 13% on a fair value basis (see below). Although in aggregate the IPS businesses have shown moderate growth in recent years, some have grown very strongly while others have faced headwinds as a result of changed market circumstances in the post-financial crisis era. Management seeks to accelerate growth and, as indicated in the 2016 Annual Report, has implemented a strategy for organic growth in each of the business lines.

The scale and regularity of the income flow provided by IPS clearly makes a significant direct contribution towards meeting LWDB's objective of steadily increasing dividends to shareholders, provides scope to even out fluctuations in dividend income from the investment trust portfolio and provides the investment trust manager with greater strategic flexibility in asset selection. As a specific example of how this additional investment flexibility works in practice, the investment trust manager, James Henderson, cites the ability to invest in late 2015 despite widespread dividend cuts that would have precluded many income funds from investing.

A further synergy resulting from LWDB's corporate structure is the ability to offset otherwise unrelieved tax losses within the investment trust against taxable earnings of IPS. The IPS effective tax rate, benefiting from the group structure, was 4.3% in 2016 and, although it will be affected by the introduction of base erosion and profit shifting (BEPS) rules from 1 April 2017 (more specifically aimed at companies that avoid tax through the use of multiple jurisdictions), a benefit will remain. Management has indicated a negative tax impact of c £450k in FY17 and c £600k on a full year basis in FY18. Reflecting the new rules from 1 April 2017, the H117 IPS effective tax rate was 11.9%.

IPS fair value

IPS is carried in the statutory IFRS financial statements at book value, substantially below its estimated fair value. In order to provide investors with greater clarity regarding the fair value of LWDB, management provides an independently assessed estimate of the fair value of IPS, based on the application of an appropriate multiple of historic EBITDA, and adhering to the guidelines provided by the International Private Equity and Venture Capital Association (IPEV). As can be seen in Exhibit 3, the EBITDA multiple applied to IPS has been relatively stable over the past three years, in a range of 8.1x-8.9x. The multiple is based on the observed market valuations for an undisclosed basket of broadly relevant companies (direct comparators are elusive), adjusted for differences in growth rates, margins, size and liquidity. An adjustment is also made for capital within the businesses that is in excess of that required. The IPS valuation is on a standalone basis and makes no allowance for the group synergies referred to above, including group-wide tax relief.

Exhibit 3: Fair valuation of IPS business

£000s	30-Jun-17	31-Dec-16	31-Dec-15	31-Dec-14
IPS valuation				
IPS EBITDA	9,880	9,880	9,333	9,515
EBITDA multiple (x)	8.3	8.1	8.4	8.9
Operational value of IPS	82,004	80,028	78,397	84,684
IPS surplus net assets	16,730	9,908	12,082	11,356
IPS fair value	98,734	89,936	90,479	96,040
IPS fair value per share (p)	83.6	76.1	76.7	81.4
LWDB fair value				
LWDB fair value per share as per IFRS financial statements (p)	599.96	560.73	472.14	486.82
IPS fair value adjustment per share (p)	65.99	62.37	61.27	65.73
Debt fair value adjustment (p)	(24.85)	(24.62)	(8.87)	(10.20)
LWDB fair value NAV per share (p)	641.10	598.48	524.54	542.35
IPS book value (IFRS) as % of total	3.0%	2.3%	3.3%	2.7%
IPS gain value as % total	13.0%	12.7%	14.6%	14.9%

Source: The Law Debenture Corporation, Edison Investment Research

Valued at fair value, IPS represented 13.0% of the total LWDB fair value NAV at 30 June 2017, reflecting a 65.99p (per LWDB share) uplift to its 17.6p IFRS book value.

The fund managers: James Henderson and Laura Foll

The managers' view: Focusing on the stocks

With their bottom-up approach to portfolio construction, the managers remain very much focused on stock selection; while noting the impact of often quite sharp swings in market sentiment, portfolio activity remains focused on seeking the appropriate balance between future growth opportunities and valuation, and adapting to new developments such as management change.

In terms of swings in market sentiment, the aftermath of the EU referendum saw a sharp decline in sterling, which was eventually reflected more positively in the performance of larger, more obviously international companies than the small- and mid-cap companies that are relatively highly represented in the LWDB portfolio; this was despite the fact noted elsewhere that overseas earnings can still be highly significant for the latter. Periods of sterling weakness, though positive for the performance of the trust's overseas holdings, had a tendency to weigh on overall trust performance.

As the valuations of some of the larger global stocks continued to push up, the trust has continued gradually and selectively to reduce some exposures, particularly in North America, recycling capital into “better value” opportunities. The retracement of the US dollar in recent months may have the effect of broadening investor interest in and perception of market risks and rewards.

Asset allocation

Investment process: Selecting for growth and value

The LWDB investment portfolio is constructed through bottom-up stock selection, primarily drawn from the UK stock market, with the managers aiming to mitigate investment risk by maintaining a portfolio that is diversified by sector, geography and the number of holdings. When selecting stocks, the managers seek out growing businesses, trading at valuations that do not reflect their long-term prospects, investing across the market cap spectrum without bias to value or growth. The strong income contribution from the IPS businesses allows investment in a wider range of opportunities than a typical income-focused fund may normally consider.

The targeted portfolio diversification, as well as the managers’ preference for buying and selling holdings on a gradual basis, results in a relatively large number of stocks across the portfolio, typically 130-140. The bottom-up approach means that although performance is benchmarked against the FTSE All-Share index, this has little influence on how the portfolio is constructed.

Overseas stock selection is driven by the portfolio managers seeking to gain exposure to areas where suitable opportunities are limited or do not exist in the UK market. As examples, the managers cite portfolio holdings Apple in the US and Toyota Motor in Japan, neither of which have UK-listed equivalents. Investments in Asia are made to gain exposure to the region’s superior long-term growth potential, and are typically made through pooled investments. The US market provides a broader range of investment opportunities than may be available in the UK, including oil services and larger industrials companies. Similarly, Europe offers additional opportunities including global healthcare companies.

Current portfolio positioning

Exhibit 4 shows LWDB’s geographic positioning, which reflects its primary allocation to the UK, enhanced by a diversified international exposure, within the investment limits set by the board. It is important to note that although LWDB is significantly invested in UK-listed companies, the underlying economic exposure is much more diversified as a result of the international operations of many of those companies; the managers estimate that more than 75% of the underlying earnings of portfolio companies come from outside the UK. The significant role played by the IPS businesses in meeting LWDB’s dividend growth objectives, which provides the investment portfolio with greater investment flexibility, can be seen in the portfolio yield; at 2.9% at the end of July 2017 it was below the 3.6% yield on the FTSE All-Share index, although above the 2.5% yield on the FTSE World index. There were slightly more than 130 holdings when the full portfolio was listed as of 30 June 2017, with the top 10 holdings representing 22.7% of the total. There were 11 pooled investments representing 10.3% of the total portfolio (10.5% at the end of July). Among the top 10 holdings shown on page 2, Rolls-Royce has replaced Senior Engineering during the past 12 months. The position in Rolls-Royce was increased earlier in the period, with the managers taking a positive view on the value to shareholders of anticipated long-term cash generation beyond the current investment phase. The Senior Engineering share price suffered from earnings downgrades, but was retained in recognition of its longer term attributes of technical expertise and barriers to entry.

The UK equity weighting has changed little over the past 12 months and the main geographic shift outside the UK during that period has been a reduction in the North American weighting and an increase in the European weighting. This change has been entirely stock-driven, reflecting a reduction in Lockheed, Deere, and Applied Materials, where the managers believe that valuations have risen too far.

Exhibit 4: Portfolio geographic exposure vs allocation guidelines (% unless stated)

	Portfolio end-August 2017	Portfolio end-August 2016	Change (pp)	Allocation guidelines
UK	70.8	71.0	(0.2)	55-80
North America	10.1	12.0	(1.9)	0-20
Europe	9.1	8.0	1.1	0-10
Other Pacific	5.5	5.3	0.2	0-10
Japan	2.0	1.9	0.1	0-10
Other	2.5	1.8	0.7	0-10
	100.0	100.0		

Source: The Law Debenture Corporation, Edison Investment Research. Note: Excluding cash and fixed interest.

In Exhibit 5 we show LWDB's sector positioning compared with the benchmark FTSE All-Share index sector weightings; we do so with the caveat that the bottom-up construction of LWDB's portfolio is not influenced by the index sector weights and should therefore be expected to show significant differences. The changes in sector weightings within the LWDB portfolio over the past year are relatively modest. Industrial stocks continue to represent the portfolio's largest exposure and greatest overweight position relative to the benchmark. The financials exposure of the portfolio has increased slightly (including additional investment in Standard Chartered) in the past year but remains significantly lower than the index weighting. Consumer goods exposure versus the index also remains low.

Exhibit 5: Portfolio sector exposure vs benchmark (% unless stated)

	Portfolio end-August 2017	Portfolio end-August 2016	Change (pp)	Index end-August 2017	Active weight vs index (pp)	Trust weight/ index weight (x)
Industrials	29.8	31.6	(1.8)	11.2	18.6	2.7
Financials	17.0	15.3	1.7	26.5	(9.5)	0.6
Oil & gas	8.7	8.7	0.0	11.4	(2.7)	0.8
Healthcare	8.3	9.4	(1.1)	8.5	(0.2)	1.0
Consumer services	7.9	7.4	0.5	10.9	(3.0)	0.7
Basic materials	7.0	5.8	1.2	7.6	(0.6)	0.9
Consumer goods	6.2	7.5	(1.3)	16.2	(10.0)	0.4
Technology	2.0	2.5	(0.5)	0.9	1.1	2.3
Utilities	1.7	2.0	(0.3)	3.1	(1.4)	0.5
Telecommunications	0.7	0.8	(0.1)	3.7	(3.0)	0.2
Pooled equity investments	10.7	9.0	1.7	N/A	N/A	N/A
	100.0	100.0		100.0		

Source: The Law Debenture Corporation, FTSE Russell, Edison Investment Research

Performance: Consistently above benchmark

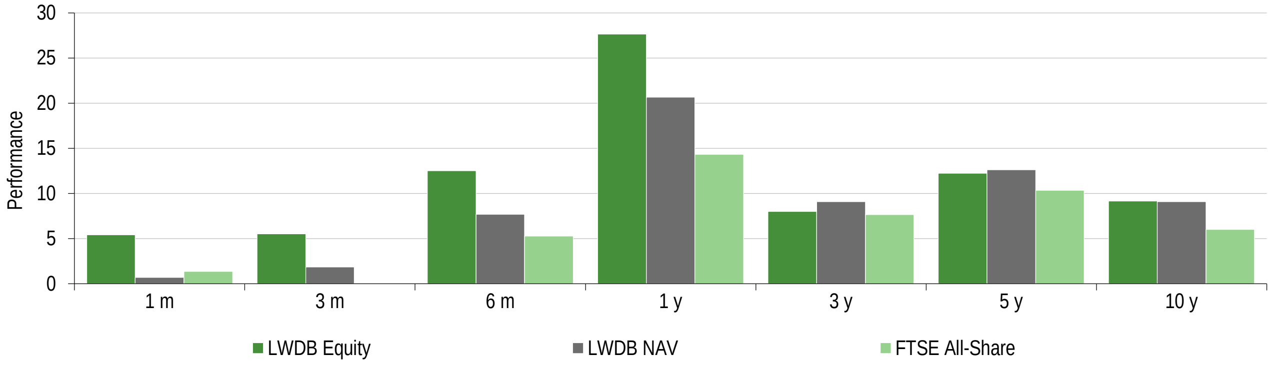
LWDB's NAV total return, calculated on a cum-income basis with debt at fair value, has outperformed its FTSE All-Share index benchmark over one, three, five and 10 years (Exhibit 7). The same exhibit shows that the share price total return has notably exceeded both the NAV total return and the benchmark total return over one year, with the discount to NAV narrowing. However, over three and five years, although the share price total return exceeds that of the benchmark, it has lagged the NAV total return, with the discount to NAV widening. The historical data have been restated to reflect the fair value of the IPS business, first published in 2016.

The long-term performance can be seen most clearly in Exhibit 6, which shows the trust generating an annualised NAV total return of 9.1% over 10 years and a share price total return of 9.2% compared with the 6.0% pa total return of the FTSE All-Share index.

NAV total return compared with the FTSE 250 index is more mixed than performance versus the benchmark FTSE-All Share index, reflecting the stronger performance of the former over most periods shown, but is positive over one year and 10 years. NAV performance has been below that of the FTSE World index over all periods, reflecting the UK bias of the trust's portfolio and the weaker performance of the FTSE All-Share index relative to global indices.

Exhibit 6: Investment trust performance to 31 August 2017

Price, NAV and benchmark total return performance (%)



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

Exhibit 7: 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 All-Share	4.0	5.5	6.9	11.7	1.1	8.8	34.4
NAV relative to FTSE All-Share	(0.7)	1.9	2.3	5.6	4.1	10.7	33.4
Price relative to FTSE 250	5.0	5.7	4.8	11.2	(6.7)	(10.3)	3.9
NAV relative to FTSE 250	0.3	2.1	0.3	5.1	(3.9)	(8.7)	3.1
Price relative to FTSE World	2.7	1.9	7.1	6.9	(18.4)	(15.3)	(5.2)
NAV relative to FTSE World	(1.9)	(1.6)	2.6	1.1	(15.9)	(13.8)	(5.9)

Source: Thomson Datastream, Edison Investment Research. Note: Data to end-August 2017. Geometric calculation.

We note that the NAV performance calculated with debt at fair value has been negatively affected by the trend decline in gilt yields, highlighted in Exhibit 8 by the comparison with total return using NAV calculated with debt at par value. The effect is particularly evident in the five-year performance, during which period (in 2015) LWDB increased its fixed rate debt by £75m.

Exhibit 8: NAV total return performance to 31 August 2017 (%) with debt at par value and fair value

	One month	Three months	Six months	One year	Three years	Five years	10 years
NAV ex income, debt at par value	1.4	1.7	8.5	17.8	32.8	88.3	139.7
NAV cum income, debt at fair value	0.7	1.9	7.7	20.7	29.9	81.2	139.1

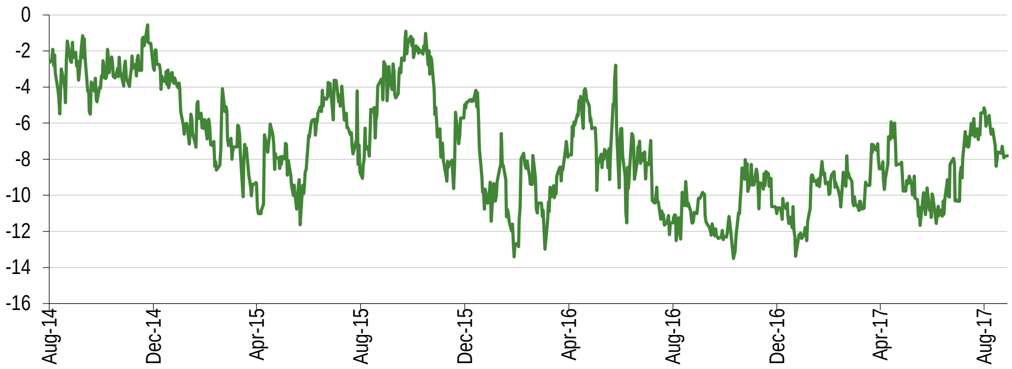
Source: The Law Debenture Corporation, Morningstar, Edison Investment Research.

Assuming that the debt is held to maturity, this negative effect on fair value NAV will eventually unwind as the value of the debt reverts to par. Moreover, for as long as market returns exceed the cost of debt, we would argue that the borrowing has had a positive overall impact on NAV.

Discount: Narrower but still above average

Exhibit 9 shows the share price discount to NAV over a three-year period, with NAV on a cum-income basis at fair value (both debt and IPS). The current discount of 7.8% is close to the 7.5% average level observed over the period, with a low of -0.5% and a high of 13.5% in early 2016, ahead of the first-time publication of a fair value for the IPS business (historical figures have been restated for this).

Exhibit 9: Share price discount to NAV (including income) over three years (%)



Source: Thomson Datastream, Edison Investment Research

Capital structure and fees

LWDB has a single share class with currently 118.2m ordinary shares in issue (excluding 0.2m own shares held). Shareholders have granted authorisation for the repurchase up to 14.99% of the shares in issue, as well as the allotment up to 7.5% of issued share capital over a three-year period. There is no share buyback programme currently in operation and the small number of share purchases and allotments made in recent years, and shown in the chart on page 2, relate to an employee share scheme.

LWDB has structural borrowing with a nominal value of c £115m and a blended average interest rate of 4.589%. Over the longer term the board anticipates that equity returns will exceed the cost of borrowing. £40m (nominal value) of 35-year bonds were issued in October 1999 with a coupon of 6.125% and £75m (nominal value) of fixed-rate, 30-year notes were issued in 2015 with a coupon of 3.77%. Both are secured by a floating charge. The £75m notes were partly used to repay and replace overdraft funding of £30m that provided the capital support ($50m) for the discontinued IPS US trust business. The discontinued business is expected to unwind by the end of 2018, freeing up capital for reinvestment in either IPS or the investment portfolio. Borrowings are carried in the financial statements at book value and LWDB provides a fair value that is included within the fair value NAV. The fair value of the debt at 30 June 2017 was £143.4m. Allowing for cash, net gearing was 6%.

Janus Henderson Investors earns a fee of 0.30% of net assets for the management of the investment portfolio under a contract that may be terminated by either side at six months' notice. Janus Henderson receives no performance fees and the underlying management fees on LWDB's holdings in Janus Henderson-managed collective funds are fully rebated. Although the investment management agreement does not cover custody, preparation of performance data or record-keeping, the board views the fee structure as being competitive for an actively managed investment trust. As we show later in this report, LWDB's ongoing charge for the costs of operating the investment portfolio, including the investment management fee, depositary and custody fees, investment performance data, accounting, company secretary and back office administration) of 0.43% in H117 (2016: 0.45%) is one of the lowest among its direct peers (see Exhibit 10).

Dividend policy and record

While LWDB's policy is to seek growth in both capital and income, the board attaches considerable importance to the dividend, which it aims to increase steadily without inhibiting the flexibility of the investment strategy. It has a strong dividend record, raising the dividend or holding it steady over a 40-year period covering a number of market cycles. As noted above, the IPS business makes a significant and regular contribution to the trust's overall revenue earnings and has provided additional flexibility in smoothing out the peaks and troughs in dividend income from the investment portfolio. We also note that revenue earnings are calculated by LWDB on a conservative basis, with all fees and expenses, including interest costs, charged in full to the revenue account.

Interim and final dividends are paid in September and April respectively. The total annual dividend per share for 2016 increased by 3.0% to 16.7p from 16.2p in 2015, and the 2017 interim dividend was increased by 5.8% to 5.5p (H116: 5.2p). At the end of 2016 and after allowance for payment of the final dividend, revenue reserves, which may be used to smooth the progression of future dividends, were equivalent to 20.3p per share.

Peer group comparison

In Exhibit 10 we show a comparison of LWDB with a peer group of the larger trusts within the AIC Global sector (24 constituents in total) that have a market cap of over £250m. To enable a consistent comparison across all periods, the data is based on ex-par NAV data for each of the trusts. LWDB's NAV total return is lower than the peer group average (and sector average) over one, three and five years, but ahead of the average over 10 years. It trades at an above average discount to NAV and its dividend yield (2.8%) is the highest among the peer group and third-highest in the sector. Ongoing charges (0.43%), which relate to the investment portfolio, are also below average and the second-lowest among the peer group. LWDB's net gearing of c 6% is modestly above average compared with both the selected peers and the sector.

Exhibit 10: Selected peer group as at 25 September 2017*

% unless stated	Market cap £m	NAV TR 1 year	NAV TR 3 year	NAV TR 5 year	NAV TR 10 year	Discount (ex-par)	Discount (cum-fair)	Ongoing charge	Perf. fee	Net gearing	Dividend yield (%)
The Law Debenture Corporation	701.5	17.8	32.8	88.3	139.7	(9.8)	(7.8)	0.43	No	103	2.8
Alliance Trust	2,456.0	23.3	58.7	99.5	125.1	(5.5)	(5.8)	0.54	No	102	1.9
Bankers	994.3	23.6	55.6	109.3	138.1	(2.2)	(2.9)	0.52	No	102	2.1
British Empire	793.7	27.5	44.1	82.9	97.8	(10.0)	(10.3)	0.90	No	105	1.7
Brunner	307.3	20.9	41.7	88.1	101.2	(13.0)	(11.5)	0.79	Yes	107	2.3
Caledonia Investments	1,477.3	14.3	40.6	93.0	87.6	(16.0)	(16.2)	1.14	No	100	2.0
Edinburgh Worldwide	318.0	26.9	64.7	124.0	167.8	(5.1)	(5.0)	0.92	No	108	0.0
F&C Global Smaller Companies	763.3	20.0	56.3	132.4	203.5	1.4	0.9	0.61	No	103	0.9
Foreign & Colonial Investment Trust	3,256.6	21.4	58.7	107.9	139.1	(4.6)	(5.5)	0.54	No	106	1.7
Independent	331.7	48.5	102.9	172.6	174.8	6.3	5.1	0.34	No	100	0.8
JPMorgan Elect Managed Growth	250.4	19.9	43.7	107.6	126.2	(2.3)	(2.6)	0.58	No	100	1.5
Monks	1,484.9	31.4	66.8	108.0	125.2	(1.7)	(1.4)	0.59	No	106	0.2
Scottish Investment Trust	664.8	18.4	47.6	87.1	109.7	(11.1)	(9.7)	0.59	No	104	1.7
Scottish Mortgage	5,711.7	40.7	93.2	205.7	274.9	(0.5)	0.3	0.44	No	103	0.7
Witan	1,822.1	21.5	53.8	117.4	153.0	(1.4)	(1.0)	0.79	Yes	108	1.9
Selected peer group average	1,422.3	25.1	57.4	114.9	144.2	(5.0)	(4.9)	0.65		104	1.5
Sector average (24 trusts)	950.5	23.4	55.1	108.7	138.3	(5.3)	(5.4)	0.79		103	1.6
LWDB rank in sector	10	20	22	18	8	17	17	23		9	3

Source: Morningstar, Datastream, Edison Investment Research. Note: *NAV (ex-par) performance data to 31 August 2017. TR = total return. Net gearing is total assets less cash and equivalents as a percentage of net assets.

The board

The board currently comprises five members, four of whom are independent non-executive directors, and the LWDB CEO Michael Adams, who replaced Caroline Banszky in August 2016. Before joining LWDB, Michael Adams spent four years at TMF Group, latterly as its global head of structured finance services. Before joining TMF, Adams spent 10 years at BNY Mellon, initially as finance director of its operating company QSR Management and ultimately as managing director of the structured finance group. The non-executive chairman, Christopher Smith, a former partner of

Cazenove & Co and corporate finance managing director at J.P. Morgan Cazenove, joined the board in March 2009 but has indicated that he will not seek re-election at the 2018 AGM. Robert Hingley will join the board as a non-executive director from 1 October 2017 and, subject to election by shareholders at the 2018 AGM, will replace Christopher Smith as chairman. He is a corporate financier with more than 30 years' experience, including senior roles at the Association of British Insurers, Lazard, and Lexicon Partners, and as director-general of The Takeover Panel. The other non-executive directors are Robert Laing (who joined the board in April 2012), Mark Bridgeman (March 2014) and Tim Bond (April 2015).

Appendix: Independent Professional Services (IPS)

As discussed above, the Law Debenture Corporation, through a group of subsidiaries operating independently from the investment portfolio, is a leading provider of independent professional services comprising corporate trusts (including trustee and escrow banking), pension trusts, corporate services (including agent for service of process), treasury services, whistleblowing services, and governance services to client boards and pension funds. The subsidiaries that provide these services are collectively referred to as IPS, representing c 3% of LWDB's IFRS NAV or c 13% on a fair value basis. IPS is highly profitable, contributing c 40% of LWDB's overall revenue per share with relatively little volatility. We also note above how the scale and regularity of this income flow provides LWDB with scope to even out fluctuations in dividend income from the investment trust portfolio, and provides the investment trust manager with greater strategic flexibility in asset selection. IPS also contributes towards tax efficiency within LWDB by providing an opportunity to utilise otherwise unrelieved tax losses in the investment trust.

The purpose of this section of the report is to provide a deeper analysis and description of the IPS businesses.

The services provided by the IPS businesses are subdivided into four broad areas of expertise:

- Corporate trusts, including trustee and escrow banking.
- Pension trusts and governance services.
- Corporate services.
- The whistleblowing service, Safecall.

Safecall operates in the UK and increasingly in Europe. The professional services are provided through offices in London, Dublin, New York, Delaware, Hong Kong, the Channel Islands and the Cayman Islands.

We show a summary financial history for IPS in Exhibit 11. The table begins with gross profit, which avoids the distortions to revenues from legal costs charged to clients (and reflected in cost of sales). In the 10 years from end-2006 to end-2016 the operating margin (operating profit/gross profit) has averaged 35.9% with a high degree of consistency. The 2016 net results exclude non-recurring group charges (£3.1m) relating to the decision to withdraw from the insufficiently profitable corporate trust business in the US. Activity had been focused on acting as an independent trustee to take a successor role in bankruptcy, requiring a capital commitment of $50m despite diminishing opportunities. LWDB expects to redeploy the $50m (within IPS or within the investment trust) by the end of 2018. In H117, a 1.8% y-o-y decline in gross profit was more than offset by lower administrative costs such that PBT increased 4.7%. Net income declined by 5.4% y-o-y as a result of the anticipated increase in the effective tax rate (to 11.9%), reflecting the introduction of HMRC's new BEPS rules from 1 April 2017. Management expects full-year results to be broadly in line with previous years.

Exhibit 11: IPS summary 10-year financial history

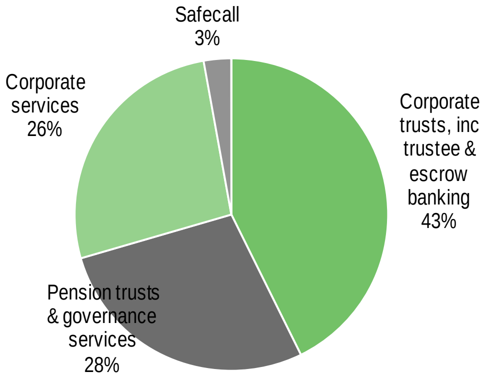
£m	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	10 year CAGR
Gross profit	18.4	24.1	22.7	23.1	24.2	26.7	26.1	27.2	27.2	27.1	27.3	4.0%
Administrative costs	(11.7)	(15.2)	(15.2)	(14.5)	(15.7)	(16.7)	(16.7)	(17.1)	(17.6)	(17.5)	(17.6)	
Operating profit	6.7	9.0	7.5	8.6	8.5	9.9	9.4	10.1	9.6	9.6	9.7	
Operating margin	36.3%	37.1%	33.0%	37.3%	35.2%	37.2%	35.9%	37.0%	35.3%	35.5%	35.7%	
Net interest	1.3	1.2	0.9	0.2	0.4	0.6	0.2	(0.2)	(0.3)	(0.4)	(0.3)	
PBT	7.9	10.1	8.4	8.8	8.9	10.5	9.6	9.9	9.3	9.2	9.5	1.8%
Tax	(2.0)	(3.5)	(2.2)	(2.1)	(1.7)	(2.0)	(1.8)	(1.7)	(1.2)	(0.8)	(0.4)	
Effective tax rate	24.7%	34.9%	25.7%	23.8%	18.8%	18.9%	18.3%	17.0%	12.9%	9.2%	4.3%	
Net income	6.0	6.6	6.3	6.7	7.3	8.5	7.8	8.2	8.1	8.4	9.1	4.2%
IPS revenue return per ordinary share (p)	5.12	5.63	5.35	5.69	6.19	7.25	6.67	6.96	6.87	7.09	7.68	
IPS revenue return as % LWDB total revenue return	42%	40%	34%	44%	47%	47%	44%	43%	41%	39%	41%	

Source: Companies House, Edison Investment Research

Although not disclosed in detail, our analysis indicates that the overall growth rate of IPS over the period reflects good progress from most business units (the growth of Safecall stands out), while the corporate trust business has faced some headwinds. As indicated in the 2016 annual report, management has implemented an organic growth strategy in each business and this is now firmly in place. The interim report says that early indicators are positive, although it will take some time for material results to become apparent, and that some investment will be required.

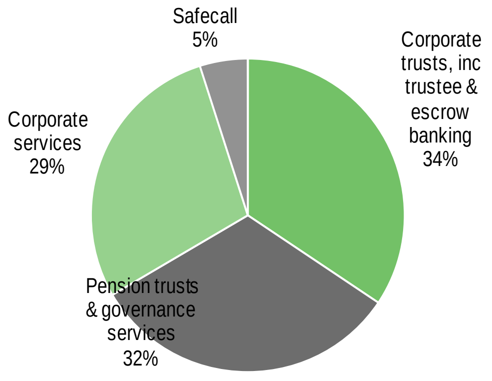
Exhibits 12 and 13 show the results of our analysis of the breakdown of gross profits of the main UK-registered LWDB subsidiaries that constitute IPS, by IPS business unit in 2007 and again in 2015. We have taken the data from publicly available filings at Companies House, choosing 2007 as an indicator of the position before the global financial crisis and 2015 as the most recent year for which all annual results have been filed (although we would not anticipate a material difference in the 2016 results). A deeper analysis of profitability after administrative costs is hampered by all UK professional services staff being employed through one subsidiary. These main UK subsidiaries account for a substantial part of IPS (85% in 2015 and 89% in 2007) and are therefore likely to be fairly representative of the overall IPS business unit split, although likely to slightly understate the contribution of corporate services and, to a lesser extent, corporate trusts.

Exhibit 12: Main UK entities, 2007 split of gross profit



Source: Companies House filings, Edison Investment Research

Exhibit 13: Main UK entities, 2015 split of gross profit



Source: Companies House filings, Edison Investment Research

Based on our analysis of the UK subsidiary data, the corporate services and pension trusts business units have both grown gross profits and share of IPS gross profits between 2007 and 2015, and Safecall has grown rapidly, but from a smaller base. As we discuss below, for the main UK corporate trust business unit subsidiary, gross profits dipped during the global financial crisis but had recovered by 2011 before drifting off.

Corporate trusts, including trustee and escrow banking

When The Law Debenture Corporation was founded in 1889 it was for the purpose of acting as trustee to facilitate the issuance of corporate debenture stock. Today, through the corporate trust business unit of IPS, it is the UK's leading independent (non-bank) corporate trustee, with many decades of experience and deep market connections, providing a wide range of services that include:

- UK and international bond issues and medium-term note (MTN) programmes.
- Securitisation, repackaging programmes, and international project finance transactions (eg holding security in relation to offshore and onshore wind farms).
- Tailor-made trust arrangements to facilitate regulatory compliance or mergers and acquisitions activity (M&A); to hold (in trust) and exercise special voting rights in complex mergers.

As a non-bank provider, with no financial involvement in transactions, IPS is more clearly free of potential conflicts of interest, which in many circumstances is likely to appeal to investors and borrowers. The business unit also operates a relatively flat structure compared with many competitors, especially large banks, which can be an advantage in terms of fast decision making and sign-off. Banks can often be fairly rigid in terms of the jurisdictions in which they choose to operate, their chosen counterparties, or the products they offer. IPS management believes that it is sufficiently nimble to look at transactions individually and react quickly.

The corporate trust business unit operates internationally to provide trustee services to a broad range of debt issuance markets, is trustee for more than 4,000 trusts, and includes a large number of high-quality issuers among its clients. We would direct readers to the company's corporate brochure that can be found on its website.

The demand for tailor-made trust arrangements is often M&A-related and generally involves the use of a trust to separate ownership from control. This may be a way of satisfying foreign ownership limits or perhaps restrictions on market concentration.

The business unit operates as an independent third party with a dedicated treasury team supporting its activities in trust and escrow appointments for project financings, whereby it receives, manages, and disburses the cash receipts. It is also trustee for the operator of the UK lottery, Camelot, and trustee for the Europe-wide lottery, EuroMillions. Additionally, M&A-type transactions, requiring an independent third party to hold cash (or shares, or other assets such as real estate) in escrow, often pending the fulfilment of warranties, is an area of increasing activity.

We have found no way of quantifying the overall market for corporate trustee services in which the corporate trust business unit operates. We believe that a substantial share is accounted for by the banks, especially large operators such as BNY Mellon, Deutsche Bank, and HSBC. Significantly, the banks are more likely to see trustee services as part of an overall package, and this may be one factor behind a highly competitive environment for setting fees in recent years. IPS prefers to seek more complex transactions where it has more possibilities to add value and generate appropriate fees.

Given the range of activities undertaken it is difficult to identify specific drivers for the business. Global debt issuance in a very broad sense (sovereign, corporate, securitised, structured etc) is obviously key to the debt-related trustee income that we suspect remains the larger share but, given the size of the overall markets, IPS's ability to secure a role in appropriate transactions on attractive terms is likely to be equally important. Participation in new issuance generates acceptance fees as well as replenishing the stock of outstanding trusts on which recurring annual fees are generated, in addition to post-issuance fees that may arise from restructurings, rating downgrades and other actions required by the trust deed. M&A activity is also likely to be a driver of some of the bespoke trust arrangements and trust and escrow appointments.

It seems likely that post-issuance work would have been boosted in the immediate aftermath of the global financial crisis and we suspect that the subsequent improvement in borrower credit quality and performance may explain the apparent decline in business unit gross profit (based on our analysis of the main UK subsidiaries) since 2011. Management describes a solid year overall for corporate trusts in 2016 and sets out in the annual report a number of the new appointments secured during the year.

Pension trust and governance services

The IPS pension trust business unit is the longest established and the largest provider of independent pension trustees in the UK. Among its more than 200 pension scheme clients, with over two million members and in excess of £150bn in invested assets, it works with some of the largest and most complex pension arrangements in the UK, as well as more than 100 smaller schemes that each has fewer than 500 members. As well as the traditional defined benefit (DB) schemes, defined contribution (DC) schemes and sole trusteeship services account for a growing share of the business. The latter provides an efficient and cost-effective simplified governance structure, which most commonly appeals to legacy (closed) DB schemes.

As a result of the rising cost of provision, active membership of UK DB schemes has declined from 2.4m in 2010 to 1.7m in 2016 (source: The Pensions Regulator) as increasing numbers of employers have closed DB schemes to new contributions and replaced them with DC schemes. Just 15% of DB schemes were open to new contributions at the end of 2016. However, as closing schemes are likely to have members who are receiving pensions or non-contributing members with preserved pension rights, and the time between a scheme closing to contributions and meeting its final pension obligations is likely to take a great many years, the decline in active members is not fully reflected in scheme numbers, which have declined at a slower pace. There were 5,900 private sector DB pension schemes in the UK in 2016, according to The Pensions Regulator, compared with 6,900 in 2010. Including DC schemes, the number of active occupational pension scheme members has increased quite noticeably from less than three million in 2013 to 5.5 million in 2015 (source: ONS). Although these numbers exclude automatic enrolment workplace pensions, it seems likely that their introduction has stimulated occupational scheme membership.

Although the steady decline in DB schemes presents a headwind, management notes that the increasing complexity, particularly of larger schemes, provides an offsetting increasing demand for pension trustee services, generally charged by the hour. The growth of DC work and sole trustee work are similarly positive. IPS indicates that new client interest remains strong and several additions to its team have been announced in recent months so as to increase capacity.

Competition in the market tends to be of a fragmented nature and it is not uncommon for experienced individuals (eg a retired CFO or company secretary) to offer trustee services. For such operators, keeping abreast of increasing complexity and regulatory developments may well prove challenging. We believe the collegiate culture that is a feature of the IPS professional services business units to be a differentiating factor compared with larger competitors and that this is a factor in maintaining high levels of service. Larger competitors include Capita, Capital Cranfield, Pitmans Law, and BESTrustees.

This business pillar also includes the smaller activities in governance services, which include the external and independent evaluation of board effectiveness against governance codes and providing advice on improvements.

Corporate services

The corporate services business unit includes the provision of a range of corporate services provided mainly to special purpose vehicles (SPVs) as well as the service of process business. The services are provided across each of the locations listed above but are tailored to each country's legal and taxation requirements.

The corporate services provided by IPS include the provision of independent corporate directors, corporate secretarial services, corporate governance services, and accounting and administration services. The SPVs include structured finance transactions (securitisations), mergers and acquisitions, infrastructure projects, sale and leaseback or any other circumstance where a third party wishes to set up a company for a specific purpose. We refer the reader to the division's corporate brochure, which can be found on its website.

The UK securitisation market is one of the largest and most developed securitisation markets in Europe and an important source of finance for UK businesses. Overall issuance of securitised product remains noticeably lower than it was before the global financial crisis (€237.6bn in 2016 versus €594.9bn in 2007) but has been growing since a 2013 low of €180.8bn, according to the Association for Financial Markets in Europe (AFME). Within the structured finance space, core competitors to IPS are Intertrust, TMF, Capita and Wilmington.

In the service of process business IPS is appointed to act as local agent for third parties who are otherwise not represented in that jurisdiction. Service of process is also known by different names in some jurisdictions, including registered agent, statutory agent or resident agent. An example of a typical arrangement involving a process agent is where an overseas entity raises a loan from a UK lending institution. The UK institution will require the overseas entity to appoint a UK process agent to whom they can, if needed, deliver court proceedings in the unfortunate event of default.

Although less significant in terms of scale, a range of similar services are provided whereby IPS can act as agent to receive notices and documentation in respect of areas such as arbitration proceedings, the UK Companies Act, or the UK Land Registry.

Most service of process business is undertaken in the UK, representing overseas customers that conduct business there but have no physical representation. Utilising the IPS network of international offices allows the business unit to provide a 24-hour-day, five-day-week efficient and flexible service to those clients (eg whatever time of day a transaction is due to close, London is able to sign off for New York and Hong Kong for London). From a market environment perspective, global transaction/global trade are key drivers. World Trade Organisation data show that despite a substantial correction during the global financial crisis and its aftermath, the volume of global trade doubled between 2005 and 2015. WTO forecasts look for 2-4% pa growth over the next couple of years.

Safecall

Safecall is the IPS business unit that provides external whistleblowing services. The business was established in 1999, when whistleblowing was in its infancy, and was acquired by LWDB in 2006. An examination of the statutory accounts for Safecall shows strong growth since acquisition, with gross profit increasing from £601k in 2007 to £1,119k in 2015 (the latest filed accounts) and PBT increasing from £116k to £390k. Average employee numbers increased from 14 to 21 over the same period. The business has also diversified geographically since acquisition, with non-UK revenues (overwhelmingly Europe) representing c 20% of the total in 2015 (wholly UK in 2007). The 2016 Annual Report indicates that demand in both the UK and Europe remained strong during 2016 as an increasing number of employers recognise the benefits of an external whistleblowing service. Among the benefits mentioned by Safecall are that it builds a culture of openness and demonstrates that malpractice and wrongdoing is taken seriously; it demonstrates a commitment to best practice and good governance to employees, regulators and investors; and may divert malpractice disclosure away from the media, thereby protecting the reputation of the organisation. In 2016 the introduction of the Modern Slavery Act during the previous year had a beneficial impact as organisations reviewed their policies to ensure robust reporting procedures were in place for both themselves and for organisations within their supply chains.

The client portfolio includes all industry sectors including public, private and listed organisations. These vary in employee and revenue sizes, ranging from compact workforces to some of the world's largest multinational organisations.

Notable appointments in 2016 included Marks & Spencer, Boehringer Ingelheim, Computacenter and Keller. Key competitors to Safecall are Expolink, Navex Global, and Convercent.

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