

Standard Life Equity Income Trust

Accelerating dividend growth

Standard Life Equity Income Trust (SLET) aims to generate a generous level of dividend as well as long-term growth in capital and income. The board has announced that the FY18 dividend will be at least 18.7p, which is +9.4% year-on-year, considerably higher growth than the rate of UK inflation. This increase will mean that SLET's dividend has grown for 18 consecutive years. Manager Thomas Moore is continuing to find attractively valued companies with positive fundamentals. He is confident that investment performance will improve with a change in investor focus away from high-growth, highly valued stocks, and he will be able to build on the trust's positive longer-term record. He says the current growth style bias in the UK stock market means that reasonably priced companies delivering strong results are not being rewarded with higher valuations.

12 months ending	Share price (%)	NAV (%)	FTSE All-Share (%)	FTSE 100 (%)	FTSE 250 (%)
30/06/14	19.2	17.1	13.1	12.3	16.8
30/06/15	13.2	14.5	2.6	0.2	14.5
30/06/16	(10.8)	(10.2)	2.2	3.8	(4.6)
30/06/17	18.3	23.6	18.1	16.9	22.2
30/06/18	14.2	8.7	9.0	8.7	10.6

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

Investment strategy: Focus on Change

Moore and his team follow the investment manager's Focus on Change philosophy, which aims to identify undervalued companies that are not reflecting attractive fundamentals or the potential for improvement. The belief is that over the long term a company's share price will be driven by its fundamentals, but that share prices moves can be less rational over the shorter term. Moore is index agnostic, meaning that stock and sector weightings are meaningfully different to those in the benchmark FTSE All-Share index. He invests across the capitalisation spectrum; currently c 70% of the portfolio is invested outside of the top 100 UK companies. Net gearing of up to 25% is permitted; at end-May 2018 it was 11.8%.

Market outlook: Opportunities in smaller caps

Over the last five years, smaller-cap indices have outperformed the large-cap FTSE 100 index. While in aggregate smaller companies are trading at higher valuations than larger firms, they have higher growth profiles and better dividend cover. With this backdrop in mind, investors may wish to consider moving down the market cap spectrum when seeking opportunities in UK equities.

Valuation: Shares trading close to NAV

SLET's current 0.1% share price discount to cum-income NAV is narrower than its historical averages. Over the last one, three, five and 10 years the average discounts have been in a range of 2.4% to 3.9%. SLET has a progressive dividend policy. The board has announced that the FY18 total distribution will be at least 9.4% higher than in FY17 and would be the 18th consecutive annual increase. SLET currently offers a dividend yield of 3.8%.

Investment trusts

11 July 2018

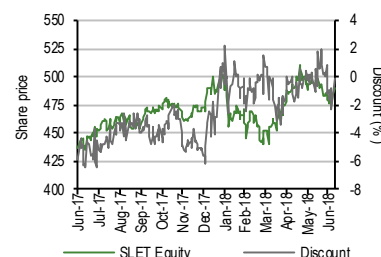
Price 490.0p
Market cap £241m
AUM £263m

NAV* 481.7p
 Premium to NAV 1.7%
 NAV** 490.6p
 Discount to NAV 0.1%

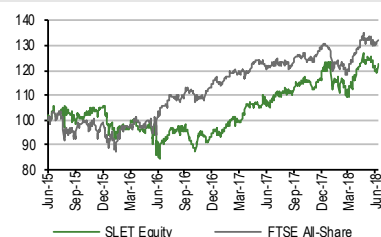
*Excluding income. **Including income. As at 9 July 2018.

Yield 3.8%
 Ordinary shares in issue 49.2m
 Code SLET
 Primary exchange LSE
 AIC sector UK Equity Income
 Benchmark FTSE All-Share

Share price/discount performance



Three-year performance vs index



52-week high/low 511.0p 435.5p
 NAV** high/low 509.6p 440.4p

**Including income.

Gearing

Gross* 11.8%
 Net* 11.8%

*As at 31 May 2018.

Analysts

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Exhibit 1: Trust at a glance

Investment objective and fund background

Standard Life Equity Income Trust (SLET) aims to provide shareholders with an above-average income from their equity investment while also providing real growth in capital and income. It seeks to achieve this through a diversified portfolio of between 50 and 70 equity holdings. The benchmark is the FTSE All-Share index.

Recent developments

- 24 May 2018: interim results for six months ending 31 March 2018. NAV TR -4.3% versus benchmark TR -2.3%. Share price TR +0.4%.
- 18 May 2018: announcement of a second interim dividend of 4.4p.
- 12 February 2018: announcement of a first interim dividend of 4.4p.
- 5 December 2017: final results for 12 months ending 30 September 2017. NAV TR +14.7% versus benchmark TR +11.9%. Share price TR +15.9%. Announcement of a final dividend of 5.5p.

Forthcoming

AGM	January 2019
Final results	December 2018
Year end	30 September
Dividend paid	Quarterly
Launch date	14 November 1991
Continuation vote	Five-yearly, next 2021

Capital structure

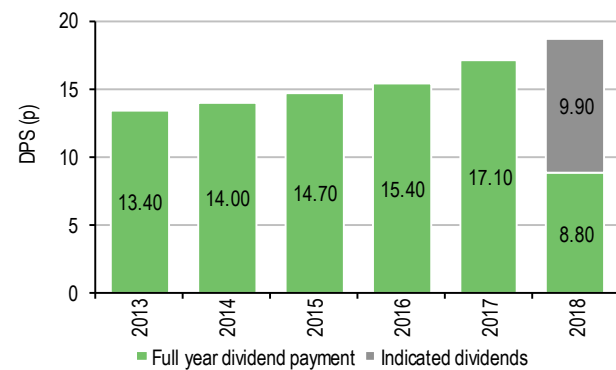
Ongoing charges	0.87% (FY17)
Net gearing	11.8%
Annual mgmt fee	Tiered (see page 7)
Performance fee	None
Trust life	Indefinite
Loan facilities	£30m

Fund details

Group	Aberdeen Standard Investments
Manager	Thomas Moore
Address	1 George Street, Edinburgh, EH2 2LL
Phone	+44 (0)345 600 2268
Website	www.standardlifeequityincometrust.com

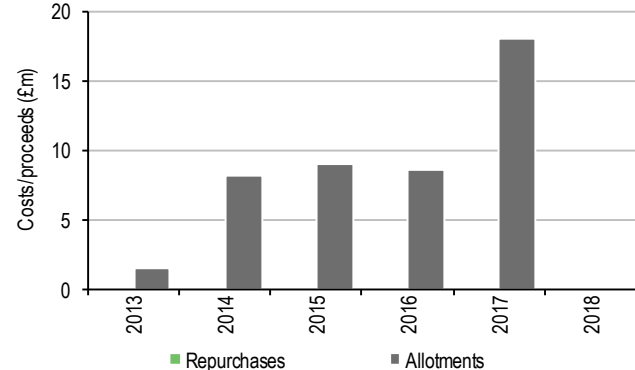
Dividend policy and history (financial years)

Dividends are paid quarterly in March, June, September and January. It is the board's intention that SLET should achieve long-term real (ie above inflation) growth in its dividend.

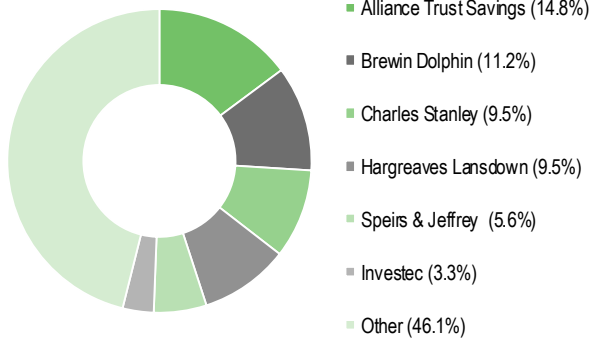


Share buyback policy and history (financial years)

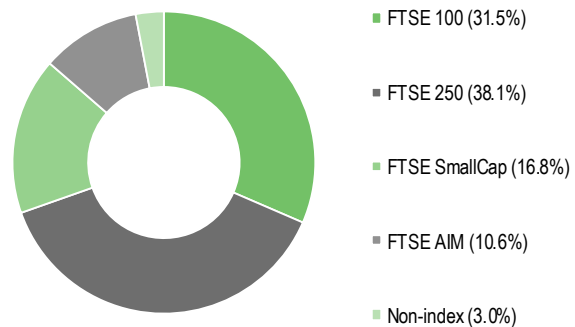
SLET may buy back up to 14.99% or allot up to 10% of ordinary shares annually to manage a discount or a premium. Figures include shares issued as a result of subscription share exercise.



Shareholder base (as at 31 May 2018)



Portfolio exposure by market cap (as at 31 May 2018)



Top 10 holdings (as at 31 May 2018)

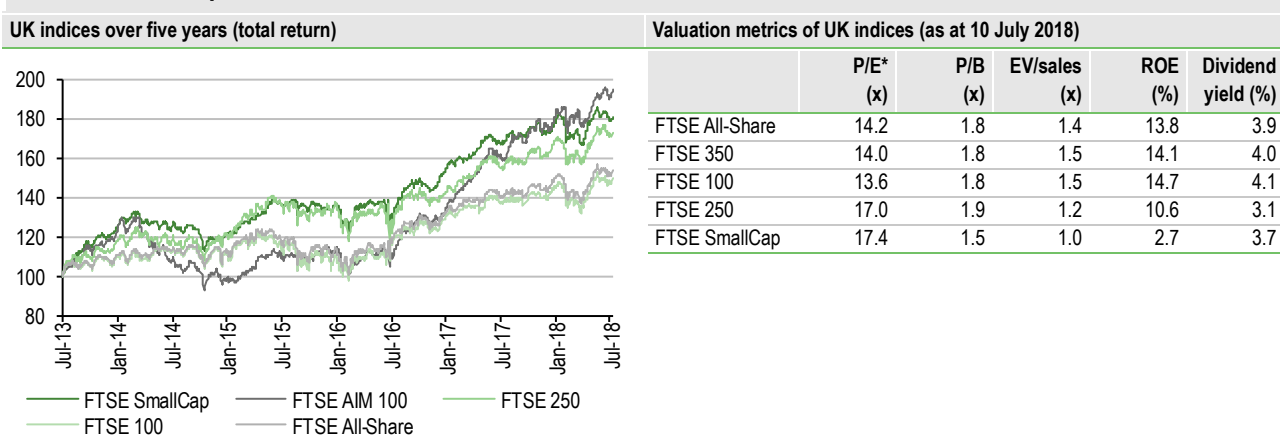
Company	Sector	Portfolio weight %	
		31 May 2018	31 May 2017*
BP	Oil & gas producers	3.4	N/A
Rio Tinto	Mining	3.4	N/A
John Laing	Financial services	3.4	N/A
Royal Dutch Shell	Oil & gas producers	3.3	N/A
GVC	Travel & leisure	3.2	N/A
Aviva	Life insurance	2.9	3.8
Prudential	Life insurance	2.8	2.7
Premier Asset Management	Financial services	2.7	N/A
HSBC	Banks	2.7	N/A
Close Brothers	Banks	2.6	2.4
Top 10 (% of holdings)		30.4	25.9

Source: Standard Life Equity Income Trust, Edison Investment Research, Bloomberg, Morningstar. Note: *N/A where not in end-May 2017 top 10.

Market outlook: Benefits from smaller-cap investing

The potential benefit to investors from investing in smaller-cap stocks is shown in Exhibit 2 (left-hand side). Over the past five years, the FTSE 250, SmallCap and AIM 100 indices have all meaningfully outperformed the large-cap FTSE 100 index. While large-cap stocks are generally trading at more favourable valuations than smaller-cap companies (right-hand table), they do not have such attractive growth profiles and dividend cover is lower. Although there are economic uncertainties, including ongoing Brexit negotiations, for investors seeking exposure to UK equities, a fund invested across the capitalisation spectrum, with a bias to smaller-cap companies and a focus on income, may be of interest.

Exhibit 2: Market performance and valuation



Source: Thomson Datastream, Edison Investment Research, Bloomberg. Note: *P/E is current, based on cash earnings.

Fund profile: Above-index exposure to smaller stocks

SLET was launched in 1991 and is traded on the Main Market of the London Stock Exchange. The trust aims to generate an above-average level of income, along with above-inflation growth in capital and income from a diversified portfolio of 50–70 UK equities. There are investment limits in place: no individual position will exceed 10% of net assets and the top 10 holdings are limited to 50% of net assets. SLET operates between net gearing of 15% and net cash of 5%; at end-May 2018, net gearing was 11.8%. The trust has been sole-managed by Thomas Moore since May 2012 (having been co-manager for the previous six months). He adopts an unconstrained investment approach, meaning that the trust's stock and sector weightings can vary significantly versus the index. For example, c 45% of the portfolio is invested in financial stocks compared to a c 25% weighting in the benchmark FTSE All-Share index. SLET also has a much higher weighting to mid- and small-cap stocks, c 70%, which compares to c 20% in the benchmark. The board believes that a focus on undervalued income stocks, whose positive fundamentals are being overlooked by the majority of investors, as well as an unconstrained investment approach, will generate good medium- and long-term returns for shareholders.

The fund manager: Thomas Moore

The manager's view: Finding attractive opportunities

Moore is positive on the investment backdrop in the UK, due to a benign interest rate environment, domestic and global economic growth, and robust corporate earnings growth. While mindful of macroeconomic risks such as ongoing Brexit negotiations and the impact of a trade war, he says

there are sectors and individual companies, with attractive fundamentals, that are trading on reasonable valuations. Moore notes that so far in 2018, there has been a polarisation within the UK stock market – investors have been focused on growth rather than value stocks. This has affected SLET's investment performance as it follows the investment manager's Focus on Change investment philosophy, which seeks companies with strong cash flow and dividend prospects that have potential for a rerating.

The manager says that in general, companies are delivering on what they have set out to achieve. However, due to investors' focus on growth stocks, not all companies delivering positive results are enjoying an uplift in valuations. Moore notes that looking at SLET's Q218 performance attribution, the companies that have been the largest detractors have not actually delivered any negative news. He remains confident in the prospects for the trust's portfolio companies and believes the general lack of focus on valuations is providing attractive investment opportunities.

Asset allocation

Investment process: Focus on Change approach

Moore and his team employ an unconstrained investment approach. They seek to invest in undervalued companies, whose share prices do not reflect positive fundamentals or the potential for improvement. Meeting company management is a key element of the investment process; members of the investment team conduct more than 3,000 company meetings each year. They look to uncover changing dynamics within individual companies and the markets in which they operate, which could lead to an increase in a firm's earnings and dividends. An improvement in investor sentiment towards a company will invariably lead to a higher valuation being placed on the business. The Focus on Change investment philosophy is based on the theory that at different stages of the economic cycle, there are different drivers of stocks and markets. The belief is that over the long term, a company's share price is driven by its underlying fundamentals but share price moves can be less rational over shorter time periods. Aberdeen Standard Investments has a proprietary stock matrix to screen the c 1,500-company universe; factors include earnings growth and revisions, share price momentum and valuation. Companies passing the stock selection screen are then subject to in-depth analysis taking into account the following five considerations:

- What are the key drivers and issues for this stock?
- What is changing?
- What is assumed in the price?
- What will make the market change its mind about this stock?
- What are the specific triggers?

The unconstrained investment approach means that SLET's stock and sector weightings vary considerably compared with those in the benchmark FTSE All-Share index. Individual weightings reflect Moore's level of conviction, which is based on an assessment of a company's management team, its strategy, business prospects and valuation. The manager notes there can be significant opportunities in companies that are under-researched by buy- and sell-side analysts. An evaluation of a company's corporate governance track record is an increasingly important part of the investment process; evidence suggests that companies that align their interests with those of shareholders may achieve above-average returns. The investment manager is aware of the need to measure portfolio risk; the company has a sophisticated risk-modelling system, which includes pre-trade analysis.

Current portfolio positioning

At the end of May 2018, SLET's top 10 positions made up 30.4% of the portfolio, which was an increase in concentration compared with 25.9% a year earlier. The manager's unconstrained

investment approach is illustrated in Exhibits 1 and 3; for example, only c 30% of the portfolio is invested in large-cap FTSE 100 stocks and the trust's sector exposures are meaningfully different to those in the index. Most notable are the c 20pp overweight in financials and the c 10pp underweight positions in consumer goods.

Exhibit 3: Portfolio sector exposure vs benchmark (% unless stated)						
	Portfolio end-May 2018	Portfolio end-May 2017	Change (pp)	Index weight	Active weight vs index (pp)	Trust weight/index weight (x)
Financials	46.2	38.3	7.9	26.0	20.2	1.8
Industrials	15.1	16.1	(1.0)	11.3	3.8	1.3
Consumer services	13.1	16.8	(3.7)	11.7	1.4	1.1
Oil & gas	9.2	2.4	6.9	14.0	(4.7)	0.7
Basic materials	5.1	4.8	0.3	7.9	(2.9)	0.6
Consumer goods	3.9	11.4	(7.5)	13.8	(9.9)	0.3
Technology	2.9	5.3	(2.5)	1.0	1.9	3.0
Utilities	1.9	1.9	0.0	2.6	(0.8)	0.7
Telecommunications	1.6	3.0	(1.4)	2.9	(1.3)	0.5
Healthcare	1.0	0.0	1.0	8.8	(7.8)	0.1
	100.0	100.0		100.0		

Source: Standard Life Equity Income Trust, Edison Investment Research. Note: Adjusted for cash and gearing.

Looking at some of SLET's recent new holdings illustrates the manager's index-agnostic approach. Moving down the market cap spectrum means he is able to find more companies with attractive valuations and growth potential.

Charles Taylor (AIM listed, market cap of c £235m) provides insurance administration services such as claims management. The manager says the company's InsureTech platform is a significant potential organic driver for the company. He believes Charles Taylor has an attractive growth profile and is trading at an attractive valuation.

Diversified Gas & Oil (AIM listed, market cap of c £375m) acquires gas assets in the Appalachian region. It is able to purchase these at attractive valuations as the major oil companies are selling their conventional assets to focus on shale operations. Diversified Gas & Oil's increased scale means operating expenses per barrel are coming down dramatically. The manager says the company's latest acquisition (announced in June 2018) is 30% accretive to earnings; the announcement of the deal led to significant share price appreciation.

Urban Exposure (AIM listed, market cap of c £180m) is a lender in the residential development sector. Since the global financial crisis, banks have been required to build up significant capital on their balance sheets, which has allowed companies such as Urban Exposure to grow their lending expertise without having the same capital requirements. SLET participated in the company's initial public offering in May 2018.

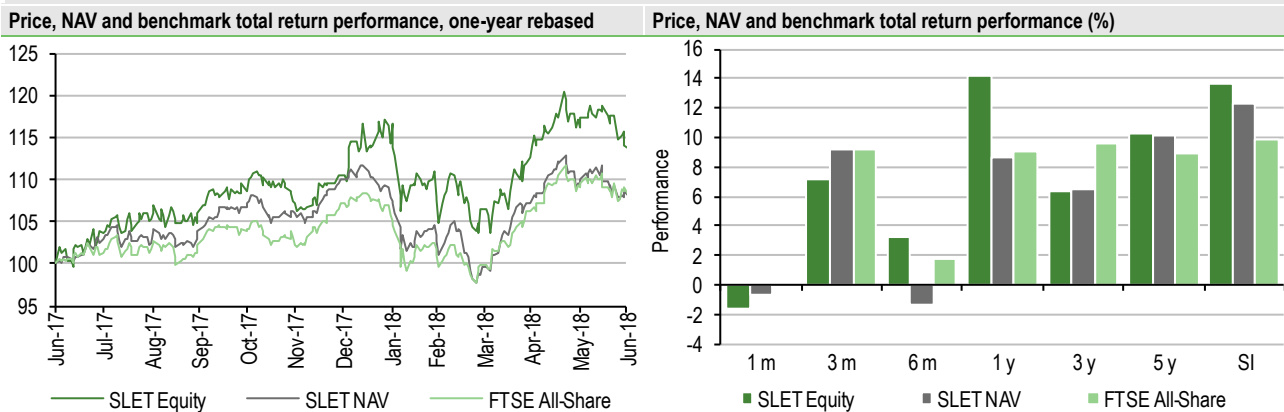
Recent sales include drinks manufacturer Britvic, house builder Countryside Properties and packaging company DS Smith, which had all appreciated strongly, meaning the manager no longer considered their valuations attractive. Vodafone was sold as Moore believes the gap between the company's cash flow and its dividend payment is insufficient for him to have confidence in a higher distribution.

Performance: Share price outperforming NAV

In H118 (ending 31 March), SLET's NAV and share price total returns of -4.3% and +0.4% compared with the benchmark's -2.3% total return. This period included a sharp pullback in equities during February and March due to concerns about higher US interest rates, with the FTSE All-Share index falling by c 11%. The best contributors to performance included small-cap investment managers Premier Asset Management and AFH Financial Group, along with emerging market debt

manager Ashmore Group. The largest negative contributor was Micro Focus, which issued a profit warning due to integration problems following its merger with HPE Software; the manager believes these issues are temporary and he continues to hold a position in the stock.

Exhibit 4: Investment trust performance to 30 June 2018



Source: Thomson Datastream, Edison Investment Research. Note: Three and five years, and since inception performance figures annualised. Since inception (SI) refers to tenure of Thomas Moore, appointed as manager on 11 November 2011.

SLET's relative performance is shown in Exhibit 5. Its NAV total return has outperformed the benchmark over five years and since Moore was appointed manager in November 2011, while lagging appreciably over three years and modestly over one year. As shown in Exhibit 6, the trust's three-year performance was negatively affected by its exposure to companies with domestic earnings following the result of the UK's European referendum in June 2016.

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

	One month	Three months	Six months	One year	Three years	Five years	SI
Price relative to FTSE All-Share	(1.5)	(1.9)	1.5	4.7	(8.5)	6.4	25.1
NAV relative to FTSE All-Share	(0.5)	(0.0)	(2.9)	(0.3)	(8.4)	5.8	15.8
Price relative to FTSE 100	(1.4)	(2.2)	1.6	5.0	(8.7)	9.4	31.8
NAV relative to FTSE 100	(0.4)	(0.4)	(2.9)	(0.0)	(8.6)	8.8	22.1
Price relative to FTSE 250	(1.8)	(0.8)	1.3	3.3	(6.5)	(5.7)	(2.7)
NAV relative to FTSE 250	(0.8)	1.0	(3.1)	(1.7)	(6.4)	(6.2)	(9.9)

Source: Thomson Datastream, Edison Investment Research. Note: Data to end-June 2018. Geometric calculation.

Exhibit 6: NAV total return performance relative to benchmark over five years



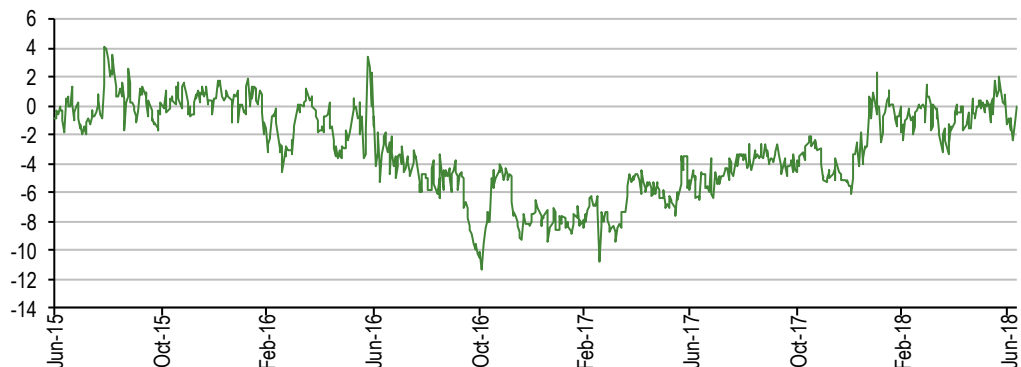
Source: Thomson Datastream, Edison Investment Research

Discount: Return to trading close to NAV

Over the last three years, SLET's widest discount to cum-income NAV was 11.3% on 3 November 2016, when there were stock market jitters ahead of the US presidential election. The trust's discount has since narrowed and, so far in 2018, its shares have traded close to NAV. The current

0.1% discount is narrower than the historical averages over the last one, three, five and 10 years (range of 2.4% to 3.9%).

Exhibit 7: Share price premium/discount to NAV (including income) over three years (%)



Source: Thomson Datastream, Edison Investment Research

Capital structure and fees

SLET is a conventional investment trust with one class of share; there are currently 49.2m ordinary shares in issue. The trust has a £30m lending facility with Scotiabank (Ireland); at end-May 2018, net gearing was 11.8%. The debt facility expires in December 2018, and the annualised cost of borrowing in H118 was 1.31%.

The investment manager is paid an annual management fee of 0.65% on the first £250m and 0.55% of total assets above £250m. Prior to October 2016, the fee was a flat 0.65%. Costs are split 30:70 between the revenue and capital accounts respectively, reflecting the board's expectation of the allocation of long-term returns between income and capital. In FY17, ongoing charges were 0.87%, which was 9bp lower than in FY16.

Dividend policy and record

SLET pays dividends quarterly in March, June, September and January. Along with the announcement in February 2018 of the first 4.4p per share interim dividend, the board stated its intention to pay the same amount for the second and third interim dividends and a higher final dividend of at least 5.5p per share. This minimum 18.7p per share distribution in FY18 is 9.4% higher than the 17.1p per share paid in FY17; the board expects the larger dividend to be fully covered by current-year earnings. The forecast dividend growth is meaningfully higher than the 6.0% compound annual growth over the last five years, as well as compared with the rate of UK inflation over the period. A higher total dividend in FY18 would mark the 18th consecutive annual increase. Revenue reserves have built significantly since 2011; at end-FY17 they were £6.7m (after taking into account the third and fourth interim dividends). This is equivalent to c 0.8x the total FY17 dividend payment. Based on its current share price, SLET has a dividend yield of 3.8%.

Peer group comparison

Exhibit 8 shows the 15 largest members of the AIC UK Equity Income sector; SLET is one of the smallest trusts in the selected peer group. Its NAV total return is above average over one and five years, while trailing over three and 10 years. The trust experienced a period of meaningful underperformance following the UK's European referendum in 2016, as a result of its high exposure

to companies with domestic, rather than international, operations. SLET is once again finding favour with investors, who may be encouraged by the board's commitment to higher dividend growth, and has returned to trading close to NAV (Exhibit 7). The trust's ongoing charge and level of gearing are higher than the selected peer average, and it has an above-average dividend yield, ranking eighth out of 15 trusts.

Exhibit 8: Selected peer group as at 10 July 2018*

% unless stated	Market cap £m	NAV TR 1 year	NAV TR 3 year	NAV TR 5 year	NAV TR 10 year	Discount (ex-par)	Ongoing charge	Perf. fee	Net gearing	Dividend yield (%)
Standard Life Equity Income	240.9	8.4	21.1	54.5	152.0	1.5	0.9	No	112	3.8
City of London	1,545.4	6.8	25.7	46.6	151.5	1.7	0.4	No	108	4.2
Diverse Income Trust	398.8	8.7	32.1	84.2		0.5	1.2	No	100	3.1
Dunedin Income Growth	384.4	4.7	26.9	34.7	114.5	(10.8)	0.6	No	120	4.9
Edinburgh Investment Trust	1,351.7	0.0	22.6	50.2	165.9	(9.4)	0.6	No	111	3.9
F&C Capital & Income	337.5	10.2	42.9	58.9	128.7	1.1	0.6	No	104	3.2
Finsbury Growth & Income	1,394.7	16.7	50.3	88.9	371.1	1.0	0.7	No	102	1.8
JPMorgan Claverhouse	424.5	11.8	35.0	58.6	136.7	(1.7)	0.8	No	112	3.6
Lowland	418.8	6.0	29.8	55.5	226.1	(5.0)	0.6	Yes	114	3.4
Merchants Trust	580.6	16.6	34.1	43.6	133.7	(6.0)	0.6	No	114	4.8
Murray Income Trust	528.7	5.1	30.0	39.5	128.5	(7.1)	0.7	No	103	4.1
Perpetual Income & Growth	870.4	0.1	12.7	39.5	159.4	(11.8)	0.7	No	112	3.8
Schroder Income Growth	204.7	8.7	28.7	55.8	165.9	(7.3)	1.0	No	107	4.2
Temple Bar	886.7	9.2	30.5	42.7	220.9	(5.7)	0.5	No	103	3.2
Troy Income & Growth	222.1	4.2	25.3	51.6	90.8	(1.1)	0.9	No	100	3.4
Average	652.7	7.8	29.9	53.7	167.5	(4.0)	0.7		108	3.7
SLET rank (out of 15 funds)	13	8	14	7	7	2	4		4	8

Source: Morningstar, Edison Investment Research. Note: *Performance as at 9 July 2018. TR = total return. Net gearing is total assets less cash and equivalents as a percentage of net assets.

The board

There are five directors on SLET's board, all of whom are non-executive and independent of the manager. The chairman is Richard Burns, who was appointed as a director in 2006 and assumed his current role in 2014. The four other directors and their year of appointment are: Jeremy Tigue (2014 and senior independent director from 2015), Josephine Dixon (2011), Mark White (2013) and Caroline Hitch (2017).

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