EDISON

# BlackRock Sustainable American Income Trust

## Unique value/ESG fund at an attractive valuation

Investment trusts
American equities

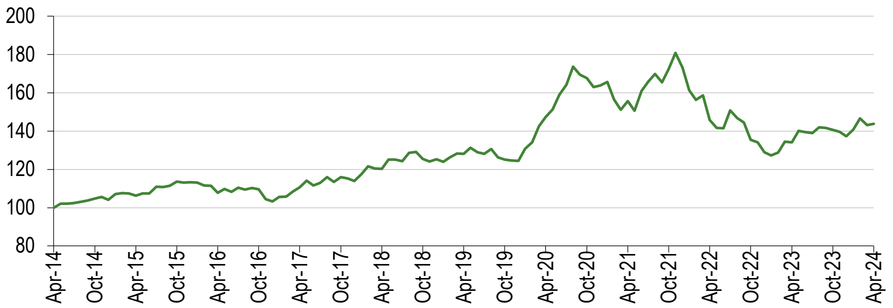
**9 May 2024**

| | | |
|---|---|---|
| **Price** | | **203.0p** |
| **Market cap** | | **£156m** |
| **Total assets** | | **£174m** |

| | | |
|---|---|---|
| NAV* | | 222.7p |
| Discount to NAV | | 8.8% |
| *Including income. At 7 May 2024. | | |
| Yield | | 3.9% |
| Ordinary shares in issue | | 77.0m |
| Code/ISIN | | BRSA/GB00B7W0XJ61 |
| Primary exchange | | LSE |
| AIC sector | | North America |
| Financial year end | | 31 October |
| 52-week high/low | 203.0p | 174.0p |
| NAV* high/low | 224.8p | 190.6p |
| *Including income. | | |
| Net gearing* | | 1.3% |
| *At 31 March 2024. | | |


**BlackRock Sustainable American Income Trust (BRSA) offers a unique opportunity to invest in a fund that focuses on both value and sustainability. The trust's three managers, Tony DeSpirito, David Zhao and Lisa Yang, aim to deliver an attractive level of income and long-term capital growth from a portfolio of attractively valued, high-quality, dividend-paying companies, which have favourable ESG credentials either as leaders, improvers or 'sustainability enablers'. BRSA's managers are finding attractive opportunities due to the historically wide valuation gap between value stocks and the broad US market. Data from BlackRock show that since 1978, following a peak in the interest rate cycle, which is the consensus outcome given moderating US inflation, quality stocks outperformed over the subsequent one, two and three years; this should also bode well for the trust's relative performance.**


**S&P 500 Growth Index/S&P 500 Value Index (total return) over last decade**




Source: LSEG, Edison Investment Research

## Why consider BRSA?

The trust is unique among the seven funds in the AIC North America sector, with its focus on companies with intrinsic values that are not fully captured in their share prices and that have favourable ESG scores. Comparing BRSA's portfolio characteristics versus those of the reference index, they have similar yields, but the trust has higher growth and quality attributes at a lower valuation.

Due to the quality and value investment approach, BRSA's portfolio is relatively defensive. This is illustrated by the upside/downside capture analysis later in the report, which show that the fund's performance should be relatively resilient during periods of stock market weakness, although it may not capture the full upside when markets rise.

The trust has considerable distributable reserves, which allows the board to continue to pay an 8.0c annual dividend. This equates to an attractive above-market 3.9% yield. BRSA's current 8.8% discount compares to a range of a 1.3% premium to a 13.6% discount over the last three years. It is wider than the 4.6% to 8.6% range of average discounts over the last one, three, five and 10 years. There is scope for a higher valuation in a more settled economic environment or if the trust's relative performance improves.

### Fund objective

BlackRock Sustainable American Income Trust (BRSA) aims to provide an attractive level of income and capital appreciation over the long term in a manner that is consistent with the trust's principles of sustainable investing. Performance is measured against a US 1000 value index (the reference index).

### Bull points

- The fund offers exposure to a specialist US multi-cap value portfolio with an ESG focus.
- Attractive dividend yield.
- Well-positioned to take advantage of broader stock market leadership.

### Bear points

- FY23 dividend was not fully covered by income.
- Reference index is not ESG based.
- US market is trading at a premium to global equities.

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**NOT INTENDED FOR PERSONS IN THE EEA**

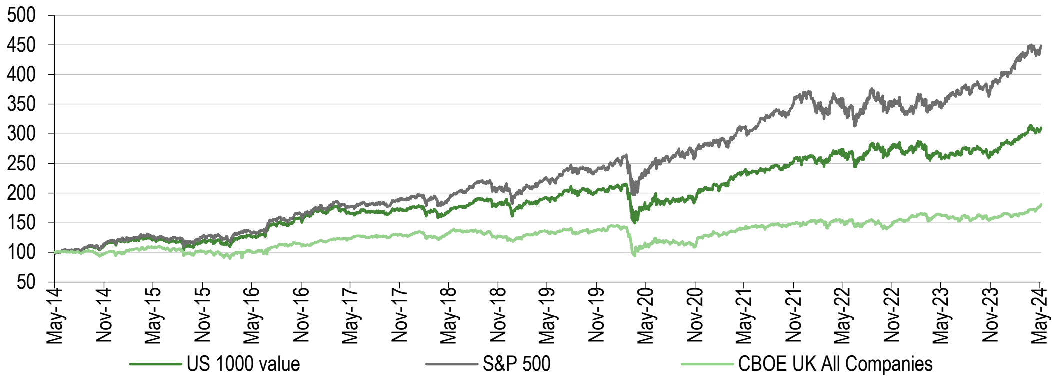
# BRSA: A unique combination of value and ESG factors

BRSA has a dual objective to outpace the performance of, and to ensure that its portfolio ESG characteristics (as measured by MSCI) are higher than those of its reference index. With its focus on bottom-up stock selection, the trust is well positioned to take advantage of a stock market that is driven by company fundamentals rather than macroeconomic developments. While the US market was led by the 'magnificent seven' technology stocks in 2023 (Apple, Amazon.com, Alphabet, Microsoft, Meta Platforms, Nvidia and Tesla), they are suffering mixed fortunes in 2024. A broader market leadership should also be beneficial for BRSA's performance.

## Market performance and valuation

The S&P 500 has performed significantly better than both US value stocks and the UK market over the last decade. A large part of this has been due to the outperformance of large-cap technology shares, which were particularly strong in 2023 helped by their exposure to artificial intelligence (AI), which is deemed to have significant, long-term growth potential.

**Exhibit 1: Performance of indices over the last decade (£)**




Source: LSEG, Edison Investment Research

**Exhibit 2: S&P 500 Index sector total returns ($)**

| % | 4M24* | % | 2023 | | 2022 | | 2021 | | 2020 |
|---|---|---|---|---|---|---|---|---|---|
| Comm'n services | 13.4 | IT | 57.8 | Energy | 65.4 | Energy | 54.4 | IT | 43.9 |
| Energy | 12.8 | Comm'n services | 55.8 | Utilities | 1.6 | Real estate | 46.1 | Cons discretionary | 33.3 |
| Financials | 7.8 | Cons discretionary | 42.3 | Consumer staples | (0.6) | Financials | 34.9 | Comm'n services | 23.6 |
| Industrials | 7.0 | Industrials | 18.1 | Healthcare | (2.0) | IT | 34.5 | Materials | 20.7 |
| IT | 6.6 | Materials | 12.6 | Industrials | (5.5) | Materials | 27.3 | Healthcare | 13.5 |
| Consumer staples | 6.6 | Real estate | 12.3 | Financials | (10.6) | Healthcare | 26.1 | Industrials | 11.1 |
| Utilities | 6.3 | Financials | 12.1 | Materials | (12.3) | Cons discretionary | 24.4 | Consumer staples | 10.8 |
| Materials | 4.0 | Healthcare | 2.1 | Real estate | (26.2) | Comm'n services | 21.6 | Utilities | 0.5 |
| Healthcare | 3.3 | Consumer staples | 0.5 | IT | (28.2) | Industrials | 21.1 | Financials | (1.8) |
| Cons discretionary | 0.4 | Energy | (1.4) | Cons discretionary | (37.0) | Consumer staples | 18.6 | Real estate | (2.2) |
| Real estate | (9.0) | Utilities | (7.1) | Comm'n services | (39.9) | Utilities | 17.7 | Energy | (33.7) |
| **Total** | **6.0** | **Total** | **26.3** | **Total** | **(18.1)** | **Total** | **28.7** | **Total** | **18.4** |

Source: Bloomberg. Note: *To 30 April 2024.

The valuation of the broad US market continues to look unappealing. As shown in Exhibit 3, using Datastream indices, on a forward P/E basis the US is trading at a c 24% premium to the world market, and its 20.5x multiple is a 13% premium to its 10-year average. The US is also trading on a much higher price-to-book multiple than the world market. Although the US market has a superior return on equity, it offers a meaningfully lower dividend yield.

Exhibit 3: Valuation metrics of Datastream indices (at 8 May 2024)

| | Last | High | Low | 10-year average | Last as % of average |
|---|---|---|---|---|---|
| **US** | | | | | |
| P/E 12 months forward (x) | 20.5 | 23.4 | 14.0 | 18.2 | 113 |
| Price to book (x) | 4.5 | 4.6 | 2.3 | 3.3 | 137 |
| Dividend yield (%) | 1.4 | 2.7 | 1.2 | 1.8 | 76 |
| Return on equity (%) | 16.1 | 18.6 | 9.9 | 14.2 | 113 |
| | | | | | |
| **World** | | | | | |
| P/E 12 months forward (x) | 16.6 | 19.9 | 12.5 | 15.7 | 106 |
| Price to book (x) | 2.3 | 2.3 | 1.4 | 1.9 | 122 |
| Dividend yield (%) | 2.2 | 3.4 | 1.8 | 2.4 | 90 |
| Return on equity (%) | 12.3 | 14.0 | 7.4 | 11.3 | 109 |

Source: LSEG, Edison Investment Research

## Perspectives from one of BRSA's managers

Yang says that although BRSA's stock selection is on a bottom-up basis, the managers do consider the macroeconomic background. She notes that the US economy has held up well, helped by COVID-19 stimulus, and the labour market has remained strong. The manager believes that the US is in the later stages of the current economic cycle, and there is a risk that higher wages could put upward pressure on inflation (keeping it above the targeted 2.0% level), limiting the Federal Reserve's ability to reduce interest rates. Yang considers this scenario presents a risk to the US stock market, as the consensus expectation is for lower interest rates.

The manager highlights that the current forward P/E multiple of the US market is notably above its long-term average. However, she sees opportunities in US value stocks, which are trading at a record discount to the overall market. Yang points to a recent publication by BlackRock that suggests while passive investment has been increasingly favoured by investors, going forward, active management will be more important. Following the global financial crisis and before the onset of COVID-19, there was a unique period known as the great moderation, where interest rates, inflation and stock market volatility were low, and there was a narrow dispersion of equity returns. The manager anticipates increased stock market volatility and a higher dispersion between equity returns, due to sticky inflation, higher interest rates and other factors including geopolitics and decarbonisation, which she says makes a strong case for active versus passive investment.

Yang highlights that looking back to 1975, following a peak in interest rates there has been a subsequent recession. With the valuation gap between the reference index and the bellwether S&P 500 Index at the widest point versus history, the manager sees opportunities to invest in high-quality stocks with strong cash flows, robust balance sheets and well-regarded management teams. Yang says that high-quality and low-beta stocks tend to outperform following interest rate hiking cycles and she is finding examples of these types of stocks in the consumer staples and healthcare sectors that are trading on lower valuation multiples than their 1996–2023 historical averages. This suggests that investors are not positioned for a stock market downturn.

### Current portfolio positioning

Exhibit 4 shows BRSA's geographic exposure. Over the 12 months to the end of March 2024, there is a notably higher allocation to US stocks (+7.2pp). This was partially offset by the disposal of the trust's Japanese stocks (-3.9pp) and a lower UK weighting (-2.3pp).

**Exhibit 4: Portfolio geographic exposure (% unless stated)**

| | Portfolio end-March 2024 | Portfolio end-March 2023 | Change (pp) |
|---|---|---|---|
| US | 89.1 | 81.9 | 7.2 |
| UK | 5.1 | 7.4 | (2.3) |
| France | 2.0 | 2.6 | (0.6) |
| South Korea | 1.5 | 0.0 | 1.5 |
| Australia | 1.2 | 1.7 | (0.5) |
| Switzerland | 1.1 | 0.0 | 1.1 |
| Japan | 0.0 | 3.9 | (3.9) |
| Canada | 0.0 | 1.4 | (1.4) |
| Denmark | 0.0 | 1.0 | (1.0) |
| | **100.0** | **100.0** | |

Source: BRSA, Edison Investment Research. Note: Rebased for net current assets/liabilities.

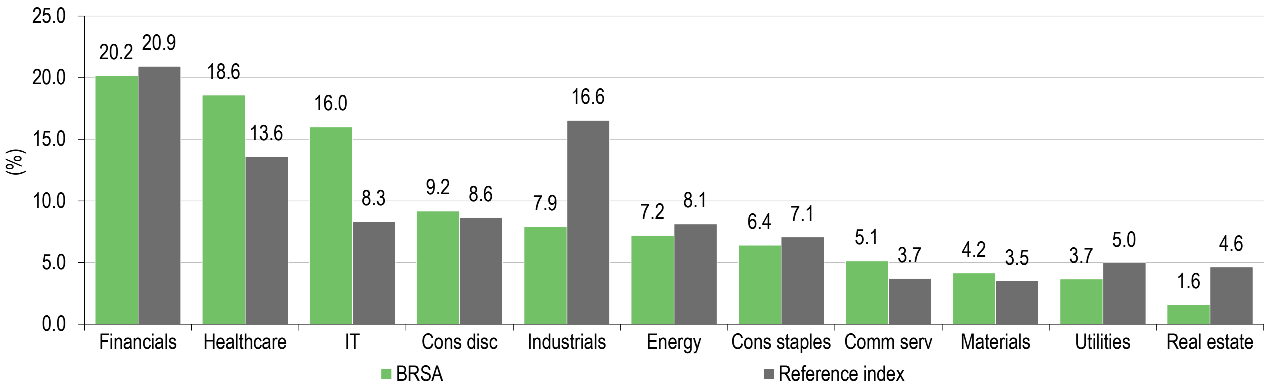
While the US market provides a wide opportunity set, Yang says that with this market trading at a premium valuation multiple to its historical average, better opportunities may be found overseas. She highlights the global pharma industry, where US companies are facing declining revenues due to an impending patent cliff, so they need to invest to bolster their product pipelines. The manager contrasts this with European pharma companies, whose revenues are expected to rise over the next decade based on their base revenues, with any successful product launches providing incremental sales.

**Exhibit 5: Portfolio sector exposure versus reference index (% unless stated)**

| | Portfolio end-March 2024 | Portfolio end-March 2023 | Change (pp) | Active weight vs index (pp) |
|---|---|---|---|---|
| Financials | 20.2 | 19.1 | 1.1 | (0.8) |
| Healthcare | 18.6 | 20.7 | (2.1) | 5.0 |
| Information technology | 16.0 | 15.3 | 0.7 | 7.7 |
| Consumer discretionary | 9.2 | 10.3 | (1.1) | 0.6 |
| Industrials | 7.9 | 6.2 | 1.7 | (8.6) |
| Energy | 7.2 | 8.7 | (1.5) | (0.9) |
| Consumer staples | 6.4 | 6.2 | 0.2 | (0.6) |
| Communication services | 5.1 | 4.3 | 0.8 | 1.4 |
| Materials | 4.2 | 3.6 | 0.5 | 0.6 |
| Utilities | 3.7 | 4.1 | (0.5) | (1.3) |
| Real estate | 1.6 | 1.4 | 0.2 | (3.0) |
| | **100.0** | **100.0** | | |

Source: BRSA, Edison Investment Research. Note: Rebased for net current assets/liabilities.

**Exhibit 6: BRSA's sector exposure versus its reference index at end-March 2024**




Source: BRSA, Edison Investment Research. Note: Numbers subject to rounding.

There were modest changes in BRSA's sector exposure in the 12 months to the end of March 2024 (Exhibit 5). Yang explains that the trust has been overweight healthcare stocks for a long time because of the industry's structural growth drivers, which are supported by an ageing global population. BRSA's largest overweight position is technology. An increasing number of stocks in this sector are what the managers refer to as industrial technology, which are companies with defensible competitive positions, well positioned to take advantage of long-term growth opportunities and are generating strong earnings and cash flow. This has led to a growing number of technology companies paying dividends to shareholders. The trust retains a notable underweight exposure to industrial stocks given the advanced stage of the current economic cycle and generally unattractive valuations. Other underweight sectors include real estate as these stocks are unattractively valued and utilities because the managers consider that climate change risks are not priced into these companies' stock prices.

At the end of March 2024, BRSA's top 10 holdings made up 26.1% of the portfolio, which was a modestly lower concentration compared with 27.3% a year before; five positions were common to both periods.

**Exhibit 7: Top 10 holdings (at 31 March 2024)**

| Company | Country | Sector | Portfolio weight % | |
|---|---|---|---|---|
| | | | 31 March 2024 | 31 March 2023* |
| Citigroup | US | Financials | 3.6 | 2.6 |
| American International Group | US | Financials | 3.0 | N/A |
| Shell | UK | Energy | 2.6 | 2.6 |
| Kraft Heinz | US | Consumer staples | 2.5 | N/A |
| Cardinal Health | US | Healthcare | 2.5 | N/A |
| Baxter International | US | Healthcare | 2.4 | 2.5 |
| Johnson Controls International | US | Industrials | 2.4 | N/A |
| Cisco Systems | US | Information technology | 2.4 | 3.0 |
| Verizon Communications | US | Communication services | 2.4 | 2.6 |
| Fidelity National Information Services | US | Information technology | 2.3 | N/A |
| **Top 10 (% of portfolio)** | | | **26.1** | **27.3** |

Source: BRSA, Edison Investment Research. Note: *N/A where not in end-March 2023 top 10.

Comparing BRSA's portfolio with the reference index at the end of January 2024, it had a similar gross dividend yield and considerably higher dividend growth. Its return on equity and forward earnings growth outlook was modestly lower but the portfolio was more attractively valued at a c 20% discount to the reference index and a much wider discount versus the US market.

**Exhibit 8: Portfolio characteristics at 31 January 2024**

| | Portfolio | Reference index | Difference (%) |
|---|---|---|---|
| Number of holdings | 60 | 846 | (92.9) |
| Gross dividend yield (%) | 2.4 | 2.3 | 0.1 |
| Dividend growth (5Y annualised, %) | 8.2 | 5.4 | 2.8 |
| Return on equity (%) | 13.8 | 12.8 | 1.0 |
| Forward EPS growth (%) | 10.7 | 10.0 | 0.7 |
| Forward P/E multiple (x) | 12.7 | 15.8 | (19.6) |

Source: BRSA, Edison Investment Research

### Recent portfolio transactions

As normal, in Q124, portfolio activity occurred across a range of industries. The largest purchases included: Avnet (electronic products distribution); Diageo (UK-based, alcoholic beverages); PG&E (electric and natural gas utility); Sensata Technologies (sensors); WPP (UK-based, communications and advertising); and Westinghouse Air Brake Technologies (transportation equipment).

The following positions were sold: Acuity Brands (lighting and building management); First American Financial (financial services); Gildan Activewear (Canada-based, apparel); Komatsu (Japan-based, construction, mining & utility equipment); Mattel (toys); Nestlé (Switzerland-based, food & beverages); and TransUnion (consumer credit ratings).

## Performance: Hurt by Meta joining the reference index

There are seven companies in the AIC North America sector; five US and two Canadian funds, which can also invest in US equities. The companies all have different investment mandates; BRSA is unique with its value and ESG focus. Its NAV total returns are above average over the last three years, ranking third, and below average over the last one, five and 10 years. An analysis using Morningstar data shows that BRSA's closest peer is abrdn's North American Income Trust (NAIT); they are the only two companies in the sector designated as large-cap value funds. BRSA's returns are superior to NAIT's over all periods shown in Exhibit 9. It has the second-highest valuation in the sector, behind JPMorgan American, which is trading at a small premium. BRSA has an average ongoing charge and a below-average level of gearing. The trust has an attractive dividend yield, which is the third highest in the peer group and 1.4pp above the sector average.

**Exhibit 9: AIC North America sector at 8 May 2024***

| % 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 |
|---|---|---|---|---|---|---|---|---|---|---|
| BlackRock Sustainable American Income | 156.3 | 17.5 | 24.8 | 59.3 | 199.3 | (9.3) | 1.0 | No | 101 | 3.9 |
| Baillie Gifford US Growth | 597.0 | 28.9 | (21.1) | 78.4 | | (9.6) | 0.7 | No | 105 | 0.0 |
| Canadian General Investments | 451.5 | 17.0 | 18.5 | 95.4 | 209.6 | (40.6) | 1.4 | No | 111 | 2.6 |
| JPMorgan American | 1,805.2 | 35.3 | 44.4 | 117.9 | 361.2 | 0.6 | 0.4 | No | 104 | 0.8 |
| Middlefield Canadian Income | 112.9 | 2.6 | 14.8 | 43.7 | 81.8 | (13.8) | 1.3 | No | 120 | 4.9 |
| North American Income Trust | 393.7 | 13.9 | 20.5 | 39.4 | 176.5 | (13.8) | 0.9 | No | 102 | 4.0 |
| Pershing Square Holdings | 7,673.2 | 28.7 | 54.3 | 214.7 | | (23.8) | 1.6 | Yes | 103 | 1.1 |
| **Simple average (7 funds)** | **1,598.5** | **20.6** | **22.3** | **92.7** | **205.7** | **(15.8)** | **1.0** | | **107** | **2.5** |
| **BRSA rank in peer group** | **6** | **4** | **3** | **5** | **3** | **2** | **4** | | **7** | **3** |

Source: Morningstar, Edison Investment Research. Note: *Performance at 7 May 2024 based on ex-par NAV. TR, total return. Net gearing is total assets less cash and equivalents as a percentage of net assets.

BRSA's relative returns are shown in Exhibit 10. The trust has underperformed its reference index since the 2021 strategy change. Yang explains that this is largely due to a single stock, Meta Platforms (formerly Facebook), which entered the reference index in 2023. Meta was not added to the portfolio as it did not meet acceptable ESG credentials; unfortunately, the company's share price rallied strongly, which negatively affected the trust's relative performance by c 150bp. Meta has since returned to the reference index's peer US 1000 growth index.

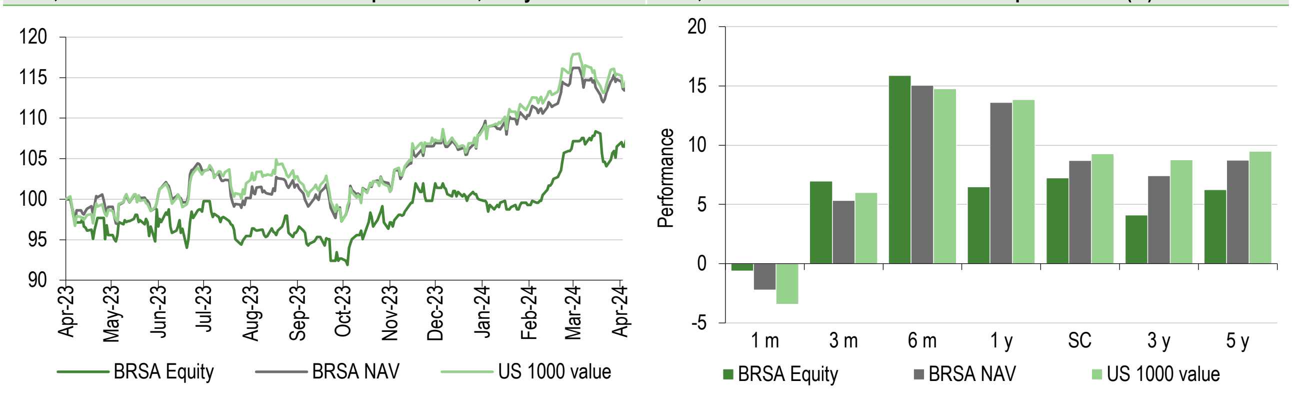
**Exhibit 10: Share price and NAV total return performance, relative to indices (%)**

| | One month | Three months | Six months | One year | SC | Three years | Five years |
|---|---|---|---|---|---|---|---|
| Price relative to US 1000 value index | 2.9 | 0.9 | 1.0 | (6.5) | (4.9) | (12.3) | (13.9) |
| NAV relative to US 1000 value index | 1.2 | (0.6) | 0.2 | (0.2) | (1.4) | (3.6) | (3.4) |
| Price relative to S&P 500 Index | 2.7 | 0.8 | (1.2) | (13.5) | (9.3) | (19.2) | (30.0) |
| NAV relative to S&P 500 Index | 1.0 | (0.7) | (1.9) | (7.7) | (6.0) | (11.2) | (21.5) |
| Price relative to CBOE UK All Cos | (2.9) | (0.5) | 1.5 | (0.8) | (2.0) | (10.0) | 4.0 |
| NAV relative to CBOE UK All Cos | (4.4) | (2.0) | 0.7 | 5.8 | 1.6 | (1.2) | 16.7 |

Source: LSEG, Edison Investment Research. Note: Data to end-April 2024. Geometric calculation. SC, since change in strategy on 30 July 2021.

**Exhibit 11: Investment trust performance to 30 April 2024**

**Price, NAV and reference index total return performance, one-year rebased** | **Price, NAV and reference index total return performance (%)**




Source: LSEG, Edison Investment Research. Note: Three- and five-year performance figures annualised. SC, since change in strategy on 30 July 2021.

**Exhibit 12: Five-year discrete performance data**

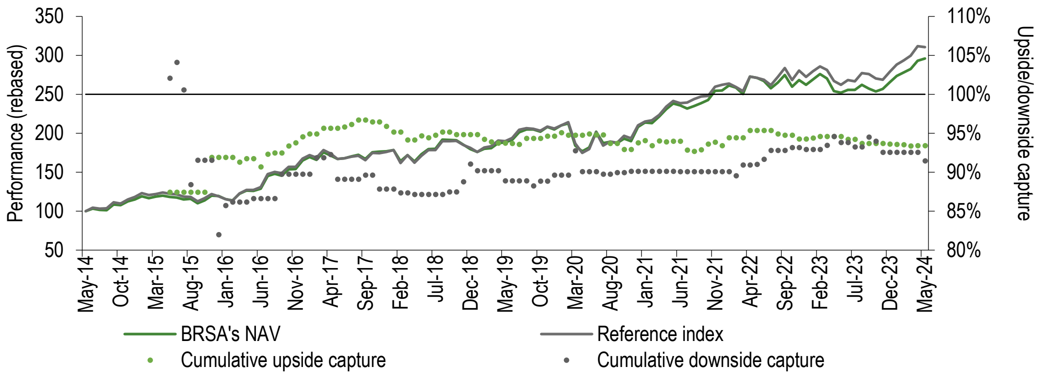
| 12 months ending | Share price (%) | NAV (%) | US 1000 value (%) | S&P 500 (%) | CBOE UK All Cos (%) |
|---|---|---|---|---|---|
| 30/04/20 | (7.3) | (5.4) | (8.0) | 4.2 | (17.2) |
| 30/04/21 | 29.4 | 29.5 | 32.9 | 33.0 | 25.3 |
| 30/04/22 | 10.5 | 12.6 | 11.7 | 10.5 | 9.1 |
| 30/04/23 | (4.1) | (3.1) | 1.1 | 2.5 | 7.0 |
| 30/04/24 | 6.5 | 13.6 | 13.9 | 23.1 | 7.4 |

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

### BRSA's upside/downside capture

Exhibit 13 shows BRSA's upside/downside capture over the last 10 years. The fund's defensive qualities are illustrated by its upside capture of 93% and downside capture of 92%, which are both less than 100%. These numbers suggest that the trust will capture around 10% less than the reference index's moves both in months when share prices rally and in months when they fall.

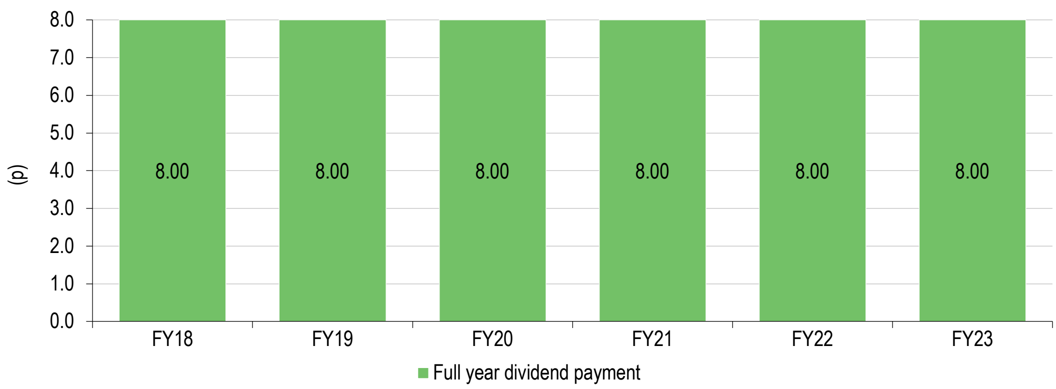
**Exhibit 13: BRSA's upside/downside capture**




Source: LSEG, Edison Investment Research. Note: Cumulative upside/downside capture calculated as the geometric average NAV total return (TR) of the fund during months with positive/negative reference index TRs, divided by the geometric average reference index TR during these months. A 100% upside/downside indicates that the fund's TR was in line with the reference index's during months with positive/negative returns. Data points for the initial 12 months have been omitted in the exhibit due to the limited number of observations used to calculate the cumulative upside/downside capture ratios.

## Dividends: Use of significant distributable reserves

**Exhibit 14: Dividend history since FY18**



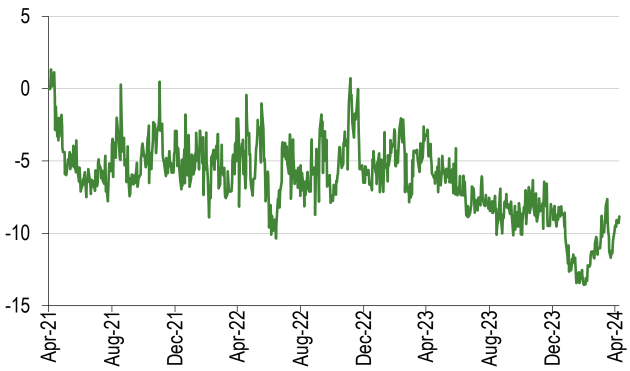

Source: BRSA, Edison Investment Research

In FY23, BRSA's earnings were 3.67p per share, which was 4.4% lower year-on-year. Four regular dividends of 2.00p per share were paid. The total annual payout of 8.00p per share has been held steady for the last seven financial years and is expected to continue in FY24 using revenues and distributable reserves. At the end of FY23, the trust had c £152.3m in distributable reserves, which is equivalent to c 24x the annual dividend payment.

## Valuation: Discount wider than historical averages

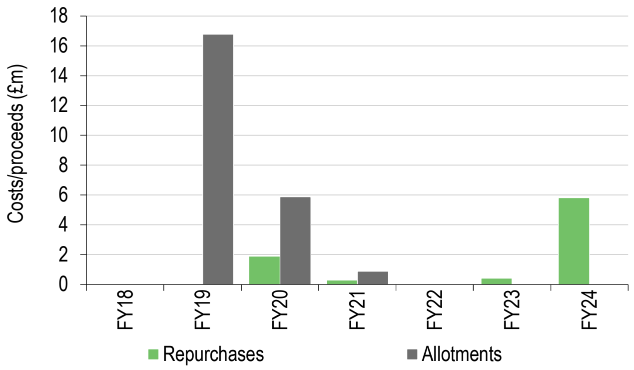
BRSA's 8.8% discount compares to a range of a 1.3% premium to a 13.6% discount over the last three years. It is wider than the 8.6%, 6.2%, 4.6% and 4.9% average discounts over the last one, three, five and 10 years respectively. Renewed annually, the trust's board has the authority to repurchase up to 14.99% and allot up to 10% of its share capital. Due to the prevailing discount to NAV in October 2023, when, in general, investment companies' discounts had widened to levels last seen during the global financial crisis, BRSA's board restarted share buybacks. Shares are currently being repurchased regularly and are held in treasury.

**Exhibit 15: Discount over three years (%)**




Source: LSEG, Edison Investment Research

**Exhibit 16: Buybacks and issuance**




Source: Morningstar, Edison Investment Research

## Fund profile: Focus on income and ESG

BRSA was launched on 24 October 2012 and is listed on the Premium Segment of the London Stock Exchange. It is managed by three of BlackRock's US income & value investment team: Tony DeSpirito (CIO, US fundamental equities), David Zhao (co-director of research) and Lisa Yang (consumer discretionary/staples specialist). There are around 25 investment professionals in the US income & value team, which has c $65bn of assets under management. BRSA's managers primarily invest in a diversified portfolio of North American equities, focusing on large- and mid-cap companies that pay and grow their dividends. To mitigate risk, at the time of investment, a maximum 10% of gross assets may be invested in a single investment, a maximum 25% in non-North American companies and a maximum 35% in any one sector. The managers also take firms' ESG characteristics into account, seeking to deliver a superior ESG outcome compared with the reference index in terms of a better ESG score and a lower carbon emissions intensity score. Foreign currency is not hedged as a matter of course, but the managers may employ specific currency hedging.

## Investment process: ESG is an integral input

There are three main elements to BRSA's investment process:

**Idea generation** – the managers aim to identify the best ESG and alpha opportunities from an investment universe primarily made up of North American large- and medium-cap equities, although up to 25% of the portfolio can be invested in liquid non-North American companies. ESG exclusion screens are used to narrow the investment universe. The managers are able to leverage the best fundamental and thematic ideas from BlackRock's US income & value platform to generate a pipeline and prioritise the research agenda.

**Fundamental research** – this involves assessing the materiality of a firm's ESG and sustainability factors and evaluating its important earnings drivers, along with engaging with company managements on business and ESG issues. A research document is prepared to illustrate the investment thesis and is discussed within the investment team. The managers evaluate how and over what time frame they expect their research insights to be reflected in a company's share price.

**Portfolio construction** – the fund typically has 30–60 high-conviction positions. Gearing of up to 20% of NAV is permitted but is likely to be in a 0–10% range, with 5% seen as a neutral level. There are clear buy and sell disciplines for both fundamental and ESG considerations. Portfolio risks and exposures are carefully monitored, with an emphasis on stock-specific risk. The fund is diversified by sector, industry and style factors.

## How ESG is integrated into the investment process

DeSpirito, Zhao and Yang seek to build a high-conviction portfolio of attractively priced, high-quality dividend-paying companies that are classified as either:

- ESG leaders – best-in-class businesses that effectively manage environmental, social and governance factors to benefit all stakeholders. For example, consumer staples company Mondelēz International has secured Global Food Safety Initiative-benchmarked certification for its manufacturing sites, which provide audits of suppliers and routine tests for final products thereby limiting the firm's product and reputational risks. ESG leaders make up the majority of BRSA's portfolio;
- ESG improvers – companies showing demonstratable progress on their ESG journey, where active engagement may lead to improving ESG practices and more sustainable outcomes. Auto manufacturer General Motors has a clear roadmap for better ESG adherence, including a commitment to end gasoline-powered passenger car production by 2035; or
- 'sustainability enablers' – firms advancing the transition to sustainable solutions, such as companies contributing to greater energy efficiency and a lower carbon footprint. Health insurance companies are also included in this category as they enable people to access healthcare products and services. Multinational telecom and media company Comcast is the leading broadband provider in the United States and is critical in enabling remote working and reducing commuter-related emissions.

Outright exclusions from the fund include businesses manufacturing controversial weapons or civilian firearms, fossil fuel miners (thermal coal and tar sands) and tobacco companies. BRSA's resulting portfolio has a premium ESG score and lower carbon emissions intensity than the reference index, as measured by MSCI, which is a leading external ratings agency.

As shown in Exhibit 17, at 31 October 2023, compared with the reference index, BRSA's portfolio had higher ESG scores in all three of the subsectors (environmental, social and governance), while its carbon emissions intensity was around half that of the reference index.

**Exhibit 17: Portfolio ESG characteristics at 31 October 2023**

| | Portfolio | Reference index | Difference (%) |
|---|---|---|---|
| MSCI ESG score (adjusted) | 7.3 | 6.4 | 14.1 |
| MSCI environmental score | 7.0 | 6.5 | 7.7 |
| MSCI social score | 5.2 | 4.9 | 6.1 |
| MSCI governance score | 6.3 | 5.7 | 10.5 |
| Carbon emissions intensity (total capital)* | 70.3 | 131.7 | (46.6) |

Source: BRSA, Edison Investment Research. Note: *Metric tons/$m total capital.

## Gearing

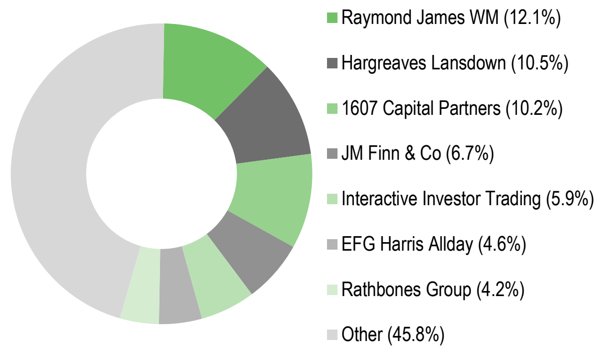
Gearing of up to 20% of NAV is permitted but is typically in a range of 0–10%, with 5% deemed a neutral level. At the end of March 2024, BRSA had a net gearing position of 1.3%.

## Fees and charges

BlackRock Investment Management (UK) is paid an annual management fee of 0.70% of BRSA's NAV, which is allocated 75% to the capital account and 25% to the revenue account. In FY23, the trust's ongoing charges were 1.03%, which was a 2bp increase versus 1.01% in FY22.

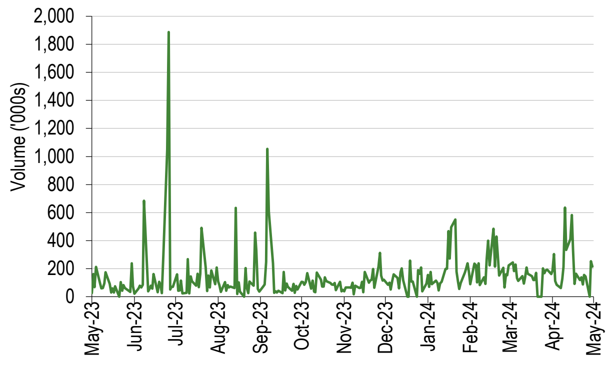
## Capital structure

**Exhibit 18: Major shareholders**




Source: Bloomberg. Note: At 31 March 2024.

**Exhibit 19: Average daily volume**




Source: LSEG. Note: 12 months to 8 May 2024.

BRSA is a conventional investment trust with one class of share. There are 77.0m ordinary shares in issue plus another 23.4m held in treasury. At the end of FY23, 78.7% (vs 96.7% at the end of FY22) of the trust's shares were held by banks or nominees, individuals 18.0% (vs 1.4%) and other 3.3% (vs 1.9%). BRSA's average daily trading volume over the last 12 months was c 156k shares.

## The board

**Exhibit 20: BRSA's board of directors**

| Board member | Date of appointment | Remuneration in FY23 | Shareholdings at end-FY23 |
|---|---|---|---|
| Alice Ryder (chair since 1 November 2022) | 12 June 2013 | £43,000 | 9,047 |
| Melanie Roberts | 1 October 2019 | £30,000 | 10,000 |
| David Barron | 22 March 2022 | £33,682 | 5,000 |
| Solomon Soquar | 21 March 2023 | £18,411 | Nil |

Source: BRSA

Alice Ryder has been a director for more than 10 years, partly to provide continuity, and has announced her intention to retire from BRSA's board at the March 2025 AGM. David Barron will become the chair. A search is underway for a new director and an announcement will be made in due course.

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