

JPMorgan European Discovery Trust

Initiation of coverage

A core option within a niche market

JPMorgan European Discovery Trust (JEDT) aims to generate long-term capital growth from a portfolio of high-quality, reasonably valued, smaller European equities. The scale of opportunities in a relatively inefficient market gives active managers an excellent opportunity set for outperforming and delivering good long-term investor returns, and JEDT has a strong long-term investment track record but has been a little more challenged of late. The trust currently offers a 1.7% dividend yield.

Why invest in European smaller companies now?

European smaller companies have proven themselves to be a fruitful market for investors over the past 20 years. As an asset class they have outperformed European large caps and most other major markets including global small caps. This has been due to the combination of high earnings growth driven by ongoing innovation and disruption in secular growth sectors. European smaller companies have historically performed well after economic disruption and so there is potential for the asset class to further outperform as the global economy recovers from the COVID-19 pandemic. With the recent correction seen in global markets year to date, European smaller companies are trading in line with long-term averages. However, investors will be hoping that secular growth tailwinds continue to drive returns.

The analyst's view

JEDT could appeal to those investors wishing to diversify their large-cap Europe ex-UK exposure or those wishing to access higher-growth markets and industries. JEDT provides investors with a large and liquid option within this dynamic market. The combination of an experienced and well-resourced management team and a proven and repeatable investment process gives this trust the potential to outperform through a variety of market conditions.

Valuation: Scope for the discount to narrow

Currently JEDT is trading on a discount to cum income fair net asset value (NAV) of 15.7%, which is outside the five-year average of 12.3%. These headline figures mask some quite extreme moves, with the shares trading at a discount to cum income fair NAV of 25.5% in March 2020 and 8.9% in November 2021. Arguably, as the largest, most high-profile option for investors in the sector, with an established manager and good long-term performance, the trust deserves to be trading closer to NAV.

Investment trusts
European small companies

14 March 2022

Price 397.5p
Market cap £631m
AUM £825m

NAV* 475.4p
Discount to NAV 15.7%

*Including income. As at 21 February 2022.

Yield 1.7%

Ordinary shares in issue 158.6m

Code/ISIN JEDT/GB00BMTS0Z37

Primary exchange LSE

AIC sector European Smaller Companies

52-week high/low 582.0p 374.5p

NAV* high/low 654.0p 451.6p

*Including income

Net gearing* 7%

*As at 10 March 2022.

Fund objective

JPMorgan European Discovery Trust (JEDT) aims to provide capital growth from a diversified portfolio of smaller European companies (ex-UK). With JEDT's focus on capital growth, shareholders should expect the dividend to vary from year to year. The company can borrow to gear the portfolio within a range of 20% net cash to 20% geared in normal market conditions.

Bull points

- A well-resourced and experienced team with access to the vast resources at JPMorgan.
- The largest vehicle in the sector.
- Focused on stock specifics with a balanced stylistic approach.

Bear points

- This is a volatile market requiring a suitable attitude to risk.
- Current valuations are only in line with long-term averages.
- Could be an element of key person risk.

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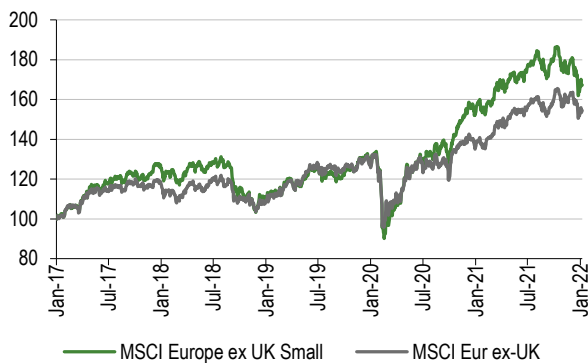
**JPMorgan European Discovery Trust
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Market outlook: Scope for small-cap outperformance

Historically, European smaller companies have outperformed their large-cap brethren six to 12 months after a financial shock as central banks seek to support and stimulate economic activity through accommodative monetary policy. In the mid to late 1990s there were a number of emerging market crises (Mexican, Asian and Russian), and then the dot-com bubble burst in 2000–01 during which European smaller companies underperformed. Post the dot-com crash, European smaller companies posted six years of outperformance. They again underperformed during the global financial crisis of 2007–08 before recovering very strongly in the next two years. The period during the European sovereign debt crisis saw underperformance in 2011, however since then and throughout the COVID-19 pandemic, smaller companies have continued to outperform larger European companies. As a segment of the market sensitive to economic growth, the recent expansion in leading purchasing managers' index (PMI) indicators seen across Europe could provide further support to European smaller companies.

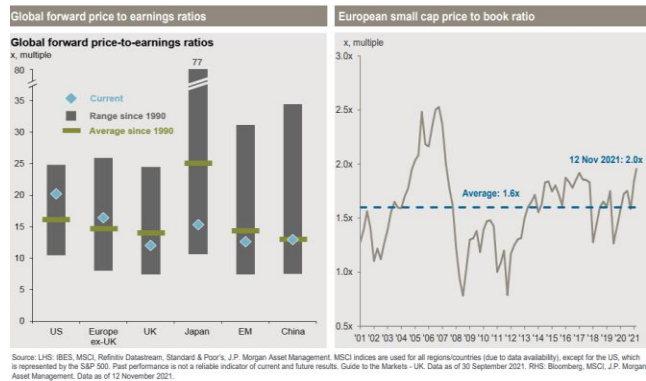
The broader European market is currently trading slightly above its long-term average on P/E measures (Exhibit 2), but given many economies are not yet fully open, corporate earnings are likely to be somewhat depressed. As COVID-19 restrictions ease and the reopening of economies gathers pace, earnings could grow quickly, supporting and justifying the current P/E ratio. Likewise on a price/book (P/B) measure, European smaller companies are looking slightly expensive relative to their own history (but arguably better value than global small caps) on 2x book value versus the 20-year average of c 1.5x. However, JEDT's managers believe that this is justified given higher expected earnings growth.

Exhibit 1: Relative performance of European large and small caps over five years



Source: Refinitiv, Edison Investment Research. Note: Total return performance in pounds sterling.

Exhibit 2: Regional valuation metrics



Source: JEDT

Asset allocation

Current portfolio positioning: Opportunities in sustainability, healthcare and technology

JEDT's portfolio is built from the bottom up on the basis of the attractiveness of individual stocks. There are, however, areas where the team is finding supportive secular growth opportunities. One such area is sustainability, via companies such as Nexans (a French high voltage cable company) and the Swiss domiciled SIG Combibloc with its focus on sustainable packaging. The trust has benefited from its renewable energy names, but reduced them as their valuations became less compelling; after a recent pullback, these are once again looking more attractive for potential reinvestment.

Lockdown has reinforced the importance of physical wellness and the trust has positions in names such as German cancer treatment healthcare stock Eckert & Ziegler and Swedish IVF specialist Vitrolife. Trigano, a French recreational vehicle (RV) manufacturer, is benefiting from a surge in younger generational appreciation of nature and staycations. Sanlorenzo, a luxury yacht manufacturer, is likewise supported by this evolving trend.

Exhibit 3: Top 10 holdings (as at 31 December 2021)

Company	Country	Sector	Portfolio weight %		Benchmark weight	Active weight vs benchmark
			31 Dec 2021	31 Dec 2020*		
Alten	France	Technology	3.6	2.5	0.4	3.2
Dieteren	Belgium	Consumer discretionary	3.0	N/A	0.4	2.6
Reply	Italy	Technology	2.8	N/A	0.3	2.5
Nexans	France	Industrials	2.5	3.0	0.2	2.3
Sanlorenzo	Italy	Consumer discretionary	2.5	N/A	0.0	2.5
Bravida	Sweden	Industrials	2.4	2.9	0.2	2.2
Vitrolife	Sweden	Healthcare	2.4	N/A	0.3	2.1
Helvetia	Switzerland	Financials	2.4	N/A	0.4	2.0
Bechtle	Germany	Technology	2.3	N/A	0.0	2.3
ASR Nederland	Netherlands	Financials	2.3	N/A	0.6	1.7
Top 10 (% of holdings)			26.2	28.3		

Source: JPMorgan, Edison Investment Research. Note: *N/A where not in December 2020 top 10.

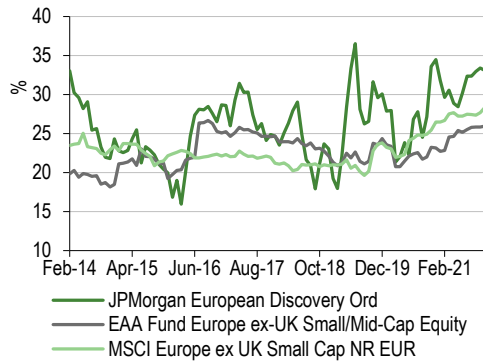
Exhibit 4: Sector weightings (% unless stated)

	Portfolio end-December 2021	Portfolio end-December 2020	Change (pp)	Index weight	Active weight vs index (pp)
Industrials	35.8	33.8	2.0	28.3	7.5
Consumer discretionary	18.6	9.3	9.3	12.4	6.2
Technology	17.7	17.5	0.2	10.1	7.6
Healthcare	7.5	8.1	-0.6	8.1	-0.6
Financials	7.0	4.6	2.4	13.3	-6.3
Basic materials	3.8	2.6	1.2	5.2	-1.4
Consumer staples	2.6	3.9	-1.3	5.3	-2.7
Real estate	2.0	3.0	-1.0	10.3	-8.3
Utilities	0.6	9.0	-8.4	2.9	-2.3
Energy	0.0	0.0	0.0	2.1	-2.1
Telecommunications	0.0	6.0	-6.0	2.0	-2.0
Cash	4.4	2.2	2.2	0.0	4.4

Source: JPMorgan

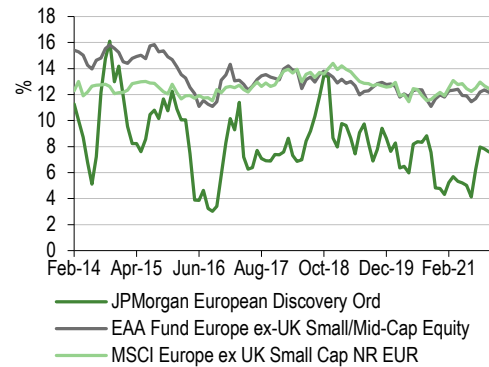
European smaller companies are rich in technology (services, software and hardware) disruptors, and the portfolio is 17.7% weighted (+7.6pp relative to the index) in such names as Alten and Reply, both top 10 positions. Alten, a French industrials company, is well placed across a range of end-markets such as aerospace and autos, while Reply is well established in IT solutions such as cloud computing across a range of industries. Valuations in this area are quite demanding, so the managers need to keep a close eye on the earnings trajectory. Europe is well known as an industrial base and the portfolio is 35.8% invested (+7.5pp relative) in this sector. The fund's allocation to the broad industrials sector (Exhibit 5) includes six top 20 positions via names such as Nexans, Bravida (building energy efficiency solutions), Interpump (hydraulic water pumps), Valmet (energy efficient paper and pulping), SPIE (energy efficiency and smart cities) and market researcher Ipsos.

Exhibit 5: Overweight industrials



Source: Morningstar. Data at November 2021.

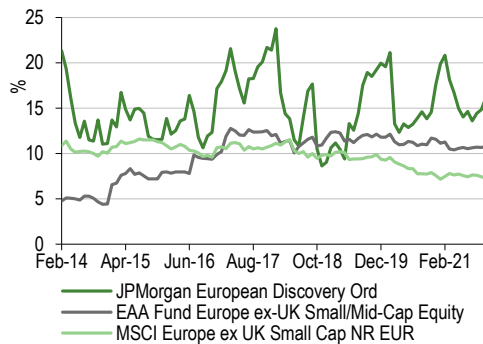
Exhibit 6: Underweight financials



Source: Morningstar. Data at November 2021.

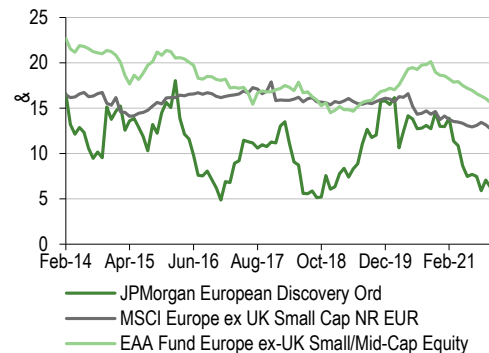
Offsetting these overweight areas are underweight sectors such as financials (Exhibit 6) and real estate. They are likely to be structurally less appealing to the managers as their earnings are often driven more by top-down macro factors such as interest rates and GDP growth. In financials, the primary exposure is in insurance rather than banks via holdings such as Helvetia, ASR Nederland and Unipol Gruppo, as this is where they find companies with attractive long-term track records of generating positive shareholder returns.

Exhibit 7: Overweight Italy



Source: Morningstar. Data at November 2021.

Exhibit 8: Underweight Germany



Source: Morningstar. Data at November 2021.

The managers often find good opportunities in some of the more unloved and cheaper markets such as Italy (Exhibit 7) and France, and are in aggregate some 32.6% invested in stocks listed in these countries versus 16.9% for the benchmark (Exhibit 9) as at the end of December 2021. Italy is home to two top 10 positions in Reply and Sanlorenzo, while French companies Alten and Nexans are also among the top 10 holdings. In contrast, Germany is a noticeable underweight, with only 5.9% of the fund invested there versus 14% within the benchmark (Exhibits 8 and 9).

Exhibit 9: Regional weightings (% unless stated)

	Portfolio end-December 2021	Portfolio end-December 2020	Change (pp)	Index weight	Active weight vs index (pp)
Sweden	18.4	15.2	3.2	19.5	-1.1
France	16.7	14.5	2.2	9.2	7.5
Italy	15.9	17.2	-1.3	7.7	8.2
Switzerland	14.1	12.2	1.9	13.5	0.6
Belgium	9.8	1.8	8.0	4.3	5.5
Netherlands	9.5	13.9	-4.4	5.7	3.8
Germany	5.9	12.7	-6.8	14.0	-8.1
Denmark	2.7	3.3	-0.6	4.7	-2.0
Finland	2.0	0.0	2.0	4.7	-2.7
Norway	0.6	5.9	-5.3	6.5	-5.9
Others	0.0	0.0	0.0	10.2	-10.2
Cash	4.4	2.2	2.2	0.0	4.4

Source: JPMorgan

Performance: Long-term outperformance

JEDT has rewarded investors with good performance in both NAV and share price terms over the long term, with 1.2% and 8.4% outperformance respectively over the past 10 years (Exhibits 10–12). Reviewing JEDT's performance over the 12 months to end January 2022, the share price and NAV increased by 8% but both underperformed the benchmark by 1.7%. Stock selection was a positive contributor to returns; however, sector positioning detracted by more than the good stock selection. The overweight positioning to industrials and good stock selection in technology were positive drivers, while the substantial underweight to financials and stock selection within utilities were the largest negative contributors to relative returns. The top three stocks accretive to performance were the large active positions in Sanlorenzo, Dieteren and Alten, while Scatec, Valeo and Stillfront detracted.

Taking a three-year perspective, the share price underperformance was a modest 0.5% while the NAV underperformed by 2%. Again, stock selection was good over this period. Not surprisingly, the overweight technology position proved to be a significant driver of returns, while being overweight a slightly lagging consumer discretionary sector detracted on a relative basis. Good stock selections in alternative energy and consumer staples were the major contributors at the stock level. Overweight positions in Solaria Energia, ASM and Encavis (which all posted exceptional returns) contributed the most, while Technogym, Valeo and Stillfront detracted the most. In a generally buoyant equity market, the use of gearing was also supportive of returns.

We would expect in the long term that stock selection would be the biggest driver of returns and that has historically been the case. However, there are other factors such as sector, country, currency and stylistic inputs that will also determine investor returns at varying points of the economic cycle. This strategy seeks to strike a balance between value, quality and momentum, on which we elaborate on page 10 in the Investment process section. While long-term performance remains robust, shorter-term performance has been more challenged with the managers highlighting 2022 ytd as particularly significant. The fund has a number of stocks that had been performing well and have strong growth stories behind them, however January was the single worst month for growth versus value, in Europe, since records began almost 50 years ago. While JEDT does have exposure to value, it was not sufficient to offset the underperformance in the growth (quality) holdings. The growth versus value debate and respective performance has become particularly polarised at this time. However, according to work done by JPMorgan, looking back to 1994, growth and value have cumulatively performed very similarly, and have both been overshadowed by the returns from momentum, putting this short-term, albeit violent, stylistic reversal into perspective.

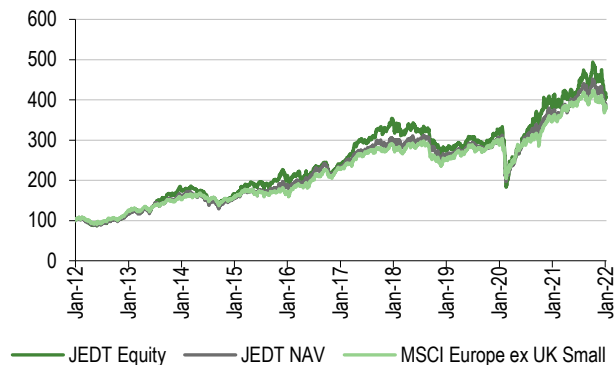
Exhibit 10: Five-year discrete performance data

12 months ending	Total share price return (%)	Total NAV return (%)	MSCI Europe ex UK Small (%)	MSCI Eur ex-UK (%)	CBOE UK All Companies (%)
31/01/18	44.8	29.8	25.3	17.4	11.3
31/01/19	(20.4)	(12.8)	(11.4)	(7.4)	(3.9)
31/01/20	14.1	11.9	13.8	15.6	10.5
31/01/21	21.4	22.0	20.4	7.5	(8.6)
31/01/22	8.0	8.0	9.7	14.0	19.3

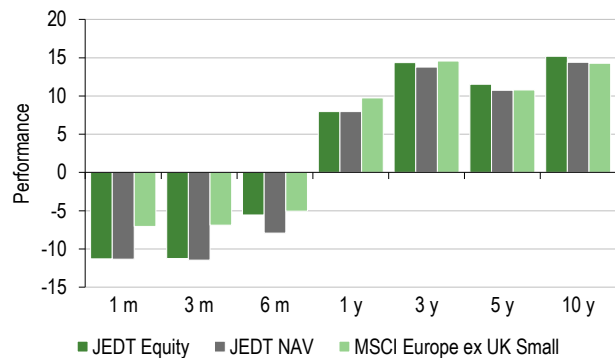
Source: Refinitiv. Note: All % on a total return basis in pounds sterling.

Exhibit 11: Investment trust performance to 31 January 2022

Price, NAV and benchmark total return performance, 10-year rebased



Price, NAV and benchmark total return performance (%)



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

Exhibit 12: Long-term % outperformance, but more challenged of late

	One month	Three months	Six months	One year	Three years	Five years	10 years
Price relative to MSCI Europe ex UK Sml	(4.6)	(4.7)	(0.5)	(1.6)	(0.5)	3.3	8.4
NAV relative to MSCI Europe ex UK Sml	(4.6)	(4.9)	(3.0)	(1.6)	(2.0)	(0.2)	1.2
Price relative to MSCI Eur ex-UK	(6.4)	(8.4)	(4.5)	(5.3)	5.7	12.1	47.0
NAV relative to MSCI Eur ex-UK	(6.4)	(8.6)	(6.9)	(5.3)	4.1	8.3	37.1
Price relative to CBOE UK All Companies	(11.1)	(13.2)	(10.4)	(9.5)	24.2	34.0	102.5
NAV relative to CBOE UK All Companies	(11.1)	(13.4)	(12.7)	(9.5)	22.4	29.4	89.0

Source: Refinitiv, Edison Investment Research. Note: Data to end-January 2022. Geometric calculation. %.

Exhibit 13: NAV performance versus benchmark over 10 years


Source: Refinitiv, Edison Investment Research

Peer group comparison

The Association of Investment Companies' (AIC's) European Smaller Companies peer group is small, consisting of four funds:

Exhibit 14: Peer group performance

Group/investment	Market capitalisation (£m)	1-year NAV TR (cumulative)	3-year NAV TR (cumulative)	5-year NAV TR (cumulative)	10-year NAV TR (cumulative)
JPMorgan European Discovery Ord	756.8	4.0	48.1	63.6	271.3
European Assets Ord	439.3	4.9	48.9	54.2	256.1
The European Smaller Companies Trust PLC	685.5	5.3	70.5	74.2	343.1
Montanaro European Smaller Ord	340.2	8.7	92.7	139.0	338.9
Simple average	555.5	5.7	65.1	82.7	302.4
Weighted average		5.3	62.0	76.5	300.8
Rank	1	4	4	3	3

Source: Morningstar. Note: Market capitalisation as at 4 February and NAV as at 3 February 2022.

It is worth highlighting in Exhibit 15 that co-manager Francesco Conte has by far the longest tenure in the sector, dating back to November 1998. JEDT is the largest fund within the group with total assets of £903m. This may contribute to the trust being slightly more exposed to larger companies within the opportunity set, with an average market cap of £3.4bn versus an average of £2.4bn.

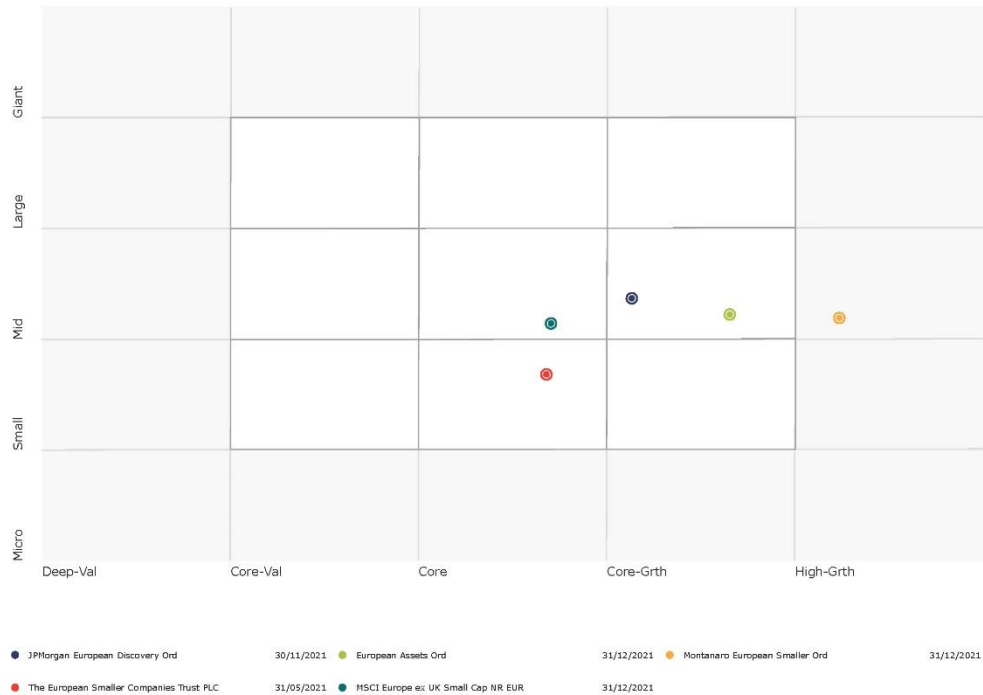
Exhibit 15: Portfolio metrics

Name	Manager tenure (average, years)	Manager tenure (longest, years)	P/E ratio (x)	ROE (%)	% of assets in top 10 holdings	Average market cap (£m)	Tracking error five years (%)	Total fund value (£m)
JPMorgan European Discovery	14.0	23.2	22.2	16.6	26.2	3,439	5.7	1,044.3
European Assets Trust	7.2	10.3	28.1	17.6	28.8	2,810	7.1	653.5
Montanaro European Smaller Cos	5.4	10.0	41.8	26.1	36.0	2,664	7.8	406.2
European Smaller Companies Trust	6.6	10.5	20.7	9.0	19.3	1,071	7.4	929.4

Source: Morningstar. Note: Data as 31 December 2021.

Three of the cohort are stylistically 'growth' in terms of their investment approach according to work done by Morningstar (Exhibit 16) with The European Smaller Companies trust exhibiting more core stylistic characteristics; although JEDT is at the more core end of the spectrum compared to MTE and EAT. however, JEDT's portfolio is one of the cheapest of the four looking at the P/E and P/B multiples of the holdings, which reinforces the valuation-conscious investment approach and balance of stylistic factors within the portfolio when compared with some peers that are notably exposed to more expensive growth stocks.

Exhibit 16: Stylistic characteristics



Source: Morningstar

While JEDT is actively managed, with an active share of 89%, it also has one of the lower tracking errors over five years, making it a good option for a core buy and hold strategy.

Exhibit 17: Divergent country and sector positioning

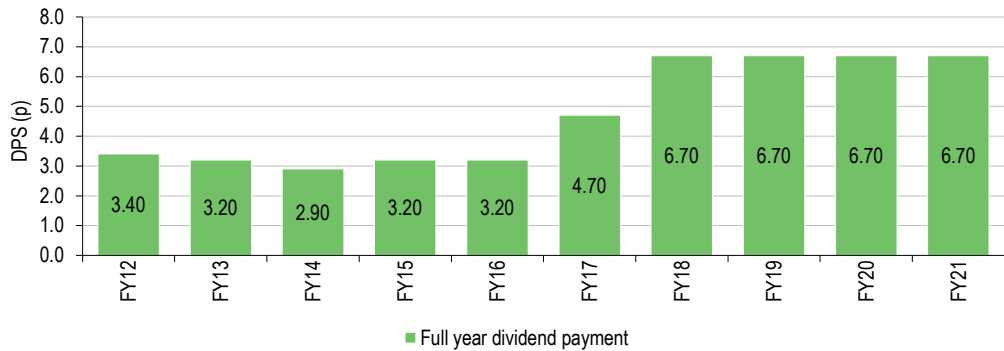
Name	Industrials %	Technology %	Financial services %	France %	Germany %	Italy %
JPMorgan European Discovery	33.1	18.9	7.6	17.8	6.3	16.2
European Assets Trust	19.0	18.3	15.4	6.9	23.8	7.3
Montanaro European Smaller Cos	16.2	32.7	7.2	10.2	15.2	10.0
European Smaller Companies Trust*	27.5	12.5	12.5	11.7	22.2	8.3
MSCI Europe ex UK Small Cap	28.2	11.4	12.7	9.1	13.7	7.7
IA European Smaller Companies	25.2	13.8	10.9	11.2	12.5	7.9

Source: Morningstar. Note: As at end of December 2021.

Dividends

The portfolio is managed for capital growth rather than dividends, which can be expected to vary from year to year. That said, they have historically been a feature here (Exhibit 18) and are paid in January and July. The focus on quality, cash-generative companies naturally provides some income. For FY21 dividends of 6.7p per share (FY20: 6.7p) were paid on revenues of 4.42p (FY20: 6.83p). Dividend income fell sharply to £7.1m in FY21 from £10.9m previously as COVID-19 affected many companies' willingness or ability to pay dividends. This has rebounded quite strongly subsequently and so it is likely that the dividend will be closer to being fully funded for FY22. JEDT currently yields 1.7%, which compares to the index yield as at the end of December 2021 of 1.88%.

Exhibit 18: Dividend history since FY12



Source: JPMorgan, Edison Investment Research

Discount: Unjustifiably wide

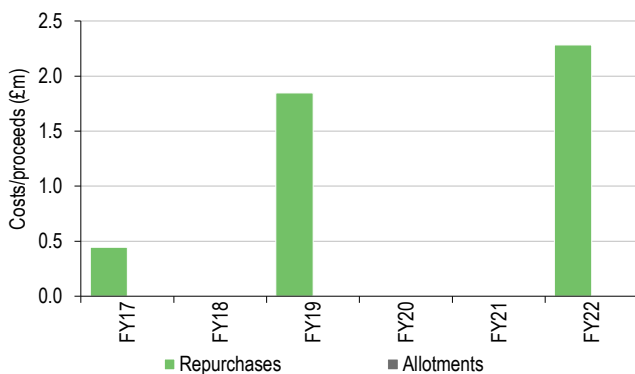
JEDT's board monitors the discount closely and has authorisation to buy back up to 14.99% of the issued share capital to minimise short-term volatility. It is a strategy that the board has tended to use sparingly over the past five years; however, FY22 has seen a significant number of shares repurchased for cancellation (Exhibit 20). The current discount is 15.7%, which is wider than the longer-term average (12.3% over five years) and is arguably excessively wide given the quality of the proposition here. As JEDT is one of the largest of the cohort it is pleasing to see that the liquidity in terms of value and number (five-year average 175,900) of shares traded is consistently high (Exhibit 19).

Exhibit 19: Average monthly value of shares traded

Name	Total fund value	1 month	1 year	5 years
JPMorgan European Discovery	£1,044,257,460	£660,000	£770,000	£700,000
European Assets Trust	£653,482,351	£910,000	£710,000	£580,000
Montanaro European Smaller Cos	£406,226,201	£1,650,000	£990,000	£430,000
European Smaller Companies Trust	£929,449,575	£450,000	£750,000	£730,000

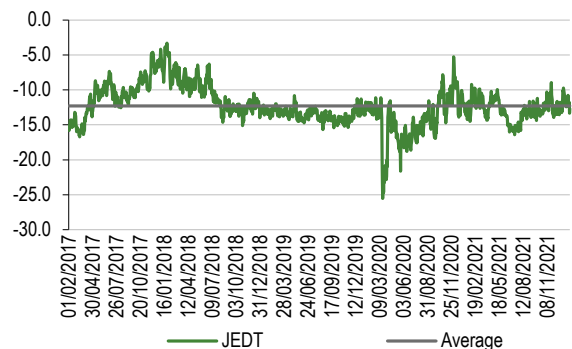
Source: AIC. Note: Data as at January 2022.

Exhibit 20: Buybacks and issuance



Source: Morningstar

Exhibit 21: Discount over five years



Source: Refinitiv

Fund profile: Diversified European small/mid-cap exposure

In June 2021 the fund changed its name from JPMorgan European Smaller Companies Trust to JPMorgan European Discovery Trust. This was to reflect that it invests across the gamut of opportunities in European smaller companies of up to an €6–7bn (£4–6bn) market cap at the time of investment. It was also to convey to UK investors that many European smaller companies are actually far larger in size vs their UK smaller company brethren. With an average market cap of some €4bn (£3.4bn), there is a range of company sizes within the portfolio. Thus, the investable opportunity set is potentially broader than purely smaller companies and the change of name reflects this. There has been no change in the investment process, which has been in place over many years.

The trust was launched in April 1990. It aims to generate long-term capital growth from a diversified portfolio of European ex-UK small-cap equities. The trust is managed by Francesco Conte (since 1998) and Edward Greaves (since 2016), who are able to draw on the broad resources of J.P. Morgan Asset Management's European equity team. The trust is benchmarked against the MSCI Europe (ex UK) small cap net total return index (until 31 March 2020 EMIX Smaller European Companies (ex UK) net total return index (in sterling terms)). The MSCI Europe (ex UK) Small Cap Index contains c 780 companies with market caps from £100m up to £6.63bn (average £1.13bn), spread across 14 developed markets. At the time of investment, a maximum 5% of the portfolio is permitted in a single stock and no more than 15% may be invested outside of the benchmark. Currency exposure is not hedged. JEDT may gear up to 20% or run up to a 20% net cash position.

One area of interest is comparing the open and closed ended versions of this strategy. The closed ended iteration has outperformed but there is relatively little difference between the two portfolios currently. In fact, as at the end of November 2021, only four stocks are held in JEDT and not the open-ended version of the strategy (Lotus Bakeries, Kinopolis, Volue and Lime Technologies) with common holdings equating to a virtually identical 99.07% and similar average market caps of c £3.5bn. Aside from the use of gearing, one might argue that there are potentially more levers that the trust could be pulling for long-term shareholder returns.

Investment process: Focus on quality

The managers aim to generate long-term capital growth from a diversified portfolio (50–75 holdings) of small-cap European ex-UK equities. Initially they use a proprietary multi-factor model to screen the universe, which is made up of c 780 small-cap European stocks. Companies passing the screen undergo thorough fundamental analysis.

There are three characteristics that the team is looking for and the portfolio will have a positive bias to these factors through time, which should help the trust to have an all-weather ability to perform consistently in varying market environments.

The team looks for attractively **valued** opportunities and put a lot of emphasis on FCF yield as it sees it as the highest-quality valuation metric. These are generally robust, cash generative companies that may be out of favour with investors, but importantly where the team can identify a catalyst for a re-rating. These companies may operate in cyclical end-markets or where investor sentiment is weak. Current positions in this category include Swedish energy efficiency specialist Bravida, French market research company Ipsos and French recreational vehicle manufacturer Trigano.

Another characteristic that they look for is **'quality'**. These companies are likely to be market leaders in niches, with robust balance sheets, high and sustainable return on equity, disciplined and proven management ability to allocate capital effectively, and high barriers to entry. Examples here include Italian digital services operator Reply, Swiss life science company Tecan and Swedish IVF company Vitrolife.

Lastly there is allocation to **momentum** as a factor. These companies are typically in structurally growing markets, and often have disruptive technology allowing market share gains and continued beating of market expectations. Current examples in the portfolio here are Dutch sustainable construction firm Arcadis, German nuclear medical imaging company Eckert & Ziegler and French high-voltage cable operator Nexans.

Each prospective company is also assessed against three additional criteria:

1. economics: does the company generate value, ie is the return on capital above the cost of capital?
2. duration: will the company continue to generate added value in the future, ie does the company have a strong economic moat?
3. governance: will minority shareholders be able to benefit from this added value or might it be wasted by management, for instance through poorly conceived acquisitions?

Position size is determined by the managers' level of conviction and a company's share liquidity. New positions are typically c 1% of the portfolio and are generally trimmed when they reach above c 3%. Reasons for selling a holding will be due to a fundamental deterioration in business conditions; if the company has grown too large; on valuation grounds; or if there is a better investment opportunity available. Portfolio turnover is currently running at c 70% a year, which is broadly in line with historical averages.

Environmental, social and governance (ESG) considerations are factored into the process, as companies that put their clients, the environment and their employees at the front and centre are likely to have long-term sustainable earnings. The team uses a range of proprietary tools such as the AI unstructured data model, which is able to sift through vast amounts of published information to unearth potential nuanced messaging from company management and wider market sentiment. There is also an Equity Failure Model that optimises 170 different inputs (such as short interest and balance sheet anomalies) that can highlight potential issues in a stock and is run on over 10,000 stocks globally.

The team: Well-resourced but some potential key person risk

The team of five is led by the experienced Francesco Conte, who has been with J.P. Morgan since 1998 and was previously a lead analyst within Italian equities at Schroders. Co-manager Edward Greaves has worked alongside Conte since 2011, having previously been at Rothschild. Jack Featherby has been in the team since January 2018, with previous experience at Rothschild and Wells Fargo. Jules Bloch has been within the team since 2017 having previously worked within J.P. Morgan's private bank. Wioletta Krejner is the most recent addition, having joined J.P. Morgan in 2017 as a graduate trainee.

The team are all generalists and have a certain latitude to follow opportunities where they present themselves, regardless of sector or country. The portfolio is built from the bottom up, but at times Conte and Greaves may direct the resource within the team towards areas with potential rich veins of opportunities. This team does not operate within a vacuum and there is regular discussion with other teams, most notably the six-strong UK small- and mid-cap team headed by Guy Anderson, lead portfolio manager of The Mercantile Investment Trust. As one would expect with the extensive resources of J.P. Morgan, the team is also free to utilise external research where appropriate, but this tends to be limited to sector or thematic research. The board has a clause that it can terminate its contract with J.P. Morgan on three months' notice (ordinarily six months' notice) should Conte

not be a named manager on the trust. This highlights the element of key person risk that exists currently with the management arrangement, although with Greeves’s long association with JEDT this risk is mitigated to an extent.

An integrated approach to ESG within the investment process

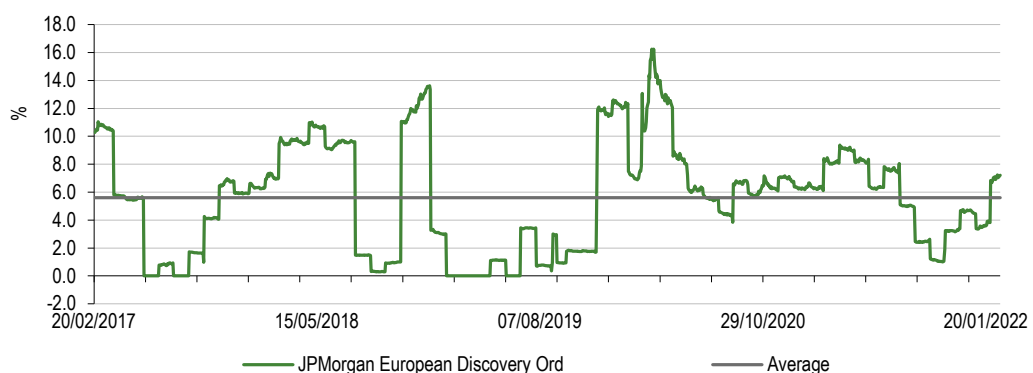
J.P. Morgan fully integrates ESG considerations into its investment process, which is executed by 500 portfolio managers and 300 research analysts, and it is an important element in their stock analysis. The firm’s heritage in this space is well established, from the 1970s and values-based investment mandates to the launch of the global socially responsible strategy in 2000 and becoming a signatory of the Principles for Responsible Investment (PRI) in 2007. In 2019 ESG was formally embedded in the investment process across the board. The company uses third-party data providers, albeit on a diminishing basis as it fully builds out its own internal proprietary scoring system (SPECTRUM). ESG is integrated across 450 strategies and around \$2.3tn of assets and the firm manages around \$7bn in dedicated sustainable mandates. The global sustainable investing team at J.P. Morgan numbers 24 and is organised by region, addressing client solutions, data and research and investment stewardship. Jennifer Wu leads this team and reports directly into the J.P. Morgan investment committee.

It is good to see that Sustainalytics scores the portfolio four out of five globes on ESG considerations. The trust also scores particularly well on emitting less carbon than the market average.

Gearing: Modest levels of gearing

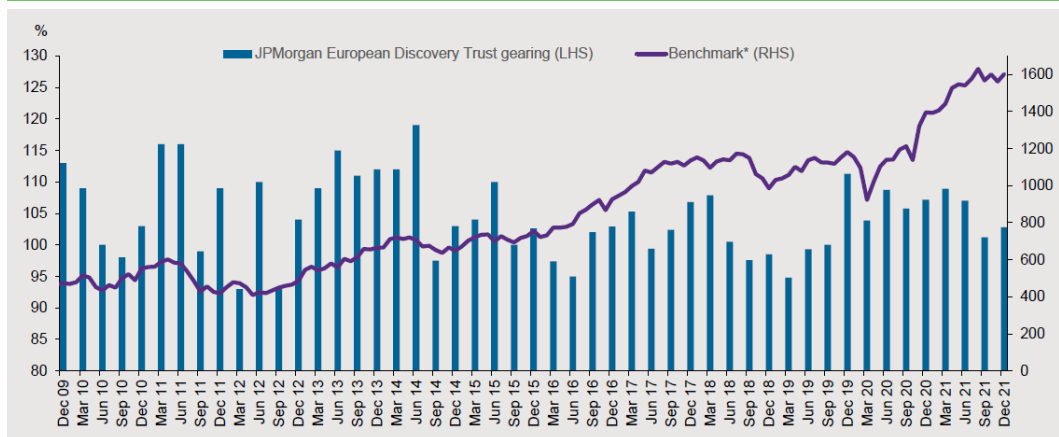
The company can be geared up to 20% or hold 20% in cash. Gearing is an investment decision made at the direction of the portfolio managers rather than in concert with or directed by the board. Gearing is arranged via a revolving credit facility of €125m with Scotiabank, which expires on 17 January 2023. The current level of gearing is 3.7%, which is a little below the medium-term average (Exhibit 22). The judicious use of gearing has been a long-term driver of returns and as markets have appreciated over time the managers have pared back its use (Exhibit 22).

Exhibit 22: Five years’ gearing



Source: Morningstar. Note: Gearing as at 18 February 2022.

Exhibit 23: Efficacy of gearing decisions



Source: JPM AM

Fees and charges: JEDT has a competitive advantage

From 1 April 2020, the annual management fee has been a flat fee of 0.85% applied to net assets, with no performance fee. The ongoing charge (which includes management and other expenses but excludes finance costs) is 0.91% and has been steadily falling over the past 10 years (2011: 1.21%). The management fee and finance costs are levied 30% against income with 70% apportioned to capital. Other more modest administrative costs are charged to income. Given the scale of the assets it is pleasing to see the fees charged here to be the lowest among the cohort, solidifying JEDT's status as a core holding in the asset class.

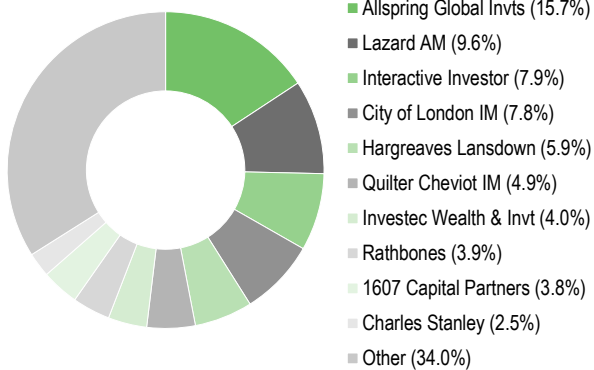
Exhibit 24: Competitive fees within the sector

Company	Latest market capitalisation (£m)	Latest ongoing charge ex perf fee (pp)	Performance fee	Latest ongoing charge inc perf fee (pp)
JPMorgan European Discovery	813	0.91	No	0.91
European Assets Trust	465	0.95	No	0.95
Montanaro European Smaller Cos	702	0.71	Yes	1.37
European Smaller Companies Trust	352	1.19	No	1.19
Simple average	583	0.94		1.10
Weighted average		0.90		1.10
JEDT rank	1	2		1

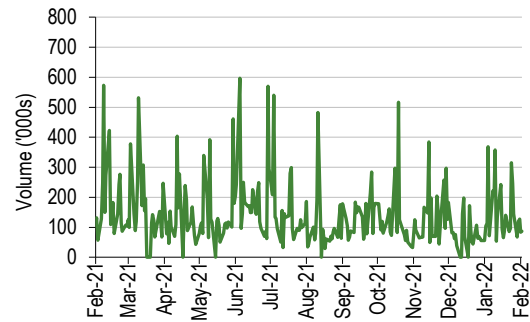
Source: Morningstar. Note: Data at 31 January 2022.

Capital structure

JEDT consists of a single class of ordinary shares (158.6m shares in issue) with no fixed life. As the largest and one of the most established European smaller companies investment trusts, it is not surprising to see a range of specialist institutional investors such as City of London Investment Management, private client fund managers such as Quilter Cheviot and retail investor platforms such as Hargreaves Lansdown. J.P. Morgan itself is a top 15 shareholder via a holding in the JPMorgan European Growth & Income Trust. This blend of shareholders provides for diversification, which should be supportive of the rating over the longer term.

Exhibit 25: Major shareholders


Source: JPMorgan, as at 31 December 2021

Exhibit 26: Average daily volume


Source: Refinitiv. Note: 12 months to 18 February 2022.

The board: Relevant and complementary skill set

Exhibit 27: JEDT's board of directors

Board member	Date of appointment	Remuneration (FY)	Shareholdings
Marc van Gelder (chair)	2016 (chair 2019)	42,000	80,000
Ashok Gupta	2013	27,500	7,500
Nicholas Smith (SID)	2015	33,950	11,600
Sarah Watters*	2021	18,300	0
Suzy Ross**	2022	0	0

Source: JEDT. Note: *Appointed July 2021. **Appointed March 2022.

The board of four has relevant and complementary skills bringing investment and corporate operational experience. Marc van Gelder is the chairman and has been a non-executive director (NED) since 1 August 2016. He has worked over several decades to CEO level in a number of European businesses. Ashok Gupta has been an NED since 1 January 2013 and has held NED positions in a variety of financial institutions including Mercer, Skandia UK and St James's Place. Nicholas Smith (chair of the Audit committee) has been an NED since May 2015 and brings extensive investment banking experience as a former CFO of Jardine Fleming. Sarah Watters was appointed in July 2021, and brings extensive investment and ESG experience as a former head of equities at BP Investment Management. Suzy Ross is the newest appointment having joined the board at the beginning of March, bringing marketing and client relationship expertise via senior positions at Google, Accenture and Jaeger.

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