Jargon buster: how to buy investment trusts

We explain how to buy investment trusts and what pitfalls to avoid...

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In our new jargon-busting series, we've already covered the fundamentals of investment trusts, including gearing, dividends and why trusts trade at a discount or premium. Next on the list is a delve into how to buy investment trusts and, more importantly, how to avoid the potential banana skins along the way...

Buying an investment trust is identical to buying shares in individual companies such as Barclays or AstraZeneca. Investment trusts are structured as public limited companies (plcs) with live share prices, allowing you to see exactly what price you'll pay or receive when buying or selling shares.

As a result, shares in investment trusts have a 'buy-sell' (or bid-offer) spread. For instance, if the buy-sell spread is 100-105 pence, you'll pay 105 pence per share if you want to buy shares and receive 100 pence per share if you're selling shares (the difference being the profit made by the broker).

And here's where the potential banana skin can come into play as a high buy-sell spread can significantly eat into profits. In the example above, if I buy shares for 105 pence, they'll have to rise by 5% (or 5 pence) to break even.

Typically, larger investment trusts have narrower spreads due to higher trading volumes: by way of example, I'd currently pay a minimal 0.3% spread on my trading platform if I bought shares in **Alliance Witan (ALW)** but, at the other end of the spectrum, a rather larger 9% spread if I bought shares in US Solar Fund (USF), meaning I'd need a near 10% rise in share price just to return to break-even.

This contrasts with open-ended funds (OEICs) which typically have a single unit price instead of a buy-sell spread. OEICs are also forward-priced, meaning you won't know the exact price at the time of placing the trade, with trades executing at the next valuation point (often midday if you place your trade first thing). This means you're better able to determine the dealing price when you're buying and selling investment trusts rather than OEICs.

Unlike with OEICs, you also can set automated investment instructions such as stop losses to sell shares in your trust automatically if the price falls below a set level which can limit your downside risk. Another option is a buy limit, whereby you set an instruction to buy shares in the trust if the price drops to or below a certain level, avoiding having to monitor share prices in real time.

In terms of placing the trade, you can do this via most DIY investing platforms, many of which offer app-based trading. It's also worth considering holding your trusts in a tax-efficient wrapper such as an Individual Savings Account (ISA) or Self Invested Personal Pension (SIPP) to maximise returns.

To help investors navigate through the multitude of options on offer, we've produced guides to the **best ISA providers** and **best SIPP providers**. And if there's anything you'd like us to cover in future jargon busters, drop us an email at **jo@keplerpartners.com** or **david.b@keplerpartners.com**.

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