



BST: High Yield And Strong Outperformance

Oct. 28, 2021 8:15 AM ET | **BlackRock Science and Technology Trust (BST)** | BSTZ | 3 Comments | 3 Likes



Obsidian Limited

346 Followers | [Bio](#)

Summary

- BST is a closed end fund that utilizes an equity focused portfolio, supplemented with derivatives, to drive current income and total return.
- The fund has a current yield of 5.58% and has outperformed the S&P 500 since inception.
- BST currently trades at an attractive valuation opening an opportunity for long term investors.



Hiroshi Watanabe/DigitalVision via Getty Images

The BlackRock Science and Technology Trust ([BST](#)) is an equity closed end fund which generates total return through current income and capital appreciation. The fund has outperformed several benchmarks including the S&P 500 and Nasdaq 100 since inception.

What is the BlackRock Science and Technology Trust?

The BlackRock Science and Technology Trust is a closed end fund which utilizes a portfolio comprised of common stock and derivatives to drive total return. The fund has provided impressive performance over all time frames since its inception including outperforming common equity benchmarks. The fund was launched in 2014 and is managed by BlackRock, [the world's largest asset manager](#). BlackRock manages an impressive lineup of closed end funds providing a layer of confidence regarding management ability.

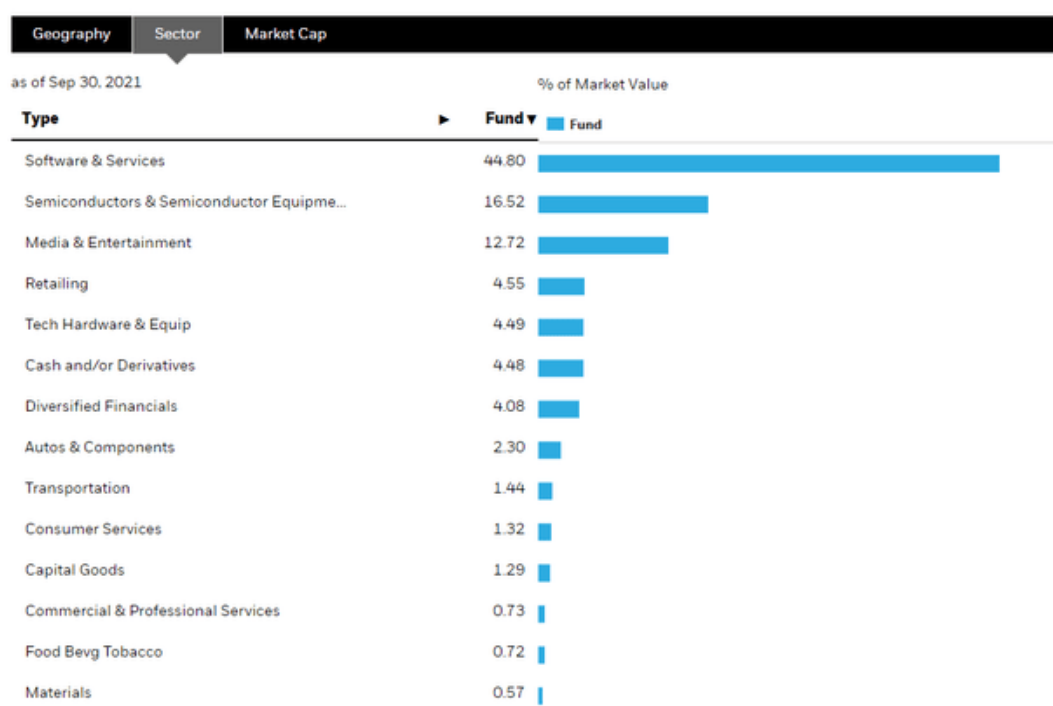
BST offers an effective value proposition to investors. The fund invests in the most successful science and technology companies, employing a yield enhancement strategy to generate additional shareholder return. The fund has delivered on its mission thus far, generating an impressive level dividend which has been increased several times since inception. Given today's investment environment, a fund with a current yield above inflation supported by growth potential is a highly attractive opportunity. Let's see what has led to BST's long term success

Portfolio

BST utilizes a technology driven strategy which has outpaced expectations due to strong sector tailwinds. The fund allocates to current market leaders with strong outlooks, further supporting returns through a [covered call strategy](#). Covered calls involve selling options contracts over positions in the portfolio collecting the premium as excess return. The strategy enhances the overall portfolio yield at the expense of capped upside, should a position take off.

The fund is large with over \$1.8 billion in assets under management. The fund currently has 134 holdings as of the third quarter. Average market capitalization of a portfolio holding is \$443 billion as the fund primarily allocates to industry leaders and established players. The fund does not employ leverage, but 28.23% of the portfolio is overwritten by call contracts. With a conservative portion overwritten, the fund can still benefit from substantial upside potential in a strong run. Sector allocations are consistent with the objectives of the fund with Software (44.8%) and Semiconductors (16.5%) representing the largest fund allocations.

Exposure Breakdowns



Source: [BST](#)

The fund's top ten holdings are recognizable names including Microsoft ([MSFT](#)), Apple ([AAPL](#)), and Alphabet ([GOOG](#)). The portfolio is not particularly concentrated with around a quarter of the total assets dedicated to the top ten positions. Although the portfolio allocated to many mega cap companies, it is refreshing to see smaller players in the top ten, including Marvell Technology ([MRVL](#)).

Holdings

Top			
as of Sep 30, 2021			
Name	Weight (%)	Name	Weight (%)
MICROSOFT CORPORATION	3.64	MARVELL TECHNOLOGY INC	1.99
APPLE INC	3.63	PAYPAL HOLDINGS INC	1.86
ALPHABET INC	2.47	ASML HOLDING NV	1.74
AMAZON.COM INC	2.10	PROJECT DEBUSSY	1.74
PROJECT KAFKA ORDINARY	2.07	SQUARE INC	1.69

Source: BST

The fund's allocation is consistent with the goals stated in the prospectus. Having said that, the technology and semiconductor focus leaves the fund exposed should sentiment change around the sectors. History has produced lucrative returns for technology shareholders, often at the expense of extreme valuations. In fact, Information Technology has led sector returns for the S&P 500 in three out of the past four years. So far, many of these valuations have been supported by unparalleled long term growth in software and broader technology.

S&P 500 Sector Performance

2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	YTD
ENRS 34.4%	CONS -15.4%	INFT 61.7%	REAL 32.3%	UTIL 19.9%	FINL 28.8%	COND 43.1%	REAL 30.2%	COND 10.1%	ENRS 27.4%	INFT 38.8%	HLTH 6.5%	INFT 50.3%	INFT 43.9%	ENRS 45.6%
MATR 22.5%	HLTH -22.8%	MATR 48.6%	COND 27.7%	CONS 14.0%	COND 23.9%	HLTH 41.5%	UTIL 29.0%	HLTH 6.9%	TELS 23.5%	MATR 23.8%	UTIL 4.1%	TELS 32.7%	COND 33.3%	FINL 25.7%
UTIL 19.4%	UTIL -29.0%	COND 41.3%	INDU 26.7%	HLTH 12.7%	REAL 19.7%	INDU 40.7%	HLTH 25.3%	CONS 6.6%	FINL 22.8%	COND 23.0%	COND 0.8%	FINL 32.1%	TELS 23.6%	REAL 23.3%
INFT 16.3%	TELS -30.3%	REAL 27.1%	MATR 22.2%	REAL 11.4%	TELS 18.3%	FINL 33.0%	INFT 20.1%	INFT 5.9%	INDU 18.9%	FINL 22.2%	INFT -0.3%	S&P 31.5%	MATR 20.7%	TELS 19.7%
CONS 14.2%	COND -33.5%	S&P 26.5%	ENRS 20.5%	TELS 6.3%	HLTH 17.9%	S&P 32.4%	CONS 16.0%	REAL 4.7%	MATR 16.7%	HLTH 22.1%	REAL -2.2%	INDU 29.4%	S&P 18.4%	INDU 16.4%
INDU 12.0%	ENRS -34.9%	INDU 20.9%	TELS 19.0%	COND 6.1%	S&P 16.0%	INFT 28.4%	FINL 15.2%	TELS 3.4%	UTIL 16.3%	S&P 21.8%	S&P -4.4%	REAL 29.0%	HLTH 13.5%	S&P 15.3%
TELS 11.9%	S&P -37.0%	HLTH 19.7%	S&P 15.1%	ENRS 4.7%	INDU 15.4%	CONS 26.1%	S&P 13.7%	S&P 1.4%	INFT 13.9%	INDU 21.0%	CONS -8.4%	COND 27.9%	INDU 11.1%	MATR 14.5%
HLTH 7.2%	INDU -39.9%	FINL 17.2%	CONS 14.1%	INFT 2.4%	MATR 15.0%	MATR 25.6%	INDU 9.8%	FINL -1.5%	S&P 12.0%	CONS 13.5%	TELS -12.5%	CONS 27.6%	CONS 10.8%	INFT 13.8%
S&P 5.5%	REAL -42.3%	CONS 14.9%	FINL 12.1%	S&P 2.1%	INFT 14.8%	ENRS 25.1%	COND 9.7%	INDU -2.5%	COND 6.0%	UTIL 12.1%	FINL -13.0%	UTIL 26.4%	UTIL 0.5%	HLTH 11.9%
COND -13.2%	INFT -43.1%	ENRS 13.8%	INFT 10.2%	INDU -0.6%	CONS 10.8%	UTIL 13.2%	MATR 6.9%	UTIL -4.8%	CONS 5.4%	REAL 10.9%	INDU -13.3%	MATR 24.0%	FINL -1.7%	COND 10.3%
REAL -17.9%	MATR -45.7%	UTIL 11.9%	UTIL 5.5%	MATR -9.6%	ENRS 4.6%	TELS 11.5%	TELS 3.0%	MATR -8.6%	REAL 3.4%	ENRS -1.0%	MATR -14.7%	HLTH 20.8%	REAL -2.2%	CONS 5.0%
FINL -18.6%	FINL -35.3%	TELS 8.9%	HLTH 2.9%	FINL -17.1%	UTIL 1.3%	REAL 1.6%	ENRS -7.8%	ENRS -21.1%	HLTH -2.7%	TELS -1.3%	ENRS -18.1%	ENRS 11.8%	ENRS -33.7%	UTIL 2.4%

Source: [Novel Investor](#)

It is worth noting that the fund does not employ leverage. Closed end funds can issue debt and preferred shares to employ leverage internally. The capital is reinvested with the anticipation of excess return over the financing cost. The results are magnified returns for shareholders, assuming those spreads are positive. Increases in underlying interest rates will directly increase the financing cost for the fund. BST's lack of leverage protects the fund from these risks. Other funds may be challenged to maintain current distributions should rates rise substantially. Meanwhile, BST will be structurally protected.

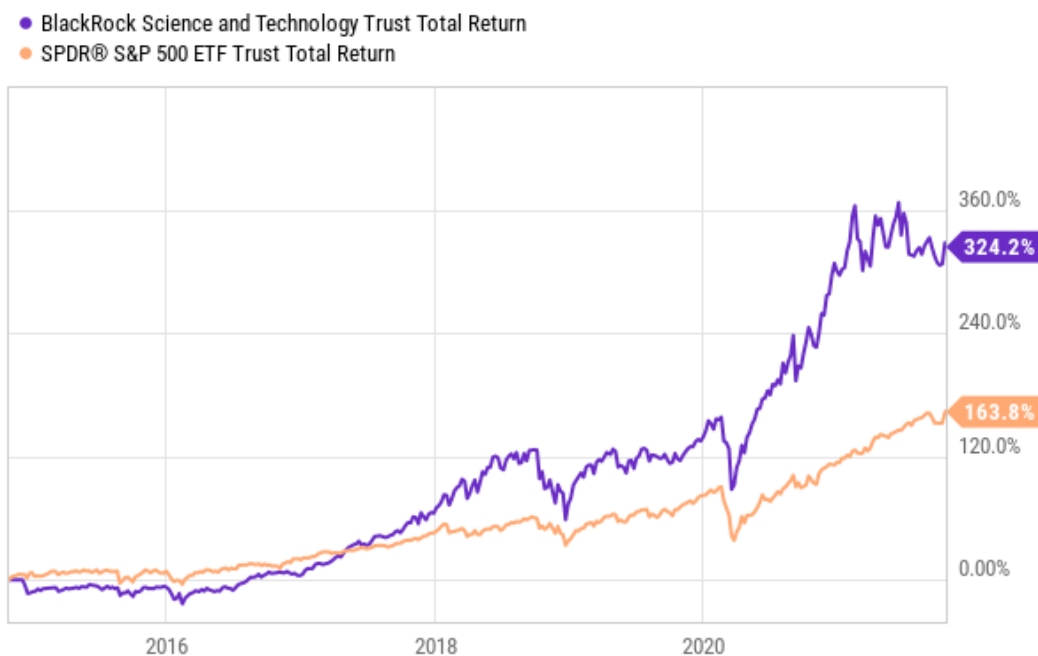
The fund charges a reasonable expense ratio of 1.00%.

BlackRock has garnered a reputation for low expense ratios due to their scale. While the fund's management fee is not the lowest in the CEF sphere, it is reasonable. The expenses are straight forward without needing to account for leverage expenses.

Performance

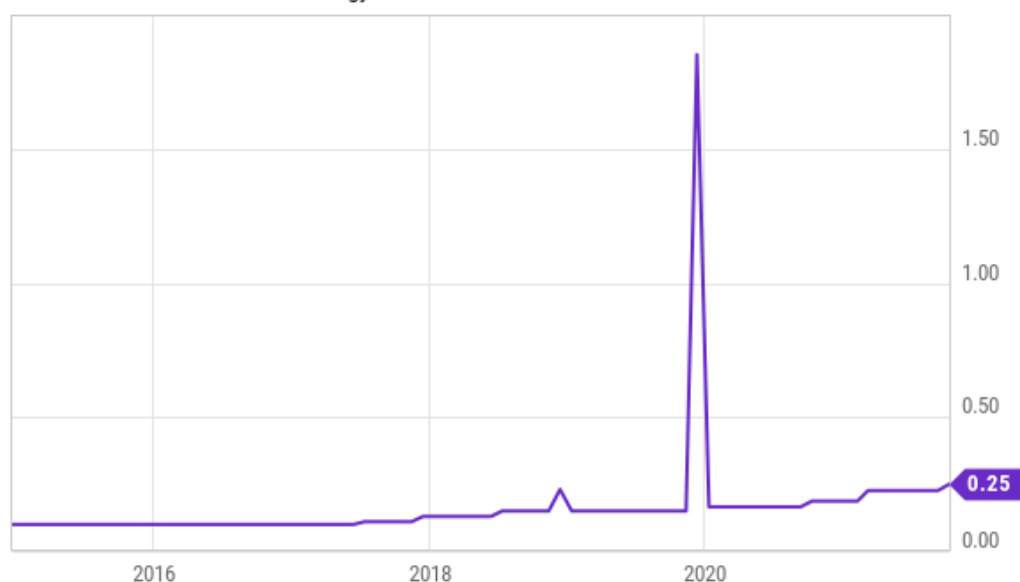
BST has seen incredible performance driven by unprecedented strength in technology. While tech has led the market over the past several years, pandemic related tailwinds have reinvigorated shareholder enthusiasm. As a result, BST has outperformed major indexes and likely shareholder expectation, delivering rising distributions and NAV growth.

As we mentioned, BST pays a level dividend distribution which is generated through dividends, capital gains, and options premiums. The fund delivers performance primarily through dividend distributions, consistent with most closed end funds. However, BST has stood out from the pack in offering investors impressive share price appreciation as well. As a result, the fund has outperformed the S&P 500 since inception. In fact, a total return of 324.2%, not accounting for tax liabilities, nearly doubles the S&P 500 since inception. On an annualized basis, BST has delivered a 24.26% annual return since inception.



BST's strong absolute return is indicative of a successful strategy. Accordingly, shareholders should expect that the distribution is equally strong. BST has successfully maintained a level distribution since inception, even delivering several increases along the way. The fund additionally distributed a substantial special dividend in 2019. The fund currently distributes a \$0.25 monthly dividend per share, which was recently increased 10.6% from \$0.226 per share. The increase marks the seventh bump in the fund's dividend since inception. BST has provided at least one increase per year since 2016.

BlackRock Science and Technology Trust Dividend

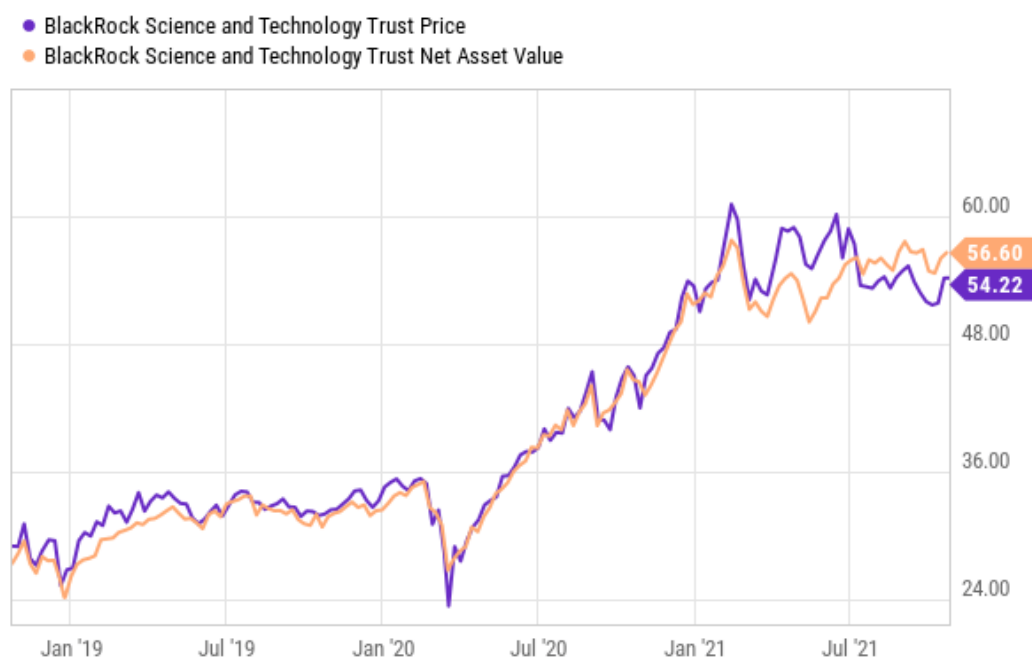


The steady, growing income provided by the fund is more attractive when accounting for the substantial NAV growth along the way. Sector performance has driven a substantial portion of the growth as BST continues to make distributions. Income seeking investors typically do not seek out high growth sectors such as tech, which reinvest a substantial portion of profit for research and development. However, the CEF structure provides the monthly distributions necessary to generate attractive income. Should sector performance continue to be strong, the fund should continue to perform well, assuming the valuation holds.

So how does BST stack up as an income producing asset? This distribution is certainly not the highest offered by any CEF, however it offers a substantial spread over other asset classes. The fund's dividend yield currently outpaces other fixed income instruments, including high yield debt. Additionally, BST outpaces real assets as the distribution offers a meaningful spread over the Vanguard Real Estate ETF's dividend.

Valuation

Closed end funds trade independently of their net asset value or NAV. Share price trades freely based on upward and downward pressure from the market despite a very transparent net asset value. While strong share price performance is generally supported by NAV growth, this is not always the case. Substantial discrepancies can arise with income shareholders footing a price substantially above what is essentially book value. Recently, we highlighted the PIMCO Corporate & Income Opportunity Fund (PTY) which trades at an expensive 27% premium to underlying assets. While the fund has performed well, an opportunity to buy into a portfolio for such an exorbitant cost can leave shareholders exposed. Meanwhile, BST trades at an attractive discount to underlying assets.



Despite impressive performance in NAV, BST has continued to trade at a discount. The current valuation offers new shareholders an opportunity to purchase shares of the fund for below their book value. While investors often describe discounts as purchasing assets "on sale", that thesis only holds water if the valuation reverts to a premium.

BlackRock Science and Technology Trust Discount or Premium to NAV



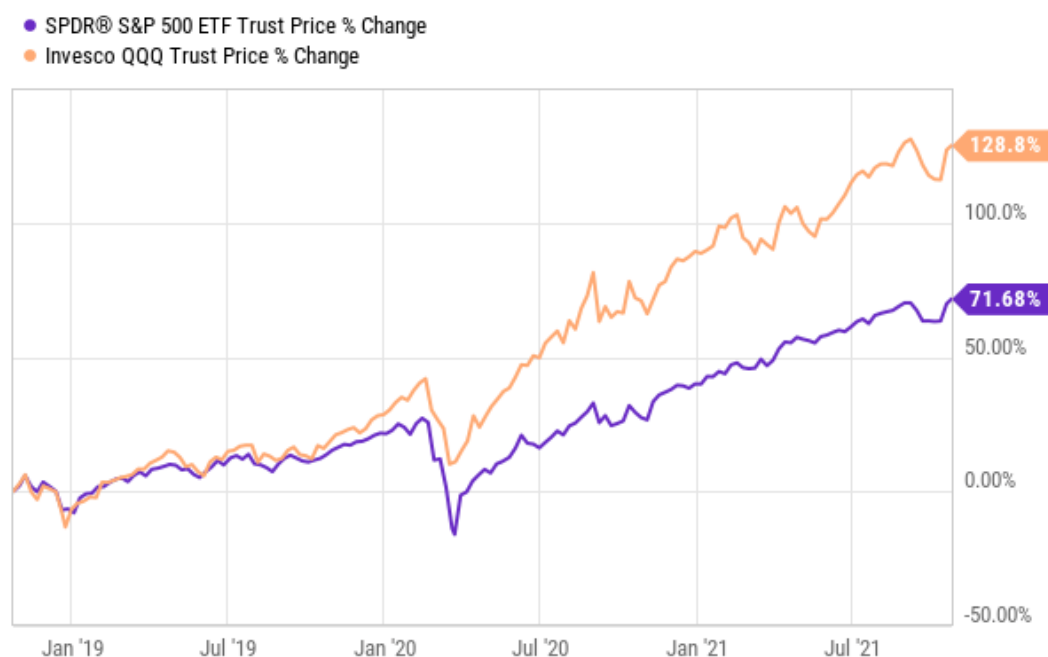
Seeking Alpha^α

Oct 25 2021, 2:34PM EDT. Powered by **YCHARTS**

Earlier this year, BST traded at a premium to NAV. At the highest point, BST traded at a 10.32% premium to net asset value, far above the current discount of 5.00%. BST's current discount is nearly the deepest of the past three years. The fund traded at a deeper discount through 2016 and 2017. Given strong historical performance and sentiment around technology, the valuation may remain stable. However, only time will truly tell.

Risks

Although BST currently trades at an attractive valuation, the fund's constituents may not. The strong economic rebound of COVID-19 has propelled an unprecedented performance of the S&P 500, specifically tech. As the chart below shows, both the SPDR S&P 500 Trust ETF ([SPY](#)) and Invesco QQQ ETF ([QQQ](#)) have both dramatically exceeded pre-pandemic prices.



Seeking Alpha^α

Oct 25 2021, 2:51PM EDT. Powered by **YCHARTS**

BST has directly benefitted from the strong performance of the broader index due to portfolio overlap. Much of this gain stems from stretching valuations in addition to underlying earnings performance. As earnings have risen, performance has outpaced and as you can see, the current multiple of 28.79x may present concerns. The valuation even looks reminiscent of the lead up to the tech bubble in 2000, however, we acknowledge that the landscape is fundamentally different today.

S&P 500 PE Ratio



Source: [Multpl](#)

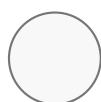
In any event, investors should take note that a portion of BST's performance has been driven by an unsustainable expansion of underlying valuations. It is unlikely the expansion will continue aggressively, and earnings must exceed expectations or share prices will fall to normalize valuations. In any event, a normalization of valuations, especially in the technology sector could be challenging for BST's NAV performance. The dividend should remain sustainable, but the fund's incredible share price outperformance may not hold.

Conclusion

Given the extraordinary success of the technology sector, BST's performance speaks for itself. The fund has offered an attractive combination of yield and growth, delivering outperforming returns to shareholders over a variety of time frames. The level, but increasing dividends offer an opportunity to income investors, especially as inflation rates remain uncharacteristically high. The lack of leverage also makes the fund attractive relative to others in the CEF sphere and provides downside protection during periods of stress.

Investors willing to stomach valuation and market risk should keep BST on a watchlist as discounts continue to offer opportunities to enthusiastic shareholders. BST is a simple opportunity to ride the technology wave that has propelled our digital economy, all while enjoying monthly dividends.

This article was written by



Obsidian Limited

346 Followers

Obsidian Limited provides investors with income focused insights and research. Using a unique approach, we... [more](#)

Disclosure: I/we have a beneficial long position in the shares of SPY, QQQ either through stock ownership, options, or other derivatives. I wrote this article myself, and it expresses my own opinions. I am not receiving compensation for it (other than from Seeking Alpha). I have no business relationship with any company whose stock is mentioned in this article.

Additional disclosure: This article is not to be considered investment advice. Research provided in this article is supportive of your own thorough and complete due diligence. Please consult your investment advisor on opportunities presented herein.

3 Likes

3 Comments

Comments

Newest

