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SHARES

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HEALTHCARE HEROES:

Invest in the companies trying to save the world from coronavirus

PLUS

COMPANY FUNDRAISING HITS **£2BN** AS FIRMS **TAP UP SHAREHOLDERS**

HOW DEFENSIVE IS THE **DEFENCE SECTOR** DURING THE CORONAVIRUS CRISIS?

THE **THEMATIC FUNDS** THAT STAY **ONE STEP AHEAD** OF THE CROWD

A simple guide to understanding market corrections

It's fairly easy to understand why shares fall and how stocks behave in different ways

A reader wants to know how market corrections work, why certain stocks fall more than others, who is selling and why some stocks bounce back first.

Stock markets involve buyers and sellers making transactions based on expectations for what might happen to a business. The price will fall if more people want to sell a stock than buy.

Equity ratings also play a role in the level of share price decline. Let's say the coronavirus crisis causes two different companies to suffer the same amount of decline to earnings. In this situation, something trading on 30 times forecast earnings is likely to fall by a greater amount than something on 10 times earnings.

For example, Company X might be trading at 200p, which is 10 times the 20p earnings per share it is forecast to make. If the market believes those earnings will drop by 25% to 15p, to maintain a price-to-earnings ratio of 10 the stock would, in theory, drop to 150p.

However, let's say Company Y is trading at 600p, which is 30 times the 20p EPS it is forecast to make. To reflect the same 25% drop in earnings, investors would effectively sell down to 450p assuming it still commanded a PE of 30.

In reality, investors may no longer be prepared to pay a premium rating, so it might de-rate to a PE of 20. Doing the maths (20 x 15), it would, in theory, trade at 300p – so its share price has halved versus a 25% drop for Company X.

Expectations were already low for Company X, given it was on a PE of 10, so there is a chance it doesn't de-rate beyond adjusting for lower earnings.

You also need to consider how the market would view a company in the current situation. **Tesco (TSCO)**, for example, has held up better than **Associated British Foods (ABF)**, because its shops are still open and demand is high. The latter owns Primark whose shops are shut, thus a chunk of its revenue has disappeared overnight. Of the two, Tesco might be seen as more attractive to investors and therefore command a higher rating. This is not the case at the moment so one has to consider if Tesco is underpriced or ABF overpriced.

It is impossible to say exactly who is selling the shares in a correction, apart from to say institutional investors must report if their positions above a certain level have changed.

In reality it could be a wide range of investors. Fund managers might have been forced to sell if their clients asked for their cash back. Retail investors might have sold if they were scared.

Traders – both institutional and retail – might short-sell certain stocks if they believe they will fall in price, as that would give them a profit. The FCA publishes a daily list revealing the institutions shorting stocks.

Leisure and oil stocks have been rallying hard following the big sell-off last month. That's because many of them were priced to go bust. Airlines are now getting government loans, investors are becoming more optimistic about the crisis being resolved soon, and oil prices have started to pick up. Therefore investors are reappraising these sectors, hence why their shares are shooting back up again. The big question is how long this recovery rally will last.

Readers should email any further questions about the market to editorial@sharesmagazine.co.uk and we'll do our best to respond in a future issue of *Shares*.

By **Daniel Coatsworth** Editor

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£2bn raised by London-listed companies in race for cash

Institutional shareholders seem to be quite willing to support companies during dark times and they're getting a good price on new stock

Approximately £2bn has now been raised by 63 London-listed companies since the start of March as businesses race to strengthen their finances during the coronavirus crisis. Of these, 34 companies have each raised £5m or more, nearly all at a discount to the market price before the fundraising was announced.

So far the biggest raises have been by cruise ship operator **Carnival (CCL)** for £400m, online fashion retailer **ASOS (ASC:AIM)** for £247m, travel retail firm **SSP Group (SSPG)** for £215m, recruitment firm **Hays (HAS)** for £200m and car-selling portal **Auto Trader (AUTO)** for £186m.

Companies are generally increasing their issued share capital by a fair chunk in order to secure new cash, thereby diluting existing investors.

At one end of the spectrum is Auto Trader which only issued 5% of its existing capital, while at the other extreme **City Pub Group (CPC:AIM)** intends to issue almost 42% of its existing capital in new shares to raise just £22m, assuming there is full take-up of its open offer component of the fundraise.

The average share price gain upon the fundraising news for the top 10 equity raisers was 11%, which suggests investors believe the

TOP 10 EQUITY RAISINGS SINCE 1 MARCH 2020

Company	Amount raised	% of existing share capital being issued	Share price reaction to fundraise
Carnival	£400m	28.8%	-9%
ASOS	£247m	18.8%	28%
SSP Group	£215m	19.3%	19%
Hays	£200m	14.3%	11%
Auto Trader	£186m	5.1%	4%
Assura	£185m	10.0%	0%
WH Smith	£166m	13.7%	13%
Restaurant Group	£57m	19.9%	3%
City Pub Group	£22m	41.6%	19%
Hotel Chocolat	£22m	8.5%	18%

Source: Shares, Peel Hunt

companies are doing the right thing by coming to the market for money.

MAKE OR BREAK

So why are companies raising money now, and why are they tapping shareholders instead of using the Government's £330bn Covid Corporate Financing Facility which is there specifically to provide funding for companies that need it?

Online retailer ASOS said the £247m equity raise and the extension to its debt facilities would 'put sufficient financing in place to weather no improvement in current trading for at least 18 months', and would enable it to emerge from the current crisis in a stronger financial position to continue to invest in the growth of the business.

Reading between the lines, we suspect that in exchange for agreeing to extend its debt facilities and loosen its covenants, the banks told ASOS to go and tap the market for money to offset some of their risk.

This is also no doubt what happened at Carnival which had to go cap in hand to investors by issuing new shares while at the same time issuing billions in debt at interest rates as high as 11.5%.

OPPOSING VIEWS

While most investors are bracing themselves for more cash calls, Invesco fund managers Mark Barnett and Martin Walker wrote to 200 or more UK companies last week warning them that the case for raising equity had to be compelling.

Barnett and Walker said that unless companies had 'a strong rationale' for coming to the market to raise money they wouldn't support them, and they urged companies to make use of the £330bn Government Covid scheme instead. They said that current market valuations mean that equity is both 'precious and expensive'.

QUALITY FIRST

According to Oliver Brown, co-manager of the **MFM Primary Opportunities Fund (B8HGN52)** which specialises in buying new and secondary issues, a telling feature of the current crop of fund raisings is the above-average quality of the companies which have come to the market first.

'SSP and WH Smith are world-leading businesses with great assets and great margins, and their share prices are down 50% or more. In a year or

so these firms will be back trading "normally" again,' he says.

In the case of premium chocolatier **Hotel Chocolat (HOTC:AIM)**, the firm raised funds to finance the expansion of its production facilities and more store openings in Japan, notes Brown.

Peel Hunt says additional liquidity/strengthening the balance sheet is the most cited reason for getting new cash from shareholders. 'However, some have flagged that the funds will be used on working capital or acquisitions, which points to more medium-term thinking and potential for share gains,' it adds.

FINANCIAL ADVANTAGE

Recruiter Hays raised £200m from its top shareholders because it saw a long-term opportunity and didn't want to take on debt.

It says raising cash will allow it to capitalise on organic growth opportunities with new and existing blue-chip clients. In fact it says it is already seeing new opportunities emerge.

As finance director Paul Venables explains to *Shares*: 'The coronavirus crisis is a defining moment. No-one has witnessed such a uniform drop in activity before and no-one knows when it will end, but we are now the best-capitalised firm in the sector and we are already attracting new business.'

He says clients are looking to reduce their number of suppliers to those that are financially sound, which should work to Hays' advantage. Venables adds: 'You don't want debt in good times and you certainly don't want it in bad times when you have no idea how long the recovery could take.'

While Hays has deferred £100m in taxes in line with Government guidelines, those taxes are effectively 'debt' which will have to settled at some point. Companies which take on additional debt at this point – including from the Government's Covid facility – risk ultimately breaking their banking covenants, warns Venables.

Promising signs as Next gets back to business

Retailer's 'very limited' re-opening could be a model which others follow

Next quickly sold out of its limited items as online sales resumed

The 'very limited' re-opening of clothing and homewares retailer **Next's (NXT)** online operations (14 Apr) shows businesses' emergence from the coronavirus-enforced shutdown is likely to be a gradual process.

Next's phased reintroduction of its online operations shows that the recovery will happen in slow motion.

Companies across all industries will need to focus on safer ways of working and confidence among shoppers will take time to return, especially if infections persist. Across Europe, some countries have allowed partial returns to work, but others have extended their lockdowns, the UK among them.

GRADUAL RE-OPENING

Having shuttered its physical stores, Next closed its online business in late March after staff at its warehousing and distribution operations expressed concern that they were still being made to work. The retailer has since re-opened online (14 Apr) but in a very limited way and only after implementing extensive additional safety measures.

Chief executive Simon Wolfson said the idea was to 'begin selling in low volumes, so that we only need a small number of colleagues in each warehouse at any one time, helping to ensure rigorous social distancing is complied with'.

Encouragingly for Next, appetite for its offering remains strong. The business hit its self-imposed daily order limit before 8.30am on re-opening and closed the site until the following day.

SALES SUBDUED

Shore Capital points out that rival clothing retailers have continued to trade their online operations despite shuttering physical shops as part of the government lockdown, including John Lewis and **Marks & Spencer (MKS)**, while shoppers have been able to purchase online from the likes of Amazon and online pure-plays **ASOS (ASC:AIM)**, **Boohoo (BOO:AIM)** and **Sosandar (SOS:AIM)**.

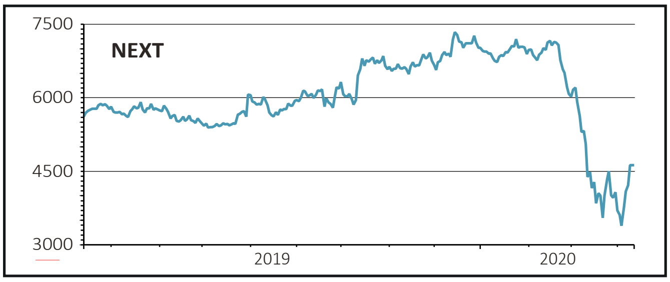
Yet the broker's view is that online order quantities will have been somewhat subdued given the restrictions on going out/cancelled holidays across Europe. 'It remains to be seen what real appetite there is for online clothing currently given the "stay at home" message and travel restrictions,' says Shore Capital.

Peel Hunt argues Next will gradually build volumes, capacity and ranges for sale over time, while maintaining a clear focus on safe working practices.

'We believe the business has a role to play in helping to clear excess third-party stock across its platform, accelerating recovery as we come out of lockdown.'

It adds that the firm will 'come out of this in a stronger market position'.

This pattern could well be repeated across other sectors with the more robust businesses able to weather the storm and pick up share from those which do not survive.



What will the coronavirus crisis mean for the defence sector?

For now defence-orientated firms are holding up much better than aerospace specialists

On 19 March NATO secretary general Jens Stollenberg made a plea for allies to maintain defence spending despite the significant economic costs associated with the coronavirus crisis.

The simple fact he was even making this statement reflects a genuine fear that expenditure in this area will be cut as public finances become more strained.

This would have clear implications for the defence sector. Because of the significant crossover in the skills and expertise required, many companies operate across the spectrum of defence and commercial aerospace and index provider FTSE combines the two in its sector classification.

However, looking at the FTSE 350 firms which sit in this classification there is a clear delineation between those which are principally focused on aerospace and those which specialise in defence.

Defence exposure has helped performance

Company	Defence and security exposure	Performance year-to-date
Avon Rubber	73%*	33.5%
BAE Systems	79%	-5.6%
QinetiQ	circa 90%+	-7.0%
Ultra Electronics	circa 90%+	-8.9%
Chemring	100%	-16.8%
Babcock	46%	-36.0%
Rolls-Royce	21%	-52.0%
Meggitt	36%	-57.6%
Senior	10%	-61.5%

Source: Latest annual reports. Sharepad, data to 9 April 2020.
*Also includes protection for emergency and security services, remaining exposure is to dairy industry

DIVERGING FORTUNES

The table offers a rough guide to companies' defence exposure and shows their share price performance year-to-date.

While defence-orientated firms have seen their shares hold up reasonably well through the market turmoil, aerospace specialists have struggled.

This makes sense. The latter category of businesses serve the big plane manufacturers like Airbus and Boeing which are currently suspending production at assembly plants to protect workers. The customer base for new planes – global airlines – are facing an indeterminate period of virtually zero demand with their fleets grounded.

The long-term implications for how coronavirus will impact air travel demand is hard to gauge but even if the huge drop in passenger numbers proves to be short term, it will have a lasting impact.

Planes and individual parts will not need replacing as soon as expected given the reduction in flight hours and those airlines which do survive will have more limited capability to invest.

This has particular implications for **Rolls-Royce (RR.)** which derives a substantial chunk of its income from spares and repairs-type agreements linked to its installed base of Trent-series engines.

WILL DEFENCE BE DEFENSIVE?

Investment bank Berenberg believes defence should, in relative terms, prove a safe haven amid the coronavirus with, in its view, the impact limited in the immediate future to 'operational disruption because of containment or disruption measures'.

It adds: 'Over the longer term, the fundamentals of defence are unchanged: 1) spending globally, and more importantly in the US, remains at an elevated level compared to history; '2) an increasing number of militaries are undertaking major equipment modernisation plans; and 3) global strategic threats are undiminished.

'Order books and win rates remain high with current business underpinned substantially by long-term contracted and committed programmes.'

While this argument has some merit, there are reasons investors shouldn't be complacent about the prospects for defence firms.

Dominant name **BAE Systems (BA.)** certainly isn't taking anything for granted judging by its most recent trading update (3 Apr).

While it didn't see any coronavirus impact in the first quarter, it has seen 'more significant disruptions' going into the second quarter. Payment of the full year dividend has been deferred (not cancelled yet) with an update on the payout promised alongside first half results on 30 July.

It is also taking measures to conserve cash, though it is pressing ahead with the $2.2bn acquisitions of the Collins Aerospace military GPS business and Raytheon airborne radios division with financing for these deals already in place.

ACTIONS BY OTHERS

On 14 April, **Ultra Electronics (ULE)** deferred the payment of its full year dividend of 39.2p even if it had not yet seen a deterioration in trading, and countermeasures specialist **Chemring (CHG)** reported all of its businesses remained open and kept its own full year payout in place. On 25 March tech and equipment supplier **Avon Rubber (AVON)** announced the award of a body armour contract that could be worth up to $333m over its three and a half year term.

In a blog post for think tank the Atlantic Council, security experts Christopher Skaluba and Ian Brzezinski write: 'There will be pressure to shift financial priorities to address the fiscal and health consequences of this pandemic, which could sound the death knell to the 2014 Wales defense investment pledge in which NATO nations recommitted to spending an equivalent of 2% of gross domestic product (GDP) on defense.'

Given many defence programmes tend to be multi-year affairs it may take time for the impact of the coronavirus to feed through.

As the chart on US defence spending shows, expenditure continued to grow in the immediate aftermath of the 2007/08 global financial crisis with the cuts only coming through in 2012 and 2013 – though this also reflected the dialling down of US commitments in Iraq and Afghanistan.

FINDING GROWTH ELSEWHERE COULD BE TRICKY

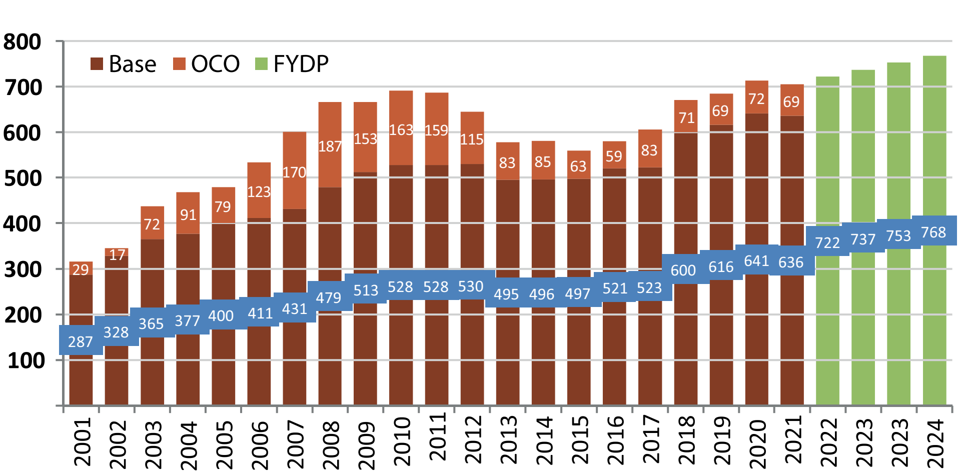
Another factor to consider is that spending in other markets, notably the Middle East, made up for cuts in Europe and the US in the wake of the financial crisis.

With the economic impact of coronavirus more widespread and with Middle Eastern countries in particular exposed to the collapse in oil prices, these markets seem less primed to provide an alternative source of growth this time round.

Prior to the full impact of coronavirus becoming apparent we argued BAE shares were worth buying on the basis of growing exposure to the world's largest defence market in the US and to areas of priority like weapon systems and secure communications.

With the shares now at a cheaper price we remain positive on the long-term story. However, investors may have to accept some deterioration in the outlook.

US defence spending ($bn): elevated level of spending to be maintained



Source: Berenberg estimates, US DoD, FYDP

FYDP: future years defense program OCO: Overseas contingency operations

Domino's Pizza is a rare lockdown winner

That's handy as a new boss is about to join and hopefully fix some big problems

DOMINO'S PIZZA
BUY
(DOM) 299p

Market cap: **£1.4bn**

One of the few winners of the country-wide lockdown is **Domino's Pizza (DOM)** as demand surges for takeaway food. Over the first week of the lockdown the company saw an acceleration in deliveries which more than offset the lack of collection business, which account for around a fifth of sales.

Like-for-like sales growth was driven by an increase in items per order and a higher overall ticket price.

Stockpiling of essential foods resulted in empty supermarket shelves, driving more people to takeaways. While supermarkets are now starting to have better availability of food and drink, it is still very hard to get a slot for home delivery. That should encourage people to keep using takeaway providers like Domino's more frequently, particularly if the media keep showing images of large queues to get into supermarket stores.

The general uncertainty around the factors driving the spread of coronavirus has raised the public's consciousness around food safety and hygiene practices. In times of uncertainty people tend to gravitate towards products they know and trust. Domino's has reminded customers that it operates to the highest standards of hygiene, ensuring the safety of its products.

In addition, the company has worked closely with its suppliers and distribution network in order to stay fully operational with minimal disruptions, something the supermarkets have found more challenging. All of the company's drivers and supply chain workers are categorised as key workers. These factors reinforce the strength of the brand and make life difficult for smaller competitors.

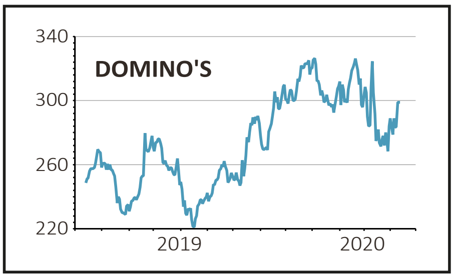
Analysts have been steadily upgrading their earnings expectations over the last three months, in contrast to the great majority of companies which have seen downgrades.

Domino's is taking advantage of the freeze in business rates and the VAT payments referral, which will benefit its franchisees, and the board is looking at other measures to support them as required.

Also important to the investment case is the long-awaited appointment of a new chief executive. Dominic Paul, the former boss of Costa Coffee, will join in May and his first job will be to repair shattered relationships with Domino's franchisees who want a greater share of profits.

The company has been in limbo for some time due to the franchisees' reluctance to keep investing in new stores for diminishing returns. Its overseas expansion has also been a flop and it is now exiting those territories.

We're now at a crucial point for the business where Domino's becomes more streamlined and all the problems are hopefully rectified.



By **Martin Gamble**
Senior Reporter

Homeserve is a resilient pick with growth ambitions

Emergency repairs firm is targeting medium-term expansion in the US and should weather coronavirus crisis

Broadly unaffected by the coronavirus crisis, home repairs firm **Homeserve (HSV)** is a FTSE 250 firm worth owning right now.

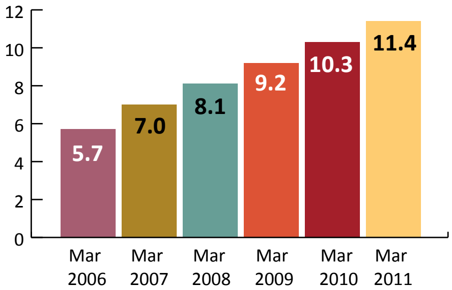
The £3.8bn market cap company is well-placed to come through the crisis with its growth trajectory intact.

A provider of home repair services, Homeserve operates a recurring membership model for its customers and covers them in the event of emergencies such as gas, plumbing and electrical issues.

Berenberg analyst Callum Battersby thinks these recurring revenues will make it a resilient business in the short-term. This makes sense as, with people spending time at home, we are even more reliant on our central heating, hot water and lights and sockets.

Notably, the company grew its policy book in each of 2008, 2009 and 2010 despite the financial crisis raging in the background.

HOMESERVE'S POLICY BOOK GREW THROUGH FINANCIAL CRISIS



Source: Homeserve
Policy numbers (millions)

HOMESERVE BUY
(HSV) £11.45

Market Cap: £3.8bn

In a worst-case lockdown scenario, Berenberg foresees that marketing campaigns (which typically take place in winter) could be paused, which would affect new customer growth. But even this is far from a disaster.

New customers for Homeserve are typically loss-making in year one, breakeven in year two and only profitable in their third year on the service.

Paradoxically, this means that there would actually be a benefit if business development projects are cut towards the end of the year (albeit future growth would be lower).

There could be a negative impact on the group's loss-making platform businesses, Checkatrade, eLocal and Habitissimo.

These platforms market more discretionary trade jobs, and therefore will be hit by falling demand under a lockdown scenario.

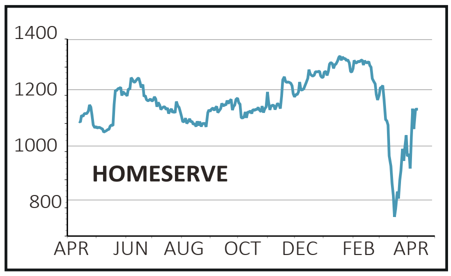
While Homeserve will cut marketing expenses to offset this slowdown in demand, Berenberg expects it to continue investing in the platforms, resulting in an increase in the division's losses.

In the near term, this could largely offset continued growth in membership earnings, although it will support the medium-term growth for these websites.

Well established in the UK and France, where it has grown the business to maturity, Homeserve is aiming to crack America.

Berenberg points out the US market is significantly bigger yet 'largely untapped', and thinks that US growth can double Homeserve's profits in the next three to five years.

The company is still relatively expensive and does trade on 23 times its 2021 forecast earnings. Ultimately, investors face a choice at present between buying out of favour businesses which are heavily exposed to coronavirus with all the risks that entails, or paying up for the reassurance of a business like Homeserve which has a much clearer outlook.



By **Yoosof Farah**
Reporter

TESCO

(TSCO) 232.3p

Gain to date: 8.3%

Original entry point:

Buy at 214.5p, 19 March 2019

SHARES IN GROCERY giant **Tesco (TSCO)** jumped 4% to 232p late last week after the company reported a sharp increase in operating profits and confirmed plans to return £5bn to shareholders.

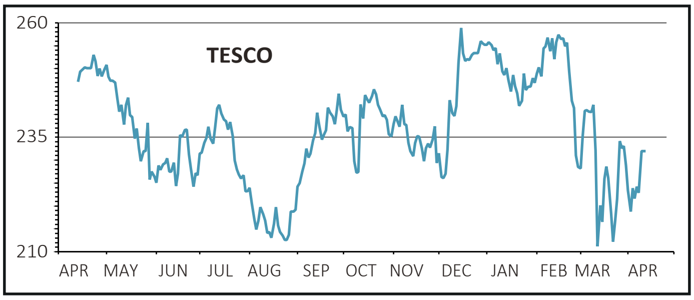
UK and Irish supermarket sales for the year to 29 February, before the Government lockdown came into force, spurring panic buying, were up 0.2% to £44.9bn.

However, operating profits for the UK and Ireland were up 17% to £2.18bn, meaning an operating margin of 4.2%, the highest for some time.

Sales for the Asian business, which is shortly to be sold, were flat at £5.2bn. Part of the proceeds from the sale are going to pay down the company's pension deficit while £5bn has been earmarked as a special dividend.

Tesco also kept its final dividend for the 2019 financial year, taking the annual payout to 9.15p per share, an increase of 58%.

While the company gave no concrete financial guidance for this year, it said that under its base case scenario that sales patterns return to normal by August, it would incur £650m of additional costs which it would be able to offset through Government help and cost cuts.



SHARES SAYS: ↗

Tesco's sales performance and special dividend are compelling reasons to keep owning the shares.

ALLIANCE PHARMA

(APH:AIM) 77.4p

Gain to date: 8%

Original entry point:

Buy at 71.6p, 3 October 2019

PHARMACEUTICALS FIRM **ALLIANCE Pharma (APH:AIM)** continued its trend of strong revenue and profit growth when it reported results for the year ended 31 December 2019 on 7 April, with revenue up 16% to £144m and pre-tax profit up 36% to £31m.

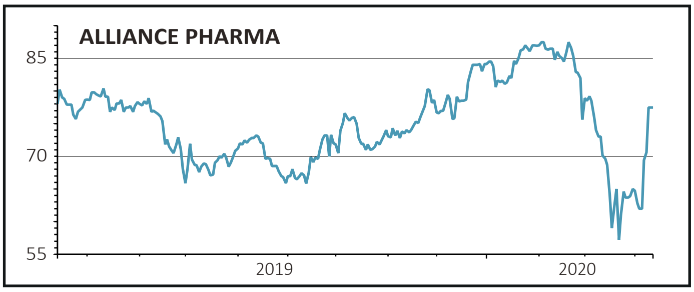
Free cash generation was 81% higher at £29m, which reduced net debt to £59m from £86m last year and resulted in a net debt to earnings before interest, tax, depreciation and amortisation (EBITDA) ratio of 1.48 times, down from 2.3 times.

The international star brands portfolio performed well, delivering like-for-like growth of 30% and these key brands now account for 45% of group revenues, with the percentage expected to increase in the current year.

Local brands delivered a stable performance with revenues of £78.3m (2018: £73m) as the company discontinued a few products as part of the regular review and trimming of the portfolio. Cash generation from these assets is expected to remain strong, reflecting limited promotional investment.

Taking a prudent approach to the ongoing coronavirus pandemic, the board cancelled the final dividend for 2019 to preserve cash.

Remote working practices and a high level of connectivity means the company has seen minimal disruption to the business. The supply chain is said to be holding up well with no material impact in the current year expected.



SHARES SAYS: ↗

We remain buyers.

Lazard Global Thematic Focus Fund

Click Here to Invest

HEALTHCARE HEROES:

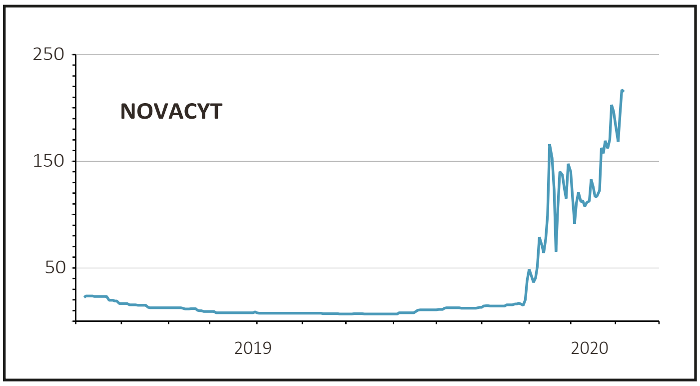
Invest in the companies trying to save the world from coronavirus

By **Martin Gamble**
Senior Reporter

Three of the best performing shares over the last three months are healthcare companies. All of them are at the leading edge, developing testing kits, therapies and vaccines to combat the coronavirus pandemic.

Realistically, developing a vaccine will likely take at least 12 months, and so the immediate priority has been to test as many people as possible alongside isolating those with the virus.

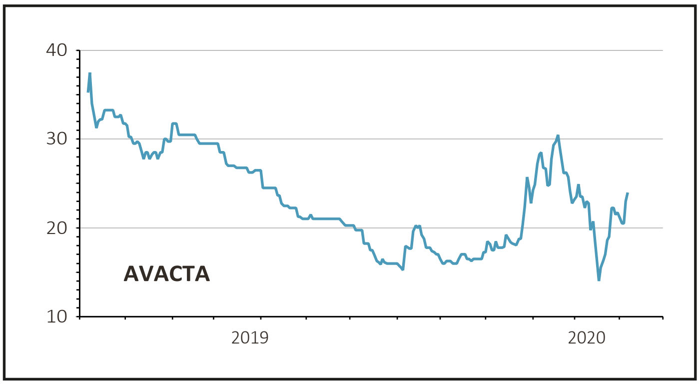
Paris-based company **Novacyt (NCYT:AIM)** has developed a unique testing kit that gives results in under 30 minutes and is being used in hospitals and testing labs. The shares have risen 13-fold since 1 January.



As of 27 March, the company had sold and received orders for over £17.8m of its CE-Mark and research use-only test. Novacyt is now selling its test to more than 80 countries and supplying 21 hospitals across the UK.

Testing is fast becoming very competitive as a number of companies enter the space, such as UK biotherapeutics firm **Avacta (AVCT:AIM)** which on 8 April announced a collaboration with therapeutics company Cytiva to develop a rapid coronavirus test, pushing its shares up 69% on the day.

The company is aiming to get the product approved and ready for sale sometime in the summer. It will be a rapid test, giving results in minutes and will work similar to pregnancy testing strips, but using saliva instead of urine.



Shares in drug discovery company **Synairgen (SNG:AIM)** which specialises in respiratory diseases, have gone up more than 10 times this year, while anti-microbial hand sanitiser firm **Byotrol (BYOT:AIM)** has seen its shares more than triple.

THREE LINES OF ATTACK

There are three broad approaches being explored simultaneously by over 30 pharmaceutical and biotechnology firms across the globe in the race to produce a vaccine.

The traditional approach is to test new candidate molecules, but this will take considerable time and resources, both currently in short supply.

The rapid spread of the virus combined with the lack of bed capacity at hospitals has created an urgency which puts other, faster approaches directly into the spotlight.

That's not to say that the search for a new molecule isn't worthwhile because all successful exits from the pandemic require an effective vaccine to be found.

The second line of attack is to test the broad spectrum of antivirals already on the market to see if they can be used in the fight against coronavirus. These drugs have already been approved for certain use, saving valuable testing time needed to approve new drugs.

Antivirals were designed to reduce the inflammation associated with a large immune system response, which can ultimately lead to death if untreated. The downside to using this approach is that antivirals are not specific to treat coronavirus.

EXPLORING DRUGS USED TO TREAT OTHER DISEASES

The most promising approach near-term involves repurposing existing drugs that have shown some success in treating other diseases. Similar to the advantages provided by antivirals, this approach could mean getting a vaccine to market much faster than the traditional approach.

For example, some people have high hopes for Remdesivir, a drug originally developed by US firm **Gilead Sciences** for treating Ebola.

Before we go on to discuss some of the promising candidates, we should mention an important caveat. The scientific data gathered so far in this category is either of low quality (no double-blind randomised testing) or at the pre-clinical stage with limited hard data.

A double-blind study is one in which neither the participants nor the experimenters know who is receiving a particular treatment. This procedure is utilised to prevent bias in research results.

REMDESIVIR

The optimism for this drug stems from a 2017 paper showing it was effective against other viruses and could also improve the respiratory function in mice.

More recently, a single case report described clinical improvement after receipt of Remdesivir in a patient infected with coronavirus whose clinical status was worsening prior to receiving the drug. While encouraging, scientists need harder evidence.

Analyst Adam Barker at broker Shore Capital highlights two trials being undertaken by Gilead that may prove instrumental in establishing the drug's effectiveness.

One is being tested on around 600 patients with moderate symptoms and the other is testing 400 severe cases, both due to be completed in May.

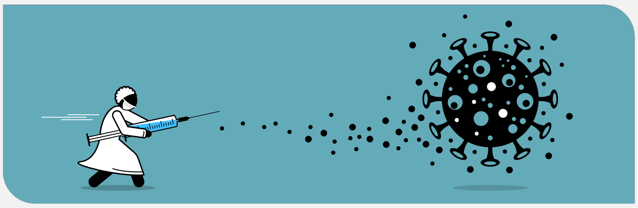
KALETRA

Developed by US firm **Abbvie**, this candidate was originally used as an HIV drug and has seen promising results in human studies against SARS and MERS, although the quality of the data is not great.

However, more robust studies are underway to support the initial findings, despite the first clinical trial (18 March) showing that Kaletra didn't offer any improvements over standard treatments.

Many of the patients in that trial had already been infected for some time, with severe symptoms, so the impact of Kaletra in mild patients is still unknown. It was disappointing that the drug seemed to fail against more severe cases of the virus.

On 18 March the World Health Organisation (WHO) launched the solidarity trial, which is a multinational project to gather data on several different therapies to provide a reliable body of evidence for all scientists to draw upon.



WHAT IS A VACCINE AND HOW DOES IT WORK?

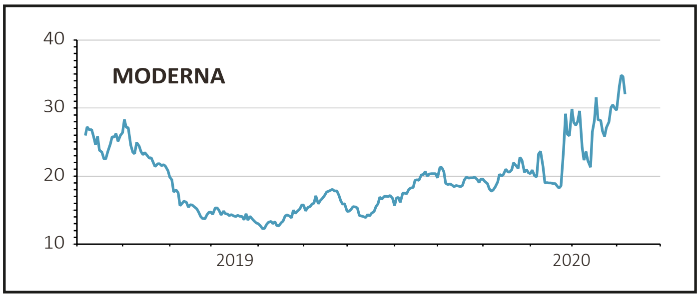
Evidence exists that the Chinese employed smallpox inoculation (or variolation, as it was then called) as early as 1000 AD. It was practiced in Africa and Turkey, before spreading to Europe and the Americas.

Edward Jenner developed the first modern vaccine in 1796 against smallpox. His method underwent medical and technological changes over the next 200 years, and eventually resulted in the eradication of smallpox.

Virologists take a sample of the virus and deactivate it by removing the proteins that would result in the virus multiplying within the human body. By introducing a 'neutered' version to the human immune system, the body is primed to recognise the virus in the future and produce antibodies to keep the invaders at bay.

LEADING THE PACK IN SEARCH OF A VACCINE

Barker believes one of the best prospects of finding a vaccine is an alternative technology being developed by US group **Moderna Therapeutics.** The technology is called mRNA and the idea here is to create a set of instructions that the body can use to makes copies of the vaccine itself.



Essentially, this means the company doesn't have to spend time growing viral proteins, potentially a huge advantage when it comes to building manufacturing capacity. However, this technology requires injecting the mRNA sequence into the correct cells, a non-trivial task and is not commercial as yet.

Plans for phase two trials are underway which will see volunteers receive two doses of the vaccine and then followed for up to one year. The company is preparing for a ramp-up of manufacturing capacity in the event of the vaccine proving successful.

A UK company which is also relevant to the search for a vaccine is pharmaceutical giant **GlaxoSmithKline (GSK)**. It is one of the biggest vaccine producers in the world, producing and distributing 1.9m vaccines every day to over 80 countries.

GlaxoSmithKline recently purchased (6 April) a $200m equity stake in US biotechnology firm **Vir Biotechnology**, paying a 30% premium to the market price.

The two firms are collaborating to find a vaccine by combining Vir's antibody technology platform with GlaxoSmithKline's expertise in genomics.

GlaxoSmithKline is also collaborating with **Sanofi** to find a vaccine.

OTHER TREATMENTS

Preventing hospitalisation and shortening the length of stay is very valuable in the context of limited resources, as well as easing suffering for patients.

Synairgen is conducting a trial on coronavirus patients with its drug, SNG001, which the WHO identified as the only therapy capable of being delivered with an inhaler.

The drug has been shown to accelerate lung function recovery in patients with a cold or flu infection. This also opens up the possibility of using the drug at home for milder symptoms and relieving pressure on hospitals.

In a similar vein, **Tiziana Life Sciences (TILS:AIM)** announced it has developed a new technology to treat the virus, consisting of the direct delivery of its TZLS-501 antibody into the lungs, using an inhaler. The device will work with other approved drugs, giving it a wider application.

The company is trialing a novel molecule aimed at certain patients with coronavirus who develop an uncontrolled immune response resulting in severe lung damage and possible respiratory failure.

Shares in medical diagnostics company **Omega (ODX:AIM)** surged 77% on 9 April after it became part of the UK Rapid Test Consortium to jointly develop and manufacture a COVID-19 antibody test.

Omega's test kits look similar to pregnancy testing strips but a blood sample is required in place of urine.

The antibody test will allow individuals who were previously ill with the virus, but never tested, to potentially go back to work with the knowledge they had built up immunity.

Research company **Ergomed (ERGO:AIM)** has been conducting a trial sponsored by the Papa Giovanni XXIII Hospital in Bergamo, Italy, one of the worst affected areas. The study is testing the drug siltuximab for the treatment of patients with the virus who have developed serious respiratory complications.

Another drug that some people were touting as a treatment, including Donald Trump, is Hydroxychloroquine, used to prevent malaria. It showed promising results in one small study in France, but its methodology has been challenged. In another small trial in China, the drug was no more effective than conventional care.

SAFETY MORE IMPORTANT THAN SPEED TO MARKET

Governments and people alike are keen to fast-track trials and get things moving, but exposing healthy individuals to a potential vaccine increases the risks compared with a situation where sick people are given experimental drugs.

For instance, there have been examples of candidate vaccines which actually make acquiring the infection easier, such as Merck's HIV vaccine study.

This emphasises the importance of doing good science, and making decisions based on robust evidence while giving companies the time they need to ensure any future vaccine for coronavirus is safe to use. After all, the number of people requiring the vaccine is likely to be very large.

HOW HAS THE VIRUS SPREAD SO QUICKLY?

Coronavirus can only spread by human contact, as far as scientists currently believe, and on average the typical infected person passes it on to between two and three other individuals. This means that the growth rate takes on a so-called exponential curve.

Exponential simply means that the starting base rate doubles each time, and the more often it doubles the steeper the curve.

For example, if the epidemic doubles every day, and one person is infected on day one, then on the eleventh day there are 1,024 infected. (The sequence is 2, 4, 8, 16, 32, 64, 128, 256, 512 and 1,024)

You might have heard the term 'super-spreaders' in the news – this refers to a person who spreads infection to significantly more people than usual. It is believed that one in five people in the population are responsible for 80% of transmissions.

There are two possible theories, the first being that some people shed large amounts of the virus, due them being sicker and therefore they are more likely to pass it on.

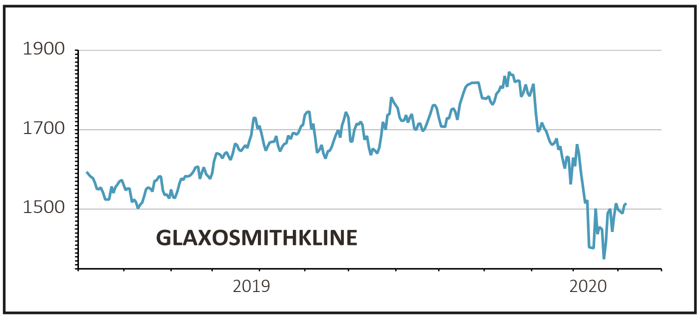
An alternative theory is that super-spreaders don't show any systems and therefore don't know they have the virus.

In the 1995 Ebola outbreak, two people were thought to have infected around 50 others while during the SARS epidemic, there were two super-spreaders in Singapore who infected 10 people each.

OUR TOP **LARGE** CAP STOCK TO BUY

GLAXOSMITHKLINE

GlaxoSmithKline is a great way to play the hunt for a vaccine and to get broader exposure to the healthcare sector. It has a world class vaccine division which, even before the pandemic, was firing on all cylinders.



The vaccines business was the standout performer when the company reported its full-year results on 2 February, showing revenue growth of 19%, aided by the success of its Shingles vaccine, Shingrix where sales more than doubled, while meningitis and influenza vaccines also recorded notable growth.

Revenue from its respiratory business was up 15% driven by demand for its chronic obstructive pulmonary (COPD) drug Trelegy Ellipta and asthma drug Nucala.

Increasing research and development costs, related to the company's push to beef-up its oncology (cancer) franchise and higher promotional costs, restricted 2019 profits, but analysts are pencilling healthy growth for 2020.

GSK and US pharma giant Pfizer are merging their respective consumer healthcare businesses, and plan to spin them off sometime in 2022. The demerged business will generate around $10bn of annual revenues and boast such iconic brands as Panadol, Voltaren, Advil and Viagra.

GSK's pedigree, know-how and collaborations place it at the forefront of vaccine science and it is well positioned to play a key role in the current battle against coronavirus. Indeed, on 14 April GSK said it would partner with Sanofi to develop a coronavirus vaccine.

The candidate vaccine is expected to enter clinical trials in the second half of 2020 and, if successful, to be available in the second half of 2021.

OUR TOP **SMALL** CAP STOCK TO BUY

AVACTA

For investors with more risk appetite, biotherapeutics firm Avacta is also a great way to get exposure to the fast developing testing market for coronavirus.

"Avacta's rapid testing strip might prove to be a game changer"

The sheer numbers (billions) of people that will ultimately need to be tested for coronavirus means that the current lab-testing approach with its two to three day turnaround is not ideal.

That is why Avacta's rapid testing strip, which can be used at home with no medical knowledge, and which will give a result within minutes, might prove to be a game changer in tackling the current pandemic.

The company owns all the intellectual property and commercial rights to the technology, but has not yet disclosed any further details.

PLANNING FOR YOUR ISA? GO THE WHOLE 'HOG

From Roman times onwards, hedgehogs have held a special place in our culture. Back then, Pliny the Elder, a renowned philosopher of that day, wrote about hedgehogs carrying apples on their spines, to sustain them through the winter months. Folk tales also cast hedgehogs in an idealised light. But these romanticised images bely their resilience and self-preservation. When a predator approaches, the hedgehog presents its spines (more than 5000 of them!), making a formidable shield.

Somewhat similar to this clever creature, investors also think about self-preservation – in order to achieve one's financial goals, and to ensure enough is put aside for the long-term. This ISA season, you might be considering something different to the most popular but often overcrowded themes of the stockmarket – so here's a round-up of our contrarian investment approach.

Built for long-term investing
The Scottish has a history of long-term investing. It boasts over 130 years as an established investment vehicle and importantly, as an independent trust, it is not constricted by short-term performance considerations.

Thinking differently
The Trust's contrarian approach is built on conviction, a search for out of favour but quality investments and an awareness of investors' behavioural traits. It is never just a case of rounding up the most unloved stocks. There have to be inherent strengths as well as potential catalysts for sentiment and share prices to recover.

A Dividend Hero
Over time, dividends make up a substantial portion of total returns. The Scottish has 36 consecutive years of increased regular dividends and currently one of the highest dividend yields in its peer group. The compounding effect of these dividends, when reinvested into the fund, is material and boosts returns over time. The Trust has been listed as a 'Dividend Hero' by the Association of Investment Companies. It should be remembered, however, that dividends are not guaranteed and income can fall as well as rise.

> " This ISA season, you might be considering something different to the most popular but often overcrowded themes of the stockmarket "

Low costs
The Scottish's ongoing charges figure (OCF) is low relative to its peer group, an important consideration given the drag that high fees can have on overall returns.

ISA: a tax-efficient way to invest
The current ISA proposition stands out as relatively attractive. The vehicle offers generous tax benefits – when you invest in an ISA you pay no further tax on any income earned or on any gains when you sell your investment. Up to £20,000 can be invested in an ISA for the current tax year which ends on 5 April 2021. ISAs are an attractive vehicle for building a substantial fund to potentially finance school fees or a deposit for a flat. Though remember that the value of any tax benefits depends on your individual circumstances and tax rules may change in the future. ■

9 April 2020

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RUSS MOULD
AJ Bell Investment Director

Why the dollar is in demand

The story behind the rise in the US currency and what it means for the markets

Whatever your opinion of Donald Trump, you always know what the US president is thinking and he could not be clearer on the dollar: he does not like a strong greenback.

This is odd, because a strong currency is usually a sign of economic strength in absolute or at least relative to international peers and rivals, but the president does not want a bouncy buck and his administration has done its best to talk down the greenback.

It even worked for a while, although a sequence of interest rate hikes from the US Federal Reserve in 2018 and America's superior economic growth record meant that economics trumped talk, if you will pardon the expression.

Then along comes the coronavirus crisis and that gives the dollar another boost. All of a sudden, investors are looking for haven assets and that generally tends to mean the world's reserve currency. As a result, the trade-weighted DXY dollar index (known fondly as 'Dixie' by traders around the globe) stands back over 100 for the first time since spring 2017, just after Trump's November 2016 election win.

DOLLAR IS ON THE RISE ONCE MORE

Source: Refinitiv

DOLLAR DYNAMICS

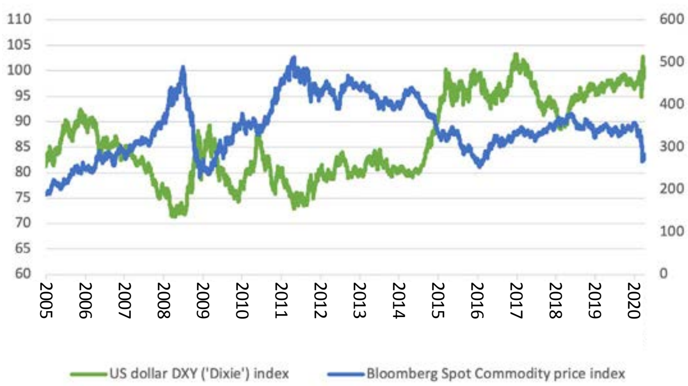
Dollar strength can therefore be a sign of concern for investors, not just presidents who fear it harms exports, as it is suggestive of fear, if not distress.

In this respect, the good news at least is that the DXY index is nowhere near the 120 level seen in 2002.

However, there are two more tangible reasons for looking at a strong dollar with some concern.

First, a rising greenback is not good for commodity demand. All major raw materials, except cocoa (which is traded in sterling) are priced in dollars, so if the US currency rises then that makes them more expensive to buy for those nations whose currency is not the dollar or is not pegged to it. Note how there seems to an inverse relationship between 'Dixie' and the Bloomberg Commodity Price index.

DOLLAR IS TRADITIONALLY SEEN AS NEGATIVE FOR COMMODITY PRICES



Source: Refinitiv

RUSS MOULD
AJ Bell Investment Director

Second, emerging equity markets do not appear to like a strong dollar either, judging by the inverse relationship which seems to exist between the DXY and MSCI Emerging Markets (EM) benchmarks.

Dollar strength at the very least coincided with major swoons in EM, or at least periods of marked underperformance relative to developed markets, during 1995-2000 and 2012-15. Retreats in the greenback, by contrast, appeared to give impetus to emerging equity arenas in 2003-07, 2009-12 and 2017-18.

EMERGING MARKETS ARE ALSO TRADITIONALLY WARY OF A BOUNCY BUCK

Source: Refinitiv

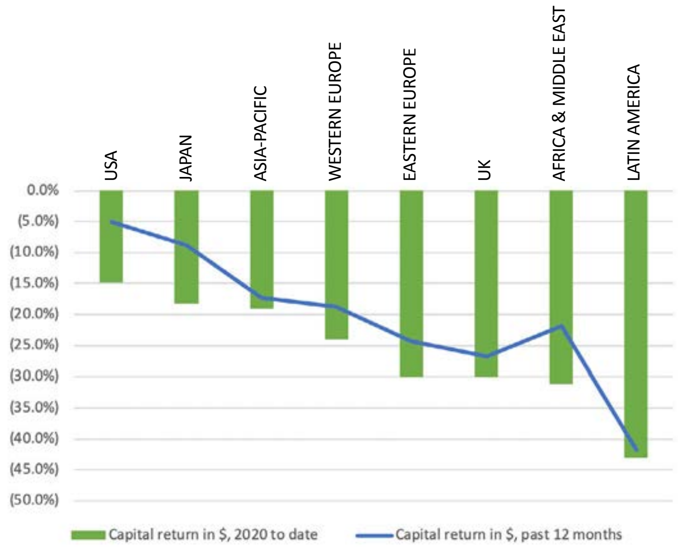
This also makes sense, in that many emerging (and frontier) nations borrow in dollars and weakness in their currency relative to the American one makes it more expensive to pay the coupons and eventually repay the original loans.

Zambia and Ecuador are already looking to restructure dollar debts while Argentina is still grappling with its $83bn in foreign liabilities. The higher the buck, the more uncomfortable those debts become as interest payments suck away cash that could otherwise be used for investment.

EYE OF THE TIGER

However, there is one trend within emerging markets that is worth noting, which is how Asia is doing markedly better than Latin America, Eastern Europe and the Africa/Middle East region. Over the past year, in dollar terms, Asian stock markets have beaten all other emerging arenas and trailed only the US and Japan.

ASIA HAS DONE RELATIVELY WELL OVER THE PAST YEAR



Source: Refinitiv

Admittedly, all Asia has done is go down less than everywhere else and many investors will take cold comfort at best from relative outperformance – they cannot pay bills with smaller losses, only income and actual profits.

It will be interesting to see if Asia can keep it up as and when global economic activity and risk appetite pick up again. Perhaps its outperformance reflects nothing more than a view that the region was first in and first out when it comes to the viral outbreak.

Perhaps it is due to the region's much lower reliance on commodity prices, relative to Eastern Europe (where Russia dominates) and Latin America. But, given the experience of SARS in 2002-03, Asia may have been better prepared and equipped to deal with such a situation and it may be that such readiness will serve the region – and investors in it – well over the longer term, too.

Don't turn your back on small caps as markets fall

They may be more volatile but the potential returns can justify higher risk, say fund managers

As the UK continues to step lightly through the coronavirus pandemic's social distancing minefield, many investors have turned their back on the small cap space. This is a mistake.

We can understand why small caps might not appeal to everyone at the moment, given this space can include unproven business models and fragile balance sheets. It can also be harder to sell small cap shares when you want compared to larger companies.

However, successful stock pickers have managed to reduce portfolio losses this year by having stakes in more resilient small cap businesses.

Data shows parts of the small cap space are holding up relatively well versus the broader UK stock market, as defined by the FTSE All-Share index which is down 23% year-to-date. Twenty one UK small cap equity funds and investment trusts have this year fallen by less the FTSE All-Share, out of a total universe of 75 funds.

The best performer is **Miton Smaller Companies Fund (B8JWZP2)** whose shares have are down 12.3% between 1 January and 9 April 2020. Other strong performers, on a relative basis, include **Octopus UK Micro Cap Growth (BYQ7HP6)**, down 13.3%; and **Liontrust UK Smaller Companies (B57TMD1)**, down 17.3%.

Nonetheless, it is important to take a balanced view by pointing out that parts of the small cap market have been terrible places to be invested. Just look at how investment fund **Crystal Amber (CRS:AIM)** has seen its share price nearly halve (-48.1%) year-to-date, and **Aberforth Split Level Income Trust (ASIT)** is down 43.7%.

WHAT TO DO NOW

'(The current market level offers) a really interesting buying opportunity,' says Jonathan Brown, who runs the **Invesco Perpetual UK Smaller Companies (IPU)** investment trust. 'There's been quite a few companies we've been waiting for a suitable entry point that are finally looking cheaper now.'

Interestingly, fellow asset manager River & Mercantile last week lifted its ban on new investment into its **River & Mercantile UK Smaller Companies Fund (B1DSZR9)** after bolting the door to new investors in 2015.

Investing in smaller companies can bring a sense of excitement, particularly as a contract win or technological breakthrough can have a large impact on earnings or company valuation. However, this is a higher risk part of the

BEST PERFORMING SMALL CAP UK EQUITY FUNDS THIS YEAR

Miton UK Small Companies	-12.3%
Octopus UK Micro Cap Growth	-13.3%
Liontrust UK Smaller Companies	-17.3%
R&M UK Equity Small Companies	-17.6%
Oryx International Growth	-18.0%
MFM Techinvest Special Situations	-18.8%
Liontrust UK Micro Cap	-19.2%
Gresham House UK Micro Cap	-19.4%
Athelney Trust	-19.7%
Odyssean Investment Trust	-19.8%
FTSE All-Share	**-23.0%**

Source: FE Fundinfo. IA & AIC UK Small Caps Equity sectors. Data 1 Jan to 9 April 2020.

investment market as setbacks can and do occur.

Investors should only allocate a small part of their portfolio to this space, and perhaps not at all if you cannot stomach large moves up and down in the share price.

For those happy to proceed, and fully understanding the risks, there are still a few things to note before you consider putting any money into the small cap space at the moment.

Watch for potential supply chain disruption, says Dan Whitestone, who runs the **BlackRock Throgmorton Trust (THRG)**. This could have one of the biggest impacts on smaller companies unable to procure the components they need to keep their businesses running.

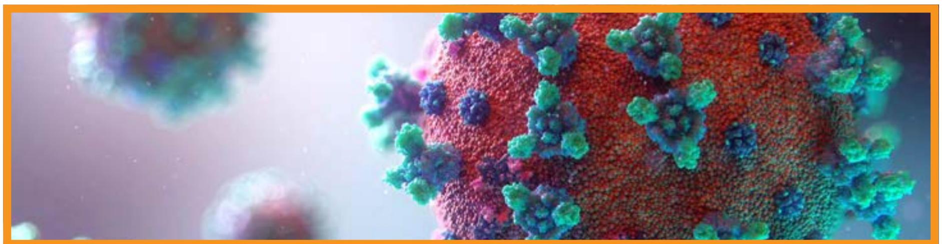
Debt is also an issue for smaller companies, says Whitestone, particularly those that may need to refinance existing borrowings.

'If you've got a lot of debt, you've got a massive problem because you may not have any earnings, you may not have any revenues, you may not have any other things, you may have a massive fixed cost base,' Whitestone explains. He adds that smaller companies can become 'totally exposed, and they may not survive'.

Highly indebted firms might be experiencing a share price rally at the moment, but that doesn't mean the rally is sustainable. These companies still need to resolve their debt problems which is unlikely to be an easy task.

THE NUMIS SMALLER Companies index (excluding investment trusts) has delivered annualised returns of almost twice that of the FTSE All-Share index between 1955 and 2018.

It has also smashed the performance of both long and short-dated government bonds, and massively outstripped UK property prices, according to data compiled by the *Financial Times*.



BEST PERFORMING SMALL CAPS THIS YEAR

Novacyt	2800%
Synairgen	857%
Byotrol	270%
e-Therapeutics	261%
Dev Clever	204%
Starvest	193%
Greatland Gold	189%
All Active Asset Capital	181%
Tekcapital	171%
Avacta	132%

Source: SharePad. Market cap <£500m. Data 1 Jan to 9 April 2020

INVESTMENT IDEAS

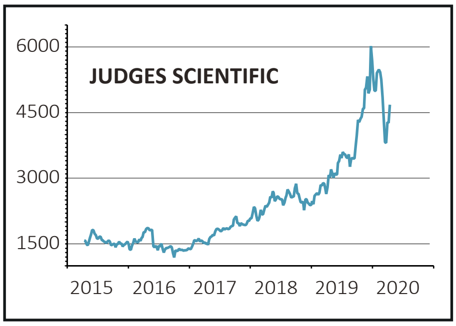
Arguably, investors would be better off focusing on higher quality businesses rather than buying whatever small caps are currently rebounding following the market sell-off.

Jeff Harris, co-manager of the **Strategic Equity Capital (SEC)**, says attractive qualities include strong cash flows, repeatable revenues, limited exposure to economic cycles and strong financial positions, citing the examples of **Alliance Pharma (APH:AIM)**, **Medica (MGP)**, **XPS Pensions (XPS)** and **Ergomed (ERGO:AIM)**.

If you want to get exposure to small caps via funds, we suggest you look at **Franklin UK Smaller Companies (B7FFF70)** and **Tellworth UK Smaller Companies (BDTM8B4)**, both of which are on AJ Bell's 'favourite funds' list.

Otherwise, we now offer three stock ideas involving attractive businesses with the right qualities to prosper longer-term. There may be a few bumps along the way, but we're happy to buy at the current price and be patient.

JUDGES SCIENTIFIC (JDG:AIM) £46.40 BUY

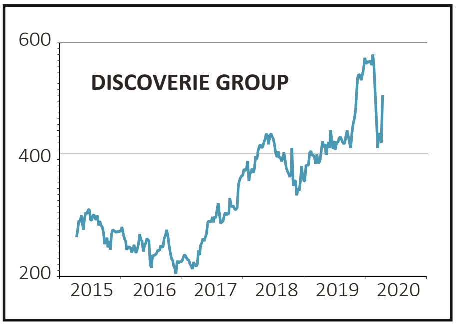


Judges Scientific has a proven model of expansion, profit growth and value creation from running a portfolio of niche science-based businesses spanning nanotechnology, fibre optic testing, advanced materials, LED design and x-ray technology.

It boasts consistent mid to high single-digit organic growth and impressive 21% operating margins with scope to expand. It throws off plenty of cash and its dividend is covered up to five times by earnings.

On 18 March it said the effect on current year trading performance would be limited if the coronavirus outbreak only lasts a further two months, but would have a progressively growing and more significant impact thereafter. However, it did add: 'It is currently expected that the impact on the group will only be temporary and, that with its robust financial position, the group's ability to conduct its business model will remain intact.'

DISCOVERIE (DSCV) 495P BUY

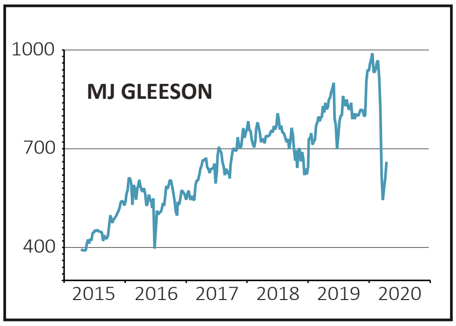


This electronics engineer has been doing a cracking job climbing the value chain in structurally growing markets where equipment specifications are high-performance, reliability, efficiency and regulations-driven.

Think medical, aerospace, transport and renewables where it designs and makes blade controls for wind turbines and AI-based telematics and connectivity components.

The company boasts strong cash flow and a balance sheet with over £100m of headroom against its debt facilities.

MJ GLEESON (GLE) 670P BUY



The housebuilder stands out from others in the sector because of its focus on the 'affordable' end of the market, where demand is most intense for new homes. Its starter two, three and four bedroom homes start at £90,000.

Gleeson recently raised £16.4m by issuing new shares for cash which puts it in a stronger position to get through the coronavirus crisis and get back to work as soon as possible.

'Gleeson's customers should be the least likely to cancel and the fastest to return,' says investment bank Liberum. '84% of customers are first-time buyers and 60% key and essential workers.

'The group has excellent liquidity, and can now withstand 23 months of zero revenues.'

DISCLAIMER: Editor Daniel Coatsworth has a personal investment in Tellworth UK Smaller Companies referenced in this article.

By **Steven Frazer**
News Editor

The thematic funds that stay one step ahead of the crowd

Lazard is confident on the themes that will shape the world over the next decade

Many investors are jumping on investment themes too late to make good money, or they are misunderstanding how you might profit from a theme. Steve Wreford, a portfolio manager at Lazard Asset Management, calls it a narrative fallacy.

'You often hear fantastic stories about something that will happen but which is barely related to underlying investment returns.

'Robotics is a good example. Yes, robots are going to be everywhere in the next 10 years. But does that mean an investor should buy a robotics ETF or themed fund filled with robot manufacturers?

'If robots are going to be everywhere it's because they are going to become inexpensive. If prices are going to collapse, why do you want to own the companies that make them? It doesn't make any sense.'

Wreford is part of the team running thematic funds at Lazard, who he believes are one step ahead in identifying not only the opportunities but also where the best money will be made.

Lazard takes a view on how the world will develop over the next decade. It then groups together insights about structural and secular change to form themes. Importantly, these themes evolve, they can be removed for valuation reasons, they may lose relevance or they are replaced by new ideas.

WAYS TO PLAY

Investors can tap into its strategy via two funds. The first is **Lazard**

LAZARD GLOBAL THEMATIC'S INVESTMENT APPROACH

THEME	DESCRIPTION	EXAMPLE PORTFOLIO HOLDINGS
ASSET EFFICIENCY	Harvesting efficiency gains from the Internet of Things	Rockwell Automation, Assa Abloy
BITS OF CHIPS	Key components capturing the value from digital transformation	ASML, Texas Instruments
DATA, NETWORKS AND PROFITS	Where artificial intelligence meets data privacy	RELX, Visa
DIGITAL RUNWAY	The emerging markets fintech and financial inclusion opportunity	ICICI, Prudential
DISTRIBUTION FOOTPRINTS	Companies that won't be killed by Amazon	Compass, Rentokil
EMPOWERED CONSUMER	Best consumer growth companies share common characteristics	L'Oreal, Walt Disney
ENDURING BRANDS	Steady growth and intangible value	Coca Cola, Johnson & Johnson
ENERGY TRANSITIONS	Diversification and opportunities from the shift to clean energy	BP, Iberdrola
EXTREME RISKS	Extreme monetary policy may have consequences	Bank of Amerca, Barrick Gold
FIRST WORLD HEALTH	Lowering costs and improving access to healthcare	Boston Scientific, Stryker
SOFTWARE AS A STANDARD	The new standards automating white collar jobs	Adobe Systems, ANSYS

Source: Lazard

Global Thematic (B464177) which generally has eight to 12 themes, each of which is populated with eight to 10 stocks worth $1bn or more and equally weighted. Wreford says this is popular with more cautious investors.

The six ideas from this group offering the strongest potential returns are used to populate **Lazard Global Thematic Focus (BKX9F08)**, essentially a best ideas sister fund.

'Our themes appear well placed as we emerge from the coronavirus pandemic. In the past few weeks we've been able to purchase shares in some of the best companies in the world for these themes, and at discounted valuations to historical standards.'

FOCUS ON THE LONG-TERM

The portfolio manager says conversations with company directors focus on the future not the present. 'We aren't asking how business is today; we're asking what will be the biggest structural change in your industry over the next three to 10 years.'

This process led to defining one of the themes in the funds' portfolios called automated efficiencies.

Imagine there are 100 robots in a factory but one is twice as efficient as the others. Today all the robots might stream data back, the team look at it and try to work out how to improve efficiency, which is a slow process.

'What you really want is for that robot to share automatically what it is doing differently with all the other robots so overnight raise the returns of the other 99 robots in the factory. Your efficiencies ought to be generated without any human involvement. That will be called a "dark factory" – no humans in it,' explains the portfolio manager.

'We know this will be real because companies are investing billions of dollars to make it happen. We have very high conviction that this is a genuine theme.'

SEEKING BROAD OPPORTUNITIES

Having established this theme, the next step for the team is to identify the companies best placed to profit. Lazard analysed previous trends across multiple sectors and realised it could learn a lesson from how the smart phone sector developed.

While you might have thought handset, battery or screen makers were the best places to invest to play the smart phone theme, the correct answer would have been investing in the companies responsible for the operating systems – namely the global duopoly that is Google (Android) and Apple (iOS).

'That's why we are looking for the operating systems that will join those robots together in the factory – and we know who the makers are.'

They include Rockwell Automation and Fanuc. 'Shares in Fanuc have been under pressure because they've spent the last three years investing heavily. Short term investors don't like it when companies invest a lot, yet Fanuc are building an operating system as I've described, called the Field System.'

To get the most from a theme, Lazard's analysts search for as many different industries as possible which could embrace it. For example, tractor maker John Deere wants its agricultural equipment to talk to each other on its own operating system.

John Deere wants to link its equipment via its own operating system

In the property space, Johnson Controls is flagged as an important player in this theme. 'It goes to a building owner and says "if you allow us to put in our operating system we will guarantee you 20% off your energy bill over the next 20 years". All the buildings on that system talk to each other and learn how to run more efficiently.'

CONSUMERS AND FINTECH

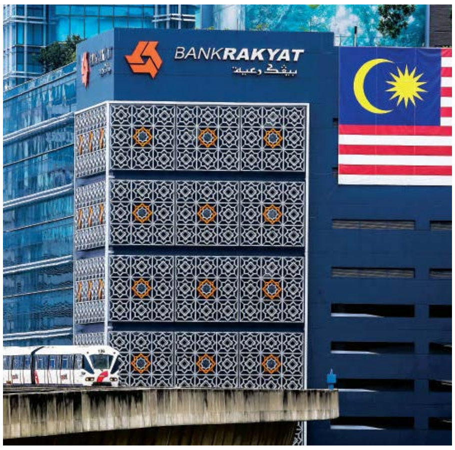
Other themes in the funds include the empowered consumer where Lazard believes there are common characteristics for businesses to be a winner for consumers in 2030.

They will need to be aligned with consumers' ethical values, have a digital relationship with each customer, and both make and sell a product. Stocks aligned to this theme in its portfolio include electronics giant Sony and video games specialist Activision Blizzard.

The digital runway theme focuses on the fintech opportunities in emerging markets. Wreford says there is a large unbanked population in places such as Indonesia who are 'crying out' for new financial services.

'Companies addressing this market can leapfrog over the technology and processes used in the West. No-one will build a bank branch.

'We invest in Bank Rakyat which has guys with iPads, travelling in speed boats to different places in Indonesia. They recruit grocery stores to be agents and they've bought a satellite which means they have their own infrastructure to connect everyone, thereby building a banking network.'



LOOKING BEYOND THE OBVIOUS

A lot of people talk about certain attributes which makes companies special such as ones that benefit from network effects – the more people use their services, the richer the environment to make money. Ebay being one example of this in action.

The Lazard portfolio manager says the benefits of these traits are already priced in by the market, which is why it is important to look further into the future to spot ways to profit from certain themes. Other examples of themes already factored into share prices include internet of things, digitisation, consumer behavioural shifts, moving software services to the cloud, and disruptive technologies.

Just take the theme of data – everyone now seems fully aware that companies with access to lots of data can use it to learn about customers. The big concern is whether this data is being used in a good or bad way and how that shapes prospects for companies.

'We want to benefit from data-orientated companies with networks but also avoid upcoming regulation of these companies that could crush their business models. For example, we believe Facebook will ultimately be responsible for the underlying content and so will be valued (much less) as a publisher and not a tech platform,' explains Wreford.

He says businesses such as Wolters Kluwer are more interesting when it comes to the theme of data, networks and artificial intelligence (AI). 'The legal profession uses its databases. Rather than spending a week looking for the right case study to support a legal case, let Wolters' AI do it within an hour.'

PAST AND FUTURE

Lazard Global Thematic Fund has delivered 15.7% total return over the past five years versus 10.8% from the Investment Association global sector, according to FE Fundinfo. The Focus version of the Lazard fund only recently launched so there isn't enough data to judge its performance.

'Coronavirus represents a catalyst that is revealing underlying conditions that have been bubbling under the surface for a while and accelerating changes we've been anticipating,' says Wreford.

'Politics will play a greater role in markets after the crisis in terms of how money is allocated. Most of our themes and companies are long-term beneficiaries of current events.'

By **Daniel Coatsworth**
Editor

Socially responsible investing: a stricter form of ESG

Why looking for ETFs and funds with the 'SRI' tag could help you find a more focused investment than just a regular ESG fund

If you want your money to be invested in a morally correct way, looking at funds with the 'socially responsible investing' (SRI) tag may be a way to do it.

SRI is an attempt by those in the fund management world to apply a stricter and more focused style of ESG (environmental, social and governance) to investing.

According to SRI criteria set by index provider MSCI, and widely followed by most in the SRI world, stocks are first screened through an exclusion list, with zero tolerance for companies with ties to controversial weapons.

There is minimal tolerance (less than 5% of revenue) for companies with links to nuclear weapons, civilian firearms and tobacco, and low tolerance (no more than 15% of revenue) for alcohol, adult entertainment, conventional weapons, gambling, genetically-modified organisms and nuclear power. It also excludes companies deriving 30% or more of their revenue from thermal coal.

Once stocks have been filtered through the list, they're all given an ESG rating and ESG controversies score (measuring their exposure to

ESG controversies and negative events reflected in global media).

The top 25% of this remaining list in each sector and region (to avoid any bias) are included in MSCI's SRI indices.

Taking the MSCI World SRI index as an example, the number of constituents is whittled down to just 386, compared to 1,643 for the MSCI World index.

APPLIES TO DIFFERENT ASSET CLASSES

This criteria is mostly used for stocks, but is also applied for corporate bonds, SRI funds and ETFs (exchange-traded funds).

While SRI investing attracted €733bn in the first eight months of 2019 according to asset manager Amundi, up from €621bn in the whole of 2018, it is still a nascent area of investing.

Until it becomes clearer what tangible difference active management can provide with SRI, it may be better to stick with passive options, particularly given the sizeable difference in cost between some active funds and passive exchange-traded funds (ETFs).

A study by two economists at St Andrews University, Jimmy Chen and Bert Scholtens, looked at the performance, cost and how actively managed SRI funds are in the US, a market that's always been a few years ahead of the rest of the world when it comes to financial innovations.

They found that only active specialist thematic socially-responsible investment funds appeared to generate risk-adjusted returns that overcome their expense ratios.

Furthermore, they found that some active SRI funds seem to operate as 'closet indexers' with a low degree of active management.

WHERE TO START

When choosing the passive route, knowing where to begin can be difficult. Even though SRI is a subset of ESG, there's still a proliferation of options out there and it's hard to tell if they're any good or actually stick to their principles.

The best way to look at SRI, according to Vanguard's head of product specialism Mark Fitzgerald, is about mitigating risk.

'There's no dictionary definition,' he explains. 'SRI tends to be, take out companies that are doing things that are truly abhorrent. You could say it's about mitigating risk such as "don't expose me to those companies, please".

'It has an exclusionary approach, whereas ESG tends to be more than just mitigating risk, it's more forward-looking.'

CHOICE OF INDEX

While this exclusionary approach can be helpful for investors as it can create a clearer picture

> **"The best way for investors to approach this area is to know what they're trying to achieve"**

of what they're investing in, a look at the top 10 holdings of many SRI index funds and ETFs shows that, because the indices themselves are market cap weighted, you will still get exposure to oil and gas companies such as **Royal Dutch Shell (RDSB)** and **BP (BP.)**.

That's also why companies like BlackRock for example have switched their iShares SRI range to track MSCI SRI Select Reduced Fossil Fuel indices instead of the straight MSCI SRI ones.

In addition, it's important to note that SRI is different to the likes of impact investing, which seeks out companies making most of their money from specifically addressing one of the world's major social or environmental challenges as identified by the UN.

Impact funds tend to be mostly active and tend to have significantly higher fees.

With SRI funds and ETFs, your top holdings are likely to include Microsoft, Proctor & Gamble and Walt Disney, firms which it's hard to argue are doing anything particularly bad in the world, but don't exactly spring to mind when you think of ethical companies.

WHAT ARE YOU TRYING TO ACHIEVE?

Fitzgerald says the best way for investors to approach this area is to know what they're trying to achieve.

Once they know what they do and do not want to invest in, picking the right SRI ETF or fund will require some digging and looking at fund factsheets, but it will help narrow their focus and ensure they end up with an investment that fits their values.

Fitzgerald adds that for those looking to go down the active route, it's important not to lose sight of the benefits of diversification.

'The more green you go and the more focused your investment becomes, you could be invested in just a handful of companies and your returns could become very different. It's always important to keep in mind the diversification benefit.'

By **Yoosof Farah**
Reporter

Why can't I transfer my defined benefit pension?

Our expert answers a frustrated investor's retirement query

I am considering transferring my defined benefit (DB) pension to a SIPP. I am a keen private investor, with a sizeable portfolio, which I've managed for many years.

I am being stymied at every turn. If an IFA provides a transfer suitability report to say that it is right for me to transfer then they say they have to manage the money due to professional indemnity considerations. I want to manage my own money but am not being allowed to.
Nicola

Tom Selby
AJ Bell
Senior Analyst says:

With the exception of unfunded public sector schemes, people with defined benefit (DB) pensions are allowed to transfer to defined contribution (DC) plans such as SIPPs.

However, there are restrictions in place and market dynamics which mean it might not be straightforward to do so.

Firstly, anyone with a DB pension worth £30,000 or more must take regulated financial advice (and give the scheme proof of having received that advice) before going ahead with a transfer. This requirement was put in place for a number of reasons, including:

- DB pensions are extremely valuable, providing a secure, increasing benefit throughout your retirement;

- moving from DB to DC involves a transfer of retirement risks, from the employer to you;

- managing your pension in DC requires active engagement from you, while DB does not;

- in DC you will have to pay costs to administer and invest your retirement pot (although these can be very low);

- once you leave your DB scheme there is no going back.

Receiving regulated advice is designed to ensure you understand these risks before you make your decision. It's worth noting you don't have to follow the advice, although some providers will only accept transfers with a positive recommendation.

Secondly, as you have experienced, some advisers may only be willing to carry out a DB transfer if they can continue to manage your fund afterwards. Many firms cite fears over future claims against them if they don't look after both the transfer and the investment of funds post-transfer.

While I understand this might be frustrating this is simply the reality of the current situation.

WHY THE CORONAVIRUS COULD LEAD TO FURTHER TRANSFER DELAYS

The coronavirus pandemic may also lead to delays in DB transfers. The Pensions Regulator, which polices DB schemes, has announced trustees – whose job it is to look after the interests of members – can suspend cash equivalent transfer value (CETV) activity for up to at least three months if it is deemed in the best interests of members.

You may also find DB to DC transfers are a bit slower than normal, with all providers having to adapt processes in order to comply with social distancing rules.

DO YOU HAVE A QUESTION ON RETIREMENT ISSUES?

Send an email to **editorial@sharesmagazine.co.uk** with the words 'Retirement question' in the subject line. We'll do our best to respond in a future edition of *Shares*.

Please note, we only provide guidance and we do not provide financial advice. If you're unsure please consult a suitably qualified financial adviser. We cannot comment on individual investment portfolios.

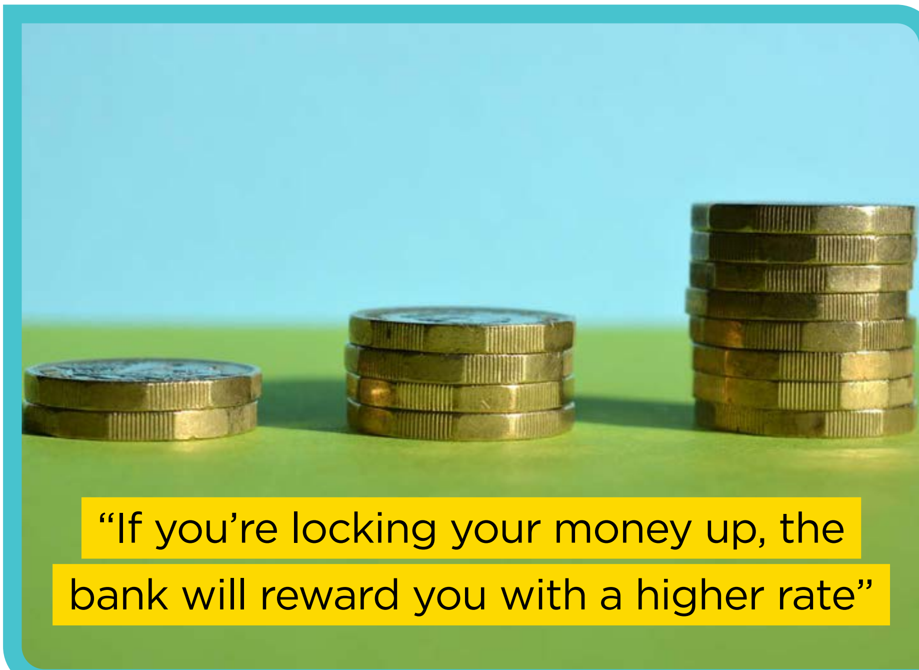
Where can you get the best rates on cash savings?

Cash is increasingly important to individuals amid fears about the stock market and a likely recession

Demand is increasing for cash savings accounts as more people become fearful about investment markets. People are also worried about tough financial times ahead and are building up their emergency cash pots in case they need to dip into them in the future.

While it might not seem worthwhile to switch your cash account, it's often easy to do and if you're earning a very low interest rate or have a large amount of savings – or both – then it can really pay off.

For example, someone with £5,000 and earning just 0.1% interest will earn a measly £5 a year in interest. But if they move this to an account paying 1.5% they'll make £75 a year in interest, for very little effort. Say someone has £50,000 the figures grow tenfold – so you go from earning £50 a year to £750 a year.



I WANT EASY ACCESS

The sacrifice you make for being able to withdraw your money whenever you want is that you'll usually get a lower interest rate. If you're locking your money up, the bank will reward you with a higher rate. Sadly no easy access account currently pays more than the current 1.7% rate of inflation.

The top-paying truly easy access account is from Marcus by Goldman Sachs, which pays 1.3% on up to £250,000. Virgin Money pays slightly more at 1.31% but only allows two withdrawals a year, so is unlikely to be worth the minuscule increase in interest. Saga also offers an account paying 1.3%, and is actually run by Marcus just with the Saga branding on it.

If you want an account that you can open inside a branch or via post your best bet is likely to be NS&I's income bonds, which pay the next highest interest rate, according to Moneyfacts, at 1.15% on sums between £500 and £1m. This rate is only valid to the end of April, when it falls to 0.7%.

I'M HAPPY LOCKING MY MONEY AWAY FOR A WHILE

If you're willing to tie your cash up and don't need immediate access to it, you can earn a bit more money. The trade-off is that you're locking in that interest rate for however long you sign up for, meaning you believe interest rates aren't going to rise during that time.

For a one-year fixed rate you can get 1.6% with BLME, where the accounts are run under Islamic finance rules so what you get is an expected rate of return rather than a guaranteed rate. This rate is also offered by Hampshire Trust Bank and Vanquis Bank.

For a two-year fixed account

the rate jumps to 1.75% with BLME, or increases slightly to 1.65% with Hampshire Trust Bank. The 1.65% rate is also offered by United Trust Bank and Vanquis.

At three years, the top rate increases slightly to 1.8%, which is offered by Investec Bank, Vanquis Bank and United Trust Bank.

Once you jump to five years and beyond the rates increase ever so slightly, with the five-year bonds from Vanquis Bank and United Trust Bank paying 1.85%. At this point you're tying up your money until 2025 and are assuming interest rates won't rise in that time.

I WANT TO SAVE REGULARLY

You can earn more interest if you put money away each month, albeit on smaller sums. Some of these accounts require a current account with the provider and also usually only offer the rate for 12 months, at which point you need to switch.

If you miss a monthly deposit with some providers you lose it and you can't double up the following month – so consider setting up a direct debit or standing order.

The top rate is 2.75% from First Direct, which lets you put in between £25 and £300 a month but you need to have a current account with it or switch to one.

HSBC also pays 2.75% if you have a current account with it, but only on up to £250 a month, and M&S Bank offers the same.

If you don't want to move your current account then Coventry Building Society pays 2.5% on up to £500 a month, while Virgin Money pays 2% on up to £250 saved a month.

The trade-off for the higher interest rates on offer is that your money doesn't get that rate all year, only the first monthly deposit earns the interest for the full 12 months, while the final deposit only earns it for one month, which reduces the total interest you earn over the year.

For example, £250 a month deposited earning 2.75% a year earns you £45.07 in interest over the year, but if that same £3,000 total deposit earned 2.75% over the entire 12 months you'd earn £83.55 interest over the period.

By **Laura Suter**
AJ Bell Personal Finance Analyst

HOW YOUR MONEY IS PROTECTED

The Financial Services Compensation Scheme is in place to protect your money should your bank or building society fail. It will cover up to £85,000 per person with each institution, or £170,000 if the money is in a joint account.

In certain cases you'll be protected up to £1m for up to six months, if you've received a windfall, such as money from the sale of your house or from divorce or redundancy. Check what's eligible here.

Some banks will have different brands but will still be counted as one institution by the FSCS, so check you're not doubling up. You can check if you're covered here.

Everything you need to know about bonds

We look at the world of fixed income and its pros and cons for investors

What are bonds and why investors might want to hold them in their portfolios? Whereas a share is literally just that, a share in the profit generated by a company, a bond is an 'IOU' which companies make to investors.

It typically carries a fixed rate of interest over a fixed period, say five or 10 years, and pays annual or semi-annual 'coupons' or interest payments. Because both these variables are usually fixed, bonds are often described as 'fixed-income' securities.

Once the bond reaches 'maturity' or its expiry date, the company which issued it is obliged to pay back the bondholder their initial investment in full.

HOW IS INTEREST PAID?

Originally, bonds had detachable, individually-numbered coupons which investors would 'clip' and send to the issuer in order to claim their payment. A good example is US railroad bonds issued in the mid-1800s, or the Confederate State bond.

The bond was issued by the Confederate States of America in August 1863 with a face value of $1,000 and a 10-year lifetime, meaning it would be repaid in July 1873.

It carried an 8% rate of annual interest, and every six months the bond holder would clip the coupon and present it at their local bank in exchange for $40 of interest in cash.

When the bond matured in 1873, the bondholder would have expected to receive back their original $1,000 investment, though the defeat of the Confederate states in the American Civil War rendered this academic.

Today, if you own a bond the interest payments are made electronically into your account.

WHAT IS A YIELD?

Unlike shares, which are quoted on the basis of price, bonds tend to be bought and sold on the basis of their 'yield'.

All bonds are issued at 'par', or 100% of their face value and they are also redeemed at face value assuming the issuer doesn't go bust.

If a bond with an interest rate of 5% is trading at 'par', its yield is 5%. If the bond trades below 'par', the interest rate will be more than 5%, and if it trades above 'par' the interest rate will be below 5%. In practice, most bonds trade either above or below 'par' for most of their lives as markets rise and fall.

The last couple of decades has seen more and more investors buy bonds, which has meant that the interest rates companies have paid to issue bonds has been getting smaller and smaller.

It has also meant that yields on bonds have got smaller and smaller as more people compete to buy them, forcing prices up.

WHO CAN ISSUE BONDS?

Companies can issue bonds, and so can governments and non-government organisations (NGOs) like the World Bank.

There is a clear pecking order in bond quality – reflecting the likelihood of getting your money back. Government bonds, known as gilts in the UK or treasuries in the US, have traditionally been seen as the most secure and as such are used to benchmark the bond market.

They are by far the biggest issuers and as long as they borrow in their own currency they should always, in theory at least, be able to print more cash to pay the coupon.

A rough guide to credit quality is provided by ratings agencies such as Standard and Poor's (S&P), Moody's and Fitch. S&P and Fitch both grade bonds in descending order from AAA to AA+, AA, AA-, BBB+ and so on.

Well-known international companies like **GlaxoSmithKline (GSK)** and **Unilever (ULVR)** are seen as likely to pay bondholders back and their bonds typically have quite low interest rates.

Companies which have

THE LONGER THE PERIOD TO MATURITY, THE GREATER THE RETURN ON THE BOND (AT LEAST IN MOST CASES)

poor financial situations, or which already have a lot of debt, typically need to pay much higher interest rates to compensate investors for the risk of buying their bonds.

The longer the period to maturity, the greater the return on the bond (at least in most cases).

This is compensation for the risk posed by the longer holding period. So, UK gilts which pay out after just a month offered a yield of 0.134% at the time of going to press while those with a 20-year term offered a yield of 0.7%. Price volatility also tends to be higher on longer-dated bonds.

WHAT ARE THE PROS AND CONS OF BONDS?

One of the main advantages of bonds compared with shares is that if a company goes bust shareholders could lose all their investment. All shares entitle you to is a share of the profits.

Bonds are a claim on a company's assets instead, so if it goes bust at least you stand a chance of getting something back.

Bondholders still tend to rank below the banks and trade creditors in terms of being paid, and the type of bond you hold determines how much of your money you might get back.

Another advantage of bonds is that they tend to be less volatile than shares, although the trade-off is that over the long term shares have performed better.

For individual investors investing in individual government and corporate bonds is not as straightforward as shares. Most investment platforms require you to invest in bonds over the phone rather than online and corporate bonds often have to be traded in denominations of £10,000 or more and are typically harder to sell than shares.

Alternatives are provided by funds and investment trusts which invest in fixed income and exchange-traded funds which track different baskets of bonds. These have the advantage of providing diversification too.

By **Ian Conway**
Senior Reporter

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KEY ANNOUNCEMENTS OVER THE NEXT WEEK*

Full year results

20 April: Pennant International. **21 April:** Anexo, ASA International, Calisen, Card Factory, Filta, Flowtech Fluidpower, Lidco, Sumo. **22 April:** Boohoo, JTC, RTW Venture Fund, XLMedia. **23 April:** Walker Greenbank.

Half year results

21 April: Associated British Foods, Egdon Resources. **22 April:** AB Dynamics, WH Smith.

Trading statements

17 April: Cranswick, Record. **21 April:** Segro. **22 April:** CRH. **23 April:** Gear4Music, Meggitt, RELX, Taylor Wimpey, Unilever.

PUBLICATION DATES ARE LIKELY TO CHANGE DURING THE CORONAVIRUS CRISIS

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