STOCKS | FUNDS | INVESTMENT TRUSTS | PENSIONS AND SAVINGS

VOL 23 / ISSUE 05 / 11 FEBRUARY 2021 / £4.49

SHARES

WE MAKE INVESTING EASIER

BOOM TIME FOR **LUXURY GOODS**

Welcome to the Roaring Twenties where wealthier people will splash the cash

PLUS

THE UK STOCKS RIDING **THE LATEST BITCOIN SURGE**

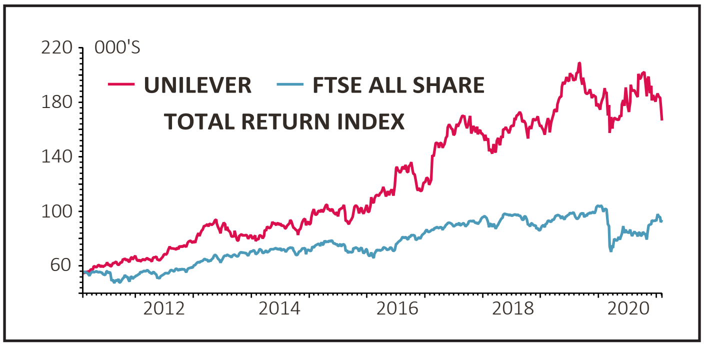
WORLD STOCK INDEX HITS NEW ALL-TIME HIGH ON US STIMULUS HOPES


BAILLIE GIFFORD MANAGED FUND
Investment world look like a big puzzle?
We've solved it in one fund.
The investment world likes to complicate everything. Our Managed Fund likes to keep it really simple. It's made up of equities, bonds and cash, and we think to generate great returns, that's all you need. The result is a balanced portfolio with low turnover and low fees. Beautifully straightforward, it's been answering questions since 1987.
Please remember that changing stock market conditions and currency exchange rates will affect the value of the investment in the fund and any income from it. Investors may not get back the amount invested.
Find out more by watching our film at bailliegifford.com
BAILLIE GIFFORD
Actual Investors

Best buying opportunity for Unilever shares in 11 months

The company ticks the right boxes with essential products, ESG actions and strong cash generation

The Marmite effect seems to have put FTSE 100 stock **Unilever (ULVR)** in the 'hate it' rather than 'love it' camp with many investors. The shares have been out of favour since the market started to prefer value stocks last November, with Unilever seen as an 'expensive defensive' and not offering the level of growth that can be found among cheaper-priced stocks.



A strategic update alongside full-year results (4 Feb) triggered another decline, with the shares at £39.80 now having fallen almost to the £37.26 low seen at the worst of the global market sell-off in March 2020. Investors were disappointed at news of shrinking margins and guidance for heavy restructuring costs over the next two years.

Unilever is targeting 3% to 5% sales growth over the longer term. The consensus analyst forecast is 2.6% growth in 2021, 3.3% in 2022 and 1.6% in 2023 so the consumer goods giant will need to work harder to meet growth targets.

In an environment where investors have been obsessed with fast growth, it is understandable why many people wouldn't be interested in Unilever. However, there is considerable merit in owning the shares for the long term.

According to SharePad, over the past 10 years Unilever has achieved 1.4% annualised sales growth, roughly on a par with **Imperial Brands (IMB)** and **Tesco (TSCO)**. While this may look dull, Unilever as an investment has been far from boring.

Over the past 10 years it has delivered a 204% total return which encompasses share price gains and dividends reinvested, based on Refinitiv data. This is nearly triple the total return from the FTSE All-Share index (71%) over the same period.

Its products are in demand in both good and bad economic conditions, hence why people call it a 'defensive' stock.

Importantly, it is one of the few companies delivering on positive environmental, social and governance factors rather than just declaring an intention.

Ten years ago, it declared an ambition to become the world's most sustainable business and its achievements to date have been commendable such as sourcing all of its agricultural raw materials sustainably. It is now driving equality in the supply chain.

Cash generated from operations is reinvested in the business which gives it an advantage in marketing and product innovation, and it funds a growing stream of dividends.

Unilever is not perfect by any means. Some of its brands have limited growth potential, so they are likely to be sold. There is talk of the company wanting to make big acquisitions and with that comes the risk of over-estimating cost synergies or overpaying, just as **Reckitt Benckiser (RB.)** did with its purchase of Mead Johnson.

The group has lagged some of the consumer goods peers during the pandemic because of its smaller exposure to cleaning products. It may also be looking with envy at Nestle which is streets ahead in pet care.

However, we're confident that Unilever can move with the times and just because the shares are unloved today doesn't mean they will stay that way permanently. A diversified portfolio needs a reliable name like Unilever and its moment in the sun will come again (and again) in the future. [DC]

Contents

CFA UK Publication of the Year CFA UK Journalism Awards 2019

News Provider of the Year (Highly Commended) CFA UK Journalism Awards 2020

World stock index hits new all-time high on US stimulus hopes

Investors are 'all in', with risk aversion at pre-pandemic lows

With markets approaching the one-year anniversary of their pre-Covid-highs, it might seem surprising that the MSCI All Countries World index, the benchmark most used by global funds, is hitting new all-time highs.

Thanks to unprecedented monetary and fiscal stimulus by the world's central banks, markets have recovered sharply from last year's depths of despair even though earnings for a large part of the economy have been wiped out.

Investors who were already bullish are even more bullish. Howard Ward, director of growth products at Gabelli Funds, says stocks are 'the only game in town'.

Bond investors meanwhile have to scrape the barrel and buy BB- or junk-rated bonds just to generate a positive real yield.

We're at the stage in markets where risk appetite is so high – or to put it another way, risk aversion is so low – that what would normally be seen as bad news has become good news.

The latest US non-farm payroll data, which showed a big downward revision to the November figure suggesting far fewer jobs were created than at first sight, actually saw the Nasdaq and S&P indices make new highs following the news.

The argument is that, under Secretary Janet Yellen, the Treasury will move quickly to deploy its stimulus in order to create more jobs, rather than wait for evidence that the economy actually needs it.

Even rising Treasury yields – the US 10-year government bond is heading towards 1.25% again for the first time since 2017 – are no longer seen as a negative. Although debt levels are high, the bulls argue that the fact the market can tolerate higher interest rates and higher inflation is another reason to own certain types of stocks.

Many analysts believe that by targeting an average inflation rate of 2%, the Fed will let prices overshoot in order not to rush into tightening, so market interest rates (yields) will continue to rise.

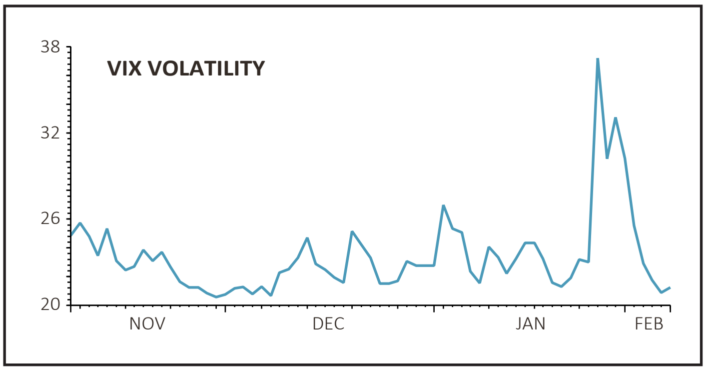
Aversion Inversion

Global stocks hit fresh record as risk aversion drops to pre-pandemic lows

Source: Bloomberg, Citigroup

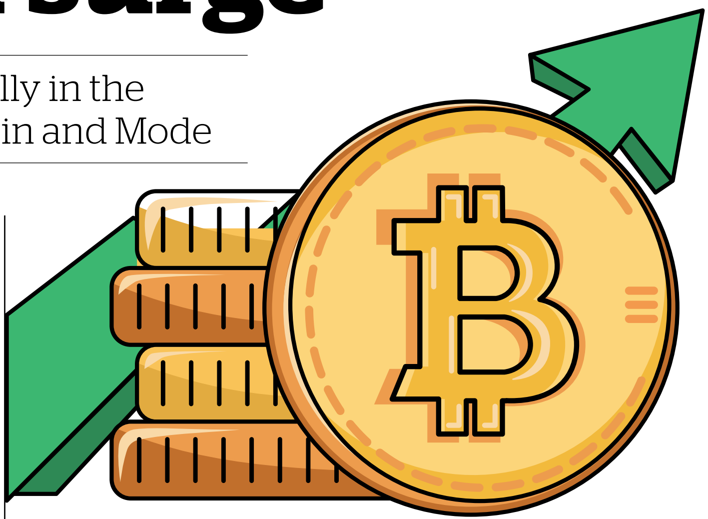
Also worth noting is the sudden fall in the Vix volatility or 'fear' index. In the week to 5 February it lost 44%, the second sharpest fall on record. This might normally be a cause for concern, yet a look at the historical returns 12 months after similar falls in the Vix is encouraging for stocks.

On the five previous occasions when the gauge fell by 40% or more in a week, 12-month returns were uniformly positive, ranging from 5% to as much as 30% with an average of 20%. [IC]



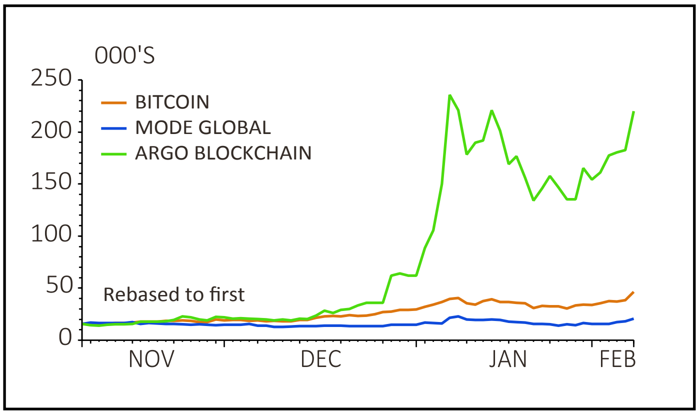
The UK stocks riding the latest bitcoin surge

Tesla's big investment has driven a new rally in the cryptocurrency, benefiting Argo Blockchain and Mode



In the few short weeks of 2021 to date a theme of unconventionality seems to be taking hold in the markets. No sooner had the Reddit-inspired short squeeze briefly added billions to the value of some beaten down US companies, cryptocurrency bitcoin is mounting another charge as it races towards the $50,000 mark.

This is driving up prices of related assets and businesses with two UK-listed firms surging higher. **Argo Blockchain (ARB)** has moved from 7.6p to 130.5p in the last three months, while recently listed **Mode Global (MODE)** is up a more modest, though still material, 30% on its October 2020 issue price.



Investors may be wondering how both businesses fit in the cryptocurrency food chain. Argo Blockchain is a cryptocurrency miner. Bitcoin and other cryptocurrencies are digital alternatives to cash and they work on 'blockchain' technology.

A block is a piece of computer code that stores the data for a transaction. It is linked to the existing chain of blocks which acts as a ledger, or a record of all transactions.

Mining cryptocurrency means verifying transactions and adding new blocks to a blockchain ledger, a complex process which is rewarded with bitcoin. Argo recently reported mining revenue of £2.48 million for January, up from £1.63 million in December 2020.

The massive increase in its market value likely reflects the limited options in terms of share-based investments for those looking to play the leap in bitcoin.

Mode is a bitcoin banking app. It saw trading volumes surge 1,500% in December. Data on its customer base is illustrative of the demographic driving the bitcoin bounce – 79% are male and 64% are 30 or under.

It also offers a 'Bitcoin Jar' product which offers the prospect of interest on holdings of the cryptocurrency.

The latest leg higher for bitcoin follows the news that electric vehicle and technology company Tesla had bought $1.5 billion worth of the cryptocurrency, something Mode did on on a much smaller scale last year when it placed 10% of its cash reserves in bitcoin.

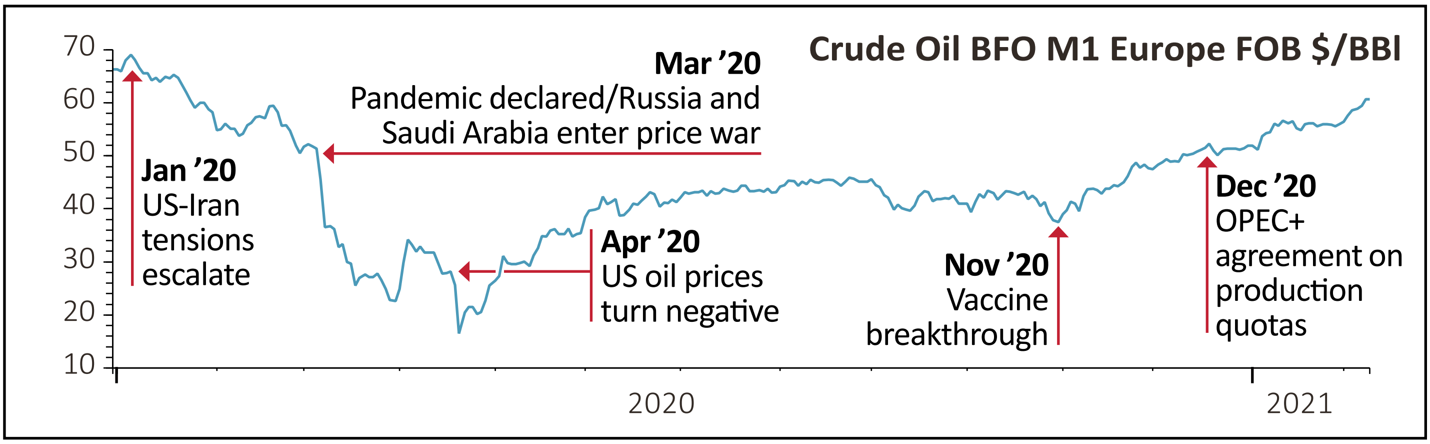
The somewhat speculative nature of the action around bitcoin is revealed in the pace of its recent rise. After breaching $20,000 for the first time in the last days of 2020 it was trading at more than double that amount within a matter of weeks.

And the surging price of joke cryptocurrency Dogecoin – linked to a canine-related viral internet phenomenon from 2013 – is a further indication of a level of frenzy in this space.

Read this article to learn why bitcoin is starting to be taken more seriously by the business and investment community. [TS]

The factors behind gushing oil prices and what could set them back

A weakening dollar, tighter supply and stimulus speculation help Brent to a winning streak



The oil price is making a big comeback. On 9 February the Brent crude benchmark marked its seventh straight session of gains – its best winning streak since January 2019 – as it returned to pre-pandemic levels above $60 per barrel.

Investment bank Goldman Sachs, one of the first to pitch $100 per barrel before that level was reached in the late noughties, believes Brent will hit $65 by the middle of the year, bringing forward an earlier forecast by six months.

While there are several interlinking factors behind the rise in the oil price, there are reasons to think the momentum may not be maintained given the difficult demand picture.

On the supply side there are some signs that the broad extension to the output curbs introduced by OPEC and affiliates like Russia are having some impact. Furthermore, the latest weekly data showed US inventories of oil fell to 475.7 million barrels, the lowest level since March 2020.

However, there are reasons not to get carried away on supply as Bank of America recently commented: 'While we see a demand recovery on the horizon, we expect OPEC+ spare capacity to limit the upside for crude prices.'

Russia is ramping up production while Saudi Arabia effectively takes the hit by keeping to quotas. That situation may not last for too long; after all, it is less than a year since the two countries started an ill-timed price war over crude.

Another factor in oil's recent price rise is the progress of a $1.9 trillion Covid relief package in the US. This is stoking inflation expectations which is supportive of real assets like oil and adding to the recent depreciation of the dollar. The latter is typically supportive for oil prices and other commodities which are dollar-denominated.

The gradual reopening of the economy should help drive demand for oil as more normalised levels of travel and other economic activity potentially resumes.

However, the patchy nature of a rebound in air travel, with countries looking to limit the spread of new Covid variants as they roll out vaccines, is likely to constrain demand for jet fuel for some time to come.

For its part the US Energy Information Administration recently said it will take until 2029 for US energy demand to reach 2019 levels. [TS]

Six potential takeover targets as M&A heats up

UK shares are in the sweet spot with relatively low valuations and an advanced vaccination programme offering more visibility

UK firms have been subject to around £28 billion of mergers and acquisitions deals so far in 2021, the highest level since 2009 according to data from Dealogic. Investors are now trying to work out which UK stocks could be next.

Temporary power supplier **Aggreko (AGK)** surged 38% on 5 February after a consortium of private equity groups TDR Capital and I Squared Capital made a possible all-cash offer of 880p per share.

TDR was also behind a 305p per share proposal for specialist distressed debt manager **Arrow Global (ARW)**, pushing the shares up 26% (8 Feb).

Increasing interest from private equity buyers shouldn't be a surprise as collectively they have around $1.5 trillion of cash to invest, according to data provider Preqin.

In addition, UK shares have lagged other developed markets due to Brexit limbo over the last year, making them cheaper in relative terms. Asset manager Schroders says UK stocks have rarely been cheaper based on a price to sales multiple.

The pandemic has created a polarised market with the leisure, hospitality and travel sectors becoming casualties while the computer games and gambling sectors have seen a significant boost. Private equity and trade buyers are looking at both losers and winners of the pandemic as they seek to take advantage of strong trading or expect a bounce from the UK economy reopening.

Investors looking for potential targets might want to focus on companies with good asset backing and reliable cash flows, as well as undemanding valuations. *Shares* ran a screen on the market for such stocks and interestingly Aggreko made the original list.

Of the names on the list excluding Aggreko, UK food retailer **J Sainsbury (SBRY)** has good asset backing and reliable revenues. The company has been reducing its debts, leaving scope for a buyer to increase leverage should a takeover happen.

Home improvement retailer **Kingfisher (KGF)** has benefited from the pandemic as people spend more cash on their home which is likely to remain a key driver of growth. Foreign private equity buyers could view Kingfisher as a strategic entry into the UK.

Tool hire firm **Speedy Hire (SDY)** is also on the list and has been increasing market share. [MG]

ARE THESE COMPANIES TAKEOVER TARGETS?

	EV/FCF	EV/EBITDA
Vodafone	9.9	4.6
Speedy Hire	9.9	5.9
J Sainsbury	9.0	6.1
Imperial Brands	6.9	6.9
Kingfisher	5.2	7.3
Royal Mail	7.9	8.5

Key: EV= Enterprise Value, FCF=Free Cash Flow, EBITDA=Earnings before interest, taxes, depreciation and amortisation

Shares' takeover screen criteria:
EV/FCF below 10
EV/EBITDA below 10
Net Debt/Total Assets below 50%

Source: Stockopedia, Refinitiv

Travel stocks could slump if summer holiday surge doesn't happen

TUI and On The Beach have both reported lower summer 2021 booking demand

Almost since the pandemic began both holidaymakers and travel companies circled summer 2021 as the period when we could finally get away again, but recent booking trends reported by some firms suggest that could be in doubt.

Any hit to demand this summer, the crucial trading period for travel firms where they look to recoup losses made in winter, could have a significant negative impact on the share prices of airlines and tour operators. This is important as shares in many of these companies have already risen close to pre-pandemic levels on the expectation of a substantial recovery in bookings this summer. That leaves them vulnerable to sharp declines if expectations aren't met.

In its first quarter results (9 Feb), tour operator **TUI (TUI)** revealed that summer bookings, including amendments and voucher rebookings, are down 44% compared to summer 2019 levels, which it has chosen as a comparative period as it was undistorted by Covid-19.

HOLIDAY FIRMS' SHARE PRICE GAINS SINCE 2020 MARKET LOW

Jet2	184%
Wizz Air	137%
On The Beach	127%
Ryanair	80%
EasyJet	55%
International Consolidated Airlines	18%
TUI	6%
FTSE All-Share	37%

Source: SharePad, 9 February 2021. Data from 23 March 2020.

TUI is optimistic of a surge in late demand and has maintained 80% of its operating capacity compared to summer 2019 levels, and says it 'shares the industry expectation of delayed bookings whilst vaccine programmes are underway, the rollout of which will support the lifting of extensive travel restrictions.'

Any setback to people taking summer holidays could put pressure on TUI's finances which are already weak thanks to very high levels of debt.

Helping dent public confidence towards travel have been recent comments from politicians and officials. Environment secretary George Eustice said the risk of new coronavirus variants arriving from other countries is set to 'remain prevalent' and added that 'for now we have to be cautious about international travel', while Professor Jonathan Van-Tam believes people are 'making guesses about the unknown' in booking holidays abroad.

Online package holiday provider **On the Beach (OTB)** said its summer 2021 bookings have been 'very weak' due to travel bans and quarantines, with its bookings taken in the four months to 31 January down 83%. Its UK website traffic and spend on online marketing activity has fallen 73% and 85% respectively.

Further evidence that UK holidaymakers are becoming more cautious comes from Thomas Cook, whose brand was bought by Chinese private equity investor Fosun after the original firm's collapse in 2019. Thomas Cook said 40% of its recent holiday bookings have been for October rather than the summer.

According to media reports, smaller independent holiday providers are also reporting similar booking patterns with customers holding off until later in the year. [YF]

The retail giant with a chance of beating Amazon

Walmart benefits from a winning combination of keen prices, a dense store network and a growing digital business

A share price pause for breath at the world's biggest retailer Walmart presents a buying opportunity ahead of fourth quarter results on 18 February. These should confirm another period of firm market share gains and online sales progress and contain an exciting update on Walmart's strategic priorities.

A $412 billion cap retail goliath, Walmart has been gobbling up market share during the pandemic and we believe these gains should stick once the Covid crisis abates.

Moreover, we think it is well worth investing in one of the few global retailers with the financial clout and online capabilities to compete with Amazon long term at least in its domestic market.

Near term, this progressive, high-quality dividend payer has 'Every Day Low Price' at the cornerstone of its strategy, leaving it well placed to benefit as hard-pressed US consumers spend their stimulus cheques online and in its stores.

WALMART
BUY
(WMT:NYSE) $145.80

Market cap: $412 billion

WALMART'S WIDE MOAT

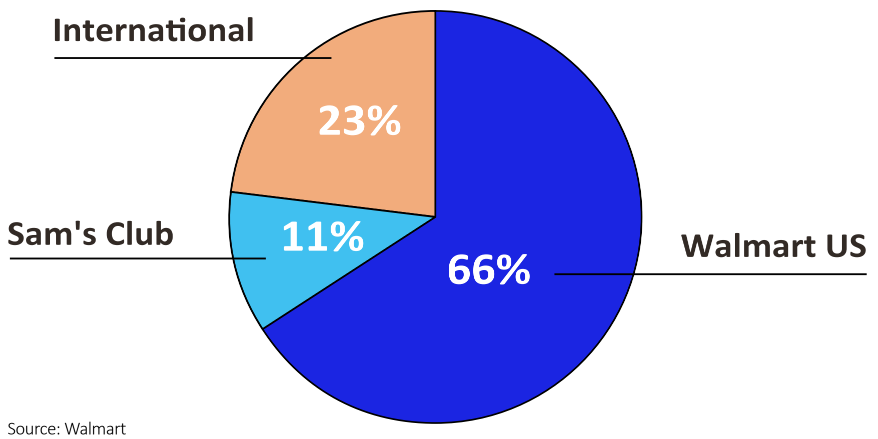
A consumer defensive colossus, Bentonville-based Walmart operates variety stores, discount stores, superstores, Sam's Clubs (its membership-only retail warehouse stores named after founder Sam Walton) and Neighborhood Markets, along with the walmart.com and samsclub.com websites.

Walmart sells everything the consumer could want, ranging from groceries and electronics to clothing, home furnishings and health and wellness products.

As of 23 Sept 2020 the company, led by chief executive Doug McMillon, operated around 11,500 stores across 27 countries including the US, Canada, Central America, Chile, China, India, Mexico and Africa.

Besides being a traditional bricks and mortar retailer, Walmart has transformed itself into a leading omnichannel player through acquisitions including Jet.com, acquired in 2016 to bolster its online

Net sales by segment - full year 2020



Source: Walmart

ambitions, and the likes of men's clothing site Bonobos and online active outdoor retailer Moosejaw as well as delivery company Parcel.

Walmart has also forged partnerships with the likes of Shopify and JD.com, invested heavily in delivery initiatives like Walmart+ and backed Indian e-commerce platform Flipkart. This dizzying array of deals has positioned the company to keep pace with the fast-moving retail ecosystem and compete with Amazon.

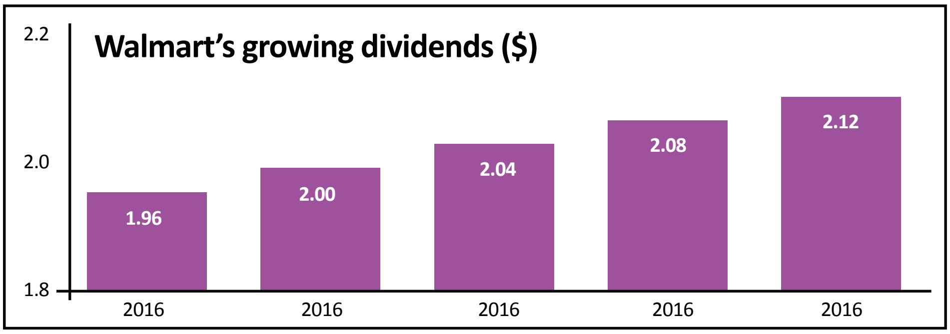
Morningstar believes Walmart has a wide economic moat and is in fact 'the only American retailer that can compete comprehensively with Amazon's retail offering', given its 'unrivalled scale', 'prodigious procurement strength', strong brand and growing e-commerce platform.

In order to sharpen its focus on core growth regions, Walmart has sold its majority stake in UK grocer Asda, offloaded its retail operations in Argentina and announced a deal to dispose of a major stake in Japanese subsidiary Seiyu.

CLEAR COVID WINNER

With non-essential retailers and mom and pop shops unable to open during the Covid-19 pandemic, Walmart has mopped up market share, benefiting from bumper demand for essential items.

In addition, the stay-at-home trend has turbo-charged its e-commerce sales. These tailwinds enabled Walmart to smash sales and earnings estimates for the third quarter of its financial year to 31



Source: Walmart. 31 January year end.

January 2021.

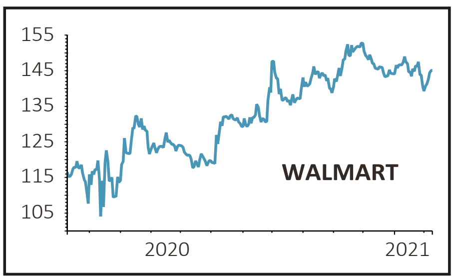
Third quarter results showed a $6.7 billion jump in total sales to $134.7 billion and marked Walmart's 25th consecutive quarter of like-for-like sales growth, with comparable sales skipping 6.4% higher thanks to strength in general merchandise, food, and health and wellness sales.

US e-commerce sales surged 79% higher with a boost from pandemic-led social distancing, though it should be noted all this extra business comes with higher Covid-19-related costs, such as higher wages and benefits and sanitisation and other safety measures. Online strategies are driving the growth, but they also require hefty investment in e-commerce expansion and technological advancements.

Nevertheless, given that the pandemic has permanently changed grocery shopping, we believe best-in-class operator Walmart will be able to keep these customers even after the coronavirus crisis ends, and that is why it is well worth paying up for the shares.

According to Refinitiv data, Walmart trades on a price-to-earnings ratio of 25.3 for fiscal 2022, a premium to the likes of **Tesco (TSCO)** on 13.4 times forward earnings or France's **Carrefour (CARR:PA)** on a prospective multiple of 9.6. But one which is justified by a more diversified and digital strategy.

For the year to January 2021, Refinitiv-compiled forecasts point to pre-tax profits of $21.86 billion, rising to $21.95 billion in 2022 and then $23.07 billion in 2023. [JC]



New-look Bango is a great way to play online payments boom

The company could be on the cusp of rapid profit and share price expansion

The digital payments space is booming and not just because of lockdown. We are all buying more stuff online, and that requires safe and easy ways to pay.

A forecast-thumping fourth quarter for industry leader Paypal earlier this month saw its stock jump to new all-time highs.

Cambridge-based **Bango (BGO:AIM)** is much smaller but well worth a look.

It runs a direct carrier billing (DCB) payments platform. This is a 'one-click' solution that allows online shoppers to buy goods and services by adding the internet shopping charges to their mobile phone bill, once they have set up an account.

That's great for many consumers uncomfortable submitting debit or credit card details online. It also provides data insights that help improve the user experience and can help to acquire more paying customers.

Bango makes its money by getting a tiny percentage per transaction, about 0.6% in 2020. This produced £12.2 million revenue last year on £1.9 billion end user spend (EUS), the latter doubling for the fifth consecutive year.

Crucially, this will mean

BANGO
BUY
(BGO:AIM) 201p
Market cap: £150 million

adjusted earnings before interest, tax, depreciation and amortisation (EBITDA) of more than £4 million, finally making the profits breakthrough after nearly two decades of trying.

But $1.9 billion EUS is a drop in the ocean compared to the $4.9 trillion of digital payments estimated globally last year. According to Statista data, the space is set for annual compound growth of 13.4% between now and 2024, putting the digital payments market at $8.17 trillion by 2024.

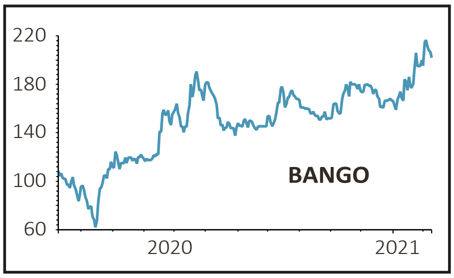
Bango already connects online app stores and merchants to over 3 billion users across the globe and on many of the world's biggest online platforms.

Merchants including Amazon, Google, Microsoft and Samsung, mobile network operators such as O2, Vodafone and T-Mobile, and pay TV, cable and fixed-line operators use Bango payment technology to provide new ways to pay that are fast, simple and secure. **BT (BT.A)** came aboard in November to help power bundled subscription services like Britbox.

FinnCap believes that Bango's DCB platform is becoming 'cornerstone technology' in the rapidly growing global market for subscription-based entertainment, and is expanding into areas like virtual gym memberships and food clubs, as well as video, music and game-streaming subscriptions.

Bundling multiple services is becoming an increasingly powerful tool, helping to win new customers for platforms and to retain existing ones.

Bango has showed promise before only to disappoint so the stock remains higher risk. That said, revenue could grow at more than 20% for several years, and with a largely fixed cost base, we anticipate rapid profit expansion which could light a fire under the stock. Forecasts will be updated following 2020 results on 16 March which could act as a near-term catalyst for the stock. [SF]



OCADO

(OCDO) £26.63

TOP STOCKS FOR 2021

Gain to date: 15.7%

Original entry point:

Buy at £23.01, 23 December 2020

ONLINE SUPERMARKET FIRM **Ocado (OCDO)** posted strong results for the year to 29 November, registering a 35% increase in retail revenues and a 52% increase in fees billed to its overseas technology customers.

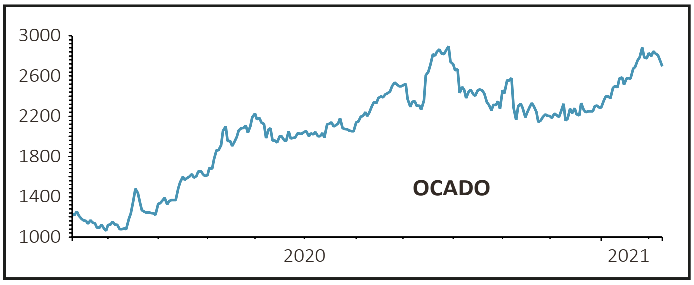
A positive result in the retail business was never in doubt as more people sign up for online grocery delivery, and operating profits jumped a staggering 265%.

The UK technology business grew its revenues by double digits, but continued investment in capacity and software/hardware meant profits were lower.

The overseas technology business finally delivered proof of concept, booking its first capacity-related fees from customer fulfilment centres (CFCs) for French hypermarket group Casino and Australia's Sobeys.

A third international CFC, for US grocer Kroger, is set to go live soon and seven more firms should be on its platform this year.

Continued high levels of investment came at the expense of group profits. The firm booked a pre-tax loss of £44 million and hinted that group operating profits would be lower this year, leading to weakness in the shares on the day of the results (9 Feb).



SHARES SAYS: ↗

Ocado is at a major turning point as overseas customers start to go live with its technology. Keep buying the shares. [IC]

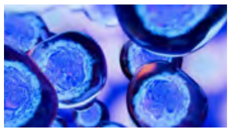
GLAXOSMITHKLINE

(GSK) £12.70

Loss to date: 3.9%

Original entry point:

Buy at £13.21, 5 November 2020



WHILE **GLAXOSMITHKLINE (GSK)** reported (3 Feb) full year 2020 adjusted profits in line with guidance, down 4% at constant currencies, the company pushed any meaningful improvement in revenues and profits out to 2022.

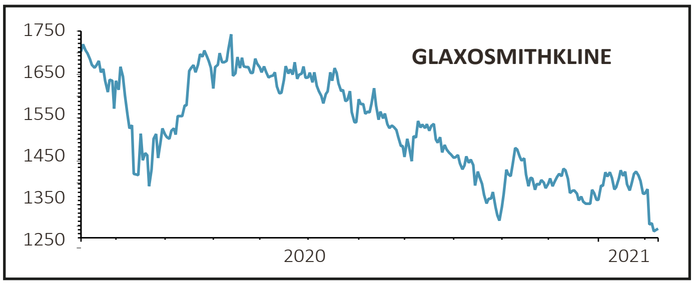
The new guidance reflects increased investment in the drug pipeline and a deferral of strong growth in the vaccine division due to the impact of the Covid-19 immunisation programmes on other rounds of inoculations. Most notably the shingles vaccine which is aimed at the elderly.

However, the results also provided evidence of good strategic progress. The respiratory franchise grew slightly as sales of new products overtook legacy products for the first time in several years.

The cancer franchise showed good momentum with Zejula (ovarian cancer) growing 48% and Blenrep (multiple myeloma) reporting £33 million in sales after launching in the third quarter of 2020.

GlaxoSmithKline expects more than 20 new product launches by 2026 with potential peak revenues of more than $1 billion.

Following the separation of Consumer Healthcare in 2022 the company will review its dividend policy.This makes sense and is designed to drive growth in the Biopharma pipeline. Glaxo will provide more details on asset allocation priorities in June.



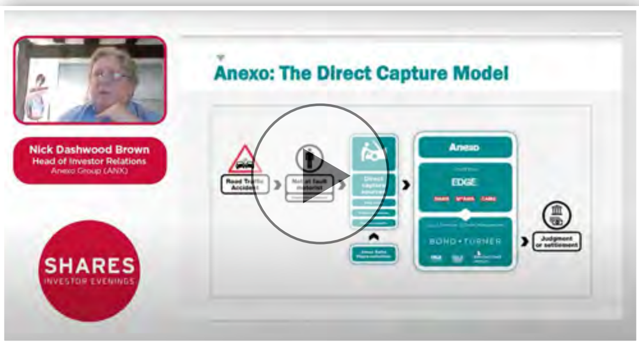
SHARES SAYS: ↗

The attractions remain in place and investors should buy on current share price weakness. [MG]

WATCH RECENT PRESENTATION WEBINARS

Destiny Pharma (DEST) – Neil Clark, CEO

Destiny Pharma is a clinical stage biotechnology company. It is engaged in the development of new anti-microbial drugs to address the growing and unmet demand for prophylaxis and treatment of life-threatening drug-resistant bacteria.



Anexo Group (ANX) – Nick Dashwood Brown, Head of Investor Relations

Anexo Group (ANX) is a specialist integrated credit hire and legal services group focused on providing replacement vehicles to consumers who have been involved in a non-fault accident.

Strix Group (KETL) – Mark Bartlett, CEO

Strix Group (KETL) is a designer, manufacturer and supplier of kettle safety controls and other complementary water temperature management components involving water heating and temperature control, steam management and water filtration.

Visit the Shares website for the latest company presentations, market commentary, fund manager interviews and explore our extensive video archive.

CLICK TO PLAY EACH VIDEO

SHARES SPOTLIGHT

www.sharesmagazine.co.uk/videos

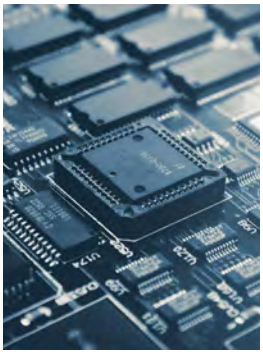
TEXAS INSTRUMENTS

(TXN:NDQ) $175.12

Gain to date: 53.1%

Original entry point:

Buy at $114.42, 21 May 2020



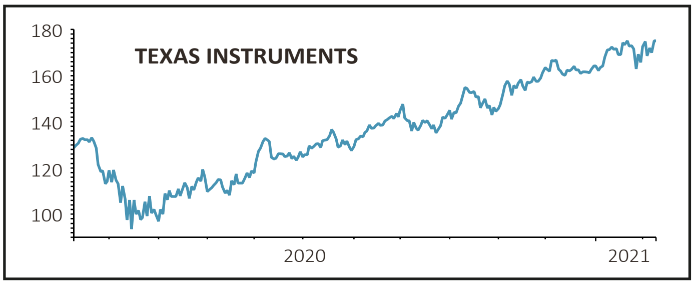
ANALOG MICROCHIPS MANUFACTURER Texas Instruments continues to knock the lights out after extending its long run of beating earnings expectations to 12 quarters in a row.

Investors who followed our original *Great Idea* in May last year will be sitting on 50%-plus returns, a superb performance for a company valued at more than $160 billion.

For the last quarter of 2020, Texas Instruments generated earnings per share (EPS) of $1.80, outstripping expectations for $1.34 by 34% and jumping 61% year-on-year. Revenue of $4.08 billion was 22% up year-on-year and 13% above forecast.

Analysts remain optimistic as the semiconductor upcycle swings through 2021 and possibly beyond. Consensus EPS estimates are currently pitched at $6.43 for the whole of this year, rising to $7.30 in 2022, compared with 2020's $5.97.

Designing vital bits of technology kit and retaining extensive pricing power, the long-run growth potential we flagged originally looks as attractive today as it did then, and that bodes well for further share price gains as the world economy recovers from its Covid hangover.



SHARES SAYS:

Still a buy for the longer-term. [SF]

EXPERIAN

(EXPN) £26.40

Loss to date: 14%

Original entry point:

Buy at £30.69, 15 October 2020

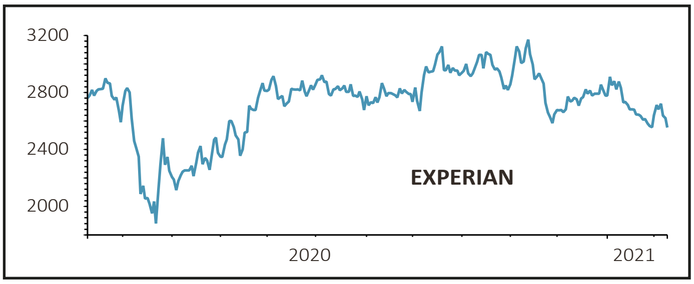
OUR BUY ON **Experian (EXPN)** hasn't worked out so far but we're sticking with it as a play on the global reopening and a 'levelling up' of consumers through the introduction of progressive new products.

The business to business division, which represents around a fifth of revenue, has struggled during the pandemic, especially with regard to the car industry which has seen sales – and therefore credit applications – shrink dramatically.

However, the consumer business still accounts for nearly 80% of turnover and in the US – its biggest market – the firm has positive tailwinds from president Biden's call for socially inclusive growth, although were it to occur the creation of a federally-backed public credit bureau would be negative.

In Brazil, another key market, the law allowing the collection of 'positive' credit data is driving an uptake of Experian's credit-scoring product and allowing consumers to improve their score and obtain affordable credit.

Bank accounts and credit card penetration in Brazil are at much lower level than the US or the UK, and studies have shown that when people are included in the financial system they are more able to support themselves through financial shocks.



SHARES SAYS:

The recent sell-off is a good opportunity to add to positions. [IC]

INVESTING IN A CHANGING WORLD

BLACKROCK NORTH AMERICAN INCOME TRUST PLC

The global economy is slowly recovering from the havoc wrought by COVID-19. Market leadership is changing and there is greater clarity on the future. Tony DeSpirito, Co-Manager of the BlackRock North American Income Trust plc, explains how the portfolio is being managed through these turbulent times.

Tony DeSpirito

Co-Manager,
BlackRock North American Income Trust plc

Capital at risk. The value of investments and the income from them can fall as well as rise and are not guaranteed. Investors may not get back the amount originally invested.

The world that emerges from the pandemic is likely to have changed in a number of crucial ways, from the way we use technology to the priorities for businesses. However, investing in 2021 will be more nuanced than simply targeting the beneficiaries of a 'new normal'. How are we investing through this unusual period?

As the world economy slowly starts to recover from the virus, a few trends are clear: the pandemic has accelerated global reliance on technology, for example. The world has grown used to a low contact world and this is likely to continue with everything from ecommerce to payments.

The US/China trade war, pandemic and then Brexit have forced companies to address the global versus local debate. Lengthy supply chains look increasingly impractical and companies are willing to pay more for local suppliers to ensure consistency. US companies are beginning to bring some of their production capabilities back into the local market. The higher costs associated with local supply could see companies cut stock buybacks and cut back on mergers and acquisitions (M&A) activity or capital expenditure.

Equally, even as earnings return to normal, companies may also reconsider the level of debt they carry on their balance sheets. Companies are usually prepared for a recession, but they are not built for months and months of zero revenue growth. That may influence their view of borrowing and may see some companies cut back.

Environmental, social and governance (ESG) considerations are becoming very important, both for portfolio managers such as ourselves and for companies. Sustainability was a hot topic even before the emergence of COVID-19, but today companies are increasingly going to find themselves judged on how they treated their employees, their customers and their local economy.

FOCUSING ON RECOVERY

These are sustainable and enduring trends. However, ensuring they are reflected in a portfolio is not straightforward. We need to take into account, for example, that the valuations for the highest profile technology stocks are extremely high. Market gains in 2020 were dominated by just a handful of stocks and the market is becoming increasingly concentrated.

Equally, we need to be careful that the gains made by these companies are sustainable. Some companies are likely to have merely brought forward demand from the future. When restrictions are lifted, will anyone want to sit in front of a boxset? These are important considerations for streaming services.

We must also take into account the recovery. News on the vaccine rollout has seen a tentative shift towards more economically-sensitive parts of the market after a long period when this type of stock was out of favour. This is to be expected. Our analysis of recessions going back as far as 1978 suggests that the cheapest stocks get cheaper moving into a recession, but then turn as economic activity starts to pick up. This trend may be even stronger this time round because the disparity in valuations is more extreme.

Again, selectivity is needed. While some leisure stocks have bounced from their lows, this is likely to be short term. It is difficult to see people rushing to get back on a crowded airplane, theme park or movie theatre. There needs to be some quality control.

PORTFOLIO THEMES

What is our solution to the world we find ourselves in? We believe the rotation into economically-sensitive and value areas of the market will continue. Corporate earnings are likely to matter a lot more in 2021 and cyclical companies have far easier year-on-year comparisons because of their weakness this year. There have been a lot of false starts for value, but we believe this one should endure.

We hold a number of stocks that should benefit from economic recovery when it emerges. However, we also want to protect our investors against heightened volatility. So, we are combining recovery-sensitive areas such as financials and energy with more stable areas such as information technology and healthcare. However, for all of our holdings, we continue to focus on quality

– that means a strong management team, healthy balance sheet and dividend growth.

Dividend growth could be particularly important for 2021. In the short term, interest rates are likely to remain low and dividend stocks should find favour as investors hunt for income. Over the longer term, companies that exhibit dividend growth have delivered a competitive return with downside protection. We believe the wave of dividend cuts seen in 2020 are now behind us.

The world is finding its way out of the crisis, but it is a slow process. As such, we believe a 'barbell' approach (an investment concept that suggests that the best way to strike a balance between reward and risk is to invest in the two extremes of high risk and no risk assets while avoiding middle-of-the-road choices), that recognises both the need for stability and the opportunities inherent in recovery, is the right one.

This material is not intended to be relied upon as a forecast, research or investment advice, and is not a recommendation, offer or solicitation to buy or sell any securities or financial product or to adopt any investment strategy. The opinions expressed are from BlackRock as of January 2021 and may change as subsequent conditions vary.

For more information on this Trust and how to access the potential opportunities presented by North American markets, please visit www.blackrock.com/uk/brna

TO INVEST IN THIS TRUST CLICK HERE

Risk Warnings: Past performance is not a reliable indicator of current or future results and should not be the sole factor of consideration when selecting a product or strategy.

Changes in the rates of exchange between currencies may cause the value of investments to diminish or increase. Fluctuation may be particularly marked in the case of a higher volatility fund and the value of an investment may fall suddenly and substantially. Levels and basis of taxation may change from time to time.

Trust Specific Risks

Exchange rate risk: The return of your investment may increase or decrease as a result of currency fluctuations.

Risk to capital through derivative use: The Fund may use derivatives to aim to generate more income. This may reduce the potential for capital growth.

Capital growth/Income variation risk: Investors in this Fund should understand that capital growth is not a priority and values may fluctuate and the level of income may vary from time to time and is not guaranteed.

Derivative risk: The Fund uses derivatives as part of its investment strategy. Compared to a fund which only invests in traditional instruments such as stocks and bonds, derivatives are potentially subject to a higher level of risk.

Gearing risk: Investment strategies, such as borrowing, used by the Trust can result in even larger losses suffered when the value of the underlying investments fall.

Important Information

Issued by BlackRock Investment Management (UK) Limited, authorised and regulated by the Financial Conduct Authority. Please refer to the Financial Conduct Authority website for a list of authorised activities conducted by BlackRock.

The Company is managed by BlackRock Fund Managers Limited (BFM) as the AIFM. BFM has delegated certain investment management and other ancillary services to BlackRock Investment Management (UK) Limited. The Company's shares are traded on the London Stock Exchange and dealing may only be through a member of the Exchange. The Company will not invest more than 15% of its gross assets in other listed investment trusts. SEDOL™ is a trademark of the London Stock Exchange plc and is used under licence.

Net Asset Value (NAV) performance is not the same as share price performance, and shareholders may realise returns that are lower or higher than NAV performance.

The BlackRock North American Income Trust plc currently conducts its affairs so that its securities can be recommended by IFAs to ordinary retail investors in accordance with the Financial Conduct Authority's rules in relation to non-mainstream investment products and intends to continue to do so for the foreseeable future. The securities are excluded from the Financial Conduct Authority's restrictions which apply to non-mainstream investment products because they are shares in an investment trust.

BlackRock has not considered the suitability of this investment against your individual needs and risk tolerance. To ensure you understand whether this product is suitable, please read the Key Investor Document (KID) and the current Annual and Half Yearly Financial Reports which are available on blackrock.com/uk/brna and which provide more information about the risk profile of the investment. If after reading this you have any questions or would like any additional information, please contact your financial adviser or speak to our Investor Services Team.

Any research in this material has been procured and may have been acted on by BlackRock for its own purpose. The results of such research are being made available only incidentally. The views expressed do not constitute investment or any other advice and are subject to change. They do not necessarily reflect the views of any company in the BlackRock Group or any part thereof and no assurances are made as to their accuracy.

This material is for information purposes only and does not constitute an offer or invitation to anyone to invest in any BlackRock funds and has not been prepared in connection with any such offer.

Want a global investment trust? Here's how 15 differ

With numerous products to choose from in the global category, picking the right one can take time. We explain everything you need to know

There are many options for an investor wanting to put their money to work right around the world.

Even if you've narrowed it down and decided to go for an investment trust instead of an open-ended active fund or a passive exchange-traded fund (ETF), choosing the trust for you can still seem a daunting task, particularly when there are 15 of them in the Association of Investment Companies' (AIC) global category.

In this article we help you understand the differences between all the global investment trusts listed on the London Stock Exchange, their objectives and the way they choose to invest.

SCOTTISH MORTGAGE - TARGETS GROWTH COMPANIES INCLUDING UNQUOTED BUSINESSES

A retail investor favourite is **Scottish Mortgage (SMT)**, run by Baillie Gifford. The trust, which has more assets than any other in the category with over £19 billion, is global rather than Scottish and has nothing to do with mortgages.

Its style is growth investing and describes itself as a way for investors to access the world's most exciting growth companies. It has been quick to shoot down suggestions it's a technology fund (top holdings include the likes of Amazon, Alibaba and Tencent) and instead says its approach is to look at companies enabled by technology.

MONKS - DIVERSIFIED EXPOSURE TO GLOBAL GROWTH

Given the popularity and success of Scottish Mortgage in the past year, it can be easy to forget Baillie Gifford also has another global investment trust, **Monks (MNKS)**.

The £2.9 billion trust takes a more diversified approach than Scottish Mortgage with over 100 stocks in the portfolio compared to 96 for SMT, while the largest 10 holdings only account for roughly 20% of the portfolio compared to over 48% for Scottish Mortgage.

While it also invests in the likes of Tesla and Amazon, other top holdings include tech investors Naspers and Softbank, as well as budget airline **Ryanair (RYA)**.

F&C - HIGHLY DIVERSIFIED AND CAUTIOUSLY MANAGED WITH EXPOSURE TO MORE THAN 450 INDIVIDUAL FIRMS WORLDWIDE

The second biggest in terms of assets is **F&C Investment Trust (FCIT)**, which markets itself as something of an all-rounder and we view it as a good option for a beginner investor looking for their first investment.

Some investment trusts and funds, including ones mentioned further into this article, prefer a focused approach, investing in as low as 30 to 40 stocks to get best exposure to their highest conviction ideas.

F&C goes the other way. A spokesman says: 'As the world's oldest collective investment scheme, F&C Investment Trust's aim is to generate long-term growth and income for investors through its highly diversified and cautiously managed portfolio, giving exposure to over 450 individual companies from around the world.'

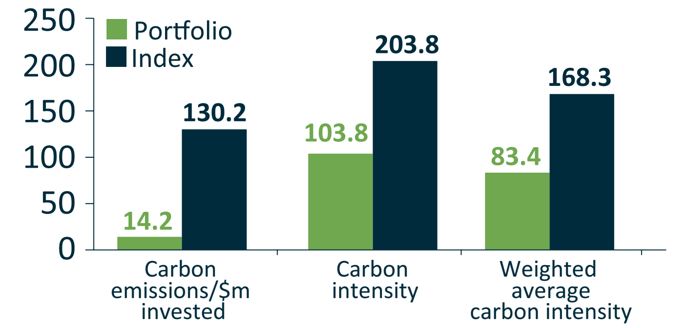
MARTIN CURRIE GLOBAL - A CONCENTRATED PORTFOLIO FOCUSED ON MEGATRENDS

On the opposite end of that spectrum is **Martin Currie Global Portfolio (MNP)**, which holds just 30 stocks with over 40% in its top 10 holdings. Its portfolio ideas are driven by three overriding megatrends – the future of technology, demographic change and resource scarcity.

Like a lot of global trusts, its top holdings include the likes of Microsoft, Visa and Taiwan Semiconductor, but others include medical technology company Masimo, luxury fashion brand Moncler and industrial giant Linde.

Third on the list with most assets is **Alliance Trust (ATST)**, which aims to generate attractive total return from both capital growth and a progressive dividend. Different to most other investment trusts, it uses a panel of third party fund managers, deemed to be the cream of the crop, to pick stocks from around the world.

Martin Currie Global Portfolio: Carbon footprint metrics



Source: Martin Currie and MSCI as at 31 December 2020.

ALLIANCE TRUST - BLENDS THE TOP PICKS OF HIGHLY-RATED FUND MANAGERS

A spokesperson says the portfolio 'provides UK investors exclusive access to the high conviction investment ideas of some of the world's best stock pickers, making it a core equity holding for every generation'.

While its approach may be different, some of the stocks it invests in are similar to other global trusts

Global Trusts: 5 year total return

Scottish Mortgage	476%
Monks	272%
Manchester & London	212%
Lindsell Train	194%
Martin Currie Global Portfolio	142%
Mid Wynd International	137%
AVI Global	128%
Bankers	124%
F&C Investment Trust	109%
Alliance Trust	106%
Brunner	99%
JP Morgan Elect Managed Growth	80%
Witan	79%
EP Global Opportunities	47%
Scottish Investment Trust	43%

Source: The AIC, as of 5 Feb 2020. Share price total return

and include the US tech giants like Apple, Amazon, Alphabet, Facebook and Microsoft, as well as other popular names among global stockpickers including Alibaba, Visa and Mastercard.

WITAN - RECENTLY REVAMPED PORTFOLIO WITH GREATER FOCUS ON GROWTH, USES PANEL OF THIRD-PARTY MANAGERS

The other trust which follows the same third-party approach is **Witan (WTAN)**, which has a clear aim to deliver a total return ahead of its benchmark, 85% of which is made up from the MSCI All Country World index and 15% from the MSCI IMI UK index, together with growth in its dividend ahead of inflation.

While it may follow the same general approach as Alliance Trust, the portfolio is rather different, with its top holding at 3% being the GMO Climate Change Fund, followed by other trusts **Apax Global Alpha (APAX)**, **Syncona (SYNC)** and **BlackRock World Mining (BRWM)**. It does also invest in individual companies.

Top stock positions include holdings in Taiwan Semiconductor, consumer goods giant **Unilever (ULVR)**, and others like MercadoLibre, the Latin American equivalent to Amazon, Heineken and **Diageo (DGE)**.

BANKERS - FOCUSED ON CASH GENERATIVE FIRMS WHICH CAN GROW DIVIDENDS

Another popular dividend-paying trust is **Bankers (BNKR)**, run by Janus Henderson. It aims to offer both growth and income and has a clear objective to achieve capital growth in excess of the FTSE World Index and dividend growth greater than inflation, as measured by CPI.

A spokeswoman for Janus Henderson says the trust primarily employs a bottom-up, valued-based investment process to identify opportunities and 'pays particular regard to cash generation and dividends'. Its top holdings include Estee Lauder and, like other global trusts, Apple, Visa and Mastercard.

SCOTTISH INVESTMENT TRUST - TAKES A CONTRARIAN APPROACH TO MARKETS

The global trust currently offering the highest dividend yield at 3.3% is **Scottish Investment Trust (SCIN)**, a self-managed value-focused trust which says it takes a contrarian approach to global stock markets, viewing them as 'irrational and ultimately inefficient'.

Its top holdings include three major mining firms – Newmont, Barrick Gold and Newcrest – as well as Pfizer, whose shares have not moved much in a year despite its Covid-19 vaccine, and UK stocks **BT (BT.A)** and **Tesco (TSCO)**.

The trust says: 'Our opportunities arise at the opposite point in the cycle – when a downturn leads to excessive pessimism about a company's prospects. This allows us to buy stocks at precisely the point when the profit opportunity is greatest.'

BRUNNER - LOOKS FOR A BALANCE OF GROWTH AND INCOME WITH FOCUS ON QUALITY STOCKS

A running *Shares Great Idea*, **Brunner (BUT)** is a trust that aims to be a 'one-stop shop' for investors looking for growth stocks around the world, and a dividend that rises over time.

The trust, run by Allianz Global Investors, isn't skewed to either a growth or a value style and has both a mix of faster growing companies trading on higher earnings multiples as well as lower growth firms on cheaper multiples.

It has some overlap with other global trusts in stocks like Microsoft, Visa and Taiwan Semiconductor, but also has some lesser known names to UK investors in its top holdings like healthcare company UnitedHealth, insurer Muenchener Rueckver and life sciences firm Agilent Technologies.

MID WYND - LOOKS FOR GROWTH WITH AN EYE TOWARDS CAPITAL PRESERVATION

Another running *Shares Great Idea* is **Mid Wynd International (MWY)**, which focuses on quality companies that more than anything have strong balance sheets, good secular growth prospects, high barriers to entry and little competition, giving them the ability to maintain pricing power over time.

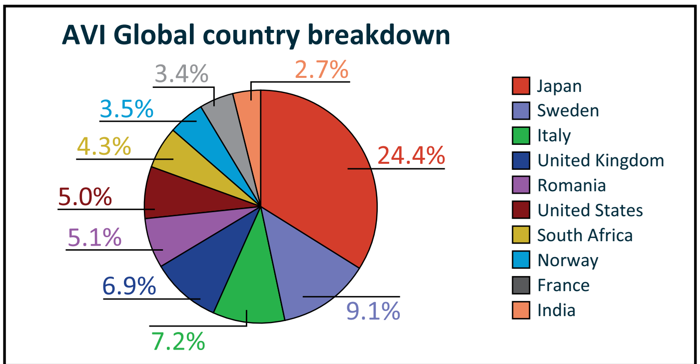
It looks to profit from long-term trends such as online services, automation and the emerging market consumer. Technology and healthcare stocks account for 43% of the portfolio. Alongside stocks like Amazon and Microsoft, it also holds big Japanese stocks like Daifuku (warehouse automation) and Hoya (tech and healthcare products), and has a skew towards Asia with 12% of assets in Japan and 7% in China and elsewhere in Asia.

Manager Simon Edelsten explains to *Shares*: 'Mid Wynd would suit more patient investors, as our disciplined approach to company selection and valuation reduces volatility. The trust will sometimes lag fast-rising markets but should be more resilient in times of crisis, leading to strong returns over the longer term.'

AVI GLOBAL - CLEAR BIAS TOWARDS VALUE STOCKS

One trust that seemingly goes under the radar, despite holding over £1.1 billion in assets, is **AVI Global (AGT)**, which invests in stocks firmly in the value bracket.

The trust invests in a range of companies across different regions and different market caps, while many of its top 10 holdings are investment-focused companies, including **Oakley Capital Investments (OCI)** and **Pershing Square Holdings (PSH)**.



Source: Morningstar, as at 31 January 2021

EP GLOBAL OPPORTUNITIES - LOOKS FOR UNDERVALUED EQUITIES, A CONCENTRATED PORTFOLIO WITH NO BENCHMARK

Another under-the-radar trust is **EP Global Opportunities (EPG)**, which also takes a value approach and unlike most other trusts doesn't have a benchmark. It has assets of £107 million.

A spokesperson tells *Shares*: 'The company invests in a focused portfolio of approximately 30 to 40 global holdings, predominately in quoted equities. It may also invest a substantial portion of its assets in debt instruments, cash or cash equivalents when the investment manager believes market or economic conditions make equity investment unattractive.'

OTHER NAMES

Other trusts in the AIC's global category include **JP Morgan Elect – Managed Growth (JPE)**, which invests in a range of JP Morgan funds as well as other investment trusts like the popular **Finsbury Growth & Income (FGT)**, **Mercantile (MRC)** and **JPMorgan Claverhouse (JCH)**.

A JP Morgan spokesperson says the trust aims to offer long term capital growth from investing in an internationally diversified range of other investment trusts, managed principally by JP Morgan Asset Management (JPMAM), as well as JPMAM open-ended funds.

One trust in the global category with perhaps surprisingly modest assets is **Lindsell Train (LTI)**, which has just £240 million of investors' money.

This may be down partly to its prohibitively high share price at £1,380, and also the fact other Lindsell Train strategies like Finsbury Growth & Income and its UK, global and Japan equity funds are more popular and a lot more marketed.

Over half of the trust's assets is invested in the Lindsell Train asset management company itself and its North American fund, while other top holdings include Nintendo, Unilever, PayPal, Heineken, Diageo and **London Stock Exchange (LSEG)**.

By **Yoosof Farah** Reporter

FINDING INCOME IN A DIVIDEND DROUGHT: A CONTRARIAN APPROACH

Whatever your stage of life, Covid-19 has caused huge changes. From unprecedented restrictions on personal movement to an accelerated shift to online working and shopping, no life has been untouched. For those in retirement, concerns about reliable income have been growing as the global economic outlook has worsened and dividend cuts abound.

Why income investors should look globally

The pandemic has had a major impact on corporate revenues, and it will take some time for companies to fully get back on their feet. To secure their long-term survival many businesses have boosted their cash reserves by reducing their dividends, with roughly half of the UK's FTSE 100 companies cancelling, cutting, or suspending payments.

For retirees reliant on equity portfolios for income, the scarcity of dividends is a headache. Historically, a relatively small number of UK stocks have provided the majority of income, but now investors with a UK bias are facing a potential shortage.

The obvious answer to concerns about the concentration of income risk in the UK is to diversify. Investing in a portfolio of global equities provides an income stream from a much broader pool of investments than is available from UK companies alone.

A contrarian approach can pay dividends

The Scottish's high-conviction, bottom-up investment approach delivers an equity portfolio that is spread across multiple regions and sectors, providing diversification of risk. Although our contrarian investment style doesn't actively target companies that pay high dividends, the out of favour investments that we are attracted to tend to pay higher dividends over the course of an economic cycle. That rewards our shareholders, while we wait for the improving business prospects that we foresee.

The Scottish has a dividend yield of around 3.2%, which is currently the highest in the AIC global sector. The recently announced final dividend extends the Company's long track record of annual regular dividend increases to 37 consecutive years.

> “the out of favour investments that we are attracted to tend to pay higher dividends over the course of an economic cycle”

A dividend reserve – the benefit of long-term thinking

Over the years, The Scottish has prudently built a substantial revenue reserve in preparation for leaner times. As at 31 October 2020, this reserve was greater than 2.5 times the targeted annual dividend for the year to 31 October 2021. It gives the Company the ability to keep paying its shareholders when many businesses opted to curtail dividend payments.

Although not guaranteed, The Scottish's intention to continue to grow the regular dividend over the longer term backs up our status as a 'dividend hero' (as recognised by the Association of Investment Companies). ■

8 February 2021

THE SCOTTISH
Investment Trust

High conviction, global contrarian investors

For more information visit **www.thescottish.co.uk**
or follow
@ScotInvTrust
The Scottish Investment Trust PLC

If you're interested to learn more about The Scottish's contrarian investment approach, and some interesting opportunities that lie ahead in a sustained reopening, you can subscribe at www.thescottish.co.uk/subscribe

RISK WARNING

Please remember that past performance may not be repeated and is not a guide for future performance. The value of shares and the income from them can go down as well as up as a result of market and currency fluctuations. You may not get back the amount you invest. The Scottish Investment Trust PLC has a long-term policy of borrowing money to invest in equities in the expectation that this will improve returns for shareholders. However, should markets fall these borrowings would magnify any losses on these investments. Investment trusts are listed on the London Stock Exchange and are not authorised or regulated by the Financial Conduct Authority. Please note that SIT Savings Ltd is not authorised to provide advice to individual investors and nothing in this article should be considered to be or relied upon as constituting investment advice. If you are unsure about the suitability of an investment, you should contact your financial advisor.

Issued and approved by SIT Savings Ltd, registered in Scotland No: SC91859, registered office: 6 Albyn Place, Edinburgh, EH2 4NL.
Authorised and regulated by the Financial Conduct Authority.
Telephone: 0131 225 7781 | Email: info@thescottish.co.uk | Website: www.thescottish.co.uk

RUSS MOULD
AJ Bell Investment Director

Insightful commentary on market issues

Why the inflation debate is more than just hot air

What rising prices could mean for different asset classes

There is a general rule that the most vituperative arguments are those that take place between academics, because the stakes (and the implications for the real world) are so small.

Usually, such debates can be watched with detached amusement, but there is one current spat which does command attention, especially from an investment perspective.

Larry Summers – former US Treasury secretary under president Bill Clinton and former economic adviser to Barack Obama – is involved in a fierce set-to with current Treasury secretary and former US Federal Reserve chair Janet Yellen. To add spice to proceedings, Summers was reportedly an unsuccessful candidate when Yellen got the post at the US central bank in 2013.

Yellen is actively endorsing the Biden administration's fiscal stimulus plans, arguing that spending too little could do more harm than spending too much.

Judging by his columns in *The Washington Post*, Summers seems to disagree, in the view that too much stimulus could unleash inflation.

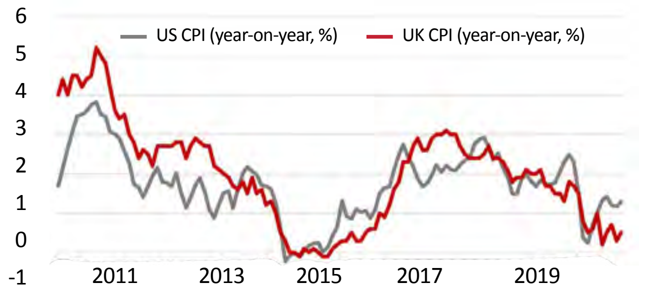
Yellen, perhaps conveniently ignoring how her four years as Fed chair employing ultra-loose policies employed by both her predecessor, Ben Bernanke, and her successor, Jay Powell, cannot point to any sustained progress in stoking inflation. She asserts that any such threat is being monitored and can be swiftly contained.

Cue much eye-rolling from Summers, whose antipathy to the quantitative easing (QE) policies used as 'temporary' measures by the Fed since 2008 is also well known.

If Yellen is right, then investment portfolios can stay slanted toward momentum and growth strategies and long-duration assets such as government bonds with a decade or more to maturity and technology and biotechnology stocks – in other words, what has a great track record over the last decade will keep delivering, if history is any guide.

But if Summers is right, then the whole game changes. If inflation pops higher and stays that way, then history suggests investors need to be exposed to short-duration assets such as 'value' equities (cyclical growth and recovery stocks), emerging markets and 'real' assets such as commodities and precious metals.

Inflation is low, but markets remain on a state of alert for its return



Source: Office for National Statistics, FRED – St. Louis Federal Reserve database

RUSS MOULD
AJ Bell Investment Director

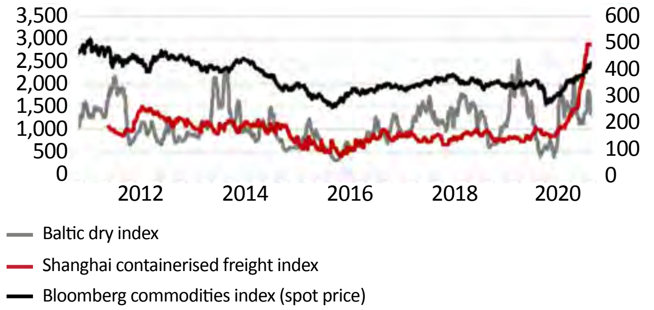
BASE EFFECT OR BOUNCE?

Again, the headline inflation numbers are benign. There will be a base effect for the rest of 2021, as the pandemic-induced recession comes up as a comparator.

Doubtless central banks will dismiss that as transitory rather than signs of a fundamental cost pressures, even if the price of vital raw materials from oil to metals and crops is on the march if the Bloomberg Commodity index and shipping's Baltic Dry benchmark are any guide.

If there is any good news here is might be that the Shanghai Containerised Freight index is maybe topping out after a stunning run, but all these trends are indicators of cost pressures building in the pipeline.

Commodities and transport costs could be hinting at inflation



Source: Refinitiv

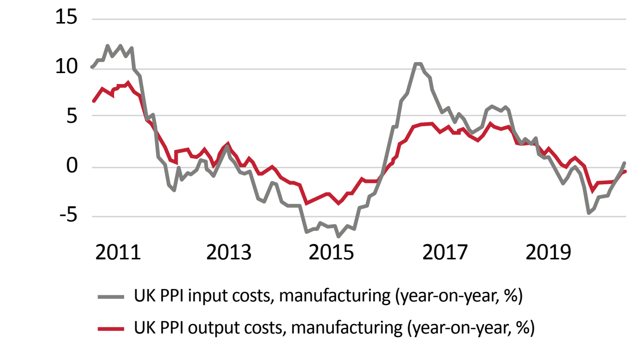
Companies are already paying attention – because they must. Input costs and output prices are showing some momentum in the UK, while American firms are flagging a sharp increase in their costs in the latest purchasing managers' indices.

Muted demand, owing to the pandemic, lockdowns and increased unemployment, could keep a lid on this trend but a strong bounce back at a time when supply is crimped by company closures and supply chain disruption remains a possibility, too.

FRETFUL FIXED INCOME

Fixed-income investors are paying attention because government bond yields are rising. They still stand at what are historically low levels, so it would be wrong to say bond investors are in a tizzy.

Companies are starting to notice higher costs in the UK ….



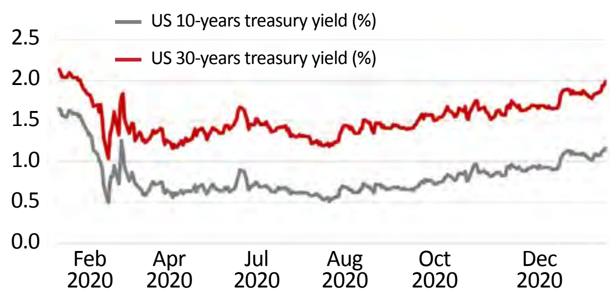
Source: Office for National Statistics

… and the US

Source: US institute for Supply Management

They still seem to believe the Yellen narrative that inflation can be managed and that central banks can just keep throwing money at fixed-income markets via QE to put a lid on bond yields. That would keep bond prices high but gilts' and treasuries' skinny yields would offer holders little or no protection if the inflation genie finally pops out of the bottle.

UK gilt yields are ticking higher, as are US Treasury yields



Source: Refinitiv

ADVERTORIAL

Schroders

Outlook 2021: **UK equities**

In terms of potential, the UK market for stock picking is comparable to the one that followed the Global Financial Crisis.

- ***Any mispriced opportunities for stockpickers.***
- ***Pick-up in M&A activity.***
- ***Companies are adapting following Covid-19.***

Introduction

If the job of stockpickers is to work out when the market is "mispricing" shares, then there is plenty for those with a focus on the UK to get their teeth into right now.

As investors look beyond events over which they have no control – such as Covid-19 and Brexit – opportunities abound at an individual stock level. Indeed, in terms of potential, today's market for stock picking is comparable to the one that followed the Global Financial Crisis (GFC).

This is at a time when many companies are looking to the future again and increasing investment. There has been some sensible bolt-on merger and acquisition (M&A) activity and many dividends are being reinstated. Plenty of companies have surplus cash to grow their businesses and reward their shareholders.

Investor confidence in the UK dropped away amid the pandemic. Having briefly re-engaged in late 2019/early 2020, global fund managers retreated back to the side-lines, according to regular investor polls by Bank of America Merrill Lynch.

As a result, UK shares are on track to lag other regions for yet another year. While the gap has recently closed a little following some positive vaccine news, the market is significantly trailing other regions year-to-date.

However, investors observe plenty of stocks whose prices are failing to properly reflect company prospects to sustain and grow earnings over time. Against this backdrop, two Schroders stockpickers explain how they're looking at the market heading into 2021.

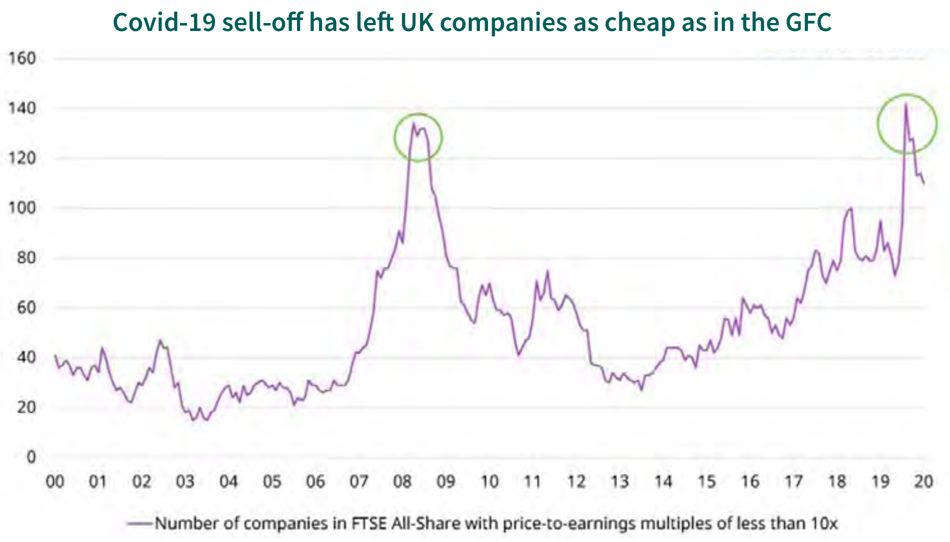
Sue Noffke, Head of UK Equities:

"The possible reasons for not owning UK shares have been extremely well publicised in recent years. We can currently see this with Brexit and the devastating Covid-19 crisis, which are both top of many investors' minds.

"The reasons for owning UK shares are much less well-known and have frequently been overlooked. It seems to me that the bad news is crowding out the good. This, in part, explains why there are so many mispriced opportunities at present.

"It's certainly good to see our optimism affirmed by other large and experienced long-term investors. This is apparent from the resumption of "inward" M&A activity as global deal-making has picked up again.

"The trend of inward M&A had begun to gather pace



Source: J.P.Morgan Market Intelligence team, data from August 2000 to August 2020. 521567

prior to the global pandemic (see Who's buying UK shares are what does it tell us?). We see many indications that it is starting to regain momentum.

"Recently announced deals include a recommended bid for RSA Insurance by a consortium of overseas rivals. Meanwhile, the eponymous owner of Las Vegas's iconic casino Caesars has seemingly prevailed in a heated contest for gaming group William Hill. This is as two North American rivals vie for control of security group G4S.

"This bid interest underlines the unloved status of many UK shares. A large number of companies are trading on very depressed price-to-earnings ratios (a commonly-used valuation metric), similar to the situation we saw in the wake of the GFC (see chart, above).

Companies back on track

"Since peak Covid-19 uncertainty around the time that the World Health Organization (WHO) declared a global pandemic in early March, we've seen many companies get back on track.

"Even before the positive news on potential vaccines, the companies we follow were looking ahead again. They were feeling sufficiently confident to give some guidance on their likely future financial performance.

"A number of these companies have also paid, or indicated plans to resume dividend payments deferred last spring.

Quintessential "exogenous" shock

"Many in the market had judged these dividends more vulnerable than they've transpired to be. Their reinstatement is a really good signal of corporate confidence, which may have been obscured by 2020's high profile dividend cuts.

"These cuts have been concentrated in the hardest hit sectors of banks, oil & gas, travel & leisure and other areas within the wider consumer services industry. Some dividends have been "rebased" to a lower level, as may also happen with the banks when they resume distributions.

"Other companies outside of these sectors have been less impacted by the pandemic. As a result confidence, and dividend payments, have been able to resume more swiftly than many had previously assumed possible or likely.

"Having said that, Covid-19 is the quintessential "exogenous" shock, one which arises from outside of the economic system, such as an extreme weather event. These shocks are less quantifiable than those which come from within, like the global financial imbalances which set the scene for the GFC.

"The acceleration of technological trends, changing consumer behaviours and the loss of demand as a result of the crisis will have long-lasting impacts.

"In some instances, these impacts may become permanent if it takes longer than expected to resolve the pandemic due to the many potential challenges which face vaccination programmes.

"These challenges could relate to manufacturing, storing and distributing a vaccine as well as levels of public uptake.

"This increases the risks around some of the worst-hit sub sectors, and underlines why valuations need to scrutinised in the context of company fundamentals.

"For this reason I'm avoiding some apparently cheap property companies (traditional retail/office), airlines and cruise operators within the travel & leisure sector.

Positives come back into focus?

"More broadly, markets could fall if expectations around vaccination programmes prove too optimistic.

"Global stock markets have recovered quickly since news of the vaccine progress. UK equities are global in nature, international developments often set the tone, and in this regard a number of uncertainties remain.

"If it does take longer than expected to resolve the pandemic, I'd expect the strongest companies with the strongest balance sheets to outperform.

"It's worth noting this scenario would not necessarily preclude UK shares in the broad performing relatively well. There are some country-specific factors at play here.

"Should, for instance, uncertainty around Brexit subside, it could create space for the UK stock market's positives to come into focus.

Strongest consolidate their positions

"The degree of negativity towards UK shares remains really quite entrenched. This is reflected in the extreme positioning of global fund managers.

"However, I'm glad to report that many of the companies we follow have unveiled new investment plans. I'm also seeing some sensible "bolt-on" M&A proposals to accelerate growth.

"I've already mentioned dividends, which in a number of cases have been reinstated on a progressive basis.

"In summary, many of the strongest companies have been able to consolidate their positions and are adjusting very well to the changes."

Andy Brough, Head of Pan-European Small and Mid Cap Team:

"Markets dislike uncertainty and, thankfully, we may have a bit of certainty heading into 2021 after an eventful 2020. In addition, I'm reasonably optimistic on the outlook for the UK economy and many of the domestically-focused small and mid-cap (SMID) companies exposed to it.

"It's not just the beneficiaries of the country's flourishing digital economy which are exciting me at present, but also plenty of the so called "old economy" stocks.

"Many of these businesses have cast aside entrenched behaviours and achieved years of change in a matter of months. That can arguably only be a good thing for their long-term profitability and the health of the economy.

Wages and salaries higher than pre-crisis

"It's easy to get gloomy and forget the positives during a global pandemic. It's worth pausing, however, taking a moment, and looking ahead to imagine what might happen when the economy restarts.

"News that UK gross domestic product (GDP) grew by 15.5% in Q3 2020 has been dismissed by some commentators as merely the product of pent-up demand. However, wages and salaries are higher now than they were in Q4 2019, which shows that government schemes are supporting income (albeit at a cost).

"The UK housing market is in very good shape, which gives me confidence in the underlying strength of the economy. Meanwhile, the retailers I speak to are really looking forward to the new year.

"The potential for 24-hour opening of stores for Christmas trading is a very interesting near-term development.

Surprising resilience seen by some sectors?

"You may be surprised to learn that UK retailers have broadly held their market values this year. The FTSE All-Share General Retailers sector has returned +0.5% in sterling terms year to date (total returns to close 18/11/2020).

"The sector is up 38% since the start of 2019, on the same calculation basis.

"We always felt that there was a gap between the perception of how retailers were trading and their actual performance (see Death of the High Street? Why we're still backing UK retail).

"This bounce back is a timely reminder that the job of stockpickers is to work out where the market is pricing incorrectly.

"Once Covid-19 restrictions are eased we could find the economy quickly comes back to strength, with entrepreneurial and animal spirits unleashed again. The recent pick-up in all variety of M&A activity augers well in this regard.

"I would also note that much of the recent recovery in deals involving UK companies (see above chart, which captures announced deals) has been driven by bids for SMIDS.

"In the past, SMIDs have attracted a relatively greater part of the M&A pie.

"Were we to see a strong economic recovery, we could see plenty of jobs being created and wages rising briskly. In this scenario the tax-take would be expected to rise to help pay down national debt.

For more information on investment trusts at Schroders, subscribe to our newsletter here.

Number of M&A deals with a UK target, 1991-present

Source: Thomson Reuters Datastream, Morgan Stanley Research, data from 1991 to November 2020. 521954

Important information:

This communication is marketing material. The views and opinions contained herein are those of the named author(s) on this page, and may not necessarily represent views expressed or reflected in other Schroders communications, strategies or funds.

Issued by Schroder Unit Trusts Limited, 1 London Wall Place, London EC2Y 5AU. Registered Number 4191730 England. Authorised and regulated by the Financial Conduct Authority.

BOOM TIME FOR **LUXURY GOODS**

Welcome to the Roaring Twenties where wealthier people will splash the cash

By **James Crux** and **Ian Conway**

Covid-19 vaccines are being injected into the arms of a grateful global populace, paving the way for a full reopening of the global economy, a rebound in intercontinental travel and an explosive release of pent-up demand.

The world could be entering a new 'Roaring Twenties' decade as fortunate individuals still with jobs are liberated from their homes and start to splash the cash saved during Covid hibernation.

In turn, the well-heeled among a vaccinated population may seek to make up for lost time by partying with wild abandon and spending big on premium or aspirational brands, boosting sales across the luxury goods sector.

Companies behind high-end, aspirational fashion brands or premium drinks brands are typically blessed with pricing power and high margins, enabling them to generate oodles of cash which can be used to fund acquisitions or progressive dividends.

LOTS TO LIKE ABOUT LUXURY

Investment bank Berenberg says the sector 'is not cheap, but luxury never is'. Investors have to pay up to access its attractive growth prospects, high barriers to entry, robust pricing power, strong cash generation and superior profitability compared to other consumer discretionary sectors, such as general retailers.

Yet the bank's analysts also argue that the recent de-rating of the luxury sector reveals interesting 'quality growth' opportunities. They say: 'Luxury has not been immune from the pandemic and near-term visibility is low. But, regardless of the shape of recovery, we believe medium term luxury demand will be largely unaffected, since all the long term structural drivers to long term demand remain fully intact.'

Moreover, Berenberg sees double-digit market growth to 2025 driven predominantly by China and digital channels, with conglomerates such as LVMH and Kering taking greater share of a market that remains highly fragmented. The bank's analysts expect the pandemic to accelerate mergers and acquisitions in the near term.

'Regardless of whether the recovery takes the near-term bull or bear case path – which

UK-listed stocks in the luxury space

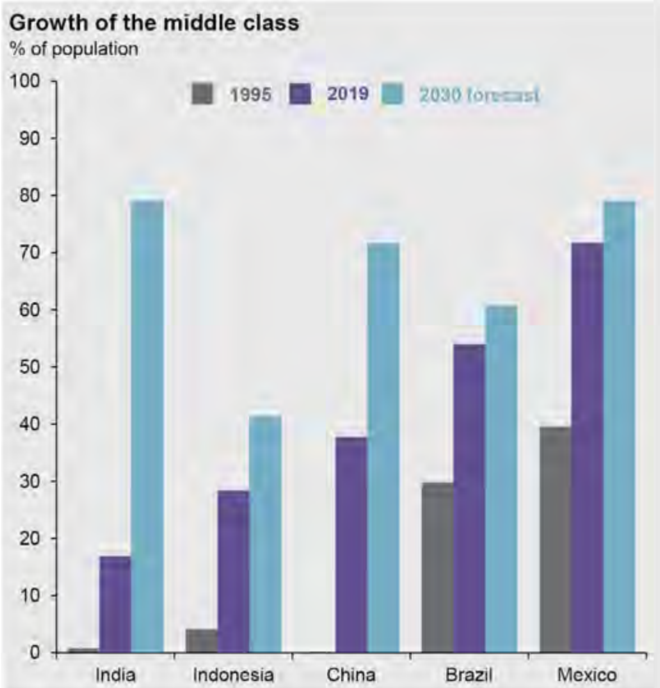
Investors can gain exposure to the luxury theme through London-listed stocks including **Burberry (BRBY)**, the trenchcoats-to-cashmere scarves seller that appears to be over the worst of the pandemic.

Famed for its iconic Equestrian Knight Device and the Burberry Check, the London-headquartered fashion house is blessed with a strong and enduring brand, and while third quarter sales dropped 9% on a like-for-like basis, efforts to reel back markdowns helped shore up profits.

Watches of Switzerland (WOSG) joined the UK stock market in June 2019 and has since seen its share price rise by 144%. The Rolex, Omega, TAG Heuer and Breitling watches retailer has coped well with the impact of lockdowns in both the UK and US thanks to strong online demand. UK online sales shot 121% higher year-on-year in the third quarter.

Also on the UK stock market is posh handbags maker **Mulberry (MUL:AIM)** where Mike Ashley's **Frasers Group (FRAS)** has built up a near-37% stake.

ultimately depends on the speed that tourism can recover – luxury demand will be largely unaffected by the pandemic on a five-year view, since all the underlying structural drivers to long-term luxury demand remain fully intact. Covid-19 has likely created pent-up demand, which will be a tailwind for future years as the luxury demand catches up,' adds Berenberg.



Source: JPMorgan Asset Management, Brookings Institute

These structural drivers are the growth of the Chinese middle class, the unstoppable rise of digital sales and the ascendancy of Millennials and Generation Z, the internet-savvy cohort that has been driving all the growth in personal luxury.

A TOUCH OF LUXURY

The global market in personal luxury goods was worth €281 billion in 2019, according to a study by consultancy Bain & Co with Europe accounting for €85 billion or around 30% of sales and the US being the single biggest country accounting for €75 billion of sales.

However, 2020 was a rude awakening for the sector with consumers cutting their spending in general, and spending on luxury goods in particular, because of the restrictions on international travel.

Sales are estimated to have shrunk by almost a quarter last year to €217 billion, the first drop in

Can you play the luxury theme via funds?

The answer is yes. The easiest way to play the space and get diversified exposure to lots of different luxury names is through exchange-traded fund **Amundi S&P Global Luxury ETF (LUXG)**.

This product tracks the S&P Global Luxury index which is made up of various companies involved in the provision or distribution of luxury goods or services, including LVMH, Daimler and Estee Lauder. We write more about this ETF towards the end of the article.

Alternatively, investors can get exposure through various funds and investment trusts that have stakes in luxury goods companies as well as other businesses which may not be related to this space.

For example, **GAM Multistock Luxury Brands Equity Fund (B637645)** has 7.3% of its portfolio in LVMH according to Fe Fundinfo.

Buy and hold investor Nick Train from asset manager Lindsell Train likes companies with luxury, premium or aspirational brands. His **Finsbury Growth & Income Trust (FGT)** holds cognac and liqueur maker Remy Cointreau, FTSE 100 constituent Burberry which he hopes will become a much bigger company in years to come, as well as spirits maker **Diageo (DGE)** which owns the Johnnie Walker, Don Julio and Casamigos brands.

Zehrid Osmani-managed investment trust **Martin Currie Global Portfolio (MNP)** invests in Kering, Italian luxury apparel brand Moncler and luxury carmaker Ferrari.

a decade and the biggest drop on record, taking the industry back to 2014 levels.

'The world has experienced a difficult year of rapid, unexpected changes and luxury has not emerged unscathed,' says Claudia D'Arpizio, partner at Bain & Co 'The industry has suffered from a pause in global travel and ongoing lockdowns, and a change in the way consumers shop and what they value.'

Sales in the first quarter of last year fell 22%, followed by a fall of 50% in the second quarter, the worst on record. However, third quarter sales are estimated to have fallen just 12%, and the range of forecasts for the fourth quarter is -5% to -20% with a base case of -10%.

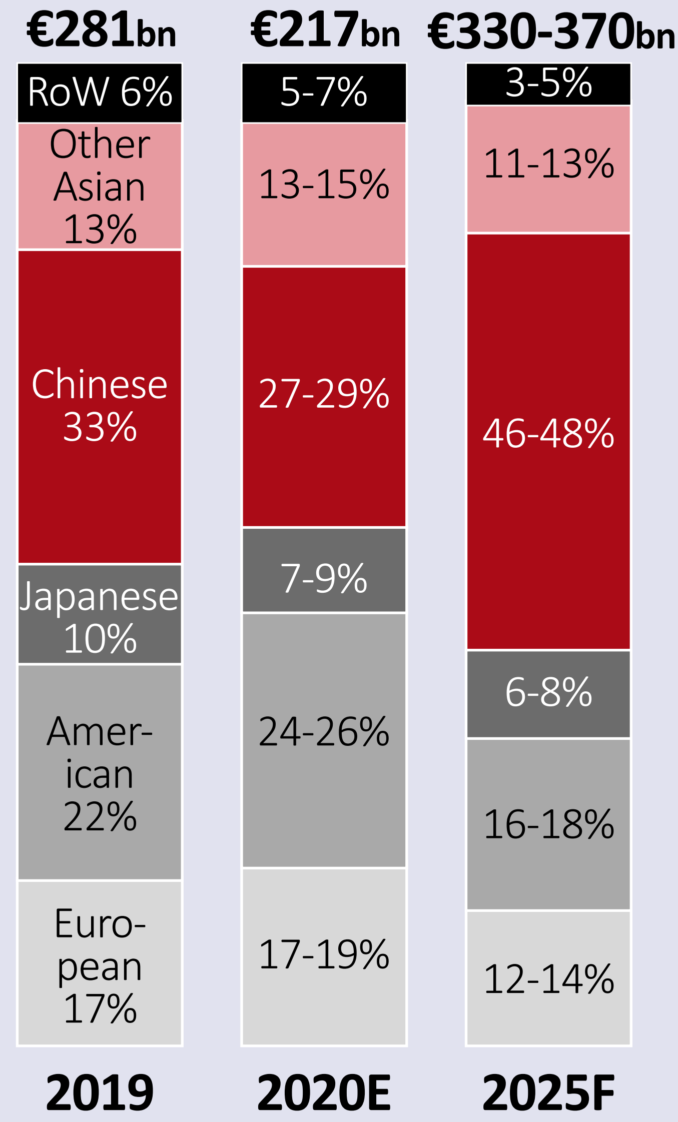
The impact on profits for the luxury sector has been brutal, with Bain & Co estimating a hit to 2020 operating profits of 60% and a decline in profit margins from 21% to 12% on average.

For 2021, the study sees a range of possibilities, from a 10% to 12% recovery in sales to a 17% to 19% recovery, depending on how fast the economy and particularly the travel industry return to something approaching normal, and also depending on consumer confidence.

The sector is not seen getting back to 2019's level of sales until late 2022 or early 2023, while profits are seen taking longer still to recover.

However, it is important to remember that the stock market is forward looking and will be pricing in an earnings recovery well before it happens, hence why the sector is ripe for investing now.

Personal luxury goods market by consumer nationality



Source: Consultancy.eu

US CONSUMERS TO DRIVE THE RECOVERY

As the largest single market for personal luxury goods, the strong position of US households bodes well for spending going forward.

The US accounts for 34% of global private consumption according to analysts at Morgan Stanley. The investment bank believes US household finances are 'as healthy as they have been in years' having entered the latest recession in a positive state with a stable debt ratio.

US consumer debt levels were the lowest in 11 years going into the pandemic, and in general they haven't risen so there is no need for balance sheet repair as there was following the great financial crisis.

Instead, the investment bank sees US consumers going on a huge spending spree this spring as the economy reopens thanks to the massive fiscal stimulus provided by policy makers.

MONEY IN THEIR POCKETS

While the recovery in the labour market has been uneven and households have lost roughly $400 billion in total income from April through November 2020, the administration has underwritten these losses in an unprecedented manner with transfers exceeding $1 trillion, according to Morgan Stanley.

In addition to this excess transfer of more than $600 billion, savings forced on consumers due to Covid-related restrictions helped US households amass around $1.4 trillion of savings as of November 2020.

A second round of stimulus payments of $1,400 per head is likely to push excess savings to $2 trillion very soon or the equivalent of 14% of personal consumer expenditure and 9% of GDP.

As vaccinations are rolled out in the spring and warmer temperatures have a downward impact on the number of new Covid cases, consumers will open their wallets, analysts believe.

To begin with, spending is likely to focus on going out, which is good for the foodservice and restaurant industry, hotels and casinos. Consumers will then likely turn their spending to durable goods such as clothing and footwear, beauty products, consumer electronics, home furnishings and luxury goods.

As hiring picks up again this should drive a virtuous circle of income gains and more spending, meaning growth could last into 2022, says Morgan Stanley.

CHINESE CONSUMERS TO SPEND MORE

A recovery in global consumer spending will have a two-fold effect on China, boosting demand for Chinese exports and increasing economic growth.

JP Morgan Asset Management's global market strategist Mike Bell forecasts a base case growth rate of 4.4% per year on average for the Chinese economy over the rest of this decade. While this may be slower than the last decade, it still means the economy could be 50% bigger than it currently is by 2030.

If per capita earnings also rise by 50% from $10,000 to $15,000, the multiplier effect on consumer spending would be enormous given China's population of 1.4 billion. Bell believes the Chinese middle class could rise from 40% of the population to more like 70% by 2030, which will be an enormous driver for luxury goods sales.

Mainland China was the only region to see growth in luxury sales last year, with consumption rising across all categories, channels and price points according to the Bain & Co study.

Analysts at Berenberg forecast double-digit annual growth in personal luxury goods sales driven predominantly by Chinese and online sales. The bank's proprietary survey of more than 4,500 Chinese consumers shows 'a clear willingness to spend more in 2021 and to travel as soon as borders reopen'.

THE STRONG ARE GETTING STRONGER

As several observers have noted, there is a clear trend among consumer goods companies towards scale and consolidation with the strong getting stronger in terms of market share and reach.

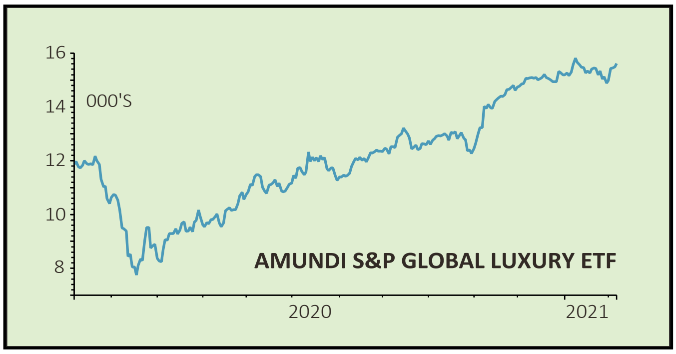
In the highly fragmented luxury sector, 'scale is winning with clear market polarisation as the "megabrands" continue to outperform,' says Berenberg.

French conglomerates such as LVMH and Kering have gained a larger piece of the pie over the last three years. Smaller brands within their respective stables have been able to leverage the benefits of scale they couldn't enjoy if they were standalone brands.

SHARES' TOP PICKS

BUY

Amundi S&P Global Luxury ETF (LUXG)
at £156.15



This is probably the easiest way for a UK investor to get diversified exposure to the luxury goods space.

The Amundi product is an exchange-traded fund tracking a basket of companies involved in the provision or distribution of luxury goods or services.

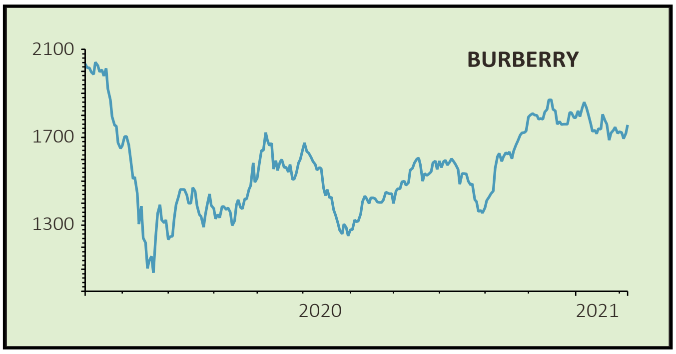
Buying the ETF will get you exposure to such names as LVMH, Kering, Hermes and Richemont, as well as luxury drinks providers Diageo and Pernod Ricard.

The portfolio also includes car companies Tesla and Daimler, and Nike which sells high-end collectable trainers as well as more affordable products.

The ETF has a 0.25% ongoing charge and returned 31.6% in 2020, according to Morningstar.

BUY

Burberry
at £17.27



A luxury 'mono brand' boasting strong heritage, Burberry's exposure to spending by globe-trotting, free-spending Asian customers proved a headwind at the height of the pandemic, derailing the momentum built under chief executive Marco Gobbetti.

In 2021 and beyond, the investment case hinges on a potential turnaround being led by creative director Riccardo Tisci and the continued economic comeback in China; encouragingly, Burberry reported strong third quarter growth in mainland China and Korea.

Burberry has an extensive store estate in China, coupled with a strong digital proposition. Berenberg believes there is clear scope to leverage the digital platform, which can support growth and margin expansion.

Even if the brand turnaround proves unsuccessful, downside is arguably limited by the fact Burberry is credible takeover target given its low relative valuation and less prohibitive ownership structure. The stock trades on 23.5 times forecast earnings for the year ending March

2022 and 20.7 times for 2023's estimates.

For the current financial year, Berenberg forecasts a 30% decline in adjusted pre-tax profit to £290 million, ahead of a 36% rebound to £396 million in 2022, rising to £449 million in 2023.

BUY

LVMH
at €498

French firm LVMH is the world's largest personal luxury goods company in terms of market share, owning many of the oldest and most iconic brands such as Louis Vuitton, Christian Dior, Loewe and Givenchy.

Despite playing on the heritage of its brands, the group – worth €251 billion – is also highly innovative and has the strongest momentum with consumers, according to Berenberg.

'Product innovation is critical to brand momentum and pricing power. The market tends to underestimate the growth potential of brands with accelerating brand "heat", so identifying inflection points in momentum is crucial,' the bank says.

As an investment, the business offers unparalleled scale and best-in-class execution, along with the financial firepower to continue consolidating and growing its market share, as shown by its recent acquisition of iconic US luxury brand Tiffany.

Fund manager Terry Smith recently invested in LVMH for the first time, adding the stock to his flagship **Fundsmith Equity Fund (B41YBW7)**.

Smith is a highly-discerning investor – his mantra is 'buy good companies, don't overpay, do nothing' – so the purchase is one that should make investors sit up and take notice. LVMH is a classic Fundsmith holding, as it is very profitable, enjoys high margins and benefits from strong brand loyalty.

The shares are listed on the Euronext Paris exchange under the code 'MC'. Investors wanting to own the shares will have to be comfortable buying overseas-listed stock and understand that this could come with some extra foreign exchange fees.

Disclaimer: Shares' Editor Daniel Coatsworth has a personal investment in Fundsmith Equity referenced in this article

LVMH consensus forecasts (€)

	2020A	2021E	2022E
Revenue	44.7bn	55.6bn	65.3bn
EBITDA	14bn	16bn	17.6bn
EBITDA margin	31.4%	28.8%	29.2%
Pre-tax profit	7.4bn	11.2bn	12.7bn
PE	49.8	33.5	28.1
Dividend yield	1.2%	1.5%	1.7%

Source: Reuters Eikon, Berenberg

Why we got it wrong on Lloyds, Cineworld and Ricardo

We revisit some older investment ideas to learn some valuable lessons from our mistakes

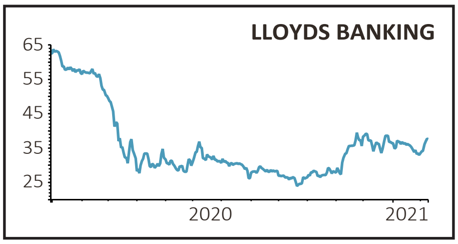
Investing successfully is hard. It takes discipline, courage and graft, and even with bags of these qualities, there will still be mistakes and misjudgments.

Some of the most successful investors, such as Warren Buffett, Peter Lynch and Jim Slater, all made bad calls through their long careers but what separates these people from many ordinary investors is the willingness and open-mindedness to learn from their errors.

Here we take a look at three of our own bad calls between 2018 and 2020 in *Shares* – **Lloyds (LLOY)**, **Cineworld (CINE)** and **Ricardo (RCDO)** – and try to draw out what we got wrong and the lessons we have learned.

LLOYDS

Our buy call on Lloyds was a very good example of how big picture factors can trip up an investment.



Our thinking in December 2019 was that Boris Johnson's election victory would result in an end to the political rollercoaster that Britain had been riding and that stability in Government and far more certainty around Brexit would make UK stocks more attractive.

We felt that banks had done a good job at repairing their balance sheets during the decade since the financial crisis, and with an assumed dose of interest rate rises, the backcloth looked hunky dory for UK banks and Lloyds.

'If they can generate stable profits and pay those profits out as high dividends, I think that will win them some fans among investors,' said fund manager Alastair Mundy at the time, comments that emboldened our own bullish view.

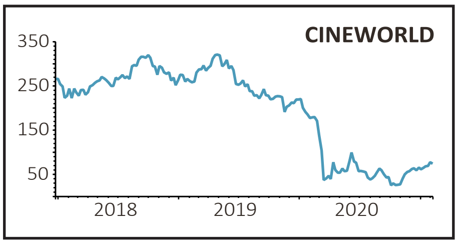
Sadly, these assumptions were wide of the mark. What we actually saw was a dragged-out pig's ear Brexit which led to investors continuing to give UK equities a very wide berth and stalling any hopes of a stock market recovery.

Covid also threw a grenade into the mix sending interest rates to all-time lows for what increasingly looks like a prolonged spell.

Compounding the investment mistake, while we ran extensive coverage of these wider issues throughout 2020, we failed to take our own advice on Lloyds, putting us well behind the curve and letting the stock clock up enormous losses – we ultimately cut the stock loose but not until September 2020, far too late. We will be more hands-on in similar situations in the future.

CINEWORLD

In May 2018 we said to buy the shares at 264.4p, encouraged by a strong slate of new movies and the belief that US expansion would quickly yield benefits.



Management told us that the inherited Regal estate in the US was underinvested, so Cineworld would spruce up the foyers and auditoriums and make them nicer places to visit. This model worked in the past and so we believed it would work again.

We were also told by management that the debt would be quickly paid down. While the investment idea did well for quite a while, we compounded what was ultimately an error by failing to react quickly when red flags started to appear.

We regularly warn readers not to be tempted by heavily indebted businesses, yet we ignored that advice ourselves here. The share price was already sliding when Cineworld revealed plans to make another major acquisition, this time in Canada.

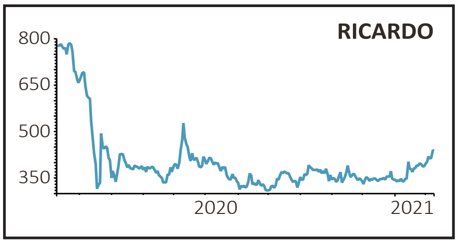
We should have immediately revised our view on the stock because the company's debts were already big without taking on more borrowings to help fund another multi-billion-dollar acquisition.

Cineworld got too greedy with its growth aspirations. The deal ultimately fell apart as Covid-19 struck and investors found out what happens when a heavily indebted business experiences a sudden downturn in trading – namely a share price collapse.

We were also guilty of allowing our emotions to get in the way of the investment decision. While we enjoy the cinema as a fun night out, we perhaps failed to appreciate that a cinema's takings are only as strong as the films it is showing, so when a weaker film slate in 2019 emerged, we didn't pay close enough attention.

RICARDO

Some might consider us unfortunate with Ricardo, with the extent and impact of the pandemic hitting home with investors barely a month after our 'buy' call in January 2020.



But we must hold up our hands and accept that miscalculations were made from the off, not least the pace of change at the Sussex-based engineering consultant.

Yes, the company is expanding its remit into new markets, such as defence, rail, energy and environmental sectors, but it remains skewed to the motor industry.

Our assumptions that workloads in emerging business lines would offset declining auto industry exposure simply did not happen and the share price plunged to depths from which it has still to meaningfully recover.

Ultimately, Ricardo was forced to raise fresh funding at a dilutive discount and investors remain very concerned about the performance this financial year to June 2021 after November's comments that it will be 'materially more weighted towards the second half of the current financial year than in previous years', interpreted by many as code for a threat of missing forecasts.

By **Steven Frazer**
News Editor

Understanding your new 'Investment Pathways'

Explaining the options available under the new FCA-backed scheme

Hundreds of thousands of people who choose to keep their retirement pot invested while taking an income through drawdown will from 1 February be offered 'Investment Pathways'. The same is true of those who transfer a drawdown plan to a new drawdown provider.

This change, instigated by the Financial Conduct Authority (FCA), is significant and it is vital savers understand the new options available to them.

One of the central aims of these reforms is to reduce the number of people holding cash or cash-like investments for the long term and seeing the value of their money whittled away by inflation.

The FCA also wants more people to think about their investments when going into drawdown so they remain appropriate to their needs.

There are a few fundamental things you need to know about these Pathways options. Firstly, they aren't being presented to you based on your personal circumstances but rather offer very broad investment options based on four basic outcomes.

Secondly, they do not take into account your appetite for risk or withdrawal strategy in any detail and must therefore not be seen by as a replacement for engagement or seeking regulated financial advice.

Finally, responsibility for investment decisions continues to rest with you.

If you chose a Pathways fund you still need to check the risk level and objective of the fund is aligned with your needs and that you are comfortable with the charges you are paying in return for the service being offered.

If you enter drawdown - whether invested in Pathways or having chosen your own investments – you need to regularly review your investments to ensure they are delivering against your objectives and remain appropriate for your evolving personal circumstances.

WHY ARE INVESTMENT PATHWAYS BEING INTRODUCED?

The reforms are designed to help savers make better decisions on how to invest their drawdown fund and ensure they do not end up holding large portions of their pension in cash or cash-like investments over the long-term.

This is because the FCA is worried people who hold too much cash in their pension risk missing out on valuable investment returns and having the real value of their pension eaten away over time by inflation.

There will be no obligation on people to invest in Pathways, however, and many will prefer to choose their own investments to better meet their attitude to risk, retirement plans and long-term goals.

WHO WILL BE AFFECTED?

The new rules will impact people who do not take financial advice and choose to keep their money invested while taking an income in retirement ('drawdown').

This includes people who move all or part of their pension savings into drawdown, or people who transfer funds already in drawdown to a new provider.

WHAT WILL PEOPLE ENTERING DRAWDOWN OR TRANSFERRING TO DRAWDOWN EXPERIENCE?

If you enter drawdown or transfer to a drawdown account, from 1 February you will initially be given the option of:

1 choosing an Investment Pathway;

2 choosing their own investments; or

3 sticking with the investments they already have

If you choose your own investments or stick with the investments you already have, your 'Pathway' journey will come to an end.

If you choose the Investment Pathway route, pension companies will be required to offer you four Investment Pathway options. These will not be tailored based on your personal circumstances, but rather designed around four very broad retirement income objectives.

Pension companies will then offer an Investment Pathway fund depending on which option you have chosen.

The FCA has identified four very broad investment objectives to design the Investment Pathway options around

Option 1:

I have no plans to touch my money in the next five years

Option 2:

I plan to use my money to set up a guaranteed income (annuity) within the next five years

Option 3:

I plan to start taking my money as a long-term income within the next five years

Option 4:

I plan to take out all my money within the next five years

WHAT HAPPENS IF I DECIDE I WANT TO BUY AN INVESTMENT PATHWAY FUND?

This will depend on the approach taken by your provider. If an AJ Bell customer indicates they want to buy an Investment Pathway fund, they will then go through the normal process of being placed into drawdown.

Once in drawdown, you retain responsibility for purchasing your investments – including Investment Pathways funds.

Where an AJ Bell customer said they wanted to buy an Investment Pathway investment then doesn't – either keeping their money in cash or choosing different investments – they will be sent a reminder of their original choices.

However, as is always the case with do-it-yourself investments, it will be up to the individual investor to complete any transaction.

HOW MUCH WILL PATHWAYS INVESTMENTS COST?

Again, this will vary from provider-to-provider. AJ Bell Youinvest customers will be offered the following Pathways funds:

OPTION 1:

I have no plans to touch my money in the next five years

Fund

VT AJ Bell Balanced Fund (BYW8RX1)

Objective: To achieve long-term capital growth with a balanced approach between defensive assets such as cash, fixed interest securities, money-market funds and collective investment schemes following alternative strategies such as property and commodities, and higher risk assets such as equities.

Fund OCF: 0.34% plus platform charge of a maximum 0.25%

OPTION 2:

I plan to use my money to set up a guaranteed income (annuity) within the next five years

Fund

VT AJ Bell Cautious Fund (BYW8RV9)

Objective: To achieve long-term capital growth with a high level of exposure (often indirect) to defensive assets such as cash, fixed interest securities, money market funds and collective investment schemes following alternative strategies such as property and commodities and a low level of exposure to higher risk assets such as equities.

Fund OCF: 0.35% plus platform charge of a maximum 0.25%

OPTION 3:

I plan to start taking my money as a long-term income within the next five years

Fund

VT AJ Bell Income Fund (BH3W744)

Objective: To generate an income, whilst maintaining capital value over a typical investment cycle. It has a target average yield of 3-5% per annum (over a trailing three year period), which is not guaranteed. This is consistent with a goal of capital preservation and drawdown of an income.

Fund OCF: 0.74% plus platform charge of a maximum 0.25%

OPTION 4:

I plan to take out all my money within the next five years

Fund

VT AJ Bell Cautious Fund (see previous)

AJ Bell Youinvest's annual platform charge for funds is:

- 0.25% on the first £250,000 funds invested;
- 0.10% on the fund value between £250,000 and £1 million;
- 0.05% on the fund value between £1 million and £2 million;
- No charge on the fund value over £2 million.

WHAT HAPPENS IF I CHOOSE TO INVEST MY DRAWDOWN FUND IN CASH OR CASH-LIKE INVESTMENTS?

If you invest 50% or more of your new drawdown fund in cash or cash-like investments then your provider will check to make sure your have made an active decision to do that.

Your provider will also warn you that the fund is in danger of being eroded by inflation.

Where can I go for further information?

Pension Wise offers free and impartial Government guidance to people over 50 who have a personal or workplace pension and will cover Investment Pathways. The Money and Pensions Service will also be offering an Investment Pathways comparison tool.

If you want more bespoke help tailored to your individual needs you should seek regulated financial advice.

DISCLAIMER: The value of investments can go down as well as up and you may get back less than you originally invested. Target yields are not guaranteed and can fluctuate.

Shares magazine is owned and published by AJ Bell. The author (Tom Selby) owns shares in AJ Bell. Shares' Deputy Editor Tom Sieber who edited this article also owns shares in AJ Bell.

By **Tom Selby**
AJ Bell
Senior Analyst

Is there early pension access for the terminally ill?

A reader wants to know their options for both a workplace and state pension

I've just been diagnosed with a terminal illness and may not be around this time next year. I am 59 and have a workplace pension. Can I access these funds or my state pension early?
Anonymous

Tom Selby
AJ Bell
Senior Analyst says:

There are specific HMRC rules which, in certain circumstances, allow people in serious ill health to take their entire pension as a lump sum tax-free. For this to apply, a medical practitioner (e.g. a doctor) must confirm in writing that the individual has less than 12 months to live.

For someone to qualify for a serious ill-health lump sum they must also:

- Have funds that have not been 'crystallised' (this just means converted into a retirement income)
- Have available lifetime allowance (the lifetime allowance in 2020/21 is £1,073,100)
- Be in a scheme which allows a serious ill-health lump sum to be taken

If someone meets the criteria and it is a defined benefit (DB) pension they should speak to their scheme administrator to find out their options in the scheme. If it is a defined contribution (DC) scheme they should contact their provider so they can process the case.

It may be sensible to contact the scheme administrator before speaking to the medical practitioner, just to check whether they have any specific requirements which need to be met. For example, some providers ask the medical practitioner to sign a specific form confirming the position.

If someone has a DB pension, has not received confirmation from a medical practitioner that they have less than 12 months to live and has not reached their scheme's normal pension age they may be able to access their retirement income early, at a reduced rate. Again, they should speak to their administrator to find out if this is the case.

If it is a DC pension, the individual has not received confirmation from a medical practitioner that they have less than 12 months to live, and they are over 55, they have the option of accessing their fund flexibly – either via drawdown or ad-hoc lump sums (provided the scheme they are in facilitates these options).

In these circumstances a quarter of their fund will be available tax-free, while the remaining 75% will be taxed.

If it is a DC pension and the individual's priority is passing on money to loved ones after they die, they may want to consider leaving the pension untouched.

If they do this and die before age 75 the money can be inherited tax-free, while if they die after 75 it will be taxed in the same way as income when their beneficiary comes to withdraw it. Anyone going down this route needs to make sure their nominations are up to date so any funds left behind are inherited by the right people.

Unfortunately, the state pension cannot be drawn early in any circumstances. However, you may be entitled to other state benefits such as Statutory Sick Pay, Employment and Support Allowance or Universal Credit.

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 information 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.

Uncovering the secrets of company analysis

We use FTSE 250 meat producer Cranswick to show how a business can perform against its competitors

As our *First Time Investor* series draws to a close we put into practice everything we have learned so far and apply the principles and techniques to a FTSE 250 company. We have selected a business at random for illustration purposes only.

However, readers may be curious about how to go about finding investment ideas.

Professional managers often adopt a systematic approach by creating fundamentally based screens which sift through data like return on equity and earnings growth to identify suitable candidates for further research.

Valuation criteria like price to cash flow or price to earnings might also be used to zero on the most promising candidates.

Some fund managers even find ideas by following the top holdings of their peers.

In short, there are many ways to find your next investment idea but what you do with it is more important so let's get started.

We have chosen to look at **Cranswick (CWK)**, one of the UK's largest food producers.

The company's website provides a good overview of the business as well as presentations, reports and accounts, and regulated news announcements.

QUALITATIVE FACTORS TO CONSIDER

As we have highlighted in prior articles, investing is a long-term endeavour and its rewards are closely linked to the growth and stability of a company's cash flows and profits.

With that in mind, our primary goal is to find out if Cranswick has a viable business with durable long-term growth prospects.

If the business doesn't make enough profit to maintain its competitiveness, then long-term viability becomes questionable and it fails to satisfy our investment needs.

Successfully fending off competitors is essential in maintaining healthy profitability and returns on capital over long periods. This characteristic is a key factor in compounding shareholder returns.

WHAT DOES CRANSWICK DO?

The report and accounts say that Cranswick is an innovative British supplier of premium, fresh, and added value food products. The UK is the core market, but the company has been also been growing its export business over the last few years.

Feeding the nation should provide a durable business to companies that make good quality food that consumers desire, at the right price.

The biggest risk is that other companies do a better job and steal market share away from Cranswick.

The company operates from 15 well invested highly efficient production facilities in the UK. It owns pig breeders and a fully integrated chicken supply chain.

The company started out in 1975 as a group of farmers before moving into food production in the 1980s.

Cranswick provides its products to customers in food retail, food service and other channels.

The historical connection to the farming communities and operating a vertically integrated model has over time created competitive advantages.

These include good provenance, a secure supply chain as well as strong supplier and customer relationships.

Vertical integration means that Cranswick has control over the complete supply chain, from rearing animals to making and distributing the finished products.

WHAT IS CRANSWICK'S STRATEGY?

It's important to understand management's long-term vision and how they intend to reach their goals. The company has a three-pronged growth plan.

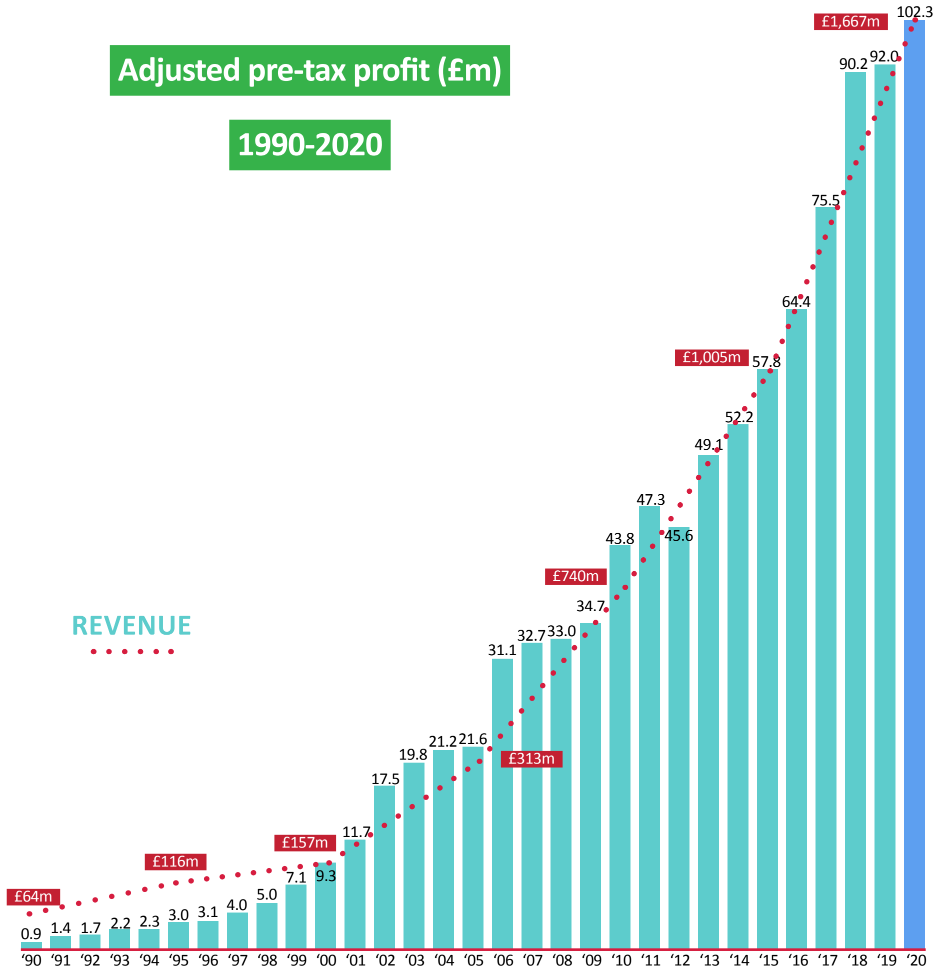
It aims to consolidate the existing market and thereby grow revenues from core pork products as well as investing in infrastructure to support growth

Expanding the product range and entering new markets and channels in the core UK market forms another leg of the growth plan.

Lastly the company intends to grow outside the UK by continuing to develop its export business.

This all seems to make sense and leverages Cranswick's core strengths of having well invested, efficient processing facilities.

It is noteworthy that operational excellence and sustainability also feature in the strategic pillars.



Source: Cranswick

Larger scale allows Cranswick to invest more heavily in state-of-the-art equipment which improves quality and efficiency, providing a competitive advantage. The big unknown is the durability of the advantage.

BIG PICTURE

How well the strategy has worked out over the last several years can be seen by the long-term chart that Cranswick provides in its annual report.

Over the last 30 years the company has grown adjusted pre-tax profit from £0.9 million to £102.3 million, equating to a compound annual growth rate of 17% a year, or 114 times the starting value.

The company has an unbroken track record of dividend growth, averaging around 10% a year.

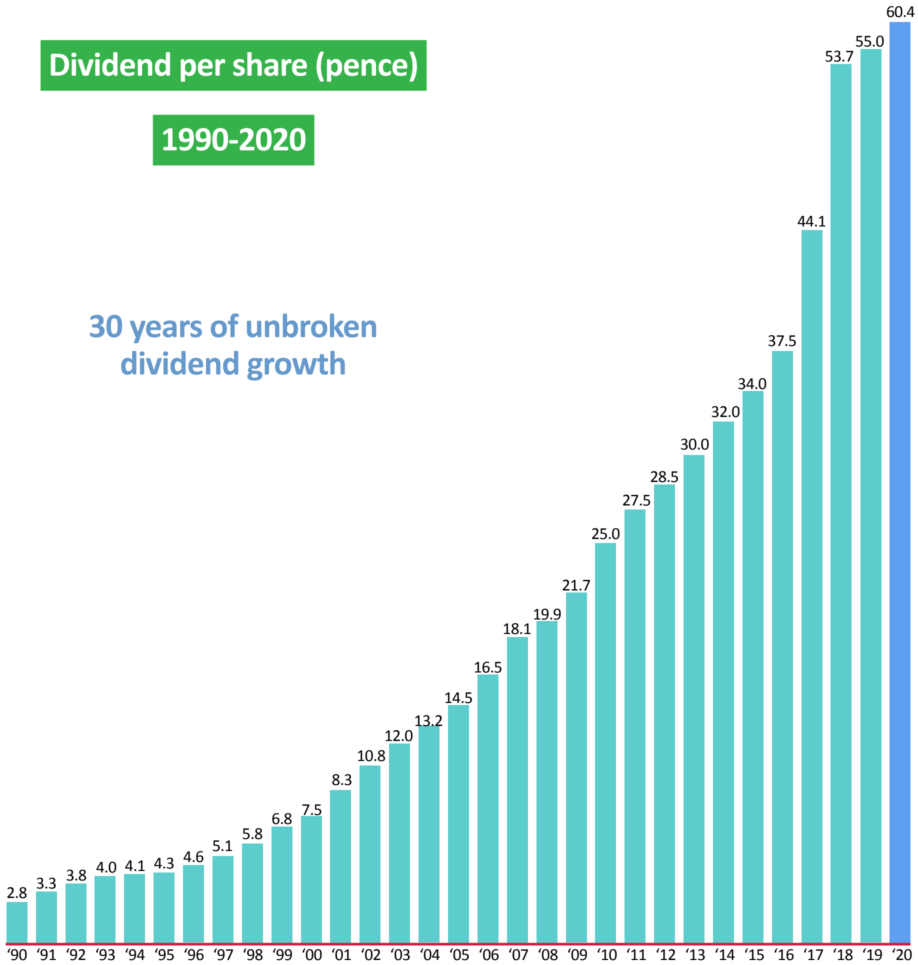
Over the last five years return on equity has averaged around 15% a year, showing that the business makes a healthy economic return.

In other words, the strategy of consolidating the market through bolt-on acquisitions and organic growth seems to be working.

Increased scale has allowed Cranswick to spend more on its facilities to make them more efficient and flexible, creating a positive feedback loop.

As we have highlighted in this series, profit is more reliable when backed by cash flow, so let's see how Cranswick does on this score.

Over the last 10 years the



Source: Cranswick

Cranswick Cash Flows

	2010-2020
Cash Generated from Operations (£m)	767
Operating Profit (£m)	718
Capital Expenditures (£m) A	457
Depreciation (£m) B	254
Growth Capital Expenditures (£m) A-B	203
Incremental Operating Profit (£m)	61.0
Return on Incremental Investment (%)	30%

Source: Stockopedia, Refinitiv

company has generated £767 million of operating cash compared with reporting cumulative operating profits of £718 million. This indicates the reported profit is backed by real cash.

What is impressive is the amount of investment that Cranswick ploughs back into the business to meet future growth and maintain asset quality, something which makes it tough for smaller food producers to compete.

Last year net capital expenditures represented nearly 6% of revenue.

The company has cumulatively allocated £457 million to capital expenditure over the last decade.

We can deduct depreciation from capital expenditures, on the basis that this represents 'maintenance capital expenditures' which is needed to maintain operations. What is left is the spend related to growth.

We can then compare the additional operating profit that the growth produced in order to calculate the incremental return on investment.

As the table shows Cranswick generated a 30% return on the investments made over the last decade which is very impressive.

Think about it as an owner of the business for a second and you will see that reinvesting back into the business has been an intelligent use of capital.

On this basis, investors should be cheering every time Cranswick identifies new capital investment projects.

CAPITAL ALLOCATION CRUCIAL

As we have pointed out in this series, management's capital allocation decisions are very important in determining future shareholder returns.

In Cranswick's case shareholders have also had the good fortune to receive growing dividends over the last 30 years.

In part two we will make a stab at estimating future shareholder returns assuming Cranswick can maintain the same level of growth and returns on capital.

We shall also take a closer look at how the business is financed and the balance sheet strength.

By **Martin Gamble**
Senior Reporter

INDEX

KEY ANNOUNCEMENTS OVER THE NEXT WEEK

Full year results

16 February: Glencore. **17 February:** British American Tobacco, Plus500, Rio Tinto. **18 February:** Barclays, Indivior, Primary Health Properties, Smith & Nephew.

Half year results

15 February: City of London Investment Group, Grit Real Estate Income. **16 February:** BHP, Blancco Technology, Pan African Resources, Petra Diamonds. **17 February:** Transense Technologies. **18 February:** Hays, Wilmington.

Trading statements

15 February: Vodafone. **16 February:** Marston's, Safestore.

WHO WE ARE

EDITOR: Daniel Coatsworth @Dan_Coatsworth

DEPUTY EDITOR: Tom Sieber @SharesMagTom

NEWS EDITOR: Steven Frazer @SharesMagSteve

FUNDS AND INVESTMENT TRUSTS EDITOR: James Crux @SharesMagJames

SENIOR REPORTERS: Martin Gamble @Chilligg; Ian Conway @SharesMagIan

REPORTER: Yoosof Farah @YoosofShares

CONTRIBUTORS Laith Khalaf, Russ Mould, Tom Selby

ADVERTISING
Senior Sales Executive
Nick Frankland
020 7378 4592
nick.frankland@sharesmagazine.co.uk

PRODUCTION
Head of Design: Darren Rapley
Designer: Rebecca Bodi

CONTACT US:
support@sharesmagazine.co.uk

All chart data sourced by Refinitiv unless otherwise stated

Shares magazine is published weekly every Thursday (50 times per year) by AJ Bell Media Limited, 49 Southwark Bridge Road, London, SE1 9HH. Company Registration No: 3733852.