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PLUS

THE FUTURE FOR **BITCOIN** AFTER SELL-OFF

THE **EASY WAY** TO INVEST IN PROPERTY

THE TOP PERFORMING **VALUE FUNDS**

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CFA UK Publication of the Year CFA UK Journalism Awards 2019

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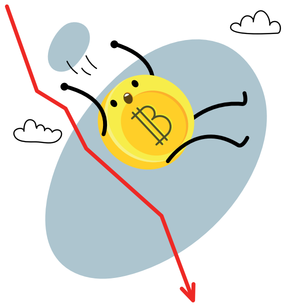
Bitcoin's entry into the mainstream is proving short-lived



Blockchain – the technology which underpins the cryptocurrency – may be more durable

For a time, bitcoin became just too big to ignore, with the cryptocurrency reaching all-time highs above $64,000 in April. When the price of an asset increases six-fold in a matter of months people are bound to sit up and take notice.

Amid signs that institutional investors were warming to the cryptocurrency, which also had a prominent and vocal fan in the form of Telsa founder Elon Musk, its entry into the mainstream of investing was looking increasingly assured.

The picture now looks a little different. Recent tweets from Musk, and his U-turn on accepting the cryptocurrency as payment for Tesla cars on environmental concerns, saw bitcoin's price drop by a third from its highs.

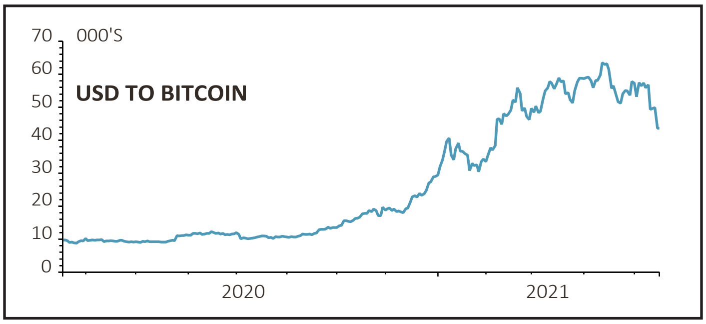
Even if Musk's subsequent denial that Tesla had divested its recently acquired holdings in bitcoin helped stem the bleeding, the simple fact that an individual tweeting about an asset could lead to such high levels of volatility helps explain why some institutions are publicly questioning bitcoin's investment credentials.

Ruffer was one of the first big asset managers to reveal it was investing in bitcoin back in November 2020 and it has reportedly begun exiting a position which it largely justified as complementing its holdings in gold.

While bitcoin may have been seen in some quarters as an alternative to the precious metal's role in protecting against inflation, gold's credentials in this area are much more long-standing.

LACK OF VISIBILITY

It is still too soon to make definitive judgements on what will happen to bitcoin over the longer term, particularly given the role regulation might have to



play. Even apparent fans of bitcoin accept the lack of visibility.

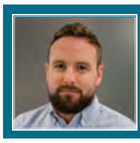
Florian Ginez, associate director, quantitative research at WisdomTree, says: 'As a new asset class, any development that may affect the outlook for adoption can have a sharp impact on price. The future looks bright for cryptocurrencies but deciphering the exact path of adoption is almost impossible.'

Blockchain, the infrastructure underpinning bitcoin, could ultimately prove more interesting in the long term. It is a verifiable electronic ledger for recording transactions and tracking assets in a business network, which could be anything from a tract of land to a key piece of intellectual property.

It provides instant and transparent access to information but is encrypted so it can only be accessed by sanctioned members of a network and cannot be modified.

Up until now there have big claims for blockchain's use in a variety of applications from finance to manufacturing and agriculture but little sign of tangible progress, partly because the process is intensive and expensive.

However, with major corporations like Amazon and JPMorgan recently announcing expanded footprints in this area, progress with blockchain could gather pace over the coming decade.



By **Tom Sieber** Deputy Editor

Indian Covid strain a threat to hospitality and travel sectors

Improved sentiment towards the UK could be affected if rising cases derail reopening

A big story of the first four-and-a-bit months of 2021 has been a recovery for UK assets with the domestic-facing FTSE 250 index reaching all-time highs and sterling recently hitting $1.42 against the dollar for the first time since 2018.

Sentiment towards the UK has been boosted by the successful vaccine rollout and the steady easing of coronavirus restrictions.

However, there are now fears that the Indian variant which chief medical officer Chris Whitty has confirmed is more transmissible than the Kent variant, could jeopardise the timing of a move to the final step on the roadmap and a full reopening of the economy, potentially undermining the recovery.

That could be a particular problem for the leisure, hospitality and travel sectors where shares have made an impressive recovery since the start of the year.

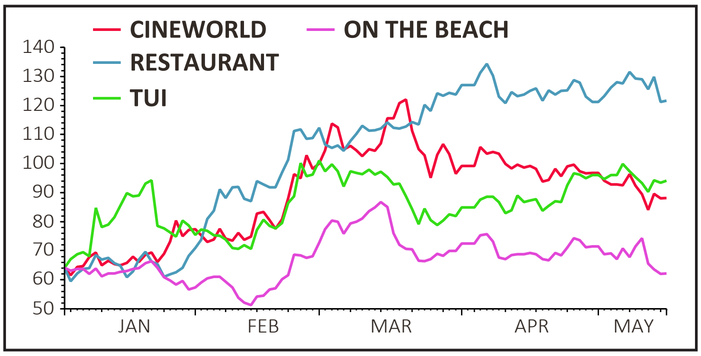
Performance hasn't been entirely based on hope either, with several trading updates showing stronger than expected trading when bars and restaurants could operate outdoors from 12 April. This suggested strong pent-up demand, despite unseasonably cold weather experienced throughout April.

Shares in premium bar operator **Revolution Bars (RBG:AIM)**, **Cineworld (CINE)**, **Fulham Shore (FUL:AIM)** and **Restaurant Group (RTN:AIM)** have all roughly doubled over the last six months.

Meanwhile, the emergence of the Indian variant could slow countries transitioning to the UK Government's travel green list, including popular destinations like Spain, Greece and Turkey which are all on the amber or red list, and is something that could impact some travel firms more than others.

Tour operator **Jet2 (JET2:AIM)** and online package holiday provider **On The Beach (OTB)** seem to have been vindicated by their more cautious view in anticipation of lower demand and restrictions potentially staying in place longer than expected, with Jet2 not restarting holidays until 24 June and On The Beach not taking bookings for holidays before 31 August.

Firms which seem more likely to be impacted are **TUI (TUI)** and budget airline **EasyJet (EZJ)**, who have started selling holidays from 17 May to amber list countries, with the latter saying it would let people 'make up their own mind about their holiday'.



TUI has been particularly bullish on the outlook for holidays this summer with plans to operate at 75% of its summer 2019 capacity, perhaps reflected by its need to bring in as much as cash as possible.

The latest setback brings the share gains over the last six months into question with TUI and EasyJet up 72% and 30% respectively while Jet2 shares are only up 3% and, On The Beach, has seen its shares fall 6%. [MG]

UK stocks slump as inflation doubles in April

Stocks have tumbled as prices look set to run higher in 2021

Inflation concerns have dominated stock markets and UK figures on 19 May show, as economists have feared, it's making a comeback.

Consumer inflation in the UK rose from 0.7% in March to 1.5% in April ahead of the 1.4% forecast. Although this has been mainly down to one-off influences like rising energy and clothing prices, expectations are that inflation will continue to run higher.

While the figure itself isn't of concern at the moment and is lower than the Bank of England's 2% target, it's the speed of jump which suggests inflation could reach that target in just a couple of months, and has investors concerned with the FTSE 100 tumbling 1% shortly after April's inflation numbers were revealed.

What stock markets are most concerned about is that we could be entering a period of abnormally strong demand which, as excess supply is used up, will naturally lead to higher inflation and with it, erode consumers' purchasing power and reduce expectations of corporate earnings growth.

Concerns about rising prices have led to a number of stock market sell-offs in recent weeks as investors position themselves for when central banks, including the US Federal Reserve and Bank of England, start tapering off support for the economy through quantitative easing and near-zero interest rates.

A survey of fund managers by Bank of America showed that inflation is seen as the biggest risk in markets with expectations remaining elevated, as 82% of respondents polled in April believe inflation is set to rise over the coming 12 months, not much below the record 94% reached in March.

UK CPI more than doubles in April to 1.5%

Stocks fell earlier in May, and at the same time safe-haven asset and well-known inflation hedge gold reached its highest level since early February, after data showed US consumer price inflation rose 4.2% year-on-year in April, its highest level of growth since 2008.

It remains unclear if April's figures are the result of one-off industry shutdowns, and there are doubts among some in the finance world whether inflation is here to stay or not. But commodity markets can be good signals of consumer inflation down the road and with the surge in prices they've been flashing warning signals for months.

This is because as commodity prices rise, they seep into factory gate (or producer) prices as companies see their input costs rise, and then the same businesses increase their prices to preserve profit margins and that's when consumers start to feel the effect.

Copper and iron ore – two metals seen as bellwethers for the global economy because of their wide range of uses – reached all-time highs earlier in May as the reopening of economies led to markedly higher demand, particularly from China, with supply failing to keep up. [YF]

This year's UK IPOs reward investors despite Deliveroo and Alphawave flops

On average you would have made good money by backing newly-listed companies

Coming just six weeks after shares in food takeaway platform **Deliveroo (ROO)** dropped more than 30% on its first day as a public company, the negative reaction to chip designer **Alphawave IP's (AWE)** market debut – down 10% in a day – has lead to wider concerns about London's merits as a listing destination and the quality of new companies joining the market.

However, these prominent disappointments do not reflect a wider picture of decent gains for recently listed firms. *Shares* has crunched the numbers on those firms that conducted a London IPO (initial public offering) since the beginning of 2021 and there has been an average 28.3% gain on the price at which the shares were first offered to investors.

Retail investors had to wait for most of these stocks to start trading before they could buy, but even if you take each stock's opening price on day one the average subsequent gain is close to double digits at 9.8%. That is good, but it also shows how retail investors are still at a disadvantage to institutional investors.

Hopes were high for Alphawave's listing given the similarities between the business and former market darling ARM, which was snapped up for £23.4 billion by Japanese investor Softbank in 2016, and the strong dynamics behind the global microchip industry as supply struggles to keep up with demand.

Like ARM, Alphawave licences out designs which other chipmakers use as the basis for their products and it then earns a royalty every time a device is sold. This asset-light model, with few demands on capital, should enable strong margins and cash generation and if ARM is any guide be rewarded with a premium market valuation.

However, Alphawave may have priced itself too high ahead of its debut. At the issue price of 410p the business was valued at £3.1 billion. This compared with the latest annual sales of $44 million, operating profit of $24 million and cash flow of $15 million.

The company was also a victim of poor timing – its first day of dealing on 13 May coincided with a bad day for technology stocks as market fears over inflation began to spiral. [TS]

UK NEW LISTINGS PERFORMANCE YEAR-TO-DATE

Company	Gain/loss now vs IPO price (%)	Gain/loss now vs opening price on first day (%)
Top performers		
Nightcap	160.9	148.5
Caerus Mineral Resources	140.5	109.1
Cornish Metals	107.1	48.7
MGC Pharmaceuticals	95.9	38.1
Auction Technology	63.2	33.2
Roquefort Investments	58.0	31.7
Amte Power	56.0	13.8
Tinybuild	55.9	21.1
Darktrace	44.9	3.8
Cellular Goods	41.4	-64.7
Bottom performers		
Parsley Box	-9.0	-11.6
Alphawave	-10.7	-10.7
Team	-11.4	-10.9
Cizzle Biotechnology (floated as Bould Opportunities)	-26.5	-36.1
Deliveroo	-38.7	-27.7
AVERAGE OF ALL 2021 IPOS	28.3	9.8

Source: London Stock Exchange, Shares, Google Finance, data to 18 May 2021.

Is good news on the UK property surge now priced into housebuilders?

Moving house and doing up existing ones adds to shortage in materials, skips and even hire vans

The muted reaction to a positive update from housebuilder **Vistry (VTY)** on 17 May suggests the market has already priced in the current buoyant property sector conditions and may be concerned about their sustainability.

In the wake of the pandemic there has been booming demand for UK houses and a parallel boost for the repair, maintenance and improvement market.

The latest report from estate agency portal **Rightmove (RMV)** showed the average price of houses coming to market between mid-April and mid-May hit an all-time high of £333,564.

That's a jump of £5,767 or 1.8% in just a month. Between mid-March and mid-April, prices had already jumped £6,733 or 2.1%.

The surge in demand has been partly fuelled by the Government's decision to remove stamp duty on house purchases up to a value of £500,000 until the end of June. After that, there is no duty on the first £250,000 until the end of September. The question is what happens after that date, particularly if there is an increase in unemployment.

Not only are prices at an all-time high but transaction volumes are also at record levels with the time taken to sell a house at an all-time low. 'Family homes with three bedrooms or more are like gold dust in many areas of the country, especially in parts of the north,' says Rightmove's director of property data Tim Bannister.

For example, there is less than half the available stock of three bedroom 'second-stepper' houses in the North East compared with 2019. Nationwide, in March almost a quarter of homes with a sale agreed had been on the market for less than a week.

COST PRESSURES

The feeding frenzy in house buying has led to spiralling demand for repair, maintenance and improvement, which in turn has led to a shortage of builders' vans, scaffolding and skips.

On top of this, Brexit and supply chain issues have led to a severe shortage of certain building materials and a spike in prices. Softwood timber has almost doubled in six months, steel joists have gone through the roof after an 80% increase in iron ore prices, and roof tiles are almost unobtainable.

According to the Chartered Institute of Procurement and Supply, building material costs are rising at the fastest pace since it began tracking them in April 1997.

This could threaten the profitability of housebuilders and construction materials firms at a time when they are seeing bumper demand.

As investment Berenberg comments: 'The large housebuilders maintain long-term procurement agreements with longstanding suppliers and, as such, while there will be some challenges in availability, that is mainly a problem for SME (small to medium sized) builders. However, price inflation does impact them.' [IC]

Buy Shield Therapeutics as it stands on cusp of US breakthrough

Iron deficiency drug Accrufer could generate hundreds of millions in revenue in the coming years

Specialty biotech company **Shield Therapeutics (STX:AIM)** is at an exciting point in its development and is worth buying before the market switches on to its full potential.

It is due to launch its proprietary iron deficiency drug Accrufer into the US market at the beginning of June 2021, after raising fresh equity of £29.2 million in March.

The product is a novel, low dose oral iron replacement therapy with patent protection until 2035. Existing non-oral solutions have the drawback of being administered intravenously, making them less attractive to patients and more costly to hospitals.

Competing existing oral solutions are heavily salt-based iron compounds with poor tolerability in the gut and low patient compliance.

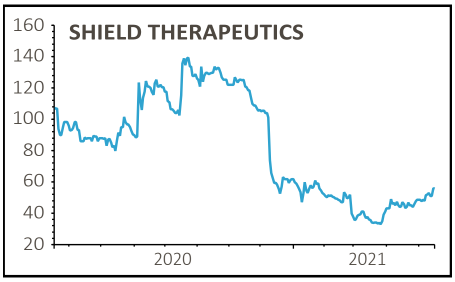
Based on management and third-party projections the company expects to generate $100 million of revenues from the third year after launch and reach $300 million-to-$400 million of revenues by years four and five.

Based on estimates from Finncap, the assumptions imply the product taking around 10% market share by year five, which doesn't look too aggressive.

Management numbers assume gross margins around 90% (the company pays a 5% royalty to Vitra) and annual sales and general marketing costs of $40-million-to-$45 million a year which results in projected free cash flow of around $225 million in five years. (£160 million)

SHIELD THERAPEUTICS
BUY
(STX:AIM) 55.9p

Market cap: **£110 million**



The key risks are skewed towards effective execution of the US commercial roll-out rather than efficacy of the product. With the business priced at £110 million, the risk to reward looks very attractive.

INVESTORS HAVE HAD TO BE PATIENT

The US Food and Drug Agency originally approved the product in 2019 when the shares were trading around 180p. The company has spent just over a year looking to attract the right partners to commercialise and distribute the product, which ultimately resulted in no progress, putting pressure on the share price.

Two withdrew for reasons unrelated to the product, but during the course of negotiations with other interested parties Shield generated insights in how they were planning to commercialise the product.

Eventually Shield ended up hiring four US executives who were employed by one of the players looking to license from Shield.

European partner Norgine will market the product (called Ferracru outside the US) in Europe, Australia, New Zealand and Scandinavia. Sales began in Belgium in January 2021.

The product has regulatory approvals in Europe and the US while partner ASK Pharm will market the product in China, Hong Kong, Macau and Taiwan once it gets approval, expected sometime in 2023.

WHAT IS IRON DEFICIENCY?

Iron deficiency anaemia is a condition where the blood lacks adequate healthy red blood cells, which carry oxygen around the body. As a result, sufferers often report that they are tired and short of breath.

Hill & Smith set to cash in on US infrastructure boom

New chief executive has the pedigree to drive growth and a re-rating of the shares

HILL & SMITH
BUY
(HILS) £15.20
Market cap: £1.25 billion

As president Biden's team begins what are likely to be weeks of horse-trading with their Republican peers over the shape and size of the new infrastructure plan, one firm which is set to benefit is FTSE 250 road safety equipment supplier **Hill & Smith (HILS)**.

A new chief executive has the ability to drive earnings growth and a loftier valuation, providing a double win for investors.

SPEND, SPEND, SPEND

Whether the Biden team try to go it alone with their $2.25 trillion plan, which needs significant tax rises, or there is a compromise with the Republicans – who have opened negotiations with an offer of $800 billion to $900 billion and no tax rises – the one area both parties agree is in dire need of increased investment is America's physical infrastructure.

According to Goldman Sachs's senior investment strategist Abby Joseph Cohen: 'The US has really fallen behind in terms of its infrastructure spend. The federal budget used to be 5% of GDP, now it's half that. And at a state and local level, budgets are strained so they cut back on things voters tend not to notice, like spending on roads and pipelines.'

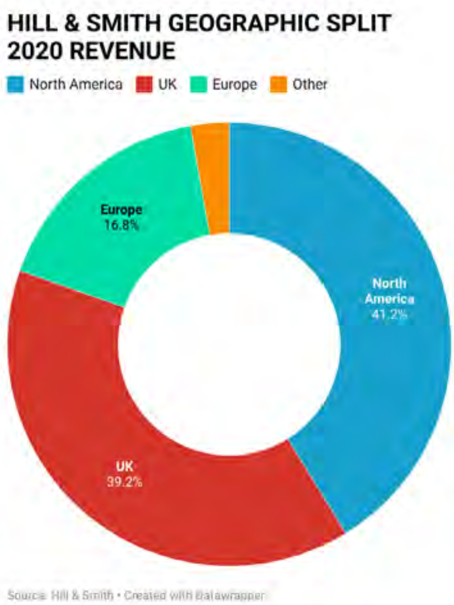
Total engineering and construction spending in the US only fell 1% last year, according to FMI Corp's *2021 Engineering and Construction Industry Overview*. However, this figure was severely skewed by residential construction which saw an 8% rise in building single-family homes and a 10% rise in spending on renovations, while some non-residential sectors saw a fall of up to 17% in spending.

The American Society of Civil Engineers recently scored the level of US critical infrastructure at C minus, noting that 'across the country a water main break occurs every two minutes, 43% of public roadways are in poor or mediocre condition, and 10,000 miles of levees remain unaccounted for and unchecked'.

According to Joseph Cohen, just to fix the existing road, rail and pipeline infrastructure in the US would cost $2.5 trillion. Rural infrastructure in particular is a problem, especially with the shift

HILL & SMITH REVENUE GROWTH

Source: Company reports, Jefferies



to remote working putting more strain on local facilities.

FASTER GROWTH, HIGHER MARGINS

For Hill & Smith, the opportunities are huge. Analysts at Jefferies estimate 'structural and stimulus-driven investment in highways, and broader infrastructure in the UK & US could drive a period of organic growth that is double the historic trend'.

Jefferies believes organic revenues could grow at 6% per year from this year to the end of the 2024-25 financial year due to the UK's £27 billion Road Investment Strategy 2 and $135 billion of proposed US spending.

As well as road and rail, US power utilities need an infrastructure upgrade as the unexpected freeze in Texas and widespread blackouts earlier this year demonstrated.

A higher volume of US orders would also benefit group margins, with Jefferies suggesting a strategic acquisition in the high-margin galvanizing business in the US could add even more upside to its forecasts.

The firm disappointed investors back in March when it released its results for 2020, as Covid-related shutdowns in the UK, France and India hit spending.

However, much of the work has simply been delayed or 'shifted to the right', while the company was quick to respond by cutting discretionary spending and driving local efficiency plans.

STRONG PEDIGREE

New chief executive Paul Simmons, who joined in September 2020 from UK engineering firm **Halma (HLMA)**, is a strong believer in the decentralised, autonomous operating model and has already laid out a strategy to build on the firm's growth potential in the UK and US, including targeted acquisitions.

'First and foremost, we will continue to focus on accelerating organic growth by increasing the rate of innovation and identifying new niche markets. Second, we will place greater emphasis on higher margins and long-term growth, and we have already fine-tuned our portfolio management criteria to that effect.'

Investors who back Simmons' pedigree include Richard Penny, seasoned manager of the **TM Crux UK Special Situations Fund (BG5Q5X2)**.

'At Halma, Mr Simmons was part of a strong shareholder friendly culture with multiple acquisitions, culminating with the shares becoming some of the most highly valued UK stock market shares,' he says.

'Initial signs are promising that if Mr Simmons can transfer some of the "Halma magic" to Hill & Smith, and with shares at a significantly lower valuation, it will provide scope for strong share price performance over the medium term.'

VALUATION UPSIDE

On current forecasts, Jefferies believes the valuation of Hill & Smith – at 18.7 times current year earnings and 16.7 times two-year forward earnings – offers a 20% discount to the UK industrials sector, whereas it sees a 5% discount as more appropriate.

Certainly compared with another big US infrastructure beneficiary, equipment hire firm **Ashtead (AHT)** – which trades on 35 times current year earnings and 29 times two-year forward forecasts – there is plenty of room for Hill & Smith to re-rate if the new chief executive can execute on his plan. [IC]

TOP STOCKS FOR 2021

DIAGEO
(DGE) £33.65

Gain to date: 14.3%
Original entry point:
Buy at £29.45, 23 December 2020

OUR positive call on alcoholic drinks giant **Diageo (DGE)** is beginning to pay off, aided by an encouraging trading update on 12 May.

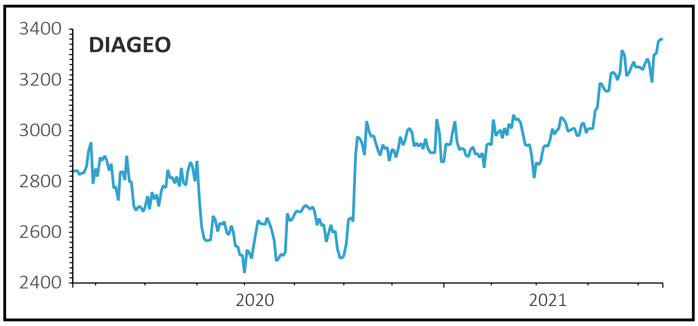
The company announced it was restarting a £4.5 billion capital returns programme, which originally commenced in 2019 and was interrupted by the pandemic, after continuing to see a good recovery across all regions.

This generosity to shareholders, with the company commencing the purchase of its own shares immediately, is underpinned by a forecast for organic operating profit growth to be at least 14% in the year to June 2021, slightly ahead of organic net sales growth.

Performance in North America, Diageo's biggest market, has 'remained particularly strong, reflecting resilient consumer demand, the breadth of our portfolio and the effectiveness of our marketing and innovation'.

In Europe, the drinks giant is benefiting from 'strong execution' in the retail channel and the partial reopening of bars, clubs and restaurants in certain markets.

In Africa, Asia Pacific and Latin America and the Caribbean, it is seeing 'a continued recovery in most markets, despite the ongoing impact from Covid-19'.



SHARES SAYS:
We are encouraged by this update. Keep buying. [TS]

COCA-COLA HBC
(CCH) £25.09

Gain to date: 7.3%
Original entry point:
Buy at £23.38 17 December 2020

OUR 'buy' call on soft drinks colossus **Coca-Cola HBC (CCH)** has marginally underperformed the wider market year-to-date despite achieving solid gains but we are confident there is more upside to come as earnings fizz higher with the reopening of the global economy.

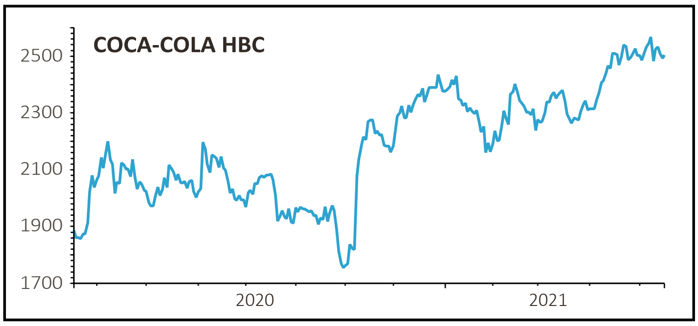
We are encouraged by a first quarter trading update (12 May) from the soft drinks bottler, a strategic partner of The Coca-Cola Company with access to strong brands, leading market shares and a geographically diversified distribution footprint.

Despite Covid-19 related restrictions continuing to impact the important out-of-home channel, Coca-Cola HBC reported a good start to the year with 6.1% like-for-like sales growth led by the sparkling and energy categories and 'strong execution' in the at-home channel.

Lockdowns in Europe continued to stir up headwinds, yet Coca-Cola HBC's geographic diversity enabled it to benefit from accelerating sales in emerging markets, with both Russia and Nigeria seeing double-digit volume growth in the quarter.

CEO Zoran Bogdanovic insists strong customer relationships mean it is well placed to capitalise on the reopening of the out-of-home channel.

'The speed and shape of recovery from the pandemic remains uncertain,' explained Bogdanovic, 'but Q1 puts us on track to achieve our 2021 guidance.'



SHARES SAYS:
Keep buying Coca-Cola HBC. [JC]

UDG HEALTHCARE
(UDG) £10.23

Gain to date: 47.4%
Original entry point:
Buy at 694p, 16 July 2020

IT SEEMS that others have noted the value we saw in health-related services business **UDG Healthcare (UDG)** in July 2020 as the board has now recommended a £10.23 per share cash offer from US private equity firm Clayton, Dubilier & Rice.l

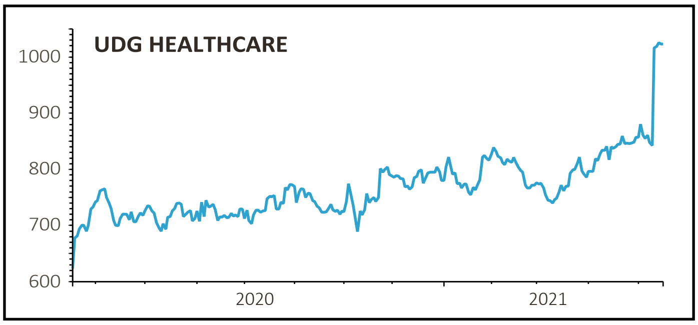
The bid represents a 30.3% premium to the volume-weighted average price of 785.3p over the past six months to 11 May.

The transaction values UDG at an implied enterprise value to EBITDA (earnings before interest, tax, depreciation and amortisation) ratio of 17.2 times. The implied enterprise value of £2.78 billion represents the combined value of outstanding equity and debt.

UDG's Ashfield division, which provides advisory, communications and commercialisation services, is said to be 'highly complementary' with CD&R's Huntsworth business which it purchased in 2020.

The company said the combination of the two businesses would create a 'unique set of global solutions' to support pharma and biotech clients across the life cycle of a drug, from development to patent expiry.

The private equity acquirer said it would invest in UDG's Sharp division, to support its growth prospects. Sharp provides high quality outsourced contract clinical trials, manufacturing and packaging services.



SHARES SAYS:
This looks to be a done deal and with the shares trading at the offer price it is worth selling now and locking in a handsome profit. [TS]

TT ELECTRONICS
(TTG) 244p

Gain to date: 15.6%
Original entry point:
Buy at 211p, 25 March 2021

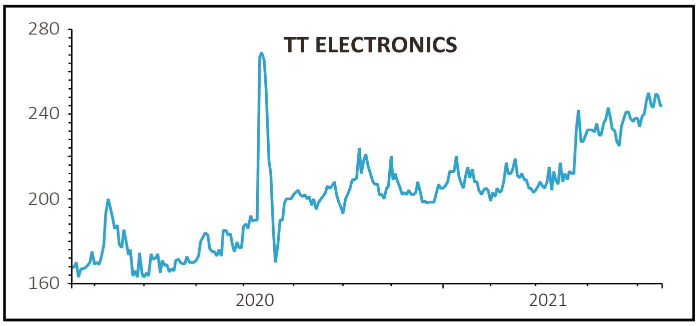
THE PACE of the reopening recovery in some parts of the global economy has seen plenty of companies raise financial guidance for 2021, **TT Electronics (TTG)** among them.

Trading has further strengthened with organic sales ahead by 7% year-on-year in the first four months for 2021 while orders continue to run ahead of sales, presumably as customers look to lock in supply chain demand to meet their own improving prospects.

What this means for TT Electronics is that earnings before interest, tax and amortisation is anticipated to be towards the upper end of market expectations.

That range had been set at between £33.6 million and £35.4 million. Profit by the same measure in 2019, the last year before the pandemic impacted trading, totalled £44.5 million, so there's still a way to go but analysts are increasingly confident. Consensus is for £51.3 million in 2023, which would be a record for TT.

As we explained in the original article, engineer TT is expanding beyond its traditional sensors and instrumentation markets into fast-growing, and more profitable, digital areas. This includes supplying complex connectivity, automation and machine learning components and systems for industrial, renewables and medical applications.



SHARES SAYS:
A revised 2022 price to earnings multiple stands at 13.9, inexpensive given the ongoing recovery scope. Buy. [SF]

Aberdeen Standard Investments

OPPORTUNITY FOR CHANGE IN REAL ESTATE MARKETS

The real estate market was a mixed bag in 2020. While industrials, particularly logistics and certain alternatives, did well during the year, there were also pockets of weakness, particularly within the high street and office markets. It would be tempting to expect the same again in 2021, but the reality may be more nuanced.

Jason Baggaley, manager of the **Standard Life Investments Property Income Trust**, says commercial property investors should expect change and that this will undoubtedly bring opportunity. He has been careful not to respond hastily to the shifts brought about by the pandemic and believes it is important to adapt the portfolio to the new world as it emerges from the post pandemic era: “We have used the period for some very deep reflection. That means challenging ourselves and our assumptions.”

What will emerge? In the short-term, there will be economic recovery, which will ease the pressure on rental payments. Baggaley says: “Our real focus over the next stage is not rental collection but assessing sustainable levels of rents. Within areas such as restaurants and town centre cafes, there has been a decline in rental values because they had become overstretched and now there is less demand. In offices, we can be fairly sure there will be less overall demand but offices themselves will need to adapt to accommodate greater flexibility of working practices. We want to ensure the rental income generated by the trust is sustainable in the long-term.”

Adapting to agile working

The office market is perhaps the area subject to the greatest change. The pandemic has ushered in a mass agile working experiment. There is now a real consensus that the work life balance is unlikely to return to where it was before, with long-term implications for the office market. Craig Wright, Head of Real Estate European Research at Aberdeen Standard Investments, says: “We don’t believe in the death of offices, but we do believe that tenants will be much more selective about what constitutes an office ‘fit for the future’. Investors have to respond to that as well and be more selective in the properties they’re targeting.” This includes flexibility, amenities, technology and sustainability.

While the office market has been particularly hard-hit by the pandemic, there are potential changes for all real estate markets. In the surging logistics market, for example, Evert Castelein, manager of **Aberdeen Standard European Logistics Income**, says that in spite of the strong year in 2020 the team is continuing to focus on the expansion of ecommerce and changing supply chains across Europe. He adds: “It has become clear that long distance supply chains are susceptible to external shocks. Take Jaguar Land Rover, for example. It was struggling to finish its cars because parts were still stuck in Asia. The near-shoring of such operations and de-globalisation of manufacturing is becoming an important trend – for many companies the labour cost arbitrage of having production offshore is starting to become less pronounced now that wage costs are rising in Asia. We see some manufacturers moving back to Europe. We believe this trend will continue in the years ahead.”

New real estate assets

There are also new opportunities across real estate markets as different types of asset are packaged up into an investable format. Emma Scott, Multi-Asset Investment Manager at Aberdeen Standard Investments, says: "We're investing more in alternative areas of real estate. That includes investment companies benefiting from long-term, inflation-linked cash flows – GPs surgeries, social housing, logistics, supermarkets. We look to them for long-term stable cash flows."

She says that yields often compare favourably with other asset classes on offer. The income available is higher than listed equity and private equity, more akin to infrastructure and asset-backed securities.

Looking under the bonnet

At Aberdeen Standard Investments, we believe the most compelling way to deal with this changing environment is to assess deals individually and on their own merit. Jason says: "For each property we assess, we ask whether it is going to meet our investors needs in the future." This nuanced approach is reflected in how he has re-engineered the portfolio in the wake of the crisis.

For Standard Life Investments Property Income Trust the area that witnessed the highest level of sales was in industrials, despite the sector performing well during 2020 he says. "We sold some multi-let estates, which we thought could be much more at risk in an economic downturn. Perhaps surprisingly, our only major purchase was a retail asset – a B&Q warehouse. It may be retail, but it has been posting very strong figures and the unit has fantastic credentials."

Evert is doing similar in-depth research for new European logistics options. As the real estate business is a local business he can call on Aberdeen Standard Investments' team of transaction and asset managers based in local offices across Europe: this network of feet-on-the-ground experts gives access to off-market opportunities, where Evert and team are not bidding against other buyers in an open market. He says: "This is a key advantage for us in this 'in demand' sector as it allows us to negotiate good terms. We always want to know that a building has good optionality for the future if the tenant were to leave the building. We are one of the largest real estate investors in Europe and have local offices across Europe in Amsterdam, Paris, Frankfurt, Madrid."

We also believe that effective management of individual assets will become increasingly important. That means 'green' buildings that suit people's changing lifestyles. Properties need good showers for people cycling to work and green areas for them to eat their lunch to aid employee wellbeing, plus the energy efficiency and renewable energy sourcing (e.g. solar panels) which helps tenants and satisfies our increasingly ESG-focused investors. Evert adds: "We want to protect our future cash flows and that means future proofing by focusing on ESG characteristics. This is really important for us and really important for our tenants."

Craig is clear that the commercial property sector still has some short-term risks to get through: recovery is vaccine-dependent and increasingly divergent between countries. However, monetary and fiscal policy will remain supportive for the sector and real estate has historically performed well in a climate of recovery. It can still fulfil its role in delivering stable, inflation-adjusted capital and income returns in a portfolio.

Companies selected for illustrative purposes only to demonstrate the investment management style described herein and not as an investment recommendation or indication of future performance.

For more information, please visit our websites:

Standard Life Investments Property Income Trust Limited
Aberdeen Standard European Logistics Income PLC
Aberdeen Diversified Income and Growth Trust plc

Important information
Risk factors you should consider prior to investing:

- The value of investments and the income from them can go down as well as up and you may get back less than the amount invested.
- Past performance is not a guide to future results.
- Investment companies are specialised investments and may not be appropriate for all investors.
- Investment companies can borrow money in order to enhance investment returns. This is known as 'gearing' or 'leverage'. However, the use of gearing can result in share prices being more volatile and subject to sudden or large falls in value. Where permitted an investment company may invest in other investment companies that utilise gearing which will exaggerate market movements, both up and down.
- There is no guarantee that the market price of the Company's shares will fully reflect its underlying Net Asset Value.
- As with all stock exchange investments the value of the Company's shares purchased will immediately fall by the difference between the buying and selling prices, the bid-offer spread. If trading volumes fall, the bid-offer spread can widen.
- Investing globally can bring additional returns and diversify risk. However, currency exchange rate fluctuations may have a positive or negative impact on the value of your investment.
- The Ordinary Shares may trade at a discount to the Net Asset Value per Ordinary Share and Shareholders may be unable to realise their investments through the secondary market at the Net Asset Value per Ordinary Share.
- There is no assurance that the Company will be able to secure suitable logistics assets. This may affect the Company's ability to meet the Target Returns and may have an adverse effect on the Company's performance, financial condition and business prospects.
- The Company may hold a limited number of investments. If one of these investments declines in value this can have a greater impact on the fund's value than if it held a larger number of investments.
- Property values are a matter of the valuers' opinions and can go up and down. There is no guarantee that property values, or rental income from them, will increase so you may not get back the full amount invested.
- Property investments can take significantly longer to buy and sell than other investments, such as bonds and company shares. If properties have to be sold quickly this could result in lower prices being obtained for them.
- The Company invests in a specialist sector and it will not perform in line with funds that have a broader investment policy.
- Yields are estimated figures and may fluctuate, there are no guarantees that future dividends will match or exceed historic dividends and certain investors may be subject to further tax on dividends.
- Derivatives may be used, subject to restrictions set out for the Company, in order to manage risk and generate income. The market in derivatives can be volatile and there is a higher than average risk of loss.
- The Company may invest in alternative investments (including direct lending, commercial property, renewable energy and mortgage strategies). Such investments may be relatively illiquid and it may be difficult for the Company to realise these investments over a short time period, which may make it difficult to realise investments and may lead to volatility in the market price of the Company's shares.

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US vs CHINA

which is best for investors and where should you put your money?

COULD THE CHINESE MARKET OFFER BETTER INVESTMENT OPPORTUNITIES THAN THE US?

By **Ian Conway** Senior Reporter

There has been a simmering debate since the start of 2021 as to whether China might overtake the US as the engine of world growth over the coming decade.

However, our belief is that ultimately the US will continue to rule the roost economically and politically for the rest of this decade. Its pro-business attitude, both from Capitol Hill and the Federal Reserve, will ensure that companies continue to thrive and the economy continues to grow.

President Biden's ambitious rescue plan is likely to pass in one form or another, and even if corporate taxes rise in the short term it is unlikely to put too much of a dampener on things.

Plus there are at least as many exciting US growth companies as there are Chinese companies.

That said, a balanced portfolio should really have exposure to both markets with actively-managed funds which seek out the most interesting growth opportunities and do all the hard work for you a good option.

At the end of the article we highlight some investment trusts to buy, all of which have shown that by superior stock selection they can beat their respective markets by a healthy margin.

CHINA'S DECADE?

China entered the pandemic earlier than other countries, and due to its unique ability to clamp down on freedom of movement it also exited the pandemic earlier, since when its economy has been firing on all cylinders and growth is expected to outstrip that of most developed countries this year and next.

The US, in contrast, was late to implement lockdown and vaccinations, and is exiting the crisis with falling industrial confidence and a stuttering jobs market, as shown by the latest disappointing payroll figures, while technology stocks are under the cosh due to inflation fears.

If the US is going to remain the dominant economic power this decade, then it's reasonable to assume that many of the most valuable companies in the world will still be American.

If on the other hand China is going to dominate, we should expect to see more Chinese companies on the list of the world's most valuable businesses.

Taking the decades which ended in 1990, 2000, 2010 and 2020, the list of the largest companies by market capitalisation at the end of each of the four periods tell their own story.

LARGEST GLOBAL STOCKS BY MARKET VALUE 1990-2020

1990	2000	2010	2020	Market Cap $m
NTT	Microsoft	ExxonMobil	Apple	2,254,000
Bank of Tokyo-Mitsubishi	GE	PetroChina	Microsoft	1,682,000
Industrial Bank of Japan	NTT DoCoMo	Apple	Amazon.com	1,634,000
Sumitomo-Mitsui Bank	Cisco	BHP Billiton	Alphabet	1,185,000
Toyota Motor	Wal-Mart	Microsoft	Facebook	776,590
Fuji Bank	Intel	ICBC	Tencent	683,470
Bai-Ichi Kangyo Bank	NTT DoCoMo	Petrobras	Tesla	668,080
IBM	ExxonMobnil	China Construction Bank	Alibaba	628,650
UFJ Bank	Lucent	Royal Dutch Shell	TSMC	565,280
Exxon	Deutsche Telekom	Nestlé	Berkshire Hathaway	544,780

Source: Reuters Eikon, Shares

Market values as of 31 December 2020 in USD

The last decade reflects the resurgence of technology stocks, both in the US and China, almost all of them consumer-facing. Interestingly, one company – Microsoft – has managed to make the list not twice but three times, showing how adept it is at finding new ways to grow.

For Alphabet, Amazon.com, Facebook and Tesla, the rise has been meteoric. From being fairly big companies to begin with, they have become goliaths, insinuating their way into most of our lives. The same is true of Alibaba and Tencent in China.

The question is, are there more Alibabas and Tencents waiting in the wings to usurp their US peers, or are there more US candidates for the 2030 list, companies which are 'bubbling under' at the moment but are about to begin their own meteoric journey?

IT'S NOT ALL ABOUT GDP GROWTH

There have been plenty of studies which show that stock markets and GDP growth have a low correlation with one another. A country with a faster-growing economy doesn't necessarily generate higher stock market returns than a country with a lower economic growth rate.

China is a perfectly good example. Over the decade from 2010 to 2019 its economy grew by an average annual rate of 7.7% against just 2.2% for the US. That means that, on a cumulative basis, China's economy more than doubled over ten years while the US economy grew by just 25%.

Yet 2010 to 2019 was pretty much a lost decade for equity investors in China, with the Shanghai Composite index losing 7% of its value over the period while the US S&P 500 index almost trebled in value.

That's not to say there haven't been some great investments in China, as demonstrated by the performance of Alibaba and Tencent, but if you had invested in a tracker fund you would have lost money.

While the Chinese economy has doubled in size, it is changes in the structure of the

GDP GROWTH RATES AND STOCK MARKET RETURNS 2010-2019

	10-year GDP Growth	10-year Price Return
CHINA (Shanghai Comp.)	110%	-7%
US (S&P 500)	25%	190%

Source: World Bank, Shares, Ycharts

GDP GROWTH COMPARISON 2010-2019

	CHINA	US
2010	10.6%	2.6%
2011	9.6%	1.6%
2012	7.9%	2.2%
2013	7.8%	1.8%
2014	7.4%	2.5%
2015	7.0%	2.9%
2016	6.8%	1.6%
2017	7.0%	2.4%
2018	6.7%	2.9%
2019	6.1%	2.2%
AVERAGE	**7.7%**	**2.3%**
COMPOUND	**110%**	**25%**

Source: World Bank, growth shown in local currencies economy which matter most. From being reliant on fixed asset investment, often inefficient and fuelled by unsustainable amounts of debt, the authorities have sought to rebalance growth over the last decade by taking advantage of the vast amount of national savings to boost consumption.

A BALANCING ACT

It is widely expected that China will continue to grow faster than the US in the early stages of this decade, after it exited the pandemic earlier and on a stronger footing.

In the latest 'Five-Year Plan' published earlier this year, the government set out its key priorities: to make China a self-reliant technological and manufacturing powerhouse, prioritise quality of growth over quantity of growth, accelerate the drive towards a low-carbon economy, achieve 'common prosperity' and 'elevate China's leadership role in regional and global economic governance'.

China's economy is increasingly service-driven, which makes it employment-intensive, but it faces a huge challenge – the labour force is shrinking. According to the latest census, the coronavirus pandemic caused the number of births in China to fall last year to its lowest since the Great Famine of 1961.

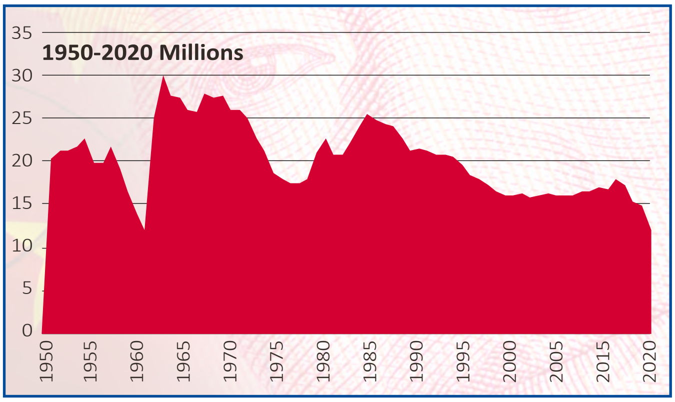
This slump in new births means China has to re-calibrate. Just a few years ago, demographers expected the population to peak in 2030, now they think it could happen as early as next year.

To combat the decline in the labour force – the working age population has already shrunk from 70% to 63% in a decade as the average age increases – tens of millions more people will need to migrate from rural areas to cities, and the government will need to raise the statutory retirement age, a contentious move which it attempted in 2015 and failed.

However, this will need to be accompanied by a huge increase in state spending on healthcare and pensions for those in work and those who have retired to continue feeling comfortable drawing on their savings to fund their spending.

Increased healthcare and state pension costs likely mean higher taxes on companies and on the working age population, so the government has to pull off a major balancing act if it is to avoid the economy slowing.

CHINESE BIRTH RATE



Source: China National Bureau of Statistics, Shares

UNPRECEDENTED STIMULUS

Meanwhile, the US has its own balancing act to pull off. president Biden's 'American Rescue Plan' calls for over $4 trillion of government spending across all areas of the economy and social life.

To put the plan in perspective, the Obama administration's Emergency Economic Stabilisation Act of 2008 cost the US government an estimated $700 billion to $800 billion, although all of the $440 billion of TARP funds used to stabilise the banking system were recovered, at a small profit.

Put simply, Biden's spending plan is vast, with $2.3 trillion set aside for infrastructure spending and $1.9 trillion for a 'families plan'.

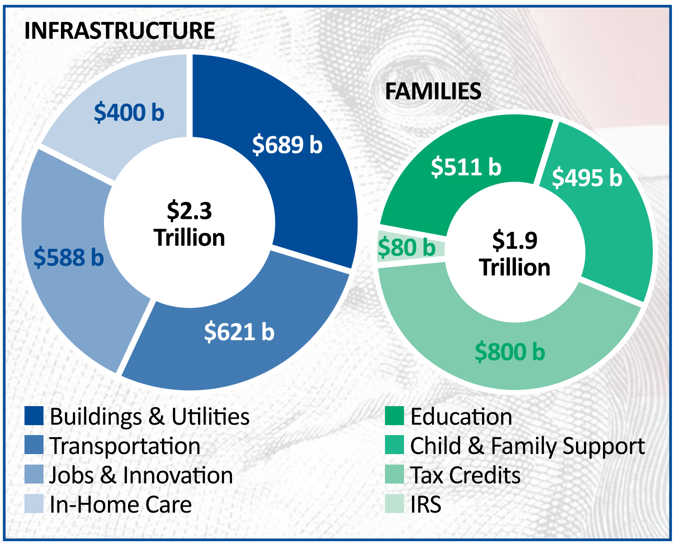
That America's physical infrastructure is dated and needs a major overhaul is in no doubt. Its transport infrastructure in particular is light years behind China's, which boats mag-lev trains and state-of-the-art airports.

The US's digital infrastructure is also in dire need of upgrading, as shown by the recent cyber attack which halted the operation of a major US pipeline supplying roughly half the gasoline to the East Coast.

Hackers were able to steal hundreds of gigabytes of data from the company running the pipeline, then lock the firm's computers and force the firm to pay a 'ransom' to prevent a data leak.

Utility companies are particularly vulnerable as their computer systems were often designed

BIDEN'S ECONOMIC 'RESCUE PLAN'



Source: whitehouse.gov, NY Times, Shares

decades ago and security features are poor, but as commerce secretary Gina Raimondo observed, these sorts of attacks 'are becoming more frequent, they're here to stay, and we have to work with business to secure networks to defend ourselves'.

THE ART OF THE DEAL

While Donald Trump pitched himself as a brilliant deal-maker, president Biden is well known in Washington for being an arch negotiator. He knows full well his spending plans – and the tax reforms he proposes to part-fund them – face opposition not just from Republicans but from some within his own party.

By 'going large' on stimulus to begin with, he has given himself room to negotiate to a position where as few people as possible are unhappy. There are fears his corporate tax proposals will stifle investment, the opposite of what the US needs right now, but similarly by starting from an extreme position he has left room for an increase which both sides can agree, a 'Goldilocks' deal.

Also, many of those that control the purse strings are allies, with several regional Fed governors supporting the President's call for 'aggressive' support for the jobs market and for families.

WHAT ABOUT TECH STOCKS?

Technology stocks have been the undoubted stars of the last decade, surfing the rollout of e-commerce, cloud computing, social media and more recently remote working which has driven demand for everything from routers and laptops to networking tools such as Teams.

The US has made noises about clamping down on the small clique of tech companies which dominate the stock market, but this would seem to be more a case of leaning on them to allow some trickle-down of technology – and ultimately earnings – to others in the sector.

In China, in contrast, the authorities are desperate to limit the power of domestic tech companies because they see them as a threat to the established order. Having amassed billions of bytes of data on the Chinese populace for their own commercial ends, the government wants to limit their power and is almost prepared to sacrifice the golden goose to get its way.

Ant Group, owner of the ubiquitous AliPay app and Huabei credit card and reckoned to be behind as much as 10% of China's total consumer lending in 2020, has been ordered by the regulators to restructure, severely weakening its credit business.

Alibaba, which owns a 33% stake in Ant Group, has been fined $2.8 billion by China's anti-trust regulators over restrictions it allegedly placed on those selling on its e-commerce platform. The fine itself is a drop in the ocean for Alibaba, but the message is clear.

New ideas and technology will still come from China, as James Anderson, outgoing manager of the **Scottish Mortgage (SMT)** trust points out. 'The creative energy within the technology industries which used to be found in Silicon Valley more than anywhere else is now more and more found in China and North Asia', he says.

So what of the current US tech leadership? We find it hard to believe that, having made the list more than once, Apple and Microsoft won't remain among the world's most valuable companies by the end of this decade.

The same can probably be said of Amazon.com and Alphabet, but could the appearance of Tesla mark its zenith? Its shares have already lost a third since their peak in January, more than enough to relegate it from the list already, and in an era when corporate governance is increasingly integrated into stock selection how many big investors can afford to look the other way while its founder makes policy on the hoof on social media platforms?

WAYS TO PLAY CHINA

Fidelity China Special Situations (FCSS)

Price: 398p
Discount to NAV: 2.7%
Gross Assets: £2 billion

The fund, the UK's biggest China investment trust, is run by 25-year Fidelity veteran Dale Nicholls and has a five-star rating from Morningstar.

The trust has beaten the MSCI China index in US dollars by a handsome margin over one, three, five and 10 years, almost entirely through capital growth as the dividend is not that much more than 1%.

Nicholls looks for growth opportunities in China's changing economy. Many of the stocks in the portfolio play into the growth of domestic consumption, supported by the natural development of the middle class, and the emergence of strong local brands.

More cyclical areas include tankers, where order books are at a historic low relative to the size of the fleet, and dry bulk such as industrial metals.

One of its most exciting holdings is Wuxi AppTec, a laboratory services firm which allows biotech companies to accelerate their research and development and plays into the healthcare and ageing population theme.

Also, the trust has invested in unlisted companies since launch in 2010 and can invest up to 10% of its assets in this space. It was an early investor in 'future disruptors' like online e-commerce firm Alibaba, which is still a top 10 holding.

JP Morgan China Growth & Income (JCGI)

Price: 583p
Discount to NAV: 5%
Gross Assets: £564 million

This fund, which also has a five-star rating from Morningstar, combines a focus on growth companies in the 'new China' with a predictable quarterly income, and yields just under 4% at current prices.

Managers Howard Wang and Shumin Huang have worked together on the fund for the last 15 years, over which time it has beaten the MSCI China index over one, three, five and ten years by a considerable margin.

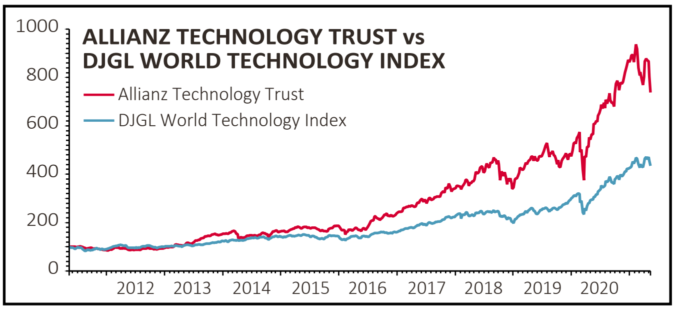
As well as holdings in Alibaba, Tencent and Wuxi, the trust owns stakes in CATL, one of the world's largest makers of batteries for electric vehicles, and Ping An Insurance, which as well as offering savings products has branched out into digital healthcare services, a market which has grown rapidly thanks to the pandemic.

Despite its income characteristics, the trust is underweight Chinese state-owned banks as they are not just slow growing but are seeing greater government involvement in their operations, something the trust is keen to avoid.

WAYS TO PLAY THE USA

Allianz Technology Trust (ATT)

Price: 256p
Discount to NAV: 7.6%
Gross Assets: £1.2 billion



Another five-star rated fund, the trust is managed by Walter Price, co-head of the AllianzGI Technology Team, who joined the firm in 1974.

It has beaten the Dow Jones World Technology Index over one, three and five years, and while its outperformance was more measured over the last one and three years it has left the index trailing since the start of 2021.

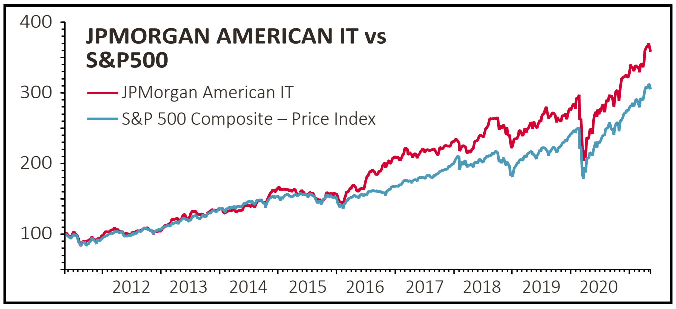
Technology stocks continue to benefit from strong tailwinds in areas such as cloud computing, big data, artificial intelligence, the internet of things and gaming.

Also, says Price, 'We are seeing a wave of innovation in the technology sector: automobiles, advertising, security, retail, and web services are all being shaped and transformed by advances in technology'.

The current chip shortage has boosted the trust's returns from stocks such as Applied Materials, Micron and Samsung Electronics, all among the top 10 holdings, while the uptick in cyber attacks will surely see companies such as CrowdStrike – another top 10 holding – continue to rack up impressive sales growth.

JPMorgan American (JAM)

Price: 632p
Discount to NAV: 4.6%
Gross Assets: £1.4 billion



For any general or non technology-biased US fund to have outperformed the S&P 500 index over the last one, three and five years is so rare that this trust is unique for being the *only one* in the Association of Investment Companies' North American sector to have achieved this feat.

Managers Timothy Parton and Jonathan Simon have worked at JPMorgan for more than 30 years and 40 years respectively, although they only took over management of this flagship fund two years ago.

The emphasis is on capital growth rather than income, and the approach is multi-cap so the managers are able to own interesting smaller companies while the 'permanent capital' structure of the trust means they can let their ideas run.

The fund's top five holdings are already among the top 10 biggest stocks in the world – Alphabet, Amazon, Apple, Berkshire Hathaway and Microsoft - while its most notable overweight versus the index is in financial stocks, with three more – Bank of America, Capital One and Loews – also on its list of top 10 holdings.

The fund's focus on quality stocks has served it well despite the 'value rotation' seen in global markets and the managers look for opportunities during sell-offs to add to their high-conviction picks.

Covid-19 diagnostic firms have fallen too far given they still play a crucial role

Despite a decline in infections, testing is likely to become routine to keep everyone safe and maintain freedoms

The successful development of vaccines was a triumph for the world and was for the most part great news for equities too, however it negatively impacted sentiment for one particularly sub-set of the market.

The initial excitement surrounding biotechnology companies involved in developing Covid-19 testing kits and treatments for sufferers of coronavirus rapidly evaporated as the focus moved from testing and treatment to the protection offered by jabs.

The massive subsequent falls seen in share prices has probably gone too far in some cases, considering the likely demand for mass testing hasn't disappeared entirely.

However, we should point out the small cap names in the sector are far more volatile than average and only suitable for investors with a reasonable tolerance for risk.

The waning enthusiasm for testing plays is not a huge surprise given the fast deployment of vaccination programmes in the UK, US and Israel. Infection rates have fallen rapidly across the UK, notwithstanding the risk of emerging new strains such as the latest Indian variant which has been classified a 'variant of concern' due to its faster transmission rates.

TESTING STILL HAS A ROLE

However, dismissing the need for Covid-linked diagnostics and medicines is an oversimplified take on the current situation with many countries now leaning towards weekly or bi-weekly mass testing programmes to fully open their economies.

In the UK the entertainment industries have adopted a rigorous testing protocol in a controlled way to allow events to happen in front of live audiences.

For example, the recent final two days of the world snooker championships in Sheffield was the first indoor event to be held in the UK with a near capacity crowd in over a year.

This was allowed on the basis that people entering the arena had proof of a negative test. Pharmaceutical analyst at Finncap, Mark Brewer argues that demand for high sensitivity tests will exist for many years despite the vaccine roll-out.

Brewer highlights the US government has spent $1.2 billion purchasing Abbot Laboratories' lateral flow tests while the UK government has spent over one billion pounds on buying hundreds of millions of Innova Medical tests.

A report from Grandview Research estimates that the global Covid-19 testing market was worth around $84.4 billion in 2020 and is expected to grow at a compound annual growth rate of 3.1% from 2021 to 2027.

Stock price performance of selected diagnostics and health care services companies

Company	Price relative to 52-week high (%)	Change since beginning of March 2020 (%)
Avacta	-5.8	1644
Omega Diagnostics	-39.0	836
BergenBio	-46.0	104
4D Pharma	-46.3	266
Abingdon Health	-57.6	n/a
Synairgen	-59.4	222
Genedrive	-65.9	686
Novacyt	-67.3	241
Tiziana Life Sciences	-69.8	159
Average	**-50.8**	**520**

Source: Stockopedia

DOWN BUT NOT OUT

As the table shows, on average, the share prices of our selected group of companies have halved relative to their 12-month highs, which were largely achieved in the early parts of 2020.

For example, shares in molecular diagnostics company **Genedrive (GDR:AIM)** peaked on 5 May 2020 at a price of 220p from which it has subsequently fallen by two thirds.

The company was recently successful in its tender for the Public Health England's microbiology framework agreement which allows it to supply all the company's Covid-19 testing equipment.

However, being part of the framework doesn't guarantee orders.

Its test kit was also approved by the Indian regulator after showing 100% sensitivity and specificity in a performance evaluation conducted by the Indian Council of Medical Research.

Sensitivity measures the accuracy of positive tests while specificity is a measure of the accuracy of correctly identifying negative test results.

At the other end of the performance spectrum is cancer therapies and diagnostics company **Avacta (AVCT:AIM)** with the shares only around 6% off the recent highs.

That's because the business has generated a lot of positive momentum in recent weeks. This month it began the commercial roll-out of its sensitive rapid lateral flow test after it gained CE marking, allowing it to be marketed across the EU.

The company's test is intended to provide a fast, low-cost means of identifying individuals with high viral loads, who are considered more likely to infect others.

In clinical studies, the test achieved sensitivity of 98% and specificity of 99% which is considered high for a lateral flow test.

Lateral flow tests had been seen as a poor relation to the 'gold standard' polymerase chain reaction or PCR tests which are designed to test genetic material in a virus.

In contrast, lateral flow tests are designed to detect the spike protein produced by the body in response to the presence of a virus.

BIG GAINS FOR AVACTA

Shares highlighted Avacta as a great way to get exposure to the Covid-19 testing market back in April 2020, on the basis that its rapid lateral flow test could be a 'game changer'. It has since been one of the best performing shares in the diagnostics space gaining 296%.

Avacta recently confirmed it has manufacturing capacity, subject to access of equipment funded by the UK government, to produce five million-to-30 million tests per month. We think the shares are still attractive.

One of the darlings of the sector last year was diagnostics firm **Novacyt (NCYT:AIM)** which was one of the first companies to develop an effective PCR test to identify the virus, which it launched at the end of January 2020.

At that time the shares were trading at 20p and they eventually rocketed to £11.94 in October, registering a 5,870% gain in a few months.

However, a profit warning on 9 April relating to the failure to extend a Covid-19 testing kit supply contract for the Department of Health and Social care, saw the shares slump 39% and they have drifted lower since.

The failure to extend the contract and souring relationship with the DHSC undermined the investment case. The contrasting

fortunes of Avacta and Novacyt underlines the heightened volatility and risks associated with the sector.

LIVING WITH COVID-19

Vaccinating the global population will likely take years, given the reluctance of some nations to share their stockpiles and the politics and logistics involved.

Health care analyst Adam Barker at Shore Capital argues that recent calls to waive intellectual property rights wouldn't necessarily achieve the hoped-for benefits of increased supply to developing nations.

'For many developing countries, knowing how to make the vaccines would be one thing, but actually being able to do it, store and transport them is a completely different issue.'

Barker points out that vaccines are incredibly hard to manufacture, with onerous safety checks being one reason why there aren't any generic vaccines.

The threshold for herd immunity is the point at which most of a population is immune to an infectious disease, either through having had the virus or through immunisation.

Some estimates put the threshold at around 70% but there isn't widespread agreement on the matter.

According to the World Health Organisation and data compiled by Our World Data, around 1.37 billion doses had been administered as at 13 May 2021 and 333 million people have been fully vaccinated, representing 4.3% of the global population, emphasizing the enormity of the task of reaching herd immunity.

While the virus is still at large and mutating somewhere on the planet, the risk of more deadly strains is ever present. This reinforces the logic of continued mass testing programmes.

The risks of investing in the sector are higher than average but likewise, the potential rewards could be significant. One such share with huge potential and whose shares have fallen 59% from the recent highs is respiratory and drug discovery firm **Synairgen (SNG:AIM)**.

Synairgen (SNG:AIM)
Price: 100p
Market Cap: £200.1 million

The company has been developing its SNG001 drug for the treatment of respiratory virus infections for over a decade.

The inhaled drug can be used in the home setting, was given fast track status from the US Federal Drug Agency in December 2020.

In a UK at-home study, SNG001 was 100% effective at preventing hospitalisations with the strongest effect seen on patients suffering marked and/or severe breathlessness.

As we have discussed the increasing number of variants pose a risk to the effectiveness of vaccination programmes.

For example, Numis noted that The Seychelles, despite being the most vaccinated country in the world, recently reintroduced widespread restrictions.

This means that Synairgen could play a crucial role in providing a solution for treating high risk patients affected by new resistant strains as well as parts of the world with high infection rates such as India.

After raising fresh equity last year, the company has £75 million of cash on the balance sheet.

By **Martin Gamble**
Senior Reporter


THE SCOTTISH
Investment Trust
We invest in ugly ducklings…
Unloved and underappreciated, our contrarian opportunities have the potential to flourish during the economic recovery and thrive over the long term.
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The value funds vying for top dog status

Shining a spotlight on the best performing value collectives since the market's vaccine boost

After more than a decade of domination for growth stocks, global markets are finally seeing a shift into value.

This in turn has benefited funds pursuing a value investing style. Growth performed relatively well through the initial course of the pandemic with technology stocks leading the way, but the key catalyst for the long-awaited rotation into value was 'Pfizer Monday' on 9 November last year.

The arrival of effective vaccines allowed investors to begin forecasting an economic recovery and stronger global growth ahead and led them out of growth stocks and into value and cyclical sectors which typically do better during periods of economic recovery.

Over the past six-and-a-half months, funds, investment trusts and exchange-traded funds (ETFs) following a value style have had a powerful tailwind behind them. *Shares* has crunched data from FE Analytics covering the period from 1 November 2020 to 12 May 2021, thereby capturing the value rally, to reveal the leaders and laggards among collectives with a value bias.

Our research shows small cap value portfolios are enjoying their day in the sun, and also demonstrates that

selective actively managed funds with a focus on value are managing to outperform competing low-cost ETFs.

In addition, several UK equity income funds have also enjoyed a rare glimpse of the top of the performance tables thanks partly to the cyclical make-up of the UK stock market, with investors reassessing the prospects for economically sensitive stocks following the arrival of coronavirus vaccines.

FUNDS FLYING HIGH

Investors seeking low-cost exposure to the value rotation could have made roughly 36.5% in six and a bit months by buying the two best-performing ETFs with a value bent. According to FE Analytics, these were **Xtrackers MSCI Europe Value (0MVO)** and **iShares Edge MSCI Europe Value Factor (IEVL)**.

Yet investors who entrusted their hard-earned cash to stock picker Jonathan Winton would have seen a superior 55% return, as his **Fidelity UK Smaller Companies (B7VNMB1)** fund proved the best-performing open-ended vehicle with a value bent since 1 November 2020.

Winton invests in companies that have gone through a period of underperformance, but where there are 'unrecognised growth options'; he believes the stock market is inefficient at pricing companies that have gone through a troubled period and are out-of-favour as a consequence.

This is particularly the case for smaller companies where a lack of research can often combine with market scepticism to leave many companies trading below the true value of their franchise, in Winton's view.

Often, it is only when an improvement in a company's trading is visible that the market moves to reprice future growth prospects. Winton places strong emphasis on understanding the downside risk of each potential investment.

Holdings span the likes of car parts-to-bicycles seller **Halfords (HFD)**, floor coverings distributor **Headlam (HEAD)**, outsourcer **Serco (SRP)** and luxury interior furnishings firm **Sanderson Design (SDG:AIM)**.

Also riding high is **TM RWC UK Equity Income (BG34293)**, the Ian Lance and Nick Purves-managed fund ranked first quartile on a one year, six month and three month basis according to Trustnet.

The overwhelming bulk of the fund's assets are invested in companies valued at larger companies (£2.5 billion plus), with strong recent performers ranging from **Royal Mail (RMG)** and mining giant **Anglo American (AAL)** to banking group **NatWest (NWG)**.

Another high-flyer is **UBS UK Equity Income (B4W5895)**, the quarterly dividend paying portfolio managed by Steven Magill, head of the European value team at UBS Asset Management.

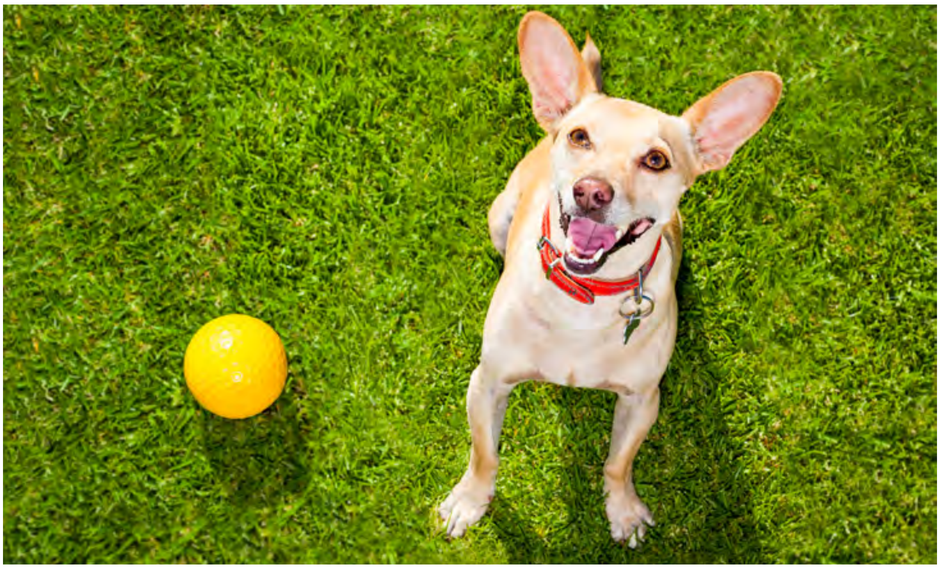
Mainly preoccupied with opportunities among the large caps, the fund has returned an impressive 49.4% during the value rally, benefiting

BEST PERFORMING VALUE TRUSTS	
Chelverton UK Dividend Trust	101.4%
Aberforth Smaller Companies Trust	78.1%
Fidelity Special Values	67.7%
Merchants Trust	58.2%
Lowland Investment Trust	55.3%
Value & Income Trust	44.8%
Aurora Investment Trust	43.2%
BlackRock North American Income	39.4%
The Scottish Investment Trust	18.4%

BEST PERFORMING VALUE FUNDS	
Fidelity Uk Smaller Companies	54.6%
TM RWC UK Equity Income	52.4%
UBS UK Equity Income	49.4%
LF Lightman European	45.9%
Halifax Special Situations	39.9%
NFU Mutual UK Equity Income	35.0%
T. Rowe Price US Large Cap Value Equity	31.1%
IFSL Sanlam US Dividend	28.8%
MI Metropolis Value	28.4%
TM Crux UK Core	28.3%

BEST PERFORMING VALUE ETFS	
Xtrackers MSCI Europe Value	36.6%
iShares Edge MSCI Europe Value Factor	36.5%
iShares Edge MSCI USA Value Factor	33.5%
Xtrackers MSCI World Value	30.9%
iShares Edge MSCI World Value Factor	30.8%

Source: FE fund info, 1 November 2020 to 12 May 2021



Revolution Bars is included in Chelverton UK Dividend's portfolio

from share price surges from top ten holdings including **Barclays (BARC)**, **BP (BP.)** and **Glencore (GLEN)**.

TOP VALUE TRUSTS

Among the top performing investment trusts with a value investing style is **Aberforth Smaller Companies (ASL)**, with a total return of 78.1% over our designated period.

Invested in companies ranging from supermarket salads-to-pizzas supplier **Bakkavor (BAKK)** to recruiter **Robert Walters (RWA)** and logistics firm **Wincanton (WIN)**, Aberforth's managers are value investors who buy shares in companies they calculate to be selling below their intrinsic value.

This is determined through detailed financial and industrial analysis, combined with 'a valuation approach that focuses on both stock market and corporate worth'.

Other noteworthy performers with an emphasis on value include **Chelverton UK Dividend Trust (SDV)**, up 101.4%, as well as **Fidelity Special Values (FSV)**, managed by Alex Wright and the aforementioned Jonathan Winton with a contrarian style which has returned 67.7% during the value rotation.

Also enjoying a revival is **Temple Bar (TMPL)**, managed by RWC Partners' Ian Lance and Nick Purves (see above), which has delivered a robust 65.2% return during the rotation into value.

Indications of rising inflation have provided a tailwind for reopening names held in Chelverton UK Dividend's portfolio, among them **Restaurant Group (RTN)**, **Revolution Bars (RBG:AIM)** and **Saga (SAGA)**.

LAGGING BEHIND

Two trusts that have delivered positive returns over the period in review, yet have lagged value peers, are **Lowland (LWI)** and **The Scottish Investment Trust (SCIN)**. The relative underperformance more glaring in the latter's case.

Trading on a 5.5% discount to net asset value (NAV), research house Edison says Lowland, managed by James Henderson and Laura Foll, offers 'a differentiated approach from peers given its value-biased style, long stock list, high weighting in smaller companies, and willingness to hold some of the portfolio in non-yielders with significant growth potential'.

And with the world reopening from lockdowns, 'the more cyclical and small-cap names favoured by Lowland Investment Trust's managers have begun to outperform'.

Sitting at an 8.9% discount to net asset value (NAV), The Scottish Investment Trust is a global fund managed by contrarian investor Alasdair McKinnon.

McKinnon seeks undervalued, unfashionable companies that are ripe for improvement and recently revamped the portfolio to take advantage of the many opportunities among unloved areas of the market he believes will benefit from a multi-year economic rebound.

Current holdings including the likes of **BT (BT.A)**, energy giant BP, US bank Wells Fargo, home improvement retailer **Kingfisher (KGF)** and restaurants operator Cheesecake Factory.


By **James Crux**
Funds and Investment Trusts Editor

BlackRock

GLOBAL RECOVERY WILL REVIVE LATIN AMERICA

BLACKROCK LATIN AMERICAN INVESTMENT TRUST PLC

Latin American markets should be a key beneficiary of the global economic recovery, says Ed Kuczma, Co-Manager of the BlackRock Latin American Investment Trust plc, even if there are still some reasons for caution.

Ed Kuczma

Co-Manager,
BlackRock Latin American Investment 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.

It has been a tough period for Latin America, with many countries hit hard by the COVID-19 crisis. However, it is possible to build a case for better times ahead for the region as the world rebuilds after the pandemic. It may be one of the most important beneficiaries of recovery in the global economy.

In common with many emerging markets, Latin America has struggled to manage the COVID-19 crisis. Population density, poor decision-making and inadequate healthcare facilities have all contributed to the weakness. Today, the region appears to be finally turning the tide, as the vaccine rollout builds momentum, but the human and economic cost has been significant.

As the region rebuilds, it will have some important tailwinds. Perhaps the most significant is rising commodity prices. Vast stimulus in the US and economic recovery across the world has pushed up demand for commodities after a period of tight supply. Global governments have ambitious, commodity-heavy infrastructure plans, particularly for green energy development.

COMMODITY-RICH REGION

While the Latin American economy has notably diversified in recent years, the region is still commodity-rich and is benefiting from improving prices. In the portfolio, we have been focused on a number of key areas: lithium is a vital component in electric cars, while copper is widely used in

renewable energy infrastructure; pulp and paper demand is growing as companies across the world re-stock and we are also bullish on Mexican cement producers, which are benefiting from strong US demand from the housing and infrastructure sectors.

Latin America is, in many cases, the lowest cost producer of these important commodities. It has relatively low labour costs and established extraction capacity. Commodities are high quality and abundant. As an example, the climate in Brazil allows a eucalyptus tree to grow to maturity in seven years. In Canada, the same growth takes 21 years.

There are also domestic factors that should support economic growth. Across Latin America, a growing middle class is fuelling domestic consumption and after a brief hiatus from the pandemic, this spending appears to be resuming. In Brazil, for example, record low interest rates continue to drive a growth in mortgages, auto sales and credit penetration.

MARKET-FRIENDLY REFORM

There is much to criticize in the way Brazilian leaders have handled the pandemic, but the economic reform agenda has remained largely intact. This continues to push for a market-

BlackRock

friendly programme of privatisations and modernisation of the tax and the public service systems, which should increase levels of private investment.

Low interest rates and economic reform are being felt in markets. Latin American markets are diversifying and Brazil in particular, has a rich IPO (Initial Public Offering) pipeline. This is bringing new sectors and more choice for investors in the region. In the trust, we have exposure to structural growth themes in the region including healthcare, e-commerce and convenience stores.

Against this backdrop, we see anecdotal evidence that generalist emerging market managers are moving away from China – which has a lot of technology names – to more cyclical markets. Latin American markets, with their focus on materials, energy and financials, are a key beneficiary. Latin America is lightly represented in emerging market benchmarks and has generally been under-owned, so it only takes a small change in sentiment to have a significant impact.

That said, it is still a region that requires selectivity. It has its weak spots – political risk may rear its head again in Brazil with the presidential elections next year and countries may be left with higher debt level as a result of the crisis. Nevertheless, there is a lot of negativity already priced into markets and we believe that the future may be much brighter than investors are currently expecting.

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

TO INVEST IN THIS TRUST CLICK HERE

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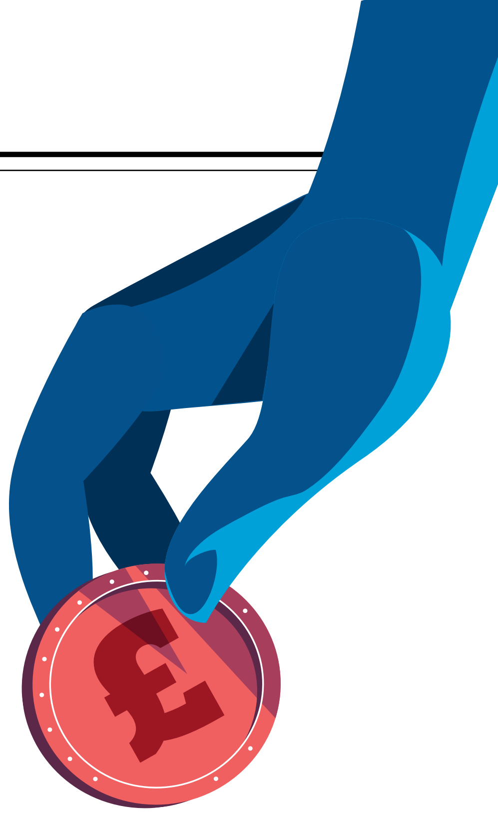
How to analyse property-focused investment trusts, aka REITs



We explain what they are, the key metrics to judge them by and the top performers

Real estate investment trusts, or REITs for short, launched in the UK in 2007 and there are now more than 50 of these vehicles listed on the London Stock Exchange.

In effect a REIT looks to replicate the experience of holding property directly for an investor.

The average person can only afford to own their home, and some might also have a buy-to-let property as well. For most, the idea of having a portfolio of properties including commercial real estate is out of the question, which is why REITs can be an advantageous and simple way of getting exposure to this asset class in an investment portfolio.

WIDE VARIETY OF REITS

REITs come in lots of different shapes and sizes, ranging from multi-billion-pound market valuations to being worth less than £10 million, and encompassing everything from office blocks and supermarkets to care homes and theme parks.

Another top-level distinction made by Numis investment companies research associate Andrew Rees is between investment company and equity REITs.

He notes the lines between the two can be blurred but says: 'Investment company REITs tend to be externally managed, with a "property adviser" or manager paid an annual management fee and sometimes a performance fee to undertake all investment decisions regarding the property portfolio, although still overseen by an independent board who ensure that the fund is fulfilling its investment objectives:

'Conversely management of equity REITs is generally internalised and so more akin to other operating companies.'

TOP PERFORMING REITS

REIT	Specialism	Five-year total return (%)
Safestore	Self-storage	195.0
Segro	Warehouses	168.0
Unite	Student accommodation	94.9
Urban Logistics REIT	Warehouses	73.2
Big Yellow	Self-storage	68.6
Tritax Big Box REIT	Warehouses	65.9
Primary Health Properties	Healthcare facilities	65.7
Londonmetric Property	Warehouses	63.2
Secure Income REIT	Diversified	60.7
Assura	Healthcare facilities	50.3

Source: SharePad, data to 11 May 2021

REITS – THE FINE PRINT

To qualify as a REIT, a company needs to be listed on a recognised stock exchange and must distribute 90% or more of its tax-exempt income (principally the rent paid by tenants) to investors.

These distributions are normally paid after deduction of withholding tax at the basic rate of income tax (20%), which the REIT pays to HMRC on behalf of the shareholder.

A REIT pays corporation tax on any profit it makes apart from through rental income, such as trading property or asset management fees, and any dividends paid out of this income are paid as normal company dividends, so without a withholding tax.

FTSE 100 REITS

Two high profile equity REITs are **British Land (BLND)** and **Land Securities (LAND)**. Both are constituents of the FTSE 100 and they take a diversified approach to investing in property, with their portfolios including shopping centres and offices.

Another FTSE 100 REIT is **Segro (SGRO)**. It is more specialist and focuses on warehouses – a seemingly dull area which has been rendered 'hot' by the growth of e-commerce and the need for businesses to store, manage and distribute products sold over the internet.

WHAT TO LOOK FOR

While different types of REIT will have different risk profiles and sensitivities to the wider property market there are three main metrics to judge them on. These are: NAV which stands for net asset value; dividend yield; and the total return encompassing dividends and either the growth in NAV or the share price.

REITs can and do trade at discounts and premiums to their NAV which is total assets minus total liabilities.

For example, Segro trades at a 30% premium to its NAV, while **Town Centre Securities (TOWN)** which is exposed to a structurally challenged high street and trades at a 50% discount.

If a REIT trades at a premium to NAV it would typically suggest that the market thinks the value of its properties is set too low or is poised to increase, whereas if it trades at a discount to NAV then the opposite is true, investors clearly believe valuations have further to fall.

THE IMPORTANCE OF YIELD

The other key thing to look at is the dividend yield. Within this it is also useful to look at the net initial yield on the property portfolio – which is the ratio of rental income to the valuation at which the property was acquired.

In 2019 giant warehouse investor **Tritax Big Box REIT (BBOX)** moved into developing assets because the yields from buying operational assets fell to levels that would struggle to have supported the level of dividends it had paid historically.

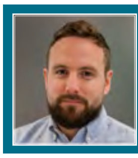
'A high yield has the potential to boost the NAV total returns, but it is crucial to understand how sustainable this dividend yield is and so you need to examine dividend cover too - calculated by dividing EPRA earnings per share by dividend per share,' says Rees at Numis.

'If the REIT is paying an uncovered dividend then this will have to be partly funded from capital and so is actually eroding the NAV. This might not be a problem for a short period but could become an issue if the company is consistently paying an uncovered dividend.'

ASSET DIVERSIFICATION

It is worth considering how diversified a REIT is in terms of number of tenants and number of properties. For example, if it is reliant on one or two large tenants which run into financial trouble, or a single asset which fell in value, this would have significant implications for performance.

Also, you could look to see if its rental agreements include a link to inflation and the source of the rental income. Some REITs, such as health care facilities landlord **Assura (AGR)** and social care specialist **Civitas Social Housing (CSH)**, receive government-backed income streams either directly or through local authorities and housing associations which should be more reliable than commercial rents.



By **Tom Sieber**
Deputy Editor

The nuances of value investing

With value stocks continuing their rise, distinguishing between different 'value' fund offerings can be challenging. Here, we look at a unique multi-asset value strategy...

It is unusual for global investment markets to move almost completely as one, with such moments usually coming at times of crisis. But in the last few months, a singular trend has driven markets, fuelled by good news and the rising tide of global stimulus.

The rotation from growth into value was almost unprecedented, after a decade in which growth stocks had dominated the markets, marked most notably by the near exponential growth of the FAANGs. Indeed, at the point of the rotation the valuation gap between growth stocks and value stocks was at a record high, leaving some to suggest that value investing might be over for good.

Of course, rumours of the death of value investing were greatly exaggerated. In the six months to 12 April 2021, the MSCI ACWI World Value Index returned 17.71%, against a 7.37% return for the MSCI ACWI World Growth Index.

TAPPING INTO THE VALUE REVIVAL

Unfortunately, many investors were caught out by this rotation. As growth continued to flourish through the 2010s, many funds opted or were forced to change their investment approaches to a more growth-focused style. As a result, portfolios were often wholly or largely growth-oriented as the value rally began in November.

While investing on a backward-looking basis alone is rarely a good plan, several financial institutions, including JPMorgan and Barclays, have said that they believe the rally has further to run. One key driver is the gradual re-opening of major economies such as the UK and US, prompted by successful vaccination programmes. With governments indicating that they are likely to continue providing economic stimulus through extended welfare programmes for some time to come, it seems likely that a pent up spending spree is on the horizon.

Naturally, investors are now looking to add more value exposure to their portfolios. However, with so many funds on offer, it is worth considering what this actually means.

For some, a value allocation focuses almost exclusively on so-called "distressed" stocks, the kinds of companies that have experienced such challenging operational environments in recent years that some investors believe they cannot recover. An example here would be cinema chains, or even GameStop, prior to its Reddit-fuelled resurgence.

For others though, value is more nuanced. For the managers of **Momentum Multi-Asset Value Trust (MAVT)** this includes applying a value lens to a broad range of asset classes, and on a global basis too.

REFINED VALUE

MAVT has long been managed with a distinctive "refined value" approach. In practice, this means applying the same value lens the managers use for their directly-held UK stocks to a broad variety of asset classes located globally, accessed largely through third-party funds.

This combination is unique, offering investors a 'core' value allocation, alongside a differentiated approach to value in the other half of the portfolio. This combination also helps prevent the fund from being too defined by its value style, and the portfolio as a whole does not show a technical bias towards value, even as the managers use this as their investment lens.

The team is finding opportunities on both sides of their portfolio. On the UK equity side, the team agrees with the institutions that the value rally has a while to run yet and have maintained their already-overweight exposure in recent months on the basis of this conviction.

This is being driven by both bottom-up and top-down observations, with the team identifying the UK market as a whole as undervalued and reporting finding numerous attractive stock-specific ideas. UK leadership relative to global peers on vaccine deployment should enable the economy to recover quicker, and a pathway to economic reopening gives the team increased confidence in consumer-facing holdings which had been punished in 2020.

On the other hand, the team are finding a number of contrarian opportunities for the other half of the portfolio. As investors have become more accustomed to the value in renewable assets, these have included more esoteric and specialised ideas in this theme. An example is Cordiant Digital Infrastructure, which invests in digital economy infrastructure like fibre optics cables, following its IPO in February.

Click **here** to read more on the value-led strategy of Momentum Multi-Asset Value Trust...

RUSS MOULD
AJ Bell Investment Director

Commodities remain central to the FTSE 100

Examining the contribution of mining and oil and gas to dividends and profit from the index

No sooner had this column raised the question as to whether its status as the single-best performer within the FTSE 350 over the last five years meant that the good news was all in the price for the Industrial Metals and Mining sector than the grouping promptly fell out of bed.

Sharp share price falls last week reflected easing investor concerns over inflation, as central bankers trotted out soothing commentary, and a pull-back in iron ore prices as China reportedly sought to cool a red-hot market. Such is the curse of the commentator.

It still remains to be seen whether galloping factory gate price inflation – where the latest readings from China and the USA are 6.8% and 6.2% respectively – translate into a sustained increase in consumer prices, and that one forces central banks to ease off on quantitative easing (QE) or even raise interest rates.

But markets remain sceptical that the current burst higher in raw material prices will last. Analysts' forecasts for miners' earnings are one indicator of this, as estimates imply a drop in the big diggers' earnings in 2022 and 2023, as discussed here last week.

This can be seen in another way. Miners are expected to generate 29% of the FTSE 100's pre-tax profit and 22% of its dividends in 2021, but the big seven stocks represent just 12% of its current market cap.

That again implies that analysts do not believe 2021's raw materials price boom and miners' profit surge is sustainable. That has potential implications for investors who like to pick individual stocks or those who prefer to glean their access to the UK equity market via funds, whether they are actively managed or passively run.

BLACK STUFF

Further advances in commodity prices could mean the FTSE 100, and instruments that seek to track its performance, offer further upside potential. The same could be said of dedicated mining funds or UK equity collectives with overweight positions in mining stocks.

But the FTSE 100 does no offer just exposure to precious and industrial metals, when it comes to the commodities complex. It is home to two of the world's oil majors, **BP (BP.)** and **Royal Dutch Shell (RDSB)**. The price of crude is more than double the level of a year ago and earnings are expected to

Miners' aggregate market cap implies analysts feel 2021's forecast profits are not sustainable

	Percentage of FTSE 100 market cap	Forecast percentage of FTSE 100 pre-tax profit 2021E	Forecast percentage of FTSE 100 dividends 2021E
Financials	20%	22%	18%
Consumer Staples	17%	16%	18%
Industrial goods & services	13%	8%	8%
Mining	12%	29%	22%
Consumer Discretionary	11%	4%	5%
Oil & Gas	8%	10%	10%

Source: Refinitiv data, Markestcreener, consensus analysts' forecasts

RUSS MOULD
AJ Bell Investment Director

Oils are expected to be the FTSE 100's biggest profit growth generator in 2021

	Percentage of forecast FTSE 100 profits growth 2021 E	Forecast profits growth (£ billion) 2021 E
Oil & Gas	**37%**	**27.5**
Mining	**30%**	**22.8**
Consumer Discretionary	11%	8.2
Financials	9%	6.9
Industrial goods & services	8%	5.7
Consumer Staples	4%	3.0

Source: Company accounts, Marketscreener, consensus analysts' forecasts

rocket here as a result.

However, unlike the miners, the oils are not expected to provide much by way of dividend growth in the wake of last year's cuts from both BP and Shell. Scepticism about the future of oil prices is also reflected in how the oil's percentage contribution to the FTSE 100's market cap (8%) reflects their forecast contribution to profits and dividends this year (10%).

Oils not expected to generate higher dividends in 2021

	Percentage of forecast FTSE 100 dividend growth 2021E	Forecast dividend growth (£ billion) 2022E
Mining	**47%**	**6.0**
Financials	36%	4.6
Consumer Discretionary	9%	1.2
Industrial goods & services	8%	1.0
Telecoms	5%	0.6
Consumer Staples	2%	0.3
Real estate	1%	0.1
Technology	1%	0.1
Utilities	1%	0.1
Health Care	-2%	-0.2
Oil & Gas	**-8%**	**-1.0**
	100%	**12.8**

Source: Company accounts, Marketscreener, consensus analysts' forecasts

GREEN DRIVE

Yet in some ways, the investment case for oils is similar to that of the miners: demand has collapsed but could rebound if the economy picks up strongly in the wake of the pandemic while supply growth is limited. BP and Shell's forecast combined capex-to-sale ratio of 6.6% in 2021 is lot nearer to its recent lows than its highs.

Better still, unlike the miners, whose shares have done well, the oils are loathed. BP and Shell's market cap contribution to the FTSE 100 stands near its lows for this century.

Big oil is still out in the cold with investors

Source: Refinitiv

This may reflect ethical and environmental concerns as much as it does financial and operational ones, as well as the prospect that the world is trying to move away from hydrocarbons as fast as it can. But the globe relies on oil not just for fuel but for vital lubricants, plastics and chemicals, which could be around for a good while yet, whether we like it or not. And it will take time before renewables provide more power than oil and gas.

Perhaps 'Big Oil' could be more capable of providing an upside surprise in the event of an inflationary recovery than the miners, to the benefit of UK equities.

Although we cannot discount the possibility that BP and Shell's hefty investments to pivot away from oil and gas help them politically and benefit wider society without bringing them much by the way of financial benefit, owing to the (rising) costs involved.

Diageo plans to repurchase £1 billion worth of stock

The case for and against share buybacks

Research shows outperformance versus peers but claims of financial engineering persist

UK companies are setting the scene to repurchase more than £8 billion of their own shares this year. Barely a year after the outbreak of Covid-19 led to a huge move by companies to protect their balance sheets and conserve cash, share buybacks are again all the rage.

Since the start of May consumer products giants **Unilever (ULVR)** and **Diageo (DGE)** have unveiled plans to repurchase approximately £2.6 billion and £1 billion worth of stock respectively in 2021. They will join a lengthening list including many of Britain's biggest businesses in buying back their own shares this year, including **Barclays (BARC)**, **BP (BP.)**, **IMI (IMI)** and **Natwest (NWG)**.

Share buybacks have always been a prickly issue. For ordinary investors, it is all but impossible to determine whether stock repurchases boost a company's share price as they are meant to.

Take IMI, for example. On 26 April the FTSE 250 engineering business announced a share buyback programme worth £200 million alongside an upbeat trading update. The news saw IMI's share price jump 11% to £15.52, and the stock has gone on to £16.50. That's an 18% share price increase that has added approximately £660 million to IMI's market value, more than three-times the value of the share buyback itself.

Importantly, the trading statement suggested that IMI will be funding the buyback out of cash flow rather than borrowing and management makes it clear that investment in growth, either organic or by means of acquisition, still comes first.

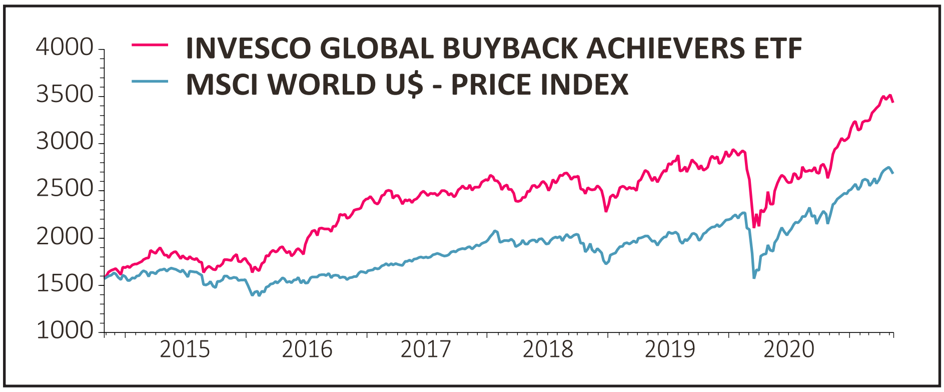
VALUE CREATION FIRST, BUYBACKS LAST

This is important since share buybacks should only happen if a company has nothing better to spend its surplus cash on, such as, for example, investing in new products, services, equipment, or acquisitions, which might bolster future growth.

£8 billion of UK buybacks announced in 2021

Company	Amount (£m)
Unilever	2,600
Natwest	1,130
Diageo	1,000
Barclays	700
BP	360
Sage	300
Ferguson	290
CRH	216
IMI	200
Spectris	200
Quilter	187
Standard Chartered	181
South32	180
Balfour Beatty	150
Berkeley Group	129
Domino's Pizza	45
Glanbia	44
Arix Bioscience	25
Contour Global	23
Plus500	18
Zytronic	10
CML Microsystems	8
Griffin Mining	7
Raven Property	7
Somero Enterprises	1
Trans Siberian Gold	1
D4t4	0.3
Gamesys	TBC
IP Group	TBC
Rightmove	TBC

Source: Company announcements



'If a company has taken all profitable investment opportunities, it should return its surplus cash to shareholders, allowing them to invest it in growing companies elsewhere in need of financing,' said Alex Edmans, professor of finance at London Business School.

Orbis Investments' UK director Dan Brocklebank believes the purchase price of a share buyback is important versus the intrinsic value of company. 'If the share price is lower than the company's intrinsic value, remaining shareholders benefit,' he says.

Intrinsic value refers to the underlying value of the company and analysts typically use discounted cash flow analysis to determine this. These are complex calculations based on implied future cash flows discounted by the cost of capital, which is linked to interest rates.

In IMI's case, its recent trading update saw Investec lift its intrinsic value per share from £15 to £17.65, suggesting that IMI's recent stock repurchases at up to £16.43 are adding value for shareholders.

However, discounted cash flows do rely on a level of 'butterfly effect' supposition, or in other words, small unexpected changes in estimates can add up to huge miscalculations over time.

Sceptics argue that this leaves share buybacks open to abuse and can be used to financially engineer the impression of earnings enhancement where there has been none.

Worse, 'buybacks create a sugar high for the corporations,' US senator Elizabeth Warren claimed during the presidential campaign last year, boosting share prices in the short run but at the cost of starving companies of investment and, potentially, falsely inflating earnings to trigger executive bonuses.

NO EVIDENCE OF BUYBACK ABUSE

However, research commissioned by the UK Government to look at potential misuse of share buybacks among companies listed on the London stock market found no evidence of abuse. 'Over 2007 to 2017, we found that not a single FTSE 350 firm used buybacks to hit an EPS (earnings per share) target that it would have otherwise missed,' said Alex Edmans of London Business School and co-author of the study alongside PwC.

This builds on a seminal paper that found that firms who buy back stock subsequently outperform their peers by 12.1% over the next four years. 'This finding is surprisingly robust,' said professor Edmans. While the research was conducted in the US during the 1980s, a more recent study (from 2018) investigated 31 other countries and found that the results hold in most of them, he said.

'This evidence contradicts the "sugar high" concerns but is conveniently ignored in claims that buybacks destroy long-term value.,' said the London Business School academic. However, he does accept that 'buybacks can destroy value in certain cases'.

MEASURING THE IMPACT OF BUYBACKS

One way to assess the long-run value of share buybacks is to look at the performance of the London-quoted **Invesco Global Buyback Achievers ETF (SBUY)**.

It aims to match the performance of the NASDAQ Global Buyback Achievers index, a basket of firms which have reduced their share count through buybacks by at least 5% over the previous 12 months, although it is dominated by US firms (60%), with just 2% from the UK.

The ETF is up 50% from its March 2020 lows, outpacing the recovery in the MSCI World which is up by 43% over the same time-frame.

Since its launch in October 2014 the product's price has advanced 119.7% against a commensurate 74% rise for the MSCI World.

By **Steven Frazer**
News Editor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Investing & Pensions
GOLD AWARD
Autumn 2020
Capital at risk.
Pension rules apply.

Should I use a SIPP or an ISA for retirement savings?

Our resident expert on the merits of the two tax wrappers when it comes to building up your pot

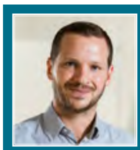
I have both an index linked personal pension and an employee salary sacrifice pension which was started in 2016. I am hopefully going to finish paying my mortgage in the next two or three years and want to invest an extra £100 a month for retirement.

I am torn between using my Stocks and Shares ISA (which is not anywhere near my annual allowance even if I decide to use this for the £100) or opening a SIPP.

I am aware that the SIPP will offer the basic tax relief top up of 20% and I can take 25% tax free when I crystallise the SIPP, whereas there is no tax to pay whatsoever on any money I withdraw from a Stocks and Shares ISA.

Which would be the better option? Or would a split between the two be a good idea?

Lee



Tom Selby
AJ Bell
Senior Analyst says:

Deciding whether to invest your money in a pension or an ISA will depend on a number of things including your goals and personal circumstances. While the tax impact is also important, it should be considered alongside these other key factors.

If you are willing to keep your money locked up until age 55 (57 from 2028), from a purely tax perspective a pension will usually give you a bigger bang for your buck than an ISA.

This is because pensions benefit from basic-rate tax relief upfront – extra money which can then benefit from compound growth over time. ISAs, on the other hand, are more flexible, benefitting from tax-free withdrawals at any time but offering no upfront bonus.

The income your pension generates – and how it compares to what you might get from an ISA - will depend in part on how you manage your withdrawals.

AN EXAMPLE

Take, for example, someone who saves £1,200 a year – equivalent to £100 a month – in a pension and an ISA. Each contribution to the pension would be topped up with basic-rate tax relief, taking the total amount invested to £1,500 a year.

If both the pension and ISA enjoy 4% annual investment growth after charges, after 30 years the pension could be worth around £87,500 while the ISA could be worth £70,000.

If the pension saver was a higher-rate taxpayer or additional-rate taxpayer, they could also have claimed extra tax relief from the taxman.

While the ISA would be accessible entirely tax-free at any time, a quarter of the pension pot (£21,875) would be available tax-free, with the rest (£65,625) taxed as income. How much they receive from this taxable portion would depend on their rate of income tax.

If we assume there is no more investment growth from the point they access their pension:

- If taxable withdrawals are within the personal allowance each year and therefore taxed at 0% then they would get £87,500 of income from their pension;
- If taxable withdrawals are taxed at 20% they would get £74,375 (£21,875 tax-free cash plus £52,500 income after tax) from their pension;
- If taxable withdrawals are taxed at 40% they would get £61,250 (£21,875 + £39,375) from their pension;
- If taxable withdrawals are taxed at 45% they would get £57,969 (£21,875 + £36,094) from their pension.

Where withdrawals cut across two different tax bands the actual tax someone pays will be different to those set out above. But provided pension withdrawals are taxed at 20% or less then, from a purely tax perspective, a pension should deliver more income than an ISA.

OTHER CONSIDERATIONS

There will, of course, be other considerations when choosing between a pension and ISA other than purely the income it could potentially generate.

Flexibility will be important for lots of investors, and on this front an ISA offers much readier access to your cash before age 55 (57 from 2028) than a pension.

The difference in tax treatment on death is also worth bearing in mind. While ISAs will form part of your estate for inheritance tax (IHT) purposes, pensions in most circumstances will not.

In fact, pensions can usually be passed on tax-free to your beneficiaries if you die before age 75, and are subject to income tax when beneficiaries come to access the money if you die after your 75th birthday.

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.

Protecting your pension income from inflation

Rising prices can really hurt retirees but there are steps you can take to ease the pain

Markets are getting increasingly worried about inflation, with the US recently registering consumer price rises of 4.2% in a year. Here in the UK, CPI still stands at just under 1%, but inflation expectations are mounting, thanks to the strong economic rebound expected in 2020.

Indeed looking at prices in government bond markets, inflation expectations have climbed to their highest levels since 2008 (see chart).

INFLATION PARTICULAR PROBLEM FOR PENSIONERS

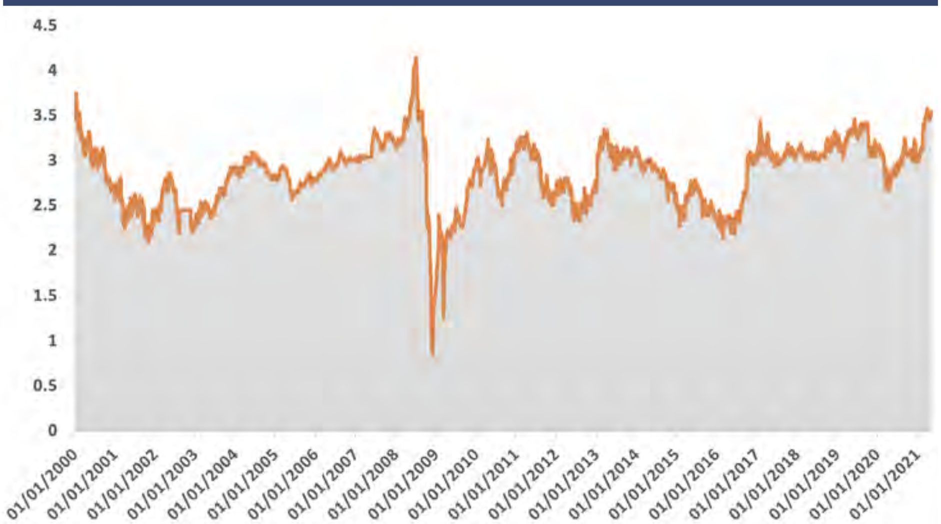
High inflation isn't a friend to anyone, but it can be particularly harmful for pensioners, because they are typically no longer earning wages, or building up their savings, so they rely on the inflation protection built into their retirement assets to help to offset price rises.

Savers hitting retirement therefore need to carefully weigh up their options in terms of protecting their pension pots from inflation.

Those lucky enough to have final salary pensions entitlement built up will happily find that their income in retirement rises each year with inflation. State pension entitlement also rises with the minimum of inflation, wages or 2.5%, so there's some protection from rising prices there too.

However personal pensions don't have any inflation-linking built in, so you need to engineer it yourself, particularly if you're planning to use some, or all, of your pension pot to buy an annuity.

UK 10 year inflation expectations %



Source: Bloomberg 10 year government bond breakevens 12th May 2021

HOW ANNUITIES ARE AFFECTED

Annuities offer savers the ability to turn money held in a personal pension or SIPP into a guaranteed income for life. However, a standard annuity comes with no inflation protection, it pays the same amount of income each year for the rest of your life. If you're retiring at 65, and live to 85, that's a 20-year period, over which even modest inflation can seriously erode the buying power of a fixed income, let alone the higher rates of inflation which are increasingly troubling markets at the moment.

You can buy an inflation-linked annuity, where the income you receive increases each year in line with consumer prices. This protects you from inflation, but the cost of this insurance is high.

Whereas a standard level annuity will pay a 65-year-old around £5,000 a year for each £100,000 pension pot, an inflation-linked annuity will only pay out around £3,000 a year to begin with. Of course this will rise over time with inflation, but investors need to be very patient for the pay off, to say the least.

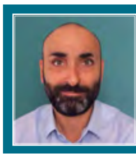
Another option which has become much more popular since the pension freedoms were introduced, is to keep your pension invested, and draw an income from your portfolio. Dividends from the stock market should rise over time, boosting your income, and providing useful ammunition in the fight against inflation.

However, unlike an inflation-linked annuity, there's no guarantee they will keep pace with inflation. They are also variable, and in some years, like 2020, will fall. However, combined with the risk and potential reward of a fluctuating capital value, as share prices go up and down, there is the potential for investors to come out ahead of inflation over the long term.

A MIX AND MATCH APPROACH

A retirement income strategy should always include a consideration of the effects of inflation, but right now, as we hopefully emerge from the pandemic, it's a particularly relevant issue. Pension savers approaching retirement don't have to choose just one of the three income options highlighted above.

In fact, a mix and match approach probably has the best chance of striking the right balance between inflation protection for the future, and enjoying a decent income stream in the here and now.



By **Laith Khalaf**
Financial Analyst

INVESTOR DIARY

Hunting for value and growth

Finding stocks on AIM and how a 'rule of 20' is helping with investment decisions

We're pleased to welcome back Malcolm from Edinburgh who is sharing his experience as someone in retirement taking charge of their investments for the first time.

After a year-and-a-half of taking responsibility for investing for retirement through my SIPP and Stocks and Shares ISA, matters are becoming clearer. There is no going on endless holidays and checking my portfolio once a fortnight, but there are smaller signs of organised progress.

After setting aside £30,000 for family contingencies, I have 13 shares invested in FTSE 100 and FTSE 250 companies and four in the FTSE AIM 100. Over the 18-month period and buoyed by recent share increases my return on investment is 6.4%, not including dividends, a pleasing result and more than could have been achieved through saving schemes.

PORTFOLIO PLANNING

In my previous column I evaluated whether investing in 30 shares was too many. However, after reviewing the outlay amount in terms of portfolio percentage, an active investment of £200,000 equates to an average £6,600 (3.3%) investment per share. In terms of risk/reward and maintaining a diversified portfolio this appears reasonable to me.

I tend towards investing higher amounts in 'value' shares in the FTSE 100 and FTSE 250, for example **Admiral (ADM)**, **Aviva (AV.)**, **Diageo (DGE)**, **Redrow (RDW)**, **UDG Healthcare (UDG)** and **Unilever (ULVR)**, and lower amounts in 'growth' shares in these indices and the FTSE AIM 100. The terms value and growth are slightly amorphous given that many companies are adapting their business model, but the general notion is helpful.

Shares in new and emerging technologies are more obvious 'growth' shares e.g., **Blue Prism (PRSM:AIM)**, **Gamma Communications (GAMA:AIM)**, **GB Group (GBG:AIM)** and **ITM Power (ITM:AIM)** from the AIM market. As these shares can fluctuate quite markedly, the amount invested in them is lower, typically £4,000 relative to the £6-£8,000 I have placed in most value shares.

LOOKING TO AIM FOR EXCITEMENT

AIM is where I find the excitement though. Take, Blue Prism, where software robots are being developed to automate routine back-office clerical tasks. ITM Power aims to take excess energy from the power network,

convert it into hydrogen and reuse it in industry. What is not to admire about these new and bold ideas?

In share price terms some hybrid value/growth investments have fared better than others. **SSE (SSE)** has moved relatively successfully from an electricity network provider to generating power from renewable sources. **BP (BP.)** and **Royal Dutch Shell (RDSB)** have similar green energy aspirations but due simply to the time the shares were purchased, changes in business orientation are not yet reflected in share price gains.

This raises an ongoing issue of what to do with these shares: hold, sell or buy more of them? Arithmetic comes into this; as in my experience, it is easier for a share/business to half in value than double in value. A £10 share can quite quickly become a £5 share, but it is more difficult for the same £5 share to become a £10 share again.

For this reason, when evaluating companies, I try to review their loss as well as profit making potential. Increased attention is paid to resilience and whether there is something sufficiently distinctive about certain companies that might generate sustained earnings growth during economically volatile times.

'RULE OF 20'

Added to these reviews is my new 'rule of 20' i.e., if a share either falls or rises more than 20% from its purchase price, then it is time to walk around the garden to review whether to sell. I neglected this approach in my earlier investment days and am still holding poorly performing shares in **GlaxoSmithKline (GSK)**, **Smith & Nephew (SN.)**, **Vodafone (VOD)** and **Wood Group (WG.)**.

Adopting the rule of 20 for shares in surplus has worked better. Reinvestment favourites **Drax (DRX)**, **Hills & Smith (HILS)**, **Howden Joinery (HWDN)**, **Kainos (KNOS)**, **Melrose Industries (MRO)** and **Persimmon (PSN)** have risen appreciably in share price at selected times; often to be followed by sufficient dips to enable rebuying to straightforwardly take place.

Arguably, such profit taking is rather short-term thinking, but it accounts for most of the 6.4% return. Shares in **Reckitt Benckiser (RB.)** highlight the point. For most of 2020 they were my standout performer. Yet I did not sell, and the shares have been in deficit for many months.

The same thing occurred with **Scottish Mortgage Trust (SMT)**. As buying and selling shares is simple, quick and relatively inexpensive, it feels like an opportunity lost. It also highlights that most of the profit gain has come through a relatively small number of companies. As trust in these companies rises, my level of investment in them is likely to increase.

KEEPING THINGS UNDER REVIEW

As for the future, the priority is to read well, to review factors influencing markets and study possible new investments in terms of their contribution and performance figures. No longer is the business supplement in the Sunday papers discarded. I also watch out much more closely than previously to when companies publish their first-half or full year results. This can often lead to excessive price volatility, which might merit a response.

Making progress continues to be a quite serious matter but also a strangely satisfying one and one which for the present is preferable to pursuing a more funds-based, laissez faire investment approach.

KEY ANNOUNCEMENTS OVER THE NEXT WEEK

Full-year results

21 May: Investec. **24 May:** Kainos, Randall & Quilter, Sirius Real Estate. **25 May:** Aveva, Big Yellow Group, Calnex Solutions, Electrocomponents, Helical, Hurricane Energy, Speedy Hire, Warehouse REIT. **26 May:** ASA International, Biffa, De La Rue, Marks & Spencer, Mediclinic International, SSE. **27 May:** Caledonia Investments, Invinity Energy Systems, Johnson Matthey, LondonMetric Property, PetsAtHome, Picton Property Income, Ted Baker, United Utilities.

Half-year results

21 May: Electra Private Equity. **25 May:** Avon Rubber, Greencore, Ixico, Shaftesbury. **26 May:** Auction Technology, Oxford Metrics. **27 May:** Daily Mail & General Trust, Impax Asset Management.

Trading statements

21 May: Close Brothers. **26 May:** Intertek. **27 May:** Aviva.

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