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Contents

Daniel **Coatsworth**

Rejoice! The retail investor is no longer being ignored for share placings

A new service means big investors aren't the only ones being offered stock on the cheap

At 4.36pm on 10 August, industrial thread manufacturer **Coats (COA)** announced its second acquisition in as many months. Not only was this unusual behaviour in that Coats rarely buys companies, but it also asked retail investors for financial help.

Historically Coats has relied upon bank debt for financing and used that money, along with internally generated cash, for deals.

The fact retail investors were offered a chance to buy shares at a discount to the market price is important. It shows how Coats as a business has found new momentum and appetite for strategic acquisitions. Perhaps more significant is that it is one of a growing number of companies treating retail investors with more respect.

Letting retail investors take part in share placings means institutional investors are no longer getting preferred treatment. Having a level playing field has long been desired by smaller investors, and technology is helping to achieve this goal.

Coats used the new REX fundraising platform which is owned by **Peel Hunt (PEEL:AIM)**, the broker and corporate financier. It is very similar to the share placing facility offered by PrimaryBid.

Customers of various investment platforms including AJ Bell receive an alert when one of their portfolio holdings is doing a share placing open to retail investors. The recipient must decide if they want to buy more shares or have their stake in the business diluted.

Investors typically have a short period – often just an hour – to apply for shares in the placing. They are either told the price in advance, or as we saw with the Coats deal, they place an order, and the price is agreed once the placing is done.

While this greater opportunity to take part in placings is a good step forward, it is by no means perfect. Most of the placings happen after the stock market is closed for the day, so any retail investor without cash in their ISA or SIPP cannot sell an existing position in a different stock to raise money to fund their share placing application.

There is the odd exception. Take TV producer **Zinc Media (ZIN:AIM)** which ran a placing including a retail investor component during market hours on 3 August.

If you're not paying attention to messages from your investment platform provider, or studying the stock market announcements like a hawk, it's easy to miss the placing opportunity. No-one is going to proactively phone a retail investor like a broker might do with institutional clients to alert them.

The take-up of recent retail offers hasn't been exceptional. For example, Coats only raised £433,103 from retail investors, and Zinc Media got £37,059 from this audience. That might be partially explained by the placings having happened during the quiet period when investors were on the beach.

What should be applauded is the fact the placings were offered to retail investors in the first place. It aligns with a push by the Government to make retail investors a more important source of funding for companies, so it might be worth checking your messages just after 4.30pm each day, as you never know which opportunity has come knocking.

DISCLAIMER: AJ Bell referenced in this article owns Shares magazine. The author (Daniel Coatsworth) and editor (Tom Sieber) of this article own shares in AJ Bell.

Dampening inflation helps drive rally in US and UK equity markets

Recent data suggests that US inflation may have peaked, prompting investors to anticipate the Fed will ease

The recent rally in US equity markets has been driven by figures showing the level of US inflation may have peaked.

Since its most recent low on 16 June the S&P 500 index has rallied by 16.7%.

The UK equity market has also risen during this period but to a far lesser extent with the FTSE 100 and the FTSE 250 rising by 6.7% and 8.6% respectively.

US consumer prices jumped 8.5% in July compared with the same month a year earlier, down from the 9.1% year-on-year increase in June.

As a result investors are now starting to factor in a shift in approach from the US Federal Reserve, implying less aggressive interest rate rises.

The stocks moving higher

Top performing S&P 500 stocks since 16 June	
Enphase Energy	76.5%
Etsy	73.8%
Netflix	43.8%
Ford Motor Co	43.6%
PayPal	41.9%
Tesla	40.8%
Amazon	38.5%
Top performing FTSE 100 stocks since 16 June	
Avast	43.5%
RS Group	41.0%
Scottish Mortgage Investment Trust	37.1%
Auto Trader	32.4%
Flutter Entertainment	30.9%

Table: Shares magazine • Source: Sharepad, data to 15 August 2022

The table shows the magnitude of some of the gains made by individual US stocks since 16 June, some of which have also been supported by strong second quarter earnings reports.

Shares in **Amazon (AMZN:NASDAQ)** have surged by 38.5% since 16 June. Its second quarter update showed 7% revenue growth, aided by an uptick in Amazon Web Services bookings, with total revenue coming in at $121.23 billion versus the $119.09 billion estimate.

Electric vehicle maker **Tesla (TSLA:NASDAQ)** advanced 40.8% over the same time-frame. Its earnings in mid-July beat consensus estimates. Revenue came in at $16.9 billion and earnings per share at $2.27. Tesla shareholders also approved a three-for-one stock split which will take effect on 25 August.

Shares in streaming platform **Netflix (NFLX:NASDAQ)** have also rallied, supported by results which were not as bad as feared.

The UK stock market has experienced more muted gains than its counterpart across the Atlantic. This is in part due to its bias towards areas like commodities and financials which typically trade on lower valuations. The FTSE 100 had also held up better than the S&P 500 in the first half of 2022.

Growth orientated stocks are more sensitive to changes in interest rate expectations than so-called 'value' stocks.

However, several UK companies have performed particularly strongly.

Avast (AVST) has risen 43.5% after the UK Competition & Markets Authority said it has provisionally cleared NortonLifeLock's acquisition of the cybersecurity firm, following an in-depth probe of the deal. [MGar]

Watches of Switzerland sales soar despite cracks in timepiece market

High-end seller shrugs off wider market worries as first quarter sales surge 31%

Shares added luxury watches and jewellery seller **Watches of Switzerland (WOSG)** to its *Great Ideas* list at 792.4p on 16 June 2022. We argued the group's global growth journey was just getting started and demand for luxury watches continued to outstrip supply.

A trading update on 16 August was an important test for the share price given recent uncertainties over the state of the pandemic-boosted watch market caused by surging inflation, the cryptocurrency collapse and concerns over a global recession.

Recent reports suggested that luxury watch prices on the secondary market were falling, presenting a risk that trend spreads into the primary market where Watches of Switzerland operates.

Reassuringly for our 'buy' thesis on Watches of Switzerland, there are no signs of primary channels seeing a demand dip thus far, and the shares ticked up 3.3% to 913p as the company delivered a robust update for the 13 weeks ending 13 July.

Watches of Switzerland also reiterated full-year guidance, albeit with the outlook factoring in a 'potentially more challenging' trading environment in the second half.

Group sales were up 31% year-on-year to £391 million despite tough comparatives, while management highlighted a continuing strong luxury watch market in the UK and the US, where sales doubled year-on-year.

'The first quarter continued with strong momentum throughout, and we carry this positive momentum into the second quarter,' insisted chief executive Brian Duffy, now expanding the business into Continental Europe. 'Despite the well-publicised concerns about the macro-environment, demand for our products remains robust with client registration of interest lists continuing to extend,' he added.

Affluent consumers are still spending money as inflation doesn't massively impact their lifestyle, supporting strong sales of luxury goods.

Bears may believe the luxury sector is at peak sales and profit, but BofA Securities has found that luxury demand accelerated in July compared with the second quarter and the month of June in Asia, the US and Europe, boosted by the return of international travel. China demand started to normalise in June and continued to do so in July, added BofA Securities.

Premium watches are seen to be a good investment as editions are limited and there are plenty of people who want to own them. Yet if second-hand prices are falling, that dilutes their appeal from an investment perspective. It's something to watch, particularly if second-hand prices for luxury watches fall below retail prices. Reports suggest we're a long way off that happening. [JC]

Watches of Switzerland

Chart: Shares magazine • Source: Refinitiv

Deliveroo and Just Eat Takeaway facing hard road to recover enormous losses

Shareholders have been the big losers in the food delivery platforms fight

Food delivery volumes more than doubled through the pandemic, yet profits remain elusive for many popular platforms, including **Just Eat Takeaway (JET)** and **Deliveroo (ROO)**, following a wave of a new investment chasing an expanded addressable market.

Data from Daxue Consulting and Bloomberg estimates the UK market was worth $6.7 billion in 2021, with $9.2 billion revenues across mainland Europe.

While analysts agree that local scale remains paramount to network effects, global scale is proving a double-edged sword as battle lines are redrawn.

This week saw shares in meal kit provider **HelloFresh (HFG:ETR)** rally after strong interim results showing €89.5 million of net profit. With a reported €642 million of cash, it is also buying back its heavily discounted stock after plunging more than 50% in 10 months.

Deliveroo and Just Eat have been successful in passing rising costs on to consumers, illustrated by revenue rising faster than overall orders, or GTV (gross transaction volume) as it is sometimes called. How far and for how long diners will be willing to stomach rising prices for home-delivered dinners remains to be seen, but investors should beware.

Marketing costs continue to rise sharply too. In the six months to 30 June, Deliveroo's marketing spend soared from £286.2 million a year ago, to £368.8 million, or from 8.6% of GTV to 10.4%, helping explain ballooning losses, up 261% to £68 million.

Berenberg analysts estimate that Just Eat will run up nearly €800 million in net losses this year, and that's presuming further cost control initiatives in the second half. The investment bank certainly isn't buying management's talk of positive-adjusted EBITDA in fiscal 2023. Berenberg forecasts net losses of €530 million and €378 million for 2023 and 2024, respectively.

Just Eat is also tackling the aftermath of its Grubhub acquisition folly in the US, which it is trying to sell. Just Eat earlier in August booked a €3 billion loss on Grubhub, bought for $7.3 billion last year. That is arguably yet to fully reflect the financial millstone Grubhub will end up being, with some analysts predicting a final sale price of less than $1 billion.

With Numis predicting that Just Eat's cash forecasts need to come down by circa €280 million this year to around €608 million, it could result in 'immediate liquidity concerns and potentially require a fire sale of assets at the expense of equity shareholders.'

Most growth stocks have declined this year as inflation and recession spooked equity investors. Yet the rot had set in on Deliveroo and Just Eat before the market's de-rating, losing 74% and 84% respectively from their highs. Recovering those losses may be beyond both companies. [SF]

Thungela could be crowned the UK market's dividend king

The coal miner is benefiting from surging commodity prices with shares up tenfold in 14 months

Coal producer **Thungela Resources (TGA)** is on a 2022 dividend yield of more than 40%, based on forecasts from Liberum. It is expected to pay above-average dividends for at least two more years.

The scramble for energy as the world emerged from the pandemic and Russia invaded Ukraine has seen thermal coal prices soar and Thungela's shares gain nearly 10-fold on the 150p price at which they started trading after its demerger from **Anglo American (AAL)** last June.

Liberum forecasts 642.2p per share in dividends for 2022 versus 93.1p in 2021. That means it could pay out more than four times the initial cost of the shares in dividends this year alone.

For 2023 the investment bank forecasts Thungela will pay out 357.8p which implies a 23.8% yield based on the current £15.06 share price; and 188p for 2024 which equates to a 12.5% yield.

It is possible the dividend could come in lower than Liberum's expectations if Thungela decided to do an acquisition, thermal coal prices crash, or the production problems linked to the poor performance of South Africa's state-owned rail operator Transnet continue.

In the long term, prospective investors would need to weigh the ethical dilemmas and potential risks of being exposed to a polluting fuel like coal as the world looks to move to net zero and the evidence of the impact of climate change continues to mount. [TS]

Cybersecurity firm Darktrace gains nearly 25% after buyout talks revealed

Investors have endured wild share price swings and may be happy to bank profits

Cybersecurity company **Darktrace (DARK)** is in talks over a possible takeover offer from Thoma Bravo, the private equity firm that has been busy consolidating the wider space in 2022.

Earlier in August, Thoma Bravo struck a deal to buy US-listed Ping Identity for $2.4 billion, its 27th cybersecurity business. It also owns former UK FTSE 250 firm Sophos, plus names like McAfee, Proofpoint and Barracuda.

After a string of upbeat trading updates and growth guidance hikes, *Shares* told readers to buy the stock at 375.13p on 21 April 2022. That the stock has jumped almost 25% since Thoma Bravo's interest became known, suggests that the market sees any deal being struck at a significant premium to recent 400p levels.

A stock market exit could suit all parties if the price is right.

Investors might conclude that going into private ownership is the best way to avoid the uncertainty of this year's market gyrations, with the potential to float the company once again in the coming years once market confidence is restored.

Darktrace shares have seen wild swings since listing in London at 250p in April 2021. In October 2021, the stock hit a record 945p, before plunging. In July the shares were trading at 292.6p.

Thoma Bravo has until 12 September to either make a firm offer or walk away. [SF]

Want to play the rebound in US stocks? Try this fund which has an interesting twist

The Xtrackers ETF has an equal weighting to all the companies in the S&P 500 index

The latest readings of US inflation suggest inflationary pressures might have peaked and are prompting improved investor sentiment across the Atlantic, with many US stocks moving back up.

There is a smart, low-cost way to play this improving picture through exchange-traded fund **Xtrackers S&P 500 Equal Weight (XDWE)**. It provides exposure to US stocks with a twist.

The S&P 500, along with the Dow Jones Industrial Average and Nasdaq Composite, is one of the benchmark US stock indices.

Launched in its current form in 1957, it includes 500 of the largest businesses listed on US exchanges selected both on their size and on other criteria like how easy the shares are to trade and financial viability.

Like most major indices the S&P 500 is market cap weighted, or in other words the stocks with the largest market valuations have the most influence on its performance.

This means the index is heavily dominated by just a handful of companies. Its top 10 constituents have a weighting of nearly 30%. As a consequence its fortunes are heavily tied to the likes of **Microsoft (MSFT:NASDAQ)**, **Apple (APPL:NASDAQ)** and **Amazon (AMZN:NASDAQ)**.

For an ongoing charge of 0.25% the Xtrackers ETF tracks an equal-weighted S&P 500 index which means each constituent has a fixed weight of 0.2%. This provides more genuine diversification for investors looking for exposure to US stocks.

For example, while the S&P 500 has a 27.9% weighting to the technology sector, the S&P 500 Equal Weight index has a little more than half that allocation at 15.8%.

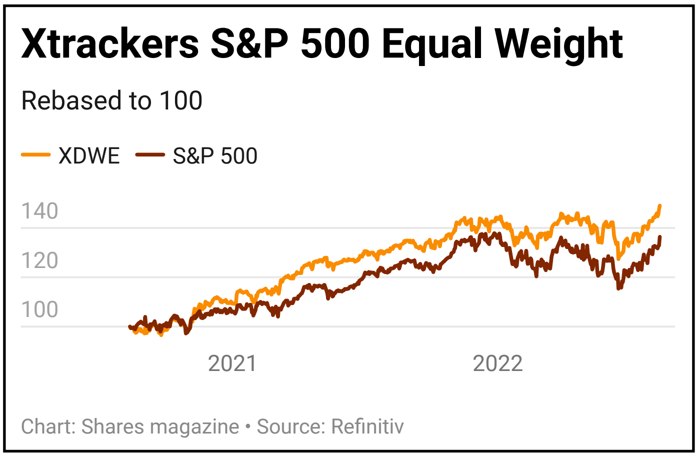
Amid all the focus on the big US tech names, it is easy to forget just how diverse and vibrant the US stock market can be.

XTRACKERS S&P 500 EQUAL WEIGHT ETF
BUY
(XDWE) £65.86

Net assets: **£2.9 billion**

Just look at **Enphase Energy (ENPH:NASDAQ)**, which has seen its share price increase more than 350-fold in the last five years. It makes kit which converts direct current from solar modules into alternating current for use in the home and has nearly half the market for residential installations in the US.

When big tech was flying high the Xtrackers ETF's performance struggled to keep pace but over the last two years it compares favourably. Its total return in sterling clocks in at 49% versus 39% for the vanilla S&P 500 index. [TS]



Construction firm offers steady growth with a strong balance sheet

Morgan Sindall is racking up record profits due to its high-quality contracts

Construction and regeneration firm **Morgan Sindall (MGNS)** posted record profits for the first half of the year, showing further growth on last year which analysts already considered to be a 'step-change in performance'.

With the office fit-out market accelerating, an elevated order book and strong cash-flow generation, we think the market is undervaluing the group's shares.

Despite a tough operating environment, where material and labour costs have affected margins on some projects, Morgan Sindall reported record pre-tax earnings for the first six months of 2022 on the back of a solid 9% increase in revenue.

The company also nudged up its full-year guidance, having already upgraded its forecasts in February when chief executive John Morgan described the group as 'in its best shape ever'.

Its strong balance sheet and substantial net cash position allows the firm to pursue a disciplined approach to contract selection, giving it a secured workload of £8.5 billion of high-quality orders at the end of June.

Construction and infrastructure made up just under half of the £1.7 billion of first-half revenue. The aim is to grow that part of the business to £1 billion of annual revenue with a combined 3%-plus operating margin.

Fit-out revenue jumped 20% in the first six months, accounting for just over a quarter of revenue thanks to a surge in demand as firms revamped their workspaces in order to attract staff back to the office.

Partnership housing and urban regeneration, where the group works alongside housing associations and local authorities, made up the balance of revenue, with an increase in the size of housing projects and healthy growth in margins.

Most of the contracts in this division are long-term with around 60% of secured work only scheduled to commence from 2024 onwards.

MORGAN SINDALL
BUY
(MGNS) £18.40
Market Cap: £867 million

It should be noted that on top of the £7 million provision for partnership housing taken under the Developer Pledge to address building safety measures, the Government has requested the firm commit to the pledge as a mixed-used developer which would involve a £40 million to £50 million charge before recoveries.

Margins in the construction business are expected to be around the top end of the company's range of estimates, while profits in the fit-out division are seen 'materially ahead' of the top end of the target range for the full year.

Analysts at Numis see profits growing 40% in the medium term, supported by strong organic momentum and an order book equivalent to 2.5 times revenues. [IC]

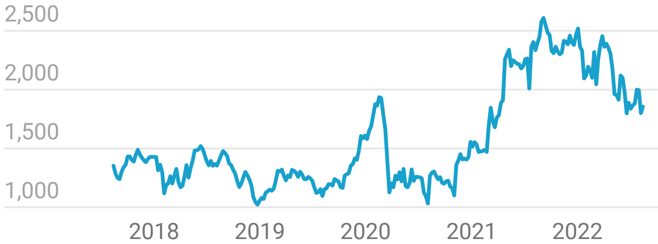


Chart: Shares magazine • Source: Refinitiv

How i3 Energy shares increased nearly three-fold in 12 months

The oil and gas producer has benefited from rising energy prices

I3 ENERGY

(I3E:AIM) 29.4p

Gain to date: 167%

When we flagged the appeal of Canadian oil and gas producer **i3 Energy (I3E:AIM)** at 11p in July 2021 we couldn't have foreseen Russia's invasion of Ukraine and the resulting surge in oil and gas prices.

We simply liked the potential for generous dividends, the business model of acquiring low-cost conventional assets and an attractive equity valuation.

WHAT'S HAPPENED SINCE WE SAID TO BUY?

At the macro level a combination of pent-up demand and the impact on supply of the conflict in Ukraine have helped drive energy prices much higher.

This has combined with rising production from Canada to significantly boost i3's cash flow and has enabled it to pay a monthly dividend since March 2022.

More recently the company agreed to a farm-out deal on its Serenity prospect in the UK North Sea, with **Europa Oil & Gas (EOG:AIM)** taking a 25% stake in return for paying 46.25% of the costs of an appraisal well up to £15 million. Anything beyond that would be shared based on the companies' respective stakes.

WH Ireland analyst Brendan Long says: 'Big picture, i3 Energy is significantly ahead of the game, in a game where that is absolutely critical. This has become one of the key characteristics of the company and what we are seeing in the North Sea is reminiscent of what led to the company's exceptional shareholder value creation in Canada,

albeit we appreciate that the risk/reward profiles of these jurisdictions are different.'

WHAT SHOULD INVESTORS DO NEXT?

WH Ireland has i3 paying a 1.7p per year dividend based on its Canadian output which at the current share price equates to a yield of 5.8%. Investors therefore have the option of holding on for the steady stream of monthly dividends.

However, given the big increase on our entry point and a potential dampening of commodity prices against a weaker economic backdrop, taking some profit might be sensible at this point. [TS]

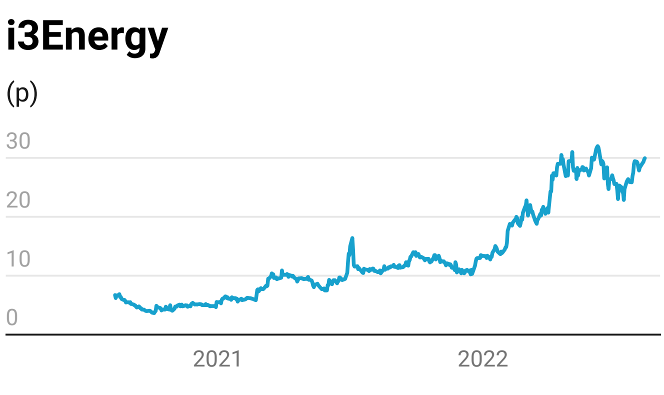


Chart: Shares magazine • Source: Refinitiv

We got it wrong with Revolution Beauty. Time to cut our losses

The company's share price has collapsed after a series of setbacks

REVOLUTION BEAUTY
(REVB:AIM) 28.6p

Loss to date: 82.1%

Last September we were attracted to **Revolution Beauty (REVB:AIM)** for the make-up, skincare and haircare brand's global growth potential in a cosmetics market that has historically exhibited resilience during downturns.

In a decision that has left us red-faced, we kept faith with the stock and failed to cut our losses as the share price continued to plummet long after we said to buy the shares at 160p.

Our optimistic view was that cost-of-living pressures had put consumer-facing stocks like Revolution Beauty on the back foot and the company appeared to be executing well. With hindsight, the collapsing share price and unexpected news on 12 May that finance director Andrew Clark was leaving less than a year after the stock market flotation were major red flags.

WHAT'S HAPPENED SINCE THEN?

On 2 August, Revolution Beauty delayed its results with auditors poring over the books and issued a massive profit warning pinned on cost inflation, retailer destocking, the halt to trading in Russia and Ukraine following the invasion, as well as a slowdown in direct-to-consumer sales as consumers returned to physical stores.

On 11 August came the bombshell news that auditors had raised accounting issues with management regarding the figures for full year 2022. If material adjustments are required, Revolution Beauty's profits could be 'materially reduced across a number of potential adjustments including stock and bad debt

provisioning and revenue recognition', warned the company.

Six days later, **Boohoo (BOO:AIM)** announced it had taken a 7.1% stake in Revolution Beauty, triggering a big share price recovery in the makeup seller.

WHAT SHOULD INVESTORS DO NOW?

Given the lack of earnings visibility and accounting issues coming to light, Revolution Beauty is in a mess.

The Boohoo news has helped to narrow some of the share price losses which means now is a good time to cut our losses and get out. There is still a risk of bad news concerning the accounting issues which could hurt the share price again.

We got this one wrong and should have heeded what the market was telling us all along. [JC]

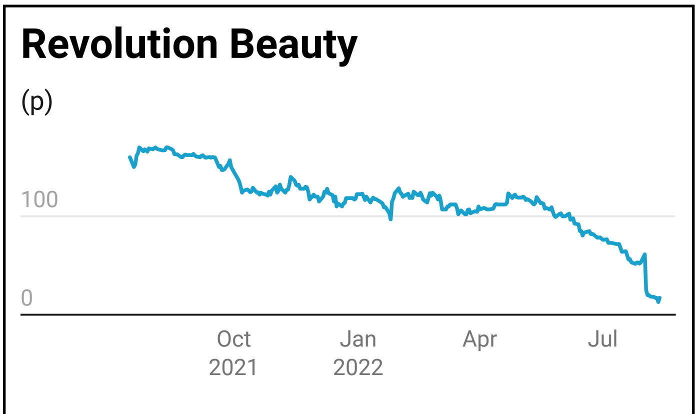
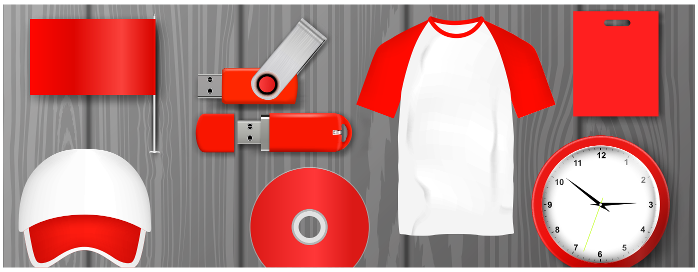


Chart: Shares magazine • Source: Refinitiv

4imprint investors made 20 times their money in 10 years

The promotional products group has been a surprise success



It's not often we get to write about UK companies which have seen their shares multiply in value by a factor of 20, especially when the company concerned makes what might be considered 'disposable' or discretionary goods.

Yet, given the sudden contraction during the pandemic in corporate advertising – one of the quickest and easiest areas of spending most firms can cut – the success of **4Imprint (FOUR)** in not just bouncing back but setting new sales records is quite phenomenal.

The firm sells promotional products in North America, the UK and Ireland to help customers build their brands and 'make lasting connections' with their own clients. In mid-July, 4imprint raised its full year revenue target well beyond market expectations.

The company revealed total orders for its primary North American business in the first half of this year were running around 14% above the level of 2019, the last 'normal year' of operations pre-Covid, thanks to market share gains and strong demand from new and existing customers.

Moreover, the value of its average order was also 14% higher than three years ago, meaning overall revenues were in the region of 30% above 2019 as customers spent more on promoting their goods and services.

As a result, 4Imprint said it would likely hit its long-held target of $1 billion of revenues this year, almost double what it made in 2020 and 16% more than it made at its previous peak in 2019.

Analysts scrambled to revise up their estimates and the shares, which were languishing at £24, below their closing level of 2020, rocketed skyward.

Having struggled to break above their pre-pandemic close, the shares were drifting when last week the company issued another trading update to say it had posted record sales and orders and was even more confident of hitting its $1 billion revenue target.

That pushed the shares to new highs just shy of £40, meaning investors who bought the shares back in 2012 at approximately 200p have made 20 times their money even before accounting for dividends.

With supply chain challenges easing and product cost inflation 'stabilising', margin pressure should be less acute in the second half while pre-agreed price increases will boost earnings.

Also, the acquisition of a small screen-printing business will give the firm the capability and capacity to service untapped demand for apparel and support continued market share growth.

As Liberum analyst Joe Brent points out, operational leverage is coming through and the firm is getting more bang for its buck on each marketing dollar. He believes the case for a special dividend has increased.

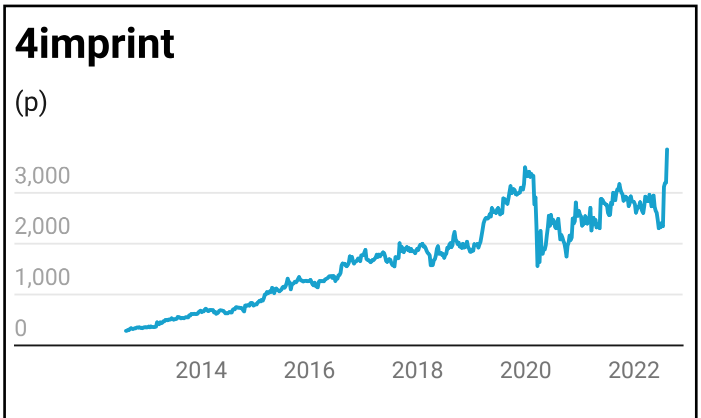


Chart: Shares magazine • Source: Refinitiv

By **Ian Conway** Companies Editor

Why there won't be relief from Zantac pain for GSK in the short term

A big settlement has already been priced into its valuation but uncertainty will hang over the stock

The stock market is forward-looking and has already priced in a significant financial hit for **GSK (GSK)** from US litigation associated with claims its Zantac heartburn treatment might have links to cancer.

The first court case, due to start next week, was withdrawn ahead of trial by the plaintiff. However, this is only one of thousands and it could be some time before a line is drawn under the issue given the first 'bellwether trial', as Shore Capital describes it, isn't scheduled to begin until February 2023.

Uncertainty over the outcome could still weigh on the stock in the interim and prevent a meaningful recovery in the share price.

Zantac became an over-the-counter drug in the mid-1990s and while it was GSK which launched the treatment on prescription in the early 1980s, others which subsequently sold Zantac and its generic equivalents are tied to the scandal including **Pfizer (PFE:NYSE)** and **Sanofi (SAN:EPA)**.

The drug's sale was banned after the discovery of a 'probable' carcinogen in the treatment in 2019.

Also dragged into the affair is consumer health specialist **Haleon (HLN)** which recently demerged from GSK. Though it is not party to any claims over sales of Zantac it may still face liabilities under contractual provisions agreed with its former owners.

This threat is compounding a miserable start to life as a public company for Haleon. Its shares began trading on 18 July at 330p after the demerger but as we write, less than a month on, they are down at 260.8p.

Berenberg analysts estimate the market has priced in a potential legal settlement for all the parties involved of $40 billion regarding Zantac. They add: 'We believe the share price risk has been overstated based on current evidence levels and the number of claimants. However, the litigious environment of the US can be difficult to predict.

'Assuming a potential $150,000 settlement per claimant, the share price moves imply over 330,000 claimants, significantly above the 3,450 personal injury cases filed and around 100,000 unfiled claims on the registry.'

Litigation analysts working for Bloomberg believe a settlement value could instead fall between $5 billion and $7 billion with GSK potentially liable for 30% of that amount, or $2 billion.

For its part GSK strongly denies the claims, arguing there is no reliable evidence of a link with any form of cancer.

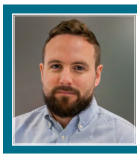
Clearly there is potential for a significant share price relief rally for the affected stocks if the settlement comes in at the lower level anticipated by Bloomberg's experts or if the cases fail to make any progress. But we won't know in the short term.

How share prices reacted to concerns about Zantac

Company	Share price performance*
GSK	−15.0%
Haleon	−12.6%
Sanofi	−11.5%
Pfizer	−2.9%

*From close on 9 August to close on 11 August

Table: Shares magazine • Source: SharePad, 15 August 2022



By **Tom Sieber** Deputy Editor

THIS IS AN ADVERTISING PROMOTION

Janus Henderson
INVESTORS

HOW ASIA MEASURES UP AGAINST THE WIDER WORLD

Sat Duhra, Portfolio Manager of **Henderson Far East Income**, discusses the key findings from the latest edition of the Henderson Far East Income Dividend Index report - highlighting how resilient dividends and profits in Asia-Pacific ex-Japan were compared to the rest of the world.

Find out more here >

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HOW TO FIND THE RIGHT FUND FOR YOU:

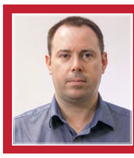
Follow these simple steps to save time and money

If you want to build up a pot of money for the future, be it retirement or paying for some of life's expenses including children's university fees or a loft conversion, investment funds can be a great way to grow your savings.

They enable you to quickly build a portfolio which could save you a lot of time and money.

You don't have to spend hours researching the market for which stocks to buy, and you won't incur anywhere near the level of dealing fees that come with building a portfolio of 20 or more stocks from scratch.

Finding the right fund for you is easier than you might think. This article is a step-by-step guide to navigating the world of funds so you can go straight to the type of product that fits your needs.



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

Don't be put off by the fact there are thousands of funds on the market. It's easy to sift through the list as they will be split into different categories including investment styles, sectors, themes and geographies. It's just a case of following a simple path to find the best ones for you.

Just remember that as part of your fund selection journey, you need to make sure that each fund's target market, style and goals fit with your own investment strategy, time horizon and risk tolerance.

STEP ONE: ACTIVE OR PASSIVE?

There are two main types of fund – active and passive. Active funds are run by a fund manager who selects which assets go into the portfolio and they are paid a fee by investors with the aim of beating the fund's benchmark index.

Passive funds aim to mirror the performance of a key benchmark or index such as the FTSE 100. You'll find these are also called tracker funds or exchange-traded funds (ETFs). The fees associated with these products are typically much lower than active funds.

Annoyingly, the funds industry isn't very good at labelling which products are active or passive. You'll need to read the description for each fund to find out. Yet as a short-cut, most products from Vanguard are passive funds in the UK, you can spot which one of Legal & General's products are tracker funds as they tend to have the word 'index' in the name, and products from iShares and SPDR are all passive funds.

Another way to find out is to use fund screening tools that offer you the ability to select 'active' or 'passive (or tracker)', such as this one from AJ Bell.

STEP TWO: GROWTH OR INCOME?

The next decision you'll need to make is whether to invest in a 'growth' fund or an 'income' fund, or one that offers both. This could be influenced by your investment goals, risk tolerance and your age.

Growth funds hold shares in companies that are expected to increase in value over time, so the value of your capital should also rise. Some growth funds might pay dividends, but the income stream is likely to be small.

Fundsmith Equity Fund (B41YBW7) is one of the most popular growth funds with UK investors and nearly all investor returns come from growth in the value of its portfolio.

Income funds prioritise investing in companies that pay good dividends or bonds with attractive coupons. Some income funds will offer an element of capital growth alongside the income stream but with others the only way you'll make money is through dividends as capital gains could be minimal. That's fine if you understand what to expect from an investment.

For example, **Round Hill Music Royalty Fund (RHM)** owns the rights to various hit songs and receives a royalty when they're played on the radio or on stage, feature in films or adverts, or are streamed online. It passes on some of these royalties in the form of dividends to investors. While it pays an income yield in the region of 4.5%, its share price has barely moved since launch in November 2020.

In contrast, **BlackRock Income & Growth Investment Trust (BRIG)** has a 3.7% dividend yield and its share price also increased by 6.6% over the past 12 months. So, you're getting a blend of income and capital growth.

STEP THREE: GEOGRAPHY OR SECTOR?

This is the point at which you can go down many different paths. One route is to consider if you want exposure to a broad range of geographies. The other is to think about choosing a specific sector such as technology or a certain asset class such as property.

The technology sector isn't typically known for generous dividends so going down this path may be of more interest to someone who just wants capital growth rather than income.

A key attraction of investing in property is to collect a regular income, but you may also see the value of your capital go up in time as well. The Association of Investment Companies, also

ACTIVE FUNDS: WHAT'S THE DIFFERENCE?

Active funds involve a fund manager deciding what should go in and out of a portfolio. They fall into two categories – 'funds' which is the generic term to describe unit trusts and OEICs, also known as open-ended funds; and 'investment trusts' which are closed-ended funds.

It may sound confusing but isn't once you understand how they work.

Open-ended means funds create or cancel new shares depending on demand from investors. They only issue one price per day, and to deal you would usually have to place your investment instruction the day before, so you don't know precisely what price you're going to get.

Some investors prefer investment trusts because there is a live price throughout the day, and you know exactly the price at which you're buying or selling.

That's because investment trusts are closed-ended, which means the fund manager is investing a fixed pool of money. Investment trusts trade on the stock market like ordinary shares and their share prices can sometimes deviate from the value of the underlying portfolio or net asset value (NAV) depending on investor demand.

The existence of discounts and premiums to NAV makes investment trusts more complex than open-ended funds. It also makes them more volatile, because as well as variation in the price of the underlying portfolio, there is movement in the discount or premium to NAV.

Investment trusts can also borrow money to invest, which is known as taking on 'gearing' and can boost returns in the bull markets but exacerbate losses in bear markets.

Funds are suited more to liquid investments such as listed shares and bonds, while investment trusts are better for investing in illiquid assets like commercial property, infrastructure or unquoted private companies.

That's because open-ended funds might have to suspend trading if lots of investors want their money back at the same time. It's hard to sell illiquid assets fast.

An advantage of the investment trust structure is it allows these companies to use their 'revenue reserves' of cash squirrelled away in good times to at least maintain dividends in bad times. Investment trusts tend to have lower annual charges than their open-ended peers, but a significant number also levy performance fees, which are rarer in the fund universe. [JC] known as the AIC, says the average yield on investment trusts that invest in UK commercial property is 4.6%.

For example, **Custodian REIT (CREI)** yields approximately 5% and has seen its share price rise by 7.5% over the past 12 months, giving investors a blend of returns from income and capital growth.

Other sector-specific funds on offer include ones targeting renewable energy, infrastructure, biotechnology and healthcare, financials and natural resources.

Some investors prefer to focus on geography than sector as they want exposure to a broad range of industries. In this case, many funds are global portfolios that put money to work in companies listed on the main international markets, whereas others focus on the UK or other developed markets such as the US, Europe and Japan.

Emerging markets funds invest in some of the world's fast-developing economies including China, India and Brazil, while there are also country specialist funds and trusts tapping into opportunities in these vast emerging markets as well as frontier markets such as Vietnam.

GOOD SOURCE OF INFORMATION ON FUNDS, INVESTMENT TRUSTS AND ETFS

There are fantastic online sources of information on funds and investment trusts to help with the selection process.

The Investment Association is a good place to find details on fund sectors and statistics, while the AIC does the same for investment trust data.

AJ Bell's website enables you to filter funds, investment trusts and exchange-traded funds and examine their performance. The AJ Bell and *Shares Money & Markets podcast* regularly features interviews with fund managers.

Shares' website is flush with fund-related articles and fund manager interviews and videos.

Trustnet is a good resource for factsheets, fund performance data and topical articles, while investment trust fans should visit Kepler Trust Intelligence and QuotedData websites for in-depth research notes.

JustETF is a useful resource for people seeking passive funds as it contains information and screening tools for ETFs.

STEP FOUR: REFINING THE SELECTION FURTHER

At this point, you may wish to think about the size of the company to whom you want exposure, or the sector they operate in as you may only want to invest in a specific theme.

Some funds focus on smaller companies, medium-sized companies or large companies, known in the industry parlance as small caps, mid-caps and large caps respectively.

If you've got to this point in the fund search process and have come to conclusion that you'd simply like a bit of everything, the answer might be to look at multi-asset funds.

These products own a mixture of shares, bonds, currencies and alternative assets such as property and infrastructure. An all-in-one solution, they take the guesswork out of spreading your money across different asset classes in the quest for performance.

For example, **Momentum Multi-Asset Value Trust (MAVT)** can invest in stocks, loans, bonds, property, infrastructure and gold. It varies the allocations depending on what's happening in the world and where it sees opportunities.

PUTTING THE SEARCH INTO PRACTICE

Let's run you through an example of how to use AJ Bell's fund screener tool.

We want to find a passive fund that invests in companies globally and where any dividends are automatically reinvested. We're happy to look globally for opportunities.

- Fund Company – the default setting is 'All Companies' and we'll leave this untouched. If you wanted to find funds for a specific asset manager, you would select their name at this point.
- Morningstar Category – Morningstar is the research company that powers the fund data on AJ Bell's website. We'll also leave this one untouched as one of the subsequent filters (IMA Sector) does something similar and we don't need to use both.
- Currency – here we select 'GBP' so we're using the UK currency.
- IMA Sector – We select 'Global' to find companies listed on stock markets around the world.
- Distribution Status – there is a choice of 'All', 'Inc' and 'Acc'. We select 'Acc' as this stands for 'Accumulation', meaning any dividends will be automatically reinvested. If you want to collect the dividends as cash, select 'Inc'.
- Morningstar Rating – The research company has a ratings system, so we select four and five stars to find the top scoring funds.
- Total Net Assets – This shows the size of a fund. We select £1 billion as the minimum.
- Max Total Expense Ratio – This is where you can look for funds based on their fees. For our exercise, we select '1.00' as the maximum, meaning we don't want to pay more than 1% annual fee. This tool is very useful if you're looking for the absolute cheapest fund for a particular area of the market.
- For the purposes of this search, we leave the Morningstar Analyst Rating, Morningstar Risk, 3 Year Standard Deviation, Return %, Minimum Initial Purchase and Max Initial Sales Charge fields untouched. However, feel free to include these in your searches as they can be useful ways to further narrow the pack.

Our screen results in a list of 10 funds, covering both passive and active products. If we narrow it down to the highest Morningstar rating of five stars, there are two funds on the list:

1. **Janus Henderson Global Sustainable Fund (B71DPP6)** and
2. **Vanguard FTSE Developed World ex-UK Equity Index Fund (B59G4Q7)**.

The former is an active fund, and the latter is a passive fund.

As our original goal was to find a passive fund, the Vanguard product is therefore a good starting point for further research to ensure it meets our investment needs and goals.

It's worth noting that the AJ Bell fund screening tool doesn't include investment trusts. For those types of fund you'll need to use this screening tool. The approach is essentially the same.

DISCLAIMER: AJ Bell referenced in this article is the owner and publisher of Shares magazine. The author (James Crux) and editor (Daniel Coatsworth) own shares in AJ Bell. Daniel Coatsworth also owns units in Fundsmith Equity

Discover the biggest dividend yields in the FTSE 350

Double-digit yields are on offer but not all income is equally reliable

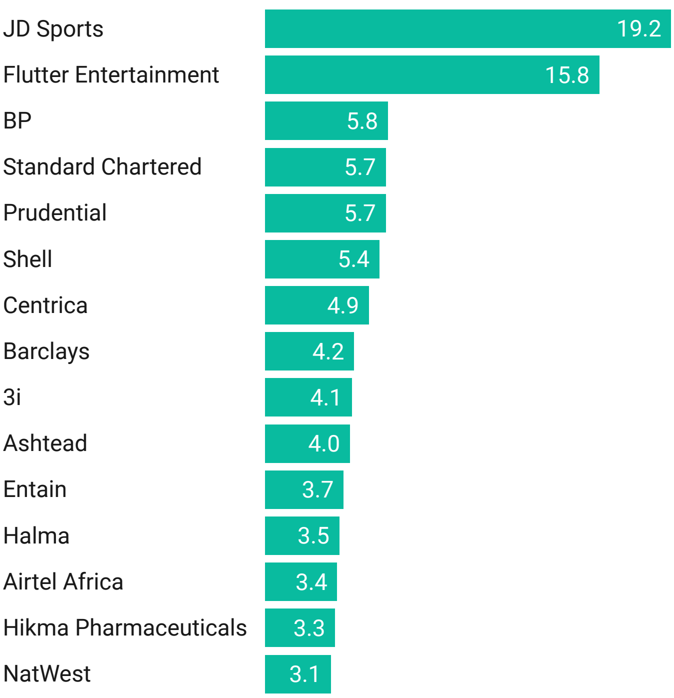
Bedevilled by soaring inflation, rising interest rates, possible recession and major disruption to global supply chains, global stock markets have fallen hard this year. A consequence of falling share prices is ballooning dividend yields, pushing double-digits in some cases in the UK.

Is this a once in a lifetime opportunity to secure inflated income yields for the long haul, or a value trap for investors if shareholder payouts are pared back from current expectations?

At the beginning of 2022, investors were worried mainly about inflation. Now, as we move into the second half, concerns are focused on inflation and recession.

FTSE 100 biggest dividend cover

Amount of times forecast dividend covered by forecast earnings per share*



A figure above 2 is considered good

Chart: Shares magazine • Source: SharePad. *Based on estimates for the next financial year to be reported. Data as of 15 August 2022

Latest data show both the US and UK economies shrinking in the second quarter to 30 June, while the IMF has recently made another gloomy prognosis in its World Economic Outlook report as consumers reel in spending as pressure mounts on household budgets.

By one well-used measure, the US has already fallen into recession after GDP – a broad measure of the price of goods and services – decreased at an annualised rate of 0.9% in the second quarter, having declined 1.6% in the first three months.

Two quarters of negative GDP growth are widely regarded as a signal that the economy has gone into recession. But the US's National Bureau of Economic Research is the official arbiter of when recessions begin and end, so while the GDP figures will play into the NBER's final verdict, it also looks at a wider range of economic factors, including the jobs market, and is unlikely to give its decision soon.

A SLOWDOWN COULD HURT DIVIDENDS

While many dividend-paying stocks come from defensive and less growth-focused sectors of the economy, a wider slowdown will inevitably have an impact on earnings and the ability of some companies to pay dividends.

Pessimists will say that firms slashed payouts in 2020 as the impact of the pandemic became apparent, and they will do so again under pressure in recession.

Optimists would argue that 2023 can't be as bad as 2020, and that the risk of recession is already being priced into many of the more economically sensitive sectors, often called cyclicals.

'Nothing can be taken for granted, especially if recession hits,' argues AJ Bell investment director Russ Mould.

In July, we witnessed a major turnaround in the stock market despite aggressive rate hikes and mounting evidence of a recession.

Stock markets around the world bounced back, posting the best month since 2020, led by cyclicals, like consumer discretionary, technology and industrials. In contrast, sectors that usually fare better in recessions (referred to as defensives), such as consumer staples and healthcare, lagged the overall market.

'High-dividend-paying stocks have been outpacing the overall stock market this year in the US, Europe, and Japan, except during July,' said Jeffrey Kleintop, managing director and chief global investment strategist at broker Charles Schwab.

'Both the S&P 500 High Dividend index and MSCI Europe High Dividend index have delivered positive total returns for the year through the end of July, while the S&P 500 is down 13% (as at the start of August 2022) and MSCI Europe index is down 7% (as measured in euros).

'In Japan, the MSCI Japan High Dividend index is up 13% this year compared with losses for the MSCI Japan index (as measured in yen).'

CAN IT LAST?

It's not clear that stock markets can sustain July's upward momentum and may rotate back to the leadership we had seen in the first half of the year.

Support for this view includes concerns over an ongoing slide in economic activity while central banks continue to tighten monetary policy in response to inflation.

'If that is the case, there may be grounds for renewed focus on dividend payers, which have often offered investors some refuge during recessionary bear markets of the past,' said Kleintop.

DIVIDEND FORECASTS

Link's latest quarterly Dividend Monitor, released on 27 July, forecasts a decent year for UK dividends in 2022 but looks ahead to a more challenging environment next year.

'As we move into 2023, headwinds will strengthen,' said Link's Ian Stokes, managing director, corporate markets UK and Europe.

The headline total for Q2 2022 jumped 38.6% year-on-year to £37 billion bolstered by large one-off special payments, but the underlying picture was also good, according to the Link data.

'Underlying dividends, which exclude these volatile specials, jumped 27% to £32 billion, boosted by the weak pound. This was the second-largest quarterly total on record, for both headline and underlying figures, just shy of the record reached in Q2 2019,' said Stokes.

HIGH YIELDING SECTORS

One of the risks of dividend investing is sector concentration, an issue that has dogged UK income seekers for years. Companies in the utilities, consumer staples and resources sectors tend to pay much higher dividends than companies in other sectors.

Seeking high-dividend payers without considering sector allocation can result in a lack of diversification, potentially making a portfolio more vulnerable during periods of high volatility.

FTSE Russell data tells us that the FTSE 350 is currently on a yield of 3.4%, or 3.5% if we strip out investment companies. That's in line with an average of 3.4% in the 25-year period between 1993 and 2018.

HIGHEST DIVIDENDS COME FROM A SMALL GROUP

One third (120) of the companies that make up the FTSE 350 index (which is made up of the FTSE 100 and FTSE 250 indices combined) are forecast to pay income yield above the average, yet most of UK's forecast dividend payments this year come from a worryingly small band of stocks.

According to AJ Bell's second quarter Dividend Dashboard data, just 10 companies are forecast to pay dividends worth £47.7 billion, or 56% of the forecast total for 2022. The top 20 payers are expected to generate 74% of the index's payout at £62.5 billion.

'Anyone who believes the UK stock market is attractive on a yield basis, and looking to buy individual stocks, glean access via a passive index tracker or buy a UK equity income fund needs to have a good understanding of, and strong view on, those 20 names in particular,' says AJ Bell.

HAVE MINING DIVIDENDS PEAKED?

Mining companies have been the engine of the post-pandemic recovery, paying generous ordinary and special dividends as commodity prices have soared. That boom is likely to have peaked, Link says, and will lead to a slowdown in UK dividend growth going forward – although banks are likely to make up some of that shortfall.

Mining payouts are closely linked to the cyclical fluctuations in mining profits. They tend to rise and fall much more over that cycle than dividends from other industries. Concerns over global growth have pushed commodity prices sharply lower in recent weeks, though they remain high in historic terms.

'The sector has confounded expectations more than once before, bending their stated dividend policies at important moments, but if mining dividends have peaked, they will act as a brake on UK dividend growth in the next 12 months having provided the main engine over the last 24,' said Link's Stokes.

The weakness of the pound is also proving a key swing factor this year. If it maintains its current level for the rest of 2022, sterling is set to have its worst ever year against the dollar, according to Link, with the translated value of dollar dividends getting a very big boost.

'The easy post-pandemic catch-up effects are soon to wash entirely out of the figures, and an economic recession will crimp the ability and willingness of many companies to grow dividends.'

FTSE 350 top 20 yielding stocks

Stock	Index	Forecast yield
Ferrexpo	FTSE 250	15.1%
Persimmon	FTSE 100	12.0%
Capricorn Energy	FTSE 250	12.0%
Diversified Energy	FTSE 250	10.7%
Jupiter Fund Management	FTSE 250	10.6%
Rio Tinto	FTSE 100	10.4%
Glencore	FTSE 100	9.7%
Direct Line	FTSE 250	9.7%
TBC Bank	FTSE 250	9.1%
M&G	FTSE 100	8.8%
Abrdn	FTSE 100	8.5%
Vistry	FTSE 250	8.3%
Bank of Georgia	FTSE 250	8.1%
Barratt Developments	FTSE 100	8.1%
Royal Mail	FTSE 250	8.0%
Taylor Wimpey	FTSE 100	7.9%
Hays	FTSE 250	7.6%
Imperial Brands	FTSE 100	7.6%
Phoenix	FTSE 100	7.4%
Dunelm	FTSE 250	7.4%

Table: Shares magazine • Source: Sharepad, 12 August 2022. Excluding investment companies

DISCLAIMER: AJ Bell owns Shares magazine. The author (Steven Frazer) and editor (Daniel Coatsworth) own shares in AJ Bell.

By **Steven Frazer** News Editor

Can investors rely on high-yield trusts to deliver on their promise?

We look at four investment trusts for answers

With inflation eating away at investors' income, high-yield trusts can look very appealing. However, the big question investors should ask before committing themselves is just how sustainable are the dividend streams?

In this article we analyse four of the highest-yielding trusts, with a diverse mix of income generation, from European real estate and specialist lending to solar assets and Far Eastern stocks.

WINNING FORMULA

The highest-yielding trust on our screen, **Schroder European REIT (SERE)**, invests in commercial property in a few select continental European cities in order to generate 'a regular and attractive level of income return together with the potential for long-term income and capital growth'.

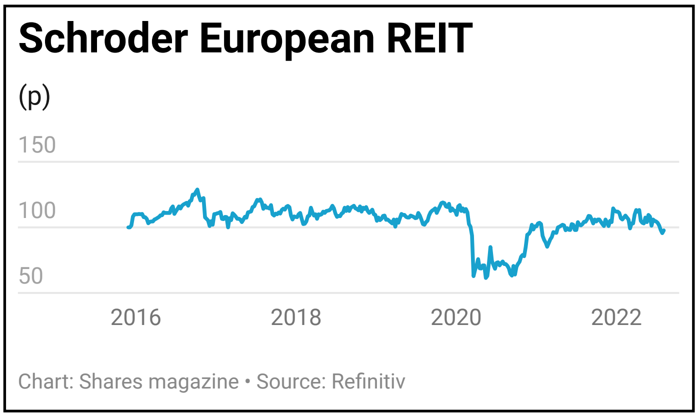


Chart: Shares magazine • Source: Refinitiv

Its investments are focused on 'winning cities' such as Berlin, Paris and Seville which have higher than average levels of GDP, employment and population growth, attract higher-value companies, have a well-developed infrastructure and are attractive places to live and work.

The trust pays dividends once a quarter. It targets a dividend yield to investors of 5.5%, but earlier this month it paid a second interim dividend of 1.85 cents (1.56p) per share together with a special dividend of 4.75 cents (4p) per share.

Added to the 1.85 cents (1.56p) first interim dividend paid in April, this takes the yield to 7% on a 102p share price.

Assuming it pays two further interim dividends of 1.85 cents for the year to September, the prospective yield is 10%.

However, this year's dividends may be an anomaly as the trust is using part of the €45 million proceeds from the forward-funded sale of a property in Paris last year to top up the regular dividend.

Investors will have to wait until the publication in December of the trust's full-year results to know whether they are in with a chance of another special dividend next year to match this year's exceptional payout. We think the current double-digit yield is unsustainable as it is dependent on exceptional property deals which can be irregular.

Examples of dividend yields on high-yield trusts

Name	Estimated dividend for current year	Dividend yield
Schroder European Real Estate (SERE)	10.24p	10.0%
VPC Specialty Lending (VSL)	8p	10.0%
Henderson Far East Income (HFEL)	23.8p	8.7%
NextEnergy Solar Fund (NESF)	7.52p	6.4%

Table: Shares magazine • Source: Shares magazine, company websites. Data correct as of 11 August 2022

SECURED INCOME

Alternative finance firm **VPC Specialty Lending (VSL)** provides asset-backed lending solutions to emerging and established businesses with the goal of building long-term, sustainable income generation.

Chart: Shares magazine • Source: Refinitiv

The £220 million company focuses on providing capital to what it calls 'vital segments of the economy', which for regulatory and structural reasons are underserved by the traditional banking industry.

Typical examples of funding include small business lending, working capital products, consumer finance and real estate, with the firm relying on its 'rigorous due diligence and credit monitoring' to generate stable income and 'significant downside protection'.

The firm primarily lends against short-duration, cash-generating assets with predictable income, which in adverse circumstances can quickly be turned to cash to repay its investment.

It says it has found a 'significant opportunity to earn attractive risk-adjusted returns through its extensive sourcing relationships around the globe,

largely focusing on emerging sectors of the digital economy where pricing margins have not yet compressed but risk can be properly underwritten'.

The firm primarily lends to privately-owned US companies, although its top five investments – which make up 45% of its net asset value – include asset-backed loans to a Latin American group and a Singapore-based group.

As of the end of March, the weighted average coupon rate on the asset-backed lending portfolio, excluding gearing, was 10.42% and the weighted average term to maturity was 24 months.

Meanwhile, the firm paid a first quarterly interim dividend of 2p per share in July for the three months to March, and assuming it follows the same pattern as the recent past it will pay 8p per share for the whole year which equates to a yield of 10% based on a current 79.6p share price.

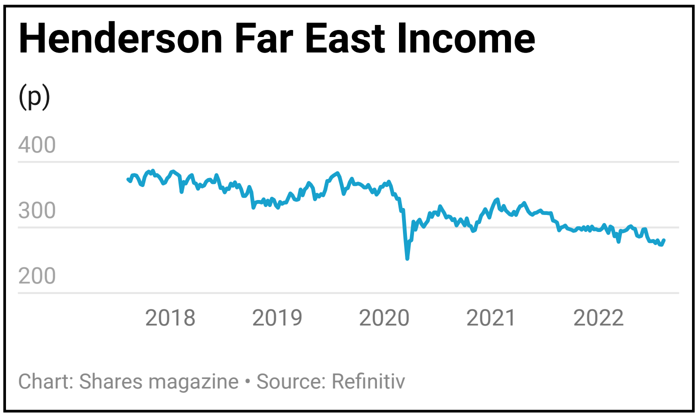
It is hard to say if the double-digit yield is sustainable – it might be if everything goes to plan, but there are plenty of examples of asset-backing lending not working out as expected.

EASTERN PROMISE

Henderson Far East Income (HFEL), which as of the end of June had £463 million of assets, describes itself as a 'strong diversifier for income and growth-seeking investors'.

The trust uses a value-driven approach to invest both in companies with high and sustainable dividends and in companies with the potential to grow their dividends.

'High dividends are for today, while rising dividends are for the future,' says manager Mike Kerley, who has been at the helm since 2007.



Companies which are growing their dividends tend to get rerated over time, generating capital gains for the trust, adds Kerley.

The trust invests in developed and emerging Asian markets, with a strong focus on cash flow as a measure of both sustainability and profitability as it is cash flow which ultimately finances dividends.

Asia has the potential to increase payouts at a faster rate than other regions, argues Kerley, because dividend levels are currently low by international standards.

The sector allocation at the end of June was heavily skewed towards financial and telecoms companies, which have a combined weighting of over 40%, although technology and energy stocks also had a significant presence at 13% and 12% of the portfolio respectively.

The trust pays quarterly dividends, and this year has so far distributed a total of 17.8p across three interim payments.

While it hasn't confirmed as much, the fourth

interim dividend to be paid in November is likely to be 6p in line to maintain the trust's long history of rising payouts.

That would equate to an annual yield of 8.7% based on a 275p share price, and while the discount to net asset value is towards the low end of its recent range, a yield of more than 8% looks very attractive. We think this level of dividend is sustainable.

BRIGHT FUTURE

With the sharp rise in fossil fuel prices this year and a resurgence of interest in renewable energy it is no surprise that solar funds, which had been out of favour for quite a while, have come good.

One of the largest UK-listed funds is **NextEnergy Solar (NESF)** which owns a portfolio of 100 solar assets – 92 in the UK and eight in Italy – with an installed capacity of 865 MW (megawatts).

Solar power is the most powerful and plentiful available, with more energy hitting Earth in a single hour than the entire global population uses in a year.

Moreover, thanks to a significant drop in the price of technology over the last decade it is also now one of the most cost-effective energy sources.

According to the NextEnergy Solar, the levelised cost of energy for solar has declined by 90% in the past 10 years making it the cost leader over other power technologies.

However, industry body Solar Energy says for the UK government to hit its net zero target by 2050 it will need to triple solar capacity by the end of this decade.

As the leading operator in terms of assets, that puts NextEnergy Solar in prime position to benefit from this expansion.

NextEnergy Solar

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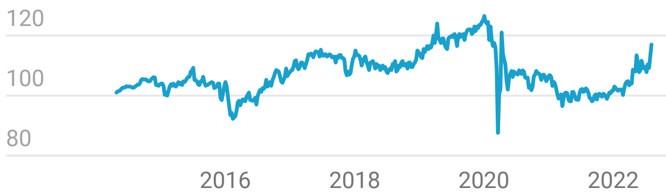


Chart: Shares magazine • Source: Refinitiv

So far, for the year to March 2023, the firm has announced an interim dividend of 1.88p per share payable in September.

The target dividend for the full year is 7.52p, which at a price of 118.2p means the shares are trading on a 6.4% yield, well above the market average.

'This will mark eight years of consecutive dividend increases from NextEnergy Solar,' said James Carthew, co-founder of research group QuotedData, in April. 'Since launch, it has paid out over £250 million in dividends. Each year, these have been covered by earnings and the statement says that the company is aiming to maintain that record.'

Unless solar prices plummet dramatically, we have confidence in NextEnergy's dividend sustainability.

By **Ian Conway** Companies Editor

The 'new normal' proves elusive: time for the old normal?

Thomas Moore, Investment Manager, abrdn Equity Income Trust plc

- The triggers for the ongoing rotation in markets may be geopolitical events, but there are signs that the shift is enduring as inflation takes hold and interest rates rise
- Growth investors were extrapolating a continuation in the 'new normal' but we are now seeing a return of the 'old normal'
- The operational performance of traditional value sectors, such as Oil & Gas, Mining and Financials, is now far stronger than fashionable growth stocks
- The valuation gap between value and growth stocks is still wide, while investor positioning also favours value stocks, suggesting that this rotation could have legs

Since the start of the year, markets have shifted dramatically. The growth stocks that performed so well over the past decade have sold off, while more traditional value stocks have started to revive. At first glance, this rotation is simply a knee-jerk response to external factors such as Covid-19 and the Russia-Ukraine war. However, on closer inspection, there is far more to the rotation than one-off events, strengthening our view that it could persist for some time.

The build-up of inflationary pressures has driven up interest rate expectations, providing impetus to this rotation. Growth stocks tend to price in long-dated cash flows that become worth far less when they are discounted back at higher interest rates. Conversely, stocks that offer strong short-term cash flows become more attractive. This has been a factor in the stronger performance of the cash-generative stocks that we hold in the abrdn Equity Income Trust in recent months.

Geopolitical events may have been the initial triggers for this rotation, but it is now being supported by a growing gap in operational performance. Many traditional sectors, such as Oil & Gas, Mining and Financials, have had far stronger earnings momentum and cash flows than the growth stocks that were previously so fashionable.

When Covid-19 first struck, investors extrapolated a 'new normal' in economic activity, resulting in a widening in the gap between growth and value stocks. The lofty valuations of growth stocks required a continuation of the benign conditions that had helped these companies during lockdown. Once the economy started to normalise, as lockdowns eased, investors became aware that operational performance was shifting back in favour of more traditional value sectors. The valuation gap was too big to ignore.

The resulting rout in in some of the previously hot segments of the stock market has been significant. The sell-off started with concept stocks, with big ideas but little or no profitability, but has subsequently extended to more mainstream technology stocks such as Netflix, Amazon and Google.

Part of the problem for many growth stocks is that investors extrapolated long-term growth trends from their short-term strength during the pandemic. The 'new normal' appears to have faded as lockdowns have ended. Streaming services have been losing subscribers, online retailers have been losing sales as consumers re-discover physical shops, while there remain questions over how companies are using data, threatening the business model of some social media companies.

Earnings momentum

This environment provides a useful backdrop for the abrdn Equity Income Trust, allowing us to scour the entire UK equity market for attractively valued stocks with positive cash flows and earnings momentum, capable of thriving as inflation reasserts itself. Our quantitative model highlights companies across the portfolio screening well for positive earnings revisions and compelling valuations.

We see many traditional sectors coping well with the more challenging macro backdrop. The momentum behind the strong performance of the Oil & Gas and Mining sectors has come from a combination of recovering demand post Covid-19 and contracting supply due to the crisis in Ukraine. At the same time, the shift to electric vehicles has increased demand for raw materials such as lithium, copper and nickel, while ESG (Environmental, Social, Governance) pressures have constrained new capital expenditure. The shift from 'new normal' to 'old normal' is also noticeable in the changing political agenda, with increasing focus on the cost of living and energy security, underlining the importance of these traditional sectors. All of this has the potential to drive earnings and cash flows, justifying a significant overweight position in the portfolio.

This environment also favours a heavy weighting in Financials. Higher inflation is driving up interest rates, with Financials the natural beneficiary, particularly those whose interest income will directly benefit. Banks have retained significant balance sheet provisions following Covid-19. As a result, we have been adding to our UK banks weighting.

Equity income renewal?

The resurgence in traditional sectors is helping the UK equity income sector to regain momentum. Bemused by the rout in growth stocks, investors are asking 'where next?'. In an uncertain environment, with many growth stocks having plummeted, investors can "touch and feel" dividends, providing an important and reassuring component of the total return investors aim for. Tastes may change, but the attraction of dividends apparent.

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.

The funds that yield more than twice the best-buy cash savings account

Income maximiser funds may look good but they come with a catch

American business magnate John Rockefeller famously remarked: 'Do you know the only thing that gives me pleasure? It's to see my dividends coming in.'

While you can now get more than 3% interest on a fixed-rate cash savings account, it is still possible to get a much bigger rate of income via dividends from investment products.

In fact, you can get double the current best-buy savings account – which is 3.5% from Aldermore for a five-year term – via a type of investment fund that goes under the banner of 'income maximiser'.

TARGETING 7% YIELD

Fund managers Kevin Murphy and Nick Kirrage target a 7% yield from **Schroder Income Maximiser Fund (B53FRD8)**, which was launched in November 2005 and has attracted over £723 million of assets under management.

They invest in a concentrated portfolio of high yielding equities. The managers trade options on these stocks to top up the yield to something higher than you'd typically find on a traditional equity income fund.

Options are contracts that give the buyer the right – but not the obligation – to buy or sell the underlying asset at a specific price on or before a certain date. Schroders' contracts typically run for three months.

Murphy explains: 'Part of the process is to effectively sell the capital appreciation in stocks and switch it for income.' The fund gets an upfront fee for writing the option, although if the share price finishes above the strike price the fund misses out on the excess gain.

STANDING UP TO CRITICS

Critics of income maximiser funds argue they

sacrifice tomorrow's growth to pay today's income.

The use of options (a form of derivatives) creates immediate income for investors at a higher rate than the dividend income paid on the underlying shares, but it means some of the long-term growth is potentially given away.

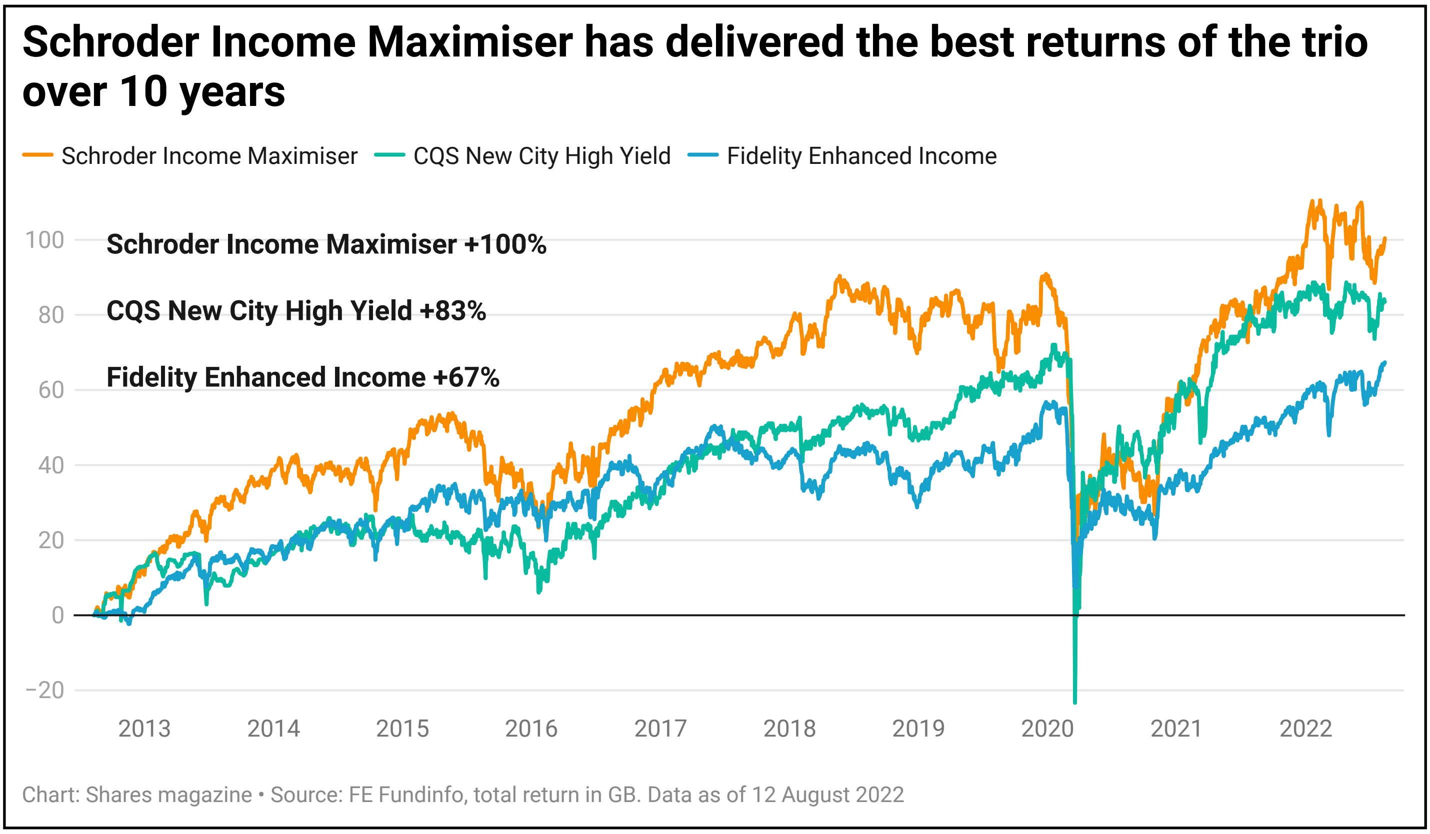
However, income maximiser funds are ideally suited to bear markets. According to Schroders, the investment strategy may underperform a similar portfolio without derivatives in periods when stock prices are rising and outperform when the underlying stock prices are falling.

A SECOND FUND WITH THE SAME APPROACH

Fidelity Enhanced Income Fund (B87HPZ9) is another 'income maximiser'-type investment product. It aims to deliver an income at least 50% more than the income generated from the FTSE All-Share index. Based on income payments over the past 12 months, the yield on the fund is 5.8%.

On a five and 10-year basis the Fidelity fund has generated annualised returns of 3.2% and 5.3% respectively, below that of the Schroders fund (3.8% and 7.2% respectively), according to Morningstar data.

Schroders currently has financials as its largest sector bet with a 25.7% allocation, followed by consumer products at 25.4% and basic materials (which covers the mining and packaging industries)



at 19.9%.

In contrast Fidelity has prioritised the consumer products sector with a 27.7% weighting. Financials account for 14.7% of the fund and basic materials at 13%.

ANOTHER ROUTE TO HIGH YIELD

An alternative to income maximiser funds can be found in **CQS New City High Yield (NCYF)** which makes high-yield investments to generate a superior level of income. It yields 8.6% based on the four most recent quarterly dividend payments and the latest share price.

Most of the investment trust's portfolio is focused on fixed-interest securities, with a select few high yielding stocks on top. Financials and real assets currently account for a large part of the portfolio.

Its ongoing charge at 1.26% is much higher than the two income maximiser funds discussed in this article – 0.85% from the Fidelity fund and 0.91% from the Schroders fund.

CQS New City High Yield has achieved 4.4% annualised returns over five years and 6.3% over 10 years, according to Morningstar.

Its current top holdings include debt security on Stonegate Pub which is yielding 8.25% and shares in natural gas producer **Diversified Energy (DEC)**.

Stonegate is the UK's largest pub company. It was originally formed in 2010 with 333 sites and now operates around 4,800 managed, leased and tenanted pubs.

Diversified Energy operates natural gas and oil wells that are primarily located in the Appalachian Basin in the US, where it describes itself as being one of the largest independent conventional producers.

The company has a low cost of production, which in theory means it is well positioned to withstand any fall in the oil price and still pay generous dividends, currently yielding 10.5% based on forecasts for 2022.

By **Mark Gardner** Senior Reporter

DANNI HEWSON
AJ Bell Financial Analyst

America's commercial electric vehicle race is beginning to heat up again

Several manufacturers are duking it out as new legislation provides a tailwind

The last couple of years have been tough for the motor industry as a whole. While Covid only brought production lines to standstill for a limited period of time the following supply chain snarl-ups created a real headache for just-in-time operators and the dearth of crucial parts like semiconductors sent prices skyrocketing.

The more established names were able to use their size to muscle their way to the front of the queue leaving start-ups and scale-ups wondering if the race to develop the next big EV (electric vehicle) evolution was over before it had even really begun.

Investors watched warily as production time frames were lengthened, delivery dates were missed and share prices tumbled.

But recent weeks have brought a slew of announcements that have piqued interest once again, particularly in US companies both big and small and in the commercial vehicle space.

US inflation appears to be finally cooling off, the supply wheels have been lubricated and Joe Biden's administration has made a big stride towards speeding up the transition to EVs.

RIVIAN ACCELERATES

The landmark climate and healthcare bill comes with a tangle of strings attached with regards to EV tax incentives. However, industry bosses are notably positive about its potential impact in the commercial space with **Rivian Automotive (RIVN:NYSE)** chief executive RJ Scaringe saying it could provide a 'powerful tailwind'.

Rivian desperately needs that tailwind having shed more than 60% of its value since its highly

Rivian Q2 2022

Revenue (million)	Net income (billion)
$364	–$1.7

Table: Shares magazine • Source: Rivian company accounts

anticipated and initially successful stock market float in November 2021. The Jeff Bezos-backed business is still haemorrhaging cash and has been forced to cut staffing costs but it's the revenue number that's finally sending investor pulse rates rising and the share price ticking up by more than 20% in a month.

It soundly beat analyst forecasts in the last quarter and its production numbers are finally reaching meaningful volumes which suggests it might just fulfil the promise of delivering 100,000 electric vans to shareholder **Amazon (AMZN:NASDAQ)** before the agreed 2024 due

DANNI HEWSON
AJ Bell Financial Analyst

date, with a second shift due to come online for vehicle assembly at its Illinois plant during the next quarter.

NIKOLA HAS FURTHER TO TRAVEL

Competitor **Nikola (NKLA:NYSE)** has even further to travel if it's to emulate **Tesla (TSLA:NASDAQ)** and mass produce a vehicle that can dominate the ongoing transition to EVs. While Rivian is focusing on the last few delivery miles Nikola knows that long range, affordable, practical haulage will be a veritable gold mine for the companies that can grab market share ahead of the pack.

Nikola Q2 2022

Revenue (million)	Net income (million)
$18.1	–$173

Table: Shares magazine • Source: Nikola company accounts

The company has had more than its fair share of challenges and its outgoing CEO Mark Russell has done a terrific job of dragging the company clear of previous scandal and to the precipice of solid production. But the next mile of the journey comes with new challenges, the kind a veteran of the auto sector like Michael Lohscheller should be more than equipped to deal with.

The appointment of the former Opel boss, due to start in January, was broadly welcomed by investors. But the business needs to show it can make good on its, currently very small, delivery targets and accelerate towards real numbers, real progress, real potential. To do that it will need continued investor support at a time when funds

are getting harder to come by.

No one understands that journey better than Elon Musk. It took 18 years for Tesla to report its first full year profit, but its latest quarterly numbers will have been eyed enviously by its less mature rivals.

THE ESTABLISHED PLAYERS RESPOND

Tesla set the bar when it comes to taking on the legacy automakers like **Ford (F:NYSE)** and **General Motors (GM:NYSE)** and judging by Musk's recent tweet it's not prepared to settle for anything less than total EV domination. He used Twitter to reveal the long-awaited Tesla Semi will ship this year and his 'Cybertruck' electric pick-up will be available from next year.

Anyone who has driven America's interstate highways will know the sheer scale of the challenge faced by hauliers and in turn the range required to make EVs a practical solution for this kind of commercial use.

EV technology is developing at a blistering pace. And it has to if it's going to become practical and affordable enough to completely replace combustion engines across the world. Companies like Ford and General Motors had been racing to

Tesla Q2 2022

Revenue (billion)	Net income (billion)
$16.9	$2.27

Table: Shares magazine • Source: Tesla company accounts

Ford Q2 2022

Revenue (billion)	Net income (million)
$40.20	$667

Table: Shares magazine • Source: Ford company accounts keep up but the last few years has helped them gain ground.

While pivoting traditional lines to electric has brought challenges, for some investors the safety of household names with solid revenue streams provides a less speculative opportunity to invest in the EV space.

But both Ford and General Motors clearly understand the importance of start-ups; the former has a significant stake in Rivian, and the latter has created subsidiary BrightDrop to help it navigate the new world.

There are plusses and minuses when it comes to scale, the larger the company the more challenging it is to shift direction but there is also some safety in being more established and more diversified.

What's certain is there will only be a finite period of time for both old and new brands to win over the market.

General Motors Q2 2022

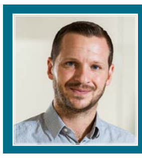
Revenue (billion)	Net income (billion)
$35.76	$1.69

Table: Shares magazine • Source: General Motors company accounts

By following the 4% rule, do I risk running out of money?

The retirement withdrawal strategy raises a few questions when inflation is high

I'm 70 and have been following the '4% rule' since I started taking an income in drawdown on my 65th birthday. However, if I keep to that plan, I'll need to increase withdrawals by 10%+ in September this year. Is that sensible or will I risk running out of money in retirement?
Paul



Tom Selby, AJ Bell Head of Retirement Policy says:

Let's tackle the obvious question first: what is the '4% rule'? It's a rule-of-thumb for people taking a flexible retirement income from their pension pot. It was first put forward by a well-known American financial planner called Bill Bengen.

According to the 4% rule, a healthy 65-year-old should be able to withdraw 4% of their initial capital value each year from their fund, rising annually in line with inflation, and be confident they won't run out of money in retirement.

This is probably easiest to illustrate with an example. Take a healthy 65-year-old with a £100,000 pension pot. If they followed the Bengen rule, they would take £4,000 in the first year of retirement.

If inflation averaged 5% over that 12-month period, in the second year of retirement they would withdraw an extra 5% to maintain their spending power (i.e. £4,000 + 5% of £4,000 = £4,200), and so on.

IS FOLLOWING THE 4% RULE A GOOD IDEA?

It's worth noting there is an active debate in financial planning circles about whether the 4% rule remains appropriate. Some have suggested a combination of rising life expectancy and stalling investment returns mean the figure should be between 3% and 4%.

It is also really meant as a guide rather than a strict set of rules to follow. What is sustainable for each person will depend on a number of things, including your health and the investment returns you enjoy.

If your fund delivers strong returns, for example, then a higher withdrawal rate may prove to be sustainable. This is one of the reasons regular reviews of your pension withdrawal strategy are so important.

Spiking inflation will also potentially put pressure on anyone following the 4% rule to the letter. Indeed, this should be considered by anyone planning to hike withdrawals to maintain their spending power.

The real risk to a sustainable withdrawal plan will come if large withdrawals in the early years of retirement are coupled with big falls in the value of your investments – something often referred to as 'pound-cost ravaging'.

This doesn't mean you shouldn't increase withdrawals to keep pace with inflation. Indeed, many will feel they have little option given the scale of price increases we are seeing in the economy. The most important thing is to have sustainability in mind when making these decisions, stay engaged and review your withdrawal plans at least once a year.

DO YOU HAVE A QUESTION ON RETIREMENT ISSUES?

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

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

Want a guaranteed income for life? It's worth noting annuity rates are going up

Annuities won't suit everyone in retirement but some will like what's on offer

There was a time when 90% of retiring investors bought an annuity with their pension pot, but in 2015, that radically changed.

The pension freedoms swept away many restrictions and allowed retiring pension savers to access as much of their pension cash as they wanted. The result is that nowadays, only around 10% of people buy an annuity. The big question is whether that is about to change.

The pension freedoms clearly had a huge impact on annuity purchases, but they also coincided with a period when interest rates were exceptionally low. With rates now going up, it's worth taking another look at the annuities space.

WHAT IS AN ANNUITY?

For the uninitiated, an annuity is an insurance product, where you swap a lump sum from your pension for an income for life.

Insurance companies base their annuity rates on bond yields, which have been hugely depressed for the last decade by loose monetary policy.

That is now changing, and the Bank of England is hiking interest rates aggressively. As a result, annuity rates have increased by around 20% this year. Based on a £100,000 pension pot, a 65-year-old can now get an income of £5,970 a year, or almost 6%, according to the MoneyHelper service.

A 6% income may sound attractive to many investors, who are perhaps used to a dividend yield from the stock market of around 3% to 4%. But there is a key difference between investment income and annuity income that means it's not a like-for-like comparison.

If you receive dividends from shares or funds, you still also have your capital invested. By contrast, with an annuity you are swapping your capital for income, so you'll no longer have a pension fund to

speak of, just an income stream.

That means a 6% annuity rate includes your capital being fed back to you, for the rest of your life. And while we know death and taxes are certain, their timing is not.

IMPORTANT POINTS TO CONSIDER

If you live a long time, an annuity might be an extremely good choice. But if you die early, you may not have received much of your money back before death, and unlike keeping your pension invested, there is no lump sum left to pass on to beneficiaries.

You can build a spouse's pension into an annuity, which continues to pay out to your spouse or civil partner after your death. A common option is a 50% spouse's pension, which continues to pay out half the income you were receiving. But depending on the age of your spouse, this could reduce the annuity rate you get by 5% to 10%, maybe more if they are significantly younger than you.

It may also be possible for retiring investors with certain health or lifestyle conditions to lock into a higher income too, because statistically speaking, insurers expect them to die at younger ages.

For instance, a regular smoker might be able to pick up a 10% uplift on standard annuity rates. If you've had a stroke or heart attack, you'll likely get more.

WILL THE PAYMENT RATE CHANGE?

It's important to note the 6% annuity rate on offer today also stays level for life, so it will be eroded by inflation over time.

At 2% inflation, an annual income of £5,970 would only be worth £4,900 in 10 years' time, and £4,020 in 20 years' time.

Periods of high inflation like we are seeing today will do even more damage. You can opt for an annuity that rises in line with inflation, but again, this reduces the initial income you get.

In our example of the 65-year-old with a £100,000 pension pot, they would initially get an annuity of just £3,220 a year, rising in line with RPI thereafter.

CAN WE EXPECT A BOOM IN ANNUITIES NOW?

It would be remarkable for the 20% rise we have seen in annuity rates this year to have absolutely no effect on their popularity. But the increase in pension savers attracted to annuities is still likely to be marginal.

Even when 90% of people bought an annuity, many of them did so begrudgingly. People really don't like the fact that if you get hit by a bus the day after you buy your annuity, all the money you have saved up over the years might bite the dust too.

Keeping your money invested in your pension is risky, but it also has benefits, like hopefully seeing your money continue to grow, passing what's left of your pension savings on to your family after you die, and managing your income to keep your tax bill in check.

- ✓ **Annuity rates are improving – they've gone up 20% this year alone**
- ✓ **They offer you a fixed income for life**
- ✗ **Your annuity ends when you die so you cannot pass on wealth this way like a pension**

UNDERAPPRECIATED ANNUITY BENEFIT

The one thing that people probably underestimate is the potential to live a very long life. More and more people are living into their nineties and even past their hundredth birthday.

Seen from this perspective, a guaranteed income for life can be a very valuable thing, if the rate on offer is a good one.

Most of us will get a guaranteed income in the form of the state pension, but at £185.15 a week, that's not enough to live a particularly comfortable life.

Some people may also be lucky enough to have defined benefit pensions, which also give them a guaranteed income for life. But many won't, and so an annuity should at least be a consideration, especially if rates rise further from here.

The good news is investors can split their pension fund if they want, using some of it to buy an annuity, and keeping the rest invested. That way they get a bit of income security, and a bit of growth and flexibility too. As annuity rates rise, more people might give this mix and match approach a proper look.

By **Laith Khalaf**
AJ Bell Head of Investment Analysis

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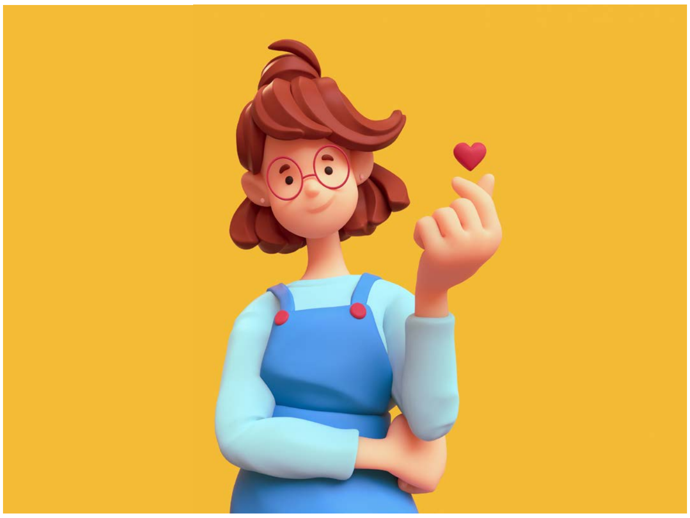

KEY ANNOUNCEMENTS OVER THE NEXT WEEK

Full-year results:

25 August: Hays, Morses Club.

Half-year results:

23 August: Aferian, **24 August:** Anglo Pacific, **25 August:** CRH, Faron Pharmaceuticals, Grafton, Hunting, Macfarlane, Puretech Health.

Trading updates

25 August: Benchmark Holdings.

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