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SHARES

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PLUS

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THREE CHEAP UK STOCKS TO BUY IN THE VALUE RALLY

WHY COVID WINNER KRAFT HEINZ COULD PROVE TO BE **A VALUE TRAP**

It is not too late to play the rally in value stocks

We explain ways to find cheap companies whose share prices could head higher

Around the world there is a universal cry from value fund managers of 'I told you so', as they finally see the value rally that's been predicted for what seems like a decade. Previously unloved stocks are moving fast, and retail investors are now having to look at a part of the market that they could previously afford to ignore (and for a long time).

Fortunately, it's not too late to go hunting as plenty of so-called value stocks have yet to join in the party. Screening for them is relatively easy, the harder part is working out why they are laggards – is it because of negative factors hanging over these businesses or has the market simply not awoken to certain opportunities?

Value stocks are moving higher on the basis that a Covid-19 vaccine will soon be approved and distributed to millions of people. That should help to reopen society and pave the way for companies to earn more money as economies recover.

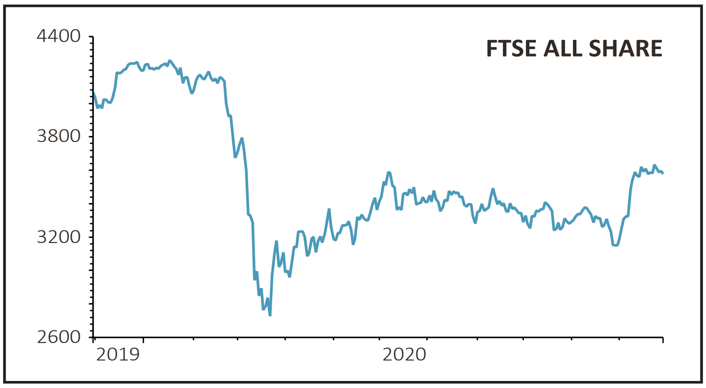
It's a rare chance to buy stocks with improved growth prospects on lower earnings multiples relative to the faster growth stocks which have been in demand for the past decade.

Liberum says we are now in phase five of the current crisis, 'where increasing visibility is driving more focus on the medium/longer-term new normal and away from short-term uncertainty'.

It says historically, in such phases, value and small cap stocks have significantly outperformed over six to nine months, with a return to growth thereafter remaining a theme for the next five years.

Anyone with access to a basic stock screening system can find companies that fit the value bill. Look for stocks trading on a price to earnings multiple of less than 20 and which have positive earnings growth forecast for 2021 and 2022. A good screener should also let you see the share price change between certain dates.

A look at the FTSE All-Share chart would suggest the value rally began in earnest at the start of



November, so you could run a screen looking at share price change since 30 October (the last trading day of the month) and now, as well as share price change between 1 January and 30 October to see the performance before the value rally took flight.

The worst performing stocks so far in November aren't all value ones – they include many fast growth and/or quality stocks that were previously sought-after, now shunned by investors in favour of value ones.

Another way to look for laggards is to examine stocks furthest below their 52-week high. 'Many of these stocks have bounced hard since the end of October, with the energy and travel and leisure sectors particularly well represented,' says broker Peel Hunt. 'Even if they doubled again from here, they would remain below their 52-week high.'

This week's issue of *Shares* discusses three UK value stocks that are laggards yet where there are reasons to be more optimistic. We also look at ways to play the value theme in the US market via funds. If that's not enough to whet your appetite, it's worth looking at our recent article on **Aurora Investment Trust (ARR)** which is also relevant to the value theme.

By **Daniel Coatsworth** Editor

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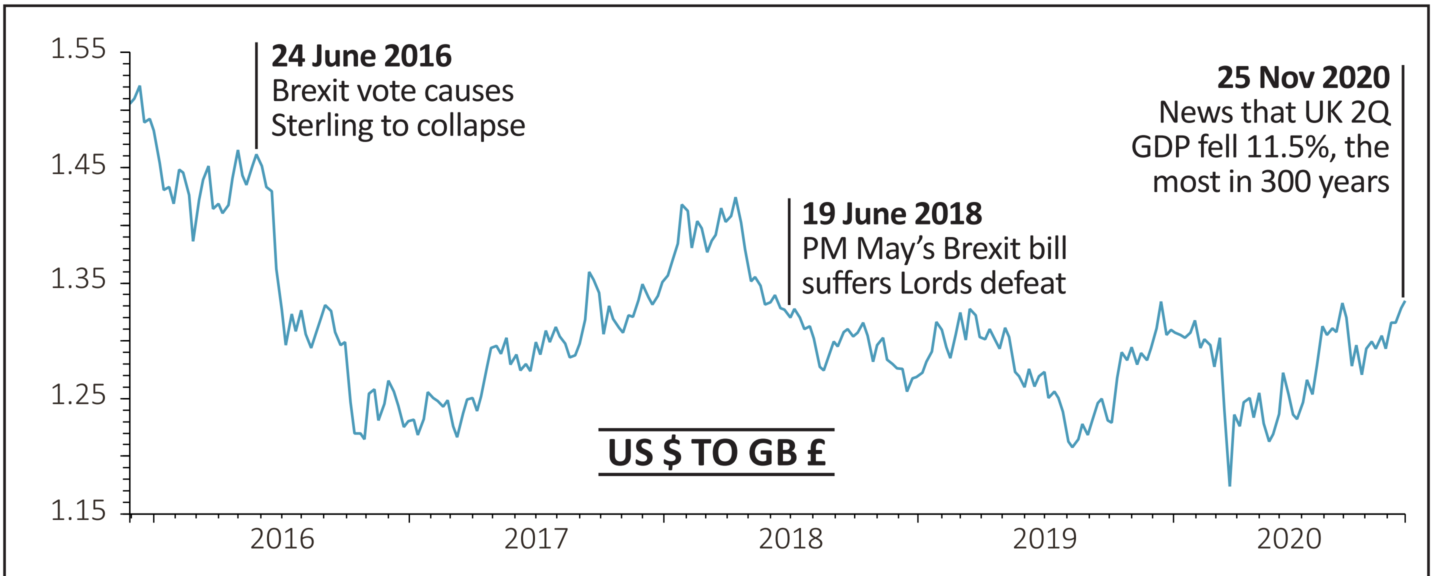
THE
MONKS
INVESTMENT
TRUST
We look to the future.
To meet your aspirations.
Our annual research agenda outlines key themes we intend to focus our attention on over the year ahead. We use it as our guide to hunt for unrecognised growth opportunities. We believe looking forward rather than backwards helps us find those companies that will shape the future. And we believe it's a better way to deliver returns you can look forward to. Over the last five years the **Monks Investment Trust** has delivered a total return of 200.0% compared to 152.8% for the sector*.

Standardised past performance to 30 September*	2016	2017	2018	2019	2020
MONKS INVESTMENT TRUST	37.9%	35.6%	19.1%	7.8%	24.9%
AIC GLOBAL SECTOR^	29.0%	26.2%	19.2%	-0.2%	34.5%

^Weighted average.
Past performance is not a guide to future returns. Please remember that changing stock market conditions and currency exchange rates will affect the value of the investment in the fund and any income from it. Investors may not get back the amount invested.
Find out more by watching our film at monksinvestmenttrust.co.uk
A Key Information Document is available. Call 0800 917 2112.
BAILLIE GIFFORD
Actual Investors

Consequences of the pound rally on certain UK stocks

Further currency strength could erode earnings for many large companies on the London Stock Exchange



In a scenario which most people involved with markets never imagined, let alone predicted, the pound is about to reach an important trading level as hopes increase of a UK trade deal with the EU.

Having collapsed to just above $1.15 to the dollar at the height of the panic selling in March, sterling has muscled its way back to its pre-pandemic highs of $1.34 and investors with an eye on currencies will be watching to see if has the momentum to head closer to $1.40.

The rally in the pound is in spite of the worst contraction in UK economic output in over 300 years, one of highest mortality rates from coronavirus in the developed world, and the lingering threat of a 'no-deal' Brexit which could see the country facing World Trade Organisation tariffs on everything from toilet rolls to cars.

UK companies which do most of their business in the US or export most of their products in dollars have benefitted from the weakness of the currency since the Brexit vote in 2016 as overseas earnings are converted back into pounds.

A move back to a higher trading band would therefore enhance returns for UK investors owning dollar assets, but at the same time reduce profits for big overseas earners whose shares are priced in sterling. Obvious casualties would be firms such as Ashtead (AHT) and Ferguson (FERG), which generate most of their sales and earnings in North America.

According to FTSE Russell, 62% of FTSE 100 revenues are generated overseas, and even the FTSE 250, which is more domestically focused, still generates 35% of sales from outside the UK.

It's worth considering how exposed your portfolio may be to overseas earnings and to prepare for more warnings from companies about 'currency headwinds' as we move into 2021.

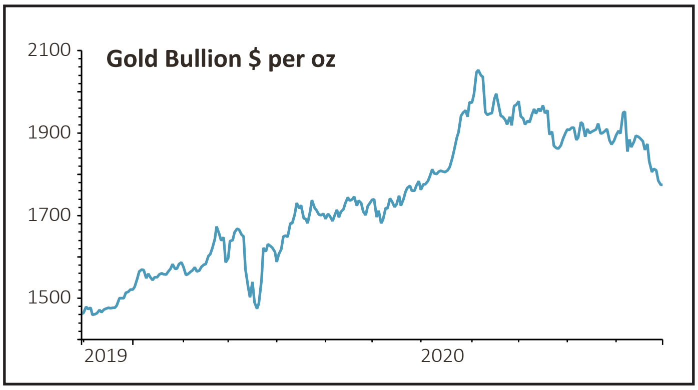
Here's why gold has sold off, copper has rallied and oil remains volatile

Investors have turned against gold but copper is back in vogue, while OPEC's delay has failed to calm oil markets

Positive coronavirus vaccine news has overwhelmingly been welcomed by investors with hopes solidifying that our lives and the economy can start getting back to normal next year.

But there is one corner of the market where such upbeat news has triggered a sell-off – gold.

A safe haven asset in times of uncertainty, gold reached all-time highs earlier this year as investor nervousness peaked, but has since declined from highs of around $1,980 per ounce at the end of July to trade around 10% lower at $1,790.



There are a few reasons for this. Firstly, the vaccine news gives some certainty over the global economic recovery, reducing the general risk of stocks and so diminishing the appeal of safe havens like gold.

Secondly, US president-elect Joe Biden has begun announcing his Cabinet and has named Janet Yellen his Treasury secretary. A former chair of the US Federal Reserve, her accommodative policies were positive for riskier markets like stocks and currencies over most of the last decade, also reducing gold's appeal.

But Yellen's appointment could have some positives for gold as it potentially raises the chance of interest rates staying lower for longer, with lower interest rates typically benefitting gold.

Finally, Biden now looks to be the clear winner of the US election, with president Donald Trump not conceding but agreeing to have his team transition to the new administration, again removing a barrier of uncertainty.

One commodity gaining traction meanwhile is copper, which has hit four-year highs on the London market, trading at around $7,674 per tonne and up around 12% on a monthly basis.

Copper is an economic bellwether and, as well as Covid-related mine closures affecting supply, its rising price reflects higher demand as economies around the world – particularly in China, the world's biggest consumer of copper – start to recover.

Investment bank Goldman Sachs is certainly bullish and set a price target of $9,500 a tonne for copper, up from $7,500. It also says it's 'highly probable' that by the first half of 2022 copper could test its record high of $10,170 set in 2011.

It's also been a big week for oil. A delay in an expected decision by oil producers' cartel OPEC and Russia to extend production cuts due to expire in January from 30 November to today (3 Dec) will do little to stem volatility in the market.

The organisation faces a tricky balancing act as it eyes a post-Covid reopening of the global economy on which the timing is uncertain. The danger being that if production is increased at a time when demand is still depressed it will put prices under renewed pressure.

Reportedly Saudi Arabia wants to maintain the status quo, Russia is pushing for a phased increase in output, while UAE will only commit to quotas if other OPEC members comply.

Kingspan ESG credentials clouded by Grenfell inquiry

The company's marketing of an insulation product is in the spotlight

Specialist building products firm **Kingspan (KGP)** is under scrutiny for the role of one of its insulation products in the 2017 Grenfell Tower fire which claimed the lives of 72 people.

Directors in the company are being questioned at an inquiry into the tragedy and since it made its first submission to the hearings on 5 November the shares have lost more than 10% of their value to trade at €72.55.

Recent news articles have focused on director share dealings in September and October ahead of the inquiry, among which saw chief executive Gene Murtagh book a £3.1 million profit.

Kingspan fire-tested its K15 cladding product in 2005 but, despite subsequently changing the formulation of K15, used the original test to sell the material as appropriate for use in high-rise buildings.

For its part the group has acknowledged and apologised for 'process shortcomings during the period 2005 to 2014' but stressed it did not advise on the suitability of K15 for use on Grenfell Tower. K15 was used on a small percentage of the façade with the remainder provided by another manufacturer, Celotex.

Kingspan is a big holding in many ESG (environmental, social and governance) funds including products from Baillie Gifford and Liontrust.

The company's ESG credentials, based on its contribution to energy efficiency through high performance 'building envelope' solutions, have contributed to a premium valuation of 32.7 times consensus forecast 2021 earnings per share.

Investors warned of tracker flip risk ahead of Tesla's S&P 500 entry

Shares in the electric car maker have soared 39% in two weeks

THERE IS A risk that the brakes could be slammed on Tesla's astonishing November run when it joins the S&P 500 index on 21 December. Experts believe that last month's astonishing share price surge may have been powered by a mad dash for Tesla stock by thousands of private investors who hope to flip their shares to tracker funds as they adjust portfolios to reflect the new S&P index entry.

But some market watchers have warned that too much stock may have been snapped up in the buying binge, and that these shares will not easily find new homes at current levels.

Calculations suggest that about 120 million Tesla shares will be needed to satisfy index fund demand when the electric car maker enters the S&P, about 15% of the free float after excluding Musk's personal 18% stake.

Since the Elon Musk-founded business won a spot in the exclusive index on 17 November, more than 480 million shares have changed hands, sending Tesla's share price soaring 39% to a record $585.76 on 27 November.

That implies a market value of $538 billion, which would make it the S&P 500's sixth largest company, ahead of Warren Buffett's Berkshire Hathaway and Walmart, the world's biggest retailer, despite being ranked number 367th on earnings.

Fabric coating Covid killer HeiQ to join UK stock market

As well as consumer and home products there is a huge potential market for the company in public transport

When a company makes a claim that its fabric coating kills all known bacteria and viruses including Covid-19 within 30 minutes and has a shelf-life of up to seven years, it tends to get attention.

The Viroblock product from Swiss-based **HeiQ Materials** was originally developed as an antimicrobial for the Ebola crisis in 2013 and now it is seeing strong demand following the Covid-19 pandemic.

Investors will soon get a chance to buy its shares as HeiQ is coming to the UK stock market on 7 December via a reverse takeover of cash shell **Auctus Growth (AUCT:AIM)**.

Oliver Brown, fund manager of **MFM UK Primary Opportunities (B905T77)**, told *Shares* that the founders happened upon the antimicrobial opportunity after completing long walks in the Swiss mountains and getting complaints from their wives about the smelly clothes.

In addition to Viroblock, HeiQ has built a presence in textile performance materials that provide enhanced features such as cooling/heating and water repellence.

It boasts blue chip clients such as Swedish company IKEA, luxury goods brand **Burberry (BRBY)** as well as performance brands North Face, Champion and New Balance.

RC Brown, Premier Miton and Amati Global Investors are among the institutional investors backing the company at the stock market listing.

Amati fund manager David Stevenson says a key attraction is HeiQ's intellectual property amassed since 2005 including multiple patents and awards for its innovative technologies.

Based on the £140 million valuation at listing,

HeiQ will trade at around 3.5 times sales compared to the 7.1 times of infection prevention specialist **Tristel (TSTL:AIM)**, and 4.4 times for antimicrobial products company **Byotrol (BYOT:AIM)**.

The company is forecast to see annual sales grow by 50% in 2021 slowing to 30% in later years. Profit for the first half of 2020 was $8.6 million.

LIFE SCIENCES INDUSTRY VETERAN DAVID EVANS LAUNCHES NEW INVESTMENT COMPANY

Life sciences veteran David Evans is using his 27 years' experience and deep industry contacts to launch an investment fund.

Intuitive Investments will start trading on AIM on 14 December via a placing of 37.5 million new shares at 20p, raising £7.5 million.

Evans told *Shares* that the company will deploy the funds into seven investments over the next two to three years with the goal of growing net asset value by 20% a year.

The idea is to build a balanced portfolio of both early and late stage investment opportunities. The first two deals are expected to be pre-IPO and late stage investments.

The companies eyeing Arcadia assets after collapse

The fallout as Phlip Green retail empire enters administration

The collapse of Philip Green's Arcadia Group, owner of Topman, Topshop, Burton and Dorothy Perkins, into administration is widely expected to see rival retailers bid for these brands.

The announcement also prompted **JD Sports (JD.)** to abandon its plan to buy department store Debenhams out of administration, with the 200-year-old chain facing liquidation – notably because Arcadia had concessions in Debenhams stores.

JD's decision to terminate this prospective deal has been greeted with relief by investors who saw the transaction as too risky. Interestingly Shore Capital analyst Clive Black believes Mike Ashley's **Frasers Group (FRAS)** might look at some of Debenhams' assets, namely the Maine and Mantaray brands.

Among the potential predators as Arcadia is broken up are JD itself, Frasers and online firm **Boohoo (BOO:AIM)**. Boohoo has form for buying ailing high street brands and taking them online, including Karen Millen, Coast, Warehouse and Oasis.

These latest developments are more bad news for landlords of physical shops and shopping malls, such as **Hammerson (HMSO)**, and it appears likely that there will be further consolidation in the retail space as the impact of the pandemic continues to be felt.

Hipgnosis benefits from change in valuation method

Music royalties are being seen as a less risky investment

MUSIC ROYALTY INVESTOR **Hipgnosis Songs Fund (SONG)** says its independent valuer has lowered the discount rate used to calculate how much its music catalogues are worth, thereby giving a big boost to the value of the investment trust's assets.

The move was done to reflect 'the decreased risk premium associated with music's more stable and predictable earnings as a result of the increased consumption of music through paid streaming,' according to Hipgnosis. By cutting the discount rate from 9% to 8.5%, Hipgnosis's net asset value increased by 9%.

The trust buys the rights to certain songs and enjoys royalty payments when they are streamed, appear on the radio, feature in adverts, films or TV shows, or are played in shops, restaurants or gyms.

Recent acquisitions have included songs by Grammy award winning songwriter Rick James and Fleetwood Mac's smash hits, *Go Your Own Way* and *The Chain*.

A rival investment vehicle to Hipgnosis has recently joined the London Stock Exchange. **Round Hill Music Royalty Fund (RHM)** has risen 4% to $1.04 since listing on 13 November. It plans to buy a catalogue of music rights that includes songs by The Beatles, Celine Dion, The Rolling Stones, Louis Armstrong, Marvin Gaye and Elvis Presley.

Cheap access to a hot style with a 4.9% yield

BlackRock North American Income looks very appealing in the current climate

With the contentious US presidential election seemingly settled and Covid-19 vaccines on the way, multinational companies that do best during periods of global growth could see a more favourable backdrop.

That scenario would be welcomed by the **BlackRock North American Income Trust (BRNA)**, a value-oriented fund invested in higher-quality large businesses.

BlackRock North American Income has scope for performance improvement if value names continue to rally. As such, a 6.5% discount to net asset value (NAV) and 4.9% dividend yield should appeal to income seekers in the ongoing era of persistent low interest rates.

Its 12-month average discount to NAV is 4%, according to Winterflood, meaning investors can currently pick up the trust at a real bargain price. A slight downside is that its 1.1% ongoing charge is higher than the AIC North American sector average of 0.96%.

Launched in late 2012, BlackRock North American's objective is to provide an attractive and growing level of income along with long-term capital growth. It has the capacity to invest up to 20% overseas at the time of investment.

BLACKROCK NORTH AMERICAN INVESTMENT TRUST

BUY

(BRNA) 162.5p

Market cap: **£129.7 million**

Managers Tony DeSpirito, Franco Tapia and David Zhao seek to uncover dynamic companies with dividend growth potential and the power to compound growth over many years, and they use options to generate additional income for shareholders.

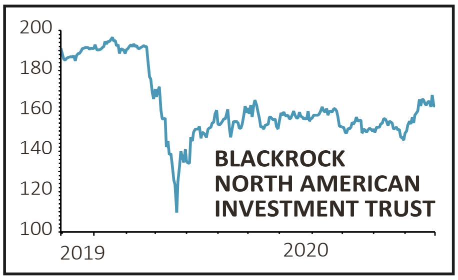
'The managers have a long-term history of working together, including at Pzena Investment Management before they joined BlackRock North American,' says Kepler analyst William Sobczak. 'They believe this familiarity helps their investment decisions – in particular, enabling honest and open debate during the stock selection process.'

When it comes to stocks, DeSpirito, Tapia and Zhao look for high-quality franchises and companies with strong dividend payout potential while keeping an eye out for dividend initiations too.

The trust's emphasis on quality, cash-generative businesses that can grow their dividends over time – principally financials such as insurers and banks, energy infrastructure stocks and software companies that aren't egregiously valued yet boast predictable growth trajectories – means the portfolio also has a defensive bent that should serve shareholders well if the pandemic-induced recession lingers for long.

As at the end of October, top 10 positions included mobile phone network Verizon and banking behemoths Bank of America and Citigroup, as well as media giant Comcast and health insurer Anthem.

According to the latest factsheet, the managers initiated new positions in Zimmer Biomet, Exelon, Philip Morris, **British American Tobacco (BATS)** and First American Financial in October, while exiting **BP (BP.)** and reducing exposure to Wells Fargo, Altria, **BAE Systems (BA.)**, Medtronic and Verizon.



Primark owner Associated British Foods is well placed for a recovery

ABF's profitable and growing foods business also offers important diversification

Value looks to be back in fashion in more ways than one, and one of the best ways to play both investors' and consumers' eye for a bargain is through Primark owner **Associated British Foods (ABF)**.

Market expectations for the company are subdued and it trades on an undemanding 12-month forward price to earnings ratio of 17.9.

But as the economy looks set to recover going into 2021 as coronavirus vaccines get rolled out and lockdown restrictions start to ease, ABF's Primark business in particular – which accounts for two thirds of the company's profit – appears to have numerous factors in its favour.

BULLISH ON PRIMARK

Even if the economic recovery isn't as strong as expected Primark's unique business model and market position mean it should do well as long as shops are open for business. That's evidenced by its fourth quarter trading over the summer which 'exceeded expectations' as lockdown restrictions started to ease.

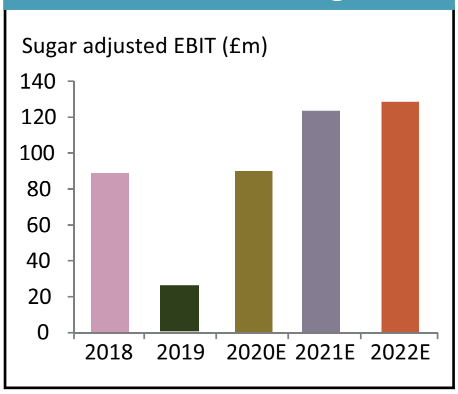
The troubles facing rivals like Debenhams and Topshop owner Arcadia should also benefit Primark, with their stores either set to close or shrink, strengthening its position on the high street.

Credit: Primark

ASSOCIATED BRITISH FOODS
BUY
(ABF) £21.46
Market cap: £17 billion

While another tailwind for the business in the run-up to Christmas is the decision in England to allow shops to stay open day and night, running from Monday to Saturday, during December and January, with Primark saying it will keep 11 of its stores open 24 hours a day.

The outlook for ABF's sugar division is much brighter



Source: Company reports, Berenberg estimates

PRIMARK BUSINESS MODEL

Analysts at Berenberg believe something that helps set Primark apart is its unique business model, which is centred on a flexible, low-cost supply chain, the continuous release of new products, and store managers who are empowered to make localised decisions on product selection, merchandising and price.

'As such, it has best-in-class sales densities (twice those of Next Retail), which in turn enable it to offer exceptional value and should allow it to take considerable offline market share,' they say.

The company also has a

Credit: Associated British Foods

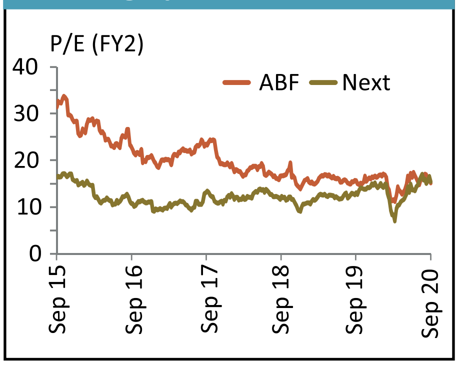
strong balance sheet with liquidity of over £3.1 billion, and it is widely expected to be one of the first retailers to reinstate its dividend when the economy picks up again.

RISKS TO CONSIDER

It's important to note there are risks with ABF surrounding any further restrictions that could be imposed, as evidenced by the £375 million sales hit it took as a result of the second England lockdown, with 57% of Primark's total selling space temporarily shut down.

It's also worth highlighting that one headwind for Primark is undoubtedly its lack of online capability. There is a Primark website with most of its products shown, but you cannot buy anything. This is one reason why

ABF trades at a small discount to Next, versus a five-year average premium of c60%



Source: Berenberg, Datastream

the business trades on a lower multiple to some of its peers.

UNDERAPPRECIATED STRENGTHS

Analysts at Berenberg believe the market underestimates Primark's ability to flourish in times of economic difficulty, and point out that during the global financial crisis, like-for-like growth ramped up from 1.8% in calendar year 2007 to 4.8%, 6.8% and 5.8% in each of the following three years as its low-priced products benefitted from consumers trading down during and after the global financial crisis.

They also believe Primark's significant international roll-out opportunity is also underappreciated by the market.

Primark has stores outside of the UK in countries like Spain, Portugal, Germany and the Netherlands, and is also expanding in the US. In addition, it has opened stores in Slovenia and Poland as it looks to enter Central and Eastern Europe, a market coveted by companies like budget airline **Wizz Air (WIZZ)** for example because of its high growth potential.

NON-RETAIL ACTIVITY

There is also more to Associated British Foods than Primark, as its name suggests, with the group offering important diversification of revenue and earnings through its foods business, which includes brands like Jordans, Ryvita and Twinings, and makes ABF the world's second largest producer of sugar and baker's yeast.

ABF generates around half of its revenue and roughly a third of its profit from its four food

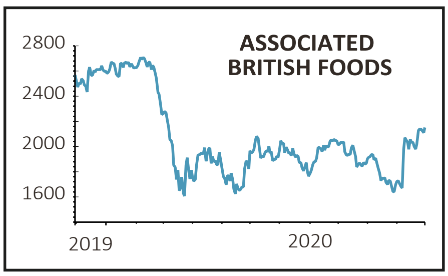

Credit: Primark

businesses, with all of them having increased profits in the year to September 2020 despite the pandemic.

Berenberg expects ABF's sugar business to continue its recovery in 2021 – the division had a bad time in 2019 as a result of the end of the EU sugar regime in 2017 and resulting fall in sugar prices – with one-off headwinds for its Illovo sugar brand now over and average sugar prices rising across Europe.

It also expects ABF's Twinings Ovaltine drinks business to continue to outgrow the other elements of the grocery division, which should help drive mix-related profit margin improvement in that business.

Overall, the analysts see ABF's food businesses growing at a 10% compound annual growth rate between 2019 and 2022.



PETS AT HOME

(PETS) 415p

Gain to date: 79.6%

Original entry point:

Buy at 231p, 5 September 2019

DESPITE A MINI wobble around the company's first half results (24 Nov), our positive call on specialist retailer **Pets at Home (PETS)** continues to bear fruit.

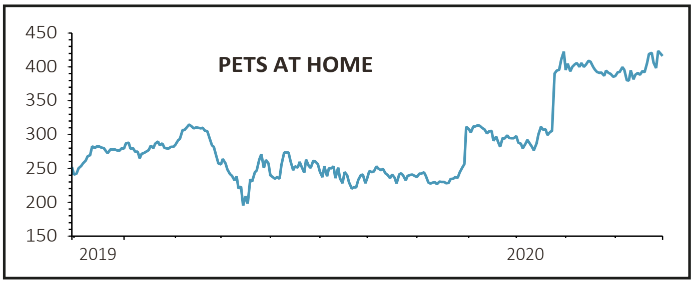
The company has subsequently announced the £15 million acquisition of animal health telephone service The Vet Connection (30 Nov) and the £100 million disposal of its Specialist referral hospitals to veterinary group Linnaeus (1 Dec).

This latest deal suggests the company is narrowing its focus to the online and retail stores and so-called 'first opinion' vet practices.

Following the transactions Shore Capital analyst Greg Lawless commented that there were 'lots of moving parts to model' but added: 'We like the Pets strategy which mixes the products and services and the self-help levers available to the company, through increased personalisation from data from the VIP loyalty club.'

Alongside numbers covering the six-month period to 8 October, Pets said a stronger second quarter performance had continued into the third quarter but also cautioned on Covid-19 risks.

Pre-tax profit increased to £38.9 million, up from £34 million year-on-year, as revenue grew 5.1% to £574.4 million.



SHARES SAYS:
We still back the strategy. Keep buying.

AVIVA

(AV.) 326p

Gain to date: 8.3%

Original entry point:

Buy at 301p, 17 September 2020

NOVEMBER BROUGHT A raft of good news from the UK's largest insurer in the shape of resilient nine-month earnings and news of two disposals for a combined £2 billion.

Trading to the end of September saw a strong performance from the UK and Irish life business as well as positive net fund flows in the savings and retirement business.

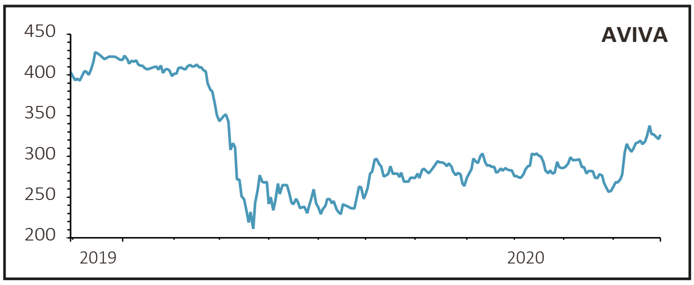
In the commercial market, the firm increased its premiums through higher rates and targeted growth, while it reduced its individual premiums as it targeted a more profitable, tightly-run portfolio.

With its Solvency II coverage ratio of 195%, and a policy of returning excess capital above 180% to shareholders, the firm proposed a 2020 dividend of 21p per share which it said would grow by 'low to mid single digits'.

Although this was a steep drop compared with prior years, investors took the news well and shares continue to make six-month highs.

Chief executive Amanda Blanc reiterated her commitment to 'simplify the business' and increase value for shareholders, which she carried through with the earlier than expected monetisation of the Singaporean life business and the sale of a majority stake in the Italian life business.

Further disposals in Italy, France and Poland are mooted, which should guarantee the firm's Solvency coverage ratio going forward.



SHARES SAYS:

We remain positive. Keep buying.

THE PANOPLY HOLDINGS

(TPX:AIM) 200p

Gain to date: 122%

Original entry point:

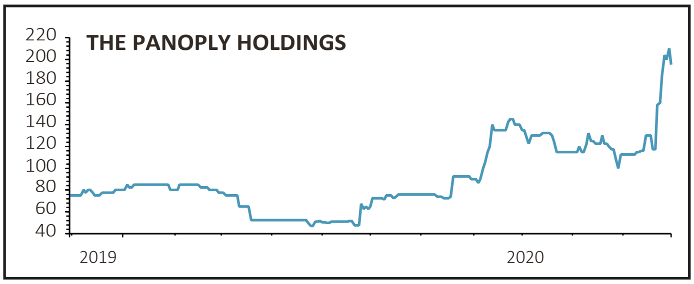
Buy at 90p, 6 August 2020

IT HAS BEEN a quite astonishing ride for **The Panoply Holdings (TPX:AIM)** and we could barely have timed better our original *Great Idea*. To more than double in value is impressive, but to do so in four months is truly remarkable.

Knock-out interim results to 30 September 2020 only bolster our confidence in the firm's fantastic prospects, with £21.2 million of revenue meaning 18% organic growth year-on-year. Underlying adjusted earnings before interest, tax, depreciation and amortisation (EBITDA) shot up 37% to £2.9 million.

Clearly The Panoply has benefitted from accelerated digital transformation trends through the pandemic, but operating efficiencies have also paid off. Seventy percent of revenue comes from the public sector, but rather than new business being bogged down in bureaucracy, as you might imagine, contracts are being won and implemented in weeks not months.

Also encouraging, founder Neal Gandi confirmed to *Shares* that the company's impressive cash generation means future acquisitions, a key part of the growth story, will not need extra funding, capping the threat of dilution to existing shareholders.



SHARES SAYS:

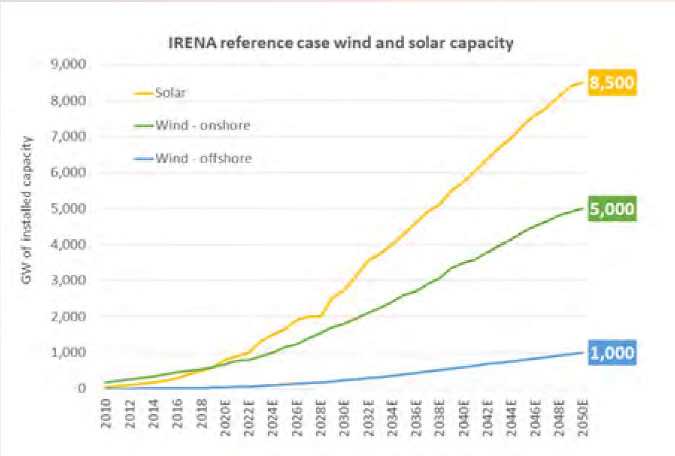
The Panoply may be small, but it does not lack in ambition or opportunity. Still a buy even after its stunning run.

STRONG GROWTH OUTLOOK FOR SUSTAINABLE ENERGY

Exciting trajectory of new wind and solar electricity supply ahead

The energy transition is upon us and it is happening first and foremost because of attractive economics; the cost of producing electricity from wind and solar is now competitive with fossil fuels in around 90% of all global electricity markets. Government commitments to reduce carbon emissions ensure that a great industrial revolution will play out in sustainable energy between now and 2050.

At Guinness we began investing in the sustainable energy area- of which solar and wind are a major component- in 2006, and we have developed a deep understanding of the forces at work. In the early years, up until 2017, we found that rapidly falling solar panel and wind turbine prices, combined with erratic government subsidies, were a headwind to profit growth for many of the companies in the space. However, these pressures enabled a remarkable transition in the cost structure of renewable power leading to, for example, the cost of manufacturing solar cells to fall by 28% on average for every time that solar industry manufacturing capacity doubled.



The chart shows the growth in solar and wind power generation capacity worldwide over the last 10 years and the base case projection for the next 30 years from the International Renewable Energy Association (IRENA). Despite their growth assumptions, IRENA believe their assumption of 14,500GW in 2050 is not aggressive enough to achieve net zero CO2 emissions in 2050 globally. We agree.

Solar and wind capacity in 2019 generated 2,100 TWh of electricity (8% of total world electricity demand, according to BP). We forecast wind and solar installations grow from 1,200GW of capacity in 2019 to around 17,000GW of capacity in 2050 meaning they will generate over 35,000TWh of electricity in 2050 (a growth rate of 19.3%pa). In 2050, solar and wind will represent around 60% of total world electricity generation (estimated to be 54,000TWh, up around 100% versus 2019 levels). While these are high growth rates for infrastructure assets, we believe that our electricity demand numbers may prove to be light if population growth, energy intensity and the electrification of transportation play out as we believe they could. As sensitivities, we consider the following three factors:

- The global electric vehicle fleet consumed 80 TWh of electricity in 2019 and is now 7m vehicles out of 1,400m total vehicles. If the entire fleet became electric and the driving range of the EVs increased, it would consume 20,000 TWh (adding 80% to current total global electricity demand) (source: Guinness based on extrapolating IEA data).

- World population is projected to grow from 7.8bn to 9.7bn by 2050 (adding 24% to current electricity demand if electricity usage per head remains unchanged).

- GDP per capita is $39,348 per capita in OECD members (1.29 bn population) and $5,900 per capita elsewhere (6.51 bn population). If GDP per capita outside the OECD doubles by 2050 it would add $38trn to global GDP, which is currently $89.2trn (this would increase electricity demand by 43% if usage per $ of GDP is unchanged).

If all of these happened, electricity usage would rise by an additional 147% not just rise the projected 100%. Our lower demand figure allows for efficiency gains and some use of other transport systems such as hydrogen or biofuels yet it still requires significant new infrastructure investment in carbon capture and energy storage technologies to ensure that energy can be delivered into the grid to satisfy periods of demand.

Why Covid winner Kraft Heinz could prove to be a value trap

The food and drink giant owns beloved global brands, but the recent sales surge may be hard to sustain

As the share price uptrend shows, investors are regaining an appetite for US-listed Kraft Heinz, the branded food and beverage behemoth where legendary investor Warren Buffett holds considerable sway.

Yet the $46.3 billion cap remains modestly valued for a global consumer staples giant due to worries over debt levels and the post-pandemic earnings outlook. Next debt is forecast to be $25.56 billion at the end of 2020.

The Nasdaq-traded company has benefitted from elevated demand during the Covid crisis, with restaurants closed and people consuming considerably more food at home, leaving sceptics to question whether its strong sales momentum can continue.

Based on Berenberg's 2021 earnings per share and dividend per share estimates of 2.4 cents and 1.6 cents respectively, Kraft Heinz trades on an undemanding forward price to earnings ratio of 14.1 – a discount to comparable global peers – while investors are also being paid to wait for a re-rating with an attractive 4.7% dividend yield, though the shares could still be a value trap as we explain in this article.

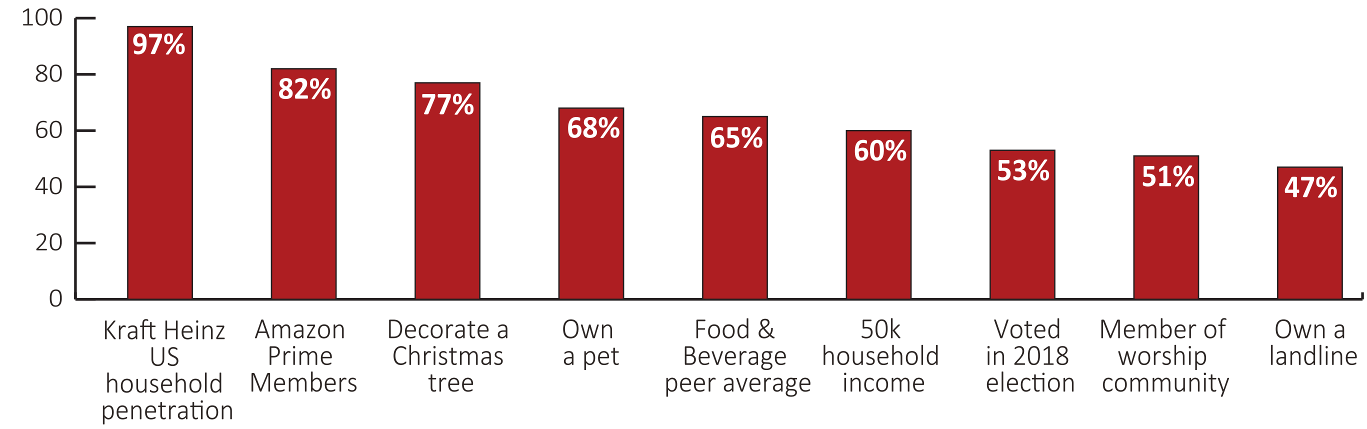
HOW DOES KRAFT HEINZ MAKE MONEY?

With the stated purpose 'Let's Make Life Delicious' the company is the product of a $55 billion, 2015 combination between Kraft and Heinz that was orchestrated by Buffett's Berkshire Hathaway and investment group 3G Capital Partners, which had teamed up two years earlier on a buyout of H.J. Heinz.

UK investors will probably recognise the Philadelphia cheese, Heinz ketchup and Kraft cheese maker best for its bold 2017 bid for **Unilever (ULVR)**.

Holding sway over 26.8% and 23.9% of the equity respectively, Berkshire Hathaway and 3G are the biggest shareholders in Kraft Heinz, which makes a diverse

Penetration of US households 2019



Source: Kraft Heinz Investor Day 2020

KRAFT HEINZ/US$

Year	Sales	Trading operating profit	EPS	DPS
2019	24.5bn	5.1	1.58	1.6
2020	26.1bn	5.5	0.53	1.57
2021	25.1bn	5.2	2.4	1.6
2020	24.7bn	5.2	2.4	1.7

Source: Berenberg

array of condiments and sauces, cheese and dairy products, meals, meats and refreshment beverages.

Guided by chief executive Miguel Patricio, the Pittsburgh-headquartered company's customers span grocers and other retailers, foodservice distributors, hotels, restaurants, hospitals and even government agencies.

Warren Buffett likes to own businesses that control beloved brands that people purchase repeatedly, so one can see why Kraft Heinz appeals to the Sage of Omaha.

Its portfolio of iconic and emerging brands includes Lunchables, Planters, Maxwell House, Kool-Aid, Jell-O and Capri Sun.

IS KRAFT HEINZ A TASTY PROPOSITION?

Kraft Heinz has an enviable brand portfolio, but some of the products have a tired feel to them.

Bears also point to the company's reliance on cost-cutting and efficiency gains to drive earnings, a key rationale behind its urge to merge with Unilever.

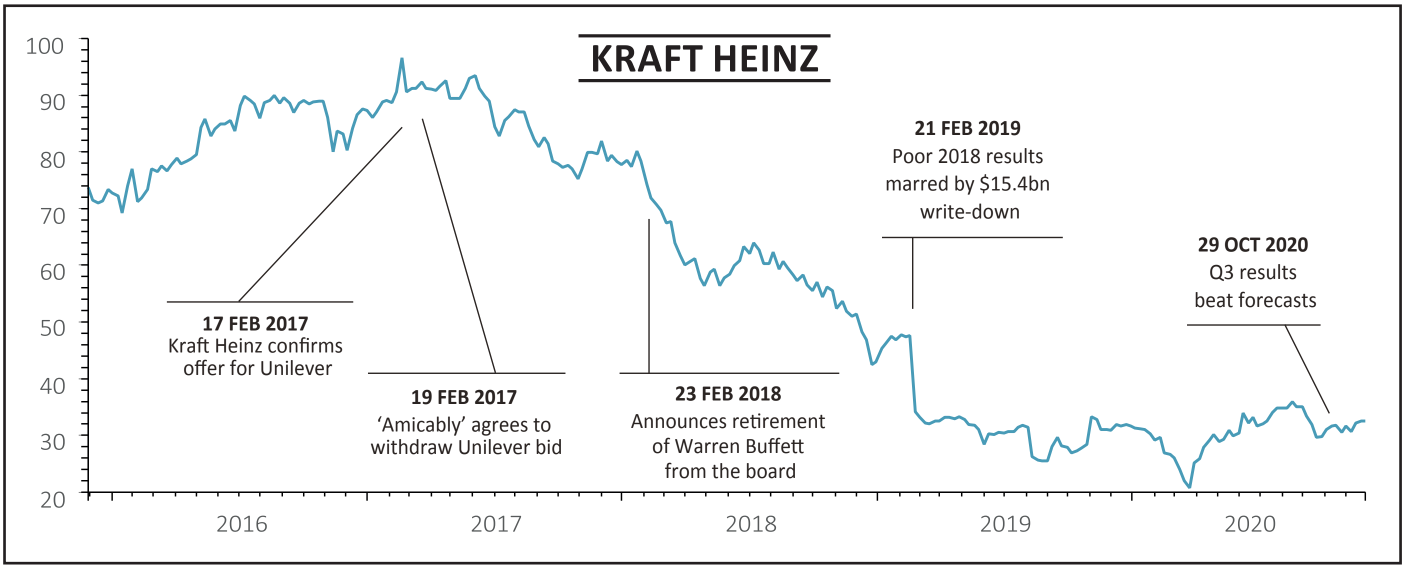
Other companies, such as Nestle for instance, are more focused on investing in the foods of the future. Investors with long memories may also recall Kraft Heinz's accounting investigation and whopping great write-down, which soured sentiment towards the stock for a time.

Kraft Heinz has been a big beneficiary of Covid-19. Its mostly 'shelf-stable' packaged products have seen elevated consumption during a pandemic in which consumers have fallen back on brands they trust and love.

Third quarter results were strong, beating market expectations on both the revenue and profit lines, with organic growth of 6.3% coming in comfortably ahead of the 4.8% consensus forecast.

This growth was driven by both volume and price, with Kraft Heinz generating strong like-for-like gains with US retailers, while the company's adjusted EBITDA margin rose 170 basis points to 25.9%, north of the 24.6% consensus estimate.

Having previously cautioned that the boom in demand for its brands was unsustainable,



management sounded more confident about the organic growth outlook with supermarket basket sizes increasing as consumers continue to cook at home.

'The continuation of our strong growth into the third quarter is a reflection of the agility we are creating as an organisation and because of that, we are raising our outlook for the full year,' explained Patricio.

'We are building momentum, and we are confidently optimistic about our near-term performance,' he continued.

'We are heading into 2021 with our new operating model fully implemented, our platform strategy coming to life in the marketplace, and our growth investments ramping up.

'And although there are multiple future scenarios we must plan for and manage against, we are in a strong position to both accelerate and exceed the strategic plan we finalised earlier this year.'

CAVEAT EMPTOR

Despite the tailwinds behind Kraft Heinz, Berenberg is lukewarm on the stock with a 'hold' rating and $37 price target (versus a $33.83 trading price at the time of writing). 'While investor sentiment is slowly improving, more confidence is required that growth will be fundamentally higher post-Covid-19 to support a sustained re-rating,' said the broker following the results.

For the 2020 calendar year, Berenberg forecasts a rise in sales from $24.98 billion to $26.1 billion and improved operating profit of just below $5.5 billion, though it forecasts a decline in revenues to $25.1 billion and an operating profit pullback to $5.2 billion in 2021.

Despite falling from their 2017 peak due to lower sales growth, increased investment and supply chain costs, Berenberg concedes that Kraft Heinz's margins are still best-in-class in packaged food.

Yet Berenberg also says Kraft Heinz faces headwinds in the form of market share gains by retailers' private label products and pricing pressure as well as retailer destocking.

Big brand owners such as Kraft Heinz are under pressure to consolidate due to international pressure on margins and constraints to their organic growth opportunities, which is one reason why it made its audacious lunge for Unilever, a company with a prized emerging markets footprint.

'With nearly 80% exposure to North America, there is little international growth to offset domestic pressures,' warned Berenberg, while also flagging that the company's new medium-term guidance is for a lacklustre 1% to 2% organic growth per year.

Investors seeking a value stock within the consumer staples space should certainly take a closer look at Kraft Heinz, although they should also be mindful that margins could decline further as it will need to invest heavily to stay competitive and may have exhausted the scope for cost savings.

Berenberg also warns that any decline in earnings in the future could also restrict the group's ability to pay down debt or even fund the dividend.

SHARES SAYS:
Kraft Heinz owns some iconic brands and has deep-pocketed backers in Berkshire Hathaway and 3G, yet we feel the elevated demand seen during the pandemic could drop away once the world returns to some normality. That means growth could disappoint. Avoid.

James Crux,
Funds & Investment Trusts Editor

WANT GROWTH?

China is the answer

By **Steven Frazer** News Editor

Experts believe that China will dominate global growth over the next decade as it continues to push ahead with its massive transition into a consumer-based economic superpower.

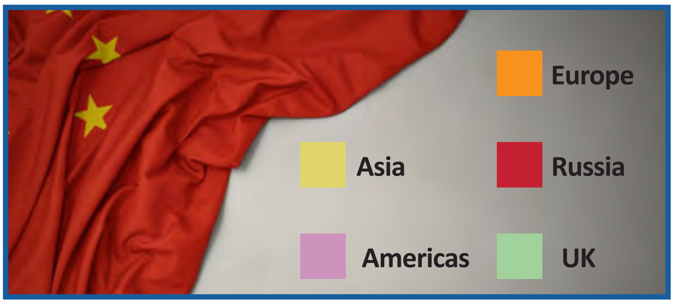
This outlook, together with the fact it is already home to some of the most exciting and innovative growth companies, means investors cannot afford to ignore it.

In this feature we will explain why China is a must for investors of all stripes. We talk about some of the companies that have helped put the nation on the investment map, and provide three great fund options that make it easy for you to take advantage of this opportunity.

THE MAKING OF CHINA

Invention, international trade success, disputes, civil unrest, wars, famine and much else makes the story of China a fascinating read. But this is not the place for a history lesson, so let's consider some basic facts that might tantalise the ordinary investor.

China's average real growth has run at more



Power shift: World's biggest economies

	1992	2008	2024*
1.	US	US	China
2.	Japan	China	US
3.	Germany	Japan	India
4.	Russia	India	Japan
5.	China	Russia	Indonesia
6.	Italy	Germany	Russia
7.	France	Brazil	Germany
8.	India	France	Brazil
9.	Brazil	UK	UK
10.	UK	Italy	France

Source: IMF, Statista *Projections, based on purchasing power parity than 9% a year since 1978, according to IMF figures, and as high as 15% in peak years. World Bank data shows that per capita income in China has increased six-fold since the turn of the millennium.

But unlike most of the UK's leading companies, which rely on overseas growth for much of their own, the majority of Chinese businesses only operate domestically. That means 1.4 billion-plus Chinese people with more disposable income than ever before buying a greater amount of made-in-China goods and services from Chinese businesses.

That's a compelling backcloth for rising revenues, soaring profits and surging share prices.

NEGATIVES TO CONSIDER

There are still challenges to overcome. The trade war with the US remains unresolved and continues to simmer, there have been marches on the streets of Hong Kong this year protesting Beijing's authoritarian rule, and growth has slowed from previous startling levels.

China has seen its share of accounting scandals, including Ruihua Certified Public Accountants, one of China's largest accounting firms. It was investigated in the summer by the country's securities regulator after a listed company it audited was found to have inflated profits by about $1.74 billion over four years, according to reports.

Despite these issues, Joe Biden becoming US president could help soothe trade tensions, and while the Covid-19 virus wreaked havoc in China earlier this year (like everywhere else), the country has been quick to recover.

'China is the factory of the world,' says Baillie Gifford fund manager Tom Slater. The shutdown of thousands of manufacturing centres in the first half of 2020 slammed the brakes on economic productivity and growth. However, China looks in a stronger position than the Western world to pick itself up following coronavirus.

In the IMF's October edition of its World Economic Outlook, China was forecast to have 1.9% GDP growth in 2020. That's its slowest rate since 1976 but also making it the only major global economy to grow in this most testing of years.

IMPRESSIVE COVID RECOVERY

The pace of China's recovery has impressed fund managers. 'China is back to normal in so many sectors,' says Dale Nicholls, who runs the **Fidelity China Special Situations (FCSS)** investment trust. Even some of the hardest hit industries, like travel, hotels and restaurants are recovering rapidly, Nicholls adds.

Investors might expect this sort of optimism from a China-focused fund manager, yet the IMF agrees. It forecasts China's growth recovery to deliver 8.2% GDP expansion in 2021. That massively outstrips the respective growth recoveries of other major economies, such as projections for the US (3.9%), Japan (2.3%), Germany (4.2%) and the UK (5.9%).

Yet local stock markets haven't always kept pace. The Shanghai

Made in China 2025 – 10 priority industries

1. **Next generation I.T.**
2. **High-end computer numerical code machine tools & robotics**
3. **Aerospace equipment**
4. **Marine engineering & high tech ships**
5. **Advanced rail transportation equipment**
6. **Agricultural machinery & equipment**
7. **Bio-medicine & high-performance medical equipment**
8. **New materials**
9. **Power equipment**
10. **Energy-saving & new energy vehicles**

Source: CLSA

Composite, China's largest and the world's fourth biggest by market value, remains well below 2008 levels even after the Covid bounce-back.

That makes China cheap compared to other major markets, on a price to earnings multiple (PE) of 16.3, according to data from macroeconomics researcher CEIC, marginally cheaper than the FTSE 100's 16.8.

The S&P 500's PE equivalent is 28.3, Nasdaq Composite 30, and even the Eurostoxx 50 trades at a hefty premium on 22.8.

BIG EARNINGS GROWTH POTENTIAL

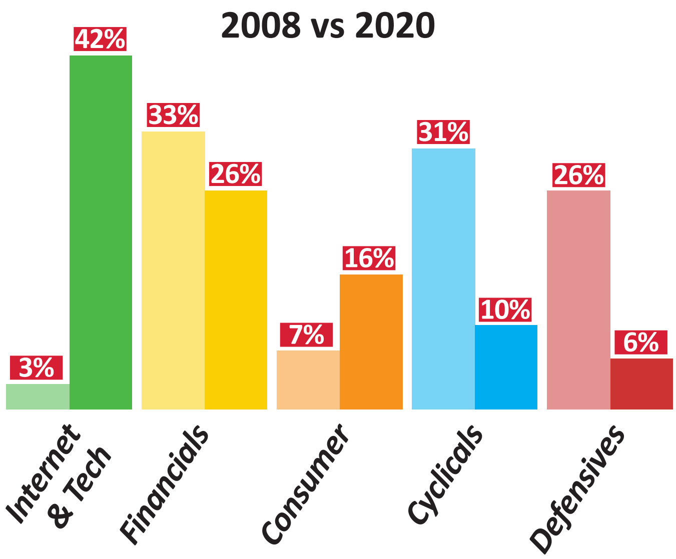
China has numerous companies which offer the potential to benefit from a rising consumer class and domestic economic activity.

What has struck Baillie Gifford's Tom Slater is the level of entrepreneurship in China. 'It is the one place creating exponential growth business opportunities comparable to Silicon Valley (in the US),' he says. Slater expects China to create more growth businesses than Silicon Valley in the future.

'On a per capita basis, China remains very much a middle-income country at this time,' says Kepler analyst Callum Stokeld. 'In my view, there is still plenty of ground to be made up on developed economies and attempts to do so will likely create huge stock opportunities.'

JPMorgan has estimated that Tencent – a Chinese technology group comparable to Facebook – can achieve annualised earnings growth of circa 22% for the coming five years.

How China's stock market has changed shape: breakdown of industries

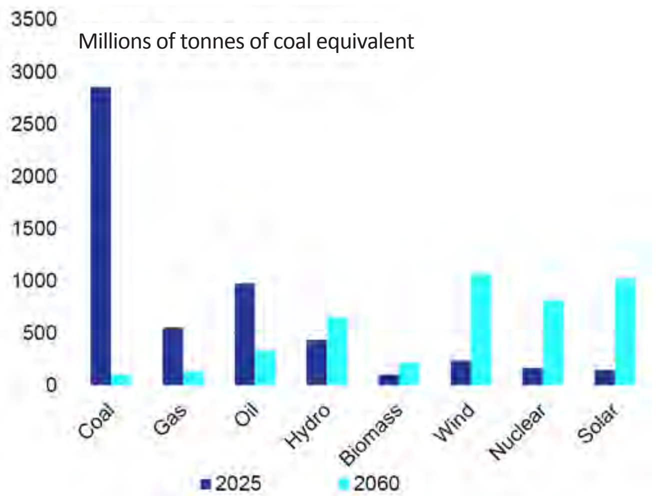


Source: UBS

Tencent and Alibaba – seen as being China's equivalent of Amazon – are hugely dominant players in the Chinese stock market, combining social networking, online shopping, gaming, streaming TV, payments and a lot of other activities, absorbing millions of Chinese people into their ecosystems.

Investors shouldn't expect these sort of growth numbers from every Chinese stock. However, with this sort of growth potential available in China on far lower valuations than equivalent US stocks, it would be 'regrettable to stand aside and not seek to participate in this single stock potential irrespective of your macroeconomic outlook,' believes Stokeld.

China's $15 trillion go-green splurge



Source: Aberdeen Standard, Bloomberg

Areas like renewable energy, artificial intelligence, e-commerce and electronic payments promise to power many of China's digital economy companies and create new stock market superstars. 'China has some of the most exciting and innovative growth companies, not just in emerging markets, but in the world,' says Sophie Earnshaw, joint manager of the **Baillie Gifford China Growth Trust (BGCG)**.

Despite these attractions, China remains incredibly under-invested as an asset class. According to Baillie Gifford's calculations, China accounts for around 18% of world market cap, 30% of listed stocks, but only 2.5% of global fund allocations. 'This is a big anomaly,' says Earnshaw. 'As the market continues to open up and China's vast potential is realised, we think this simply has to change.'

China is already 40% of emerging market indices, 50% of Asia ex-Japan, she adds. 'It's simply becoming too big to ignore and already, investors are starting to talk about China ex-EM and China ex-Asia. So, we think investors would be wise to consider allocating directly to China now to get ahead of this substantial anomaly.'

ELEPHANTS IN THE ROOM

Governance and state interference remain two major objections for investing in China, but 'stewardship laws have changed for the better,' says Chetan Sehgal, director of emerging markets at Franklin Templeton.

There remains 'a list of complex issues that are slowly being worked out,' says Baillie Gifford's Tom Slater,

but the government is 'reasserting its power to pursue what they think the population wants and needs.'

The recent stock market listing postponement of payments giant Ant Financial was a good example of Chinese regulators flexing their muscles. 'China's authorities are ensuring that it retains control over its own financial system,' states Slater.

Franklin Templeton's analysts take their time running due diligence checks on companies before investing, and then spend a lot of time with company management teams over years getting the know the nitty gritty of investee companies' culture.

'Deep engagement with management, board composition – this is the most important part of assessing companies, and building trust,' says Sehgal.

'Although China's markets have moved up a lot [since the Covid-19 crash in March], there are still many stocks that have been left behind on good valuations,' believes Fidelity's Dale Nicholls.

With bonds yields at unattractive levels, experts argue that China is as good a market for income as the US, Europe and the UK. 'There are companies on free cash flow yields in the high single-digit to low-teens,' says Sehgal.

The insurance sector is an area Nicolls likes a lot. 'This is a classic area that is underpenetrated,' he says. 'As people get richer, they'll want protection and cover, particularly in healthcare. Such growth is not in valuations.' That's why his special situations fund is overweight the sector.

Global economic normalisation, or at least continued recovery, should continue to benefit domestic economic activity in China. With growth dynamics hard to fund elsewhere, particularly from mature economies like the UK, Europe, US and Japan, fund flows into China are likely to accelerate, powering China's share prices higher.

'I think overseas investors have been historically quite gun-shy of investing in domestic Chinese equities,' says Devan Kaloo, head of global emerging markets at Aberdeen Standard. 'That has started to change.'

He firmly believes that China's listed companies are more receptive to foreign investors and now take their responsibilities to all shareholders seriously. While investing in China does come with risks, 'I think the nation's outlook is still very good,' concludes Kaloo.

"Experts argue that China is as good a market for income as the US, Europe and the UK"

THREE CHINA FUNDS TO BUY

BAILLIE GIFFORD CHINA (B39RMM8)

From the highly-rated Baillie Gifford stable, this £535 million China fund aims to find growth for the longer-term, holding stakes for at least five years.

Managers Mike Gush and Sophie Earnshaw have done an outstanding job to date, beating the performance of the Investment Association's China index over one, three and five years, returning a fraction less than 200% over the longer time frame versus 123% for the index.

The fund provides large exposure to the digital commerce/social media platforms, with large stakes in the likes of Tencent, Alibaba, delivery platform Meituan and JD.com.

FIDELITY CHINA SPECIAL SITUATIONS (FCSS)

Manager Dale Nicholls is a big fan of insurance with key holdings including Ping-An, China Pacific and China Life. He also has big stakes in Alibaba and Tencent, stocks that have helped the £1.2 billion investment trust achieve a 177% return over five years, according to Sharepad data.

The trust takes a slightly different approach to many other China funds in that it will invest in non-Chinese companies as long as they have significant exposure in the country.

The downside of the trust being so successful this year (63% return in the first 10 months of 2020) is that the shares can no longer be bought on the cheap. The stock now trades almost exactly in line with net asset value, whereas over the past 12 months they've averaged a 7.8% discount, according to Winterflood.

MATTHEWS CHINA SMALL COMPANIES (BJN4L97)

Finding little-known smaller companies in China to fuel good returns is a specialist area and one best left to professionals with on-the-ground resources rather than ordinary UK investors stock-picking themselves. Matthews China Small Companies Fund is a good solution.

Joint managers Andrew Mattock and Winnie Chwang have a built a portfolio that holds stakes in a broad mix of businesses in semiconductors, new energy, property and pet food.

The small caps expertise does come at a price, with ongoing charges of 1.5% a year for the sterling-denominated version, which launched at the start of 2020. The A class US dollar-denominated version (as featured in the accompanying chart) has a longer track record and has beaten the MSCI China NR USD benchmark by 31.5% in 2020 with a 57.1% return year to date, and outperformed the benchmark by 6.6% last year.

Emerging Markets 2020: Experience and expertise never more needed

Discover how the J.P.Morgan Emerging Market Investment Trust's experience and expertise enable it to cut through the noise and focus on the fundamentals

In the current environment an approach based on proven experience and expert analysis of the growth potential of individual stocks is essential for investing successfully in emerging markets.

To the uninitiated, emerging markets may seem a difficult area in which to invest in the second half of 2020. But despite concerns that COVID-19 fallout has slowed capital flows to emerging markets, long-term investors focusing on the right portfolio of stocks still have reasons to be positive.

Aside from the effect of the pandemic, concerns around US-China relations, falling earnings and currency weakness may be off-putting for investors, but it's important not to let the short-term noise drown out medium to longer-term thinking. A clear focus on evidence-based stock selection, targeting strong fundamentals and long-term growth potential, will continue, in our opinion, to drive gains. With veteran Lead Portfolio Manager Austin Forey and his team at the helm, the JPMorgan Emerging Markets Investment Trust continues to make the most of the long-term potential the best emerging market companies have to offer.

The changing face of Emerging Markets

If you still think of emerging markets as being about commodities, banks and property companies, then think again. While a country like China once based its economic growth model on a capital-intensive, infrastructure-driven model, the structure of emerging markets has transformed over recent years.

"People who still think about EM as a commodity-dominated asset class are very much stuck in the last decade," says Investment Specialist Emily Whiting. "These days commodities are barely touching double digits as a percentage of the Emerging Markets Index; I remember back in 2007-2008 they made up around a third of it."

"There's been a very significant change in the past 10 years towards businesses which create value without needing capital to do so," says Whiting. "One of the most interesting things about emerging markets today is that the kinds of business models that have been so successful for shareholders in the US over the last 20 or 30 years are now much more widespread in emerging markets. For example, social networks, consumer brands, software and e-commerce companies."

The JPMorgan Emerging Markets Investment Trust portfolio is notably and deliberately tilted towards these types of low capital intensity, high-growth businesses which benefit from a huge potential market.

Confidence born of experience

The Emerging Markets Trust team has a wealth of experience in the sector – in particular, Forey, who has been with the Trust since the mid-nineties and so has weathered enough storms to view current events calmly. Whiting sees that depth of specific emerging market experience as hugely important.

"If you have emerging markets as an offshoot of global equities then the minute all these analysts and portfolio managers move into EM they get absolutely shocked by double-digit declines in a day, which we're quite hardened to. Thankfully they're not too frequent but the increased volatility comes as part of the asset class."

The key as a long-term investor is having the experience to look through the market noise, to focus on fundamentals not headlines. That results in low turnover rather than the portfolio being frequently shuffled around or changed.

"There are times the market will sell down everything in a country just because of the country it's in. But if you believe that you've bought good quality businesses, if you trust their management, if they have a robust balance sheet, and if they have a superior product – then, sitting on your hands is the best course of action."

As a result, the Emerging Markets portfolio changes little, and, as far as Forey is concerned, that's a good thing. In a tumultuous year, stock turnover is in single digits, while performance remains strong, with excess returns of around 3% above the Index in the Trust's fiscal year to the end of June 2020.

Eyes and ears on the ground

With analysts and portfolio managers largely unable to travel during the pandemic, the advantage provided by the Trust's 100-strong global team is more obvious than ever. In a rapidly changing environment, the ability to access granular firsthand insight is invaluable. The Emerging Markets team collectively speak over 20 different languages, conducting around 5,000 face-to-face meetings a year in mother tongue.

However, it's not only those formal meetings which can make the difference – being immersed in the local culture can be just as valuable, as Whiting explains.

"Out of any asset class the breadth and the cultural differences across emerging markets make it so important not to just be sat behind a Bloomberg terminal looking at numbers. Having people on the ground in the likes of Shanghai and Taipei means we see first-hand the pick-up in traffic, or queues for restaurants again."

> *"Ultimately for the Trust, it's not about regions, countries or even sectors but about individual businesses.*

The weak get weaker, the strong get stronger

The Trust team is fully conscious that not all in emerging markets is rosy, with those countries having weak fundamentals to start with being weakened further by the current crisis.

"That's something we have to be aware of when we think about markets and growth rates for individual companies – it's very important to understand what the drivers are," says Forey.

However, as Whiting points out, ultimately for the Trust, it's not about regions, countries or even sectors but about individual businesses.

"More than anything, in this sort of situation the strong will get stronger," says Whiting. "If you've got companies with money behind them, with a strong balance sheet, with a clear, differentiated offering, you will do well."

Three cheap UK stocks to buy in the value rally

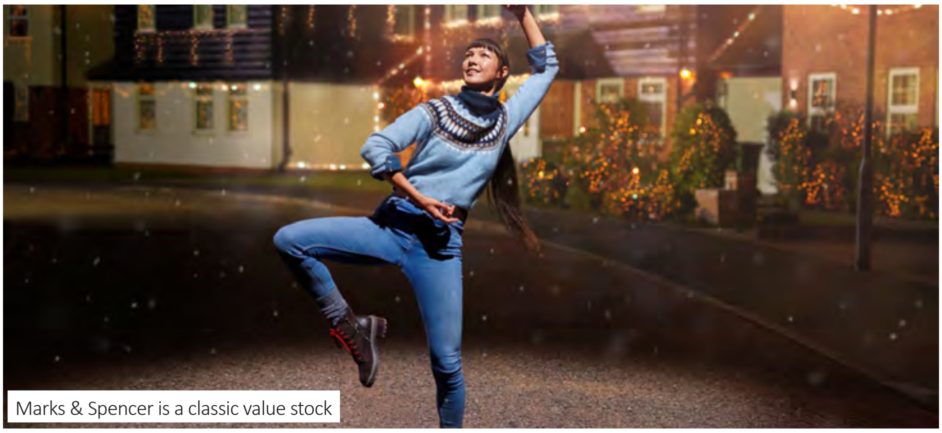
Investors are racing to own previously-beaten up stocks in the hope that a Covid vaccine will improve corporate earnings prospects

With markets jumping last month on a combination of clarity over US politics and hopes of a vaccine-led economic recovery, unloved value stocks have rallied more than most.

Many, like banks, energy and travel stocks, still face major headwinds even if their businesses are ever to return to anything resembling normal.

Meanwhile, there are a handful of stocks which are just as cheap and unloved, but which have worked hard during the pandemic to improve their businesses yet aren't feeling the same amount of love.

Here are three which we believe are worth buying as high-risk but potentially high reward trades. They are not suitable stocks for anyone who cannot afford to lose money.


Marks & Spencer is a classic value stock

CAPITA'S COMEBACK?

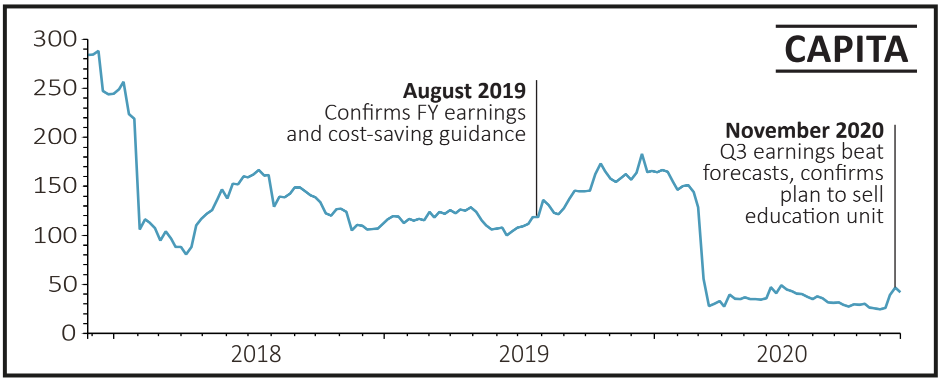
Companies don't come much more unloved than **Capita (CPI)**, whose shares are still down 70% this year and more than 90% below their 2015 highs, even though they have doubled from their October lows.

The firm's dramatic fall from grace came after repeated profit warnings due to provisions for poorly performing contracts and write-downs on assets and disposals. In retrospect, the inflated levels of accrued income and prepayments on the balance sheet should have been a warning that asset quality was deteriorating.

After a £700 million rights issue in 2018 and a thorough review of underperforming contracts, the firm has made good progress although there is still more work to do.

This year was set to be a pivotal period for Capita when it expected to see revenue growth and sustainable cash flow. Instead, the firm has had to manage its way through the crisis, although the pandemic has forced it to accelerate certain strategic decisions such as the sale of its Education Software Solutions business.

Covid is likely to continue to negatively impact revenues and transaction levels, and the inflection to sustainable cash flow generation has been delayed by one to two years,



but the firm continues to win local and central government contracts and a stronger balance sheet will improve market confidence.

It's clearly not a stock for widows and orphans but having made it through the pandemic Capita isn't going bust, yet it trades on just six times 2022 earnings forecasts. It meets the definition of a value stock and could see further share price appreciation in the coming weeks and months if value remains in fashion, but this is one for brave investors only.

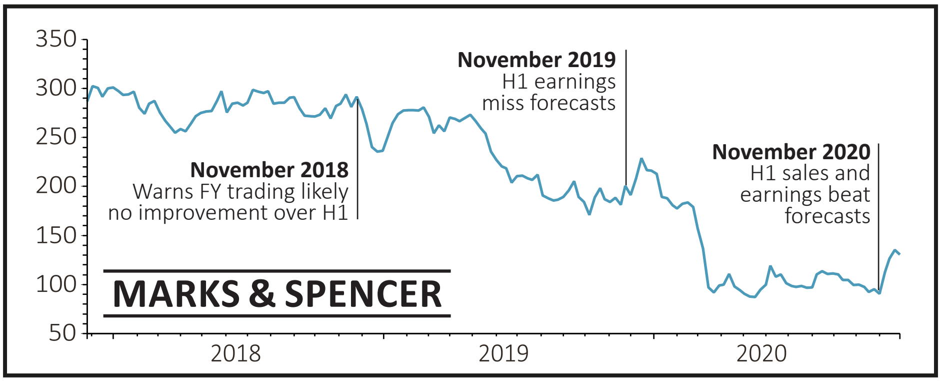
BABCOCK'S APPEAL

Engineering services and support firm **Babcock (BAB)** isn't a stock for widows and orphans either – nor will it feature on any ESG lists given its heavy reliance on UK and US defence spending. But like Capita it has had to take a hefty dose of self-help to see it though Covid.

While customer demand held up in most businesses due to the mission critical nature of its services, the civil aerospace market was predictably weak and the UK Government's decision to insource management of the Magnox and Dounreay nuclear facilities was an unexpected hindrance.

Higher health and safety costs during the pandemic impacted margins and led to a 55% drop in reported operating profits for the half to the end of September, but cost cuts and disposals allowed the firm to keep gearing around two times, out of the danger zone.

In addition, orders continued



to roll in with wins including the Dreadnought submarine programme, the Nuclear Technical Support contract at the Clyde naval base and an extension to the Met Police fleet management contract. There is also potential for growth in new markets, with the firm having received considerable overseas interest in its Type 31 frigate platform.

Shore Capital sees the first half representing the low point in performance, while further restructuring, balance sheet strengthening, and contract news should stoke investor interest. On eight times 2022 earnings, expectations seem sufficiently low to make it a worthwhile bet.

M&S LOOKS THE MOST APPEALING OF THE THREE

Finally, **Marks & Spencer (MKS)** should be on investors' shopping list. Like Capita and Babcock, its shares have popped since the news of a vaccine but considering where they were 18 months ago and given how much the business has improved, they are still a bargain.

Were it not for lockdown, earnings per share for the year to March 2020 would have been around 15% higher than reported (19p vs actual 16.7p). At the current share price of 130p, the shares are trading on less than seven times 'normal' earnings.

Analysts at Morgan Stanley and Shore Capital value M&S's 50% stake in the retail joint venture with **Ocado (OCDO)** at more than £1 billion. As Morgan Stanley points out, strip out the Ocado stake and M&S trades on four times 'normal' earnings.

As important, the pandemic has energised M&S management to deliver three years' change in one. The clothing and home division, which was shut in-store during both periods of lockdown, has grown its market share online and new head Richard Price – a former M&S man before he ran the F+F clothing brand for **Tesco (TSCO)** – is accelerating its transformation.

With shopping likely to be frantic online and in-store this Christmas, and with the possibility of life returning to 'almost normal' next year, M&S shares have significant upside potential.

By **Ian Conway**
Senior Reporter

Three funds to play a rally in US value stocks

Value is coming back into fashion with 2021 expected to see the best US economic growth since 1999

The US stock markets may be associated with big tech names that are an integral part of our lives but in 2021 it could be the historically unloved and beaten down shares that become the stars of the show.

According to Bank of America, the first three weeks of November saw the second highest inflow ever into value stocks, ahead of a new year which is set to be all about vaccines not viruses and reopening not lockdown.

It expects US GDP to rise by 4.5% in 2021, the country's best economic growth since 1999. It sees commodities, commercial real estate, small and mid-caps, and value stocks as the ones to outperform.

Fund managers at Janus Henderson also believe there will be a pronounced rotation into value stocks. Portfolio manager Jonathan Coleman believes the flow of good news on coronavirus vaccines and therapeutics will mean 'factors dominating the market like momentum and extreme growth will break down', with the reopening of the physical economy set to spark investors' increased interest in value stocks.

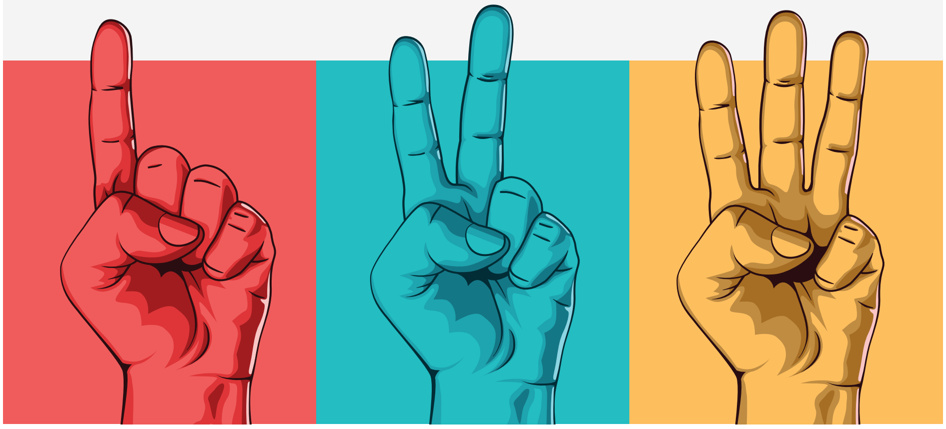
Janus Henderson all-cap growth manager Doug Rao says one sector that will benefit next year is travel and leisure.

– THREE US-FOCUSED VALUE FUNDS TO BUY –

Lyxor Russell 1000 Value ETF: Tracks a basket of value-style stocks

JP Morgan US Equity Income: Has a value tilt by investing in dividend-paying stocks

MFS Meridian US Value: Invests in companies it believes to be undervalued compared to their perceived worth



He explains: 'There's an innate need to travel, and this pent-up demand is just building up by the day. We see a prolonged period of growth ahead for the travel and leisure industry.'

'DON'T GO FULL-ON INTO VALUE'

Fund management giant BlackRock is also a fan of American stocks for 2021, expecting US equities to benefit from both structural growth trends and a potential cyclical upswing.

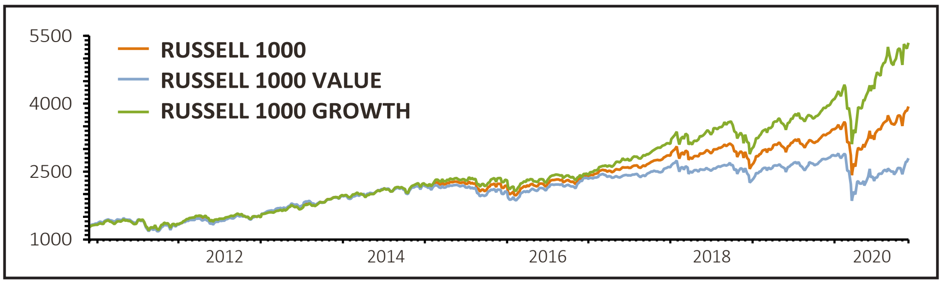
But it cautions against going full-on into value and believe this is not an either/or question between value and growth, instead advocating a barbell strategy that includes allocations on one side to quality companies benefitting from structural growth trends, and on the other to selected cyclical exposures. The asset manager says this can help achieve greater portfolio resilience amid still high levels of uncertainty about vaccine deployment.

Like the fund managers at

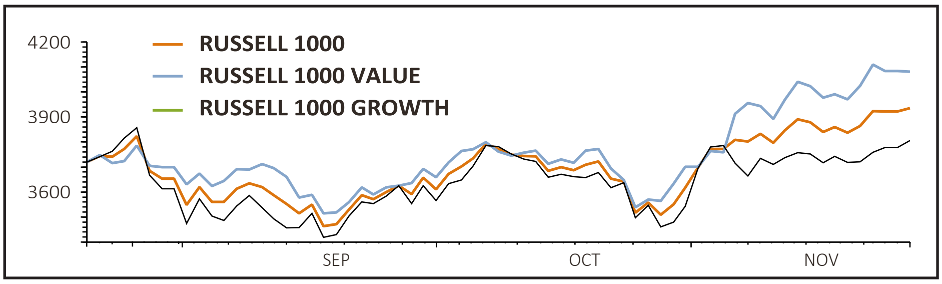
Janus Henderson, BlackRock also thinks both fiscal and monetary policy support is 'still a crucial bridge' for the stock market before the roll-out of effective vaccines.

But on this point, it cautions that the risks of policy fatigue are rising. The US Treasury's decision to end several emergency lending programmes has highlighted the risk of fading fiscal support, even though for now the action may pose only limited risks to financial stability and credit availability, and the Fed could extend lending facilities if needed. A Biden administration could be constrained in implementing its key policy plans including large fiscal spending.

The Russell 1000 Value index has lagged the normal index and the growth version over 10 years...



...But the Russell Value index has outperformed in the past month



HOW TO PLAY THE VALUE ROTATION

So how can investors play this recovery in 2021 and the rotation into value? From a fund perspective, investors could consider an exchange-traded fund which tracks a basket of value stocks.

Whenever value comes back into fashion across the pond, analysts and commentators on Wall Street typically focus on the FTSE Russell 1000 Value index, which captures the top 1,000 – and 90% of the market cap – of the FTSE Russell 3000 index.

After the Pfizer vaccine announcement on 9 November, the Russell 1000 Value index outperformed the Russell 1000 Growth index by 6%, the highest daily excess return over the past decade. The former index also captures more value stocks than oft-used MSCI USA Value Index, with 849 holdings compared to 412 for the MSCI.

To play this theme, we suggest you buy **Lyxor Russell 1000 Value ETF (RSVL)**, which has an annual ongoing cost of 0.19%. The top holdings include Warren Buffett's investment vehicle Berkshire Hathaway and consumer health products group Johnson & Johnson.

The increased diversification on offer has seen it outperform another US value ETF, the **iShares Edge MSCI USA Value (IUVF)** by 2.4% so far this year, returning -1.8% versus -4.2% for IUVF. Performance has notably been picking up in the past month as value comes back into fashion.

In actively managed space, income funds might be interesting as dividend-paying companies tend to be more in the value bracket compared to fast growing companies which typically do not pay generous dividends, if at all.

JP Morgan US Equity Income (B3FJQ59) could do well when value is in fashion, with more than a fifth of the portfolio in financials which is very much a value sector. It yields 2.5%.

There aren't many specific US-focused value funds available to UK investors, but of the select few we suggest you consider **MFS Meridian US Value (B08N668)**, which manages more than $1.5 billion of investors' money.

Value is generally seen as a long-term game with some ideas taking a long time to play out, and this is something the managers of the Meridian fund take to heart with an average holding period of seven years and a third of the portfolio held for over 10 years. The fund has still delivered a good return in the meantime, with a five-year annualised return of 11.04%. Its ongoing costs are 0.83% a year.

By **Yoosof Farah**
Reporter

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RUSS MOULD
AJ Bell Investment Director

What the dollar's decline may mean for markets

The currency has fallen 9% since Donald Trump's inauguration on 20 January 2017

It wasn't always easy to understand what US president Donald Trump wanted, but at least he was consistent about the dollar. He spent much of his four-year tenure in the White House complaining about how the greenback was too high and ultimately he got his way, even if he may have finally come around to the view in 2020 that a rising currency was a back-handed compliment from markets about the relative strength of the US economy.

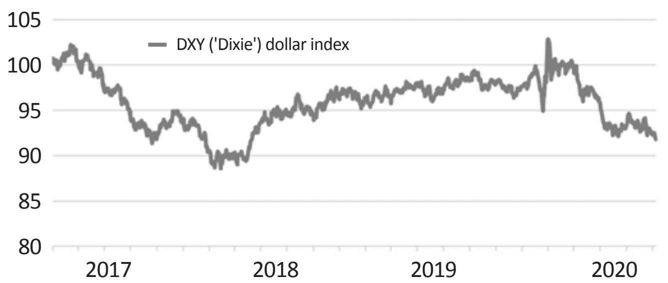
The dollar has fallen 9% since his inauguration on 20 January 2017, using the trade-weighted basket of currencies that makes up the DXY (or 'Dixie') index as a guide, and now trades at a two-and-a-half-year low.

A loss of value in the globe's reserve currency, and a major haven asset, has potential implications for a range of markets, and not just foreign exchange.

GLOOMY GREENBACK

There are multiple possible reasons for the buck's case of the blues. First, the president regularly

The US dollar weakened during the Trump Presidency



Source: Refinitiv

railed against the US Federal Reserve's monetary policy, arguing that chair Jay Powell and the Federal Open Markets Committee were running it too tight.

Whether they listened to the president, heeded stress in the financial markets in autumn 2019 or took other data on board, Powell and colleagues had begun to push through interest rate cuts even before the global pandemic pulled the rug from under the US economy in 2020.

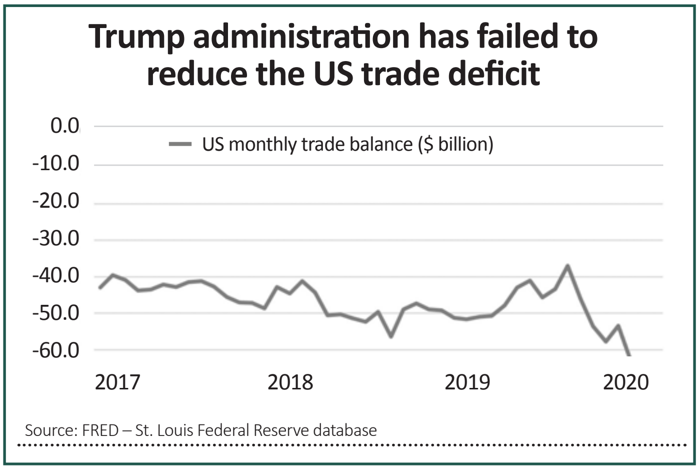
Second, the president's trade war with China unsettled markets and seemed to bring no great economic benefit. The US trade deficit has surged back toward its all-time high, with the result that dollars are flowing out of America to pay for the overseas-produced goods that consumers are sucking into the country.

In some ways this can be seen as a good sign. In 1960, economist Robert Triffin argued that America would always have to run a trade deficit, and hand out more than dollars than it received, to ensure the world had enough of the reserve currency to go around.

The alternative would be a painful liquidity squeeze on the globe's economy and financial markets alike as dollars flooded home.

Third, the markets' latest round of optimism that the pandemic may soon be over and a global

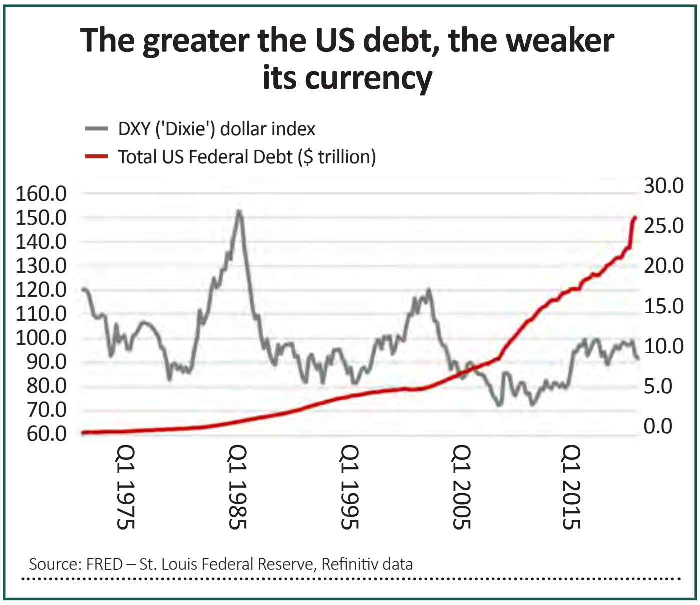
RUSS MOULD
AJ Bell Investment Director



economic recovery underway, following the vaccine announcements from Pfizer-BioNTech, Moderna, and AstraZeneca and the University of Oxford, means that perceived havens such as the dollar are less in demand.

Finally, and perhaps most fundamentally, Trump oversaw a huge increase in the Federal deficit. When he took office America's national debt was $18.9 trillion. It began to surge even before the pandemic and has soared in its wake to $27 trillion. Although Republicans and Democrats have failed to agree upon another round fiscal stimulus, the debate centres on the degree of further borrowing, not whether there should be further debt creation or not.

This argument is not unique to America –



something which may be sparing the dollar a few more blushes – but it will surely continue a trend of ever-higher government debt ceilings.

That dates to the early 1970s, when Richard Nixon took America off the gold standard so he could pay for welfare programmes and the Vietnam War, but the trend is clearly accelerating.

Remember that Moody's downgrade of America's credit rating, and summer of turmoil in financial markets, came after 2013's debt ceiling suspension, when the limit was $16.7 trillion. It had taken America 237 years to get there but Uncle Sam has taken just seven years to overspend by a further $9.3 trillion.

ROAD TO RUIN

Anyone who takes the view that American debt is not a sustainable path will be wary of the dollar.

Anyone who feels that Covid-19 can be contained, and the world builds a reliable recovery, will also fight shy of the buck. Triffin's theories imply that a weak dollar is the natural result of a strong US economy and robust global trade flows – both of which would logically benefit emerging markets and commodities, asset classes that traditionally do well when the dollar is weak.

The dollar is likely to hang tough for a while yet, not least as suitable candidates to replace it as the world's reserve currency are in short supply.

China's renminbi is not fully convertible, a return to gold will impose disciplines which no politician or central banker will accept (or can afford) and cryptocurrencies do not have universal acceptance.

But any attempt to reset currencies and debts could yet be spearheaded by central bank-backed digital currencies, a trend which must be closely watched.

Best performing open-ended funds in 2020

Outside of technology, US markets and ESG, it's been a year many investors want to forget

This year may be one that people wish to forget and instead look to next year when some sense of normality might return. However, it wasn't all bad news with a few global stock markets and investment themes notching up stellar returns.

Heightened volatility has meant that the divergence between the winners and losers has been especially wide so far in 2020, with the best almost doubling and the worst dropping by almost a third. It also means that where you have been invested has mattered a lot more than usual.

PERFORMANCE OPEN-ENDED FUNDS IN 2020

BEST PERFORMING OPEN-ENDED FUNDS IN 2020	YTD %
Baillie Gifford American Fund	106.8
BGF Next Gen Technology Fund D2	92.6
Allianz Global Artificial Intelligence Fund	87.9
Baillie Gifford Long Term Global Growth Fund	87.1
BlackRock World Technology Fund	70.9
WORTHY MENTIONS	**YTD %**
Baillie Gifford Positive Change Fund	69.8
Schroder Global Energy Transition Fund	67.5
Matthews Asia-China Small Companies Fund	58.9
LF Miton UK Smaller Companies Fund	52.0
WORST PERFORMING OPEN-ENDED FUNDS IN 2020	**YTD %**
Guinness Global Energy Fund	-34.9
Schroder Global Energy Fund	-33.1
Brown Advisory Latin American Fund	-32.3
Jupiter UK Growth Fund	-29.0
GVQ UK Focus Fund	-27.9

Source: Morningstar data at 30/11/20

KEY TRENDS

Before we look at some of the best performing open-ended funds (unit trusts and Oeics) it's worth considering some of the underlying trends prevalent this year.

After all, there isn't much merit in comparing a UK income manager, who has had to contend with a torrid headwind, with a global technology growth-oriented manager where conditions arguably couldn't have been any better.

The technology-centric Nasdaq 100 index is up 37% year-to-date and the broad S&P 500 index is up 11%. Other notable winners this year include China with the SE Composite index gaining 10% and Japan's Nikkei 225 which is 8% ahead.

All these markets are ahead of the FTSE World index which has gained just under 8%. Despite the UK's poorly perceived attractions, the FTSE AIM All-Share index is up 7.5% after recently making new all-time highs.

At the other end of the spectrum is the Russian stock market which is down 19% and the FTSE 100, losing 16% so far. Also unloved in 2020 has been the Brazilian market, down almost 8%, while most European markets are in negative territory. One exception is Denmark with the OMC25 index generating a gain of 27%.

THE TOP PERFORMING FUND

The best performing fund in 2020 is the **Baillie Gifford American Fund (0606196)** which has more than doubled, up 106.8%, and compares with growth of 31.4% for its benchmark, the Russell 100 Growth index, based on Morningstar data.

It is also the best performing

BEST PERFORMING UK SMALLER COMPANIES FUNDS

LF Miton Smaller Companies (B8JWZP2) topped the smaller companies fund category in 2020 with a return of 51.7%.

Other top performing funds were **Baillie Gifford British Smaller Companies (0593135)** at 20.6% and **ES River and Mercantile UK Equity Smaller Companies (B1DSZS0)** with 12% return.

The latter £308 million fund is significantly ahead of the benchmark over the last decade having generated an average annual return of 16.2% compared with 9.8% for the benchmark. The fund has an ongoing charge of 0.87% a year.

Top holdings include **Smart Metering Systems (SMS:AIM), Diversified Gas and Oil (DGOC)** and gaming company **Team 17 (TM17:AIM)**.

fund in the large cap equity growth category. The £5.2 billion fund doesn't pay a dividend but has a very competitive ongoing charge of 0.51% a year.

Top holdings include Tesla representing almost 8% of the fund, while Shopify, Amazon and Wayfair each have weightings around 7%, or collectively around 30% of the fund.

IN SECOND PLACE

Technology was a clear winner even before the pandemic arrived, and the enforced global lockdowns accelerated existing trends towards e-commerce, providing a huge boost for online companies and the companies providing the technology.

The $1.4 billion BlackRock-managed **BGF Next Generation Technology Fund (BG094W8)** did very well in 2020 with a gain of 92.6%.

Around half of the fund is invested in the US, with the UK making up 27% of assets and Greater Asia, comprising developed and developing Asia, representing around 17% of the fund.

The biggest holdings include Ming Yuan Cloud at 1.5% of the portfolio and Tesla representing 1.4%. Among the top 10 holdings is a position in recently listed Corsair Gaming which provides gear for gamers and content providers.

Despite opening 11% below the issue price of $17 on the first day of trading (23 September) Corsair's shares have since risen 224% to $49.

WORTHY MENTIONS

A somewhat surprising success in 2020 has been the strength of Chinese stocks which nobody was forecasting at the beginning of the year. **Matthews China Small Companies Fund (BJN4L97)** has delivered a return of 58.9%, handsomely beating the 22.6% benchmark return.

The fund is on the small side at $218 million and has relatively high running costs at 2.25% according to research group Morningstar. Top holdings include Silergy at 5.6% of the fund and Kingdee International Software also at 5.6% of assets. The top 10 holdings represent about a third of the portfolio which contains 52 holdings.

Another popular investment theme has been green and ethical investing and **Schroder Global Energy Transition Fund (BK4Q6F0)** stands out with its 67.5% return in 2020.

The $236 million fund focuses on companies that the manager believes are associated with the global transition towards lower carbon sources of energy.

Interestingly the fund has generated strong performance despite having nearly 60% of its portfolio invested inside the Eurozone and only 11% invested in the US.

Top holdings include Italian transmission system operator Terna which represents 3.6% of the portfolio, together with Danish manufacturer Vestas Wind Systems and Spanish electricity grid operator Red Electrica, both representing around 3% of the portfolio.

The fund has an ongoing annual investment charge of 0.7% a year according to Morningstar data.

WHICH FUNDS TO BUY OR AVOID?

While not impossible, it is unlikely that the Baillie Gifford American will double again in 2021. Doubling returns every year is extremely unusual. Secondly, US stock markets have looked through the deep slump in the economy. This has resulted in a stretched valuation relative to history and to other markets.

If the global economy experiences a rebound next year as many commentators expect, it more likely that markets which have lagged will play catch-up. Therefore, we wouldn't rush to put money into the Baillie Gifford fund now, although we do acknowledge its attractions on a longer-term basis.

Instead, there is another fund which has greater appeal in the current climate and that's **Janus Henderson Global Sustainable Equity (B71DPP6)**. The sustainability theme still has a long runway and this fund has an excellent and consistent long-term track record with performance ahead of the benchmark and peers. It has achieved 27.9% return this year.

The £1.2 billion fund has a medium and smaller company tilt and an overweighting in economically sensitive sectors which should benefit from global reflation. Morningstar gives the fund its highest sustainability rating.

BEST PERFORMING SMALL CAP FUNDS IN 2020	YTD %
LF Miton Smaller Companies Fund	52.0
MFM Techinvest Special Situations Fund	24.6
FP Octopus UK Micro Cap Growth Fund	20.2

BEST PERFORMING GLOBAL FUNDS IN 2020	YTD %
Baillie Gifford Long Term Global Growth Fund	87.1
Baillie Gifford Positive Change Fund	69.8
Baille Gifford Global Discovery Fund	62.6

BEST PERFORMING ASIA PACIFIC-EX JAPAN FUNDS IN 2020	YTD %
Baillie Gifford Pacific Fund	55.7
BNY Mellon-Newton Oriental Fund	49.5
Allianz Total Return Equity Asia Fund	45.9

Source: Morningstar, data at 30/11/20

BEST PERFORMING UK INCOME FUND

In the UK Equity Income category, the **LF Miton UK Multi-Cap Income Fund (B41NHD7)** was the only fund in this space to achieve a positive return in 2021, at 2.8%.

This was enough for the £768 million fund co-managed by Gervais Williams and Martin Turner to be the best performing fund in the category where the average fund performance was -15.5% year-to-date.

The portfolio has a 62% weighting in cyclicals and a big underweighting in defensive sectors which represent only 12% of the fund compared with 31% for the benchmark.

The fund's top holdings

include financial companies **CMC Markets (CMCX)**, **Randall & Quilter (RQIH: AIM)** and **Admiral (ADM)**, representing almost 10% of the portfolio in aggregate.

The fund offers a dividend yield of 4.1%, paid quarterly, and the ongoing annual charges are 0.82% according to Morningstar.

By **Martin Gamble**
Senior Reporter

Higher rate pensions tax relief could face the chop

It's an obvious target as the Government seeks ways to save money

Wealthier individuals could lose out from potential pension tax relief changes

The Government is facing a large hole in its finances, and while it's not yet acknowledging the elephant in the room, this almost certainly means tax rises in the near future.

The Conservative election manifesto rules out rises to income tax, National Insurance or VAT, which are the three big levers the Chancellor could otherwise pull. That leaves the burden falling squarely on other areas, and pensions could be one of them.

HOW DOES THE SYSTEM WORK?

The current system of pensions tax relief is costly, and favourable to higher earners. That's because when savers put money into a pension, they get a top-up from the tax man – effectively the tax they would otherwise pay if they drew that contribution as salary.

Each £100 contributed to a pension costs a basic rate taxpayer £80, a higher rate taxpayer £60, and an additional rate taxpayer £55.

The growth and income that contribution generates is free from tax while it is in the pension wrapper. This is more beneficial the more you earn.

When you come to take money from your pension, 25% is tax-free. The remaining 75% is taxed at your marginal rate of income tax. Once you have used up your £2,000 annual dividend allowance, income is taxed at 7.5% for basic rate taxpayers, 32.5% for higher rate taxpayers, and 38.1% for additional rate taxpayers.

Being taxed on some pension withdrawals isn't as bad as it sounds because many people will find themselves dropping down a tax band when they retire.

For instance, a higher rate taxpayer in working life is going to drop down to being a basic rate taxpayer unless they have a retirement income of £50,000 or more, based on current tax bands. Along with the 25% tax-free cash, it's this downhill tax gradient which makes pension contributions such an attractive proposition.

But by the same token, taking away higher rate relief on pension contributions looks pretty tempting for the Government. It would save them billions each year, and wouldn't necessarily be too much of a drag on the economy in the immediate future, because it could be implemented in a way which reduces retirement income, rather than draining expenditure in the here and now.

It would also tick the box of progressive taxation because it places the burden on the broadest, wealthiest shoulders.

MAKE THE MOST OF THE CURRENT SYSTEM NOW

For the moment, higher rate and additional rate taxpayers can enjoy the benefits of higher and additional rate relief on their pension contributions, and it is perhaps a good time to make hay while the sun is shining.

You can currently contribute up to £40,000 a year into a pension unless you are a very high earner or have already started to take pension benefits.

Within this annual allowance, there is also a limit on the level of personal contributions you can make and benefit from tax relief, which is 100% of relevant UK earnings. Broadly, this includes earned income such as salary and bonuses, but not investment income such as property.

However, you won't receive any more in higher rate tax relief than the higher rate tax you have paid in the year. The same goes for additional rate taxpayers.

For instance, if your total income is your salary of £60,000, you only pay higher rate tax on the £10,000 that sits in the higher rate tax bracket, currently starting at £50,000.

In this example, £10,000 is the maximum amount you can contribute while also getting higher rate tax relief. Contributions above this amount would still attract basic rate tax relief, usually up to the £40,000 cap. It's important to factor contributions to your workplace pension into this calculation too.

UNUSED ALLOWANCE

You might also want to use the carry forward provision, which allows you to utilise unused annual allowance from the previous three years.

Make the most of the current pension system while you can

At £40,000 a year, that's potentially an extra £120,000 you might be able to contribute on top of the £40,000 allowance for this year. It's still the case that you would only receive higher rate relief for higher rate tax you have paid in this tax year, however.

This provision therefore only makes sense for very high earners who have lots of their annual income subject to higher rate or additional rate tax.

WORRYING ABOUT NOTHING?

Now it's fair to point out that higher rate tax relief on pensions is like a cat with nine lives. There has been continuous speculation over most of the past 10 years that it's going to get the chop, but it still lives to tell the tale.

This is probably because it's such a toxic subject for politicians to address, not to mention fraught with difficulties when it comes to implementation.

That may well prove to be the case this time around, but the pandemic has placed significant pressure on government finances, and something must give.

Unlike previous administrations of the last 10 years, the current Government also has a big majority in the House of Commons to play with, which gives it greater scope to push potentially unpopular policies into legislation.

Sounding the alarm over pensions tax relief does feel a little like being the boy who cried wolf. But we should remember that at the end of that fable, the fearful canine does actually show up.

By **Laith Khalaf**
Financial Analyst

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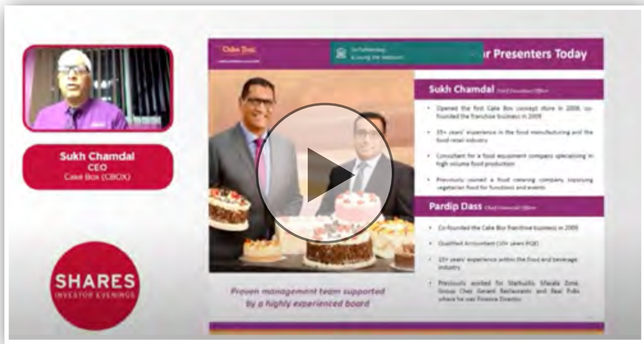

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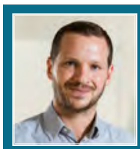
How will the Government's RPI change impact me?

Our resident expert looks at the impact of pensions tracking a different inflation index

I'm 68 and currently receive an annual defined benefit (DB) pension worth about £20,000 a year. At the moment it goes up in line with RPI inflation. Will this be affected by the Government's decision to scrap RPI from 2030?
Anna



Tom Selby
AJ Bell
Senior Analyst says:

Documents published alongside chancellor Rishi Sunak's Spending Review last week confirmed long-trailed plans to effectively replace the Retail Prices Index (RPI) inflation measure with a version of the Consumer Prices Index that includes housing costs (CPIH).

This is happening because RPI has been deemed an inappropriate measure of cost of living increases by the UK Statistics Authority. It is estimated that, on average, RPI overstates inflation by around 0.8 percentage points every year.

The change will occur from 2030 (statisticians wanted to bring it in earlier but the chancellor refused) and will impact savers and investors in a number of ways.

In your case, it is likely the RPI-linked increases in the value of your pension are written into the terms of your contract. This means that, from 2030, the value of these increases will likely be lower on average as a result.

It's probably easiest to illustrate this with an example. Take someone who has a £20,000 annual pension which is linked to RPI. Over the course of a 30-year retirement, if RPI rose by 2.8% a year they would have received a total income of £947,000.

However, if instead it rose in line with CPIH at 2%, over the same 30-year retirement they would receive a total income of roughly £828,000.

This means a simple switch from RPI to CPIH could cost someone in this position £119,000 in lost retirement income.

While lower annual increases in the value of your pension are not ideal, remember you still have a valuable guaranteed pension that is protected against inflation. It's just that up until 2030 you'll likely enjoy an annual uplift in the real value of your retirement income, whereas post-2030 your spending power will be maintained.

UK GILTS AND ANNUITIES

Investors in UK gilts, which currently rise in line with RPI, will also see the value of those investments fall from 2030.

As DB pension funds are big investors in these financial instruments, some will likely need to find extra cash in order to pay retirement incomes to their members.

Where DB members have yet to reach their scheme's retirement age and the rules promise RPI-linked increases, the value of that pension promise is likely to reduce, meaning the amount of money they might be offered to transfer out (known as the 'Cash Equivalent Transfer Value') could fall as well.

Finally, anyone who has bought an annuity – a guaranteed income for life paid by an insurance company – with RPI-linked inflation should expect to see these increases reduce from 2030 onwards.

DO YOU HAVE A QUESTION ON RETIREMENT ISSUES?

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

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

You should always study a company's shareholder base

It is worth finding out about the big investors in any of your holdings and their intentions

As a shareholder you are often one among hundreds or even thousands of individuals and institutions which also own a slice of a business.

Many of these fellow shareholders will remain faceless or nameless entities but you can uncover the identity of the major shareholders in a company and there are several good reasons for keeping tabs on them.

DISCLOSURE RULES

In the UK the identity of anyone who owns 3% or more of a listed firm needs to be disclosed. Major shareholders can be asset management firms who will likely hold their position through a specific fund, founders and directors of the business, or sometimes larger companies in the same or a related industry (who possibly have some kind of commercial arrangement with the relevant company).

Businesses will disclose a list of major shareholders on their corporate website or in their annual report. Among the key things to look for, particularly in a smaller or medium-sized company, is if there are any asset management firms whose names might add some credibility to the story.

While you will almost always see the asset manager rather than the individual fund in the list of major shareholders, you could always check if one of your favourite products from a particular stable is invested by looking at the list of top holdings on the latest factsheet.

If you trust the process and acumen of the relevant manager, this might help you with the decision of whether or not to invest, particularly when you consider they will have done some digging into the fundamentals of the business and may well have had direct access to management.

HOW CONCENTRATED IS THE SHAREHOLDER BASE?

Another thing you can uncover by looking at the list of major shareholders is how concentrated the shareholder base is or, in other words, what proportion of the issued shares are held by the largest holders.

This has several implications. It can impact the so-called 'free

Shareholders driving change

Major shareholders inevitably carry more weight with a company's management and can therefore exert pressure to effect a change in strategy, for example, or push for the sale of a part of the business which is perceived as underperforming, or hold management's feet to the fire over environmental or governance issues.

Some outfits specialise in being 'activist investors', buying stock in a company having already identified the changes they want to effect in the hope this will drive an improvement in the share price. Examples of activist investors include **Crystal Amber (CRS:AIM)** and ValueAct.

Analysing a shareholder list

Quarto's major shareholders	
Chuk Kin Lau	40.8%
Giunti / Montecristo 2019	20%
L Orbach	10%
Herald Investment Management	3.4%

Source: Refinitiv, 26 November 2020

The table shows a list of substantial shareholders in publishing firm **Quarto (QRT)**.

Former Quarto chief executive and current executive director Chuk Kin Lau is the top shareholder at 40.8%. As Quarto's registered office is in Delaware in the US, a mandatory offer under the Takeover Code wasn't triggered when Lau's holding went above 30%.

Second on the list is Italian publisher Giunti, followed by another former chief executive, Laurence Orbach.

In 2018 Orbach and Lau managed to get themselves and two other individuals elected as directors at that year's AGM without having made a proposal in advance of the meeting.

Orbach briefly served as executive chairman before stepping down. At the time their combined holdings added up to 47% of the issued share capital.

Herald Investment Management is fourth on the shareholder list, with some basic research revealing the shares are held in its **Herald Investment Trust (HRI)**.

float' which is the amount that is publicly available to trade and not restricted. If most of the shares in a company are held by a few different parties who perhaps aren't that keen to sell, then the number of shares that are freely bought or sold can be quite limited.

As an individual investor this can make it difficult to trade stocks, particularly if there is a piece of significant news like a contract win, profit warning or better-than-expected results.

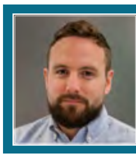
DOMINANT SHAREHOLDERS

Under the UK Takeover Code if a single shareholder moves above 29.9%, they are required to make a bid for the outstanding shares.

However, the Code only applies to listed companies with a registered office in the UK, Channel Islands or Isle of Man (as well as some incorporated in Europe). There are many firms on the London Stock Exchange to which this does not apply.

If one shareholder or group of shareholders is too dominant it can be bad news for minority holders as their interests may be neglected. Measures such as the appointment of friendly directors or even a delisting of the company could be forced through against their will.

If a dominant shareholder opts to push for a delisting it can have very negative implications for other investors. Once a firm has left the public arena, they will find little or no market for their shares.



By **Tom Sieber**
Deputy Editor

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Sean Guest, President and CEO

Valeura Energy is an upstream oil & gas company, with a clear strategy to add value for shareholders.

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Event details

Presentations to start at 18:00 GMT

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KEY ANNOUNCEMENTS OVER THE NEXT WEEK

Full year results

4 December: M&C Saatchi. **7 December:** Hardide.
8 December: Renew. **9 December:** Victrex.
10 December: Character, Marstons, On The Beach, RWS.

Half year results

4 December: Stenprop. **7 December:** IMImobile, Ted Baker, VP. **8 December:** Begbies Traynor, GB Group, SDCL Energy Efficiency Income Trust, Solid State, Vianet. **9 December:** Creightons, Duke Royalty, SDI Group, Stagecoach. **10 December:** Cohort, DS Smith, DWF.

Trading statements

8 December: Ashtead. **10 December:** Ocado.

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