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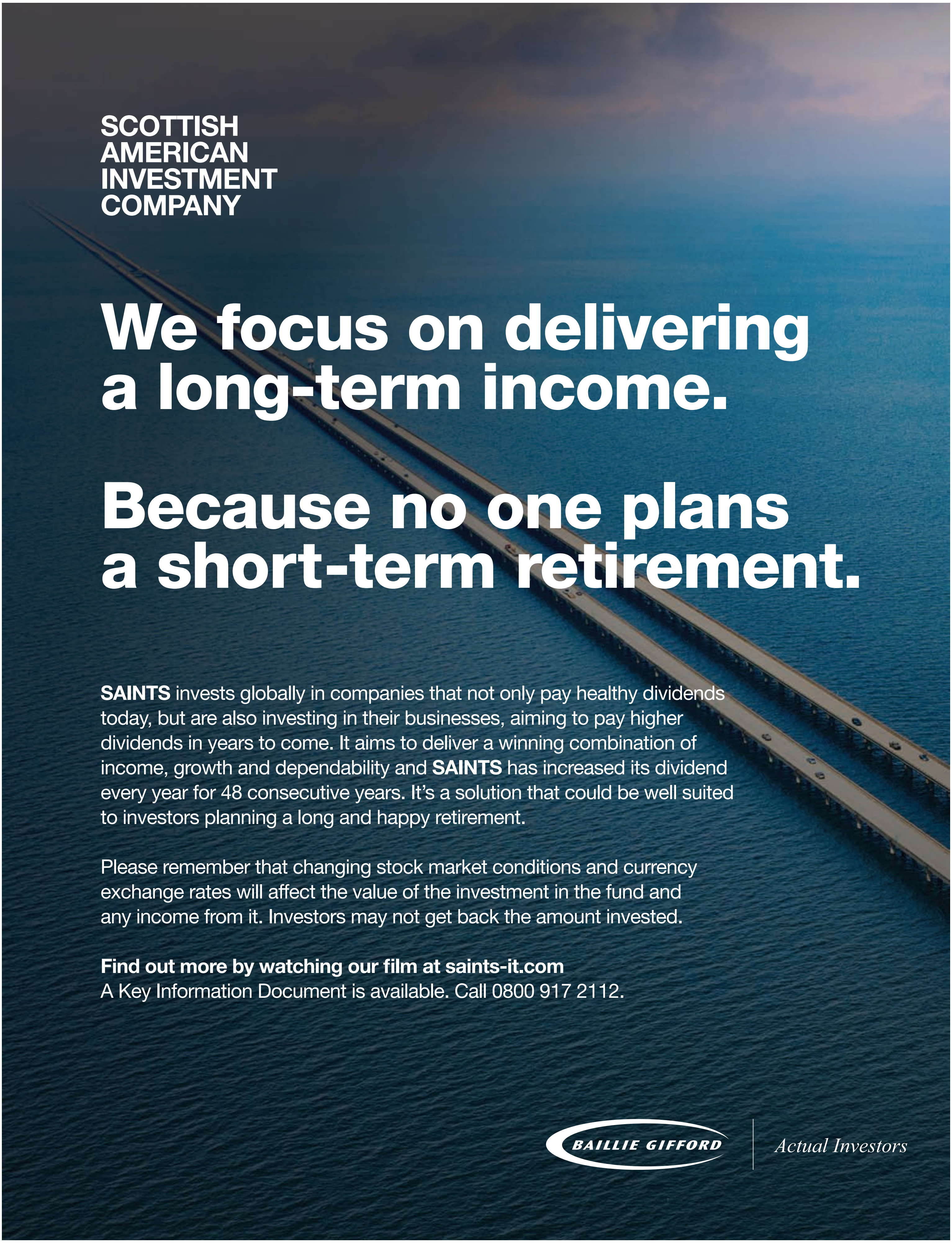
SHARES

WE MAKE INVESTING EASIER

FIGHTING CYBER ATTACKS:

Invest in the world's digital defenders

DIVIDEND GROWTH VS YIELD: The trade-off between current and future income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BAILLIE GIFFORD
Actual Investors

Contents

Retail takeovers: when is a brand worth salvaging?

Fashion name Ted Baker is attracting interest but could other names catch a bid

For all the troubles it has endured in recent years **Ted Baker (TED)** is still seen as a brand with some value based on the news US private equity firm Sycamore is weighting up a potential takeover of the clothing retailer.

Ted Baker, once something of a stock market darling, has struggled in recent times. The fall from grace started with accusations of inappropriate behaviour levelled at founder Ray Kelvin, then a series of profit warnings followed, a short-lived CEO and accounting errors only compounding things.

Margins suffered as the company responded to a competitive market with price cuts, not exactly a testament to the strength of the company's brand.

Nonetheless, the Sycamore bid interest has helped to breathe life into a depressed share price which is now up more than 40% since 15 March.

Shore Capital analyst Eleonora Dani commented: 'While undoubtedly all the attention will be on Ted shares, we see the potential for read-across to other UK lifestyle brands, **Superdry (SDRY)** and **Joules (JOUL:AIM)**.'

Dani notes that shares in both have fallen sharply despite retaining 'a varying degree of brand equity'.

'We would not be surprised if private equity firms targeted these brands, now in deep value territory.'

However, history is littered with examples with consumer brands which have disappeared without a trace despite once enjoying widespread popularity.

Think of Woolworths, bookstore Borders and Toys R Us in the past 20 years. These chains mainly sold third party products, so perhaps a better comparison for Ted Baker is American Apparel.

There are some eerie echoes of the Ted Baker story. American Apparel, known for offering brightly coloured, US-manufactured clothing, twice filed for bankruptcy in the wake of sexual harassment allegations against its founder Dov Charney, who left as CEO in 2014.

Tarnished brands

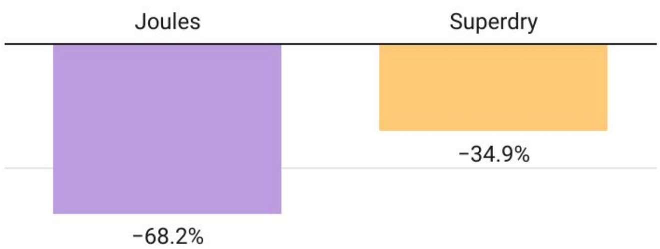


Chart: Shares Magazine • Source: Sharepad, data as at 21 March 2022 • Created with Datawrapper

Bought out of Chapter 11 by Canadian retailer Gildan Activewear for $88 million in 2017, in its current online-only guise it is a shadow of the 281-site and $634 million business it once was.

Perhaps that is where the future lies for the likes of Ted Baker, as well as Superdry and posh welly seller Joules.

At one time Superdry's faux Japanese stylings felt quite ubiquitous but tastes change and perhaps it no longer warrants a bricks and mortar presence, with its more devoted fans still able to buy its products over the internet.

Certainly, from a private equity perspective you could see the logic of getting rid of the costs associated with maintaining physical stores and just moving to an online-only model.

The great thing for individual investors looking at this space is that it is relatively easy to make your own judgement about consumer brands and whether they have staying power.

You may not always be right, but you can at least interact with the products and get your own 'literal' feel for how a lifestyle brand compares with the competition.

By **Tom Sieber** Deputy Editor

Value and inflation protection leave FTSE 100 well placed

UK markets offer stocks which have done well against rising prices

As the first quarter draws to a close most investors will be hoping for less turmoil for the remainder of 2022, with major markets sitting well below where they started the year.

For example, the S&P 500 is down around 7% while the technology driven Nasdaq 100 is off 12%, as higher interest rates take a heavy toll on growth stocks.

In Europe Germany's Dax and France's CAC 30 are both down around a tenth. These performances make the UK's blue-chip FTSE 100 index stand outs given it almost unchanged.

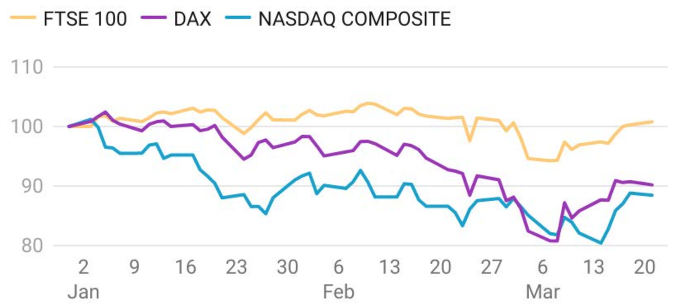
The mid-cap FTSE 250 and FTSE All-Share are down 12% and 3% respectively.

The FTSE 100 index has benefited from its high exposure to booming industrial metals prices and other commodities impacted by the invasion of Ukraine.

Rising energy and metals prices will create upward pressure on near-term inflation, possibly creating a period of stagflation (high inflation and low growth).

Research from investment bank Jefferies looked at prior periods of stagflation and the evidence showed UK inflation-linked bonds and precious metals miners outperformed the market.

FTSE 100 outperforms in 2022



Rebased to 100

Chart: Shares Magazine • Source: Refinitiv • Created with Datawrapper

The UK market is also attractive from a relative valuation perspective according to Invesco's global asset allocation team.

Having reduced equity exposure to 'neutral' in November 2021, the bank has now moved back to an 'overweight' stance.

Invesco expect the best returns to be generated by UK and Emerging market equities over the coming year and have allocated those regions 'maximum overweight'. [MGam]

Chancellor Sunak's spring statement full of surprise support measures

Cuts to National Insurance contributions and fuel duty

AT A TIME when UK households face an unprecedented squeeze on their budgets, the chancellor's targeted tax cuts will go some way to helping those on low and middle incomes.

The ceiling for National Insurance contributions has been equalised with that of personal tax at £12,570 starting from July.

That amounts to a £6 billion cut in deductions or an average of £330 more in salary per person per year, although for almost three quarters of workers the cut means more than a £330 per year uplift.

Instead of a windfall tax on big oil producers, which never looked likely, there is a 5p per litre cut in fuel duty for the next 12 months which will help those who drive.

There was no substantial help for those facing a huge jump in their home energy bills next month, however.

For small business, there will be a 50% discount on annual business rates up to £100,000 from next month and an increase in employment allowance which will undoubtedly help areas such as hospitality.

Lastly, the basic rate of income tax will be cut from 20% to 19% in 2024. [IC]

IG and Plus500 venture overseas with mixed success

Plus500 looks to Japan after IG reports a notable slowdown for US business

Trading platform **Plus500 (PLUS)** announced on March 21 that it is entering into the Japanese market. This move is motivated in part by the success its rival **IG (IGG)** has experienced in the region.

IG is on track to generate revenue of nearly £90 million per annum from its operations in Japan. This equates to approximately 20% of Plus500 full year expected 2022 revenue, and provides an indication of the size of market opportunity that the it represents.

Plus500's move into the Japanese market follows its decision in July 2021 to enter the American futures market with the $30 million acquisition of Cunningham.

However investors recently took fright at the slowdown at IG's Tastytrade, its American online brokerage platform, announced at its recent trading update on March 16.

This has rekindled concerns that IG overpaid for Tastytrade, and highlights the potentially precarious nature of overseas acquisitions.

Plus500 is entering the Japanese market through the purchase (for an undisclosed sum) of EZ Invest which is licensed as a Type 1 Financial Instruments Business Operator. Its offerings include CFDs (contract for differences), and OTC (over the counter) foreign exchange.

The rationale is to scale the business up by leveraging Plus500's technology and marketing expertise. This mirrors the strategy adopted with the group's entry into the American market last year with the acquisition of Cunningham.

The market was spooked by IG's recent management guidance that revenue growth for Tastytrade will miss the previously guided 25% to 30% revenue growth target for 2022.

IG paid $1 billion for Tastytrade in 2021

The reduced guidance for Tastytrade accompanied an otherwise positive trading update. However the market marked the shares down on the news.

At the time of the Tastytrade acquisition (it completed in June 2021) there were fears that the $1 billion price tag was excessive. However the deal was justified on the basis that the US options and futures market was the largest in the world, commanding high margins.

However US options trading volumes have slowed, a trend that has continued into the start of the fourth quarter, prompting management's cautious guidance.

The lowering of management revenue guidance for Tastytrade re-opens the debate over whether IG paid over the odds for an asset that was a transitory beneficiary of the pandemic.

With consumers forced to work from home Tastytrade benefited from the sharp uptick in individuals trading.

Now that normal activity has resumed, there is a fear that the long-term structural growth outlook for Tastytrade will be more muted than current analysts' expectations. [MGar]

Robust results from Nike as direct to consumer strategy delivers

The athletic apparel leader continues to make progress with a winning strategy

Third quarter results published on 21 March from Nike beat analysts' expectations and sent shares in the world's largest sportswear company higher in US after-hours trading.

Despite ongoing supply chain disruption, Oregon-based Nike managed to boost margins as it accelerates its shift to direct to consumer sales, which form a key plank of its growth strategy.

NIKE Direct sales were up 17% to $4.6 billion in the quarter amid further digital market share gains and a boost from 'the steady normalisation of traffic' in Nike-owned brick and mortar stores.

With customer demand for the Nike brand outpacing supply, the sneakers-to-soccer balls seller benefited from robust demand in its biggest market, North America, where it delivered 33% digital sales growth.

However, Nike also flagged short-term volatility driven by consumer inflation, stock shortages, the war in Ukraine and China lockdowns.

Sales in North America grew by 9% year-on-year in the third quarter, though Nike expects to see a decline in fourth quarter sales in the region as it faces a tough comparison with the same period 12 months ago.

Revenue was down 5% year-on-year in Greater China, where Nike is rebuilding its business after a boycott of western brands by Chinese consumers hit sales early last year.

Any worsening in relations between China and the West over the former's support for Russia could be damaging for Nike given the importance of the Chinese market. [JC]

Ferguson to leave the FTSE 100 in May as it focuses on the US

Plumbing outfit set to follows BHP's FTSE 100 exit in May this year

PLUMBING PRODUCTS FIRM **Ferguson (FERG)**, which generates 100% of its revenue in North America, is set to move its primary listing to the US after shareholders recently approved the move.

This will see the company exit the FTSE 100 on 12 May as it moves to a 'standard listing' on the UK market where it will no longer qualify for inclusion in FTSE indices.

Numis analyst Christen Hjorth says there is a 'risk of potential indigestion as the group falls out of the FTSE index'.

Ferguson follows hot on the heels of mining giant **BHP (BHP)** which moved its own main listing to Australia and departed the UK's flagship index in January 2022.

Ferguson had sold its UK operation – Wolseley – to US private equity firm Clayton, Dubilier & Rice in February 2021 so the move looks logical but its decision will further erode the depth and breadth of the FTSE 100.

Russian firms **Evraz (EVR)** and **Polymetal (POLY)** were recently deleted from the FTSE indices in response to Russia's invasion of Ukraine.

Chip designer ARM's planned listing on Nasdaq rather than making a feted return to the UK market, where it was a member of the FTSE 100 until its $31 billion takeover by current owner, Japan's Softbank, in 2016, also reflects the UK's struggle to attract and retain large businesses. [TS]

Hospitality enjoys good times despite spending pressures

Low unemployment and £300 billion of excess savings remain supportive

Leisure and hospitality shares are trading below pre-pandemic levels but arguably the underlying fundamentals have improved. Financially strong operators have taken advantage of favourable market conditions to accelerate their expansion plans.

These include Wagamama owner **Resturant Group (RTN)**, **The Gym Group (GYM:AIM)**, **Loungers (LGRS:AIM)**, and **Fulham Shore (FUL:AIM)**.

Despite lingering impacts from the Omicron variant and rising cost inflation challenges recent data suggest the sector is still benefiting from robust pent-up demand.

For example, the Coffer CGA business tracker for managed pubs and restaurants showed February's like-for-like trading 3% higher than pre-pandemic levels.

Strong recovery and a preference for experiential spending rather than buying 'things' is expected to continue to gain momentum according to research from Liberum.

This is backed up by the ONS (Office for National Statistics) based on credit card data. March spending on social activities, like going out to eat and travelling is above February 2020 levels.

By contrast spending on 'delayable goods' such as clothing, footwear and household goods is 20% below.

Lumina Intelligence forecasts the UK restaurant market to recover to 94% of 2019 trading by the end of 2022 with the top branded restaurants capturing around 20% annual growth and smaller groups facing a mixed recovery.

Liberum expects Restaurant Group and all-day restaurant and bar group Loungers to lead the market in sales recovery in the year ahead. [MGam]

Hong Kong suspends shares in Chinese property giant Evergrande

Investors brace for news from world's most heavily geared developer

SHARES IN THE world's most indebted property company and several of its subsidiaries were suspended from trading by the Hong Kong stock market regulator as the company promised a plan to deal with its borrowings by the end of July.

Evergrande, which has over $300 billion in loans and liabilities, has been in difficulty for the last year or so since it surfaced that some of its banks were no longer willing to continue extending credit.

In the last 12 months its shares have lost more than 90% of their value.

The developer, which missed interest payments on some of its domestic loans last year sparking a wave of liquidity fears across the Chinese property sector.

Given the importance of the property sector to China's economy and in particular its role as a savings tool for the country's growing middle classes, the authorities have been working overtime to ensure any default is 'orderly'.

Work on many of Evergrande's hundreds of construction projects has ground to a halt despite efforts by the firm's owner, once China's richest man, to restore confidence among investors and suppliers. [IC]

BlackRock Throgmorton is a great fund for a smaller company recovery rally

Focus on high-quality growth stocks has delivered benchmark-beating performance for years

We believe that many smaller companies have fallen too far amid the indiscriminate sell-off this year, and that there is real scope to pick up many well-run, high-quality business at knock-down prices.

One of the best ways to take advantage, in our view, is to buy the **BlackRock Throgmorton Trust (THRG)**, one of the very best smaller company investment trusts available.

This is a multi-award-winning trust with peer-beating performance over many years. In a *Shares* analysis of the smaller companies trust space in December 2021, BlackRock Throgmorton came second out of 15 trusts over 10 years on a total returns basis with 599.2%, topping the peer group over both three and five-year periods (107.7% and 240.7%).

According to the trusts' own data, it has outstripped its benchmark, the Numis Smaller Companies plus AIM (excluding Investment Companies) Index in each of the past five years on both share price and NAV (net asset value), by close on 50% last year (to 30 November 2021).

INVESTMENT DNA

Steered by manager Dan Whitestone, BlackRock Throgmorton invests primarily for long-run capital growth in small and mid-sized UK companies that are either driving innovation or benefitting from structural change. This might sound like another technology-themed fund but that's not strictly true – industrial, consumer discretionary and financials are its three largest sector exposures representing 70% of assets, with technology forth worth 8.3% of the fund, based on 31 January 2022 data.

That said, Whitestone firmly believes that financially sound, well-managed companies with differentiated products that have a tailwind of secular trends are most likely to undergo exponential growth, and it's true that embracing new technologies and online distribution methods plays a big role.

BlackRock Throgmorton's trailing returns

	1-year	3-years	5-years
Share price	12	78	153
NAV	13	67	104
Benchmark	12	37	42

Source: BlackRock, 31 January 2022 • Created with Datawrapper

Watches of Switzerland

BlackRock Throgmorton's top 10 holdings

Electrocomponents	3.5%
Gamma Communications	3.3%
Watches of Switzerland	2.9%
IntegraFin	2.9%
Oxford Instruments	2.9%
Impax Asset Management	2.6%
Auction Technology	2.5%
YouGov	2.3%
Baltic Classifieds	2.3%
Dechra Pharmaceuticals	2.3%

Table: Shares Magazine • Source: BlackRock, 31 January 2022 • Created with Datawrapper

(WOSG) is a prime example of Whitestone's approach. It is a retailer that has provided multiple strong updates with upgrades to forward guidance as it continues to benefit from the secular demand for luxury watches in a supply-constrained industry.

It has been able to achieve 'record sales and profits despite most of their stores being closed through their financial year,' said Whitestone. This was partly due to the strength of the category, but also because management have successfully navigated a difficult retailing environment by enhancing its business model through digital 'clientelling', in other words using software to enhance long-term relationships with their clients.

'We firmly believe Watches of Switzerland has emerged from Covid-19 with a significantly enhanced market position and strengthened its relationship with the luxury brands, which leaves the company well placed to pursue its international expansion ambitions,' said Whitestone in BlackRock Throgmorton's full year results, released on 7 February 2022.

Other notable contributors to the trust's performance last year included **Tatton Asset Management (TAM:AIM)**, **YouGov (YOU:AIM)**, **Auction Technology (ATG)**, and IMIMobile, a the marketing and communications platform business which soared after the company agreed to a 595p per share takeover from US listed IT giant Cisco Systems, marking a five-fold increase in value since its initial public offering in 2014.

As discussed earlier, this is exactly the type of medium to longer-term investment opportunity that BlackRock Throgmorton strives to spot early, and it is a strategy that continues to deliver in spades for investors.

Stakes in **Games Workshop (GAW)** and **Avon Protection (AVON)** dragged on performance yet with 120-odd stocks in the portfolio, there is plenty of diversification.

TOOLS TO MAXIMISE RETURNS

Uniquely for a smaller companies trust, BlackRock Throgmorton also uses short positions in stocks to bet against firms that Whitestone believes are in a weak position. The short book provides a separate avenue for the manager to add value through stock selection skills, while the trust will also use gearing to maximise strong markets and limited downside during sticky patches.

Gearing (how much the trust has borrowed to invest) currently stands at 24% of net assets, demonstrating Whitestone's firm belief that there is widespread value available in today's stock markets.

BlackRock Throgmorton typically trades at a premium to net assets, such is its outstanding returns performance. Yet that premium has been whittled down to just 0.11%, as of 18 March 2022, below the 12 months 0.94% average, based on BlackRock data.

It's worth noting that the trust's fee structure is heavily skewed towards performance rather than the fixed management fees. The fixed ongoing charge stand of 0.6% a year, with performance fees only levied on outperformance of its benchmark. Last year annual fees were 1.38% versus 1.6% in 2020.

This means we would anticipate Whitestone continuing to use high levels of gross market exposure, shorting and to maintain conviction in his high-quality growth-led approach. That may not make the trust suitable for all investors, but those looking to take advantage of the deep smaller company sell-off, this is one of the very best options available. [SF]

BlackRock Throgmorton Trust

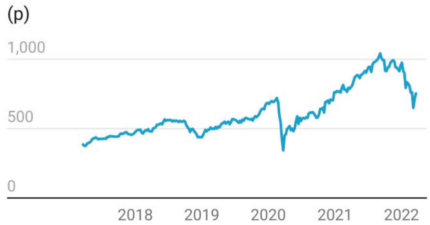
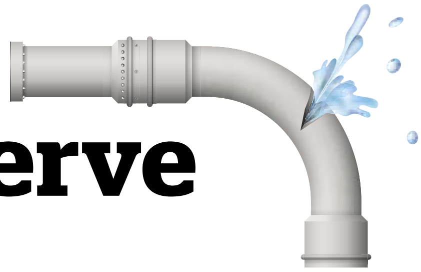


Chart: Shares Magazine • Source: Refinitiv • Created with Datawrapper

US growth can drive undervalued Homeserve shares higher



Concerns over the mature nature of the UK business have been overdone and robust growth across the Atlantic is likely to prompt investors to revisit the stock

Shares in business services group **HomeServe (HSV)** have been oversold on concerns surrounding the growth prospects in the UK.

However the star performer is the US business, and management has indicated that it is currently ahead of schedule in achieving its medium-term target of $230 million of earnings before interest and tax from this region.

And while the domestic operation has been losing customers, this should start to bottom out as it works with water partners to enhance its product offering.

All in all the shares offer good value at current levels. The current squeeze on consumers' finances caused by rampant fuel and food price inflation is likely to encourage more people to take out policies in order to avoid large repair bills.

The share price has fallen by 31% over last six months, which explains why the stock is trading on 2022 price earnings of 13 times, falling to a price earnings multiple of 12.1 times for 2023.

The 5 April pre-close trading update is likely to act as a catalyst for the shares.

Homeserve has two business lines. It sells homeowners insurance against unexpected plumbing, heating or electrical emergencies. This model works by selling these products through partnerships with utility companies, and has expanded from the UK into France, North America and Spain.

It also provides qualified tradespeople to sort things out if there's a problem. Homeserve also runs the Checkatrade platform, charging tradespeople to advertise.

The share price weakness largely relates to concerns surrounding the UK business which has been hampered by a series of setbacks.

In 2021 it took an £85 million provision to write off its customer relationship management platform, which was no longer fit for purpose, hammering earnings.

The UK business is mature and customer numbers fell to 1.6 million at the end of 2021. However broker Liberum anticipates that it will trough shortly at 1.5 million customers.

Management are confident in the group's ability to increase the number of US customers from the first half 2022 level of 4.8 million to a *Milestone 2* target of six million to seven million.

According to Liberum double that figure is achievable long term.

HOMESERVE
BUY
(HSV) 675p

Market cap: : **£2.26 billion.**

Assuming that 30% of the market is insurance minded and that there are 151 million households in the US, the addressable opportunity is 45 million households

If HomeServe maintains its share it should be able to increase the number of customers from 4.7 million to 14 million.

There are a number of reasons to believe these projections are achievable.

HomeServe has a proven operating model, a strong balance sheet and is targeting the acquisition of 28 utility books. It also has 72 million affinity partner households in the US. [MGar]

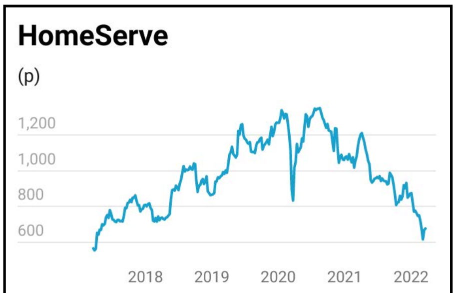


Chart: Shares Magazine • Source: Refinitiv • Created with Datawrapper

FDM

(FDM) £10.02

Loss to date: 15.7%

Original entry point:

Buy at £11.88, 20 January 2022

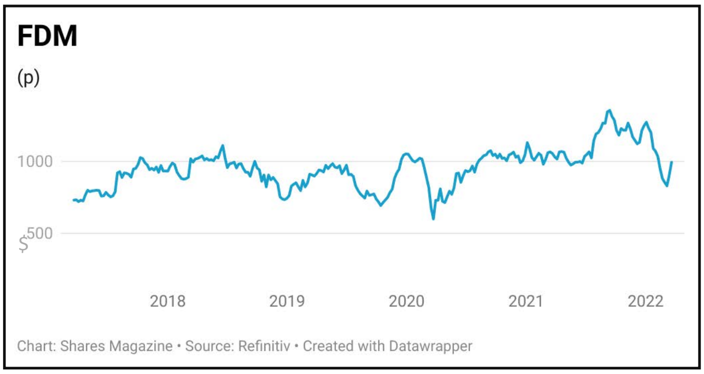
A CLEAR EXAMPLE of how some share prices have become detached from the fundamentals, **FDM (FDM)** is making the most of its ability to plug IT skills shortages, as we said it could. Results for full year 2021 saw the company's adjusted operating profits rise 11% to £47.3 million on stable revenues of £267 million, although surpassing expectations of analysts on the latter metric.

The share price had lost 35% in 2022 before the recent sharp rally.

Investors should also note strong utilisation of its IT consultants, or 'Mounties', at 97.3% versus 94.8% in 2020, while 78 new client wins (up from 52 year-on-year) augurs well for 2022 results. Stifel also notes that 2,410 new consultants completed training in 2021, 80% up on the year before at setting a new company record.

Many of those new consultants will get dropped into FDM's largely financial services customers who are clearly investing heavily in digital transformation and security, the latter driven in part by the elevated security risks that have emerged as part of the Ukraine conflict.

Analysts are forecasting around £50 million adjusted pre-tax profit this year (£46.7 million 2021), rising to around £56 million in 2023.



SHARES SAYS:

A reliably high-quality business perfectly placed, FDM shares remain a firm buy. [SF]

BERKSHIRE HATHAWAY

$352.50

Gain to date: 10.2%

Original entry point:

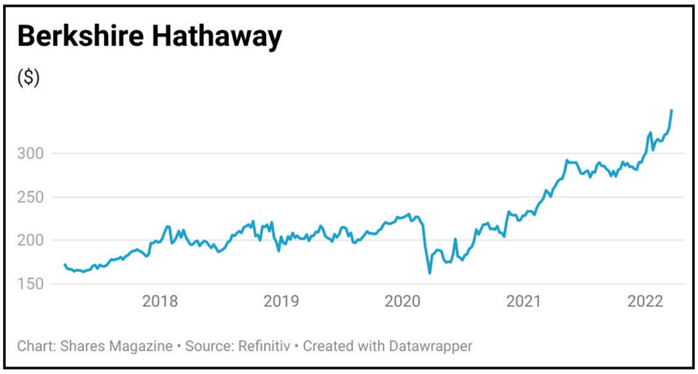
Buy at $320, 17 February 2022

OUR BULLISH CALL on Warren Buffett-run Berkshire Hathaway is paying off handsomely, with the trade 10.2% in the money as the B shares test new highs. Berkshire Hathaway has been bid up during the recent market turmoil with rattled investors keen to access its diverse portfolio of financially strong and market leading businesses.

The market responded positively to news (21 Mar) of the $11.6 billion purchase of insurance company Alleghany Corporation. This is Berkshire's biggest acquisition in almost seven years and we are pleased to see the multinational conglomerate deploying some of its enormous cash pile.

A business run by CEO Joseph Brandon, a long-time friend of Buffett's, Alleghany will be added to Berkshire Hathway's portfolio of insurance brands that includes GEICO and General Re.

As outlined in our original thesis, Berkshire Hathaway is a great vehicle for achieving a ready-made exposure to a diverse group of some of the best companies in the US and increasingly, elsewhere in the world, in sectors spanning railroads, confectionery, home furnishings, house building, insurance and energy.



SHARES SAYS:

Still a sound defensive option for investors. [JC]

ESSENTRA
(ESNT) 310p

Gain to date: 0%
Original entry point:
Buy at 310p, 11 November 2021

THE KEY FOCUS for the market when **Essentra (ESNT)** reported full year results (18 Mar) was management confirmation on the timescales for the strategic exit from both its packaging and filters arms.

In October 2021 Essentra announced that both divisions would undergo a strategic review and be divested in the second quarter of 2022, at the earliest.

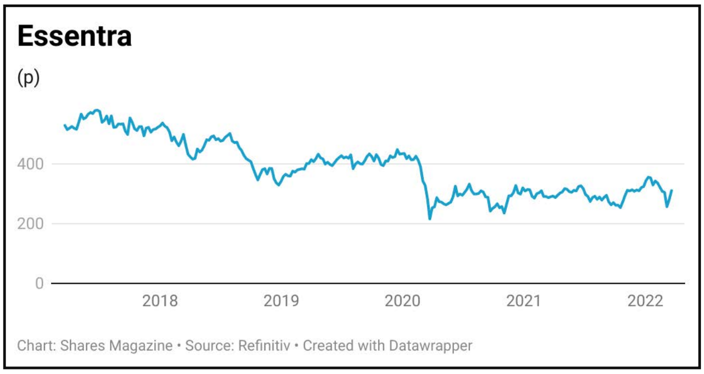
Essentra's packaging business has been successfully turned around and now offers a focused proposition in secondary healthcare packaging. It will be an attractive asset to many potential buyers.

However, Essentra filters is a more difficult sell. If no cash buyer is found, Essentra will try to combine it with a competitor or spin it off.

Following the disposals, Essentra will become a standalone components business.

The components peer group which includes companies like **Electrocomponents (ECM)**, and **Diploma (DPLM)**, trade at a clear premium to Essentra.

Indeed, the peer group trades on an average enterprise value/earning before interest, tax depreciation and amortisation of 14.4 times. This compares with Essentra that trades on a comparable multiple of around seven times.



SHARES SAYS: ↗
Keep buying. [MGar]

CORDIANT GLOBAL INFRASTRUCTURE
(CORD) 106.6p

Gain to date: 1.5%
Original entry point:
Buy at 105p, 13 May 2021

IN ITS LATEST update specialist investor in mid-market data-centres, mobile communications, and fibre optic networks **Cordiant Global Infrastructure (CORD)** confirmed it has no exposure to Ukraine, Russia or Belarus.

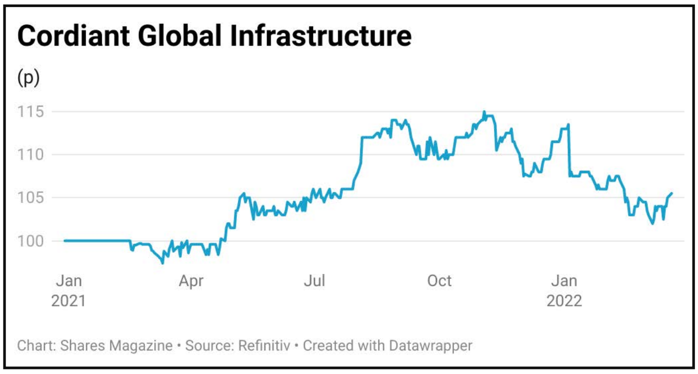
The £352 million acquisition of Polish of multi-asset digital infrastructure company Emitel announced in January 2022 has received anti-trust approval from the authorities.

This marks an important step in the multi-stage government and regulatory process. Since the invasion of Ukraine, the Polish zlotty has seen elevated volatility.

The company has responded accordingly and is implementing a prudent currency risk management strategy. On completion Emitel will represent half of the trust's assets.

Cordiant Digital's pipeline of acquisition opportunities has grown to more than €3 billion. To facilitate the pipeline the company is in discussions with lenders to secure structured finance.

Geographically, targets are split evenly between North America and western Europe which will provide more balance and welcome diversification.



SHARES SAYS: ↗
The shares remain a buy. [MGam]

FIGHTING CYBER ATTACKS:

Invest in the world's digital defenders

By **Steven Frazer** News Editor

In 1983's War Games, a young Matthew Broderick unwittingly hacks into military central computer while searching for video games and almost inadvertently starts World War III. While the prospect of cybercriminals and cyberterrorism can make thrilling TV and films, the real life threat is far more worrying, and for many, scary.

About a week before Russian troops invaded Ukrainian territory, the first Russian cyber attack of the Russian/Ukraine conflict was launched. Called NotPetya, it attacked around 70 Ukrainian government sites, among them the National Security and Defence Council.

'Analysis of the NotPetya suggests that it likely targeted Ukraine using a piece of tax preparation software as the initial vector for infecting businesses operating there,' said Tom Record and Tom Morris, co-managers of the **Majedie Global Equity Fund (BN31TC5)**.

Though the attacks have not yet caused major damage, experts in the cybersecurity world know very well what Russian capabilities are. In June 2017, the Ukrainian government announced that a virus had penetrated ministry computers and caused them to stop working. All the signs pointed to Russia.

That virus was the forerunner to NotPetya, simply called Petya, and it was used to attack the postal service, the system for monitoring radiation at the Chernobyl nuclear plant, banks, and the country's largest telephone company.

In the US president Biden recently warned (21 Mar) that US businesses need to be prepared for Russian cyber attacks. For investors, where there is fear there tend to be opportunities and cybersecurity is an investment niche jam-packed with potential for years to come. In this feature we will try to explain how big this investment space already is, why cyber crime and warfare will become an increasingly dangerous threat, look at some of the key industry stocks, and offer several options for investors wanting to position their portfolios to take advantage of the vast value creation potential.

Growth and returns of key cybersecurity players

	5-year annual growth average	5-year annual return average
Fortinet	21%	54%
Check Point Software	5%	7%
Palo Alto Networks	25%	38%
NortonLifelock	-7%	6%
Trend Micro	7%	10%
CrowdStrike	94%	N/A
Okta	52%	N/A
Mimecast	30%	31%
Zscaler	53%	*48%
CyberArk	18%	20%
Rapid7	28%	48%
Darktrace	*53%	N/A
Avast	*31%	*26%

** = less than five years, since listing on the stock market*

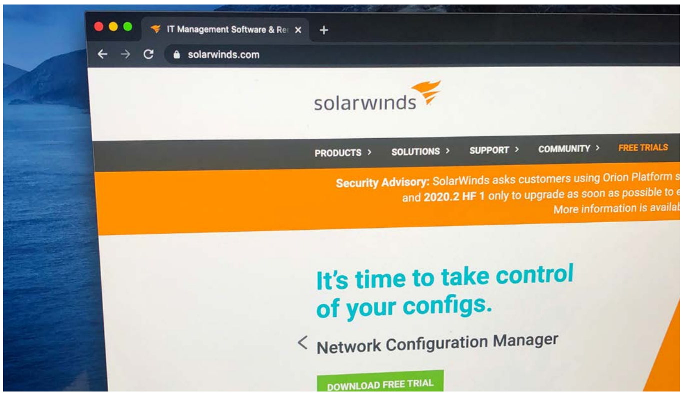
Table: Shares Magazine • Source: Morningstar • Created with Datawrapper

CYBERSECURITY LANDSCAPE

Many UK investors will have read of **Darktrace (DARK)**, emerging as one of the world's most innovative cybersecurity companies, or **Avast (AVST)** a consumer anti-virus kit supplier in the process of being bought by US peer NortonLifelock. The UK's Sophos will also be a fairly familiar name, listed in the UK until its 2020 take private deal.

Yet these UK cybersecurity firms are dwarfed by the largely US-based industry giants. If you know something of Check Point Software, Palo Alto Networks, Fortinet, Trend Micro and CrowdStrike you may be in the minority, yet these are among the global leaders in the cybersecurity industry, while the likes of Okta, Mimecast, Zscaler, CyberArk and Rapid7 are fast establishing themselves.

For reference, Fortinet was the biggest single



contributor to the performance of **Smithson's (SSON)** 18.9% net asset growth in 2021. Specialising in firewall appliances and security software, the shares have been strong ever since the SolarWinds hacking attack was discovered in December 2020, after which many corporate technology departments made clear their intention to increase spending on cybersecurity.

'This has been reflected in the growth of

Fortinet's revenue, which at 33% in the last reported quarter, was the fastest since 2016, and has resulted in the share price increasing by more than 140% during the year,' said the investment trust's manager Simon Barnard.

Okta, Crowdstrike and Zscaler are holdings in the **Allianz Technology Trust (ATT)**, one of the UK's most popular tech funds with informed retail investors.

WHY CYBERSECURITY IS GROWING FAST

The creation of the internet has removed borders, has globalised businesses, moved experiences and assets from the physical to the virtual world and underwritten massive growth in productivity.

But it has also brought the unwelcome rise of cyber crime, a multi-billion-dollar industry that impacts individuals, companies and institutions. The growth of cybercrime activity and adjacent cybersecurity investment over the last few decades was already substantial, but a post-Covid world puts the digital market front and centre.

'The Covid-induced remote working trend and related spikes in internet traffic have materially increased the cyber-attack surface,' say analysts at Canaccord Genuity.

According to data compiled by Statista, about $9.52 billion of revenue will be generated by the UK cybersecurity market this year, rising to $13.58 billion by 2026, implying 9.3% compound annual growth. Yet this is relatively small beer compared to the US.

Across the pond the cybersecurity market was valued at $156.5 billion in 2019, with more than half of the money spent on services, the rest from supplying unique software solutions and increasingly clever hardware.

By 2027, however, the US cybersecurity market is expected to growth to $326.4 billion, according to forecasts by Grand View Research, representing a compound annual growth rate of 10%.

Cyber attacks come in many forms, from thefts to ransomware to pure destruction, a nightmare for victims at the time, incidents can also be wake-up calls for companies to really get on top of their IT systems.

Yet this is a fast-moving landscape where new threats emerge a quickly as the industry can plug gaps, meaning that new cyber exploit are always just around the corner. 'Threats have become even more complex, and companies and governments have had to significantly step up their defence efforts,' say Majedie Global Equity's Record and Morris.

'In our view most are still not doing enough, with human nature partly to blame - people tend to overvalue the physical world and undervalue the virtual one, even though the distinction between the two is getting blurrier by the day.'

Illustrating their point, in 2017 Danish shipping giant Maersk saw most of its IT systems completely shut down at the hands of the NotPetya attack, a piece of malware (the catchier name for malicious software) named after a satellite in the James Bond film Goldeneye. 'Employees were locked out of 49,000 laptops, 1,200 of the company's global applications were inaccessible, and more than half of its servers were inoperable,' explain Record and Morris of Majedie Global Equity.

The cyber attack also hit communications, including phones and email, severely hampering any kind of coordinated response. Maersk's head

Most businesses today have more intangible assets like brands and databases than tangible assets such as plant and machinery.

of technology summed it up as '100% destruction of anything based on Microsoft that was attached to the network.'

The incident forced Maersk to rethink its whole approach to IT and prompted it to invest in more efficient and secure systems. The company made an astonishing recovery from the assault and shared everything it learned as it went along with all the other companies who had been affected, including **WPP (WPP)**, **Reckitt Benckiser (RB.)** and Mondelez.

Even the most sophisticated software tools may not be able to eliminate all vulnerabilities but they can hobble the hackers and choke many threats, helping to protect against the worst outcomes.

'We expect the cat-and-mouse game between organisations, consumers and the cybercriminals who covet their data to intensify this year,' say analysts at Global X, a New York-based thematic ETF provider.

'The latest concern is a vulnerability in internet software known as Log4j that could jeopardise hundreds of millions of systems globally,' say Global X analysts Pedro Palandrani and Alec Lucas. This threat follows multiple high-profile breaches in 2021, including the ransomware attack that compromised Colonial Pipeline's fuel distribution across the eastern US.

Ransomware is a type of virus that freezes IT systems, with the hackers demanding cash (a ransom) to unlock the virtual handcuffs.

Cyber events like these continue to grow more frequent and costly, especially attacks on critical infrastructure and supply chains, and the threat will only get more acute as the global economy continues to digitalise and put sensitive data at risk.

'As a result, we expect heightened awareness of and expenditure on cybersecurity solutions to create long-term tailwinds for the cybersecurity investment theme,' say Palandrani and Lucas.

By Gartner's estimate, spending on data protection and risk management could increase 11% from 2021 to $172 billion this year.

President Biden earmarked an extra $1.7 billion of spending to modernise federal cybersecurity capabilities, standardize response strategies to cyberattacks, and increase information sharing requirements for government contractors. This could rise to $7 billion of additional investment to improve the country's cybersecurity infrastructure.

'In our view, recent financial commitments to thwart cybercriminals can form tailwinds for cybersecurity companies in 2022 and strengthen the long-term investment case for the cybersecurity theme overall,' conclude Global X's Palandrani and Lucas.

HOW INVESTORS CAN GET IN ON THE THEME

Cybersecurity is a booming industry with hundreds of companies scrambling to protect us from having intellectual property, health records, financial information, and other vital data compromised.

Among the companies that are benefiting from the surge in cybersecurity spending include those building firewalls, secure servers, routers, antivirus software, and malware detection tools. Firms that specialize in consulting and solving related security problems are also getting plenty of interest.

Beyond these fast-growing areas, cybersecurity companies are increasingly looking at consolidation. Typically, cybersecurity providers specialise in specific verticals, forcing customers to secure their data using a patchwork of different providers.

As Allianz Technology's manager Walter Price points out, this offers organisations a 'layered defence' that helps offset the risk that a weakness is discovered to be exploited in any one software provider or tool kit.

That said, prominent cybersecurity providers remain engaged in a strategy of vertical integration, and often the fastest way to expand products and expertise is to buy a peer.

Noteworthy activity in 2021, for example, included CrowdStrike's $352 million acquisition of Humio, and Rapid7's $335 million acquisition of IntSights, allowing the companies involved to field more integrated product offerings.

Portfolio split

Microsoft	
Amazon	
UPS	
Zoom	
Apple	

Source: Microsoft

This is also a hot area for the big Cloud providers. In early March 2022 Alphabet made a massive move into the cybersecurity space after agreeing a $5.4 billion deal to buy Nasdaq-listed specialist Mandiant Security, beating out Microsoft in a hotly contested battle, according to analysts.

It will make Google Security a clear number two against Microsoft's Azure Sentinel, according to Megabuyte analysts. 'This is a clear shot across the bow from Alphabet to Microsoft which has, with its Azure Sentinel offering, dominated the hyperscale Cloud security space for several years now,' said Indraneel Arampatta of Megabuyte.

'The deal illustrates the importance of cyber security and the price that you have to pay for it,' said Stifel analyst George O'Connor. Alphabet is paying 8.2-times Mandiant's expected sales this year.

This surge in consolidation activity is likely to continue in 2022 and beyond.

Picking individual stocks is one option for investors but funds are also a great way into the space. The UK market is blessed with cybersecurity-themed ETFs.

Curated by experienced and proven investment teams, these thematic portfolios offer exposure to a broad range of developers and companies invested in cybersecurity, providing investors with easy and relatively inexpensive ways to access 30, 40 and often more leading cybersecurity names in a single fund, so you can benefit from both takeover targets and the industry consolidators.

Among the UK-listed cybersecurity ETFs are **Global X Cybersecurity (BUG)** and **L&G Cyber Security (ISPY)**. The former has an ongoing charge of 0.5% and the latter 0.75%. Relatively high for ETFs, which reflects their higher complexity and niche focus. Both offer exposure to all the big US names in the space. A cheaper option is **iShares Digital Security (LOCK)** which has an ongoing charge of 0.4% and tracks a similar basket of names.

Disclaimer: The author Steven Frazer has investments in Smithson and Allianz Technology Trust referenced in this article.

London-listed cybersecurity ETFs

	Ongoing charge
First Trust Nasdaq Cybersecurity UCITS ETF	0.60%
Global X Cybersecurity UCITS ETF	0.50%
iShares Digital Security UCITS ETF	0.40%
L&G Cyber Security UCITS ETF	0.69%
Rize Cybersecurity Data Privacy ETF	0.45%
WisdomTree Cybersecurity UCITS ETF	0.45%

Table: Shares Magazine • Source: Morningstar • Created with Datawrapper

A trust for all seasons

MAVT has performed well under duress, will it do the same with some tailwinds working in its favour?

Listen in on any conversation between investors, professional or amateur, and the odds are the unending debate between ‘value’ and ‘growth’ will at some point crop up. In some ways it can feel a bit pointless.

That’s because for much of the past decade the growth crowd have been able to laud it over their value rivals. Buying stocks at high valuations, on the basis that future cash flows will justify doing so, has proven a solid strategy for much of the post-financial crisis era.

And yet as we entered the new year, all this unbridled optimism came crashing down. Whether it was fears of inflation, a belief that fundamentals had started to lag too far behind share prices, or conflict in Europe, many highly valued growth stocks saw dramatic falls in price.

In contrast, value stocks have been relatively stable or even seen some gains. Looking back at the 12 months up until the end of February, the MSCI World Value Index increased in value by 19.1% on a total return basis. The MSCI World Growth Index increased by just 11.2% over the same period.

The end of the growth boom?

It’s still early days and the world is feeling even more unpredictable than it normally is, but there are some signs the reversal into value stocks may be more permanent than growth investors are hoping for.

Inflation appears to be the primary driver. Higher prices do not seem as transitory as they did two years ago, when central banks began churning out vast sums of cash to keep economies afloat. Any subsequent rise in interest rates looks likely to squeeze some of the eye-watering multiples that many stocks have been trading at.

Having said all of this, it’s worth keeping in mind that even if value investors may not have been the star performers of the 2010s, they weren’t always poor performers either. In fact, plenty of value-oriented investment trusts still delivered the goods for shareholders.

Momentum Multi-Asset Value Trust (MAVT) is one example of this. The trust’s objective is to deliver a total return that’s equal to the consumer price index plus 6%. It also seeks to pay a rising dividend that increases in line with inflation.

As its name suggests, the trust invests across different asset classes and geographies. As at 18 March 2022, a little over half the portfolio is in equities, with about 33% in UK companies and another 21% in European stocks. Specialist assets comprise a bit more than a third of the portfolio and the remainder is made up of cash, credit and defensive assets.

The trust has usually met its objective over the past decade. In the ten years up until 03/03/2022, the trust’s shares delivered a compound annual growth rate of 9.83% on a total return basis. Given its focus on value and skew towards the UK, which has also seen serious underperformance since Brexit, this is arguably even more impressive than it otherwise would be.

Headwinds to tailwinds?

The trust’s managers were able to deliver those results, and not fall off the track as some other value funds have, because of the approach they take to the market.

Fund manager Gary Moglione uses a refined value process that attempts to separate the good from the bad in the value space. That has meant not getting stuck in the value trap and buying firms that look cheap but have ended up performing extremely poorly.

The ability to invest across asset classes has helped too. Investments in alternatives, like music royalties, along with green energy infrastructure and rental income, have helped to support both the trust’s capital appreciation targets, as well as its income goals.

These are also the sorts of assets that look more likely to perform well during a period of inflation. Streamers, energy producers, and property owners can all raise their prices in line with currency devaluations.

Obviously these are attractive qualities for a trust to have in the environment we find ourselves in. But what’s perhaps just as reassuring is that MAVT’s managers delivered strong results, even when there were major macroeconomic trends working against them.

Future success is never guaranteed but investors may want to keep an eye on the trust now that some of those problems have started to disappear and some tailwinds have emerged in their place.

Click **here** to read our latest research on Momentum Multi-Asset Value...

New world order: the big impact of a geopolitical earthquake

Fund managers and investment experts give their view on the aftershocks

Under Donald Trump, geopolitics was focused on US-China trade ties and pacifying North Korea and Russia.

President Biden is a different animal. He has the reputation of being less interventionist as the withdrawal of troops from Afghanistan demonstrated.

The subtle change to soft power and more diplomacy may have been a contributory factor in the timing of Putin's move on Ukraine.

The invasion of Ukraine is the largest military campaign in Europe since the second world war. It has changed geopolitics dramatically and is now too important for investors to ignore.

WHAT SHOULD INVESTORS DO?

While the current geopolitics seem scary, chief investment officer for Europe, Middle East and Africa at Morningstar Dan Kemp reminds investors to stay calm and focus on the long-term.

Kemp told *Shares* that investor responses to unexpected events like war are predictable. In other words, there is a tendency to panic and become too focused on the short-term.

What is more important, said Kemp is to try to figure out the probable effects on a company's long-term cash flows.

It is also important to think about different scenarios and the chances of them happening rather than making specific forecasts.

Finally, explained Kemp, share prices can move fast. This means they may have already discounted the worst case.

In other words, investors need to think about what they see as fair value for shares in relation to how they have already moved.

EVENTS MOVING AT SPEED

Events have certainly been moving at speed and resulted in developments which until recently seemed unimaginable. For instance, Germany said it would ramp up military spending by €100 billion, more than doubling planned 2022 spending on the military.

Chancellor Olaf Scholz said Germany could purchase US F-35 fighter jets made by US firm Lockheed Martin while also urging European partners to build their own 'next generation' fighter jets and tanks.

Reversing a decades long policy of not supplying weapons to 'conflict zones' Germany said it would send anti-tank weapons, surface-to-air missiles and ammunition to Ukraine.

Perhaps European leaders have realised they need to protect their borders irrespective of NATO (North Atlantic Treaty Organisation). NATO has 30 members and was set up in 1949 to guarantee freedom and security through political and military means.

While it is often thought NATO was set up in response to the threat from the Soviet Union, it has broader purposes. These include forbidding nationalist militarism in Europe and encouraging political integration.

The West has so far restricted its actions to implementing financial deterrents by imposing the most stringent sanctions ever seen to strangle the Russia's finances and force it to the negotiating table.

At the same time, Britain, the US and other European countries are providing weapons and ammunition to Ukraine so it can protect itself more effectively.

US investor Bill Ackman, the founder and lead manager of **Pershing Square Holdings (PSH)** believes in providing more weapons to Ukraine.

On social media he has said this will make it more painful for Russia and shorten the time to a negotiated resolution.

While the current geopolitics seem scary, chief investment officer for Europe, Middle East and Africa at Morningstar Dan Kemp reminds investors to stay calm and focus on the long-term.

In an earlier thread on *Twitter* he commented: 'In January 2020, I had nightmares about the potential for a pandemic, but everyone seemed to think I was crazy. I am having similar nightmares now. WWIII has likely started already, but we have been slow to recognize it. Putin has invaded Ukraine and it is not going well.'

OTHER PARTIES TAKING ADVANTAGE

There are concerns the war in Ukraine could create domino effects in other politically sensitive parts of the world.

The US administration has raised concerns again recently over North Korea's development of long-range nuclear weapons. In January North Korea launched an intermediate-range ballistic missile test for the first time in four years.

US intelligence believes its range could be up to 4,500 kilometres which means it could reach Japan.

More tests were conducted in February and March and officials are worried the North Koreans are tinkering with a new system which could allow weapons to travel greater distances, even as far as the US.

> *'WWIII has likely started already, but we have been slow to recognize it. Putin has invaded Ukraine and it is not going well.' Bill Ackman*

The timing of these activities could be linked to the build-up in tensions on the Ukraine border.

It raises the possibility of North Korea and other nations hostile to the West using the Ukraine invasion as an opportunity to challenge the US while it is preoccupied with Eastern Europe.

Biden has said he is willing to engage with Korean leader Kim Jong Un but there doesn't seem to be a sense of urgency to engage in the same manner as his predecessor Trump.

A NEW WORLD ORDER

The biggest unknown quantity in the current conflict is the role China might play. China is the second biggest economy in the world, equivalent to the combined size of Japan, Germany, UK and France.

While president Xi Jinping is on friendly terms with Putin, China has a vested interest in maintaining a stable world economic system and its membership of the WTO (World Trade Organisation).

The reason is because China's does most of its trade with the EU and the US. The yuan is China's currency unit used in the international financial system. The official currency is called renmimbi.

The yuan is the eighth most traded currency in the world and held as reserve currency by major central banks. China has ambitions to make the yuan the world's leading reserve currency, taking over from the mighty US dollar.

For decades all the world's major commodities have been priced in US dollars.

News of Saudi Arabia discussing the possibility of selling some of its oil to Russia in yuan may be a significant turning point, should it come to fruition, according to Carlos von Hardenberg, co-founder of **Mobius Investment Trust (MMIT)**.

Saudi-US relations have become less cordial after the civil war in Yemen and negotiations with Iran over its nuclear program.

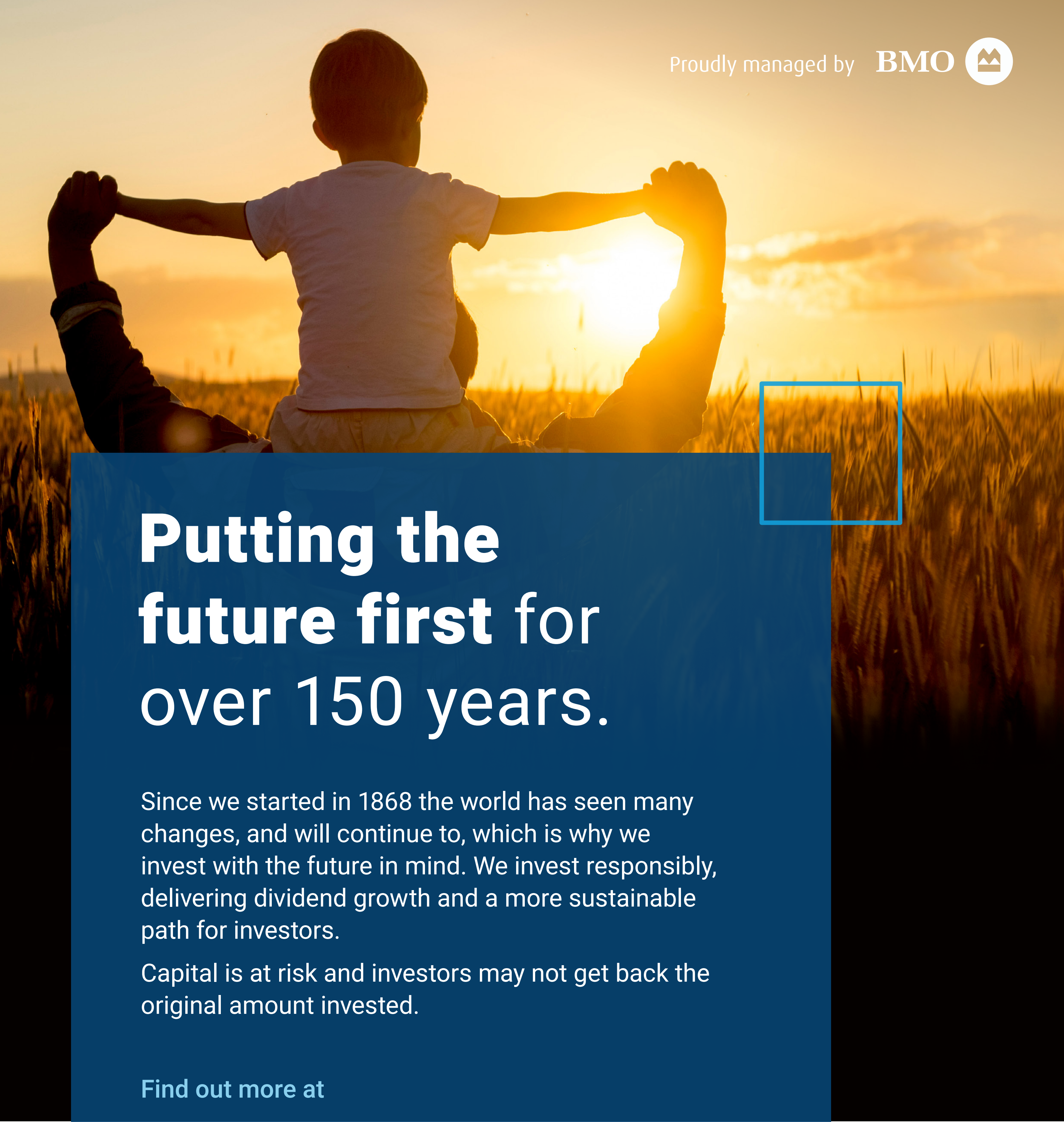
This could mark a critical shift in the dollar's dominance in international trade and tip the balance of power further towards Asia.

Hardenberg told *Shares* he believes China's long-term goals are stability, economic growth and increasing the influence of the yuan in world trade.

Despite speculation China might use the distraction of the war in Ukraine to initiate a military-led integration of Taiwan, Hardenberg thinks this is highly unlikely.

Although China has never recognised the country as an independent territory, it has always taken a very long-term approach to achieving its goals, explained Hardenberg.

By **Martin Gamble,** Education Editor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Why Magners maker C&C can cope with unprecedented cost inflation

Analysts believe profitability could soon return to pre-pandemic levels at the branded drinks maker

Shares in Dublin-headquartered drinks business **C&C (CCR)** frothed higher following a positive trading update (16 Mar) from the maker of everything from cider brands Magners, Bulmers and Orchard Pig to beer brand Tennent's and Tipperary Pure Irish Water.

Investors toasted evidence of continued recovery in its markets and a significantly reduced debt pile. Indeed, Shore Capital noted C&C can not only broaden its drinks portfolio and gain greater market share, but also recover cost inflationary pressures and return profitability to pre-Covid levels of €120 million in the year to February 2024.

HOSPITALITY REOPENING BOOM

C&C, which also owns Matthew Clark Bibendum, the UK's largest independent drink distributor to the on-trade, is benefiting from the lifting of Covid restrictions and the reopening of the UK and Ireland hospitality industries.

The FTSE 250 constituent has guided to an operating profit of between €45 million and €47 million for the year to February 2022. While this was below the €50 million to €55 million range given at October's interim results, the guidance was ahead of the €43 million Shore Capital was looking for with the December and January volume impact from Omicron proving less bad than feared.

'In January 2022, restrictions in our core markets of the UK and Ireland were eased and we are pleased to see positive trading in the on-trade,' enthused C&C.

'We were back trading with 81% of direct delivered outlets in February 2022 versus February 2020, with corresponding volumes at 68% and momentum building as outlets continue to re-open.'

LEVERS TO PULL

The drinks industry is experiencing unprecedented cost pressures, only exacerbated by the conflict in Ukraine, but C&C insisted it is 'afforded a degree of protection through our successfully executed €18 million cost reduction plan, our recent price increases and input cost hedging'.

Shore Capital sees further price increases on the cards 'were recent elevated costs not to unwind', with C&C's branded drinks conferring pricing power on the business.

Forthcoming full year results and an accompanying capital markets day (17 May), where the company will update on the market recovery, set out the opportunity for its distribution-led model and the potential to pass on higher costs, offer the next potential re-rating catalyst, with C&C languishing on 11.3 times Shore Capital's €0.23 (18.9p) earnings forecast for 2024.

Shore also notes that C&C's leading distribution business should benefit thanks to its scale and range from increased environmental considerations, with an emphasis on large, less frequent deliveries.

The company's broad portfolio of beverages should also, in Shore's view, stand it in good stead with a consumer which is increasingly 'promiscuous' in its brand choices.

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

Which is better – high yield today or dividend growth tomorrow?

There is a trade-off between current and future income, but the two aren't incompatible

Given present geopolitical and economic uncertainties and the stock market declines seen year-to-date, the portfolio support provided by dividends remain important to investors.

Thankfully this year, we have continued to witness a restoration of dividend payments by an array of companies following the hiatus seen in 2020 when firms suspended payouts to preserve cash at the onset of the pandemic.

For years, investors have worried about the sustainability of UK dividends and come to view higher yield stocks as value traps. The UK stock market has its fair share of large caps in more mature, slower growth sectors such as banking, telecoms, tobacco, oil and mining and tobacco sectors, which partly explains why the market's above-average dividend yield versus other developed markets. During the Covid crisis, some companies did use the pandemic as an excuse to cut their dividends.

UK offers higher yield than other regions

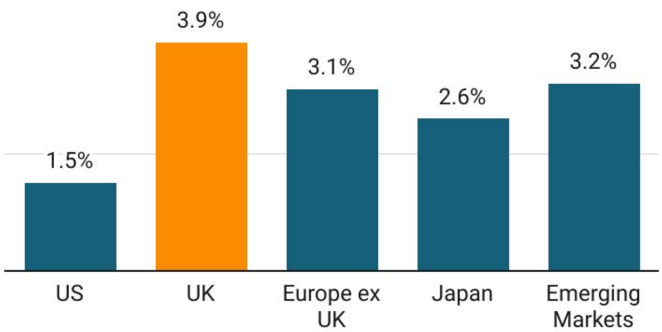


Chart: Shares Magazine • Source: Schroders, IBES, Datastream Refinitiv, MSCI. Data to 28 February 2022 • Created with Datawrapper

But the encouraging news is dividend cover in the UK has improved since the nadir of the pandemic with banking, oil and mining company earnings bouncing back especially strongly.

As Graham Ashby, UK fund manager at **Schroders (SDR)**, explains: 'What happened with Covid is some of the issues around the sustainability of dividends came to the fore and overall dividends ended 2021 around 20% lower compared with prior to the pandemic.

'As a consequence, dividend cover is back closer to two times compared to 1.5 times for a number of years prior to the crisis. We are in a stronger position than we have been for a while for dividend growth and the sustainability of yields.'

THE INCOME TRADE-OFF

Income investors have always faced a trade-off between maximising their income today and growing dividends in the future and there is no right or wrong answer when selecting a fund, trust or stock for income.

A 70 year-old retiree wouldn't be well served by a strategy that delivers higher levels of annual income at a timescale beyond their life expectancy. Conversely, a younger investor seeking to build up a pool of income generating assets to fund a future retirement might choose to forego present income with a view to enhancing future income streams.

High dividend paying stocks are often well-established businesses that generate lots of distributable free cash, yet are mature with limited growth prospects. Dividend growth companies on the other hand tend to pay lower yields as they reinvest part of their cash flows to generate future growth, though dividends of smaller companies are, in general, more volatile but they enjoy higher cover.

GRAPPLING WITH THE DILEMMA

'It is a dilemma that we grapple with day in, day out,' says Matthew Bennison, UK Equity Fund Manager at Schroders. 'The approach that we take in the **Schroder Income Growth Fund (SCF)** and **Schroder UK Alpha Income (B7F32Y0)** fund is a "barbell" approach, very much designed to balance our requirement for yield today versus growth tomorrow.'

Bennison explains that 'if you focus too much on the former, you can crowd into companies that are perhaps overdistributing or don't have high enough growth prospects and you are unlikely to beat inflation with the growth in the income in the medium term.

'Focus too much on the latter and you are less likely to be able to satisfy your income requirements today. If you just have a portfolio of low yielding high growth companies, the absolute yield might only be 1.5%-2% of the portfolio and that is probably unlikely to satisfy the requirements of an investor that is probably looking for 4%.'

With these aforementioned funds, Schroders 'blends the two aspects together' to give a premium yield to the market with dividend growth ahead of inflation. Large high yielders at the value end of the spectrum provide the yield today, while the 'more exciting, more innovative, more growthy companies that have strong franchises and cash generative models' deliver the dividend growth of tomorrow.

TRUST OPPORTUNITIES

In a recent piece of research John Dowie, analyst at investment trust researcher Kepler, pointed out it is important for investors to 'make careful consideration of whether a trust is tilted towards generating a high yield as soon as possible or is orientated towards dividend growth when selecting an investment, in order to make sure it suits their needs and time horizons.' Fortunately, the investment trust space has a mixture of approaches that should meet most requirements.

Dowie drew attention to Troy Asset Management, which has committed to dividend growth in both **Securities Trust of Scotland (STS)**, the global equity income trust Troy took over management of in late 2020, and in UK equity income trust **Troy Income and Growth (TIGT)**.

Troy has rebased the dividends for both to allow for more robust and sustainable future dividend growth, reflecting its view that the current dividend/dividend growth dilemma will become exacerbated over time due to the diminishing quality and growth prospects of today's large, incumbent, old economy dividend payers.

Speaking to *Shares* about Securities Trust of Scotland, manager James Harries explained: 'We are trying to build an optimum balance of quality, income and growth. We have a yield of about 2.7% today and we think that will grow pretty consistently. And we were also keen to rebuild the revenue reserve, which we are doing, so that we can be more secure and certain and give investors a more resilient growing income over time.'

Other trusts with allocations to high dividend payers and stocks with good dividend growth prospects include **Aberdeen Standard Equity Income (ASEI)**, which has 21 years of consecutive dividend growth under its belt and greater exposure to small and mid caps with better capacity for dividend growth than many UK equity income peers.

According to the Association of Investment Companies, the trust boasts a bumper 6.1% yield and also has an attractive five year dividend growth per annum rate of 6.6%. Manager Thomas Moore recently told *Shares* 'it is possible for a high yield trust to be achieving dividend growth. I don't think the two things are incompatible.'

Also shifting to more of a barbell strategy is **BMO UK High Income (BHI)**, whose manager Philip Webster has transitioned the portfolio from a more traditional approach to UK equity income investing to a highly active and often contrarian style, investing in high-quality, innovative firms with attractive growth prospects.

WHY HIGH YIELD WORKS

Simon Gergel manages **Merchants Trust (MRCH)**, which offers an attractive 4.9% dividend yield according to the AIC website. Merchants seeks to provide an above average level of income, income growth and long-term growth of capital through a policy of investing mainly in higher yielding large UK companies.

Holdings span **Scottish & Southern Energy (SSE)**, **Shell (SHEL)** and **Rio Tinto (RIO)** as well as retailers **Next (NXT)** and **Tesco (TSCO)** and dividend growth stocks **DCC (DCC)** and **Homeserve (HSV)**.

'There's a lot of evidence that high yielding shares have historically performed well,' Gergel recently told *Shares*. Not so much in the last few years when investors have chased growth names higher, 'but over longer periods of time, definitely'.

Gergel hasn't 'seen the evidence that dividend growth necessarily works particularly well'. He pointed out many of the companies with the highest dividend growth 'tend to have the highest ratings because they tend to have the highest earnings growth, and high valued companies tend to underperform over time, statistically.

'That doesn't mean that you can't make money as a growth investor, but I'm not sure there's evidence that high dividend growth has been a particularly successful investment style.'

10-year average excess return per year of high versus low dividend US stocks

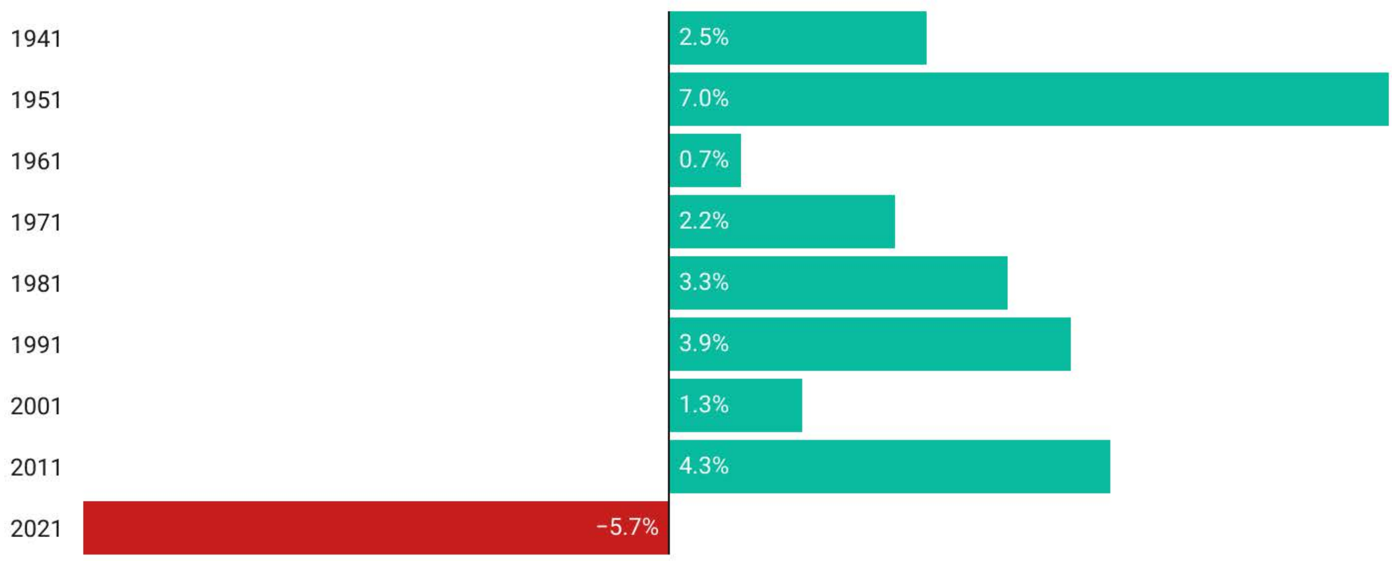


Chart: Shares Magazine • Source: Allianz Global Investors • Created with Datawrapper

Whereas some posit that if you'd bought the companies with the best dividend growth of the last decade you'd have made a fortune, the difficulty according to Gergel is 'you would have had to identify 10 years ago which companies were going to have the best dividend growth and avoid the ones which blow up along the way'.

As for Merchants, Gergel explained: 'We tend to find over time that we get underlying dividend growth out of our portfolio but that's supplemented by this rotation effect, where you might buy a company with a yield of 5% and sell it when it has got a yield of 4% because it goes up 25%.

'And then you've got more money to invest back in at a yield of 5% again, and by doing that you actually boost the income by a substantial amount over time. We get underlying dividend growth but we also get an element of income increasing from this rotation factor.'

Though he fishes in a pond of high yielding stocks, Gergel stressed that 'identifying and avoiding value traps is absolutely critical for any value style and we never buy a company just because it has got a high yield – we only buy companies where we think can make money.'

SUSTAINABLE PAYOUTS

Also weighing in on the debate is Mark Whitehead, who co-manages the **Sanlam Sustainable Global Dividend Fund (B518H39)** with Alan Porter using a bespoke sustainability scorecard, in addition to excluding companies with more than 10% exposure to alcohol, tobacco, gambling, weapons, adult entertainment, and fossil fuel extraction.

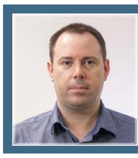
'Over the 15 or so years that I have been investing in dividend paying companies I believe focusing on a company's ability to pay a dividend consistently and to grow it throughout the business cycle could be the best approach to take for more reliable returns,' said Whitehead.

Simply selecting a company with a high yield, however attractive, can 'very often lead to sub-optimal outcomes for investors', he warned.

'Companies exhibiting a high yield very often do so for a reason. The share price may have fallen and therefore the yield is artificially high indicating that the company is not performing. Or the company operates a high earnings pay-out approach as they have nothing better to do with the cashflow they are generating, as the returns on reinvestment in their business are poor.'

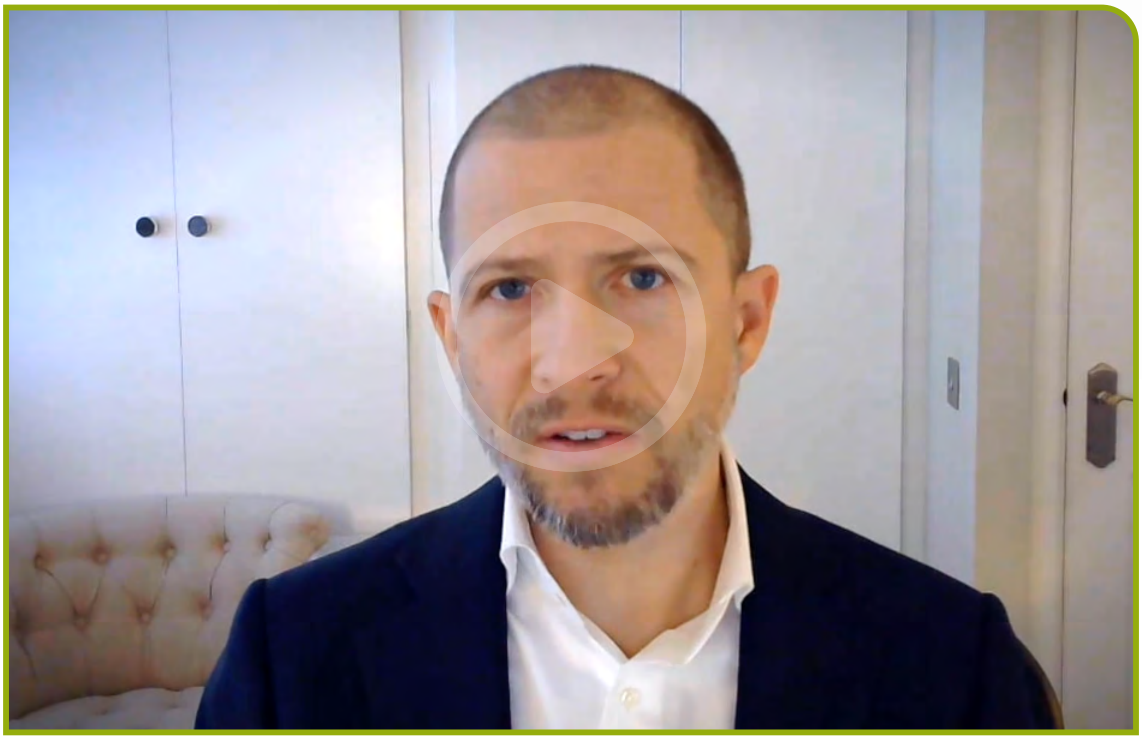
Whitehead also noted that looking at past performance, no guide to future returns of course, 'the MSCI World Dividend Masters Index has consistently outperformed the MSCI World High Dividend Yield Index over long periods. The latter has a higher yield premium to the MSCI World Index, confirming that overreaching for yield can be detrimental to total returns.

'That's why we favour companies that can grow their revenues, earnings and cashflows, even in more difficult operating environments, whilst maintaining their asset bases and re-investing into future growth opportunities. These attributes, combined with prudent balance sheets, liquidity management and sustainability leadership, offer the potential of superior returns to shareholders. These qualities are the hallmark of a successful dividend paying company.'



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

INVESCO BOND INCOME PLUS LIMITED: NAVIGATING THE HIGH YIELD BOND MARKET IN 2022



Rhys Davies
Fund Manager and Senior Credit Analyst

Rising inflation, interest rate hikes, market volatility. What does this all mean for bond markets, and specifically high yield bonds? Can opportunities be found within this sector?

Rhys shares his thoughts and gives an update on the Invesco Bond Income Plus Limited investment trust within this market landscape.

Invesco

GLOSSARY OF TERMS

Duration
Duration is a measurement of a bond's sensitivity to changes in interest rates. Duration is expressed in years and takes into account factors including how long before the bond matures, its yield and coupons.

Maturity
Related to bonds with a final end date ("maturity date"), this is the length of time until the principal amount of a bond must be repaid by the issuer.

Credit risk
Credit risk is the possibility or risk of loss that may happen from a borrower's failure to repay a loan.

Credit spread
Credit spread is the difference in yield between bonds of the same maturity but different credit quality for example, a government bond and a corporate bond of the same maturity.

The yield on a government bond is usually considered to be a benchmark rate and so the credit spread indicates the additional risk that lenders take when they buy a corporate bond vs a government bond of the same maturity.

Credit spreads are measured in basis points, for example a 1% difference in yield would be equal to a spread of 100 basis points.

Credit spread widening
Credit spread widening means there is an increase in the credit spread.

Investment risks
The value of investments and any income will fluctuate (this may partly be the result of exchange rate fluctuations) and investors may not get back the full amount invested.

When making an investment in an investment trust you are buying shares in a company that is listed on a stock exchange. The price of the shares will be determined by supply and demand. Consequently, the share price of an investment trust may be higher or lower than the underlying net asset value of the investments in its portfolio and there can be no certainty that there will be liquidity in the shares.

Invesco Bond Income Plus Limited has a significant proportion of high-yielding bonds, which are of lower credit quality and may result in large fluctuations in the NAV of the product.

The product uses derivatives for efficient portfolio management which may result in increased volatility in the NAV.

The use of borrowings may increase the volatility of the NAV and may reduce returns when asset values fall.

The product may invest in contingent convertible bonds which may result in significant risk of capital loss based on certain trigger events.

As a result of COVID-19, markets have seen a noticeable increase in volatility as well as, in some cases, lower liquidity levels; this may continue and may increase these risks in the future.

Private equity has made a lot of people rich – how do you invest in it?

While companies are remaining unlisted for longer, you can still invest in them

Listing shares on a stock market used to be the default option for many businesses, providing them with access to a large pool of investors to tap up for funding and the ability to use their shares to pay for acquisitions.

However, private equity funding now provides many businesses with a lot of the benefits of a public listing but without all the hassle.

Even though an increasing number of businesses are shunning the stock market, retail investors can still get exposure to privately-owned companies. The simplest way is to buy shares in a private equity-focused investment trust or exchange-traded fund. These funds invest directly or indirectly in private businesses.

BENEFITS OF STAYING PRIVATE

So why are more companies staying private for longer? Private companies can avoid the scrutiny of semi-annual reporting, and the associated media and investor scrutiny that comes with being listed on the stock market. Moreover, by remaining private, a company can retain more control over its ownership and ensure finances and strategies remain confidential.

For investors it is important to acknowledge that increasingly the real value and growth is often created at an earlier stage in a company's lifecycle.

Invariably this is when companies are private. In many instances, companies come to the public market after private equity investors have made their money and are looking to cash out.

WHAT IS PRIVATE EQUITY?

In a nutshell, private equity involves investing in companies that are not listed on the public equity market. These are often referred to as unquoted or unlisted companies.

Private equity investments typically aim to create value in businesses by financing growth, operational improvements, and other changes.

THE ACTIVITIES OF PRIVATE EQUITY COME UNDER THREE BROAD CATEGORIES:

1. Buyouts:
This is where a private equity takes a controlling stake or outright ownership of a business with the intention of helping the company grow profit. Typically, after three to five years, the private equity group would seek an exit either through a trade sale or an IPO. The latter stands for initial public offering, and which is the first chance for the public to directly own shares in a business via the stock market.

2. Venture Capital:
A form of financing that private equity firms provide to young companies and small businesses that are believed to have long-term growth potential. The investor will also provide advice on using capital markets to raise finance in the future.

3. Growth capital:
A private equity firm will make a minority investment in a more developed company. The capital is used to enable the company to expand or restructure operations, enter new markets, or finance a significant acquisition without a change of control.

AIC Private Equity Investment Trust sector

Ranked by 5-year performance

Trust	1 year (%)	3 years (%)	5 years (%)	10 years (%)
Dunedin Enterprise IT	48	37	201	207
HgCapital Trust	19	114	186	437
Oakley Capital Investment	32	109	157	204
ICG Enterprise Trust	10	48	91	271
3i Group	3	35	91	785
HarbourVest Global Private Equity	18	60	86	438
BMO Private Equity Trust	64	45	83	366
Apax Global Alpha	−2	66	80	n/a
NB Private Equity Partners	37	57	75	414
Standard Life Private Equity Trust	2	32	65	291
Pantheon International	14	35	63	278
Princess Private Equity	8	45	60	262
JPEL Private Equity	30	−4	3	90
LMS Capital	−6	−18	−12	−36
AVERAGE	**20**	**47**	**88**	**308**
MSCI World index (a popular benchmark for global listed equities)	10	42	54	216

Table: Shares Magazine • Source: FE Fundinfo, total return in sterling, 9 March 2022 • Created with Datawrapper

HOW MUCH MONEY COULD YOU HAVE MADE?

The average return from 14 investment trusts in the AIC's private equity sector over the past 10 years is 308%, factoring in both share price gains and dividends. That compares to a 216% return from the MSCI World index which is a popular benchmark for global listed equities.

This outperformance can also be seen on a five, three and even one-year basis.

While there are no guarantees that private equity will continue to deliver superior returns, the past performance data does highlight the attractions of this part of the investment universe.

RISKS TO CONSIDER WITH PRIVATE EQUITY INVESTING.

Before you make the step and invest in a private equity-themed fund or investment trust, there are four main areas of potential concern to consider.

The first is the fact that investments in private companies are illiquid. It can take time for a private-equity investor to sell their holding in an unquoted business as they've got to actively seek a buyer. They can't simply sell the shares on the market, which is what a fund manager would do if they invested in quoted equities.

Valuation is another issue. Valuations of unquoted holdings are often updated only once a quarter, so there is a lack of immediate transparency that investors have with companies which trade on a stock market.

Private equity often involves the use of debt to acquire companies and the investee companies may have borrowings. Given that we are in a rising interest rate environment, debt is a potential area of concern.

Another risk associated with private equity is that charges can be high and performance fees are often levied. Conversely, public equities can be accessed at lower cost levels.

However, it is important to recognise that private equity can be a high returning asset class. Arguably the associated fees are a necessary pre-requisite to access these potential returns.

THE ETF ROUTE

For investors looking to gain exposure to the private equity sector, there exists an exchange-traded fund called **LPX Private Equity Swap (XLPE)** which tracks a basket of private equity companies including EQT, Blackstone and KKR.

These three companies account for 34.6% of the portfolio, so there is concentration risk – i.e. if someone goes wrong with one or more of these three companies it will have a notable impact on the ETF's performance.

The ETF charges a fee of 0.7% a year. Over the past 10 years, it has delivered 15% annualised returns according to Morningstar. However, performance year to date has been disappointing, with a 17.8% decline to 9 March. This illustrates how private equity can be a volatile investment.

THE INVESTMENT TRUST ROUTE

Alternatively, investors can get exposure via private equity investment trusts, which tend to fall into one of three categories.

You have trusts which hold direct investments in private companies such as **3i (III)** which has a big stake in European retailer Action.

There are also trusts which fall under the category of 'growth capital', namely where they provide money to help already-established businesses to scale up in exchange for a stake in the company. A good example is **Chrysalis Investments (CHRY)** which invests in buy now, pay later group Klarna.

And then you have private equity fund of funds. These are private equity investment trusts which invest in other private equity funds. You should get much greater diversification through these products than the other two types of private equity trusts. Examples include **Pantheon International (PIN)** and **HarbourVest Global Private Equity (HVPE)**.

PANTHEON INTERNATIONAL AND HARBOURVEST GLOBAL PRIVATE EQUITY

Approximately half of Pantheon's portfolio is invested in the US, 28% in Europe and 11% in Asia and emerging markets. In addition to its investments in funds, Pantheon directly finances companies, alongside some of its best private equity managers. Moreover, it participates directly in the secondary market (buying companies from other investors, often at a discount).

HarbourVest Private Equity also spreads its interests far and wide. Managing director Richard Hickman says: 'HarbourVest Private Equity is well diversified; we have exposure across the whole range, from early-stage venture investments, through growth equity buyouts of all different sizes. We also have real assets including infrastructure and a small amount of credit which is the floating rate debt in private companies.'

Pantheon has delivered a 278% total return over the past 10 years, yet its shares currently trade at a 29% discount to net asset value. In a similar boat is HarbourVest which trades on a 28% discount to NAV despite generating 438% total return over 10 years.

Large discounts are commonplace among many private equity trusts, particularly ones in the fund of funds category. That can be explained by them being less transparent, a greater amount of illiquid underlying holdings and uncertainty over the true valuation of the assets.

By **Mark Gardner** Senior Reporter

Deere still going strong after 185 years at the forefront of farming

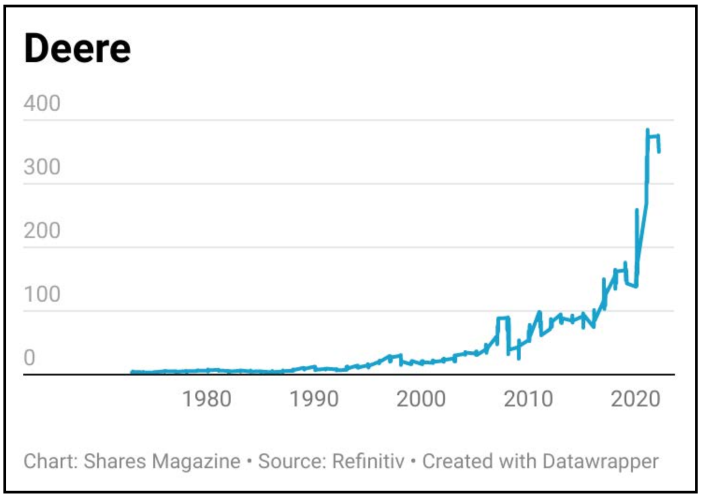
The Illinois firm's next big seller could be self-driving tractors as it continues to innovate

With its signature green and yellow branding, Deere may be the most recognisable tractor maker in the world, but it does a lot more besides selling farm equipment.

With the war in Ukraine highlighting the importance of food production and food security as well as efficient farming practices, Deere's cutting edge agricultural equipment could be in strong demand.

Many of its products use up-to-the-minute technology which both save time and money and also improve sustainability, an increasingly important consideration as environmental concerns move to the forefront.

While it can trace its history back to 1837, and still has its group headquarters in Illinois, the company is far from being stuck in the past.



A LEADER IN ITS FIELD

From its origins as a plough maker, Deere hit the jackpot just under a century ago in 1923 with the introduction of the Model D tractor.

Originally equipped with a 30hp engine, the Model D turned mechanised farming into a reality in the US and was so popular production lasted 30 years.

During the Depression, farming was probably the hardest occupation in America as the global economic slowdown coincided with one of the worst and longest droughts in US history.

The firm survived, however, and in 1945 it introduced the Model M with its Quick-Tatch system of attaching implements, another quantum leap forward in farming.

Always looking for ways to improve its products, in 1954 Deere was the first firm to introduce power steering on its tractors.

This was followed by power brakes, a cab for protection and eventually functions such as air conditioning and dust filtration.

Today, Deere employs more software engineers than mechanical engineers and its tractors are jam-packed with the technology.

They employ precise global navigation satellite systems technology, advanced connectivity and telematics, on-board sensors and computing power and automation software.

Guided by sat-nav, they can 'tell' the spraying boom which plants are weeds and which are crops so that only the weeds are sprayed with pesticide.

At an average 12 miles per hour, that means the tractor and the boom are monitoring around

2,000 square feet per second, which makes it an incredibly efficient way of treating weeds.

It also cuts down the use of pesticides, which is important for farmers trying to establish a balance between higher yields and sustainability.

Using advanced telematics, the tractor's systems can even connect equipment owners, business managers and dealers to equipment in the field to provide real-time alerts and information about its location, utilisation, performance and maintenance.

In January the firm unveiled an autonomous tractor. And in 2021 chief technology officer Jahmy Hindman told *Decoder*, a podcast produced by US tech news site *The Verge*, that 'operatorless operation in, say, fall tillage or spring planting, we're right on the doorstep of that.

'We're knocking on the door of being able to do it.'

STRUCTURE AND PERFORMANCE

The firm is organised into four divisions, the two largest of which are dedicated to agricultural machinery and make up roughly two thirds of sales.

Production and Precision Agriculture develops and manufactures equipment and technology for production-scale farming such as tractors, combines and seeding and crop care equipment.

Small Agriculture and Turf supplies mid-size and small growers, and also makes production systems for dairy and livestock. Products include small tractors, ride-on mowers, golf course equipment and utility vehicles.

The Construction & Forestry division manufactures earth movers, material handling, timber harvesting and road building equipment and accounts for roughly a quarter of sales

The fourth division is Financial Services, which provides credit to buyers of Deere equipment and makes up roughly 10% of sales.

EARNINGS AND SALES GROWING FAST

	2021 Actual	2022 Estimate	2023 Estimate
Equipment Sales	$39.7 billion	$47.6 billion	$51.4 billion
Earnings per share	$18.99	$22.67	$25.99

Data correct as of 15 March, 2022

Table: Shares Magazine • Source: Zacks consensus estimates, Shares magazine • Created with Datawrapper

In the financial year to October 2021, the firm generated net sales of $44 billion compared with $35.5 billion the previous year.

Equipment sales reached $39.7 billion compared with $31.3 billion the previous year, an increase of 27% thanks to a combination of higher volumes and higher selling prices.

Operating profits for the equipment business almost doubled from $3.56 billion to $6.87 billion thanks to more sales of high-margin products and a gain on the sale of a factory in China.

Net income for the equipment business more than doubled from $2.18 billion to $5.08 billion, while net income for the financial services business increased 55% from $556 million to $881 million.

At a group level, cash flows from operations were $7.73 billion, which allowed the firm to buy back $2.54 billion of its own shares and pay out $1 billion in dividends, so shareholders were well rewarded.

CURRENT TRADING AND OUTLOOK

In the first quarter to 30 January, revenues were $9.57 billion against a FactSet consensus of $8.28 billion, with net sales from equipment operations alone reaching $8.53 billion.

Net earnings per share were $2.92, below last year's figure of $3.87 per share due to higher production costs and supply chain bottlenecks but significantly ahead of the FactSet consensus of $2.27 billion.

By division, the firm is expecting 25% to 30% revenue growth in its Production and Precision Agriculture business, 15% growth in Small

Agriculture and Turf and between 10% and 15% in Construction and Forestry.

Chief executive John C. May raised full year net earnings guidance for the group from $6.5 billion to $6.7 billion to between $6.7 billion and $7.1 billion citing the 'strong fundamentals' of demand for farm and construction equipment.

Zacks Equity Research says the ongoing rally in commodity prices will continue to fuel agricultural equipment demand, encouraging farmers to boost spending on new farm equipment.

It points out that corn and soybeans are the most important grains for cash crop farming in the US. Given Russia and Ukraine account for around a fifth of global corn output, prices are likely to keep rising.

At the same time, owing to high potash prices, farmers are opting to cultivate soybean as it is a less fertiliser-intensive crop. With soybean prices also rising, farm income is growing meaning more demand to upgrade old equipment.

Meanwhile, Deere's construction equipment business is likely to benefit from growth in non-residential investment and strong order activity from independent rental companies.

Global roadbuilding markets are expected to be up between 5% and 10%, with growth in the North American market offsetting some weakness in China, adds Zacks.

Morningstar believes the big issue for heavy machinery firms like Deere isn't demand but supply, although it sees pressures easing over the course of the year.

'Deere's first quarter results showed its continued resiliency despite a challenging operating environment', says analyst Dawit Woldermariam.

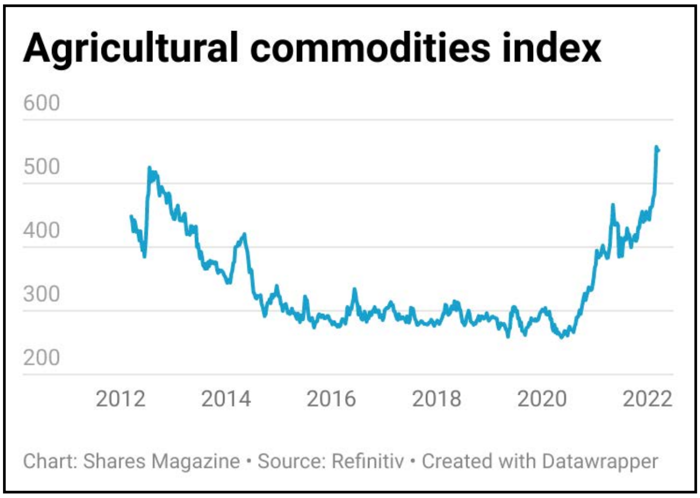


Chart: Shares Magazine • Source: Refinitiv • Created with Datawrapper

Pressure on margins will start to reverse in the next couple of quarters, according to Woldermariam.

Deere's position as a premium equipment maker gives it the ability to consistently raise prices through the cycle, he adds.

OWNING DEERE

UK investors can buy shares in Deere directly, although dealing charges are typically higher for overseas shares than for UK shares and there are also foreign exchange charges to take into account.

For those looking for a broad exposure to agriculture as a theme there are a couple of funds worth considering.

The **Pictet Nutrition Fund (B54YLC1)** invests in companies developing solutions to help secure global food supplies, including improving farming productivity and maximizing the nutritional content of what we eat.

The fund's biggest position is Deere, followed by Dutch ingredients firm DSM and Irish nutrition company **Kerry Group (KYGA)**.

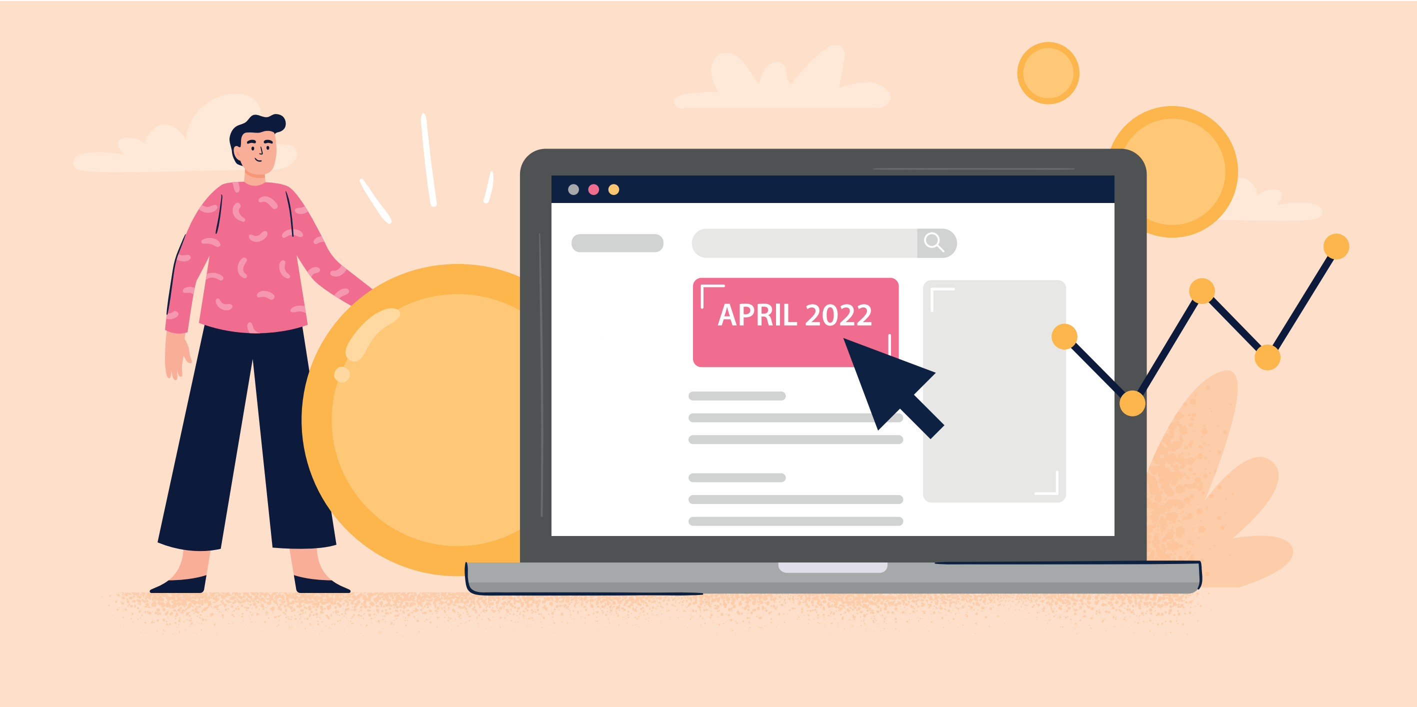
The fund has lagged the MSCI World Index in sterling over the last six months, which might make this a good time to take a closer look especially as it only has an ongoing charge of 1.1%.

The **Sarasin Food & Agriculture Opportunities Fund (B77DTQ9)** also lists Deere as its number one holding and has also under-performed its benchmark, although it has a ongoing charges of 1.75%.

By **Ian Conway** Companies Editor

What not to do as the tax year end looms

Four things to consider with the 5 April HMRC deadline on the horizon



STICKING WITH CASH IN A HIGH INFLATION WORLD

Inflation is expected to peak at more than 7% in April, just as ISA season comes to a close. Fears of savings being eaten away by inflation is probably near the top of investors' list of worries right now. Inflation is the enemy of cash, as no cash ISA account interest rate comes anywhere near the current rate of inflation, let alone what it's going to peak at this year.

For example, £10,000 saved in a cash account 10 years ago would now be worth just £9,385 today, after inflation is taken into account. But in the next 12 months alone, Cash ISA savers face a similar loss in buying power to the one they have experienced over the last decade. £10,000 saved into the average Cash ISA today could be worth just £9,600 this time next year, based on the latest Bank of England forecasts for interest rates and inflation, and the current margin between base rate and ISA rates (see chart, next page).

That means that you should only have your essential, short-term money in cash. While cash is a great place for short-term savings or money you need quick access to, it's not ideal for long-term savings.

So, work out what you need in the next five years or as an emergency pot, and see how that stacks up against the amount you've got in cash. If you've got more than that set aside, think about investing it to generate a potentially higher return.

If you saved £200 a month into a cash ISA, earning the current average ISA interest rate of 0.19% you'd have a pot worth £24,250 after 10 years.

But if you invested that and earned 5% returns a year you'd have almost £31,700 – £7,444 more. Of course, there is no guarantee that an investment in the stock market will beat inflation, but over the longer term, investing in stocks is one of the key defence's savers have against rising prices.

Interest rate and inflation expectations

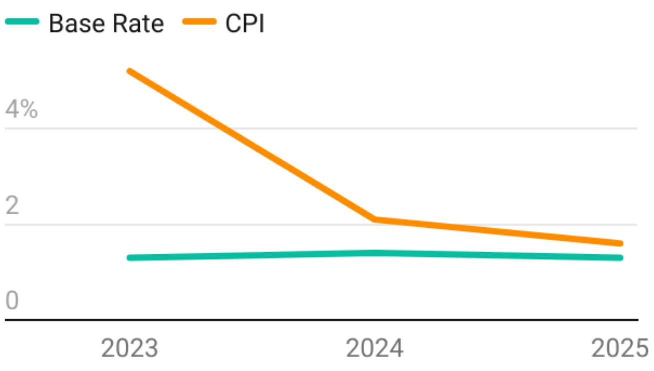


Chart: Shares Magazine • Source: Bank of England, the path for Bank rate implied by forward market interest rates and CPI projections based on Bank rate following that path. • Created with Datawrapper

NOT AUTOMATICALLY REINVESTING YOUR DIVIDEND INCOME

Any dividends from investments in your ISA can be withdrawn tax-free, but if you don't need the income now you could use them to turbo-charge your returns. If you reinvest them you can buy more shares in the same investment, which can have a dramatic impact on the size of your ISA fund over the long term.

This is because when you buy more shares each time you receive a dividend, you then receive more dividends next time there is a pay-out, which can then be reinvested again and so on. Some investment platforms allow you to set this up to happen automatically.

Let's assume someone invests the full ISA allowance of £20,000 and we assume a compound annual growth rate of 5% and annual dividend yield of 4% a year. The initial £20,000 will be worth £53,066 after 20 years, and on top of that £26,453 would also have been banked in cash dividends, to give a total return of £79,519. However, an investor who reinvests the dividends rather than banking them would have £112,088 – more than £32,500 extra. The figures become even more attractive over longer periods.

GETTING CAUGHT IN A TAX TRAP

The tax-free personal allowance for most people is currently £12,570. When your taxable income reaches £100,000, your personal allowance is cut by £1 for every £2 of your income, which means you lose it completely once your income reaches £125,140.

For example, someone who gets a pay-rise from £100,000 to £110,000 will lose £5,000 of their personal allowance. They will be taxed at the normal 40% income tax on their pay rise,

The impact of dividend reinvestment

	5% compound annual capital return only	Dividends paid in cash (4% yield)	Investment value + cash dividends	5% compound annual capital return PLUS 4% dividend yield reinvested	Difference
Initial investment	£20,000	-	-	£20,000	-
After 10 years	£32,578	£10,062	£42,640	£47,347	£4,707
After 20 years	£53,066	£26,453	£79,519	£112,088	£32,569
After 30 years	£86,439	£53,151	£139,590	£265,354	£125,764

Table: Shares Magazine • Source: AJ Bell • Created with Datawrapper amounting to £4,000, and then taxed at 40% on their lost personal allowance, amounting to £2,000. This means they pay £6,000 on the £10,000 pay rise – an effective tax rate of 60%.

If you are in this position you could consider reducing your taxable income so that it falls below the £100,000 level where the personal allowance starts to be eroded. Two ways you can do this are by making charity donations or contributing to a pension if you have pension annual allowance available. By contributing to a pension you are making tax savings in the form of getting your personal allowance back while also saving for your future and benefiting from pension tax relief at 40%, so you wipe out the 60% effective tax rate completely.

In a similar way as above, people will start to lose their child benefit when one half of the couple earns more than £50,000 – and the benefit will be wiped out entirely when they hit £60,000. A parent with two children will get £1,828 a year in child benefit in 2021/22 (£1,885 in 2022/23), but for every £1,000 they earn over £50,000 they will lose 10% of their child benefit – so someone earning £51,000 will lose £183.

However, parents who have just tipped over the threshold can get around this by increasing their pension contributions. What's counted for the purposes of the child benefit 'High Income Charge' is your salary after any pension deductions. This means if you contribute enough to your pension to get your salary back to £49,999 then you'll get the full child benefit again.

FORGETTING ABOUT THE KIDS

Between them a family of four can now put £116,000 in tax-free accounts in the month of April. Each adult has a £20,000 annual ISA limit and the Junior ISA limit is a whopping £9,000 now. If all four family members maxed out their allowance in early April and then again in the new tax year, they'd protect £116,000 from tax. What's more, a weird loophole means that if your child is 16 or 17 they get the full adult ISA allowance, just for a cash ISA, as well as the Junior ISA allowance. So with one 16 or 17-year-old as part of the family your limit gets bumped to £156,000.

Now, clearly not many families have £156,000 stuffed down the back of the sofa. But it's important to remember everyone's ISA allowances and to also put money away for your children if you have spare cash. If you put money into a Junior ISA your children won't be able to access the money until they are 18, at which point it automatically turns into a normal ISA and transfers into their name, giving them full access.

If you contribute the maximum £9,000 each year from birth and achieved a 5% investment return after charges each year, the pot would be worth almost £266,000 by the time your child turns 18. Even a more modest £50 a month, earning 5% returns a year, would give your child a £16,000 present on their 18th birthday.

If your child is a bit older you don't need to feel like you've missed the boat. Even if you don't start saving until the age of 10 and you put away £50 a month then you'd have built up a pot worth almost £7,000 when they hit 18. If you increased that contribution to £150 a month then you'd have £20,850.

DISCLAIMER: Financial services company AJ Bell referenced in this article owns Shares magazine. The author of this article (Laura Suter) and the editor (Tom Sieber) own shares in AJ Bell.

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

SECURITIES TRUST OF SCOTLAND
INCOME MATTERS

TROY ASSET MANAGEMENT was established by Lord Weinstock of GEC renown, and Sebastian Lyon in 2000 to protect and grow investors' capital - in that order. Troy, having seen the GEC business destroyed in the technology boom, recognised that times of heightened speculation can be catastrophic to wealth preservation if one loses perspective, patience and discipline.

At the core of this is to invest without reference to benchmarks but with reference to the underlying quality of the businesses in which you invest and have an absolute return mind set. Capital allocation is a function of seeking to balance quality, growth and income while ensuring adequate diversification and no notion of being "overweight" or "underweight" in any particular sector or company. Once a portfolio is established, we believe turnover should be kept low, recognising that the real money is made in the patient compounding in a settled, quality portfolio and not in the continuous buying and selling of shares. Finally this inherently conservative but quality-focussed approach should deliver above average returns with below average volatility over a full market cycle. This is especially important for those with irreplaceable capital and in need of income – two things which often coincide with retirement.

In these disquieting times, this approach is more relevant today than ever. Even before COVID-19 appeared, the backdrop was laden with risk to the unwary investor. After years of structurally declining interest rates and rising asset markets, we are left with an opportunity set across capital markets (bonds, equity, credit, property and so on) that is fully valued by many historical measures which implies low returns. This is at a time when several other underlying factors are also reaching historical extremes. These include levels of indebtedness, declines in working age populations owing to demographics and the pace of technological disruption, which are making economic growth and inflation hard to achieve.

So what are we to do? We believe that investing globally in a portfolio of high quality income bearing equities remains a compelling prospect for investors to meet their needs. But it must be done in a way that recognises and accommodates these distortions and challenges. We are therefore highly selective about the businesses in which we invest , concentrating on those that demonstrate their quality by having a high return on capital employed. This is derived from identifiable and durable competitive advantages and a business model that does not require large amounts of capital to grow and enables companies to both invest adequately in their businesses as well as pay an income. We want businesses that are well financed and sensibly managed. Such a portfolio should generate consistently growing free cash flow which funds both income and capital growth in a predictable way.

In Securities Trust of Scotland, we have constructed a historically resilient portfolio that generates an approximately 5% free cash flow yield funding a current 2.5% income yield which we expect to grow next year and beyond. In this way, we are able to meet the needs of our investors and face the future with confidence despite the uncertain outlook.

James Harries, Manager of Securities Trust of Scotland

Rate hike: what it means for mortgage borrowers and savers

Looking at the Bank of England's latest decision and the impact it will have

The Bank of England has increased interest rates for the third time in four months, taking the Base Rate to 0.75%. The Monetary Policy Committee, who decide whether rates will be increased or not, voted 8-1 in favour of a rise from 0.5% to 0.75%.

The rate decision will have a big impact on anyone with a mortgage and cash savers. Let's look at how it affects them.

MORTGAGE BORROWERS

Anyone on a variable rate mortgage will see their interest rates go up. Trade body UK Finance estimates that about two million households will see an immediate increase in their mortgage payments. The increase from 0.5% up to 0.75% will mean someone with a £250,000 variable rate mortgage will pay an extra £384 a year. (Assumes a repayment mortgage with a 25-year term, at the current average variable rate of 2.47%, based on BoE figures.) With higher borrowing of £450,000 the increase is more dramatic, with those homeowners having to pay an extra £684 a year.

But mortgage holders on a variable rate should be braced for even higher bills. The current market expectations are that the base rate will rise four more times this year, taking it to around 1.75% before the end of 2022. If this is the case, homeowners with £250,000 of borrowing will have to pay an extra £1,956 a year, or £163 a month, while those with £450,000 of borrowing will have to find an extra £3,528 a year, compared to when Base Rate was 0.5% – which is a lot of spare cash to find when so many other costs are already rising.

Anyone who wants to beat these price hikes can fix their mortgage rate to get a better deal, although they need to be quick to beat further increases by mortgage companies. But the potential savings are big. Someone with a £250,000 mortgage who is currently on the average variable rate could save £4,184 over the next two years by switching to the current top two-year fix, which is 0.99% from Furness Building Society. If you fix your mortgage rate for longer you'll get a slightly higher rate, but save more over the longer term.

SAVERS

Interest rate rises are good news for cash savers. As a result of the past two interest rate hikes we've seen the top easy-access savings account rate rise from 0.65% ahead of the December rate increase to the current 1%, based on data from Moneyfacts.

However, anyone who wants to access these higher rates needs to hunt around for a better deal – it won't just be handed to them. Lots of people's savings are just sitting in their current account or old savings account, earning 0.01% – and these people likely won't see an increase in the interest rate they're being paid.

One area savers need to be wary of is fixing their savings rate for a year or more. By fixing savers can access higher rates, for example the current top two-year fix pays 1.9%, based on data from Moneyfacts, which is almost double the top easy-access rate.

But savers need to seriously consider what interest rates will do in that two-year period and if that deal will look attractive in a year or two's time. While nothing is certain, markets are expecting more increases this year and for rates to be sitting at around 1.75% by the end of 2022. If that's the case we'll see the interest offered on fixed rate accounts rise and anyone who has already fixed won't be able to benefit from those rises.

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

The UK's sterling start to 2022

Ben Ritchie, Investment Manager, Dunedin Income Growth Investment Trust

The UK stock market has had a strong start to the year, with the FTSE 100 outpacing the FTSE World by almost 7% over the past three months. This reappraisal from investors is welcome, given how unfashionable the UK market has been in recent years, but many will be asking whether it can endure longer than previous short-lived rallies.

It may be tempting to dismiss the UK's recent outperformance as just a function of the flip-flop between value and growth. Certainly, the UK does have more exposure to companies that would be deemed 'value' – commodities, metals, oil or big banks, However, these companies aren't doing well just because they are value companies. The earnings prospects for many of these areas have notably improved. The recent share price improvement is as much a reflection of that improvement as it is a value rotation.

Some of the UK's largest companies are benefiting from rising oil, gas and iron ore prices. These have been driven higher both by the crisis in Ukraine, but also by longer-term supply and demand imbalances. The UK's banks will benefit from rising short-term interest rates as the monetary policy environment changes. It isn't just about cheap multiples and it is worth noting that some stocks on low multiples that have actually performed very poorly. Companies have needed more in their armoury to do well.

The UK market has also benefited from the stocks it doesn't have. It isn't inundated with high valuation

growth companies, unlike some other markets. As such, it hasn't been dragged lower by the sell-off seen in areas such as technology. Overall, while this dynamic has been difficult for Dunedin Income Growth Investment Trust's relative performance against the FTSE All-Share one positive is that it has supported its return against other major markets. While we are confident in our longer term positioning towards more sustainable and higher quality companies it would be churlish to dismiss the performance of a number of sectors as not respecting near term fundamentals when it clearly does!

Rising activism

There have been a number of high profile activist investors becoming involved in UK companies. Cevian has pushed for a sweeping overhaul at Vodafone, while Trian has built a stake in Unilever. Elliott Management has demanded changes to the board at SSE.

There are a few possible conclusions to be drawn from the pick-up in activity. The first is that international investors see value in the UK market. These activists are usually global hedge funds, who can choose where in the world they invest. They have chosen UK companies because they are trading on low valuations relative to their growth potential.

Also, the UK has the corporate governance structure that allows this type of activity. In general, there are no significant government stakes in UK companies, and activists are unlikely to encounter family ownership issues. There aren't complexities such as multiple share classes with different voting rights. The UK's strong corporate governance structure allows individuals to have a significant impact through their shareholdings.

It also shows that there are lots of ways to realise value. The activist way is to do it in public. We prefer to realise value by engaging in a different way. In many cases, we are pushing for similar reform to the activists, encouraging good governance structures or a change in strategic direction, but we're doing it behind the scenes.

Structural growth in healthcare

Healthcare is our second largest overweight position in the Dunedin income Growth portfolio. The sector has long had some interesting structural tailwinds as a result of shifting demographics and the ageing global population. More recently, the sector has also benefited from an explosion in scientific exploration. This is focused on significant pockets of unmet need, notably in areas such as oncology.

Against that backdrop, the trust has exposure to Novo Nordisk, which has leading market share in diabetes treatments. It is unfortunately a growing market and they also have impressive new obesity treatments in development. AstraZeneca is another holding in the trust. The company has a significant presence in oncology, having built a leading position in immunotherapy. Following its recent acquisition of Alexion it now has a portfolio of rare diseases treatments as well.

Both companies are undertaking significant research and development. Increasingly, they recognise the benefit not of simply having a product and letting it roll through, but seeing how its life cycle can be extended. Can it be used on other types of cancer, for example? Or in conjunction with other drugs to deliver better outcomes? The trust also has exposure to some smaller healthcare companies in niche areas such as animal health or genetics. These are subject to different dynamics to the standard healthcare companies. They don't have to deal with patent expiry, for example, which enhances their competitive position.

When to worry

There is a lot to worry about at the moment – from rising interest rates to the war in Ukraine to market volatility. Which areas are the greatest risk to share prices? At their current levels, rising interest rates are not a significant break on economic growth. The market is pricing in five rate rises for the year ahead, taking the base rate to around 1.25%. This would be manageable and unlikely to derail growth. If rising inflation pushes central banks to act more forcefully, it may start to have a negative impact on growth. It is worth remembering that rising interest rates can be helpful for some sectors, such as the banks.

The greater worry is that the earnings environment for companies is getting a little more difficult. The impact of withdrawing monetary and fiscal support remains unknown and may not be clear for six months or more. In the meantime, recovery is already slowing and businesses are facing diverse challenges from higher inflation and rising borrowing costs. We are making sure that the companies in which we invest are in good shape and prepared for a range of eventualities, and are able to deliver consistently on earnings and dividend growth. These will be the areas prized by investors in a more challenging outlook for profitability.

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

RUSS MOULD
AJ Bell Investment Director

Just how far could commodity prices go?

Examining the prospects for metals and energy markets after a strong recent run

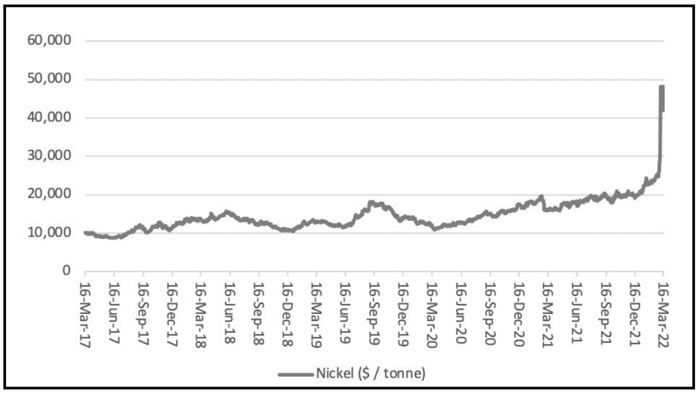
And so Xiang Guangda, founder of Chinese nickel firm Tsingshan, joins an infamous list of firms and traders who have had their trousers pulled right down when trading commodities. But neither the humbling experience nor its scale – a reported $8 billion paper loss – are as rare as you might think.

The main lesson to draw from this when it comes to commodities trading is therefore 'don't try this at home', especially if you are using leverage (or trading margin using borrowed money) to do it.

Take a considered long-term view on commodities as part of a diversified portfolio - by all means, if it fits with your overall strategy, time horizon, target returns and appetite. Go all in on one commodity and trade it like a dervish – definitely not.

The main question that this accident begs is just how far can commodity prices go? The London Metal Exchange had to suspend trading in nickel, such was the chaos, and one business began again the metal quickly retreated. This is not the sort of action that you see at market bottoms when sentiment is washed out.

Nickel has been a very volatile market



Source: Refinitiv data

That in turn begs the question of what could happen to commodity-related stocks? They represent almost a fifth of the market capitalisation of the FTSE 100, so further gains or losses could have an impact on the headline index, something which investors who own tracker of ETFs (exchange-traded funds) should consider, even if they have no interest in researching or buying individual stocks themselves.

HEAVY METAL

Xiang Guangda's troubles stem from a short position on nickel. This was based on the premise the metal would fall in value but instead it rose sharply as traders and industrial buyers fretted about the potential loss of Russian supply and he then had to close out his position, buying more metal and creating a self-fulfilling (and in Xiang's case self-defeating) upward price spiral. The net result was an $8 billion loss, on paper anyway, and entry into a far-from exclusive club of big commodity price losers which includes:

- The Bunker Hunt brothers' $1.7 billion loss when they tried to corner the silver market in 1979;
- The German conglomerate Metallgesellschaft lost $1.3 billion on oil futures in 1993;
- Sumitomo's Yasuo Hamanaka, who lost $2.6 billion in copper in 1996;
- Liu Qibing racked up losses thought (but never confirmed) to be more than $1 billion

when trading copper for China's State Reserve Bureau in 2006;
- The hedge fund Amaranth blew itself up with a $6 billion loss as natural gas price fell, instead of rising as expected, in 2006.

The Tsingshan losses are the first major accident in the commodities market for a while (and in inflation-adjusted terms the Bunker Hunts came a far bigger cropper) but they do beg the question of whether they are sounding a bell for a market top in the price of not just nickel but raw materials across the board after their recent surge.

The best cure for high prices is high prices as they prompt a search for other options or force users to consume less. Unlikely as it may seem right now, any sort of ceasefire or peace deal in Ukraine could also ease a lot of fears over supply from Russia, which is a top-five global provider of palladium, diamond, gas, oil, platinum, aluminium, potash, nickel, titanium and steel.

INFLATED EXPECTATIONS

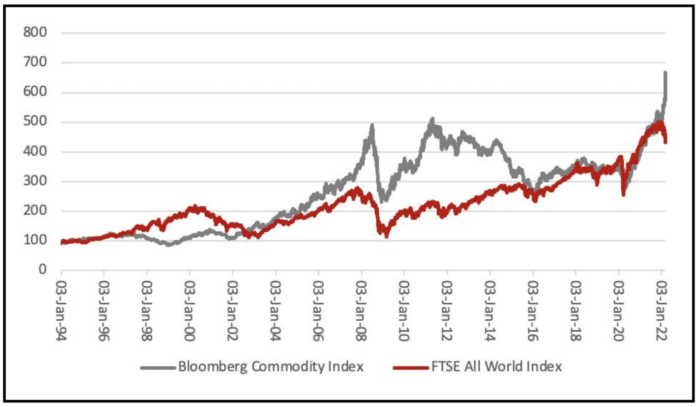
However, the conflict is not the only story when it comes to commodities (and nor are commodities the only story when it comes to the conflict, given the human suffering involved).

Neither miners nor oil explorers have invested heavily for some time in new capacity, owing to the combination of weak commodity prices in the middle of the last decade, the need to pay down debt after an acquisition spree, calls for higher cash returns from investors or pressure from environmental campaigners (and the wider public).

If demand remains strong, either from industrial buyers as the global economy ticks along, or financial ones if they feel the need to seek a haven from inflation, then raw material prices could yet move higher over time.

Some of the potential upside does look priced in, since the Bloomberg Commodity index is once more handily outperforming the FTSE All-World equity index, just as it did during 2000-2010 period when central banks had to slash interest rates in two cycles in the face of two economic and stock market busts – maybe the policy response to the pandemic will produce another upswing.

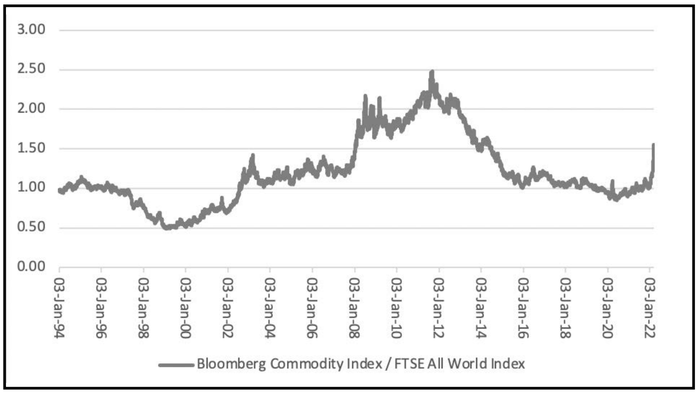
Commodities are once more outperforming equities



Source: Refinitiv data

But analysis of the Bloomberg benchmark against the FTSE All World on a relative basis shows a slightly different picture. If commodity prices really go into orbit, then this suggests 'real stuff' could outperform 'paper assets' for a good while and by a good degree yet, especially if inflation or stagflation are the ultimate economic outcome. Commodities' outperformed much more strongly and for much longer in the 2000s than they have thus far this time around.

Commodities not outperformed equities to the degree seen in the early 2000s



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Equally a recession would in all likelihood for bad news for many commodities, especially industrial metals, although precious metals could yet shine under those circumstances, depending upon the policy response from governments and central banks.

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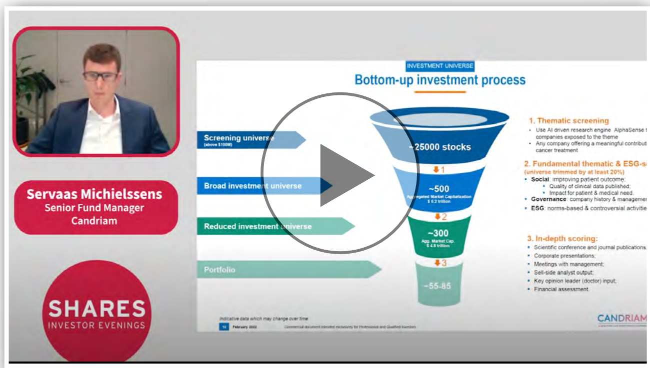

Candriam
Servaas Michielssens, Senior Fund Manager

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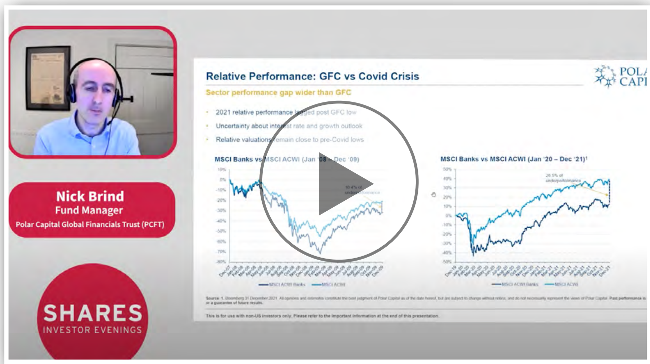
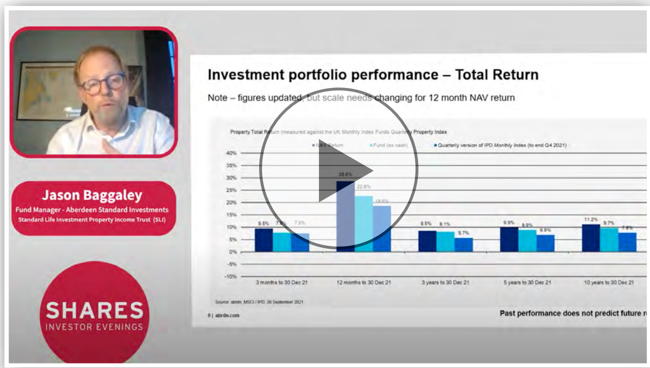


Polar Capital Global Financials Trust
Nick Brind, Fund Manager

Polar Capital Global Financials Trust aims to select the best investment opportunities from the world of financials. The five-strong investment team, with almost 100 years' experience invest solely in financials, scouring the globe and actively investing in developed regions such as the US as well as emerging economies and Asia.



Standard Life Investment Property Income Trust
Jason Baggaley, Fund Manager

The Trust aims to provide shareholders with an attractive level of income together with the prospect of income and capital growth. This is achieved by investing in a diversified portfolio of UK commercial properties. The majority of the portfolio is invested in direct holdings within the three main commercial property sectors of retail, office and industrial.

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KEY ANNOUNCEMENTS OVER THE NEXT WEEK

Full-year results:
28 Mar: Dialight, Octopus Renewables Infrastructure Trust, RTC, Tandem. **29 Mar:** Animalcare, Aquis Exchange, Bank of Cyprus, Boku, Central Asia Metals, CPP, EKF Diagnostics, Ergomed, Fireangel Safety Technology, Flowtech Fluidpower, Good Energy, IQE, The Mission, NAHL, S&U, STM, Ten Entertainment, Tinybuild, Xaar, XLMedia. **30 Mar:** Equals, Gulf Keystone Michelmersh Brick Holdings, Next, Strix, Team17. **31 Mar:** BBGI Global Infrastructure, Elecosoft, Hostelworld, Reach, RTW Venture Fund, S4 Capital.

Half-year results:
29 Mar: Bellway, Genedrive, Orchard Funding, SkinBioTherapeutics. **31 Mar:** Aptamer, James Halstead.

Trading announcements:
30 Mar: Electrocomponents. **1 Apr:** Pennon.

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