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SHARES

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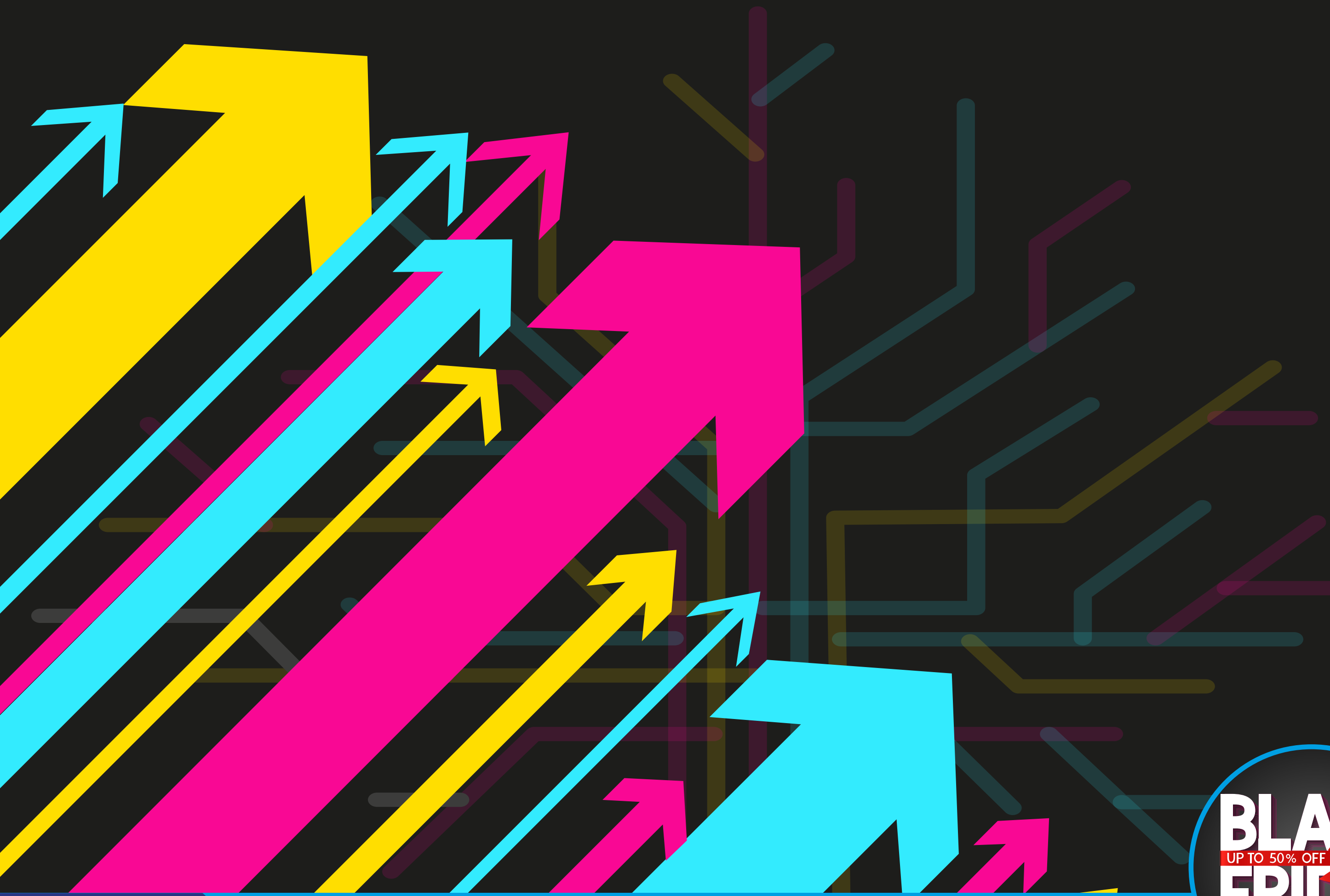
6 UK STOCKS TO BUY NOW

Markets are starting to recover



NEWS Black Friday sales expected to fall as consumers cut back on spending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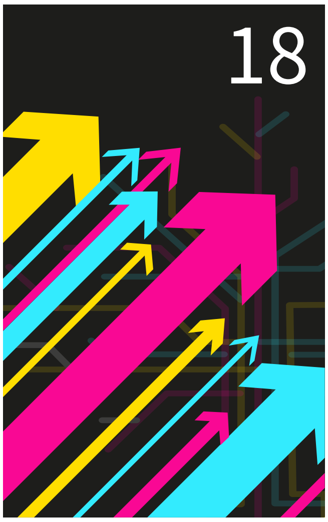
Contents



Daniel **Coatsworth**

Might 10 November 2022 go down in history as the year's turning point for shares?

Investor sentiment has greatly improved as more worries are crossed off the list

There have been several distinct turning points in depressed markets in recent years. Monday 23 March 2020 saw the US Federal Reserve say it would do whatever it took to stop the US economy collapsing from the Covid pandemic. Monday 9 November 2020 saw Pfizer and BioNTech say their Covid vaccine was more than 90% effective.

In both cases, the news triggered a massive rally on the stock market as investors shifted from pessimism to optimism.

Have we just had another significant date for the history books? Thursday 10 November saw shares soar after the latest data showed US inflation was less severe than expected. The US consumer price index rose by 7.7% in October from a year earlier, and down from 8.2% in the previous month. This suggests the US central bank's policy to raise interest rates to ease inflation is working.

US stocks soared on the news including a 7.4% rally in the Nasdaq index. UK shares also fared well, particularly mid-caps where the FTSE 250 jumped 3.9% on the day.

What's interesting is how markets were already moving higher ahead of the 10 November inflation figures. At the time of writing, the FTSE 250 was up 17% from its 12 October low and on the verge of hitting bull market territory (a 20% rise from the low).

One by one the market's worries have been crossed off. In addition to inflation relief, UK political chaos has eased since Rishi Sunak became prime minister. Luiz Inácio Lula da Silva beat far-right incumbent Jair Bolsonaro in the Brazilian presidential election, and the Democrats did better than expected in the US midterms.

Ukraine is making significant progress fighting off Russia, concerns over China potentially invading Taiwan haven't escalated, and China itself is showing signs of easing Covid-related restrictions. Furthermore, there are signs of deflation in China and shipping rates are falling, which is good news for those buying goods from this country.

However, that doesn't mean everything is completely fine for investors. The US Federal Reserve's goal is to bring down inflation and the current rate is still far from its 2% target. Therefore, there is a good chance interest rates will keep going up and we won't see the near-turn pivot in strategy desired by so many people.

Vladimir Putin could try something new in the Ukraine war, possibly nuclear, which would be disastrous for the world. China could easily increase its efforts regarding an invasion of Taiwan, so there are still plenty of issues on the table.

It's probably premature to go full-on bullish regarding the stock market. Some of the biggest rallies happen in bear markets and we have no indication this bear is over yet. However, sticking to a plan that involves putting money into an ISA or pension monthly regardless of what is happening in markets makes sense. You're feeding your investment pot and not trying to time the market. Over time, the benefits should shine through.

Black Friday sales expected to fall as consumers cut back on spending

A lot of people simply cannot afford to splash out this year

Retailers will be hoping that money-off deals at this year's Black Friday event (25 November) will be enough to tempt cash-strapped consumers into buying goods. However, Statista forecasts that UK consumer spending will drop to £8.71 billion over the four days starting with Black Friday, down from £9.42 billion in 2021.

Many households have been cutting back on spending as the higher cost of living means they have less money after paying the bills. Black Friday's discounts could be their chance to buy Christmas presents at cheaper than normal prices.

While that would help retailers shift stock – many of whom are sitting on excess inventories – it won't be good for their profit margins.

Originally a one-day event designed by US shops to boost sales after Thanksgiving, it has morphed into a weeks-long marketing bonanza and spawned other retail 'holidays' like Small Business Saturday and Cyber Monday.

Value of spending over the Black Friday weekend in the UK

	£bn
2018	8.3
2019	8.6
2020	8.0
2021	9.4
2022f	8.7

Table: Shares magazine • Source: Statista. F = Forecast. Covers the four days from Black Friday to Cyber Monday

UK retailers including **AO (AO.)**, John Lewis and **Currys (CURY)** have already been offering special deals for over a week, and firms such as **Dunelm (DNLM)** and **Halfords (HFD)** are promising big discounts with early access for selected customers.

With the strain on UK family finances due to the increase in food prices – which hit a record 14.7% in October according to analysts at Kantar, adding £682 to the average annual grocery bill – and new austerity measures expected in this week's Autumn Statement from the Government, it remains to be seen whether consumers will be in much mood to spend on non-essentials.

US retailers may also be disappointed as consumers have been shopping for the holidays early this year by all accounts. Analysts believe many households have already splurged on big-ticket items after stores found themselves with too much inventory and reduced prices to 'clear the decks' before the holiday season.

E-commerce has remained robust with US shoppers spending over $72 billion online last month according to Adobe Analytics. Household goods like air fryers and mini fridges have been selling well, along with outerwear, electronics, toys and holiday decorations.

In Asia, the world's biggest shopping event – which typically eclipses Black Friday and Cyber Monday – took place on 11 November. Singles Day, also known as Double 11, was launched by Chinese retail giant **Alibaba (BABA:NYSE)** in 2009 as an antidote to Valentine's Day and a means for people not in romantic relationships to indulge themselves.

Sales this year were expected to top one trillion yuan ($140 billion), which while it may sound impressive would represent growth of just 5% on last year's figure which already marked a slowdown from previous years. [IC]

FTX collapse hurts shares in Microstrategy and Argo Blockchain

Bitcoin hits lowest level in more than three years as fears of contagion build in the crypto world

A horror year for cryptocurrencies reached its latest zenith as crypto exchange FTX filed for bankruptcy. This has raised fears over contagion in this nascent asset class and seen investor nervousness grow over other participants in the market.

In what resembled a digital version of a bank run, concern about the financial position of FTX and other firms owned by its founder and, now former, chief executive Sam Bankman-Fried led many customers to try and withdraw funds from the exchange.

This created a big cash squeeze and, after attempts to secure a bailout failed, many were unable to access their money. Filing for Chapter 11 bankruptcy will at least give FTX the chance to restructure its debts as it continues to operate for the time being.

The CEO of Crypto.com Kris Marszalek dismissed speculation that his platform could be next to suffer, offering reassurance via an interview on YouTube that the exchange has a 'very strong balance sheet'. Recent events will only add to clamour for greater regulation of this market.

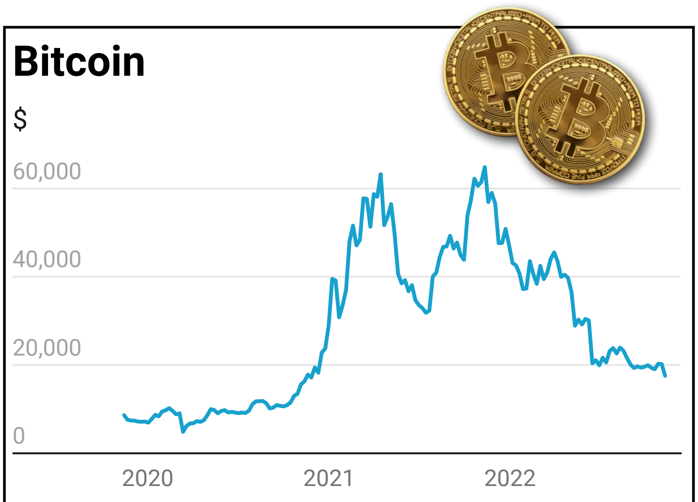


Chart: Shares magazine • Source: Refinitiv

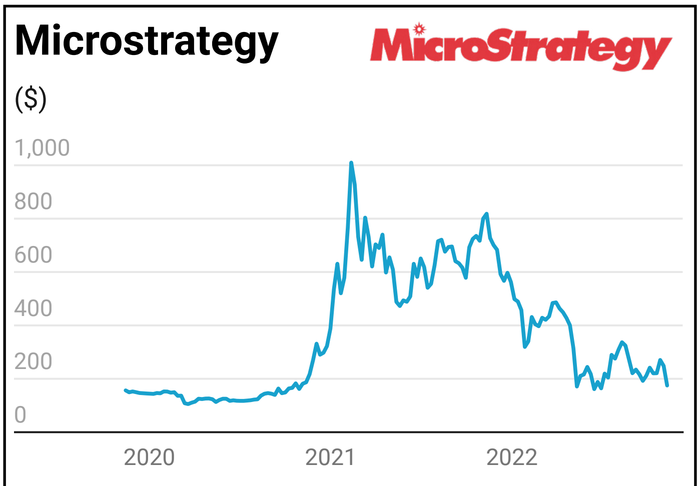


Chart: Shares magazine • Source: Refinitiv

In the wake of the demise of FTX the price of bitcoin fell to levels last seen in October 2020 at less than $16,000. To put this into perspective it traded at an all-time high above $69,000 almost exactly a year ago, with the continued volatility belying claims that it could represent a durable alternative to gold as a store of value.

Analytics software firm **Microstrategy (MSTR:NASDAQ)** has a big investment in bitcoin which has seen it get caught up in the current turbulence. In October it held 130,000 bitcoins acquired at an average purchase price of $30,639.

UK-listed bitcoin miner **Argo Blockchain (ARB:AIM)** extended its share price losses to trade down more than 90% so far in 2022. Bitcoin works on 'blockchain' technology, and a block is a piece of computer code that stores the data for a transaction. It is linked to the existing chain of blocks which acts as a record of all transactions.

Mining bitcoin means verifying transactions and adding new blocks to a blockchain ledger, a complex process which is rewarded with bitcoin. [TS]

Warren Buffett ditches Procter & Gamble for Asian tech group TSMC

Investment in world's leading 'foundry' chipmaker is a first for the legendary investor

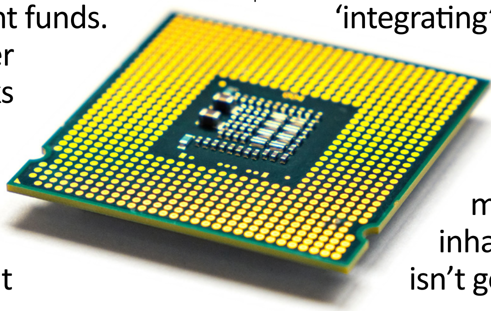
Warren Buffett's investment company **Berkshire Hathaway (BRKB:NYSE)** had sold its stake in US personal products giant **Procter & Gamble (PG:NYSE)** and invested in Taiwanese semiconductor maker **TSMC (2330:TPE)** instead.

TSMC is the world's largest made-to-order chip maker and is expected to generate close to $75 billion in sales this year. It is a popular holding for global and Asia-focused investment funds.

Berkshire's stake, worth just over $4.5 billion at current prices, marks a rare foray by the Buffett-led conglomerate into Asian stocks and into the IT hardware manufacturing sector.

The investment is also significant from a political perspective as it suggests Buffett is confident in Taiwan's future.

In the run-up to the midterm elections the Biden administration had to be seen as tough on China as the Republicans, hence there was a lot of talk of 'defending' Taiwan, but the rhetoric was aimed squarely at the US electorate not the international community.



At the same time, when China talked about 'integrating' Taiwan, fears of it launching a military invasion became vastly overblown.

The bottom line is if President Xi wants to win the hearts and minds of Taiwan's 24 million inhabitants, he knows full well he isn't going to do it militarily. [IC]

Walmart beats forecasts and raises guidance on market share gains

Company announces further $20 billion share buyback plan

SHARES IN US retail giant **Walmart (WMT)** reacted positively to its latest trading update (15 November), climbing 7.5% to $149 pre-market for a year-to-date gain of 3% compared with a loss of 17% for the S&P 500 index.

The firm reported revenues for the third quarter of $152.8 billion, up 8.7% on a headline basis or 9.8% in constant currencies and comfortably ahead of market forecasts of $148 billion.

US sales climbed 8.2% on a like-for-like basis as the firm made further gains in the grocery market, with the Sam's Club cash-and-carry business posting 10% like-for-like growth.

International sales were up 7% to $25.3 billion, driven by double-digit growth at the Mexican subsidiary **Walmex (WALMEX:BMV)**, although the strong dollar took a bite out of overseas revenues.

Adjusted group earnings per share were $1.50, more than 13% above the consensus estimate of $1.32 per share, building on the second quarter's 10% beat and leading the firm to raise its full year operating earnings guidance to a decline of 6.5% to 7.5% from 9% to 11% previously.

In addition, the company announced a new $20 billion share buyback, replacing the existing programme which still had $1.9 billion remaining at the end of September.

President and chief executive Doug McMillon said the company had 'significantly improved' its inventory position and would continue to reduce stocks during the fourth quarter. [IC]

Agricultural sector suppliers continue to harvest tasty gains

The recent softening of commodity prices hasn't put agriculture-related stocks off track

Companies that process crops benefit when drought or wars such as the Russia/Ukraine conflict create shortages in parts of the world.

Prices for food-related commodities including wheat, corn and soybeans remain elevated on a five-year view, though they have softened since Russia agreed for grain exports to resume through the Black Sea.

Against a backdrop of supply shortages and food inflation, select agriculture-related companies are in demand with investors and news flow remains positive.

Shares in German fertiliser supplier **K+S (SDF:ETR)** are up almost 45% year-to-date while tractor maker and agricultural equipment seller **Deere (DE:NYSE)** has harvested a 16% gain.

On a streak of beating earnings estimates is global grains merchant **Archer-Daniels Midland (ADM:NYSE)**, the dividend aristocrat which recently announced (25 Oct) its strongest third quarter profit on record and raised full year earnings guidance off the back of robust demand for grain and oilseeds and tight supplies. CEO Juan Luciano insisted Archer-Daniels Midland is 'well positioned to end 2022 strong, and carry that momentum into 2023'.

On 26 October, American agribusiness **Bunge (BG:NYSE)**, the soybean exporter also involved in food processing, grain trading and fertiliser, lifted its 2022 earnings per share outlook after reporting a strong third quarter performance in its refined and specialty oils business.

Corteva Agriscience (CTVA:NYSE) shares are testing new highs, as the agricultural chemical-to-seed company benefits from farmers seeking to maximise yields at a time of low global grain supplies, and on 3 November the company raised the mid-point of its full year operating EBITDA guidance following a strong third quarter. CEO Chuck Magro said the 'outlook for ag fundamentals is strong' and believes farmers will 'continue to prioritise top-tier technologies to increase productivity on the farm'.

On the UK stock market, agricultural supplies group **Wynnstay (WYN:AIM)** has upgraded profit guidance for the year to October 2022 once again after favourable trading conditions continued in September and October across all core activities.

The £140 million cap, whose farmer customers have more money to spend when milk prices are high, has seen sustained outperformance in its arable business (grain, seed and fertiliser products).

Also trading well is feed, food and fuel distributor **NWF (NWF:AIM)**, while **Carr's (CARR)** has a speciality agriculture division which makes and supplies feed blocks, minerals and boluses containing trace elements and minerals for livestock. [JC]

Soft commodity prices

All lines rebased to 100

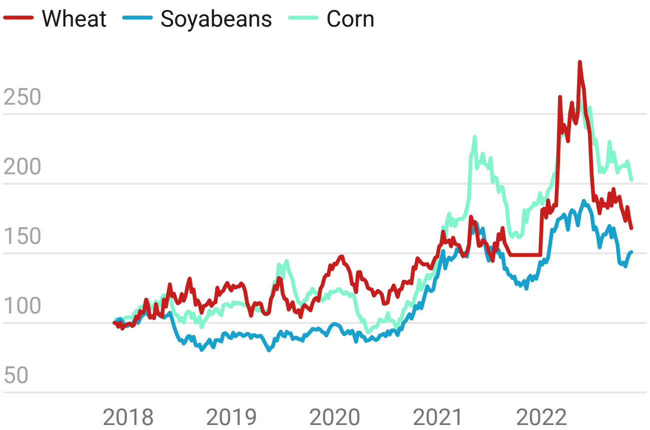


Chart: Shares magazine • Source: Refinitiv

How Energean has been fired up by first gas from Israel and strong prices

'Significant milestone' could mean big quarterly dividends for shareholders

SHARES IN OIL and gas firm **Energean (ENOG)** continue to rise as it benefits from higher energy prices and first gas from its Karish field offshore Israel in October.

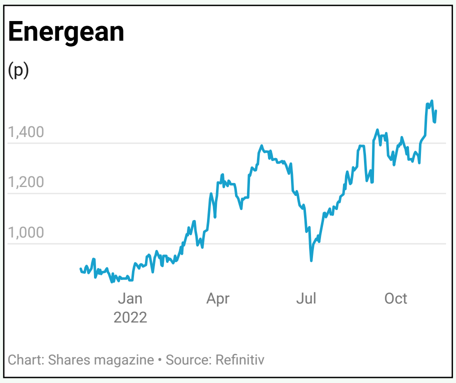
The FTSE 250 constituent is up 68% year-to-date to £14.96 as it has successfully brought the flagship Karish asset on stream.

Berenberg analyst James Carmichael says: 'This is a significant milestone for the company and should drive material growth in production, cash flow and shareholder return over the next 12 to 24 months.'

The initial contracted sales volumes and prices achieved from Karish underpin long-term cash flow forecasts which imply an average free cash flow yield at the current market valuation of more than 20% between 2023 and 2030.

Based on Energean's stated dividend policy it could be paying out as much as $100 million on a quarterly basis once it hits production targets, which would represent a 14% yield. Berenberg estimates production will eventually average around 200,000 barrels of oil equivalent per day.

Inevitably given the field's location there are political and security risks and Lebanese militant group Hezbollah has threatened Karish. The field is situated in waters which are the subject of dispute between Israel and Lebanon. [TS]



Why Tesla's big share price fall isn't just about Twitter

The electric vehicle maker is also facing increased competition

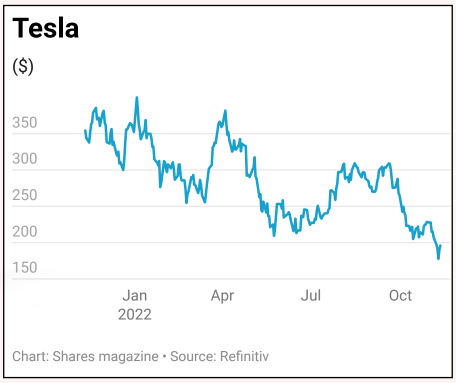
SHARES IN ELECTRIC vehicle maker **Tesla (TSLA:NASDAQ)** recently slipped to their lowest levels in nearly three years after founder Elon Musk sold a big slug of shares in the company to help fund his takeover of social media platform Twitter.

Musk's struggles with Twitter are inevitably grabbing lots of headlines and will only add to investor concern that his focus is being diverted from the day job at Tesla, but there are other reasons why the latter's share price is struggling.

Sentiment towards Tesla, which is recalling more than 40,000 of vehicles in the US because of a potential power-steering problem, has also been affected by analysts downgrading earnings forecasts, a third quarter revenue miss on 19 October and price cuts in China linked to rising competition.

As Berenberg observed in the wake of the third quarter numbers: 'Although Tesla has so far shown its ability and willingness to pass on costs through pricing, it may become less aggressive in the face of competitor model launches.'

While the shares rallied sharply after a lower-than-forecast US inflation reading on 10 November, they are still down 51% year-to-date and the company undoubtedly faces increasing competitive pressures from traditional automotive firms and electric vehicle specialists alike. [TS]



Bill Ackman: why we might see a stock market recovery in late 2023

Pershing Square Holdings' manager talks to Shares' editor about markets and other big issues

Billionaire investor Bill Ackman of FTSE 100 investment company **Pershing Square Holdings (PSH)** believes markets could have a better time in 2023 than in 2022. He says: 'Predicting the market in the short-term is a sucker's game' but believes the latter part of next year could be when stocks pick up.

In a series of exclusive interviews with *Shares*' editor Daniel Coatsworth, Ackman outlined his belief US interest rates could hit 5% in the short term and stay around that level for most of 2023.

'Once the market starts to see inflation taper, they can begin to predict that the Federal Reserve is going to take its foot off the brake a bit and start taking down rates. I think that will be a perceived and probably likely buying opportunity. That's a potential catalyst more towards the end of 2023,' he comments.

Ackman points out that the Ukraine war is still ongoing, energy prices remain high, and the general market backdrop is challenging.

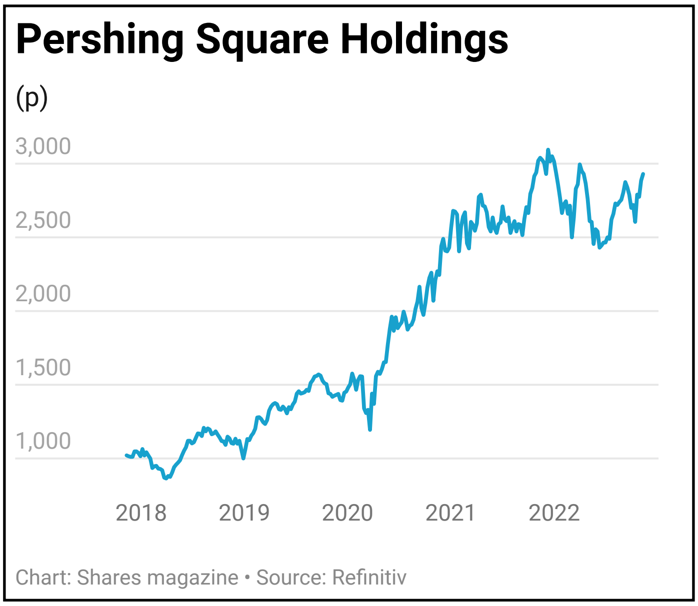


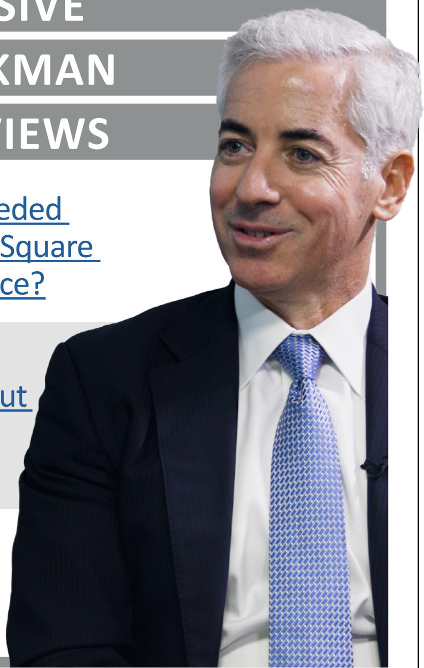
Chart: Shares magazine • Source: Refinitiv

EXCLUSIVE
BILL ACKMAN
INTERVIEWS

VIDEO 1: What's needed to improve Pershing Square Holding's performance?

VIDEO 2: Are you worried about a recession hurting your investments?

VIDEO 3: What's your outlook for 2023?



'We try to find businesses that are resilient, we call them super durable growth companies. Regardless of what's going on in the world, people are going to listen to music which is why we like owning **Universal Music (UMG:AMS).** We think people will continue to renovate their homes and in an interest rate environment where people can't move, they will want to upgrade their own homes and will go to (portfolio holdings) **Home Depot (HD:NYSE)** and **Lowe's (LOW:NYSE)**.'

Pershing Square Holdings has held up relatively well with a mere 2% year-to-date share price decline versus a 17% decline in the S&P 500 and a 28% slump in the Nasdaq. However, its shares trade on a 31% discount to net asset value, much to the frustration of the manager.

Ackman gives his thoughts on what it might take to narrow the discount in this video. In a further video, the manager elaborates on why he believes the consumer-facing stocks in his portfolio should cope with a recession.

Why this Baillie Gifford fund is a really smart way to play Japan

Japanese companies have attractive valuations and strong balance sheets

A swift recovery in Japan's economy from a recent setback should set the scene for a strong showing from attractively valued Japanese stocks and *Shares* has identified an excellent way to play this market.

Steered by an experienced team, **Baillie Gifford Japanese Income Growth Fund (BYZJQH8)** has built up a strong track record since its inception in 2016 as it has benefited from an increasingly shareholder-friendly attitude among Japanese companies.

This was a key plank of the late Japanese prime minister Shinzo Abe's so-called 'Abenomics' approach when he assumed power a decade ago, with firms encouraged to return some of the cash they had been hoarding to investors and improve their corporate governance.

There are risks associated with investing in Japan right now, weakness in yen against the dollar helped push the economy into a surprise contraction in the third quarter. However, the reopening of Asian economies should benefit inbound tourism and Japanese consumer-facing businesses and currency weakness should be a positive for the competitiveness of Japanese exporters.

The Baillie Gifford fund has positioned itself to take advantage of these supportive trends. While the fund's name implies an income focus, the emphasis is very much on dividend growth rather than capturing high dividend yields, reflected in a historic yield of 2.7%.

In common with other Baillie Gifford funds, it pursues a long-term approach with an investment horizon of at least three to five years and more typically five to 10 years. It also deviates significantly from the TOPIX benchmark index.

The fund splits the portfolio into four different buckets: secular growth, growth stalwart, special situations and cyclical growth.

BAILLIE GIFFORD JAPANESE INCOME GROWTH
BUY
(BYZJQH8) 152.3p

Assets: £797 million

Fund manager Karen See characterises secular growth firms as being exposed to long-term growth areas like automation, while growth stalwarts are Warren Buffett-type investments with deep moats. Special situations can be anything from companies sitting on a lot of cash to 'companies with huge potential going through a difficult moment'.

See notes that one of the most well-known companies in the portfolio – video games giant **Nintendo (7974:TYO)** – has moved from the special situations to growth stalwart bucket. She says: 'Nintendo is now better managed, less reliant on console launches which made revenue quite lumpy, and it has one of the greatest collections of characters globally.'

More broadly Japanese firms and households continue to sit on lots of cash relative to their counterparts in the West and this should engender resilience heading into a potential downturn for the economy. The ongoing charges on the fund are 0.62%. [TS]

Baillie Gifford Japanese Income Growth

Chart: Shares magazine • Source: Refinitiv

Kape Technologies is the cheap way to invest in the hot cybersecurity trend

A forward PE ratio of 6.4 looks like growth at an absolute bargain price

We believe the cybersecurity industry looks like a great place to invest for the long-run, and **Kape Technologies (KAPE:AIM)** is an under-the-radar way to do so.

As the number of hacking attacks on government agencies and major businesses surge, digital defence budgets are also rising rapidly, and increasingly consumers are having to think hard about how they protect themselves and their valuable online data.

Kape provides consumer cybersecurity solutions, moving rapidly to expand its suite of privacy and security services since 2016 through acquisitions, including Cyberghost, Intego, PIA and Webselenese for around $300 million combined.

Yet it was September 2021's $936 million purchase of virtual private network group ExpressVPN that promises to be transformational. Alongside bolstering its market strategy and research and development capabilities, Kape has already started realising 'significant' operational benefits, such as back-office cost-savings and leveraging of economies of scale in infrastructure and marketing.

The group has relied on a combination of equity and debt raises to support this M&A, with equity raises include a $354 million placing in September 2021 to partially fund the ExpressVPN acquisition and, just last month, another $222.5 million capital raise to refresh its war chest.

Kape had been looking to raise approximately $100 million to $200 million but investor demand saw it raise more, including money from entrepreneur Teddy Saggi, whose Unikmind trust retained its 55% shareholding. Saggi founded gambling software firm **Playtech (PTEC)**.

Such strong support for Kape will have been helped by compound annual growth of revenue and adjusted EBITDA (earnings before interest, tax, depreciation and amortisation) of 56% and

KAPE TECHNOLOGIES
BUY
(KAPE:AIM) 235p

Market cap: **£1 billion**

83% respectively, according to Shore Capital analysis, since 2017.

Half-year results on 12 September revealed 217% revenue growth to $302.4 million, a 19% increase on a pro forma organic basis, and reiterated the full year outlook for 117% pro forma adjusted EBITDA growth at the midpoint of the guidance range of $166 million to $172 million. Importantly, cash generation remains strong, having reported $352 million of free cash flow in 2021.

Gross margins run at over 90% although return on equity and investment metrics could do with improvement, at 9.6% and 8.7% respectively, according to Investing.com data. The company said in September that it is more confident than ever in its prospects.

A 2023 calendar price to earnings multiple of 6.4, based on Shore Capital forecasts, means the shares are very cheap. [SF]

Chart: Shares magazine • Source: Refinitiv

Ongoing strong growth at ME International remains under-appreciated

Formerly known as Photo-Me, earnings continues to be upgraded yet the shares remain cheap

ME INTERNATIONAL
(MEGP) 103.05p

Gain to date: 27%

SHARES SAID TO buy instant service equipment company **ME International (MEGP)** – previously known as Photo-Me – on 16 June 2022 based on its good growth potential and pricing power which was not reflected in the lowly eight times 2022 price to earnings ratio.

So far, the decision has been vindicated with the shares jumping 27% from the 81.2p entry price. Despite the pleasing gain, the price to earnings multiple has only expanded to 8.9-times, while the consensus analysts forecast for 2022 earnings estimates has gone up by 10%.

WHAT HAS HAPPENED SINCE WE SAID BUY?

In addition to the corporate rebrand, the company has increased full year guidance yet again. For the year to 31 October, the firm now expects revenues to be between £256 million and £262 million, versus previous guidance of £257 million.

Meanwhile EBITDA (earnings before interest, tax, depreciation, and amortisation) is expected to be between £82 million and £85 million, up by 2.5% from the middle point of the prior range.

Management said it continued to see stronger consumer demand for all the group's services while trading in Asia remained subdued due to pandemic restrictions remaining in place for longer.

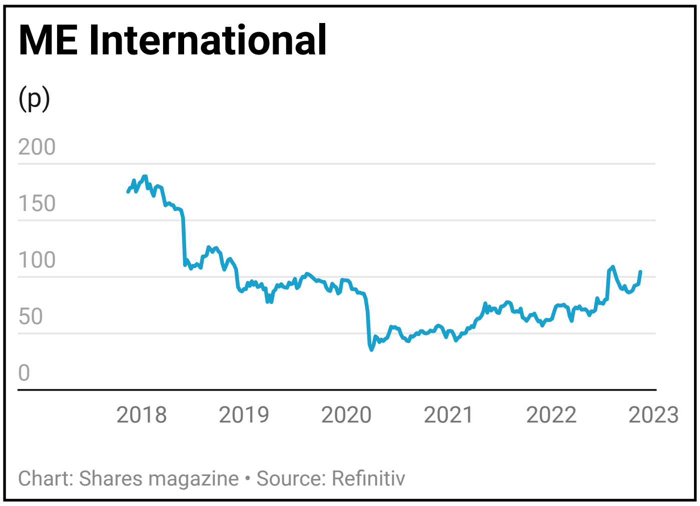
FinnCap analyst Guy Hewitt upgraded his revenue estimate by 4% and his EBITDA estimate by 9% to £84 million while James Wood at Canaccord raised his earnings per share forecast by 12%.

Wood commented: 'We believe the group's strong trading performance demonstrates the resilience and pricing power of the Identification vertical which is attributable to non-discretionary demand for official documentation as well as a return of travel related spend (c.35% of ID revenues).'

WHAT SHOULD INVESTORS DO NOW?

The company's revenues are underpinned by long-term client relationships and multi-year contracts which provide good visibility and strong cash flows.

The low valuation of the shares does not reflect the high quality and growth potential of the business. Keep buying the stock. [MG]



Slump in net asset value at Scottish Mortgage raises some big questions

Some shareholders may be losing patience after recent events

Investors in growth-oriented **Scottish Mortgage Investment Trust (SMT)** seemed to be in forgiving mood last week, sending the shares gently higher despite a slump in returns.

The Baillie Gifford-managed trust saw its net asset value per share slide from £10.22 at the start of March to 842p at the end of September, a return of -15% compared with a 7% fall in the FTSE All-World index.

Although the managers don't give a breakdown of returns, unlike many other funds and trusts, most of the damage came from the company's exposure to biotech and technology.

The top six listed holdings at the end of September – **Moderna (MRNA:NASDAQ)**, **Tesla (TSLA:NASDAQ)**, **ASML (ASML:AMS)**, **Illumina (ILMN:NASDAQ)**, **Meituan (3690:HKG)** and **Amazon (AMZN:NASDAQ)** – which made up 25% of total assets, lost 20% on average over the half.

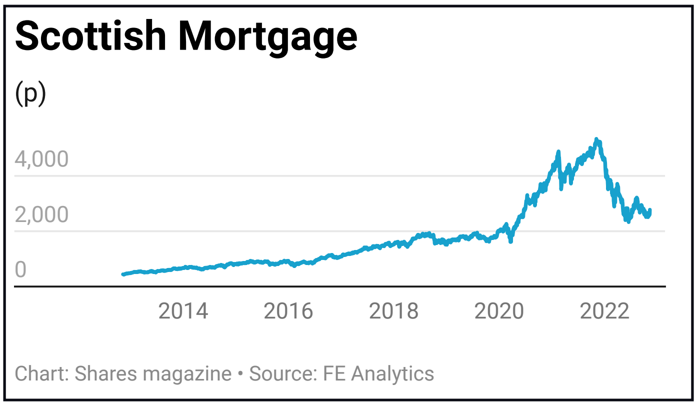
In addition, the trust reduced its holdings in several large Chinese technology companies such as internet group **Tencent (700:HKG)** whose share price slumped 37% during the period.

As usual, the managers maintained their focus on the broader picture: 'Scottish Mortgage's long-term capital appreciation has come from financing and patiently supporting the development of growth companies. It is important at times of stress to remember this founding story: corporate potential has little to do with the cycles of greed and fear in stock markets.'

The trust continues to focus on key global themes such as digitalisation, decarbonisation and the intersection of technology and healthcare.

For that reason, the managers are sticking with therapeutics company Moderna, which lost 23% over the first half and recently posted disappointing results, and electric vehicle maker Tesla, whose shares lost a more modest 9% over the period but faces growing competition from Chinese rivals.

At their lowest point last week, Scottish Mortgage shares had fallen 50% from their late 2021 highs which has been painful for many thousands of small investors.



The last six months have been tough for growth stocks, and as the funds team at Numis observe the short-term outlook for the trust 'will continue to be influenced by investor sentiment towards growth stocks' which while it may have turned positive in the last few days 'will no doubt be choppy'.

Not everyone will agree with the decision to stay invested in stocks such as Tesla, or to cut the trust's Chinese technology exposure just as the country seems to be preparing to lift some of its Covid restrictions and free up the economy.

Over the long term, however, the team have shown the benefits of their 'buy and hold' approach and the faithful will no doubt do the same.

DISCLAIMER: The author owns shares in Scottish Mortgage

By **Ian Conway** Companies Editor

abrdn

The impact of the energy crisis on UK equities

Iain Pyle, Investment Manager, Shires Income PLC

- Energy prices remain elevated and are likely to be the catalyst for a global synchronised recession
- The impact of higher prices is far-reaching. Many companies are facing higher costs, at a time when margins were already being squeezed
- Pressure on margins is likely to increase, as energy costs rise and wage demands increase

The state of the energy market is having a profound effect on the UK corporate sector. Few companies remain unaffected by rising energy prices, with some significant beneficiaries and others facing higher input costs and tighter margins. For Shires Income, it has become an increasingly important factor in our analysis of companies.

There has been some divergence in energy markets in recent months: the war in Ukraine continues to constrain supply, but recession fears have also started to weigh on markets. We believe this may have lulled some investors into believing the crisis may be nearing an end. In reality, energy prices remain elevated and are likely to be the catalyst for a global synchronised recession over the course of the next 12 months.

The impact of the energy market on equities has been profound. Many companies are facing higher costs, at a time when margins were already being squeezed. Energy companies have benefited, particularly those exposed to gas. Utilities are also benefiting from higher power prices, while companies involved in the energy transition

have become more important as governments seek to create energy security.

On the other side, consumer companies have been hit hard. Consumers are facing higher energy bills and have become more cautious as a potential recession looms. That has had a clear impact on consumer demand. There are also companies facing second order effects – higher inflation has pushed central banks to raise rates, which has hurt companies with higher debt. It has also prompted a notable rotation from growth to value by investors.

What happens next?

Governments across Europe have put in place measures to shield consumers from the worst impact of rising energy prices. Even with these defences in place, households have been forced to draw down on any savings buffer they built up during the pandemic. It is also affecting sentiment in the corporate sector. Expectations for new orders have declined and manufacturing has been hit.

It is difficult to see this uncertain backdrop changing significantly. Certainly, Europe has been successful in building up its gas inventories, and, in some places, in curbing demand. This is a better starting point, though there are still risks that prices could spike higher and rationing might be needed, particularly if it is a very cold winter. Prices are likely to settle higher than historic norms.

This should create an ongoing tailwind for the energy sector. Energy companies are already generating strong cash flow, which is allowing them to pay down debt. They have generally been disciplined on capital expenditure and returning cash to shareholders. With the floor under commodity prices higher, we still have a relatively high energy sector weighting in Shires Income.

These companies also have a longer-term tailwind from the move into clean energy trading and renewables, where many have significant investments. This doesn't get a lot of credit from investors today, but is likely to become increasingly important over time. In a tight, disrupted energy market, energy trading becomes increasingly valuable.

Renewables

Renewables are also likely to be longer-term beneficiaries from the energy crisis. The recent events have brought home to governments the need to transition away from conventional fuels, both from an environmental and energy security perspective. There is a good understanding between companies and governments that they need to earn a competitive rate of return to provide infrastructure and clean energy supply. Therefore, renewable companies such as SSE and National Grid have a potentially good pathway of growth.

That said, there are interesting opportunities elsewhere. Good quality retailers with strong balance sheets should emerge from this difficult period with greater market share. Valuations remain very low. In contrast, industrials facing a sharp slowdown in demand and the expiry of their energy hedges at the end of the year should be avoided.

Inflation and interest rates

The shift from a low inflation, low interest rate world, to a high inflation, high interest rate world has been a significant change over the past 12 months. This has prompted a rotation from growth into value and into certain sectors, such as financials.

We have to assume that inflation will continue to weigh on markets. Against this backdrop, we prefer to own quality companies with pricing power. Pressure on margins is likely to increase, as energy costs rise and wage demands increase. We have started to see the 'quality' factor find favour with investors as recession fears have emerged. Companies that are resilient and able to protect their margins during a downturn have found favour with investors.

The energy crisis presents a challenge to all investors, affecting margins across all sectors. With little imminent resolution to the crisis, it is an important factor in our decision-making at Shires Income today. The portfolio is positioned to help ensure that our investors are less vulnerable to the crisis and its secondary effects.

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.

Important Information

Risk factors you should consider prior to investing:

- The value of investments, and the income from them, can go down as well as up and investors may get back less than the amount invested.
- Past performance is not a guide to future results.
- Investment in the Company may not be appropriate for investors who plan to withdraw their money within 5 years.
- The Company may borrow to finance further investment (gearing). The use of gearing is likely to lead to volatility in the Net Asset Value (NAV) meaning that any movement in the value of the company's assets will result in a magnified movement in the NAV.
- The Company may accumulate investment positions which represent more than normal trading volumes which may make it difficult to realise investments and may lead to volatility in the market price of the Company's shares.
- The Company may charge expenses to capital which may erode the capital value of the investment.
- There is no guarantee that the market price of the Company's shares will fully reflect their underlying Net Asset Value.
- As with all stock exchange investments the value of the Company's shares purchased will immediately fall by the difference between the buying and selling prices, the bid-offer spread. If trading volumes fall, the bid-offer spread can widen.
- Certain trusts may seek to invest in higher yielding securities such as bonds, which are subject to credit risk, market price risk and interest rate risk. Unlike income from a single bond, the level of income from an investment trust is not fixed and may fluctuate.
- With funds investing in bonds there is a risk that interest rate fluctuations could affect the capital value of investments. Where long term interest rates rise, the capital value of shares is likely to fall, and vice versa. In addition to the interest rate risk, bond investments are also exposed to credit risk reflecting the ability of the borrower (i.e. bond issuer) to meet its obligations (i.e. pay the interest on a bond and return the capital on the redemption date). The risk of this happening is usually higher with bonds classified as 'sub investment grade'. These may produce a higher level of income but at a higher risk than investments in 'investment grade' bonds. In turn, this may have an adverse impact on funds that invest in such bonds.
- Yields are estimated figures and may fluctuate, there are no guarantees that future dividends will match or exceed historic dividends and certain investors may be subject to further tax on dividends.

Other important information:

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GB-040522-170389-1

SIX UK STOCKS TO BUY NOW

Markets are starting to recover

By **Daniel Coatsworth**, **Ian Conway**, **Martin Gamble** and **Tom Sieber**

UK equities have had a healthy bounce in the past month with the FTSE 100 index advancing 7.6% and the FTSE 250 rallying 16% since 12 October.

The reasons for the sudden about-turn are two-fold – the normalisation of UK government bond yields after they spiked following the political upheaval of the summer and disastrous mini-Budget in September, and generally better-than-expected corporate earnings.

From a low of 2% in August 10-year UK government bond yields jumped to almost 4.5% in mid-October as investors panicked over unfunded tax cuts and the strain on UK finances.

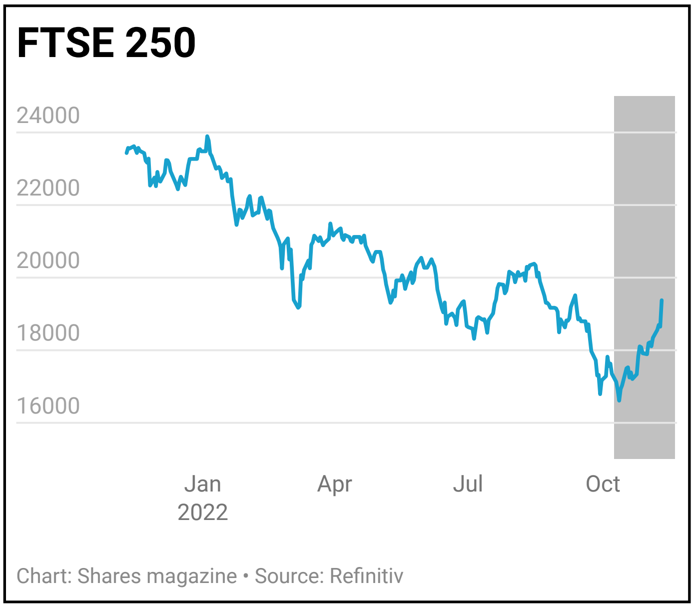
Since then, yields have dropped back to 3.3%, triggering a rally in shares and in particular risky stocks.

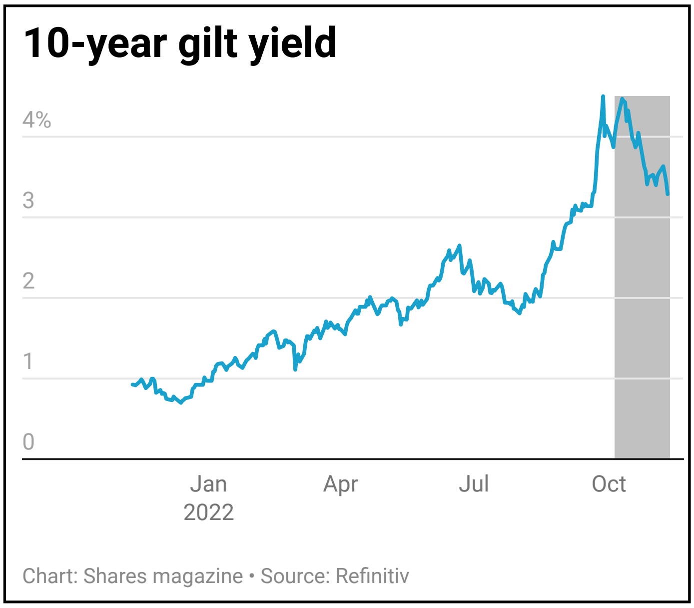
At the same time, while there have been one or two calamities, on the whole company updates over the last month have generally been in line with or slightly better than expectations suggesting UK plc is doing alright.

Weaker than expected US inflation figures have also helped to drive share prices higher around the world.

Big FTSE 100 companies have benefited from

Look how the FTSE 250 picked up as gilt yields retreated





Some of the best performing stocks over past month

Company	Price change (%)
THG	132%
Cineworld	93%
Ocado	87%
Just Eat Takeaway	80%
Wizz Air	66%
Aston Martin	66%
Trustpilot	54%
Carnival	50%
Boohoo	48%
Musicmagpie	43%

Table: Shares magazine • Source: SharePad. Data to 11 November 2022

overseas demand together with a tailwind from the strength of the dollar, while smaller FTSE 250 companies which mostly sell into their home market have shown they are coping reasonably well with a slowing UK economy.

UK stocks are relatively cheap compared with other markets, and many bombed-out stocks have rallied hard but could just as easily fall back again.

Now is the time to look for opportunities to buy good quality companies, with strong fundamentals, at a discount.

Some of the best performing stocks over past month with positive earnings revisions

Name	Price change (%)	EPS Upgrade (%)
XP Power	40.5%	0.1%
Zotefoams	37.3%	6.0%
Jet2	37.1%	0.2%
Watches of Switzerland	37.0%	0.8%
Next Fifteen Communications	34.4%	4.2%
Workspace	31.0%	0.1%
Smiths News	30.4%	1.7%
Hammerson	30.2%	2.2%
Pagegroup	29.3%	2.0%
Morgan Advanced Materials	27.7%	1.6%

Table: Shares magazine • Source: Stockopedia. EPS upgrade refers to next financial year to be reported. Revisions in past month. Price change data 1 month to 11 November 2022.

STABLE OR UPGRADED EARNINGS REVISIONS

A LOT OF companies have just reported their latest results or updated on trading which has given analysts the important information needed to revise their earnings estimates. Investors should look for stocks where earnings estimates are stable or, even better, been revised upwards.

Analysts will have already factored in a more difficult environment for companies and so those which are holding up well or doing better than expected will be the ones catching investors' attention.

Remember that over the longer term, earnings drive share prices so you want to avoid those where earnings expectations are in decline.

Here are three stocks from the list of companies with upgrades to earnings forecasts over the past month, according to data from Stockopedia.

DR. MARTENS (DOCS) 273.8p BUY

Iconic British footwear brand Dr. Martens has seen its shares gain 25% over the past month while analysts have increased their earnings expectations by 5%.

Chart: Shares magazine • Source: Refinitiv

Shares believes the strength of the brand and its inherent pricing power leaves the business well positioned to continue its growth path despite the tough economy, supporting further share price gains.

A comprehensive brand study conducted by the company earlier in the year showed 'that our brand is stronger than ever, with significant growth in awareness, familiarity and recent purchase'.

In a July trading update the company said it had successfully pushed up prices to offset inflation, seen third-party factories return to higher capacity levels after Covid disruption and enjoyed improved shipping lead times.

Dr. Martens maintained full-year guidance to 31 March 2023 for revenues to increase by a mid-teen percentage. Analysts seem more bullish, with the consensus being a 19% increase to £1.08 billion.

In the medium-term Dr. Martens expects the proportion of e-commerce sales to reach 40% of total sales and to achieve a 30% group EBITDA (earnings before interest, tax, depreciation and amortisation) margin.

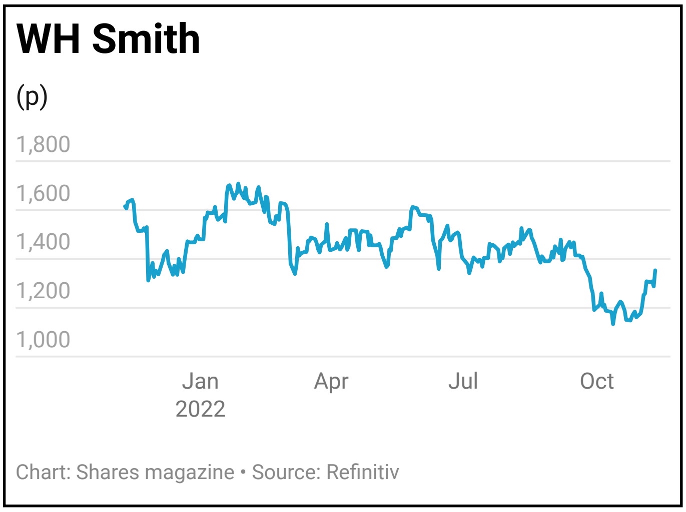
The company anticipates opening 25 to 35 new stores a year in the medium-term as it strives to exploit the brand's global potential.

WH SMITH (SMWH) £13.66 BUY

The resumption of its dividend, guidance that the North American travel operations are about to become more profitable than its UK high street stores, and progress with various digital initiatives show WH Smith is no longer a stuffy old-fashioned retailer.

Many people view it as one of the last men standing on the tired UK high street, but what they miss is how these shops are cash cows. They provide a solid backbone to the business, allowing the company to be quite aggressive with its expansion plans in the travel arm which includes shops in airports and train stations.

The latest results were solid, and management was upbeat about the future. It is doing well in



the UK, US and Australia and there is good reason to suggest its overseas fortunes could be even better as the travel market continues to reopen.

While the shares have been moving higher in recent weeks, they are still down 13% year-to-date. That presents investors with a great opportunity to buy a decent business at an undemanding rating. The shares trade on 16.5 times forecast earnings for the year to August 2023.

Disruption to its travel arm during the pandemic means the past few years' profits and returns on investment look unattractive. It's better to look back pre-Covid to see how WH Smith generated returns on capital employed above 50%. Put simply, the money invested in expanding its business has generated very strong returns.

HALFORDS (HFD) 207.33p BUY

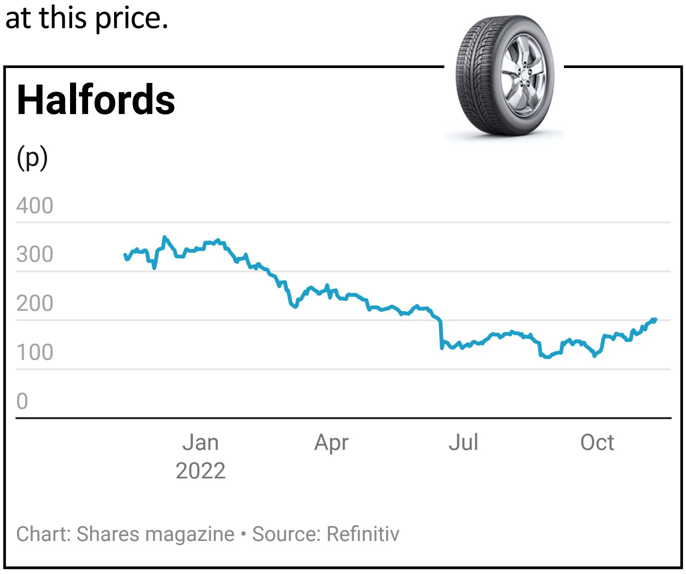
Motor accessories and push bikes seller Halfords has perked up on the stock market since September thanks to a combination of factors.

A cheap valuation and attractive dividend yield caught the attention of value investors. No change to earnings guidance in a 7 September update was a relief to the market, and the acquisition on 5 October of a motoring services business went down well with investors.

Halfords has a strategy to derive more revenue from motoring services, saying they provide more resilient, needs-based revenue streams. While the boom in cycle sales during the pandemic was short-lived, investors can have a lot more confidence in the motoring accessories and services part of Halfords.

No matter the state of the economy, people will need their cars fixed. If anything, they've probably more willing to keep an existing motor running than buy a new one if we're heading into a recession. Also, there isn't the risk that people put off such spending as you can't delay an MOT.

Halfords is by no means a perfect company – there is scope to greatly improve efficiency and have more joined-up systems. Yet investors are being given the chance to invest at a depressed valuation, with the stock trading on 7.5 times forecast earnings for the financial year ending April 2024. The risk/reward is in investors' favour at this price.



STOCKS THAT OFFER GOOD DIVIDEND GROWTH OR A UK BASE RATE-BEATING DIVIDEND YIELD

EVEN THOUGH UK rates are expected to hit or exceed 4% next year, investors can still find plenty of options among stocks and shares that offer higher yields.

The trick is to look for companies which can afford to pay good dividends well covered by earnings and where they've reported resilient trading, so the market won't start to worry about the sustainability of the dividend.

We've looked for more robust dividend stocks where there has been some recent good news, signs of healthy trading and where the valuation is attractive.

SMITHS NEWS (SNWS) 43.1p

Business has picked up sharply for the distributor of newspapers and magazines as the economy has reopened, with sales at rail stations and airports seeing a particularly strong recovery.

Revenues, profits and cash generation are ahead of forecasts while the firm has paid down its debt significantly, freeing up cash for a big final dividend which puts the shares on a yield of 10%.

Contracts for over a third of revenues have been renewed to 2029, providing a good degree of visibility, and discussions will start in the next year or so on the firm's remaining contracts, so the good news should continue.

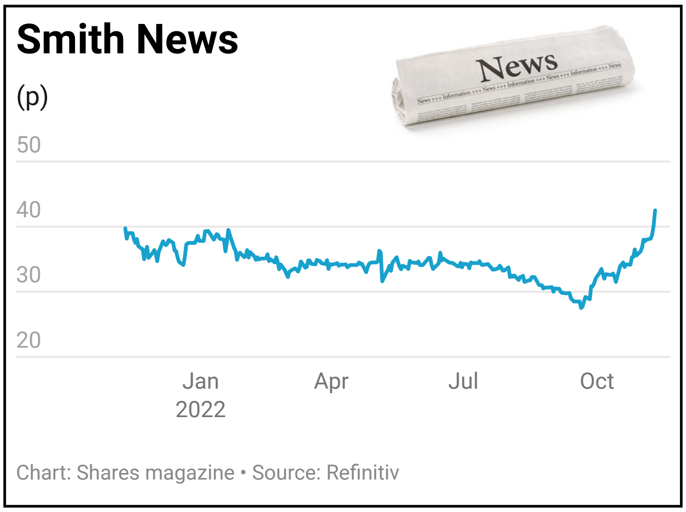


Chart: Shares magazine • Source: Refinitiv

Some of the best performing stocks over past month with dividend yields above 4%

Name	Price change (%)	Yield (%)
UP Global Sourcing	53.1%	4.8%
Liontrust Asset Management	44.4%	6.6%
Appreciate	43.8%	4.3%
Reach	43.7%	6.7%
Abrdn	41.1%	7.8%
XP Power	40.5%	4.4%
Mortgage Advice Bureau	39.2%	4.1%
DFS Furniture	39.0%	5.0%
Jupiter Fund Management	38.9%	6.3%

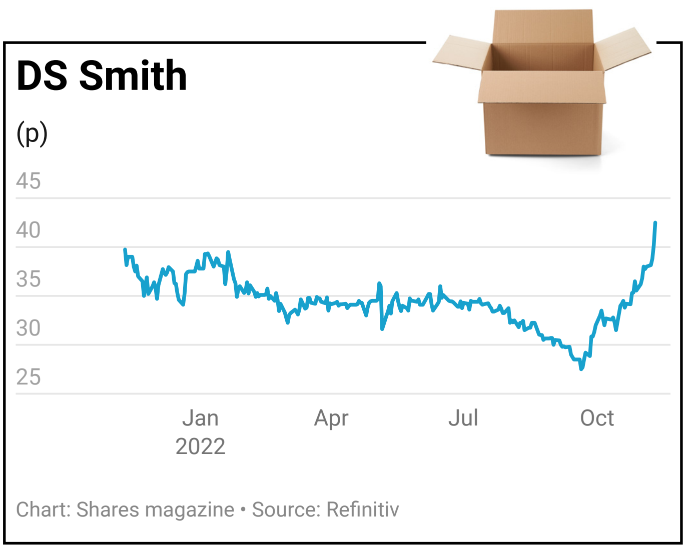
Table: Shares magazine • Source: Stockopedia. Price change data 1 month to 11 November 2022

DS SMITH (SMDS) 314.3p

Packaging firm DS Smith has demonstrated the quality and resilience of its business in spades of late.

It's no surprise in this context that investors have recently snapped up the shares. Even after a 17% return in the past month the stock still trades on just 8.7 times 2024 consensus forecast earnings per share. It offers a 5% dividend yield.

During the pandemic DS Smith and its peers were in big demand as an acceleration in the e-commerce trend drove demand for cardboard boxes. They were also popular with fashionable funds focused on ESG (environmental, social, governance) factors thanks to their commitment to recycling.



Sentiment then weakened as attention turned to the sector's exposure to a deteriorating economic picture and exposure to inflationary pressures.

However, while a 10 October trading update did reveal a slight drop in volumes DS Smith pointed to full-year performance ahead of expectations as it demonstrated pricing power and a good handle on costs.

It would be wrong to suggest there are no risks to the outlook – including news of potential strike action around pay by members of the GMB union working at the business. However, these look more than reflected in the current valuation and investors happy with the risks should take advantage and buy the shares.

UP GLOBAL SOURCING (UPGS) 143.5P

The kitchenware and homeware maker is going from strength to strength with its expanding portfolio of familiar household brands and new products.

Sales are split between UK supermarkets, international markets and online, all of which are growing between 20% and 30%, and the firm has its finger on the pulse as shown by the runaway success of energy-saving products such as slow cookers and air fryers.

By investing in automation to improve productivity and product quality the firm is adding value to its offering and building yet another moat around its business, separating it from competitors. An approximate 5% dividend yield is attractive.

STOCKS THAT HAVE GONE UP WITHOUT POSITIVE EARNINGS REVISIONS

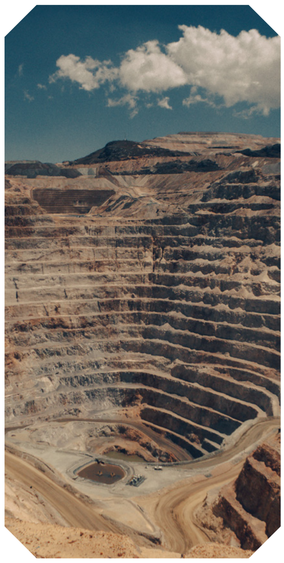
IT'S EASY TO get excited about UK stocks going up and assume it's all based on good news. However, there are quite a few stocks that have moved higher over the past month despite having their earnings forecasts downgraded in the same period.

In such situations, shares might struggle to stay higher unless they were supported by positive fundamentals. The risk is that such stocks would soon fall back in the absence of good news. Here are two relevant stocks to avoid.

Some of the best performing stocks over past month with negative earnings revisions

Name	Price change (%)	EPS downgrade (%)
Synthomer	48.5%	−10.7%
Liontrust Asset Management	44.4%	−6.0%
Reach	43.7%	−4.1%
DFS Furniture	39.0%	−38.1%
Jupiter Fund Management	38.9%	−6.1%
Lendinvest	35.5%	−21.1%
Currys	30.4%	−4.9%
Atalaya Mining	28.8%	−20.6%
ASOS	28.5%	−31.3%
Alpha FX	28.2%	−44.1%

Table: Shares magazine • Source: Stockopedia. EPS downgrade refers to next financial year to be reported. Revisions in past month. Price change data 1 month to 11 November 2022



RESTAURANT GROUP (RTN) 36.48p

Frankie and Benny's and Wagamama owner Restaurant Group has seen its shares jump 14% over the last month although year-to-date they have lost around two-thirds of their value.

Restaurant Group has done a good job of mitigating increased costs, having hedged its utility costs out to fiscal 2024. In addition, the firm has reduced interest rate exposure by arranging a cap on £125 million of gross debt from November 2022.

Despite the business showing resilience with like-for-like sales growth ahead of the market, the pressure on households' budgets and consumer spending is likely to intensify. That raises the risk that families will switch from a trip to Restaurant Group's outlets to a cheaper experience like **McDonald's (MCD:NYSE)**.

Shares believes it would be wise to avoid the shares given heightened risks of a consumer slowdown and persistent downward earnings revisions.

Over the last year analysts have reduced their earnings forecasts for 2022 and 2023 by 20% and 50% respectively.

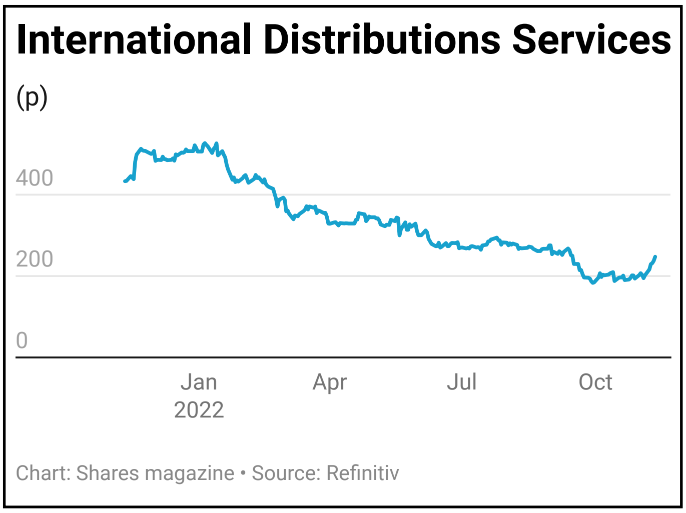
INTERNATIONAL DISTRIBUTIONS SERVICES (IDS) 246.07p

Given at their 2022 nadir shares in Royal Mail owner International Distributions Services had fallen by more than two thirds it's only natural they have recently attracted bargain hunters, with the stock jumping nearly 19% over the past month.

However, there's little in its operational performance and earnings profile to suggest this is anything other than a value trap.

The company's strained relationship with its workforce is creating huge problems and while strikes in mid-November were called off, there is still a planned walk-out over the busy Black Friday and Cyber Monday events.

The only potential catalyst for the shares is a demerger of its more robust GLS international parcels division but investors can have no certainty over when or if that will come.

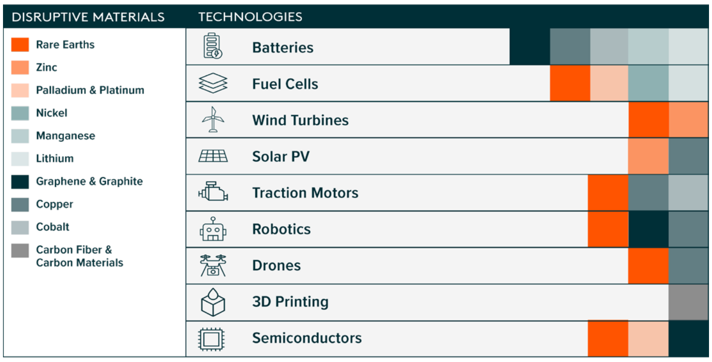


The Case for Disruptive Materials

The world is rapidly embracing digital and clean technologies that can help slow climate change, improve productivity, and connect millions of people around the world. Behind these disruptive technologies are many essential inputs like metals, minerals, and materials. Without them, these technologies would not exist as we know them.

Rare earth materials include nickel, lithium, copper, graphene and graphite, cobalt, manganese, palladium and platinum, zinc, as well as carbon fibre to name a few. These commodities are critical but often unheralded basic ingredients fuelling the advancement of modern technologies. In the current economic environment, disruptive materials stand out as key drivers of long-term growth in the clean energy and digital transition.

RARE EARTHS MATERIAL TO TECHNOLOGY RELATIONSHIP CHART
Source: Global X ETFs.

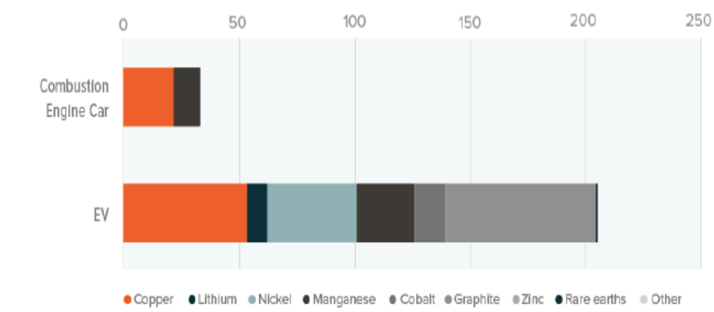


A SUPERCYCLE ERA FOR DISRUPTIVE MATERIALS

As economic conditions change, most cycles, or fluctuations in supply and demand for materials, tend to last anywhere from a few months to a few years. Supercycles, on the other hand, occur when prices rise above trend for extended periods of time, often decades long.

Historically, rapidly growing demand combined with persistent and insufficient supply have created the conditions necessary to spark a supercycle. The simultaneous emergence of several game-changing technologies that have been, and continue to be, heavily adopted could create similar conditions for supercycles in specific materials. We've started to see this in the ongoing transition from internal combustion engine (ICE) vehicles to electric vehicles (EVs) which is poised to be a significant driver of demand for materials like lithium, graphite, copper, nickel, cobalt, and manganese. An EV requires six times more of these materials than a traditional ICE.[1]

DISRUPTIVE MATERIALS USED IN EVs VS. ICE VEHICLES (KG/VEHICLE)
Source: IEA, May 2021.



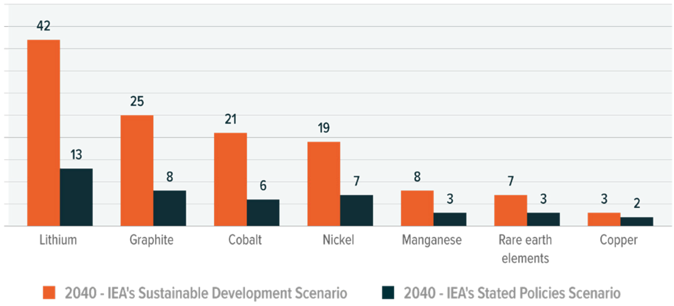
Other clean technologies such as wind turbines and electric motors require rare earth minerals to manufacture permanent magnets such as neodymium, praseodymium, terbium and dysprosium.[2] Copper also continues to gain importance because of its properties that make it a reliable conductor of electricity and heat, and resistant to corrosion. Solar power generation, for example, requires about 5 kilogrammes of copper per kilowatt, roughly twice that of conventional power generation.[3] Given that copper is much cheaper than precious metals with similar electrical conductivity, it is frequently the metal of choice for the generation, transmission, and distribution of electricity. It is also a key component of renewable energy systems and data transmission in the telecommunications industry, including internet services and cable wiring.

Graphene's use in end-markets like automotive & transportation, aerospace, electronics, and construction is expected to grow too. Often described as a wonder material, graphene is the thinnest and strongest material known, being 100 times stronger than the toughest steel.[4] Graphene has a myriad of use cases, including quantum computing, sensors, transistors, and other electronic components.

Carbon fibre provides greater strength, stiffness, heat resistance, and durability than other 3D printed materials such as thermoplastics.[5] Today, approximately 30% of all carbon fibre is used in the aerospace industry because of its extraordinary strength-to-weight ratio.[6]

Platinum has also become a vital material for the electronics industry, particularly for hard disks. It is additionally foundational for hydrogen fuel cells, as it is used as the catalyst that separates hydrogen into protons and electrons, which then generate an electrical current.[7]

ESTIMATED DISRUPTIVE MATERIALS GROWTH BY 2040 (GROWTH MULTIPLES RELATIVE TO 2020)
Source: IEA, May 2021.



QUANTIFYING THE OPPORTUNITY

Climate change and clean technology initiatives have ignited many of the key demand drivers for disruptive materials. Renewable energy sources continue to gain on fossil fuel-based sources as they become more affordable. We expect to see continued adoption, driven by electrification, economies of scale, and climate action.

Today, the disruptive materials theme is in its early stages amid structurally changing demand drivers for certain raw components. Several companies across the Energy and Materials sectors are looking to enhance their exposure to the space by buying mines, land, processing capabilities, and established companies involved in disruptive materials. BP, one of the world's largest oil & gas producers, expects to become net zero by 2050 or sooner, leveraging renewables, biofuels, and hydrogen.[8]

As companies move further into disruptive materials, we expect revenue profiles to shift significantly. According to one estimate, revenue from disruptive materials could increase five-fold by 2040, reaching over $250 billion, while mining coal revenues could decline by 59%.[9]

LOOKING AHEAD

We believe the disruptive materials theme is an overlooked area in a decades-long shift towards digitalisation and clean energy. As technology continues to play an increasingly important role in all aspects of our lives, the fundamental ingredients for technology hardware are likely to become more and more critical. Given the physical limitations of mining, producing, and enhancing materials however, we believe demand could structurally outstrip supply, resulting in a targeted supercycle and rising prices. Investors with exposure to Clean Technology, Electric Vehicles, and/or Technology Hardware may be wise to consider upstream exposures to the disruptive materials-related activities as well in an effort to gain broader exposure to the ecosystem of companies that may benefit from the rise of several emerging technologies.

The Global X Disruptive Materials UCITS ETF (DMAG LN) seeks to invest in companies producing metals and other raw materials that are essential to the expansion of disruptive technologies, such as lithium batteries, solar panels, wind turbines, fuel cells, robotics, and 3D printers. Targeted materials include companies involved in the exploration, mining, production and/or enhancement of Rare Earth Materials, Zinc, Palladium & Platinum, Nickel, Manganese, Lithium, Graphene & Graphite, Copper, Cobalt & Carbon Fibre.

Capital at risk. The value of an investment in ETFs may go down as well as up. Prospectuses and Key Investor Information Documents (KIIDs) for this ETF is available in English at https://globalxetfs.eu/funds/dmat.

INTERESTED IN LEARNING MORE? EXPLORE THE FULL-LENGTH ARTICLE AND SUBSCRIBE TO UPDATES.

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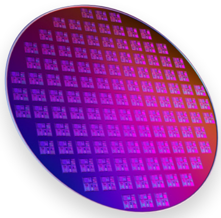
Brighter outlook for chip equipment giant ASML triggers share price rebound



Dutch company dominates lithography technology used to make microchips

Dutch microchip equipment maker **ASML (ASML:AMS)** has dished out some good news for investors. Earnings forecasts have been upgraded and a €12 billion share buyback programme is planned, news of which sent the share price surging nearly 15%, its biggest one-day gain since 2002.

The company now expects revenue of €30 billion to €40 billion by 2025, up from a previous estimate of €24 billion to €30 billion. The company's 2021 sales totalled €18.6 billion.

ASML said it expects sales to continue growing for years to come, with a sales target of €44 billion to €60 billion by 2030.

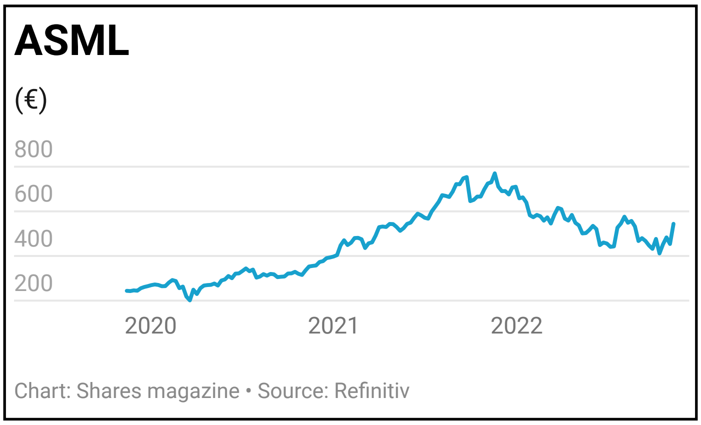
'While the current macro environment creates near-term uncertainties, we see longer-term wafer demand and capacity showing healthy growth,' said the Eindhoven-based company and Europe's largest semiconductor equipment producer.

The stock's rally coincided with the PHLX Semiconductor index jumping 7.7%, with all 30 components gaining ground, while the S&P 500 surged 5.5% in the wake of weaker than expected US inflation data.

ASML dominates the market for lithography systems which are large machines used to map out the circuitry of semiconductors. It has been caught in the crossfire of a battle between the US and China to control semiconductor manufacturing technology.

The €228 billion business had been pressured by Washington to withhold its state-of-the-art EUV extreme ultraviolet technology from Chinese customers amid growing hostility between the US and China.

'Based on our initial assessment, the new restrictions do not amend the rules governing lithography equipment shipped by ASML out of the Netherlands and we expect the direct impact on ASML's overall 2023 shipment plan to be limited,' ASML's president and chief executive officer Peter Wennink said on 19 October 2022.



Major ASML customers include **Intel (INTC:NASDAQ)**, **Samsung (005930:KS)**, **Taiwan Semiconductor (2330:TPE)** and **Micron Technology (MU:NASDAQ)**, microchip manufacturers which have all announced big plans for increased chipmaking capacity in the US over the past year.

ASML said it expects to expand production of its flagship EUV extreme ultraviolet machines, which cost about €200 million each, to 90 annually from around 60 at present, by 2026, and 600 DUV deep ultraviolet systems and 20 high-NA EUV systems.

This demand tailwind helped drive new orders to a record €8.92 billion in the three months to 30 September 2022, of which €3.8 billion was for EUV machines. Gross profit margin expanded from 49.1% to 51.8%.

The recent pick-up in ASML's share price will be welcomed by shareholders after a weak stock performance earlier this year.

By **Steven Frazer** News Editor

RUSS MOULD
AJ Bell Investment Director

History shows US stocks do well in the third year of a presidential term

This suggests 2023 could be a much better year for investors

The rapturous response offered by equity and bond markets to a lower-than-expected US inflation print last week (10 Nov) only served to reinforce the importance of the debate over whether or when the Federal Reserve and other central banks will pause or pivot on monetary policy.

The mere whiff of an easing in the rate of inflation is prompting speculation that central banks will swiftly take the opportunity to stop hiking rates and start cutting them again, so they can stave off (and do not get any blame for causing) a recession.

After a dismal 2022, when share prices have struggled and bond prices have been hammered, it is easy to see why markets are keen to latch on to any good news they can find. Investors with exposure to US assets will be particularly relieved as, at the time of writing, the price of the benchmark US 10-year Treasury is down by 19% in 2022 and the S&P 500 is down by 17%.

But investors will also be assessing the US political situation, for two reasons. First, the results of the mid-term elections may not be known until December, once the run-off for the Senate seat for Georgia takes place. Second, the US stock market has an uncanny habit of performing strongly in the third year of a presidential term – and in this electoral cycle, that means 2023.

POLLING POWER

Using the Dow Jones Industrials as a benchmark, the US stock market has risen by an average of 16.2% in the third calendar year of a presidential term across 18 presidencies going back to Harry Truman in 1948-1951.

This compares to the average single-digit percentage gains generated during the first, second

Dow Jones Industrials has, on average, done best in the third year of a presidential term

	Year 1	Year 2	Year 3	Year 4	Term
Average - all	7.3%	5.2%	16.2%	5.3%	38.2%
Average - Democrat	**13.8%**	**1.3%**	**14.1%**	**10.3%**	**46.4%**
Average - Republican	**1.4%**	**8.7%**	**17.9%**	**0.9%**	**26.7%**

Table: Shares magazine • Source: Refinitiv data. Capital returns in dollars. Covers period from Harry Truman (1948-1951) to first two years of Joe Biden (2021 to date).

and fourth and final years of a presidency.

The only year when the 30-stock Dow fell during the third year of a presidency was in 2015, during Barack Obama's second stint in the White House.

The theory seems to be the incumbent president starts to pull out the economic stops and get the

Dow Jones Industrials has, on average, done best in the third year of a presidential term

Calendar year	Name	Party	Year 3 return from Dow Jones	House Year 3	Senate Year 3
1975	**Gerald Ford**	Republican	**38.3%**	Democrats	Democrats
1995	**Bill Clinton**	Democrat	**33.5%**	Republicans	Republicans
2003	**George W. Bush**	Republican	**25.3%**	Republicans	Republicans
1999	**Bill Clinton**	Democrat	**25.2%**	Republicans	Republicans
2019	**Donald Trump**	Republican	**22.3%**	Democrats	Republicans
1955	**Dwight Eisenhower**	Republican	**20.8%**	Democrats	Democrats
1991	**George H. W. Bush**	Republican	**20.3%**	Democrats	Democrats
1983	**Ronald Reagan**	Republican	**20.3%**	Democrats	Republicans
1963	**Lyndon Johnson**	Democrat	**17.0%**	Democrats	Democrats
1959	**Dwight Eisenhower**	Republican	**16.4%**	Democrats	Democrats
1967	**Lyndon Johnson**	Democrat	**15.2%**	Democrats	Democrats
1951	**Harry Truman**	Democrat	**14.5%**	Democrats	Democrats
2007	**George W. Bush**	Republican	**6.4%**	Democrats	Democrats
1971	**Richard Nixon**	Republican	**6.1%**	Democrats	Democrats
2011	**Barack Obama**	Democrat	**5.5%**	Republicans	Democrats
1979	**Jimmy Carter**	Democrat	**4.2%**	Democrats	Democrats
1987	**Ronald Reagan**	Republican	**2.3%**	Democrats	Democrats
2015	**Barack Obama**	Democrat	**(2.2%)**	Republicans	Republicans
2023	**Joe Biden**	Democrat	**?**		
	Average		**16.2%**		
	Average - Democrat		**14.1%**		
	Average - Republican		**17.9%**		

**John F. Kennedy assassinated in November 1963 and replaced by Lyndon Johnson **Richard Nixon resigned August 1974 and replaced by Gerald Ford*

RUSS MOULD
AJ Bell Investment Director

economy firing on all cylinders before they go for a second term, or at least try to lay the foundations for their successor's campaign for the White House.

The Republicans are still hoping the mid-term elections give them control of both the House of Representatives and the Senate, but even then, history does not suggest such an impasse is seen as a negative outcome by investors in US equities.

Four of the six best third years for capital returns from the Dow came when the president, in the form of Richard Nixon, Bill Clinton (twice), Dwight Eisenhower and George W Bush, had to confront both a House of Representatives and a Senate that were under control of the opposition party.

Indeed, financial markets may welcome such checks and balances, in the view that any rash or egregiously foolish policies will be blocked by a logjam on Capitol Hill.

PAUSE OR PIVOT

However, politics alone is unlikely to shape the fortunes of the Dow Jones and America's other leading equity indices, as the backdrop to the best (and worst) returns from the third year of a presidency suggests.

The 1975 bonanza under Nixon's successor, Gerald Ford, came after the market collapse of 1973-74, while the surge under Bill Clinton in 1995 followed the Greenspan interest rates shock and mid-cycle growth pause of 1994.

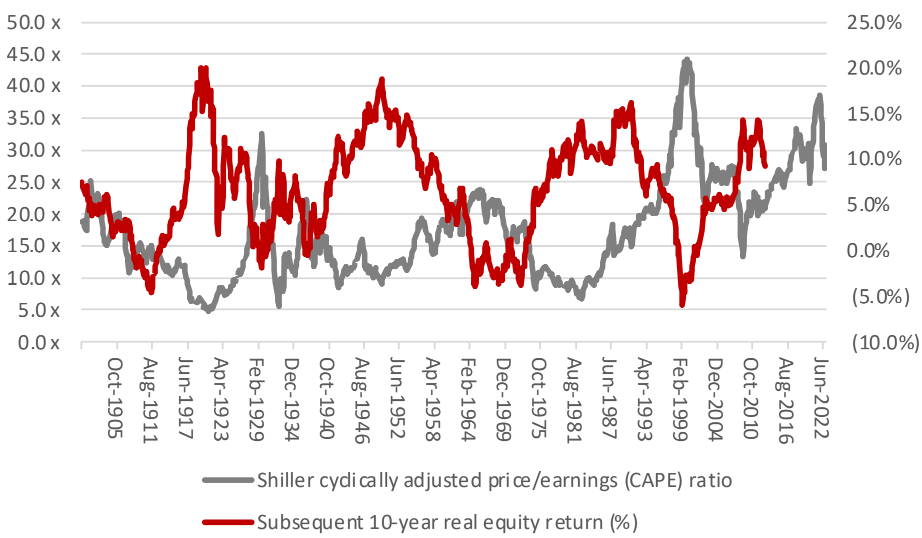
In 2003 under George W Bush, the US was emerging from the wreckage of the technology bubble bust of 2000-2002 while in 1999 that bubble was expanding rapidly during the final half of Clinton's second stint in office.

On the downside, Jimmy Carter's third year was dogged by a fresh oil shock and another surge in inflation after the fall of the Shah of Iran, while the Black Monday crash of 1987 took the wind out of the sails of Ronald Reagan's second term. US stocks fell for the only time during a third year of a presidency under Barack Obama in 2015. Global growth worries, after the bursting of a bubble in Chinese equities, Greece's debt default and what proved to be a temporary halt in quantitative easing in the US combined to hold back the Dow and buck history at the same time.

Investors will therefore have to keep a close eye on events in Washington, but an even closer one on inflation, interest rates and corporate earnings growth, as well as valuation, which remains the ultimate arbiter of investment return. After the 1973-74 collapse and 1994's stumble, US equities looked good value, at least with the benefit of hindsight, and unfortunately that may not necessarily be the case right now, even after 2022's US stock market falls.

According to Robert Shiller's cyclically adjusted price/earnings CAPE ratio, another major US index, the S&P 500, is still trading on more than 27 times earnings, a valuation multiple that has been historically commensurate with market tops and not market bottoms.

Shiller CAPE suggests US equities are still expensive relative to their history



Source: http://www.econ.yale.edu/~shiller/data.htm

US small caps: a savvy way to invest in a robust American economy

Why the turn away from globalisation and a strong greenback could spark gains for US-listed smaller companies

Amid all the current turmoil the US economy, thanks in part to its relative energy independence, could fare better than its G7 counterparts.

Often when people look to invest in the US they focus on the mega-caps but it's actually the domestic-oriented small caps which look particularly well placed.

A new era of deglobalisation, inflation and rising interest rates is leading to a domestic focus and could provide opportunities for this part of the market. Columbia Threadneedle Investments' head of US equities, Nicolas Janvier notes small caps have outperformed in previous rate hiking cycles.

WHY THERE'S BEEN A SHIFT IN THE MARKET

Janvier points out that the 10 year-plus period of globalisation was tailor-made for the leviathans at the top of the S&P 500 riding the global technological wave – think **Amazon (AMZN:NASDAQ)**, **Alphabet (GOOGL:NASDAQ)**, **Apple (AAPL:NASDAQ)** and **Microsoft (MSFT:NASDAQ)**.

However post-pandemic and now with the Russia/Ukraine conflict, 'we have begun to see the emergence of a new environment: one of deglobalisation, rising prices, persistent and high inflation, rising interest rates and recession,' says Janvier.

His observation is the global connections built up over the past few decades, particularly in food chains and energy supplies within Europe, are becoming problematic and a reliance on other countries, 'particularly Russia for your gas, is not desirable.'

Yet the US, where the Federal Reserve is raising rates to combat inflation, stands a little bit apart from this situation. It has relative energy security due to its high domestic production levels, and it doesn't import as much food as Europe.

'It is, however, still experiencing rising rates and could well face recession, but it is showing resilience,' says Janvier.

The US consumer also has a 'huge store' of spending power, notes Janvier, driven by the $5 trillion Covid-19 stimulus package which was designed to shield households and businesses from the pandemic shock.

IN A SWEET SPOT

'Right now, US small caps are in quite a nice sweet spot for a couple of different reasons,' says Janvier's Columbia Threadneedle colleague and US fund manager Andrew Smith.

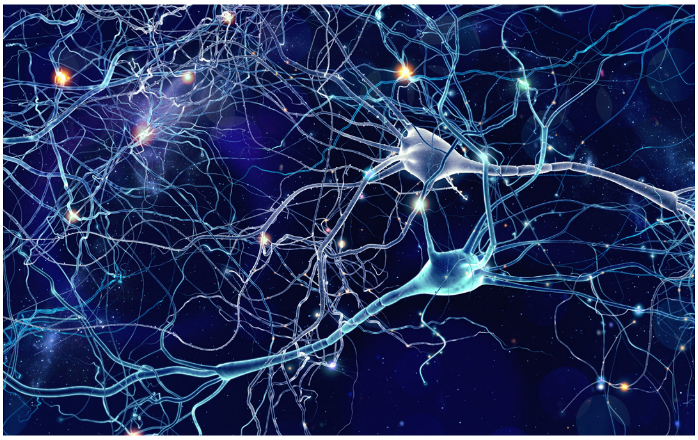
He notes they are much more inherently leveraged to the domestic economy. 'If you look at the median breakdown of where revenues are sourced from, on average small caps are 90% to 100% domestic revenue, whereas the large caps are international companies.

'In a situation where the US should hold up better than the rest of the world in a growth sense, then small caps should stand to do well,' he adds.

Jon Brachle, one of the managers of investment trust **JPMorgan US Smaller Companies (JUSC)**, points out the S&P 500 gets approximately 40% of its revenues from overseas compared to the Russell 2000's 20%. 'US small caps are much more of a domestic play, with around 80% of revenues coming from the domestic market.'

Despite some recent weakness in the dollar, the greenback remains strong against other currencies and dollar strength is a 'huge headwind' for large cap overseas earners according to Smith, because 'when they translate their revenues back into dollars they lose a lot on the earnings. Being more domestic, small caps are more protected from the strong dollar effect, whereas international companies are feeling that a lot more and it is starting to show in earnings reports.'

Smith explains small caps tend to do well in times when borrowing costs are going up as rising rates 'tend to be reflective of health in the underlying economy'. Inflation tends to go up when demand is strong and 'even though we are seeing a slowdown right now, we've had a very strong US economy. We're thinking just a shallow recession and then a quick acceleration out of that next year and beyond.'



Best performing US smaller companies ($500 million to $5 billion market cap) over 5 years

Company	Share price change (%)
Xenon Pharmaceuticals	1460%
Tandem Diabetes Care	1460%
Digital Turbine	1060%
Axsome Therapeutics	997%
Calix	992%
Fulgent Genetics	988%
Cassava Sciences	952%
Vertex Energy	836%
Centrus Energy	825%
Arrowhead Pharmaceuticals	821%

Table: Shares magazine • Source: SharePad. 15 November 2022

The well-regarded Cormac Weldon, manager of **Artemis US Smaller Companies (BMMV576)**, finds it interesting that even in an environment where interest rates are rising and earnings growth has slowed significantly, capital expenditure is 'up 20% this year' and domestic companies have contributed significantly to and benefited from that trend.

'We are entering a period of what we expect to be higher interest rates. Weaker companies only kept alive by the oxygen of low interest rates will start to suffer. We prefer good, strong businesses that can gain market share as more indebted, weaker competitors fail.'

WHAT ARE FUND MANAGERS BUYING?

Investors can access the asset class through dedicated funds such as **Brown Advisory US Smaller Companies (BASC)**, the Chris Berrier-managed trust whose 12.3% discount to net asset value might tempt bargain hunters.

Berrier is bullish about **Bentley Systems (BSY:NASDAQ)**, an industrial software company originally bought and sold previously on its initial public offering (IPO). Since then, Berrier has been waiting for the stock to decline toward his buy range and the recent sell-off in software moved it into the upper end of his purchase band. Berrier views this as 'a great opportunity to get access to a high-quality company that we hope will reward our investors over the long term'.

Artemis US Smaller Companies' Weldon says the strong dollar has been a headwind for many larger companies but less so for smaller businesses that are domestically focused. 'In that sense investing selectively in small caps has been a way to play the tougher US economy without currency being a problem.'

He has recently been buying so-called 'off-price retailer' **Burlington (BURL:NYSE)**, which buys excess inventory from other retailers cheaply and sells it on to price-sensitive customers.

Weldon says Burlington has 'a great opportunity to increase profitability over the next number of years as freight costs plunge, supply chain difficulties diminish and there is more and more excess inventory' and points out the strong greenback has enabled Burlington to purchase inventory overseas at a cheaper price too.

Weldon's most recent purchase is housing industry building materials provider **Builders FirstSource (BLDR:NYSE)**.

'Rising interest rates have hammered the housing market and it is trading cheaply,' he explains. 'Over the next couple of years we believe there will be a housing recovery and in the meantime, this business is interesting because it provides computerised pre-cut timber framing that reduces the need for skilled joiners on site, which is helpful in a tight labour market.'

A fund which looks to blend growth and value is the Nicolas Janvier-managed **CT American Smaller Companies Fund (B8358Z8)**. 'We don't want all our returns to be driven by just hugging a factor,' explains Smith. 'We'd rather just drive it from the bottom-up stock selection which is where we feel we have an edge.' The focus is on 'stocks where we are seeing improvement in their fundamental characteristics like improving market share, profits, return on invested capital, free cash flow that is underappreciated in the valuation right now.'

Top 10 holdings include **WillScot Mobile Mini (WSC:NASDAQ)**, a portable modular storage company seeing underappreciated synergies following a merger. The Arizona-headquartered company also has 'good leverage to construction, which is still having a good boost in the US', and crucially in this inflationary environment, possesses pricing power.

Janvier and Smith also invest in cemeteries and funeral homes operator **Carriage Services**

Annualised performance - all rising rate months

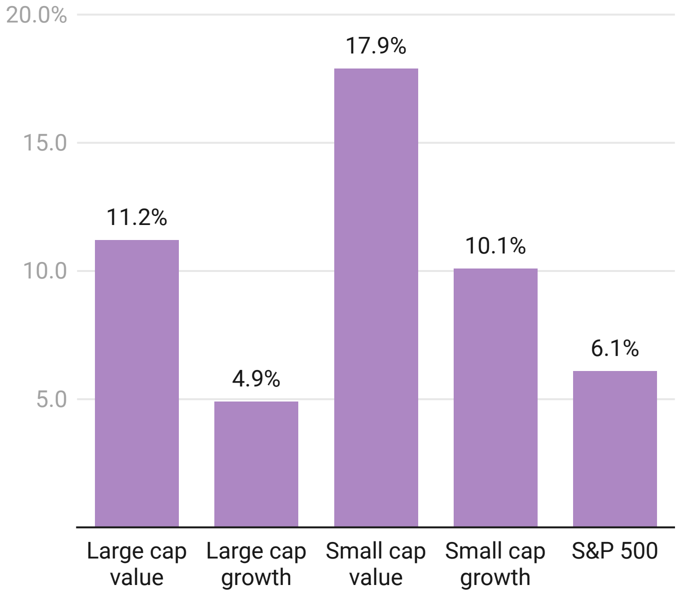


Chart: Shares magazine • Source: Hotchkis & Wiley, 2017

(CSV:NYSE), which Smith says has proved 'really good at growing margins and cash flows through giving extra added value services to consumers'. Janvier and Smith are being selective when it comes to consumer-facing sectors, though Smith notes Texas-headquartered chicken wings seller **Wingstop (WING:NASDAQ)** has 'done well coming out of the pandemic as things have reopened'.

COMPELLING VALUATIONS

Investment trust JPMorgan US Smaller Companies trades at a 10.7% discount to net asset value and aims to provide capital growth by investing in US smaller fry with sustainable competitive advantages that are well-run and trade at discounts to intrinsic value.

'When we look at our universe of investable names, valuations are more compelling than they have been for some time,' says manager Brachle.

He observes that the Russell 2000, a well-used proxy for small caps in the US, is currently trading at 11 times forward earnings, its lowest valuation level in more than three decades.

Brachle adds: 'We are not trying to call a bottom, but are looking through to the other side, and trying to position the portfolio for the next three to five years.'

Holdings include service payroll processor **Paycor (PYCR:NASDAQ)**, which has no non-US foreign exposure so generates 100% of its revenue in dollars. 'It is neither positively nor negatively impacted by the strength of the dollar. The company is currently benefiting from a tight labour market in the US and a rising interest rate environment.'

In the third quarter, the trust bought shares in **Freshpet (FRPT:NASDAQ)**, a provider of fresh, natural food choices to help improve the lives of dogs and cats which also owns and operates Freshpet Kitchens and Freshpet Fridges. Brachle likes Freshpet because it is 'a market leader in fresh and natural pet food and we have historically liked the pet/animal health sector as we view pet food as resilient given its staple-like nature, and stickiness of the category'. This niche has 'high barriers to entry (store refrigerator network, owned manufacturing assets),' he explains.

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

What's the latest for UK investors holding Russian stocks and funds?

Some investors are still in limbo as the war rumbles on

Nine months on from Russia's invasion of Ukraine and the fate of many Russia-focused stocks and funds remain up in the air.

High profile names have fallen by the wayside – notably Russian gold miner Petropavlovsk.

Prevented from selling its gold due to sanctions, the company entered administration and exited the UK stock market in July leaving shareholders with nothing. Real estate group Raven Property also delisted in the weeks after the conflict started.

Many holders of other Russian investments have been left in limbo as the war has raged on, with no sign of an end to the conflict in sight.

IMPACT ON RUSSIAN INVESTMENTS

While there were always risks attached to investing in an emerging market like Russia, particularly one so exposed to geopolitical ructions, Moscow-listed shares traded on cheap valuations heading into 2022 when there was chatter about a build-up in military activity close to Ukraine.

Many observers doubted Russian premier Vladimir Putin would follow through on his threat to invade the country, but it happened with devastating effect on 24 February.

Firms with links to Russia are an increasingly endangered species on the London stock market but there is the odd survivor. Unlike Petropavlovsk, fellow precious metals miner **Polymetal (POLY)** continues to operate.

In a trading update on 3 November the company unveiled robust production figures and maintained cost guidance. This is expected to translate into meaningful cash flow in the fourth quarter of 2022 and help the company pay down net debt from $2.8 billion at the end of September to $2.3 billion by the end of the year.

Polymetal has been helped by its holdings in Kazakhstan, representing around a third of the portfolio, which at least provided some diversification from Russian risks.

Investment bank Berenberg notes that during September Polymetal began to 'meaningfully unwind' its accumulated inventory after completing the restructuring of its sales channels away from

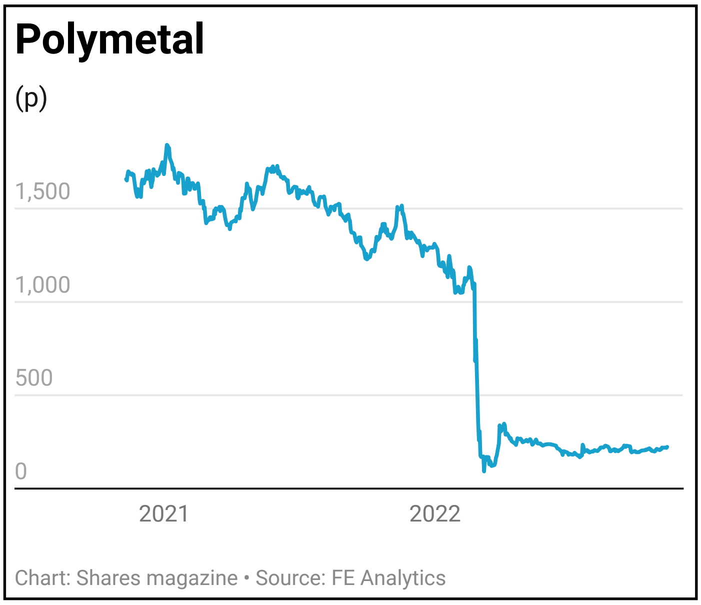


Chart: Shares magazine • Source: FE Analytics the West and towards Asia.

The shares are still down more than 80% year-to-date at 223p but have at least recovered appreciably from their lows.

The position of Russian steel firm **Evraz (EVR)**, part-owned by Russian oligarch Roman Abramovich, is more perilous with the company recently seeing its auditor EY quit in the face of continuing sanctions and its shares remain suspended.

The sanctions reflect the firm's central position in the Russian steel industry, and the support this provides to the Russian military. Sanctions were also recently extended to two Evraz shareholders, Alexander Abramov and Alexander Frolov, both associates of Abramovich.

WHAT ABOUT RUSSIAN GDRS?

Like Evraz those Russian GDRs (global depositary receipts) which are still listed in the UK are suspended.

A GDR is a certificate that represents stock in an overseas company. A bank buys shares, holds them in a depositary, and sells the receipt to an investor, typically in another currency. Generally, each GDR will contain more than one share per depositary receipt.

Many fund managers who hold these instruments have written their value down to zero.

The managers of **Liontrust Russia (B86WB79)** have taken a different approach, valuing them at their last traded prices. In a recent update for holders of the fund, dealing in which is currently suspended, Liontrust noted it was 'in the process of converting some of these holdings into the underlying local shares which are trading in Moscow, as some of these depositary programs will be discontinued and the shares delisted from Western markets.'

This followed new Russian legislation banning some Russian firms from listing in 'unfriendly' countries. Rosneft, Gazprom and Severstal are among those to have delisted their GDRs from the London market. 'As the majority of the portfolio is already held in local Russian shares there is no significant impact on the fund,' Liontrust concluded.

Russian GDRs still listed on the London Stock Exchange – but currently suspended

EN+
Norilsk Nickel
Novatek
Novolipetsk Steel
Novorossiysk Commercial Sea Port
PhosAgro
Ros Agro
Rostelecom
Tatneft

Table: Shares magazine • Source: London Stock Exchange

WHY RUSSIAN FUNDS HAVE BEEN SUSPENDED

Liontrust Russia is one of several Russian funds which have suspended dealing, with **HSBC GIF Russia Equity** and **Pictet Russian Equities (B8JBCF8)** in the same boat. These funds have also temporarily waived their annual management charge and administration fees.

Russia-focused exchange-traded funds have been suspended and some liquidated as the indices they track are discontinued.

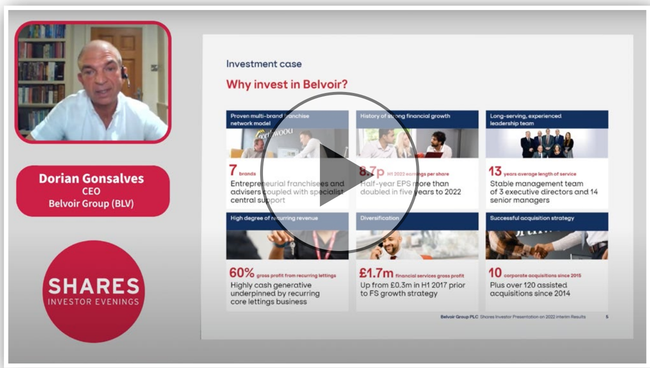
The actively managed funds are left waiting on a reopening of the Moscow stock market to all overseas investors, not just those from countries which have not imposed sanctions on Russia. Though as Liontrust notes, 'these may not be the only factors required to unsuspend the fund'.

Thanks to enjoying a different structure from open-ended funds, the one specialist Russian investment trust **JPMorgan Russian Securities (JRS)** has continued to trade.

However, as *Shares* reported, the trust plans to broaden its mandate to include other emerging economies in Europe as well as Africa and the Middle East. A meeting will be held on 23 November to collect shareholder votes on the proposed changes.

By **Tom Sieber** Deputy Editor

WATCH RECENT PRESENTATIONS



Belvoir Group (BLV)
Louise George, CFO & Dorian Gonsalves, CEO

Belvoir Group is a UK-based property franchise group delivering residential lettings and sales, and property-related financial services to the individual businesses nationwide.

CentralNic Group (CNIC)
Ben Crawford, CEO

CentralNic Group is a UK-headquartered tech company achieving over 60% annual organic growth selling recurring revenue services. CentralNic is now over 200 times the size it was when it IPO-ed less than a decade ago. It has grown its profits every year and has been called "a cash generation machine."

STV Group
Simon Pitts, CEO & Lindsay Dixon, FD

STV Group (STVG) is Scotland's digital media brand, providing consumers with a wide range of high-quality content on air, online and on demand. STV Group comprises three dynamic operation divisions: Channel 3 broadcaster, STV; free streaming service, STV Player; and production company, STV Studios.

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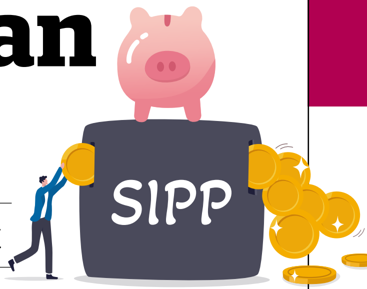
Can I get pension contributions paid into a SIPP rather than a workplace scheme?



Our resident expert on the options for someone saving for retirement

I'm being automatically enrolled into a workplace pension but I'm not particularly happy with the scheme. It charges 0.75% and the performance has been consistently poor. Can I have my contributions directed to my SIPP instead?
Simon

Tom Selby, AJ Bell Head of Retirement Policy, says:

If you are aged 22 to 66 (state pension age), employed and earn more than £10,000 a year, you should be automatically enrolled into a workplace pension scheme. At a minimum, your employer contributes 3% of 'qualifying earnings', you contribute 4% and a further 1% comes via basic-rate pension tax relief. In 2022/23, 'qualifying earnings' are salary between £6,240 and £50,270.

Some companies will offer pension contributions well above this level, so it's worth checking to see if you are entitled to more than you are getting.

Responsibility for choosing the workplace pension scheme into which you are auto-enrolled rests solely with your employer.

There are certain minimum criteria your workplace pension scheme needs to satisfy, including offering a 'default' investment fund with charges capped at 0.75%. This default fund will aim to be broadly appropriate for all employees, although because it is designed for a diverse workforce of different ages and risk preferences, by definition it will not be directly catered towards your personal circumstances and preferences.

Your employer is not obligated to offer you a pension scheme beyond the one it has picked, although some will choose to do so. Check with whoever is responsible for your pension scheme – usually HR or payroll – to see if there is an alternative option.

You may also be able to select alternative investments beyond the default fund from your existing scheme. These investments will not be protected by the 0.75% charge cap, although they may still charge at or below that level. Speak to your provider or log on to your account online to find out your options.

You cannot demand your employer pays your auto-enrolment pension into the scheme of your choice. Losing out on this valuable benefit may mean you have less savings available when you retire.

However, if your employer doesn't offer you the option of a different pension scheme and you want to transfer your hard-earned retirement pot elsewhere, there is nothing stopping you doing so. The new pension provider will take some details from you and do all the legwork.

There are some things you need to consider before transferring. Firstly, make sure there aren't any valuable guarantees you will lose. This is unlikely if you are transferring an auto-enrolment pension, but it's worth checking with your provider.

Secondly, while a SIPP may offer you a greater choice of investments, they will not be protected by a 0.75% charge cap. It is, however, possible to build your own portfolio for much less.

DO YOU HAVE A QUESTION ON RETIREMENT ISSUES?

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

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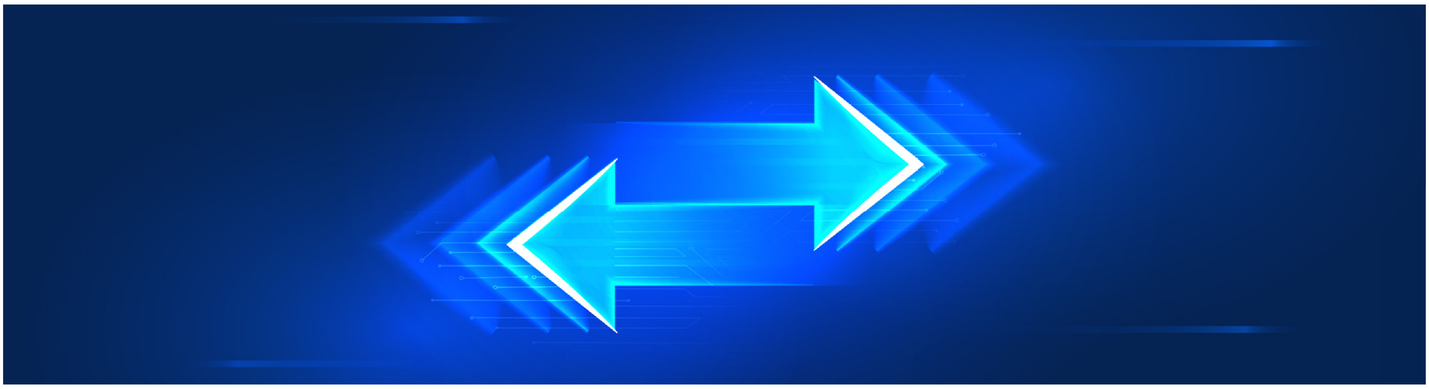
Why convertible bonds can be an attractive alternative to shares

The specialist knowledge required to invest in convertibles means they are best tackled via funds



Convertibles are hybrid debt instruments issued by companies which have an option to convert into ordinary shares. What makes them stand out is that they combine the relative safety of bonds and the potential upside of shares.

Convertible bonds can be an attractive option for investors looking to supplement their income without sacrificing growth and those looking to adopt a slightly more defensive or cautious approach while still having some level of exposure to shares.

The size of the market is around $500 billion according to Brendan Ryan, senior research analyst at Aviva Investors. Although that might sound big, it is tiny compared with the global traditional corporate bond market which is around $8 trillion.

The Refinitiv Global Focus index is a good proxy for the market and comprises around 275 issuers, the bulk of which are US mid-cap growth companies.

Typically, convertibles have a shorter duration (average lifespan) than corporate or government bonds with an average duration of two-to-three years. This means they are less sensitive to interest rates.

HOW DO CONVERTIBLES PERFORM COMPARED TO SHARES AND BONDS?

Given their hybrid characteristics, you might expect convertibles to perform similarly to the broad stock market but with less downside risk.

Ryan of Aviva says a typical long-only balanced convertible strategy is looking to capture between 60% and 75% of the equity upside and around 40% to 50% of the downside.

However, 2022 has been a difficult year for bonds and shares as global interest rates have spiked in the face of surging inflation.

Convertibles have benefited from their lower duration which has limited their fall to 9% on average compared with 20% for the Bloomberg Aggregate Bond index and 20% for the S&P 500 stock index.

Over longer periods convertibles have performed well. According to data provider Morningstar: ‘Over the trailing 15 years through October 2020, the typical convertible-bond strategy notched a healthy 8% (annual) gain, which was on par with the average large-cap equity fund.

‘This return was a couple of percentage points ahead of the high-yield bond category average and nearly double the result of the intermediate core bond category norm.’

WHY DO COMPANIES ISSUE THEM?

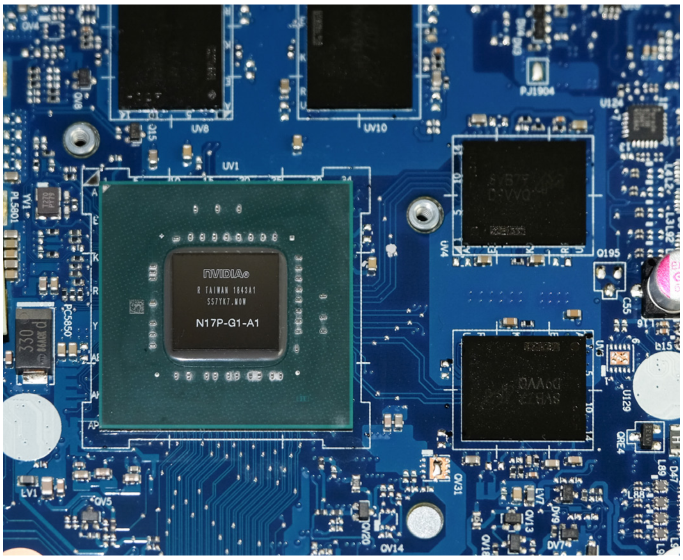
Generally, convertibles are more flexible than traditional bonds. They have the advantage of being cheaper and speedier for companies to issue because they are not rated by credit rating agencies.

They are cheaper because of the intrinsic value attached to the equity option. Ryan explains that convertibles are the only security available which allow companies to monetise the volatility of their share price.

More volatile (unstable) shares have a greater option value because they are just as likely to gain 50% over the next few months as fall 50%.

This increases the likelihood of a convertible reaching its conversion price. The higher the option value, the lower the coupon a company might need to pay.

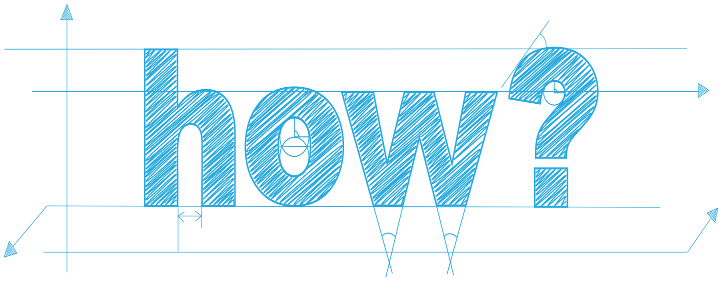
Convertibles are often issued for specific investment projects which have a finite life and payback expectation.



A good example illustrating the flexibility of investment product is the $1 billion convertible issued by chip maker **Nvidia (NVDA: NASDAQ)** in 2013, explains Ryan.

The company had around $3 billion of cash trapped overseas which it couldn't tap to buy back its shares. The company was very cash generative, had no debts, but its shares were volatile, so the company proceeded to monetise the volatility by issuing a convertible.

Issuing convertibles also means avoiding equity dilution, although if the business is successful, convertibles merely delay dilution in the medium



HOW DO CONVERTIBLE BONDS WORK?

Convertibles pay semi-annual interest like traditional bonds based on the coupon rate. A bond with a 5% coupon will pay £5 per £100.

An important concept is the conversion ratio which determines the number of shares received on conversion of the bond.

For example, a five-to-one ratio means a bond will convert into five shares. The conversion price is the face or par value of the bond divided by the number of shares for which it exchanged. In the example above it would be 100/5 or £20.

The conversion price is usually set above the prevailing share price. The difference is known as the conversion premium.

In the example above, if the stock appreciates beyond £20, it makes sense to convert the bond into shares unless the holder believes the shares will move even higher.

In practice, balanced convertible fund managers are more likely to take profit in a convertible when the share price has moved to within 80% or 90% of the conversion price.

The reason is that as the share price approaches the conversion price the bond behaves more like a pure share. Fund managers typically sell and recycle the cash into other convertibles with more appreciation potential.

If the share price remains below the conversion price the holder would hold the bonds until maturity, collecting the coupons along the way and the principle at maturity.

Convertibles trading significantly below the conversion price are referred to as 'busted'.

Aviva Investors Global Convertibles Fund

Chart: Shares magazine • Source: FE Analytics

term. Dilution refers to the increased number of shares which reduces the earnings and dividends allocated to each individual share.

The price of a convertible bond tends to trade close to its theoretically correct price because of the actions of arbitrageurs who look to profit from any mispricing.

The goal is to consistently make money regardless of market direction while keeping volatility low. Often leverage is used to magnify returns but these types of investments are not suitable for retail investors.

HOW TO INVEST IN CONVERTIBLES

There are also challenges for retail investors looking to invest in traditional individual convertibles.

First, the convertibles market is not very liquid and dealing spreads can be very wide compared with trading in shares. Second, the minimum investment size can be prohibitively expensive, running up to hundreds of thousands of pounds or euros in the UK and Europe compared with only $1,000 in the US. Therefore it's easier to invest via a fund.

One example is **Aviva Investors Global Convertibles Fund (B86L3G9)** which has an ongoing charge of 0.85% a year.

The £267 million fund has delivered returns of 91.5% and 30.7% over the last 10 and five years respectively, handsomely beating the benchmark returns of 74.2% and 14.7%.

An alternative option is to invest in an exchange-traded fund which tracks an index of convertible bonds. For example, **SPDR Refinitiv Global Convertible Bond ETF (GCVB)** has exposure to convertible bonds issued by the likes of cybersecurity group **Palo Alto Networks (PANW:NASDAQ)** and car maker **Ford (F:NYSE)**.

By **Martin Gamble** Education Editor

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Why now is the perfect time to sort out your will

Don't put off making plans in this area

Around half of us in the UK don't have a will, and I was one of them until this week. It's no surprise that people put off making a will, it involves grim conversations about your death and awkward ones about which of your family members you like enough to leave some money to versus others. Not to mention the tricky conundrum of who you want your kids (or pets) to live with if you die.

My discussions around wills this week involved the comedic phrase of 'double death scenario' and a weighing up of which of mine and my husband's siblings would most like to live with our sassy two-year-old should we peg it. All in all, not a joyous task.

WHY WRITING A WILL IS SO IMPORTANT

I'm glad that I've ticked it off the mental to-do list. It's been lurking on that list for about seven or eight years and took another step up in urgency when I had a child two years ago. But still I put it off and prioritised something else in my seemingly endless list of admin.

The perfect solution arrived this month to spur me on: Make a Will Month. This is a scheme run by Will Aid where solicitors donate their time in November to make wills for people, and in return those people donate money to a charity, Will Aid. There is a suggested donation of £100 for a single will and £180 for a pair or basic mirror wills – but you can contribute more if you want to (or think your case might be trickier).

In the absence of any huge wealth or complicated family structures I plumped for basic mirror wills for my husband and I. And, like most things you've been putting off for years, it was far more painless and quicker than I imagined it would be.

WHERE TO START

The first step was to find a solicitor on the website who had signed up to the scheme – and they don't necessarily need to be local, mine was 200 miles away in Doncaster. After setting up the call (the biggest hassle of which was coordinating my husband and my calendars to find a time when we were available and child-free) we were on track.

The night before my husband and I decided that we should probably think about some of the big decisions: like who would have our daughter and who we wanted to be executors. A top tip would be not to discuss this immediately before going to bed, like us. It leads to some pretty depressing dreams.

But the call led us through all the decisions we needed to make, from whether we wanted to leave any gifts to friends to what we wanted to do with our personal chattels (wills are very old school and use some weird language).

I had debated about whether to get one of those DIY will kits and go it alone – I take a DIY approach to all other areas of my life, whether it's house repairs or my investments, so why not this. But I'm genuinely pleased I didn't.

WHY IT COULD BE A MISTAKE TO DO IT YOURSELF

First, because I fear that a DIY will kit would have gathered dust and never been filled in. But second, our solicitor raised some very useful points that I wouldn't have thought of alone. Such as what age we wanted our child to inherit our estate should that dreaded double death scenario happen, or what we wanted to do with our money if all three of us died (admittedly not the cheeriest point, but a useful one).

She also suggested we have a letter of wishes alongside the will, which lays out things like preferences for our funeral (turns out my husband has some pretty clear ideas) and items we want to leave to friends or family. The benefit of these not being in the will is that it's easier to change a letter of wishes should our circumstances (or song choices for the funeral) change.

After verbally agreeing everything, our wills are now winging their way to us in the post, when we'll need to sign them and return them. At that point it is job done, unless something dramatically changes in our lives. And it feels like a win-win: we've got a will cheaper than we would have paid, some charities have got some money they wouldn't have otherwise got, and I've finally ticked the task off my to-do list. Now onto the next one.

You can book a solicitor through Will Aid by following this link.

By **Laura Suter**
AJ Bell Head of Personal Finance

KEY ANNOUNCEMENTS OVER THE NEXT WEEK

Full-year results:
21 November: Diploma, Genedrive.
23 November: Ten Lifestyle.

Half-year results:
18 November: Liontrust Asset Management.
21 November: Big Yellow, Molten Venture, Sysgroup.
22 November: Accsys Technologies, AO World, CML Microsystems, Helical, Homeserve, Severfield, Tatton Asset Management, Telecom Plus, Trifast. **23 November:** Discoverie, Eckoh, HICL Infrastructure, LondonMetric Property, United Utilities. **24 November:** Dr. Martens, LXI REIT, Motorpoint, NewRiver REIT, Omega Diagnostics, Polar Capital, Severn Trent, XPS Pensions. **25 November:** Pets at Home.

Trading updates
21 November: MTI Wireless Edge. **22 November:** Restore. **23 November:** DP Eurasia, Rotork. **24 November:** Intertek, Kingfisher, Safestore. 25 November: Breedon, Vesuvius.

WHO WE ARE


EDITOR:
Daniel Coatsworth
@Dan_Coatsworth


DEPUTY EDITOR:
Tom Sieber
@SharesMagTom


NEWS EDITOR:
Steven Frazer
@SharesMagSteve


FUNDS AND INVESTMENT TRUSTS EDITOR:
James Crux
@SharesMagJames


EDUCATION EDITOR:
Martin Gamble
@Chilligg


COMPANIES EDITOR:
Ian Conway
@SharesMagIan

CONTRIBUTORS:
Danni Hewson
Laith Khalaf
Russ Mould
Tom Selby
Laura Suter

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

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