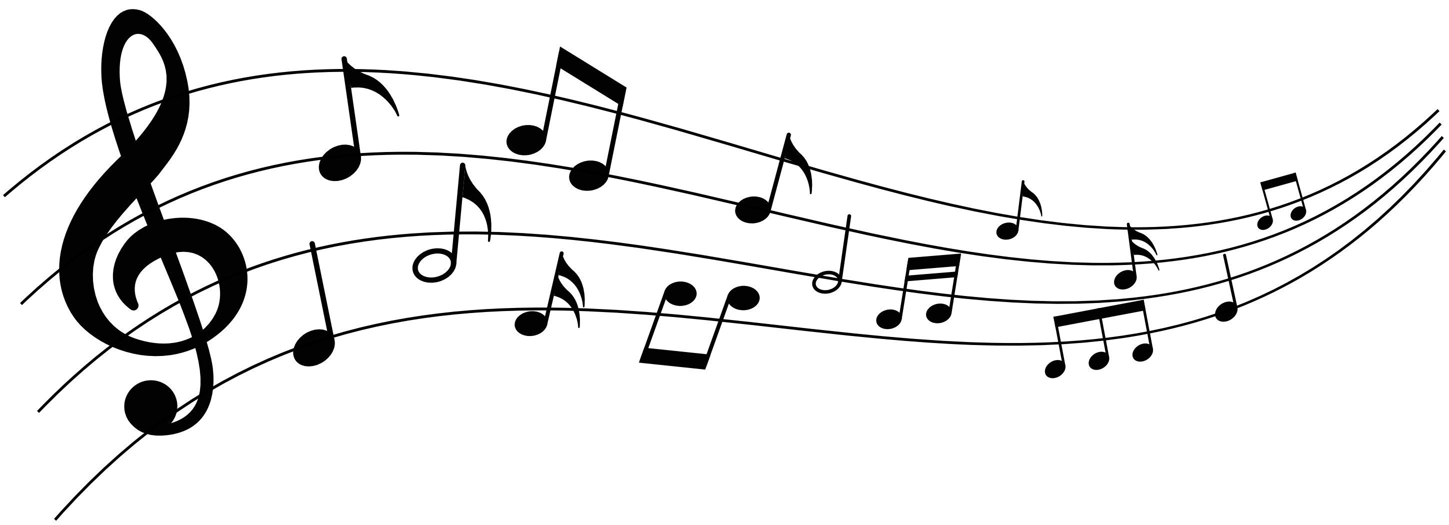
STOCKS | FUNDS | INVESTMENT TRUSTS | PENSIONS AND SAVINGS

VOL 25 / ISSUE 14 / 13 APRIL 2023 / £4.49

# SHARES

WE MAKE INVESTING EASIER

# SWEET SOUND OF **DIVIDENDS**



## How to find quality sources of income

**OUR PICKS: 18.5%** VERSUS **MARKET: 3.8%**

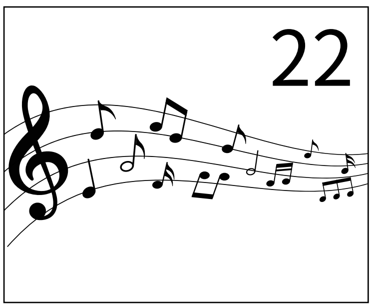
**TIPS OF YEAR REVIEW**

Our 2023 picks significantly outperformed the market in Q1

# Contents







# Three important things in this week's magazine


Feature: Tips of the year review

Our top picks for 2023 have made a superb start to the year

OUR PICKS: 18.5% VERSUS MARKET: 3.8%

**Our portfolio of 10 stocks for 2023 have delivered nearly five times the return of the UK market**

Read our tips of the year review where we've significantly outperformed the FTSE All-Share index since the portfolio was launched in December 2022


Danni Hewson: Insightful commentary on market issues

Space investing comes crashing back down to earth after Virgin Orbit bankruptcy

**Investing in the space theme has been a big disappoint**

Virgin Orbit is the latest company to let down investors despite the promise of great things from the sector


SWEET SOUND OF DIVIDENDS

How to find quality sources of income

GOLDEN RULE #1

THREE GOLDEN RULES FOR FINDING QUALITY INCOME

**There are three golden rules for finding quality sources of income**

Read our feature which explores way to invest (directly or through funds) in high-calibre companies which can afford to pay a growing stream of dividends

# Visit our website for more articles

Did you know that we publish daily news stories on our website as bonus content? These articles do not appear in the magazine so make sure you keep abreast of market activities by visiting our website on a regular basis.

Over the past week we've written a variety of news stories online that do not appear in this magazine, including:


Why Shell shares are higher despite the company flagging a quarterly loss

Fulham Shore shares up 34% after agreeing all-cash takeover


Ashoka WhiteOak Emerging Markets seeks £100 million through London IPO


Wall Street Week: recession fears hit stocks as Tesla stalls

# Why consumer-facing companies are among London's most-shorted stocks

## Retailers feature prominently as living standards slide

Institutional investors continue to bet against consumer-facing companies, despite the International Monetary Fund predicting that advanced economies including the UK could return to ultra-low interest rates once inflation is tamed.

The IMF argues recent increases in interest rates are likely to prove temporary. When inflation is brought back under control, it says central banks are likely to ease monetary policy and bring interest rates back toward pre-pandemic levels.

Forecasts from the Office for Budget Responsibility show the UK will avoid recession this year, yet it still sees the economy contracting overall in 2023 and has warned living standards are expected to fall by the largest amount since records began.

The latest figures from BRC and KPMG show UK retail sales rose by 5.1% in March, but volumes fell as households prioritised spending on essentials with inflation continuing to bite.

Hard-pressed consumers continue to count their pennies which might explain why consumer-facing companies dominate the list of most-shorted stocks on the UK stock market.

Loss-making **Ocado (OCDO)** is London's most-shorted stock with 6.1% of the shares out on loan after its joint venture with **Marks & Spencer (MKS)** suffered a 7.5% drop in its first quarter basket size as trading remained 'challenging'.

Others in short-sellers' crosshairs are online fast-fashion retailers **ASOS (ASC)** and **Boohoo (BOO:AIM)** as well as online greetings cards seller **Moonpig (MOON)**.

Institutional investors are also betting against home improvement giant **Kingfisher (KGF)**, a big beneficiary of a now-fading lockdown DIY boom, which saw like-for-like sales soften 2.1% in the year to January 2023.

In terms of current trading, Kingfisher reported (21 March) 'broadly flat' year-on-year big-ticket sales as it laps demanding comparatives, while

### Most shorted UK-listed stocks

| Company | % short |
|---|---|
| Ocado | 6.1% |
| ITM Power | 5.6% |
| ASOS | 5.5% |
| Moonpig  | 5.3% |
| Boohoo | 5.1% |
| Kingfisher | 4.9% |
| Hammerson | 4.7% |
| Naked Wines | 4.0% |
| THG | 3.9% |
| Victoria | 3.8% |
| Petrofac | 3.7% |
| Cineworld  | 3.3% |
| Standard Life Aberdeen | 3.3% |
| Technology Minerals | 3.0% |
| Metro Bank | 2.9% |
| Harbour Energy | 2.8% |
| Primary Health Properties | 2.8% |
| Renewi | 2.8% |
| XP Power | 2.8% |
| First Derivatives | 2.7% |

Table: Shares magazine • Source: ShortTracker.co.uk

short-sellers are also lining up against the likes of unloved e-commerce brand platform provider **THG (THG)** and indebted floor coverings manufacturer **Victoria (VCP:AIM)**.

Last November, Victoria warned it was likely that disposable incomes in some markets would come under further pressure from higher interest rates and inflation, so it might struggle to push through further price increases to offset higher input costs. [JC]

# The story behind sterling's big move to 11-month highs versus the dollar

Expectations around interest rates in the UK and US have diverged

Sterling is on a comeback trail against the dollar, reaching 11-month highs against the US currency on divergent rate expectations. The move to reclaim the $1.25 mark is a combination of strength in the pound and weakness in the dollar.

The recent banking crisis started across the Atlantic with the collapse of Silicon Valley Bank and the US regional banking sector is perceived as more vulnerable than UK banks.

This means the Federal Reserve may have to prioritise its role in preserving financial stability over pursuing further rate hikes to firmly stamp out inflation. The upshot is the market is now pricing in at least one more rate hike from the UK versus no more from the Fed in the near-term.

UK economic data has been more resilient than expected against a more settled political backdrop, with progress on relations with the EU over Northern Ireland and the disastrous mini-Budget becoming more of a distant memory.

The latest survey from the British Chambers of Commerce showed just over 50% of UK companies expect their turnover to grow in the coming months. Strong private consumption saw fourth quarter GDP estimates upgraded by 0.1 percentage points at the end of March. Deutsche Bank recently updated its forecasts and no longer expects the UK economy to contract in 2023.

**Sterling versus the US dollar**


Chart: Shares magazine • Source: Refinitiv


At the same time, US data has come in weaker than expected. Since the start of April manufacturing PMI (purchasing managers' index) data showed factory activity levels contracting more than expected, while the services sector expanded less than forecast and job openings were lower than anticipated at 9.93 million against the 10.49 million estimate.

It is also worth noting the US has already made more progress in its battle against inflation – the year-on-year reading of US CPI for February was 6% against an unexpectedly higher 10.4% for the UK.

In part this reflects the UK's greater exposure to energy prices, with the US benefiting from much higher levels of domestic supply.

Stronger sterling may in itself help reduce inflation as it decreases the cost of buying in goods and services from abroad. It could, however, be a headwind for the FTSE 100 as it diminishes the relative value of its dominant overseas earnings.

Consultant Capital Economics says investors should not get too used to the current situation: 'Although the Fed may now be done with rate hikes, in most previous tightening cycles the dollar continued to appreciate even after short-tern US interest rates peaked.

'Our judgement is that "safe haven" demand in a global downturn is likely to prove the dominant factor in currency markets over the coming months, driving the dollar (and the yen) higher in the near term.' [TS]

# Journeo travels to new heights as earnings show rapid progress

## Small cap transport technology specialist is winning over investors as it chalks up contract wins

Transport technology specialist **Journeo (JNEO:AIM)** is seeing the momentum behind its earnings feed into a strong share price performance. The stock market minnow is up more than 34% over the last six months.

On 28 March Journeo, which provides a range of technical and data-related solutions to rail, bus and coach operators, reported underlying profit up 100% to £1.2 million on revenue up 35% to £21.1 million. The company also announced two new contracts to provide passenger information displays to Transport for Wales for a combined £1.6 million.


Consensus earnings per share forecasts for 2023 imply a price to earnings ratio of 9.3 and earnings growth of 76.5%. Estimates have been consistently revised higher over the last 12 months.

The company is looking to transition to a SaaS (software as a service) model, a software licensing and delivery blueprint in which software is used on a subscription basis and is centrally hosted.

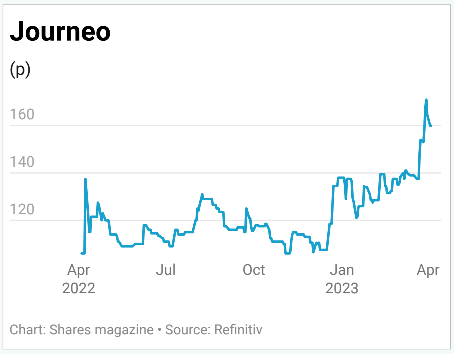


Chart: Shares magazine • Source: Refinitiv

Cenkos analyst Andrew Renton comments: 'Journeo has gone from strength-to-strength over recent years, consistently growing revenues and profits whilst building the foundations of a high margin SaaS business model.' [TS]

# Cineworld shares slump as wipeout looms for certain investors

## Existing shareholders will not be allowed to subscribe for shares in the new equity offering

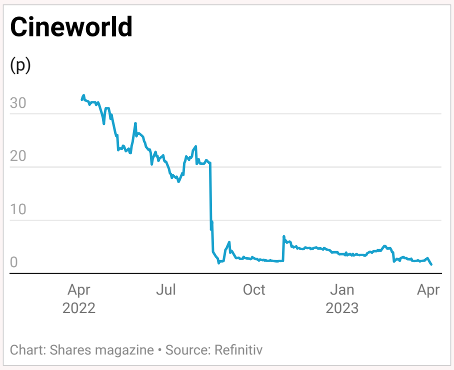


Chart: Shares magazine • Source: Refinitiv

Beleaguered cinema operator **Cineworld (CINE)** saw its shares drop a further 28% to 2p on 3 April taking the losses to 42% over the last three months and 94% over the last 12 months.

It is likely current shareholders will be wiped out completely following news the company's lenders plan to move ahead with a $4.53 billion debt for equity swap and raise a further $800 million in fresh equity.

Current investors in the shares will not be able to participate with the company indicating the proposed restructuring 'does not provide for any recovery for holders of Cineworld's existing equity interests'. The shares will however remain trading while the restructuring takes place and potentially even thereafter too.


Unless the company receives an offer for the whole group more than the value established under the restructuring plan, it will not sell the US, UK, and Ireland assets.

However, the company said the restructuring plan 'will provide sufficient flexibility to accommodate a sale of the Rest of the World business'.

Although no announcement has been made the *Financial Times* reported that the restructuring would likely mean CEO Mooky Greidinger 'relinquishing control of his third-generation family business'. [MG]

# UK UPDATES OVER THE NEXT 7 DAYS

**HALF-YEAR RESULTS**
**20 April:**
WH Smith, Centamin

**FULL-YEAR RESULTS**
**14 April:**
888, AO World, Lifesafe, Flowtech Fluidpower
**17 April:**
Schroder UK Public Private Trust, Surface Transforms, Diaceutics
**18 April:**
Billington, Property Franchise Group
**19 April:**
M Winkworth, Distribution Finance Capital
**20 April:**
Arecor Therapeutics, Intelligent Ultrasound Group, Oxford Biomedica

**TRADING UPDATES**
**14 April:**
888, Hays
**17 April:**
Sirius Real Estate, Ashmore
**18 April:**
Entain, IntegraFin, Liontrust Asset Management
**19 April:**
Hochschild Mining, Network International Holdings
**20 April:**
Dunelm, SEGRO, Rio Tinto, Rentokil Initial

# Contrasting fortunes for 888 and Entain shareholders ahead of big updates

**William Hill's £19 million fine for gambling protection failures adds to compliance issues at new owner, 888**

Online gambling and gaming company **888 Holdings (888)** will release full year results and a first quarter trading update on 14 April while larger peer **Entain (ENT)** will give a first quarter trading update on 18 April.

Investors will be looking for some reassurance at 888 after it shocked investors (30 January) by revealing an internal probe amid compliance breaches in the Middle East which led to the resignation of CEO Itai Pazner.

At its 2022 results Entain flagged continuing regulatory headwinds coming into 2023 but said trading had started with positive underlying momentum.

On 5 April Entain announced the acquisition of leading scores and sports media company 365scores for $150 million. Investors will be looking for signs that Entain's US business remains on track to turn a profit in 2023. [MG]

# Why WH Smith is confident of delivering another year of growth


**The FTSE 250 retailer offers investors a play on improving global passenger numbers**

Investors will be seeking confirmation that **WH Smith (SMWH)** continues to benefit from the recovery in airport passenger volumes and that its store rollout programme is going to plan when the retailer reports half-year results on 20 April.

The high street and travel retailer has already issued an upbeat trading update for the 20 weeks to 14 January 2023, with CEO Carl Cowling insisting WH Smith was in 'its strongest ever position as a global travel retailer'. Combined with the continued improvement in global passenger numbers, Cowling expressed confidence in 'another year of significant growth in 2023'. [JC]

# Taiwan Semiconductor Manufacturing Company

**This could be a make or break set of numbers**

At the start of the year **Taiwan Semiconductor Manufacturing Company (TSM:NYSE)**, which has a listing in New York, played it cautious with 2023 guidance. Talk of a 'slight growth year' because of a cyclical downturn in the chip industry came alongside weakening demand for micro chips and building inventories. Analysts are hopeful that this could begin to change as 2023 progresses, with the world's largest contract chip maker a sector bellwether. TSMC is seen reporting earnings of 7.58 Taiwan dollars on T$524.7 million revenue on 20 April. [SF]

# Netflix will be hoping its new price plan will stave off competition

**All eyes will be on subscriber numbers when the streaming platform reports**

Streaming platform **Netflix (NFLX:NASDAQ)** is set to report its first quarter results on 18 April.

Netflix lost subscribers in the first half of 2022, yet for the year as a whole it achieved 4% growth in subscriber numbers.

Despite the company ceasing to give subscriber guidance in an attempt to shift investor focus to revenue, no doubt there will still be plenty of attention on this metric when Netflix reports. Take-up of its new ad-supported tier and its move into games publishing will also be closely scrutinised. So far Netflix has made more than 20 mobile games available for free to subscribers.


Netflix's shares almost halved in value last year leaving it open to takeover speculation. Some media reports suggest tech giant **Microsoft (MSFT:NASDAQ)** might be a likely suitor. [SG]

## US UPDATES OVER THE NEXT 7 DAYS

### QUARTERLY RESULTS

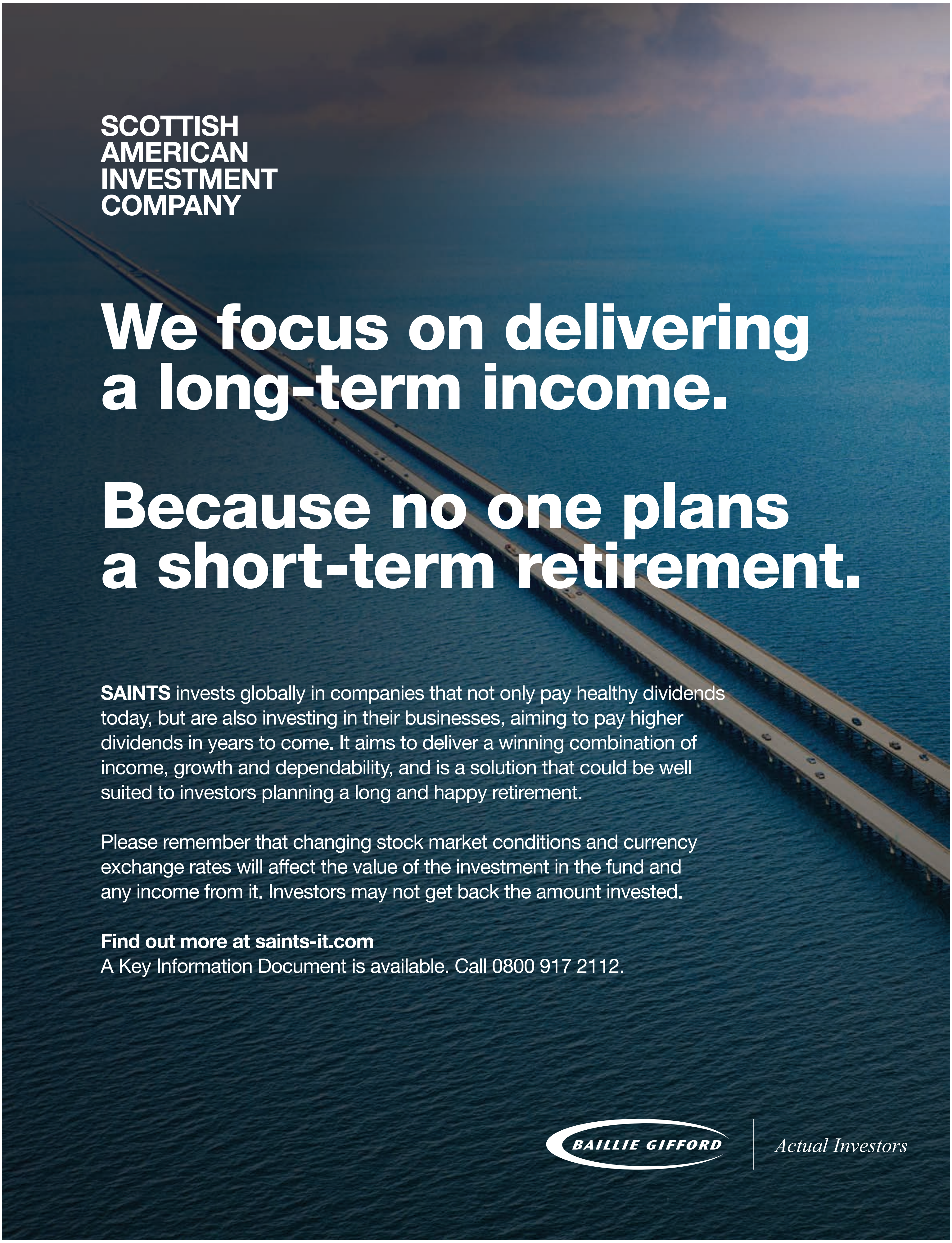
**14 April:**
UnitedHealth, JP Morgan, Hermes International, Wells Fargo, Citigroup, PNC Financial, Eaton Vance, TomTom

**17 April:**
Charles Schwab, State Street, M&T Bank, JB Hunt, Equity Lifestyle, Wintrust, Pinnacle

**18 April:**
J&J, Bank of America, Netflix, Goldman Sachs, Bank of NY Mellon, Interactive Brokers, Omnicom, United Airlines, First Horizon, Manpower

**19 April:**
Tesla, Louis Vuitton, Abbott Labs, Morgan Stanley, IBM, Rio Tinto, Blackrock, US Bancorp, Travelers, Nasdaq, Equifax

**20 April:**
Philip Morris, American Express, Union Pacific, Marsh McLennan, Taiwan Semiconductor Manufacturing Company


SCOTTISH
AMERICAN
INVESTMENT
COMPANY
We focus on delivering a long-term income.
Because no one plans a short-term retirement.
SAINTS invests globally in companies that not only pay healthy dividends today, but are also investing in their businesses, aiming to pay higher dividends in years to come. It aims to deliver a winning combination of income, growth and dependability, and is a solution that could be well suited to investors planning a long and happy retirement.
Please remember that changing stock market conditions and currency exchange rates will affect the value of the investment in the fund and any income from it. Investors may not get back the amount invested.
Find out more at saints-it.com
A Key Information Document is available. Call 0800 917 2112.
BAILLIE GIFFORD
Actual Investors

# Brunner: a great way to invest in stocks around the world on the cheap

Take advantage of the discount in this consistent performer and dividend-paying stalwart

**BRUNNER**
(BUT)
Price: £10.71
Net asset value: £11.53


The 7.1% share price discount to net asset value on investment trust **Brunner (BUT)** provides an opportunity to buy a balanced global portfolio for less than the value of the underlying assets.

The trust has delivered consistent returns across the market cycle and has particular appeal during the current period of uncertainty. A quarterly dividend payer, Brunner is one of the Association of Investment Companies' 'Dividend Heroes', having grown the shareholder reward for 51 successive years.

Brunner's long-term performance has been strong versus the global sector and the year to November 2022 marked the trust's fourth consecutive year of outperformance of the benchmark across a range of market conditions.

Managed by Allianz Global Investors' Christian Schneider and Julian Bishop with support from Marcus Morris-Eyton, Brunner seeks to provide a progressive dividend alongside capital growth over time. It has a 0.63% ongoing charge.

The trust is diversified across 61 holdings with a focus on attractively valued, quality companies blessed with high market shares, pricing power, strong balance sheets and a sustainable competitive advantage. This approach should offer investors comfort in today's unpredictable environment of higher inflation and interest rates, geopolitical tensions and banking crises.

As Morris-Eyton explained on a recent investor call, Brunner is 'proving to be an all-weather fund that has been able to cope in most of those market environments.'

Brunner seeks companies set to benefit from structural growth trends and its top 10 holdings include **Visa (V:NYSE)** and **Taiwan Semiconductor Manufacturing (TSM:NASDAQ)**.

Themes in the portfolio include digitalisation, through names such as software groups **Microsoft (MSFT:NASDAQ)** and **Adobe (ADBE:NASDAQ)**, and electrification via names such as energy giant **Shell (SHEL)** and **Schneider Electric (EPA:SU)**.

The trust also offers a play on rising health and wellbeing spend through US healthcare firm **UnitedHealth (UNH:NYSE)**, Danish pharmaceutical company **Novo Nordisk (NVO:NYSE)** and consumer health products provider **Haleon (HLN)**, as well as the rise of the emerging market middle class through the likes of luxury goods group **LVMH (LVMH:BIT)** and restaurants operator **Yum China (YUMC:NYSE)**.

One key issue to consider is that Brunner has seen several lead manager changes in recent years. Lucy Macdonald stepped down in 2020 when she quit Allianz. Her replacement, Matthew Tillett, only lasted two years in the top job before moving to rival asset manager Premier Miton.

Investors should take comfort that new co-lead manager Schneider has been with Allianz since 2000 as part of the global equities team. Fellow co-lead manager Bishop joined Allianz last year but used to help manage Tesco's pension scheme and has more than 25 years' fund management experience. [JC]

**Brunner**


Chart: Shares magazine • Source: Refinitiv

# Buy Empiric at a big discount to the other main player in student property

The valuation differential with Unite looks too large given Empiric has made positive changes to its portfolio of assets

**EMPIRIC STUDENT PROPERTY**
(ESP)
Price: 91p
Market cap: £549 million

Student accommodation is a segment of the property market with supportive dynamics coming out of the pandemic and we think **Empiric Student Property (ESP)** is an attractively valued way of gaining access to this space.

Empiric trades at a substantial discount to its larger peer **Unite (UTG)**, reflecting a somewhat more uneven track record and its smaller scale, but we think the managers of the real estate investment trust have got their act together. Investors should take advantage and buy the shares.

Based on 2023 net asset value forecasts from Berenberg of 112.8p and 950.8p respectively, Empiric is at a 19.3% discount while Unite trades at a 3.1% premium. Empiric is hoping to increase its dividend by 18% in 2023 to 3.25p per share, implying a 3.6% prospective yield.

Student property has resilient valuations and high occupancy rates thanks to significant undersupply, rising demand from overseas and at home as well as, in the longer term, a growing population.

Empiric offers modern, premium student accommodation with facilities like private gyms and cinemas which help it to attract and retain tenants.

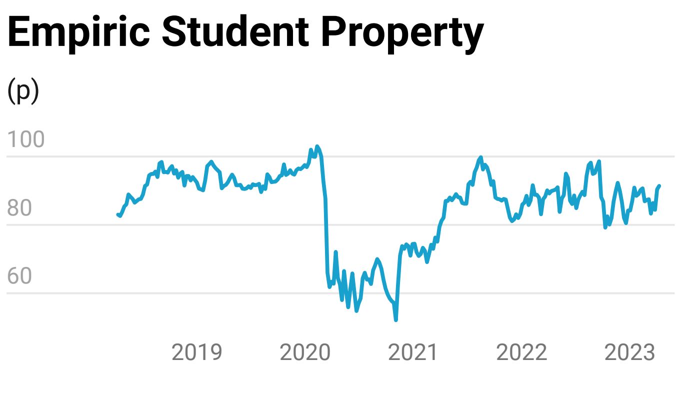


Chart: Shares magazine • Source: Refinitiv

Berenberg analyst Kieran Lee observes: 'The Empiric of today bears little resemblance to the same company at the onset of the Covid-19 pandemic. The portfolio has been refined, operations overhauled, necessary capex expended and there remains significant opportunity in complementary verticals.'

Empiric has shifted its strategy to focus on 'clustering'. This means expanding in areas where it already has a presence. By doing so it can boost revenue without necessitating a big increase in costs because it can make use of its existing marketing or building management teams in the relevant area. This is helping to support an improvement in margins.

The trust also has the opportunity of expanding the number of tenants it has which are on postgraduate courses and a pilot scheme is underway in Edinburgh.

Empiric has sold more than £70 million worth of assets as part of a restructuring and the focus is now on a select group of cities which contain the best universities, with the proceeds from disposals being recycled back into the portfolio. This process is expected to be completed by the end of 2023.

A risk for investors to weigh is the increased cost of borrowing and the impact this will have on the economics of new developments. The weighted average cost of debt rose from 3% in 2021 to 4% in 2022. [TS]

# Rathbones raises its sights with £100 billion Investec wealth deal

The company and analysts believe the wealth management market is 'ripe for consolidation'


## Rathbones (RAT) £19.10

## Loss to date: 10%

We recommended wealth management outfit **Rathbones (RAT)** in April 2022 as a read-across from RBC's £1.6 billion bid for UK asset manager Brewin Dolphin, but since then things have been extremely quiet on the UK corporate front.

Financial firms in general have had a rough ride of late, and it is no reflection on Rathbones that its shares are 10% lower since we said to buy – shares in the UK's largest quoted fund manager **Schroders (SDR)** are down twice as much over the same period.

### WHAT HAS HAPPENED SINCE WE SAID TO BUY?

Despite an unfavourable investment backdrop, Rathbones increased its operating profits last year thanks to higher fee income, commissions and net interest income on the back of higher rates.

This month Rathbones revealed it had seized the initiative and agreed to take over the UK wealth management unit of Anglo-South African bank **Investec (INVP)** in a share-for-share merger to create a group with £100 billion of assets under management and administration.

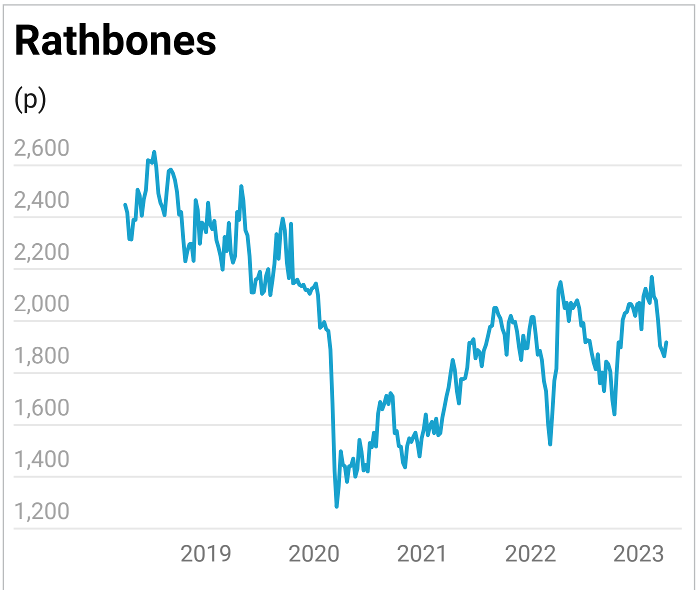



Chart: Shares magazine • Source: Refinitiv

Under the terms of the deal, which values Investec's UK wealth and investment business at around £840 million, Investec will own a 41.25% economic interest in the enlarged Rathbones but just a 29.9% voting share.

### WHAT SHOULD INVESTORS DO NOW?

In a sense, things are just warming up for Rathbones with the takeover of the Investec UK private wealth management business.

The firms share a similar culture and similar business models, so putting the two together and extracting cash synergies shouldn't be a difficult task.

Rathbones' chief executive Paul Stockton predicts annual savings of £60 million within three years due to economies of scale and higher net interest income, but Jefferies analyst Julian Roberts reckons £60 million is 'not a big stretch' and is forecasting a 15% uplift to Rathbones' earnings per share as early as 2025.

Roberts calls the deal 'a step change in scale' for Rathbones and says he expects more consolidation in the sector. With management executing well, it is worth holding on to Rathbones shares. [IC]

# Laboratory owner offers a cheap way into a growing specialist market

Higher rents and new developments should see long-term holders rewarded

## Life Science REIT (LABS) 61.5p

## Loss to Date: 14.6%

The trust, which specialises in owning properties leased to companies in the life science sector, raised £350 million when it launched in November 2021 and at the end of last year its portfolio was valued at £388 million.

Its properties range from offices to labs and production facilities in the 'Golden Triangle', which stretches from Oxford and Cambridge to the Knowledge Quarter of north London and is attracting a high level of investment from life sciences firms.

### WHAT HAS HAPPENED SINCE WE SAID TO BUY?

We hoped the drubbing for real estate companies had run its course since our call last October, but a combination of lower property valuations and investor aversion to 'alternative' assets has seen the share price fall 15% in the interim.

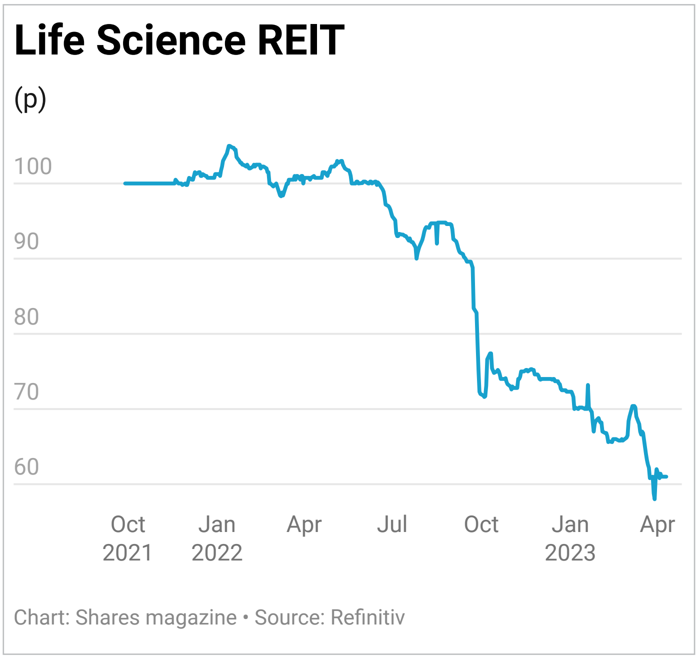
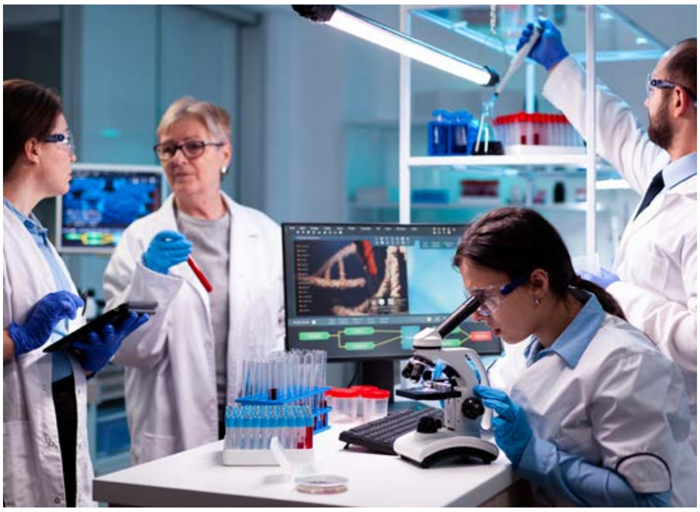


Chart: Shares magazine • Source: Refinitiv



The managers have stuck to their brief, investing only in high-quality assets, but the portfolio suffered a £31 million revaluation loss at the end of last year.

The contracted rent roll at the end of 2022 was close to £14 million, while the estimated rental value of the portfolio was £17.2 million leaving plenty of room for upward revisions to rents.

The estimated rental value was lifted by active management of the assets including lab conversions at Rolling Stock Yard in north London and the refurbishment of The Merrifield Centre in Cambridge.

Including deals signed since the year-end and those under offer, life science tenants account for just over 40% of the occupiers and this proportion will keep rising as the development portfolio – which includes the 20-acre Oxford Technology Park – becomes available.

### WHAT SHOULD INVESTORS DO NOW?

The trust is still a work in progress with significant potential to raise rents as more of the portfolio is converted into lab space, so investors who want long-term exposure to life science assets should sit tight as the shares are at a 33% discount to its last net asset value. Hopefully this gap should narrow over time.

In the meantime, income investors should be attracted by the 4p target dividend for this year which puts the shares on a 6.5% yield. [IC]

Schroders

# Asian investment trusts: **an abundance of opportunity**

***Exploring investors' renewed enthusiasm for Asian equity.***

After a challenging period of performance, Asian equity markets have sprung into life in recent months. The removal of zero-covid policies in China appears to have rejuvenated prospects for the entire region, with pent-up demand being unleashed and investors suddenly waking up to a regional opportunity that has an improved near-term economic outlook, as well as positive longer-term structural foundations.

On the face of it, valuations in Asia look appealing, particularly compared to other regions such as the US (When the S&P 500 is compared against the MSCI Asia Pacific ex Japan index between 2013 to 2023)

Indeed, after a decade of outperformance, investors appear to have taken last year's correction in the US stock market as an opportunity to re-appraise the attractiveness of that market when compared to other regions. According to a recent Bank of America Global Fund Manager survey, allocations to US equities have fallen by the most since records began and now stand at their biggest underweight since October 2005.

From an economic perspective too, the fundamentals look to be improving in Asia, while North America and Europe remain at risk of recession. The same survey suggested that global fund managers are becoming more optimistic on the economic growth outlook for Asia. As a proxy, more than 90% of respondents said they expected a stronger Chinese economy, up from 13% in November last year.

**WHAT'S HAPPENING IN CHINA?**

Regulatory crackdowns, geopolitical worries, a property market crash, and the extended zero-covid policy have all weighed on sentiment and economic activity in China over the last couple of years. But some of these clouds do appear to be lifting. The removal of covid restrictions in December has been seen by many as the catalyst for the recent improvement in Asian equity market performance. It may lead to an "exit wave" of new covid infections, as has been the case in other regions that have emerged from lockdown, but on balance, recent developments in China are seen as an economic positive, with Schroders economics team now anticipating growth of more than 6% in 2023 compared to just 3% last year. That is a modest rate of growth compared to what we've regularly seen from China over the last 30 years, but it looks attractive in comparison to what developed economies are expected to deliver in 2023.

Nevertheless, considerable risks remain. China no longer benefits from the positive demographics that have assisted growth in recent decades and youth unemployment is a growing problem. Many commentators also fear that the government's more interventionist policy stance will continue in the years ahead, to the detriment of its private sector. Meanwhile, on the global stage, the ongoing trade war between the US and China as well as geopolitical tensions over Ukraine and Taiwan has continued to strain relations between these two powerful nations.

As a result of all this, Schroders' fund managers are generally cautious on China. The near term economic outlook has clearly improved, but longer-term structural concerns linger. Fortunately, Asia has a much broader opportunity set, and you don't need to be invested directly in China to be exposed to some of its positive attributes.

## BEYOND CHINA

Other Asian economies can benefit from the improved outlook for China and look capable of delivering decent growth in the years ahead. Neighbours Taiwan and South Korea are just a short hop away and possess global industry leaders in key Asian export sectors, including technology stocks such as Samsung Electronics and TSMC that have favourable long-term secular growth drivers. Valuations in these markets tend to be even more appealing than they are in China. Meanwhile, several financial companies in Hong Kong, Singapore and other parts of Southeast Asia should be beneficiaries of higher interest rates and offer attractive valuations and yields.

Other economies such as India, Vietnam and Indonesia, have helpful demographics and relatively low debt burdens, which should lead to decent long-term economic growth, and interesting company specific opportunities as domestic consumption increases.

## CONCLUSION

Overall, Asia looks to offer plenty of exciting opportunities for experienced stock pickers to capture. Asian equity investing has always been a core strength for Schroders, with bottom-up stock picking at the heart of its historic success. Schroders runs three pan-Asian investment trusts, each of which targets a specific opportunity within this diverse and attractive region.

**Click here to find out more**

# Our top picks for 2023 have made a superb start to the year

We're actively managing the portfolio with profits already taken on three stocks

Helped by a positive first quarter for stocks our top selections for 2023 have made a superb start to the year.

At the time of writing the share price return on the portfolio of 10 names is 18.5%, substantially outpacing the FTSE All-Share which is up just 3.8% and with not a single name in negative territory. We have also significantly outperformed the MSCI World's 4.6% advance in sterling.

**OUR PICKS: 18.5%**

**VERSUS**

**MARKET: 3.8%**

The key drivers behind our success have been a combination of being exposed to the right areas of the market and individual stock-specific catalysts.

Recognising the risks of a deterioration in sentiment over the remainder of the year we moved quickly to book profit on three of our selections during the first quarter.

### WHERE AND WHY DID WE TAKE PROFIT?

The three top spots in our table ranking the 2023 picks' performance are occupied by names where we chose to make a sharp exit.

At the top is sports retailer **JD Sports (JD.)** which posted a bullish post-Christmas trading update on 11 January where it guided for full-year profit at the top end of the £933 million and £985 million forecast range.

A 40% return in less than a month on a consumer-facing stock in a cost-of-living crisis made a strong case for getting out while the going was good.

We did well to take advantage of a positive early reaction to returning CEO Bob Iger's plans to revive the fortunes of global entertainment leader **Walt Disney (DIS:NYSE)**. Earnings for the three months to 31 December were 27% ahead of expectations at $0.99 and Iger signalled plans to pay a dividend before the end of 2023. The shares have subsequently drifted back since we took profit in February as the market awaits further progress with the recovery plan.

African gold miner **Shanta Gold (SHG:AIM)** was boosted by a spike in gold prices linked to the collapse of Silicon Valley Bank and the ensuing banking crisis. With some concern about operational risks at the business after production missed guidance in the fourth quarter, it felt an opportune time to take our money off the table, which we did in March.

### WHAT ELSE HAS DONE WELL?

Improved sentiment towards technology names, as concerns about financial stability have brought down interest rate expectations, have been helpful to **Apple (AAPL:NASDAQ)** and chip equipment maker **ASML (ASML:AMS)**. In January Netherlands-based ASML announced a 37% increase in fourth quarter net system sales to €4.75 billion with services revenue up 10.5% to €1.68 billion.

The fourth quarter gross margin was better than expected at 51.5% and the company guided for 25% sales growth in 2023.

Apple shares are approaching a new record high as investors flock back to profitable technology companies. The market also brushed off a rare miss on forecasts with Apple's first quarter earnings running to 31 December.

Earnings per share of $1.88 on sales of $117.2 billion represented a three to four percentage point miss. This was the first time since October 2021 that Apple had fallen short on sales, and it was the worst revenue performance since the September 2016 quarter.

However, reassuring noises on supply chain issues, a strong showing for its services business and

## Shares' 2023 stock portfolio

| | Entry price | Latest (or exit) price | Change (%) |
|---|---|---|---|
| JD Sports* | 114.6 | 161 | 40.9% |
| Shanta Gold** | 9.0 | 12 | 31.4% |
| Walt Disney*** | 85.8 | 108 | 26.0% |
| Apple | 132.4 | 166 | 25.5% |
| ASML | 534.5 | 622 | 16.4% |
| Premier Foods | 107.6 | 123 | 14.4% |
| ME Group International | 113.0 | 129 | 14.2% |
| Prudential | 1049.0 | 1,131 | 7.8% |
| Compass | 1908.0 | 2,021 | 5.9% |
| GSK | 1418.0 | 1,449 | 2.2% |
| **TOTAL** | | | 18.5% |
| FTSE All-Share | 4026.9 | 4,179 | 3.8% |

**JD Sports profit taken 19 Jan. **Shanta profit taken 23 Mar. ***Disney profit taken 16 Feb. On stocks where profit has been taken, the percentage change figures relate to exit point, not latest price (4 Apr). Walt Disney and Apple priced in dollars, ASML in euros, otherwise the rest in pence.*

Table: Shares magazine • Source: Shares, Google Finance. Entry prices taken 20 Dec 2022. Latest prices taken 4 Apr 2023

returning demand from Asia have helped ease any investor concerns.

### TWO UK MID-CAPS SHINE

A pair of UK mid-caps in the portfolio, **ME Group (MEGP)** and **Premier Foods (PFD)**, have delivered impressive returns.

Formerly known as Photo-Me, photo-booth and laundry operator ME Group reported double-digit increases in revenue and profit for 2022 and raised the total dividend paid for the year from 2.89p to 12.1p (factoring in a 6.5p special dividend). The company said it expected pre-tax profit of between £61 million and £65 million for 2023 – ahead of previous consensus forecasts.

Maker of Mr Kipling cakes and Bisto gravy, Premier Foods continues to enjoy positive trading momentum. The company recently said pre-tax profit would be ahead of the previously guided £135 million for the 12 months to 31 March.

### WHAT HASN'T DONE AS WELL?

Catering giant **Compass (CPG)** and Asia-focused insurer **Prudential (PRU)** may not have shot the lights out but have offered solid performance.

Prudential's shares rallied at the start of the year on hopes that business would improve in China following a relaxation of Covid rules. However, they slipped back in February as sentiment soured towards the financial sector and as concern built around unrealised losses in its bond portfolio (something which has hit its peers too). This overshadowed a decent set of results on 15 March. The shares have subsequently started to recover.

Pharmaceutical outfit **GSK (GSK)** is the only notable underperformer versus the FTSE All-Share with a 2.2% gain. The market is perhaps waiting to see the outcome from litigation in the US alleging its heartburn drug Zantac causes cancer. Early signs from legal cases have pointed towards a positive result for GSK.

By **Tom Sieber** Deputy Editor

Editor's View: Daniel Coatsworth

# The Creme Egg effect: 'How do you pick your stocks?'

While there are plenty of ways to take a nibble at the stock market, some methods work better than others

For years, Cadbury's has tempted chocolate fans with its Creme Egg adverts asking, 'how do you eat yours?'. While *Shares* readers may have enjoyed their fill of the gooey stuff at Easter, Cadbury's marketing technique has led me to think about how investors find stocks for their portfolio.

'How do you pick yours?' is an interesting question for investors and one that can probably be put into six buckets: earnings momentum, ratings change, relative valuation, share price performance, director dealings and a good narrative for the company or its sector.

While this is by no means an exhaustive list, it does cover the key methods by which investors seek out ideas and do their research.

Just as there are many ways to eat a Creme Egg and still enjoy its sweet taste, the same applies with investing. There is not a right or wrong way to find an idea, it's all about following a process that works for you.

Some investors are happy to screen the market for stocks trading on lower-than-average valuations, ones that have a history of delivering good returns, or simply jump on the bandwagon and buy shares that are already doing well.

Perhaps less effective is to look at changes in broker ratings. I'm more interested when an analyst does a double upgrade or downgrade which is to move from 'sell' to 'buy' or vice versa, skipping the 'hold' rating entirely, than a rating change up or down one level at a time.

Turning a rating on its head is a more powerful signal to sit up and take notice. However, like many broker calls, the success rate is mixed at best.

Last week we saw a double upgrade for **Direct Line (DLG)** after its share price was obliterated following profit warnings and dividend cancellations, with Citi now implying the motor insurance sector is past the worst following weaker policy pricing. While the shares jumped 6% when the research note was published, other recent examples suggest that double upgrades or downgrades should be taken with a pinch of salt.

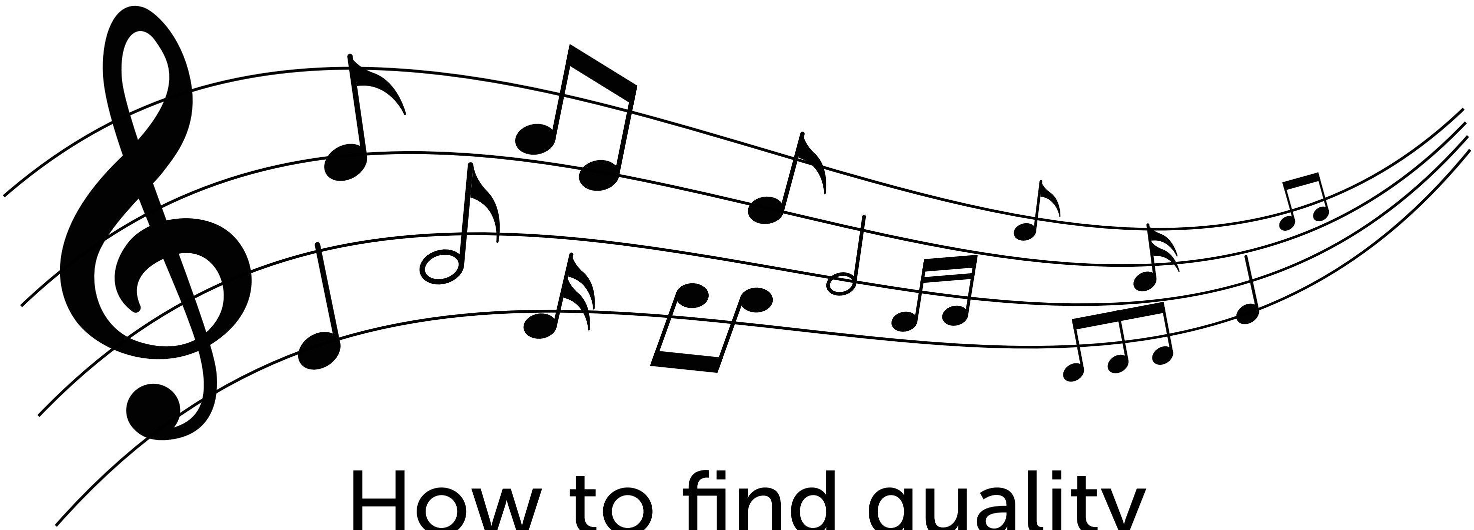

Online furniture seller **Wayfair (W:NYSE)** got a double upgrade from JPMorgan in January, with the analyst saying they were previously negative on the stock in the belief market share gains during Covid were going to fade, earnings estimates were too high and that consumers would return to in-store shopping.

That was correct, but the analyst said more recently Wayfair had started to regain market share and was finding ways to slash costs. They also said the shares had sunk to below pre-Covid levels. The double upgrade caused the shares to soar, but the excitement has since fizzled away and the share price has lost all those broker upgrade-driven gains.

**Tripadvisor (TRIP:NASDAQ)** got a double upgrade from Bank of America in February, from 'underperform' to 'buy', which triggered a 5% rise in the share price on the day. After staying up for a week, the shares then went into a steady decline and are now trading 20% lower than the point of the double upgrade.

It's tempting to eat three Creme Eggs in a row. Equally, it's tempting to blindly follow a broker recommendation with investing. Don't let greed cloud your judgment. Put temptation to one side and think hard about your decisions or you could regret it afterwards.

# SWEET SOUND OF DIVIDENDS



## How to find quality sources of income

The cost-of-living crisis, job insecurity and uncertain economic conditions mean people are eager to find investments that pay a dependable stream of income.

The aim is to find something that can deliver sustained growth in the dividend each year and for the capital value to also grow over time.

## GOLDEN RULE #1

There are three golden rules to follow when searching for quality sources of income. The first is not to become fixated on finding the highest yield possible. Often companies cannot sustain high dividends and cut their pay-out, which in turn can drive down the share price as the stock becomes less attractive to income investors.

It can be better to invest in a company with a lower dividend yield that grows the pay-out rather than one that struggles to pay a generous stream of income.

Ian Mortimer pays close attention to dividend sustainability when picking stocks for the **Guinness Global Equity Income Fund (BVYPP13)**. He looks for quality factors such as a strong balance sheet and robust cash flow.

'We believe that as we navigate the more uncertain economic environment we are currently in, having robust businesses with persistent cash generation underlying the dividend income an investor receives is more important than ever.'

### THREE GOLDEN RULES FOR FINDING QUALITY INCOME

1. **Don't be fixated by finding the highest yield possible**
2. **Consider total return (capital gains and dividends), not just yield when making an investment decision**
3. **Diversify by sector and geography**

## GOLDEN RULE #2

The second golden rule is to consider that returns from an investment come from more than just dividends. Ideally you also want your capital to grow in value.

Ben Peters, manager of **Evenlode Global Income Fund (BF1QNC4)**, says: 'Investors shouldn't just look at the yield of the company when they are making their investment decision but look at the company's growth potential to give them an income and assess whether the business is a stable one.'

That might explain why the Evenlode fund does not invest in banks or energy companies – while they have high dividend yields, they also have unpredictable earnings so it is impossible to call them quality sources of income. Instead, Evenlode invests in companies from the healthcare, technology, business-to-business media, branded consumer goods, medical equipment and services and pharmaceutical sectors.

## GOLDEN RULE #3

The third golden rule for establishing a quality stream of income from your portfolio is diversify your holdings across sectors and geographies. For example, while countries in the West such as the UK and US are experiencing higher interest rates which makes it more expensive for companies to borrow money, rates remain extremely low in Japan. Having a blend of sectors and geographies helps to spread risks.

The FTSE 100 index of UK companies has a reputation of paying decent dividends, currently yielding 3.9%. However, it is not the only source of generous income, with regions like Asia seen as attractive alternatives.

For example, **Murray International Trust (MYI)** generates income for its shareholders via investing in various parts of the world including just over a quarter of its assets in Asia Pacific and a further 13% from Latin America and emerging markets. It invests in both equities and bonds.

'Diversification is important, as data from Abrdn show that over the last decade, the highest market annual returns (in sterling terms) have come from a variety of regions: the United States (five years), which until 2022 had benefited from the strong performance of its major technology companies, Latin America (three years), and Japan and Asia Pacific ex-Japan (one year each),' says Mel Jenner, director of investment trusts at research group Edison.

'Murray's managers seek high-quality, cash-generative businesses, with high returns and above-average dividend yields, which can grow regardless of the economic environment. As quality companies are often fully priced, the managers look for mispriced assets.

'The managers are confident that Murray's portfolio of high-quality assets has the potential to perform relatively well in an environment of higher interest rates and anticipated lower equity returns.'

### WHY QUALITY MATTERS

Market conditions remain unpredictable which is why it can pay to put money into investments that have high quality characteristics.

Mortimer at Guinness says high-quality dividend paying stocks can offer useful defensiveness in volatile times. 'Quality income stocks have persistently high profitability, strong balance sheets, robust competitive advantages and, in certain cases, attractive valuations. As a result, they should offer relative safety compared to companies with greater inflation and interest rate risk such as companies with little pricing power, growth stocks with extreme valuations, and companies with high debt levels.

'Quality companies could prove able to escape the worst of the downward earnings revisions currently seen in the broader market. Inflation has proved stickier than expected, and companies able to effectively pass on price increases, manage costs, or that are in industries less levered to the economic cycle should provide steadier, if moderate, earnings growth potential. This should be rewarded in any period where relative returns are trending lower,' Mortimer concludes.

## FUND OPTIONS FOR INVESTORS

There are ways to obtain exposure to quality sources of income through funds. Products relevant to the theme including **Trojan Global Income (BD82KQ4)** which looks for stocks displaying high returns on invested capital with durable competitive advantages. Names in its portfolio include drinks and snacks group **PepsiCo (PEP:NASDAQ)** which has grown its dividend every year since 1965. The fund yields 3.2%, has a 0.89% ongoing charge and has achieved 55% total return over the past five years.

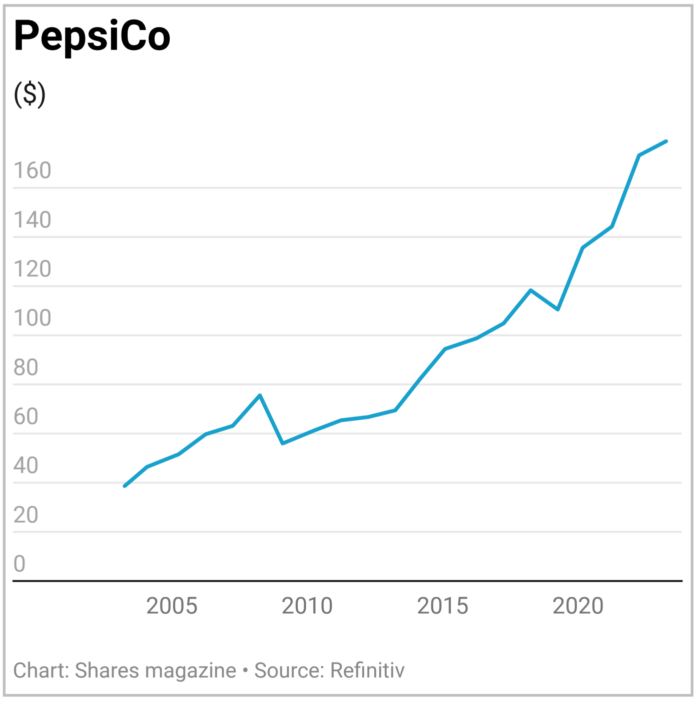



Chart: Shares magazine • Source: Refinitiv

Evenlode Global Income has 45% of its portfolio invested in companies listed in mainland Europe. A further third are in North America and a fifth in the UK. Over the past five years it has delivered a 70% total return. 'Our holdings produce sustainable income and dividends to cope with economic volatility,' says fund manager Ben Peters. The historic yield is 2% and the ongoing charge is 0.84%.

Guinness Global Equity Income has a bigger bias towards US-listed stocks, representing 60% of its portfolio, with the rest spread across Europe, Taiwan and Australia. It has a 2.3% historic yield

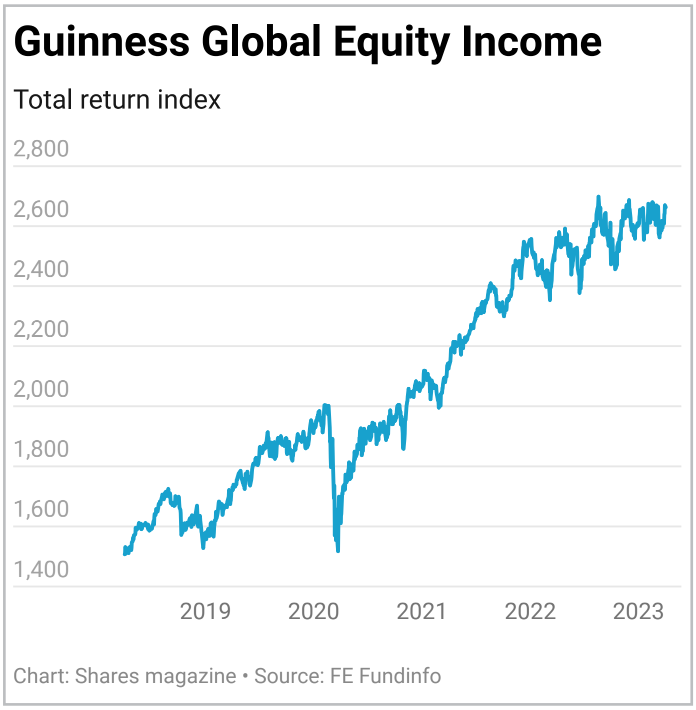


Chart: Shares magazine • Source: FE Fundinfo

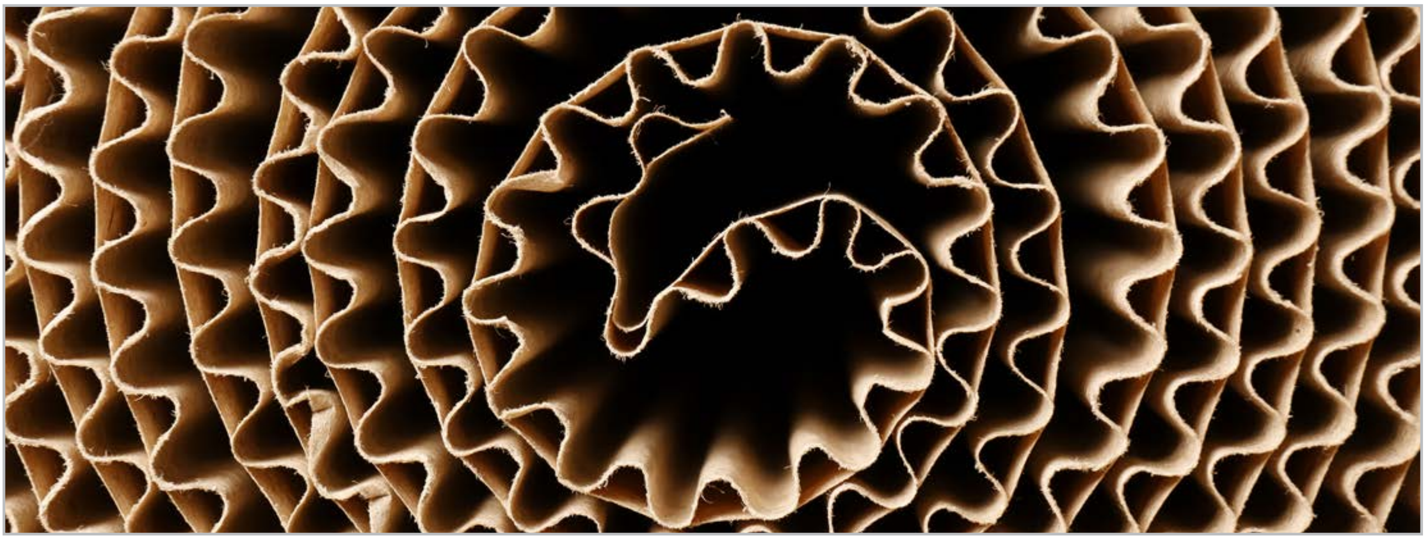
and over the past five years has achieved a 77% total return. The ongoing charge is 0.79%.

Murray International yields 4.1% and has a 0.52% ongoing charge. Holdings include pharmaceuticals group **Abbvie (ABBV:NYSE)** and cigarette maker **Philip Morris (PM:NYSE)**. It has achieved 43% total return over the past five years.

If you do not want to pay a fund manager to run a portfolio, there are a tracker funds on the London Stock Exchange which play to the quality income theme.

For example, **Fidelity Global Quality Income ETF (FGQD)** tracks the performance of an index of the same name. It has a 2.7% yield and 0.4% ongoing charge. The portfolio currently includes **Apple (AAPL:NASDAQ)**, **Nvidia (NVDA:NASDAQ)** and **Procter & Gamble (PG:NYSE)**. It has achieved 71% total return over the past five years.


To qualify for the Fidelity index, companies must pay dividends and they must tick the box for three quality criteria. The screening exercise establishes whether a company is efficient at converting sales to cash, its profitability from capital invested in the business, and its ability to generate positive free cash flow. For banking stocks, the screen looks at return on equity and debt to assets.



## STOCK OPTIONS FOR INVESTORS

Investors who prefer to own individual shares can look at the holdings of the aforementioned funds as part of their research, or they might want to use one of the stock screening services available online.

Stockopedia has a 'Quality Income' screen on its website. This is based on a dividend strategy that focuses on companies with strong fundamentals and higher yields. It uses checklists to identify strong financial health, low bankruptcy risk and high – but not excessive – yields. Eighteen stocks currently meet the criteria including mining group **Glencore (GLEN)**, housebuilder **Barratt Developments (BDEV)** and packaging group **Smurfit Kappa (SKG)**.

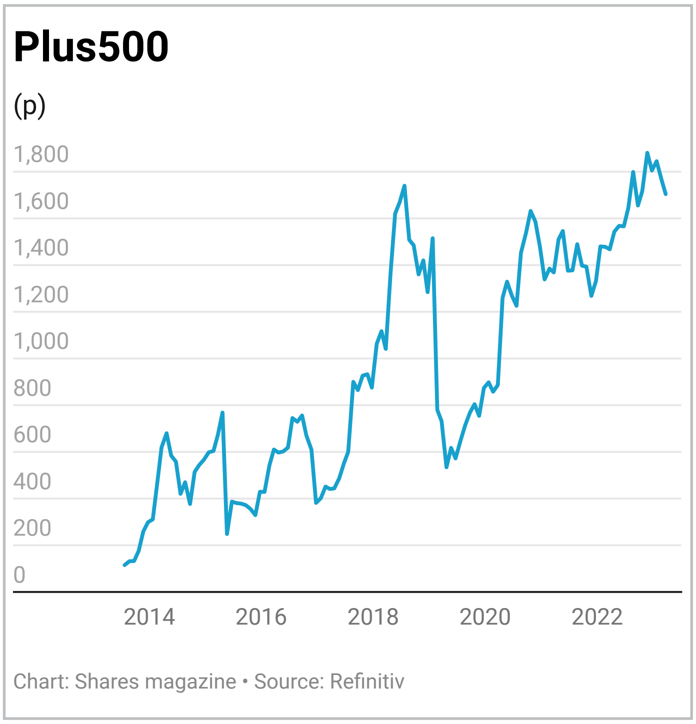
Investors might argue these stocks do not meet the quality criteria given they have unpredictable or cyclical earnings – this stresses the importance of understanding any pre-set screening filters or even what a fund is looking for.

Another screen on Stockopedia's site is 'Winning Growth & Income' which looks for companies with a high yield, an above-average return on equity, a below-average price to earnings ratio and where analysts have been upgrading their earnings forecasts. It also looks for companies whose share price has been less sensitive to movements in the market.

Thirteen companies pass the test including trading platform **Plus500 (PLUS)** and property and casualty insurer **FBD (FBH)**.

If you want to do your own research on a stock-by-stock basis, it is important to dig deep into a company's financials and returns profile.

While investors often check to see the number of times earnings per share will cover the dividend per share – known as dividend cover – it can be better to look at the ratio of free cash flow to dividends.




This is the amount of cash generated from operations minus money needed to keep the business going. Ideally, we want to see at least twice as much free cash flow coming in as dividends going out.

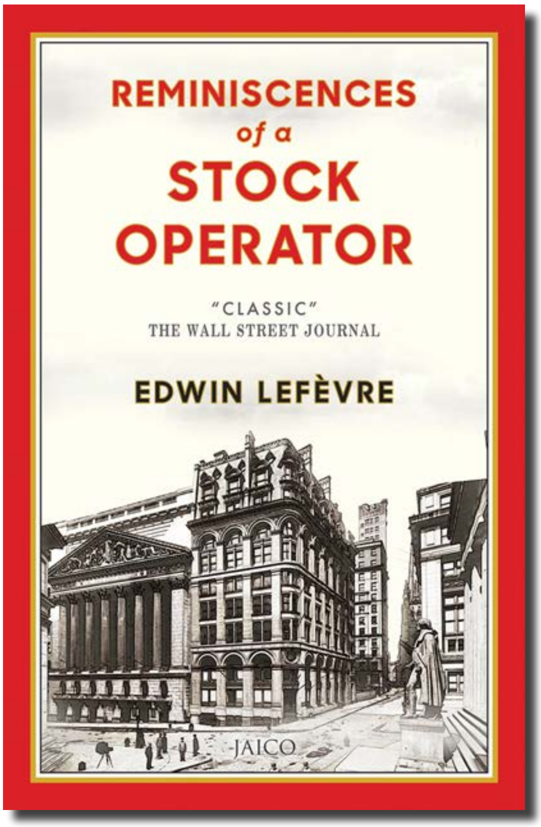
It is also good to look at operating profit margins – a double-digit margin implies a company has money to reinvest in its business, fund debt repayments, pay dividends and/or buy back shares.

***Disclaimer: Daniel Coatsworth, who edited this article, has a personal investment in Evenlode Income.***

By **Sabuhi Gard** Investment Writer

# Celebrating 100 years since classic investment book *Reminiscences of a Stock Operator* was published

A century on, how relevant is it to modern investors?




Whenever there is a poll of the greatest books on the stock market, it is a fair bet that *Reminiscences of a Stock Operator* by Edwin Lefèvre will feature high on the list.

In its centenary year, *Shares* asks whether the book deserves its reputation and if it offers any useful lessons for investors today.

The 'Reminiscences' are the first-hand accounts of a fictional trader called Larry Livingston who began his career as a quotation-board boy in a small broking firm as a teenager.

The subject of the book is famed speculator Jesse Livermore, who allegedly built a $100 million fortune – equivalent to $1.5 billion in today's money – in the decades before the Great Crash in 1929 and is considered one of the pioneers of day-trading.

In the book, Livingstone recounts how he made $1,000 by the age of 15 and then $10,000 by the age of 20 simply by 'reading the tape' and anticipating the market's next move while trading 'on margin'.

'Reminiscences' is first and foremost a romp down Wall Street as it was over 100 years ago, with bucket shops and broking houses on every corner open six days a week including Saturday. Think 'The Wolf of Wall Street' with top hats and frock coats.

As such, there is little in the book for long-term investors, as Livermore is an out-and-out trader, punting in and out of everything from stocks to corn and cotton.

Where the book excels is in its portraits of those who operated in a market which to this day regularly extracts the most money from the least prepared.

There are of tales of old-timers who gave him sage advice, and of those whose advice turned out to be good for nothing, but there is always a valuable lesson, and it is usually that experience comes at a price.

There are also hair-raising experiences – such as when he sells his money-making position in **Union Pacific (UNP:NYSE)** and takes a sizeable short position the day before the company unexpectedly declares a 10% dividend – and the losses he incurs are still large sums of money even by today's standards.

Livermore never reveals his system, but for those who love the cut and thrust of trading he has this advice: 'I have been in the speculative game since I was fourteen. It is all I have ever done, and the conclusion I have reached after nearly thirty years of constant trading, both on a shoestring and with millions of dollars, is this: a man may beat a stock or a group at a certain time, but no living man can beat the stock market.'

By **Ian Conway** Companies Editor

# Finding Compelling Opportunities in Japan

AJOT
AVI Japan Opportunity Trust

Asset Value Investors (AVI) has been finding compelling opportunities in Japan for over three decades. Despite a year filled with challenges and volatility, Japanese equities fared relatively well.

Many investors may be surprised to hear of Japan's resilience during what was a difficult year for global equity markets. After all, Japan has suffered from stagnant growth and an ageing population for a prolonged period of time. However, Japan has a relatively stable economy and the attitude towards corporate governance has improved significantly since the onset of 'Abenomics'. Japan is now the world's second largest activist market. Activist events have risen 110%* over five years, as pressure from shareholders continued to intensify. This was accompanied by a surge in corporate buybacks as cash was returned to investors.

Excess cash is one of the things that the investment team at Asset Value Investors (AVI) look for in Japan. AVI's portfolio of 20-25 stocks are all companies that have been thoroughly examined by the investment team to find value, quality, and an event to realise the upside. Key to the strategy is to build relationships with company management, actively working together to improve shareholder value. While AVI can launch public campaigns, it aims to work behind closed doors with management to find mutually beneficial solutions. The depth of the investment team provides AVI the resources to undertake detailed and targeted research.

In 2022, our engagement was mostly behind the scenes. Over 120 meetings were held with 26 portfolio companies and 24 detailed letters or presentations were sent to these companies. This engagement is well supported by the broader changes in the attitudes of Japanese management as they are encouraged by the Japanese Corporate Governance Code to better allocate capital. The result is long term sustainable improvements in returns for investors.

As anyone who has invested in Japan will know, change takes time. Discovering overlooked and under researched investment opportunities requires a long-term approach. A long-term time horizon aligns AVI with the interests of the management to work together on creating shareholder value.

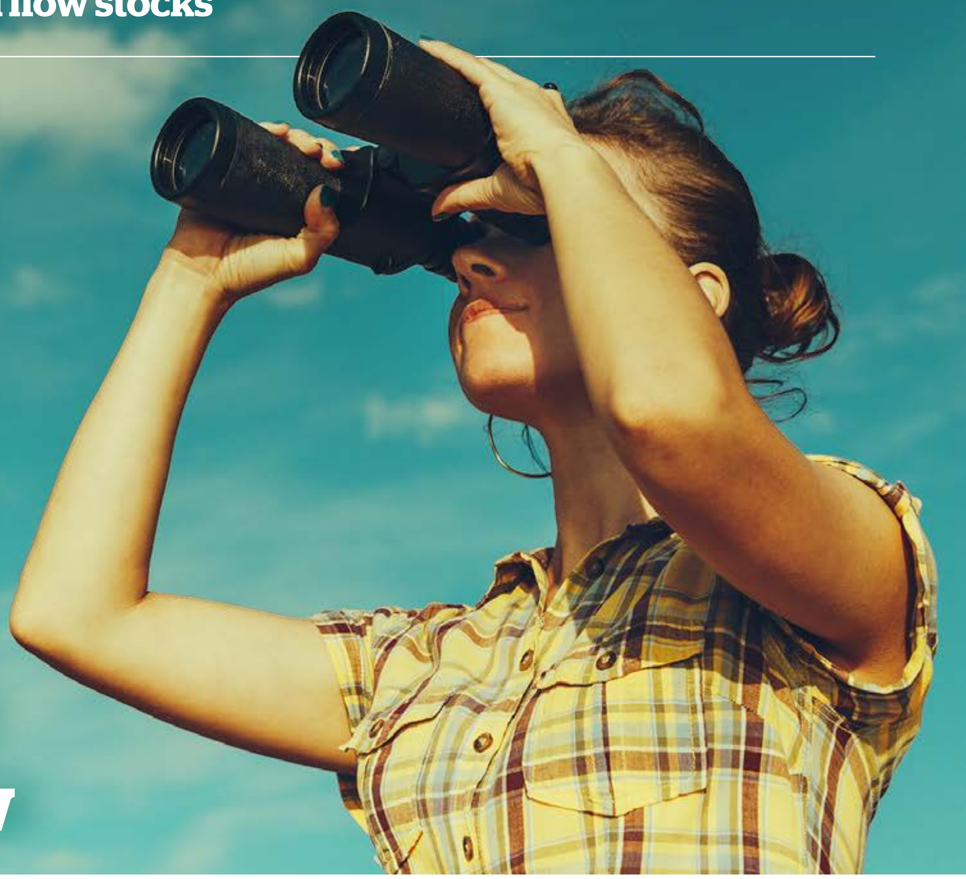
**The companies AVI invests in have cash on their balance sheets and attractive business models with either stable earnings or structural growth trends to ensure corporate value is growing.**

In 2018, AVI launched the now c. £149m* AVI Japan Opportunity Trust (AJOT). The strategy's first four years bears witness to the success of this approach, with a strong NAV total return and outperformance of its Japan small-cap benchmark. AVI's aim is to be a constructive, stable partner and to bring our expertise – garnered over three decades of investing in Japan. We are optimistic about the macro environment in Japan. The weak Yen makes Japan highly cost-competitive, both for tourism and manufacturing. Our portfolio includes a variety of sectors, with strong exposure to the domestic Japanese economy. Inflation has returned after a 40-year absence and with wage growth and increased spending, we expect to see better allocation of capital and improved productivity, which would support returns for investors. AVI is well positioned to capture this long-term opportunity with a unique investment approach and established track record.

Discover AJOT at www.ajot.co.uk

*Source CLSA and AVI, as at 31 December 2022.
Past performance should not be seen as an indication of future performance. The value of your investment may go down as well as up and you may not get back the full amount invested. Issued by Asset Value Investors Ltd who are authorised and regulated by the Financial Conduct Authority.

AVI
Asset Value Investors



# Hunting for companies which look cheap against their cash flow

The transparency of this metric makes it extremely useful in identifying value

Given profit can be subject to alterations and adjustments and presented in a flattering light, trying to find value purely based on the ratio between a company's share price and earnings per share can trip you up.

A solution is to look at firm's cash flow instead. It is best practice to look at free cash flow which is the cash a company generates through its operations minus any capital expenditure. This metric is transparent and companies which produce sustainably high free cash flow year after year are ones with quality characteristics.

Private equity firms often use the free cash flow yield, calculated by dividing free cash flow by the enterprise value of a business (its market valuation plus any net debt or minus any net cash), when assessing targets. They compare the free cash flow yield to the cost of borrowing to make acquisitions.

> "best practice to look at free cash flow which is the cash a company generates through its operations minus any capital expenditure"

To help with idea generation, *Shares* has run a screen of the market using Stockopedia data to identify stocks which look cheap relative to cash flow. Doing homework on the full list we have picked three stocks worth buying.

## SCREENING THE MARKET FOR CANDIDATES

First, we narrowed our search to businesses with market values above £100 million as below this threshold the liquidity of the shares can be an issue and the risks are typically higher. We also stripped out financials and property stocks because the complexity of their balance sheets and accounting can make like-for-like comparisons with other sectors less meaningful.

Next, we looked at firms with a ratio of enterprise value to free cash flow of less than 10 on a trailing 12-month basis – this is our core value metric. We also looked for names with a five-year average return on equity of 6% or more to ensure we are capturing reasonable quality businesses.

Finally, to ensure the amount of cash generated by our businesses is growing, we looked for a positive five-year compound annual growth rate in free cash flow.

This produced a list of 32 names. Housebuilders feature heavily but we are cautious on their immediate prospects for the sector as the housing market begins to show signs of stress.

Resources firms also feature heavily but investors should consider the volatility in the underlying commodities from which they derive their cash flow.

In the end we have arrived at a trio of different businesses, all of which generate good amounts of cash and look cheap relative to this cash flow. [TS]

## CLARKSON (CKN) *£30.45*

Shipbroking and shipping services firm **Clarkson (CKN)** may be over 150 years old, but it knows how to move with the times.

Its investments in technology and solutions mean its clients have been able to ride out the disruption to global trade caused by the pandemic and the invasion of Ukraine, generating record profits of a tick over £100 million for the firm in 2022.

On top of its highly successful broking business, the firm's sale and purchase division had a good year due to the lack of new capacity coming to the market.

Clarkson is also ready for the future with its Green Transition consultancy, which advises clients on the most pressing issue facing the whole transport sector – how to drive down carbon emissions.

Analysts at Canaccord believe the firm's technological edge means cash flow will grow faster than sales, supporting further increases in the dividend which has risen every year for the past two decades. [IC]

### Stocks which are cheap relative to their free cash flow

| Company | 5-year FCF CAGR (%) | Return on equity (%) | EV/FCF |
|---|---|---|---|
| Gulf Keystone Petroleum | 32 | 19 | 1 |
| Impellam | 34 | 6 | 3 |
| Anglo-Eastern Plantations | 67 | 10 | 3 |
| Sylvania Platinum | 47 | 26 | 3 |
| Kenmare Resources | 68 | 9 | 3 |
| Clarkson | 33 | 6 | 4 |
| Tremor International | 18 | 9 | 4 |
| Shell | 25 | 9 | 5 |
| Shoe Zone | 33 | 13 | 5 |
| Crest Nicholson | 20 | 7 | 6 |
| Card Factory | 8 | 14 | 6 |
| Central Asia Metals | 16 | 15 | 6 |
| Ecora Resources | 8 | 10 | 6 |
| Barratt Developments | 0 | 12 | 7 |
| DS Smith | 12 | 9 | 7 |
| Luceco | 37 | 26 | 7 |
| Playtech | 6 | 13 | 7 |
| Epwin | 15 | 11 | 7 |
| Iomart | 4 | 11 | 8 |
| Andrews Sykes | 17 | 26 | 8 |
| DFS Furniture | 13 | 8 | 9 |
| Imperial Brands | 1 | 31 | 9 |
| James Latham | 38 | 17 | 9 |
| Sureserve | 5 | 12 | 10 |
| Pagegroup | 19 | 28 | 10 |
| Inchcape | 10 | 8 | 10 |
| Mondi | 10 | 19 | 10 |
| Science | 14 | 11 | 10 |
| Future | 92 | 9 | 10 |
| Hollywood Bowl | 29 | 15 | 10 |
| Glencore | 50 | 11 | 10 |

*FCF=free cash flow, EV=enterprise value, CAGR=compound annual growth rate. EV/FCF is based on trailing 12 month data*

Table: Shares magazine • Source: Stockopedia, data to 3 April 2023

## HOLLYWOOD BOWL (BOWL) *232.5P*

Ten-pin bowling and mini-golf centre operator **Hollywood Bowl (BOWL)** has grown free cash flow by around 28% a year over the last five years, demonstrating its cash generating characteristics.

The company provides an affordable treat for families which means the business should remain resilient should the economy falter from rising interest rates.

Hollywood Bowl is more profitable than before the pandemic, generating EBITDA (earnings before interest, tax, depreciation and amortisation) for the financial year ending 30 September 2022 of £61 million against £38 million in the last pre-pandemic financial year.

Despite strong performance the shares remain valued below 2019 levels with a price to earnings ratio of 13.4 times compared with 14.4 times in 2019 based on forecasts for the 12 months to 30 September 2023.

This looks far too grudging given a plan to open 12 new centres across the UK out to September 2025 and the opportunity to consolidate the Canadian market which the company entered in May 2022. [MG]

## SHOE ZONE (SHOE:AIM) *240P*

Value footwear retailer **Shoe Zone's (SHOE:AIM)** incredibly cash-generative business model has delivered a five-year free cash flow compound annual growth rate of 33% according to Stockopedia.

A discounter in the relatively non-discretionary footwear category, Shoe Zone does an exceptional job of managing its direct-from-factory supply chain and keeps a tight lid on costs across the business. This includes reducing its rent bill through proactive discussions with landlords with an average lease length of just 1.8 years giving the retailer the flexibility to respond to changes in any retail location at short notice.

Debt free once again and back on the dividend list after a pandemic-induced hiatus, Shoe Zone is returning capital to shareholders through ordinary and special dividends as well as a share buyback programme that started in August 2022.

Prospects look solid with Shoe Zone profiting from the cost-of-living crisis as families on a budget trade down to cheap shoes, boots, trainers and slippers. The company is also benefiting from the post-pandemic return to physical stores, store refits and investments to improve digital efficiency. [JC]


By **The *Shares* Team**

# How Jupiter UK Special Situations keeps on delivering strong returns

Discover the philosophy and process behind value investor Ben Whitmore's good performance

One of the outstanding long-run performers in the Investment Association's UK All Companies sector is **Jupiter UK Special Situations (B4KL9F8)**, the £2.1 billion fund managed by Jupiter Asset Management.

Adorned with a five-star Morningstar rating and a Gold Morningstar analyst rating, the fund is ranked first quartile over one, three, five and 10 years, and year-to-date.

It is managed by the highly-regarded Ben Whitmore (*pictured*), who seeks to generate a higher return than that provided by the FTSE-All Share index over at least five years and deliver capital growth by exploiting 'special situations', which means UK companies he considers to have undervalued share prices.

Jupiter UK Special Situations has delivered an impressive 10-year annualised total return of 7.3%, which rises to 18.6% on a three-year basis as value investing has enjoyed a renaissance. This is comfortably ahead of Morningstar's UK Large-Cap Equity category over both timeframes.

## DISCIPLINE AND PATIENCE

'We are value investors,' Whitmore informs *Shares*. 'We believe that valuation is the key determinant of future returns and there's a lot of evidence around value investing over time.' Disciplined and patient in their search for value, Whitmore's team use statistical techniques to 'screen' companies for certain characteristics and narrow their search for the best value opportunities.

They look for low valuations as their starting point using a couple of screens. The first is a Benjamin Graham and David Dodd-inspired screen, popularised more recently by Robert Shiller as the cyclically-adjusted price to earnings CAPE ratio, while the second is based on the methodology of successful investor Joel Greenblatt.

'One of the things Graham and Dodd suggested is you want to look at a company's earnings power across a business cycle,' explains Whitmore, who looks at valuations on 10-year average earnings. The Jupiter stock picker doesn't waste time over macroeconomic forecasting. 'It is too difficult,' he says. 'The area to concentrate on is individual companies.'

### Top 10 holdings

(as at 28 Feb 2023)

| | |
|---|---|
| BP | 6.0% |
| Standard Chartered | 5.0% |
| Shell | 4.4% |
| Imperial Brands | 4.3% |
| GSK | 4.0% |
| WPP | 3.4% |
| HSBC | 3.1% |
| Bayer | 2.8% |
| Aviva | 2.7% |
| Centrica | 2.6% |

Table: Shares magazine • Source: Jupiter Asset Management

He focuses on screening for 'out of favour, lowly valued' but strong-at-heart businesses which he believes will be rerated over time. As at 28 February 2023, the fund was spread across 48 holdings, the bulk of them large and mid cap companies.

These companies have become lowly valued for different reasons, falling out of favour with investors because profits are falling or 'the stock market doesn't like them, and that might be caused by bad management or just the economic cycle', he continues. 'What we tend to find is that unpopular shares have got problems or some issues and that can often lead to a change in management.'

### NUMBERS OVER NARRATIVE

Jupiter UK Special Situations' consistently robust returns are all the more impressive given the five years to 2020 was 'the worst period in financial markets history going back to 1920 for value investors versus growth investors', according to Whitmore. Value investors just have to accept there will be periods when their style is out of favour. 'For us, it is about trying to be very consistent with the philosophy and process,' he stresses.

There will be periods when 'judged against the index, we look not very good, periods when we look better, but cumulatively over time, we have shown that our philosophy and process adds up to a good outcome' for investors. Rather than a 'buy-and-hold forever investor', Whitmore waits for extreme undervaluation to normalise and says the sweet spot for the companies he invests in, 'if we're correct, tends to be 18 months to three years'.

## Jupiter UK Special Situations

Total return index


Chart: Shares magazine • Source: FE Fundinfo

## Jupiter UK Special Situations returns versus its benchmark

| | FTSE All-Share | Jupiter UK Special Situations |
|---|---|---|
| 1 year | 2% | **11%** |
| 3 years | 55% | **75%** |
| 5 years | 26% | **34%** |
| 10 years | 81% | **107%** |

*Data to 6 April 2023. Total return*

Table: Shares magazine • Source: FE Fundinfo

Whitmore is also 'a great believer in the numbers not the narrative', refusing to be unduly influenced by CEOs with the gift of the gab. 'Meeting management when they are new to a situation is quite helpful because they give you balanced account of the business,' says Whitmore, but he has become more nervous about putting too much faith in what management have to say about the future.

'We want to see the 10-year history in terms of numbers for all companies we consider.'

The Jupiter man starts with forensic scrutiny of the balance sheet, the cash flow statement and the profit and loss account. The focus is purely on the statutory numbers not those which have been adjusted by management.

### PORTFOLIO POSITIONS

Jupiter UK Special Situations is invested in names ranging from energy giant **BP (BP.)** and mining group **Rio Tinto (RIO)** – to banking provider **HSBC (HSBA)**, insurer **Aviva (AV.)** and drugs specialist **GSK (GSK)**.

Interestingly, Whitmore sold shares in Sensodyne-to-Panadol maker **Haleon (HLN)** following its spin-out from GSK as they were 'too expensive for us' and he saw 'better opportunities' elsewhere. Among the strong recent contributors is **BAE Systems (BA.)**, the defence giant that has been 'sharply reappraised as to the valuation of its franchise'. Whitmore initiated the position in the FTSE 100 firm 'about four or five years ago' when the shares were very lowly valued and seen as 'exceptionally dull, but people now understand that the defence of the free world is very, very important'.

While at least 70% of the fund is invested in UK stocks, up to 30% of the portfolio can be allocated to other assets including overseas-based companies. Whitmore initiated a position in microchips giant **Intel (INTC:NASDAQ)** in 2022 on the basis of its strong franchise and attractive valuation.

Intel's poor performance over the last six to nine months reflects worries about a correction in demand for PCs and Whitmore recalls that Intel slipped up and lost its way about five years ago, making missteps in its process technology and losing the lead over **Taiwan Semiconductor Manufacturing Company (2330:TPE)**.

But new management led by CEO Pat Gelsinger is trying to 'put Intel back on a better path'. Patient investor Whitmore believes that if Intel can turn things round, the upside is 'very considerable' and if not, the downside is 'limited'. His team are always thinking about the 'asymmetry of risk/reward and trying to find companies where we think the upside is a multiple of the downside'.

One rival fund manager recently described **Imperial Brands (IMB)**, a top 10 position in Jupiter UK Special Situations, as a 'burning platform'. The thoughtful Whitmore concedes that tag would have been accurate a few years ago, but the cigarettes maker is now on a firmer footing, able to make investments to help it transition from a heavy reliance on cigarettes to next generation products.

Previously, Whitmore observes, the Davidoff, John Player Special and Lambert & Butler maker was losing market share in most of its key markets and spending money, not very wisely as it turned out, on next generation products.

But new management, steered by CEO Stefan Bomhard, have got to grips with the business in Whitmore's view and Imperial is now taking market share in aggregate across its top five categories, not in each one, but in aggregate, and the fundamentals of the business are much improved in terms of how it is run. Imperial Brands was late to next generation products, but Whitmore notes the new management team is

'trialing and testing and launching, and they want to be a "fast-follower" in heat-not-burn, vaping and oral'.

## NERVES OF STEEL

Whitmore's other holdings include HSBC, the global banking giant whose UK subsidiary recently stepped up and paid £1 to take over the UK arm of Silicon Valley Bank.

He points out that in the last six years, SVB was growing its assets very fast, by 30% per year in fact, and 'very fast growing banks or insurance companies are dangerous'. He notes in contrast that HSBC's balance sheet has hardly grown in the last six years. 'Well-run banks can deliver good returns,' he argues.

He is also backing new management to turn things round at **Smith & Nephew (SN.)**, the medical devices company where one of three divisions has proved problematic. 'Two of the divisions have done very well – Advanced Wound Management and the sports injury business (Sports Medicine),' explains Whitmore, adding that the Orthopaedics business has been poorly run.

He also points out that Smith & Nephew has had too much inventory, what it had got wasn't in the right place, and Smith & Nephew hasn't been able to provide the right inventory sets to the surgeons at the right time, especially in the US. 'That has meant that when procedures were fast to recover post-Covid, Smith & Nephew did not recover as fast, but the new management team has got a plan to put that business back into a better position.'

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

Kepler | Trust Intelligence



# A new frontier for income investors

**The managers of Middlefield Canadian Income think valuations and a new immigration policy put this little known destination for UK investors in an attractive position...**

In his book '*The Intelligent Investor*', Benjamin Graham claims that a defensive investor should follow a few rules when investing in equities. In the copy of the book I own, which was updated in 1971, one of these was to only invest in companies that had a dividend track record dating back to 1950.

Diktats like these can seem silly given the dynamism that markets exhibit. However, you get the sense that Graham may have been on to something if you compare the returns of the S&P 500 with the S&P 500 Dividend Aristocrats Index, which is comprised of US-listed firms that have paid a rising dividend for at least 25 consecutive years.

From the end of 1992 through to the end of 2022, the dividend index delivered annualised total returns of 17.33% in dollar terms. The S&P 500 returned an equivalent return of 14.8% over the same period. What this arguably reflects is the quality of reliable dividend payers, who must generate consistent positive, excess cashflows so that they can make those payments to shareholders.

That is something which has also been demonstrated over the past 18 months. Even with inflation and interest rate hikes, companies in the Aristocrats index delivered positive total returns from the start of Q4 2021 through to 20/03/2023, at the same time as the S&P 500 declined. Similarly the much maligned FTSE 100 has hit a record high.

Less discussed has been Canada. Perhaps because the North American news flow is so dominated by its southerly neighbour, investors may not be aware of the strong dividend culture that the country's stock market has.

But as with the other indices mentioned above, the S&P/TSX Composite Index has delivered positive total returns over the past 18 months. Like the UK, that has partly been fuelled by sizeable weightings to commodities and financials, both of which may be better able to handle the economic problems we're facing today.

These are some of the opportunities that **Middlefield Canadian Income (MCT)** tries to tap into. The trust aims to pay consistent dividends to shareholders by investing in Canadian companies. The trust yields 4.6% as at 20/03/2023 and has a portfolio concentrated in energy, financials and real estate.

Manager Dean Orrico is careful about avoiding value traps and so firms in the portfolio must have strong balance sheets and sustainable cash flows. Firms that use debt financing to cover their dividends, for example, would immediately raise red flags with the team.

Having said that, there are plenty of signs that Canadian companies today offer good value, not value traps. If you factor out technology, which tends to inflate US valuations, Canadian firms are still trading at two or three multiples lower than their US peers on a price-to-earnings basis.

Financials, which MCT has a 20% weight to, are arguably a good example of the opportunities these lower valuations present for income investors. Canadian firms have proven to be extremely robust in the past, with the major banks not cutting dividends in the financial crisis or during the pandemic.

Another area Dean believes is particularly interesting is real estate, a sector that Middlefield specialises in and to which MCT is substantially overweight relative to its benchmark. Listed housing funds in Canada have seen their discounts widen substantially due to interest rate hikes. In some instances shares were trading at 50% of net asset value (NAV).

Income investors may find this an interesting moment at which to look at the trust as a result. Large sell offs have already taken place over the past 12 months, with the existing discount potentially providing some cushion against further volatility. At the same time, the managers adding to existing positions and buying substantial amounts of shares in the trust itself demonstrate that they believe valuations are attractive.

None of this is a guarantee of returns but for investors who believe Graham's views are as relevant today as they were in 1971, MCT's focus on dividends and the lower valuations on offer, both in the Canadian market and via the trust's discount, may be appealing.

Click **here** to read our latest research on Middlefield Canadian Income...

## Danni Hewson: Insightful commentary on market issues

# Space investing comes crashing back down to earth after Virgin Orbit bankruptcy

Nascent industry has significant potential but it's unclear when ordinary investors will see any kind of return


**Virgin Orbit**

($)


Chart: Shares magazine • Source: Refinitiv

Satellite firm **Virgin Orbit's (VORB:NASDAQ)** filing to the SEC on the day it announced it was entering Chapter 11 bankruptcy protection laid bare the mountain the company had been trying to scale.

The company expected revenues for 2022 to be in the region of $30 million but overall Virgin Orbit expected to post a loss more than six times that figure.

Space is an expensive business; in the past the huge costs meant it was the provision of just governmental organisations, but the potential of large profits has drawn in some of the world's richest investors.

But those investors need to have very deep pockets and an endless supply of patience.

On paper Virgin Orbit's business model makes sense. Space data analysts Euroconsult expect that by 2030 there will be around 1,700 satellites needing a piggyback to orbit every year as increasingly our lives rely on technology. Virgin's USP was flexibility, but by the time of its IPO in December 2021 risk appetite was already beginning to wane and the window of opportunity was starting to close.

January's failed UK launch undoubtedly hammered another nail into Virgin Orbit's prospects but the company was already coming under increasing pressure from Elon Musk's SpaceX. After smashing the record for the number of satellites launched on one rocket in 2021, the latter hit new highs in 2022 with a record number of orbital launches.

### THE SPACEX FACTOR

With scale comes an ability to cut costs and the company's ride-share option now starts at as little as $275,000. SpaceX is a dominant force and Musk has shown little inclination for taking it public, saying its long-term goals are not in line with the short-term demands of the being a public company listed on the stock market.

Whether it is profitable or not is impossible to pinpoint but **Tesla (TSLA:NASDAQ)** has proved that Musk is magnate for retail investors and institutional investors alike. SpaceX is undoubtedly the best-known name in the space game, but in the absence of a pending IPO there are limited ways for retail investors to buy in right now, bar Virgin Orbit's sister company, space tourism outfit **Virgin Galactic (SPCE:NYSE)** whose own shares are down more than 60% over the last 12 months.

There is a lot of risk involved in space investments so most should be treated as an investment moon-shot; small, speculative additions to a diverse portfolio but being part of that one small step will be alluring, especially with NASA working on plans to take people back to the moon.

### LIMITED OPTIONS FOR INVESTORS

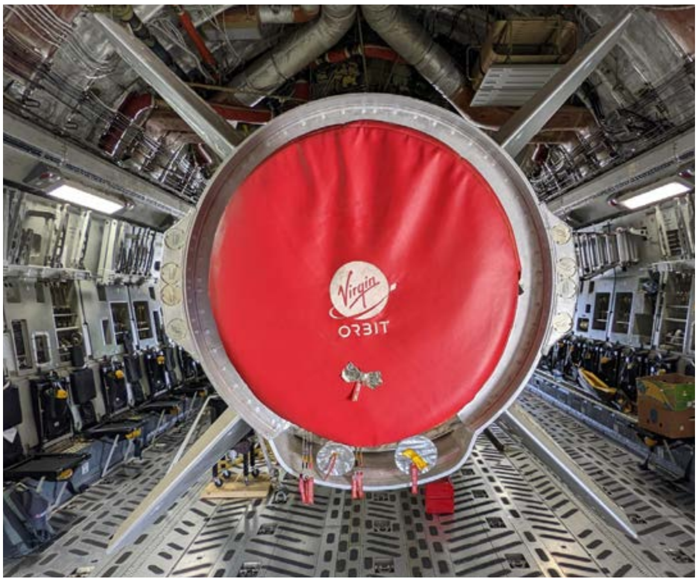
Euroconsult recently published the ninth edition of its annual space market overview. This estimated the global space economy was worth $424 billion in 2022 – implying annual growth of 8% which is significant by any standards.

For those put off by the big money being lost by players like Virgin Orbit an investment trust like **Seraphim Space (SSIT)** provides the option to invest in a whole galaxy of smaller companies, though the risk profile is still elevated and is reflected in the shares trading on a 61% discount to net asset value according to data from the Association of Investment Companies.

The portfolio reads a bit like a Star Trek script with fantastic names like ICEYE, Constellr and D-Orbit. All promise a riff on the same theme – ground-breaking, next generation technology for tomorrow's world.

### OTHER PARTICIPANTS

For more cautious investors, some existing defence stocks like **BAE Systems (BA.)** could provide exposure to the space race in a more traditional way. The company announced it will launch its first multi sensor satellite cluster into low earth orbit in 2024 which will provide military customers with 'information and intelligence'.




BAE Systems snapped up In-Space Missions in 2021 and is working on integrating that into its extensive operations and by doing so it could become a key building block of those UK space ambitions that were so rudely crushed by Virgin Orbit's failed Cornwall launch in January.

By chance one of the biggest companies in Seraphim's portfolio, ICEYE is working with BAE on its Azalea project.

This is tomorrow's world, but we know how quickly tomorrow's technology becomes ingrained today.

Some analysts have pointed out that the space sector is looking an awful lot like the commercial air travel sector after World War II – poised for massive growth. However, it is still unclear who the winners will be and when investors will start to see any meaningful returns.

# Investors hope for brighter future with cannabis stocks after two years of pain

According to Grand View Research the global medicinal cannabis market is expected to grow at 21.8% a year to 2030

Cannabis stocks have been through the classic stages of the hype cycle – rallying on expectations for big things and crashing as they don't live up to earlier promises. Many investors have lost interest but some are still holding out for a rebound thanks to pockets of positive news.

A good example is medicinal cannabis supplier **Celadon Pharmaceuticals (CEL:AIM)** which jumped as much as 124% on 14 March after the Home Office updated its licence, enabling the firm to start the commercial supply of medical cannabis.

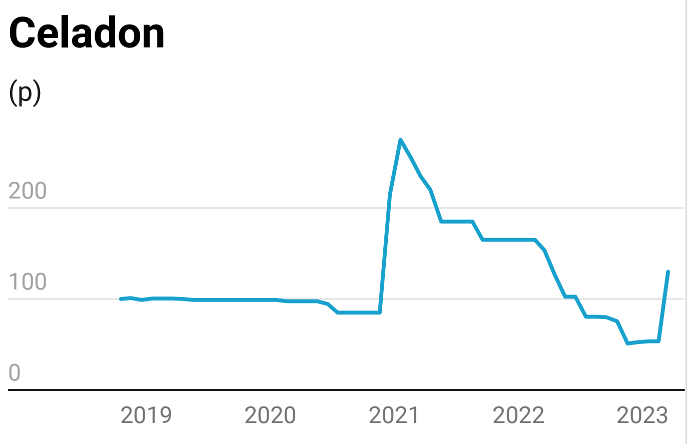


Chart: Shares magazine • Source: Refinitiv

This follows the company's registration as a GMP (good manufacturing practices) manufacturer by the UK Medicines and Healthcare Products Regulatory Agency.

The directors believe it is the first GMP registration for a UK pharmaceutical facility to supply high tetrahydrocannabinol cannabis containing an active pharmaceutical ingredient since the legalisation of medical cannabis in 2018.

While the news for Celadon has been positive, its shares had previously spent two years in freefall, much like the wider sector. Most cannabis stocks and cannabis-themed tracker funds remain around 75% below the peaks reached in February 2021.

*Shares* highlighted the long-term potential for the sector in April 2021 but also cautioned the road ahead could be rocky because of its fledgling state and the challenges stemming from the negative image associated with cannabis.

In hindsight, it didn't help that cannabis stocks got caught up in the meme stock mania during Covid lockdown which pushed share prices to unsustainable levels.

Trying to pick the best stocks among the few quoted players seemed a herculean task in 2021 and looks even more so today. Therefore, anyone who wants to have exposure might be better off considering a fund that provides diversified exposure to the broad medicinal cannabis and life sciences market rather than picking individual shares.

At $2.95, the price of **Rize Medical Cannabis and Life Sciences ETF (FLWR)** sits roughly where it was before the onset of the global pandemic, having peaked at more than $10 in 2021.

Its top holdings have changed slightly with a bigger exposure to large healthcare stocks such as **PerkinElmer (PKI:NYSE)** and Irish-based over-the-counter wellness products firm **Perrigo (PRGO:NASDAQ)**.

The biggest change is that speciality gardening company GrowGeneration is no longer the fund's largest holding and has dropped from 23% of the fund to 6% of assets.

Its largest holding is **Jazz Pharmaceuticals (JAZZ:NASDAQ)** which purchased GW Pharmaceuticals (the fund's former largest holding) which provided it with a world-leading cannabinoid science platform.

While the general performance of cannabis stocks has been very disappointing the industry's growth potential is still significant.

By **Martin Gamble** Education Editor

# Can you crystallise a pension without taking out any cash?

Our resident pensions expert Tom Selby has the answer

*You recently mentioned holding off crystallising a pension until after 5 April if it would otherwise use up your lifetime allowance. Can you crystallise a pension by taking a small portion under drawdown and taking out no cash? If so, would this mean the pension is not subject to any future lifetime allowance test if it were to be reintroduced?*
***Nick***

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

For the 2023/24 tax year, the lifetime allowance tax charge has been abolished, with the maximum tax-free cash someone can take held at £268,275.

The term 'crystallising' usually refers to choosing a retirement income route for your pension pot. The most common actions that lead to a 'benefit crystallisation event' include taking your tax-free cash, entering drawdown, taking an ad-hoc lump sum direct from your pension, and buying an annuity from an insurance company. 'Crystallising' means committing your fund to drawdown – there is no obligation to actually take an income.

When one of these benefit crystallisation events takes place before 6 April 2024, the amount of lifetime allowance you use at that point will be tested by your scheme administrator and reported to HMRC. Prior to 6 April 2023, if you exceeded your lifetime allowance, you would have been subject to a lifetime allowance tax charge. However, in the 2023/24 tax year this tax charge is removed.

There is also a lifetime allowance test at age 75 designed to capture any pensions that had not yet been crystallised and any growth on funds remaining in pensions in drawdown. Where someone dies before age 75, a lifetime allowance test will be carried out on any uncrystallised funds.

The abolition of the lifetime allowance charge means that in 2023/24 these tests will be less of an issue. However, you still need to provide information on lifetime allowance usage and any lifetime allowance 'protection' you have to your provider when you access your pension. If the lifetime allowance is exceeded and you choose to take the excess as a lump sum (rather than to provide an income), then although the excess will not be subject to a lifetime allowance charge, it will be subject to income tax.

I cannot tell you how any future lifetime allowance test might work. It is possible that a Labour government would attempt to reintroduce the lifetime allowance framework that existed before 6 April 2023, but it could feasibly make changes to capture any actions it feels were designed to dodge its policy intention in the interim.

It is sensible to deal with the tax rules as you see them, rather than trying to make decisions today to avoid some possible future tax system of which we have no detailed knowledge.

## DO YOU HAVE A QUESTION ON RETIREMENT ISSUES?

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

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

# Want to spring clean your portfolio? Here are six areas to consider


April is the perfect time to give your ISA, SIPP or dealing account a health check

## HOW TO SPRING CLEAN YOUR PORTFOLIO

If you're flitting around the house this April, brandishing a feather duster and a mop, spare a thought for your investments, which may need a bit of sprucing up too.

Even the most considered portfolios still need regular reviews, in order to keep them on track and to ensure there are no dusty corners.

There is no need to make changes simply for the sake of it, but equally you might find a few holdings in your portfolio which leave you scratching your head as to why they are there. To add some structure to the process, it might help to consider six key questions.

**1. Has your personal situation changed?**

Probably the most important thing to assess is whether there have been any material changes in your personal situation. Getting married, having a child, or buying a bigger house can have an impact on your finances, such as your life insurance requirements, and the need to update your will.

But life events might also affect how much risk you're willing to take with your investment portfolio. For instance, if you're approaching retirement, you might need to think about dialling risk down a bit.

By contrast, if you've received a healthy inheritance, you might find you're willing to stomach more volatility because financial pressures have eased. Consider what, if anything, has changed personally, and how this might affect your attitude to risk and your financial goals.

**2. Has your portfolio become bent out of shape?**

Market prices aren't static, and as a result, neither is the shape of your portfolio. Over short periods this won't make much difference, but given time, the equilibrium in your portfolio can be lost as some bits move up faster than others.

Regular rebalancing is an important discipline to keep your portfolio in good order. Consider the regional split of your portfolio, as well as the allocation across asset classes.

You should also consider whether any sectors have performed particularly well, and now make up an outsized part of your portfolio.

Finally, see if any specific funds have done a lot better than others and now constitute a large part of your portfolio. That's clearly a good sign, but it's worth making sure that your returns are not too heavily reliant on just one fund manager, no matter how good they are, because even the very best can go off the boil.

**3. Do you own any serially poor performers?**
At the other end of the spectrum, you should check your portfolio for any serially poor performers. These are not funds which have had a bad year, or even three years, which can happen simply because their investment style is out of favour. Rather funds of concern will be those which have lagged behind competitors for a long period and show little sign of change for the better.

You should consider replacing duds with more promising active funds, or cheaper tracker funds, which won't outperform, but at least aren't charging the higher fees associated with active management.

**4. Is the investment case still solid?**
As well as inspecting performance, it is worth checking the fundamental reasons you bought an investment are still in place.

For funds and investment trusts, check there hasn't been a change in fund manager or strategy, and if there has, consider whether it's still fit for purpose.

For shares, reflect on whether the reason you bought an investment has now run its course, or has still got some legs. Also consider if the business has undergone a material change in strategy or circumstances which make it a less attractive investment proposition.

**5. Have any new ideas or opportunities cropped up?**
A portfolio review is a decent time to scout around for new investment ideas, which might replace funds or stocks you're selling.

Are there any emerging trends you might want to buy into? Or are there any fund managers who have finally clocked up a long enough performance record to merit inclusion in a portfolio?

One thing which has changed dramatically over the last year is the bond market. There has been a big fall in bond prices and a rise in yields. Those who have shunned bonds as part of the diversification in their portfolio, preferring instead perhaps property, gold, cash, or absolute return funds, might think about putting bonds back on the menu.

**6. How can I reduce my tax bill?**
The final piece of the jigsaw is to make sure your portfolio is invested as tax efficiently as possible. A new tax year means fresh pension and ISA allowances, which will protect your investments from capital gains tax and income tax once they're wrapped inside the tax shelter.

This year tax planning feels particularly relevant because the capital gains tax allowance is being cut from £12,300 to £6,000, and the dividend allowance is being cut from £2,000 to £1,000.

These allowances will fall to £3,000 and £500 respectively from April 2024, and any gains or dividends above these amounts are taxable if held outside of a tax shelter. The sooner you put your investments inside the ISA or pension, the sooner the protection kicks in.

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

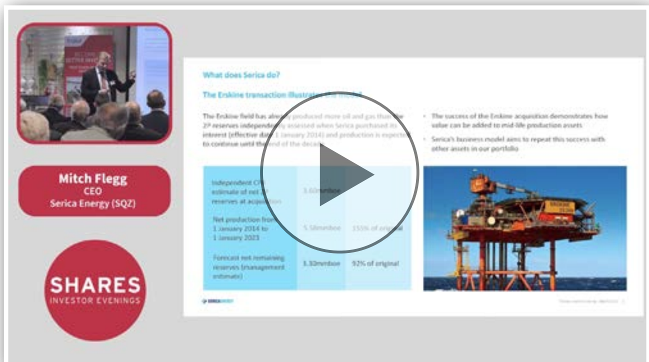

# WATCH RECENT PRESENTATIONS


**Mercia Asset Management (MERC)**
Dr. Mark Payton, CEO & Martin Glanfield, CFO

Mercia Asset Management is a proactive, specialist asset manager focused on supporting regional SMEs to achieve their growth aspirations. Mercia provides capital across its four asset classes of balance sheet, venture, private equity and debt capital; the Group's 'Complete Capital Solution'.


**Reabold Resources (RBD)**
Sachin Oza, Co Chief Executive & Stephen Williams, Co Chief Executive

Reabold Resources is an investment company in the natural resources sector. The principal activity of the company is an investment in pre-cash flow upstream oil and gas projects, primarily as significant minority interests in unlisted oil and gas companies or majority interests in unlisted oil and gas companies with non-operating positions on licenses.




**Serica Energy (SQZ)** Mitch Flegg, CEO

Serica Energy is a British independent upstream oil and gas company with operations focused on the UK North Sea, where our assets span the full cycle of exploration, development and production. Our main aim is to build a portfolio of assets which enables the company to utilise its technical and commercial experience to add value to existing producing assets, as well as to explore and develop new reserves.

**Visit the Shares website for the latest company presentations, market commentary, fund manager interviews and explore our extensive video archive.**

CLICK TO PLAY EACH VIDEO

SHARES SPOTLIGHT

**www.sharesmagazine.co.uk/videos**

# Index













## 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

**INVESTMENT WRITER:**
Sabuhi Gard
@sharesmagsabuhi

**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



Shares magazine is published weekly every Thursday (50 times per year) by AJ Bell Media Limited, 49 Southwark Bridge Road, London, SE1 9HH. Company Registration No: 3733852.




## DISCLAIMER

Shares publishes information and ideas which are of interest to investors. It does not provide advice in relation to investments or any other financial matters. Comments published in Shares must not be relied upon by readers when they make their investment decisions. Investors who require advice should consult a properly qualified independent adviser. Shares, its staff and AJ Bell Media Limited do not, under any circumstances, accept liability for losses suffered by readers as a result of their investment decisions.

Members of staff of Shares may hold shares in companies mentioned in the magazine. This could create a conflict of interests. Where such a conflict exists it will be disclosed. Shares adheres to a strict code of conduct for reporters, as set out below.

**1.** In keeping with the existing practice, reporters who intend to write about any securities, derivatives or positions with spread betting organisations that they have an interest in should first clear their writing with the editor. If the editor agrees that the reporter can write about the interest, it should be disclosed to readers at the end of the story. Holdings by third parties including families, trusts, self-select pension funds, self select ISAs and PEPs and nominee accounts are included in such interests.

**2.** Reporters will inform the editor on any occasion that they transact shares, derivatives or spread betting positions. This will overcome situations when the interests they are considering might conflict with reports by other writers in the magazine. This notification should be confirmed by e-mail.

**3.** Reporters are required to hold a full personal interest register. The whereabouts of this register should be revealed to the editor.

**4.** A reporter should not have made a transaction of shares, derivatives or spread betting positions for 30 days before the publication of an article that mentions such interest. Reporters who have an interest in a company they have written about should not transact the shares within 30 days after the on-sale date of the magazine.