STOCKS | FUNDS | INVESTMENT TRUSTS | PENSIONS AND SAVINGS

VOL 25 / ISSUE 48 / 07 DECEMBER 2023 / £4.49

SHARES

WE MAKE INVESTING EASIER

I'VE OPENED A SIPP

WHAT NEXT?

PLUS

Christmas retail winners and losers

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Three important things in this week's magazine

You've opened a SIPP – what next?

A step-by-step guide to planning and populating your personal pension with investments – with three different hypothetical scenarios.

Christmas retail winners and losers

Which brands and businesses will do well in the crucial festive trading period and which look in real trouble.

AI trackers under the microscope

ETFs focused on the artificial intelligence theme have struggled to keep pace with the trend's really hot stock Nvidia. Why?

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 Alphabet stock weakness may not be over yet

Strong pre-Christmas trading and bookings at pubs group Marston's

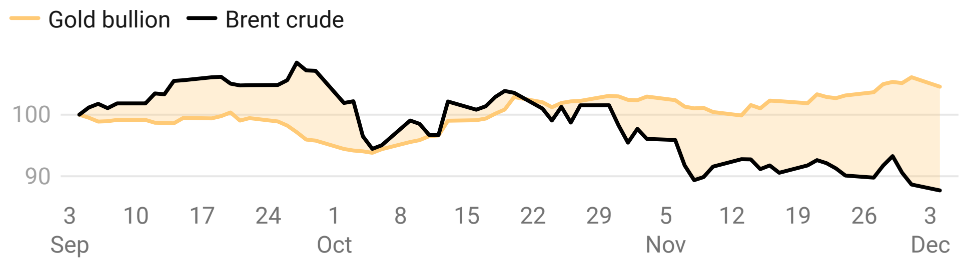
Mike Ashley's Frasers raises Boohoo stake above 17%

Are the supermarkets past their sell-by date now inflation is falling?

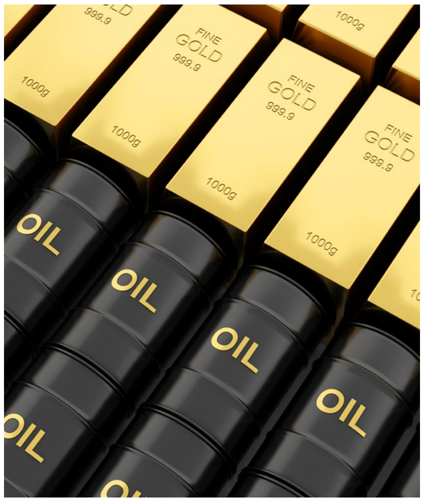
Find out why gold and oil prices are diverging

The Federal Reserve appears to have finished raising interest rates, at least for now

Gold and oil prices are heading in different directions



Rebased to 100
Chart: Shares magazine • Source: LSEG



Gold is back in vogue with the spot price making a new all-time high this week after touching $2,147 an ounce, surpassing the prior peak seen in May 2023.

Meanwhile, oil is close to entering a new bear market with Brent crude prices dropping nearly 20% in the last month despite war in the Middle East and efforts by OPEC+ to restrict production and prop up the market.

There are many reasons which could explain the diverging price trends, but the overriding factor is the change in investor sentiment seen over the last month.

There has been a growing realisation among investors that the major central banks have finished raising interest rates due to signs inflation is now heading back towards target.

Since the softer-than-expected US inflation print on 14 November, stock and bond markets have turned in their biggest price gains of the year.

Over the same period the US dollar has dropped around 4% against sterling and the euro as markets begin to price in earlier interest rate cuts than expected just a few weeks ago.

Historically, gold tends to get a boost from a weaker dollar, which is playing a role in positive recent momentum, but there is another factor to consider.

If the US Federal Reserve decides to allow more time for inflation to come back to its 2% target it implies inflation could remain elevated for longer. This might be useful for another reason.

Given the high level of government debt built up during the pandemic, cynics might argue it is more palatable to pay off that debt with deflated dollars.

The Fed is trying to walk a tightrope to weaken the economy enough to bring down inflation without causing a recession – a ‘Goldilocks’ scenario – and markets now seem convinced the central bank is on track to achieve that goal.

However, that scenario may yet prove illusory as the impact from tighter monetary policy has arguably only just begun.

That’s because excess consumer savings from the pandemic and fixed-rate mortgages have so far shielded many consumers from high interest rates.

By some estimates, only a third to a half of the effects from high interest rates have fed through to the economy so far which means times could get tougher over coming months.

This could also explain the weakness in the oil price, as investors start factoring in a fall in energy demand as the world economy slows down.

Data coming out of China has been weaker than expected in recent weeks, while the Eurozone remains close to recession after contracting 0.1% in the third quarter. [MG]

Fund manager hails Cybertruck solution to Tesla's soggy share run

Gary Black believes market is underestimating scope to grab a large piece of untapped market

The first handful of Cybertrucks are being delivered to customers this month reigniting optimism that **Tesla's (TSLA:NASDAQ)** long-awaited flatbed electric vehicle can spark the shares beyond $280 2023 highs.

Tesla investor and managing partner of the US-based Future Fund, Gary Black, remains optimistic about demand for the Cybertruck, countering the scepticism from some market analysts. Black expressed his confidence through a post on X, the former Twitter, stating 'consumer interest in Cybertruck is insane'.

He downplayed concerns about some customers cancelling their reservation deposits, emphasising that a substantial number are still eager to expedite their deliveries. According to Black, the Cybertruck is poised to have a positive 'halo' effect on Tesla's entire line-up, similar to the impact of the Model Y launch in 2020.

The fund manager highlighted that the Model Y launch led to a substantial increase in volume growth from 36% in 2020 to 87% in 2021, resulting in a seven-fold surge in Tesla's stock.

Unveiled in 2019, the Cybertruck took its time getting here, slogging its way through a global pandemic, a presidential election, two ongoing wars, and many other challenges over four years. But there are sceptics that believe Tesla is facing a vastly different world than it did in 2019, dominated by higher interest rates, pressure on consumer budgets and plummeting profit margins, factors that have eaten away at investor confidence.

Since peaking at $293.34 in July this year, Tesla shares have lost around 20%, wiping around $250 billion off the market cap and falling out of the exclusive trillion-dollar club.

Black is hopeful that Cybertruck can ignite a reversal of fortune through 2024, estimating Tesla delivering 100,000 vehicles and 250,000 in 2025,

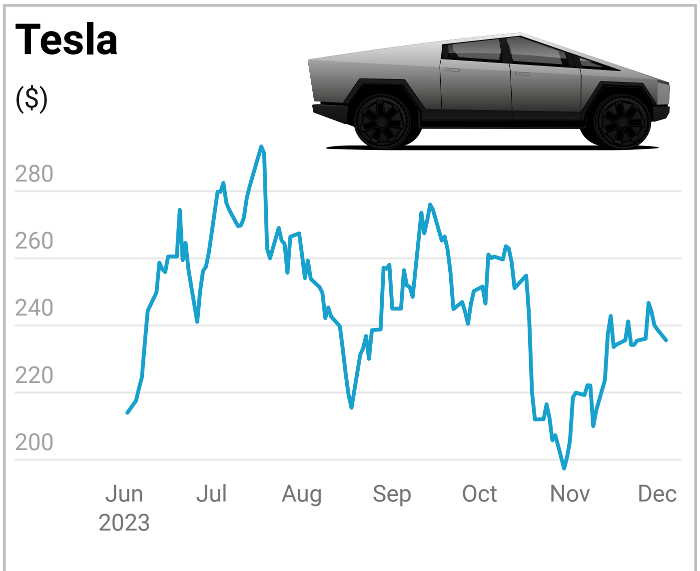


Chart: Sares magazine • Source: LSEG

as predicted by Tesla CEO Elon Musk himself. By 2027, Tesla will deliver 600,000 Cybertrucks, Black believes.

Assuming an average selling price of $60,000 among other factors, Black estimates 2017 sales will add $1 per share to earnings and up to $40 a share in future stock price value. The Wall Street estimates, however, are less optimistic. They imply Cybertruck deliveries of around 270,000, or less than half of Black's estimates, in 2027.

Despite initial concerns on Wall Street regarding the Cybertruck's high pricing and fears of it becoming a niche product rather than a mass-market success, Black contends that a volume ramp-up and subsequent price cuts will prove these estimates wrong.

He believes that the Cybertruck's potential to expand Tesla's total addressable market to the pickup segment, a space so far untapped by Tesla and constituting approximately 20% of all US vehicles sold, is being underestimated. This, coupled with the forthcoming $25,000 Model 2, positions Tesla as the only investable pure-play electric vehicle company, in Black's view. [SF]

Disney CEO Bob Iger under increasing pressure from share activists

Peltz and ex-Marvel executive Perlmutter launch 'proxy fight' for board seats

It's action stations at entertainment giant **Walt Disney (DIS:NYSE)**, where despite fourth-quarter results beating analysts' expectations activist investors Nelson Peltz and ex-Marvel executive Ike Perlmutter are not happy bunnies.

In collaboration with Perlmutter, Peltz and his firm Trian Fund Management recently launched a 'proxy fight' for multiple seats on the House of Mouse's board piling on the pressure for chief executive Bob Iger.

Peltz's firm Trian Fund owns approximately $3 billion of Disney stock.

Another US activist firm, San Francisco-based ValueAct Capital, has also built a sizeable stake in Disney over the past few months although its precise value is unknown.

Minority investors might be forgiven for thinking Iger, whose contract runs to 2026, is already losing control of the company.

For his part, the chief executive has flatly rejected Trian's demand for board representation but the activists are unlikely to go quietly.

Peltz is unhappy with Iger's management of Disney, accusing him of devaluing the company: 'Disney's share price has underperformed proxy peers and the broader market over every relevant period during the last decade and over the tenure of each incumbent director.

Year-to-date Disney shares are up just 4% to $92.58, more than 15% behind the S&P 500 index.

'Investor confidence is low, key strategic questions loom, and even Disney's CEO is acknowledging that the company's challenges are greater than previously believed', adds Peltz.

The chief executive already has plenty on his plate as it is in terms of fixing the company without having to fend off unhappy shareholders.

Ben Barringer, technology analyst at Quilter Cheviot, said: 'The company has managed to keep a lid on costs and is reducing spend on content, but revenues are lighter than expected as Disney continues to suffer from being a legacy media giant.

'Traditional TV continues its decline, and while Disney+ subscriptions were better than expected it is now guiding for lower-than-expected subscriber growth as price increases bite. The parks and resorts side of the business continues to do well and is being helped by a strong American consumer – although how long this will last with interest rates much higher for longer remains to be seen.

'Ultimately Bob Iger is still trying to sort out the mess Disney has created for itself, and you are starting to see why this is becoming a longer-term project for him. With the price for the remaining Hulu stake likely to rise, the writer and actor strikes causing content issues, attempts to sell off the Indian business and worries around Disney+'s scalability and profitability, the task ahead of him is a big one.' [SG]

Chart: Shares magazine • Source: LSEG

Shift in interest rate expectations sends Barratt Developments to year-high

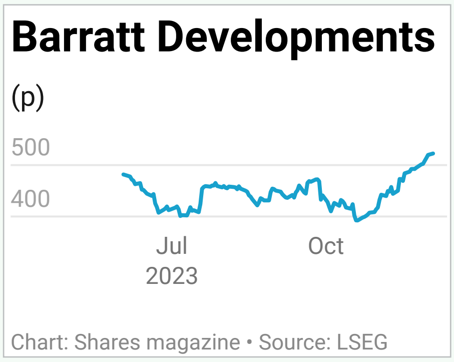
Housebuilder rallies on hopes of a revival in first-time buyer demand

Although its latest trading update in October did little to dispel the gloom surrounding the new housing sector, shares in the UK's leading developer **Barratt Developments (BDEV)** have rallied sharply in the last few weeks and are currently hitting new 12-month highs.

While private reservations have tumbled and the firm issued a much lower build target for the full year, Barratt shares have been boosted by the change in expectations for UK interest rates and all of a sudden are now up more than 30% for the year.

Whereas over the summer the consensus was for rates to top 6% and stay at that level for the whole of 2024, by the autumn the market began to bet instead on the Bank of England holding rates steady at the current rate of 5.25% for an indefinite period.

More recently, expectations have risen that the Bank may even *cut* interest rates in mid-2024, meaning mortgage rates will continue to come down, encouraging first-time buyers back into the market and reviving sales. [IC]



New energy firm Ceres Power has failed to live up to expectations

Delays in signing contracts and increased investment have mean twider losses

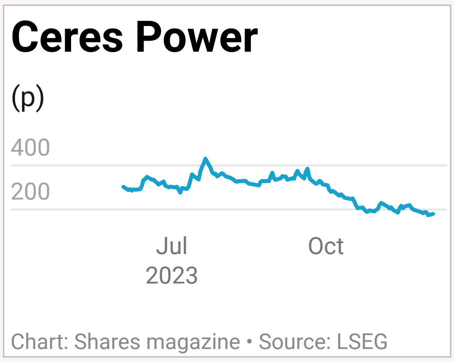
Horsham-based fuel cell and electrolysis firm **Ceres Power (CWR)** has had a torrid 2023, with its shares losing almost half their value after a series of disappointing trading updates.

The firm's fuel cells are used for power generation and storage, while its electrolysis technology is used to produce 'green' hydrogen as part of the global energy transition.

In July, the firm cut its full-year revenue forecast by almost a third from £49 million to around £34 million due to delays in recognising payment from its Chinese joint ventures which were still pending sign-off and regulatory clearance.

In September, the firm reported pre-tax losses had widened after it increased its capital spending to scale up manufacturing in its existing fuel-cell business and develop its 'game-changing' electrolyser technology.

On 30 November the firm lowered its revenue forecast again to £20 million to £21 million, or less than half its original target for this year, after it became apparent licenses with new potential partners also wouldn't be signed in time for the income to be registered by the year-end. [IC]



Unloved electricals giant Currys needs to deliver some earnings spark

Same-store sales, gross margins and costs will be in focus when the retailer reports

What the market expects of Currys

	EPS (p)	Revenue (£bn)
Year to April 2024	7.04	9.08
Year to April 2025	8.99	9.14

Table: Shares magazine • Source: Stockopedia

Shares in **Currys (CURY)** are down 20% year-to-date, so the technology products retailer needs to maintain its full-year guidance and deliver a solid trading update with its first-half results, due on 14 December, if the equity is to regain some spark.

Operating against a difficult consumer backdrop, the focus will be on like-for-like sales trends at the FTSE 250 TV, washing machine and laptop seller.

Investors will also be hoping for confirmation of continued gross margin improvements as well as delivery against cost savings targets.

On 7 September, Currys reported a solid start to the financial year to April 2024. Although UK & Ireland like-for-like sales were down 2% in the 17 weeks to 26 August, revenue trends improved in July and August while sales in the challenged Nordic region 'improved slightly' during the period.

Significantly, Currys is selling its Greece and Cyprus retail business which trades as Kotsovolos to Public Power Corporation for net proceeds of £156 million.

The disposal will enable Currys to laser in on the UK & Ireland and the Nordics, while simultaneously strengthening the balance sheet giving chief executive Alex Baldock more headroom to grow the business.

Liberum Capital points out that with the shares trading at a low valuation 'it cannot be ruled out that Currys could be subject to approaches from interested parties'.

Mike Ashley's **Frasers (FRAS)** has already built a 12.7% stake through shares and derivatives, which the broker argues is 'a potentially substantive, but not blocking, stake'. [JC]

Chart: Shares magazine • Source: LSEG

UK UPDATES OVER THE NEXT 7 DAYS

FULL YEAR RESULTS
December 11: Associated British Foods
December 12: RWS Holdings, Chemring

FIRST HALF RESULTS
December 8: Berkeley
December 11: Begbies Traynor
December 12: Vianet
December 13: Cohort
December 14: Currys

TRADING ANNOUNCEMENTS
December 14: Balfour Beatty

Can Oracle maintain its cloud growth mojo?

Enterprise software giant needs to show it can execute faster growth

What the market expects of Oracle

	EPS ($)	Revenue ($bn)
Q2 forecast	$1.32	13.05

Table: Shares magazine • Source: Yahoo Finance. Year-end 31 May

Oracle

($)

Chart: Shares magazine • Source: LSEG

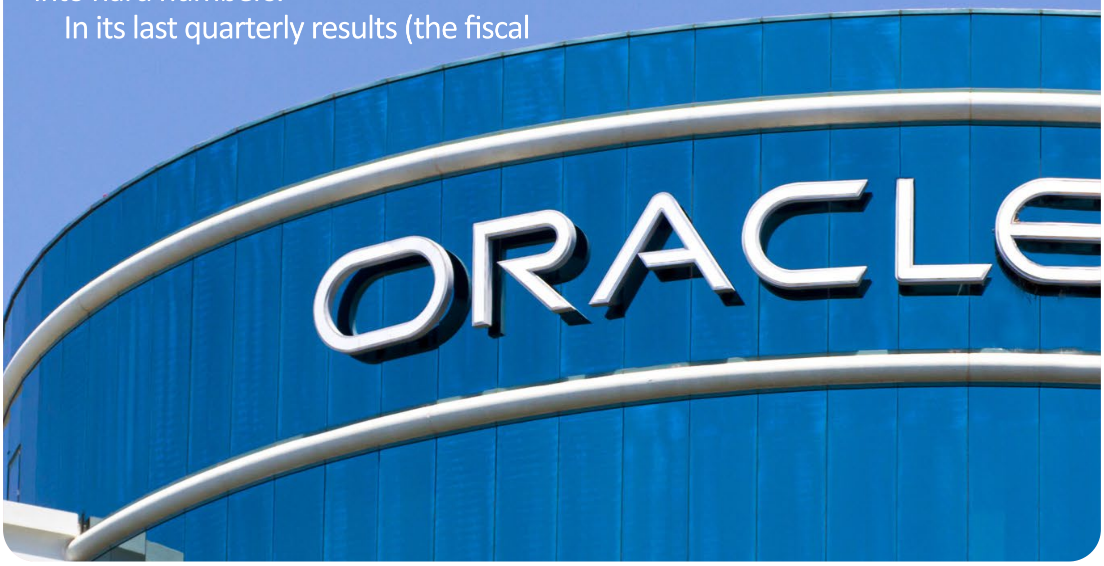
There has been a good deal of bullish commentary of around **Oracle (ORCL:NASDAQ)** this year as it finally starts delivering on its long-promised cloud growth.

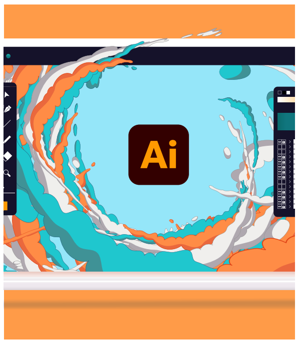
Year-to-date, the stock is up nearly 40%, and while most of that rally happened in the first half of the year, when investors began getting the growth bug again the shares put up double-digit gains in November.

The Austin, Texas-based company has been banging the cloud drum for more than a decade, but only recently has that optimism begun to translate into hard numbers.

In its last quarterly results (the fiscal first quarter to May 2024), published in September, Oracle reported $1.19 of earnings per share on $12.5 billion revenue, narrowly beating expectations in both cases.

Analysts are forecasting $1.32 of earnings on just over $13 billion of revenue for the second quarter to 30 November, which will come after-hours on 14 December, and current estimates point to accelerating growth rates for full year 2024 and 2025. Investors will want to see evidence of that if the stock is to maintain its recent momentum. [SF]





US UPDATES OVER THE NEXT 7 DAYS

QUARTERLY RESULTS

December 8: IES Holdings, Phreesia, Johnson Outdoors
December 11: Caseys
December 12: Uranium Energy
December 13: Adobe, Lennar, Nordson, Photronics
December 14: Oracle, Costco, Scholastic, Planet Labs,


BING!
BANG!
BONG!

This Fidelity fund looks a really smart way to play US stocks

A value focus could pay off given wider markets across the Atlantic are looking expensive

Fidelity American Special Situations

(B89ST70) £23.17

Fund size: £665 million

BUY

The US has been one of the most prosperous regions for investors over the past decade or so, with its stock market offering access to a range of exciting companies taking on the world. Investors are right to have large exposure to the US but they need to keep an eye on valuations.

Fidelity American Special Situations

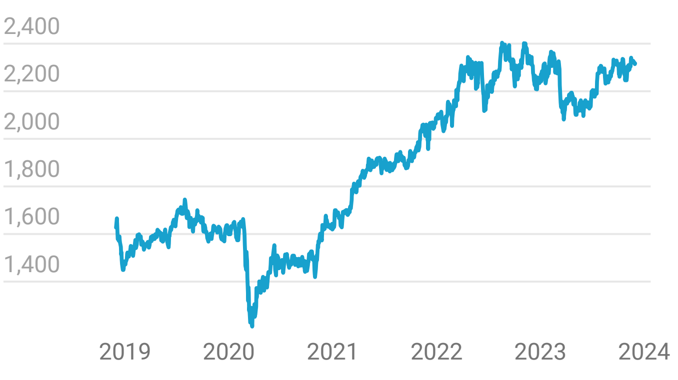


Chart: Shares magazine • Source: LSEG

The Nasdaq 100 trades on 28 times forward earnings and the S&P 500 trades on 20 times forward earnings, according to data from Birinyi Associates. While these figures are not out of the ordinary when looking back over the past 20 years, they are still high enough to make stocks vulnerable to big falls upon the first sign of

unwelcome news.

That is certainly a trend we have seen building over the past few months as multiple US-listed companies have experienced double-digit share price declines on negative news flow. With various companies talking about a slowdown in the pace of growth, investors might need to be on guard.

One solution is to tilt part of your US exposure in a portfolio towards a value-style fund. **Fidelity American Special Situations (B89ST70)** looks like an ideal candidate as it focuses on investing in companies with quality characteristics trading below what the fund managers believes to be their intrinsic value. Its portfolio traded on an average 14.1 times earnings as of 31 October 2023.

VALUE'S BIG COMEBACK

The value investing style was out of favour between 2009 and 2020 because of low economic growth, falling inflation expectations and low interest rates which meant investors were happy to pay a premium to buy shares in companies capable of delivering strong earnings growth in that environment.

The tables have turned in recent years thanks to inflation and interest rates going up. The MSCI World IMI Growth index has returned 14.9% since the start of 2021 whereas the MSCI World Value index has achieved 26.4%. Fidelity American Special Situations has done even better over the same period, returning 42.8%. The fund has a 0.86% ongoing charge.

LOOKING THROUGH NEAR-TERM ISSUES

US pharmaceuticals distributor **McKesson (MCK:NYSE)** is one of the fund's biggest holdings. Despite facing significant headwinds centred around its alleged role in fuelling the US opioid epidemic, the shares have performed strongly over the past five years.

'When we invested in McKesson it was under scrutiny because of the opioid crisis and perceived competitive threats from Amazon,' explains portfolio manager Rosanna Burcheri. '(On the former) there were a huge number of lawsuits and the possibility of unlimited liability according to certain analysts.

'The reality we've seen in the past, when you have these big legal cases, is that the company reaches a settlement. Yes, it's a lot of money but the fact that you can put a number on that and run your valuation is what gave us the confidence to go ahead and invest.'

Burcheri says almost 90% of US prescription drugs flow through the distributor. Three companies dominate this industry and they have 95% market share combined. 'I like this situation as it gives them high pricing power.'

SEEING VALUE WHERE OTHERS DON'T

FedEx (FDX:NYSE) also sits in the fund's top five holdings and is another situation where the shares have faced a barrage of unwelcome news, yet the stock has eventually pushed higher.

September 2022 saw the package delivery giant issue a profit warning linked to a gloomy economic outlook, causing the share price to fall by 21%, the biggest one-day drop since it joined the stock market in 1978. By April 2023 it had made up the lost ground and the stock has risen further despite margins coming under pressure.

'There is still a huge amount of value in the business. We have a new management team and the plan put in place makes sense. The company is going through a huge refresh of the aircraft fleet compared to competitors like UPS – it has the youngest fleet and is more efficient. There is a need to cut costs as the organisation had ballooned during the pandemic. Everyone was ordering goods so costs built up, which it is now trying to reset.'

Burcheri says there is an opportunity to combine the express and ground business, saying FedEx does not need two different trucks running around the same neighbourhood.

'The market is underestimating the cash earnings power of FedEx,' she adds. 'The profitability and return on investment are still much below UPS which was always considered the gold standard in the industry and there is the potential of catching up.'

Elsewhere, Fidelity American Special Situations holds a stake in Google's parent company **Alphabet (GOOGL:NASDAQ)**. Burcheri believes the market is underestimating the franchise value of Google and that Alphabet has significant opportunities with cloud computing and its YouTube video platform.

PORTFOLIO CONTENDERS

Next up for the fund could be one or more investments in stocks caught up in the drama around weight-loss drugs.

The hype around companies selling these treatments has led investors to sell down positions in businesses they perceive to be losers from a weight-loss boom. Think snack companies, fizzy drink manufacturers and pharmaceutical groups providing treatments to illnesses caused by obesity such as heart disease and diabetes. Burcheri says she has spotted names now trading at levels rarely seen in her career.

The market has a habit of overreacting to perceived threats and there is no guarantee that weight-loss drug sales will match lofty expectations. Reports of unpleasant side-effects from these treatments could even make people hesitant about taking them. [DC]

SharkNinja is stealthily attacking a global market

The growth story has just begun at the innovative household appliances play

SharkNinja

(SN:NYSE) $49

Market cap: $6.81 billion

Add a fast-growing company with a massive international market share opportunity to portfolios by buying **SharkNinja (SN:NYSE)**. This household appliance innovator is the group behind two exciting global brands, Shark and Ninja. The clue is in the name.

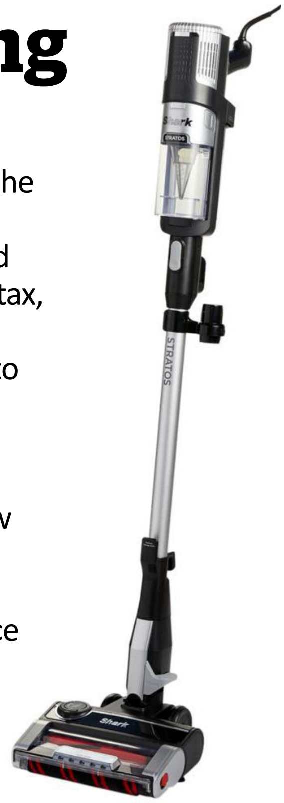
Shares in the Massachusetts-headquartered company have had a strong run since their New York Stock Exchange debut (31 July), yet they remain modestly valued relative to the firm's growth potential and have scope to swim higher as well-received new product launches driving an improved market position and earnings upgrades.

Spun-out from Hong Kong's **JS Global Lifestyle (1691:HKG)**, the $6.8 billion cap designs household appliances ranging from smart vacuum cleaners and air fryers to electric grills, blenders and hairdryers.

CEO Mark Barrocas has described SharkNinja as a 'consumer-solving engine'; by bringing disruptive consumer products one after another to a massive, fragmented market and entering new product categories, SharkNinja has successfully driven significant growth and market share gains.

Shares believes the stock market newcomer's products, which are sold through key retailers including **Amazon (AMZN:NASDAQ)**, **Walmart (WMT:NYSE)**, **Currys (CURY)**, Argos and distributors around the world, will be a big hit with consumers this Christmas. Its portfolio of cooking and beverage appliances and food preparation appliances looks particularly well placed and strong sell-through and re-stocking from customers could prove the catalyst for further upgrades from the company.

SharkNinja raised its full year 2023 sales and profit outlook following forecast-beating results (9 November) for the third quarter to September. These revealed a 38.4% surge in adjusted EBITDA (earnings before interest, tax, depreciation and amortisation) to $208.7 million on sales up 13.1% to nearly $1.1 billion. Encouragingly, Barrocas highlighted 'good momentum as we head into the holiday season'. Management now expects full year 2023 sales to increase by 11.5% to 12.5% year-on-year, up from previous guidance of growth in the 9% to 11% range.



The company also reported a significant uptick in quarterly gross margin to 45.5% thanks to supply chain tailwinds, cost efficiencies and price increases, not to mention strong, higher margin direct-to-consumer sales, notably in the beauty category. Flush with $170.4 million cash, SharkNinja also treated shareholders to a $1.08 per share special dividend.

Based on Stockopedia data, SharkNinja trades on a prospective price to earnings ratio of 15.6 for the year to December 2023, falling to 14.8 times for 2024. There are risks to weigh as the bulk of sales are derived from North America, where consumers are feeling the pinch, and SharkNinja has significant exposure to China, where geopolitical tensions with the US could create future problems. [JC]

Infrastructure play Costain continues its long overdue rerating

Shares are trading at a new 52 week-high

Costain
(COST) 64.8p

Gain to date: 18.7%

Original BUY @ 54.58p on 31 August 2023

When we recommended buying shares in infrastructure and engineering group **Costain (COST)** we flagged its superior revenue and earnings visibility, thanks to the size of its order book and the security of its customers, which tend to be county councils and major utilities.

We also suggested the firm's lowly valuation, its large cash pile, and the fact free cash flow had improved to the point where the board might contemplate restarting dividends meant the shares wouldn't stay cheap for long.

WHAT HAS HAPPENED SINCE WE SAID TO BUY

Sure enough, within a week the firm declared a 0.4p per share interim dividend, its first payout to shareholders since before the pandemic.

Also in September, the firm was appointed by water company **Severn Trent (SVT)** as part of its Capital Delivery Framework, just a couple of months after it was appointed as a Managed Service Provider for a further two years by **United Utilities [UU.)**.

The United Utilities work is its first under AMP8, the latest five-year asset management period for the water industry, and Costain expects to see considerable growth in this area going forward.

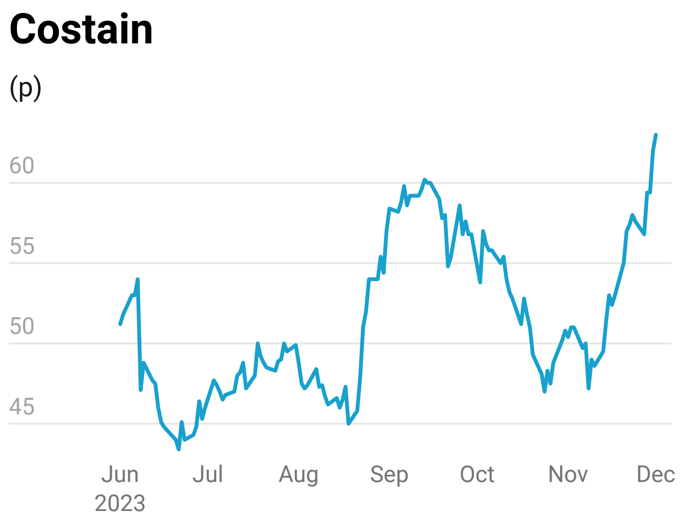


Chart: Shares magazine • Source: LSEG

WHAT SHOULD INVESTORS DO NOW?

The firm's full-year results won't be released until next March, but the current consensus is for sales of £1.37 billion and EPS (earnings per share) of 10.8p, which puts the shares on a current PE of six times.

Meanwhile, analysts are forecasting the group will have a net cash pile of £128 million at the end of 2023, rising to £150 million in 2024, which given its market cap is just £180 million means the operating business is currently valued at £52 million or less than two times earnings.

We are confident this undervaluation won't last long – either the market will see to it, or private equity buyers will swoop in and take advantage of the prodigious cash flow the firm generates, so we remain bullish. [IC]

I've opened a SIPP
WHAT NEXT?

Your step-by-step guide to investing through a SIPP

Making a start to any enterprise is often the hardest part – so if you have opened a SIPP (self-invested personal pension) you have already taken one of the most important first steps towards a more comfortable retirement.

This article will talk you through the next steps so you can start putting your money to work in the global stock markets and grow your wealth.

By **Sabuhi Gard** Investment Writer

What to do once you've opened a SIPP

Step 1	Assess your current retirement plan
Step 2	Determine the income you will need in retirement
Step 3	Decide how much you can invest
Step 4	Consider all the charges
Step 5	Decide what to invest in
Step 6	Make the transaction

STEP ONE: ASSESS YOUR CURRENT RETIREMENT PLAN

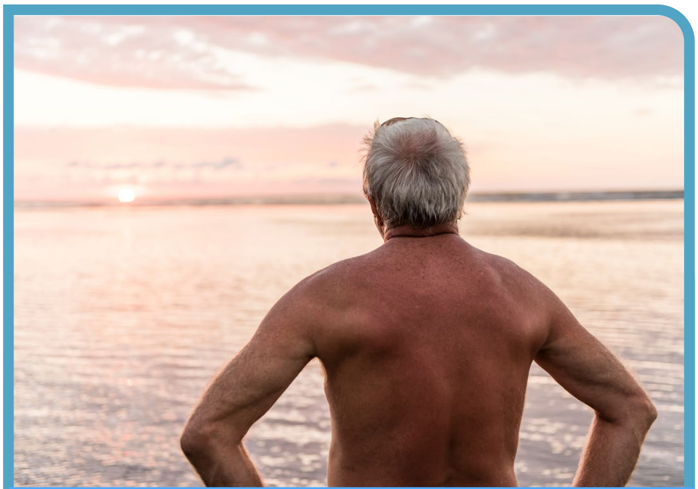
Retiring for some people might be a long way off but there are real benefits to starting investing and saving for it early. Whatever the time horizon, the most important thing to do first is to assess your current retirement plan.

If you are employed rather than self-employed you will be automatically enrolled in the company's workplace pension scheme (unless you opt out). This is valuable because for every 5% of your earnings per month paid into your workplace pension, your employer must pay 3%.

There is also another type of workplace pension called a defined benefit (DB) or final salary pension scheme. This provides an income for life and is usually based on your salary and the number of years you have been a member of the scheme.

A SIPP can be a useful way of supplementing an existing workplace pension and some employers may even pay pension contributions directly into a SIPP. If you have accumulated several pensions through the course of your career these can be consolidated within a SIPP, with plans for a pension 'pot for life' announced in the Autumn Statement still very much an aspiration rather than anything which is close to fruition in the near term.

The Pension Tracing Service is a useful tool to locate missing pensions, and some providers also



SIPPS AND PENSIONS THE BASICS

A SIPP is the most flexible type of personal pension. It allows you access to a wide range of different investment choices and gives you a number of options on how you draw your cash when you reach 55 (or 57 from 2028).

Pensions benefit from tax relief. Therefore contributing to one can be a good use of cash that isn't needed to repay expensive debts or pay bills. Thanks to the generous tax relief on offer, £1,000 paid into a pension will automatically be topped up to £1,250 via 20% basic rate tax relief based on the total contribution.

Those who pay a higher rate of tax can claim an additional 20% through their self-assessment tax return or by contacting HMRC.

If your taxable income is over £150,000, you'll pay a tax rate of 45% on everything over this threshold. You can claim additional tax relief on that amount – an extra 5%, to give you 45% tax relief in total on all pension contributions from your income over this threshold. In Scotland slightly different tax rates apply.

While SIPPs benefit from up-front tax relief any income drawn from them is subject to taxation (unlike ISAs).

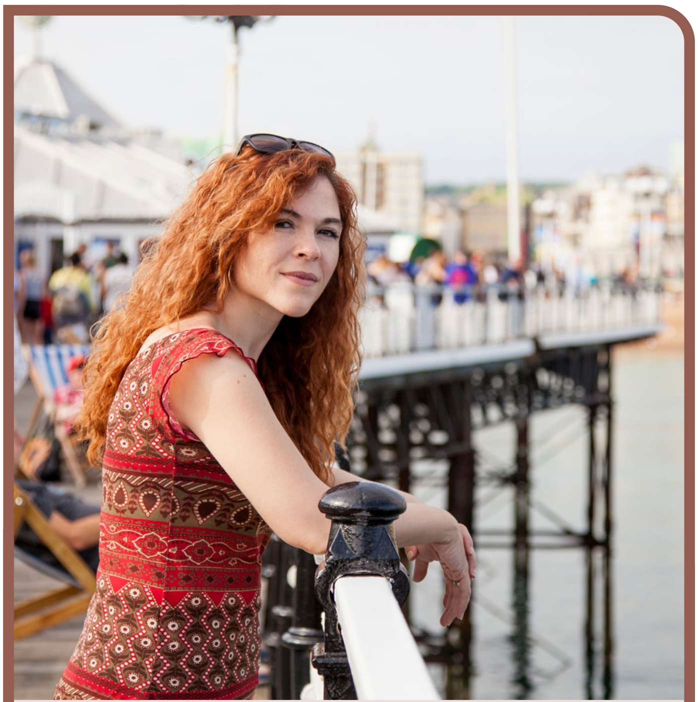
You have three main alternatives at retirement: buy an annuity (an insurance-like product providing an income for life); drawdown regular chunks or income from your pension pot as and when you wish; or take the lot in one go. Up to 25% of your pension can be taken tax-free with the rest taxed as normal income.

may be able help.

There is also the state pension. The full 'new' state pension is worth £203.85 per week in 2023/24 but you may get more or less, depending on your national insurance record.

You'll qualify for payments when you reach 66, but this is scheduled to rise to 67 between 2026 and 2028.

In the future, however state pension provision might not be as generous, this simply adds to the case for supplementing your retirement income with the SIPP you have just opened.



CASE STUDY: PHOEBE IS GETTING STARTED EARLY

Brighton-based Phoebe is an 18-year-old student who has just started college. She has always been fascinated by investing and is keen to plan for retirement even though it is a long way off. Phoebe has a very long-time horizon so she can afford to be 'adventurous' in her investment selection gaining exposure to emerging markets and more moderate assets like corporate bonds and commercial property. Among Phoebe's investments is **JP Morgan Emerging Markets Income Fund (B5M5KY18)** which invests in a mix of Chinese, Taiwanese, South Korean, Mexican, Hong Kong, Indian, Indonesian, and Brazilian equites. It has a dividend yield of 3.86% and over 10 years it has delivered an annualised return of 5.39%. The ongoing charge is 0.88%.

STEP TWO: DETERMINE THE INCOME YOU WILL NEED IN RETIREMENT

Ideally, a SIPP will be able to provide you with enough cash for a retirement suitable for your needs. It is important to remember that these needs vary from person to person.

You may want to travel the world in retirement, buy a holiday home, need to factor in care costs (if you or your partner have a terminal illness), you may want to downsize from the family home or pay for the grandkids' university education.

In March 2023 consumer watchdog Which? surveyed 5,000 retirees about their spending habits.

For a single person to fund a 'basic' retirement lifestyle where essentials are covered (food, transport, utility bills) an income of £13,000 per year is needed, for couples £19,000.

Spending rises to £20,000 (£28,000 for couples) when you include some leisure spending, and £32,000 (£44,000 for couples) to include luxuries such as extended long-haul holidays.

The Which? survey has concluded that people living alone will need a total pot of around £173,000 alongside their state pension to achieve the 'comfortable' target of £20,000 a year, assuming they access their savings via pension drawdown (drawdown figures are based on a saver withdrawing all their money over 20 years from age 65, and assume investment growth at 3%, inflation at 1% and charges of 0.75%).

If you opt to buy an annuity, which gives you a guaranteed income for life, that figure rises to £182,000.

Meanwhile, couples would need to aim for a combined pot £115,000 if opting for drawdown, or £131,000 if buying a joint-life annuity.

If aiming for luxury retirement target of £32,000 a year (£44,000 for couples) as specified by the Which? survey, you'd need a total pot worth at least £400,000 – or £420,000 for couples. All of these pot sizes reflect how much you would need in private pensions to achieve this level of income.

CASE STUDY: JAMES AND CHARLOTTE ARE TAKING A CAUTIOUS APPROACH

James is a 32-year-old estate agent from London, and his wife Charlotte is a 28-year-old teacher. James has a workplace pension with his employer, but he is keen on supplementing his retirement income by opening a SIPP. His wife Charlotte is happy with her pension for now – she has a defined benefit pension scheme from the Teachers' Pension Scheme (TPS). He has decided to adopt a more cautious approach to his portfolio and grow his money over time.
One of James's investments is **Artemis Strategic Bond Fund (B2PLJR10)**. The fund aims to provide a combination of income and capital growth over a five-year period. The fund invests 80% to 100% in debt and debt-related securities.
It has a dividend yield of 4.58% and an ongoing charge of 0.59%.

STEP THREE: DECIDE HOW MUCH YOU CAN INVEST

It is worth setting aside some time to go through regular outgoings and work out how much you could find for pension contributions. Even if you start small to begin with you can always build your contributions as you are able to.

You need to be aware of the annual limits on what you can contribute to a pension – which is for all pensions you have, rather than per pension. For most people that annual allowance will be £60,000, but you also can't put more into your pension than you earned in any year – so if your earnings are lower, your annual limit will be too. The lifetime allowance is set to be abolished from 6 April 2024 so you can accumulate pension pots of any size without penalty.

STEP FOUR: CONSIDER ALL THE CHARGES

Setting up a SIPP is completely free with most platform providers. For example, with AJ Bell, setting up your account is free, paying money into your account is free, it is free to access your SIPP and there is no inactivity fee.

However, there are funds custody charge on the AJ Bell platform, for example, (including unit trusts, OEICs and structured products) – 0.25% on the first £250,000 of funds, 0.10% for funds between £250,00 and £500,000 and no charge on the value of funds over £500,000.

There is a shares custody charge (including investment trusts, ETFs, gilts, and bonds), of 0.25% (maximum £10 per month).

For buying and selling investments per deal. It is £1.50 for funds (including unit trusts and OEICs) online, £9.95 for shares (including investment trusts, ETFs, gilts, and bonds online) and £4.95 for shares where there are 10 or more share deals in the previous month.

STEP FIVE: DECIDE WHAT TO INVEST IN

Using a SIPP to save for your retirement offers many benefits, for one you can manage your pension yourself and have financial control.

When selecting what to put in your SIPP you can choose from investment trusts, funds, shares, bonds and exchange-traded funds (ETFs).

However, make sure you do your research before putting money into any investment. A good starting point is *Shares* – as a digital magazine we cover a range of investments as well as educational material to aid your understanding of the markets and investing.

Other useful sources of information include the personal finance and business sections of newspapers and your investment platforms, or you could look at financial data platforms including SharePad and Stockopedia which offer useful screening tools. Though these come with a subscription charge.

Whatever you choose to do it is best to have a diversified portfolio – to spread the investment risk. Diversification means not just different products but various regions, asset classes and sectors.

If you have several more decades of working life before you retire then you can take on a reasonable amount of risk as you have time to see out any ups and downs in the market. This might mean investing in areas which potentially offer higher growth like emerging markets and technology.

One approach could be to invest in a product like **Fidelity Index World (BJS8SJ3)** which offers exposure to a broad basket of developed market stocks for an ongoing charge of 0.12%. From this core building block, you could then create a more diversified portfolio with exposure to different sectors and

BUYING AN ANNUITY

An annuity can give you a guaranteed income in return for some or all of your pension pot. These annuities can provide an income for life or for a fixed period of time. The amount of money you receive in retirement depends on how much you put it in your lifetime and your annuity rates at the time of retirement – these have improved thanks to higher interest rates.

For example, Tariq has £300,000 in his pension. He chooses to take £100,000 out of his pension, leaving him with £200,000. He takes the first 25% as tax free lump sum of £25,000. He then uses the remaining amount of £75,000 to buy an annuity which pays him an income (which is taxed).

The rest of his pension stays invested until a later date when he can buy another annuity or choose another option, for example drawdown. Buying an annuity means crystallising the value of a least a portion of your pension so you would need to bear this in mind when the purchase point approached so you weren't caught out by short-term market volatility.

CASE STUDY: SALLY USING A SIPP TO CONSOLIDATE PENSIONS

Sally is single in her late 40s with no partner or children. She has been working for 30 years in public relations. In that period, she has worked for several employers and accrued five small pension pots from each workplace.

Sally is looking to combine her small pensions in one pension pot through a SIPP which will give her more financial control of her investments in the run up to retirement.

With another 15 to 20 years until retirement, Sally has decided to take a 'balanced' approach to invest in her recently opened SIPP. She has decided to invest part of her SIPP in **Jupiter UK Special Situations (B4KL9F89)**. The fund aims to provide a return higher than that provided by the FTSE All Share over the long term (at least over five years). At least 70% of the fund is in shares of companies based in the UK. The ongoing charges are 0.76% and the 10-year annualised return is a smidge over 6%

themes depending on your appetite for risk.

The nearer you get to retirement, the less risk you might want to take on particularly if you plan to buy an annuity.

STEP SIX: MAKE THE TRANSACTION

For a one-off investment in your SIPP, you will start by clicking on the deal or trade button. Remember to check you have enough cash on your account to fund any charges. Your account can be funded through a lump sum or regular payments through a direct debit.

Before you invest in a fund, you will need to confirm you have read the necessary information about a fund including the Key Information Document or KIID.

It often takes a day for the order to buy a fund to be processed and completed. For a transaction in shares, investment trusts and ETFs you will be provided with a time-limited quote to buy (or sell) at a certain price. In an equivalent way to funds you can either select how much money or how many shares you want to trade. You will then be shown the total cost of the transaction.

Once you have made your first investment then, congratulations you are a fully-fledged SIPP investor.

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

Cash burners can fire **outstanding returns**

While balance sheet discipline is often a welcome feature of a potential investment, occasionally it pays to consider businesses that are spending cash on themselves, as we have done for Lowland Investment Company.

Listen to any fund manager presentation and the core script will almost invariably include lines like this: "We buy strong, growing companies that are generating lots of cash and have strong balance sheets and barriers to competition… Blah, blah…"

Well, perhaps not "Blah, blah…" – but you get the gist. It would be nice to hear a manager say that sometimes they include in their portfolio companies burning cash so fast that without an urgent injection of capital they face ruin.

You might ask why on earth anyone would want such a company, but many of the best investments I have ever made have fallen into this category. One of our best performers this year has been Rolls-Royce, which is up 140% so far.

This is a company that in January was described by its new boss as a "burning platform". Tufan Erginbilgic pointed to the disappointing returns made on invested capital and set about changing things.

He has sold off non-core businesses – one of the largest being the €1.8bn disposal of Spanish joint venture ITP Aero. He has focused spending on priority areas and renegotiated maintenance contracts.

Post-Covid recovery in air transport has helped. The combination means that in just the first six months of the year operating margins soared from 3.4% to 12.4% and the company generated twice as much profit as analysts were expecting – £673m.

Those earlier analyst forecasts have shown how a gloomy mindset can set in around a company. Rolls-Royce was certainly not one for investors who only like companies with attractive cash flows. They have missed out.

Unearthing these opportunities takes research. Often you are looking for yesterday's leaders in recovery, like Rolls-Royce. But more usually you find them in smaller companies. When investing in these businesses you must always be aware that at some point you may be touched for more cash – or see your shares diluted. It is called a "rights issue".

It is easy to forget that the purpose of the

stock exchange is to help companies raise capital. In return they offer a stake in the business and a share of all future profits for as long as the company operates and those shares are in operation.

Companies can seek to raise cash for all sorts of reasons. In the AIM market it would usually be to build new plant, expand production or take a new product from prototype to production. Examples in our portfolio include alternative energy companies such as AFC, ITM and Ceres. These are still fairly early-stage businesses but could have enormous potential as we move to a low-carbon world.

Sometimes companies can experience a cash squeeze because of events, like Covid. For investors who support any fund-raising endeavours the hope may be that if the business can get through to the other side of the crisis it will find competition weakened and gain significant market share.

One of the most memorable examples of a company raising capital because of a crisis was in 2001. Following the terrorist attack on the Twin Towers in New York, insurer Hiscox came to the market twice – in 2001 and 2002 – seeking around £164m. We backed it. With that money it was able to write new business at an attractive rates, because many of its competitors were out of the market in light of their own cash struggles. It helped enable Hiscox, then a relatively small business, to step into the big leagues. The rights issue shares were £1.20 and £1.65. Today Hiscox shares trade at more than £10.

There is heightened risk in cash burning investments, but risks can be mitigated. We want to understand clearly what is behind the cash burn and how quickly investment might be expected to pay off. Is it a Covid-style crisis and a story of the fittest survivor thriving when normal service resumes?

A crucial question we ask ourselves is how much we trust management. Often new management will launch a rights issue as part of a big reorganisation plan. Does that plan excite us? Can we see the potential or is it pouring good money after bad?

It might be that the plan is not articulated well and is not convincing. It might be that we do not have confidence in management's ability to execute it. In such cases we may not just decline to pay up – we may sell our shares altogether. Sometimes it is better to take your losses and move on, putting your money to work in more promising areas.

Of course, we have had failures, but when you get the decision right the rewards from a cash burner can far outpace those offered by the majority of healthy cash generators that can form the core of portfolios.

GLOSSARY

Balance sheet
A financial statement that summarises a company's assets, liabilities and shareholders' equity at a particular point in time. Each segment gives investors an idea as to what the company owns and owes, as well as the amount invested by shareholders. It is called a balance sheet because of the accounting equation: assets = liabilities + shareholders' equity.

Free cash flow (FCF)
Cash that a company generates after allowing for day-to-day running expenses and capital expenditure. It can then use the cash to make purchases, pay dividends or reduce debt.

DISCOVER the Christmas retail WINNERS AND LOSERS

The stocks to watch as we enter the annual festive spending frenzy

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

We are now a little more than a fortnight away from Christmas Day with TV adverts pushing festive products, high streets adorned with Christmas decorations and shops flush with discount offers.

The so-called 'Golden Quarter' including Black Friday is the most hotly contested period of the year amongst retailers and those that suffer disappointing sales or resort to overly-promotional strategies typically disappoint with profit warnings when the festive updates are posted in January. Conversely, shopkeepers with winning customer propositions will trade profitably, grow like-for-like sales and potentially deliver earnings upgrades in the new year.

Christmas alone won't make or break a retailer. But strong sales over 'peak' provide an opportunity to win over customers and secure market share which can be consolidated over ensuing periods, whereas market share losses can tip struggling retailers with weak balance sheets into trouble if they are left with obsolete stock and their cash flows come under strain.

Investors can position themselves ahead of January's retail reporting frenzy, traditionally kickstarted by sector star turn **Next (NXT),** by bagging shares in the likely winners ahead of time.

BLACK FRIDAY BONANZA

Consumers grappling with cost-of-living pressures were predicted to buy fewer goods this Black Friday given signs that people are buying less stuff and being more wary when parting with their cash.

On 27 November **Barclays (BARC)** said the volume of UK Black Friday transactions was 0.63% lower compared with 2022 due to the impact of cost-of-living pressures and the trend towards launching discounts earlier in November. A significant risk for retailers is that Black Friday has pulled forward spending which could fall away in the run-up to Christmas and they suffer a bleak start to 2024 as consumers focus on paying credit card bills.

However, the latest consumer confidence survey from GfK suggested that Christmas could still be a winner for shopkeepers, showing a sharp rise in

GfK index score November 2022 – November 2023

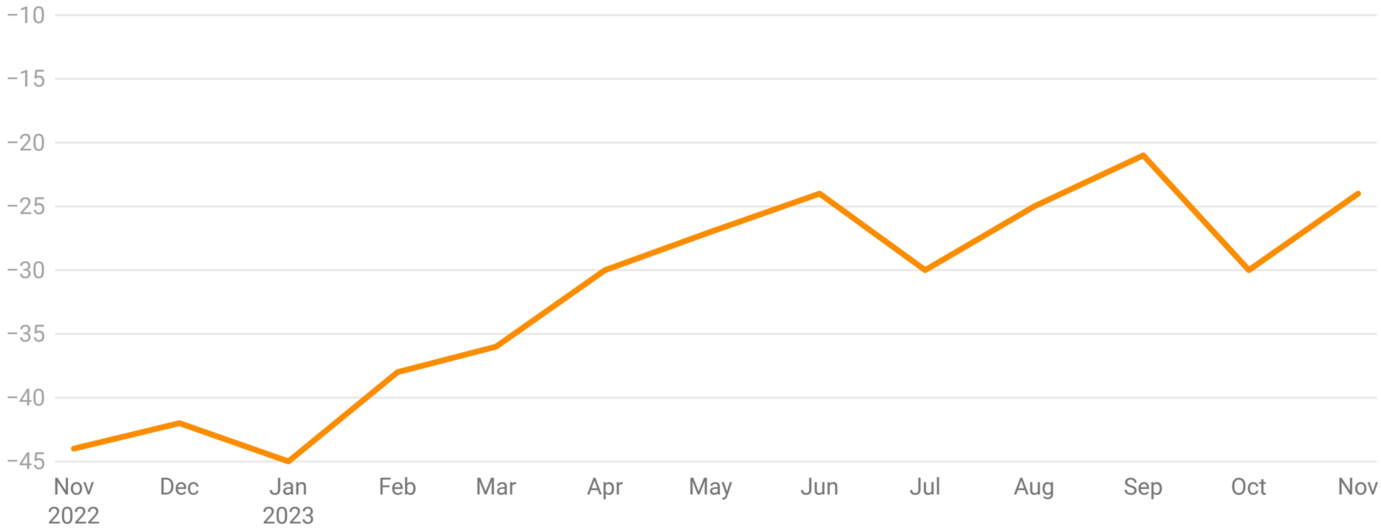


Chart: Shares magazine • Source: GfK Consumer Confidence Barometer powered by NIM (November 2023)

sentiment including a greater willingness to commit to major purchases. GfK's long-running consumer confidence index rose by six points in November despite ongoing cost-of-living concerns, although it still languishes firmly at minus 24.

In addition, retail analyst MRI Software, previously known as Springboard, said the Black Friday week offered optimism for UK retail destinations with footfall jumping by 7.9% versus the previous week. Meanwhile, German discounter Lidl is expecting a 'record-breaking Christmas' trading period, footfall to its stores having surged in the past six weeks as cash-conscious shoppers stocked up on Christmas gifts, decorations and mince pies earlier this year.

WINNERS & LOSERS

For investors, the best strategy is to focus on retailers that are best placed to bag market share, not only during Christmas but into 2024 and beyond. Christmas is a crucial time for supermarkets including **Tesco (TSCO)** and **Sainsbury's (SBRY),** although the grocers won't feel the benefit of food price inflation this year. It's also a particularly important period for seasonal specialists with a value focus such as **Card Factory (CARD)** and **The Works (WRKS)**, while online cards-to-gifts platform **Moonpig (MOON)** also has a lot riding on the next few weeks.

Our winter retail winners

Company	Market cap	Forward price to earnings ratio	Dividend yield	Share price YTD
Marks & Spencer	£4.99bn	12.2	1.4%	99.8%
JD Sports Fashion	£8.2bn	11.8	0.6%	22.0%
B&M	£5.79bn	15.4	4.0%	36.2%
Dunelm	£2.1bn	14.0	6.3%	5.5%
Currys	£497.4m	6.2	4.9%	−22.8%
Walmart	$419bn	24.1	1.5%	8.4%

Table: Shares magazine • Source: Stockopedia, Google Finance, 1 December 2023

One large cap retailer with clear momentum and scope for further upgrades is high-flying **Marks & Spencer (MKS)**, whose millions of Sparks customers are able to access festive treats on the app, with food sales remaining strong and the retailer's more appealing clothing designs are resonating with the public.

At the time of Marks & Spencer's forecast-smashing first half results on 8 November, CEO Stuart Machin insisted 'trading momentum has been maintained through October, with customers responding positively to our Christmas ranges'. This upbeat commentary augurs well for sales of everything from festive pyjamas and decorations to Christmas trees, and Machin promised shareholders that 'all of us will be sleeves rolled up, out in stores and distribution centres, bringing the magic of M&S alive for our customers this Christmas'.

Another likely winner is discounter **B&M European Value Retail (BME)**, the £5.8 billion cap with the ability to seasonally flex its product range, on the basis shoppers on a budget will trade down to its keenly priced toys, Christmas decorations, confectionery and booze. *Shares* anticipates positive news when B&M issues its third quarter update on 9 January.

At the first half results (9 November), B&M did flag softer UK trading in the opening six weeks of the Golden Quarter, with like-for-like sales growth slowing from 6.2% in the first half to 1.6%. However, Alex Russo-led B&M assured the market that momentum had proved 'particularly strong in the last three weeks'.

Also set up for the seasonal sales sprint is **JD Sports Fashion (JD.)**, the self-styled 'king of trainers' whose core 'sneakerhead' consumer, typically a youthful shopper unfettered by mortgage and energy bills, should prioritise spending on that must-have pair of trainers.

One risk to consider is that JD Sports is lapping tough comparatives, having delivered total revenue growth of 20%-plus over the six weeks to 31 December 2022. However, recently raised guidance from US retailers **Dick's Sporting Goods (DKS:NYSE)**, **Hibbett (HIBB:NASDAQ)** and **Foot Locker (FL:NYSE)** offers a positive read-across for JD Sports and instils us with a measure of confidence.

DISCRETIONARY SPEND UNDER PRESSURE

Judging by a profit warning (29 November) from **Halfords (HFD)** pinned on weak sales of discretionary categories including bicycles, purveyors of big-ticket items are in for a rougher ride this Christmas.

We would expect subdued sales performances from the likes of sofas seller **DFS Furniture (DFS)** and home improvement duo **Kingfisher (KGF)** and **Wickes (WIX)** as cash-strapped consumers put off DIY projects to the new year.

Shifting big ticket furniture may prove challenging for homewares leader **Dunelm (DNLM)** too, but this high-quality beneficiary of Wilko's demise should provide comfort and joy

ELF ON THE SHELF – BEAUTY PRODUCTS PURVEYORS TO PROVIDE SOME GLITTER?

The opportunity to glam up for Christmas party season should boost sales at companies beyond the retail sector such as French beauty and cosmetics behemoth **L'Oréal (OR:EPA)** and its US counterpart **Estée Lauder (EL:NYSE)**.

And *Shares* sees strong Christmases in store for beneficiaries of the so-called 'lipstick effect', the idea that consumers spend more on low-price luxuries during tougher times. Festively-monikered mass market cosmetics brand **e.l.f. Beauty (ELF:NYSE)** is gobbling up market share, while affordable colour cosmetics supplier **Warpaint London (W7L:AIM)** should benefit from retailer restocking given strong sell-through this Christmas

WHAT ABOUT THE US BIG BEASTS?

Christmas is enormously important for US retail giants **Walmart (WMT:NYSE)** and **Amazon (AMZN:NASDAQ)**, which can be relied upon to enhance their market shares this year. However, while the third quarter results season was robust, retailers across the pond are cautious over the outlook for 2024 with pandemic savings draining away and inflation and higher rates finally beginning to hurt US shoppers.

The deteriorating trend was confirmed by the latest profit warning (30 November) from British bootmaker **Dr. Martens (DOCS),** which bemoaned an 'increasingly difficult consumer environment' in the US.

According to Adobe Analytics, US Black Friday online sales came in at $9.8 billion, up 7.5% versus the 2022 numbers, while Cyber Monday spending rose 9.6% year-on-year to reach $12.4 billion, representing the biggest online shopping day of all time.

But a key factor behind the increase was the growth in 'buy-now, pay-later' options, which shows consumers are feeling the effects of inflation and higher rates and points to a gloomy 2024 in store.

Shares expects Bentonville-based Walmart, which posted strong third quarter results on (16 November), to lure in price-sensitive shoppers with its cheap groceries, fashion, toys, electronics, and seasonal decorations. Despite its compelling value offering, Brian Cornell-bossed **Target (TGT:NYSE)** could find the going tougher given its skew towards more discretionary general merchandise.

US shoppers' desire for a bargain should drive further market gains for off-price retailers including discount apparel-to-home fashions seller **TJX Companies (TJX:NYSE)**, which is nicely positioned as a shopping destination for Christmas gifts, while department store chain **Burlington (BURL:NYSE)** has positive festive momentum, having delivered (21 November) robust third quarter earnings and comparable store sales as inflation-weary shoppers traded down and boosted takings.

for investors as consumers spend on its affordable soft furnishings. The self-styled 'Home of Homes' is an ideal destination for hard-pressed shoppers and hard-up university students to load up on everything from decorations and Christmas bedding to festive lights and turkey platters.

Also capable of delivering some festive sparkle is lately unloved technology products purveyor **Currys (CURY)**, a possible beneficiary of robust demand for gadgets ranging from laptops and cameras to headphones to gaming headsets and smart toys. Currys has results for the first half to October 2023 on the slate for 14 December, but investors will have to wait until 18 January for an update on how the retailer performed this Christmas.

Other names gearing up for Christmas are toy and hobby products plays such as fantasy miniatures maker **Games Workshop (GAW)** and **Hornby (HRN:AIM)**, the small cap behind the eponymous train sets, Scalextric sets and Airfix kits which entered the Christmas period with a bulging order book. 'Although, like everyone, we are seeing the ramp up into Christmas trade coming later than in previous years,' said Hornby on 23 November, 'we are starting to see some encouraging increases in performance.' Hornby's sales should also benefit from its recent launch of The WonderWorks in Margate, its first experiential site comprising an exhibit, a large retail space and a café.

As conflict rages in the Middle East and Ukraine – understand the dynamics of the defence sector

We explore how to play the industry through funds and stocks

Conflict is always an unhappy subject, but it remains an area of real focus across the globe. Cross-border collisions of ideology, hegemony, raw materials, and even survival, mean national budgets reach astronomical levels, especially in the US, by far the world's largest military spender.

In 2022, global military budgets hit an all-time high of $2.2 trillion, according to data released by the Stockholm International Peace Research Institute, or SIPRI, the eighth consecutive year that spending has increased. By far the sharpest rise in spending (up 13%) was seen in Europe. This was largely accounted for by Russia and Ukraine in the wake of war.

Amid a major escalation of violence in the Middle East, defence stocks have been on an almost universal upwards trajectory, leading portfolio managers and analysts to examine the potential long-term effects of a more protracted conflict in the region.

Yet the link between conflict and profit is not as simple as the investing public may occasionally imagine, argue Morningstar analysts. 'We see October's sudden price increase in defence stocks as an overblown and simplistic reaction to the outbreak of war in Israel and Gaza,' says Nicolas Owens, equity analyst at Morningstar.

'The dots between military combat and the profit of a defence contractor do not connect nearly as directly as they seem to in the investing public's imagination.'

Owens and his team see no reason to alter ratings or valuations of defence contractors considering the latest violence, believing that long-term development and resupply of missile defence technology is already baked sufficiently into their forecasts.

AN ETHICAL QUESTION

Some industries feel more taboo to invest in than others. Nobody wants to see war happen, but when it does, the defence industry is there. Defending our way of life and the freedoms we take for granted is also part of a larger picture, and that will attract many investors to turn to the sector for typically steady returns from relatively low-risk businesses.

At its core the defence industry produces the vehicles and aeroplanes, weapons and defence systems needed to wage a war, and to defend

World's biggest military spenders ($bn)

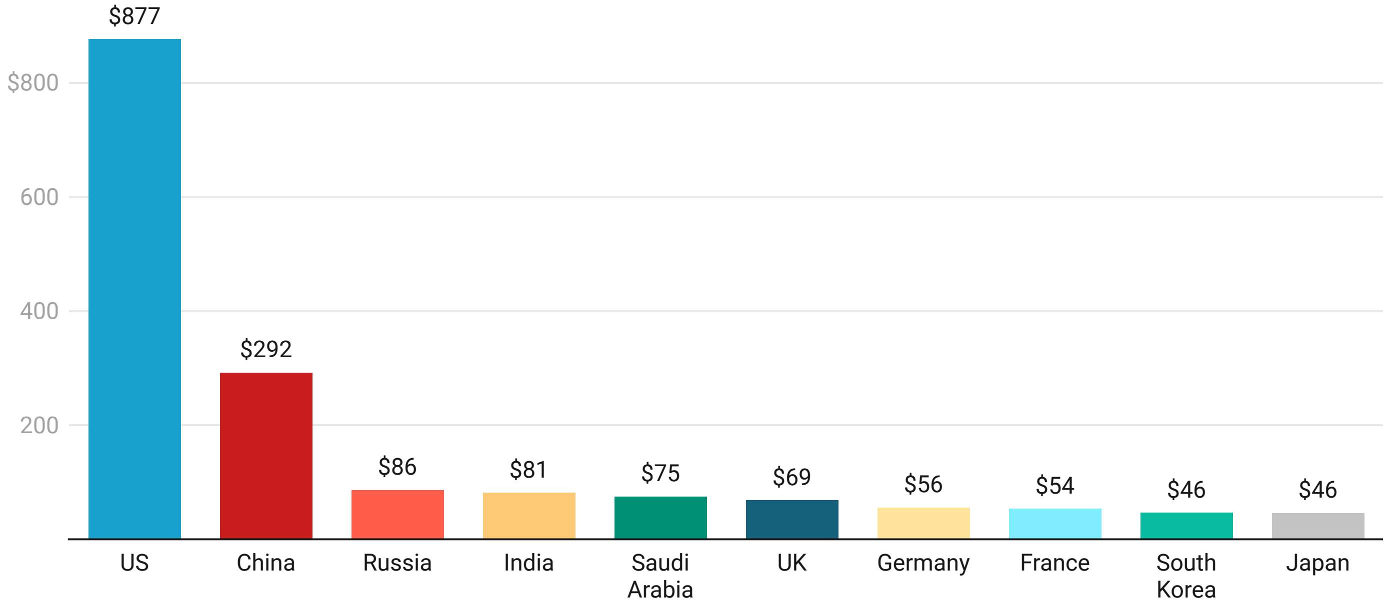


Chart: Shares magazine • Source: Stockholm International Peace Research Institute (SIPRI), 2022 data

World's biggest military spenders (%)

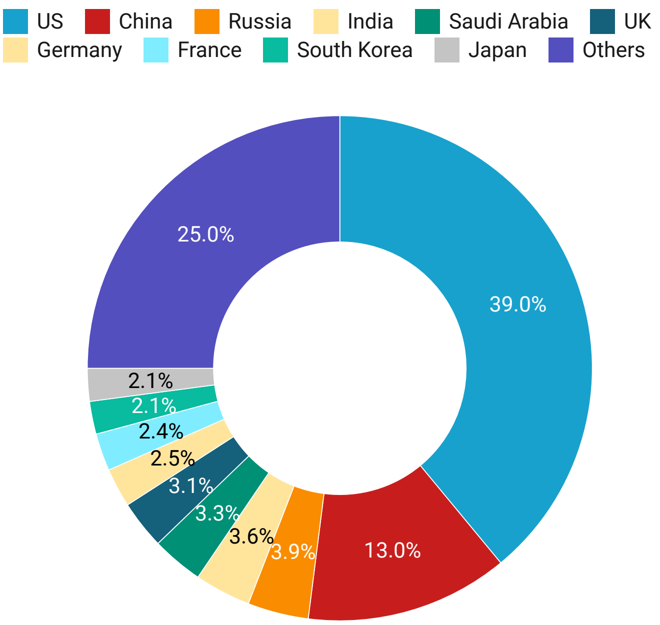


Chart: Shares magazine • Source: Stockholm International Peace Research Institute (SIPRI), 2022 data

oneself from aggressors. But it also comprises otherwise mundane companies like data centre and IT network businesses, warehouse operators to manage inventory and administrative functions, and software companies to provide vital data.

Equity market investors have long recognised that defence is becoming a long-term growth theme.

WHAT IS THE CURRENT BACKDROP?

The war in Ukraine has fundamentally shifted the geopolitical calculus and has accelerated what might be called the fragmentation game – a dynamic that breaks up and realigns global supply chains to account for what will become a multipolar world over time.

The US and China were already engaged in the fragmentation game since the early days of the Trump administration with Europe reluctant to get involved because of its deep trading relationships with China and especially Germany's dependence on selling machines to China and getting cheap energy from Russia.

The war in Ukraine and Russia's attempt to weaken Europe through its energy exports pulled Europe into the fragmentation game. 'Europe's defence budgets are now increasing at a rapid pace and will continue growing over 10% a year over the next five years,' says Peter Garnry of Saxo Bank.

'Central and western European states spent $345 billion in 2022, which in real terms surpasses the spending in 1989, the last year of the cold war. The new spending level takes central and western European countries almost on par with military spending in East Asia, highlighting that Europe is still a formidable power.'

World's biggest defence contractors

	Total arms sales, 2021 ($m)
Lockheed Martin (US)	$60,340
RTX (US)	$41,850
Boeing (US)	$33,420
Northrop Grumman (US)	$29,880
General Dynamics (US)	$26,390
BAE Systems (UK)	$25,851
China North Industries (China)	$21,570
Aviation Industry (China)	$20,110
China Aerospace & Tech (China)	$19,100
China Electronics (China)	$14,990
CASIC (China)	$14,520
Leonardo (Italy)	$13,870
L3Harris Technologies (US)	$13,360
China State Shipbuilding (China)	$11,130
Airbus (France)	$10,850

Table: Shares magazine • Source: Statista, 2023

BIG MILITARY BUDGETS

European defence companies continue to see strong order intake as Europe is significantly increasing its defence spending in a response to the war in Ukraine. 'Our defence theme basket, which is one of the best performing baskets over the past year, and especially driven by European defence stocks such as **Saab (SAAB-B:STO)**, **Hensoldt (HAG:ETR)**, Norway's **Kongsberg Gruppen (NSKFF:OTCMKTS)** as well as **Leonardo (LDO:BIT)** and **Rheinmetall (RHM:ETR)**.

In March 2023, German arms manufacturer Rheinmetall joined Frankfurt's DAX index after seeing its share price surge 124% in 2022.

The Dusseldorf-based company has now joined Germany's corporate titans such as **SAP (SAP:ETR)**, **Volkswagen (VOW3:ETR)** and **Siemens (SIE:ETR)** on the nation's blue-chip index.

In a country still haunted by the Second World War, German weapons manufacturers are not celebrated like its world class carmakers or engineering firms, yet it remains a major player on the global stage. Germany was the world's fifth-largest arms exporter between 2018-2022, according to a report earlier this year SIPRI, ranked just behind China and accounting for 4% of the global market.

Rheinmetall, which makes parts of the Leopard tanks that Berlin has sent to Ukraine, posted record results in 2022 (to 31 December) and has been racing to hire more staff and boost capacity through 2023.

BAE SHARES HAVE RALLIED

Among the defence stocks to have benefited from recent geopolitical instability is **BAE Systems (BA.)**, which is the UK's largest manufacturer. Its shares have posted a 21% gain this year and have rallied more than 7% since the most recent conflict in Gaza. BAE produces everything from GPS communications products to boats and naval canons and has just won a trilateral contract to manufacture next-generation nuclear submarines for the South China Sea-oriented

UK defence sector

	Market cap (£m)	Five-year performance
Avon Protection	£240	-39%
Babcock	£1,999	-30%
BAE Systems	£31,802	114%
Chemring	£874	88%
Cohort	£210	22%
Melrose	£7,003	-94%
MS International	£123	281%
Qinetiq	£1,738	-2%
Rolls-Royce	£22,746	-7%
Senior	£724	-28%
Velocity Composites	£20	43%
Westminster	£4	-86%

Table: Shares magazine • Source: Sharepad, LSE

BAE Systems

(p)

Chart: Shares magazine • Source: LSEG

Aukus pact.

In August, Morningstar analysts maintained their Wide Moat Rating on the company, while raising their fair value estimate for its stock to £11.70, reflecting an environment of higher defence spending over the medium term. This compares with a current share price of £10.47.

But Morningstar's Owens says the leap between the situation in Israel and the belief that BAE Systems will stand to benefit specifically from events in the region is a big one. 'Live footage of Israel's domestically-developed short-range missile defence system referred to as the 'iron dome' demonstrates capabilities most closely associated with **RTX's (RTX:NYSE)** and BAE Systems' munitions portfolios, neither of which exceed 10% of company revenue,' he says.

WHICH COMPANIES CAN I INVEST IN?

RTX is the renamed Raytheon Technologies, one of the world's largest defence contractors.

'When combat depletes munition stockpiles, they will be resupplied from allies' existing stockpiles with zero impact to the manufacturer that previously delivered them', says Owens.

Eventual orders for more of the weapons may come, if current production rates will not refill stockpiles in time, but 'adding capacity

is expensive and time consuming, and thus not a bullish outcome in our view,' says the Morningstar analyst.

In use since 2011, the Iron Dome is a mobile collection of surface-to-air rocket launchers distributed across 10 'batteries' throughout Israel. As for defence giant RTX, which makes missiles and targeting systems, It sits among the major US defence companies Morningstar analysts believe are undervalued.

The UK sector is rather threadbare these days after overseas takeovers of Cobham, Meggitt and Ultra Electronics, with BAE and defence technology firm **Qinetiq (QQ.)**, which was spun out of the Ministry of Defence in the early 2000s, standing out. **Rolls-Royce (RR.)** is largely a civil aerospace company with limited exposure to defence spending.

CAN I PLAY THE THEME THROUGH FUNDS?

Very much so if you're willing to take an unfussy approach. Most of the global defence leaders are included in the S&P 500, so a general S&P ETF gives some exposure, while BAE is in the FTSE 100, as is Rolls-Royce, although it doesn't have as big of a footprint in defence. **Babcock (BAB)** and Qinetiq are part of the FTSE 250.

Getting more specific exposure is trickier. The **HANetf Future of Defence UCITS ETF (NATP)** and **VanEck Defense UCITS ETF A (DFNG)** are two small ETFs that have several defence companies in their top 10 holdings, plus a load of more general engineers and other stocks that you might not call defence firms as such, but may earn part of their revenue from specialist suppliers to the industry, such as French firm **Thales (HO:EPA)**, or US networks kit manufacturer **Cisco Systems (CSCO:NASDAQ)**.

Both ETFs are small, with £11 million and £80 million of managed assets and neither is cheap, with annual charges running at 0.49% and 0.55% respectively, but they may be worth further investigation for some investors.

OUR TOP STOCK PICK

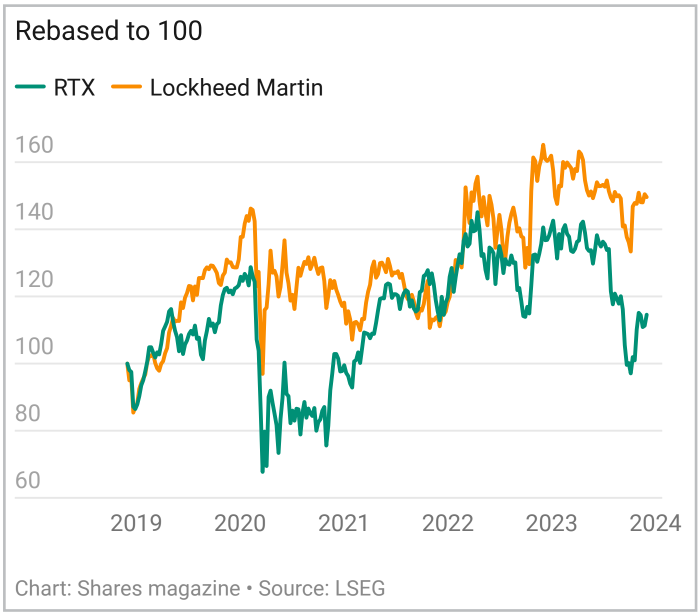
LOCKHEED MARTIN (LMT:NYSE) $449.41

The biggest defence company in the world, Lockheed Martin produces top fighter jets like the F-35A aircraft and has a $7.8 billion contract with the US government to produce missiles and electronics. It's a stable company, although the stock has fallen around 6% this year.

But that, we believe, presents an opportunity. Return on capital and equity stand at 21.6% and 67% respectively, and low double-digit operating margins have scope to rise. Net profit has consistently grown faster than revenue and free cash flow has been impressively consistent over recent years.

Net debt needs watching, net gearing is 149% of assets according to Stockopedia data, but that free cash flow and the long-term nature of contracts suggest a company capable of managing above average debt levels.

At $449.41, the 12-month rolling price to earnings multiple is 16.8, while the shares carry a prospective 2.85% income yield.



Learning big lessons from Calnex and Synthomer mistakes

Examining situations where we got it wrong and any conclusions to draw

As we approach the end of the year it is a good time to take stock with your investing, and it's no different for the team at *Shares*. We do our best to furnish you with strong investment ideas every week, but we clearly do not get it right every time.

Two big losers from the last 12 months or so which stand out as examples where we need to hold our hands up and acknowledge we got it wrong, and where a reader has (very politely) asked for an update, are telecoms network and cloud computing testing outfit **Calnex (CLX:AIM)** and plastics manufacturer **Synthomer (SYNT)**.

Looking back at investments which have gone awry can be a useful exercise. If you are prepared to take on board the lessons from these episodes you stand a much better chance of making better decisions in the future.

Notably both Calnex and Synthomer are small-cap stocks where the risks are inherently greater. These less mature businesses can see a single setback make a big impact across the wider group. A bad purchasing decision or botched computer systems upgrade can be the difference between meeting and missing expectations.

With Synthomer we have to go back to September 2021 when we first flagged the shares' appeal in a wider look at the chemicals space. The shares have been in retreat almost ever since. Unfortunately, we doubled down in May 2022 flagging the company as an ultra-cheap stock to buy.

In simple terms the company was hit by lower demand for latex medical gloves coming out of the pandemic. Its NBR division supplies the nitrile latex used in the manufacture of these gloves. The company has subsequently suffered from wider economic weakness which has hit other parts of the business.

> **"We do our best to furnish you with strong investment ideas every week, but we clearly do not get it right every time"**

The first pointer that all was not well with Synthomer was the lowly rating – suggesting the market did not believe the earnings forecasts. Such situations can represent big opportunities, but often the market is proved right and that's certainly been the case here. Chemicals firms are also typically highly sensitive to fluctuations in the economy, meaning we should have taken a closer look at the balance sheet which became increasingly strained as trading deteriorated.

Synthomer's problems became so bad it was forced into a £276 million rights issue at a heavily discounted price in September 2023. Berenberg analyst Sebastian Bray believes the rights issue has fixed its balance sheet.

'The stock's current situation, characterised by depressed end markets and low valuation multiples, is reminiscent of the period post-financial crisis; shares more than quadrupled in the subsequent two years. We believe shares offer attractive early-cycle exposure to any economic recovery,' argues Bray.

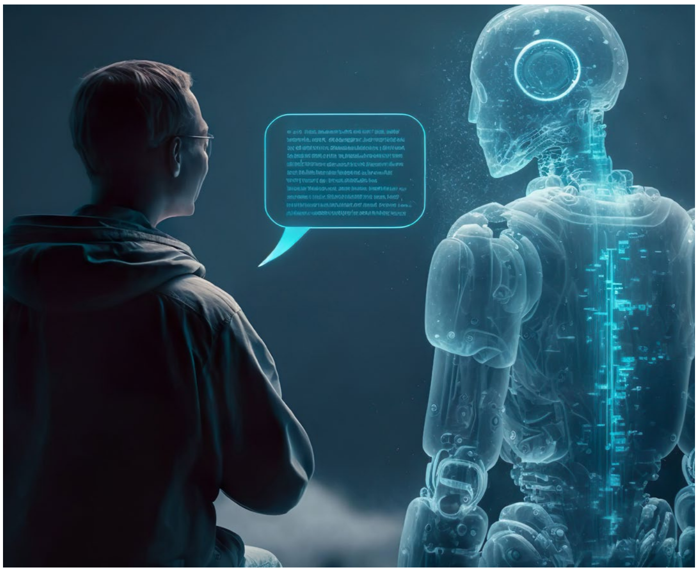
It would be a brave investor who looked at the chart for the last two years and opted to invest for such a scenario.

Scotland-based Calnex was a more recent misstep on our part. We highlighted it in August. It has nearly halved in the interim – the hammer blow to the shares coming from a warning on 10 October.

Revenue was pitched at being 20% to 30% below previous expectations thanks to subdued order levels. Profit warnings often come in threes (at least), so buying after an earlier warning predicated on a weak macro-economic backdrop, which hadn't really shifted in the meantime, was in hindsight a mistake. At least in the case of Calnex it has net cash on the balance sheet.

Is it worth investing in artificial intelligence ETFs?

AI trackers have materially underperformed Nvidia in 2023



Artificial intelligence (AI) exchange traded funds (ETFs) have struggled to keep pace with the big AI stock of 2023 – Santa Clara-based microchip designer **Nvidia (NVDA:NASDAQ)**.

Nvidia's shares have risen 245% year-to-date (valuing the chipmaker at $1.22 trillion) in contrast the main AI ETFs: **L&G Artificial Intelligence (AIAG)** has returned 34.7% and **WisdomTree Artificial Intelligence (INTEL)** has returned 28.6% over the past year.

Over three years the WisdomTree Artificial Intelligence UCITS ETF has delivered a return of 8.2% and the L&G Artificial Intelligence UCITS ETF has returned 7.4%.

LOOKING AT AI ETF PERFORMANCE

That doesn't mean these products are not fit for purpose but it underlines the value of understanding what underlying investments they hold.

Chris Ganatti, global head of research at WisdomTree tells *Shares* AI ETFs have surrendered some of their popularity with investors in the latter part of this year: 'Investing in AI ETFs has been more popular in the first half of than the second half of 2023.

'Even though the AI story is [ever present] US investors have been reluctant to invest due to uncertainty surrounding what direction the US central bank, the Federal Reserve is going to take with interest rates. There is also the issue of US inflation. This has perhaps dampened investor enthusiasm a little bit towards investing in AI ETFs.'

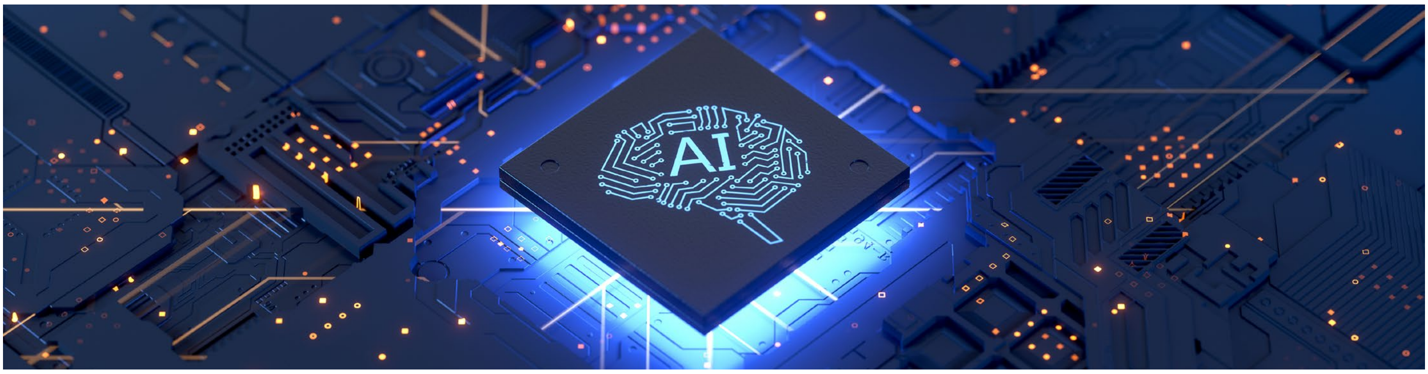
AI ETFs provide exposure to a large basket of AI stocks – so an investor can have diversified exposure to the AI theme. The additional bit of good news is the costs associated with AI ETFs are relatively low: 0.49% per annum for the L&G Artificial Intelligence UCITS ETF and 0.4% for the Artificial Intelligence UCITS ETF.

How AI ETFs have performed

ETF	One-year total return	Three-year total return	Ongoing charges
L&G Artificial Intelligence	34.7%	7.4%	0.49%
WisdomTree Artificial Intelligence	28.6%	8.2%	0.4%
Global X Robotics & Artifical Intelligence	19.0%	n/a	0.5%

Data to 29 November 2023

Table: Shares magazine • Source: JustETF



WHAT DO AI ETFs INVEST IN?

There are some similarities in what AI ETFs invest in, for example most of them hold Nvidia as you would expect but holdings are fully diversified across various themes like automation, robotics, deep learning and computer vision.

L&G Artificial Intelligence

Top holdings

Company	%
Splunk	2.9%
Alteryx	2.6%
Microsoft	2.5%
Palo Alto Networks	2.4%
Crowdstrike Holdings	2.3%
Alphabet A	2.1%
ServiceNow	2.1%
Advanced Micro Devices	2.1%
Arista Networks	2.1%
Nvidia	2.0%

Data to 31 October 2023

Table: Shares magazine • Source: Legal & General Investment Management (LGIM)

L&G Artificial Intelligence UCITS ETF, for example, has 62 holdings which, apart from Nvidia, include US software and data science firm **Alteryx (AYZ:NYSE)**, San Francisco-based machine data firm **Splunk (SPLK:NASDAQ)** and US cybersecurity company **Crowdstrike (CRWD:NASDAQ)**.

Interestingly WisdomTree does have Nvidia in its portfolio but it is not one of the top holdings – likely explaining its slightly weaker showing over the last year relative to the L&G product. It tracks an index created in partnership with Nasdaq which includes the following:

- **Enhancers:** Companies who are a prominent force within AI, but whose relevant product or service within AI is not currently a core part of their revenue;
- **Enablers:** Companies who are key players in the AI space, with some of their core products and services enabling the continued development of AI;
- **Engagers:** Companies whose main focus is in providing AI-powered products and services.

Wisdomtree Artificial Intelligence

Top holdings

Company	%
Splunk	2.9%
MediaTek	2.8%
United Microelectronics	2.4%
Dassault Systemes	2.4%
Synopsys	2.4%
Micron Technology	2.3%
Mobileye Global	2.3%
Realtek Semiconductor	2.3%
CCC Intelligent Solutions	2.3%
Palo Alto Networks	2.3%

Data to 31 October 2023

Table: Shares magazine • Source: WisdomTree UK

Within each group, an AI intensity score is assigned to each company based on factors including: the estimated portion of a company's revenues which are attributable to AI products and services; how core AI is to the company's product offering and positioning; the market prominence of a company's AI solution.

Then, the companies with the top AI Intensity Score in each group are selected for inclusion. The groups' total weight is set to 10% for Enhancers, 40% for Enablers and 50% for Engagers. Finally, individual companies within each group are equally weighted.

Global X Robotics & Artificial Intelligence ETF (BOTZ), as the name suggests, invests in companies with a robotics focus alongside AI stocks.

Tejas Dessai, research analyst at Global X says: 'An AI ETF can hold a mix of 'Big Tech' companies (who have the budgets to innovate), chipmakers, semiconductors, data storage providers, robotics, and automation companies.'

The global robotics market is set to nearly double to $96 billion by 2026 from $55 billion in 2021, according to GlobalX, and is a 'growth area', according to this provider.

Global X's Robotics & Artificial Intelligence vehicle holds 38 companies ranging from Nvidia (its largest holding at 14.12%) to **Intuitive Surgical (ISRG:NASDAQ)** (9.98%), a robotics assisted surgery pioneer and maker of the da Vinci surgical systems and **ABB (ABBN:SWX)** a Swedish-Swiss multinational robotics and machine automation supplier (8.28%).

IS THE THEME OVERPLAYED?

Global X's Dessai does not think investors have missed the boat on AI, he tells *Shares*: 'We think there are opportunities still ahead of us in the AI sector. We are now in the first phase of the AI revolution.'

While Nvidia has been the clear AI winner on the stock market this year, it could be difficult to call exactly which companies will benefit most from this theme in the medium term and this is the argument for using an ETF to gain diversified exposure. Just make sure you do your homework.

By **Sabuhi Gard** Investment Writer

Spotify wraps up job cuts for investors but could a short-term rally turn sour?

Shares up sharply as return to profit is accompanied by news it will trim global workforce by 17%

When music streaming platform **Spotify's (SPOT:NYSE)** announcement of a return to profitability was immediately followed by plans for further job cuts – its share price jumped more than 7%.

There's nothing investors like more than hearing an executive team has their fingers wrapped tightly around a company's' purse strings.

Costs have become a major issue over the past year and even as inflation cools businesses are having to get used to the new economic landscape where money is expensive and wages a significantly bigger burden.

Year to date Spotify's share price is up almost 150% as the company reined in spend on controversial and less than prolific podcast creators like Harry and Meghan, bumped up prices and still managed a significant growth in subscriber numbers.

In a letter to employees, Spotify's chief executive,

Daniel Ek said that 'substantial action to right-size our costs was the best option to accomplish our objectives' which include reaching a billion users by 2030.

But 17% is a sizeable chunk of Spotify's workforce and comes off the back of two separate culls earlier in the year, which must prompt questions about whether the company can maintain performance with such a reduction in headcount.

Spotify Technology

Chart: Shares magazine • Source: LSEG

Danni Hewson: Insightful commentary on market issues

Attracting users to service requires creating unmissable content and delivering a consistent user experience, any slippage would result in audiences defecting to competitors more than happy to add to their own numbers.

SPOTIFY IS NOT ALONE

Spotify is far from alone in its predicament. Many tech companies rushed to build up their employee base during the pandemic and are now having to reassess as the economic backdrop becomes more uncertain and growth slows significantly.

According to layoffs.fyi the website that tracks tech job cuts, tech companies globally laid off 165,000 employees in 2022.

That number has jumped to over 255,000 tech workers being let go in 2023 to date, once you factor in the latest Spotify cuts. **BT (BT.A)** announced in May it was turning to AI to replace some of its 55,000 workers it plans to axe by the end of the decade, others like Meta told investors they'd simply got the sums wrong and had hired too many people too quickly without a clear business need.

Always controversial, Twitter boss Elon Musk said during an interview at the *Wall Street Journal's* CEO Council in May that he felt many companies could and should go much further seeing 'potential for significant cuts at other companies without affecting their productivity, in fact increasing their productivity'.

IS IT THE RIGHT MOVE?

Many analysts have delivered similar commentary on the changing jobs picture but considering the current trajectory for Musk's social media platform, following a massive reduction in headcount, there will be many taking what he has to say with a liberal pinch of salt.

The efficacy of that sort of stance is questioned in JP Guthrie's paper entitled *Dumb and Dumber, the impact of downsizing on firm performance as moderated by industry conditions*.

It raises questions about the impact of cuts on the productivity of those left behind and finds there can be subsequent decreases in profitability following downsizing.

Morale is crucial especially for companies like Spotify with an eye on continued growth. Then there's the conundrum that if the company does achieve that growth and it then needs to add to its headcount, can it find employees with the same level of skills to replace those it let go?

Training and skills are often quoted as two of the things needed for an economy to grow and training takes time and money if it's done correctly.

THE VALUE OF STAFF

Investors aren't wrong to want profitability, they aren't wrong to be worried about costs, but they should also concentrate on outlook and ambition and bosses need to consider the value of staff beyond that of items on a spreadsheet that need to be minimised in order to deliver an upbeat message on an earnings call.

And of course, there's also the question about where those skilled workers might end up, because if it's in the employ of a competitor the repercussions could be felt for years.

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Patrick Moloney, CEO

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Louis Florentin-Lee, Managing Director

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Why the UK stock market may not be the value opportunity you think it is

London-listed shares have fallen behind their global counterparts in 2023 yet again

Once again it looks like the year is going to finish with the UK stock market being a notable laggard on the global stage. So far this year the FTSE All Share has returned around 4%, compared to 14% from the S&P 500, and over 10% from the European stock market.

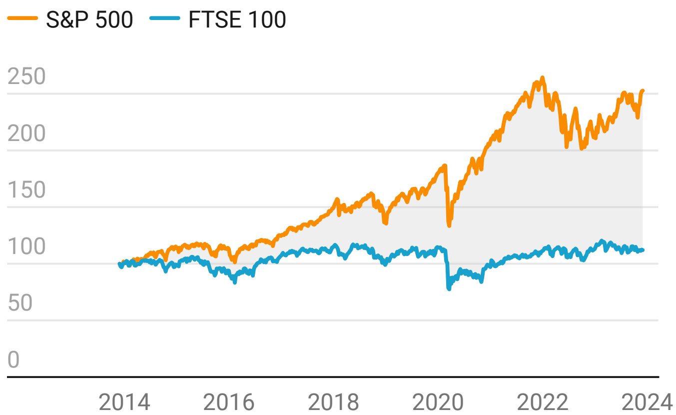
The UK has been viewed by some as unloved and undervalued for a while now, and with a reasonable amount of justification. But there are longstanding trends which go some way to explaining the negative sentiment towards the UK market, and which don't look like shifting in the immediate future.

UK IN GENERAL IS UNLOVED

One current malaise affecting the UK stock market is negative sentiment towards the UK economy. The IMF predicts the UK will grow by only 0.5% this year, and by 0.6% next year. The UK economy and the UK stock market are of course two very different beasts. Around 80% of FTSE 100 revenues come from overseas, and that falls to around 60% for the FTSE 250.

However, you can turn those figures on their head, and say that still means 20% or 40% of the respective revenues of these indices come from the UK. If you have a negative view of the UK economy, why would you want such a big slug of exposure? Especially when you can hop across the pond and invest in the S&P 500, which has only a few percentage points of its revenues derived from the UK and has been performing very nicely.

FTSE 100 is left in the shade



Rebased to 100

Chart: Shares magazine • Source: LSEG

There is widespread acceptance that interest rates look to have peaked in the UK, and markets are actually now anticipating three rate cuts in the second half of next year. On the face of it that should be good news for UK economic growth, but that's not the whole picture. The Bank of England reckons that only half of the interest rate hikes pushed through in the last two years have taken effect on the economy.

Analysis from the IFS and Citi back this up. Their figures show the spike in housing costs from higher mortgages and rents will actually peak in the first quarter of 2025. That's not because interest rates are forecast to rise, but because mortgage holders across the country are only gradually rolling off older and cheaper fixed term deals.

NOT OUT OF THE WOODS YET

Inflation receding and interest rates flatlining or even falling in future is undoubtedly good news for the UK economy, compared to the alternative. But it feels premature to say we're out of the woods just yet. And the very sizeable and rapid shift in monetary conditions we have witnessed presents large downside risks to economic forecasts. Ultra-low interest rates and QE were an experiment that took us all through the looking glass, and we have now been unceremoniously yanked back into the real world where borrowing money actually costs us a pretty penny. A period of adjustment is only to be expected. Add in the fact that the tax burden is forecast to rise to a post war high in the next five years, and you can see how UK consumer purses might not be precisely gushing for some time to come.

The good news about the economy at such junctures is that it is cyclical. Better rates of growth will return to these shores at some point. And while the US economy is performing well, many of our European cousins are not doing so much better than us. The German economy, in particular, is forecast by the IMF to contract by 0.5% this year.

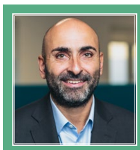
THE IMPACT OF PASSIVE INVESTING

Perhaps not as transitory is the appeal of passive investing, a trend which has been gathering pace for the last decade, and which might be partly responsible for the UK's lacklustre performance. It's true there are plenty of passive funds available which track the UK market, but logically, passive investing is a global game. If you simply want to follow the stock market based on the size of the companies in it, then it doesn't make a huge amount of sense to limit yourself to just the UK. Doing so is actually making an active decision about regional asset allocation. Granted some people will take this approach, but many more passive investors, and indeed professional active investors who are tied to a benchmark, will invest globally. Currently that means investing around two thirds of your portfolio in the US, and only around 4% in the UK. A global stock market tracker now has greater exposure to each of **Apple (AAPL:NASDAQ)** and **Microsoft (MSFT:NASDAQ)** than it does the whole of the UK stock market. There is a legitimate question about whether the strong showing of the US stock market and weak performance of the UK stock market have now gathered a momentum of their own because of the rise of index investing, which favours the big at the expense of the small.

WHAT THE UK IS GOOD AT

There are some things the UK stock market is undoubtedly good at, and one of those has to be providing dividends. That makes it an attractive destination for income seekers. The UK's small cap sector is also worthy of a mention. Like the rest of the market, it's laid low at the moment, but has delivered dazzling returns over the long term.

Looking at the UK market as a whole, it does look undervalued, both compared to the US and its own history. It's true sentiment can shift quickly in markets, and ahead of changes in the real economy, but the factors which explain that might not dissipate any time soon. Those still invested in UK plc have exhibited remarkable forbearance in recent years, but they may yet have to exercise more patience before there is a turnaround.



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

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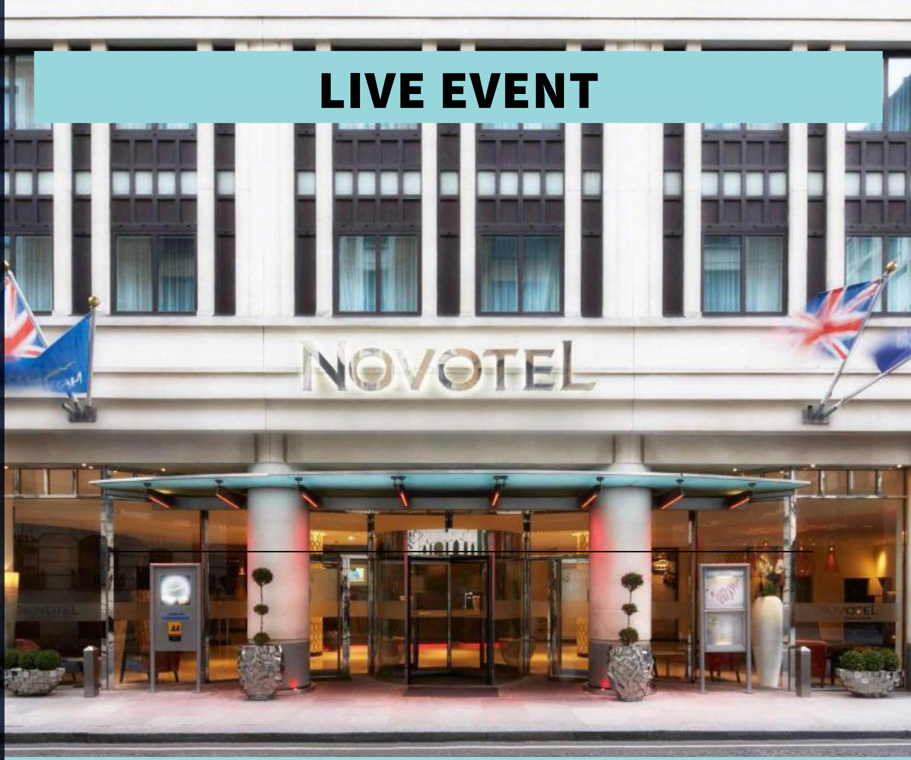

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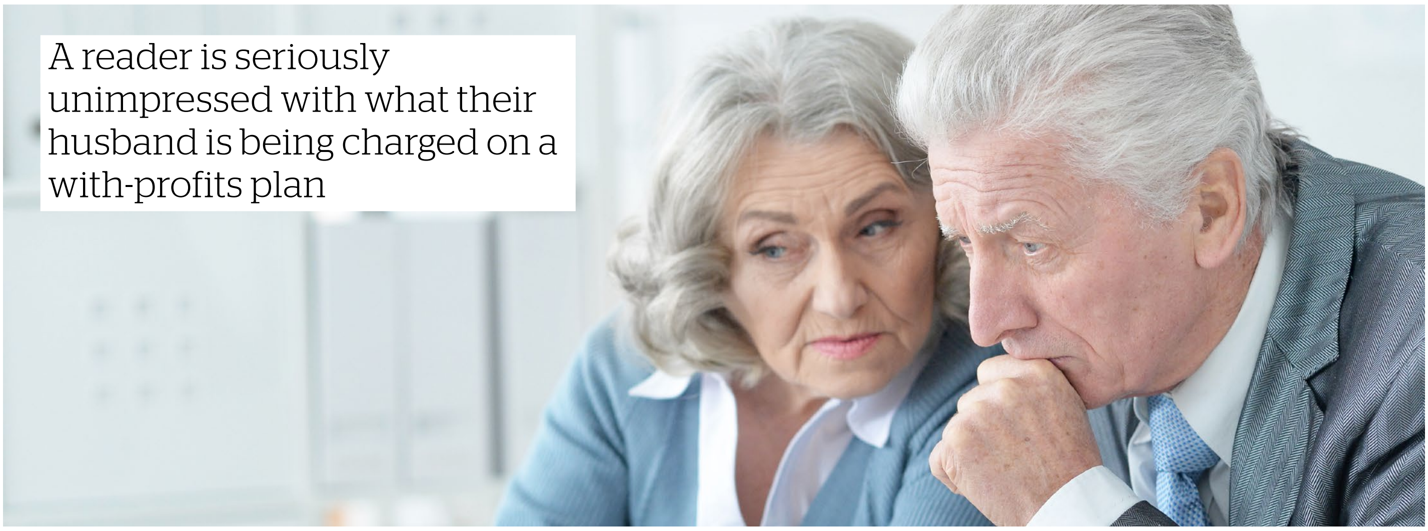
I'm fed up with high pension costs: should I switch provider?



A reader is seriously unimpressed with what their husband is being charged on a with-profits plan

My husband is aged 69 and does not plan to retire until he is 75. He has had a 'with-profits' personal pension plan since 2004. The current plan value (excluding the final bonus) is £127,116, the final bonus (which they say they can't guarantee) is £72,319 and the market value reduction is £5,657.

Last year, he paid £3,000 in personal pension contributions to the plan. Total charges and costs were 1.47%. Both of us were horrified by the eye-watering charges, which all but wipe out any growth on his plan, before factoring in the impact of inflation.

We both invest with a different platform now (SIPPs and ISAs) and were wondering about transferring his with-profits pension to invest in a SIPP instead. However, the opaqueness of the merit of the with-profits plan makes it impossible to weigh up the risks - the default position (of course) being that my husband sticks with his existing provider.

Why are pension providers still allowed to operate these immoral schemes and impose such high charges and arbitrary transfer penalties?
Sarah

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

If you have a with-profits pension, your contributions will be invested with those of other members into a collective pot.

With-profits pensions will usually offer to pay 'annual' and 'final' (sometimes called 'terminal') bonuses – the former each year, the latter at the end of your policy term. These bonuses will be a percentage of the value of your fund. The aim of this approach is to smooth out investment performance, so you are less directly exposed to rises and falls in the value of your investments over the shorter term.

A market value reduction or 'MVR' is sometimes applied when a with-profits investor chooses to transfer their pot to a new provider before the end of their policy term. The purpose of an MVR is to ensure fairness across members.

For example, suppose there are three investors in a with-profits fund whose policies are worth £100,000, meaning the total value of the fund is £300,000.

If the fund dips in value by 10%, for example because of a market shock, and one investor chooses to take their policy without an MVR being applied, only £170,000 would be left between the two remaining investors (i.e. £85,000 each).

In these circumstances, the provider may apply a 10% MVR on the transferring investor in order to ensure all members receive fair value (i.e. £90,000 each).

In terms of costs and charges, it is crucial to keep these as low as possible, while also investing in a diversified range of assets and taking an approach that is in line with your risk appetite. It is normal for a percentage charge to be based on your total assets, although a figure of 1.47% is relatively high by modern standards.

Unfortunately, your husband is not alone in feeling trapped in a product that isn't delivering what was hoped for. Lots of people sold with-profits policies have seen their investments perform poorly, meaning large MVRs can be applied to those transferring out.

While I sympathise with your view this feels unfair, the key question is whether or not the policy clearly set out that an MVR could apply in these circumstances.

If you feel this was not properly explained to you – or not properly spelled out in the scheme documentation – you can complain to your pension provider. If this complaint is rejected, you can go to the Financial Ombudsman Service for an independent adjudication.

You can find more information on how to make a complaint to the FOS on its website.

In terms of whether or not to transfer, this equation will depend on the performance of your investments after charges with any new provider, taking into account the MVR, versus the performance of your investments at your current provider, where the MVR doesn't apply. This will always be uncertain, but it's worth speaking to a regulated financial adviser to fully assess your policy and the options available.

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.

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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.

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