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Why the US economy might not be in as great shape as you think

Investors might be getting carried away with the latest growth figures

On 26 April US GDP figures apparently showed an economy in much ruder health than anyone had imagined.

The headline annualised growth figure of 3.2% was significantly ahead of the 2.3% forecast by economists and the best first quarter performance since 2015. The positive surprise helped drive US equities to new record highs; job done, move along, nothing else to see here, right?

Well, not quite. This was definitely an example where there is a strong case for looking beyond the headlines to examine what lay behind the growth.

For the most part the answer is highways investment, a sharp rise in inventories and a rise in net exports. All three of these factors look temporary.

And some observers have pointed out that the rise in inventories in the first quarter could actually be a significant headwind in the second quarter if the build-up in stockpiled goods leads to reduced demand in the manufacturing sector.

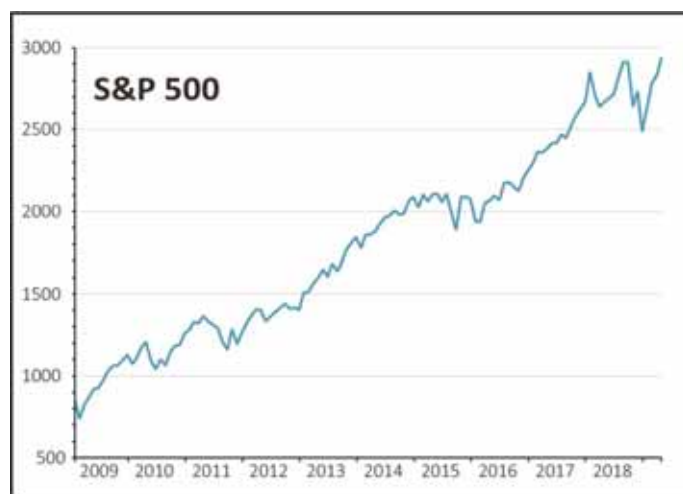
The US remains a consumer-driven economy. Personal consumption accounted for nearly 70% of GDP in 2018.

Here the news was much less positive. Consumer spending was up just 1.2% – perhaps unsurprising given the impact of the shutdown in Washington.

There have been signs recently that spending is beginning to pick up, notably in robust March retail sales and personal spending figures, however business investment remains weak and the housing market contracted for the fourth quarter in a row in the first three months of 2019.

THE DEVIL IS IN THE DETAIL

Rupert Thompson, head of research at wealth manager Kingswood, says: 'The equity rally has been given added fuel in recent weeks by signs



that global growth is starting to bottom out.

'And on first sight, US Q1 GDP numbers were very reassuring on this front with growth picking up. The details, however, were distinctly less impressive with underlying domestic demand growing only 1.3%, the slowest rate since 2015.'

Like the US, China's economy also did better than expected in the first quarter with growth of 6.4%. But in this case the concerted stimulus efforts pursued by the Chinese authorities – areas like infrastructure spending, tax cuts and the central bank boosting the money supply – were seen as playing a big part. And even then, there are serious question marks about the credibility of the numbers themselves.

That's not to say all is doom and gloom, clearly it is better to see key economic data come in ahead of forecasts, but it is important investors do not become complacent and assume global growth concerns have evaporated overnight.



By Tom Sieber Deputy Editor



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Consumer goods firms taking their pricing power back

Firms are raising prices and volumes for the first time in years

A funny thing happened in the world of consumer goods last quarter: companies were able to raise prices without buyers deserting en masse.

For the last few years, the global fast-moving consumer goods (FMCG) companies have struggled to entice consumers to pay up for flagship brands due to the explosion in competition from own-label products which most consumers seem to find do the job just as well.

In an environment of low growth and low to no wage growth, who pays up for Kellogg's Corn Flakes when **Tesco's (TSCO)** own-brand flakes are half the price? Who uses **Reckitt Benckiser's (RB.)** Finish dishwasher tablets when Aldi's Magnum tablets are half the price?

That has been the story for the last couple of years, but in the first quarter of this year the big brands seem to have fought back. They have raised prices while at the same time increasing volumes, which is almost unheard of.

Kellogg and Reckitt have yet to report but Swiss coffee-to-confectionary giant Nestle delivered like-for-like sales growth of 2.2% in the first quarter with 1.2% of that growth coming from pricing. Similarly, US chocolate- and snack-maker Mondelez grew organic sales by 3.7% in the first quarter with 2% coming from pricing.

Anglo-Dutch consumer-goods colossus **Unilever (ULVR)** revealed first quarter organic sales growth of 3.1% with 1.9% due to pricing.

Even Procter & Gamble, the US maker of Gillette razors and household cleaners which has struggled for years with tepid growth, showed its strongest top line growth for eight years last quarter as organic sales rose 5% thanks to a 2% increase in prices.

It's extremely hard to get the balance right and not every big consumer firm is there yet: Danone and Kimberly-Clark both raised prices and saw volumes fall.

However when companies can find that sweet spot of higher prices *and* higher volumes it results in a big boost to operating margins which is great news for investors.

Q1 EARNINGS SEASON – HALF-TIME REPORT

In the US there have been some positive surprises in terms of earnings as the first quarter earnings season reaches the halfway stage – notably from Twitter and JP Morgan – as well as sizeable disappointments from Alphabet (Google's parent) and scotch tape maker 3M.

In Europe data from investment bank Morgan Stanley suggests that as at 29 April, 50% of companies had beat earnings expectations and 22% missed – which if maintained would be the best showing since the first quarter of 2017.

However, in both Europe and the US, the story seems to be one of companies outdoing very gloomy expectations rather than kicking into gear, with Morgan Stanley suggesting European earnings are actually tracking down 5% year-on-year.



Procter & Gamble sales rose 5% last quarter

What next for Sainsbury's after failed Asda merger blow?

Some relief as profit beats forecasts, but beleaguered supermarket still faces uphill battle to compete

Shares in supermarkets operator **Sainsbury's (SBRY)** rallied off a low base on better than expected full year results (1 May), but this could prove a false dawn for the embattled grocer.

Chief executive officer (CEO) Mike Coupe is under immense pressure to show his charge can succeed as a standalone business and having squandered an eye-watering £46m in fees on a failed merger attempt with Asda.

POSITIVE SURPRISE

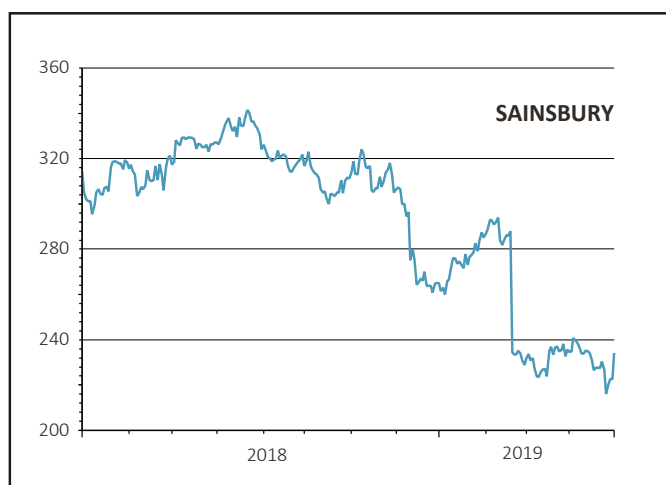
Sentiment towards Sainsbury's is poor, with the Competition & Markets Authority's prohibition of its bold merger with Asda representing a huge body blow to Coupe and the entire Sainsbury's investment case at a time when established rivals are reinvigorated and German disruptors Aldi and Lidl remain rampant.

Following on from Kantar grocery share data (30 Apr) showing a 1.2% sales decline for the 12 weeks to 21 April, the retailer's results for the year to 9 March were not as bad as feared, with underlying pre-tax profit and the dividend both up 7.8% to £635m and 11p respectively and net debt ahead of target.

However, profit was boosted by synergies from 2016's Argos acquisition as well as a reduced interest bill. Furthermore, reported pre-tax profit fell from £409m to £239m after pension scheme costs and the aforementioned £46m of Asda-related costs.

A ROTTEN CORE?

Worryingly, Sainsbury's core supermarkets underperformed the UK grocery market for much of the financial year and like-for-like grocery sales were down a disappointing 0.6% in the fourth quarter to 9 March.



Given that backcloth, Coupe needs to devise a 'Plan B' in light of the Asda debacle. It appears he is being given time for a strategy refresh. The market will have to wait until an investor day on 25 September for more details.

What we do know is Sainsbury's will be increasing and accelerating investment in a core business that must surely have been neglected while Coupe & Co were distracted by Asda. Coupe is also making a new commitment to pare net debt 'by at least £600m over the next three years'.

UNCERTAIN OUTLOOK

In terms of the outlook, Sainsbury's laments retail markets which are 'highly competitive and very promotional', with the discounters and Co-op gaining share from the rest of the market, while describing the consumer outlook as 'uncertain'.

Shore Capital seems unconvinced, seeing 'no cost-free or quick turnaround' for the supermarkets or Sainsbury's Bank and believing the outlook is 'challenged'. The broker also worries about the trajectory of earnings per share and the supermarket's dividend paying capabilities.

Sirius Minerals has a plan to solve its financing requirements

The FTSE 250 miner has unveiled the structure of a \$3.8bn financing package

It looks like short-term pain before long-term gain for shareholders in **Sirius Minerals (SXX)** after it launched a \$3.8bn fundraising to help build its North Yorkshire-based Woodsmith potash project.

The shares fell 15% to 18.6p on news that it would issue \$400m worth of new stock below the preceding day's market closing price. The following day it confirmed the new shares would be issued at 15p and that it had raised a higher amount at \$425m. It also raised a further \$400 from the sale of convertible bonds.

It is seeking \$500m from senior debt and JPMorgan said it would provide a \$2.5bn revolving credit facility.

While shareholders will be unhappy that project costs went up last year and there will now be additional share dilution, Shore Capital analyst Yuen Low believes there is light at the end of the tunnel.



'The next few weeks represent the crucial juncture for the company,' says Low. 'Successfully securing the Stage 2 financing is effectively the key to unlocking Sirius's vast potential, and we expect [it] should catalyse a major re-rating of the shares.'

The project has drawn enthusiasm from investors because of the huge potential of polyhalite, a form of potash used in fertiliser products which Sirius intends to extract from the mine. Production from the mine is expected to begin in 2021.

Why there is juice in the Photo-Me growth story

Sempa acquisition takes faltering firm in fresh direction

BEATEN DOWN photobooths-to-laundry machines operator **Photo-Me International's (PHTM)** growth story has been juiced up following its entry into a new and large market.

The acquisition (25 Apr) of 96% of Sempa, a France-based maker of commercialised fresh fruit vending equipment, takes it into the vast \$154bn fresh fruit and vegetable juice market, one underpinned by consumers' increasing focus on health and wellbeing.

Challenging conditions in the UK market have weighed on the share price of Photo-Me, whose latest profit warning was blamed on Brexit-driven consumer uncertainty. Entry into the large juice vending machine market will help diversify the group's vending operations.

Sempa made €3.7m of pre-tax profit on €9.4m sales in 2018 and the bulk of its revenue is based on recurring annual lease finance contracts. Its net cash position of more than €9m also means the net

cash consideration paid by Photo-Me was €11.6m.

Sempa provides a large global market opportunity for Photo-Me, whose management plans to replicate Sempa's success in France by rolling its equipment out across Photo-Me's European network.

Following the earnings enhancing deal, FinnCap has upgraded its 2020 earnings per share estimate by 6% to 10p, ahead of 10.4p in 2021.

The week's big news: banks, BP and more

We look at the share price movers and key announcements

The report card for the banks' first quarter reporting season looks a mixed one at best.

On 25 April numbers from **Barclays (BARC)** came in short of expectations thanks to a weak showing from its investment banking division, with income down 11% and profit falling 29% to £846m.

This is expected to add grist to the mill for activist investor Edward Bramson who wants the company to downsize this part of the business.



Shareholders in **Royal Bank of Scotland (RBS)** faced the dual shock of the departure of chief executive Ross McEwan and a disappointing update for the first three months of the year (26 Apr).

The latter saw adjusted profit miss expectations amid a material quarter-on-quarter decline in its net interest margin – a key measure of a bank's profitability. At 242p the company has surrendered a chunk of its year-to-date gains in response.

Emerging markets focused peer **Standard Chartered (STAN)** bucked this negative trend on 30 April. While it has a recent track record dogged by scandals and misconduct, its own first quarter statement showed signs it could be rehabilitated as profit beat consensus forecasts and the company announced a \$1bn share buyback – its first in two decades. The shares are up nearly 20% since the start of April at 705.7p.

The first quarter of 2019 again saw **BP (BP)** beat expectations (30 Apr), repeating the trick it managed for every quarter of 2018. Profit actually fell on a quarterly and annual basis as the oil market started the year in a depressed state before recovering.

Advertising giant **WPP's (WPP)** results for the first three months of the year reflected the loss of major US clients with sales down 2.8% but at least they were no worse than the market expected and year-to-date the shares are now 14% higher at 969p.

FTSE 350 MOVERS OVER THE PAST WEEK – BEST PERFORMERS

STOCK	SHARE PRICE RISE/FALL	REASON
AJ Bell	14.2%	Says half-year results to beat market expectations
Computacenter	13.2%	Bullish trading update
Stagecoach	12.5%	Broker note considers potential for Souter family to buy Stagecoach

SMALL CAP MOVERS OVER THE PAST WEEK – WORST PERFORMERS

STOCK	SHARE PRICE RISE/FALL	REASON
Ferrexpo	-24.0%	Auditor resigns in wake of charity probe
Funding Circle	-14.6%	Lowers expected returns for retail investors, lifts default estimates
Sirius Minerals	-13.5%	Unveils dilutive fundraising plans

DISCLAIMER: AJ Bell, reference in this table, is the owner of Shares magazine

Source: Shares, Sharepad

Why you should buy ultra-reliable Computacenter

Track record suggests FTSE 250 IT company can continue to feed off digital transition

In a modern world of technology dominated by US giants (Amazon, Microsoft, Apple) many investors might reasonably ask, **Computacenter (CCC) who?**


Yet this is a pan-European IT enterprise operator whose 14,000-odd staff annually ship more than 25m products to 4.2m end users, and provide valuable advice support and services before and after in 30 different languages. It has been part of the FTSE 250 index for most of the last 10 years.

In an era of unprecedented technological change there are thousands of organisations needing help with adaption and adoption, be it to stay competitive, engage better with customers, improve access to information and services, bolster efficiency or simply trim costs.

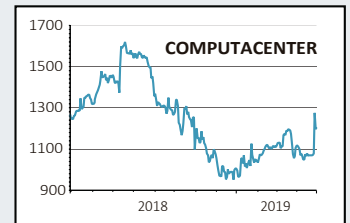
WHAT THE COMPANY DOES

Computacenter operates in three parts. On the infrastructure side it supplies customers with the PC desktops, tablets, smartphones and other devices on pretty skinny profit margins.

Professional services is where Computacenter experts consult and advise clients on a multitude of best-in-class software and applications, and resell what's right for them. We're talking about proper blue-chip vendors, such as Microsoft, Oracle, Adobe,

COMPUTACENTER 
(CCC) 968p
Stop loss: 344p

Market cap: **£1.38bn**



Cisco and Symantec.

Managed services go further still, providing an entire outsourced IT solution, which means clients don't need to run their own large and expensive in-house IT teams. Computacenter effectively runs the IT show remotely on the client's behalf, with 24/7 support, advice and problem solving available and local software engineers on-call when needed

It is a model that has worked for years thanks to steady growth, consistent profits and superb cash flows that feed into reliable dividends. Computacenter has an unbroken track record extending beyond 10 years for annual earnings increases.

BIG RETURNS FOR SHAREHOLDERS

Computacenter also hates to sit on idle cash. Since 2006 the company has handed back something like £350m to shareholders. This has made Computacenter shares an excellent investment over the years, producing an average 52.5% return per year over

the past decade, according to calculations by Stifel analysts.

We believe this sort of performance will continue into the medium, even longer-term, and recent trading seems to back that view up.

The company recently said that its first three months to 31 March was 'one of our best quarters ever' and beyond management's original expectations. It was also highly encouraging that even in the face of challenges such as Brexit, questions over global growth and other concerns Computacenter has seen little or no impact on technology investment demand.

Current consensus for earnings per share of 77.3p imply a price to earnings multiple of 15.6 for 2019, falling to below 15 in 2020. This year's anticipated 31.8p per share dividend implies a 2.6% income yield, plus there's every chance of fresh cash returns on a longer-term view.



By **Steven Frazer**
News Editor

Aviva's shares are too cheap to ignore at a 7.3% yield

Snap up the shares before market sentiment starts to improve towards the life insurer

We believe **Aviva (AV.)** looks very interesting at the current price as its shares are cheap and a new CEO could reshape the business.

Anyone investing in the shares must understand that change could take time, however the potential rewards look very good.

'Aviva is undergoing a revolution in its balance sheet strength that will leave the group with more equity, less debt and more prudent asset and liability valuations than consensus expects, thus ensuring long-term dividend sustainability,' says Jefferies analyst Philip Kett.

Aviva is the UK's largest composite insurance company with around half of sales coming from its home market and half from Canada, France, Holland, Ireland and Poland.

Most of its sales come from life insurance where customers and premiums tend to be 'stickier' than in household or car insurance although it has a top three UK share in non-life markets.

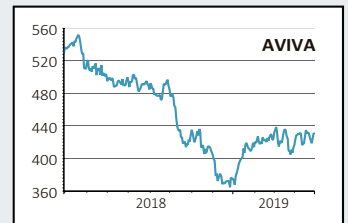
Aviva looks undervalued at 8.2 times this year's earnings and less than 8 times next year's. In comparison, **Prudential (PRU)** is valued at 11-times and 10-times respectively while Swiss Life is valued at 14-times and 13-times.

In October chief executive officer Mark Wilson stepped

AVIVA  **BUY**

(AV.) 430p
Stop loss: 344p

Market value: **£16.6bn**



down, supposedly over a disagreement with the board over strategy. He has since been replaced by Maurice Tulloch who says he will simplify the business.

MARKET CONCERNS

The current concerns hanging over the shares are Aviva's high debt levels compared with its peers and its perceived lack of earnings growth. The company said in April that sustaining momentum for operating earnings this year would be difficult.

Operating profit grew just 2% in 2018 and the average growth rate for the next three years is estimated to be just 3% to 4%, but improvements to its balance sheet combined with the lowly valuation make Aviva stand out.

'Aviva continues to invest in improving customer service by reducing the complexity at both the point of sale and claim,'

comments Kett. 'The aim is to increase customer retention and shift from the industry norm of strained / adversarial customer relations. Like the market, we struggle to value this but acknowledge that if it be achieved, this would be a paradigm shift in the insurance business model.'

Its dividend policy was recently reset so that payments progress in line with growth in earnings, which disappointed the market but gives Aviva the flexibility to reduce its debt or invest more in the business.

Despite these change the shares are still very attractive from an income perspective. It is forecast to pay 31.5p in dividends for 2019, implying a 7.3% yield.



By **Ian Conway**
Senior Reporter

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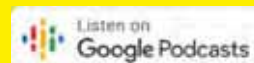


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SHARES 



MARLOWE

(MRL:AIM) 432p

Gain to date: 1.4%**Original entry point:****Buy at 426p, 28 June 2018**

SHARES IN FIRE and water safety expert **Marlowe (MRL:AIM)** have strengthened in recent weeks for three reasons.

First, the service group appointed investment bank Berenberg as joint corporate broker alongside Cenkos, helping to raise its profile among institutional investors.

Berenberg believes Marlowe's shares could be worth 620p in the next 12 months based on a discounted cash flow model and expectations that it will keep making acquisitions at decent prices.

Marlowe also pleased the market on 29 April by saying full year adjusted earnings before interest, tax, depreciation and amortisation (EBITDA) will be ahead of market forecasts after enjoying 'significant growth' in revenue and profit.

Coinciding with this news was an event for investors to learn more about the business including information on the recently-acquired William Martin operation, which is Marlowe's first acquisition in the health and safety audit and inspection market.

William Martin is growing faster than the rest of the group, it has a higher proportion of recurring revenues and it generates higher operating margins.

**SHARES SAYS:** ↗

We're pleased to see our trade on Marlowe is back in positive territory after a weak period for the share price. The investment case remains highly attractive so keep buying.

FDM

(FDM) 973p

Gain to date: 5.3%**Original entry point:****Buy at 924p, 4 April 2019**

JUST A FEW weeks on since our original **FDM (FDM)** investment idea pitch and there are already promising signs for the months ahead.

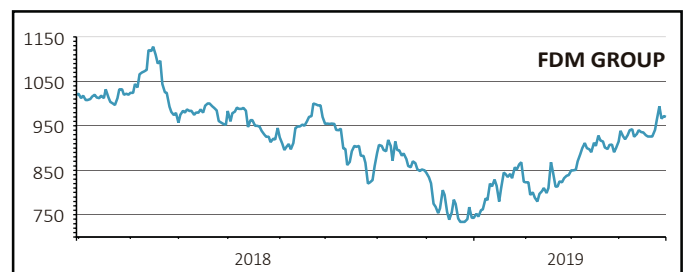
As we explained in detail earlier this month, the IT projects business is pulling back from employing expensive margin-sapping day contractors to concentrate on its Mountie army profit engine.

Mounties is a term the company uses to describe members of its team of IT consultants which are trained and deployed in clients' businesses.

The company told investors at its AGM that Mountie revenues were up 16% in the first quarter to 31 March, outstripping the 14% overall revenue rise.

It has also managed to install an extra 500-plus Mounties into client sites versus the first three months of 2018, working on all sorts of digital development, IT testing, project management and more. Demand clearly remains strong for the right IT skills to help organisations adapt to the digital world.

There are precious few figures to go on beyond those above but the wider rhetoric remains cautiously optimistic for the rest of 2019, the company saying it is confident of delivering 'long-term, sustainable growth.'

**SHARES SAYS:** ↗

An encouraging start from a high-quality business.

AUTO TRADER

(AUTO) 574.8p

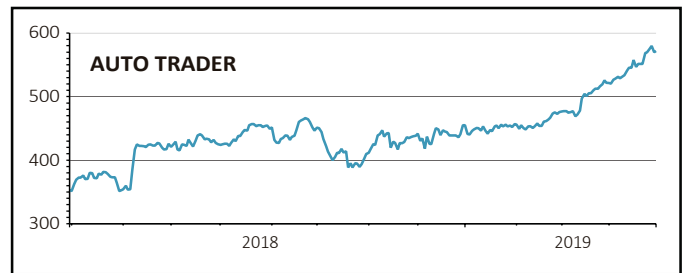
Gain to date: 52.2%

Original entry point: 377.7p, 17 May 2018

OUR VIEW NEARLY a year ago that the market had called it wrong on **Auto Trader (AUTO)** has been vindicated. The shares have increased by more than 50% in value and the stock even motored into the FTSE 100 at the end of 2018.

Despite fears over the UK car market and a competitive threat from online rivals, the car listings website has demonstrated its ability to continue growing earnings by squeezing more out of the retailers which buy its subscription products.

Half year results announced in November showed revenue up 7% to £176.8m with average revenue per retailer forecourt per month increasing £152 to £1,826 and earnings per share up 12%.



However, on 29 April the company announced the man who had led the company through its successful IPO and to a strong start as a public company, Trevor Mather, will step down at the end of the current financial year in March 2020.

He will be a hard act to follow for his replacement Nathan Coe, currently the finance chief at the company. A price-to-earnings ratio of more than 23 times March 2020 forecast earnings leaves limited margin for error.

SHARES SAYS: ⬇️

While we like the business, the valuation now looks more stretched and a change at the top represents a good opportunity to take profit.



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What the extinction rebellion could mean for investing

Sustainability is back in the spotlight after recent events

Anyone who has picked up a newspaper or tuned into the news in the last fortnight will have noticed that climate change has managed to topple Brexit as the hot topic of discussion in the UK.

Just a week ago, a group of environmental protesters glued themselves across the entrance to the London Stock Exchange while others staged a 'die-in' at the Natural History Museum and thousands more blocked Waterloo Bridge and Oxford Circus to draw attention to climate change.

In a poignant moment, 16-year old Swedish climate activist Greta Thunberg told an audience of MPs that her future and that of children everywhere had been sold by politicians 'so that a small number of people can make unimaginable amounts of money'.

Public demonstrations aimed at raising awareness of climate issues have been staged as far afield as Australia and India.

INVESTING FOR CHANGE

Investment managers, under pressure themselves to integrate environmental, social and governance (ESG) policies into their processes, are putting increasing pressure on companies to act more sustainably and to



publicise their strategies.

As climate change makes the weather less predictable, countries are under pressure to build resilience into their agricultural strategies using new farming methods and improved water infrastructure.

Funds such as **Impax Environmental Markets (IEM)** are exposed to the growing market for environmental services through stakes in quoted companies, particularly those related to alternative energy, energy efficiency, water treatment and pollution control.

Investment trusts such as **John Laing Environmental Assets (JLEN)** own a range of real assets instead, from wind and solar farms to water treatment and biomass plants. These can benefit from predictable, long-term, partly or wholly inflation-linked cash flows.

Asset manager **Gresham House (GHE)** is the UK's largest commercial forestry manager as

well as owning the UK's largest energy storage business, the separately-listed **Energy Storage Fund (GRID)**.

'SIXTH MASS EXTINCTION'

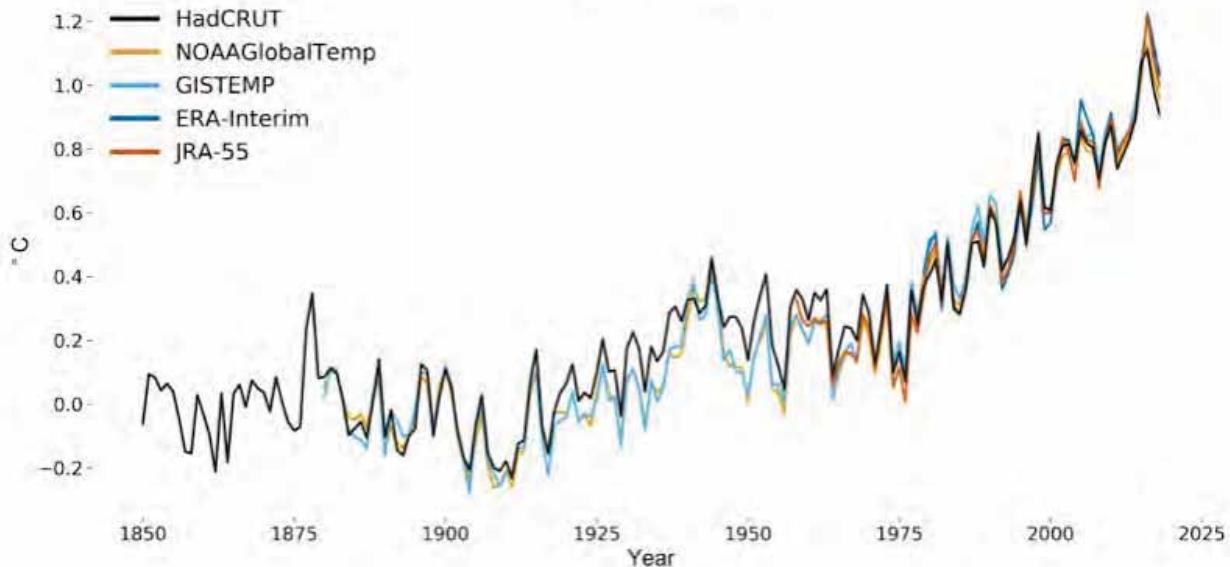
Why are the stakes seen as so high? Environmental campaigners claim that, due to climate change, the planet could be facing a Mass Extinction Event for only the sixth time in the last 540m years. A mass extinction is characterised as the loss of three quarters of existing species in a geologically short period of time.

If climate change isn't countered, campaigners claim, the effects on nature and society could spiral out of control. Rising sea levels, desertification, wildfires, extreme weather, water shortages, crop failure, disease and a rise in conflicts are all potential outcomes.

Due to human activity, in particular the burning of fossil fuels, the Earth's average surface temperature has risen by around

Met Office

Global mean temperature difference from 1850-1900 (°C)



© Crown Copyright. Source: Met Office

1.1 degrees Celsius since the late 19th century. Globally the last four years have been the hottest on record and the 20 warmest years in history have occurred in the last 22 years.

Globally, species are going extinct 1,000 times faster than the background extinction rates typical of Earth's past due to climate change, over-exploitation of natural resources and the introduction of invasive alien species.

The average rate of vertebrate species loss over the last century is up to 100 times higher than the background rate. In other words without climate change it would have taken up to 10,000 years for the same number of species to disappear.

CLIMATE RELATED DISASTERS RISING

The number of extreme climate-related disasters, including extreme heat, droughts, floods and storms, has doubled since the early 1990s, with an average

of 213 events occurring every year from 1990 to 2016.

The American West is experiencing its worst mega-drought in more than 500 years according to academics at Columbia University: only three previous mega-droughts – in the late 800s, mid-1100s and late 1500s – were worse than the current period.

As well as costing the insurance industry billions in catastrophe claims these events harm agricultural productivity, contributing to shortfalls in food availability causing food price hikes and income losses that reduce access to food.

DEPLETING EARTH'S RESOURCES

Research organisation Global Footprint Network estimates that demand for natural resources on top of carbon emissions means that last year we reached Earth Overshoot Day – the date when our annual demand on nature exceeds what the planet's

ecosystems can regenerate – on 1 August.

Overshoot Day has been arriving ever earlier: in 1970 it was 29 December, by the 1980s it was November and by 1995 it was in September.

As the deficit grows, ecosystems are lost meaning less clean water, soil and air, which has devastating knock-on economic and social effects.

People across 51 countries and territories are facing crisis levels of acute food insecurity or worse. The number of people affected just between 2015 and 2017 has risen by 50% to 124m.

The risk of extreme weather hitting several major food producing regions of the world simultaneously could triple by 2040 making it a one in 30 year event rather than one in 100 years.



By Ian Conway
Senior Reporter

CAN THE FTSE 100 BREAK FREE?



FTSE 100: bottom of the global league table

Index	YTD return (%)
NASDAQ 100	23.5
CAC 40 (Paris)	17.4
S&P 500	16.7
DAX Xetra (Germany)	16.3
Russian Trading System Index	16.2
Hang Seng (Hong Kong)	14.5
Dow Jones Industrial Average	13.4
Nikkei 225	11.2
FTSE 100	10.2

Source: SharePad, 26 April 2019

The 10.2% year-to-date rise in the FTSE 100 is a great result but the UK stock market's flagship index is still being comfortably outpaced by its international counterparts.

And seen on a longer-term view the FTSE has definitely underperformed relative to other global benchmarks.

In this article we explain why this has happened, which super sectors have contributed to the relative underperformance of the FTSE and what needs to happen in these sectors for this trend to reverse.

We will also look at some of the best performing sectors and consider the strong influence on the index's performance from **Royal Dutch Shell (RDSB)**, which when its 'A' and 'B' share classes are both factored in accounts for more than 10% of the index on its own.

WHAT'S ACTING AS A DRAG ON THE FTSE?

It would be easy to conclude that Brexit is behind the FTSE's woes. This is not the case.

While markets hate uncertainty, the bulk of

the FTSE's earnings come from overseas. This means weakness in sterling, the main barometer of fears over a chaotic Brexit, has actually been a strong catalyst as it boosts the relative value of these foreign earnings.

More relevant are concerns over global growth, a slowdown in China and growing tensions between the US and seemingly all of its major trading partners – to which the FTSE is disproportionately exposed through many different industries.

You need to consider the *weighting* of the different stocks and sectors in the index. For those who are unfamiliar with this term, it refers to how much of the total market value of the FTSE said industry or share represents.

We have already indicated that Shell makes up in excess of 10% of the FTSE. And, for example, the Oil & Gas super sector in total has a weighting of nearly 17%. We have calculated a weighting for relevant sectors in the FTSE 100 encompassing those stocks from the sector which have underperformed the wider index to give a clearer picture of what has been dragging on its performance.



BANKS

Weighting in the FTSE 100*: 9.5%

Year-to-date performance**: 6.1%

*Encompassing those stocks from the super sector which have underperformed the FTSE 100 **Based on the average return from constituents of the sector which have underperformed the FTSE 100 year-to-date

Source: Thomson Reuters, Sharepad, 26 April 2019

THE BANKING sector makes up a good chunk of the FTSE 100 with **HSBC (HSBA)**, the second largest stock in the index, accounting more than half of the weighting.

HSBC has gained just 3.2% and because of its large weighting it has distorted the sector return.

We discussed in January three reasons why we believe investors shouldn't own HSBC. Despite its seemingly attractive dividend yield, we think the stock is higher-risk than it appears because:

- Revenues and earnings are still dominated by the bank's exposure to China;
- The UK mortgage market is soaking up capital with miniscule returns;
- The investment banking unit is doing the same but with the added downside risk that trading global markets entails.

Barclays (BARC), **Lloyds (LLOY)** and **Royal Bank of Scotland (RBS)** are much more focused on the UK retail and commercial banking market and in spite of fears over a Brexit-related slump the domestic economy seems to be holding up.

However, like HSBC, Barclays has an investment banking unit which absorbs a great deal of capital and over the long term has added very little value.

HEALTH CARE

Weighting in the FTSE 100*: 9.1%

Year-to-date performance**: 1.4%

*Encompassing those stocks from the super sector which have underperformed the FTSE 100 **Based on the average return from constituents of the sector which have underperformed the FTSE 100 year-to-date

Source: Thomson Reuters, Sharepad, 26 April 2019

HOLDING BACK the gains from the Health Care Super sector have been volatile share price rides from FTSE 100 listed private hospital operator **NMC Health (NMC)** and drug manufacturer **Hikma Pharmaceuticals (HIK)**.

Drugs goliaths **GlaxoSmithKline (GSK)** and **AstraZeneca (AZN)** have also failed to keep pace with the wider FTSE 100 rally. 2018 was a better than expected year for GlaxoSmithKline, thanks to a strong performance in vaccines and no generic competition for its leading respiratory treatment *Advair* entering the US market.

Alas, after several delays, a generic entrant was accepted by the FDA at the end of 2018 and the market is pricing in significant earnings declines due to pricing and volume pressure in 2019. Fellow pharma giant AstraZeneca is also fighting off generic competition for some big products, although continued healthy sales of newer drugs - supported by a step-up in R&D spending, could help alleviate market fears.

More recently, AstraZeneca's shares were knocked by news of a \$6.9bn deal with Japan's Daiichi Sankyo to develop and sell the latter's breast and gastric cancer drug. This didn't go down too well with a market seemingly more focused on the deal mechanics than the deal rationale.

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PERSONAL & HOUSEHOLD GOODS

Weighting in the FTSE 100*: 3.5%

Year-to-date performance**: 4.4%

*Encompassing those stocks from the super sector which have underperformed the FTSE 100 **Based on the average return from constituents of the sector which have underperformed the FTSE 100 year-to-date

Source: Thomson Reuters, Sharepad, 26 April 2019

THE PERSONAL & Household Goods super sector includes FTSE 100 housebuilders **Berkeley (BKG)**, **Persimmon (PSN)**, **Barratt Developments (BDEV)** and **Taylor Wimpey (TW.)**, not to mention packaged consumer goods colossus **Unilever (ULVR)**.

Performance in parts of the sector relative to the FTSE 100 has disappointed year-to-date with gains constrained by uncertainty surrounding tobacco stocks and company-specific concerns at

Reckitt Benckiser (RB.). Shares in the consumer health products maker behind *Nurofen*, *Gaviscon* and *Strepsils* have been volatile with the market concerned over recent soft sales growth trends.

CEO Rakesh Kapoor, architect of the transformational acquisition of US baby formula maker Mead Johnson, is retiring and more recently, Reckitt reversed on concerns it could be caught up in a US probe involving **Indivior (INDV)**, which it demerged in 2014, which has been accused of opioid treatment-related fraud. Resolution of this uncertainty is a potential upside catalyst but Reckitt has already set aside \$400m to cover liabilities and the ultimate fine may end up being substantially higher.

Reckitt's infant formula business derives a portion of its sales from US government contracts and thus could also be at risk. Also weighing on the Super-Sector's relative showing is **Imperial Brands (IMB)**. Investors remain worried about the ability of next generation products to help offset falling demand for traditional tobacco and there's also major US regulation uncertainty to fret about.

Sentiment towards Imperial was negatively impacted by the recent announcement of a bill in the US to raise the national minimum age to purchase tobacco products (including e-cigarettes) from 18 to 21.



TELECOMMUNICATIONS

Weighting in the FTSE 100*: 3%

Year-to-date performance**: -5.3%

*Encompassing those stocks from the super sector which have underperformed the FTSE 100

**Based on the average return from constituents of the sector which have underperformed the FTSE 100 year-to-date

Source: Thomson Reuters, Sharepad, 26 April 2019

UTILITIES

Weighting in the FTSE 100*: 2.4%

Year-to-date performance**: - 2.1%

*Encompassing those stocks from the super sector which have underperformed the FTSE 100 **Based on the average return from constituents of the sector which have underperformed the FTSE 100 year-to-date

Source: Thomson Reuters, Sharepad, 26 April 2019

STOCK MARKET classification has typically split the wider utility space into component electricity and gas, water and telecoms sectors. But while running a power station, supplying sewage services, keeping the lights on or providing 24/7 internet access on the go may look entirely different these industries are all faced with very similar core problems; an increasingly hawkish regulatory environment, intense competition and the need to invest millions of pounds into their respective infrastructure and networks.

And that cuts to the chase of what links British Gas-owner **Centrica (CNA)** with mobile phones giant **Vodafone (VOD)**, **United Utilities (UU.)**, the UK's largest water services supplier, and **BT (BT.A)** – dividends, and their sustainability at current levels.

Utility companies of most stripes have long held a prominent place in investor portfolios thanks to their implied defensive characteristics, reliable

revenues and inflation-proofed income. But this is no longer the case.

Take Vodafone, for example. Its shares have declined nearly 10% so far in 2019 as questions linger over its payout. This year's forecast €0.15 per share dividend implies an income yield of about 9%, but you know what they say about things looking too good to be true.

Worries persist about sky-high levels of debt, where net borrowings run to about €32bn, or roughly 75% of the company's £37bn market value. The pinch is exacerbated by significant competitive threats (it was recently voted the worst of the big four UK mobile networks by consumers) and the substantial spending needed to deliver next generation 5G services.

Arguably, Centrica dividend is most at risk among UK utilities. The energy firm has signalled that energy price caps will constrain cash flow this year and has explicitly linked dividends to meeting cash generation and debt targets.

The consensus forecast which underpins Centrica's forward yield of 9.2% in 2019 is 9.7p which implies a 19% cut from 2018's 12p figure, but there are some analysts who think a cut considerably larger is possible. RBC is anticipating a 2019 dividend of 8p. Centrica's credit rating was recently downgraded (pushing up its cost of borrowings) while its British Gas consumer energy arm continues to haemorrhage customers, neither of which is helpful.

Similar questions over dividend sustainability are still to be answered at energy supplier **SSE (SSE)** and BT, while the water sector has not been immune from hard line demands by its own watchdog, Ofwat.



TRAVEL & LEISURE

Weighting in the FTSE 100*: 3.7%

Year-to-date performance**: -1.7%

*Encompassing those stocks from the super sector which have underperformed the FTSE 100 **Based on the average return from constituents of the sector which have underperformed the FTSE 100 year-to-date

Source: Thomson Reuters, Sharepad, 26 April 2019

THE FTSE 100 Travel & Leisure sector is extremely diverse, covering airlines to fast food delivery and hotels, and while the sector is up 4.9% year to date

the performance of individual stocks is equally diverse, from -26% to +26%.

Just Eat (JE.) has had a strong run since January helped by a return to profits last year and pressure from an activist investor to up its game.

The two biggest laggards, **International Consolidated Airlines (IAG)** and **TUI (TUI)**, have been negatively affected by the continuing price war in European air travel with TUI also incurring heavy losses through grounding its fleet of Boeing 737 Max airliners.

For income investors it's worth noting that the sector is rich in terms of shareholder returns with most companies either paying special dividends or buying back their own shares this year which might help the sector return to favour.

Whitbread (WTB) is returning at least £2.5bn of the £3.9bn cash it received from the sale of Costa coffee to Coca-Cola, beginning with a £500m share buyback ahead of its full year results.

IAG announced is paying a special dividend of €700m or €0.35 per share on top of the ordinary dividend of €0.31 per share, while **Carnival (CCL)** operates a continual buy-back programme and bought in \$250m of shares last quarter.

WHY SHELL IS SO IMPORTANT TO THE FTSE 100

Weighting in the FTSE 100: 10.9%

Year-to-date performance: 5.3%

Source: Thomson Reuters, Sharepad, 26 April 2019

ANGLO-DUTCH oil major Royal Dutch Shell can have a big influence on the FTSE because it represents more than a tenth of the total value of the index.

The company developed as a combination between Shell in the UK and Netherlands firm N.V. Koninklijke Nederlandsche Petroleum Maatschappij.

This explains why it has an A and B share structure. The A shares face a 15% Dutch withholding tax on dividends but the B shares are exempt from this levy. The performance of the shares, while firmly in positive territory year-to-date, has lagged the FTSE 100.

This might come as a bit of a surprise given the strong recovery in oil prices and given that its closest peer on the UK market **BP (BP.)** is up around 13%.

The shares may have been held back by reports of potential criminal charges in the Netherlands relating to corrupt practices in Nigeria.

However, the longer oil prices remain above \$70 per barrel, the greater faith investors might have in the company's dividend which at a share price of £24.70 implies a dividend yield of nearly 6%.

A strong second half showing for Shell could have positive implications for the FTSE 100's performance in the remainder of the year.



WHICH PARTS OF THE FTSE 100 HAVE BEEN DOING WELL AND CAN THEY KEEP IT UP?

THE RETAILERS have had a strong start to 2019, with several of the sector's constituents among the top performers including **Tesco (TSCO)** whose turnaround under chief executive Dave Lewis has continued to gather momentum.

Whether this can continue is likely to depend on the jobs market, if the recent uptrend in 'real' – that is adjusted for inflation – wages can continue and if a chaotic Brexit ends up hurting consumer sentiment.

Mining behemoth **Rio Tinto (RIO)** and oil heavyweight **BP** have both contributed to the FTSE's gains. While Rio's strong performance also reflects a very resilient first quarter showing in the face of several operational challenges, their fortunes are likely to remain closely tied to

volatile commodity prices.

Individual heavyweight stocks which have contributed to the FTSE's rise include global insurance business **Prudential (PRU)** and **British American Tobacco (BATS)**. Prudential has enjoyed a recovery rally after a disappointing share price showing in 2018. Full year results which came in slightly ahead of expectations acted as a catalyst.

British American Tobacco has also enjoyed a rebound, having hit multi-year lows in early January on regulatory and competition concerns.

By Tom Sieber, Steven Frazer,
James Crux and Ian Conway



Why you should consider going against the herd with Henderson Eurotrust

Rigorously analytical money manager Jamie Ross has a focus on quality and return on capital

Investors looking for an opportunity to put money to work in currently unloved European markets should consider **Henderson EuroTrust (HNE)**. This investment trust aims to deliver superior total returns from a portfolio of high quality European (ex UK) investments.

Former deputy manager Jamie Ross took over as lead manager following the long-serving Tim Stevenson's retirement in February.

Although the investment process and style remain largely the same – the fund will continue to be comprised of good quality, reliable companies from 'developed Europe' which offer consistent returns – Ross has reduced the number of holdings, leaving the fund more concentrated on his high conviction ideas.

The trust trades at a 9.3% discount to net asset value that may appeal to bargain hunters.

The focus is more on growth and total returns than the dividend, but Henderson EuroTrust does provide a growing level of dividends and offers a decent 2.8% yield.

Admittedly, the portfolio and the benchmark FTSE World Europe ex UK index declined in value over the half year ended 31 January 2019 as volatility



FUND MANAGER, JAMIE ROSS

returned to global markets.

However, on a 10 year cumulative performance basis, Henderson EuroTrust has returned 230.2% versus 176.1% for the benchmark, albeit much of it under the predecessor to the current manager.

GROWTH, QUALITY & CONSISTENCY

Henderson EuroTrust has the tagline 'seeking growth, quality

and consistency'.

The aim is to achieve this by selecting companies with strong market positions and strong balance sheets, consistent growth and high quality management.

The trust invests in large and medium-sized companies which Ross perceives to be undervalued relative to their growth prospects, or on account of a significant change in management or structure. He informs *Shares* of an increasing focus on integrating ESG analysis into his investment theses too.

Ross seeks out 'what we would define as good quality businesses in Europe. We're not trying to reinvent the wheel or do things in a really complex way. We're not trying to take on high risk, high return opportunities. We want good businesses and we want to own them for a decent period of time.'

ROSS' ANALYTICAL RIGOUR

One of Henderson EuroTrust's competitive advantages in the sector is the analytical rigour of Ross, determined to meet with management teams as often as possible in order to further his understanding of industries and businesses.

'I am a real details guy on the companies,' he explains. 'So for



me, the job is all about knowing these businesses that we invest in better than anyone else. It is impossible to do the level of research that we want to do and run a 70 stock portfolio. You either run a long list of companies and don't know them particularly well or you run a short list of companies and know them very well, and that's how we want to do things.'

Ross (and a recently hired analyst) undertake their own financial modelling. As he explains: 'If you read our research, it is much more about "what is this company, what does it do, does it generate decent returns?'. The focus on return on capital is absolutely key to our process.

'It is the key metric – you have to be forming a strong opinion on where return on capital goes in the future. That is the whole basis for the work we do.'

Ross absolutely will not buy cheap companies just because they are cheap. 'Some of the businesses we own we would define them as cheap, but we do not own them because they are cheap. We own them because we feel there is an underappreciated return on capital story or there is a chance for return on capital to go from a low level to high level at

TOP TEN HOLDINGS (As at 16 April 2019)	
Company	Portfolio weight (%)
DSM	4.9%
Munich Re	4.8%
Roche	4.7%
Novo Nordisk	4.7%
Nestle	4.6%
Total	4%
SAP	3.7%
Equinor	3.4%
Deutsche Telekom	3.3%
Philips	3.3%

Source: Janus Henderson Investors

which point the equity valuation will re-rate.'

COMPOUNDERS, IMPROVERS & SPECIAL OPPS

In terms of the investment process, Ross splits the holdings into three broad classifications; 'compounders', 'improvers' and 'special opportunities'.

Compounders are high-quality businesses that have a high return on capital, pricing power, typically strong brands and 'a tendency to operate in industries where there are only one or two competitors. They have a tendency to be big companies with big moats around them, as Warren Buffett would say.'

A great example in the fund is Novo Nordisk, a Danish pharma

company focused on diabetes and obesity which operates in a defensive market where Ross believes returns will stay high for a number of years.

He describes improvers as 'businesses where return on capital is not particularly interesting, but where the return on capital profile will go up, but the market is not pricing them for that'. These include Koninklijke Philips, the Dutch health technology company with a big opportunity for improving margins and returns over time.

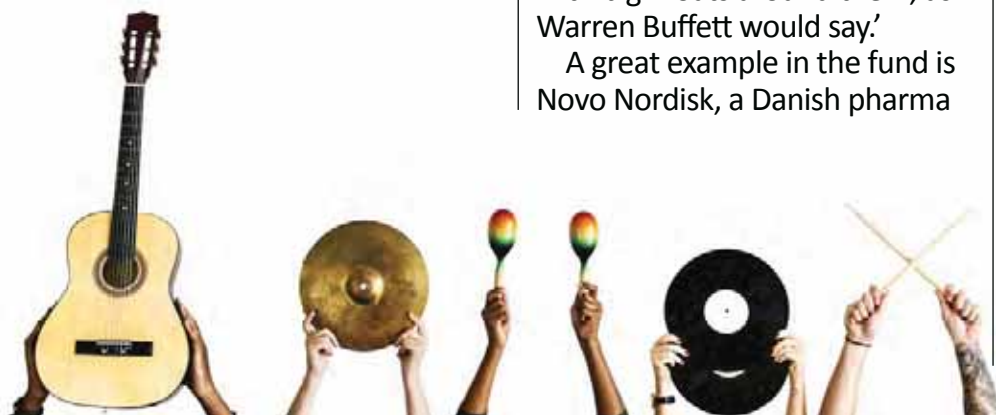
Special opportunities are investments based around a specific event or catalyst. A new Henderson EuroTrust holding that sits within this silo is Vivendi, the French media conglomerate controlled by billionaire Vincent Bollore that houses an 'extremely attractive' music content business in the form of Universal Music Group.

Ross, a fan of The Libertines, insists the music business is 'hugely exciting on a multi-year view. We're going to see a massive growth in music consumption over the next 20 years.'

He argues the market is failing to correctly price Universal Music Group or the incremental return on invested capital (ROIC) improvements of Vivendi. He has spotted a strong re-rating catalyst in the upcoming partial sale of Universal Music Group to a partner that should validate his thesis and materially increase Vivendi's intrinsic value to boot.



By James Crux
Funds and Investment
Trusts Editor



INCOME LETDOWN FROM ABERDEEN STANDARD EUROPEAN LOGISTICS

5.5% → 5.0%

THE INCOME YIELD target of **Aberdeen Standard European Logistics Income (ASLI)** has been trimmed just 15 months after its launch.

Initially pitched at 5.5% based on its 100p IPO price in December 2017, the investment trust has cut that target to 5% after talks with its largest shareholders, including the East Riding Pension fund.

Yield compression from a re-pricing of European property assets has been blamed, a factor that has seen the share price fall 17% in six months.

This is surprising given the ballooning demand for the sort of modern warehouse assets that the trust invests in given thriving online commerce that requires complex delivery logistics.

Aberdeen Standard European Logistics Income currently has a portfolio of 10 assets with 26 tenants spread across mainland Europe.

WHAT CHANGE AT THE TOP MEANS FOR RIT CAPITAL PARTNERS

LORD ROTHSCHILD IS stepping down as chairman and director of **RIT Capital Partners (RCP)** and will take up the role of president, maintaining his active involvement with the trust he founded.

This follows several years of succession planning at RIT, a trust focused on long-term capital growth twinned with capital protection.

Under Rothschild's stewardship, net assets have grown from £280m at listing in 1988 to around £3bn today. Reassuringly, Rothschild has reaffirmed

his family ties with RIT.

Holding sway with a 21.35% stake, the family will continue to be represented on the board by his daughter, Hannah Rothschild, appointed as a non-executive director in 2013 as part of the succession planning.

Numis Securities says: 'Ultimately, we regard today's announcement as a positive development for shareholders as it resolves any uncertainty over Lord Rothschild's future, and removes the threat that his family stake could be regarded as an overhang.'

RIT FINANCIAL SUMMARY AS AT 28 FEBRUARY 2019

PERFORMANCE	1 year	5 years	10 years
NAV per share total return	3.7%	49.0%	138.8%
Share price total return	6.4%	72.5%	187.2%
RPI plus 3.0% per annum	5.5%	29.5%	79.6%
MSCI All Country World Index (50% £)	2.3%	58.9%	246.9%

Source: RIT Capital Partners

SUPERMARKET INCOME REIT SNAPS UP TESCO STORE

IN THE SAME week that **British Land (BLND)** sold 12 **Sainsbury's (SBRY)** stores for £429m, specialist investor **Supermarket Income REIT (SUPR)** inked a £45m deal to buy a Tesco Extra supermarket in Mansfield.

While British Land's

decision was seen as a sign of the diminishing appeal of supermarkets as a property investment, its much smaller niche rival clearly sees value in the right kind of asset.

Investment bank Stifel comments: 'The large store has characteristics

exactly in line with the company's acquisition criteria to which we consider it has strictly adhered since the IPO: a long unexpired lease length of 20 years, upward-only and RPI-linked rent reviews, the next of which falls in March 2020.'



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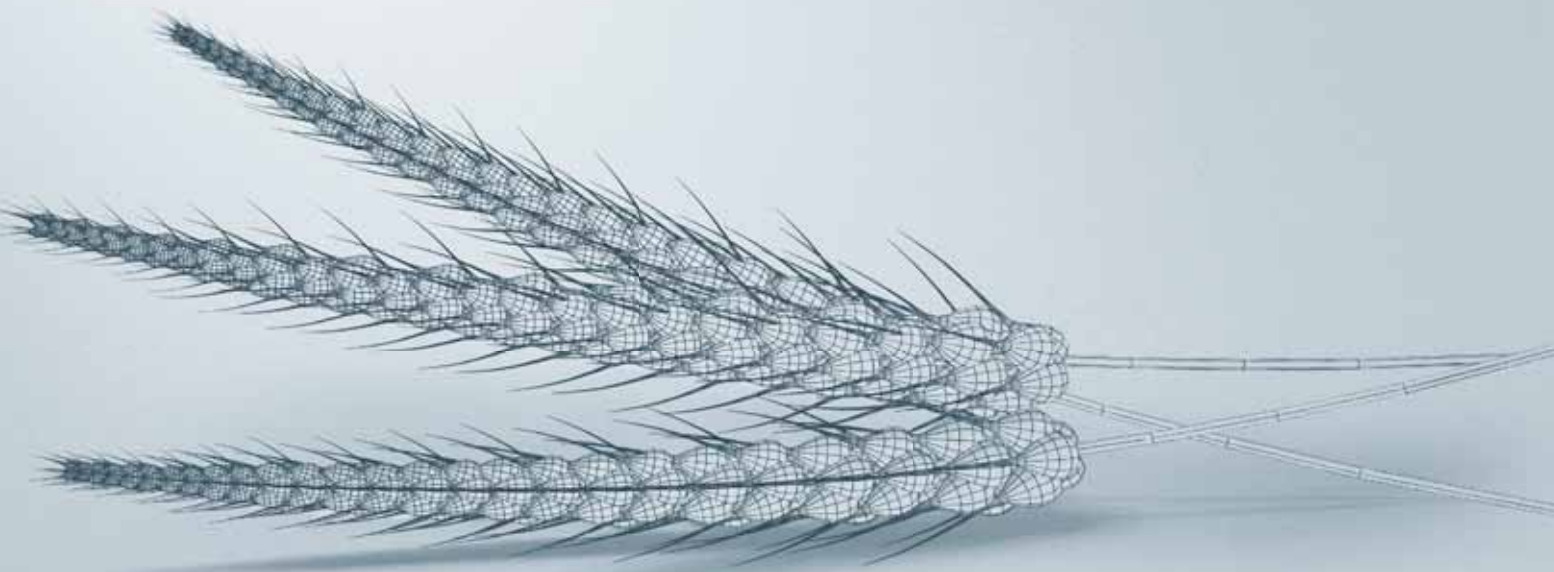
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Understand your level of risk appetite

How some simple checks can help you determine what kind of investor you will be

Investing is always a risk, whether your money is in a government-backed bond or emerging markets equities, but there are many different levels of risk.

Every investor will have a different appetite for and tolerance of risk and taking the time to assess what yours is can mean the difference between sleepless nights and a comfortable investment journey.

Risk tolerance is, simply, how much volatility you can stand in your investments before it makes you feel uneasy. One of the first things that is said about investing is that it should be for the long term as this gives you the time to ride out any ups and downs in the stock market, but these ups and downs should never be so extreme as to make you panic.

HOW MUCH RISK ARE YOU PREPARED TO TAKE?

While some investors are ready to ramp up the risk in the hope of achieving greater gains, others would prefer a steadier ride; this latter strategy might mean the potential returns are not as high but should ensure you can sleep at night.

Patrick Connolly, chartered financial planner at Chase de Vere, says: 'When people hear "risk" in association with investing, the first thought tends to be about loss of capital. But risk goes much further than



that: it is about the full extent to which investments can make or lose money.

'If you can understand what risk is really about and can identify your own attitude to risk, then you will be in a better place to create a portfolio that includes risk at a level you are comfortable with.'

But assessing your own appetite for risk can be difficult as it is an inherently subjective concept: one person's high risk is another's steady Eddie. Risk questionnaires are one way to help determine what level of risk you are likely to be comfortable taking.

ANSWERING THE RIGHT QUESTIONS

Risk questionnaires can take numerous forms. Many robo-

advice websites, such as Nutmeg, have these built into their set-up. These ask new clients to answer some relatively simple questions to help direct them to one of a number of ready-made portfolios – the one that is most suitable to their needs.

Nutmeg asks your investment goal and time horizon and how much you will invest before asking you to select from risk/reward options including cautious, steady, balanced, growth and adventurous. Wealthify, another robo-advice site, asks the same questions: what is your goal, how much are you investing and for how long. It asks investors to rate their investment style on a scale of one to five.

Such sites may be suitable for those starting out with small



amounts to invest, but other investment groups offer more sophisticated questionnaires. Standard Life and Oxford Risk pose ten statements, including ‘My friends would say that I am cautious’ and asks investors to say how accurate the statement is ranging from strongly disagree to strongly agree.

Other statements include: ‘Even if I could get high returns, I would prefer not to invest my money in something that might decline in value’ and ‘Being financially cautious is important to me’. Investors are then ranked on a scale from 1 to 50, to indicate whether they would suit a lower, medium or higher risk investment.

GETTING MORE THOROUGH

There are more thorough questionnaires available to investors too, although these may cost money or be available through a financial adviser. One such example is Finametrica, which asks 25 multiple choice questions such as ‘When you think of the word “risk” in a

“**WHEN INVESTING MONEY, IT’S IMPORTANT TO CONSIDER MORE THAN JUST YOUR ATTITUDE TO RISK. YOU NEED TO THINK ABOUT YOUR CAPACITY FOR LOSS AND YOUR NEED TO TAKE RISK TO MEET FINANCIAL GOALS.**”

financial context, which of the following words comes to mind first: Danger, Uncertainty, Opportunity or Thrill?’ Other questions include ‘Would you prefer more job security

and small pay increase, or less job security and a big pay increase’ and ‘How easily do you adapt when things go wrong financially?’

While such questionnaires are more in-depth, there are still limitations with using these. A question about how an individual adapts when things go wrong, for example, may be relevant if they are picking investments for their own stocks and shares ISA but will not be so helpful if they are setting up a Junior ISA for their child or grandchild.

Connolly adds: ‘An online questionnaire, such as those available from a robo-adviser, doesn’t benefit from the engagement, further probing and empathy that you would experience if you’re face-to-face with a financial adviser.’

SWAYED BY MARKET SENTIMENT

There is also the risk that the answers given are influenced by the current environment; investors may, for example, feel more open to risk when stock markets are soaring and more cautious after market falls, which could influence the way they interpret and answer questions.

Martin Bamford, managing director at adviser firm Informed Choice, says: ‘When investing money, it’s important to consider more than just your attitude to risk. You need to think about your capacity for loss and your need to take risk to meet financial goals.’



By **Holly Black**

Why you should pay attention to the opening of China's bond market

Geoffrey Lunt, fixed income specialist at HSBC Global Asset Management, explains the appeal of Chinese debt

From this month, for the first time in history, one of the most followed global bond indices – the Bloomberg Barclays Global Aggregate Index – will contain Chinese government and high quality renminbi bonds. Investors might shrug their shoulders and say ‘so what?’

But we believe this news is very significant in two ways. Firstly, it underscores the Chinese authorities’ drive to integrate their economy into the global financial system. Secondly, it can help investors to diversify their holdings and seek out investments they had not previously considered.

China has opened its bond market to global investors because it needs investment to support its currency and finance new projects. Long gone are the days when China enjoyed massive surpluses as the world’s low cost producer.

The economy is now driven far more by domestic demand which is vulnerable to a weak currency. Opening its financial markets also means greater international use of the renminbi, cementing ties with trading partners and reducing reliance on the US dollar.

The inclusion supports an



ongoing need for investors to diversify their portfolios. With interest rates still at rock bottom in the UK and across much of the rest of the world, the option to invest in high quality, higher yielding foreign bonds is an alluring prospect.

While this means that a UK investor will be taking currency risk, we believe the Chinese authorities are incentivised to keep the renminbi steady, if not slightly stronger, against a weighted basket of the currencies of their trading partners.

The **HSBC RMB Fixed Income** fund – as well as other similar funds available on the market – allow UK investors to take advantage of the attractive characteristics of Chinese bonds.

While investing in Chinese bonds may seem a scary prospect for many investors who are used

to sticking to their home markets and familiar environments, we believe that this is another step in the ongoing evolution of global financial markets.

The difference this time is that China is by far the largest economy and market to ever integrate into the global financial system.

But just as we have quite quickly got used to China being an essential part of the global economy, so we believe that investing in Chinese assets will soon become mainstream and no one will question the wisdom of doing so.

ALTERNATIVE WAYS OF GAINING EXPOSURE TO CHINA-RELATED BONDS INCLUDE:

Baring China Bond Fund (B6Z0NH4)



Fullgoal FTSE China Onshore Sovereign and Policy Bank Bond 1-10 Year Index ETF (RMB2)



Xtrackers II Harvest China Government Bond ETF (CGB)

Source: Shares

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Do commodity prices suggest stock markets are right to be bullish?

The performance of individual markets has been very diverse

A surge in the oil price to six-month highs above \$70 a barrel, using Brent crude as a benchmark, is grabbing a lot of headlines.

Uncertainty over Libyan and Venezuelan output is contributing to crude's gains but a greater near-term influence appears to be US president Donald Trump's determination to exclude Iranian supply from global markets.

The White House is withdrawing a sanctions waiver from eight nations who buy oil from Tehran with the likely result that around 1.2m barrels of oil per day (bopd) will be unavailable – no small matter in a market where supply and demand are already finely balanced around the 99m bopd mark.

That said, Trump is already calling on OPEC, and Saudi Arabia in particular, to increase output to ensure that oil prices do not rise sharply. A big jump in prices at gas stations is the last thing Mr Trump will want to see, as it may jeopardise his target of 4% GDP growth and also dent consumer confidence as he prepares for the November 2020 Presidential election.

And this shows the inherent difficulty of investing in commodities, as so many factors can affect supply or demand in the near term. They can be related to technical issues, the weather, geopolitics, human error, changes in taste or fashion, disease and currency movements, as well as economic growth.

WIDE RANGE OF RESULTS

These challenges are reflected in the performance of individual commodities in 2018 and 2019. Very few clear trends emerge over the last 16 months.

The exceptions being perhaps the strong gains made by palladium, helped by a switch by car-buyers from diesel to petrol cars following a string of emissions scandals; a fall in coffee, due to last



COMMODITY	2018	COMMODITY	2019 to date
Wheat	24.1%	Live hogs	58.2%
Palladium	19.6%	Oil - WTI	44.5%
Corn	7.1%	Oil - Brent	41.4%
Live cattle	1.9%	Nickel	15.5%
Gold	(1.7%)	Zinc	13.8%
Silver	(8.8%)	Palladium	12.3%
Soybeans	(9.2%)	Platinum	10.6%
Cotton	(11.1%)	Copper	6.9%
Live hogs	(14.1%)	Cotton	5.8%
Platinum	(14.3%)	Sugar	1.8%
Nickel	(16.5%)	Live cattle	0.1%
Sugar	(17.3%)	Gold	(0.1%)
Aluminium	(17.4%)	Aluminium	(1.1%)
Copper	(17.5%)	Soybeans	(2.9%)
Coffee	(18.6%)	Silver	(3.5%)
Oil - Brent	(20.2%)	Corn	(4.9%)
Zinc	(24.5%)	Wheat	(12.5%)
Oil - WTI	(25.3%)	Coffee	(24.0%)
Bloomberg Index	(10.5%)		8.3%

Source: Refinitiv

year's bumper Brazilian crop and a drop in Brasilia's currency, the real, which is fuelling low-priced exports; and the failure of gold and silver to do much at all.

You would have needed a crystal ball to spot (and buy) the best-performing individual commodities of 2018 and 2019 to date.

Last year, wheat sat on top of the pile, thanks to hot and dry conditions hitting supply of American hard red winter wheat and crops grown in Southern Russia.

This year's biggest gainer so far are live hogs. An outbreak of African swine fever in China, home to the world's largest pig population, is driving prices higher amid fear that up to 130m animals, or a third of the total Chinese drove, could be lost.

GLOBAL TRENDS

The lack of a yield and their price volatility may still deter many investors from seeking exposure to commodities and they may not be suitable or appropriate for everyone. Those who do feel raw materials may offer some useful diversification in a balanced portfolio still have to address the question of how best to address the asset class.

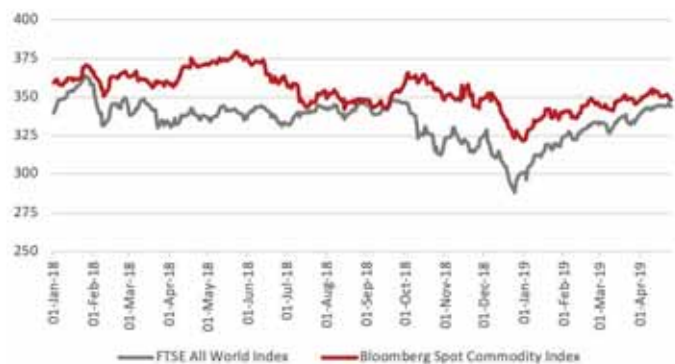
The wide range of performance between individual commodities means that time-pressed investors are unlikely to want to take the risk of trying to choose between the 'right' and 'wrong' commodities at any given time.

They may instead prefer to seek broad-brush exposure, via a tracker which follows a basket of materials of a fund that invests in quoted companies that are involved in agriculture, energy or mining.

This strategy is at least gaining some succour from a solid performance in 2019 to date of the Bloomberg Commodities index, a basket of 23 raw materials following this year's first-time inclusion of low-sulphur gas oil.

The 10% fall in the benchmark in 2018 is easy to understand in the context of the global growth scare and equity market sell-off which gripped financial markets in the fourth quarter. And this year's 8% advance looks to make sense in the context of a recovery in the US equities in particular, but also the broad FTSE All-World index, which is up by a handy 15% in 2019 to date.

BLOOMBERG COMMODITY INDEX IS RECOVERING FROM A ROCKY 2018



Source: Refinitiv

This gain may also give buyers of bonds some pause for thought, if it does mean that a truly inflationary recovery is finally upon us.

The situation is still far from clear cut, since energy represents 30% of the Bloomberg Commodity Index, oil's 40%-plus gains this year will be exerting great influence over the benchmark. But those investors who are bullish on equities (or commodities for that matter) may be able to draw some comfort from a 6% gain in 'Doctor Copper', the ductile, malleable widely-used metal which is traditionally seen as a good guide to the health of the global economy.

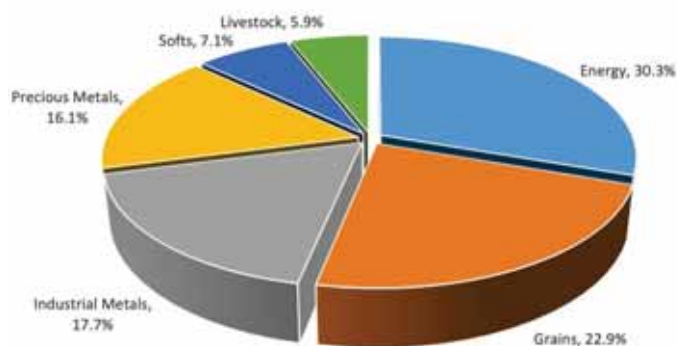
One potential warning sign, however, remains

'DOCTOR COPPER' IS SHOWING WELCOME SIGNS OF A RETURN TO HEALTH IN 2019



Source: Refinitiv

ENERGY AND GRAINS ARE LARGEST CONSTITUENTS OF BLOOMBERG COMMODITY INDEX

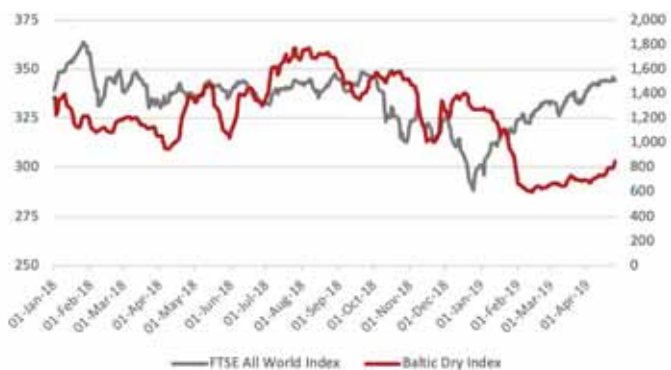


Source: Refinitiv

the Baltic Dry shipping index, a measure of activity in dry bulk cargoes such as grains, ores, coal and building materials. It is still down by around a third this year, to perhaps reflect weak global trade flows, and a recovery here would provide some comfort that equity and commodity markets are right to have faith in the globe's economic growth prospects for 2019 and beyond.



BALTIC DRY SHIPPING INDEX SANK SPEEDILY IN EARLY 2019



By **Russ Mould**
AJ Bell Investment Director

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The easy way to invest in global markets

ETFs and trackers can take the stress out of picking a fund



Knowing where to start when looking at global equity funds can be a complex task given there are over a thousand of them, investing in all kinds of sectors, countries and market caps.

One way to begin investing in global equity is via tracker funds, which follow all the companies in an index and include some of the world's biggest names including Apple, Amazon, Facebook and Microsoft.

Using AJ Bell's favourite funds list, we've found two funds which may suit those looking to access global markets for the first time, the **Fidelity Index World Fund (BJS8SJ3)** and the **Lyxor Core MSCI World (LCWL)** exchange-

traded fund (ETF).

Both products follow the MSCI World Index, a basket of stocks that contains 1,635 mid and large cap companies across 23 developed market countries. Over 62% of such companies are in the US, with others in countries like Japan, the UK, France, Canada and China.

A CHEAPER OPTION

Compared to active funds they are considerably cheaper, with both having a fund manager's charge of 0.12% a year. For active funds, depending on the fund, the figure can vary from around 0.6% to more than 1%.

Both the Fidelity tracker fund and the Lyxor ETF have

performed broadly in line with the benchmark, the Fidelity fund returning 15.08% annualised over three years, while the Lyxor ETF in the year-to-date – the only figure available since its inception in February last year – has returned 15.69%.

The comparable figures for the benchmark are 14.9% and 15.89% respectively.

However, while the returns are decent compared to some other asset classes, particularly in global equities active funds have tended to outperform the benchmark in recent years.

Two of the most popular active funds in global equity are **Fundsmith Equity (B41YBW7)** and **Lindsell Train Global Equity**

(B3NS4D2), both of which use the MSCI World Index as a benchmark. The funds have an annualised three-year return of 20.63% and 24.11%, and have a fund manager's charge of 0.95% and 0.71%.

But that's not to say all active funds have had such a good time in recent years. **Newton Global Income (B7S9KM9)** and **Schroder Global Recovery (BYRJP3)**, two other well-known funds popular with investors, have both performed below the benchmark with an annualised three-year return of 13.32% and 12.58%, and charges of 0.8% and 0.87%, respectively.

“ONCE THE CURRENT QE CYCLE ENDS AND SUCH COMPANIES START GROWING LESS, IN THEORY VALUE STOCKS SHOULD START MAKING A COMEBACK. IT IS UNCERTAIN HOWEVER WHEN EXACTLY THAT TIME WILL COME”

Though it's worth noting that the type of stocks both funds invest in – income stocks and value stocks – haven't done as well in the short term.

Value stocks in particular have underperformed in the last five years, as measures from central banks to boost the money supply, such as quantitative easing (QE), in countries like the US has meant the more fashionable companies, like tech firms, have seen a lot of this capital invested in them.

But once the current QE cycle ends and such companies start growing less, in theory value stocks should start making a comeback. It is uncertain however when exactly that time will come.

So the Fidelity Index World and Lyxor Core MSCI World ETF would therefore seem to represent a good middle ground given their decent returns and low cost. But which one is the better option?

WHICH ONE TO CHOOSE?

In truth both products would be suitable for most investors. Choosing between them may simply come down to a matter of preference.

As a mutual fund as opposed to an ETF, the Fidelity fund is available to trade only once a day and is bought and sold at its net asset value.

An ETF on the other hand is traded throughout the day, like a stock, potentially offering a greater level of transparency.



By **Yoosof Farah**
Reporter

Why the recovery at Luceco looks attractive

Optimism is rapidly returning to electricals to LEDs manufacturer

LED lighting and electricals manufacturer **Luceco (LUCE)** is on track to roughly double pre-tax profit in 2019 as it bounces back from a series of problems. These challenges have included retail-facing customers running down existing LED stocks and price increases on key raw materials, particularly copper.

But it was the disastrous stock and currency mis-management that really hurt, smashing profit margins to pieces and causing the company to issue two profit warnings, first in December 2017 and then again in March 2018.

This has left the company's 2018 trading performance deeply scarred and the share price significantly discounted. But the stock market is forward-looking and we believe more recent positive noises from the company make this an opportune time to revisit the longer-term investment story.

WHAT DOES LUCECO DO?

The Telford-based business operates supplies a large collection of electrical products to both retail and wholesale suppliers, covering industries such as commercial construction, residential housebuilding and housing maintenance operators, what is often called the RMI market, or repair, maintenance and improvement.

Customers investors may have heard of include FTSE 100 plumbing supplies group **Ferguson (FERG)** – previously known as Wolseley – **Travis Perkins (TPK)** and **Grafton (GFTU)**, plus major DIY chains such as Homebase and the Screwfix and B&Q chains owned by **Kingfisher (KGF)**.

Luceco operates through four brands – BG (wiring accessories), Masterplug (extension leads, cables and portable power) and Ross (TV wall mounts). The final leg is

the Luceco branded LED lighting business.

The LED business is the one that retail investors are likely to know best. Since the company joined the stock market in October 2016 is frequently referred to as LED lighting company Luceco.

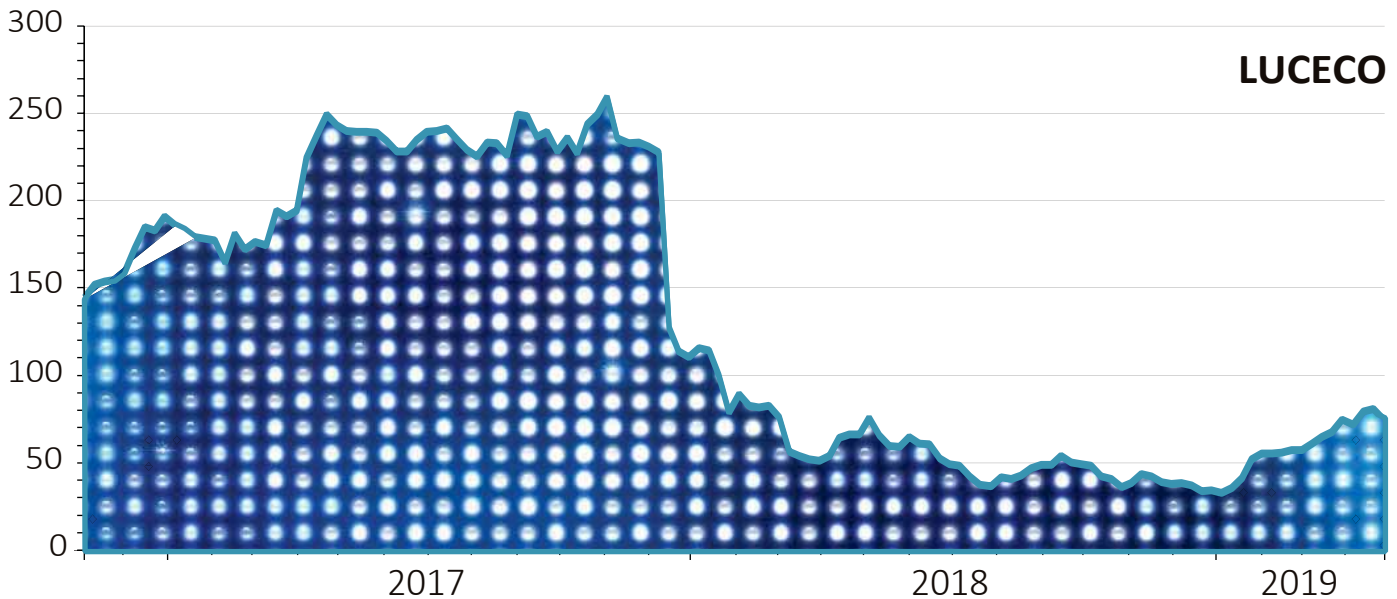
This is a little misrepresentative since the LED lighting business was built from scratch just five years ago. While it does offer promising growth potential in the future its profit track record is patchy.



	LED Lighting	Non-LED lighting	Total
2010	5%	95%	\$1.6bn
2011	9%	91%	\$1.5bn
2012	15%	85%	\$1.5bn
2013	20%	80%	\$1.6bn
2014	26%	74%	\$1.8bn
2015	32%	68%	\$1.9bn
2016f	39%	61%	\$2.1bn
2017f	44%	56%	\$2.2bn
2018f	47%	53%	\$2.2bn
2019f	50%	50%	\$2.3bn

Source: AMA LED Lighting report, Luceco

LUCECO –THE LAST THREE YEARS



In contrast, the wiring and cables businesses have been around for decades and have had time to establish themselves as go-to suppliers of market leading products where quality and safety is more important than price. Who wants to buy cheap where 240 volts is concerned?

BG and Masterplug accounted for two-thirds of revenue in 2018 and nearly all of the £8.5m pre-tax profit, after adjustments.

WHAT WENT WRONG?

While managing end customer demand and commodity pricing are largely part of the normal cycle of doing business Luceco holds up its hands on the inventory miscalculation mistakes made. That led to the resignation of the company’s financial controller at the time and prompted a detailed rethink of internal controls and processes.

This resulted in significant investment in things like sales and marketing, product development while also streamlining parts of the

business, including closing down its small US operation.

What this means is that costs needed to get the business back on track are now largely sunk with the rewards still to come.

So while 2018 results to 31 December, announced on 9 April, looked ugly the company’s rhetoric is becoming increasingly optimistic.

‘We currently have a strong order book and revenue growth is running in line with expectations,’ chief executive John Hornby said then, before adding his confidence that operating profit for 2019 will be ‘comfortably ahead of current market expectations.’

Operating profit forecasts had been pitched at £13m for 2019 but unsurprisingly analysts at broker Numis still lifted their estimates by another £1m to £14m even after having previously upgraded 2019 estimates as recently as January.

Importantly for the medium-term, operating profits are now expected to continue their

rapid recovery into 2020, with Numis now anticipating £16.5m, implying 18% growth.

This is possible through the combined dynamics of solid single-digit revenue growth, a lower-cost manufacturing base in China, plus rebuilding operating profit margins from high single-digits forecast for 2020 back to the mid-teens of a few years ago.

There are still challenges to overcome, not least ongoing questions about the sustainability of global growth, as well as Brexit uncertainty and what that might do for exchange rates and commodity pricing.

SHARES SAYS: ↗

Luceco’s destiny feels back in its own hands and looks like a relatively lower risk recovery-to-growth story on a 2019 price to earnings multiple of 13.4-times, based on a 78p share price.



By Steven Frazer
News Editor

‘How do I find the best annuity rate?’

Our pensions expert talks a reader through comparing providers

‘There are numerous publications and websites to compare platforms but how can a private investor find the best annuity rate?’

David



Tom Selby
AJ Bell
Senior Analyst says:

Can I start by commending you for looking to shop around the retirement income market - this is an absolutely essential part of getting the right solution at the best price without overpaying in costs and charges.

It is particularly crucial for anyone buying an annuity as this decision is irreversible. By contrast, savers who enter drawdown have the option of switching providers if they are not happy for any reason.

There are various sources you can use to compare annuity rates but I’d suggest the Money Advice Service (MAS) annuity calculator, which you can access [here](#).

There are a couple of reasons I like this annuity comparison tool. Firstly, MAS is an independent organisation created by the Government, so you can be confident the information presented to you doesn’t have any commercial bias.

Some comparison services work on a ‘pay-to-play’ basis, meaning you are only seeing

offers from providers which have agreed to pay a commission to the broker.

The MAS service searches for quotes from the following providers: Aviva, Canada Life, Hodge Lifetime, Just, Legal & General, LV= and Scottish Widows. You can draw comfort from the fact this list dominates the annuity best-buy tables and contains firms offering individually underwritten policies. This means if you have any life limiting factors – for example an illness or you smoke – you could be offered a better rate.

Secondly, this comparison service allows you to input your own personal details to ensure you can access both the right product and the best deal.

This includes questions about your age, inflation protection, guarantee periods, spouse’s benefits, any illnesses and lifestyle choices that could affect your rate one way or another. As a result, the quote that comes out incorporates a degree of individual underwriting.

Once you’ve picked your



provider you’ll need to go through their underwriting process (the MAS service doesn’t allow you to transact).

At this point it’s worth double-checking you’re comfortable with your decision to secure all or part of your pot as a guaranteed income for life, as well as ensuring you understand the features of the product you’re buying.

For many securing a portion of their income through an annuity will be a sensible decision but it is also a significant one which demands careful planning.

As always, given the significance of this decision you should consider speaking to a regulated financial adviser to make sure you’ve got all the bases covered.


DO YOU HAVE A QUESTION ON RETIREMENT ISSUES?

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

Please note, we only provide guidance 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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7 May: Domino's Pizza. **8 May:** Direct Line Insurance. **9 May:** RSA Insurance, Barratt Developments, Superdry, Morrisons. **10 May:** International Consolidated Airlines.

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