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THE ULTIMATE GUIDE TO **INVESTING IN THE TECHNOLOGY SPACE**

Understanding the impact of inflation on your investments

The Bank of England warns that the cost of living could exceed its 2% growth target in 2021

Many investors fail to factor in the impact of inflation when thinking about what their money can buy and the true value of their investment returns. This isn't wise as individuals are potentially overestimating the power of their money.

It is easy to see why inflation is overlooked as rates have been relatively low for some time. For example, UK inflation recently hit a two-year low at 1.8%.

The Bank of England has a 2% target and thinks CPI inflation could be lower than the current 1.9% rate in the short-term in reflection of lower expected retail energy prices. Howard Archer, chief economic advisor to the forecasting group EY ITEM Club, even believes inflation could get as low as 1.6% during the year.

The drop in inflation is good news for consumers but this may only be a temporary phenomenon. The Bank of England last week upgraded its GDP growth forecast to 1.5% in 2019, 1.6% in 2020 and 2.1% in 2021 – versus previous estimates of 1.2%, 1.5% and 1.9% respectively.

The Bank of England fears this growth could turn into rising prices and inflation could exceed its 2% target. That suggests the potential for more interest rate rises than is currently expected by the market in order to stop the economy racing ahead too fast.

Investors need to consider this outlook and put inflation front of mind when considering their desired returns from both cash and investments. A rising cost of living affects various economic factors which in turn influence stock and bond prices, and your own purchasing power.

A rising interest rate scenario would imply better returns on cash savings, however you must think about whether the interest rate on a cash account is wiped out by inflation.

The top easy-access savings account at the moment is Marcus, paying 1.5%. The current rate of inflation at 1.9% means you would be getting a 0.4% negative real return from cash in such an account. In this situation anyone saving in cash is worse off when factoring in inflation.

Bond investors tend to suffer during periods of rising inflation. And for investments in individual company shares, inflation reduces the net present value of a company's expected cash flows – implying that stock prices should fall as a result. Yet rising prices also suggest future cash flows will be higher because companies are able to make bigger profits.

'In theory, these two forces should cancel each other out. In practice, markets often recoil at signs of inflation for fear the economy is overheating and interest rates will go up,' says Phil Thornton, lead consultant at Clarity Economics.

Equities – another term for stocks and shares – have delivered 4.7% real returns (i.e. adjusted for inflation) each year over the past 50 years versus 1.1% from cash, according to Barclays.

Those figures are a good indication of what you can expect to make from different asset classes, albeit history tells us there could be tough patches. For example, equities delivered a 1.5% negative real annual return between 1998 and 2008, found Barclays, versus a 2.4% positive real annual return from cash.

By **Daniel Coatsworth** Editor

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Three stocks that match Warren Buffett's criteria as he eyes a UK acquisition

His Berkshire Hathaway vehicle has $120bn cash and is hungry for a deal

Arguably the world's most famous living investor, Warren Buffett has once again signaled that his investment vehicle Berkshire Hathaway could make a sizeable acquisition in the UK.

Having revealed his willingness to strike such a deal in a recent *Financial Times* interview, Buffett repeated this desire last weekend at Berkshire Hathaway's annual shareholder meeting.

His company's cash pile is currently worth $120bn, meaning that Berkshire Hathaway has considerable resources to make a very large acquisition.

He said at the meeting: 'I am not an Englishman, but I have a feeling it was a mistake to vote to leave, but it doesn't destroy my appetite in the least for making a very large acquisition in the UK.'

Berkshire Hathaway previously invested in UK supermarket chain **Tesco (TSCO)** and still owns 69.1% of Northern Powergrid, which distributes electricity in the north east of England.

We believe Buffett would want to buy a large UK business with at least $100m of pre-tax profit.

He has a tendency to favour companies generating lots of free cash flow and a consistent record of earning high rates of return on equity. Those criteria reduce the universe down considerably.

Warren Buffett at the annual Berkshire Hathaway shareholder meeting last week (4 May 2019)

Consumer franchises such as **Unilever (ULVR)** would fit the criteria, but it has previously rebuffed an offer by Berkshire and its partner 3G Capital.

Screening for Buffett-type stocks also reveals **Taylor Wimpey (TW.)** and **Berkeley (BKG)** as possible targets. Berkshire Hathaway understands housebuilders well; it has a dominant 49% share of manufactured homes in the US, through its ownership of Clayton Homes.

It is far more likely that Buffett will strike a deal with a family-controlled business, where the cultural fit with Berkshire Hathaway is strong and the family is looking to exit, confident that the business will receive careful stewardship.

AN AUDIENCE WITH BUFFETT AND MUNGER

Often called 'Woodstock for capitalists', Berkshire Hathaway's annual shareholder meeting took place on 4 May, with 44,000 people flocking to Omaha, anticipating words of wisdom from leaders Warren Buffett and Charlie Munger.

Over the decades Berkshire Hathaway's meeting has grown from a small gathering at a cafeteria of National Indemnity to a weekend-long extravaganza. Buffett and Munger typically answers questions for five hours on stage.

For the last few years the event has been live-streamed over the internet and the webcast also translated into Mandarin. It is estimated that the event is watched by 3.1m people worldwide.

Investors continue to desert UK and European equity funds

More than £2.4bn overall has been pulled out as uncertainty reigns

Investors continue to shun UK and European equity funds in favour of global exposure as economic and Brexit uncertainties continue to hold sway.

More than £2.4bn has been pulled out of the funds space during the first three months of the year according to data from the Investment Association, the trade body that represents UK investment managers.

Both retail investors and institutions have been net sellers with broader opportunities being sought out.

UK equity funds have now experienced 23 consecutive months of outflows, totalling £8.6bn according to stockbroker Numis.

Funds in the UK All Companies sector which saw large amounts of money taken out by investors in March included £158m of outflows from **Woodford Equity Income (BLRZQ73)** and £121m from **Invesco High Income (BJ04HQ9)**.

'Savers have turned towards global equity funds and mixed-asset funds in the first quarter, whilst fixed income funds have seen a return to inflows,' says Chris Cummings, chief executive of the Investment Association.

Fixed income assets were the best-selling asset class during March with £810m in net retail sales, according to the report, as UK investors reduced their appetite for risk. There was also an escalation of investors moving into cash, with money market products the second best-selling asset class in March, with net retail sales of £127m.

This is despite a growing number of UK fund managers talking up the relative attractions of UK shares including Alex Wright, Fidelity's highly rated contrarian manager.

BEST PERFORMING UK FUNDS 2019*	
Standard Life Investments UK Opportunties Retail Platform	26.38%
Legal & General Growth Trust	22.63%
Baillie Gifford UK Equity Alpha Fund	22.51%
Aberdeen UK Mid-Cap Equity Fund	21.65%
Marlborough UK Multi-Cap Growth Fund	21.64%
Allianz UK Mid-Cap Fund	20.58%
Royal London UK Opportunities Fund	19.93%
AXA Framlington UK Mid Cap	19.90%
GVQ UK Focus Fund	19.34%
Franklin UK Mid Cap Fund	19.12%

Source: AJ Bell Youinvest *returns performance year-to-date

BEST PERFORMING EUROPEAN FUNDS 2019*	
Legg Mason IF Martin Currie European Unconstrained Fund	19.83%
Barings European Growth Trust	19.17%
Schroder European Fund	17.63%
LF Miton European Opportunities Fund	17.22%
Scottish Widows European Select Growth Fund	17.14%
Artemis European Opportunities Fund	16.92%
Aberdeen European Equity	16.89%
Man GLG Continental European Growth Fund	16.71%
Allianz Continental European Fund	16.44%
BlackRock European Dynamic Fund	16.41%

Source: AJ Bell Youinvest *returns performance year-to-date

Lloyds, HSBC, Domino's and other recent news

We run the rule over some of the past week's big share price movers

Numbers from **Lloyds Banking (LLOY)** and troubled challenger **Metro Bank (MTRO)** on 2 May did little to lift the mood after a difficult first quarter reporting season for the banks.

Lloyds reported flat first-quarter profits that fell short of market expectations amid exceptional costs including charges relating to payment protection insurance (PPI) and an estimated charge for pulling the Standard Life Aberdeen investment mandate.

Impairments also ticked up in the period, reminding investors that the company's destiny is heavily tied to the UK economy. The company has a lot of exposure to secured and unsecured lending and there is a risk a chaotic Brexit could see bad debts spiral.

If this was a disappointing update, Metro Bank's was downright disastrous. The number of new customers continued to rise across both personal banking and business banking but 'a small number of large commercial and partnership customers' withdrew deposits after the January trading update due to 'adverse sentiment'.

This resulted in a net reduction in average deposits per branch of £2.9m compared with an increase of £4.7m in the fourth quarter of last year.

At least **HSBC (HSBA)** did better with its own Q1 performance (3 May), with adjusted pre-tax profit coming in substantially ahead of expectations though the number was flattered by $400m worth of favourable one-off items.

The misery continued for shopping centre landlord **Intu Properties (INTU)** on 3 May, with a profit warning driving the shares to fresh all-time lows around 90p. Like-for-like net rental income for 2019 is expected to be down by 4% to 6% compared with previous guidance for a decline of 1% to 2%.

On 7 May pizza takeaway firm **Domino's (DOM)** and hybrid estate agent **Purplebricks (PURP:AIM)** were both stung by overseas struggles.

Domino's warned that its international business would not break even as promised in 2019 and Purplebricks said it would exit Australia and scale back ambitions in the US due to various struggles, resulting in the departure of founder and chief executive Michael Bruce.

FTSE 350 MOVERS OVER THE PAST WEEK – BEST PERFORMERS

STOCK	SHARE PRICE RISE/FALL	REASON
AJ Bell	11.1%	Continuing positive reaction to strong first half update
Smith & Nephew	7.6%	Says it expects full year sales at top end of target
Indivior	7.3%	Promises 'strong defences' against US fraud charges

FTSE 350 MOVERS OVER THE PAST WEEK – WORST PERFORMERS

STOCK	SHARE PRICE RISE/FALL	REASON
Metro Bank	-19.4%	Profit halves in first quarter period
ContourGlobal	-9.0%	Mixed reception to Kosovo power plant news
Aston Martin Lagonda	-8.5%	Lingering weak sentiment and negative read-across from poor BMW results

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

Source: Shares, Sharepad

TI Fluid has it all: growth, cheap shares and dividends

The FTSE 250 member is under the radar of most investors so get in quick

The ultimate goal for many investors is to find a mid or large cap stock offering earnings growth, decent dividends and trading on a cheap valuation.

Stocks with all of those attributes are rare in the current market. Fortunately we've spotted one which ticks all the boxes and hardly anyone has heard of it. This is your chance to buy the shares while the stock is under the radar and trades on a bargain rating.

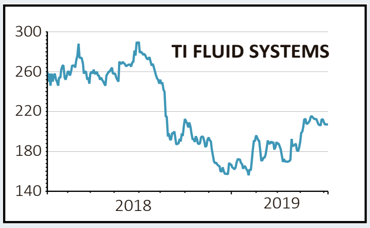
The company in question is **TI Fluid Systems (TIFS)**, a £1bn auto specialist which has been around for more than 100 years and has a global footprint as a critical supplier to vehicle manufacturers.

The FTSE 250 member trades on a mere 6.5 times next year's earnings and sports an attractive 5.1% dividend yield.

Peel Hunt analyst Harry Philips said on 20 March: 'We accept that TI Fluid is a "newish" company to the market and Bain Capital has a 54% holding but a 2019 PE (price-to-earnings) ratio of just 6.6, an EBITDA multiple of 3.5 and a free cash flow yield of 13.3% for a proven business model is the wrong price.' To put that in some context, the sector median EBITDA multiple is 6.6-times. The figures cited by Philips are slightly different to the table because the share price has subsequently changed.

TI FLUID SYSTEMS
BUY
(TIFS) 207p
Stop loss: 150p

Market cap: £1bn



WHAT'S THE CATCH?

You may ask why this stock is trading so cheaply. There are several factors; the shareholder list is dominated by the aforementioned private equity group Bain Capital and a few large institutions, limiting liquidity; Bain loaded the company with a lot of debt prior to floating it in October 2017; and the business is not well known outside a few fund managers and analysts.

Bain last year sold a bit of its stake and is likely to sell more shares in the future, such is the model of private equity firms.

Some investors are weary towards companies that have previously been owned by a private equity outfit in the belief that they've suffered from underinvestment. While that is a fair point, we don't believe this applies to all private-equity backed companies.

NEGATIVE SENTIMENT

Another factor to consider is weak market sentiment towards anything related to the automotive sector. Reassuringly, TI Fluid's most recent full year results, published in March, talk about 2018 being a 'great year'

TI FLUID SYSTEMS - KEY FIGURES

	2018A	2019E	2020E	2021E
Sales (€m)	3473	3543	3650	3765
EBITDA (€m)	484	501	515	535
Op.Margin (%)	10.8	10.5	10.5	10.6
Adj pre-tax profit (€m)	235	251	263	283
Adj EPS (c)	29.9	30.4	31.7	34.0
PE (x)	6.9	6.8	6.5	6.1
DPS (c)	9	10	10.5	11
Dividend yield (%)	4.3	4.8	5.1	5.3
Free cash flow yield (%)	11.6	10.9	11.5	12.7

Source Company Accounts, Peel Hunt estimates, Dec year-end for the company. Pre-tax profit increased by 37% to €217.1m.

Chief executive William Kozyra says: 'Despite a slight softening in global light vehicle production growth, we achieved strong organic growth, solid profit margins and free cash flow generation.'

The cash generation is important as it provides the power for TI Fluid to pay down borrowings – it currently has an €822.4m net debt position.

The benefits of deleveraging can super-charge investor returns. Interest charges currently swallow c43% of all the cash that TI Fluid generates from operations. As debts are paid off, the interest cost falls and therefore a greater proportion of the cash will be 'owned' by shareholders.

Investors, in theory, should be willing to pay a higher rating for companies with lower leverage as essentially there is reduced financial risk.

PROSPECTS BETTER THAN THE SHARE PRICE IMPLIES

Fuel efficiency and lower emissions are two megatrends here to stay for the long run and TI Fluid Systems is at the forefront of developing proprietary solutions to both these problems.

Its main line of business is fuel carrying systems where it has 35% market share and has developed strong relationships with all the global vehicle manufacturers. It has an untapped opportunity to leverage this strong market position to drive growth in the electric vehicle and hybrid electric vehicle markets.

Electric vehicles require a

substantial increase in additional fluid content to thermally manage them effectively. In addition, by using lightweight nylon lines TI Fluid has reduced the weight of a vehicle by 30% to 60% compared to traditional aluminium and rubber.

The company has been awarded significant contracts for the design of thermal efficiency management systems. TI Fluid estimates it is currently seeing 50% share of these electric vehicle systems. They have a lifetime value of $700m and an eight to 10-year lifespan.

PLENTY OF FUEL IN THE TANK

Its second line of business is in fuel tank systems, where it has 15% market share. The company has developed a pressurised plastic fuel tank that utilises proprietary technology to meet the new increased fuel vapour pressure requirements of hybrid electric vehicles. Management estimates it is taking a 20% market share in this segment.

According to a report by consultant McKinsey, production of electric vehicles will quadruple by 2020 to 4.5m units. China has a dominant position in the production of electric vehicles; it currently has a larger market than the US and Europe combined. That's fortunate as TI Fluid has a dominant market share in China.

The company has delivered above-average market growth historically. We believe it is well positioned to continue delivering above average-growth in the future.

There is an element of flexibility to the business. TI Fluid claims it can quickly adjust to market disruptions, such as the emissions scandal, and move its costs down in line with production, thus mitigating the impact on profitability.

Over time, particularly as it is a FTSE 250 name, TI Fluid should have better analyst coverage, and liquidity in its shares should improve.

The company is organising a capital markets day for analysts and investors in September, which will hopefully raise its profile and increase the general understanding of the business model. Get on board now before the wider market picks up on the story.

By **Martin Gamble**
Senior Reporter

Irn-Bru maker A.G. Barr is worth its premium price

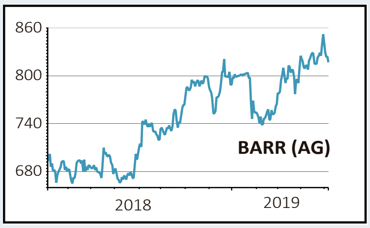
We believe the profitable drinks company can continue to deliver sparkling returns

Do not be put off by a premium equity rating at **A.G. Barr (BAG)**, since the Glasgow-headquartered soft drinks firm has a proven recipe for success.

We believe the *Irn-Bru* maker can continue to compound earnings and generate sparkling returns on a long-term view and given a largely UK sales profile, Brexit appears less of an issue for the FTSE 250-listed company than for internationally-focused beverages firms.

A.G. BARR
BUY
(BAG) 817p
Stop loss: 653.6p

Market cap: £937.75m



WHAT DOES IT DO?

A.G. Barr is a soft drinks manufacturer whose competitive advantage lies in a portfolio of differentiated, highly prized brands spearheaded by iconic Scottish fizzy drink *Irn-Bru*, launched in 1901 and made to a secret recipe.

More recent additions include *Rubicon*, *Strathmore* and cocktail mixers name *Funkin*. The business also benefits from best-in-class manufacturing assets.

SUCCESSFUL RECIPE

Resilient results for the year to 26 January showed adjusted pre-tax profit up 2.5% to £45.2m on sales 5.6% higher at £279m.

The numbers were impressive given a backcloth of market disruption encompassing the implementation of the sugar tax.

Successful reformulation means 99% of A.G. Barr's soft drinks portfolio is now exempt. Extreme weather and the costs associated with an industry-wide CO2 shortage were also headwinds.

Growth was particularly strong in the core carbonate portfolio, driven by *Irn-Bru's* market share gains, notably in England where distribution wins by zero calorie *Irn-Bru Xtra* were a key growth driver.

This shows A.G. Barr is successfully moving with changing consumer tastes as sugar free variants now account for 40% of the total *Irn-Bru* brand.

SPARKLING RETURNS

Debt-free and highly cash generative, A.G. Barr continues to invest in its asset base while repurchasing shares and funding a progressive shareholder reward. Its proud history of dividend increases continued with a 7% total dividend hike to 16.6p for the past financial year.

Despite consumer uncertainty and the risk of further regulation, management is confident of making further progress this year with a return to its long-term strategy of prioritising value over volume set to help margins stabilise.

For the year to January 2020, Investec forecasts pre-tax profit growth to £46.6m, ahead of £48.3m in 2021. Based on the broker's current year earnings per share estimate of 33.2p, with dividend progression to 17p shaded in, A.G. Barr swaps hands for almost 25 times prospective earnings.

Long-term investors should view this as a price worth paying for a dependable, defensive and growing portfolio compounder.

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

BURFORD CAPITAL
(BUR:AIM) £15.50

Loss to date: 1%
Original entry point:
Buy at £15.62, 25 October 2018

IT HAS BEEN a trying time recently for **Burford Capital (BUR:AIM)** after analysts at broking firm Canaccord Genuity cut their earnings forecasts and their target for the stock.

The broker has challenged Burford's claimed 85% return on invested capital (ROIC) and argues that future returns may be lower than the market expects. It also suggests that the firm may need to raise more capital.

Therefore, it argues, the current valuation doesn't reflect the risks involved in owning the stock and it has cut its target price from £15.43 to £11.96.

On the day the broker published its note (30 April) the shares lost 118p or nearly 7% of their value to £16.35, and since publication the shares are down over 200p or 11.5% to £15.50.

NO QUESTION OVER THE GROWTH

Litigation finance is a highly attractive business which continues to grow quickly and Burford has successfully built itself a market-leading position.

In its first year of business almost a decade ago, it received 131 enquiries for funding. Last year it received 1,470 enquiries for funding, so there is no lack of demand.

However income can be very 'lumpy' as investments take between 18 months and two years on average to come to fruition.

Over half of the enquiries that entered Burford's underwriting pipeline last year were related to cases where the estimated damage claim was over $100m. Typically the bigger and more

complex a case, the longer it takes to settle.

By its own admission, Burford is now more like an investment bank for the law business than a litigation funder. Last year it committed $1.3bn of funding, more than three times the amount it invested in 2016, as well as launching a $1bn 'strategic capital relationship' with one of the world's biggest sovereign wealth funds.

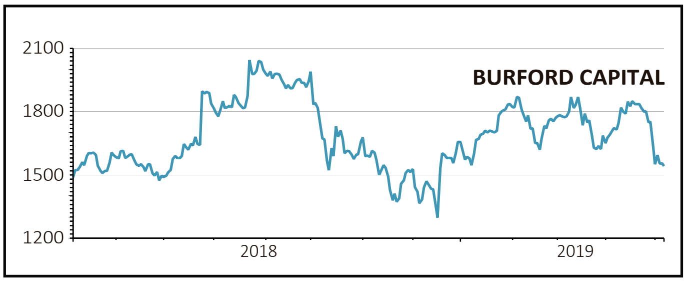
QUESTIONS OVER THE RETURNS

Canaccord argues that Burford's claimed 85% ROIC is misleading and it believes the 'real' return on concluded investments is 51%. It believes that going forward the company should reference the lower number in all of its reporting.

The broker has cut its 2019 and 2020 earnings forecasts by 18% and has questioned whether Burford will be self-funding by the end of the year or whether it will need to raise more capital, diluting returns for shareholders.

In Burford's defence, the company complies fully with IFRS accounting and it is the accepted norm to assume a fair value for the portion of investment which is ongoing while cases are pending final settlement.

DISCLAIMER: The author owns shares in Burford Capital



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RESTAURANT GROUP
(RTN) 147.9p

Gain to date: 30.6%
Original entry point:
Buy at 113.2p, 11 April 2019

LAST MONTH WE flagged to the appointment of a new chief executive as a potential catalyst for shares in **Restaurant Group (RTN)** but we admit to being a little surprised at the identity of the new person in charge.

The incoming boss Andy Hornby is likely to be most familiar with investors from his spell in charge of bank HBOS during the financial crisis, when the company had to be rescued in an emergency takeover by **Lloyds (LLOY)**.

While this is hardly the best calling card, Hornby has held several executive roles out of the spotlight in the intervening period, including a spell in charge of Alliance Boots and more recently as co-chief operating officer of gambling firm **GVC (GVC)**. He enjoyed a successful spell at Coral before its merger with Ladbrokes and subsequent takeover by GVC.

Shore Capital analyst Greg Johnson for one is impressed, saying: 'He brings significant experience in retail, M&A integration and also new channel distribution, which will be increasingly key, especially given the acquisition of Wagamama.'

SHARES SAYS:
It is probably fairer to judge Hornby on his recent track record which is more encouraging than his HBOS days. Keep buying.

NEXT
(NXT) £57.22

FANTASTIC STOCKS FOR 2019

Gain to date: 36.5%
Original entry point:
Buy at £41.91, 20 December 2018

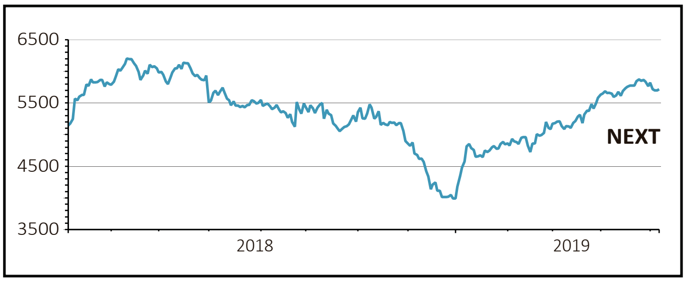
SHARES IN HIGH street bellwether **Next (NXT)** are up an impressive 36.5% since we selected the clothing retail firm as one of our top picks for 2019.

While some may be tempted to take profits off the table following a strong share price run, we're staying positive as the cash generative retailer is run by one of the sector's best-in-class management and remains set fair for online market share gains.

First quarter results (1 May) beat expectations with full price sales growth of 4.5% for the 13 weeks to 27 April boosted by unusually warm Easter weather. Next's management also noted particular strength in February against last year's snow-impacted comparatives.

Despite the quarterly sales beat, reflecting a 3.9% like-for-like sales decline in retail and online sales growth of 11.8%, Next's management team led by CEO Simon Wolfson believes it is too early in the year to upgrade revenue and profit guidance for the year to January 2020, especially as sales comparatives toughen from here.

Guidance remains for pre-tax profit of £715m, down 1% year on year, and 3.4% earnings per share growth after Next's £300m share buyback programme.



SHARES SAYS:
We're sticking with Next for its copious cash generation, capital returns and best-in-class management team, one able to navigate the tricky high street backdrop. (JC)

Investing in the circular economy

How companies can target more sustainable growth – for the planet and their investors – by 'closing the loop'

Since the advent of the industrial era, linear economic models have been dominant. Resources have generally been extracted, used, and then cast aside as waste.

This "take, make and dispose" approach has its limits though, of course. Especially in a world that is growing in both population and wealth, and therefore in the amount it consumes.

Not only are many important resources finite, or increasingly difficult to obtain, but their extraction and single-use can have costly implications for the environment and society.

An alternative to the linear model, and a potential solution to some of its challenges, is moving to a more circular economy, where waste from production and consumption becomes a resource to be recycled, repaired and reused. We can see this as 'closing the loop'.

Waste not, want not

As well as reducing unnecessary waste and mitigating the risks of resource scarcity, making the transition to closed-loop processes can help decouple long-term growth from the extraction of resources.

The importance of this shift is reflected in the UN Sustainable Development Goals, which articulate the world's most pressing sustainability issues. Specifically, Goal 12 is to ensure sustainable consumption and production patterns.

Realising this ambition could also deliver an economic windfall. Research by Imperial College London in 2015 estimated that successfully transitioning to a circular economy could add almost £3 billion to the UK economy each year alone, and create 175,000 new jobs.

This transformation will take more than a change in mindset; it also requires new processes and systems. Durable goods must be designed so they can be repaired, not replaced, and global supply chains will have to be reimagined to enable the reuse and recycling of materials.

Closing the loop

Some companies and sectors have already made great progress towards closed-loop processes that can overcome sustainability challenges. A good example is in the packaging industry.

The widespread use of disposable packaging, for all kinds of purposes, has contributed to highly visible environmental challenges, including plastic waste.

The sustainable practices adopted by one of the world's largest producers of corrugated boxes illustrates how innovation can transform a challenge into an opportunity.

DS Smith is an industry leader when it comes to closed-loop recycling – a process whereby waste is collected, recycled and then used again to make the same product it came from. After collecting corrugated paper from retailers and other businesses, the company processes the recycled material in its own paper mills to create new corrugated boxes. By recycling paper fibres, the company estimates it can save over 360,000 trees a year from being cut down.

Targeting sustainable growth

I believe the transition to a more circular economy should create compelling long-term opportunities for investors who would also like to deliver a positive impact for the environment.

Where companies can successfully shift to closed-loop business models, shareholders can expect to benefit in a range of ways. Transforming waste into a resource should unlock greater value for businesses and, in many cases, reduce costs and risk in their supply chains.

Pioneering companies can also be expected to profit from tailwinds where their businesses align with sustainability trends, such as growing demand for responsibly sourced goods. Early movers stand to steal a march on competitors.

As investors in companies that contribute to a more circular economy – and therefore to more sustainable consumption and production patterns – I believe we can target a positive impact on the environment, alongside sustainable financial returns over the long-term.

Ben Constable-Maxwell is Head of Sustainable and Impact Investing at M&G Investments

The rise of market power and what it means for investors

Companies with dominant market power are likely to face greater scrutiny in the future


In November last year we examined the issue of 'skew' in markets and suggested one explanation for the outsized contribution of a few stocks to the market's overall return might be their outsized returns on capital compared with the market average.

We said at the time that a few firms – notably Amazon, Google and Microsoft – had used their technology to create dominant market positions with no 'trickle-down' benefit for their competitors.

This market power enables them to raise prices to consumers while limiting increases in salaries for their workers and turn more of their revenue into profit, for the benefit of shareholders.

The economic implications of this concentration of market power are a hot topic of discussion among policymakers and regulators, and while the debate hasn't hit the mainstream yet it's important for investors to grasp the concepts involved.

WHY DOES MARKET POWER MATTER?

In its April *World Economic Outlook,* the International Monetary Fund (IMF) looked at the evidence for the existence of market power and its potential consequences.

It found that since the year 2000 market power has clearly increased in advanced economies, but not yet in emerging ones; and that the increase has been 'fairly widespread across industries but concentrated among a small fraction of firms'.

It also found that while the macroeconomic effects so far have been small, 'further increases in the market power of these already-powerful firms could weaken investment, deter innovation, reduce labour share incomes and make it more difficult for monetary policies to stabilise output'.

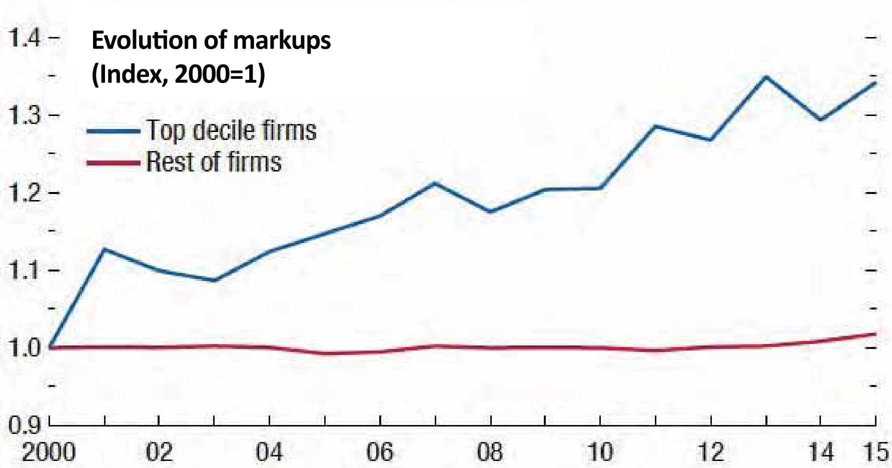
The IMF examined whether market power was responsible for what it called 'worrisome' current economic trends. These include the low level of corporate investment despite low interest rates; the growing gap between returns on capital and those on safe assets like government bonds; the growing gap between financial and productive wealth; falling productivity; and growing income inequality due to the falling share of income going to workers.

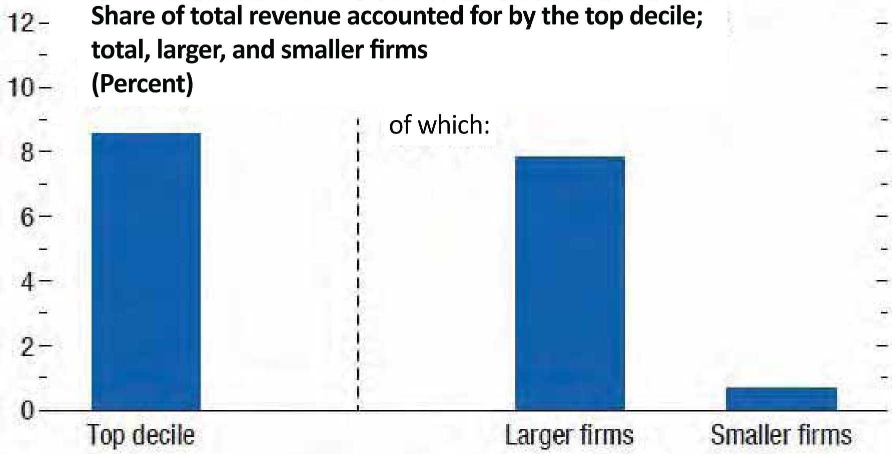
While other factors may explain some of these negative trends, it found that increased market power has contributed to all of them. The question is, what has caused it and what is the appropriate response?

SURVIVAL OF THE FITTEST

For policymakers and regulators, the key issue is whether the dominance of a small group of companies is the result of anti-competitive market regulations and weak anti-trust enforcement, or whether it is a case of 'winner takes most' as more productive and innovative firms take market share from weak competitors.

The IMF found that in advanced economies concentration of market power led to average price mark-ups of 8% from 2000 to 2015, with the most pronounced price rises in non-manufacturing industries in the US.





Source: Orbis; and IMF staff calculations.

Most of the mark-ups were generated by a small number of large firms which had higher than average productivity, were 'more likely to invest in intangible assets such as patents and software' and gained market share at the expense of firms with low mark-ups and lower productivity.

This would suggest that markets have fundamentally changed since 2000 allowing the most innovative and productive firms, with high levels of intangible assets such as technology, customer databases, technical and managerial skill and network effects, to increase their market share to the point of dominance.

In other words market power isn't necessarily the result of less competition. Jeffrey Meli, head of research at Barclays, suggests that if anything more open markets have intensified competition which 'has tilted the playing field, allowing the most productive firms to capture sales from their less efficient rivals' and forced the least efficient out of the market altogether.

A key aspect of the 'winner takes most' narrative is that even small competitive advantages can lead to an increase in market power. New forms of technology, slightly more efficient supply chains and more streamlined processes can all add to a firm's market power.

Source: Barclays | Equity Gilt Study 2019

WHAT DOES IT MEAN FOR INVESTORS?

For investors who have backed Amazon, Google and Microsoft – firms with seemingly unassailable market power – the returns have been outstanding. However, as concern over the reach of these corporate giants grows among policymakers and regulators, the risks are increasing in tandem (read this discussion about the rise of regulatory scrutiny).

The IMF suggests that 'with mounting risks of adverse growth and income distribution effects from rising corporate power, policymakers should keep future market competition strong'. It suggests cutting barriers to entry in trade and services and allowing lagging firms to catch up on technology.

It also warns that mergers and acquisitions (M&A) typically result in 'significantly higher mark-ups' and that structural reforms are needed to prevent dominant firms from 'entrenching their positions by erecting barriers to entry'.

All of which sounds like a call for more, not less, supervision of firms with dominant market power and greater scrutiny of M&A deals going forward.

By **Ian Conway**
Senior Reporter

STREAMING THE FUTURE

Tom Slater on tomorrow's opportunities

The value of your investment and any income from it can go down as well as up and as a result your capital may be at risk.

Following a meeting with Amazon boss Jeff Bezos in Seattle, Tom Slater considers the online giant's prospects in the changing world of new media.

In the past Scottish Mortgage has drawn a distinction between offline and online media but as the issues have moved on, so has our portfolio, Today Amazon and Netflix along with Tencent, Alibaba and Spotify dominate our media exposure.

We see the decline of the traditional media industry accelerating. ESPN, the sports TV channel and powerhouse of the US cable industry, peaked at 100 million subscribers in 2011. Since then that number has fallen by 14 per cent. Disney's 2018 purchase of 21st Century Fox and Comcast's purchase of Sky, also last year, illustrates the kinds of market pressure this is creating.

Since peak ESPN, Netflix has grown from 25 million subscribers to 137 million today. It is spending close to double what the biggest traditional media companies spend on content and customers are voting with their eyeballs. As many as 45 million households watched Netflix's horror thriller Bird Box in its week of release, more than twice the total number of cinema tickets sold that week in North America for all films.

Even some of our best-loved programmes have made the shift too. Amazon poached the trio of hosts from the BBC show Top Gear in 2015, producing The Grand Tour for Prime Video a year later.

With the industry in flux, it is understandable why this area is such a priority for Jeff Bezos. Amazon spent just under $5 billion on content

last year, signing Jen Salke from NBC as the new head of its studios business. As Amazon is data-driven, this outlay is motivated by data derived from customer spending patterns. When a Prime member watches their first piece of content on Prime Video, they become a much more committed Prime member. Renewal rates improve.

This brings us back to Amazon's business model advantage: it doesn't have to make money right away. Spending on content sells more product. And in the age of on-demand viewing, channels no longer compete for audience share at a particular time of day. All the competition is for the talent that creates unmissable content.

Music streaming is another area where Amazon has focused attention. The Amazon Music service competes with Spotify, giving users the opportunity to stream their favourite tracks and albums. As with Prime Video, the attraction for Amazon is to offer yet another channel of compelling content that will draw users into their ecosystem. It offers discounts for subscribers to Prime or for those who plan to play their music through an Echo device. In a recent article discussing the Amazon's digital assistant, we touched on the potential of voice-driven content search and discovery. The cut-price music subscription when played through an Echo device shows the importance Amazon places in the development of Alexa.

I mentioned Spotify, which is still the market leader in music streaming. But original content production is just as important to the Swedish company. Its recent acquisitions of Gimlet Media and Anchor – both podcast-related businesses – are a testament to that. By taking control over the creation of original audio content, it can better balance the revenues directed to record labels as its business grows. There was positive news for Spotify in March as it released its service in India. With over a million users added in the first week, there is significant potential to add users incrementally from India's vast population of over a billion people.

But competition for content is not just coming to our video screens and headphones. The gaming industry continues to grow, and in the UK, it is now bigger than the music industry and video industry combined. The British-made Grand Theft Auto franchise holds the record as the most financially successfully media title of all time. It is a trend that Netflix CEO Reed Hastings knows all too well, noting in a recent investor call: "We compete with – and lose to – Fortnite more than HBO". Fortnite is the popular online video game developed by Epic Games, where another portfolio holding Tencent has a controlling interest.

Amazon is also active in the industry through its gaming streaming-platform Twitch, which it bought five years ago for $1bn. A few years earlier, Facebook paid a similar price for Instagram, now a hugely popular platform with over one billion users. More than ten million people log-on to Twitch every day and the number of viewer hours on its platform totalled over nine billion in 2018, 50 per cent more than the National Football League (NFL) gets each year. Twitch streams the feats of gamers to an engrossed audience, in the same way Instagram 'influencers' post photos and videos to their followers. Streamers charge subscriptions to their channels with advertisers happy to pay for such valuable screen time during streaming breaks.

It is still early days for Twitch, but it is an example of the prescience of Jeff Bezos and that preference he told us about for "spending most of [his] time in the future". Gaming has been a popular pastime for decades, but the Twitch business model has only become viable recently, as improving computer processing power and faster network speeds – combined with the rise of social networks – facilitate seamless streaming of content to desktop computers and mobile phones.

In other words, there is a revolution happening within the media industry, and Bezos is more likely than most to have seen it coming many years ago.

Tom Slater
Tom graduated BSc in Computer Science with Mathematics from the University of Edinburgh in 2000. He joined Baillie Gifford the same year and worked in the Developed Asia and UK Equity teams before joining the Long Term Global Growth Team at the start of 2009. Tom became a Partner in the firm in 2012. Tom was appointed Joint Manager of Scottish Mortgage Investment Trust in January 2015 having served as Deputy Manager for the previous five years. In 2015 Tom was appointed Head of the US Equities Team and is a decision maker on Long Term Global Growth portfolios. Tom's investment interest is focused on high growth companies both in listed equity markets and as an investor in private companies.

BILLION DOLLAR STOCKS

SHOULD YOU INVEST IN THE BIG NAMES JOINING THE MARKET?

We're seeing a large number of high profile companies join, or plan to join, the stock market in 2019. The catch is that they are choosing the main stock exchanges in the US rather than listing in the UK.

That isn't generally a problem in terms of getting access as most UK stockbrokers and investment platforms let you buy shares in overseas-listed companies.

The real issue is whether you should want to invest in the likes of Uber, WeWork, Pinterest and Lyft, all of whom are big names offering retail investors the chance to buy their shares once they hit the market.

These are all fast-growing businesses either disrupting industries or creating new ones. On paper they are exciting with bold ambitions to keep driving up sales. While the majority earn large amounts of revenue, nearly all are loss-making.

Buying their shares would mean having faith in them achieving growth goals. Some of the companies will need significant amounts of new cash to help them on their path to positive earnings. Others need to overcome significant regulatory or legislative hurdles which threaten to derail their sales momentum.

WHAT TO LOOK FOR

Being a 'hot' name with fast growth is not enough to warrant making an investment. You need to think about financial strength, competition, other risks, and also question why existing backers want to use the stock market listings as a partial or full exit. After all, has the easy money already been made?

Most of these new stock market floats are companies previously backed by venture capital funds or private equity. The fact that numerous so-called 'unicorns' – start-ups valued at more than $1bn – are now coming to the market would suggest the current backers are seeing an opportunity to cash out while the going is good.

'We have had a dearth of tech IPOs (initial public offerings) in recent years as the so-called unicorns have got fat on private equity money. Now those same investors want to realise their investment and that's where I see the risks,' says Richard Holway, analyst at TechMarketView.

'We should remember that in the dot.com bubble of 1999/2000 the majority of companies that floated either failed or were bought out at fire-sale prices over the next three to five years. I suspect a similar fate awaits many of the current IPO crop.

'BUT we also had a few mega stars. Again I expect there will be a few of the current IPO crop that will shine brightly too,' he adds.

THE NEXT BIG THING

Jake Robbins, fund manager of **Premier Global Alpha Growth Fund (B6740K6)**, also believes the big tech unicorns are taking advantage of strong equity markets to go public. 'It's only natural that investors are seeking to identify the next big thing that could join the $1trn club,' he says.

'Investing in some of these companies requires quite a leap of faith that selling services or goods at a loss can one day create a network that can support real profits.

'Clearly if it can't then they won't be able to support any kind of valuation let alone the sky high prices currently being bandied around. For those companies that do succeed then their investors will be phenomenally well rewarded, but for the many that fall by the wayside current valuations will, with the benefit of hindsight, look very much like an investment bubble,' add Robbins.

UK INVESTORS FLOCK TO US STOCKS

US-listed stocks are popular among UK investors, according to investment platform provider AJ Bell Youinvest.

For example, more of its customers hold shares in Tesla than classic British companies **Whitbread (WTB)**, which owns the Premier Inn hotel chain, and retailer **Next (NXT)**. Other US-listed stocks widely held among AJ Bell Youinvest customers include Amazon, Facebook and Netflix.

Tesla is popular with UK investors

HOW DO YOU BUY AN OVERSEAS-LISTED STOCK?

Buying a stock listed on an overseas exchange such as New York or Nasdaq is relatively easy, assuming the company is large and liquid enough.

You buy the shares in the same way as you would for a UK-listed stock. The only extra bits to consider are foreign exchange charges which can be up to 1% for dealing and potentially 0.5% fee to convert any dividends into sterling.

For US-listed shares, you will need to complete a W-8BEN form which will be available from your investment platform provider.

OFF TO THE RACES

It helps that investor sentiment in the US is being supported by markets trading at record highs, thus making it relatively easy for companies to be confident about floating.

Many of the recent unicorn floats have soared on their first day of trading including video conferencing firm Zoom Video Communications which jumped by 80%. Online scrapbook Pinterest floated at $19 a share on 18 April and two weeks later it was trading at $31.23.

Lyft initially did well, rising by 25%, but has since pulled back and is now trading 18% below its listing price. Its disappointing performance on the stock market is a good illustration of why you shouldn't get caught up in the hype around all the unicorn companies.

DISRUPTOR FATIGUE?

We sense that many investors are getting tired of

18+

WHAT IS AVAXHOME?

companies claiming to be market disruptors. There is an increasing shift among long-term investors back to companies which make positive earnings as they believe 'profit is better than promise', to borrow a phrase from a recent article in the *Evening Standard*.

This is a good reason why we believe Airbnb stands a better chance of generating good returns for investors than Uber – the former already makes a profit and the latter has no idea when its earnings will turn positive. However, you also need to factor in valuation for any company and not simply pick the profitable ones.

Many fund managers like to wait until a company has been trading on the stock market for some time before considering an investment. They want to see how the market has reacted to the stock, as well as how the management have performed in the public spotlight.

You may argue that waiting means missing out on potential gains, yet a good company should still be able to generate positive returns for shareholders over time.

Furthermore, it also means you avoid the initial period where many people like to trade in and out on stock market floats. You often see a pattern in the share price where an IPO rises, falls back as traders bank profits, and then rises again as longer-term investors take positions.

IPOS TO BUY OR AVOID

Of the recent batch of new stock market entrants, we like the look of Beyond Meat for significant earnings growth potential albeit recognise that it is very highly valued. We are cautious towards Uber as costs are ballooning and its bigger-picture plans to be a mobility champion are likely to require very large amounts of investment.

Among future potential stock market listings, Airbnb looks the most interesting as an investment, assuming its valuation isn't excessive. Palantir is also a fascinating business but we're lacking detailed financial information at present. Avoid WeWork's parent We Company which is listing later this year.

If you don't want to risk your money on individual stocks, it is worth considering there are plenty of investment trusts and funds with access to these types of fast-growth businesses thanks to being able to invest in unquoted companies. For example, **Scottish Mortgage (SMT)** already has stakes in Airbnb and Palantir, alongside more mature companies.

2018 IPO SUCCESS STORIES

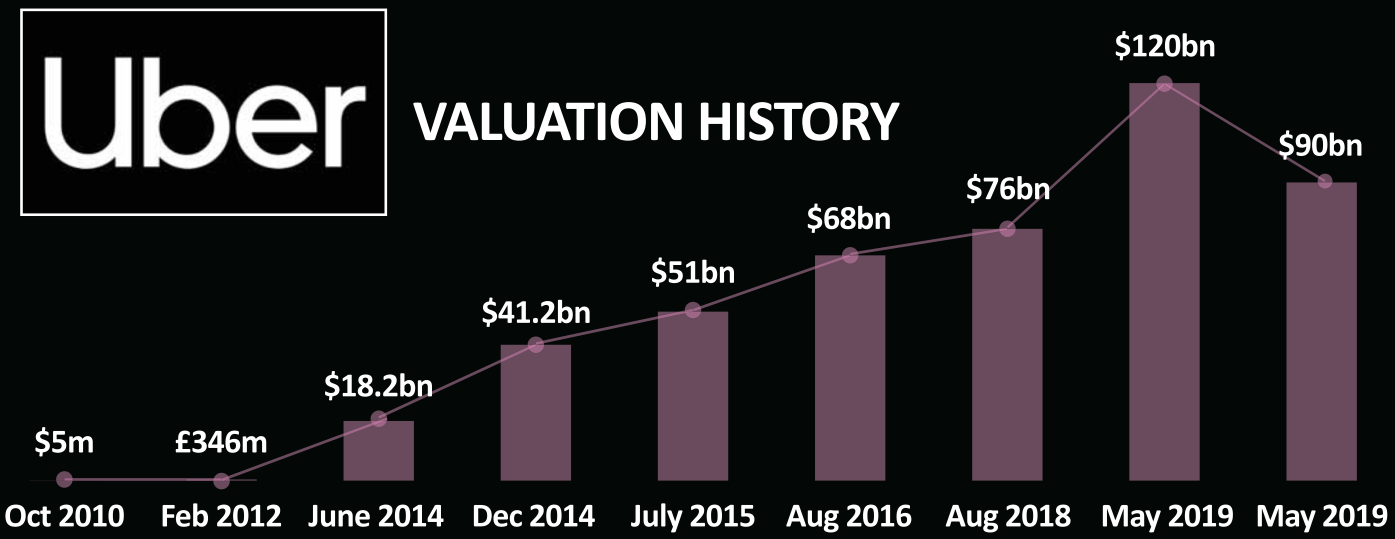
Last year saw some spectacularly successful US technology stock market floats. The best performer was cyber-security firm Zscaler, which went public in March 2018 at $16 per share with a valuation of $1.9bn.

By the end of the year the shares had gained 160%, valuing the business at almost $5bn. This year the shares have gained another 80%, giving the company a value of almost $9bn.

Having racked up quarterly losses of $5m to $10m, Zscaler is slowly moving towards making a profit although it isn't there yet.

The next-best performing public offering was Elastic which powers the searches which connect ride-share customers with drivers at Lyft and Uber and which connect lonely-hearts on dating app Tinder.

Elastic floated at $36 per share in early October and on the first day of trading the shares soared 94% to $70, giving the company a valuation of $5bn. By the end of the year the shares were up 115%, and since the start of 2019 they have added a further 25%. That makes the total shareholder return so far 135% and values the business at $6.2bn even though it still hasn't turned a profit.



Source: Shares, public information

WHAT IS THE GAME PLAN?

Uber wants to grow in areas such as electric bikes and scooters, freight and self-driving vehicles, as well as its core ride-hailing and food delivery interests.

In less than 10 years Uber has extended its service to over 700 cities on six continents, making 14m trips every day.

Yet it still accounts for less than 1% of all miles driven globally every year, and only a small proportion of people in countries where the service is available have ever used it.

Uber believes that the total addressable market is 11.9trn journeys a year which equals a market worth $5.7trn.

In theory it can keep on expanding into this market while its in-house technology and network of connected consumers, drivers, restaurants, carriers and shippers gives it the ability to grow in new markets like food delivery and logistics.

So far investment needs and payments to drivers – which by the end of last year totalled $78bn – mean that it continues to run big losses.

WHO IS THE COMPETITION?

On the travel side its principal competitor is Lyft as well as traditional taxis and public transportation. **Just Eat (JE.),** Delivery Hero, Deliveroo and GrubHub are among the names competing against Uber to deliver food to your home.

DOES IT MAKE A PROFIT?

No. Uber lost $3bn last year and net losses for the first quarter this year are estimated to be $1.1bn.

WHAT ARE THE KEY RISKS?

First and foremost, valuation. Second, regulation. Uber treats its workers as independent contractors but costs could go up a lot if they had to classify them as employees.

Investors may look at Amazon, which ran losses for decades as it invested in its business yet still made its early shareholders rich beyond belief, and assume that Uber will do the same.

However Uber is betting on one thing to be profitable: driverless vehicles. A fully autonomous fleet would be available 24/7, would offer safer, more efficient rides for customers but most crucially would save it tens of billions of dollars.

As seductive as the idea is, large-scale deployment of autonomous vehicles is a long way off meaning Uber is set to continue racking up losses for many years to come.

SHARES SAYS: This IPO is strictly for high risk-takers only. It is expected to float on 10 May.

wework

WHAT IS THE GAME PLAN?

The We Company uses the WeWork brand to provide shared workspaces for smaller, often start-up companies that cannot afford a large initial office, as well as property services for firms of all sizes, from freelancers upwards. The firm has also opened other divisions, such as WeLive (apartments) and WeGrow (schools).

WHO IS THE COMPETITION?

Regus – owned by **IWG (IWG)** – is the major player in the business of offering co-working, shared office space. ImpactHub, founded six years before The We Company in 2011, is also building a strong global community while there are also lots of local options, including Convene in the US. Freelancers also have the option of working at home and bigger firms can use premises offered by more traditional landlords or buy their own property.

DOES IT MAKE A PROFIT?

No. For a nine-year old firm, its 2018 results were almost embarrassing as net losses of $1.9bn outstripped sales of $1.8bn. Sales may have doubled, but so did the losses.

WHAT ARE THE KEY RISKS?

A $6bn cash pile gives The We Company time to work on its strategy but its bonds are already rated junk by the ratings agencies who clearly see the firm as a risky proposition thanks to its losses.

The firm is diversifying into new areas before its core area is profitable. Any economic downturn could lead to tenants cutting back on space or going bust and there is no shortage of competition.

SHARES SAYS: Avoid. The financials tell a worrying story.

slack

WHAT IS THE GAME PLAN?

Slack aims to take online messaging to the next level by providing a software platform that workers can use to share information in one place, making collaboration easier, so customers get a better service. It has more than 10m daily active users worldwide.

WHO IS THE COMPETITION?

The main competition is email, which most firms and workers still use as their prime form of communication. Microsoft Team, Facebook Workplace, Alphabet's own chat system and Cisco are all directly comparable rival services.

DOES IT MAKE A PROFIT?

No. It generated $400m revenue in the year to 31 January 2019 and made a $138m pre-tax loss.

WHAT ARE THE KEY RISKS?

Slack is six years old and has a relatively limited revenue base. Its core service is offered for free and customers then pay for additional features, so there is a risk that companies do not upgrade and stick with what they know (which is email) – people and firms can be resistant to change. Slack also faces lots of competition from bigger, well-funded rivals.

SHARES SAYS: Users of Slack talk very highly of its services which is promising. Its challenge is to get more people to pay to use its messaging platform. Definitely worth a look.

airbnb

WHAT IS THE GAME PLAN?

Having cracked the short-term rented accommodation market, Airbnb's ultimate plan is to have an end-to-end travel platform that will handle every part of a trip. More than half a billion people have so far stayed in homes, yurts, treehouses and more via its platform, and hosts offering accommodation have earned more than $65bn.

WHO IS THE COMPETITION?

These include traditional accommodation providers such as hotels, travel agents and bed and breakfast operators, as well as websites like Booking.com and TripAdvisor.

DOES IT MAKE A PROFIT?

The company says it has made a profit for the past two years on an EBITDA (earnings before interest, tax, depreciation and amortisation) basis, although it does not disclose any figures.

WHAT ARE THE KEY RISKS?

Regulators are cracking down on Airbnb in various parts of the world including restrictions in places likes Paris and Amsterdam on the number of nights a home can be offered via its platform.

SHARES SAYS: The business is well-established and already has considerable scale. This is one of the more interesting names to watch for a forthcoming IPO. Get ready to buy, assuming the valuation isn't excessive.

Palantir

WHAT IS THE GAME PLAN?

Palantir is a data analytics group that makes people better at doing important work, such as battlefield intelligence systems for soldiers. It is involved in a lot of activity for government agencies as well as corporates such as United Airlines. The plan is to grow its position across the public, private and not-for-profit sectors.

WHO IS THE COMPETITION?

Mu Sigma, Splunk and Tableau are considered to be key competitors to Palantir. However, the broader big data and analytics space is also very crowded.

DOES IT MAKE A PROFIT?

We don't know as Palantir has been very secretive about its finances.

WHAT ARE THE KEY RISKS?

Palantir is considered to be heavily reliant on government contracts which exposes it to the risk of public sector budget constraints. A stock market float may not give investors detailed company information as much of its work is likely to be highly classified.

SHARES SAYS: We await IPO details with interest. Its business is fascinating but the financials and projects are surrounded by mystery.

RECENTLY LISTED

Pinterest

WHAT IS THE GAME PLAN?
Pinterest is an online scrapbook which people view to find inspiration for their lives. It makes money from a range of different advertising formats. Growth is ‘pinned’ on making it easier for users to buy things they like, developing new features for specific industries such as automotive and travel, and having deeper relationships with brands, retailers and content creators.

WHO IS THE COMPETITION?
Pinterest argues that it is unique, however you could argue that Instagram, Facebook and Snap are competitors.

DOES IT MAKE A PROFIT?
No. It made a $63m net loss in 2018.

WHAT ARE THE KEY RISKS?
It is still in the very early stages of trying to monetise its platform and is heavily dependent on advertising. The company was founded in 2009 and hasn’t really been through a difficult period for the global economy, so it is hard to say if its business model is resilient enough to survive a sharp economic downturn. It needs to attract more advertisers, increase scale with existing advertisers and offer more advertising products, otherwise it may find it hard to sustain revenue growth.

SHARES SAYS: Pinterest doesn’t come across as having the right qualities for a business with everlasting appeal.

BEYOND MEAT

WHAT IS THE GAME PLAN?
Beyond Meat’s timing is perfect. It has floated on the stock market precisely at the time when demand for plant-based meat substitutes is really taking off. That might explain why so many investors rushed to own the stock on the first day of dealings (2 May) where the shares jumped by an incredible 163% to $65.75.

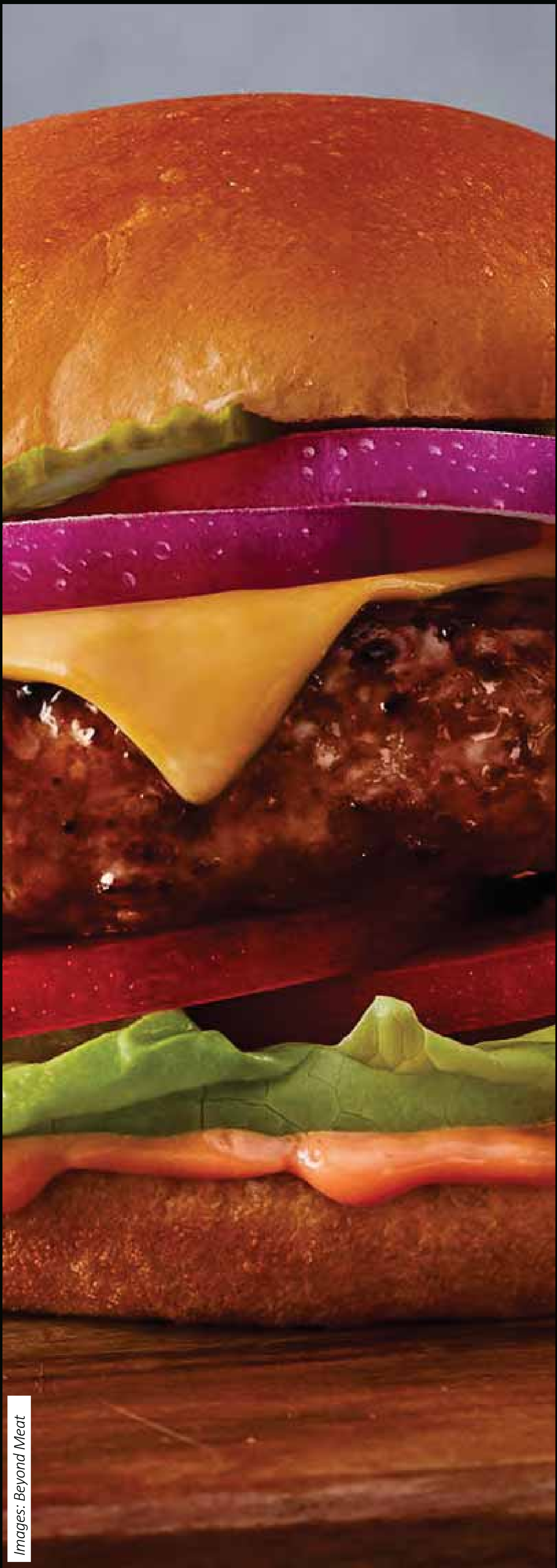
Consumers are turning their back on meat for cost, health and environmental reasons. That’s led to growing demand for plant-based food – importantly this demand is quite widespread rather than simply coming from people who don’t eat meat.

Many people have opted to reduce the amount of meat in their diet and switch to vegetarian or vegan food several days a week or on an ad-hoc basis. This presents an opportunity for Beyond Meat to sell to a mainstream rather than a niche audience.

The company’s ‘Beyond Burger’ product is designed to look, cook and taste like traditional ground beef. It has done a fantastic job of getting its products in stores across the US and now overseas, and brand awareness is strong enough for its name to prominently feature on menus in restaurants, hotels and other food outlets.

Growth plans include setting up production capabilities in Europe next year and expanding across Asia.

WHO IS THE COMPETITION?
Impossible Foods (which is now supplying Burger King in the US), Hungry Planet and Next Level Burger are among the main competitors, yet you also have big companies such as **Unilever (ULVR)** getting in on the act. Unilever last year bought meat-free food company The Vegetarian Butcher and Nestle is using its Garden Gourmet brand to also capitalise on the same market.



Images: Beyond Meat

DOES IT MAKE A PROFIT?

It made an estimated $8.5m gross profit in the first three months of 2019 but incurred a $2m loss from operations. In 2018 it made $87.9m revenue and a $29.9m pre-tax loss.

Beyond Meat warns that operating expenses and capital expenditures will increase substantially in the foreseeable future as it invests to increase its customer base, supplier network and co-manufacturing partners. It also flags plans to spend money on marketing, distribution and manufacturing facilities, hiring more staff and boosting its technology and production capabilities.

WHAT ARE THE KEY RISKS?

It relies on a limited number of raw material suppliers and adverse weather conditions hurting crop yields could have a major negative effect on its earnings. It has already experienced interruptions with the supply of pea protein.

Beyond Meat has done a good job getting its products into stores but that also means competitors will be thinking hard about how to do the same thing. Copycat products are a major risk, particularly as Beyond Meat is probably too young a business to command brand loyalty.

Another key risk is working capital requirements. The company says existing cash will last it for another 12 months or so – beyond that it may need to raise new cash.

SHARES SAYS: Competition is tough but we're encouraged by Beyond Meat's progress and believe its earnings growth trajectory could be very good over the coming few years. We accept that the valuation is very high at $3.8bn but believe it has the right ingredients to do well. Treat this as a stock to own as a bit of fun alongside an existing diversified portfolio, rather than risking all of your money on it. The downside of having such a high valuation is that the stock is priced for perfection – any mistakes and the share price could collapse. Long-term investors who focus on fundamentals may not be able to justify paying top dollar when revenue is relatively small.

lyft

WHAT IS THE GAME PLAN?

Lyft wants to keep growing, and establish itself as a leading player, in areas such as ride-sharing services, electric bikes and self-driving vehicles and continue to develop its platform so that it offers services that cover a wide range of transport.

WHO IS THE COMPETITION?

On the car ride-sharing side Uber is the principal competitor in the US while Uber and Jump are rivals in the bike-sharing and scooter markets. Travellers also have the traditional options of using their own cars, taxis and other forms of public transportation. There is a long list of rivals in autonomous driving, including Alphabet's Waymo project, GM Cruise, Tesla and a range of Chinese, Japanese, European and Korean development programmes.

DOES IT MAKE A PROFIT?

No. In 2018, Lyft provided 619.4m rides and generated $2.2bn in sales but it lost $911m, or $1.47 for every ride it offered.

WHAT ARE THE KEY RISKS?

Competition is intense. Riders could press for higher pay, so any legal changes relating to the gig economy may be crucial. Its research effort in autonomous vehicles may not pay off. And the company continues to make substantial losses, with a profit looking very unlikely for several years to come.

SHARES SAYS: Avoid. The risks look very high versus the potential rewards from an investment. Its aspirations are admirable but this is not a stock for the faint-hearted.

zoom

WHAT IS THE GAME PLAN?

Zoom wants to offer a seamless, cloud-based video-oriented platform that makes communicating easier, so less time is wasted travelling to and from meetings and companies can work more efficiently.

WHO IS THE COMPETITION?

Zoom has a long list of rivals that includes Google, Cisco, Microsoft, TeamViewer and Polycom. Business people may also still prefer to travel to a face-to-face meeting.

DOES IT MAKE A PROFIT?

No. In 2018 the company broke even, as sales more than doubled to $331m.

WHAT ARE THE KEY RISKS?

Zoom faces lots of competition and quality of service is paramount – any technical failures with its cloud-based infrastructure or the internet more generally could compromise the quality of its service and reputation. Companies could delay trying, buying or upgrading its services if times get tough and money becomes tight.

SHARES SAYS: The stock has doubled in value since joining the market on 18 April. While investors have been happy to pay top dollar to get a slice of the business, we don't share their enthusiasm.

By **Daniel Coatsworth, Ian Conway and Russ Mould**

Why there may never be zero-fee ETFs in the UK

Products that don't include a levy emerge in the US but are not crossing the Atlantic

Exchange-traded funds (ETFs) that don't charge a fee can sound too good to be true, and for people in the UK this may well turn out to be the case.

Zero-fee ETFs, as the name suggests, are funds that do not come with any product charges.

Fidelity was the first company to offer zero-fee ETFs when it launched four index funds last year with what it calls a 'zero expense ratio', whereby no management fees, service fees, and other things like transaction costs are charged.

While other providers are also planning to launch zero-fee ETFs, all of them, including Fidelity's products, are only available in the US.

The ETF market is more developed in the US than in the UK and so American providers are able to keep costs lower in a way European firms aren't able to, according AJ Bell's head of passive portfolios Matt Brennan.

However, it is worth noting many investment platforms will allow you to trade US-listed securities.

US ALWAYS ONE STEP AHEAD

The US market for ETFs has always been regarded as one step ahead of the UK, with innovation mostly taking place in America first. The first ETF ever launched was available to investors in the US in 1993, while UK investors had to wait until 2000.

> "DON'T BE BLINDSIDED BY THE CHARGE. THERE ARE SOME VERY LOW COST OPTIONS FOR UK INVESTORS ANYWAY"

Brennan says the likes of Fidelity are able to launch zero-fee funds because they themselves can create the indices that will be tracked, which helps them keep costs low.

'On a FTSE 100 ETF for example, a large part of the fee goes to the index provider – FTSE, MSCI, etc – but in the US, the big firms can create their own index and that can lower the costs of an ETF by one, two or three basis points,' he explains.

European providers like Legal & General Investment Management and Amundi already have low cost ETF ranges, with some funds costing as low as 0.04% and 0.05% respectively.

They have been able to lower costs in part by moving away from following some FTSE and MSCI indices and instead using ones from independent providers like Solactive,

something which Brennan says is a clear indication that following a well-known index makes up a big part of the fee for some of these ETFs.

But being able to create their own index still eludes most ETF providers.

DIFFERENT RULES

A major incentive for companies in launching zero-fee ETFs comes from stock lending. Short-sellers pay a fee to borrow shares from fund companies, which means there is a viable business model for zero-fee ETF providers in the US.

Such ETF providers are likely to gather a lot of assets thanks to having zero fees meaning they have more money to buy shares, and therefore more shares to lend out. For example, Fidelity's zero-fee Total Market Index fund pulled in $2.1bn in six months.

These stock lending rules don't apply in the UK, notes Adam Laird, Lyxor's head of ETF strategy for northern Europe, meaning fund managers can't keep the fees they make from lending shares to short-sellers. Instead they have to put it back into the fund.

On this basis, Laird believes we won't ever see zero-fee ETFs in the UK. 'A fund's operating expenses need to be paid. If it's going to be viable it needs to make money somehow,' he says.

NEED FOR TRANSPARENCY

Laird doubts there would be enough demand in the UK for such products anyway, given our different investment mindset compared to investors in the US.

'We want to know how an investment is being paid for. In the UK, we know that if it looks too good to be true, it probably is. But in the US, investors put more scrutiny on cost and are maybe less conscious on the risk element,' he explains.

Brennan on the other hand thinks at some point down the line we could see zero-fee ETFs hit the UK market, though that will rely on companies being allowed to keep the fees from lending out shares.

'There's a lot of different dynamics in the market in Europe, but as it grows and if regulation isn't adapted (to stop providers keeping fees from stock lending), there's no reason why we couldn't see zero-fee ETFs in the UK,' he says.

One thing they both agree on is that looking at the fee should always be only one aspect of choosing a fund.

DO NOT FOCUS EXCLUSIVELY ON COST

'Don't be blindsided by the charge. There are some very low cost options for UK investors anyway, but you need to make sure the investment is right for your portfolio and objectives,' warns Laird.

Brennan adds that the ETFs' performance is also an important factor, as even with a supposedly free ETF you could be paying for it in ways that aren't immediately clear.

'Focusing on the fee is a bit of a red-herring,' he says. 'If an ETF costs 0.2% but it always beats the benchmark by 0.3% each year, then it's outperforming by 0.1%. But if you have a zero-fee ETF that's performing 0.1% behind the benchmark, then you're effectively paying 0.1% on that fund.'

By **Yoosof Farah**
Reporter

Grab global growing dividends with Securities Trust of Scotland

The investment trust yields 3.5% and pays big attention to ESG factors

'We go global to hunt down the best, most sustainable income ideas,' says Mark Whitehead, manager of the quarterly-dividend paying **Securities Trust of Scotland (STS)**.

This is an investment trust generating a geographically diverse source of income from a carefully selected cohort of high quality businesses.

With average retirement in the UK expected to last 19 years, this trust should be front of mind for savers seeking to accrue a reassuringly large pension pot and protect their income against inflation.

Securities Trust of Scotland is in fact one of *Shares'* running *Great Ideas* selections and we recently jumped at the chance of a catch-up with the manager, Martin Currie's head of income Whitehead, in order to check up on the progress of the portfolio. Read our original article here.

NOT BENCHMARK DRIVEN

The fund's objective is to achieve rising income and long-term capital growth through a balanced portfolio of global equities; this is a focused 35 to 55 stock portfolio that is unconstrained by geography, sector, stock or market capitalisation.

Whitehead prefers the term 'benchmark agnostic' to 'unconstrained' and benefits from the flexibility to invest in his best ideas from around the world.

A global equity income portfolio provides more choice than a country specific income portfolio and avoids the risk of income concentration.

All the stocks in the portfolio, well diversified across sectors and countries, should exhibit a combination of attractive dividend yield and dividend growth.

'The trust was really set up as a savings solution and the main objective is to produce a high income, and grow that income stream at least in line with inflation,' explains Whitehead.

He believes savers 'need to buy a trust that has global exposure because global will outperform and you really need to own more equities –

TOP TEN HOLDINGS (As at 31 March 2019)

Company	Portfolio weight (%)
Microsoft	5.5%
WEC Energy	4.0%
Procter & Gamble	3.9%
Merck	3.9%
Air Products & Chemicals	3.8%
Sanofi	3.5%
Zurich insurance	3.4%
Crown Castle	3.4%
Koninklijke DSM	3.3%
Taiwan Semiconductor	3.2%

WEC Energy features in Securities Trust of Scotland's portfolio more "growth assets" – in your portfolio.'

At pains to point out the risk of purchasing stocks purely for high yields, since these are often the precursor for a dividend cut, he says: 'What I try and do is invest in growth companies. We really believe high quality businesses that are able to generate strong and sustainable returns on invested capital are often managed well, they are high quality companies that will generate strong dividend growth and they are committed to that dividend.'

MARTIN CURRIE – AN ESG LEADER

Whitehead's robust investment approach involves proprietary screening of stocks, detailed evaluation of companies and includes credit analysis to determine the sustainability of cash flows and the ability of the balance sheet to withstand adverse scenarios.

ESG (environmental, social and governance) factors are an essential input into his investment management process, because he believes that positive behaviour exhibited by companies in these areas will add shareholder value over the longer term.

Stewardship factors are an integral part of Martin Currie's investment philosophy and process and the investment manager has been a signatory of the Principles for Responsible Investment (PRI) since 2009.

'We integrate ESG all the way through our investment process,' insists Whitehead. 'When we're looking at a company, all the time we are asking questions – do we think the management is high quality? Are they investing sustainably? We talk to management teams all the time about their sustainable footprint.'

NUMBER OF HOLDINGS: 44

YIELD: 3.5%

One portfolio example is Dutch health, nutrition and materials multinational DSM, offering exposure to the structural growth themes of nutrition, health and sustainable living.

'DSM has put together a bank debt with a syndicate of banks and the coupon that they have to pay is directly linked to their carbon emissions,' explains Whitehead. 'So if they hit their targets to lower emissions, then they have to pay less for that debt. It is good for the profit and loss.'

Whitehead is also able to generate additional income for the trust by selling derivative contracts known as 'puts' in the stocks on his buy list.

By selling a put option Whitehead essentially takes on an obligation to an option buyer to buy the security at a predetermined price, which is typically lower than the prevailing share price.

Part of the reason this is lucrative is thanks to the put options market predominantly being used by investors who buy put options as an insurance policy for stocks they already own and whom are willing to pay a large premium to guarantee a set sale price for their stock in volatile markets.

DEDICATED TO DIVERSITY

Diversified by country and industry, Securities Trust of Scotland also holds the likes of healthcare giant Merck, owned for its superior market positioning in immuno-oncology and other growth-orientated products, as well as UK clay brick maker **Ibstock (IBST)**, viewed by Whitehead as a play on structural demand for housing.

Also in the portfolio are US-listed consumer goods powerhouse Procter & Gamble and food conglomerate Danone, the yoghurt maker which has made a number of acquisitions in recent years including WhiteWave Foods, a deal adding a new growth dimension in international plant-based products.

BAD APPLE?

Among Securities Trust of Scotland's recent sales is iPhone maker Apple, despite the company jockeying for the title of most valuable US company with Amazon and Microsoft, in a demonstration of the manager's strict sell discipline amid concern over its growing reliance on services revenue.

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

LIMP US TECH REPORTING SEASON IMPACT ON UK INVESTMENT TRUSTS

A RELATIVELY impressive first quarter of 2019 for many of the world's largest technology companies (Google parent Alphabet aside) has failed to move the needle of the three investment trusts most exposed to the technology stocks.

Shares in **Allianz Technology Trust (ATT)**, **Polar Capital Technology Trust (PCT)** and **Scottish Mortgage Investment Trust (SMT)** have barely budged since Amazon and Microsoft got the ball rolling in late April.

Yet year-to-date performances have been strong for the trio. The Allianz, Polar and Scottish Mortgage trusts have an average share price return of 23% so far this year, led by Allianz's impressive 33% rally.

TEMPLETON EMERGING MARKETS LOOKS TO APPEASE INVESTORS

INVESTMENT TRUST **Templeton Emerging Markets (TEM)**, which currently trades at a 10% discount to net asset value (NAV), says it will hold a tender offer in five years' time if the performance over the period falls short of the benchmark.

This would allow shares to be sold back to the trust at NAV minus 2%. The offer is subject to both 2019's and 2024's continuation votes being approved. Largest shareholder City of London has committed to voting in favour of continuation in July.

BlackRock star manager Prentis to retire this summer

Mike Prentis will step down as manager of **BlackRock Smaller Companies Trust (BRSC)** at the company's June AGM, calling time on a distinguished 32-year fund management career.

Prentis has managed the fund since August 2002, originally at 3i Investments, then for 14 years at BlackRock. Under his stewardship, the portfolio has delivered sparkling NAV total returns of 957% or 15.3% per year, substantially outperforming the 530% (11.8% per year) from the Numis Smaller Companies ex-Investment Companies index.

Co-manager Roland Arnold becomes the lead manager following the AGM and will continue to use Prentis' tried-and-tested quality growth bias approach.

Prentis' departure is no major surprise given his lengthy tenure and the early 2018 management handover of **BlackRock Throgmorton Trust (THRG)** to Dan Whitestone.

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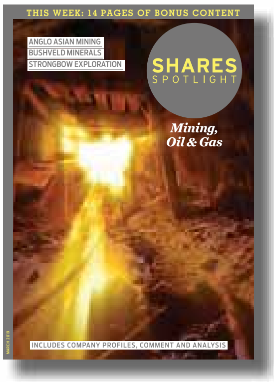
ECSC
Speaker: IAN MANN, CEO
ECSC (ECSC) is a full-service cyber security information provider, specialising in 24/7/365 security breach detection and artificial intelligence.

OPG POWER VENTURES
Speaker: Dmitri Tsvetkov, CFO
OPG Power Ventures (OPG) is a developer and operator of power generation plants in India.

PCF BANK
Speaker: Scott Maybury, Chief Executive
PCF Group (PCF) is a long established bank, whose shares are quoted on the AIM market of the London Stock Exchange.

BONUS CONTENT

Have you seen our quarterly Spotlight supplements?



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Time to abandon funds on a road to nowhere

How to spot sub-scale funds that aren't attracting new money

Small funds that have high fees and haven't seen new investors for years account for around a quarter of all funds sold in Europe, new research has found.

So-called 'orphan' or 'zombie' funds are those that have failed to reach scale (or previously reached scale and then saw massive outflows) and haven't seen any significant inflows for years. They are the forgotten funds that need dusting off, and in many cases closing down.

Because they are smaller than their counterparts they tend to charge high fees, as there are no economies of scale, meaning that a small number of investors have to bear the costs of running a fund.

WHY DOES THIS SITUATION OCCUR?

There are a large number of fund launches each year – for example, in the past year 183 funds were launched – but the bulk of the flows go to a small number of funds, which means there are many that fail to get off the ground.

Data group Morningstar recently looked at the problem, to try to get a grip on how many of these funds exist. It deemed an orphan fund to be one where it has €100m in assets or less, has been running for at least five years and hasn't seen inflows or outflows of more than €10m in each of the past five years. These are basically stagnant funds failing to attract assets and which have been running for some time.

There are 194 funds in the UK that meet this criteria, and according to Jonathan Miller, head of research at Morningstar, a large chunk of those are multi-asset funds or fund-of-funds, which are products that invest in other funds.

ARE YOU INVESTED IN AN ORPHAN FUND?

Investors don't need to stick to Morningstar's criteria to see if they are invested in an orphan fund, but it's a good starting point.

Essentially you want to see whether any of your funds are tiddlers in size but have been running for a while. Many funds will be small if they're new and still building up assets, but if it's been running for five years or more and has failed to reach a decent size, that's a warning sign.

Size is dependent on the sector the fund is operating in. Some funds choose to close at smaller sizes as they invest in niche areas of the market and so reach capacity sooner. For example, if you're investing in a niche Japanese technology fund it's

likely to be smaller than a global equity fund.

A downwards trend in the asset size is an important warning sign. Another thing to consider is whether the charges are higher than the average fund. Smaller funds will typically have higher costs, as there are fewer investors to spread some of the fixed costs around, and the fund manager will still want to make a profit.

WILL A FUND CLOSE IF IT GETS TOO SMALL?

There's no real incentive for fund managers to close zombie or orphan funds, unless they become unprofitable to run – and the high charges on the fund usually mean they pay their way.

Often the costs of shuttering the funds and the bad press coverage the firm might get, along with the admin of dealing with existing investor assets, means it's not an option entertained by many fund managers.

Another option, and one that happens a fair amount, is that the fund is merged with another fund – and typically one that is much larger. This can work well for investors as it gives them the option to transfer to the other fund or to cash out – it also alerts them to the fact that they might be in a dud fund.

> “SO-CALLED ‘ORPHAN’ OR ‘ZOMBIE’ FUNDS ARE THOSE THAT HAVE FAILED TO REACH SCALE (OR PREVIOUSLY REACHED SCALE AND THEN SAW MASSIVE OUTFLOWS) AND HAVEN'T SEEN ANY SIGNIFICANT INFLOWS FOR YEARS.”

However, for smaller asset managers this isn't likely to be an option, as they won't have a similar fund into which they can merge the assets. It means that fund managers are unlikely to warn if you're in one of these funds, because that would just make the problem worse and potentially lead to more outflows.

Morningstar's Miller adds that some fund houses want to keep hold of the funds for ‘optionality’. This basically means they want to keep the funds so that their product range looks broader, but also so that if the sector comes back en-vogue they have a product already there, with a track record and at least some assets.

HELP, I HAVE ONE OF THESE FUNDS

If you've got one or more orphan funds in your portfolio the obvious next step is to consider switching into a larger fund, with lower costs and one that has grown in recent years. But it's not always as simple for investors to just vote with their feet and sell the existing fund.

Some investors may have been in the fund for a long time and so have substantial capital gains on the investment. If it's not within an ISA or pension they may want to sell in stages to make use of their capital gains tax allowance and avoid a massive tax bill. Ultimately, investors should be looking for the exit, even if they stage it over a few years.

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

‘How can I avoid breaching the lifetime allowance?’

AJ Bell pensions expert Tom Selby explains the key rules

I’m 41 and have managed to save around £310,000 overall in three defined contribution pension pots.

I wanted to know what pension growth rate I should use as a conservative estimate to highlight what I might expect at 58 (earliest age to retire), 60 and 65.

Should I continue paying into my pension pots, albeit at a reduced rate as I worry I might breach the lifetime allowance if the growth rate over time does this?

Steve

Tom Selby
AJ Bell
Senior Analyst says:

Just a reminder that I can’t give advice, but I can provide a bit of information about how the rules work.

Let’s start with the lifetime allowance. This is the cap on total tax-incentivised pension savings a person can build up throughout their lives. It currently stands at £1,055,000 and is due to increase every year in line with Consumer Prices Index (CPI) inflation.

It’s worth noting that because this is due to rise in line with inflation, by the time you retire it should be much higher. If we assume inflation of 2.5% a year, in 20 years it’ll be just north of £1.7m. This depends on the Government not tinkering with the rules, which unfortunately cannot be guaranteed.

One thing to consider is that if you breach the lifetime allowance, any tax charge will only be applied on the excess once you draw a retirement income (or turn 75). The lifetime allowance charge is designed to negate the tax relief incentives you’ve enjoyed on the money you’ve paid in, so you won’t lose everything.

The investment growth you might enjoy will depend on a wide variety of things including the performance of your underlying funds, the charges you pay and how much risk you take.

If you take more risk you have the chance of achieving higher returns, but this will come with more uncertainty. Equally a lower risk portfolio should deliver a more certain outcome, but your potential for market-beating returns will be reduced.

Crystal ball-gazing can be a fool’s errand – you’d be much better reviewing your portfolio regularly (at least once a year)

to make sure you’re happy with how much you’re paying in, your charges and the level of risk you’re taking.

Sadly I cannot tell you whether or not to stop paying in as that would constitute advice. However, I can say that the tax treatment of pensions is extremely generous – you get a minimum of 20% tax relief on contributions and 25% of withdrawals are tax-free from age 55.

Provided you are within the annual and lifetime limits, saving in a pension remains a sensible idea for most people.

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.

The ultimate guide to investing in the technology space: part 1

We explain the appeal of the sector and the key drivers

Modern history has seen a remarkable pace of change. Disruption is everywhere and changes to established industries, employment dynamics and how we all live are shaking to their foundations almost every aspect of life. From transport to energy, communications to healthcare, manufacturing, entertainment, education, even government.

Yet many investors remain reluctant to invest in the technology space – either through company shares or investment funds. They are put off by high failure rates for companies, often inflated stock valuations and sometimes limited profits and cash flow.

To avoid the space entirely is a mistake and an expensive one for those with a longer-term investment horizon.

This is illustrated by research conducted by consultancy McKinsey. It found that evolving technology as a percentage contributor to world output growth had risen from 33% in the mid-20th Century to around 50% today.

MASSIVE RETURNS POTENTIAL

The technology space has an almost unique ability to create wealth for investors. For example, Apple is the world's largest company by market value, worth around $1trn, and a stock that has made investors a lot of money over the years.

A £1,000 investment in Apple 10 years ago would today be worth more than £16,000 (as of May 2019). Yet it is not the best-performing wealth creator among the US mega tech companies. Amazon has rallied 3,526% over the same decade. The online shopping colossus would have turned a £1,000 investment into a nest egg worth more than £35,000.

TECHNOLOGY EMBRACED BY ALL

Business and entertainment have been transformed by the invention of the personal computer, the internet and now migration to the cloud.

Customers are constantly looking for cheaper, faster and better services, and providers like Amazon, Salesforce, Netflix, Uber, Airbnb, and many others, have the solutions.

The UK has seen **ASOS (ASC:AIM)** emerge into a £3.3bn online fashion retail colossus in less than 20 years. **Rightmove (RMV)** and **Auto Trader (AUTO)** have used technology to evolve how we buy and sell homes and cars, while clever robotics designed by **Ocado (OCDO)** are shaking the grocery logistics industry to its foundations and offer a glimpse into a possible automated future.

Little of this would have been possible without Microsoft's breakthrough in desktop computing, Google's clever internet search algorithms, Amazon's transformation of how

Robeco's 'megatrends'

- **TRANSFORMING TECHNOLOGIES**
  Emergence of new disruptive ways of changing what we do and what we want

- **SOCIO-DEMOGRAPHIC CHANGE**
  Managing a larger, wealthier and increasingly elderly global population

- **PRESERVING EARTH**
  Managing climate change and natural resource scarcity through better environmental awareness and regulation

we buy stuff and the technology creations of countless others.

It is no coincidence that the five largest publicly-listed companies in the US by market value (including overseas companies with US listings) are in the technology sector – Apple, Amazon, Microsoft, Alphabet (the parent company of Google) and Facebook.

Together these five companies account for more than 16% of the overall $25.6trn value of S&P 500 index. The wider technology sphere is now the largest sector in the S&P 500, making up nearly 29.3% of the index. For investors, technology matters.

FLOATING ALL BOATS

This new digital explosion, sometimes called the fourth industrial revolution, has the potential to raise global income levels and improve the quality of life for populations around the world.

To date those who have gained the most from it have been consumers able to afford and access the digital world but technological breakthroughs and disruption to the ways things are currently done have the potential to make products and services available to all, increasing the quality and longevity for everyone.

Ordering a cab, booking a flight, buying a product, making a payment, listening to music, watching a film, or playing a game – any of these can now be done by almost anyone, almost anywhere.

Breakthroughs in medical science, energy efficiency, agriculture and more offer the promise of improvements in almost every part of our lives, and those of our children and future generations.

MAJOR INVESTMENT THEMES

Transforming technologies, such as artificial intelligence, the sequencing of DNA or quantum computing, is one of three fundamental 'megatrends' according to analysts at asset management company Robeco.

It sits side-by-side with major socio-demographic change and 'preserving Earth' as themes that will dominate the future, creating opportunities for investors to participate in solving some of the biggest questions facing humanity.

Tech winners are big news and their headline-grabbing growth draws the attention of the mass media and investors at every level, from institutions and pension funds to retail investors.

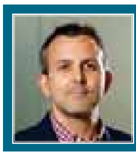
But not every tech story is a Microsoft or a Google. According to Steve Jobs, the co-founder and former chief executive of Apple, his company was just 90 days away from bankruptcy in 1996. For every big winner there are inevitable tech stock disappointments who fail to live up to their early promise. Blackberry, Napster, Palm, Netscape and Friends Reunited spring to mind.

This illustrates the significant risks involved. Technology changes quickly, and one-time leaders can quickly fall behind, or even go out of business.

'This can be challenging, yet it can also bring significant opportunities,' states Allianz Global Investors' head of investment trusts, Melissa Gallagher.

Some investors may still prefer to do their own research, crunching their own numbers and selecting their own technology stocks. But there is

a plentiful supply of managed help for those that prefer to take a broad position, investing in the expertise and experience of a trusted fund manager to do the work for you. This approach can spread risk and introduce investors to successes they might not otherwise have known.



By **Steven Frazer**
News Editor

Industrial revolutions

- 1780s: Steam, water, mechanical production equipment
- 1870: Electricity, division of labour, mass production
- 1969: Electronics, IT, automated production
- 21st Century Digital: cyber-physical systems, connectivity

Source: World Economic Forum

WHY INVEST IN TECH?

- **DEMAND**
  Corporations and governments have seen and experienced the benefits of next generation solutions in areas such as the cloud, storage and networking and are accelerating their transition from last-generation technologies.

- **RESILIENCE**
  Tech companies can generate rapid growth in defiance of economic conditions.

- **INNOVATION**
  The technology sector is an unparalleled source of innovation. Companies that are doing something new may often have a number of years of super-normal returns before the rest of the market catches up. For an investor, this means that share prices can grow very rapidly over a relatively short space of time.

- **REACH**
  Every other sector of the modern economy is reliant on technology to improve quality or productivity, maintain competitiveness or spur expansion. This gives the technology sector unique growth characteristics.

- **YIELD**
  Some large cap technology companies have very high cash flow yields and hundreds of billions of dollars on their balance sheets. They are starting to offer reasonable yields from dividends and could potentially increase their dividends substantially, returning more cash to investors.

- **LONG-TERM PERFORMANCE**
  Technology stocks can offer a valuable long-term complement to a portfolio of traditional equities, having outperformed the FTSE 100 over five, 10 and 20 years – although past performance is no guarantee to future returns.

Source: Allianz Technology Trust

NEXT WEEK:

Don't miss part 2 of our guide to investing in the technology space. We will discuss many of the popular stocks, funds, investment trusts and ETFs which provide relevant exposure to tech-related themes. Out on 16 May 2019.

Why Ankara and Buenos Aires remain important to global portfolios

We try to make sense of the latest events in emerging markets

Last summer, many analysts were wondering whether Turkey was about to pull the rug from under global financial markets. Ankara's currency, the lira, was in free fall as the economy over-heated and found itself over-reliant on foreign capital for funding, via a large current account deficit.

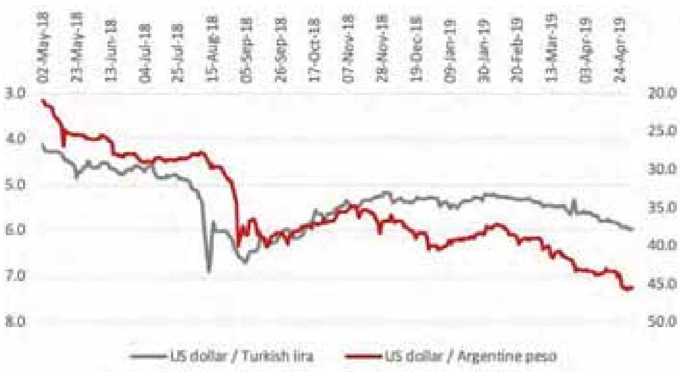
A stronger dollar, fuelled by higher US interest rates, was draining away liquidity and the reluctance of President Recep Tayyip Erdogan to follow what was seen as orthodox policy in the West – namely to jack up interest rates – was making matters worse.

EMERGING MARKETS ARE RECOVERING ALONGSIDE DEVELOPED ONES FROM THE SELL-OFF SEEN IN LATE 2018

Source: Refinitiv

Yet last winter's wider market panic is seemingly becoming a distant memory. As this summer approaches Turkey seems to barely warrant a mention, even though inflation is still near 20%, the lira trades 10% lower against the dollar compared to January and the economy is in recession, thanks in part to the prevailing 24% interest rate which the Central Bank of Turkey is using to defend its currency.

SLIDING CURRENCIES MAY REFLECT ECONOMIC AND POLITICAL WORRIES CONCERNING ANKARA AND BUENOS AIRES



Source: Refinitiv

The weak economic outlook is having a political impact, too, with President Erdogan's Justice and Development Party (AKP) losing ground in this year's local elections (which may explain why he was less than keen on those lofty interest rates).

The opposition CHP party won five of the country's six major cities, although a contested ballot in Istanbul is about to be re-run.

Another election which may require more of investors' attention is the one due to be fought in Argentina in October. An inflation rate of more than 50% and a near-halving of the peso's worth from nearly 23 to the dollar to barely 45 are pouring the pressure on right-wing President Mauricio Macri and giving impetus to the opposition's campaign, spearheaded by his left-wing predecessor Cristina Fernandez de Kirchner, whose policies are blamed by many economists for the country's current woes.

SMALL EARTHQUAKES, NO-ONE INJURED

Yet it is easy to see why some economists and strategists are arguing that any upset in Ankara and Buenos Aires are just local difficulties that should not unduly influence the performance of investors' portfolios.

Turkey is a small part of the emerging markets indices. It represents just 0.7% of the assets of **Vanguard FTSE Emerging Markets ETF (VFEM)**, which tracks the performance of 1,083 individual emerging market equities.

Argentina is not even classified as an emerging market, but a frontier one and the Buenos Aires exchange provides just 14% of the assets of New York-listed exchange-traded fund iShares MSCI Frontier 100 ETF – which tracks the MSCI Frontier Markets 100 index.

No other emerging markets have anything like the same inflation problems as these two locations, with most leading emerging markets nations coming in at 5% or below.

Even after his embarrassment in the local elections, President Erdogan looks unassailable after constitutional changes and the AKP's crushing general election win of 2018.

And while Macri could be unseated – especially as he appears to be reaching for the desperation (and surely discredited) measure of price controls to try and fix inflation – global markets have witnessed the arrival of left-wing governments in Argentina before without being unduly concerned.

ACTION REPLAY

Equally there remains the risk that such a view is complacent. An economic crisis and currency slide in Malaysia in 1997 went on to have global implications in 1998, as the FTSE All-Share and FTSE All-World stock indices both fell sharply as ripple effects led to a devaluation in Russia and the meltdown (and subsequent bail-out) of the Long-Term Capital Management hedge fund.

Contagion is possible. Losses in one market can lead to fund redemptions or the search for liquidity from others. That is why all correlations go to one during financial crises and any fund manager brave enough to have argued two years ago that it would be different this time in Argentina under Macri is getting their deserved reward.

Buyers of the country's 100-year bond, issued in 2017, have seen the paper slide to barely 73 cents on the dollar, to add their currency losses.

It remains to be seen whether Turkey or Argentina's problems remain local or go global but attention should be paid, not least as there remains the risk that a worldwide trend gives emerging market assets pause for thought.

A STRONG DOLLAR HAS HISTORICALLY TENDED TO BE A HEADWIND FOR EMERGING MARKET EQUITIES

Source: Refinitiv

Even though the US Federal Reserve is putting interest rate rises on hold, the dollar, as benchmarked by the trade-weighted DXY or 'Dixie' index, keeps rising, thanks to the (relative) strength of America's economy.

And keen students of market history will know that a bouncy buck can hurt emerging markets – especially those that have lots of overseas debt, like Turkey and Argentina, to pluck just two names out of the air.

The MSCI Emerging Markets equity index may be trading some 15% below its January 2018 high with good reason after all.

By **Russ Mould**
AJ Bell Investment Director

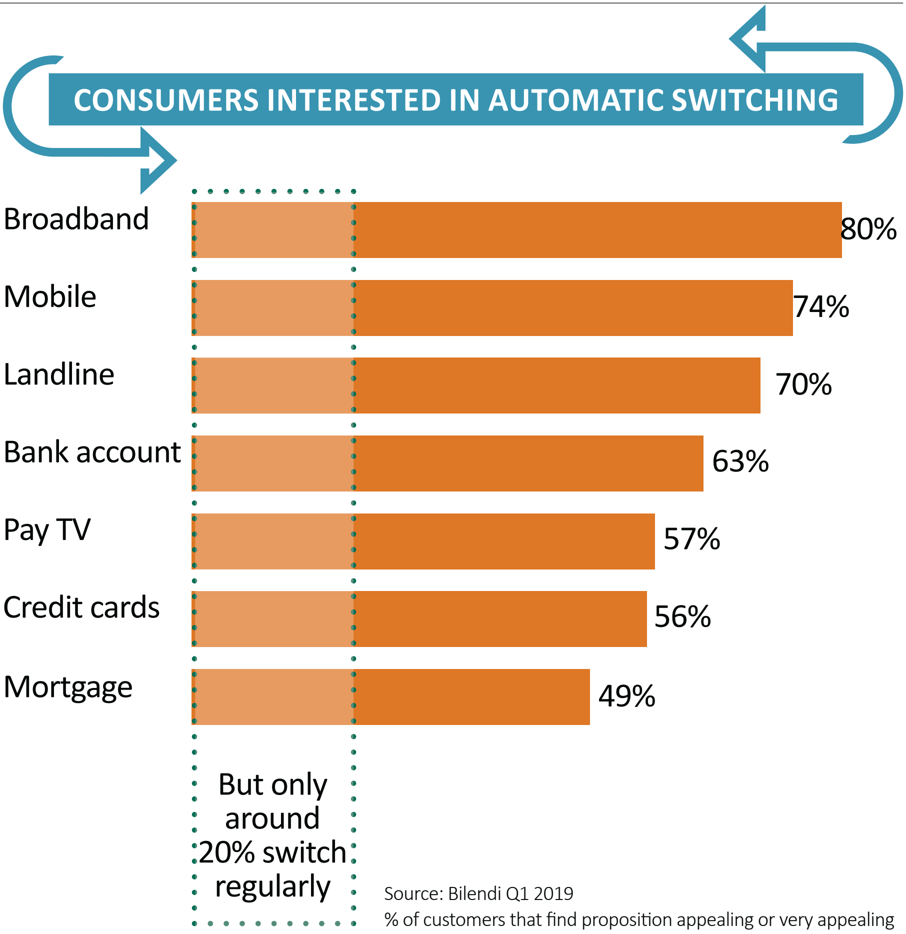
Can GoCompare disrupt the price comparison sector?

The company is pinning its fortunes on a new automated switching venture

Few of us love household admin and even if we did, even fewer of us are blessed with huge amounts of time to devote to it no matter the savings we could achieve.

It's no wonder that a new platform which could take the stress out of switching energy, broadband, insurance and financial services providers is generating excitement about the investment case at price comparison site **GoCompare (GOCO)**.

In this article we will look in detail at its WeFlip service and consider whether the internal and external hype over its potential is justified.



Source: Bilendi Q1 2019
% of customers that find proposition appealing or very appealing

GOING FOR A SONG

Probably best known for its irritating adverts starring opera singer Gio Compario, the company was previously owned by Esure but became a separately-listed company in November 2016. Its shares hit a peak of 143p in summer 2018 after it rebuffed a takeover offer from property listings site Zoopla.

The shares have since subsided thanks to fears over a possible competitive threat posed by Amazon plus factors such as the impact of falling motor premiums on the wider insurance market, and a plan to protect margins by cutting marketing spend and thereby surrendering market share.

In March 2019 the shares were boosted by insurance industry guru Peter Wood growing his stake in the company.

Wood, the founder of **Direct Line (DLG)**, Esure and Sheila's Wheels, has been involved with GoCompare since its acquisition by Esure in 2014 and currently sits in the chairman's seat.

Stakebuilding took Wood's holding from 25.6% to 29.9% and at the time he outlined his excitement over the automated energy switching venture. Subsequently the company spelled out its plans in this area at an investor day on 20 March.

WHAT IS WEFLIP?

GoCompare sees WeFlip as a way of reaching beyond the 20% of consumers which in its parlance are 'Savvy Savers' to those who rarely or never switch providers.

Customers complete a quote form for their first 'flip' and then confirm they are happy for the service to act as their agent. Once the customer is signed up in this way their preferences will be collected and WeFlip will monitor the market to identify the best deal.

If the customer's current tariff is the best one available then nothing changes, but if WeFlip finds a better deal the customer will automatically be switched.

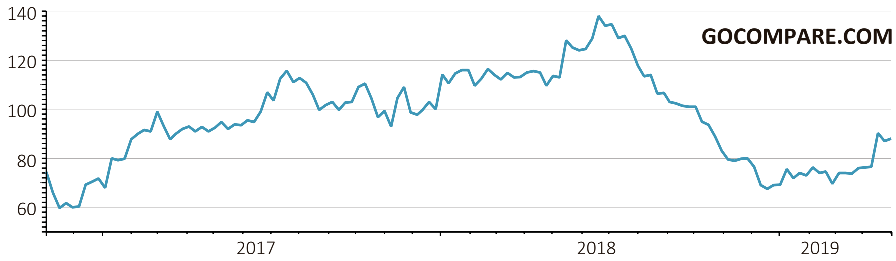
Officially launched in January 2019 (after a soft launch in October 2018) WeFlip is currently focused on the energy market but the company sees potential for a similar approach in other areas including broadband, insurance and credit cards.

The hope is that WeFlip will help GoCompare supplant the typical price comparison approach – which has limited barriers to entry and involves heavy marketing spend to compete for the attention of those which do switch – to create a subscription-based savings-as-a service model with higher levels of retention and lower marketing costs and ultimately a higher quality of earnings.

To be clear, the consumer would not be charged for this 'service' as GoCompare's revenue would come from the supplier.

COULD THE COMPANY TRADE ON A HIGHER VALUATION?

The whole plan is underpinned by the company's proprietary SaveStack technology platform. If successful, and it remains unproven at this stage, the strategy could see the company rewarded with a more premium stock market valuation.



Despite a recent modest recovery in the shares, they still trade on a low price-to-earnings (PE) ratio of 12.7-times. By way of comparison rival **Moneysupermarket (MONY)** trades on a PE of more than 20-times.

GoCompare's management appear to be flagging 2022 as the point at which its savings-as-a-service approach will have transformed the business and analysts have done some number crunching on the likely financial impact.

Liberum analyst Ian Whittaker remains a bit sceptical: 'Our view is that only a minority of consumers will be willing to give WeFlip the authority to switch services automatically and that energy companies, and others in the future, will be wary of signing up for a service that dramatically facilitates switching.'

This underpins a forecast for WeFlip to generate £17m or 9% of group revenue by 2022. Whittaker notes that if this proves overly-cautious and the service was to generate £40m of revenue in 2022, earnings per share forecasts for 2022 would be increased by 25%.

THE BULLISH VIEW

Whittaker's counterparts at investment bank Berenberg are more bullish. Its analysts say: 'If the price comparison website model could engage those infrequent or non-switchers to switch their energy bill once per year, this would open a £3bn market opportunity across car insurance, home insurance and energy (gas and electricity) alone.'

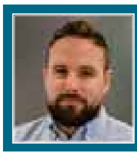
By expanding into new areas like broadband, mortgages and mobile, GoCompare 'will ratchet up the average revenue per user and thus have a multiplier effect on the revenue model', they add.

Both Berenberg and Liberum see the required investment in a roll-out of WeFlip and in marketing the proposition as constraining earnings in the short-term.

Given there is nothing to stop its peers attempting something very similar, GoCompare may need to move fast to fully exploit its first mover advantage.

SHARES SAYS:

Any new venture involves material risks but for investors comfortable with that reality, there appears to be relatively little in the share price to reflect the launch of a new product for which logically you can see a significant appeal to consumers. Buy at 86.9p.



By **Tom Sieber**
Deputy Editor

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Half year results

10 May: International Consolidated Airlines, Millennium & Copthorne Hotels. **13 May:** Bank of Cyprus, Diploma, TBC Bank, Victrex. **14 May:** BGEO, EI Group, ITE, Stock Spirits, Zytronic. **15 May:** Brewin Dolphin, Compass, CYBG, JPJ, Marston's, Ten Lifestyle, TUI. **16 May:** Euromoney, Grainger, Thomas Cook.

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