STOCKS | FUNDS | INVESTMENT TRUSTS | PENSIONS AND SAVINGS

VOL 19 / ISSUE 16 / 27 APRIL 2017 / £4.49

# SHARES

WE MAKE INVESTING EASIER

UTILITY STOCKS HIT BY CONSERVATIVE PARTY PRICE CAP THREAT

## IS IT TIME TO SELL FTSE 100 AND BUY FTSE 250?

# THE BIG SWITCH

***SDX ENERGY*** *UP 75% SINCE OUR FEBRUARY ARTICLE*

***OVERSEAS PUSH TO FUEL JD SPORTS FASHION***

***IS THE MOTOR SECTOR ON A PCP COLLISION COURSE?***

# Why can't firms see basic flaws in their business?

It is frustrating when companies are blind to obvious problems

It amazes me how some companies get into a mess over the most basic flaws in their business model. Common sense should have prevailed in the board room and ensured that problems are fixed straight away.

Too many companies limp along until they reach crisis point and a 'turnaround' expert is parachuted in. With that in mind, you might want to look at retailer **Debenhams (DEB)** and leisure operator **Goals Soccer Centres (GOAL:AIM)** as both are topical examples of 'recovery' stocks.

**LOST THE PLOT**

Debenhams' revival plan (20 Apr) looks weak. It failed to include sales or profit targets and the company still can't seem to grasp the basics of retailing: being the first place that comes to mind when you want to buy a particular product.

The new strategy is full of naff ideas, in my opinion. For example, the use of phrases such as 'mobile @everywhere' is bizarre; it screams of the days when everyone added .com to their corporate name to appear as if they were leading the internet revolution.

The 'mobile @everywhere' tag line is Debenhams' attempt to capitalise on customers having mobile phones on them at all times.

It also uses the phrase 'Meet me @Debenhams', saying it wants its stores to be somewhere where 'customers can spend time with family and friends'. Surely that's a leisure centre or a shopping mall, not a department store?

I taught my daughter to tread water in the deep end of the swimming pool last weekend. I should have asked Debenhams for some tips, as it must be a master at trying to keep its head above water without sinking.

**PROBLEMS STARING YOU IN THE FACE**

A previous visit to a Goals Soccer Centres five-a-side football site struck me how the place was a mess, lacked customers and badly needed refurbishment.

Making the place more appealing seemed like such an obvious way to fix the business – yet it took several years before Goals took a hard look at why it was struggling and decided to take corrective action.

Its latest results showed a return to like-for-like sales growth, following a multi-million pound refurbishment and modernisation programme. The business appears to have stabilised, but where does it go from here?

Chief executive Mark Jones told me in March that growth would be driven by the US. 'The UK is just about refurbishment and sweating the assets.'

**FAILURE TO UNDERSTAND LOCAL MARKET**

Interestingly, he said the company's first US site ran into cash flow difficulties. One problem was failure to understand cultural differences between the US and UK.

Goals replicated the UK design overseas including a big room for children's parties. It discovered California's sunny weather meant no one wanted to be stuck inside, plus a culture of the whole extended family turning up for parties.

It couldn't capitalise on the revenue opportunity because it lacked a large enough outdoor area for parties. That mistake could have easily been avoided with basic research.

There is now another twist to the story as Goals is sounding out a possible merger with UK rival Powerleague. This seems like a defensive move, ensuring there isn't a major competitive threat in the UK while it concentrates on the US.

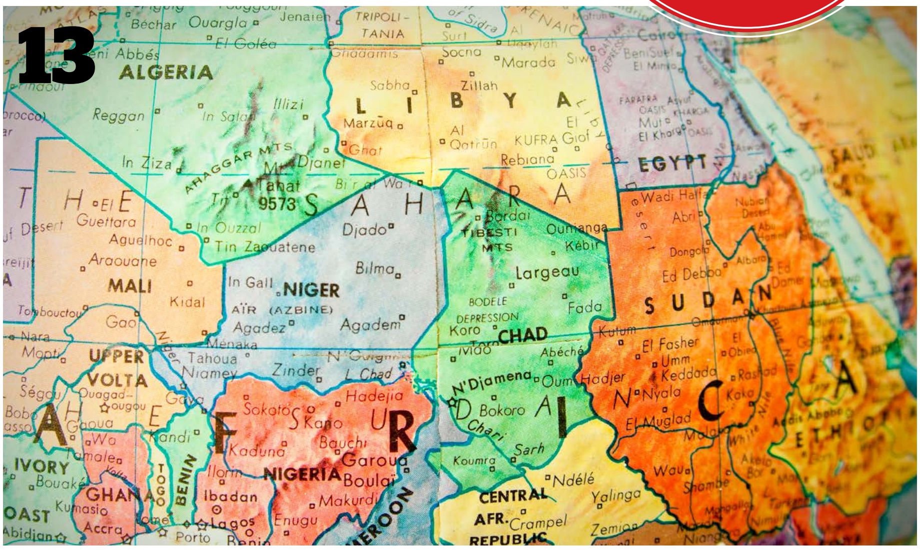
I'd imagine the deal would cause all kinds of fuss among the competition authorities as the two companies control about 60% of the market.

# Contents

## 27 April 2017



06




13

**INTERACTIVE PAGES**

CLICK ON PAGES NUMBERS TO JUMP TO THE RELEVANT STORY

# Contents



20

24





## WHO WE ARE

**EDITOR:** Daniel Coatsworth @SharesMagDan

**DEPUTY EDITOR:** Tom Sieber @SharesMagTom

**NEWS EDITOR:** Steven Frazer @SharesMagSteve

**FUNDS AND INVESTMENT TRUSTS EDITOR:** James Crux @SharesMagJames

**REPORTER:** David Stevenson @SharesMagDavid

**JUNIOR REPORTER:** Lisa-Marie Janes @SharesMagLisaMJ

**CONTRIBUTORS** Emily Perryman, Nick Sudbury, Tom Selby, Emma Lunn

**PRODUCTION**
Head of Production
Michael Duncan

Designer
Rebecca Bodi

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

**MANAGING DIRECTOR**
Mike Boydell

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




## BROKER RATINGS EXPLAINED:

We use traffic light symbols in the magazine to illustrate broker views on stocks.

Green means buy, Orange means hold, Red means sell.

The numbers refer to how many different brokers have that rating.

Eg: 4 2 1 means four brokers have buy ratings, two brokers have hold ratings and one broker has a sell rating.

The traffic light system gives an illustration of market views but isn't always a fully comprehensive list of ratings as some banks/stockbrokers don't publicly release this information.

# Energy in a spin over plans for power price cap

Utility stocks under pressure but income impact may be minimal

Energy supply companies have again been thrust into the spotlight with confirmation that the Conservative Party election manifesto will feature a commitment to cap certain power tariffs.

Press speculation earlier this week claims that the current Government would propose plans that cut gas and electricity costs by an average of £100 a year for 17m families, roughly the number estimated by the energy regulator, Ofgem, to be on standard variable tariffs (SVTs).

'This will be of some concern to income investors in particular, as **SSE (SSE)** is the fifth highest yielding stock in the FTSE 100 and **Centrica (CNA)** (the owner of British Gas) the eleventh highest,' says Russ Mould, investment director at AJ Bell. Their ability to grow those payouts to match or beat inflation may be called into question.

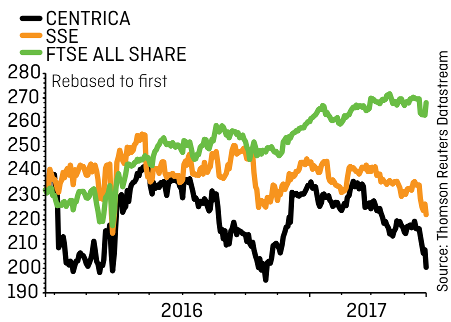
According to our rough calculations, a 10% cut in the SSE dividend this year to 31 March 2018, from 94.2p to 84.8p, would have minimal impact.

Investors with £5,000 worth of stock currently would see their forward income yield decline from 6.67% to 6%, yet that would reduce the annual income by just £33 this year to £300, a hit that would likely be covered by their household switching to a cheaper energy tariff.

That doesn't account for the inevitable fall in the share price that would result from a cut to the dividend.

## IN THE DARK

With details still be published by the Conservative Party, market analysts remain in the dark about how any price cap might work. Even then, many agree that uncertainty could rule over some utility stocks for the foreseeable future. There are also concerns over reduced competition presuming price caps are applied across the entire energy supply market and not just to the so-called big six, which could squeeze many independents out.




The share prices of Centrica and SSE are predictably weak as *Shares* goes to press on 25 April 2017, reversing 2.9% and 2.2% to 201.7p and £14.13 respectively. The pair sit number one and two in the UK in terms of the number of energy customer accounts, according to latest Ofgem figures, with roughly 6.64m and 3.86m respectively.

'It could be material to earnings per share (EPS),' speculate analysts at Morgan Stanley, which would impact dividend cover and potentially ultimately payouts. 'But how much would depend on the level of cap, whether it would be company specific, when it could come in to force,' note the investment bank's research team.

'It remains to be seen if this is just political noise or if it will actually impact profitability,' agree utility industry watchers at Berenberg, the investment bank. (SF)

# Wincanton joins list of potential takeover targets

The UK firm has a global customer base and encouraging growth prospects says analyst

Logistics firm **Wincanton (WIN)** could be the next British company to be taken over by a foreign business, according to analysts.

'We would argue that Wincanton is a potential takeover candidate given its market position, customer relationships, contract portfolio and attractive valuation. The recent devaluation of sterling could make it particularity attractive to an overseas buyer,' says Canaccord Genuity analyst Gert Zonneveld.

'Contract retention is high and annual revenue churn low, creating a solid revenue and profit stream with a high degree of visibility and relatively low volatility.'

Wincanton works for many well-known names in the food and drinks industry including **Britvic (BVIC)** and **Sainsbury's (SBRY)**.

'We expect Wincanton to deliver solid, if modest growth in the coming years, in line with that of the broad UK logistics market,' adds Zonneveld.

Net debt has been cut from £176.4m in 2009 to £32.2m as of 30 September 2016 following the disposal of non-core operations and improved cash generation.

Any suitor would also have to factor in Wincanton's £169.2m pension deficit in their calculations.

At 278.25p, the business trades on 9.9 times forecast earnings for the year to March 2018.

Canaccord believes the shares could hit 322p over the next year. (LMJ)

## Sportech easier to swallow after pools sale

### Company could be M&A target after selling off weak part of the business

A STREAMLINED **Sportech (SPO:AIM)** could be a takeover candidate according to Investec analyst Alistair Ross.

Shareholders in the betting services provider approved the £83m sale of its Football Pools operation to private equity firm OPCapita on 19 April and the deal is expected to complete in May.

Any M&A speculation may have to wait until after a ruling from the Supreme Court in July 2017 which will decide if Sportech is owed compound interest after a dispute over VAT with HMRC.

Investec reckons a successful outcome could be worth between £150m and £250m before tax or 81p and 135p per share. The company is already planning a £20m one-off return and there could be more to come assuming the Football Pools deal completes and it wins its case at the Supreme Court.

Funds are also likely to be funnelled into expanding the US gaming business which now represents its core area of focus. This includes the Sportech Racing and Digital betting hardware and software business and Sportech Venues gambling venue operation.

The company has already indicated its intention to pursue bolt-on acquisitions. (TS)

# Virgin Money shrugs off unsecured debt concerns

Bank's credit card operation looks solid despite rising debt levels in UK

Despite growing concerns over levels of unsecured debt in the UK, **Virgin Money (VM.)** has confounded the doubters by producing a strong set of lending results.

The company now has credit card balances of £2.7bn with what it describes as 'stable customer behaviour and arrear levels'. Credit cards are the company's highest growth sector.

Investec says that credit card growth in the first quarter was particularly strong, up £204m on the previous quarter to £2.65bn.

That was well above Investec's growth forecast of £160m and around 70% above the consensus prediction of £120m. It adds 'the £3bn year-end target looks a breeze'.

Virgin Money is bullish on the UK economy, saying it has remained stronger than expected following the referendum result. The company admits it watches the increase of consumer indebtedness closely but claims its credit card customers are 'showing no signs of strain in the current market'.

The Financial Conduct Authority is taking action over persistent debt. According to investment bank Jefferies, this should not concern Virgin Money as it views the company's book of credit card business as 'prime'. Virgin says it uses a 'strict and consistent application of underwriting standards' which lowers the risk of lending.

The bank's mortgage lending and deposit balances are up 3% apiece to £30.68bn and £28.98bn respectively in the first quarter of 2017. (DS)

## Whitbread burnt by Costa sales decline

SHARES IN **Whitbread (WTB)** took a knock on 25 April amid poor results from its Costa Coffee brand. Like-for-like sales fell by 0.8% between 1 December 2016 and 2 March 2017 versus 3% growth in the previous nine months. The company has a cautious outlook for the leisure brand, anticipating a tougher consumer environment in the UK over the coming year. (DC)

## Tritax investors offered cheap shares

INVESTORS IN **Tritax Big Box REIT (BBOX)** have the chance to buy slightly discounted shares as the warehouse specialist tries to raise £200m. An open offer will run until 10 May enabling existing investors to buy one new share at 136p for every 11 shares they already own. That compares with a 140.94p trading price at time of writing. (DC)

## Spanking for Sports Direct

IN AN excoriating research note (21 Apr) entitled 'From Damascus to Delaware', stockbroker Peel Hunt has put the boot into **Sports Direct International's (SPD)** $101m acquisition of 50 loss-making stores from a distressed US business. The company's focus should be on turning round Sports Direct's UK business rather than a US foray, according to Peel Hunt. (JC)

# Robotics stocks could get boost from Trump policies

A revival of industrial production in the US would require automation

Tech stocks fell when Donald Trump was elected president last November as investors rotated into banking stocks in the hope of friendly policies towards the sector from the new administration.

This trend is reversing according to Walter Price, senior portfolio manager of **Allianz Technology Trust (ATT)**, as some aspects of the 'Trump trade' failed to materialise.

Price remains hopeful certain elements of Trump's policies will see the light of day, especially his promise to bring manufacturing back to the US. For the country to remain competitive, production would have to be automated and this would boost robotics stocks.

To capitalise on this, Allianz invested in Cognex, a US robotics firm that specialises in machine vision, allowing systems to identify parts and detect faults.

The fund also added Teradyn, a semiconductor company which has acquired Denmark's Universal Robotics, a collaborative robotics company which makes robotic arms.

Price is not placing his hopes on robotics stocks solely on Trump's policies. He says there's also a trend in China for more automation due to a shortage of workers because of the one child rule. Automation can also be a cheaper than moving production to countries with lower wages such as Vietnam. (DS)


ZOOPLA HAS A £3bn revenue opportunity, according to investment bank Liberum. The online property portal trades on the stock market under the name **ZPG (ZPG)**.

Liberum has a 450p price target on the stock. It sees £650m of potential in its property services business, £850m in its comparison services arm and £1.5bn in its professional and data services division.

It reckons the company has only tapped 5% of this opportunity so far, based on 2016 revenue figures.

# 71 MONTH HIGH

BUSINESS ACTIVITY IS thriving in France despite a backdrop of security fears and political upheaval. The latest purchasing managers' index showed the tenth consecutive month of private sector growth.

The flash reading of 57.4 puts the PMI composite index for France at a 71-month high, according to IHS Markit data.

'While the dominant service sector remained the overall driver of growth, the rate of expansion in the manufacturing sector accelerated sharply from March, as demand for French goods continued to be buoyed by the relatively weak euro,' says IHS Markit economist Alex Gill.

# $5.4trn RECORD ETF FLOWS BOOST WORLD'S LARGEST ASSET MANAGER

BLACKROCK, THE world's largest asset manager, has increased its assets under management (AUM) to $5.4tn. The firm's exchange-traded fund division iShares record first quarter sales of $64.5bn is crucial in propelling BlackRock's AUM to this incredible figure.

iShares is the global leader for ETFs with a market dominating position globally. Its scale allows the firm to price its products lower than most competitors, controlling almost half of the European ETF market.

# GB £1,470 PAY RISE

IN ITS FIRST quarter update (20 Apr) online price comparison business **Moneysupermarket.com (MONY)** says it helps customers cut their motor and home insurance and energy bills by £1,000 on average. It says this equates to the same after tax as a £1,470 pay rise.

Should you put any of this extra cash into Moneysupermarket shares? Liberum says not: 'We remain cautious as revenue growth is heavily dependent on marketing spend and MoneySupermarket remain expensive relative to other internet portals.'

# £150M

## DEBENHAMS' COSTLY TO-DO LIST

THIS IS THE increased annual spend over the next three financial years **Debenhams (DEB)** has budgeted in order to upgrade its mobile systems, store estate and supply chain. It is a material hike from a current annual spend of around £130m. Alongside half year results (20 Apr) showing a 6.4% drop in pre-tax profit to £87.8m, new boss Sergio Bucher unveiled his plan to revive the department store's fortunes. 'Debenhams Redesigned' will look to tap into the trend towards 'social shopping' – shopping as a fun leisure activity shared with friends and family through social media.

# $100bn

Search advertising market is booming

GO!

NO WONDER GOOGLE'S parent company Alphabet is the world's second biggest company, worth nearly $589bn. It is the market leader in the booming online search advertising market. Web search is the largest segment within the $227.8bn estimated global digital advertising industry in 2017, expected to generate in excess of $100bn this year according to data from Statista. Online banner and social media are the next largest digital advertising segments, which helps explain why Facebook ranks number five in the world by market cap, worth $415bn. (SF)

## A SELECTION OF COMMODITY PRICES MOVEMENTS SO FAR THIS YEAR

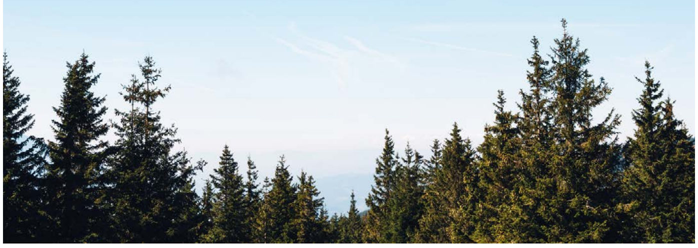
| | |
|---|---|
| Palladium | 18.8% |
| Cotton | 13.6% |
| Silver | 12.6% |
| Gold | 11.6% |
| Wheat | 2.8% |
| Coffee | -1.8% |
| Iron Ore | -5.8% |
| WTI Oil | -6.4% |
| Brent Oil | -6.9% |
| Cocoa | -14.7% |

Source: SharePad. Data to 21 April 2017
Based on a mixture of composites and spot prices.

## BEST PERFORMING FTSE 350 SECTORS SO FAR THIS YEAR

| | |
|---|---|
| Forestry & Paper | 18.1% |
| Personal Goods | 16.0% |
| Electronic & Electrical Equipment | 15.5% |
| Industrial Engineering | 12.3% |
| Household Goods & Home Construction | 11.1% |
| Tobacco | 10.5% |
| Real Estate Investment & Services | 9.4% |
| Aerospace & Defence | 8.4% |
| Financial Services | 8.2% |
| Support Services | 7.0% |

Source: SharePad. Data to 21 April 2017



# Imperial Brands won't run out of puff

## The tobacco titan offers a reliable stream of dividends

Troubled by the potential for market correction? Then consider investing in high quality mega cap **Imperial Brands (IMB)** which is committed to growing dividends by at least 10% a year. *Shares* believes the FTSE 100 company is worth buying ahead of first half results (3 May), which should provide reassurance through yet another dependable dividend increase.

### BRAND POWER

The tobacco multinational's resilient earnings and robust cash flows stem from a strong portfolio of brands which confer pricing power upon the business. These include Davidoff, Gauloises Blondes, West and JPS cigarettes, Rizla papers and Cohiba and Montecristo cigars.

Negatives hanging over the global industry include demand, duties and regulation. The decline in tobacco volumes is expected to continue as smoking rates fall across the world, yet global population growth means smoker numbers won't be much changed by 2025, according to the World Health Organisation.

Guided by CEO Alison Cooper, Imperial continues to bear down on costs and is investing an extra £300m behind its brands and key markets in 2017 to drive medium term sales growth.

Imperial has guided (30 Mar) towards a strong uptick in sales and earnings per share for the half to 31 March despite a deterioration in industry volumes. These results will show a boost as overseas earnings are translated into weak sterling.

**IMPERIAL BRANDS**
**BUY**
(IMB) £38.33
Stop loss: £30.66

Market value: £35.9bn

### GROWTH PUFF?

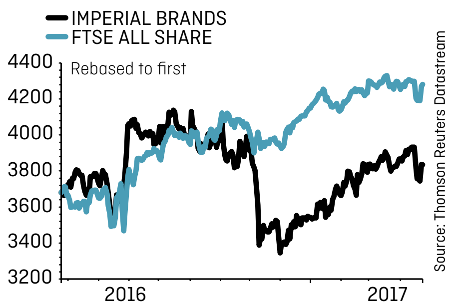
Imperial Brands recently inked (11 Jan) a joint venture to drive the growth of West and Davidoff in China, the world's biggest tobacco market. This builds on 2015's acquisition of a number of US cigarette brands, including Winston and Kool and the international rights to the blu e-vapour brand, in a deal which transformed Imperial's presence in the world's most profitable tobacco market outside China.

### M&A OPTIONALITY

For the financial year to September 2017, consensus earnings and dividend per share estimates are currently pitched at 272.91p (2016: 249.6p) and 171.1p (2016: 155.2p) respectively, rising to 284.83p of earnings and a 188.28p shareholder reward for 2018. Based on these latter forecasts, Imperial Brands trades on a prospective PE ratio of 13.5 times and offers an attractive 4.9% dividend yield.

We view this as reasonably undemanding for such a high quality stock. The merger between **British American Tobacco (BATS)** and Reynolds American has reignited speculation about further industry consolidation. Imperial Brands is the outstanding industry bid target, with Japan Tobacco International considered the logical acquirer. (JC)

**BROKER SAYS:** 13 4 1



# Eland is primed for share price surge

The company is focused on lifting output from Nigerian asset

A material ramp up in output from Nigerian oil producer **Eland Oil & Gas (ELA:AIM)** over the next six months could act as a significant catalyst for its share price.

The company's main asset is the OML 40 licence onshore in Nigeria's Niger Delta, in which it owns a 22.05% stake through its Elcrest Exploration and Production joint venture. It contains two fields, Opuama and Gbetiokun, with current proved and probable reserves of 83m barrels.

Elcrest is estimated to owe Eland as much as \$360m and until this sum is repaid Eland receives 100% of the cash flow from Elcrest's 45% interest in OML 40.

**\$26.3m free cash flow forecast for 2018**

## BIG PRODUCTION UPLIFT

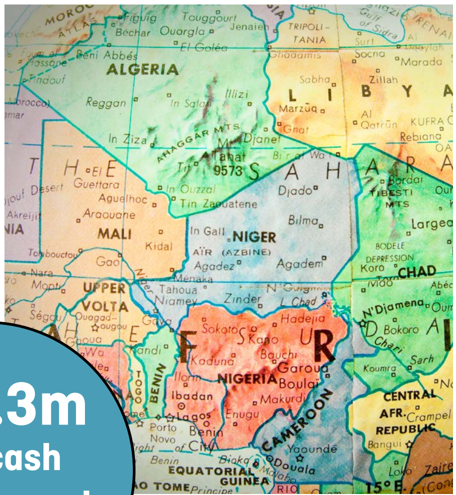
The plan is to boost production from OML 40 from a current 8,000 barrels of oil per day (bopd) to 17,500 bopd early in the second half of 2017 and 25,000 bopd around the turn of the year.

This will partly be achieved through drilling a side-track on the Opuama-7 well (using a different hole or wellbore to gain access to the oil) for which the company is fully funded following a redetermination of its borrowing base.

Eland has \$9m left unused on its \$24m lending facility and a current cash balance of \$7.5m. It is also set to receive an \$8.5m payment for its crude in the near-term.

**ELAND OIL & GAS**
**BUY**
(ELA:AIM) 57p
Stop loss: 45.6p

Market value: £106m




An extended shut down of the country's Forcados oil terminal due to militant attacks has seen an alternative route to market developed, shipping crude using tankers. This solution has a maximum capacity of 20,000 bopd.

Chief executive George Maxwell says the revenue from the oil minus the costs of getting it to market on the shipping solution is \$12 per barrel at an oil price of \$50 per barrel. That compares with \$27 per barrel (revenue minus costs) if Forcados was operational.

## WHAT IS THE UPSIDE POTENTIAL?

Canaccord Genuity values Eland at 40p based on the shipping option and 110p on Forcados coming back on stream.

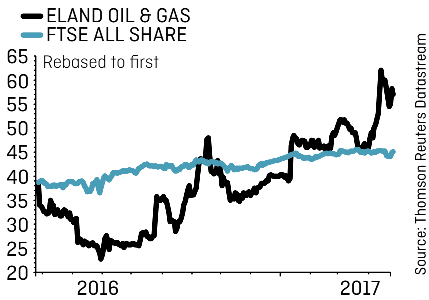
The company trades on 5.8 times forecast adjusted 2017 earnings per share falling to 3.1 times for 2018 when free cash flow of \$26.3m is also pencilled in.

From our point of view this more than prices in the significant security and political risks associated with operating in the Niger Delta.

Maxwell set up Eland with Leslie Blair in 2009 and moved from the finance director role to replace Blair, who moved to an advisory role, as CEO in 2014.

Both are former employees of Addax Petroleum, one of the few UK-listed success stories in Nigeria which was snapped up for \$7.2bn by Chinese firm Sinopec in 2009. (TS)

**BROKER SAYS: 6 0 0**



## SDX ENERGY
## (SDX:AIM) 67p

### Gain to date: 75%

**Original entry point:**
**38.23p,** 2 February 2017

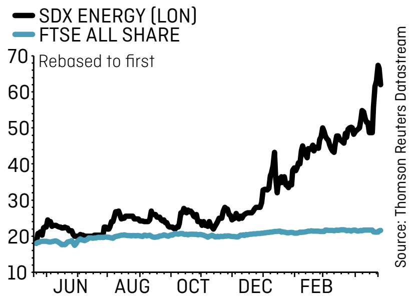
OUR ORIGINAL ARTICLE on **SDX Energy (SDX:AIM)** on 2 February cited broker Cantor Fitzgerald as saying investors could double their money within a year on this stock. We're already three quarters of the way to achieving that goal.

The Egypt and Morocco-focused oil and gas producer is riding high after drill results revealed a gas discovery in the Nile Delta.

An exploration well on the South Disouq project found gas in the first of three target areas and will now progress to test two deeper oil prospects.

Chief executive Paul Welch is aiming to lift production to 20,000 barrels of oil equivalent per day (boepd) in the medium-term, a process which was supercharged by the acquisition of assets from rival Circle Oil earlier this year. This transaction took output beyond the 4,000 boepd mark.

The company will drill seven new wells on its Lalla Mimouna and Sebou permits in Morocco having secured extensions from the relevant authorities.




These wells could be brought on to production rapidly given the proximity to existing infrastructure.

**SHARES SAYS:** ↗
**We see further scope for upside as SDX executes on its drilling plans in Morocco and Egypt. Cantor has a 78p price target. (TS)**

**BROKER SAYS:** 1 0 0

## SCISYS
## (SSY:AIM) 100p

### Loss to date: 9.5%

**Original entry point:**
**Buy at 110.5p,** 6 April 2017

SHARES IN THE IT services and projects supplier went within a whisker of our stop-loss after a press reports suggested Brexit could scupper further European Space Agency (ESA) work. **SciSys' (SSY:AIM)** subsequent denial comes as no surprise; management had previously reassured *Shares* on this issue. It benefits from strong relationships (it's a supplier on the ongoing Galileo programme, for example) and its base in Germany, through which it should meet any new EU rules.

**SHARES SAYS:** ↗
**We remain confident on the company's prospects and the stock's re-rating potential. (SF)**

**BROKER SAYS:** 1 0 0

## GB GROUP
## (GBG:AIM) 341.75p

### Gain to date: 35.1%

**Original entry point:**
**Buy at 253p,** 27 October 2016

THE MOST IMPORTANT point of **GB's (GBG:AIM)** year end update is the profit beat, adjusted operating profit of £17m versus £16.4m consensus. That's a 19.5% operating profit margin, a full percentage point ahead of analyst hopes for the 12 months to 31 March 2017 and easily on track for 20% targets by 2019. Sentiment had been unfairly dogged by a slow GOV.UK verify programme, and our call to take advantage has paid-off impressively, the share price 35.1% up in exactly six months.

**SHARES SAYS:** ↗
**A quality business; we remain happy to continue backing even on a forward price to earnings (PE) multiple of 31.9. (SF)**

**BROKER SAYS:** 7 0 0

## ELEMENTIS

(ELM) 312.7p

### Gain to date: 33%

**Original entry point:**

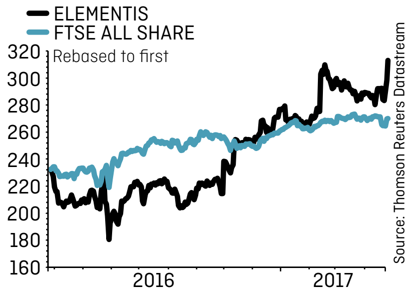
**Buy at 234.5p,** 10 November 2016

BROKER N+1 SINGER has upgraded **Elementis' (ELM)** 2017 profit and earnings per share forecast by 5% as the $360m acquisition of SummitReheis has completed three months earlier than expected.

Analyst James Tetley is confident the company will return to earnings growth after a slump in profits and earnings last year as the strong dollar and low oil prices dragged on performance.

He believes there is scope for outperformance in the share price once the SummitReheis acquisition is integrated.

Elementis said in February that it expected the acquisition to boost earnings in the current financial year which ends on 31 December 2017.




The chemical firm said on 25 April that the new calendar year had started well.

Its largest divisions, Specialty Products and Chromium, have bounced back thanks to strong growth in its personal care and energy businesses, as well as more demand outside North America.

Its chemical solution Surfactants division benefited from favourable pricing conditions.

**SHARES SAYS:** ↗

**Keep buying at 314.2p. (LMJ)**

**BROKER SAYS:** 5 4 0

## ST JAMES'S PLACE

(SJP) £11.12

### Gain to date: 44.5%

**Original entry point:**

**Buy at 769.5p,** 7 July 2016

WEALTH MANAGER **St James's Place (STJ)** is going from strength to strength, with another record quarter seeing net inflows up 46% to just under £2bn. This brings its group funds under management to £79.84bn in the first quarter of the year.

The company is a favourite of various analysts, with Numis saying it continues to hold it in 'high regard' and Shore Capital adding that its model is 'flourishing'.

Analyst Panmure Gordon is so smitten it has added the company to its Q2 2017 Conviction List of top picks, with the wealth manager's Q1 results 'simply reinforcing that view'.

**SHARES SAYS:** ↗

**Keep buying. (DS)**

**BROKER SAYS:** 15 3 0

## JIMMY CHOO

(CHOO) 185.75p

### Gain to date: 39.7%

**Original entry point:**

**Buy at 133p,** 8 December 2016

OUR BULLISH CALL on luxury shoe retailer **Jimmy Choo (CHOO)** is now a handsome 39.7% in the money. News (24 Apr) the British luxury brand has put itself up for sale, a move backed by majority shareholder JAB Luxury, saw the shares spike again and we are taking our tidy 39.7% profit off the table. Following its 2014 IPO at 140p, Jimmy Choo's shares initially struggled amid testing global luxury market conditions. However, the equity has since rebounded strongly and the decision to sell looks rather opportunistic, Jimmy Choo perhaps viewing this as the moment to fetch a decent price for the business.

**SHARES SAYS:** ↗

**Sell in the open market now, since there's no guarantee a sale will take place. (JC)**

**BROKER SAYS:** 3 2 0

## FRIDAY 28 APRIL

| | |
|---|---|
| **FINALS** | |
| Jersey Oil and Gas | JOG |
| **TRADING STATEMENTS** | |
| Barclays | BARC |
| Royal Bank of Scotland | RBS |
| Rotork | ROR |
| Ultra Electronics | ULE |
| **AGMS** | |
| HSBC | HSBA |
| **ECONOMICS** | |
| **UK** | |
| GfK Consumer Confidence | |
| Preliminary GDP | |
| BBA Mortgage Approvals | |

## MONDAY 1 MAY - UK STOCK MARKET CLOSED

## TUESDAY 2 MAY

| | |
|---|---|
| **INTERIMS** | |
| Shire | SHP |
| **AGMS** | |
| Capital & Regional | CAL |
| Howden Joinery | HWDN |
| Lighthouse | LGT |
| Randgold Resources | RRS |
| **ECONOMICS** | |
| **UK** | |
| Construction PMI | |

## WEDNESDAY 3 MAY

| | |
|---|---|
| **FINALS** | |
| Inspiration Healthcare | IHC |
| Osirium Technologies | OSI |
| **INTERIMS** | |
| Indivior | INDV |
| **TRADING STATEMENTS** | |
| Direct Line | DLG |
| Paddy Power Betfair | PPB |
| **AGMS** | |
| Lancashire Holdings | LRE |
| Ocado | OCDO |
| Standard Chartered | STAN |
| Secure Trust Bank | STB |
| The Renewables Infrastructure Group | TRIG |
| Virgin Money | VM. |
| **ECONOMICS** | |
| UK | |
| Services PMI | |

## THURSDAY 4 MAY

| | | |
|---|---|---|
| **AGMS** | | |
| Computacenter | CCC | |
| Gresham Computing | GHT | |
| GlaxoSmithKline | GSK | |
| Ladbrokes Coral | LAD | |
| Moneysupermarket.com | MONY | |
| Rolls-Royce | RR. | |
| Trinity Mirror | TNI | |
| **ECONOMICS** | | |
| **UK** | | |
| Mortgage Approvals | | |
| **US** | | |
| Unemployment Claims | | |
| **EX-DIVIDENDS** | | |
| Albion Development | AADV | 2p |
| Card Factory | CARD | 6.3p |
| Cello | CLL | 2.4p |
| Croda International | CRDA | 41.25p |
| Derwent London | DLN | 52p |
| Derwent London | DLN | 5.8p |
| Derwent London | DLN | 32.7p |
| Ebiquity | EBQ | 0.65p |
| Empresaria | EMR | 1.15p |
| EP Global Opportunities Trust | EPG | 1p |
| EP Global Opportunities Trust | EPG | 4.3p |
| F&C Private Equity Trust | FPEO | 6.48p |
| H&T Group | HAT | 5.3p |
| Highcroft | HCTF | 26p |
| Holders Technology | HDT | 0.25p |
| Henderson | HGG | 7.3p |
| Hastings | HSTG | 6.6p |
| James Halstead | JHD | 3.75p |
| JRP | JRP | 2.4p |
| Kingfisher | KGF | 7.15p |
| Lookers | LOOK | 2.36p |
| London Stock Exchange | LSE | 31.2p |
| Mortgage Advice Bureau | MAB1 | 10.5p |
| Microgen | MCGN | 3.5p |
| McColl's Retail | MCLS | 6.8p |
| Morgan Advanced Materials | MGAM | 7p |
| Pembroke VCT | PEMB | 1p |
| Polymetal | POLY | $0.18 |
| Playtech | PTEC | €0.22 |
| Rightmove | RMV | 32p |
| Safecharge International | SCH | 7.64p |
| Servelec | SERV | 4p |
| Stock Spirits | STCK | €0.05 |
| SThree | STHR | 9.3p |
| Swallowfield | SWL | 1.7p |
| Total Produce | TOT | €0.02 |

*Source: Shares*

**ROYAL DUTCH SHELL**

**First quarter numbers on 4 May from oil major Royal Dutch Shell (RDSB) are likely to reveal how the company is standing up to volatile oil prices.**

**They may also provide an opportunity to address a bribery scandal in Nigeria. Leaked emails earlier this month appeared to validate claims of corruption over an $1.3bn oil deal in the country in 2011.**

**SHIRE**

**Shire's (SHP) dry eye disease treatment XIIDRA shot to success in the first four months of its debut in 2016, capturing 19% of market share in the US.**

**First quarter results on 2 May could provide a chance for Shire to update on sales momentum. Investors will also want to know if Roche is continuing to chip away at sales in Shire's underperforming haemophilia franchise.**

**PADDY POWER BETFAIR**

**FTSE 100 betting behemoth Paddy Power Betfair (PPB) reports on first quarter trading next week (3 May).**

**The performance of online gaming and Australian business Sportsbet will be in focus, as will Paddy Power Betfair's performance over recent major UK horseracing events.**

**The gaming giant's recent full year results (7 Mar) revealed strong increases in stakes, revenues and earnings on an underlying basis for 2016.**

Click here for complete diary

# KEEP READING THIS WEEK'S SHARES AND DISCOVER:

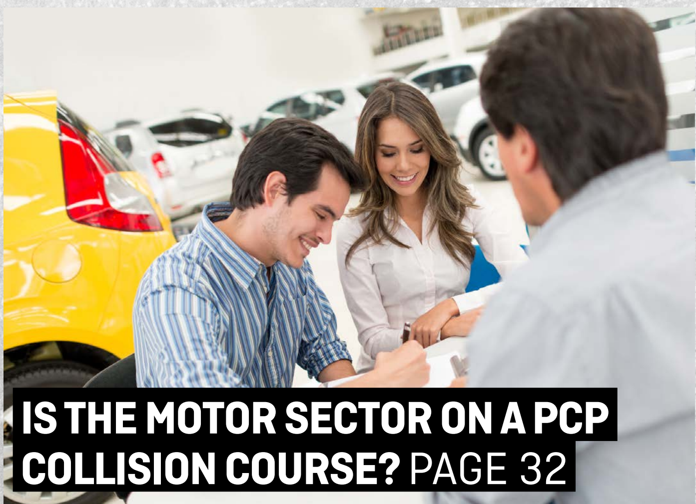
CLICK ON THE BOXES TO JUMP TO A STORY


**WHAT COULD THE GENERAL ELECTION MEAN FOR SAVERS?**
PAGE 20


**FUNDS TO PLAY BRITISH BARGAINS**
PAGE 36


**THE BIG SWITCH: IS IT TIME TO SELL FTSE 100 AND BUY FTSE 250?**
PAGE 24


**THE PACKAGING FIRM ON THE CUSP OF THE FTSE 100** PAGE 38



**IS THE MOTOR SECTOR ON A PCP COLLISION COURSE?** PAGE 32


**KEEP BUYING JD SPORTS FOR OVERSEAS SUCCESS**
PAGE 40

# BECOMING AN ACTIVE SHAREHOLDER

## IF YOU HAVE A 'SHARE' OF A COMPANY YOU HAVE A SAY IN HOW IT IS RUN

Imagine yourself sipping a latte and chatting to the CEO of **Taylor Wimpey (TW.)**, **Barclays (BARC)** or **HSBC (HSBA)**. What would you say?

Becoming a shareholder of a company gives ordinary people the opportunity to take large corporates to task on issues ranging from executive pay to the environment.

Publicly-listed companies (those whose stock is bought and sold by investors) are required to hold an annual general meeting (AGM) within six months of the end of the financial year– so between April and October.

### VOTING RIGHTS AND ASKING QUESTIONS

At the AGM, company directors present their reports and accounts and important aspects of company policy, such as the re-election and pay of directors, are voted on by shareholders.

All shareholders, no matter how small their shareholding, have the right to attend and vote at an AGM. Crucially, shareholders also have the right to ask questions, which the board are obliged to answer. For individual shareholders, this could be their best opportunity to make their voices heard.

Activist shareholders can go it alone or join forces with other shareholders to influence large companies.

ShareAction is a charity which brings together investors and gives them the tools and training to make their collective voice heard. ShareAction's 'AGM Army' project supports individuals attending company AGMs and raising issues directly with the board.

### VITAL PREPERATION

ShareAction spokesperson Beau O'Sullivan says shareholders should plan ahead before attending an AGM. 'Research the issue you'd like to raise. If your question requires a detailed answer, write to the chairman prior to the AGM,' he suggests.

'You should also research the company. Have a look at its website and the sections of its annual reports and accounts that are relevant to your question, and see whether the company has been mentioned by the media recently.'

It's a good idea to write out your question in advance of the meeting, keeping it short and concise. The process for asking a question will vary from company to company; some organisations require you to register your question in advance of the AGM, or on arrival. At other AGMs, shareholders can simply raise their hand during the question session.

## PUTTING FORWARD A RESOLUTION

Keen activist shareholders might want to take things one step further and put forward a 'shareholder resolution' at the AGM. These are different to 'company resolutions' put forward by the company, and could relate to any issue of concern to shareholders.

'Under UK law (the Companies Act 2006), shareholders have the right to file a resolution at a publicly listed company if they represent at least 5% of the total voting rights, or the concerned members number at least 100, holding shares on which there has been paid up an average sum per shareholder of not less than £100,' says O'Sullivan.

'Resolutions have to be framed to further the interests of the company and its shareholders. To become legally binding, the resolutions need to gain the support of 75% of the vote at the ballot on the AGM.

'Without the support of management, it is extremely rare for special resolutions filed to be passed at an AGM.'

## SUCCESS STORIES

In 2015 shareholder resolutions at both **BP (BP.)** and **Royal Dutch Shell (RDSB)** on climate risk disclosures became historic events by gaining the support of the boards of management, and passing at the AGMs with nearly 99% of the vote.

'AGM activism has helped us secure significant wins that changed lives all over the world,' says O'Sullivan, 'For example, our AGM question at **AstraZeneca (AZN)** helped to galvanise its commitment to using 100% renewable electricity and joining the RE100 initiative.

'Last year, ShareAction teamed up with other organisations to convince BP to abandon its plan to drill for oil in the pristine waters of the Great Australian Bight.'

## TACKLING THE PAY QUESTION

Alongside the environment, pay is a key subject for activists; not just executive compensation but at the other end of the pay scale too.

ShareAction is campaigning for FTSE 100 companies to pay the Living Wage (£9.75/hour in London and £8.45/hour for the rest of the UK) to all employees. It claims companies including Barclays, **Aviva (AV.)**, **Burberry (BRBY)**

LAST YEAR, SHAREACTION TEAMED UP WITH OTHER ORGANISATIONS TO CONVINCE BP TO ABANDON ITS PLAN TO DRILL FOR OIL IN THE PRISTINE WATERS OF THE GREAT AUSTRALIAN BIGHT

and **Centrica (CNA)** have all become accredited as Living Wage employers following Share Action campaigns.

You only need to own one share in a company to earn the right to attend, ask questions, and vote at its AGM. The voting process will depend on whether you own the shares in your name or in a nominee account.

ShareSoc is another organisation which encourages individual investors to make their voices heard and encourages them to vote at AGMs.

'If you hold a paper share certificate or are a Personal Crest Member then it is easy. You will be sent a paper voting form or can opt in for electronic notification. You can then vote by post or electronically,' says ShareSoc deputy chairman Roger Lawson.

'If your shares are held in a nominee account, as most are nowadays, then it gets a bit more complicated. In essence you will have to get your nominee operator (stockbroker) to submit your votes on your behalf because they technically own the shares not you (i.e. their name is on the share register). You just have a "beneficial interest" in them. But the voting rights are still yours.' (EL)

# What could the general election mean for savers?

We look at five key issues relevant to people working out how to fund their retirement

The forthcoming general election on 8 June is likely to be a bun fight for the so-called 'grey vote'. Labour has already made its big pitch to older people with its 'Pensions Pledge Card', while the Conservatives have traditionally polled strongly among this demographic.

From the so-called triple-lock to the state pension age and pensions tax relief, retirement issues are likely to be front-and-centre of all parties' general election campaigns.

## 1 STATE PENSION TRIPLE-LOCK

Under the triple-lock guarantee, the state pension increases each year in line with the highest of either the rise in average earnings, consumer price inflation or 2.5%.

While Labour has promised to retain the policy until 2025, it remains unclear where the Conservatives stand.

Theresa May will be nervous about potentially angering the pensioners whose votes will be crucial in the final outcome of the election.

In their 2015 manifesto, the Liberal Democrats pledged to make the triple-lock permanent, so it's a fair bet they will repeat that promise this time round.

Both John Cridland's independent state pension age review and the influential Work and Pensions Committee have said the policy should be scrapped.

## 2 STATE PENSION AGE REVIEW

Going into a general election on a manifesto commitment to increase the state pension age would be extremely risky.

The Government is scheduled to respond to the Cridland state pension age review – which suggested the state pension age should rise faster than under current plans – in May this year.

Given the political sensitivities surrounding the decision, it would be no surprise if the Conservatives quietly shelve any decision on until after the vote is done and dusted.

**'PERMANENTLY CUTTING SAVINGS INCENTIVES TO FILL A SHORT-TERM FINANCIAL GAP WOULD BE AWFUL POLICYMAKING'**

The other political parties, and particularly Labour, could use the election as a platform to promise not to enact the state pension age rises proposed by Cridland's review.

Such a policy clearly has short-term appeal but with people living longer and state pension costs expected to rise, Jeremy Corbyn would need to explain how the party would ensure that the system remains sustainable in the long-term.

## 3 PENSION TAX RELIEF

When the Government u-turned earlier this year on plans to increase National Insurance contributions for the self-employed, it did so purely because the decision broke a manifesto pledge.

Chancellor Philip Hammond argued the policy remained fair given the increased entitlements these workers now receive under the single-tier state pension. Logic dictates this policy should form part of the Conservative's 2017 manifesto.

Elections have a funny habit of shifting political priorities and it would be no surprise to see Theresa May kick this can as far down the road as possible.

If this is the case, the Conservatives will still need to fill a £2bn black hole from the Budget, with reports suggesting annual allowance for pension tax relief could be in the firing line.

Permanently cutting savings incentives to fill a short-term financial gap would be awful policymaking and could also prove unpopular among the electorate.

If the Conservatives claim a significant victory, it would be no surprise to see the party revisit various radical reform proposals. These include a possible 'Pension ISA' or flat-rate of relief for all taxpayers.

## 4 PENSION SCAMS CLAMPDOWN

The momentum behind banning pension cold-calling and taking the fight to scammers more broadly seemed unstoppable ahead of the Autumn Statement last year.

But five months on from the announcement of a long overdue clampdown on fraudsters, the Government has still not confirmed when the ban will be introduced or how other measures will be implemented.

The Brexit preparations already risked sapping Treasury time and energy away from this important work. With a snap election now on the horizon, we are deeply concerned this vital consultation will be kicked into the long grass. This must not happen.

The industry, advisers and regulators have already stepped up efforts to inform and educate the public about the risks of pension scams.

While such work can be effective, only the Government can put in place barriers to the business models used by these firms to fleece often vulnerable savers out of their hard-earned pensions. Every day that action is delayed, the more savers are put at risk of falling victim to fraudsters.

In the meantime, if you receive a call out of the blue about your pension from someone you don't know, the best thing to do is hang up the phone.


**'THE UK NEEDS ITS LEADERS TO PRESENT A LONG-TERM SAVINGS VISION WITH STABILITY AT ITS CORE.**

## 5 CLEAR LONG-TERM POLICY DIRECTION ON PENSIONS

Theresa May has talked of the need to deliver stability and security for the UK as a whole. The Government has so far failed to deliver on these aims for pensions, an area crying out for certainty and long-term thinking.

The UK needs its leaders to present a long-term savings vision with stability at its core. This should include a pledge to end incessant tinkering with the rules governing pensions. Savers need to be confident the ground won't shift beneath their feet as they plan for the future.

TOM SELBY,
senior analyst, AJ Bell

# Why you should have cash for life emergencies

Having a rainy day fund means you won't be forced to sell investments if you suddenly need money

Investing is undoubtedly the best way of building up a nest egg, but it's important not to lock away all your wealth.

Although cash has become somewhat of a dirty word in the current era of rising inflation and poor returns, it could be a lifesaver if an emergency strikes.

### EQUITIES VS CASH – WHAT ARE THE RETURNS?

Putting your money away to prepare for your future – whether that's retirement, buying a home or university education – is an incredibly wise move. We'd argue it is a particularly good if you're investing this money in the stock market.

Long gone are the days when Cash ISAs offered returns of 5% or more. Today, it's a struggle to find Cash ISAs with returns of just 1%, which is paltry when you compare it with the current UK inflation rate of 2.3%.

Equities – another name for stocks and shares – have achieved 5.6% average annual return over the past 50 years, claims the 2016 *Barclays Capital Equity Gilt Study*.

If you want your money to grow, equities are likely to offer the best combination of risk and return for the majority of individuals.

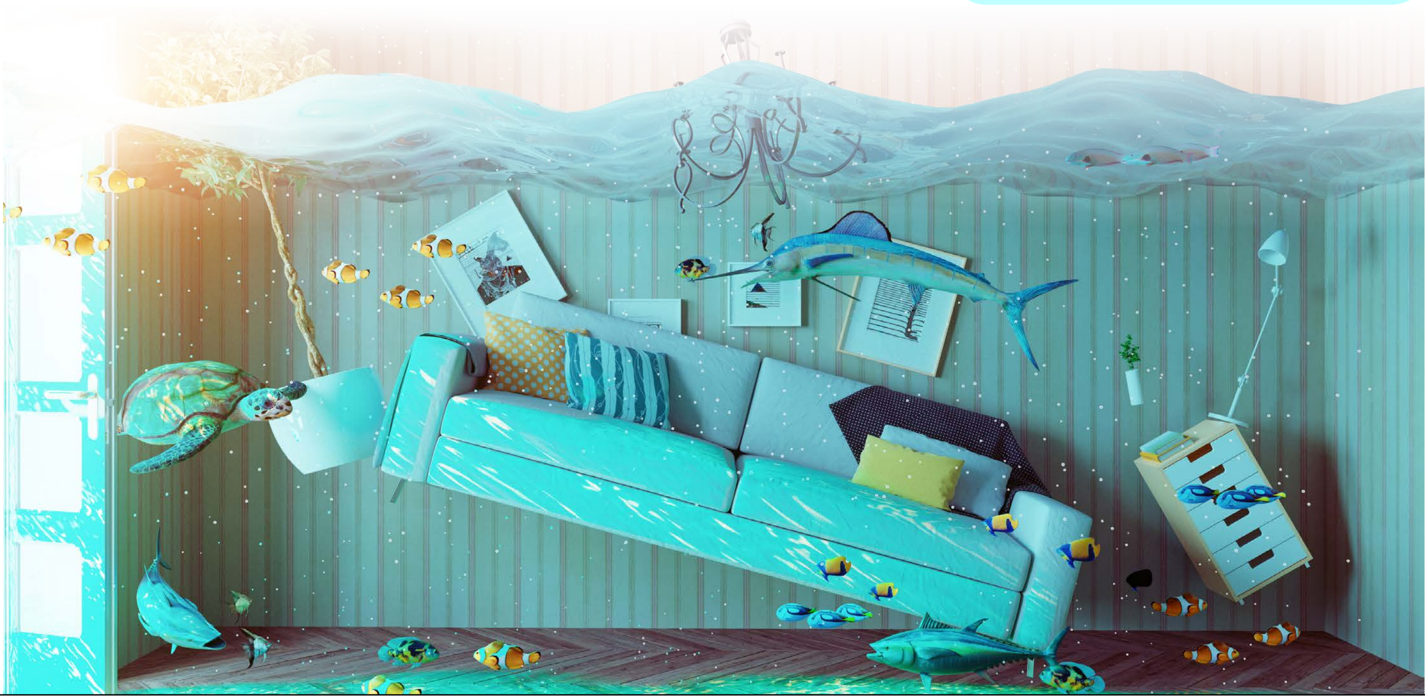
### WHY SHOULDN'T I PUT EVERYTHING IN EQUITIES?

Experts strongly advise not to invest all your wealth into the stock market. Equities should be viewed as a long-term investment, which means investing in them for at least five, or even 10, years.

The reason for this is that while equities rise over the long-term, they will probably go through some ups and downs along the way. If you suddenly need to access your wealth and your shares or funds have gone down in value, you'll end up crystallising your losses.

There are lots of reasons why you might need access to your money – a period of unemployment, ill-health, a major expense that isn't covered by insurance, divorce, and so on.

Because these events could strike anyone at any time, it's advisable to keep some money aside in cash that can be accessed quickly.



### HOW MUCH SHOULD I KEEP IN CASH?

The exact amount of money you put aside as an emergency fund will depend on what other assets you have and how quickly they can be turned into cash.

The split between your savings and investments will also be determined by your risk appetite.

Some experts suggest setting aside the value of three months' essential outgoings in cash. For example, if you usually spend £1,000 a month on bills, food and other things you can't live without, you could aim to have three times this amount in emergency savings.

Tom Riley, head of savings at building society Nationwide, recommends saving an emergency fund that is the equivalent of three months' salary.

'This can help take the pressure off if you lose your job or are unable to work for a period of time, but also useful if you receive an unexpected bill,' he says.

Trevor Clark, operations director at financial advice firm Rutherford Wilkinson, suggests analysing your costs such as money needed to repay a mortgage, loans or credit cards.

'Debt that accrues interest at a higher rate than you would earn on saving cash should be paid off first and foremost,' he says.

If you're unable to create an emergency fund straightaway, you could start by putting a regular amount aside each month, perhaps via a standing order.

### WHERE SHOULD I PUT MY EMERGENCY FUND?

As your fund is earmarked for emergencies, being able to access the money easily is key. You don't want to be putting this portion of your wealth into saving and investment products with fixed terms; otherwise you could face paying an exit penalty.

Easy access Cash ISAs are useful because they shelter your money from tax, but slightly better returns are to be found in savings accounts.

The flexible RCI Bank Freedom Savings Account pays 1.1% interest. You can open it with a minimum of £100 and make unlimited payments and withdrawals.

TSB's Classic Plus Account pays 3% on balances up to £1,500, although we'd assume most people would need a higher amount in emergency savings. Therefore you may wish to put the maximum permitted in the TSB account to get 3% interest and the rest somewhere else.

You could also consider a regular saver account. These accounts are designed for savers who want to put a regular amount aside each month and typically offer a higher rate of interest – First Direct, M&S Bank and HSBC all offer 5%.

You'll need to have a standard current account with the provider to qualify and there are restrictions on how much you can pay in. The rate will drop after one year when you should consider switching to a better deal. (EP)

### WHAT ABOUT TAX?

Holding cash in a traditional savings account means you don't enjoy the tax benefits associated with an ISA. However, the personal savings allowance means a basic rate taxpayer can earn up to £1,000 and a higher rate taxpayer up to £500 in savings income tax-free each year.

'For the latter, an individual would need £10,000 in savings earning 5% to reach £500 in interest. Therefore, while large amounts of money invested in the market and protected in a tax shelter make sense, smaller sums held as cash will have to work hard before exceeding the personal savings allowance,' explains Clark at Rutherford Wilkinson.

# THE BIG SWITCH

## IS IT TIME TO SELL FTSE 100 AND BUY FTSE 250?

Markets are driven by sentiment and identifying when sentiment is shifting can help you spot investment opportunities.

For the last 10 months four key interlinked factors have held sway: Brexit, sterling weakness, Donald Trump becoming US president and the return of inflation.

The surprise news of a UK general election on 8 June changes the story. We believe there is now the start of a big switch in investor interest from the overseas-focused FTSE 100 into the more domestic names on the FTSE 250.

**CONSERVATIVES ENJOY A 21-POINT LEAD IN THE POLLS**

### GAME CHANGER

Prime Minister Theresa May's shock announcement of a snap election is, in the words of Deutsche Bank's currency team, a 'game-changer' for sterling.

The basic argument runs as follows. The Conservatives' 21-point lead in the polls could translate into a big increase in their current House of Commons majority of 17 seats once the general election result is published on 9 June.

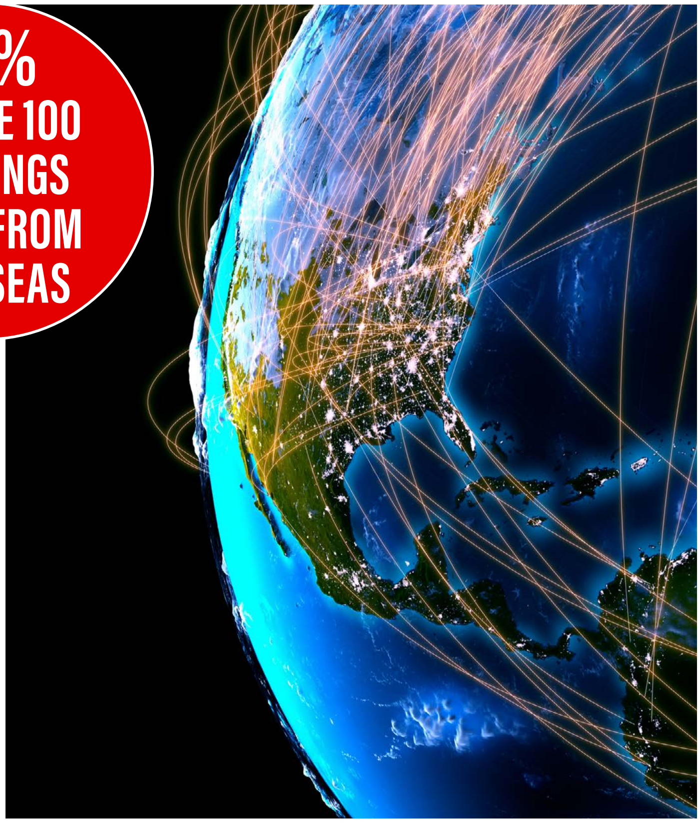
Some projections suggest May could command a majority of up to 100 seats which would give her a stronger mandate and greater leeway to negotiate a Brexit deal.

Since she made her announcement shortly after 11am on 18 April sterling has gone from around $1.25 against the dollar to more than $1.28 – a big move in currency terms. However, very weak monthly data on UK retail sales on 21 April has subsequently taken some shine off the pound.

This election-driven move in the foreign exchange markets has coincided with a significant reversal for the FTSE 100 which has now wiped out any year-to-date gains from the index.

The recovery in sterling hits the value of profits earned overseas when translated back into pounds, and around 70% of FTSE 100 earnings come from abroad. However, as we discuss later in this article, currency movements are not the only reasons behind the FTSE 100's recent collapse.

**70% OF FTSE 100 EARNINGS COME FROM OVERSEAS**



## MID CAP COMEBACK

The big question for investors is whether now is the opportune moment to load up on the more domestic-focused names in the FTSE 250.

While mid-caps underperformed in the wake of last June's Brexit vote, the FTSE 250 index quickly recovered and has been on a strong run so far this year.

## ECONOMY NOT AS BAD AS FEARED

Many market commentators inmediately after the Brexit vote expected a big hit to economic growth in the UK. That hasn't really happened. In fact, we're actually seeing upgrades. That's clearly positive for FTSE 250 stocks which principally generate earnings from the UK.

For example, The International Monetary Fund is forecasting the UK economy will grow by 2% in 2017 compared with a previous projection of 1.5% just three months ago.

Observers reckon May could have greater room for compromise on Brexit after June's vote, thereby reducing any negative impact on economic growth.

Crucially it also pushes the timing of the next election from 2020 to 2022, leaving space for a more orderly transition period as the UK leaves the EU.

As analysts at investment bank Credit Suisse note: 'If Theresa May wins it would be a powerful mandate for her and her type of Brexit, which in turn would limit the ability of either the pro-EU or furiously anti-EU sects of the Conservative party to derail her Brexit.

'This could mean that it might be slightly easier for Theresa May to give some concessions in the Brexit negotiations and possibly deliver a softer Brexit than the one she has outlined so far.'

**IMF FORECASTING 2% GROWTH FOR UK ECONOMY IN 2017**

# SWITCHING INTO DOMESTIC MID-CAPS

**DEAD HEAT BETWEEN FTSE 100 AND FTSE 250**

BETWEEN THE BREXIT vote in June 2016 and the announcement on 18 April 2017 of a UK general election, the FTSE 250 slightly lagged behind the FTSE 100. The mid-caps were up 13% against a 16% advance for their blue chip counterparts.

Since the election news the FTSE 100 has eased back slightly and the FTSE 250 has held firm.

The FTSE 250 has a more domestic bias than the FTSE 100 but does derive around 50% of its earnings from outside the UK.

City Index research director Kathleen Brooks notes the FTSE 250 has actually been outperforming the FTSE 100, particularly since the beginning of February, and that its outperformance may have become 'stretched'.

However, certain sectors like retail, housebuilding, travel and leisure are tightly focused on the UK and they have been among the key underperformers since the Brexit vote.

This is largely down to a combination of the weak pound pushing up inflation and the wider pressure from a loss of consumer confidence, reflected in retail sales recording the biggest fall in seven years in March. For travel firms, the slump in sterling has also made overseas trips more expensive for British holidaymakers.

**FTSE 350 STOCKS WITH THE BREXIT BLUES**

| Company | EPIC | Performance (%) |
|---|---|---|
| ITV | ITV | -0.8 |
| Greggs | GRG | -0.9 |
| Barratt Developments | BDEV | -1.0 |
| Countryside Properties | CSP | -2.2 |
| Ocado | OCDO | -2.4 |
| Berkeley | BKG | -3.2 |
| Domino's Pizza UK & IRL | DOM | -5.2 |
| Marks & Spencer | MKS | -5.3 |
| Land Securities | LAND | -6.1 |
| Halfords | HFD | -6.9 |
| Royal Bank of Scotland | RBS | -8.8 |
| Marston's | MARS | -9.2 |
| Intu Properites | INTU | -9.5 |
| Kingfisher | KGF | -11 |
| Great Portland Estates | GPOR | -11 |
| Bovis Homes | BVS | -11 |
| Mitchells & Butlers | MAB | -11 |
| Howden Joinery | HWDN | -11 |
| Lloyds Banking | LLOY | -13 |
| British Land | BLND | -14 |
| Card Factory | CARD | -16 |
| Virgin Money | VM. | -19 |
| Sports Direct | SPD | -20 |
| Next | NXT | -24 |
| Dixons Carphone | DC. | -26 |
| Pets at Home | PETS | -30 |
| Dunelm | DNLM | -38 |

Source: Sharepad, close 23 Jun '16 to 18 Apr '17

## UK DOMESTICS ON COMEBACK TRAIL

If the pound reverses the negative trend seen since the EU referendum and the UK's economic prospects brighten then some of these stocks could be attractive.

The accompanying table shows domestic-facing companies which were in negative territory for the period covering the Brexit vote and up until Theresa May's announcement of a snap election.

From this list, we particularly like greetings card retailer **Card Factory (CARD)** and kitchens seller **Howden Joinery (HWDN)**, both of which are already constituents of our *Great Ideas* portfolio.

Card Factory offers excellent cash generation, a generous dividend and is a beneficiary of downsizing by its competition – most notably Clintons.

Staying in the retail sector, Liberum sees high street electronics shop **Dixons Carphone (DC.)** as a structural winner noting that 'through its leading multi-channel, specialist retail position and deep supplier relationships it is gaining share faster than any competitor'.

## '...THE STAGE IS SET FOR A GOLDEN PERIOD FOR THE UK HOUSEBUILDERS' - JEFFERIES

Liberum's 430p price target for Dixons implies upside of more than 30% from the current 325.1p share price.

The investment bank is more negative on another underperformer, **Pets at Home (PETS)** which it argues faces intensifying competition from online and store-based specialists as well as discounters and supermarkets.

We are unconvinced by the turnaround efforts at department store **Debenhams (DEB)** and the jury is still out on online groceries business **Ocado (OCDO)** given the competitive threats it is facing, notably from Amazon's newly launched rival service.

### STANDING ON FIRM FOUNDATIONS

Like the overall economy, previous forecasts for a property crash have so far proved wrong. That has seen investors continue to be supportive of housebuilders.

Investment bank Jefferies comments: 'In our mind, the stage is set for a golden period for the UK housebuilders with demand outstripping supply (placing upward pressure on the price of homes) and increased land supply where the country most needs homes (placing downward pressure on the price of land).'

On this basis **Bovis Homes (BVS)**, which recently walked away from takeover talks and appointed industry veteran Greg Fitzgerald to lead a turnaround of its fortunes, could be an interesting stock for investors to research.

On the leisure side, analysts at investment bank Berenberg like pubs operator **Marston's (MARS)** noting that through disposals and a roll-out of new-build managed pubs, the company has 'materially improved the quality of its estate' and the market is yet to price this in.

Marston's trades on a price-to-earnings ratio of 9.3 times, based on a forecast 15.1p earnings per share for the year to September 2018.


## WHAT TO THINK ABOUT

DON'T RUSH IN blindly. Investors looking to play a rebound for UK domestic-facing mid-caps should still tread carefully as politics and the currency markets are often volatile.

'There could be further upside if markets get what they want from this election, namely a strong Conservative majority allowing Theresa May to pursue a softer Brexit with a longer, more market-friendly transitional agreement with the EU post-2019,' says Neil Wilson at ETX Capital.

As well as being the most 'market-friendly' outcome it also seems the most credible one given the Conservative's dominance in the polls.

But, as Brexit and Donald Trump's election as US president have demonstrated, polls can be wrong.

There seem to be two other possible ways the election could play out:

1. Theresa May failing to materially increase her majority after the election would be treated as a disappointment by the market.

2. The much more remote possibility of May losing office and being replaced by a coalition government would be a severe market shock in the vein of the Brexit vote itself.

# WHERE NEXT FOR THE FTSE 100?

THE FTSE 100 HAD a very good year in 2016, rising by 14% in value. That is nearly four times higher than the 3.7% gain from the FTSE 250 index, according to data from SharePad.

Currencies are the principle reason behind this disparity. The dollar appreciated by 19% versus sterling in 2016. It also strengthened against many other major currencies including the euro (+3.3%).

## TAILWINDS… BUT FOR HOW LONG?

Nearly all the top performing FTSE 100 stocks in 2016 generated a large chunk of their revenue in dollars. They've enjoyed a significant tailwind from favourable foreign exchange rates.

Apart from the miners, most of these companies report their financial results in sterling, so there has been a translation boost to their earnings. That's naturally boosted their share price, too.

The miners have still benefited, nonetheless; all their shares are priced in sterling – so there has also been a translational boost when comparing their market value against earnings strength.

## TREND REVERSAL

The dollar has fallen approximately 4% against sterling so far in 2017, implying that the translational boost is fading away.

**FTSE 100 TOP PERFORMERS IN 2016**

| Company | Sector | Share price gain |
|---|---|---|
| Anglo American | Mining | 290% |
| Glencore | Mining | 210% |
| Fresnillo | Mining | 72% |
| BHP Billiton | Mining | 72% |
| Rio Tinto | Mining | 60% |
| WM Morrison Supermarkets | Food Retail | 56% |
| Randgold Resources | Mining | 55% |
| Royal Dutch Shell | Oil & Gas | 53% |
| Smiths | General Industrials | 51% |
| 3i | Financial Services | 46% |
| BP | Oil & Gas | 44% |
| Antofagasta | Mining | 44% |
| CRH | Construction | 44% |
| Ashtead | Support Services | 41% |
| Rentokil Initial | Support Services | 39% |

Source: SharePad

As mentioned earlier in this article, news of the snap general election in the UK has helped to further strengthen the pound. That's why many of last year's top performers (boosted by the stronger dollar) have seen this year their share prices grind to a halt (restrained by the weaker dollar).

## DON'T AUTOMATICALLY SELL ALL YOUR FTSE 100 STOCKS

The big question now is whether you should take profit in all stocks that have enjoyed a translational boost over the past year.

To answer that question you need to consider the following:

1. A strong dollar isn't the only reason why certain stocks rallied in 2016

2. Some of the companies who enjoyed a dollar boost could also benefit from a stronger pound

3. How are these companies performing if you look at constant currency rates, not actual rates?

Let's address those points one by one.

**FTSE 100 TOP PERFORMERS IN 2016… HOW HAVE THEY FARED SO FAR IN 2017?**

| Company | Sector | Share price gain |
|---|---|---|
| BP | Oil & Gas | -11.8% |
| Royal Dutch Shell | Oil & Gas | -10.3% |
| BHP Billiton | Mining | -7.4% |
| Anglo American | Mining | -3.4% |
| Rio Tinto | Mining | -1.5% |
| CRH | Construction | 1.0% |
| WM Morrison Supermarkets | Food Retail | 1.9% |
| Ashtead | Support Services | 4.6% |
| Randgold Resources | Mining | 6.9% |
| Rentokil Initial | Support Services | 10.4% |
| Glencore | Mining | 12.2% |
| 3i | Financial Services | 13.6% |
| Smiths | General Industrials | 14.9% |
| Antofagasta | Mining | 23.7% |
| Fresnillo | Mining | 23.8% |

Source: SharePad. Data to 25 April 2017

## 1 OTHER FACTORS AT PLAY

The FTSE 100 hit the headlines last week when the pound rallied on the election news (18 April). Most people attributed the blue chip index's decline to the currency movement.

What most commentators failed to explain was that the FTSE 100 was already trading down that day BEFORE the election news was out – principally as a result of commodity price weakness.

You have to remember that the FTSE 100 is a market cap weighted index. A stock that accounts for 10% of the index, for example, will have a more pronounced influence on the FTSE 100's pricing than something that only accounts for 0.1%.

Oil, gas and mining companies mostly sit at the top end of the FTSE 100 – so commodity price movements can cause the overall index to move as these relate to products being sold by the resource firms.

A large fall in the price of iron ore was the principal cause of the FTSE 100's initial decline on the day of the election announcement. **Glencore (GLEN)**, **BHP Billiton (BLT)** and **Rio Tinto (RIO)** all generate earnings from that commodity and they are all in the top 15 largest stocks by weighting in the blue chip index.

## 2 LOOK FOR CURRENCY CUSHION

A few stocks which benefited from US dollar tailwinds last year also do business in the UK – so you could argue that dollar weakness this year could be cushioned by gains in sterling and potential movements in other currencies.

Construction equipment firm **Ashtead (AHT)** only generates about 10% of its earnings from the UK, so we don't think any sterling recovery will really make a difference to its share price. Investors pretty much assume it is a pure play on US infrastructure activity.

In contrast, distributor **Bunzl (BNZL)** generates about 40% of sales from outside North America. It says currency movements helped to boost group revenue by 10% in 2016.

About 15% of Bunzl's revenue comes from the UK and a further 18% from mainland Europe. That should be big enough to provide a meaningful cushion to offset some of the translational weakness should the dollar (and the euro) continue to fall against sterling.

## 3 LOOK AT THE CONSTANT CURRENCY NUMBERS

Over the past few months we've tried to focus on constant currency numbers when reporting on corporate accounts in order to measure the true health of a business.

Currency movements tend to iron themselves out over time, so you should never expect one year's exceptional forex-led uplift in earnings to be repeated year in, year out.

Although not a FTSE 100 stock, British manufacturing company **Rotork (ROR)** is a great example of why it pays to study the numbers.

It reported an 8% rise in revenue in 2016 to £590.1m and a 10.6% decline in pre-tax profit to £91.1m. That's based on actual exchange rates. Take a closer look and you'll see currency tailwinds inflated its results by 10%.

The outcome is very different when you strip out an acquisition and run the numbers on a constant currency basis. Rotork's revenue actually fell 8% and it suffered a 20.5% drop in pre-tax profit. The business is therefore not as healthy as the headline figures would suggest.

# WHAT SHOULD I DO NEXT?

WE'D TAKE PROFIT on FTSE 100 companies considered to be 'obvious' beneficiaries of increased US infrastructure investment such as Ashtead and **CRH (CRH)**.

Investors have been over-optimistic with regards to the opportunity with many people assuming an immediate boost to earnings. The reality is that Trump's spending plan will take time to realise... if at all.

As for the miners, you'd have to look at valuations and take a view on individual commodities. Analysts say Rio Tinto is among the miners most at risk near-term given its dominance in iron ore where the outlook is negative.

Silver and gold producer **Fresnillo (FRES)** at £15.18 is trading on 1.8 times net asset value, as based on forecasts for 2018 by stockbroker Numis. That's at the upper end of where we would expect decent gold miners to trade in a bullish commodity price environment.

We're only in the early stages of a commodity price recovery, certainly nowhere near prime conditions where you could justify gold miners trading on up to 2.0 times NAV.

If you don't want to sell any of your FTSE 100 holdings, you may wish to consider hedging your position through buying a short ETF on the index. It would profit from any decline in the value of the FTSE 100. (TS/DC)

# Is the motor sector on a PCP collision course?

More stringent affordability checks threaten to dent car dealers' earnings

Drivers could face tougher affordability checks to qualify for car loans, according to recent press headlines. This could have negative implications for many of the car retailers whose shares trade on the London stock market.

The potential clampdown on car loans is related to concerns that a new financial crisis could be brewing. Drivers may soon have to complete an affordability test similar to the ones used when applying for a mortgage.

Reports state the amount of money being borrowed to buy new cars has trebled over the past eight years to more than £30bn, although booming higher ticket new car sales and a soaring UK population mean the size of the market has also grown.

**9 OUT 10 NEW CAR SALES ARE FINANCED BY PCP FINANCE**

### PCP PILE-UP?

An estimated nine out 10 new car sales are now financed by 'personal contract plans' (PCP) which can enable people on low incomes to afford brand new cars.

Drivers pay a small upfront fee and then a monthly 'rental' before buying the car outright or handing back the vehicle and upgrading to a different car after several years.

Headlines predicting a financial apocalypse on a par with the credit crunch are teetering toward the hysterical.

Daksh Gupta, respected chief executive of automotive retail and leasing group **Marshall Motor (MMH:AIM)**, informs *Shares* that 'all of the finance houses we deal with do affordability tests and credit checks; it's in their interests.'

He says 'our default rate with both of our two biggest funders is well less than 1% and has been for years. It is not the dealer that makes the lending decision, it is the finance company, and they have stringent lending criteria.'

Gupta is also keen to stress that PCP funding is highly affordable, typically with 'low single digit APRs (interest rates)'. It is also an asset-backed form of financing.

'Ultimately PCPs enable customers to drive newer, more economical cars for affordable payments whilst enjoying their residual value being protected,' says Gupta.

### CAR SALES BOOM

'PCP has been massive for the new car market,' concedes Zeus Capital analyst Mike Allen. 'At over 80% penetration that is what has been driving the new car market.'

Helped by PCP, the UK's new car market grew by 8.4% in March, with 562,337 new cars registered according to the Society of Motor Manufacturers

& Traders (SMMT). That makes it the biggest month since records began. However, the latest SMMT forecast points to a 5% year-on-year decline for 2017 as a whole.

Allen comments: '2017 is expected to remain another competitive year with almost 70 new launches planned over the next 12 months giving consumers significant choice with low cost finance still available.

'We believe new car price inflation will become a more prominent issue in 2017, and we believe there is evidence of this coming through albeit with monthly payments on PCPs maintained, offset by lower dealer contributions, slightly higher interest costs or higher customer deposits required.

'While the first quarter of 2017 will go down as a record for the industry, we believe the true impact of Brexit has yet to play out,' adds Allen.

'OEM (original equipment manufacturer) behaviour over the coming months is likely to be increasingly forex driven, and we are monitoring consumer confidence trends carefully.

'We also note the change in (vehicle) tax rules that came into force in April. As the SMMT has stated this has likely pulled sales forward into the first quarter, meaning registrations trends will likely weaken from here.'

**'BALANCE SHEET STRENGTH ACROSS THE SECTOR IS GENERALLY ROBUST, AND WE ARE LIKELY TO SEE FURTHER CONSOLIDATION ACTIVITY AS SMALLER OPERATORS BECOME MORE DISTRESSED IN OUR VIEW.'**

## SHOULD I STILL INVEST IN CAR RETAILERS?

For those still keen to invest in the sector, Allen believes the PLC dealer valuations are attractive and remain close to trough levels.

'Balance sheet strength across the sector is generally robust, and we are likely to see further consolidation activity as smaller operators become more distressed in our view.

The Zeus Capital expert also points out that motor dealers typically generate roughly 60% of their pre-tax profits during the first half, so the bumper March sets them up nicely for the rest of 2017.

'We believe our forecast assumptions are very conservative and more than compensates for this risk and therefore believe the sector remains attractive on a long-term basis,' says Allen.

## STOCK IDEAS

We agree with Allen's view that car retailers with flexible balance sheets and strong operating models are the ones to own.

Allen name-checks **Vertu Motors (VTU:AIM)**, which has 'the strongest balance sheet in the sector', and admires the Mark Lavery-led franchised motor dealer **Cambria Automobiles (CAMB:AIM)**.

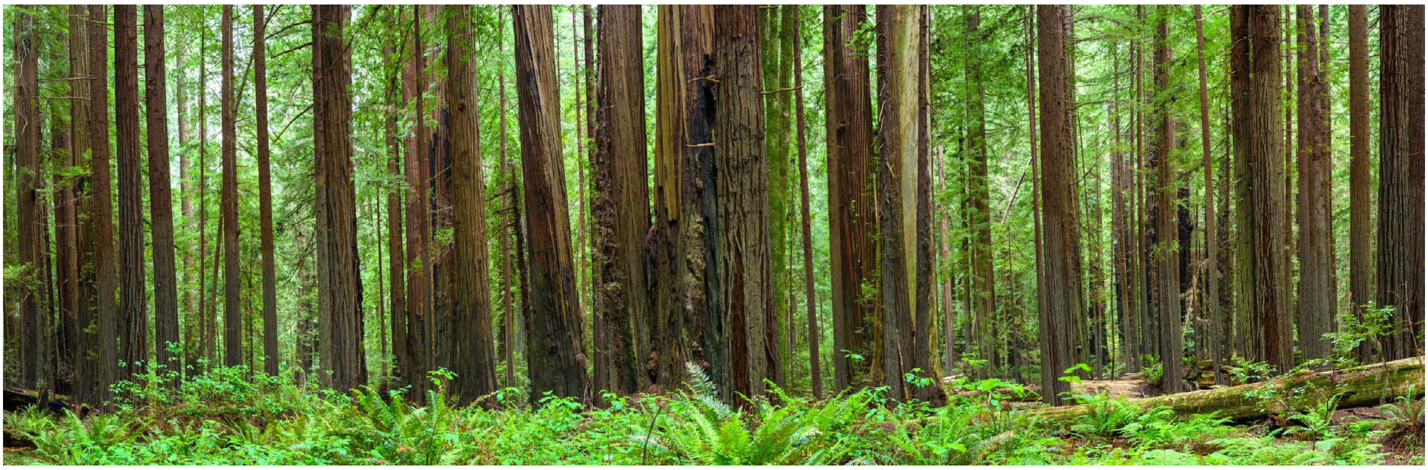
We would also highlight the attractions of Gupta's Marshall Motor, growing organically and via acquisitions and boasting a property-backed balance sheet.

The UK's seventh largest dealer group's latest annual results showed underlying pre-tax profit up 60.4% to £25.4m in 2016 and a bigger-than-expected 85% dividend increase to 5.5p.

Marshall Motor is trading at 170p, a discount to latest reported net assets per share of 188p, which to us represents a strong buying opportunity. (JC)

# Fund manager reveals sources of good income

Henderson High Income Trust may interest anyone wanting generous dividends



With the number of retirees set to grow by an estimated 50% over the next 20 years, there is a pressing need for income to fund those who fall into this demographic.

Looking at where cash and bonds are at the moment, traditional sources aren't going to fund it, but perhaps **Henderson High Income Trust (HHI)** could provide one part of the solution.

The investment trust, which yields in the region of 4.8%, is differentiated from similar products due its capacity to hold bonds according to manager David Smith.

While it can hold up to 40% of its portfolio in bonds, the current amount sits at a historic low of just 10% given the lack of yield, or income, offered by the assets at present.

Smith doesn't dismiss the idea of increasing the trust's bond holdings. For now, he sees more value from equities on a yield basis than bonds.

### OPPORTUNITIES IN THE FINANCIAL SECTOR

Henderson High Income Trust has increased its holdings in the banking sector. There is a growing belief among fund managers that regulatory pressures and endless fines on banks may have peaked.

Smith favours **Lloyds Banking Group (LLOY)** and **Barclays (BARC)**, in particular, having increased holdings in these banks following their fall in price after the Brexit referendum. Despite being a UK investment trust, Smith says he also added Dutch retail bank ING so to not increase UK domestic risk.

**THE FUND MANAGER LOOKS FOR THREE TYPES OF STOCKS:**

**1. Stable growth**

**2. Quality cyclicals**

**3. High yielders**

### GOOD LONG TERM TRACK RECORD

Although the trust has a stellar longer term track record, more recent performance has lagged the benchmark.

For the year ending 31 December 2016, the investment trust's net asset value return was 8.9%. That compares with 15.5% total return from its benchmark (80% FTSE All Share, 20% ML Sterling Non-Gilts).

Over the five years to 28 February 2017, Henderson says its investment trust has delivered

89% net asset value total return versus 74% from the benchmark.

Smith is candid when it comes to the fund's underperformance last year. It was hurt by a double whammy of being underweight in mining, oil and gas as well as being exposed to other UK stocks when Brexit struck.

The large blue chip mining and energy companies benefited from the drop in sterling and firms such as **Sky (SKY)** and **BT (BT.A)** were negatively impacted by the Brexit vote and weaker investor sentiment towards the UK.

The fact that some of the large miners cut their dividend payments 'makes it hard for us to have exposure to the mining sector in that scenario', says Smith. He is running an income trust, after all.

## TARGETING THREE SILOS

The portfolio comprises three categories of stock. 'Stable growth' includes companies such as **RELX (REL)** and **Hilton Food (HFG)**.

'Quality cyclicals' include companies with strong balance sheets capable of earning good returns, such as **Whitbread (WTB)** and **Victrex (VCT)**.

'High yielders' are the third category including stocks such as **Imperial Brands (IMB)** and **National Grid (NG.)**.

Smith says he bought **Whitbread (WTB)** as following Brexit its valuation became more attractive. Due to concerns over core inflation and its resulting impact on UK consumers' disposable income, he sold pubs operator **Marston's (MARS)** and holiday provider **TUI (TUI)**.

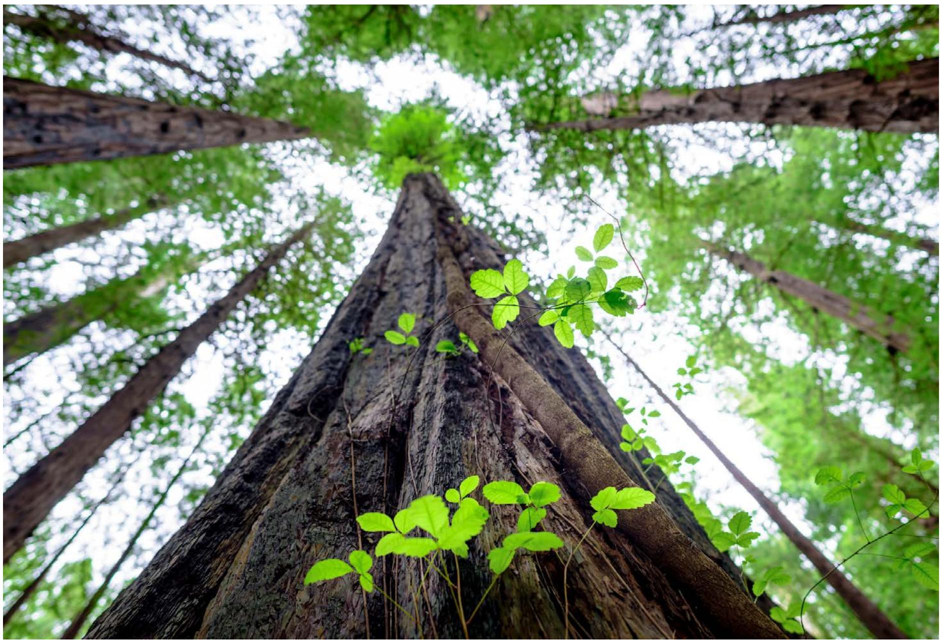
## DIVERSE SOURCES OF INCOME

The trust's income by sector is extremely diverse; no one company makes up for more than 5% of it. Despite the fact that the top 20 UK stocks make up 70% of market income, Smith says it 'doesn't mean you have to build a concentrated portfolio to get UK income'.

'Looking at dividend yield in isolation can be a misleading guide to value,' says Smith. He adds that it's important for a company not just to sustain the dividend but grow over the long term.

For this reason, he's happy to own companies with low dividend yields as long as they can grow the payment over time.

He adds that due to the relatively small size of the trust, it has the ability to move up and down market cap scale to find opportunities in all the market cap areas that can grow dividends in the long term. Its annual dividend has increased yearly since 2012. (DS)



### HENDERSON HIGH INCOME TRUST (HHI)

Share price: **190p**
Net asset value: **187.7p**
Market cap: **£213m**

**Top holdings:**
**British American Tobacco**

**AstraZeneca**

**Royal Dutch Shell**

# Funds to play British bargains

UK small and mid-cap investment trusts available on wide discounts

One of the main factors that determines the average investment trust discount in a particular sector is investor sentiment towards that part of the market.

The most out-of-favour areas currently include the UK small and mid-cap funds, which creates a contrarian opportunity for those who are prepared to take a long-term view.

According to data from Numis Securities Research, the UK Smaller Companies sector was recently trading at an average discount of 14.7% with many of the individual funds available at 15% to 20% less than their underlying net asset value.

The small and mid-cap stocks in which these funds invest tend to be more dependent on the UK economy for their earnings than the multi-nationals in the FTSE 100 index. This suggests that it is likely to be concern about the possible impact of Brexit that is responsible for the negative sentiment at present.


## COULD THE UK DO BETTER THAN EXPECTED?

June's general election could ultimately be good news for the UK economy.

Small and mid-cap funds with large UK exposure could do extremely well if the economy holds up better than expected. They would also be less vulnerable than the large cap and global funds if the pound continues to recoup some of its post Brexit losses.

## INVESTMENT OPPORTUNITIES

Analysts at Stifel have recently highlighted the contrarian opportunity offered by UK small and mid-cap trusts. Their report points out that these areas were a notable laggard in 2016 and experienced widening discounts.

One of the funds they highlight is the £173m **Schroder UK Mid Cap (SCP)** which aims to generate a total return in excess of the FTSE 250 index. It is trading on a 20% discount to net asset value (NAV) despite the fact that it has a decent long-term track record with the share price and NAV returns comfortably outperforming its benchmark over 10 years.

Stifel has a positive recommendation on the £287m **BlackRock Throgmorton Trust (THRG)** that is trading at a discount of 20%. The small cap fund has a strong long-term track record and is unusual as the manager can short stocks that he thinks will fall in value.


## SMALL CAN BE BEAUTIFUL

The team at Numis Securities Research favour **Aberforth Smaller Companies (ASL)**, which has a well-defined value approach; and **Henderson Smaller Companies (HSL)** which has a good record under manger Neil Hermon through a diversified portfolio focused on growth at a reasonable price.

Numis acknowledges that Aberforth's returns look dull, but it rates the management team highly and says there is a role for a value-orientated fund. Aberforth Smaller Companies has a market value of £1.16bn and is trading on a 15% discount to NAV. The share price is up 118% over 10 years, which is slightly behind the benchmark and sector average.

Henderson Smaller Companies has a market cap of £547m and Numis considers it to be an attractive core holding for those who want exposure to small cap stocks. Its manager looks for undervalued companies with good growth prospects, sound financial characteristics and strong management.

It is trading on a 15% discount, which is in line with its 12-month average. It has a diversified portfolio of 112 stocks with the share price up 171% over 10 years.

## BEST IDEAS LIST

The investment companies team at Winterflood Research have included three UK small cap funds in their 2017 Model Portfolio. These represent their best ideas and are the funds that appear well-placed to outperform their peers on an 18 to 24 month view through a narrowing of the discount or outperformance of the underlying portfolio.

Their recommendations in this area are: **BlackRock Smaller Companies (BRSC)**, **River & Mercantile UK Micro Cap (RMMC)**, and the aforementioned Henderson Smaller Companies.

They note BlackRock Smaller Companies has an impressive performance record, both in terms of its relative performance and consistency, having outperformed the benchmark in each of its last 13 financial years. It also has a good record against the sector average.

Mike Prentis, the manager, looks for companies that have five sustainable growth characteristics, namely: strong management, strong market position, sound balance sheet, cash generative, and with a track record of growth.

He has put together a diversified portfolio of 167 stocks with the 10 largest positions accounting for just 20% of the assets. The shares are trading on a 17.5% discount to NAV and have returned 235% over the last 10 years.

River & Mercontile UK Micro Cap aims to generate long-term capital growth from a diversified portfolio of UK micro-cap equities that typically have a free float market value of less than £100m. Its manager, Philip Rodrigs, believes this part of the market is often overlooked, but has historically generated superior returns.

The £104m fund was created in December 2014 and has generated an NAV return of 50% since the launch. Its shares are currently trading on a 3.6% discount, which is slightly less than the 4.6% average discount calculated over the last 12-months. (NS)

# The packaging firm on the cusp of the FTSE 100

You should get to know DS Smith as it may soon reach the top league of London's biggest listed firms


It's been around since 1940, listed on the London stock market since 1986 and just narrowly missed out on FTSE 100 promotion in March. You'd think we were talking about a household name, but £4bn packaging group **DS Smith (SMDS)** is unfamiliar to most people. That may soon change.

If you've bought a new TV or PC, had a parcel delivered after buying something online or seen food products sitting in cardboard display units on a supermarket shelf, then you'll be familiar with the type of robust packaging produced by DS Smith.

Its customers include **Unilever (ULVR)**, Nestle and Procter & Gamble. These are giants of the consumer goods industry.

DS Smith now also collects and recycles packaging, lowering its own costs while helping customers make progress in achieving their own green targets.

Packaging is a steady industry that tends to grow roughly in line with GDP. That's about 2% annually at the moment across its key European markets. The rise of internet shopping is one of the levers helping the company expand at a faster rate than 2%.

## HEAVY SPENDING

DS Smith has spent about £500m on acquisitions over the past few years, mainly in Europe but also in the US through Indianapolis-based Parish Manufacturing.

It's been able to do big deals by leveraging its own scale and borrowing capacity in the knowledge that debt can be rapidly paid down from its own reliably large cash flow.

The company threw off £237m of cash from operations in the six months to 31 October 2016; and it is on track to beat the £363m generated in the last full year.

Hand-in-hand with expansion comes production streamlining. This led to the 2015 closure of its 250-year-old paper mill in Wansbrough, Somerset. Updating its creaking production lines was deemed too expensive.

That was bad news for the local community and not great for shareholders given the £79m associated cost of shutting down

Wansbrough (although this headline figure also included other closures, restructuring and acquisition expenses).

Pre-tax profit for the year to 30 April 2016 grew by 3% at constant currencies to £201m. Perhaps a better indication of performance is adjusted pre-tax profit (before amortisation and associate charges) which rose 15% to £332m.

Stockbroker Stifel forecasts pre-tax profit will grow to £378.4m in the year to 30 April 2017 and then hit £416.2m a year later. Those are very decent levels of growth for a company the size of DS Smith, in our opinion.

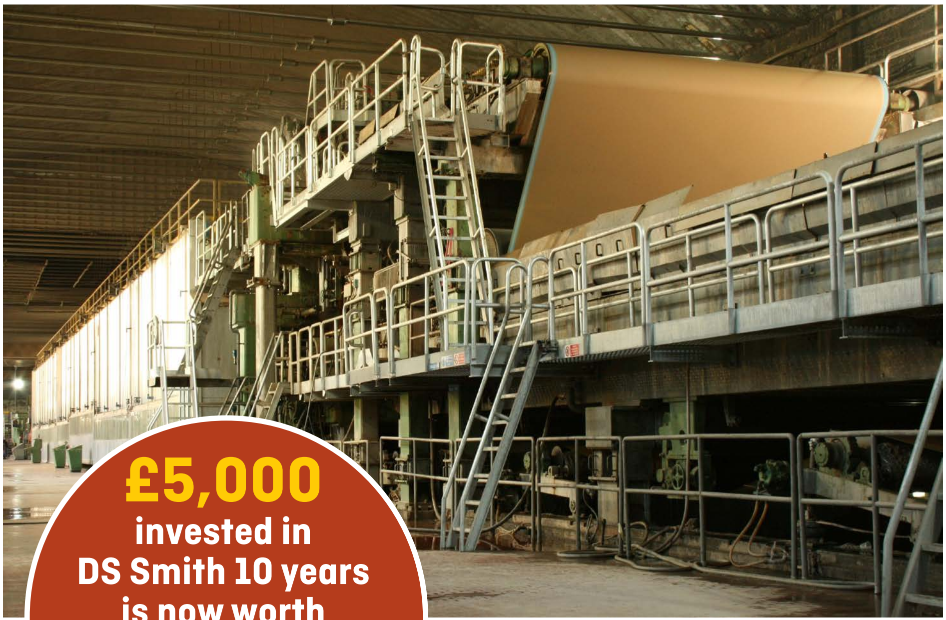
Stifel has a 515p price target, which implies about 23% upside from the current 418.5p share price. DS Smith is also forecast to pay 14.9p dividend over the next financial year. That would equate to a 3.5% prospective dividend yield.

Adding the 23% implied share price upside to the 3.5% potential yield gives you an indicated 26.5% potential total return over the next year – which is very attractive. We'd caveat that statement by saying such a return is not guaranteed.

### TELL ME MORE ABOUT THE INVESTMENT CASE

Arguably, the criticism levelled at DS Smith most is its implied cyclicality. By that, we mean the company's fortunes could rise and fall in line with global economic strength or weakness.

Analysts, including JP Morgan's Alexander Mees, increasingly argue that earnings volatility is being reduced by concentrating on the FMCG (fast moving consumer goods) space.



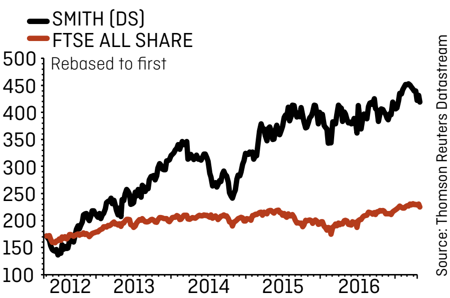
**£5,000 invested in DS Smith 10 years is now worth £19,055 with all dividends reinvested**

That debate is likely to keep running although the group's growth record during the past few years is fairly unblemished.

Input costs remain important factors to monitor. For example, you should look at the raw fibre materials used to make paper and cardboard, and energy prices given a paper mill's heavy use of electricity.

Both of these costs can be partly offset by the use of energy efficient technology, while some of any extra expense has often been successfully passed on to customers.

'It is the proof of DS Smith's business model that, in general, market input changes cause variation in earnings expectations of no greater than the range of forecast error,' says Hector Forsythe, analyst at investment bank Stifel.




### A CLOSER LOOK AT IMPORTANT NUMBERS

Net debt at the half year stage on 31 October 2016 stood at £1.16bn. First half interest payments of £31m are comfortably covered by earnings and cash flow.

Return on average capital employed stood at 15.1%, which is a healthy figure and at the upper end of its 12% to 15% target range. This ratio reveals the profitability against investments made in the company.

**SHARES SAYS:** ↗

**DS Smith has adapted an old economy business to the digital age well. We see more incremental upside to the share price and believe it stands a good chance of getting in the FTSE 100 in the near future. (SF)**

**BROKER SAYS:** 8 5 0

# Keep buying JD Sports for overseas success

## Sportswear retailer remains a highly attractive stock for investors to own

Record full year results (11 Apr) from **JD Sports Fashion (JD.)** confirmed a third consecutive year of double digit store like-for-like growth from the core Sports Fashion business. Can it keep going?

Toughening comparatives suggest this breathless same-store growth rate will be hard to sustain. There are also concerns about high levels of personal debt among UK consumers which could eventually curb retail spending.

We still rate the stock as a 'buy' because the branded sportswear retailer's global growth potential is immense.

In particular, we believe the market's focus will increasingly be on its international business which is in excellent health.

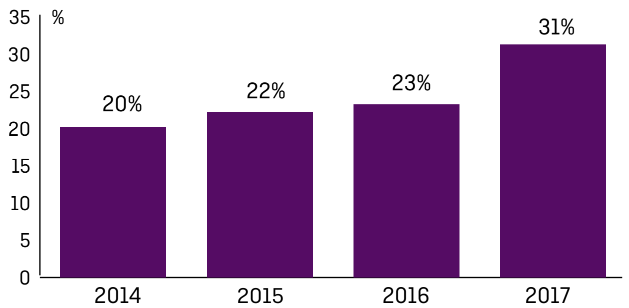
JD Sports now generates approximately 30% of its business from outside of the UK, up from 23% a year ago and a mere 5% seven years ago.

'Whilst the core UK Sports Fashion business remains the engine room of the business we are encouraged to see significant growth in other parts of the group,' says Cantor Fitzgerald analyst Mark Photiades.

'JD is now fully recognised by the leading sportswear brands as a major global partner and player and the opportunity for further international growth in Europe and beyond is significant.'

Clearly differentiated from rival **Sports Direct International (SPD)**, Cowgill has successfully turned JD Sports into an important retailer for major international brands, principally Nike and Adidas.

PERCENTAGE OF JD SPORTS' SALES GENERATED OUTSIDE OF THE UK




Source: Cantor Fitzgerald. Refers to financial year ending 31 January.

**£5,000 INVESTED IN JD SPORTS 10 YEARS AGO IS NOW WORTH £113,223**


Cantor forecasts 21.5p earnings per share for the year to January 2018. Based on the latest share price of 447.9p, JD trades on a price to earnings (PE) multiple of 20.8 times. We believe it deserves such a premium rating, given rapid growth and ongoing expansion potential.

'The valuation, in our view, still does not reflect the true value of the JD concept, which is trading in a booming segment of the retail market,' says Photiades.

'The JD format has a great track record growing operating profits by 44% per year over the last three years. It is clearly differentiated from its closest UK competitor, has the support of the leading sports brands in sports fashion and has significant potential to be developed overseas, where it now has clear momentum.'

**BROKER SAYS:** 7 0 0

# Gattaca takes a hit to build a better future

Recruiter suffers profit warning; will a dividend cut be the next bit of bad news?

Specialist tech and engineering recruitment agency **Gattaca (GATC:AIM)** implies it could have avoided a profit warning on 13 April by cutting costs. Instead it made the decision to continue investing in the business in the hope of longer-term gains.

Gattaca has suffered from a higher cost base and subdued net fee income amid softer demand, clients taking longer to make hiring decisions in the UK, as well as some projects being delayed.

Some of the higher costs relate to setting up overseas offices as well as delays in realising back office cost savings.

**8.2%**
**DIVIDEND YIELD**
**...TOO GOOD TO BE TRUE?**

### EYE ON LONGER TERM PRIZE

Chief executive Brian Wilkinson says he didn't want to take short term actions on costs to maintain profitability, preferring instead to keep spending money if it puts Gattaca in a stronger position to capitalise on overseas opportunities down the line.

He says there is a growing demand for specialist recruitment firms in developing markets which is the driving force behind ongoing investment.

For example, an engineering operation has been established in China which the CEO forecasts to be one of the company's key international growth drivers over the coming months alongside the US.

We note that another UK-listed staffing agency, **Robert Walters (RWA)**, recently said 'in Shenzhen and Guangzhao they need engineers, not lawyers'. That market backdrop should, theoretically, benefit Gattaca's Chinese business given its engineering focus.

### ACQUISITION SETBACK

Gattaca acquired former AIM-quoted rival Networkers in 2015 to boost its presence both at home and overseas. Unfortunately Networkers appears to have been a bit of mixed bag.

The business is highly dependent on a small number of telecom vendor clients and there has been volatility driven by changes in those clients' workload.

Broker Numis describes the recent profit warning as 'disappointing' although retains its 'buy' rating.

It forecasts pre-tax profit falling 19% to £16.5m in the year to July 2017, before recovering to £20m in 2018.

### CAN IT AFFORD THE DIVIDEND?

Gattaca is forecast to pay 23p per share dividend in 2017 and 2018, implying a prospective 8.2% dividend yield.

We would heed caution with prospective yields in excess of 6% as higher figures are the market's way of saying it doesn't believe the dividend is sustainable.

Numis' financial model implies Gattaca will generate £9.1m in free cash flow in the year to July 2018, and pay out £7.2m in dividends. That doesn't leave much room for further business investment unless it takes on more debt.

We are therefore sceptical over Gattaca's ability to sustain dividends at 23p unless earnings really pick up. (DS)

# WANdisco makes cash burn breakthrough

New business push and cost control is set to pay off

Data replication technology developer **WANdisco (WAND:AIM)** is rebuilding investor confidence as it passes a vital cash flow breakeven milestone.

Shares in the Sheffield and Silicon Valley-based company soared 17.5% to 452.5p on 24 April as it announced that cash burn had been slashed to zero for the three months to 31 March 2017. WANdisco has significantly streamlined its cost base during the past year.

The excitement was intensified by news that the firm had also secured a $4.1m volume-limited, perpetual licence for its *Fusion* big data replication platform.

WANdisco's technology allows users to update multiple data storage server computers instantaneously. This cuts downtime in the event of power outages or cyber attacks, for example, and is hugely important for high volume internet business users such as online retailers or banks.

The recent award is the company's single biggest contract to date but also important is that it was secured through its channel partner agreement with US technology giant IBM. Amazon Web Services and Oracle are among WANdisco's other channel partners.

The customer is a 'major financial services multinational,' according to the announcement and *Shares* understands the technology will be specifically used to transfer data between the client's operational and disaster back-up data storage bases.

**SHARES SAYS: ↗**
**There's an exciting growth opportunity if progress can be maintained, Stifel analysts have a 623p price target on the stock. Buy at 452.5p. (SF)**

**BROKER SAYS:** 1 2 0

## Digital driver for Tax Systems

MIDDLESEX-BASED **Tax Systems (TAX:AIM)** has bolstered its sales, technology development and senior management. The move is designed to put the company is a firm position to help UK organisations meet the Government's *making tax digital* initiative by 2020. Tax Systems supplies corporate tax reporting software to more than 1,000 clients, including 23 of the top 25 UK accounting firms, and 43 of the FTSE 100. (SF)

## Debt-free Trifast is looking healthier

SPECIALIST INDUSTRIAL fastenings engineer **Trifast (TRI)** is expected to emerge virtually debt-free by the end of its current financial year. The Sussex-based business supplies bespoke solutions to motor manufacturers, heavy industry and electronics customers across Europe and Asia. Strong cash generation is expected to leave net debt at just £0.1m for the 12 months to 31 March 2018. (SF)

## Small businesses are feeling buoyant

OPTIMISM AMONG small and medium sized enterprises is at its highest point since the middle of 2013, according to the latest Quarterly Enterprise Index from asset manager Smith & Williamson. The report shows optimism is 30% higher than in the last quarter of 2016 and 85% of entrepreneurs and small business owners are planning for growth. It says 80% are optimistic about their prospects over the next 12 months. (TS)

**KEY**

- **Main Market**
- **AIM**
- **Fund**
- **Investment Trust**