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SHARES

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PLUS

TOP SLICED: THE MANAGER WHO SOLD APPLE BEFORE THE WARNING

BOARDROOM BATTLE: QUEST FOR CONTROL OF SMALL CAP TRUST

RETIREMENT ISSUES: YOUR PENSION QUESTIONS ANSWERED

Have the markets become too negative?

We look at the prospects for a turnaround in fortunes for equities

Amid the relief rally which followed US Federal Reserve chief Jerome Powell's conciliatory comments on interest rates (4 Jan), one thing Powell said seemed somewhat curious.

He observed that markets were 'well ahead of the data' in pricing in downside risks. While in one sense this was worthy of note, given he was speaking in the aftermath of a very strong US jobs report, in another he need hardly have pointed that out, given markets are always 'ahead of the data'.

After all, 'the markets' are made up of a multitude of trades by countless individual investors all of which are taking a view on how the future will pan out.

It is crucial that every investor understands this point as it is how a business is likely to perform in the future, not how it has performed in the past, which will dictate the future direction of its share price.

> **Investors aren't cautious without reason**

Another thing to bear in mind is that markets are not always 100% efficient and will often overshoot on both the upside and the downside. We discuss the value opportunities this can create for investors in this week's main feature.

This tendency to overshoot creates the possibility that market sentiment has become too depressed through a period which on Christmas Eve saw every sector but one (the traditionally defensive consumer staples space) on the S&P 500 trade in 'technical' bear market territory. This is defined as being more than 20% down on their most recent high.

TIME FOR AN UPGRADE?

A recent report from the strategists at investment bank Morgan Stanley suggested that two of the three elements required for an upgrade to its market view were in place.

They note that valuation 'has been improving rapidly' with equities as an asset class looking cheaper after the correction, with the forward earnings multiple for global stocks now below 13-times.

Further they observe that sentiment is 'cautious, but not extreme' adding that net bullishness of US retail investors is the lowest since 2009, something they describe as a good sign.

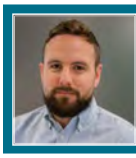
The only sticking point is fundamentals or in other words what's happening in the real world. They comment: 'Cheaper prices and more bearish investors raise the chance of a bounce. But any sustainable rally will need fundamental support. And here is where the challenges remain most serious.

'Investors aren't cautious without reason; there are serious problems that have carried over from 2018 to 2019, some of which are still underestimated on Morgan Stanley forecasts.'

Still, the team believe a number of things could happen to change the fundamental picture and provide a catalyst for shares.

These include: compromises in the face of market weakness from the Trump administration on government funding and trade; a more market-friendly approach from the US Federal Reserve; stimulus from China; only a *modest* reduction in US growth; 'ok' fourth quarter earnings; and the UK avoiding no-deal Brexit while European growth rebounds.

They see a chance of at least some of these occurring by the end of the first quarter and *Shares* will itself be keeping close tabs on all of these areas in the weeks ahead.



By **Tom Sieber** Deputy Editor

9.3% p.a.

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Is IAG putting dividend at risk with Norwegian Air pursuit?

Citi is worried that Norwegian's debt pile could result in bad news for investors

Investors attracted to British Airways-owner **International Consolidated Airlines (IAG)** for its near-5% dividend yield could face a dividend cut if its acquisition of Norwegian Air goes through.

Analysis by investment bank Citi says the ratio of free cash flow compared to the dividend would fall from approximately 2.3-times to below 1.0 times if a takeover occurred. A free cash flow-to-dividend ratio of less than one would, if the dividend is maintained, imply debt is being used to prop up payments.

International Consolidated Airlines has a history of steady dividend growth over recent years so any cut in the payout may come as a nasty surprise and could put the shares under pressure.

In 2018, the airline was rebuffed twice by Norwegian, but could return with another bid. If it cannot acquire Norwegian, the company says it will sell its stake of 4%. As we write it is yet to offload the shares.

Norwegian sells competitively priced seats on long-haul routes, which could help International Consolidated Airlines offer cheaper fares, particularly to the US.

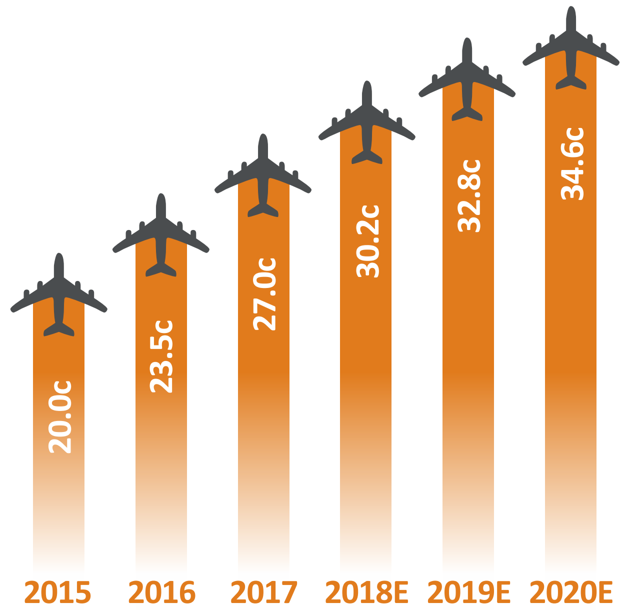
The takeover attempts have been branded as opportunistic and undervaluing Norwegian, which reportedly faces bid interest from other rivals, including German carrier Lufthansa.

While International Consolidated Airlines is in reasonably robust shape, loss-making Norwegian is not. It is struggling with sector-wide issues such as Brexit, volatile oil prices and spiralling costs, which have pushed the business further into the red.

IS THE DIVIDEND CURRENTLY SAFE?

On a free cash flow basis, International Consolidated Airlines currently looks to have the dividend reasonably well covered. Free cash flow is vital to look at as it focuses purely on leftover cash after money has been factored in for operational needs.

IAG: ANNUAL DIVIDENDS



Source: SharePad, 8 January 2019

According to analysts' data from Refinitiv, free cash flow in 2017 of around €2bn easily covered a total outlay on dividends of €512m payout in the year to 31 December 2017.

While free cash flow is forecast to nearly halve to €1.23bn in 2018, this still comfortably covers an estimated €558.1m to be paid out in dividends in 2018.

Looking ahead to 2019 and 2020, free cash flow is forecast to remain steady at €1.2bn while annual dividends are forecast to increase to €624m.

International Consolidated Airlines is scheduled to report its 2018 results on 28 February 2019.

By **Lisa-Marie Janes** Reporter

Sky-STV deal throws spotlight on potential ITV profit boost

All eyes on the media sector as re-transmission deals hit the headlines

At the start of this week **STV (STVG)** and Sky announced a five-year deal giving Sky customers in Scotland access to STV's programming in full HD for the first time. This has direct relevance to **ITV (ITV)**, as we now explain.

STV shows will also be available on catch-up using STV Player on Sky Q and Sky+ set-top boxes and mobile streaming from the second half of this year. Programmes include flagship ITV1 shows such as Britain's Got Talent, Coronation Street and I'm a Celebrity.

The news went down well with investors who sent STV shares up 8% on 7 January, giving the company a market value of £145m.

The STV-Sky agreement is a re-transmission deal in all but name. Sky and Virgin Media have insisted in the past that they won't pay to re-transmit ITV1 so there is no direct reference to it in the STV announcement but it seems to be implicit from the programming.

ITV agreed a transmission deal with Virgin Media last year and is due to renegotiate its agreement with Sky this year.

On the basis of the deal with Virgin, analyst Ian Whittaker at broking firm Liberum estimates that a new Sky deal could bring ITV an additional £120m of revenue per year.

That may not seem much given 2017 turnover of £3.1bn but as with the Virgin deal there is no additional cost so the extra revenue translates directly into profit.

ITV's pre-tax profit was £500m in 2017 with Liberum forecasting profit of £777m for 2018, then £858m for 2019 and £1bn for 2020 excluding the uplift from the Sky deal.

Despite the rise of pay-tv and streaming video services ITV's family of channels still had the highest total share of viewing in 2017 with 22% of the market. It also led the television advertising

market with a 48% share.

In its third quarter 2018 trading update in November ITV warned that overall advertising revenue was likely to be down 3-4% in the final quarter as Brexit uncertainty continued.

That would mean advertising revenue for the full year to December would be flat compared with a rise of 6% in the first nine months.

In the last fortnight ITV shares have been trading at 125p valuing the firm at just under 12 times 2018 forecast earnings and under 11 times 2019 forecast earnings.

Disclaimer: The author owns shares in ITV

By **Ian Conway** Senior Reporter

Founder wants back in at Athelney investment trust

Robin Boyle bids to wrest back control of small cap trust

Veteran investor Robin Boyle, the founder and former managing director of small cap focused **Athelney Trust (ATY)**, wants back in at the trust he founded in 1994.

Boyle has called a shareholder meeting (22 Jan) to restructure the board and restore him to his former roles as managing director and investment director of Athelney.

In response, Athelney is consulting shareholders over a possible tender offer for those who want an exit, alongside the issuing of new shares for potential new investors.

CLOSE-RUN THING

'It'll be a damn close-run thing, but I think I'm just the favourite,' Boyle informs *Shares*.

The dispute between the City mainstay and the current board arose over his continuing role in the company after Boyle stepped aside from his executive roles.

Boyle understood he was to stay on as a non-executive director for a period of time. He insists the original draft of the official announcement to the **London Stock Exchange (LSE)** declared he was staying on as a non-executive director, yet the line was removed from the version eventually published.

SOLVING THE SUCCESSION ISSUE

A substantial shareholder, Boyle proposes to work with **Gresham House (GHE:AIM)**, the asset manager with an excellent network in the UK small cap investment space, to grow the trust's size, reduce costs and provide long term succession planning.

The 74-year-old explains he'll be teaching Gresham House investment manager Laurence Hulse 'everything I know about small cap value and income', which means 'the management succession problem is solved at a stroke'.

'My daughter and I have 20.8% (of the shares),' continues Boyle, stressing his EGM vote will be counted.

In the official shareholder meeting release, he also complains: 'I do not see how Athelney's investment strategy can be carried out by someone who spends the majority of his time some 10,000 miles away in a different time zone as is the case currently.'

This reference is to Athelney Trust's managing director, fund manager and significant shareholder Manny Pohl.

As for the Athelney Trust board, it comments: 'On succession planning, in September 2018 it had been amicably agreed between the then directors (Robin Boyle, Manny Pohl and Simon Moore) that there would be a smooth handover from Robin Boyle as fund manager and managing director of Athelney Trust to Manny Pohl over a period of two to three years.

'So the sudden resignation of Mr Boyle was extremely surprising. It is regrettable that a distinguished track record, with 15 years of uninterrupted annual dividend increases, has come to this.

'The board have been working to ensure business as usual for shareholders. Shareholders should feel confident in the ability of the current board and that the new fund manager will be able to deliver on Athelney Trust's objectives of long term growth in both capital and dividends from a portfolio of UK smaller companies.

'The board wants to grow the company so shareholders can benefit from greater economies of scale. Dr Pohl has also agreed to a reduction in the annual management fee from 1% to 0.75%.'

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

Dunelm, Gear4Music, Morrisons and more news from the past week

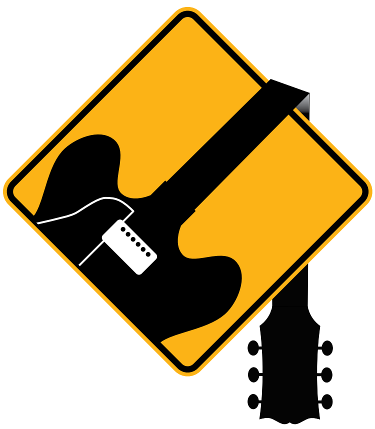
We examine some of the key announcements and the market reaction to them

The amount of corporate news has been fairly limited since the Christmas break as investors await festive trading updates with some trepidation. So far **Next (NXT)** and **Dunelm (DNLM)** have been particularly well received by investors and **Gear4Music (G4M:AIM)** has been the biggest shocker.

Homewares retailer Dunelm saw its shares soar on 7 January after reporting 9% growth in second quarter revenue growth. Its like-for-like store revenue rose 5.7% to £246.4m, while comparable online sales shot up by a forecast-busting 38% to £36.1m. The company also announced plans to launch a new, more flexible web platform to build on the strong contribution from internet-based sales.

Online musical instruments firm Gear4Music was heavily out of favour on 4 January with its shares at one stage losing more than 50% of their value after a major profit warning.

In some respects Gear4Music is a victim of its own success. Sales growth of 41% in the final four months of 2018 was impressive. Yet it hit capacity constraints and will now have to invest to get up to speed. Earnings for the year to 28 February 2019 will subsequently come in below the previous year's result.



Gear4Music's shares fell more than 50%

Pharmaceutical business **Vectura (VEC)** got the thumbs-up from the market with its full year trading update (3 Jan). Despite revenue guidance being left unchanged the company said earnings would be 'materially ahead' of expectations.

Improvements in margin performance, progress on productivity and a better mix of business all contributed to the beat.

In the groceries space **Morrisons (MRW)** was first in its sector with a Christmas update on 8 January and ultimately disappointed the market.

Chief executive David Potts faced a tough task after a bumper festive period the previous time round and like-for-like retail growth of just 0.6% seemed to be the main sticking point for investors. This figure was down from the 1.3% reported in the third quarter and 2.1% growth from a year earlier.

By **Tom Sieber** Deputy Editor

Fortify your defences with 5.8% yielding Henderson High Income Trust

Prudently well-spread trust should appeal to the risk-averse as volatility returns

Risk-averse investors unnerved by the return of volatility, not to mention slowing global economic growth and European political uncertainties, might view share price weakness at the **Henderson High Income Trust (HHI)** as a compelling entry point.

We believe the outlook for income from this highly diversified portfolio is robust. Moreover, the historic dividend yield of 5.8% is attractive and we are confident the dividend will be maintained or increased in future, a facet of the trust that should entice patient portfolio builders.

Managed by David Smith since 2014, Henderson High Income aims to provide a high dividend income with the prospect of capital growth by investing in a prudently diversified selection of well-known and smaller companies alike.

Smith scours the market for overlooked, lower valued companies with solid cash generative business models.

Launched in 1989, Henderson High Income has a strong long term performance record, having generated annualised 10-year price and net asset value returns of 11.79% and 11.54% respectively.

HENDERSON HIGH INCOME TRUST ↗ BUY
(HHI) 161.5p
Stop loss: 110p

Total assets: £272m

The investment trust offers investors exposure to a high and growing income stream. The dividend for the 2017 calendar year was increased by 2.7% to 9.4p and given the trust's ample revenue reserves, dividend growth looks sustainable in what may prove to be more difficult years ahead.

It uses debt to enhance both income and capital returns for shareholders. This includes investing in shares and bonds, with the significant fixed interest portion of the portfolio providing secure income and boosting the trust's overall yield.

Fund manager Smith has an unwavering focus on income sustainability, ever determined to avoid dividend cuts and value traps.

According to the latest factsheet, Henderson High Income's top holdings include dividend paying stalwarts **Diageo (DGE)**, **Royal Dutch Shell (RDSB)** and **HSBC (HSBA)**.

This reassuringly well-diversified portfolio focuses on three types of stocks: 'stable growth' names such as publisher **RELX (REL)** and pork-to-cooked poultry processor **Cranswick (CWK)**; 'quality cyclicals' including packaging outfit **DS Smith (SMDS)** and chemicals concern **Victrex (VCT)**; and high yielders such as tobacco giant **Imperial Brands (IMB)** and fixed line telecoms specialist **Manx Telecom (MANX:AIM)**.

One of the trust's new holdings is **Coca-Cola HBC (CCH)**, the soft drinks bottling business which has scope for margin improvements and a strong balance sheet, giving management the flexibility to deploy capital to accretive acquisitions or return more cash to shareholders.

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

POLAR CAPITAL

THE CHANGES IN HOW HEALTHCARE IS MANAGED, DELIVERED AND PAID FOR

The fast-changing landscape

The structural changes we are seeing in the healthcare industry will benefit an ageing population that both needs and demands better healthcare provision. However, while these demands are driving up costs, the challenge for society is to provide better healthcare to more people for less money.

Given this backdrop, there are two clear investment trends emerging: the first is innovation in the form of new drugs and medical devices; the second is a transformation in how healthcare is being managed and delivered. Traditionally, it has been the smaller companies with more nimble, dynamic business structures that have been credited with innovation. We feel the tide is turning and it is now the larger companies that are transforming healthcare. Over the next decade, it is they who will more heavily influence the way healthcare is managed, delivered and paid for.

The first of these trends is already happening thanks to a move from a fee-for-service model where a hospital or doctor is paid for everything they do, that rewards utilisation, to value-based reimbursement which rewards medical outcomes. This move, plus aligned incentives, will reward those healthcare systems focussed on outcomes, which should ultimately lead to an improvement in the quality of care provided.

We live in a world where consumer expectation of any service has been forever changed by the likes of Amazon and Netflix. People expect everything on demand at the push of a button and access to care is no exception. Instead of having to typically wait at least a week to see a doctor, today's technology allows the consumer to instantly book an appointment online for the following day, or have a video call with a GP allowing a same-day consultation.

The final piece is 'democratised health' where the individual takes more responsibility for their own health. A good example of this is the Apple Watch. The latest version includes an electrocardiogram (ECG) that, while it does not give any diagnosis, will indicate whether or not you need further tests with your GP. This is a new market that is set to develop hugely in the future, with different types of wearable and different types of clinical measurement possible beyond an ECG.

What we need to do as a result is consider the types of company we want to invest given how they are adapting to the changes going on around them and exploiting the new market opportunities. We need to look at not just innovation within the small companies but also innovation and transformation driven by the larger companies.

Our expertise is in healthcare though we are fully cognisant of external market factors such as interest rates and inflation as well as political factors such as Brexit – we spend a lot of time thinking about politics, particularly in the US. The companies we invest in have solid balance sheets, sustainable and growing cash flow, manageable debt levels and, ultimately, what that means for investors is compounding returns. We think those large companies that are transforming healthcare look to be well positioned for growth next year. That is where our portfolio is focused.

Dan Mahony and Jamie Douglas, Fund Managers
Polar Capital Global Healthcare Trust
4 January 2019

Dan Mahony, manager of the Polar Capital Healthcare Trust, explained what he sees as the future landscape for healthcare at the AJ Bell Retirement Conference last December.

To watch him explain these in more detail, please click the image.

This cash-generative oil play has big potential

Eland Oil & Gas is poised to deliver material increases in output in 2019

The potential for significant production growth and exploration success at Nigerian oil producer **Eland Oil & Gas (ELA:AIM)** in 2019 makes this a must-have share for investors with an appetite for high-risk stocks.

We previously flagged Eland as a *Great Idea* in April 2017 and the shares are now trading at nearly twice the 57p level at which we first highlighted the scope for upside.

The advance in the shares has been matched by operational progress on its OML 40 licence. It has seen robust output expansion with 13,500 barrels of oil per day coming from the Opuama field on the licence.

As such, we view Eland as much more than a speculative oil play as it is a genuinely cash generative business, and one which house broker Peel Hunt forecasts could be sitting on net cash of $125.3m by the end of the year.

ANOMALOUS VALUATION

Peel Hunt's forecasts imply an EV/EBITDA (enterprise value-to-earnings before interest, tax, depreciation and amortisation) ratio of 0.6-times.

While oil price volatility and the possibility of delays leaves forecast earnings open to revision, this still seems like an anomalous valuation and one which could move upwards through the course of the year as Eland delivers on its work programme.

ELAND OIL & GAS BUY
(ELA:AIM) 105.5p
Stop loss: 84.4p

Market value: £233m

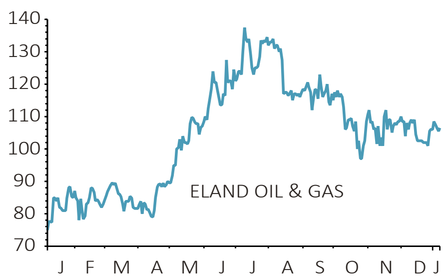
Central to this programme is development drilling on the Gbetiokun field. This is expected to deliver gross production of 15,000 barrels of oil per day from an early production system and the company says it could ultimately deliver output of 45,000 barrels of oil per day.

Although it boasts a long history of oil production and has well established fiscal terms there are clear challenges, particularly around security in Nigeria.

Investors can take some reassurance from the fact the company has demonstrated its ability to deal with these issues. For example, when the Forcados oil terminal, which currently takes its crude, was shut down due to militant attacks in 2016 and 2017, Eland found an alternative route to market by shipping its oil in small tankers.

It is also worth bearing in mind that a company of Eland's size would probably not be able to secure an interest in assets of this scale and quality in more stable operating environments.

In the third quarter of 2019 the company plans to drill a well on its Amo-1 prospect targeting up to 78m barrels of oil equivalent, providing a further catalyst for the share price.



By **Tom Sieber**
Deputy Editor

MONEY & MARKETS

LISTEN TO OUR WEEKLY PODCAST

A good investor keeps their ear to the ground. That's why *Shares* and AJ Bell have launched a new weekly podcast – so you can stay up to speed with everything investing.

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SHARES

AJBell

CODEMASTERS

(CDM:AIM) 180.5p

Loss to date: 1.1%

Original entry point:

Buy at 182.5p, 22 November 2018

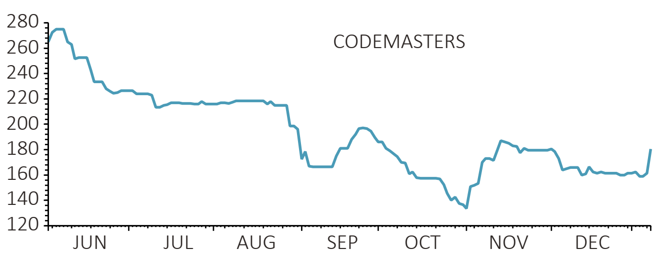
A DEAL TO make a new mobile game with Chinese group NetEase triggered a 12% rise in **Codemasters' (CDM:AIM)** shares on 8 January.

Codemasters will receive at least $8m in revenue over the next three years, of which $4m is expected to come in the current financial year. That prompted the company to guide for its earnings in the period ending 31 March 2019 to beat previous expectations.

'In addition to the apparent cash benefits, we believe the deal also highlights the value and monetization potential of Codemaster's proprietary technology and IP assets, validating the company's position as a leading specialist in racing titles,' says Jefferies analyst Ken Rumph.

The other bit of good news for investors to note is Chinese regulators lifting a suspension on new games in late December 2018. Rumph says this is a positive development for Codemasters as its DiRT Rally 2 title is expected to launch next month and will be published by NetEase in China.

Codemasters formed a partnership deal with NetEase last November whereby the latter would be the exclusive publisher for three of the UK company's upcoming PC titles in China, which is the world's biggest gaming market. Adding a mobile game therefore strengthens the relationship between the two parties.



SHARES SAYS: ↗

These developments should hopefully help to win back the market's support following a patchy time for the share price. Keep buying.

NEXT

(NXT) £48.65

FANTASTIC STOCKS FOR 2019

Gain to date: 16.1%

Original entry point:

Buy at £41.91, 20 December 2018

WE ARE OFF to a flying start after last month flagging retailer **Next (NXT)** as one of top picks for 2019. The company reported robust festive trading in an update (3 Jan) which reignited market interest in the stock.

Against very downbeat expectations and despite a difficult November, the high street stalwart managed to increase full price sales between 28 October and 29 December by 1.5% year-on-year which was exactly in line with the guidance given in September.

Online business did a lot of the heavy lifting with web-based sales up 15.2% through the period. Investors were well prepared for the 9.2% decline in sales achieved in physical stores given the pressures on the high street and so this figure didn't cause widespread concern.

The market was even prepared to look past a small downgrade in guidance for the year to January 2019 from £727m to £723m.

Shore Capital analyst Greg Lawless says Next has a 'strong track record of under promising and over delivering'. He adds: 'The company exerts strong cost and stock control and is highly cash generative, evidenced in the recurring £300m share buy-back programme.'

SHARES SAYS: ↗

We continue to back chief executive Simon Wolfson's ability to steer Next through a difficult backdrop. Still a buy.

How worried should you be about China?

We look at some of the key worries for the market and the stocks and funds which might be affected

A 2 January warning from Apple that sales and earnings for the three months to December were hurt by weak Chinese demand sent a shockwave through world markets, so does this mean we should be worried about China?

According to chief executive Tim Cook, Apple was wrong-footed by 'the magnitude of the economic deceleration in Greater China', blaming it for 'most of our revenue shortfall to our guidance and over 100% of our year-over-year worldwide revenue decline'.

Analysts and journalists have suggested that Apple's selling prices are too high, especially for the iPhone, but could falling handset sales be a sign that Chinese consumers no longer feel like spending?

Last year however the stock market lost 25% of value meaning that $2tn of 'wealth' has disappeared from investors' pockets

MANUFACTURING SURVEYS SUGGEST ECONOMY IS SLOWING

Last week the privately-sponsored Caixin manufacturing purchasing managers index (PMI) surprisingly fell below the key 50 level for the first time since May 2017.

A reading above 50 signals expansion while a number below 50 usually signals contraction.

This was just days after the official government-sponsored PMI fell to its lowest level since February 2016.

Moreover in the quarter to the end of September, Chinese GDP growth was 6.5% which was below estimates and the lowest level since the financial crisis.

Sensing a slowdown, commodity investors have been piling out of copper, where China is the world's largest consumer, and into gold and silver.

As a result copper prices are now at 18-month lows while gold prices are at six-month highs.

ARE TRADE TARIFFS TO BLAME?

It is hard to gauge the extent to which a slowdown in Chinese demand is due to trade tariffs.

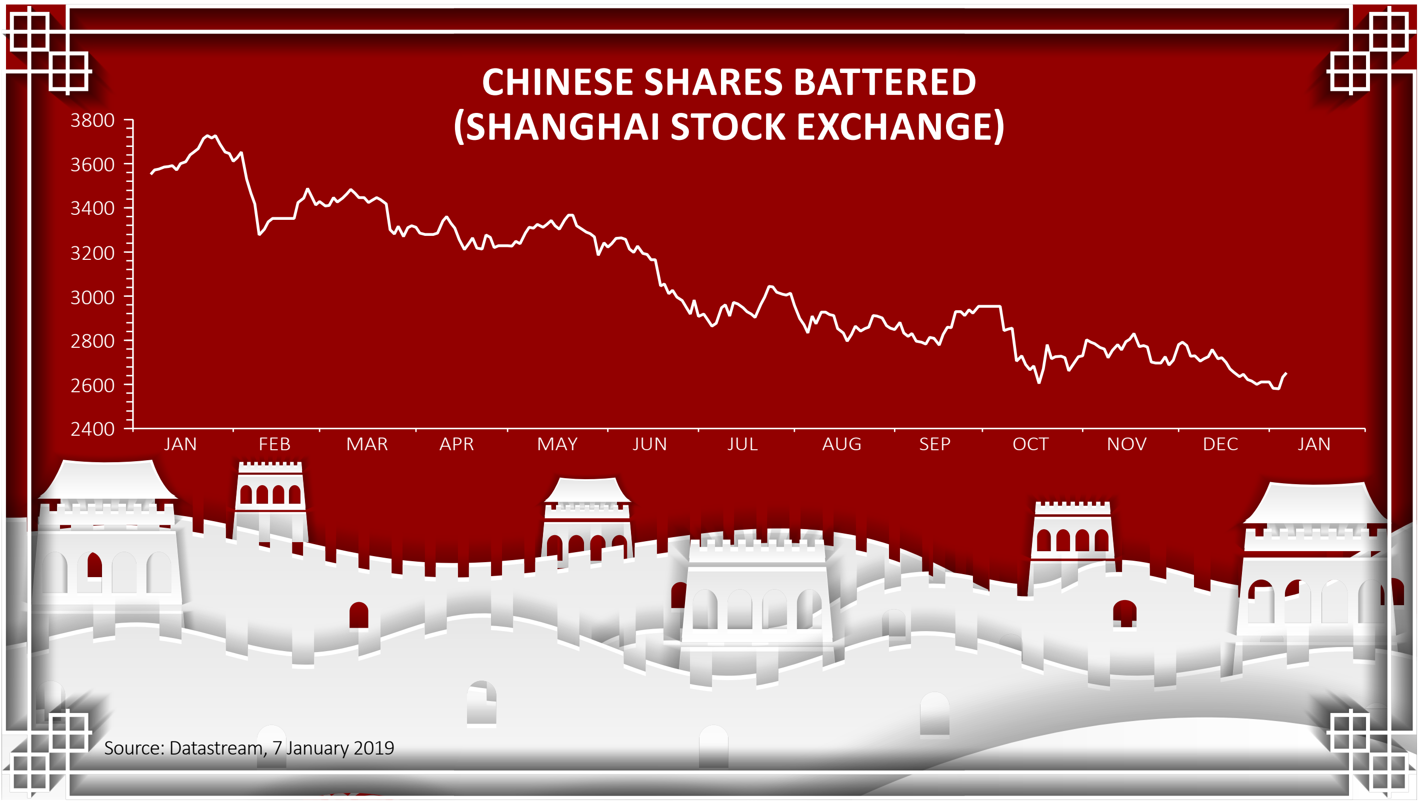
The 25% tariffs slapped on Chinese steel imported into the US from March last year have effectively stopped exports dead in their tracks. That has meant a surplus of steel on world markets which has depressed prices.

However Chinese exports overall have grown this year with November's trade surplus hitting nearly $45bn, the largest level since December 2017 and well above the market forecast of $34bn.

China's trade surplus with the US, its largest export market, hit a record high of $35.5bn in October as exports outpaced imports suggesting that Trump's tariffs may actually be hurting US firms more than Chinese firms.

US manufacturers are hardly dancing in the streets, with the much-followed Institute of Supply Management's PMI index of factory activity suffering its biggest drop last month since October 2008, sending tremors through US stocks.

Trump's reaction has been to call a 90-day truce in the tariff war, while US and Chinese trade negotiators are due to meet in Beijing this week in a bid to avert further trade tensions.



Source: Datastream, 7 January 2019

IS THE DOMESTIC ECONOMY SLOWING?

Consumption accounts for a steadily growing share of the Chinese economy but in a worrying sign retail sales growth hit its lowest level in 15 years last month.

Car sales have actually gone into reverse falling 18% in November, the sixth consecutive month of declines.

The total number of vehicles sold last year will be down on 2017, the first annual fall since the early 1990s. China is the world's largest passenger-car market.

Part of the reason for lower sales is a government crackdown on non-bank lending such as peer-to-peer platforms, which is part of a wider policy of reining in easy credit.

Another part is that Chinese consumers have tended to rely on the stock market and property prices to generate surplus income.

Last year however the stock market lost 25% of value meaning that $2tn of 'wealth' has disappeared from investors' pockets.

Also property values, which have been rising for many years, have levelled out with new home prices in Beijing and Shanghai more or less flat over the last year.

The government is doing what it can to stimulate the economy, reducing business taxes and cutting its reserve requirement so that the banks can keep lending, but investors seem unconvinced.

WHICH STOCKS COULD BE AFFECTED?

Plenty of UK stocks have exposure to China but miners and luxury stocks look to be the most exposed in terms of sales and profits.

On the day that Apple warned, mining stocks were instantly marked down with **BHP Group (BHP)** losing 2%, **Antofagasta (ANTO)** losing 4% and **Glencore (GLEN)** losing 4%.

Meanwhile clothing firm **Burberry (BRBY)** dropped 6% and in Paris shares in luxury conglomerates LVMH and Kering lost 4% and 5% respectively.

Aston Martin Lagonda (AML) saw its shares fall 3% as most of its growth this year has come from China.

In terms of smaller-ticket consumer spending, drinks makers **Diageo (DGE)** and Remy Cointreau generate significant sales in China and consumer health giant **Reckitt Benckiser (RB.)** has large exposure through its infant formula business.

In the investment trust world **Edinburgh Dragon Trust (EFM)** is a pure play on China and therefore worth monitoring.

By **Ian Conway**
Senior Reporter

'Will there be a cap on tax-free withdrawals from pensions?'

AJ Bell expert Tom Selby a trio of questions in this week's column

To kick off 2019 we've got a bumper edition of 'Ask Tom', with resident AJ Bell pensions expert Tom Selby answering three of the questions sent in over the festive period.

By **Tom Selby**
AJ Bell Senior Analyst

Question 1 Anonymous

My pension closed at age 60 and I transferred what monies were in it (£4,000) into a SIPP. I did not claim any tax relief on it. It is now with another provider and I still do not claim any tax relief on it, even though its value has increased.

Can I claim tax relief or not?

The way pension tax relief is added to your fund depends on that type of scheme you saved in. If you were in a defined benefit (DB) scheme then tax relief will have been added automatically, so it will be included in any money you transferred to a SIPP.

If it was a 'net pay' defined contribution (DC) pension – where your contribution is taken from your salary before any tax has been paid - then your tax relief should also have been added automatically, unless you were earning

below the personal allowance at the time you made your contribution.

If it was a 'relief at source' DC scheme then your provider should have added on tax relief at the basic-rate (20%), regardless of how much you were earning at the time. You would then be able to claim back an extra 20% or 25% if you were a higher or additional-rate taxpayer through your tax return.

So it's likely you'll have received some or all of the tax relief you were entitled to automatically, although this will depend on the type of scheme you were in.

If you do think you have missed out on tax relief it's worth writing to HMRC to set out your case. You can find details on how to do this here.

However, even if you are eligible to reclaim tax relief this will based on the value of your original contribution only, so won't take into account any investment growth your fund has enjoyed since.

Question 2 Clive, 59

I have consolidated all of my defined contribution pensions into a SIPP, but I also have a small defined benefit pension which is due to start paying out in 3 months' time.

Will this affect my ability to put the full amount into my SIPP? If so, I'm guessing I would need to defer my DB pension payout (not including tax-free amount).

DO YOU HAVE A QUESTION ON RETIREMENT ISSUES?

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

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

As you have alluded to in your question, the amount you can save in a UK pension scheme each year is determined by the annual allowance.

Slightly confusingly, there are different annual allowances depending on your earnings or how you have accessed your pension savings.

For most people, the annual allowance is £40,000 (including tax relief). However, those with total earnings above £150,000 could be subject to the annual allowance 'taper', which gradually reduces the amount you can save in a pension each year to a minimum of £10,000.

There is also a third version called the 'Money Purchase Annual Allowance' (MPAA). This kicks in when you access your fund using the pension freedoms introduced in April 2015.

In order for the MPAA to take effect two conditions must be met.

Firstly, the income you withdraw must be taxable (i.e. taking a tax-free lump sum won't affect your annual allowance).

Secondly, it must be a flexible withdrawal from a defined contribution pension from age 55.

Provided you do not meet both of these conditions the MPAA shouldn't affect you. So receiving a DB pension shouldn't impact on your ability to save in a DC vehicle such as a SIPP.

Similarly, if you purchased a non-flexible annuity – a product which provides a guaranteed income for life – this should not impact your annual allowance.

Question 3 Brian

I've read stories suggesting the Government is going to cap the amount you can take tax-free from your pension at £40,000. Is this true, and if so should I take my tax-free cash now while I still can?

No, it's not true. While clearly you can never rule anything in or out categorically when it comes to political decisions such as this, there are no current plans to alter pension tax relief or reduce the amount you can withdraw tax-free.

I suspect the story you have read was reporting on proposals from a think-tank called the Resolution Foundation, which has put forward a number of ideas designed to save money and make the tax system "fairer".

Even if there were to be any changes in this area – and it should be noted that despite constant rumours the entitlement to 25% tax-free cash has remained unaltered – it is likely some sort of transitional arrangements would be put in place. Anything less than this would risk fundamentally undermining trust in pensions.

More broadly, it's rarely a good idea to make decisions which could affect your financial future based on speculation which may or may not be grounded in fact.

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Destiny Pharma is an innovative pharmaceutical company focused on the development of novel medicines.

SERICA ENERGY
Speaker: Mitch Flegg, CEO
Serica Energy is a British independent upstream oil and gas company with operations focused on the UK North Sea.

ST MARK HOMES (SMAP)
Speaker: Barry Tansey, Chief Executive
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Warren Buffett once said that as an investor, it is wise to be 'fearful when others are greedy and greedy when others are fearful'.

Shares' best value ideas

- Aviva
- EasyJet
- Imperial Brands
- Inchcape
- Melrose Industries
- TUI

Fear is not in short supply right now.

There are rising concerns over the state of the US economy, and whether after a number of relative boom years, slowing growth might lead to a recession.

Interest rates are rising, inflation is emerging and there is the not insignificant matter of an ongoing trade dispute between the US and China, as the world's two largest economies slug it out.

The UK backcloth continues to be dominated by the Brexit quagmire as the debate rages on and the pound remains in the doghouse.

DIAMONDS IN THE ROUGH

Many investment experts believe equity markets, and the UK in particular, are littered with very attractive opportunities, made more so by the constant talking down of stock market prospects.

In this article we reveal six of the best value opportunities in the FTSE 350 index, identified using three tried and trusted valuation metrics.

'The unfolding cyclical downturn coupled with the fall-out from the trade conflict between America and China should provide a compelling opportunity to build longer-term positions,' says Philip Saunders, Investec's co-head of multi-asset growth.

Others go further. 'The unrelenting negativity that investors are demonstrating towards UK equities is making me feel more and more positive on their prospects for 2019,' says Alex Wright, fund manager at **Fidelity Special Situations (B4566K2)** and **Fidelity Special Values (FSV)**. He is a natural contrarian investor who feels comfortable going against the grain.

'It might be counterintuitive to think that the UK market could be among the top performers globally in the year that we leave the EU (if indeed we do). But markets have a way of confounding expectations and surprising the consensus,' he adds.

As Wright points out the negativity has been unrelenting of late. UK stocks had a very difficult 2018 and the mood has barely lightened in the early days of 2019.

Since peaking at a record 7,877.45 on 22 May 2018 the FTSE 100 index has chalked up a 16%-plus decline at its lowest ebb in late December. That makes it among the worst performing major stock markets anywhere in the world over the past six to 12 months, but also now one of the cheapest.

World's top indices by PE

- NASDAQ **17.2**
- S&P 500 **14.4**
- DOW JONES **13.7**
- EUROSTOXX 600 **12.8**
- FTSE 100 **11.2**
- TOPIX **11.2**

UK AT A GLOBAL DISCOUNT

At roughly 6,750 (at time of writing) the FTSE 100 is trading on a next 12 months price to earnings (PE) multiple of 11.2. That's down from 11.6 in November.

It probably doesn't need saying that this represents a significant discount to the major US markets, yet it is also trading below the Eurostoxx 600 and Australia's ASX and India's Sensex. Even Japan's Topix index in on par with the UK's main index.

Yet out of adversity comes opportunity. 'Price is what you pay, value is what you get,' to paraphrase another of Buffett's nuggets of wisdom. Or in other words, while the herd power of market sentiment cannot be ignored, it is often only short term. Valuation drives share prices in the long run.

SIMPLE VALUATION MEASURES

In this feature we have run the numbers with the aim of highlighting examples of stocks that may be getting an unfair bashing. We have kept things fairly simple, looking for stocks that look like they may offer attractive value using metrics that will be familiar to many investors.

First, we have drawn together a list of interesting investment ideas based on the price-to-earnings (PE) ratio, an easy-to-use favourite of investors.

We have also tapped into the extra power implied by the price-to-earnings growth (PEG) measure, first popularised in the 1970s by private investor guru Jim Slater.

HOW TO WORK OUT PE AND PEG

- Earnings per share (EPS) ÷ share price = price-to-earnings (PE) ratio
- PE ratio ÷ annual EPS growth = price-to-earnings growth (PEG) multiple

The PEG is used to determine a stock's value while also taking the company's earnings growth potential into account. This gives a more rounded picture of a stock's relative value than the PE ratio alone.

It can be applied to historic earnings but, given the forward-looking nature of stock markets, is arguably better suited to forecasts of future earnings.

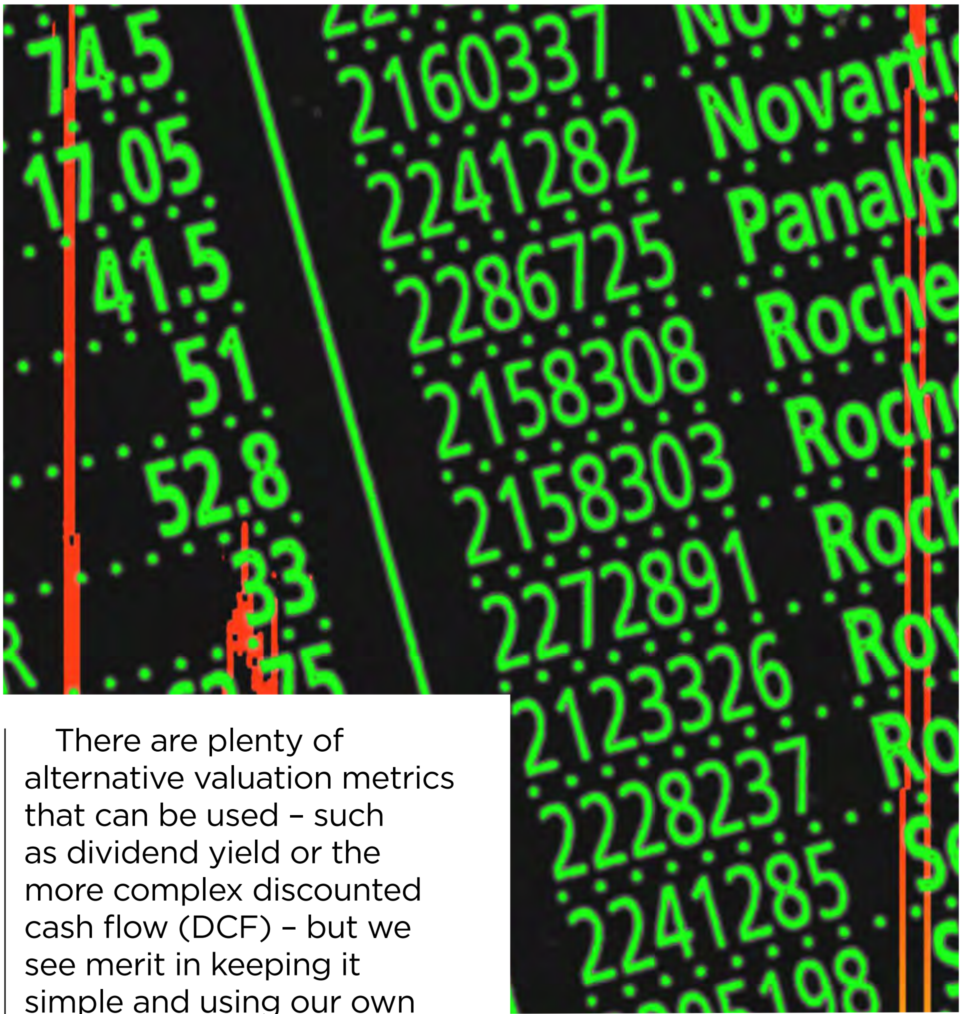
Lastly, we have accounted for the relative balance sheet strength or risks of highly cashed-up or heavily-indebted companies by using enterprise value (EV).

We have measured this against the most common profitability metric of earnings before interest, tax, depreciation and amortisation, or EBITDA for short.

EV is calculated by taking a company's market value, then adding any net debt, or subtracting net cash. It's a neat way of seeing what the market thinks the whole business is worth.

HOW TO WORK OUT EV

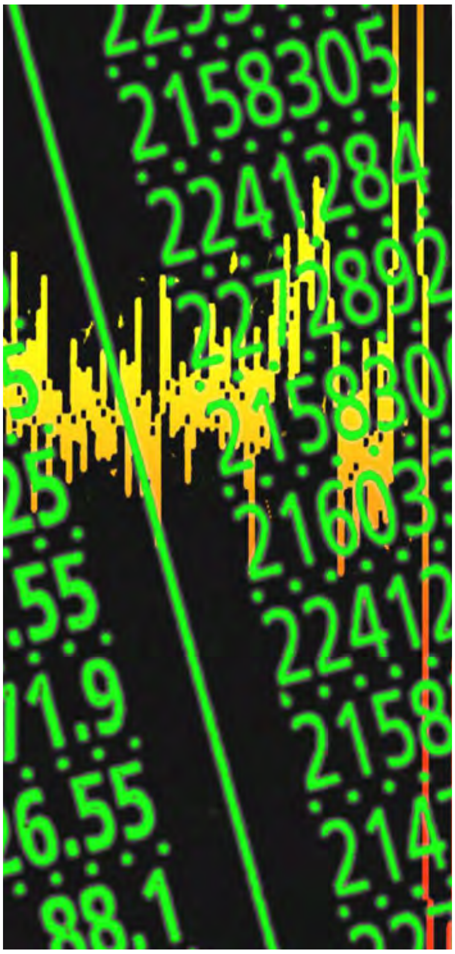
- Market cap plus net debt (or minus net cash) = enterprise value



There are plenty of alternative valuation metrics that can be used – such as dividend yield or the more complex discounted cash flow (DCF) – but we see merit in keeping it simple and using our own knowledge to identify the best ideas from the list. We also publish in full a list of top 40 stocks in each category to support your own idea generation.

The widespread decline in share prices over recent months has understandably made investors nervous about remaining invested in the stock market. But rather than ripping up portfolios entirely and donning tin hats, we believe investors can make subtle shifts to provide extra portfolio protection.

This could involve increasing stakes in reliable income-bearing stocks, funds and trusts that will help improve diversification. And we also think select oversold stocks may offer significant upside over the medium-term.



FTSE 350 - Cheapest PEs top 40

Company	Forward PE*
Barclays	6.7
Lloyds Banking	6.9
Persimmon	6.9
Paragon Banking	7.0
Petrofac	7.0
Superdry	7.0
Mitchells & Butlers	7.1
Tullow Oil	7.2
Phoenix	7.4
Plus500	7.5
DS Smith	7.6
Kingfisher	7.7
Intu Properties	7.7
Saga	7.7
Royal Bank of Scotland	7.8
Bovis Homes	7.8
Investec	7.8
John Laing	7.8
RHI Magnesita	7.8
British American Tobacco	7.9
Legal & General	7.9
Imperial Brands	8.1
Stagecoach	8.1
Smurfit Kappa	8.2
TUI AG	8.2
EI Group	8.2
Restaurant Group	8.2
WPP	8.3
Glencore	8.3
RPC	8.3
EasyJet	8.4
Greene King	8.4
Ashtead	8.5
Prudential	8.6
Capita	8.6
ITV	8.7
Man	8.7
Halfords	8.7
Inchcape	8.7
Micro Focus International	8.8

Source: SharePad, 2 January 2019

LOW PE IDEAS

Imperial brands (IMB) £23.76
Forward PE: 8.1

A single digit PE ratio implies **Imperial Brands (IMB)** has run out of growth puff, yet the market may be too pessimistic about the *Davidoff*, *Gauloises Blondes* and *JPS* maker's long-term prospects. Tobacco twosome Imperial and **British American Tobacco (BATS)** languish on historically low ratings due to concerns over declining cigarette volumes, the economics of Next Generation Products (NGPs) and regulatory crackdown fears. Though it is worth noting that British American has greater exposure to a potential ban on menthol cigarettes across the pond. Imperial is successfully trimming its brand portfolio (a divestment programme on track to deliver up to £2bn of proceeds) and migrating niche brands to global brands with scale, a strategy designed to deliver better growth and enhanced margins. Re-rating catalysts include a continuation of Imperial's improving market share performance,

evidence its investments in e-vapour brand *blu* are earning a profit, as well as growing investor appetite for Imperial's strong dividend growth. For the year to September 2019, UBS forecasts a hike from 187.8p to 206.6p, though the implied prospective dividend yield of 8.7% suggests investors should be cautious over a potential reduction in the dividend. As the smallest of four global tobacco giants, Imperial Brands is also the likeliest takeout candidate, although any takeover would likely be a complicated consortium bid.

Numerous housebuilding and financial stocks populate our top 40 of FTSE 350 stocks on the lowest price-to-earnings ratios. This reflects two issues. First, these companies are often not assessed on earnings multiples but instead on how their market valuation stacks up against the value of their assets. Second, both sectors have been badly hit by Brexit fears thanks to their UK domestic bias. The next few months, with a range of possible outcomes for the UK's future relationship with Europe, could be decisive in determining whether investors are attracted by the apparent value on offer from the sectors.

LOW PE IDEAS

Inchcape (INCH) 547p
Forward PE: 8.7

A screeching share price reverse at **Inchcape (INCH)**, reflecting margin pressure and currency headwind concerns, leaves the shares languishing on an inexpensive price to earnings ratio. That should interest value-seekers, since Inchcape is an automotive distributor and retailer with truly global scale, operating in 32 markets. Partnering with leading high-end car brands, BMW, Jaguar Land Rover, Aston Martin and Mercedes-Benz among them, Inchcape has a cash generative, defensive and higher margin distribution business at its core. The company's third quarter update (8 Nov) drove earnings downgrades, revealing flat group revenue

of £2.28bn and with CEO Stefan Bomhard also conceding the easing of retail margin pressure in the UK and Australia had been slower than anticipated. However, potential catalysts of the share price include an easing of retail margin pressures into 2019 as well as the organic and acquisitive growth of the distribution arm. As Numis Securities explains, 'the value in a professional, well-invested and experienced partner is growing for manufacturers', meaning Inchcape is well-placed to continue winning new distribution contracts. A strong balance sheet and robust cash generation should enable Inchcape to execute on a healthy M&A pipeline whilst funding a progressive dividend, the shareholder reward increased by a healthy 12.7% to 8.9p at the interim stage.

FTSE 350 cheapest PEGs top 40

Company	Forward PEG*
Playtech	0.5
Wizz Air Holding	0.5
Sports Direct International	0.5
Wood (John)	0.5
Rolls-Royce	0.5
Royal Bank of Scotland	0.5
Amigo	0.5
Bovis Homes	0.6
Man	0.6
Weir	0.6
IP Group	0.6
Investec	0.6
TI Fluid Systems	0.7
International Consolidated Airlines	0.7
Kingfisher	0.7
Ashtead	0.7
Drax	0.7
Restaurant Group	0.7
Micro Focus International	0.7
Balfour Beatty	0.7
SIG	0.7
Energean Oil & Gas	0.7
McCarthy & Stone	0.7
Paragon Banking	0.7
Aviva	0.7
Barclays	0.7
Prudential	0.7
Redrow	0.8
TP ICAP	0.8
Vodafone	0.8
Melrose Industries	0.8
CRH	0.8
Saga	0.8
Tesco	0.8
Ibstock	0.8
Hastings	0.8
SSE	0.8
Mediclinic International	0.8
Serco	0.8
B&M European Value Retail	0.8

Source: SharePad, 2 January 2019

LOW PEG IDEAS

Aviva (AV.) 375p
Forward PEG: 0.7

Aviva (AV.) is the UK's largest insurance company with around half of sales coming from its home market and half from France, Holland and Poland. Most of its sales come from life insurance where customers and premiums tend to be 'stickier' than in household or car insurance. 2018 was a busy year for Aviva. In April it incurred the wrath of shareholders when it said it would cancel £450m of preference shares which carry a higher dividend than the ordinary shares. In May it raised eyebrows by buying almost £1bn of pension liabilities from embattled retailer M&S in its largest 'bulk annuity' deal to date. In October the chief executive stepped down leaving the company leaderless just as the UK financial regulator and the competition watchdog started looking into the home and car insurance markets. The current concerns are Aviva's high debt levels compared with its peers and its perceived lack of earnings growth. But if

the consensus forecasts are correct, Aviva will deliver at least some growth this year despite its lowly earnings multiple. And analysts are almost unanimous in backing the stock. Their consensus price target of 550p implies close to 50% upside from here.

The table shows a diverse set of companies from the FTSE 350 which look cheap relative to their forecast earnings growth. Some of the oil-related stocks may have made the list because the market is increasingly sceptical forecasts will be hit after the big decline in oil prices in the latter part of 2018. The presence of **Tesco** and **Rolls-Royce (RR.)** would suggest their ongoing recovery stories are yet to fully convince the market. Respective chief executives Dave Lewis and Warren East are highly regarded in the world of business.

LOW PEG IDEAS

Melrose Industries (MRO) 157.3p
Forward PEG: 0.8

The strategy behind engineering play **Melrose (MRO)** is relatively straightforward. It buys poorly managed but good quality manufacturing businesses which are suffering from a lack of investment. It looks to drive operational improvements and boost cash generation before selling the firms for a healthy profit. This has, according to figures quoted by the company, helped deliver a total shareholder return of 3,019% since joining the stock market in October 2003. The controversial £8bn purchase of UK industrial engineer GKN in 2018 represented a big step up compared with the scale of the businesses previously acquired by Melrose. A lack of any hidden problems at GKN when the company reported its half year results on 6 September 2018 was reassuring but media speculation that a planned sale of the group's powder metallurgy unit had attracted a lower than anticipated price hit investor sentiment in November. Melrose has also been affected by concerns over a possible global slowdown which might hit demand for GKN's automotive and aerospace operations. However, if the company can demonstrate material progress in its turnaround of GKN in 2019, particularly in terms of

margin performance, then investors should respond to the value opportunity in the shares.

FTSE 350 cheapest EV/EBITDA top 40

Company	Forward PEG*
Galliford Try	3.1
Playtech	3.1
FirstGroup	3.3
Royal Mail	3.6
Cairn Energy	3.6
TI Fluid Systems	3.9
International Consolidated Airlines	3.9
KAZ Minerals	4.0
Acacia Mining	4.0
Centamin	4.0
Hochschild Mining	4.0
Ferrexpo	4.2
Dixons Carphone	4.2
Barratt Developments	4.2
Kingfisher	4.2
BP	4.2
Wizz Air	4.2
Redrow	4.3
Capita	4.3
Bellway	4.4
Persimmon	4.4
Tullow Oil	4.4
Crest Nicholson	4.5
Glencore	4.5
Rank Group	4.5
ContourGlobal	4.5
Sainsbury (J)	4.5
Evraz	4.6
Taylor Wimpey	4.6
Cineworld	4.6
Stagecoach	4.7
EasyJet	4.7
Ashtead	4.7
Mondi	4.7
TUI	4.8
Anglo American	4.8
Aggreko	4.8
Royal Dutch Shell	4.9
Antofagasta	4.9
Marks & Spencer	5.0

Source: SharePad, 2 January 2019

LOW EV/EBITDA IDEAS

EasyJet (EZJ) £10.95
Forward EV/EVITDA: 4.7

Shares in **EasyJet (EZJ)** appear undervalued with investors overlooking a strong balance sheet that will help the airline weather potential volatility as the UK's exit from the EU fast approaches.

EasyJet is confident it can continue operating flights across the EU 'regardless of the Brexit outcome' via the creation of EasyJet Europe with headquarters in Vienna.

Unlike embattled rival **Ryanair (RYA)**, EasyJet has been able to drive profitability higher with its impressive pricing power and passenger growth despite widespread strike disruption. EasyJet is currently on a cheap 4.7 times enterprise value/earnings before interest, tax, depreciation and amortisation, reflecting in part the strength of its balance sheet. Cantor Fitzgerald analyst Robin Byde argues EasyJet is one of the leading airlines and is in a prime position

to sweep up its European rivals. The airline's robust financial position should help EasyJet navigate several short-term factors, including a potential softening of demand in Europe, an expected decline in unit revenues and the impact of fuel costs if prices rise.

Companies with little debt or lots of cash can sometimes have a low EV/EBITDA (enterprise value-to-earnings before interest, tax, depreciation and amortisation) multiple which helps explain why many mining stocks make the list. Mining firms have slashed their debt and stockpiled cash in recent years following a crash in commodity prices. However, they are still vulnerable to volatility in resources markets and wobbles in the global economy so being cheap doesn't necessarily make them low-risk. This situation also means earnings can be tricky to forecast. When companies want to make acquisitions, they often look at the EV/EBITDA multiple of the target as it includes debt which other metrics based purely on market valuation like price-to-earnings do not. As such, the accompanying list could include potential takeover targets.

TUI (TUI) £11.51
Forward EV/EBITDA: 4.8

Travel operator **TUI (TUI)** is setting itself apart from the competition by tapping into demand for experiences. TUI generates over 70% of its earnings from its holiday experiences comprising hotels, cruises, excursions and destination activities. A raft of profit warnings from rival **Thomas Cook (TCG)** has somewhat overshadowed TUI's robust performance, which is expected to continue into 2019. TUI currently trades on 4.8 times enterprise value to earnings before interest, tax, depreciation and amortisation, despite targeting at least 10% earnings growth every year to 30 September 2020.

Future catalysts for growth include an extensive pipeline of hotel openings in popular destinations such as Greece and Turkey, as well as new cruise ships this year.

Berenberg analyst Stuart Gordon argues the market is overly pessimistic on the company's cruise and hotel divisions. He forecasts a €25m year-on-year improvement in earnings in the hotel and resorts division, driven by new openings and a recovery in Eastern European markets.

Strong demand and the launch of three new ships this year is expected to deliver further strong growth in the cruises division with earnings set to soar by €55m to €379m in 2019.

By **Steven Frazer, James Crux, Ian Conway, Tom Sieber and Lisa-Marie Janes**

Technology fund expert who'd been slicing Apple long before the warning

Polar Capital Technology's Ben Rogoff has used stock selection flexibility to out-do benchmark

Leading technology fund manager Ben Rogoff had been cutting back on his appetite for Apple long before the consumer electronics giant's shock profit warning (2 Jan).

The respected manager of the **Polar Capital Technology Trust (PCT)** has become increasingly wary of potential threats to the Cupertino giant's iPhone sales volumes against a backcloth of aggressive trade rhetoric from both the US and Chinese governments.

Apple chief executive Tim Cook has tried various ploys to patch potential leaks from his company's earnings from global smartphone saturation. This has included schemes like launching an array of new and more expensive handsets, cranking up its services revenues from streaming music, apps and much else, plus enormous share buybacks, for example.

ALARM BELLS RING

This came to a head just two days into 2019, the company reporting the grim news that its revenue and earnings numbers would be lower than it had forecast at the last quarterly earnings report in November.

Apple blamed faltering sales in

Asia, particularly in China, for the adjustment, but the share price tanked, losing about 10% of their value to $144.04.

Adding to Rogoff's concern was Apple's controversial decision last year to stop telling investors how many iPhone units were shipped, seen by many commentators as a slap in the face for transparency.

Being seemingly ahead of the curve should be, at least partially, satisfying for Polar Capital investors. Back in August 2017 Apple ranked as the investment trust's second largest holding, with 7% of its funds tied up in the smartphones designer.

Today the stake is 5.4%. That remains sizeable (Apple is still Polar Capital's third biggest investment) yet our back of note book calculations suggest that more than £17m of net assets have been funnelled out of Apple and into other investments during that 17 month spell.

Critics might say that this still leaves the trust with egg on its face. A 5.4% net assets stake in Apple implies that something close to £9m of the trust's value was eaten away by the Apple warning.

Rogoff sees Apple's cast iron balance sheet as a major positive for the company going forward, backed by a $237.1bn cash pile (as of 1 November 2018) that will

> **A 5.4% net assets stake in Apple implies that something close to £9m of the trust's value was eaten away by the Apple warning**

continue to fuel share buybacks.

But the manager also remains 'benchmark aware' to its Dow Jones World Technology Index, which means some very large technology stocks simply must be owned.

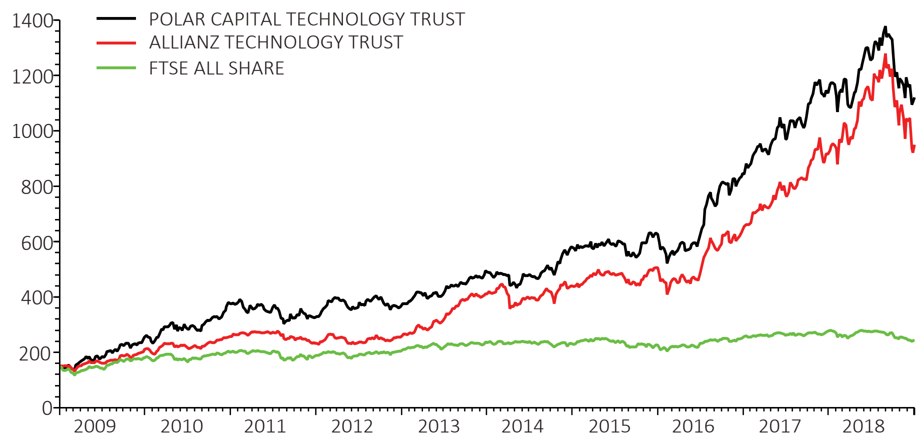
WILLING TO LOOK BEYOND THE BENCHMARK

But it is encouraging that Rogoff shows a distinct willingness to look beyond the benchmark in his stock selection when he can to gain access to the very best long-term growth opportunities, as any active fund manager should look to do.

Polar Capital Technology's largest holdings

HOLDING	% OF PORTFOLIO
Alphabet	9.0%
Microsoft	9.0%
Apple	5.4%
Facebook	3.3%
Tencent	3.3%
Alibaba	3.3%
Amazon.com	3.0%
Taiwan Semiconductors	2.3%
Salesforce.com	1.9%
Adobe Systems	1.9%
Total	**42.4%**

Source: Polar Capital, as at 30 November 2018



It is a strategy that stands up to performance scrutiny. Overweight holdings (meaning they are a higher proportion of the trust than in the benchmark) such as chip maker Advanced Micro Devices and software stocks like Alteryx, Twilio, New Relic and Hubspot joined better-known names (Amazon, Dropbox, ServiceNow) to significantly bolster the half year performance to 31 October 2018.

During that six-month trading period Polar Capital saw its net asset value (NAV) increase 8.5%, about a fifth better than the 7% of the Dow Jones World Technology Index.

Yet the trust's share price has, perhaps understandably given concerns for global stock markets and growth, continued to struggle, falling about 17% since 'Red October's' sell-off kick-in.

That leaves the stock changing hands now at £11.10. The share price discount to NAV had widened to 6.5% at 31 October, although it has since narrowed again to about 3%, more in line with its 10-year average of 3.8%, according to Winterflood data.

NEXT DISRUPTIVE TECH CYCLE

While recent months have seen an extreme spell of volatility across technology markets Ben Rogoff remains as chipper about the long-run prospects for select technology themes as ever, flagging cloud computing, software-as-a-service, digital marketing, complex microchips and robotics/automation as some of his pet favourites.

'Ben Rogoff makes a compelling case for the continuing emergence of the next technology cycle and the disruptive effect that it is having on many of the sector's existing large cap incumbents,' points out Emma Bird, analyst at Winterflood.

It has certainly worked in the past. Over the last 10 years the fund has delivered a NAV total return of 551%, smashing the 423% return of the Dow Jones World Technology benchmark. That's also modestly better than its closest UK–listed peer, the Walter Price-run **Allianz Technology Trust (ATT)** at 534%.

By **Steven Frazer**
News Editor

Where European stocks stand two decades after the euro's launch

We talk to fund managers about the prospects for the single currency and Eurozone shares

This month marks two decades since the introduction of the euro, when 12 European nations cast aside their own currencies to unite under a single coin.

As the euro launched in 1999, investors saw spreads between core nations such as Germany and France tighten with those of peripheral members such as Greece and Portugal.

Ian Ormiston, manager of the **Merian Europe ex UK Smaller Companies (BRTNQ88)** fund, explains: 'The cost of capital tumbled for peripheral equity markets and their perceived risk premium collapsed.'

SPREADS HAVE WIDENED AGAIN

Today, however, Italian government bonds are trading around their widest spread in five years compared to German bunds. At the start of 2019, Italy's budget is one of the key issues facing the eurozone. It's just one of many clouds over the investment outlook for the region.

The value of the euro is holding steady against other major currencies, but its future remains in doubt. The UK's decision to leave the European Union along with the rise of populist political parties has sparked concerns that more countries could try to leave the union or its currency.

Thomas Brown, co-manager of **Miton European Opportunities (BZ2K2M8)**, says: 'The euro, like Facebook, was supposed to bring us all together. But it has had the opposite effect; driving substantial divergences in Eurozone economies, which currently appear insoluble. Currency union without federal union looks doomed to fail.'

Indeed, the union has faced a number of unprecedented issues over the past decade, as the European Central Bank has tried to manage its way out of a global financial crisis with member states at varying states of boom and bust.

REGION FACING SEVERAL HEADWINDS

In 2018, Europe had to cope with myriad headwinds, including trade war concerns, political uncertainty in Italy and the UK, and monetary tightening in the US. Growth in Europe was just 0.2% in the three months to November – its lowest level in more than four years – and ECB President Mario Draghi has said the base rate is unlikely to rise before the summer.

Despite that, many fund managers remain optimistic about the year ahead. A recent rout has seen company valuations fall, but Edward Greaves, co-manager of the **JPM European Smaller Companies (JESC)** trust, points

out that earnings growth for many smaller firms on the continent is forecast to be close to 10% this year.

He is particularly upbeat about the outlook for businesses in the healthcare and technology sectors. He has investments in Swiss firm Vifor Pharma and French consultancy company Altran Technologies. The trust has returned 17.3% over three years.

Chris Hiorns, manager of **EdenTree Amity European (0844833)**, thinks the European economy as a whole looks to be in much better shape than it has been for the past decade. The introduction of new emissions controls has hurt the automotive sector, but he thinks it's a temporary issue, which could provide an investment opportunity.

FOCUS ON LOWLY VALUED CYCLICAL STOCKS

Hiorns is focusing on cyclical stocks trading on low valuations, yielding 4% or more. Among the constituents of the portfolio are tyre manufacturer Michelin, recruitment firm Randstad, and building materials company St Gobain. The fund has returned 25% over three years.

Merian manager Orimston says: 'As a stock picker, it has been possible to find companies unaffected by their local bond market woes. Germany's domestic market has never been so strong, as its export sector has been hampered by the relentless rise of the Deutsche Mark. Even in Italy, we are able to find manufacturers that have benefitted from the crushing of domestic inflation.'

Some 7.2% of his fund's assets are in Italian equities with other investments in German, French and Dutch stocks. Top holdings include Belgian manufacturer Ontex Group and Norwegian retailer Europris. The fund has returned 16% over three years.

James Sym, manager of **Schroder European Alpha (B6S00Y7)**, is looking for companies that are likely to benefit if inflation picks up. This includes sectors such as telecoms, where the infrastructure needed to supply services already exists so capital expenditure isn't too high, and rising wages mean customers can bear price rises.

He also likes financial firms, which are able to increase their rates on loans and other products as inflation creeps up, helping to boost revenue. The fund has returned 20.8% over three years.

VOLATILITY SET TO PICK UP

Two decades on from the launch of the euro, the outlook for the region is by no means a simple one to navigate. Brown thinks growth - both economic and earnings - will be lower this year, while volatility is likely to pick up. His fund, which has returned 50.3% over three years, invests in names including Ferrari, Finecobank and Netherlands eyecare retailer GrandVision.

While fears abound about potential recession, trade wars, rising rates and political crises, it is important to remember that a country's stock market often has little to do with its political or economic environment. So much uncertainty often creates opportunities for stock pickers who can cut through the noise.

Miton man Brown adds: 'Our approach is not to spend time second-guessing the macro-economic environment, but to focus on owning the few great world leading-companies in Europe that we think will continue to perform well whatever the economic weather.'

By **Holly Black**

FEATURE

Everything you need to know about impact investing

We look at how certain types of investment look to actively do good with your money

A New Year is typically a time to make resolutions and beyond self-improvement many of us will be considering ways we can make a positive contribution to the world around us.

The investment industry is responding to this aspiration with vehicles which look to do good with your money as well as generating a healthy return.

At first glance 'impact investing' doesn't seem that different from ethical investing which has been around for decades.

The main difference is that where ethical investing is about directing investment *away* from companies that do social or environmental harm, impact investing directs investment *towards* those that have a positive influence.

Impact investing also means generating a positive financial return, which although it sounds obvious hasn't always been a priority with ethical investing.

A LARGE AND GROWING MARKET

By 2017 the amount of money devoted to impact investing stood at $228bn making it a distinct, specialised investment class in its own right.

According to the World Economic Forum the market grew five-fold from 2013 to 2017 and even if the world economy slows and stock markets struggle this year money will continue to flow into impact funds.

For now the market is led by development-finance institutions and specialist asset managers but a growing number of investors are looking for ways to generate benefits for society alongside healthy financial returns.

Once impact investing 'tips' into the institutional market, where assets under management are over $100tn, growth could really take off as the investment style gets adopted by the mainstream.

Already fund management firms have lent their support to The Big Exchange, an impact investing platform backed by The Big Issue magazine which aims to raise £3bn of assets over the next five years.

KEY DRIVERS ARE GLOBAL CHALLENGES

The main drivers behind impact investing are the big issues facing all of us: a growing global population, rising living standards, natural resource constraints and above all climate change.

As consumers we are becoming increasingly aware of the need to conserve natural resources and above all not to pollute the environment.

The public support for the campaign to ban single-use plastic following the BBC's *Blue Planet II* series and the success of the ban on 'disposable' plastic carrier bags are examples of 'people power'.

Some of the key investment areas for impact funds are low-carbon power generation such as wind and solar plants, water supply and treatment and improved healthcare in developing countries.

In these areas solutions are already available but they need funding to enable them to scale up over the coming decades.

However there are still major issues to solve such as how to tackle air pollution, how to improve nutrition in poorer regions without impacting the environment and of course how we can avert a serious change in the global climate.

SETTING OUT PRINCIPLES AND ACHIEVABLE TARGETS

One of the drawbacks of impact investing is that despite the increase in interest there are still no clear, established guidelines which means it can be hard to distinguish between impact and other forms of responsible investing.

Most impact investors have adopted the United Nations' Sustainable Development Goals to define the relationship between their investments and their goals.

Also the International Finance Corporation, part of the World Bank and one of the earliest backers of sustainable investing, recently set out eight principles which it hopes will help managers set measurable social and environmental goals.

This spring it aims to finalise these principles and sign up some of the world's most influential investors, academics and politicians.

TWO DECADES OF EXPERIENCE

One of the pioneers in the field is **Impax Asset management (IPX:AIM)** which has been investing for social and environmental change for 20 years.

Over that time sustainable investing has grown from a niche industry with a focus on micro- and small-cap environmental technology stocks to a business worth hundreds of billions of pounds invested in companies of all types and sizes across global markets.

Impax's investment teams run a range of strategies covering resource efficiency, environmental markets, food and agriculture, and water infrastructure.

In the year to the end of September assets under management were £12.5bn, an increase of 72% thanks both to new inflows and to the acquisition of Pax World Management.

Impax's funds themselves had a good year, with the **Impax Global Opportunities Fund (BSXNJK4)** generating almost double the return of the MSCI World Index.

A new arrival on the scene is the **Global Sustainability Trust** which aims to invest in private markets along the lines of the UN's SDG goals.

Open to applications until 28 January and due to commence trading on 31 January, the trust will be managed by Aberdeen Standard Investments, part of **Standard Life Aberdeen (SLA).**

It is targeting £200m of capital in its first round of fund raising with a net return to investors of 6-8% per year after fees.

By **Ian Conway**
Senior Reporter

How to measure the earnings power of corporate America

Looking at the market context as quarterly updates start to trickle in

A sour trading update from Apple leaves those investors who have exposure to US equities – and technology stocks in particular – with a few questions to answer.

Although disappointing demand in China grabbed most of the headlines, Apple's chief executive officer, Tim Cook, also blamed weaker growth across emerging markets more generally, a stronger dollar and a slower-than-expected product upgrade cycle in the West – all issues which could affect not just Apple but any US-based multi-national.

This is why the forthcoming quarterly reporting season in America will be a particularly important one, as investors try to get a read on whether the second-half sell-off suffered across US equities in 2018 was merited or not.

VALUE CASE

According to research from Standard & Poor's the pull-back leaves the US stock market on 14.3 times forward earnings per share estimates of $171 for the S&P 500 in aggregate for 2019.

S&P 500 ANNUAL EARNINGS PER SHARE

Source: Standard & Poor's

- Bulls will argue that a 9% increase is perfectly achievable, especially with the US economy primed to rack up GDP growth of 2.5% to 3.5% for 2019. Throw in that 9% earnings increase, some multiple expansion from that 14.3 times level if confidence returns – and a dividend yield of around 2.1% - and you can see how forecasts of double-digit returns from US equities for 2019 may easily add up.

- Bears will challenge that 9% growth estimate by pointing out that the forecast 2018 earnings per share figure for the S&P 500 of $157 already represents a record high. With corporate profit margins of 12.1% in Q3 2018 also a record high, it seems legitimate to ask how US corporate earnings can keep on growing, as the benefits of the Trump tax cuts fade and higher wages, higher interest bills (thanks to the Federal Reserve's four interest rate increases last year) and the stronger dollar make their presence felt.

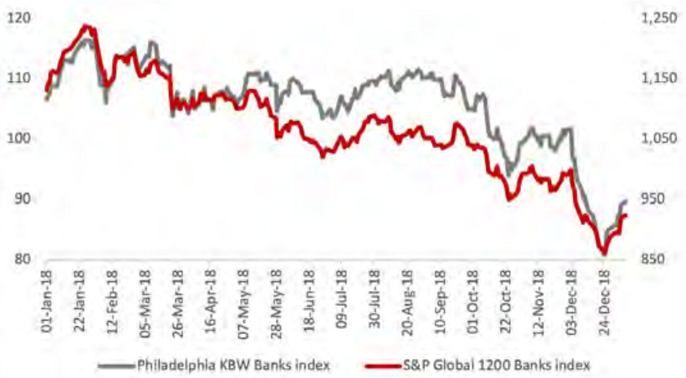
EARLY TEST

Hopes for a trade settlement between America and China, a softer approach from the US Federal Reserve and the announcement of both fiscal and monetary stimulus by Beijing's President Xi Jinping have given markets a boost but the imminent fourth-quarter results season will be good early test for the US equity market – especially as Apple, silicon chip maker Micron (which gave out a profit warning just before Christmas) and Delta Airlines have got it off to a bad start.

Around 30 of the S&P 500 index's members report quarterly results in the coming week. Most of them are financial stocks, including megabanks Citigroup, JPMorgan Chase, Wells Fargo, Bank of America, Goldman Sachs and Morgan Stanley.

Investors will be looking for strong numbers here as the banks sector was a terrible stock market performer the world over in 2018 – and if there is one sector that all portfolio-builders would like to know is healthy some ten years after the Great Financial Crisis then surely it is the banks.

HOW THE BANKS HAVE PERFORMED



Source: Refinitiv data

Overall, Standard & Poor's is looking for 26% earnings per share growth, helped by the Trump tax cuts for the final time – the beneficial comparative effect will drop out from the first-quarter results that will be released in April and May.

S&P 500 QUARTERLY EARNINGS PER SHARE

Source: Standard & Poor's

> **All issues which could affect not just Apple but any US-based multi-national**

MARGIN FOR ERROR

The second-half retreat in US equities to around the 2,500 mark on the S&P 500 at the time of writing leaves the headline index some 14% below its September all-time high. And the fact that US stocks are now 14% cheaper than they were makes them more interesting.

However, tempting as that 14.3-times forward multiple may be, there may be still little room for disappointment when it comes to the quarterly reporting season.

The 10% hammering handed out to Apple on the day of its warning suggests as much, as does the work of Professor Robert Shiller.

His cyclically-adjusted price/earnings ratio (CAPE) calculation, which is based on inflation-adjusted historic earnings on a ten-year rolling basis, still argues that US stocks may be overvalued, at 29 times forward earnings.

The S&P 500 reached a CAPE rating of around 30 times on two prior occasions, in 1929 and 1998-2000, and both of those episodes ultimately ended badly.

S&P 500 CAPE RATING

Source: http://www.econ.yale.edu/~shiller/data.htm

By **Russ Mould**
AJ Bell Investment Director

Can you make money from investing in pub companies?

The pubs sector experienced mixed fortunes in 2018 as changing trends and higher costs hit trading

Britain is a nation that loves a pint of beer or a glass of wine, yet younger generations aren't as enamoured with alcohol.

More under-65s were not drinking at all in 2017 compared to 2005 according to the Office for National Statistics.

While this trend may be welcomed by the overburdened NHS, pub operators may understandably feel differently as a reduction in demand for alcoholic drinks could weigh on their earnings and growth.

Should investors go teetotal with their portfolios and ditch pubs entirely? We think that's a bit extreme as pubs have historically been decent investments and they remain an important part of everyday life, despite some shifting trends.

In a year where most stock markets fell around the world, three UK-listed pub companies would have delivered shareholders with a positive total return (share price gains and dividends) since the start of 2018. These are **City Pub Group (CPC:AIM)**, **EI Group (EIG)** and **Greene King (GNK)**.

Yes, the sector is battling various cost pressures and a mixed appetite from consumers towards casual spending, in addition to reduced alcohol interest among younger adults. But in the long term we still think there may be opportunities for select companies in the sector.

We like EI Group as management seem focused on the operations once again, having previously been distracted by years of non-stop questions about the group's large debts. Net debt has been reduced to £2bn which equates to a 56% loan-to-value.

Investors should expect returns to come from a rising share price with EI as it is not expected to pay dividends in the near-term.

We like **Young's & Co (YNGA:AIM)** for its premium estate and a proven dividend growth track record, although we recognise the shares aren't cheap. They are trading on 18.6 times forecast earnings for the year to March 2020. Although the prospective yield is only

PUB STOCKS TOTAL RETURN SINCE 1 JAN 2018

Source: SharePad. Data to 7 Jan 2019

Young's Burger Shack is one of the fresh initiatives from Young's & Co

1.6%, this is a great stock for reinvesting a growing stream of dividends so as to enjoy compounding benefits.

Panmure Gordon analyst Matthew Webb argues that Young's premium rating is warranted thanks to its 'far superior estate, exceptional like-for-like record and conservative balance sheet'.

Greene King's shares are considerably cheaper than Young's, trading on 8.6 times forecast earnings for the year to April 2020. There is a good reason why its rating is low: earnings are forecast to stay flat until at least the 2021 financial year. Analysts have pushed through numerous earnings downgrades over the past few years and the business seems to have lost its way.

Chief executive Rooney Anand is seen as an old-school operator with traditional values. He leaves the company later this year and investors may hope that a more modern-thinking replacement breathes new life into the business.

WHY DID SOME PUBS STRUGGLE IN 2018?

Investors may not be surprised by the list of headwinds dragging on the sector as pub operators have struggled with the weather-related impacts, higher labour costs and more competition for dining out.

The depressed high street environment is another factor, but some observers believe the pubs are faring a good deal better than their counterparts in the retail sector.

Canaccord Genuity's leisure analyst team says: 'In contrast to the retail sector which had an abysmal end to 2018, circumstances appear more upbeat for the eating and drinking out sector.

'Christmas Day continues to grow in importance to the pub companies as families increasingly prefer the treat of a pub event to the effort of cooking a feast at home. Greene King reported that Christmas bookings were well ahead of last year at its interims.'

Over the scorching summer, there was also a short-term boost as people flocked to pubs to enjoy the World Cup. Perhaps surprisingly given the societal decline in drinking, wet-led pubs performed better through 2018, while pubs with more exposure to food sales struggled as customers were spoilt for choice thanks to an over-saturated casual dining market.

EI TAKES THE CROWN

The UK's largest pub operator EI delivered the best returns for shareholders in 2018, driven by progress on rebuilding its business following years of being weighed down by significant debt. It was also in the right part of the market with its drinks-led proposition – food was less of a driver for the sector compared to previous years.

Investors may be also have been bidding up the shares ahead of a potential catalyst as EI plans to sell its portfolio of commercial properties to shore up its balance sheet and possibly reward shareholders with a special dividend.

Canaccord Genuity analyst Nigel Parson says the bids are estimated to be valued at between £320m to £350m, but the final price could be up to £400m.

EXPANSION STRATEGY PAYING OFF

City Pub Group is newest company among the UK-listed pub stocks, growing from a start-up in 2011 to an estate of 42 pubs, which are mainly drinks-led.

In the six months to 1 July, nine new pubs have been opened. City Pub Group is ambitious in

Investors would have lost money in Marston's in 2018

its growth strategy as it wants to double in size by 2021.

With modern bars and restaurants in affluent areas in England and Wales, including a contemporary pub near Brighton's i360 tower, City Pub arguably has more unique assets than its rivals.

It also has the financial firepower to hit its acquisition target of between eight and 10 new pubs, and even pursue further openings.

Liberum analyst Anna Barnfather argues Brexit uncertainty and revised business rates may work in the company's favour as it faces less competition for sites at potentially cheaper market prices.

PREMIUM BENEFITS

Shares in Young's failed to take off despite a robust performance at its pubs, which boast strong interior design, many riverside locations and fresh food made with local ingredients. We don't think there is anything to worry about, as Young's has a good track record of delivering earnings growth which is the ultimate driver for the share price.

Over the summer, its pub gardens attracted thirsty drinkers with Young's posting double-digit growth in drink sales in the 26 weeks to 1 October.

Sales and profitability have been on the rise thanks to investment in its premium estate. Young's is generous with its dividend policy, delivering its 22nd consecutive year-on-year interim dividend hike, leaving the payout at 9.9p per share.

WHO ARE THE SECTOR LAGGARDS?

Investors would have lost money in 2018 investing in **Marston's (MARS)**, **Mitchells & Butlers (MAB)**, **Fuller, Smith & Turner (FSTA)** among others.

With a 14.4% share price decline over the last year, Marston's has been struggling with falling food sales at its pubs.

Many investors are drawn to Marston's (and Greene King) for generous dividends, yet the former failed to lift its dividend at the latest full-year results, reported in November.

The company is taking a cautious view of life in 2019 and will reduce its normal capital expenditure plans by £30m including a reduction in the number of new pub, bars and lodgings.

The company is also hoping to reduce debt and slash pension contributions to improve cash flow and its balance sheet.

SPENDING MONEY TO MAKE MONEY

Adjusted pre-tax profit fell by 1% in Fuller's latest half-year results to £23.6m. Chief executive Simon Emeny said the business had decided to 'front-load' its investment programme, buying new pubs and investing in its brewing and IT operations.

Peel Hunt analyst Douglas Jack is confident Fuller's is making the right decisions even if it is impacting profitability, flagging further expansions and refurbishments are in the pipeline.

As we enter 2019, there are little signs that the pressures facing the pub sector will let up so Fuller's attempt to get is estate in the best possible shape looks a prudent strategy.

By **Lisa-Marie Janes**
Reporter

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KEY

- Main Market
- AIM
- Investment Trust
- Fund
- IPO coming soon

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15 Jan: Games Workshop. **16 Jan:** The Works

Trading Statements

11 Jan: AO World, Grafton. **14 Dec:** JD Sports Fashion, PageGroup, Revolutions Bars. **15 Jan:** Ashmore, The Gym Group, Hays, Provident Financial, Persimmon. **16 Jan:** Diploma, Headlam. **17 Dec:** Associated British Foods, DP Eurasia, Rio Tinto, SSP Group, Workspace, Whitbread, Experian.

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