STOCKS | FUNDS | INVESTMENT TRUSTS | PENSIONS AND SAVINGS

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# SHARES

WE MAKE INVESTING EASIER

# INVESTING UNDER THE CLOUDS OF BREXIT

## HOW TO POSITION PORTFOLIOS FOR A DEAL, NO DEAL OR DELAY

**PLUS**

THE COMPANIES THAT COULD BENEFIT FROM **THOMAS COOK'S DEMISE**

**SHOULD YOU INVEST IN AIRBNB** WHEN ITS SHARES HIT THE STOCK MARKET NEXT YEAR?

KNOW YOUR FUND: WHAT'S INSIDE **LINDSELL TRAIN GLOBAL EQUITY?**

# Shareholders feel the pain of Thomas Cook's demise

They won't get anything back as part of the liquidation process

The demise of travel operator Thomas Cook is not only awful for its customers and staff but also for shareholders who have lost all their money.

While its customers should be able to get a refund for any holidays booked and not yet taken, via the ATOL scheme, travel insurance cover or debit/credit card issuers, shareholders don't have such protection.

The Government has explicitly stated that shareholders will receive nothing from the liquidation of Thomas Cook. It says 'there is no prospect of a return' to shareholders.

This situation is a good reminder of the higher risks associated with investing in stocks and shares. There is a pecking order to follow during liquidation and shareholders are at the back of the queue when it comes to seeing if any value can be realised by selling a failed company's assets.

When a company goes into liquidation, creditors fall into different groups ranked in a specific order. The first group must be paid in full before funds are allocated to the next group.

**Creditors are ranked as followed:**

- Secured creditors
- Preferential creditors
- Secured creditors with a floating charge
- Unsecured creditors
- Shareholders

A lot of investors focus on what could go right with a business – but not enough attention is paid to what could go wrong.

Thomas Cook has been in financial difficulty for a long time due to having large amounts of debts to repay, fees on aircraft leasing and Brexit uncertainty causing the public to delay booking holidays. The lack of cash left over to invest in the business has also left it lagging behind the competition.

Arguably these factors aren't new and so anyone investing in Thomas Cook should have been aware


of the major risks to owning the stock.

Having the right expectations for potential returns is crucial with investing. Picture a ladder and the different rungs, each representing a higher risk investment as you climb up.

Someone who doesn't want to take high risks would naturally look to park their money in cash or something like UK Government bonds. They would be at the bottom of the risk ladder. Next up might be an investment grade corporate bond and as you keep climbing you eventually reach equities.

But even equities are spread across a range of risks and Thomas Cook would arguably be nearer the top. You hold the shares expecting a positive return as compensation for the risks involved. The upside for a very high risk investment is a big capital gain and the downside is losing everything, as the holiday company's shareholders have now discovered.

One private investor on Twitter said they bought Thomas Cook shares at the start of the year, with no doubts about the high risks. Having still owned them at the time of the liquidation, they said: 'Please feel sorry for the potential stranded holiday makers, not me. I fully understood the magnitude of the gamble.'

This is a good example of someone who had set the right expectations and was aware of what could go wrong. Losing money is always unpleasant but it does reinforce the message that investing is not easy and you always need to know what you've got yourself into.

By **Daniel Coatsworth** Editor

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# The companies that could benefit from Thomas Cook's demise

The travel operator's collapse creates opportunities for a number of UK stocks

The collapse of the world's oldest travel company Thomas Cook has major implications for other companies on the stock market. Our preferred stocks to play this situation are **Dart (DTG:AIM)** and **On The Beach (OTB)**.

Thomas Cook has approximately 2.5m customers, representing 28% of the UK's offline market and 10% of the online market. Rival travel companies will now be trying to lure these individuals and increase their own market share. Capacity will also reduce significantly, boosting the pricing environment.

On the day of Thomas Cook's collapse shares rallied in various travel operators including holiday sellers and airlines.

There is some logic to these moves if the collapse of Monarch airlines in October 2017 is any guide to the current situation.

Back then short-haul holiday revenues from the UK were boosted across the whole sector, with Dart seeing a 16% jump in its average fare per passenger mile in the summer of 2018.

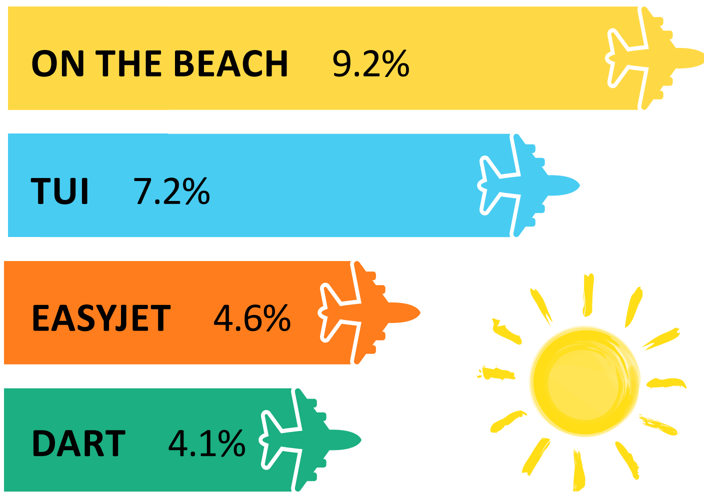
Dart could be a major beneficiary because it offers both flight-only and package holidays and is a natural home for customers looking for something similar to Thomas Cook's propositions.

In particular, Dart's Jet2.com and Jet2Holidays are well placed to strengthen their market leading positions on the Iberian Peninsula given that the region represented a third of Thomas Cook's capacity.

**TUI (TUI)** should welcome the removal of Thomas Cook from the market, particularly as it reduces competition at a time when it is finding life hard.

On The Beach is well positioned to profit from the situation, but will likely suffer shorter term costs. Historically 15% to 20% of its flights were booked using Thomas Cook so the company will have to find alternative arrangements, which will inevitably be more expensive.

### BIGGEST STOCK MOVERS ON THOMAS COOK'S COLLAPSE




Data refers to one-day movement on 23 September 2019. Source: Shares, SharePad

Analysts at Liberum believe the company will take around a £7m hit, higher than the £2m charge it booked due to the Monarch collapse.

However there will be opportunities to grab market share in light of the company's Classic Package Holidays business which boasts over 1,300 agents on its business-to-business portal.

The effects should crystallise in the second half of next year with more significant benefits from 2021 onwards. Liberum calculates that if the company were to hold its current market share, it could see revenues increase by close to a third.

**EasyJet (EZJ)** and **Ryanair (RYA)** should benefit strategically from reduced competition in the European short haul market. It also comes at an interesting time for EasyJet which is trying to build up a holiday business.

# Should you invest in Airbnb when its shares hit the stock market next year?

The accommodation platform looks more interesting than recent stock market flops Uber and Lyft

Home-sharing start-up Airbnb plans to join the US stock market in 2020. The news broke just days after WeWork, the office space sharing business, was forced to delay its own stock market plans after struggling to convince investors of its long-term profitability and having corporate governance issues.

Airbnb looks a much more attractive investment proposition to us than WeWork. Its business model is fairly simple: it provides a platform for people to book a stay in someone else's home.

It claims to have 7m listings in over 100,000 cities worldwide, with 8.2m guests staying in Airbnb-listed properties in the year to 31 July 2019.

The company was last valued at $31bn in September 2017 and while limited financial data is available, analysts believe the company will look for a market valuation of between $38bn and $50bn.

'Airbnb has a really scalable business model and, frankly, if it prices its IPO (initial public offering) realistically I would expect it to be well received,' says Richard Holway, founder of the TechMarketView website.

The company was founded in 2008 by chief executive Brian Chesky, along with two roommates. The trio started the business by renting air mattresses in a room in San Francisco and it has grown rapidly, raising around $4.4bn of growth funding from backers, including Amazon's founder Jeff Bezos.

Airbnb owns no property and simply acts as a broker between traveller and property owner. It also manages payments, acts as a mediator in the case of grievances, and lists reviews of both hosts and travellers.

This asset-light model gives the company far more flexibility over large hotels chains with vast property estates to run and fund.


Airbnb generated more than $1bn revenue in its most recent quarter and has made more than $80bn for Airbnb hosts since its launch 11 years ago. Although no profit figures were disclosed all previous announcements have indicated that Airbnb was profitable in both 2017 and 2018.

Diversifying and expanding its platform and revenue streams has included complementary travel services, allowing guests to book local tours, cooking classes, and other cultural immersion activities through its platform.

Plans also include a loyalty programme, attracting higher quality places to stay, and creating a corporate travel business. It also wants to break into China.

Regulation remains a risk. Airbnb has faced criticism of feeding over-tourism in some destinations, pushing up rents beyond the reach of local residents. The company has also mulled starting its own airline, which would represent a huge departure from its current business model.

We need more detailed data to form a proper opinion on the investment case, but at this early stage Airbnb looks a lot more enticing than some of the headline grabbing stock market flotations this year, such as Uber and Lyft, which have both flopped.

# Climate change protests put sustainable investing back in the spotlight

New UN goals and an 'impact exchange' could be on the agenda

Last Friday (20 Sep) saw coordinated demonstrations around the world by young people angry at what they see as a lack of progress by governments and businesses in tackling climate change. This topic is becoming increasingly important to investors.

The latest data from the World Meteorological Organization shows that the five-year period from 2014 to 2019 is the warmest on record.

The amount of greenhouse gases going into the atmosphere actually rose by 20% in the last five years compared with the previous five years.

The oceans have absorbed 90% of the excess heat generated by global warming, fuelling a rise in temperatures, acidity and sea levels.

There are fears that the increase in sea levels in particular has passed a tipping point, and rather than slowing it is actually accelerating, contributing to the recent disasters in the Bahamas and Mozambique.

As well as the human and environmental toll, the growing frequency of natural disasters is heaping costs on the global insurance industry.

On Monday (23 Sep) the United Nations (UN) held a climate change summit in New York at which it proposed ending subsidies for all fossil fuels for power generation, accelerating the closure of existing coal-fired power stations and an end to building new plants.

This would clearly be negative for thermal coal-mining firms like **Anglo American (AAL)** and **BHP (BHP)**, although UK electricity generators such as **SSE (SSE)** have already invested heavily in renewable energy and would be less affected.

Ironically, while China, India and the EU committed themselves to tougher carbon-reduction plans, the US – which under President Trump has rolled back over 80 climate change regulations – refused to take an active role.

**"President Trump has rolled back over 80 climate change regulations"**

In another example of the environment grabbing the agenda, a new UK 'impact-focused' stock exchange has been proposed.

Based in Scotland, the exchange hopes to be the first in the world to mandate the annual reporting by issuers of the social and environmental impact of their business.

The proposal has the backing of the UN, which described the exchange as 'a game-changer for our planet'.

Companies and funds wanting to list will need to prove that they 'generate a measurable, beneficial social or environmental impact alongside a financial return', while their performance will be measured against the UN's Sustainable Development Goals.

Potential candidates for inclusion may include **Biffa (BIFF)**, **Impax Environmental Markets (IEM)**, **John Laing Environmental Assets (JLEN)**, **Gresham House Energy Storage Fund (GRID)** and **Pennon Group (PNN)**.

# India-focused investment funds rally on economic stimulus plan

Four London-listed investment trusts could benefit from India's tax changes

Indian Prime Minister Narenda Modi has slashed corporate tax rates in a bid to boost the faltering economy in a move triggering euphoria in the Indian equity markets.

Shares in the UK stock market's quartet of India-focused investment trusts all joined in the rally, being **Aberdeen New India (ANII)**, **Ashoka India Equity (AIE), India Capital Growth Fund (IGC)** and **JPMorgan Indian (JII)**.

Modi's $20bn tax cut package, estimated at 0.8% of GDP, risks increasing the budget deficit. But by reducing India's effective corporate tax rates from 35% to 25% it provides a major boost to the domestic manufacturing sector and the 'Make in India' vision.

Taxes on new manufacturing investment were slashed to 17%, making India more competitive versus tax rates in Vietnam, Indonesia and Bangladesh.

Against a backdrop of rising US-China trade tensions, which are reconfiguring global supply chains, India's corporate tax cuts are expected to help encourage jobs-generating foreign direct investment.

Ramesh Mantri of White Oak Capital Management, the investment adviser to Ashoka, says this reform will reduce the cost of doing business in India and make India globally competitive to attract new investments and new businesses.

He adds: 'A boost to corporate earnings and earnings growth is just the first order impact. The second order effects could be lower consumer prices, aiding demand revival along with spurring private investments.

'While there could be fiscal deficit concerns, the resultant growth spurt and better tax compliance due to lower taxes are major mitigants.'

David Cornell, fund adviser to India Capital Growth, believes the biggest immediate beneficiaries will be consumer discretionary and banking. He comments: 'Any new investment in manufacturing will enjoy a rate cut from 25% to 15%, making India's tax rates globally competitive at a time when investment into China is under threat.'

Rob Brewis, an investment manager at Aubrey Capital Management, argues the corporate tax cut 'throws up very few losers and plenty of winners'.

He adds: 'The economic impact will hopefully be felt mostly in corporate investment, especially in manufacturing and infrastructure, which will in turn lead to much needed job and income growth.'

**INDIA-FOCUSED INVESTMENT TRUSTS RALLY ON TAX NEWS**

| Investment Trust | Share price change* |
|---|---|
| Aberdeen New India | 10.1% |
| JPMorgan Indian | 8.9% |
| India Capital Growth | 8.6% |
| Ashoka India Equity | 5.3% |

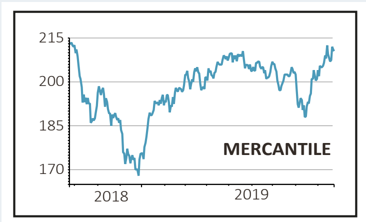
*20 Sep to 24 Sep 2019. Source: Shares, SharePad

# Mercantile's 10% NAV discount is too good to miss

135-year-old trust invests in tomorrow's market leaders

**THE MERCANTILE INVESTMENT TRUST**
**BUY**
(MRC) 210.5p
Stop loss: 168.4p

Total assets: £2.14bn




Investors have a chance to buy highly-respected **The Mercantile Investment Trust (MRC)** for 10% less than the value of its underlying assets. A key reason why it is trading cheaply is exposure to UK stocks and the market pricing in a Brexit discount should the UK economy sour.

The mid-cap specialist trust focuses on identifying tomorrow's market leaders by targeting companies outside of the FTSE 100 with significant room for growth.

The 135-year-old trust seeks to provide long-term capital growth from a portfolio of UK stocks, while achieving long-term dividend growth at least in line with inflation.

Steered by fund managers Guy Anderson and Anthony Lynch, the focus is firmly on valuation and catalysts.

According to Morningstar, the quarterly dividend payer puts money to work with firms where it believes the stock market's perception of their profitability is underestimated and which can 'gain market share in rapidly growing markets, those able to disrupt incumbents, or those availed with a nimble business model'.

Within the value space, Mercantile seeks stocks that have disappointed or been neglected by the market, where there is an attractive valuation and the prospect for a turnaround to drive a higher share price.

Within the growth arena, Anderson favours stocks whose earnings and cash flow profiles are underestimated by the market and where there is solid valuation support.

Morningstar also points out that under Anderson's guidance, the portfolio has become higher conviction with fewer holdings and looks increasingly different to the benchmark (a higher active share).

*Shares* believes Mercantile's

*Rolex* seller, Watches of Switzerland feature in Mercantile's portfolio

bias to small and medium sized companies provides welcome diversification to a portfolio focused on UK large caps.

And despite the perceived domestic nature of UK-listed stocks, over which Brexit continues to weigh, it is worth noting that just under half of the revenues are derived from overseas markets, mainly shared between Europe, North America and emerging markets.

Top 10 positions as at 31 August included alternative asset manager **Intermediate Capital (ICP)**, housebuilder **Bellway (BWY)**, and **Softcat (SCT)**, a UK IT reseller.

Other names include building products play **Marshalls (MSLH)** and the gold and silver miner **Polymetal (POLY)**.

Mercantile also hold stakes in two recent additions to the stock market: train and bus ticket seller **Trainline (TRN)** and **Watches of Switzerland (WOSG)**, which distributes over half of the UK's *Rolex* watches.

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

# Filtration firm Porvair is a reliable business built on large recurring revenues

Regulation and niche markets are ideal places for steady growth

With roots in the engineering world **Porvair (PRV:AIM)** has emerged as quite the expert in the filtration process. It has earned a reputation for reliability and is well-placed to withstand the economic knocks of the future.

The company is active in various different parts of the market. For example, it provides filters used in aluminium casting and super alloy manufacturing.

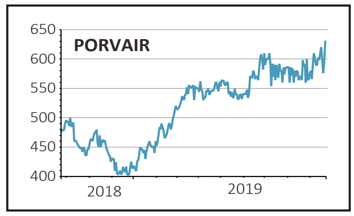
Its filters are also used in aviation fuel and cooling supply systems, energy industry gasification equipment (turning fossil fuel or biomass into gas). It also has a laboratory analysis arm which is involved in areas like testing for chemicals in water supply systems.

Porvair's filters are vital components for the smooth running of some very expensive capital equipment. For example, a temporary shutdown of an aluminium smelting works or the grounding of planes because they do not have the right filters would cost operators millions of pounds in lost earnings.

Its filters are designed for systems that are often patent protected and bespoke. This leads to lots of repeat business on long lifecycle kit, about 80% of recurring sales, the company has said. This means income tends to be recurring and predictable, while also making it an expensive and time-consuming process for a customer to switch supplier.

**PORVAIR BUY**
(PRV) 630p
Stop loss: 504p

Market cap: £289m




Porvair deliberately targets niche markets where demand drivers and strong barriers to entry are high, either through technology development or from increasing regulation.

That doesn't entirely rule out an element of lumpiness in sales but the company has managed volatility impressively in the past. Between 2014 and 2019 the company has put up 8% average revenue growth per year and 14% in earnings, while order books are said to be healthy with order intake strong in the third quarter.

Nevertheless, this remains something for investors to watch, as is expansion. Porvair is fairly new in China where it now runs two sites. Part of the challenge is moving the Chinese aluminium industry (the world's largest) from cost-conscious quantity to quality. Embracing better filtration performance should be a boon for Porvair, although overseas firms have failed in China before.

Dividends are small with a mere 0.9% yield but this remains a growing business and payouts are increasing in the mid-to-high single digits.

Investors should note that the stock trades on a premium rating of 23.9 times forecast earnings for the next 12 months. However, that is justified by good earnings visibility, defensive characteristics and attractive earnings growth prospects.

Forecasts call for adjusted pre-tax profit of £14.5m in the year to 30 November 2019, rising to £15.6m in 2020 and £17.2m in 2021.

By **Steven Frazer**
News Editor

# DIVERSIFYING FOR GOOD AND GROWING INCOME OPPORTUNITIES

In its latest Dividend Monitor, looking at income paid by companies to shareholders, Link Asset Services reported an important feature that is often overlooked, dividend growth. In this case, its report highlighted that underlying dividend growth of UK listed companies was weaker than expected. So, why is this important? Research shows that dividend growth companies tend to outperform the market in the long term.

However, as Michael Kempe, chief operating officer at Link Market Services said: "the UK's dividend clothes are starting to look a bit threadbare underneath."

One way to combat this trend is to look at a wider set of income opportunities. The Diverse Income Trust plc is able to do just this as it invests across a range of larger and smaller listed companies looking to generate a good and growing stream of dividend income. One of the great advantages of this approach is the broader investment universe it can access.

Many investments that have an objective of delivering dividend income invest in the largest listed companies as these are the largest sources of dividend income.

However, the largest listed companies tend to operate in a limited range of industry sectors, which means that their dividend income is closely linked to the prosperity or otherwise of the relevant industries. The Diverse Income Trust invests across a much wider investment universe and its portfolio income is therefore derived from a broader range of sectors. Importantly, this wider opportunity set also enables the fund managers to avoid participating in some industry sectors where their dividend prospects are anticipated to be less certain.

The company has demonstrated that it is able to deliver good and growing income. Since the Trust launched in 2011 it has increased its dividend year-on-year by 8.8%. The bar chart below shows the Trust's dividend history.

Furthermore, with a larger universe of company shares to choose from there is better scope to be risk sensitive, for example through minimising the need to hold the shares of companies that have significant corporate debt. Many of the companies in the portfolio have been selected on the basis that they tend to have stronger balance sheets, as those with excessive debts often suffer disproportionately during more economically challenging periods.

It is also anticipated that, if the Trust succeeds at delivering dividend growth, then over the longer term this could be accompanied by capital gain.

**The Diverse Income Trust plc**

*powered by* Miton

*Genuinely active investing*


**RISKS**

**The value of investments will fluctuate which will cause trust prices to fall as well as rise and investors may not get back the original amount invested.**

**Forecasts are not reliable indicators of future returns.**

**Past distributions of dividends are not a guide to future distributions.**

**In certain market conditions companies may reduce or even suspend paying dividends until conditions improve.**

**Find out more at** mitongroup.com/diverseincome

The Diverse Income Trust plc Dividend Distributions (pence per share)


The fourth interim dividend and the special dividend have not yet been paid but have been declared by the Trust and are subject to a shareholder vote at the Company's AGM on 9 October 2019.

## NEXT
### (NXT) £58.26

**Gain to date: 39%**

**Original entry point:**
**Buy at £41.91,** 20 December 2018

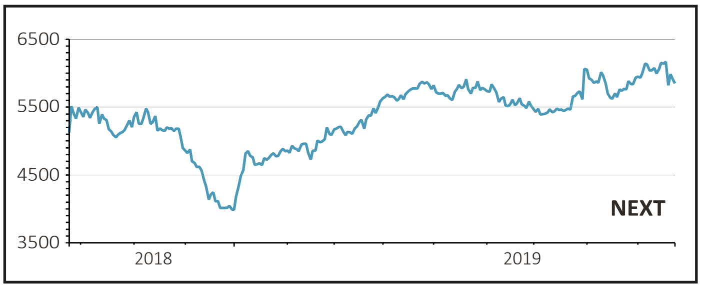

SHARES IN HIGH street bellwether **Next (NXT)** have eased back on profit-taking following first half results (19 Sep), with the absence of further earnings upgrades and a cautious outlook statement weighing on the stock.

Yet we're sitting on a near-40% gain since saying to buy the shares last December.

Results for the six months ending 31 July 2019 showed 12.6% growth in online sales, while retail sales declined by 5.5%. Pre-tax profit nudged 2.7% higher to £320m and Next maintained full year guidance for pre-tax profit to be up 0.3% at 'around £725m' with earnings per share growth of 5.2%.

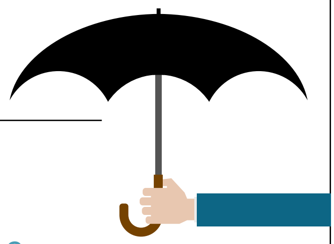
Chief executive officer Simon Wolfson highlighted a weak start to the autumn season due to warm September weather and the expectation is the fourth quarter will be better than the third quarter.

Next isn't panicking over Brexit, saying it will 'only materially affect consumer spending in the event that it triggers inflationary pressure on prices or logistical problems at our ports'.




**SHARES SAYS:**
**Next's shares have had a stellar run year-to-date, but we are sticking with the high-quality, cash-generative shopkeeper as one of our key picks in the structurally challenged retail sector.**

## S&U
### (SUS) £21.40



**Loss to date: 4%**

**Original entry point:**
**Buy at £22.20,** 30 May 2019

SHARES IN MOTOR finance and bridging loan provider **S&U (SUS)** have traded in a narrow range since we said to buy in May at £22.20, despite steady progress in the business.

The non-prime segment of the used car market serviced by S&U's Advantage motor finance brand has been relatively immune to the challenges facing the new car market and applications for loans continue to hit record levels.

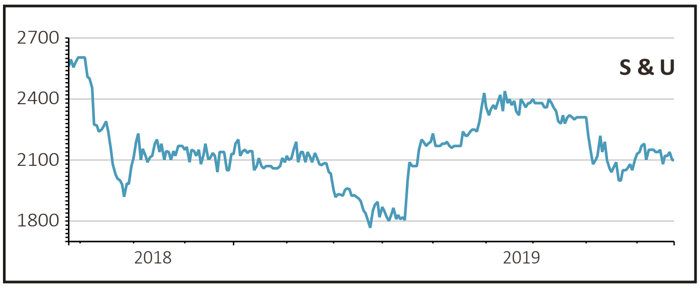
That has allowed Advantage to be more selective in whom it lends to and the terms it sets, which means that the quality of its lending has improved.

The appointment of Graham Wheeler, who brings many years of finance experience at VW and Jaguar Land Rover, to head up Advantage is also a positive move.

Meanwhile the property lending business, Aspen Bridging, has also seen record loan enquiries but a prudent approach means the loan book remains high quality.

Since inception more than half of Aspen's 137 loans have been repaid in full and only one has experienced impairment, which was a loss of some default interest rather than capital.

Both the used car market and the new home market offer plenty of room for growth, and on 8.5 times this year's earnings with a 5.8% dividend yield the shares still look good value.




**SHARES SAYS:**
**Keep buying S&U**

THIS IS AN ADVERTORIAL

Allianz Global Investors

# Digitalisation – Opportunities and Risks

**LUCY MACDONALD**
Portfolio Manager of The Brunner Investment Trust

Stock markets can be very volatile in the short term. Economic data, current affairs and swings in sentiment can all move prices up and down sharply. Over longer time periods, these short-term movements tend to be outweighed by longer-term fundamental trends.

One trend that has played a particularly important role is digitalisation. Companies are bringing technology into every aspect of our lives, creating new industries and forcing mature ones to adapt. For investors, this has presented both opportunity and risk. Some companies – both new and old – have been able to use technology to their advantage, whilst others have suffered under the brutal force of capitalist logic.

Over the past decade, many of Brunner's best investments have had their roots in correctly assessing the longer-term impact of new technology. Just as important however, is understanding where our view differs from consensus. This is well illustrated by Microsoft, the Trust's largest holding.

We first bought shares in Microsoft in 2012. At that time, the company was heavily dependent on sales of traditional Windows and Office software. Some investors feared Microsoft's earnings would suffer as new mobile and cloud-based operating systems (such as Android) entered the market. Consequently, the shares carried a remarkably low valuation for such an enormously profitable business.

What the stock market missed was Microsoft's ability to transition its own customer base to a cloud subscription model, thereby ensuring the survival of its valuable monopolistic position. At the same time, the company built up a powerful web services business that has been and continues to be a key driver of growth and profits. These changes have led to a change in the stock market narrative on Microsoft, from imminent maturity and decline towards innovation and growth. This has been reflected in the shares, which have risen threefold in response.

Today, the theme of digitalisation is front and centre of our investment landscape. That there will be big winners and losers is now conventional wisdom and well reflected in stock market valuations. We see investors crowding into the big names such as Amazon and Google. Both are without doubt successful companies, but do they really have enough future growth to justify their now enormous market capitalisations? Even if they do, we think there are easier pickings elsewhere.

We see numerous opportunities for companies to benefit from digitalisation, though many of these are in ways not

## The Brunner Investment Trust PLC

immediately obvious to the casual observer. Nor are they typical "Technology" names. Instead, we look for strong business models that have withstood the test of time and where technological innovation may present an opportunity to improve growth and profitability substantially. And of course, as an asset manager, we want a valuation that doesn't already reflect this upside potential.

**To discover more about Brunner, visit www.brunner.co.uk where you can register for regular updates.**

All sources Allianz Global Investors GmbH unless otherwise noted. This is no recommendation or solicitation to buy or sell any particular security. A security mentioned as example above will not necessarily be comprised in the portfolio by the time this document is disclosed or at any other subsequent date. Investing involves risk. The value of an investment and the income from it may fall as well as rise and investors may not get back the full amount invested. Past performance is not a reliable indicator of future results. The views and opinions expressed herein, which are subject to change without notice, are those of the issuer and/or its affiliated companies at the time of publication.

**Lucy Macdonald is CIO of Global Equities at Allianz Global Investors and is portfolio manager of The Brunner Investment Trust PLC. Brunner aims to provide its investors with growing dividends and capital growth by investing in a portfolio of global equities. Although past performance is no guide to the future, Brunner has paid a rising dividend to shareholders for 47 consecutive years.**

## BAE SYSTEMS
(BA.) 563.2p

### Gain to date: 12%
**Original entry point:**
**Buy at 503p,** 17 January 2019

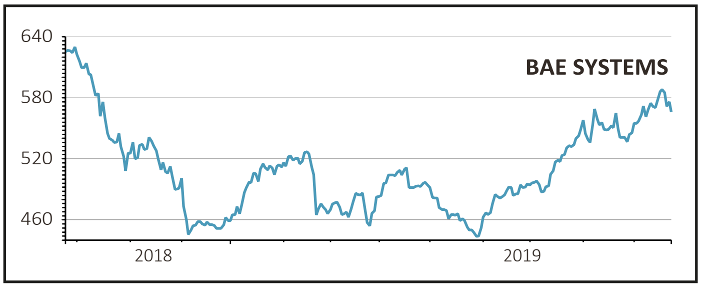
SHARES IN AEROSPACE and defence contractor **BAE Systems (BA.)** have continued to make steady progress following first half results which showed healthy growth in revenue, earnings and margins.

Defence spending is rising in the US, where BAE is winning more work, and among NATO countries such as the UK, the Netherlands and the Baltic states.

In the US, major multi-year contracts include the F-35 fighter, which uses BAE's short take-off and vertical landing technology, and the latest generation of armoured multi-purpose vehicles for the US Army.

Meanwhile a deal to supply Qatar with Typhoon fighters has been accelerated and closer to home work for the Navy continues with the new 'Prince of Wales' aircraft carrier and the fourth Astute-class submarine due to undertake sea trials soon.

Better sales growth and improved visibility of earnings has led to a 25% re-rating in the shares this year, putting them on 14 times earnings against 11-times in January, but they still look attractive compared with US rivals Lockheed Martin and Northrop Grumman which trade on 18 to 19 times earnings.




**SHARES SAYS:**
**While a 'hard' Brexit doesn't present a major business risk, there is still political risk in the UK should Labour win a general election and risks around doing business with Saudi Arabia remain. On balance we are still happy to continue buying the shares.**

## JUDGES SCIENTIFIC
(JDG:AIM) £38.30

### Gain to date: 68%
**Original entry point:**
**Buy at £22.80,** 11 April 2019

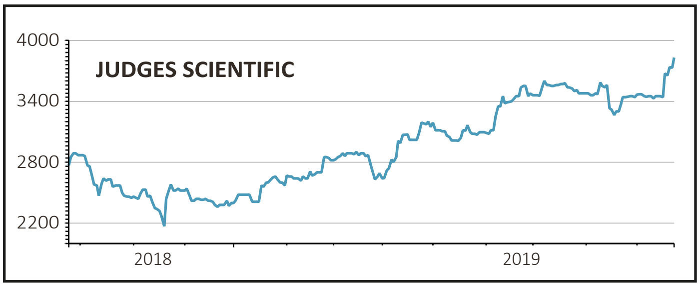
HALF YEAR RESULTS delivered everything investors could have desired, underlining once again how science kit maker **Judges Scientific (JDG:AIM)** is a high quality business.

New first-half records were set for revenue, adjusted pre-tax profit, earnings per share, cash generation and dividends, the latter up 25% to 15p per share that is still covered seven times by adjusted earnings. All of this growth was achieved without any help from acquisitions.

That the share price jumped 7% on the day (18 September) and has continued its steady rise stands testament to how increasing numbers of investors like the stock.

Stockbroker Shore Capital increased its earnings per share forecasts by 9.2% to 208p for 2019, and by 5.2% to 208.2p for 2020.

Our original article claimed the stock deserved a higher price-to-earnings earnings multiple than 14.8 times 2019 earnings. The shares have jumped 68% yet the rating still only stands at 18.4 which is not excessive given its qualities and achievements.

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**A very good business that we continue to support. Keep buying the shares.**

SHARES AJBell

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**The best and worst performing shares this year, planning a tidy death, investing for a house deposit and the most popular job searches**

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# Why M&S' relegation from the FTSE 100 doesn't mean the death of the High Street

ADVERTORIAL

Schroders

**Fund manager Jean Roche argues why M&S' historic relegation from the FTSE 100 is not all doom and gloom for UK retailers.**

Marks and Spencer (M&S) was relegated from the FTSE 100 after the close of business, 20th September 2019. This was the first time that the company has lost its blue chip status.

The UK retailer was a founder member of the FTSE 100 and a stalwart of the UK High Street. But its share price has fallen 37% since the start of 2018 and is now at a near 20-year low amid online competition and falling sales.

M&S opened for business as a market stall in Leeds in 1884. "Don't ask the price, it's a penny" was its slogan and by 1984 it had grown to become one of the UK's 100 biggest companies.

There are now just 27 original members left in the FTSE 100.

**Jean Roche, Fund Manager, Pan-European Small and Mid Cap Team**, says: "M&S is not alone among traditional bricks and mortar retailers when it comes to the challenges they face."

"In the past, retailers have been able to be mediocre, but profitable. People now have much more choice, so retailers have to be smarter considering the competition posed by online disruptors such as Amazon and more nimble new competitors.

"Those that find a way to adapt will survive and prosper. Those that don't will fall by the wayside."

**What is the FTSE reshuffle?**

The FTSE reshuffle occurs once every quarter.

Companies are automatically promoted to the FTSE 100 from the FTSE 250 when they rank within the top 90 companies in the UK in terms of value.

Firms are automatically ejected from the FTSE 100 if they fall outside the top 110 largest companies.

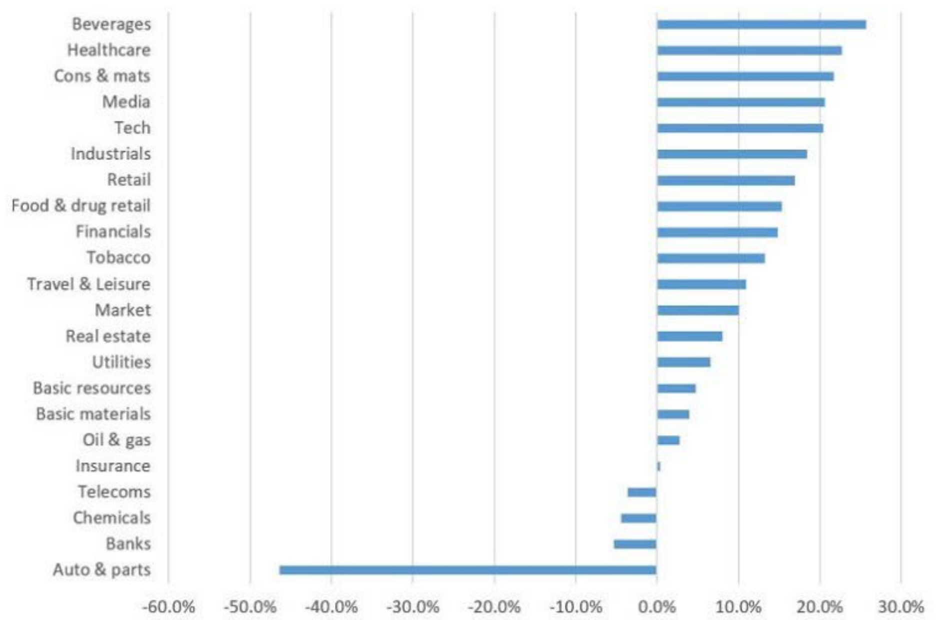
**Look beneath the headlines**

The relegation of M&S to the FTSE 250 index is the latest in a long line of downbeat headlines for the UK's High Street retailers. It has been the same for the last decade.

From the closures of Woolworths and HMV, to Debenhams and House of Fraser falling into administration, the obituaries for the High Street have long been written.

But amid the gloom there have been some rays of light. For instance, JD Sports, the sportswear retailer, got promoted to the FTSE 100 during the previous reshuffle three months ago.

**UK sector performance in 2019 – year-to-date**




Source: Schroders. Refinitiv data correct as at 4 September 2019. Past performance is not a guide to future returns.

**How UK sectors have performed in 2019**

You might also be surprised to find out that UK retailers have recorded double-digit returns this year (see graphic, above), which includes dividends as well as share price gains.

Retail is the seventh best performing sector in 2019, returning 16.9% up to 4 September.

This is more than the market which is up 10%, according to the Thomson Reuters UK Index tracker.

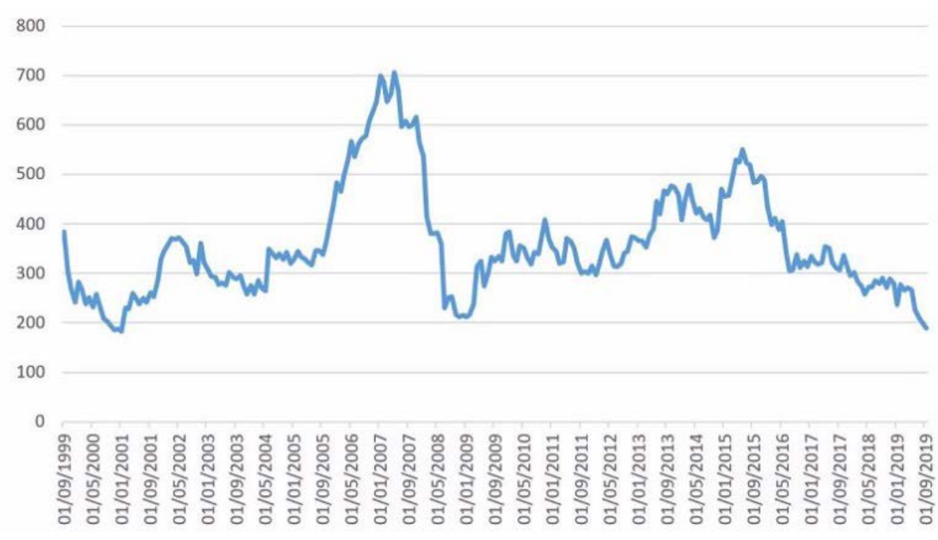
Beverages and healthcare lead the pack with returns of 25.7% and 22.6% respectively.

The auto sector is the worst performing, losing 46.4%.

**Retailers have endured a poor decade**

This year's performance should be put in context. Over the last ten years retailers have returned 2.8% on an annual basis.

**Marks and Spencer's share price over the last 20 years**




Source: Schroders. Refinitiv data correct as at 4 September 2019. Past performance is not a guide to future returns.

That compares with the UK market which has returned 4.5% annually. The best performing sector – technology has returned 17% a year.

UK inflation over that same period has been 2.7% according to the Bank of England inflation calculator.

That means returns adjusted for inflation, or "real" returns for the retailers has been 0.1% a year over the last decade, 1.8% for the overall market and 14.3% for the tech sector.

The relentlessly downbeat mood music from the media (and pessimism among analysts) appears to have filtered through to investors.

But is it confirmation that the UK consumer is in full retreat, and consumer-exposed sectors are in deep trouble?

Jean Roche sees plenty of reasons for optimism.

**Specialist retailers shine through**

"Some major bricks-and-mortar retailers have suffered sharp sales slowdowns, resulting in multiple profit warnings last year and this," says Roche.

"But among businesses that are better adapting to the structural shifts reshaping the High Street, the news has been encouraging; many have capitalised on their competitors' weaknesses.

"Companies such as homewares retailer Dunelm, pets supplies specialist Pets At Home and athleisure leader JD Sports have bucked the gloomy retail trend.

"They are all good examples of retailers giving customers what they want, coping well with the shift online and investing to improve customer experience.

"They are also benefitting from structural growth in their underlying markets, for example, in the case of Pets at Home, an increase in spend on pets.

"The promotion of JD Sports from the FTSE 250 to the top flight, just as Marks and Spencer, a FTSE 100 founding constituent, is rejected, encapsulates the changes underway in the retail sector.

"It also supports our belief that the odds of success are skewed in the favour of investors in UK small and mid-cap (SMID) companies.

"This is an area of the market packed full of companies taking advantage of new technologies and the internet to drive growth, disrupt and take share from sector incumbents.

"In a fast-evolving world, SMIDs are generally better able than large caps to capitalise on the opportunities as they tend to be more dynamic, and have a small base from which to achieve growth.

"The rise and demise of these two companies perhaps also serves to underline the importance of an active approach to investment.

"There has been a significant difference in performance between the best and worst retail stocks this year and investors who merely tracked the sector will not have been able to capitalise on this.

"Towards the end of 2018, a number of consumer-focused sectors, including UK retailers, "de-rated" significantly in excess of the wider market. In other words their shares fell sharply without any marked change in underlying earnings expectations as investors became concerned there could be further bad news to come.

"For a time dividend yields in high single digits were not unusual. In some instances they correctly signalled impending distress. This was certainly the case with Marks and Spencer, which subsequently re-set its dividend by 40%.

"The strong year-to-date performance by the sector as a whole suggests that investors lost some perspective earlier in 2019

"Also, perhaps, the standout returns of the best retail stocks tells you the market at times is simply unable to discern good companies from poor ones.

"Investors who stuck with the best companies have done particularly well, with Pets at Home, JD Sports and Dunelm being the three top performing retail stocks.

"They are up 105%, 77% and 63% respectively year to date (as at 30/08/19, total return basis, FTSE All-Share general retailers sector).

"Valuation discrepancies in the sector may not be quite what they were at the beginning of 2019.

"However, in our opinion there remains plenty of reasons to be optimistic about the outlook for the UK's dynamic and innovative retailers."

"The strong year-to-date performance by the sector as a whole suggests that investors lost some perspective earlier in 2019"

# Record levels of corporate debt is not good news

Investors should stay on their toes as the era of low interest rates draws to an end

The failure of Thomas Cook is a timely reminder of the destructive power that excessive debt can have on shareholder value. Investors have been wiped out by the strain of the package holiday firm's £1.5bn borrowings.

A decade on from the global financial crisis and UK corporate leverage is back at pre-crisis highs, having risen steadily since 2012.

Andrew Coury, an analyst at investment bank Liberum, says corporate debt came off sharply in the wake of the financial crisis but has since steadily climbed. 'The current level of leverage in the UK is now in line with pre-financial crisis levels,' he adds.

This adds up to a record £443.2bn for UK plcs, according to the September Link Group Debt Monitor 2019, which tracks borrowings for UK listed companies, following eight consecutive years of growth.

While the change in debt has varied widely, very few sectors have managed to reduce their leverage over the past 10 years. 'Only the housebuilding, staffing and technology sectors had an improved net debt-to-earnings before interest, tax, depreciation and amortisation (EBITDA) ratio over the last 10 years,' reveals Coury. 'Leverage of debt-heavy sectors, such as telecoms, leisure and pharma has worsened.'


> **"Borrowing will always rise over the long term because debt is almost always a cheaper means of raising capital for investment than equity"**

## CHEAP TO BORROW

This situation is not altogether surprising given the loose monetary policy of successive UK governments since 2009, when a string of quantitative easing programmes combined with the lowest base interest rates in generations made borrowing very cheap.

'Borrowing will always rise over the long term because debt is almost always a cheaper means of raising capital for investment than equity,' says Michael Kempe, chief operating officer of Link Market Services, which produces the Debt Monitor.

'As companies grow, their capacity to take on new loans to finance their expansion increases.'

This is all well and good as

long as decent growth can be maintained, but that is not the case at present. The Profit Watch UK's second quarter report shows that UK plc revenues inched only 1.6% ahead between April and June, with a third of companies reporting lower sales year-on-year.

The same report shows profits for UK companies rose 3.1% between April and June, yet only because they were puffed up by the weak pound, and propped up by above-average profit from the top 40 UK-listed multi-nationals.

'Those outside the top 40 saw profits drop by a third, the fifth consecutive quarter of declines,' Profit Watch UK says. More than half of companies reported lower profits thanks to a widespread and dramatic margin squeeze since 2007, meaning an extra £787bn of revenue only generated £16bn more in profit.

## MANAGING THE EARNINGS IMPACT

Brexit bickering and parliament's prorogue paralysis has left the Bank of England loathe to raise rates and run the risk of plunging the UK into a damaging recession.

Last week the Bank of England left its base rate unchanged at 0.75%, a decision widely anticipated by the markets as interest rate policymakers juggle keeping inflation in check versus stimulating growth.

This gives the Bank of England room to cut rates in the event of a no-deal Brexit, but it has previously taken the view that a tightening of policy may be necessary post-Brexit.

If the Bank of England lifts the base rate, current levels of debt could weigh heavily on corporate earnings and share prices as companies bear increased costs of servicing debt.

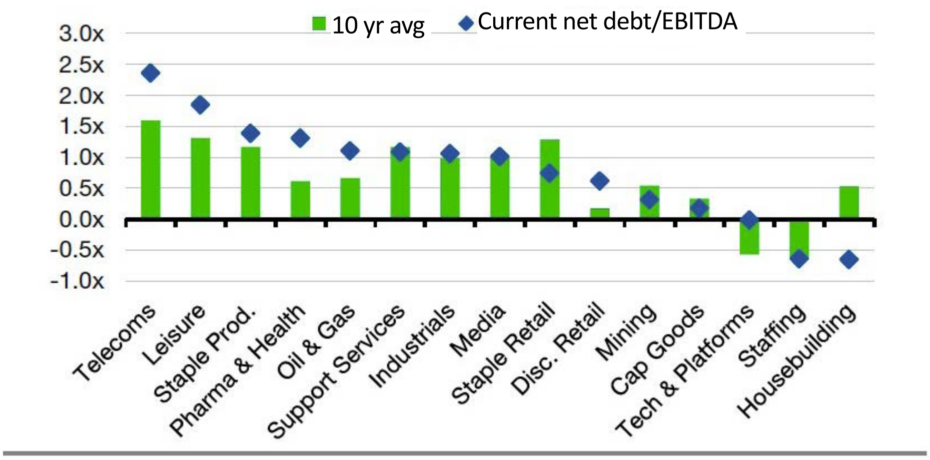
But there is little reason to panic now. 'Considering UK plc's debt pile in isolation doesn't tell the whole story,' says Link Market Services' Michael Kempe. 'Despite debts reaching new records, the measures of debt burden and sustainability are not yet stretched.'

He adds: 'It's really important to consider the burden of debt, and how sustainable it is as well. This is why the increase in borrowing in 2018/19 isn't a cause for concern.

'It's well backed by assets, and easily serviced at present by the profits companies are making. There are companies and sectors under strain, but the overall picture is reasonably comfortable.'

By **Steven Frazer**
News Editor

## FEW SECTORS HAVE MANAGED TO IMPROVE THEIR INDEBTEDNESS OVER THE LAST DECADE




Source: Liberum, Datastream. NB Equal weighed. Chart is ranked by level or change in the last 10 years

## LEVERAGE HAS CLIMBED TO PRE-FINANCIAL CRISIS LEVEL


Source: Liberum, Datastream. NB Equal weighed Net Debt/EBITDA for the FTSE 350 ex Investment Trusts

# INVESTING UNDER THE CLOUDS OF BREXIT

## HOW TO POSITION PORTFOLIOS FOR A DEAL, NO DEAL OR DELAY

With just over a month to go until the UK's scheduled departure from the European Union and, just like everyone else, investors are none the wiser on whether we face further Brexit delay, no deal or a negotiated exit.

Which of these three potential outcomes comes to pass is likely to be determined at a crunch EU summit on 17 and 18 October.

And, barring a vote of no confidence by MPs for which there is precious little time, prime minister Boris Johnson looks set to be leading the negotiations with the EU.

Heading into that event Johnson appears to have suffered a setback in his arm wrestle with MPs over the destiny of Brexit following a damaging decision from the Supreme Court on his decision to prorogue parliament.

But still there are considerable uncertainties over how we arrive at deal, no deal or delay. To help you navigate what could be a choppy end to 2019 this article will examine the potential scenarios in turn and what the likely market impact will be.

**LIFE AT THE CLIFF EDGE**

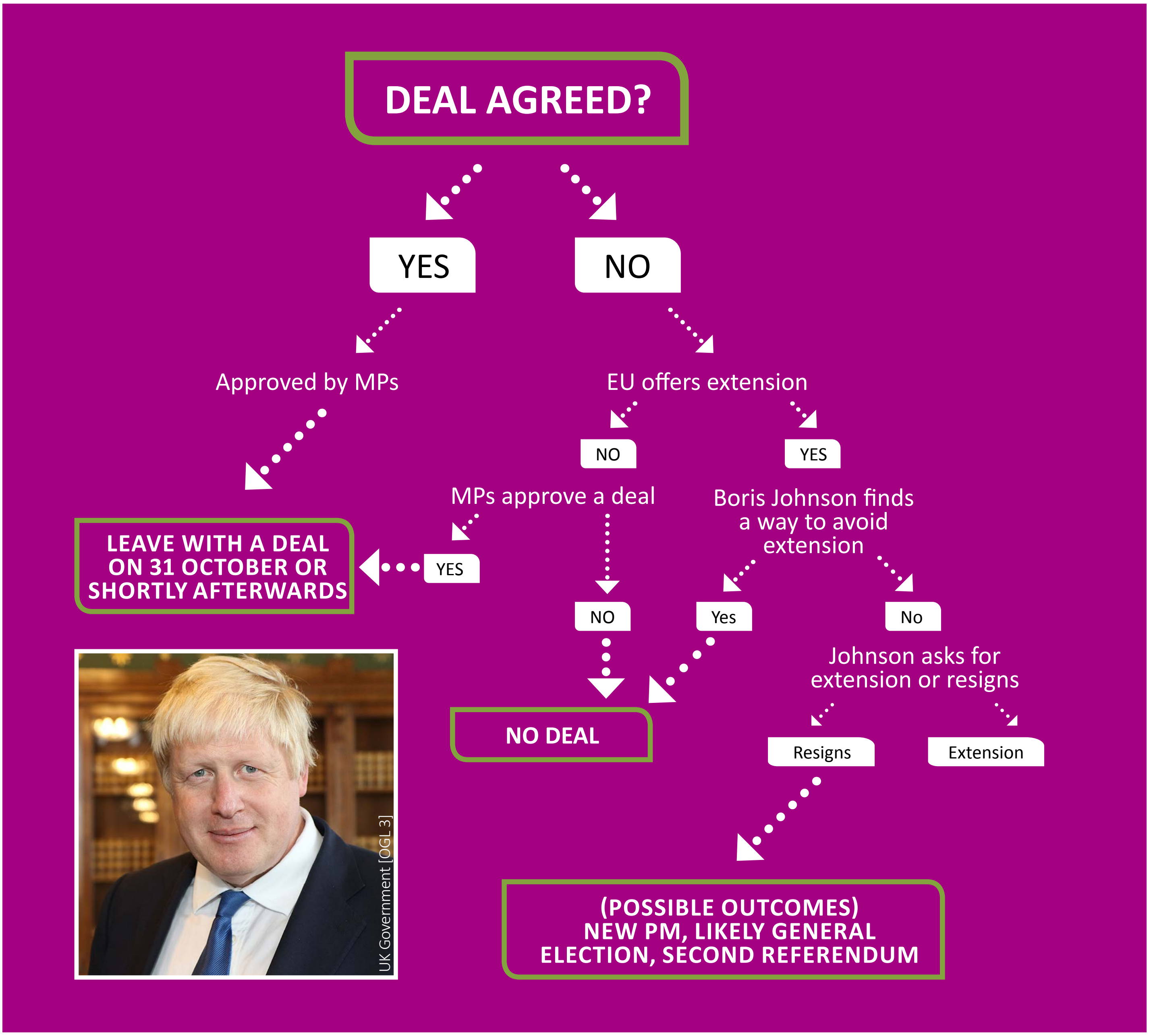
Uncertainty is the key issue for markets rather than Brexit itself. Panmure Gordon chief economist Simon French says: 'Part of the frustration with Brexit is that it is neither a single issue, nor does leaving the EU in itself codify what type of UK economy will emerge.

'The decisions over regulation, immigration, tariffs, standards and industrial strategy will be of far larger significance for the economic outlook than the simple act of being outside the EU's legal and political order.

'That Brexit enables more flexibility to frame these issues in the UK's image is a potential upside for economic growth, but that upside can also be squandered if the UK chooses to diverge from its biggest trading partner with no obvious objective.'

The main barometer for Brexit will be

# A SHORT-TERM BREXIT ROAD MAP




sterling and how it performs against other major currencies such as the euro and the US dollar.

Since the June 2016 vote to leave the EU sterling has traded in a rough range between \$1.20 to \$1.40 against the dollar, having been at around \$1.50 immediately before the vote amid expectations for a remain result. (See chart on next page)

More recently, and since the election of Johnson as Conservative Party leader and ultimate elevation to Number 10 this summer, it has traded much closer to the \$1.20 mark. This reflects Johnson's apparent greater willingness to accept a no deal outcome than his predecessor Theresa May.

Nigel Green, chief executive of wealth management firm deVere, says: 'Since Boris Johnson succeeded Theresa May in July, our consultants have registered a 35% increase in investors – both UK domestic and international – seeking to reduce their exposure to UK assets, including UK pensions, bonds and sizeable holdings of sterling. The only exception is UK property.'

## FOREIGN PREDATORS SWOOP FOR UK FIRMS

The weakness in the UK's currency has also made its companies less expensive for foreign suitors and we've seen several high profile deals since the Brexit vote.

For example, UK technology champion ARM was snapped up by Japanese firm Softbank as early as July 2016. Comcast snared pay-TV broadcaster Sky for £30bn in 2018 and **London Stock Exchange (LSE)** was recently the target of a blockbuster bid from its Hong Kong counterpart – a proposal which has been firmly rebuffed for now.

# WHAT A BREXIT DEAL COULD MEAN FOR INVESTORS

### SNAPSHOT OF POTENTIAL MARKET REACTION

- **Potential winners**: domestic stocks and funds including housebuilders, retailers, real estate and banking sectors, UK property, sterling, gilts
- **Potential losers**: exporters, multi-national FTSE 100 stocks, overseas funds

### HOW WOULD WE GET THERE?

In some ways this is the simplest outcome to unpick. The short-term possibility is that Boris Johnson secures a deal at the EU summit, perhaps with some adjustment to the key sticking point of the backstop.

European Commission president Jean-Claude Juncker remarked last week that a new Brexit deal could still be reached before 31 October, triggering a small rally in the pound.

Given the limited time available to ratify a deal there might be a brief extension to allow this process to be completed.

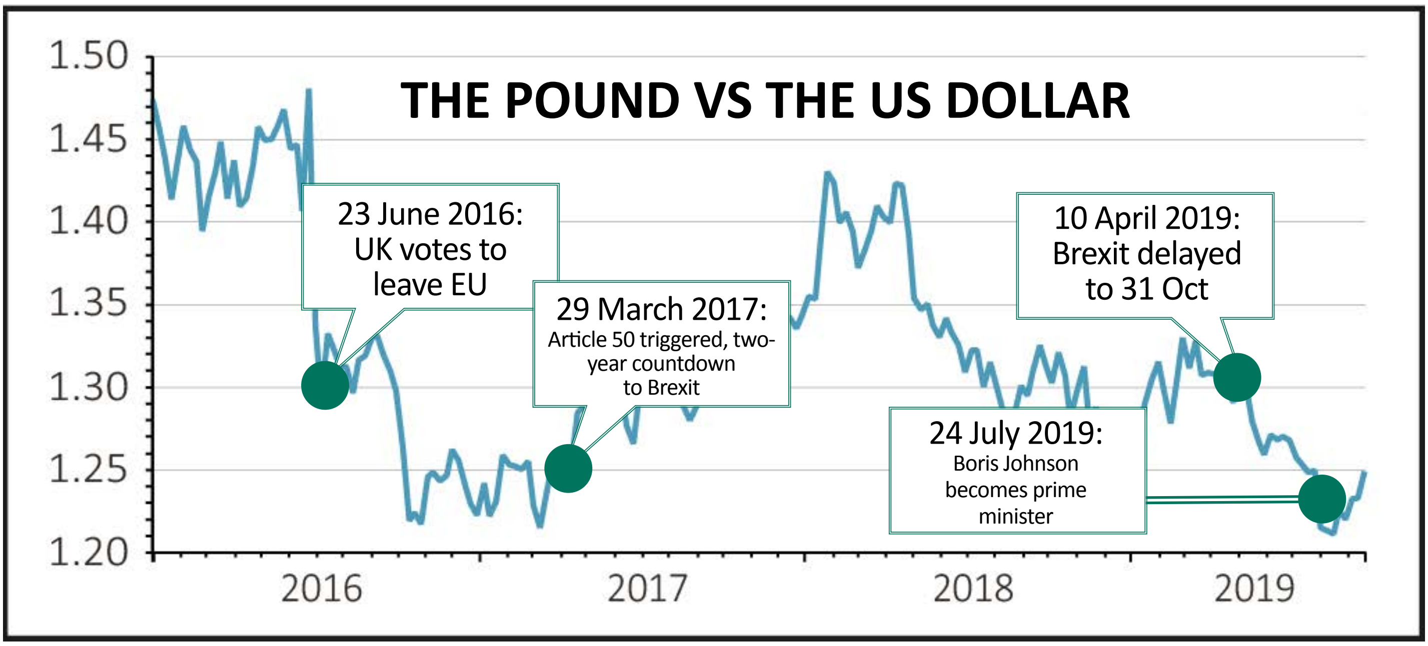
Or in the face of an imminent no deal scenario MPs could vote for a version of the deal Theresa May agreed with the EU but tried and failed to get through the House of Commons.

Alternatively a different government formed in the wake of a general election could negotiate its own deal. Or a freshly negotiated deal could be put to voters in a second referendum and win a majority.

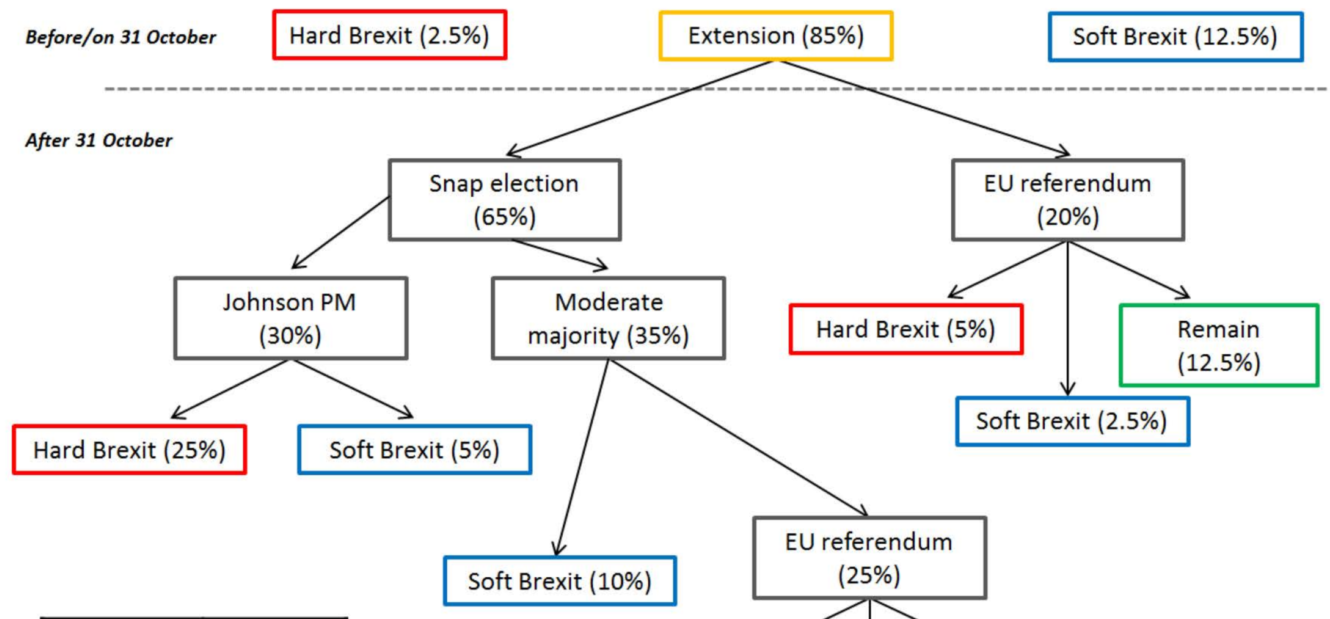
### WHAT WOULD BE THE IMPACT?

Panmure Gordon's Simon French says: 'Brexit is so multi-layered that the impacts on companies and households will vary significantly. However a sensible starting point is to assume that a deal with the EU will remove some of the near-term uncertainty and lead to a short, but significant boost in business investment, export orders and appetite for big ticket purchases.'

This sounds like good news for the UK retail sector and housebuilders, property stocks, banks and other domestic firms could get a boost. **Fidelity Special Values (FSV)** – a recent addition to our *Great Ideas* portfolio and which focuses on undervalued domestic stocks – is a good example of a fund that could benefit from a Brexit deal.



## THE CHANCES OF VARIOUS BREXIT OUTCOMES (according to Berenberg)




| Outcome | Total |
|---|---|
| Hard Brexit | 35% |
| Soft Brexit | 35% |
| Remain | 30% |

*Source: Berenberg*

# WHAT A NO-DEAL BREXIT COULD MEAN FOR INVESTORS

### SNAPSHOT OF POTENTIAL MARKET REACTION

- **Potential winners:** exporters and multi-national FTSE 100 stocks, overseas funds, likely short-term boost for warehouse owners and logistics firms

- **Potential losers**: domestic stocks including housebuilders, retailers, real estate and banking sectors, UK property, sterling, gilts

### HOW WOULD WE GET THERE?

Berenberg senior economist Kallum Pickering recently put the chance of a no-deal outcome on (or before) 31 October at 2.5% following MPs' move to legislate against this outcome. The fact there is a slim chance, rather than none at all, of having a no-deal reflects the belief that Johnson could find a loophole in this legislation.

There is now insufficient time for a general election before 31 October but an election seems almost certain at some point soon given Johnson is currently operating without a majority in the House of Commons.

If he were able to secure a majority in an election, he would be free to pursue a no-deal outcome presumably at the end of January 2020 based on the three-month extension described in the Benn bill blocking no deal.

Alternatively MPs could approve a second referendum with no deal as one of the options presented to voters, and this option could prevail.

Finally, and perhaps the most likely of these scenarios, the EU could refuse an extension, although the potential impact on member state Ireland might count against this.

**WHAT WOULD BE THE IMPACT?**

In the short-term no-deal Brexit is likely to mean significant disruption, despite more concerted efforts on the part of the UK Government to prepare for such an outcome.

Panmure's Simon French says: 'A no deal will, at a scale that is hard to know for certain, introduce additional costs for households and businesses and mute economic growth. Given the current rate of growth is quite modest, a technical recession is possible.'

The OECD is forecasting a 3% hit to UK GDP and a recession in 2020 under a no-deal Brexit.

French adds that further weakness in the pound seems inevitable. 'The scale of this drop will depend on how long the disruption persists for – but a move down towards $1.15 and parity with the euro is not out of the question,' he says.

This outcome could hurt domestic-facing stocks like housebuilders, real estate owners and banks the hardest.

Counter-intuitively the FTSE 100 might benefit, barring some short-term volatility, because weaker sterling boosts the relative value of earnings in other currencies.

Logistics businesses and warehouse owners might benefit from stockpiling as corporations look to deal with the short-term disruption.

In the longer term no deal is unlikely to result in a clean break but instead lead to further negotiations as the UK and EU grapple with movement of goods and the thorny issue of the Irish border.

## WHAT A BREXIT DELAY COULD MEAN FOR INVESTORS

**HOW WOULD WE GET THERE?**

The least complicated route is that Boris Johnson steps away from his 'dead in a ditch' rhetoric and asks for an extension, as MPs have mandated, and the EU agrees.

If he cannot find another route out, and still refuses to contemplate a delay, he would probably have to resign and somebody else would have to form a government.

Whether a 'unity' candidate or the leader of the official opposition Jeremy Corbyn – this individual's first act would be to ask for an extension.

**WHAT WOULD BE THE IMPACT?**

A delay in market terms would probably prolong the current limbo situation. Bank of England governor Mark Carney recently warned a further delay would hurt the economy by extending the uncertainty for companies and workers.

Longer term either a government emerges which takes the UK out of the EU under no deal or through a hard Brexit deal. The alternatives include a rival administration agreeing a softer Brexit with stronger ties to the EU or there is a second referendum which results in the country remaining in the EU.

The Liberal Democrats have said they would revoke Article 50 and cancel Brexit if they form a majority government after an election.

# WHAT COULD HAPPEN UNDER A LABOUR GOVERNMENT?

Some market observers have characterised the current situation as a choice between two paths, a no-deal exit under Boris Johnson or remaining in the EU under a government led by Labour leader Jeremy Corbyn.


David Hunt

The situation is not that simple. Current polling suggests Corbyn would be unlikely to form a majority government, but the political winds are very unpredictable at present and some of Corbyn's stated policies would likely have a material impact on investors.

There is always a chance he might get some of them through with the help of partners in a coalition. Corbyn heading a coalition government seems a much more live possibility.

**WHICH AREAS ARE MOST EXPOSED TO A CORBYN GOVERNMENT?**

- Transport operators
- Infrastructure firms
- Utilities
- Gilts

A pledge to renationalise the UK's utilities and transport system would be bad news for shareholders in these sectors.

More broadly, higher taxes would likely pressure how much you have to invest and there has to be a risk a Labour government would be less generous with the investment tax breaks available through ISAs and SIPPs.

Greater spending could provide a boost for infrastructure firms, depending how contracts were awarded, but could damage public finances particularly when you consider the costs of renationalisation.

Artur Baluszynski, head of research at asset manager Henderson Rowe, says this is not fully appreciated by the market. He adds: 'The market is using the pound as a Brexit risk gauge in the short term, but the risk no one is talking about is the UK gilt market.

'Even if we manage to avoid a no-deal Brexit, but end up with a fiscally irresponsible Labour government which tries to undermine London's status within the global financial system, the UK's credit quality could come under pressure.

'This would mean the UK's ability to run external deficits for an extended time without serious negative consequences could be questioned.'

By **Tom Sieber** Deputy Editor

# Know your fund: what's inside Lindsell Train Global Equity?

Second only to Fundsmith, there's a reason this fund is so popular

When you think of good, dependable investments to buy and forget, a fund from Lindsell Train may spring to mind.

Its most popular one, **Lindsell Train Global Equity (B3NS4D2)**, has generated a return of 347.9% since launch in March 2011, compared to a return of 165.7% from its MSCI World index benchmark.

## LIMITED TURNOVER OF STOCKS

Like a number of its peers in the fund management world, such as Fundsmith, it has what can be considered a low number of holdings in its portfolio with the number of stocks ranging from 20 to 35 on average.

It also has a very low turnover, meaning it doesn't change around the companies it invests in that often, adopting a buy and hold strategy.

This becomes evident in the comments from its monthly factsheet. Most fund factsheets typically list the two, three or four companies the manager has sold that month and the ones they've purchased, with a small paragraph or two explaining why.

But given that Lindsell Train Global Equity is a fund with what's called a 'concentrated portfolio' (this usually refers to a fund holding around less than 30 stocks) and has a low turnover, the manager often goes to town explaining why a new stock has been bought or, more likely, retained.

Lindsell believes in Prada's ability to innovate

Earlier this year, the fund added the Italian luxury goods company Prada to its portfolio, the first new stock it has bought since 2017.

In its monthly factsheet for August, portfolio manager Michael Lindsell got through over 800 words justifying why he took a position in the company.

Covering the company's long and storied history in detail, as well as his hopes for the Prada family's prodigal son Lorenzo, Lindsell explained the investment case and what the fund desires in a business.

## PUSHING PRADA

Believing Prada shares are 'potentially worth two to three times more than today's

| LINDSELL TRAIN GLOBAL EQUITY | |
|---|---|
| 3 YEARS ANNUALISED RETURNS | 20.6% |
| 5 YEARS ANNUALISED RETURNS | 22.1% |

Source: Morningstar, as of 20 Sep 2019

valuation', Lindsell argues that the firm's ability to innovate and drive its premium brand value will appeal to the 'growing aspirational demographic' in the world, where Prada is 'uniquely positioned' with high sales in China and other Asian countries.

That at its core is what the fund is about – investing in good, strong, well-known names which might be out of vogue with the market.

## HOUSEHOLD NAMES

A look at the fund's holdings from its annual report at the end of June reads like a who's who of well-known brands.

Walt Disney, Ebay, Pepsi, PayPal, Heineken and Nintendo all feature, and for the football fans out there, so do Juventus and Celtic, two famous clubs with long histories.

Other names include **Unilever (ULVR)**, **Diageo (DGE)** and Mondelez International the brains behind household brands Marmite, Guinness and Cadbury, respectively.

In the case of Prada, the story centres on the potential for fashion icon Muiccia Prada and her husband Patrizio Bertelli to recapture the brand's 'pioneering zeitgeist' in order to seize the opportunities from an aspirational Asia and once again rise to the throne of the fashion world.

But the fund is not all iconic fashion brands, football clubs and consumer staples.

## BACKING THE LSE

One of its biggest holdings is **London Stock Exchange (LSE)**, the focus of much attention in the finance world at the moment having been the subject of a blockbuster £32bn takeover bid from the Hong Kong stock exchange operator HKEX.


**LINDSELL TRAIN GLOBAL EQUITY TOP 10 HOLDINGS**

| COMPANY | SECTOR | % OF FUND |
|---|---|---|
| Unilever | Consumer goods | 8.3 |
| Diageo | Alcoholic beverages | 7.7 |
| Heineken | Alcoholic beverages | 7.3 |
| London Stock Exchange | Finance | 5.8 |
| Shiseido | Cosmetics | 5.6 |
| Nintendo | Video games | 5.3 |
| Intuit | Business software | 5.0 |
| PepsiCo | Non alcoholic beverages | 5.0 |
| Walt Disney | Entertainment | 4.9 |
| RELX | Publising | 4.9 |

Source: Lindsell Train

The stock has been a strong performer in 2019, rising from £41.24 at the start of the year to around £72.50 now.

London Stock Exchange has long been a Lindsell Train holding, and the fund group is its largest UK-based shareholder.

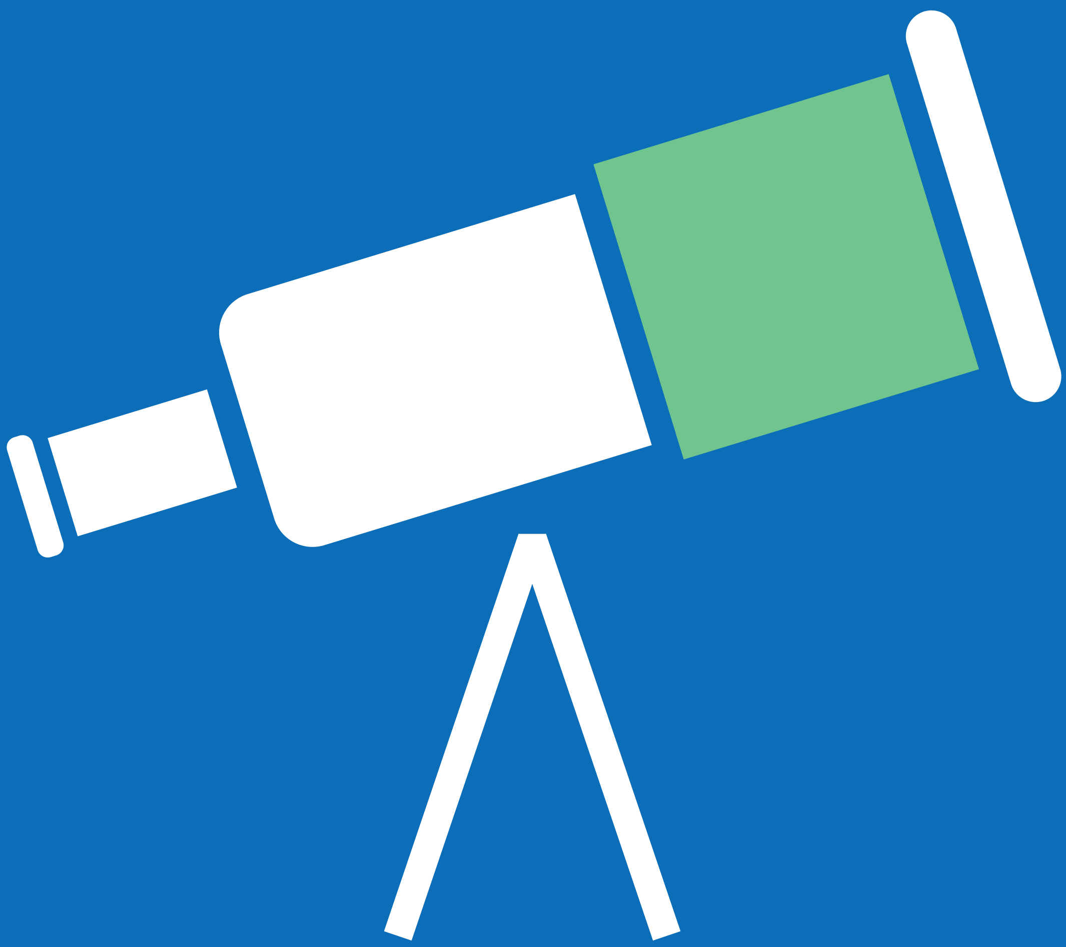
The exchange's strong share price performance has helped drive that of the fund, which over three years has done better than any other global equity fund available in the UK, and over five years is only beaten by **Fundsmith Equity (B41YBW7)**.

Such success comes at a price, and while Lindsell Train Global Equity's ongoing charges figure (effectively its yearly fee) of 1.15% per year isn't the most expensive, it isn't the cheapest either.

But with over £9bn of investors' money poured into it, clearly many out there see it as a fee well worth paying.

**SHARES SAYS:**

**Lindsell Train manager Nick Train recently admitted his funds could embark on a period of poor performance after a strong run in the past decade. But the fund's focus on higher quality, potentially lower risk businesses could see it hold up better than many other funds in a market downturn. We view it as an ideal buy and forget investment.**



# Understanding how the Hong Kong stock market relates to China

We take a look at the different types of Chinese share

China is one of the world's largest economies yet its stock market can be difficult for private investors, and even some professionals, to follow.

There are three main types of Chinese share.

**A-shares:** renminbi-denominated shares in mainland China-based companies whose ownership is restricted to mainland citizens and foreigners under the regulated Qualified Foreign Institutional Investor system.

**B-shares:** quoted in foreign currencies (such as the US dollar) and can be purchased by domestic and foreign investors (with a foreign currency account).

**H-shares:** Hong Kong dollar-denominated shares in Chinese companies which are listed in and trade on the Hong Kong Stock Exchange.

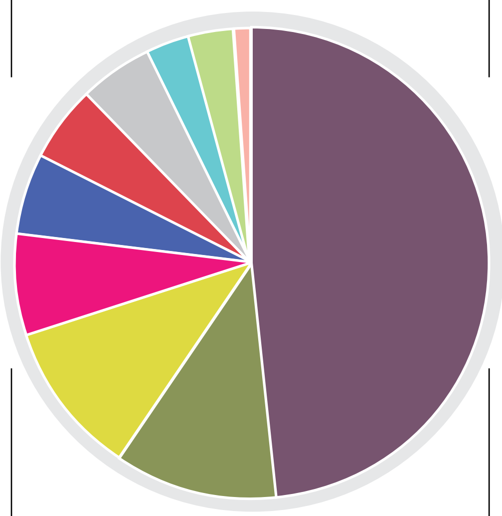
Chinese firms which are listed and trade on the Hong Kong Stock Exchange have typically been the most accessible for overseas investors – although markets in mainland China are slowly beginning to open up to foreign institutions.

Hong Kong has been in the spotlight not just due to simmering tensions and ongoing demonstrations but also in the financial world following the £32bn bid from Hong Kong Exchanges and Clearing for **London Stock Exchange (LSE)**. A move which has been firmly rebuffed.

The main stock index in Hong Kong is the Hang Seng. The unhelpful political situation in the country and the ongoing trade war between China and the US has seen the index really lag global peers so far in 2019 – up just 3.5% against a 9% rise for the FTSE 100, 9.9% gain for the Nikkei 225 and 19.9% advance for the S&P 500.

And a long way behind emerging markets such as Russia up 29% and Brazil's Bovespa index which is up 18%. As of the end of August the index traded on a price-to-earnings ratio of 10.2 times and offered a yield of 3.8%.

**HANG SENG – INDUSTRY WEIGHTINGS**



| | |
|---|---|
| **Financials** | 48.5% |
| **Properties & construction** | 11.1% |
| **IT** | 10.5% |
| **Consumer goods** | 7.0% |
| **Energy** | 5.4% |
| **Telecoms** | 5.3% |
| **Utilities** | 5.0% |
| **Conglomerates** | 3.2% |
| **Consumer services** | 3.1% |
| **Industrials** | 0.9% |

Source: Hang Seng Index, August 2019

# Emerging Markets: Views from the Experts

Three things the Franklin Templeton Emerging Markets Equity team are thinking about today

**1.** August saw US-China trade tensions escalate with several rounds of retaliatory actions following US President Donald Trump's announcement early in the month of new tariffs on Chinese goods. The United States also formally labeled China as a currency manipulator after the Chinese renminbi depreciated to above seven per US dollar for the first time since 2009. These events sparked a broad and deep selloff in Chinese equities as well as global stock markets. However, we believe that China's economy may be better able to absorb the trade issues than the market fears.

**2.** Social unrest in Hong Kong, which entered its third month in August, has been adversely affecting key business areas in the city. A deterioration in the retail, hospitality and real estate sectors as well as a reduction in tourist arrivals has resulted in sharp share price corrections in related companies. Although retailers have been especially impacted, it is important to note that some companies have substantial operations in neighbouring markets such as mainland China, which continue to contribute to earnings. Valuations have also become more attractive with decent dividend yields, which are particularly appealing in an environment of low interest rates.

**3.** The Mexican economy has been buffeted by weaker-than-expected data and bouts of uncertainty. In the second quarter, gross domestic product (GDP) (on a year-on-year basis) contracted for the first time since the 2009 economic crisis. While we expect the volatility in financial markets to continue in the interim amid uncertainty about policies the newly elected administration will pursue, we believe the financials and consumer discretionary sectors remain attractive.

**TEMPLETON EMERGING MARKETS INVESTMENT TRUST (TEMIT)**

**Porfolio Managers**

**Chetan Sehgal**
Singapore

**Andrew Ness**
Edinburgh

TEMIT is the UK's largest and oldest emerging markets investment trust seeking long-term capital appreciation.

BAILLIE GIFFORD

ADVERTORIAL

# PUTTING FUNDAMENTALS FIRST

Lucy Isles, joint-manager of the High Yield Bond Fund, explains how the fund's genesis has resulted in a forward-looking research approach our genesis has resulted in a forward-looking research approach, focusing on fundamentals first. The focus on fundamentals before valuation allows us to achieve the right balance of risk and reward and helps us to avoid costly mistakes. Our approach to high yield has been born out of our roots as a long-term equity house, which is unique within the market.

**The value of an investment in the fund, and any income from it, can fall as well as rise and investors may not get back the amount invested.**

We seek to identify a diverse range of under-appreciated resilient businesses that will adapt to our changing world. We define resilience as comprising three factors – a durable competitive position, good governance and a sustainable approach (synonymous with Environmental, Social & Governance) and an appropriate capital structure. Resilience, however, is not static, so we have developed rigorous monitoring tools to inform position sizing and our sell discipline. We think about risk differently, taking active positions in companies who face very different risk profiles. Knowing our holdings well is our first risk control, diversity is our second. We currently lend to 73 issuers from 15 countries in 18 sectors.

The combination of all these factors allows us to invest for the long term, with a three to five-year investment horizon, resulting in low turnover – a further differentiating characteristic of the fund. We allow time for fundamentals to assert themselves over fluctuating market sentiment and avoid unnecessary trading in what is a costly asset class. In doing so, we believe our investments are better placed to capture the opportunities of today and the future, to deliver long-term income, not short-term yield.

The result is top quartile performance in all timeframes, one, three, five and ten-year and since inception, 18 years ago. We deliver this outperformance by investing in bonds we consider to be resilient and then rigorously monitoring our holdings. This allows us to determine how the businesses are responding to our capricious world, and whether the initially identified resilience remains or we need to consider selling the bonds. We have delivered this top quartile performance with an 18-year track record for some of the lowest, if not the most competitively priced fees in the industry, with total charges for the fund of 0.37 per cent, with no entry or exit fee.


In doing so, we believe we remain true to Baillie Gifford's principal goals - to add value to clients, support companies and benefit society through thoughtful long-term investment.

**ANNUAL PAST PERFORMANCE TO 30 JUNE EACH YEAR (%)**

| | 2015 | 2016 | 2017 | 2018 | 2019 |
|---|---|---|---|---|---|
| Baillie Gifford High Yield Bond Fund (B Inc Shares) | -0.7 | 0.9 | 12.6 | 1.7 | 6.7 |
| Investment Association Sterling High Yield TR | -0.7 | 0.7 | 10.4 | 1.0 | 5.1 |

Past performance is not a guide to future returns

Source: FE. Single pricing basis, total returns. Sterling.
The manager believes this is an appropriate comparison for this fund given the investment policy of the fund and the approach taken by the manager when investing.

# The search for undervalued companies in Europe

TR European Growth's manager believes the market is too pessimistic about Europe's smaller businesses

Investors remain pessimistic over Europe. Outgoing European Central Bank (ECB) president Mario Draghi has just cut the deposit rate to -0.5% (charging banks more to park their money with the ECB) in order to get them to lend while also resuming quantitative easing (QE) to stimulate the economy.

Although sentiment is negative, the positive news for value-oriented portfolio builders is that European stocks look cheap relative to both their own historical levels and global peers.


DFDS is in TR European Growth Trust's portfolio

### UNDER-OWNED & UNDER-RESEARCHED

European smaller companies, in particular, could have significant potential upside. This grouping actually outperformed their larger counterparts over the decade to 31 May 2019 and many pay attractive dividends despite their relatively smaller size.

Currently, they remain under-owned and under-researched, shunned by many analysts, fund managers and investors amid much economic and political uncertainty.

Most investors are huddled in the more expensive quality growth and mature parts of the market but one fund willing to venture down the market cap spectrum and put money to work with more adventurous early cycle companies and turnarounds is **TR European Growth Trust (TRG)**.

### DEEPLY DISCOUNTED RATING

Seeking capital growth by investing in smaller and medium sized companies in Europe (excluding the UK), the fund is managed by Ollie Beckett, assisted by Rory Stokes and Julia Scheufler.

A true small cap focus differentiates the fund from European trust peers, although income seekers should note TR European Growth pays a progressive dividend and bargain hunters may appreciate a steep 13.1% discount to net asset value (NAV) at the current share price of 883p.

TR European Growth Trust's shares have de-rated from a previous premium not too long ago with its small cap value style out of favour with investors.

On a 10-year view, the trust's NAV (total return) has outperformed the benchmark European Euromoney Smaller Companies Index (ex UK) but over the last three and five year periods, performance has disappointed with the trust underperforming the benchmark.

### REASONS TO BE CHEERFUL

Lead manager Beckett believes his carefully assembled portfolio has the potential to re-rate, once value investing swings back into fashion, while investors sheltering in the more expensive parts of the market could be in for future disappointments.

'Weirdly, Europe is the most exposed to global trade,' he explains. 'Trump and (China's) Xi have the punch-up, but Europe feels the pain. The thing that Europe is lacking is fiscal policy.

'But we are likely to see some

may be compelled to sell as investors seek to reinvest funds elsewhere.

The fund is managed by Ollie Beckett

fiscal spending which should stimulate the economy and I don't think it is inevitable we will have recession. And a lot of the cyclical companies, some of which we own, are priced for a recession.'

## SEEKING OPPORTUNITIES

Beckett looks to take advantage of depressed valuations in smaller European companies whose growth potential he believes is underappreciated by the wider market, although he stresses 'we're very much focused on Western Europe' and 'the only things we don't touch are biotechnology or pure (resource) exploration stocks'.

Each year, the TR European Growth Trust team meets hundreds of companies to assess the durability of their business models, quality of management, their growth drivers and catalysts for revaluation.

'We will do lots of valuation screens and lots of management meetings and calls,' explains Beckett, proactive in meeting management teams off-diary. 'If you are someone's only meeting or call of the day, they tend to be a lot more responsive,' he points out.

In terms of differentiation to the peer group, Beckett says 'we will invest in smaller companies than most people, so we get in at an earlier stage, and we will get involved in companies where things have gone slightly wrong and where there is a turnaround and the returns are going to improve.

'We're not necessarily buying the best companies in the world because they tend to be valued accordingly. We're trying to buy undervalued companies where we believe the perception of the market is wrong, something that worked well, until the last 18 months.'

To mitigate stock-specific risk, Beckett runs a very diverse book flush with 143 holdings as at 31 August and the portfolio IS broadly spread by country and industry sector. As opposed to the open-ended fund structure of unit trusts, one key benefit of the closed-ended structure of an investment trust is that the managers don't have to sell good companies in falling markets in order to meet redemptions, where investors ask for their money back.

This means Beckett can be patient, using current pessimism to pick up mispriced companies that have strong structural growth or self-help characteristics, and which his open-ended competitors

## WHAT'S UNDER THE HOOD?

Top 10 positions as at 31 August included Dutch-based wealth manager Van Lanschot Kempen, the German non-prescription drugs company Dermapharm, and Danish ferry and shipping company DFDS, 'the ultimate Brexit stock' according to Beckett, being one of two Dover-Calais ferry operators.

Other holdings include Paris-based Nexans, a maker of cables for construction, telecoms and high-voltage power lines and GTT, the market leader in liquefied natural gas (LNG) container liners. It is growing off the back of the decline of the nuclear industry and China's environmental push involving a switch from coal to gas.

| TOP TEN HOLDINGS (AS AT 31 AUGUST 2019) | |
|---|---|
| Van Lanschot Kempen | 2.3% |
| Nexans | 2.1% |
| DFDS | 2.0% |
| Dermapharm | 1.7% |
| GTT | 1.7% |
| Karnov | 1.7% |
| TKH | 1.6% |
| Banca Farmafactoring | 1.4% |
| Aareal Bank | 1.4% |
| Conzzeta | 1.3% |

Source: Janus Henderson Investors

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

POLAR CAPITAL

# 10 YEARS AFTER THE BANK LOWS – IS IT TIME TO RETURN TO FINANCIALS?

Ten years after banks hit their lows, sentiment towards the sector has once again turned sharply negative. Most bank shares are now at a 40%+ discount to broader equity markets which is significantly larger than their historic levels. This is despite the huge amount of work, led by regulators and legislators over this period, making the banking sector far stronger, more stable and therefore more attractive to investors today. So, is the current pessimism misplaced or still valid?

The crisis led to a concerted effort by governments and regulators worldwide to ensure individual banks were run as financially stronger businesses. Today, however, expectations for interest rates to be cut from their already low levels, against a background of relatively lacklustre economic growth, has resulted in markets expecting a weaker outlook for the sector. Therefore, at best share prices have lagged the underlying equity market, or at worst fallen in absolute terms.

Nevertheless, we believe investors are hugely overestimating the risks. Years of very little loan growth, much tougher regulation and stronger balance sheets all suggest a banking system that is well placed to weather a downturn. The amount of capital a bank is obliged to hold to compensate for the risk of individuals or companies defaulting on loans is now at multi-year highs. Lloyd's Bank, for example, now holds twice as much capital as it did in 2008.

Another change we have seen in the past decade is a huge shift to digital banking, with many commentators talking about the risk the sector suffers in the same way as retailers have thanks to technology-led disruption, in this case from fintech companies. Investors, however, are underestimating the ability of traditional banks to compete in this area, their ability to outspend new entrants and cut costs alongside the fact that the regulatory advantage start-ups are likely to have will be eroded as they grow.

Ten years on, a duller, more boring banking sector is what makes the financial sector overall a much more attractive proposition today. It is made more attractive when coupled with the high level of capital return via dividends and buybacks that they offer. Maybe we will have to go through another downturn for investors to finally believe that risks have reduced, and that any slowdown may well be the catalyst for a recovery in the sector.

As John Maynard Keynes said: "When the facts change, I change my mind. What do you do, sir?"

**Nick Brind and John Yakas**
**Co-Managers, Polar Capital Global Financials Trust**
**September 2019**

# Why are so many CEOs stepping down?

The revolving door of management change is spinning fast in the UK and US

American football may not be everyone's cup of tea but no less a figure than former Manchester United manager Alex Ferguson drew inspiration from a biography of the legendary Green Bay Packers coach Vince Lombardi.

He shaped a small club in Wisconsin into the National Football League's dominant force, winning the first two Super Bowl championship games in the early 1960s, and leaving behind him both a sporting legacy and a rich trove of inspirational quotes.

One gem from Lombardi was 'Winners never quit and quitters never win'. With that in mind, this column is intrigued to see how the number of chief executives (CEOs) leaving their post is running at a relatively high level among the elite ranks of the FTSE 100 in the UK and at record levels in the US.

This is not to say that all of those individuals have just thrown in the towel. But it is intriguing to see changes in the boardroom running at, or above, levels previously only seen during much tougher times for the economies and stock markets of the UK and US.

Should investors therefore be taking the hint that those individuals with perhaps the best insight into their charges' fortunes are bailing out now, while the going could still be seen as good?

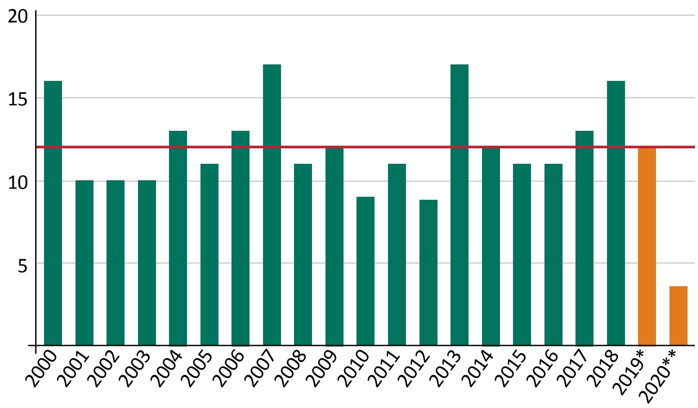
## FTSE'S TWELVE

When **Kingfisher (KGF)** boss Véronique Laury stepped down on 25 September she became the tenth FTSE 100 CEO to do so this year.

Two more changes, at **Royal Bank of Scotland (RBS)** and then **Ferguson (FERG)**, will become effective before the year end and three more bosses are already preparing to step down in 2020, in what **Auto Trader (AUTO)**, **Land Securities (LAND)** and **Centrica (CNA)** are hoping will be smooth transitions.

This year's tally of a dozen CEO changes with three more announced compares to a post-2000 average of 12 changes a year.

**NUMBER OF FTSE 100 CEO CHANGES**




Source: Company accounts. *2019 changes as already happened or due to happen.*2020 changes as already announced in 2019 and planned for 2020.

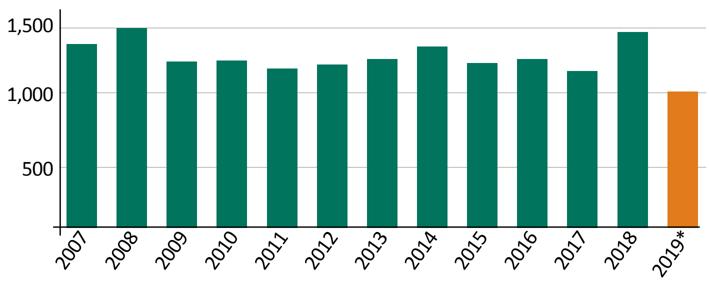
But it is not just in the UK where changes at the top are coming quickly. Research from recruitment specialist Challenger, Gray & Christmas finds that America has just seen the highest number of CEO departures in any individual month in 17 years.

## BOARDROOM SHUFFLE

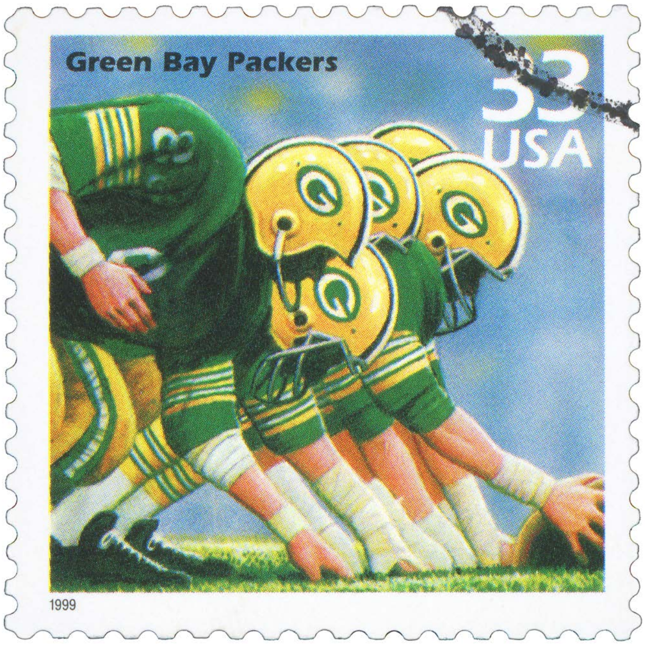
According to the latest monthly data from the Chicago-headquartered firm, 159 US CEOs stepped down in August 2019, a monthly record.

That takes the total number of changes in boss Stateside to 1,009 year-to-date, 15% higher than a year ago and the highest total for the first eight months of the year since Challenger, Gray & Christmas began to keep records in 2002.

**NUMBER OF US CEO DEPARTURES**




Source: Challenger, Gray & Christmas




This puts the US on track to exceed the number of CEO departures seen in 2008, when many bosses took the chance to head for the hills when they could.

The question that investors must now address is whether the pace of CEO change is telling them something about the global economy and corporate profits.

## ALL CHANGE

There are several reasons why a CEO should go, voluntarily or otherwise:

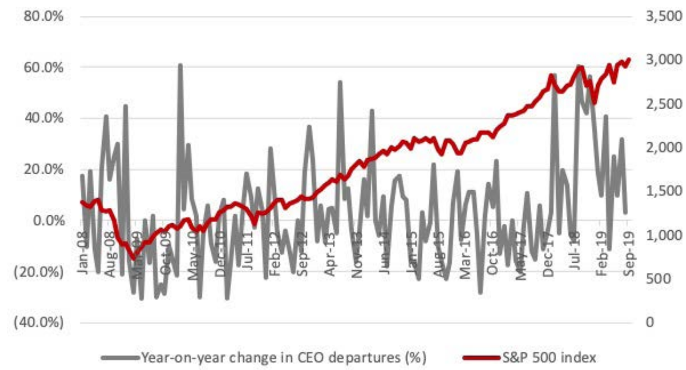
- Share price performance has been poor, something has gone wrong or both and investors or the board felt it was time for a change. The rise of activist investing continues to increase the pressure on CEOs to deliver
- Companies where perhaps investors felt it was time for a change or the executive in question felt ready for a fresh challenge or a break
- There may be instances where the executive feels now is a good time to go, to ensure their legacy looks like a good one

With this latter point in mind, the more cynically-minded may wonder whether some American executives are getting out while the going is still good, and their share options are looking promising, as the benchmark S&P 500 index reaches for the 3,000 mark once more.

After all, the previous peak in CEO changes, according to Challenger, Gray & Christmas' American data, came in 2008, just before the wheels fell off the global economy and stock market alike.


Source: Challenger, Gray & Christmas, Refinitiv

It is possible to counter such dark thoughts. August's US CEO departure rate of 159 is just 3% higher than August 2018 and the rate of growth in changes of leader has slowed markedly over the past 12 months.




Source: Challenger, Gray & Christmas, Refinitiv

It can be argued that economic data is starting to stabilise in the US, after a sticky patch. Bulls will assert that the worst could be over; especially if Washington and Beijing can reach a trade accord and central banks can keep growth going with a fresh round of interest rate cuts. Any drop in the pace of boardroom changes could be seen as a sign of gathering optimism about the future.

By **Russ Mould**
AJ Bell Investment Director

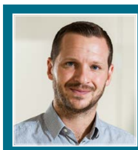
# ‘Should I hold off from taking the state pension for a year?’

Deferring can boost future payments but it takes a long time to make up for 12 months of lost income

*I understand that you can defer taking the state pension and wondered whether or not it would be financially sensible to do so. I’m 60 now so due to receive my state pension at age 66 (assuming the Government doesn’t move the goalposts again).*

*What exactly are the rules and how likely is it that deferring will eventually pay off?*

***Bridget***



**Tom Selby**
AJ Bell
Senior Analyst says:

If you decide to take your state pension later than your state pension age, you’ll receive a higher weekly amount in return. Your annual state pension payment will increase for every week you defer, provided you defer for a minimum of nine weeks.

For those who reached state pension age before 6 April 2016, the Government offers a particularly generous 10.4% uplift for every year you delay taking the benefit. However, for those who reach state pension age after 6 April 2016 the rate has been cut substantially to 5.8%.

Given the vast majority of

people deferring will now be caught by the 5.8% rate, it is this I will focus on here.

If someone is entitled to the full flat-rate state pension of £168.60 a week, deferring one year will mean that at age 67 they receive a weekly payment of £178.38.

At the moment annual state pension payments are also protected by the ‘triple-lock’, meaning they rise in line with the highest of average earnings, inflation or 2.5%.

So at what point would you ‘break even’ in monetary terms if you put off taking your state pension for a year? When you plug the numbers in (I’ve assumed the state pension increases by 2.5% a year in both cases), it suggests you’ll have to wait until around your 89th birthday for the higher annual payments to make up for the year of income you missed out on.

Whether it makes financial sense to delay getting your state pension will depend on your personal circumstances and, in particular, life expectancy.

This will be affected to a large degree by your health and lifestyle choices. So if, for example, you are a heavy smoker or have a life limiting illness such as diabetes or cancer, the chances of you living long enough to earn back the deferred year of state pension might be relatively slim.

If you are in good health, on the other hand, there is a better chance deferring your state pension will eventually pay off.

## 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.

# Self-employed pension saving: is it worth it?

We examine how those who work for themselves might plan for retirement

The UK is in recovery mode from a looming retirement crisis. Automatic enrolment has been introduced for those in employment, nudging millions to save for their future for the first time.

But if you're one of the near-5m self-employed people living and working in the UK, you'll need to take responsibility yourself.

According to the Office for National Statistics, just 14% of self-employed people are saving into a pension. That means around six out of seven risk facing a serious income shortfall when they want to stop working unless they take action.

The flexibility and choice pensions offer means they are increasingly attractive to all – including those who work for themselves. Furthermore, there are various features that could be particularly appealing to the self-employed.

## TAX RELIEF BOOST

One of the biggest benefits of making personal savings in a pension (e.g. a SIPP) is the bonus added through tax relief.

Tax relief at 20% is automatically added, while higher (40%) or additional (45%) rate taxpayers can claim up to an extra 20% or 25% through their tax return.

The accompanying table shows you how much saving £100 in a SIPP will cost.

## PAYING YOUR PROFITS INTO A PENSION

If you are a business owner, you might consider paying directly from your business into your pension.

Pension contributions are business expenses, so your company would get corporation tax relief of 19%. If you chose to make a payment to your pension rather than take profits as dividends then you also save on income tax.

Note this option isn't available if you're a sole trader, although you can still make personal pension contributions.

## PENSIONS 'CARRY FORWARD'

There is another way the self-

| THE COST OF SAVING £100 IN A SIPP | | | |
|---|---|---|---|
| Tax bracket | Upfront cost of £100 in a SIPP | Extra relief claimed through tax return | Effective cost of £100 in a SIPP |
| Basic-rate taxpayer | £80 | £0 | £80 |
| Higher-rate taxpayer | £80 | £20 | £60 |
| Additional-rate taxpayer | £80 | £25 | £55 |

Source: AJ Bell

employed and business owners could further boost their pension fund.

Carry forward is particularly useful for anyone who has set up a pension but hasn't been able to use up their available allowance. This is often the case for people who may need to prioritise investing in their business in the short-term over saving for the future.

Carry forward is essentially a flexibility which allows you to make up for lost time. Provided you were a member of a pension scheme at the time, you are allowed to utilise up to three years of unused annual allowances in the current tax year.

That means you could benefit from an annual allowance of up to £160,000 using carry forward, including tax relief.

## FLEXIBILITY AT AGE 55

Historically a major drawback of pensions for self-employed people was the perceived lack of flexibility.

The old 'locked-box' structure

– where most people ended up buying an annuity at age 65 – might not have fit into their plans.

Savers can now choose how to spend their retirement funds from age 55 (or age 57 from 2028). There are three main options:

- **Drawdown**: take up to 25% of your fund tax-free, with the rest taxed in the same way as income when you take it out. Your fund will stay invested and you'll need to think about a range of things including how much risk you want to take and how much income you can safely withdraw;
- **Ad-hoc pension lumps sums:** take individual chunks out of your pension with 25% of each chunk tax-free and the rest taxed in the same way as income;
- **Annuity:** hand your pension pot to an insurer and receive a guaranteed income stream in return. These can be over a fixed-term or for life, and you can add things like pensions for your spouse and inflation protection (although this will lower your starting income).

For many people a combination of these income routes will provide the right retirement solution.

And while pensions are first and foremost designed to provide an income in retirement, ultimately it's your money and you can use it how you want.

### CASE STUDY

EMMA SET UP a small bakery in her hometown four years ago. She now employs two people, is a higher-rate taxpayer and in the 2019/20 tax year expects to turn a profit of £20,000.

After corporation tax of 19%, Emma could take a dividend of up to £16,200.

Emma would then receive the first £2,000 of the dividend (the 2019/20 dividend allowance), and the remainder would be subject to income tax at 32.5%, meaning a total of £11,585 in her pocket.

However, if her business paid the entire £20,000 directly into a pension, no corporation or dividend tax would be payable. The money will also be able to grow tax-free, with tax only coming into play when she comes to make a withdrawal from her pension.

By **Tom Selby**
AJ Bell Senior Analyst

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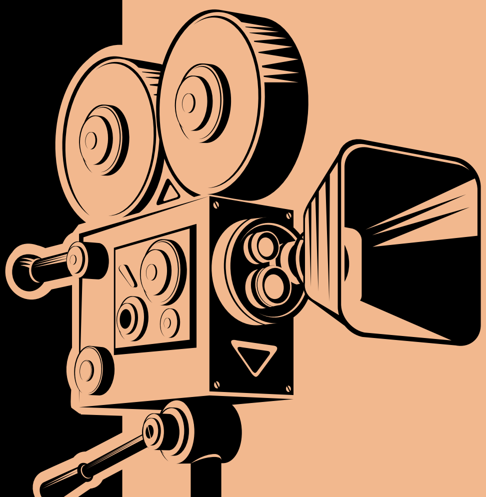
**Cathal Friel, CEO**
**Open Orphan (ORPH)**

Cathal outlines the investment case for Open Orphan and its future plans.


**Michael Hunt, CFO**
**ReNeuron Group (RENE)**

Michael explains this clinical stage stem cell company and the allergenic treatments it produces.



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## SHARES SPOTLIGHT

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www.sharesmagazine.co.uk/videos

# Six fascinating things you didn't know about Morrisons, AO, Laura Ashley and more

London-listed companies are full of surprises such as online firms owning physical stores and retailers having hotels

Investors typically get to know companies well if they follow their story through trading updates and financial results. That doesn't always give you the full picture.

Several quoted businesses have unusual assets which aren't front and centre of the investment case. There is often logic behind these quirky assets and you may be interested to read about a few examples.

We've spotted a number of companies that fit the bill and would love to hear from readers who can offer any more examples – please email editorial@sharesmagazine.co.uk with your insights.

### MORRISONS' ABATTOIRS

If you've ever wondered where sausages come from and how they get onto the supermarket shelf, then it might surprise you to learn that Bradford-based supermarket chain **WM Morrison Supermarkets (MRW)** is the only large UK retailer to have its own abattoir.

At age 17, Jack Woodhead found himself in charge of a butchers shop near Bradford when his father fell ill. He then built up a business which supplied Ken Morrison's first supermarket and subsequently becoming one of Britain's biggest meat suppliers.

Gear4music's showroom

In 1991 the business became a subsidiary of Morrisons and its first vertically integrated supplier. Today the company slaughters over 200,000 cattle a year, more than 700,000 lambs and well over one million pigs at its three abattoirs.

Not only does this provide a cost advantage to the company, it also provides provenance and total control over the supply chain, ensuring high quality standards.

### ONLINE RETAILERS WITH PHYSICAL STORES

Investors may presume that companies classified as online retailers only operate via the internet. There are two examples where this is not the case.

**Gear4music (G4M:AIM)** sells musical instruments and music equipment via its website. Yet this is not pure-play online business. It also operates from brick and mortar showrooms in York (where it is headquartered), Sweden and Germany.

Physical showrooms are a contractual requirement of the vast majority of the industry's suppliers. Besides its own-brand instruments, Gear4music sells premium third-party brands such as Fender, Yamaha and Roland.

Gear4music's European showrooms are required to open up buying opportunities in Europe. Yet it is important to stress that the company's York showroom also makes a healthy positive contribution to the profit and loss account.

Physical showrooms are also a good way for Gear4music's staff to touch, feel and play around with some of the products whose benefits they are expected to extol to customers and they are also useful for training and tech support sessions.

Showrooms are also an invaluable method of gathering 'offline' customer feedback, particularly from regular customers, while presentation of instruments and equipment to a high standard builds further credibility with brands and suppliers.

## AO'S CLAIM TO FAME

The second online company with a surprise physical shop is electrical retailer **AO World (AO.)**.

It joined the stock market in 2014 with fanfare aplenty, outlining a bold ambition to disrupt the UK white goods market with a key focus on customer service. In addition to its core online business is something called 'AO Outlet', a brick and mortar shop located in Telford.

The strategic rationale behind running a physical store is rather compelling, because AO Outlet is actually attached to AO World's enormous recycling facility – in fact this is the biggest fridge recycling plant in the country. The Telford store sells professionally refurbished and end-of-line goods direct to the public.


Hotel Chocolat's hotel in St Lucia

## TIME FOR A CUPPA

Quintessential British fashion brand **Laura Ashley (ALY)** is going through a bit of a rough patch, with its home furnishings in particular going out of vogue with customers.

But one area where it does see potential is in hospitality. Despite few people knowing that Laura Ashley is involved in this sector, the company actually has nine licensed tea rooms and two licensed Laura Ashley hotels in the UK, and plans to expand this further.

Situated typically in bourgeois hotels and the like, Laura Ashley believes its tea room concept can take off and become a key part of total group revenue going forward. It also plans to expand this concept internationally.

Also embracing the hospitality sector is **Hotel Chocolat (HOTC:AIM)**, a chocolate seller who lives up to its name by having a hotel, based in the Caribbean.

The only bean-to-bar chocolate manufacturer in the UK, Hotel Chocolat has its own cocoa plantation on the Rabot Estate in St Lucia. And given its idyllic surroundings, the company sought an opportunity to live up to its name and build a real hotel on site, named Boucan.

The firm doesn't talk about the hotel in its financial results, but in documents accompanying its admission to the stock market in 2016 Hotel Chocolat said the hotel – which has 14 rooms, a spa and a luxury restaurant – made $2.5m sales and $400,000 earnings before interest, tax, depreciation and amortisation (EBITDA) in its 2015 financial year, with 80% room occupancy.

## TRAVIS PERKINS: A FASHION ICON?

Did you know builders' merchant **Travis Perkins (TPK)** used to have a workwear fashion brand up until 2018? It sold clothes under the Scruffs brand, principally to tradesmen. Scruffs sat under the Birchwood Tools subsidiary which was offloaded to rival firm Toolstream last year.

Workwear clothes now have mainstream appeal thanks, in part, to the popularity of US brands Carhartt and Dickies. Skateboarders and musicians are among the big fans of these clothes which tend to last longer than your average outdoor apparel.

By **Daniel Coatsworth, Yoosof Farah, Martin Gamble and James Crux**

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## KEY ANNOUNCEMENTS OVER THE NEXT WEEK

### Full year results

**27 September:** Byotrol, CVS. **30 September:** Grit Real Estate Income. **1 October:** Ferguson, James Halstead, Revolution Bars, SCS Group. **2 October:** Ceres Power, Kin & Carta. **3 October:** Genedrive

### Half year results

**27 September:** ADES International. **30 September:** Bidstack, Creo Medical Group, President Energy. **2 October:** Inspiration Healthcare, Tesco. **3 October:** Arcontech, Ted Baker.

### Trading statements

**27 September:** Pennon. **1 October:** Greggs. **2 October:** Topps Tiles. **3 October:** CMC Markets, Moneysupermarket.com, Photo-Me International.


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**THIS WEEK: 14 PAGES OF BONUS CONTENT**

**PLEXUS**
**TRINITY EXPLORATION**
**UNION JACK OIL**

# SHARES SPOTLIGHT

## *Mining, oil and gas*

**INCLUDES COMPANY PROFILES, COMMENT AND ANALYSIS**

ISSN 2632-5748

SEPTEMBER 2019

# Introduction

Welcome to *Spotlight*, a bonus magazine which is distributed eight times a year alongside your digital copy of *Shares*.

It provides small caps with a platform to tell their stories in their own words and this edition is dedicated to the natural resources space.

The company profiles are written by the businesses themselves rather than by *Shares* journalists.

They pay a fee to get their message across to both existing shareholders and prospective investors.

These profiles are paid-for promotions and are not independent comment. As such, they cannot be considered unbiased. Equally, you are getting the inside track from the people who should best know the company and its strategy.

Some of the firms profiled in *Spotlight* will appear at our investor evenings in London and other cities where you get to hear from management first hand.

Click here for details of upcoming events and how to register for free tickets.

Previous issues of Spotlight are available on our website.

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# Snapshot of the energy and metals markets

The most heavily traded commodity by volume worldwide is crude oil and derivatives such as heating oil and gasoline. These products are traded on the New York Mercantile Exchange (NYMEX), ICE Futures, the Dubai Mercantile Exchange (DME) and the Central Japan Commodity Exchange (C-COM).

Oil, like most commodities, is traded in futures contracts. The purchase or sale of a barrel of oil will be agreed at a fixed price for delivery on a specified date. These will typically be set one month, three months or six months out.

**LOOK TO THE FUTURES**

The futures market allows the buying and selling of commodities without taking physical delivery of them. Only a tiny fraction of contracts are settled by delivery. The price quoted for immediate delivery is known as the spot price.

The crude oil market has two main benchmarks: West Texas Intermediate (WTI) and Brent. US oil is largely priced off WTI and Brent is used in Europe and Asia.

While the world's thirst for oil increases, its supply of conventional crude is diminishing. However, the increasing exploitation of oil found in shale rock in the US has opened up a significant new source of supply.

Geopolitical issues can have a significant influence on the oil price. The Organisation of the Petroleum Exporting Countries (OPEC) produces around 40% of the world's oil and this gives the 12-member cartel a degree of control over the future direction of prices.

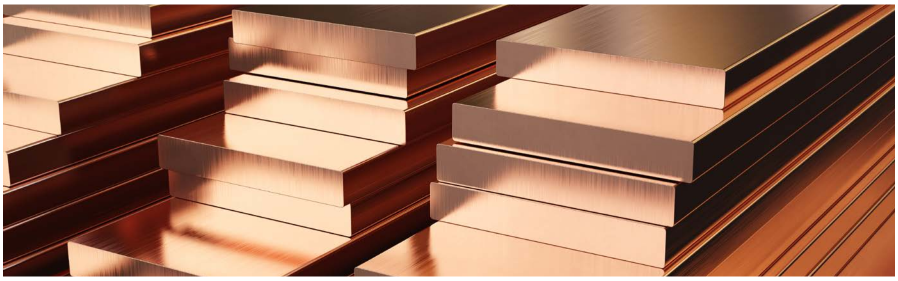
**ENGINE OF GROWTH**

Oil is one of the key engines of economic growth and prices are closely linked to the fortunes of the global economy – so it is particularly prone to volatility.

The natural gas market has traditionally been closely associated with oil although in the last decade the link between the two, at least in terms of pricing, has broken down.

This resulted, in part, from the increased exploitation of unconventional sources of gas in the US, which opened up a new source of supply and put significant pressure on prices, in particular the main North American pricing benchmark Henry Hub.

The development of liquefied natural gas (LNG)




has also made it easier to transport gas and made an increasing number of gas developments commercially viable.

**FUTURE OF COAL**

Coal, the fossil fuel which facilitated the industrial revolution, remains an important contributor to the global energy mix. Despite significant environmental concerns, around 40% of the world's electricity is generated by burning thermal coal. Asia is by far the biggest market and accounts for more than 60% of global consumption. Unlike oil the future supply of coal is not a pressing issue with enough to meet current demand for several more centuries.

Uranium, used to produce nuclear power, is also relatively abundant with a study from the International Atomic Energy Agency and Nuclear Energy Agency suggesting there is enough of the commodity to meet projected demand for at least the next 130 years.

**ON YOUR METAL**

The main industrial metals are aluminium, copper, lead, nickel, tin and zinc. They are traded on a number of global exchanges but the benchmark contracts are on the London Metal Exchange (LME).

Copper's reputation as a barometer of the health of the global economy has earned it the nickname 'Dr Copper'. The red metal is used in a broad variety of different industries and products including electronics, homes and infrastructure.

Precious metals are, by definition, scarce and have a high economic value by volume. The platinum group metals (PGM) – platinum, palladium, iridium and rhodium – are used by industrial customers. Their main use is in the construction of emissions limiting technology in cars. Silver is used by electronics manufacturers and in some medical formats such as wound dressings but, like gold, a significant proportion of output is used in the manufacture of jewellery.

**EVERYTHING THAT GLITTERS**

Gold has limited applications in industry. It tends to be in demand during periods of economic or geopolitical strife, when inflation threatens paper currencies or there are significant falls in bond and equity markets.

Its status as a 'safe haven' asset is based on its historic role as a store of value and the fact that, unlike currencies, its value cannot be manipulated through adjustments to interest rates.

PLEXUS
safer performance | faster service | reduced costs

# Plexus transforming wellhead technology

## Website: www.plexusplc.com

Admitted to AIM in 2005, **Plexus (POS:AIM)** is an established oil and gas engineering company with a blue-chip customer base that has collectively deployed its patented POS-GRIP friction grip method of engineering wellheads on hundreds of wells worldwide.

Now well into its second decade as a publicly traded company, Plexus emerged from the 2015/16 industry downturn leaner and fitter – unlike many service companies who were forced to close or merge.

Management believe the Aberdeen-based engineering company is now ideally placed to establish its wellhead equipment as a superior standard for the oil and gas sector, one which raises performance, reliability and safety standards across the industry, whilst importantly generating value for shareholders.

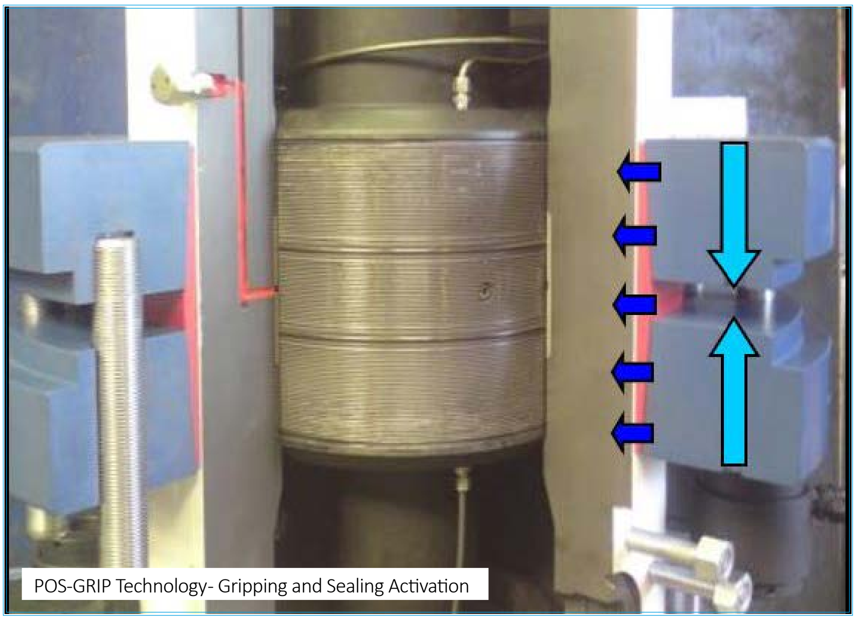
### GAME-CHANGING TECHNOLOGY

Such a goal is testament to the game-changing benefits Plexus' proprietary technology offers, including true and verifiable metal-to-metal leak proof annular seals, enhanced safety and operational features, and material time and cost savings due to lower or zero throughout field life maintenance and remedial spend.

POS-GRIP's simplicity lies behind its superiority over conventional technologies which typically comprise of many more individual components, each of which has the potential to compromise seal integrity and are vulnerable to fretting/ movement as wells cycle through temperature and pressure variations.

POS-GRIP involves applying an external force to squeeze the housing until it engages an end connection (casing or tubing hanger in wellheads), to generate a gripping force. This eliminates assembly tolerances and eventually merges the two members with such force that the parts effectively become one, delivering a lifetime leak proof metal seal solution.

**INTRODUCING PLEXUS**
**A SMALL CAP OIL SERVICES COMPANY WITH A PROPRIETARY WELLHEAD TECHNOLOGY**


POS-GRIP Technology- Gripping and Sealing Activation


A POS-GRIP HG Wellhead System Installed Offshore

The process is accurately controlled by hydraulic pressure and occurs within the elastic limits of the material, so that the connection is reversible which has many advantages including facilitating side tracking and delivering further savings on decommissioning.

POS-GRIP's simple design has significantly raised wellhead standards for HP/HT and standard pressure operations.

Having developed what management believes is the only true long-term wellhead metal seal which can be tested and qualified as a system to mirror true field life conditions, rather than component testing, Plexus was confronted with a problem often faced by companies with disruptive technologies – how to make inroads into a major market dominated by a handful of long-established dominant players with deep pockets?

## ESTABLISHING A RENTAL BUSINESS

Plexus' initial answer was to take its product directly to the niche jack-up exploration market sector by establishing a rental wellhead business to showcase and prove its technology out in the field. It did more than that as it expanded the reputation of Plexus' equipment from beyond the UK Continental Shelf to the European Continental Shelf, and then globally.

In addition to becoming a profitable, dividend-paying business, by 2016 Plexus had become the dominant supplier of wellheads for HP/HT jack-up exploration operations in the North Sea and, as a testament to its technical capabilities, was selected by Total for its Solaris well in what is believed to be the highest pressure well ever drilled and tested in the region.

Having achieved what it had been set up to do, and set against a backdrop of depressed 2015/16 levels of global exploration drilling activity, Plexus took the strategic decision to sell its jack-up exploration business and rental wellhead inventory to TechnipFMC in February 2018. The sale was structured so that Plexus retained the jack-up exploration application rights for Russia and the CIS through its licensee Gusar.

Furthermore, Plexus and TechnipFMC entered into an R&D IP Collaboration Agreement with the objective of finding new and revolutionary ways in which to challenge convention and apply alternative technologies to make petroleum equipment safer and more efficient.

## A STRATEGIC SHIFT

This transaction heralded a strategic shift for Plexus. Without the distractions of running a wellhead rental inventory business, the sale freed up management's resources, significantly strengthened the cash-rich balance sheet and reduced the company's cost base, enabling Plexus to embark on the next stage of its development: breaking into more lucrative and sizeable markets, namely surface production (land and offshore) and subsea exploration and production.

Plexus has moved quickly, establishing a joint venture, Plexus Pressure Control Ltd, with UK-based BEL Valves Limited to offer operators a turnkey solution so that it can compete on a level playing field with top tier suppliers.

Thanks to the JV, in which Plexus owns a majority shareholding, Plexus can now supply operators with highly qualified surface xmas trees and valves, alongside its own POS-GRIP production wellhead systems, and as a result is now well-placed to go for multiple surface production projects where wellheads are typically purchased as part of a package of equipment.

The timing of the JV could not be better when one considers the column inches in the press occupied by methane leaks and the significant damage they cause to the environment. Methane, the principal component of natural gas, has a global warming potential of up to 86 times greater than carbon dioxide over a 20-year period.

Preventing methane leaks is therefore crucial especially as according to recent studies, gas leaks from the wellhead to the consumer are far higher than had previously been thought. Indeed, methane leaks from gas infrastructure have the potential to reverse the perceived environmental benefits of natural gas compared to coal derived energy should only circa 3% of gas produced escape as emissions.

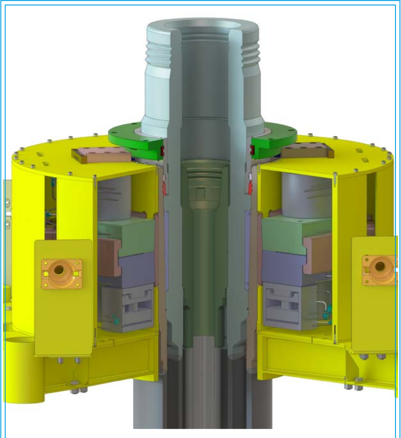
## FOCUS ON LEAKS

With many operators actively favouring and gravitating towards natural gas over other dirtier forms of hydrocarbons such as coal and crude oil, the energy industry, regulators and lobbyists are taking methane leaks seriously and have launched a range of initiatives. Shell has pledged to limit methane emissions to less than 0.2% of the total volume of natural gas it extracts.

**BP (BP.)**, Eni, ExxonMobil, Repsol, **Royal Dutch Shell (RDSB)**, Statoil, Total and Wintershall have agreed to reduce methane emissions under the Guiding Principles, a collaboration between organisations, including the International Energy Agency and the United Nations.

A number of the world's largest oil and gas companies have formed and funded an organisation called the Oil and Gas Climate Initiative (OGCI). The Independent Energy Standards Corporation's TrustWell Responsible Gas Program has been launched to help buyers source gas responsibly by rating wells according to risks and impacts, including methane leaks. A study recently published in Environmental Geosciences profiles wells based on how likely they are to leak methane.

Leak proof technologies are



Python subsea wellhead up to 20 Ksi

essential for helping efforts to tackle methane leaks, and the industry is actively seeking such solutions.

## A TECHNOLOGICAL SOLUTION

Plexus' POS-GRIP wellhead and HG metal sealing system, which delivers a leak proof solution at the wellhead end of the supply chain, is one such technology.

Combine this capability with the potential to deliver major cost savings over the lifetime of the well by negating the need for remedial maintenance, and management believes POS-GRIP is a must-have technology that meets operational and environmental needs.

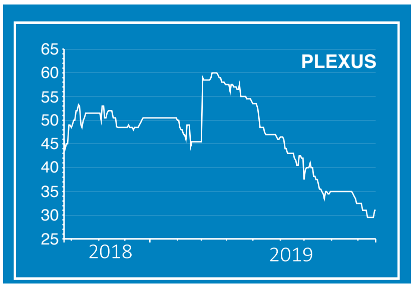
The benefits offered by POS-GRIP are not confined to jack-up exploration and production wellheads. Wherever metal to metal sealing is required or advantageous, management believes POS-GRIP can raise performance, reliability and safety standards.

Connectors are a good example as POS-GRIP is ideal for high integrity, low fatigue applications, and connectors for wellheads, risers, subsea jumpers, pipelines, and even vessel mooring can all benefit from the simplicity of POS-GRIP. The Company already has a suite of POS-GRIP products including subsea exploration and production wellheads, as well as abandonment solutions for the fast-growing decommissioning market.

Management's aim is to capitalise on the superior design and economics of POS-GRIP and build a portfolio of Plexus products, each capable of generating its own separate revenue stream.

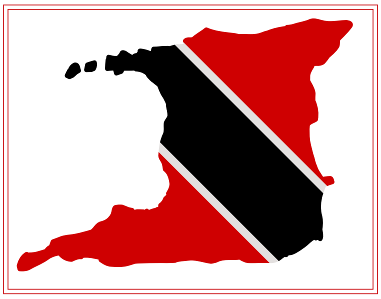
Currently, revenue is generated from the three year earn-out agreement with TechnipFMC for the jack-up exploration business outside the Russian and CIS markets; from the licensing agreement with Russian partner, Gusar, which recently won a first jack-up exploration wellhead contract with Gazprom; and from organic contracts for products outside jack-up exploration, including production and abandonment.

Following Gusar's breakthrough Gazprom order, the Plexus Pressure Control Ltd JV, and with work underway to develop new products for new markets, management expects a major step-up in revenues in the next two-to-three years. At this point, Plexus would have been transformed into a highly profitable, global supplier of its proprietary POS-GRIP equipment, capable of generating significant returns for investors.



# Trinity Exploration & Production is reborn

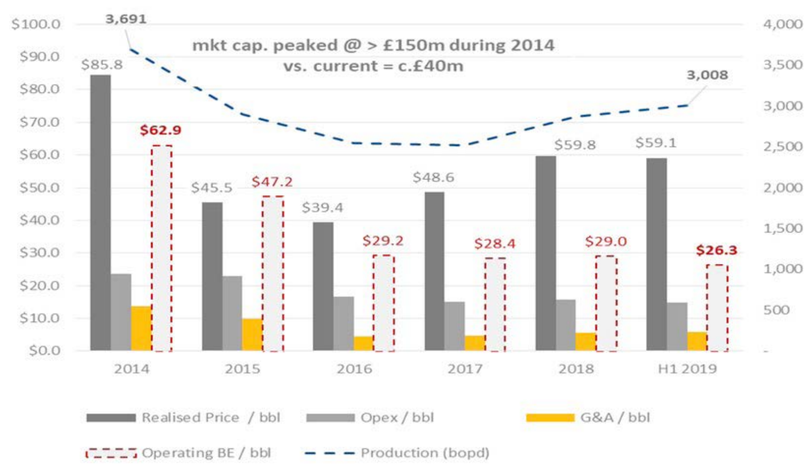
## Website: www.trinityexploration.com



AIM-quoted **Trinity Exploration & Production (TRIN:AIM)** is a pure play Trinidad focused small cap E&P company which operates a portfolio of producing, development and exploration assets both onshore and offshore in the shallow waters off the west and east coasts of Trinidad.

It is a local oil producer of scale, supplying circa 5% of Trinidad's total black oil production. It has operated in Trinidad since 2010 but a new management team was put in place in 2015.

A TRANSFORMED BUSINESS: EVOLUTION OF OPERATIONAL PERFORMANCE




### THE ASSETS

Trinity operates nine licences onshore and offshore Trinidad with 2018 2P (proved and probable) reserves of 24.5 million barrels (mmbbls), 2C resources of 18.8 mmbbls, and production of c.3,000 barrels of oil per day (bopd).

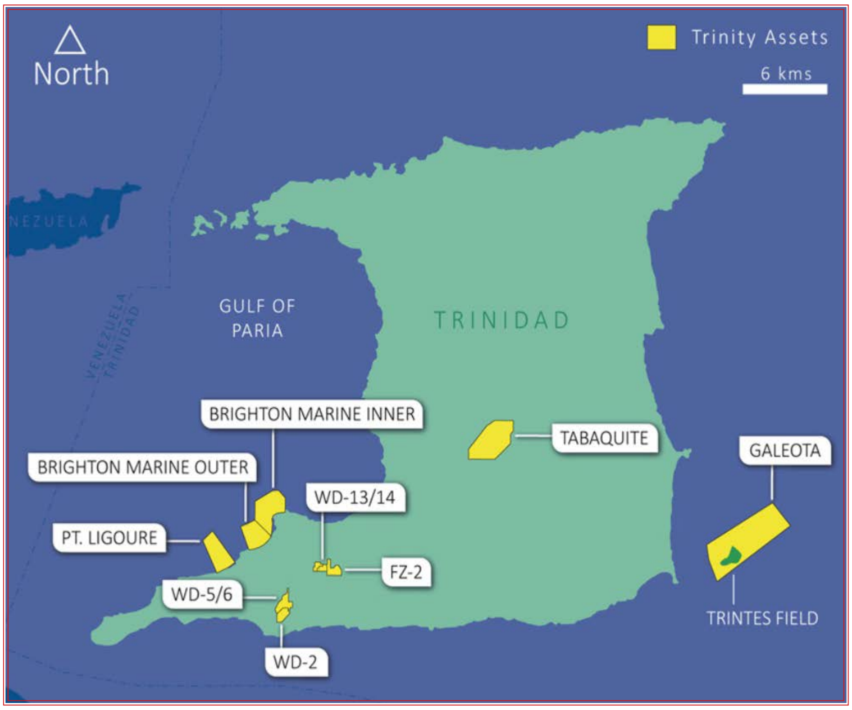
The short-term focus is on leveraging production and cash flow via an onshore development programme (drilling up to eight new wells per year) with a medium term opportunity to deliver the first phase of the Galeota development (of the TGAL discovery, offshore East Coast) which has the potential to deliver standalone peak production rates in the range of 5,000 to 6,000 bopd

**INTRODUCING... TRINITY EXPLORATION & PRODUCTION**

**A PURE PLAY TRINIDAD FOCUSED SMALL CAP E&P COMPANY**

### WHAT'S NEW: H1 2019 KEY DEVELOPMENTS

The company maintained production with no new drilling and benefited from reduced costs and increased margins, which meant that key performance metrics moved in the right direction – with adjusted earnings before interest, tax, depreciation and amortisation (EBITDA) increasing 20% to $11.2m for the first six months, a margin of 35%, and its operating break-even falling further to $26.3 per barrel. The cash plus working capital




surplus almost doubled to $22m which comprised cash balances of almost $18m and a working capital surplus of over $4m.

Such high operating margins and low operating break-even ensures financial resilience and cushions Trinity from downside risk should there be unfavourable moves in the oil price.

During H1, Trinity was busy high grading drilling locations for its recently recommenced drilling programme and production has already commenced from the first new infill well of the H2 campaign with production from the second well expected imminently. This second well is Trinity's first High Angle Well (HAW).

The third well of the campaign has spudded and should be completed mid-September.

## THE FUTURE

The drilling programme is designed to enable the company to generate sustainable and significant free cash flow in the coming years. Trinity's strategy and approach to operations is focused on maintaining a low operating break-even, reducing operating costs per barrel via increased production (preserving base production and increasing individual well production rates) and leveraging economies of scale, new technology applications and well optimisations.

## DOING THINGS DIFFERENTLY

Trinity has recently drilled its first HAW onshore, which has intersected net oil sands 1.5 times the thickness of those expected had it been drilled as a conventional vertical well on that particular target.

Drilling went to plan on timings and costs and is the first of a series of HAWs that it expects to drill and complete in the near term. Although not commonly deployed onshore in Trinidad, HAWs are now the industry standard in many basins around the world and have been modelled by the company to yield initial production rates and reserves of more than two times those achieved from conventional vertical wells.

Trinity is very focused on maximising production rates and is continually exploring new technologies to help drive value. It recently entered a partnership with Weatherford International as part of an overall Supervisory Control and Data Acquisition (SCADA) approach to production optimisation. This is the first time technology of this kind has been deployed in the onshore oil producing acreage of Trinidad and they believe that it will enable the company to further reduce operating costs and increase reserves and production.

## WHY INVEST NOW

Brokers currently suggest almost 200% upside upside with a consensus 36.5p target price. Having paid down all of its convertible loan notes and its outstanding debt liabilities, while increasing production Trinity is currently trading at £0.9/2P and £0.5/2P+2C, significantly below its Latin America focused peer group.

The company has robust operating margins, is highly cash generative and is progressing its fully funded onshore drilling programme. Continued onshore growth with significant offshore upside suggest strong equity growth potential for the Trinidad based producer.

# Union Jack flies the flag for UK onshore oil and gas

## Website: www.unionjackoil.com

The directors of **Union Jack Oil (UJO: AIM)** see the United Kingdom onshore as being an attractive target for investment in hydrocarbon ventures, considering the relatively low-cost operating environment and a fully transparent licencing regime.

The company has adopted a business model, typically acquiring interests in late stage projects, minimising risk and offering exposure to wells with the scope to dramatically change the dynamics with the drill bit, West Newton, Biscathorpe and Wressle being prime examples.

Union Jack holds what the board considers to be high-value material project interests with significant upside potential in their axis areas of operations in the East Midlands, Humber Basin and East Yorkshire. This interest is believed to be able to assist in delivering material growth in the medium term and build a sustainable mid-tier UK onshore focused conventional hydrocarbon producer.

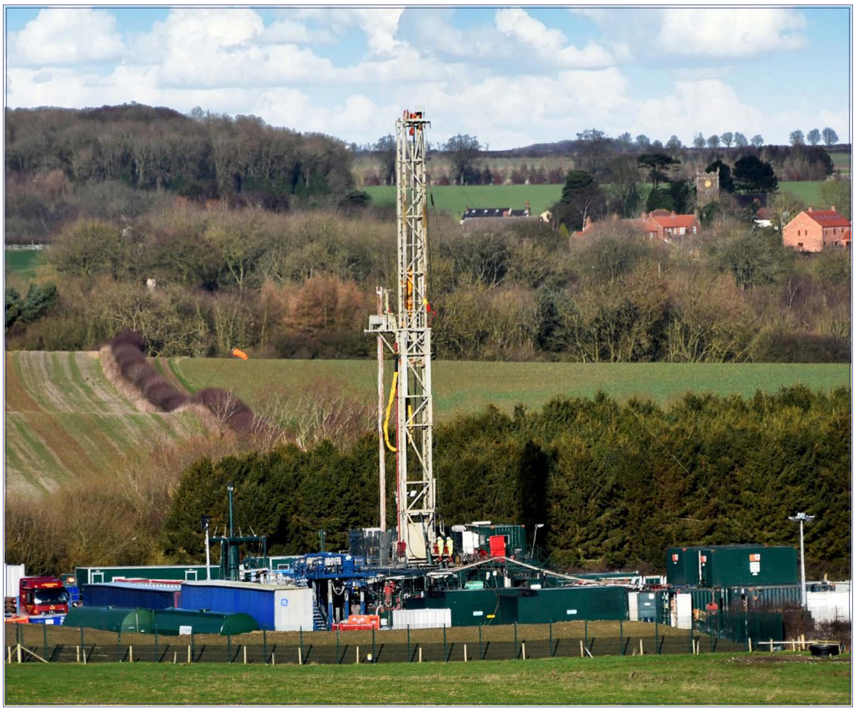
### ASSET OVERVIEW

The company has acquired interests in numerous licences all being located within established hydrocarbon producing provinces.

- **PEDL183** West Newton gas and oil discoveries 16.665% interest
- **PEDL253** Biscathorpe 22% interest
- **PEDL180** and **PEDL182** Wressle and Broughton North 27.5% interest
- **PEDL005(R)** Keddington oilfield 20% interest
- **EXL294** Fiskerton Airfield oilfield 20% interest
- **PEDL241** North Kelsey 20% interest
- **PEDL201** Widmerpool Gulf 26.25% interest
- **PEDL181** Humber Basin 12.5% interest
- **PEDL209** Laughton 10% interest
- **PEDL118** Dukes Wood 16.67% interest
- **PEDL203** Kirklington 16.67% interest

INTRODUCING ... UNION JACK OIL

A UK ONSHORE OIL AND GAS PLAY



### PEDL183 WEST NEWTON A1 AND A2 DISCOVERIES

During late 2018, Union Jack completed a farm-in to licence PEDL183 located in East Yorkshire and within the Western sector of the Southern Zechstein Basin, containing the West Newton A-1 discovery, with Rathlin Energy, a subsidiary of Canadian registered Connaught Oil and Gas.

The West Newton A-2 well reached a total depth of 2,061 metres and 28 metres of core was recovered from the primary target, the Kirkham Abbey formation, and all planned logging, operations were completed.

Initial petrophysical evaluation identified a gross oil column of 45 metres underlying a gross gas column of 20 metres. The West Newton A-2 well exhibits encouraging porosities on logs and in core, particularly in the identified oil zone, where in excess of 30 metres of good porosity has been measured.

The operator and joint venture partners now believe that West Newton represents a significant oil and gas develpment project.

> **West Newton represents a significant oil and gas development project**

Following the integration and evaluation of the core, petrophysical, seismic and test data, the operator and joint venture partners intend to commission a revised CPR to re-assess volumetrics and revise NPV10 values based on the information acquired from the West Newton A-2 well.

### PEDL253 BISCATHORPE

PEDL253 is within the proven hydrocarbon fairway of the South Humber Basin and is on-trend with the Saltfleetby gasfield, Keddington oilfield and the Louth and North Somercotes Prospects.

In February 2019, the Biscathorpe-2 well was drilled and logging operations were conducted. Preliminary analysis indicated that the primary objective, the Basal Westphalian Sandstone, was not encountered as the well was drilled high to prognosis and did not thicken as expected in the pre-drill model.

Union Jack's independent technical team was greatly encouraged by the significant elevated gas readings and shows from logging, supported by calculated oil saturations in the Dinantian Carbonate over an interval in excess of 150 metres, which included a suite of gas indications C1 to C5 and nC5, which is indicative of an effective petroleum system in close proximity to the Biscathorpe-2 well.

As a result of these compelling indications of hydrocarbons, the joint venture commissioned independent consultants APT to perform a detailed geochemical analysis of drill cutting samples.

The objective of the APT analysis was to provide geochemical evidence for the presence of live hydrocarbons, together with an estimate of the likely oil quality.

The key result from the report was the likely presence of a 35 metre live oil column with API Gravity of 33° to 34° in the top of the Dinantian interval. Additionally, data evaluated at the base of the analysed section were suggestive of possible extra hydrocarbon pay at the base of the Dinantian interval.


This analysis has upgraded the Biscathorpe-2 well result, indicating proximity to an effective petroleum system, and validates Union Jack's and its joint venture partners' belief in the additional potential that exists within the PEDL253 licence area.

Following the drilling of the Biscathorpe-2 well and subsequent technical analysis, Union Jack management's view is that this prospect remains one of the UK's largest onshore un-appraised prospects.

The joint venture is continuing with detailed seismic re-processing and further technical studies to confirm the next steps in relation to a possible side-track of the Biscathorpe-2 well.

## PEDL180/PEDL182 WRESSLE DISCOVERY

Located in Lincolnshire on the Western margin of the Humber Basin, PEDL180 and PEDL182 contain the substantial Wressle conventional oil discovery with proven reserves and significant upside from contingent resources, from which first commercial oil is expected to flow at a constrained rate of 500 barrels of oil per day following successful planning approval.

In July 2019, the joint venture received notification that, in a closed meeting, a decision was made by the North Lincolnshire Council that it will not be presenting evidence at the Public Enquiry to be held on 5 November 2019, and will withdraw its case in respect of the appeal subject to the agreement of acceptable planning conditions.

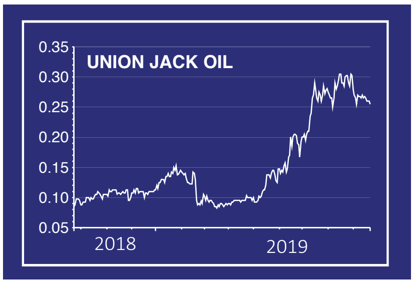
The Wressle-1 well discovered hydrocarbons in 2014. During testing, a total of 710 barrels of oil equivalent per day were recovered from three separate reservoirs, the Ashover Grit, the Wingfield Flags and the Penistone flags. In September 2016, a CPR provided independent estimates of reserves and contingent and prospective oil and gas resources for the Wressle discovery of 2.15 million stock tank barrels classified as discovered (2P+2C).

## NEWS FLOW

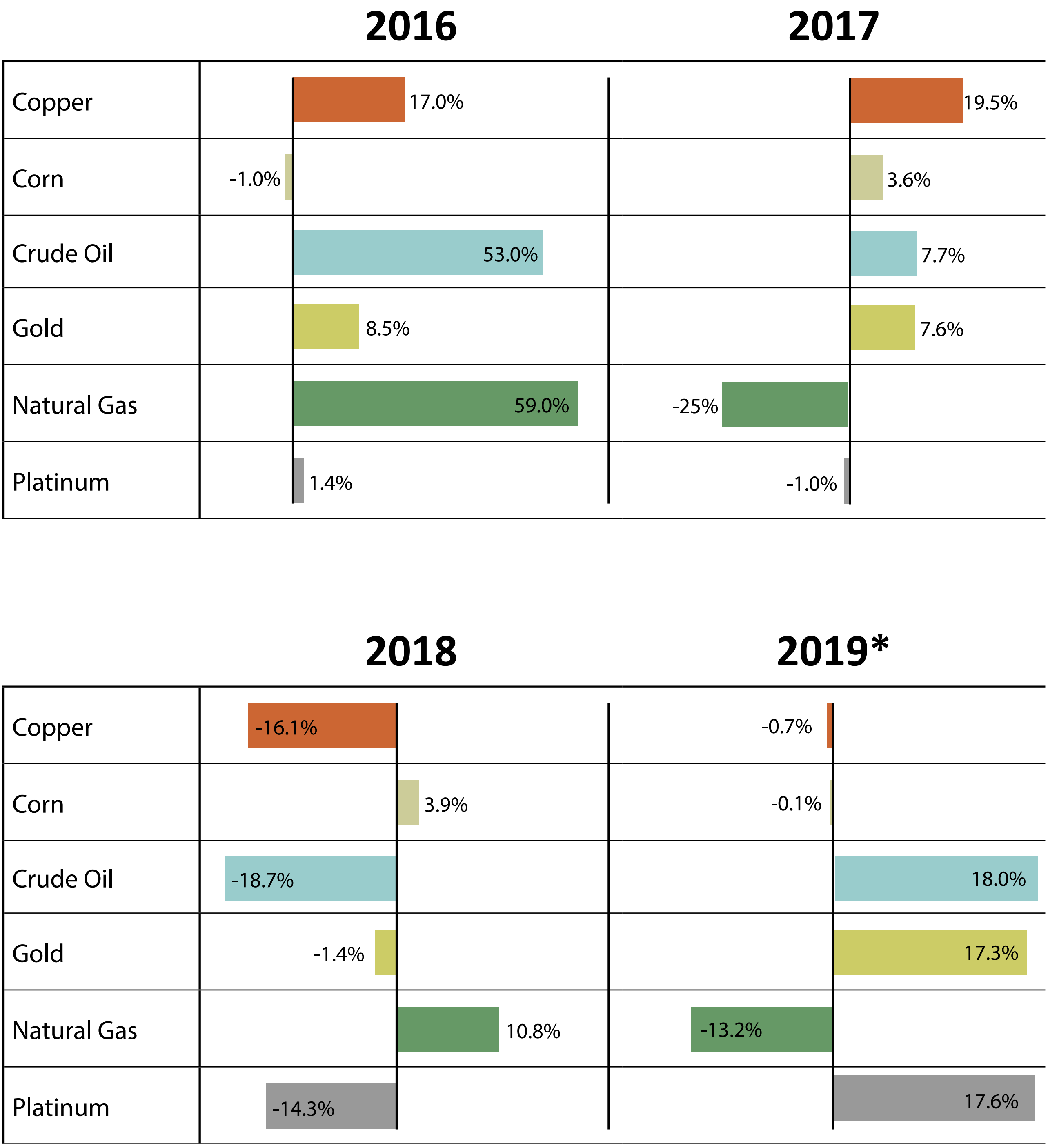
Union Jack has a balanced portfolio of production, development and drill-ready interests.

The company's strategy of focusing on conventional relatively low-risk and low-cost projects, avoiding early stage and frontier ventures is showing signs of reaching fruition and allows investors to become involved at the end of the exploration phase and the beginning of the development cycle.

There is a strong chance with projects such as West Newton, Biscathorpe and Wressle ongoing, that an active stream of news flow will be seen during the remainder of 2019 and beyond.

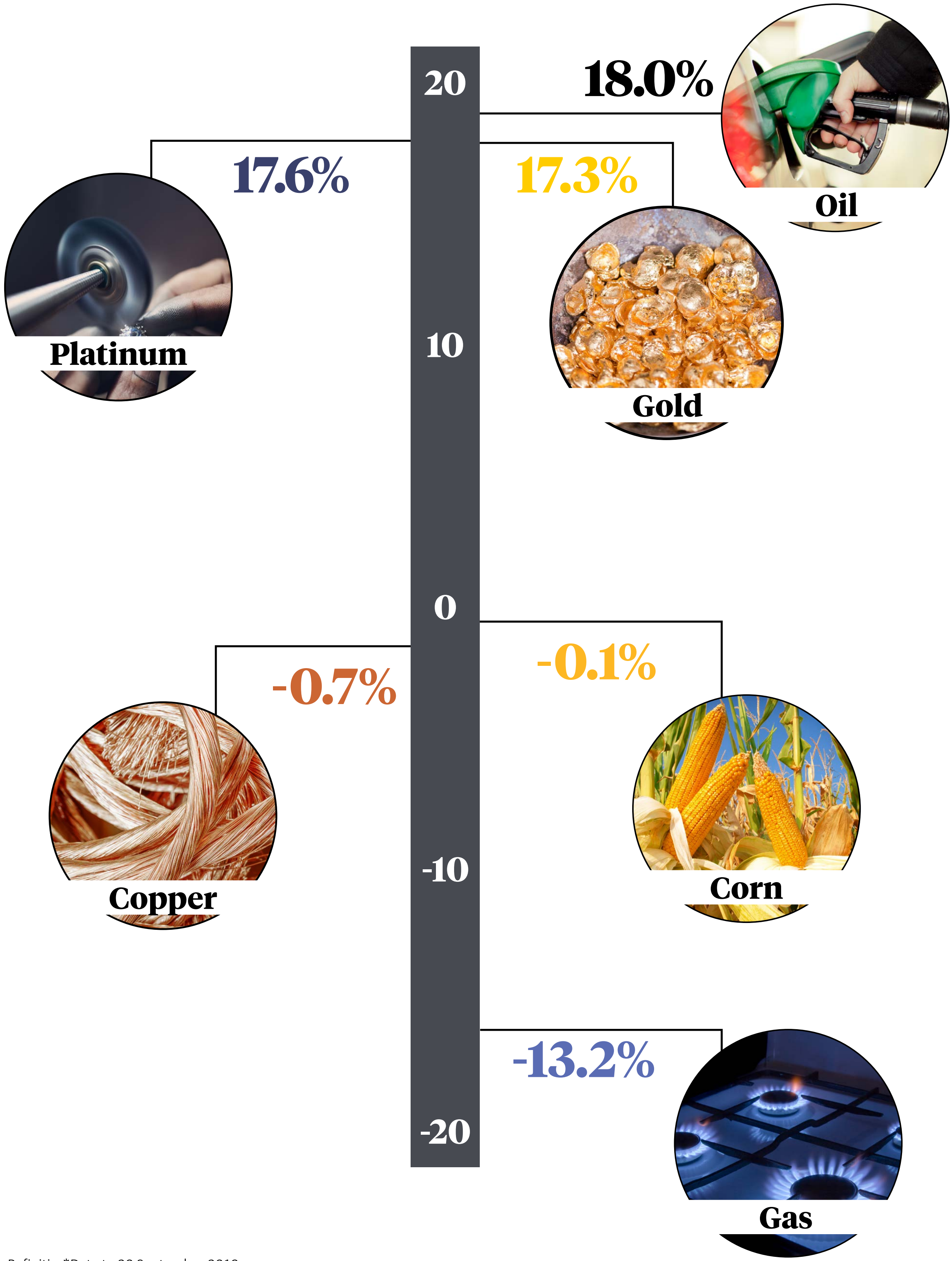


# **Databank** – Commodity price performance 2016-2019




Source: Refinitiv. *Data to 20 September 2019

# **Databank** – Gain / loss so far in 2019




Source: Refinitiv. *Data to 20 September 2019