JOHN BARON: HOW MY FOCUS ON NEW GROWTH THEMES IS REAPING REWARDS

investors CHRONICLE

Stockbroker platforms compared
Tune in to sweet music
Hurricane Harvey fallout
A lesson in incentives

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FIXED?

Testing the health of the banks 10 years on



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SEVEN DAYS

EDITORIAL

Investors left smarting



When Barclays Stockbrokers took the wrecking ball to its old sharedealing website, and replaced it with a new build, called Smart Investor, it was inevitable there would be grumbles and complaints. It takes time to get used to change and new builds are notorious for their flaws and faults.

But the issues at Barclays that have led to a torrent of angry emails to our office go much deeper than teething problems and hint at a wider, more worrying issue. This relaunch isn't a makeover, it's a whole new proposition – one designed for low-maintenance fund investors.

It's that which has prompted verdicts of "cumbersome", "inferior to its predecessor", "inadequate", and "unquestionably a downgrade".

Besides the teething issues, which are serious enough, there are much bigger frustrations for share investors. Critical functionality has been removed. It is now only possible to see five years of transaction history, which will surely create terrible capital gains tax headaches; while overseas shares are no longer supported. ISINs will no longer be displayed – which is a bit like knowing where you are flying to and at what time but not actually having your flight number. The ability to amend a stop-loss has been removed – you must start from scratch each time.

There is deep anger too over the integration of sharedealing accounts with bank accounts, and over the withdrawal of access to partner accounts. It seems perfectly sensible to me that the investor in the family should manage other accounts, but Barclays no longer allows this. And it's hardly Barclays' place to suggest as they did to one long-standing customer who has managed a spouse's investments for three decades (with her full authorisation) "as the account is in her name, it really should be her that's managing it".

Barclays Stockbrokers is a business and one must suppose the changes have been made for its convenience, not its clients'. It admits it wanted "to appeal to a wider audience including at the novice end of the market". It's not hard to see why. Regulatory and cost pressures heaped on traditional stockbrokers in recent years have increased. The temptation must be to discard models that are costly to support and to shunt your new and old customers into a less costly, more profitable fund-focused platform. It's the same force that has railroaded investors into pooled nominee accounts, stripping them of valuable rights.

The uncomfortable truth is that investors in the UK are increasingly seen as a burden rather than customers to be served and it's why they get a rough deal – yes, technology has brought down the cost of trading, but serious investors also need access to good-quality research, essential tools and support and up-to-date, accurate information.

With 200,000 customers, Barclays Stockbrokers is still one of the biggest retail brokers in the UK, although it trails Hargreaves Lansdown (with around 950,000 customers) by some way. For it to let investors down is a big blow. But it's also an opportunity for rivals to steal that business.

John Hughman is away. Rosie Carr is deputy editor

THE BIG STORIES

Back to normal

Call for end to QE

Germany's finance minister, Wolfgang Schäuble, has called for the European Central Bank (ECB) to return to more normal monetary policy, just two weeks after the euro rose to an eight-year high against sterling. Mr Schäuble said the ECB should end its bond-buying programme and negative interest rates, on the back of a stronger eurozone economy. The ECB is scheduled to begin discussion on tapering its €2 trillion bond-buying programme in 2018. It is buying up to €60bn of bonds each month at present, and is set to continue doing so until the end of the year.

Sports Direct re-elects

Chairman reinstated

Sports Direct (SPD) chairman Keith Hellawell survived an attempt to oust him by the skin of his teeth. Despite several institutional shareholders announcing their intention to vote against Mr Hellawell's reappointment, he was re-elected by 53.2 per cent of independent shareholders. Some investors have raised concerns about corporate governance and working conditions, including placing temporary staff on zero hours contracts. This followed news that trading across its new flagship sites had exceeded management's expectations.

Services slow

Orders down

Growth within the UK services sector slowed to its lowest in nearly a year in August, according to the HIS Markit CIPS purchasing manager's index. The index declined to 53.2, from 53.8 in July. A figure above 50 indicates expansion. The services sector accounts for about 80 per cent of the UK economy. The PMI survey indicated that new order volumes in the services sector increased last month at the second slowest rate since September 2016, while cost pressures also picked up.

THE NUMBERS

1%

The amount the Bank of Canada raised interest rates to, sending the Canadian dollar up to its highest level against the greenback in two years.

$1,000

The amount Bitcoin declined by within three days, after China announced plans to ban initial coin offerings, which allow companies to raise funds using digital tokens.

15%

The probability of a US government shutdown, according to estimates by Goldman Sachs. That's down from 35 per cent the prior week, with post Hurricane Harvey rebuilding efforts expected to reduce the risk of a showdown over federal funding.

GOOD WEEK FOR: ARROW GLOBAL P49

BAD WEEK FOR BLANCCO TECHNOLOGY P9



Trump tweets

North Korea's latest nuclear missile test has drawn more ire from Donald Trump. Alongside his regular threats of a military response to Kim Jong-un's administration in the Asian province, the President has suggested he will impose trade sanctions on any country "doing business" with North Korea. This includes America's trade deal with China, which last year supported $450bn (£344bn) of imports and $115bn of exports. It's hard to see how such a trade deal could stop without significant damage to both the US and global economies.

"Their plan to transform the group's consumer credit division went down as well as black pudding at the annual meeting of the Vegan Society"

MR BEARBULL, PAGE 16



Mining woes

Acacia/Shanta cash-flow remedies

In yet another reminder of the drastic impact the Tanzanian ban on exports of gold concentrate has had on Acacia Mining (ACA) and Shanta Gold (SHG), the gold miners updated the market on remedial measures to stem cash outflows. The former is to reduce operational activity at its Bulyanhulu mine. It said 35 per cent of its production has been affected to date, leading to a $265m build-up of concentrate inventory and a cash outflow of $210m. Meanwhile, Shanta announced measures including a 15 per cent salary cut for senior management and a switch in discretionary executive pay from cash to shares.

Challenger ahead

Charter Court IPO

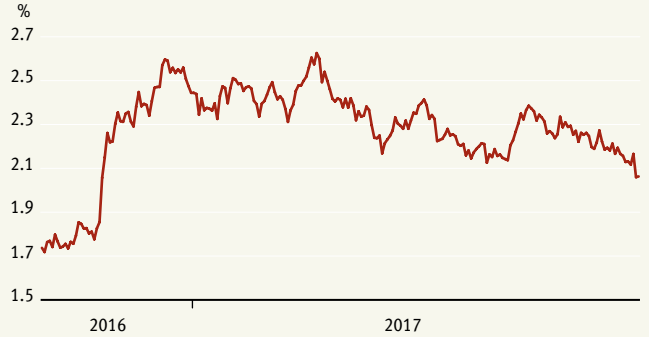
Challenger banks Onesavings Bank (OSB) and Aldermore (ALD) have enjoyed rapid growth in their loan books during recent years. Now rival mortgage lender Charter Court has announced its intention to float on the premium segment of the London Stock Exchange. At the time of going to press no pricing data had been announced. However, the group is looking to raise £20m from the IPO, with an additional over-allotment option representing 15 per cent of the offer size. Old Mutual Global Investors has also signed a letter of intent for £100m of shares.

BNN suspended

Change at the top

BNN Technology (BNN) has suspended its shares from trading on Aim, after chief financial officer Scott Kennedy resigned on Friday 1 September. As part of his resignation, Mr Kennedy "made a number of serious allegations" regarding the company, and the actions of chief executive Darren Mercer and Wei Qi, China chief executive and group chief operating officer. Financial controller Patrick O'Connor has stepped in as interim chief financial officer. BNN also announced that while it "does not have sufficient information to comment definitively on the allegations", it has decided to suspend the employment of both Mr Mercer and Mr Qi effective immediately.

Chart of the week: US treasury yields dip to 10-month low



Source: Bloomberg

US treasury yields fell to their lowest level since just after the US election, on the back of escalating tension with North Korea this week.

Yields – which move in the opposite direction to prices – dipped to 2.06 per cent (see chart). The rally in US treasuries followed North Korea's detonation of its largest nuclear advice to date, as well as the threat of Hurricane Irma hitting the US.

Comments from Federal Reserve governor Lael Brainard urging caution on lifting US interest rates while inflation remains subdued, also likely hastened the risk-off approach from investors.

Risers and fallers (%)

▲ Aveva	+28.47
▲ Luceco	+15.91
▲ Victrex	+13.58
▲ Zotefoams	+11.85
▲ Amec Foster Wheeler	+10.56
▼ Indivior	-31.77
▼ HSS Hire	-25.23
▼ Exillon Energy	-13.59
▼ Acacia Mining	-12.35
▼ Nanoco	-12.15

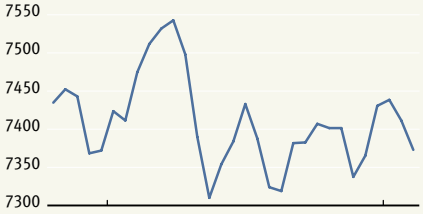
Week to 5 September 2017

For more market data go to page 8

UK stock market

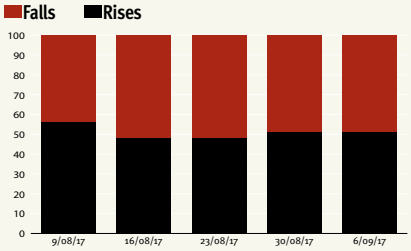
Index	5/09/17	1-week change (%)	1-month change (%)	1-year change (%)	Year high	Year low	PE	Dividend yield (%)
FTSE 100	7,372.92	+0.48	-1.85	+7.17	7,547.63	6,665.63	24.8	3.89
FTSE 250	19,726.83	+1.02	-1.22	+9.44	20,024.92	17,271.24	22.0	2.68
FTSE All-Share	4,044.60	+0.58	-1.69	+7.84	4,130.15	3,641.91	24.3	3.65
FTSE Aim	5,157.82	+0.94	+2.26	+36.78	5,188.40	3,786.98	45.2	1.22

FTSE 100 rolling 30-day



Source: Thomson Datastream

Share performance



IC ONLINE

For more UK market data, see http://markets.investorschronicle.co.uk

Other major markets

Index	5/09/17	1-week change (%)	1-month change (%)	1-year change (%)	Year high	Year low	PE	Dividend yield (%)
Eurofirst 300	1,468.30	+1.39	-2.39	+6.40	1,558.02	1,296.32	20.95	3.37
CAC 40	5,086.56	+1.09	-2.25	+12.01	5,432.40	4,332.45	18.08	3.26
Dax 30	12,123.71	+1.49	-1.41	+13.60	12,888.95	10,259.13	16.87	2.77
Dow Jones	21,753.31	-0.51	-1.54	+17.64	22,118.42	17,888.28	19.55	2.42
S&P 500	2,457.85	+0.47	-0.77	+12.75	2,480.91	2,085.18	21.04	2.02
Nasdaq Comp	6,375.57	+1.17	+0.38	+21.44	6,435.33	5,046.37	39.05	1.14
Nikkei 225	19,385.81	+0.12	-2.84	+13.78	20,230.41	16,251.54	15.04	1.79
Hang Seng	27,741.35	-0.09	+0.65	+17.30	28,094.61	21,574.76	15.08	3.16
Australia ASX All Ords	5,767.80	+0.60	-0.10	+4.41	5,976.40	5,238.30	18.03	4.20

Key emerging markets

Index	5/09/17	1-week change (%)	1-month change (%)	1-year change (%)	Year high	Year low	PE	Dividend yield (%)
Brazil iBovespa	na	+1.15	+7.85	+21.13	72,150.88	56,820.77	22.53	2.74
Russia RTS	1,100.83	+3.11	+7.22	+12.62	1,195.61	960.32	7.54	5.18
India CNX Nifty	10,357.50	+1.70	-0.83	+14.63	10,465.10	8,093.89	23.13	1.33
China SE Comp	3,384.32	+0.57	+3.75	+10.16	3,384.32	2,980.43	17.74	1.86
Thailand SET	1,620.42	+0.39	+2.67	+8.57	1,620.42	1,406.18	17.38	2.98
Turkey ISE 100	108,872.90	-1.40	+0.30	+39.95	110,423.10	72,519.81	10.61	2.46
Argentina Burcap	67,643.94	+2.12	+10.39	+50.66	67,643.94	43,465.10	na	0.82

Economic indicators

Indicator	UK	US	Germany	Japan
Inflation (Index Jan 87=100) Change on year	272.9 (Jul) +3.6%	244.8 (Jul) +1.7%	109.3 (Jul) +1.7%	99.7 (Jul) +0.2%
Unemployment Change on year	0.81m (Jun) +4.6%	6.98m (Jul) -9.9%	2.54m (Jul) -5.4%	1.89m (Jun) -8.7%
Industrial production Change on year	104.7 (Jun) +0.3%	105.2 (Jun) +2%	112.9 (Jun) +2.5%	102.3 (Jun) +5.5%'
Average earnings Change on year	£473 (May) +2.2%	$9.3 (Jul) +0.8%	111.2 (May) +2.7%	100.2 (Jun) -0.5%
Retail sales volume Change on year	115.9 (Jun) +2.9%	$479,507m (Jun) +3.3%	110.1 (Jun) +1.5%	¥11,572bn (Jun) +2.2%
Current account Actual change on year	-£16.9bn (Q117) +£8.83bn	-$116,781m (Q117) -2%	+€23.64bn (Jun) -1.7%	+¥1,522.5bn (Jun) -4.2%
Money supply – M1 Change on year	£82.4bn (Jul) +4.8%	$3,531.6bn (Jul) +8.8%	€2,846.2bn (Jun) +5.7%	¥714,972bn (Jul) +7.5%

Commodities

	5/09/17	Year high	Year low
Dow Jones UBS Comm. Index	340.59	347.28	306.53
Brent Crude $/barrel	53.63	57.06	43.84
Comex gold $/ounce	1,337	1,345	1,127
LME three-month copper	6,900	6,917	4,620
Cocoa £/mt	1,519	2,270	1,390
Coffee Brazil ¢/lb	124.29	170.90	115.39

Currencies

	Rate	1 year max.	1 year min.
US$ vs £	1.30	1.34	1.21
Euro vs £	1.09	1.20	1.08
Yen vs £	141.82	147.75	126.09
SFr vs £	1.25	1.31	1.19

MORE ONLINE

For more cross rates and a currency convertor, see http://markets.investorschronicle.co.uk

Official interest rates

	Rate (%)	Since
UK Bank rate	0.25	4/08/16
ECB Repo rate	0	16/03/16
US Fed Funds	1.00-1.25	14/06/17
Japan	-0.1-0.1	29/01/16

Government bonds

Govt bond yields	%	Year high	Year low
UK: 10-year gilts	1.05	1.51	0.64
US: 10-year Treasuries	2.13	2.61	1.54
Germany: Bunds	0.26	0.57	-0.22
Japan: JGBs	0.01	0.11	-0.09

MORE ONLINE

For more global bond data, see http://markets.investorschronicle.co.uk

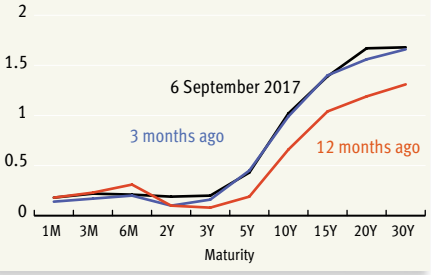
Corporate bond indices

	5/09/17	Yield (%)	Year high	Year low
Investment grade	97.82	1.02	99.75	96.42
High yield	120.47	2.65	120.85	116.54

MORE ONLINE

For prices of popular corporate bonds and Pibs, see www.investorschronicle.co.uk/bonds.

UK yield curve



NEWS

OIL & GAS

Oil market weighs Harvey effect

The fallout from hurricane Harvey has started to emerge in global energy markets

ALEX NEWMAN

For the past decade, Houston and the wider US Gulf have been at the centre of the country's shale revolution. Over the past fortnight, the region has found itself devastated by the first major hurricane to make landfall in the US since 2005, forcing the closure of a third of the country's refinery capacity, and oil and gas production across Texas and Louisiana.

Two of **Royal Dutch Shell's (RDSB)** deep water facilities have been affected by Harvey, according to chief executive Ben van Beurden. A restart of the oil major's refining and petrochemicals complex at Deer Park, Houston, which processes 325,700 barrels of crude a day, was only just being prepared at the time of writing. Elsewhere, flooding in downtown Houston meant the US headquarters of **BP (BP.)** and **ConocoPhillips (US:COP)** remained closed as of this week, according to the local media.

One London-listed company may have been particularly hard hit. On 30 August, **Pantheon Resources (PANR)** warned that Harvey's path could pass its projects in Tyler and Polk counties, north-east of Houston. The Aim explorer acknowledged that suspension of its operations would result in delays to drilling at its VOBM#2H and VOBM#4 wells, although there had been no further update on potential damage to wellheads or associated facilities as we went to press.

For others, the wider ramifications were gradual, and may yet be unmasked through the steady release of US storage data. The latter has been a key indicator for oil markets, which are continually sizing up the force of US onshore production. Concerned that a sudden drop in processing demand from shuttered refineries could lead to a fall in crude prices, some commodity traders initially viewed Harvey as a bearish event.



Hurricane Harvey has forced the closure of oil and gas production across Texas and Louisiana

But with Gulf refineries, pipelines and ports restarting, and the US government forced to release 4.5m barrels of crude from its strategic reserves, the short-term pricing outlook for oil producers has brightened. Indeed, the S&P 500 Energy Index (SP500-10) – a composite of the largest US-listed explorers and producers (E&Ps) – is up 3 per cent since Harvey made landfall. At $53.83 a barrel, Brent crude is at its highest point since May.

Analysts at HSBC noted that the decline in crude stocks had been above average so far this summer, but cautioned that US data "is likely to be extremely volatile in the coming weeks", as the industry digests swings in US imports and exports. In the longer term, the ramifications could be enormous. Harvey will inevitably lead to questions over the capacity of the US Gulf's highly concentrated oil and gas infrastructure to sustain extreme weather events that scientists tell us are increasingly likely. Forget fears of persistent global oversupply; climate change's meteorological effects are an even greater current danger to the US energy renaissance.

Blancco warns (again) on profits

It had already been a disappointing year for Blancco Technology's (BLTG) shareholders before the shares tumbled a further 26 per cent on the day of its latest profit warning. Management plans to reverse £2.9m of sales booked for two contracts during the 12 months to 30 June this year and has revised down its sales expectations for that year.

Sales are now expected to be 15 per cent ahead of the prior year at constant currency, down from the 30 per cent gain announced in July. That's resulted in a 41 per cent cut to adjusted cash profit expectations, to £4.1m. On the back of this announcement, chief executive Pat Clawson has resigned, with interim chief financial officer Simon Herrick temporarily stepping in to the top job.

Management said cash flow had not been affected by the reversal of the revenue for the two contracts. That's just as well, since it had already been forced to conduct a review of its cash flow following the release of its half-year results in March. Costs from previous acquisitions, plus a large government contract delay during its final quarter, meant it needed to raise an additional £4m in cash.

Blancco – formerly Regenersis – stacked up considerable M&A-related costs during the first half of the year, as it tried to transition to a pure software business. The shares are down more than two-thirds during the past 12 months and trade at just 10 times forward earnings. We're looking for evidence of tighter controls on revenue recognition and sufficient growth to support its numerous purchases. At 71.5p, hold.

Emma Powell



Indivior had 31 per cent knocked off its market value after losing a patent battle in the US

PHARMACEUTICALS & BIOTECHNOLOGY

Indivior: too risky to hold

The opioid addiction specialist's shares crumbled after US court decision

MEGAN BOXALL

Can **Indivior (INDV)** recover from a major setback in its ongoing patent dispute? A US court concluded that an unbranded version of the group's opioid addiction treatment – made by Indian pharma company Dr Reddy's – does not breach Indivior's patent, clearing the way for lower-priced competition. The highs of recent months – when many courts ruled in favour of Indivior's various legal proceedings – have been replaced with a crashing comedown. Indivior intends to appeal the US District Court for the District of Delaware's decision. The shares plummeted 31 per cent on the day of the announcement and have only made up a small amount of ground since.

Indivior has been attempting to satisfy a growing demand for addiction treatments, caused by an increase in the number of opioid addicts in the US. Its flagship drug, Suboxone, is prescribed for adults who are dependent on prescription or illegal drugs – a market currently worth about $2bn (£1.5bn) and growing by around 10 per cent a year.

But the UK group is not the only company active in this market. Mylan, Actavis and Teva are just a handful of the many pharmaceutical groups to have developed a similar drug. This rising competition caused Suboxone's US market share to contract to 57 per cent by June this year, from 61 per cent six months earlier.

But 57 per cent market penetration will be nothing but a fond memory if Dr Reddy's cheaper version of Suboxone does indeed find its way onto the shelves. The court's ruling that the treatment bypasses Indivior's patent means Dr Reddy's will be allowed to launch its drug if it is given the green light by US regulators. Suboxone's US sales contributed about 80 per cent of total Indivior revenue in 2016 and the arrival of Dr Reddy's generic competition could wipe two-thirds off the top line within a matter of months, according to management.

However, analysts are keeping a positive stance. Although broker Numis has warned of a 25 per cent cut to 2018 forecasts if just one generic hits the market, analyst Paul Cuddon "sees little chance of Dr Reddy's launching in 2017". The broker has retained its buy call on Indivior, citing the good value in the group's shares following their mammoth fall.

Meanwhile, the impending launch of a monthly injection of Suboxone could yet be the drug's saviour. Keeping opioid addicts on their treatment is a massive challenge in the US and doctors are more likely to prescribe drugs that require less patient responsibility.

Indivior remains impeded by legal battles. The shares are trading at 10 times Bloomberg's consensus forecast earnings for this year, just a small discount to its historical average of 12 times. The market may be attractive, but persistent competition and continuing costs of patent disputes gives a murky outlook. We think investors would be better off avoiding for now. Sell.

AIM: TRAVEL & LEISURE

Expansion is costly for Fulham Shore

HARRIET RUSSELL

Shares in Franco Manca owner **Fulham Shore (FUL)** plunged 22 per cent on the day the group revealed cash profit for the current financial year will fall short of market expectations.

Trading weakened significantly over the summer, especially at locations across London suburbs. That's despite a benign pricing environment, as Fulham Shore has kept prices flat for fear of alienating customers. The group also plans to pay the national living wage in accordance with legislation – all of which is putting pressure on the bottom line. It also plans to offload its singular franchise of the Bukowski Grill as it simplifies operations.

We've long said the valuation of Fulham's shares looked toppy, despite ambitious growth plans and seeming success across the Franco Manca and Real Greek brands. This perhaps proves our point that fast growth often comes at a price. Hold at 13p.

ON THE WEBSITE THIS WEEK

Income Majors Podcast

Investors have long favoured dividends for many reasons: the regular year-on-year income, a sign of management confidence about the future and arguably as compensation for the risk of investing in a company over the long term. In July we took a look at the FTSE 100's top 10 dividend payers in our 'Income Majors' special feature, examining the stability of the payments being made.

In the second episode of our 'Income Majors' podcast series, we examine the telecoms and mining sectors. Companies editor Ian Smith asks specialist writers Megan Boxall and Alex Newman whether dividends are safe at BT (BT.A), Vodafone (VOD), Rio Tinto (RIO) and BHP Billiton (BHP). Will BT's spending commitments and latest profit warning put pay to its payouts? What does a certain activist investor mean for BHP's income attractions?

To listen to this podcast and more, go to www.acast.com/investorschronicle.

Aveva's enhanced bid for scale

The terms of Aveva's plan to combine with Schneider's software are more favourable for its shareholders

HARRIET CLARFELT

The phrase 'third time's a charm' seems to ring true for **Aveva (AVV)** and Schneider Electric. The London-listed group will combine with Schneider's software business via a reverse takeover, given the relative size of the latter. Since 2015, two rounds of takeover talks have failed. However, judging by the jump in Aveva's share price of almost a third on the day of this latest announcement, investors are eager for the merger to succeed. The deal is valued at £3bn, with the enlarged group retaining a London listing.

'Management estimates combined pro-forma revenue for the year ended March 2017 would have reached around £649m, more than three times that achieved by Aveva during that period'

Under the terms of the agreement, Aveva will issue 97.4m new shares to Schneider, giving it a 60 per cent stake in the combined entity: equivalent to approximately £1.7bn. Meanwhile, Aveva shareholders will receive aggregate payments of up to 1,014p a share. This includes a payment from Schneider of approximately 858p a share in cash (£550m in total), and a return from Aveva itself of 156p a share, or £100m in total from its balance sheet. They will retain 40 per cent of the enlarged group's stock. There will be a standstill agreement limiting Schneider's ability to build its stake further for three-and-a-half years post-completion.

So, how does this takeover attempt differ from the last couple of times a potential agreement was on the table? Back in July 2015, when discussions were first under way, Schneider was to have a 53.5 per cent stake in the larger Aveva group, while its target would retain 46.5 per cent ownership. Clearly, Aveva's allocated share has since reduced. But investors will receive significant payments for allowing this to happen. Analysts at Barclays believe Aveva shareholders are "by far the key beneficiary" in this latest deal.

This deal has actually been agreed, rather than being a preliminary discussion. What's more, Schneider Electric is bringing a lot more to the table this time around. Additional software assets make the business around 20 per cent larger than at the time of the last talks in 2016, according to estimates from broker Numis Securities. These include the oil and gas pipeline management solutions segment of Telvent, acquired by Schneider in 2011.



Schneider Electric is 20 per cent bigger than at Aveva's last merger attempt, including parts of Telvent, acquired in 2011

What are the reasons for this reverse takeover? The language used in the prospectus was encouraging, claiming the combination would allow the group to achieve "scale and relevance in key markets as well as an extensive technology portfolio". Management estimates combined pro-forma revenue for the year ended March 2017 would have reached around £649m, more than three times that achieved by Aveva during that period. This would have produced adjusted pre-tax profit of £146.3m, compared with Aveva's £55m, according to the deal's prospectus.

The combination of the businesses should also increase Aveva's end-market coverage and give it exposure to new sectors. Schneider Electric Software Business has leading positions in the chemicals, food and beverage and pharmaceuticals segments. Admittedly, it would increase Aveva's dependence on cyclical industries, including oil and gas, and mining and marine. What's more, analysts at Numis forecast earnings per share for the enlarged group of 66.9p for the year to March 2018, down from an estimate of 69.9p prior to the transaction due to the enlarged share capital.

The two parties are working to select a new chief executive for the enlarged group, with the required track record and experience. For now, Aveva chief executive James Kidd stays – but he will move into the role of deputy chief executive and chief financial officer once a replacement is announced.

This deal has been on (and off) the cards for some time now, but it looks as though both businesses are satisfied with the new terms. Completion is expected to occur around the end of 2017, subject to various conditions, including Aveva shareholders voting in favour of the deal at the general meeting on 29 September. Shareholders will be ceding some control via this deal. However, we reckon it has the potential to significantly boost Aveva's growth prospects, by giving it greater scale within North America and access to the freight owner-operator market – a long-held strategic goal of Aveva's. With the improved terms also in mind, accept.

US debt: a ticking timebomb

Jonas Crosland says the US has already reached its debt limit and time is running out to secure a new ceiling

President Donald Trump has shown his ability to ruffle more than a few feathers, but when it comes to taking on economic reality he is likely to come a poor second. The issue comes in the form of the budget deficit that in March reached the debt ceiling as set by Congress. At the moment that stands at $19,800,000,000,000m or $19.8 trillion (£15.3 trillion) for short, and that limit has already been touched this March. Since then, the Treasury has been muddling through using so-called extraordinary measures. These can cause damage because such cash management operations include suspending investments in pension funds for federal workers. And time is running out; it may only be a couple of weeks before the shutters come down with the end of the financial year on 30 September. Given that the Republicans have control of the White House and Congress; this shouldn't be a problem under normal circumstances. But the administration's inability to get legislation onto the statute book tends to suggest that it may not be plain sailing lifting the debt ceiling.

'The administration's inability to get legislation onto the statute book tends to suggest that it may not be plain sailing lifting the debt ceiling'

The situation is not a new one, having occurred in 2011 and 2013, and in 2011 the situation went right down to the wire before an increase was authorised, while in 2013 there was a 16-day Federal shutdown. The latest situation comes at an awkward time because as one of the biggest buyers of US government debt, the Federal Reserve, has hinted that the time has come to prune its balance sheet and wind back its Treasury bill purchases. That is likely to be put on hold until debt markets are free of uncertainty.

Reaching a solution might take some time because within the Republican Party there are pressure groups that are unlikely to give their blessing to any rise in the debt ceiling without getting something in return. So what happens if President Trump calls all the bluffs and allows a financial shutdown? In 2011, the delay in raising the debt ceiling had some immediate and unpleasant consequences. First to go was the US credit rating suffering its first ever downgrading. This was followed by a significant fall in equity markets and higher borrowing costs as lenders demanded a greater risk premium. The obvious way out is to reduce the spending bill, but even that would attract fierce opposition, notably from the Democrats, while the big corporations would also lobby hard if there were any attack on their vested interests.



US Treasury Secretary Steve Mnuchin has said that hurricane Harley aid should be tied to increasing the debt ceiling

It seems likely that some sort of fudge will be arrived at. President Trump has been putting pressure on Congress to agree funding for his border wall, but all bets seem to be off in the wake of the hurricane in Texas, which will require substantial Federal aid, and any delays in solving the budget deficit could affect funding any relief effort.

Next week's economics...

Among a whole host of economic data due for release in the UK next week, inflation is likely to be among the most closely watched indicators. The retail price index reading is due for release on Tuesday, having risen by slightly more than expected in July to a year-on-year rate of 3.6 per cent. This takes on a greater importance because on Thursday the Bank of England's Monetary Policy Committee meets to decide on what to do with interest rates. The August meeting showed two committee members voting for a rise in rates while the remaining six voted to leave rates unchanged. It is 10 years since the Bank raised rates, and it would not be unusual for people to forget that the Bank always runs the risk of falling behind the curve in an attempt to curb inflation, rather than acting pro-actively.

However, inflation at the moment is largely a by-product of cost inflation and less the result of a supply/demand imbalance pushing prices higher. And as estimates on economic growth – currently rather weak – are very much a hostage to fortune as the Brexit process drags on, it may not yet be the time to see how well the economy can cope with a rise in borrowing costs. It's also worth remembering that sterling is now higher against the dollar than it was in the wake of the referendum result, so the cost of currency-related imported inflation should now be less. However, there may be pressure building on the employment side, where an increasingly tight labour market could put upward pressure on wage inflation.

ECONOMIC CALENDAR

There's now a comprehensive calendar of worldwide economic events and news releases on our website at:
http://markets.investorschronicle.co.uk/Research/Economic-Calendar

COMMENT

SIMON THOMPSON



Riding earnings momentum

Simon Thompson highlights three small-cap companies offering strong earnings momentum

It's always good when a company on my watchlist beats market estimates, and even more so after I have just initiated coverage. That's the case with **Ramsdens Holdings (RFX:169p)**, a diversified and fast-growing financial services company that joined London's junior market earlier this year. I was pretty impressed by the investment case when I covered the maiden results, so I suggested buying the shares at 132p, placing a target price of 180p ('A jewel in the north', 12 June 2017).

I had good reason to be bullish because earnings momentum skewed the investment risk to the upside: house broker Liberum Capital had upgraded its pre-tax profit and EPS estimates by 13 per cent on the back of a pre-close trading update in April. In the event, Ramsdens exceeded those forecasts by a few percentage points, reporting a 73 per cent rise in pre-tax profit to £4m to produce adjusted EPS of 10.1p on revenues up 15 per cent to £34.5m in the 12 months to end-March 2017.

A key driver has been Ramsdens' foreign currency arm, which exchanged £408m-worth of currency with more than 600,000 retail customers to underpin an 18 per cent increase in the division's gross profit last year, to £9m. The segment accounted for 37 per cent of the company's gross profits of £24.3m, and there was every reason to expect the growth to continue, as has proved to be the case. Trading activity has been buoyant over the summer, so much so that analyst Justin Bates at broking house Liberum Capital believes Ramsdens' foreign currency arm's gross profits will rise by 20 per cent to £10.8m in the 12 months to end-March 2018, or £300,000 more than forecast when I initiated coverage. And this isn't the only driver behind Liberum's latest eye-catching 22 per cent pre-tax profit and earnings upgrade for this year, and the 19 per cent hike in its expectations for the 2018-19 financial year.

The surge in the gold price and sterling's weakness has clearly been benefiting the company's pawnbroking business, which accounts for a quarter of gross profits. In fact, Liberum has upgraded its divisional gross profit estimates by £500,000 for both financial years to around £6.8m, and justifiably so given that the sterling gold price has risen by 13 per cent to £1,033 an ounce (oz) since December 2016. A rising gold price enables the business to offer larger pledges, boosts profits on scrap and gold dealing, and mitigates the risk of losing money if a customer fails to redeem their pledge and the item has to be sold. The company is also benefiting from its jewellery retail initiatives, including increasing the proportion of jewellery sold through its retail outlets, in many cases after being refurbished following purchase, and increasing stock levels on the retail merchandising side.

These catalysts explain why Liberum upgraded its gross profit estimate for the company from £26.8m to £27.5m for the current financial year to end-March 2018, implying 13 per cent year-on-year growth, on revenues up 9.5 per cent to £37.8m. The reason why Ramsdens' pre-tax profits and EPS are expected to come in even higher at £5.9m and 15.3p, respectively, representing 45 to 51 per cent year-on-year growth, is that the company made £400,000-worth of savings on store openings. Liberum is factoring in six new stores this year, or half its previous forecasts, following the decision of the directors to "proceed carefully when deciding which new sites to complete on..... given the myriad of opportunities in the market". This should not detract from the long-term strategy of expanding the 127-store estate, and Liberum has factored in 12 new store openings in the 2018-19 financial year when it expects Ramsdens to deliver revenues of almost £41m, gross profits of £29.6m, pre-tax profits of £6.2m and EPS of 16.1p.

The bottom line is that although Ramsdens' share price is 28 per cent higher than when I initiated coverage in June, the forward rating of 11 times earnings estimates has hardly budged following upgrades. Moreover, a prospective dividend yield of 3.9 per cent, rising to 4.2 per cent in the 2018-19 financial year, remains attractive – as is a cash pile that's set to rise from £9.6m to almost £13m by the end of April, a sum worth 42p a share. This means that the company is being valued on just over five times cash profit estimates of £7.5m to its current enterprise value of £39m, a hefty ratings discount to larger rival **H&T (HAT:330p)**, a constituent of my 2017 Bargain Shares Portfolio, and one that's doing rather well too. H&T is rated on eight times cash profit estimates to enterprise value for the calendar 2018 financial year, a valuation that still offers 14 per cent further share price upside to my initial target price of 375p.

In the circumstances, I am edging up my fair value target price for Ramsdens to a range between 190p and 200p. Buy.

Stadium on track

I had an informative results call with the management team at **Stadium (SDM:123p)**, a niche electronics company specialising in wireless, power and human machine interface products. I last advised running profits on the shares at 133p after they hit my 130p target ('Value opportunities', 19 July 2017), having first advised buying at

Simon Thompson's book **Stock Picking for Profit** *can be purchased online at www.ypdbooks.com, or by telephoning YPD Books on 01904 431 213 and is being sold through no other source. It is priced at £14.99, plus £2.95 postage and packaging. Simon has published an article outlining the content, 'Secrets to successful stockpicking', which can be read on the Investors Chronicle website.*

75p ('Switch on to the Stadium of light', 30 July 2014), and booked dividends of 7.7p a share.

A key take for me is the company's burgeoning order book, which has risen by 19 per cent to a record high of £30.8m since the start of the year, and is up from £28m when I covered the full-year results in March. A £40m-plus design-led pipeline of business in its high-margin technology products division augurs well too. This segment has been growing organically, and by acquisition, and now accounts for 61 per cent of Stadium's revenue, up from only 21 per cent in 2013, reflecting its transition from an electronic manufacturer to a design-led technology company.

This trend is being driven by demand for technology products, including high-growth wireless devices such as insurance telematics, and the rapidly growing market for the 'internet of things', which encompasses security, smart home devices and energy management. The company's four design centres, including the newly expanded centre at Kista Science City, Stockholm, a global hub for wireless technology, provides Stadium's customers with an integrated technology solution for turnkey design, manufacture and fulfilment.

Importantly, the ramp-up in research and development spend by almost 150 per cent to £714,000 in the six-month period is paying off as the company has secured several new original equipment manufacturer (OEM) design-led orders for automotive and smart home projects, primarily in Europe and the US. The recently opened sales office in Salt Lake City, on the back of demand from customers, provides a footprint for expansion into North America. Interestingly, almost half the pipeline in the connectivity business comes from the region, up from 10 per cent last year, highlighting the potential for growth there.

Stadium has been adding to its capability in its power division, too, having just announced the earnings accretive complementary acquisition of Berkshire-based PowerPax, a specialist maker and distributor of power supplies, battery chargers and LED products, for an initial cash consideration of £2.5m, the fifth acquisition in as many years. With the benefit of a new £15m debt facility with HSBC, expect further bolt-on deals, and justifiably so given the returns that can be made: finance director Winston North informed me that Warrington-based United Wireless, acquired in the summer of 2014, has produced a 40 per cent-plus profit return on the £6m initial consideration.

True, Stadium's low-margin assemblies business proved a drag, but it is being increasingly used to supply orders in Stadium's technology products division and this is supportive of double-digit second-half growth, according to Mr North. Chief executive Charlie Peppiatt expects vertically integrated activity levels to exceed half of the unit's revenues by the fourth quarter. Adverse currency movements had a negative impact too, but the company still reported a 13 per cent rise in first-half normalised pre-tax profits to £1.8m and, with the benefit of a robust order book, which underpins the seasonal second-half weighting skewed into house broker N+1 Singer's forecasts, Stadium is well on course to lift full-year pre-tax profits by 26 per cent to £5.3m. On this basis, the shares are rated on 11 times earnings estimates, hardly a punchy rating for a company that's also well placed to deliver 20 per cent-plus EPS growth in 2018. A 2.6 per cent prospective dividend yield is attractive, too.

The bottom line is that if the order book continues to grow, then this will de-risk 2018 forecasts and support a much higher target price. Chart watchers will note than a share price move above the 138p resistance level that has capped progress since May would be a bullish sign, too. I would run profits for now, but would turn a buyer again on a break-out.

Gama Aviation in the ascent

The directors of Aim-traded **Gama Aviation (GMAA:260p)**, an operator of privately owned jet aircraft, were in confident mood during our half-year results call, and with good reason. The headline numbers are telling: underlying pre-tax profit increased by 40 per cent to $7m (£5.4m) in constant currencies on group revenues up 45 per cent to $291m, the vast majority of which is being fuelled by the US air business, which increased revenues from $110m to $190m following the Landmark fleet joint venture with **BBA Aviation (BBA)**. Divisional operating profits rose even faster, up 150 per cent to $6m, reflecting a 90 basis point improvement in margins to 3.1 per cent, driven by increased scale and operational gearing. The integration of the BBA business is delivering the benefits envisaged at the time of the merger, adding complementary west coast coverage to the existing east coast business; diversifying the overall client base; cross-selling maintenance services into Gama Aviation's wholly owned US ground business; and delivering cost savings, too.

Operating profits in Gama's European air arm rose from $0.6m to $1.5m, and operating margins almost trebled to 3.5 per cent, moving towards the 5 per cent target rate, an outcome that vindicates management's decision to exit underperforming contracts last year. The third driver behind the robust first-half performance was Gama's European ground services business, which increased operating profits by almost 30 per cent to $4.16m on a modest rise in revenue to $20.9m. This reflected the benefits of last year's restructuring, an uptick in discretionary spending among customers and a six-month contribution from the February 2016 acquisition of Jersey-based Aviation Beauport.

Gama's cash generation stands out too: operating cash flow of $5.7m represented a sharp improvement on an outflow of $1.1m at this stage last year, buoyed by tighter working capital management and fewer debt impairments. The sale of two legacy aircraft accounted for $4.2m of the sharp reduction in net borrowings from $19.4m at the start of the year to $14.3m, and prompted analyst John Cummins at broking house WH Ireland to slash his year-end debt estimate by a third to $8.2m, in line with expectations of Gama delivering a 28 per cent rise in full-year pre-tax profits to $17.5m to produce EPS of 32.9¢, or about 26p. Mr Cummins notes that Gama could move to a net cash position by the end of 2018, auguring well for prospects of a hike on last year's dividend of 2.6p a share.

So, having maintained my buy advice all year, and highlighted the trading opportunity ahead of the half-year results when Gama's share price was pressurising the 250p key resistance level ('Value opportunities', 19 July 2017), I have every reason to maintain my bullish stance with the shares priced on a 40 per cent earnings discount to peers. In fact, I am raising my target price from 300p to 325p. Buy.

MORE ONLINE

Simon has published the following articles since the start of last week:

- **Kromek:** Buy at 26.5p, target 34p ('Repeat buying opportunities', 29 Aug 2017).
- **Bango:** Buy 225p, target 300p ('Repeat buying opportunities', 29 Aug 2017).
- **Satellite Solutions Worldwide:** Buy at 7.25p, target 10.5p ('Repeat buying opportunities', 29 Aug 2017).
- **Record:** Buy at 46p, new target 60p ('Repeat buying opportunities', 29 Aug 2017).
- **PV Crystalox Solar:** Hold at 22p ahead of September's ICC ruling ('Balancing risk and reward', 30 Aug 2017).
- **Chariot Oil & Gas:** Run profits at 10.25p ('Balancing risk and reward', 30 Aug 2017).
- **BATM Advanced Communications:** Buy at 18p ('Balancing risk and reward', 30 Aug 2017).
- **Cohort:** Buy at 390p, target 450p ('Seeking value', 4 Sep 2017).
- **Marwyn Value Investors:** Buy at 170p, new target 190p to 200p ('Seeking value', 4 Sep 2017).

MR BEARBULL



The incentive is all

Bad incentives can destroy good companies, as Provident Financial has come close to showing

Hiring a poor soul and labelling him or her a 'customer experience manager' is likely to prompt hoots of derision all round. No one can look friends or strangers in the eye and say "I am a customer experience manager" and expect to be taken seriously, least of all in the grittier parts of northern England. Yet that's precisely what consumer credit lender **Provident Financial (PFG)** did. Its bosses hired 2,500 customer experience managers and were then gobsmacked when their plan to transform the group's consumer credit division, whose typical customers are the hard-pressed barely employed, went down as well as black pudding at the annual meeting of the Vegan Society.

Actually, the problem was not just that the Provvy hired 2,500 folk and gave them a silly job title. Simultaneously, the bosses of the Bradford-based lender decided that the business model its home-credit operation had used since the late 19th century needed a radical shake-up. So about 10,000 self-employed agents – mostly former customers working for pin money – were told "thanks, but you won't be needed much longer because you're being replaced by customer experience managers". Then – and here's the really stupid bit – the Provvy's bosses imagined that during the transition those agents would continue working normally, doing their weekly rounds, knocking on doors, collecting the loan instalments.

For Provident, the reality was as grimy as many of the streets on which it does business. Agents gave up on the job and weekly collections, which normally run at about 90 per cent of the money due, dropped to 57 per cent in the summer. As a result, Provident dished out a brutal profit warning. For 2017, the consumer credit division, which made £115m pre-tax profit in 2016, will dive into losses of maybe £120m, with £20m of one-off costs in addition. For good measure, the dividend for 2017, the interim part of which was announced in August, has been axed.

Provvy's bosses would surely have done better if they had paid attention to Charlie Munger, Warren Buffett's nonagenarian sidekick at the enormous US conglomerate **Berkshire Hathaway (US:BRK.B)**. Mr Munger is convinced that what matters most in business, if not in all human affairs, is incentives.

But incentives work both ways – give people good incentives and they will work well, but give them perverse incentives, and they will behave perversely. The challenge is often knowing how to frame the incentive.

Mr Munger is fond of quoting the example of **FedEx (US:FDX)**, the Memphis-based global courier famed for its overnight shipping service. At the heart of FedEx's promise of next-day delivery is the ability to load up planes quickly so that they will meet their slot. The problem was that, no matter what FedEx's bosses did, the night shift would always overrun. Eventually, after going through the gamut of bonuses, pleas, threats, you name it – all of which failed – FedEx chanced on the happy solution. Rather than pay employees by the hour, which created the perverse incentive to eke out a task, it paid them by the shift and, when the plane was loaded and the work done, they could go home. Instantly, problem solved.

'Give people perverse incentives, and they will behave perversely'

Still in the courier business, but this time closer both to home and to Provident Financial's problem, there was an infamous episode of perverse incentives created at courier company City Link while it was owned by **Rentokil Initial (RTO)**. City Link had been built up as a franchise operation in which a national network of agents linked up a disjointed parcel service run by British Rail. In 2005, Rentokil decided it wanted to buy in the franchises prior to expanding the operation. In effect, that gave franchisees the incentive both to be bolshy and to do sweet f.a. for the following 18 months. City Link was never the same again and was eventually sold to a private equity firm that oh-so-kindly put it into administration late on Christmas Eve 2014.

Which is not to imply that a similar fate awaits the Provvy's consumer credit division. But it's not as though Provident Financial's misery ends there. It also faces regulatory threats at Vanquis Bank, its fastest growing part, which provides credit cards for borrowers with poor credit scores. The Financial Conduct Authority is investigating Vanquis's 'repayment option plan', which is effectively insurance against late payment and the worry must be that the product came with predatory pricing. Most likely, incentives were at work there, too.

Whether Provident Financial's sorry state provides an incentive to buy its shares is also a thought. It's easy to come up with that notion. After all, we know of the stock market's instinct to overreact and here are shares that, at 858p, are 74 per cent below their 12-month high. And the company's equity is now valued at barely seven times average net profits for the past six years.

That suggests Provident's bosses won't have to get too much right for the stock to be cheap in the long run. The key factor may be the incentives that tie customers to the Provvy. In personal finance, the bore of switching is often an incentive to stay with a provider, yet many of the Provvy's typical customers don't even have the luxury of choice. That might add up to a powerful business franchise but, first, those customer experience managers may have to patch up some goodwill. Let's hope they have the right incentives despite that risible job title.

Mr Bearbull's column has appeared since the 1950s. It aims to help readers manage their investment portfolios. email: bearbull@ft.com

THE TRADER



Vexed about the Vix

Does it really help?

How many more times will we be forced to hear platitudes and meaningless mantras about markets? That they hate uncertainty; this creates volatility; sharp moves are not good for investors; that we need a level playing field. Stop, think. Uncertainty is one of life's perennials. I don't know if I'll be run over by a bus as I leave the office.

'Investors have doubled the amount (to $2.5bn) allocated to 'inverse' Vix Exchange Traded Products. They believe the US S&P 500 index will settle down and the so-called 'fear gauge' will drop'

No volatility means a lack of opportunity in business, career prospects and life. As James Goldsmith famously said, "when you marry your mistress you create a vacancy". As for the playing field, as a trader I believe I have an edge, just as stockpickers believe they have one too.

What is interesting is that, as reported recently by the *Financial Times*, investors have doubled the amount (to $2.5bn) allocated to 'inverse' Vix exchange traded products. They believe the US S&P 500 index will settle down and that the so-called 'fear gauge' will drop.

The Vix index, originally developed by Menachem Brenner and Dan Galai in 1986, was launched as a futures contract on the Chicago Board Options Exchange in 2004; options on this future were introduced in 2006. It measures the implied volatility of a series of options on the expected annualised change in the S&P futures with a one-month time horizon. Robert Whaley computed this series retrospectively to 1986 and the record low was 8.89 per cent in 1993. We have matched this for the first time this year – explaining the rise in popularity of the inverse Vix funds.

Deutsche Börse, in conjunction with Goldman Sachs, developed the VSTOXX index which measures the volatility of the Euro STOXX top 50 shares in the euro-zone. The options are traded on the Eurex exchange and again have a rolling 30-day expiry. Look at the chart below and you can see that the volatility here is quite a bit higher than that of the S&P. This does not necessarily mean the shares themselves are more volatile; it means that those selling the options are able to charge more for the privilege of owning this insurance product.

The FTSE 100 index also has a one-month implied volatility measure called VFTSE. While volatility has on occasion been lower than the S&P's, what is striking is how expectations regularly double and halve.

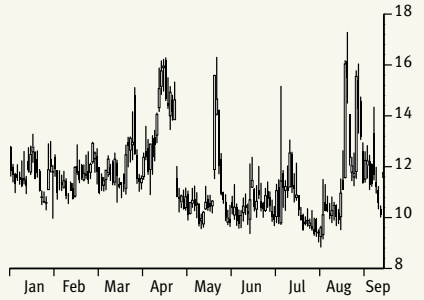
The final chart is the implied volatility of 30-day at-the-money options on the euro against the US dollar. Generally, foreign exchange volatility – both implied and observed (also called historical) – tends to be lower than that of equity indices. It's due to a mix of an ultra-competitive market and an instrument that's less flighty.

As those writing options know, it's like 'picking up nickels in front of a steamroller'. If you charge too little the chance of getting wiped out when the claims start coming in is high. A black swan event cannot be ruled out and the result is catastrophe. Conversely, buying options may give one a false sense of security and recurring expenses quickly eat into potential profits.

And for some, equity volatility options provide no adequate cover. This is becoming more of an issue as investors are warned against over-diversification and encouraged to hold between 10 and 20 core holdings. Unlucky, if one of those had been the UK's Provident Financial, which dropped 66 per cent in a day.

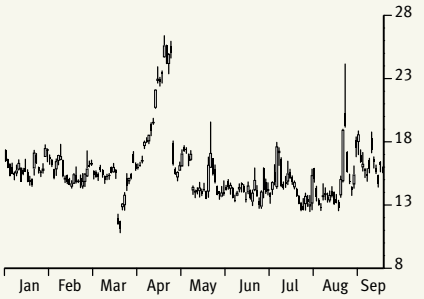
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S&P 500 Vix



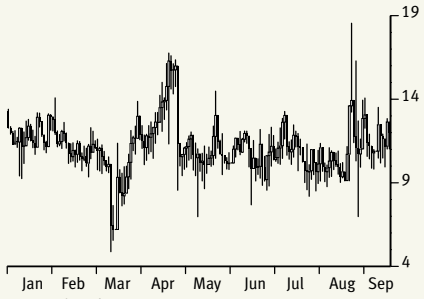
Source: Bloomberg

Eurostoxx 50 volatility



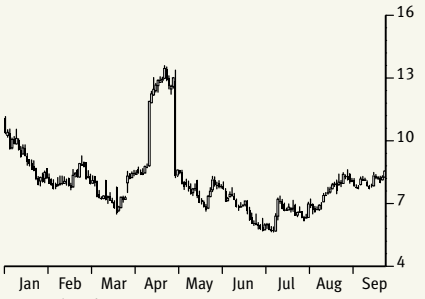
Source: Bloomberg

FTSE 100 volatility



Source: Bloomberg

Euro/US dollar volatility



Source: Bloomberg

FIXED?

UK-listed banks may have improved their capital adequacy, but a series of provisions, low rates and an uncertain credit environment pose a threat to their recovery. **Emma Powell** reports



One of the defining features of the response to the financial crisis by the UK's major banks was the desire to simplify their operations. Considering the circumstances leading up to the 2007 crisis, they had good reason. Ferocious growth in securitisation, slack capital adequacy controls and deregulation during the prior two decades had fuelled the rapid expansion of banks. In an increasingly internationalised financial system, setting up offices across the globe to grow the client base even further made sense.

Since the fallout a decade ago, the drive for simplification has been twofold. At a basic level, operating costs are the only lever banks can directly control. The misconduct costs and challengingly-low interest rates that have followed the financial crisis have necessitated a reduction in operating costs. More importantly, stricter capital requirements under Basel III regulations – in addition to impairments for bad debt – have pushed banks towards lower-risk business models.

The most pronounced consequence of this for many of the banking heavyweights has been a rapid downsizing of their investment banking operations. The requirement to hold more capital for owning riskier assets has taken away some of the attraction of investment banking – just one reason that reducing risk-weighted assets (RWAs) has been at the forefront of all the UK-listed banking majors' recovery strategies. The Prudential Regulation Authority's ring-fencing rules, requiring banks to separate retail money from riskier investment banking activity, have also contributed to the shift.

At **Lloyds Banking (LLOY)** and **Royal Bank of Scotland (RBS)**, the reduction in investment banking and the move towards lower-risk activities has been most pronounced. Lloyds has focused on UK retail and commercial banking, the former of which accounted for more than two-thirds of its loan book at the end of June. Admittedly, it does carry out activities including currency hedging and asset securitisation. However, it doesn't do takeover advice, equity capital markets or stock trading. Just 3 per cent of its loans and advances will sit within its non-ringfenced bank, Lloyds Bank Corporate Markets.

Similarly, RBS has focused on retail banking, after being burnt by years of overreaching acquisitions. That's not to mention the fact that asset disposals were a condition of its £45bn state bailout. Its personal and banking business now accounts for 42 per cent of its net loans at the end of June. Meanwhile, NatWest Markets had net loans of £17.7bn, equivalent to just 5 per cent of its total loan book.

In terms of risk reduction, focusing on retail banking has borne fruit. Since 2014, when capital requirements under the Basel III rules came into effect, Lloyds has reduced its risk-weighted assets by 15 per cent to £218bn at the end of June. During the same period RBS has reduced its RWAs by 45 per cent to £215bn. Of these, £27bn were RWAs related to its 'bad bank' Capital Resolution – a 43 per cent reduction since 2014. That's a bigger reduction in its run-off division than expected – management is now flagging RWAs for the end of the year to be at the lower end of its £15bn to £20bn target range.

As a result, the common tier one equity ratio – of equity as a proportion of RWAs – at both banks has improved (see table). However, that's also where the similarities between the two retail-focused banks end. Where Lloyds has rebuilt its capital position to a level substantial enough to warrant the re-commencement of dividend payments, RBS's position is more fragile. RBS has been mired in litigation and conduct disputes, including its 2008 rights issue, for which it has taken sizeable provisions. The bank failed the Bank of England's most recent stress test, which modelled a UK and global recession. Under the scenario its core capital ratio declined to 5.5 per cent, below a hurdle rate of 6.6 per cent, even after including debt that could be converted into equity. It was forced to submit a revised capital plan to the regulator and issue £2bn-worth of A1 securities. While the bank has settled some of its litigation issues, it is still under investigation by the US Department of Justice over alleged mis-selling of mortgage-backed securities during the run-up to the financial crisis. The bank has already taken a £3.1bn provision for this in 2016, but there could be more to come and eat into the book value. The UK government has also refused to sell down any more of its stake until the matter is resolved.

How the banks compare

	Share price (p)	Leverage (Tangible assets/equity)	CET1 ratio (%)	Book value	EPS (p)	Dividend per share (p)
Barclays	190	23.3	13.1	0.7	7.1	1
HSBC	748	14.3	14.7	1.4	35¢	20¢
Lloyds	64	21	14	1.1	2	1
RBS	250	17.8	14.8	0.8	7.9	0
Standard Chartered	762	14.1	13.8	0.8	29.5	0

Source: Companies, at 30 June 2017

'The requirement to hold more capital for owning riskier assets has taken away some of the attraction of investment banking'

Barclays (BARC) has kept a foot in both camps, retaining its investment banking operations, albeit in a downsized guise. Crucially, the bank has simplified its operations considerably. Following the sale of its African operations – for which it took a £1.1bn loss – and Egypt business during the first half of this year, losses associated with its non-core division reduced by around two-thirds. It also helped lift its core tier one equity ratio to 13.1 per cent, from 12.4 per cent in the previous year – within management's target range. However, like Lloyds, provisions for payment protection insurance continue to be a thorn in the bank's side. It had £700m in provisions during the first half. However, the Financial Conduct Authority has set a deadline of 29 August 2019 for new payment protection insurance (PPI) claims, which should draw a line under what's been an incredibly costly hindrance to UK banks' bottom lines.

Focusing on UK retail banking may help reduce a bank's risk profile, but it has also presented problems in generating sufficient earnings to restore profitability. Against a backdrop of ultra-low UK interest rates, maintaining a decent net interest margin is a tough job. UK-listed banks have experienced downward pressure on their net interest margins and the return they can make on their equity during recent years. Admittedly, a lower cost of funding did provide some fillip to margins for most lenders during the first six months of the year.

Asia-focused banks **HSBC (HSBA)** and **Standard** ▶

15%
SINCE 2014, LLOYDS HAS REDUCED ITS RISK-WEIGHTED ASSETS BY 15 PER CENT TO £218BN AT THE END OF JUNE

▶ **Chartered (STAN)** have not escaped the pressure of low rates. In November 2015 Standard Chartered chief executive Bill Winters scrapped the final dividend and in August last year pushed out its target of achieving an 8 per cent return on equity by 2018. However, despite failing to reinstate the dividend at the midpoint of the year, the bank has made progress on its capital adequacy. The bank has focused on affluent retail banking customers, instead of investment banking, and has sold off or reformed capital-intensive businesses.

This strategy has borne fruit. Risk-weighted assets declined 17 per cent to $271bn (£209bn) during the two years to the end of June. It has also taken $2.9bn of the $3bn restructuring charges expected once the overhaul is complete. A recovery in emerging markets sentiment and commodities prices has also meant it has left behind the huge impairments it had been forced to take on commodities loans turned sour during 2015 and 2016. Its common tier one capital stood at 13.8 per cent at the end of June, up from 11.5 per cent two years earlier.

HSBC has not entirely escaped the pressure of low rates, either – last August it scrapped the timetable for hitting its 10 per cent return on equity target by the end of this year. Nevertheless, as we detailed in our recent 'Income Majors' feature (IC, 14 July 2017), HSBC remains the capital king of the UK-listed banks. It has consistently delivered the highest return on equity of all the banks, partly by continuing to participate in higher-risk investment banking activities. That's not to say it hasn't been reducing its risk profile during the past two years. It has been gradually selling down the investment bank's legacy credit and long-dated rates books, as well as reducing its capital financing activities and redeploying capital away from Turkey and Brazil.

In 2015 chief executive Stuart Gulliver set a target of reducing the bank's risk-weighted assets by around a quarter – or $290bn. Last year alone it cut risk-weighted assets by $143bn. By the end of June the bank's risk-weighted assets stood at $876bn, meaning it had exceeded the 2015 target. HSBC's core tier one equity ratio stands at 14.7 per cent, comfortably above management's 12 to 13 per cent target range. At the end of the year the ratio is forecast to be 14 per cent, rising to 14.1 per cent the following year. As well as a reduction in risk, the bank has benefited from an improvement in the quality of revenue, primarily because of its 'Asia pivot'. The region's rising middle class and maturing savings and wealth management markets are what HSBC has pinned its hopes on for driving growth. That also leaves the banking group exposed to the waxing and waning of emerging markets fortunes.

'HSBC remains the capital king of the UK-listed banks. It has consistently delivered the highest return on equity of all the banks'

Perhaps the largest threat on the horizon for UK banks is a potential reduction in demand for consumer credit. On that front, Lloyds is the most exposed. Its acquisition of HBOS in 2010 granted it the largest share of the UK mortgage market, where it has already suffered a contraction in margins due to competitive pressures. Its purchase of Bank of America's credit business, MBNA, earlier this year has increased its vulnerability to a reduction in credit quality. For now, Lloyds' status as a very well-capitalised bank gives us confidence in its ability to withstand moderate pressure here.



How stressful are stress tests?

As part of the central bank's efforts to ensure the UK's major lenders had enough capital backing their loan books, in 2013 the financial policy committee recommended regular stress testing be carried out on the banking system. Stress tests are conducted annually on what the Bank of England calls the UK's 'systemically-important' lenders: Barclays, HSBC, Lloyds, Nationwide, Royal Bank of Scotland and Standard Chartered.

A stress test is meant to examine the potential impact of a hypothetical adverse situation on banks' balance sheets, not just their ability to withstand such shocks, but also to support the wider economy if these stresses materialise. The severity of the scenario applied depends on the point of the financial cycle at the time, rising as risks do. As the Bank of England states: "The scenario might therefore be most severe during a period of exuberance — for example, when credit and asset prices are growing rapidly and risk premia are compressed." The idea is that it runs counter to the level of risk-taking at the time.

The results of the first stress test were published in December 2014, designed to assess the risk of high household indebtedness. The stress scenario featured an initial shock to productivity, which led to an "abrupt" reassessment of the prospects for the UK economy. Under the scenario this was followed by a sharp depreciation of sterling and a rise in inflationary pressures. Monetary policy was assumed to tighten in response to these inflationary pressures, with the base rate rising by about 4 percentage points. The downturn in economic activity led to a 12 per cent rise in unemployment and falls in a range of asset prices, including a 35 per cent decline in house prices. Since then stress scenarios have included a downturn in emerging markets, and in 2016 a UK and global recession and additional pressure from misconduct costs.

From this year the Bank of England will carry out two tests – an annual cyclical scenario and a biennial scenario, exploring the impact of long-term risks to the banking sector's health. For 2017, the cyclical scenario will model a global and UK recession – wiping 4.7 per cent off UK GDP – a 4 per cent increase in interest rates and a 33 per cent decline in UK house prices. The long-term exploratory scenario will examine the effects of weak growth and falling world trade, a weak bank rate and rising competition within the banking sector.

However, this method of assessing the capital adequacy of bank balance sheets is not without its critics. One of the most rigorous interrogations of the system was carried out by Durham University's Professor Kevin Dowd and published by economic think-tank the Adam Smith Institute. He argues that the annual stress test is reliant on a single, insufficiently stressful adverse scenario, with "extremely low pass standards and inadequate metrics". He also disputes the use of risk-weighted assets to adequately assess a bank's leverage ratio. Instead, the Bank of England should assess leverage ratios by calculating a bank's total equity as a proportion of its total assets, Professor Dowd argues.

NORTHERN ROCK: 10 YEARS ON

The collapse of Northern Rock – 10 years ago this week – was a small part of a global malaise whose effects linger. **Philip Ryland** explains

The queues that formed on Britain's high streets on the morning of Friday 14 September 2007 were orderly but subdued. If there was tension, it was not the anticipation of success – the feeling that comes from, say, being in the front of the queue for Wimbledon's centre court. Rather, it was the tension of entitlement that might be denied; the worry of how to cope with the anger that would well up with the injustice of being told you could not have what was yours.

As it happened, those who queued – across the country there were at least a few thousand – need not have worried. All got what they wanted – their savings back from Northern Rock, the UK's fastest-growing bank that was experiencing the first run on a British bank since the 19th century.

Ten years on, those scenes outside most of Northern Rock's 76 branches still seem slightly surreal. A run on a bank was something that happened in inflation-ridden Argentina or in the dustbowl towns of mid-west America in the 1930s; certainly not in the towns of middle England in the 2000s. Was it that Britain's financially naive Mr and Mrs Average had panicked when rumours of Northern Rock's difficulties came over the BBC news that morning? Or was it that the sophisticates – the ones who were supposed to know a CDO from a CDS and who had the pinstripes and the cuff links to prove it – had messed up big time?

More the latter than the former. By mid September 2007, Northern Rock had been in the doo-doo for some while and long before its bosses realised it. In the summer, they still imagined they were in clover. In late July, they released first-half results for 2007. These claimed a 27 per cent rise in underlying profit, a 24 per cent return on equity and – maybe most amazing in the light of what was developing – promised a 30 per cent rise in the dividend, made possible because Northern Rock had convinced its regulators that it needed to hold less capital. Had they paid more attention to what was happening in the US, Northern Rock's bosses might have been more cautious.

In the eight years to 2006, US house prices had risen on average by 67 per cent and home ownership had reached an all-time high of almost 70 per cent of households. Simultaneously, mortgage indebtedness had almost doubled to $10.5 trillion (£8.1 trillion). Americans had taken advantage of this by extracting over $1 trillion in cash from their homes via second mortgages, including $330bn in 2006 alone.



Northern Rock customers queue to gain access to the Moorgate branch in London, on Monday 17 September 17 2007

'The first clear pointer that non-payments were infecting Wall Street's wholesale money markets on which Northern Rock depended for its funding appeared in June 2007'

But by early 2007 it was becoming clear that house prices had peaked. Despite this, the machine that kept generating new mortgages, packaging them into mortgage-backed securities then parcelling those of the lowest quality into collateralised debt obligations (CDOs) remained on full throttle. However, the lack of stability at the base – the point where borrowers actually made their mortgage payments (or, increasingly, didn't make them) – was beginning to show.

The first clear pointer that non-payments were infecting Wall Street's wholesale money markets on which Northern Rock depended for its funding appeared in June. Bear Stearns, a New York investment bank, froze redemptions on two in-house hedge funds that bet on the value of CDOs. In response, Merrill Lynch, another investment bank that had lent to the funds, seized $850m-worth (£655.18m) of CDOs that had been ▶

$10.5 trn
THE AMOUNT OF MORTGAGE DEBT IN THE US IN 2006

▶ posted as collateral and attempted to auction them. It only found buyers for $180m.

In July, it got worse. IKB Deutsche Industriebank, a small German lender, was using an off-balance-sheet vehicle, Rhineland, to buy CDOs, which it funded by selling commercial paper (essentially, post-dated cheques) in the money markets. New York's investment banks had happily stuffed Rhineland full of CDOs but were becoming increasingly loathe to market its commercial paper. IKB felt the need to reassure its investors that ratings downgrades of mortgage-backed securities would have only a limited impact on its business; that was on 20 July, five days before Northern Rock announced its happy-go-lucky half-year results. But no one believed IKB. Within days, Goldman Sachs, Wall Street's most powerful investment bank, told IKB it would no longer touch Rhineland paper. In response, on 27 July Deutsche Bank, IKB's major lender, cut off its credit lines to IKB. Without a bail-out from its major shareholder, IKB was as good as dead.

The moral of IKB was the same as whenever a bank goes under. It is killed by what happens on the liabilities side of its balance sheet regardless of the quality of the investments – good or bad – on the assets side. It's what can happen to any business that borrows short to lend long. Whether or not toxic mortgages lurked somewhere in Rhineland's assets or whether the assets were pure gold was neither here nor there. Investors didn't want to stop to find out. They had lost their faith in mortgage-backed securities. They weren't going near them. So they left Rhineland high and dry without funding. As a dress rehearsal for what the markets would do to Northern Rock a few weeks later, IKB's near-death experience was spot on.

And by August even Northern Rock's bosses could see it coming. Put simply, the bank was running out of money. Its previous capital raising had been in May when it tapped the US wholesale markets by selling bundles of securitised mortgages. The next fund-raising was due in September, but it was obvious it wouldn't happen.

In mid-August, Northern Rock's bosses confessed the company's troubles to its chief regulator, the Financial Services Authority (which no longer exists). The question arose whether it would need emergency funding from the Bank of England, acting in its role as 'lender of last resort'. Yet that possibility floundered because at that time the Bank of England's responsibility for the stability of the UK's financial system was not clear cut and the bank was being run by a governor – Mervyn King – who was a monetary economist from academia with no experience of banking or the City.

Mr King's response was that of the theoretician, fearful of the 'moral hazard' that could spread through the system by lending to a bank that had taken too many risks. It would be better if Northern Rock could fall into the arms of a bigger bank.

In desperation, Northern Rock hawked itself around and came close to finding a buyer in the shape of Lloyds TSB (now Lloyds Banking). But Lloyds would only deal if Northern Rock were lent £30bn by the Bank of England. The UK's financial regulators ruled that out as "inappropriate to help finance a bid by one bank for another". Yet the ironic consequence was that the Bank of England had no choice but to give Northern Rock the emergency funding it had been so reluctant to offer.

Even that was messed up. News of the impending rescue leaked out so the government dashed out a statement on 14 September whose meaning Mr and Mrs Average mistook. Rather than grasping that Northern Rock had been – belatedly – saved by the Bank of England's support, they thought it meant the savings bank was in real trouble. It did not help that, back then, the UK's deposit insurance scheme only guaranteed 90 per cent of the first £35,000 of a deposit account. Mr and Mrs Average didn't wait to find out more. They were on that bus to the high street. To join the queue.

The real significance of Northern Rock

The tale of Northern Rock is a dramatic story in its own right. It's the tale of a little building society that became a big bank, whose shares were in the FTSE 100 index, and a power house in its native north-east of England. It's the story of dramatic growth based on an innovative business model that relegated the tedious and expensive necessity of running a branch network to a subsidiary role. Its growth was such that, just as Northern Rock was about to crash, it was funding almost one in every five new mortgages arranged in the UK. But Northern Rock is also a tale of hubris; of a bank being run by people who weren't as clever as they thought, who did not really understand what they were doing, who had conveniently ignored the warning signs that had pressed up against their operations three years earlier and who were legged over by the most brutal market that Anglo-Saxon capitalism offers – the New York fixed-interest market.

However, the real significance of Northern Rock is that it is emblematic of much that was wrong with the developed world's financial systems, the consequences of which are still with us today. So there is a bigger question: what is the explanation of the financial crisis that took Northern Rock as its first victim but which proceeded to find bigger prey, not stopping at banks but gorging itself on almost every aspect of the developed world's economic systems? Answer that and we can understand many anomalies that are both baffling and dangerous: why growth remains so elusive; why interest rates remain so low; why capital assets have performed so well.

In a way, there are two explanations. There is the academic explanation and the popular one; the intellectual explanation and the one with a human face. Of course, that's a simplification and, besides, the two overlap. But let's start with the popular explanation.

This focuses firmly on the US housing market in the early 2000s – how home ownership expanded, how house prices rose and, most of all, how purchases were financed. It is the story of how a laudable aim – raising the level of home ownership, especially for the poor – was achieved by the brilliance of financial innovation – the process of securitising loans – but became corrupted by greed and human frailty.

The corruption took the form of financial regulators failing – and even conniving – in the creation of

'The real significance of Northern Rock is that it is emblematic of much that was wrong with the developed world's financial systems, the consequences of which are still with us today'

mortgage-backed securities that were supposedly low risk but which, actually, few people either studied or understood. It took the form of collapsing standards for mortgage lending such that, when the US housing bubble had inflated to its fullest extent, two-thirds of loans made by the country's two biggest mortgage lenders were so-called 'liar loans' – ie, they required little or nothing in the way of back-up documentation. And most dramatically it took the form of a mad, bad and dangerous securitisation machine, which generated a momentum of its own as it created collateralised debt obligations (CDOs), followed by CDOs squared (CDOs that invested in other CDOs) and then synthetic CDOs (CDOs that bet on the performance of CDOs).



Michael Lewis's book, *The Big Short*, made into a film of the same name (pictured), reminds us that financial markets have people at their centre

The popular explanation has its fullest and arguably its best account in an unlikely source – the official US government report into the crisis, called – appropriately enough – the Financial Crisis Inquiry Report. Published in 2011, the report is fast-paced and reads more like a financial thriller than the deliberations of an eight-man commission chaired by Phil Angelides, a Democrat politician from California. It rubbishes the notion that the crisis was unavoidable and incapable of being predicted – "the crisis was the result of human action and inaction, not of Mother Nature or computer models gone haywire", it says.

Its genesis was aided by "more than 30 years of deregulation (that had) stripped away key safeguards which could have helped avoid catastrophe". It was abetted by "dramatic failures in corporate governance and risk management" where "too big to fail meant too big to manage". And it was stimulated by a "systematic breakdown in accountability and ethics". The report reserves special criticism for "stunning instances of governance breakdown and irresponsibility". Those include the conduct of the bosses of AIG (American International Group), prior to the crisis the world's biggest insurance company. AIG was colloquially known as 'the golden goose of Wall Street' thanks to its willingness to underwrite 'credit default swaps' (CDS), derivatives that paid out if CDOs went into default. Yet it turned out that its bosses had little knowledge of the $79bn exposure to this risk on its books.

Similarly reckless was the conduct of Wall Street's leading investment banks, which operated with "extraordinarily thin capital" and so much leverage that "less than a 3 per cent drop in net asset values could wipe out a firm". In the case of two firms – Bear Stearns and Lehman Brothers – that's pretty much what happened. However, Bear Stearns was fortunate enough to collapse first. That meant that, after a fashion, it was rescued. Lehman was not so lucky. It failed in September 2008 and by then the US central bank had decided that saving Bear Stearns had actually been a bad move – it stimulated the moral hazard that had so exercised the Bank of England's Mervyn King a year earlier. Therefore, reckoned Ben Bernanke, Mr King's friend and counterpart at the US central bank, Lehman should be allowed to fail. Bad move. Sorting out the 900,000 derivatives contracts on Lehman's books was the sand in the engine – the global financial system ground to a halt.

Not that it should have been too much of a surprise that Mr Bernanke made such a bad call. The commission reckoned that "senior public officials did not recognise that a bursting of the bubble could threaten the entire financial system". Through the summer of 2007 both Mr Bernanke and the Treasury Secretary, Henry Paulson – formerly the boss of Goldman Sachs – "offered public assurances that the turmoil in the subprime mortgage markets would be contained". Then their decision to rescue Bear Stearns but to let Lehman sink "increased uncertainty and panic in the market".

Yet there were those who spotted what was coming – and made shed-loads of money. To meet them, you need to read Michael Lewis's brilliant book, *The Big Short*. There, you will encounter the likes of Michael Burry, Steve Eisman, Gregg Lippmann and the kids from Cornwall Capital.

The big short

Michael Burry was the boy with the glass eye and Asperger syndrome who became a neurologist but was obsessed by numbers and the stock market. He quit medicine to become a full-time investor and could not believe the madness he found in the US housing market. He pretty well invented credit default swaps – a way of betting on the failure of CDOs – to profit from the insanity.

Steve Eisman, a hedge fund manager for JP Morgan Stanley, was deeply disposed to find tragedy in all he saw following the sudden death of his baby son. Thus the potential tragedy within the sub-prime housing boom came easily to him. He met and somehow teamed up with his antithesis, Gregg Lippmann, a Deutsche Bank salesman who, according to *The Big Short*, "was a walking embodiment of the bond market, which is to say that he was put on Earth to screw the customer".

Then there was Cornwall Capital, a hedge-fund start-up run from an artist's studio in New York's Greenwich Village. If Goldman Sachs were The Rolling Stones of investment banks, Cornwall Capital was the garage band that made even The Ramones sound accomplished. Yet – relative to their size – they profited the most because they were predisposed to make the most outrageous bets. In the crisis, they bet not against the lowest quality CDOs, which were likely to default even if the market just got shaky, but against the triple-A rated securities that were supposed to be able to withstand a flood. As such, they captured returns where risk was most badly priced.

The great merit of both The Financial Crisis Inquiry and *The Big Short* is that they remind us that financial markets – like all economic systems – have people at their centre. Thus the crisis was caused by people, chiefly those who responded to bad incentives framed by other people.

As for the intellectual explanation, this deals with the global forces that were at work in the early 2000s and which, to an unnerving extent, are still with us today. In that sense, these forces are both the cause of the crisis and the reason that its consequences remain so difficult to shake off.

Explaining them begins with a "conundrum"; at least, that's the famous word with which Alan ▶

▶ Greenspan, the head of the US central bank, described the behaviour of the world's bond markets in early 2005. What especially puzzled Mr Greenspan was that his central bank, the Federal Reserve, had just raised short-term interest rates yet long-term rates continued to fall. This was perverse – long-term rates should have been rising to reflect the move in short-term ones. And this wasn't just happening in the US. Throughout the developed world, the yield curve – the pattern of interest rates across the spectrum of maturities – was inverted (ie, long rates were lower than short ones).

As to the cause, Ben Bernanke, then a board member at the 'Fed', came up with the theory of a savings glut. This idea focused on the way some nations were saving hard. The proof was that they were running big surpluses on their current account balance of payments, which indicated that domestic demand was insufficient to absorb domestic output. Therefore there was nowhere for the surplus money to go but to be saved.

The really odd feature was that many of these nations in surplus – and especially China – were still in their development phase when, according to conventional wisdom, they should have been running a trade deficit as they imported lots of goods and services to help propel their expanding economy. The explanation for their trade surpluses was to avoid the successive crises that developing nations got themselves into during the 1990s and early 2000s as they expanded too fast, ran up deficits, then found themselves prisoners of developed-world interest rates and financial markets.

This oddity – that poor nations were lending to rich ones – neatly explained Mr Greenspan's conundrum. But it had further, perverse, consequences. It meant that rich nations were able to – and, in a sense, had to – run current-account deficits, which also meant that they were able to – had to – borrow cheaply. That persuaded players of all sorts in the financial markets to behave with "irrational exuberance", to use a phrase that Mr Greenspan had coined a decade earlier in connection with the dot-com boom.

The irrationality was characterised by the response to falling interest rates. These signalled lower future returns, which should have told punters and investors to take less risk since such risks would be less well rewarded. Yet the punters did the opposite. As rates fell – and, implicitly, the reward for taking risks dropped with them – they responded by taking more risks, partly because it was so easy for them to do it. The raw material was abundant and cheap in the form of low-cost debt. So punters did what they have done throughout history when the going got intoxicating – they added leverage to their bets using other people's money. The hope – even the expectation – was that leverage would gear up returns from respectable to wonderful.

This would more easily be achieved in a world where regulations were fewer and innovation was greater. Happily, the trend towards less regulation had been a feature of financial markets since the early 1980s and reached its high-water mark in 1999 with the scrapping of the last remnants of the Glass-Steagall banking laws that had separated racy-and-risky investment banking from dull-but-worthy commercial banking. This released a wall of capital that could surge into sexier products than five-year fixed-interest loans.

Cue the innovation that would conjure up the products. Wall Street's tool of choice became 'securitisation', the process of bundling up lots of small loans into securities. These were then sold, chiefly to institutional investors who could use the interest they received, via the coupon on the securities, to match their own liabilities, usually the money they owed on insurance and pension policies.

At its core, securitisation was a brilliant idea. Not only did it meet the needs of investing institutions but it reached from Wall Street to the suburbs of middle America where it began by doing good. Since pretty well any form of consumer debt could be securitised, securitisation enabled consumers to get rid of their expensive unsecured debt – the loans that funded credit-card spending, buying a car, putting the kids through college – by swapping it for cheap debt that was secured on the collateral of their homes. In other words, they took out a second mortgage whose interest rates was less than half the rate on their consumer loans.

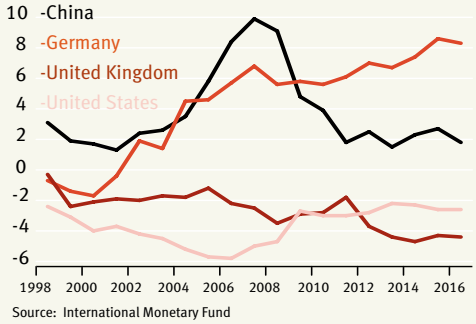
Then those mortgages were bundled into securities and sold to institutions. So far, so good. Almost needless to say, however, the process got out of hand. Egged on by salesmen responding to perverse incentives all the way from Wall Street to Main Street and emboldened by a cocktail of cheap debt and rising house prices, consumers took to mortgages that were used to punt on property prices.

As we know, that process wasn't confined to the US. An imitation of what was happening Stateside propelled Northern Rock into oblivion. It did almost the same to other former building societies, most notably HBOS and the Royal Bank of Scotland, which – driven by the ferociously ambitious Fred Goodwin – smashed into the pile-up of broken banks created by Lehman's crash.

As we also know, the factors that contributed to the financial crisis linger. As Chart 1 below shows, China's trade surplus remains substantial; although it has been overtaken by Germany's, both as a fraction of national output and, more important, by size. Simultaneously, the US and the UK remain in current-account deficit. This may not matter so long as enough foreign investors are willing to own US or UK government debt and/or invest in the US and the UK.

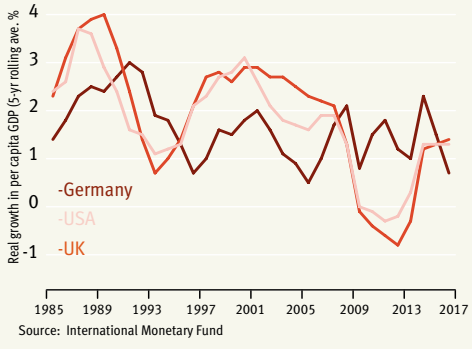
"The crisis was the result of human action and inaction, not of Mother Nature or computer models gone haywire"
Phil Angelides

Chart 1: In surplus and deficit



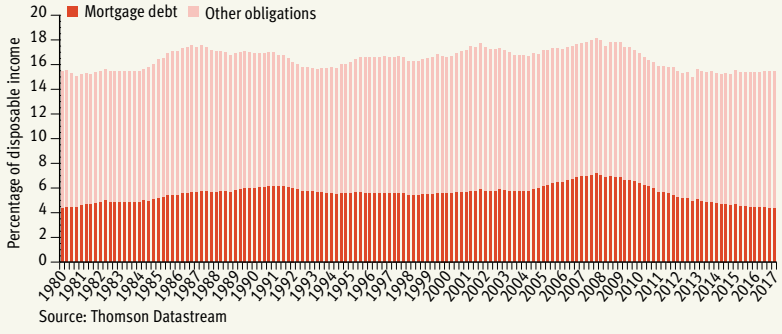
Source: International Monetary Fund

Chart 2: Still feeling poor



Source: International Monetary Fund

Chart 3: The indebted US consumer



Source: Thomson Datastream

Clearly both countries have advantages – the status as the world's reserve currency for the US dollar; smoothly functioning markets and well-defined property rights for the UK. Even so, it's not a happy state for either country. They are – as the governor of the Bank of England, Mark Carney warned (adapting a famous line from Tennessee Williams) – dependent on the kindness of strangers.

Meanwhile, it has taken exactly 10 years for employment levels in the US to return to where they were before the financial meltdown. About 8.5m jobs were lost by the time the recession reached its pit and – taking into account expansion of the US labourforce – it took the creation of 10m new jobs to make good the loss. That mark was reached in July, according to the Hamilton Project, a US think-tank.

Yet not all jobs are created equal. A disproportionate number of the new ones are low paid, a fact that is revealed in Chart 2, which shows real growth – ie, after deducting inflation – in per capita output for the US, the UK and Germany since 1985. The data are expressed as the five-year rolling average so as to emphasise the trend, which is downhill. True, it has bounced in 2014-16, but it is still below the growth rates of the 1990s, which themselves were heading downwards. Especially in the UK, where inflation is shifting upwards, consumers in the developed world continue to get poorer.

Michael Lewis addressed this issue in *The Big Short* with the rhetorical question: "How do you make people feel wealthy when wages are stagnant? You give them cheap loans." That response was at the heart of the financial crisis and it's still not far away today. Chart 3 shows that US consumers continue to fund debt obligations that are just one percentage point below their average for 1980-2016 – 15.5 per cent of disposable income compared with 16.5 per cent. That difference almost entirely comprises the drop in monthly mortgage payments. But it is a function of lower interest rates, not lower indebtedness. In other words, such stability as there is depends heavily on interest rates staying at rock bottom. Ten years on, those in the US and the UK have to pray that the savings glut does not run dry and that Chinese consumers remain happy to lend to them. Not a happy prospect.



The names that disappeared

Northern Rock
It was formed by the 1965 merger of Northern Counties Permanent Building Society and Rock Building Society. It was demutualised and listed and its shares were in the FTSE 100 index by 2000. It was rescued by the Bank of England on 14 September 2007 and nationalised on 22 February 2008. The savings bank was bought by Virgin Money in January 2012 and rebranded to Virgin in October 2012. The mortgage book remained in government ownership as Northern Rock (Asset Management), part of UK Asset Resolution. At end March 2017, the mortgage book was down to £8.6bn; £60bn-worth of mortgages have been offloaded since 2010; and it repaid government loans of £17bn. The outstanding government loans are £4.6bn.

HBOS
Formed from the 2001 merger of Bank of Scotland and Halifax. The Bank of Scotland was founded in 1695 and still has authority to print its own bank notes. Halifax, the UK's biggest building society for most of the 20th century, demutualised and listed in June 1997. Merger of the two formed "the fifth force in British banking". It was pushed into the arms of Lloyds TSB in January 2009 when the alternative was nationalisation; the government ended up owning 43 per cent of the enlarged Lloyds anyway. The HBOS name survives in a few residual entities, but Bank of Scotland and Halifax continue to trade as if nothing ever happened.

Bradford & Bingley
Formed by the 1964 merger of Bradford Equitable and Bingley Permanent building societies. It was demutualised in December 2000 and listed. Independence was untenable following the flop of a £400m rights issue in June 2008. The savings accounts and branch network was acquired by Santander in September 2008 and rebranded as Santander in January 2010. The mortgage book and wholesale-market liabilities were nationalised and became the other half of UK Asset Resolution. At March 2017, the mortgage book was down to £10.9bn following the agreed sale of £11.8bn portfolio of loans; therefore, outstanding loans from the government of £20.4bn are set to be substantially reduced.

Alliance & Leicester
Formed by the 1985 merger of Alliance Building Society and Leicester Building Society. It demutualised and listed in April 1997; almost immediately became a component of FTSE 100 index. It received £3bn line of credit from the Treasury in November 2007. In July 2008 it accepted a £1.3bn bid from Santander; it was rebranded in January 2010.

REFINING THE GROWTH STRATEGY

John Baron explains the changes to the Growth portfolio during August, after further strong outperformance year-to-date from both portfolios

After a quiet few months for the Growth portfolio in terms of activity, August saw a number of changes that perhaps serve to confirm some of the thinking behind the portfolio's asset allocation and thematic preferences as autumn approaches. At a time when there is much concern about the level of markets, this is also a useful moment to remind ourselves of some of the many growth opportunities that currently exist for the patient investor.

Opportunities

Investment opportunities abound when it comes to technology and biotechnology. In general, advances are introducing more and more solutions to problems and/or are lowering costs on a sustainable basis – and this is helping to create sector cycles that are more independent of the general economy. This is a golden age of innovation, in which the frontier of what was thought possible is advancing all the time. Our confidence in these developments is illustrated by the extent to which my website's other portfolios pursue these themes – and their reward for doing so.

And given improved technology is allowing easier and cheaper access to established practices and markets, smaller companies, in particular, should disproportionately benefit. Accordingly, **Edinburgh Worldwide (EWI)** was introduced to the portfolio during August. Speaking recently with Douglas Brodie, the lead manager, EWI pursues a global growth mandate from entrepreneurial companies, which are typically less than $5bn in size when bought, and has a high exposure to the technology, biotechnology and healthcare sectors.

This approach was adopted in 2014 when the company changed from being a mainstream global equity fund, since when performance has been very good. Douglas and his team are able to feed into Baillie Gifford's long-term global growth team, with a key theme being the search for companies trying to solve 'big' problems. Given this focus on disruptive technologies and EWI's size bias, the portfolio is well diversified – but, importantly, can retain successful companies as they grow, regardless of size.

This purchase was funded by top-slicing both **North American Income (NAIT)** and **International Biotechnology Trust (IBT)** – these sales are in part compensated by the fact that a significant element of EWI's exposure is invested in North America and in biotechnology, while IBT had enjoyed a strong run, which had seen the discount narrow considerably to around 4 per cent when sold.

> 'Given improved technology is allowing easier and cheaper access to established practices and markets, smaller companies, in particular, should disproportionately benefit'

In the same vein, I have also introduced **Allianz Technology Trust (ATT)** to the portfolio to increase sector exposure. ATT focuses on achieving capital growth from mostly quoted companies on a global basis, and has built an enviable track record. Speaking with Walter Price, the lead manager, his team benefits from being located near to Silicon Valley, where many of the world's leading technology companies are based. Indeed, around 80 per cent of ATT's exposure is in North America. Importantly, around 25 per cent of the portfolio is invested in smaller companies under $10bn in size.

Walter understands that investors are nervous given that the sector has performed well and that some valuations appear demanding. However, he believes valuations are more than supported by excellent growth in earnings – unlike the technology bubble in the late 1990s. Indeed, looking out to 2018, ATT's portfolio as a whole is on around 25 times earnings, but harbours earnings growth of 35-40 per cent. Meanwhile, the sector outlook is more positive than for many years, with many companies now correcting their previous underfunding of much-needed projects.

This purchase was funded by top-slicing both **JPMorgan Japan Smaller Companies (JPS)** and **TR Property (TRY)**. Both had enjoyed a strong run and discounts had narrowed somewhat – TRY's ▶

www.johnbaronportfolios.co.uk **reports on seven real investment trust portfolios as they achieve a range of strategies and yields up to 6.0 per cent.**



John's book explores the merits of investment trusts, the stepping stones to successful investing, and how to run and monitor a trust portfolio. Available from Amazon and other bookshops.

▶ being around 5 per cent when sold. Both remain excellent trusts, but taking profits is seldom the stepping stone to ruin – particularly when other opportunities exist.

Another sector that currently offers opportunities is the commodities sector, where sentiment remains depressed. While each commodity has its own narrative, sentiment generally trails fundamentals given the extent of cost-cutting and capacity reduction over recent years. This should change as economic growth gradually recovers and perceptions start to focus on a possible uptick in inflation.

In wishing to broadly maintain its commodity exposure, and because it is less constrained by income requirements, I have funded the introduction of **Riverstone Energy (RSE)** to the Growth portfolio by selling its holding in **City Natural Resources (CYN)**. RSE is a private equity company that invests exclusively in the global energy industry via a combination of conventional and unconventional oil and gas activities primarily in North America – shale being the largest exposure.

As such, the company is one of the few ways for UK investors to access the 'shale revolution', which is ongoing courtesy of technology, innovation and therefore falling costs. Speaking recently with the management, who have large shareholdings, all are energy 'lifers' who know the business well. Having been created in 2013, RSE's acquisition of assets has been well timed, and the company is now nearly fully invested.

It should be acknowledged that RSE's narrower focus may result in higher volatility when compared with CYN, given the latter's exposure to a broader range of commodities. RSE is therefore perhaps better suited to those portfolios that pursue a higher risk/reward remit, such as my Thematic portfolio, or are of the size and remit to accommodate smaller percentage holdings, such as the Growth portfolio.

Finally, during August I added to the portfolio's existing holding in **Templeton Emerging Markets (TEM)**. An explanation as to the merits of emerging markets in general was highlighted in a previous column ('Emerging returns', 5 May 2017). Meanwhile, TEM continues to outperform both its benchmark and peer group since Carlos Hardenberg became lead manager towards the end of 2015 – a fact not yet fully reflected in its discount of 13 per cent when bought.

A refocusing of the portfolio towards technology and consumer stocks, with each now accounting for around 30 per cent of NAV, is reaping rewards. The opportunities from e-commerce are considered particularly promising in the Far East, given that the technology is addressing a demand arising from the difference in shopping habits and use of shopping malls when compared with the West. There has also been a modest shift towards smaller companies.

Conclusion

Particularly at times of uncertainty, it is wise to reflect on mankind's proven ability to overcome problems and progress for the common good. Accordingly, portfolios will continue to benefit from patiently focusing on those companies that are solving problems, adding value and creating wealth over time – and from seeing volatility as an opportunity in itself.

John Baron waives his fee for this column in lieu of donations by Investors Chronicle to charities of his choice. As these are real portfolios, he has interests in all of the investments mentioned.

John Baron's Growth portfolio

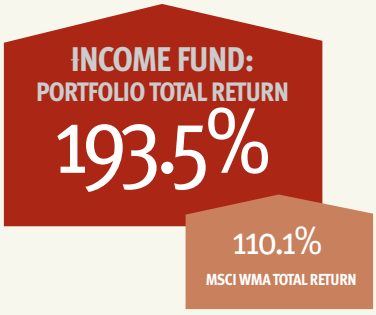
Bonds	
New City High Yield IT	6.5%
UK shares	
Finsbury Growth & Income IT	6.5%
Standard Life Equity Income Trust IT	6.0%
The Merchants Trust IT	5.0%
Chelverton Small Cos Div Trust IT	4.5%
Henderson Smaller Cos IT	4.5%
JPMorgan Mid Cap IT	3.5%
Oryx International Growth Fund IT	3.0%
International shares	
Monks IT	6.0%
Henderson Far East Income IT	5.0%
European Assets IT	4.0%
North American Income Trust IT	4.0%
Templeton Emerging Markets IT	4.0%
JPMorgan Japan Smaller Companies IT	3.0%
Edinburgh Worldwide IT	3.0%
Themes	
International Biotechnology IT	4.5%
Bluefield Solar Income Fund IT	3.5%
Herald IT	3.5%
Standard Life Private Equity Trust IT	3.0%
Golden Prospect Precious Metals IT	3.0%
Riverstone Energy IT	2.5%
Allianz Technology Trust IT	2.0%
Commercial property	
TR Property IT	4.5%
Standard Life Property Income IT	3.5%
Cash	**1.5%**
Total	**100%**

Holdings are rounded to the nearest 0.5%

John Baron's Income portfolio

Bonds	
Invesco Perpetual Enhanced Income IT	8.5%
New City High Yield IT	7.0%
TwentyFour Select Monthly Income IT	3.5%
UK shares	
Standard Life Equity Income Trust IT	6.0%
Perpetual Income and Growth IT	5.5%
The Merchants Trust IT	5.5%
JPMorgan Mid Cap IT	5.0%
Acorn Income Fund IT	4.0%
Aberdeen Smaller Companies Income IT	3.5%
International shares	
European Assets IT	6.0%
Henderson Far East Income IT	6.0%
JPMorgan Japanese IT	4.0%
North American Income Trust IT	3.5%
Themes	
Bluefield Solar Income Fund IT	4.5%
International Biotechnology Trust IT	4.0%
City Natural Resources IT	4.0%
Utilico Emerging Markets IT	3.5%
Commercial property	
Standard Life Property Income IT	6.0%
F&C UK Real Estate Investment IT	3.5%
Regional REIT IT	3.0%
Cash	**3.5%**
Total	**100%**





Portfolio performance 1 January 2009-31 August 2017

	Growth	Income
Portfolio Total Return [%]	248.8	193.5
MSCI WMA Total Return [%]	141.4	110.1
Relative Performance [%]	107.4	83.4
Yield [%]	2.8	4.5

The MSCI WMA Growth and Income benchmarks are cited [total return]

MONEY

FINANCIAL PLANNING

Time to switch from Barclays Smart Investor?

Barclays' new Smart Investor platform has drawn heavy user criticism. What are the alternatives?

EMMA AGYEMANG

Barclays (BARC) launched a new investment platform last week, but traditional stockbroking customers have been angered at changes that have made the service more expensive for large share-only portfolios and have made it harder to deal more complex holdings. Frequent share dealers and those seeking more specialised investment tools may want to look to an alternative platform to cater to their needs.

Barclays moved 200,000 customers to its new Smart Investor service over the bank holiday weekend with assets of around £14bn. The shift was designed to appeal to a broader customer base and benefit buy-and-hold fund investors and less sophisticated customers. However the move was met with anger by many of its customers, who did not approve of the changes and suffered a raft of issues with the new site, including difficulty logging in, missing transactions and inconsistent stock pricing.

Barclays has said it is working on those issues, but many customers are still keen to leave due to the range of services Barclays no longer provides. It no longer offers the ability to trade overseas equities, formerly facilitated via a white label service offered by Saxo, or more complex financial products including covered warrants. Investors are also unable to manage spouses' accounts. Previously investors could authorise access to third-party accounts with a letter of authorisation, but the bank says that this will no longer be the case for security reasons.



'The shift was designed to appeal to a broader customer base and benefit buy-and-hold fund investors and less sophisticated customers'

The new service also means customers can no longer hold multiple investment accounts of the same type under one name.

Barclays will still carry over power of attorney, executor or court appointed third-party agreements, but this will become a telephone-only service. However customers will be charged the online transaction rate to trade rather than the telephone rate of £25 per trade to buy and sell funds or shares.

Smart Investor customers will also no longer be able to hold portfolios in trust. Previously Barclays Stockbrokers customers could manage shares and funds in bare trusts if they were the trustees.

Meanwhile investors who trade daily and often rely on research tools such as daily live price changes and broker notes have also expressed their unhappiness about the changes. Whereas before investors could view daily live price changes in their stocks compared to the previous day's price, the platform now only allows you to view the change in value against the book cost rather than prior day value. Previously investors could also see summaries of recent brokers' notes for individual stocks, but these have now been condensed to a single "consensus" number.

Barclays said many of its old research features including RNS and news announcements were still available in its Smart Investor Research Centre and recommended customers watch its how-to videos for more information, or contact the bank.

Holly Mackay, chief executive officer of personal finance website *Boring Money* says: "For people who are hobbyist investors who liked the complexity of the old site I think many of them will see it as being dumbed down," she adds. "The go-live issues are teething troubles and I imagine Barclays will sort those out, but there is a bit of a backlash because the new platform is obviously a strategic change in direction. They're making people log in through the core business site. This is something other banks – including HSBC and Santander – are starting to move on too; namely ways they can capitalise on their large market base to drive up their investment business."

Smart Investor: will you pay more?

Barclays' platform overhaul was completed to embrace a wider mix of investors and has resulted in reduced costs for many fund investors. However stocks and shares investors, who previously paid a flat fee to hold shares, could end up paying more due to the new charging structure.

Investors with large fund portfolios will benefit from reduced annual charges, down from 0.35 per cent of assets to just 0.2 per cent of assets per year. Fees will be charged

monthly and be subject to a minimum charge of £4 – or £48 a year.

Customers with large share portfolios will generally pay more under the new model. Investors in stocks, investment trusts and exchange traded funds (ETFs) will be charged a percentage-based fee of 0.1 per cent on their assets instead of a single fixed annual fee of £30 plus value added tax (VAT). Generally fixed fees are better for those with larger pots and previously customers with a Barclays Stockbrokers individual savings account (Isa) or general investment account would pay just £36 a year. The new minimum charge for any account will be £48.

Shares, ETFs and investment trusts will now cost a fixed fee of £6 per trade. Previously customers that made fewer than nine trades in the previous month paid £11.95 per trade, with only those trading more than 20 times in a month charged the lowest fee of £5.95. However it now costs £3 per transaction to trade funds, which were previously free to trade.

Alternatives to Barclays

If you do decide to switch, investors looking for a platform that offers more specialised investment tools, assets and services should focus on those with a stockbroker heritage as they are more likely to meet high-end requirements. Examples include Alliance Trust Savings, Charles Stanley Direct and The Share Centre.

Alliance Trust Savings charges £10 per month for its dealing and Isa accounts, which includes four online trades a year. To trade funds or shares online it costs £9.99 per transaction; with its loyalty discount for customers who have held an account for between five and 10 years, this falls to £8.99, £8.49 for customers of 11 to 15 years, £7.99 for customers of 16 to 20 years and £7.49 for customers of 20-plus years.

The platform allows you to trade international equities and covered warrants at its standard price, but for international trading a foreign exchange fee will also apply. This ranges from 1.5 to 0.35 per cent depending on the value of the transaction.

Investors can also manage a spouse's account or power of attorney managed account for no extra charge. The only account the platform allows to be managed through a bare trust is its child dealing account. The usual fee for its First Steps Account of £3.33 a month applies.

Charles Stanley Direct charges an annual custody charge of 0.25 per cent to hold stocks and shares, with a minimum of £24 and maximum of £240 a year, across all its accounts. To hold funds it charges a tiered fee of 0.25 per cent for values of 0-£250,000, 0.20 per cent for £250,000-£500,000, 0.15 per cent for £500,000-£1m, 0.05 per cent for £1m-£2m and there is no charge for values over £2m. It costs £11.50 to trade stocks and shares online, and funds are free to trade.

Investors cannot trade covered warrants, but are able to trade international equities at the following cost: First £10,000: 1.25 per cent; Next £90,000: 0.375 per cent; balance over £100,000: 0.275 per cent. A foreign exchange fee also applies which ranges between 1 and 0.15 per cent depending on the value of the transaction. And there is an annual custody charge of £30 per line of international stock.

Customers can manage a spouse's account for no extra charge, but the platform does not allow investors to hold accounts in bare trusts. And power of attorney accounts can be managed via telephone for no extra charge.

The Share Centre charges £1.50 per month + VAT for its dealing account and £4.00 per month + VAT for its Isa account. To trade funds or shares, investors are charged £7.50 for deals less than £750 or 1 per cent for those £750 and above.

Investors are able to trade covered warrants at the platform's standard prices. However as the platform mostly focuses on UK investments you can only trade a limited range of international shares including those across European or North American markets, as long as they are traded in sterling and are able to settle through the UK settlement system, CREST. There is no extra charge to do this.

"AJ Bell Youinvest is another interesting option," Ms Mackay adds. "I think it's got a lot better over recent times and it is cost competitive, equally strong on pensions and funds and there is a lot of share information there too."

To hold shares in its dealing and Isa account AJ Bell Youinvest charges 0.25 per cent a quarter with a maximum of £7.50 per quarter (£30 per year). To hold funds it charges 0.25 per cent on the value up to £250,000, 0.10 per cent on the balance between £250,000 and £1m and 0.05 per cent between £1m and £2m, with no charge on the value above £2m.

To trade shares, ETFs, investment trusts, gilts and bonds AJ Bell charges £9.95 per trade, but if you traded more than 10 times in the previous month this falls to £4.95. To trade funds or for regular investing the platform charges £1.50 per trade. To transfer the underlying assets from your Isa or dealing account to another platform will cost £25 per holding.

She also likes TD Direct Investing due to its historical stock trading heritage. The platform was recently acquired by Interactive Investor, which is another DIY investor service she rates for people looking to trade regularly. Both have fixed fees, which tend to be better for larger portfolios.

TD Direct's dealing account charges £20 + VAT twice a year, which is waived if you hold a linked TD Isa or self-invested personal pension (Sipp), or if you place one or more trades in its six-monthly charging period or have a portfolio worth at least £15,000 or funds worth at least £10,000. Its Isa account charges £30 + VAT per year, which is waived if you have a portfolio of at least £5,100 or set up a regular investing facility.

Interactive Investor's dealing and Isa accounts charge £20 per quarter, which covers your first two trades in the quarter.

However both platforms will be integrated into one platform with one fee structure later this year, so the current fees will change.

How can you complain?

If you are angry about issues relating to Barclays and want to complain, you can take your issue to the Financial Ombudsman Service (FOS). The FOS is there to resolve problems between consumers and financial businesses and can demand compensation be paid in cases where it judges consumers have been financially harmed. But the process will not be quick. If you want to make a complaint, you must first prove you have attempted to resolve the issue with Barclays.

The business then has eight weeks to give its 'final response' to your complaint (make sure you request this). When you have received the final word – or if you have not received that within eight weeks – and assuming you remain unhappy with the response, you can take the query to the FOS, which will then consult both you and – in this case – Barclays and come to a conclusion.

The FOS does compensate for investment losses, in theory. When considering the level of compensation you deserve for investment losses that you believe were not your fault, the FOS's aim is to put you as far as possible in the position you had been in had you not received bad service. For example, that may mean compensating you for the value of a holding that you would have sold that subsequently fell in value while you were unable to trade. This will be determined on a case-by-case basis.

Mark Polson, principal at financial services company Lang Cat, says: "The FOS is a big stick to hit people with and it's not straightforward. If you do want to complain to the FOS be very clear on the timeline and make sure you've exhausted all the channels that exist and be very clear on the detriment you have suffered." *KB*

MORE ONLINE



See the online version of this article at ***www.investorschronicle.co.uk*** **for a table comparing all fees**

Use tax breaks to bolster your strong position

Our reader and his wife should make sure they are taking advantage of their tax allowances

CHRIS DILLOW, WAYNE BERRY & STEWART SANDERSON

Patrick is 61 and retired this year. He has started to receive a defined-benefit (DB) public sector pension, which is paying him just over £50,000 a year. His wife has started to draw down from her various pension schemes and has a cash lump sum of £75,000, but will not have access to her state pension and a small DB scheme until 2024. They have also opened self-invested personal pensions (Sipps) into which they have transferred various pots of cash, and Patrick has realised a £170,000 lump sum from his DB pension, also in cash. Some of this has been used for this tax year's individual savings account (Isa) allowances.

"We want to generate an income of about £20,000 a year over the next six years until we both reach state pension age and around half that amount thereafter," says Patrick. "The main issue is what to do with all this cash. We would like some ideas about how to rebalance the portfolio for the long term – in the past we would have invested it in fixed interest, but the environment has changed. Our portfolio has been built up over 20 years, and as my attempts at investing in individual shares have mostly not been successful I prefer collective investments.

"I am a higher-rate taxpayer, but my wife has almost no income of her own and has not paid tax for a couple of years. We are in good health, but will need to make provision for the probability that one of us will eventually need long-term care. We own our own house, which is worth about £1.5m, and don't have children so inheritance planning is not an issue."

THE BIG PICTURE

Chris Dillow, Investors Chronicle's economist, says:

This is a conservative portfolio, almost two-thirds of which is in safe assets such as investment-grade bonds and cash – **Fidelity Moneybuilder Income (GB00B3Z9PT62)** and **Personal Assets Trust (PNL)** hold bond investments. So should you rebalance towards equities?

Your age is largely irrelevant. The idea that older people should own fewer stocks was shown to be an old wives' tale by Narayana Kocherlakota and Ravi Jagannathan in the mid 1990s. It's tempting to make such a shift simply because returns on cash and bonds are paltry. There are, though, good reasons to resist this temptation.

> 'One reason why returns on safe assets are so low is that investors fear either falls in share prices or sustained periods of low growth'

One reason why returns on safe assets are so low is that investors fear either falls in share prices or sustained periods of low growth. We can't tell if such fears will come to pass, but they are reasonable. Think of cash and bonds as insurance – and insurance is expensive when everybody wants to buy it.

Your income requirements are very low. If equity returns are around average, you can get an income of £20,000 a year even with a conservative asset allocation.

And the prospect of a big long-term care bill perhaps argues for a safer asset allocation, simply to avoid the small but nasty risk you'll be hit with such costs after share prices have fallen. It's almost impossible to quantify this danger, but Andrew Dilnot estimated that one in 10 people will need to spend over £100,000 in 2009-10 prices – around £125,000 in today's money.

On the other hand, you can think of your defined-benefit pension as a safe asset. If we take this into account your asset allocation is very cautious so you might want to hold more equities.

Patrick and his wife's portfolio

Holding	Value (£)	% of the portfolio
Syncona (SYNC)	49,497	3.97
Fidelity MoneyBuilder Inc. (GB00B3Z9PT62)	55,132	4.43
Fundsmith Equity (GB00B41YBW71)	57,567	4.62
Personal Assets Trust (PNL)	57,008	4.58
RIT Capital Partners (RCP)	55,819	4.48
Schroder Global Cities Real Est. (GB00B1VPTY75)	34,082	2.74
Scottish Mortgage Investment Trust (SMT)	58,550	4.7
UBS MSCI Japan UCITS ETF (hedged to GBP) (UB0C)	24,328	1.95
Vanguard Emerging Markets Stock Index (IE00B50MZ724)	30,898	2.48
Threadneedle High Yield Bond (GB00BPZ55D21)	35,958	2.89
Finsbury Growth & Income Trust (FGT)	58,917	4.73
NS&I Index-linked Savings Certificates	64,772	5.2
Cash	500,500	40.18
Fidelity BlackRock GI Equity 50:50 Index pension fund	162,500	13.05
Total	**1,245,528**	

Wayne Berry, divisional director at Brewin Dolphin, says:

Given the asset base the two of you have and the requirements from your investments, your target income should be achievable. And because you hold a good deal of this in tax-efficient wrappers the income could be taken in a very tax-efficient manner.

You are a higher-rate taxpayer so any withdrawals taken from your Sipp will attract higher-rate tax which is unnecessary given the other assets you hold. As your wife is a non-tax payer and inheritance tax (IHT) is not a consideration, I would suggest taking withdrawals from her pension arrangements to use up some or all of her annual personal allowance of £11,500. But if IHT were to become a consideration for you both this would probably not be a good option, based on current legislation.

You are right to continue to subscribe to Isas each year and shelter more investments from tax. Based on the current value of the investments you do not have in Isas, it will take another three tax years to move the remaining investments into the Isas.

I agree with your preference for collectives as you will be reliant on the income produced from the investments to maintain your standard of living. The use of collectives such as open-ended investment companies and investment trusts not only spreads the risk of the capital falling but the income too.

Your cash balance is relatively high, especially if we add it to the NS&I holdings. You are right, however, to be nervous about adding fixed income investments at the

How to improve the portfolio

Chris Dillow says:
The most obvious way to increase your equity exposure is to invest the £170,000 lump sum in a global equity tracker fund. You should think of it as a cheap fund of equity funds, and the default option for investing in equities.

The case for doing this might be especially strong for you, because your existing equity investments probably carry less general market risk than most people's. Some of them are focused on defensive stocks – **Personal Assets Trust and Finsbury Growth & Income (FGT)** have large holdings in defensives. And **Scottish Mortgage Investment Trust (SMT)** and **Fundsmith Equity (GB00B41YBW71)** come closer to being proper stockpickers than most funds, so are bets on their managers' ability to do this. Given such holdings, a global tracker might help spread equity risk.

Even if you want to keep a high cash weighting, I'm not sure you should do this in Sipps. Cash returns on these are generally awful. A better option might be to hold savings bonds of which the interest rates are a little better. As your wife has little other income she should do this to take advantage of her income tax allowance.

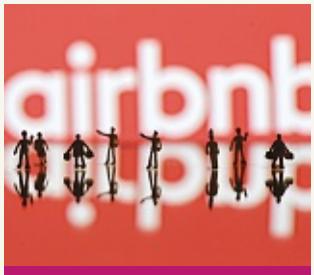
As for how you should take income, remember that you have a capital gains tax (CGT) allowance and that you can create your own dividends simply by selling some of your investments each year. You do not need to invest in income stocks or to take taxed dividends.

Wayne Berry says:
The Isas, taxable account and your wife's pensions have a capital value of nearly £877,000. An income of £20,000 would equate to a yield of about 2.3 per cent on these, which is more than achievable.

This can be achieved via a few tweaks to the portfolio to increase the natural yield from the holdings to cover the income withdrawals. As most of the investments are in some form of tax wrapper – Isa or pension – whether the return comes from income or capital growth doesn't matter.

As you both have at least 25 years to plan for, exposure to emerging markets is advisable as this is where tomorrow's growth will largely come from. Your holdings in Scottish Mortgage Investment Trust and **RIT Capital Partners (RCP)** should also provide attractive compounding growth over that time. It is worth taking profits on these occasionally to 'lock in' some of the capital gains you have accumulated. I tell clients who have seen attractive capital growth that taking gains is a good discipline to have. Capital growth is meaningless until the investments are actually sold.

I suggest investing the cash in all the pension funds to generate some returns – even if Patrick's is not touched for now. Higher-yielding funds such as **Man GLG UK Income (GB00B0117D35)** and **CF Miton UK Multi Cap Income (GB00B4M24M14)** have impressive yields of over 4 per cent and good performance records over the longer term. Regarding overseas allocation, **Artemis Global Income (GB00B5N99561)** would complement the holdings in Scottish Mortgage Investment Trust and RIT Capital Partners.



'Scottish Mortgage Investment Trust offers exposure to unlisted investments otherwise unavailable to most investors, for example, Airbnb, Spotify and Grail'

Another area to consider adding to is infrastructure as this can offer attractive income and, in most cases, inflation-linked returns. We will always need infrastructure even when robots and technology companies take over the world. Ways to add exposure to this area include **HICL Infrastructure (HICL)** and **Legg Mason IF Rare Global Infrastructure Income (GB00BZ01WT03)**.

Stewart Sanderson says:
Your Isa appears to be well diversified geographically. However, I would question the equity content given that you do not need to take much risk to achieve your objectives. Having said that, you have some stellar performers – Scottish Mortgage Investment Trust in particular. This trust offers exposure to unlisted investments otherwise unavailable to most investors, for example, Airbnb, Spotify and Grail where you are invested alongside Bill Gates, Jeff Bezos and Google, as well as top-performing listed companies such as **Amazon (US:AMZN)**, **Tesla (US:TSLA)** and **Ferrari (ITA:RACE)**.

Make sure you use your income, CGT and dividend allowances with your taxable investments, or by taking income from your wife's pension. To rebalance the portfolio I would reduce the risk of the Isas and invest cautiously in the Sipps. There is little value in fixed income, so choose managers with large allocations to fixed income alternatives such as market neutral funds.

If you do want a pot to 'play with' I would use your Sipp because you may not need to access this for some time, if at all.

moment as rising interest rates will have a negative impact on the capital value of your bond holdings. I would suggest holding your cash at current levels for the immediate future and reassess periodically – especially if gilt yields rise in the next few years. While this can be frustrating at current interest rates, the cash element will help balance the overall exposure to equities with the rest of the investments.

Stewart Sanderson, head of relationship management, Seven Investment Management, says:

Your affairs are well organised, you are making use of the available tax wrappers – pensions and Isas – and you have accumulated excess cash. Your pension income is guaranteed by the UK government, which is as good as it gets, and you have enough funds to generate the additional income you require, so you are in good shape.

Make sure both your wills are up to date, and your expressions of wishes are complete for passing on the pensions. If you pass pensions on before you are 75 they are tax-free – even on drawdown. You could also give part of them to a charity free of tax.

I would consult a financial planner to ensure you have made use of the available pension and Isa allowances, including any carry forward available from previous years. Although annuity rates are currently poor, they may be sufficient to provide your requirements with limited risk. A planner could explain this as the death benefits of the various pensions may impact the income requirements for the survivor.

Your income requirements are relatively straightforward and do not require you to take much risk. Because of this, and because you do not need to plan for IHT, you are in the fortunate position of being able to spend some of your excess cash. You could even draw on your Isa to enjoy your retirement – I would be thinking of a holiday home in the sun if I were in your position!



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None of the commentary here should be regarded as advice. It is general information based on a snapshot of the reader's circumstances.

TIPS

SHARES 34 FUND TIP 39 TIP UPDATES 40
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TIPS OF THE WEEK



Ladbrokes, recently merged with Coral, seems to be getting its digital act together

TRAVEL & LEISURE

LADBROKES CORAL (LCL)

BUY

Take a bet on Ladbrokes Coral

Bull points

- Improving digital revenues
- Multi-channel play
- Technology optimised for new products
- Lowly rated compared with rivals

Bear points

- Fear of tougher regulations
- Falling high-street revenue

Accepting the risks is inherent in gambling, and buying shares in **Ladbrokes Coral (LCL)** is little different. Potential investors may find it difficult to look past the UK government's review of fixed-odds betting terminals, due in October. The Department for Culture, Media and Sport is looking at the maximum stakes and prizes for gaming machines that have been labelled the 'crack cocaine' of gambling; how many machines can be present on one premises, and how can the risks to gamblers looking for a quick fix be minimised?

Since 56 per cent of Ladbrokes Coral's high-street revenue comes from fixed-odds betting terminals, a cap on the amount punters could spend on them would be bad news. City analysts reckon that if the maximum stake took the extreme hit and was cut to £2 a play from the current £100 maximum, this would wipe around £450m from annual revenue and £100m per year off pre-tax profits. This could send EPS down as much as 40 per cent. But Interactive Investor's head of equity strategy, Lee Wild, points out that these scenarios don't include benefits from the inevitable cost cutting that would follow the worst outcome.

Meanwhile, Ladbrokes' bosses claim that levels of problem gambling in the UK are relatively low compared with other countries, and have not increased since fixed-odds betting terminals were introduced to betting shops.

Besides, management wants to focus on the five themes they've identified to drive growth in the group formed by the merger of Ladbrokes and Coral less than a year ago. These are: technology, product, marketing, multi-channel and international expansion.

IC TIP RATING
Tip style: SPECULATIVE
Risk rating: HIGH
Timescale: LONG TERM

All UK brands have now moved onto the same digital platform with the aim of improving efficiency. In order to accelerate new product launches, back-office staff have all moved to one location in east London. Admittedly, the digital platform move came at the expense of new sportsbook products for the Ladbrokes website. But new products are on their way to coincide with the start of the 2017-18 football season, including Ladbrokes OddsBoost and Coral Build-My-Bet.

The marketing team is focusing on higher-value customers, or those prepared to spend more, which should help achieve a higher return on investment. Ladbrokes has cut its UK marketing spend from 33 per cent to 28 per cent of net revenue by investing less in those channels that were delivering high volumes of lower-value customers.

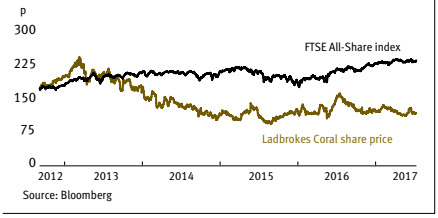
Marketing is also encouraging customers to use several products, so those used to popping into a betting office start to download the app onto their smartphone. Access to an online wallet will be launched in Ladbrokes' shops in the second half of the year. This means punters can use their online credit on self-service betting terminals and playing the fruit machines.

In the first half of 2017 digital gaming revenue was up 11 per cent to £194m. Multi-channel gambling made up more than a third of revenue for Ladbrokes' website and half of Coral's online sales. Revenue at betting shops fell 6 per cent to £703m as customers spent an average of 7 per cent less per stake. Overall, group revenue improved by 1 per cent to £1.2bn.

Last month, acquisition-driven online gambling company GVC (GVC) made a fresh approach with a takeover offer rumoured to be as much as £3.6bn. This is the second time GVC has made a move for Ladbrokes. It approached the company last year as it was in merger discussions with Coral.

At 10 times forecast earnings for 2017, falling to eight times for 2018, the shares are rated lower than fellow high-street bookies William Hill (WMH) and Paddy Power Betfair (PPB). Yet analysts at investment bank UBS think the shares are undervalued at less than six times enterprise value to cash profits, and that a significant re-rating could be around the corner if the online business continues to beat expectations. Still, much depends on the outcome of the government's review of gambling and the UK Gambling Commission's decision to fine 888 Holdings may actually signal good news. Shares in 888 rallied after last month's announcement because, although the £8m fine was a record high, it paled in comparison to the worst-case scenario where 888 could have lost its licence. Here's hoping that the government's review shows a similarly light touch. Buy. *JF*

Share price 117p



Source: Bloomberg

Ladbrokes Coral

Ord Price: 117p **Market Value:** £2.24bn
Touch: 116.8-117p **12-Month High:** 161p **Low:** 110p
Forward Dividend Yield: 5.3% **Forward PE Ratio:** 8
Net Asset Value: 73p* **Net Debt:** 75%
*Includes £2.6bn of intangible assets, or 135p a share

Year to 30 Jun	Revenue (£bn)	Operating profit (£m)	Earnings per share (p)	Dividend per share (p)
2015**	2.12	217	9.1	3.00
2016**	2.35	264	6.6	3.00
2017**	2.47	315	11.3	3.77
2018**	2.59	405	15.4	6.16
% change	+5	+29	+36	+63

**2015 & 2016 – pro-forma figures; forecasts from Numis Securities
Normal market size: 20,000 Matched bargain trading Beta: 0.75
Last IC view: Hold, 133p, 23 Mar 2017



The retailer is generating impressive growth in a difficult market and the dividend yield remains fat

GENERAL RETAILERS

BUY

CARD FACTORY (CARD)

Card Factory still a winner

Bull points

- Strong like-for-like growth
- Market-leading position
- Still generating lots of cash
- Flexible pricing structure

Bear points

- Pressure on profit margins
- Consumer confidence weak

IC TIP RATING
Tip style: INCOME
Risk rating: MEDIUM
Timescale: MEDIUM TERM

Retailing is a difficult sector to invest in this year, one where dependable growth comes at a premium. But those on the hunt both for growth and income should pay attention to **Card Factory (CARD)**, especially following a recent first-half trading update which suggested it is possible to deliver solid like-for-like growth in a sub-sector of retailing that many say is in decline. True, like many retailers, Card Factory will have to tackle cost inflation and waning consumer confidence, but the group's evolving position as the market leader, as well as its flexibility regarding prices, make it a strong contender for income portfolios.

The first half of 2017-18 has been particularly impressive, with like-for-like sales growth of 3.1 per cent – the best growth rate since the shares were listed in 2014 and well ahead of the 0.2 per cent growth rate produced in last year's first half. Adjust for the same number of trading days, and group sales grew by 6.7 per cent. That was a substantial improvement on last year's underlying growth rate of 4.3 per cent and even better than the 6.1 per cent recorded in the first quarter.

These gains were achieved without the majority of price increases that management had considered towards the end of last year. They also came from both the card and non-card categories equally, with average transaction values rising in addition to strong overall volumes. This suggests that Card Factory's product range has been received well by customers.

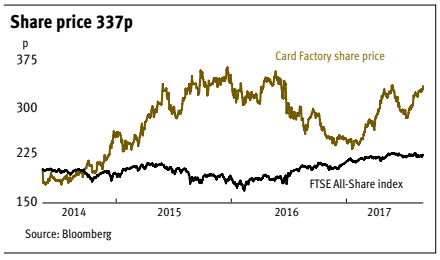
According to City analysts, the group still has room for future price rises too, particularly as it establishes itself as the market leader. This would make like-for-like growth rates such as those noted above a more regular and predictable occurrence. True, there is the risk of downward pressure on profit margins this year because of both sterling's continuing weakness and higher wage costs, yet this might make price hikes all the more necessary. But that concern is unlikely to stop analysts upgrading their forecasts at the time of interim results later this month, particularly as Card Factory, like all retailers, has fairly high fixed costs so, as sales rise, more income flows through to profits. Analysts now expect their conservative forecasts for 2.5 per cent ▶

▶ like-for-like growth in the second half to be outperformed.

The introduction of contactless payment methods in store should encourage a rise in transaction volumes as customers pay for smaller basket values more quickly. Then there are store openings – 30 stores, net of closures, opened during the first half and the full-year target is for an extra 50. This included a store in the Republic of Ireland and the pilot scheme over there is set to expand.

Finally, those still sceptical of the growth prospects on offer can take encouragement from the company's track record for dividends – both ordinary and special. True, net debt as at 31 July 2017 was £146m against £122m a year earlier, but management continues to highlight strong cash generation and intends to keep returning surplus cash to shareholders. The company will update on the quantity and timing of the next special dividend at the interim announcement, but analysts expect the fat payouts to continue (see table).

Looking ahead, the company isn't up against demanding comparative figures, which look easily beatable given the strength of underlying trading and the continued store roll-out. True, the share price has gained 36 per cent since our last buy call (247p, 24 November 2016), but we believe there is still room for upside. What's more, shares in a company with such a strong market position and growth prospects should not yield close to 8 per cent, yet that only helps to sweeten the deal. Buy. *HR*



Card Factory

Ord Price: 337p **Market Value:** £1.15bn
Touch: 336-337p **12-Month High:** 343p **Low:** 232p
Forward Dividend Yield: 7.7% **Forward PE Ratio:** 16
Net Asset Value: 73p **Net Debt:** 54%

Year to 31 Jan	Turnover (£m)	Pre-tax profit (£m)	Earnings per share (p)	Dividend per share (p)
2015	353	42.7	10.6	6.8
2016	382	83.7	19.5	23.5†
2017	398	82.8	19.3	24.1†
2018*	427	87.1	19.9	25.0
2019*	453	93.7	21.4	26.0
% change	+6	+8	+8	+4

Normal market size: 1,500 Matched Bargain Trading Beta: 0.2
*Peel Hunt estimates (profits & EPS not comparable with historic figures);
†Includes special dividends of 15p Last IC view: Buy, 325p, 15 Aug 2017

SUPPORT SERVICES

BUY

COMMUNISIS (CMS)

Value at Communisis

Bull points

- Low rating compared with peers
- Restructuring beginning to show results
- Falling debt
- Big contract wins

Bear points

- Pension deficit
- Heavily UK focused

IC TIP RATING
Tip style: VALUE
Risk rating: MEDIUM
Timescale: LONG TERM

Like many companies exposed to the declining world of print publishing, marketing services provider **Communisis (CMS)** has had a rough time in recent years. Goodwill on legacy acquisitions had to be written off, pushing down profits. In addition, the company has been pursuing a costly restructuring programme to improve efficiency and facilitate its shift towards digital communications, including the launch of Psona, its digital agency. The costs associated with this restructuring have yet to let up, with £0.8m incurred in the first half of 2017, but the turnaround looks as though it is beginning to bear fruit. In the first half of 2017, all the key figures moved in the right direction – profits and cash flow were up and net debt was down.

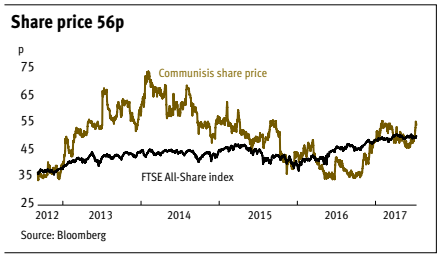
Digital and services-based work has been growing as a proportion of overall revenues, accounting for 60 per cent at the latest half-year, from 57 per cent a year earlier. The group is investing heavily in technology both to expand its services and improve its efficiency. In the first half, central costs increased by £0.6m, spent on improvements such as enhanced cyber security and preparation for the introduction of general data protection regulation next May. Yet that's good because Communisis's bosses reckon that as regulation increases, so do barriers to entry for competitors, making the company's defences stronger.

Communisis does marketing for a wide range of blue-chip clients, recently winning contracts with the UK's taxman, insurer LV= and HSBC. In the first half of 2017 it signed multi-year renewals with Nationwide, Virgin Money and Co-op.

While the UK remains the focus for the company, management is working to diversify business internationally. But it still has some way to go to reduce this risk. At the latest update, 30 per cent of revenues were generated internationally, up from 24 per cent in 2016. Outside of the UK the group has performed well in Spain, Poland and the Netherlands.

Communisis has a defined-benefit pension scheme – a common burden for older UK companies. At the most recent triennial valuation the deficit had increased to almost £30m from £19.5m at the 2014 valuation. The company has agreed to pay repair contributions starting at £2.55m annually, increasing in line with the rate of dividend growth or at least by 3 per cent. In addition, it will pay £1.15m annually into an arrangement designed to fund the scheme should the company go bust. Arrangements like this are common, and the recently agreed plan gives investors some clarity about the likely costs of plugging the pension deficit.

Given the turbulent history at Communisis, the seemingly-low multiple of approaching nine times 2018's forecast earnings is slightly ahead of where the shares have been rated in the past few years. That said, the rating still looks low compared with similar media companies and the decent dividend yield helps make the shares a play for value as well as recovery. Buy. *TD*



Communisis

Ord Price: 56p **Market Value:** £117m
Touch: 55-56p **12-Month High:** 58p **Low:** 34p
Forward Dividend Yield: 5.2% **Forward PE Ratio:** 8
Net Asset Value: 62p* **Net Debt:** 22%
*Includes intangible assets of £186m, or 89p a share

Year to 31 Dec	Turnover (£m)	Pre-tax profit (£m)	Earnings per share (p)	Dividend per share (p)
2015	354	14.5	5.2	2.2
2016	362	16.7	6.1	2.4
2017**	379	17.8	6.2	2.6
2018**	394	18.9	6.5	2.7
2019**	400	19.6	6.7	2.9
% change	+2	+4	+3	+7

Normal market size: 5,000 Matched bargain trading Beta: 0.62
**finnCap forecasts, PTP and EPS figures adjusted
Last IC view: Hold, 51.75p, 13 Mar 2017

AIM: OIL & GAS PRODUCERS

BUY

EUROPA OIL & GAS (EOG)

Bulls set to go for Europa

Bull points

- Huge and enticing prospective resource
- Shares below placing price
- Cheap UK onshore output

Bear points

- Hugely speculative
- Little cash flow

In tipping shares in **Europa Oil & Gas (EOG)** – an Aim minnow with limited financial muscle, but enormous speculative oil prospects in the Irish Atlantic margin – we do so with a huge health warning. These shares have the potential to move sharply in one of two directions, possibly in the next few weeks. At the same time, we view the company as an exciting risk-reward play on drilling being done on other companies' dimes.

IC TIP RATING
Tip style: SPECULATIVE
Risk rating: HIGH
Timescale: SHORT TERM

That statement takes some unpacking, and even more context. Europa may be small, but it has a large acreage position in the South Porcupine basin, offshore of south-west Ireland. In fact, geological work to date has led management to suggest that its four licences in the region might hold 4.2bn barrels of oil equivalent. That estimate is the "gross mean un-risked prospective resource" – ie, potentially or technically recoverable, assuming no drilling risk and Europa's total ownership.

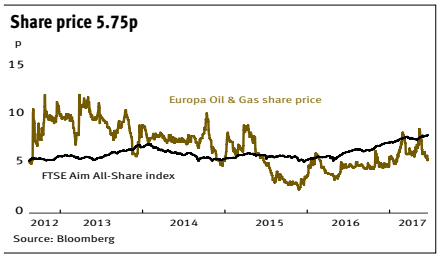
Why should we give credence to these fanciful figures? The answer can be traced to Bay du Nord, a major discovery made by Norway's national oil company, Statoil (OSE:STL), in offshore Newfoundland in 2013. This exploration pioneered the so-called pre-rift play, which has geological analogies with the Irish Atlantic Margin, and explains why a 2015 licensing round resulted in a flood of applications from the industry's largest players, including Exxon Mobil (US:XOM). Parallels with Statoil's discovery are currently being tested by London and Dublin-listed Providence Resources (PVR), which is drilling in an area surrounded by three licences in which Europa has an interest.

The first prospect – Druid – was a disappointment. Providence provided no reference to hydrocarbons when it updated the market on the exploration well last month, which analysts at broker Panmure Gordon said pointed to "a failure". The drill ship has since moved onto the Drombeg prospect, where it is aiming to determine whether an in-place unrisked prospective resource of 1.9bn barrels is commercially viable. Results are expected imminently. Success could significantly 'de-risk' (read 're-value') Europa's portfolio. That would attract larger explorers looking to acquire or to farm-in to the Aim company's three 100 per cent-owned licences either side of Drombeg.

Failure wouldn't be terminal for Europa, which has other catalysts ahead. A fourth field has already attracted one larger player – Cairn Energy (CNE) – which acquired a 70 per cent interest in the licence from Europa in April in exchange for a $6m 3D seismic programme. And even if Cairn ultimately waives its option to drill, Europa has a backstop: sufficiently cheap existing UK onshore production to cover operational cash flows.

We don't usually tip stocks of this size, with good reason. Europa's shares are illiquid and come with a speculative and thus high-risk investment case, and might move on the back of this tip alone. Given the risky nature of the drilling programme, and thus Europa's assets, valuations contain a fair amount of guess work, so we take Canaccord Genuity's risked net present value target price of 20p a share with a chunk of salt.

Then again, valuations have a tendency to rocket when discoveries are made, which explains why the company had little trouble raising £3.4m at 6p a share in an open offer and placing in June. The share price is now below that level. Speculative buy. *AN*



Europa Oil & Gas

Ord Price: 5.75p **Market Value:** £17.3m
Touch: 5.25-5.75p **12-Month High:** 9.4p **Low:** 4.2p
Forward Dividend Yield: nil **Forward PE Ratio:** na
Net Asset Value: 1.5p† **Net Cash:** £1.4m†

Year to 31 Jul	Turnover (£m)	Pre-tax profit (£m)	Earnings per share (p)	Dividend per share (p)
2014	3.88	-0.68	-0.21	nil
2015	2.21	-4.13	-0.86	nil
2016	1.27	-1.90	-0.67	nil
2017*	2.20	0.30	nil	nil
2018*	2.30	nil	nil	nil
% change	+5	na	na	na

Normal market size: 30,000 Market makers: 6 Beta: 0.9
*finnCap forecasts; † As at 31 Jan, excludes proceeds of June's £3.4m placing and open offer Last IC view: None

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The eight tips we selected at the start of 2016 delivered a 16.1 per cent total return compared with the FTSE All-Share, which returned 20.8 per cent. Over five years, the Tips of the Year returned 132.8 per cent versus 63.1 per cent from the index.

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INVESTMENT TRUST

HICL INFRASTRUCTURE (HICL)

BUY

Buy HICL while it is trading at a single-digit premium

Bull points

- Inflation-linked income
- Attractive yield
- Narrower-than-average premium
- Uncorrelated returns

Bear points

- Portfolio more correlated than in past
- Premium could narrow further

HICL Infrastructure (HICL) offers high, inflation-linked income from a portfolio of long-term infrastructure assets and is trading on a far narrower premium than usual, making now a good entry point.

HICL is a popular trust and normally trades on high double-digit premiums because of its fairly low-risk profile, inflation-linked dividends and uncorrelated returns to equities and bonds. It invests in long-term infrastructure projects in three main areas – public-private partnership (PPP) finance projects, regulated assets such as water utilities and higher-risk demand-based assets such as toll roads.

Currently HICL is yielding 4.8 per cent and is sitting on a premium of 8.8 per cent compared with a 12-month average premium of 13.8 per cent. Its premium has narrowed because HICL has been on an acquisitive spree in recent months and has raised a substantial amount of equity in order to fund those transactions.

In the year to date, HICL has invested in its third demand-based toll road, bought a stake in the UK's largest water-only utility, Affinity Water, and most recently agreed to acquire a stake in High Speed 1 (HS1) – the high-speed rail link running between London St Pancras and the Channel Tunnel – as part of a consortium.

In March, HICL raised equity worth £260m and £267.7m in June. HICL is likely to return to the market in order to fund its most recent deal and this expectation has been keeping a lid on its premium.

Its acquisition of a 35 per cent stake in HS1 is costing up to £320m. HICL has so far funded the deal by using its credit facility and cash reserves, but said it expected to have a net funding requirement of £140m according to Liberum. Numis said: "We would expect further issuance given the net funding requirement of £140m, although the timing of this is uncertain."

Investors might want to consider drip-feeding money into this trust, in order to take advantage of its currently narrow premium as well as the potential future opportunity.

The trust delivered a share price total return of 158.7 per cent over 10 years, compared with 75 per cent for the average infrastructure investment trust.

IC TIP RATING

Tip style: INCOME
Risk rating: MEDIUM
Timescale: LONG TERM

It also benefits from inflation-linked returns and income, and high yield, both of which have been boosted by the trust's recent acquisitions. The correlation of the portfolio's long-term returns to inflation improved during its 2016-17 financial year to 0.7 at 31 March 2017 from 0.6 at the same point in March 2016. The HS1 acquisition boosts that correlation to 0.8.

However, HICL's correlation to wider equity markets and to sterling has increased over the past year, as it has been forced to move up the risk scale and invest in more demand-based assets. Fewer UK PPP deals are being commissioned today, meaning greater competition over those assets. PPP assets now account for around 75 per cent of HICL's portfolio by value compared with 95 per cent at March 2016.

Correlation to GDP has increased from 9 per cent to 16 per cent as a result, according to Numis, between March 2016 and March 2017, and the portfolio could be more correlated to market movements.

However, Mr Brierly says: "We believe that HICL has a key role to play in improving portfolio diversification; we expect it to continue to deliver superior long-term returns and it remains a long-term constituent of our model portfolio. The shares have experienced a sharp de-rating in the past year, but we regard this as an attractive buying opportunity.

"HICL offers an attractive yield and genuine capital preservation characteristics, and we believe these have significant value, particularly when we reach the next phase of the cycle."

Opt for HICL for inflation-linked, stable income from a portfolio of lower-risk assets all on a rare single-digit premium. Buy. *KB*

HICL Infrastructure

Price: 162.9p	**NAV:** 149p
AIC sector: Sector specialist: infrastructure	**Premium to NAV:** 8.80%*
Fund type: Investment trust	**Yield:** 4.81%
Market cap: £2.9bn	**Ongoing charge:** 1.26%
No of holdings: 115**	**More details:** https://www.hicl.com/
Set-up date: 29.03.06	
Manager start date: 29.03.06	
Gearing: 0%	

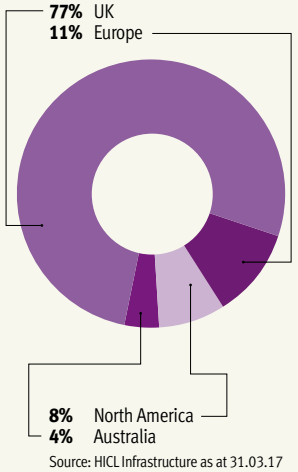
Source: Morningstar, as at 5.09.17, *Winterflood, as at 05.09.17, **HICL, as at June 2017

Top 10 holdings

Northwest Parkway	**6%**	**A63 Motorway**	**4%**
Home Office Accommodation	**5%**	**Dutch High Speed Rail Link**	**3%**
Pinderfields and Pontefract Hospitals	**5%**	**Queen Alexandra Hospital**	**3%**
Southmead Hospital	**5%**	**Allenby & Connaught**	**3%**
AquaSure 0.000	**4%**	**A13 Senior Bonds**	**2%**

Source: HICL Infrastructure

Geographic breakdown



Source: HICL Infrastructure as at 31.03.17

Performance

Fund/benchmark	1-year share return (%)	3-year cumulative share price return (%)	5-year cumulative share price return (%)
HICL Infrastructure	-4.9	29.1	72.5
FTSE All-Share index	12	23	64
AIC Infrastructure specialist sector average	2	34	66

Source: FE Analytics, as at 5.09.17

AIM: GENERAL RETAILERS

VERTU MOTORS (VTU)

Vertu buoyed by scrappage schemes

A July update from car retailer **Vertu Motors (VTU)** – which hinted at pressure in new car sales and used car margins – helped prompt our recent bear call on the company's shares (Sell, 42p, 10 August 2017).

So perhaps it's no surprise that a pre-close update ahead of the group's half-year results in early October was fairly thin on detail. Aside from news of a £14m profit on disposal following the sale of its freehold Jaguar Land Rover dealership property in Leeds, progress across the wider business was kept vague. Suffice to say, bosses confirmed the group had continued to trade "in line with the trends set out in that [July] update and in line with market expectations".

So why do the shares appear to be up despite events? The trading statement coincided with news from car manufacturers Volkswagen and Toyota that both intend to initiate scrappage schemes – the former for diesel models and the latter for both diesel and petrol vehicles. They join BMW, Ford, Hyundai, Mercedes-Benz and Vauxhall which have all launched similar schemes and have also been followed by Renault-Nissan and Kia.

Scrappage schemes largely saved British motor retailers during the last recession, and given recent difficulties in new car sales we're not surprised to see manufacturers falling back on this strategy. But the UK economy has yet to fall back into an official recession, so we can't be convinced the answer is this simple. Sell at 44p. *HR*

Sell

VERTU MOTORS

What we said: SELL
When: 10 AUGUST 2017
Price: 42P

+4%

AIM: LEISURE GOODS

CHARACTER (CCT)

What we said: Buy
When: 29 September 2016
Price: 455p
Share price change to date: +14%

Shares in toymaker **Character (CCT)** rose 8 per cent following news that the group has been appointed as the main distributor in the UK and Ireland for merchandise associated with the Pokémon brand.

Financial details of the deal have yet to be disclosed, but Jon Diver, joint managing director at Character, said he was "thrilled" to be adding the "iconic" brand to Character's product line-up.

Character is on a winning streak with contracts at the moment, having agreed a three-year extension to its master toy licence with DHX Brands for the Teletubbies franchise in July. What's more, the shares trade on just 11 times Bloomberg consensus forecast earnings – still a considerable discount to London-listed peer Games Workshop (GAW). Buy at 525p. *HR*

Buy

GENERAL RETAILERS

HALFORDS (HFD)

What we said: Sell
When: 20 July 2017
Price: 334p
Share price change to date: -3%

High street chain **Halfords (HFD)** surprised the market with better-than-expected like-for-like growth over the first 20 weeks of its financial year. Sales rose 2.7 per cent across the group on an underlying basis, and 3.5 per cent across the retail division – enough to send the shares up 4 per cent in response.

But the group was up against extremely weak comparative figures thanks to last year's terrible weather and, looking ahead, corresponding growth rates are going to become increasingly tough to beat. There's also no change to margin guidance, prompting some analysts to leave forecasts unchanged.

For us, margins make up most of our bear call on Halfords' shares. There's also still a management issue as chief executive Jill McDonald moves on to Marks and Spencer (MKS). Aside from this momentary bounce, the shares have enough downward momentum to keep us out of the game. Sell at 323p. *HR*

Sell

SOFTWARE & COMPUTER SERVICES

MICRO FOCUS (MCRO)

What we said: Buy
When: 4 February 2016
Price: 1,410p
Share price change to date: +61%

Micro Focus (MCRO) has become the UK's largest public technology company, with a market capitalisation of £9.9bn. This follows Friday's announcement that the software group completed its $8.8bn (£6.8bn) merger with Hewlett Packard's software business.

On Wednesday, Micro Focus published the performance of HPE's software business for the three, nine and 12 months ending 31 July 2017. For the three months to July, revenue fell 3 per cent to $718m but the operating margin rose to 24.9 per cent, from 17.8 per cent a year earlier. Looking forward, total adjusted revenues are expected to range between $2.89bn and $2.96bn for the full year to 31 October 2017. This is lower than the $3.05bn adjusted revenue achieved in the 12 months to the end of July, but is driven by "the active reduction of less profitable professional services in sub-scale service lines and geographies".

When the merger was first announced, Micro Focus forecast combined annual revenue of $4.5bn and cash profit of $1.35bn. We still see further upside. Buy at 2,378p. *HC*

Buy

AIM: FINANCIAL SERVICES

MORSES CLUB (MCL)

What we said: Buy
When: 3 November 2016
Price: 120p
Share price change to date: +31%

Provident Financial's (PFG) profit warning last week sent shareholders heading for the exit. Some of those investors may want to take a look at rival sub-prime lender **Morses Club (MCL)**, after it flagged an increase in credit issuance of around a quarter during the 26 weeks to the end of August.

The home credit specialist issued a further £82m in finance during the period, thanks to steady growth in its agent numbers. Customer numbers were up 12 per cent year on year to around 233,000.

Importantly, impairments are expected to be within management's target range, while the proportion of loans to highest-quality customers has increased by 7 per cent.

Management expects its recently secured loan facility to allow it to hire a further 400 agents. The shares are up almost a third since our buy tip, after rising an aggregate 13 per cent during the two days following this update. *EP*

Buy

FUNDS

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NEWS

Baillie Gifford slashes fees on top performers

LEONORA WALTERS

Baillie Gifford is cutting the management fees on a number of its funds including top performer **Baillie Gifford Japanese (GB0006011133)**. The fee cuts take effect from 1 October.

Baillie Gifford said the cost reductions are part of a continued strategy of offering active management at an attractive price whenever fund scale and ongoing costs allow. They follow a reduction in **Baillie Gifford American's (GB0006061963)** annual management fee from 0.65 per cent to 0.5 per cent in January.

Baillie Gifford Japanese's management fee has fallen from 0.65 per cent to 0.6 per cent, taking the already reasonable ongoing charge of 0.68 per cent for its B share class down to 0.63 per cent. The fund, which is run by top Japan manager Sarah Whitley alongside Matthew Brett, is one of the best performers in the Investment Association (IA) Japan sector over one, three and five years, and now one of the cheapest active Japan funds available to UK private investors.

"Any fee cuts for active funds are to be applauded, and when it is cuts to fees on funds with excellent performance even more so," says Darius McDermott, managing director at Chelsea Financial Services. "They didn't need to do it to attract inflows, given the strong returns. The standout Baillie Gifford fund for us is the Japanese fund but they have been in a real sweet spot recently across their equity franchise. [For example] **Baillie Gifford Emerging Markets Growth (GB0006020647)** is the top-performing fund in its sector over one year and **Emerging Markets Leading Companies (GB00B06HZN29)** is second. So we are seeing reductions in funds with excellent track records."

Baillie Gifford Developed Asia Pacific (GB0030492044), **Baillie Gifford European (GB0006058258)** and **Baillie Gifford UK Equity Alpha (GB0005858195)** funds will undergo the largest cuts, with their fees falling from 0.65 per cent to 0.55 per cent. This will reduce Baillie Gifford Developed Asia Pacific's B accumulation share class's ongoing charge from 0.69 per cent to 0.59 per cent, making it one of the cheapest active Asian funds available to UK private investors.

Baillie Gifford European's B accumulation share class's ongoing charge falls from 0.7 per cent to 0.6 per cent and UK Equity Alpha's from 0.68 per cent to 0.58 per cent, making them among the cheapest active funds in the IA European and UK All Companies sectors.

However, when choosing a fund fees are not the only consideration.

"Fees are important as they form a part of the total return that investors receive," said Mr McDermott. "However, historic alpha generation, repeatability of process, fund size and whether a fund manager invests in their own funds are also among other very important factors. But if we had an equal opinion of two funds we would go for the one with the lowest fee."

Brian Dennehy, managing director at research and dealing site FundExpert.co.uk, added: "Our priority is fund performance net of charges, where performance is many multiples more important as a driver of net returns. Knowing a fund's charges tells us nothing about the likelihood of a fund being able to generate outstanding performance net of charges in the future."

Aberdeen New India Trust (ANII) is also going to cut its management fee. It charges 1 per cent of net assets but from 1 April 2018 it will charge 0.9 per cent on net assets up to £350m, and 0.75 per cent on those above that. The trust currently has assets of £309m and its ongoing charge is 1.31 per cent, but this could fall.

"The fee reduction reflects the ongoing pressure for investment trusts to reduce fees to remain competitive," comment analysts at Numis Securities. "The closest peer, **JPMorgan Indian (JII)** charges 1 per cent a year of gross assets and has an ongoing charge of 1.22 per cent, while **India Capital Growth (IGC)** charges 1.5 per cent of gross assets." It has an ongoing charge of 1.83 per cent.

Baillie Gifford has also introduced tiered investment fees on investment trusts it runs including top performer **Scottish Mortgage Investment Trust (SMT)** earlier this year, resulting in a reduction. Since 1 April Scottish Mortgage's annual management charge continued to be 0.3 per cent on its first £4bn of assets under management but on assets above that it is 0.25 per cent. The trust has net assets of about £5.9bn.

Scottish Mortgage Investment Trust has one of the lowest ongoing charges of all active funds of 0.44 per cent.

Templeton Emerging Markets' tech transformation

The trust's small-cap and tech stocks have sent it soaring

KATE BEIOLEY

Templeton Emerging Markets (TEM) has come full circle from an underperforming fund concentrated in mining and resources to a stellar performer with large chunks in 'sexy' technology companies under new manager Carlos Hardenberg. Just don't ask if he's a value investor.

A look at Templeton's top 10 holdings two years ago would have revealed a host of miners and natural resources companies. Today, **Samsung Electronics (SMSD)** makes up 7.1 per cent of assets, Chinese ecommerce giant **Alibaba (US:BABA)** accounts for 3.4 per cent and Taiwanese electronics company **Hon Hai Precision Industry (2317:TAI)** and Chinese internet giant **Tencent (700:HKG)** feature too.

Technology stocks are responsible for much of the recent emerging markets renaissance. The MSCI Emerging Markets index is up 23 per cent in the year to date and rose by 32.6 per cent in the 2016 calendar year, due in large part to the stellar performance of the technology sector, which now accounts for 26.6 per cent of the index.

Mr Hardenberg says it is his investments in disruptive smaller companies, introduced since he took over in October 2015, and his contrarian picks that have driven the fund's outperformance against the index. In 2016 Templeton delivered a share price total return of 47.9 per cent and it has already generated a 30.2 per cent return in the year to date.

"The reason we performed so well was because we picked a lot of good stocks, including consumer-orientated businesses such as the BMW subsidiary in China, which has doubled in value over the past 12 months. We also have two banks in Brazil, including **Itau Unibanco (ITUB4:SAO)**, a noodle and cookie producer in Brazil **(M Dias Branco (MDIA3:SAO)** and our holdings in the Philippines, such as bank **Banco De Oro (BDO:PHS)**, did well, too.

"We have an active share of around 80 per cent and this is still a truly contrarian portfolio that is not in any way close to the index even though some of the bigger names are well-known index names," he says.

But the tech theme is key to his vision too. When Mr Hardenberg took over in October 2015 he pledged to reduce the concentration in blue-chip emerging market stocks in traditional industries and open the trust's doors to exciting, nascent technological disrupters from across the emerging world.

His portfolio holdings have doubled in number since he took over and now contains 90 stocks, of which the majority of new additions have been mid- and small-caps. Around 32 per cent of the portfolio is now invested in stocks with a market capitalisation of under $50bn (£38.6bn). And he is dedicated to unearthing companies that are set to disrupt traditional industries. In order to do that he has recruited two teams of analysts solely to work on the information technology and healthcare sectors.

> 'Technology stocks are responsible for much of the recent emerging markets renaissance. The MSCI Emerging Markets index is up 23 per cent in the year to date'

In Latin America he has bought ecommerce companies such as **B2W Digital (BToW3:SAO)**. "This is an Amazon-like business in Brazil backed by the family that owns the Ambev brewery company. This business just didn't exist seven years ago and it is being backed by traditional local conservative money now," he says. In Kenya he added three companies, a brewery and two banks. "**Kenya Commercial Bank (KCBK:NAI)** is one of the main partners of [mobile payment company] M-PESA. Local banks give you exposure to all parts of the economy – they give loans to start-ups and alternative energy providers, which is why we buy them," he says.

He has also introduced Saudi Arabia to the portfolio for the first time and a new investment in Brazil, as well as a raft of healthcare-focused investments.

The nature of emerging markets stocks has changed, he says. "Emerging markets have now overtaken the west in terms of patent registration. And research and development has increased hugely too. Fintech is huge in emerging markets, healthcare is a business in its own right, as is technology. China is now the largest automotive maker in the world and that's totally new."

That brings with it different risks and a very different approach to valuation.

"Technology changes fast," says Mr Hardenberg. "For example, in the battery space it's totally unclear which battery technology will be the winner. This is a very different universe which requires us to have a different approach, learn a different language and use new tools to analyse these stocks.

"In the past we very much focused on cash flows and earnings multiples and it's still the case that discounted cash-flow analysis plays a very big role, but for some of the technology companies it's more important to quantify the ability of a management team to monetise an existing group of consumers and clients.

"In many cases they can be lossmaking for many quarters and years, and overnight they start charging for something and the company just begins to print money. You cannot find that in a number, so it's more about understanding the ability of management to turn existing businesses into more profitable businesses and you need to be able to understand the mindset of management."

Technology companies such as Alibaba, which currently trades on a price/earnings (PE) ratio of 56.94 times trailing 12-month earnings, certainly are not cheap on any number. How does that sit with a manager running a dedicated value-focused fund? Does Mr Hardenberg consider himself a value manager?

"Is that a trick question?" he asks. "I've trained my entire life as a value manager and I think the DNA of Templeton (where he has worked for 17 years) is to value companies. But does that mean that I only buy low PE ratio stocks? No, I'm an opportunistic manager who tries to understand the real value of companies and my passion is to uncover situations where we think the market is mispricing an asset.

"I respect value principles, but we've invested a lot of further resources and thinking to expand our understanding of value in emerging markets. We don't want to be stagnating and focusing on just a few companies and wait for them to fall to a low PE ratio. That's not going to give you much of a sexy portfolio."

MARKETS AND YOUR MONEY



Gold not the only thing glittering

Investors sought safety in August but bought risk assets, too

KATE BEIOLEY

Escalating tensions surrounding North Korea's nuclear ambitions resulted in a flight to gold and other perceived safe assets throughout August and punctured a run in US stocks. But by the end of the month risk assets were doing well too.

Gold, the yen and highly-rated government bonds started out the month on a high after US President Donald Trump waded into a war of words with North Korea. Trump promised to bring "fire and fury" to the state, North Korea mooted missile strikes near the US territory of Guam, and the world grew nervous.

On 10 August 2017 gold hit a two-month high and US stocks sank – a rare dip in an otherwise stratospheric year of gains for indices including the tech-heavy Nasdaq Composite and S&P 500. Even the recently sanguine CBOE Vix Volatility index, an indicator of investor anxiety (or lack thereof), spiked briefly.

That fear was replaced by renewed complacency in the middle of the month, and emerging markets and Asian equities continued to rise. But Japanese equity funds and gold funds still ended up among the top of the pile for the month. **Investec Global Gold (GB00B12B5S05)** returned the most of any open-ended fund in the calendar month and Japanese equity funds were among the best-performing Investment Association funds, too, mainly due to the performance of the currency. The country's main index, the Topix, actually fell over the month in local currency terms, but the Investment Association Japan Smaller Companies sector was the second best-performing sector across August.

Ben Yearsley, director at Shore Financial Planning, said: "August was the month of North Korea sabre rattling boosting the price of gold to over $1,300 an ounce and more worries about consumer debt, slowing growth and stagnating wages.

The market in a minute

Style:

GROWTH & QUALITY | VALUE

Assets:

GOLD | EQUITIES

Sectors:

MINING & INDUSTRIALS | BANKS & TELECOMS

Equities:

ASIA & EMERGING MARKETS | EUROPE

Bonds:

GILTS | HIGH-YIELD BONDS

"Are there any quiet months now in world markets? There always seems to be something going on unnerving investors – maybe that's a sign of toppy valuations?"

Mr Yearsley added: "Emerging markets had a good month, with both China and Russia performing well – the Hang Seng was the best performing of the major markets increasing by 2.25 per cent over the month."

The emerging markets story is partly one of recovery – after spending several years in the doldrums between 2011 and 2016 these stocks are still getting their mojo back. But there is more to the rebound, including political change, growing company earnings and the outperformance of tech stocks such as **Alibaba (US:BABA)** and **Tencent (HKG:700)**.

Chinese stocks have surprised some onlookers, though. Investors might have expected the issues surrounding North Korea to take a toll on the market's winning streak. Not so – the CSI 300 index was up around 6.2 per cent over the month while the Investment Association China and Greater China sector posted the best average gains of any open-ended fund sector for the month.

China bears point to the latent risks in China's debt-fuelled economy. But Beijing's market interventions have resulted in stronger-than-expected growth for the region. Alastair Winter, chief economist at Daniel Stewart & Co, says: "Although official data often seems remarkably in line with Mr Xi's targets there seems little doubt that China's economy is still growing much more rapidly than developed economies. The trouble is much of that growth is fuelled by debt that is becoming increasingly difficult to service even by public sector borrowers."

Meanwhile Harvey – the hurricane that tore through Texas at the end of the month – impacted the price of oil. The market was spooked by fears of a US oil shortage following the major storm and raised the price of oil. However, it did not last. The price of West Texas Intermediate oil remains far lower than at the start of the month, at $47.51 per barrel.

Winners and losers

Top-performing open-ended funds over August were Investec Global Gold and **Invesco Perpetual Japanese Smaller Companies (GB00BJ04J523)**, followed by **Neptune Russia (GB00B86WB793)**. The biggest fallers were **MFM Techinvest Technology (GB0032832841)** and **Woodford Equity Income (GB00BLRZQB71)**.

Renowned manager Neil Woodford has had a bleak few months, too. He was punished for his holding in doorstep lender Provident Financial, whose shares lost two-thirds of their value in a single day on Tuesday 22 August following its second profit warning in three months. The previous month saw him licking his wounds from share price falls at **AstraZeneca (AZN)**, AA (AA) and **Imperial Brands (IMB)**, among others. The fund lost 4.01 per cent between 1 August and 1 September 2017.

Mr Yearsley says: "Don't write Neil Woodford off just yet, but by his standards it is two dreadful months in a row with his three biggest holdings having a torrid time."

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TAKING STOCK

Ian Smith is companies editor



FTSE 100 comings and goings

The bear case on the risers and the bull case on the fallers

Joining the big league is more than a prestige moment for listed UK corporates. United Arab Emirates-based private healthcare provider **NMC Health (NMC)** and housebuilder **Berkeley Group (BKG)** made the step-up in the September reshuffle: a share price fillip the reward from FTSE 100 tracker funds making some room for these two new holdings.

We picked NMC as one of the stocks in our own portfolio of 'Brexit-proof' stocks back in our late June feature, when the shares were trading at around 2,186p; they are testing new highs at 2,725p. The rationale was that the company is protected from a weaker pound, earning its revenue in a currency pegged to the dollar, while its operations are insulated from a tortuous UK-EU divorce. Acquisition-led growth in an expanding private healthcare market is feeding an upgrade cycle.

What can go wrong? Well, the company's recent half-year results reflected some of the stress of that growth. Net debt has broken the billion-dollar mark, equating to three times expected full-year cash profits. In the first half, $609m of net cash went on acquisitions compared to $98m generated from operations. Analysts see balance sheet room for further acquisitions, but the risk – simply, if starkly put – is that operational problems, perhaps caused by regulatory change, threaten the company's ability to continue as a going concern.

Readers won't need much of a recap on Berkeley's current fortunes. Its shares are reaching all-time highs at more than 3,700p, as selling prices keep rising and a programme of dividends and buy-backs are returning a big chunk of its market value to shareholders.

> 'What makes Royal Mail unique is also what makes it unprofitable: an obligation to deliver letters, whether profitable or not'

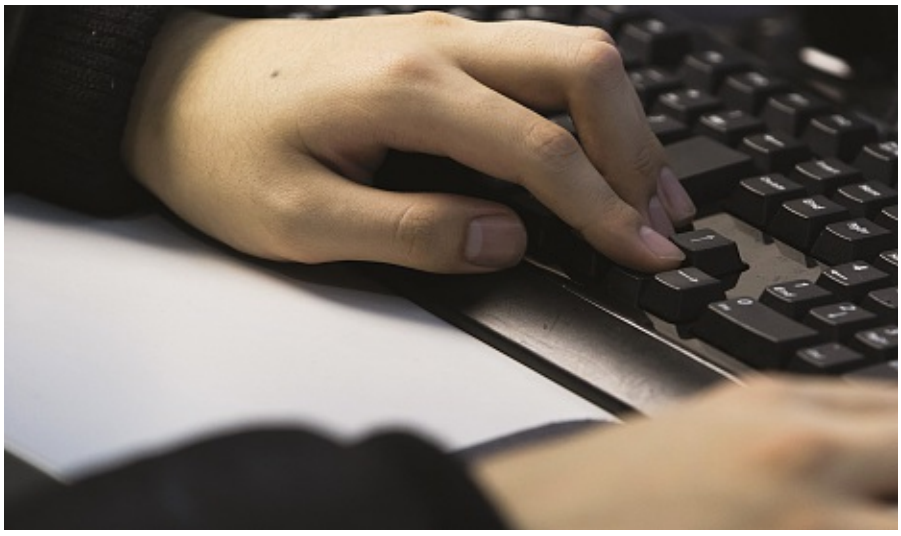
Valuation does present a threat, though. The shares are valued at 2.5 times the housebuilder's book value per share, against a sector average of 2.1 times, and a historical average of 1.4 times running back to the late 1990s. If the market is working effectively then all that shareholder return is in the price, and new buyers will find it tricky to make a buy case; especially given uncertainty over the housing market and mounting political discomfort on the sector's Help to Buy-assisted profitability. Forgive me if you've heard that one before.

Leaving the party are **Royal Mail (RMG)** and **Provident Financial (PFG)**. Both businesses are suffering from industry change. Five hundred and one years since the first Master of the Posts was appointed by Henry VIII, what makes Royal Mail unique is also what makes it unprofitable: an obligation to deliver letters, whether profitable or not. The higher-margin parcels delivery service has Amazonian-sized challenges. Not to mention a long-running dispute over pensions.

It is difficult to make the bull case for Royal Mail. Still, on almost every valuation it looks cheap against its recent history as a listed company and its international peers. Its enterprise value is 0.4 times sales: if the company can manage any kind of earnings growth (Liberum analysts forecast nothing in the next two years), its fortunes could change.

When it comes to the Provvy, the buy call is a little easier to countenance, as reflected by the shares' bounce from their nadir last month. If the regulatory investigation into its Vanquis credit card does not turn out to be a redress issue, then much certainty will return to the forecast profitability. And returning home credit managing director Chris Gillespie could stop the rot in the doorstep loans business. The underlying credit quality of Provident's customers has not deteriorated, which would support a recovery take.

There's a few fairly big variables there, and this column, like much of the market, had argued after the first warning that there was "little point in Provident turning back" ('Are you listening carefully?', 28 July 2017). Perhaps there was a point, although the damage may have already been done. The Provvy had been a case study in reshaping an analogue business for the digital age. The latest chapter reminds us of the risks of top-down re-organisations.

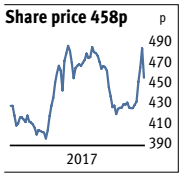


Alfa achieved strong top-line growth and improved its customer pipeline in the first half

SOFTWARE & COMPUTER SERVICES

Alfa lands on its feet

Alfa Financial Software's (ALFA) revenue topped analysts' expectations in its maiden results since listing on the main market in June this year. Sales were partly buoyed by currency movements: the US accounts for 45 per cent of Alfa's turnover. But, at constant currencies, the top line still rose by 29 per cent. The company, which specialises in software for the asset finance industry, also saw adjusted earnings before interest and taxation of £21.4m; up 77 per cent against the first half of 2016. The market reacted positively, sending its shares up 5 per cent on results day.



Alfa was the biggest UK technology IPO since 2015. The offer price implied a market capitalisation of £975m, but the shares leaped on their debut. Today, the market capitalisation is £1.37bn. Its main product is Alfa Systems, a software platform that provides pricing, contract and customer management and other services to asset finance providers. It is billed as a "highly scalable and flexible" product that allows clients to adapt to a changing regulatory environment.

In the IPO prospectus, reasons for listing included raising the group's profile, potential benefits in "recruiting, retaining and incentivising key management and employees" and giving the selling shareholder a return on its investment: that was CHP Software & Consulting Ltd.

Alfa secured two clients in the first half, against a target of two or three in the full year, taking the total to 31. One is a global equipment manufacturer and finance group, which will see the Europe-wide implementation of Alfa Systems, and the other is a US auto finance provider.

The company's net cash position fell to £20.5m from £36m a year earlier, driven by pre-IPO dividend payments of £33.7m (net of loan repayments), and non-recurring IPO costs of £3m. On the prospect of future dividend payments, management explained that Alfa is cash generative, but wants "optionality".

Analysts at Numis forecast pre-tax profit of £41.3m and EPS of 10.6p for FY2017, up from £33.4m and 8.6p in 2016.

These maiden results are encouraging, with strong top-line growth, customer wins and a 94 per cent staff retention rate. But Alfa's shares are trading on an eye-watering forward multiple of 43 times forecast earnings. We stay neutral, awaiting a longer post-IPO performance track record. *HC*

Hold

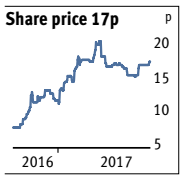
Ord Price: 458p **Market Value:** £1.37bn
Touch: 457-458p **12-Month High:** 494p **Low:** 395p
Dividend Yield: nil **PE Ratio:** na
Net Asset Value: 12.8p* **Net Cash:** £20.5m
*Includes intangible assets of £24.7m, or 8.2p a share

Half-year to 30 Jun	Turnover (£m)	Pre-tax profit (£m)	Earnings per share (p)	Dividend per share (p)
2016**	28.7	12.2	2.61	nil
2017**	45.1	14.0	3.58	nil
% change	+57	+15	+37	nil

**Alfa joined the main market in June 2017 Excludes pre-IPO dividends
Last IC view: None

AIM: MINING

Base turns a maiden profit



Four years after first production from **Base Resources' (BSE)** mineral sands plant at Kwale in Kenya, the company has generated a maiden profit. A 20 per cent uptick in ore mined was outweighed by a fall in heavy mineral grade, resulting in a 3.5 per cent drop in plant output. Instead, it was higher sales volumes, and a strengthening of ilmenite and zircon prices, that boosted earnings before interest and tax by 449 per cent to A$60.1m (£37m).

Operating costs – or as Base reports 'cost of goods sold' – remained constant at A$88.6m, which translated to a revenue to cost of sales ratio of 2.4, up from 2.0 a year ago. The metric is managing director Kim Carstens' preferred method of measuring the company, unsurprising given broker Numis expects post-tax profit to sharply decline in 2019 and 2020 after peaking at A$66.6m (with earnings per share of 9¢), in the current financial year.

Accordingly, investors should look beyond the excellent cash generation reflected in these results and promised in Numis's 50 per cent free cash-flow yield estimate for 2018. That's because grades are set to fall further. To compensate, the board has given the green light to Kwale Phase 2, which will maximise the feed of concentrate to the mineral separation plant, thereby boosting production volumes.

Base investors can point to three sources of reassurance: buoyant pricing in the titanium dioxide and zircon markets, a sharp decline in outstanding debt, and the prospect of exploration upside. Reliance on the latter leaves us somewhat nervous. *AN*

Hold

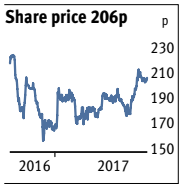
Ord Price: 17p **Market Value:** £128m
Touch: 16.5-18p **12-Month High:** 21p **Low:** 7p
Dividend Yield: nil **PE Ratio:** 10
Net Asset Value: 31.6¢ **Net Debt:** 55% £1=A$1.62

Half-year to 30 Jun	Turnover (A$m)	Pre-tax profit (A$m)	Earnings per share (¢)	Dividend share (¢)
2013	0.1	-6.7	-1.25	nil
2014	29.1	-14.0	-2.50	nil
2015	146	-16.0	-2.85	nil
2016	169	-20.9	-3.41	nil
2017	215	28.8	2.85	nil
% change	+27	–	–	–

Last IC view: None

TRAVEL & LEISURE

Expansion plans at Gym



More people are lacing up their trainers and heading to **Gym (GYM)** locations – 19 per cent more to be exact – as the group has clocked an average 500,000 members. To accommodate them, six new sites were opened over the period, bringing the total number to 95. As such, cash profit reported was nearly a fifth higher at £13.7m, although this was helped by an accounting change that added £0.8m to the bottom line. Margins also appeared stable at 32 per cent although, take into account that change in depreciation policy, and underlying margins actually fell 180 basis points. What's more, there also appeared to be little momentum in average revenue per customer, which remained relatively flat at £14.49.

But Gym is pressing on with new plans, specifically with a trial of its premium membership across 40 of its locations. For an extra £5 a month premium members will enjoy access to multiple Gym sites, be able to bring a friend, and access services that help track their fitness progress. A new digital member management system was launched in July, which chief executive John Treharne believes will make operations more efficient by cutting staff costs.

Analysts at broker Numis Securities expect pre-tax profit of £12.4m in the year to December 2017, giving EPS of 7.5p, compared with £8.7m and 5.6p in 2016.

Management expects to open a total of 20 new sites this year, but we're still concerned about rising levels of competition in the private, budget gym sector and how this could impinge on underlying growth. The shares are now trading at 27 times earnings, which arguably prices in any near-term growth prospects, but leaves little room for error. *JF*

Sell

Ord Price: 206p **Market Value:** £264m
Touch: 206-208p **12-Month High:** 235p **Low:** 155p
Dividend Yield: 0.5% **PE Ratio:** 34
Net Asset Value: 92p* **Net Debt:** 4%
*Includes intangible assets of £48.8m, or 38p a share

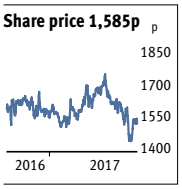
Half-year to 30 Jun	Turnover (£m)	Pre-tax profit (£m)	Earnings per share (p)	Dividend per share (p)
2016	36.1	3.4	2.0	0.25
2017	42.8	5.9	3.5	0.30
% change	+19	+75	+75	+20

Last IC view: Sell, 184p, 15 Mar 2017 | Ex-div: 7 Sep | Payment: 29 Sep

INDUSTRIAL TRANSPORTATION

James Fisher delivers growth

The engineering company has kept up with its reputation of improving profits and margins despite difficult conditions. Foreign exchange rates helped half-year results from **James Fisher & Sons (FSJ)** beat analysts' expectations. Operating profit grew by 7 per cent at actual exchange rates although, even at constant currencies, they still rose 4 per cent to £21.3m. This was driven largely by the specialist technical division, as defence and diving equipment business JFD enjoyed a full contribution from the Indian submarine rescue project compared with just three months worth during the first half of 2016.



Marine support also fared well, with revenue up by 14 per cent to £105.6m. The group started operating in Brazil, which helped offset weaker volumes in ship-to-ship transfers in Asia Pacific, while South African marine service business Subtech managed to win contracts in the Middle East and West Africa.

These performances helped make up for the offshore oil segment, where revenue fell 7 per cent at constant currencies. Chief executive Nick Henry said that maintenance activity in the oil and gas sector had begun to pick up, which should lead to stronger growth in the second half. Analysts at Investec expect pre-tax profit of £50.7m in the year to December 2017, giving EPS of 84.6p, compared with £45.8m and 76.3p in 2016.

The company has continued to grow underlying profit and margins despite tough market conditions due to its geographic and operational spread. Given the group's defensive nature, and the fact that the shares are trading near our buy tip valuation at 19 times earnings, we see no reason to lose faith at this stage. *JF*

Buy

Ord Price: 1,585p **Market Value:** £796m
Touch: 1,580-1,588p **12-Month High:** 1,775p **Low:** 1,436p
Dividend Yield: 1.7% **PE Ratio:** 20
Net Asset Value: 525p* **Net Debt:** 49%
*Includes £186m of intangible assets, or 370p a share

Half-year to 30 Jun	Turnover (£m)	Pre-tax profit (£m)	Earnings per share (p)	Dividend per share (p)
2016	209	17.4	29.6	8.55
2017	236	17.6	28.7	9.40
% change	+13	+1	-3	+10

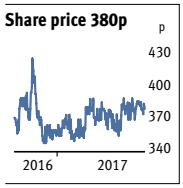
Last IC view: Buy, 1,598p, 9 Mar 2017 | Ex-div: 5 Oct | Payment: 3 Nov

MEDIA

Gloomy forecast for STV

Rob Woodward may have presented his last set of results as chief executive of **STV (STVG)** with an air of confidence – which is mirrored by a 25 per cent hike in the dividend – but the numbers tell a different story. Weakness in the UK's TV advertising market has left the Scottish broadcaster nursing a 10 per cent fall in advertising revenue, a decline which is expected to continue until at least the end of September.

That negative outlook is not surprising given the difficulties recently reported by ITV, which sells all of the advertising space on STV's main channel. Even so, broker Numis has trimmed its revenue forecasts for both the current financial year and next. However, pre-tax profit and EPS in the year to December 2017 are expected to be flat at £18.5m and 39p, respectively.



Outside of the core broadcasting operations, the outlook is slightly brighter. In April, STV launched its second channel which is already attracting over 900,000 monthly viewers. Since its launch, advertising revenue on the channel – which STV sells itself – has risen fourfold. Revenue at the production arm is also expected to tick up in the second half after four new commissions from the BBC in the reported period. Meanwhile, demand for online advertising sent group digital revenue up 14 per cent to £4m.

Attempts at diversification away from merely broadcasting ITV in Scotland are certainly welcome, but progress is slow. The vast majority of STV's revenue still comes from that partnership and its production company remains unprofitable. Despite a lowly forward price-to-earnings ratio of just 10 times, we remain at hold. *MB*

Hold

Ord Price: 380p **Market Value:** £150m
Touch: 380-385p **12-Month High:** 440p **Low:** 348p
Dividend Yield: 4.2% **PE Ratio:** 14
Net Asset Value: * **Net Debt:** £34m
*Negative shareholders' funds

Half-year to 30 Jun	Turnover (£m)	Pre-tax profit (£m)	Earnings per share (p)	Dividend per share (p)
2016	56.2	10.2	21.2	4.0
2017	54.6	7.5	16.2	5.0
% change	-3	-26	-24	+25

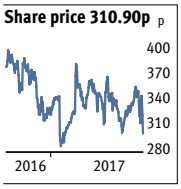
Last IC view: Hold, 360p, 6 Mar 2017 | Ex-div: 28 Sep | Payment: 27 Oct

TRAVEL & LEISURE

Restaurant Group cuts prices

When Andy McCue took over as chief executive of **Restaurant Group (RTN)** he identified the previous management team's desire to keep prices up as one of the key problems holding the company back. Part of his turnaround strategy was to cut prices, and this is clearly under way in the first half of the year.

Frankie & Benny's has launched a more competitive menu with comparable dishes an average of 7 per cent cheaper and the cheapest priced dish for each category reduced by more than a fifth. Marketing has also targeted lapsed customers with discounts and seasonal promotions. Chiquito reintroduced fixed price value menus and is trialling a new menu with more competitive prices at 20 of its locations. Another element of the strategy involves making the business more efficient, with £10m of costs expected to be saved by the end of the year.



Like-for-like sales fell 2.2 per cent over the period, although this was better than analysts had been predicting. This decline, along with inflationary cost pressures and lower prices, put pressure on operating margins – down 2.6 percentage points to 7.9 per cent – leading to a 30 per cent fall in adjusted operating profit to £26.5m. Analysts at Numis expect pre-tax profit of £59.2m in the year to December 2017, giving EPS of 23.2p, compared with £77.2m and 30p in 2016.

Free cash flow remained relatively flat at £35.1m, which helped management maintain the dividend. The turnaround at Restaurant Group will take some time, but we're encouraged with the cost-cutting and new menus so far. Shareholders can enjoy a 5.1 per cent forward dividend yield, which at 13 times forward earnings, still makes the shares good value in our view. *JF*

Buy

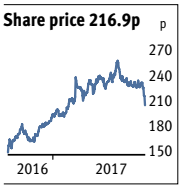
Ord Price: 310.90p **Market Value:** £625m
Touch: 310.90-311.40p **12-Month High:** 410p **Low:** 282p
Dividend Yield: 5.6% **PE Ratio:** na
Net Asset Value: 95p **Net Debt:** 10%

Half-year to 2 Jul	Turnover (£m)	Pre-tax profit (£m)	Earnings per share (p)	Dividend per share (p)
2016	359	-22.5	-11.2	6.80
2017	333	2.8	0.6	6.80
% change	-7	–	–	–

Last IC view: Buy, 348p, 26 May 2017 Ex-div: 14 Sep Payment: 12 Oct

CONSTRUCTION & MATERIALS

Melrose given the brush-off



The share price of **Melrose Industries (MRO)** pulled back on the publication of these results even though the turnaround specialist managed to follow up a reported pre-tax loss at the 2016 half year with a profit this time around. Melrose, which has a reputation for acquiring distressed manufacturing companies and putting them back on track, revealed that trading at its Brush subsidiary, which sells specialist equipment to the oil and gas industry, had continued to deteriorate. With "no recovery in generators expected in the foreseeable future", the Brush business is now subject to a detailed review, but the news dampened sentiment despite some positive developments elsewhere.

The glaring disparity in the comparative top line is due to the marquee deal to acquire Nortek in August 2016. Nortek, a manufacturer of high-end air-conditioning systems for industry, along with security systems for homes and offices, contributed £987m in revenue and £146m in underlying operating profit; the former was flat on a pro-forma basis, while the latter represented an increase of 54 per cent on an impressive 5.5 percentage point increase in the underlying margin to 14.7 per cent.

JPMorgan Cazenove gives adjusted earnings before interest and taxation of £282m for the December year-end, leading to EPS of 9.6p, against £104m and 4.4p in 2016.

Brush came as part of the 2008 deal to acquire manufacturing conglomerate FKI, but no one could have predicted the prolonged slump in oil prices that has seen industry capital budgets slump. The shares look cheap across a range of metrics, but harsh medicine may be needed. *MR*

Hold

Ord Price: 216.9p **Market Value:** £4.21bn
Touch: 216.7-216.9p **12-Month High:** 262p **Low:** 146p
Dividend Yield: 1.5% **PE Ratio:** nil
Net Asset Value: 102p* **Net Debt:** 34%
*Includes intangible assets of £2.45bn, or 126p a share

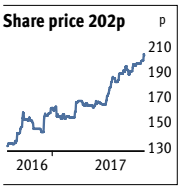
Half-year to 30 Jun	Turnover (£bn)	Pre-tax profit (£m)	Earnings per share (p)	Dividend per share (p)
2016**	0.10	-9.2	-0.6	0.3
2017	1.09	47.8	2.0	1.4
% change	+937	–	–	+367

**Restated for August 2016 rights issue
Last IC view: Hold, 240p, 6 Jul 2017 Ex-div: 7 Sep Payment: 6 Oct

AIM: FOOD & DRUG RETAILERS

Total Produce grows in North America

Fruit and veg supplier **Total Produce (TOT)** has continued its push into North America by upping its stake in Oppenheimer Group – which under its Oppy brand supplies 'Irresistible Mexican blackberries' and 'Juicy California grapes' – from 35 per cent to 65 per cent. In addition, Progressive Produce, the Los Angeles-based company in which Total also holds a 65 per cent stake, acquired Keystone Fruit Marketing in a push for scale. Acquisitions helped to drive up revenue in spite of foreign exchange headwinds. On a like-for-like basis revenue was up 4 per cent, largely due to price increases.



Trading conditions in America were difficult. Volumes were up but they were also higher in the wider market which meant lower pricing, and bad weather led to a decline in produce quality. Across Europe, however, things looked better, with cash profits for eurozone and non-eurozone operations up 3.9 per cent and 11.7 per cent, respectively, with the eurozone being held back by continued challenges in Holland.

Bloomberg consensus forecasts have adjusted earnings per share, climbing to 13¢ for the full year 2017, then remaining flat in 2018 (12¢ in 2016).

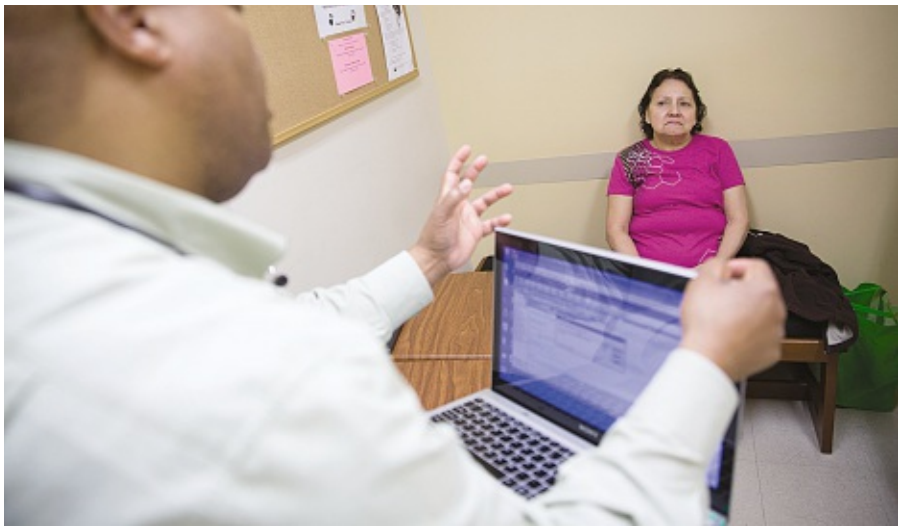
Acquisition activity has predictably led to a jump in the net debt figure and despite a decline in the pension deficit, the pension-adjusted net debt increased as a proportion of total equity from 44 per cent at the end of June 2016 to 58 per cent. It's not a concern yet but investors should keep an eye on it in future updates. At 17 times forecast earnings, the shares are more or less in line with peers and we think this makes it a prudent time to return to hold. *TD*

Hold

Ord Price: 202p **Market Value:** £648m
Touch: 198-205p **12-Month High:** 203p **Low:** 134p
Dividend Yield: 1.4% **PE Ratio:** 20
Net Asset Value: 73¢* **Net Debt:** 50%
*Includes intangible assets of €292m, or 91¢ a share £1=€1.08

Half-year to 30 Jun	Turnover (€bn)	Pre-tax profit (€m)	Earnings per share (¢)	Dividend per share (¢)
2016	1.91	25.6	4.77	0.81
2017	2.15	35.4	6.95	0.89
% change	+12	+39	+46	+10

Last IC view: Buy, 161p, 3 Mar 2017 Ex-div: 14 Sep Payment: 13 Oct

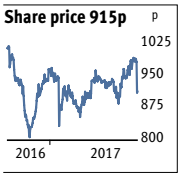


Healthcare software company EMIS has faced up to the challenges of falling NHS spending

AIM: SOFTWARE & COMPUTER SERVICES

EMIS solid in turbulent UK health sector

The beauty of providing data services to big organisations is that once customers sign up, they are likely to stay. That is particularly true in healthcare, where patient information is sensitive and the implications of losing data are high. Software specialist **EMIS (EMIS)** continues to benefit from these dynamics. Recurring revenue – defined by the group as contracted or habitually repeating sales – rose 4 per cent to £66.8m in the six months to June 2017, and now makes up 84 per cent of total group revenue.



But the financial struggles of the NHS means new customers are harder to come by. The acute care division has been especially hurt by falling spending by the health service. A reduction in large one-off projects sent revenue there down 14 per cent.

The UK's pharmacies are also feeling the force of a reduction in NHS spend but this has had a positive impact on EMIS's Community Pharmacy (EHCP) segment. To plug the revenue gap left by lower NHS spending, pharmacies are increasingly turning to the software provider in a bid to offer their customers more services. As a result, EHCP revenue rose 5 per cent, and operating profit rose 16 per cent. The outlook for the division is also buoyant due to the impending rollout of its ProScript Connect dispensary management product into the Celesio pharmacy estate. This is expected to drag EMIS's share of the UK pharmacy market up from 37 to 50 per cent by the end of 2019.

The outlook is also improving in the group's two smallest divisions, Specialist & Care (eye screening and other services) and medical information service Patient.info. The former increased its market share from 18 per cent at the year-end to 26 per cent, and the latter reported a 42 per cent rise in revenue in the first half.

Reported profit was dented by the 'reorganisation programme', which resulted in a £2.5m exceptional charge. But lower staff and operating expenses is expected to save £3.5m over the full year. Even so, the ongoing costs of the restructuring means broker Numis expects pre-tax profit and EPS to fall to £37.5m and 47.1p, respectively, in the year to December 2017 (from £39m and 49.2p in 2016).

In spite of the challenges caused by the struggling NHS, these are characteristically strong results. EMIS is well placed for the demands of the UK's healthcare market and its shares trading on 19 times forward earnings fail to reflect that. *MB*

Buy

Ord Price: 915p **Market Value:** £579m
Touch: 914-917p **12-Month High:** 1,050p **Low:** 793p
Dividend Yield: 2.7% **PE Ratio:** 32
Net Asset Value: 175p* **Net Cash:** £10.5m
*Includes intangible assets of £106m, or 168p a share

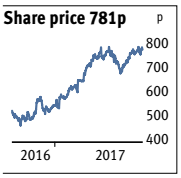
Half-year to 30 Jun	Turnover (£m)	Pre-tax profit (£m)	Earnings per share (p)	Dividend per share (p)
2016	78.7	12.2	14.9	11.7
2017	79.2	10.7	13.1	12.9
% change	+1	-12	-12	+10

Last IC view: Buy, 862p, 23 Mar 2017 | Ex-div: 21 Sep | Payment: 27 Oct

SUPPORT SERVICES

Grafton doubles down in the Netherlands

Grafton (GFTU), better known for its building merchant subsidiaries Selco, Buildbase and Plumbase, has had a great start to 2017. Against a decent rise in the top line, profits grew by double digits on both a statutory and adjusted basis in the six months to June, motored by the Irish merchanting business, where operating profit increased 39 per cent at constant currencies to £16.5m. Encouragingly, a step-up in investment was vindicated by a 13.2 per cent return on capital employed, a gain of 70 basis points year on year.



Although its size precluded a major impact on the bottom line, the Netherlands merchanting division was the star performer. January's acquisition of the 14-branch Gunters en Meuser business, together with market-beating growth, fed through to a 38 per cent swell in revenue at constant currencies. This expansion caused a 90 basis point decline in the adjusted operating margin. At 10.4 per cent, this is still 4.8 percentage points higher than the UK average, and explains why analysts at broker Numis think the Netherlands should form management's primary focus amid expectations of a flat period of domestic trading ahead.

Those same analysts are guiding for pre-tax profit of £149m and EPS of 50.9p in the year to December 2017, up from £136m and 47.4p in 2016.

The second half has started in earnest, with daily like-for-like revenue up 6.5 per cent in the eight weeks since 1 July, and if continental expansion continues apace the shares' momentum should continue. But against "sustained" softer trends in the UK market, a 15 times forward earnings multiple dampens our appetite to buy. *AN*

Hold

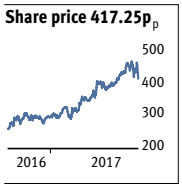
Ord Price: 781p **Market Value:** £1.8bn
Touch: 780-782p **12-Month High:** 800p **Low:** 462p
Dividend Yield: 1.8% **PE Ratio:** 18
Net Asset Value: 472p* **Net Debt:** 7%
*Includes intangible assets of £640m, or 270p a share

Half-year to 30 Jun	Turnover (£bn)	Pre-tax profit (£m)	Earnings per share (p)	Dividend per share (p)
2016	1.23	62.8	21.5	4.75
2017	1.34	74.1	25.5	5.25
% change	+9	+18	+19	+11

Last IC view: Hold, 658p, 7 Mar 2017 | Ex-div: 7 Sep | Payment: 5 Oct

FINANCIAL SERVICES

Arrow Global heads to Ireland



Arrow Global (ARW) intends to continue its march across Europe via its acquisition of UK and Ireland mortgage servicing company Mars Capital for an enterprise value of £15.5m. The purchase would represent its first foray into the Irish distressed debt market. Chief executive Lee Rochford says the market is attractive because of the large number of non-performing loans still on banks' balance sheets and the desire by these lenders to continue to deleverage.

After completing its purchase of Zenith Services during the first half, management committed to acquiring two small loan portfolios for €10m (£9.2m). Arrow Global grew its assets under management in Italy by €2bn since the start of the year by using Zenith's relationships with Italian institutional investors.

In total, the distressed debt collection specialist increased its organic loan portfolio purchases by almost a third to £125m, with a face value of £968m. Core collections were up 11 per cent as a result of its growing asset base. Expected remaining collections for the next 84 months – an important pipeline measure – rose almost a quarter year on year to £1.5bn.

Analysts at Shore Capital expect adjusted net assets of 107p a share at 31 December 2017.

During the six months to the end of June, Arrow's overall collections performance represented 103 per cent of the original forecast, indicating the effectiveness of its data-driven collecting approach. The shares are up solidly on our buy tip (375.75p, 27 April 2017) and trade at 3.9 times forecast net assets and are becoming more fully valued. However, its strong collections record and the fragmented nature of the European distressed debt market keeps us buyers. *EP*

Buy

Ord Price: 417.25p **Market Value:** £731m
Touch: 417.25-417.75p **12-Month High:** 480p **Low:** 250p
Dividend Yield: 2.3% **PE Ratio:** 52
Net Asset Value: 93p* **Net Debt:** £930m
*Includes intangible assets of £184m, or 105p a share

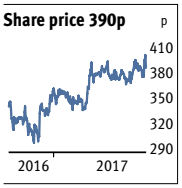
Half-year to 30 Jun	Turnover (£m)	Pre-tax profit (£m)	Earnings per share (p)	Dividend per share (p)
2016	102	20.5	9	2.7
2017	150	4.9	2	3.2
% change	+47	-76	-78	+19

Last IC view: Buy, 357.75p, 27 Apr 2017 | Ex-div: 7 Sep | Payment: 3 Oct

LIFE INSURANCE

Chesnara's cash rises with markets

Chesnara's (CSN) April acquisition of Legal & General's (LGEN) Dutch business – rebranded Scildon – provided a one-off £20.7m boost to the closed book life assurance consolidator's profit during the first half. However, it was its pre-existing UK,



Swedish and Dutch businesses that allowed it to do exactly what the market had hoped, increasing its cash generation and half-year dividend payment.

Overall cash generation more than trebled to £46m, with two-thirds of that coming from the domestic business, which benefited from £9m of previously trapped surplus capital being extracted from two ring-fenced with-profit funds. Improved equity markets also helped increase the business's economic value by £22m.

That was also true for the Swedish and Dutch businesses. Assets under management at Swedish open book life business Movestic increased by £0.3bn on the December year-end, helping push up its economic value by 6 per cent to £243m. Scildon – which is also open to new business – generated £1.7m in new business profit and increased its share of the term assurance market to 7.4 per cent. Management also derisked the business's portfolio, reducing its equity exposure and investing in lower-risk assets, which also cut its capital requirements.

House broker Shore Capital expects economic value of 455p a share at December 2017, up from 390p (ex-dividend) in 2016.

The shares are up on our buy tip (326p, 9 July 2015) and trade at an undemanding 0.9 times forecast economic value. With a potential dividend yield of 5.1 per cent, the shares remain a buy. *EP*

Buy

Ord Price: 390p **Market Value:** £584m
Touch: 390-393p **12-Month High:** 402p **Low:** 291p
Dividend Yield: 5% **PE Ratio:** 7
Net Asset Value: 286p* **Solvency II Ratio:** 143%
*Includes intangible assets of £190m, or 127p a share

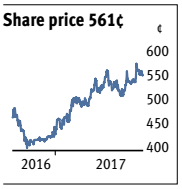
Half-year to 30 Jun	Net premiums (£m)	Pre-tax profit (£m)	Earnings per share (p)	Dividend per share (p)
2016	32.9	0.2	0.4	6.8
2017	66.4	51.6	31.2	7.0
% change	+102	–	–	+3

Last IC view: Buy, 357.75p, 3 Apr 2017 | Ex-div: 7 Sep | Payment: 11 Oct

TRAVEL & LEISURE

Shipping boosts Irish Continental

Transporting 175,000 cars, 700,000 passengers and 163,000 containers between Ireland, the UK and Europe helped **Irish Continental (ICGC)** book a 3.7 per cent increase in revenue in the first half (see table). But fuel costs increased by almost half – a result of the rebounding oil price – so this strong top-line performance fed through to



fall in underlying operating profit from €20.8m (£19.1m) to €19.1m.

But reported numbers benefited from the €44.7m sale of the MV Kaitaki ferry to New Zealand transport company KiwiRail. According to management, the ship had become "surplus to ICG's operational requirements" since the acquisition of cruise ferry Ulysses in 2001. The sale also helped ICG swing into a net cash position despite a slight fall in free cash inflows in the period.

Booming imports in Ireland kept demand for container shipping high, which helped spark a 5.7 per cent increase in revenue and a 1.5 per cent rise in adjusted cash profit in the container and terminal division. This helped offset a slightly disappointing 4.2 per cent decline in adjusted cash profit in the ferries division.

Consensus forecasts are for a 2017 adjusted pre-tax profit of €68m, giving adjusted EPS of 30.3¢ (from €60.4m and 31¢ in 2016). Beyond that, the arrival of a new ship in 2018 should provide further capacity for earnings growth.

Recent strong demand for Irish Continental's shares have given them a forward price-to-earnings ratio of 19 times. That seems fair given the group's growth opportunities and its exposure to Brexit-related uncertainty, foreign currency movements and the oil price. *MB*

Hold

Ord Price: 561¢ **Market Value:** €1.06bn
Touch: 546-566¢ **12-Month High:** **Low:** 404¢
Dividend Yield: 2.1% **PE Ratio:** 13
Net Asset Value: 101¢ **Net Cash:** €26.7m £1=€1.09

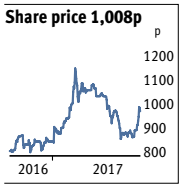
Half-year to 30 Jun	Turnover (€m)	Pre-tax profit (€m)	Earnings per share (¢)	Dividend per share (¢)
2016	151	19.7	10.3	3.82
2017	156	47.5	22.8	4.01
% change	+4	+141	+121	+5

Last IC view: Hold, €5.08, 7 Mar 2017 | Ex-div: 21 Sep | Payment: 6 Oct

AIM:H'HOLD GOODS & HOME CONSTRUCTION

Churchill tilts towards exports

While bureaucrats wrangle over the terms of the UK's eventual exit from the European Union, businesses up and down the country simply have to get on with it. **Churchill China's (CHH)** half-year figures provide a case in point. Despite uncertainties over our future trading arrangements, the Stoke-based ceramics manufacturer has been steadily building its export base in continental Europe and beyond. Exports accounted for 57 per cent of first-half revenue, up from 49 per cent at the December year-end.



With sterling in retreat, the rise in exports has bolstered revenue, effectively adding £1.3m to the top line, although the impact on earnings was muted due to an increase in imported raw material costs. At constant currencies, revenue was up 2 per cent, with the growth in the hospitality segment offsetting continued weakness in the domestic retail market.

Churchill has also successfully increased the proportion of the top line derived from "higher margin added value products". They now account for 40 per cent of revenue generated by the hospitality segment, a seven percentage point increase from the 2016 half-year.

N+1 Singer gives adjusted pre-tax profit of £7.5m and EPS of 54.9p for the year-end, against £6.6m and 48.6p in 2016.

The group's hospitality markets are growing at 2-3 per cent a year. Management is looking to build market share on the back of sterling depreciation, while the transition to an value-added range has had a favourable impact on margins. Churchill is delivering on its strategic objectives, and its move up the value chain acts as another barrier to entry. We see scope for the share price to revert to its historic premium to peers on an enterprise value to cash profit basis. *MR*

Buy

Ord Price: 1,008p **Market Value:** £111m
Touch: 990-1,025p **12-Month High:** 1,175p **Low:** 800p
Dividend Yield: 2.2% **PE Ratio:** 19
Net Asset Value: 264p **Net Cash:** £10.4m

Half-year to 30 Jun	Turnover (£m)	Pre-tax profit (£m)	Earnings per share (p)	Dividend per share (p)
2016	24.0	2.0	14.8	6.3
2017	25.8	2.7	19.6	7.4
% change	+8	+30	+32	+17

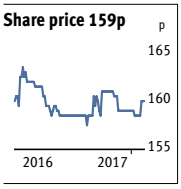
Last IC view: Buy, 895p, 18 Aug 2017 Ex-div: 7 Sep Payment: 5 Oct

AIM: INDUSTRIAL TRANSPORTATION

Eddie Stobart in growth mode

Eddie Stobart Logistics (ESL) was spun out from the larger Stobart Group (STOB) to reduce its debt and further its acquisitive growth strategy. Joining Aim in April this year helped fund its £45m takeover of e-commerce logistics specialist iForce. After the period-end, ESL took a 50 per cent stake in business-to-businesss specialist Speedy Freight. Chief executive Alex Laffey says future acquisitions are on the cards, although most announced deals have been "in the works for some time".

The advantage of these transactions, in Mr Laffey's view, isn't limited to cross-selling opportunities or cost synergies. These deals bring with them "a strong contracted customer base", he says.



Although these numbers only include a small contribution from iForce, the business is trading in line with management's expectations.

Group profitability was dented by one-off IPO-related expenses, although revenue on an underlying basis rose by a solid 13 per cent. This reflected revenue growth across the manufacturing, industrial and bulk segment of 22 per cent, and 51 per cent in e-commerce contracts.

Cenkos expects pre-tax profit of £41.3m for the year ending November 2017, giving EPS of 11p, against £25.6m and 10.9p in FY2016.

ESL seems to know what it's already good at, but also where acquisitions could help it grow. Much of this will depend on maintaining a healthy balance sheet, so it was encouraging that the period provided free cash inflow of £11.1m, with more than half of underlying cash profit converting. The shares' forward earnings ratio of 14 is still cheaper than rival Clipper Logistics (CLIP). *HR*

Speculative buy

Ord Price: 159p **Market Value:** £567m
Touch: 158-159p **12-Month High:** 164p **Low:** 156p
Dividend Yield: 0.9% **PE Ratio:** na
Net Asset Value: 57p* **Net Debt:** 47%
*Includes intangible assets of £258m, or 72p a share

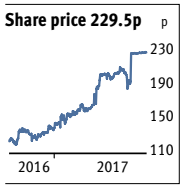
Half-year to 30 Jun	Turnover (£m)	Pre-tax profit (£m)	Earnings per share (p)	Dividend per share (p)
2016**	266	1.7	0.5	nil
2017**	287	-7.6	-2.5	1.4
% change	+8	–	–	–

**Company admitted to Aim in April 2017
Last IC view: Speculative buy, 161p, 24 Apr 2017
Ex-div: 7 Sep Payment: 20 Oct

PERSONAL GOODS

Jimmy Choo steps up ahead of Kors takeover

Jimmy Choo (CHOO) shareholders are now in receipt of documents relating to the group's impending takeover by US luxury house Michael Kors (US:KORS). Just three months after its largest shareholder announced the shoe king was up for sale, Michael Kors agreed to a 230p all-cash offer totalling £896m, representing a 37 per cent premium to Choo's undisturbed share price and making it one of the most generous offers seen this year in the luxury retail sector.



And by the look of these half-year numbers, Kors might have bagged itself a company that has finally got some of its affairs in order. Retail sales grew by a steady 3.5 per cent on a like-for-like basis (compared with a 4 per cent decline in last year's first half) which, thanks to the one-off nature of last year's losses on foreign exchange and finance expenses, allowed pre-tax profit to flourish.

Licensing also fared better year on year, although wholesale reported a 1.6 per cent revenue decline (compared with 5.6 per cent growth this time last year) following an expected reduction in orders from US department stores. Lower working capital commitments meant cash conversion rates improved from 84.5 per cent to 118.9 per cent, helped by net debt falling by 16.4 per cent to £119m.

Analysts have suspended their forecasts in light of the pending takeover.

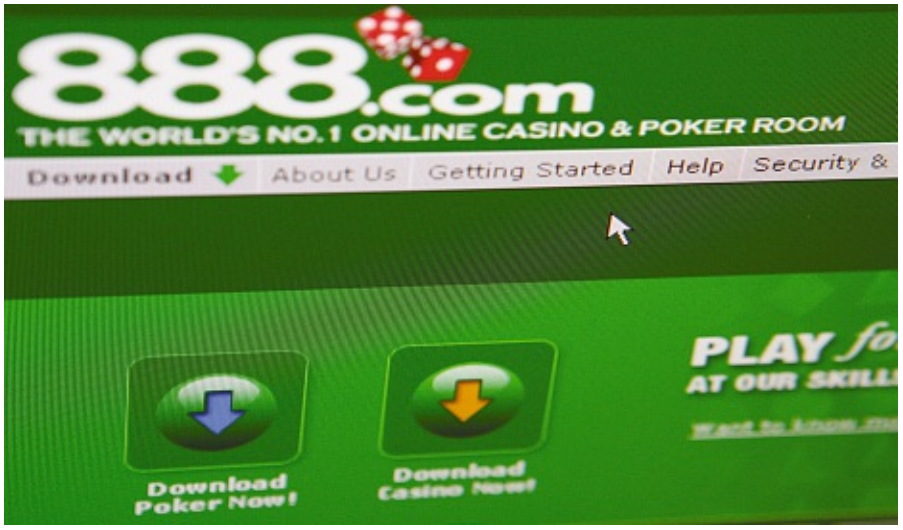
At the time of the takeover news, we concluded that the premium was a generous exit strategy and recommended investors accept the offer. Although the shares now trade around the agreed price, our view is unchanged ahead of completion. *HR*

Accept

Ord Price: 229.5p **Market Value:** £894m
Touch: 229.5-229.6p **12-Month High:** 231p **Low:** 120p
Dividend Yield: nil **PE Ratio:** 37
Net Asset Value: 127p* **Net Debt:** 24%
*Includes intangible assets of £607m, or 155p a share

Half-year to 30 Jun	Turnover (£m)	Pre-tax profit (£m)	Earnings per share (p)	Dividend per share (p)
2016	173	6.6	1.5	nil
2017	202	18.1	3.6	nil
% change	+16	+174	+140	–

Last IC view: Hold, 228p, 26 Jul 2017

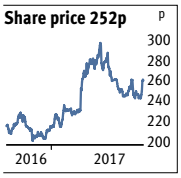


Gambling company 888 saw good momentum in the first half, but has been censured by the regulator

TRAVEL & LEISURE

888 boosts sales but fines hurt

On a constant currency basis, **888 Holdings' (888)** top line rose 9 per cent in the first half of 2017. Though ultimately dampened by negative exchange movements, this resolute performance was eclipsed last week when the UK Gambling Commission (UKGC) fined the group more than £7.8m for "serious failings in its handling of vulnerable customers". On the bright side, for 888 shareholders this ends a period of uncertainty, which started when the regulator's review into the company was announced in May. Plus, the group has kept hold of its operating licence.



Two exceptional items account for the pre-tax loss. A one-off charge of $5.5m represents the £4.25m that the UKGC has ordered 888 to direct to a cause that will "invest in measures to tackle gambling-related harm". A further £3.5m, not recorded in these figures, must be paid to more than 7,000 self-excluded customers who were still able to deposit money into accounts over 13 months, gambling £50.6m.

The other cost of $45.3m (£34.7m) relates to potential VAT payments for the provision of gaming services in Germany before 2015. 888 concedes that other services could result in a further cash outflow of up to $18.5m.

Elsewhere, "increasing recognition of [online business] 888Sport as a premium sports betting brand" led to a reported sales bump of 35 per cent to $33.7m, or 45 per cent at constant currencies. The casino business also performed well, with an underlying sales boost of 11 per cent attributed to growth on mobile devices and increased content. Bingo sales were down 3 per cent on an underlying basis, but declined 15 per cent in reported terms, owing to sterling's weakness and a "highly competitive UK bingo market".

Regionally, there was good momentum in Italy, where a strong contribution from sports betting led to revenue growth of 40 per cent. In Spain, 888's second-largest individual market, sales rose 23 per cent thanks to marketing campaigns and a "comprehensive" product base. The company exited markets with no "sustainable future opportunities", such as Australia, Poland, Slovenia and the Czech Republic.

Numis forecasts pre-tax profit of $68.8m and basic EPS of 16.4¢ this year, up from $63.1m and 15.5¢ in 2016.

The fine won't significantly dent 888's cash pile. For now, there is enough sales momentum in key sectors and markets to keep faith that the generous dividend payouts will continue. *HC*

Buy

Ord Price: 252p **Market Value:** £906m
Touch: 251.8-252p **12-Month High:** 302p **Low:** 196p
Dividend Yield: 6%* **PE Ratio:** 99
Net Asset Value: 26¢** **Net Cash:** $153m
*Includes special dividend of 10.5¢ a share paid in May 2017
**Includes intangible assets of $160m, or 44¢ a share
£1=$1.29

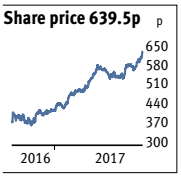
Half-year to 30 Jun	Turnover ($m)	Pre-tax profit ($m)	Earnings per share (¢)	Dividend per share (¢)
2016	262	27.8	6.1	3.8
2017	270	-17.3	-5.0	4.0
% change	+3	–	–	+5

Last IC view: Buy, 271p, 16 May 2017 | Ex-div: 14 Sep | Payment: 11 Nov

H'HOLD GOODS & HOME CONSTRUCTION

Redrow delivers fourth year of record profits

Full-year results from **Redrow (RDW)** quickly crushed any ideas that house-builders are losing momentum. Transactional volume in pre-owned houses may be falling, but the appetite for new homes remains undiminished.



Redrow added to the previous year's record results by pushing profits and earnings ahead by a quarter and rewarding shareholders with a 70 per cent increase in the annual dividend payout. Completions rose by 15 per cent to over 5,400, and with a record £1.1bn forward order book, Redrow now expects turnover to reach around £2.2bn by 2020, giving pre-tax profit of £430m, and by then the dividend is expected to have risen to 32p a share.

Greater exposure to the southern part of the UK helped lift average selling prices by 7 per cent to £309,800. Crucially, almost all the legacy land acquired before the financial crash has been used up, and operating margins rose from 18.9 per cent to 19.4 per cent. Strong cash generation also helped to reduce net debt from £139m to £73m. Trading in the new financial year remains robust, with sales up 8 per cent in the first nine weeks.

Peel Hunt forecasts adjusted pre-tax profit for the year to June 2018 of £356m and EPS of 79.5p (from £315m and 69.9p in 2017).

Redrow's shares have risen sharply this year and are well ahead of our buy tip (415.4p, 23 March 2016) yet trade on a price/net asset value discount to the peer group. We think there's more to come. *JC*

Buy

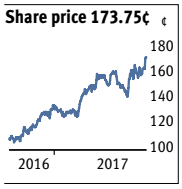
Ord Price: 639.5p **Market Value:** £2.36bn
Touch: 639-640p **12-Month High:** 666p **Low:** 367p
Dividend Yield: 2.7% **PE Ratio:** 9
Net Asset Value: 334p **Net Debt:** 6%

Year to 30 Jun	Turnover (£bn)	Pre-tax profit (£m)	Earnings per share (p)	Dividend per share (p)
2013	0.60	69	14.6	1
2014	0.86	133	28.3	3
2015	1.15	204	44.5	6
2016	1.38	250	55.4	10
2017	1.66	315	70.2	17
% change	+20	+26	+27	+70

Last IC view: Buy, 470.6p, 8 Feb 2017 | Ex-div: 21 Sep | Payment: 10 Nov

H'HOLD GOODS & HOME CONSTRUCTION

Cairn growing fast in Dublin



Cairn Homes (CRN) was floated a little over two years ago, and the costs associated with expanding the business saw a statutory loss for the Irish house-builder in the six months to June. However, after taking out increased administrative expenses and the cost of floating on the Irish stock exchange, gross profit jumped by 191 per cent to €5.1m (£4.7m).

And the pace of growth suggests that profit will increase significantly. The group has nearly doubled the number of active sites, which will deliver over 3,250 homes. In the first half of the year, just 94 sales were completed, but there are 474 forward sales already in place with a total sales value of €188m, of which over 200 are expected to complete in the first half next year. A slight fall in the average selling price to €397,000 reflected a change in the sales mix to include more starter homes.

On the land side, non-core site disposals generated €14.1m, while acquisitions included an 8.64-acre site in a prime Dublin location. In fact, Cairn is ideally placed to benefit from an extreme supply/demand imbalance, with a total of 1,577 new homes sold in Dublin in the first six months of the year against an estimated annual requirement of nearer 18,000 new homes.

Analysts at broker Davy Research are forecasting adjusted pre-tax profit of €11.1m and EPS of 1.3¢ for the year to December 2017, rising to €61m and 6.7¢ the following year.

Cairn Homes is in the right place at the right time, and with such an explosive growth rate, low debt and modest price to book value, the shares offer great value. *JC*

Buy

Ord Price: 173.75¢ **Market Value:** €1.32bn
Touch: 173.5-173.75¢ **12-Month High:** 174¢ **Low:** 105¢
Dividend Yield: nil **PE Ratio:** na
Net Asset Value: 94¢ **Net Debt:** 10%

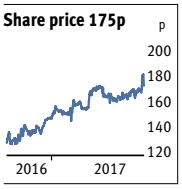
Half-year to 30 Jun	Turnover (€m)	Pre-tax profit (€m)	Earnings per share (¢)	Dividend per share (¢)
2016	16.0	-0.7	-0.10	nil
2017	41.2	-0.4	-0.04	nil
% change	+157	–	–	–

Last IC view: Buy, 135.75¢, 10 Mar 2017 £1=€1.09

SUPPORT SERVICES

Hays delivers a special dividend

Anyone who has been following our recent coverage of **Hays (HAS)** will not be surprised at the announcement of the recruiting giant's inaugural special dividend. The company has a policy of paying out net cash above £50m to shareholders. In respect of these full-year results this means an additional payout of 4.25p a share, bringing the total to 7.47p a share and the historic yield to a respectable 4.3 per cent. This was underpinned by a net cash inflow from operating activities of £134m, up from £103m last year. Group finance director Paul Venables stressed that investors should view this as the first of a series of special dividends, potentially making for an attractive income play.



Hays' full-year performance followed a familiar pattern. Europe led the other geographies with 12 per cent net fee growth on a like-for-like basis. Germany and France saw headcount increases of 24 per cent and 12 per cent, respectively, reflecting their perceived importance to future growth.

The UK continued to struggle with a net fee decline of 7 per cent. Mr Venables reported signs of improvement for a division that may even generate modest fee growth at the next update. Consensus forecasts are predicting adjusted EPS of 10.7p in 2018, rising to 11.6p in 2019 (9.5p in 2017).

Hays remains highly cash generative, and is growing in all but one of its main markets. With a special dividend on the way and the possibility of more to come, a forward PE ratio of 16 times is attractive. *TD*

Buy

Ord Price: 175p **Market Value:** £2.53bn
Touch: 175.2-175.4p **12-Month High:** 176p **Low:** 123p
Dividend Yield: 1.8% **PE Ratio:** 18
Net Asset Value: 41p* **Net Cash:** £112m
*Includes intangible assets of £242m, or 17p a share

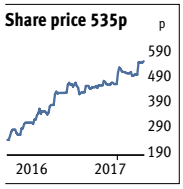
Year to 30 Jun	Turnover (£bn)	Pre-tax profit (£m)	Earnings per share (p)	Dividend per share (p)
2013	3.70	119	5.1	2.50
2014	3.68	132	6.1	2.63
2015	3.84	156	7.4	2.76
2016	4.23	173	8.5	2.90
2017**	5.08	205	9.7	3.22
% change	+20	+18	+14	+11

**Excludes special dividend of 4.25p a share
Last IC view: Buy, 170, 20 Apr 2017 Ex-div: 5 Oct Payment: 17 Nov

AIM: FINANCIAL SERVICES

Alpha to profit from political waves

Corporate currency hedging provider **Alpha FX (AFX)** is carving a niche within the industry. Rather than speculatively playing market movements to ramp up a client's profits, Alpha FX focuses on achieving a balance between over- and under-hedging cash flows based on their business needs, says chief executive Morgan Tillbrook. Alpha only listed on Aim in April, raising £13m to give the group additional liquidity to back a growing forward book of currency trades.



Judging by this maiden set of results, Alpha is appealing to companies seeking to hedge their currency exposure. It secured 46 new clients in the period, taking its total to 269. Underlying operating profit rose 84 per cent to £3.2m, helped by a subdued first-half last year as clients were reluctant to hedge prior to the referendum.

The average commission per trade also increased to 0.61 per cent, from 0.36 per cent during the same period in 2016. That was thanks to a higher proportion of forward trades as well as larger trades and a more favourable mix in the currencies traded.

Analysts at house broker Liberum expect pre-tax profit of £6.2m during the 12 months to the end of December 2017, giving EPS of 15.2p (from £4.3m and 10.5p in 2016).

With the large multinational banks holding around 85 per cent of the market, Alpha FX is a challenger within the sector. With currency fluctuations increasingly likely against a backdrop of Brexit negotiations and trade disputes between the US and China, Alpha has growth potential. However, the shares have more than doubled on the placing price of 196p and trade at a lofty 35 times forward earnings. *EP*

Hold

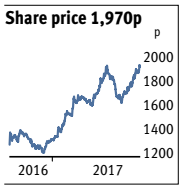
Ord Price: 535p **Market Value:** £175m
Touch: 520-550p **12-Month High:** 570p **Low:** 217p
Dividend Yield: 0.3% **PE Ratio:** 37
Net Asset Value: 60p **Net Cash:** £12m

Half-year to 30 Jun	Turnover (£m)	Pre-tax profit (£m)	Earnings per share (p)	Dividend per share (p)
2016*	3.31	1.72	5.1	nil
2017	6.29	2.38	6.3	1.5
% change	+90	+38	+24	–

*Pre-IPO figures
Last IC view: None Ex-div: 14 Sep Payment: 13 Oct

PHARMACEUTICALS & BIOTECHNOLOGY

North America drives Dechra higher



North America continues to drive growth for veterinary pharmaceuticals specialist **Dechra (DPH)**. In the year to June 2017, stateside revenue nearly doubled at constant currencies after "exceptional" sales from recently acquired businesses were added to the 16.5 per cent underlying growth. North America now makes up more than a third of total revenue, up from 24 per cent in 2016.

Europe also benefited from acquisitions completed within the past 18 months. A modest 3.6 per cent uptick in underlying revenue was boosted by the first full-year contribution from Croatian group Genera and eight months of sales from Australian business Apex.

Looking ahead, it's unlikely that acquisitions will have such a big impact on overall performance. Dechra may have the financial firepower to keep shopping – it generated £94m in net cash last year and reduced its leverage ratio to 1.4 times – but the global veterinary market is already highly consolidated and acquisition opportunities are becoming few and far between. Instead, sales growth is likely to come from the new product pipeline, which received £15m of research and development (R&D) investment in the reported period.

For the year ending June 2018, broker Numis has forecast pre-tax profit and EPS of £90m and 73.5p (from £77m and 64.3p in FY2016).

Dechra's shares trade on 27 times forward earnings. But having delivered compound annual earnings growth of 29 per cent in the past three years, we think it is well deserving of a premium valuation. *MB*

Buy

Ord Price: 1,970p **Market Value:** £1.84bn
Touch: 1,970-1,973p **12-Month High:** 1,995p **Low:** 1,225p
Dividend Yield: 1.1% **PE Ratio:** 70
Net Asset Value: 323p* **Net Debt:** 40%
*Includes intangible assets of £396m, or 425p a share

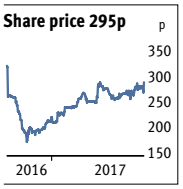
Year to 30 Jun	Turnover (£m)	Pre-tax profit (£m)	Earnings per share (p)	Dividend per share (p)
2013	189	12.5	12.5	14.0
2014	194	21.4	22.2	15.4
2015	203	25.8	22.1	16.9
2016	248	14.5	14.0	18.5
2017	359	28.6	28.1	21.4
% change	+45	+96	+101	+16

Last IC view: Buy, 1,699p, 6 Jul 2017 | Ex-div: 26 Oct | Payment: 17 Nov

AIM: FINANCIAL SERVICES

Curtis Banks dials down acquisitions

After a spate of acquisitions during the past three years, self-invested personal pension (Sipp) scheme provider **Curtis Banks (CBP)** has spent time consolidating its business. Management closed the Chilmark office and is about to enter a staff consultation at its Market Harborough site, both of which were taken on through previous deals. It's also introduced single, group-wide branding for the first time and plans to implement a new operating system to administer its Sipps, which it hopes will improve efficiency, and thus margins.



A full six-month contribution from Suffolk Life helped boost the number of Sipps under administration to 74,900, although the group managed to add 2,825 Sipps organically after taking into account scheme attrition. This meant assets under administration increased 29 per cent to £23.1bn. The Financial Conduct Authority's (FCA) decision to increase capital requirements for Sipp providers caused a wave of consolidation within the industry. However, chief executive Rupert Curtis says the group will now focus on underlying growth. While most revenue is earned via management fees, the group is trying to diversify its revenue stream. As part of this it plans to extend its property management services by offering conveyancing and tenant relations services to clients who have a commercial property as part of their Sipp.

Peel Hunt forecasts adjusted pre-tax profit of £10.5m in the 12 months to December 2017 and EPS of 15.6p (from £7.1m and 11p in 2016).

The shares are trading at 19 times forward earnings, a sizeable discount to the rating of 25 times they demanded 12 months ago. With the benefits of increased scale still yet to fully bed in, we stick with buy. *EP*

Buy

Ord Price: 295p **Market Value:** £158m
Touch: 285.5-297.75p **12-Month High:** 325p **Low:** 176p
Dividend Yield: 1.5% **PE Ratio:** 26
Net Asset Value: 80p* **Net Cash:** £4m
*Includes intangible assets of £47m, or 88p a share

Half-year to 30 Jun	Turnover (£m)	Pre-tax profit (£m)	Earnings per share (p)	Dividend per share (p)
2016 (restated)	57	1.24	2	1
2017	201	4.08	6.1	1.5
% change	+254	+230	+211	+50

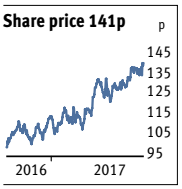
Last IC view: Buy, 265p, 27 Mar 2017 | Ex-div: 12 Oct | Payment: 15 Nov

AIM: SUPPORT SERVICES

Johnson Service chief to retire

After 33 years at the company, **Johnson Service Group's (JSG)** chief executive, Chris Sander, is leaving. He will retire during the first half of 2018, but wants to leave the company in good shape. So far so good: adjusted pre-tax profits rose 23.5 per cent during the six months to June 2017, following a steady 19 per cent improvement at the top line.

The group continues to combine organic growth with acquisitions. Management said price and volume increases helped deliver underlying revenue growth of 4.8 per cent over the period, while the disposal of the long-troubled dry cleaning business in January furthered the shift to higher-margin textile services work. The acquisition of high-volume hotel linen business PLS also added to the group's capabilities in Scotland and Northern England.



There are no plans to dramatically reduce the company's debt, though. Finance director Yvonne Monaghan said gearing is measured using a custom figure, which doesn't include rental stock depreciation. The long-term target is to stay below two times this measure; the company currently sits around 1.7 times.

Analysts at Investec are forecasting adjusted pre tax profit of £38.4m, giving EPS of 8.4p for the year to December 2017 (up from £33.8m and 7.6p in 2016).

Against their recent history, JSG's shares are starting to look expensive at 17 times forecast earnings. However, they still lag the sector average of 19 times and, with the business now focused on higher-margin work, we remain keen. *TD*

Buy

Ord Price: 141p **Market Value:** £516m
Touch: 140-141p **12-Month High:** 145p **Low:** 99p
Dividend Yield: 1.8% **PE Ratio:** 22
Net Asset Value: 43p* **Net Debt:** 57%
*Includes intangible assets of £160m, or 44p a share

Half-year to 30 Jun	Turnover (£m)	Pre-tax profit (£m)	Earnings per share (p)	Dividend per share (p)
2016**	116	9.9	2.3	0.80
2017	138	12.9	2.8	0.90
% change	+19	+30	+22	+13

Last IC view: Buy, 115, 1 Mar 2017 | Ex-div: 5 Oct | Payment: 3 Nov

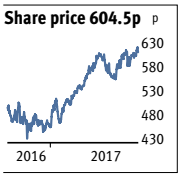


Barratt's return on capital reached a 12-year high, while output was the best for nine years

HOUSEHOLD GOODS & HOME CONSTRUCTION

Barratt promises another special dividend

To give some idea about how well house-builders have bounced back since the financial crash, you only have to look at the dividend payout from **Barratt Developments (BDEV)** which, since 2013, has increased by an astonishing 1,568 per cent, when including the latest special dividend of 17.3p.



And in the year to June 2017, Barratt once again ticked all the right boxes, boosting operating margins from 15.8 per cent to 17.2 per cent, and delivering a return on capital employed of 29.8 per cent, up from 27.1 per cent a year earlier and the highest for 12 years. Completions were marginally ahead at 17,395, while total average selling prices rose by 6 per cent to £275,200. On private completions prices rose 8 per cent to £313,100. Margins were also boosted by more use of higher-margin land and the steady run-down in legacy assets (high-priced land acquired before the financial crash), with 92 per cent of completions made on higher-margin land, up from 86 per cent a year earlier.

Land values remained benign, and the group continued to exceed its minimum hurdle rates on land purchases of 20 per cent gross margin and 25 per cent return on capital employed. Land purchases were down slightly from the previous year at £957.2m, equating to 18,497 plots. Barratt holds a relatively short land bank, equivalent to 3.5 years of output, which helps to boost return on capital when blended with a fast build-and-sell model.

Improved efficiency and a more simplified range have helped to offset the pressures generated by a shortage of skilled labour. And material costs have also been kept under control, with 90 per cent of materials manufactured or assembled in the UK. Overall build cost inflation for the year to June 2018 is expected to be around 3-4 per cent.

So far, analysts at Peel Hunt are still forecasting adjusted pre-tax profits for the year to June 2018 of £818m and EPS of 66.2p, compared with £774m and 61.3p in FY2017.

Operating margins are still below the sector average, and Barratt will be working to close this gap. The business throws off a lot of cash, and Barratt expects to pay another special dividend in 2018. The shares have risen by around a third this year, but still trade at a discount to the sector in terms of price to net assets. *JC*

Buy

Ord Price: 604.5p **Market Value:** £6.1bn
Touch: 604-604.5p **12-Month High:** 630p **Low:** 430p
Dividend Yield: 4% **PE Ratio:** 10
Net Asset Value: 427p* **Net Cash:** £724m
*Includes intangible assets of £892m, or 88p a share

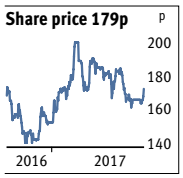
Year to 30 Jun	Turnover (£bn)	Pre-tax profit (£m)	Earnings per share (p)	Dividend per share (p)**
2013	2.61	105	7.7	2.5
2014	3.16	391	31.2	10.3
2015	3.76	566	45.5	15.1
2016	4.24	682	55.1	18.3
2017	4.65	765	61.3	24.4
% change	+10	+12	+11	+33

**Excludes special dividends of 10p a share in 2015, 12.4p in 2016 and 17.3p in 2017
Last IC view: Buy, 526p, 22 Feb 2017 Ex-div: 26 Oct Payment: 20 Nov

CONSTRUCTION & MATERIALS

Alumasc leans on US dollar income hedge

For the first time in its seven-decade history, **Alumasc (ALU)** was focused purely on building products during the most recent financial year to June. Anyone cognisant of the UK construction market's current rate of growth – 1.2 per cent a year – might question that strategic shift. On balance, though, these half-year results served as another reminder of the Kettering-based group's ability to identify products and specialities that can be converted into earnings growth.



All divisions posted top-line improvements, although momentum was most apparent at the solar shading and architectural segment. Revenue leapt 41 per cent here to £24.4m, buoyed by a doubling of export sales to North America, which in turn doubled underlying operating profit to £2m. Further growth in greenback-denominated income explains management's continued investment in its US sales, and its confidence in a further expansion in the operating margin, which edged up 270 basis points to 8.2 per cent in the period under review. Elsewhere, another good outing for the housebuilding and ancillary business explains why chief executive Paul Hooper is happy to spend £2m on a new factory in Goole, south of York.

FinnCap expects adjusted pre-tax profit of £9.5m and EPS of 21.2p in the 12 months to June 2018, rising to £10.7m and 23.7p in FY2019.

The period wasn't all rosy: public sector façade refurbishment has lagged, while rising steel prices weighed on margins. Then again, the market is asking little of the shares, which trade on eight times this year's earnings and boast a 4 per cent yield. *AN*

Buy

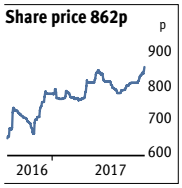
Ord Price: 179p **Market Value:** £63m
Touch: 176-181p **12-Month High:** 203p **Low:** 138p
Dividend Yield: 4% **PE Ratio:** 10
Net Asset Value: 58p* **Net Cash:** £6.1m
*Includes intangible assets of £18.9m, or 53p a share

Year to 30 Jun	Turnover (£m)	Pre-tax profit (£m)	Earnings per share (p)	Dividend per share (p)
2013	117	2.8	5.3	4.5
2014	88.9	6.1	13.4	5.0
2015	90.3	6.3	13.5	6.0
2016	92.2	6.8	14.5	6.5
2017	105	8.1	18.3	7.2
% change	+14	+20	+26	+10

Last IC view: Buy, 171p, 1 Feb 2017 Ex-div: 5 Oct Payment: 31 Oct

AIM: FINANCIAL SERVICES

Mattioli self-directs its investments



Gaining more discretionary business has been crucial for wealth managers' growth, so **Mattioli Woods' (MTW)** launch of its structured products fund in November was a smart move. The fund invests in a range of structured products – whose performance is linked to selected underlying indices – and had raised £98m by end-May. This helped take gross discretionary assets under management up by more than a third to £1.6bn.

Total assets under management, administration and advice increased more than half to £7.8bn. Advising clients on pension and personal investments also continued to be the largest contributor to group revenue, up almost a quarter on 2016 to £21m. However, the biggest gain in assets was via self-invested pension plans administered by the pension and consultancy and administration business.

The employee benefits business suffered a £56m decline in the assets held in the corporate pension schemes it advises on, following the loss of a large client in the North Sea oil and gas industry. Nevertheless, it still managed a 2 per cent uplift in sales to £5.4m.

Analysts at FinnCap expected adjusted earnings per share of 35.5p for the 12 months to May 2018, up from 34.1p in 2017.

The shares are well ahead of our buy tip (678p, 15 September 2016) and exchange hands for 24 times forward earnings – a premium to the sector average. But we still like Mattioli's bent towards specialist advice given the continuing trend towards self-directed investment. *EP*

Buy

Ord Price: 862p **Market Value:** £223m
Touch: 852-872p **12-Month High:** 872p **Low:** 651p
Dividend Yield: 1.6% **PE Ratio:** 35
Net Asset Value: 280p* **Net Cash:** £23m
*Includes intangible assets of £44m, or 172p a share

Year to 31 May	Turnover (£m)	Pre-tax profit (£m)	Earnings per share (p)	Dividend per share (p)
2013	23.4	4.6	19.2	7.0
2014	29.3	5.1	22.0	9.1
2015	34.6	5.3	19.8	10.5
2016	43.0	6.3	20.9	12.5
2017	50.5	7.6	24.8	14.1
% change	+18	+21	+19	+13

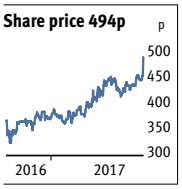
Last IC view: Buy, 791p, 9 Feb 2017 | Ex-div: 21 Sep | Payment: 27 Oct

TRAVEL & LEISURE

Room numbers grow at Dalata

Fears over the rapid devaluation in the pound are continuing to weigh on **Dalata Hotel (DAL)**. Weaker sterling deterred a number of British visitors from travelling to Dublin – a crucial city location for the company – although this was helpfully offset by higher tourist numbers from North America and continental Europe.

The other Irish cities are less exposed to the risk of declining UK tourism and have continued to grow. Revenue from regional Ireland was up 18 per cent on last year. In addition, the group's UK hotels did well, thanks to the relative value on offer. As such, adjusted cash profits rose 27 per cent over the first half of 2017, as both total occupancy rates and average revenue per room climbed higher.



The group has been buying up and building hotels in Ireland and the UK, including the 300-room Clayton hotel in Manchester and the Maldron in Portlaoise. Overall, the group has spent €17.1m (£15.6m) on new builds and extensions, while also pursuing a room refurbishment programme. So far it has spent €5.7m, not including the €1.8m spent as part of the rebrand of former Clarion hotels to Clayton. Dalata is due to open another 1,280 rooms in 2018.

Analysts at Davy are forecasting pre-tax profit of €69.9m, giving EPS of 32.5¢ for the year to December 2017 (from €44.1m and 19.1¢ in 2016)

Dalata's numbers speak for themselves. The group is growing rapidly, net debt is lower than at its last update, while both room numbers and revenue per room are growing. Brexit may prove a challenge in the future, but at 17 times forecast earnings we think there's still room for upside. *TD*

Buy

Ord Price: 494p **Market Value:** £907m
Touch: 483.5-493.5p **12-Month High:** 494p **Low:** 325p
Dividend Yield: na **PE Ratio:** 21
Net Asset Value: 355¢ **Net Debt:** 27%

Half-year to 30 Jun	Turnover (€m)	Pre-tax profit (€m)	Earnings per share (¢)	Dividend per share (¢)
2016	130	18.2	8.5	nil
2017	162	32.7	15.5	nil
% change	+24	+80	+82	–

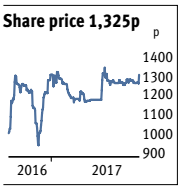
Last IC view: Buy, 380p, 3 Mar 2017 | £1=€1.09

AIM: SOFTWARE & COMPUTER SERVICES

New product exciting for Craneware

The ball is rolling on the migration of **Craneware's (CRW)** customers to its new cloud software platform, Trisus. The US-focused healthcare services company launched the first product in the new suite in June and management has been encouraged by its early uptake.

But Trisus' launch caused a short term drop in Craneware's average contract length (from five to four years) which sent reported new sales down 40 per cent to $35.4m (£27m) in the period. The fact that fewer contracts were up for renewal this year also caused a 34 per cent drop in the total value of group contracts to $54m.



No matter. Adjust for the one-off contraction to contract length, and new product sales on a like-for-like basis were actually up to over $60m. This, added to the group's strong market growth in recent years and its 110 per cent contract renewal rate, means total visible revenue for the next three years currently stands at $164m. With $56m of that expected to be recognised in the next financial year, Craneware has already booked over 80 per cent of Peel Hunt's FY2018 revenue forecast. The broker is expecting pre-tax profits of $20.3m, giving EPS of 50.7¢ (from $17.8m and 50.3¢ in FY2017).

The arrival of Trisus means revenue visibility should improve over the next few years as a higher number of products means customers will spend more each time their contracts renew. We think Craneware shares deserve their premium forward rating of 34 times. *MB*

Buy

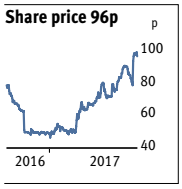
Ord Price: 1,325p **Market Value:** £358m
Touch: 1,300-1,350p **12-Month High:** 1,365p **Low:** 960p
Dividend Yield: 1.2% **PE Ratio:** 34
Net Asset Value: 220¢* **Net Cash:** $53.2m
*Includes intangible assets of $19.8m, or 73.5¢ a share £1=$1.3

Year to 30 Jun	Turnover ($m)	Pre-tax profit ($m)	Earnings per share (¢)	Dividend per share (p)
2013	41.5	10.6	30.7	11.5
2014	42.6	11.3	31.9	12.5
2015	44.8	12.5	35.0	14.0
2016	49.8	13.9	39.4	16.5
2017	57.8	16.9	50.2	20.0
% change	+16	+21	+27	+21

Last IC view: Buy, 1,200p, 7 Mar 2017 | Ex-div: 9 Nov | Payment: 7 Dec

AIM: CONSTRUCTION & MATERIALS

Aquisition boosts Michelmersh Brick



Without context, investors could be spooked by **Michelmersh Brick's (MBH)** latest results, which revealed a 47 per cent drop in pre-tax profit. Adjusted numbers were much better, although profit still fell slightly to £2.4m from £2.6m due to an increase in administrative expenses. The numbers were hit hard in the period by costs associated with the acquisition of Carlton Main Brickworks, a deal that analysts at Cenkos have said will be "transformative" for the brick maker.

The newly acquired group was only factored in for seven days of this half-year period, but should have a more significant impact in the second half of the year. Pro-forma numbers from management indicate it could raise the company's brick output by 49 per cent and double adjusted cash and operating profit. In pursuing the deal, the group took on £27m-worth of debt, although leverage is expected to fall now that the transaction has completed.

Michelmersh Brick also has a stronger forward order book of 55m bricks – a record in fact – along with a slightly improved average selling price. Analysts at broker Cenkos have forecast adjusted pre-tax profit of £6.1m and EPS of 5.8p for the year to December 2017 (from £4.8m and 4.6p in 2016).

With the shares now trading at 17 times forecast earnings, Michelmersh looks more expensive compared with the last time we analysed the group. However, the shares' valuation is still shy of the sector average, and with its newly improved capacity we think there's still value to be found here. *TD*

Buy

Ord Price: 96p **Market Value:** £82.8m
Touch: 95-97p **12-Month High:** 100p **Low:** 45.5p
Dividend Yield: 2.8% **PE Ratio:** 30
Net Asset Value: 66p* **Net Debt:** 37%
*Includes intangible assets of £23.7m, or 27p a share

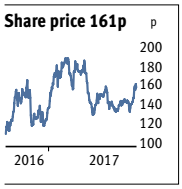
Half-year to 30 Jun	Turnover (£m)	Pre-tax profit (£m)	Earnings per share (p)	Dividend per share (p)
2016	15.3	2.6	2.57	nil
2017	16.2	1.4	1.35	0.70
% change	+6	-47	-47	–

Last IC view: Buy, 58p, 20 Mar 2017 | Ex-div: 14 Dec | Payment: 12 Jan

AIM: MINING

Highland weighs cost inflation

Ideally, gold would only be mined in the United States. That would at least remove foreign exchange swings from the many sources of volatility in the shares of gold mining companies, which typically book sales in dollars and costs in local currencies. Unfortunately for investors in **Highland Gold Mining (HGM)**, this isn't the case. Indeed, a strengthening rouble and attendant cost inflation has prevented shares in the Russian miner from matching the 16 per cent 'return' of a dollar-denominated ounce of gold in 2017.



The price has been an 11 per cent rise in all-in sustaining costs to $674 (£518) per ounce, which fed through to a 4 percentage point drop in the cash profit margin, and a slight increase in the net debt position. The latter can partly be explained away by a 46 per cent jump in capital expenditure to $27.4m, reflecting a step-up in exploration costs at Mnogovershinnoye, $13.5m-worth of spending at the Kekura project, and expansion to processing capacity at Novoshirokinskoye.

On average, analysts are predicting full-year pre-tax profit of $78m and adjusted EPS of 18¢, compared with $66.2m and 20.2¢ in 2016.

Longer-term currency movements tend to come out in the wash – particularly when the cost base is as modest as Highland's. With its enterprise value sitting at five times cash profits, Highland trades at a 10 per cent discount to Centamin (CEY). The latter – one of our preferred picks in the sector – lacks Highland's range of projects and relative stability of ore grade. On this recent share weakness, we upgrade to buy. *AN*

Buy

Ord Price: 161p **Market Value:** £524m
Touch: 161-162p **12-Month High:** 196p **Low:** 111p
Dividend Yield: 5% **PE Ratio:** 19
Net Asset Value: 233¢ **Net Debt:** 27% £1=$1.30

Half-year to 30 Jun	Turnover ($m)	Pre-tax profit ($m)	Earnings per share (¢)	Dividend per share (¢)
2016	147.1	48.8	11.3	5.0
2017	147.2	43.5	7.9	5.0
% change	+0.1	-11	-30	–

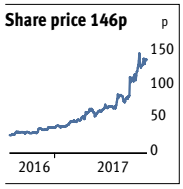
Last IC view: Hold, 189p, 18 Apr 2017 | Ex-div: 14 Sep | Payment: 13 Oct

AIM: TECHNOLOGY, HARDWARE & EQUIPM'T

Market digests IQE's inflection

Consider the following investor quiz question: a high-growth technology company in your portfolio has just posted a 2 per cent decline in adjusted operating profit, a 10 per cent drop in half-year cash generation, and an 18 per cent increase in leverage. Its chief executive maintains the company is poised to prosper from an industry inflection point, and that the outlook "has never looked better". Do you a) sell out, or b) increase your stake?

When **IQE (IQE)** published its half-year numbers, the market initially gave the first answer. Perhaps fearful that demand for the semiconductor supplier's much vaunted VCSEL (vertical-cavity surface-emitting laser) wafers was slower than expected, or that half-year figures were only given a gloss by the post-referendum devaluation of sterling, investors ran for the exit. The stock, up threefold already in 2017, duly fell 10 per cent.



By the end of the day's trading session, investors had scratched out their original response and doubled down, pushing the stock 6 per cent higher on chief executive Drew Nelson's assertion that capacity, demand, revenue diversity and growth will all rocket in 2018. Peel Hunt chimed in, flagging another possible upgrade to earnings forecasts, although its analysts still expect full-year adjusted pre-tax profit of £23m and EPS of 3.3p this year, against £20.6m and 3p in 2016.

Analyst upgrades aren't the only source of momentum. Despite the sky-high valuation, investors were sufficiently inspired by these numbers to push IQE's shares higher. That suggests there could be more to run, although we've got few qualms about closing out our spectacularly-timed original call (22p, 25 June 2015). We choose option a) *AN*

Sell

Ord Price: 146p **Market Value:** £1.0bn
Touch: 145.8-146.3p **12-Month High:** 150p **Low:** 26p
Dividend Yield: nil **PE Ratio:** 59
Net Asset Value: 29.4p* **Net Debt:** 21%
*Includes intangible assets of £105.9m, or 16.1p a share

Half-year to 30 Jun	Turnover (£m)	Pre-tax profit (£m)	Earnings per share (p)	Dividend per share (p)
2016	63.0	10.5	1.49	nil
2017	70.4	6.8	1.07	nil
% change	+12	-35	-28	–

Last IC view: Buy, 98p, 20 Jul 2017

WEEK AHEAD

Monday 11 September

Interims: Cloudcall, Crossrider, Deltex Medical, EKF Diagnostics, Luceco, Penant International, Restore, XLMedia
Finals: 1pm, Abcam, K3 Capital
Trading statement: Associated British Foods
AGMS: CH Bailey, Empyrean Energy, PHSC, Real Estate Credit Investments
EGMS: Big Sofa Technologies, MBL
Company paying dividend: AstraZeneca (68.9p)

Tuesday 12 September

Interims: Applegreen, Empiric Student Property, Flowtech Fluidpower, Futura Medical, Goals Soccer Centres, Hilton Food, Hydrogen, JD Sports, Manx Telecom, Midwich, Petropavlovsk, SafeCharge International, Servelec, Smart Metering Systems, STM, Tasty, TP, TyraTech
Finals: Innovaderma, Murgitroyd, Vernalis
Trading statement: Ashtead
AGMS: AEW UK Reit, Ashtead, Bushveld Minerals, Daejan, Emmerson, Limitless Earth, Liontrust Asset Management, Mulberry, Oxford Instruments, SuperGroup, Van Elle
Economics: Consumer price index, Retail price index, Producer prices, House price index
Company paying dividend: Yu (1.5p)

Wednesday 13 September

Interims: Advanced Medical Solutions, Alliance Pharma, Columbus Energy Resources, Epwin, Eve Sleep, Gaming Realms, Ingenta, Just, MyCelx Technologies, Soco International, SQS Software Quality Systems, Surgical Innovations, Ten Entertainment
Finals: Dunelm, Galliford Try, Haynes Publishing, Town Centre Securities, Wilmington
AGMS: Argo, Games Workshop, Hardy Oil & Gas, Intercede, Tricorn, Versarien
Economics: Employment data, Average earnings
Companies paying dividends: Cohort (4.9p), G4S (3.59p), Hiscox (9.5p), Mobeus Income & Growth VCT (9p), Rentokil Initial (1.14p)

Thursday 14 September

Interims: Corero Network Security, Gresham House, GVC, Next, Ophir Energy, Property Franchise, Regional Reit, Spire Healthcare, William Morrison Supermarkets
Final: Ricardo
AGMS: Abzena, Arian Silver, Colefax, Columbus Energy Resources, Falcon Oil & Gas, Xafinity
EGM: Colefax
Economics: RICS house prices, Retail sales, Bank of England interest rate announcement, asset purchase target, corporate bond target
Companies paying dividends: 4imprint (13.8p), Quartix (2.4p)

Friday 15 September

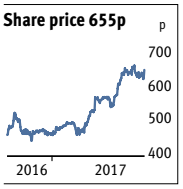
Final: JD Wetherspoon
AGMS: Blenheim Natural Resources, Netalogue Technologies, Tungsten Corp
Companies paying dividends: Apax Global Alpha (4.24p), Ashtead (22.75p), Berkeley Group (51.76p), Carnival (31.25p), Chemring (1p), Greene King (24.4p), Hazel Renewable Energy VCT1 (5p), Hazel Renewable Energy VCT2 (5p), IMI (14.2p), Informa (6.65p), Lazard World Trust Fund (5.1p), Maven Income & Growth VCT2 (3.41p), Maven Income & Growth VCT5 (2p), North Midland Construction (3p), Pearson (5p), Securities Trust of Scotland (1.45p), Severfield (1.6p), Synectis (1p), Walker Crips (1.29p)

Companies going ex-div 14 Sep

Company	Dividend (p)	Payment
Aberdeen Diversified Inc. & Grwth Trst	1.631	9 Oct
Assura ord 10p	0.6	18 Oct
BBA Aviation ord 29 16/21p	2.93	3 Nov
BCA Marketplace	4.55	29 Sep
Carr's ord 2.5p	0.95	6 Oct
Centaur Media ord 10p	1.5	5 Oct
Communisis ord 25p	0.89	13 Oct
Computacenter ord 6p	7.4	13 Oct
Costain ord 50p	4.75	20 Oct
Derwent London ord 5p	17.33	20 Oct
Eco Animal Health ord 5p	4.6	6 Oct
Equiniti	1.75	26 Oct
Foresight Technology VCT	4	29 Sep
Gocompare.com	0.7	6 Oct |
Highcroft Investment Trust ord 25p	16.25	13 Oct
Holders Technology ord 10p	0.25	10 Oct
Inmarsat ord €0.0005	16.6	20 Oct
Jupiter Green Investment Trust	1.2	6 Oct
Naspers	4.77	28 Sep
Octopus Second Aim VCT	2.1	29 Sep
Restaurant Group ord 25p	6.8	12 Oct
RPS ord 3p	4.8	13 Oct
Sophos	2.55	13 Oct
Tex ord 10p	2.5	6 Oct
Total Produce €0.01	0.8906	13 Oct
Trifast ord 5p	2.5	13 Oct
XP Power ord 1p	16	12 Oct
Zotefoams ord 5p	1.91	12 Oct

AIM: MOBILE TELECOMMUNICATIONS

Gamma benefits from modern office



Office telecoms services are in the midst of a shift. Demand for traditional landline and broadband connectivity is dwindling and, instead, businesses are signing up for cloud computing and voice-over-the-internet products (VOIP). **Gamma Communications (GAMA)** has positioned itself well in this evolving market. In the six months to June 2017, the group reported a 13 per cent increase in revenue from its data, mobile and cloud products to £62m, which more than offset a decline in demand for traditional services.

SIP Trunking and Cloud PBX were, once again, the two standout products. Trunk installations and PBX users increased by 18 per cent and 20 per cent, respectively, far outpacing the wider market growth for both of these types of products.

But bending to the demands of the modern office has forced Gamma to invest in its network. This caused a 26 per cent uptick in underlying capital expenditure (capex) to £8.6m, which increased operational gearing. Second-half capex is expected to be pushed higher with £5m-worth of upgrade investments to the group's national fibre broadband network – although this will provide Gamma with its core infrastructure for the next 25 years.

Broker Peel Hunt has forecast pre-tax profit and EPS of £25.8m and 22.2p, respectively, in the year to December 2017 (from £24.5m and 21.1p in 2016).

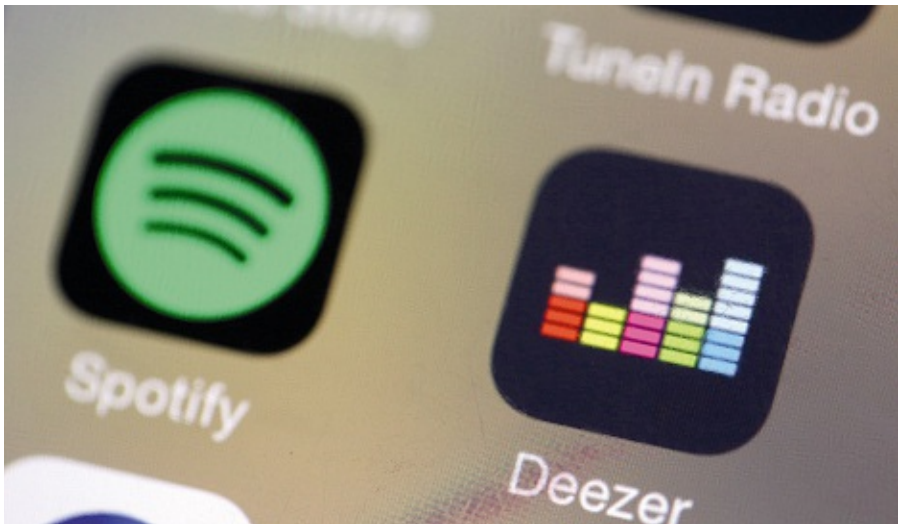
Investors seem to have finally realised the opportunities for Gamma, sending the share price up over 40 per cent in the past 12 months. We still like the long-term prospects on offer here, but a forward price-to-earnings ratio of 30 times now looks a bit stretched. *MB*

Hold

Ord Price: 655p **Market Value:** £610m
Touch: 655-662p **12-Month High:** 670p **Low:** 440p
Dividend Yield: 1.2% **PE Ratio:** 30
Net Asset Value: 94p **Net Cash:** £28.7m

Half-year to 30 Jun	Turnover (£m)	Pre-tax profit (£m)	Earnings per share (p)	Dividend per share (p)
2016	105	10.6	9.5	2.5
2017	115	12.5	12.0	2.8
% change	+10	+18	+26	+12

Last IC view: Buy, 473p, 21 Mar 2017 | Ex-div: 21 Sep | Payment: 19 Oct



Spotify speculation: a float would give investors a chance to buy into a popular service

The latest sounds in music

With technology driving changes in music, we look at ways to buy into the sector

HARRIET CLARFELT

Historically, music was conveyed in physical format only. After vinyl, therein followed the CD revolution. With increasing digitalisation, we saw the arrival of MP3 files. **Apple's (US:APPL)** ascent brought us iTunes, allowing users to buy and download songs, while today subscription streaming services are the main vehicle for music consumption. Account holders benefit from ongoing access to vast music libraries and it's at this end of the market that private company Spotify dominates in terms of subscriber numbers. PricewaterhouseCoopers' (PwC) latest Global Entertainment and Media Outlook report said that in 2016 digital streaming generated revenues of $6.7bn (£5.2bn), up from $4bn a year earlier. This figure is only set to grow.

One issue arising from the shifting nature of music consumption centres on licensing and rightsholding. In September 2016, the European Commission (EC) released a proposal for a directive on copyright in the digital single market. Referencing the emergence of new digital technologies, the EC noted that authors and rights holders needed a guarantee they would "receive a fair share of the value that is generated by the use of their works and other subject matter".

Some of the biggest public music companies are listed in the US. But investors can also buy into the industry here in the UK, where businesses are helping to drive different experiential forms: for example, virtual reality. And the Aim market plays host to a number of companies specialising in hardware and instruments for making music.

The physical decline

Despite what one reads day to day, it's a fact that CD sales are generally waning. Physical format revenues fell by 7.6 per cent in 2016, according to recording industry expert IFPI – an acceleration on the previous year's 3.9 per cent decline. Physical music still constitutes 34 per cent of the global market, buoyed by Japan and Germany, but PwC finds that both physical recorded music revenues and digital download revenues are expected to continue shrinking until 2021 against other formats.

Streaming towards growth

Inevitably, this means there's increasing competition among the top music streaming companies, with each seemingly striving for dominance. In the US, Nasdaq-listed technology and software behemoths Apple and **Amazon (US:AMZN)** each have their own streaming services: Apple Music and Amazon Music. The former currently costs £9.99 a month for an individual subscription, and in June reported 27m subscribers. Amazon Music costs the same, but offers a reduced rate to existent Prime subscription members.

Apple and Amazon are huge, diversified companies, and their respective music businesses can be viewed as subsidiaries. Apple doesn't break out music revenues within its financial statements, rather these fall into the broader 'services' category – a division that grew sales 22 per cent year on year in the third quarter of 2017 to $7.3bn, which represented 16 per cent of Apple's overall top line.

By comparison, Spotify focuses purely on music. Accounts for the full year to 31 December 2016 revealed revenue growth of 52 per cent to €2.9bn (£2.7bn) and a 70 per cent rise in gross profits to €451m. But the effects aren't being felt further down the income statement: operating losses widened significantly to €349m, from €236m in the previous year, due to "substantial investments" in "product development, international expansion and a general increase in personnel".

In recent months, there's been media speculation that Spotify will undergo a direct listing on the New York Stock Exchange, whereby investors could buy shares in the company from existing owners without new capital being raised. A potential float would give investors another choice in which to invest irrespective of Spotify's possible path. The company is currently the most popular service, with 140m users as of June 2017 and more than 60m subscribers as of July 2017. Growth has been rapid: when we last covered the music industry in January 2016, Spotify had around 20m subscribers and 75m listeners. Again, subscribers pay £9.99 a month for a premium account, or opt for free accounts which include advert breaks.

But with Apple and Amazon Music giving chase, what can Spotify do to maintain its momentum? Not to mention Chinese technology giant Tencent, which may take its music streaming business public. It apparently has 15m paid subscribers, 600m

monthly active users, and licensing agreements with all the key record labels.

Streaming services rely on their music libraries, which are enabled by licensing deals. Spotify has renewed agreements with the top three global music labels: Sony Music, Universal Music Group and, most recently, Warner Music Group. As the latest deal was announced, Warner Music Group's chief digital officer, Ole Obermann, noted: "It's taken us a while to get here, but it's been worth it, as we've arrived at a balanced set of future-focused deal terms."

Radio has also entered the streaming realm. Apple, Amazon and Spotify all have personalised radio services, while New York-listed **Pandora Media (P)** specialises in tailormade radio streaming. Here in the UK, Aim-traded **7digital (7DIG)** provides technical infrastructure and music rights to customers for music streaming and radio services.

Live music

Do people still attend concerts when so many digital options are available? The answer is yes. PwC forecasts that live music ticket sales will climb to $28.9bn by 2021 from $25bn in 2016, with the US out in front. By comparison, total digital revenues are forecast to reach $18.7bn. New York-listed **Livenation (LYV)** dominates the live music segment, particularly as it owns TicketMaster, the world's leading ticketing company. That said, Reuters reported recently that Amazon was allegedly seeking to partner with US venue owners with a view to selling tickets.

In the UK, Aim-traded **Accesso Technology (ACSO)** also earns revenues from ticketing and queuing services for events including music festivals and concerts – enabled by its ShoWare cloud-based technology. The company saw 10 per cent revenue growth to $103m, reduced net debt and improved cash conversion during 2016.

An alternative to attending concerts in person could be watching from home with a virtual reality (VR) headset. Aim-traded **EVR (EVR)**, a creator of VR music content, floated last year and has struck agreements with hardware developers, rights holders and music labels – including the big three recording companies. MelodyVR, EVR's main product, hasn't launched yet, so there aren't any sales figures or indeed forecasts. Chief executive Anthony Matchett explains that the VR market needs to reach a buoyant level of 25m-30m headsets before the app can go live, which might happen by Christmas 2017 or early 2018.

Investing in equipment

Aim-traded **Focusrite (TUNE)** is a global music and audio company selling software and hardware to both professional musicians and complete beginners. It has two core brands: Focusrite, which provides audio interfaces and other products for recording musicians; and Novation, which the company acquired in 2004. This enables customers to make electronic music with synthesisers, and is also known for its Launchpad device.

Gear4music (G4M), also Aim-traded, sells music equipment and instruments online. A focus on expansion – it opened new distribution centres in Sweden and Germany during the most recent financial year – has reduced cash levels. But a placing in May raised a further £4.2m to help Gear4music fund "various ongoing organic growth projects".

Focusrite's chief executive Tim Carroll says we are witnessing the democratisation of how music is made. This observation could apply to the broader music industry – for better, and for worse: companies like Focusrite should benefit from people gaining improved access to music and taking a greater interest in the equipment used to make it. But we also anticipate continued tensions between music creators and digital music companies, as each side seeks fair pricing and revenue allocation. And, while such giants exist in the streaming sector, smaller peers may be squeezed out.

Favourites

Apple's Music offering should benefit from the overall group's scale and significant cash pile, as well as its in-house expertise and the connectivity of the Music service with (ubiquitous) Apple hardware devices. And we remain positive about **Focusrite**, which continues to impress with top-line growth and product development. At 307p, the shares are up 92 per cent on our original tip. **EVR** represents an exciting prospect; but for now we see it as a highly speculative punt.

Outsiders

7Digital's shares trade on a lower forward multiple than the peer-group consensus average, while a June update revealed revenue growth of around 13 per cent to £5.9m for the first half. But it remains a smaller fish in a pool of huge streaming competitors, with a market capitalisation of only £11.8m. We have concerns about its ability to keep up in the long term. Similarly, in the US, Pandora also faces competition from other streaming services; its shares have fallen over 40 per cent in the past 12 months.

THE EXPERTS' VIEW

Invest and innovate

In 2016, the global recorded music market grew by 5.9 per cent, the fastest rate of growth since IFPI started tracking it in 1997. This was a second consecutive year of global growth for the industry, with revenue increasing in the majority of markets, including nine of the top 10. But this should be viewed in the context of the industry losing nearly 40 per cent of its revenue in the preceding 15 years.

Streaming has been the clear driver of this growth, with revenues surging by 60.4 per cent. With more than 100m users of paid subscriptions globally, streaming has passed a crucial milestone. It makes up the majority of digital revenue, which, in turn, now accounts for 50 per cent of total recorded music revenues.

Record companies are driving this digital evolution. Even through more than a decade of market decline, they continued their central mission to discover, nurture and promote artists and their music. Alongside this, record companies have built the systems and infrastructure that have enabled the widespread licensing of digital music services and supported their development.

Far from being the conclusion of a long-term transition, record companies see this moment as the start of a new chapter in recorded music, albeit one that is underpinned by a continuing commitment to invest in music and develop artists, and driven by the need to deliver their music to fans in ever more varied and exciting ways.

Crucially, the industry is also working to convert the positive revenue trend currently being experienced into sustainable growth. To achieve this, music must be properly protected in an increasingly digital marketplace. The market flaw known as the 'value gap' must be fixed and fair revenue must return to those who invest in and create music.

Based on an extract from IFPI, Global Music Report 2017

TAKEOVERS

TAKEOVERS IN DEPTH

Takeovers involving UK-domiciled companies are overseen by the Takeover Panel. Often, the first step is that a company enters an 'offer period' – that is, it discloses it has received an approach which may result in a bona fide bid. Being in an offer period restricts what a company may do, and typically bars analysts who cover the company from publishing new research.

The next step is usually that the board of the target company recommends a formal offer, in a document that details the terms of the proposed deal, the timetable the bidding process and, in some cases, potential costs and synergies. The offer document is then dispatched to shareholders, normally within 28 days of a bid announcement, which starts the 'bid clock'. The offer document usually details a closing date for investors to vote in favour or against the proposed combination, which tends to fall three weeks after it is dispatched.

If the bid is hostile, a defence document must be published within 14 days of the offer document being dispatched. Target companies may publish price-sensitive information up to 39 days afterward, and a bidder may revise its terms within 46 days. If a rival bidder emerges, the clock is reset when the second bidder posts its offer document.

A takeover offer succeeds when all its conditions are met, which usually happens within 60 days of the offer document's release. If the bidder acquires more than 75 per cent of the shares, it can delist the target. If it acquires more than 90 per cent, it can forcibly acquire the remaining 10 per cent.

Many agreed takeovers are now structured as schemes of arrangement, because they're quicker to complete. However, they are controversial because they can proceed even if only a minority of shareholders vote in favour of them. A scheme involves the target effectively cancelling its share capital by agreement with its own shareholders, and issuing new shares to the bidder. After the closing date passes, shareholders typically meet to approve or reject the bid, then a court hearing is held to sanction the scheme, and finally the company's shares are cancelled.

TAKEOVERS

Target	Bidder	Terms	Value	Closing date
Aveva Software services	**Schneider Electric** Engineering	*	£2.8bn**	29/09

*1,014p cash per share and a 40 per cent stake in the enlarged group. **£1.7bn-worth of shares are being issued to Schneider Electric which will account for 60 per cent of the enlarged group. French engineering group Schneider Electric is combining its software business with Aveva – the UK's oldest software company. The merger is structured as a reverse takeover with the French group taking a majority stake in the enlarged company, which will retain its London listing. Schneider is contributing £550m of cash which, alongside £100m of excess cash from Aveva's balance sheet, will be returned to shareholders on the completion of the merger. **Accept**.

EG Solutions Software services	**Verint WS** Software services	113p cash per share	£26.3m	tba

US-based software group Verint has offered to buy EG Solutions at an 11 per cent discount to its closing price on the day prior to the announcement. Unsurprisingly the British software group's share price fell off the back of the announcement, although management has recommended the offer, which is a 53 per cent premium to EG's average share price in the last six months. **Await documents**.

ASA Resource Mining	**Rich Pro Investments** Asset management	2.1p cash per share	£35.5m	12/09

In order to block this offer from RPI, the board of ASA Resources called in administrators and declared the shares were non-transferable while the company is in administration. But RPI – whose offer values the shares at a 65 per cent premium to the closing price on the day before the initial announcement – has informed the administrators of its intention to provide $40m (£30.7m) of financing at a 5 per cent interest rate to help the company out of administration. The bidder has also extended the offer deadline to mid-September. **Accept**.

Cape Oil equipment & services	**Altrad Investment Authority SAS** Construction equipment	265p cash per share	£332m	12/09

The offer, which has the backing of Cape's directors, represents a 46 per cent premium to its closing price on the day prior to the announcement. Altrad Bidco has received valid acceptances for 94.2m shares in Cape, representing 77.8 per cent of the issued capital. As this remains short of the 90 per cent required for the deal to go through, the bidco has extended the deadline for acceptances again. **Accept**.

Jimmy Choo Retail	**Michael Kors** Retail	230p cash per share	£896m	14/09

This all-cash offer values Jimmy Choo's shares at a 37 per cent premium to the share price before the company was put up for sale. The directors have therefore, unsurprisingly, recommended investors accept the offer. **Accept**.

Kennedy Wilson Europe Real estate	**Kennedy Wilson Holdings** Real estate	*	£1.5bn	tba

*0.667 new Kennedy Wilson (KW) shares for each Kennedy Wilson Europe (KWE) share, or 0.3854 new shares and 300p in cash. The cash-and-shares option implies a share price of 1,145p, up on the original offer of 1,030p. We await the scheme documents before making a judgement on the most attractive option. **Await documents**.

Paysafe Financial technology	**PI UK Bidco** Bidco	590p cash per share	£2.96bn	24/09

Since May, digital payments processor Paysafe has been batting away attention from various private equity firms. Now management has recommended an all-cash offer – which values the shares at a 42 per cent premium to the closing price on the day before the takeover was announced – from a bidco created by Blackstone and CVC Capital Partners. **Accept**.

Revolution Bars Restaurants & bars	**Stonegate Pub Company** Restaurants & bars	203p cash per share	£102m	tba

This recommended offer is a 63 per cent premium to the target's share price prior to the start of the offer period in July. But Revolution Bars has also received interest from late night entertainment group Deltic. The possibility of a bidding war has sent the target's share price above the offer from Stonegate. **Await documents**.

Touchstone Innovations Investment services	**IP Group** Investment services	*	£466m	15/09

*2.2178 new IP Group shares in exchange for each Touchstone share. This offer, which values Touchstone at 304p has now received over 90 per cent acceptances which it requires to go through. **Accept**.

Worldpay Financial technology	**Vantiv** Financial technology	*	£9.3bn	tba

*55p cash per share and 0.0672 new Vantiv shares, excluding a 0.8p half-year dividend and a 4.2 special dividend that will be paid to Worldpay shareholders on the completion of the merger. This recommended offer values the shares at a 33 per cent premium to the closing price on the day before it was announced. The combined group is expected to be one of the largest fintech companies globally with an enterprise value of £22.2bn. **Await documents**.

*Booker and Sky have both received takeover offers which are being assessed by competition regulators.

DIRECTORS DEALINGS

BUYS

Company	Director	Date	No. of shares	Price (p)	Value (£)	Holding (shares)	Holding (%)
Allied Irish Banks♥	Helen Normoyle	29 Aug 17	2,000	501.3	10,026	2,000	0.000
Aura Energy♥	Peter Reeve (ch)	30 Aug 17	15,000	1.47773	222	12,852,365	1.619
Aura Energy♥	Peter Reeve (ch)	30 Aug 17	50,000	1.41616	708	12,617,365	1.590
Aura Energy♥	Peter Reeve (ch)	30 Aug 17	220,000	1.41616	3,116	12,837,365	1.617
BCA Marketplace♥	Avril Palmer-Baunack (ch)	24 Aug 17	180	186	335	725,572	0.093
BCA Marketplace♥	Avril Palmer-Baunack (ch)	24 Aug 17	263	184.38	485	725,001	0.093
BCA Marketplace♥	Avril Palmer-Baunack (ch)	24 Aug 17	391	184.51	721	725,392	0.093
BCA Marketplace♥	Avril Palmer-Baunack (ch)	24 Aug 17	533	184.38	983	724,205	0.093
BCA Marketplace♥	Avril Palmer-Baunack (ch)	24 Aug 17	533	184.38	983	724,738	0.093
BCA Marketplace	Timothy Lampert (cfo)	25 Aug 17	4,071	181.1	7,373	23,303	0.003
BCA Marketplace	Timothy Lampert (cfo)	29 Aug 17	3,929	179.31	7,045	27,232	0.003
Communisis	David Gilbertson (ch)	29 Aug 17	93,000	53.7362	49,975	93,000	0.044
Dixons Carphone	Andrea Joosen	25 Aug 17	2,600	178	4,628	11,676	0.001
Dixons Carphone	Humphrey Singer (cfo)	25 Aug 17	25,000	178	44,500	444,748	0.039
Dixons Carphone	Ian Livingston (ch)	25 Aug 17	54,655	182	99,472	105,631	0.009
Dixons Carphone	Gerry Murphy	30 Aug 17	30,000	176	52,800	50,000	0.004
Dixons Carphone	Fiona McBain	25 Aug 17	19,129	182	34,815	19,129	0.002
Dixons Carphone	Sebastian James (ceo)	25 Aug 17	25,000	178	44,500	631,835	0.055
Dixons Carphone♥	Tony DeNunzio	25 Aug 17	50,000	178	89,000	100,000	0.009
Ediston Property Inv. Co.	Colin Skinner	29 Aug 17	30,000	113.75	34,125	30,000	0.023
F&C Private Equity Trust	Swantje Conrad	30 Aug 17	8,323	324.465	27,005	8,323	0.011
FirstGroup	Tim O'Toole (ceo)	25 Aug 17	7,126	116.8	8,323	1,157,556	0.096
Greencore	Kevin O'Malley	29 Aug 17	19,500	197.6	38,532	19,500	0.003
Greencore ♥	Eoin Tonge (cfo)	25 Aug 17	25,132	196	49,259	396,818	0.056
Greencore ♥	John Warren	25 Aug 17	17,693	187.6	33,192	89,289	0.013
Greencore	Patrick Coveney (ceo)	25 Aug 17	50,000	188.4	94,200	3,478,366	0.493
Greencore	Gary Kennedy (ch)	24 Aug 17	10,000	196.1	19,610	158,441	0.022
Greencore	Sly Bailey	25 Aug 17	13,269	187.8	24,919	84,865	0.012
Greencore	Thomas Sampson	25 Aug 17	35,000	196.2	68,670	35,000	0.005
Griffin Mining	Dal Brynelsen	30 Aug 17	25,000	62	15,500	422,001	0.248
Menzies (John)	Philipp Joeinig	25 Aug 17	20,000	700	140,000	20,000	0.024
Primary Health Properties♥	Harry Hyman	25 Aug 17	378	113.25	428	2,876,085	0.480
Princess Private Equity Hjdg	Richard Battey	24 Aug 17	5,000	1000	50,000	40,000	0.058
Riverstone Energy♥	Kenneth Ryan	24 Aug 17	10,000	1,296.71	129,671	5,084,783	6.019
Riverstone Energy♥	David Leuschen	24 Aug 17	10,000	1,296.71	129,671	5,084,783	6.019
Riverstone Energy♥	Pierre Lapeyre Jr	24 Aug 17	10,000	1,296.71	129,671	5,084,783	6.019
Scientific Digital Imaging	David Tilston	24 Aug 17	25,000	26.45	6,613	25,000	0.028
Shanta Gold	Robin Fryer	30 Aug 17	120,000	3.75	4,500	930,000	0.121
Standard Life Private Eq. Trust	Alan Devine	25 Aug 17	102	317.86	324	5,613	0.004
Tarsus	David Gilbertson	29 Aug 17	16,000	310	49,600	26,000	0.023
Trinity Exploration & Prod.	James Menzies	24 Aug 17	250,000	11	27,500	500,000	0.177
WPP	Jacques Aigrain	25 Aug 17	4,000	1,438.94	57,558	13,000	0.001
Zenith Energy	Andrea Cattaneo (ceo)	30 Aug 17	100,000	7.67	7,670	2,647,485	2.127

SELLS

SThree	Steve Quinn	25 Aug 17	19,949	312.6	62,361	339,884	0.259

*Placing/tender/open offer ♥Spouse/connected party

Dixons directors show confidence after warning

HARRIET RUSSELL & HARRIET CLARFELT

Since giving ourselves a well-deserved pat on the back for suspecting all was not well at **Dixons Carphone (DC.)**, it only seems fair to follow up on the most recent director dealing activity after the group's August profit warning.

The shares plummeted 30 per cent following that update, so it's no surprise to see the board buying up. Chief executive Seb James had blamed a sluggish UK mobile market for triggering the warning, but that hasn't stopped him ploughing an additional £44,500 of his own money into the company's stock. He wasn't alone in this effort to shore up confidence, either – chief financial officer Humphrey Singer handed over the same sum, while chairman Ian Livingston coughed up £99,472 for an additional 54,655 shares.

The company is clearly on a mission to assure remaining shareholders that future prospects are good. Some City analysts even agree, citing the imminent launch of **Apple's (US:AAPL)** iPhone 8 as a potential catalyst for the shares. We're more sceptical, and want to see clear evidence that price inflation and the squeeze on British consumers isn't doing more long-term structural damage. Hold at 170p. *HR*

Supermarket sweep at Greencore

You'd be forgiven for thinking that shares in **Greencore (GNC)** have mimicked the pattern of British summer weather: things look reasonably steady in July, before being dampened down in August. The global grocery producer stated on 24 August that it was "not aware of any developments" since its third-quarter trading update in July that could explain the weaker share price, although it said one site in Florida would now focus on fresh food and would no longer produce frozen products. In the past fortnight, management has collectively increased its shareholdings – perhaps in a bid to inspire greater confidence among investors.

Chief executive Patrick Coveney bought 50,000 shares at 188p each, worth £94,200. He holds 3.5m shares, or 0.49 per cent of the company. Meanwhile, chairman Gary Kennedy spent £19,610 on 10,000 shares at 196p each. Chief financial officer Eoin Tonge's spouse bought 25,132 shares worth £49,259. Together with purchases by four other directors or their spouses, the investments totalled £328,382.

At 207p, the shares are down 12 per cent on our original tip (Buy, 235p, 1 February 2017), but we still see further upside. Buy. *HC*

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*Alternative Investment Market †Overseas shares

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