STOCKS | FUNDS | INVESTMENT TRUSTS | PENSIONS AND SAVINGS

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SHARES

WE MAKE INVESTING EASIER

ALL CHANGE

How new management can be good for companies and their share price

THIS WEEK
WHITBREAD, SAGA, ASOS, CRODA, IAG
AND MORE

ANTIVIRUS EXPERT AVAST PRIMED FOR MEGA UK TECH IPO

WHICH IS MORE IMPORTANT FOR STOCK PICKING: QUALITY OR VALUATION?

WILL THE NEXT BATCH OF US CORPORATE EARNINGS **LIVE UP TO EXPECTATIONS?**

Which is more important: quality or valuation?

We want you to join in the debate about ways in which to pick stocks

Which is more important when considering making an investment into an individual stock: quality of the business or its valuation? It's an interesting debate which recently cropped up on a social media channel.

The boss of a US asset management company argued that the price of fundamentals, such as price to earnings (PE) or price to cash flow (P/CF), is more important than measures of quality. The latter can include return on capital employed (ROCE) and whether a company is deemed to have an economic moat which keeps competitors at bay.

In response, several social media users argued that the opposite applies; quality is deemed more important than valuation.

One person gave the analogy that you would do better buying property in London's Mayfair region than in Detroit over the long-term. We assume they implied the former may be a lot more expensive than the latter when making the initial investment, but the returns could be better over time.

Another person suggested that valuation was more important if you frequently rebalanced your portfolio, whereas quality of the business was more important for investors adopting a buy and hold strategy.

HOW TO IDENTIFY QUALITY

We've regularly discussed the importance of ROCE in *Shares* in helping to identify high-quality companies. We like companies which consistently make a good profit on the money they invest in their business, as represented by the return on capital employed figure.

In simple terms, ROCE is operating profit margin multiplied by capital turnover – the latter is calculated by dividing annual sales by shareholders' equity. The sales figure can be found on a company's income statement and shareholders' equity is found on the balance sheet.

ROCE will be based on historical information, whereas many investors will use earnings forecasts to measure the valuation of a share.

There is merit in using forecasts as the stock market is forward looking and the share price represents how the market believes the company will perform in the future. However, you have to remember that forecasts don't always prove to be correct.

IS A HIGH LEVEL OF ROCE SUSTAINABLE?

Many investors are happy to pay a high earnings multiple to own a quality business, arguing that the long-term returns will more than compensate for the high entry price.

However, this approach assumes that superior levels of ROCE will be maintained indefinitely. In reality, a high or rising ROCE is attractive to competitors or new entrants to an industry. That could serve to challenge a company's ability to sustain high levels of ROCE.

The concept of an economic moat comes into play here. Traditionally a moat refers to the water around a castle – something that makes it difficult for an invader to reach and conquer it.

An economic moat represents a competitive advantage that enables a business to fight off competition and maintain strong levels of market share.

Financial data and research provider Morningstar uses the concept of economic moats in its stock analysis. It says the moat is a structural feature that allows a firm to sustain excess profits over a long period of time.

HOW TO IDENTIFY A MOAT

Morningstar identifies five sources of long term competitive advantage which, where present, may indicate a company has an economic moat.

These include:

- **Intangible assets.** These are brands, patents or valuable licences that explicitly keep competitors at bay.
- **Cost advantage.** A firm that can provide goods or services at lower cost than its peer group has an advantage because it can undercut rivals on price. The firm may also wish to sell products and services at the same price but get a bigger profit margin than competitors.
- **Switching costs.** There is a competitive advantage in charging chunky exit fees to leave a company's service. It stops customers leaving, unless they are offered a large improvement in either price or performance with a third party.
- **Network effect.** Strong companies can get even stronger when more people use their product or service.
- **Efficient scale.** This is when a market of limited size is effectively served by one or just a few companies. It's not worth another party entering the market, because their participation would result in insufficient returns for all players.

MOATS CAN BE DESTROYED

It is important to stress that moats, once obtained, are not indestructible. For example, Nokia enjoyed a majority position in the mobile phone market until Apple launched the iPhone.

And more recently, we note Morningstar has downgraded its moat ratings on utility stocks **Centrica (CNA)** and **National Grid (NG.)** from 'narrow' to 'none'.

Centrica's moat loss is attributed to mounting political risk and competitive pressure, as well as the profitability collapse of the gas storage business that the group has ceased to operate. A tariff cap is likely to squeeze margins at Centrica's British Gas business. Morningstar also believes the proposed merger of two of the UK's biggest energy suppliers, Npower and **SSE (SSE)**, will create a 'powerful competitor'.

As for National Grid, Morningstar no longer has confidence that it will generate returns on invested capital above its assumed weighted average cost of capital over a full business cycle.

THE MAGIC FORMULA

Anyone seeking to combine both valuation and quality may wish to look at Joel Greenblatt's 'magic formula' which is about identifying good quality businesses at cheap prices.

Financial data websites like SharePad should have specific filters to apply this formula to the market, although it is worth noting the information will be based on historical data and won't have predictions on future profits. We will run a feature looking at Greenblatt's magic formula in a forthcoming edition of *Shares*. (DC)

WHAT DO YOU THINK?

We want you to get involved in the debate. Send us your views on whether quality or valuation is more important, and we'll publish the best responses in the digital magazine. Email yourviews@sharesmagazine.co.uk with 'Quality valuation debate' in the subject line.

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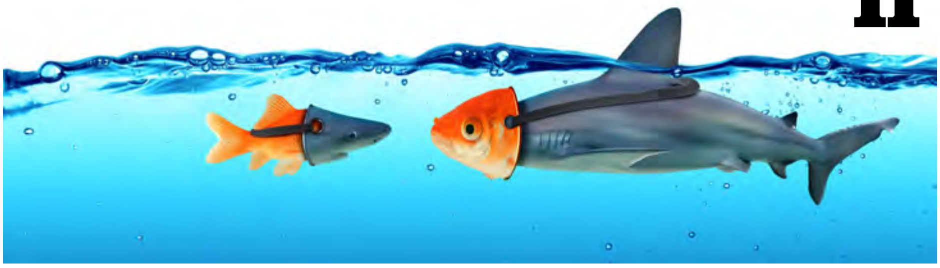

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4. A reporter should not have made a transaction of shares, derivatives or spread betting positions for seven working days before the publication of an article that mentions such interest. Reporters who have an interest in a company they have written about should not transact the shares within seven working days after the on-sale date of the magazine.

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BROKER RATINGS EXPLAINED:

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

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

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

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

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

Costa spin-off calls at Whitbread gain momentum

Activist investors with a history of pushing for change now control 10% of Whitbread

A potential break-up of Costa Coffee and Premier Inn owner **Whitbread (WTB)** looks possible after US activist hedge fund Elliott Capital Advisors built a 6% stake in the company.

This is the largest single holding in Whitbread, and adds to the pressure to spin off Costa.

Elliott is the second activist investor to take an interest in Whitbread after Sachem Head snapped up a 3.4% stake in December, meaning nearly 10% of its shares are now controlled by investors that are pushing for change.

In the past, Sachem supported a break-up of pharma business **Shire (SHP)** while Elliott is currently trying to re-shape miner **BHP Billiton (BLT)**.

AJ Bell's Russ Mould says there is a 'widely-held belief' Whitbread should separate Costa Coffee from its Premier Inn division as they are both different businesses and could be worth more as individual entities.

Costa has recently struggled as like-for-like sales dipped 0.1% in its third quarter.

Stockbroker Numis analyst Tim Barratt argues it is difficult to know whether Costa could attract a premium if sold, believing a demerger would be the more straightforward route. (LMJ)

Activist investor Elliott rumoured to have Micro Focus in its sights

Suse Linux spin-out or complete sale believed to be possible options

SHARES IN **Micro Focus (MCRO)** have spiked higher after reports that activist investor Elliott is building a stake. While the size of any investment remains unknown and Elliott's intentions unclear, stock market gossip suggests that Elliott plans to push for major changes at the FTSE 100 enterprise software business.

This could involve Micro Focus spinning out its Suse Linux business acquired as part of its Attachmate acquisition in 2014. Alternatively, Elliott could try to force the sale of the entire company, probably to a private equity investor.

Micro Focus' shares are trading at £12.76, close to their highest level since collapsing in March after revealing integration issues with its $8.8bn HPES acquisition.

Meanwhile Elliott has exited its long held position in **GAME Digital (GMD)**, the video games hardware-to-software retailer closely aligned with shareholder **Sports Direct International (SPD)**.

It has disposed of its 36.98% stake in GAME, attempting to morph from a seller of physical games into a gaming experiences provider, eliminating a large overhang in the stock. (SF/JC)

Pound pushes to highest level since Brexit vote

Currency movements could help explain the underperformance of the FTSE 100

The pound is back on the front foot, reaching its highest levels versus the dollar since the Brexit vote as we went to press.

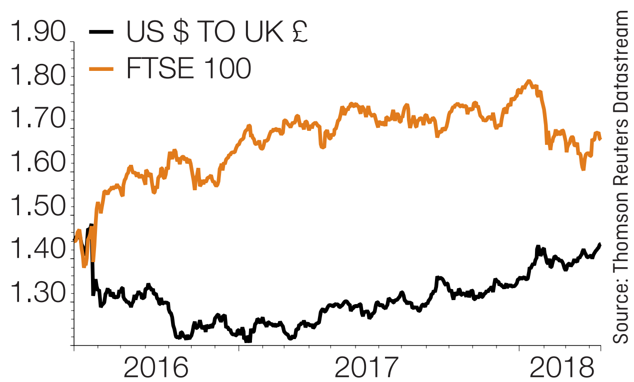
The resurgence of sterling reflects the first increase in UK interest rates in more than a decade in November 2017, expectations for a further hike when the Bank of England (BoE) next meets on 10 May, and the impact on the dollar of tensions over trade between the US and several countries, most notably China.

As the chart shows, the renaissance of sterling has implications for the performance of the FTSE 100, undermining the relative value of its constituents' large amount of overseas earnings.

Although there has been a wider hit to global markets this year thanks to issues in the technology sector and the war of words over trade, the strong pound may explain why the FTSE 100 has underperformed other global indices of late.

Pound above $1.437 vs the dollar on 17 April

The scope for the BoE to increase rates is enhanced by a release from the Office for National Statistics showing that when wages are compared with its new CPIH measure of inflation (which includes housing costs), average weekly earnings rose 0.2% year-on-year in the three months to February. (TS)



Cyber security firm Avast set for £2.8bn IPO

Technology company to tap pent up online defence demand

CONSUMER ANTIVIRUS provider **Avast** hopes to float on the London stock market next month, potentially attracting a valuation in excess of $4bn (£2.8bn) according to reports.

This would be one of the biggest technology floats ever in the UK and is likely to ping the company into the FTSE 250 at the first opportunity.

The company aims to raise around $200m of funding (roughly £140m) from new investors, although this will largely be used to pay down some of its approximate $1.4bn to $1.6bn net debt.

Avast mainly sells direct to consumers, both under its own banner and through its popular AVG suite of antivirus tools, which it bought in 2016.

The company also supplies various endpoint protection, device performance and privacy tools, password management and parental control solutions to small and medium-sized businesses.

Around 435m people worldwide use Avast solutions to protect PCs, laptops and smartphones from malware and computer viruses.

The company has put up impressive growth figures over the past three years, reporting underlying operating profit of $299.7m in 2017, on $652.9m of revenue. A raft of one-off costs and amortisation charges meant that it made a $28.9m pre-tax loss. (SF)

British Airways owner eyes takeover of Norwegian Air

The company hopes to fire up discussions with struggling rival

British Airways owner **International Airlines Group (IAG)** is considering making a takeover offer for embattled low-cost rival Norwegian Air Shuttle.

The airline acquired a 4.61% stake in the firm to kick-start discussions with Norwegian Air, which it believes is an 'attractive investment.' The latter's strategy has been to try and apply a low-cost model to long haul routes.

International Airlines' interest in Norwegian Air could be seen as opportunistic after the latter airline became a victim of its exceptionally fast growth, with costs escalating just as fast.

IAG aquires 4.61% stake in Norwegian

At the end of 2017, Norwegian Air reported operating losses of approximately NOK2bn, down from an operating profit of NOK1.8bn in 2016.

Davy Research analyst Ross Harvey argues 2018 is an important year for Norwegian Air as it needs to get costs under control, whatever the outcome of the potential bid situation.

Over the last 12 months, the airline sector has experienced significant turbulence with Monarch and Air Berlin buckling under the pressure of a price war, intense competition and higher oil prices. (LMJ)

Apollo stalks FirstGroup with takeover interest

NEW YORK PRIVATE equity firm Apollo Global Management has made a takeover approach for transport operator **FirstGroup (FGP)**.

Although FirstGroup did not disclose any financial details when rebuffing an initial approach, it looks to be an opportunistic move given the shares have been weak over the last 12 months.

Any deal could face political obstacles with Liberum analyst Gerald Khoo noting: 'Private equity ownership of rail franchises seems unlikely to be acceptable.' (TS)

ImmuPharma collapses on trial failure

SHARES IN DRUG discovery company **ImmuPharma (IMM:AIM)** collapsed on 17 April showing how risky early stage drug development really is.

The company's lead drug Lupuzor failed to show meaningful statistical benefits over a placebo in Phase III trials. Lupus is an autoimmune disease that affects millions, famously including American singer and actress Selena Gomez.

ImmuPharma's share price crashed 85% to 22.7p on the news, leaving the firm's market value at just £32m. (LMJ)

JD Sports is still fighting fit

JD SPORTS FASHION'S (JD.) record full year results (17 Apr) confirm the athleisure boom among youthful gym-goers and fashion-conscious consumers still has legs.

Shrugging off the wider UK retail malaise, the trainers-to-gym kit seller 'remains confident in the robustness and international potential of the JD proposition', management 'excited by the major developments ahead'.

International development of the JD brand continues, while the acquisition of US footwear seller Finish Line could transform growth prospects in the world's biggest sport lifestyle footwear and apparel market. (JC)

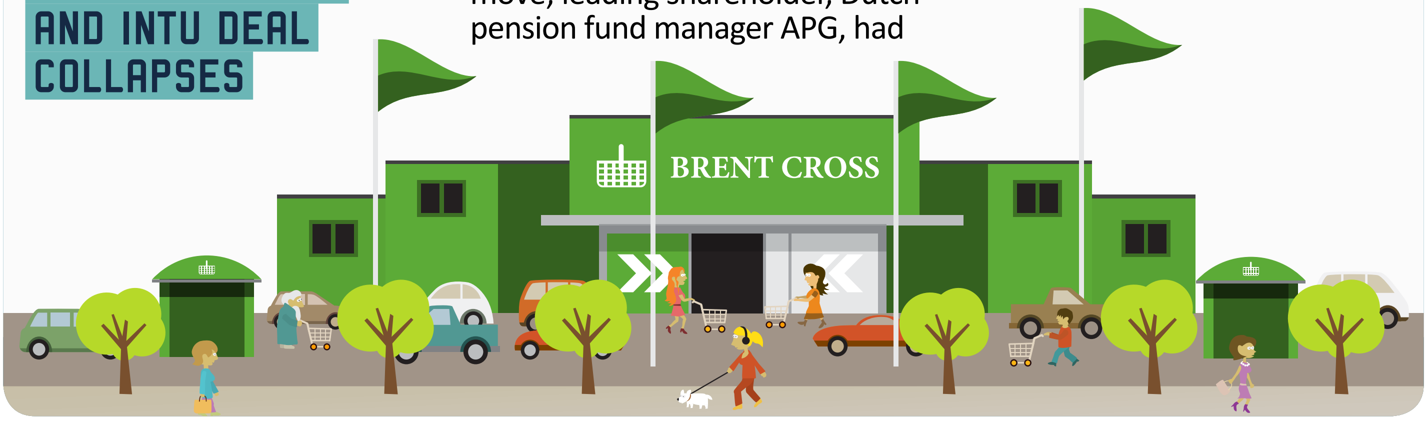
635p

KLEPIERRE WALKS AWAY FROM HAMMERSON BID AND INTU DEAL COLLAPSES

KLEPIERRE HAS GIVEN up on its pursuit of shopping centre landlord **Hammerson (HMSO)** after seeing a 635p per share takeover bid rebuffed.

Hammerson has also abandoned its own £3.4bn merger with **Intu Properties (INTU)** amid mounting investor unrest over the move; leading shareholder, Dutch pension fund manager APG, had come out against the deal.

Shares in Hammerson had reached 570p in the wake of Klepierre's interest but last week fell back to 473p when that deal collapsed. They made a recovery to 505p after Hammerson scrapped the Intu deal on 18 April.



DUNELM SHIFTS GROWTH FOCUS TO ONLINE CHANNEL

HOMEWARES MARKET leader **Dunelm (DNLM)** delivered impressive organic online growth (excluding its worldstores.co.uk and kiddicare.com sites) of 35.7% in the third quarter to 31 March.

Acknowledging the challenging consumer backdrop, new boss Nick Wilkinson says he is 'increasingly excited about the opportunities available to Dunelm to develop and grow a truly multichannel proposition'.

With consumers increasingly choosing to shop online, the Leicester-based bedding, curtains and kitchenware seller has halted store openings for the rest of this financial year as it focuses on growing web-based sales.

INTERCEDE TO COULD DO WITH A CHANGE OF GROWTH IDENTITY

THERE'S A new boss at **Intercede (IGP:AIM)** with Klaas van der Leest becoming chief executive of the identity management software minnow.

Getting the company to accelerate growth will be a priority given the company's dismal financial track record in recent years.

Under former combined chairman, CEO and founder Richard Parris (he's staying on as a non-executive director), Intercede consistently struggled to gain traction for its *MyID* identity and authentication suite of solutions.

Revenue since 2012 has stumbled up and down within a rough £7m to £11m range, slipping to £8.3m in its last reported full year to 31 March 2017. Analysts expect a little more than £9m for the more recent 12-month period. The company hasn't posted an operating profit since 2014.

Be brave and snap up Saga for a handsome 7% dividend yield

The equity valuation appears to be fully discounting recent setbacks to the business

We're taking a bold step and saying now is the time to buy over-50s travel and insurance specialist **Saga (SAGA)**. We believe the business still has significant appeal despite some recent setbacks. You're also getting paid a near-7% dividend yield while you wait for the return of earnings growth.

Four months ago Saga flagged trading issues in its insurance broking and travel businesses, in part due to the collapse of airline Monarch. Forward earnings guidance was also slashed due to higher investment spend to target high affinity customers and increase its customer numbers across the business in the coming years.

So why are we saying to buy now? Full year results to 31 January 2018 (published on 12 April) were in line with the revised guidance issued in December 2017. The company also remains highly cash generative, plus it reported 'promising' early signs with new business as a result of its plan to boost its customer base.

WHAT TO EXPECT

We think investors should approach Saga as an income investment and not expect

SAGA BUY
(Saga) 127.2p
Stop loss: 100p

Market value: £1.4bn

significant share price growth in the near-term. The company needs to show evidence that its capital employed is generating a decent return in order to win back the market's favour. That could take a year or more to achieve.

Any capital gains (i.e. share price rise) should therefore be treated as a nice bonus; if the share price goes nowhere then you're still being rewarded with a nice dividend.

Saga's travel business enjoys great visibility of bookings as its customers prefer to book their holidays in advance. However, travel only makes up for around 10% of the company's profits, so its fortunes arguably rest with its dominant insurance business.

The company has shifted to an affinity model and uses a panel of insurance brokers to find solutions for its customers and retain their loyalty.

This should help address the threat of customers researching the market themselves and picking a third party product aimed specifically at their demographic.

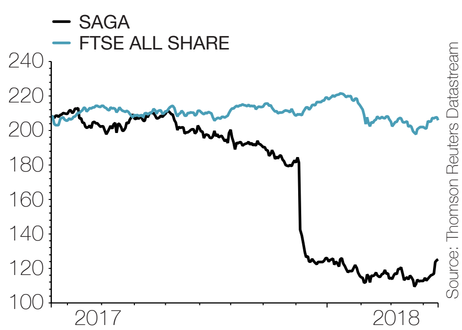
Another new initiative is a membership scheme called Possibilities which has already amassed over half a million members. The company believes this scheme greatly increases the chances of cross-selling opportunities.

WHAT'S THE EARNINGS POTENTIAL?

Stockbroker Numis forecasts 8.75p dividend for the current financial year, implying a 6.9% yield on the latest share price. Pre-tax profit is expected to dip slightly this financial year to £177m, before progressing to £184.8m in the year to 31 January 2020.

This isn't a risk-free investment, yet the shares trading on a mere 9.9 times forecast earnings look like they've fully factored in the recent setbacks. (DS)

BROKER SAYS: 3 5 0



SciSys looks far too cheap given its performance

The IT projects specialist could re-rate substantially as earnings quality improves

SCISYS BUY
(SSY:AIM) 139.5p
Stop loss: 111p

Market value: £40.5m

The market finally appears to have got over its Brexit hang-up regarding projects-based IT systems and services supplier **SciSys (SSY:AIM)**. Helping to win back the market's favour earlier this month was a €3.9m contract commitment from the European Space Agency (ESA) via contractor Airbus.

Yet there remains a huge valuation gap between the company and peers in price to earnings (PE) terms of more than 50% according to some analysts.

At 141p, SciSys is trading on a mere 12 times forecast earnings for 2018, and only 10.1 times 2019's estimates. That compares to a typical 25 to 30-times multiple for many other UK quoted software businesses.

This discount is unwarranted given how SciSys' earnings are moving forward. Pre-tax profit is expected to increase by nearly 16% this year to £4.4m; and by more than 18% to £5.2m in 2019.

The long-run nature of many of its contracts with blue-chip organisations, falling net debt, reliably decent dividends and ambitions to drive operating profit margins into double-digits (versus 2017's 8%) are all supportive factors for a share price re-rating.

If you presume the rating moves up to 14-times over the next year, SciSys could therefore trade around the 190p mark based on earnings forecasts for 2019.

WHAT DOES IT DO?

Chippenham-based SciSys provides project-based IT skills and services to large public sector (the ESD division), broadcast media (M&B) and space industry clients.

The Ministry of Defence is a big public sector client, while it has worked for years with the previously mentioned ESA, including on its Galileo and Mars missions. SciSys also works with the satellites sector, a rapidly growing industry in the always-connected digital age.

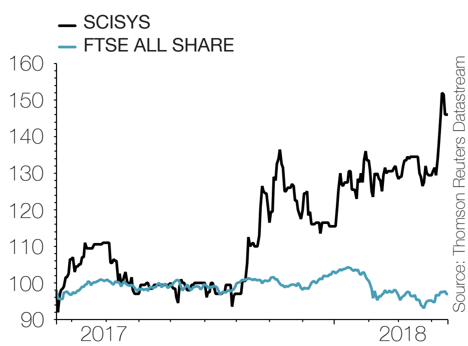
With a substantially bolstered media division since the £23.8m acquisition of German business ANNOVA in November 2016, it now has another genuine growth arm. A 12-year deal with the BBC was extended for another 10 years in February, helping Auntie to deliver local and national news, entertainment and archive material.

The order book at the end of 2017 was worth £91.3m, 41% higher than the year before. Organic growth opportunities may also be bolstered by bolt-on acquisitions.

Impressive cash flows (£8.5m of free cash flow in 2017) saw net debt cut to £5.9m at the year end. This should help maintain recent dividend growth in excess of 10%. There is a useful if modest 1.7% income yield but it demonstrates good financial discipline to shareholders.

Previously flagged as a *Great Idea* in *Shares* at 110.5p a little more than a year ago, we believe the stock offers further attractively-priced potential ahead so buy now. (SF)

BROKER SAYS: 1 0 0



FILTA

(FLTA:AIM) 196p

Gain to date: 15.3%

Original entry point:

Buy at 170p, 14 September 2017

FULL YEAR RESULTS from deep fat fryer cleaning specialist **Filta (FLTA:AIM)** were very impressive with revenue (excluding a business that's been sold) up 36% to £11.5m and a pre-tax profit of £1.6m (2016: £0.3m loss).

The key metric to assess the health of the business is MFUs (mobile filtration units) which increased by 16% to 394. These are the drivers for repeat revenue, says chief executive Jason Sayers.

Although there was minimal net growth in the number of franchise owners to 184 (2016: 182), Sayers explains to *Shares* that the quality of the network has improved as 'the big guys are getting better'.

Some of its biggest existing franchisees have been buying out struggling franchisees and also investing in new vans to take on more work.

Sayers says there is no problem in finding work; the issue lies with a lack of suitable technicians in the US, a geography accounting for 72% of group revenue. 'With full employment in the US, it's hard to find people. However, the strong economy also means franchisees can charge more in certain markets.'

The company is seeking acquisitions to boost its high-margin UK drainage business FiltaGMG and it is already seeing uplift in demand for its high-margin fridge seals business, also based in the UK.

SHARES SAYS:

Stockbroker Cenkos forecasts £2.6m adjusted pre-tax profit in 2018, rising to £3.2m in 2019. We remain big fans. Keep buying. (DC)

BROKER SAYS: 1 0 0

EDDIE STOBART LOGISTICS

(ESL:AIM) 136p

Loss to date: 14.2%

Original entry point:

Buy at 158.5p, 29 June 2017

EDDIE Stobart Logistics (ESL:AIM) has struggled on the stock market as investors are concerned about its ability to deliver growth and returns as Brexit negotiations continue.

The company operates storage facilities across the UK and a fleet of specialist equipment to carry heavy loads and transport cargo for businesses.

Shares in Eddie Stobart Logistics have reversed 14.2% to 136p since we flagged them as a *Great Idea* in June 2017 despite recently delivering a strong set of annual results (10 Apr).

In the year to 30 November 2017, the company revealed impressive underlying sales growth with revenues rising 9.4% to £623.9m.

The strong performance was driven by the e-commerce division where sales soared 111% to £103.4m.

Eddie Stobart is taking advantage of the fragmented UK market to further build its business through M&A, particularly in e-commerce as more people sell and buy products online.

In 2017, the company completed the acquisition of e-fulfilment specialist iForce, same-day delivery service Speedy Freight and Logistic People.

SHARES SAYS:

We remain optimistic about Eddie Stobart and feel its performance on the stock market does not reflect its prospects, however we will be monitoring the progress of Brexit talks on the free movement of goods between the EU and UK. (LMJ)

BROKER SAYS: 3 0 0

CRODA
(CRDA) £46.40

Gain to date: 6.4%

Original entry point:
Buy at £43.47, 15 February 2018

CHEMICALS BUSINESS **CRODA (CRDA)** has enjoyed further share price gains following a recent capital markets event, which focused on its small yet exciting seed enhancement business Incotec.

Incotec was acquired in 2015 and focuses on maximising seed performance through a range of services, including disinfection, film coating, encrusting, pelleting and analytical quality testing.

This will improve the quality of vegetable and field crops, which is essential as agricultural productivity must increase by 60% over the next 30 years, according to Croda.

The shares could gain further momentum following a trading update on 25 April, which may reveal more sales growth in its personal care division.

Numis analyst Kevin Fogarty is impressed by Incotec's seed enhancement tech, highlighting Croda is targeting a market worth $2.5bn, which is growing at 6% compound annual growth rate.

While Incotec is only a £50m revenue business at present, Fogarty notes Croda plans to boost growth by capitalising on macro themes of global population growth and threats to food production.

Croda is aiming to double the revenue base to approximately £100m and drive profit margins to over 20%, marking a substantial jump from Incotec's initial margins of 10%.

SHARES SAYS: ↗
We remain positive. (LMJ)

BROKER SAYS: 6 7 2

SAGE
(SGE) 597.8p

Loss to date: 23.9%

Original entry point:
Buy at 785.5p, 21 December 2017

SAGE'S (SGE) out of the blue growth shock on 13 April caught the whole market on the hop and it has caused huge damage to investors.

The shares may have fallen barely more than 8% on the day (recovering from early session declines of 20%-odd) but the stock has continued to be weak since.

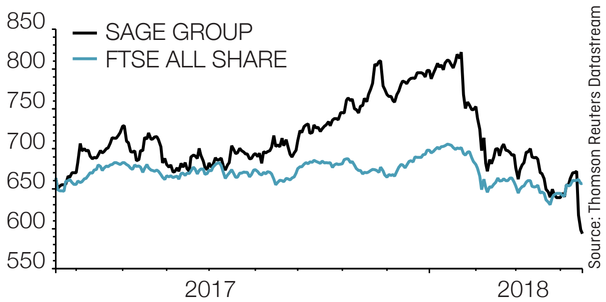
The company blames sluggish recurring revenue sales and software subscriptions, with traditional licenses and services seemingly growing at their expense.

Cynics might argue how well Sage's subscription-focused strategy is really working. However, it seems at least in part the problems have been self-inflicted judging by comments of 'inconsistent operation execution'.

That's two quarters running when organic revenue has failed to hit 8% targets leaving a lot to do even to catch up to lowered 7% growth rates for the full year. At least operating profit margins targets have been held at 27.5%.

The quicker Sage can remedy the situation, presuming it can, the better. Speeding up organic growth rates was a fundamental premise of our *Top Picks for 2018* story.

Sage has been putting up very decent returns for shareholders for years and that suggests management deserve the benefit of the doubt.



SHARES SAYS: ↗
Slicker execution is needed and we remain hopeful it will be delivered. (SF)

BROKER SAYS: 8 7 4

Watched pots do boil

Will the next batch of US corporate earnings live up to expectations?

With forecast growth at its highest level since 2011, we look at why the next batch of US results is relevant for many UK investors

As we write the US first quarter corporate earnings season is in full swing. Whereas in the UK most companies report results just twice a year, US firms report in full once a quarter.

This has attracted some criticism on the basis it leads to too great a focus on short-term performance among investors and, more crucially, management teams.

Short-term expectations this time are high. Overall analysts at New York-based investment strategist CFRA expect a 16.3% advance in earnings in the first quarter. This would represent the most significant growth since 2011.

WHY ARE EXPECTATIONS SO ELEVATED?

President Donald Trump signed a bill in December which lowered US corporation tax from 35% to 21%. This should boost the bottom line at companies with material US operations. The economic picture also remains supportive.

'Strong current profit growth is largely a reflection of favourable economic conditions,' says investment bank UBS.

'Healthy business confidence and still-low financing costs are boosting business spending on investments and labour. In turn, this is boosting consumer confidence and driving consistent gains in consumer spending.'

However, stock market volatility and tensions over trade between the US, China and to a lesser extent Mexico could see forward guidance from US firms disappoint.

Management, looking to massage expectations, may reach for these macro-economic factors as they look to lower the bar for earnings releases in the remainder of the year.

WHAT HAS HAPPENED SO FAR?

Against the high expectations there has been an uncertain start with big US banks Citigroup, JP Morgan Chase and Wells Fargo all disappointing investors to a greater or lesser extent.

This reflected uncertain messaging on the outlook, the fact that profit increases had already been priced in to their stock valuations ahead of time, and JP Morgan CEO Jamie Dimon's comment that 'the environment is intensely competitive and lending was flat for the quarter'.

WHY IS THIS IMPORTANT FOR UK INVESTORS?

The US is by some distance the largest and most liquid market in the world and as such tends to set the tone for other global exchanges.

Listed in the US are global leaders in several different industry sectors, with household names like Facebook, Coca-Cola and Apple all present and correct.

Many UK investors will have exposure to US stocks through funds or exchange-traded funds even if they do not invest across the pond directly.

Finally, because many UK companies do not report on a quarterly basis or, if they do, typically report later, investors look for clues in US companies' earnings on how their UK-listed counterparts might be faring.

WHO'S REPORTING WHEN AND WHAT'S THE READ-ACROSS TO UK STOCKS?

Next week sees the peak of the reporting season. Read on to discover the industry leaders which are scheduled to update the stock market.

For three key examples we show the earnings per share forecast and relevant London-listed businesses which are either competitors or suppliers to these US titans. (TS)

US EARNINGS DATES FOR THE DIARY

20 APRIL

PROCTOR & GAMBLE

EARNINGS IN FOCUS
GENERAL ELECTRIC

Why is it interesting?
General Electric can be a useful bellwether due to the sheer scale of diversity of its global operations which encompass aviation, healthcare, power, renewable energy, venture capital and finance, transportation and oil and gas.

Relevant UK-listed companies: **Rolls-Royce (RR.)**, **Smiths Group (SMIN)**, **Weir (WEIR)**

23 APRIL

ALPHABET (GOOGLE)

24 APRIL

CATERPILLAR
COCA-COLA

EARNINGS IN FOCUS
LOCKHEED MARTIN
EPS SHARE FORECAST: $3.42

Why is it interesting?
One of the largest global defence businesses, Lockheed's earnings performance and outlook comments may demonstrate if the recent increase in geopolitical tensions, including airstrikes in Syria, could benefit demand for industry players.

Relevant UK stocks: **BAE Systems (BA.)**, **QinetiQ (QQ.)**, **Ultra Electronics (ULE)**

25 APRIL

AT&T
BOEING
FACEBOOK
TWITTER
VISA

EARNINGS IN FOCUS
COMCAST
EPS SHARE FORECAST: $0.59

Why is it interesting?
As the largest broadcasting and cable television firm by revenue in the world, the owner of NBC and Universal should offer some insight into global TV advertising trends.

For UK investors, Comcast's interest in pay-TV firm **Sky (SKY)** is also a consideration with management commentary on this situation possible alongside the numbers.

Relevant UK stocks: **ITV (ITV)**, Sky, **WPP (WPP)**

26 APRIL

AMERICAN AIRLINES
CONOCOPHILLIPS
GENERAL MOTORS
MICROSOFT
TIME WARNER
STARBUCKS

27 APRIL

CHEVRON
EXXONMOBIL

Source for reporting dates: Yahoo Finance

ALL CHANGE

How new management can be good for companies and their share price

One of the key ingredients in the success or failure of a company is the quality of its management. When change at the top of a struggling company occurs, it can often act as a catalyst for an underperforming business and trigger a share price boost.

Evaluating the skill sets of boardroom leaders is no easy feat, yet there are CEOs out there with proven pedigree in turning companies around or taking them to the next level. In business as in football, recruiting a best-in-class manager can make all the difference between success and failure.

Thomas Wilson, UK Equity Fund Manager at BMO Asset Management, says management change can be important in ensuring a high-quality business that is currently under-earning can fulfil its potential and hence fairly reflect its prospects. 'Poor management can be extremely detrimental to businesses and share prices. A change of management can however be the catalyst needed for a company to meet its capability,' he adds.

In agreement is Alex Savvides, manager of the **JOHCM UK Dynamic Fund (GB00B4T7HR59)**. 'Positive corporate changes, particularly new management teams with new strategies, can be a major driver of stock market returns,' says Savvides.

'Investors are quick to discount known or quantifiable threats, but they are typically slow to identify and assess how company management teams are responding to these threats and tackling issues in their businesses. This often results in these stocks trading at pronounced discounts to their intrinsic long-term values, which is where the opportunity lies for investors.'

Savvides reckons backing the right management team is a critical component of investing. He and his team spend a long time meeting management in order to form an informed view on their abilities.

'It's a qualitative judgment but an essential part of investing in corporate change stories, one centred on understanding the management team's approach to capital allocation and cash flow and ensuring that they really understand why the company was previously struggling,' he adds.

'We want senior management to show rational thought but also to exhibit an activist mentality, being unafraid to challenge the status quo and drive through positive strategic change.'

Simon Gergel, manager of **The Merchants Trust (MRCH)**, pays 'close attention to the management teams of the businesses we invest in. This is particularly important in turnaround situations where a change of management can provide a powerful catalyst to drive performance.'

Gergel says Leo Quinn has been instrumental in the recovery strategy at **Balfour Beatty (BBY)**, bringing in rigorous controls and disciplines, which are critical in construction businesses, as well as numerous other changes to operational processes.


Leo Quinn

Nevertheless, investors shouldn't buy part a doomed business solely on the appointment of a new CEO, seasoned or otherwise. As Warren Buffett once quipped: 'Our conclusion is that, with few exceptions, when management with a reputation for brilliance tackles a business with a reputation for poor fundamental economics, it is the reputation of the business that remains intact.'

1 January 2015

Leo Quinn takes up his position as Balfour Beatty CEO

Mr Fixit – Leo Quinn

Share price return as CEO of De La Rue =

180%

Share price return as CEO of QinetiQ =

9.6%

Share price return as CEO of Balfour Beatty* =

30.4%

*As at 13 April 2018

THE LATEST CHANGES

Management change is a hot topic right now. Advertising agency **WPP (WPP)** ihas parted ways with CEO Martin Sorrell amid an investigation into his personal conduct, while **Tesco's (TSCO)** turnaround has triggered fresh speculation that its CEO Dave Lewis is in the frame for the top job at Marmite maker **Unilever (ULVR)**, with long-serving Paul Polman preparing to step down by the end of the year.

Meanwhile, the **London Stock Exchange (LSE)** has appointed Goldman Sachs veteran David Schwimmer as its new CEO.

Quoted company leadership undergoing significant change is the fast-evolving retail sector. Struggling baby goods purveyor **Mothercare (MTC)** recently ousted Mark Newton-Jones and appointed retail industry veteran David Wood as its new CEO, tasked with completing its transformation plan and return to growth.

The new Mothercare head honcho has form in turning around retail businesses, notably US grocer-to-pharmaceuticals business Kmart, and a return to growth in the Middle East, where the heritage brand has cache, gives Wood something to work with.

Fresh leadership is in play at electricals-to-telecoms retailer **Dixons Carphone (DC.)**, which has drafted in Shop Direct boss Alex Baldock for his digital expertise succeeding Sebastian James as CEO and recruited **Halfords (HFD)** bean counter Jonny Mason as its new numbers man. Nick Wilkinson, known for his stewardship of Evans Cycles, is the new CEO broom at homewares leader **Dunelm (DNLM)**.

1 SEPTEMBER 2014

DAVE LEWIS TAKES CONTROL OF TESCO

HAIL TO THE CHIEF(S)

Two of the country's biggest retailers are being successfully turned around by a pair of 'Daves'; Tesco's Dave Lewis and rival David Potts at **WM Morrison Supermarkets (MRW)**.

Stephen Message, manager of the **L&G UK Equity Income Trust (GB00B6HBD759)**, recalls about Tesco: 'Current CEO Dave Lewis joined the business in 2014 with the task of restoring profitability and improving the health of the balance sheet. Tesco had suffered through overexpansion, accounting issues, lost market share to discount retailers, deteriorating supplier relationships, poor brand perception and customer loyalty. This ultimately led to the business suspending dividends until performance improved.'

Message continues: 'Having previously spent 27 years at Unilever, the new CEO initiated a restructuring programme to reduce operating costs whilst improving the range and Tesco's brand perception to win customers back.

'Move forward three years and profit margins have started to recover whilst the dividend was recently reinitiated. Another interesting development in the recovery phase has been the recently completed merger with food wholesaler Booker.

'This should provide the combined group with more levers to make improvements. Booker itself was also subject to a turnaround under CEO Charles Wilson, who joined Tesco as part of the merger and will become the UK division's CEO.'

David Potts

Annual numbers (14 Mar) from Morrisons confirmed the Bradford-based grocer has become far more competitive under Potts, appointment to the hot seat in early 2015 and developing the vertically-integrated food retailer's wholesale business into an underappreciated additional growth engine.

For the year to 4 February 2018, Morrisons reported an 11% increase in underlying pre-tax profit to £374m and net debt reduced to £973m. Shareholders were also treated to a surprise 4p special dividend reflecting Potts' confidence in continued cash generation and growth.

Away from retail, sweeteners giant **Tate & Lyle (TATE)** has a positive catalyst in the promotion of CFO Nick Hampton to CEO, providing the prospect of a renewed strategy to accelerate the £2.63bn cap's transformation to a higher margin speciality ingredients play. Recently (1 Apr) handed the CEO baton from Javed Ahmed, Hampton has an opportunity to enliven Tate & Lyle's share price when communicating his exciting plans for the business at May's full year results.

Nick Hampton

REPAIRING THE MESS CREATED BY PREVIOUS MANAGEMENT

BMO Asset Management's Wilson cites **Bovis Homes (BVS)** as a recent successful management change story. 'Although a cyclical business, Bovis has on average generated a return in excess of its cost of capital, even when allowing for the credit crisis,' says Wilson. 'The returns are driven by a competitive advantage compared to smaller players, with its technical expertise allowing it to construct big and complex sites, and its relationships with local authorities allowing it to get planning permission and add-value through the design process.'

Sadly, for shareholders, Bovis lost its way and was poorly run with previous management 'prioritising growth over returns'.

'The quality of homes built fell significantly and the company generated operating profit margins well below those of peers,' Wilson says. The company issued multiple profit warnings during 2016. Unsurprisingly, share price performance, especially when compared to other listed UK housebuilders, was extremely poor through this period.'

5 April 2017

Greg Fitzgerald appointed CEO of Bovis Homes

A poor strategy, execution and culture triggered the parting of the ways between the company and its CEO of eight years, David Ritchie, in January 2017. New CEO Greg Fitzgerald was installed in April 2017 and 'subsequently set out a strategy to shrink the business to improve the quality of the product, ensuring customers were happy with the house they were buying and ultimately improving profit margins'.

Wilson notes progress has been 'exceptional' with the company enjoying a 4-star Home Builders Federation rating from its customers.

'Ultimately this was a case of a high-quality business not being valued to fairly reflect its prospects because of poor management,' Wilson says. 'A change in management team changed all that.'

JOHCM UK Dynamic's Savvides says one of his largest active positions, component distributor **Electrocomponents (ECM)**, is a good example of where a change in leadership transformed a company's fortunes. Lindsley Ruth was appointed as CEO in April 2015 at a time when the company was underperforming.

1 April 2015

Lindsey Ruth hops into the hot seat at Electrocomponents

'He implemented a new, multi-faceted strategy that has succeeded in the face of market scepticism and the share price has risen sharply as a result,' says Savvides. 'Of course, not every new management team we back will deliver. That's part of the challenge.'

Elsewhere, Aviva Investors' Head of UK equities Trevor Green comments: 'Paper and packaging is not at first sight a glamorous sector, but under Miles Robert's watch he has made **DS Smith (SMDS)** an attractive investment culminating in the stock entering the FTSE 100 index last year.

'Every time someone buys anything from Amazon in the UK, the item has to come in a package. Most likely, this package will come from a DS Smith factory. Miles became CEO in 2010 and quickly moved the company away from being a highly cyclical paper company into a more stable higher-returns business, which has been applauded by shareholders.'

Management change in action

Marks & Spencer (MKS) 266.5p

CEO: Steve Rowe
Chairman: Archie Norman

Steve Lowe

Bleak UK high street conditions and a rapid shift to the internet that many argue foretells the demise of physical stores are key factors behind the weak share price of structurally challenged **Marks & Spencer (MKS)**.

Yet M&S has carried out a senior management overhaul which bulls argue means the right team is in place to improve its lacklustre performance. The British retail institution is steered by CEO Steve Rowe, appointed in 2016 and whose transformation programme is beginning to stop the rot; Marks & Spencer's Christmas trading was mixed rather than disastrous.

He is trying to bring the FTSE 100 stalwart back into full favour with shoppers by getting the fashion basics right, focusing on quality rather than price, cutting down on store space and getting the online operations right. Ruthless Rowe – nicknamed 'Nails' – has also shuttered stores in loss-making international markets. Crucially, he is now being assisted by Archie Norman, the British business titan who joined the board as non-executive chairman on 1 September 2017.

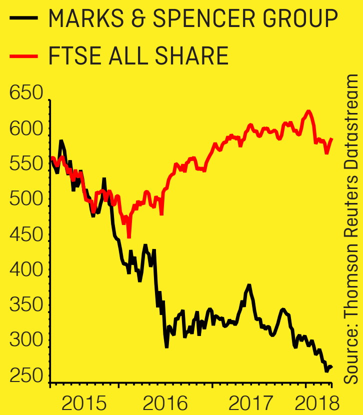
Very much hands-on, Norman is shaking up the culture at Marks & Spencer and is the ultimate trouble-shooter for the ultimate turnaround, previously instrumental in transforming ASDA and **Kingfisher (KGF)**.

Marks & Spencer also now has former Halfords boss Jill McDonald in place as managing director of Clothing & Home; Stuart Machin takes up the new role of managing director Food in late April and the senior management team will be joined by new finance director Humphrey Singer from Dixons Carphone in July.

The high street doyen therefore boasts a strong brand, a compelling plan backed by experienced leadership and investors are also being paid a 7% dividend yield while they wait for the recovery to bear fruit. The task won't be easy – clothing, home and food like-for-like sales weakened in the third quarter to 30 December.

While Marks & Spencer remains over-spaced, shoppers still like to see and feel products, socialise while they shop and enjoy the experience of some retail therapy.

This gives the bricks-and-mortar, operationally geared shopkeeper an advantage *if* Rowe and Norman can get the tills ringing again. Ahead of full year results (23 May), Shore Capital forecasts improved adjusted pre-tax profit of £593.2m (2017: £584.5m) and a maintained dividend of 18.7p. (JC)



How do analysts rate Norman's chances?*

Buys: 7

Holds: 7

Sell: 11

*Based on analysts' recommendations on the stock. Source: Thomson Reuters

Management change in action

Dialight (DIA) 530p

Chief executive: Marty Rapp

Marty Rapp

Shareholders in LED lighting systems designer **Dialight (DIA)** are pinning their hopes on new leadership drawing a line under manufacturing execution problems. The £170m company is at the cutting edge of LED technology, specialising in modern and efficient lighting solutions for hazardous and challenging industrial applications.

Think power plants, utility installations and oil rigs, or vast factories, warehouses, distribution centres, for example. It also supplies warning lights for tall buildings, mobile masts and wind turbines, among other things, designed to stop planes and helicopters crashing into them at night.

LEDs are brighter and about 10-times as energy efficient as normal light bulbs, so there are large cost savings to be had for big energy users.

This creates long-run demand, something that Dialight has struggled to manage over recent years. Failure to meet production targets led to the decision in 2017 to outsource manufacturing so it could concentrate on the design process. Silicon Valley-based Sanmina was selected as its partner, but the transition has been beset with problems, including product launch and production delays.

This led to two profit warnings during 2017. Those problems came to a head in early January this year and cost former chief executive Michael Sutsko his job. It is early days for his replacement Marty Rapp, but analysts believe the new boss has the engineering and manufacturing background to turn things around.

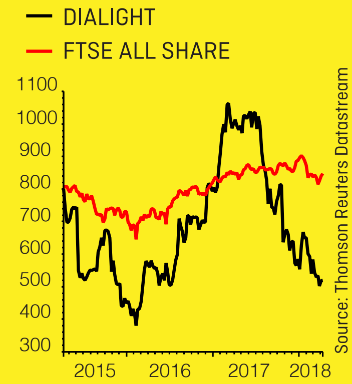
Rapp is a former executive at electronics designer and manufacturer **Laird (LRD)**, which recently agreed to a £1bn takeover. He has also held engineering positions at Monsanto, the Fortune 500 agriculture giant.

'His main priority is to accelerate the recovery after the relationship with contract manufacturer Sanmina began so poorly,' say analysts at Investec. Results for the year to 31 December 2017 show the scale of the job at hand, reporting expected declines in underlying pre-tax profit and operating cash flow on pretty much flat revenue.

'Even the deliveries that were achieved incurred additional costs, reducing margins,' pointed out Investec in February. But there is firm belief that Dialight's destiny is in its own hands, with Investec continuing to believe that Dialight's production problems can be remedied, enabling it to achieve strong growth and restore investor confidence.

If it is right, then there is scope for significant share price appreciation in the months and years ahead. Investec has a 12-month target price of 790p, implying 49% upside from the current 530p level. This is a company who's shares traded at close on £14 levels just five years ago.

Analysts at investment bank Berenberg believe there may have been large market share declines during months of upheaval. Winning back lost customers means regaining trust. In our view there is scope for recovery but evidence of better execution is needed. (SF)



How do analysts rate Rapp's chances?*

Buys: 1

Holds: 2

Sell: 1

*Based on analysts' recommendations on the stock. Source: Thomson Reuters

Management change in action

ITV (ITV) 144.8p

Chief executive: Carolyn McCall


Carolyn McCall

In some respects, the new chief executive of **ITV (ITV)** has a hard act to follow but there are reasons for optimism as **EasyJet (EZJ)** alumni Carolyn McCall gets to grips with the free-to-air broadcaster.

Under the tenure of predecessor Adam Crozier, which lasted from April 2010 to June 2017, the share price advanced 160%, debt was substantially reduced, and the company became increasingly profitable. A 2009 pre-tax profit of £25m was dwarfed by 2016's total of £847m.

More recently, sentiment towards the stock has soured as advertising revenue has come under pressure. McCall's challenge, having taken up the reins at the start of 2018, will be to capitalise on opportunities in areas like video-on-demand (VOD) and TV production.

ITV trades on an undemanding valuation of 9.6 times 2018 forecast earnings and the outlook for advertising spend is boosted by the football World Cup in Russia this summer.

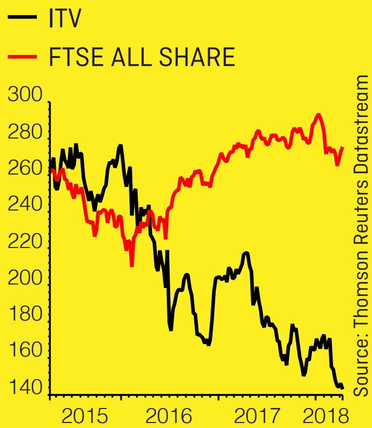
McCall has already made some early moves to refresh the strategy of the business, which in the early part of Crozier's tenure at least was focused on steadying the ship and getting the financial performance back on track.

The network programme budget, or in other words how much its spends on the programming across its channels, is being increased for 2018 to £1.1bn from a little over £1bn in 2017, a level it had roughly been held at since the financial crisis. The money is evenly split between drama and sports rights.

The company also outlined investment of between £15m and £20m on property, online and data investments. The extent to which McCall can monetise VOD might dictate how her leadership of the business comes to be viewed in the future and she may outline her plans in more detail alongside half year results on 25 July.

In theory ITV has a substantial opportunity. In its own words this service offers 'more targeted demographics and a high-quality, trusted and measured environment for online advertisers'.

The reference to quality and trust is highly relevant given the issues advertisers have faced with other providers of online content. In May 2017 some big names pulled ads from YouTube after their brands were displayed alongside extremist material. This risk is arguably reduced with ITV's VOD service.



Liberum analyst Ian Whittaker has estimated that if the company was to capture 10% of the online display advertising market by 2020 against his current forecast of 6.5% it could deliver a 7% boost to earnings. (TS)

How do analysts rate McCall's chances?*

*Based on analysts' recommendations on the stock. Source: Thomson Reuters

FRIDAY 20 APRIL

TRADING STATEMENTS	
Reckitt Benckiser	RB.

MONDAY 23 APRIL

FINALS	
Arix Bioscience	ARIX
Midatech Pharma	MTPH

TUESDAY 24 APRIL

FINALS	
Circassia Pharmaceuticals	CIR
Sportech	SPO
INTERIMS	
Focusrite	TUNE
TRADING STATEMENTS	
Anglo American	AAL
London Stock Exchange	LSE
St James's Place	STJ

WEDNESDAY 25 APRIL

FINALS	
Warpaint London	W7L
Whitbread	WTB
INTERIMS	
Fenner	FENR
GlaxoSmithKline	GSK
TRADING STATEMENTS	
Antofagasta	ANTO
Croda	CRDA
Intu Properties	INTU
Lloyds	LLOY
Persimmon	PSN
Tullow Oil	TLW

THURSDAY 26 APRIL

FINALS	
Air Partner	AIR
Capita	CPI
Touchstar	TST
U and I	UAI
INTERIMS	
Barclays	BARC
TRADING STATEMENTS	
Cobham	COB
Domino's Pizza	DOM
Elementis	ELM
Kaz Minerals	KAZ
Meggitt	MGGT
Synthomer	SYNT
Taylor Wimpey	TW.
Weir	WEIR

EX-DIVIDEND

Aberdeen Asian Income Fund	AAIF	2.25p
Antofagasta	ANTO	$0.41
Bankers	BNKR	4.86p
Henry Boot	BOOT	5.2p
BlackRock Latin America	BRLA	$0.07
Central Asia Metals	CAML	10p
Capital Drilling	CAPD	$0.01
Curtis Banks	CBP	4.75p
Churchill China	CHH	17.2p
Custodian REIT	CREI	1.61p
T Clarke	CTO	2.9p
Charles Taylor	CTR	7.7p
City of London Investment Trust	CTY	4.55p
Dunedin Enterprise Investment Trust	DNE	5.5p
Eurocell	ECEL	6p
Man Group	EMG	4.18p
Foxtons	FOXT	0.27p
Franchise Brands	FRAN	0.33p
Fresnillo	FRES	$0.3
Glencore	GLEN	$0.1
Hunters Property	HUNT	1.5p
Harwood Wealth Management	HW.	2.24p
Impax Environmental Markets	IEM	2.5p
International Public Partnership	INPP	3.41p
IWG	IWG	3.95p
Legal & General	LGEN	11.05p
Mortgage Advice Bureau	MAB1	11.9p
Morgan Sindall	MGNS	29p
Marshall Motor	MMH	4.25p
Nahl	NAH	10.6p
National Express	NEX	9.25p
NewRiver Retail	NRR	5.25p
Petrofac	PFC	$0.25
Portmeirion	PMP	27.62p
Porvair	PRV	2.7p
RELX	REL	27.7p
Smart Metering Systems	SMS	3.46p
StatPro	SOG	2.05p
Spirax-Sarco Engineering	SPX	62p
Secure Trust Bank	STB	61p
SThree	STHR	9.3p
TT Electronics	TTG	4.05p
Weir	WEIR	29p
William Hill	WMH	8.94p

AN ESCALATION IN tensions over Syria have helped oil prices move above $70 per barrel as investors await first quarter numbers from oil major **Royal Dutch Shell (RDSB)** on 26 April.

Investors may be looking for more clarity on the company's share buyback plans.

Fourth quarter results from the previous financial year revealed a disappointing performance from its refining business.

Out-of-favour consumer health and hygiene products powerhouse **Reckitt Benckiser (RB.)** needs to restore confidence in its growth story when reporting on first quarter progress (20 Apr).

Reckitt issued tepid sales growth guidance for 2018 with its full year results (19 Feb) and investors are concerned about a structural market slowdown and weak pricing.

HIGH STREET BANK **Lloyds (LLOY)** is updating the market on its first quarter performance on 25 April with investors hoping for a positive performance from the FTSE 100 constituent.

Full year results for 2017 contained news of a £1bn share buyback plan.

Click here for complete diary
www.sharesmagazine.co.uk/market-diary

Get ready for an important development with Chinese shares

We explain the importance of MSCI including more than 200 Chinese A-shares in its emerging markets index

With the war of words over tariff wars intensifying between the US and China, you may question the wisdom of investing in China at present.

However, from June index provider MSCI will begin to include 222 large cap China A-shares into its emerging market index as part of a two stage process, completing in September. That's a very important development, as we now explain.

WHY DOES IT MATTER?

The Chinese government has been making efforts to open up its domestic equities markets to foreign investors for some time.

It has operated a quota system, the qualified foreign institutional investor programme (QFII), which allowed fund managers to invest in China's capital markets.

The next development was the Hong Kong-Shanghai Connect in 2014 (followed by the Hong Kong-Shenzhen connect in 2016), allowing

international and Chinese investors to trade securities in each other's markets.

China is now also allowing foreign asset managers to set up shop in the country for the first time and tap their huge investment market. For the firms that have been awarded a wholly foreign owned enterprise (WFOE) licence, the products they launch are only available to Chinese investors.

However, a spokesman for asset manager **Standard Life Aberdeen (SLA)** says that being on the ground in China is a 'combination of servicing the domestic client base and undertaking on-the-ground due diligence to invest in Chinese companies on behalf of our clients where ever they are based in the world'.

Last year, Aberdeen's funds started making direct investments into China's domestic equities, called 'A-shares'. The country is now one of the asset manager's biggest allocations, doubling its exposure in 2017.

Investors looking for exposure to Aberdeen's China stock picks have a number of the company's investment trusts at their disposal. These include the **Aberdeen Asian Income Investment Trust (ASCI)** for instance.

CAN YOU AFFORD TO IGNORE CHINA?

China has produced some real heavyweight companies, the BATs for instance (Baidu, Alibaba and Tencent). However, if investors want exposure to

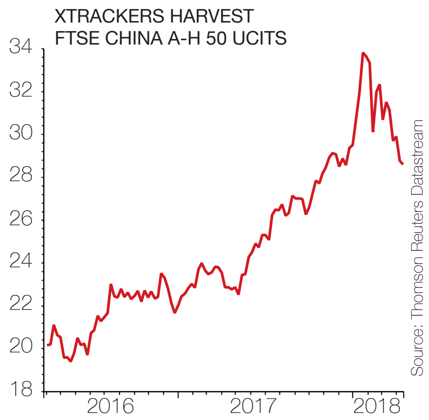
these companies, access to domestic A-shares is not required as they're also listed on other exchanges including Hong Kong's Hang Seng index, the New York Stock Exchange or traded in numerous places as American Depository Receipts.

Using Hong Kong is the main way Charlie Awdry, manager of **Janus Henderson China Opportunities Fund (GB0031860934)**, plays China. His fund does have an allocation to A-shares and accesses these using the Hong Kong-Shanghai stock connect. The manager has a preference for large cap, mature cash generative businesses mostly found on the Shanghai index.

Other managers prefer the smaller companies found on the Shenzhen exchange. Tiffany Hsiao, manager of **Matthew Asia China Small Companies (LU0721876364)**, says small cap Chinese companies are less volatile than their large cap peers and offer decent returns potential. One of her top picks, electrical appliances company Wuxi Little Swan, has returned 47.7% in a year.

ISN'T THE CHINESE MARKET VOLATILE?

Investors may still have the events of 2015 still in their minds, when the Shanghai Composite Index lost around 30% of its value in under a month. Such bouts of volatility, including the market being suspended twice on the opening day's trading of 2016, may reasonably



make investors reticent.

Another area of concern for those investors looking to China is that of corporate governance. Fortunately there are signs of improvement. Flavia Chong, head of Asia Pacific ex-Japan Equities at Aberdeen, says 'while corporate governance standards still leave much to be desired, we have found notable exceptions'. Among these, Chong counts drinks company Kweichow Moutai and white goods-maker Midea.

Paul Jackson, head of multi-asset at Invesco Powershares, says foreign interest in A-shares, has mainly disappeared since the 'rollercoaster ride of 2015'. However, he adds that with the inclusion of A-shares to the MSCI emerging market index coming up 'investors will be obliged to take an interest and others may be encouraged to do so'.

MSCI estimated in June last year (when it first announced the plan to include A-shares) that the Chinese shares would only account for 0.7% of its emerging market index and just 0.1% of its All Country World index.

Due to the small weighting of A-shares, Jackson says their inclusion is unlikely to cause a 'flood of money'. He does add that it's an important 'psychological step' that could put the equities onto the radar of many international investors.

MSCI has also indicated that it may increase the number of A-shares at a later date as well as increase their weighting on the index.

HOW TO GET PASSIVE EXPOSURE

For investors seeking to gain more direct A-shares exposure through a passive product there are a plethora of products available. For example, **Lyxor UCITS ETF CSI 300 A-Share (CSIA)** is comprised of stocks from both the Shanghai and Shenzhen exchanges and adds to diversity.

For a more concentrated approach, **DB X-trackers Harvest FTSE China A-H 50 UCITS ETF (AH50)** reflects the performance of the top 50 companies in the Shanghai or Shenzhen index.

With many ways to access to the Chinese equities markets compared to just 10 years ago, it's important to remember that the market is towards the top end of the risk spectrum.

David Hillier, head of multi-asset at Insight Investment, says 'investing in China brings its own special risks because, as a centrally planned economy, there is always the risk that the government can enter or regulate markets in unexpected ways at short notice'. (DC)

Produced by AJBell Media

RETIREMENT money show

13 June 2018
12:30 - 17:30

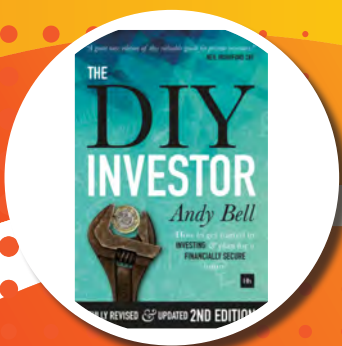
ARE YOU RETIREMENT READY?

Come to the **Retirement Money Show** at America Square, London, EC3N 2LB to find out more about retirement planning.

All attendees will receive a goody bag that includes:

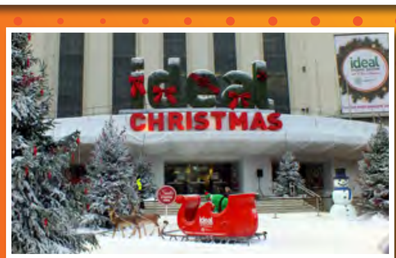
REGISTER NOW

A Mag-Lite Solitaire Incandescent Torch in a presentation box



The new DIY Investor book written by Andy Bell, CEO of AJ Bell (RRP £17.99)

PLUS all attendees will be entered into free prize draws for: Two tickets to the Windsor Enclosure at Royal Ascot, Two weekend tickets to the Ideal Home Show at Christmas and Two tickets to the RHS Hampton Court Flower Show.



It's no fun getting old when you're worried about running out of money, so do you have a financial plan for the possibility of living to be 100? Did you know that the current average retirement age is 64 years old and the average life expectancy is now 81 years old? To put this into perspective you might have to plan your retirement pot to last 17 years.

Come along to the **Retirement Money Show**, the London-based afternoon event run by Shares and AJ Bell Media which takes place on 13 June 2018 and features expert pension and financial speakers who will help investors better understand pensions and savings.

Register for free today and receive your **Retirement Money Show** goody bag when you arrive!

Discover more about the most important retirement issues and how best to manage your hard-earned money. The show is suitable for people still in employment and wanting to better **understand financial planning**, as well as those already in retirement looking to get the most from their pension and other assets.

Our speakers will be covering topics that are relevant to both those already in retirement and those who are still in work.

Knowing how to manage your pension pot either in preparation for later life or during retirement is one of the big challenges facing millions of people today and a central theme to the free-to-attend **Retirement Money Show**. It is one of a number of topics that we will discuss during the afternoon, so come along to the event armed with questions as there will be a wide range of people happy to talk to you.

You will have the opportunity to ask questions to most of the speakers and to **interact with specialists in savings, income, funds, ISAs and pensions/SIPPs** on the exhibition stands.

If you are new to the world of investing and pensions, don't think this event is only for financially-savvy people with years of experience in buying stocks, shares and funds. We purposely created an event that will serve the needs of both amateurs and experienced investors.

The **Retirement Money Show** is free to attend; you simply need to register in advance to secure your ticket. The afternoon event is being held on 13 June 2018 between 12.30 and 17.30 at the America Square Conference Centre, 1 America Square, 17 Crosswall, London, EC3N 2LB. The venue is well served by public transport with several tube stations on its doorstep.

Learn about:

- Managing cash flow & liquidity in retirement
- Balancing competing near and long-term financial demands
- Living your life during retirement years
- Making sure you retire on the best income
- Personal pensions – your guide to managed or self-investing
- ISAs – an alternative to pensions
- Long term managed income through Funds and Investment Trusts

If these are some of the many retirement planning issues that apply to you, then you need to join us at the **Retirement Money Show**.

Hear from:

Mike Boydell, Managing Director – Shares
Dan Brocklebank, Director – Orbis Access
John Carnegie – Monks Investment Trust
Stewart Cazier, Head of Retail – ThinCats
Nick Brind, Fund Manager – Polar Capital Financials Trust
Paul Mahoney, MD & Founder – Nova Financial
Tom Selby, Senior Analyst – AJ Bell
Paul Stallard, Commercial Director – The House Crowd
Presenter TBC – J.P. Morgan Asset Management
Presenter TBC – Close Brothers Asset Management

AT
AMERICA SQUARE, LONDON EC3N 2LB

To find out more and register
www.retirementmoneyshow.com
dimple.patel@sharesmagazine.co.uk
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How much investment risk do I need in retirement?

Balancing growth and risk is crucial as life expectancy increases

Getting the right balance between investment growth and risk is important for every investor, but for retirees it is even more crucial.

You need to ensure your money keeps growing so that it lasts throughout your retirement, and protect yourself from a market crash that could wipe out your savings.

WHY DO I NEED INVESTMENT GROWTH IN RETIREMENT?

The retirement landscape is vastly different than it was when your parents retired.

Most people used to work towards a retirement date when they would buy an annuity – a policy that provides a guaranteed income for life. It made sense to gradually reduce investment risk in the lead up to that date.

Nowadays many people opt for income drawdown, where there isn't a clean cut-off date.

Drawdown offers investors flexibility and control, but the lack of a guarantee means investments have to carry on working for the rest of your life.

These challenges are compounded by the fact that retirees today have much longer life expectancies than their parents and grandparents did. A man aged 65 can now expect to live to 85.6 years and a woman to 87.8 years, according to the Office for National Statistics.

That means you might need your pension to last for more than 20 years.

'In simple terms, if you have a drawdown pension that you depend upon which suffers continuous poor growth after charges and inflation, you are unlikely to have a sustainable retirement, and your standard of living will eventually reduce,' says Oliver Smyth, financial adviser at Walker Crips Wealth Management.

'It is crucial to match your attitude to investment risk with realistic income objectives to ensure you have a coherent strategy for a sustainable retirement.'

HOW MUCH RISK IS TOO MUCH?

If you want to grow your investments, you need to take on risk. That means investing in the stock market.

But if you take on too much risk it could have a devastating impact on the value of your pension.

Once you start withdrawing money from your pension, the impact of a stock market downturn becomes far greater. As fund values drop, you need to sell down a higher proportion of your fund to generate the same income. This means you'll deplete your pension pot far more quickly.

'High levels of income withdrawal when capital values are suppressed can be particularly destructive,' says Charles Calkin, financial planner at James Hambro & Co.

'The right level of risk is a sensible balance between giving you income and potential for capital growth to protect against inflation and not putting your security in jeopardy.'

HOW DO I MEASURE RISK?

What constitutes too much risk is personal to each retiree.

This is because you need to assess your capacity for loss – i.e. how much your lifestyle would be affected if you were to suffer a significant loss from your pension.

Smyth says if a retiree requires 10% of their fund as an income each year, this is unlikely to be achieved via a cautious or medium risk portfolio.

However, if the retiree doesn't have a great deal of capacity for loss, then pursuing a higher risk strategy could be harmful in more negative market conditions.

'In this instance, it may be more beneficial to revise your lifestyle and spending to see if there is any way to decrease the burden on your drawdown income and create a more sustainable retirement plan,' Smyth adds.

Simon Molica, fund manager at AJ Bell, says many retirees are probably not taking on enough risk within their overall pot of wealth.

'The last decade has demonstrated the danger of having too much wealth tied up in bank saving accounts, which potentially can erode purchasing power, especially given today's low interest rate environment,' he says.

'It is important to ensure that the income generated from your investments is not slowly eroding the capital of your wealth in an unexpected manner.'

WHAT SHOULD I INVEST IN?

Matt Swatton, private client partner at Thomas Miller Investment, suggests that a typical 65 year-old seeking investment growth that isn't overly risky should aim for a 30% to 50% allocation to equities.

The remainder would be split between bonds, gilts, property, alternatives and cash.

Swatton reckons **Standard Life Investments MyFolio Market III (GB00B758J660)** is worth looking at. The fund aims to generate a total return from a combination of income and capital growth by solely investing in passive funds.

'The passive portfolio construction of the fund means that the overall cost of the underlying holdings are cheaper, which would suit a client with a smaller retirement pot,' says Swatton.

'As it's designed for a client with a balanced attitude to risk – who isn't necessarily seeking risky investments but isn't avoiding them either – it would seem to suit a retired investor with a longer-term time horizon.'

AJ Bell's Simon Molica favours **Fidelity MoneyBuilder Income (GB00B3Z9PT62)** and **TB Evenlode Income (GB00BD0B7D55)**, both of which focus on generating income.

Fidelity MoneyBuilder Income is a UK corporate bond fund which aims to produce a strong level of income, low volatility and equity diversification.

Evenlode Income is a UK equity fund which seeks to invest in quality companies with resilient profit streams, sustainable growth profiles and limited capital reinvestment needs or reliance upon leverage.

If you're not comfortable picking individual funds, a multi-asset fund is a simpler option. These 'one-stop-shop' funds spread your money across lots of different assets according to a specified risk profile. (EP)

A cut-out-and-keep guide to defined benefit pension transfers

Everything you need to know about cashing out of a DB pension or staying put

Since joining AJ Bell two years ago, I've had more questions from investors about defined benefit (DB) pension transfers than any other subject.

This spike in interest has undoubtedly been driven by the launch of the pension freedoms in April 2015, as well as a number of high profile company collapses (most notably retailer BHS and construction firm Carillion).

The numbers involved are striking. According to the Office for National Statistics, some £5.4bn of pension transfers took place in 2014. Fast forward to 2017 and this figure had risen to almost £35bn. The vast majority of this increase is likely due to savers leaving their DB schemes in the wake of the pension freedoms.

So what are the key things you need to consider when deciding whether to retain the security of DB or opt for the flexibility of a defined contribution (DC) pension such as a SIPP? And what hoops will you need to jump through if you decide you want to transfer?

TAKE YOUR TIME

Ditching a DB pension could be the biggest financial call you make.

Many make the mistake of rushing to a decision, particularly with commentators and newspaper articles suggesting transfer values – the cash lump sums companies offer in exchange for guaranteed pensions – are at record levels. In most cases, however, the wisest choice will be to stick with your DB scheme.

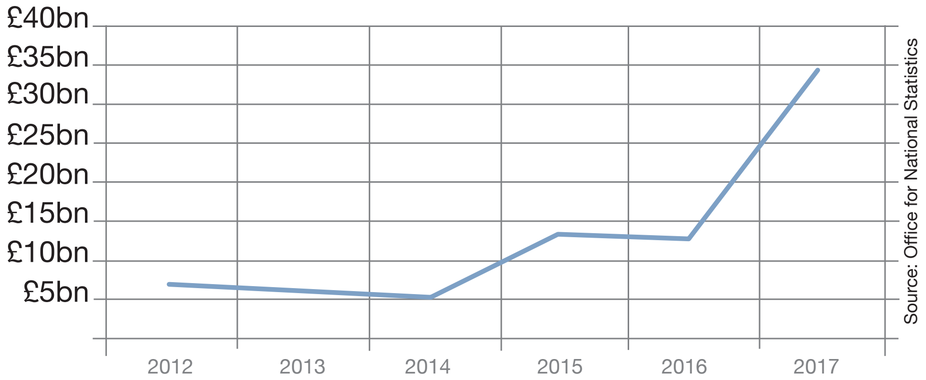
This transfer value will usually be a multiple of the annual income your pension guarantees. For example, someone in a DB scheme that will pay out an inflation-linked pension worth £10,000 a year from age 65 might be offered a cash lump sum of 20x this amount, or £200,000.

Clearly having such a huge cash carrot dangled in front of you is seriously tempting. But before snapping their hand off you need to think how you will fund your retirement lifestyle without that stream of income.

There are also a lot of complicated and uncertain factors you need to weigh up:

- How much investment risk are you willing to take if you choose to swap DB for drawdown?
- When will you need to start accessing the money?
- How much will you take out?
- Are you happy that the drawdown income won't have the same inflation protection offered by your DB scheme?
- For how long will you need your pension to last?

Value of DB pension transfers since 2012



I'M WORRIED MY EMPLOYER IS GOING TO FAIL

In light of a series of high profile company failures, you might be concerned about the ability of your current or former employer to survive long enough to pay your pension.

If this is the factor driving your thinking, remember the Pension Protection Fund (PPF) provides a valuable backstop in the event the scheme sponsor goes bust.

The level of compensation you get from the PPF depends on your circumstances. If you have already retired and reached your scheme's 'normal pension age' you should get 100% compensation, although you may lose some inflation protection.

If you have yet to retire or you took your pension early then your annual payment will usually be cut by 10%, though is also subject to a cap. For a 65-year old this is set at just over £39,000 a year. You may also lose some inflation protection.

So while falling into the PPF is far from ideal, the scheme provides a valuable insurance policy for DB members which must be taken into account.

You can find more information on the PPF and the compensation it provides at www.pensionprotectionfund.org.uk

LISTEN TO YOUR FINANCIAL ADVISER

Rules introduced alongside the pension freedoms mean that anyone who wants to transfer a DB pension worth £30,000 or more is required to take regulated financial advice first.

> **A number of investors I've spoken with complain they have struggled to find an adviser willing to take on their transfer case**

This can vary in cost – Unbiased, an adviser directory, reckons for a £100,000 pension this would usually come to about £1,500.

If you're desperate to get your hands on the cash, you might be tempted to treat this as a rubber-stamping exercise. This would be a mistake – you're paying for an expert to talk you through the options and the potential long-term implications of your decision, so you should get your money's worth by listening to what they say and asking as many questions as you can.

A number of investors I've spoken with complain they have struggled to find an adviser willing to take on their transfer case. This is a common issue – some advisers simply don't have the necessary qualifications to carry out pension transfers, while others are steering clear because they are worried clients will complain in the future if things go wrong.

Unfortunately there is no easy fix to this problem, and you may need to contact several advisers before finding one to take on your case. They may also advise against the transfer – in these circumstances (known in the jargon as 'insistent client transfers') some pension providers will refuse to accept your money.

If you're looking for an adviser www.unbiased.co.uk is a good place to start. You can also find more useful information through the Government's Pension Wise guidance service at www.pensionwise.gov.uk

Tom Selby, senior analyst, AJ Bell

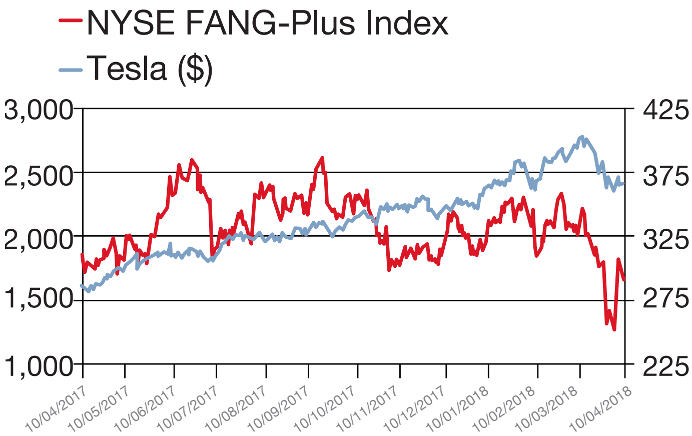
How the SOX index can help investors work out whether stock markets are going to rock or roll

Why tracking the performance of chipmakers can offer valuable insights

A slide in the share prices of Facebook, Apple, Amazon, Netflix and Google's parent Alphabet, the so-called FAANGs, and Tesla is grabbing all of the headlines.

Whether this is down to a collection of company specific reasons – such as questions over Facebook's involvement in the Cambridge Analytica data use scandal, attacks on Amazon by President Trump (which could just be payback for Amazon boss Jeff Bezos' ownership of the *Washington Post* newspaper) or Tesla's inability to meets its production targets or get even close to making a profit – or a wider move away from highly-valued, momentum-driven, risky securities remains to be seen.

WEAKNESS IN THE FAANG STOCKS AND TESLA MAY BE HERALDING A WIDER SHIFT IN MARKET SENTIMENT



Source: Thomson Reuters Datastream

Such stock-specific niceties may not trouble all investors. But if they really want to get a real grip on technology stocks and stock markets more generally then they should be keeping an eye on the Philadelphia Semiconductor Index, more commonly known as the SOX index.

The benchmark contains 30 companies who are involved in the design, manufacture and sale of silicon chips and it is therefore a very useful guide for investors on two counts.

These integrated circuits are everywhere, from smart phones to computers to cars to robots, so they offer a great insight into end demand across a huge range of industries and therefore the global economy.

Chip-makers' and chip-equipment makers' shares are generally seen as momentum plays, where earnings growth is highly prized and valuation less of a consideration. As such they can be a good guide to broader market appetite for risk.

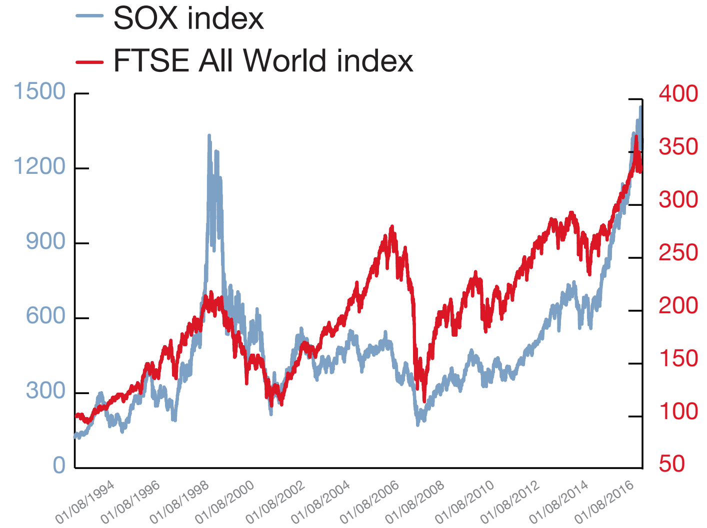
Since its launch in summer 1994 the SOX has been a good guide to America's S&P 500 index but also the FTSE All-World benchmark. Peaks in the chip index in both 2000 and 2007 warned of trouble ahead on a much broader scale.

THE 30 CONSTITUENTS OF THE SOX INDEX

No.	Stock	Country	SOX index weighting
1	Intel	USA	8.6%
2	Broadcom	USA	8.1%
3	Texas Instruments	USA	7.9%
4	NVIDIA	USA	7.6%
5	Qualcomm	USA	7.0%
6	LAM Research	USA	4.3%
7	TSMC	Taiwan	4.2%
8	Micron	USA	4.2%
9	Analog Devices	USA	4.2%
10	Microchip	USA	4.1%
11	Applied Materials	USA	3.9%
12	Skyworks	USA	3.7%
13	Xilinx	USA	3.6%
14	KLA-Tencor	USA	3.4%
15	Maxim Integrated	USA	3.3%
16	ASML	Netherlands	3.1%
17	Marvell	USA	2.1%
18	ON Semiconductor	USA	2.1%
19	Advanced Micro Devices	USA	1.9%
20	Quorvo	USA	1.8%
21	Teradyne	USA	1.7%
22	Microsemi	USA	1.6%
23	MKS Instruments	USA	1.3%
24	Cypress Semiconductor	USA	1.2%
25	Entegris	USA	1.0%
26	Monolothic Power	USA	1.0%
27	Integrated Device	USA	0.8%
28	Silicon Labs	USA	0.8%
29	Mellanox	Israel	0.8%
30	Cirrus Logic	USA	0.5%

Source: NASDAQ OMX, iShares

THE PHILADELPHIA SEMICONDUCTOR INDEX – THE SOX – COULD PROVIDE FURTHER USEFUL INSIGHT INTO MARKETS MORE BROADLY



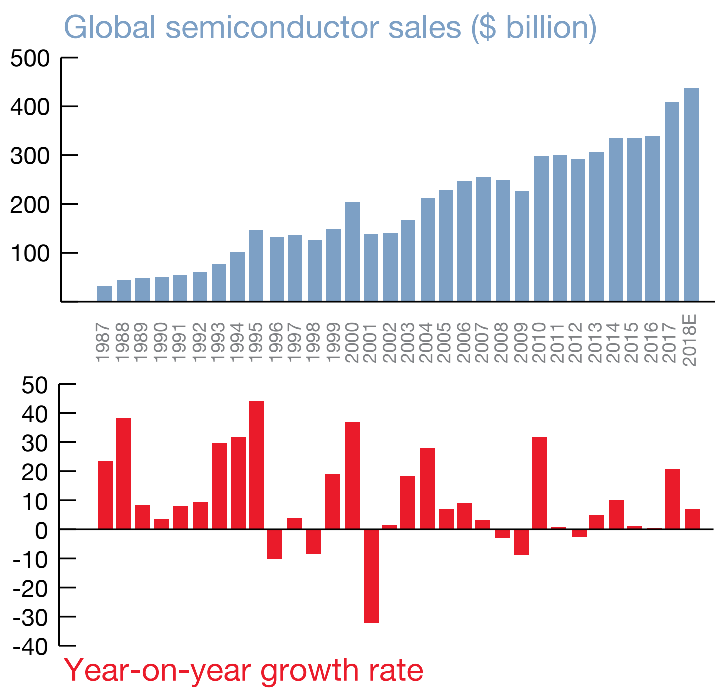
Source: Thomson Reuters Datastream

PULL UP THE SOX

The SOX could be every bit as useful a guide during this equity bull market, which began in 2009.

The good news, for the moment, is that the semiconductor industry grew like a rocket in 2017, as global sales surged by 21% to a new all-time high of $409 billion. Better still, revenues are expected to rise by at least 7% in 2018.

GLOBAL SEMICONDUCTOR SALES ARE BOOMING



Source: Statista

This may help to explain why technology overall has been a huge driver of equity market returns for investors.

The net result is that 10 of the world's 25 biggest companies by market capitalisation now hail from the tech sector.

This list includes three silicon chip makers – Intel (the world leader in microprocessors), Samsung Electronics (the world leader in memory chips) and Taiwan Semiconductor Manufacturing Company (the world's biggest foundry, or chip maker on an outsourced basis).

IMMINENT NEWS FLOW

The good news is that Samsung Electronics has got the first-quarter reporting season off to a good start by estimating that profit for the January-to-March period will rise by 58% year-on-year.

However, that did not prevent a dip in the shares, which are still trading a fraction below March's all-time high of Won 2.88 million.

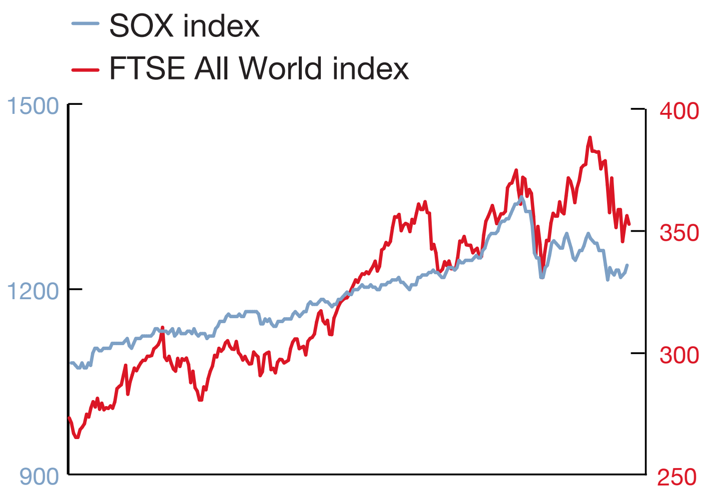
Investors will therefore be looking to the first-quarter reporting season from Intel, TSMC and other leading SOX index members such as Broadcom, Texas Instruments, NVIDIA and Qualcomm for reassurance on both end-demand and also share price momentum, especially as the silicon chip benchmark is no higher than it was in November.

THE WORLD'S 25 BIGGEST COMPANIES BY MARKET CAPITALISATION

No.	Name	Sector	Country	Market Cap ($ billion)
1	Apple	Technology	USA	844.7
2	Alphabet	Technology	USA	698.7
3	Amazon.com	Technology	USA	693.0
4	Microsoft	Technology	USA	688.3
5	Tencent	Technology	China	500.6
6	Berkshire Hathaway	Financial services	USA	485.3
7	Alibaba	Technology	China	458.2
8	Facebook	Technology	USA	444.6
9	JPMorgan Chase	Financial services	USA	368.3
10	Johnson & Johnson	Consumer staples	USA	341.9
11	Industrial & Commercial Bank	Financial services	China	328.3
12	Exxon Mobil	Energy	USA	308.5
13	Bank of America	Financial services	USA	300.5
14	Samsung Electronics	Technology	Korea	297.2
15	Royal Dutch Shell	Energy	UK/ Netherlands	265.4
16	China Construction Bank	Financial services	China	260.5
17	Walmart	Consumer discretionary	USA	260.0
18	Wells Fargo	Financial services	USA	251.0
19	Nestle	Consumer staples	Switzerland	246.6
20	Visa	Financial services	USA	241.1
21	Intel	Technology	USA	231.5
22	Anheuser-Busch InBev	Consumer staples	Belgium/ Brazil	221.8
23	AT&T	Telecoms	USA	218.4
24	TSMC	Technology	Taiwan	217.6
25	Chevron	Energy	Energy	214.1

Source: Bloomberg

THE SOX INDEX IS LOOKING TO RECAPTURE ITS RECENT ALL-TIME HIGHS



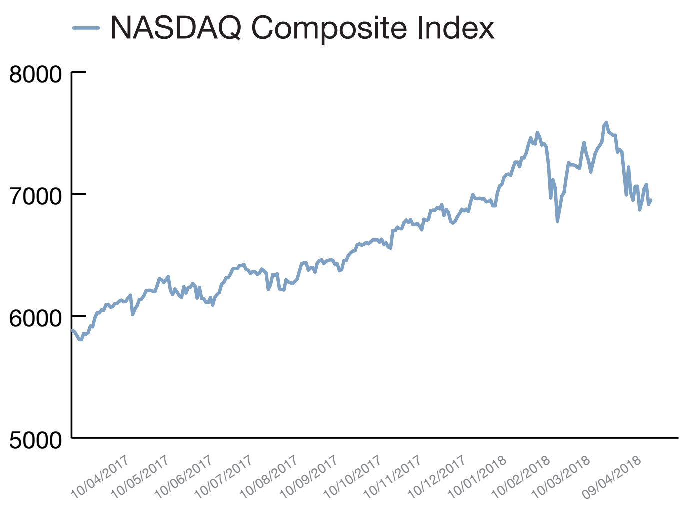
Source: Thomson Reuters Datastream

After all, some cracks have already appeared in the technology edifice.

Despite the apparent success of the Dropbox and Spotify initial public offerings (IPOs), at least if they are measured by immediate share price performance in the wake of their listings, investors have begun to ask more questions of technology stocks and richly-valued but ultimately loss-making companies.

We have already seen the sharp drop in the FAANG stocks and the recently-created index that tracks them, as well as the retreat in wider, technology-laden NASDAQ index.

THE NASDAQ COMPOSITE INDEX IS ALSO LOOKING TO RETURN TO A RECENT RECORD PEAK



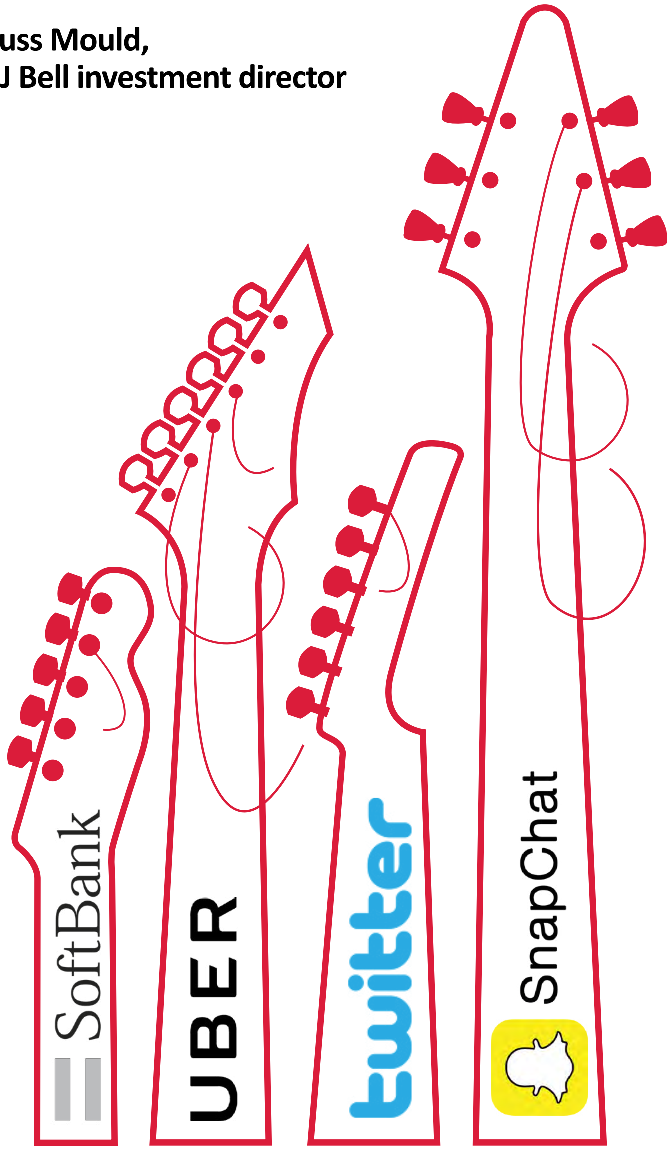
Source: Thomson Reuters Datastream

• Softbank may have shown faith in transport technology platform (or taxi service, depending on your viewpoint) Uber, despite its governance and regulatory problems, but the Japanese technology investment behemoth injected capital at a price which implied a one-third cut in Uber's valuation to $48 billion. This is known as a "down round" in the world of venture capital and is not normally seen as good news.

• Twitter and Snap have both struggled to hold on to the share price gains they made in the wake of their respective stock market flotations in 2013 and 2017 respectively.

None of these have to signal that the tech is about to fall out of favour and take risk assets more generally with it. But tracking the SOX index and silicon chip stocks in particular may help investors in forming their view on this sector and, as a result, their asset allocations more broadly.

Russ Mould,
AJ Bell investment director



ASOS's increased spending plans are not a reason to dump the shares

Plans to boost spending on warehouses, automation and technology haven't gone down well

Online fashion retailer **ASOS (ASC:AIM)** says its spending needs to rise materially on logistics and distribution to support its rapid and globally-derived growth.

While that hasn't gone down well with investors, we do see positives longer-term in having more robust infrastructure to cope with expected demand.

The online business is unencumbered by the same level of overheads as a bricks-and-mortar shopkeeper, yet still has to spend big to support its stellar growth.

This is providing some fodder for investors who dislike the stock and argue the toppy valuation is hard to justify; even after a reverse to £61.22 per share, the AIM giant still swaps hands for over 60 times this year's forecast earnings.

In contrast, fans of the company argue ASOS represents a compelling play on the clothing market's channel shift to the internet and as chief executive Nick Beighton reminds investors, 'ASOS's market shares remain relatively modest around the world, offering significant opportunities for continuing growth in the years to come.'

Half year results to 28 February revealed a 26% surge in retail sales to over £1.13bn amid strong UK and overseas growth, and a 10% hike in pre-tax profit to £29.9m.

Encouragingly, the £5.27bn cap's retail gross margin rose by 100 basis points to 48% and ASOS received more than a billion site visits during the first half for the first time, although growth did slow in the US and Rest of World regions.

Full year and medium term sales and earnings guidance were unchanged, but ASOS cautioned that total capital expenditure will increase to between £230m-to-£250m in the financial year to August, up from the previously guided £220m.

This level of infrastructure and technology-related spending is set to continue for the next two financial years.

Ambitious ASOS is laying the foundations for £4bn of sales over the medium term, although the upgraded spending guidance means the retailer expects to be free cash flow negative this year and next, returning to free cash flow positive in the year to August 2020.

Stockbroker Numis Securities forecasts 26% rise in pre-tax profit for 2018 to £100.6m, ahead of a 20% rise to £120.6m next year.

Based on this year's forecast 26% growth in earnings per share to 97.9p, rising to 117p next year, ASOS's growth potential is reflected in a forward multiple of 63.3 times and a punchy PEG ratio of roughly 2.4 times.

SHARES SAYS: ↗

A pull back from £77.30 in mid-March to £61.22 probably won't be a big enough fall to interest investors nervous about 'priced for perfection' stocks as the equity valuation is still very rich.

However, those with a long-term view may be encouraged by the scope of ASOS's global growth ambitions and the fact that it remains a highly profitable business despite tough retail sector conditions. We reiterate our 'buy' rating on ASOS. (JC)

BROKER SAYS: 13 7 5

Boku set for 2018 profit breakthrough as apps store payments soar

Recent stock market arrival could beat quoted rival Bango in the quest for positive earnings

App store and digital content company **Boku (BOKU:AIM)** may soon be a profitable business. Stockbroker Peel Hunt forecasts $0.7m of pre-tax profit (approximately £0.49m, the company reports in dollars) for the year to 31 December 2018. That could soar to $8.5m in 2019 if the broker has got its assumptions right.

Analysts believe the company's value proposition and supplier relationships with key digital content partners could spark a re-rating of the share price to 105p or more. Boku, currently trading at 86.5p, joined the AIM market at 59p in November 2017.

APP STORES AND MOBILE CARRIERS

Boku was established in the US in 2008 to provide smartphone payments for apps, movies, music and other online content. It operates a direct carrier billing (DCB) platform that allows consumers to charge online purchases to their mobile phone bill.

It has key relationships with content providers such as Google, Apple, Facebook, Xbox and Netflix. Mobile networks operators such as **Vodafone (VOD)**, O2, Softbank and T Mobile are also clients.

Digital content spending continues to soar around the globe as consumers increasing shop online using their smartphones. They also want payments to be made as simple as possible.

Boku makes its money by taking a slim cut of the overall value of each transaction, or what the company calls total processed volume (TPV). For example, if you paid £5.99 for a movie on the Google app, £5.99 would count towards TPV. Boku makes about 1.4% on TPV which is booked as its own revenue.

RAPID DIGITAL SPENDING GROWTH

This TPV margin has been under pressure with app store operators and content generators wanting

more of the profit pie themselves. For example, **Bango (BGO:AIM)**, which also runs a DCB digital payments platform, has seen 4% to 5% margin hopes erode dramatically in recent years, currently running at around the 1.4% ballpark that Boku earns.

Analysts predict further erosion of TPV margins in the coming few years where they are likely to bottom out at something in the region of 0.8%. However, such is the rapid growth in Boku's TPV income its profits are still predicted to growth fast.

Peek Hunt estimates Boku's $1.24bn TPV in 2017 will soar to beyond $5bn by 2020, fuelling pre-tax profit of $8.5m in 2019 and $15.5m in 2020.

SHARES SAYS:

It's always interesting to see a company forecast to move into profit, however we have reservations about low margin small cap companies such as Boku. We prefer to watch from the sidelines until it is a stronger position financially and has gained greater scale before taking a view on whether the shares are worth buying or not. (SF)

Liontrust roars into 2019 looking like a new beast

Despite a market sell-off in February, this asset manager looks well positioned

Continuing a strong trend for small cap asset managers, **Liontrust Asset Management (LIO)** is yet another pint-sized fund house that has been performing well.

For investors who are familiar with this space, the company is larger than **Miton (MGR:AIM)** but smaller than **Polar Capital (POLR:AIM)**, for example.

The company enjoyed a substantial increase in assets under management (AUM) as it acquired Alliance Trust Investments in April last year.

In the 12 months to 31 March 2018 Liontrust's AUM was up 61% to £10.5bn, also enjoying inflows into its funds during its financial year of more than £1bn. This was more than double the £482m it managed in the 2017 financial year.

Its closing AUM would have been higher if not for the recent market volatility which wiped £336m off this figure.

Chief executive John Ions described the previous year as 'transformational' and for a relatively small asset manager with a market cap of £277m, it had the eleventh highest retail fund sales in the UK.

This position in the list is all the more notable when you consider it includes products offered by the global titans of investing such as the world's largest asset manager BlackRock.

A HIGHLY DIVERSE OFFERING

Liontrust has a wide variety of funds, growing with the Alliance Trust Investments acquisition which added new products under the Liontrust banner.

Its fund range includes regional income plays such as **Liontrust Asia Income Fund (GB00B7BZB324)** as well as more esoteric investments such as **Liontrust Special Situation Fund (GB00B57H4F11)**.

Unlike some other smaller asset managers, Liontrust has invested in a bond fund offering with the recruitment of David Roberts, Phil Milburn and Donald Phillips. While bond fund sales performed relatively well last year, the increase in inflation and the first UK rate hike might undermine the attractions and performance of the asset class going forward.

Broker Numis is not overly optimistic on this area of the business, saying 'we assume only a minimal contribution from the recently hired global fixed income team'.

Liontrust also acquired a sustainable investment team at the start of the past financial year, whose AUM increased in the 12 months by £500m to nearly £3bn.

The diversity of its offering, with funds ranging from mainstream to highly specialised, increases the scope of its appeal to investors.

At 564p the shares trade on 13.4 times Numis' forecast March 2019 earnings and pay a prospective yield of 4%. The market will get a further opportunity to appraise the company's performance on 27 June when it reports its March 2018 results in full. (DS)

KEY

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