AJBell Investcentre

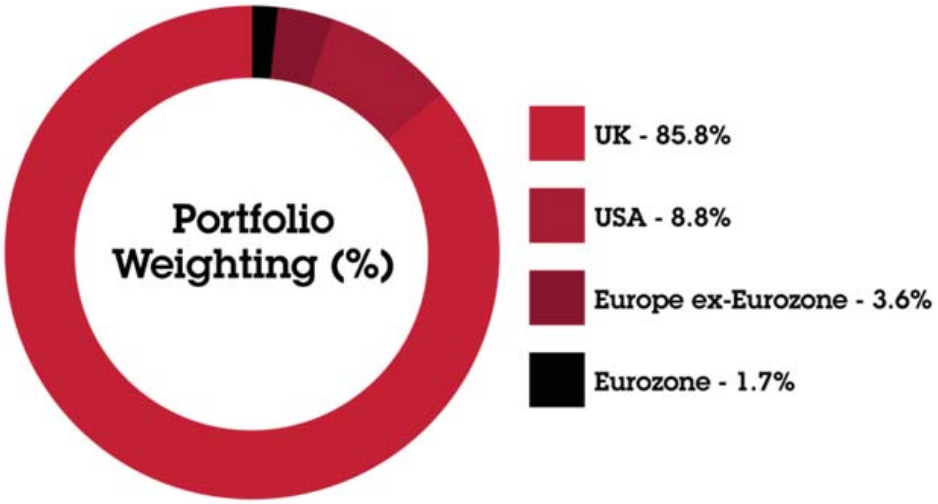
Fundamentals with Russ Mould

November 2016

Hello, I'm Russ Mould, AJ Bell's Investment Director, and welcome to Fundamentals, where I'm going to look at one of the most popular funds on the AJ Bell Investcentre platform right now, namely Invesco Perpetual High Income.

[CAPTION: Invesco Perpetual High Income Y (Acc) SEDOL – BJ04HP8ISIN – GB00BJ04HP86]

The £11.3 billion collective's mandate is to provide income and it seeks to do so by investing primarily in firms listed in the UK, although at the moment 9% of the assets are in the USA and 5% in Europe, as we can see here:



Source: Invesco Perpetual factsheet, Morningstar

Some may question the 'high income' tag when the yield on the fund is currently 3.2% (which, by the way comes in semi-annual payments, although note that with this accumulation class of fund the cash will be reinvested).

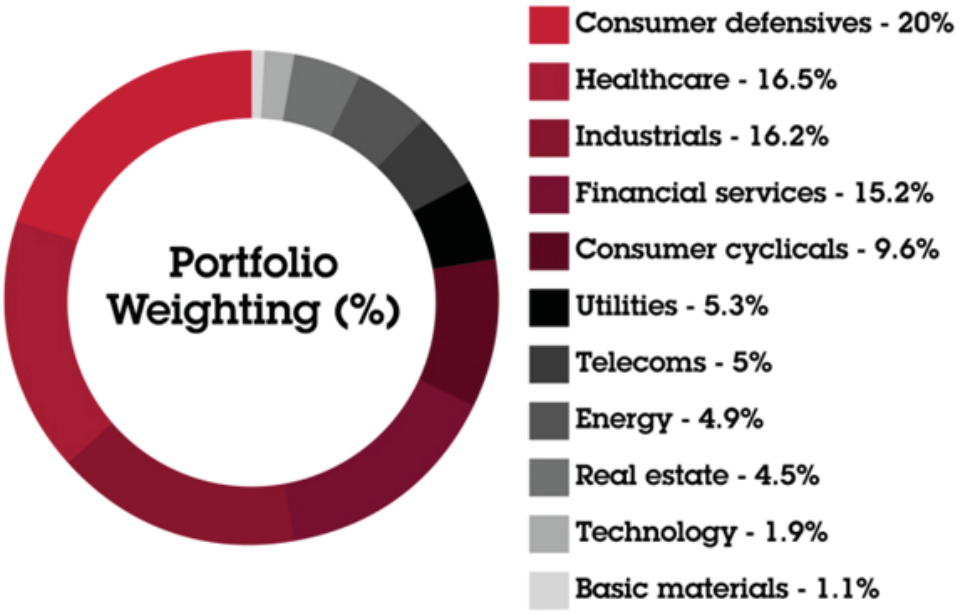
This reflects the views of manager Mark Barnett, who is as well-known as he is respected. I've recently heard him speak at both an Invesco Perpetual event in London and also at our very own Investival and his views are pretty clear.

- He is not convinced that dividends can keep growing faster than earnings, as they have in the past few years and expects a slowdown can continue so cover can be rebuilt.
- He is not convinced by the reflation trade which has become popular following the election of President Trump. Barnett argues that key deflationary trends like debt and demographics have not gone away and that price pressure is unlikely to desist either, even if the headline inflation numbers pick up – so firms with pricing power are still what he is seeking.
- He does flag how the UK market has become very split, with dollar-and overseas earners in vogue and domestically-focussed stocks out in the cold. He thinks this is throwing up valuation opportunities among the domestic names, where he is starting to dip his toe in once more.

As a result of that, tobacco stocks still remain a key part of the portfolio – Reynolds American, British American Tobacco and Imperial Brands are all in his top six holdings (and interestingly he thinks BAT may have to pay a little if it is to acquire its US target, Reynolds).

He remains wary of banks' long-term earnings power, even if he concedes valuations look lowly and prefers insurers, while Barnett also feels the big oil firm dividends are safe and here he has a preference for BP over Shell. BP is the third biggest position, behind Reynolds and BAT.

All of this means that consumer staples and healthcare are still the biggest sector weightings within Invesco Perpetual High Income, while basic materials and the miners do not get much of a look-in.



Source: Invesco Perpetual factsheet, Morningstar

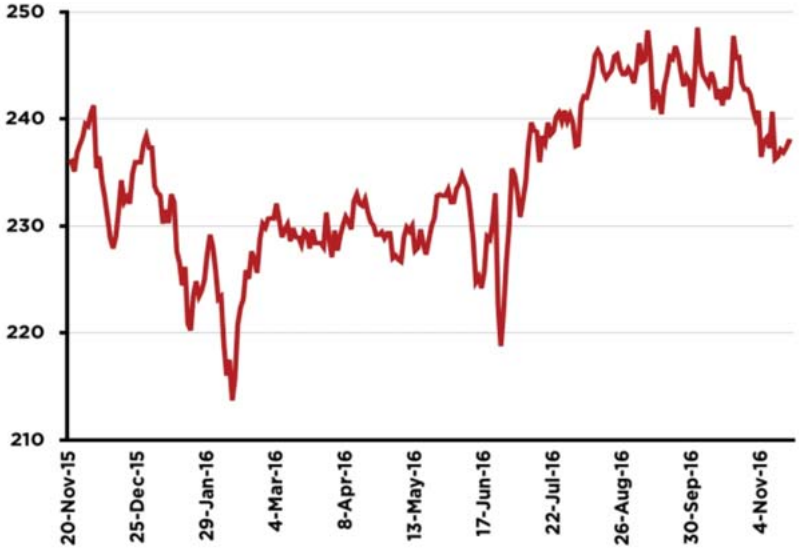
As a couple of final points, the fund is eligible for SIPPs and ISAs and it comes with an annual ongoing charge figure of 0.87%.

So those are the mechanics. So the question is why would advisers and clients potentially be buying now?

Well, the world view outlined by Mark Barnett himself, as briefly outlined above, will explain some of the continued interest in this high-profile fund.

- First, there is no guarantee that Trumpflation will prevail, so the dash from defensives to cyclicals and yield-generators to turnaround plays will continue
- Second, there is no guarantee that interest rates will shoot higher even if inflation does pick up and that will still place a premium on dependable income. In addition, Government bond yields are still below where they were 12 months ago, as benchmarked by the UK 10-year gilt and a 1.44% yield here may not do the job for everyone
- Third, earnings cover for dividends in the UK equity market remains skinny. Although we have had fewer cuts this year – only Sainsbury's and easyJet within the FTSE 100 have pared back their shareholder payments of late – a skilled and experienced fund manager should be able to add value for income-seeking advisers and clients, by picking out dependable payers and dodging dividend cutters.

There are risks. Patience will be required and income could fall temporarily out of fashion if the reflation trade truly takes hold, leaving consumer staples and quality defensives out in the cold. In addition, every fund and fund manager can have their blips and Invesco Perpetual High Income has lagged its peers in the UK Equity Income category in the last 12 months.



Source: Thomson Reuters Datastream

As with any fund, advisers and clients must ensure they think the collective represents value for money and that it also fits with their overall strategy, target returns, time horizon and tolerance for risk.

Thank you for watching and I look forward to seeing you next time.

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