Focus on . . .

ARCHIVE COPY
For Information Only

High Yielding Shares and Britannia's National High Income Trust.

Recent History of High Yielding Shares

In May 1979, which was about the time that high yielding shares started to weaken after 5 years of above average performance, there were 87 shares on the London Stock Market that yielded over 9% (all sizeable companies capitalised at over £10 m).

Of these 87 stocks, 11 have subsequently been taken over, but that is the end of the good news. Of the balance, no less than 41 have subsequently cut or passed their dividends and another 3 have gone into liquidation. So from that core list of high yielding shares, exactly one half have reduced their dividends over the past 2½ years including major companies such as Courtaulds, GKN, Turner & Newall and Tube Investments.

As for their share prices, approximately one third of these stocks have more than halved since 1979 and a mere one in five has risen in line with the market.

This piece of history mainly serves to emphasise the recovery potential that exists within the sector and which has started to be reflected in some of the price increases that have taken place in the recent market rise.

Current High Yield List

Despite the massive round of dividend cuts, the current high yield list still contains 80 shares yielding over 9% (and the market is now some 20% higher than in 1979). Breweries, insurance companies, banks and stores all now feature although it is the manufacturers (notably engineering) that still predominate.

The reason for this high number of depressed stocks is collapsed profits and share prices so battered that in some cases companies remain high yielding even **after** cutting their dividends, e.g. Delta, Glynwed, Turner & Newall, Metal Box and Tootal.

Recovery Potential within the Sector

The significant point is that today's high yielding equity is typically the type of U.K. company that has been forced during the recession to do most to make itself more efficient through the instigation of cost cutting programmes involving mass redundancies and plant closures. Tangible evidence is beginning to accumulate showing that this costly phase is both now ending and working to advantage — witness recent figures from Courtaulds, Allied-Lyons, A.E., Tootal and Tate & Lyle, which show little volume upturn but substantial profit recovery. In national terms the productivity point is made vividly by the latest Government figures showing U.K. unit labour costs rising at an annual rate of only 3.9% in the third quarter of 1981 — less than in Japan and West Germany. Improvements such as these are being concentrated in the manufacturing sector and it is not difficult to visualise, given an actual pick up in demand, profits from these revamped concerns leaping dramatically and by a sufficient amount to make many of their current share prices look cheap.

The other key point is that high yielding shares tend to under-perform in times of recession and high interest rates and vice versa. The past 2½ years have provided perhaps the worst ever conditions in this respect — deep recession and record high interest rates. The likelihood now is that we are moving towards the more favourable conditions of falling interest rates and economic recovery. **It is the trend that counts.**

Cautious Dividend Outlook

We do not expect dividends to increase much in 1982 because managements will be anxious to restore finances as a first priority. Indeed, although the pace has slowed, dividend cuts are still being made. It may, therefore, be even harder to maintain our Trusts' distributions in 1982 than it was in 1981 although we look forward to a resumption of income growth in 1983.

Type of Investment Held

The Britannia income trusts — particularly **National High Income** — are heavily weighted in the type of company that has made itself leaner and more efficent; companies such as Imperial Group, ICI, Courtaulds, Allied-Lyons, Glynwed, Reed International and Tootal, to mention some of the larger holdings. Barring only a renewed economic downturn the fortunes of this type of company, already on the mend, are destined to improve from now on and in some cases sharply.

The 12 largest holdings in National High's portfolio account for 50% of the fund. They typify the company that we actively seek to invest in, namely the concern that has been going through a difficult patch, has fallen from favour as a result but on the other hand has been doing something positive about its problems and most important of all is reaping beneficial results from its efforts. Due to the recession there is currently a larger than usual number of recovery prospects of this type to choose from. We concentrate upon larger companies not just because of their better marketability but because invariably it is the long established company that can generate the ability to overcome its problems and instigate a revival in its fortunes.

Our ideal company should also be in a reasonably healthy financial condition and be rich in assets and brand names (in fact the average asset backing for all our holdings works out at twice the share price). This strengthens the takeover propect which is always very present in the case of a lowly rated company, with some of those who prove slow in turning themselves round being among the first to catch the eye of a predator — a good each way bet!

Bryan Quinton