Gibraltar Asset Management Stock Market Commentary

# 'Global stock markets record several weeks of unbroken gains'

GIBRALTAR ASSET MANAGEMENT LIMITED
STOCKBROKERS & INVESTMENT MANAGERS

| MPC Bank Rate | Coupon | Annual Dividend (p) | Yield at 540p |
|---|---|---|---|
| 0.75% (current) | 1.75% | 17.5p | 3.24% |
| 1.00% | 2.00% | 20p | 3.70% |
| 1.50% | 2.50% | 25p | 4.63% |
| 2.00% | 3.00% | 30p | 5.56% |
| 3.00% | 4.00% | 40p | 7.41% |
| 4.00% | 5.00% | 50p | 9.26% |
| 5.00% | 6.00% | 60p | 11.11% |

The stock market has logged several weeks of unbroken gains, which is starting to make contrarians cautious. The gains, however, are broad-based with every sector positive year-to-date, showing none of the thinness associated with frothy tops. It has also been accompanied by upward moves across global equity markets and asset classes with emerging markets, oil, gold and copper all rising strongly. The danger in this rallying market is that the latest support is coming from talk; hot air can hold up balloons, but it can lift stocks for only so long. Nevertheless, the broad-based advance reflects positive realities - the Fed's move to an accommodative stance and hopes of a resolution to trade talks.

by **Mark Maloney**, Managing Director, Gibraltar Asset Management Limited

### Market Outlook

**Our allocation to the stock market remains at overweight**. We continue to favour equities in this environment. Economic data indicates that the economy is chugging along nicely. Bond yields have retreated, providing less competition for equities. Yield-oriented sectors have been the year-to-date laggards. Indeed, far from gravitating to sectors with a more stable earnings profile, investors have favoured growth-oriented sectors.

We continue to look for P/E multiple expansion, following last year's significant contraction.

This market also has some seasonal wind in its sails, with multiple positives on the calendar. For one thing, given the long-term bullish disposition of investors in response to ongoing economic growth, stocks tend to do better than average in years following a below-average year. For all years since 1980, the S&P 500 has averaged capital appreciation of 9.7%. But for years following a year that was flat or down by up to 10%, average capital appreciation has averaged 20.3%.

Additionally, good Januaries are associated with above-average years, and 2019 was the best January since 1987. For all years with up Januaries since 1980, full-year capital appreciation has averaged 15.2%.

Finally, the third year of the US Presidential cycle has averaged 16.1% capital appreciation, the best of the four years; and 2019 is year number three in the current term.

### Recommended Investment

**Investec plc Non-Cumulative Floating Rate Perpetual Preference Shares**

This month's recommendation may appear a mouthful but it is actually quite a simple and interesting investment.

Investec plc is one of South Africa's largest banks with a dual listing in Johannesburg and London. In addition to its conservative banking activities, the company is engaged in asset management, property and investment banking. The UK entity is rated BBB+ with a stable outlook by Fitch, which means that it is regarded as "investment grade".

Issued by the UK-listed entity, these shares are "preference" shares listed on the London Stock Exchange (Ticker INVR.L). Shareholders do not participate in the profits of the company, but receive a fixed dividend in perpetuity paid twice a year (in June and December). As their name suggests, shareholders have preferential rights over any dividends paid - an ordinary dividend will not be paid unless a preference dividend is also declared. The shares are non-cumulative, meaning the dividend will not be paid twice next year if one is not paid in the current year. However, for reputational reasons, we believe Investec will always pay the dividend if they are able to do so. During the last financial recession, for example, Investec maintained dividends on both the ordinary and preference shares throughout.

The floating rate dividend is calculated at 1% over the UK MPC bank rate (currently 0.75%). As the stock has a £10 nominal value, the dividend therefore amounts to 17.5p (£10 x 1.75%) to produce a yield of 3.4%. The floating rate nature of the issue offers protection against a rise in interest rates, whilst providing a decent current yield.

Although rises in interest rates might not be imminent, the table below shows how the yield will be affected by rising interest rates and, furthermore, demonstrates the geared effect on yields where floating rate shares are bought at a significant discount to par:

Therefore, if interest rates rise modestly to 3%, the yield on these preference shares will increase to 7.41%. With interest rates close to all-time lows, the future direction is likely to only be up. On that basis, we rate these preference shares a **strong buy**.

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# Behind the Lens...

**These are from the Monochrome Prints Competition on the theme: MADE OF METAL.**
**The judge was Jonathan Bull.**


Gerry Fagan - Letterbox - 29 points (1)