Premier Miton UK Multi Cap Income Fund

Key Facts

Fund launch date	14 October 2011
Fund type	OEIC
Fund managers	Gervais Williams Martin Turner
Fund size	£901.0m
No of holdings	116
IA Sector	UK Equity Income
Base Currency	GBP
Valuation point	12:00 midday
Accounting dates	Final - 31 May Interim - 30 Nov

Distributions

XD date	Pay date	Dividend
27 Nov 20	31 Jan 21	2.9231p
1 Sep 20	31 Oct 20	2.9012p
1 Jul 20	31 Jul 20	3.0226p
2 Mar 20	30 Apr 20	1.1090p
Historic yield		3.29%

The historic yield reflects distributions declared over the past twelve months as a percentage of the mid-market price, as at 01.02.21. It does not include any preliminary charge and investors may be subject to tax on their distributions.

Ratings and Awards

defaqto EXPERT RATED

FE fundinfo Crown Fund Rating

Past performance is not a guide to future returns.

Summary

- We believe the prospects for the Premier Miton UK Multi Cap Income Fund are very strong at present.
- Now the open-ended uncertainties of Brexit are past, the UK is well-placed for a period of performance catch up.
- The upside potential is even greater amongst various financial and commodity stocks.
- Any takeovers should be rejected at present, given the upside is so much greater than their takeover premiums.

Market Review

Global asset market returns were generally good during 2020, with earnings disappointments from the pandemic-induced recession more than offset by a rise in stock market valuations. The unprecedented scale of the monetary and fiscal stimulus over recent quarters has been the key driver of asset market trends.

Since the pandemic remained virulent during January, many investors entered 2021 anticipating further financial stimulus. Whilst asset valuations did rise further early in the month, the positive was offset by bond valuations falling back due to inflationary fears. The outcome was a month when stocks in the energy and materials sectors were some of the best performers, and the FTSE All-Share Index itself fell by -0.8%.

UK small-caps have tended to outperform larger stocks over recent quarters, in part because younger businesses have a better chance of sustaining growth during a recession. The FTSE Small Cap Index (excluding Investment Companies) rose 1.6% in January, and the FTSE AIM All-Share Index was up 0.4%.

Calendar year performance

	YTD	2020	2019	2018	2017	2016
Fund	1.0	8.1	13.1	-7.7	15.7	3.1
IA UK Equity Income	-0.7	-10.7	20.1	-10.5	11.3	8.8
FTSE All-Share Index	-0.8	-9.8	19.2	-9.5	13.1	16.8
FTSE AIM All-Share Index	0.4	21.8	13.2	-17.1	26.0	16.1
FTSE SmallCap (excluding Investment Companies) Index	1.6	1.7	17.7	-13.8	15.6	12.5

Source: FE Analytics. On 30 November 2020, this fund moved from a single pricing basis (mid) to a swing pricing basis, which is where the price can swing to either a bid or an offer basis depending on the investment and redemption activity in the fund. This means the investor selling or buying fund shares bears the associated [dis]investment costs and protects the continuing holders in the fund. Performance could be shown on a combination of bid, mid or offer prices, depending on the period of reporting. Performance is shown net of fees with income reinvested. The fund is classified in the IA Equity Income sector, which we believe is a meaningful comparator to help investors assess the performance of the fund. As the fund invests in UK companies, we believe the FTSE All-Share Index and FTSE AIM All-Share Index are also useful performance comparators.

For investment professionals only

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Performance

Generally, equity market returns have been so good for so long that it is easy to misjudge how much markets can change trend. In our view, the ongoing rise of the stock markets lulled many quoted companies into paying out overly generous dividends, pushing them up at a faster rate than their underlying earnings. When interest rates were so low, it didn't seem to matter if there was any temporary shortfall in annual cash generation because interest rates were so incredibly low.

Unfortunately, during 2020, the downside risks of overdistributing dividends turned out to be terrifying. The pandemic led to numerous mainstream plc's cancelling previously declared dividends. Thereafter, those that did resume dividends, then did so at a much lower level than previously.

The strategy of Premier Miton UK Multi Cap Income Fund has always focused on generating sustained and sure-footed dividend income for our investors, without reference to the weightings of the peer group or the FTSE All-Share Index. Specifically, through investing across a broader investment universe than most others, it is possible to pick out all sorts of stocks that have serious potential to generate superior dividend income. The holding in Kenmare Resources, that has built a new ilmenite mine is a good example. Seven per cent of global, white pigment, principally used in paint, is now supplied by the new mine. During January, Kenmare confirmed that Q4 volumes remained strong, which prompted its share price to go up by another 22%. Even so, commodity stocks like this remain very much overlooked by most other investors. Touchstone Energy, which is bringing a major onshore gas field into production in Trinidad is another example. With the firmer energy prices in January, Touchstone's share price also appreciated by 24%, and like Kenmare we believe that it will justify a much higher share price when the scale of its future cashflow comes on stream. Share prices don't just go up in a straight line of course. The share price of AO World peaked out during January, and it was the greatest detractor in the month. Even so, the share price of AO World should be seen in the context of a stock that has risen by 86% over the last six months.

In our view, it is the ability to pick stocks like these with the prospect of generating sizable and growing dividend income that is a key differentiator of the Premier Miton UK Multi Cap Income Fund. By extending the investment universe beyond the restrictions of the mainstream stocks, the portfolio has the potential to pick out plenty of stocks that are continuing to deliver good and growing dividend income. Specifically, with a broader number of potential investments, there is also room to prioritise stocks that have strong balance sheets, which can sometimes sustain dividends through temporary downturns. Clearly, with the scale of the dividend cuts, the portfolio did have some companies that cut their dividends in the first half of 2020. What is interesting, is that a number of these have subsequently fully reinstated them again because they aren't under pressure to divert cashflow into repaying past debt balances.

The bottom line for clients is that the dividend trajectory of the Premier Miton UK Multi Cap Income Fund has been improving over recent months, which is why we believe the fund has outperformed many others in its peer group recently. This pattern was evident again in January, when the fund was up 1.0%, a little ahead of most of the comparatives.

Portfolio Activity

With the rising stock market trend over the final quarter of the year, there were opportunities to take some profits in January and reallocate the capital into others standing on more overlooked valuations. The fund's holdings in the spread betting stocks have been a major contributor to return over recent quarters for example. Whilst these companies are continuing to report strong results, their share prices have now risen so substantially that in aggregate CMC Markets, IG Group and Plus500 were starting to represent a significant weighting of the overall portfolio. With the concentration of correlation risk, we have taken profits on all three holdings over the last couple of months. If anything, the dividend growth prospects of CMC Markets and Plus500 are better than those of IG Group, so in January the IG Group holding was sold completely.

Another holding that has been steadily reduced over recent months has been Manolete. Whilst the company's share price did perform strongly in previous years, its model of buying into legal cases of insolvent companies has been affected by the pandemic. We worried that with fewer court sittings, their profitability would be affected. As it happened, Manolete confirmed the more challenging trading conditions during January, and hence the last of the fund's holding was sold at that time.

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Before long, the lockdowns will come to an end, sparking a resurgence of consumer demand for goods and services. Unfortunately, few consumer stocks are in a position to generate significant cash surpluses or pay generous dividends. Therefore, the portfolio is more skewed to the mining, energy or financial sectors, which have plentiful recovery potential, but are better positioned to generate plentiful surplus cash, and pay good and growing dividends. Interestingly, the prospects for these stocks would improve were inflationary pressures to return. Indeed, with so many of these stocks standing on unusually low valuations, their share prices could appreciate even more vertiginously in that scenario.

Outlook

Over 2020, global stock market returns turned out to be very satisfactory, especially in the context of the global pandemic, that was still very much at large, even in January 2021. Although China and some of the Asian economies have recovered well from the economic setback, a large part of the global economy is still very much mired in recession. Overall, global earnings reduced sharply over 2020, but this was offset by the valuation of stock markets rising even faster, so that global share prices appreciated over the year in aggregate.

This outcome underlines the unprecedented scale of financial and fiscal stimulus injected by central banks and governments over 2020. Whilst this stimulus may have moderated the risk of corporate insolvency, and scaled back unemployment, there are risks associated with creating so much extra cash without matching it with a similar increase in productive assets:

1. The extra cash has boosted speculative behaviour by investors. In the US for example, various unicorn stocks have been driven to much, much higher valuations. Elsewhere, numerous private investors have banded together to drive up the share prices of hedge fund shorts, forcing them to buy back their positions because of the unlimited liability. Juicy returns like this tempt fund managers to chase highly-speculative holdings.

2. Normally during recessions, companies with overstretched balance sheets are obliged to scale back their operations and sell off assets to repay debt, in a process that ultimately reduces money supply. These actions are deflationary and explain why the giant stimulus after the Global Financial Crisis didn't lead to a bout of inflation. At present, with cash being so plentiful, even those with overstretched balance sheets aren't necessarily scaling back their operations. We believe there is a significant risk that inflationary pressures may become more pronounced over the coming quarters, driving up longer-dated bond yields, which would lead to a collapse of speculative share prices.

Changeable markets like this can catch out investors. We take comfort in the fact that the UK stock exchange has largely missed out on the general rise in international corporate valuations over recent years, because of the open-ended uncertainties of Brexit. As it happens, the UK mid and small-cap stocks tend to stand on even lower valuations, as any hint of a domestic bias was considered particularly unappealing during the period of Brexit. Furthermore, a large part of the UK exchange comprises financials, and mining & energy stocks which have greater recovery potential when the economic recovery arrives. The key point is that the UK stock market has few speculative stocks, and its returns are largely uncorrelated with those that have performed well over recent years.

Now that the nature of Brexit is largely defined, UK-quoted stocks are well positioned for a period of performance catch-up, relative to their international comparators. In particular, the recovery potential for many income-generating, UK-quoted, mid and small-caps are all the greater because so many are coming from such low valuations. The scale of the upside should be further assisted by the cyclical nature of the financial and commodity stocks during the economic recovery after the pandemic.

Furthermore, if inflationary pressures were to become more pronounced in future quarters, then the upside potential on various financials and commodities income stocks would be even greater. They have been so out of favour for so long that it is easy to underestimate the full scale of their upside recovery potential.

Our very upbeat assessment is verified by the remarkably low valuations of so many well-financed UK income stocks with the potential to deliver abnormally large cash surpluses. Even some of the best performers in the fund's portfolio are still standing on absurdly low price earnings ratios.

In short, we consider the prospects for the Premier Miton UK Multi Cap Income Fund to be very strong at present. If UK share prices don't recover well

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in the next few months, then we believe international corporates will take advantage of the situation via numerous agreed takeovers, even for FTSE 100 Index companies. At present, we are currently engaging with the boards of the portfolio holdings, highlighting why we believe they shouldn't feel under heavy pressure to agree a takeover just because they are a premium to their current share prices. The key point is that their share prices have so much greater recovery potential than any takeover premium.

Risks

The performance information presented in this commentary relates to the past. Past performance is not a reliable indicator of future returns.

The value of investments may fluctuate which will cause fund prices to fall as well as rise and investors may not get back the original amount invested.

This fund may experience high volatility due to the composition of the portfolio or the portfolio management techniques used.

Forecasts are not reliable indicators of future performance.

In certain market conditions companies may reduce or even suspend paying dividends until conditions improve. This will impact the level of income distributed by the Fund.

Fees will be deducted from capital which will increase the amount of income available for distribution; however this will erode capital and may constrain capital growth.

Investment in the securities of smaller and/or medium sized companies can involve greater risk than may be associated with investment in larger, more established companies. The market for securities in smaller companies may be less liquid than securities in larger companies. This can mean that the Investment Manager may not always be able to buy and sell securities in smaller and/or medium size companies.

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Important Information

For Investment Professionals only. No other persons should rely on any information contained in this document.

Source of performance data: FE as at 31.01.2021, On 30 November 2020, this fund moved from a single pricing basis (mid) to a swing pricing basis, which is where the price can swing to either a bid or an offer basis depending on the investment and redemption activity in the fund. This means the investor selling or buying fund shares bears the associated [dis]investment costs and protects the continuing holders in the fund. Performance could be shown on a combination of bid, mid or offer prices, depending on the period of reporting. Performance is shown net of fees with income reinvested. Source for all other data: Premier Miton Investors as at 31.01.2021.

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All data is sourced to Premier Miton unless otherwise stated. Persons who do not have professional experience in matters relating to investments should not rely on the content of this document.

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For your protection, calls may be monitored and recorded for training and quality assurance purposes.

A free, English language copy of the fund’s full prospectus, the Key Investor Information Document and Supplementary Information Document are available on the Premier Miton website, or you can request copies by calling us on 01483 306090.

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