



Alan Porter

Manager
Securities Trust of Scotland

Alan joined Martin Currie's Global Equities team in 2008. He has 20 years' investment experience, including time with Insight Investment and Hill Samuel Asset Management.

He is responsible for Martin Currie's global equity income strategy and was appointed manager of Securities Trust of Scotland on 1 August 2011.

CONTACT

Visit the trust's website at
www.securitiestrust.com

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LOOKING FOR INCOME?

Let us pick the global winners

Historically, UK-based investors who want income from their equity funds have focused on the UK market. British companies are well known and well understood, and their fortunes are easy to follow in the daily newspapers. People trust what they know. This has led to a perception that domestic companies are the best choice for income-minded investors.

But in today's globalised world, that perception is misplaced. The case for a wider investment horizon has never been stronger. Given the global reach of many of the world's best companies, country-based limits are arbitrary, and countries of listing often represent no more than a 'flag of convenience'. So, with global earnings streams and the increased importance of the major emerging markets, an international approach is becoming indispensable.

That's all the more true from an income perspective. Of the world's 100 highest-yielding companies, just 10 are listed in the UK. So a domestic fund cuts off 90% of the best high-income opportunities. Indeed, 13 other developed equity markets offer a higher dividend yield than the UK stockmarket. These include France, Germany, Switzerland, Spain, Portugal, the Netherlands and the Scandinavian countries, as well as Australia.

So, if you want income, you would do well to think globally. And you probably should be thinking about income even if capital growth is your primary aim. Despite what many investors believe, yield and growth are not mutually exclusive – far from it. Studies show that companies that pay more dividends exhibit strong subsequent 10-year earnings growth. In fact, over the past 15 years, the highest-yielding companies (as represented by the MSCI Global High-Yield index) have outperformed the rest of the market (as represented by MSCI World Index) on both a capital-return and total-return basis.

In an ongoing environment of very low interest rates (in developed markets at least), it is also worth noting that high-yielding stocks currently compare very favourably with other asset classes, particularly government bonds. And we should remember that any panic is essentially an overreaction – and every overreaction in the market throws up opportunities.

Those opportunities will be select rather than general. But they will be very real. Given a tentative and uncertain economic recovery in the developed world, businesses with high-quality franchises, strong balance sheets and effective management should command a premium. So investors should always consider the best stocks, not the broader stockmarkets. Identifying the 'winners' will be especially important in the years ahead.

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So, the best approach in these volatile times is probably to hunker down, screen out the day-to-day 'noise' and focus on the fundamentals of individual companies. Then, in cases where quality is evident, short-term weakness should present excellent buying opportunities. Over the longer term, we expect further outbreaks of panic to punctuate the next few years – at least until some lasting resolution is reached in Europe, the US addresses its fiscal deficit, and the global recovery finds a firmer footing. But we should remember that the fierce competition in an environment of constrained growth will entail high stakes for companies – with the winners taking all.

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