

7%

Current yield of the FTSE 100 on a prospective P/E ratio of under 10x

## Ian Williams on UK Income



### (IA) UK Equity Income: Over three years

	3yr % chg	Rank	Vol monthly	Fund size (£m)	Morningstar rating™
<b>Top 5</b>					
<b>LF Miton UK Multi Cap Inc</b>	-13.51	1	2.72	711.16	★★★★★
<b>BMO Responsible UK Income</b>	-13.84	2	2.79	278.08	★★★★★
<b>Unicorn UK Ethical Income</b>	-14.00	3	3.73	28.60	★★★★
<b>Man GLG UK Income Professional</b>	-15.68	4	3.54	800.14	★★★★★
<b>Trojan Income</b>	-16.54	5	2.70	2,642.67	★★★★★
<b>Bottom 5</b>					
<b>Janus Henderson UK Eq Inc&amp;Gr</b>	-33.57	74	3.30	161.68	★★
<b>ASI UK Income Unconstrained Eq</b>	-33.63	75	3.82	1,007.21	★★
<b>L&amp;G UK Equity Income</b>	-35.26	76	4.15	233.56	★★
<b>ASI UK High Income Equity P1</b>	-35.50	77	3.81	401.63	★
<b>UBS UK Equity Income</b>	-40.04	78	3.97	17.29	★★
<b>SECTOR AVERAGE</b>	<b>-24.82</b>		<b>3.39</b>	<b>465.50</b>	

Performances calculated bid to bid, net income re-invested, GBP to 16/03/20. Source: © 2020 Morningstar.

Back in early February I warned it was too soon to discount the potential impact of coronavirus on the global economy. As the Western world now scrambles to fight the pandemic with a barrage of economic and fiscal injections, the risks of a global recession have increased in the past month.

It is still unknown at the time of writing how big a public health problem this will become. What is almost certain, though, is that interest rates are now likely to stay at or near zero in the developed world for at least this year.

That has presented a once-in-a-decade investment opportunity where the reward/risk equation in favour of equities is so heavily skewed to the reward side as to make the risk of owning shares pretty low relative to bonds.

This is the scenario currently facing UK income investors given the yield differential between British gilts & blue-chip equities. To give a live example, an investor can sell a 10-year gilt on a gross redemption yield of 0.6% and buy shares in Rio Tinto on a 9% dividend yield. If you do not like this stock, a host of other blue chips also offer high and sustainable yields.

Such dividend yields are not only above historic norms but also more likely to rise over a 10-year period while the yield on a gilt is fixed. The FTSE 100 is currently yielding almost 7% and on a prospective P/E ratio of under 10x. Even adjusting for a grim year ahead that is discounting a lot of pain.

### Bull Points

UK equities are at bargain basement levels

Bond markets have peaked

### Bear Points

Investor caution may delay stockmarket rally

Prolonged recession may hurt equities further

Bond markets, which were nudging record highs before the virus began to spread, are now riding for a correction as the world's central banks flood the markets with new paper. Corporate bonds potentially face an even worse fate as liquidity dries up completely.

Put bluntly, gilt prices at current levels are not sustainable for any protracted period and could collapse over the average life of the bond.

Investors who are prepared to look past the current bear market in equities are likely to enjoy double-digit returns over a 12-to-18 month view once economic activity returns to normality. Focus on companies with strong balance sheets and sustainable cashflows to fund their dividends. We also favour cyclicals such as large-cap base and precious metal miners, housebuilders and utilities.

*Ian Williams is chairman and chief investment officer of Charteris Treasury Portfolio Managers*