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Artemis duo focus on banks for income

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By David Thorpe

The duo who run the £548m Artemis Monthly Distribution fund have revealed how they are finding income in the bond market in a world of low interest rates and rising inflation.

James Foster, who runs the bond portion of the £548m Artemis Monthly Distribution fund, said the current "rosy" economic environment appears to be positive for high yield bonds because it increases the chances of the companies being able to repay the money.

He cited the example of the bonds of Center Parcs, a holiday company.

Mr Foster said in 2012 the company was issuing bonds with an annual coupon of 11.62 per cent.

In 2017, when the original bonds had matured, new bonds were issued with a yield of 4.25 per cent.

Mr Foster said the fundamentals of the company have improved in recent years, but that bond yields have generally fallen, and not always in circumstances where the fundamentals of the company have improved.

He said the prudent course of action for investors seeking to have bond exposure is to focus on bonds with a short date to maturity as protection against interest rate risk.

Both the fund managers take the view that inflation will rise and global economic growth will remain robust from here.

Mr Foster said the bonds of banks and insurance companies are a "core" part of his portfolio as the benefit from the higher bond yields he believes will be the consequence of higher inflation.

Banks and insurance companies benefit from higher bond yields as they are required by regulators to hold a significant slug of their assets in liquid assets such as bond.

Mr Foster added he is "more confident" in the durability of European banks, making their bonds better value, while he is sticking with the UK banks despite the current political uncertainty.

The largest investment in the Artemis Monthly Distribution fund is a UK government bond with a date to maturity of 2019.

Jacob De Tusch Lec, who runs the equity portion of the fund that is focused on bank shares, said the yields on the bonds of financial companies are being driven "ever lower" and this implies greater value for the dividends banks pay.

He said: “The latest ‘stress tests’ by the Federal Reserve sought to establish the health of the US banking system.

"It might be debatable just how rigorous this stress testing was (the Fed doesn’t disclose the assumptions it makes or the details of its tests) but it is interesting that the 34 largest banks in the US, having rebuilt their balance sheets, are to be allowed to return capital to shareholders through increased dividends and/or share buybacks.

"So banks in the US appear on the cusp of turning into dividend-paying machines. There are clear and prudent reasons why one might not like to invest in them due to macroeconomic considerations.

"But from a ‘bottom-up’ point of view we expect to be spending more time looking at US banks from this point.”

Jonathan Davis, who runs Jonathan Davis Wealth Management in Hertford, said: “I see little value in high yield at these levels.

"In any case, to invest in these presumes corporates are sound. In that case, I’d prefer to be an owner of the equity. UK shares are strong, from early last year.

"I remain bullish UK and international shares, until the market tells me not to be.”