

## SHINING A LIGHT ON..... THREADNEEDLE UK EQUITY INCOME FUND

### **At a glance**

There are over 400 UK Equity Growth and Income Funds; providing investors with access to many different investment styles. So choosing the right fund depends upon understanding their methods and aims.

Performance is part of the equation but equally the management team is crucial. We have met a number of talented Fund Managers, from the likes of Standard Life Investments, Neptune, Schroders, Legal and General, and Liontrust (not all of these are in our portfolios).

One manager I have met several times is Richard Colwell who manages the Threadneedle UK Equity Income Fund. On the occasions I have met him I never get a deep sense that what he is offering is anything different to any of the other big UK equity income funds. I have also felt that there are more dynamic managers which offer more.

However, one thing we always do is challenge our thinking and in our latest meeting it dawned on us that perhaps our view of the fund (and manager) is wrong. The reason being that the fund is by its very nature cautiously managed. In the latest discussion Richard explained how the approach borders on being defensive with a focus on good quality stocks.

When I started digging around further it became apparent that where other large UK Income Funds have faltered this fund has continued to deliver strong outperformance. It is therefore worthy of consideration for investors either looking for income or for those looking to re-invest the income for growth.

In this review we will look to unpack the fund further enabling potential investors to consider whether this is a fund for them.

### **Who are the team behind the fund?**

The lead manager is Richard Colwell. Richard joined Threadneedle in 2010 as the fund manager for this fund. He also manages the UK Growth and Income Fund, UK overseas Earnings and Monthly Extra Income Funds.

Prior to Threadneedle he worked at Aviva, Credit Suisse and Schroders as well as the Bank of England.

He is supported by Leigh Harrison who joined Threadneedle in 2006 and is Head of Equities at Threadneedle.

### **Fund highlights?**

Threadneedle have recently suffered losses to their UK team with one of the senior managers leaving together with members of the team. Part of the update was to assure investors and potential investors that the changes would not impact on the funds they manage. Threadneedle are a large company and have always emphasised the importance of the team rather than individuals and

## LWM Consultants Ltd

---

certainly the feeling is that although the loss does create a vacuum the breadth and depth of the team has insulated them.

This fund in particular has not had suffered any impact from the departures.

Turning to the fund, Richard describe it as a plain vanilla fund i.e. 'it is what it is'. Richard focuses on the total return which he says is made up of capital growth and income.

This makes it very difficult to compare to other large income funds so we asked him about the types of stocks he holds to try and understand how he is different. Richard claims this is a pure stock pickers fund with an emphasis on areas where other people are not necessarily following.

So for example one of the unloved sectors is retail and in particular food. Taking this further one unloved stock is Morrison's and this has many problems but the management is starting to turn the business around. There are other retail food businesses but in his view this offers the best option. He believes the shares will re-rate but in the meantime the dividend pays them to wait.

There are also sectors which he avoids – for example he has zero weighting to banks. He covered Lloyds and said although they are paying a dividend and this should be seen as a positive there are issues around the loan book which he remains uncomfortable with. The only bank he might consider is HSBC and with rising interest rates this may benefit. Also he avoids miners especially those more reliant on China where he feels margins will be squeezed.

Other areas he likes are insurance companies like L&G and Aviva which have focused on improving cash flow and businesses focusing on closed books (for example Phoenix). We also touched on AstraZeneca which is a large holding and is being held because he feels the market is under estimating its cash flows.

The style is about focusing on solid large cap companies and the fund typically holds between 45 and 60 holdings, currently it has around 55. It has a low turnover so Richard is happy to wait for return to come through. Richard says there is conviction in his style and some holdings do have over 3% holding.

There are recovery stories he points to Morrison's as an example.

My concern would be over the size of the fund but he has continued to consistently outperform and therefore this doesn't seem to be dragging down performance.

In summary this fund is not exciting and as the manager says it should be seen as a cautious / defensive fund. The performance is strong and it may well blend into a portfolio of holdings especially as the market is fairly volatile at the moment. The use of recovery stocks provides the additional potential upside but this balanced with under-priced large cap stocks with good dividend yields.

# LWM Consultants Ltd

---

## Fund performance

Performance over the last five years is shown below, and year to date.

	2009	2010	2011	2012	2013	2014
<b>Threadneedle UK Equity Income Fund</b>	18.18%	16.65%	1.00%	16.58%	28.96%	4.75%
<b>Lyxor ETF FTSE All Share</b>	32.63%	13.34%	-6.62%	17.46%	24.15%	4.42%

*You should note that past performance is not a reliable indicator of future returns and the value of your investments can fall as well as rise. The total return reflects performance without sales charges or the effects of taxation, but is adjusted to reflect all on-going fund expenses and assumes reinvestment of dividends and capital gains. If adjusted for sales charges and the effects of taxation, the performance quoted would be reduced. Returns are based on the US share class.*

## Conclusion

We believe this to be a well-managed fund delivering long-term out-performance. The management team is strong and there is little to be negative about. It is not exciting but this points it more to a core holding to provide downside 'protection' whilst also participating in upside growth.

*The source of information in this note has been provided by Threadneedle and is correct as at September 2014. These are notes from meeting the fund manager or representative and should not be seen as a recommendation to purchase any fund mentioned. Any reference to shares is not a recommendation to buy or sell. Should you wish to make a decision based on these notes we cannot take responsibility for this and you should carry out your own research before making a decision. You should note that past performance is not a reliable indicator of future returns and the value of your investments can fall as well rise.*