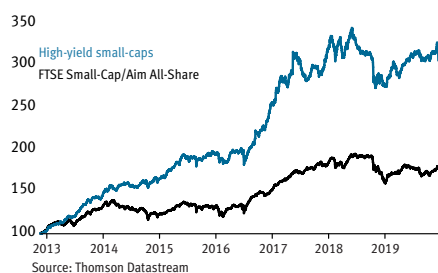




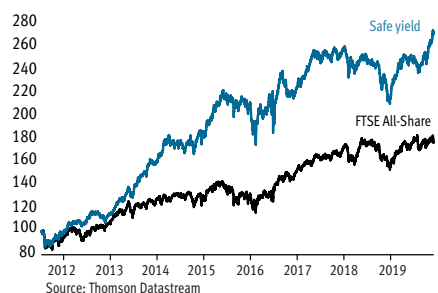
AlphaScreens: Finding dividend diamonds

Dividends are an important source of returns and also a useful valuation measure that can be used to identify shares with the potential for capital growth. But it's important to screen out potential value traps when using yield as a guide

High-yield small-caps



Safe yields (large-caps)



Algy Hall's view:

Investors neglect dividends at their peril. Over the 25 years to the end of 2019, the average annual return from the FTSE All-Share based on share price alone stood at 4.15 per cent, compared with a 7.4 per cent total return once dividends are factored in. And the benefit of reinvesting dividends over the long term makes the difference even more pronounced, with the 25-year cumulative total return from the FTSE All-Share standing at 497 per cent, compared with 176 per cent ignoring dividends. As well as providing income, a good yield can suggest a company has attractive qualities that could support share price performance, and a robust dividend record can indicate a company in good financial health with a strong and stable business.

Foreword by Alpha Editor:

Monday kicked off with another spate of furious selling and the FTSE 100 was down 8 per cent at one stage. In times like these, investors could pick up solid dividend paying stocks at a bargain, although prices could fall further. Another risk that opportunities need to be weighed up against is that dividends can be cut. This is likely if growth in the real economy takes a nose dive thanks to the spread of Covid-19, and consequences of measures to contain it.

One of the measures on our FTSE All-Share dividend screen is to check for beta of companies – how closely their share price is correlated to the index. Companies with a low beta are considered to have defensive properties. This isn't the case for a lot of the companies that score well against the rest of our dividend screen, with the top four all failing the beta test.

No company included on the All-Share gets 8/8 and the other two companies that pass seven tests fail because their dividend isn't covered twice by earnings.

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Large-cap dividend diamonds criteria

Our large-cap screen is tilted towards companies that show signs of having stable prospects associated with dividend staying power. To help assess this, we use a measure of historic share price volatility against the wider market called beta. Betas of below one indicate that a stock has been less sensitive to market movements and suggest it could boast some defensive qualities. The large-cap Alpha dividend yield screen is conducted on all FTSE All-Share stocks using the following criteria:

- A dividend yield higher than the median (mid-rank) average of all dividend-paying shares screened.
- Dividend covered at least twice by earnings.
- Earnings growth forecast in each of the next two financial years (ie dividend cover is not expected to dramatically fall).
- Operating cash conversion of 100 per cent or more (ie earnings are being tuned into cash with which to pay dividends).
- Interest payments covered at least five times by operating profits (ie interest payments on borrowings are not likely be a significant threat to maintaining dividend cover).
- Return on equity of 12.5 per cent or more (i.e. an indicator that the business may be of decent quality [if the interest cover test is also met, it suggests high returns on equity are not overly dependent on high debt levels]).
- A beta of 0.75 or lower.
- No dividend cut in the past three years.

Not many stocks pass such a stringent list of criteria. The ones that pass all the tests are listed at the top of the table, followed by those failing one test, then those failing two tests as detailed in the ‘Tests passed’ column. All stocks must pass the dividend yield test to feature in the table that follows. Special dividends are included in the yield calculation used by the screen, and where a special dividend has been paid, it is highlighted in the table’s ‘Special dividend’ column. While the primary ranking of the stocks is based on the number of tests they pass, inside each of these groupings, stocks are ordered according to their attractiveness based on a combination of dividend yield and dividend cover.

Small-cap dividend diamonds criteria

The small-cap Alpha dividend yield screen is more growth-focused than our large-cap screen, and is conducted separately on the FTSE All-Small and FTSE Aim All-Share indices, with the results presented in two separate tables. While the screen's dividend yield test is more aggressive than the one used by our large-cap screen, the lower average yields from small-caps mean little difference in the absolute level of yield both screens require. The screen uses the following criteria:

- A dividend yield among the top third of all dividend-paying shares screened.
- Dividend covered at least one-and-a-half times by earnings.
- Earnings growth forecast in each of the next two financial years and average growth of 5 per cent or more (ie rising earnings to support dividend growth and maintain or improve dividend cover).
- Positive free cash flow (ie a weak test that earnings are turned into cash with which to pay dividends).
- Interest payments covered at least five times by operating profits (ie interest payments on borrowings are not likely to be a significant threat to maintaining dividend cover).
- A three-year compound annual dividend growth rate of 5 per cent or more.
- A three-year compound annual earnings growth rate of 5 per cent or more.
- A market capitalisation of more than £10m (ie not severely illiquid).

Not many stocks pass such a stringent list of criteria. The ones that pass all the tests are listed at the top of the table that follows, followed by those failing one test, then those failing two tests as detailed in the 'Tests passed' column. All stocks must pass the dividend yield test to feature in the table. Special dividends are included in the yield calculation used by the screen, and where a special dividend has been paid this highlighted in the table's 'Special dividend' column. While the primary ranking of the stocks is based on the number of tests they pass, inside each of these groupings, stocks are ordered according to their attractiveness based on a combination of dividend yield and dividend cover.

Stock screen methodology formulated and explained by Algy Hall

Large-cap dividend diamonds selection (passing at least 6 out of 8 tests)

Name	TIDM	Market cap	Price	Fwd NTM PE	Dividend yield	EPS grth FY+1	EPS grth FY+2	3-month momentum	Net cash/debt (-)	Currency	Test Failed	Special dividend	Tests passed (out of 8)
Sirius Real Estate	LSE:SRE	£846m	82p	18	3.8%	8.4%	10.9%	-6.6%	-278m	EUR	/Beta	NO	7
Hollywood Bowl	LSE:BOWL	£330m	220p	14	5.4%	4.5%	4.7%	-16.0%	-2m	GBP	/Beta	YES	7
Norcros	LSE:NXR	£176m	219p	7	3.8%	1.5%	6.0%	-15.6%	-71m	GBP	/Beta	NO	7
BAE Systems	LSE:BA	£19,136m	597p	12	3.9%	6.3%	6.5%	2.0%	-1,954m	GBP	/Beta	NO	7
Moneysupermarket.com	LSE:MONEY	£1,654m	308p	16	3.8%	5.6%	8.5%	-6.7%	-10m	GBP	/DivCov/	NO	7
MJ Gleeson	LSE:GLE	£486m	878p	13	3.9%	8.8%	9.3%	6.7%	27m	GBP	/DivCov/	NO	7
Taylor Wimpey	LSE:TW	£6,525m	200p	10	9.3%	1.2%	5.7%	6.7%	518m	GBP	/CashConv/Beta	YES	6
Signature Aviation	LSE:SIG	£2,065m	250p	19	5.7%	5.6%	16.3%	-28.1%	-2,210m	USD	/IntCov/RoE/	NO	6
Hays	LSE:HAS	£1,853m	126p	14	7.4%	-25.5%	6.5%	-28.2%	-215m	GBP	/EPSGrth/Beta	YES	6
Int. Consolidated Airlines	LSE:IAG	£8,568m	432p	5	6.3%	-14.5%	30.4%	-26.7%	-7,612m	EUR	/EPSGrth/Beta	NO	6
PageGroup	LSE:PAGE	£1,206m	380p	13	7.0%	-8.1%	15.8%	-24.9%	-31m	GBP	/EPSGrth/Beta	YES	6
Aviva	LSE:AV	£13,451m	343p	6	9.0%	-9.0%	8.7%	-21.1%	10,485m	GBP	/EPSGrth/Beta	NO	6
Barratt Developments	LSE:BDEV	£7,428m	732p	9	6.4%	3.9%	4.5%	3.3%	375m	GBP	/CashConv/Beta	YES	6
Bodycote	LSE:BOY	£1,337m	705p	13	5.5%	-7.7%	4.8%	-22.5%	-112m	GBP	/EPSGrth/Beta	YES	6
PayPoint	LSE:PAY	£556m	823p	13	10.2%	2.1%	3.3%	-16.5%	21m	GBP	/DivCov/DivGrth/	YES	6
Wincanton	LSE:WIN	£303m	245p	7	4.4%	3.9%	3.3%	-13.1%	-139m	GBP	/RoE/CashConv/	NO	6
SSE	LSE:SSE	£16,182m	1,575p	17	6.2%	15.5%	13.4%	12.4%	-9,936m	GBP	/DivCov/IntCov/	NO	6
Ibstock	LSE:IBST	£923m	226p	12	6.5%	2.3%	3.9%	-20.1%	-115m	GBP	/DivCov/Beta	YES	6
S&U	LSE:SUS	£263m	2,170p	9	5.4%	3.3%	9.7%	3.3%	-126m	GBP	/IntCov/CashConv/	NO	6
Redrow	LSE:RDW	£2,439m	711p	7	4.3%	3.1%	2.3%	0.3%	14m	GBP	/CashConv/Beta	NO	6
Photo-Me International	LSE:PHTM	£315m	83p	9	10.1%	7.3%	3.2%	-7.6%	8m	GBP	/DivCov/DivGrth/	NO	6
Prudential	LSE:PRU	£30,910m	1,194p	8	4.1%	-7.1%	8.3%	-14.3%	-10,891m	GBP	/EPSGrth/Beta	NO	6
Mondi	LSE:MNDI	£7,712m	1,591p	12	4.5%	-12.6%	7.7%	-8.9%	-2,202m	EUR	/EPSGrth/Beta	NO	6
National Express	LSE:NEX	£1,962m	385p	11	4.2%	6.4%	5.8%	-20.2%	-1,279m	GBP	/DivCov/IntCov/	NO	6
IMI	LSE:IMI	£2,597m	959p	13	4.3%	1.5%	9.2%	-23.9%	-434m	GBP	/DivCov/Beta	NO	6
Vitec	LSE:VTC	£387m	850p	11	4.6%	-4.8%	15.2%	-26.3%	-96m	GBP	/DivCov/EPSGrth/	NO	6
Telecom Plus	LSE:TEP	£1,051m	1,342p	20	3.9%	9.1%	7.0%	-4.9%	-41m	GBP	/DivCov/Beta	NO	6

Source: S&P Capital IQ, 9 March 2020

Continued on the next page

FTSE All-Small dividend diamonds selection (passing at least 6 out of 8 tests)

Name	TIDM	Market cap	Price	Fwd NTM PE	Dividend yield	EPS grth FY+1	EPS grth FY+2	3-month momentum	Net Cash/Debt (-)	Currency	Test failed	Special dividend	Tests passed (out of 8)
UP Global Sourcing	LSE:UPGS	£48m	61p	7	6.7%	3.0%	5.2%	-32.9%	-14m	GBP	/FwdEPSGrth/	NO	7
City of London Investment	LSE:CLIG	£97m	390p	11	6.9%	6.8%	7.8%	-11.6%	11m	GBP	/DivCov/	NO	7
Hollywood Bowl	LSE:BOWL	£330m	220p	14	5.4%	4.5%	4.7%	-16.0%	-2m	GBP	/FwdEPSGrth/	YES	7
STV	LSE:STVG	£141m	360p	8	5.6%	8.5%	12.8%	-12.5%	-55m	GBP	/EPSGrth/	NO	7
BlackRock Latin Am. IT	LSE:BRLA	£159m	404p	-	6.6%	-	-	-19.5%	-25m	USD	/FwdEPSGrth/EPSGrth/	NO	6
Record	LSE:REC	£62m	32p	11	9.4%	-9.8%	-2.2%	-22.2%	22m	GBP	/FwdEPSGrth/DivCov/	YES	6
Bluefield Solar Inc. Fund	LSE:BSIF	£511m	138p	-	6.0%	-	-	-3.1%	1m	GBP	/FwdEPSGrth/IntCov/	YES	6
Photo-Me International	LSE:PTM	£315m	83p	9	10.1%	7.3%	3.2%	-7.6%	8m	GBP	/EPSGrth/DivCov/	NO	6
S&U	LSE:SUS	£263m	2,170p	9	5.4%	3.3%	9.7%	3.3%	-126m	GBP	/IntCov/FCF/	NO	6
Target Healthcare REIT	LSE:THRL	£533m	117p	19	5.7%	25.3%	6.0%	-2.1%	-80m	GBP	/DivGrth/DivCov/	NO	6

Source: S&P Capital IQ, 9 March 2020

Aim dividend diamonds selection (passing at least 6 out of 8 tests)

Name	TIDM	Market cap	Price	Fwd NTM PE	Dividend yield	EPS grth FY+1	EPS grth FY+2	3-month momentum	Net Cash/Debt (-)	Currency	Test failed	Special dividend	Tests passed (out of 8)
STM	AIM:STM	£15m	25p	4	7.9%	6.1%	6.5%	-3.1%	15m	GBP	na	NO	8
Finsbury Food	AIM:FIF	£103m	81p	8	4.3%	7.8%	3.1%	-7.1%	-44m	GBP	na	NO	8
Gateley	AIM:GTLY	£215m	185p	13	4.3%	6.1%	7.5%	-0.9%	-27m	GBP	na	NO	8
M&C Saatchi	AIM:SAA	£69m	72p	6	15.3%	-51.7%	-18.0%	-34.9%	-31m	GBP	/FwdEPSGrth/	NO	7
Somero Enterprises	AIM:SOM	£130m	230p	9	6.3%	-9.1%	-3.8%	-1.8%	13m	USD	/FwdEPSGrth/	NO	7
Polar Capital	AIM:POLR	£429m	460p	11	7.2%	-23.9%	6.2%	-15.3%	120m	GBP	/FwdEPSGrth/	NO	7
NWF	AIM:NWF	£78m	160p	10	4.1%	-1.9%	11.1%	2.6%	-34m	GBP	/FwdEPSGrth/	NO	7
MTI Wireless Edge	AIM:MWE	£30m	35p	-	4.5%	-	-	-14.5%	7m	USD	/FwdEPSGrth/	NO	7
Rotala	AIM:ROL	£25m	49p	7	5.5%	26.7%	9.1%	-5.8%	-35m	GBP	/IntCov/	NO	7
Trans-Siberian Gold	AIM:TSG	£60m	69p	-	9.2%	-	-	-6.0%	-10m	USD	/FwdEPSGrth/DivGrth/	YES	6
Northern Bear	AIM:NTBR	£12m	63p	-	6.4%	-	-	-10.1%	-2m	GBP	/FwdEPSGrth/FCF/	YES	6
RTC	AIM:RTC	£9m	61p	-	6.8%	-	-	16.2%	-6m	GBP	/FwdEPSGrth/MktCap/	NO	6
Wynnstay	AIM:WYN	£53m	267p	8	5.3%	0.3%	5.9%	-14.0%	4m	GBP	/FwdEPSGrth/EPSGrth/	NO	6
ULS Technology	AIM:ULS	£34m	53p	9	4.8%	-13.0%	-23.2%	6.5%	-5m	GBP	/FwdEPSGrth/DivGrth/	NO	6
Belvoir Group	AIM:BLV	£53m	141p	11	5.1%	8.5%	16.2%	-0.8%	-10m	GBP	/DivGrth/FCF/	NO	6
Highland Gold Mining	AIM:HGM	£803m	221p	9	5.6%	98.1%	-4.7%	20.6%	-217m	USD	/FwdEPSGrth/DivCov/	NO	6
Real Estate Investors	AIM:RLE	£95m	51p	12	7.4%	9.2%	3.3%	-8.5%	-90m	GBP	/DivCov/IntCov/	NO	6
Amino Technologies	AIM:AMO	£97m	128p	13	5.7%	20.8%	11.4%	17.0%	1m	USD	/EPSGrth/DivCov/	NO	6

Source: S&P Capital IQ, 9 March 2020

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