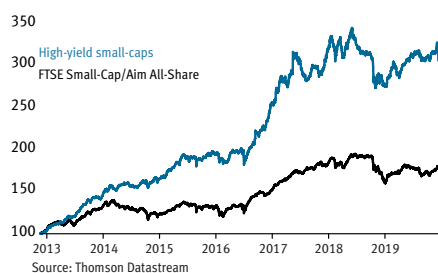




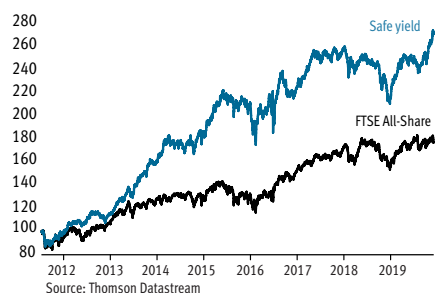
AlphaScreens: Finding dividend diamonds

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:

- **Sirius Real Estate (SRE)**, which focuses on German property still tops our FTSE All-Share dividend screen. Share price momentum has continued, and earnings growth forecasts are roughly where they were a month ago.
- Entertainment group **Hollywood Bowl (BOWL)** also gets top marks against our criteria.
- The type of business should be a consideration when assessing tests failed. Comparison site **Moneysupermarket.com (MONY)** fails our strict dividend cover test, but as it has no long-term debt and requires little long-term capital expenditure, it can afford to pay out a higher proportion of its earnings.
- The biggest companies don't tend to score well against our screen, and those that do could be flashing warning signals. For example, the market is clearly signalling scepticism about the sustainability of tobacco giant **Imperial Brands' (IMB)** dividend policy.

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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 to 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 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	£947m	91p	21	3.3%	8.4%	10.9%	22.0%	-278m	EUR	na	NO	8
Hollywood Bowl	LSE:BOWL	£426m	284p	19	4.2%	4.5%	4.7%	12.8%	-2m	GBP	na	YES	8
Apax Global Alpha	LSE:APAX	£884m	180p	-	4.7%	-	-	7.5%	116m	EUR	/EPSGrth/	NO	7
Moneysupermarket.com	LSE:MONY	£1,778m	331p	18	3.3%	5.0%	6.2%	-4.9%	-13m	GBP	/DivCov/	NO	7
Telecom Plus	LSE:TEP	£1,179m	1,506p	23	3.5%	9.0%	7.0%	21.8%	-41m	GBP	/DivCov/	NO	7
TBC Bank	LSE:TBCG	£689m	1,250p	5	4.3%	9.6%	7.6%	-7.7%	-3,016m	GEL	/IntCov/CashConv/	NO	6
Barratt Developments	LSE:BDEV	£8,112m	799p	11	5.8%	2.6%	3.1%	29.7%	375m	GBP	/CashConv/Beta	YES	6
PageGroup	LSE:PAGE	£1,526m	481p	14	5.4%	-0.3%	3.8%	3.6%	-57m	GBP	/EPSGrth/Beta	YES	6
Bodycote	LSE:BOY	£1,643m	867p	16	4.5%	-7.3%	4.7%	7.5%	-112m	GBP	/EPSGrth/Beta	YES	6
SSE	LSE:SSE	£16,467m	1,602p	17	6.1%	15.4%	13.4%	28.0%	-9,936m	GBP	/DivCov/IntCov/	NO	6
PayPoint	LSE:PAY	£659m	975p	15	8.6%	2.1%	3.3%	6.6%	21m	GBP	/DivCov/DivGrth/	YES	6
S&U	LSE:SUS	£267m	2,200p	9	5.4%	4.0%	9.6%	8.5%	-126m	GBP	/IntCov/CashConv/	NO	6
Wincanton	LSE:WIN	£359m	290p	8	3.8%	3.8%	3.3%	14.8%	-139m	GBP	/RoE/CashConv/	NO	6
Mondi	LSE:MNDI	£7,996m	1,650p	12	4.2%	-9.4%	-10.7%	-3.2%	-2,341m	EUR	/EPSGrth/Beta	NO	6
Redrow	LSE:RDW	£2,642m	770p	8	4.0%	2.1%	2.4%	26.0%	14m	GBP	/CashConv/Beta	NO	6
Countryside Properties	LSE:CSP	£2,261m	507p	12	3.2%	9.3%	8.7%	43.0%	78m	GBP	/CashConv/Beta	NO	6
Photo-Me International	LSE:PHTM	£336m	89p	10	9.5%	7.3%	3.2%	-5.4%	8m	GBP	/DivCov/DivGrth/	NO	6
Vistry Group	LSE:VY	£3,038m	1,398p	13	4.2%	10.0%	19.7%	27.5%	80m	GBP	/DivCov/Beta	NO	6
Prudential	LSE:PRU	£37,836m	1,461p	10	3.4%	-8.4%	5.6%	6.8%	-10,891m	GBP	/EPSGrth/Beta	NO	6
Headlam	LSE:HEAD	£453m	539p	14	4.6%	-10.1%	2.4%	12.5%	-14m	GBP	/DivCov/EPSGrth/	NO	6
Imperial Brands	LSE:IMB	£17,185m	1,832p	7	11.3%	-3.6%	2.8%	2.7%	-11,350m	GBP	/DivCov/EPSGrth/	NO	6
BAE Systems	LSE:BA	£20,985m	655p	14	3.5%	7.4%	3.0%	12.2%	-3,369m	GBP	/DivCov/CashConv/	NO	6
MJ Gleeson	LSE:GLE	£516m	932p	14	3.7%	9.3%	9.3%	14.0%	30m	GBP	/DivCov/CashConv/	NO	6
Severfield	LSE:SFR	£268m	88p	11	3.3%	13.2%	7.0%	13.8%	10m	GBP	/DivCov/RoE/	NO	6
Vitec	LSE:VTC	£471m	1,035p	13	3.6%	-12.6%	11.9%	-17.7%	-108m	GBP	/DivCov/EPSGrth/	NO	6
Tate & Lyle	LSE:TATE	£3,680m	790p	15	3.7%	3.1%	2.4%	9.4%	-433m	GBP	/DivCov/DivGrth/	NO	6
Clipper Logistics	LSE:CLG	£272m	268p	15	3.6%	26.9%	6.7%	14.2%	-250m	GBP	/DivCov/IntCov/	NO	6
Ten Entertainment	LSE:TEG	£204m	314p	16	3.6%	16.1%	13.8%	9.8%	-10m	GBP	/DivCov/DivGrth/	NO	6

Source: S&P Capital IQ, 10 February 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	£52m	66p	8	6.2%	3.0%	5.2%	-25.9%	-14m	GBP	/FwdEPSGrth/	NO	7
BlackRock Latin Am. IT	LSE:BRLA	£192m	490p	-	5.5%	-	-	7.7%	-25m	USD	/FwdEPSGrth/EPGrth/	NO	6
Record	LSE:REC	£76m	38p	13	7.8%	-9.8%	-2.2%	-1.1%	22m	GBP	/FwdEPSGrth/DivCov/	YES	6
S&U	LSE:SUS	£267m	2,200p	9	5.4%	4.0%	9.6%	8.5%	-126m	GBP	/IntCov/FCF/	NO	6
Photo-Me International	LSE:PHTM	£336m	89p	10	9.5%	7.3%	3.2%	-5.4%	8m	GBP	/EPSGrth/DivCov/	NO	6
Target Healthcare REIT	LSE:THRL	£565m	124p	20	5.4%	25.3%	6.0%	7.3%	-80m	GBP	/DivGrth/DivCov/	NO	6
Devro	LSE:DVO	£281m	168p	11	5.3%	5.3%	4.9%	6.4%	-149m	GBP	/DivGrth/DivCov/	NO	6

Source: S&P Capital IQ, 10 February 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	£16m	28p	5	7.2%	6.1%	6.5%	-33.6%	15m	GBP	na	NO	8
M&C Saatchi	AIM:SAA	£87m	93p	8	11.8%	-48.2%	-15.2%	-47.1%	-31m	GBP	/FwdEPSGrth/	NO	7
Somero Enterprises.	AIM:SOM	£152m	270p	9	5.5%	-2.4%	-3.7%	42.3%	13m	USD	/FwdEPSGrth/	NO	7
Polar Capital	AIM:POLR	£522m	560p	14	5.9%	-23.8%	4.9%	6.6%	120m	GBP	/FwdEPSGrth/	NO	7
Rotala	AIM:ROL	£27m	54p	7	5.0%	26.7%	9.1%	3.8%	-35m	GBP	/IntCov/	NO	7
Trans-Siberian Gold	AIM:TSG	£48m	55p	-	11.8%	-	-	-34.4%	-10m	USD	/FwdEPSGrth/DivGrth/	YES	6
Northern Bear	AIM:NTBR	£14m	73p	-	5.5%	-	-	2.1%	-2m	GBP	/FwdEPSGrth/FCF/	YES	6
Vertu Motors	AIM:VTU	£132m	36p	7	4.5%	0.3%	9.8%	-6.6%	-82m	GBP	/EPSGrth/IntCov/	NO	6
Wynnstay Group	AIM:WYN	£56m	283p	9	5.0%	0.3%	5.9%	1.4%	4m	GBP	/FwdEPSGrth/EPGrth/	NO	6
ULS Technology	AIM:ULS	£41m	63p	10	4.0%	-13.0%	-23.2%	21.9%	-5m	GBP	/FwdEPSGrth/DivGrth/	NO	6
Vianet Group	AIM:VNET	£43m	154p	16	3.7%	17.5%	-1.1%	14.6%	-1m	GBP	/FwdEPSGrth/DivGrth/	NO	6
Redde	AIM:REDD	£310m	101p	8	11.5%	6.2%	-0.5%	-6.5%	-35m	GBP	/FwdEPSGrth/DivCov/	NO	6
Highland Gold Mining	AIM:HGM	£766m	210p	9	5.9%	98.1%	-4.7%	7.0%	-217m	USD	/FwdEPSGrth/DivCov/	NO	6
Belvoir Group	AIM:BLV	£66m	178p	14	4.0%	8.5%	16.2%	48.1%	-10m	GBP	/DivGrth/FCF/	NO	6
Real Estate Investors	AIM:RLE	£105m	57p	13	6.6%	9.2%	3.3%	4.3%	-90m	GBP	/DivCov/IntCov/	NO	6

Source: S&P Capital IQ, 10 February 2020

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