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PENSIONS & ISAS SPECIAL REPORT

# Unearthed: five hidden pockets of yield

## As income from familiar sources disappears, *Laura Suter* examines some lesser-known high-yielding investments

Investors are facing the fiercest struggle in generations to obtain income from their investments.

The financial crisis and the response to it by the world's leading central banks – including the Bank of England – has resulted in returns on shares, bonds and cash plunging to record lows.

Bonds have traditionally been a staple holding in a mixed portfolio, but in many cases now deliver owners a modest loss. This has pushed more investors into company shares, which are riskier. But prices in this market have now been pushed up, meaning the yield on offer has reduced.

What is left for hunters of yield?

### Infrastructure

**Why?**

Investing in the building of roads, train lines, bridges and energy generation and distribution offers potentially outsized returns.

Many are also expecting the Government to announce more funding for UK infrastructure projects in November's Autumn Statement from new Chancellor Philip Hammond.

Darius McDermott, of Chelsea Financial Services, the advice firm, said: "There will be a lot of government-backed infrastructure projects coming up for grabs."

This helps investors in a number of ways. In some cases governments part-fund projects, with private investors – in the form of funds in which individuals or institutions invest their money – sitting alongside as part owners of the projects. In other cases the infrastructure funds invest in other businesses which will be major suppliers and contractors in the government-backed ventures.

**How can you invest?**

Mr McDermott said for those wanting an active fund investing in global infrastructure projects, the Legg Mason IF RARE Global Infrastructure is a good option. The fund targets a 5pc yield, and is run by a "very experienced team".

For investors wanting a "passive" investment fund, which tracks a related sector, Russ Mould, of fund shop AJ Bell, recommended the ETFS US Energy Infrastructure exchange traded fund. The fund tracks 25 companies that invest in the US energy sector, including the pipelines. It has a yield of more than 6pc and low ongoing costs.

But Mr Mould warns that the ETF is "synthetic", which means it does not own the shares in the companies, and instead buys derivatives designed to mimic price movements of those shares. This adds an extra level of risk. Those wanting a "closed ended" fund, or investment trust, will find many are now trading at big premiums. A "premium" is when demand for a trust's shares is such that their price rises above the value of the underlying assets. This is offputting for investors, as it suggests they are over-paying.

The GCP Infrastructure Investment trust has a decent yield of around 5.5pc, but trades at over a 20pc premium. Likewise, the HICL Infrastructure Company yields about 4.5pc, but is trading at a premium of just under 20pc. Laith Khalaf, of investment shop Hargreaves Lansdown, warns of a significant risk to capital if these premiums narrow, with share prices falling into closer alignment with the value of the holdings.

### Property

**Why?**

Commercial property –office space, warehousing and shops – offers good yields, made better by the dent in confidence this sector suffered following the EU referendum. That had the effect of pushing down prices, with rental yields thus rising.

Experts think investors would be wrong to dismiss the sector altogether, but say their choice of investment vehicle is key.

"Open-ended" funds, which allow investors to withdraw their money, were hit in the panic after the EU vote, and many stopped investors taking money out or charged large "fees" for doing so. These fees were in some cases a reduction in the value of departing investors' holdings which aimed to reflect the likely fall in the properties' values, even though no properties had at that stage been sold.

Meanwhile "closed-end" funds, or investment trusts, did not suffer the same problems, as they are traded like shares on the stock market. They have a fixed pool of capital invested in buildings. Departing investors sell their holdings to other shareholders on the open market. These shares also suffered a sharp slump in the period after the referendum.

Mr Khalaf said: "Closed ended property funds are a better bet but they can be expected to be more volatile because of the movement of the share prices as well as the underlying assets."

**How can you invest?**

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Mr McDermott likes the Henderson UK Property fund, which is an open ended fund. It is one of the funds that closed to prevent investor withdrawals, but is reopening this Friday. It has a 3pc yield.

Another option for investors who want to have more access to their money should they wish to redeem is the Premier Pan European Property fund, which has delivered a 4.2pc return in the past year.

Rather than investing in physical property, such as office buildings and shopping centres, the fund invests in the shares of property companies, making it easier to buy and sell investments. For those wanting a closed-ended fund, Mike Deverell, investment manager at Equilibrium Asset Management, tips the Kames Property Income fund, which is currently yielding 5.75pc. In particular Mr Deverell likes the fund because it has no allocation to London property, which he thinks is more likely to see a downturn following the EU vote.

## Student property

**Why?**

More niche than broad property is the student property sector. Mike Pinggera, fund manager at investment house Sanlam FOUR, said that a lack of supply and high demand for student property are the attractions.

The Government recently removed the cap on student numbers, meaning from last year universities can recruit as many students as they like. This is tipped to lead to more demand for student accommodation.

"The attractions of student accommodation are quite simple: on one side, we have strong demand from both a growing population and the removal of the caps on the number of students; and on the other side, a lack of beds in terms of both number and quality," said Mr Pinggera.

Investors can buy student property directly. However, this means the investment will be very exposed to one market, and will also face the stricter requirements on mortgages and taxation the buy-to-let industry is facing at the moment.

There are a few ready-made portfolios in the market. GCP Student Living is one, and it has grown from around £70m three years ago to £384.8m in assets today, and is currently yielding more than 4pc.

Mr Pinggera said that there are a number of companies listed on the stock exchange that offer exposure to the sector. One is Unite Group, which is the largest single owner of student property with a market cap of £1.4bn. It currently yields 2.4pc. Empiric Student Property has a smaller market cap of £600m and yields just over 5pc.

## Commodities

**Why?**

For inflation protection. If and when inflation returns, investing in assets that usually see a price rise in line with inflation could be a good call.

Commodities are one such investment. Over the longer term, indebted governments are likely to want to encourage a return to inflation, and most commentators expect further measures to stimulate growth and inflation alongside.

**How can you invest?**

There are numerous commodity funds, including a number of exchange-trade funds that track commodity sectors. Mr Mould likes the City Natural Resources High Yield fund. As an investment trust it is a listed fund, currently yielding 4.8pc. It invests in the shares of gold, silver and copper miners, oil companies and diamond diggers. While it is fairly costly, with an ongoing charge of 1.74pc, the trust is trading at a discount to its net asset value of 18pc, offering potential additional returns if that discount narrows.

## Emerging markets or high-yield bonds

**Why?**

Many government bonds across the world are offering record low returns, and some are now paying out negative yields. However, bonds from emerging markets are still paying out higher rates, as are bonds from riskier companies.

Mr Mould said: "Ten years ago you could have got around a 5pc yield from a 10-year UK Government Gilt but to find that now investors have to

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consider either low-grade corporate debt or emerging market debt."

**How can you invest?**

Investing via a fund can help to cut the risk, with fund managers spreading the portfolio between different countries and companies.

Mr Mould said the Baillie Gifford Emerging Markets Bond fund offers a yield of around 5.6pc. The fund can hold bonds issued by governments, companies and by the public sector. However, he warns that performance has not been reliable.

Mr McDermott highlights the Aberdeen Emerging Market bond fund, which has a yield of 7pc.

In the high-yield bond market, Mr Khalaf highlighted the Royal London Sterling Extra Yield bond fund, which currently yields over 6pc, although he warns this is variable and not guaranteed, and the Artemis Strategic Bond, which currently yields just over 4pc.

## 'Investing in infrastructure can offer potentially outsized returns'

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**Infrastructure**
ETFS US Energy Infrastructure
Yield: 6pc

**Property**
Kames Property Income
Yield: 5.75pc

**Commodities**
City Natural Resources High Yield
Yield: 4.8pc

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**Global search** Three investments, above, that offer the chance of above-average returns

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