Interest rate rise ahead but sustainable dividends still the better bet

by John Harrington

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With interest rates looking like they are likely to go up before the end of the year, income stocks might come under a bit of pressure. Let's not kid ourselves, though; returns offered by savings accounts are unlikely to get people salivating, even if the Old Lady of Threadneedle Street ups the reference rate by half a point.

Better returns are available in equities, though the problem with dividends is that they are not guaranteed. If you are a real risk-averse income investor, then dividend cover – earnings per share divided by dividend per share – of two or more is a good level to aim for.

You'll find just 51 FTSE 100 companies have dividend cover of two or more based on forecast earnings; only 149 FTSE 350 companies meet the criteria.

Reinvested dividends have accounted for around two-thirds of total returns from the FTSE All Share index over the past 30 years, so the argument for having a high proportion of dividend payers in the portfolio is a strong one.

Some people will still like the prospect of a bit of sizzle, however, which was why we set up the "**Aim sustainable dividends portfolio**", to identify growth stocks (though the terms "Aim-listed" and "growth stock" are not necessarily synonymous) that are paying dividends, and likely to go on doing so.

Portfolio is showing a small profit and outperforming the FTSE 100

Created in April of this year the portfolio is showing a small profit – and that's even after factoring in dealing costs and bid/offer spreads - whereas the FTSE 100 over the same period is down 0.7%. There are just three stocks in the portfolio, because the criteria for inclusion are fairly demanding, and in fact only one of them – **Zytronic** PLC (**LON:ZYT**) - is showing a profit, but it's an impressive 37% gain that has more than offset the thus-far disappointing performance of **James Halstead PLC** (**LON:JHD**) and **Miton Group PLC** (**LON:MGR**).

Halstead is a manufacturer of flooring products, so its shares have been affected by the slow-down in the housing market.

Miton is an investment management company focused, appropriately enough, on small companies that pay sustainable dividends. It had a bit of a summer slump but the shares have been picking up recently; it rose 2.7% today on the back of some well-received half-year results. Assets under management rose to £3,354mln at the end of June from £2,542mln a year earlier, but had dipped to £3,490mln by the end of August. Adjusted profit before tax declined to £2.9mln from £5.1mln the previous year, and trading for the full year is expected to be at least in line with current market expectations. The group does not pay interim dividends but with cash of £18.2mln, and last year's dividend soaking up just £1.5mln, the dividend looks set to be at least maintained, and hopefully improved.

Halstead will report its full-year results on 2 October, at which point we will review whether it deserves to stay in the portfolio.

The software screen will be the ultimate arbiter but it is tempting sometimes to override the machine and seize on a dividend company that catches the eye, particularly as there was nothing this month that cropped up on the stock filter that was worthy of consideration.

Bowled over by one stock

One stock to attract my notice was **Ten Entertainment Group PLC** (**LON:TEG**), the ten-pin bowling alleys operator, which recently surprised the market by announcing a dividend of 3p in its first set of interim results as a public company. That's certainly a good start, and it seemed to catch broker Numis Securities on the hop.

READ Ten Entertainment's current trading picks up as wet weather drives leisure seekers indoors

Numis increased its forecast for the full-year dividend to 9.7p; if it proves to be on the money, the shares are yielding 4.9%. It is not always wise to go for the biggest yielders, however, so we'll have to see whether Ten Entertainment has what it takes to tick the other boxes required for inclusion in the 'Aim sustainable dividends portfolio'.

In the meantime, here's a quick check on how the portfolio is doing:

Company	Number of shares	Total cost	Average price per share	Current bid price	Current value	Profit/loss (£)	Profit/loss (%)
James Halstead	195	£998	511.69p	425.5p	£830	-£168	-17%
Miton Group	2,240	£1,000	44.67p	40p	£896	-£105	-10%
Zytronic	229	£1,000	436.55p	590p	£1,351	£351	+35%

- Cash: £6,940
- Market value of current holdings: £3,076
- Market value (including cash): £10,017
- Unrealised profit on current positions: +£79
- Dividends received: £44
- Profit/loss from closed positions: -£105
- Total realised profit/loss + dividends: -£61

Lost share certificates – update

We have reported previously on the battle waged against Capita Registrars by shareholders Deryn and Derek Hemment, who owned £1.5 million of Compass shares. They faced an attempted charge of £25,000 by to indemnify against the consequences of a lost share certificate. The certificate had been mailed to Capita so that a small part-sale could be made. The balance certificate had been returned by regular mail and had been lost.

The story has a happy ending. After a two-year battle the Hemments resorted to the Small Claims Court, which found in their favour, citing negligence by the registrar.

Charging for unnecessary indemnities is a standard piece of gouging by registrars. A past survey of UKSA members revealed a number of examples. Such certificates are no longer legal proof of ownership and if fraudulently presented as such would be exposed by the electronic ownership records which the registrar operates.