The Daily Telegraph

Saturday 4 March 2017

YOUR MONEY

The ultimate funds for income seekers

While some funds seem to deliver income *or* growth, an elite group has managed to generate both. *Laura Suter* reports

PA ARCHIVE

Francis Brooke of the Trojan Income fund has produced the biggest returns. His firm, Troy, was named after the racehorse that won the Derby in 1979 with Willie Carson in the saddle

Investors who want the highest possible income from their funds will normally have to sacrifice capital returns, new figures show. Data on the fund managers who have delivered the highest income over the past 10 years lays bare the compromise that incomehungry investors face: higher income now at the cost of capital returns. Investors can have jam today or jam tomorrow – not both.

Over the past 10 years, the fund manager to have produced the most income, Nick Purves, has given investors £5,649 in income on an initial investment of £10,000. However, investors with Mr Purves, who currently runs the RWC Enhanced Income fund, have at the same time faced a 21.2pc fall in their initial capital, taking their £10,000 initial investment to £7,880.

The research, from Hargreaves Lansdown, the fund shop, looks over the past 10 years and tracks managers rather than just funds. This means that when a fund manager has moved from one firm to another to run a similar fund, his or her track record has been counted across these funds. There are just 34 fund managers who have a track record over 10 years.

One example is Neil Woodford, who worked for many years at Invesco Perpetual before starting his own fund management house, Woodford Investment Management.

Hargreaves' data shows that four of the top 10 fund managers by income actually lost investors money on their original capital.

Tim Rees, who currently runs the Insight Equity Income Booster fund, has handed investors £5,463 in income on a £10,000 initial investment over the 10 years. However, during this time their initial money has fallen to £7,560.

Similarly Michael Clark, who currently runs the Fidelity Enhanced Income fund, has generated £5,180 in income over the period but the original £10,000 investment has dropped to £8,880.

A number of the funds that appear top for income – including those of RWC, Insight and Fidelity – use complicated techniques to boost the income they deliver. They sell "derivatives" that essentially involve the fund manager agreeing to share any future capital gains with a third party. A fee is paid for the agreement, which creates immediate, upfront cash. This can be distributed to investors as income.

'A lower capital base will affect the potential to generate high levels of income in the long run'

However, if the fund's holdings rise in value, some of the gain goes to whoever bought the derivatives. This explains the lacklustre capital returns from many of these funds.

"Ultimately, a lower capital base will affect the potential for these funds to generate high levels of income in the long run, so they are appropriate for those who prioritise high income in the short term over capital and income growth over the long term," said Laith Khalaf of Hargreaves Lansdown.

There are some exceptions. Thomas Moore, who currently runs the Standard Life UK Equity Income Unconstrained fund, generated the fourth highest income of his peer group over the 10-year period, of £4,571. Over that time he also boosted the capital value by 52.2pc, turning £10,000 into £15,220.

Different income funds will work for different investors. Funds that deliver a healthy income and grow capital are the holy grail for most investors, with Hargreaves' figures showing that 26pc of a typical DIY investor's fund portfolio is invested in UK income funds.

For those later in life, who are relying on the income from their investments to fund their lifestyle, higher income is usually the goal. However, younger individuals will often be happy to sacrifice some income in order to get a better return on their original investment.

Others automatically reinvest the income generated by these funds, using it to buy fund units, so are focused on the total return of income and capital gains combined.

If investors are willing to accept a lower income, they can get attractive total returns.

Francis Brooke, who currently runs the Trojan Income fund, has almost doubled investors' money, turning £10,000 into £19,379 if the investor had taken the £4,549 income over the 10 years and left their original capital invested. If they had chosen "accumulation units", which automatically reinvest any income back into the fund, they would have seen a 127pc total return – or £22,700. Mr Brooke's firm, Troy, was named after the racehorse that won the Derby in 1979.

Mark Barnett, who currently runs the Invesco Perpetual High Income fund, has generated £19,165 of total return. This is made up of £3,685 of total income, which, while less than many peers, is in addition to £5,480 of capital growth on the initial £10,000.

Mr Barnett has outperformed his predecessor, Mr Woodford, over the period. Mr Woodford has returned £3,784 in income and £4,090 in capital growth. If investors had reinvested their income they would now have £20,420.

Part of the performance difference between Mr Woodford and Mr Barnett is due to Mr Barnett's previous fund, Invesco Perpetual Strategic Income, being more heavily invested in medium-sized companies than Mr Woodford's previous funds. Such companies have outperformed over the period.

The difference is also due to the fact that Mr Woodford had a period in which he was not running funds, between his stints at Invesco and Woodford Investment Management.

"Partly this is simply a demonstration that, like Neil Woodford, Mark Barnett is a very good fund manager," said Mr Khalaf. However, the importance of picking the right fund is highlighted by the figures. The average return produced by the UK equity income sector, into which these funds fall, is actually lower than that from tracker funds, a lower-cost option that just tracks the performance of a market.

Over the 10 years, the UK equity income sector delivered an average total return of £15,799, compared with £16,367 for a tracker of the FTSE All Share index.

This is partly because the sector average includes funds that have been closed or merged over the 10 year period, often done as the fund failed to attract enough assets or did not deliver sufficient performance to survive.

Another factor is that the sector has strict criteria for inclusion and many high-profile funds that have failed to meet them have been kicked out. In many instances these funds have actually outperformed over the long term, further affecting the average figures.

Top funds by total returns

Manager	Current fund	Total return	Income on £10,000
Francis Brooke	Trojan Income	127%	£4,549
Thomas Moore	SLI UK Equity Income Unconstrained	122.8%	£4,571
Mark Barnett	Invesco Perpetual High Income	117.1%	£3,685
Richard Colwell	Threadneedle UK Equity Alpha Income	116.2%	£4,020
Martin Cholwill	Royal London UK Equity Income	108.2%	£4,270
Neil Woodford	Woodford Equity Income	104.2%	£3,784
Clive Beagles	JOHCM UK Equity Income	102.5%	£4,551
Chris White	Premier Monthly Income	95.1%	£4,469
Matt Hudson	Schroder UK Alpha Income	91.8%	£4,220
Michael Clark	Fidelity MoneyBuilder Dividend	89.9%	£4,333

Source: Hargreaves Lansdown, Thomson Reuters Lipper

Top managers by income produced

Manager	Current fund	Total Return	Income on £10,000
Nick Purves	RWC Enhanced Income	£5,649	49.4%
Tim Rees	Insight Equity Income Booster	£5,463	53.6%
Michael Clark	Fidelity Enhanced Income	£5,180	59.1%
Thomas Moore	SLI UK Equity Income Unconstrained	£4,571	122.8%
Clive Beagles	JOHCM UK Equity Income	£4,551	102.5%
Francis Brooke	Trojan Income	£4,549	127%
Chris White	Premier Monthly Income	£4,469	95.1%
Tineke Frikee	Smith & Williamson UK Equity Income	£4,381	53.4%
Michael Clark	Fidelity MoneyBuilder Dividend	£4,333	89.9%
Martin Cholwill	Royal London UK Equity Income	£4,270	108.2%

Source: Hargreaves Lansdown, Thomson Reuters Lipper