

Stock up on oil while bank shares take a back seat

MUCH debate is being held about the benefits of the government taking decisive action by implementing a comprehensive set of measures to make commercial investments in UK banks.

The aim is to help stabilise the financial markets and support the long-term strength of the economy.

Nevertheless, while the immediate benefit is to maintain the banking system, there will be disadvantages for shareholders, particularly from the lack of dividend payments over the next few years.

Out of interest, when the Scandinavian governments bailed out their banks on the same lines, it took at least six years for lending levels to return to normal and, even after that point, the governments were still not able to recoup their investments.

At the time of writing, it appears that the UK government is aiming to take a 57 per cent stake in RBS, a 43.5 per cent stake in HBOS and a 43.5 per cent stake in Lloyds TSB,

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leaving Barclays, Standard Chartered and HSBC as free-standing institutions.

Investors need to consider whether it is best to move across to the free-standers to benefit from dividends over the next few years as the returns from the nationalised institutions will be less than average and, in many cases, will only comprise of additional stock rather than cash payments.

Outwith the financial sector, the banking rescue plan should prove beneficial particularly to companies providing essential goods and services and this is where we see security of dividend payments over the foreseeable future.

For example, utility companies, energy companies and food and drink companies can continue paying dividends in an environment where they feel more secure about their banking arrangements and, for investors, they are at least companies that generate real earn-



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ings from proper businesses rather than from growth companies, which rely on complex financing arrangements.

LOOKING ahead, there will be the inevitable currency gyrations and one of our views is that the US dollar is likely to come under sustained pressure as the propensity to print money leads to the inevitable fear of inflation. In fact, there may be a major devaluation of the US dollar over the next five-year period.

Although there is a degree of salvation for the corporate world, it is still anticipated that the property environment will continue to be extremely difficult as lending arrangements are no doubt tightened up and we see a reversion to the lending practises of the 1950s, 60s and 70s, where lending and borrowing was undertaken on a strict, formulated basis.

The result of all this will be that property prices will take much longer to recover than anticipated and will probably have to face the problem of high interest rates before the market recovers.

This leads us to be more comfortable backing utility investments or oil shares such as BP or Royal Dutch Shell as both are trading on historically low multiples, providing dividend yields to an excess of 5.5 per cent. Banks will have to take a backseat for a while longer.

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