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Mid-cap stocks still dominate the STAR selections

I have now been writing updates on the Share Tracking and Ranking (STAR) High Income Portfolio since October 2005. Writing regular updates on existing portfolios creates something of a problem if you did not invest in the original selection. I have tried to solve this problem by adding in a current selection at the end of each article but obviously it is impractical to recap on all the different share selections that have been listed in the past.

So in essence what I do every other month is to follow up and comment on the original selections made in 2005 while also listing those shares that would be recommended now if you were constructing a new High Income Portfolio. The basic idea is to try to provide a regular update for the long-term management of an income-based equity portfolio.

The investment background

Although the STAR process is

essentially a "bottom up" approach to share selection, the overall trends in investment fashion will obviously affect both the absolute and relative returns on the original investment. This is especially the case over the short term. As explained in *The IRS Report* on 17th March – issue no. 268 – the basic STAR methodology is contrarian by nature. It usually selects shares in unfashionable sectors that have been overlooked by the market. Over the longer term this can be an advantage although taking a shorter term view, say less than 6 months, performance results may be disappointing. It sometimes takes some time for market sentiment to wake up to changes in the fundamental investment climate. Recent examples of these shifts include the dramatic upgrading of the second line FTSE 250 Index stocks over the past 18 months and the recent downgrading of the mining sector.

When I set up the High Income Portfolio in October 2005 I made a note of the values of the FTSE

All-Share Index, the FTSE 100 Index and the FTSE 250 Index at the start date. The relative movements since then dramatically illustrate the variations that can occur over time between sectors of the market. Over this period the shares of the largest 100 companies as measured by the FTSE 100 Index have risen by 21%. The FTSE All-Share Index has increased by 25% while the 250 second largest companies have soared by 54% as measured by the FTSE 250 Index.

Following up on this theme I was intrigued to look through the five-year performance of a friend's share portfolio that was set up in May 2002. It comprised the ten largest UK quoted companies at that time, such as AstraZeneca, HSBC and Vodafone. This "blue chip" basket of shares has managed to record average price gains of no more than 3.7% during the past five years compared with respective advances of just under 40% by the FTSE All-Share Index, over 20% by the FTSE 100 Index

Portfolio		The STAR High Yield selections						
Company	ICB Sector	EGR %	Holding	Purchase price p	Cost £	Yield %	Current price p	Value £
Findel	General Retailers	19	230	435	1,001	2.7	689	1,585
Greene King	Travel & Leisure	22	154	649	1,000	1.9	1,113	1,714
Legal & General	Life Insurance	16	892	112	999	3.5	157	1,400
Low & Bonar	Construction & Materials	34	691	143	989	3.1	142	981
Premier Foods	Food Producers	104	426	301	1,001	3.5	302	1,287
Prudential Corp.	Life Insurance	111	196	510	1,000	2.1	802	1,572
Smiths News	Support Services	1	305	0	0	2.8	152	464
Uniq	Food Producers	190	501	197	988	3.6	192	962
WH Smith Group	General Retailers	33	305	328	999	2.5	452	1,379
XP Power	Electronic & Electrical Equip.	24	263	380	999	3.6	498	1,310
Yell Group	Media	61	202	490	989	3.1	485	980
TOTALS		55			10,000	2.9		13,632

Data as at 8th May 2007. The High Income Portfolio is selected using the STAR share evaluation system developed by John Mulligan. John Mulligan has interests in Findel, Legal & General, Premier Foods and XP Power.

