Investment update

24 June 2010

Q&A with Philip Hunter

Philip Hunter, manager of the Old Mutual Asian Select Fund

Philip Hunter rejoined Old Mutual in September 2008 from US wealth manager Bessemer Trust, where he was a fund manager focusing on Asia. He previously worked within the Old Mutual group for 11 years, holding a variety of fund management and analytical roles and focusing on Asia-Pacific markets and the global financial sector. Prior to this he was an analyst at private client investment group Merchant Securities. Phil is a CFA Charterholder.

STANDARD &POOR'S AA FUND MANAGEMENT RATING

Philip Hunter, manager of the Old Mutual Asian Select Fund, considers recent activity in Asian markets.

What changes have you made to the portfolio recently?

Broadly we have continued the themes of the first half of the year. We've seen a recovery in economies across the Asian region, and while 2009 was about strong economic growth in a small number of countries like India and China, 2010 is seeing economic growth recoveries really broaden out across the region.

So we don't have to look at one or two countries for really strong economic growth, it can be found across the region which gives us the opportunity to broaden out our exposure. We have been adding to some of the smaller countries, like Indonesia, Malaysia, Singapore, in the second quarter of 2010.

Does investing into some of the smaller markets increase illiquidity risk?

Illiquidity is one of our primary concerns. Whenever we initiate a position in the portfolio, we look at average trading volumes, and our performance and risk team pay keen attention to this area. We are not running a small cap fund, so we do not invest in very small illiquid names, and therefore illiquidity is not a concern for our fund.

Will Asia avoid eurozone contagion?

From an economic perspective, I think so. Government balance sheets in Asia are very different from those in Europe. However, contagion may spread if some of the European fiscal consolidation affects demand for products that are exported from Asia to Europe. In addition, if the euro continues to devalue, that also could impact the export earnings of some Asian companies. And finally globalised risk appetite impacts Asian equities; any increase in risk aversion in developed economies feeds straight through to Asian markets.

Are Asian equities cheap?

Yes, given the recent downturn in the market because of risk aversion and concerns about sovereign debt in Europe, I would say that Asian equities are below fair value at current levels.

Are you concerned by rising interest rates in Malaysia, Australia and India?

Not at present. I think this is more a process of interest rate normalisation. Rates are starting from a very low level and monetary policy is still accommodative across the region. I think Australia is most advanced in its tightening, and interest rates there are probably really just getting back to a normal level.

What sectors do you favour?

We are still underweight banks where we see a risk of provisions having to rise, such as in China, where after really strong loan growth in 2009, we think there will be an increase in

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provisioning. The banking system in China is going through a process of raising fresh capital at the moment. In other parts of Asia, however, where economic growth is strong, there is an attractive environment for banks and in this recent downturn we have been able to increase our weights in the banking sector.

We see three positives for the banking sector, including a recovery in loan growth, stabilisation in lending margins, and a stabilisation in asset quality as the economic recovery plays out. So there is quite a good environment for banking in general across Asia, but where we think returns could be pressured or if we think that banks are going to have to provide for potential bad loans in the future, we'll be underweight.

What about individual stocks in your portfolio?

Samsung Electronics is one of our larger holdings, but it is not a large active weight. Although it is a large part of our benchmark, equally it is a company that we are happy to hold. There are three main businesses, the one we like most being the storage technology. They have a leading market share in NAND Flash and DRAM for computer memory. As the penetration of smart phones increases, and high definition cameras proliferate, there will be an increasing need for memory and Samsung is a leader in that technology and in managing the cost of manufacturing, so they are well positioned to continue their success.

The other two businesses are consumer electronics, particularly LCD TVs, which is a category that is still growing strongly at the moment; and finally the telephone business, where they have a good selection of smart phones in which we expect to see continuing volume growth.

What is your outlook for the remainder of the year?

Given the strength of the economic recovery that we've seen this year right across the Asian region, I think Asian companies are going to be in a very good position to deliver the earnings growth that's been forecast this year. Capex has been increasing more slowly than corporate cashflows, so dividend payments are quite well underpinned and leverage levels are low. So I would expect payout ratios to increase in the future.

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