Investment update

1 September 2011

Simon Murphy, manager of the Old Mutual UK Select Equity Fund

Simon Murphy has been the manager of the Old Mutual UK Select Equity Fund since he joined OMAM in March 2008. Prior to joining OMAM, Simon worked for almost 10 years at M&G Investments, spending the last three as the manager of the M&G UK Growth Fund. He is a qualified chartered accountant and a specialist in corporate taxation.

The view ahead

Equity markets have been swayed by fear in recent weeks. As we move through the current challenges we should see a return of economic growth and a more optimistic outlook

Growth has been slowing but you have held with your preference for economically sensitive stocks, why is that?

Growth has slowed over the last couple of quarters globally but it's our belief that this is very much a mid-cycle slowdown, precipitated by a number of factors. The terrible earthquake in Japan in the first quarter caused disruptions to global supply chains, directly impacting industrial production. More recently we have had concerns over sovereign debt, in the US as well as in the eurozone. The effect has been what we believe is a short term drag on global growth. As we start to work through these issues, and in particular as industrial production comes back in the second half, we ought to see global growth starting to accelerate again. And if that's the case, being exposed to high quality cyclical companies should be rewarding.

You're still strong on mining stocks, is that still one of the better ways to access global growth?

We have a long term belief in the mining sector on the basis that incremental demand is still robust in economies such as China and India, where industrialisation still has a long way to go. At the same time, supply remains tight and we're seeing production disappointments in copper, iron ore and other commodities. The supply/demand imbalance suggests the producing companies will maintain their ability to generate high prices and, as a result, high profits for shareholders. These are companies generally rated fairly lowly in the stock market, given that people are concerned about the longevity of the growth cycle. In my view, it has another couple of years at least to run and as a consequence I think the cashflow and profits of those companies are going to remain attractive to shareholders.

You're relatively light in your exposure to the oil majors – such Shell and BP – but you have a significant overweight with companies that supply their equipment. Why is that?

The investment case is not dissimilar to the mining sector. As a global economy we are struggling to obtain new oil resources as much as new mineral resources. What we are seeing is that the major oil producers are investing a lot of capital in trying to find new reserves, which are tending to be in difficult areas geographically, in deep water or very hostile environments. The companies that are best placed to benefit from that capital expenditure are the companies that supply the kit, which can be complicated and involve a significant input of proprietary technology.

Diversified financials are a key active position, the likes of SVG, Paragon, what's the story there?

What we have tried to do in our financial holdings is find interesting, fairly niche type businesses. We particularly like companies whose position strengthened as the credit crisis reduced their competition. Paragon is a good example. It's a buy-to-let lender, a market

Old Mutual Asset Managers (UK) Limited
2 Lambeth Hill
London, EC4P 4WR, UK

www.omam.co.uk
+44 (0)20 7332 7500

OLD MUTUAL ASSET MANAGERS

which most of the big banks have exited. Paragon has been in that market for many years and remains a market leader. It now has most of the market to itself and is able to lend on attractive terms.

You're cautious on UK domestic growth but you're sticking with your holding in ITV, why?

ITV is what I would class as one of my internal change stocks. It has had a host of headwinds over the last 10 years, from difficult regulation to the shift to pay-TV through cable and satellite. It has had to fight against that and cope with the loss of audience share. That seems to be stabilising and the regulatory environment seems to be improving. A new management team has been in place for nearly two years. I think they are capable of turning this into a more efficient, more productive business. They are changing the business model, expanding the production side, diversifying overseas and moving into online and paid-for distribution. This is a self-help story somewhat independent of the business cycle and I think there are a lot of good prospects going forward.

You mention Sky. BSkyB has been in the news a lot recently. Is it a buy or a hold?

We used to own BSkyB because we were attracted to the strength of the franchise. We sold at a good point, when the News International bid looked likely to succeed. Things have moved on since then and the shares have come under pressure. We are looking at it again as we do like the fundamentals.

What is your outlook on the market? Is now the time to be swayed by fear or greed?

The market has consistently rotated through fear and greed over the last couple of years. There are clearly some big economic issues that need to be resolved. In recent weeks investors have been in the sway of fear, but as we move through some of our current challenges, and as economic growth starts to pick up in the second half, then it will be right to be a bit more optimistic on the outlook for the markets.

Old Mutual Asset Managers (UK) Limited
2 Lambeth Hill
London, EC4P 4WR, UK

www.omam.co.uk
+44 (0)20 7332 7500

OLD MUTUAL ASSET MANAGERS