Investment update

24 June 2010

Stephen Snowden, manager of the Old Mutual Corporate Bond Fund

Stephen Snowden is a highly experienced fund manager who has specialised in corporate bonds for the last ten years. Earlier in his career he focused on equities, which gave him a strong grounding in company analysis, which is at the cornerstone of his investment process. Stephen combines top down analysis with bottom up stock selection, believing that selecting good bonds, rather than good companies, is the key to delivering returns for investors.

Stephen Snowden joined OMAM in 2004 and is the manager of the Old Mutual Corporate Bond Fund, as well as the bond element of the Old Mutual Extra Income Fund. He was previously Head of Retail Fixed Income at Aegon Asset Management where he managed the Aegon Extra Income Fund.

Stephen Snowden: market outlook

Stephen Snowden, manager of the Old Mutual Corporate Bond Fund, outlines his view on markets

Over the course of the past six months or so markets in general and the corporate bond market in particular, have been preoccupied with sovereign default risk, first in Dubai in December, then in Greece in January and February and most recently in the other 'PIIGS' markets of Portugal, Italy, Ireland and Spain in April and May. In between times, sovereign concerns have been put to one side as the focus has switched to the more positive factors of good company results and improving economic newsflow. This has resulted in a volatile market environment in which liquidity has periodically been limited. We have responded to this by adding to risk during periods of weakness and reducing risk as the market has recovered. This strategy has served us well this year.

We acknowledge that budget deficit reduction is a process rather than an event and will therefore take time, hence we expect similar market conditions to continue to prevail during the coming months. In the UK the budget deficit is considerable, with the latest official forecast suggesting £155 billion. However, this is an improvement on the estimate given by the previous chancellor, Alistair Darling, of £178 billion, and earlier expectations among City economists that the true number would be closer to £220 billion.

Despite the enormity of the deficit in the UK, we are not overly pessimistic about the gilt market, while on the other hand neither are we overtly bullish. Although there are plenty of gilts in issue, they are cheap, the yield curve is the steepest in the industrialised world and the term structure is very favourable - the UK has a history of issuing long dated government bonds and there is little refinancing risk. Finally, domestic ownership is high and therefore there is limited reliance on overseas investors.

The state of the UK's finances is such that we anticipate tighter fiscal policy going forward, although monetary policy will need to remain loose in order to stimulate growth. We have recently seen a rise in inflation, although this is largely attributable to base effects, given the changes to VAT and the sharp moves in fuel prices. With sterling stabilising of late, imported inflation is less of an issue; household consumption will come under pressure from higher taxation and government spending will also be constrained. Unemployment is also expected to rise, meaning less pressure on wage growth – the largest component of overall inflation. In imposing its strictures, the government will need to strike a balance between acting quickly enough to satisfy the markets and delaying long enough to avoid derailing economic growth.

An environment of stable, if unspectacular, economic growth combined with loose monetary policy should be conducive to further progress for corporate bonds. Furthermore, issuance remains modest as corporate balance sheets are being repaired faster than anticipated, while banks are lending again as corporate activity has increased. Against this backdrop we are following a theme of long term value, focusing on more cheaply valued areas such as banks and asset-backed securities, in preference to more fully valued sectors such as telecoms and utilities. At the same time we will continue to add value by taking shorter term tactical decisions – which, with our fund size, we are well-placed to be able to do - as we expect positive economic and corporate news to continue to vie with sovereign default fears over the coming months.

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

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

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

Important information: Past performance is no guarantee of future results. The value of an investment and the income from it can fall as well as rise and investors may not get back the amount originally invested. OMAM has no house market view and opinions expressed are the views of individual fund manager(s) as at the time of writing. These views may no longer be current and may have already been acted upon. Any underlying research or analysis has been procured by OMAM for its own purposes and may have been acted on by OMAM or an associate for its or their own purposes. OMAM is the appointed investment adviser for Old Mutual Fund Manager's in-house OEIC funds. Old Mutual Asset Managers is the trading name of Old Mutual Asset Managers (UK) Limited and Old Mutual Fund Managers Limited. Old Mutual Fund Managers Limited, 2 Lambeth Hill, London EC4V 4AD. Authorised and regulated by the Financial Services Authority. A member of the IMA. Old Mutual Asset Managers (UK) Limited, 2 Lambeth Hill, London EC4P 4WR. Authorised and regulated by the Financial Services Authority. Telephone calls may be recorded for security purposes and to improve customer service. U5224/06/10