

## Investment update

15 September 2011



**Ian Heslop, manager of the Old Mutual Global Equity Absolute Return Fund**

The fund is managed by OMAM's quantitative strategies team which is headed by Ian Heslop. Ian joined the team in May 2004 and has over 13 years investment experience (9 years quantitative investment experience), including OMAM and BGI.

The team includes specialists in portfolio construction, research and systems development. The investment process is designed to exploit market inefficiencies and is based on a proprietary multi factor return model. The process calculates a forecast return for each stock and the resulting portfolio is optimised in terms of risk, cost and return.

# Capturing positive returns

The fund's dynamic valuation strategy allows it to account for investor sentiment. This helps to support positive returns during market downturns

Absolute return funds have proven their worth in the financial crisis. From the peak of the UK equity market on 7 July to the trough on 10 August, the FTSE All-Share fell 17.5%. The IMA Absolute Return sector, by contrast, fell only 2.3%.

The Old Mutual Global Equity Absolute Return Fund, which was top of the sector in the period, returned 5.3%. For the three months to the end of August the fund returned 8.8%, compared to -1.68% for the sector and -9.42% for the All Share. Over 12 months to the end of August, the fund returned 19.3%, compared 2.6% for the sector and 7.1% for the All Share.

Old Mutual Global Equity Absolute Return Fund is highly diversified, typically holding around 300 stocks, drawn from a pool of around 3500 companies worldwide. As a market-neutral fund it has low to negative correlation to other asset classes – around 10% with global equities (significantly less to UK equities) and even lower in respect to bonds and commodities. This makes it a strong option for any portfolio needing diversification.

Market-neutral funds aim to significantly reduce market volatility, delivering pure alpha through stock selection and some degree of sector allocation. This is usually achieved by matching long and short positions. The Old Mutual Global Equity Absolute Return Fund, following this model, is typically structured to be half long and half short.

The fund has a targeted volatility of 6% a year, giving it an annual return target of cash plus 6%. In practice, since launch on 1 July 2009 to 31 August 2011, the fund had an average annualised volatility of only 4.9%, with a cumulative return over the same period of 14.7%.

The fund is managed using a systematic, dynamic investment approach, focused on highly liquid large and mid-cap global equities. The approach is focused on five key investment characteristics:

- **Valuation** – Does the current market share price reflect the company's intrinsic value, as expressed, for example, in its balance sheet?
- **Market Dynamics** – Does the macro environment support the business?
- **Sustainable Growth** – Is the business growing and can it continue to do so?
- **Analyst Sentiment** – What do professional equity analysts think of the shares?
- **Company Management** – Do they have a history of making good decisions?

In my view, an important element in the fund's outperformance is the fact that stock selection incorporates not only historic performance or current data and forecasts, but critical issues in the macro-economic environment. Taking both 'micro' and 'macro' factors into account, the fund is continually optimised to ensure it includes the shares we believe will outperform within the defined risk limits. As the performance to date demonstrates, it has been possible to outperform while keeping risk substantially below the target.

The period since the fund's launch has been one of extreme volatility. Following a sharp recovery in 2009, macro-economic data and political events have often been at odds with the strong earnings reported by companies. This has led to an environment often described in the phrase 'risk on, risk off', in which investors switch by the month or the week, and often by the day, from bullish to bearish and back again. It is in this difficult, unpredictable climate that the Old Mutual Global Equity Absolute Return Fund's dynamic valuation approach, which takes account of short-term measures as well as longer-term trends, has shown its strength.

For investors looking for positive absolute returns as much as for those seeking meaningful diversification, we believe the Old Mutual Global Equity Absolute Return Fund is a compelling proposition. Its track record shows it can add value in difficult conditions, and across all phases of the market cycle.

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### Old Mutual Asset Managers (UK) Limited

2 Lambeth Hill  
London, EC4P 4WR, UK

[www.omam.co.uk](http://www.omam.co.uk)

+44 (0)20 7332 7500



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