Investment update

25 October 2011

Christine Johnson, manager of the Old Mutual Dynamic Bond Fund

Christine Johnson joined OMAM in September 2010 from Halbis Capital Management (formerly HSBC Asset Management), where she was a senior fixed income fund manager, initially focusing on sterling credit before also managing global portfolios. She moved to Halbis from Investec Asset Management, which she joined as a high yield credit analyst, becoming a high yield fixed income fund manager a year later. She began her asset management career as a credit analyst at Royal & Sun Alliance Investment Management, having previously been a relationship manager at NatWest Bank. Christine has a BA in Economics from Manchester University.

Fundamentals are not driving the market

Uncertainty surrounding the eurozone, and the potential impact on global growth, is outweighing market fundamentals

The Old Mutual Dynamic Bond Fund had a pick-up in performance in the third quarter. What was behind that?

I think there's been three reasons. The first is that we correctly anticipated Operation Twist which the US Federal Reserve announced in the last month of the quarter. The second was that, in response to the eurozone and what that means for global growth, we cut our exposure to corporate bonds. Finally, on the currency side, we had positions in both yen and the US dollar, which were both positive relative to sterling, the base currency of the fund.

Markets seem to be mesmerised by the eurozone. Is there a way out of the crisis?

We don't know what the way out is. I don't think anybody does. One thing that's clear is that as time has gone on the situation has become more complicated, more politicised, possibly more entrenched. What originally was going to cost a few hundred billion is now looking like one or more trillion. Our response in the fund is to try to preserve flexibility. If and when a resolution comes we can decide if we want to take our hedges off, which will give us an immediate exposure to risk.

Is 2011 proving to be a rerun of 2008?

That's the question on everyone's lips at the moment. It is not a rerun of 2008 in that the drivers are different. But it is perceived that way due to the uncertainty and the apparent need for some sort of forced bank recapitalisation. We are very alive to the possibility of there being further downside for risk assets.

Have you cut back any direct and indirect exposure to Europe?

Over the last year we have withdrawn from direct exposure to the eurozone peripherals, either through sovereign bonds or from companies domiciled in those regions. One thing that came up early in our analysis was that French banks remain heavily exposed to Italian and Spanish sovereign debt. As a result, we cut right back on French bank exposure - that was a big change for us. Before, we'd been keen on the idea of national champions, that the French would always support their banking system. We changed our view when we saw how extreme the capital losses could be and the consequences that would have for bonds further down the capital structure.

Have you cut back your exposure to German banks?

They have much less exposure. Almost all of the German banks' exposure to peripheral Europe is concentrated in Commerzbank.

If yields on corporate bonds are high and companies have a lot of cash, is now a good time to be buying corporate bonds?

On any fundamental measure corporate bonds now offer very good value. If you look at the

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amount you stand to lose, even if you went through the worst period in history for credit, including the Great Depression, you are now being fairly compensated to own on corporate bonds. But we have to accept that we are in a period where fundamentals are not driving the market. For us, it's the asset allocation story rather than the fundamental story which is driving our positions.

Is there going to be a turning point for the markets?

We need something conclusive to come out in terms of Europe, and we need it sooner rather than later.

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