

## **SHINING A LIGHT ON..... M&G Optimal Income Fund**

### **Update....**

In our last review we highlighted the strength of the management team, the strong performance and the go anywhere approach of the strategy. One of the concerns we had on the fund was liquidity and this should be a consideration for investors.

In July 2015 it was reported by Citywire that the fund had seen £2.7 billion removed by investors from the fund over the second quarter. The fund however still has about £20 billion worth of assets. In this update we were looking for some guidance from the managers on how the fund might respond to a rising interest rate environment to help investors (and potential investors) decide whether this is the most appropriate fund to provide exposure to bonds going forward.

In the last review the manager was reducing exposure to High Yield bond and equities. This strategy remains. Although the fund can take up to 20% exposure to equities the manager feels that equities are overvalued compared to their fixed income alternatives and therefore the weighting is almost zero. Government bond holdings have also dipped to 10% for liquidity purposes, High Yield remains around 25% and Investment Grade over 60%.

The managers appear fairly optimistic about the markets. They discussed credit markets and don't feel there is a bubble. They feel companies are taking advantage of lower borrowing costs but they have the ability to meet those repayments. However, although the trend is below the average it is moving up and this is something they are monitoring. Where they see most value is in BBB US Investment Grade companies especially compared to Europe and the UK.

The fund has less exposure to interest rate risk as they think this is the best place to be at the moment. The challenge they feel at the moment is in volatility within the market and this brings additional risk.

Throughout the update the managers didn't touch on liquidity and with a fund of this size it has to be something that investors need to be aware of. The managers clearly have the experience and expertise to navigate this market but 10% of the fund has been withdrawn over the last three months and there is a danger that investors could withdraw more in coming months. Other bond managers are saying the market is not as liquid as it was in the past and therefore for big funds this could be a challenge.

The performance of the fund remains positive to flat and although the manager didn't want to predict future performance he did suggest low to mid-single digit returns gross of charges. This means after charges investors could expect 1 to 3% a year with increased risk and volatility. Of course nothing is guaranteed and investors will need to consider whether they are being adequately rewarded for the risk they need to take.

In summary the fund is managed by a talented team, and has an excellent track record. For those investors wanting exposure to bonds this might be considered a safe pair of hands. The projected performance is probably no different to other bond managers but the liquidity aspect of the fund is one to consider. The company have issued a statement saying it is not a problem but other bond managers feel the market is not as liquid as it has been in the past.

# LWM Consultants Ltd

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## Fund performance

Performance over the last five years is shown below:

	2010	2011	2012	2013	2014	2015
<b>M&amp;G Optimal Income Fund</b>	9.29%	6.59%	13.75%	7.79%	5.26%	-0.23%
<b>IA OE Global Bonds</b>	8.89%	2.44%	7.98%	-2.54%	4.87%	-2.00%

	1 Year	3 Years	5 Years	Since launch
<b>M&amp;G Optimal Income Fund</b>	1.06%	18.80%	41.81%	8.40% p.a.
<b>IA OE Global Bonds</b>	-0.01%	3.12%	14.18%	5.40% p.a.

*You should note that past performance is not a reliable indicator of future returns and the value of your investments can fall as well as rise. The total return reflects performance without sales charges or the effects of taxation, but is adjusted to reflect all on-going fund expenses and assumes reinvestment of dividends and capital gains. If adjusted for sales charges and the effects of taxation, the performance quoted would be reduced.*

*The source of information in this note has been provided by M&G Optimal Income and is correct as at August 2015. These are notes from meeting the fund manager or representative and should not be seen as a recommendation to purchase any fund mentioned. Any reference to shares is not a recommendation to buy or sell. Should you wish to make a decision based on these notes we cannot take responsibility for this and you should carry out your own research before making a decision.*