

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

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

In our last update one of the main concerns we raised on this fund was its size and the apparent lack of clarity from the managers on this. In this latest update much more clarity was provided which we will cover as well as positioning and comparisons of cash and fixed interest.

One question Richard was asked was what kept him awake at night and I thought this might give some insight as to whether the size of the fund featured in this. His answer was things that create trade barriers like wars, and not the size of the fund. We talked about the size of the fund and he explained that because the fund has the ability to invest across the fixed income spectrum and equities he has many opportunities still open to him.

Taking this further he went onto explain that there are advantages and disadvantages of having a large fund but it is about getting the balance right. There are some stocks they can't have but as he added they have been managing a fund of this size for some time and been able to deliver good performance.

On performance a comment was made about short term fixed interest vs cash and Richard reflected that performance had not been as strong recently but this isn't about a 12-month time frame, it is about the long term. The aim is about outperforming all fixed income sectors over the long term but there will be periods in the short term when this doesn't work. We dwelled on cash and he explained that the two just don't match.

As he explained cash in its purest form doesn't return you anything. To get any return you need to take risk, i.e. to get a positive return you have to put something in to get it. In the past people used cash in a particular way with banks offering 4 to 6% returns.

Although savers were willing to take this what they didn't understand was that the banks were taking risks to deliver those returns. The financial crisis showed the end result of this and going forward savers cannot expect banks to subsidise saving accounts, so returns will be lower even with interest rates going up.

The only way to get real returns over the long term is therefore investing in bonds, property and equities.

In part because the performance has dropped back and in part people's nervousness around bonds the fund has seen outflows but again Richard explained this is the nature of the fund. He is used to managing both large inflows and outflows. Outflows enable you to tidy the portfolio as he added.

Turning to positioning Richard sees the greatest value in BBB Investment Grade Bonds and this reflects a 50% + weighting to Investment Grade in the fund. He feels High Yield still offers opportunities but there is a deterioration in the market with the ratio between debt and earnings increasing and defaults gradually increasing, so within this field careful stock is needed. The fund has about 25% + exposure to High Yield with the other major weighting being Government Bonds.

Due to the current market the fund is positioned defensively with a duration (duration is useful in measuring a bond fund's sensitivity to changes in interest rates) of 2.4 years. So a 1-percentage-point rise in interest rates would lead to an estimated 2.4% decline in the share price

## LWM Consultants Ltd

---

In summary this update was less about the positioning and more about the liquidity and how the fund responds to this. For investors or potential investors this is really important because it gives them something to consider when looking to invest in this fund.

Additionally, it is worth considering that this fund has an excellent track record and M&G manage 16 funds in the fixed interest space with assets of £36 billion; you can argue that if anyone can respond to this market then they should be able to. The question remains whether size really is an important consideration or not and that is something individual investors will need to consider.

### Fund performance

Performance from 1 January 2010 to 30 September 2015.

	2010	2011	2012	2013	2014	2015
<b>M&amp;G Optimal Income I Fund</b>	9.83%	7.12%	14.31%	8.30%	5.78%	-1.52%
<b>IA OE Global Bonds</b>	8.89%	2.44%	7.98%	-2.54%	4.87%	-1.93%

1, 3, 5 and since launch performance:

	1 Year	3 Years	5 Years	Since launch
<b>M&amp;G Optimal Income I Fund</b>	-0.19%	16.32%	38.47%	107.96%
<b>IA OE Global Bonds</b>	-0.62%	2.56%	10.58%	59.03%

*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 October 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.*