

SHINING A LIGHT ON..... GLG TOTAL RETURN FUND

At a glance

Over the past ten plus years bonds have enjoyed a bull market; this is likely coming to an end. Investors can no longer expect the same level of returns and potentially there could be greater volatility. Volatility is what investors hate - this is the swing in the value of their investments, either in a positive or negative direction and for bond investors it's definitely not what they are after!

In 2008 Standard Life launched a Global Absolute Return Strategy Fund which effectively was a hedged portfolio of blended assets giving bond plus type returns with the same or lower levels of volatility. The aim was to drive down the volatility but deliver returns at around 70 to 80% of equities and target a return of cash plus 5% after charges. This strategy has been successful and the fund now has over £30 billion worth of assets.

The key to the fund is that it is not a bond fund but invests across a range of different asset classes (equities, bonds, currency etc). We use the fund in the fixed interest part of our portfolios as a main holding and we have since been looking for a second fund which we can blend into the fixed interest portfolios to work alongside this.

The GLG Total Return Fund was launched in July 2013 and follows a similar strategy to Standard Life. In essence the fund pulls together different strategies to create neutral market risk which means that it is not dependent on the rise and fall of the market to make money and more importantly not dependent on one asset class. For investors who have concerns about bonds this fund takes that risk away and equally for investors concerned about the volatility in equities it does the same.

Often these funds are seen as complex because of the different strategies and investors avoid them for this reason. This needs reverse thinking, the fund is a fund of ideas which draw down on the management's view of the world, and these are referred to as themes. They don't mind which asset class or classes have the potential to deliver on that theme but more around the impact on risk and reward within the portfolio.

For investors the potential downside is track record. This was only launched in July 2013 at a time of extreme market volatility and to date the strategy has not delivered positive returns. This review will consider their strategy further.

Who are the team behind the fund?

Standard Life has over 30 people working on their strategy and although they have seen people leave they have been able to cushion this because of the team. We have seen launches by the likes of Invesco but lack of depth within their team have raised concerns for us.

The lead fund manager for GLG is James Ind who we have met twice to discuss the strategy in detail. He joined GLG in 2013 and the fund was launched for him. Previous to this he worked at Russell Investments delivering absolute return strategies. Over a four year period he has outperformed his peer group and has a strong track record.

Although he is at the helm the team behind him is crucial. There are two aspects to this, firstly GLG are part of the Man Group who have Hedge Fund Expertise which we believe is vital to the

management of this type of strategy. And secondly the team itself consists of 16 people which, for a new fund, demonstrates support from within the company.

What is the story behind the investment?

The story behind this is very simple. Portfolio construction emphasises the need to have bonds as part of the portfolio primarily because they are seen as low risk and drive down volatility. Bond funds are moving away from a secular bull territory where strong returns were achieved to a more bearish territory where it will be harder to achieve positive returns.

This means investment managers will need to be creative to provide an element of “protection” to portfolios similar to bonds but deliver returns. Different strategies are now coming into the market and with the success of Standard Life; there are a number of “me to” strategies which on the whole have been unimpressive.

Fund highlights?

It is very hard to judge the performance of the fund over a short period of time. For example, when the Standard Life Fund was launched in 2008 it performed poorly but over the subsequent years it has achieved what it has set out to do.

We recently received an update from the manager on strategies which we will discuss however all strategies evolve around three pillars. Absolute value which looks at longer term time horizons (2 plus year) – this would look at something like Brazilian inflation debt. Relative value which looks at medium term horizons so less than two years plus – this might be for example short the Australian Dollar vs US Dollar and then opportunistic so for example short US equities. Shorting means you don't effectively own the asset and if it falls you make a profit, if it rises you make a loss.

With the Australian Dollar the over-valuation of the dollar has seen a 10% decline since October and therefore this has benefited the fund. An opportunistic investment in Nationwide's perpetual bond instrument has seen a 20% return since its launch with a coupon (payment) of 10.25%.

Emerging Markets is an example where the funds position has worsened as investors have fled to rising domestic stock markets. Investors see emerging markets as a homogenous group whereas selective markets are strong and offer significant discounts to developed market equivalents. This then opens up long-term opportunities but these trades have suffered due to the continued volatility within the region, as the dust settles and the stronger countries are recognised and rewarded this strategy will benefit but as of now we are in the falling tide sinking all boats phase!

Another position of the fund is short Japanese Government Bonds – the argument is that yields are around 0.66% and have the potential to rise to 2.5%. For the time being these are being kept artificially low and therefore the upside potential over the long term is significant.

The point is that to expect these strategies to work over a short period is the wrong way to look at the fund. The Standard Life Fund dropped over 5% in one month in 2013 however returned nearly 6% for the year. Strategies over the short term can go against the fund but because of the number of positions, different strategies will deliver at different times and this is what will deliver the positive returns in aggregate.

LWM Consultants Ltd

Fund performance

The table below shows performance since launch in 2013.

	1 month	3 month	6 months	Since launch
GLG Total Return	-1.68%	-1.57%	-3.11%	-3.16%

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.

Conclusion

The fund targets a return of cash plus 5% over a rolling three year period. It has entered the market at an extremely volatile time and although some strategies have delivered positive return to the portfolio as a whole value has deepened on others and until this corrects the performance will look poor.

We took a calculated risk with the Standard Life Fund and gradually increased our exposure to the fund and this has paid dividends. We believe that the track record of the manager and the team behind this have the potential to deliver an alternative strategy to Standard Life and therefore we would consider adding a proportion of our portfolios to this fund and then gradually increasing over the coming years as the management team demonstrate their ability to deliver returns.

The source of information in this note has been provided by GLG and is correct as at January 2014. 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. You should note that past performance is not a reliable indicator of future returns and the value of your investments can fall as well rise.