SHINING A LIGHT ON……
JP Morgan Income Opportunity Fund

Update….

In our initial review of this fund we concluded that the fund might appeal to investor's seeking a bond strategy with some downside protection. The fund doesn't guarantee a positive outcome however the fund manager aims to deliver this.

What concerns me about this strategy (and other similar strategies) is that it is fairly complex and only delivers a minimal return. The target is simply to beat cash. However on the flip side, if investors accept the complexity with the need to have exposure to bonds then this might be a fund to consider.

There were two areas we covered in the discussion firstly the state of the market for bonds and then how the fund is positioned.

We have been hearing more and more fund managers express concerns about the bond market but there are managers who claim this is over egged. Bill covered a number of things but three points really stuck out:

1. Interest Rates – in the US the Fed keeps telling the market it is on track to raise interest rates. However, the markets think the Fed is wrong and won't raise rates until the end of the year. If the Fed goes early (or when they say they will) then this will have a negative impact on bonds because the market has not priced this in. If rates go up when the markets are predicting then there will be little change because the market has already priced it in.

2. Risk – there are two reasons for investing in fixed income assets. Both are interlinked risk and volatility. Bill explained to get returns for investors you have to take more risk. At the moment there is no safe haven, it is about flipping coins and betting on what you think is right. The bond market is extremely volatile at the moment, for example this week (10 August 2015) US treasuries went up ten basis points one day and down the same the next day. Risk is about a permanent loss of capital, it is unlikely investing in a fund will mean investors will loss all their capital but for example US High Yield has fallen 3 to 4% over the last 15 months so in the short term capital paper losses may occur. Investors need to accept that fixed income is no longer a safe, risk free asset class.

3. Liquidity – some big fixed income fund managers carrying little cash in their funds claim there are no liquidity issues in the market. Bill disputes this. His fund is currently carrying over 40% in cash and he is trading daily. His view is that liquidity is a problem. Large trades are much harder to do and the market is not the same as it used to be. He added investors should not be panicking but liquidity is an issue, and it will get more challenging. For larger funds with minimal cash positions this will get worst.

Turning to the fund the question is how Bill can drive returns. Firstly it is worth remembering that he is not afraid to hold cash, so the fund is not fully invested. Currently the cash is at just over 40%. Secondly he will invest in areas that he doesn't necessarily like but where he sees opportunities.

There are three main areas he is focused on at the moment. Firstly lower rate credit. He feels that bad news is overpriced in this sector. The sector has seen two years of negative returns, defaults are overpriced and it is priced for recession. This provides opportunities to invest. On the question of recession, if a recession was due then not only would it be bad news for bonds but also equities and he just doesn't think that is the case.

Secondly he has a small holding in selective securitised real estate assets in the US and thirdly one-off opportunities. On one-off opportunities Bill highlighted Venezuelan short dated bonds. They are very cheap and priced for default. If they don't default over the next 12 months then the return will be over 60%. If it does he believes the downside is limited because of their reserves of gold and other assets.

In summary for investors looking for bond assets this is a fund to consider especially as returns are being squeezed and will get lower. Liquidity is an issue and funds with little liquidity will likely struggle going forward. However, it is worth noting that returns will be minimal in the short term and it is worth asking whether the added complexity equates to the likely returns.

Fund performance

Performance over the last five years is shown below:

	2010	**2011**	**2012**	**2013**	**2014**	**2015**
JPM Income Opportunities Fund	4.64%	-0.18%	6.71%	1.94%	-0.17%	0.38%
IA OE Money Market	0.32%	0.03%	0.49%	0.23%	0.29%	0.14%

	1 Year	3 Years	5 Years	Since launch
JPM Income Opportunities Fund	-0.28%	1.53% p.a.	2.21% p.a.	4.06% p.a.
IA OE Money Market	0.28%	0.29% p.a.	0.27% p.a.	0.58% p.a.

Based on A Dist Perf GBP Share Class launched February 2008, up to 31 July 2015.

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 JP Morgan 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.