

SHINING A LIGHT ON..... JP MORGAN INCOME OPPORTUNITY FUND

At a glance

It is becoming increasingly harder for investors to call a position on bonds. The argument is that the bull market that has been enjoyed, cannot continue and investors should be prepared for flat or negative returns moving forward. However, the market is not responding in a normalised fashion. In 2013 for example gilts were one of the worst performing asset classes, but against all market expectations they were one of the best in 2014.

Clearly investing in bonds is now much more complicated and volatile than ever before. But cautious investors continue to favour bonds to equities despite this uncertainty and volatility (or perhaps not realising it).

The options seem threefold – either an investor chooses a fixed interest sector they believe over the long term will do well (or a mixture of sectors), so high yield, government bond etc, they go to a strategic bond manager who takes that decision away from them or they go for an alternative strategy which may or may not include bonds.

The challenge with the third category is that the strategies can be complex, and often offer very little return. A fund which has been available since 2007 is the JP Morgan Income Opportunity Fund which aims to deliver positive returns above cash from a mixture of fixed income and currency markets. Returns over 1 year are flat but over three years it has returned 2.9% p.a. The share class of the fund we reviewed was launched in February 2008.

In this update we will touch on the manager and the fund. It is important to stress this is a complex strategy and might not appeal to all investors.

Who are the team behind the fund?

The fund is managed by Bill Eigen.

Bill is the head of the Absolute Return and Opportunistic Fixed Income Group at J.P. Morgan Asset Management. Prior to joining the firm in 2008, Bill headed Highbridge Capital Management's Fixed Income Group and spent 12 years at Fidelity Investments as an analyst and lead portfolio manager, where he managed approximately USD 10 billion across a number of multi-sector mutual funds and institutional products, including the USD 8 billion Fidelity Strategic Income Fund.

Bill began his career in 1990 as a Group Pension Investment consultant in the Retirement and Investment Services Group at CIGNA, where he completed his tenure as a Stable Value (GIC) Investment manager, focusing specifically on the development of dedicated fixed-income portfolio management strategies. He holds a B.S. in finance from the University of Rhode Island and is a CFA charterholder. Bill has served on the Board of Directors of the Boston Security Analysts Society and is a current member of its Education Board.

Fund highlights?

Interest rates must at some point rise, we just don't know when. A rise in rates will have a negative impact on the value of fixed income investments.

In the discussion with Bill the first thing he said was that things don't look good! He expects market rates to go lower before they go up, the problem is that they are close to zero and if they touch it then it makes it almost impossible to make money. He is also concerned that in this market investors are buying any yield, including negative yield and that is not good news.

The challenge is that, in the past, if equities go down then bonds were an area of protection almost operating in an opposite direction. Now with rates so low, if equities go down then fixed interest can no longer protect.

So if a bond manager is saying this then why invest in this strategy (or any bond strategy). Firstly the aim is to deliver an absolute return above the cash benchmark, this means that investors might get slightly higher returns than holding in cash and secondly the volatility of the fund is extremely low. For one year this is 0.63%, for three years it is 1.22% and five years 2.25% (equities tend to be 10% plus and bonds around the 5 to 8%).

Bill will take large cash positions if he cannot find suitable investors, so he will not invest for the sake of investing which again could appeal to investors. Cash has been reduced by 20% in recent months but the fund continues to hold around 46% in cash.

An area which he is looking to exploit is high yield and this accounts for the majority of his bond holdings. The sell-off in oil created opportunities and this accounted for some of the reduction in cash holdings. Other areas he likes are debt and currency markets using derivatives (which are a financial instrument).

The concern we have with this is that the strategy is fairly complex for a minimal return. However, it has to be weighed against an individual's desire to achieve above cash returns with minimal risk, and if this is the requirement then this may be a fund to consider.

In summary this is a well-managed fund and may appeal to investors seeking a bond strategy without some downside protection. It is a complex strategy and doesn't guarantee to achieve a positive outcome however that is the aim of the manager.

Fund performance

Performance since launch is shown below.

	2010	2011	2012	2013	2014	2015*	Since Launch (2008)
JPM Income Opportunity Fund	4.64%	-0.18%	6.71%	1.94%	-0.17%	0.04%	34.18%
IMA OE Money Market	0.32%	0.03%	0.49%	0.23%	0.29%	0.03%	4.32%

***1 January to 31 January 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.

Conclusion

This fund is designed for investors seeking fixed income investments, and low volatility with the ultimate aim to deliver above cash returns. Its performance has delivered as expected. Two things for investors to consider and it touches on a point that Bill made. He made the comment that it seems mad that investors are paying for a negative yield. With this investment you need to factor in two things – inflation and charges. These two things are important because if the fund is only going to deliver returns of between 0% and 2% going forward then inflation and charges are likely to turn this into a negative return. However this challenge remains with any of these types of investments.

The source of information in this note has been provided by JPMorgan and is correct as at February 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. 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.