

CUSTOMISED SOLUTIONS

EQUITIES AND THE CHANGING MOODS OF "MR MARKET"

One of the defining features of markets is change. As Benjamin Graham in the investment classic *The Intelligent Investor* said, the mood of "Mr Market" is prone to temperamental swings. These moods may range from a "risk on" to a "risk off" environment and may swing from a currency-weakening environment to a currency-strengthening environment. Each of these environments or moods represent distinct periods that can have significant impacts on equities and their related performance.

It is therefore advantageous to understand how, over meaningful periods of time, an investment strategy that underlies an equity fund performs under different market conditions or moods. The article below contrasts the performance of the (ASISA) South African EQ General Peer Group Median within the unit trust sector versus the Old Mutual Managed Alpha Equity Fund over the decade to 31 May 2017 under 6 distinct market environments measured monthly. The (ASISA) South African EQ General Peer Group Median may be viewed as a proxy for the average general equity strategy.

PERFORMANCE UNDER A RANGE OF MARKET MOODS

Over the last decade to 31 May 2017, "growth" strategies outperformed "value" strategies. This is highlighted in the performance table below

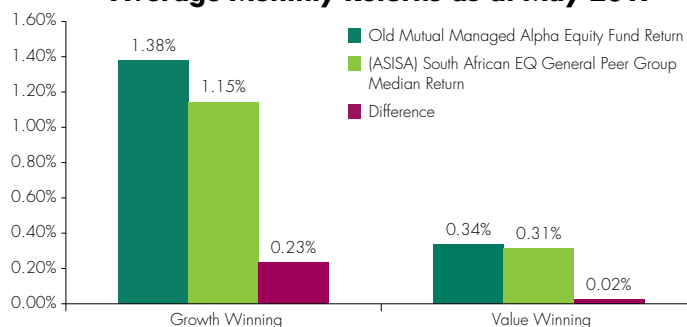
	FTSE/JSE Growth Index	FTSE/JSE Value Index
Annual Return	10.73%	7.23%
Standard Deviation (Risk)	16.7%	15.6%

Sources: Old Mutual Investment Group, Johannesburg Stock Exchange (JSE), Morningstar

GROWTH VS VALUE MARKET ENVIRONMENTS

How did the respective strategies perform on average when the FTSE/JSE Growth Index outperformed the FTSE/JSE Value Index? Alternatively, how did the strategies perform when the market environment changed to one where the FTSE/JSE Value Index outperformed the FTSE/JSE Growth Index? The Old Mutual Managed Alpha Equity Fund outperformed its peers in both "value" and "growth" market environments.

Average Monthly Returns as at May 2017



Sources: Old Mutual Investment Group, JSE, Morningstar

TABLE 2: Small Caps Outperformed Large Caps (At Lower Risk!)

	FTSE ALSI40 Index	FTSE Small Cap Index
Annual Return	9.27%	9.83%
Standard Deviation (Risk)	16.2%	12.8%

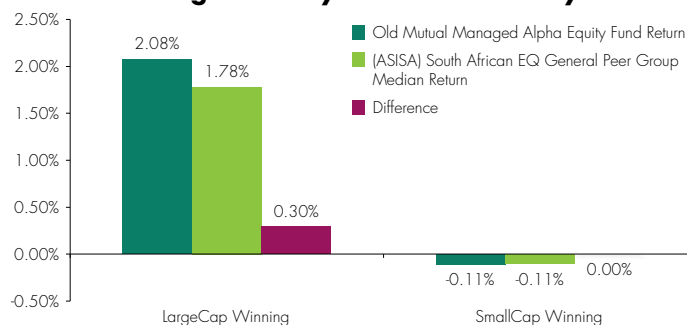
Sources: Old Mutual Investment Group, JSE, Morningstar

Small caps outperformed Large caps at significantly less risk. This highlights that higher return does not necessarily imply higher risk.

LARGE CAP VS SMALL CAP DRIVEN MARKETS

When Large caps outperformed Small caps, the Old Mutual Managed Alpha Equity Fund outperformed the (ASISA) South African EQ General Peer Group Median. Conversely, when Small caps outperformed Large caps, the Old Mutual Managed Alpha Equity Fund performed in line with the (ASISA) South African EQ General Peer Group Median.

Average Monthly Returns as at May 2017



Sources: Old Mutual Investment Group, JSE, Morningstar



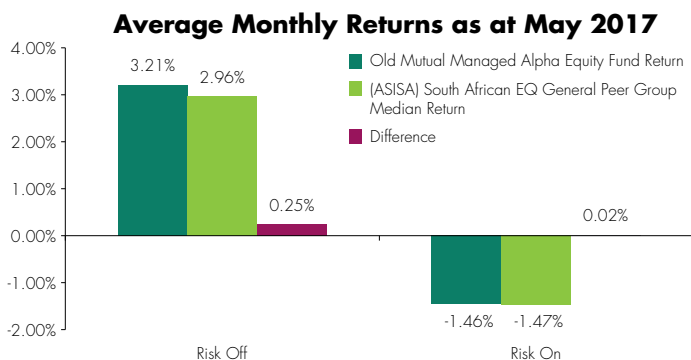
RISK ON/RISK OFF ENVIRONMENTS

“Risk on” or “Risk off” environments can be measured by the change in the South African Volatility Index (SAVI). This index measures the implied volatility in the Top 40 options and can be used as a measure of risk appetite of investors. Over the last decade, the SAVI has fallen by 3.4%, which implies investors have over the last decade been in a “risk on” or less risk averse mood. Equities typically tend to decline when the market is in a “risk off” mood and rise when the market is in a “risk on” mood.

	SAVI Top 40 Index
Annualised change in volatility	-3.40%
Annualised standard deviation	42.09%

Sources: Old Mutual Investment Group, JSE, Morningstar

Over this time period, the Old Mutual Managed Alpha Equity Fund outperformed the (ASISA) South African EQ General Peer Group Median in both risk off and risk on environments.



Sources: Old Mutual Investment Group, JSE, Morningstar

CONCLUSION

Over the last decade to end of May 2017, “Mr Market” has experienced a range of distinct moods. We compared the performance of the typical equity strategy (as proxied by the (ASISA) South African EQ General Peer Group Median) and the Old Mutual Managed Alpha Equity Fund in six market environments. The Old Mutual Managed Alpha Equity Fund outperformed the (ASISA) South African EQ General Peer Group Median in five of the six market environments analysed and tied in one. The question then, may rightly be: was this outperformance accidental or by design? The answer is by design. The Old Mutual Managed Alpha Equity Fund systematically identifies undervalued shares in a particular market mood. As the mood of the market changes, the nature of the shares selected changes accordingly and the strategy ensures the portfolio is positioned to gain from the change in mood of the market. This is the secret to the fund’s long-term success. As at 30 June 2017 the fund was top quartile for three, five, seven and 10 years.

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OLD MUTUAL
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