Nomura Global Dynamic Bond

Sterling Strategic Bond

Introduction

(Offshore)

The fund aims to deliver an attractive level of total return including a reasonable level of income through an unconstrained approach to investing in bond markets.

Click here to read the Nomura approach to ESG investing.

Why RSMR Rate this Fund

- Offers investors an unconstrained, absolute return approach to bond markets
- Aims for above average income through a strategy of hedging out risk whilst maintaining higher yielding assets
- The manager will look to deliver returns primarily through top-down themes and asset allocation positioning
- The fund management team are focussed only on this product but have access to wider Nomura resource if required
- Dynamically and actively managed
- Fund returns are likely to be driven by manager skill rather than bond market beta.

Fund Process

The fund's stated objective is to deliver an attractive level of total return, with the manager aiming to deliver both income and capital gain. The fund will look to maximise total returns while reducing volatility through allocation to a wide range of bond sectors, alongside an efficient derivative based hedging overlay. The investment universe includes developed market government bonds, emerging markets, investment grade and non-investment grade corporate bonds together with inflation linked bonds and related derivatives. The fund can also invest in equity put options to hedge out credit risk if these are attractively priced.

The fund features top-down investment themes and sector allocations, combined with bottom-up trade ideas and security selection with an efficient portfolio hedging mechanism using derivatives. The derivative overlay is used to mitigate specific shorter term risk to both credit and interest rates. There is dynamic adjustment of this overlay to control costs and maximise protection. Risk control is multi layered with VaR the primary measure, together with monitoring by both the named fund managers and an independent risk management team. The underlying portfolio is managed in US$ with a minimum of 80% hedged back to the base currency (although higher in practice). Emerging market exposure is limited to 30% and the fund can invest up to a third of its assets in high yield and can hold convertibles.

The fund manager believes that unconstrained fixed income investment allows for the greatest possible diversification and can also deliver a yield in excess of cash. The fund looks to deliver capital gains, but with less volatility than conventional bond indices. The manager and his team are solely focused on this strategy. Nomura have 130+ fixed income investment professionals across six global locations whose views and expertise can be accessed by the team if required. The overall direction of the fund is determined by the manager as is the decision where to allocate risk. There is then delegation to individuals in terms of how these investments are implemented. Around 70-80% of the ideas for the fund come from within the team with other Nomura personnel used to confirm ideas rather than generate them.

The purpose of the fund is to generate an attractive total return including a total yield which aims to be 3-5%. To deliver this there needs to be some risk exposure, but the fund has the ability to hedge out risks from binary events.

Asset allocation is actively managed and whilst cash physical positions can often be held for 2-3 years, hedging strategies are implemented to reduce risk positions in the funds rapidly, if deemed appropriate. The fund can and has used equity put options to protect against a fall in risk appetite and hedge out credit risk when the pricing of volatility has made these attractive on a risk/reward basis.

The manager employs specialists on his team to provide the bottom-up work to match the themes and opportunities he uncovers including specialists in convertible bonds, credit, and derivatives.

The process also looks to deliver some capital upside to investors over the longer term. The overriding driver of performance is understanding the big picture and positioning the fund accordingly, with top-down research complemented by bottom-up security selection. Use of hedging strategies allows the fund to actively steer itself through short term market risks and themes. Top-down research looks at interest rates and the credit cycle, as well as other economic and corporate fundamentals together with using the in-house credit research findings. The manager will also look for longer term market themes and shorter-term opportunities which in some cases could be described as shorter-term special situations within, for example, emerging markets or unsubordinated debt of financials. The manager looks at valuations and relative value when deciding the overall level of appropriate risk exposure for the fund.

The primary driver of returns will be top down factors after the team has identified areas of the market where attractive returns can be expected either through capital appreciation or carry. The fund will also look to capitalise on shorter term opportunities through market mispricing. Hedging strategies are used to remove risks from potentially three areas: spreads, break evens or rates. When constructing the fund the team look for a balance of risks. All hedging contracts are simple and liquid and currency risk is in practice at least 90% hedged away using currency forwards and options. Duration and yield curve exposure can be hedged using a combination of bond futures, options and interest rate swaps. Using options allows the fund to control the costs of hedging strategies. The fund aims to add value from asset allocation, interest rate directionality and relative value trades.

Evaluation

The returns from this completely unconstrained fund will be driven by manager skill more than the underlying returns of bond markets. The fund may have more credit exposure at times than some within the peer group, depending on the manager's top-down views. The fund is not managed by way of comparison in terms of asset mix with any bond indices or funds in the peer group/sector.

Application

This fund is suitable for investors wanting an unconstrained approach to bond markets with a fund which makes no reference to the composition of bond market indices. For many investors it would be best used as a satellite holding but could be used as a core offering for investors who wanted a bond fund taking an absolute rather than a relative approach to returns and seeking above average levels of income.

Our Opinion

This is an unconstrained fund where the primary driver of return will be top down views and positioning. The manager has an individualistic and distinctive style of unconstrained bond investing and has built a specialist team for the management of the fund. It is a fund with no benchmark, is totally unconstrained and looks to deliver a relatively high level of income. The manager has devised a strategy which delivers this income and potentially some capital gains using strategies to hedge out risk asset exposure whilst maintaining the underlying cash holdings delivering the yield. The fund has at times hedged out credit risk through equity put options to achieve this, with the manager arguing this is more efficient, liquid and cost effective than the traditional methods of selling cash bonds or buying CDS protection.

Fund positioning reflects the manager's top-down views which include both longer-term thematic positions, together with shorter-term opportunities which might be in selective emerging market local currency debt, or unsubordinated financials.

While the fund relies heavily on the considerable flare of the manager, he and his team are only running one strategy at Nomura, so the fund is the sole focus of their attention and efforts. Throughout his career the manager has demonstrated he is an able and talented manager prepared to think outside the box and this fund is a useful satellite holding within the sector and has potential to deliver returns with a low correlation both to the sector and fixed interest indices.