



Geof Marshall
*Vice-President, Portfolio Management and
Portfolio Manager, Signature Global Advisors*

Spotlight on Geof Marshall

The new Signature High Yield Bond Fund and Signature High Yield Bond Corporate Class have what no other high-yield fund in Canada has – the expertise of the 30 member Signature Global Advisors team.

Geof Marshall, Vice-President at Signature and Lead Portfolio Manager of the new fund, says he has just one rule, “Don’t lose money. If you underperform in an up market it means you didn’t take enough risk – and I can live with that – but if you’re losing money it means you’re wrong, and the two things I hate the most are losing money and being wrong.”

In 2006, Geof joined Signature from Manulife Financial, where he was also a portfolio manager. Since he started, the

high-yield corporate bond portfolio – which makes up part of the Signature Corporate Bond, Signature High Income, Signature Diversified Yield and Signature Income & Growth funds – has grown to \$5 billion from \$1.2 billion. Signature has one of the largest high-yield portfolios in Canada.

As Geof explains, “Ten years ago, high-yield bonds would have been considered a niche asset class – they still had the stigma of the high-flying 1980s and investors were skeptical. Since then, the high-yield bond market has grown dramatically and matured. I think Canadian advisors and investors are gradually educating themselves and embracing high yield because they realize the benefits.”

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High-yield bonds have historically been slightly negatively correlated to both short and long-term U.S. interest rates and highly correlated to stocks. Investors have received about 90% of the return of equities with 45% of the volatility. Since 1980, the Sharpe ratio for high yield has been double that of equities – which means that it is a more efficient asset class.

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“In the past,” Geof says, “high yield has been seen as an asset class to trade or a place to wait while equity markets recover, but the Sharpe ratio suggests it’s actually more of a core portfolio strategy. For example, if you have a portfolio that is 60% stocks and 40% investment-grade bonds, and take 5% from the equity portion and 5% from the fixed-income and allocate it to high-yield bonds, it will lessen the portfolio’s exposure to both interest rate risk and some equity volatility.”

According to Geof, high-yield bonds provide investors with the best of both worlds. “As we all know, interest rates have been at historical lows for some time. We’ve had a 30-year bull market in interest rates, but there’s going to be a time when interest rates start rising and investors start experiencing negative returns on bonds. That’s when they are going to want something that is levered to economic growth and trades on a price basis, like the high-yield bonds, not on a spread basis, like investment-grade bonds.”

As with equities, individual fundamental security analysis is crucial in the high-yield bond sector. In addition to the dedicated high-yield team – which includes Kevin McSweeney and Brad Benson – Geof draws on the expertise of the entire Signature lineup of portfolio managers and analysts, including a team of global equity sector specialists, other income asset class specialists and global strategists. In addition, his default forecast, which is one of the primary drivers of high-yield returns, is based on Signature’s macro view of the economy.

Describing Signature’s approach to high yield, Geof has a motto: “Lend like a banker, position like a portfolio manager and execute like a trader.”

“Lend like a banker” means doing intense and ongoing due diligence on the issuers, management teams, sectors, the company’s products and their competitive advantages on the assumption that if trading liquidity is lost, Signature would be comfortable holding the bond until maturity.

“Position like a portfolio manager” means incorporating the Signature macro view on rates, sectors, and commodities, and working with the Signature team to be in right names and sectors at the correct time.

“Execute like a trader” means paying attention to the trading data and the technical indicators. Geof says, “In a market where one point bid/ask spreads are the norm, having the sell-side traders on our side helps ensure the best execution which can really drive performance.”

“Altogether, that means focusing on the four Cs of credit investing – capacity to repay, character of management and the equity holders, covenants and collateral.”

On the risk management side, Geof says, “Liquidity and credit risk are the two most important factors in assessing a holding. Liquidity is a real risk because high yield is not always the most liquid asset class. That’s one of the reasons we have higher weights in our higher-quality names and smaller weights in riskier names.”

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Credit risk is the primary risk that Geof is managing. “Generally, the bonds you avoid are more important than the positions in your portfolio. You win big by not owning the companies that default. In high yield, the risk/return profile is asymmetrical, so it’s much easier to lose 100 cents on the dollar than it is to double your money.”

Historically, the default rate for the market has averaged 4%, but the Signature high-yield portfolio has experienced rates much lower than that.

Unlike other bonds, duration is less important because it's not an asset class that has a positive correlation to rates. Also, high-yield bonds have a much shorter duration than investment-grade bonds and many are called early, thereby offering less sensitivity to interest rates.

Signature High Yield Bond is currently fully invested in high-yield bonds, but the mandate is flexible enough to allow it to invest in U.S. Treasuries and Government of Canada bonds when there is a need to be defensive and secured leveraged loans when interest rates are rising. The average credit quality of the fund is BB low, as it is for the high-yield holdings in other Signature income funds. In total, there are about 150 holdings in the portfolio, representing 125 companies, but Geof says that will grow over time.

The fund is 60% invested in the U.S. because at US\$1 trillion, it's the largest high-yield market in the world. In comparison, the Canadian market is about C\$7 billion, but expected to grow by C\$3-\$5 billion per year over the next five years. Canadian holdings are 28%. While Geof has 5% invested in Europe, he says the high-yield market isn't very developed. The remainder of the fund is invested in Australia, Mexico and Brazil. Nearly all of the holdings are in denominated in U.S. dollars and the fund is managed with active currency hedging.

The monthly payout of the trust version of the fund is 5.5 cents per unit for an annual targeted yield of 6.6%. Since there is a forward contract on the fund, distributions are classified as tax-efficient capital gains or return of capital.

"Currently," he says, "the high-yield market is fairly valued. It's priced at 95¢ on the dollar and yielding 8.6%. If we go into recession in 2012, which is unlikely, I don't think high-yield default rates will spike dramatically. The default rate is about 2% now, but it could rise to 3%-5% if the economy slows. Historically, during recessions it has been 8% or higher."

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"Another factor is that high yield can perform well on a relative basis in a low growth, low interest rate environment, which is where the economy is likely to be over the next five years. Below that, defaults become a problem and above that you probably want to own equities."

Geof says the biggest benefit of the fund is diversification. "This is an asset class you can't do yourself. With high-yield bonds, you need to own a diversified portfolio, and actively manage the liquidity and credit risks and currency. Signature High Yield Bond gives you all that – and you also benefit from the expertise of the Signature team."

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at the Canadian Investment Awards

CI Investments was selected as the recipient of two 2011 Morningstar Canadian Investment Awards, which recognize superior investment products and services. Over the past decade, CI and its portfolio managers have won 33 Canadian Investment Awards.



Portfolio Series[™]

Portfolio Series was named **Best Fund of Funds**. Portfolio Series is a managed solution that also offers an IPO, IPS and enhanced reporting, along with a strong track record. The Portfolio Series funds hold over \$4 billion in assets and are managed by CI Investment Consulting.

Signature[®]
GLOBAL ADVISORS

Signature High Income Fund was chosen **Best Global Balanced Fund**. The fund, managed by the Signature Global Advisors team, is a three-time Canadian Investment Award winner and a three-time winner of Lipper Fund Awards. It invests in a diversified portfolio of high-yielding securities.

For more information see: www.ci.com