OMNIS INVESTMENT UPDATE: GREECE

JULY 2015

Prior to the financial crisis, the Greek economy enjoyed a period of rapid expansion. However, growth was fuelled largely by borrowing and, subsequently, the burden of accumulated debt has proved too severe for the Greek economy. This has led Greece's principal creditors - the European Central Bank (ECB), the European Commission and the International Monetary Fund (IMF) - to insist that any economic assistance is delivered in return for efforts to reduce Greece's debt burden, primarily through public sector austerity.

However, Greek economic output is a quarter lower than its pre-crisis peak while youth unemployment in some parts of the country is as high as 60%. The creditors' demands for the imposition of further economic hardship have, therefore, not been favourably received by the Greek population. This stance was further clarified by the outcome of the snap referendum held on Sunday 5 July. While discussions have so far failed to find an agreeable solution, it's clear that full-scale default and Greece's exit from the eurozone is in neither party's interest. Further attempts to achieve a diplomatic solution are therefore expected.

Though Greece is only a small component of the global economy, the potential political, economic and financial market implications of these attempts deserve consideration. Each of the investment managers responsible for day-to-day decision making in the Omnis funds has given significant thought to the consequences of events in Greece. A summary of their views and portfolio positioning is provided below.

NEWTON INVESTMENT MANAGEMENT

Omnis Multi-Asset Income Fund

Nick Clay, co-manager of the Omnis Multi-Asset Income Fund, sets out Newton's position:

"(We have) held the view for some time now that the Greeks cannot pay back the debt and that they will default. Our central view remains that a compromise will be found, writing off the debt (or extending it so far out that it is in effect a default) but retaining Greece within the eurozone. The recent "no" vote simply strengthens the Greek's hand in this matter. This is a reminder that we are investing in a fragile backdrop – contrary to popular belief – and therefore we remain focused upon businesses and assets which can weather the volatility. Retaining a stable income in this environment is key, so that such volatility can ultimately be used to our advantage".

COLUMBIA THREADNEEDLE ASSET MANAGEMENT

Omnis UK Bond Fund & Omnis Managed Funds

Recognising "the risks of Greece's departure from the eurozone as underpriced", Colombia Threadneedle has adopted a defensive positioning across the Omnis portfolios. However, Toby Nangle, Deputy Manager of the Omnis Managed funds, admits:

"From a market perspective, it is a challenge to understand the prospective channels for contagion. Greek assets are not widely held across the private sector following the efforts in 2011 by European states to transfer privately held Greek debt in publicly held Greek debt. Those channels of contagion that persist are political, and sentiment based. Both are hard to analyse."

While the Omnis Managed Adventurous and Omnis Managed Balanced funds do contain some direct exposure to Greece (via a single holding in the Threadneedle Global Emerging Markets fund), in both cases this represents less than 0.03% of the fund's assets. The UK Bond Fund contains no direct exposure to Greece.

OCTOPUS INVESTMENTS

Omnis Alternative Strategies Fund & Omnis Multi-Manager Funds

Colin Lunnon, Co-Manager of the Omnis Alternative Strategies and Omnis-Multi-Manager funds, expects an "ongoing flurry of meetings between the key players" and notes that "although the latest news has added to uncertainty, there remains a lot of political will to resolve current differences".

Turning to the Omnis funds, Colin explains that asset allocations have been actively managed to mitigate risk and to take advantage of opportunities presented by the volatility:

"We took advantage of highs in European stock markets earlier in the year, selling holdings that allowed us to capture profits. In the last few weeks, however, we have begun slowly adding again to a broad spread of holdings as opportunities have arisen. However, as the crisis unfolds it is hard to determine which assets may benefit and which may be disadvantaged, so we continue to maintain a balanced position. It needs to be recognized that if terms over Greece's debt can be agreed amongst the various parties, current market prices offer compelling value. We therefore aim to stick to a globally diversified portfolio invested across numerous asset classes."

SCHRODER INVESTMENT MANAGEMENT

Omnis UK Equity Fund & Omnis Global Bond Fund

Neither the Omnis UK Equity Fund nor the Omnis Global Bond Fund have any direct exposure to Greece. Furthermore, in the latter, exposure to Southern European sovereign bonds is limited to a small number of holdings in Spanish and Italian government bonds. Schroders comments:

"Whilst an exit is not a certainty at this point, the probability has significantly increased. However, the consequence of a Greek default will have a dramatic effect on Greece but a limited economic bearing on the wider eurozone."

While financial markets may witness increased volatility, Schroders believes reasonable valuations offer some downside protection for UK equities. Meanwhile, the ECB is committed to continuing the purchase of bonds through its quantitative easing programme, thereby providing a safety net for holders of European sovereign debt and ensuring "bond market contagion is very limited".

THOMAS WHITE INTERNATIONAL

Omnis Developed Markets (Ex US, Ex UK) Equity Fund

The Omnis Developed Markets (Ex-US, Ex-UK) Equity Fund contains no direct exposure to Greece. Nonetheless, the fund manager continues to monitor the situation, focusing on potential contagion effects in currency markets, and in countries like Italy and Spain where the Fund is invested in two of the highest quality banks for those respective markets. Thomas White International also notes that the fund benefits from exposure across Asia and North America, which are less directly impacted by events in Greece.

JUPITER ASSET MANAGEMENT

Omnis Emerging Markets Fund

The global equity index provider, MSCI, has classified Greece as an emerging market since November 2013. Ross Teverson, manager of the Omnis Emerging Markets Equity fund, holds no direct exposure to Greece but believes "the outcome of the Greek referendum is likely to have a short-term impact on sentiment towards risky assets, including emerging market equities". Jupiter notes, however, that Greek equities make up a negligible proportion of the global emerging equity markets. Consequently, beyond increased market volatility in the short-term, events in Greece are likely to have little direct impact on the asset class.

THE BOSTON COMPANY ASSET MANAGEMENT

Omnis US Equity Fund

As expected, the Omnis US Equity Fund has no direct exposure to Greece. However, the fund manager remains acutely aware of the potential downstream effects of the Greek crisis. The Boston Company states:
"(We are) carefully monitoring the Greek situation and importantly, the economic and financial channels of contagion from Greece to the rest of the world in the case of an impasse regarding their debt and potential Greek exit from the EU".
One potential channel for contagion is the US dollar-euro exchange rate, and The Boston Company is giving much thought to the potential impact of currency market fluctuations on company earnings.

GRAPHENE MODEL PORTFOLIOS

The Graphene Model Portfolios comprise the seven funds of the Omnis Portfolio ICVC, appropriately weighted to suit the risk appetite of cautious, balanced and adventurous investors. The asset allocation weightings are designed to be appropriate over the long-term and, as such, are not flexed in response to short-term market volatility - such as that currently being sparked by events in Greece. While the asset allocation of the Model Portfolios remains constant, as the above comments demonstrate, the risks entailed by shorter-term market events are at the forefront of the fund managers' minds. Their active management of the Omnis funds ensures shorter-term risks within the portfolios are managed and, where appropriate, mitigated at the fund level.