



LAURA PEDERSEN / NATIONAL POST

Los Angeles-based bond guru Jeffrey Gundlach prefers emerging-market debt to corporate junk bonds. He's starting a new fund for CIBC Asset Management, the Renaissance Flexible Yield Fund.

THE NEW BOND KING COMES TO CANADA

JONATHAN RATNER

Bond guru Jeffrey Gundlach isn't shy about voicing his opinion on everything from Donald Trump to Puerto Rican bonds. But he's perhaps best known for accurately predicting several market events, most recently, the dramatic plunge in oil prices and before that, the decline in U.S. treasury yields.

Gundlach, who passed up on the opportunity to give Bill Gross a job after he left PIMCO in late 2014, is now considered by many to be the new Bond King. And he's coming to Canada. More specifically, he's managing a new fund from CIBC Asset Management: the Renaissance Flexible Yield Fund.

Run out of DoubleLine Capital's Los Angeles offices, which

Gundlach founded in 2009, the fund is designed to provide high-yield-like returns, but with lower volatility through the use of tactical allocation, active duration management and diversified sources of yield.

Gundlach visited Toronto recently and spoke with Financial Post reporter Jonathan Ratner. This is an edited version of their conversation.

Q *What are your views on interest rates right now?*

A I think the complacency about interest rates is getting close to where it was in 2012, where people are starting to say they simply can't go higher.

The argument for U.S. bonds versus other developed nations

government bonds has basically been a relative value argument. With Japan at negative 14 basis points, with Germany down near zero, and many countries in Europe negative at the short end, the U.S. looks like a high rate.

Q *Are central banks on the right track?*

A I think the evidence is piling up that there is something perverse about negative interest rates — that they deliver an outcome exactly the opposite of what they seem designed to produce. Europe went negative back in the first quarter of 2015, and what's happened since then? The euro has got stronger and their stock markets have underperformed tremendously.

Then Japan tries negative earlier this year, and it's like someone rang a bell. The yen started rallying instantaneously and significantly.

Q *Do you think their attitudes will change?*

A I'm waiting for the moment when central banks decide what they're doing isn't working. I think they'll go more negative first, which almost seems like the definition of insanity.

Negative interest rates to fight deflation is a very strange thing, because negative interest rates are deflation. Your money is going away, it's shrinking.

You're actually fighting deflation with deflation, which seems like a very unusual thing to expect to work.

Q *Is the next step even more unconventional policy?*

A Ben Bernanke said we will never have deflation because we can drop money out of helicopters. It's happening.

The United States did it twice, and in Sweden, everybody gets the equivalent of US\$600 now per year, even the billionaires.

There are serious people calling for 5,000 euros (\$7,100) to be given to every single European citizen. And if that doesn't work, do it again.

I don't think there is anything left in the monetary tool kit, so maybe if we go to the stipend world, that could be the endgame.

Q *What is your opinion of the Fed in particular?*

A The Fed has capitulated. One of the most beneficial investment themes for the past 18 months was the Fed is out to lunch, and completely incapable of executing on the rate hikes that they claim to be planning. Those rate hikes were 300 basis points by the end of 2018 — 100 this year, and so on. That's just absurd, there is just no way they'd be able to execute on that type of a program. So fading the Fed — that they would capitulate — was a good idea.

It finally happened over a two-week period in March, when the Fed basically admitted that it can't raise rates four times this year, so it would make two its base-case guess. So I think it is going to be a rolling two — when we get to June, they'll say they

can't raise rates, so it will be two by next June. They'll just keep pushing it forward.

Q *How does the inflation outlook impact things?*

A When I started in this business over 30 years ago, everybody was scarred by inflation. Everybody decided inflation was really bad and we had to get rid of it.

Now we kind of have just the opposite, people are worried that deflation is unstoppable.

There is reason to fear that when you look at the indebtedness in virtually every country, a deflationary cycle would turn into chaos — failure of the banking system, and a debt repudiation cycle.

So people are now incrementally coming to believe that inflation is good. Certainly the central banks think inflation is good. Not high inflation, but we live in a funny world.

Q *How so?*

A They way we define price stability globally is two per cent. Since when is two-per-cent inflation price stability? It's gradual price instability, but it's price instability. When you think about it, over the course of a generation and a half, you lose half of your purchasing power. Over the course of a lifetime, you lose 75 per cent of your purchasing power. It's not price stability, but in an indebted world, you create new nomenclature.

Q *How has this impacted your positioning?*

A We're more likely to own treasury bonds now than we were a couple of years ago, because back then, two- or three-year treasury bonds yielded very close to zero. There was no real chance from that segment of the portfolio of delivering anything resembling LIBOR plus two or three per cent.

Q *Are you investing outside of the U.S.?*

A Since the end of 2013, our emphasis has really been to favour emerging-market risk over high-yield bond risk. There have been fits and starts, but I think for

the full period, you've been better off in emerging-market debt than you have been in corporate junk bonds.

Q *What are some other areas you like?*

A We also own securitized credit,

which seems to be much safer relative to corporate credit, because non-guaranteed mortgage debt has no exposure to weak commodity prices. If gasoline prices fall, I suppose it makes the payback on mortgages more likely, because the consumer has a little bit more money. The real estate market has been pretty steady, so we've taken those types of credits instead.

Q *Tell us a little about the strategy on the CIBC fund.*

A It's a very flexible, absolute-return type of concept that we intentionally named "other than unconstrained."

In the U.S., a category has developed in the past five years called "unconstrained bond funds." I think many of them are dangerous, and a great many have actually been negative in terms of return — some for three years in a row.

They take credit risk and then some short treasury bonds in order to take the interest rate risk away. The problem with that is you're long risk, but you're also short safety. Try selling that to your grandmother.

We are also a little bit longer-term focused. We're probably among the lowest-turnover fixed-income investors of our size in the U.S., and rarely have to sell things.

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