



# Total Return Funds Through Active Management



## 1. **Top Down** - The Indispensable Macro Picture

- Last Ten Years
- Next Ten Years

## 2. **Top Down** - How to create **protected absolute returns** next 5-10 years?

## 3. **Bottom-Up** - How to create **protected absolute returns** next 5-10 years?



## Three Imbalances That Affected Returns

- Asian Accumulation of Reserves
- US Debt Load
- European Debt Load



- **Asian Accumulation of Reserves**
  - FX policy drove imbalances
    - Undervalued currencies since Asian crisis meant Asia earned disproportionate level of global output.



## Asian Accumulation of Reserves

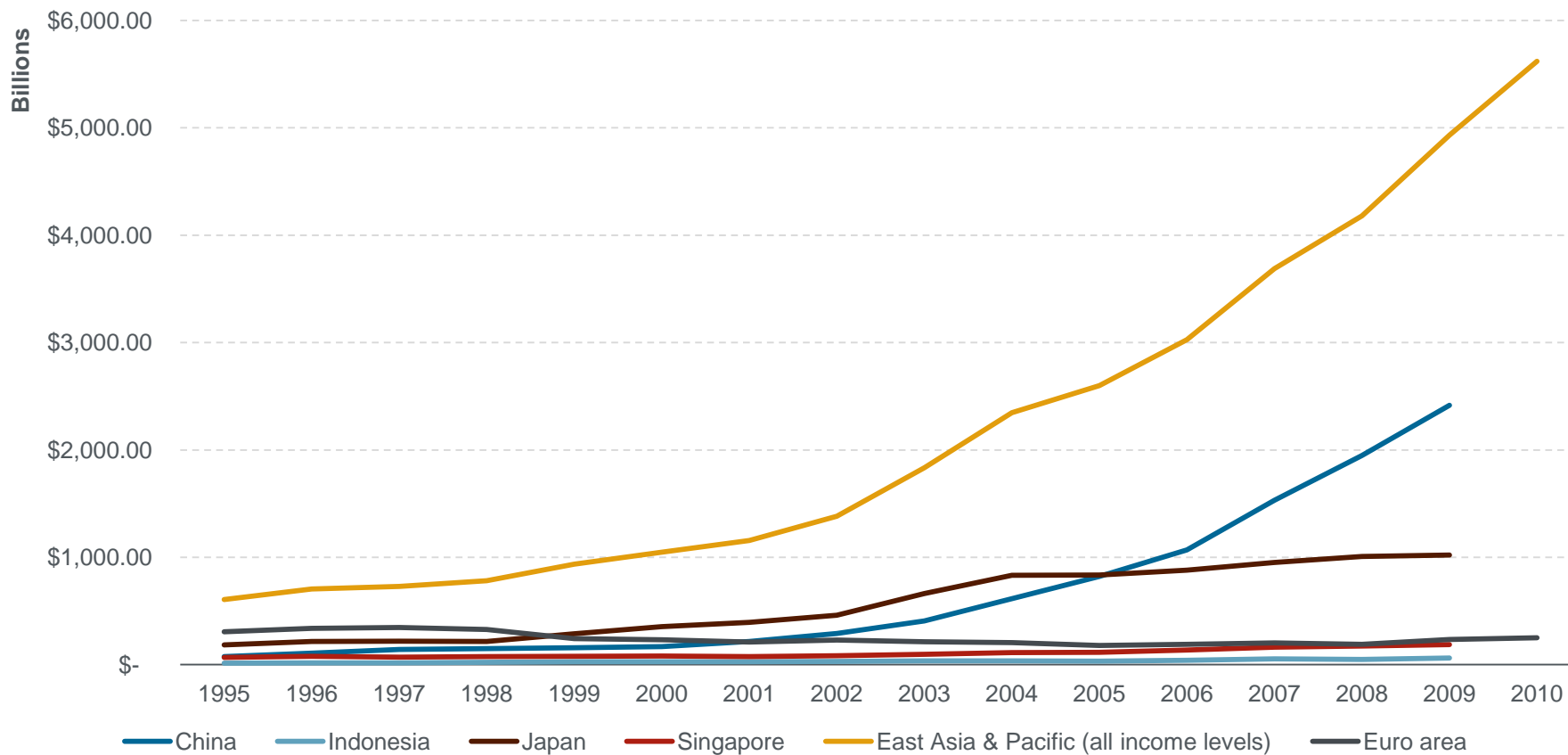


Chart Source: World Bank



## Asian Accumulation of Reserves: Current Account Balances

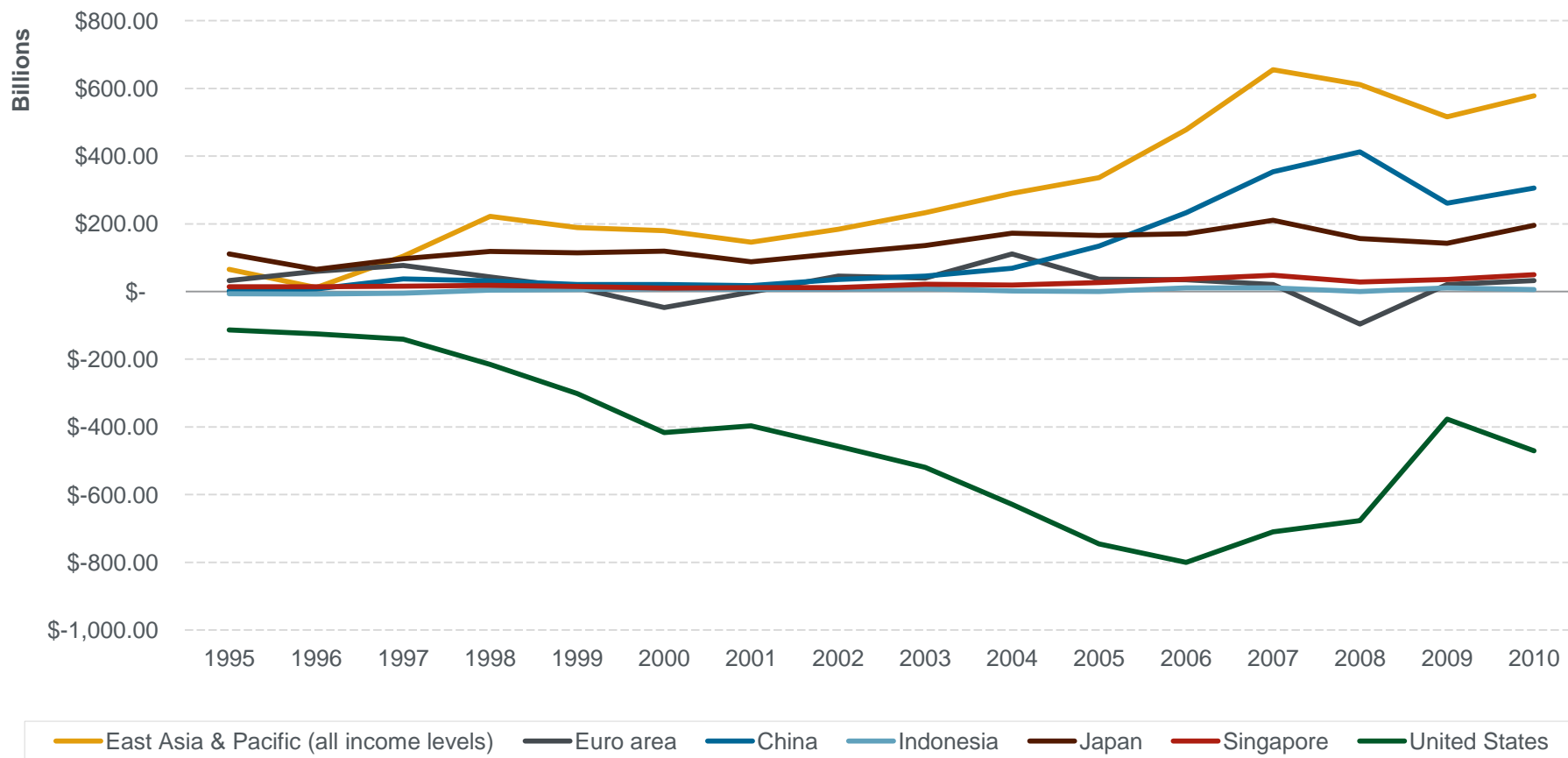


Chart Source: World Bank



## Asian Accumulation of Reserves: Chinese Investment

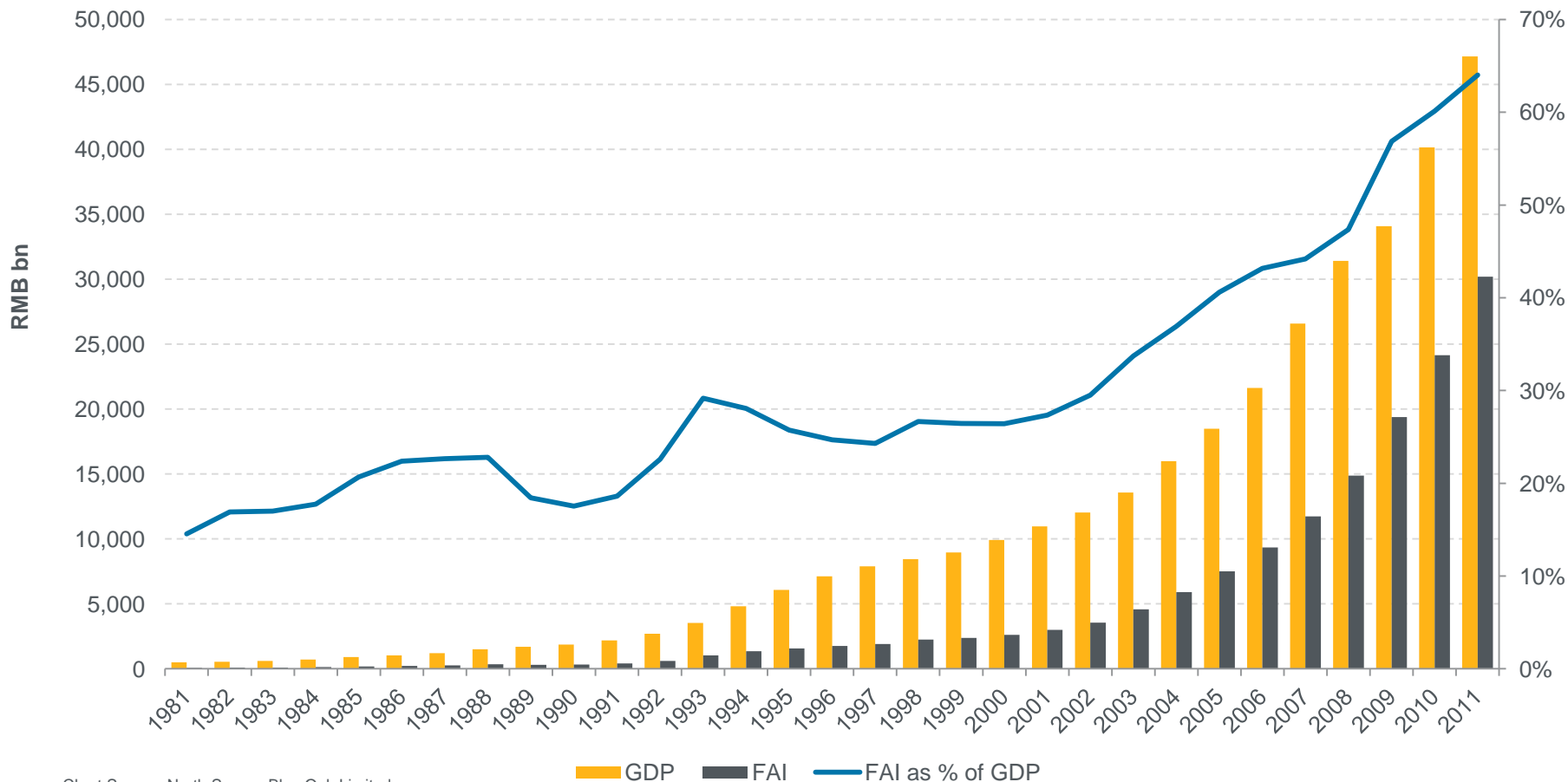


Chart Source: North Square Blue Oak Limited



- **US Debt Load**

- Two land wars
- Subprime housing / CDO build out
- Entitlements
- Monetary policy response to 2008

= US entering climactic government payments crisis

# Last Ten Years



## US Debt Load =

- Loose fiscal policy, deleveraging depressing growth, repair
- Extremely loose monetary policy, risk of deflation
- \$ Devaluation against developing world and hard assets
- Debt reduction through repayment + default + growth + inflation

### US Gov't Total Debt Outstanding Trillions

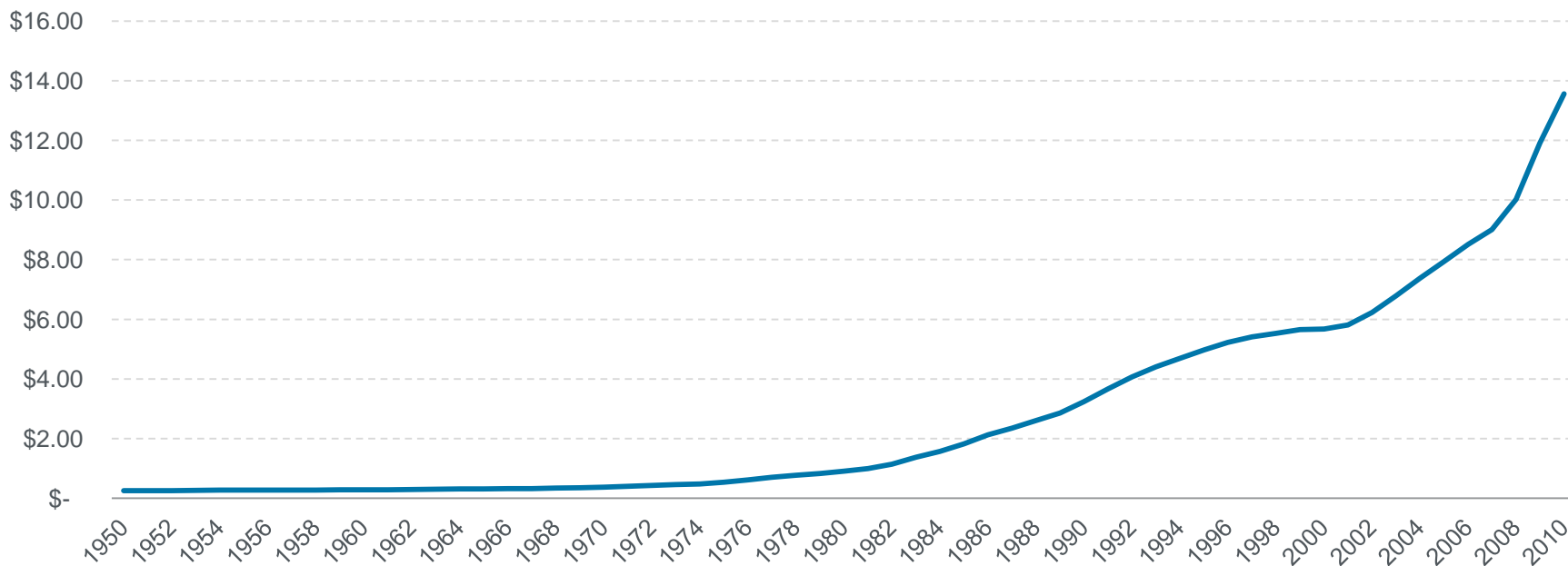


Chart Source: Bloomberg



## US Debt Load: US Outlays and Receipts

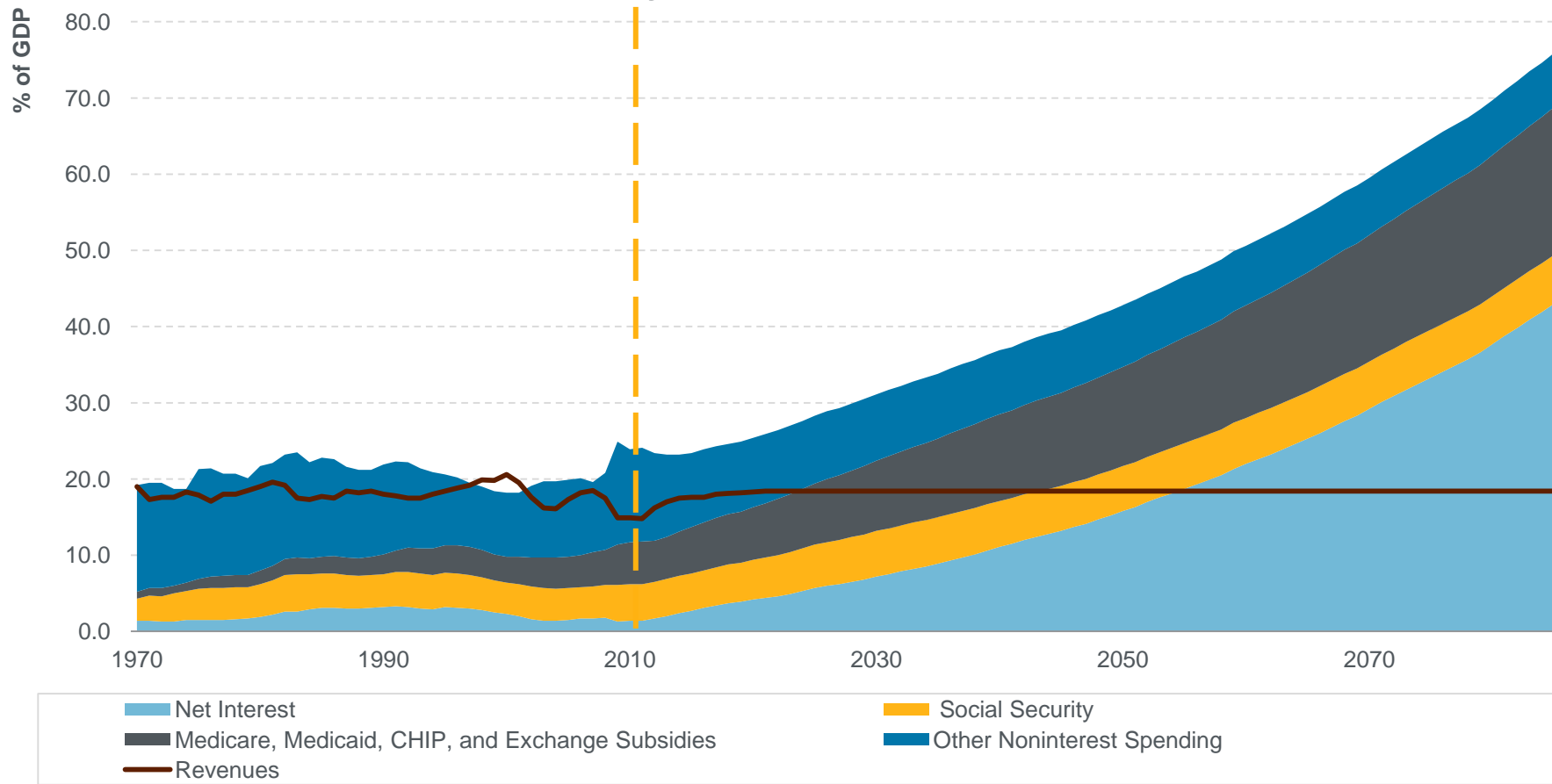


Chart Source: Congressional Budget Office



- **Europe - Debt Load**
  - Common currency and monetary policy created imbalances
    - Euro monetary policy to less developed, peripheral states
    - South borrowing (government and private)

# Last Ten Years



## Europe Debt Load - 10 Yr Gov't Bond Spreads

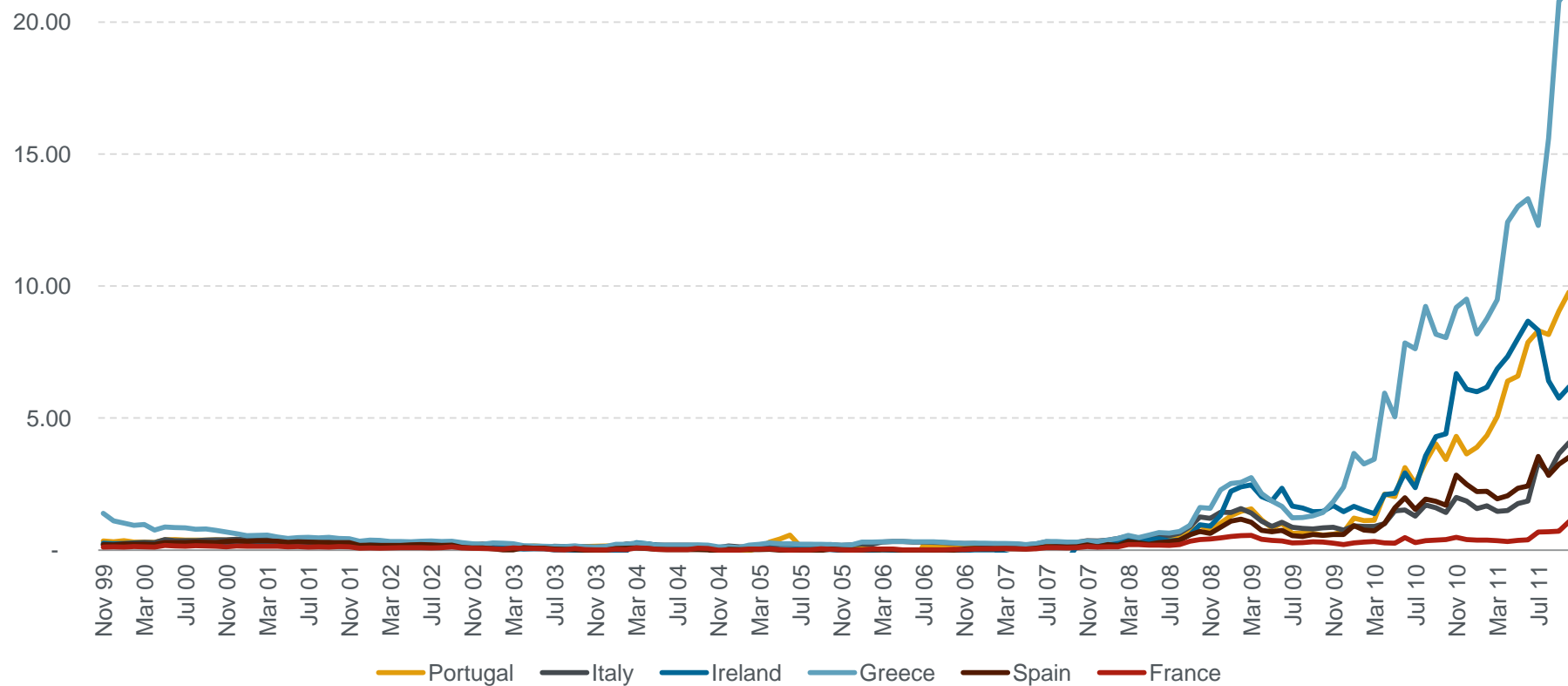


Chart Source: Bloomberg / Signet Calculations 12



- **Global Reflationary Support – Asian CBs, US, UK, EUROPE(!), Switzerland**
- **Growth In Emerging Markets**
- **Deleveraging in the West**
- **Be Aware of Demographic Influences**

# Global - Outlook

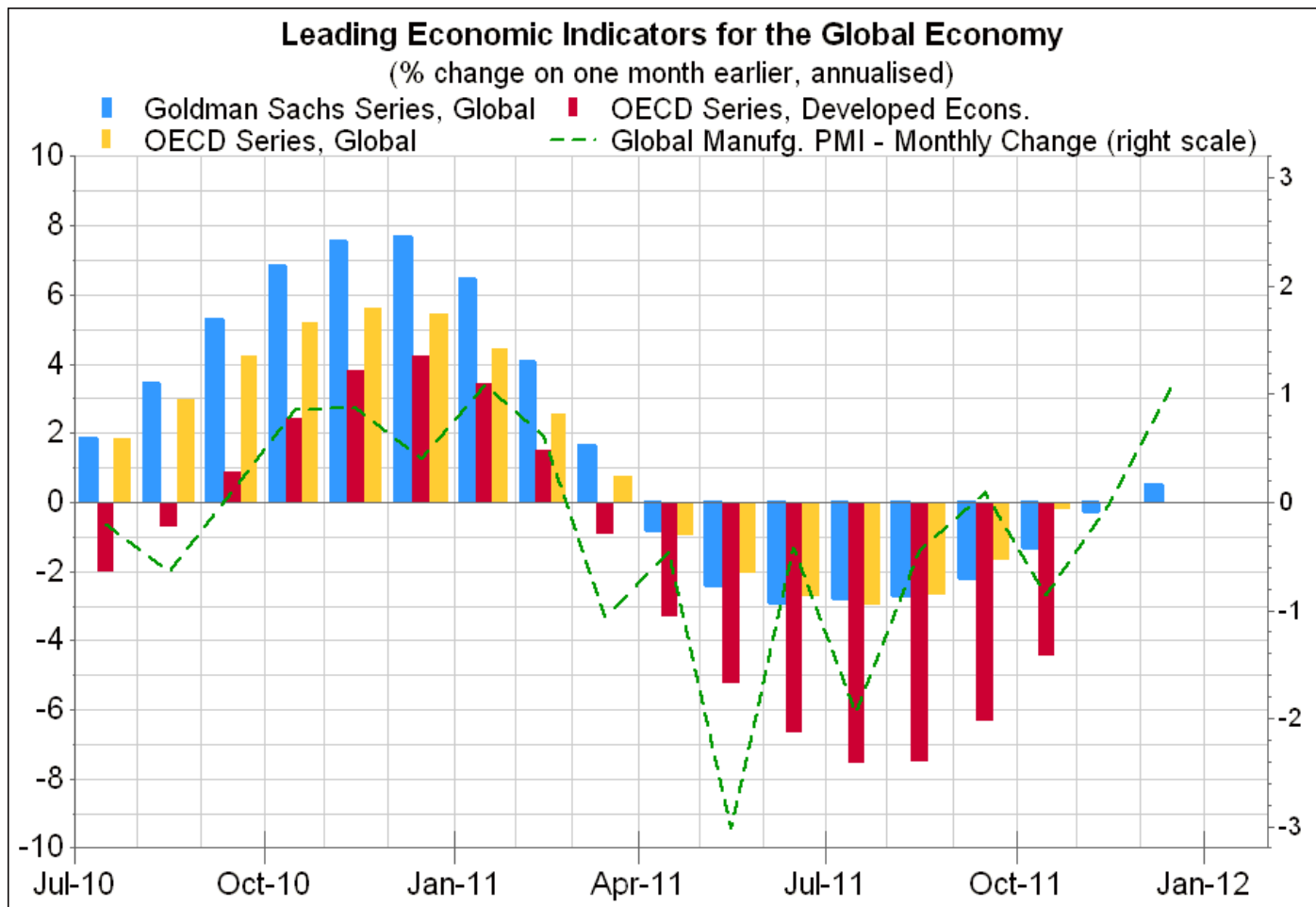


Chart Source: Financial Times

# Next Five To Ten Years



## EM - % Growth Rate of GDP



- Growth in EM

- Secular revaluation against developed world, due to significantly higher growth and yields

# Next Five To Ten Years



- **US** (C+I+G+Ex=GNP)

- Resolving past excesses, shrinking government sector

- Two Part Economy

- Depressed & deleveraging (gov't, housing)

- Growing un-leveraged (technology, healthcare, consumer staples, exports) + repairing finance

= Current account deficit shrinking, less \$ overseas, \$ stable

= Stocks up

= HY bonds offer best risk-adjusted gains, US mortgage bonds last bit of good US distressed



## U.S Dollar Index Bottoming? - 20 Years



Chart Source: Bloomberg

# Next Five To Ten Years



## US Stocks - NASDAQ 100



Chart Source: Bloomberg

# Next Five To Ten Years



## US Stocks - S&P Sectors

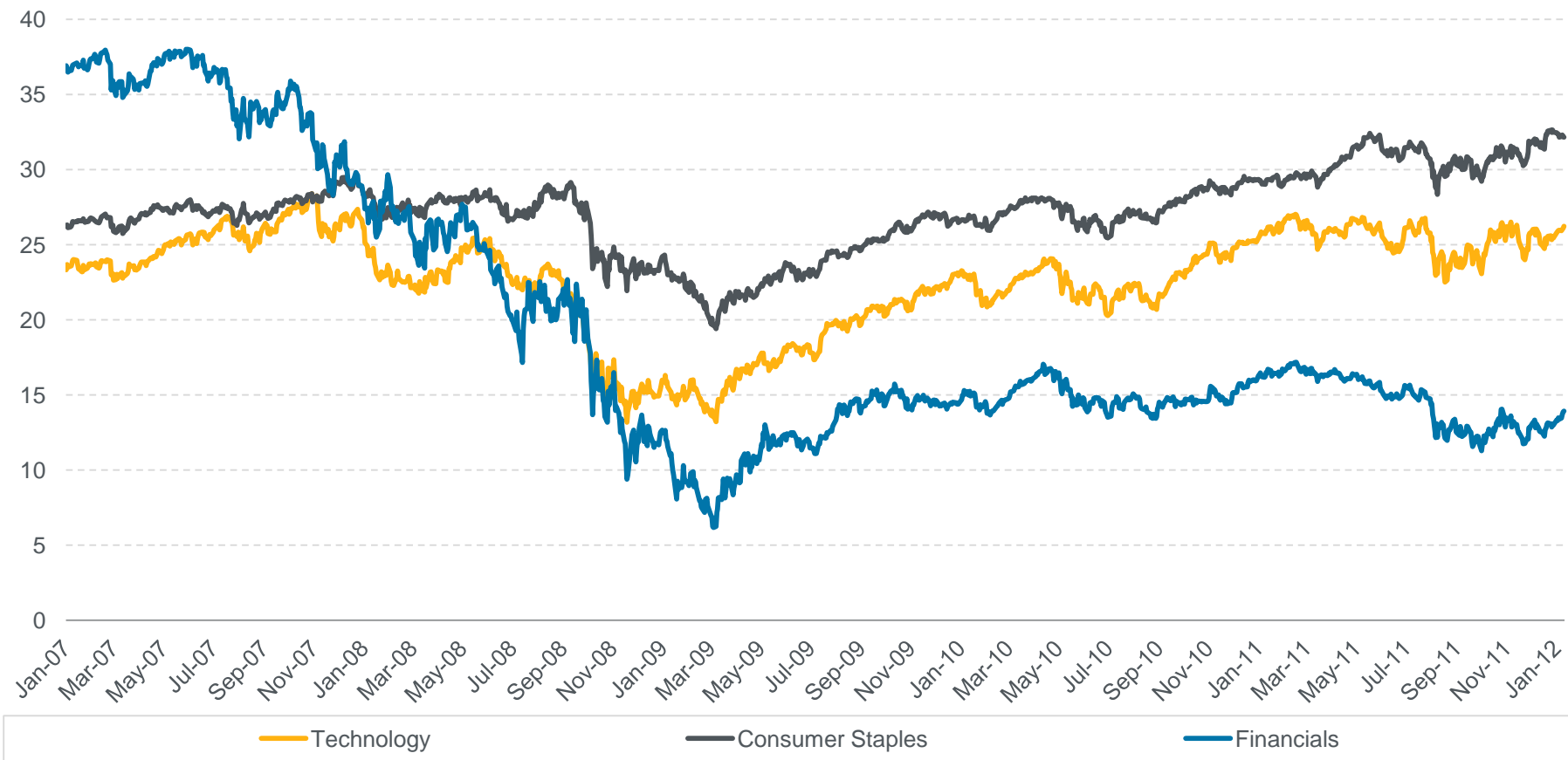


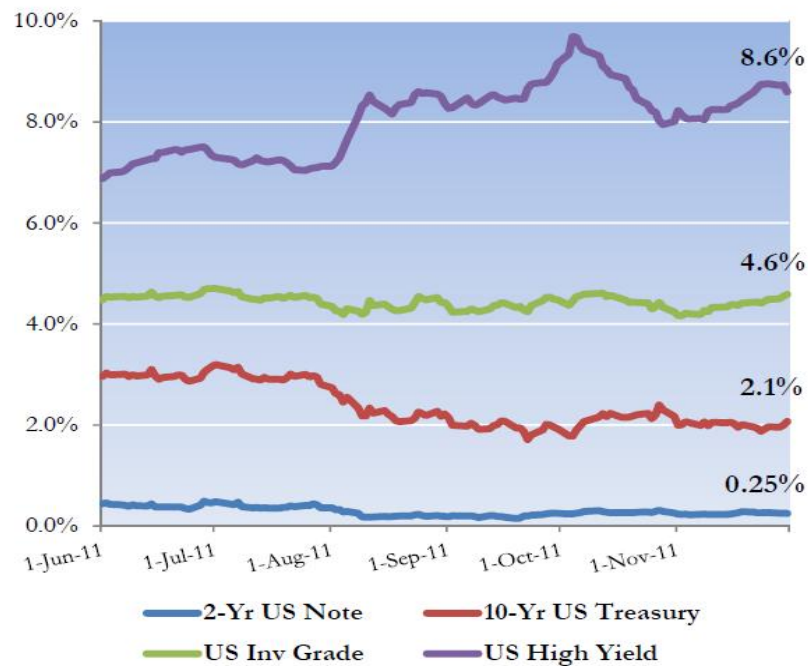
Chart Source: Bloomberg

# Next Five To Ten Years



## US Bonds

Slim yields for “safety”



Source: JP Morgan Dataquery as of December 1, 2011

STANDARD  
& POOR'S

### Leveraged Commentary & Data

High-Grade: Liquid names continue to lock in low coupons

Published Nov 29, 2011



Aa3/AA- 0.60% due 2014  
Aa3/AA - 2.45% due 2021



Aa3/A+ 0.875% due 2014  
Aa3/A+ 2.90% due 2021



A2/A 0.875% due 2014  
A2/A 4.125% due 2041

# Next Five To Ten Years - Influence of Falling Gov't Participation in Economy

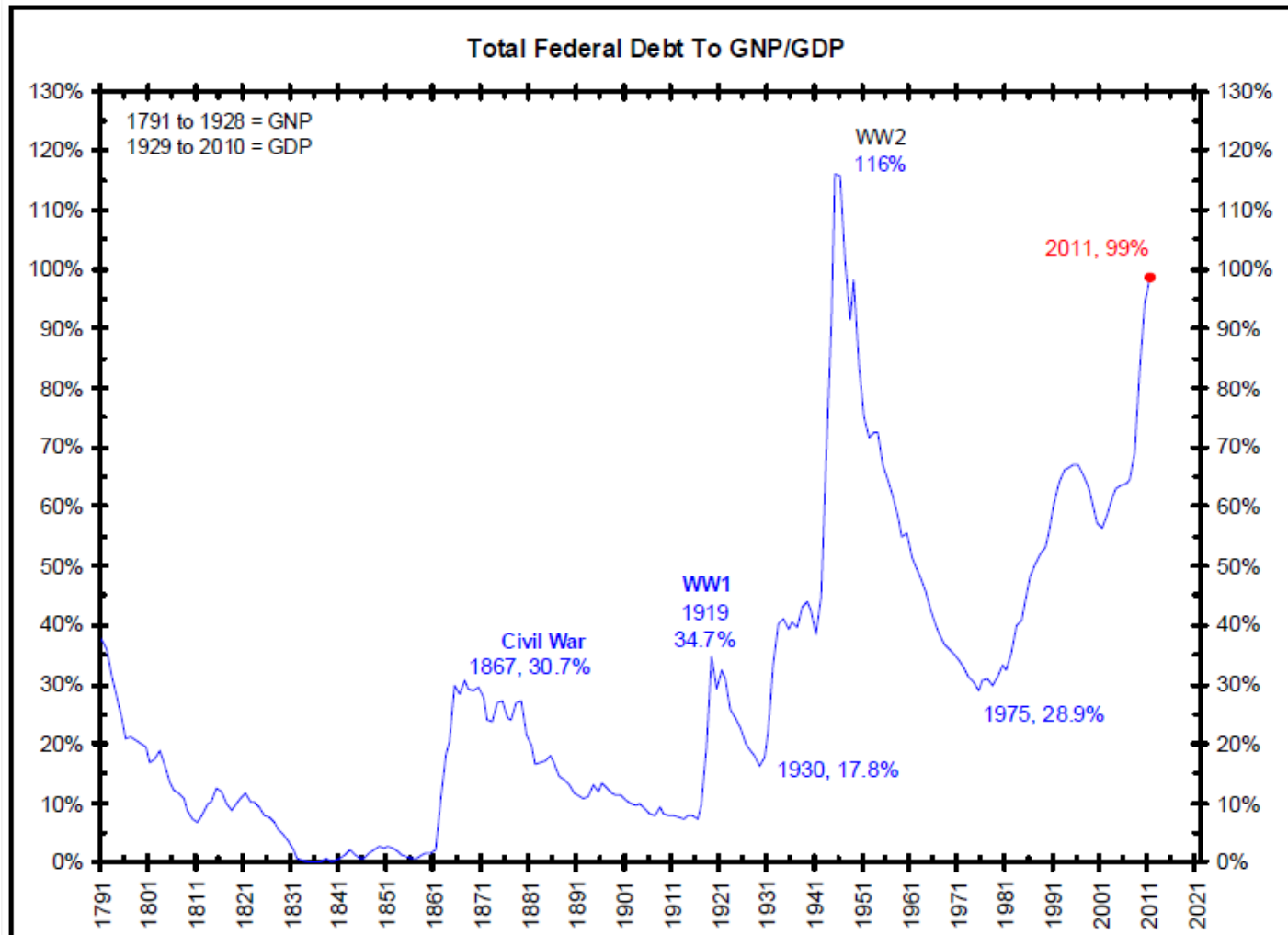


Chart Source:  
Bianco  
Research

# Next Five To Ten Years - Influence of Falling Gov't Participation in Economy

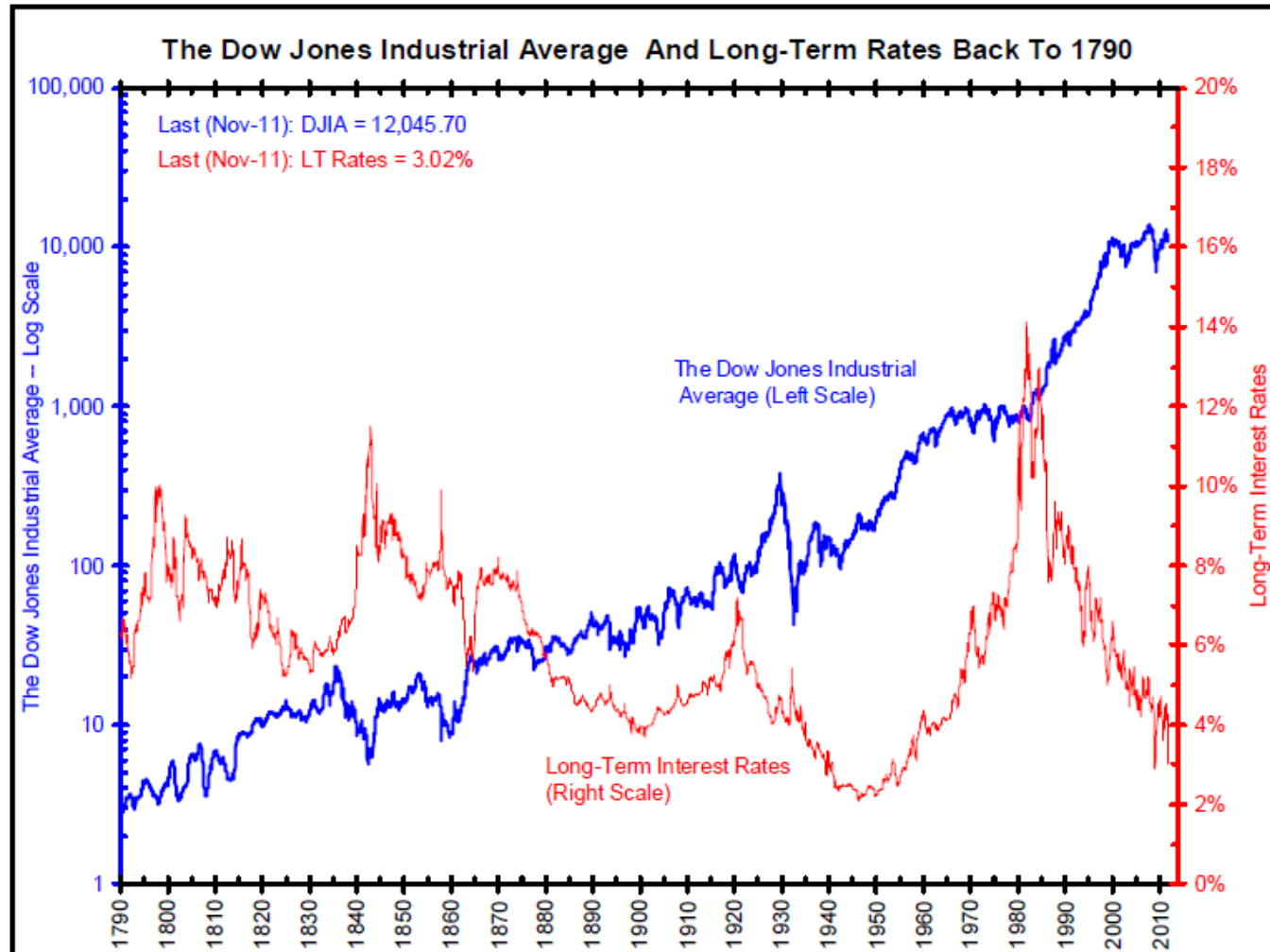


Chart Source:  
Bianco  
Research



- **Europe - Recession / Resolution, What Changed?**

- LTRO/ rate cuts / weaker euro? – ECB supports banks as they de-lever/ unsterilised liquidity injections

- Attempts to keep gov't bond yields under control

- = Huge liquidity / euro should head lower, credit and stocks supported, waxing European crisis

- = Takes away all systemic risk, allows system TIME to convalesce

- = Thawing of European credit conditions

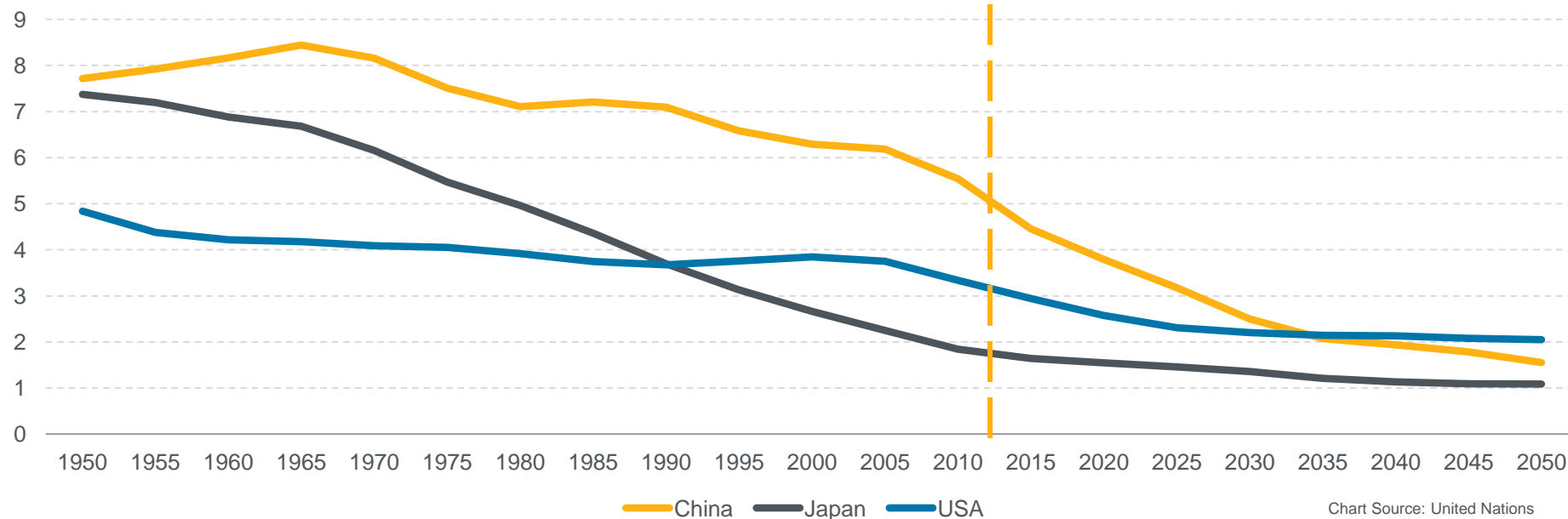
- = Stocks up

- = Credit better than expected and under-owned

# Beginning of Demographic Influences



## United Nations: Proportion of Prime Workers (15 - 59) to Aged People (60+)



- Japan example – not just headline number
  - Working age population decline – Japan plummets
  - 1/3 55 or older, so 50% of electorate retired or soon to be
  - % child-bearing women falling sharply



## Not Optimal Strategies

- **G4 Macro Rates, Currency, Commodities**
  - Requires falling rates
  - directionality,
  - = zero sum game currently



## Not Optimal Strategies

- **European Equities for volatility averse investors, requires:**

- Valuations
- Economic and Profit growth?
- Expanding excess liquidity / non-deflationary environment?
- No political convulsions
- Growing demographics?

= Equities are a perpetual call on future profitability, continuing deflationary environment should cap growth to a dull trend, GIPS liquidity squeeze accident prone



## Optimal Strategies

- **Emerging Market Macro – growth dynamic**
  - Offer value, falling rates, expanding excess liquidity, growth
  - Currencies increasingly floating
  - Sovereign credits improving
  - Yield curves extending / deepening
  - Corporate balance sheets expanding through leverage



## Optimal Strategies

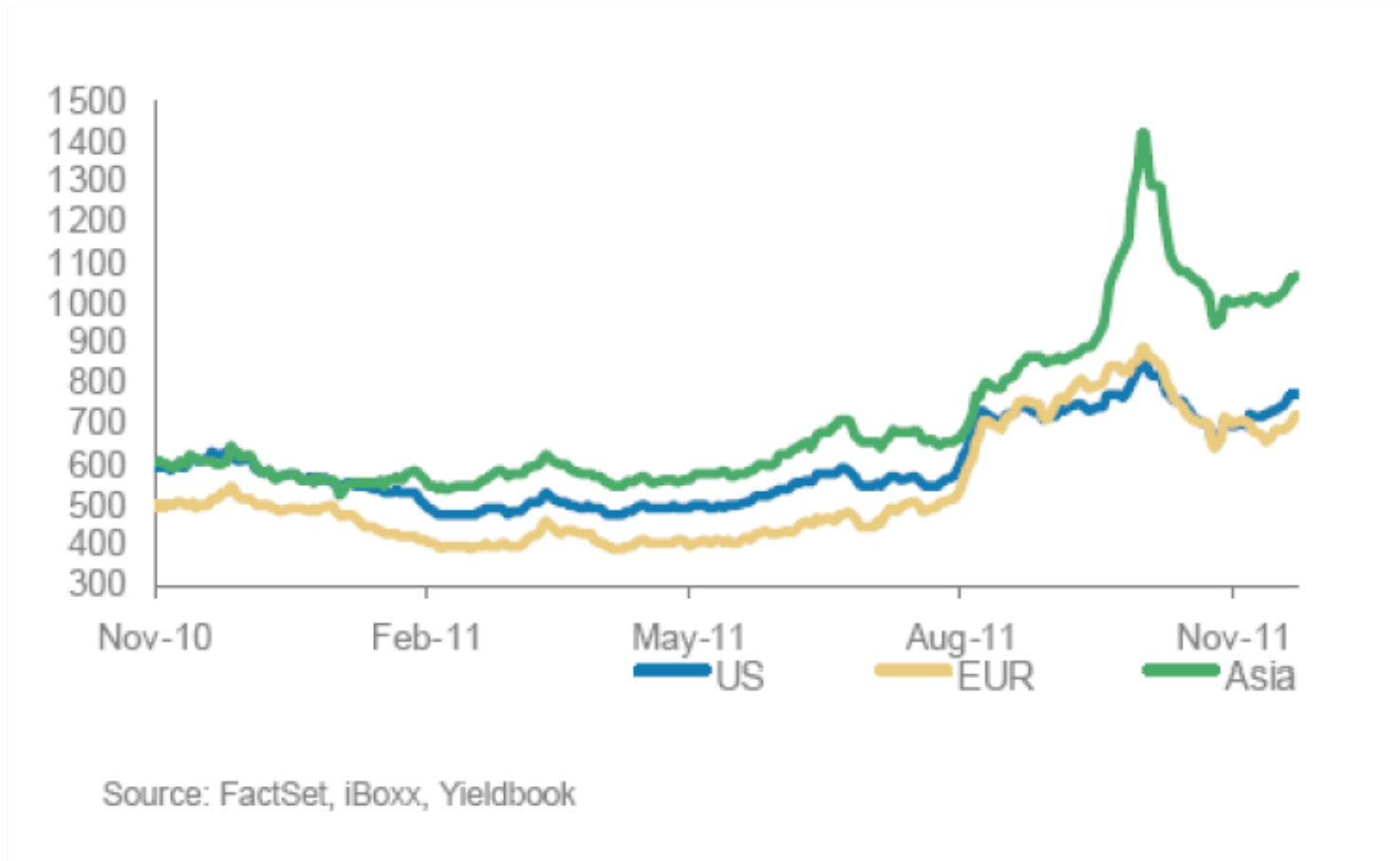
- **Emerging Market Equities**
  - **US Equities**
    - Valuations
    - Falling or flat rates
    - Expanding excess liquidity
    - Growth
- =Outperformance of Europe through Alpha + Beta capture



## Optimal Strategies

- **Global HY Credit #1 Risk Adjusted Return in 2012**
  - Senior, secured call on cash flow, not on profitability like equity
  - Yields
  - Pull to par
  - Debt Maturity – a defined event
  - Anemic growth
  - Corporate interest rates may remain large due to uncertainty premium

# High Yield Cash Spreads



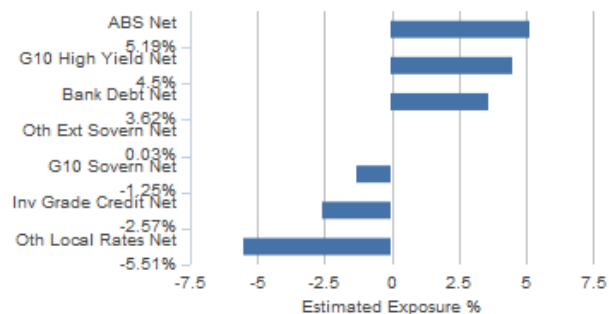


- **Manager Selection**
  - Fundamentals
  - Macro
  - Market intuition
  - Risk management / tolerance
- **Portfolio Aggregation**
  - Understanding exposures
  - Manage for the tails

# How to create absolute return next 5-10 years? Bottom-up

## • Portfolio Aggregation Examples

### Fixed Income Exposures



### Scenario Estimates

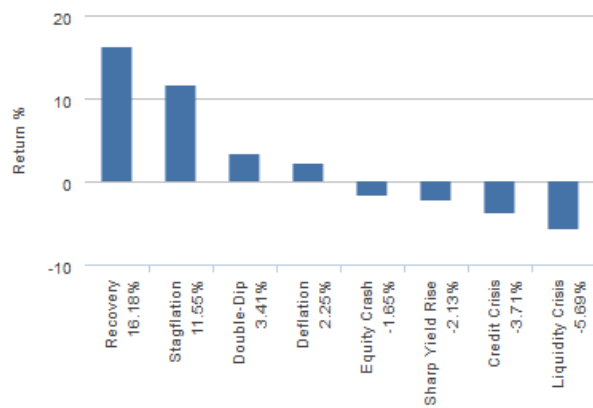
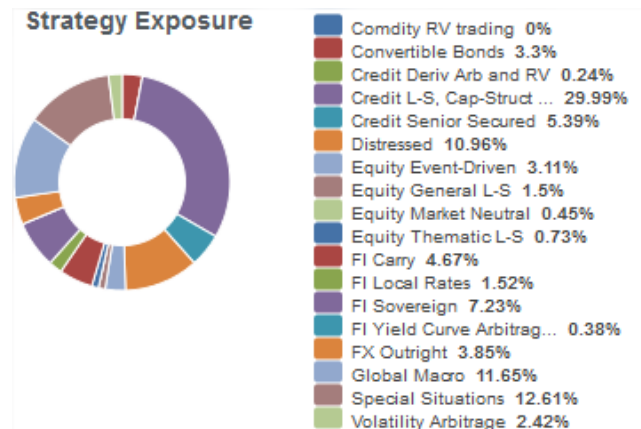
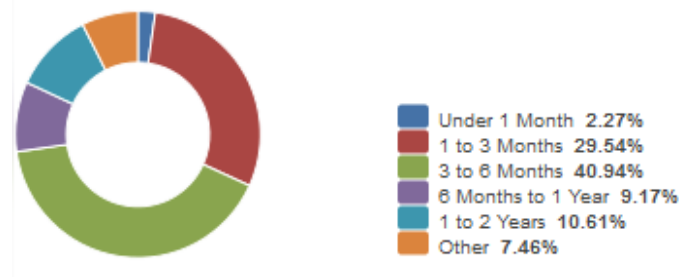


Chart Source: Signet Internal Calculations

### Strategy Exposure



### Liquidity Exposure



# How to create absolute return next 5-10 years? Why Hedge Funds?



## Cumulative Return

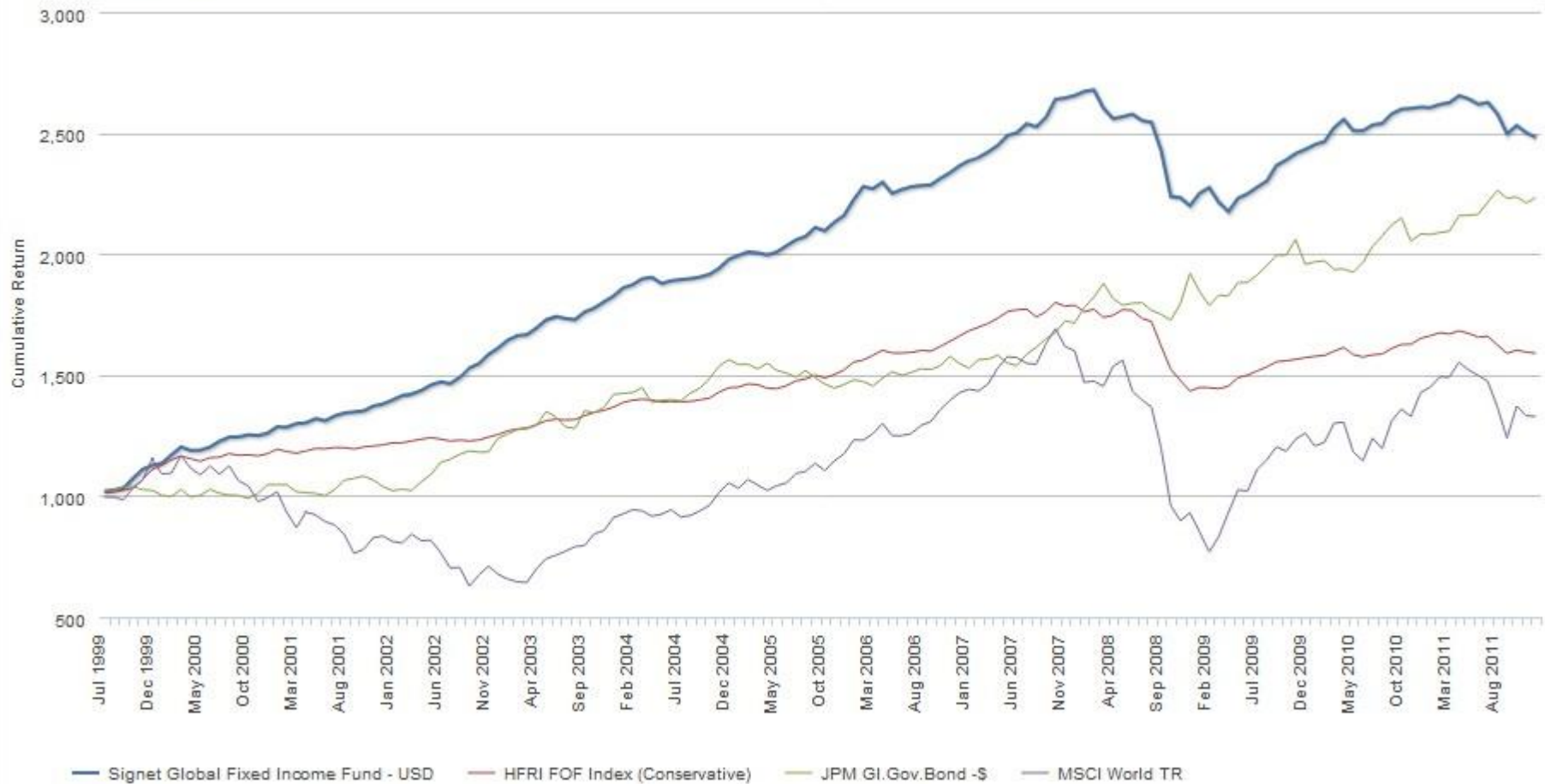


Chart Source: Bloomberg (Indices), SS&C (Signet Funds NAV), Signet Internal Calculations

# How to create absolute return next 5-10 years? Why Hedge Funds?



## Cumulative Return



Chart Source: Bloomberg (Indices), SS&C (Signet Funds NAV), Signet Internal Calculations

# How to create absolute return next 5-10 years? Why Hedge Funds?



## Cumulative Return



Chart Source: Bloomberg (Indices), SS&C (Signet Funds NAV), Signet Internal Calculations

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