Elgin asset management

investment commentary monthly

Monthly Commentary 2nd December 2015

November was a mixed month for financial markets. Equities were largely flat, with the exception of Europe (up almost 3%) and Emerging Markets (down almost 4%). Bonds did not do much either while in currencies the USD regained the upper hand as it has done most of the year. One notable laggard was the commodity complex. Oil resumed its downward spiral and fell more than 10% while gold had a horrible month, falling almost 7%.

There has been a lot of gloomy news lately. The attacks in Paris, the unprecedented refugee crisis in Europe, the turmoil in the Middle East and North Africa, and tension between Russia and Turkey. With the exception of very short-term reactions, the equity and bond markets have been taking them all in stride. Gold has done the "opposite" of what one might expect of a seemingly "safe haven" and had few bidders. As we have mentioned in the past, we will say once again that geopolitical tensions are not market-movers in the medium and long term. Short of a catastrophe slide into a serious multi-nation conflict, it is the economy and corporate profits that determine how markets fare. And for now, it seems that they are capable of climbing the walls of worry.

On Alternative Investments and the Grandmaster Fund

It has not been easy for asset allocators to determine how much to allocate to alternative investments such as hedge funds. This has been especially relevant in a low interest rate environment where bond yields are meagre, and at historically low levels. Both institutional and retail investors have been allocating an increasing amount to alternatives, and providers have been quick to react by putting an ever-increasing supply in the market. As with anything that is in over-abundance, it is becoming very difficult to differentiate between the truly unique funds that offer value and the majority of offerings that are mediocre at best.
At Elgin, we target anywhere between 10% and 20% of our asset allocation to alternative strategies, and this was implemented through two or three solid funds that have by and large added value to the overall portfolio. In looking for ways to add more value to this component, and to add greater diversification/exposure to quality holdings, we decided to put all our best alternative ideas in one fund (called Grandmaster), thus rationalising the process. Below is a Q&A:

Q&A on Grandmaster Fund

Where does the fund invest?
The fund will invest in our best hedge fund ideas and therefore will fall under the alternative component of the portfolio. Ideally the fund will consist of no more than 4-8 funds covering all areas of hedge funds such as long/short, managed futures, market neutral and multi asset. It might also employ other strategies to generate alpha (the excess return of the fund relative to the return of the benchmark index)., thus taking advantage of the expertise of our affiliated quant team.

How will the fund benefit a portfolio?

a) Access to funds that have high minimums and are otherwise inaccessible to retail investors.

b) Lower fees for many of these funds, as we can invest in institutional (instead of retail) classes.

c) Higher diversification for both larger and smaller portfolios. Especially for smaller portfolios, which with, for example, €50k can get exposure to a number of top hedge funds.

d) Lower transaction costs with the custodians

e) Our ability to produce alpha by arbitraging between top long-only funds and their underlying index through the use of derivatives.

When will the fund launch?
The fund was launched on the 1st of December.

What is the liquidity of the fund?
The fund has monthly liquidity.

Where is the fund regulated?
Luxembourg.

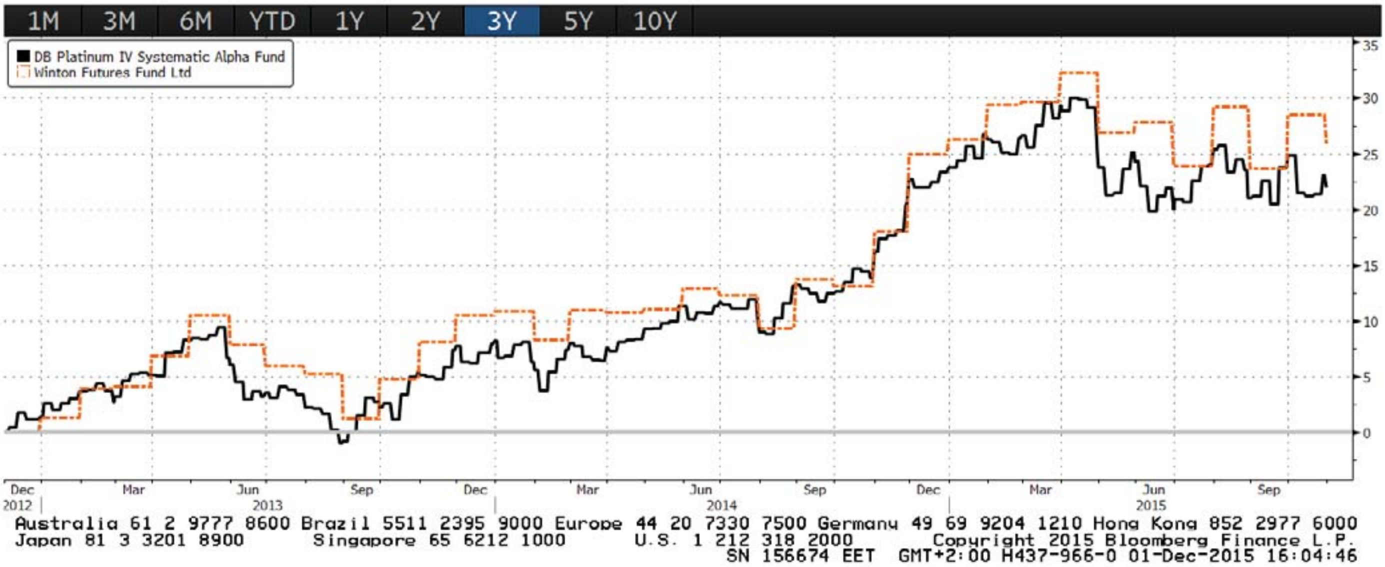
What will happen to existing hedge funds in client portfolios?
Existing hedge funds will be virtually transferred to the Grandmaster Fund, i.e. we have placed instructions to sell these funds and once we receive the proceeds we will buy the Grandmaster Fund, which will include the existing hedge funds.

What is the expected annual return of the fund?
The underlying funds have had an annual return in the upper single digits. Given the low level of prevailing interest rates, we target a net return of 3-7% annually.

What will be the cost to a portfolio?
The management fee of the fund is 1% annually. This should be covered by the lower transaction costs as well as access to more cost-effective funds. As such we expect that overall, clients shall benefit from holding the Grandmaster fund vs the few hedge funds that they were invested in before.

What is an example of the increased efficiency and cost rationalisation of the fund?
In the past the managed futures component was invested in the DB Platinum Systematic Alpha Fund, which was the only way we could access the highly rated Winton Futures Fund that has a minimum entry level of $1M. This has served us well as the fund produced 7% annually in the last three years. But while the minimum investment in the former was as low as $10K, the total expense ratio was quite a bit higher. As a result the main Winton Fund outperformed it by more than 1% annually – see below. The Grandmaster Fund will invest directly in the Winton Fund.

DBSI1CU LX Equity	97) Settings		Page 1/52	Comparative Returns	
Range 11/30/2012 - 10/30/2015		Period Daily		No. of Period	1064 Day(s)
Security	Currency	Price Change	Total Return	Difference	Annual Eq
1) DBSI1CU LX Equity	USD	21.94%	21.94%	-3.86%	7.04%
2) STAMWIF VI Equity	USD	25.80%	25.80%		8.19%
3)					



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