The Greenwich Roundtable Quarterly™

2013

EXPLORING NEW FRONTIERS OF INVESTING

The Greenwich Roundtable Inc.
One River Road
Cos Cob, CT 06807
Tel: (203) 625-2600
Fax: (203) 625-4523
rsvp@greenwichroundtable.org
www.greenwichroundtable.org
www.grbestpractices.org

Expanding Our Curriculum to Academia

The Education Committee will be presenting a series of Best Practices lectures at the leading business schools as part of its mandate to share our research to the broader investment community. Members of the Committee will be bringing the *Best Practices in Alternative Investing* series to the next generation of investment professionals as we begin to collaborate with Columbia, NYU, and Fordham.

Mark Silverstein, Chairman of the Education Committee and Trustee said "This program executes on our mission of education for investors. We are reaching a segment of the next generation of professional investors and sharing the vast knowledge and experiences of our membership developed over years that are refined in our Best Practices white papers." While the Committee has developed and shared Best Practices over the past decade, the educational outreach at Columbia and Fordham is intended for students who will be entering the industry in the New York metropolitan area. In all, the Committee has penned seven white papers focusing on a range of topics from due diligence on various strategies to case studies on how to avoid mistakes in manager selection and monitoring.

One of the most important aspects of the lecture series will be its ability to share the experience of our committee members. Various members of the committee will be presenting different Best Practices, personalized to highlight the lessons they have learned over their careers. If you are interested in lecturing or in organizing a series of lectures at your alma mater, please contact Mark Silverstein at msilverstein@enduranceservices.com.

Education Committee Chairman's Update

Over the past years, the mission of the Education Committee has been to undertake projects which document the knowledge and experience of our membership and redistribute it for the benefit of all interested investors.

In 2012, we completed our seventh Best Practices whitepaper, Avoiding Mistakes, which examines the causes of hedge fund failures and helps investors develop the tools to prevent being involved in such a fund. Aside from outright fraud, the most common causes were inappropriate combinations of leverage, complexity and illiquidity.

With a range of content now developed, from Due Diligence to Portfolio Construction to Avoiding Mistakes, our focus has shifted to sharing this valuable material with a wider audience. To start, I encourage you all to take advantage of this material and share it with others. This year, the Education Committee has been working on a number of projects to meet this goal. A dialogue has started with the CFA on ways to cooperate. To date, they have started to post our materials on their website. We have also started a program to work with MBA and Finance programs to assist in the classroom and with clubs, using our Best Practices materials as a core for mini curriculums and lectures.

We continue to explore other ways to reach a broader, yet appropriate audience. Rest assured, the Thursday symposiums will always remain an exclusive benefit for Greenwich Roundtable members.

I want to thank all the members who have taken part in Education Committee which has been core to our mission as an organization. It has been a mutually beneficial activity and we welcome participation from our membership. The value of our output for all the membership is directly related to the involvement of individuals. The Committee and the Board of Trustees appreciates your support and contribution to these activities.

Regards,

Mark Silverstein

Refer a New Member

Members are the Roundtable's greatest asset. The Greenwich Roundtable is the gold standard for education in alternatives. We encourage you to nominate candidates for Membership that would be a good addition to our tight-knit group. Your referrals are the key for us to reach a wider audience of sophisticated investors. If joining the Roundtable can add value to any limited partner, please refer them to Adam at Adam@greenwichroundtable.org. We'll familiarize prospective candidates with our mission and invite them to experience a symposium for a practical evaluation of the benefits of Membership

Asset Allocation for 2014 Navigating the Risks & Charting the Opportunities

September 26, 2013 • UNDERWRITTEN BY HEDGSERV

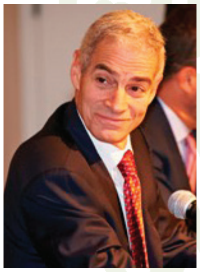
Our annual Asset Allocation session seeks to help us chart the opportunities and risks for what the world might bring in the coming year. Had we listened carefully a year ago, we might have been led to riches…perhaps with a few rags thrown in. We heard that opportunities from the stabilization of the EU would have profound effects on stocks in 2013, and indeed it did. We also heard that 2013 would prove a return to equities, and indeed it has. And at times, predictions proved wrong to our benefit, such as the precaution that returns in 2013 would be cyclical and difficult, and we should expect high volatility and low returns. In retrospect, few seem to complain that the opposite has transpired, although the bellies of risk-averse active managers certainly grumble a tad more than their indexed brethren.

Our panelists a year ago also warned of ominous risks on the horizon. We were told that rate expectations would rise sooner than people think, and for a tad there in the spring and summer, indeed they did. We heard that within the next 2-5 years, we would experience a series of unpredictable, non-linear shocks in the capital markets. (The good news is we haven't yet; the bad news is we still have 1-4 years left to learn if this call was correct). Lastly, we were told that a bumper year was possible in 2013, but would likely be followed by a down year in '14.

Of course, not all the views of a year ago proved accurate. Had we heeded advice that Brazil was stabilizing and undervalued, we might be left scratching our heads as to whether Brazil now is still stabilizing and just more undervalued. We were told that the same stabilization of the EU would have a profound effect on bonds and commodities. It turns out that particular effect was only on the opportunity cost of our capital lost if investing in either space.

Forecasting is only difficult when it pertains to the future, and yet forming views that turn into profits can only come after a thorough investigation of sound information that turns to theses. For those prerequisites, we turn once again to our panel of wise men to help us think through the year to come.

Ted Seides
October 2013



Mickey Levy

Mickey Levy
Blenheim Capital Management

The uncertainty created by unsustainable policies around the world seems to be giving way to improving fundamentals. The US is improving cyclically. Our potential for growth is high. We're in the 7th or 8th inning of the recovery from the financial crisis. The probability of recession is low. Monetary policy works with a big lag and those lags are about to kick-in. Europe is stabilizing after years of crisis, perhaps in the 2nd or 3rd inning. The tail risks have been taken away but there's still a long way to go. The process of recapitalizing the banks hasn't begun yet. Getting a single bank regulator with resolution authority, supervision with teeth is critical. The recovery is sustainable but gradual. Japan has the strongest growth of any large nation now. Will the Abe administration follow through with its promises of stimulus? The lower yen is raising exports but they need a boost in capital consumption. China as a consequence of its robust export-related growth is experiencing a dramatic increase in its cost of labor. Thus its overall growth will be slowing and China's leadership is managing expectations. Mexico is an emerging nation whose fundamentals are amazing. They may see 5 percent growth with their authentic pro-growth reforms. Some background issues may affect asset allocation decisions. First, the US is getting higher returns to capital and lower returns to labor. This is a fact of life now. Second, the oil and shale boom is a positive factor that will affect things in positive stages. History has shown us that when the Fed hiked rates the stock market followed by going up. The US economy is tighter. Inflation may be inching up in 2014. When a central bank pumps liquidity into the system it sloshes around and bids up financial asset prices. It doesn't disappear until it's spent or it's drained. Tapering doesn't do it. The Fed wants to leave it there until it's spent. It's not acting as a fiscal agent for the government. Should the US, Europe and Japan continue their current trajectory then the broader environment surrounding asset allocation issues is more favorable.

Louis-Vincent Gave

Louis-Vincent Gave
GaveKal Research

Equity bull markets rest on three pillars; that you need decent economic growth, attractive valuations, and excess liquidity to push valuations higher. There's little to worry about on the growth side. The data has been fine. Global trade was decelerating but now it's picking up thanks to a rebound in Chinese consumption and production. After months of destocking Chinese inventories are at record lows. There are so many sources of liquidity, the ECB, BOJ, People's Bank of China, and all the other domestic banking systems around the world. There are two changes that may not be on your radar screen. The BOJ did nothing from 2008-2012. The leadership changed and they promised to print money until inflation reached 2 percent. Japanese households are the richest in the world. Will they continue to hold cash earning zero percent? With a falling Yen and rising asset prices it makes less sense to hold cash. Where will that money go? From 2003-2012 it made sense to front-run the Chinese. Buying whatever the Chinese wanted to buy, Bordeaux wine, copper, gold, Vancouver real estate or modern art, was a good trade. That period is over. China has rolled over demographically and they're not expanding their balance sheet. The big idea for the next 5 years will be what do the Japanese want to buy? Japanese savings could become a proper source of global liquidity. The internationalization of the RMB may be the second largest source of liquidity that no one is talking about. Every currency in Asia is down 5-15 percent except the RMB. Bond markets in Asia have been a blood bath. The Chinese offshore bond market (Dim Sum market) rose 6 percent. The returns are impressive because their volatility is half of that in the West. China's growth story was never dependent on foreign capital. Until 2008 China was happy to be part of the US dollar orbit. When the US collapsed into recession they were surprised that exports could fall so fast. China and Korea couldn't trade with each other. Korea was captive to trade financing from US banks and couldn't get US dollars. They asked themselves, why are we being punished for behavior from badly managed US banks. They're forming a direct relationship with each other denominated in RMB. China created the Dim Sum bond market to supply assets for Korea to hold in their central bank. China's biggest comparative advantage is not cheap labor, it's Honk Kong with its credible, deep financial markets. Big markets take at least 50 years to build. The British are good at building financial markets. In 1997 they gave it to China and said, don't mess it up. To China's credit, they haven't. For the past 10 years China sold cheap clothing for US dollars. For the next 10 years China wants to sell telecomm switches to India, oil rigs to Australia, earth moving equipment to Indonesia, and railroads to Africa. They'll sell the equipment to Indonesia for half the cost and provide financing in RMB. China isn't interested in financing the US consumer. They're interested in providing trade financing for the emerging markets. This transition will be facilitated by, for example, Indonesian bonds denominated in RMB and held by Japanese households. Asian savings are the fastest growing in the world which were recycled in the US. This will change in the next 10 years. The transition is similar to what Europe experienced in the 1970's when it went from being denominated in US dollars to German marks. This is a structural shift that's bullish for emerging markets.

James Dunn

James Dunn
Wake Forest University

Every endowment thinks we're unique. However we're all basically the same. We try to do things a bit differently at Wake Forest by being more concentrated. Wake Forest is a small liberal arts college in North Carolina. When I arrived in 2009 they'd just lost 28% or $290 million. This is not other people's money. This is everything. Our mission is to protect, perform and provide…to invest in the lives of our students. This is not a race to win first place or to achieve a 12 percent return. I'm the second CIO in 176 years. The politics are Machiavellian. And people have long memories. Fifty years from now they'll still remember that Jim Dunn messed up. Protect the endowment is our first duty. Perform over inflation is our second. Inflation kills an endowment. We have professors that teach until their nineties. We can't put money into bonds and go to sleep. We have a 5.3 percent spending rate so we need to manage our liquidity very carefully. We don't have a hedge fund bucket or an asset allocation model. We have a factor model. We have 25 factors that we optimize our portfolio to. A few of those factors are momentum, growth, spread, duration, and value. Do we really want to buy growth in the US at the rate of 2.5 percent? Today we have more African stocks than we do US stocks because it's growing at 9 percent. We have a concentrated portfolio with 50 managers. The factor model allows us to express a conviction around a certain factor or a manager. Mike Tyson says 'everybody has a plan 'til I punch 'em in the mouth'. Every endowment had a strategy until 2009 when they got hit. We believe you should never panic. But if you do panic be the first. Understanding the factors and the exposures that drive our returns allows us to hedge at the position level. This isn't a tail risk hedge. But it allows us to build our conviction in a manager and buy some protection to lower our risk. Volatility has been cheap this year. We've been able to add hedges that were not possible 2 years ago. Those trades have helped us lower our volatility. In the last 4 years since I arrived we've been able to get 9 percent return with less than 4 percent volatility. We try to find interesting managers that can do more than one thing well. We try to find managers who are interested in Wake Forest, in our factor model and who can work with us. The show up and throw up style doesn't work well here. We look for managers who've done their homework on us. We look for managers who can add value to our factor model. It's a different conversation than the same old talk around the pitch book. We also believe in humility, mission and character. Activism is difficult. We can't have a manager that goes after one of our Trustees companies. Our managers can't be on the cover of New York Magazine bragging about their art collection. The golden circle is a framework where certain people or companies are so much better than anyone else. Why is Apple so innovative? It's what you are, what you did to get there, and why do you do it. Our conversations with managers revolve around how we can help the students. Nowadays we like distressed sellers rather than distressed assets. Buying hedge fund side pockets is one example. We have 100 year capital. We do a lot of work on long-tailed, long-dated investments. We have a cocoa farm in Nicaragua. We bought sea finance companies. We own a soybean farm in California. We're buying nuts in Australia. We're into student housing, particularly seniors rather than the grad students who may go home without paying their rent. Distressed shipping is another interesting area. There are very few managers and the cycle is bottoming. We love volatility. We've seeded some interesting managers in this space. Wake Forest's portfolio is 40 percent credit, 30 percent equity and 30 percent real assets today.

The Role of the Chief Investment Officer II

May 16, 2013 • UNDERWRITTEN BY FLAG

The topic for our May session, The Role of the Chief Investment Officer is our latest update on how the investing process is conducted and the roles and responsibilities of the staff, trustees, consultants and investment managers. This session is a continuation of our previous symposium on the topic in 2005 when we first examined this important aspect of the investment industry and how the CIO role is evolving in response to the rapid growth both in institutional assets and the changing governance landscape. In 2009 our Best Practices in Portfolio Construction called on the chief of staff to educate the investment committee, and it also called on the investment committee to enable the staff to do its best work in an increasingly challenging environment.

With the growth of assets in the past 30 years and the addition of alternative strategies, CIO's are faced with increasing portfolio complexity and the challenge of conducting adequate due diligence, monitoring and risk management, often with limited staff resources. In response to these trends, many institutional investors have outsourced all or part of the management of their portfolios to consultants and managers. Assets invested in various outsourcing models have grown very rapidly in the past ten years and this growth is expected to continue. While outsourcing can solve many problems faced by resource-constrained institutions, it challenges investment committees and staffs to determine the best governance model for their institution CIOs have the responsibility to hire, train and manage a talented team of professionals. They must continually educate themselves and their fellow team members about trends in the investment business as well as uncover opportunities to exploit in an increasingly global marketplace. Whether the assets are internally or externally managed, the job of the CIO can still be fun and exciting. Many CIOs are in their jobs for long periods and their compensation is often substantial, but the pressure is always on them to perform.

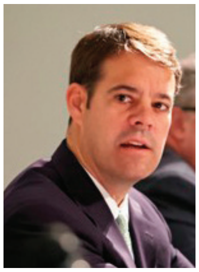
Our panel was made up of three experts in the field: Ellen Shuman, Former CIO of the Carnegie Corporation in New York; Kevin Quirk, a Partner at Casey, Quirk & Associates; and Rick Nelson, CIO at Commonfund. These three individuals brought a wealth of experience in the investment business and offered insights into how the role of the CIO is changing in response to industry trends.

John Griswold
August 2013

Ellen Shuman

Ellen Shuman

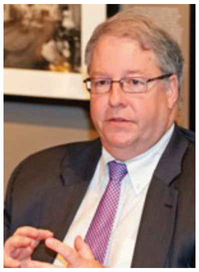
We have the best job in the world. It's dynamic, challenging, interesting and it's fun. We're looking at different asset classes and strategies all over the world. We work with really smart, passionate people who care deeply about what they do. But in the same way really good teachers get promoted to the principal's job, really good investors get promoted to the CIO job. The dilemma is that we're spending a lot of time on managing and administration but not on investing. The challenge is to manage your time as a CIO. Although we love investing we suddenly find ourselves as senior administrators dealing with a lot of bureaucratic issues. Managing your team and cultivating good people is critical. You need a great team because they're doing the investing. You need to instill a discipline, a culture and hopefully your contrarian instincts into your team. Investment organizations haven't been very good at professional development. Rather if performance was good you got a bonus. If it wasn't there is no bonus or you got fired. They haven't emphasized the importance of delegation, training and collaboration. It's really important to inculcate teamwork and systematic communication in your staff so they know how to make a decision and why they're making it. Although our job is to empower our team and work collaboratively, the buck stops with the CIO. We need to know about every investment, every manager and how it all comes together. The tension lies between doing it ourselves and delegating it to our protégés. The challenge is getting the right balance. It was gratifying to see the two senior investment professionals at Carnegie become co-CIO's. It was a thoughtful succession. The second most important aspect for the CIO is to educate your constituency…your board, your investment committee or your clients. Education is very important because it helps the staff articulate its investment philosophy, its culture and its decision-making. Education must be done before there's a disruption in the capital markets or a period of poor performance. In this way they're comfortable with your strategy when the markets go against you. It also gives you the conviction to buy at the bottom because your constituents will support and have confidence in your decision. David Swensen is one of the best educators in the world. The Yale investment committee approves every investment. We took the same approach at Carnegie because if the committee understands your decision process they're less inclined to second guess an out-of-favor strategy. The urge to sell at the bottom is an indication that the governing body is not always thoughtful and education hasn't been done very well. Also having a good network is everything. Learning about what's out of favor can be very profitable.



Kevin Quirk

Kevin Quirk

We study what investors and intermediaries are thinking for our clients, the asset managers. In the past 7 years our research shows that being a CIO was fun. The markets are more difficult, more volatile and more uncertain. The complexity of alternatives is troubling investors too. The role of the CIO and the staff is being questioned. This includes their advisors. Very large institutions have sophisticated investment committees as well as the breadth of staff and resources to get the job done. Then there are the small to midsized investors who are struggling with the model. This can be daunting especially if they're trying to implement a sophisticated portfolio. Our research tells us that investors are questioning the classic investment consulting model. The consultant is an advisor with little discretion or accountability over the portfolio. Their job is to conduct manager research, to give perspective on asset allocation and to give advice to the investment committee. Investors are now questioning the consultant's alignment and the expertise of the staff. Outsourcing is a prominent trend that we are studying very closely. Investment committees and investment offices are taking a good hard look at themselves to understand whether their existing model, in sourced or in sourced plus consultants, makes sense. Is there a better option? The outsourced CIO is a prominent theme especially for smaller investors who can't afford the resources to implement a sophisticate portfolio. Implementation differs from complete to partial discretion. Everyone is wondering whether the outsourcing model really works. Geography, staff and board sophistication as well as compensation tension are other factors in play. Supply is outstripping demand primarily because consulting and fund of funds need to transform their business models. We're probably in the third inning of this trend.



Rick Nelson

Rick Nelson

Being a CIO is a lot of fun if you enjoy being quizzed every month by some of the smartest investors like Seth Klarman or Mohamed el Arian. What is most important is to understand what the client wants. Secondly, understanding the process of investing. Third is the business aspect of putting it all together. Client, investment and business are one dimension. The other dimension is tactical and strategic issues. Not all CIOs can be good at everything. While CIO's may not be experts in all these aspects, they should have strong principles. They need to be open to different views and different investment approaches, especially if they serve many different clients and time horizons. As the world gravitates to customization, just offering a suite of funds becomes less important. Recently the role of the CIO in a pool of perpetual assets has meant taking more illiquid investments to maximize returns. Nowadays getting CPI plus five is being challenged by the markets. Clients are asking for a more holistic approach. Endowments need to ask themselves 'when can we withstand poor returns'? Understanding when a portfolio will do well and when it will do poorly, the payoff pattern and the appetite for risk is nuanced for every client. Having a plan for what can go wrong must be done before it happens. You'll want a long term view on asset allocation as well as a short term view that tries to pinpoint where you are in the cycle. Avoiding blowups will allow compounding to do its job. My own challenge is coming to grips with the fact that more diversification isn't ideal for everyone. When selecting an outsourced CIO look for a provider who understands your needs and has the skills to balance the many dimensions of the job.

We will continue to monitor the changes we see in the role of the CIO since the position is a critical to the success of most investment portfolios. As the outsourcing business grows, it will inevitably change the role of the CIO. There has rarely been a time in our history when the performance of investments has been more critical to the health and well-being of our citizens, since individuals, pension plans and nonprofit funds are all dependent on the effective management of asset pools.

Into Japan: Reform, Revival or Regret?

March 21, 2013 • UNDERWRITTEN BY HEDGESERV

Our March 2013 session's panelists, who discussed the current backdrop for investing in Japan, follow bravely in the footsteps of two distinguished prior panels – the first in early 1999, and the second in late 2007 – who shared their views with the Roundtable on this most complex and at times inscrutable market, during similar periods of relative optimism amidst what was otherwise a depressing decade and a half. Interestingly, each of the two prior panels culminated in split decisions regarding the outlook for investing in Japan, as the fund managers on both panels cited the breadth of seemingly ultra-cheap stock valuations, while the economists were more circumspect, and pointed to a variety of structural challenges and policy fumbles. Timing was everything: since 1992, there have been five 40%+ up-moves in the TOPIX, with a median duration of 13 months, followed at times by sharp sell-offs.

At least historically, understanding Japan, and making money in Japanese securities, has been anything but straightforward. The key question for our panelists and for us is whether this time it's really different. We are now experiencing the early dawn of Abenomics: at the time of our session, the Topix was up roughly 45% in yen terms since the rally began in November, and 18% since the beginning of the year. The move has been highly negatively correlated with the depreciation in the yen, which is sensible given the pronouncements of inflation targeting and the reshuffling of the BoJ.

The bull case for investing in Japan is that Prime Minister Shinzo Abe's "Three Arrows" strategy, dubbed Abenomics, truly represents a sea change in monetary policy (the first arrow), which, coupled with the proposed fiscal and structural initiatives (the second and third arrows) is capable of unleashing domestic inflation, consumption and investment, and propelling Japanese capital markets. If Japanese policymakers can engineer a sustainable reflationary cycle, our panel's fund managers could be right this time around. If not, investors may endure more disappointment, as the bear case becomes more pronounced and investors increasingly worry about potentially unsustainably high debt levels, poor demographics and the potential for a return to the long-term cycle of investment malaise.

Once again, our panelists included a combination of experienced macro investors and stock pickers. Mark Mezvinsky founded Eaglevale Partners, a New York-based global macro hedge fund. Robert Macrae is CEO of Arcus Investment, a longstanding value-oriented Japan long/short equity hedge fund with offices in London and Tokyo. Alex Kydd is a senior partner at Sloane Robinson, a London-based Asia-focused equity hedge fund; Alex is co-manager of Sloane-Robinson's Japan strategy. The speakers guided us through this timely and complex topic, and helped us to understand the prospects and risks of investing in Japan. Their comments are summarized below.

Ray Gustin
July 2013


Marc Mezvinsky

Marc Mezvinsky
Eaglevale Partners

I'll break my remarks into four concrete parts. One is to be a student of history. Second is to look at the environment and the short-term catalysts. Third is what can go wrong. And fourth is implementation. Everyone is talking about Japan's new reformer Shinz Abe and Abenomics. But the real guy to study is Takahashi Korekiyo. In the 1930's he looked and acted like an Asian Ben Bernanke. To understand Bernanke you need to understand Takahashi. To understand Abe you need to understand Takahashi. Why is he significant? He took Japan off the gold standard in 1931 for the second time. He realized the key to helping Japan avoid depression was growth and inflation. Thanks to Takahashi's policies, Japan never experienced negative growth in the 1930's. He realized that inflation expectations are everything. Today there's real nostalgia for Takahashi's policies. Inflation expectations are rising, consumer confidence is rising and real asset prices are edging up. It becomes a self-feeding loop. The Bank of Japan realizes that deflating the currency was the key. History is repeating itself. We don't need a new playbook for trading Abe. Just look at Takahashi's playbook. Abe's success was deflating the currency to save Japanese corporations. This is an inflation trade. The catalysts are led by history. The risk is exogenous. Trade wars with China may get in the way. Japanese retail investors are buying Australian, Mexican and American. Finally, we construct trades from the top-down. We look at the equity, the currency and rate markets. At this point in the cycle this is a beta trade with an emphasis on financials. Targeting other sectors will not deliver better returns. Just go long. It's a consensus trade that requires risk management because the pull backs will be nasty. We like to short the yen against the dollar, the Mexican peso and the Australian dollar. Don't fight the Bank of Japan. Trade wars will hurt the yen in the short run. In the long run the yen will outpace Japanese stocks. Japan is still underweighted in most portfolios. We think this is the second or third inning of the Japan trade. One of the tricks of momentum is getting in after a big move. Higher prices feed higher prices. Don't be afraid.


Robert Macrae

Robert Macrae
Arcus Investment

The parallels to history are persuasive. Coming off the gold standard and shrinking those big debts were the solution. You need inflation or the expectation of inflation to get started. For 20 years, Japan has been the worst place to invest. In the last four months, their market rose to just below book value, with competitive dividend yields. There was no evidence of distressed companies. There was no debt. This was the rare case of a Japanese politician (Abe) with a good idea. His plan is real. But will it work? What can go wrong? Change has been moving too slow. If the world economy slows down it will be tough for Japan to progress. The MoF is a threat. Their mission is to balance the books. Every time the economy shows improvement, they want to raise taxes. The BoJ will follow the lead of the new government. Korea has protested the big move in the Japanese yen. This cross rate sets the price for many consumer goods. Korea won't allow too much appreciation as the yen unwinds against the won. China's faith in their benevolent political leadership is too good to be true. Because of the belief that China's economy is growing so fast, any fantasy to buy debt can be justified, because in the future the economy will be so big, the debt will be relatively small and all the trains to nowhere and the empty office buildings will be put to use. My experience with Japan is that this belief is unwise. Everyone knows China has a terrific balance sheet with cash hordes built-up by exporting. Most domestic assets are built on real estate. Given the primitive state of property law, prices are set by one politically connected entity to another. Valuations are theoretical. The country is large, unstable and rather hostile. I don't trust their balance sheet or their income statement, and I don't rate their management. I don't buy the China story. As the biggest export destination, this is a problem for Japan. We're actively engaged in hedging away the China risk from our Japanese portfolio. There's a new problem with Abenomics. If inflation erupts, bond prices will rise and the government won't be able to pay its debts. The evidence shows this isn't happening. We've had four years of expansionary policies in the West and bond prices haven't risen. It's wrong to consider bonds in isolation. Japan is a nation of savers and the government has been the spender of last resort. This is a dumb way to run a country. But people are beginning to spend. If they spend on entrepreneurial activity, Japan will become a healthy economy. Deflation has been punishing entrepreneurs for 20 years. The roughly 20% currency move is big. This should translate into a 30% increase in corporate earnings. Japanese equities still look cheap. Since 2009, investors have paid a premium for stable earnings in places like the private railway and food companies. Financial and operational companies have been discounted. There's been no change in market leadership especially around a big event. The valuation structure is still very interesting. After two decades of disappointments, investors have abandoned Japan. Japanese equities may be the best performer over the next decade.

Alex Kydd

Alex Kydd
Sloane Robinson LLP

What's different in Japan this time? There's a reflation plan. This is the first time the authorities share a common agenda. The authorities understand that nominal GDP growth will allow growth in taxes, which will solve the massive debt problems. Gross debt to GDP is 230%. 1990 tax revenue was 60 trillion yen. Today it's 42 trillion. Reflation possibilities are compelling news for equity investors. Before reflation the environment was fertile, especially for reformer companies. Corporate Japan has responded to reflation with operational efficiencies. Fixed expenses have been cut by 12% and variable expense reductions have been sustained. Toyota has been a superb reformer. They are now profitably exporting at a yen-to-dollar rate of 79. They cut fixed expenses by 10% in 12 months. Panasonic is a non-reformer. In five years they've accumulated losses of $20 billion and destroyed 65% of their book value. Hitachi is a reformer who withdrew from unprofitable markets. Management is obsessed with its competitor's cost structure. Hitachi's goal is to double its profit margins to 10% by 2016. NEC is a non-reformer with poor margins, unpredictable earnings and low returns. Some companies have improved their focus on ROE and some haven't. The market, as measured by the TOPIX, had an ROE of 3% in the 1990's. Today it's 6%. The market ROE is holding up much better than in past cycles. Reformer ROEs are 20%. What happens when reflation hits this fertile ground? Inflation means domestic companies can reclaim their pricing power. The weak yen is a transmission mechanism and a consequence of inflation. Reductions in operating costs mean strong operating leverage from a weaker yen. The third benefit of reflation is monetary easing. This is good for real assets. Japanese REITs would turn around with office vacancy rates peaking and residential rentals bottoming. What effect does reflation have on valuations? The TOPIX will deliver 10-14% ROE in 2014 due to cost-cutting, a weaker yen, operating leverage and reflationary impact. What are the risks? There's political risk in politicians losing their resolve. There's fiscal risk in the size of the debt mountain. 92% of government debt is held by on-shore Japanese. There's international risk that a global slowdown will derail the domestic economy. Sino-Japanese tensions were inherited by two new governments and common sense will prevail. An appreciating yen will hurt corporations. I expect a depreciating yen. It goes in long cycles and we're just beginning a new cycle. Takahashi's example was correct. Under Takahashi, real GDP grew by 60%, the yen depreciated by 60% and the Nikkei rose by 79% between 1931 and 1936. Corporate backsliding is a risk. Will Japanese corporations go back to funding unprofitable ventures? Good stock-picking will sort out the offenders. I believe Japan will reflate. Japan is a multi-year investment opportunity that's independent of inflation.

Since our March meeting, the TOPIX is over 15% higher and the yen has depreciated against the dollar by roughly 5%. However, this trend was shaken badly during May and June, on concerns over the BoJ's effectiveness and overall investor concerns about the knock-on implications of the Fed's announced plans to taper U.S. monetary easing. So far, Abenomics appears to be delivering early results, as inflationary expectations are rising and Abe's party convincingly won control of the upper house in the July elections. These recent mile markers suggest the prescience of our panelists' positive views on the long-term direction of Japanese equity markets.

Fellows:

Muhammad Al Agil
Philip Andryc
Trevor Barnett
Michael Castine
J. Patrick Cave
Douglas Cullen
Kurt Dalton
Peter DaPuzzo
Charles Davidson
Lyman Delano
Tom Dunn
Ronald Fingerhut
Scott Frantz
Ed Glassmeyer
Claudia Hardin
George Hubbard
Meredith Jenkins
Erica Ray Johnson
Barbara Justiz
Nigol Koulajian
John Loeb, Jr.
Susan Lynch
Peter Malkin
Lansing Martin
Rui Mendes
Juan Meyer
Joanna Migdal
Brian Miller
Morgan Mitchell
Richard Papetti
Jose Mario Quintana
Xenia Razinski
Daniel Rizzuto
Sami Robbana
Margarethe Rokkum-Testi
Adrian Sales
Kent Scott
Robert Steel
Robert Stone
Daniel Tapiero
Bruce Nelson Terry
Fred Weintz Jr.
Frank Helmut Weymar

Founding Members

Charlie Eaton
Marilyn Freeman
Luke Imperatore
Thomas Isreal
Stephen McCarthy
William Raver
Ken Shewer
David Storrs

Members of Record

Benjamin Alimansky
Colin Ambrose
Edgar Barksdale, Jr.
Brett Barth
Lawrence Bartimer
Dean Benner
Rodney Berens
Spencer Boggess
Susan Carter
Laurent Chaix
William Cody
George Crawford
James Crystal
Mark Dalton
John Daly
Rian Dartnell
Robert Davis
Alain De Coster
Susan Dubin
Graham Duncan
Alan Fischer
Brian Fitzgerald
Robert Goergen
John Griswold
Ray Gustin IV
Jonathan Harris
Phillip Harris
Elizabeth Hilpman
James Hodge
Von Hughes
Heather James
Mary Ann Johnson
Jeffrey Kelly
Peter Kimmelman
Lillian Knight
Jeff Landle
Peter Lawrence
Ernest Liebre
Leo Marzen
Brian Matthews
Carol McFate
Jamie McLaughlin
David Minella
Matthew Mordus
Robert Niehaus
William Orum
Thomas Peterffy
David Phillips
Todd Pines
Afroz Qadeer
Rip Reeves
Jon Rotolo
Robert Salomon, Jr.
Alberto Santulin
Ted Seides
Chris Shumway
Jeffrey Silverman
Mark Silverstein
Roy Simpson
Ian Slome
Barry Sternlicht
Mark Stitzer
Ryan Tie
Seth Tobin
Robert Voreyer
Susan Webb
Dr. Thomas Weber
Casey Whalen Sellers
Richard Witmer
Tamara Yiannakou
Cliff Yonce
Philip Zecher
Kellie Zesch
Paul Zummo

Associate Members

Hamad Ali
Abby Barlow
Afsaneh Mashayekhi Beschloss
Heinrich Blennemann
Lawrence Bowman
Robin Bradbury
Jack Buchmiller
Mary Cahill
Terri Chernick
Hugh Culverhouse
Ward Davenport
Sally Dungan
Richard Elden
Michael Fisher
Ben Funk
Shane Galie
Richard Gass
Nathan Gelber
Gwendolyn Goffe
Jonathan Hook
Brian Kaufman
Chris Kleinert
Lawrence Kochard
James Larkin
Laurence Morse
Dr. Joseph Nelson
Gumersindo Oliveros
Hunter Reisner
Eckhart Richter
David Salem
J. Scott Simon
Pascal Spielmann
Paula Volent
Aleksander Weiler
David Weinstein
Mark Yusko

Underwriter's Council:

Commonfund Institute
Flag Capital Management
HedgeServe Limited

Research Council:

BlackRock, Inc
Blenheim Capital Management
Bridgewater Associates, Inc
Halcyon Asset Management
The Orchard Farm Foundation
Tudor Investment Corporation

**THE GREENWICH ROUNDTABLE IS A NOT-FOR-PROFIT ORGANIZATION.
WE RELY ON YOUR CONTRIBUTIONS FOR OUR FUNDING. WITH YOUR SUPPORT, WE WILL CONTINUE OUR PURSUIT OF EXCELLENCE.**

The Greenwich Roundtable

One River Road, Cos Cob, CT 06807

Yes, I will make a contribution* in the amount of:

$100 _____ $250 _____ $500 _____ $750 _____ $1,000 _____ $3,000 _____

My enclosed check is made payable to "The Greenwich Roundtable, Inc."

Name ______________________ Phone ______________________

Company ______________________ Email ______________________

Address ______________________

City/State/Zip ______________________

*Contributions are tax-deductible and eligible for "Corporate Matching" programs.

The Greenwich Roundtable

One River Road
Cos Cob, CT 06807

The Greenwich Roundtable Letter

KNOWLEDGE, VERACITY, FELLOWSHIP

2013

The Greenwich Roundtable Inc.
One River Road
Cos Cob, CT 06807
Tel: (203) 625-2600
Fax: (203) 625-4523
rsvp@greenwichroundtable.org
www.greenwichroundtable.org
www.grbestpractices.org

Expanding Our Curriculum to Academia

The Education Committee will be presenting a series of Best Practices lectures at the leading business schools as part of its mandate to share our research to the broader investment community. Members of the Committee will be bringing the *Best Practices in Alternative Investing* series to the next generation of investment professionals as we begin to collaborate with Columbia, NYU, and Fordham.

Mark Silverstein, Chairman of the Education Committee and Trustee said "This program executes on our mission of education for investors. We are reaching a segment of the next generation of professional investors and sharing the vast knowledge and experiences of our membership developed over years that are refined in our Best Practices white papers." While the Committee has developed and shared Best Practices over the past decade, the educational outreach at Columbia and Fordham is intended for students who will be entering the industry in the New York metropolitan area. In all, the Committee has penned seven white papers focusing on a range of topics from due diligence on various strategies to case studies on how to avoid mistakes in manager selection and monitoring.

One of the most important aspects of the lecture series will be its ability to share the experience of our committee members. Various members of the committee will be presenting different Best Practices, personalized to highlight the lessons they have learned over their careers. If you are interested in lecturing or in organizing a series of lectures at your alma mater, please contact Mark Silverstein at msilverstein@enduranceservices.com.

Education Committee Chairman's Update

Over the past years, the mission of the Education Committee has been to undertake projects which document the knowledge and experience of our membership and redistribute it for the benefit of all interested investors.

In 2012, we completed our seventh Best Practices whitepaper, Avoiding Mistakes, which examines the causes of hedge fund failures and helps investors develop the tools to prevent being involved in such a fund. Aside from outright fraud, the most common causes were inappropriate combinations of leverage, complexity and illiquidity.

With a range of content now developed, from Due Diligence to Portfolio Construction to Avoiding Mistakes, our focus has shifted to sharing this valuable material with a wider audience. To start, I encourage you all to take advantage of this material and share it with others. This year, the Education Committee has been working on a number of projects to meet this goal. A dialogue has started with the CFA on ways to cooperate. To date, they have started to post our materials on their website. We have also started a program to work with MBA and Finance programs to assist in the classroom and with clubs, using our Best Practices materials as a core for mini curriculums and lectures.

We continue to explore other ways to reach a broader, yet appropriate audience. Rest assured, the Thursday symposiums will always remain an exclusive benefit for Greenwich Roundtable members.

I want to thank all the members who have taken part in Education Committee which has been core to our mission as an organization. It has been a mutually beneficial activity and we welcome participation from our membership. The value of our output for all the membership is directly related to the involvement of individuals. The Committee and the Board of Trustees appreciates your support and contribution to these activities.

Regards,

Mark Silverstein

THE GREENWICH ROUNDTABLE IS A NOT-FOR-PROFIT ORGANIZATION. WE RELY ON YOUR CONTRIBUTIONS FOR OUR FUNDING. WITH YOUR SUPPORT, WE WILL CONTINUE OUR PURSUIT OF EXCELLENCE.

The Greenwich Roundtable

One River Road, Cos Cob, CT 06807

Yes, I will make a contribution* in the amount of:

$100 _____ $250 _____ $500 _____ $750 _____ $1,000 _____ $3,000 _____

My enclosed check is made payable to "The Greenwich Roundtable, Inc."

Name ____________________ Phone ____________________

Company ____________________ Email ____________________

Address ____________________

City/State/Zip ____________________

*Contributions are tax-deductible and eligible for "Corporate Matching" programs.

The Greenwich Roundtable
One River Road
Cos Cob, CT 06807