



# GLOBAL VIEWS

4th Quarter 2011

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Schreiber Associates International

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### Schreiber Associates International

Chemin Champ du Lac 1  
St Sulpice; VAUD 1025  
Switzerland

Tel: +41 (0) 22 548 3712  
Fax: +41 (0) 22 594 8812

Email: [info@s-aint.com](mailto:info@s-aint.com)  
Web: [www.s-aint.com](http://www.s-aint.com)





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## Exchange Traded Investments (ETI)

Many investors will hold the above. Sometimes you will hold them and not even be aware, as many fund managers utilize ETI within portfolios. A classic example would be the use of an ETI in a managed fund to gain an exposure to commodities - gold especially. The issue with gold is that some gold funds actually buy the physical commodity, some ETI track the value, and others actually buy gold mining shares, such as BHP, where the price will tend to follow that of actual gold, but not precisely.

However, whilst there are some distinct advantages of utilizing an ETI, (e.g to get exposure to gold), such as high liquidity (selling an ETI is a lot simpler than selling a lump of gold), there are also many pitfalls. One pitfall, which the regulators have highlighted, is being able to identify exactly what the ETI does.

Hitherto there have been three main forms of ETI. Exchange Traded Funds (ETF), which tend to track stock market indices Exchange Traded Commodities (ETC), which aim to track commodity prices and Exchange Traded Notes (ETN), which can be linked to the price of a variety of assets.

ETI were launched in the early 1990s, and have grown to over 2500 available, representing almost £1.0 trillion in investments.

Their rise in popularity and use has meant the number and range has grown massively. In addition to the more traditional ETI, there are now a number which seek to "short" the market, to attempt to make money when the market falls. In addition a number of newer offerings also employ leverage to increase returns, (and of course risk).

There is also concern when ETI utilize derivatives in order to access an asset. This will frequently lead to tracking errors as the synthetic price is not always exactly aligned with the real price. This may also lead to the ETI having to close its position and buy another position in order to realign.

The moral of the story is, do your research and ensure that you are buying what you want, or ask us. We have the research tools at our disposal to assist.

## Who Wants to Be a Millionaire?

That's what the song said - nowadays the song might not sound so attractive, since to be a millionaire now, according to those that know, you actually need around 6.0 million - and we are not talking Zloty.

Obviously a million does not go as far these days as it used to. Inflation still exists however much you have, and the price of a Ferrari or a luxury yacht continue to rise.

Nonetheless being a millionaire in whatever currency, say USD, Euro or GBP here, is an important step on the road to financial freedom.

## Swiss Banking May Not Be So Watertight After All

For centuries a Swiss Bank has epitomized, in films and folklore, the realm of the ultra-wealthy, or for those who needed to keep things very secret (after all even Jason Bourne had one).

However, recent events have shaken the Swiss Banking industry to the core, and suddenly having a Swiss Bank account may actually be a liability.

A series of "arrangements" have been made with UK, American and other EU countries to make deductions from client accounts and to pass "tax" revenues.

Also in recent news, a former Swiss Banker, Rudolf Elmer, allegedly provided WikiLeaks with a list of star celebrities and wealthy individual's corporations, totalling 2000 clients from his former Swiss Bank.

Apparently the banker has had sudden pangs of remorse about his role in cheating the system. He states that the disclosure of the names will shock the world. Perhaps his motives are true, but it is interesting that his sudden pang of conscience only came after his employer fired him. He subsequently spent 30 days in prison for breaking Swiss Banking law, for forging documents and sending threatening messages to bank employees.

Add to this the recent news of fines for UBS from the US Revenue Service, and a series of disastrous investments from other Swiss Banks and it is easy to see how the allure is fading.

However, it must be remembered that the Swiss currency, the Swiss Franc, has traditionally been one of the most secure currencies in the world, and historically deposits in Swiss Banks have been backed by at least 40% in gold reserves.





## Inflation: The Silent Embezzler

*"Inflation is as violent as a mugger, as frightening as an armed robber and as deadly as a hit man."* Ronald Reagan

The former US president said these dramatic words in the early 1980s, shortly after US inflation had reached 13.5% in 1979. He may have been over dramatizing but the pronouncement was made in order to shock the US corporate and private sector into accepting the forthcoming tightening of monetary policy.

We would argue that today inflation is more of a silent assassin or perhaps an embezzler and it is in the interests of policy makers in developed markets to allow a prolonged period of above target inflation in order to manage their enormous debt burdens.

As an example, the UK uses two measures to monitor inflation, the Consumer Price Index (CPI) and the Retail Price Index (RPI). The Bank of England's (BOE) mandate is to maintain CPI at 2%. However, over the 12 months to the end of August 2011 the CPI index has risen 4.5% and RPI has risen by 5.2%.

With real interest rates therefore at -4% (CPI at 4.5% and BOE Base Rates at 0.5%), savers are therefore seeing their real wealth contracting at an alarming pace.

We expect that due to the massive debt and deficits in the West, inflation will remain much more persistent than the consensus view.

*"Inflation is the one form of taxation that can be imposed without legislation."* Milton Friedman

Western Governments are incentivised to monetise their debt (print new money to pay old debt), thereby destroying the real value of that debt. Over the past decade, UK M4 (a broad measure of money supply used by the BOE) has risen from £0.8 trillion to £2.2 trillion (9.5% per annum growth). Generally, when the growth in money supply is greater than economic growth, inflation is the result. We believe inflation from this rapid increase in money supply has previously been masked by deflationary forces coming from China. Outsourcing to emerging markets reduced the cost of goods produced and increased Western productivity dramatically. However, emerging markets are now becoming an inflationary force, as they fight their own inflationary battles and compete for resources with the West.

Almost every investor has the need to grow their investment portfolio at a rate above inflation. Any return less than inflation is actually destroying their purchasing power, but not many investments are designed with this specific objective.

This has put investors in a difficult situation. The fund management industry has been slow to create solutions with target returns and risk constraints aligned with their client's needs. Most products are linked to equity markets or bond indices and peer groups. These products are blunt instruments which may beat inflation by chance, but do not have this as their core objective. Many cautious investors are drawn to the lower volatility and safety of government bonds. Unfortunately we believe many of these investors

are at the greatest risk of losing ground to inflation as UK 10 year gilts yield 2.8% (at end August), which is also less than the CPI.

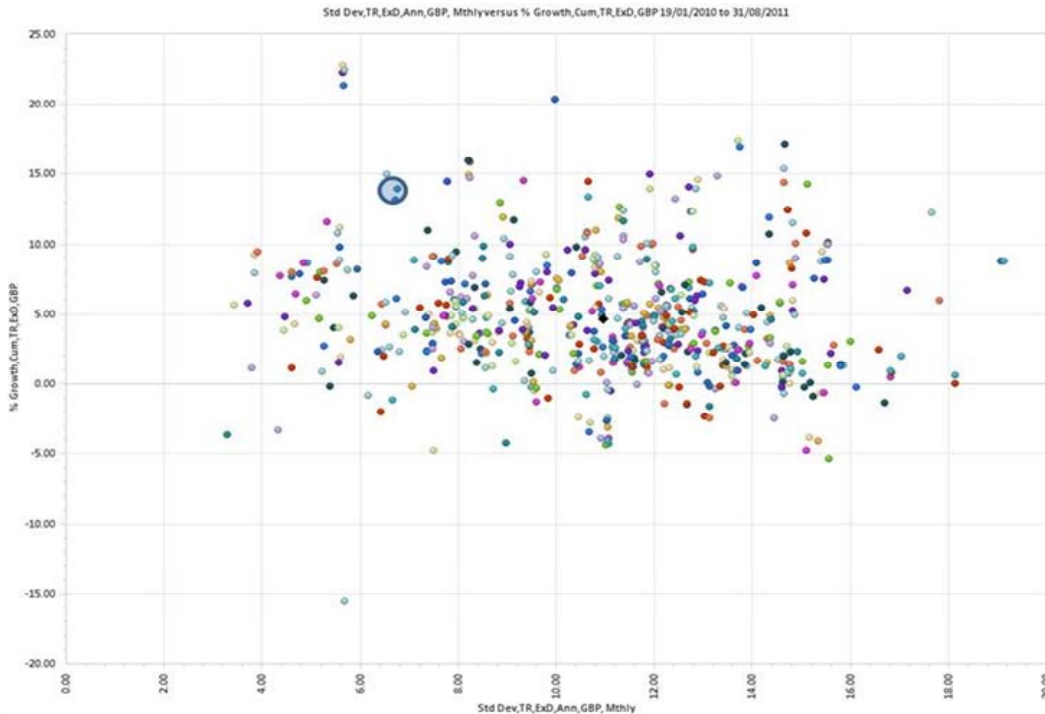
Many investors look to equities as a higher risk asset class with the potential to protect their portfolios from the ravages of inflation. Historically there has been a strong relationship between inflation and the P/E (price divided by earnings) multiple the markets put on earnings from equities. However, inflation can also hurt equity prices. As inflation rises the P/E multiple tends to fall and unfortunately the narrowing of P/E multiples have been particularly pronounced in periods when CPI has moved above 6%.

We believe the most robust way to invest for inflation is to consider a broad and truly diversified range of opportunities which can deliver a yield or capital growth above the rate of inflation.

The AIM DRR+ fund has this as its core investment objective .

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The AIM Diversified Real Return Plus (DRR+) Fund:

DRR+ targets inflation + 4% per annum over a market cycle with a third of equity risk. This is in line with total returns on equities per annum over the past century. DRR+ invests in all liquid asset classes and a vast range of instruments on a global basis thus contributing significant diversification to any portfolio. DRR+ is transparent, daily liquid and available in EUR, GBP and USD.

Armstrong's Diversified Real Return (DRR) Fund has consistently delivered market leading risk adjusted returns since launch - annualized return of 13.9% an annualized monthly volatility (standard deviation) of 6.8% since its launch on 19/01/10 to 31/08/11. This results in a Sharpe Ratio of 1.0. The fund is 7<sup>th</sup> out of 448 funds in the 2.0. IMA Managed sectors.

Fund summary/Key points

- Comprehensive growth solution suitable for low to medium risk investors
- Excellent liquidity - daily dealing / no redemption notice required
- Multi asset strategy, ability to invest in all liquid asset classes for maximum diversification
- Delivers market leading risk-adjusted returns targeted to beat inflation + 4%
- UK FSA regulated Investment Manager
- Third party administrators, custodians and auditors

Armstrong Investment Managers (AIM), an award winning investment team that has been working together for more than a decade during which time they founded the Managed Accounts

Program (MAP) at UBS and the Multi-Asset Group (MAG) at Insight Investment (Halifax Bank of Scotland) while managing \$6 billion and \$2 billion respectively.

AIM's focus is on the delivery of risk-based, inflation-benchmarked investment solutions. The reason why Armstrong focus on risk and inflation is because the primary concern for most investors is the risk of losing capital in the short term and beating inflation in the medium to long term as inflation is the ultimate destroyer of everyone's purchasing power.

For more information please contact us.





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## We Live in Troubled Times

There is no getting away from it - the markets are in turmoil. A combination of the concerns around the US and Euro zone debt is making life very uncomfortable for investors.

In such volatile times you may well be watching the value of traditional investments (e.g. mutual funds, company shares) dropping almost daily. But not all investments are impacted in the same way by such market events. Autocall notes are a great example of an investment which can weather the financial storms.

Autocall notes are designed with two things in mind. The first is an attractive return, seeking around 2-3 times top deposit rate return, and the second aim is to deliver those returns with a low level of risk to capital.

A typical "safety net" of 50% is built into these investments. It means a market would have to halve before you lost any of your original capital, thus protecting you against anything but the most catastrophic fall.

As an example the FTSE100 recorded a year to date high of around 6100. However at its current level of around 5200 the index would need to fall below 2600 before your capital is at risk. That level has not been seen for over 15yrs.

So why is it a good time to invest?

- More volatility increases the returns on offer - up to 20%+ p.a.
- Lower start levels mean markets have to fall to levels not seen for 15+ years before capital is at risk
- More likelihood of a market recovery triggering an early maturity

Even if the current conditions carry on for a while you don't have to worry about your capital and if markets recovered to their initial level in for instance 3 years time you would receive 3x the stated annual coupon. It is often better for a note to call later in its life and deliver multiple coupons as a return of perhaps 30%+ after 3 years when markets are only slightly up can be very satisfying. It is certainly not a disaster if the notes don't call at the earliest opportunity.

As advisors, we plan for poorly performing markets when selecting suitable products for our clients to invest in as we want to help you continue to make money in these difficult markets and avoid any particular unpleasantness for you, the investor.

We'll continue to pay attention to the downside risks involved with investing (bank monitoring, proper consideration of underlying investments) as well as highlighting the positive benefits we hope to provide for you as a valued client.

To find out more about how an autocall note could be right for you please contact us without delay.

## FTSE to Rebound by Year End

This is the view of a large number of Bank Investment Houses, and analysts. The broad consensus is that the FTSE will close close to 6000. (Currently 5200 ish).

It has to be recognized that many of these experts are the people who were predicting at the start of the year the FTSE would close at 7000. There will also be a large number of them who got their investments so wrong they had to be bailed out by the government, which ultimately means you and me, as tax payers. So for me I will take the prognosis with a pinch of salt.

However, I will remain conscious of the fact that the FTSE 100 holds what are arguably the "best" UK companies. OK they are there because they have a large market capitalization, which does not necessarily make them the best. But many of these companies remain profitable, many have increased their dividend payments, many have seen their share prices fall due to the herd instinct of sell, sell, sell. Many of them have directors who are buying more stock, whilst the price is low, so perhaps there is a sound basis for the prediction.

Alternatively, you may follow the doomsday approach, where we enter a deep recession, sovereign defaults occur, the Euro fails, the US defaults and it's the end of the world, as we know it.

Happy investing.

