



3A
Alternative
Investments

Alternative Outlook

15 October 2009

Key Information at a Glance

L/S Equity	↗
Macro - CTA	↗
Arbitrage	→
Credit	↗
Event Driven	↗
Nat. Res., Commo.	→

6-month forecasts

Index Performance (HFRI FoF)

	MTD	QTD	YTD
<i>Composite Multi Strategy</i>	1.64%	4.33%	9.75%
<i>Conservative Low Volatility</i>	1.23%	3.54%	8.32%
<i>Diversified Multi Strategy</i>	1.65%	4.28%	9.63%
<i>Market Defensive Short</i>	0.80%	2.20%	3.88%
<i>Strategic Long Short</i>	1.88%	4.97%	11.14%

Estimated figures as at 30 September 2009

The investment community has been welcoming the growing idea of a recovery this year after the apocalyptic scenarios that were being increasingly discussed last year. The seven consecutive positive months of stock market gains and the impressive rally in the credit market have been supported by positive economic news flow, and have been perceived as a sign that the actions taken by central banks and government are having an effect. Nevertheless, the question whether markets are overbought and the issue of valuations reaching pre-Lehman levels is at the front of most managers' minds. Whether their strategies are bullish, uncertain or even radically bearish, most of the strategies are being implemented in a cautious manner. What is interesting to note is that managers' longer-term views do not necessarily match their positioning and may differ substantially as the bulk of them have developed a more trading-oriented approach to cope with the current environment.

Our favoured strategies, which are Equity Long/Short and Global Macro, typically have the flexibility to react quickly and adjust their positioning as well as their views. We continue to focus our screening efforts on some very appealing Asian hedge funds strategies where we think we have an edge thanks to our presence in Hong Kong. In addition, we have started to take a closer look at credit managers that offer an exposure to the credit cycle in a way we could be comfortable with, i.e. a clear view of the underlying investments and appropriate liquidity terms. The number of opportunities for alternative strategies is important and genuine and we therefore consider that the current timing is very attractive for investing into hedge funds.

Outlook by Strategy

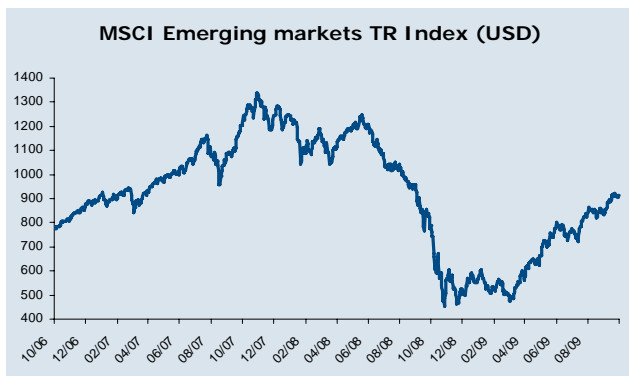
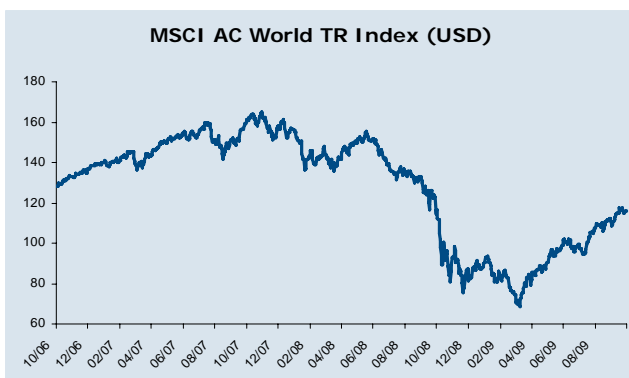
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Outlook by Strategy

Long/Short Equity

The majority of Long/Short managers have fared relatively well this year. Those that proved most robust last year have found it difficult from a valuation standpoint to ramp up the net and gross and ride the much-debated rally. Only a few managers have managed to outperform the markets since their lows in March, and those that did, may have had a little bit of luck on their side with regards to their timing.



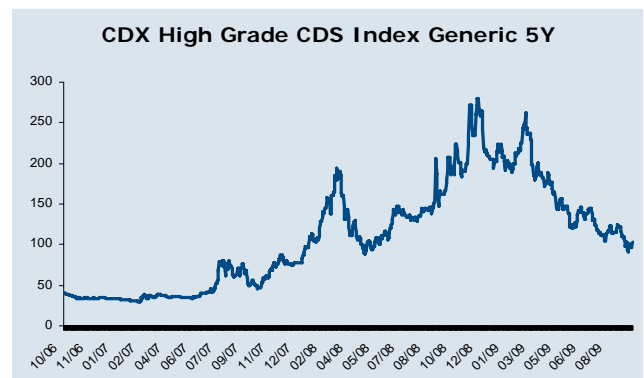
Market dynamics have changed and will change going forward. An increasing number of managers believe the most beaten-up stocks of 2008 have had their rally and left the 'good quality' companies behind. As mentioned in previous newsletters, the time for identifying stock dispersion by filtering the sound companies within each sector from the companies with deteriorating fundamentals and weak business strategies, is over. This process will have its natural outcome in good time but going forward it is only the consumer that can keep corporations growing. The US is becoming increasingly competitive on an international basis and is well ahead of Europe on its toxic asset write-down plan. We expect the US to be the leaders of recovery in the West, and thus offer opportunities on both the long and short side, with Europe following behind.

Event Driven

There have been opportunities in all spaces. The tempo has not been at its fastest for sometime now but within restructuring, share conversion, capital raising, rights issues and Mergers and Acquisitions there has been enough to do. The new era underscores the fact that managers need to fully understand what they are doing and more importantly to size and diversify their books accordingly. Managers have to be active as the current environment is still choppy and potentially vulnerable to government intervention in one way or another, which could again result in unconventional outcomes, as we have seen in the past.

Credit

September was another good month for Credit strategies. The widening that occurred in August was short-lived as the credit spread across the board tightened again and more than offset the previous month's widening. The CDX Investment Grade and CDX High Yield Index tightened by 13.75% and 14.95% respectively over the month and the picture in Europe was no different as the Itraxx Investment grade and the Itraxx Higher volatility companies tightened by 2.49% and 14.22% respectively. The credit space has contracted in 6 out of the last 7 months, clearly helping credit managers; nonetheless, whilst we believe that there is still further to go in the credit space before normalisation, we truly think that the added value of managers relies on their credit selection. Going forward we are confident that there is still enormous value to extract from the strategy and, as long as the credit market remains rational, be it contracting or widening again, credit managers will manage to extract value from this market.



Arbitrage Strategies

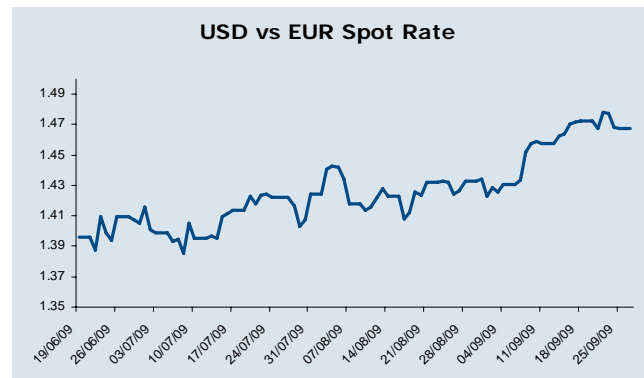
Convertible Bond arbitrageurs posted another strong month in September. They generated healthy returns in company specific trades, capturing volatility around the event. Going forward, we expect this approach to continue to do well as corporates still have an incentive to restructure their balance sheets. The new issue market has been buoyant in September with almost USD 11 billion of issuance with attractively priced deals.

Going forward, the convertible market will remain an attractive source of capital for companies as equity remains volatile and straight debt quite expensive. Implied volatility is taking an increasing role in alpha generation as new issues and the recent market rally increased the number of volatility-sensitive bonds. Leverage was higher and more accessible but remains well below historical values.

Statistical Arbitrage performed well over the reporting period and still benefits from the lack of competition. We anticipate above-average returns in this strategy for the coming month as the amount of capital chasing opportunities is much smaller. In the Fixed Income area, managers generally posted small positive returns. This strategy should continue to perform in line with expectations as long as fixed income markets' volatility remains high.

Macro & CTA

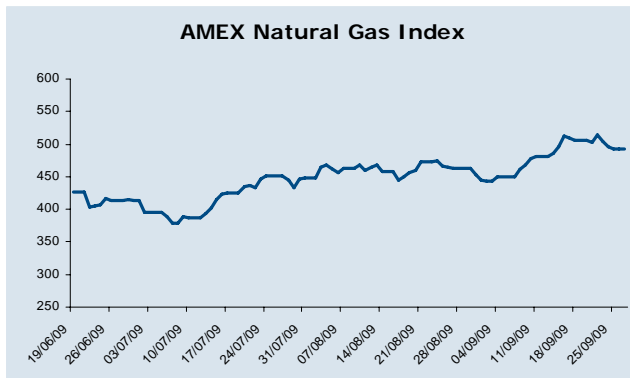
September was a decent month for CTA and Macro Systematic. Currency, namely short dollar positions, provided extremely good returns for all strategies. The short positions in the yield curve also proved profitable as both short rates and long rates came down during the month. Long metal positions, namely Gold, provided the third common pocket of returns across all strategies. Equity trading was more mixed as some funds had turned their exposure long, some had kept it short and others have been switching positions frequently during the month; nonetheless, overall Equity index futures trading was profitable in all strategies, i.e. medium-term, short-term and macro systematic. On the commodity side, energy and grains were trickier and generated some losses for the medium-term CTAs that were mostly long, while the short-term CTAs navigated the month well and managed to post positive performance, similar to macro systematic funds, which were mostly short throughout the month. September was the first month in a while now to show some consistent trends – although far from strong, they were strong enough for the strategy to take advantage of them. We believe that the inflexion period is slowly ending and that trends will gain strength going forward, which will benefit the strategy.



Natural Resources & Commodities

In September the commodity sector overall generally traded sideways. However, as it is often the case, some individual commodities displayed large, when not huge, volatility. Despite copper prices more than doubling since their lows in December 2008, and declining at the end of September on lower Chinese imports, several managers are bullish copper. Inventories are tight even for a low demand environment scenario and new mine developments will be necessary by 2012, otherwise global mine supply will fall short of world consumption. In precious metals, gold surged to USD 1024 per ounce in intraday trading on 18 September as investors focused on renewed weakness in the USD and concerns that government policies might prove inflationary.

In energy, crude oil prices traded sideways for most of the month on news flow that played against each other such as rising Chinese manufacturing offsetting weaker U.S. employment numbers. Volatility continued in the natural gas market, which displayed strongly steep contango. Prices reached a bottom at the beginning of the month and then bounced back sharply (up 85% from the lows!), as they probably fell below break-even costs and became unsustainable. Some managers with a focus on this market were hit in September as they lost on their front-end short positions. Similarly, some managers with a focus on softs whilst still long sugar experienced a volatile month. More generally, for diversified commodity managers, performance numbers were modest in September, and similar to the overall commodity market.



Several managers currently consider that the combination of economic conditions, bouncing back from lows and technical factors, will create strong upside for commodity prices in the near term. Also noteworthy is the renewed interest in commodities by institutional investors, including sovereign wealth funds, driven by China's story and dollar weakness. Long-only, passive investments (so not the type of investments that hedge funds pursue) have become popular again, as illustrated by the surge in assets under management in such products from USD 23bn to USD 86bn during the second quarter. Hedge fund managers generally don't complain about this phenomenon, as it increases markets liquidity and provides additional trading opportunities.

Chart sources: Bloomberg