Leveraged Low Risk

16 July 2009

Investment Committee

JYSKE GLOBAL
ASSET MANAGEMENT

Recommendation

We recommend investors with Medium, High Risk or Speculative profiles to invest in a leveraged Low Risk portfolio. We believe the present economic situation favor bond investments and the Low Risk portfolio is primarily invested in bonds. Furthermore, the leveraged investment takes advantage of a steep yield curve, borrowing at a low interest rate and investing in high yielding bonds.

Both Managed and Advisory clients with JGAM can invest in a leveraged Low Risk portfolio, but only a Managed portfolio can obtain the full advantage of the strategy.

Background

Year-to-date JGAM's leveraged Low Risk portfolio has been our best performing investment strategy. With one gear this portfolio has generated a return of 11.4% on 30 June (i.e. almost 23% pa.). Even though past performance is not an indication of future return we think there are strong arguments in favor of the Leveraged Low Risk strategy also for the rest of the year.

We don't believe the economic recession is over yet. As argued in the June memo on Asset Allocation Strategy we expect the turnaround to be L-shaped (not V-shaped). This means economic growth is not expected to return to normal levels in a foreseeable time. Lack of growth will limit companies' earnings potential and reduce the risk of inflation. This cocktail favor bonds and is a disadvantage to stocks. The issue on inflation is addressed in the July memo on Asset Allocation Strategy. We do not expect inflation to be a real threat for a very long time.

Another argument in favor of the leveraged strategy is the present steep yield curves. Short term interest rates are historically low whereas medium to long term bond yields are relatively high, the present recession taken into consideration. Furthermore, there is an attractive yield pick up on corporate bonds compared to government bonds, even for high quality corporate bonds which JGAM recommend. We expect the yield curve to stay steep as this "structure" is intentionally put in place by central banks to help distressed banks. Fundamentally, banks make a living from borrowing (client deposits) at low short term interest rates and lending to customers at higher long term rates. This "artificial respiration" is necessary if many banks shall not go bankrupt in a recession scenario where more clients must be expected to be unable to service their debt.

However, we emphasize that leveraged investments are risky investments. Leverage is like a "turbo" on a portfolio. As a rule of thump a non-leveraged performance of 1% becomes 2% with a one-time-leverage. However, a loss of 1% also becomes a 2% loss with same leverage. Furthermore, as the loan currencies are often not the same as the currencies we invest in there is also a significant currency risk to a leveraged investment. Hence, only clients with a proper risk profile will be accepted to invest in a leveraged portfolio.

Finally, leveraged investments can be obtained by both Managed and Advisory clients with JGAM. However, we recommend investors to take advantages of the Managed accounts when leveraging a portfolio. First, JGAM will monitor the portfolio actively and second, your portfolio can be invested in a wide range of global securities (not available for Advisory clients). With an Advisory account you will in most cases be limited to currency investments and therefore not be able to take full advantage of the investment strategy described in this memo.

Important notice

Lars Stouge is responsible for the Investment Committee and its Asset Allocation strategy. Lars can be contacted on mail lars.stouge@jgam.com or phone +45 8989 5902.

All investments involve risks. The price of currencies and securities and the price of various services follow the development in the financial markets. Past performance is not necessarily a guide to future return. Investment in a foreign currency or your own currency may result in losses/gains due to the market development.