EPH

EXPAT PENSION HOLLAND

ACTIVE INVESTMENT FUNDS

‘WHICH ASSETS/SECTORS/LOCATIONS?’

Investments

Expats who are interested in investing private capital can choose between investing in Individual Objects or Investment Funds.

We prefer Investment Funds as they in general:
- provide a much better spread and risk reduction;
- have substantially lower costs;
- offer a better liquidity.

Investment Funds

Passive Funds
These Passive or Tracker (ETF) Funds do not try to generate a better return on investment than the index. Thus they only follow the index at the lowest costs possible. This cost reduction is their only challenge.

Active Funds
Active or Vision Funds do believe that it is possible to in the long run outperform the index.

Often this leads to (substantial) additional costs. It is relevant to check if the additional profit outweighs the additional costs. Which is not always the case. Thus our critical attitude towards these funds.

As of now we will only focus on Active Funds in order to provide our clients objective general information.

Active Funds: Fundamental/Technical Analyses

Active Funds need to have a policy regarding the use of fundamental and/or technical equity selection.

Fundamental Equity Selection

This approach looks into the 'real' or fundamental value of the company and how this reflects in the stock price. The ideal would be to buy stock of a company with a strong financial and market position while the stock price still is undervalued (according to the Fund).

The idea behind this approach is that even as equity is a high risk investment, due to the good underlying company value the risk will be to some extent more acceptable.

Technical Equity Selection

This approach does not focus on the company. It only looks at the volatility of the stock price and what recent movements might mean for the future. It is about trying to predict future trends and act accordingly.

This approach has nothing to do with investing and is pure speculation. Even though we are highly critical towards this approach, it can't be denied that in the past it *sometimes* did work.

Active Funds: Sector Allocation

What is Sector Allocation?

Each economy can be divided into a number of different sectors which each have their own character.

A common enumeration is:

- Technology
- Financials
- Health Care
- Energy
- Industrials
- Telecom
- Materials
- Utilities
- Consumer Staples
- Discretionary

As Active Funds aim for the highest profit, they try to choose the sectors with the best prognoses.

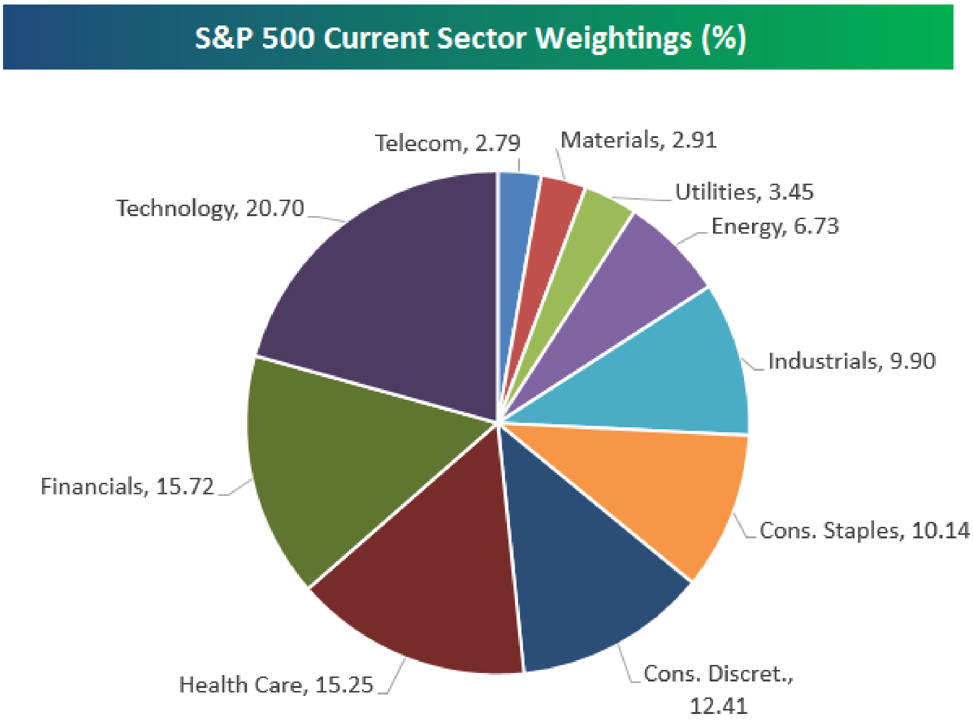
The business cycle has four phases which reflect fluctuations in the economy. Each phase may have an effect on sector performance. Historically some sectors tend to perform better or worse than others in certain phases. Monitoring the business cycle may help Active Funds to determine which sectors they should focus on during each phase.

For example:

- Cyclicle Sectors: They quickly react to a change in economic pace. Sectors like Construction/Chemical/Dredging/Employment Agencies.
- Non Cyclicle Sectors: They tend to have a more stable or defensive character. They often pay-out a higher dividend. Sectors like Supermarkets, Consumer Products, Utility, Real Estate. These sectors are often carefully compared with High Yield Bonds.

Example of Index Sector Allocation

The S&P 500 can be divided into 10 sectors and together they comprise the total value of the index in terms of dollar amount.



The Importance Of Sector Allocation

As each index has all sectors, this provides a certain stability. Active Funds lack that kind of stability. If they implement a specific approach and the opposite happens, the risk exposure is much more substantial. Active Funds that implement sector allocation agree to this additional risk.

Sector Rotation

This approach seeks to generate excess return through both sector rotation and factor-based security selection as well as risk management approach during declining economic environments.

The combination of maneuvering through sectors in various economic cycles and the expected ability to lower equity allocations might provide the portfolio with enhanced risk control. History has shown sharp equity market downturns correlate highly with economic slowdowns and recessions.

The Sector Allocation portfolio seeks to identify these disruptions as they occur and adjust allocations accordingly.

Active Funds: Global Allocation

Allocation of Equity/Bonds/Real Estate
After the Active Fund has determined the investment categories, it has to decide the global allocation thereof.

Why Global?
Global allocation of assets means to be able to in a professional manner evaluate economic conditions, currency issues, market opportunities and risks across the global landscape.

With a comprehensive global market viewpoint, it seeks to deliver more consistent returns with less severe drawdowns through all types of market conditions.

Which does not mean that this global allocation will always provide a higher return on investment at lower risk and lower costs than by means of a certain local portfolio.

Global Tactical Asset Allocation
This is a top-down investment strategy that attempts to exploit short-term mis-pricings among a global set of assets. The strategy focuses on general movements in the market rather than on performance of individual securities.

Three Type of Markets
Around the globe, investment regions are usually described as:

- Developed Markets: they represent companies in mature economies and efficient infrastructures, specifically for financial market transactions. For example USA/EU/UK.
- Emerging Markets: they provide the greatest opportunity for return, as they are some of the largest and fastest growing economies in the world. For example China/India/Brazil.
- Frontier Markets: they will offer the highest risk, as they are the least developed. For example Argentina/Koeweit/Vietnam.

Example: Global Equity Strategy

The equity strategy divides the world's stock markets i.e. into nine broad asset classes:

- Four USA related;
- Five none USA and international.

Existing research shows that over a long period of time:

- Eight of the asset classes have outperformed the S&P 500 while the ninth is the S&P 500.
- Some of the asset classes have even outperformed the S&P 500 by more than 10% average compounded per year. These asset classes do carry additional risk.
- When these asset classes are mixed together, because they have low correlations to one another, the resulting risk at the portfolio level is not substantially higher than the S&P 500.

Abandon Global Allocation?

The decision to abandon Global Asset Allocation should according to research only be made, if the investor is certain that he can consistently time the world's markets.

There is no evidence that any investor has been able to meet that test and no reason to believe that any ever will.

Active Funds: Conclusion

Due to the many complex and volatile aspects related to an Active Fund, we advise clients who prefer such a Fund to be highly critical when choosing their Fund.

It seems recommendable to only look at Funds who have:

- A risk signature that fits into the personal risk profile and investment horizon;
- The best reputation;
- Fine previous performances;
- Low costs.

International experience and Network

We have more than 20 years of experience in international expat and collective pension consultancy. Thus we have an elaborate international network. If so desired, we can advise and act swiftly in international matters.

Contact

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