



## Interesting Times – Where do we go from here?

Many of you are familiar with the Chinese curse, “May you live in interesting times.” Our present times are particularly interesting. Consider the global financial concerns, especially in Europe, but also here at home as Congress debates conditions attached to raising the deficit ceiling and whether the August 2<sup>nd</sup> deadline will even be met. Economic growth as measured by the gross domestic product (GDP) rose just 1.9% in the first quarter of 2011, which is significantly less robust than the 3.1% growth rate reported for the fourth quarter of 2010. And if you've take a trip to the gas pump or the grocery store, you are probably not surprised that the inflation rate reached 3.9% in the first quarter.

As you've no doubt read elsewhere, we are experiencing an unusual recovery from an unusual recession. In past economic downturns, the economy has come roaring back during the recovery, but today we are dealing with a more deliberate climb out of the hole. A quarterly survey of economists by the Associated Press suggests that the U.S. economic recovery will be slow and deep, held back by shoppers reluctant to spend and employers hesitant to hire. A poll of 42 economists concluded that economic growth will probably stay below 3% for the rest of this year and early next year, and their crystal balls say that the U.S. unemployment rate will end the year about where it is now: between 9.0% and 9.5%. GDP growth would have to reach 5% for a full year to drive the unemployment rate down by one percentage point; 125,000 jobs must be added each month just to keep up with population growth. In May, the latest month where we have statistics, 54,000 net jobs were added, down from 194,000 in March and 232,000 in April.

None of this is necessarily bad news for investors, but the rocky month of June which started with six straight days of losses in the U.S. markets, is further evidence that even positive growth and positive returns don't guarantee a smooth ride. The returns of the first half of the year have come with a certain share of anxiety, but it may be helpful to remember that the returns of 2009 came at a time when many investors were living in a state of fear bordering on terror. Let's count our blessings; the mild reversal of the past three months wasn't enough to offset the gains in the first quarter of the year for most of the elements in a *HAS* diversified investment portfolio.

## Executive Summary

- Good news - our diversified investment portfolios held up well during the recent downturn, thanks both to broad diversification and our emphasis on moderate and reduced risk investments.
- Economic recovery has slowed. Gross domestic product (GDP) rose only 1.9% in 2011 Q1 versus 3.1% during the last quarter of 2010.
- As always, many things could go right (Congress passes beneficial reforms) or could go wrong (think Europe and Greece). Thus a balanced approach is prudent, especially during the present times of heightened uncertainty.
- Because of global financial uncertainty, we favor reduced and moderate risk investments that offer upside rewards and downside protection.
- We detail Managed Risk and Opportunity Investing which is one of our four main client investment strategies. Our objective is to produce superior risk-adjusted returns, with special attention to both risk and reward.

## Managed Risk and Opportunity Investing

Given the current market environment, we decided it was especially appropriate to illustrate Managed Risk and Opportunity Investing which is one of our four main investment strategies. Our objective here is to produce superior risk-adjusted return, with heightened attention to both risk and reward. Part of our process includes careful selection of specialist fund managers who share our philosophy of downside protection and upside returns. Let's explore the type of fund we're interested in and then show some examples.

We like to find a market niche that's too small or too complex to garner much interest from big investors and then discover a smart investment team that devotes all of its efforts to that niche. This combination is often a recipe for investment success. Closed-end funds are a perfect niche for professional investors to target. Unlike a regular mutual fund, a closed-end fund typically issues shares just once, when it first goes public. After that, it trades like a stock – often selling at either a discount or a premium to the value of its underlying assets. Individual investors account for nearly 90% of the roughly \$200 billion in U.S. closed-ends.

These investors tend to buy high, sell low and pay a hefty 5% commission premium to their broker.

Closed-end funds issue a fixed amount of shares and they are traded on the stock exchanges or over-the-counter markets. When buying or selling closed-end funds, price is determined by the market environment and attractiveness to buyers and sellers. The price can be at net asset value (NAV) which reflects the underlying market value, above NAV (premium), or below NAV (discounts). When retail investors panic, driving price much lower than NAV, shares may be bought at significant discounts and at *HAS*, we like to buy these funds on sale when they trade at a discount.

A climate of fear in the market can create opportunities, like the chance to buy investments at attractive prices. For example, during the financial crisis in the fall of 2008, many closed-end funds were temporarily on sale at levels approaching 30%! When purchased opportunistically, closed-end funds can offer an ideal combination of global diversification, professional management, generous income and discount pricing. This combination creates a greater margin of safety along with boomerang potential to snap back quickly to profitable results. (Refer to the attached graph which illustrates average sale “discounts” over time in various market conditions).

One of our favored funds is the Cohen & Steers Closed-end Opportunity Fund, managed by Doug Bond. Doug has 30 years of industry experience and has originated over 150 closed-end fund offerings totally approximately \$50 billion. Doug has been generous with his time, personally sharing his wisdom and insights with me. (Thanks to Doug’s mentorship, I was featured in a Wall Street Journal article on closed-end fund strategies). This Cohen & Steers Fund currently offers a generous 7.7% distribution yield

and sells at a 7% discount (below NAV). The fund’s investment objective is total return, consisting of high current income and potential capital appreciation. To illustrate the “boomerang-back” effect, a \$10,000 investment in Cohen & Steers as of 3/1/2009 grew to \$20,876 as of 5/31/2011. The fund has returned 7.4% this year thru June 30th.

Another Managed Risk & Opportunity Investment, the Pimco Global Multi-Asset Fund is intended to be an all-weather investment that actively protects against the risk of a big market decline. The investment provides global diversification including stocks, bonds, real estate and commodities. To protect against market declines, this fund employs a risk-factor investment process along with “tail-risk” hedging strategy which may be likened to insurance protection. The management team employs a flexible, tactical approach that dials up and down risk-reward based on market valuations and perceived threats and opportunities. This year thru June 30th the Global Multi-Asset Fund gained 4.8% and 12.3% in 2010.

One final example is the Pimco All Asset All Authority Fund that provides complimentary strategies and diversification. The objective is maximum inflation-adjusted returns, consistent with preservation of capital. The manager handpicks a global mix of assets from an array of some 40 different Pimco funds. In 2010 +10.7% and 4.5% in 2011.

*Past performance is no guarantee of future results. All content in this newsletter is intended as general information, not specific advice. Performance data listed is for illustrative purposes only. Portfolios are personalized and often consider many variables, including investment objectives, age, time horizon, risk tolerance, client requests and tax variables. Information contained herein has been obtained from sources believed reliable, but not guaranteed*

***Hillegas Advisory Services is an independent Registered Investment Advisor offering investment management, retirement and wealth management services.***

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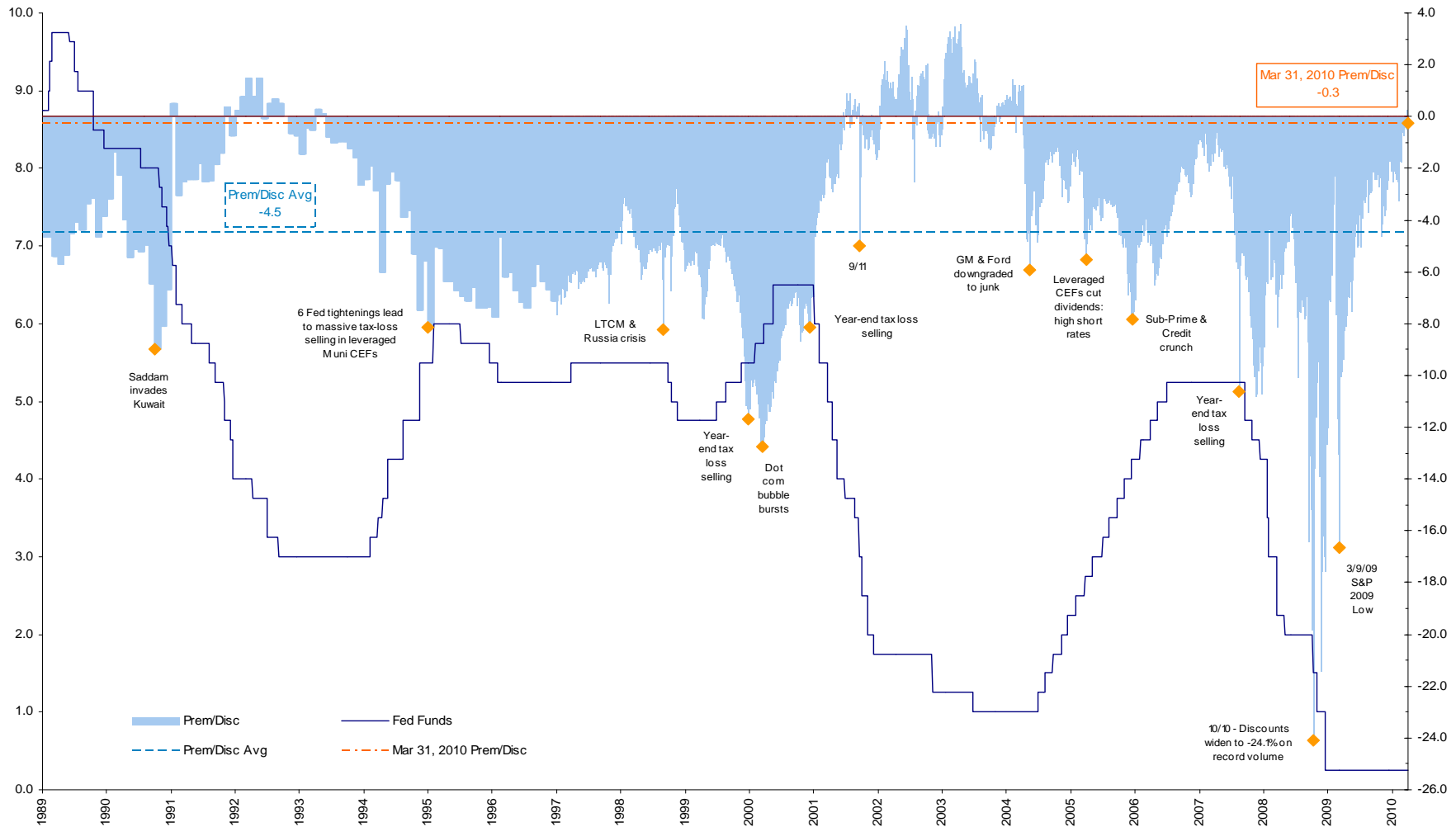
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# Historical Closed-End Fund Premium/Discounts

From January 1989–March 2010



Source: Fundamental Data (FundData.com), Bloomberg, Cohen & Steers.

Data is monthly January 1989–December 1996 and daily from January 1, 1997–March 31, 2010. Daily premium/discounts are of the FundData All Taxable Ex-Foreign Equity Closed-End Fund Index.

Note that the solid blue graph illustrates average closed-end fund premiums and discounts over more than 20 years. Wide discounts typically bounce back within fairly short time periods. The "Fed Funds" line illustrates the current Federal Reserve rate which remains at only 0.25% as of July 2011.

## Global Multi-Asset And All Asset : Different Approaches And Target Markets

- Both are compelling asset allocation strategies, though they have different objectives, processes and characteristics

Global Multi-Asset Fund	All Asset Fund
<p><b>GMAF Objective:</b></p> <ul style="list-style-type: none"><li>The Fund seeks total return which exceeds that of a blend of 60% MSCI World Index/40% Barclays Capital U.S. Aggregate Index.</li></ul>	<p><b>AAF Objective:</b></p> <ul style="list-style-type: none"><li>The Fund seeks maximum real return, consistent with preservation of real capital and prudent investment management.</li></ul>
<p><b>Process:</b></p> <ul style="list-style-type: none"><li>Allocations are driven by <u>PIMCO's</u> investment process</li><li>Based on a largely <u>qualitative</u> approach</li><li>Assesses exposure to key <u>risk factors</u></li><li>Risk management is <u>explicit</u>, including tail risk hedging</li><li>Implementation through the most efficient combination of <u>underlying PIMCO Funds and direct holdings</u></li></ul>	<p><b>Process:</b></p> <ul style="list-style-type: none"><li>Allocations are driven by <u>Research Affiliates'</u> investment process</li><li>Based on a largely <u>model-driven</u> approach</li><li>Assesses exposure to <u>asset classes</u></li><li>Risk management is <u>implicit</u>; no tail risk hedging</li><li>Implementation exclusively through <u>underlying PIMCO Funds</u></li></ul>
<p><b>Characteristics:</b></p> <ul style="list-style-type: none"><li>Seeks volatility comparable to that of a 60/40 blend<sup>1</sup> over a business cycle</li><li>Should be positively <u>correlated to 60 stocks / 40 bonds</u><sup>1</sup> over a business cycle (3-5 years)</li></ul>	<p><b>Characteristics:</b></p> <ul style="list-style-type: none"><li>Seeks volatility comparable to U.S. TIPS<sup>2</sup></li><li>Should be positively <u>correlated to U.S. TIPS</u> over a business cycle (3-5 years)</li></ul>

<sup>1</sup> As represented by the secondary benchmark of 60% MSCI World Index / 40% Barclays Capital U.S. Aggregate Index.

<sup>2</sup> Represented by the Barclays Capital U.S. TIPS Index.

Global Multi-Asset Fund Total Annual Fund Operating Expenses (Institutional Share Class): 1.58%

All Asset Fund Total Annual Fund Operating Expenses (Institutional Share Class): 0.885%

Refer to Appendix for additional index and risk information.