

December 2010

Welcome to our Christmas edition of the Quartet Capital Partner's newsletter. As with previous newsletters we report on our investment performance, our views on portfolio asset allocation going forward and Quartet Capital's development.

Quartet Capital focuses on providing discretionary investment management services to high net worth private clients. We believe that the approach we take really is *different* and as a reminder, we have set out what we do at the end of this newsletter.

Absolute Return Partners LLP (ARP) is a founding partner of Quartet Capital and we rely heavily on their economic views and analysis in constructing Quartet Capital's portfolio asset allocations. ARP's latest newsletter is attached for your interest.

### Investment Performance

Although all our client portfolios are bespoke, we reference each portfolio against one of four model portfolios dependant on risk profile to ensure we are not deviating too far from how we would like to position a client for assuming a defined and agreed level of risk.

	1 Year ended 31 July 2010	Quarter ended 31 October 2010	1 November 2010 30 November 2010	Since Inception
<b>Risk Profile</b>				
- Capital Preservation	7.39%	1.89%	0.27%	9.72%
- Cautious	10.31%	2.24%	0.06%	12.85%
- Balanced	15.71%	3.99%	0.47%	20.89%
- Aggressive	15.44%	4.72%	0.34%	21.30%
<b>Benchmarks</b>				
FTSE UK Gilts All Stocks Index	2.74%	1.27%	-1.42%	2.57%
FTSE All Share Index	15.38%	8.13%	-2.54%	21.59%
FTSE World Index	8.40%	8.83%	-2.48%	15.04%
ARC Sterling Cautious	7.12%	3.21%	-0.50%	* 10.00%
ARC Sterling Balanced	10.20%	5.04%	-0.40%	* 15.29%
ARC Sterling Steady Growth	12.87%	5.74%	-0.30%	* 18.99%

Returns are net of all fees and charges. Past performance is not a guide to future performance and the value of investments can fall as well as rise.

### KEY:

\* ARC performance figures for October & November 2010 have been estimated by Asset Risk Consultants.

As can be seen in the table above, our returns over the past month, relative to our peers and also market indices, were good. Given that around half of client portfolios are invested in passive or index tracking investments where the returns match their respective index, any outperformance

(or under performance!) is due to one of two factors: our tactical asset allocation and/or the performance of our “alpha enhancing” investments.

Over the course of the last month the investment performance was aided by tactical asset allocation decisions and partly hindered by one of our Alpha Enhancing Investments:

*Tactical Asset Allocation:*

- At the start of the month we became very nervous about the state of global equity markets. This was driven by our concerns over what was happening in the Eurozone and potential knock on effects into other markets. As a result we decided to hedge a large part of our equity market exposure by purchasing volatility. This is a relatively new asset class and is negatively correlated to equity markets. Its price therefore rises if markets fall and vice versa. Markets subsequently fell by over 2% giving us a nice gain.

*Alpha Enhancing Investments:*

- Our Special Situation position in a listed property company fell back over the month on little news flow and even less volume. This has been a frustration but our view remains unchanged that significant upside exists.

**Asset allocation going forward**

In terms of our positioning of client portfolios going forward our views on the major asset classes, based on the conclusions from our Investment Committee meeting at the start of December, are as follows:

*Equities (Neutral/Positive)*

Over the short term we have shifted somewhat to be slightly more positive on Equities. Whilst we would love to see a 5 - 10% pullback in markets to enable us to go overweight we think now is a touch premature.

We continue to have a bias towards the US and the UK and for the very aggressive a very small allocation to some parts of Europe. Emerging market stocks and, in particular, BRIC markets remain expensive and in our opinion do not offer good risk adjusted value at current levels.

*Fixed Income (Neutral/Positive)*

No significant change to our position from our earlier newsletter. We continue to take a relatively positive stance towards conventional government debt. The debate between inflation and deflation continues and we remain aware of deflationary pressures caused in the main by cuts in government spending, high unemployment rates and wage deflation to name a few. However, at the same time inflation has remained stubbornly above the Bank of England’s target which raises the potential for an earlier than previously expected interest rate rise in 2011. We continue to monitor the various inputs extremely closely and will make changes to our asset allocation as the outlook requires.

Where we have made changes is in our corporate debt exposure. We believe little value now exists in highly rated corporate bonds as the “easy money” has been made. Instead we have made an allocation to a long/short credit manager. This allows us to maintain an exposure to the asset class to benefit from diversification but takes out much of our directional market exposure. We now have no exposure to high yield or emerging market debt as the risk spread does not represent good value on a risk adjusted basis.

*Currencies (Neutral US\$; Positive £; Negative €)*

This is a change in positioning from our last newsletter. We have reversed our preference for the US Dollar in favour of Sterling. We do however remain very wary about the Euro.

*Commercial Property (Neutral)*

The sector has, over the past few months, been overbought and whilst we may be close to the bottom of the property cycle a wall of money is chasing what opportunities are around pushing prices up. If the UK and European economic recovery remains lacklustre property investors may be disappointed with returns going forward.

*Commodities (Neutral)*

We maintain a position in physical Gold as a form of disaster insurance. In fact we doubled our exposure for more cautious portfolios. This may strike some readers as odd given our previous warnings about speculative bubbles but it acts as a hedge against potential market falls.

*Hedge & Absolute Return Funds (Positive)*

We remain very positive towards this asset class. Hedge fund returns have however been mixed year to date albeit positive. We maintain a bias towards managers that are macro orientated in nature and have little exposure to equity-related strategies.

**Quartet Capital's progress**

We continue to be delighted by the positive response that we have received from professional advisors, clients and potential clients. We are glad to report that assets under management continue to grow at a healthy rate. More is always welcome!

We hosted our first Investment breakfast at our offices in Richmond for Professional Intermediaries this month (unfortunately the City breakfast fell foul to the snow). It was a fantastic opportunity for Intermediaries to hear the macro views of Niels Jensen, our Head of Investment, and discuss investment opportunities and risks for 2011. For those not able to attend a copy of the ARP newsletter is attached which covers the risks we discussed. The feedback from the breakfast has been very positive. We will be organising regular events throughout 2011 and will update you in due course.

Finally, we need to congratulate Colin and Peter who have respectively now become a Chartered Fellow and Chartered Member of the Securities Institute.

On other matters the office is closing on the evening of December 23<sup>rd</sup> and will reopen on Tuesday January 4<sup>th</sup> 2011. If you need to contact any of the team in the interim our details are as follows:

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**A reminder of what we do:**

We believe that there are a few key points about Quartet Capital's investment approach that make us different.

- Bespoke portfolios. We do not believe in shoehorning clients into predetermined investment solutions, therefore all client portfolios are managed on a bespoke basis.
- Portfolio construction. We start by addressing each individual client's risk profile which in turn yields a strategic asset allocation. This is then adjusted tactically depending upon our macroeconomic views to finally arrive at a bespoke client portfolio.
- Asset allocation. We believe (and studies have shown) that asset allocation is by far the biggest driver behind investment performance. This is what we focus on getting right and where we believe we add significant value.
- Investments. Very few fund managers consistently beat their respective index and they also tend to have high fees and costs. We therefore use passive investment vehicles for core portfolio holdings. Tactical investments which make up the balance of most portfolios are specific investment counters or actively managed funds which are included to try and produce the best risk-adjusted returns (add alpha). All portfolios are managed on a multi-asset basis to diversify risk.

If you have any questions, queries, comments and feedback, good and bad(!), or if you are interested in a confidential meeting with Quartet Capital, please contact Colin McInnes, Managing Partner, on (020) 8939 2920 or via email at [cgm@quartetcapitalpartners.com](mailto:cgm@quartetcapitalpartners.com).

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The portfolio performance information presented in this letter is estimated, unaudited, net of applicable fees and is subject to change. No representation is being made that the portfolios will or are likely to achieve profits or losses similar to those shown on the monthly performance table. Past performance is not indicative of future results and a client may not get back the amount originally invested.

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