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<u>There May be Trouble Ahead? – MAY 2017</u>

Yesterday, US equity markets suffered their biggest one-day drop for a year. At just under 2%, it was hardly earth-shattering – those of us that have been in the markets for longer than five minutes will remember when this was a regular occurrence. But in a world of zero interest rates, the chase for yield has ensured equity prices have simply edged higher and higher. Consequently, and despite all the disclaimers stating that "prices may fall and you may not get back all of your investment", it seems everybody has forgotten that prices can go down as well as up.

The world we live in today? Let's just mention the following (in no particular order); Brexit, a US administration in chaos, North Korea testing nuclear weapons on a regular basis, elections to come in Germany and Iran (the Iranian election is tomorrow, 19th May), and a still-fragile European Union (especially Italy and Greece). And all the while, lurking in the shadows, is radical Islam which has an unfortunate habit of creating all the wrong headlines from time to time. As irritating as it is, the phrase "climbing the wall of worry" has never been more appropriate.

> "Anybody can jump a motorcycle.
> The trouble begins when you try to land it."
> *Evel Knievel, Stunt Performer, 1938-2007*

I have no idea whether the move in the equity market yesterday was simply a slightly larger correction in the ongoing bull market, or whether it marked a turning point and signalled the start of something much more significant on the downside. The good news is that I am not alone. Nobody knows what happens next.

So how do you protect an equity-heavy portfolio in times of trouble? Clearly the answer lies in having a diversified portfolio that has a sufficient quantity of other assets that aren't correlated to equities. As we noted in a previous report;

"It seems to us that there are three obvious and simple steps to successful portfolio management: Firstly, try to ensure that any potential investment can provide an attractive *risk-adjusted* return. Secondly, try to ensure that when such potential investment experiences a challenging environment (as they all do from time to time) that it is able to contain downside performance. Finally, try to ensure that such potential investment is not correlated to your other investments. It's not rocket science, but it is easier said than done. "

> "The trouble with having an open mind, of course, is that people
> will insist on coming along and trying to put things in it"
> *Terry Pratchett, Author, 1948-2015*

As you know, we operate three different investment strategies as follows;

The ULTRO Strategy: a fully discretionary strategy, focusing on exchange-traded metals markets
The AEGIR Strategy: a fully systematic strategy, focusing on exchange-traded energy markets
The VARIO Strategy: a systematic strategy, focusing on exchange-traded metals and energy markets.

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All three of our strategies are robust, standalone investment strategies and have solid track records (the latest performance reports and all previous research reports are available on our website). So far so good. So far so obvious. But following a discussion with one of our existing investors, I thought it might be worthwhile to track the performance of a portfolio that invested in all three strategies. I looked at returns for the last three years (May 2014 to April 2017) and I also looked at how such a portfolio (I called it J3S) might measure up against some benchmarks as follows;

J3S = An equally weighted allocation to each of our ULTRO, AEGIR and VARIO strategies
ULTRO = Jaguar ULTRO Strategy
AEGIR = Jaguar AEGIR Strategy
VARIO = Jaguar VARIO Strategy
GSCITR = S&P GSCI Total Return Index
CTAI = Societe Generale CTA Index (Formerly Calyon/Newedge CTA Index)
STTI = Societe Generale Short Term Traders Index
SP500 = S&P 500 Index

	Annualised Compound Rate of Return
SP500	+8.18%
AEGIR	**+6.04%**
VARIO	**+5.98%**
J3S	**+5.19%**
CTAI	+4.50%
ULTRO	**+3.47%**
STTI	-0.68%
GSCITR	-23.27%

	Annualised Volatility
J3S	**2.55%**
ULTRO	**2.61%**
AEGIR	**3.43%**
VARIO	**4.71%**
STTI	6.86%
CTAI	8.81%
SP500	10.36%
GSCITR	20.79%

	Sharpe Ratio
J3S	**2.00**
AEGIR	**1.73**
ULTRO	**1.32**
VARIO	**1.26**
SP500	0.81
CTAI	0.54
STTI	-0.07
GSCITR	-1.16

	Maximum Drawdown
J3S	**-0.97%**
ULTRO	**-1.89%**
AEGIR	**-2.05%**
VARIO	**-3.29%**
SP500	-8.88%
CTAI	-10.50%
STTI	-13.78%
GSCITR	-60.50%

	Worst 12m Rolling Return
AEGIR	**+1.48%**
J3S	**+0.74%**
ULTRO	**-0.02%**
VARIO	**-0.82%**
SP500	-8.17%
CTAI	-8.50%
STTI	-11.73%
GSCITR	-42.69%

	Calmar Ratio
J3S	**+5.35**
AEGIR	**+2.95**
ULTRO	**+1.84**
VARIO	**+1.82**
SP500	0.92
CTAI	0.43
STTI	-0.05
GSCITR	-0.38

	Best Month/ Worst Month
J3S	**3.42**
VARIO	**2.36**
ULTRO	**1.85**
CTAI	1.33
SP500	1.33
AEGIR	**1.13**
STTI	0.83
GSCITR	0.78

	%age Up Months
AEGIR	**75%**
J3S	**69%**
ULTRO	**61%**
VARIO	**61%**
SP500	58%
STTI	53%
CTAI	50%
GSCITR	39%

	Sortino Ratio
J3S	**1.73**
ULTRO	**1.00**
AEGIR	**0.92**
VARIO	**0.83**
SP500	0.42
CTAI	0.27
STTI	-0.03
GSCITR	-0.37

You can see from the tables above that all three of the Jaguar strategies compare favourably with the relevant benchmarks – and that investing in the J3S portfolio enhances the majority of the risk metrics.

Importantly for the purposes of this note (and your portfolio) is that two of the three core Jaguar strategies are inversely correlated to the S&P 500, as is J3S. The exception is ULTRO, which has virtually zero correlation as shown in the table below;

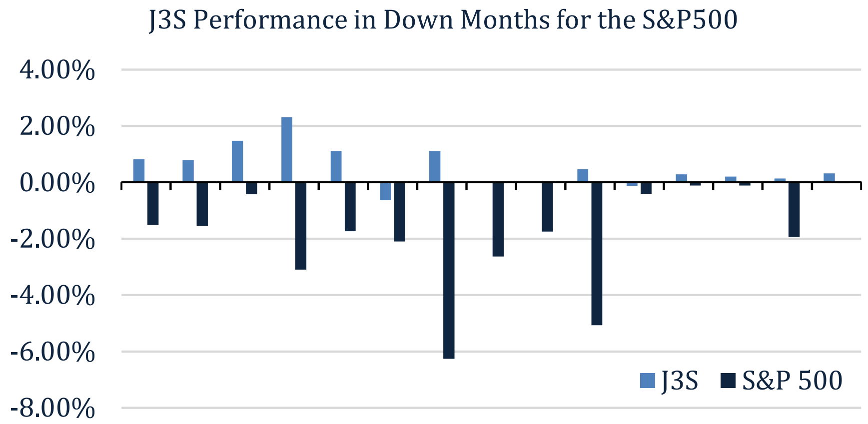
Correlation to S&P 500 (monthly returns);

- **AEGIR** = -0.39
- **J3S** = -0.31
- **VARIO** = -0.22
- **ULTRO** = +0.02

"The trouble with the world is that the stupid are cocksure, and the intelligent are full of doubt."

Bertrand Russell, Philosopher and Writer, 1872-1970

The numbers would indicate therefore, that J3S is a robust, investable strategy – but how does it fare when the S&P 500 is struggling? In the 36 months sampled, the S&P 500 lost ground in 15 of them and on average lost 1.92% per month. Of those 15 months, the J3S made money in 11 of them and on average returned 0.82% per month. In the 4 months it lost money, it lost on average 0.20% per month.



So how much J3S should you incorporate into your portfolio? I have assumed that no equity enthusiast is likely to sacrifice much more than 25% so the table below shows the metrics for the S&P 500 on its own and then the metrics for a portfolio of 75% S&P 500 and 25% J3S. I have also included the metrics for a 50:50 split;

Portfolio	Annualised Compound RoReturn	Annualised Volatility	Sharpe Ratio	Maximum Drawdown	Worst 12m Rolling Return	%age Up Months
S&P 500	+8.18%	10.36%	0.81	-8.88%	-8.17%	58%
75/25	+7.55%	7.60%	1.00	-6.34%	-4.55%	64%
50/50	+6.84%	4.94%	1.37	-3.87%	-0.91%	69%

You can see that by introducing a 50% allocation to the J3S strategy, the portfolio does sacrifice approximately 10bps per month, but both volatility and drawdown are enhanced by more than 50%.

We would be pleased to explain our strategies to you in more detail.

Notes

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