

# Fey Asset Management Free Newsletter

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## The Market

The market outlook is positive, despite the influence of investor fear and greed on the market. Equity markets are worried more about a Lehman-style banking collapse than on the slow economic growth. Stocks rose despite poor economic data— [jobless rate 9.1%](#), disappointing Sep retail sales (up [1.1% from Aug](#)), CPI annual rate up [3.9%](#), slightly more than expected, and estimates of third quarter annual [GDP growth of 2.5%](#), less than expected. This reflects a sluggish economy but not a recession. Stocks benefitted from Europeans taking the first step to finalize their plan to resolve the crises. As a result, the fear of an imminent crisis was lowered.

### October Market Performance

**Currencies.** October, Brazil up 7.2%, Australia 5.8%, S. Korea 5.2%, Russia 5%, Sweden 4.8%, Norway 4.6%, Poland 3.4%, Mexico 3.1%, Canada 3%, Euro 2.1%, Switzerland 2%, U.K. 1.2%, China down 1%, India -1.1%, US -1.5%, Japan -4.7%.

**Asset Classes.** October, Small Value up 16%, RAFI 1500 15%, Small Cap 15%, Small Growth 15%, Microcap 14%, Mid Growth 13%, Mid Cap 13%, Mid Value 13%, Large Value 11%, RAFI 1000 11%, Large Cap 11%, Large Growth 10%.

**Sectors:** October, Oil & Gas up 25%, Metals & Mining 23%, Steel 22%, NA Ntrl Resources 18%, Energy 17%, Copper 17%, Trans 16%, Agribusiness 16%, Silver 16%, Basic Mtrls 16%, Oil Futures 15%, Finance 14%, Real Estate 13%, Rgnl Banks 12%, Technology 12%, Private Equity 11%, Clean Energy 11%, QQQ 10%, Timber 10%, Solar 8%, Precious Metals 8%, Telecom 6%, Healthcare 6%, Biotech 5%, Utilities 5%, Gasoline 4%, Merger & Arbitrage 2%, Ntrl Gas 0%, Global Carbon -19%.

**Foreign Investments.** October, Russia up 20%, Brazil 20%, Australia 18%, Latin America 17%, China 17%, Germany 16%, Sweden 16%, Emerg Europe 15%, Asia-J 15%, BRIC 15%, Emerging Mkts 15%, Italy 14%, Britain 13%, Mexico 13%, France 13%, EU 13%, US 11%, Singapore 11%, World 11%, India 11%, Canada 11%, World-US 10%, Taiwan 10%, EAFE 10%, Spain 9%, Switzerland 8%, Belgium 6%, Japan down 0%.

**Fixed Income.** October, BuyWrite 9%, Floating Rate 9%, High Yield 8%, Cushing MLP 8%, Alerian MLP 6%, EM Sovereign Debt 5%, US\$ Emerging 5%, Intl Inflation Protected 3%, Corporate 3%, Intl Treasury 2%, TIP 2%, Annaly 1%, Bond 0%, MBB 0%, Absolute down 0%, GNMA -0%, Muni -1%, 7-10yr Treasury -1%, Build America -1%, 20+yr Treasury -4%.

## How Harvard and Yale Reacted to Downturn

### 1. Introduction

We will discuss how Harvard and Yale achieved a [12%](#) and [13%](#) annual return respectively for the last 20 years, what their current asset allocation is, how they responded to the recent downturn, and how you can mimic their portfolios.

Harvard manages [\\$32 Billion](#), Yale [\\$16 Billion](#). This amount of money attracts the [best and brightest](#). They achieved spectacular results in up and down markets in all asset classes. It is worthwhile to see how they did it and what we can learn from it.

We cannot overemphasize how outstanding it is to achieve a 12% return for 20 years

### 2. Historical Returns

Table 1 shows annualized returns, nominal and real (i.e. inflation adjusted) for Harvard and Yale to June 2010.

Years	Harvard		Yale	
	Nominal Return	Real Return	Nominal Return	Real Return
1	11.0%	9.9%	8.9%	7.8%
5	4.7%	2.4%	6.2%	3.9%
10	7.0%	4.6%	8.9%	6.5%
20	11.9%	9.3%	13.1%	10.5%

Table 1 Harvard and Yale's Historical Returns.

### 3. Method of Asset Class Allocation

Harvard and Yale use a [disciplined method](#) to determine the amount to invest in each asset class. They first select the available asset classes, then look at historical returns, future expected returns, volatility of returns, correlations of returns.

### 4. Asset Class Performance

Figure 1 shows the 10-year performance by asset class, to June 2010, of [Harvard](#), [Yale](#), and [benchmark](#). Both Yale and Harvard have exceeded benchmarks. Yale generally has higher returns than Harvard except for Harvard's unusually high returns in fixed income.

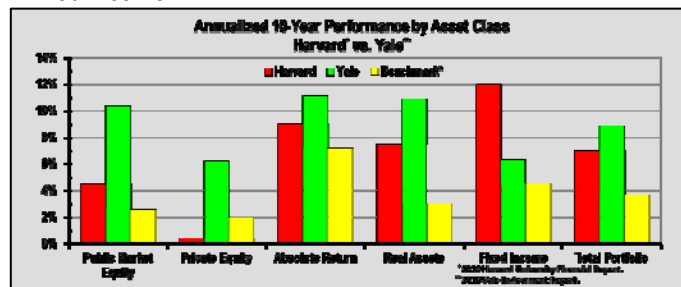


Figure 1 10yr Performance by Asset Class.

## 5. Private Equity & Absolute Returns

As can be seen by [Harvard's most recent](#) 1 year performance (Figure 2) Harvard and Yale have access to the best investments, many of which are not available to the individual investor.

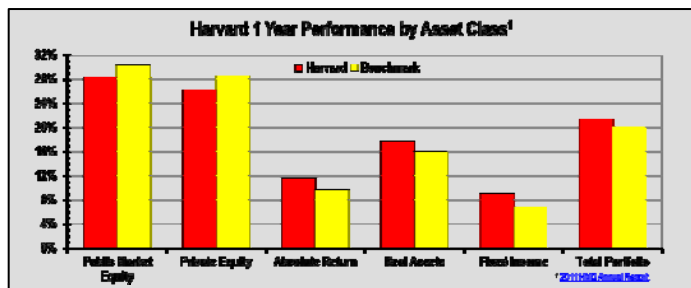


Figure 2 Harvard 1yr Performance by Asset Class.

[Private Equity](#) consists of Venture Capital to start new firms, Mezzanine Capital needed when the initial funds run out, Emerging Firms, capital needed to grow the firm, and Leveraged Buyouts. A Leveraged Buyout occurs when an investor, typically a financial sponsor, acquires a [controlling interest](#) in a company's equity and when a significant percentage of the purchase price is financed through [leverage](#) (borrowing). The company often has been operating for several years at a loss, accumulating substantial tax losses that the investor can use.

Private Equity Investors must commit large amounts of money for the long term. Most investors cannot invest in the best private equity funds.

[Absolute Return Funds](#) try to invest [long and short](#) to obtain returns slightly higher than fixed income in up and in down markets. But the best, Absolute Return Hedge Funds, are not available to most individuals.

## 6. Harvard & Yale Response to Downturn

Harvard and Yale continued their long term trend in asset allocation. They left the percentage of fixed income unchanged. Harvard and Yale decreased their slight margin. They decreased high volatility Real Assets (real estate and commodities) and Absolute Returns. Yale continued to increase Private Equity.

	Harvard					Yale				
	2005	2008	2009	2010	2011	2005	2008	2009	2010	2011
US Equity	15%	12%	11%	11%	11%	15%	11%	10%	8%	7%
Foreign Equity	15%	22%	22%	22%	22%	15%	15%	15%	10%	9%
Private Equity	13%	11%	13%	13%	13%	18%	19%	21%	26%	33%
Fixed Income	27%	16%	13%	13%	13%	8%	4%	4%	4%	4%
Real Assets	23%	26%	26%	23%	23%	20%	28%	29%	37%	28%
Absolute Rtrns	12%	18%	18%	16%	16%	25%	23%	21%	15%	19%
Cash	-5%	-5%	-3%	2%	2%	0%	0%	0%	1%	0%
Total	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%
Portfolio Return	19%	9%	-27%	11%	21%	22%	5%	-25%	9%	NA

Table 2 Harvard and Yale's Policy Portfolio Evolution.

## 7. What We Can Learn from Harvard and Yale

Harvard's and Yale's objectives are similar to a person in the early withdrawal phase of retirement. In fiscal 2010 they spent 6% of their endowment for their operations.

a. Hence, using their strategy as the piston that drives your investment management is a smart move.

- b. Despite their income needs Yale has only [4%](#) in fixed income and Harvard [18%](#). You are unlikely to match Harvard's [8.5%](#) annual fixed income return.
- c. Harvard and Yale do not change their asset allocation with up and down markets. They do not increase bond holding when the market goes down.
- d. Harvard and Yale evolve their portfolios slowly over time as the economy changes.

## 8. Mimicking Harvard's Portfolio

Harvard and Yale have access to investments that are not available to most individual investors. Hence, we did not include private equity and use only 5% absolute returns.

Asset Class	Adj Wgt	Max DD	Returns to 6/30/11			
			1 Mo	1 Yr	3 Yr Annl	(6/11-10/11)
Domestic Equities ( <a href="#">DVI</a> )	15%	44%	-1%	29%	7%	-1%
Developed Markets ( <a href="#">PID</a> )	14%	53%	-1%	31%	0%	-5%
Emerging Markets ( <a href="#">DEM</a> )	14%	44%	-1%	39%	11%	-12%
Absolute Returns ( <a href="#">PDCRX</a> )	5%	NA	NA	NA	NA	NA
Commodities ( <a href="#">DBC</a> )	17%	57%	-4%	34%	-13%	-4%
Real Estate ( <a href="#">RWX</a> )	11%	56%	-1%	42%	1%	-12%
Domestic Fixed Income ( <a href="#">BLV</a> )	3.5%	11%	-2%	2%	8%	16%
Domestic Fixed Income ( <a href="#">AMLPL</a> )	3.5%	NA	1%	NA	NA	1%
Foreign Fixed ( <a href="#">BWJ</a> )	6%	11%	0%	16%	5%	0%
High Yield ( <a href="#">HYG</a> )	7%	27%	-1%	16%	9%	0%
Inflation Prctd Bonds ( <a href="#">TIP</a> )	4%	12%	1%	7%	5%	7%
Cash ( <a href="#">SHY</a> )	0%	1%	0%	1%	2%	1%
Portfolio	100%	NA	NA	NA	NA	NA
70% Stocks ( <a href="#">VGTSM</a> )/ 30% Bonds ( <a href="#">AGG</a> )	100%	37%	-1%	22%	2%	-8%

Table 3 Example Portfolio to "Mimic" Harvard's Portfolio.

## 9. Comparison with Newsletter Recommendations

For comparison we show the performance of our newsletter recommendations through June.



Returns to 6/30/11	1 Mo	6 Mo	1 Yr	Annl	3 Yr Max DD	(6/11-10/11)
<a href="#">Wilshire Total Market</a>	-1.5%	5.7%	31.4%	3.4%	42.3%	-5.1%
<a href="#">Vanguard Total Internatl</a>	-1.5%	3.7%	30.9%	-0.4%	50.0%	-12.9%

Fey Asset Management Newsletter Recommendations.

## 10. Take Aways

- Harvard and Yale are some of the most successful investors. We cannot overemphasize that.
- They do not increase their fixed income percentage in down markets.
- You need good reasons to deviate from their tried and proven strategy.

*Contact me for a more detailed analysis.*