



It takes **wisdom** and  
**experience** to spot  
the best opportunities

## Select Alternative Investments

# What We Do

## Three Types of Investment Portfolios

- Global Macro (long/short)
- Multi-Strategy (long-only)
- Custom Alternatives (tax-sensitive, low turnover)

## Low Fees

Asset-based or performance-based fee (not both)

## Minimum Investment

\$500,000

## Concentrated Portfolios

20-25 low-cost, liquid, passively-managed, factor-based ETFs

## Separately-Managed Accounts

Clients have complete control, liquidity, and transparency

# What We Believe

## Alternative investors want low correlations and attractive returns

- Investing long and short is the best way to achieve low correlations with stocks and bonds.
- Systematically exploiting market inefficiencies is the best way to achieve attractive returns.

## Value and momentum are a powerful combination

- They are the strongest and most consistent market inefficiencies.
- They also diversify each other.
- They are effective in selecting groups of securities and factor tilts.

## Active asset allocation adds the most value

- Asset allocation/factor selection drives portfolio performance
- Security-specific risk is diversified away

# Kevin Means, CFA – Principal

## Area of Expertise

## Background and Experience

### Investment research

- Director of Quantitative Research at INVESCO
- Expert at developing structured investment processes

### Multi-asset class management

- Chief Investment Officer at INVESCO, Aeltus (Aetna investment subsidiary), and Alpha Equity Management
- Developed and managed multi-asset class “lifestyle” funds
- Hired and supervised asset class specialist managers

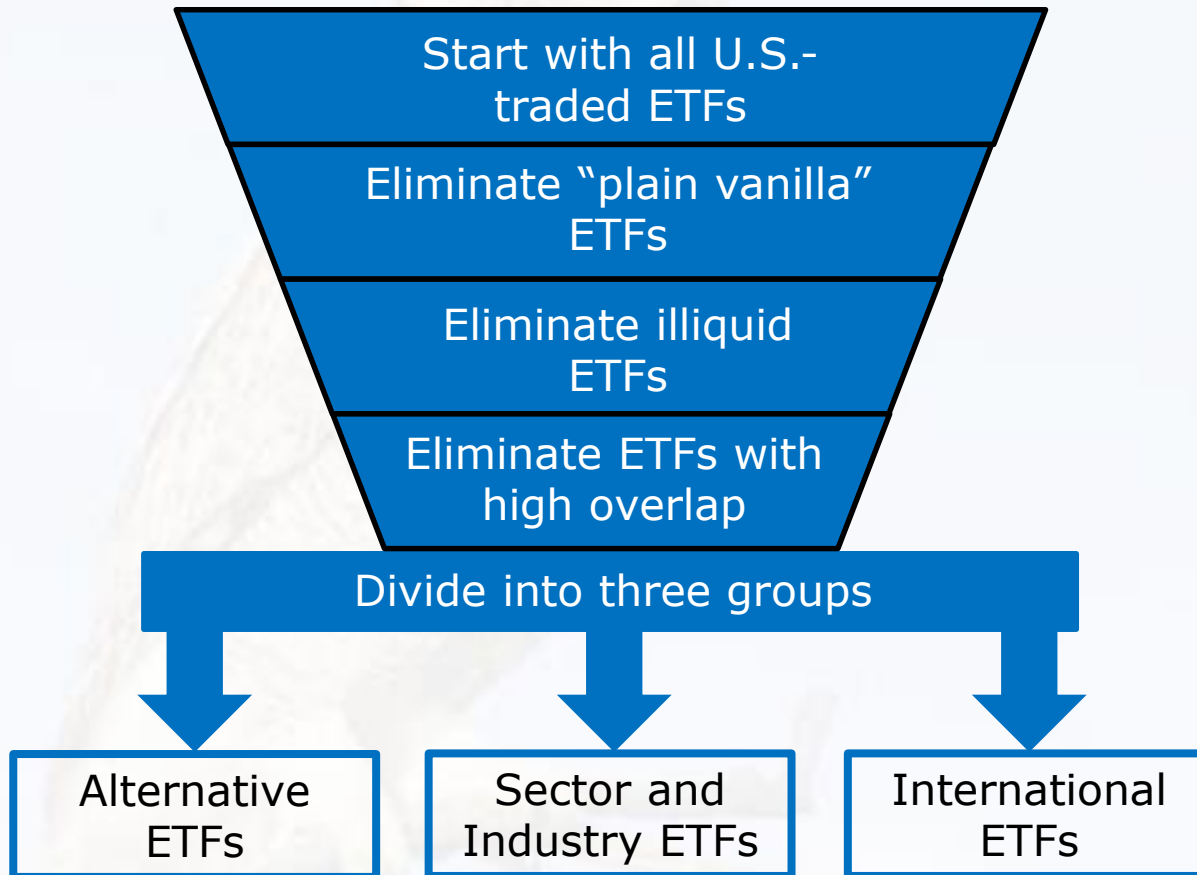
### Alternatives management

- Founded a hedge fund firm – Alpha Equity Management
- Known as a pioneer in 130/30 management
- Managed a variety of long/short equity hedge funds: U.S., international, and real estate

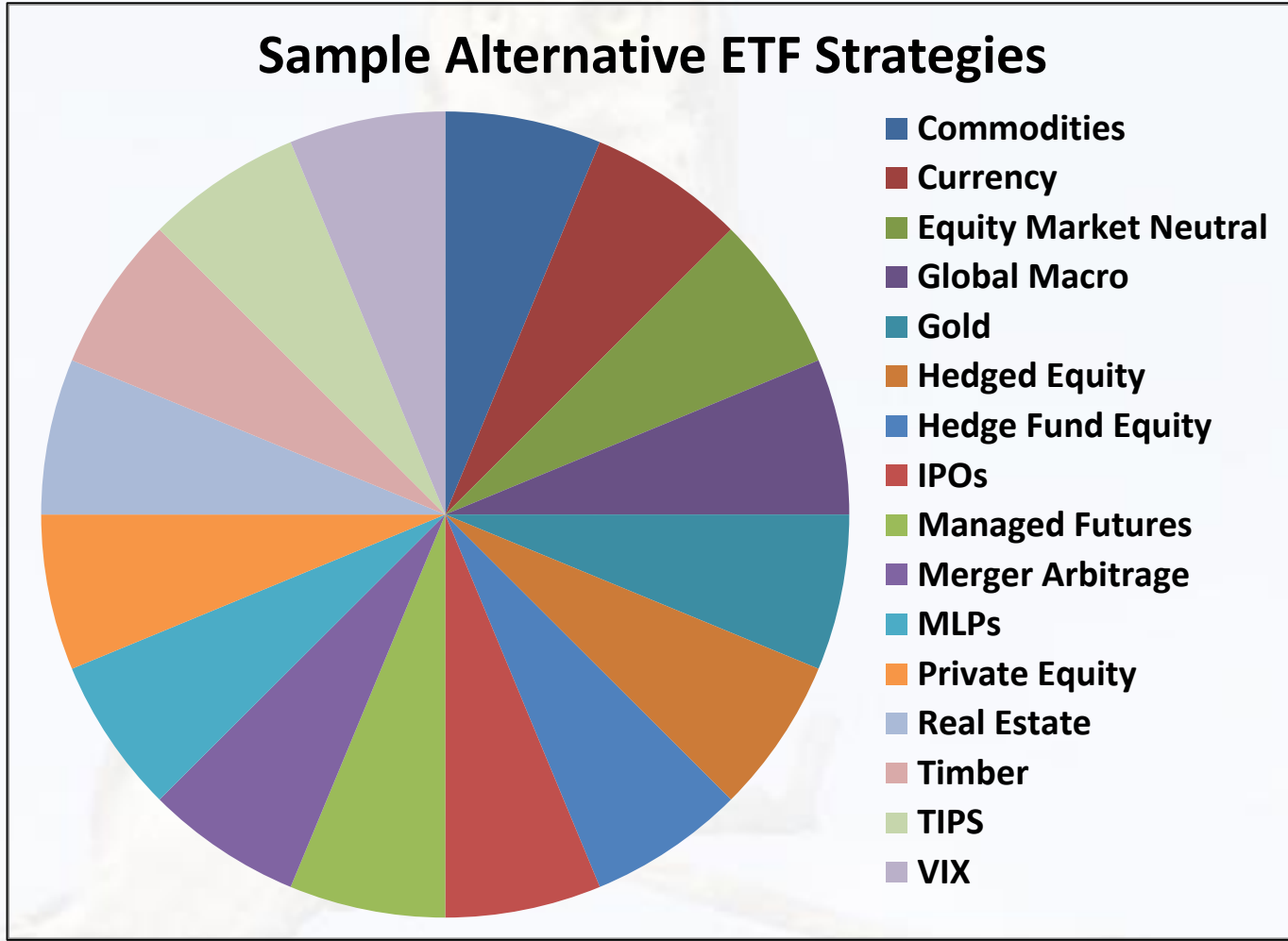
### Portfolio management

- Managed a Morningstar five-star mutual fund (Alpha Equity Mgmt.)
- Managed large funds (> \$11 billion) at Aeltus
- Managed multi-asset class portfolios for over 25 years

# What We Invest In



# What Are Alternative ETFs?



# How We Invest



**Measure** ETF historical risk sensitivities.

**Categorize** return as risk-related or residual.

**Forecast** risk-related and residual returns.

**Combine** forecasts for ETF total return forecast.

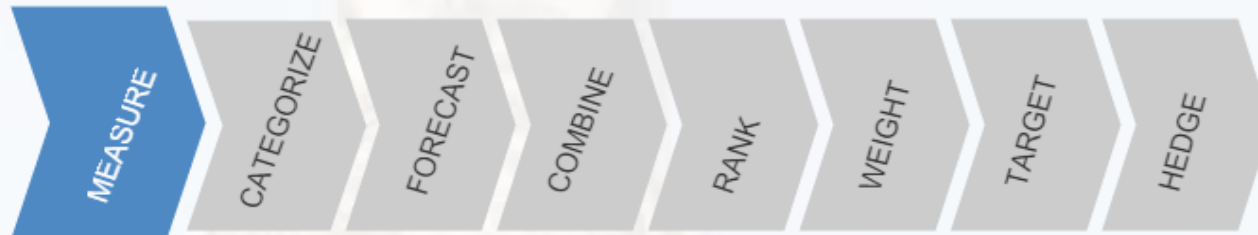
**Rank** ETFs according highest utility scores.

**Weight** 16 most attractive ETFs in descending order.

**Target** portfolio risk factor exposures.

**Hedge** to achieve desired risk exposures.

# Measure ETF Risk Sensitivities



Measure the historical sensitivity of each ETF to:

- Stock Market Risk (MKT) – S&P 500 Index
- Interest Rate Risk (LTB) – 10Y Treasury Index
- Currency Risk (DLR) – U.S. Dollar Index
- Commodity Risk (OIL) – WTI Crude Oil Index

Use proprietary database of pro-forma historical ETF pre-launch returns

Use sophisticated statistical techniques to estimate ETF risk sensitivities

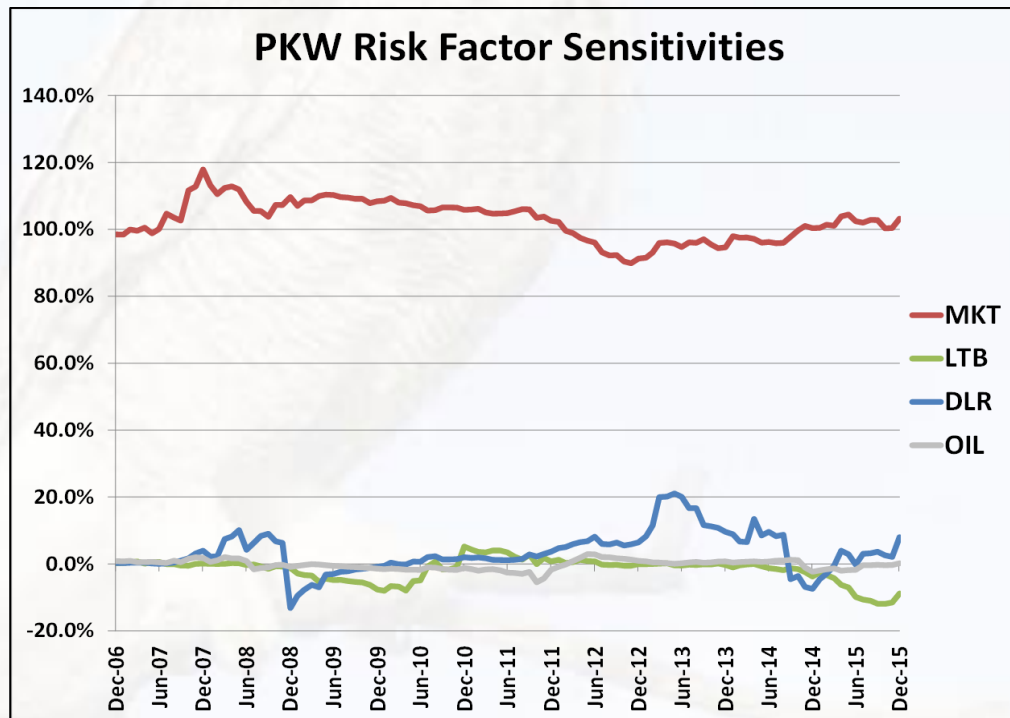


# Measure ETF Risk Sensitivities

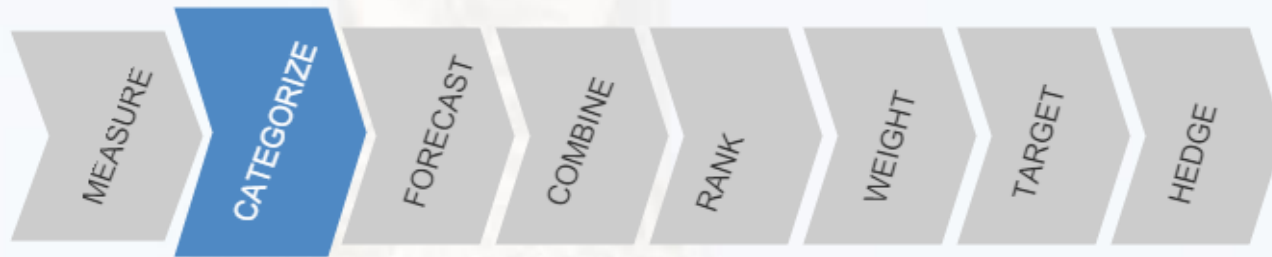
For example, PowerShares Buyback Achievers ETF (PKW)

A factor-based portfolio of companies that have had net stock buyback of 5% or more

As an equity ETF, its most important risk is equity market risk (MKT)



# Categorize returns



For each ETF, separate historical return into two components:

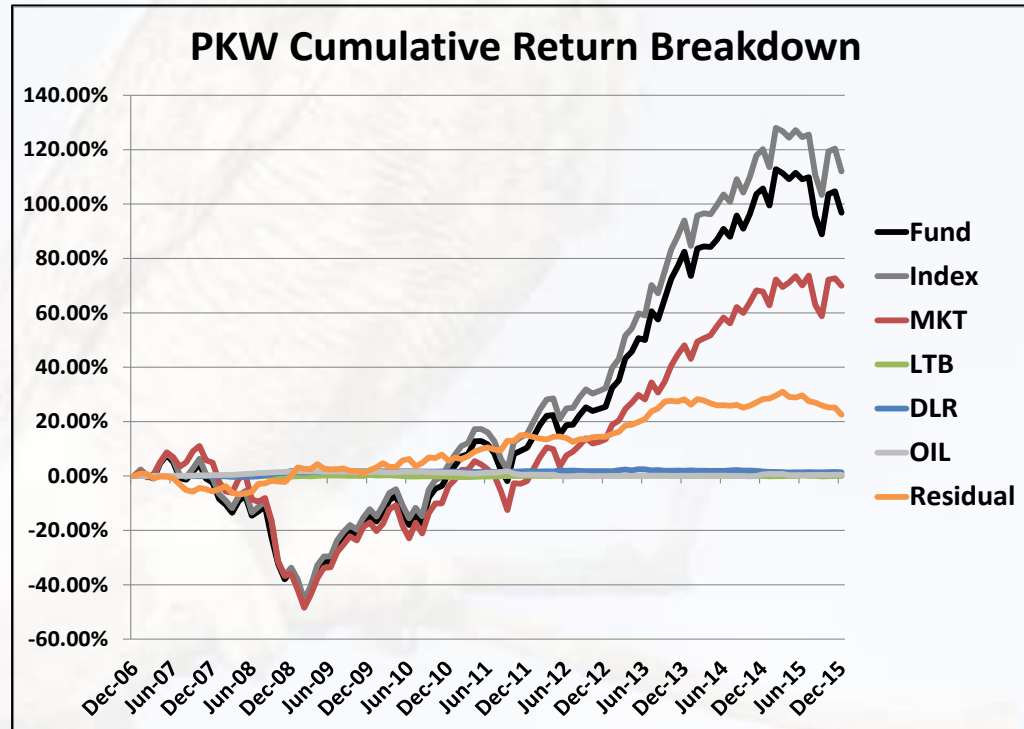
- Risk-related return
- Residual return

# Categorize returns

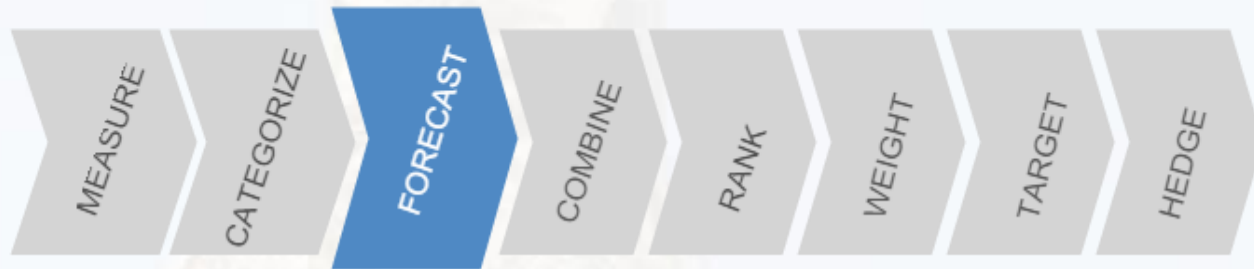
PowerShares Buyback Achievers ETF (PKW) has had significant residual return (net of risk)

Residual returns are variable, so timing exposures is important

Residual returns tend to trend



# Forecast risk-related returns



Forecast the expected return of each risk factor:  $\text{base case} + \text{mispricing} = \text{total return}$

Calculate the base case for MKT return:  $\text{yield} + \text{long-term growth}$

Set base case for LTB, DLR, and OIL to: zero

Forecast mispricing returns for all four risk factors using multi-factor models

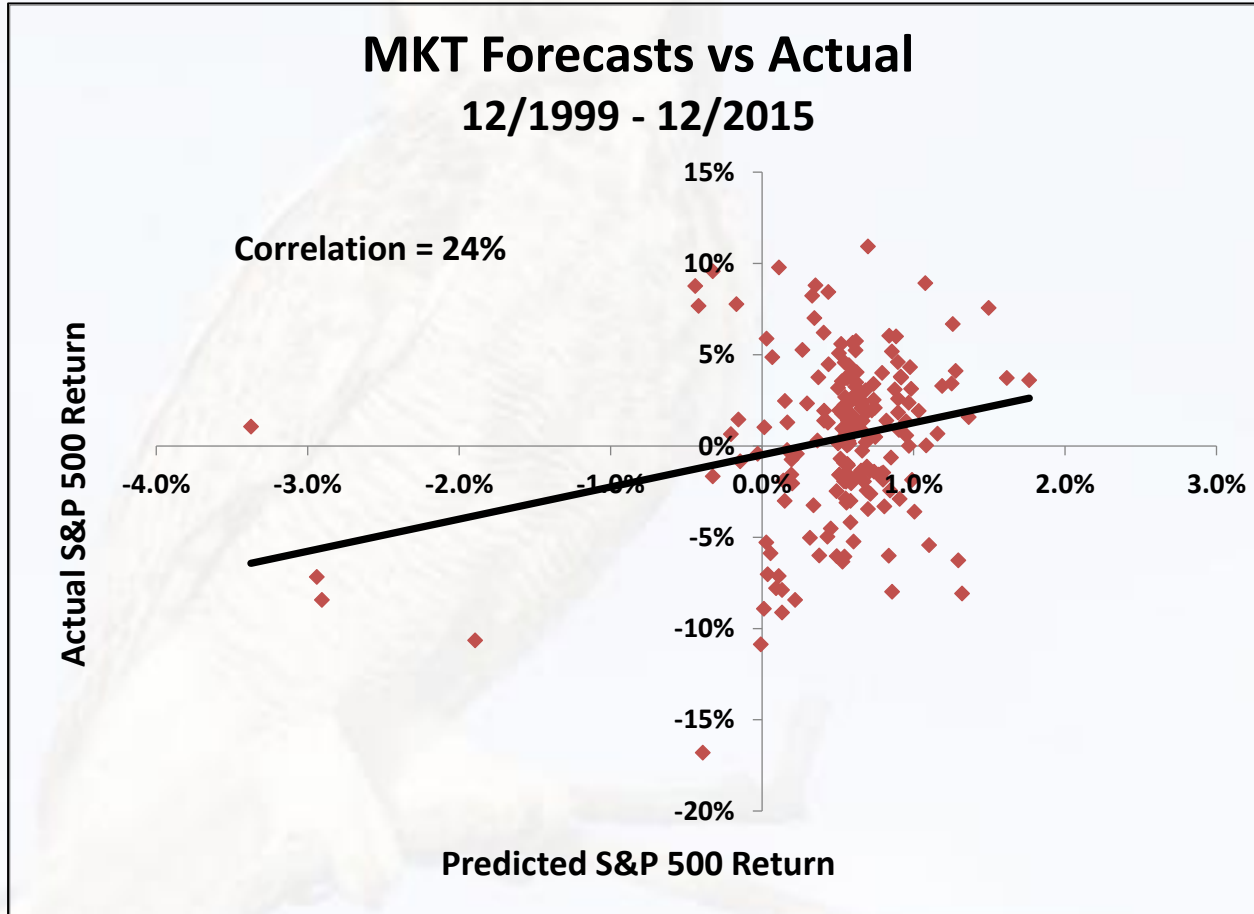
# Forecast risk-related returns

## Expected Returns on U.S. Stocks: Base Case

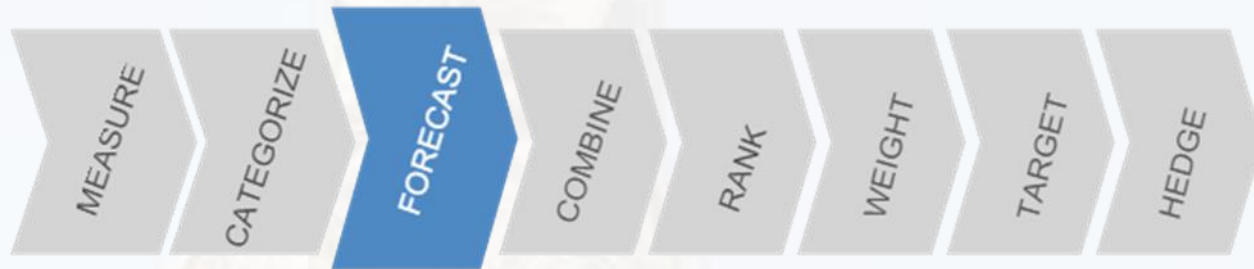
12/31/2015

|                         | <u>S&amp;P 500</u> |              |              |
|-------------------------|--------------------|--------------|--------------|
|                         | <u>Low</u>         | <u>Mid</u>   | <u>High</u>  |
| Current yield           | 2.15%              | 2.15%        | 2.15%        |
| Net buyback yield       | 1.00%              | 2.00%        | 3.00%        |
| Expected inflation      | 1.50%              | 2.00%        | 2.50%        |
| Expected real growth    | <u>1.50%</u>       | <u>2.00%</u> | <u>2.50%</u> |
| Nominal expected return | 6.15%              | 8.15%        | 10.15%       |

# Forecast risk-related returns



# Forecast residual returns



Forecast ETF residual returns using multi-factor models:

- Value factors
- Momentum factors

Base factor weights on trailing historical forecasting effectiveness

# Forecast residual returns

| <b>SelectAlts</b><br>Residual Return Multi-Factor Model<br>Factors by ETF Universe |               |           |                 |                |                |                 |                     |                   |                  |
|--|---------------|-----------|-----------------|----------------|----------------|-----------------|---------------------|-------------------|------------------|
| ETF Universe   | Value Factors |           |                 |                | Momentum Fctrs |                 |                     | Economic Factors  |                  |
|  | Yield         | EPS/Price | LT Avg Residual | Value+Momentum | Change in EPS  | Total Return Mo | Resid Rtrn Skewness | Yield Curve Slope | 3M Change in PMI |
| Alternative  | X             | X         | X               | X              | X              | X               | X                   |                   |                  |
| Sector & Industry  | X             | X         |                 | X              | X              | X               | X                   |                   |                  |
| International  | X             | X         |                 | X              | X              | X               | X                   | X                 | X                |



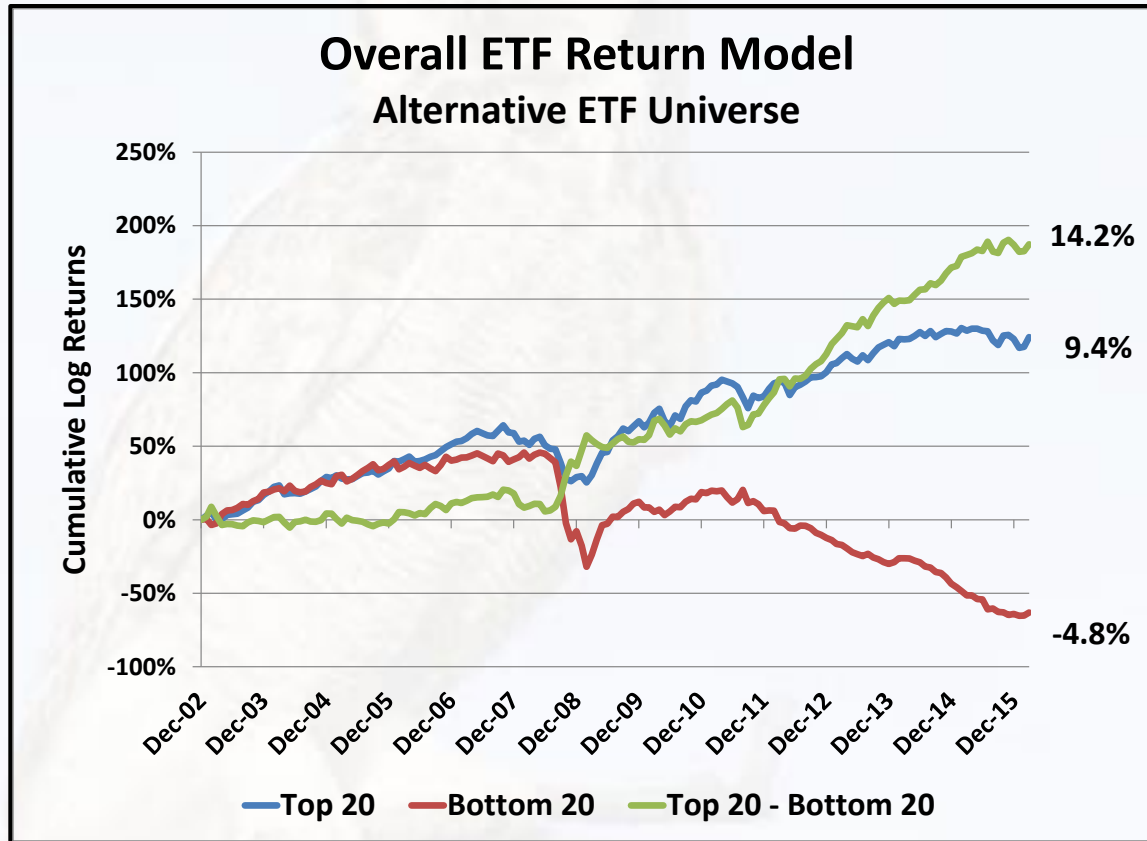
# Combine risk and residual forecasts



Calculate ETF expected total return:

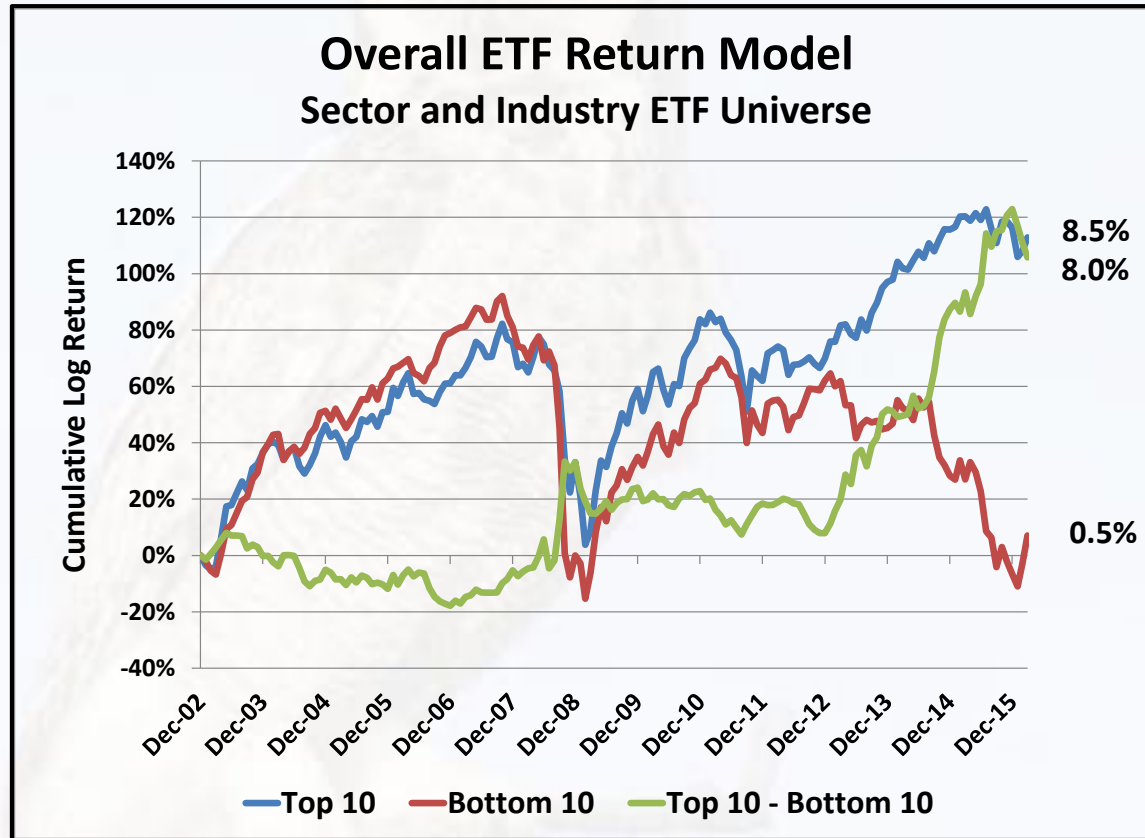
$$\begin{aligned} & \text{ETF expected risk-related return} \\ & + \text{ETF expected residual return} \\ \hline & = \text{ETF expected total return} \end{aligned}$$

# Combine risk and residual forecasts



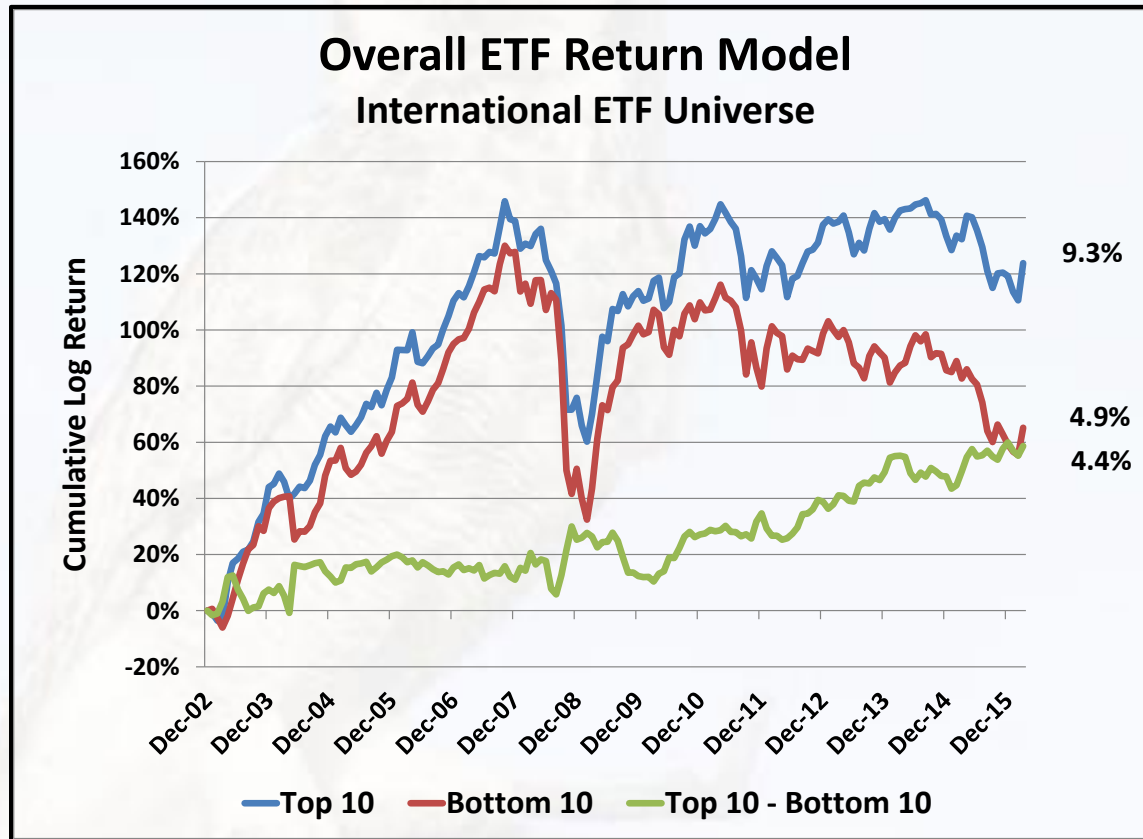
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# Rank

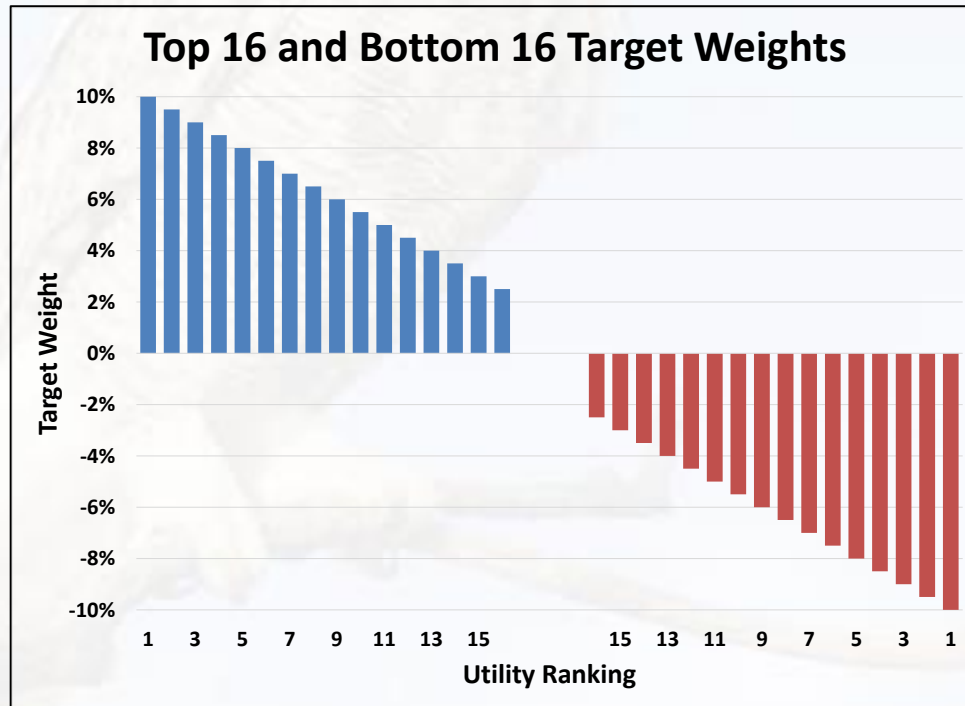
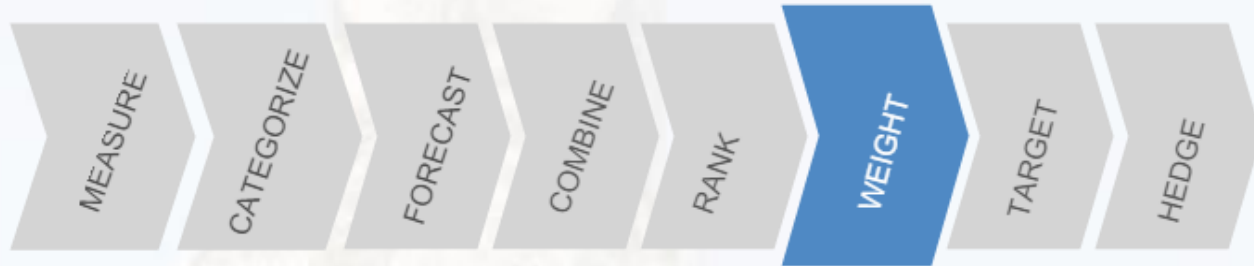


Rank the utility of each ETF using the formula:

- Expected total return*
- *Systematic risk penalty (MKT, LTB, DLR, and OIL)*
- *Residual risk penalty (downside volatility of residual returns)*
- *Implementation shortfall (fund tracking error to index including expense ratio)*
- *Bid/ask spread*
- *Commission*
- *Borrow cost (for shorts)*
- = *Utility*

OUR INVESTMENT PROCESS

# Weight



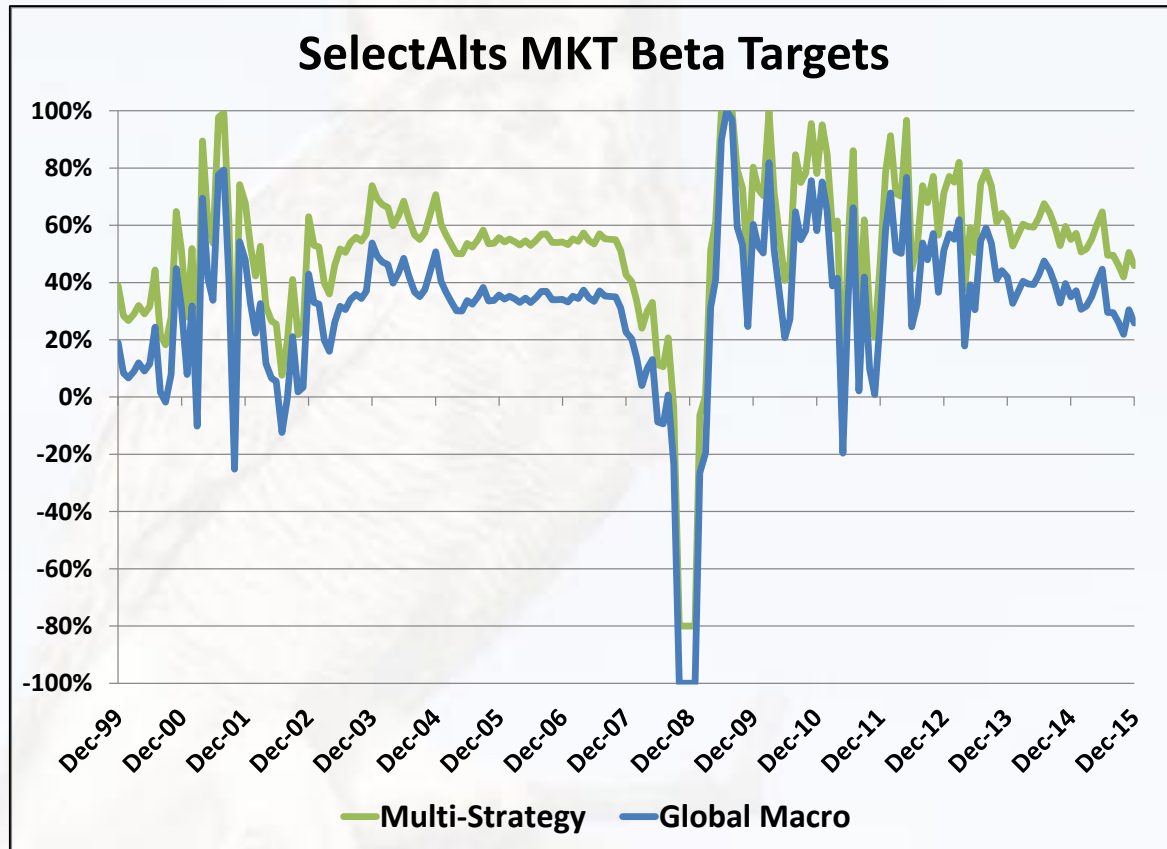
# Target



Target risk factor exposures based on risk factor expected returns:

- MKT exposure for Global Macro: avg.  $\approx 35\%$
- MKT exposure for Multi-Strategy: avg.  $\approx 55\%$
- LTB, DLR, and OIL exposures: avg.  $\approx 0\%$

# Target





OUR INVESTMENT PROCESS

# Hedge



Trade hedging ETFs as necessary to achieve target positions.

# Our Edge

## Breadth of scope

Over 250 niche strategies

## Flexibility

No benchmark hugging, no artificial constraints, go anywhere

## Nimbleness

Highly liquid ETFs and small AUM

## Exploitable inefficiencies

Many relatively new and poorly understood ETFs (e.g., VIX)

## Lack of competition

Few sophisticated ETF-focused investors

## Proprietary data and models

Developed for and focused on ETFs

## Principal's background and expertise in:

- Quantitative research
- Multi-asset class management
- Long/short portfolios

# Why SelectAlts?

## Return

- Seeks a higher return than most diversified alternative funds
- Actively manages equity market beta to participate in up markets and protect in down markets

## Diversification

- Designed for low correlation with stocks and bonds
- Exposure to a wide variety of asset classes and strategies

## Simplicity

- A “one-and-done” overall alternatives solution in a single investment
- Offloads the task of deciding how much to allocate to which asset classes and strategies

## Peace of mind

- ETFs are publicly traded registered investment vehicles
- Client owns and controls the assets in a separately-managed account

# SELECT ALTERNATIVE INVESTMENTS LLC

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