Greetings from the Greenwich Roundtable.

Our session titled *Asset Allocation for 2004: Navigating the Risks, Charting the Opportunities* was held as a large tropical storm approached the East Coast, and in a climate where we continue to wrestle with the cloud of uncertainty hanging over global investment markets. The mood was optimistic for the near term, but turning gloomy as we move into the middle of next year. Macro strategies seemed to posses the advantage. Spencer Lampert is the head of research inside our favorite savvy hedge fund. John Makin leads a respected think tank and is the chief economist of a legendary hedge fund. Alan Brown is a highly articulate chief investment officer for the largest traditional money manager on the planet.

Spencer Lampert, Tudor Group

US economy is growing at 5-6 percent in the third and fourth quarters. Sentiment and momentum are improving. But the US stock market has discounted this already. Growth in 2004 is uncertain. We may be in an environment of going nowhere. Corporate profits grew at a record 30% pace in the second quarter, but it's not sustainable. The downside risks are not priced into the market yet. Consumers are indifferent to terrorism risk. They are indifferent to the risk of war with Korea or Iran. Corporations, still, do not want to build inventories or make investments yet. Valuations are still high. US stocks will deliver lackluster results. Correlations between the financial markets are persistently high. Stocks and bonds may no longer be negatively correlated. The US Fed may hike rates, not in March, but much later in 2004, if at all. Opportunity exists in the short end of the G-5 fixed income markets. Currencies are uncertain. Euroland has its own problems. The Australian dollar will continue to benefit from the growth in Asia. Gold is attractive. Commodities are a mixed bag. Energy has a large oversupply of crude. Industrial metals are mixed but attractive as China grows. Hedge fund strategies based on momentum have run their course. Focus on your best stock traders to survive a difficult equity environment. Macro strategies will continue to benefit from their flexibility and the many disconnections and mispricings that will erupt.
slampert@tudor.com

John Makin, Caxton Associates

We have a classic set up situation unfolding. The dislocations and mispricings that Spencer described will produce volatile markets. Traditional money managers will experience difficulty. Macro strategies will benefit in this environment. The big issue is facing central banks. The post 9-11 boomlet produced a growth surge. The Fed injected massive liquidity and the White House introduced tax cuts. The US economy started growing. But interest rates rose and home refinancing slowed. Another tax cut is not likely. Corporations are shedding jobs, selling from their inventories and replacing, not investing in equipment. China has a large supply of labor and manufactured goods. US employment is getting worse. Without stimulus, GDP growth will slow to 2-3%. This will jeopardize the Japanese recovery. Post-bubble, deflationary conditions have begun. Central banks must influence markets towards inflation. They need to make prices rise. Forty years ago this would have been deemed irresponsible. The US Fed is amplifying the problem as they continue to cut rates.

Ten-year bond yields may drop again. Their fear of inflation is a problem. They should adopt a policy of maintaining inflation at 1-2 percent. The Japanese are toying with the idea of printing money. The European central bankers are still fighting the last battle, still fighting inflation. It's a problem when the US wants a weak currency. Gold will be a good play when all currencies are weak. This stimulus-induced recovery will fail and the central banks will print money. But it will be too late. jmakin@caxton.com

Alan Brown, State Street Global Advisors

I have two arguments to make today. First, best practices for institutions are flawed and, at best, unsound. Typically, an asset allocation model is run, strategic benchmarks are selected, an implementation plan is written, managers are hired, outliers and trackers are monitored and the exercise is repeated every 3-5 years. Focusing on strategic benchmarks is wrong. Institutions relied too much on two unrealistic assumptions embedded inside asset-liability models. One is that your appetite for risk doesn't change when your wealth changes, and the other is that your appetite for risk doesn't change when your opportunities change. This is as sensible as the flat earth society. The risk premium is not a constant. Wealth changes over time. We need to abandon strategic benchmarks and adopt a policy that anticipates how the institution will respond to changes in wealth and changes in opportunity. Today, like a deer in the headlights, most institutions are watching their wealth deteriorate but haven't taken any action. Figuratively, we chart a course for Bermuda, raise all the sails, and regardless of the wind and weather we don't change our course or trim the sails. We should embrace absolute return investing and begin to separate alpha and beta. Institutions will change but glacially slow. Second, the interplay between the EU and the Euro has not been priced into the market. Euroland enjoys a single interest rate. But a uniform interest rate policy is destabilizing because there are no funds transfer mechanisms to move money between countries with low growth-low inflation and countries with high growth-high inflation. Individual countries cannot print money any longer. Countries that are growing slowly will continue that way. Although the goal of a single currency is to create a uniform capital market for Europe, the country differences are not over. They are beginning to widen. The opportunity lies in a complex arbitrage that can identify buying opportunities in high growth countries in Southern Europe and shorten them in low growth Northern European countries. Alan_Brown@SSGA.COM

Please join me in expressing our special gratitude to **Dan Vandivort** and **Nassos Michas** of **Robeco-Weiss Peck & Greer** whose generous grant made this symposium possible. Robeco has built a splendid alternative investment practice. They also share our commitment to education as demonstrated by their underwriting this important symposium. Nassos.Michas@robecousa.com

As always, please send me your comments and suggestions.
http://www.greenwichroundtable.org/

Steve McMenamin
12 October 2003