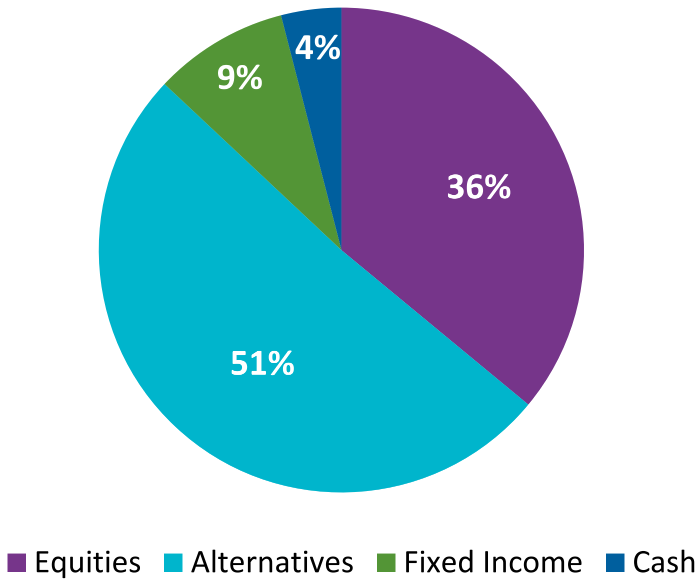
NATIXIS
GLOBAL ASSET MANAGEMENT

Implementation of Alternatives

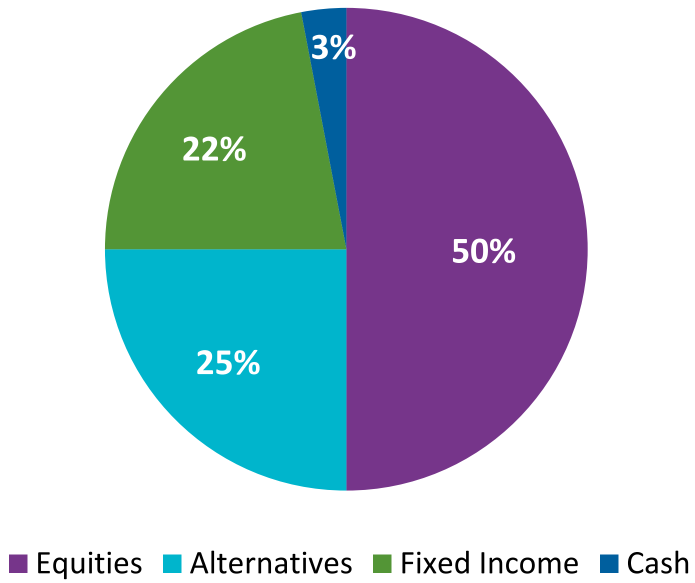
Institutional use of alternatives

Institutional experience with alternatives

Endowment FY2014 allocations



State pension FY2014 allocations

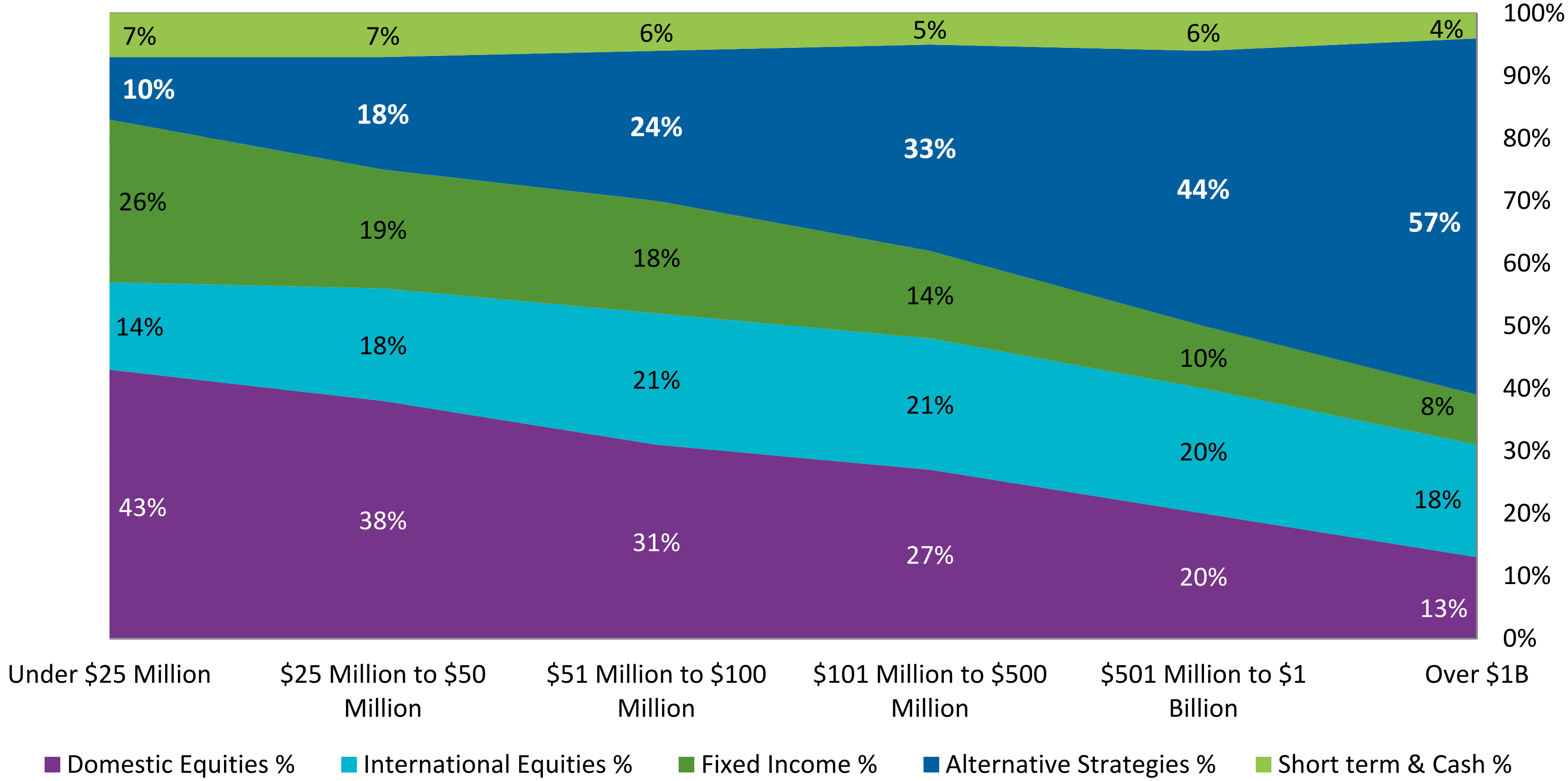


Alternatives in this case are defined as allocations to private equity, marketable alternative strategies (hedge funds, absolute return funds, market neutral, long/short), venture capital, private equity real estate, energy and natural resources, and distressed debt.

Source: 2014 NACUBO-Commonfund Study of Endowments FYE 2014, www.nacubo.org/About_NACUBO/Press_Room/2014_NACUBO-Commonfund_Study_of_Endowments_(Final_Data).html

Varying institutional adoption of alternatives

FY2014: Asset allocation for U.S. foundations & endowments



Source: 2014 NACUBO-Commonfund Study of Endowments FYE 2014, www.nacubo.org/About_NACUBO/Press_Room/2014_NACUBO-Commonfund_Study_of_Endowments_(Final_Data).html

A look at endowment performance

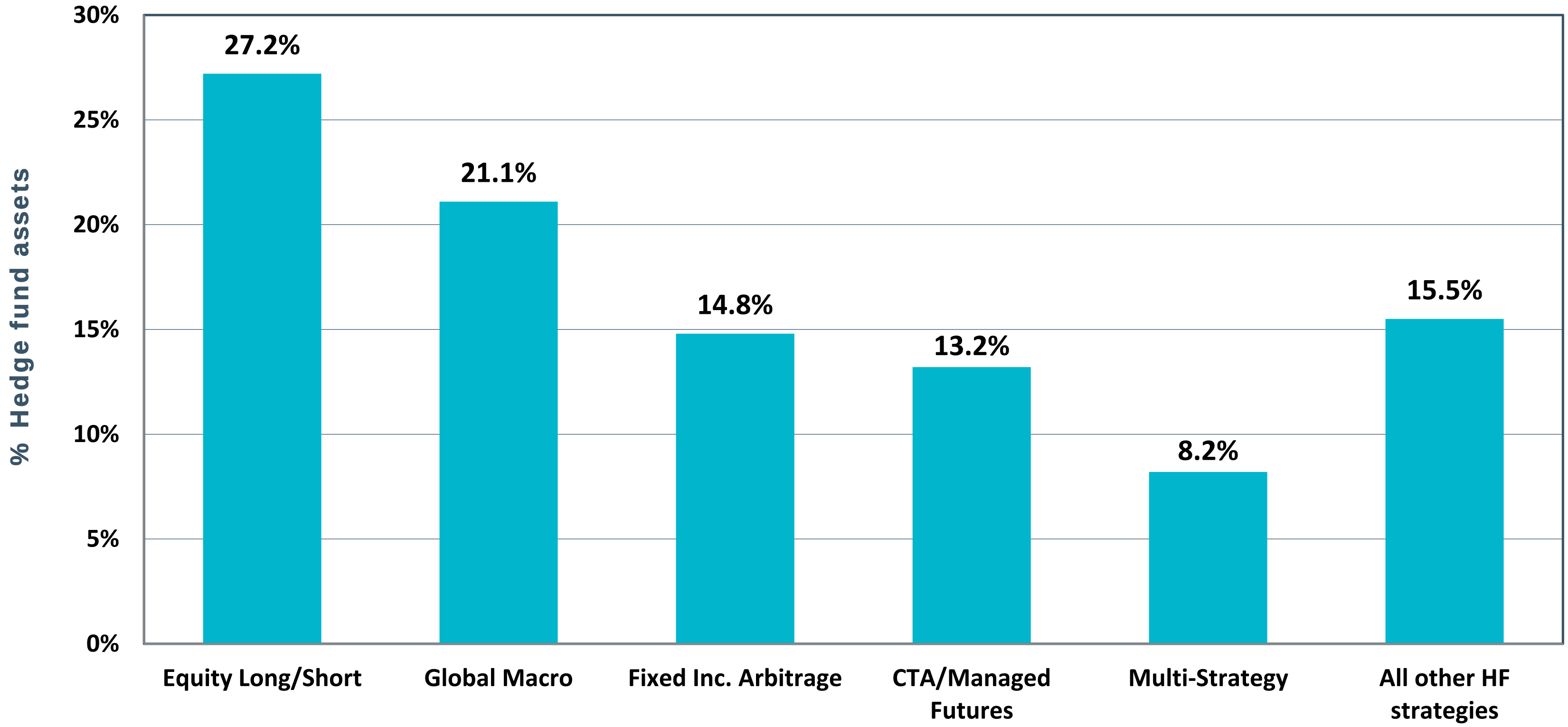
Trailing performance as of FY2014

Size of endowment	3 years	5 years	10 years
Over $1B	9.5%	12.1%	8.2%
$501 million to $1 billion	9.1%	11.8%	7.3%
$101 million to $500 billion	8.9%	11.8%	7.1%
$51 million to $100 billion	8.7%	11.4%	6.5%
$25 million to $50 billion	8.9%	11.4%	6.5%
Under $25 million	9.4%	12.0%	6.6%

- Larger endowments have been able to **outperform their counterparts over a 3, 5 and 10 year period**
- Larger endowments have tended to make greater use of **alternatives**
- Over a period of 10 years:
  - $1,000,000 compounded at 8.2% would be worth $2,199,240
  - $1,000,000 compounded at 6.6% would be worth $1,894,000

Source: 2014 NACUBO-Commonfund Study of Endowments FYE 2014, www.nacubo.org/About_NACUBO/Press_Room/2014_NACUBO-Commonfund_Study_of_Endowments_(Final_Data).html

Breakdown of hedge fund assets



Source: Citi Prime Finance. Note: Hedge Fund data is self-reported; each calculation is based on the respective data from funds who have reported for the current period. Asset and Strategy breakdowns updated as of 3/31/15. https://www.citibank.com/mss/products/investor_svcs/prime_finance/business_advisory/monthly_hfm.html#11

Implementation of Alternatives

A road map for implementation

Implementing alternatives: Process

1. Set specific goals: Strategic or tactical?
2. Determine method of implementation
3. Source the alternative allocation
4. Size the alternative allocation

Implementing alternatives: Process

Set specific goals: Strategic or tactical? → Determine method of implementation → Source the alternative allocation → Size the alternative allocation

Step 1: Set goals for implementing alternative strategies and asset classes

- Is this allocation strategic or tactical in nature?
- Determine what risks you want to address in the portfolio.

Implementing alternatives: Process

Set specific goals: Strategic or tactical? → **Determine method of implementation** → Source the alternative allocation → Size the alternative allocation

Step 1: Set goals for implementing alternative strategies and asset classes

- Is this allocation strategic or tactical in nature?
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Step 2: Determine method of implementing alternatives

- Consider a Core-Satellite approach for a strategic allocation.
- Determine whether a packaged solution or "build-it-yourself" method is appropriate.

Implementing alternatives: Process

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Step 3: Sourcing the alternative allocation

- Consider pulling money from equities, fixed income or a combination of both.
- What is the impact of allocating away from a particular asset class?

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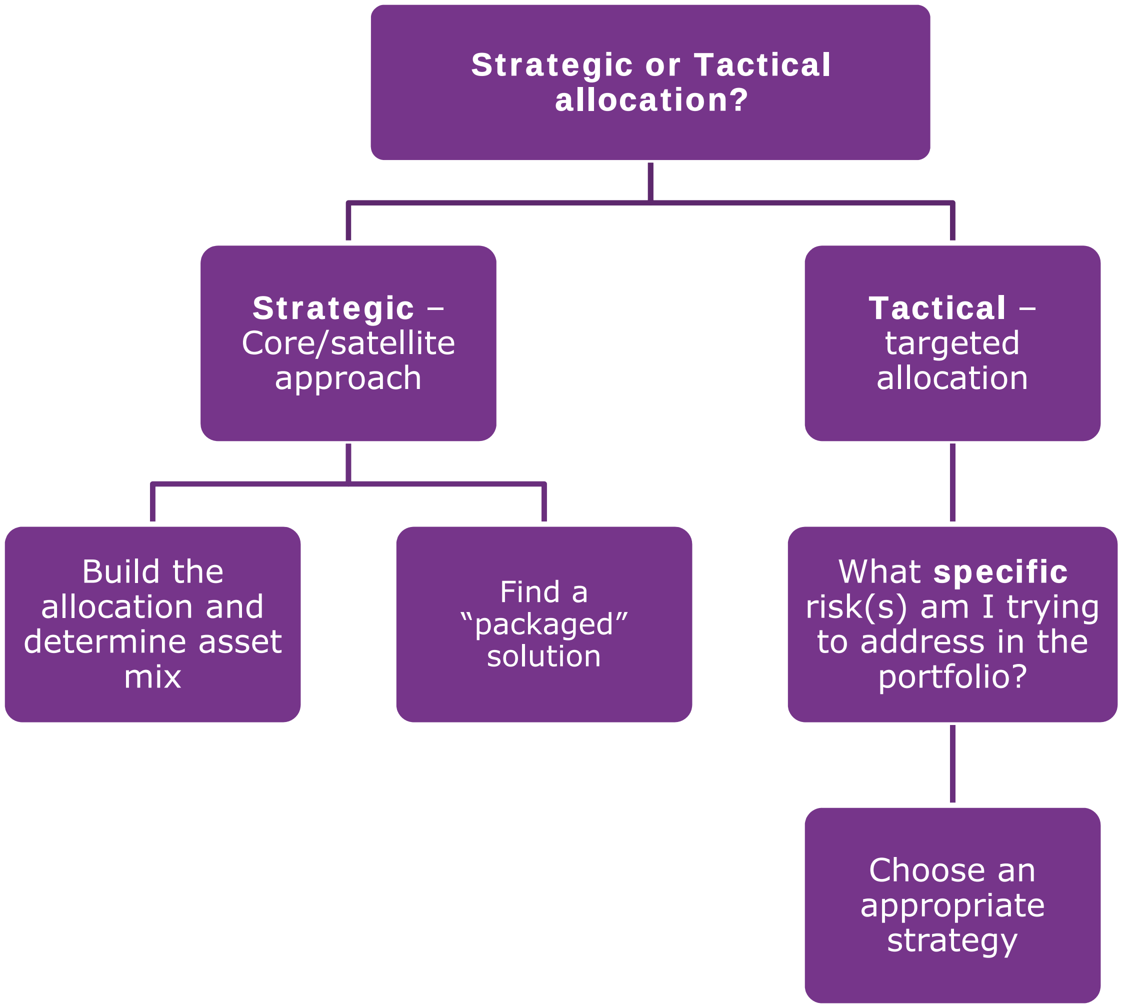
Step 4: Sizing the alternative allocation

- Determine the impact on risk and returns of an allocation to an alternative strategy.
- There is no single *correct* amount.
- What are the opportunity costs of the investment?

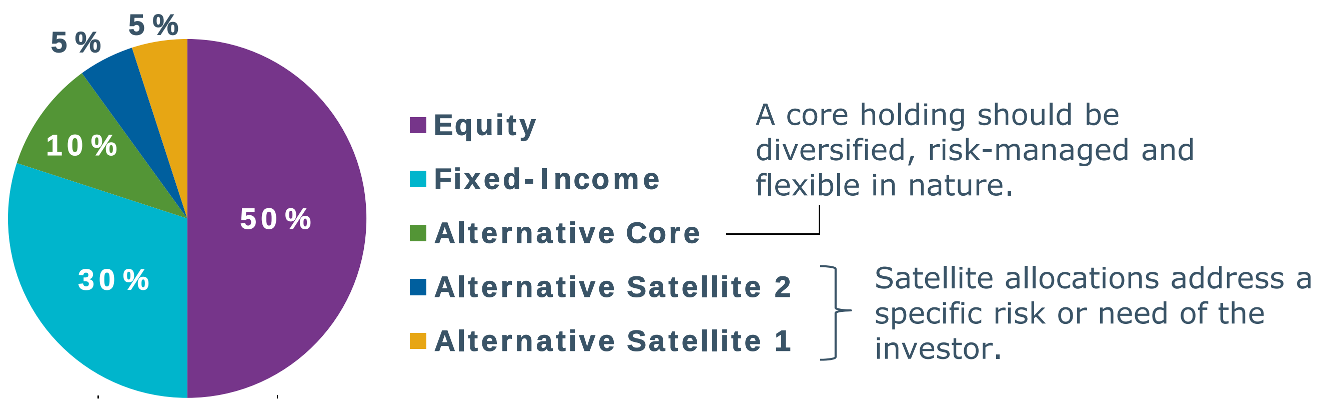
Step 1: Setting goals for an allocation



Step 2: Method of implementation – strategic allocation

A core/satellite approach

Core-satellite approach



Why should investors consider a strategic allocation to alternatives?

- May enable investors to **stay invested** across a variety of markets
- **Satellite** allocations allow advisors to address a **specific risk or need**
- The **opportunity costs** of investing in alternative investments may be high
- The **dispersion in returns** in alternative categories is **high** versus traditional mutual fund categories

Common mistakes when allocating to the alternative space

- **Chasing** performance – either of a particular fund or asset class
- **Optimizing** portfolios based on a single event, e.g. the financial crisis of 2008
- "De-risking" portfolios after market turmoil, known as "**barn door closing**"
- **Improper sizing** at the portfolio level, generally too little to make an impact

Alternative investments involve unique risks that may be different from those associated with traditional investments, including illiquidity and the potential for amplified losses or gains. Investors should fully understand the risks associated with any investment prior to investing.

Step 2: "Core" alternative strategies

What to look for in a "core" alternative

- **Risk management**: Is the strategy either explicitly or implicitly risk-managed?
  - Risk statistics to consider: Standard deviation, max drawdown and time to recover
- **Diversification:** Able to potentially make money from a variety of sources.
  - MPT statistics to consider: Correlations to S&P 500® and Barclays Aggregate Bond Index
  - Is the strategy highly correlated with either equities or fixed-income?
- **Flexible approach**: Can the fund adapt and change with market conditions?
  - Does the fund only make money in certain types of markets?
  - Can the strategy change over time given market conditions?

What types of strategies might fit as a "core"?

- **Multi-strategy funds**
  - Many of these funds will utilize a number of hedge fund managers as sub-advisors
  - Seek to provide the diversified approach of a multi-strategy hedge fund
- **Hedge fund replication strategies**
  - Seek to provide transparent, liquid and efficient exposure to a broad hedge fund universe
- **Absolute return strategies**
  - Can target a return over cash or inflation
  - Seek to provide a consistent level of return, regardless of market conditions

Step 2: "Satellite" alternative strategies – tactical

"Satellite" Alternative: Addresses a specific need in the portfolio: risk, return or diversification

Portfolio need / strategy name	Alpha differentiation	Volatility hedging	Equity risk offset	Inflation protection	Correlation benefits	Rising rate protection
Long/short equity	X	X			X	
Multialternative	X	X	X	X	X	X
Market neutral	X	X			X	X
Managed Futures	X	X	X	X	X	X
Multicurrency	X	X			X	
Non-traditional bond		X	X			X
REITs	X			X	X	X
Commodities	X			X	X	X

Step 3a: Sourcing the alternative allocation – correlations

How did correlations hold up during the last market correction?

Correlation Statistics (Oct 2007-Feb 2009)		
Correlations: Traditional Indices	BC Agg. Bond	S&P 500
MSCI AC World Index	0.47	0.96
MSCI Em Mkt.	0.42	0.82
NAREIT Index	0.34	0.85
Barclays HYLD Corp.	0.34	0.73
DJ UBS US Comm. Index	0.26	0.47
BC Agg. Bond	1.00	0.40
BC U.S. Muni	0.28	0.28
BC Long Gov.	0.86	0.21

Correlation Statistics (Oct 2007-Feb 2009)		
Correlations: Alternative Indices	BC Agg. Bond	S&P 500
HFRI Fund Weighted Index	0.26	0.72
HFRI Equity Hedge Index	0.27	0.77
HFRI Relative Value Index	0.28	0.66
HFRI Fund of Funds Index	0.16	0.58
HFRI Market Neutral Index	-0.17	0.10
Newedge CTA Index	-0.07	-0.42
Morningstar Gbl Long/Short Currency	-0.53	-0.64
HFRI Macro Index	0.07	-0.05

>=0.7
0.5>=x>0.7
0.3>=x>0.5
< 0.3

Correlations drive the asset allocation decision for sourcing the trade

1) Correlations aren't fixed in time
2) Correlations provide a sense of how assets move together
3) However, correlations don't explain the **magnitude** of a movement

Source: MPI Stylus, Morningstar, Statistics are shown from October 1st 2007 to February 27th, 2009.
This period is meant to illustrate a significant drawdown on the S&P 500®.

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Step 3b: Sourcing the alternative allocation: Risk statistics and "fit" in a portfolio

Risk Statistics (Oct 2007-Feb 2009)		
Risk Statistics: Traditional Indices	Beta to S&P 500	Max Drawdown
MSCI AC World Index	1.13	-54.9
MSCI Em Mkt.	1.47	-61.4
NAREIT Index	1.92	-64.8
Barclays HYLD Corp.	0.72	-32.7
DJ UBS US Comm. Index	0.69	-54.3
BC Agg. Bond	0.10	-3.8
BC U.S. Muni	0.10	-5.7
BC Long Gov.	0.15	-9.2

Risk Statistics (Oct 2007-Feb 2009)		
Risk Statistics: Alternative Indices	Beta to S&P 500	Max Drawdown
HFRI Fund Weighted Index	0.32	-21.4
HFRI Equity Hedge Index	0.46	-30.6
HFRI Relative Value Index	0.30	-18.0
HFRI Fund of Funds Index	0.26	-22.2
HFRI Market Neutral Index	0.02	-8.9
Newedge CTA Index	-0.15	-4.5
Morningstar Gbl Long/Short Currency	-0.27	-2.9
HFRI Macro Index	-0.01	-4.9

Risk statistics provide a sense of "where" the investment fits

1) Beta measures the magnitude of how an investment moves over time compared to another index/investment
2) Looking at **rolling** standard deviation or beta can help figure out the range of risk over time
3) Come back to the risk of the individual investment; asset classes are a guide

Source: MPI Stylus, Morningstar, Statistics are shown from October 1st 2007 to February 27th, 2009. This period is meant to illustrate a significant drawdown on the S&P 500.

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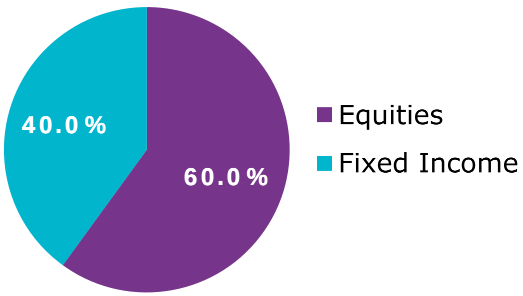
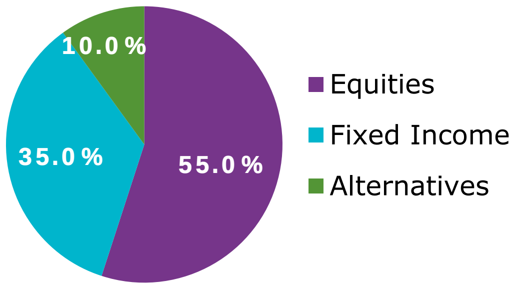
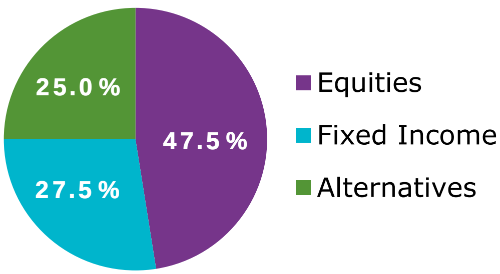
Step 4: Sizing the alternative allocation

Adding alternatives could have improved returns and reduced risk

Comparison of hypothetical allocations
(1/2/1990 – 6/30/2015)







60/40 Portfolio
Annualized Return.......................... 7.18%
Annualized Standard Deviation... 9.26%
Sharpe Ratio.................................... 0.40
Maximum Drawdown.................... -33.25%

Adding 10% in Alternative Strategies
Annualized Return.......................... 7.54%
Annualized Standard Deviation... 8.98%
Sharpe Ratio.................................... 0.45
Maximum Drawdown.................... -32.69%

Adding 25% in Alternative Strategies
Annualized Return.......................... 8.06%
Annualized Standard Deviation... 8.63%
Sharpe Ratio.................................... 0.52
Maximum Drawdown.................... -31.87%

Equities are represented by the MSCI World Index, fixed-income is represented by the Barclays Global Aggregate Bond Index and alternatives are represented by the HFRI Fund of Funds Index.

Source: MPI, Data from 1/2/1990 to 6/30/2015.

Alternative investments involve unique risks that may be different from those associated with traditional investments, including illiquidity and the potential for amplified losses or gains. Investors should fully understand the risks associated with any investment prior to investing.
Past performance is no guarantee of future results. Performance over different time periods may differ.

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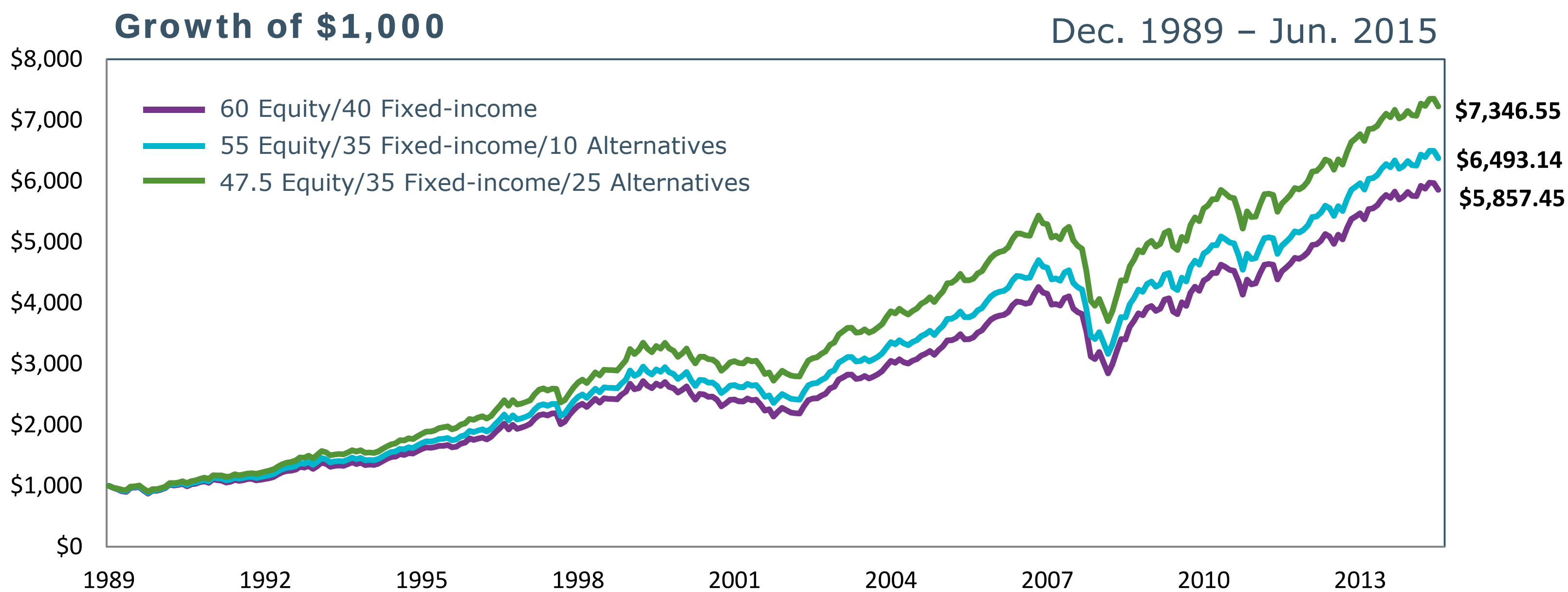

The next step: Benchmarking and measuring success with clients

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Equities are represented by the MSCI World Index, fixed income is represented by the Barclays Global Aggregate Bond Index and alternatives are represented by the HFRI Fund Weighted Index. Data provided by MPI. Performance over different time periods may differ.

Disclosure

Investing involves risk, including the risk of loss. Investment risks exist with equity, fixed-income, and alternative investments. Sophisticated and aggressive investment techniques such as leverage, derivatives, and short-selling can magnify a gain or loss.

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Barclays Global Aggregate Index provides a broad-based measure of the global investment-grade fixed income markets. The three major components of this index are the U.S. Aggregate, the Pan-European Aggregate, and the Asian-Pacific Aggregate Indices. The index also includes Eurodollar and Euro-Yen corporate bonds, Canadian government, agency and corporate securities, and USD investment grade 144A securities.

HFRI Fund of Funds Composite Index – Fund of Funds invest with multiple managers through funds or managed accounts. The strategy designs a diversified portfolio of managers with the objective of significantly lowering the risk (volatility) of investing with an individual manager. The Fund of Funds manager has discretion in choosing which strategies to invest in for the portfolio. A manager may allocate funds to numerous managers within a single strategy, or with numerous managers in multiple strategies. The minimum investment in a Fund of Funds may be lower than an investment in an individual hedge fund or managed account. The investor has the advantage of diversification among managers and styles with significantly less capital than investing with separate managers.

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MSCI All Country World Index is a market capitalization weighted equity index of stocks traded in 47 world markets.

Absolute Return Strategies: Absolute return strategies are not intended to outperform stocks and bonds during strong market rallies, and may underperform during periods of strong market performance.

Hedging Fund Replication / Hedging Techniques / Hedged Equity involves taking offsetting positions intended to reduce the volatility of an asset. If the hedging position behaves differently than expected, the volatility of the strategy as a whole may increase and even exceed the volatility of the asset being hedged.

REITs: Real estate investing may be subject to risks including but not limited to declines in the value of real estate, risks related to general economic conditions, changes in the value of the underlying property owned by the trust and defaults by borrowers.

Commodity: Commodity-related investments, including derivatives, may be affected by a number of factors including commodity prices, world events, import controls, and economic conditions and therefore may be more volatile than investments in traditional securities.

Options: Options may be used for hedging purposes, but also entail risks related to liquidity, market conditions and credit that may increase volatility.

Equity Securities: Equity securities are volatile and can decline significantly in response to broad market and economic conditions.

Concentration: Concentrated investments in a particular industry may be more vulnerable to adverse changes in that industry or the market as a whole.

Derivatives Derivatives, such as options, futures and forward contracts, involves risk of loss and may entail additional risks. These include lack of liquidity, possible losses greater than the Fund's initial investment, increased transaction costs, and higher volatility. Option premiums paid for or received by the Fund are small relative to the market value of the investments underlying the options. This means that buying and selling put and call options can be more speculative than investing directly in the securities they represent. Under certain market conditions, the Fund could be forced to sell securities or to close derivative positions at a loss. Because derivatives depend on the performance of an underlying asset, they can be highly volatile and are subject to market and credit risks.

Disclosure

Market Neutral strategies attempt to eliminate the risks of the market by holding 50% of assets in long positions in stocks and 50% of assets in short positions. Market neutral funds match the characteristics of their long and short portfolios, keeping factors such as P/E ratios and industry exposure similar. Stock picking, rather than broad market moves, should drive a market-neutral fund's performance.
Multicurrency strategies invest in U.S. and foreign currencies using short-term money market instruments; derivative instruments including (and not limited to) forward currency contracts, index swaps, and options; and cash deposits.
Multi-strategy funds offer exposure to several different alternative investment tactics and have a majority of their assets exposed to alternative strategies. Their tactics may change slightly over time in response to market movements. This category includes funds with static allocations to alternative strategies as well as funds that allocate tactically among alternative strategies and asset classes. Gross short exposure is greater than 20%.
Non-Traditional Bond strategies diverge in one or more ways from conventional bond fund investing. Many non-traditional bond funds describe themselves as "absolute return" portfolios, which seek to avoid losses and produce returns uncorrelated with the overall bond market, and they employ a variety of methods to achieve those aims.
Foreign Securities: Foreign securities may be subject to greater political, economic, environmental, credit, currency and information risks. Foreign securities may be subject to higher volatility than U.S. securities, sue to varying degrees of regulation and limited liquidity.
Leverage: Leverage can increase market exposure and magnify investment risk.

Before investing, consider the fund's investment objectives, risks, charges, and expenses. Visit ngam.natixis.com or call 800-862-4863 for a prospectus or a summary prospectus containing this and other information. Read it carefully.

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