

Macro Views, Sector Gains

In the world of absolute return, unlocking the patterns of broad economic and market catalysts is the key to successful investing. Michael Aronstein, portfolio manager of the Marketfield Fund, combines long and short strategies with insights into large scale macroeconomic forces and thematic factors to move a step ahead of the mechanisms that drive the markets.

What is your investment philosophy?

We look at it from a standpoint of what our value proposition is as a manager. We structure the fund to allow for maximum flexibility, so that you can use both sides of the market - the long and the short side. The short side, which is limited but significant, gives us the ability to exercise some hedging and express opinions that have to do with negatives as well as positives.

We believe we have a more comprehensive insight into the large scale macroeconomic forces, the exogenous forces that affect all companies, out of broad thematic movements within the economy generally set off by economic anomalies, by unusual sets of relationships. These tend to drive the economic environments at the margin for years and years.

How do you implement this philosophy into your investment process?

On the way up in this cycle, the extraordinarily low level of interest rates, both nominal and real, starting in 2001, 2002, and persisting right up until 2004, created an environment that was driven largely by people's desire to take advantage of that kind of limitless and undervalued credit, where people were bent on figuring out how to create leverage. The easiest way for most individuals to

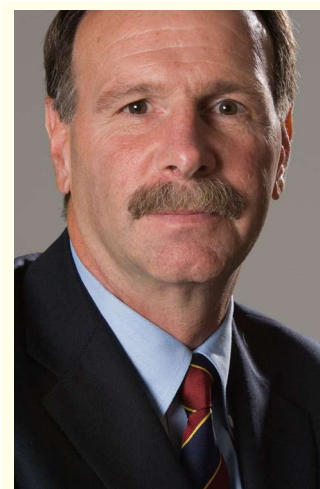
"We have maintained the view that if we couldn't find reasons to invest in the economically sensitive stocks, we wouldn't want to invest in stocks at all."

achieve that was with single-family homes; for most businesses, it was with securities. Both can be leveraged instantaneously and extensively. Margin requirements in the institutional securities world are rather lax and the leverage ratio is high. We look back in hindsight but, in some cases, you could get a single-family home at or near 100% leverage.

After 2002, the economy was not doing badly and the Fed didn't recognize that pattern. In that environment, we moved people toward what we believed were the most leverage-sensitive assets. These were the first derivatives that were linked to emerging markets, commodity related, and all things that would benefit from that environment. That theme persisted for four years without much deviation.

In terms of the investment cycle, there was some cyclical but nothing major. It culminated in late 2005 and early 2006 driven by mortgage securities in housing, which led to overinvestment. We feel that our value resides in our understanding of those driving forces; each cycle has a unique set of them and they are persistent, unlike markets. Markets fluctuate a lot but the main driving forces behind them do not. They are generally quite persistent and this one, which is the reversion of the whole credit cycle, has been in force in various forms for three years.

We spend most of our time looking at factors that affect those marginal driving forces. There are hundreds of them around the world, shifting in every cycle, and that is what makes them so difficult to



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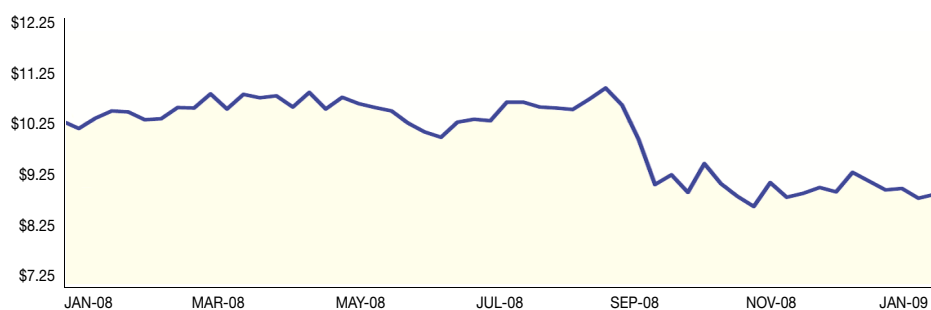
Prior to joining Oscar Gruss in 2004, Aronstein was Chief Investment Strategist at Preservation Group, a provider of independent macroeconomic and strategic advice to professional investors.

Aronstein began his investment career in 1979 at Merrill Lynch, where he remained for nine years, holding positions as Senior Market Analyst from 1980 to 1983 and Senior Investment Strategist and Manager of global investment strategy from 1983 to 1987. In 1993 he founded West Course Capital, a discretionary commodity management firm that managed funds for domestic and international clients, taking a long term approach to investment in traditional industrial and agricultural commodities.

In 1995, Aronstein was cited in the *Financial Times Guide to Global Investment* as one of the ten best investors of the decade.

Performance - Price History N.A.V.

Marketfield Fund (MFLDX)



model quantitatively. For similar reasons most of the quantitative approaches to capturing the macroeconomic forces and modeling them have failed. That is why we have a qualitative approach, driven by the input of a lot of data with fully qualitative assessment and a lot of experience behind it. This model drives the whole investment process that we employ.

We try to look at the outgrowth of the forces that we believe are shaping the economic environment in order to see whether there are prices at odds with what we think the major risks or rewards might be. This is where whole sectors have been thrown overboard because of a perception that whatever the prior cycle was is going to persist forever. That was the case with emerging market stocks in 2003, when people had absolutely no interest for a stand in any of them. It was fully based on a belief that the somewhat deflationary environment that arose after 2000 was going to persist. The developing market economies could not survive in an environment like that, and we took a strong opposite view, combined with stock market valuations that were compelling too. At that time, you could buy many high-grade companies at four, five and six times earnings. Those companies had been in business for about fifty years and had gone through currency devaluations, labor strikes and wars.

We have strong opinions that we try to express with some degree of restraint at turning points. The portfolio doesn't look unusual; it's the strengths of the opinions behind it as we try to be interested in maintaining some discipline rather than concentrate across either

asset types or sectors. We have had unusually aggressive positions at times. For instance, we have had good exposure to gold mining stocks, but it is near 10% of the portfolio, not 40% or 50%, which I would categorize as more of an aggressive hedge fund type of bet.

What is your portfolio construction process?

Because we are an absolute return fund, we do not have any benchmarks. We look at ideas where we believe we can make money. There may be a big variance between the fund any of the major benchmarks or averages. We look at where we think there is value and where there are forces that are acting on the macroeconomic environment that are destructive to some enterprises.

We have never even had 1% net exposure to anything related to finance for the last 18 months. At one point the financial sector in the S&P index was 22% of all industries. We probably had a net exposure of negative 15, and that is an enormous variance.

Even now, we have zero net exposure to financials and this is largely due to our world view that they are not beneficiaries, at least not directly. Some of the stocks that are \$2 or \$3 could double or treble but our macroeconomic view does not lead us to a comfort level that that is the likely outcome. If such a stock is going to double or treble, we'd rather own a homebuilder with a good balance sheet that is generating positive cash flow because the two of them are not going to diverge that much in terms of the environmental impacts.

We go about portfolio construction opportunistically, out of what the implications are across various sectors of the environment we believe is evolving. Then we try to diversify, so that we don't wind up with correlations sector to sector or company to company where you have really single point determinants that are all local. In contrast, we are talking about global determinants that we think are overlooked or at least misunderstood by the majority of people. We would not want to compound with a lot of local correlation because we could be right about the entire environment, but having too many stocks in a group means that any kind of local distress may cause all of them to go down at once for no particular reason.

How do you use the macro view before you decide what sectors of the economy to invest in?

We formulate our own macro view and we compare it to where the markets are, what is implicit in their structure, and whether the markets are somewhat in accordance with that view. We also seek to compare whether there is a real disparity between the implied view across markets and our own view, in which case we tend to be more aggressive.

We are aware of the belief that the current environment will turn, but that will not happen because of the banks. We think the catalyst will be the capital markets, the provision of credit directly through the capital markets that is going to refinance those parts of the economy that are in jeopardy right now. Our view is that the necessary precondition to seeing things improve to an extent would be not only a repair of the bond markets but also the beginning of issuance. That is, new issuance showing that the capital markets were receptive to a refinancing, at least of high-grade credits.

There are billions of dollars placed in those markets on a weekly basis, and that is a mechanism for circumventing the impaired portions of the banking system. The entire banking system is not impaired; it is really the hybrid investments that were concentrated too much in the real estate end. With that view in front of us, we feel that there are real opportunities in stocks that are tied to the overall economic environment. We have maintained the

view that if we couldn't find reasons to invest in the economically sensitive stocks, we wouldn't want to invest in stocks at all.

Today, it is popular to begin putting money back in stocks as long as you buy the food, tobacco, drugs, and personal care stocks. Those are somewhat apart from the normal fluctuations in the economy. Yet, if those stocks are all you want to own, you will be better off owning bonds. If your assumption is that the environment cannot improve to a point where some of these technology, transportation, consumer cyclical names and home builders do better, then it's not worth taking the equity risk. We are in an environment where if you are willing to take risk, you need to take the risk that the environment is going to change.

A big component of this economy is that it is extraordinarily interest sensitive. That is the flip side of the fact that we are an indebted economy. Even though spreads are reasonably wide, the absolute level of rates of all corporate bonds and some of the upper grade corporate bonds are all below their 50 and 60 year averages in terms of yield. In terms of spreads, mortgage rates are around 5%; long-term conforming mortgages and the refinancing activity is really proceeding at an intensive rate. Generally, these are all the things you would want to see to suggest that the emergency conditions of the fourth quarter of 2008 are beginning to abate.

How is the current account surplus in Asia and the Middle East likely to be spent or invested in the future?

Treasury bonds have been the best returning asset of any of these sovereign wealth funds. The total return in the last couple of years has been tremendous to the extent that they don't wish to hold liquid assets that are dollar denominated, which means that they are going to spend the money. They are not going to mind whether they can buy raw materials, distribute it to the population, capitalize their own banks.

How are the currently imbalance global financial systems likely to pay out in the near future?


At present, we are in an asset deflation that

is leveling off. When it does level off and turn the other way, people are going to treat that as a big positive. If the price of copper goes from \$3,000 to \$5,000 a ton, that move is going to be looked upon with great glee. But, if it goes from \$5,000 to \$12,000, then it will be perceived as an issue and it is really going to hurt the consumers. There is enough liquidity in the world to allow for even more imbalances. At some point people are going to be including these central bank liquidity funds; they are not going to sit there with safe monitor type of assets, whether they are dollar, euro, or yen based. The returns are going to be inadequate and investors are going to look for alternatives.

I don't think that we should shape our risk model based on the assumption that we are going to have a repeat of the last two years. It is possible that you have enough financial distress, enough out of sample failures, and then disruptive occurrences where you see another round of forced liquidation of everything. However, I don't think that governments are pointing in that direction right now. I simply do not believe that there is any more appetite to let another round of financial institutions, pension funds or big manufacturing companies fail.

What is your approach to risk management?

Our risk management is based upon a belief that the biggest risk for an investor is that of the stampede. Risk is having an opinion that is shared in terms of the distribution of ownership in a market. If that opinion proves right, even if it is temporarily invalid, you are going to be run over by everybody else trying to exit. Risk is a serious impairment of capital that derives from the popularity of our views.

We try to be extremely disciplined about our exposures at turning points when we commit to certain plays. That means we will never be 110% long in equities. We are probably never going to be 60% or 70% invested in allied sectors because, with the opinions being strong as they are, the expression has to be moderated. We are not trying to net 50% or 60% a year. Our objective is to present a reasonable risk adjusted equity type of return to the people we run money for, which includes many of the members of our firm and families. 

Marketfield Fund

Symbol	MFLDX
Website	www.marketfield.com
Address	Marketfield Asset Management LLC 292 Madison Avenue, 14th Floor New York, NY 10017
Telephone	888-236-4298
Inception	07/31/2007

PORTFOLIO	
Total Net Assets*	\$34.2
Avg Mkt Cap (\$ Weighted) *	\$50,400
Average Price/Earnings Ratio	20.4x
Average Price/Book Ratio	3.2x
Turnover Ratio	123%

INVESTMENT INFORMATION	
New Investment	Open
Min Initial Investment	\$25,000
Min Subsequent Investment	\$100
Min Initial IRA Investment	\$25,000

RETURNS VS. LIPPER FLEX PORT FD INDEX		
	MFLDX	Index
Since Inception (Ann.)	-13.10%	N/A
1 Year (Cum.)	-14.61%	-30.74%

FEES AND EXPENSES	
Max Sales Charge - Front	0.00%
Max Sales Charge - Deferred	0.00%
Max Redemption Fee**	1.00%
Total Expense Ratio	1.75%

PORTFOLIO MANAGER	
Michael Aronstein	07/16/2007

*millions **2 months after purchase
01/31/2009; Source: Company Documents; Lipper

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