

## MAAP February Review

March 1, 2010

MAAP had a positive return in February as five of the six asset groups contributed to the gain. Gains in order of their relative contribution included long positions in energy, grains, metals, S&P 500, and currencies. A small loss occurred in the short U.S. Treasury bond position. Our systematic risk process, which when triggered limits leverage in the three commodity sectors, remained in effect throughout February. As a result the long positions in the energy, grains, and metals sectors were at 50 percent of maximum. In the near future, the MAAP portfolio may expand the markets traded to include the Mexican peso in the currency group, and the Japanese Nikkei 225 Index within the equity group.

Two events since early January have contributed to corrections in the markets. First, the Chinese government is attempting to rein in excessive credit used to finance real estate speculation in China. Their goal is not to stop economic expansion in China but to prevent excessive speculation and curb inflationary pressures. Their greater government control of economic and financial activity allows more targeted intervention than in more democratic societies. While success may be achieved in controlling real estate speculation, they will have greater difficulty controlling inflation, so long as they prevent their currency, the yuan, from appreciating. We fully expect that China will either revalue their currency on a one time basis, or allow it to appreciate before the end 2010. When this occurs, it will dampen inflationary pressures in China as imports become cheaper and demand is able to increase. This increase in raw material demand will put upward price pressure on all global commodity prices denominated in dollars. In summary, while Chinese monetary decisions have created a temporary hiccup in commodity markets, growing global economic activity, and the potential for a yuan revaluation, will continue to exert upward pressure on commodity prices as 2010 unfolds.

The second factor roiling markets has been the sovereign debt crisis in Europe, with the attendant threat to the euro as a currency. The euro is an imperfect currency unit, most notably because it was created before a single sovereign government was created in the Euro block of countries. While there are many shortcomings, the cost efficiency for business, of a single currency unit and the elimination of tariffs, are so great that it is hard to imagine a dissolution. Furthermore, the European Union is in approximate equilibrium in terms of its balance of payments with the rest of the world, unlike the U.S. which is in serious deficit. As the world continues to look for alternatives to the dollar, the euro will remain a beneficiary of this diversification. Although the world has been focusing on the Greek debt problem, debt problems within several of the largest U.S. states are far more serious. Therefore negative psychology is likely to refocus on the dollar in the next several months.

It remains our view that the global economy is in an expansion that is led by the developing world. There is a self reinforcing momentum, as the middle class in these countries expands and seeks lifestyles similar to those in the developed world. This demand growth in the developing world is putting upward price pressure on basic commodities. While the developed world continues to suffer from an excess debt hangover, the one bright spot is export growth of manufactured goods to the developing world. In this global environment, commodity and precious metals prices will continue to provide relative price strength eventually causing a broadening of inflationary price pressures. In addition the dollar should resume its long-term weakness along with pressures for rising interest rates on long-term bonds. In this global environment, MAAP is well positioned to offer diversified investment opportunities.