Rethinking Absolute Return

March 2013 | White Paper

Our Goal

Is to help you learn why:

- Alternatives are gaining in popularity for advisors to use with investors.
- Absolute return, a type of alternative investment, should be considered as part of an investor's overall investment strategy to help address persistent volatility.
- The Brinker Capital Crystal Strategies Suite of absolute return Portfolios are appropriate for different life stages – building wealth, at or near retirement.

Imagine yourself standing at the top of a mountain. You are faced with three routes to ski down – green, blue or black.

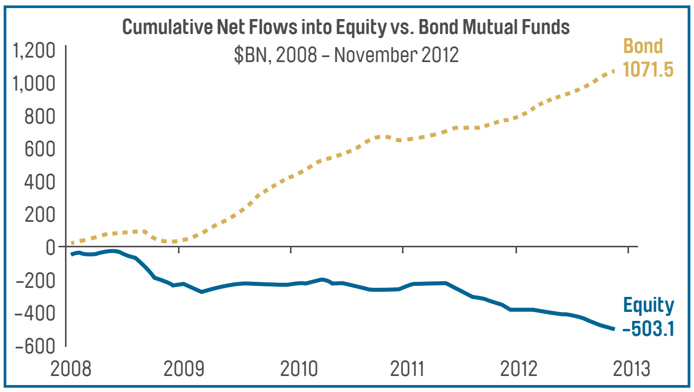
The green circle is considered a beginners slope and typically the easiest and most well-groomed trails on the mountain. The blue square marks an intermediate slope with trails generally steeper than the beginner trails, yet easy enough for advanced skiers. Finally, there is the black diamond option, which marks the most difficult trail marked by steep, narrow or ungroomed terrain. In order to properly choose the route that is right for you, it is important to not only evaluate your options, but understand the level of risk-taking you are most comfortable with.

Investing can be similar to skiing. There are typically numerous ways for an investor to reach their investment goals, they just need to identify the most comfortable route based on personal objectives and level of risk tolerance.

A Rocky Ride

Undoubtedly, the market has been anything but comfortable for investors during the past few years. The 2008 credit crisis exposed new risks and nearly every asset class saw significant declines. No style seemed safer than another. This volatility, combined with falling home prices, high unemployment and a general lack of trust in the government to bring spending down, has driven many investors to question if they can stomach the unpredictability and if they should remain invested.

With the fear of the stock market clouding emotions, many investors shifted their assets out of the equity market and into "safer" bond funds. While bonds have performed well since 2009, averaging about 26.5% in total return, the S&P 500 increased 83.7%.[1] Volatility has increased dramatically in the equity markets over the past decade and the trend is expected to continue. While in 2011 the long-term performance of bonds outpaced that of stocks over the previous 30 years, there is concern from many analysts that this is an indication of bond prices peaking and that bonds could prove to be disappointing in the coming years.[2]



Source: Strategas Research Partners

Volatility Fatigue

It's no surprise that investors are exhausted. Many have seen their investments seesaw repeatedly during the last five years and wonder when it will end. Now many analysts are suggesting that the risk has shifted and valuations for equities might be cheaper.

Many advisors now believe that more diversification needs to be placed into their client's portfolios; however, they understand that it may be challenging to re-engage investors out of a cash position or fixed income instrument.[3] This is emphasized by a recent study that revealed an overwhelming number of advisors (85% of those surveyed) believe that equities will raise more money than fixed income in 2013. Consequently, in 2013 advisors say they will be allocating more of their clients' assets toward equities, emerging markets, alternatives – absolute return – less to private equity and international, and about the same to fixed income.[4]

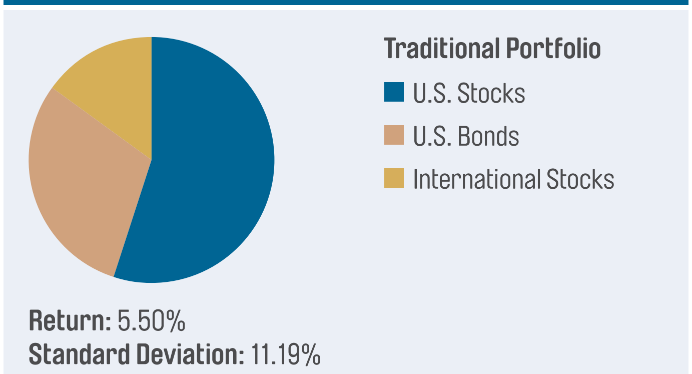
There Must be a Better Way

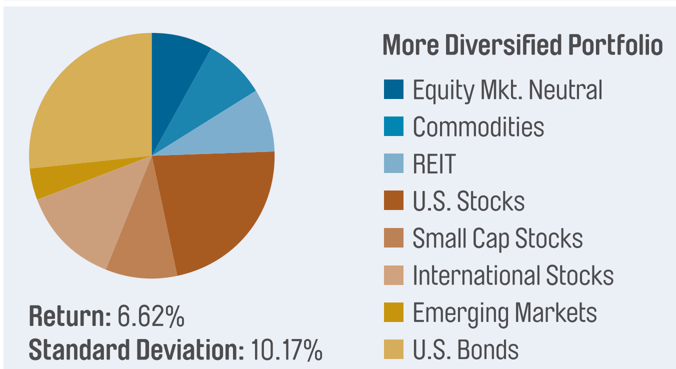
For years, a diversified portfolio of stocks and bonds was considered the optimal way to invest. However, after 2008, many began to revisit this premise. During the depths of the downturn, traditional asset classes became increasingly correlated, declining in tandem instead of offsetting each other.

Dissatisfied investors lamented that there must be a better way to invest. Several groups of investors, from large pension plans to endowments to high-net-worth individuals, have employed a better way for years by using alternative asset classes that are less correlated to the markets and that provide additional opportunities for growth and risk management. These sophisticated investors have enhanced their diversification potential resulting in an improved risk-return profile overall.

Consider that from 1998-2012 a traditional portfolio combining stocks and bonds returned an average of 5.50% with a standard deviation around 11%. Adding alternatives, such as hedge funds, private equity and real assets, improved the trade-off by boosting returns and lowering risk overall.

A multi-sector portfolio that includes alternatives can improve your risk-return profile





Source: FactSet, Brinker Capital (1998–2012). See Page 6 for additional disclosure.[5]

Advantages	Drawbacks
Seeks positive performance regardless of market conditions	"Lock-ups" may reduce liquidity
Returns are less market-driven and more dependent on manager's skill	Not as transparent in terms of reporting
Manager has fewer constraints—wide variety of tools at disposal (including the use of leverage)	Usually involve higher fees, including an incentive component

The Alternative Approach

Alternative investments, specifically absolute return strategies, we believe offer many advantages: returns are less market driven and more dependent on manager's skill and they seek positive performance regardless of market conditions – relative to traditional investments, but their restrictive packaging has some drawbacks.

Some drawbacks to consider: the liquidity of the portfolio may be reduced by lock-up periods, reporting is not as transparent and they usually involve higher fees.

Ongoing volatility has only served to fuel investors' appetite for alternatives. Adding alternatives to a portfolio may provide the opportunity to better manage and control volatility. And when paired with a traditional asset allocation, alternatives offer the potential for a more consistent return overall.

As investors have started to dive deeper into the world of alternatives, absolute return strategies have emerged as a strong contender. Absolute return strategies seek to take advantage of both good and bad markets as they are free from chasing a specific index. They are designed to meet targeted needs over a specified timeframe, rather than compete against the financial markets, making them suitable for many types of investors.

The Best of Both Worlds

	Traditional Hedge Fund	Separately Managed Account	Mutual Fund Hedged Strategies
Daily Liquidity		■	■
Daily Holdings Transparency		■	
Client Tax Loss Harvesting		■	
Lower Fees (compared to many absolute return vehicles)		■	
Unconstrained Investments	■	■	■

Source: Brinker Capital

Brinker Capital has designed a suite of absolute return products, Crystal Strategies, that are savvy like hedge funds, multi-sector, unconstrained and tactical, in an investor-friendly separately managed account (SMA) platform – liquid, transparent and cost-effective. And better yet, they are available in a format that is easy and preferable for advisors to access. (A study reveals that 57% of advisors prefer to access absolute return strategies for clients via separately managed accounts).[6] Through innovative investment solutions such as Crystal Strategy I, Brinker Capital seeks to provide real purchasing power for investors and sustainable purchasing power for future generations.

> The Crystal Strategies Suite of Portfolios uses extensive diversification as the primary method to generate a positive return, while protecting on the downside.

This results in being able to potentially reduce volatility while having multiple strategies and asset classes at work at all times.

Crystal Strategy I, one of the products in the suite, has the objective of mirroring the Consumer Price Index plus 3% – 5% over a three-year market cycle. Crystal Strategy I seeks to participate in the equity markets but also provides greater stability during periods of volatility and offer downside protection.

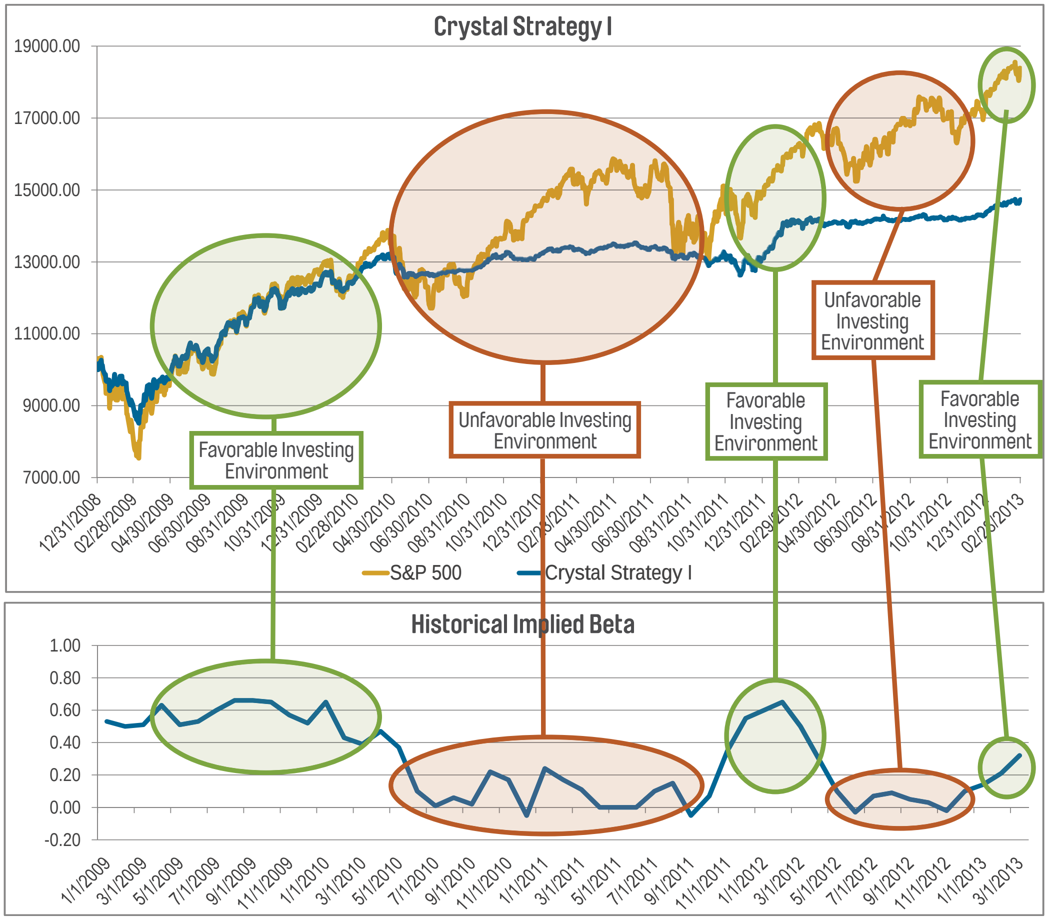
Manage Volatility
- Reach targeted return over three-year market cycle
- Achieve "equity-like" capital appreciation

Six Asset Class Diversification
- Active and passive vehicles
- Highly focused stock selection

Active Risk Management
- Strategic perspective
- Tactical overlay
- Hedging capabilities

Looking Back

Although quite unpredictable, history can often be an indicator of things to come. Brinker Capital knows this and has the ability with Crystal Strategy I to vary its investment strategy depending on the perceived market and economic conditions. As a result, the portfolio is dynamic and will change over time. During turbulent markets, Brinker Capital will strive to reduce risk through hedging or increase the weighting to more conservative strategies. During periods of economic and market growth, Brinker Capital can tilt the portfolio towards strategies more focused on capital appreciation. Crystal Strategy I allows investors to participate in the market while smoothing out the ride.



Source: Brinker Capital

There Will be Moments of Volatility

Drawdowns, or the reduction a portfolio might experience when the market retraces, are the inevitable part of any investment. There will be periods where investors will make decisions based on emotion, and not rational thought and Brinker Capital understands that. Crystal Strategy I was designed with these periods in mind to act as a cushion during periods when the S&P 500 retraces – and it has worked. Below is an illustration of how Crystal Strategy I helped to manage the volatility of the S&P 500 and provide a relatively consistent portfolio experience. Because Crystal Strategy I can go long or short, it has limited drawdowns more effectively than the S&P 500 since its inception.

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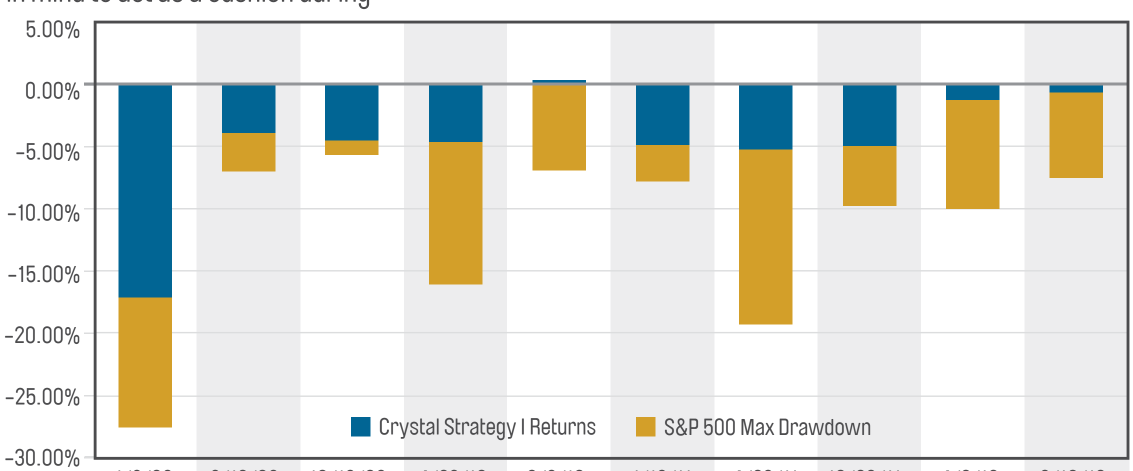

	1/6/09 – 3/9/09	6/12/09 – 7/10/09	10/19/09 – 10/30/09	4/23/10 – 7/2/10	8/9/10 – 8/26/10	1/19/11 – 2/8/11	4/29/11 – 10/3/11	10/28/11 – 11/25/11	4/2/12 – 6/4/12	9/10/12 – 11/12/12
Crystal	-17.12%	-3.92%	-4.46%	-4.59%	0.13%	-4.40%	-5.31%	-4.93%	-1.24%	-0.68%
S&P	-27.50%	-7.08%	-5.60%	-16.00%	-7.10%	-8.10%	-19.38%	-9.80%	-10.00%	-7.60%

Source: Brinker Capital. See page 6 for additioanl disclosures.[7]

Evaluating Your Route

An investor's experience of a loss is two times greater than the positive feelings of a gain.[8] Many advisors understand (79% of those surveyed) this concept and frame discussions to focus on overall progress towards investment/retirement goals and objectives rather than a benchmark like the S&P 500.[9] By benchmarking against your personal goals, such as saving for college or purchasing a vacation home, instead of an arbitrary capital market index, the progress becomes more meaningful to your specific needs.

Brinker Capital's goal is to provide an alternative paradigm that gives you an additional option and way to construct a portfolio that can mitigate the emotional impact often realized when investing in only stocks and bonds.

Utilizing both tactical and strategic processes, Crystal Strategy I seeks to outpace inflation by 3% - 5% over a full market cycle. Brinker Capital brings this time-tested investment strategy to you in a way that endowments and hedge funds haven't done before, providing you with the liquidity and transparency you need to stay well informed.

Brinker Capital broadly diversifies across six major asset classes and can have an average of 40 different strategies at work at any given time. In addition to researching and adding industry-leading managers, a focused stock selection approach is employed. To manage volatility and potentially reduce overall risk, Brinker Capital has the ability to actively hedge portfolios. Brinker Capital may use multiple risk reduction tools—taking short positions, reallocating to stable asset classes or emphasizing strategies with less market

Source: Brinker Capital

risk—depending on which is the most efficient given the market environment at the time.

Choose Blue

Whether you're at or nearing retirement or just starting to build wealth, the Crystal Strategies Suite of Portfolios can offer key benefits to support your overall investment strategy. Crystal Strategies can be used as a complement to a relative return strategy to help manage volatility, as a core satellite approach for the long-term growth of assets, as a fixed income replacement or to help bridge the accumulation and distribution phases to protect against inflation.

No longer do you have to sacrifice liquidity, transparency and competitive fees in order to capture the benefits of investing in alternatives. Whether you are an investor that is more comfortable with "black diamond" risk, or just a beginner that is more reserved and tends to favor the "green circle slopes", the Brinker Capital Crystal Strategy Suite of Portfolios can help navigate the bumps of investing and offer a smoother ride to obtaining your goals and objectives.

Contact your financial advisor today to determine which Crystal Strategies Portfolio is right for you.

Portfolios that Address Many Different Types of Investor Goals

Investment Time Horizon (years)	3-20	21-40	40+
Investor Profile	Retirement	Nearing Retirement	Building Wealth
Priority	Manage Volatility	Inflation Protection	Long-term Growth of Assets
Strategic Approach	Complement to Relative Return Strategy	Bridge from Accumulation to Distribution	Long-term Alternative to Risk Protection Assets

Source: Brinker Capital

Disclosures and Sources

[1] Source: Thompson Reuters, 1/1/2009–2/28/2013.

[2] Source: Bonds Beat Stocks in 2011 – But Don't Expect That to Repeat. DailyFinance.com, January 2012

[3] Source: Scared Stockless: How Advisors Calm Jittery Clients, AdvisorOne, March 2013

[4] Source: Brinker Barometer, 2013

[5] Source: FactSet, Brinker Capital (1998–2012). Allocation created by Brinker Capital. Indexes and weights of the traditional portfolio are as follows: U.S. Stocks: 55% S&P 500 Total Return; U.S. Bonds: 30% Barclays U.S. Aggregate; International stocks: 15% MSCI EAFE Gross Return. Indexes and weights of the more diversified portfolio are as follows: Equity Market Neutral: 8.3% HFRI Equity Hedge, Equity Market Neutral; Commodities: 8.3% DJ UBS Commodities Total Return; REITs: 8.3% FTSE NAREIT Equity REITs Total Return; U.S. Stocks: 22.2% S&P 500 Total Return; Small Cap Stocks: 8.8% Russell 2000 Total Return; International Stocks: 13.2% MSCI EAFE Gross Return; Emerging Markets: 4.4% MSCI EMF Gross Return; U.S. Bonds: 26.5% Barclays U.S. Aggregate. Performance is from a hypothetical portfolio and is shown for illustrative purposes only. Past returns are no guarantee of future results. Diversification does not guarantee investment returns and does not eliminate risk of loss.

[6] Source: Brinker Barometer, 2013

[7] Source: Brinker Capital. Performance shown is based on a model account assuming an average 1.61% quarterly fee and is shown for illustrative purposes only. Past returns are no guarantee of future results.

[8] Source: "The Framing of decisions and the psychology of choice," Tversky, Amos, Kahneman, Daniel, 1981

[9] Source: Brinker Barometer, 2013

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