



Opalesque Round Table Series '13 HARD ASSETS

Opalesque Roundtable Series Sponsor:



Editor's Note

Dramatic increases of activity, interest and investment options in Hard Assets

"Hard Assets" are experiencing dramatic increases in activity and investor interest. Since the financial crisis, this sector has considerably matured and innovated - investors today probably have more choice than they realise.

Many are receptive to the idea of investing in gold in order to hedge against various types of uncertainties, including financial crises, unintended consequences of QE, fiat currency risk, or purchasing power, among others. For those investors, gold is basically an insurance play. Others on the other hand, believe that passive long exposure to the market, be it in bullion or through an ETF, will likely fail to deliver the returns these investors are looking for. To address those issues, a new breed of managers is using options to construct a strategy that is flat or short premium and able to address both issues of tail risk and capital preservation. Tactical strategies have replaced the "long GSCI and bury your head in the sand" type of commodities investing, also in soft commodities.

And who says hard assets are necessarily illiquid? Eurex's new exchange-listed derivatives offer access to diverse assets such as property futures based on commercial real estate sector indexes, or futures based on European Processing Potatoes.

The Opalesque Hard Assets Roundtable also discussed:

- **Are ETFs suitable to invest in Hard Assets? What is required from a Diamond ETF?**
- **What are the primary sources of Alpha in agricultural commodities trading?**
- **Are there sound entry and exit strategies for the diamond, colored gemstone, fine jewelry and antiquities markets?**
- **Why was 2013 the year of the "massive gold wealth transfer"?**
- **"One of the best ROIs": Why Stephen Silver gave away the Cullinan Blue Diamond Necklace as a donation strategy**
- **Does De Beers really have a "strategic diamond reserve"?**
- **What trends are happening in the different Hard Assets markets right now? How do government and central bank policies affect Hard Assets strategies?**
- **Where do managers find opportunities and generate alpha?**

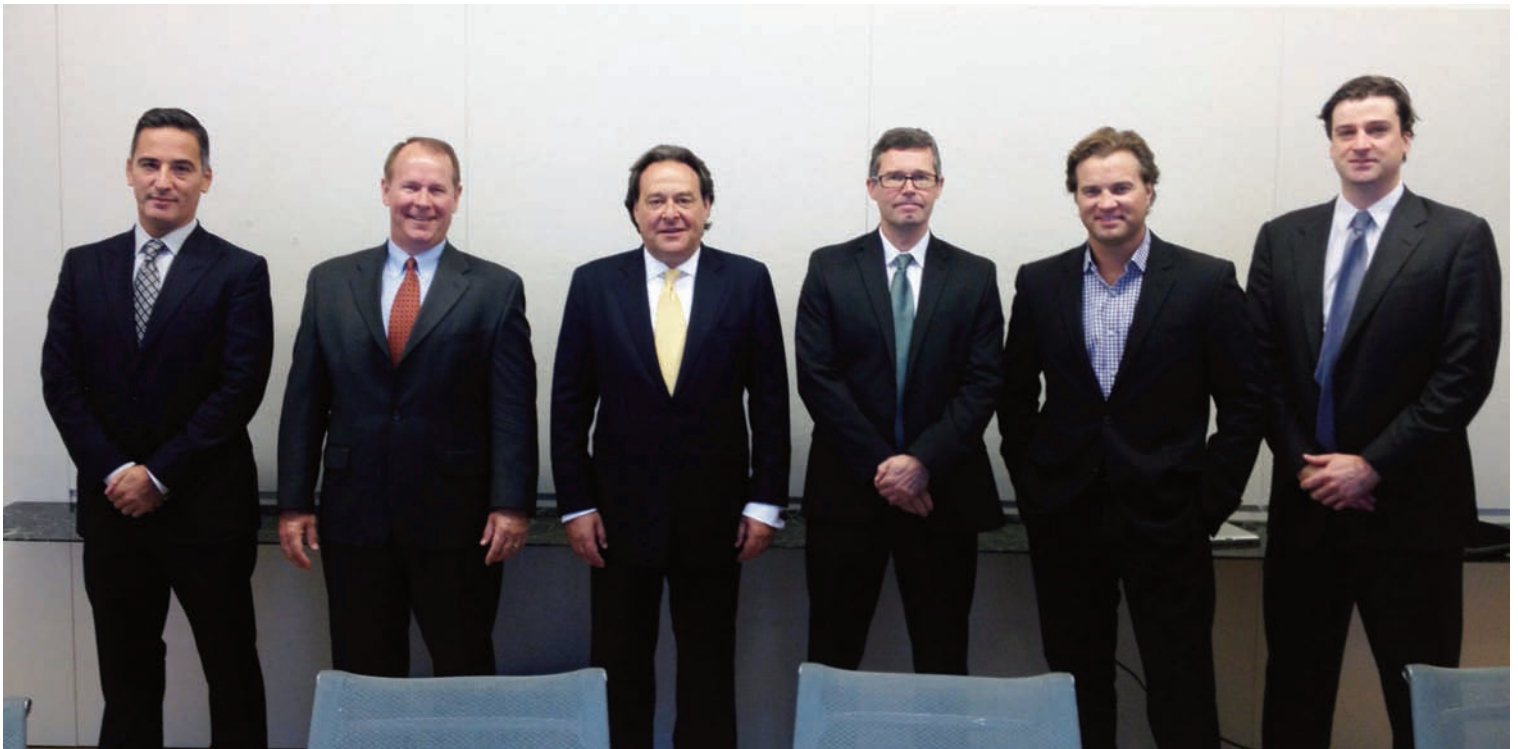
The inaugural Opalesque Hard Assets Roundtable was sponsored by Stephen Silver Fine Jewelry and Eurex and took place in the Chicago office of Cortland Fund Services with:

1. **Chad Burlet, Principal and Chief Trading Officer, Third Street AG Investments**
2. **Paul Sacks, Co-founder and CIO, Aurum Options Strategies**
3. **Axel Vischer, Product Research and Development, Eurex**
4. **Stephen Silver, Founder, S.H. Silver Company and Stephen Silver Fine Jewelry**
5. **Tim Pickering, Founder and CIO, Auspice Capital Advisors**

Enjoy!

Matthias Knab
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Participant Profiles



(LEFT TO RIGHT)

Paul Sacks, Chad Burlet, Stephen Silver, Axel Vischer, Tim Pickering, Greg de Spoelberch



STEPHEN SILVER

FINE JEWELRY

THE RESPECTED SOURCE FOR INVESTMENT
GRADE DIAMONDS, COLORED GEMSTONES & RARE JEWELRY

- Founded in 1980, Stephen Silver Fine Jewelry has been successfully advising high net worth individuals in diamonds, colored gemstones and rare jewelry as hard assets for more than 30 years.
- The company's worldwide client base currently includes venture capitalists, technology executives and Silicon Valley's distinguished residents.
- The depth of resources at Stephen Silver Fine Jewelry allows the company to readily source investment grade diamonds, colored gemstones and rare jewelry.

For more information please contact us at: info@shsilver.com or 650.325.9500

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Introduction

Chad Burlet

Third Street AG Investments

I am Chad Burlet from Third Street AG Investments. We are a fundamental, discretionary agricultural CTA.

Paul Sacks

Aurum Options Strategies LLC

My name is Paul Sacks. I am co-founder and CIO of Aurum Options Strategies LLC, a New York based precious metals CTA/CPO. We offer an option-based discretionary strategy that seeks to maintain upside exposure to gold prices while attempting to drastically limit downside during corrective periods. The strategy offers diversification of gold exposure by emphasizing efficient leverage and capital preservation. It represents an attractive alternative for the passive long gold investor.

Axel Vischer

Eurex Group

My name is Axel Vischer. I am with Eurex Product Development and responsible for product and market development in the U.S., Canada and Latin America.

Eurex Group is one of the world's leading derivatives exchange operators, offering a broad range of international benchmark products, including the most liquid fixed income and equity index markets in the world. With market participants connected from 700 locations worldwide, trading volume on the Eurex Exchange exceeds 1.5 billion contracts a year.

In this Roundtable my focus will be on agriculture and real estate.

Stephen Silver

S.H. Silver Company and Stephen Silver Fine Jewelry

I am Stephen Silver and I will be talking about diamonds, colored gemstones, antique jewelry and strategies in that arena. I own S.H. Silver Company and Stephen Silver Fine Jewelry.

Tim Pickering

Auspice Capital Advisors

My name is Tim Pickering. I am the Founder and CIO of Auspice Capital Advisors. We are a CTA out of Calgary, Canada. Auspice has launched products from commodity and CTA ETFs, mutual funds, 40 Acts, right down to the classic CTA funds. We have been an innovator in the space, and were the first CTA to launch an ETF in 2008.

Eurex. An Exchange for the better.

When you're on Eurex Exchange, you're in a one-stop-shop with more than 2,000 products to trade.

Here you'll find one of the world's most active markets in euro-based fixed income and equity index derivatives, including sector derivatives. Plus a broad offering in single equity products.

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Discover more on Eurex Exchange.

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Tim Pickering: First of all, we trade everything, not just commodities. In our CTA programs, we are tilted commodity versus some of the big names out there that may have them as only a small portion of their portfolio, often less than 10-20%.

We run 50-60% commodity exposure, which ranges from our flagship fund program (Auspice Diversified) right through to the index strategies that we offer for the Direxion funds in the US, and the Horizons ETFs in Canada that we support.

My background was in trading commodities, originally for TD Bank. Then I was the head trader for Shell, so this explains our focus. Why do we trade commodities? Because we see the asset class as a great opportunity. We believe that if you want to trade, you want to trade something that moves. If you are disciplined at risk management then commodities are a great place to be, and of course there are also the diversification benefits which we all know about.

Where we stand out is through our capability to build custom commodity products. This can be with a CTA tilted product, or is exemplified by our launch of the first physical Natural Gas ETF in the world, which led us into the indexing and ETFs in general. Everything we do has a commodity tilt to it.

In general, our strategies are trend following. People might say that's been a tough place to be lately, but trend following is a human, innate thing. We follow trends in fashion, music, and historically, in animal migration. It's not going away, and it's not going away in the financial markets. There are going to be periods of time when trend following isn't the most appropriate as a strategy, but that's why we create a suite of products and that's why our business is based across a suite of things.



Chad Burlet: As a fundamental discretionary agricultural program, we keep our focus very narrow. We concentrate on corn, wheat, and soybeans. We monitor worldwide production, worldwide grain flows, worldwide consumption, and we identify dislocations, mispricings that inevitably occur on a global scale that cannot be sustained over time. From those we identify trading opportunities. We use exchange listed futures and options to execute those strategies.



The primary source of Alpha in our sector is found in spreads and in options. Spreads can be inter-commodity spreads, intra-commodity spreads, like calendar spreads, or inter-exchange spreads; like Kansas City Wheat versus Chicago, or Chicago vs. Minneapolis. Options are a good fit for our fundamental approach because of their longer time horizon. Some of the random noise that occurs in flat price trading is also less of an issue in options.

Paul Sacks: At Aurum Options Strategies we offer a unique industry focused, sector specific gold diversification vehicle.

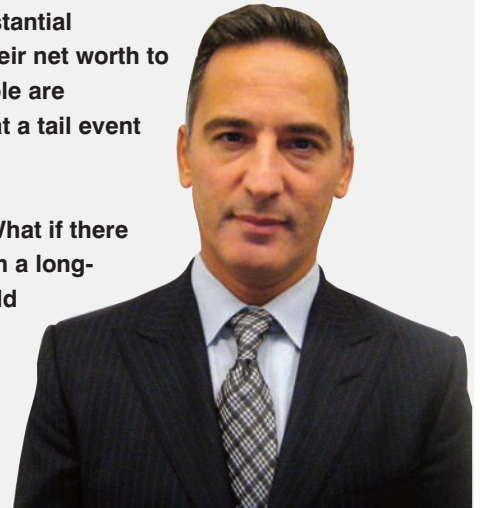
Many are receptive to the idea of investing in gold in order to hedge against various types of uncertainties, including

financial crises, unintended consequences of QE, fiat currency risk, or purchasing power, among others. For many investors, gold is basically an insurance play.

We posit that passive long exposure to the market, be it in bullion or through an ETF, will likely fail to deliver the returns that investors are looking for -- fail to deliver the insurance like payoff. It's true, gold may rally 25%, it may double or triple in the event of a crisis, or it may actually go down if entities have to sell gold to meet margin calls elsewhere. That's why our strategy really focuses on two things: tail risk and capital preservation.

Should there be some type of revaluation scenario for gold resulting from a substantial decrease in value of the USD, those who have allocated a small percentage of their net worth to gold will be looking for it to provide a big return. This is something we find people are interested in. Not for a 25% gain or a 50% gain, but a 10x or 25x gain. That's what a tail event calls for.

Equally important is prioritizing capital preservation. What if nothing happens? What if there isn't a need for an insurance payout? What if gold just goes sideways down? I am a long-term bull, but it's not hard to make sound arguments for a substantially lower gold price. Therefore, we use the options marketplace to specifically construct a strategy that is flat or short premium. This means you are really not at risk of losing a substantial sum should nothing severe happen in the marketplace. We feel this is a unique approach for someone who wants to expose themselves to the gold market, or improve the efficiency of an existing gold investment.



Stephen Silver: Most companies within our industry that focus on precious gemstones and important jewelry as an investment category are “buy and hold” strategies, primarily for long-term appreciation.

Our company's methodology is different. The science of our product as well as the macro and micro markets within our industry is studied and analyzed constantly so we can take advantage of an ever-changing marketplace. We invest time and money evaluating the fundamentals of the diamond, colored gemstone, fine jewelry and antiquities markets, including establishing sound entry and exit strategies for each category. This is a key differentiator as a lot of people who promote this sector as an investment often fail to establish sound analytics addressing short or long-term strategies. Additionally, we have a transparent fee structure, unique to our industry that is much less egregious than what is commonly seen within our industry.

We have a strong base of sophisticated investors who are interested in various kinds of alternative investment strategies. Much of their interest in our category is focused on the preservation of multigenerational wealth and the challenges of passing assets on to future generations.

A major reason we are participating in this roundtable is because we have recently experienced dramatic increases in activity amongst active and prospective collectors and investors. We are now examining and considering launching some form of a hybrid fund. This idea of a fund is something that has not been seen very often in our sector and certainly not within our category of alternative investments.

Those are some of the elements that differentiate us. Our strategies are very, very different. The success of some of these strategies has led us to closely consider developing some type of hybrid equity fund in the future.



Axel Vischer: Eurex Exchange provides exchange-listed derivatives contracts that allow investors to get new forms of exposure to certain assets. For example, we offer property futures based on commercial real estate indexes. The main index family Eurex Exchange uses at the moment is from Investment Property Databank, now a subsidiary of MSCI Inc. The focus is on commercial real estate with the exception of a very small portion of “specialized residential funds”. Looking at the UK, the invested market reflected in the UK Annual All Property Index covers approximately £ 14bn, which represents roughly 53% of the total direct commercial property market.

Our IPD Futures have a notional of £ 50,000 and five consecutive annual maturities, each covering the total return (capital gain and income return) of the corresponding index in one calendar year.

Another example is one of our products in our small but growing agricultural segment, namely our futures contracts on European Processing Potatoes. The futures are cash settled with the underlying index representing the spot market price for potatoes in Germany, France, Belgium and The Netherlands. It is predominantly used by the French fries industry. In contrast to the U.S. where most potatoes planted have their prices fixed before they are planted, in Europe a significant part of the crop has no pre-negotiated prices and is therefore more volatile.

Our potatoes futures have a contract size of 25 tonnes and follow an April, June and November maturity cycle reflecting the potatoes marketing season.



Greg de Spoelberch

What is your market doing right now and where are you finding opportunities and generating alpha? What trends are happening in your market right now?

Tim Pickering: We are a systematic nondiscretionary trader. We took discretionary approaches that work, and applied discipline along with a repetitious process around it. I come from a farming family that farmed in Saskatchewan for 100 plus years. I stepped into that space about seven years ago, built up a corporate farm and have since sold it, so I understand the fundamentals of the grain and commodity markets and what’s driving them.

In Calgary, where I live, I see the facts. The Chinese have been buying up the oil play in Canada. They would buy the whole thing if our government would let it happen, but that doesn’t change my focus regarding my investments. I don’t know where the opportunity is going to come, when it’s going to come, so to me it’s participating in the grain market, participating in the metals market, participating in the energies market in a disciplined and ongoing way, because I don’t know from which sector the opportunity is going to come from.

There is no doubt China is changing things. The demand is there, but it goes up and down, and is hard to gauge. That fluctuation in commodities demand is not going to change anything anytime soon, so we take advantage of that in our commodities-tilted CTA and across all programs that we supply. I don’t think these dynamics are going to change; it’s just how you participate in those markets.

For example, some pension clients have come to us looking for long commodity exposure. We are not interested in providing such clients a simple long GSCI “bury your head in the sand” type vehicle, but have come up with some long flat tactical approaches that approach the market from a more trading-oriented, discretionary perspective.



Chad Burlet: One reason people have interest in Third Street is that while food is a central human need, people have a difficult time figuring out how to actually participate in the agricultural space. Agricultural land can be a difficult asset class to manage and is not very transparent or liquid. Agriculturally focused businesses have underperformed the major stock market indexes, especially this year. Long-only funds or ETFs struggle over time because the products are mean reverting in terms of the price. So it's becoming clear that you need to actively manage and analyze a market to have favorable returns over time.

The markets are dynamic; they are changing every minute. The core fundamentals that drive the market are production, transportation, and consumption. As you see trades unfolding on a daily basis, it's clear that there are high-priced and low-priced markets around the world. The U.S. remains central to the world pricing mechanism of corn, wheat, and soybeans and this is where a majority of the futures contracts reside. As participants enter or exit a market they do so in an uneven fashion. In doing so, they can force one market to be severely mispriced relative to another. Wheat, historically and for other physical and fundamental reasons, has a greater value than corn, but it will occasionally trade at a discount to corn. That relationship is one that will correct over time. That's a trade that we have participated in over the years, buying wheat when it is well priced to corn.

Another relationship we watch actively, and one which has triggers on both the supply side and the demand side, is corn versus soybeans. On the production side they compete for the same acreage, and on the consumption side their by-products are both key ingredients in animal feed. As their price relationship shifts, both production patterns and consumption patterns change. When one gets historically cheap, for various short-term reasons, it presents us with an excellent trading opportunity.



Greg de Spoelberch

Axel, Eurex is offering agricultural and real estate products. What developments and trends do you see from your side?

Axel Vischer: Let me get back to the family farm in Saskatchewan first. This is a very good example to address, because this family farm is basically integrated into the North American and the global market. We have a totally different situation, where we are coming from. Until a few years ago the European agricultural markets were rather self-focused. Many products were subsidized and the market was not liberalized. It has only been a few years that these markets have started to become less driven by political intervention.



For us as an exchange, that means that we need to develop products from the ground-up in a totally new market, while all the other markets, like here in the U.S., are already a part of the global markets. This means we are helping the European industry – our underlying market – from farmers to food producers here, to manage their price risks as part of global agricultural markets.

In terms of alpha, potatoes, like corn or soy, are very sensitive to the weather, including temperature levels, amount of sunshine and rain. July and August are the crucial months during the growing season. During the recent growing season we were faced with extreme weather conditions for some of the growing areas, resulting in increased market volatility due to differing opinions on what the quality and quantity of the harvest would be.

Property prices are influenced by many factors as well: investor demand, structural supply, demographics, yield curve dynamics, monetary and fiscal

policy, national or supra-national regulations on property investments, subsidies, tax reliefs, government schemes, financial regulation (e.g. mortgages accepted as collateral). Futures pricing also is strongly influenced by liquidity. There is a tendency to find more natural longs, more buyers of exposure in the market than sellers. However, nevertheless there are some specialized funds that tend to systematically sell the market

I mentioned the UK All Property Future, which is the complete market, but in addition we offer futures on subsectors of the commercial real estate market. We have seen interest from people in trading the subsectors against the All Property Future. For example, you trade offices in the West End, or the London City, or Shopping Centers, or Retails Warehouses against the whole UK commercial market. These subsectors provide great opportunities for dynamic strategies like that.

Stephen Silver: I will address your question regarding alpha from 100,000 feet and work down. We have three different sectors within our industry that trade their goods creating what the world perceives as the jewelry trade: loose diamonds, loose colored stones, and jewelry fabrication. What investors must understand is that 99% of what I just described has nothing to do with investment. It's purely adornment.

Our alpha comes from understanding the mining of rough stones (uncut gems), as well as cutting and re-cutting a variety of gemstones. It also comes from understanding the unique intricacies of how to evaluate important estate, antique and modern jewelry.

There is a very small selection of rare product within our industry that qualifies for investment. If the initial purchase of that rarity is handled properly and strategically, the probability is that it will act as an investment and produce a strong ROI upon exit, within a reasonable period of time. This is where we fully differentiate ourselves from others and create opportunity for our collectors and investors.

Our alpha within this category is realized when we purchase something of extreme rarity by either recognizing value that others miss or, in an effort to create more value, buy with the intent to apply our company's intellectual property by recutting or refabricating. This strategy applies when we acquire highly important second hand inventory as well.

When we are presented with an opportunity to acquire a rare and important piece, we critically analyze current and past market conditions and apply those findings to that piece. Once we have performed a full analysis, we then establish a sound strategy for both the initial purchase and eventual exit.

An example of creating alpha for our collectors and investors occurred in 1999-2000. We bought an intense blue diamond slightly under 7cts with the sole intention of successfully recutting the diamond, keeping it above 6cts and deepening the depth of color in the face up position to achieve the rarest grade called "vivid blue". This category of "vivid blue" is exponentially rarer than the category of "intense blue". We executed, and it took us from a \$3m purchase to a value of approximately \$5m. The process took 90 days from the point of purchase. These are the kinds of things that can happen within our category. What we do is very unique, and very few companies within our industry have the capabilities to execute as I just described.

Addressing your question regarding emerging markets, recently (the last five to ten years) the Chinese, Eastern European, Russian, and Middle Eastern markets have driven a lot of the activity in the investment category of gemstones and jewelry. The large and rare diamonds that are fetching high premiums at auction are really being driven by the demand of the wealthy and ultra-wealthy in these markets. Much of this demand is generated by their desire to diversify and move into investments that are either more transportable and/or in line with their cultural traditions of strategically collecting rare gems.



One of the advantages we offer our investors is that we take the time to educate them about the trends and fundamentals of strategic collecting. For example, the sharp appreciation in prices for larger white diamonds has created what we believe to be an overbought market. Investors interested in our area have to be very careful about trends like this. This is a marketplace just like any other that moves up and down, influenced by fundamentals like supply and demand, politics, and world economic pressure.

Greg de Spoelberch

How does the commodity price affect your business from the alpha perspective?

Stephen Silver

Not very much. It becomes a natural hedge for us as long as we are consistently purchasing the same amount of precious metals on a daily basis.

Our exposure is that we are required by law to hold all secondhand purchases for 30 days. As a result we are exposed to the volatility in the metals markets until we are free to sell on the 31st day. Because of this 30 day hold we further protect our long position by purchasing metals at a discount of their spot value.

Paul Sacks

At the time of this Roundtable, Gold is approximately off \$600 per ounce from its highs in 2011. This year looks to mark gold's first losing year after 12 consecutive annual gains.

Paul Sacks: I would describe 2013 as the year of the massive gold wealth transfer. Many hundreds of tonnes of gold have been liquidated by the West (selling of GLD ETF), while long lines have formed in the East (China, India) to purchase physical gold as the price has fallen. The gold has gone from short term momentum traders to long term investors. Gold plays a critical cultural role in the East, from wedding ceremonies to intergenerational wealth transfers. They are not buying this gold just to sell it next month if the price rallies \$50 per ounce. It is familial tradition and cultural practice in the East vs. hedge fund managers in the West.

Regarding how the global environment impacts my strategy, we closely follow all developments from around the world, with special attention devoted to the happenings in China and India. It depends on how one values the information that comes out of China, but a hard landing there certainly would have a detrimental effect to the entire commodity complex. India also regularly alters gold import tariffs in an attempt to address its current account deficit. Of course any alterations to QE would have dramatic effects.



At my firm, we are most concerned with the role gold plays in a portfolio over the long term; maximizing that benefit more so than short term trading profits. Our approach to addressing these types of risks is in how we create asymmetric risk opportunities in our core positions.

When you say to an investor, "You are allocating 5% of your portfolio to gold, what does the world look like if gold is trading at \$3,000 an ounce? Are you protected? How is the other 95% of your portfolio faring?" When you point that out, people become very interested in other options.

If you are in gold, it can be hard to keep your chip on the table permanently; investors can be get chopped to bits, stopped out constantly. They are at the mercy of trading algorithms and many other external factors. That leads investors to consider how they might be able to avoid the risk of stop loss and have leveraged exposure to the upside.

On the topic of market change, the impact of electronic trading cannot be

overstated. The trading and landscape of investing in gold has evolved dramatically. It was a very different game as recently as 10 years ago. The listing of the GLD certainly had its effect. Then, more importantly, when the GLD listed options in 2008, trading desks started a professional arbitrage between options on the GLD and options on the NYMEX, which is where I trade.

Now we have an electronic environment where bid-ask spreads are very tight and liquidity is very robust. I would argue there is more liquidity than there should be based on the risk. In other words, at the core of this arbitrage are two instruments that vary in a very significant manner, deliverability. On the NYMEX you can take delivery of the gold. The GLD does not offer this. To me, that makes these products different. There is a potential problem there, but I am happy to take advantage of the liquidity that this arbitrage is providing.

In my opinion, the time is now for intelligent market taking instead of market making, so you can really take advantage of the big picture and make sure you are positioned correctly for when the correlations break down, if they do.

Additionally, in terms of alpha, to my knowledge there are a few unique things about the floor. When I say floor I mean not only the physical location, but the electronic marketplace that exists now and will continue to exist, even if the physical floor shuts down. You have real access to information like what bank has what position on, what broker is executing, on behalf of whom? At our firm, we refer to that as accurate transactional value ascription. Who is doing what and why? It's very important, and it helps inform your market opinion.

Paul Sacks

I'd like to Ask Stephen something. Of course the gold ETF has had a huge impact on my business, and I remember reading a year or two ago about the possibility of a diamond ETF, but I am not sure whether they created it or not. Was this ever created?

Stephen Silver

Not yet.

Stephen Silver: The idea of a diamond ETF is one that we looked at four or five years ago. We didn't do it, and we didn't even attempt to do it because at the time I believed the diamond market would have had a couple of fundamental problems launching a successful ETF. One of the biggest challenges was liquidity. That challenge is still present today. There are too few large cap publicly traded companies within our category to create enough liquidity. I perceive this to be a big hurdle, possibly insurmountable.

In addition, if you are going to construct a diamond ETF to be like a gold ETF, standardization issues are still a major hurdle. However, there are a few patents pending that attempt to address this issue. We'll see how that develops.

The other fundamental problem with a diamond ETF is that 85% of our supply chain comes from one source. This may present the perception of a big risk, maybe so much so that a diamond ETF can't be formed. However, from my perspective I don't believe this is much risk because De Beers has managed the monopoly of our supply extremely effectively, efficiently, and fairly for a very long time, which gives me a sense of confidence should they choose to get involved.



Paul Sacks

De Beers has what amounts to basically a strategic reserve, do they not?



Stephen Silver: Rumor has it, they do. They have never publicized how much is held in the strategic reserve, but I have heard that De Beers' strategic diamond reserve could be as much as a 100 year stockpile at the rate we consume today.

Stephen Silver

To summarize my discussion of a possible diamond ETF, it is interesting and I would be interested but only after some of these key issues have clearly been addressed.

Greg de Spoelberch

Let's look at the current public policies, how do government and central bank policies affect you?

Tim Pickering: That touches our business in a number of capacities. If I talk about the beta-based ETFs we did, position limits are obviously a big deal. When we launched a physical ETF on natural gas in Canada, we had a regulatory issue to deal with.

As a commodity trader in general, at our current size it's not hugely significant for us. When I traded for Shell, or you are running at a Winton-like size, it is a big concern because it makes a huge difference in terms of the positions you can hold in your fund.

Again, a large part of our business is taking certain strategies and creating investment products with them, whether it's an index, a 40 Act mutual fund, an ETF, a UCITS product; all of a sudden we are getting regulatory changes that also affect the client who is buying the product. So at all levels new regulations affect our business, whether it's the beta side of our business, the position side of our core alpha business, or for the client. Regulation is everything today - when I stepped out of Shell to start this business seven years ago, I wouldn't have guessed regulation would be such a big deal, but it is, and it's not going away.

I don't know if it helps or it hinders when you hear for example some of the biggest players out there saying derivatives are a bad thing, but at the same time it's a fact that their business wouldn't exist without derivatives. Things like that aren't helping the situation.



Stephen Silver

How much do regulations affect the cost of operating business and the development of new products?

Tim Pickering: Cost-wise, the impact of regulations on the whole product creation process is very significant. One of the reasons why we at Auspice did not chose to launch our own ETFs and our own 40 Act funds was because the cost was prohibitive for a startup company. We chose to first partner with Claymore ETFs, then Direxion Funds in the U.S., and even BlackRock for a period, because they do that heavy lifting and are more efficient at it. Product creation is very expensive, and of course a layer of that gets embedded into the product.

If you are trying to launch an ETF with a very efficient cost, that becomes a dilemma. Then, if you have got ongoing layers of transaction costs like swaps underlying your product, or if you turn one type of product into another, or have to get rid of some tax problem, or create certain efficiencies, that adds cost as well. At every level, these layers are all additive to the cost of the product for us to run our business, and in the end also for the client.



Stephen Silver

There is no barrier to entry in our industry because there is not a formal licensing requirement. Although irresponsible behavior is limited to a very small percentage of industry participants, it does create a negative public perception of our industry when exposed. I believe that if there was a

licensing requirement, we would eliminate a lot of these bad apples and set a better professional standard.

One example which is strictly regulated and monitored is the precious metals we use to manufacture. In our country the government agency that oversees this is The Department of Weights and Measures.

Another example of a global regulation that has had a positive effect is the “Kimberly Process”. This addressed the blood diamond issue by enforcing accountability from the source of rough diamonds. We now track rough diamond from the source to the manufacturer.

Chad Burlet: We view the regulatory environment on a global basis and we have seen some very positive trends. Key countries have gone from what we call a single desk or government controlled environment to a free market environment. Axel mentioned how this has occurred over the last decade in Europe. We have also witnessed it in Canada, and in Australia. To those of us who appreciate unfettered and competitive free world trade, there has certainly been a great deal of positive change in the global trading environment.

The other place where we see the importance of government policy is in the area of renewable fuels. In the U.S. we know it as ethanol and biodiesel, in Brazil it is biodiesel, and in Southeast Asia they are burning palm oil. That is a key factor on the demand side of the grain sector around the world. In our opinion the renewable fuels craze has peaked and it will flat line for a while. Eventually it will go into decline because it's a flawed policy.

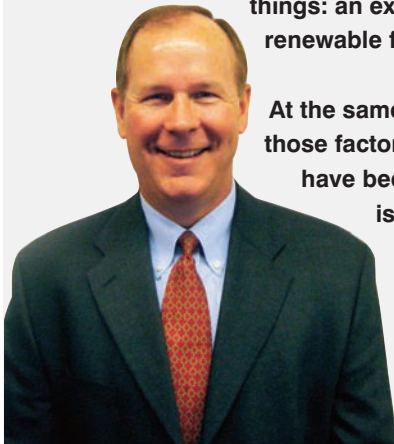
Another regulatory change that we've seen in the past 15 years has been the significant increases in speculative position limits at the exchanges as agricultural commodities have become securitized. In general we find ourselves in a rather favorable regulatory environment both domestically and internationally.



Greg de Spoelberch

Can you give some insight into emerging markets and the steep rise of the demand curves in the sectors you cover?

Chad Burlet: For a long period of time the agricultural world experienced steady growth on both the production side and the demand side. There were a few bumps along the way caused by crop problems or bad farm policy. About five years ago we had what we call the hockey stick, a steep acceleration on the demand side, which was caused by two things: an explosion in the size of the middle class in India and China, and the explosive growth of renewable fuels.



At the same time we experienced several production difficulties around the world. Because of those factors we had a paradigm shift in prices. For the past five years corn and soybean prices have been 55% and 65%, respectively, higher than they were the previous five years. The world is now responding with greater productivity, additional land brought into production, better seed technology, and investments in infrastructure. We are now going to see the other side of the equation. The cure for high prices is high prices and the world is very awkwardly working towards unraveling some of what it has done in the last five years. We are going to experience a painful transition from pricing land into production to pricing land out of production.

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Axel Vischer: I'd love to come back to the buzz words of position limits and regulation. Trading at Eurex Exchange takes place under the rules and regulations of the Exchange, which in turn is regulated by BaFin on a national level in Germany. There are no explicit limitations – IPD property futures as well as our Potato Futures can even be traded from terminals located in the U.S. and the CFTC no-action relief.

The upcoming regulatory framework, be it Dodd-Frank, EMIR or MIFID2, certainly impacts our market. It is difficult at the current point in time to give a clear outline of potential changes, but one example of a possible negative impact could be potential position limits for financial investors trading in commodity futures.

Chad mentioned the recent price fluctuations. From an exchange perspective I see those very clearly. In the last couple of years there were enormous fluctuations in the prices of the various products we have listed.



Tim Pickering: One of the arguments I have heard in Europe is that one of the reasons they are trying to restrict commodity investment through CTAs and other traders is protection of the prices of those commodities to the ultimate end customer or consumer of those products.

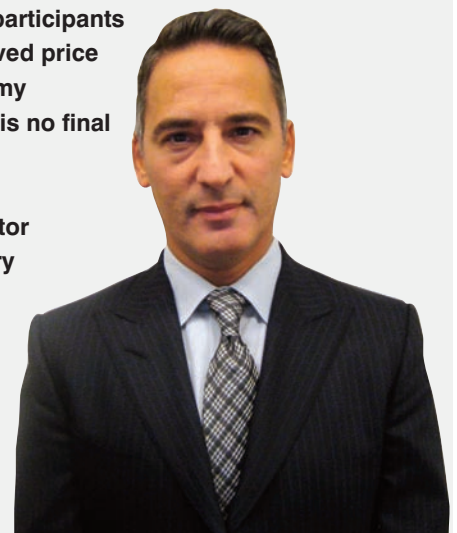
Yet, study after study has shown that whether it's ETFs or other products they are not explicitly distorting the price of the underlying commodities. A lot of academic and commercial work has been done in that regard, yet still in Europe and in other regions as well we are harping on this restriction to allow access for the consumer to invest in commodity products. Where does this end? It seems wrong, and the wrong thing or trend just seems to be getting worse. I would like to see a more clear path there.



Paul Sacks: As far as public policies, Dodd-Frank and other regulations have forced investment banks to disseminate or spinoff their trading operations. This disruption to the trading infrastructure and markets has affected trading volumes, and indirectly affected the exchanges ability to act as a mechanism for price discovery.

Ultimately, I am in favor of everything coming to the exchange level where market participants can see who is doing what. This allows for an increase in transparency and improved price discovery. This benefits all involved, especially the customer. The danger lies, in my opinion, in the OTC universe where all are exposed to counterparty risk, and there is no final guarantor of the transaction.

As far as central bank policies – of course they play a critical role in how any investor approaches the gold market. We are in uncharted territory with respect to monetary policy in the U.S., and abroad. The Federal Reserve is currently purchasing \$85bn worth of U.S. Treasury and mortgage-backed securities each month. When will they start to taper? The size of the Fed's balance sheet is in the trillions, and continuing to grow rapidly. Central banks around the world are buying gold en masse as a way to 'own a few less dollars'. It's a way for them to start to mitigate the risk of the U.S. debt they own.



Axel Vischer: OTC versus on exchange is a very big topic. Like the other issues we discussed, this one is currently in flux because regulators are changing the situation both here and in Europe with Dodd-Frank and EMIR. The final result and how the market will evolve is very hard to predict.



There are markets in which almost a complete move from off-exchange to on-exchange took place, like the energy market in the U.S. where all the swaps were moved into exchange-trading and clearing. In Europe the shift was less pronounced, but still a significant part has become on-exchange. Another good example of the transition is the case of dividend derivatives. Within a few years, we were able to capture around 50% what was previously a purely swap market. The whole market is now much bigger than when it was OTC only.

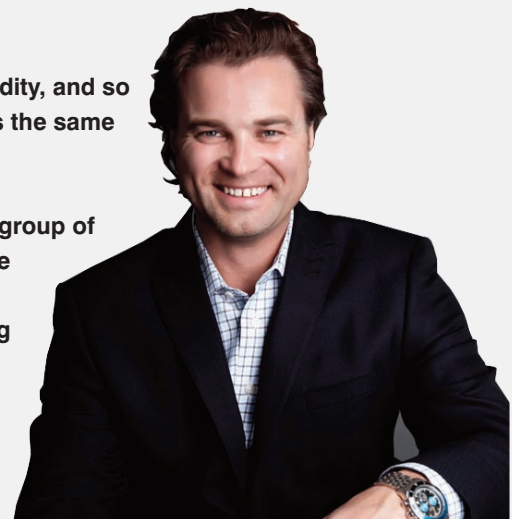
On the other hand, there are examples, like certain physically settled commodities, where the vast majority are still bilateral. It could very well be that these takes some time to migrate to clearing houses, but we are closely involved in the process.

Tim Pickering: I wanted to comment on overregulation. I don't think we are overregulated, but I do see an issue with all the different jurisdictions affecting each other, or what's also called extra territorial regulation. Everybody, or every regulatory body, has a different thesis or a different driver. Here it is the CFTC versus the SEC versus the NFA getting involved from that standpoint; then dealing with regulation in the multiple provinces in Canada, then going to Europe you also deal with multiple versions of the same framework in multiple countries – these things are a huge problem.

When standardization does not even exist within countries, how can you create a product that crosses borders? If we didn't partner with firms in Canada, the U.S., and Europe, it would not be possible.

Paul correctly pointed to the all the people spinning out of bank prop trading operations. These prop operations were important in terms of discovery, liquidity, and so on, and the question now is when people spin out and start their own firms, is the same level of liquidity going to come into the market?

In my opinion, the answer to that is no, because why would we believe that a group of prop traders from banks can spin out and launch their own businesses and be as good at running businesses as their institution used to be? It's a quantum leap from being a prop trader at Goldman and setting up on your own, fighting to survive. I don't believe that trader will add the same level of liquidity to the market. So by definition, markets are going to fragment and volumes inevitably drop off, and I think that's an unwanted effect that probably the people that created those rules don't care about, but it's happening.



Greg de Spoelberch

Tell me more about the investors in your funds. Let's maybe start with Stephen, because your product is extremely rare and idiosyncratic, something our readers probably have not seen very often.

Stephen Silver: The common thread is a desire to diversify their core investments with the addition of tangible assets. The prospective investor is the high net worth or ultra high net worth individual. Our typical investor is one who looks at our category as an opportunity to diversify an investment strategy and to continue to accumulate and/or preserve multigenerational wealth. To satisfy those needs we look at each investor independently, focusing to create a game plan or strategy within our category for them.

For example, one investor's interest at an older age was not to invest for his own benefit, but to apply an overall strategy for the benefit of his kids or grandchildren. His position was that he didn't care about what short-term markets looked like. His was a very long term perspective.

In accordance with his wishes we have bought some very rare and important items. As with all of our investment recommendations, a lot of time was spent on coming up with a strategic plan detailing the deployment of the capital.

For this investor a very unique item was bought: a very important Art Deco Cartier Mystery Clock. For him we were buying into a unique subcategory of the market to satisfy his investment perspective which was very broad, very deep and very, very long-term.

Then of course we have the investor who is looking for returns that are strategically placed over a shorter period of time. We look at different ways of analyzing his/her needs, but again we are dealing with an investor relationship that is extremely high net worth. Usually these investments are more long-term than short-term, with a strong interest in hedging and creating investment strategies within our category that are rather uncorrelated.

Many times these investments also become emotional. My sector is an exciting area to participate in; it's beautiful, interesting, and in a lot of cases it's wearable art. This makes the investment also enjoyable for the investor's wives or children. The attitude is often similar to that of an investor in fine art.

In fact, the *Capgemini-Merrill Lynch World Wealth Report* recently found that our category was the second most attractive category within "investments of passion". It is right there next to fine art. So again, there has been a noticeable attitude shift over the course of the last 10 years, whereas our sector wouldn't have been considered as an investment strategy in the past.



Stephen Silver

A lot of the improvements have to do with how we define our product today, which is much different than how we and our industry defined our product in the past. The grading systems have become far more acute and easier to understand. Therefore, it is much easier for us to make statements about the product because of this dependable third party verification.

Greg de Spoelberch

Paul, tell me more about what kind of investor is looking at gold? What behavioral elements are involved with investing into gold, and what they are looking for?

Paul Sacks: Our investors to date have been high net-worth individuals. They allocate a small portion of their portfolio to gold because they understand the value of an uncorrelated asset. For them it's not get rich, it's stay rich. They understand the importance of true preservation of purchasing power.

With that in mind, we talk to them about the role derivatives can play. Derivatives get a lot of bad press but are unmatched in their ability to deliver efficient leverage and diversification. The very wealthy are starting to be concerned with the recent volatility in bonds, rates increasing, and the effects of tapering QE; how that will affect a

large part of their portfolio, which of course resides in bonds.

Most of these peoples' lives won't be adversely affected if gold falls to a price of \$800 per ounce or lower, but they know what role they want gold to play should it trade at \$2,000 or \$3,000 an ounce. Furthermore, they realize that the physical bullion and GLD that they have might not be a vehicle that can deliver what they are looking for.

They see that the price of gold might be a lot higher in the future, but it might not get there in a linear fashion. There might be some normal volatility, up and down, then one day we are just going to wake up to find that there's a totally different handle on the price. Those investors want to make sure that their chip is on the table.

If you take a look at the U.S.'s balance sheet, it's not impossible to imagine the USD coming under pressure in the future. It wouldn't take much. Market perceptions change, the velocity of money picks up; out of nowhere inflation starts to appear. China sells some US debt. Bonds fall. Rates rise more. One or two credit ratings agencies downgrade the U.S. The USD starts to lose its international reserve currency status, and every foreign government looks to mitigate its USD risk by buying gold, as much as possible, as fast as possible. By most measures, it's improbable that all these events occur; improbable, but not impossible. But what if one or two occur, and of course there are many others not listed here. An investor seeks gold exposure not because he is sure these events will unfold, but because he understands that they might. An options based strategy devoted to big beta leveraged upside exposure can deliver returns that correspond to such a market scenario. A tail risk event calls for a tail risk payout. A professionally managed options position can strive to deliver this asymmetric return, while mitigating downside risk should the price of gold continue its decline.



Stephen Silver: When it comes to our investors, we find that we ourselves have very similar attitudes. One of the areas mentioned earlier that I didn't come back to yet are the benefits of donations. This is a very real and proven vehicle that high net worth individuals can use to create great financial rewards.

I will use my own experience as an example. In 1993 I was fortunate enough to purchase the Cullinan Blue Diamond Necklace, which is a very rare, historical piece of artwork. I was lucky enough to be the first owner of this piece outside of the Cullinan Family. The piece was made when Thomas Cullinan, the owner of the Premier Diamond Mine, created the necklace for his wife when they were knighted by King Edward for gifting him the great Cullinan Diamond. That diamond was subsequently cut into the Crown Jewels of England. Needless to say, this is a tremendously historical and important piece.



I toured this necklace, lending it to major museums around the world for the better part of 25 years. This created a wonderful provenance for the piece. In 2008, I decided to donate the necklace to the Smithsonian National Museum of Natural History, so that it could become a part of our National Gem Collection. Today this piece sits next to the Hope Diamond in the Winston Gallery.

There was a tax benefit that I received for the donation. Needless to say, the donation acted as probably one of the best ROIs that I ever realized.

That donation reflects what I have done on multiple occasions with various different nonprofits. It is a reliable, legal, and attainable way of converting an acquisition to a sale, as it affects your income tax.

Tim Pickering: I set up my company because I believe that alternative, non-correlated investments are going to become the core of peoples' portfolios. That goes from institutions to retail investors, no matter the size or sophistication. That for me is the trend that's happening. It takes time, but I believe it's shifting this way.

I wanted to create a product suite that ranged from alpha to beta and had different qualities and characteristics, different transparencies, and different costs, depending on the investor type. We really focused on spanning that range. Clearly, our business is driven by alpha. If you can't put up solid alpha numbers in a year like 2008 for a business like ours, you are not on the map. We definitely have that capability to deliver, but we also need to create the different products that meet different investor needs.

**Tim Pickering**

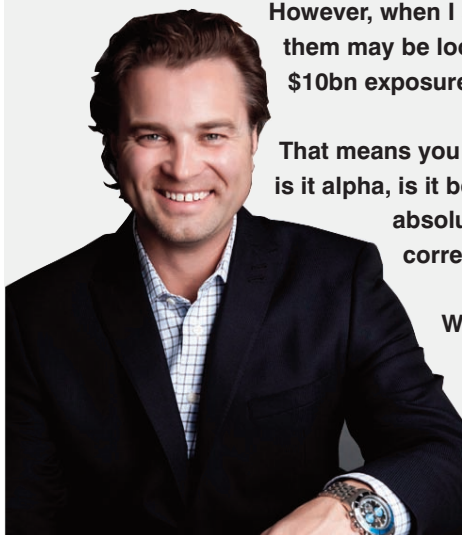
I had already mentioned that there is a commodity tilt in my business, and given my background that will probably always be there, because we believe that if you are disciplined at risk management, commodities is one of the best places to be.

Tim Pickering: There are a lot of sophisticated institutional investors that understand the value of commodities and the various ways of getting exposure, whether it's through synthetic means or by investing in farmland, forests or whatever that may be. Many sophisticated investors do already have such exposure, and there are even more coming up the curve, so we are seeing a whole push from the institutional side looking for products like ours.

However, when I say product, they are not necessarily looking for the best alpha product. Some of them may be looking for a better way to have a tactical long exposure that can to replace their \$10bn exposure they have to GSCI or some other similar kind of exposure.

That means you need to sit down with those institutions and figure out what they are looking for; is it alpha, is it beta or enhanced beta? Or what exposure are they looking to replace? But there is absolutely no doubt that institutions and endowment foundations are tilting non-correlated alternatives.

We work with some institutions that are 50%, 60% in that alternative bucket – that is 50%-60% of the entire asset pool. They are getting far better results, and some of those results have been published and are public. I believe we are just going to see more and more of that. This trend towards non-correlated alternatives will drive the wealth management, RIA space, which will in turn drive the individual investor.



Paul Sacks: I would ask institutional investors to consider their goals and expectations regarding gold exposure. What do they want their gold positions to accomplish within the context of their entire portfolio? If they are invested in bullion, an ETF or futures, does linear P&L exposure accomplish this?

An institutional investor is well aware of the voluminous amount of research in support of the many benefits and advantages of gold investment. We posit efficient leverage and capital preservation can make a good investment better. Passive long exposure to gold has worked very well in the past, but profit taking is difficult to time. A derivative based strategy dedicated to leveraged upside and mitigating risk to the downside, used as an overlay, can produce a more effective overall gold exposure.



Chad Burlet: Our investors represent a good cross-section of the industry. We certainly have high net worth individuals, fund of funds, different trusts and foundations participating. Interestingly enough, we've also found that a lot of experienced traders have interest in participation in the agricultural space, and some of our investors have come from that sector. Even agricultural traders who want to participate in the agricultural sector under a different strategy have invested with us.



The strategy we run is not capital intensive. The margin to equity are very modest, so we afford the investor a good degree of leverage if that is something they are comfortable with and we think is appropriate. Our beta is also very low, so we appeal to a lot of people.

As I mentioned earlier, there are not a lot of good ways to participate in the agricultural sector. There are some trend followers that have not fared well over time. The long-only strategy is flawed, as is the ETF strategy, and they have generated poor results. There is a very small universe of actively managed agricultural CTAs, and that's serving us well.

Greg de Spoelberch

Axel, do you want to add anything as far as your clients?

Axel Vischer

Yes, I would like to skip agriculture because I agree with most of what Chad said. But let me talk a little bit about commercial real estate. It's a very recent product, but the user base has been growing fast.

Axel Vischer: The market for property derivatives is roughly seven years old. Different derivative instruments compete in this space like property swaps, property notes and investment certificates, REITs and structured products on REITs, and property futures. Eurex Exchange launched the IPD futures in 2009, very early in the market life cycle of the property derivatives market. The volumes have constantly developed upwards, especially after the start of the crisis.

At the moment the preferred instrument is still the UK All Property Futures, giving exposure to UK property market returns. Mainly because it is a good means to hedge for example a swaps book, laying off part of that risk, and is preferred by the few banks acting in this space also to hedge other structures they sell such like property notes/certificates. The open interest at Eurex Exchange represents approx. £500m notional. In 2012 more than 50% of property derivative deals based on IPD indexes were traded on-exchange rather than purely OTC.

The open interest as per the end of Q2 2013 was about £400m in notional. That is significant, because from all the open interest outstanding, both on exchange as well as purely OTC, that represents about 30%, so one third is already kind of hedged or traded out on exchange, which is strong and very positive for such a new market.



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