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Macro Strategy & Research

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The Best of the Street

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Although we don't have any shortage of personal opinions, macroeconomic ideas and investment approaches at Orcam, we know that there is no shortage of great minds in the global economy. Our research will occasionally try to provide clients with what we believe are the best recent insights from investors, analysts and pundits who we follow. The Best of the Street reports will offer clients a more well-rounded view of the investment world through a lens that is hopefully different from our own, but still based on the same sort of pragmatic and sound reasoning we attempt to use. Attached are some of our favorite insights from recent weeks.

"The best is the enemy of good."
— Voltaire

David Rosenberg—Gluskin Sheff

"the best advice I can give you is to search for sources of relatively secure income. This can mean select REITs – especially with the US residential rental vacancy rates edging down to a mere 4.6% and rental growth steady at roughly 1% per quarter (as per the latest Reis data). Yields on average have declined to 1.7% but that is still better, more than double, in fact, what you can garner at the mid-part of the Treasury curve. Intermediate Investment Grade bonds too are a happy medium between risky equity markets and safe treasuries – the average fund has generated a return of over 6% so far this year. With speculative grade corporate default rates well below average at around 3%, high yield bonds with an average coupon of over 6% are perfectly reasonable, especially given the strength in corporate balance sheets." - David Rosenberg, 10/4/12

Jeff Saut—Raymond James

"Mark Twain once remarked, "October, this is one of the peculiarly dangerous months to speculate in stocks. The others are July, January, September, April, November, May, March, June, December, August, and February." However, if the typical presidential election year trading pattern continues to play, after a pause/pullback stocks should trade higher (see chart on page 3). And, this week is full of economic reports that could cause a pause/pullback. This week we get the global manufacturing data and the U.S. jobs data. The wildcard, however, is Spain. The bulls are hoping that last week's Spanish budget proposals will pave the way for a bailout request by Mariano Rajoy's government. If so, it would be a step in clearing some of the uncertainty in the euro zone. Whatever the news, I don't think stocks pull back much from here."— Jeff Saut, 10/1/12

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David Kostin, Goldman Sachs

"A look at the 2011 trading pattern of the S&P 500 explains the reason for our belief that the market has an asymmetric risk profile and offers more downside risk than upside opportunity. Political realities and last year's precedent suggest the potential that Congress fails to reach agreement in addressing the 'fiscal cliff' is greater than what most investors seem to believe based on our client conversations." David Kostin, 8/25/12

Jan Hatzius, Goldman Sachs

"As we have discussed recently, our worry about the fiscal cliff has increased in recent months as neither Democrats nor Republicans seem inclined to budge on the most contentious issue, namely the fate of the upper-income Bush tax cuts. While we have not changed our baseline assumption of an ultimate agreement to extend most of the major provisions--with the conspicuous exception of the payroll tax cut--the risk of at least a short-term hit from all of the fiscal cliff provisions as well as a permanent expiration of the upper-income tax cuts and/or the availability of emergency unemployment benefits has clearly grown. " - 10/4/12

Buffett's Alpha, via Yale University

"Buffett's performance is outstanding as the best among all stocks and mutual funds that have existed for at least 30 years. Nevertheless, his Sharpe ratio of 0.76 might be lower than many investors imagine. While optimistic asset managers often claim to be able to achieve Sharpe ratios above 1 or 2, long-term investors might do well by setting a realistic performance goal and bracing themselves for the tough periods that even Buffett has experienced.

In essence, we find that the secret to Buffett's success is his preference for cheap, safe, high-quality stocks combined with his consistent use of leverage to magnify returns while surviving the inevitable large absolute and relative drawdowns this entails. Indeed, we find that stocks with the characteristics favored by Buffett have done well in general, that Buffett applies about 1.6-to-1 leverage financed partly using insurance float with a low financing rate, and that leveraging safe stocks can largely explain Buffett's performance." - Buffett's Alpha, Yale University

If you have questions or concerns please contact Orcam Financial Group, LLC at (858) 220-5383 or by email at info@orcamgroup.com

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