GMP Investment Management
Maximizing Return, Minimizing Risk

GMP Diversified Alpha Fund

Monthly Market Commentary August 2010

The Alpha Master Fund (the “Fund”) generated a net positive return of 0.08% for the month of August, net of all fees. YTD, the Fund is up 3.06% and since inception up 16.95%. The Fund is ahead of the S&P 500 since inception by over 3700 bps and has outperformed the TSX by over 2700 bps. While this return is very positive, it is our risk posture that we continue to highlight. The rolling 12 month volatility for Alpha is 3.70%, considerably less than the 17.35% volatility on the SPX and 14.51% on the TSX 60. This performance is consistent with our mandate of providing a consistent risk adjusted return experience for our investors, and above all, protecting invested capital.

August was another interesting month, one where volatility, jobs (in the U.S.) and Potash Corp (in Canada) were the lead stories. In the U.S., the SPX gave back the majority of the return earned in July and had negative performance of 4.74%. The weekly “jobs” number pushed the markets lower during August as the reported unemployment picture remained at 9.6% nationally, although several state pictures look worse (specifically California, Nevada and Michigan each with reported numbers above 12%). The persistent high level of unemployment is destroying consumer confidence, thereby challenging any enthusiasm that developed in the markets during July. The August selloff in the equity markets did offer us an opportunity to pare our shorts and reduce our overall SPX Index put position with profit. As a result, the Fund was positioned to be more “long” as we entered September. As a supportive counter-indicator to the direction of our book, Lipper FMI data for the week ending September 1st, showed that Equity Mutual Funds in the U.S. experienced outflows of $580MM while taxable Bond Funds experienced inflows of $2.6 billion. Experience continues to demonstrate that this retail asset flow tends to be late and a reliable contrary indicator of short term market performance. Our internal allocation models continue to support the theme of adding to the Fund’s equity allocation which we did as we exited August and entered September.

Equity Strategy

The equity book generated negative returns for the month of August primarily driven by losses in select technology and energy holdings. Although these returns were disappointing compared to the positive return of the S&P TSX Index, they materially outperformed global equity benchmarks which experienced losses of between 3% and 5%. The positive returns for the S&P TSX Index were very narrowly driven. Outside of the 45% return from Potash Corporation of Saskatchewan (we did not have a position in POT), and the strong returns from gold equities, positive returns were difficult to generate. During the month, the Fund transitioned away from expensive defensive holdings and materially increased its net exposure to equities that were more economically sensitive with lower valuations.

Credit Strategy

The Credit Strategy generated positive performance in August from both our corporate bond and Canadian ABCP positions. Overall the credit markets performed well from a new issuance standpoint as corporate issuers took advantage of the current low interest rate environment and the demand from investors for yield products. Yields actually widened during the month as markets were concerned with the stagnating pace of the economic recovery. As we exited the month, the strategy reduced a portion of its short exposure.

Quantitative Strategy

The Quantitative Strategy was positive in August due in large part to our volatility arbitrage strategy where we are short index options. Volatility implied by option prices was significantly higher than realized volatility (realized volatility reflects the actual trading of the indices for the month). This reflects a risk premium being priced into the market as participants continue to be fearful. It is our view that actively managing these positions present good risk return potential for the Fund.

Risk Management

In August we had a protective put spread position that represented over 10% of the assets of the Fund and roughly 50% of our equity exposure for the month. Our lower overall beta exposure to the equity market was intact at the start of the month; however, we increased our overall equity exposure by month end. We entered September with our models indicating that assuming more risk was appropriate at this point in time.

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