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Portfolio Commentary

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It has become increasingly clear that the European Debt Crisis is not an issue that will be resolved anytime soon. The million dollar question “can contagion be avoided” appeared to be answered and the answer was “No”. Headline after headline offered proof of contagion and drove a “risk-off” market. Further downgrades of financial institutions and sovereign countries, sky rocketing yields on peripheral nations’ debt, and the unfolding of the MF Global saga, offered proof that Europe’s tremors have not been contained. Yields on peripheral government bonds, including Spain, Portugal, and Italy, remained elevated with little signs of easing as progress on European policymaking offered little relief. Just before Thanksgiving, the Eurozone issues were compounded when the US Congressional Super Committee missed their deadline to produce \$1.2 Trillion worth of deficit reductions. There was some good news after the holiday, however, when central banks announced their plans to coordinate and work together in an effort to contain the European disaster and protect the global economy.

The dominant theme in Europe continues to be politics standing in the way of substantive reform and viable long-term solutions. November witnessed the changing of political guard in several Eurozone countries including the new Prime Ministers in both Greece and Italy. The policy and political tension in Europe and the US continue to overshadow improving US economic conditions. The Fed maintains its commitment to low rates and promises to intervene, if necessary. The FOMC revealed that they consider QE3 a viable option, although, an imminent implementation is not likely. Attention has turned to budget cuts in the US, in hopes that a plan from Congress will help bolster market sentiment. Just before the Thanksgiving holiday, the Super Committee announced that they failed to reach an agreement by the November 23rd deadline. Rating agencies Standard & Poor’s and Moody’s, reaffirmed their current US Sovereign ratings, but warned continued inability to cut the deficit may result in a downgrade of US debt.

The MF Global bankruptcy in October caused further disruption in the market. The market has been predominantly in “risk-off” mode for several months now, but the announcement of MF Global’s failure and the missing margin money, led investors to again flock to cash positions, at the expense of global commodities and equity markets. Capital preservations taking center stage yet again.

Given the limited appetite for risk, yields on the short end of the curve are expected to remain floor bound, as investors stay close to short- and intermediate-term investments. Despite S&P’s downgrade of US Sovereign debt in August, US Treasuries continue to be the investment of choice for safety and liquidity. But investment grade corporate bonds are increasingly being utilized as an alternative safe haven investment. Many corporations have historically high levels of cash on their books and have overhauled their balance sheets improving their overall credit profile. Investors recognize these improvements and have flocked to these investments which offer better returns than comparable US Treasury securities. We expect demand to continue for top rated commercial paper and corporate notes especially on the short end of the curve.

We continue to search the short end of the curve for high quality credits. Horizon employs both technical and fundamental analysis to monitor our existing approved list of issuers, keeping a watch on potential headline risks. We also utilize this strategy to identify credits that offer investment opportunity. In commercial paper and corporate notes, we prefer high quality names in the consumer staples sector and are cautious among financial institution credits. The MF Global collapse has placed a spotlight on prime brokers and the safety of funds held in customer segregated accounts. Horizon continues to be an alternative to passive assets, excess margin money or other cash, residing at a fund’s prime brokers. We continue to apply a conservative and prudent approach to managing cash balances.

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