CENTURION Asset Management

610 W. Germantown Avenue, Suite 150
Plymouth Meeting, PA 19462

November 2010

As we approach the end of the year, investors are re-positioning themselves after two recent events: quantitative easing and congressional seat changes. Let us review the recent movements of the financial markets and the economy, and share some thoughts on the effect of QE.

October ends

The last week of October was generally flat for the markets, with the Dow Jones Industrial Average finishing down fractionally to 11,118 and the S&P 500 Index unchanged at 1,183. The technology company heavy Nasdaq Composite finished up, rising 1.1% to 2,507. For the year, the Dow is up 6.62%, the S&P is up 7.84%, and the Nasdaq is up 10.5%. Those are all nice turnarounds from the beginning of September, and up over 10% over that short period. The best performing sectors year-to-date are as follows:

Sector	Percent return YTD
Consumer Discretionary	19.40
Industrials	16.30
Telecom	12.00
Consumer Staples	10.80
Materials	9.50
Technology	6.40
Utilities	5.50
Energy	4.80
Financials	1.90
Health Care	1.40
S&P 500	7.80
	Source: J.P. Morgan AM Weekly Market Recap

The economic backdrop is rather mixed. The third-quarter gross domestic product (GDP) preliminary report showed that the economy grew at a rate of 2.0% (annualized) which was in-line with expectations. This figure implies slow growth in our economy, but is a continued improvement from the recent past. For the 4th quarter, growth levels are expected to be between 2.0% to 2.5% (annualized). This slow growth expectation is countered by easier financial conditions and banking standards heading into 2011.

In order to boost growth, the Fed announced that their central bank will begin to purchase securities in the open market, which is referred to as "quantitative easing" (QE). This is a similar program to the one rolled out last year, and is now being termed QE2. The policy behind this Fed decision is to stave off the possibility of a Japan-style deflation in our economy. Japan has experienced 20 years of near-zero nominal interest rates, and found it a difficult cycle to escape. The Fed's action is designed to help stimulate growth and ward off deflation, thus avoiding Japan's conundrum.

Under the program, the Fed will buy $600 billion in longer-term Treasuries by the end of June 2011, a pace of $75 billion per month. Many economists feel this could cause *inflation* after the Fed was trying to stave off *deflation*. It is a tricky proposition, but one the Fed is defending in light of their ability to make the right maneuvers, something Japan proactively did not.

The top of the class

Endowment funds have become a frequent topic of conversation among asset managers and individual investors, over the past several years. Why? Because of their size – the top 10 endowments are all over $5 billion – these pools of money are managed by some of America's best academic minds, thus we are curious to see the interplay between these institutions and the public and private markets. Let us focus on the Yale endowment for a peak at how you may balance your investable assets.

Largest Endowments (U.S.)		
ranked by total assets in billions, as of June 30, 2009		
Rank	Institution	Assets
1	Harvard University	$ 26.00
2	Yale University	$ 16.30
3	University of Texas System	$ 15.20
4	Stanford University	$ 12.60
5	Princeton University	$ 12.60
6	Massachusetts Institute of Technology	$ 8.00
7	Northwestern University	$ 5.84
8	University of Michigan	$ 5.83
9	Columbia University	$ 5.70
10	The Texas A&M University System	$ 5.37
Source: NACUBO		

The Yale endowment ends and reports its yearly performance mid way through the year. For the year ending June 2010, the endowment rose to $16.5 billion after an 8.9 percent gain. The endowment recognized $1.4 billion in investment gains, $136 million in gifts, and a payout of $1.1 billion to the university. During the previous year the endowment lost 24.6 percent.

Securities offered through NRP Financial, Inc., Member FINRA/SIPC and advisory services provided by NRP Advisors, Inc.

David Swensen is the Chief Investment Officer at Yale University since 1985. He is responsible for managing and investing the University's endowment assets and investment funds, and accumulated an exemplary track record over his 20 years of managing the fund. He has amassed an 8.9% return over the past 10 years.

Swensen developed the concept of institutional diversification into ill-liquid assets like timber, hedge funds, and private equity funds, and has held firm to the strategy even after a steep loss of 2009. By comparison, over the past 10 years Harvard trails Yale in portfolio growth, 7.0 percent to 8.9 percent (average annual return). Yale's record is even better against the average institution, coming in at more than double over the last 10 years (8.9% vs. 4%).[i]

University of Pennsylvania graduates should be proud – their endowment posted a 13 percent investment return for fiscal year ending June 2010. That follows a decline of 15 percent the previous year, when many large endowments lost far more during the financial crisis and recession. The Pennsylvania endowment, led by Kristen Gilbertson, was valued at $5.7 billion as of June 30, 2010.

The returns are impressive, but let us consider the philosophy, and the allocation for the Yale endowment, and how it either helped or hurt their return.

Swensen and Dean Takahashi developed what has come to be known as "The Yale Model" several years ago. It consists of broadly dividing a portfolio into five or six roughly equal parts and investing in a different asset class. At the center of the model are decisions to avoid asset classes with low expected returns such as fixed income and commodities.

This idea of diversification and asset selection is familiar to most investors, however, when the idea was first introduced in the endowment community, most endowment portfolios were simply invested in treasuries and short-duration bank instruments. The Yale Model took a more revolutionary approach, and implemented Modern Portfolio Theory to the endowment pool, there-by investing for the long-term, similar to an individual's 401k account.

Now, the Yale endowment has access to investments that most of us do not, but there are some principals that investors can emulate when making investment decisions. For example early in 2010 it was known that Yale increased its allocation to Real Estate, commodities, and private equity, while it reduced its exposure to U.S. and foreign equities, and remained relatively un-invested in bonds.

We can assume Swensen sees the real estate, commodity, and private equity markets as undervalued long-term. Also, he stated, "Yale is not particularly attracted to fixed income assets, as they have the lowest historical and expected returns of the six asset classes that make up the endowment." Further, "…the government bond market is arguably the most efficiently priced asset class, offering few opportunities to add significant value through active management."

Because of Yale's long-term performance, some may conclude they are terrific outliers who have a magical approach and superior access to impactful investment opportunities. However, the cause of their great performance in reality is their willingness to stick to the tenants of diversification, and a long-term perspective, while also remaining active with their investment weightings.

For several years we have written about the merits of an active approach to investing. When coupled with a diversified portfolio, the act of overweighting and underweighting investments in different asset classes and styles is in our opinion the best manner in which to achieve market outperformance. Swensen and the Yale endowment exemplify this belief.

Next month we will again touch on the effect of QE2, and review the year to date figures of the markets against some of our early 2010 predictions.

Past performance is no guarantee of future results. Indexes are unmanaged, do not incur fees or expenses and cannot be invested in directly. Investing in sectors may involve a greater degree of risk than investments with broader diversification. International investments are subject to additional risks such as currency fluctuations, political instability and the potential for illiquid markets. Investing in emerging markets can accentuate these risks.

The information contained herein is obtained from sources believed to be reliable, but its accuracy or completeness is not guaranteed. This report is for informational purposes only and is not a solicitation or a recommendation that any particular investor should purchase or sell any particular security. All expressions of opinions are subject to change without notice.

[i] 2009 NACUBO- Common Fund Study of Endowments