GLOBAL VOLATILITY SUMMIT 2012

February 8th, 2012 Newsletter

Event Details

Date. March 6, 2012

Details. A one day summit to educate investors on the universe of volatility funds and tail hedging managers and discuss the market environment.

Location. Skylight Studio in Soho in New York City.

Event Details

Keynote speakers. We are excited to report that General Stanley McChrystal and The Honorable Rahm Emanuel (Mayor of Chicago) will be speaking at the event.

Managers. The following managers will be speaking at the event.

36 South Capital Advisors
Acorn Derivatives Management Corp.
Alphabet Partners
Amundi Asset Management
ArrowGrass Capital Partners
Blue Mountain Capital
Capstone Investment Advisors
Fortress Investment Group
III Associates
JD Capital Management
Man Group
Parallax Fund
Pine River Capital Management
Vulpes Investment Management

Registration. Space is limited, please visit the website to sign up as soon as possible.

Agenda and speakers. Please continue to check the website for event details and tentative agenda.

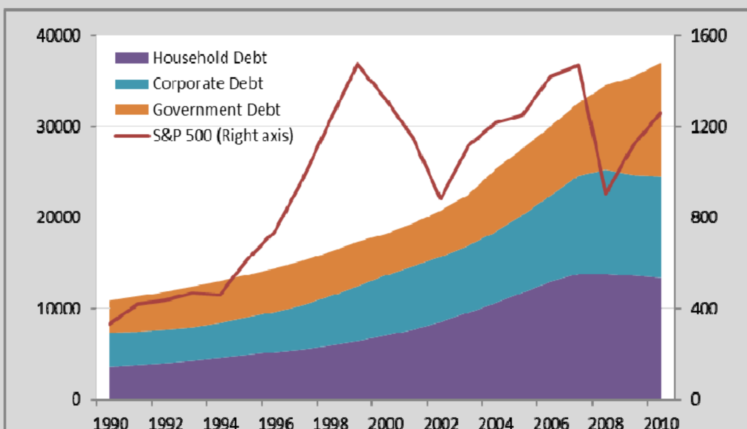
Questions? Please contact info@globalvolatilitysummit.com

The goal of the Global Volatility Summit ("GVS") is to educate investors about investing in volatility. With the approach of the third annual GVS, we felt it was appropriate to launch a newsletter continuing this mission. Leading up to GVS, we have asked industry experts to discuss their thoughts and opinions on the volatility universe. This past year we have seen an uptick in interest in various strategies available in the volatility space, namely in relative value and tail risk, and we are keen to ensure investors are kept abreast of the most recent developments in all relevant strategies. We believe there is a volatility strategy that can be a suitable component of every investor's portfolio. That said, a concerted effort from the volatility community is required to continue to educate investors so they are aware of the pitfalls and benefits of various strategies available to them.

We asked *John-Mark Piampiano, Portfolio Manager at Pine River Capital Management* **to share his outlook for tail hedging in 2012.**

Cheers,
Global Volatility Summit

In the first GVS newsletter, Paul Britton (CEO of Capstone) predicted that the large oscillations in the price of volatility which characterized 2011 would continue in 2012 on the basis that the rapidly evolving regulatory environment has led to a dearth of liquidity in option markets. At Pine River, we also believe that these oscillations in the price of volatility will continue, but our rationale is founded on different grounds. The events which have precipitated the extreme fluctuations in the price of volatility since the onset of the subprime lending crisis in 2007 have been characterized by a focus on excess leverage. Whether that leverage was in the form of U.S. mortgage debt in 2008 or Greek government bonds in 2011, each time the creditworthiness of a large subset of debtors has been called into question, the ensuing uncertainty has roiled financial markets. If recent turmoil has been driven in part by leverage, a return to "normalcy" should be predicated in part on a reduction in leverage at the broad economic level. In fact, the pace of debt expansion in the United States has not changed significantly over the past five years, as evidenced by the chart below which shows Federal Reserve data on U.S. debt outstanding:



Source: Federal Reserve and Bloomberg

The relationship between debt levels and equity volatility at the corporate level has been extensively studied, starting with Robert Merton's seminal 1974 model exploring the valuation of equity as a call option on corporate assets. Subsequent academic work has made significant strides to define the relationship between credit, equity, and volatility in increasingly rigorous and complex terms. The broad implications of these models have potential ramifications to today's market: as credit spreads widen, equity volatility should rise and the sensitivity of equity volatility to a change in credit spreads increases as the ratio of debt to equity rises. The continued growth of debt in the U.S. in the face of an equity market capitalization which has not changed materially over the past decade suggests that equity volatility and the high sensitivity of equity volatility to credit market developments will continue until total debt falls relative to equity capitalization. Obviously this can occur by either a reduction in debt or an increase in the equity capitalization.

The picture is complicated by significant structural shifts in the character of the expansion in U.S. debt outstanding. As we can see from the chart on the previous page, corporate and household debt in aggregate actually shrank since 2007, but the explosion in U.S. government debt has maintained the growth trajectory of outstanding debt at pre-crisis levels. While this consumer/corporate de-levering could contribute to a gradual decline in equity volatility, there is a risk that U.S. government tax and fiscal policy will play a role in the strength of the relationship between government debt and equity volatility. For example, it is possible that if the government debt burden is shifted to households and corporations via higher taxation, that taxation may operate as a transmission mechanism to neutralize the decline in volatility implied by the improvement in household and corporate balance sheets.

John-Mark Piampiano
Portfolio Manager
Pine River Capital Management