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After Hours Quarterly

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Letter from the CEO

Dear Clients and Friends,

On behalf of the entire Penserra team we are motivated and inspired by the opportunities that you give us. Delivering results that exceed your expectations is our highest priority. We remain dedicated to continually developing our core offerings, strengthening our capabilities, and building trusting relationships with our clients and partners.

Recently a number of financial services firms have ceased to offer transition management services. Various reasons have been speculated and cited in news articles that you have likely already seen. These are large firms that have left this segment of the industry; and the decisions to exit range from decreased profitability, regulatory challenges, or conflicts with other service lines.

At Penserra, we are committed to providing transition management services for the long term. Our company was founded and built with transition management as one of its strategic business lines. We continue to grow our firm, integrate new technology, and make experienced hires. We are also proud that the leadership within our Transition Management team hails from a number of well-respected firms throughout the industry including Russell, Black Rock (Barclays Global Investors) and Knight Capital to name a few .

Transition management is more important than ever. The ability to provide exceptional communication, transparent reporting, and fiduciary oversight has allowed Penserra to build an exceptional brand with clients from some of the most sophisticated pension plans, corporations, asset management firms, and consultants in the country.

Thank you to our clients and friends for allowing us the opportunity to be your trusted partner. You have my commitment that we will continue to work hard for you and that we will reinvest in our business to provide exceptional transition management services for years to come.

Sincerely,

George Madrigal
President and CEO

What's New at Penserra

We are happy to announce new additions in the first quarter to the Penserra team. Jason Harrod has joined us as a Senior Equity Trader in our Orinda office. Jason has a 14 year trading career and most recently worked at Lazard Capital Markets. The firm also hired Chuck Drummond as an investment banker focused on equity and debt underwriting as well as buy-backs. Chuck has more than 30 years of industry experience and most recently worked with MFR Securities. Please join me in welcoming Jason and Chuck.

EQUITY RESEARCH UPDATE

As announced in our last quarter newsletter, we have introduced a new research product. In the first quarter, we initiated on 18 companies (see table below).
Some of the highlights:

iRobot (IRBT)
We predicted IRBT to beat consensus and they beat by .56%. Surveys indicated a strong holiday season, with customers returning and upgrading their models. IRBT showed strong sales, especially in their newer models.

Samuel Adams (SAM)
We had SAM beating consensus, which they did, but they had a weak bottom line. This was due to a higher demand in product volume, which increased costs for shipping and production. Surveys picked up the higher volume and gaining in market share, which accounts for the higher demand in product but failed to identify the weak bottom line.

Molson Coors (TAP)
We predicted TAP to come in at 1028 and beating consensus. TAP posted at 1028. Surveys indicated that Coors was the best seller, but craft beers were starting to take market share from Coors and Coors light. TAP accounted for 29% of the 2013 Craft beer growth in the U.S. with their own craft beer.

Brown Forman (BF/B)
We predicted a 3.18% miss from consensus; however, they beat consensus by .31%. Surveys only account for the United States, which only account for 40% of BF/B's revenue. While the United States had strong revenue, BF/B recorded large growth in revenue internationally which was not surveyed.

Vera Bradley (VRA)
We predicted a slight miss by VRA, however they beat consensus by 7.07%. Our model was too aggressive in pricing in the effect of poor weather, and although sales were low, they weren't as low as we expected. However, surveys indicated lower market share, and low foot traffic. VRA has since lowered guidance and is expecting a poor fiscal 2015.

Commercial Vehicle Group (CVGI)
We had CVGI beating consensus; however, they fell short by 4.19%. Our surveys indicated a turnaround for CVGI after 5 very tough quarters. CVGI is experiencing a turnaround, but it probably won't show until next quarter.

As we continue to roll out new companies, and accumulate additional data on a quarterly basis, we believe that our research will become more detailed and refined.

Penserra Research First Quarter Initiations

CVGI	Commercial Vehicle Group	ACAT	Artic Cat
SKX	Skechers	ETH	Ethan Allen
TAP	Molson Coors	IRBT	Irobot
BKS	Barnes & Noble	WHR	Whirpool
BNNY	Annie's	CASY	Casey's
LL	Lumber Liquidators	DKS	Dick'S Sporting Goods
SAM	Samuel Adams	ULTA	Ulta Beauty
BF/B	Brown Forman	BWS	Brown Shoe
WGO	Winnebago Industries	VRA	Vera Bradley

For a copy of any reports, or to be added to our research list, please contact research@penserra.com

CAN ETFS OVERTAKE MUTUAL FUNDS?

I used to get asked regularly on the conference circuit whether or not ETFs could overtake mutual funds. At first my answer was no, and I was almost in shock that anyone would even think that could happen. Then my answer became no, but perhaps with qualifiers such as ETFs going into 401Ks or active ETFs taking off. Today, my response is that it will probably happen, it's just a matter of time. Earlier this year, at ETF.com's "Inside ETFs" conference, the largest conference dedicated to the ETF space, the opening keynote presentation proclaimed that ETFs will have $15.5 trillion AUM in 10 years, which will be bigger than mutual funds. That statement certainly got my attention and I think it is worthy of a closer look. Let's first take a look at the evolution of ETF usage within the institutional, intermediary, and retail spaces; and then take a look at how some of the trends that have drivengrowth over time may look in the future.

It is estimated that roughly 50-55% of ETF assets are owned by institutions, but only 18% of institutions own ETFs. Some recent research has also indicated that holding periods for ETFs within institutions have also been increasing. Institutions, who once viewed ETFs more as a short term tactical solution for things like cash equitization and transition management, now view them as more of a long term strategic allocation. A perfect example of this transformation happened about a year ago when the Arizona State Retirement System seeded 4 new ETFs launched by Blackrock iShares. There is clearly room for much more growth in the institutional space and much of it has been driven by cost. Expense ratios have come down over time and have been especially compressed in the most core funds, where many institutions would have the most interest anyway. Perhaps the biggest driver of growth for institutions has been liquidity. ETFs now account for roughly 25% of all exchange trading volume on a daily basis; and the majority of the top 10 traded names by volume are typically in ETFs. Take, for example, buying a slice of the Russell 2000 index relative to buying the Russell 2000 ETF managed by iShares. Buying the underlying index will cost you about 20 bps in spread cost plus commission where buying the ETF will cost you 1 bp in spread cost plus commission, and depending on the way you trade it you may be able to further reduce commission and spread costs from there with the ETF.

Financial intermediaries and self directed retail investors have followed a similar path of evolution in ETF adoption and usage. In general, over the last several years, more intermediaries and retail investors have started to use ETFs. Furthermore, the people who used ETFs in the past have increased their usage and made them more of a core holding. Many intermediaries who were historically paid on commissions from transactions within an investor's account have moved to a fee only model where the focus is more on cost control. ETFs are cheap and have become cheaper over time. Beginning with a program that Schwab launched in late 2009 there are also several platforms that offer no commission ETF trading. Considering retail investors tend to have the smallest trade sizes, the no commission offerings have been especially effective with that audience. Probably the biggest story with retail investors has simply been education and awareness. As recently as 5-10 years ago you could ask a room full of retail investors what they knew about ETFs and you would not get much of a response. Many investors had never heard of ETFs, including people who at least had an idea what a mutual fund was. That is changing big time as advertising has gone more mainstream and wider adoption seems to beget even more interest.

Although it's difficult, if not impossible, to know where each new dollar going into an ETF came from, it's worth noting that ETFs don't just compete against mutual funds. It is widely believed that the majority of new money going into ETFs is coming from individual stocks and bonds as well as cash. This could be the most compelling argument for ETFs eventually overtaking mutual funds. At year end 2013 Blackrock estimated the value of the broad US investment landscape at $74.3 trillion which broke down as $1.7 trillion in ETFs, $11 trillion in mutual funds (ex money market funds), $22.3 trillion from underlying US equity markets and $39.3 trillion in underlying US bond markets. Given the historical advantages of ETFs over other vehicles such as low cost, liquidity, tax efficiency and transparency coupled with continued innovation and diversity in the types of ETF products launched, it seems likely that it is no longer a question of whether ETFs can overtake mutual funds, but a question of when that will happen.

For additional information please contact Dustin Lewellyn at ETF@Penserra.com.

CHANGES IN THE FED'S RATE GUIDANCE

For more than a year, the Fed has kept its guidance on its "easy" monetary policy by publicizing that it wouldn't raise rates as long as the unemployment rate is more than 6.50% and the outlook for inflation is no more than 2.50%.

As we approach the 6.50% threshold with the unemployment at 6.7%, the Fed's guidance is becoming obsolete. The most recent Fed's comments suggest no raising of rates until sometime in 2015.

Janet Yellen's first FOMC meeting as the Federal Reserve Chair comes on March 18-19th. One of her largest challenges will be to: "replace the threshold with guidance that is less specific while also making it clear that rates won't rise anytime soon. If the Fed retreats to language that investors find vague and economic data comes in strong, traders are likely to move forward their estimate of when the Central Bank will raise rates, creating volatility in financial markets" (Bloomberg News 3/12/14: Craig Torres and Joshua Zumbrun).

The delicate balance appears to be in having less specific guidance thresholds mixed with keeping volatility to a minimum and preventing the markets from perceiving an earlier raising of rates.

Yellen's view that a broader range of data is needed to better understand the job market focuses on the problem of just looking at the headline unemployment number. "With total joblessness at 6.7% in February, still higher than the Fed wants, the rate for those who have been out of work less than 27 weeks, was just 4.2%. That's near the lowest since April 2008 and .6% percentage point below the average since 1948." Some economists take this to suggest the labor market is tightening and will eventually lead to a pickup in inflation.

As we move forward, the Fed must deal with withdrawing the "punchbowl", ie. "tapering", while formulating a program of interest rate guidance for the markets to digest.

Post Script/Post Yellen:

In hindsight, we can see Janet Yellen and the Fed did drop 6.5% unemployment threshold and moved towards a "qualitative forward guidance" (a more unspecific basis). "The Fed in its official policy statement, said it planned to keep short term rates below what it sees as appropriate for a normal economy even after the unemployment rate and inflation revert to typical levels" (Jon Hilsenrath, WSJ 3/23/14).

The surprise came at the press conference following the conclusion of the March FOMC meeting. Her remarks suggested the Fed may start raising rates sooner than the markets had perceived or as little as 6 months after the tapering had ended.

With the $10 Billion decrease in tapering largely expected at each of the coming FOMC meetings, this might suggest that 5-6 meetings might mark the end of the tapering (either October or December 2014). Adding an approximate 6 months after this would bring an expected initial Fed Funds hike between April to June 2015. This earlier expected raising of short term rates comment immediately brought short term treasury rates up within minutes. As a reaction, Janet Yellen tried to moderate the earlier rate hike perception with a speech on March 31st. In this speech she stated that there was "considerable slack in the labor markets", and the Fed's accommodation will be needed for "sometime".

As more economic data becomes available, the market will listen to Janet Yellen and the Fed governors for more specific rate guidance.

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- Thematic Views of Asia – Monthly report highlighting views from Brokers, Buy-Side Firms, and Industry groups
- Updated IPO and Secondary Calendar for Asia and Japan – Bi-monthly
- The Marginal Prophet –a topical thought-provoking piece that humanizes the crazy industry we work in

To receive an individual report, or to be added to our distribution list, please contact: research@penserra.com

ABOUT PENSERRA

Founded in 2007, Penserra Securities is a full service broker/dealer servicing institutional clients with offices located in the New York, Chicago, and San Francisco areas. Through state of the art technology, Penserra delivers products and services in equity, fixed income, interest rates, and credit markets. Our networks deliver global connectivity to customers seeking unparalleled liquidity and flow in orderly marketplaces. Penserra Capital Management LLC is a Registered Investment Advisor and affiliate of Penserra Securities LLC. Advisory and fiduciary services including transition management and ETF sub-advising offered through Penserra Capital Management LLC, a Registered Investment Advisor and affiliate of Penserra Securities LLC.

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