



# MANCHESTER

CAPITAL MANAGEMENT, LLC

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## *Price Versus Value*

An important control you have when investing is the price you pay for something. Once you have bought it, be it a stock, a mutual fund, an index fund, or a bond, the markets are in charge. They will set the price for your security going forward, either up or down, and while you can sell at any time, you are at the mercy of the market's decision on what you will be paid back.

Price and value are not necessarily the same thing. Successful investment results require an understanding of the real value of an investment and the risk of loss it poses. Unfortunately, markets are sometimes not good indicators of either value or risk. Like the \$800 fashion item that you find later in a discount store for \$80, the markets can offer widely varying prices for an investment depending on the fashion of the day.

Markets react to a host of inputs that are a combination of financial calculations, human behavioral patterns, unexpected events, and momentum trends caused by feedback loops. There are as many exceptions as there are rules.

Typically, when there is strong consensus that something represents good value, it really means all the buyers have bought it and they are trying to convince each other of their wisdom. These buyers tout the inherent quality of their investment. They believe this "quality" limits the risk of loss and hope the trend will continue. Sometimes there are fewer buyers left to maintain price, and sellers begin to dominate, negatively tipping the price movement.

The opposite is also frequently true. When the herd has declared an investment hopeless, and too risky to warrant purchase, often it just means the sellers have all sold. Some of the best returns come from investing in such positions and places that enjoy depressed prices. Value conscious buyers take advantage of the low price.

The internet debacle in the spring of 2000 is a classic example of

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what happens when there is excess optimism in financial markets. The despair of bond investors in the early 1980s, when we had double digit interest rates, is an example of when low prices offered the beginning of outstanding returns. In hindsight, the greatest risk was at the point when there was the most enthusiasm. The least risk was at the time of greatest fear. An old market saying is that you should "buy when there is blood in the streets."

The current domestic stock markets have enjoyed a terrific run to achieve new highs. There remains some healthy skepticism about stock market prices which makes it hard to know when the momentum will change. The US economy has definitely slowed, but corporate earnings remain strong, growing exports are helping with the trade balance, and cheap money is inciting a tidal wave of corporate takeovers, mergers, and buyouts.

We are watching corporate acquisitions by private capital with some concern as new owners more often take advantage of a balance sheet to line their own pockets rather than improve the core business. These investment bankers, LBO funds, and now increasingly hedge funds load up the company with new debt, squeeze capital investments, and sell off assets. They are after their fees as they take from the value to push up the price.

We also continue to have alarm about the growing complexity of financial instruments. The latest one to take our breath away is a CPDO, which stands for a Constant Proportion Debt Obligation. This nifty leveraged pool of credit derivatives pays junk

bond interest rates while somehow garnering a triple-A risk rating, as if it represented the best credit quality bond. It is the financial equivalent of a great hot fudge sundae, whipped cream and all, but with no calories.

We work very hard to understand the real value of any investments we purchase for our clients. We know the final outcome will depend on the price we pay at the beginning, and the risk we are accepting for the opportunity. We know that the price can often be greater or less than the true value.

*Ted Cronin, CIO*

### *Real Estate Services*

At MCM, we believe a component of managing a superior investment process should give due consideration, where appropriate, to direct ownership of real estate assets. We have a full-time team of real estate professionals dedicated to this effort making us unique in the multi-family office business. Our team has a successful track record in developing and investing in a wide range of real estate across multiple property types and geographic locations including commercial and private residential real estate, resort development, conservation land and easements, and raw land.

As a result, Manchester Capital Management offers in-house expertise able to acquire, develop, create, manage, and dispose of customized real estate portfolios for clients. In addition, we are able to leverage off this expertise to formulate real estate investment strategies for all of our clients utilizing real estate partnerships and REITs, both in the US and abroad.



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The international real estate securities market is one that may provide investors enticing risk/return opportunities, while offering very attractive diversification benefits. The market is growing very rapidly, doubling in size from \$400 billion in 2003 to almost \$900 billion in 2006, and most experts agree it will surpass the \$1 trillion mark in 2007. Much of that growth can be attributed to the increasing liquidity of the real estate investment trust (REIT) market.

Many international real estate companies are electing to “go public” and access the capital markets by structuring themselves as REITs, taking advantage of new REIT legislation sweeping through many countries. The securitization process provides greater liquidity, tax efficiency, and transparency to the local markets, all while allowing for the easy flow of capital into the country.

As a small component of one’s overall diversified portfolio, international REITs carry very attractive features. Volatility is similar to that of global equities, dividend yields are 2.5%, and international REITs offer the dual diversification benefits of exposure to foreign currency and foreign properties, all with low correlations to the traditional asset classes. In addition, the returns have been outstanding. Over the past five years ending March 31, 2007, the FTSE EPRA/NAREIT Global ex US Real Estate Index has returned 31.6% per year, compared to just 6.3% for the S&P 500. Consensus estimates supplied by UBS predict 12-15% returns in 2007 in this asset class.

International real estate business is

highly localized with supply/demand characteristics driven predominantly by the local fundamentals. Most countries have healthy GDP, benign interest rate environments and modest inflation expectations—optimal conditions for commercial real estate. Capital flows are expected to remain high, as many pension funds are beginning to dedicate part of their global real estate portfolios to the public markets. Even after 30%+ returns international REITs still remain attractively valued relative to the private market.

For those clients seeking direct ownership of investment real estate properties, our real estate team will develop and execute an investment strategy collaboratively with such clients. This process will include quantifying an appropriate range of portfolio exposure to real estate and the development of investment criteria such as geographic locations, property types, and acceptable financial structures and vehicles. Next, our real estate team will execute the plan within a targeted time frame and provide ongoing asset management services with a view to optimize investment return. Alternatively, we can assist “real estate heavy” clients with the selective and tax efficient disposition of real estate assets in order to reduce risk through portfolio diversification.

Furthermore, our real estate advisors are experienced in the identification and acquisition of legacy real estate assets that may be held for multiple generations. We also assist clients in utilizing real estate to achieve the client’s or a related family foundation’s charitable purposes including the use of



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conservation easements to protect environmentally sensitive lands.

Manchester Capital believes its in-house capability, along with the principal orientation of its Real Estate Services advisors, provide its clients comprehensive real estate investment services unmatched by most investment advisory and multi-family office firms.

*Bart Kraft, Vice President*  
*Bart Earley, CFA, CFP, Investment Analyst*

### The Case for International Real Estate Securities

1994- 4 countries with listed REITs



2007- 17 countries with listed REITs, 3 with legislation in place and 10 under consideration



Source: UBS April 2007

### Inside MCM

We are pleased to welcome Erin Marsh to MCM!



Erin joined the firm in March 2007 and works as an Operations Associate in our Manchester office. She is responsible for portfolio administration, performance reporting, and database management. Previously, Erin worked for an independent broker-dealer as their Operations Manager. In March 2006 she obtained her NASD Series 7 and Series 63 licenses. She is a Cum Laude graduate of Southern Vermont College with a BS in Business and an AS in Accounting. While in college she was captain of her volleyball team and served as Treasurer for the Student Government Association. Erin currently resides in Arlington, Vermont and spends most of her free time with her family and two year old German Shepherd, Lexi. She loves to go camping, watch live music, and play ball with her dog.