

# Real Assets: Preparing for an Inflationary Regime

11<sup>th</sup> September 2008 – Professional Pensions Forum

Presented in the U.K.

The services and products described in this communication are only available to professional clients as defined in the Financial Services Authority's Handbook. This communication is not a public offer and individual investors should not rely on this document. Opinion and estimates offered constitute our judgment and are subject to change without notice, as are statements of financial market trends, which are based on current market conditions. We believe the information provided here is reliable, but do not warrant its accuracy or completeness.

PIMCO Europe Ltd (Registered in England and Wales, Company No. 2604517), Registered Office Nations House 103 Wigmore Street London W1U 1QS Tel: 44-20-7872-1300. Authorised and regulated by the Financial Services Authority (25 The North Colonnade, Canary Wharf, London E14 5HS).

# Biographical Information

P I M C O

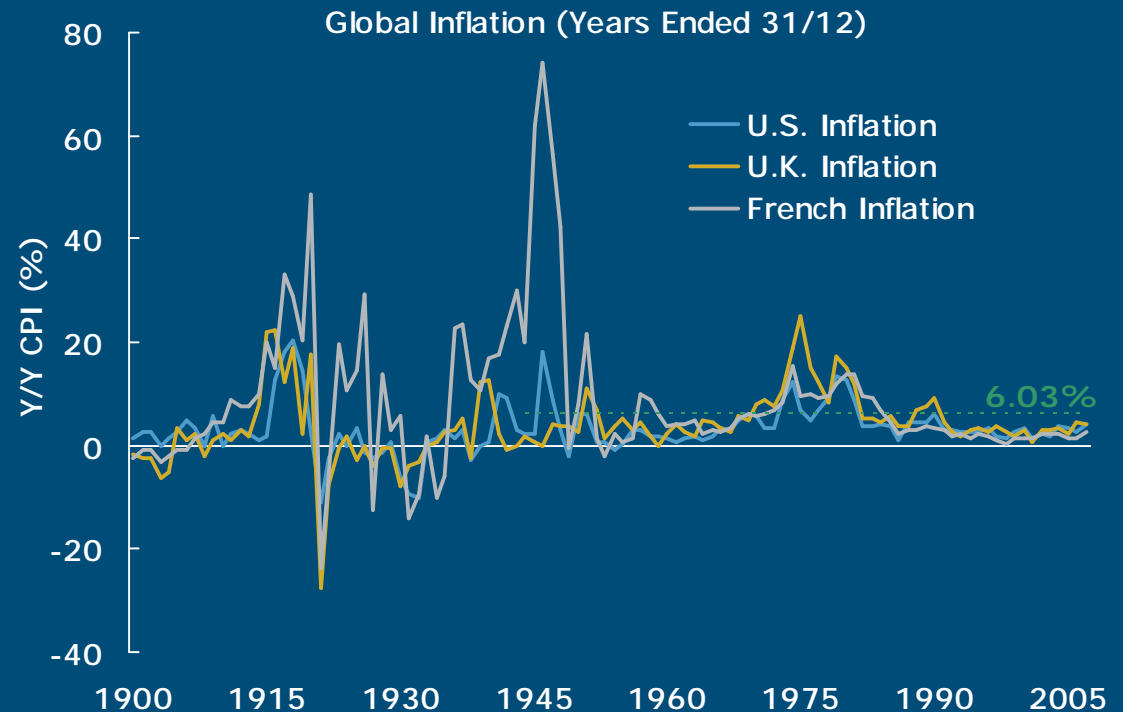
## **Antoinette Eltz**

Ms. Eltz is a Vice President and Product Manager responsible for European and UK Real Return Products. She joined PIMCO in 2007, having previously worked in the executive office of Allianz Global Investors for two years. Prior to that, Ms. Eltz was a proprietary derivatives trader and Eurex market maker with Botta Derivatives Trading GmbH in Frankfurt, Germany. Antoinette has 5 years of investment experience and holds a bachelor's degree in biology from Swarthmore College and an MBA from the Wharton School of the University of Pennsylvania.

# Inflation in Context

P I M C O

- § Historically there have been several periods of high inflation
- § Inflation occurs quickly and unexpectedly



From January 1944 through December 2007:

- Average U.S. Inflation: 4.03%
- Average U.K. Inflation: 5.50%
- Average French Inflation: 8.55%

SOURCE: U.S. Bureau of Labor Statistics  
Please refer to Appendix for additional index information

# Period of Disinflation Drove Allocation Biases

P I M C O

- § Inflation has not been a major concern in recent decades
- § Post-1970s defined by disinflation and declining rates
- § Was a period to favour financial assets vs real assets
- § What defined the past is not likely to define the future

# PIMCO's Secular Outlooks Calls for "Inflationary Handoff"

P I M C O

- § Commodity price pressures
- § Rising wages in emerging economies
- § Increased social spending in developed economies
- § Depreciating developed currencies vs emerging currencies
- § U.S. monetary policy that may be inflationary globally

Refer to Appendix for additional outlook information.

# Aligning Strategic Diversification with Regime Shift

PIMCO

REAL GROWTH

High/Rising

Low/Falling

Best: Equities  
Mixed: Commodities & Nominal Bonds  
Worst: ILBs

Best: Nominal Bonds  
Mixed: Equities & ILBs  
Worst: Commodities

Best: Commodities  
Mixed: Equities & ILBs  
Worst: Nominal Bonds

Best: ILBs  
Mixed: Commodities & Nominal Bonds  
Worst: Equities

Low/Falling

High/Rising

INFLATION

Refer to Appendix for additional diversification and risk information.

# Capturing Real Returns

P I M C O

## § Inflation-Linked Bonds

- Predictable real return, low volatility

## § Commodities

- Diversification, hedge inflation surprises

## § Real Return Multi-Asset Approach

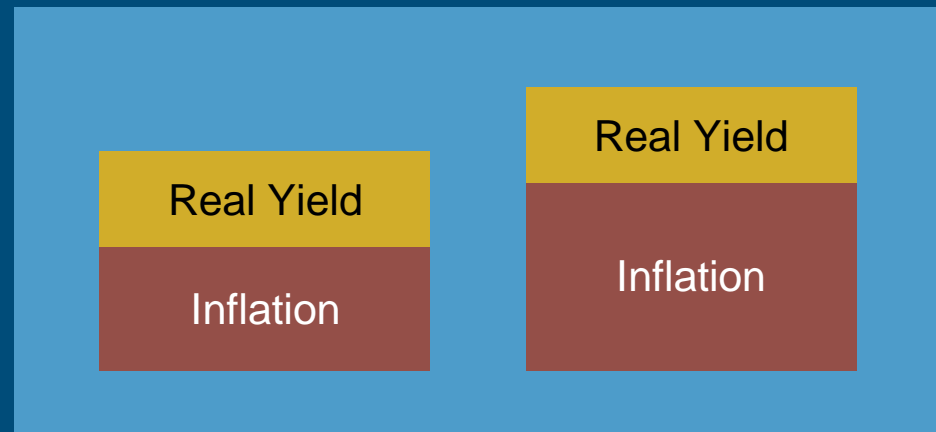
- Diversified exposure, tactically optimised for high real returns

Refer to Appendix for additional diversification and risk information.

# ILBs Diversify the “Disinflationary Bias” of Traditional Fixed Income

PIMCO

- § Predictable real return
- § Total returns explicitly linked to inflation



Refer to Appendix for additional diversification and risk information.

# Commodities Diversify Equity Risk and Hedge Inflationary Drivers

P I M C O

## Inflation Hedging

- § Positively correlated to inflation
- § Positively correlated to changes in rate of inflation

## Diversification

- § Negatively correlated to equities
- § Negatively correlated to bonds

## Return Potential

- § Magnitude of returns comparable to equities (1970-2007)
- § Volatility comparable to equities

Refer to Appendix for additional risk, correlation and diversification information.

# All Asset: Multi Asset Real Return Strategy

P I M C O



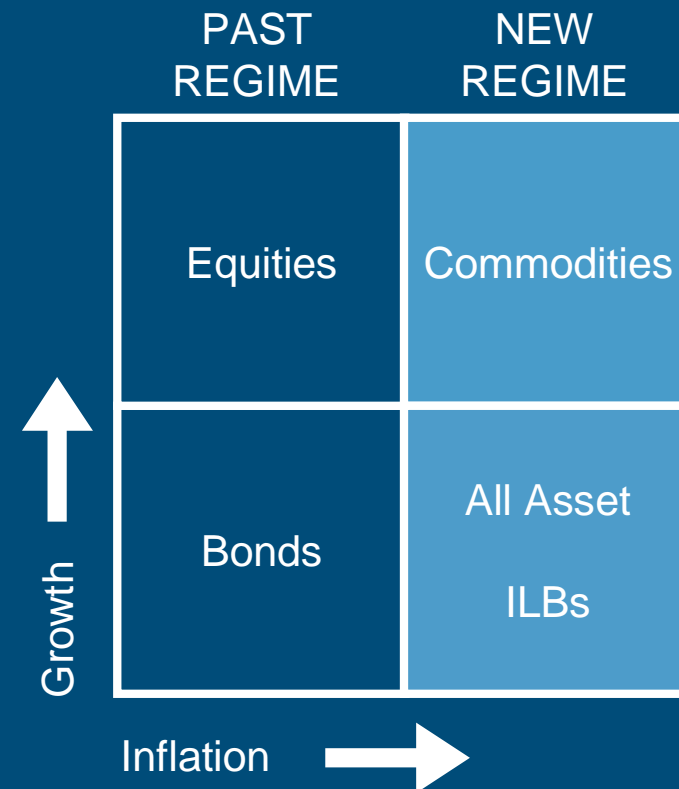
- § Seeks inflation + 4%
- § 6%-8% volatility
- § High ILB correlation
- § Low equity correlation

Refer to Appendix for additional risk, correlation, outlook and strategy information.

# Position for the Journey, Not the Destination

P I M C O

- § Strategic allocations should align with secular macro views
- § Real assets diversify during the regime shift, not after it!



Refer to Appendix for additional diversification and risk information.

# Appendix

PIMCO

## Outlook and Strategy

Statements concerning financial market trends are based on current market conditions, which will fluctuate. There is no guarantee that these investment strategies will work under all market conditions, and each investor should evaluate their ability to invest for the long-term, especially during periods of downturn in the market. Outlook and strategies are subject to change without notice.

## Risk

Each sector of the bond market entails risk. Municipals may realize gains and may incur a tax liability from time to time. The guarantee on Treasuries, TIPS and Government Bonds is to the timely repayment of principal and interest, shares of a portfolio that invest in them are not guaranteed. Mortgage and asset-backed securities are subject to prepayment risk and may be sensitive to changes in prevailing interest rates, when they rise the value generally declines. With corporate bonds there is no assurance that issuers will meet their obligations. An investment in high-yield securities generally involves greater risk to principal than an investment in higher-rated bonds. Investing in non-Euro securities may entail risk as a result of non-Euro economic and political developments, which may be enhanced when investing in emerging markets. Inflation-indexed bonds issued by the various Governments around the world, also known as ILBs, are fixed-income securities whose principal value is periodically adjusted according to the rate of inflation. Repayment upon maturity of the original principal as adjusted for inflation is guaranteed by the Government that issues them. Neither the current market value of inflation-indexed bonds nor the value a portfolio that invests in inflation-indexed bonds is guaranteed, and either or both may fluctuate. Inflation-indexed securities decline in value when real interest rates rise. In certain interest rate environments, such as when real interest rates are rising faster than nominal interest rates, inflation-protected securities may experience greater losses than other fixed income securities with similar durations. Commodities are assets that have tangible properties, such as oil, metals, and agricultural products. An investment in commodities may not be suitable for all investors. Commodities and commodity-linked securities may be affected by overall market movements, changes in interest rates, and other factors such as weather, disease, embargoes, and international economic and political developments, as well as the trading activity of speculators and arbitrageurs in the underlying commodities.

## Diversification

Diversification does not ensure against losses.

## Correlation

The correlation of various indices or securities against one another or against inflation is based upon data over a long time period. These correlations may vary substantially in the future or over shorter time periods, resulting in greater volatility.

## Index Descriptions

The Consumer Price Index ("CPI") measures prices of a fixed basket of goods bought by a typical consumer, including food, transportation, shelter, utilities, clothing, medical care, entertainment and other items. The CPI, published by the Bureau of Labor Statistics in the Department of Labor, is based at 100 in 1982 and is released monthly. It is widely used as a cost-of-living benchmark to adjust Social Security payments and other payment schedules, union contracts and tax brackets. Also known as the cost-of-living index. It is not possible to invest directly in an unmanaged index.

This presentation contains the current opinions of the manager and such opinions are subject to change without notice. This presentation has been distributed for informational purposes only and should not be considered as investment advice or a recommendation of any particular security, strategy or investment product. Information contained herein has been obtained from sources believed to be reliable, but not guaranteed. No part of this presentation may be reproduced in any form, or referred to in any other publication, without express written permission of PIMCO Europe Ltd (Registered in England and Wales, Company No. 2604517), Registered Office Nations House 103 Wigmore Street, London W1U 1QS. ©2008, PIMCO.