

Subject: Re: Fw: KCP Trade Ideas [I]

From: Caroline Kitidis <[REDACTED]>

Date: Thu, 17 Oct 2013 17:12:39 -0400

To: Chip Packard <[REDACTED]>

Cc: Haig Ariyan <[REDACTED]>

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I am speaking w/ Josh on this - to better coordinate and leverage resources/ideas.

But in general so you are aware, there is a bit of a disconnect that we should

try to rectify over time. I am seeing a few issues / crossing of wires:

1. For KCP - we have clients who want capital markets business, therefore the flow and structured transactions are important - a good example of this is Paul Morris/Epstein. This may not be as relevant today for PCS, but I believe we will have this offering for KCP clients (we definitely see this in EMEA and

Asia understanding that the PWM business is different there)

2. Global KCP is focused on capital markets and idea generation - Vinit has been tasked with focusing on this with the regions, so there is product and ideas focus from this end as well.

3. Yves team has to be ready and able to have the content and capabilities to do this, not sure they are at this point yet...

Kind regards,

Caroline Kitidis

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Caroline V. Kitidis

Managing Director | Head of Key Client Partners & Wealth Investment Coverage

-  
Americas

Deutsche Bank Securities Inc  
Deutsche Asset & Wealth Management  
345 Park Avenue, 26th Floor  
New York, NY 10154-0004  
Tel. [REDACTED]  
Mobile [REDACTED]  
Email [REDACTED]

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From: [REDACTED]

To: [REDACTED]

Cc: [REDACTED]

Date: 10/17/2013 02:13  
PM

Subject: Re: Fw: KCP Trade Ideas  
[I]

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Agree. Let's share with Yves and Josh to see what they can provide. They already have lots of trading commentary coming out daily by asset class.

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Chip Packard  
Co-Head, Wealth Management Americas

Deutsche Asset and Wealth Management  
345 Park Avenue, 10154-0004 New York, NY, USA  
Tel. [REDACTED]  
Fax [REDACTED]

EFTA01478562

Mobile [REDACTED]  
Email [REDACTED]

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From: [REDACTED]  
[REDACTED]

To: [REDACTED]

Date: 10/17/2013 12:23  
PM

Subject: Fw: KCP Trade Ideas  
[I]

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Here is what we are putting together daily - we update for timely tactical trades - to speak to in short term, and longer-term themes, that have a longer shelf life.

Some of these more structured transactions are KCP oriented (Euro curve steepening, European credit trades, Muni dislocation)  
Would be great if someone was putting this together or at least parts of it!

Kind regards,

Caroline Kitidis

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EFTA01478563

Caroline V. Kitidis  
Managing Director | Head of Key Client Partners & Wealth Investment Coverage  
-  
Americas

Deutsche Bank Securities Inc  
Deutsche Asset & Wealth Management  
345 Park Avenue, 26th Floor  
New York, NY 10154-0004  
Tel. [REDACTED]  
Mobile [REDACTED]  
Email [REDACTED]

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----- Forwarded by Caroline Kitidis/db/dbcom on 10/17/2013 12:20 PM -----

From: [REDACTED]  
[REDACTED]

To: KCP-  
Americas,

Date: 10/17/2013 12:13  
PM

Subject: KCP Trade Ideas  
[I]

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Hi All,

Please see the updated KCP trade ideas below. Presentations on the Euro curve steepener, the CLN on peripheral European sovereigns, and borrowing in JPY to invest in USD are attached below if you would like more information on those trades.

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## Market Update

- § Senate agreement will reopen and fund the government until January 15 and will raise the debt limit until February 7
- § Budget negotiators must wrap up talks by December 13
  - § If lawmakers do not negotiate on the sequester, \$19 billion in automatic cuts will occur on January 15
- § World equity markets have responded tepidly to U.S. debt deal – stocks were mixed in Asia, Europe started the day in negative territory, and U.S. stock futures were little changed (S&P 500, Nasdaq, and Dow all gained more than 1% on Wednesday)
- § Some analysts say Congress is just kicking the can down the road (again); default threat could reemerge in February
  - § Deal seen as stop-gap, which sparked long-term growth concerns that could further delay Fed taper – caused U.S. Treasuries to rally
  - § Joe LaVorgna's updated forecast for Q4 GDP growth is 2.5% yoy
- § S&P forecasts that the government shutdown took 0.6% from Q4 GDP; DB's Torsten Slok estimates the impact was probably only a few tenths of a percent
- § Frank Kelly's take on last-minute debt ceiling resolution:
  - § 81-18 Senate vote shows surprisingly strong bipartisan base
  - § 205-144 in House vote, including 87 Republicans - Proves that Boehner had 100 votes in back pocket (he released some hard-line members so they could save face)
  - § Cautiously optimistic that a comprehensive budget will get done by December 15 deadline
    - § If they can pass a budget, February debt ceiling becomes a non-event because the Fed will be able to issue debt without approval well into May
- § VIX (S&P volatility) has dropped back to 14.52 from Tuesday's recent high of 18.61 (1-year average is 14.95)
  - § Selling volatility no longer as attractive
- § With forwards low, we still like synthetic longs going into year-end

## Tactical Trades

## Single stock ideas

- § MON –  
<https://ger.gm.cib.intranet.db.com/ger/document/pdf/-0900b8c0875896f3.pdf>
  - § Climate Corp acquisition set to drive earnings growth

§ Integrated Farming System (IFS) represents a transformational platform

§ Buy rated; Price target 120 (15% upside from current 104)

§ AAPL -

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§ Strong sales and margins for iPhone 5S and 5C set to drive gross margins

§ New product pipeline appears robust (new iPad, 5 inch iPhone, new Macs)

§ Potential for China mobile deal and/or larger capital return program

§ Buy rated; Price target 575 (15% upside from current 500)

§ TRLA -

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§ Upside potential driven by inventory expansion effort

§ Favor TRLA over Z given under-monetization and valuation

§ Buy rated; Price target 51 (18% upside from current 43.06)

§ INTC -

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§ Delivered better Q3 results and profitability remains solid

§ Profitability and incremental 2014 growth drivers remain underappreciated

§ Buy rated; Price target 26 (10% upside from current 23.54)

§ TJX -

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§ Potential upside in HomeGoods; analyst day on October 22nd is possible catalyst

§ Buy rated; Price target 62 (10% upside from current 56.20)

Puerto Rico Sales Tax Bond

§ Cofina sales tax srs 0% '54 yielding 6.83% based on 10/16 average price of 6.456

§ Recent Moody's downgrade from Aa3 to A2 had more to do with rating discrepancy between sales tax and G.O. bonds than concern about quality of sales tax revenues

Euro curve steepening trade (10s/2s) – See attached presentation

§ Principle-Protected Note – Issuer: JPMorgan, Maturity: 5 years, Underlying: EUR Swap Annual, Spread: EUR 10 year swap rate – EUR 2 year swap rate, Coupon: 4.75% per annum x n/N

§ N = # of days in coupon period, n = # of days where spread is between upper & lower barriers

§ Upper barrier: 2.5%, Lower barrier: 1.5% (equal to current

spot

spread), Commission: 1%

§ Unique monetary environment causes curve steepening during an economic recovery (e.g. Treasury curve has steepened over the

- last six months)
- § 5 year forward spread is 65 bps for 10s/2s – Market is pricing in curve flattening
- § In addition to taking a curve steepening position, this note effectively sells volatility, which is currently high on long-term rates

#### EURUSD puts

- § 6-month ATM (1.3664) EUR put costs 218 bps; break-even is 1.3382
- § AWM GIC year-end EUR/USD forecast is 1.31

#### Longer-Term Themes

Rates/Yield: Take advantage of recent rally (10 year Treasury yield has dropped from 2.96% on 9/10 to 2.67% on 10/16) ahead of expectations for rising rate environment.

- § Interest rate hedging
  - § 5 year swap rate is 1.51%; historical 10-year average is 3.15%
  - § Interest rate swap still makes sense given AWM GIC 12-month Treasury forecast of 3.70% and 5 year forward rate has come down 40 bps from September highs (current: 4.24%)
- § Floating rate investments
  - § DWS Floating Rate Fund (Ticker: DFRTX)
    - § YTD return of 3.81% vs. index return of 0.79%; 12 month yield: 4.69%
    - § Duration is essentially zero due to LIBOR funding for senior bank loans

Global Equities: Bullish (global) equities. Global Markets forecasts S&P to hit 1750 by year-end, driven by increased earnings growth and a recovery in capex. S&P 500 volatility has dropped back to normal levels (VIX closed at 14.71 on 10/16; 1-year average is 14.95) on reports of a fast-tracked Washington debt deal.

- § Emerging Market absolute return note
  - § EEM 2yr twin win, 72% barrier (observed daily at market close),
    - 25% cap; priced on 10/16/13
    - § Have 2mm lead order; will close if EM volatility increases to improve terms
    - § EEM is down 6.92% YTD – good entry point
    - § Global Markets expects recent emerging markets slowdown to reverse given positive outlook in developed economies and predicted soft landing for China but downside risk exists if Fed reverses QE too quickly
    - § Barrier ~31 has not been breached since 2009
    - § EM currency weakness should continue with Fed set to taper in late 2013 or early 2014 – might want to hedge

currency risk

- § CROCI (Cash Return on Capital Invested) U.S. Dividends Structured Note
  - § 3-Year Delta-1, Total Return Note (less adjustment factor of 1.5% per annum) on CROCI U.S. Dividends (DBUSSDUT); DB AG is issuer (A2/A+)
    - § Fees: 1% up-front with 1% trailer in Years 2 and 3
    - § Puttable daily with 0.50% repurchase fee and annually without fee
    - § We would need to create at least 1mm in demand to close
  - § Has outperformed S&P by 3.4% YTD (as of 8/30/13) and 7.8% annualized over last 5 years
- § Short Euro, Long SPX
  - § Dual Digital Option Format – Maturity: 6 months, Offer: 18% of payout
    - § If SPX is greater than 102% of initial value and the EURUSD is below 98% of initial value, the payout is

~5.5x

- initial investment. Otherwise, payout is zero
- § Note Format – Issuer: TBD, Maturity: 6 months, Notional: TBD
  - § If SPX is greater than 102% of initial value and the EURUSD is below 98% of initial value, the payout is 110% of notional. Otherwise, payout is 97.5%
- § References: SPX = 1709, EURUSD = 1.3500
- § AWM GIC 12-month S&P 500 forecast is 1810 (6% upside from reference level) on the back of projected earnings growth
- § AWM GIC 12-month EUR/USD forecast is 1.25 (7.4% downside from reference level) due to projected USD strength stemming from relatively high economic growth and future monetary tightening

Municipals: Opportunistic entry points in municipal debt based on recent Detroit default, Puerto Rico credit concerns and general municipal market dislocation, with 100%+ ratios over Treasuries

§ Municipal Total Return Swaps

- § Good investment due to steepness of yield curve and municipal cheapness (many are trading at over 100% to Treasuries)
- § Client puts up 10 to 30% margin, pays SIFMA plus a spread, and receives 100% of income, 85% of appreciation, and 100% of depreciation
  - § Margin and spread depend on client's credit worthiness and bond characteristics
  - § SIFMA is a 7-day market index comprised of municipal variable rate debt obligations
- § Attractive to buyers who are interested in municipals without triple tax-free income and are comfortable with leverage and

DB

credit risk

Currencies: Long-term bullish USD due to relatively high growth rate in U.S. and the likelihood that the Fed will be the first developed market central bank to tighten monetary policy. Bearish EURUSD, USDJPY, GBPUSD.

§ Borrow in JPY, invest in USD – See attached presentation

- +75bps,
  - § Cross-currency swap where client receives 3 month Libor
  - pays fixed JPY rate of 0.65%, and JPY/USD exchange rate is fixed
    - § Client uses the proceeds of USD loan to invest in USD bond portfolio – Cost of funds becomes the JPY fixed rate, which generates a leveraged positive carry
    - § Client bears the risk of JPY appreciating against USD
      - § AWM GIC USD/JPY 12-month forecast is 114 (15.4% relative depreciation in JPY from current 98.81)

European Recovery: The combination of external demand and reduced fiscal austerity should promote slow but positive GDP growth.

- § Credit-Linked Note on European “Distressed” Nations – See attached presentation
  - § Issuer: TBD, Currency: USD, Maturity: 5 years, Underlying: Portugal, Spain, Italy, and Ireland, Coupon: 3 month LIBOR + 400 bps
    - § Each credit event will cause a reduction on the note’s notional of 25%, which will also affect subsequent payments and the redemption at maturity. If all four countries default, the redemption value will be zero
      - § Peripheral sovereign spreads are still relatively wide
        - § iTraxx Main, Europe’s IG Index, is trading at 87 bps; the X-Over (High Yield) is trading at 352 bps
        - § The average 5 year spread of these 4 countries is 228 bps
      - § With the European economic recovery under way, the risk that the peripheral countries default is increasingly lower
- § DB X-Trackers – Exposure to European recovery without currency risk (we are long-term bullish USD)
  - § Be aware of liquidity risk, especially for funds with a short track record
  - § MSCI Germany Hedged Equity Fund (DBGR) – Expense ratio: 0.5%, 1-year return: 11.04%
  - § MSCI EAFE Hedged Equity Fund (DBEF) – Expense ratio: 0.35%, 1-year return: 29.76%
  - § MSCI Europe Hedge Equity Fund (DBEU) – Expense ratio: 0.45%, Inception: 10/1/13
- § Blackstone Dislocation Opportunities Fund
  - § Call on October 22 will provide more information

Real Estate/RE Linked: Price upside because of low U.S. supply (limited construction over the last four years), plus low correlation to other asset classes and strong inflation hedge. Monetizing cyclical and opportunistic dislocations.

- § RREEF Property Trust (RTP)

REITs § Up to 80% direct U.S. real estate, 15% in publicly-traded  
(liquidity), 5% in real estate debt  
§ New Bond Street (KCC Only)

Tail Risk Hedging: Protect against U.S. government default concerns – This is no longer a pressing theme because an agreement was reached to raise the debt ceiling until February 7. This theme can be re-explored in February.

§ Sell VIX calls to buy crash protection in gold, the Euro Stoxx 50, and U.S. financials

§

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§ Option premiums on VIX and GLD fell on 10/16 (Nov-13 VIX 22 call fell 0.56, Nov-13 GLD 108 put fell 0.21) in the wake of Washington debt deal announcement. Concerns over a U.S.

default

(however remote the possibility) dissipated, causing a drop in volatility.

§ Original trade with updated pricing

§ Sell Nov-13 VIX 22 calls for 0.55 (current: 14.71, 6-month closing high: 20.49)

§ Buy Nov-13 GLD 108 puts for 0.16 (current: 123.54)

§ Buy Nov-13 FEZ 31 puts for 0.15 (current: 40.02)

§ Buy Nov-13 XLF 17 puts for 0.03 (current: 20.68)

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Kind regards,  
Tim Shields

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Tim Shields  
Analyst

Deutsche Bank Trust Company Americas  
Deutsche Asset & Wealth Management  
345 Park Avenue  
New York, NY, 10154  
Tel. + [REDACTED]  
Mobile [REDACTED]  
Email [REDACTED]

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