Aquantum Pegasus Index

Absolute returns through a transparent, market-neutral commodity futures trading strategy

Make it happen™

RBS™
The Royal Bank of Scotland

"The Aquantum Pegasus Index allows investors to access a systematic, commodity market-neutral trading strategy which in the past would have generated positive returns each and every year"

Thomas Morrow

aquantum ALGORITHMIC

Overview

The Aquantum Pegasus Index (the "Index") is a commodity market-neutral index linked to the performance of an advanced quantitative futures trading strategy. The Index is denominated in USD and published at least once per day.

The Index references a diversified portfolio of commodity futures from various sectors including: energy, metals, agriculture and livestock. Based on two complimentary systematic trading programs, simultaneous long and short positions are established in certain futures contracts with the aim of benefiting from convenience yields which are present in commodity markets.

Based on simulated past performance since August 1997, the Index has generated returns in excess of 20% p.a. with less than 4% p.a. volatility. The correlation of the Index to other asset classes is low, making it an excellent addition to an investor's portfolio.

Index highlights

- The Index aims to deliver absolute returns with a low level of volatility.
- Based on an extensive 12-year empirical analysis, the Index has recorded positive returns every calendar year.
- The Index references a market-neutral strategy, meaning its performance should not depend on the direction of the commodities to which the Index is linked.
- It is uncorrelated to other benchmark asset classes and therefore an ideal portfolio diversification tool.
- The Index is fully transparent, rules-based and liquid.
- Based on simulated past performance since August 1997, the Index would have
  - realized less than 3.9% annualized volatility,
  - achieved a positive performance in 95.8% of all months with a worst daily return of only -1.55%,
  - had a maximum loss (drawdown) from a prior high of -2.5%,
  - generated an average monthly performance of 1.64%.

Note: This information refers to historical data commencing 7 August 1997. Past performance cannot be relied upon as an indicator for future performance. The performance information is based on the gross performance of the Aquantum Pegasus Total Return Index (USD) ; the performance will be lower when fees, commissions or other charges are deducted.

aquantum. alternative investments redefined.

The Index creator

Aquantum is a specialist provider able to develop absolute return strategies across all asset classes including equities, foreign exchange, interest rates and commodities. Its principal, Thomas Morrow, who resides in Oxford, England, has over 20 years experience in banking and finance, managing systematic trading strategies at major investment banks and one of the world's largest and most highly regarded hedge funds.

Utilizing advanced mathematical and statistical techniques, Aquantum develops innovative financial market trading strategies that aim to generate consistent positive returns with limited volatility. The company's name represents its philosophy, with Aquantum being derived from the words "Aqua", symbolizing transparency and liquidity, and "Quantum", symbolizing cutting-edge mathematical modeling and quantitative research.

Originally from London, Thomas Morrow emigrated to Australia after graduating in Pure and Applied Mathematics. He joined Bankers Trust in the late 1980s and started to develop algorithmic trading systems while working in the fixed income and structured derivatives groups. During this time he developed systematic models which traded more than 80 different futures markets. In 1999, Thomas Morrow joined Deutsche Bank as a systematic trader and continued to develop models across many different asset classes. He moved back to the UK in 2007 to join Winton Capital Management, one of the world's premier algorithmic trading hedge funds. In 2009, Thomas Morrow decided to create Aquantum.

The hedge provider

RBS Sempra Energy Trading LLC ("Sempra") is one of the world's largest physical commodity trading companies. In addition to the acquisition of ABN AMRO in October 2007, The Royal Bank of Scotland ("RBS") acquired Sempra Commodities in April 2008. The combined RBS organisation brings together a leading commodity trading business and a strong global bank to create one of the most comprehensive commodity franchises worldwide. Sempra acts as the hedging counterparty with respect to securities linked to the Index.

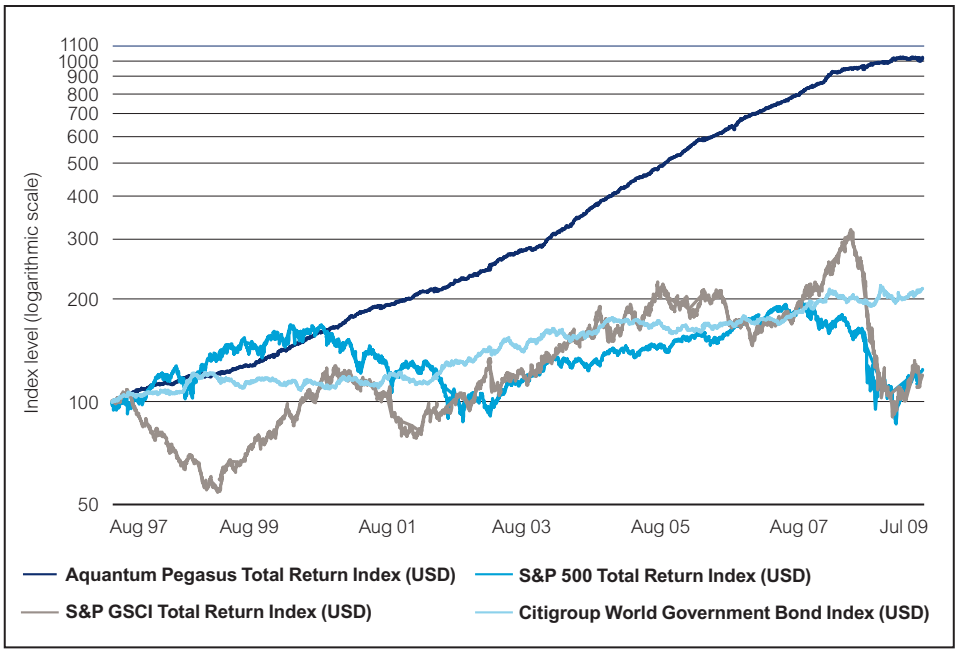
Reasons to invest

The Aquantum Pegasus Index allows investors to access an innovative, commodity market-neutral trading strategy which in the past would have generated attractive returns with a very low level of volatility. In addition, as demonstrated by historical analysis, the returns of the Aquantum Pegasus Index would have exhibited low or even negative correlation to the returns of other asset classes, for instance equities or bonds. Therefore, the Index would have been an ideal instrument to increase the risk-return profile of an investor's portfolio. Moreover, since the Aquantum Pegasus Index is a commodity market-neutral index, its returns, tend to be much less volatile than those of a long-only investment in commodities, which is an attractive feature especially during times of economic turmoil.

Unique features of commodity markets

Based on empirical analysis, the Index would have generated a positive performance in 95.8% of all months since August 1997.

Historical performance of the Aquantum Pegasus Total Return Index vs key benchmark indices



Source: RBS, Bloomberg; June 2009.

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Commodities – becoming an ever more interesting asset class

As investors sought to diversify their portfolios away from fixed income and equity investments, commodity investing rapidly grew in popularity over recent years. During times of sustained macro economic growth, spurred by the escalating demand from emerging economies like China, commodity investments tended to be of a bullish nature where investor returns were linked to price appreciation. However, commodity investments, like equity investments, tend to be highly cyclical and can result in large losses for investors. Additionally, long-only commodity investments tend to be highly volatile.

Versions of the Aquantum Pegasus Index

The Index is available in both Total Return and Excess Return versions and can be seen on Bloomberg.

Aquantum Pegasus Total Return Index (USD): AQUAPEGT Index <GO>

Aquantum Pegasus Excess Return Index (USD): AQUAPEGE Index <GO>

Aquantum's Bloomberg page: AQTM <GO>

Investing in commodities

Storing commodities is generally expensive and few investors have the required facilities to buy and hold corn, crude oil or natural gas, for example. As a result, it is not usually the physical commodity itself that is bought by investors, but almost always commodity futures contracts. Futures are standardized, exchange traded contracts which oblige the buyer (seller) to take (make) delivery of a set quantity and quality of a specified underlying commodity at an agreed price on a fixed date in the future.

For the vast majority of investors, it is much more practical to invest in commodity futures rather than physical commodities. This means that the performance of such an investment typically depends on the commodity's futures price rather than its spot price. Commodity futures are contracts with fixed expiry dates and require the payment of margins against the changing value of the futures contracts. In order to continue a longer-term commodity investment, commodity futures require "rolling", meaning that the expiring contract is sold while a contract with an expiry date still in the future is bought.

Commodity indices remove the burden of rolling futures contracts for investors. Essentially, a commodity index references the prices of certain futures contracts and can be long-only in nature (notionally comprising of long futures positions) or reflect more interesting trading strategies, like the Aquantum Pegasus Index which, as described later, takes simultaneous long and short positions in certain contracts aiming to produce stable positive returns.

Market-neutral commodity trading

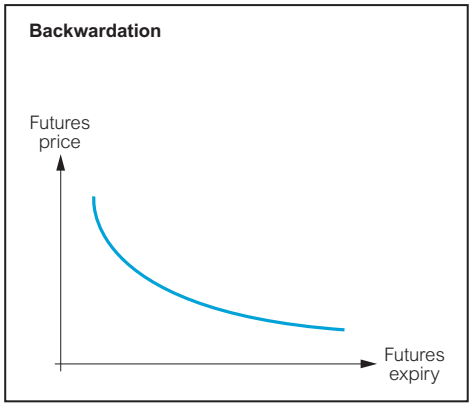
Commodity markets have some unique features that are not applicable to other financial markets. Commodities are consumable, either directly (e.g. wheat, sugar, coffee, live cattle) or indirectly when input into a production process (e.g. oil, natural gas, copper, nickel). Market-neutral commodity trading, for a given underlying commodity, occurs when a long position in one futures contract is offset by a short position in another futures contract with a different expiry date. In such case, the position is unlikely to be strongly impacted by price changes in the spot market, but instead exposed to the relative price moves between the different expiries.

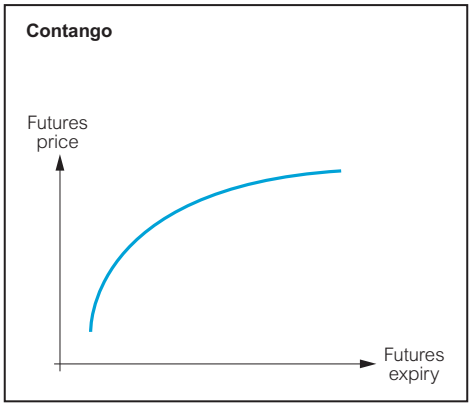
The forward price curve

The futures curve (or forward price curve) shows the prices of futures contracts for a given commodity that expire at different points in time in the future. Commodity futures prices are influenced by spot prices, interest rates, storage costs including insurance premiums, convenience yields and supply and demand. Two situations can occur.

Backwardation occurs when near term contracts are more expensive than longer-dated contracts, for the same underlying commodity. This scenario is generally the result of physical supply shortages. As demand exceeds supply, prices in the spot market increase. Producers are inclined to increase production and clear out stored inventory as the expected margin of selling in the spot market is high. To secure such margins for the future, producers start selling forward today.

Contango occurs when near term contracts are cheaper than longer-dated contracts, for the same underlying commodity. In most cases, contango scenarios are caused by the physical oversupply of a certain commodity. Oversupplies will depress spot prices and, as a consequence, producers will commence storing the commodity (and wait for the price to increase again in order to sell for a higher margin) and/or stop producing it. As the market is oversupplied and market participants are unwilling to purchase all the produce today, consumers start buying the commodity forward.





Commodity futures

Contract features

- Traded on a regulated exchange
- Standardized terms and conditions
- Require initial margin and subsequent (maintenance) margins
- Each contract has a pre-defined expiry date
- Positions in expiring contracts have to be 'rolled' into a longer dated contract
- Can require either cash or physical settlement

What are managed futures?

Managed futures strategies are run by professional investment managers, commonly known as Commodity Trading Advisors (CTAs). CTAs may run fully systematic trading systems (like Aquantum) or use discretionary investment methods

Benefits

- Usually uncorrelated or negatively correlated to other asset classes
- Able to enhance the risk-return profile of an investor's portfolio through additional diversification
- Can produce positive returns in rising and falling markets as CTA managers can take both long and short positions in global futures markets (commodities, currencies, equities etc.)

Contango and backwardation

Rolling futures

All futures contracts have fixed expiry dates. Therefore, to invest in commodities over the long term, and to avoid having to take (provide) physical delivery when a long (short) contract expires, futures positions need to be closed before they expire. To continue the desired exposure in the same commodity, an investor must buy a futures contract with a longer term when he exits the expiring position. This process is known as "rolling". When futures are rolled, the investment amount in the futures contract which is about to expire is generally rolled over into the futures contract that is scheduled to expire next. As shown by the hypothetical futures curves on the previous page, futures contracts with different expiry dates will usually trade at different price levels. As a result, rolling will generally impact the performance of an investment in commodity futures. Such impact may be positive if the futures curve is in backwardation (selling the more expensive near dated contract and buying the cheaper longer dated contract) or negative if the futures curve is in contango (selling the cheaper near dated contract and buying the more expensive longer dated contract).

Spot return, excess return and total return

Spot return is the return that would be achieved through buying, storing and later selling a physical commodity. Excess returns relate to returns earned through trading futures contracts. Investors who purchase futures contracts are not required to make a principal investment which covers the total market value of the contract, but only have to make a margin payment. Following the futures transaction, investors will earn interest on the "margin" and retain the remainder of their notional amount which is available to also earn interest. This is known as an "excess return" because it is earned in excess of the returns which investors can achieve by retaining and using their principal amount. Total return is the return which adds all interest earned to the excess return.

Spot return — Measures the return in the futures contract with the closest expiry date

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Roll return — Measures the return that arises from "rolling" futures contracts

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Excess return + **Interest** = **Total return**

Measures the return of a rolling futures position

Means the interest which is earned on the notional value of the investment

Convenience yield

Convenience yield is the value which market participants attribute to the physical ownership of a particular commodity. When the market is prepared to pay a premium for immediate physical ownership rather than future physical ownership, the convenience yield is positive. Otherwise, it is negative. Where backwardation exists (near dated futures contracts trade at higher prices than longer-dated contracts), the convenience yield is positive. The market continually assesses the value of physically possessing a commodity depending on present and expected supply and demand, the current level of interest rates as well as cost and durability of storage. Therefore, convenience yields have a large part to play in determining whether a commodity forward curve trades in backwardation or contango.

Backwardation

occurs when near term contracts are more expensive than long term contracts

is caused by physical ownership having a higher value than future ownership

is generally the result of scarce supply and/or substantial demand

means that being able to utilize a given commodity immediately exceeds associated interest and storage costs

Contango

occurs when near term contracts are cheaper than long term contracts

is caused by physical ownership having less value than future ownership

is generally the result of oversupply and/or weak demand

means that the convenience arises from not having to store a certain commodity (the convenience yield to physically own the commodity is zero or negative)

The Index follows a systematic, transparent trading strategy designed to produce absolute returns using only highly liquid futures contracts

The Aquantum Pegasus Index – a systematic trading strategy

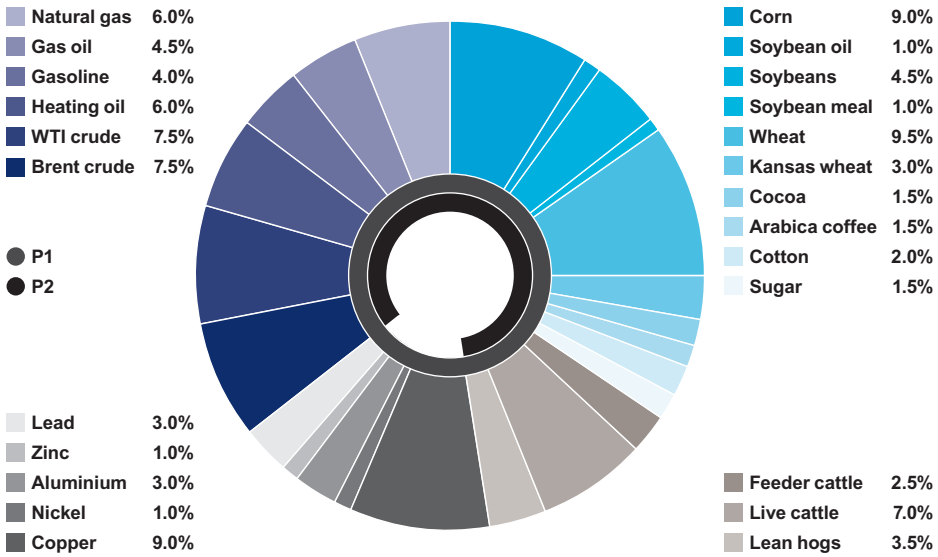
The Aquantum Pegasus Index systematically takes long and short positions in selected commodity futures, aiming to profit from relative changes between the prices of futures contracts with different maturities, for the same underlying commodity. This is sometimes referred to as 'calendar spread trading'. The Index is a leveraged index; for every 1 USD invested, the Index will reference short positions with a total notional of 3.5 USD as well as long positions with a total notional of 3.5 USD.

Two systematic trading programs are used in conjunction. Each month, Program-1 ("P1") takes long and short positions in all commodities contained in the Index and aims to generate positive returns from a sustained extraction of the commodity convenience yield. Program-2 ("P2") takes positions in certain commodities at certain times of the year depending on the availability and periodicity of futures contracts.*

P2 is scheduled to buy the spot month contract, which is the first contract on the futures curve. Simultaneously, P2 is set up to sell the contract which expires immediately after the spot month contract. P2 positions will only be traded if a spot month contract is available for the commodity in question. P1 is scheduled to sell the same contract as P2 and will buy the next contract on the futures curve.

**Unlike equity markets where futures contracts have regular (e.g. monthly or quarterly expiry dates), commodity futures change periodicity depending on seasonal factors which relate to, for example, summer and winter in energy markets, or harvest cycles in agricultural markets. P1 and P2 operate in tandem aiming to provide stable and robust returns for the Index with all positions being rebalanced on a monthly basis.*

Index composition



Diversification

Diversification is achieved by using two complimentary trading strategies, P1 and P2, across a variety of commodity markets. As of 30 June 2009, 24 different commodity futures are included from a variety of different commodity sectors including: agriculture, livestock, metals and energy. Weights in individual commodities are restricted to ensure diversification and monthly rebalancing resets individual weights ensuring that diversification remains intact.

Source: RBS; June 2009.

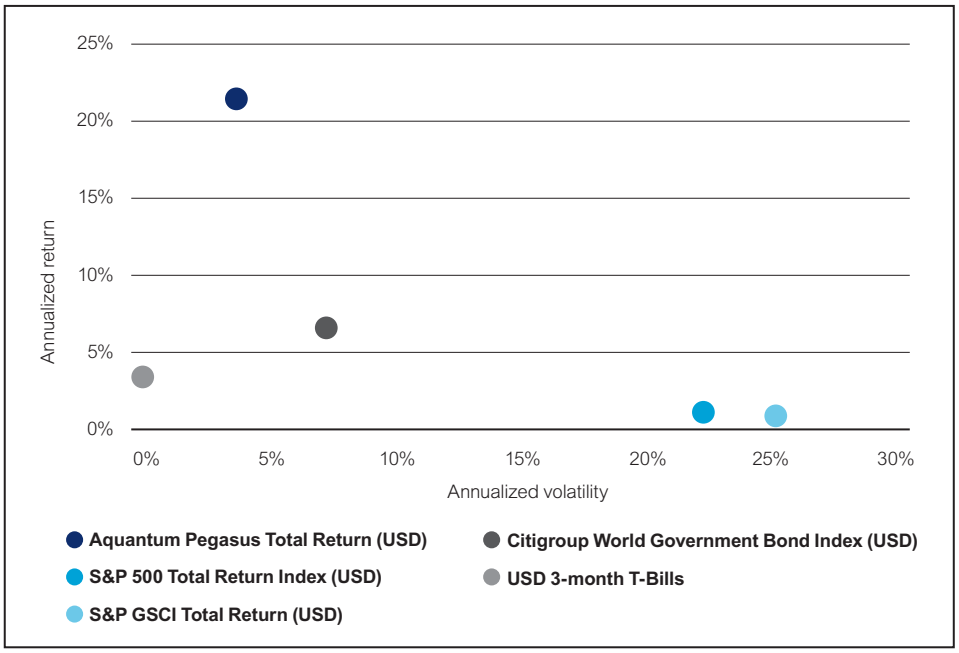
Historical performance

Historical performance – analysis

This section compares the Aquantum Pegasus Total Return Index (USD) to the S&P 500 Total Return Index (USD), the S&P GSCI Total Return Index (USD), the Citigroup World Government Bond Index (USD) and USD 3-month T-Bills.

Comparative risk-return profiles

Historically, the Aquantum Pegasus Total Return Index (USD) would have delivered superior returns with lower volatility when compared to equities, bonds or other commodity indices.



Source: RBS, Bloomberg; June 2009.

Note: The historical performance of the Aquatum Pegasus Total Return Index (USD) in the chart above is calculated based on backtesting and using historical data from the period of 7 August 1997 to 30 June 2009, while the data for other indices are taken from Bloomberg. The chart does not incorporate fees, costs or other charges, which will result in the actual performance of any securities linked to the Index underperforming the gross Index performance shown above. Past returns are not indicative of the future performance of the indices.

Historical performance – overview

The Aquantum Pegasus Total Return Index (USD), in the past, has been able to produce high returns with a low level of volatility. This compares favorably to the S&P 500 Total Return Index (USD) and the S&P GSCI Total Return Index (USD).

	Aquantum Pegasus	S&P 500	S&P GSCI
Annual return	21.43%	1.06%	0.86%
Annual volatility	3.81%	21.94%	24.72%
Return/risk	5.62	0.05	0.03
Worst day	-1.55%	-9.46%	-9.17%
Maximum drawdown	-2.50%	-55.25%	-71.40%
Profitable calendar years	100%	63.64%	63.64%
Best calendar year	40.26%	28.68%	49.74%
Worst calendar year	9.46%	-37.00%	-46.49%
Profitable calendar months	95.80%	58.74%	53.15%
Best calendar month	5.06%	9.78%	19.67%
Worst calendar month	-2.02%	-16.79%	-28.20%

Source: RBS, Bloomberg; June 2009.

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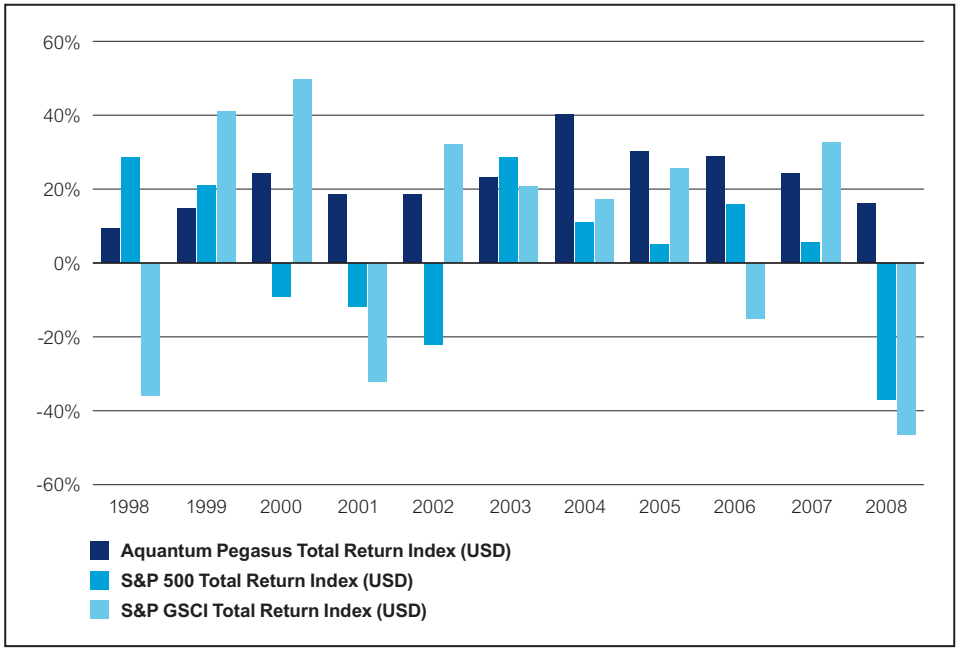
Calendar year returns



Analysis of simulated returns from 1997 onwards shows that the Aquantum Pegasus Total Return Index (USD) would have been profitable every year. This compares favorably to the S&P 500 Total Return Index (USD) and the S&P GSCI Total Return Index (USD) which have both experienced large declines in a number of years. It can also be seen that the Aquantum Pegasus Total Return Index (USD) has generated positive returns in many years, including 2008, during which both the S&P 500 Total Return Index (USD) and the S&P GSCI Total Return Index (USD) declined.

Source: RBS, Bloomberg; June 2009.

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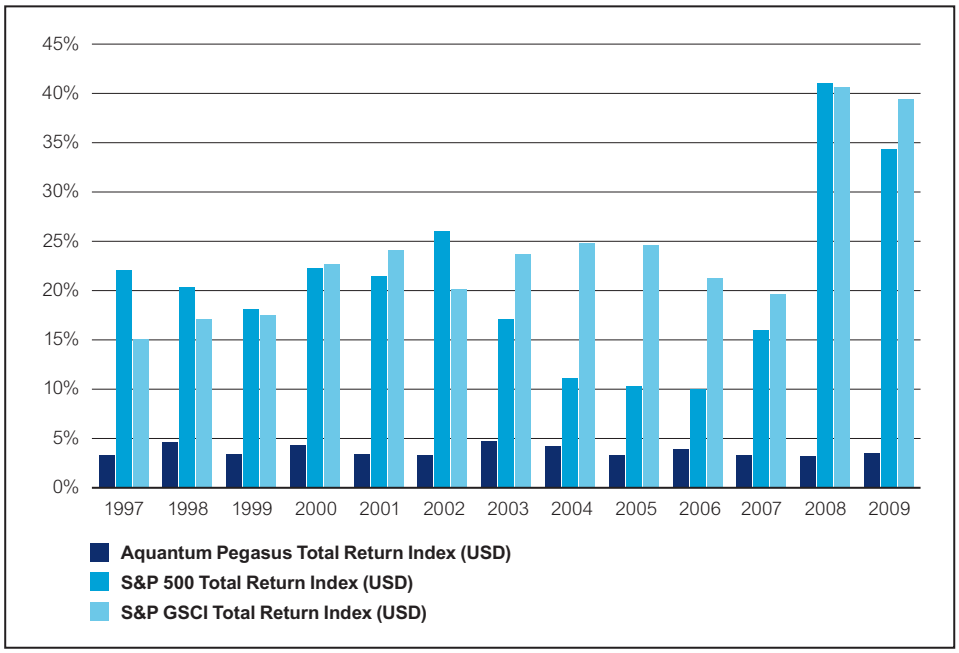
Calendar year volatility



Based on simulated past peformance, volatility for the Index has averaged 3.9% p.a. since 1997. The highest annualized volatility recorded by the Index was 4.72% in 2003. In recent years, when the S&P 500 Total Return Index (USD) and the S&P GSCI Total Return Index (USD) both realized in excess of 40% volatility per year, the volatility of the Aquantum Pegasus Total Return Index (USD) volatility remained below 4% p.a.

Source: RBS, Bloomberg; June 2009.

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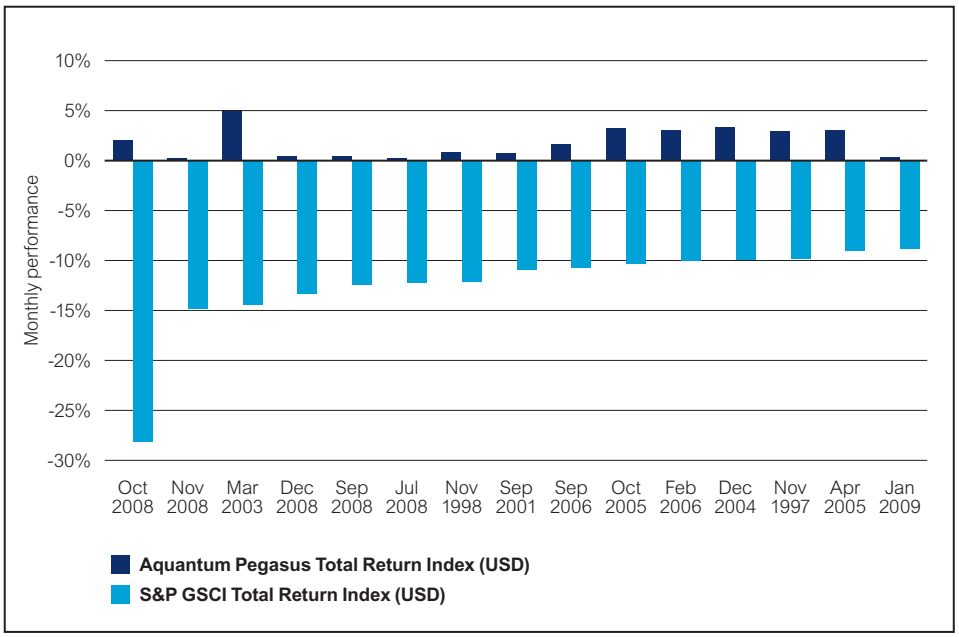
Consistent returns and low volatility

Robust and consistent performance regardless of market conditions

This chart ranks the worst 15 monthly losses for the S&P GSCI Index and shows how the Aquantum Pegasus Index would have performed in each of these months. Since the Aquantum Pegasus Index is designed to be commodity market-neutral, its past returns have been stable and robust even during times of extreme turmoil in the commodity markets. In many cases the Aquantum Pegasus Index was able to produce positive returns when the S&P GSCI Index recorded large losses.



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Monthly returns – Aquantum Pegasus Total Return Index (USD)

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Year
2009	0.32%	1.51%	0.76%	-0.21%	0.41%	-0.65%	-	-	-	-	-	-	2.15%
2008	1.19%	3.30%	4.02%	-0.33%	1.75%	0.66%	0.23%	1.18%	0.40%	2.04%	0.26%	0.40%	16.08%
2007	1.40%	2.25%	1.49%	1.94%	1.27%	1.84%	0.88%	3.00%	1.10%	2.91%	2.20%	1.74%	24.35%
2006	3.21%	3.00%	3.13%	0.85%	1.54%	1.16%	1.48%	2.35%	1.66%	2.92%	2.35%	1.88%	28.69%
2005	1.32%	2.41%	2.84%	3.03%	0.68%	1.93%	2.56%	1.94%	3.19%	3.23%	1.68%	1.77%	30.04%
2004	4.39%	2.10%	2.57%	2.62%	2.76%	2.98%	2.49%	3.41%	3.39%	2.49%	1.76%	3.38%	40.26%
2003	1.27%	0.46%	5.06%	3.31%	1.43%	1.69%	0.62%	1.38%	1.76%	-0.15%	1.64%	2.54%	23.03%
2002	2.71%	1.82%	0.23%	1.07%	0.34%	1.65%	1.36%	3.42%	0.70%	0.62%	1.77%	1.53%	18.58%
2001	3.81%	1.05%	3.02%	0.55%	1.71%	1.13%	0.08%	1.97%	0.77%	1.22%	0.76%	1.16%	18.57%
2000	4.27%	0.48%	1.91%	2.30%	1.36%	1.98%	2.10%	1.50%	0.96%	2.19%	1.47%	1.42%	24.25%
1999	0.73%	1.33%	1.24%	0.49%	1.47%	1.48%	0.95%	0.37%	1.81%	1.64%	2.02%	0.35%	14.77%
1998	0.71%	1.97%	0.52%	0.74%	1.05%	-0.65%	2.04%	1.78%	0.92%	1.24%	0.83%	-2.02%	9.46%
1997	-	-	-	-	-	-	-	0.92%	2.12%	0.73%	2.96%	1.16%	8.12%

Source: RBS, Bloomberg; June 2009.

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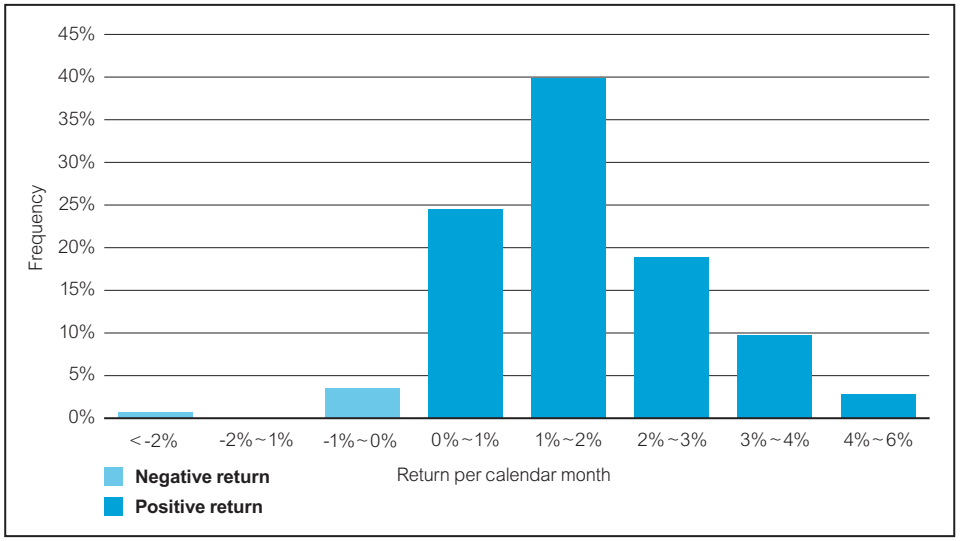
Distribution of monthly returns

Historically, for the Aquantum Pegasus Total Return Index (USD), 95.80% of all monthly returns have been positive. In 39.86% of all cases the Index has generated a return between 1% and 2% per calendar month. The average monthly return is 1.64%.



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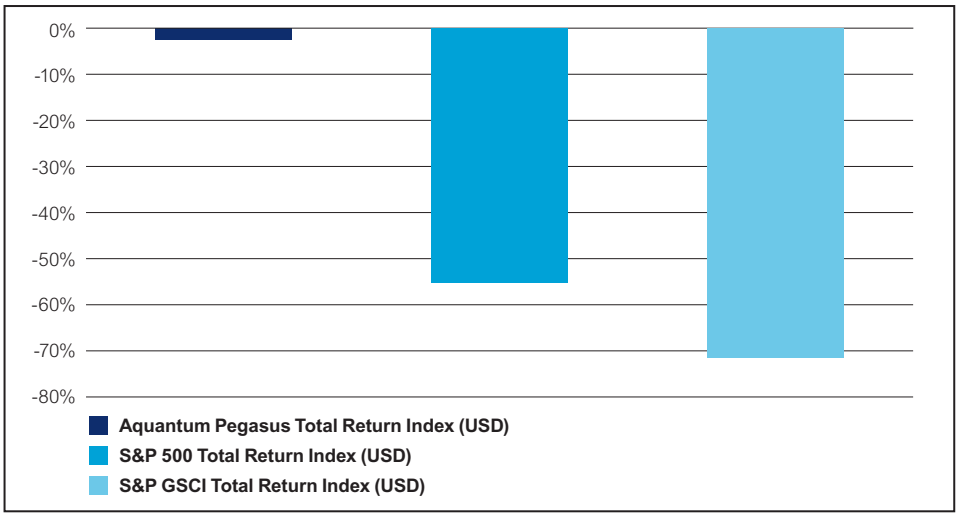
Comparison of drawdowns

For the Aquantum Pegasus Total Return Index (USD) the worst drawdown from a previous high was -2.5%. Subsequently, it took the Index 87 business days to recover from that loss. On average, upon the occurrence of a drawdown event, it takes the Index 3.66 business days to recover. This compares favorably to both the S&P 500 Total Return Index and the S&P GSCI Total Return Index which recorded drawdowns of -55.25% and -71.40%, respectively.



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Key facts

Index components: listed commodity futures contracts.

Positions: simultaneously long and short in contracts with different expiry dates for each commodity in the Index.

Position selection: fully systematic, according to two independent programs.

Liquidity: the underlying futures contracts are very liquid and traded on some of the world's major exchanges including the Chicago Board of Trade and London Metal Exchange.

Transparency: Index calculations are transparent and rule-based.

Market-neutrality: The Index is designed to be market-neutral and aims to generate positive performance regardless of the direction of the individual Index components. To do this the Index incorporates short positions as well as long positions, which could cause the value of the Index to potentially fall even if any or all of the Index components rise.

Leverage: Due to the use of futures contracts and the notional use of leverage, changes in the value of the Index may be amplified (either positively or negatively). However, a leveraged long or short position taken in one contract expiry will be coupled with an opposite direction position in the same contract with a different expiry which substantially mitigates any leverage risk to any underlying commodity price.

Specific risks: The performance of the Index arises from the Index creator following a fixed rule systematic program developed by Aquantum Pegasus Index. Neither Aquantum Pegasus Index nor any other entity guarantee that the stated aims or objectives will be met or evaluate the likelihood of such aims being met. This document seeks only to describe the Index and does not seek to describe any securities, or the risks of such securities, that may be linked to the Index. The full Index methodology is available to investors, on request.

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