Aventicum SPC European Alpha Fund SP – Class C EUR

For qualified investors only • August 2015

AVENTICUM CAPITAL MANAGEMENT

## Investment Policy

The objective of the Segregated Portfolio is to achieve attractive risk adjusted returns in all market environments through a Long Short Equity Strategy which primarily focuses on European equities.

The investment strategy of the Segregated Portfolio follows a bottom up fundamental approach and focuses on alpha generation rather than beta exposure. It aims to keep to a minimum the correlation with the underlying equity markets and focuses on capital preservation through a rigorous and disciplined risk management process.

### Historical Monthly Performance in %[1]

| Year | Jan | Feb | Mar | Apr | May | Jun | Jul | Aug | Sep | Oct | Nov | Dec | YTD |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **2015** | 3.09% | 3.79% | 2.09% | 2.21% | 0.61% | -2.44% | 3.02% | 0.35% | - | - | - | - | 13.30% |
| **2014** | - | - | - | - | - | - 2.79% | 0.65% | -0.39% | 1.21% | -1.18% | 1.23% | -1.60% | -2.91% |

### Top 5 Long Positions

| | |
|---|---|
| Elisa | 8.18% |
| Coach | 7.60% |
| Lagardère | 7.38% |
| Ericsson | 6.62% |
| Adidas | 6.42% |

### Portfolio Positioning

| | |
|---|---|
| Long Exposure | 149.08% |
| Short Exposure | 115.16% |
| Gross Exposure | 264.24% |
| Net Exposure | 33.92% |
| Beta Adjusted Net Exposure | 34.99% |
| Ex-Ante Daily VaR (99% 1-year) | 1.59% |
| Number of Long Positions | 31 |
| Number of Short Positions | 30 |

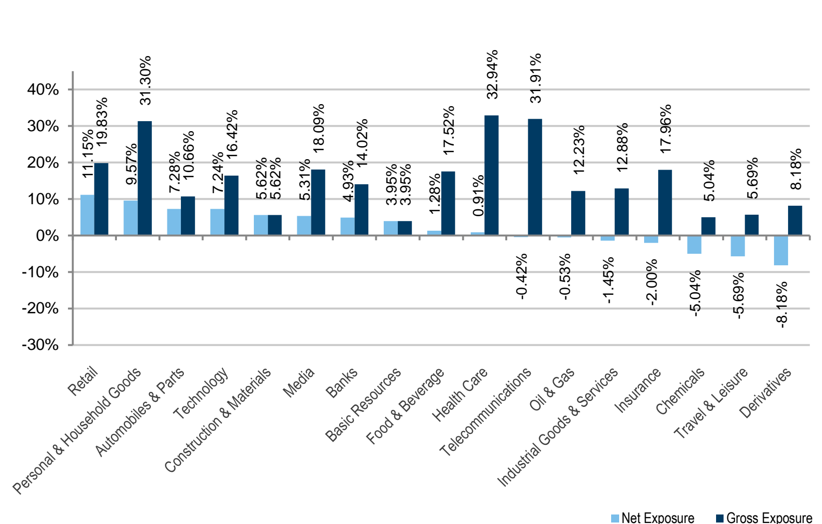
### Fund Return Statistics

| | |
|---|---|
| Return Since Inception | 10.00% |
| Annualised Return Since Inception | 7.92% |
| YTD Return | 13.30% |
| 3 month Rolling Return | 0.86% |
| 6 month Rolling Return | 5.89% |
| 1 Year Rolling Return | 12.87% |
| Highest Month Return Since Inception | 3.79% |
| Lowest Month Return Since Inception | -2.79% |
| % Of Positive Month Since Inception | 67% |

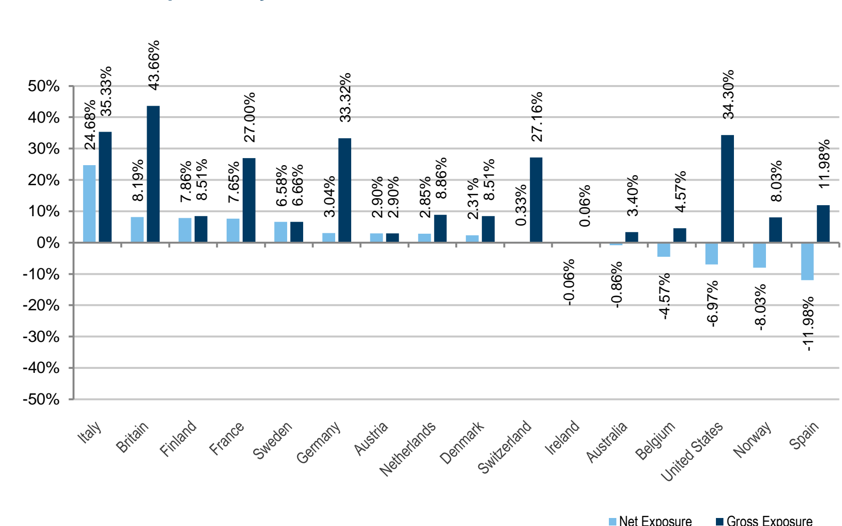
### Fund Risk & Efficiency Statistics

| | |
|---|---|
| Annualised Volatility (3 Yrs.) | - |
| 1 Year Volatility | 6.84% |
| Maximum Drawdown | -2.91% |
| Sharpe Ratio (3 Yrs)* | - |
| Sharpe Ratio (1 Yr)* | 1.88 |
| (3 Yrs) Correlation to MSCI Europe Loc. Index | - |

### Net & Gross Exposure by Sectors




### Net & Gross Exposure by Countries




1) Historical performance indications and financial market scenarios are no reliable indicator for current or future performance. Performance indications do not consider commissions levied at subscription and/or redemption.

*Sharpe Ratio is calculated using the average 1m Euribor over the relevant period

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## Fund Facts

| Fund Facts | | | |
|---|---|---|---|
| **Fund manager** | Aventicum Capital Management (Switzerland) Ltd | Total net assets (EUR) | 151,638,335 |
| **Location** | Geneva | Inception date | 01 Jun 2014 |
| **Portfolio managers** | Riccardo Cavo, Andrea Buda, Barry Kelly | Management fee in % p.a | 1.50 |
| **Legal advisors** | Collas Crill & Charles Adams Ritchie & Duckworth, Lecocq Associate and Bingham McCutchen LLP | Performance fee in % | 20.00 |
| **Fund Administrator** | Credit Suisse Administration Services (Ireland) Ltd | | |
| **Auditor** | KPMG | Unit Class | C |
| **Prime broker** | Credit Suisse, Morgan Stanley | Unit class currency | EUR, USD |
| **Fund domicile** | Cayman Islands | Net Asset Value | 110.00 |
| **Fund currency** | EUR | | |
| **Close of financial year** | 31 Dec | | |

## Market Commentary

Following what was already a very solid year to date performance, we are happy to report the fact that the Aventicum European Alpha Fund also managed to deliver a positive return of +0.35% in August. Given the extreme market conditions, with some of the highest volatility we have witnessed in a number of years, we feel this was a remarkable achievement. The Fund is now up 13.30% since the beginning of the year and has proven its ability to generate alpha over the period whilst maintaining a strong focus on capital protection during turbulent markets.

Global equity markets went into meltdown during the month. The S&P 500 and DAX lost 12% and 17% respectively before partially recovering into the month end. Some of the volatility we observed was reminiscent of the darkest days of 2008. European volatility, as measured by the VSTOXX Index, reached over 45%, the highest levels in over 4 years. Currency markets also experienced extremely high levels of volatility with emerging market currencies depreciating sharply on G10 crosses. While it is difficult to isolate one single catalyst for the vicious sell-off, we believe a number of events combined triggered it:

- The probability of the FED increasing interest rates in September reached a high of 55% (as measured by Fed Funds futures), the highest levels year to date.
- The People’s Bank of China unexpectedly devalued the renminbi by the most in two decades, fuelling fears that China was about to enter the global currency devaluation war.
- Global equities with exposure to China being sold aggressively.
- Ongoing volatility in the Chinese stock market related to concerns on the health of the domestic economy.
- The collapse in the China related commodity complex fuelling fears of deflation.
- Oil prices falling over 20%.
- The resignation of Greek Prime Minister Alexis Tsipras and the announcement of snap elections next month.

These events zapped investor’s confidence, resulting in indiscriminate dumping of stocks. A number of prominent investment banks also cut their global GDP estimates in the wake of the turmoil, mainly due to a more pronounced slowdown in Chinese GDP. In Europe, we saw the “darling” trades of 2015 unwind most of their gains and in some cases erased all the positive performance since the European Central Bank unveiled its quantitative easing programme.

In the latter part of the month China responded to the market turmoil by reducing its benchmark one-year lending rate by 25 basis points to 4.6%. The bank also cut the one-year savings rate and said it would lower the reserve requirement ratio for banks. Markets reacted positively to this news with the Eurostoxx50 rallying to eventually end the month down 9%.

In Europe, the economic data continues to show positive trends. The final readings on second quarter GDP were broadly in-line with expectations and the Markit Composite PMI was ahead of expectations. M3 money supply data released during the month also accelerated in the year to July to 5.3% up from 4.9% in June. Loans to non-financial corporations grew by 0.4% in the year to July representing the first positive figure recorded since May 2012. This development will further reassure the ECB that their policy is beginning to feed through to the wider real economy and support the momentum in the European economic recovery story.

At the portfolio level, we were invested in a total of 61 equity positions across all sectors at the end of August. Exposures changed slightly vs. the previous month, with gross lowered to 264 % and net increased to 34%, in line with the beta adjusted exposure. It’s worth noting that the short term beta, calculated on 125 days, is 8% lower than the “official” beta adjusted exposure, calculated on 375 days, demonstrating an embedded protection in the Fund.

At sector level, Healthcare, Telcos, HPC and Retail had the highest percentage gross exposure. We were net long Retail, HPC and Autos, whilst Travel & Leisure, Chemicals and Insurance were net short.

We availed of the opportunity to close some of our short positions on the back of the significant downturn in the markets. This was the main reason for the increase in net exposure.

The gross exposure reduction was mainly in Media; we also made some changes in terms of market exposure: we neutralized the net long exposure in Telcos, increased the net in Tech and Autos, where we added to our net long exposure, and Travel & Leisure where we reduced our net short exposure by locking in some nice profits.

At the country level, the net short position which we held in Spain was the best contributor during the month. We used the market correction as an opportunity to reduce the position by 5%, to circa 12%, crystalizing some positive performance on the short book. We did something similar in the UK, where we also closed some short positions, in particular in the Media strategy.

China and EM revenues exposure, along with the entire commodity space, suffered significantly as a theme. In contrast, Eurozone and DM consumer exposed companies, together with Italy and Switzerland, were much more resilient.

European Equities, as a result of the pronounced correction were back to low single digit YTD returns at the end of August.

Several sector level barbell strategies contributed to the portfolio’s positive performance, along with downside derivative protection. The long portfolio proved to be very resilient with the main contributions coming from Baxalta, Straumann and Pirelli.

In summary, our alpha generation capabilities via bottom up stock picking and selective country and sector allocation have proved fruitful in the most extreme of market environments. We remain very convinced of the long term potential of this investment philosophy to generate positive returns in all kinds of volatility regimes.

The largest positive contributions from a performance attribution perspective were Healthcare, Travel & Leisure, Industrials and Oils.

At single stock and strategy level there were a number of notable movers throughout the month. We will elaborate on some individual names/themes hereunder in order to attempt to give an overview on our current positioning and strongest convictions.

**William Hill** ceded just over 11% in the month following their H1 results.

While the results certainly had some positives, such as strong underlying earnings growth, and a pretty resilient retail performance, we remain concerned over further potential negative regulatory risks and at William Hill Australia, previously a driver of growth, losing share alarmingly quickly, which going forward will drag on earnings.

We also fear the impact that the Coral / Ladbrokes and Paddy Power / Betfair proposed mergers will have on William Hill, should they get cleared.

Finally, in the last year a new CEO has been appointed, and a new CFO commences duty at the beginning of November. While we don’t doubt their ability or their credentials, we do fear that the management changes could impact operational performance very near term. For us the risks currently outweigh the opportunities.

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**Baxalta**, a long position we have as a result of a recent spin off from Baxter, appreciated by 10% during the month. We have been following the bioscience area (immunoglobulins and haemophilia disease) for a long time and were strongly convinced by the strengthening fundamentals and attractive valuation of the company. They have strong take-over defence in place, but unexpectedly at the start of August, Shire Pharmaceuticals made it public that they had approached the management of Baxalta with an offer to merge with an all share swap at a 30% premium; their offer was rebuffed. Since then Shire's share price has fallen by almost 15% along with the pharma sector, hence the accretion of the deal is much less visible for Shire shareholders, especially since the management of Baxalta have publicly stated that they would engage, but only at a higher price, probably closer to USD 50. We have realised some profits, but remain convinced by our long position. We believe that Shire management, with whom we have spoken directly, are very determined to get hold of the company and are likely to increase the offer. Should the offer be withdrawn we still believe there is compelling upside for Baxalta at current levels.

**WPP** reported a broadly in-line set of H1 results, which highlighted a slowing revenue growth trend in Q2 vs Q1. While this doesn't unduly concern us, we remain concerned that there is a risk to FY guidance should their faster growing markets, such as China and Brazil, not reaccelerate in the 2nd half of the year. Secondly, they have highlighted the fact that there will be FX pressure on margins. With such a significant part of their revenues generated in markets that have recently experienced currency depreciation, we wonder if this is fully appreciated by the market.
Lastly, there are still question marks over the impact of the record number of account reviews happening this year, and whether these reviews will lead to a more competitive pricing environment longer term.

**Total**, as a short in our portfolio, was very weak during the month and suffered significantly, in line with falling oil prices. There are also on-going concerns about dividend sustainability, which is clearly no longer funded by cash flows and doesn't appear to be sustainable in the current environment.
Dividend yield attraction has been one of the main appeals of the investment case. We have already highlighted on previous occasions that the introduction of the scrip dividend is, in our opinion, a clear sign of weakness, with the company management appearing to buy some more time before taking a more structural decision on the dividend policy going forward.
Total also have one of the highest reserve decline rates in the industry at around 3.5%. This may force the company to increase investment so as not to see further declines in production.
As a further negative catalyst, we believe that project delivery is still one of the major risks for Total with FCF yield turning negative next year. With this in mind, we believe that the company, sooner rather than later, will have to address its mid-term guidance and dividend policy.

**Anheuser Busch Inbev** is a short position that contributed to our positive results in the Food & Beverage strategy during the month. Several factors were responsible for the fall in share price, not least the weak Brazilian Real (ABI own almost 70% of Ambev) and Mexican Peso (ABI bought Modelo 2 years ago).
There is also increasing evidence that ABI is finding it harder and harder to fight against major headwinds in the US, where it sources around 50% of its profits: the long term decline of the beer category and the loss of market share towards craft beer. Despite this, the stock has not been de-rated and is still one of the most preferred staples companies in Europe.

Source: Aventicum, otherwise specified

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