

Spring Ocean Capital Newsletter 3Q 2016

Portfolio Performance

Our portfolio performance for the first 3 quarters of the year were:

	S&P500	Spring Ocean Composite*
2016 1Q	1.4%	8.6%
2016 2Q	2.5%	8.9%
2016 3Q	3.9%	3.7%
2016 1-3Q	7.8%	22.5%

** We use the Interactive Broker's portfolio analytic data output. It includes all manage accounts. For detailed monthly return data, please see the other report (IB portfolio performance report). Performance data are not audited.*

The following table shows our five best and worst performing stocks for the first 3 quarters. It also shows their mark to market Profit and Loss as a percentage of consolidated NAV at end of 3Q 2016. (For simplification, we use end of 3Q NAV as denominator for PnL percentage calculation here. Because we have significant asset increase during the quarter, the PnL% shown here is smaller than time-weighted return calculation.)

	Profit%	Loss%
PCI (PIMCO Dynamic Credit Income)	3.3%	
OUTR (Outwall Inc)	2.3%	
EMC (EMC Corp)	1.9%	
CJR.B (Corus Entertainment Inc.)	1.6%	
ORV (Orvan Minerals Corp)	1.4%	
MCD H6 (Canadian Dollar Future)		-0.2%
MDY (SPDR S&P MIDCAP 400 ETF TRST)		-0.2%
MNDO (MIND C.T.I. Ltd.)		-0.2%
ES H6 (S&P 500 future)		-0.9%
BKE (Buckle Inc.)		-1.2%
Total:	10.6%	-2.6%

The top 5 best performing stocks had a total PnL of 10.6%. The bottom five had a total PnL of -2.6%.

Two in our top 5 profitable positions were acquired last quarter. They were OUTR and EMC. OUTR was privatized by a private equity firm. EMC was acquired by Dell. Both acquisitions helped to realize the profits. CJR.B was one of our large position initiated last year due to the attractive valuation and high dividend. However, Shaw Communication (the parent company of CJR.B)'s corporate event, in which Shaw let CJR.B to acquire the media subsidiary of Shaw Communication with debt, made CJR.B highly leveraged and less desirable. We reduced our position thereafter. Due to the timing of the selling and the low price at the start of the year, we also had some profit realized here. ORV is a small gold-mining stock. Due to the high volatility of the stock, our total weight in this stock was about 0.8% at end of 3Q.

PCI was our largest positions. As we discussed last quarter, it offered some of the highest yields and was managed by one of the best fixed-income management company (PIMCO) in the world. When we

started these positions a year ago, its market value had a huge discount compared to their net asset value (NAV) due to the concern that the Fed would increase rate and the long bond bull market would end. The fund had limited duration about 3. We reasoned that as long as the Fed did not increase the interest rate too quickly, we could still make money. We had been correct so far and market has respond by closing the discount gap and this position contribute nicely to our profit in the third quarter.

Among the 5 biggest losers, BKE(Buckle Inc.) is a retailer of casual apparel for young men and women. It was in the bottom 5 the second quarter too. The fundamental of this stock had deteriorated, but not as much as the price. I did not foresaw the retail down trend could last this long and the revenue of BKE had decreased so much (down 10-15% annually). However, I still believe BKE offers value and a committed management team. We will keep a close eye on this position.

MNDO is a small Israel based telecom software provider. Nothing changed much in the third quarter in terms of both price and the fundamental. We will still hold the position and wait for the market to realize the company's potential.

MDY, ES H6, and MCD H6's were our hedging positions. We sold short MDY and ES H6(S&P 500 index future) to hedge some of the market risk. For the first three quarters, the market went up, and we incurred some loss in the MDY as well as the ES H6 future position. MCD H6 was a hedging position on some of our Canadian dollar exposure. Since they were hedging positions, their loss were usually cancelled out by the other positions that made money.

In summary, our first three quarters performance of 22.5% was significant better than the market. We were happy with the results.

Major positions at the end of 3rd quarter 2016

Our major 5 positions at end of Sep 2016 were:

	Jun 2016	Sep 2016
MDY(SPDR S&P MIDCAP 400 ETF TRST)	-14.7%	-21%
PCI (PIMCO Dynamic Credit Income Fund)	19.4%	18.6%
PDI(PIMCO Dynamic Income Fund)	13.4%	10.5%
PFN(PIMCO Income Strategy Fund II)	11.2%	9.7%
GILD(Gilead Sciences)	3.8%	9.2%
EMC(EMC Corp)	15.8%	0%

As we expected, Dell completed the acquisition with EMC last quarter. We realized the profit and eliminated the position. We increased the position for GILD significantly in the third quarter. We also slightly reduced some Fixed-income position in anticipate the coming rate increase in December.

Our positions by asset class at the end of third quarter were:

	Jun 2016	Sep 2016
Equity	51.1%	58.6%
Equity Index Hedge	-13.0%	-21.9%
Fixed-income fund	48.6%	44%
Arbitrage	15.1%	-0.7%
Cash	-1.8%	20%

The biggest change in the third quarter was the large increase of cash. The 20% cash position was mostly due to the realization of previous arbitrage positions which all happened close to the end of third quarter. (i.e. EMC acquisition and OUTF acquisition). Going forward, we will cautiously to deploy the cash to more interesting positions.

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