

Spring Ocean Capital Newsletter 2017 3Q

Portfolio Performance

Our portfolio performance for 2016 and this year was:

	S&P500	Spring Ocean Composite*
2016	11.95%	26.8%
2017 1Q	6.1%	3.7%
2017 2Q	3.1%	4.3%
2017 3Q	<u>4.5%</u>	<u>4.7%</u>
2017 YT3Q:	14.2%	13.2%

** We used the Interactive Broker's portfolio analytic data output. It included all managed accounts after all expenses and fees. For detailed monthly return data, please see the other report (IB portfolio performance report). Performance data were not audited.*

We performed marginally better than S&P 500 in the third quarter. Year to third quarter, we still underperformed the S&P 500 index. The following table shows our five best and worst performing stocks for the first three quarters. It also shows their mark-to-market Profit and Loss (PnL) as a percentage of consolidated Net Asset Value (NAV) at the beginning of 2017.

	YT3Q Profit%	YT3Q Loss%
PCI (PIMCO Dynamic Credit Income)	2.8%	
DVMT(DELL TECHNOLOGIES INC)	2.4%	
GILD(Gilead Sciences)	1.9%	
PFN (Pimco Income Strategy Fund II)	1.9%	
KORS(Michael Kors)	1.2%	

T (AT&T)		-0.03%
TGZ (Teranga Gold Corp)		-0.1%
APEI (American Public Education)		-0.3%
BKE (Buckle Inc.)		-0.9%
Index Hedging(Index ETFs)		-1.6%

Total:	9.6%	-2.9%

The top 5 best performing stocks had a total PnL of 9.6%. The bottom five had a total PnL of -2.9%.

PCI and PFN were our two largest fixed income positions. The fixed income fund still kept the price momentum even after FED increased interest rate twice this year. Usually, when interest rate increases, fixed-income (Bond) price will decrease.

In the third quarter, 3 new positions showed up on the top performing stocks, they are DVMT, GILD, and KORS. They replaced ABC, SEC and PFL in previous quarter. It is interesting that the KORS was our bottom 5 in second quarter, and now it is in the top 5.

GILD (Gilead Sciences) announced acquisition of Kite Pharma for \$12B in the third quarter. Kite had a pending FDA drug named **Yescarta**. The drug uses genetically-engineered T-cells to attack cancer cells. (As of 10/18, it was approved by FDA for adults with advanced lymphoma). It was the second CAR-T therapy approved by FDA after recent big news of Novartis \$475,000 CAR-T therapy. Market is ignited by

possible growth of the acquisition and changed the view of Gilead Sciences; the GILD stock price improved from recent low of \$64 to end of quarter price at \$81.

DVMT is the tracking stock of VMware. Its price momentum comes from the VMware's stock price change.

Our biggest loss in the first three quarters is our index hedging position. The market went up about 14% in the first 3 quarters, we experienced some expected loss here. As we said before, the hedge position was used to decrease our portfolio volatility. In the long run, those hedge positions will cost us money as the market in general moves up. But it also gives us some valuable opportunity when the market goes down. In the down market, we may experience less downside movement and have resources to pick up some attractive investments.

BKE was one of our major retail holdings. The retail industrial had lots of headwind recently. We haven't see any turn around yet. However, after we revisited the stock's fundamental, we could still wait it out as the company is still profitable and has a large discount to our valuation. Similarly, KORS is one in the retail industry and its stock performed well in the third quarter.

T is a very small position and due to price fluctuation, we experienced some loss here.

In summary, our portfolio outperformed the market marginally in the third quarter. First three quarters, we still underperformed the S&P 500 by a small margin. At the end of the third quarter, we still underweight equity. We believe we need to take a defensive position right now and the slight underperformance is probably worthwhile in the long run.

Major positions

Our major 5 positions at the end of Sep. 2017 were:

	Jun. 2017	Sep. 2017
SYT (Syngenta)	12.7%	18.7%
Index ETFs	-19.3%	-19.8%
PCI (PIMCO Dynamic Credit Income Fund)	16.2%	14.2%
GILD (Gilead Sciences)	12.5%	11.6%
ABC (AmerisourceBergen Corp.)	12.3%	11.1%

Compared to previous quarter, we increase our position on SYT. This is an arbitrage position. ChinaChem finished the tender offer for SYT, and is expect to finish the squeeze out merger between Oct and December. This position is like a short term cash position with an annualized interest rate between 5-7%, depending how fast the merger can be finished. We also decreased our position in ABC and GILD slightly to reduce risk and lock in some profit.

Our positions by asset class at the end of Sep. 2017 were:

	Jun. 2017	Sep. 2017
Equity	65.7%	64.5%
Equity Index Hedge	-19.3%	-19.8%
Fixed-income fund	28.3%	22.8%
Arbitrage	12.4%(22.5%, -10.1%)	18%(32.8%, -14.8%)*
Cash/cash equivalent	12.9%	12.0%

**The arbitrage position consist of 32.8% long and -14.8% short positions, net of 18%.*

We trimmed some of our fixed-income fund positions due to concern of rising interest rate as well as stock price appreciation. We also increased arbitrage position on SYT.

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