Spring Ocean Capital Newsletter 2017 4Q

Portfolio Performance

Our portfolio performance for 2016 and 2017 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	4.5%	4.7%
2017 4Q	6.6%	3.1%
2017:	21.8%	16.7%

** 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. Individual account performance may vary.*

Our performance of 16.7% would have been good in a normal year, but not in 2017. Compared to the overall market, we underperformed S&P 500 by about 3.5% in the fourth quarter and by 5% for the whole year. The market performed extremely well in 2017 with no single down month. The Sharpe ratio (annual return/standard deviation of returns) for the S&P 500 based on monthly returns in 2017 is about 5. Sharpe ratio is commonly used in investment industry to measure the risk adjusted return. For similar risk, the higher the Sharpe ratio, the higher the return. For comparison, Buffet's Berkshire stock's Sharpe ratio was 0.75 for 1976-2011, and the overall market's Sharpe ratio for the same period was 0.39. The 2017 year market's risk adjusted return is about 13 times the historical average. We do not think the excellent performance of the market in 2017 will last for long. (As of the writing in early February, the market experienced one of the most volatile swings since 2008.)

We had a couple new client accounts opened and funded in 2017. In the steady growing bull market, I became very defensive, and did not purchase stock aggressively. The new founded accounts had more cash at hand than the composite average. Thus, those new accounts did not perform as well as the composite. Old clients would saw slightly better performance than the composite return number. New accounts performance will get very close to the composite performance number after the asset is invested and the cash level brought to composite average.

The following table shows our five best and worst performing stocks for 2017. 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.

	2017 Profit%	2017 Loss%
KORS(Michael Kors)	2.9%	
PCI (PIMCO Dynamic Credit Income)	2.5%	
DVMT(Dell Technologies Inc.)	2.3%	
ABC (AmerisourceBergen Corp.)	1.9%	
PFN (PIMCO Income Strategy Fund II)	1.9%	
T (AT&T)		-0.03%
TGZ (Teranga Gold Corp)		-0.04%
GNW (Genworth Financial Inc.)		-0.8%
Index Hedging(Index ETFs)		-2.7%
Total：	11.2%	-3.6%

The top 5 best performing stocks had a total PnL of 11.2%. The bottom 4(We only have 4 loss's excluding long/short combo positions) had a total PnL of -3.6%.

PIMCO Dynamic Credit Income Fund (PCI) and **PIMCO Income Strategy Fund II (PFN)** were our two largest fixed income positions. The fixed income fund still kept some of the price momentum even after FED increased interest rate three times in 2017. Usually, when interest rate increases, fixed-income (bond) price will decrease.

Michael Kors (KORS) was in our bottom 5 list as recently as in the second quarter of 2017; it became the top performance contributor of the year. The performance improvement was mostly due to the market sentiment for retail industry.

Compared to the third quarter, **AmerisourceBergen (ABC)** replaced **Gilead Sciences (GILD)**'s position. ABC is in the pharmaceutical distributing business. We added some significant position in 2016. Now after about a year, it bore fruit and became one of the top 5 performance contributor.

Dell Technologies (DVMT) is the tracking stock of VMware. Its price momentum came from VMware's stock price change.

Our biggest loss in the year was our index hedging position. The market performed extremely well and went up about 21%; we experienced some relatively big loss here.

Genworth Financial (GNW) replaced Buckles (BKE) in the bottom positions compared to the third quarter. GNW is an arbitrage position, China Oceanwide offered to acquire GNW for $5.43 per share. Due to recent regulation uncertainty, especially after news that Ma Yun's Ant Financial failed to get approval to acquire MoneyGram, the price of GNW went down. However, we still believe there is a large chance that the merger will go through. Even if the merger fails, the improved financial condition of GNW may give us some downside support.

Both AT&T (T) and Teranga Gold (TGZ) are tiny legacy positions. Due to price fluctuation, we experienced some small loss here.

In summary, we underperformed the S&P 500 by about 5% in 2017. The market performed extremely well for the year, and we underweighted equity and were taking a defensive position.

Major positions

Our major 5 positions at the end of 2017 were:

	Sep. 2017	Dec. 2017
SYT (Syngenta)	18.7%	21.3%
Index ETFs	-19.8%	-20.2%
PCI (PIMCO Dynamic Credit Income Fund)	14.2%	13.6%
ABC (AmerisourceBergen Corp.)	11.1%	12.3%
GILD (Gilead Sciences)	11.6%	10.9%

Compared to the third quarter, we slightly increased our position on Syngenta (SYT). This arbitrage position was completed as we wrote this newsletter, and we were paid full cash amount on this position. The total investment time was longer than we originally expected; we made a profit on this position but not to our expectation. We added some more positions on AmerisourceBergen (ABC) and Gilead Sciences (GILD). GILD's price change in the 4th quarter decreased the weight.

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

	Sep. 2017	Dec. 2017
Equity	64.5%	63.3%
Equity Index Hedge	-19.8%	-20.2%
Fixed-income fund	22.8%	18.9%
Arbitrage	18%(32.8%, -14.8%)	21%(34.9%, -13.9%)*
Cash/cash equivalent	12.0%	16.9%

**The arbitrage position consist of 34.9% long and -13.9% short positions, net of 21%.*

We trimmed some of our fixed-income fund positions mostly due to stock price appreciation. The increase of the arbitrage category are mostly comes from our position on Syngenta (SYT).

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