Pelargos Japan Alpha Fund
July 2015

Fund Performance

The Pelargos Japan Alpha Fund Class B decreased -2.94% in July. Since July 2008, inception-to-date (ITD), the fund is up 49.63% with a realized volatility of 7.3%.

Fund Performance

Share Class	NAV	MTD	YTD	ITD
Class A EUR	1,314.99	-3.07%	4.11%	31.50%
Class A USD	967.98	-3.04%	4.05%	-3.20%
Class A JPY	95,585	-3.14%	3.61%	-4.41%
Class B EUR	1,496.34	-2.94%	4.42%	49.63%

Market Environment

In July, the MSCI Japan appreciated +1.7% in Japanese Yen (JPY) terms and +0.2% measured in USD. Despite posting a small monthly gain, the market did not go up smoothly with volatility picking up. In early July, the market corrected over 5%, as Chinese equities continued its sharp decline and the Greek debt situation became increasingly uncertain after the European rescue package was rejected in a referendum. In the second half of the month, global news flow turned for the better as Greece was allowed to roll its debt and Fed Chair Yellen reiterated her believe in the resilience of the US economy, which pushed up the odds for a September rate hike in the US. Japanese equities bounced sharply on this news and were further supported by solid corporate earnings into month-end.

Sector and style-wise, the same trends that drove performance in June, persisted in July. Expensive, high price-momentum, defensive sectors such as consumer staples and household products performed very well. Furthermore, utilities bounced strongly after the restart of the first nuclear reactor by Kyushu Electric since the nationwide shutdown was implemented in 2012. Cyclical sectors such as semiconductors, capital goods and materials continued to perform poorly and lagged the winning sectors by a significant margin. The up- versus down-days were evenly balanced, with 11 up and 12 down days. However, most of the losses were generated in the short book as only 10% of our fundamental shorts declined and the average return of our short book was 7.4%, handsomely outperforming the MSCI Japan.

Top & Bottom Industry Movers

Industry Group	MTD	YTD	PB	PE
Utilities	12.5%	30.8%	1.1	12.5
Household Products	9.8%	42.8%	2.2	30.5
Food Beverage	8.7%	30.7%	1.2	22.1
Industry Group	**MTD**	**YTD**	**PB**	**PE**
Semiconductors	-11.4%	-15.5%	0.9	11.4
Capital Goods	-4.9%	6.3%	0.9	11.8
Materials	-3.3%	6.3%	0.7	12.8

Source: Bloomberg

General Statistics

% Return long book	0.8%
% Return short book	7.4%
# Long stocks	52
# Short stocks	10
% Long stocks ↑	50%
% Short stocks ↓	10%
# Up days / Down days	11 / 12
Daily Correlation with MSCI JP	0.78
Turnover as % NAV	64%

Source: Factset

Largest Long & Short Holdings

Longs	Shorts
Ryosan	Kikkoman Corp
Moshi Moshi	Nippon Express
Fancl Corp	Nissin Foods
Chiyoda Co	THK
Tokyu Corp	Komatsu

Source: Citi Financial Services

Single Stock Activity

Largest Buy & Buy Cover*		Largest Sell & Short Sell**	
Tokyu Corp	B	Tonengen Sekiyu	S
Itochu Corp	B	Komatsu	SS
East Japan Rail	B	Kose Corp	SS
Fancl Corp	B	Nippon Express	SS
Invincible REIT	B	Acom	S

** B = Buy; BC = Buy Cover* *Source: Citi Financial Services*

*** S = Sell; SS = Short Sell*

Investment Strategy

The largest long positions are mainly unchanged except for Fancl, which replaced Ichigo in the top 5 longs. We met the company several times over the past few years and started to build a position late 2014. Fancl is a pioneer in additive-free skin care products. The stock has been trading at steep valuation discounts to its peers as profitability was weak and dragged down by its nutritional supplements business. Last fiscal year, chairman and founder Kenji Ikemori returned at the helm of the company to implement various reform programs. Profitability has improved since. Like most other Japanese cosmetics companies, Fancl is benefitting from inbound tourism demand. However, given their valuation discount , we see further upside potential.

We closed long positions in Tonen General as well short positions in Nippon Building Fund and Japan Real Estate Investment Corporation. The short position in latter two REITs worked well and July's sharp declines provided a good opportunity to take profits. At current price levels, we feel more comfortable holding a net long position in office and hotel REITS.

Pelargos Japan Alpha Fund
July 2015

Investment Strategy

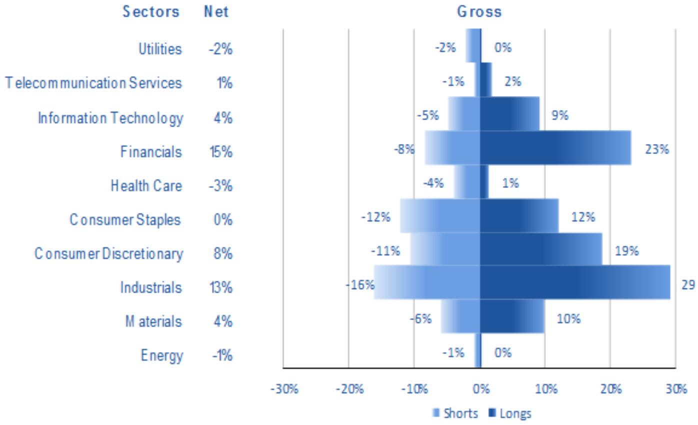
The top gainers last month were all long positions. Acom contributed +50bps on the back of solid earnings. The consumer credit cycle seems to be improving, though after the recent rally the stock is not cheap anymore. Chiyoda, Japan's second largest shoe retailer, which we discussed in June's monthly newsletter, also benefited from solid earnings growth.
The gains by Pola Orbis, Fancl and Seven&I can be largely attributed to the strong performance of defensive sectors such as household goods. Unfortunately, these gains were cancelled out by short positions in Kikkoman and Nippon Express. Other losing positions were Moshi Moshi Hotline, which has now given back most of recent gains as its shares will drop out of the JPX400 index late August. Their latest earnings seemed on track and the company won a mandate to support the social security my-number introduction. Fujitec and Komori are exporters with sizable China businesses, which investors are now worrying about, given weak macro economic developments.

The net exposure in financials declined marginally to 13% and remained our largest net exposure on a sector level. More than half of this is REITS which carry attractive yields of 4% which in our opinion are subject to further upward revisions as the upward rent-revision cycle has just started.

Top Gainers & Losers

Gainers		CTR*	Losers		CTR*
Acom	L	0.5%	Moshi Moshi	L	-0.3%
Chiyoda Co	L	0.4%	Kikkoman Corp	S	-0.3%
Pola Orbis	L	0.2%	Nippon Express	S	-0.3%
Fancl Corp	L	0.2%	Fujitec Co	L	-0.2%
Seven & I	L	0.2%	Komori Corp	L	-0.2%

**CTR = Contribution* *Source: Factset*

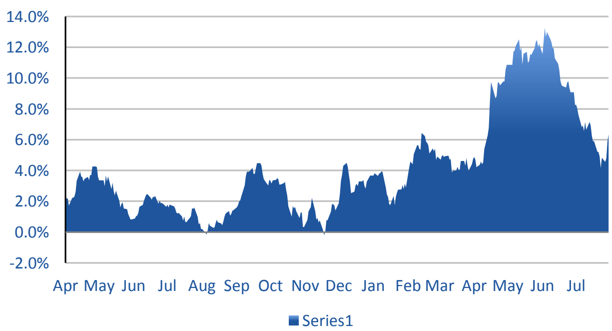


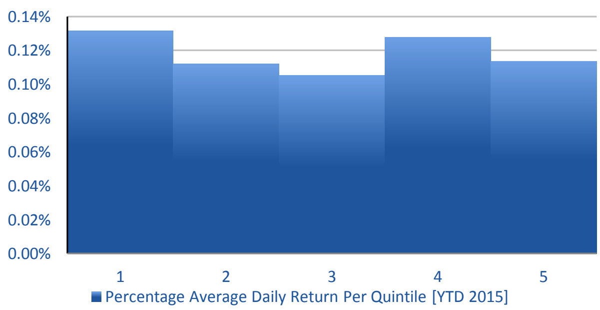
Source: UBS PAS

Value Factor Performance*

	P/E	EV/EBITDA	P/B	Div Yld	EV/IC	FCF
MTD	-2.5%	-3.1%	-2.9%	-1.7%	-1.3%	0.8%
YTD	3.0%	-0.9%	-1.0%	0.2%	0.5%	2.9%

*Source: Factset**





*Source: Factset**

Style Performance

On a daily basis we track numerous style factors based on our proprietary quant model. This helps us to detect misallocation of capital within the market and helps our understanding of style trends and investor's behavior in Japan.

Value performance was strong earlier this year, which was very supportive to our alpha capturing approach. Since peaking out in May, the Japanese equity market has seen a sharp reversal in the performance of value factors. This weakness was seen across all value factors, with price-earnings-ratio (P/E), price-to-book (P/B) and enterprise-value-to-EBITDA (EV/EBITDA) being down the most. P/B and EV/EBITDA have now given back all their positive returns for this year.

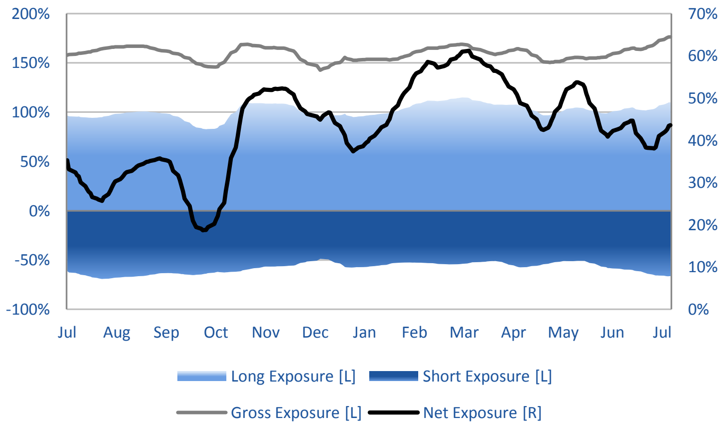
Dividend yield as a style suffered as well. The fund is long dividend exposure mainly through the REIT space. The REIT index peaked out in January this year, in absolute terms and relative to the broader market. Real estate fundamentals remain solid as vacancy rates are coming down and rents have finally started to pick up after 5 years of declines. We will look to selectively add to our REIT exposure, and we see most value in B-class offices and hotels.
The current exposure characteristics in the fundamental book are shown on the next page.
With regards to the value factors the biggest spread is in P/E, P/B and EV/EBITDA. The long book has significantly higher earnings momentum compared to the short book. Price momentum has dropped below the short book as a result of the correction in value stocks to which we have significant exposure in our long book.

Pelargos Japan Alpha Fund
July 2015

Risk Measurement and Management

The chart below shows the rolling 12-month net and gross exposure for the fund. In order to improve readability of the chart, the exposures are shown as 10 (trading) days moving averages.
The gross exposure has been in a rather stable range between 150-160%, but increased to 175% in July. During the month we expanded the short exposure and added to our highest conviction longs.

The net exposure at the end of July stood at 44%, which was unchanged over prior month. The ex-ante volatility estimate rose from 7.9% to 8.9% as a result of higher gross exposure and rising market volatility. The average ex ante beta of the long book is a relatively low 0.9.



*Source: Citi Financial Services**

Fund Overview

	Long	Short
Price to Earnings (PE)	19.5	38.9
EV/EBITDA	8.6	14.1
Price to Book (PB)	1.6	2.2
Dividend Yield	1.9	1.4
EV/IC	1.0	1.6
1 month momentum	3.2	5.8
6 month momentum	19.8	17.2
9 month momentum	23.8	33.9
Earnings momentum (1M)	8.1	-9.0
Earnings momentum (3M)	4.8	-15.7
CFROI	7.0%	6.1%
Cash/MarketValue	35.8%	22.3%

Source: Factset

Style Exposure

	Long	Short
Beta	0.9	1.0
Volatility	16.7%	17.3%
Debt-to-equity	17.00	49.00

Source: UBS PAS

Risk Statistics Delta Adjusted

Volatility (ex-ante; 1yr daily data)	8.9%
Volatility (ex-ante; 5yr monthly data)	7.4%
Var (99%, 5 days)	2.1%
Beta (ex-ante)	0.31

Source: GS and UBS PAS

Outlook

Strategic Framework - Outlook 2nd half of 2015
Economic data is normalizing after last year's VAT hike. Finally underlying trends are meaningful again. The Japanese economy is not in great shape, but neither is the global economy. Nevertheless, at least the Japanese data has stopped disappointing. The weak Japanese Yen continues to be a support for a rather dull economy. The most interesting development is the volatility spill over from currency markets and commodity markets into fixed income markets and as of mid-June, finally into equities. Central banks aimed to suppress risk premia/volatility through monetary activism and 'achieved' the lowest long dated bond yields in centuries. A healthy financial system can cope with volatility. Accepting price swings yields the most efficient capital allocation, it rewards savvy market participants and punishes mis-judgement as well as overly leveraged risk taking. The manipulation of market segments by central bankers results in underestimating risk and introduces second and third layer of unintended consequences. Not all prices can be controlled all the time. Ultra low interest rates did not matter for a long time and now that the US Fed wants to 'normalize' interest rates currency markets need to re-price for policy divergence. The single most important economic variable for the second half of 2015 is the US dollar. As long as the US dollar appreciation and sell-off in long dated bonds is gradual, the repercussion for the US economy remains limited and the Japanese market can continue its ascent. The collapse of commodities and emerging market equities have so far been ignored by developed market investors. But for how long? A lot of 'ifs' indeed, nevertheless a useful roadmap to keep in mind.
Tactical assessment – Outlook August 2015
After the strong value performance earlier this year, expensive quality stocks made a come back in June and July, putting our thesis of shorting this smart beta bubble to a serious test. The systematic smart beta buying is an institutional trend supported by trust/pension funds. That said, the Japanese pension re-allocation to equities is running its course and the incremental buying is diminishing. In our opinion, the market as a whole is fair value. However, the market is well-supported by improving economic fundamentals. More importantly, the yen weakness has had a material positive impact on Japan's corporate profitability, which has resulted in a significant improvement of general economic activity and confidence. This renewed dynamism in combination with Abenomics' third 'structural reform' arrow has resulted in a very strong push to improve corporate governance. The best upside opportunities in our opinion are mid-sized domestic demand related companies, which have started to address their inefficient balance sheets and low shareholder returns. This will be a multi-year re-rating story and should still do well in with growing macro economic weakness and uncertainty.

Pelargos Japan Alpha Fund
July 2015

pelargos capital

Historic Fund Performance (Monthly)

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
Class A EUR												
2015	-1.28%	4.85%	-0.32%	3.21%	2.54%	-1.63%	-3.07%					
2014	-3.21%	-0.64%	-0.59%	-1.03%	-2.28%	1.40%	0.19%	-0.64%	2.01%	-1.94%	-1.28%	0.92%
2013	4.99%	-0.58%	6.55%	6.10%	-1.05%	-0.78%	0.26%	-0.91%	1.08%	-0.79%	1.35%	1.61%
2012	-1.43%	3.77%	1.31%	-1.26%	-3.88%	1.72%	0.79%	0.89%	1.28%	0.54%	2.53%	3.78%
2011	0.84%	-0.06%	-1.56%	0.10%	-0.19%	0.38%	-0.01%	-3.68%	0.64%	-0.41%	-2.64%	1.64%
2010	0.65%	-0.25%	3.27%	3.16%	-2.71%	-1.27%	1.12%	-0.39%	0.82%	1.03%	1.28%	1.75%
2009	0.35%	1.62%	-0.76%	-0.71%	0.98%	1.03%	-1.84%	2.07%	-1.61%	-0.40%	-3.37%	3.19%
Class A USD												
2015	-1.37%	4.79%	-0.51%	3.48%	2.62%	-1.70%	-3.04%					
2014	-3.16%	-0.74%	-0.68%	-1.11%	-2.26%	1.30%	0.21%	-0.63%	1.88%	-1.89%	-1.36%	0.92%
2013							-1.92%	-1.15%	1.29%	-1.04%	1.58%	1.74%
Class A JPY												
2015	-1.40%	4.80%	-0.51%	3.11%	2.88%	-1.92%	-3.14%					
2014	-3.24%	-0.80%	-0.71%	-1.19%	-2.27%	1.26%	0.19%	-0.65%	1.86%	-1.97%	-1.60%	0.87%
2013							-1.82%	-1.26%	1.23%	-1.06%	1.59%	1.73%
Class B EUR												
2015	-1.24%	4.89%	-0.27%	3.25%	2.57%	-1.67%	-2.94%					
2014	-3.16%	-0.60%	-0.56%	-0.99%	-2.24%	1.44%	0.23%	-0.60%	2.06%	-1.89%	-1.24%	0.96%
2013	5.35%	-0.58%	6.98%	6.48%	-1.07%	-0.78%	0.31%	-0.92%	1.18%	-0.80%	1.46%	1.73%
2012	-1.38%	3.81%	1.35%	-1.21%	-3.83%	1.76%	0.84%	0.93%	1.32%	0.58%	2.50%	4.06%
2011	0.93%	-0.03%	-1.55%	0.14%	-0.14%	0.42%	0.03%	-3.63%	0.69%	-0.38%	-2.60%	1.68%
2010	0.73%	-0.23%	3.52%	3.39%	-2.83%	-1.31%	1.23%	-0.37%	0.91%	1.13%	1.40%	1.89%
2009	2.07%	1.67%	-0.73%	-0.67%	1.34%	1.13%	-1.93%	2.24%	-1.68%	-0.39%	-2.99%	2.84%
2008							0.96%	-1.35%	1.40%	3.44%	0.52%	1.39%

Historic Fund Performance (Yearly)

	2015	2014	2013	2012	2011	2010	2009	2008
Class A EUR	4.11%	-6.99%	18.86%	10.24%	-4.96%	8.66%	0.36%	
Class A USD	4.05%	-7.38%	0.43%					
Class A JPY	3.61%	-8.06%	0.35%					
Class B EUR	4.42%	-6.52%	20.57%	10.95%	-4.48%	9.67%	2.75%	6.46%

Fund Facts

Investment Manager	Pelargos Capital
Legal Status	FGR (fund for joint account)
Fiscal Status	VBI (tax exempt)
Dividend Policy	Reinvestment
Base Currency	EUR
ISIN Class A EUR	NL0009051887
ISIN Class A USD	NL0010545570
ISIN Class A JPY	NL0010545588
ISIN Class B EUR	NL0001118015
Inception Date Class A EUR	January 2009
Inception Date Class A USD	July 2013
Inception Date Class A JPY	July 2013
Inception Date Class B EUR	July 2008

Fund Facts

Fund Size in EUR	€ 93,812,804
Fund Size in USD	$103,043,983
Participations Outstanding Class A	436
Participations Outstanding Class B	62,382
Minimum Subscription Class A	EUR 10,000
Minimum Subscription Class B	EUR 10,000
Dealing Day	First business day of each month
Subscription	Any dealing day, 5 business days notice
Redemption	15 business days notice
Management Fee Class A	1.5%
Management Fee Class B	1.0%
Performance Fee Class A	20% subject to High Watermark
Performance Fee Class B	15% subject to High Watermark
Early Redemption Fee	max 1% (accrues to Fund)
Lock-up Class B	1 year

Pelargos Japan Alpha Fund
July 2015

Company Facts

Firm AUM in EUR	€ 232,174,354
Firm AUM in USD	$255,020,310

Portfolio Managers

Richard Dingemans

Michael Kretschmer

Service Providers

Prime Brokers	UBS AG, Goldman Sachs International
Administrator	BNY Mellon Fund Services
Accountant	PricewaterhouseCoopers
Legal	De Brauw Blackstone Westbroek N.V.
Title Holder	SGG Netherlands N.V.
Depositary	Bank of New York Mellon

Fund Description

Investment Strategy	Equity Long/Short
Investment Style	Value with a twist
Investment Objective	Capital appreciation through investing in long/short positions in Japanese securities

Contact Details

WTC The Hague, Tower E 7th floor

Prinses Margrietplantsoen 43

2595 AM, The Hague

The Netherlands

+31 (70) 7568030

www.pelargoscapital.com

Disclaimer