



MARKET COMMENTS

In September, the MSCI Japan appreciated a whopping +4.8% and despite the strong rally the index was barely up for the year. So far, 2018 has been a big challenge with little trending behavior, plenty of whipsawing and the Japanese equity index spending 90% of its time in negative territory. The Japanese yen (JPY) rapidly depreciated last month, declining -2.4% against the US dollar. With 10-year US treasury rates surpassing 3%, holding the low yielding JPY becomes increasingly unappealing. The weakening JPY should be a great boost to earnings for the third quarter. The equity rally from the September 7th low was driven by short covering and was to a large extent futures-driven. As a result, large capitalization stocks with high index weights massively outperformed small cap stocks. The MSCI Small Cap index barely appreciated, gaining 1% in September.

In general, macro-economic data is decent, but softening. Especially China related factory automation and smart phone related capex is cooling off. The market biggest concern is that higher US yields will further tighten global US dollar liquidity, which is, and we have written many times about these causalities over the past few years, certainly negative for Asian risk assets. For Japan, higher US yields and a stronger US dollar are a good thing as long as it is well contained and does not lead to a US dollar funding crisis.

SINGLE STOCK OBSERVATIONS

Taihei Dengyo was the best single stock contributor last month and added +0.4% to fund performance. Taihei Dengyo is a domestic engineering company, which constructs and maintains industrial, thermal power and nuclear plants. This business enjoys mid-single digit operating margins with historically, low single digit growth. Most important the stock price trades at a 20% discount to book value, 20% of the market capitalization is cash and another 20% in treasury shares and cross shareholdings. Thus, an extremely undervalued business and the order book shows strong growth, which bodes well for futures revenues. To the regular readers of this newsletter, Taihei Dengyo's business might look familiar, as it is a smaller competitor to our largest holding Toshiba Plant Systems.

In September, we made 0.3% with the short position in Daito Trust and 0.3% with the long position in Maeda Construction. We are very enthusiastic about the business development at Maeda Construction. Its push into concession business, which is rather new to Japan is a major shift in business model. Maeda already participated in a toll road project, airport project and convention center project. This type of concession business has stable, long duration cash flows and if structured in joint-ventures with reliable partners and appropriate leverage, it produces very attractive returns.

Unfortunately, we gave back the 30bps gain in FamilyMart and lost 70bps this month. Our short thesis unfolded in a rather different direction as the new shareholder Itochu seems to be very determined in terms of size and speed of restructuring the loss making GMS (general merchandise store) business. Based on valuations, the stock was already heavily shorted to begin with and at the end of September the first analyst reports appeared indicating that FamilyMart UNY's earnings will be in-line with expectations as aggressive cost cutting offsets weak top-line growth. Another significant loser last month was Alpine. The stock trades in-line with the Alps merger ratio and Alps stock price suffers from current weakness in the handset market. On September 27th, Alpine announced to distribute a special dividend to appease minority shareholders. This is indeed a good signal and step in the right direction, but insufficient for Alps to get its approval in December to fully acquire its consolidated subsidiary Alpine. To be continued ...

RISK ALLOCATION

The net exposure at the end of the month stood at just 28% and the gross exposure at 154%. The gross exposure remained constant and elevated as we have identified plenty of opportunities in the long as well as the short book. That said, the net exposure, especially beta-adjusted, is significantly lower as our current risk assessment warrants less market exposure despite valuations being attractive.

STYLE ASSESSMENT

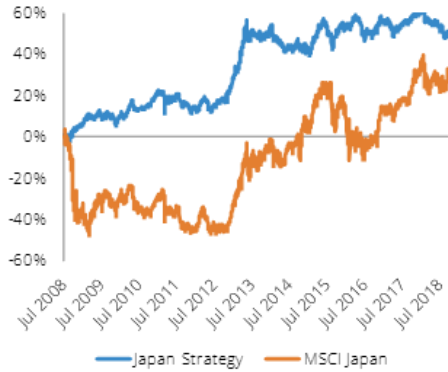
Last month we wrote about the correlation between value style and interest rates/the yield curve. US yields were somewhat higher and with it low price-to-book financials had a strong rally. Nevertheless, across the entire market value performed poorly last month. We observe little systematic behavior, the only exception being stocks with high earnings momentum and strong earnings revisions continue to perform well irrespectively of valuation.

OUTLOOK

We are getting increasingly positive with regards to the market outlook for the coming 3-6 months. To begin with, valuations in Japan are attractive, especially against a background of improving shareholder returns, thus higher margins, more buybacks and therefore higher Return on Equity. At the same time, the global economic growth momentum is slowing and there are pockets of weakness in auto, semiconductor capex and Chinese factory automation. That said, sentiment is negative, reflected in lack of liquidity and low valuations, in our opinion to such an extent that we are ready to consider increasing risk exposure.



FUND CHARTS AND FACTS



TOP 5 GROSS POSITIONS

Toshiba Plant Sy
Ichigo Hotel REIT Investment C
Ichigo REIT
Alpine Elec
Taihei Dengyo

TOP 5 MOVERS

Taihei Dengyo	0.40%
Daito Trust Cons	0.29%
Maeda Corp	0.29%
Ichigo REIT	0.26%
Ariake Japan	0.23%

TOP 5 SHAKERS

Familymart	-0.69%
Alpine Elec	-0.65%
Ichigo Group	-0.22%
Sumco Corp	-0.16%
Pepper Food Serv	-0.13%

FUND FACTOR

	Long	Short
Price to Earnings (PE)	16.9	22.5
EV/EBITDA	11.6	16.4
Price to Book (PB)	1.7	4.2
Dividend Yield	2.3	1.9
EV/IC	1.1	3.6
1 month momentum	4.0	0.4
12-1 month momentum	15.4	8.6

FUND PERFORMANCE*

Month to date performance	0.36%
Year to date performance	-6.13%
Inception to date performance	50.74%

**based on share class B EUR*

FUND FACTS*

Fund size in mln EUR	98.20
Fund size in mln USD	114.06
Firm size in mln EUR	226.91
Firm size in mln USD	263.55

RISK STATISTICS

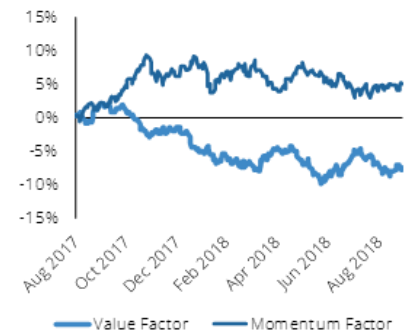
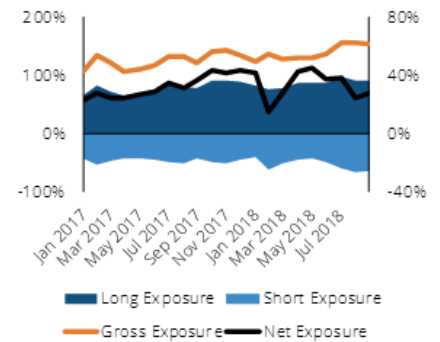
Net Exposure	28%
Gross Exposure	154%
Volatility (ex-ante; 3 months daily data)	5.5%
Beta (ex-ante)	0.29
Sharpe Ratio	0.60
Sortino Ratio	1.15
Sterling Ratio	0.49
Max Drawdown (monthly)	-8.4%
Annualized Return	4.1%

SECTOR EXPOSURES (IN PERCENT)

	Long	Short	Net	Gross
Consumer Discretionary	12	-7	5	19
Consumer Staples	6	-7	-1	12
Energy	0	0	0	0
Financials	2	-1	1	3
Health Care	1	-1	-1	2
Industrials	34	-11	23	46
Information Technology	5	-5	0	10
Materials	4	-3	1	7
Real Estate	23	-8	15	32
Telecommunication Services	0	0	0	0

GENERAL STATISTICS

% Return long book	2.86%
% Return short book	4.58%
# Long stocks	49
# Short stocks	16
% Long stocks ↑	78%
% Short stocks ↓	38%
# Up days / Down days	10 / 10
Turnover as % NAV	42%



FUND PERFORMANCE: CLASS B EUR	Year	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	YTD	ITD
	2018	-0.26%	-1.77%	-1.03%	-0.63%	-0.06%	-0.36%	-0.87%	-1.66%	0.36%					-6.13%
2017	0.56%	-0.92%	-1.63%	-0.57%	0.23%	1.32%	1.18%	0.46%	0.99%	1.25%	0.20%	0.14%		3.22%	60.59%
2016	1.27%	0.92%	1.18%	-0.16%	-1.08%	-4.33%	2.12%	-1.05%	-0.29%	2.38%	0.88%	0.39%		2.07%	55.58%
2015	-1.24%	4.89%	-0.27%	3.25%	2.57%	-1.67%	-2.94%	-3.01%	2.46%	1.88%	2.06%	-1.42%		6.36%	52.42%
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%		-6.52%	43.31%
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%		20.57%	53.31%
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%		10.95%	27.15%
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%		-4.48%	14.60%
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%		9.67%	19.97%
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%		2.75%	9.39%
2008							0.96%	-1.35%	1.40%	3.44%	0.52%	1.39%		6.46%	6.46%

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