SANNING CAPITAL
EFFICIENCY FUND

October 2014 – Stocks on the Rollercoaster

In October, volatility suddenly returned to the stock market after 3 years of gradual VIX decline. S&P 500 made its way down by the biggest intraday plunge since 2011 on October 15 only to recover in the second half and touch the historical highs.

Negative sentiment in the first half of the month was started by disappointing comments on TLTRO by Draghi, and by a steep drop in the German exports, which again deepened doubts about Europe's future. As if this was not enough, following negative factors surfaced: concerns about global economy growth (IMF revision of forecasted GDP), Ebola spreading, and falling prices of energy, mainly oil.

However, we were not too taken by these simple explanations and suspected that US Fed ending its quantitative easing program was lurking in the background.

While reviewing this, we focused on several important questions, such as: 1. Is the high correlation between stock market and Fed's balance sheet going to persist? 2. Is the reduction of the Fed balance sheet (currently above 25% GDP), going to happen and how will it affect the market? 3. Could Fed's flow of cheap money and low lending cost have led to over-leveraging of US companies and artificial inflation of their earnings?

Of course, the questions raised are by no means easy to answer, but after relatively deep analysis we have concluded following:

1. Correlation of market and Fed's balance sheet is far from causality. This is supported by the fact that most of the cheap money stayed at banks' balance sheets as reserves.
2. FED will probably be very cautious about cutting the fat from its balance sheet too fast. It even expressed its preference to keep its assets such as treasuries and commercial mortgages to

maturity of some 10 years and longer.

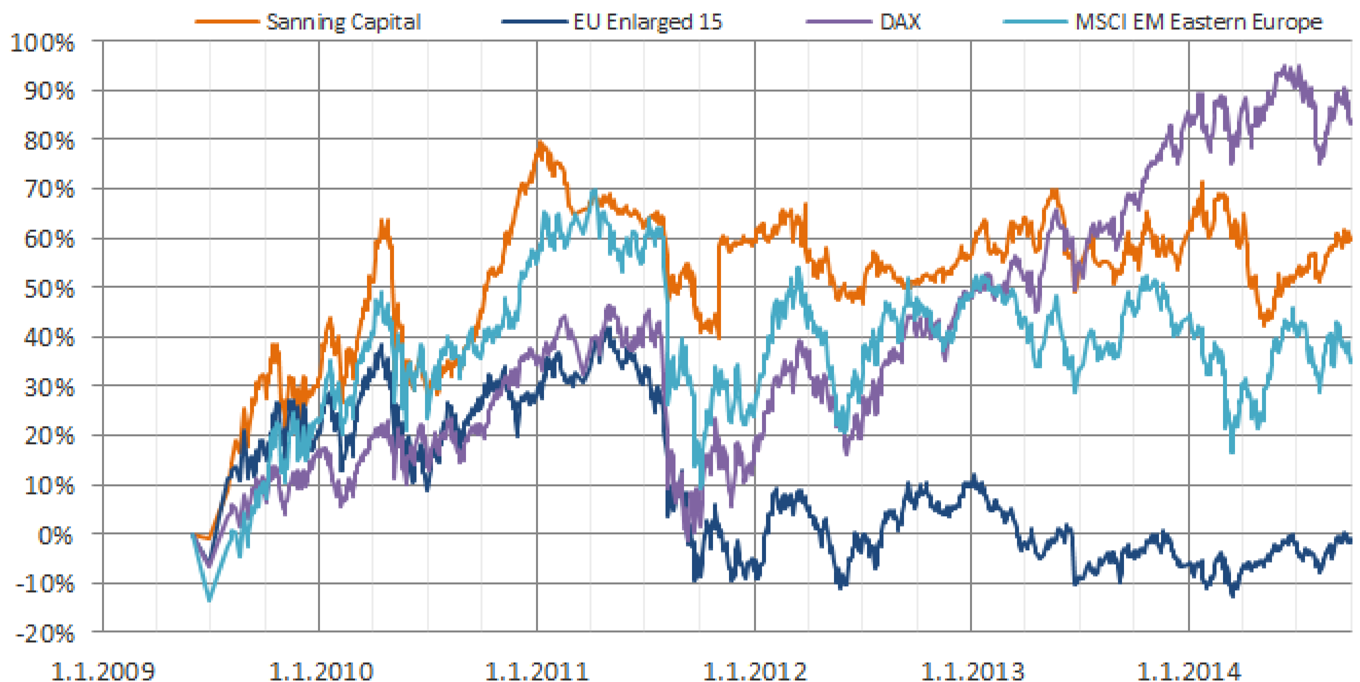
3. The leverage of non-financials has not changed significantly since the start of QE and interest expenses as a part of the EBIT remained flat supporting the view that corporate profit gains are driven by productivity gains.

From all the above we concluded that we don’t believe that Fed’s exit poses a huge risk for stocks at the moment. Moreover, with current valuations we believe that the US market has room to grow.

Quick recovery in the second half of the month somewhat confirmed our thesis by being fueled mostly by positive earnings surprises and actions of ECB and BoJ.

This month we added **1.9%** beating **EU Enlarged 15** (-2.9%), **DAX** (-1.6%) and **MSCI EM** (-1.6%). We underperformed **S&P 500** (2.3%) and **NASDAQ** (3.1%). During the month we stepped into SolarCity position as energy stocks in US plunged due to low oil prices. We believe that oil price does not affect US electricity price directly and thus SolarCity business. Our thought was confirmed by price reversal and we closed the position with 9.2% return.

Fund vs. Indices



Fund Manager

Jan Pravda

Launch Date

2.6.09

Location

Prague

Fund Currency

EUR

Share Price

€ 1 631.70

Performance Fee

20 % HWM

Management Fee

2% p.a.

Cumulative Performance

Period	Sanning[1]	EU Enlarged[2]	MSCI EM EU[2]	DAX	S&P 500	Nasdaq
1 month	1.9%	-2.9%	-1.6%	-1.6%	2.3%	3.1%
3 months	6.5%	2.7%	0.5%	-0.9%	4.5%	6.0%
12 months	2.0%	-2.5%	-11.4%	3.2%	14.9%	18.1%
3 years	15.2%	-6.0%	1.3%	51.9%	61.0%	72.5%
5 years	---	---	---	---	---	---
Since inception (2.6.2009)	**63.2%**	-3.9%	33.3%	81.3%	113.6%	152.1%

Further Characteristics

Beta relative to:			
		Volatility [3]	**18.7%**
EU Enlarged 15	**0.29**	Alpha (vs EU15)	**0.10**
DAX	**0.21**	Sharpe ratio	**0.48**

(1) Net off management fees, gross off performance fees

(2) These two indeces presented only to illustrate performance in 2009-2014, when focused on Central Eastern Europe

(3) Annualized standard deviation since inception

SANNING CAPITAL LIMITED is an opportunity fund based on fundamental research focused on investments into publicly traded companies providing global improvements of eifficiency and/or reduction of consumption of energy, capital and time. It is funded by the managers' own capital and several private investors.

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