Andy Pfaff

From: Andy Pfaff

Sent: 18 February 2008 04:03 PM

Subject: Trendline January 2008 Return 9.88%

Back to our Roots

For about 18 months we grappled with reducing the volatility or our monthly returns in order to conform to the payoff profile of the demographic bulge of the South African hedge fund industry, namely the long-short market-neutral equity fund. We were successful in reducing not only the volatility of the returns, but also the returns themselves, making neither our investors nor ourselves happy.

After a period of introspection we have arrived at the conclusion that, to be true to ourselves & our investment strategy, we must return to our roots. We have identified certain changes introduced into our position management algorithm as responsible for the significant change in the funds' payoff profile. We have therefore determined to revert to the original principles of our investment style, namely cutting the losers & letting the winners run.

This reversion to our earlier position management style will result in the standaanrd deviation of our returns increasing, partly as a result of profits - being the outliers - increasing the dispersion of returns. However the advances in our risk budgeting process and also the broadening of our investment universe will compensate to a degree. We therefore expect the volatility of our returns to increase, but not to the highs of three years ago.

We also believe that we have now put behind us a protracted period that has been frustrating for both investors and managers. In a month in which hedge fund returns have ranged from +10% (Trendline) to -20% (not Trendline), we are nearly at our high water mark, and we look forward to the rest of 2008.

Market comment

The global anxiety in the financial markets reached its' interim capitulation point in late January, culminating in the liquidation of rogue trader Evil Knievals' futures position and $8 billion of the bank's capital with it (Jerome Kerviel from SocGen).

This suited us, and our short equity exposure was profitable from the first business day of 2008. Increasing market volatility resulted in the disciplined reduction of our position sizes, and the reduced equity exposure was not materially hurt by the bounce late in the month. Simultaneous with the equity bounce, our short bond & long commodity positions assumed favourable trends, compensating for the profit give-back by the equity exposure. We therefore approach Trevor Manuel's annual Budget speech with our major position being short of government bonds (please note that this position has been dictated by our long-standing investment process that examines price behaviour alone, and not by any subjective opinion of the contents of the budget).

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regards

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