SIL

NAV 02/08/2019: 25,7976

INVESTMENT TEAM

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QUADRIGA RHO INVESTMENTS

The fund´s objective is to return net positive returns every year, regardless the behavior of traditional assets. To achieve it, the fund allocates to six different strategies: Active, Relative Value, Macro Selection, Micro Selection, Special Situations and Deep Value. The strategies are focused on finding cheap assets with asymmetric profiles.

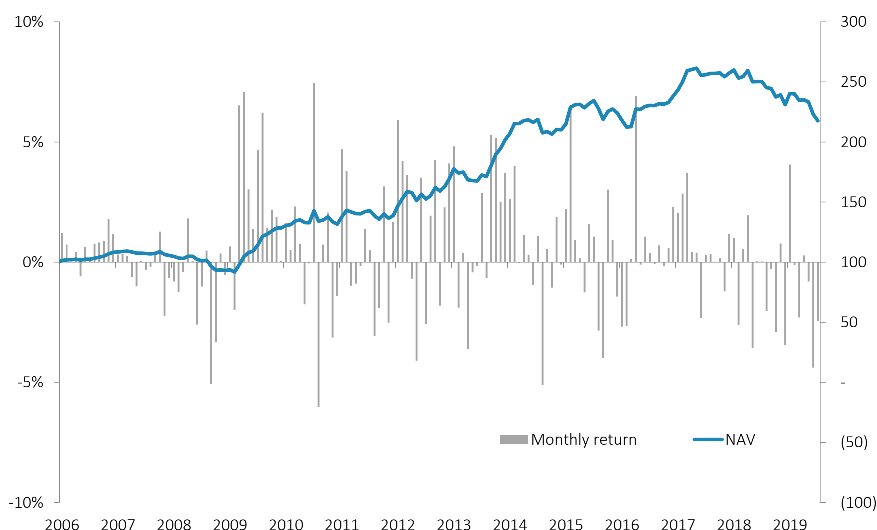
July 2019 Update

Let me start this month´s newsletter with a little self-referential story that illustrates very well the dysfunctionality of monetary policy and the rationale underlying our contrarian bearish stance on European rates. Over year after my full time return to Spain, and having sold my London residence at the top of the market, I got my property mojo and decided it was time to buy a home in Spain. Rather than reinvest the proceeds of the sale into my new residence in Spain I thought that made more sense to invest the money in the fund and borrow as large an LTV as possible vs the value of the new property. The rationale for this trade was solid: I could borrow below 2% fixed for 30 years which made me confident that not only that the long-term annual returns provided by Rho would comfortably the cost of the mortgage but also that inflation would at some point in the life of the mortgage would turn my effective real borrowing rate zero or even lower. It was December 2017. Now over two and a half years later I was reflecting on the wisdom of my property trade **Cont...**

Fund Facts

Structure	SIL
Domicile	Luxembourg
Mgmnt. Fee	0,0%
Perf. Fee	0,0%
Min. Investment (Professional inv.): 50,000€	
Min. Investment (Well-informed inv.): 100,000€	
NAV Currency	EUR
Liquidity	Weekly
ISIN	ES0155144035
Bloomberg Code	S1412 SM
Custodian	Banco Santander

Historical Evolution (% Net) (*)



Monthly Returns (% Net) (*)

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Year
2006	1.2%	0.7%	0.0%	0.4%	-0.6%	0.6%	0.1%	0.8%	0.8%	0.9%	1.8%	1.2%	8.2%
2007	0.3%	0.3%	0.3%	-0.6%	-1.0%	0.1%	-0.3%	-0.2%	0.4%	1.3%	-2.2%	-0.7%	-2.4%
2008	-0.8%	-1.3%	-0.4%	1.8%	0.1%	-2.6%	-1.0%	0.5%	-5.1%	-3.3%	0.4%	-0.5%	-11.8%
2009	0.7%	-2.0%	6.5%	7.1%	3.0%	1.4%	4.7%	6.2%	1.4%	2.2%	1.9%	0.0%	38.0%
2010	1.6%	0.5%	2.3%	0.8%	-1.8%	0.0%	7.4%	-6.0%	0.7%	2.1%	-3.1%	-1.4%	2.5%
2011	4.7%	3.8%	-1.0%	-0.9%	-0.2%	1.4%	0.5%	-3.1%	-1.9%	3.1%	-2.5%	1.7%	5.4%
2012	5.9%	4.2%	3.6%	-0.7%	-4.1%	3.5%	-2.6%	1.9%	4.2%	-1.8%	2.3%	4.1%	22.1%
2013	4.8%	-1.9%	0.4%	-3.6%	-0.4%	-0.2%	2.9%	-0.7%	5.3%	5.2%	2.5%	3.7%	19.0%
2014	2.6%	4.0%	0.0%	1.1%	0.3%	-0.9%	1.1%	-5.1%	0.6%	-1.1%	1.9%	-0.1%	4.2%
2015	2.2%	6.5%	0.9%	0.2%	-1.3%	1.6%	1.1%	-2.8%	-4.0%	3.0%	0.9%	-1.4%	6.7%
2016	-2.7%	-2.6%	-0.8%	7.9%	-0.1%	1.1%	0.4%	-0.1%	0.6%	-0.2%	0.6%	2.3%	6.2%
2017	2.1%	2.9%	3.7%	0.4%	0.4%	-2.3%	0.3%	0.3%	0.0%	0.2%	-1.2%	1.2%	8.0%
2018	1.0%	-2.6%	0.5%	1.2%	0.2%	-3.7%	0.0%	-2.1%	-0.3%	-2.9%	0.8%	-1.8%	-9.4%
2019	4.1%	-0.1%	-2.3%	0.3%	-0.8%	-4.4%	-2.5%						-5.8%

(*) Since inception

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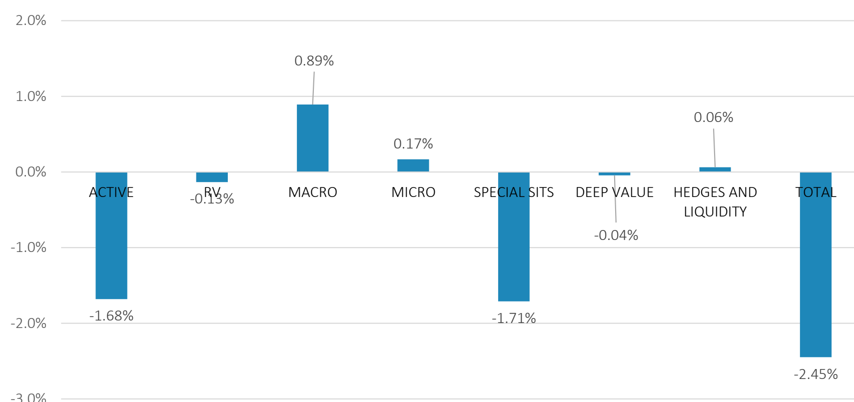
Comparative Risk / Return

	RETURNS (CAGR)			VOLATILITY		
	5 years	3 years	Since inception	5 years	3 years	Since inception
Rho Investments	-0.43%	-2.39%	5.80%	8.33%	6.95%	8.78%
Stoxx 600	3.36%	4.88%	1.84%	12.37%	10.44%	14.23%
Iboxx Eur Corporate	2.65%	1.70%	3.81%	2.69%	2.46%	3.79%

Returns (% Net)

2019	-5.77%
CAGR*	5.80%
July 2019	-2.45%

Performance attribution across strategies (% Net)*



Risk / Return

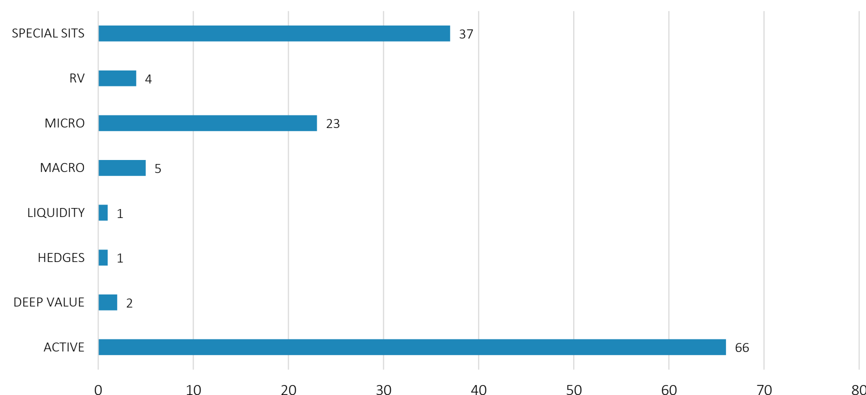
Volatility*	8.72%
Sharpe Ratio*	0.67
Sortino Ratio	0.96
Parametric VaR 1-d	1.34%

Top Five Positions

German Govt. Bond Future	-114.49%
Spanish Gvt. Bond	-15.23%
NATLA Secured Loan	10.73%
BNP Corp. Bond	7.97%
BFCM CORP PERP	5.82%

Risk Concentration and Distribution Metrics

Number of positions per strategy



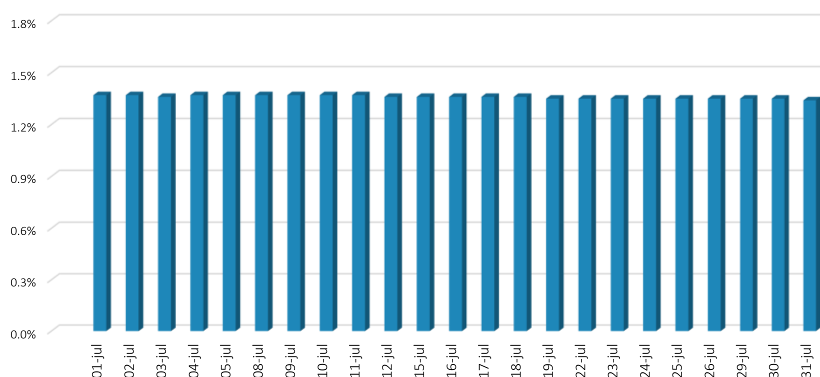
% Exposure

Gross	422.51%
Net	-16.24%

% of Gross Exposure per Strategy

Active	54.67%
Relative value	3.20%
Macro	8.50%
Micro	9.04%
Special Situations	13.55%
Deep Value	1.62%
Hedges	4.18%
Liquidity	5.25%

Var % Contrib Hist 3Y



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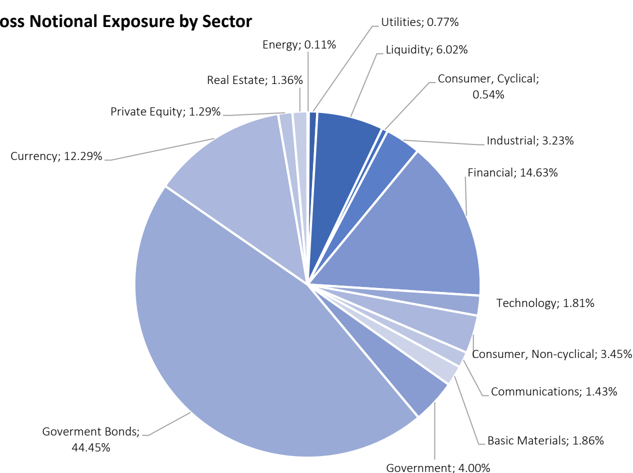
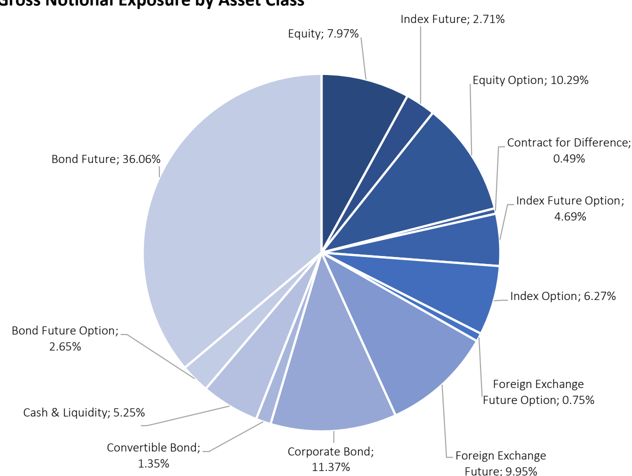
Risk Concentration and Distribution Metrics (2)

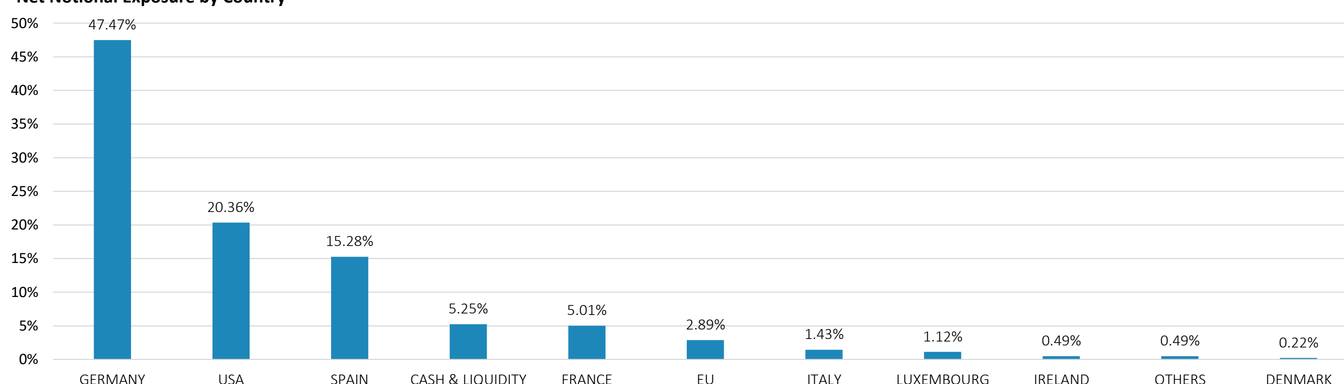
Gross Notional Exposure by Sector



Gross Notional Exposure by Asset Class



Net Notional Exposure by Country



July 2019 Update (cont...)

Cont... in conversations with my wife (I always call upon her exceptional skills at playing devil´s advocate for important decisions!). Based on the strong track record of the fund and the exceptional and extensive experience of all the Rho team members in navigating difficult market conditions I had no doubts that Rho´s returns would outperform the nominal rate on the mortgage over the life of the loan. However, a serious doubt crept into my mind: unlike the timing with my UK property sale, was my borrowing fixed rate for 30 years awfully premature? Had to be! After all, the ECB has facilitated the flow of credit and substantially decreased the cost of borrowing in an effort to reactivate economic activity and bolster household balance sheets. Since the banking system role is to transmit the effects of monetary policy in the context of a highly developed and competitive market place for credit, this cheaper cost of borrowing must been passed on across the curve to some extent, and in the last 20 months 30-year swaps and 30-year Bund rates have come off by approximately 128bps! Oh dear! Indeed my timing surely must have been awful. Being a perennial masochist I needed to know with exactitude what my opportunity cost has been, so I asked my bank for an update as to where are they offering 30-year new mortgages to good clients like my good self. Well, the puzzling answer is that despite a substantial curve inversion and a reduction in reference long-term rates of 1.28%, a new mortgage under same terms would cost me approximately 30bps more, and this is in a context where banks are desperately competing with each other for loan book growth. This did not make any sense. I could only assume that my bank (a particularly conservative one) was taking an insanely prudent stance on lending to the point of being utterly uncompetitive. So I decided to peruse the Bank of Spain macro statistical tables, and these also confirmed that since December 2017, and across all tenors, the average mortgage lending rate (the available statistics do not differentiate between fixed and floating) across all maturities has actually increased between 5 and 34bps. Perversely, according the same tables, the only form of bank credit that has cheapened up significantly is consumer lending, where the average rate has come off between 7 and 76bps (and up to 1% in credit card lending). But hey, why lend at 2% secured if new regulation, monetary repression and comparably favourable returns on capital consumption push you, in these upside world of negative yields, towards four-times more lucrative rates in consumer lending (10.5 times more if we look at credit card lending)?. This is the end of my little story, and apologies if I have dragged on, but I think that from this we can draw some important conclusions: 1) Monetary policy is ineffective because the traditional transmission mechanism is clearly failing in many ways. 2) If we want monetary policy to work we need to make sure that we remove the obstruction to the free flow of money and unprofitable banks render monetary policy ineffective. 3) The current monetary paradigm incentivises an increase of risk in the system to compensate for the “tax” of negative interest rates. 4) With monetary policy rendered ineffective at more negative rates, the only potential way to stimulate growth is through an expansive fiscal policy. Cont...

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July 2019 Update (cont...)

Cont... We think at this stage of the QE experiment that the marginal effect of further cuts in policy rates are actually counterproductive. The vast amounts of new monetary supply created are being deployed in one of two ways. On one hand the wise and prudent, wary of the fragility of this new monetary paradigm are either hoarding cash (potentially physical cash, as the cost of building Fort Knox facility and guarding it with an army of Navy Seals is cheaper than the cost of short-term rates for large portfolios), or otherwise parking it into gold (the lower dollar and lower rates reducing the opportunity cost of owning the shiny metal). On the other hand the bold, the blind believers in the ECB´s bazooka or the Fed´s monetary put, are happy to either park the cash in artificially inflated government bonds (due to a restrictive mandate or regulation that pushes them to do so) or pursue a desperate search for yield and venture in an unsuspecting tourist-like fashion into virtually anything that promises a pick up vs all bonds subject to QE (high yield, private lending, structured credit, stocks, etc.). The result of current policies are an inflation in financial assets and a polarisation in society (the have and have nots in terms of financial assets), but certainly no stimulus to the real economy. We estimate that further ECB policy cuts as currently priced by the market would potentially render 25% of the European banking sector unprofitable. How can the ECB reconcile that with a fluid transmission of monetary policy? We think that the governing council of the ECB will have to make substantial concessions to the banking sector even beyond a deposit tiering which has already been discussed. This makes us think that bank valuations are overly pessimistic and we maintain our bullish stance in domestic banking institutions such as Liberbank and Unicaja, which are not only exceptionally cheap but also both have incredible optionality from an M&A angle. We also think that the ECB will make renewed calls for fiscal support to monetary policy, which constitute the only way to address the social inequality heightened by QE. We believe that disappointment at ECB´s inability to lower rates as to the levels demanded by the markets in current pricing coupled with pressures for further fiscal spending in the medium term will act as repricing catalysts to European rates, and (heavily indebted) peripheral ones in particular. As a result we keep a firm conviction in our contrarian European rates short. These two high convictions amid an otherwise large scepticism surrounding broader risky asset valuations continue to weigh on our performance, and are largely responsible for the fund´s -2.5% drawdown in the month of July. This return compares unfavourably vs the rest of the market, and US stocks in particular. Whilst our Iberian bias typically makes the comparison more straightforward with the Ibex35 (-1.37% total return in the month), our aim remains absolute return generation and we do not compare well with the Eurostoxx 50 (+0.84%), S&P 500 (+2.43% in USD terms), Nasdaq 100 (+2.96% in USD terms) or Itraxx Crossover CDS Index (+0.84%). But then again, we see these broader indices as substantially over valued, stance that has so far been strongly validated in the month of August. Our strategic approach remains the same: Reliance on highly idiosyncratic trades in credit and contrarian calls in stocks and relative value positioning to generate performance, limiting as much as possible directional exposure and correlation to the market. In terms of risk, at the end of July gross market exposure saw a significant increase (largely driven by some additions of relative value positions to the options-driven risk hedges we had already added in June) up to 4.2 from 3.6 times the month before. However, this increase in gross market exposure has to be seen in the context of very small levels of net leverage: -16% at the end of June vs -22% at the end of May. Furthermore overall statistical risk usage measured as 1-day 99.5% confidence VaR decreased from 1.61% at the end of June to 1.34% at the end of July as did daily VaR utilisation which decreased to 1.36% throughout the month of July (vs 1.87% average daily statistical risk employed during the month of June).

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