Bronte Capital
Amalthea Fund

13 December 2013

Investors' Letter for November 2013

This was a month of two halves. During the first half of the month most things went right. The returns you see are from the first two weeks. During the second half we had a few mishaps but mostly stayed flat. It was a good month after all but, by the end, we were getting frustrated.

Running our portfolio is all hard work. It is said that a week is a long time in politics. When you live this, a month feels a long time. From the outside you see the sporadically good returns and they add up. From the inside, all we see is the grind.

The first couple of weeks of December have also been grinding, and we are down a little.

When it feels good and John starts feeling triumphant he always has Simon to put him in his place. We are a team, but only in that we kind of enjoy pricking each other's balloons and there are no hard feelings about it.

Going all Nancy Reagan: Just say no to drugs

Dr Trent Gu is a director of several Bronte funds and has a PhD in genetics. He occasionally helps us with biotechs and Asian stocks.

Given our run in biotech stocks this year, you think we should take seriously Nancy Reagan's famous advice: "just say no to drugs".

Biotech stocks (particularly the highly promoted scams) are stocks you buy to get rich. They

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have super-high beta and in a melt-up market like 2013 they go up very hard. The more promoted, the harder they go up. We have done nothing but lose money on "biodrecks"™ this year. Shorting the hottest stocks in the hottest sectors in a bull market is not much fun.

But then we managed to lose money on the long positions too.

Trent suggested a position in the Sanofi Contingent Value Right (CVR) over the MS drug Lemtrada. MS is an auto-immune disease. Simply put, the immune system attacks your own nervous system, permanently damaging it. Lemtrada is a truly ugly drug. It works by turning the immune system off, hopefully resetting it so that it no longer attacks the body. The drug has horrific side-effects. For example, the risk of dying is about one percent, and there is about a thirty percent chance that the patient's thyroid would get destroyed.

The drug however seems to work for some people. The anecdotal stuff from the MS blogs is very strong. There are people in the trial who swear by it.

However the side-effects data is ugly and the trial could not be designed to meet normal double-blind criteria. [The side-effects are so strong that the patient and doctor would know which drug they are on]. Instead the person who graded the patient's disability level for the trial was meant to be unaware of which drug the patient was on. The European Medicine Agency (EMA) accepted this "rater-blinded" trial design and approved Lemtrada in Europe.

Anyway the FDA staff came out and argued that the drug should not be approved (side effects, bad trial design). An advisory panel took the other view (they treat MS on a day-to-day basis and the anecdotal stuff matters to them). Nevertheless, the CVR collapsed at the cost to you (dear clients) of about a percent and a half.

So this year we have lost on biotech shorts and biotech longs. We wish we had just said no to drugs.

That said, it's unlikely we will. The area is pregnant with scams and we reasonably expect to make money over time. The right response to Nancy Reagan, we believe, is "everything in moderation".

These days we are even shorting biodrecks™ from Japan. (Strangely, those are profitable so far …)

<u>The S&P call insurance policy</u>

Throughout this year we have sunk small amounts of capital into buying way-out-of-the-money S&P calls. We run an aggressive short-book and we were petrified of an extreme late-1999 style melt-up market. The calls were statistically very cheap (they were pricing volatility way below historic volatility) so they were a cheap insurance policy.

The insurance policy calls are now fairly close to the money. At peak we had a few percent of the portfolio invested in S&P calls only just out of the money and with several months to run. If the market continues to rise, this position might wind up very large indeed – however we will almost certainly trim some as the market rises. At the moment, this protects us from a market melt-up. For people who are short-sellers by nature this is comforting.

That said, this position has hurt somewhat in the first weeks of December and (at pixel time) the position is under one percent of the portfolio. [This has not helped the early December results.]. Still, the shorts should now provide more (although partial) protection against market declines. And the insurance is still there to protect against a melt-up market.

Season's Greetings

This being our last letter before Christmas and the start of the New Year, we wish all our investors and friends the compliments of the season. During the year Bronte Capital Management ("Bronte") opened this "Amalthea" fund[1] and also considerably grew its USA and Cayman funds. More importantly, during a strong up market which has seen many fund managers throw in the towel on their short books, ours remains intact. In the New Year, Bronte will welcome new recruits to the business and move to larger offices nearby.

Thanks again

John and Simon

Performance

	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Apr	May	Jun	Fin Year to Date Return	Average Monthly Return
FY13											5.4%	1.3%		2.8%
FY14	6.0%	-2.5%	0.4%	3.6%	5.7%								13.6%	

[1] Not available to USA investors