FIDANTE CAPITAL

Highbridge Multi-Strategy*

Set to exploit market volatility and dislocations

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4 February 2019

Key details	
Bloomberg code	HMSF LN
Share price	210.00p
Last NAV	218.84p
Premium/(discount)	(4.0%)
Market cap	£220.5m
Net assets	£229.8m

Source: the Company, Bloomberg. Data as at 30 January 2019. *Current corporate client of Fidante Capital. Each analyst individually certifies, in relation to each security or issuer referred to in this communication, that (1) the views expressed are an accurate reflection of his/her personal views and (2) no part of his/her compensation is linked directly or indirectly to the views so expressed in this communication. This communication contains written material that a third-party firm has engaged Fidante Partners Europe Limited (trading as "Fidante Capital") to provide on an ongoing basis. The third-party firm has paid Fidante Capital to provide this communication. This communication is made available at the same time to any investment firms who wish to receive it and to the public on www.fidante.com. Accordingly, Fidante Capital is of the view that this communication constitutes a "minor non-monetary benefit". This communication has been disclosed to the third-party firm or the relevant issuer and, where appropriate, included in this communication. This communication will not be regularly updated.

Overview

2018 has been a difficult year for hedge funds and by some measures the asset class had its worst performance since the Global Financial Crisis (GFC). While Highbridge Multi-Strategy Fund (HMSF; the Company) was not able to avoid a negative return in 2018 (its first losing year since launching in 2006, with a NAV return of -2.0%), its NAV performance was significantly better than that of the average hedge fund and, of course, stock markets. This outperformance supports the Company's assessment, that it has a competitive advantage in an environment of high market volatility, and that HMSF can provide stability to a portfolio of other investments, if included, during periods of turbulence.

The Company's assets remain well-managed by one of the highest quality hedge fund managers in the world, Highbridge Capital Management (HCM), which has the experience, developed over more than 25 years, to potentially exploit the rich opportunity set for relative value strategies, the area in which they specialise.

Since 2016, when HCM took over management of the portfolio, substantially all of HMSF's assets have been invested in the Highbridge Multi-Strategy Fund (the Master Fund), an open-ended global multi-strategy hedge fund managed by HCM, launched in 1992 and diversified across a wide range of relative value strategies. The Master Fund targets an annualised return of 7-12%, an annualised volatility of 3-6% and a beta to the S&P 500 index of less than 25%.

Both HMSF and the Master Fund have generated good absolute and relative risk-adjusted returns over a number of years, with low/negative beta/correlation to equity markets. The Master Fund has delivered an annualised NAV return of 5.3% over the seven years since the current CIO at HCM, Mark Vanacore, took over at the start of 2012, with an annualised volatility of 3.4% and a beta/correlation to the S&P 500 index of 13.5%/42.9%.

Overall, the Master Fund was able to protect capital relatively well in what were difficult market conditions. Several of the sub-strategies within the Master Fund portfolio were able to thrive in the volatility that gripped the markets at various times in 2018. However, one sub-strategy contributed a loss during the year more than three times greater than the second worst performing sub-strategy and has now been removed from the portfolio – relative underperformance over time also contributed to the removal of this sub-strategy.

HCM has made changes to the make-up of the Master Fund portfolio through 2018 with the aim of helping ensure that it can benefit from the new market conditions, notably the elevated market volatility, which they believe is here to stay. This positioning has contributed to the very good start in January 2019 (HMSF has returned 1.7% up to 25 January 2019), with positive performance derived from a range of high conviction sub-strategies. We believe that this breadth of sources of return bodes well for the prospects in 2019.

During the first eleven months of 2018, the Company's shares traded at a small premium of 0.2% on average, the best rating amongst the established single manager listed hedge funds, but in December 2018 the shares started to decline sharply, taking the discount to around 3.8% by the end of 2018. Since then, the shares have stabilised at around the 4.0% discount level. We believe this sell-off was, at least in part, due to the overall increase in risk aversion in capital markets in the last three months of 2018. This may prove to be an attractive entry level, especially if the NAV recovers further from this point.

The Company sold c. £18.9m of shares out of treasury in 2018, to help manage the premium. Since the discount started to widen again in December 2018, share buybacks have resumed, with c. £1.8m of shares repurchased to date.

Source: Fidante Capital, the Company, HCM. Past performance is not a reliable indicator of future results.

SWOT analysis

Strengths	Weaknesses
• The Master Fund has generated consistent returns since launch in 1992, with only four of the 26 full years showing negative performance and 2018 being the first losing year since 2011; furthermore, the returns have had low beta to traditional assets such as equities and bonds. These returns were also above traditional fixed income returns. with fixed income-like volatility. • The shares are currently trading at a c. 4.0% discount, having traded at a small premium of around 0.2% on average over the first eleven months of 2018 – this may represent a good entry point for new shareholders. • The Company has been a net issuer of shares out of treasury since the start of 2018, which has boosted liquidity and underpins potential future growth prospects. • The investment manager, Highbridge Capital Management, is highly experienced in managing funds investing in relative value hedge fund strategies, having done so for more than 25 years, and is institutional in nature.	• Liquidity in the Company's shares has been limited (typically their liquidity is in the middle of the pack compared to the other listed single manager hedge funds, both in absolute terms and market cap-adjusted); however, this may improve if the Company is able to grow assets under management further.
Opportunities	**Threats**
• The Company's NAV performance may benefit from higher levels of market volatility and from generally rising short-term rates. • The Company has few peers in the diversified, listed single manager hedge fund universe - there are ten investment companies classified as listed single manager hedge funds, but only two of these companies have a similar diversified investment approach to HMSF. If the Company's NAV and share price performance improves, it has the potential to grow its net assets and become more established amongst its direct competitors. • The Master Fund portfolio is very diversified by sub-strategy and this, together with the sub-strategy turnover, suggests that the managers are willing and able to proactively alter exposures in order to drive performance.	• If traditional asset classes such as equities continue the good performance of 2019 so far, following the sell-off in Q4 2018, while bond yields rise as central banks normalise rates, it will become increasingly difficult to engage investors in the relative value strategies adopted by the Company. However, if the market volatility continues, the Company should be able to act as a diversifier and preserve capital while generating consistent uncorrelated returns.

Source: Fidante Capital. Past performance is not a reliable indicator of future results.

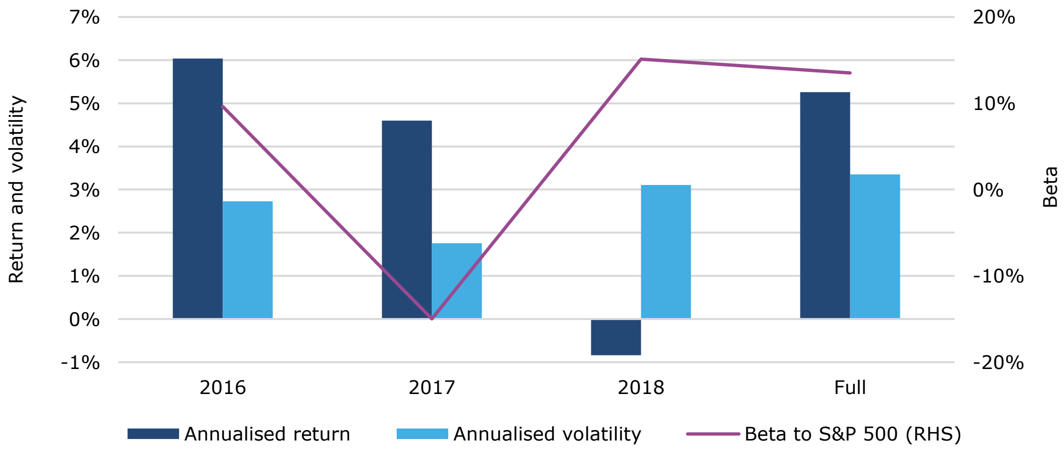
Highbridge Multi-Strategy Fund – Master Fund

Introduction

Highbridge Capital Management (HCM), founded in 1992, was a pioneer amongst multi-strategy hedge fund managers. The firm's headquarters are in New York, with investment offices in London and Hong Kong. HCM has around 160 employees, of which more than 50 are investment professionals. HCM currently has assets under management of $4.0bn (as at 1 January 2019), all of which is in hedge funds. The Highbridge Multi-Strategy Fund (the Master Fund) has assets under management of around $2.8bn. The CIO at HCM is Mark Vanacore, who joined at the firm's founding in 1992. He has had sole responsibility for the asset allocation within the Master Fund since January 2012. Each of the sub-strategies within the Master Fund is managed by a team headed by an experienced portfolio manager.

For the seven years since Mark Vanacore became the CIO in January 2012, the Master Fund has generated an annualised return of 5.3% and an annualised volatility of 3.4%. The net beta to the S&P 500 index has been 13.5%, and the correlation to that same equity index was 42.9%. The average rolling 12-month excess return over the risk-free rate has, over this period, been 480bps.

Fig 1: Master Fund performance



Source: Fidante Capital, HCM. For the USD shares, to 31 December 2018. "Full" indicates since Mark Vanacore became CIO at HCM in January 2012. Past performance is not a reliable indicator of future results.

Strategy changes

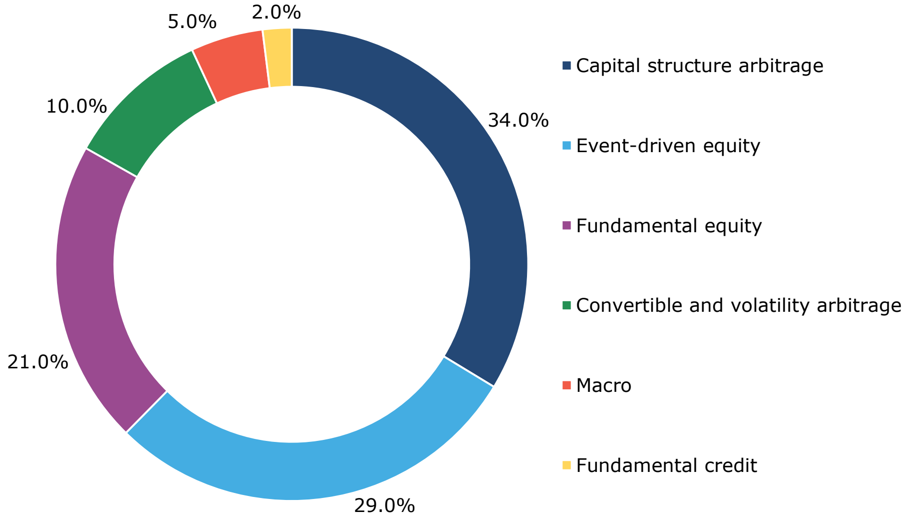
HCM have made some (sub-)strategy changes to the Master Fund's portfolio since the start of 2018. Generally, these adjustments were made to better position the portfolio in response to the evolving market conditions, notably the increased volatility. More specifically, the introduction of new strategies and increased allocations to existing strategies were driven by good performance, and/or the identification of new opportunities, and/or increasingly favourable environments for those strategies – the converse was true for strategy removals and underweightings. The changes made (summarised in a table in the Appendix) were as follows:

- on 1 January 2018, the event-focused North American long/short equity sub-strategy was removed due to its sub-optimal risk/return ratio – some of the team's personnel were kept on and started running a smaller amount of capital within the US event long/short equity sub-strategy;
- also at the start of 2018, the real estate long/short equity sub-strategy was rolled into sector-focused long/short equity;
- an emerging markets rates/macro strategy was introduced to the Master Fund in

January 2018, as part of the fundamental macro sub-strategy;
- the statistical arbitrage sub-strategy (and hence the quantitative equity strategy) was removed during Q3 2018 because of its sustained period of underperformance;
- a new sub-strategy, convergence long/short equity, was added at the end of Q3 2018 – this is part of the fundamental equity strategy and its aim is to benefit from themes suggesting sector convergence (it currently covers the TMT, consumer and industrial sectors);
- at the end of 2018, the sector-focused long/short equity sub-strategy was removed from the portfolio, having been reduced dramatically during the year due to its sub-optimal risk/return ratio.

The Master Fund now has a globally diversified allocation to six broad investment strategies and 13 sub-strategies across equity, credit, convertibles, capital structure and macro. The three largest strategy allocations within the Master Fund's portfolio are capital structure arbitrage, event-driven equity and fundamental equity. Overall, the predominant exposure is to relative value strategies - these have proven to be the most stable and reliable investment strategies in the past.

Fig 2: Master Fund strategy exposures



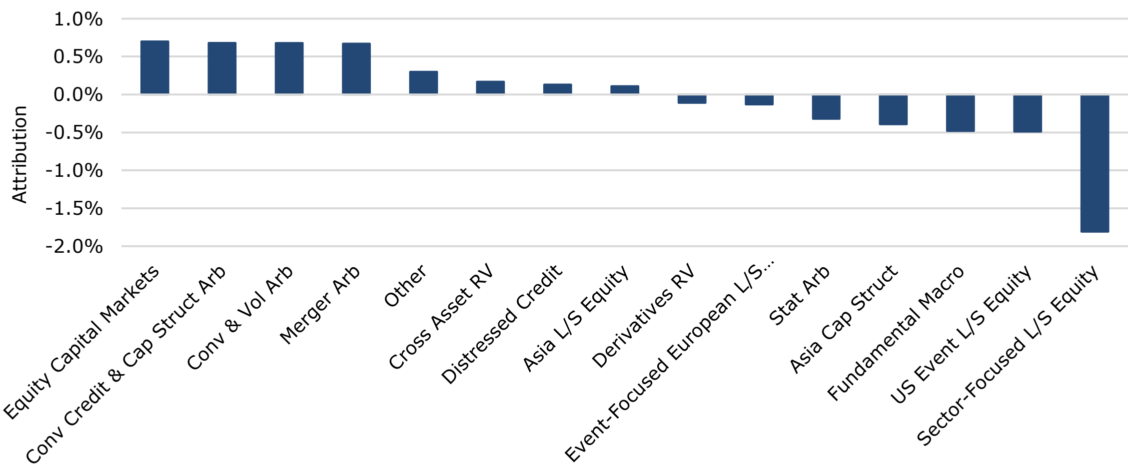
Source: Fidante Capital, HCM. As at 1 January 2019.

Performance

The Master Fund returned -0.84% in 2018 (net; in USD). Overall, capital was protected relatively well in difficult market conditions. In terms of sub-strategy contributions during the year, the largest (gross) contributions to positive performance came from equity capital markets, convertible credit and capital structure arbitrage, convertible & volatility arbitrage and merger arbitrage (each of the four sub-strategies contributed around +0.7%), which thrived in the volatility that gripped the markets at various times in 2018.

The largest loss was generated by sector-focused long/short equity, which contributed -1.8%, having found it difficult to make profits in the prevailing equity market environment, despite having low-beta characteristics. As noted above, this sub-strategy was removed from the portfolio at the end of 2018, with the portfolio managers trading on behalf of this sub-strategy having been "let go" as the year progressed.

Fig 3: Sub-strategy contributions to Master Fund performance in 2018



Source: Fidante Capital, HCM. Past performance is not a reliable indicator of future results.

Manager outlook

Looking ahead, HCM believe that the current market volatility is here to stay. They are seeing attractive investment opportunities across a wide range of strategies following the market sell-off in Q4 2018, which has led to several market dislocations. The actions taken by HCM during 2018 with respect to (sub-)strategy exposures mean that they feel confident going into 2019, more so than they were at the start of 2018. The portfolio is still low-beta and:

- is more simplified than before, with fewer (sub-)strategies;
- has a larger exposure to HCM's higher conviction (sub-)strategies and portfolio managers; and
- is positioned to be able to benefit from the credit and stock picking opportunities that exist.

A couple of the more dislocated segments of the financial markets at the start of 2019 are:

- Japanese equities – cyclical growth stocks sold off sharply in Q4 2018, with industrials and tech stocks in particular trading at very low multiples; these assets were trading at very distressed prices, creating attractive opportunities for derivative structuring; exposure within the Master Fund portfolio has been increased to the relevant strategies;
- cross-asset relative value - this sub-strategy invests in the debt versus equity of single name corporates, mainly in the US - for the first three quarters of 2018, credit held up well, but in the final quarter there were large downward moves in single name corporate credits which were out of line with the fundamentals of the companies in question and with the equity.

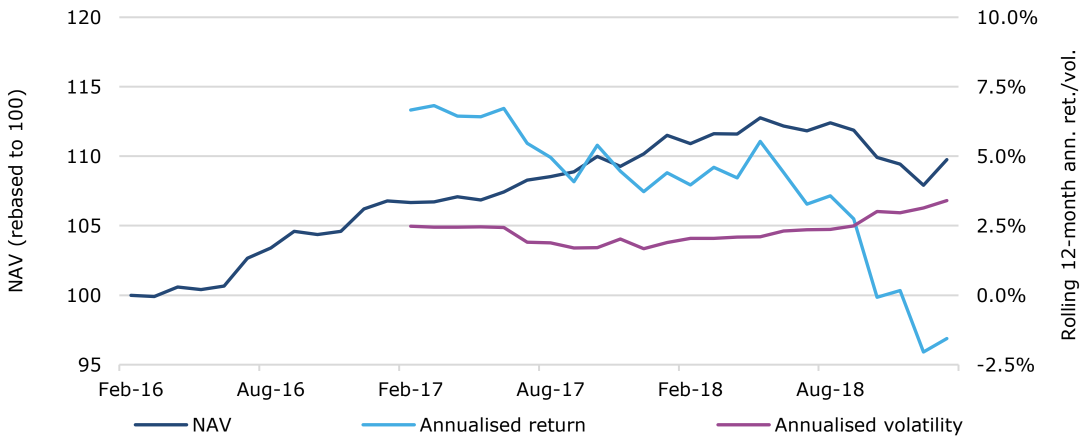
The changes made to the Master Fund portfolio over the course of 2018 have contributed to the very good start in January 2019 (HMSF has returned 1.7% up to 25 January 2019) following the recoveries seen in Asian equity and in credit. Positive contributions to the performance in January have come from a range of different strategies in the Master Fund portfolio, including Asia strategies, cross asset relative value and convergence equity long/short, which we believe bodes well for the prospects in 2019.

HMSF NAV, share price and rating

The Company's net assets stood at around £229.8m as at 25 January 2019. There remains an exposure of around 0.5% to certain legacy positions which are in the process of being liquidated. Cash and cash equivalents were around 1.0% of the Company's net assets as at the end of 2018.

Based on monthly NAV performance data, the Company's annualised NAV return and volatility since HCM was appointed investment manager (on 29 February 2016) to the end of 2018, have been 2.7% and 2.7%, respectively. From mid-2016, the HMSF net asset value per share climbed steadily and was up c. 12% by August 2018, in part due to the quarterly tender offer in October 2016 (for c. £54m) and share repurchases (c. £4m in 2016 and c. £12m in 2017).

Fig 4: HMSF NAV performance – rolling 12-month annualised return and volatility



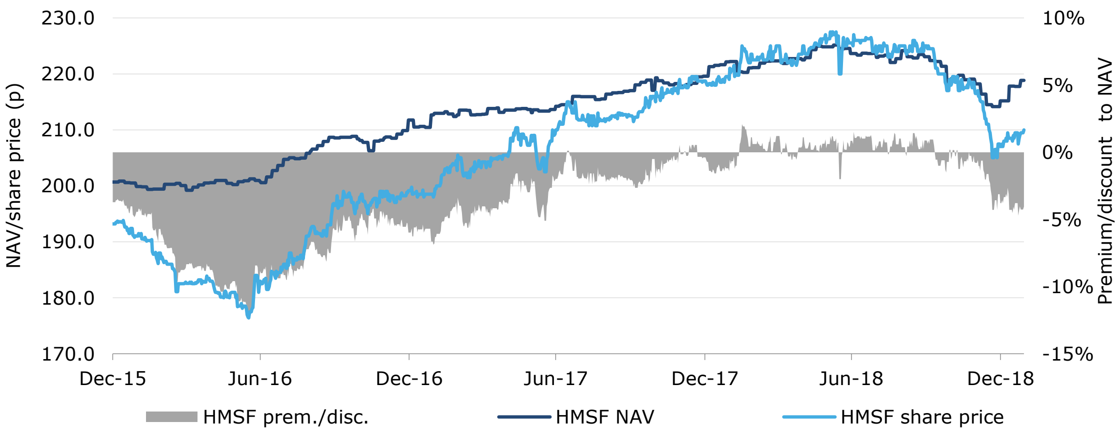
Source: Fidante Capital, the Company. From 28 February 2016 to 25 January 2019. The NAV performance to 25 January 2019 has been taken as the performance for January 2019. Past performance is not a reliable indicator of future results.

The share price discount to NAV was at its widest in the middle of 2016 (around 12%) but it reduced gradually thereafter, reaching par towards the end of 2017. The shares traded at a small premium of 0.2% on average during the first eleven months of 2018, but in December 2018 the shares started to fall off sharply, taking the discount to around 3.8% by the end of 2018. Since then, the shares have stabilised at around the 4.0% discount level, its widest since the middle of 2017. We believe this sell-off was, at least in part, due to the overall increase in risk aversion in capital markets in the last three months of 2018.

The stabilisation of the Company's share price discount to NAV, along with equity markets, in late 2018 and early 2019, indicates that the current discount is more a reflection of general market sentiment (and an indiscriminate aversion to hedge funds independent of their track record and 2018 performance) and not a reflection of deteriorating fundamentals of the Company. Hence, we believe that this pullback in the share price represents a good entry point, especially if the NAV starts to recover in 2019 and investor risk aversion continues to subside.

The Company sold c. £18.9m of shares out of treasury in 2018, to help manage the premium. Since the discount started to widen again in mid-December 2018, share buybacks have resumed, with c. £1.8m of shares repurchased to date.

Fig 5: HMSF share price premium/discount to NAV



Source: Fidante Capital, the Company, Bloomberg. From 1 January 2016 to 29 January 2019. Premium/discount is for the share price with respect to the most recent NAV. Past performance is not a reliable indicator of future results.

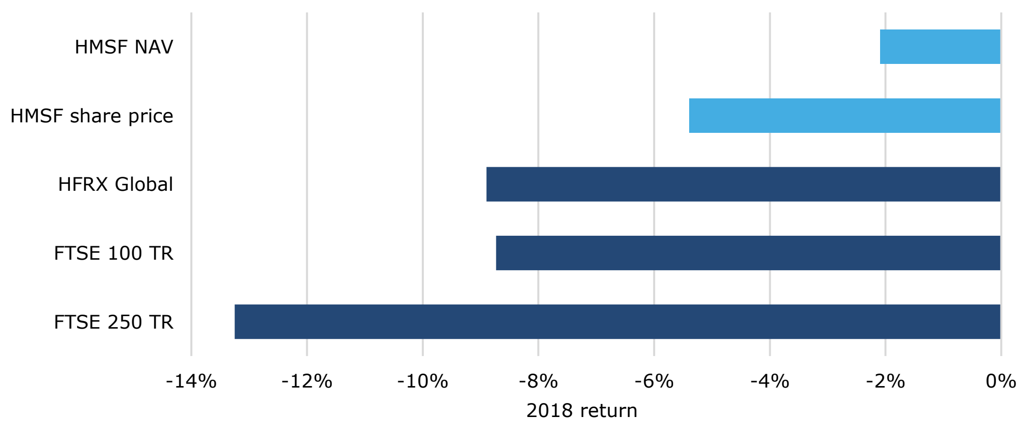
HMSF outperformed in a difficult year

The NAV performance in 2018 (down around 2.0% in Sterling), together with a 5.4% loss for the share price (also in Sterling), was the Company's first negative annual performance since its launch in 2006. However, in a year when practically all asset classes, from bonds to equities to hedge funds, generated negative returns, and when only money market instruments managed to create positive returns, a small decline of 2.0% in the NAV should be considered a good result. In Fig. 6 we compare the performance of the Company's NAV and share price with the HFRX Global Hedge Fund Index and the UK stock market in 2018. Compared to the average hedge fund, HMSF's shares outperformed by 3.5% in 2018 and the NAV outperformed by 6.8%. The outperformance of HMSF to the FTSE 100 and FTSE 250 indices were 6.6% and 11.2%, respectively, if we use the NAV of HMSF as a comparison (3.3% and 7.9%, respectively, using the HMSF share price). These results indicate that HMSF would have been able to protect investors against potentially larger losses in their portfolios, if included, when compared to investments in equities and the average hedge fund.

The ability of HMSF to offer protection in declining markets can be better appreciated in Fig. 7, which shows the drawdowns through the calendar of 2018 for the different track records appearing in Fig. 6. Only on rare occasions during the year did the drawdown of the Company's NAV or its share price exceed the losses in other hedge funds (as measured by the HFRX index) or the stock market. Furthermore, in the first three quarters of 2018, because the HMSF drawdowns were so small, any losses were quickly recovered. In effect, during much of the first half of 2018, the NAV performance of HMSF was positive, while the average hedge fund showed drawdowns of 3% to 5% and equity markets suffered temporary setbacks of up to 10%.

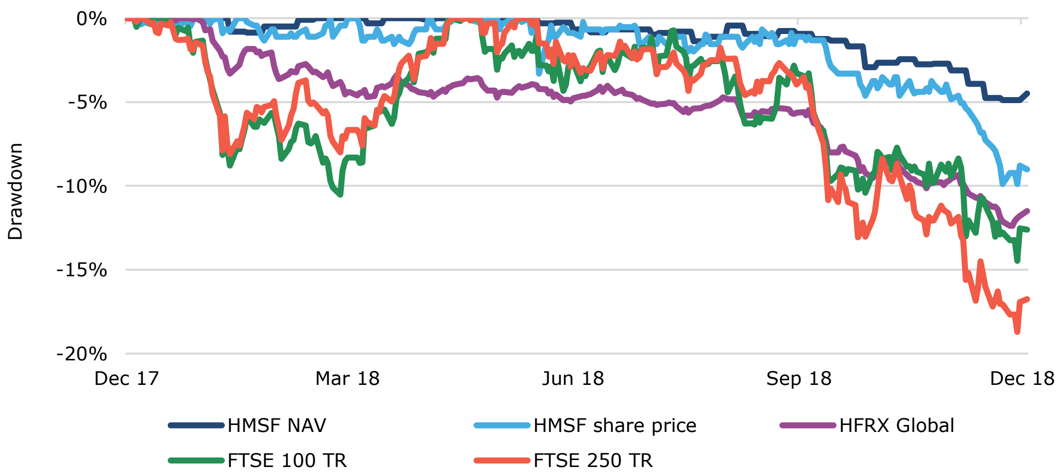
It was only in the fourth quarter of 2018, when all asset classes declined and risk aversion increased materially, that drawdowns in HMSF's NAV and share price became larger. But throughout Q4 2018, the HMSF NAV drawdowns remained much lower than for other hedge funds and for stocks. The performance advantage for HMSF's shares remained at c. 5% throughout most of the fourth quarter of 2018 and only declined in the second half of December, when the sell-off in risk assets reached its peak and investor sentiment turned sharply negative. It is important to note that during December 2018 the NAV of the Company declined much less than the share price, indicating that investors were, to some extent, selling the shares indiscriminately and without consideration of the fundamental performance of the Company's portfolio.

Fig 6: HMSF performance in 2018 compared to indices



Source: Fidante Capital, Bloomberg. Past performance is not a reliable indicator of future results.

Fig 7: HMSF maximum drawdown in 2018 compared to indices



Source: Fidante Capital, Bloomberg. Past performance is not a reliable indicator of future results.

Appendix

Fig 8: Key features of HMSF

Company	Highbridge Multi-Strategy Fund Ltd.
Sector	Listed hedge funds
Listing	Official List, admitted to trading on the Main Market of the LSE
	25 May 2006
Domicile	Guernsey
Share class	GBP
Management	Highbridge Capital Management is the investment manager; Mark Vanacore is the CIO; the Company has an independent, non-executive board
Investment objective	To seek consistent returns with low volatility through an investment policy of investing substantially all of its assets in the Highbridge Multi-Strategy Fund
Target performance	Target annualised return (net): 7%-12%; annualised volatility (net): 3%-6%; target beta to S&P 500 (net): < 25% (all for the Master Fund)
Dividends	Dividends not paid
Gearing	At the Company level, non-structural borrowing up to 10% of net assets at the time of drawing, to manage cashflows, meet expenses and fund share repurchases; the Master Fund leverage typically ranges from 2x – 4x
FX hedging	Non-GBP underlying FX exposures are hedged into GBP (the base currency)
Fees	No management or performance fees at the Company level; management fee at the underlying fund level of 1.50% per annum for assets invested in the Master Fund of up to £250m and 1.25% for assets invested of more than £250m; performance fee at the Master Fund level of 20% of profits (realised and unrealised) per annum with high watermark
Ongoing charges*	0.28% (excluding management fees)
Reporting	December year-end; weekly and monthly NAV estimates
Discount management	Quarterly redemption facility for up to 20% of the issued share capital, at the board's discretion; continuation vote at AGM in 2021 and every five years thereafter; share repurchases
Life	Unlimited, subject to the five-yearly continuation vote in 2021 and every five years thereafter
Board	Vic Holmes (Chairman), Paul Le Page (Senior Independent Director, Chairman of the Investment and Market Risk Committee), Steve Le Page (Chairman of the Audit Committee and Chairman of the Management and Remuneration Committee), Sarita Keen; all directors non-executive and independent
Website	https://www.highbridgemsfltd.co.uk

Source: Fidante Capital, the Company. * Ratio of operating expenses to average net assets for H1 2018, annualised.

Fig 9: HMSF NAV returns (%, GBP)

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Year
2016	-0.52	-0.27	-0.10	0.69	-0.19	0.26	1.99	0.72	1.15	-0.23	0.23	1.53	5.36
2017	0.55	-0.12	0.05	0.33	-0.21	0.55	0.78	0.24	0.31	1.02	-0.66	0.82	3.73
2018	1.21	-0.53	0.65	-0.03	1.05	-0.52	-0.32	0.53	-0.49	-1.75	-0.42	-1.40	-2.04
2019	1.71												1.71

Source: Fidante Capital, the Company. To 25 January 2019. The shaded cells (January and February 2016) show the period during which BlueCrest Capital Management was still the Company's Investment Manager. Past performance is not a reliable indicator of future results.

Fig 10: Master Fund sub-strategy changes in 2018

Date	Sub-strategy	Change	Reason
1 Jan. 2018	Event-focused North American L/S equity	Removed	Sub-optimal risk/return ratio
1 Jan. 2018	Real estate L/S equity	Rolled into sector-focused L/S equity	Rationalisation
Jan. 2018	Fundamental macro	Emerging markets rates/macro strategy introduced	New opportunity identified
Q3 2018	Statistical arbitrage	Removed	Sustained underperformance
1 Oct. 2018	Convergence L/S equity	Added to fundamental equity	New opportunity identified
1 Jan. 2019	Sector-focused L/S equity	Removed	Sub-optimal risk/return ratio

Source: Fidante Capital, HCM. "L/S" denotes long/short.

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