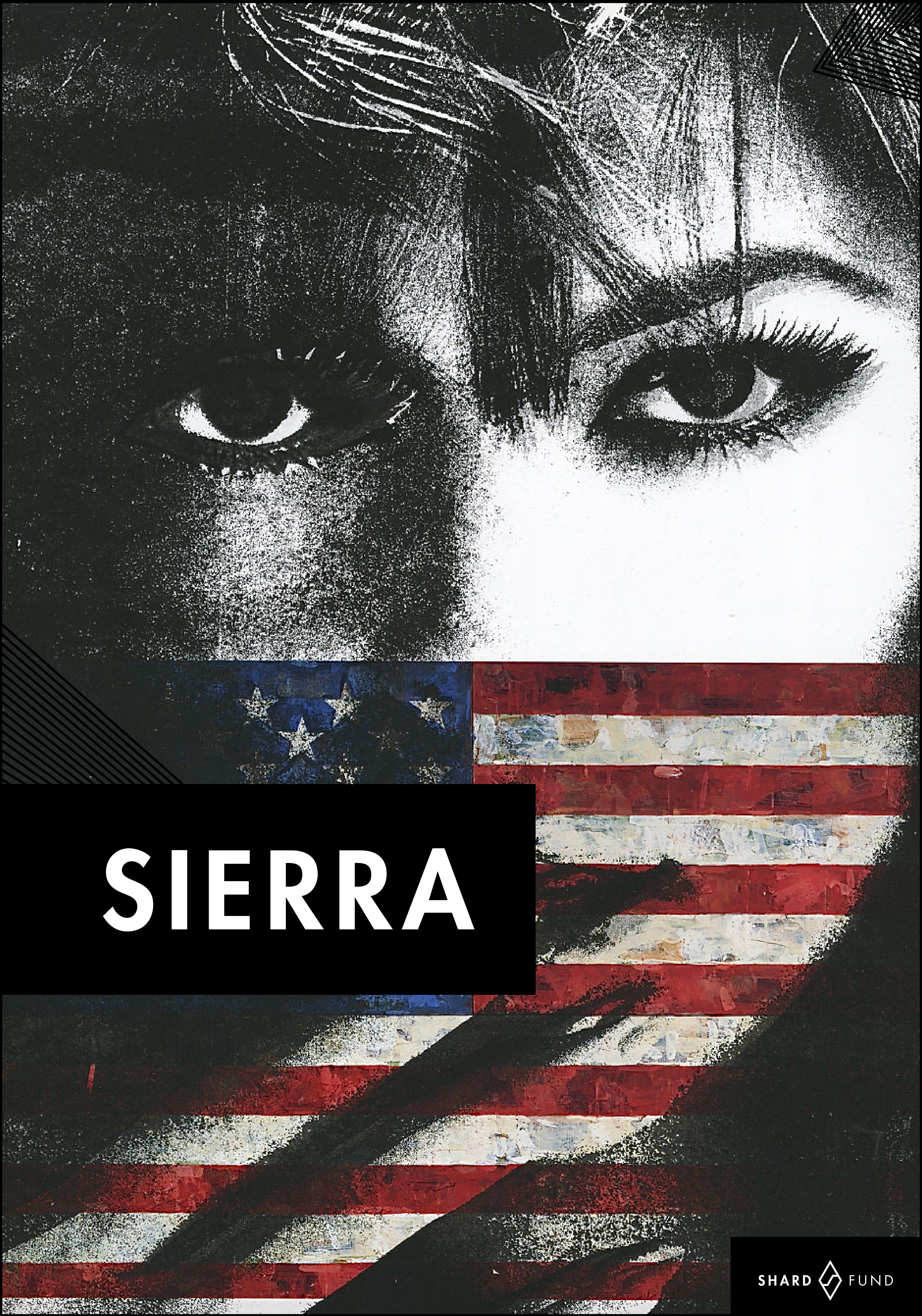
SIERRA



SHARD FUND

A JOURNEY ACROSS FINANCIAL MARKETS

January 1st - December 31st, 2013 | End of 2013 Issue

TEAM:

Stelian Nenkov
Georgi Stanoev
Petar Tsachev
Ivan Nachev

CONTRIBUTORS: David Twomey; Contributor/Editor

USA

Living the American Dream

Highlights of 2013:

- S&P 500 up 30% in 2013 (best since 1997)
- US 10yr Treasury yield finishes the year at 3.03% (up from 1.84% on Jan. 2nd)
- Q3 Final GDP rose 4.1% (highest since Q4 2011)
- USD (measured by the DXY index) basically unchanged at 80
- The Federal Reserve decreased its asset purchases program by USD 10 billion
- Once again officials in Washington showed their incompetence and caused a 2-week government shutdown that almost ended up with a default (not really...)

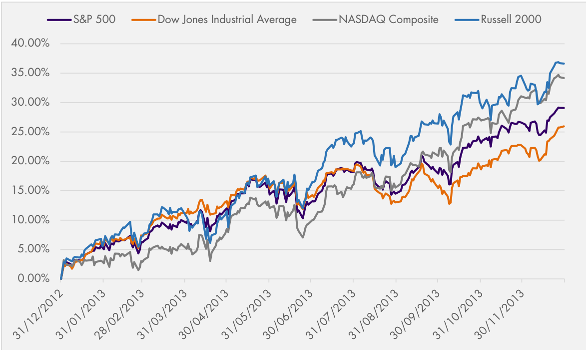
If you are a stock market participant who made a wish on 31st of December 2012 for a strong year, you definitely got more than you expected. The US stock market and economy absolutely crushed expectations of major banks and other experts. But that's the thing about estimates, they are very subjective, based on personal views and emotions, as well as different ways of calculations.

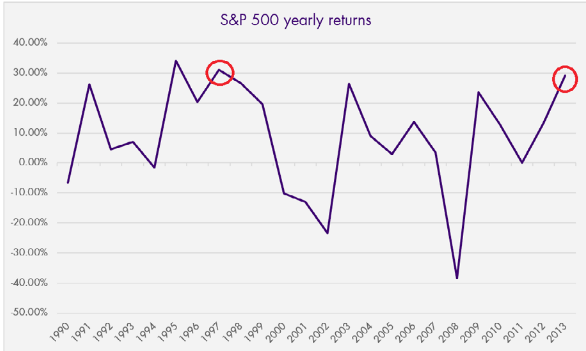
Firm	S&P 500 Target	Missed by (as of 10.12.2013)
Wells Fargo	1,390	29.70%
UBS	1,425	26.50%
Morgan Stanley	1,434	25.70%
Deutsche Bank	1,500	20.20%
Barclays	1,525	18.20%
Credit Suisse	1,550	16.30%
HSBC	1,560	15.60%
Jefferies	1,565	15.20%
Goldman Sachs	1,575	14.50%
BMO Capital	1,575	14.50%
JP Morgan	1,580	14.10%
Oppenheimer	1,585	13.80%
BofA	1,600	12.70%
Citi	1,615	11.60%
AVERAGE	**1,534**	**17.50%**
MEDIAN	**1,560**	**15.60%**

With estimates so low, the year-long surprise to the upside (by economic activity and earnings) fueled new all-time highs, as well as the highest returns in more than a decade.
The sector performance tells us a relatively straightforward story. Cyclical sectors are the top performers this year, while, except Healthcare, other defensive sectors underperform, with Utilities being the absolute loser this year. This is important, as cyclical sectors tend to accelerate with growth, while defensive companies usually pay high dividends and are related to slower economic growth. This tendency has been well illustrated this year. A range of indicators suggested an increasingly healthier economy, also captured by economic output, which

Consumer Discretionary	40.88%
Healthcare	39.02%
Industrials	37.89%
Financials	33.37%
Energy	23.93%
Technology	23.88%
Consumer Staples	23.15%
Materials	23.12%
Utilities	8.73%

accelerated in three consecutive quarters. Overall, except certain high volatility moments caused by central planners, US indices have increased quite uninterrupted. Their performance also suggest a strong growth year, with the volatile Russell 2000 index (small caps) being the top performer, while Dow Jones Industrial Average (stable blue chips) scoring the lowest return (which also stands quite high at 25%).

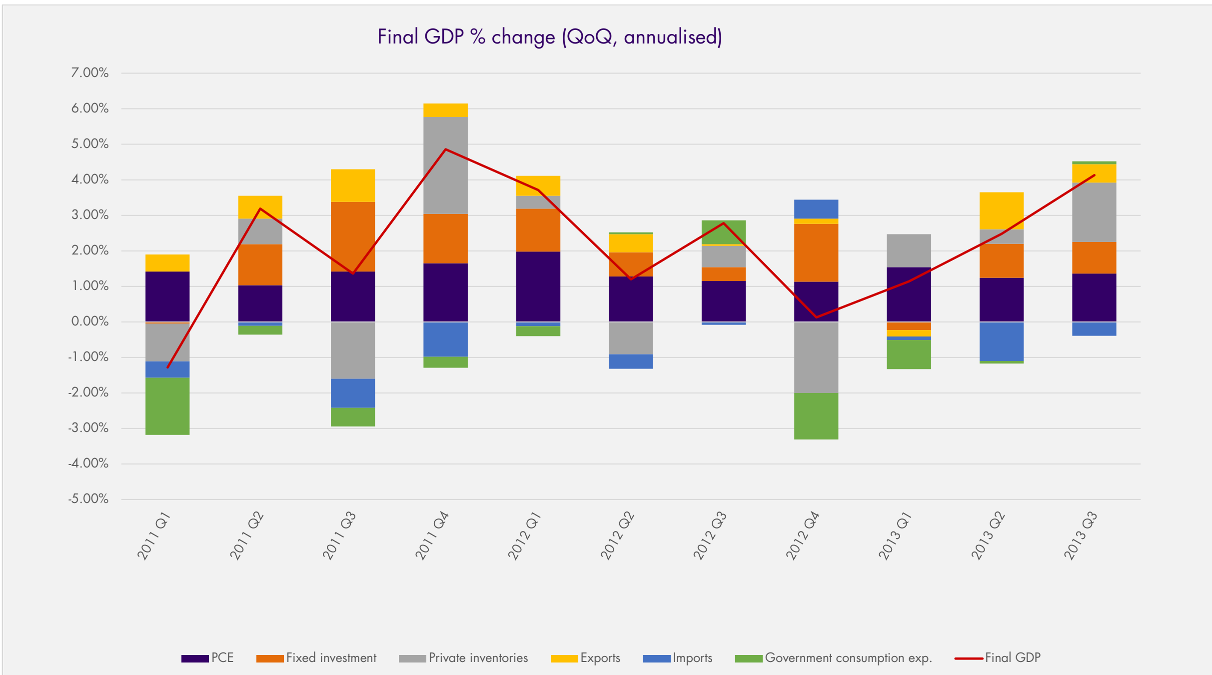




THE YEAR IN GRAPHS

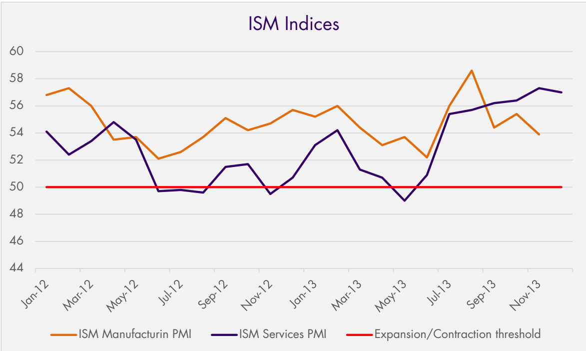
GDP

Against all expectations, the economy expanded with a surprising pace. Three consecutive quarters of faster growth brought the economy to an expansion of 4.1% (annualised) in Q3, compared to only 0.14% in Q4 2012. Many market participants blamed higher private inventories for that 'unjustified' growth, however, we are not too concerned about that. If personal consumption expenditure goes back to its average level, it will offset any decline in private inventories or even push GDP growth even higher.



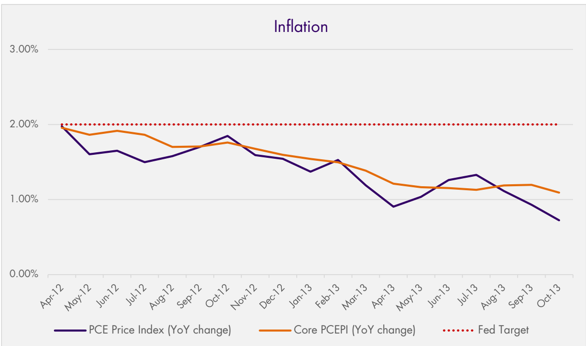
ISM

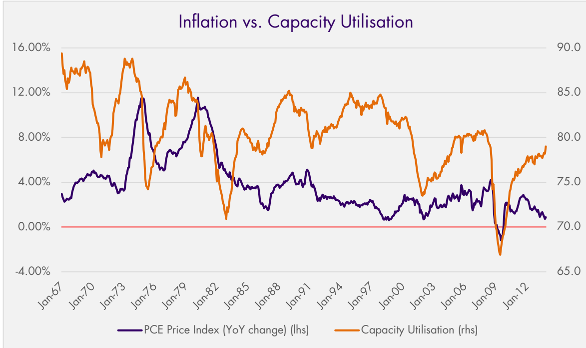
The year began slowly for the ISM indices, but then gradually picked up and accelerated considerably in the second half of the year. The strong increase is consistent with both the improving labour market and overall economy. In September, there wasn't much consistency in this or any other data, so, as we had predicted, the Fed decided to wait more before reducing its asset purchases. That changed in December, after a solid run in many indicators. Judging by the close correlation between the ISM manufacturing index and GDP growth, we expect a strong Q4 number, to conclude a great year for US economy and markets.



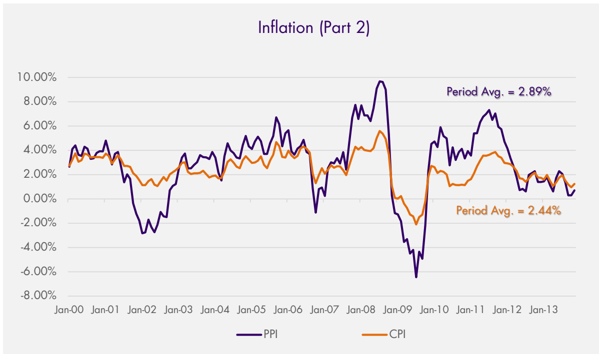
INFLATION

Inflation is still quite low, which is strange, considering all the money going into the overall marketplace. But that's a topic for another conversation. With inflation so low, one might question if the economy is actually getting better. Also looking at the Fed target, we might expect a slower pace of reduction in asset purchases if inflation doesn't start to



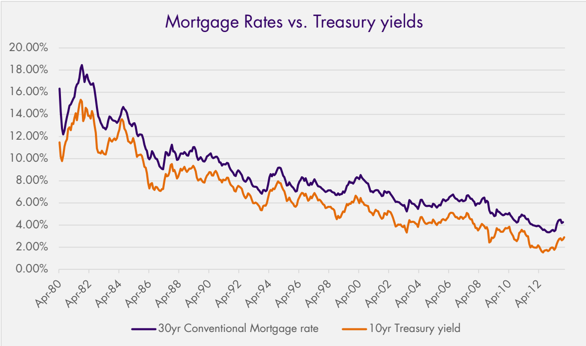


tick up any time soon. Considering the power of capacity utilisation as an indicator driving inflation, it is fair to say that inflation should start expanding in following months and reach Fed's target as projected. Also, increasing demand driven by higher sentiment should help. However, capacity utilisation also tells us another thing. There is an upper-limit for inflation, which is consistently getting lower, due to decade-after-decade downward trend in capacity utilisation. Thus, using all-time averages for inflation might be wrong, as there is a mega-trend interrupting a potential mean-reversion. Instead, we prefer using decade-long (more or less) averages.

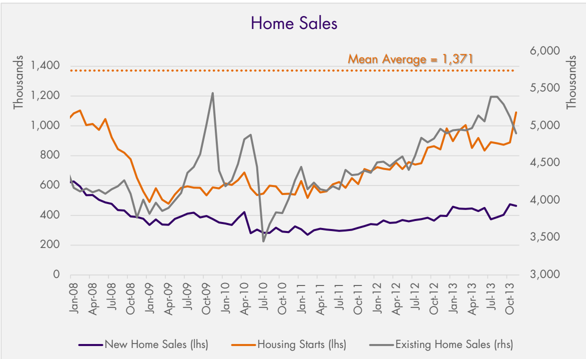


HOUSING

The housing market performed well in the first half of the year, benefiting from all-time low mortgage rates. The economy experienced a very strong spring season, which is typically known to be the time for buying a house. Companies in the industry, like PulteGroup Inc. and D.R. Horton Inc., experienced very strong performance of their stock price. However, after in May Ben Bernanke mentioned that tapering might come soon

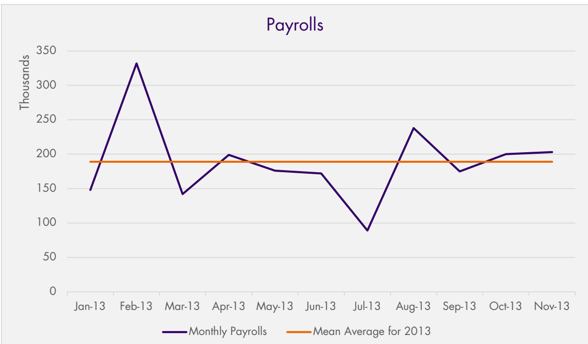


(how dare he?!), treasury yields almost doubled, lifting mortgage rates as well. This triggered a summer-long decline in mortgage applications, which consequently hurt the housing market in the second half of the year. With economic stability and consumer sentiment rising, we expect housing demand to pick up again, despite a trend reversal in treasury yields.

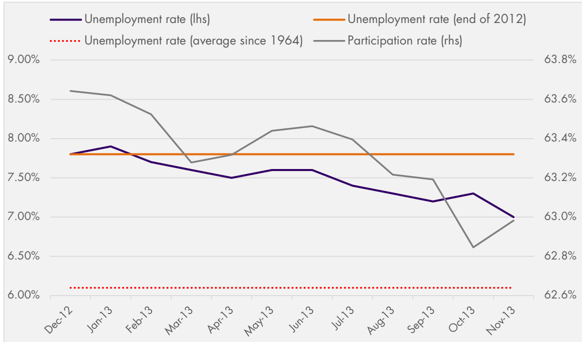


EMPLOYMENT

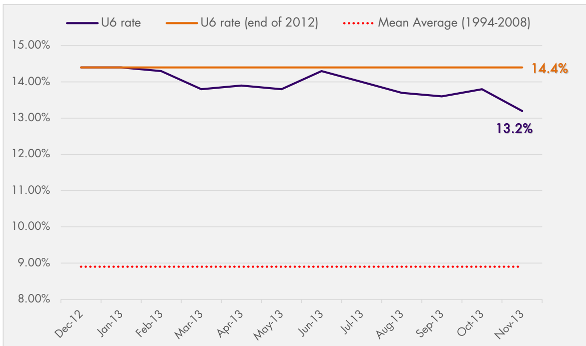
Employment situation was fairly strong, as the economy added 189,000 nonfarm payrolls on average per month. The unemployment rate decreased by 0.8% from December 2012, and currently stands at 7.0%.



Many people argue that the improvements in the labour market are fictitious, due to a decreasing labour force participation rate and a boom in part-time workers. There might be some reason for such assumptions, but jumping quickly to conclusions is definitely wrong.

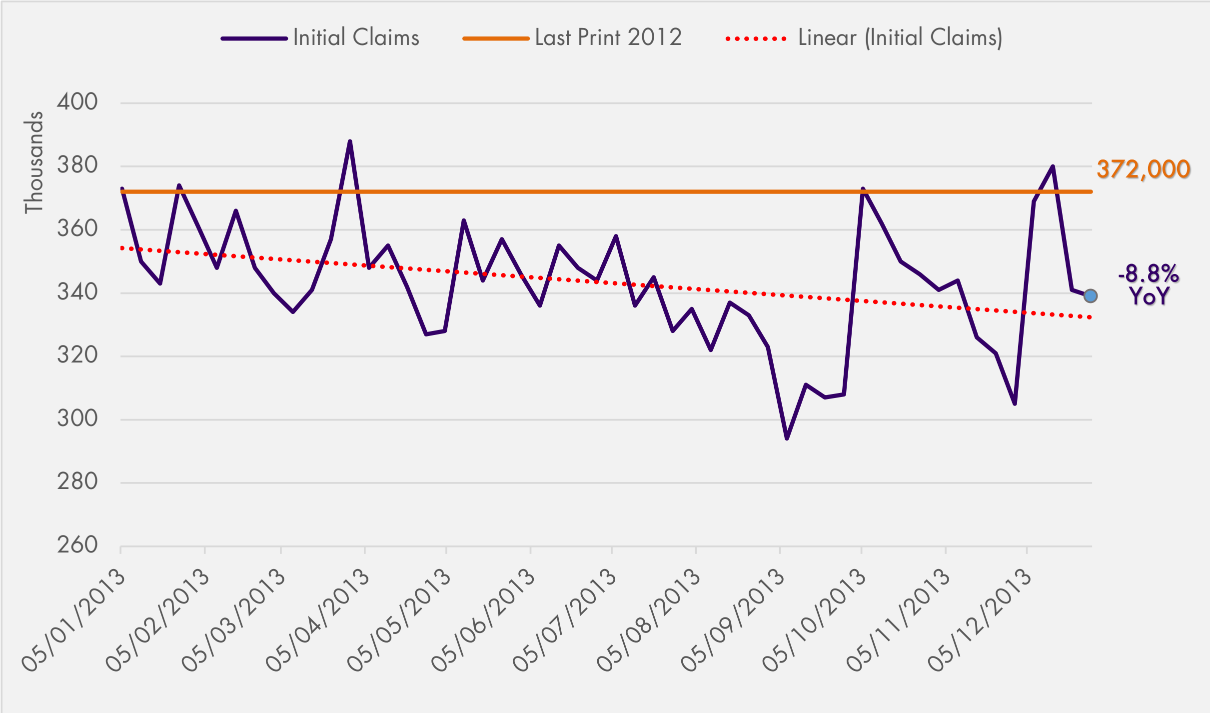


The labour force participation rate is mainly driven by long-term trending demographic factors, which has little to do with the current economy. The financial crisis has definitely magnified that trend, however, it is not the main cause. On the other hand, the U6 rate[1]



clearly shows an improving labour market, which is less and less driven by part-time workers. On top of that, initial jobless claims have decreased by 8.8% (YoY) and are in a strong downward trend. Yet, the situation is far from perfect, with major employment indicators far from their mean averages. This justifies our general argument for further economic growth.

1 Total unemployed, plus all marginally attached workers plus total employed part time for economic reasons.

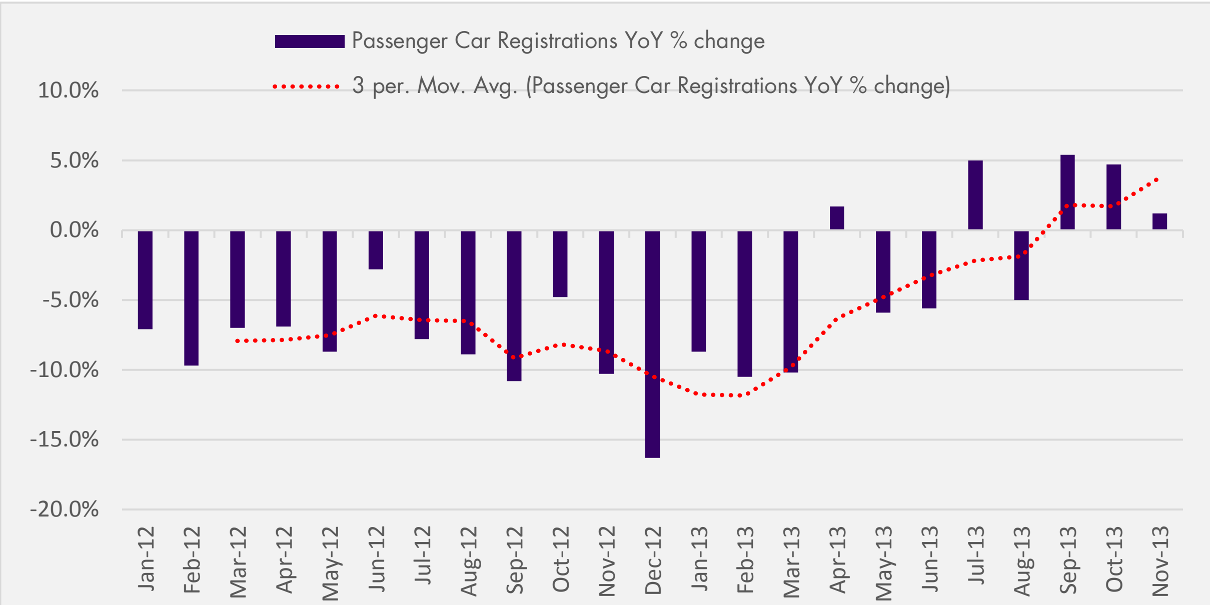

Initial Claims
Last Print 2012
Linear (Initial Claims)
Thousands
400
380
360
340
320
300
280
260
372,000
-8.8%
YoY
05/01/2013
05/02/2013
05/03/2013
05/04/2013
05/05/2013
05/06/2013
05/07/2013
05/08/2013
05/09/2013
05/10/2013
05/11/2013
05/12/2013

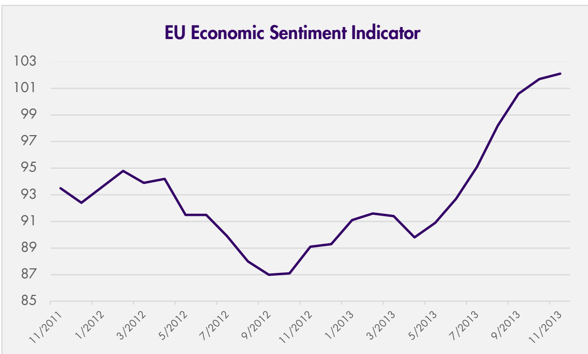
EUROPE

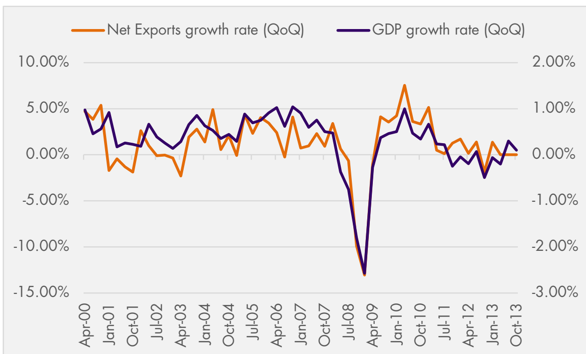
European Union, stay hungry – stay bullish

- The most preferable investment geographic area for investors;
- Finally getting on the right track of recovery;
- Euro Stoxx 50: 17.83% YTD increase

Without doubt, this year was more than good for the Old Continent. Most of its indicators managed to surprise the investors, by performing better than forecasted, for most of the time during the year. Starting with the economic sentiment, ranging from GDP growth and finishing with the car registration: every single figure indicated the strength of the EU recovery. However, it is too early to think that Europe is fully recovered, but examining this year's development signposts it is on the right path of stabilisation.



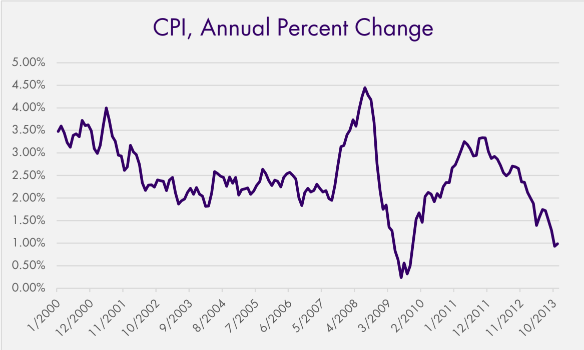




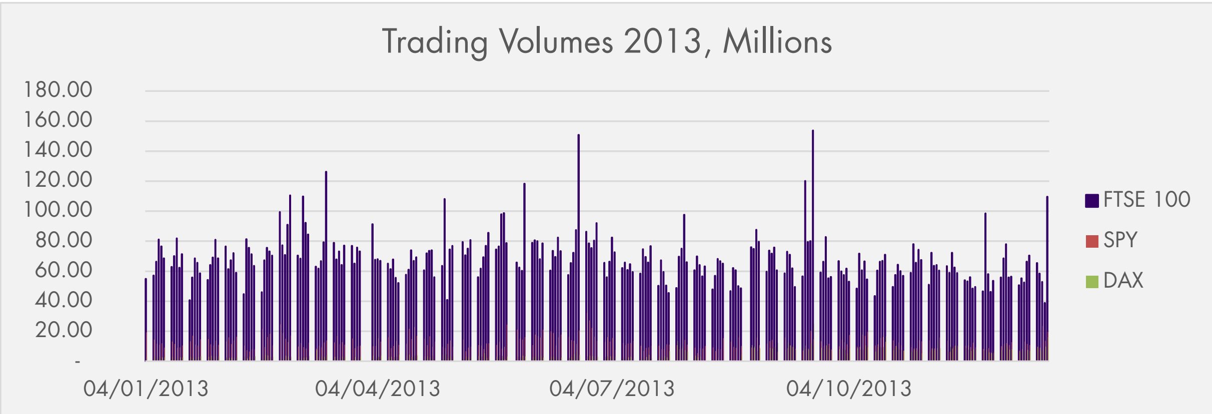
We believe the Euro area economy will continue to expand at a modest pace in 2014. Moreover, the global purchasing manager indexes (PMI) indicate increasing demand for Euro area exports. That definitely would contribute to the growth of the EU (taking into consideration the correlation of net exports and GDP growth rate).

The Euro area crisis, as characterised by persistent and acute financial volatility and recession, looks to have passed. But that does not mean that the Euro area's problems are over. There are still considerable financial, economic, and political challenges ahead. One in particular being inflation, which is putting a downside pressure on the continent.

Euro area inflation has dipped below 1% on measures of the core and headline consumer price index. This disinflation is partly driven by the internal devaluations of the peripheral economies as they seek to regain competitiveness by lowering their domestic price levels.



The ECB has taken note of inflation and lowered the refinancing rate to 0.25% in November. We do not expect the ECB to cut any time soon, but they have guided us towards expecting further easing of monetary conditions through non-standard measures such as adjustments to accepted collateral or new longer-term refinancing operations. Talk of quantitative easing has emerged but we do not expect the ECB to engage in a new asset purchase program, unless the global economic backdrop deteriorates.



Regarding equity performance, European stocks are poised for a third year of gains, restoring almost all the losses suffered during the financial crisis. Furthermore, the European equity market was definitely one of the most preferable financial area for investors.

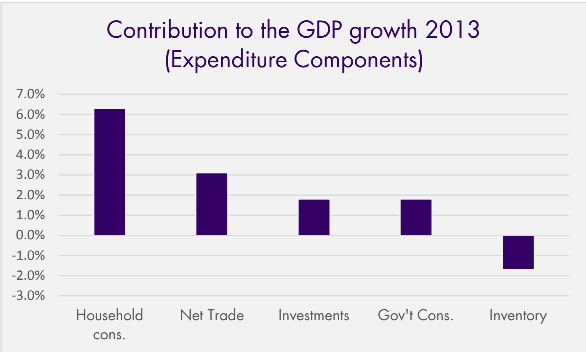
We believe that the macro backdrop is likely to remain supportive for equities — modest, but accelerating growth, low inflation and low interest rates. Moreover, it is hard to see the global economy becoming too hot (strong recovery) or too cold (recession) in the next couple of years and high levels of total debt also remain an effective cap on growth and should also keep interest rates lower for longer. That would affect the stock market positively.

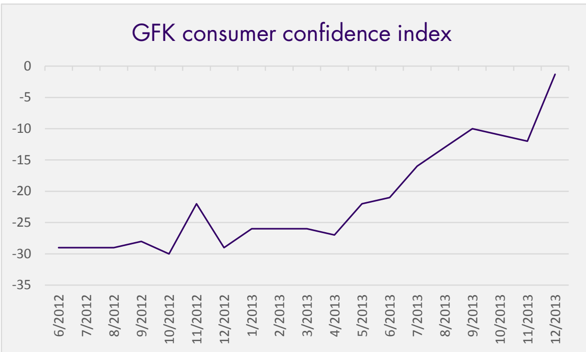
UNITED KINGDOM

Broad – base recovery in UK:

- Strong economic development during the year;
- 13.03% YTD increase of FTSE 100;
- Bubble performance of the housing sector.

It took a while, but we can finally declare with a degree of certainty that the UK's recovery is gathering a solid footing. After broadly stagnating since mid-2010, UK's GDP grew by 1.8% in the year to September.

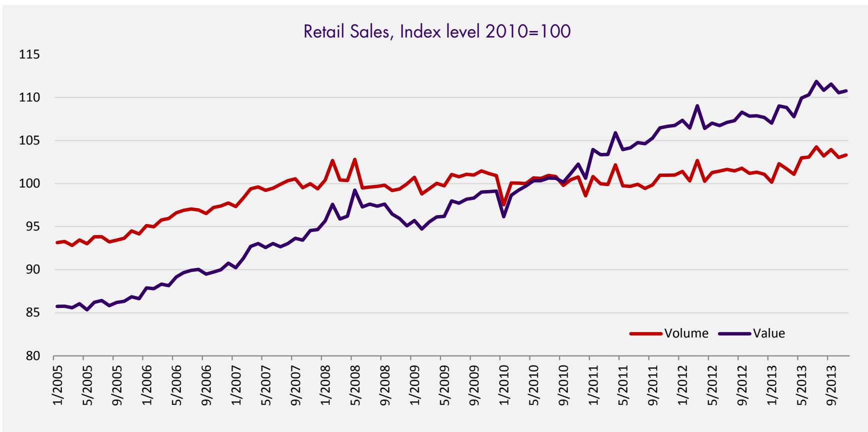




The figure shows that all expenditure components, with the exception of stock formation, contributed positively to growth in the first 3 quarters of 2013.

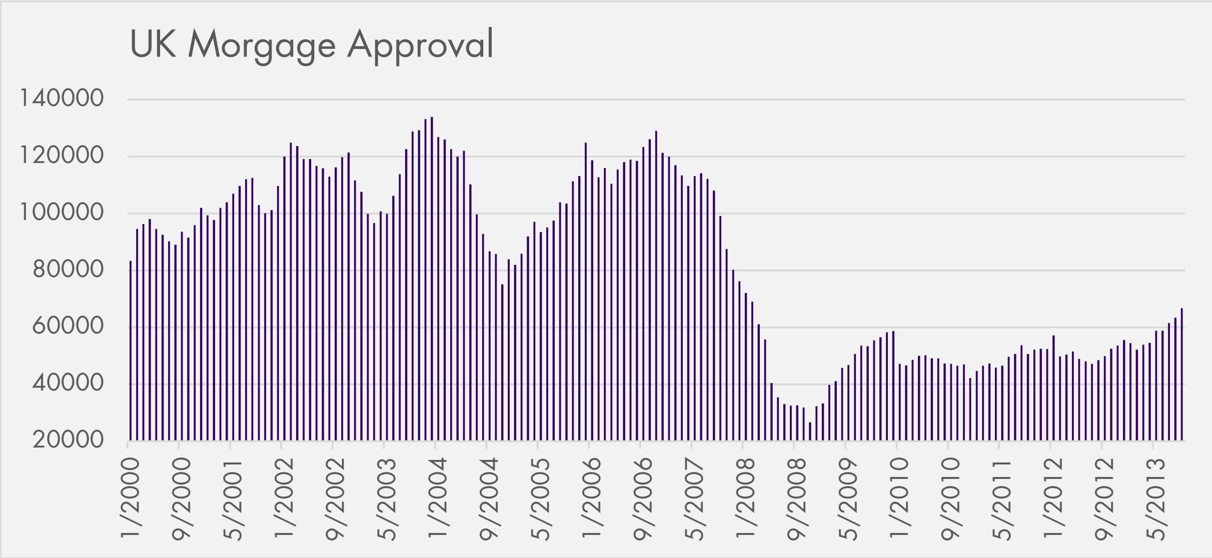
Some reliable indicators suggest that growth is not expected to slow down

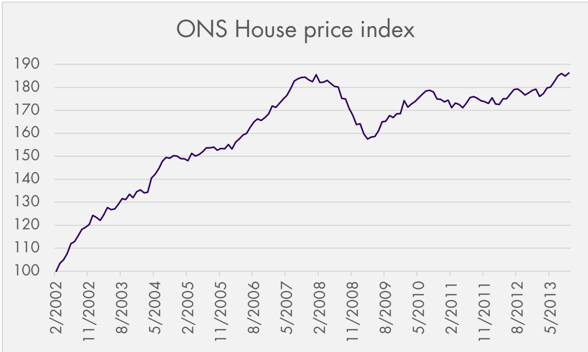
Some reliable leading indicators suggest that growth is not expected to slow down in the coming year. The manufacturing and services PMI are both way above the neutral level of 50 and the CBI retail and industrial surveys are strengthening further. Consumer confidence has also surged spectacularly. This may explain why retail sales has picked up significantly.

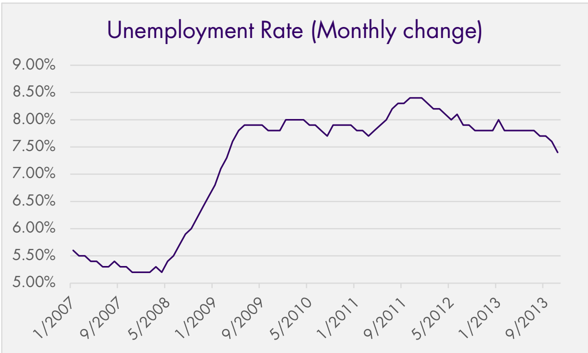


Other three core drivers of the recovery are:

- A better external backdrop, in particular a stabilization in the euro area (the UK's main trading partner
- Less fiscal policy drag this year and next.
- Better credit conditions (with boosts from both legs of the 'Help to Buy' scheme).







The property market in UK created a lot of tension during the year. The housing market revival on the back of the Funding for Lending and Help-to-Buy schemes was supporting consumer sentiment. Indeed, very low mortgage rates and looser credit conditions have released some pent-up housing demand. This led BoE to stop their Help–to-Buy incentive scheme, in order to reduce the bubble risk. However, the housing market played its role in the United Kingdom's recovery.

Regarding the rise of the benchmark interest rate from BoE, we do not expect a rate increase any time soon, as it has been stated recently in a MPC message. However, we do still expect a first rise in mid-2015, when one of the inflation knockouts should go (we do not expect the 7% unemployment threshold to be hit until 4Q15).

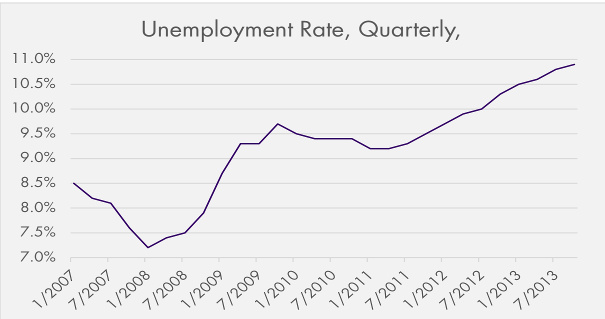
Looking ahead, growth is expected to remain in positive territory and pick up speed in the coming years.

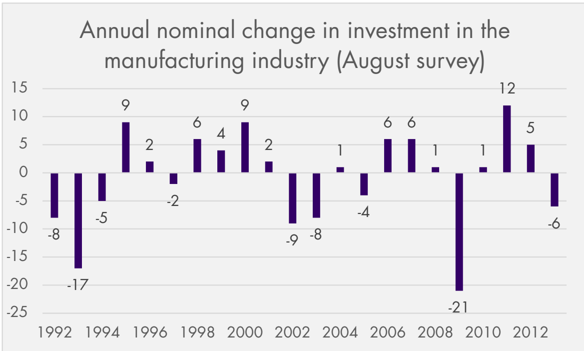
FRANCE

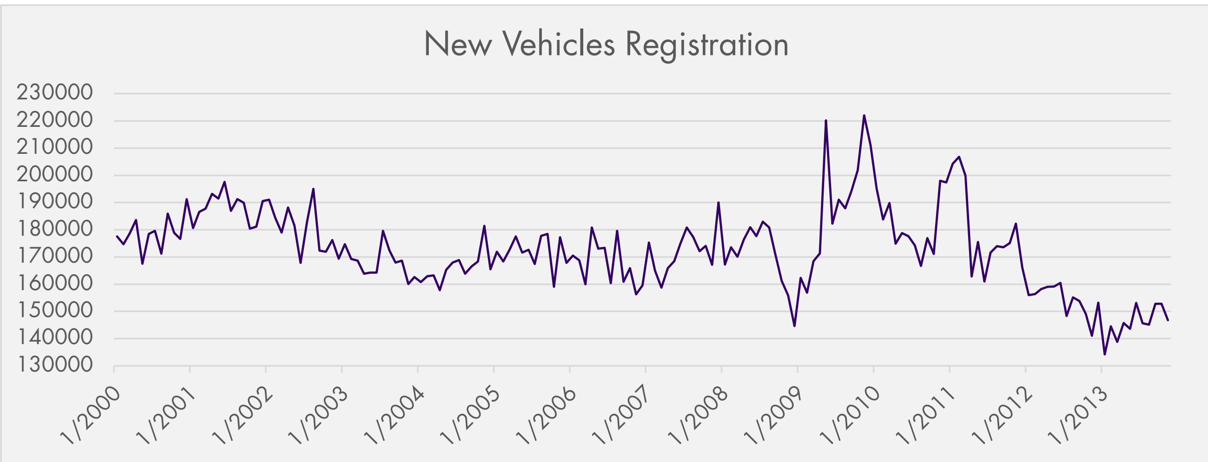
Sluggish performance of France:

- Political tension
- Leak levels competitiveness.
- CAC 40 valued by 15.8% YTD

France is today the real ‘sick man’ of Europe, suffering from bloated government spending, a pervasive lack of competitiveness, rigid labour laws and a wasteful education system. These were the factors that dictated their performance this year.
After two consecutive years of stagnation, we might witness a leak growth of the GDP next year. However, the economy still faces significant challenges. Firstly, given large imbalances in the public sector, fiscal policy will likely remain restrictive. The political debate over taxes suggests that uncertainty about the fiscal outlook is set to persist, causing consumers and businesses to remain cautious spenders. Secondly, a source of concern is the weakness of the corporate sector, which may restrain capital spending further.

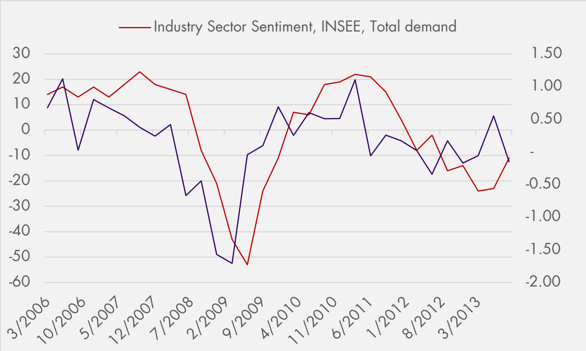


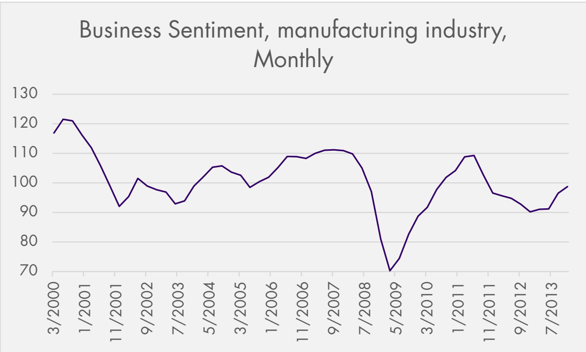




Because of the reasons given above, the immediate future consumer spending will remain rather weak, reflecting the labour market conditions, with slow job growth and a stubbornly high unemployment rate. The uptick in inflation next year, on the back of the VAT hike, should erode household purchasing power slightly. What’s more, fragile balance sheets and low profitability should imply continuing weakness of capital spending and hiring. The competitiveness tax break should strengthen profit margins

somewhat, but gives high uncertainty about the near-term outlook.
It appears only car registrations are recovering.





However, the only positivism is coming from the business sentiment and the car registrations. The recent surveys point to a continuing improvement in business climate in services and above all in industry (the index is close to the long-term average).

It appears only car registrations are recovering

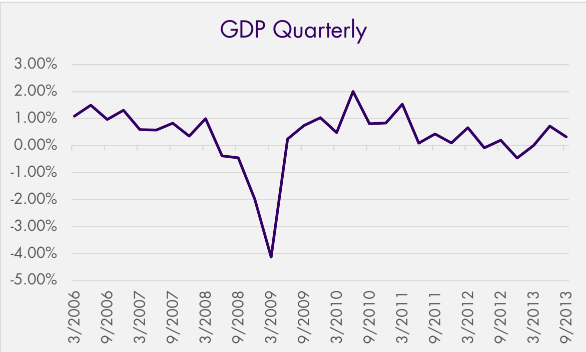
Surely, that could give some wings of the business environment in France, which could boost the development in the second half of 2014.

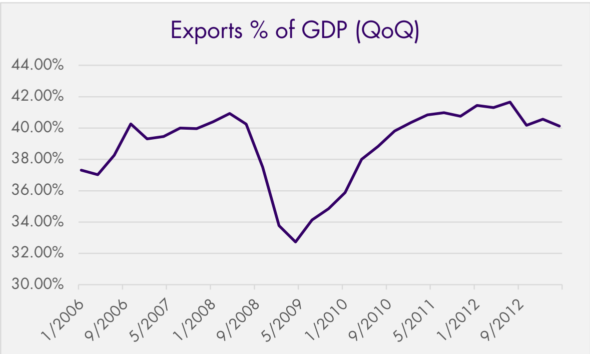
GERMANY

Stable as usual:

- The diamond of the EU;
- Outperformance of equity market, comparing to the rest of the EU: DAX 24% YTD;
- Strong economic performance

Germany is currently at the peak of its economic prowess. Recently, it could be stated that it is now enjoying a golden decade, supported by robust trend growth, low unemployment, a healthy fiscal position and reasonable gains in consumption. During the year, the GDP growth was its biggest gainer (despite the weak correction in the last quarter), on the back of stronger consumer spending growth and a rebound in investment spending.

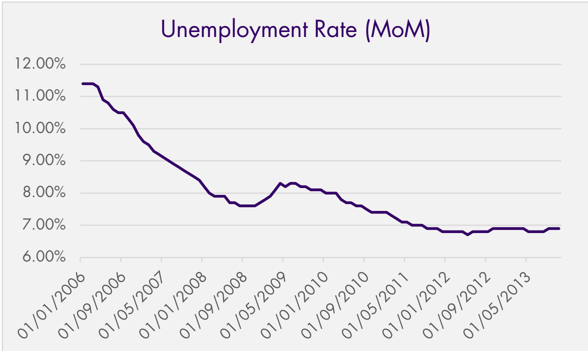




The only thing that weighed down on growth were the weak net exports. However, this was largely compensated for by local spending (corporates and households). We expect to follow a 'slight boost' headline regarding growth again soon.

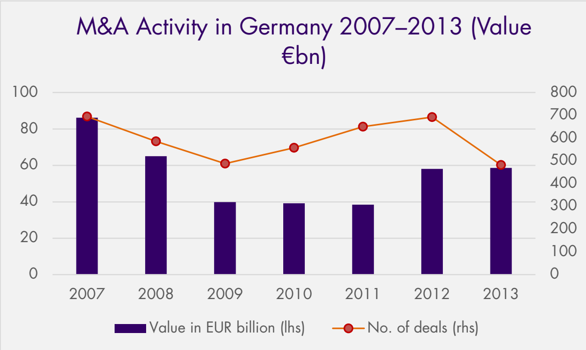
The only thing that weighed down on growth, were the weak net exports

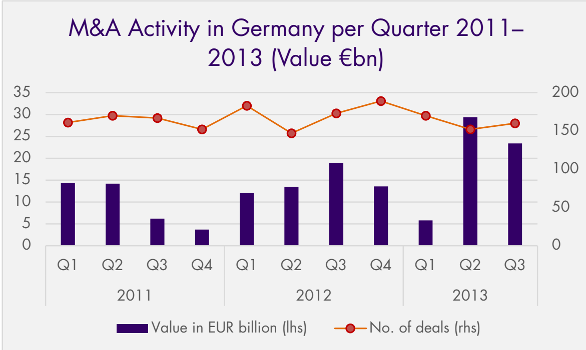
The unemployment kept its steady good performance during the year. However, it is likely to rise marginally due to an influx of new job seekers in the up - coming year. Inflation will likely stay above the Euro area average, at around 1.5%Y, reflecting that the German economy is operating near full capacity and that pay rises are likely to pick up further.

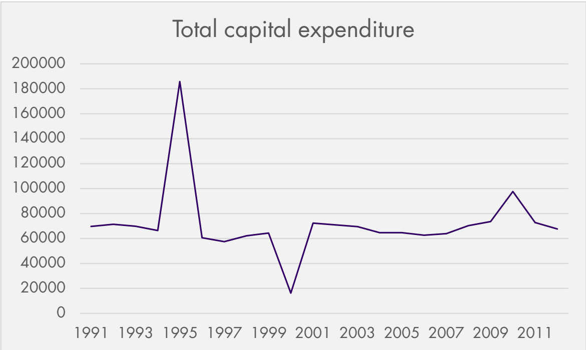


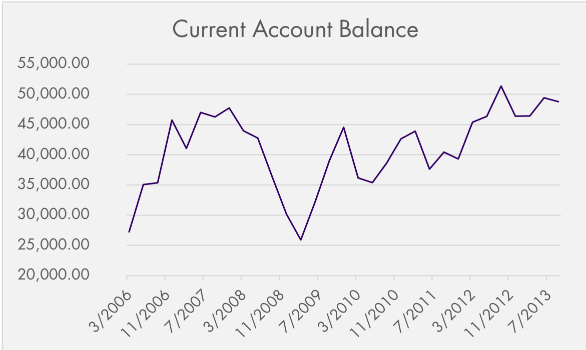
The following year we do not expect any noticeable headwinds. The outlook is strongly positive:

- German GDP growth is expected;
- Pick-up in capital expenditure and investment to bolster growth, in particular overseas;
- Likewise, increased M&A and buyout activities given improved outlook.
- Further deleveraging in the banking sector driven by Basel III and ECB stress tests.









We can find, however, possibility of damaging figures for the German CAPEX. While the commitment to additional infrastructure spending is welcome, the planned amount looks limited in light of the pent-up demand for repair/replacement. Together with higher wages and tighter labour market regulations, this could turn out to be a headwind for the national capital expenditure.

Another thing that was significant for Germany in 2013 was the growth of its current account surplus. In our view, continued under-investment was the key driver of this. Instead of investing in its own productive capacity, Germany invests a large part of its domestic savings in financial assets abroad. To harness the domestic growth potential in full, we believe that the government will need to address the labour market issue, the energy policy question and the concerns of a degenerating public infrastructure.

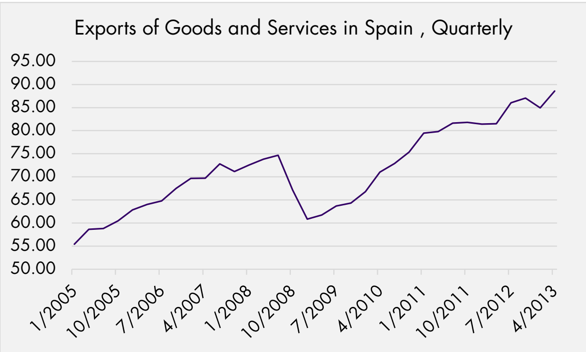
The big picture is communicating that Germany will continue its positive run at the upcoming year. We strongly believe that the strongest economy in the EU will remain, one more time, a synonym of stability, security and growth, in all dimensions of the investment world: macro figures & stock market performance - a pillar of the Old Continent.

SPAIN

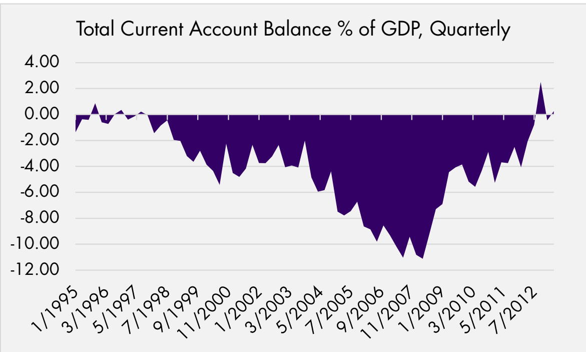
Spain was the informal winner during 2013, in terms of recovery:

- Positive GDP growth rate, boosted by exports;
- Increase in the competitiveness of the country;
- IBEX 35: 13.5% YTD return;
- Still struggling labor market.

Spain was the big informal winner in the European Union. The growth of the GDP, the slow-down of the unemployment rate and increased car registration figures, were only one part of the figures that performed better than forecasted during the year. That increase of Spanish economic development speaks most determinately when it comes to a EU crises exit, more than any other country. Moreover, we witnessed a good recovery, driven by export growth.

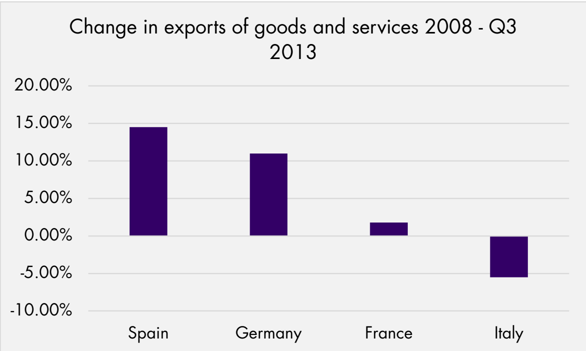


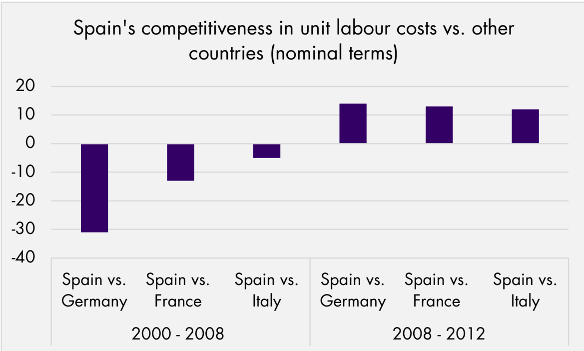
The investment in equipment and machinery has risen in the last two quarters - a powerful signal for the on-going recovery.
Furthermore, their exports are structurally strong, and continue to grow (as a % of GDP) as the lost competitiveness from the inception of the EMU is being reaped, courtesy of wage moderation – in part due to labour market reforms.
Consequently, Spain's current account deficit dropped from 17 bn Euro in 1Q12 to1.5bn Euro in 1Q13 (a ~91% contraction). Over the same period, the deficit on merchandise trade balance fell from 18.6bn Euro to just 5.8bn Euro (a ~69% improvement). That trend is a big one... We expect it to continue into next year!



The investment in equipment and machinery has risen in the last two quarters - a powerful signal for the ongoing recovery

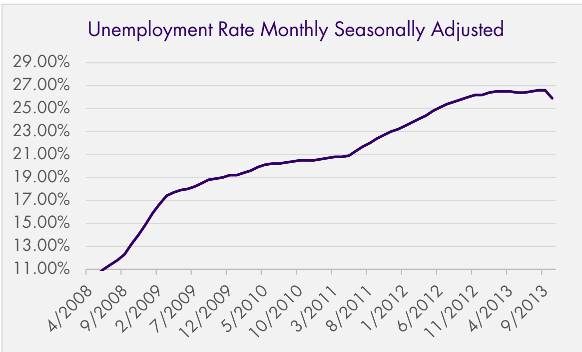
Looking at the details, beyond price-competitiveness factors, the growing geographical and sector diversification of Spanish exports, the increase in the Spanish export base, and the behavior of exports of non- touristic services reveal that they have been key drivers of the recent performance of Spanish exports.





The numbers give a huge advantage to “La Corrida”. Spain has significantly closed the gap with countries like Italy and France in terms of its macroeconomic outlook. Even though the current level of the Spanish imbalances is (slightly) worse than those in Italy and France, the Spanish medium-term trend looks more promising. In particular, we note that Spain is outperforming these two countries in terms of export growth, gains in competitiveness and policy execution of structural reforms.

In terms of labour market performance, we believe that the jobless rate has probably peaked. Yet our worry is not that unemployment will rise. It is that it will not come down quickly enough. The economy has only started to create jobs despite growing twice as fast as current growth (even though recent labour market reforms might have lowered the threshold for employment growth).



ASIA & OCEANIA

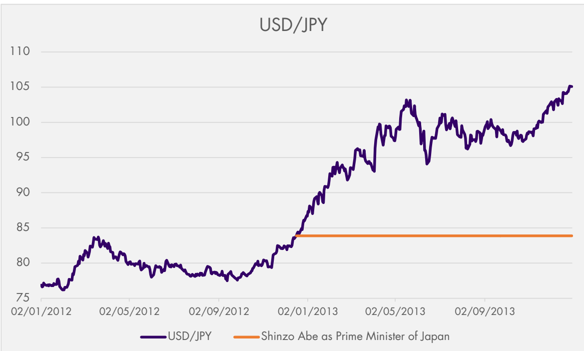
The surplus is strong with this one

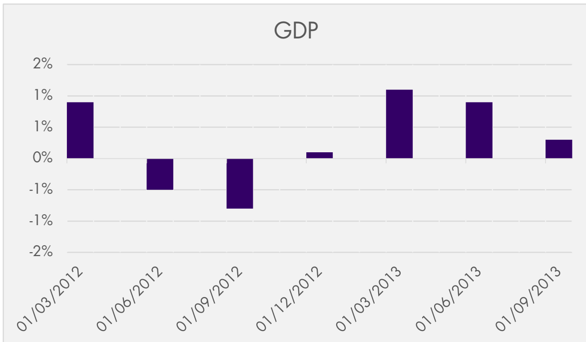
JAPAN

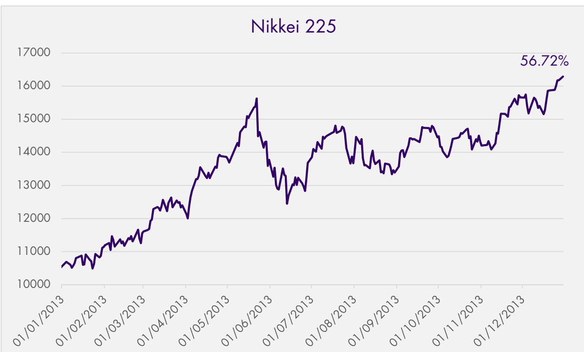
Abeland:
- Top performing market for us: 56.72%
- USDJPY among the most strongly trending currencies
- 2014 tax hike from 5% to 8%
- CPI on the rise because of Abenomics?

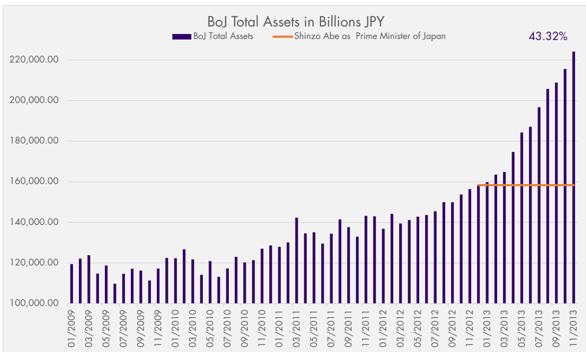
For 2014 we are quite positive on the Japanese economy and stock market. We construct our views on a number of bearing walls. Firstly, we saw in 2013 that the economic, capital market growth, as well as stock market speculation/investment, was largely led by the three arrows of Abenomics:
- aggressive monetary easing from BoJ
- accommodative fiscal policy
- structural reforms

The first arrow has played the leading role so far, depreciating the yen by more than 20%, thus boosting both growth and inflation. There is an old Bulgarian story, which teaches how one can break many arrows one by one, buy may not break them all when together. For us, this explains largely the support role of the second and third arrows of Abenomics.

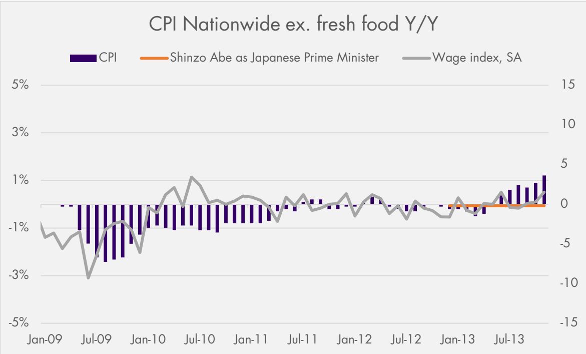




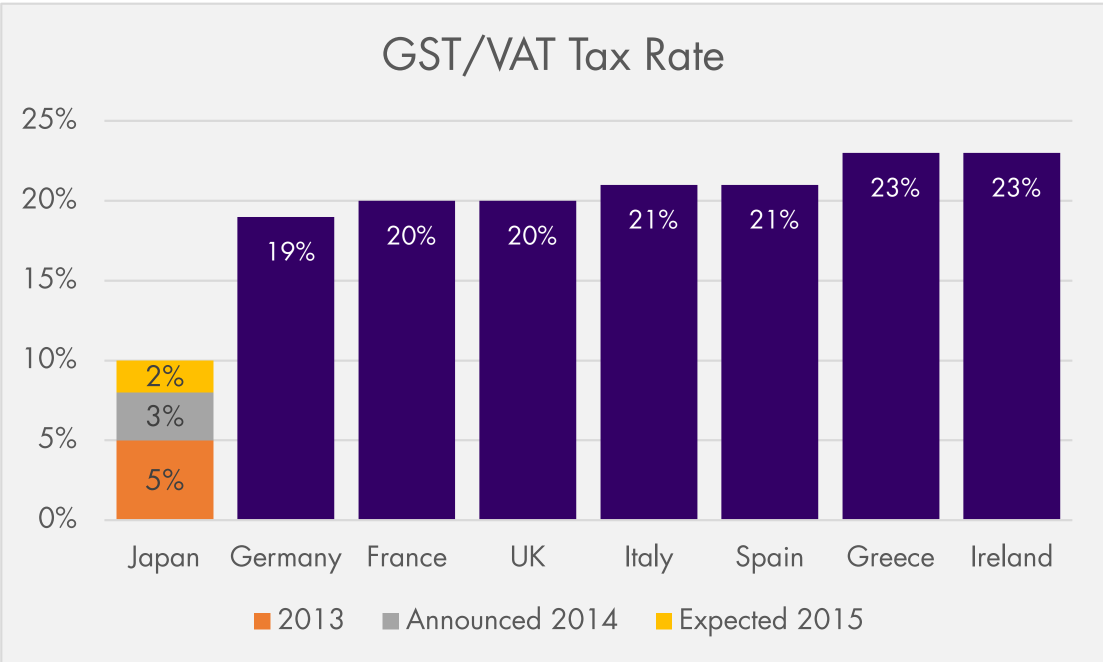




For example. ¥10,000,000,000,000 fiscal support package (roughly 2% of GDP) was introduced in January 2013.
Together, the policy changes have also significantly improved corporate earnings and margins (non-financial companies' recurring margin in April-June 2013 was 5.03%, up about 1% from 2012). All this has priced very well in the stock market, making it one of the best performers for 2013: 56.72% increase.



One of the major issues Japan has is deflation. Mr. Abe, managed to get the economy out of a 15 year deflation, however the question is: Is this sustainable? If it is, then, Abenomics is indeed showing stronger signs of progress. If not, then there is still a long way more to go. Looking at the CPI, since Shinzo Abe became Prime Minister of Japan, inflation has appeared once again on the economic statistics. However, the main contributing factor towards the CPI increase is the jump in import costs (due to yen's decline) and the electricity rates hike as a result of the Fukushima accident. We see sustainable inflation coming from wage rises, which has not yet happened.
Looking forward into 2014, the national sales tax's hike is likely to weigh down on the growth momentum. We view this as a positive thing, because after all, Japan has a roughly 2.5xGDP debt, which Abenomics alone (focused on spending) cannot fix. There will also be a ¥5,000,000,000,000 fiscal support package to offset the tax's negative impact, thus keeping the economy's momentum (otherwise, viewed mathematically, this wouldn't make sense. It's all about timing it.).
Also, Shinzo Abe is very determined in what he does (kind of like ex-chairman Bernanke) which seem to always have a very positive impact from short term investors/speculators point of view.
Having noted this, we believe that BoJ has all the reason to continuing or most likely even expand its asset purchases (probably likely in June or July 2014, after the consumption tax hike), hence we are still bullish on Japanese equities and yen's devaluation, even though we expect it to be harder to achieve 2013-like returns.

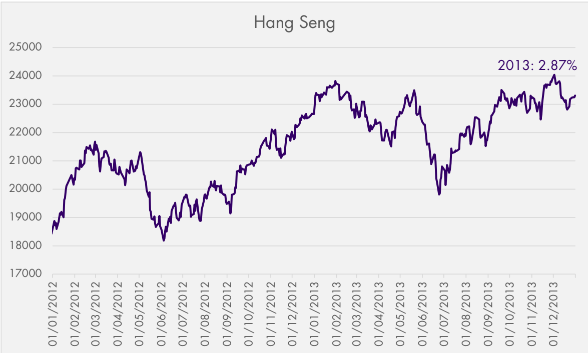


CHINA

The new China!

- Housing prices continue to rally
- Fed taper slap
- CNY liberalisation

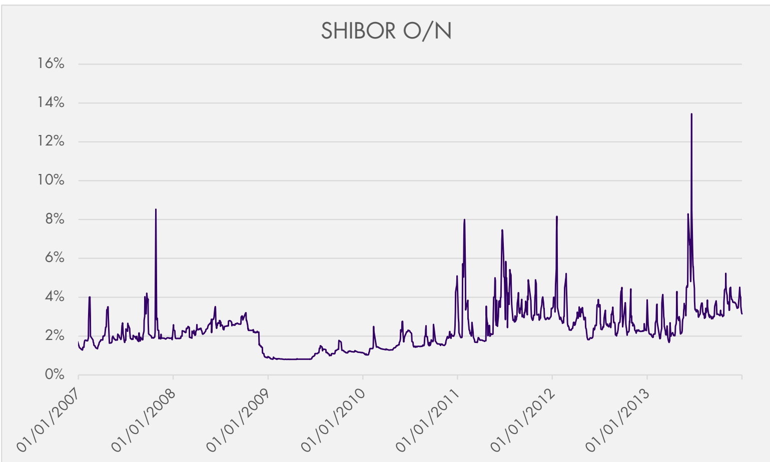
This has been a very mixed year in regards to outlook for China and as a result, the Hang Seng has finished 2013 flat-ish: 2.87%.



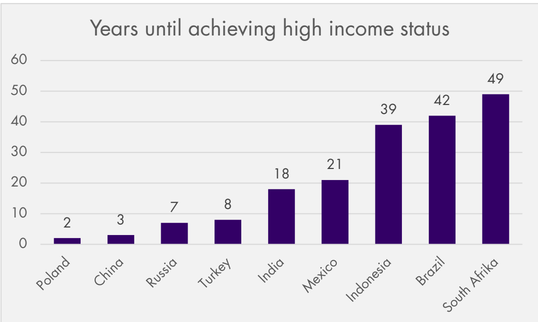
House prices have continued to rally through 2013. There has been lots of talk about a housing bubble in China. The main argument against seems to be that, such sharp rises, when occurring in emerging markets, are apparently more bubble proof that if they were in developed markets. Our view (and positioning in the portfolio) is that housing prices are likely to start their decline in the near future as a result of the structural changes facing the Chinese economy...yes, maybe it's too simple of an argument.

One of the major events for China was the Third Plenum, which took place on 9-12 November 2013. It was very important because the current leadership's ideas for reforms were unveiled (to read more check **Sierra 46**). During the Plenum, the Chinese stock market made it's largest yearly jump, suggesting that investors liked what has been put forward during the Plenum.

This year was also remembered as being very volatile for the SHIBOR (Shanghai Interbank Offered Rate). There are various speculations on what the causes were, but we'll just call it liquidity mismanagement by PBoC. Looking ahead, this, along with the overall shady banking in China, is causing some uncertainty for investors. On the bright side though, the reforms introduced along with the renminbi liberalisation and Chinese's officials determination, it seem that there is enough things to but on both the negative and positive side of the scale. Making it very hard to judge or said otherwise - high risk. High risk is always high returns, so we tried to put forward the ideas we are most certain in and thus still be exposed to the risk in China.



1. We derived a major and very simple theme for our 2014 portfolios - Chinese babies. It's projected that 9.5M babies will be born as a result of the reform. This (even though not a ridiculously high number), is not ignorable and will most certainly have an impact on the financial statements of companies in the baby products business.
2. According to BofA Merrill Lynch, there are 3 years left for China until rising to a high income status economy, which means that the country's middle and upper class is getting proportionately higher. As a result, another bet of ours is the booming luxury market. The Chinese have an affinity towards western luxury brans and for this reason, we have selected a few companies that we find worth considering for 2014:

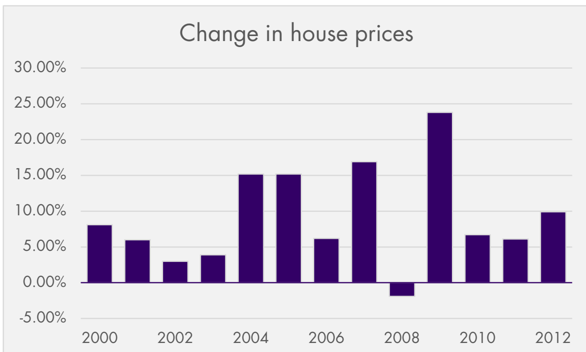


- Prada: derives 23% of its group sales from China
- Burberry: outperforming its Chinese peers
- Chow Tai Fook: the largest listed jeweller globally by market cap and a leader in China
- Tiffany & Co: sexy
- While Ralph Lauren: early stages of strategic changes

3. With property prices in China rising to all time highs (again), we are shorting some ETFs and considering into looking some companies for short positions later on; e.g.
   - China Resources Land Ltd, even though it's very risk, as it had a great run so far.
   - Franshion Properties (China) Limited
4. Chinese cinema also seem attractive for us because of the following reasons:
   - There are expected a few IPO of some major Chinese wanna be Hollywood-like companies (Shanghai Film Group Corp./China Film Group Corp.)
   - Wang Jianlin - China's richest man, has made the massive investment of $8.2B in the creation of the world's largest film-studio
   - China has not yet opened its doors to Hollywood blockbusters

With property prices at all times highs (again), we are shorting ETFs

This year, China seemed injured by Fed's taper talks. The speculations led to significant outflow of capital from emerging, to developed markets. Now that tapering has started (and will continue to tightening eventually), investors are pricing in their expectations accordingly and keeping in mind that fundamentally, this is a good sign. We view this as a less uncertain environment and therefore, we do not put much weight on this issue for now. We only consider that there is a possibility of capital starting to flow back into emerging markets in the very near future.



AUSTRALIA

A bump during the long growth ride.

- Depreciation of AUD against major currencies: -9.83%
- GDP growth below trend
- Shift from mining to non-mining investment

The current Governor Reserve Bank of Australia – Glenn Stevens, has made in total 11 speeches for 2013 and in each one he has mentioned two things:

- "commodity prices have declined from their peaks, but generally remain at high levels by historical standards"
- "a lower level of the exchange rate is likely to be needed to achieve balanced growth in the economy"

He has also mentioned numerous times that:

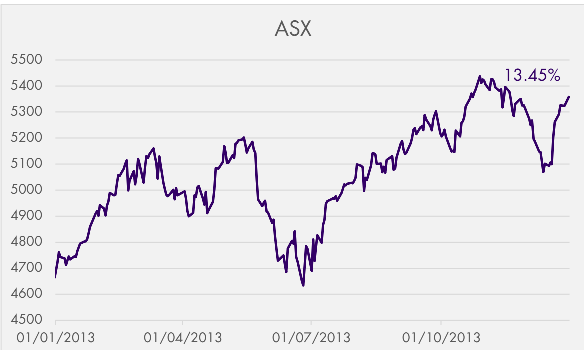
- "global financial conditions remain very accommodative"
- "long-term interest rates remain very low"
- "the economy has been growing a bit below trend" due to lower levels of mining investment"

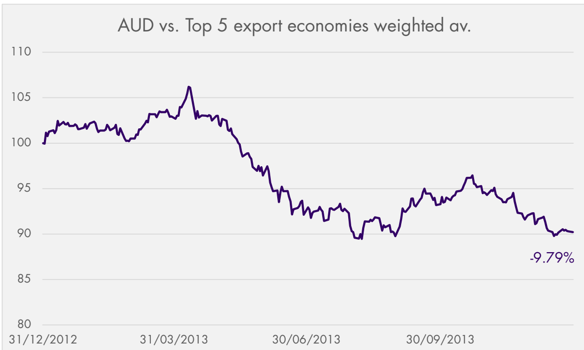
These statements pose a few question that we wish to answer:

- Is RBA going to cut it's cash rate again(currently 2.5%)?
- Is Australia growing below trend in 2014?
- Will non-mining outperform mining companies in the stock market?

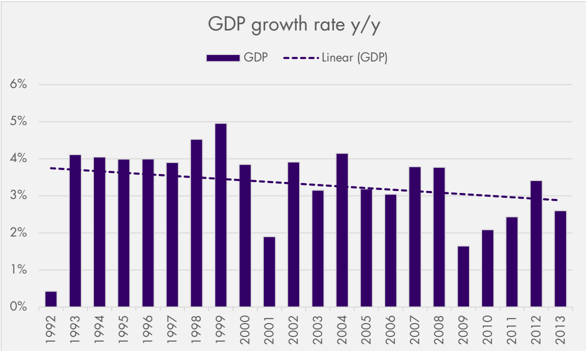
We all know that when country's currency devaluates, it's exports become relatively cheaper. We also know that Australia is a very export driven economy (especially in commodities). This information gave us the bearing walls of our analysis. We start by looking at the Australian dollar's movement against the economy's top 5 export destinations. The largest move made was a 17.03% drop against the Chinese renminbi (biggest export destination) and the lowest was against Japan (second biggest): a 3.66% appreciation. Overall, the Australian dollar made a 9.83% depreciation against it's top 5 export destination's currencies, which led to about 15% increase of it's exports for 2013 (consistent with the depreciation). This suggest that indeed a lower lever of AUD, will help the economy grow at or above trend.

export destination	export vol.	adj. export vol.	export 2013	AUDvs.Currency
China	31.60%	47.66%	31.72%	-17.03%
Japan	18.80%	28.36%	-4.19%	3.66%
Republic of Korea	7.70%	11.61%	8.53%	-14.99%
India	4.60%	6.94%	no data	-3.32%
United States	3.60%	5.43%	1.97%	-14.31%
Average weighted currency depreciation (based on top 5 export dest.)				-9.83%





On the other side, this year was a horror show for commodities. Global commodity prices fell about 5% (as measured by the TR Core Commodity CRB Index) and Australian mining companies' shares fell close to 30% (as measured by the Chimaera Australian Mining Index). This indeed gave a strong hit to the Australian economy.

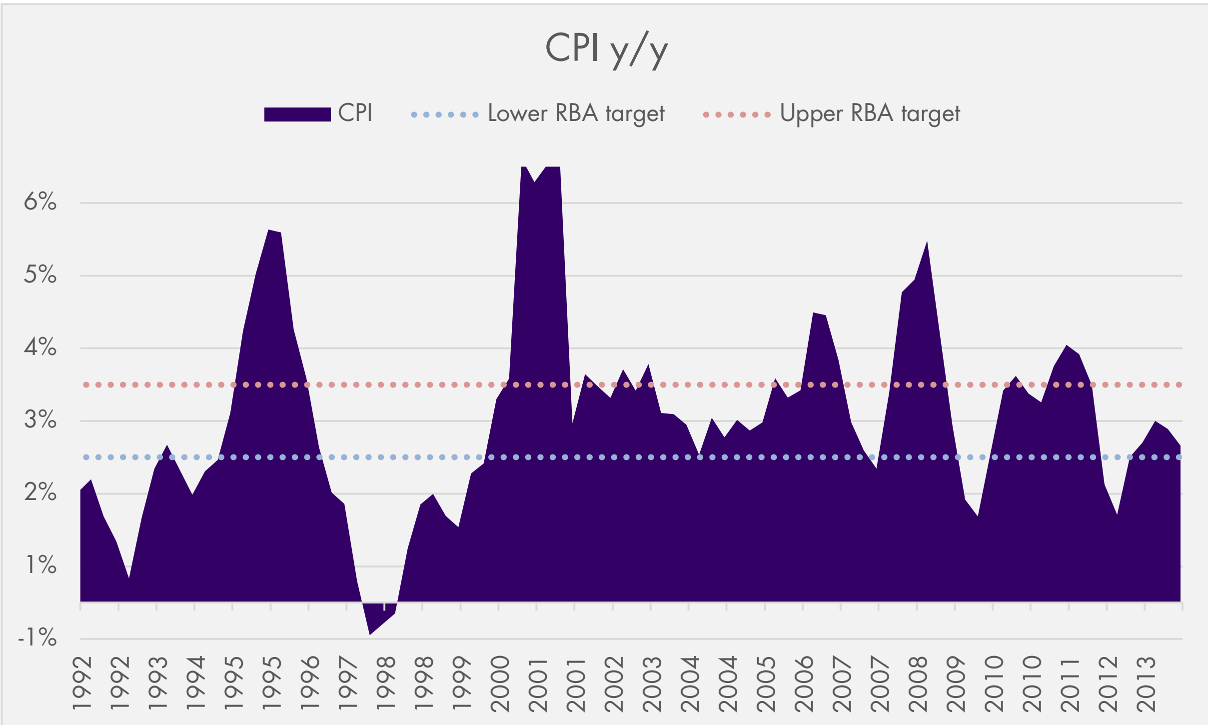


Looking forward we are counting on two things:

1. If the CPI stays within bounds (currently closer to lower bound), the RBA could manage to lower once again its cash rate and thus contribute towards the devaluation of the AUD, boost exports and provide cheaper credit to fuel non-mining investment.

RBA could manage to lower once again its cash rate

2. There were elections in 2013 and we will follow the deliverables of this event during 2014, as we have found such events significant, if one managed to detect the changes at an early stage.

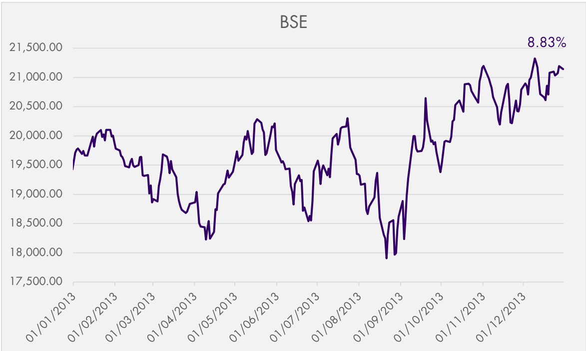


INDIA

A possible alpha for 2014

- Bombay Stock Exchange: 8.83%
- Political situation: shady
- Reserve Bank of India made 7 rate changes
- Rupee vs. USD: -12.38%

Year to date for 2013, India has not performed very well. The reason for this was mainly the unresolved political problems within the economy.

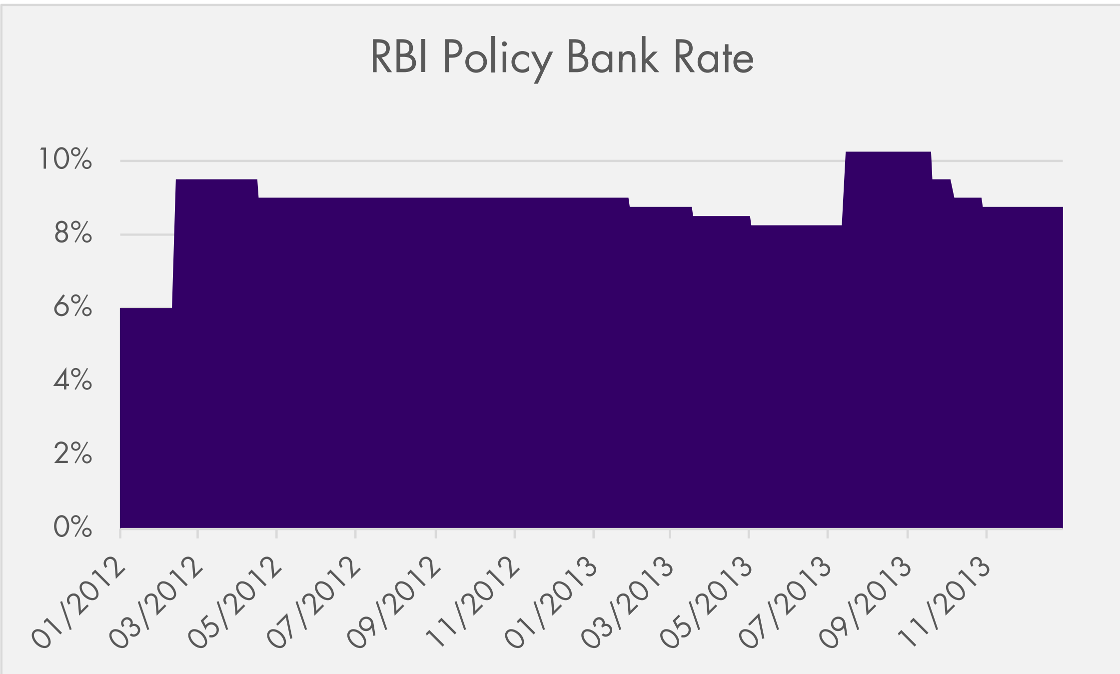


The key risk for 2014 is the same as it was during 2013: Political instability. The difference now is the general elections to be held in April.

RBI changed its Bank rate 7 times during 2013. Three cuts during the first half of the year, with three cuts in the second half and one massive raise in between, which was

RBI changed its Bank rate 7 times during 2013

made to stimulate the INR and help open the parachute during it's drop... well that didn't happen. Instead, it caused quite a fiasco for investors.



As the standard way of boosting growth these days seems to be (from one side) via rate cuts, we expect the RBI continue (hopefully a much smoother) rate cutting in order to support growth. This fundamentally means a longer drop for the currency.

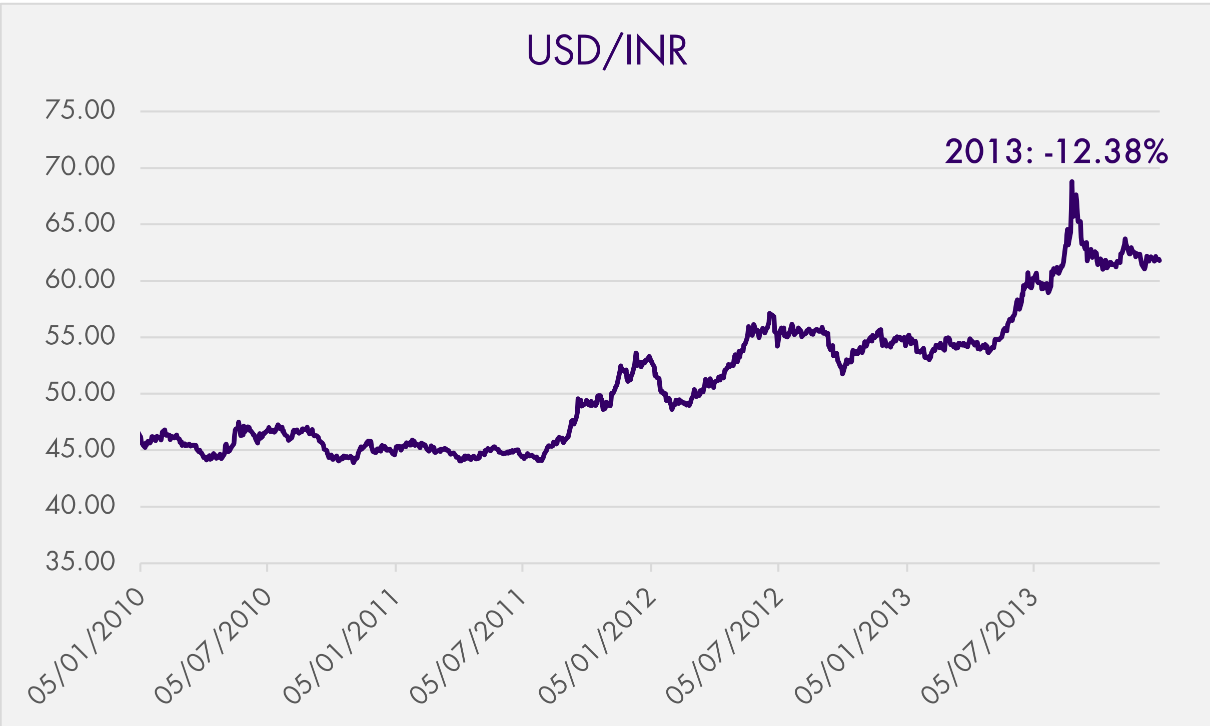
From an investor perspective, just like in China, India is an even more emerging economy and the outflow from Fed taper talk should now be pretty much priced in, therefore as tapering is a fundamentally a sign on a recovering economy, 2014 may be the year of capital inflow for emerging economies. If this happens to be the case, India will certainly be the place to be:

- Increase in risk appetite
- Higher US demand to boost exports (with weaker INR...even better)
- Less bond buying will likely stabilise commodity prices such as oil

Let's talk about the risks now:

The INR has usually gone up against the dollar during monetary tightening (not tapering, we know... but it's along the way). This happens because of the reason mentioned above - risk appetite increases, so investors start looking towards India. Therefore, we are looking for RBI to be aggressive and the investors sentiment to be well determined like in the JPY.

From a macroeconomic point of view, elections should be no major worry to the economy and stock market (e.g. Bulgaria: the nation protests in demand of government step down; when that happened it got re-elected; didn't manage to re-assemble, so a new government is in power now; people protest with the same demands for step-down again. Political situation: Bad/Unknown but Stock market: 2013: 49.19%). India however seems strongly driven by this, therefore the election of a stable coalition build around either the ruling Congress or the Opposition Bharatiya Janata Party will be good.

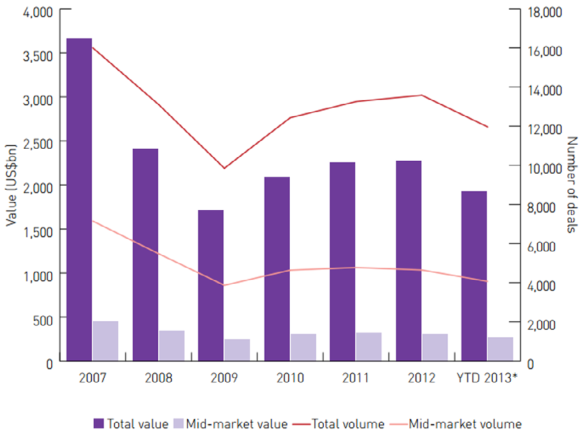


M&A and IPOs

The calm before the storm

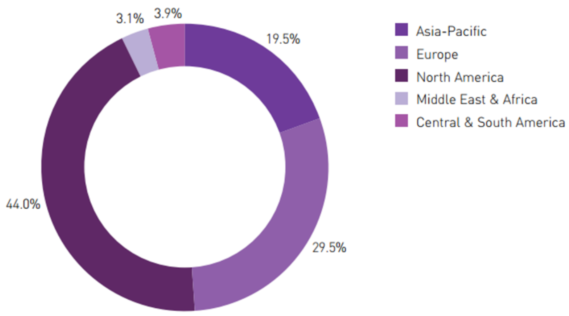
M&A

In beginning of 2013, the coming year was predicted, by many analysts and institutional investors, to be very busy in terms of M&A activity. Now as the year is approaching its final day, we can safely say
this was not the case. Despite a few large deals the year was quiet, volume and value of deals were lower than 2012 and 2011.

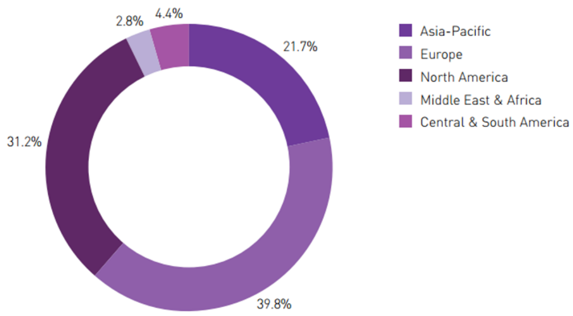


Moreover volumes were significantly lower. We like to think of it as a calm before the storm. With other major economic indicators at 2007 or above levels M&A activity has lagged the recovery. In our view this is largely due to uncertanty about future market stability and the nature of mergers and acqusitions, which are longer term investments. According to a recent survey from Ernst & Young, 52% of U.S. executives expect deal volumes to improve and 41% plan to pursue acquisitions in the next 12 months.
With record levels of cash holdings and low rates continuing, we see 2014 as a highly potent year for mergers and acquisitions. The decrease in uncertainty and increase in consumer and business sentiment creates a pleasant environment for strategic expansion. Thereafter we anticipate a trend reversal in 2014, with deals approaching 2012 levels. We see continuing strong activity in the Energy, Mining and Utilities, Consumer, Pharmaceutical and Technology sectors.

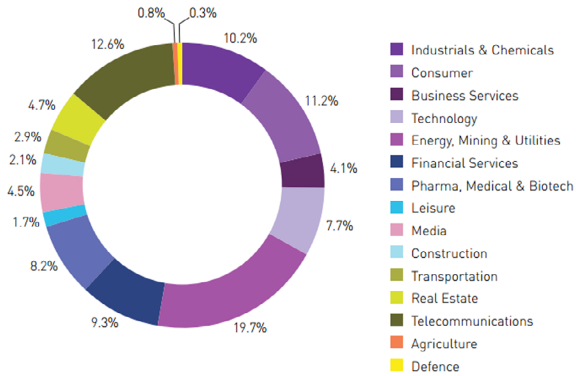
VALUE

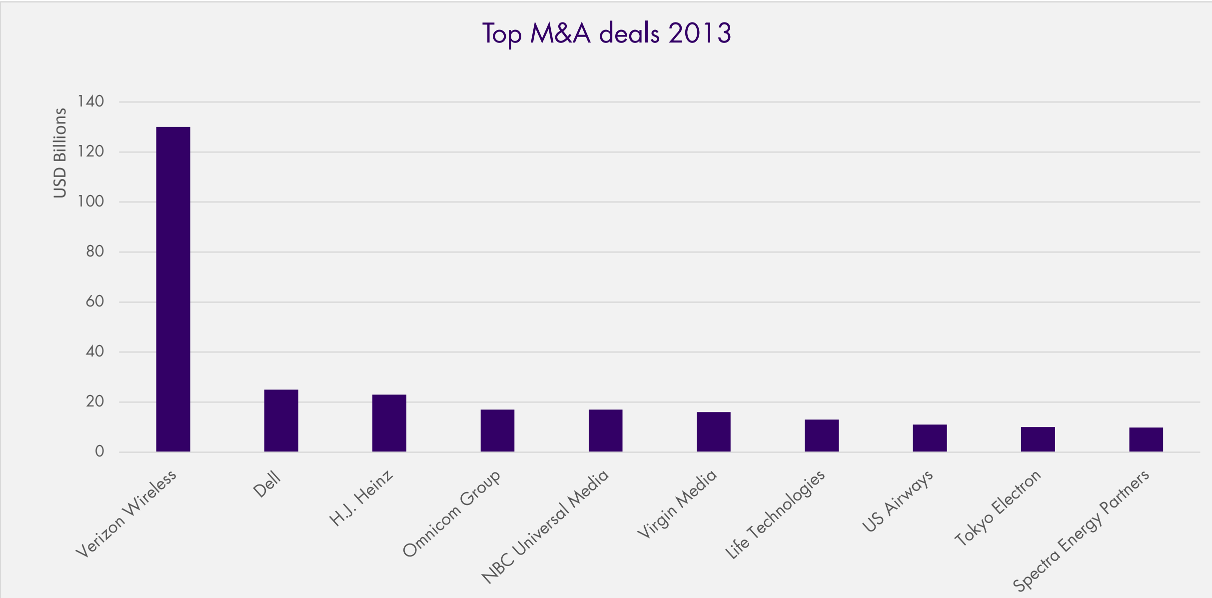


VOLUME



At ShardFund we see great opportunities in anticipating acquisitions. Therefore we allocate around 10% of the holdings in one of our portfolios (Cortez) in companies with the potential of being acquired. Through our analysis we identified 3 companies, which we categorise as probable takeover targets. OZ Minerals (ASX:OZL), an Australian mining company, Chico's FAS (NYSE:CHS), an own-brand apparel retailer, Aeropostale (NYSE:ARO), another clothes retailer, are our 3 picks which we expect to be bought out by private equity companies and larger corporations.



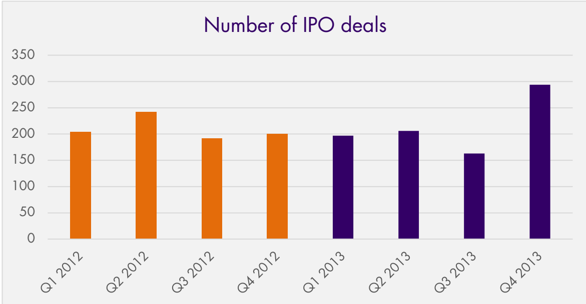


IPO

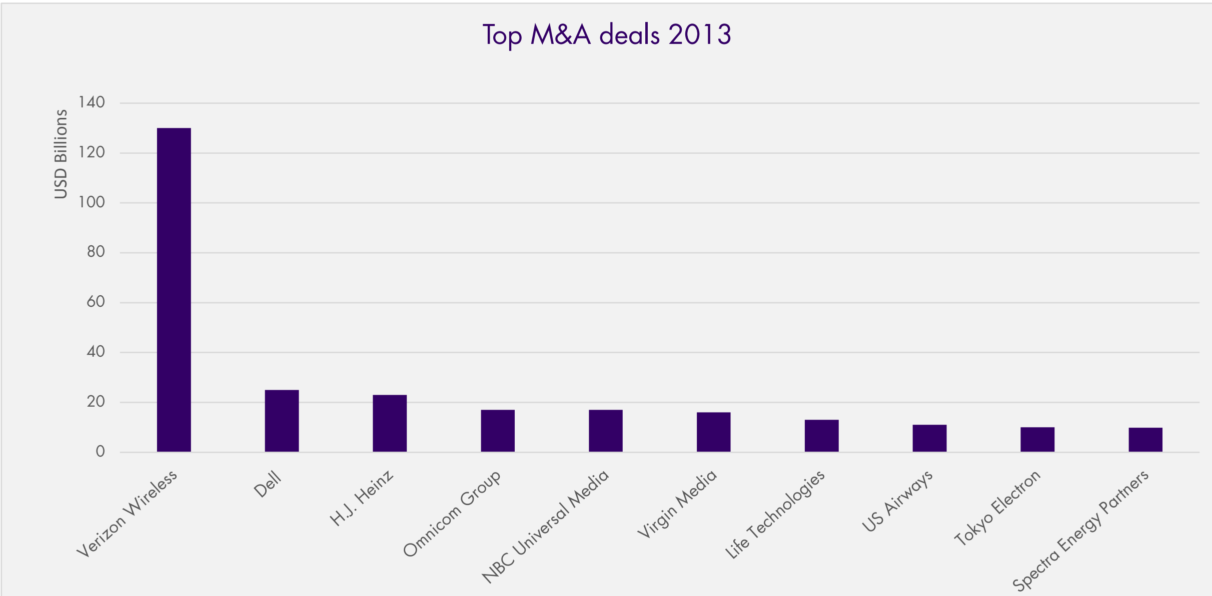
Mixed first three quarters of 2013, but Q4 solidifies the year as active and a positive fundamental sign for next year. 2013 beats 2012 both in terms of deal values and numbers. The number of IPOs in 2013 is an indicator of improving market sentiment and reinvigorated market activity.

There were 864 IPO deals globally in 2013

There were 864 IPO deals globally in 2013, compared to 837 deals in 2012. Capital raised this year was USD163 billion compared to USD 128.6 billion in 2012 – a 27% increase. Similar to our view for a potentially improving M&A deals, we expect higher IPO activity in the coming year. Chinese stock market should have a busy year of initial public offerings, as the ban on IPOs was lifted in November. Real Estate, Financials, Technology and Pharmaceuticals are the top IPOs expected to extend their performance, in terms of deal numbers, in 2014.



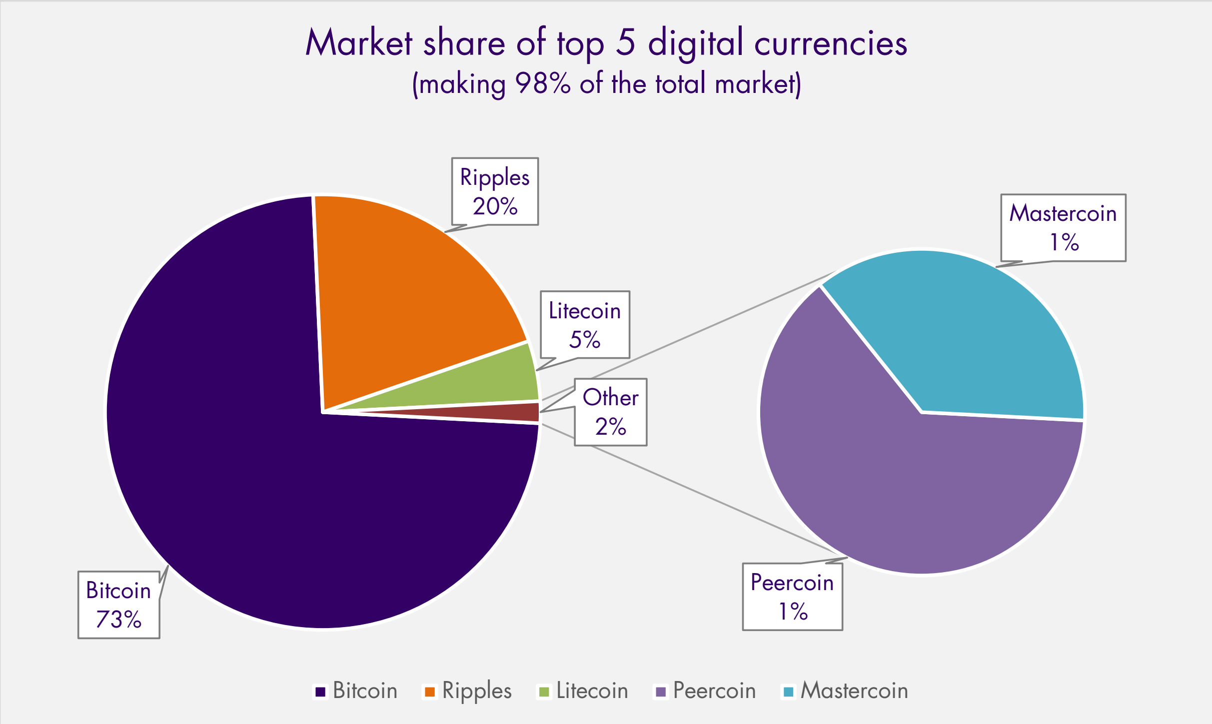
Stay tuned for our IPO 2014 Outlook Report, where we go in detail with our top picks for 2014.



DIGITAL CURRENCIES

New lucrative investment opportunity or all too familiar bubble?

Very quickly, what actually is a digital currency? A digital currency is defined as purely 'electronic money' that acts as an alternative currency (Thanks Wikipedia). Perhaps the most notable and largest in existence, the Bitcoin, has made headlines since its introduction in 2009. Others names include Litecoin, Ripple and Peercoin.



The market is still very concentrated, with the top three currencies (based on market cap) capturing 97% of the whole market. However new entrants are flooding the market and overall everything changes very quickly. In fact, by the time this report is posted, some of the data presented might be irrelevant. Just compare the top 8 crypto–currencies (by market cap) for the period of 1 month.

The reason behind increasing digital currency development and investment is the modern transition to phone and digital banking marking it a fast expanding business opportunity: there is a large piece of financial pie for anyone who can instigate and force widespread adoption of a viable digital currency and wallet technology.

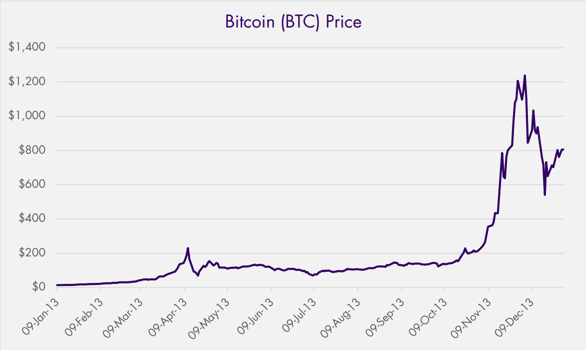
Name	Market Cap (USD million)
Bitcoin	11,780.95
Litecoin	656.65
Peercoin	77.36
Namecoin	56.48
Primecoin	16.85
Feathercoin	13.05
Novacoin	12.63
Megacoin	11.72

*End of November 2013

Name	Market Cap (USD million)
Bitcoin	10,020.73
Ripples	2,783.49
Litecoin	610.91
Peercoin	142.30
Mastercoin	81.97
Nxt	67.34
Namecoin	54.30
Quark	25.24

*Beginning of January 2014

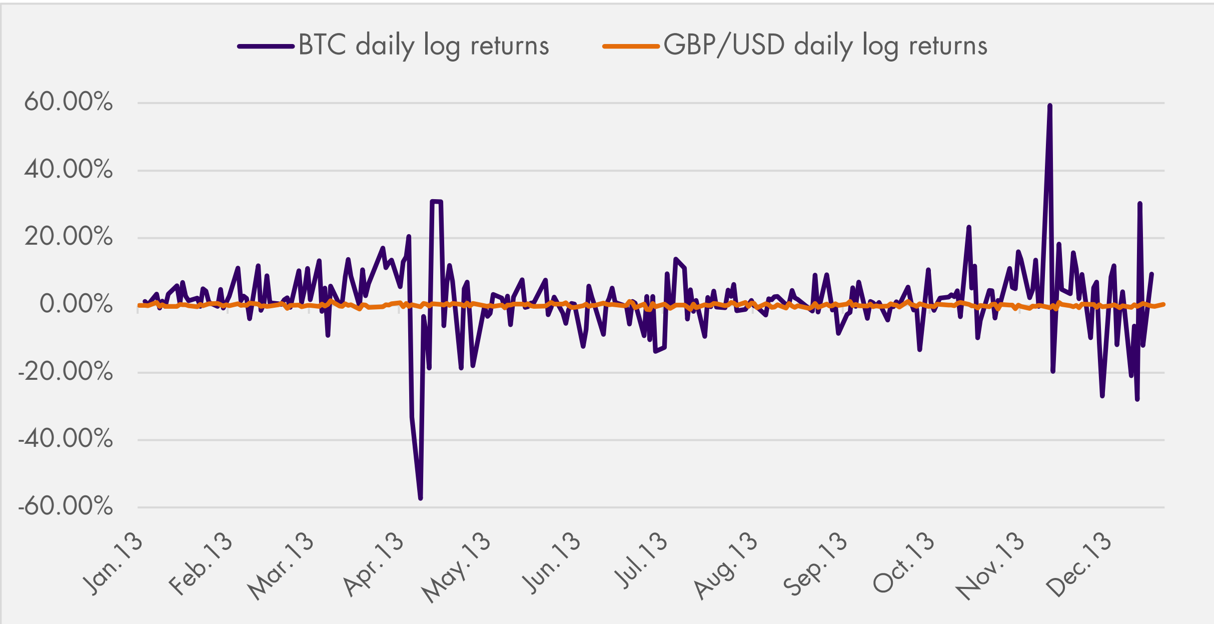
Indeed, there appears to be a behind the scenes battle triggered by Bitcoin's success with large corporates such as Google, Paypal, Apple to produce some kind of implementation. JPMorgan last week filed plans for their own digital currency following Apple revealing an iMoney patent earlier in December.



The big boys are interested, but should we be? Examining the price history of the Bitcoin (see chart above), if you bought $100 worth of Bitcoins at the start of the year and cashed in at the end of the year you would left with $5931.9. Not bad. However, when we consider the risk of this kind of investment the risk exposure is big. These currencies are not regulated by a central bank and Bitcoin's price as one example is wildly volatile, its price clearly driven by media coverage. The highs experienced in November were believed to be caused by Chinese investors stashing money offshore. China has since banned investment in Bitcoins and their value halved from $1270 to $650. We can from chart below compare the volatility of returns from Bitcoins compared to the USD/GBP exchange rate.

top three currencies holding 97% of the whole market

A direct investment in Bitcoins would be inadvisable this year since many believe the November highs seen were a bubble inflated by speculators looking to make a quick buck. Furthermore, there has also been a concerning and increasing amount of fraud and theft from exchanges pointing to potential security weaknesses in the currency. What may be a better strategy would be to watch future developments closely and look out for new technologies which improve on Bitcoin's drawbacks and limitations. Once we see more stability and longer-term investment the rise of the digital currencies can commence.



PORTFOLIOS

MAVERICK

security	L/S	date
Volkswagen AG	Long	03/09/2013
Datang International Power Generation Co. I	Long	03/09/2013
ENN Energy Holdings Ltd	Long	03/09/2013
China Longyuan Power Group Corp. Ltd	Long	03/09/2013
Tracker Fund of Hong Kong	Short	03/09/2013
Nike Inc	Long	15/10/2013
SPDR Financials Sector	Short	28/10/2013
Corning Inc.	Long	23/10/2013
INR/USD	Long	04/11/2013

security	L/S	date
CNY/USD	Long	04/11/2013
BMW	Long	07/11/2013
ProShares UltraShort Lehman 20+ Yr(ETF)	Long	04/11/2013
Tracker Fund of Hong Kong	Short	17/12/2013
SPDR Utilities Sector	Short	17/12/2013
Hengan International Group Co Ltd	Long	24/12/2013
Orange SA	Short	02/12/2013
Telefonica SA	Long	02/12/2013

CORTEZ

security	L/S	date
Pandora A/S	Long	03/09/2013
Valeo SA	Long	03/09/2013
Aspen Technology Inc	Long	03/09/2013
Prudential Plc	Long	30/09/2013
USD/JPY	Long	07/10/2013
Aeropostale Inc	Long	15/10/2013
OZ Minerals	Long	15/10/2013
Greenhill and Co. Inc.	Long	20/10/2013
Easyjet plc	Long	20/10/2013

security	L/S	date
Chico FAS	Long	15/10/2013
H&M	Long	15/10/2013
Restoration Hardware	Long	23/10/2013
Claymore/AlphaShares China Real Est ETF	Short	04/11/2013
Claymore/AlphaShares China Real Est ETF	Short	17/12/2013

EVENTS

USA

- Mid-Term Elections
- Debt ceiling negotiations
- New Fed Chairman (J. Yellen)

EUROPE

- ECB: Bank Stress Test Report
- EU Parliament: Elections
- BoE: Monthly Reports
- ECB: Monthly Reports

ASIA & OCEANIA

- Japan: Tax hike
- India: Elections
- Australia: RBA rate decisions
- China: Reform implementation

REFERENCES

Reserve Bank of India, Reserve Bank of Australia, MOF, Bank of Japan, Bloomberg, Reuters, Seeking Alpha , National Bureau of Statistics, S&P 500 Target Chart - http://rpseawright.wordpress.com/2013/12/10/missed-it-by-this-much/, Allen and Overyhttp://www.allenovery.com/SiteCollectionDocuments/m-a-q3-2013.pdf, Investor place - http://investorplace.com/2013/12/mergers-and-acquisitions-biggest-deals-2013/11/#.UsbhofQW1Ys, Mergermarket Group, Berenberg, Bank of America, JP Morgan, BBVA, La Banque Postale, Deutsche Industriebank, FRED, EuroStat, BoE, ONS, Yahoo

DISCLAIMER

ShardFund is not a registered entity, it's a project. This report expresses the opinion of ShardFund's team and is not a solicitation to buy or sell any security. The writing represents our best judgment as of the date of preparation, and is subject to change without notice. Before making any investment decision you should always consult your personal financial advisor and conduct your own due diligence. The recipient of this report should also assess his own financial situation, goals, and sophistication prior to making any investment. All views expressed, implied, or otherwise are solely derived by Shard Fund's team members. The information herein was obtained from sources believed to be reliable, but has not been independently verified by ShardFund. Therefore, we do not guarantee its accuracy.