

From: [REDACTED]

To: Jeffrey Epstein <jeevacation@gmail.com>

Subject: Fwd: ATorus Daily Portfolio Report 4/15

Date: Wed, 16 Apr 2014 18:29:36 +0000

Attachments: ATorus_BacktestNAV_041514.pdf

Daily Portfolio from Michael Fowler

----- Forwarded message -----

From: Michael Fowler [REDACTED]

Date: Wed, Apr 16, 2014 at 2:13 PM

Subject: ATorus Daily Portfolio Report 4/15

To: [REDACTED]

[REDACTED]

Please find attached the Daily Portfolio Report for 4/15 along with the below commentary. Have a good day!

- Daily Commentary -

Risk of Ruin & Position Sizing/Portfolio Exposures

'Risk of Ruin' we think is one of the most interesting concepts in understanding how sequencing coupled with the sizing of specific risks can have a disproportionate effect on end-outcomes. One can have a mathematical edge and wager correctly, but a sequence, over enough period of time will occur where the randomness of the draw will significantly negatively impact one's portfolio. The way to mitigate this is three fold:

- (1) Compound capital, and thereby continually increase risk allocations but risk-adjusted (in dollar terms, not outsized risk given mathematical edge) so the base capital grows. This is likely obvious to most.
- (2) Second, is attempting to mitigate correlation so all risks are not moving the same way.
- (3) Less obvious and less frequent, even if implementing (1) & (2), but just as important in the the end-outcome is mitigating deviations in risk exposures because of a known but unlikely sequence. Imagine playing 100 blackjack tables and counting cards and making the appropriate wagers given the count. Ideally and likely, the games are uncorrelated. Yet, what happens if the games become correlated in the participant's favor and wherein the 'run' occurs all the same time but doesn't get monetized all at the same time? Would you resize new wagers to this new level at that specific table given the new significantly increased bankroll? The answer is no, which may appear counter intuitive, if the games are not correlated and one is showing the correct discipline in sizing wagers going forward. The problem resides in that your large 'winners' may still be in active games where you have large yet-to-be-monetized gains but relative to the current bankroll is not proportional to the new wagers.

We point this out, as this sequence is itself uncommon when correlation is attempted to be mitigated, yet does occur. Making sure this 'basis' risk is mitigated, where the individual games are not viewed in isolation but rather in the context of the whole bankroll, is critical at those particular moments to mitigate drawdowns. You don't want your large mathematically significant winners (in dollars) to be equal to mathematically insignificant losers (in dollars) because of an unusual sequence.

Curious Changes in Portfolio Exposures

We wanted to point out some noticeable movement in exposures over the past week that we find curious.

- (1) As we stated a few weeks ago regarding biotech and healthcare stocks, we are now seeing this rotation come to fruition.
- (2) A majority of the decline in net exposure in AMER is driven by this, not new shorts. Yet, significant realized profits (as we pointed out with CELG, and now GILD) have been monetized. This is irrespective of 'beta' as many lower vol names (PFE, MDT, BMY) have had equivalent movement in vol-days.
- (3) We have noticed a change in net exposure to many G20 rates, especially those that are tied to US monetary policy.

As always, we have clear fundamental ideas why this has happened given shifts in what the market perceives in the superposition of the probabilities of a series of potential outcomes. Yet this doesn't factor into our directional basis or exposure. Rather the latter only occurs as realized volatility and price trajectory change concurrently, thereby dynamically altering our time perspective. Again our win ratio is only 55%, but our profit factor is high as a result of capturing the large movement that represents the majority of the price trajectory.

In the aggregate we are noticing a change in the way risk is allocated across our global opportunity set. Given our opportunity set, we have the ability to notice these transitions more than most.

Best Regards,

Michael J. Fowler

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