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ABSOLUTE FOCUS FUND

Perennially behind the Curve

After five consecutive months of losses (and a cumulative decline of 17% in the local currency FT World Share Index), stock markets were due a bounce and the promise from European leaders to come up with a comprehensive and credible plan to tackle the euro-zone crisis before the G20 Cannes summit provided the catalyst. We find it hard to reconcile, however, the content of what was announced with the biggest monthly gain in the FT World Share Index since April 2009 and, staggeringly, the best month for the US's S&P Composite Index since December 1991. Neither the European Financial Stability Fund's proposed increase in size to €1trn nor the €106bn of new capital which will supposedly make the euro-zone's banks bullet-proof are enough. Similarly, the revised debt restructuring plan which hopes to cut Greece's debts to 120% of GDP by 2010 (merely twice the figure permitted under the Maastricht criteria for a country to adopt the euro) is a joke. Demonstrating how hopelessly behind the curve the euro-zone's policymakers continue to be, the spotlight in Europe has already shifted with the bond markets of Italy, Spain and even France moving now in the crosshairs. Yields in Italy's €1.9trn bond market have recently breached the critical 7% level, Spain's are heading the same way and France is suffering the ignominy of having to pay almost 2% more than Germany to borrow.

We are not overly disappointed that Absolute Focus's performance in October compares unflatteringly with the gains in stock market indices or even with peer-group returns (the HFR Funds of Hedge Funds Index was up by 1.4%). Our vastly superior performance in the preceding five months can be attributed to precisely the same reason and that is that we are striving to provide an investment which is genuinely hedged. The bottom line is that investors in Absolute Focus have made money year-to-date (albeit not a lot) and, even after October's extraordinary rally, the FT World Share and HFR indices are still down by 5% and 4% respectively. Additionally, share prices of Absolute Focus are just 1.5% below their all-time highs (set in August this year) whilst the FT and HFR indices are still respectively 20% and 12% adrift of their October 2007 peaks.

Very sharp rallies in stock markets are every bit as challenging for our strategy as steep falls. Cash-heavy investors,

fearful of underperforming their benchmarks and peers, are left scrambling to catch up and this can lead to even bigger rises in so-called higher 'beta' and more speculative shares. For example, whilst the US's S&P Composite Index rose by 11% in October, the smaller company Russell 2000 Index was up by 15%. The outperformance of lower quality shares resulting from this behaviour makes short-selling particularly difficult and managers can suffer exaggerated losses in short investments. Thus, our 6% aggregate allocation to two defensively-positioned funds was disproportionately costly in October, reducing overall performance by almost 0.5%. We are kicking ourselves about the timing of our switch from USLS10 into USLS8 at the beginning of October. Although USLS8's manager is first and foremost a short-seller, the fund pursues a 'balanced' investment strategy and net market exposure has varied between -20% and +40%. The fund has also made money every year for investors since it was launched in 2003 and so this was an exciting discovery. However, USLS8 had made huge returns in August (+5%) and September (+9%) as key 'short' themes in China and solar energy paid off and we should have been wary of a rebound and delayed our investment. Prior to October, USLS8's biggest monthly loss was less than 4% but the fund is still up by 14% year-to-date. A good investment badly timed – mea culpa.

With the euro-zone crisis entering a potentially dangerous phase, we are certainly sleeping easier having almost halved Absolute Focus's aggregate exposure to European equity long/short funds at the end of October. We are confident that we can re-deploy the money more profitably and more safely elsewhere. In this respect, the pipeline of potential new investments, particularly in the US, at various stages of our due diligence process is strong and competition for a place in Absolute Focus's portfolio is fierce. In the last few months, we have added new investments in Divisar and Compenio and our level of overall conviction is extremely high. We are determined to translate that conviction into competitive returns for Absolute Focus's investors.

Charles Hovenden & Andrew Wheeler
21st November 2011

Results

Share Class	NAV	October 2011		Year-to-date	
		Fund (%)	FT World (%)*	Fund (%)	FT World (%)*
Class A - US\$	US\$122.39	(0.01)	+10.68	+0.52	(3.63)
Class B - £	£124.00	+0.05	+6.82	+0.79	(6.53)

*Index in the currency of the respective share class – Source: FT/Bloomberg

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Biggest 5 Holdings as at 31st October 2011

Name of Fund	Size %	Strategy	October (%)	Year-to-date (%)
USLS3	9.3	US Equity Long/Short	+0.9	+41.6
USLS2	7.8	US Equity Long/Short	+0.3	+10.1
JELS1	7.2	Japanese Equity Long/Short	+0.2	(0.2)
EELS2	7.1	European Equity Long/Short	+0.3	+4.2
JELS2	6.9	Japanese Equity Long/Short	+1.9	+16.3

Best 3 Funds in October

Name of Fund (size)	Strategy	October %	YTD%
USLS9 (3.4%)	US Equity L/S	+2.2	+0.0
USLS1 (3.4%)	US Equity L/S	+2.1	+2.7
USLS6 (6.8%)	US Equity L/S	+2.0	+4.8

Worst 3 Funds in October

Name of Fund (size)	Strategy	October %	YTD%
USLS8 (3.0%)	US Equity L/S	(9.3)	+13.6
PI1 (3.4%)	Portfolio Insurance	(4.6)	(1.6)
USLS7 (6.7%)	US Equity L/S	(2.2)	+19.2

Full Track Record & Summary Statistics (Class B - £)

	Jan	Feb	Mar	Apr	May	June	July	Aug	Sept	Oct	Nov	Dec	Year
2005									0.98	(0.05)	0.77	1.83	3.57
2006	2.13	(0.19)	0.94	0.99	0.25	(0.99)	(1.61)	0.88	0.32	(0.36)	0.30	1.86	4.55
2007	0.23	1.12	1.08	0.59	1.72	1.17	0.17	(0.11)	0.66	2.59	(0.87)	0.70	9.39
2008	(0.65)	0.76	(0.51)	0.54	0.57	0.93	0.27	0.19	(0.72)	(1.01)	1.12	0.24	1.72
2009	0.60	0.15	(0.69)	(0.99)	1.48	0.02	(1.18)	0.05	0.57	(0.12)	(0.15)	0.72	0.43
2010	0.00	0.03	0.47	0.28	(0.83)	(1.35)	0.68	(0.09)	0.75	0.59	0.66	0.49	1.67
2011	0.64	1.03	(0.05)	(0.15)	(0.19)	0.27	0.76	(1.61)	0.06	0.05			0.79
Annual Rate of Return	3.55		Sharpe Ratio (@ 3% risk free)				0.19		Biggest Monthly Loss			(1.61)	
Standard Deviation	2.88		Correlation FT World Index (Local)				0.30		Biggest Peak-to-Trough Drawdown			(2.58)	

Source: Absolute Fund Managers LLP

General Information

Description: Equity-focused fund of hedge funds
Firm AuM: US\$81.3m/£50.4m
No. of Holdings: 17
Share Classes: US\$, £ and Euro
Basic Fee: 0.50% p.a.
Incentive Fee: 15% of profits
High Water Mark: Yes
Dealing: Monthly (with 35 days notice for redemptions)
Min. Investment: US\$100,000
Fund Domicile: Cayman Islands
Listing: Irish Stock Exchange

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Source: Absolute Fund Managers LLP