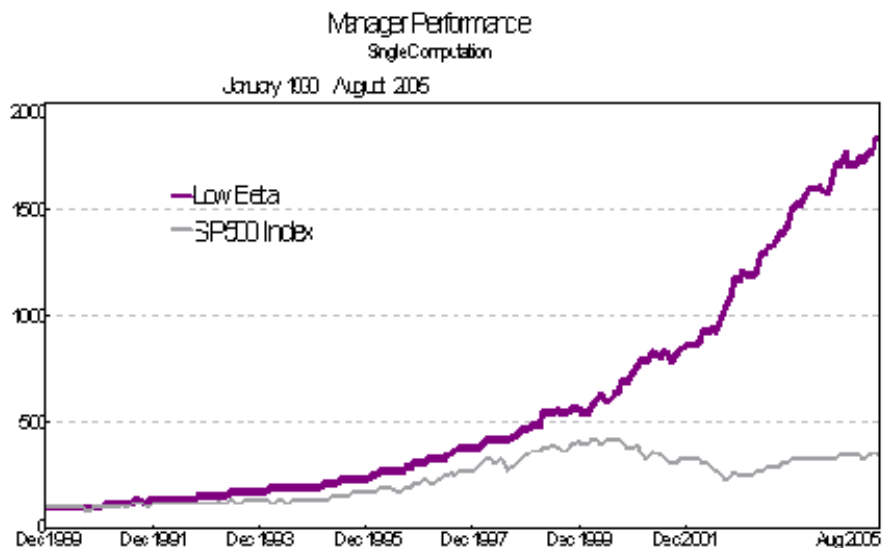


The D050 Volatility-Protected Market Neutral Equity Fund – a Modern Interpretation of Hedge Fund Strategy

Proteom's proprietary algorithmic modelling and trading platform facilitates the design of customized equity strategies to suit specific investment objectives. A case in point is the D050 strategy, which was designed as a market neutral strategy with additional downside risk protection. The strategy, which is unlevered, incorporates not only the customary long and short equity components, but also integrates a long-volatility hedge, implemented with a combination of variance swaps and VIX futures. The investment universe comprises the S&P500 index member stocks, and the portfolio typically holds an average of 200 names, with approximately monthly turnover.

	2005 YTD (Aug)	3.73%
	2004	18.17%
	2003	27.94%
From Inception	Annual Return	20.40%
	Volatility	8.41%
	Alpha	14.76%
	Beta	-0.05
	Sharpe	1.92
	Information Ratio	0.89
	Max Annual Drawdown	-7.04%
	Avg. Annual Drawdown	-4.09%



Long Volatility Hedge and its Benefits

Volatility increases non-linearly during market declines, which means that it provides a more effective offset than an equivalent short equity position alone. The non-linear behaviour of volatility provides a greater cushion of support for the strategy against extreme market conditions, resulting in lower drawdowns (averaging just over 4% annually). Moreover, because volatility behaves asymmetrically, increasing more in market downturns than it declines during market rallies, the hedge overlay creates less of a performance drag during up-market periods.

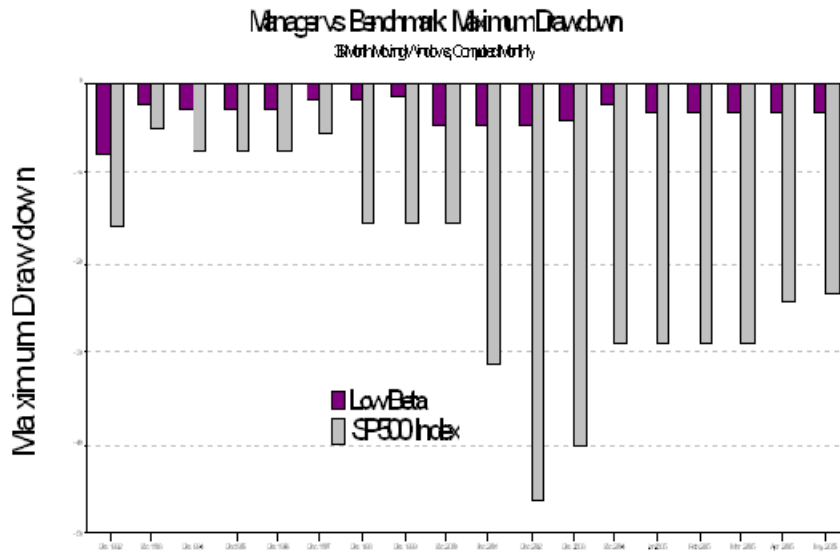
These characteristics are well illustrated in the period 2000-2003.

	2000	2001	2002	2003
Fund	28.66	18.55	35.73	27.94
S&P 5000	-10.14	-13.04	-23.37	26.39

During the market crash of 2000-2002, the strategy made substantial gains not only on the short equity position, but also on the long volatility hedge, due to the rapid increase in index volatility which accompanied the market downturn. In fact, the strategy also made money on the long equity component of the portfolio, resulting in a very substantial out-performance vs. the benchmark S&P 500 index. The volatility asymmetry effect enabled the strategy to participate fully in the market rally in 2003, despite the steady deterioration in volatility levels during the year.

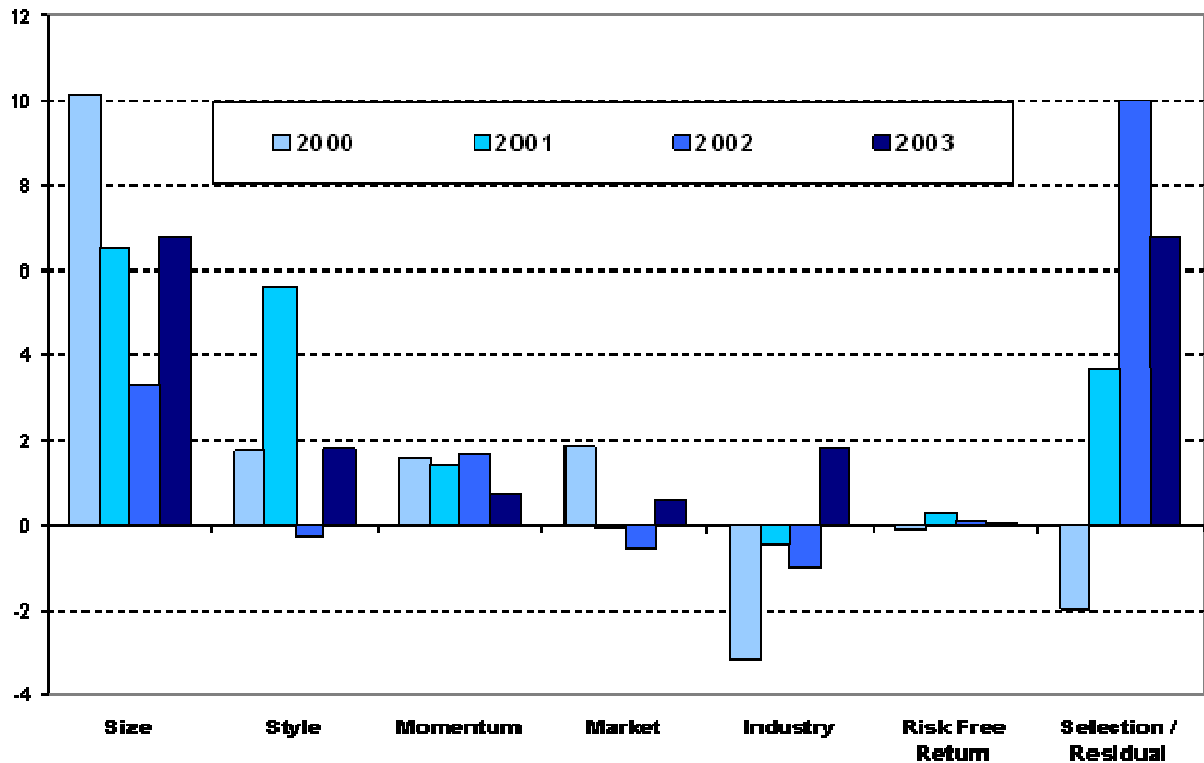
Lower Drawdowns

The hedging benefit of the equity-neutral/long volatility combination is clearly seen in the strategy drawdown, compared to the benchmark S&P500 index.



Alpha Generation

Another key ingredient of the strategy's successful formula lies in the algorithm's stock selection ability. Detailed analysis indicates that around half of the strategy alpha is derived from stock selection, while the remainder is derived from strategy style (see attribution analysis chart)

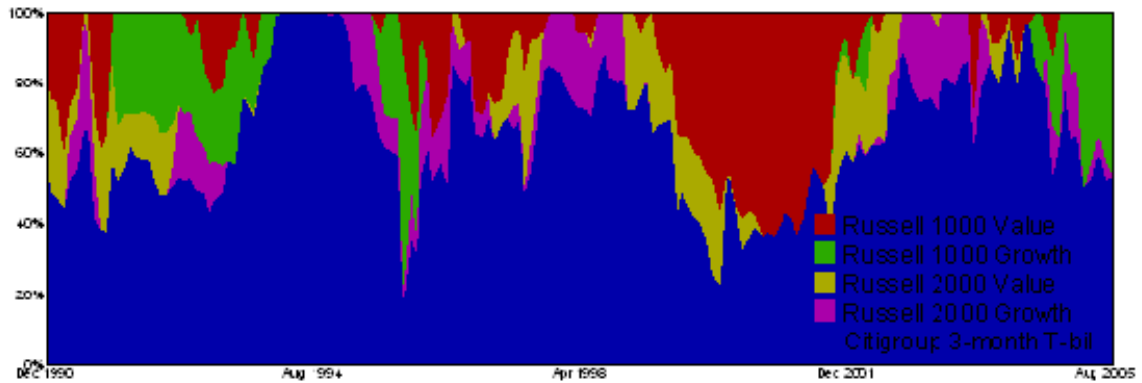
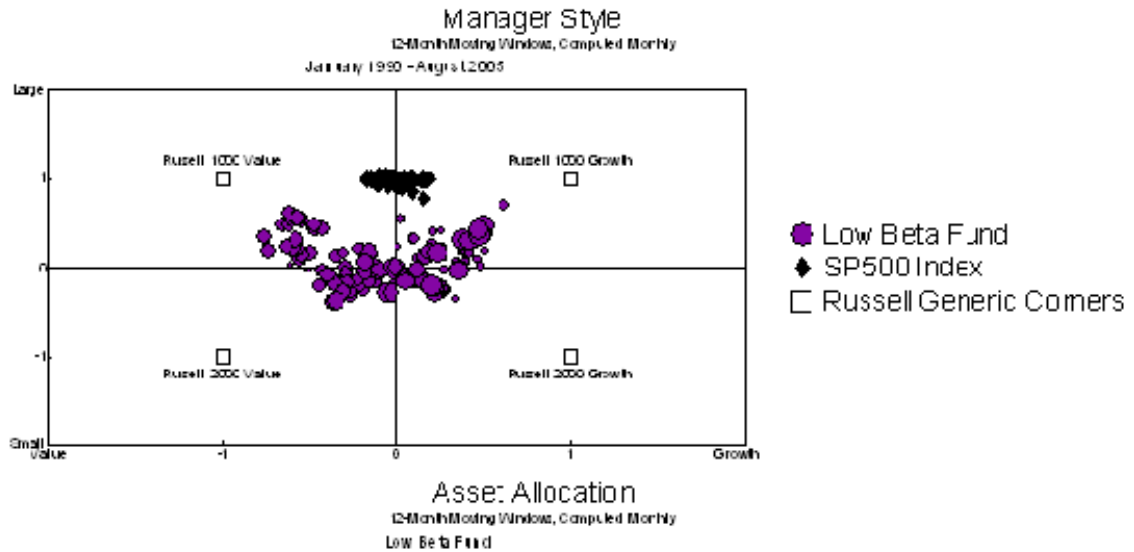


Stock Selection

A subtle feature of the model's stock selection capabilities lies in the ability to avoid losers as much as in its ability to pick winners. The algorithms track the behaviour of virtual traders who consistently lose money, or who make money inconsistently, and seeks to avoid similar behaviour in its own selection processes. This enables the strategy to avoid the money-losing strategies that typically result from the behaviour of traders who tend to trade irrationally during difficult markets.

Style

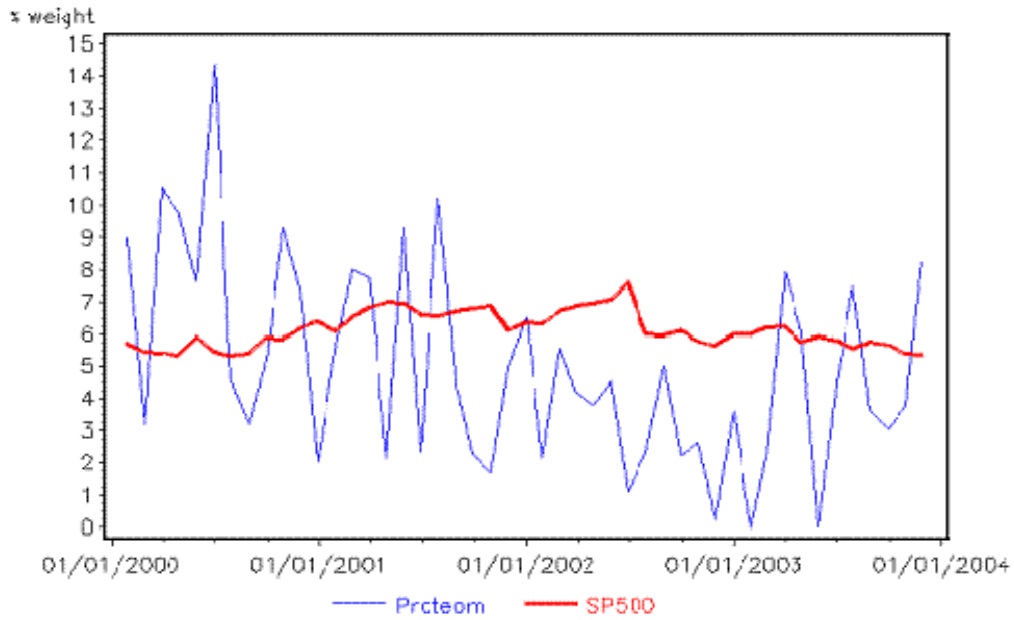
Although it tends to favour value stocks over the long term, there are significant variations in strategy style from month to month as illustrated in the following charts. Here we can see the algorithms steadily increasing the allocation to value stocks over the mid-to late 1990's as the equity bubble formed and eventually burst (in 2000). This ability to adjust the style of the strategy to suit market conditions contributes substantially to its robustness and ability to outperform under adverse market conditions.



Diversification, Sector Rotation

Yet another source of strategy alpha lies in the model’s ability to identify sectors that are likely to under- or out-perform. Although overall every sector is fully represented in a typical portfolio holding of over 200 S&P index member stocks, the strategy will rotate into or out of sectors that the models judge to be relatively strong or weak. Average turnover is relatively slow – usually around 3%-5% daily - but during certain market conditions, for example when the market is trading sideways, the model will often favour higher turnover trading strategies with shorter holding periods. The chart below gives an indication of how the model has chosen to underweight or overweight allocations to the energy sector, relative to the benchmark index.

Proteom Capital Management v SP500
Sector Weighting 2000-2003
SECTOR=ENERGY



More information about Proteom Strategies, including performance analysis, files of returns and sample portfolios, can be downloaded from our web site at www.proteomcapital.com.