East Lodge Capital Investor Letter December 2014

East Lodge Capital Credit Opportunities Fund

East Lodge Capital Partners LLP ("East Lodge") is a London based investment management firm founded by Alistair Lumsden in August 2013. The East Lodge Capital Credit Opportunities Fund ("The Fund") is focused on opportunities across the global structured finance and direct lending markets, with a particular focus on investments in the European space.

Performance Since Inception[1]

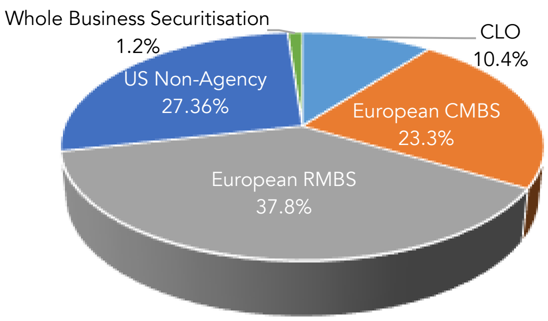
	JAN	FEB	MAR	APR	MAY	JUN	JUL	AUG	SEP	OCT	NOV	DEC	YTD*
2014				4.27%[2]	1.21%	1.81%	0.54%	-0.42%	1.05%	-0.55%	-0.39%	-0.48%	7.15%

*Fund launched in April 2014

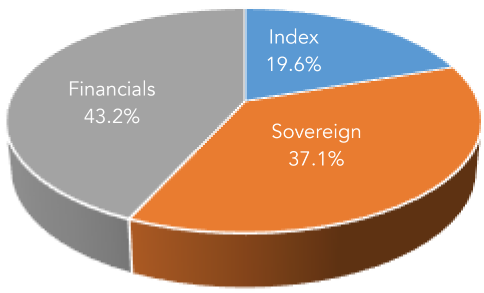
Assets Under Management

Fund AUM as at 1st December 2014	Firm AUM as at 1st December 2014
$577,990,000	$577,990,000

Long Credit Exposure (LCE)



Short Credit Exposure (SCE)



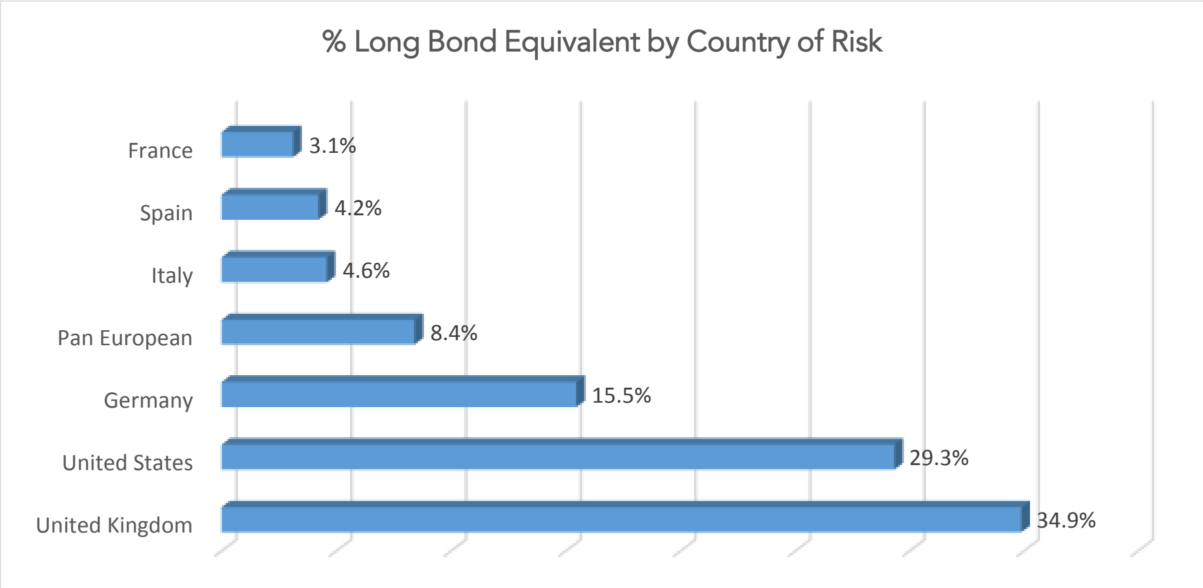
Portfolio Summary as at 31st December 2014

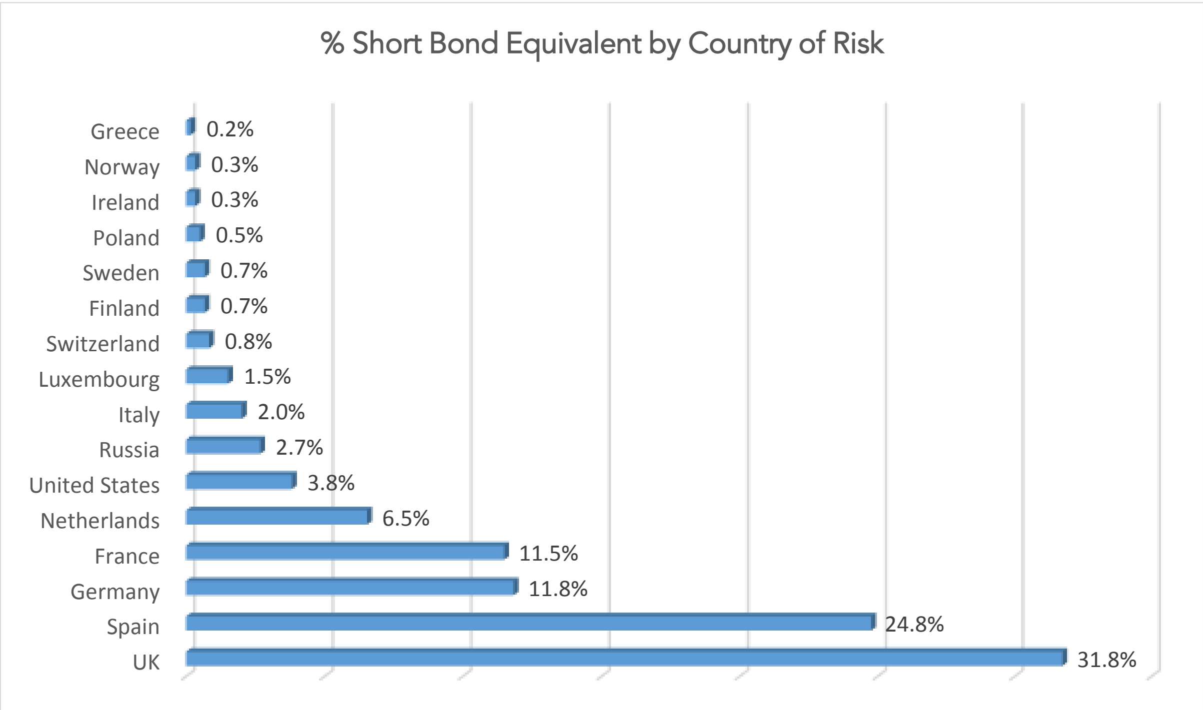
Total Long Credit Exposure as % of NAV	Total Short Credit Exposure as % of NAV
166.4%	45.2%

[1] Performance shown is the weighted average returns of the Class A Shares of the East Lodge Capital Credit Opportunities Fund, Ltd. for April 2014 – June 2014, and the weighted average return of Class B Shares for the Offshore Fund for July 2014 onwards and are shown net of fees and expenses. The returns are unaudited. Please see disclaimer for further details.

[2] Performance for April 2014 reflects the capping of certain Fund expenses. In addition, as only principal capital was invested in the Fund during the month of April 2014, no management or performance fees were charged (which fees, had they been charged, would have had the effect of reducing the returns shown).

Country Analysis as at 31st December 2014

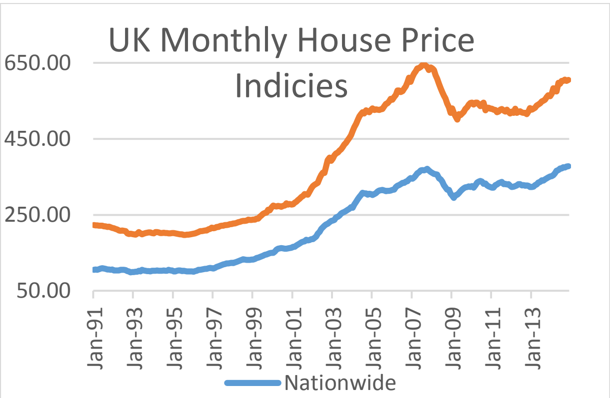




Commentary

December saw a challenging environment for risk assets, especially longer duration assets, as a mix of political news headlines and holiday liquidity brought about a cautious tone. The CLO book was flat on the month as the demand technical re-established itself after the wave of November supply whilst the shorter duration of the European CMBS helped ensure more buoyant marks and positive performance in this part of the portfolio. The sector that experienced the most pressure was certainly European RMBS and, to a much lesser extent, US Non-Agency RMBS, where mid-month strength failed to translate itself into a strong month-end, as illustrated by a widening in bid/ask spreads versus a lowering of offer levels.

European RMBS

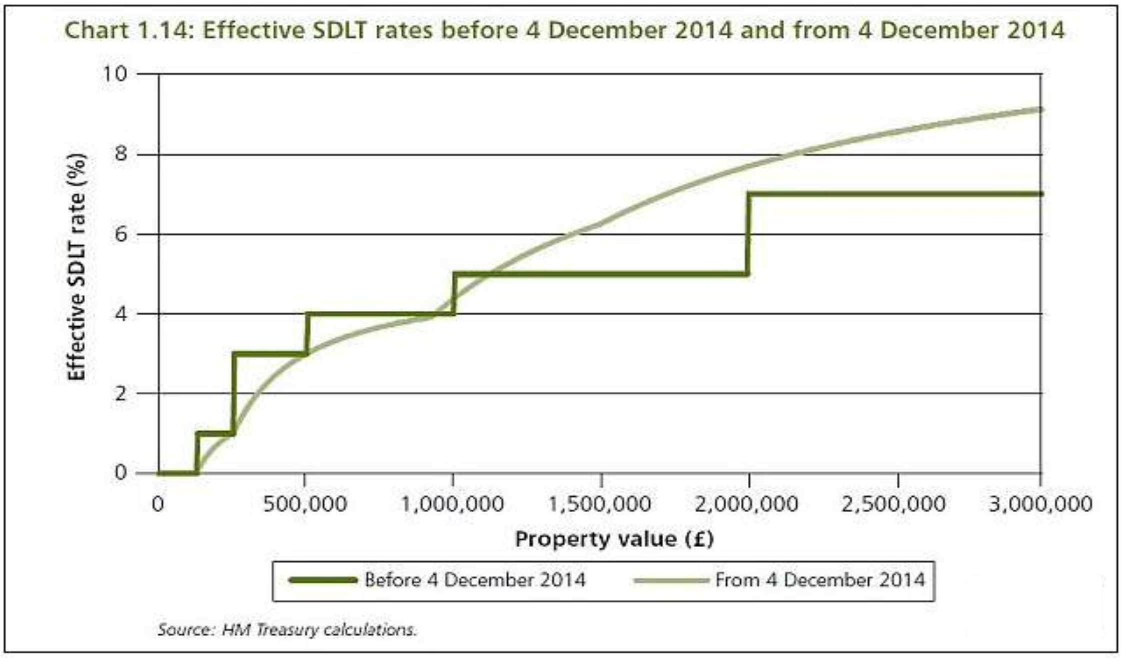


Dec-14	**Halifax**	**Nationwide**
Annual Change	7.80%	7.20%
Quarterly Change	0.30%	1.10%
Month Change	0.90%	0.20%
Average Price	188,858	188,559
From 2007 Peak:	-5.39%	2.20%
Q4 2014		
Best Performing Region	N. Ireland (+9.4%)	London (+2.5%)
Worst Performing Region	North (-2.3%)	Wales (-0.6%)

UK

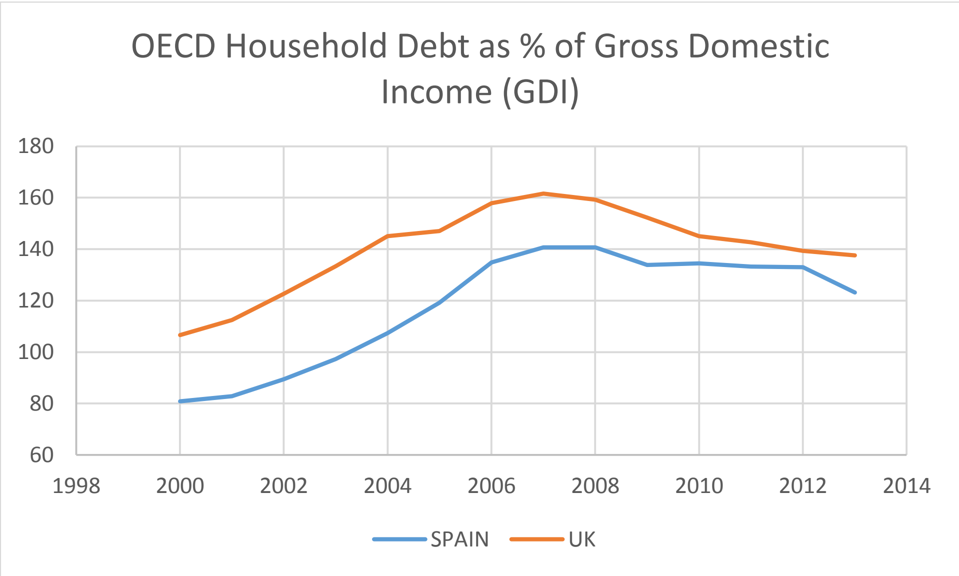
The UK experienced a solid year of price growth as the above graph and statistics show, but the pace of house price appreciation slowed into the close of the year. News headlines tended to be phrased negatively and focused on the slowing rate of increase, which is not the same concern as an expected drop in house prices. Indeed consensus forecasts point to 3-5% price appreciation in 2015 that may well be focused outside of London and the Southeast given the increase in regulation to prevent profligate credit being extended at high lending multiples. The market does remain buoyant, and the last quarter of 2014 saw a significant rise in first-time buyer lending. October's figures from the Council of Mortgage Lenders (CML) showed £4.4bn was advanced which represents a rise of 12% on the prior month and 14% on the prior year.

The big news for the path of house prices at the lower end of the price spectrum was announced in the Chancellor's Autumn Statement on December 4th 2014 when Stamp Duty, a transaction tax paid by the house purchaser, was changed from the old 'slab' system to being levied progressively. Under the slab system, the rate was charged on the entire balance of the purchase price, naturally suppressing prices from rising past the thresholds into the next tax band given the step up in tax paid. For example prior to the change, a house purchased at £249,999 paid £2,500 in tax, but at £250,001 a levy of £7,500 was due – under the new system it would be £2,500.03 at the higher price (as shown below). Given our exposure to the typical non-conforming borrower is on properties at the lower end of the pricing spectrum, valuations in the collateral backing our assets should improve as this change works its way through the system.



Since our last quarterly update, fixed mortgage rate deals have continued to drop, with 5-year fixed rate credit now available at 2.48% (by comparison this was 2.89% three months ago). It is not only the high street lenders that are chasing this low rate business as shown by the specialist lender Platform introducing a 2-year fixed rate product at 1.64%. Dependent on the path of UK interest rates, fixed mortgage rates have room to drop further given the spread to swaps on the cheapest fixes is currently of the order of 60-70bps which is multiple times higher than the spread on a typical fixed loan product in 2006/07 when lenders were competing harder for the business. The Bank of England (BoE) data shows that fixed lending continues to be popular, as the proportion of gross advances at fixed rates increased for the eighth consecutive quarter to 82.6% in Q3 2014, the highest proportion since the series began in 2007. Given the backdrop of a growing UK economy and the higher proportion of fixed rate debt, it can be argued borrowers are, in general, better setup to deal with a rate rise than you might expect, however with the potential for a disorderly outcome of the UK general election on May 7th 2015, it may be late 2015 or even 2016 before we see a rise.

The price action seen in the UK Non-Conforming mortgage backed product was mixed into year-end. Despite continued strong collateral performance aided by cheaper mortgage credit availability, "lower for longer" rates to aid debt servicing costs and rising house prices, the bid for this longer duration risk suffered. The duration on many of these profiles make for lower cash prices and thus provide convexity to the upside on a move tighter but can languish when there is less sponsorship of the sector. Most of the pressure in the sector came from an abundance of senior risk profiles being sold into the close of the year, with one dealer in particular pushing prices lower as they cleared their balance sheet for year end. This led to softer month end pricing, despite the stronger performance in remittance reports and the lack of availability of any sizeable offerings at these levels. We continue to find this sector appealing, and look to add paper as more becomes available in the New Year.



Spain

House price data released during the fourth quarter by the Instituto Nacional de Estadística showed a small rise of +0.3% year-on-year driven by a quarter-on-quarter rise of +0.2%. While this is not as exciting as the improvements in the UK housing market, stability is certainly welcomed. Further improvement can be seen throughout the economic data, for example, the latest numbers available from the Spanish Ministry of Labor show unemployment has dropped to a two year low and that during the quarter, household debt declined further back to 2006 levels as shown on the above chart. This illustrates the painful deleveraging that has gone on in Spain is now starting to reap rewards, which should, eventually, lead to increased demand as households repair their balance sheets.

With this continued stability, and as a result of deleveraging of the economy as a whole, lenders are finding comfort with the economic situation and are willing to extend credit once again – even the weaker financial institutions appear keen to get in on the act after passing the ECB stress tests. For example, this quarter saw Bankia ask EU authorities to relax the lending restriction imposed during the bank restructuring despite them having one of the highest non-performing loan (NPL) ratios even after transferring some of their worst assets to SAREB (Spanish bad bank). Were Bankia to be successful in relaxing these restrictions, it would undoubtedly be a positive development for credit availability and likely speed up the recovery in the housing market.

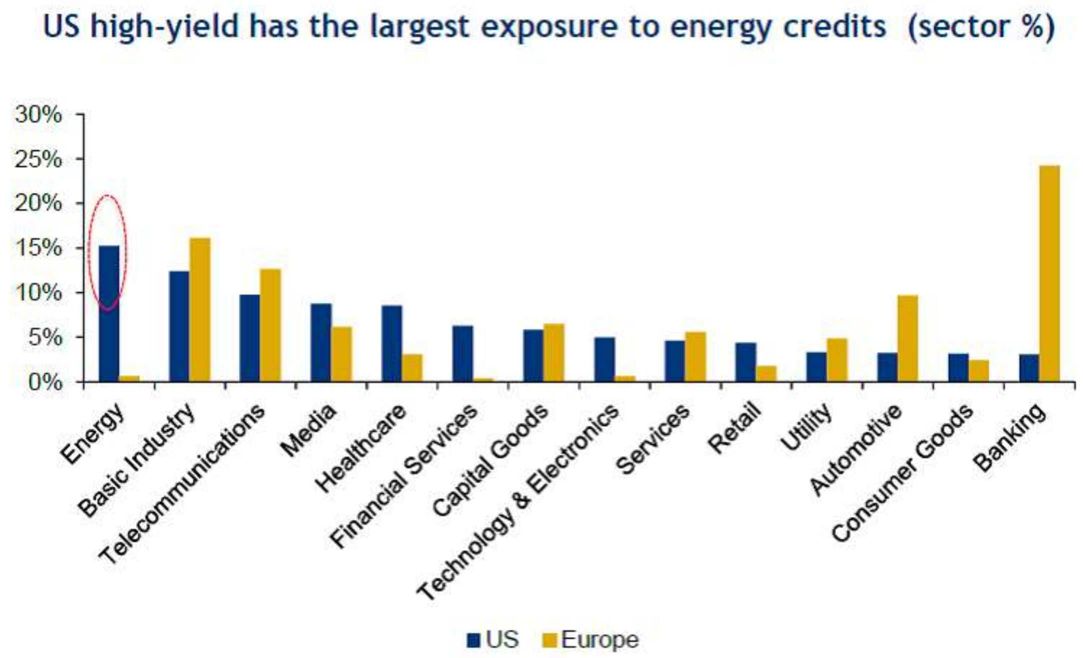
The Spanish securitization market had seen some spread tightening on the back of expectations of large amounts of purchases from the ABS purchase program (ABSPP). We had previously highlighted that we expected more of the purchases to come from primary rather than secondary, and thus lower purchase amounts running into year-end was not a surprise. After five weeks of operation, the four mandated managers had bought €1.7bn with €1bn coming in the last week before the Christmas hiatus. The market also traded a little softer into year end, despite the fundamental performance continuing to meet or exceed expectations. We had an upside surprise in a large prepayment of Spanish mortgages on one of our top ten holdings, approximately five times larger than expected for the quarter.

CLO

Given the volatility in High Yield (HY) credit during the fourth quarter of the year it was unlikely that the levered loans that back our CLO investments would emerge unscathed. Of course, given the better credit position in senior secured loan debt over unsecured HY bonds, it fits that there was less volatility in loans outside a few idiosyncratic credit stories that continue to play out in Europe. Despite the better performance of the underlying, a congested primary CLO issuance pipeline in November – 15 deals attempted to launch which would have represented approximately one third of 2014 issuance – put pressure on spreads to the point that the new deal economics broke down and postponed or delayed deals into 2015. The "2.0" issuance market in Europe is still maturing and will no doubt put this bump in the road behind it in the New Year assuming stability in the credit backdrop.

The quarter saw pressure on a number of food/retail names in Europe, predominately in HY bond issuance, including Iceland (UK frozen foods), Hema (Dutch retail) and Takko Modemarkt (German discount retail), to name a few. Given the typical bond bucket in a "2.0" CLO is rather small (0-10%) the exposure to these sectors and specifically to these names can be minimized without too much difficulty with appropriate deal selection. In terms of loans that are on our watch list, (i.e. when we are reviewing managers, we specifically screen for exposure to these names) the story of Van Gansewinkel Group (VGG), the Dutch waste management company previously known as AVR, continues to rumble on with the sponsors CVC and KKR putting the company on the block for sale. However the bids seen were disappointing, and we do not expect a resolution before April 2015.

By contrast, the story for US CLOs in the quarter focused on companies involved in the energy sector given the shock in oil prices. European CLO deals typically have less than 1% exposure to the energy sector while their US equivalents will typically have exposure of 5-10% which is well below the equivalent US HY bond index, where the exposure is 15%+ (as shown in the chart below), but substantively higher than our European CLO investments. Our exposure to US CLOs is a much smaller part of the portfolio, at less than 2%. The deals we own have single digit percentage exposure to the energy sector and, in our view, have sufficient subordination to be protected as the situation unfolds, but we are watching this closely. As ever, not all energy companies are created equal, and some can be found to have strong assets, for example established fields or drilling equipment that is already well let for 2015, and when defensively funded at low leverage multiples (1.5-3x EBITDA much below the typical 4-4.5x for the first lien loan market) can make interesting opportunities to build credit subordination in the CLO if prices are impacted on the back of macro headlines for deals ramping up their portfolio or still in their reinvestment window.



As the year closed two important regulatory items were published. The European Banking Authority (EBA) released a report that included recommendations on what would count as appropriate risk retention to help the market better understand what might be considered "loopholes and abuse". This was a positive step as it gave greater clarity to market participants that the originator structures in use by certain managers, such as GSO Capital Partners, would be appropriate for risk retention. Across the Atlantic, the US released their finalized rules for risk retention under Dodd-Frank, which CLO vehicles will need to meet starting December 24th 2016. The rules appear workable, but it will take some time for managers to ensure they fully comply with these new requirements which will likely lead to some tweaks to structures and a reduction of primary issuance in 2015, particularly for smaller managers unable to commit the long term capital to retain the appropriate slice of risk. The main disappointment of these two pieces of regulation is that they are not fully harmonized, meaning that on the face of it, European risk retention compliant deals would not initially be complaint for US risk retention. As the year progresses, however, structures will undoubtedly be created to meet both sets of rules.

The outlook for 2015 is one of reduced supply that should in turn lead to tighter spreads. In addition, as the legacy "1.0" issuance continues to pay off and more deals are called, market participants will be forced to focus more on "2.0" issuance which should increase liquidity; currently "2.0" secondary trading accounts for only 15% of the volume of a typical top tier CLO dealing desk. We continue to see the sector as offering value and look to add strong seasoned deals on weakness when the product is available.

European CMBS

The European Commercial Real Estate (CRE) recovery continues to gain momentum - yields have come down in prime markets, and investors are now being directed to secondary markets throughout Europe for increased yield opportunities. As Moody's reported, "CRE investment activity is strong in Europe, up 24% year on year to the third-quarter of 2014, which has supported the work-out of defaulted loans. High investment levels reflect the relative attractiveness of the CRE markets for investors seeking higher yields. Because of increased competition for prime assets in core markets, lenders have shifted their attention to secondary assets and peripheral markets such as Spain, Italy and Portugal. Moody's expects further growth in lending activity outside core markets in 2015.

The seasonal drop in liquidity in CMBS appeared to happen very early this year. There was a dearth of activity from both sellers and buyers from mid-November through to the end of December. A number of factors outside of the usual "seasonal effect" contributed to the lack of activity. Many CMBS participants experienced a solid 2015 and therefore had little motivation to put results at risk prior to the New Year. In addition, CMBS was not immune to the weakness seen across all markets into year-end, and caused many participants to avoid putting new capital to work in December. Also, as expected, the ECB is taking its time to deliver on the ABS purchase program which caused the dealer community to be long ABS into year-end.

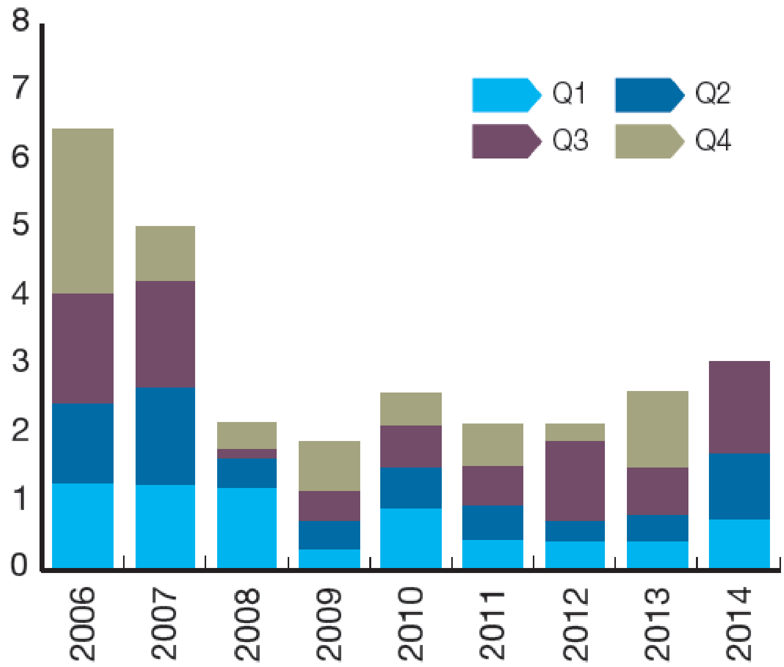
Prices in European CMBS remained relatively flat throughout the quarter. October was an Interest Payment Date (IPD) for much of the CMBS universe and we experienced several pay downs, some anticipated and some unexpected. November and December were very quiet months allowing the market to take a breath and market participants to catch-up on surveillance with quarterly servicer reports released. As 2015 came to a close, the number of notices that were released regarding sales, pay downs and restructurings increased ahead of the January IPD. We are noticing increased signs of life in the CRE markets with a number of valuations re-assessed upwards and a continuation of underlying property sales. In the final weeks of the year, several dealers once again became more aggressive with their bids, and we expect to see this carried over into the New Year.

As we commented in our November letter, one of the greatest surprises to the CMBS market this quarter was the explicit inclusion of CMBS in the ECB purchase program. The initial excitement was quickly diluted as the market realized that no CMBS deals currently meet the eligibility criteria, therefore its inclusion was largely theoretical. Among the restricting criteria: deals cannot be structured (i.e. have a junior loan) and require different loan level reporting to the criteria currently followed. In December, we saw the issue first hand with a new CMBS transaction (DECO 2014-BONX) announced, priced and placed. This transaction failed to meet the reporting standards and thus did not meet the eligibility criteria. There are a number of deals in the pipeline for 2015, but it remains to be seen whether the current criteria can be met, and thus the senior bonds placed with the ECB.

The new issue CMBS transaction, DECO 2014-BONX, was the first new issue transaction since October and one of the largest (€680 mm) of 2014. The transaction is a single loan secured by a portfolio of 29 offices located throughout Germany. The largest tenant, Allianz Deutschland, comprises circa 55% of the income and the overall occupancy stands at 89%. The Day 1 LTV was 69.1%, with an Interest Coverage Ratio (ICR) of 3.06x and initial debt yield of 8.5%. Given the lack of new issuance recently, the strong pay downs experienced in November and anticipated pay downs in January, it came as a surprise to many market participants that the deal struggled to get over the line. The deal had to be widened at all levels in order to be fully subscribed. In the end, the deal was priced at 125bps for the 'AAA' rated Class A and 345 bps for the BBB rated Class E. Pricing levels were wider than initially guided, and the widest of all issued 2014 CMBS transactions.

As we have identified before as one of our investment themes, the recovery in the UK commercial property market isn't now solely based in London. Recoveries in the UK's key regional markets are proceeding apace. Tenant demand in Q3 2014 was reported at its highest in four years and 40% above the five yearly quarterly average. With development slow to follow, headline rents are beginning to grow. Investment activity in the regional office market saw £1.03bn of transactions, the highest since Q3 2007. As the chart below highlights, total volume for 2014 to date (through Q3) stands at £3.1bn, which eclipsed the annual total for each of the last six years.

Regional office investment volumes
(£bn)



Source: Property Data

Prices for European commercial real estate rose 7% during Q3 2014, reflecting the continuing demand for assets in non-core markets. DTZ's latest European transactions index showed prices were 11% higher than a year ago, although still 13% below the previous peak in Q2 2007. CBRE reported that commercial real estate investment in Europe totalled €48.4bn in Q3 2014, a 27% increase on Q3 2013 and 4% higher than Q2 2014.

Ireland and Spain are close to reaching record breaking levels for commercial real estate investment in Europe. Ireland achieved a peak level in Q3 2014 with €1.6bn of investment, surpassing the previous high of €1.5bn in Q3 2006. In Spain, the €3.5bn invested in Q3 2014 was the country's second highest quarter on record.

Q1 2015 will be an important period for the new issue market, which promises to be the over-riding theme for the quarter with a number of transactions rumored to be in the pipeline and several jurisdictions believed to be considered including Ireland, UK and Italy. The early part of 2015 will help the market assess whether the pricing of the DECO 2014-BONX was solely due to seasonal market factors or if there is greater concern for the transaction or the European CMBS market as a whole. We believe it was much more of a seasonal effect, and as the market continues to shrink with the pace of repayments and work-outs we anticipate strong demand for new issue paper with many people having cash to put to work. It will be interesting to see whether CMBS reporting can meet the ECB purchase program eligibility criteria. If originators can finally get over the hurdles around eligibility, we could see a significant number of deals come to market in 2015. European CMBS continues to offer good relative value and we expect demand levels to remain strong.

Whole Business Securitization

The whole business securitization market is dominated by the pub groups – with a number of pub companies having securitization debt. This is typically an operating company / property company structure (opco/propco).

As we reported in our November letter, the sector was badly impacted by the news that the House of Commons had voted through parliament a bill requiring pub companies that have tied management agreements to offer tenants an option to pay a market rent instead. The tied tenancy is an old practice dating back many years, however, as wet-led (beer) sales have declined in recent times, the pub industry began to adjust toward a greater focus on food sales. Tied tenancy agreements have been on the decline and less pub companies have utilized them with a change to the managed and franchise business models. The ruling therefore had the greatest impact on those groups that hadn't reflected the changes – most notably Punch Taverns and Enterprise Inns.

As the bill is being passed through Parliament and amendments are made and agreed upon, the ultimate impacts remain unclear, but as a result of the bill, virtually all pub names have been impacted and tarnished to some extent (although some more than others.) We believe this may prove to be a buying opportunity, particularly in those names that are not impacted or are less impacted, but whose price has declined in sympathy.

Given the timing of Christmas this year and the relatively good weather experienced in the UK over the holiday period, we expect sales to have been strong and this is being backed up by early trading indications released over the first few weeks of January. As the impact of the bill becomes clearer, several pub companies will stand out above others and we believe there will be opportunities to capture good relative value. We also anticipate that the buying pressure of the ECB will filter through to the WBS market. It is perhaps seen as more esoteric, and for this reason can trade wider to standard securitization and corporate bonds, and while the WBS market isn't ECB eligible, we believe the buying of eligible assets will force real money buyers in particular, to look to alternative markets such as WBS.

US Non-Agency

Other than the temporary blip in October, spreads on legacy non-agency remained firm throughout the fourth quarter, and trading volumes remained robust right into year-end. Spreads softened only slightly as the market shut down for the holidays, with a widening in bid ask as opposed to a lowering of offer levels. Overall, the outlook for non-agency spreads is positive. The combination of continued strong demand and lack of new supply should provide a solid foundation for the market. The non-agency market is currently about $750 billion in outstandings. Since the deals pay down about 15% per year, the market will shrink by about $110 billion in 2015. $75 billion of this will be a return of principal which will need to be reinvested so this should provide good support for spreads. In addition, the NAIC (National Association of Insurance Commissioners) released new breakpoints which improved NAIC ratings, so insurance company demand for the bonds should increase as well.

Liquidity in Agency Credit Risk Transfer (CRT) deals continues to be an issue. From the end of September, spreads on the lowest tranche of the CRT deals widened about 80 bp, although December was unchanged. New deals in October and November pushed spreads substantially wider, while the lack of issuance in December helped keep the market quiet. New deals are expected in both January and February, while secondary trading has been fairly thin. Both FNMA and FHLMC are aware of the liquidity concerns and are attempting to address them. 2014 issuance in CRT totalled $10.8 billion, with similar volume expected in 2015.

Winter is upon us. The Case Shiller 20 City index was down 0.1% in the most recent release (October data) leaving the year over year change at up 4.5%. This was 6.7% at the end of the third quarter. The strongest performers over the past year included Miami (+9.5%), San Francisco (+9.2%), Las Vegas (+8.0%) and Dallas (+7.6%). The weakest markets were Cleveland (+0.9%), Chicago (+1.9%), New York (+2.0%) and Phoenix (+2.1%). Unlike this same point last year, the range of outcomes is much tighter as most cities have reverted back toward the national average. Looking forward into the winter season, the next several months show the weakest seasonal housing price growth. In each of the winter months, expected house price growth is close to 1% below the average so this will have a dampening effect on the non-agency universe. However, the combination of low rates (10-year Treasury down to 2.17% in December from 2.49% in September, the FHLMC 30-year mortgage rate down to 3.87% from 4.19%), solid economic growth (unemployment down to 5.8% from 6.7% at the start of the year) and a declining percentage of distressed sales (down 22% this year) should keep HPI solidly positive in 2015. Most forecasts are in the range of 3.5% to 5.0% growth.

Despite an overall slowing of voluntary prepayments in the colder months, the trend continues towards improved borrower performance. Over the past three months, 60+ delinquencies are down 50 bp in Alt-A, 64 bp in Pay Option ARMs (POA) and 72 bp in subprime. Voluntary prepayments were somewhat mixed with Alt-A down 0.3 CPR, subprime falling 0.9 CPR and POA rising 0.5 CPR. Liquidations fell 0.6 CDR in Alt-A and 0.9 CDR in POA, while rising 0.5 CDR in subprime. Loss severities rose 6.1% in Alt-A and 1.8% in POA while dropping 5.2% in subprime. We continue to like the better performance characteristics in POA and the higher geographic concentrations in the higher HPA states. Solid economic growth combined with improving house prices should allow the trend of improving borrower performance to continue into 2015. Despite the improving performance, one area which is less likely to show improvement is loss severities on the deals themselves. Since the percentage of liquidations in judicial states continues to rise, this will create upward pressure on overall severities, at least in the short run. Judicial states have longer liquidation timelines which translates into higher loss severities.

On the political front, while everyone acknowledges the need for expanded credit availability, U.S. Congress has been unable or unwilling to provide relief. This seems unlikely to change in the foreseeable future, however, the FHFA and FHA, in the absence of congressional action, have taken steps to expand availability to low income and first time home buyers. Overall improving economic conditions are also extending credit to additional borrowers as economic growth, house price inflation and low mortgage rates make more borrowers eligible for existing alternatives. Borrowers below 80 LTV show substantially higher prepayment rates than borrowers between 80 and 100 LTV. As borrowers can demonstrate a longer clean payment history, financing opportunities open up as well. Typically, a 24 month clean payment history makes financing much easier, however due to uncertain legal liability, lenders remain cautious. As the CEO of Bank of America recently stated "I don't think there's a big incentive for us to start to try to create more mortgage availability where the customers are susceptible to default."

While the start of payments on settlements has appeared imminent for some time, it seems 2015 may finally be the year. Bank of America seems likely to pay in 2015, with the next court date set for February 2015 and fewer objectors blocking the path as Bank of America negotiates side agreements with some objectors. In December, Trustees on the deals in the Citigroup settlement, acting largely in line with expectations, accepted the proposed settlement on the majority of the 68 deals included in the offer. The settlement was rejected for 7 collateral groups (across 4 deals) and the deadline was extended for two other loan groups. The bankruptcy court for Lehman approved the protocol for loan file review, setting claim deadlines of June 2015 and March 2016.

Financials/Short

It has been a volatile quarter as the market wrestles with turmoil in Greece, the price of oil, Russian aggression and geopolitics and an increasing divergence between the US and European macro backdrop. In contrast, it also awaits fully-fledged quantitative easing [QE], with the ECB's balance sheet still short of implied targets at €2.15trn following a total €213bn TLTRO take up plus Covered bond and ABS purchases. Supportive comments from ECB council members influenced market levels strongly throughout the quarter and helped support peripheral bonds in December.

First, looking at Greece. In mid-October, the market became concerned about Greece's ability to exit its bailout programme. Comments on policy from US politicians, a reduction in Greek haircuts and rumors of ECB corporate bond buying drove a partial recovery a week later, and into the December 4th ECB meeting it seemed everyone was long. Following the December 8th meeting of Eurozone ministers discussing bailout, the current European Financial Stability Facility (EFSF) programme was extended two months to the end of February 2015 and the Greek government announced it was bringing forward the presidential election by two months to December. On December 29th after three rounds of voting, Dimas garnered 168 votes, failing to receive the 180 required out of 300. Parliament must now be dissolved and general elections will take place on January 25th. Markets are particularly reactive due to the consistently leading position of leftist party Syriza in polls. Syriza wish to curtail austerity, achieve debt relief for the country and oppose troika intervention, albeit with a recently less draconian stance. While the situation is not as bad as it was in 2012, not least because Greece now runs a primary surplus rather than a substantial deficit, volatility looks set to continue, and it raises questions about whether Greek bonds could be included in any form of QE if it is announced, and when. We are also cognizant that both Portugal and Spain have general elections this year, the latter having the similarly leaning and newly formed Podemos in the running. The Greek election is just three days after the ECB meeting at which many are expecting announcement of full QE which further fuels speculation as to details on size, timing and nature of any QE such as the potential for national central banks to buy their own country's bonds, or only buying AAA bonds.

To add more spice to the mix, a plummeting oil price came to the fore, causing the Ruble to decline dramatically in mid-December as it went through 60 Rubles to the dollar. Recessionary Russia raised its key rate to 17% from 10.5% on December 15th only to see further depreciation to above 76 the next day, sparking discussions of capital controls. The next day saw a strong rally on stories of FX Intervention. According to BAML research, every $10 move in oil has a 100bp impact on Russian GDP, so at $60 oil, the Russian central bank is looking at a 2015 GDP for Russia of -4.5%, and brings geopolitics around Ukraine into focus which have helped boost Putin's approval ratings thus far. Oil driven volatility appears ongoing, and the potential boost to consumer spending as a result of more cash available post energy spend has to be weighed against the effect on inflation figures and a key target for the ECB, which brings us back to QE.

We had two stress tests in Q4; the long anticipated Comprehensive Assessment on October 26th and the UK's Prudential Regulation Authority (PRA) test on December 16th. To recap, the EU showed 25 banks failing with gross capital shortfalls of €24.6bn (net €8.5bn) and significant Asset Quality Review (AQR) write-downs (€136bn), especially in Italy and Greece. In November, some banks chose to take these in Q3 earnings whereas others didn't – we expect more to follow suit and view the stress tests as being the first step in the development of the ECB's new role as regulator. Most focus was on the Common Equity Tier 1(CET1) ratios post-test, but we think looking at an institution's fully loaded Basel III ratios and minimum leverage ratios is more interesting. In the UK, the PRA test ran scenarios for eight institutions: Barclays Bank, Co-operative Bank, HSBC Bank, Lloyds Banking Group, Nationwide Building Society, Royal Bank of Scotland, Santander UK and Standard Chartered. As expected, Co-op failed (albeit rather more spectacularly than anticipated with a result of a -2.6% CET 1 ratio). This test was more stringent than the ECB's despite its lower threshold rate of 4.5% for the adverse scenario. The adverse scenario includes a house price decline of 35% (the EBA ran 20% for the UK and 15% for the Euro area) as well as a greater Commercial Real Estate stress. The test also included base rate spikes, (again no deflation) and there were methodology differences such as dynamic balance sheet assumption, whereas the EBA test used static balance sheets.

The Financial Policy Committee (FPC) took a less pass/fail approach than the European Banking Authority (EBA) with other factors taken into account such as leverage ratios, hence its comments that Lloyds and RBS "needed to strengthen their capital position further." The FPC report specifically mentioned that the treatment of deferred tax assets had been checked after RBS had to restate their EBA's adverse scenario result in November by 103bp to 5.65% only just passing the 5.5% hurdle rate due to an error calculating these. The FPC also indicated that an explicit leverage ratio threshold would be set in future. Only the Co-operative Bank was required to submit a revised capital plan which has been accepted and no system-wide, macroprudential actions were judged to be needed.

Projected CET1 capital ratios in the stress scenario:

	Actual (latest 2q14, 3q14)	Actual (end 2013)	Minimum Stressed Ratio (before 'strategic' management actions)	Minimum Stressed Ratio (after 'strategic' management actions)
Barclays	10.0%	9.1%	7.5%	7.0%
Co-operative Bank Plc	11.5%	7.2%	-2.6%	-2.6%
HSBC Bank Plc	11.2%	10.8%	8.7%	8.7%
Lloyds Banking Group	12.0%	10.1%	5.3%	5.0%
Nationwide Building Society	17.6%	14.3%	6.7%	6.1%
The Royal Bank of Scotland Group	10.8%	8.6%	5.2%	4.6%
Santander UK	11.8%	11.6%	7.9%	7.6%
Standard Chartered Plc	10.5%	10.5%	8.1%	7.1%

Oh, what a tangled web we weave in the work of regulation and policies, with new minimum levels, timelines, jurisdictions, company structures and how they inter-relate and drive institutional behavior. All the following came up during Q4: risk weighted ratios versus absolute leverage, risk weighting reviews, loss absorbing capacity, buffer capital, accounting treatments and Global Systemically Important Financial Institutions (G-SIFIs). A quick overview….

The UK's leverage ratio was set between 3 and 4.05%, depending on the institution. The ratio comprises a 3% minimum requirement plus supplementary buffers of 35% of the corresponding risk weighted systemic and countercyclical leverage buffers. Leverage ratios challenge those institutions with low risk weightings i.e. mortgage lending and investment banking operations. The Total Loss Absorbing Capacity (TLAC) Framework proposal followed, a process that is far from complete and not due for implementation until January 2019 but sets probable requirement for loss absorbing instruments to be at 16-20% of risk weighted assets and definitions for eligibility. Here the challenges are for institutions with higher risk weightings and larger deposit bases. The EBA also published its consultation paper on Minimum Required Eligible Liabilities (MREL) which is the EU's version of TLAC. The Financial Stability Board's (FSB) update on G-SIFIs lowered UBS and Credit Agricole capital buffers from 1.5% to 1%. In mid-December, the Federal Reserve proposed capital surcharges for US banks that are stricter than FSB requirements and take into account short term funding; only JP Morgan falls short under these proposals. And finally, UK banks will have to use their deferred tax assets more slowly as the Autumn Statement proposed restricting the amount of profit that can be offset by carry-forward losses. This doesn't affect capital itself but rather dampens future internal generation of capital.

"Recurring One-offs" are set to continue. There is progress on known issues but corrections to reserves seem likely into year end. We have sanctions, FX, anti-money laundering and RMBS issues filtering through for the European banks as well as a couple of remaining US banks. This quarter's list of "one-offs" include…more Payment Protection Insurance (PPI) mis-selling in the UK, albeit tailing off; Citi, JPM, RBS, UBS and HSBC settled $4.3bn with regulators for FX misconduct; The New York Department of Financial Services (NYDFS) installed monitors at Deutsche Bank and Barclays and is investigating both institution's trading algorithms with respect to FX. Neither participated in the group settlement; Barclays apparently withdrew due to the NYFDS issues and its £500m fine was confirmed by the CEO as insufficient. Similarly, other stated reserves may be lacking, e.g. JPM by up to $5.9bn. Citigroup announced a Q4 charge of $2.7bn for existing FX, LIBOR and anti-money laundering issues. Commerzbank is in line for approximately $1bn for anti-money laundering/US sanction breaches, roughly $400m more than thought, and RBS may face a fine of more than £5bn in the context of provisions of £1.9bn for Federal Housing Finance Agency. Away from banks, Ocwen looks to be fined $150m by the NYDFS, and key man, Bill Erbey is being forced out. The potential impact of the settlement going forward on Ocwen could be far reaching. They will be subject to management oversight, further loan files must be released, MSR acquisition is curtailed and monitors have been put in place. As a result, and at the very least, revenue growth will be restricted at the same time as costs inevitably increase. The impact at certain related companies that rely on Ocwen-derived business could be greater.

European Direct Lending

Within the scope of the Side Pocket, a number of opportunities have been, and continue to be under negotiation and/or due diligence during the quarter. Focus remains upon the funding of both existing and new commercial real estate projects within the UK and mainland Western Europe, specifically in the office and light industrial sectors. Funding proposals have ranged from the short-term "bridge" in nature, to longer, three to four year maturity profiles. Structurally, we continue to seek enhanced returns by negotiating, where appropriate, a form of hybrid structure; providing secured traditional funding combined with an element of equity participation to share in the potential "upside" the sponsor will achieve through the provision of our funding.

The nature of commercial real estate-backed funding leads itself to often protracted periods of negotiation. This can range from lender/borrow, to the negotiation of inter-creditor agreements between lenders, to further discussions between borrower and vendor, in the case where financing is being negotiated pre-purchase. That said, we anticipate that our first investment into this space will occur during January, with a pipeline of further opportunities under advanced discussion/negotiation.

Glossary

EFSF	European Financial Stability Facility
TLTRO	Targeted Long Term Refinancing Operation
PRA	Prudential Regulation Authority
AQR	Asset Quality Review
CRE	Commercial Real Estate
FPC	Financial Policy Committee
FSB	Financial Stability Board
EBA	European Banking Authority
DTA	Deferred Tax Asset
G-SIFI	Global Systemically Important Financial Institution
TLAC	Total Loss Absorbing Capacity
PPI	Payment Protection Insurance
NYFDS	New York Department of Financial Services
CET 1	Common Equity Tier 1

Gross Return Attribution by Strategy as at 31st December:

Strategy	Attribution (%)	LCE (%)
CLOs	0.00%	10.37%
European CMBS	0.02%	23.26%
European RMBS	-0.20%	37.83%
US Non-Agency	-0.10%	27.36%
Whole Business Securitisation	0.01%	1.18%
Hedge	0.05%	N/A
Financing	-0.09%	N/A
Total Return (%)	**-0.31%**[3]	**100.0%**

Ten Largest Positions by Sector as at 31st December:

Position	Sector	Seniority	% of Portfolio
1	European RMBS	Senior	3.34%
2	European RMBS	Senior	3.01%
3	European RMBS	Senior	2.08%
4	US Subprime	Mezzanine	2.04%
5	European CMBS	Senior/Second Pay	2.03%
6	US POA	Senior	2.01%
7	European CMBS	Senior/Second Pay	2.0%
8	European RMBS	Residual	2.0%
9	European RMBS	Mezzanine	1.89%
10	European CMBS	Senior/Second Pay	1.87%

[3] Gross return used for attribution purposes. See disclosure notes that follow.

Stress Tests

Stress Test	Result (% NAV)
Equities -10%	0.0013%
Equities +10%	-0.0013%
Corporate Credit Spreads -25%	-0.58%
Corporate Credit Spreads +25%	0.50%
Equity Volatility –5 pts	0%
Equity Volatility +5 pts	0%
FX -10%	-0.10%
FX +10%	0.10%

VaR

VaR (1 Day 95%) (% of Nav)	0.33%

Long Equity Delta	Short Equity Delta
0%	0.013%

ASC 820

Category	% LCE
Level 1	0%
Level 2	98.0%
Level 3	2.0%

Estimated Liquidity

Category	% LCE
< 30 Days	38.02%
30-60 Days	59.98%
>60 Days	2.00%

East Lodge Capital Investor Letter December 2014

Fund Terms

Minimum Investment ($ mn)	1
High Water Mark	Yes
Side Pocket	Optional (subject to 20% limit)
Redemptions	Quarterly
Redemption Notice	90 days[1]
Gate	25% (Investor-level)
Management Fee	2%[2]
Performance Fee	20%[2]

Lock	1 year soft[1]
Prime Brokers	Bank of America Merrill Lynch Barclays Bank Plc
Administrator	Wells Fargo Global Fund Services LLC
Auditor	EY
US/UK Legal Counsel	Schulte, Roth & Zabel International LLP
Cayman Legal Counsel	Mourant Ozannes

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[1] Redemption notice must be provided in writing no later than 90 days prior to the end of the quarter in which a redemption is requested. In the event a redemption is made from the fund within 12 months following an investor's initial investment, a 4% redemption penalty will be applied

[2] Refers to fees for Share Class B

Legal Disclaimer

This document contains general information on East Lodge Capital Credit Opportunities Fund Ltd. (the "Offshore Fund") and East Lodge Capital Credit Opportunities Fund LP (the "Domestic Fund", each a "Fund", and together with the Offshore Fund, the "Funds") which are managed by East Lodge Capital Partners LLP ("East Lodge").

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An investment in either Fund is speculative and involves a high degree of risk and there is no guarantee that the Fund's investment objective will be achieved. Opportunities for withdrawal/redemption and transferability of interests are restricted, so investors may not have access to capital when it is needed. There is no secondary market for the interests and none is expected to develop. The Master Fund's portfolio, which is under the sole trading authority of East Lodge, is a credit strategy with a focus on securitized products and this lack of diversification may result in higher risk. Please see the Memorandum for a more detailed description of the risks involved with an investment in the Funds. An investor should not make an investment unless he/she is prepared to lose all or a substantial portion of his/her investment. The fees and expenses charged in connection with this investment may be higher than the fees and expenses of other investment alternatives and may offset profits. [i]

Past performance of the Funds should not be construed as in indicator of future performance.

Any projections, market outlooks or estimates in this documentation are forward looking statements and are based upon certain assumptions. Other events which were not taken into account may occur and may significantly affect the returns or performance of the Funds. Due to market risks and uncertainties, any projections, outlooks or assumptions should not be construed to be indicative of the actual events which will occur.

Fund Net Performance

Performance shown is that of Class A Shares of the Offshore Fund for April 2014 – June 2014, and Class B Shares for the Offshore Fund for July 2014 onwards. Returns are unaudited and are shown net of all fees and expenses, though we note that the April 2014 performance number reflects the capping of certain Fund expenses. In addition, as only principal capital was invested in the Fund during the month of April 2014, no management or performance fees were charged during that month (which fees, had they been charged, would have had the effect of reducing the returns shown). In addition, an individual investor's rate of return may vary based on the terms of its subscription and the timing of its investment in the Fund.

Portfolio Statistics

Unless otherwise noted, all portfolio statistical information shown is for the Master Fund and is calculated by East Lodge and is unaudited. Portfolio information is as at the date shown; accordingly, the current portfolio of the Fund may vary, sometimes materially, from that shown.

- Long Credit Exposure (LCE): Shows asset class exposure as a percentage of total long credit exposure at month end mark to market.

- Country Analysis: Shows country of risk for each long credit asset as a percentage of total long credit exposure; where a security has more than one country of risk, the largest country of risk for that security is used.

- Gross Return Attribution by Strategy: Shows an estimate of the gross return attribution of the various long and short fund exposures. Any FX and funding costs are assumed to be distributed pro rata amongst the various asset classes based on profits.

- Estimated Liquidity Profile: reflects the liquidity profile of the long credit portfolio using the following methodology:
  - < 30 days Senior tranches
  - 30-60 days Large exposures >$50m, 2nd lien senior bonds, mezzanine ABS
  - 60-90 days Residuals, CLO tranches rated below BBB

- ASC 820 classifications are unaudited and are estimates assigned solely by East Lodge. East Lodge makes no representation as to the accuracy of such classifications.

- Stress tests are calculated by East Lodge and reflect estimated impacts due to changes in FX rates and the impact of changes in credit spreads on the Funds' financial holdings.

- VaR is calculated by East Lodge using simulations based on historical portfolio price information derived from Markit Partners.

Direct Lending

Please note that the examples discussed are representative of the investment opportunities that are currently available to the Fund; however, there can be no guarantee that such investment opportunities or similar opportunities will be made by the Fund. The Fund's investments may be materially different than the examples discussed.

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[i] We are pleased to announce that Greg Bennett has joined Nick Gaze at Danesmead Partners as at Jan. 1, 2015. To that end, we have terminated our director services agreement with The Harbour Trust Co. Ltd effective Dec 31 2014.