

Seeking to add Alpha and Downside  
Protection to a Diversified Portfolio

**HDGE**

AdvisorShares Ranger Equity Bear ETF



Sub-Advised by Ranger Alternative Management, L.P.



## Disclosures

There is no guarantee that the Fund will achieve its investment objective. An investment in the Fund is subject to risk, including the possible loss of principal amount invested. The Fund may invest in (or short) ETFs, ETNs and ETPs. In addition to the risks associated with such vehicles, investments, or reference assets in the case of ETNs, lack of liquidity can result in its value being more volatile than the underlying portfolio investment. Other Fund risks include market risk, equity risk, short sales and leverage risk, large cap risk, early closing risk, liquidity risk and trading risk. Short sales involve leverage because the Fund borrows securities and then sells them, effectively leveraging its assets. The use of leverage may magnify gains or losses for the Fund. See prospectus for specific risks and details.

Before investing you should carefully consider the Fund's investment objectives, risks, charges and expenses. This and other information is in the prospectus, a copy of which may be obtained by calling (877) 843-3831 or by visiting the website at [hedge.advisorshares.com](http://hedge.advisorshares.com). Please read the prospectus carefully before you invest. Foreside Fund Services, LLC, distributor.



## Executive Summary

- The AdvisorShares Ranger Equity Bear ETF (NYSE Arca: HDGE) sells short individual stocks based on detailed analysis of earnings quality and aggressive accounting methods.
- HDGE seeks to produce gains when the stock market falls.
- The ETF structure gives HDGE the benefit of having daily liquidity so investors can enter and exit the Fund based on their needs, and full transparency, so investors know exactly what the Fund is invested in.
- Because of the benefits of daily liquidity and transparency, the strategy may be useful for swing traders and long-term investors alike.
- HDGE seeks capital appreciation regardless of market direction.



## HDGE/s Role in a Diversified Portfolio

- May offer downside protection and reduced portfolio drawdown during the bear phase of the stock market cycle
- Potential to reduce portfolio volatility during fast declines within the bull phase of the stock market cycle
- May reduce portfolio correlation to benchmark indices



## HDGE Overview

### Disciplined and Repeatable Investment Process

- Central to the HDGE strategy is a **forensic accounting evaluation on each company** in the portfolio, rather than limiting the scope to companies that may only have fad products or broken business models
- A forensic accountant dissects a company's financial statements, crunching the numbers in search for evidence that the data may suggest operational deterioration or manipulative sales and revenue recognition.

### Experience

- The strategy is managed by a portfolio management team with over 30 years of combined short selling research and investment experience.



## HDGE Overview - Why HDGE?

	<b>HDGE</b>	<b>THE POTENTIAL HDGE ADVANTAGE</b>
<b>PHILOSOPHY</b>	FOCUSED ON ACCOUNTING FORENSIC-BASED SHORT IDEAS	DEDICATED EXPERTISE
<b>PORTFOLIO SELECTION</b>	DIVERSIFIED ACROSS INDUSTRIES AND SPECIFIC COMPANIES; FOCUSED ON CATALYSTS THAT DRIVE LOWER STOCK RETURNS	LIQUIDITY FOCUSED SCALABLE
<b>RISK MANAGEMENT</b>	TACTICALLY MANAGE POSITIONS; LOWER SHORT INTEREST STOCKS	TACTICALLY MANAGE RISK
<b>RISK OF STYLE</b>	ACCOUNTING CONCERNS COULD ABATE	CONSISTENT APPROACH



## HDGE Overview - Portfolio Construction

**HDGE has a two-pronged approach to short selling:**

- “Core” Fundamental positions are established based on earnings quality analysis.
- “Tactical” trading positions are utilized to add exposure in bull or bear markets, which assist the portfolio in circumnavigating the market

**The combination of both core fundamental positions and tactical trading positions seeks smoother performance and consistent alpha.**



## HDGE Overview - Investment Process

IDEA GENERATION	FUNDAMENTAL ANALYSIS	TECHNICAL ANALYSIS	POSITION SIZE
<ul style="list-style-type: none"> <li>- QUANT SCREENING</li> <li>- QUALITATIVE ANALYSIS</li> <li>- 3RD PARTY CONSULTANTS</li> </ul>	<ul style="list-style-type: none"> <li>- ANALYZE SEC FILINGS (10-K, 10-Q, 8-K)</li> <li>- CONFERENCE CALLS</li> <li>- DEVELOP SUSTAINABLE EPS MODEL</li> </ul>	<ul style="list-style-type: none"> <li>- STOCKS IN DOWNTRENDS</li> <li>- AVOID IBD 100-TYPE STOCKS OR MOMENTUM SECURITIES</li> <li>- EMPHASIZE LOW SHORT INTEREST TO MITIGATE SQUEEZE RISK</li> <li>- CONSIDER SHORT REBATES</li> </ul>	<ul style="list-style-type: none"> <li>- TYPICALLY 2-7% POSITIONS</li> <li>- MANAGE EXPOSURE VIA TECHNICAL ANALYSIS</li> <li>- TYPICALLY 20-50 STOCK PORTFOLIO</li> </ul>



## HDGE Overview - Investment Process: The Income Statement

Income Statement	
Line Item	Concern
Revenue	Aggressive Revenue Recognition
<u>Cost of Goods Sold</u>	Inventory Issues
<u>Gross Margin</u>	Inventory & Reserve Concerns
Sales & Marketing	Reserve Concerns
R & D	
General & Admin	
<u>Restructuring &amp; Other</u>	Serial Charges
<u>Operating Expenses</u>	
<u>Operating Income</u>	
<u>Income before Taxes</u>	
<u>Provision for Taxes</u>	Tax Issues
<u>Net Profit</u>	
<u>Share Count</u>	

**MOST CRITICAL**

**LEAST CRITICAL**

**Hierarchy:** HDGE ranks a company's warning signs in direct proportion to where they reside on the income statement. The higher up the warning sign, the greater the concern for the company.

**Revenue:** This is the highest concern. If the revenue is fictitious, then the entire financial model for the company is questionable.

**COGS/Gross Margin/Operating profits:** HDGE looks for unsustainable sources of margin expansion. For example, analysts will often cheer a company that creates a reserve in one quarter and then reverses it the next period. Writing off inventory in one quarter and then selling it the following quarter creates a 100% gross margin profit boost. However, rising margins attributable to accounting maneuvers like this are not generally sustainable.

**Ratio Adjustments:** A company's adjustment to P/E, P/CF, and/or P/S may indicate questionable accounting issues.



## Potential Active ETF Advantages over Inverse Index ETFs

**Inverse index ETFs suffer from a negative compounding effect, which impacts both leveraged and unleveraged ETFs.**

- In a low-volatility downward-trending market, compounding can also result in longer-term returns that are less negative than the sum of the individual daily returns. In a volatile market, compounding can result in longer-term returns that are less than the sum of the individual daily returns.
- In a low-volatility upward-trending market, compounding can result in longer-term returns that are greater than the sum of the individual daily returns.

### **What does this mean for the investor?**

- Holding an inverse ETF may prove to be destructive for a portfolio as it can lead to undesired results. Inverse ETFs are meant to be held for periods of a day or less. Anything longer can result in a negative compounding effect due to tracking errors.



## Past Trade Example

### Conns, Inc (CONN)

Conns, Inc. is engaged in the specialty retail of durable consumer products in the US. The company's stores offer home appliances, which include refrigerators, freezers, washers, dryers, dishwashers, ranges, and room air conditioners. It also provides repair service agreements and installment credit programs, as well as various credit insurance products, such as credit disability, credit involuntary unemployment, and credit property insurance.

Due Diligence	Decision to Short	Exit Strategy
<ul style="list-style-type: none"> <li>CONN increasingly financed customer purchases with 94% buying on credit in late 2013 vs. 71% three years prior. CONN financed 80% of purchases itself compared with 62% two years prior.</li> <li>Delinquent accounts rose Y/Y 150 bps to 8.5% in Oct 2013.</li> <li>Accounts Receivable grew by 50% over last 2 years while inventory increased Y/Y for four consecutive periods.</li> </ul>	<p>CONN shares had a significant run up out-pacing fundamentals which were deteriorating. Shares became very overbought and as momentum waned, a short position was built.</p>	<p>CONN pre-announced a significant earnings miss and guided down for fiscal 2015. Guidance went from \$3.96 to \$3.40-\$3.70. Shares plummeted on the news (35-40%) and HDGE covered the position.</p>

References to specific portfolio holdings presented herein are for investment process illustration purposes only and are not recommendations to buy or sell any security. It should not be assumed that current investments and those made in the future will be profitable or will be equal to the performance of the securities listed herein. In addition, such holdings may not be representative of all or a portion of HDGE's current holdings or holdings purchased in the future.



## Past Trade Example

### 3D Systems Corp (DDD)

3D Systems Corporation, through its subsidiaries, operates as a provider of 3D printing centric design-to-manufacturing solutions in the United States, Germany, the Asia-Pacific, and other European countries. Its 3D printers convert data input from computer aided design generated software format or 3D scanning and sculpting devices to printed parts.

Due Diligence	Decision to Short	Exit Strategy
<ul style="list-style-type: none"> <li>• DDD ranked 1,000th out of 1,000 stocks in the HDGE earnings quality model at one point.</li> <li>• Spike in accounts receivables led to concerns of “channel stuffing.” Absent channel refill, revenue would have fallen several percentage points shy of estimates.</li> <li>• Consumer demand was well below internal company expectations.</li> <li>• DDD scored an “F” for shareholder yield in the HDGE model.</li> </ul>	<p>Shares of DDD had a significant run up in 2Q 2013 while earnings quality deteriorated further. Estimates for margins remained too high in the HDGE portfolio manager’s opinion.</p>	<p>DDD pre-announced earnings and had a significant share decline. After the price started to rally on weak volume, the position was added to HDGE again. Currently, shares are under significant distribution and momentum is weak.</p>

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## HDGE Portfolio Management Team

**John Del Vecchio, CFA** serves as a HDGE Portfolio Manager and Principal of Ranger Alternative Management, LP ("Ranger"). Mr. Del Vecchio has managed short only portfolios for Ranger since October, 2007. From 2003-2007, Mr. Del Vecchio served as an Analyst with David W. Tice & Associates / Behind the Numbers, LLC selecting short sale opportunities utilizing forensic accounting research on behalf of institutional clients and the Prudent Bear Fund.

**Brad Lamensdorf** serves as a HDGE Portfolio Manager and Principal of Ranger Alternative Management, LP ("Ranger"), and provides trading and market strategy for Ranger's short only portfolio. Mr. Lamensdorf has served as a Trading and Market Strategist for Ranger since 2009. Mr. Lamensdorf also served as principal and portfolio manager for Tarpon Capital Management, L.P., which managed long/short hedge funds. From 1992 through 1996, Mr. Lamensdorf worked on the equity trading desk for the Bass family in Fort Worth, Texas, where he co-managed an extensive equity portfolio with emphasis on short selling and derivatives strategies. He is also the CIO of the Lamensdorf Market Timing Report.

## HDGE Resources

To find all of the available resources for the HDGE ETF, please visit <http://hdge.advisorshares.com>:

- HDGE ETF Fact Sheet
- HDGE Investment Process Sheet
- HDGE Performance
- HDGE Monthly Portfolio Manager Commentaries
- HDGE Monthly Audio “Manager Minutes”
- HDGE Daily Holdings and Pricing

To learn more about the portfolio manager, Ranger Alternative Management, LP, please visit <http://www.rangeralternatives.com>



## Definitions

**Selling Short** - The sale of a security that is not owned by the seller, or that the seller has borrowed. Short selling is motivated by the belief that a security's price will decline, enabling it to be bought back at a lower price to make a profit.

**Drawdown** - The peak-to-trough decline during a specific record period of an investment, fund or commodity.

**Volatility** - A statistical measure of the dispersion of returns for a given security or market index.

**Correlation** — A statistical measure of how two securities move in relation to each other.

**Alpha** — The premium an investment earns above a certain benchmark.



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