Burford Capital (BUR:LN)

Muddy Waters Dreams of a Black Cat That Just Is Not There

"The hardest thing of all is to find a black cat in a dark room, especially if there is no cat."

Caro-Kann Capital LLC
September 9, 2019

www.caro-kann-capital.com

Disclaimer

The presented views and analysis are an opinion of Caro-Kann Capital LLC. Caro-Kann Capital LLC and / or its affiliated entities are long Burford shares. Various factors may influence or factor into the analysis or the opinion. The author does not assume any obligation to update the analysis.

About Caro-Kann-Capital

Caro-Kann Capital LLC is a research-intensive investment firm focused on small cap stocks. The firm was founded in late 2014 and is an exempt reporting advisor under the laws of the State of California.

Caro-Kann's investment philosophy is based on the principles of value investing. We are primarily drawn toward special situations and compounder opportunities.

The “Caro Kann Defense” is a well-regarded chess opening that emphasizes safety and encourages players to establish a defensible position before contemplating an offensive strategy. A strong foundational opening tends to lead players to more positive endgames. These principles guide our firm's investment strategy.

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"The hardest thing of all is to find a black cat in a dark room, especially if there is no cat."

* * *

This proverb[1] talks about a black cat that was not there. We think the same concept applies to recent attempts by short sellers to find corporate improprieties in Burford Capital (BUR:LN).

We provide a point-by-point rebuttal to the Muddy Waters short thesis over the next 50+ pages. We should note that we purposefully skipped certain points made by Muddy Waters because we felt that Burford's management has already responded to them in sufficient detail, and there was little value for us to be repetitive on those issues. We encourage everybody to read management's response and the full write up which follows, but we offer our consolidated perspective in the summary version below to whet your appetite. You can find a full ~70-page rebuttal on our website[2].

Muddy Waters asserted a number of claims throughout its 25-page report that Caro-Kann Capital wishes to take issue with:

Claim #1: Burford Categorized a Loss as an Investment with Significant Return and Might Have Acted in Concert with Its Own Largest Shareholder to Deceive

The strongest card in the Muddy Waters hand stems from claims that (1) Burford reported a profitable investment before the resolution of a case; (2) Burford's client, Napo Pharmaceuticals, subsequently *lost* the case that Burford funded, and (3) Burford and its largest shareholder, Invesco, who also happened to be an investor in Napo purportedly colluded to design a highly complex corporate restructuring to enable Burford to keep reporting its profitable investment. This was meant to be Muddy Waters' Mike Tyson uppercut, a good night and good luck to the Longs. Given the market's knee-jerk reaction to the report, it seemingly was.

But there is no smoking gun. Caro-Kann believes this point to be a *phantom punch*. The more facts and explanations Muddy Waters has demanded on this matter, the more disclosures Burford has provided. Burford has come out better looking as a result.

First, while Muddy Waters asserted that Burford inappropriately recorded *Napo* as concluded and reported high ROIC on the matter presumably in its attempt to impress investors with its track record, it turned out that Burford's reporting was in fact *conservative*. Here are a few illustrations:

- ✓ At the end of 2013 when Burford's entitlement became unconditional, Burford applied a discount of ~50% to the receivable on the balance sheet and the

[1] It appears almost impossible to trace the origins of this proverb.
[2] http://caro-kann-capital.com/#research

concluded case value in its non-IFRS investment data. To be more specific, the receivable and the concluded case investment were accounted at ~$15.75M while Burford was *legally* entitled to ~$30M.

- ✓ At the end of 2015 Burford did *not* include the effect of the accruing interest at a rate of 18%.
- ✓ At the end of 2016 Burford carried the Napo investment at ~$21.3M while it was legally entitled to ~$51.1M.

Why did Burford apply such a conservative approach? Burford did so because it was not certain about collectability of its entitlement. This shows thoughtfulness and conservatism as opposed to aggressiveness to impress investors with returns as implied by Muddy Waters.

Second, Burford's explanation of events matches several public documents, including:

- ✓ Settlement Agreement between Glenmark and Napo[3]
- ✓ Petition to Confirm Arbitration Award filed by Glenmark with United States District Court for the District of New Jersey – this is the very court document that Muddy Waters included into 2019-08-26 Report "Burford: Was MW Wrong About Napo?"[4] as an exhibit.

Third, Muddy Waters also *correctly* noted that Nantucket, Burford's affiliate that held Jaguar Health (e.g., successor to Napo) shares had its address of record listed in 2017 Proxy Statement that was *identical* to Invesco's global headquarters address. Muddy Waters did not comment on implications of this, but it would not be unreasonable to think that *at least some readers* (and probably a lot more than some) viewed this "cozy address sharing" as circumstantial evidence of concerted efforts by Invesco and Burford to orchestrate the entire transaction. The reality appears a lot duller: a careful review of *prior* and *subsequent* filings shows that Invesco's address listed as Nantucket's address was a result of a clerical error.

Claim #2: Deemed Recoveries Lead to Increased IRRs

Another key component of the short thesis relates to Burford's recovery practices. Muddy Waters asserts that Burford unjustifiably reported a higher IRR on an investment where it collected proceeds only a few years later. Muddy Waters cites the *Desert Ridge* case as a telling example of such "abuse".

We view the Desert Ridge case from a radically different perspective. In our opinion, *Desert Ridge* shows Burford's outstanding deal making abilities and a general commitment to shareholder communication and transparency.

Thanks to such deal making abilities, Burford turned an initial profit of $17.6M into a $31.1M profit (~76.7% increase) and increased ROIC from 254% to 448%. This occurred at the

[3] https://www.sec.gov/Archives/edgar/data/1585608/000104746917003695/a2232030zex-10_60.htm
[4] https://www.muddywatersresearch.com/research/bur/was-mw-wrong-about-napo-no/

expense of a slight reduction in IRR from 51% to 47%, from 2010 to 1H 2016. Burford did so by agreeing to wait to collect what it was owed and converting its entitlement which was an unsecured obligation of the client into a first lien mortgage that carried a very attractive rate. A brilliant move in our humble opinion.

In other words, Burford made *a lot more money* and sacrificed ~4 percentage points of IRR on the initial IRR of 51%. We bet that every hedge fund manager out there would take such an IRR reduction in order to gain a higher ROIC. While Muddy Waters correctly pointed out the decrease in the IRR, it neglected to mention a massive increase in profits of 76.7% (from $17.6M to $31.1M) and ROIC increase from 254% to 448% as a result. We find this omission a bit misleading and a bit too convenient.

Claim #3: Burford Does Not Reduce ROIC and IRR from *Investments* that It Acquired by Purchase Price It Paid for Acquired *Operating* Businesses

Muddy Waters argues that Burford does not allocate the purchase price of operating businesses to the cost basis of acquired investments. Let us explain what Muddy Waters means by that.

In the past, Burford completed few acquisitions of operating businesses because it wanted to bring a particular area of expertise / skillset in-house (e.g., asset recovery) or gain speed to market (e.g., acquisition of asset management business – Gerchen Kellner (GKC)). Muddy Waters asserted that (1) Burford acquired investments as part of those M&A deals and (2) returns (ROIC and IRR) on those investments should be reduced by allocating some purchase price against ROIC and IRR of such investments.

We respectfully disagree with Muddy Waters' viewpoint in two ways: conceptual and fact specific. Furthermore, examples that Muddy Waters provided to prove that Burford misrepresented IRRs on investments in questions are not persuasive. Burford pointed out multiple factual inaccuracies in Muddy Waters' examples. Management's position on the matter is fact based and well supported, and Muddy Waters has yet to challenge those corrections. In fact, a careful review of past disclosures demonstrates that Muddy Waters is mistaken.

For example, Burford previously disclosed that it *separately* acquired two small investments (~$4.3M) concurrently with the acquisition of the operating business of GKC[5]. We are satisfied with that, and we broadly feel that Muddy Waters has simply gotten this point wrong. More detail follows in the full write-up.

Claim #4: Burford Inappropriately Calculates ROIC of Partial Recoveries

We disagree with Muddy Waters' approach to critiquing this metric and believe that the cost allocation approach deployed by Burford is conceptually preferred and is an intellectually

[5] https://otp.investis.com/clients/uk/burford_capital/rns/regulatory-story.aspx?cid=1377&newsid=828798 – see FN 2.

honest method. That said, Burford provides *so much data in its detailed disclosures* that one can calculate ROIC any way they want, a practice for which Burford should be credited.

We diverge further from Muddy Waters' perspective with regard to some of its supporting evidence. Muddy Waters presented factually correct data about the *Akhmedov* case to support its assertions. However, many of these data points such as the length of prior divorce proceedings are *irrelevant to Burford at this point* because Burford was *never* involved in divorce proceedings. Their length, whatever it was, is a matter of the past and is irrelevant to Burford. Burford simply pursues a judgment issued *after* the divorce proceedings, which is an entirely different legal matter.

Other data points such as public information about Mr. Akhmedov's lawsuit against Burford are optically sensational and appear damning but lack relevant context. The actions outlined by Muddy Waters are, in fact, typical for high stakes litigation. Outcomes are too early to judge, and the high headline number does not mean much at this stage. Furthermore, *the judgment issued by an English court remains outstanding and valid and is enforceable*. We believe Muddy Waters has done the market a disservice by not providing the relevant context on this point.

Claim #5: Burford Delayed Recognizing a Trial Loss for Two Years

Muddy Waters relies on *Progas*, an international investment arbitration case that Burford's client lost to demonstrate that Burford delays recognition of its losses.

Here is an example in which Muddy Waters needs to mention that Burford also delayed recognition of sizable wins *under the very same policy*. In our opinion, *Progas* and *Teinver* cases show that Burford *consistently* applies the same reporting policy. In *Progas* their policy resulted in a "delay" of recognition of a loss. In *Teinver* the same policy resulted in a "delay" in recognition of a massive win with 700%+ ROIC. Again, we find the claims misleading and questionably selective.

Claim #6: Burford Keeps Trial Loses Out of the "Concluded Investment" Category

Muddy Waters provides three examples of how Burford purportedly kept trial losses out of the "concluded investments" category.

After digging into all three examples provided by Muddy Waters, we do not see any evidence proving that Burford keeps trial losses out of the "Concluded Investment" category. None of Muddy Waters' examples proves this claim. For example, in *RCR Tomilson*, a securities class action in Australia, Muddy Waters asserted that prospects to collect any recoveries are remote at best.

We see facts differently. As recently as mid-August 2019 three law firms and three litigation funders were fighting to represent the plaintiffs. Burford and IMF Bentham would be funding the litigation together. The litigation has not even *"really"* started as the plaintiff's

counsel was just determined. We do not see why this case should be viewed as a "concluded investment".

In our view, Burford is consistently applying the set of policies that it told investors it would apply.

Claim #7: Burford Failed to Deduct Various Costs and Operating Expenses Against Recoveries

Muddy Waters asserted that shareholders are overpaying management because of an extraordinary high expense ratio of ~9%. To provide more context, Muddy Waters gets to ~9% expense ratio by removing all fair market value gains from the capital base and gets to the *Adjusted* Capital Base of ~$880M. Given that Muddy Waters has not proven that fair value adjustments are inappropriate, *we do not see any reason why one should rely on the Adjusted Capital Base*.

We see an expense ratio of ~4.25% and the entire "expense ratio" is lower than what a hedge fund with a 2% and 20% fee structure would charge given the returns Burford has been delivering. We believe these expenses to be reasonable based on the firm's exceptional creation of value over the past decade.

A good conceptual parallel is a hedge fund manager that charges a management fee and an incentive fee based on the amounts invested by limited partners *and* unrealized capital gains when investments with such gains are carried into the next year. In our view, investable assets are $2B+ (excluding 3rd party hedge funds where Burford acts as a general partner). As a result, we arrive to ~4.25% expense ratio.

Claim #8: Burford's ROIC Is Highly Reliant On a Few Outlier Cases[6]

We find this line of argument to be problematic on multiple levels. To start, on what basis is it sensible to discount Burford's biggest wins? Burford's business is about both protecting downside and capturing the occasional home run outcome. Sounds familiar, does it not?

The return streams and attribution of highly successful fund managers are not normally distributed – limited number of ideas tend to generate the vast majority of a fund's alpha. What would venture capital *as an asset class* look like if you applied the same treatment? Perhaps more telling: What would Muddy Waters' track record look like if you wipe out its biggest and best calls? Ironically Burford is still a highly profitable enterprise even if one removes its biggest wins measured by ROIC (and even more so when adjusting for errors in Muddy Waters' adjusted ROIC).

[6] This claim was not numbered by Muddy Waters. We will assign "number 8" to it as a matter of convenience.

Muddy Waters claims that ROIC without those "outlier" cases is 19%. In reality, it is 30%+. Muddy Waters mismatched IFRS reporting for *all* cases and non-IRFS investment data that covers *only core litigation* matters and does not cover complex litigation strategies that have substantially lower ROIC (~15% to ~20%) but strong IRR.

Finally, such analysis ignores the fact that such high ROIC comes together with longer duration and while IRRs are still higher than portfolio averages, the difference is a lot less dramatic. For example, *Teinver* was an unquestionable success and generated 722% ROIC but "only" 39% IRR. Over the same period of time Burford could have invested in several cases with lower ROIC but still an attractive IRR of ~30%.

Claim #9: Burford Had Ulterior Motives for GKC Acquisition Such as to Consolidate Assets In Order to Make Debt Load Look Less Ominous[7]

> *"We cannot help but feel that BUR had ulterior motives for this acquisition, such as to consolidate assets in order to make its debt load look less ominous, or to ensure it is valued as an operating business, rather than as a closed-end fund. BUR has issued $646.9 million of retail bonds, and yet has no credit ratings."*
>
> *-Muddy Waters*

The core problem with this argument is that GCK as any asset manager was an asset light business. As a result, the lion's share of the purchase price ($133M or ~80%) was allocated to goodwill.

We do not see how making an acquisition and recording a goodwill of $133M helped Burford boost its balance sheet.

We believe that the acquisition had a genuine and clearly articulated business purpose of entering the asset management business. It was a buy vs. build decision. The rapid growth of Burford's asset management division shows that it was, in fact, a very good M&A transaction.

Claim #10: Burford Is "Arguably Insolvent"[8]

This is a punchline of Muddy Waters' report:

> *"BUR is arguably insolvent. If subtracting BUR's funded debt balance of $637.8 million from the adjusted capital base, there is only a $243.1 million cushion. However, BUR has future balance sheet litigation commitments of $708.2 million. Historically, approximately 85% of these commitments are eventually deployed, implying that BUR has an off balance sheet liability of $602.0 million. When looking at BUR's solvency*

[7] This claim was not numbered by Muddy Waters. We will assign "number 9" to it as a matter of convenience. See page 4 of Muddy Waters 2019-08-07 Report.
[8] This claim was not numbered by Muddy Waters. We will assign "number 10" to it as a matter of convenience. See page 24 – 25 of Muddy Waters 2019-08-07 Report.

through this methodology, BUR has negative equity of -$358.9 million relative to the adjusted capital base."

-Muddy Waters

After twenty-three pages of one-sided interpretations, Muddy Waters believes it has finally found a black cat in a dark room – the "insolvency" of Burford.

How did Muddy Waters get to that conclusion? Muddy Waters did the following: (1) reduced book equity by all fair value gains, (2) assumed that all bonds become payable overnight, (3) assumed that funding commitments come due, and (4) gave Burford zero chance to generate any cash inflows from investments that may conclude over coming months.

We find this approach *sensational and incorrect*.

First, we already discussed why removing all fair value gains is incorrect.

Second, assuming that all debt (~$637.8M) becomes payable overnight is a product of strong imagination given ***Burford's thoughtfully created maturity ladder*** over the next seven years. Why these bonds would become immediately payable is quite unclear and we wish Muddy Waters had explained the rationale in their report.

Third, Muddy Waters' analysis assumes ***cash outflows beyond imagination*** and ***ignores any potential cash inflows***. For example, some of the current investments are very likely to come to conclusion over the coming months and bring cash to Burford.

Fourth, Muddy Waters ignores Burford's ability to sell some of its investments.

Fifth, Muddy Waters ignores Burford's ability to syndicate its own deals by partnering up with other litigation finance providers instead of funding its solo. We want to be crystal clear: this is a matter of last resort and we do not envision it happening.

Not surprisingly, ***we strongly disagree with Muddy Waters' solvency punchline***. ***There is no cat in the dark room, and with respect to Burford, we feel there is no reason to question its financial durability***.

* * *

In Summary, We Do Not Find Muddy Waters' Claims Persuasive, Let Alone Conclusive of Improper Behavior

We do not find Muddy Waters' claims persuasive, let alone conclusive of Burford's improper behavior. Muddy Waters provided many correct facts, but often selectively so. Their interpretations of these facts are, however, unusual and appear to be colored by a strong bias in selection. We find the rigor of their work on the name to be uncharacteristically short of their generally high standard. To put it simply, we disagree with Muddy Waters.

Ben Graham famously said that in the short run, the market is a voting machine, and the market definitely voted in the weeks after Muddy Waters published its report. But in the long run, the market it is a weighing machine. We strongly believe that the market will weigh Burford properly in the long run.

Below you can read the full analysis.

How to Access Full Rebuttal of Muddy Waters Report

You can download the full, ~70 page rebuttal report "*Burford Capital: Muddy Waters Dreams of a Black Cat That Just Is Not There*" at http://caro-kann-capital.com/#research

Get in Touch

If you want to discuss Burford Capital, please get in touch with us. You may reach the author of this report at artem.fokin@caro-kann-capital.com or you can visit our website at www.caro-kann-capital.com. Thank you for reading.

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I. Background

We have tremendous respect for short sellers who expose frauds and corporate wrongdoings. They do hard investigative work that many others prefer not to do. We are fortunate to count some of these short sellers among our friends. Muddy Waters and Carson Block stand out among this group of smart investors. The firm has a very impressive track record of deconstructing complex schemes and exposing them to the investment world.

Muddy Waters' prior track record does not mean that they are always right. Burford is one such example. We believe Muddy Waters is mistaken in their conclusions about Burford Capital's reporting and accounting practices, as well as its financial position.

We, Caro-Kann Capital, are arguably the most publicly recognizable long investor in Burford, having published our long thesis on the stock in December 2018. Our Burford investment thesis was selected as the winner in "Top Stocks for 2019" by SumZero[9]. The report was shared extensively by SumZero and others earlier this year. We were also invited by the Manual of Ideas[10] to present the investment thesis at their Best Ideas 2019 conference. Anecdotally, many fund managers reached out to us on Burford after reading or watching our investment thesis.

You can download the original investment memorandum submitted to SumZero here[11] and MOI Global presentation here[12]. You can also watch a video of our presentation here[13].

We are long Burford shares. It is a business that is defining and leading a new industry – litigation finance. It is a company that many smaller competitors aspire to emulate. It has grown many times over in the past 10 years and has a long growth runway ahead of it. It generates a ~30% ROE and yet trades today at less than 6x earnings (LTM). Such a valuation typically implies a cigar-butt type situation; yet Burford's earnings are growing while the balance sheet is not over levered (in fact, it is probably under levered).

Burford used to trade at double its current valuation just a month ago. However, a critical short thesis published by Muddy Waters made ~$2B of market cap disappear into thin air. This report serves a purpose to share an alternative view on Burford.

[9] https://sumzero.com/headlines/telecom/SATS/444-the-top-stocks-for-2019
[10] https://moiglobal.com/artem-fokin-201901/
[11] http://caro-kann-capital.com/#research
[12] http://caro-kann-capital.com/#conferences
[13] http://caro-kann-capital.com/#videos

II. Claim #1: Burford Categorized a Loss as an Investment with Significant Return and Might Have Acted in Concert with Its Own Largest Shareholder to Deceive

1. Essence of Muddy Waters' Claims

The strongest card in the Muddy Waters hand stems from claims that (1) Burford reported a profitable investment before the resolution of a case; (2) Burford's client, Napo Pharmaceuticals, subsequently *lost* the case that Burford funded, and (3) Burford and its largest shareholder, Invesco, who also happened to be an investor in Napo purportedly colluded to design a highly complex corporate restructuring to enable Burford to keep reporting its profitable investment. This was meant to be Muddy Waters' Mike Tyson uppercut, a good night and good luck to the Longs. Given the market's knee-jerk reaction to the report, it seemingly was.

2. Caro-Kann Capital's Position

But there is no smoking gun. Caro-Kann believes this point to be a *phantom punch*. The more facts and explanations Muddy Waters has demanded on this matter, the more disclosures Burford has provided. Burford has come out better looking as a result.

Both Muddy Waters and Burford wrote numerous pages about *Napo*, its facts, interpretations, accounting, and non-IRFS reporting. Retelling what has already been written is not a productive use of anyone's time. We encourage everybody to read the following on the subject of *Napo*:

- ✓ 2019-08-07 Muddy Waters Report[14]
- ✓ 2019-08-08 Burford's initial response[15]
- ✓ 2019-08-26 Muddy Waters follow up[16]
- ✓ 2019-09-02 Burford follow up[17]

Instead of repeating what was already written, we will share three important conclusions.

3. Burford's IFRS and Non-IFRS Accounting with Respect to *Napo* Was Conservative

While Muddy Waters asserted that Burford inappropriately recorded *Napo* matter as concluded and reported high ROIC on the matter presumably in its attempt to impress investors with its track record, it turned out that Burford's reporting was in fact *conservative*. Here are a few illustrations:

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[14] https://www.muddywatersresearch.com/research/bur/mw-is-short/

[15] https://www.burfordcapital.com/wp-content/uploads/2019/08/2019.08.08-Burford-Capital-Response-to-Muddy-Waters-FINAL-1.pdf

[16] https://www.muddywatersresearch.com/research/bur/was-mw-wrong-about-napo-no/

[17] https://www.burfordcapital.com/wp-content/uploads/2019/09/2019.09.02-Burford-Capital-Chronology-of-Napo-Investment-Website-FINAL.pdf

- ✓ At the end of 2013 when Burford's entitlement became unconditional, Burford applied a discount of ~50% to the receivable on the balance sheet and the concluded case value in its non-IFRS investment data. To be more specific, the receivable and the concluded case investment were accounted at ~$15.75M while Burford was *legally* entitled to ~$30M.
- ✓ At the end of 2015 Burford did *not* include the effect of the accruing interest at a rate of 18%.
- ✓ At the end of 2016 Burford carried the Napo investment at ~$21.3M while it was legally entitled to ~$51.1M.

Why did Burford apply such a conservative approach? Burford did so because it was not certain about collectability of its entitlement. This shows thoughtfulness and conservatism as opposed to aggressiveness to impress investors with returns.

4. Burford's Explanation of Events Is Well Supported by Prior SEC and Court Filings

Burford's explanation of events is supported several public documents, including:

- ✓ Settlement Agreement between Glenmark and Napo[18]
- ✓ Petition to Confirm Arbitration Award filed by Glenmark with United States District Court for the District of New Jersey – this is the very court document that Muddy Waters included into 2019-08-26 Report "Burford: Was MW Wrong About Napo?"[19] as an exhibit.

For example, this was the timeline of important events in *Glenmark* – the case that led Burford to recognize *Napo* as a concluded investment.

- ✓ August 21, 2012 – Interim Award is issued
- ✓ September 27, 2013 – Partial Final Award is issued
- ✓ December 2013 – Glenmark and Napo entered into the Settlement Agreement[20]
- ✓ January 10, 2014 – Final Award was issued.

5. Did Nantucket (Burford's Affiliate) and Invesco Share the Same Address?

Muddy Waters also *correctly* noted that Nantucket's address of record is listed as that of Invesco's global headquarters on Jaguar Health's 2017 proxy statement. Nantucket is Burford's affiliate that held Jaguar Health shares (Jaguar is Napo's corporate successor). Muddy Waters did not comment on implications of this, but it would not be unreasonable to think that *at least some readers* (and probably a lot more than some) viewed this "cozy address sharing" as

[18] https://www.sec.gov/Archives/edgar/data/1585608/000104746917003695/a2232030zex-10_60.htm
[19] https://www.muddywatersresearch.com/research/bur/was-mw-wrong-about-napo-no/
[20] Napo signed the Settlement Agreement on December 9, 2013, and Glenmark signed it on December 29, 2013.

circumstantial evidence of concerted efforts by Invesco and Burford to orchestrate the entire transaction. The reality appears a lot duller:

- ✓ The first Form 13G filed on August, 2017[21] listed address in *Guernsey*.
- ✓ Form 13D filed on February 12, 2018[22] listed address in *Guernsey*.
- ✓ Jaguar Health 2017 Proxy Statement dated April 24, 2018[23] listed Invesco's address in *the U.S.* as Nantucket address indeed.
- ✓ Form 13G filed on April 27, 2018[24] listed address in *Guernsey*.
- ✓ Form 13G October 24, 2018[25] listed address in *Guernsey*.
- ✓ Jaguar Health Proxy Statement dated January 24, 2019[26] listed address in *Guernsey*.

Below we provide SEC filings that support this analysis.

Nantucket filed its very first filing with respect to its ownership in Jaguar health on August 9, 2017. It was Form 13G[27]. Here is how Nantucket's address was reported:

CUSIP No. 47008L106 **13G** **Page 4 of 8 Pages**

Item 1(a). **NAME OF ISSUER**
The name of the issuer is Jaguar Health, Inc. (the "Company").

Item 1(b). **ADDRESS OF ISSUER'S PRINCIPAL EXECUTIVE OFFICES**
The Company's principal executive offices are located at 201 Mission Street, Suite 2375, San Francisco, California 94105.

Item 2(a). **NAME OF PERSON FILING**
This statement is filed by:

(i) Nantucket Investments Limited, a company organized under the laws of Guernsey ("Nantucket"), with respect to the shares of Common Stock (as defined in Item 2(d) below) directly held by it; and

(ii) Burford Capital Limited, a company organized under the laws of Guernsey and publicly traded on the London Stock Exchange ("BCL"), with respect to the shares of Common Stock directly held by Nantucket.

The foregoing persons are hereinafter sometimes collectively referred to as the "Reporting Persons." Any disclosures herein with respect to persons other than the Reporting Persons are made on information and belief after making inquiry to the appropriate party.

The filing of this statement should not be construed in and of itself as an admission by any Reporting Person as to beneficial ownership of the securities reported herein.

Burford Capital LLC, a Delaware limited liability company, is the investment adviser to Nantucket. Burford Capital Holdings (UK) Limited, a company organized under the laws of England and Wales, is the sole owner of Burford Capital LLC and is majority owned by BCL. Each of Nantucket, BCL, Burford Capital LLC and Burford Capital Holdings (UK) Limited disclaim beneficial ownership of the securities reported herein.

Item 2(b). **ADDRESS OF PRINCIPAL BUSINESS OFFICE OR, IF NONE, RESIDENCE**
The address of the business office of each of Nantucket and BCL is PO Box 282, Regency Court, Glategny Esplanade, St. Peter Port, Guernsey GY1 3RH.

Item 2(c). **CITIZENSHIP**
Nantucket and BCL are Guernsey companies.

[21] https://www.sec.gov/Archives/edgar/data/1585608/000090266417003230/p17-1687sc13g.htm
[22] https://www.sec.gov/Archives/edgar/data/1585608/000090266418000893/p18-0506sc13d.htm
[23] https://www.sec.gov/Archives/edgar/data/1585608/000104746918003122/a2235346zdef14a.htm
[24] https://www.sec.gov/Archives/edgar/data/1585608/000090266418002053/p18-1008sc13g.htm
[25] https://www.sec.gov/Archives/edgar/data/1585608/000090266418003808/p18-1940sc13ga.htm
[26] https://www.sec.gov/Archives/edgar/data/1585608/000104746919000176/a2237551zdef14a.htm
[27] https://www.sec.gov/Archives/edgar/data/1585608/000090266417003230/p17-1687sc13g.htm

About six months later on February 12, 2018 Nantucket filed Form 13D[28] and the address was also a Guernsey address:

Item 2. **IDENTITY AND BACKGROUND**

(a) This statement is filed by:

(i) Nantucket Investments Limited, a company organized under the laws of Guernsey ("Nantucket"), with respect to the Shares directly held by it and the Shares issuable upon conversion of the Non-Voting Shares (as defined in Item 4 below) held by it; and

(ii) Burford Capital Limited, a company organized under the laws of Guernsey and traded on the AIM Market of the London Stock Exchange ("BCL"), with respect to the Shares directly held by Nantucket and the Shares issuable upon conversion of the Non-Voting Shares held by Nantucket.

The foregoing persons are hereinafter sometimes collectively referred to as the "Reporting Persons." Any disclosures herein with respect to persons other than the Reporting Persons are made on information and belief after making inquiry to the appropriate party.

The filing of this statement should not be construed in and of itself as an admission by any Reporting Person as to beneficial ownership of the securities reported herein.

Nantucket is indirectly owned by BCL. Burford Capital LLC, a Delaware limited liability company, provides services to Nantucket, its wholly owned subsidiary. Burford Capital Holdings (UK) Limited, a company organized under the laws of England and Wales, is the sole owner of Burford Capital LLC and is majority owned by BCL. Each of Nantucket, BCL, Burford Capital LLC and Burford Capital Holdings (UK) Limited disclaims beneficial ownership of the securities reported herein.

(b) The principal business address of each of Nantucket and BCL is PO Box 282, Regency Court, Glategny Esplanade, St. Peter Port, Guernsey GY1 3RH.

(c) The principal business of Nantucket is to hold and monetize investments. The principal business of BCL is finance for the legal industry.

On April 24, 2018 Jaguar Health filed its Proxy[29] and this is Nantucket's address was indeed reported as the same as Invesco's:

Name and address of beneficial owner	Voting Common Stock		Series A Convertible Participating Preferred Stock	
	Number of Shares Beneficially Owned	Percentage of Shares Beneficially Owned	Number of Shares Beneficially Owned	Percentage of Shares Beneficially Owned
5% Stockholders:				
Sagard Capital Partners, L.P.(1)	32,082,626	19.99%	5,524,926	100%
Invesco Ltd.	26,885,838	20.94%	—	—
Nantucket Investments Limited(2)	23,634,341	16.06%	—	—
Entities affiliated with Kingdon Capital Management L.L.C.(3)	12,846,405	9.09%	—	—
Named executive officers and directors:				
Lisa A. Conte(4)	1,797,332	*	—	—
Steven R. King, Ph.D(5)	648,970	*	—	—
Karen S. Wright(6)	413,645	*	—	—
James J. Bochnowski(7)	1,104,760	*	—	—
Jeffery C. Johnson	—	—	—	—
Folkert W. Kamphuis(8)	342,850	*	—	—
John Micek III(9)	236,382	*	—	—
Jiahao Qiu(10)	65,395	*	—	—
Jonathan B. Siegel	—	—	—	—
Zhi Yang, Ph.D.(11)	1,627,831	*	—	—
All current executive officers and directors as a group (10 persons)(12)	6,237,165	4.70%	—	—

* Less than 1%.

(1) Represents 32,082,626 shares of Common Stock issuable upon conversion of shares of Preferred Stock that are convertible at any time, after giving effect to the 19.99% Limitation described elsewhere in this proxy statement. If Proposal 2 is approved and the 19.99% Limitation is removed, an additional 17,641,704 additional shares of Common Stock would be issuable upon conversion of shares of Preferred Stock, resulting in an aggregate of 49,724,330 shares of Common Stock issuable upon conversion of shares of Preferred Stock, which shares would be entitled to 47,540,060 votes as further discussed elsewhere in this proxy statement. The address for Sagard Capital Partners, L.P. is 280 Park Avenue, 3rd Floor West, New York, NY 10017.

(2) Represents (i) 4,884,245 shares of Common Stock and (ii) 18,750,096 shares of Common Stock issuable upon conversion of shares of non-voting common stock that are convertible at any time. The address for the reporting person is 1555 Peachtree Street NE, Suite 1800, Atlanta GA 30309.

(3) Represents (i) 1,291,986 shares of Common Stock, (ii) 566,668 shares of Common Stock issuable upon exercise of warrants, and (iii) 10,987,751 shares of Common Stock issuable upon conversion of the Kingdon Notes owned by Kingdon Capital Management, L.L.C. that are convertible or may become convertible within 60 days of April 23, 2018, excluding any accrued and unpaid interest on the Kingdon Notes. The address for the reporting person is 152 West 57th Street, 50th Floor, New York, NY 10019.

However, just three days later, on April 27, 2018, Nantucket filed Form 13G[30] and the address was still a Guernsey address:

[28] https://www.sec.gov/Archives/edgar/data/1585608/000090266418000893/p18-0506sc13d.htm
[29] https://www.sec.gov/Archives/edgar/data/1585608/000104746918003122/a2235346zdef14a.htm
[30] https://www.sec.gov/Archives/edgar/data/1585608/000090266418002053/p18-1008sc13g.htm

Item 1(a). **NAME OF ISSUER**
The name of the issuer is Jaguar Health, Inc. (the "Company").

Item 1(b). **ADDRESS OF ISSUER'S PRINCIPAL EXECUTIVE OFFICES**
The Company's principal executive offices are located at 201 Mission Street, Suite 2375, San Francisco, California 94105.

Item 2(a). **NAME OF PERSON FILING**
This statement is filed by:

(i) Nantucket Investments Limited, a company organized under the laws of Guernsey ("Nantucket"), with respect to the shares of Common Stock (as defined in Item 2(d) below) directly held by it; and

(ii) Burford Capital Limited, a company organized under the laws of Guernsey and publicly traded on the London Stock Exchange ("BCL"), with respect to the shares of Common Stock directly held by Nantucket.

The foregoing persons are hereinafter sometimes collectively referred to as the "Reporting Persons." Any disclosures herein with respect to persons other than the Reporting Persons are made on information and belief after making inquiry to the appropriate party.

The filing of this statement should not be construed in and of itself as an admission by any Reporting Person as to beneficial ownership of the securities reported herein.

Nantucket is indirectly owned by BCL. Burford Capital LLC, a Delaware limited liability company, provides services to Nantucket, its wholly owned subsidiary. Burford Capital Holdings (UK) Limited, a company organized under the laws of England and Wales, is the sole owner of Burford Capital LLC and is majority owned by BCL. Each of Nantucket, BCL, Burford Capital LLC and Burford Capital Holdings (UK) Limited disclaims beneficial ownership of the securities reported herein.

Item 2(b). **ADDRESS OF PRINCIPAL BUSINESS OFFICE OR, IF NONE, RESIDENCE**
The address of the business office of each of Nantucket and BCL is PO Box 282, Regency Court, Glategny Esplanade, St. Peter Port, Guernsey GY1 3RH.

Item 2(c). **CITIZENSHIP**
Nantucket and BCL are Guernsey companies.

Another Form 13G with a Guernsey address was filed on October 24, 2018[31]

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Item 1(a). **NAME OF ISSUER**
The name of the issuer is Jaguar Health, Inc. (the "Company").

Item 1(b). **ADDRESS OF ISSUER'S PRINCIPAL EXECUTIVE OFFICES**
The Company's principal executive offices are located at 201 Mission Street, Suite 2375, San Francisco, California 94105.

Item 2(a). **NAME OF PERSON FILING**
This statement is filed by:

(i) Nantucket Investments Limited, a company organized under the laws of Guernsey ("Nantucket"), with respect to the shares of Common Stock (as defined in Item 2(d) below) directly held by it; and

(ii) Burford Capital Limited, a company organized under the laws of Guernsey and publicly traded on the London Stock Exchange ("BCL"), with respect to the shares of Common Stock directly held by Nantucket.

The foregoing persons are hereinafter sometimes collectively referred to as the "Reporting Persons." Any disclosures herein with respect to persons other than the Reporting Persons are made on information and belief after making inquiry to the appropriate party.

The filing of this statement should not be construed in and of itself as an admission by any Reporting Person as to beneficial ownership of the securities reported herein.

Nantucket is indirectly owned by BCL. Burford Capital LLC, a Delaware limited liability company, provides services to Nantucket, its wholly owned subsidiary. Burford Capital Holdings (UK) Limited, a company organized under the laws of England and Wales, is the sole owner of Burford Capital LLC and is majority owned by BCL. Each of Nantucket, BCL, Burford Capital LLC and Burford Capital Holdings (UK) Limited disclaims beneficial ownership of the securities reported herein.

Item 2(b). **ADDRESS OF PRINCIPAL BUSINESS OFFICE OR, IF NONE, RESIDENCE**
The address of the business office of each of Nantucket and BCL is PO Box 282, Regency Court, Glategny Esplanade, St. Peter Port, Guernsey GY1 3RH.

Item 2(c). **CITIZENSHIP**
Nantucket and BCL are Guernsey companies.

Finally, on January 23, 2019 Jaguar Health filed its Proxy[32] and Nantucket's address was in Guernsey.

[31] https://www.sec.gov/Archives/edgar/data/1585608/000090266418003808/p18-1940sc13ga.htm
[32] https://www.sec.gov/Archives/edgar/data/1585608/000104746919000176/a2237551zdef14a.htm

Name and address of beneficial owner	Voting Common Stock		Stock	
	Number of Shares Beneficially Owned	Percentage of Shares Beneficially Owned	Number of Shares Beneficially Owned	Percentage of Shares Beneficially Owned
5% Stockholders:				
Sagard Capital Partners, L.P.(1)	3,314,956	10.13%	5,524,926	100%
Invesco Ltd.(2)	1,803,524	6.27%	—	—
Bryan Ezralow(3)	1,666,667	5.79%	—	—
Nantucket Investments Limited(4)	1,575,621	5.47%	—	—
Knight Therapeutics, Inc.(5)	1,500,000	5.21%	—	—
Sabby Healthcare Master Fund, Ltd.(6)	1,311,580	4.56%	—	—
Named executive officers and directors:				
Lisa A. Conte(7)	306,012	1.16%	—	—
Steven R. King, Ph.D(8)	107,436	*	—	—
Karen S. Wright(9)	69,383	*	—	—
James J. Bochnowski(10)	190,265	*	—	—
Jeffery C. Johnson(11)	30,089	*	—	—
John Micek III(12)	64,129	*	—	—
Jiahao Qiu(13)	6,716	*	—	—
Jonathan B. Siegel(14)	70,089	*	—	—
Greg Divis(15)	21,351	*	—	—
Murray David MacNaughtan(16)	21,351	*	—	—
All current executive officers and directors as a group (10 persons)(17)	886,820	3.38%	—	—

* Less than 1%.

(1) Represents 3,314,956 shares of Common Stock issuable upon conversion of shares of Preferred Stock that are convertible at any time, which shares would be entitled to 3,169,338 votes as further discussed elsewhere in this Proxy Statement. The address for Sagard Capital Partners, L.P. is 280 Park Avenue, 3rd Floor West, New York, NY 10017.

(2) As reported on Form 13G filed on November 13, 2018. The address for the reporting person is 1555 Peachtree Street NE, Suite 1800, Atlanta GA 30309.

(3) As reported on Form 13G filed on October 15, 2018. Bryan Ezralow beneficially owns 1,666,667 shares of Common Stock of which 1,250,000 shares are held by the Bryan Ezralow 1994 Trust u/t/d December 22, 1994 (the "1994 Trust"), of which Mr. Ezralow is the sole trustee, and 416,667 shares are held by EZ MM&B Holdings, LLC ("EZ MM&B"), where Mr. Ezralow as the sole trustee of one of the trusts that is a manager of EZ MM&B, and as a co-trustee and manager, respectively, of the two trusts and limited liability company that comprise the managing members of one of the other managers of EZ MM&B, shares voting and dispositive power over such shares, and thus, may be deemed to beneficially own such shares. The address for the reporting person is 23622 Calabasas Road, Suite 200 Calabasas, CA 91302.

(4) Represents 1,575,621 shares of Common Stock issuable upon conversion of shares non-voting common stock owned by Nantucket Investment Ltd. The address for the reporting person is PO Box 282, Regency Court, Glategny Esplanade, St. Peter Port, Guernsey GY1 3RH.

(5) As reported on Form 13G filed on October 17, 2018. The address for the reporting person is 3400 Boulevard De Maisonneuve West, Suite 1055, Montreal, Quebec Canada H3Z 3B8.

Muddy Waters is right that Jaguar Health 2017 Proxy Statement listed Invesco's address as Nantucket address. However, *prior and subsequent* filings referenced above indicate that the address in 2017 Proxy Statement was most likely a ***trivial clerical error***. We believe it would have been helpful if Muddy Waters had pointed out that five out of six filings list a Guernsey address while only one filing lists a U.S. address. Not mentioning those five filings appears a bit too convenient.

6. Conclusion

We intentionally have not covered all aspects of Napo so that we do not repeat what has been written before. We encourage everybody to refer to the sources that we have referenced.

III. Claim #2: Deemed Recoveries Lead to Increased IRRs. *Desert Ridge* Is Evidence

1. Essence of Muddy Water's Claim about Desert Ridge

In Muddy Water's opinion, the *Desert Ridge* case demonstrates that "BUR has misleadingly boosted its IRR numbers by deeming amounts recovered when in reality they were years away from collection." This is because Burford's initially reported IRR of 51% decreased to 47% in a few years.

2. Caro-Kann Capital's Position

We have the opposite view. *Desert Ridge* shows:

1. Tremendous transparency about Burford's key performance metrics as Burford disclosed ROIC and IRR *every single year* while recoveries were pending and kept investors updated on this issue.
2. Clear communications by Burford's management as they explained *why* it chose to delay recoveries.
3. Burford's substantial deal making abilities as Burford turned an initial profit of $17.6M into a $31.1M profit (~76.7% increase) and increased ROIC from 254% to 448%. This occurred at the expense of a slight reduction in IRR from 51% to 47%, from 2010 to 1H 2016. In other words, Burford made a lot more money and sacrificed ~4 percentage point of IRR on the initial IRR of 51%. We bet that every hedge fund manager out there would take that IRR reduction on their portfolio in order to gain a higher ROIC.
4. Muddy Waters did not mention increases in total recoveries, total profit, and ROIC in its report and, therefore, did not present all relevant data.

Given that our conclusions and Muddy Waters' conclusions are almost the opposite, let's recap the facts and circumstances of the *Desert Ridge* case first. To save space, we will do so in a somewhat simplified fashion.

3. Desert Ridge: Recap of Facts of the Matter

A real estate developer sought litigation funding from Burford to protect its rights and interests. Such funding was provided by Burford's affiliate Ganymede, a Guernsey corporation. A top U.S. law firm, Simpson Thacher, represented the real estate developer. The plaintiff's lawyer was Simpson Thacher partner Barry Ostrager[33], a highly regarded litigator who in June 2015 became a justice in New York State[34].

[33] http://www.abajournal.com/news/article/top_law_firms_turn_to_litigation_finance_companies_to_fund_suits/
[34] https://www.nycourts.gov/courts/comdiv/ny/newyork_bio_ostrager.shtml

Burford's client won the case in 2010. The litigation risk *was removed*, and Burford *appropriately started treating this case as* concluded. This is critical for anybody who is following Burford (as well as other litigation finance companies) to understand clearly and unequivocally: once the litigation risk is gone, Burford treats the case as concluded.

4. Why Burford Capital Did Not Receive Cash Recovery Right Away

After the case was adjudicated, Burford's client agreed to a settlement with a defendant under which the client received a piece of valuable real estate as opposed to cash. It is important to keep in mind that these decisions are the domain of the client and not the litigation funder. However, the client still owed money to Burford and … the client did not have the money. By 2012 Burford received some money back (~$4M was received while the invested amount was $7M). More was owed to Burford. In 2012 Burford and the client agreed to convert an unsecured debt to a first mortgage on the recovered property. Thus, Burford's position as a creditor *improved substantially through skillful negotiation*: Burford put itself ahead of all other creditors.

Could Burford collect the money back in 2010 when the matter was resolved? The answer is almost certainly "yes". Burford had a legally enforceable right to collect. Why did Burford not collect the money and instead agree to delay the collection? In our opinion, there were at least two reasons. First, Burford believed that it would be economically beneficial to delay the collection. Second, Burford probably thought that turning against its client and suing to collect the money would not enhance Burford's reputation in the eyes of potential clients. While the second reason is difficult to judge with certainly, as events unfolded, Burford's belief that it could make more money by waiting was ultimately proven correct.

5. How Burford Accounted for the Litigation Receivable

Burford's decision to delay collection created important accounting consequences. Burford recorded a receivable from its client and started carrying it on the balance sheet. Since the mortgage carried a high interest rate, Burford started recording interest income. At that time Burford also stopped applying the fair value accounting to the receivable.

One of the beautiful things about Burford is the amount of information Burford management discloses about its business and accounting practices. Burford laid out how a situation such as the Desert Ridge would be treated under IFRS in its Annual Report 2012:

> *"we should also note that once our entitlement in a matter is sufficiently definite, it moves to a receivable and we stop fair valuing it. The value at the time it moves to a receivable determines the amount we record as a realised gain, and any future incremental value (such as for interest running on an unpaid entitlement, which for us can sometimes be substantial) does not*

show up as incremental realised gain but rather as "interest and other income".

Source: Burford Capital 2012 Annual Report.

In 1H 2016 Burford sold its note to an unrelated buyer[35]. Burford received $32.8M in addition to prior interim payments of $5.3M, amounting to total cash receipts of $38.1M against a total investment of $7.4M, for a 415% return on invested capital and a 47% IRR.

6. What Exactly Is Muddy Waters' Criticism? IRR Has Decreased. Let's Dig into Why It Happened

These are the facts of Desert Ridge investment made by Burford. Muddy Waters does not dispute those facts. ***Hence, what's wrong with the investment that generated 415% ROIC and 47% IRR over ~ 7.5 years?***

Muddy Water points out that IRR dropped from 51% to 47%. This is unquestionably correct. In fact, Burford has been diligently updating the ROIC and IRR of the Desert Ridge *every single year* when recoveries were pending.

Below I provide information about how ROIC and IRR of the Desert Ridge evolved over the years.

Here is the relevant part of 2013 Annual Report performance table[36]:

Concluded Investment Performance
($ million)

Vintage	Total investment	Total recovered	Return on invested capital	IRR
Investments made in 2009 – 100% complete	7.0	24.6	254%	51%
	2.0	2.0	(1%)	–
	2.5	–	–	–
2009 Performance to date	**11.5**	**26.6**	**133%**	**33%**

Here is 2014 Annual Report performance table:

[35] https://azbigmedia.com/real-estate/big-deals/heres-how-crown-realty-got-121m-worth-of-prime-land-for-54m/
[36] Please note that our ROIC calculation produces 251.4% ROIC as opposed to 254%. We attribute this to rounding.

Concluded investment performance

$ in millions	Total investment	Total recovered	Return on invested capital	IRR
Total investment recoveries to date	130.6	208.6	60%	24%
Concluded investments made in 2009 • 100% of vintage	7.0	31.7	355%	53%
	2.0	2.0	(1%)	(3%)
	2.5	0.0	(100%)	0%
2009 performance to date	11.5	33.7	193%	35%

Here is the relevant part of 2015 Annual Report performance table[37]:

Concluded investment performance

$ in millions	Total investment	Total recovered	Return on invested capital	IRR
Investments made in 2009 • concluded • 100% of vintage	7.0	35.4	408%	49%
	2.0	2.0	(1%)	(3%)
	2.5	0.0	(100%)	0%
2009 performance to date	11.5	37.4	225%	33%

Finally, here is the relevant part of Burford's Investment Data provided on their website.

INVESTMENT DEMOGRAPHICS						INVESTMENT SUMMARY										
Vintage Status Structure	ID	Type	Industry	Geography	New $ Out / In	% of Vintage	Original Commit	Prior Follow-on Commit	2019-H1 Follow-on Commit	Total Commit	Total Deploy	Total Recover	ROIC	IRR	Weighted Average Duration
Litigation Finance															
2009						100%	11.5			11.5	11.5	40.1			
Concluded Investments						100%	11.5			11.5	11.5	40.1			
Single															
	111057	Contract	Media & Entertainment	North America		18%	2.0			2.0	2.0	2.0	-1%	0%	0.6
	111061	Contract	Real Estate	North America		61%	7.0			7.0	7.0	38.1	448%	47%	5.0
	111068	Contract	Telecommunication Services	North America		21%	2.5			2.5	2.5	0.0	-100%	0%	0.7

It is 100% correct that Burford did not end up recovering the exact amount of money it said it would recover back in 2010 Annual Report. Back then Burford said it would get $24.6M of total recoveries (per its table of concluded investments). ***It ended up recovering … $38.1M!***

These ***numbers have been consistently presented by Burford over the years while recoveries were pending***. These numbers are indirectly confirmed by media coverage that we pointed out. Finally, these numbers are not disputed or challenged by Muddy Waters.

Muddy Waters only pointed out – correctly – that the IRR decreased from 51% to 47%. Muddy Waters *did not mention*, however, that the total amount recovered *increased* from $24.6M to $38.1M or by ~55%, the profit increased from $17.6M to $31.1M or by ~76.7%, and

[37] Please note that our ROIC calculation produces 444.3% ROIC as opposed to 448%. We attribute this to rounding.

ROIC increased from 254% to 448%. We find this omission a bit misleading and a bit too convenient.

7. How Burford Communicated Desert Ridge Results over the Years

It is critical to emphasize that Burford consistently disclosed these numbers and never attempted to conceal them. The discerning reader of Burford reports would have spotted the changing recoveries number in this case *easily* and could have matched those changing numbers with a case that Burford generally described as "Arizona real estate case" in its filings. Using $7M of invested capital, one would match those quite easily.

To put this claim to rest, below we provide quotes from Burford's writings relevant to Desert Ridge case.

Burford 2011 Annual Report

> *"This year, Burford has had a very good year given its young age. However, one of our profitable cases has not yet produced cash – because we believe we will ultimately fare better by waiting for the US real estate market to recover further than by forcing monetisation today."*

Burford 2012 Annual Report

> *"In addition to the foregoing matters, our long-running saga concerning the large 2010 Arizona real estate victory that has been previously reported took a major step further forward. As we have reported previously, we have already received $4 million in cash against our $7 million investment in this matter, but the real money was in our entitlement to a portion of the proceeds from the sale of the underlying land. In 2012, after significant negotiations and substantial effort, we succeeded in converting that inchoate entitlement into an interest bearing first mortgage. The mortgage has a face value of $51 million if not paid until its maturity in 2016 and includes a high rate of interest (one tranche is at 30% and another at 16%). If prepaid, for example, at 30 June 2013, the amount due under the mortgage would be $18.4 million. This matter in total under any scenario of repayment will have produced very high returns for Burford; we will report precise returns once the mortgage is paid."*

Burford 2016 Interim Report

"Of particular note for longstanding Burford shareholders, part of our cash generation this period was the full payment of our receivable from the Arizona real estate matter – indeed, we ended up recovering more than our receivable balance and thus also generated a further $2.8 million gain in the period on this investment. We have reported on this matter from time to time since its win at trial in 2010, and it is a good illustration of why a successful litigation finance business needs not only strong litigation talent but also deep deal and financial skills to maximise returns.

To recap the history of this matter, one of our earliest investments was in support of a leading trial team at a major US law firm, Simpson Thacher & Bartlett, which was representing a real estate developer in a dispute over a commercial development in Arizona. The case won following a jury trial and received a substantial damages award – much more than the underlying real estate was worth following the collapse of the Arizona real estate market in 2008–2009. Ultimately, the case settled post-trial by the plaintiff – Burford's client – taking a significant land interest but no cash with which to pay us. At that point, we could have elected to force the sale of the land, which certainly would have been the fastest path to cash for us, but we did not believe that was the value-maximising approach – and it certainly would not have been in our client's best interests. Instead, we agreed to restructure our investment and allow the client to wait for a recovery in the real estate market.

Now, after years of perseverance, we have concluded the investment. We received $32.8 million in the current period in addition to prior interim payments of $5.3 million, amounting to total cash receipts of $38.1 million against a total investment of $7.4 million, for a 415% return on invested capital and a 47% IRR. Had we been structured as a limited life fund or had we lacked the scale and deal skills to let the matter run its course, we would likely not have been prepared to forestall and would not have optimised our returns."

Burford 1H 2016 Results Presentation (slide #9)

> *"Arizona real estate investment concluded producing total cash receipts of $38.1 million on an investment of $7.4 million generating a 47% IRR".*

Burford 2017 Annual Report

> *"We would also note a significant change in our investment receivables balance. In many cases, a resolution of the underlying litigation is accompanied by a cash payment of our entitlement rapidly thereafter. However, there are some matters that take time to pay, often through agreement with the defendant, and those matters become receivables on our balance sheet. Our long-running and lucrative Arizona real estate matter that we won in 2010 and for which we ultimately received our core payment in 2016, with a 448% ROIC, would have been an example of a litigation receivable. We have an excellent success rate on collecting such receivables; indeed, we have never failed to do so. Moreover, we often garner considerable economic benefit from the delay, as was the case in the real estate matter. This year, however, we saw tremendous collections success, and our receivables balance has fallen to $3.2 million (from $39.4 million at the end of 2016). This is an area to which we devote significant attention and we are pleased with our continuing success."*

8. Why Did Burford Management Write about Desert Ridge Extensively? Here is Caro-Kann Capital's Explanation

Burford management wrote about the Desert Ridge saga extensively. ***Why did they write so much about it?***

While CEO Christ Bogart is better suited to answer this question, we will volunteer our hypothesis. Burford management wrote about this case extensively for three reasons.

First, the total recoveries of Desert Ridge were high relative to Burford's size at that time. Thus, keeping shareholders updated on this matter was appropriate.

Second, it was a successful case.

Third, it was an ***unusual*** case because Burford received a promissory note that was later converted into a mortgage as opposed to receiving cash right away. Hence, management felt compelled to tell shareholders about it and explain why Burford did what it did.

This shows management's desire to communicate openly and extensively.

9. Does Contingent Liability in Desert Ridge Exist?

Muddy Water pointed out that few years after Burford sold its mortgage notes to an unrelated seller, there were new developments in the case. To quote Muddy Waters:

> *"As a result of BUR's actions years after the conclusion of the investment, Gray's bankruptcy estate is now suing BUR for violating its "duties of good faith and fair dealing", alleging the note sale sent a signal to the market that Gray was not able to find a buyer for the property. BUR has adjusted down IRRs on Desert Ridge to 47% today. However, BUR has not acknowledged the significant contingent liability that accompanies this lawsuit, in which Gray's bankruptcy estate claims more than $200 million in damages. Final recoveries remain uncertain more than six years after Desert Ridge was concluded. BUR has not acknowledged the significant contingent liability that accompanies this lawsuit."*
>
> *Source: 2019-08-07 Muddy Waters Report.*

We have already discussed Muddy Waters' point about the decrease in IRR and why we think that despite its factual accuracy, it lacks sensible economic context and does not prove any wrongdoing by Burford.

Let's address the point about the contingent liability. It involves the court case *Epicenter Partners LLC et al. vs Burford Capital Limited et al*. Currently, the actual plaintiff is ELR[38]. We were not aware of this lawsuit and we appreciate it that Muddy Waters brought it to our attention. To be clear, we do not follow every single case that Burford funds and we do not try to predict which one will be a winner and which one will be a loser. After all Burford employs a large number of highly skilled and experienced litigators and still does not get 100% success rate. Nobody does. We do not expect that we would do a better job than Burford on this front. This is similar to public markets investing: clients allocate funds to an investment manager and do not question every investment decision that such manager makes.

After researching *Epicenter Partners* and reviewing relevant court documents, we have come to the following conclusions.

1. The lawsuit was indeed filed in Arizona.

[38] Epicenter Partners LLC ("Epicenter") and Gary, Meyer, Fannin LLC ("Gary") each filed for bankruptcy on May 16, 2016. (Doc. 1-2 at 72). On May 1, 2018, pursuant to an Order in the bankruptcy cases, R.O.I. Properties, LLC ("ROI"), as Liquidating Trustee of the May Liquidating Trust, became authorized to pursue claims on behalf of Epicenter and Gary. (Id.) On August 22, 2018, the Bankruptcy Court approved a settlement, and under the terms of the settlement ROI transferred the claims it brought on behalf of Epicenter and Gary to Epicenter and Gary. (Id.) On August 31, 2018, Epicenter and Gary assigned this claim to Epicenter Loss Recovery, LLC ("ELR"). (Id.) On September 18, 2018, Plaintiffs filed a Second Amended Complaint ("SAC") which substituted ELR as the only Plaintiff in this litigation. (Doc. 1-3 at 71). Therefore, the only Plaintiff remaining in this litigation is ELR.

2. Burford objected and claimed that this dispute is subject to arbitration in London.
3. Judge agreed with Burford's position and *put a stay on the case*. It means that before the court hears the case (if at all), it must first be subject to arbitration proceedings.
4. Judge further ruled that it will be up to an arbitrator to decide which claims are subject to arbitration and which are not.
5. Burford's position appears to be very strong. However, we do not pass our own judgment on the prospects of any cases that Burford is involved in even if we feel one way or another.
6. The plaintiff suing Burford was seeking litigation funding and because it was having a difficult time obtaining such funding, it has not pursued arbitration as of early August 2019.
7. The plaintiff's original lawyer withdrew from representation. The court imposed a deadline on the plaintiff to engage other counsel. On the day of the deadline (August 8, 2019) a new counsel for the plaintiff entered the case.

Based on our analysis, there have been no judicial or arbitration decisions that would require Burford to recognize a potential liability if it were to lose the case. Thus, we do not see any wrongdoing on Burford's part here, either.

IV. Claim #2 (Cont'd): Deemed Recoveries Lead to Increased IRRs. *"Dead Inventor"* Case Is Evidence

1. Essence of Muddy Waters' Claim about the *"Dead Inventor"* Case

Muddy Waters provides another example to show that Burford aggressively counts litigation / arbitration awards and settlements with questionable collections.

2. Caro-Kann Capital's Position

In our opinion, the *"Dead Inventor"* case merely shows that Burford receives recoveries in non-cash form on rare occasion. It is worth noting that the dollars involved here are relatively nominal. The unusual nature of this case was exactly what compelled management to talk about otherwise inconsequential situation from a dollar perspective.

3. What Happened in the *"Dead Inventor"* Case

This is what Muddy Waters wrote:

> *"in H1 2019 (case 122094), BUR disclosed a perplexing scenario in which it had received as proceeds certain intellectual property "that was dependent on the inventor's continuing activities". The inventor died, and according to BUR, it had to write down the recovery in the associated case by $3 million. Whether this tragic event was foreseeable or not is impossible to gauge, but the fact that BUR received a non-cash recovery with a subjective valuation does not inspire confidence in the caliber of said "recoveries".*
>
> *Source: 2019-08-07 Muddy Water Report.*

We agree 100% with the facts that Muddy Waters laid out. In fact, Burford has provided those facts in its 1H 2019 Interim Report:

> *"The other matter is a small investment where a settlement was achieved in a case involving some intellectual property that was dependent on the inventor's continuing activities; regrettably the inventor died unexpectedly, calling into question the ongoing viability of the intellectual property and causing us to reduce our previously-recognised return by $3 million both in our portfolio reporting and on our income statement."*
>
> *Source: Burford 1H 2019 Interim Report.*

This claim by Muddy Waters did not require investigative work. In this case Muddy Waters used what management clearly disclosed less than a month ago to its advantage.

Why did Buford management talk about this case? It did not have to bring up this case at all. It was a tiny case given Burford's scale. Again, our assertion is that management *wanted* to discuss this case because it was unusual to begin with and had even more unusual – and negative – ending. This again demonstrates management's commitment to shareholder communication.

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V. Claim #3: Burford Does Not Reduce ROIC and IRR from *Investments* that It Acquired by Purchase Price It Paid for Acquired *Operating* Businesses

1. Essence of Muddy Waters' Claims about Misrepresentation of Returns on Investments Acquired Through Acquisitions of Operating Businesses

The essence of Muddy Waters' critique here is straightforward: when Burford acquires an operating business (and as a result of such acquisitions also receives litigation investments), Burford should allocate a portion of the purchase price for the operating business to the cost basis of investments' when Burford calculates ROIC and IRR. To support its views, Muddy Waters provided two examples.

2. Caro-Kann Capital's Position

We respectfully disagree with Muddy Waters' viewpoint in two ways: conceptual and fact specific. Furthermore, examples that Muddy Waters provided to prove that Burford misrepresented IRRs on investments in questions are not persuasive. Burford pointed out multiple factual inaccuracies in Muddy Waters' examples. Management's position on the matter is fact based and well supported, and Muddy Waters has yet to challenge those corrections. In fact, a careful review of past disclosures demonstrates that Muddy Waters is mistaken.

3. Why Is Muddy Water's Conceptually Incorrect?

Let's start with conceptual disagreement. ROIC and IRR are the "unit economics" of Burford's business. We use ROIC and IRR to determine whether Burford is good at its job – picking up and funding litigation and arbitration cases. This analysis is not about whether Burford is good at M&A (though we believe Burford management is very strong at M&A as well).

If we were measuring Burford's M&A ability, then the purchase prices indeed become relevant. However, those purchase prices should *not* be applied against the ROIC and IRR of investments as Muddy Waters suggest. Instead, purchase prices should be compared to net income / free cash flow received from running acquired businesses.

Muddy Waters is mixing two disparate approaches in its analysis and, as a result, arrives at a conclusion that we disagree with.

4. Muddy Water Appears Mistaken About Facts of Those Examples

We do not have unique insights about the two examples that Muddy Waters provided. However, Burford's management came out with factual rebuttals to those examples. Muddy Waters did not address management's responses on any of these examples in their follows up.

In the interest of completeness, we will provide Muddy Waters' examples and management rebuttal below.

a. Focus Intelligence and Asset Recovery Business

Muddy Waters starts with an example of Focus Intelligence that Burford acquired to enter the asset recovery business:

> *"BUR acquired asset recovery business Focus Intelligence Limited in January 2015, and an attendant Legal Services case (Case Number 154586) is shown as generating $4.9 million on a $2.2 million investment, with an ROIC of 186% and an IRR of 138%. However, BUR excludes the $1.5 million spent to acquire Focus Intelligence in the first place. Because the acquisition was essential to putting the case on BUR's balance sheet, a portion of the purchase price should be included in the investment denominator."*
>
> *Source: 2019-08-07 Muddy Waters Report.*

This is what Burford management wrote in response:

> *"In 2015, Burford acquired Focus Intelligence, the foundation for what is now its asset recovery business. The purchase price of £1 million was not for any investments, but for the operating business itself. Indeed, the principals of Focus retained for their personal account their principal investment matter at the time, which had concluded but was awaiting payment. The investment cited in the report is a post-acquisition matter; it did not exist at the time of the acquisition (indeed, it was one of our first investments to put capital at risk in the asset recovery business). The report is simply wrong on its facts."*
>
> *Source: 2019-08-08 Burford Rebuttal.*

Again, we do not have unique insights as to whether Burford took Legal Services case after the acquisition or not. We find management's response credible. Furthermore, Muddy Waters did not address management's response in its follows up.

b. Magnesium Corporation of America Case

Muddy Waters provided another example showing that Burford misleadingly represented an investment that Burford inherited through acquisitions at a favorable IRR – *Magnesium Corporation of America* case.

> *"BUR's behavior in a bankruptcy case interest it acquired via the Gerchen Keller Capital acquisition, Magnesium Corporation of America, et al., ("MagCorp"), demonstrates another instance of BUR's manipulating investment costs. In 2017, pursuant to a judgement in favor of the bankruptcy estate, BUR booked an ROIC of 93% and an IRR of 75% on the investment. BUR makes no adjustment for the allocation of the $160 million purchase price of Gerchen Keller to Gerchen Keller's $15.0 million investment cost. Against a recovery of $28.9 million, allocating even $3 million from the purchase price would drop the ROIC to 63%. Viewed from the context of any reasonable apportionment of the acquisition cost, MagCorp returns would not appear as stellar.*
>
> *Furthermore, after buying Gerchen Keller, BUR made further investments in the MagCorp case from its own balance sheet ("MagCorp BS"). However, BUR marked this balance sheet investment separately, starting from the date of the Gerchen Keller acquisition. This maneuver allowed the company to report a MagCorp BS ROIC of 92%, similar to the original, but with a higher IRR of 107%. BUR would quite possibly have been unable to gain a late entrée into funding the MagCorp case but for purchasing Gerchen Keller. By not only excluding any acquisition costs, while also cherry picking the investment start date in an arbitrarily separate investment, BUR again manipulated its ROICs and IRRs."*

This is what Burford management wrote in response:

> *"In 2016, Burford acquired Gerchen Keller Capital ("GKC"). GKC was a fund manager, not generally a direct balance sheet investor like Burford, and we were buying GKC for its fund management platform. Our acquisition was of GKC's operating business as a fund manager; it was not the acquisition of GKC's investments (which were owned by the funds managed by GKC, not by GKC itself). Burford reports in its investment data chart the performance of fund investments for the information of investors and so that investors may take views on potential performance fee income, but when Burford publishes returns on its core litigation finance business, as it does each period, those returns are solely for balance sheet investments as is made clear in the disclosure. It is obviously wrong to say that Burford "booked" direct investment*

> *returns from the GKC funds' MagCorp investment, as is apparent from the face of the investment data chart.*
>
> *The third point in this section is also wrong. Burford did not make "further investments" in MagCorp. Rather, as disclosed in our 14 December 2016 RNS (at footnote 2), in addition to the acquisition of GKC itself, Burford separately purchased at cost two small interests in litigation finance investments held directly by the GKC manager. MagCorp was one of those investments, as reported in the investment data chart, and its returns for the Burford balance sheet were computed as they always are, without any "cherrypicking" – from the date cash was deployed to the day it returned."*

Indeed, RNS dated December 14, 2016 that announced Burford's acquisition of GKC states the following[39]:

> *"Concurrently with the transaction, Burford is purchasing from GKC at cost minority participations in two existing litigation finance investments in which GKC took an on-balance sheet interest. Those investments have been reviewed and approved by Burford's Investment Committee. The aggregate purchase price of those investments is $4.3 million."*

We find Burford's response satisfactory, logical, and appropriate.

5. Muddy Waters' Examples Do Not Prove that Burford Misrepresented IRRs of Investments that It Obtained through Acquisitions

We do not find examples that Muddy Waters provided proof that Burford misrepresented IRRs on investments that it has obtained through acquisitions. We do not find Muddy Waters' approach persuasive either at the conceptual level or fact-specific / case specific level.

[39] https://otp.investis.com/clients/uk/burford_capital/rns/regulatory-story.aspx?cid=1377&newsid=828798

VI. Claim #4: Burford Inappropriately Calculates ROIC of Partial Recoveries; e.g. the *Mr. Akhmedov* Case

1. Essence of Muddy Waters' Claims about Inappropriate Denominator in ROIC Calculations and Akhmedov Case

Muddy Waters' opinion on this matter is nothing new. Muddy Waters broadly repeats an argument that Canaccord Genuity pioneered in their 2019-04-30 analyst report. That approach suggests that Burford should not do any allocation of cost basis in case of a partial recovery and as a result Burford should report a negative ROIC until the initial investment is recouped.

Muddy Waters used the *Akhmedov* case to support its assertions and pointed out a multimillion-dollar lawsuit that Mr. Akhmedov filed against Burford.

2. Caro-Kann Capital' Position

We disagree with Muddy Waters' approach to critiquing this metric and believe that the cost allocation approach deployed by Burford is conceptually preferred and is an intellectually honest method. That said, Burford provides so much data in its detailed disclosures that one can calculate ROIC any way they want, a practice for which Burford should be credited.

We diverge further from Muddy Waters' perspective with regard to some of its supporting evidence. Muddy Waters presented factually correct data about the *Akhmedov* case to support its assertions. However, many of these data points such as the length of prior divorce proceedings are *irrelevant to Burford at this point* because Burford was never involved in divorce proceedings. Their length, whatever it was, is a matter of the past and is irrelevant to Burford. Burford simply pursues a judgment issued *after* the divorce proceedings, which is an entirely different legal matter.

Other data points such as public information about Mr. Akhmedov's lawsuit against Burford are optically sensational and appear damning but lack relevant context. The actions outlined by Muddy Waters are, in fact, typical for high stakes litigation. Outcomes are too early to judge, and the high headline number does not mean much at this stage. Furthermore, *the judgment issued by an English court remains outstanding and valid and is enforceable*. We believe Muddy Waters has done the market a disservice by not providing the relevant context on this point.

3. Two Potential Approaches to Calculating ROIC and IRR on Partial Recoveries

Muddy Water's position here addresses a well-known issue that has been discussed at length in the past: ***how should partial recoveries be treated when calculating ROIC and IRR?***

This is the essence of the matter. Imagine that Burford makes $10M investment in a litigation matter. Imagine further that Burford receives $3M back while a litigation matter has

not been concluded and further recoveries are possible. How should Burford report this matter in its investment data (non-IRFS reporting)?

Conceptually, one can take one of two approaches: the **"all you see is all there is" approach** and the **cost allocation approach**.

In **"all you see is all there is" approach** one would say that Burford so far has recovered only $3M against its "cost basis" of $10M. Thus, Burford has a loss of $7M or ROIC of negative 70% so far. If Burford receives more money, then Burford would revise it up. For example, if Burford subsequently receives another $12M for a total recovery of $15M, Burford later can report 50% ROIC. There is nothing wrong *per se* with this approach. Will it be the most informative to investors? Probably not. Indeed, many cases would be reported at large losses using this lens as many initiatives involve recoveries over time and thus, it may not be the right tool for investors to accurately gauge a firm's ability to deploy capital.

Under **the cost allocation approach**, one would apportion the cost basis between the recoveries that already occurred ($3M in our example) and the remaining recoveries in the future. This approach is analogous to cost allocation in stock investing. If one bought 100 shares of Amazon at $1,000 per share for a total of $100,000 and then sold 30 shares out of 100 at $1,300 for a total proceeds of $39,000, that person or institution would reasonably say that they made a profit of 30% or $9,000 on the exited part of their investment. Using the "all you see is all there is" approach would lead to a conclusion that such investor has a loss of $61,000 (cost basis of $100,000 minus proceeds of $39,000).

4. Can Cost Allocation Approach Be Applied to Litigation Finance Investments?

The cost allocation approach seems very logical in the context of stock investing.

Does the same logic apply to the field of litigation finance? Conceptually, there is no reason why the cost allocation approach should not apply to litigation finance investments.

5. Burford Chose the Cost Allocation Approach But Provides Plenty of Data to Investors to Apply Whatever Approach *They* Choose

Burford has chosen to apply the cost allocation method and utilizes certain methodologies to allocate the cost basis. We believe that is the right approach, and we have already explained why. However, should anyone disagree, Burford provides plenty of data so that a discerning investor does not have to follow Burford's approach and instead can run their own math and apply the "all you see is all there is" approach. Burford should be created for this practice.

It is also important to keep in mind that partially concluded investments eventually move to the concluded investments, and one can see how those "partially concluded" investments' ROIC and IRR have played out eventually.

The "all you see is all there is" approach was pioneered by Canaccord Genuity in April 30, 2019 analyst report.

Burford management outlined their own thinking on this matter in 1H 2019 Interim Report:

> *"One analyst has made the derisible suggestion that we should compute the return associated with partial resolutions against the cost of our entire investment, instead of engaging in the allocation process described above; we do not typically discuss analyst views but we discuss this point because of its deliberately sensationalized dissemination in the market. That is akin to saying to an equity investor who bought 200 shares of stock and sold 50 of them that the return on the 50 shares sold should be computed using as the denominator the cost of all 200 shares. To use a real Burford example, we made a multi-case portfolio investment in 2017 in which the Burford balance sheet invested $127 million. It is early days still for that investment; thus far we have recovered $21.5 million from that portfolio and we have allocated $17.8 million of cost against those recoveries in a classic example of a partial investment resolution. Therefore, we are reporting a $3.7 million gain from an attributable $17.8 million investment, with a 21% ROIC to date. That return will form a part of our total return disclosure, on a weighted-average basis. All of this is publicly disclosed on a line-item basis in our investment portfolio reporting. The analyst in question, on the other hand, would include all $127 million in the denominator of our ROIC computation the moment we have any recovery at all in the portfolio, which would treat the investment at present as generating $105.5 million of losses for return computation purposes. We are unaware of anyone computing returns like that in any sector of the financial services industry."*

One thing that we cannot emphasize enough is that ***Burford does not impose its views on anybody (even though it clearly indicates which approach it finds most accurate) and provides plenty of data to investors to calculate Burford's returns under either method***.

Hence, Muddy Waters' argument here is nothing new.

6. Akhmedov Case

Muddy Waters digs deeper, however, and uses a well-publicized case that Burford is pursuing as part of its asset recovery business: the collection efforts against Mr. Farkhad

Akhmedov, a case which Burford has funded and has been providing asset recovery services to Ms. Tatian Akhmedova, ex-wife of Mr. Akhmedov.

In the *Akhmedov* case, Burford deployed ~$18M and received partial recoveries of $5.2M. Burford reported a ROIC of 59% using $3.5M of allocated cost basis.

Muddy Waters points out that:

(1) "denominator as an arbitrary small amount"
(2) "ROIC and IRR seem absurd on other fronts":
    a. "this divorce is highly complex and has already spanned over half a decade"
    b. "the defendant has made significant efforts to make assets collection-remote"
    c. Mr. Akhmedov's yacht that was impounded in Dubai was released
    d. Mr. Akhmedov is suing both Ms. Tatiana Akhmedova and Burford in Dubai for $85M in damages for the yacht's wrongful impoundment.

Let's go through this point one by one.

a. Denominator Is Arbitrary and Small Amount

Without knowing the exact cost allocation methodology, it is *impossible* to judge whether Burford's allocated cost is too small. We are not privy to such facts. We expect that Muddy Waters is not privy, either. Most likely, Burford management applied its usual methodology to determine the denominator. As the case further progresses, these numbers almost certainly will be updated and revised.

b. The Divorce Is Highly Complex and Has Already Spanned Over Half a Decade

We agree with Muddy Waters that this particular divorce was highly complex and took a long time. One can review multiple news articles referenced by this Wikipedia page[40] to get a sense of how the divorce proceedings developed.

However, we will point out that ***the duration of the divorce proceedings is irrelevant*** because Burford has nothing to do with the divorce. On recent conference calls, investors have expressed a large amount of confusion about this case. We can attempt to provide a brief explanation to ameliorate some of that confusion.

The divorce proceedings ended in England before Burford entered the stage. It is our understanding that the divorce proceedings ended in 2016 and Ms. Tatiana Akhmedova received an award in her favor that was reported to exceed $500M. There is an outstanding court judgment issued by an English court. Mr. Akhmedov did not pay the award. As common in

[40] https://en.wikipedia.org/wiki/Farkhad_Akhmedov

such situations, the party who received an award need to engage in various enforcement activities – *i.e.*, activities to enforce the judgment.

At that point the nature of the court proceedings that led to an award is *irrelevant*. In other words, it does not matter whether the award was granted as a result of the divorce proceedings, commercial dispute, or construction litigation. It is just a litigation award. This is now the point at which Burford enters the situation. It was reported that Burford got involved in 2018.

Thus, while true that the divorce proceedings lasted from 2013 to 2016, *that duration means nothing for Burford or its investors*.

c. The Defendant Has Made Significant Efforts to Make Assets Collection-Remote"

We tend to agree with this statement by Muddy Waters. We would take it even one step further. We strongly suspect that every asset recovery matter that Burford takes involves a defendant that is not willing to pay and may have made efforts to make assets collection-remote. So what? This is why Burford is brought in. If a defendant loses a case in court and says "there is a court judgment; I owe a plaintiff $20M; I will go to a bank and wire the money tomorrow", Burford has no role to play.

d. Mr. Akhmedov is Suing Both Ms. Tatiana Akhmedova and Burford in Dubai for $85M in Damages for the Yacht's Wrongful Impoundment

This lawsuit has been widely reported. In fact, we have seen media articles saying that the lawsuit is actually for $200M. We have not reviewed the court papers in Dubai to be certain which reported amount is accurate.

Based on the media coverage, the litigation about the yacht Luna was a true court battle. The court of first instance ruled in favor of Burford but was overturned by the appellate court.

The legal matters of enforcing judgments in a jurisdiction other than the jurisdiction where court proceedings took place are incredibly complex and teams of highly qualified lawyers fight hard to gain an edge. We tend to think that Burford's loss in Dubai does not mean that the English court judgment cannot be enforced in other jurisdictions. However, we do not pretend to be experts either in English law or Sharia law.

The lawsuit against Burford is also quite live. Matters of litigation are unpredictable. Can Burford lose this lawsuit and be on the hook for a substantial amount of damages? Yes, it is possible. Litigation finance in general and asset recovery in particular are adversarial activities, and any legal battle involves a risk of being countersued. It is highly unlikely that Burford leadership, the investment committee, and attorneys do not understand that basic, self-evident truth.

We believe that Burford analyzed those risks and concluded that the investment and particular course of action in Dubai was justified. It does not mean that their analysis gave them certainty. Like in investing, certainty does not exist. At this point, we simply do not know what will happen. Muddy Waters does not know, either.

If Burford loses the court battle in Dubai, we would expect that Burford will update its investment data per its policies.

e. Mr. Akhmedov Case: Conclusion

Muddy Waters presented factually correct data about Akhmedov case. However, many of the surrounding data points presented (such as the length of prior divorce proceedings) are irrelevant to Burford. Other data points such as public information about Mr. Akhmedov's lawsuit against Burford make look concerning or even scary but are quite typical for high stakes litigation. Outcomes are simply too early to judge.

VII. Claim #5: Burford Delays Recognizing a Trial Loss for Two Years / *Progas* Case

1. Muddy Waters' Claims about *Progas*

Muddy Waters relies on *Progas*, an international investment arbitration case that Burford's client lost, to demonstrate that Burford delays recognition of its losses.

2. Caro-Kann Capital's Position

In our opinion, *Progas* and *Teinver* cases show that Burford *consistently* applies the same reporting policy. In *Progas* that policy resulted in a "delay" of recognition of a loss. In *Teinver* the same policy resulted in a "delay" in recognition of a massive win.

3. What Muddy Waters Asserts and *Progas* Case Background

According to Muddy Water, Burford delays recognition of a trial loss so that such loss does not impact its reported ROIC and IRR on concluded investments in a timely manner.

Muddy Waters provided an example of *Progas Energy Ltd. vs. Pakistan* ("Progas").

The case was an Investor-State arbitration case where an investor (Progas) asserted that the sovereign state (Pakistan) violated rights granted to Progas under the Mauritius – Pakistan bilateral investment treaty[41]. Progas was seeking to receive ~$500M from Pakistan. It was a potentially lucrative case, and Burford funded it in 2010.

International investment arbitration cases are complex and span multiple years unless settled by the parties. Finally, in 2016 the arbitration tribunal decided in favor of the state – Progas lost. However, Progas had the right to appeal and Progas chose to do so.

It is important to highlight that an appeal after the investment treaty arbitration decision is very different from an appeal in litigation proceedings. Let's start with the litigation proceedings. After the trial court decides a case, a plaintiff or defendant can exercise their right to appeal, and the appellate court would hear the case. The grounds for appeal are broad and the appellate review is also broad. While we are by no means litigation lawyers, it is our understanding that in the United States, an appellate court can decide any issues related to the law applied by the trial court.

In a situation when an arbitration decision is appealed, the grounds to nullify the arbitration decision are extremely limited. Due to such limited grounds, *very few annulment*

[41] https://www.italaw.com/sites/default/files/laws/italaw6181.pdf
The full name of the treaty is Agreement between the Government of the Republic of Mauritius and The Government of the Islamic Republic of Pakistan for the Promotion and Reciprocal Protection of Investments. However, international lawyers often refer to these treaties as bilateral investment treaties or BIT for short.

decisions are granted. We have heard various lawyers quote 1% to 3% as a possible success rate.

Hence, Progas had a very low chance of getting an annulment decision.

That's why Burford wrote the following in 2018 Annual Report:

> *"The final matter was also against a government which, our client alleged, had broken its promises about the operation and regulation of the market in which the client was participating. The facts were compelling and the arbitral tribunal criticised the government's conduct but ultimately decided that the principal cause of the client's damages was its flawed business plan, even if the government's bad acts had exacerbated the situation, and thus precluded any recovery, causing the loss of our $10.4 million investment and the bankruptcy of the client. We continue to believe that the decision was deeply flawed but arbitration decisions are very difficult to overturn and it rarely makes sense to spend incremental capital trying to do so."*
>
> *Source: 2018 Burford Annual Report.*

It appears that Burford did not outlay additional money to fund Progas' appeal, which seems prudent given the likelihood of success. Progas lost its appeal in 2018.

Muddy Waters *correctly* pointed out that the loss was not reported in Burford's investment data until 2018.

4. Why Does a *Factually* Correct Assertion by Muddy Waters *NOT* Mean that Burford Did Something Inappropriate?

Muddy Waters is correct about the facts presented in this case. However, we do not see why management's behavior is not appropriate, and we believe the reporting was accurate and truthful.

Under Burford's longstanding and well-articulated approach, a matter is not concluded if any appeal is pending. Progas was pursuing an appeal and as a result the matter was *not* treated as concluded. This approach is logical. Therefore, Burford did not report a loss until 2018.

We would point out that this approach sometimes delays recognition of a loss and sometimes delays recognition of an impressive win. ***The rule cuts both ways***. We will provide an example.

Teinver is an excellent example of where this approach in question "delayed" reporting *Tienver* matter as concluded. *Teinver* is a well-publicized arbitration case where Burford made a profit of $94M on a $13M investment and generated 722% ROIC and 39% IRR[42].

In 2017 the arbitration panel decided the matter in Teinver's favor. However, Burford – ***according to the same exact policy*** that was applied in *Progas* – did not report the investment as concluded. The underlying legal nature of the disputes in *Progas* and *Teinver* is almost identical: we are dealing with investment treaty arbitration cases. After the arbitration panel ruled out in favor of Teinver, Argentina still could appeal, and it did so. Probabilistically, Argentina faced about the same chances of success as Progas did: between 1% and 3%. Still, Burford did not report *Teinver* as a concluded investment following the same logic as it followed with respect to *Progas*.

This is how 2010 vintage investments appeared in 2017 Annual Report:

Investment performance

$ in millions	# of investments	Total commitments	Total invested	Total recovered	ROIC	IRR
Concluded	3	$11.5	$11.5	$40.1	**251%**	**32%**
Partial realisation	–	–	–	–		
Ongoing	–	–	–	–		
2009 vintage total	**3**	**$11.5**	**$11.5**	**$40.1**		
Concluded	12	$70.5	$57.8	$75.6	**31%**	**10%**
Partial realisation	–	–	–	–		
Ongoing	4	$44.8	$44.8	–		
2010 vintage total	**16**	**$115.3**	**$102.6**	**$75.6**		

Source: Burford 2017 Annual Report.

In 2018 Burford sold its entitlement to third parties and received cash. However, the appeal was *still* pending. Hence, the buyers and Burford agreed that if the appeal is decided in favor of Argentina (again – small chance), Burford would return the cash to the buyers and Burford can pursue other litigation venues.

As a result of this – and under the same exact policy Burford applied to *Progas* – Burford did not recognize *Teinver* as concluded matter.

This is how 2010 vintage investments appeared in 2018 Annual Report:

[42] https://otp.investis.com/clients/uk/burford_capital/rns/regulatory-story.aspx?cid=1377&newsid=1271410

Investment performance

Core balance sheet litigation finance investments

$ in millions	# of investments	Total commitments	Total invested	Total recovered	ROIC	IRR
Concluded	3	$11.5	$11.5	$40.1	**251%**	**32%**
Partial realisation	–	–	–	–		
Ongoing	–	–	–	–		
2009 vintage total	**3**	**$11.5**	**$11.5**	**$40.1**		
Concluded	13	$81.8	$68.3	$75.6	**125%**	**21%**
Partial realisation	1	$13.0	$13.0	$107.0		
Ongoing	2	$22.3	$22.3	–		
2010 vintage total	**16**	**$117.1**	**$103.6**	**$182.6**		

As you can see "***total recovered"*** *did not change from 2017 to 2018 with respect to 2010 vintage*.

Finally, in May 2019 the annulment was not granted to Argentina (*i.e.*, Argentina lost). It meant that no litigation risk remained outstanding, and Burford *correctly* moved Teinver to concluded investments.

This is how 2010 vintage investments appeared in 1H 2019 Interim Report:

Investment performance

Core balance sheet litigation finance investments

$ in millions	# of investments	Total commitments	Total invested	Total recovered	ROIC	IRR
Concluded investments	3	$11.5	$11.5	$40.1	**251%**	**32%**
Partial realisation - concluded portion	-	-	-	-		
Partial realisation - ongoing portion		-	-	-		
Ongoing investments	-	-	-	-		
2009 vintage total	**3**	**$11.5**	**$11.5**	**$40.1**		
Concluded investments	14	$94.8	$81.3	$182.7	**125%**	**21%**
Partial realisation - concluded portion	-	-	-	-		
Partial resolution - ongoing portion		-	-	-		
Ongoing investments	2	$22.5	$22.4	-		
2010 vintage total	**16**	**$117.3**	**$103.7**	**$182.7**		

Source: Burford 1H 2019 Interim Report.

* * *

Thus, one could argue that in *Teinver* Burford "delayed" recognition of a win while one could similarly argue that in *Progas* Burford "delayed" a recognition of a loss. Alternatively, one can say – and ***this is our view*** – that ***Burford consistently applied the same logical and clearly articulated policy in both cases***. We rest our case and view Muddy Waters' assertion of delaying recognition of a trial loss does not support a view of Burford's inappropriate reporting and behavior.

VIII. Claim #6: Burford Keeps Trial Losses Out of the "Concluded Investment" Category

1. Essence of Muddy Water's Claim

Muddy Waters provided three examples of how Burford purportedly has kept trial losses out of the "concluded investments" category to boost ROIC and IRR:

(1) Neptune cases
(2) RCR Tomilson
(3) Husfeld LLP portfolio of cases.

2. Caro-Kann Capital's Position

We disagree with Muddy Waters' assertions and do not find examples persuasive. Let's go through all three of them.

3. Neptune Cases

Muddy Waters wrote the following:

> *"BUR financed a number of Inter Partes Review (IPR) patent challenges by generic drug company Neptune Generics, LLC ("Neptune"). However, by October 2017, one of these had received an adverse judgement. Neptune's loss was upheld on appeal. Meanwhile, other IPR petitions were not even instituted in the first place. However, Neptune remains Unconcluded, rather than Partially Concluded, contrary to what a reader might expect. The associated $7.6 million in commitments and $6.2 million in deployed capital for Neptune is unimpaired, per BUR's reporting".*
>
> In footnotes Muddy Waters wrote that Neptune matter is Case 166813.
>
> *Source: 2019-08-07 Muddy Waters Report.*

Burford wrote the following in its Rebuttal:

> *"the Neptune investment is entirely a fund investment; the Burford balance sheet has no part of it, and it predates Burford's acquisition of GKC. As discussed earlier, we report fund investment performance for investors' information but we do not include fund performance in our published investment returns. Investment 166813 cited by the report as Neptune is in fact not Neptune; Neptune is investment 177598. Neptune is a portfolio investment with a variety of results to date (both positive and negative) and is appropriately shown as a partially concluded investment. The investment discussed in the report is in fact a separate non-Neptune investment, 166813, which is appropriately classified as ongoing."*
>
> *Source: 2019-08-08 Burford Rebuttal.*

We are not in a position to say which matter is *indeed* Neptune and which is not. However, given that Muddy Waters' did not object to Burford's response to this particular point, we tend to think that management response is correct and accurate, and non-Neptune example does not prove that management keeps trial losses out of the concluded investment category.

4. RCR Tomlinson

RCR Tomlinson is as an Australian securities class action case.

RCR Tomlinson is an Australian company that allegedly misrepresented material facts in its disclosures and is being sued in securities litigation. Australian securities class action litigation is an area where many litigation finance firms operate and actively provide funding. In fact, some industry participants say that the litigation finance in its modern shape and form originated in Australia 15 – 20 years ago. Thus, Burford's involvement in this case is nothing unusual. In fact, Burford wrote about its activity in Australia in 2018 Annual Report:

> *"We have not historically been very active in the Australian market. Australia is very far away from our main centres of activity and we were neither ready to put someone on the ground in the country nor to try to manage a market position from thousands of miles away.*
>
> *However, in late 2016, we hired Craig Arnott as the head of our business outside the Americas. Although Craig is based in London, he is an Australian barrister (as well as a Rhodes Scholar who taught jurisprudence at Oxford and a lawyer who has practiced in New York, London and Europe as well as Australia)*

> *with deep insight into the market. That has enabled us to take some steps towards greater activity in Australia, which is a particularly litigious market.*
>
> *We think the Australian market has potential but we also think it is today characterised by oligopolistic tendencies, and we believe our entry into the market has the potential to disrupt it considerably. Our first foray, just in the last few months, is for a large shareholder claim against one of Australia's major financial services firms, AMP, where a number of its senior executives admitted a variety of corporate misconduct, causing the departure of its Chairman, CEO and CFO and the loss of more than A$2 billion in its market capitalisation. We have offered to finance that claim at a price well below conventional Australian norms (while still offering the potential for Burford to earn an appropriate risk-adjusted profit), and we shall see if we are successful both in landing the engagement and in transforming the Australian market."*
>
> *Source: Burford 2018 Annual Report.*

According to the media[43], the class action lawsuits alleged that RCR breached its prospectus and continuous disclosure obligations and engaged in misleading or deceptive conduct. The plaintiffs claim that RCR was aware or should have been aware of the risks associated with the company's portfolio of solar projects.

Muddy Waters pointed out that:

> *"BUR committed $4.8 million to finance a stockholder class action suit against RCR Tomlinson ("RCR"), an Australian engineering group. The case is marked as ongoing. However, after the initiation of the related class action suit, RCR Tomlinson entered bankruptcy with a significant secured and unsecured debt load ahead of equity. As a result, stockholders are likely to recover little to nothing from previously announced suits. BUR has not adjusted down RCR's carrying value to account for the likely restructuring."*
>
> *Source: 2019-08-07 Muddy Waters Report.*

It is correct that RCR entered into administration.

[43] https://www.lawyerly.com.au/two-firms-one-funder-out-after-judge-consolidates-rcr-tomlinson-class-actions/

It is *possible* that equity holders will recover nothing. First of all, they can lose the case in court. Second, there may be no money to collect.

However, the developments in the case indicate that this outcome is far from being certain. In fact, in the first half of August 2019, three law firms and three litigation funders were fighting in court to represent the class. Law firm Quinn Emanuel Urquhart & Sullivan was funded by Burford. IMF Bentham was funding Piper Alderman while Investor Claim Partners was funding Shine Lawyers. In the first half of August 2019 NSW Supreme Court Justice David Hammerschlag consolidated the cases[44]. As a result, Quinn Emanuel will be the only counsel representing the equity holders in the lawsuit and it will be jointly funded by Burford and IMF Bentham.

Does it mean that the equity holders will win *and* collect the money after? Of course not.

It does mean, however, the following:

(1) As recently as mid-August 2019, three profit-seeking enterprises were competing to "get" the case.
(2) Burford could have probably exited that competition at that time if it did not believe in the prospects of the case.
(3) After a law firm funded by IMF Bentham did not get the representation, IMF Bentham chose to stay and fund Quinn Emanuel together with Burford.

How can the collectability be possible given the high debt load that is ahead of equity holders in the capital structure? One reason can be D&O insurance coverage that RCR Tomlinson may have. However, we are not experts in Australian securities litigation. We prefer letting specialists such as Burford and IMF Bentham think about it.

All these facts indicate that a win and collectability of any award in RCR Tomlinson is very possible. All commercially driven actors are behaving that way.

5. Hausfeld LLP Cases / Volkswagen Cases

This example involves a portfolio transaction that Burford did with Husfeld LLP. That portfolio involves Volkswagen cases litigated in Germany. Muddy Waters asserts that there have been negative developments in those cases and implications are "recovery-killing". Despite those, Burford did not make many changes to its non-IRFS performance reporting.

> *"In 2015, BUR agreed to finance a portfolio of law firm Hausfeld LLP's cases. Since then, BUR has committed $44.3 million and deployed $34.4 million for these. However, several negative developments have come down in the Hausfeld cases. For example, a three-judge tribunal expressed a skeptical view of the*

[44] https://www.lawyerly.com.au/two-firms-one-funder-out-after-judge-consolidates-rcr-tomlinson-class-actions/

> *merits of a lawsuit against Volkswagen that Hausfeld filed on behalf of automobile owners, eventually denying the case in January 2019. Hausfeld must now appeal that ruling at the Federal Court of Justice, Germany's highest court. Furthermore, the Federal Court of Justice handed down a ruling in February 2019 denying BUR the ability to collect proceeds from a separate Hausfeld case. BUR's marks on the Hausfeld portfolio do not incorporate any of these negative developments, despite their potentially recovery-killing implications."*
>
> *Source: 2019-08-07 Muddy Waters Report.*

Here is Burford's response:

> *"the Volkswagen matters are also active litigation matters (and part of a diversified and cross-collateralized portfolio) and we can't comment on them. However, any dispassionate observer of the VW litigation would not be taking the view that its current posture is "recovery-killing", as the report suggests, with VW having already paid more than $30 billion in settlements related to the subject matter of this litigation."*
>
> *Source: 2019-08-08 Burford Rebuttal.*

We are not lawyers qualified to practice law in Germany, and we are cautious to infer exact legal implications from particular German court decisions. After all, Germany is a civil law country as opposed to a common law country. Precedents work differently in Germany or France than in the U.S. or the U.K.

However, we will discuss legal developments in Germany that Muddy Waters viewed as "potentially recovery-killing implications".

Muddy Waters talks about two legal developments in the Hausfeld LLP portfolio of cases. The first development involves a loss in court by a consumer because such driver did not buy the car directly from the manufacturer. This is the Bloomberg article[45] that Muddy Waters cites. The decision is currently being appealed and, therefore, the outcome of proceedings is still unknown.

It appears to us that this loss is limited to a particular set of facts and circumstances – *i.e.*, a driver purchased a car *not from the manufacturer*. It does not mean this court decision will have "recovery-killing implications" in other cases that may have a different fact pattern.

[45] https://www.bloomberg.com/news/articles/2018-12-18/vw-seen-scoring-new-victory-in-german-test-case-by-diesel-owner

Even more, the appeal was still pending when Muddy Waters published its report. Thus, according to Burford's policy the case is *still* ongoing.

The second development involves a "ruling … denying BUR the ability to collect proceeds from a separate Hausfeld case". This White & Case client alert covers it well[46].

The facts of that case seem to be very particular. The consumer association sued a telecommunications provider for wrongdoing. If the consumer association had won, the unlawfully generated profits would go to the federal budget of Germany, while a share of such profits would be paid to a litigation funder.

The consumer association won in the first and second instance courts. However, the German Federal Court of Justice ruled that the litigation funder could not get its share of confiscated profits.

According to White&Case:

> *"It [the Court] held that consumer associations may not promise a litigation funder any shares of the profits gained because this would amount to an abuse of rights (section 242 of the German Civil Code, which applies not only to questions on the merits but also on procedural conduct)."*
>
> *"The Court's decision is based upon an interpretation of the meaning and purpose of section 10 UWG. The Court held that the legislator explicitly wanted to avoid that an action for confiscation of profits is brought based on extraneous motives, such as the financial interests of a litigation funder."*

As far as we can tell, the key decision factor was that the consumer association was not obtaining any payout in case of its victory and all profits would be going to the German Government.

Indeed, this is what White & Case concludes:

> *"The good news for litigation funders is that the decision is not likely to affect the general principle established by the German Federal Court of Justice, according to which, litigation funding is admissible in civil proceedings. Indeed, the reasoning is specific to confiscation of profits by non-profit consumer association and cannot be transferred to damages claims."*

[46] https://www.whitecase.com/sites/whitecase/files/files/download/publications/german_federal_court_of_justice_prohibits_third_party_funding.pdf

Thus, it appears that this ruling may have relevance for some Burford's cases and not have much relevance for other cases. Time will tell.

This is how Burford reports this case in its Investment Data:

INVESTMENT DEMOGRAPHICS						INVESTMENT SUMMARY											BALANCE SHEET		
Vintage Status Structure	ID	Type	Industry	Geography	New $ Out / In	% of Vintage	Original Commit	Prior Follow-on Commit	2019-H1 Follow-on Commit	Total Commit	Total Deploy	Total Recover	ROIC	IRR	Weighted Average Duration	Simple Duration	BS Commit	BS Deploy	B Recove
Portfolio																			
	144379	Mixed Portfolio	Mixed	Europe	x	19%	44.3		22.0	66.3	35.3						66.3	35.3	
	144464	Antitrust	Telecommunication Services	Europe		7%	24.0			24.0	13.4						24.0	13.4	
	177521	IP	Media & Entertainment	North America		1%	2.5			2.5	2.5								

We believe there is another reason why Burford may be carrying this portfolio matter as *not* concluded. There may be cross-collateralization among matters.

Regardless of how these court disputes are resolved in the future, we see plenty of reasons why Burford *correctly* does not treat this portfolio as "concluded". ***Thus, the Hausfeld portfolio does not prove that Burford is delaying recognition of losses***.

6. Conclusion

Despite Muddy Waters' claims and after digging into all three examples we do not see evidence that Burford keeps trial losses out of the "Concluded Investment" category. Instead, Burford is consistently applying the set of policies that it told investors it would apply.

IX. Claim #7: Burford Failed to Deduct Various Costs and Operating Expenses Against Recoveries

Muddy Waters writes that Burford reports its ROIC and IRR without taking its operating expenses into account.

As with several other claims, this is factually correct, but this is not the point of the disclosures of ROIC and IRR provided by Burford.

Imagine that you are analyzing a publicly traded investment manager. What would you look at? Revenue, operating income, earnings. That makes sense. Will you stop there? Probably not. Would you want to know the track record of the fund (*i.e.*, how much money they made by picking stocks)? Most likely.

The intent behind Burford's disclosure of its ROIC and IRR is similar except for the fact that Burford has historically invested mostly from its own balance sheet.

In other words, Burford provides ROIC and IRR data so that investors can evaluate "unit economics" of this business and see whether Burford team members are good at what they do – picking litigation and arbitration cases to fund. This is a critical piece of information to have as a prospective investor.

Any discerning investor would also want to look at operating expenses, operating income, and net income. This is what IFRS financials are for.

To conclude, netting out operating expenses of Burford against its reported ROIC and IRR would destroy the purpose of Burford's entire non-IRFS reporting. Thus, we respectfully disagree with Muddy Waters on this point.

X. Claim #7 (Cont'd): Muddy Waters Claims that Burford Has a High Expense Ratio (9%) as a Percent of Its *Adjusted* Capital Base

1. Essence of Muddy Waters' Claims

Muddy Waters asserted that shareholders are overpaying management because of an extraordinary high expense ratio of ~9%.

2. Caro-Kann Capital's Position

We disagree. We see an expense ratio of ~4.25% and the entire expense ratio is lower than a hedge fund with a 2% and 20% fee structure would charge given high returns Burford has been delivering.

3. How Expense Ratio is Calculated

Mathematically, Muddy Waters is correct.

However, Muddy Waters stated that it is using *Adjusted* Capital Base – capital base excluding fair value adjustments.

Given that Muddy Waters has not proven that fair value adjustments are inappropriate, we do not see any reason why one should think about expenses of Burford as a percent of its *Adjusted* Capital Base and not as a percent of Capital Base. After all, the Capital Base has grown and now those assets are worth more.

On June 30, 2019, Burford had (excluding interests in a consolidated but not wholly owned fund):

- ✓ ~$1.566B of litigation investments
- ✓ ~$120M of due from settlements of litigation investments
- ✓ ~$186M of cash and cash equivalents

We are omitting some smaller items from this list for the sake of brevity.

Thus, Burford has $1.872B+ of investments and investable assets. This number is 100%+ higher than what Muddy Waters uses. Thus, 9% operating expense ratios becomes ~4.25%.

Is this number (4.25%) reasonable? To answer that question, let's look at a hedge fund fee structure: 2% and 20%. Let's keep in mind that Burford returns are substantially higher than a typical hedge fund and not correlated with the stock market and economy.

Let's pick a gross return of 30% and apply 2% and 20% fee structure. Management fee is 2%. Thus, the incentive fee = (30% minus 2%) * 20% = 5.6%. 2% management fee + 5.6% of incentive allocation = 7.6%.

Well, 7.6% is almost twice as high as Burford's expense ratio of 4.25% that we calculated above.

Again – while Muddy Waters is factually correct, we disagree with their approach.

XI. Claim #8: Burford's ROIC Is Highly Reliant On a Few Outlier Cases[47]

1. Essence of Muddy Waters' Claims

Muddy Waters asserted that Burford ROIC is better assessed without four cases since they represent outliers.

2. Caro-Kann Capital' Position

We find this line of argument to be problematic on multiple levels.

3. Buford Investment Style: Downside Protection and Occasional Home Run

To start, on what basis is it sensible to discount Burford's biggest wins? Burford's business is about both protecting downside (even though some cases end up being complete losses) and capturing the occasional home run outcome (e.g., asymmetric return profile).

4. Return Attribution of Highly Successful Investors

The return streams and attribution of highly successful fund managers are not normally distributed – limited number of ideas tend to generate the vast majority of a fund's alpha. What would venture capital as an asset class look like if you applied the same treatment?

5. Burford Is Still Highly Profitable Even without Four Outlier Cases

Ironically Burford is still a highly profitable enterprise even if one removes its biggest wins measured by ROIC (and even more so when adjusting for errors in Muddy Waters' adjusted ROIC).

Muddy Waters claims that ROIC without those "outlier" cases is 19%. In reality, it is 30%+. Muddy Waters mismatched IFRS reporting for *all* cases and non-IRFS investment data that covers *only core litigation* matters and does not cover complex litigation strategies that have substantially lower ROIC (~15% to ~20%) but strong IRR.

6. Tension between ROIC and IRR

Finally, such analysis ignores the fact that such high ROIC comes together with longer duration and while IRRs are still higher than portfolio averages, the difference is a lot less dramatic. For example, *Teinver* was an unquestionable success and generated 722% ROIC but "only" 39% IRR. Over the same period of time Burford could have invested in several cases with lower ROIC but still an attractive IRR of ~30%.

[47] This claim was not numbered by Muddy Waters. We will assign "number 8" to it as a matter of convenience.

XII. Claim #9: Burford Had Ulterior Motives for GKC Acquisition Such as to Consolidate Assets in Order to Make Debt Load Look Less Ominous[48]

1. Essence of Muddy Waters' Claims

Muddy Waters questioned the true motivation of Burford for acquiring GKC, a U.S. based asset manager (e.g., a litigation finance hedge fund):

> *"We cannot help but feel that BUR had ulterior motives for this acquisition, such as to consolidate assets in order to make its debt load look less ominous, or to ensure it is valued as an operating business, rather than as a closed-end fund. BUR has issued $646.9 million of retail bonds, and yet has no credit ratings."*
>
> *Source: 2019-08-07 Muddy Waters Report.*

2. Caro-Kann Capital's Position

We consider the GKC acquisition in 2016 to be a smart strategic move. Plus, the acquisition was done at an attractive price. We do not share Muddy Waters' perspective that there was an ulterior motive to boost the balance sheet.

3. How Was GKC Acquisition Reported under IRFS?

As any asset manager, GCK was an asset light business. Under IFRS, Burford had to conduct a purchase price allocation. Burford paid $173M which included $13M of contingent equity consideration. Hence, this was the amount of consideration that Burford had to allocate. Not surprisingly, GKC did not have that many assets to allocate the purchase price to. After all, what assets do you need to run an asset management business? Not many.

As a result, the lion's share of the purchase price ($133M or ~80%) was allocated to the goodwill. Footnote 15 in 2016 Annual Report provides a detailed breakdown of the purchase price:

[48] This claim was not numbered by Muddy Waters. We will assign "number 9" to it as a matter of convenience. See page 4 of Muddy Waters 2019-08-07 Report.

15. Acquisition of subsidiary

On 14 December 2016, the Group acquired GKC Holdings, LLC ("GKC"), the parent of Chicago-based Gerchen Keller Capital, LLC. The Company has acquired 100% of the share capital of GKC.

GKC is a legal and regulatory risk focused investment manager registered as an investment adviser with the US Securities and Exchange Commission.

The amounts recognised at the time of acquisition in respect of the identifiable assets acquired and the liabilities assumed are as set out in the table below:

	$'000
Assets	
Intangible asset in connection with investment management income	39,666
Tangible fixed assets	402
Receivables	1,126
Cash at bank and in hand	469
	41,663
Liabilities	
Payables	(1,174)
Total identifiable net assets	40,489
Goodwill (Note 17)	133,011
Total consideration	173,500
Satisfied by:	
Cash	93,750
Loan notes	43,750
Equity consideration	22,500
Contingent equity consideration	13,500
Total consideration	173,500

We do not see how making an acquisition and recording a goodwill of ~$133M helped Burford boost its balance sheet.

We believe that the acquisition had a genuine and clearly articulated business purpose of entering the asset management business. It was a buy vs. build decision. Rapid growth of Burford's asset management division shows that it was a very good M&A transaction.

XIII. Claim #10: Burford Is "Arguably Insolvent"[49]

1. Essence of Muddy Waters' Claims

This is a punchline of Muddy Waters' report:

> *"BUR is arguably insolvent. If subtracting BUR's funded debt balance of $637.8 million from the adjusted capital base, there is only a $243.1 million cushion. However, BUR has future balance sheet litigation commitments of $708.2 million. Historically, approximately 85% of these commitments are eventually deployed, implying that BUR has an off balance sheet liability of $602.0 million. When looking at BUR's solvency through this methodology, BUR has negative equity of -$358.9 million relative to the adjusted capital base."*
>
> *Source: 2019-08-07 Muddy Waters Report.*

After twenty-three pages of one-sided interpretations, ***Muddy Waters has finally found a black cat in a dark room*** – the "insolvency" of Burford.

How did Muddy Waters get to that conclusion? Let's walk through the steps.

First, Muddy Waters took Burford's equity of ~$1.566B and removed all fair value adjustments of ~$686M and as a result arrived to the Adjusted Capital Base of ~$880M.

Second, Muddy Waters assumed that all debt of ~$637.8M becomes payable. Muddy Waters assumed that despite the fact that Burford management has thoughtfully created a maturity ladder: GBp 90M in August 2022, GBp 100M in October 2024, $180M in August 2025, and GBp 175M in December 2026. Why these bonds would become immediately payable is quite unclear and we wish Muddy Waters had explained the rationale for that.

After reducing the Adjusted Capital Base (*i.e.*, book equity minus fair value adjustments) by the total debt, Muddy Waters got to the cushion of $242M.

Third, Muddy Waters accounted for Burford funding commitments in the amount of $708M by applying a historical funding percentage of 85%. Thus, Muddy Waters concluded that Burford would need to fund $602M.

As a result of this math, Muddy Waters delivered its punch line: the funding commitments would lead to Burford's insolvency and the funding gap is ~$358.9M.

[49] This claim was not numbered by Muddy Waters. We will assign "number 10" to it as a matter of convenience. See page 24 – 25 of Muddy Waters 2019-08-07 Report.

Please see the table summarizing the math below.[50]

Muddy Waters' "Arguable Insolvency" Analysis

IRFS Book Equity	$M	1,768.4
3rd party interetss	$M	202.2
Burford's equity ex-3rd party interests	$M	1,566.20
Fair Value Gains	$M	686.0
Adjusted Capital Base	$M	880.20
Debt	$M	637.8
Equity Cushion	$M	242.40
Commitments	$M	708.20
Deployment percentage	%	85.0%
Expected deployments	$M	601.97
Funding gap	$M	(359.57)

Source: Caro-Kann Capital's analysis based on 2019-08-07 Muddy Waters Report.

2. Caro-Kann Capital Position

We find this analysis *sensational and incorrect*.

First, we already discussed that removing all fair value gains is incorrect.

Second, assuming that all debt (~$637.8M) becomes payable overnight is a product of strong imagination. Muddy Waters assumed this despite the fact that ***Burford management has thoughtfully created a maturity ladder***:

- ✓ GBp 90M bond maturity in August 2022
- ✓ GBp 100M bond maturity in October 2024
- ✓ $180M bond maturity in August 2025
- ✓ GBp 175M bond maturity in December 2026.

Why these bonds would become immediately payable is quite unclear and we wish Muddy Waters had explained the rationale in their report.

[50] Please note that there are small discrepancies in the Muddy Water's math and the table that we replicated based on such math. We attribute these discrepancies to rounding.

Third, Muddy Waters' analysis assumes ***cash outflows beyond imagination*** and ***ignores any potential cash inflows***. For example, some of the current investments are very likely to come to conclusion over the next few months and bring cash to Burford.

Fourth, Muddy Waters ignores Burford's ability to sell some of its investments.

Fifth, Muddy Waters ignores Burford's ability to syndicate its own deals by partnering up with other litigation finance providers instead of funding its solo. We want to be crystal clear: this is the matter of last resort and we do not envision it happening.

Not surprisingly, ***we strongly disagree with Muddy Waters' punchline***. ***There is no cat in the dark room.***

XIV. Burford Has Increased the Amount of Disclosure *Massively* Over the Years

In addition to our rebuttal of Muddy Waters' views about perceived "wrongdoings" by Burford above, we would like to discuss more subtle, almost behavioral elements of Burford and its management.

Normally, a company engaged in financial manipulation gives as little disclosure as possible. After all, the more details investors and short sellers have, the easier it will be to point out inconsistencies and inaccuracies in company's disclosures.

Does Burford fit this description? Not at all.

Over the past 10 years Burford has been increasing the amount of disclosure every year. One can go through annual and semiannual reports from Burford's inception to 1H 2019 Interim Report to see how much more detailed and – more importantly – useful information Burford provided.

The culmination of this increasing disclosure occurred in March 2019 when Burford provided a 7-page disclosure of returns for each matter: concluded, partially concluded, or ongoing.

How many companies do you know that provide as much disclosure about their business? We do not know many.

In fact, this increased disclosure resulted first in an unfavorable report by Canaccord Genuity issued on April 30, 2019, and Muddy Waters report. This is what Muddy Waters wrote:

> *"Just this year, BUR began publishing more detailed investment data. This data proves that BUR has been egregiously misrepresenting its ROIC and IRRs, as well as the state of its overall business".*
>
> *"It is only since BUR finally provided an investment data table in H1 2019 on its website that it has now become possible to analyze individual cases and understand how misleading BUR's presentation of returns is."*
>
> *Source: 2019-08-07 Muddy Waters Report.*

If Burford was indeed engaged in manipulating its metrics, why would management provide such a detailed disclosure? It seems highly illogical. I have heard a view that as Burford got bigger, investors demanded more capital and Burford was raising 3rd party money for its asset management business. As a result, Burford had no choice but to provide its voluminous disclosure of each litigation matter. We respectfully disagree with that assertion for several reasons.

First, Burford raised plenty of 3rd party capital, including its deal with a sovereign wealth fund *before* it provided its case-by-case disclosure.

Second, Burford could provide such detailed disclosure only to prospective investors into its third-party funds, including the sovereign wealth fund, on a confidential basis so that public market investors did not get that data.

Third, Burford does not need to issue equity.

Fourth, Burford has issued bonds on several occasions without having such a detailed case-by-case disclosure.

We tend to think that the only reason why Burford issued its case-by-case disclosure is because shareholders have been asking for it and Burford has a long history of meeting shareholders' demands.

That's why we disagree with Muddy Waters' statement.

> "By remaining listed on AIM despite being a midcap company, the company's disclosure requirements are lighter than they would be for the main board – and far lighter than they should be".
>
> *Source: 2019-08-07 Muddy Waters Report.*

Burford has provided investors with plenty of disclosure.

XV. Insider Sales

Muddy Waters correctly pointed out:

> "The CEO has sold a total of GBp 59.4 million of stock".
>
> *Source: 2019-08-07 Muddy Waters Report.*

That's true. We would *actually add* that CIO Jonathan Molot *also* sold approximately the same number of shares.

What Muddy Water did not mention, however, is that ***both CEO Chris Bogart and CIO Jonathan Molot still owned more than 8.5 million Buford shares each. Thus, each of their investment in Burford shares was worth ~GBp 130 million*** before Muddy Waters announced that it would publish a short thesis on an unnamed company.

While we never like to see insiders selling a substantial number of shares, we recognize that circumstances of this case are fairly rare. Yes, two founders sold shares and "cashed out" substantial sums of money. However, they still own plenty of shares that are worth even more. Plus, two founders have built Burford from nothing and most likely had the vast majority of their net worth in Burford shares. If they chose to get some level of diversification in March 2018, we will not blame them for that.

XVI. What Has Muddy Waters' Report *Really* Demonstrated?

Muddy Waters' wrote something that we agree 100% with. This is the direct quote:

> *"It is a fund that invests in an illiquid and esoteric asset class, which few investors can understand well."*
>
> *Source: 2019-08-07 Muddy Waters Report.*

Burford definitely invests in an illiquid and highly esoteric asset class. Indeed, ***very few investors can understand it well***. This is the exact reason why Burford shares and even bonds fell dramatically after Muddy Waters presented facts that we mostly agree with and its interpretations that we mostly disagree with.

Management has done an extraordinary job of educating investors about litigation finance in general and Burford's business in particular. Yet, this area is very complex, and many investors got easily confused.

While we used to feel quite indifferent to Burford's lack of a U.S. listing, the events of August 2019 have persuaded us that U.S. listing is a necessary step.

We hope that a NYSE or NASDAQ listing will attract the attention of more sophisticated investors whose research will be more thorough and understanding of Burford will be more profound compared to many legacy holders who sold Burford shares after Muddy Waters published their report. That's why ***we applaud management's decision to list on NASDAQ***.

Based on 1H 2019 Burford Interim Report we understand that management had been seriously considering such a U.S. listing, but Muddy Waters' report highlighted that it really is necessary.

XVII. Conclusion: We Do Not Find Muddy Waters' Claims Persuasive, Let Alone Conclusive of Burford's Improper Behavior

We have provided detailed explanations of why we do not find Muddy Waters' assertions and claims to be persuasive. Muddy Waters provided many correct facts. However, their interpretations are highly unusual and very much stretched. To put it simply, we disagree with Muddy Waters.

Ben Graham famously said that in the short run, the market is a voting machine, and the market definitely voted in the weeks after Muddy Waters published its report. But in the long run, the market it is a weighing machine. We strongly believe that the market will weigh Burford properly in the long run.

XVIII. Get in Touch

If you want to discuss Burford Capital, please get in touch with us. You may reach the author of this report at artem.fokin@caro-kann-capital.com or you can visit our website at www.caro-kann-capital.com. Thank you for reading.

Disclaimer

The presented views and analysis are an opinion of Caro-Kann Capital LLC. Caro-Kann Capital LLC and / or its affiliated entities are long Burford shares. Various factors may influence or factor into the analysis or the opinion. The author does not assume any obligation to update the analysis.