2021

Tomorrow's
Titans

the **hedge fund journal**

Introduction
Fifty Rising Stars

HAMLIN LOVELL

This is the sixth edition of our *Tomorrow's Titans* report; previous reports were published in 2010, 2012, 2014, 2016 and 2019. The format has been expanded from previous editions, which published fifty short profiles. This year, thirty-six managers have short profiles, and fourteen have extended profiles written off the back of interviews.

Increased appetite on the part of managers to give interviews reflects a generally optimistic mood around hedge fund performance and asset raising, notwithstanding some anxiety around Brexit and European fundraising for some UK-based managers.

The report highlights portfolio managers who are already leading managers in distinctive strategies – or close to becoming leading managers – with promising performance, the potential to grow assets, and in some cases with scope to further develop their strategies as they grow.

Nominations come from our extended network of readers, subscribers and contacts, including: pension funds; family offices; endowments; foundations; funds of funds; private banks and wealth managers; insurance companies; prime brokers; administrators; custodians; depositaries; law firms; accountancy firms; exchanges; technology providers, and others.

The geographic breakdown, with twenty-six managers in the Americas, nineteen in Europe, and five in Asia, is near to the split of industry assets, though we expect Asia may grow its share in future based on the buoyancy of launch activity.

There is naturally a bias to London and the New York tri-state area, but in the Americas, we also feature managers based in the Bahamas; Miami; Baton Rouge, Louisiana; Houston; Nevada and Los Angeles, as well as Montreal, north of the border in Canada. In Europe, locations include Athens; Amsterdam; Moscow; Lucerne; Stockholm and Vienna. In Asia, the featured managers are in Hong Kong; Singapore; Mumbai and Perth.

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Most of the managers – 45/50 – have launched their own management company, and most of those have done so in the past four years. Notwithstanding the Covid pandemic, eighteen launched in 2020, and two in 2021, as the industry has swiftly adapted to remote working. A few managers are about a decade old but took more time to develop a higher public profile.
A handful of them have launched funds with existing well-established firms, such as CIFC Asset Management; Serone Asset Management; Rockefeller Capital Management; Dalton Investments and Ambienta SGR. In some cases, these firms have also provided seed capital.

Assets, structures and strategies

Day one capital, as well as strategic and acceleration capital after launch, comes from dedicated seeders, such as Borealis Strategic Partners, Investcorp Tages, Stable Asset Management and Inception Point (which was itself started by a former *Tomorrow's Titan*, Keith Anderson). It has also come from hedge fund managers such as Fir Tree Capital and Harbert Management Corporation, and from fund managers who have become family offices, such as David Tepper.

Insurance companies, such as Austria's UNIQA Insurance Group, have seeded some funds. A handful of managers were seeded by family offices, which are not usually disclosed.

Investment structures are most likely to be Cayman, Luxembourg or Ireland private funds or managed accounts, but a few have launched with a UCITS fund as their first vehicle: such as Venkat Pasupuleti of Dalton and Markus Schanta of BlueBalance.

There is a wide range of assets under management: some managers have raised more than $500 million or $1 billion – in some cases from day one – while others might have started with as little as $20 million, using a third-party management company and outsourced service providers. Many have offered, or are still offering, discounted fees in founders' or early bird share classes. A few managers started off working with a regulatory hosting platform of some kind, before building out their own full scope management company.

Strategies represented include seventeen equity long/short; one equity market neutral; eleven credit; three activists; three event-driven; two fixed income relative value; two discretionary macro; one systematic macro; one relative value equity arbitrage; five CTAs or multi-strategy quantitative; two commodity and one index and event arbitrageur.

Irrespective of whether managers are discretionary or quantitative, many are keen to emphasize their factor awareness – and sometimes their factor neutrality – especially after the violent factor rotation seen in 2020.

TMT equity long/short, and distressed credit

Most of the strategies are discretionary. The key strategy clusters of launches include equity long/short including TMT, and credit, event driven, special situations and distressed. There is a lot of enthusiasm about the post-Covid opportunity set for a new distressed debt cycle. Many managers integrate ESG into their investment process to a greater or lesser extent, and some of the strategies are explicitly ESG-oriented, including Ambienta X, Thomist Capital and Longchamp Dalton India UCITS Fund.

In the quantitative space, statistical learning and machine learning are areas of growing interest. At least six managers – ActusRayPartners, Blueshift, Leibniz, Rosetta, Manteio and Bayforest – are using some degree of machine learning but all apply it differently in their own ways, and only one of them claims to be applying 100% deep reinforcement learning.

Generally, the quantitative managers have previously worked for larger quantitative managers, such as AQR, Man Group, Tudor Capital Europe, and Credit Suisse Asset Management, though one of them – Blueshift – came from a proprietary trading firm and another – Rosetta – was previously at an investment consultant and OCIO. Some firms, such as ActusRayPartners, are in a sense hybrids between discretionary and quantitative while others such as Haven Cove and Shikuma Capital contain both discretionary and quantitative sub-strategies.

The largest source of discretionary managers seems to be the large multi-billion managers, such as Millennium Capital Management, Citadel, Point72, Och Ziff and Appaloosa, though some managers have emerged from investment banks such as Goldman Sachs. One manager, Tommaso Mancuso of Shikuma Capital, was previously at pension fund manager Hermes. Another, Bluebell Capital Partners, has morphed from running an advisory firm counselling activists to become an activist itself.

A handful of managers have worked for managers who have featured in previous *Tomorrow's Titans* reports, and there are some serial launches.

As hedge fund managers are sometimes converging with other alternative investment strategies, we have an alternative credit group, Alpha Blue Ocean, providing financing for smaller public companies, and there is also some crossover with private equity. One manager, Fabio Pecce, joined a private equity firm, Ambienta, to launch a liquid strategy while another, Acer Tree, was backed by a private equity firm (Cabot Square Capital). A handful of managers cross over into private equity investing, separately from their public markets' strategies, such as Christian Vogel-Claussen of

Alanda Capital Management, and Eduardo Costa of Calixto Global Investors.

The report features only four women, which is regrettable, though it is worth pointing out that our *50 Leading Women in Hedge Funds* report which has run since 2009 has showcased several hundred senior women including portfolio managers and investment professionals.

The majority of launches we have tracked are still all-male; some of the nascent female start-ups have not reached a level of maturity, in terms of organization or track record, where we can realistically include them, though we are keen to monitor such early-stage managers for the long term, potentially for this and other reports.

Andrew Alexander

Chief Executive Officer and Chief Investment Officer
ActusRayPartners Limited
Hong Kong

Andrew Alexander co-founded ActusRayPartners in 2019 with Raymond Chan and Patrick Cheung. There is a collaboration agreement with Sun Hung Kai & Co which provides longer term assets under management, working capital, office space and support services, all in exchange for a revenue share. ActusRayPartners employs a discretionary probabilistic investing process. There are two parts to the process: (i) a quantitative base, and (ii) discretionary adjustments. The quantitative base uses fundamental, sentiment, technical and alternative data, and employs advanced statistics, natural language processing, machine learning and artificial intelligence techniques. The discretionary work focuses on addressing challenges with purely systematic processes and is not fundamental or macro driven. Alexander was previously Senior Managing Director and Head of Portfolio Management at Macquarie Quantitative Hedge Funds, where the founders previously helped manage the Macquarie Asian Alpha Fund and the Macquarie European Alpha Fund, which had combined peak strategy assets of $3 billion. Alexander previously formed a joint venture with AXA Investment Managers and earlier was a partner at three Asian hedge funds: LIM Advisors, Asia Debt Management and Pacific Group. He is a Fellow of the Institute of Actuaries of Australia and holds a Bachelor of Economics degree from Macquarie University in Sydney.

Eiad Asbahi

Founder, Managing Partner and Portfolio Manager
Prescience Point Capital Management
Baton Rouge, Louisiana

Eiad Asbahi founded Prescience Point in August 2009 to pursue an opportunistic long/short equity strategy. Asbahi utilizes activism to catalyze investments on both the long and short sides. For example, Prescience Point spearheaded a proxy fight at the MiMedx Group in 2019, which led to six new directors and the appointment of a new auditor. Most recently, in April 2021, Prescience Point ran another proxy contest at MiMedx that nominated four more directors including Asbahi. On the short side, the firm has had notable successes uncovering fraud and publishing research leading to executive resignations, SEC investigations, and eventual de-listings. In 2017, Prescience Point published a report on the trucking firm Celadon Group, which is now defunct after Asbahi identified numerous red flags including fraudulent accounting practices and nefarious related party transactions. The firm manages approximately $150 million through the primary long/short fund and a dedicated vehicle invested in MiMedx. Since inception, the strategy has annualized over 24% per year with low correlation to US equities. Prior to founding Prescience Point, Asbahi was an investment analyst with several hedge fund managers in New York: Sand Spring Capital, Cohanzick Management and later Kinderhook Partners. Asbahi has an MBA and a BS in Microbiology from Louisiana State University. He is a CFA Charterholder.

Peter Avellone

Managing Partner and Chief Investment Officer
Cartenna Capital LP
Stamford, Connecticut

Peter Avellone launched Cartenna Capital, a long/short equity hedge fund, in April 2020. Cartenna operates a lower-net exposure strategy focusing on industrials and consumer cyclical sectors. The fund uses a rigorous bottom-up process and overlays a deep understanding of industrial cycles to identify investment themes and ideas. Avellone and his team utilize a contrarian, catalyst-driven approach to achieve uncorrelated, strong, risk-adjusted returns. Cartenna spends approximately 60% of its research time on the short side of the portfolio working to differentiate returns with short alpha. The strategy returned 18.9% net of fees in 2020, averaging 12.4% net exposure with a Sharpe ratio over 3.0. Cartenna has a heightened awareness of style and factor risks but does not operate a factor-neutral strategy. The fund seeks to preserve capital with closely monitored risk and drawdown limits. Avellone has over 15 years of industry experience having previously managed teams at Millennium Management, Citadel LLC and Point72. Avellone's first buyside role was at a long/short real estate focused hedge fund within Angelo Gordon & Co. He began his career in investment banking at Lehman Brothers, and has a BA in Economics from the College of Holy Cross in Worcester, Massachusetts.

António Batista

Managing Partner and Chief Investment Officer
Caius Capital LLP
London

António Batista co-founded Caius Capital with COO Will Douglas in October 2016 and the firm manages over $1 billion as of January 2021. The strategy invests long and short in distressed and special situations relating to leveraged capital structures of companies, banks, sovereigns and asset-based businesses. Exposure is mainly in Europe but also opportunistically in emerging markets and the US. A wide variety of instruments, ranging from post-reorg' equity to bonds, loans, asset-backed paper and liquidation claims, can be traded based on deep, fundamental bottom-up research. The strategy can hedge unwanted commodity, currency or macro risks, and can go net short. Performance has annualized in low double digits between inception and December 2020 with a high hit rate and a high win-to-loss ratio. Batista believes that we are facing the best opportunity set for distressed investing since the GFC, arising both from restructurings in traditional corporate sectors as well as from the complexities inherent in the banking and energy sectors. Batista was previously a partner and portfolio manager for European distressed credit at Och Ziff, and earlier worked at Goldman Sachs. He has an MSc in Econometrics and Mathematical Economics from the London School of Economics and an MSc in Economics from the University of Bonn.

Martin Beck

Founder and Chief Investment Officer
Astaris Capital Management LLP
London

Martin Beck founded Astaris in 2019, initially raising just under $100 million. Assets under management are now approaching $200 million, with the increase being attributed to both strong performance and additional capital raising. The strategy, which invests in European events, takes long and short positions across the capital structure to exploit mis-priced, stressed/distressed and special situations and generated gross returns of 35% in 2020. Beck sometimes takes an activist stance; in August 2020, his public proposal secured a substantial coupon and consent fee increase for bonds issued by travel group TUI. The proposal also paved the way for an early repayment of the bonds at above par. He envisages pursuing more corporate activism as the firm grows. Prior to founding Astaris, Beck worked for Centerbridge Partners and before that was a founding partner of Sothic Capital Management, where his strategy annualized at 18.7% (gross) over 8 years. Sothic's former Head of Operations, Geoffrey Haffner, is now COO at Astaris. Beck began his finance career at JP Morgan's principal investing business in 2004, focusing on event driven distressed debt and special situations. Two former colleagues from JP Morgan and Centerbridge, Björn Bischoff and Robert Pohlhausen, have joined Astaris as founding partners. Beck holds MBAs from the European Business School and the University of Pittsburgh, Katz Graduate School of Business.

Giuseppe Bivona and Marco Taricco

Co-Chief Investment Officers
Bluebell Capital Partners
London

In 2019, co-CIOs Giuseppe Bivona and Marco Taricco founded Bluebell Capital Partners, along with Chairman Francesco Trapani, to transition their track record in advising on activist campaigns at Bluebell Partners into their own investment strategy. As advisors, the team worked alongside the likes of Elliott and JANA Partners on campaigns such as Tiffany, Ansaldo STS, TIM, Monte dei Paschi di Siena, NKT and Mediaset. In 2020 Bluebell were involved in several high-profile and successful campaigns, pursuing both long (i.e., Vestas, Mediobanca) and short (i.e., Cineplex) strategies. In 2021, Bluebell called for and obtained the removal of Danone's CEO, Emmanuel Faber, and has also questioned the independence of Unicredito's Chairman-designate, Pier Carlo Padoan. ESG forms one of Bluebell's key value levers. In addition to a thoroughly articulated ESG framework and policies, Bluebell also commits to undertaking one "One Share ESG campaign" per year, where with just one share they engage with a company to improve on their E or S practices. This may evolve into a fully sized position, either long or short, depending on the evolution of the campaign. Its first one is focused on the waste disposal practices of Belgian chemical group Solvay, which remarkably is awarded a triple A ESG rating by MSCI, one of the main rating agencies. Bivona previously worked for McKinsey, Morgan Stanley, Lehman Brothers and Goldman Sachs; Taricco at Goldman Sachs, Morgan Stanley and JP Morgan. Trapani was formerly the CEO of Bulgari and led its IPO and sale to LVMH. Bivona and Taricco both have MBAs from Columbia Business School, where they met. Bivona has a degree in Mechanical Engineering from the University of Rome; Taricco has a degree in Business Administration from Turin University and is a qualified chartered accountant.

Michael Cash

Founding Partner and Chief Investment Officer
Manteio Capital
New Jersey and Athens

Michael Cash co-founded Manteio with CEO Peter Christodolou and CTO Justin Yang, former colleagues from Credit Suisse Asset Management's (CSAM) Quantitative Trading (QT) group. Manteio pursues global artificial and liquidity intelligence strategies targeting high Sharpe ratios and uncorrelated alpha. Data science and proprietary AI and machine learning are used to trade across asset classes – sovereigns, municipals, mortgages, corporate debt, interest rates swaps, single stocks and ETFs – rotating around styles and swiftly adapting to changing market regimes. The founders believe that the market climate is opportune for liquidity provision; high turnover relative value fixed income yield curve and mortgage arbitrage trading; next generation statistical arbitrage; and debt and equity capital markets strategies. Cash was previously Global Head of Fixed Income at CSAM's QT group. He was earlier CIO of Westfield Research and founded other hedge fund firms. Prior to that, he worked for Credit Suisse proprietary trading running US rates trading in the Global Arbitrage Group. His finance career started trading bonds for Salomon Brothers. Cash has an MBA from Columbia Business School and a BS in Computer Science from the University of Stony Brook. Manteio means 'oracle' in ancient Greek.

Don Casturo

Founding Partner and Chief Investment Officer
Quantix Commodities
Greenwich, Connecticut

Don Casturo co-founded Quantix in 2018. The Quantix Commodities Alpha strategy, which runs more than $700 million, is a discretionary relative value approach based on index arbitrage, which trades inefficiencies that arise from passive investment in commodities. Quantix estimate that passive investment in commodities via index swaps, ETFs and index futures taken together could be as high as 40-50% of open interest. The Quantix strategy, which takes long and short positions across commodity futures including energies, precious and base metals, and agriculturals, has been very lowly correlated to equities, and other hedge fund strategies. The strategy, which can use options as well as futures, takes account of factors such as futures rolls, curve slope, seasonality, deliverable criteria, and time spreads. The models are regularly revised every few months. Casturo was formerly Global Commodities COO and Head of EMEA Commodity Trading at Goldman Sachs, where he and the other two founding partners – Daniel Cepeda and Tom Glanfield – sat on the Commodities Risk Committee. The trio developed enhanced index and alpha swap strategies, which outperformed conventional commodity indices. Casturo has an MBA from Duke University and an MS in Mechanical Engineering from Stanford University.

Michael Fine and Alexander Brown

Founding Partners and Chief Investment Officer and Chief Executive Officer/Head of Research and Trading
A6 Capital Management
New York

A6 Capital Management launched in October 2020 with over $85 million and now manages more than $100 million, including an anchor investment from Borealis Strategic Capital Partners in Chicago. A6 is distinguished by taking a hedged approach to stressed and distressed corporate credit investing, which entails trade structuring with idiosyncratic hedges. A6 also operates within the more liquid end of the distressed space and seeks shorter term catalysts within 12 to 18 months. A6 focuses on scalable multi-billion-dollar capital structures, where they can hedge investments, reduce tail risks, and run a more concentrated portfolio of best and highest conviction ideas. Combining derivatives and stressed/distressed credit in a coherent, repeatable strategy that engineers asymmetric payoff structures is fairly uncommon. A6 sometimes pursues credit activism, and the managers have previously led restructurings and liability management exercises in a multitude of industries and across the capital structure. The founders previously worked together at LibreMax Capital, where Fine was Head of Corporate Credit and Brown was Director of Corporate Credit; LibreMax founder Greg Lippman featured in a previous edition of this report. Fine earlier worked at Carlson Capital, Patriarch Partners and Gracie Capital. Brown previously worked in distressed investing for Credit Suisse on the buy side and sell side. Fine has a BCom from McGill University and Brown has a BA in Economics from New York University.

Philip Giordano

Founder and Chief Investment Officer
Livello Capital
New York

Philip Giordano launched his flagship opportunistic credit strategy in May 2020 and has delivered meaningful outperformance to his investors in the fund's first year of trading. Grounded in fundamental research with a top-down markets-driven discipline, the firm opportunistically deploys capital across high yielding bank debt, non-investment grade corporate credit, trade claims, and rescue finance/direct loans focusing on distressed and deep value special situations where structural *(Continued on page 20)*

Founder and CIO
Balchug
Moscow

David Amaryan

An innovative event and value investor

David Amaryan's Balchug strategy holds no more than 15 positions, with the highest conviction and most liquid of them sized up to 15% of gross exposure. The strategy has annualized at over 16% since 2010. Since launching a fund in January 2019, performance has accelerated to 90% over the past two calendar years, including an advance of 23% in 2020.

Balchug is broadly a value and event driven strategy picking stocks often outside the big index names and emphasising emerging markets, but 2020 illustrates its tactical trading, risk management and wide range of influences, with the US equity market playing an important role. Born in Yerevan, Armenia, Amaryan won a scholarship to study in the US aged 14 and briefly worked for Alliance Bernstein in growth and value equity in New York before returning to the Commonwealth of Independent States.

The strategy has tended to be long-biased but can become tactically more defensive at times. "Over the years we have been getting better at managing risk and volatility, which includes using some mainly exchange traded derivatives," says Amaryan.

Balchug turned cautious in February 2020, hedging part of its Russian equity exposure with a triple leveraged short ETF and a Russian oil company, and going short of some Macau-exposed casino operators.

The strategy did not go net short overall however, and swiftly rebuilt risk as markets crashed because Amaryan had confidence in economic, commodity market and equity market recoveries. He doubled down on longstanding favourites such as oil firm Tatneft and bought into several US recovery plays in travel, hospitality, retail, real estate, financials and energy. By mid-March, Balchug was 150% net long and Amaryan admits that this was a week before the market trough. By late April, some stocks had appreciated 50-60% and he top-sliced exposures: "With the benefit of hindsight, of course some profits were taken too early, but we needed to stay within risk limits. A few of these US names are still held, with Devon Energy having tripled from the lows".

Russian equities

Selected Russian equities have been a more enduring fixture. Over the years Amaryan has held either long or short positions in most constituents of Russia's RTS index, and he could contemplate running a pure Russia mandate. Amaryan has for some years believed Russian equities are undervalued: "Russian equities are at a historically high valuation discount to emerging markets, and I am constructive on the outlook for commodity prices. I see oil around $70 a barrel, based on OPEC supply discipline and recovering demand creating a deficit. My favourite oil stock, Tatneft, is a very lean and well-run company, which pays out nearly all its cashflows as dividends. It is minority owned by the Tatarstan government so nobody will take it away. This was one of the few companies we did not sell in March 2020 – we doubled our position as it dropped by 50-60%. Steel making new highs at $400 a tonne has already surged ahead of forecasts and some steel firms offer dividend yields of 20% or 25%".

Russian equities in general offer some of the highest dividend yields, which have grown from 1.5% some years ago to a forecast level as high as 7 or 8% this year. State ownership stakes in some firms is a positive at least in terms of making dividends more stable and predictable. Amaryan estimates that dividend income has contributed over 10% of his historical returns.

Dividend yields are also one driver of domestic retail inflows since local deposit rates have not only declined but are also now taxed; the number of retail brokerage accounts has increased from 4 million to 11 million, and substantial Russian household savings in bank deposits could be shifted into equities. There are also growing institutional flows from pension funds, which have very low equity allocations of 6% that could easily grow by multiples up to 40%. These domestic inflows could even counterbalance or outweigh some scenarios around sanctions.

Sanctions

Amaryan is of the opinion that sanctions under the Biden regime were probably priced into equity prices and is perplexed to see Russia underperforming its emerging markets peers by 20-30% amid a commodities boom. "We could see 30-40% upside in Russian equities, based on history when the threat of sanctions has put more pressure on the market than the sanctions themselves. During this period of uncertainty, the market underperforms, expecting the worst. Our observations show that when the sanctions are announced, this overhang is removed, and the stocks advance. This has been confirmed by the market reaction to the US sanctions announced in April 2021, which met our expectations. The worst part of it was the restriction on US institutional investors buying future Russian sovereign debt on the primary markets. This does not restrict them from buying it on the secondary market."

However, he is closely monitoring the situation – and has cautiously avoided some banks that might be vulnerable to ratchetting up of sanctions. "We will be watching carefully how the two countries behave. There are no illusions of the relationship improving drastically, but we hope, that it will be more constructive and predictable. A lot will depend on the meeting between Putin and Biden, which should take place in Austria soon. If the situation in Ukraine/Donetsk worsens or, God forbid, Navalny passes away, the next round of sanctions will be much harsher and will hurt the market much more."

Event-driven trades

Balchug does not need to observe any sanctions, but has sometimes taken advantage of sanctions-related selloffs, which are one example of event catalysts, along with debt restructuring, management change, index inclusion, increases in dividends or changes in dividend policies. Event driven situations can also include corporate events, such as M&A or spin offs, as well as exogenous events such as natural disasters, force majeures or political and regulatory developments.

Arrival of electric commercial vehicles

Amaryan's event driven book can also accommodate some disruptive early-stage growth companies. One example is electric commercial vehicle maker, Arrival, a UK company with a Russian CEO and Russian roots, which was taken over by US listed SPAC, CIIG Merger Corporation. "Within 10 years a big share of cars is going to be electric, driven by governments and consumers. We analysed this firm two years before its IPO and liked it very much. We feel that Arrival should deliver most of what it has promised, in terms of key driver orders and micro-factories. The strategy is scalable. Of course, there is a lot of hype, but what is most important is what is left after the dust has settled."

"We did not get an IPO allocation but bought soon after it floated via a SPAC. We reduced the position above $30 based on our risk management rules and have recently been buying it again. The stock has had a pullback as the market does not understand the story. The banks looking at it see 100% upside, while some management and smaller investors reckon it could be a ten-bagger up to a $100 billion valuation. We think it could be a 50 billion company, implying 400% upside. The fact that it is a UK company is a plus – there would be country risks if it were based in Russia".

Niche biotechs

Biotechs are another key group in Amaryan's event-driven growth category. Moderna was bought well before its vaccine was approved. It was one of the first to announce a vaccine but was not in fact a binary bet on approval since the company is developing treatments for a variety of diseases. The stock has roughly tripled since Amaryan bought.

He has also researched a pool of 20-30 specialised and promising biotechs. One example is TG Therapeutics, which treats a special type of leukemia, and hopes to get approval for a multiple sclerosis treatment. "There is little competition and TG's therapy could be better than existing treatments. We see 100% upside. We are also monitoring stocks involved in immunology and gene therapy."

Deep research

The private equity style research and due diligence process used to generate these innovative ideas includes extensive channel checks including traditional methods and some extra research: "We like to dig deep into the prospects of the company and sector, talking to managers and regulators at all levels. We might analyse a company for months and can pay attention to small things. Once when an analyst put coverage under review, we judged this was a positive signal because the investment bank was most likely to become an adviser. We recently shorted a Russian miner based on environmental issues and a mine flood that affected 30% of output. We sent an investigator to the region to quantify how long it would take to reopen the mine".

Amaryan has occasionally been invested in firms that were targeted by activists and those seeking a boardroom coup, however he has not played an active role in these situations.

A broad mandate

Public equity exposure has historically been the main asset class, but the mandate is potentially broader: "We could invest up to 20% in pre-IPO and see an interesting pipeline of offerings in Russia, including both privatisations and flotations from private equity companies. We have good relationships with local brokers including former colleagues. Secondary private offerings already contributed to returns in 2020 as discounts were quickly repriced".

Elsewhere in emerging Europe, Amaryan has connections in Turkey and is keeping an eye on bank stocks there but is not ready to invest yet given the authoritarian and unpredictable politics. He has had exposure to some London listings of frontier market companies, such as Kazakstan's Kaz Minerals. Balchug is monitoring a range of other local frontier equity markets in and around the CIS: Ukraine, Armenia, Georgia and Uzbekistan, though their equity markets are not yet liquid enough; some 75% of the Balchug book can be liquidated in a day, and there are also limits on how much liquidity risk is taken with the rest.

Balchug can invest into commodities or sovereign or corporate debt, though with a maximum of 15 positions there is a high bar to compete with equity holdings. Criteria include upside of at least 50%, combined with limited downside: "Credit will never be plain vanilla, there has to be some special event," says Amaryan.

Firm assets are $250 million, and the client base is mainly ultra-high net worth individuals and family offices, some of whom Amaryan met while working in private banking at Citigroup, and on the equity trading desk at Troika Dialog, Moscow's biggest investment bank. Many investors have been with him from the start, and he has drawn inspiration from some highly successful clients. The strategy was applied to managed accounts for 8 years, reflecting client preferences, before launching a Cayman-domiciled fund run pari passu. The fund, which has assets around $50 million, is now raising assets globally, and Balchug contemplates opening offices in London and New York over the coming years to complement its Moscow and Yerevan offices. Fund fees of 1% management and 15% performance are competitive, given the return history.

Though the strategy is creative, mid-2021 themes could re-emphasise the enduring approach: Amaryan anticipated the shift from growth to value investing in late 2020, and he now envisages a longer period of value investing and emerging markets equities being in vogue.

Co-Founder, Head of Investments
Rosetta Analytics
Minden, Nevada

Julia Bonafede

Deep reinforcement learning and next generation alpha generation

Julia Bonafede co-founded women-led firm Rosetta with Angelo Calvello to disrupt active asset management. Since 2015, Rosetta has rolled out four live investment strategies based on applying advanced AI and deep reinforcement learning (DRL) to liquid markets. "DRL is such an early-stage technology that investors are only just starting to see the benefits of it. In other industries such as robotics and healthcare it is already widely used," says Bonafede.

It is the culmination of the accelerating evolution of quantitative investing which Bonafede witnessed over 24 years at investment consultant and outsourced CIO, Wilshire Consulting, which during her leadership had over $1 trillion of assets under advice. "I saw quant develop through two lenses: I evaluated many asset managers and used multi-factor risk models to monitor manager styles. The earliest quant approach was indexing, followed by style investing with tilts similar to Fama French factors such as size, value and growth, which grew into iterations of over 100 factors including currency, country, industry and fundamentals. Then came smart beta, with a more rules-based approach, and more active systematic bets. Now AI lets the models derive relationships directly from the data, rather than from screened behavior identified in academic research."

Rosetta believes that its technology has more accurate predictive power than traditional quant, but also recognizes that it is harder to explain. "Many investors' comfort zone is a 50-year-old linear regression equation. The name Rosetta is a start towards explaining the approach, since a Rosetta stone translates pictures or images into languages – and neural networks can turn all sorts of data into actionable signals," says Bonafede.

DRL can however cause confusion because so many asset managers are talking about machine learning, though they may not be applying it holistically to investment signals, if at all, according to Calvello, who previously co-founded Blue Diamond Asset Management AG and Impact Investment Partners AG: "It takes a certain type of talent to create DRL models and most people working at asset managers do not hire those with the right background. It is hard to do this, and many asset managers will not take the risk. Why would they invest the time and money when they already have good profit margins?" Bonafede has also heard scepticism first hand: "Many managers tell us they are not using deep learning and DRL, and this even includes some managers who have published on it academically".

Managers may be using machine learning for one or more of operational routines, trade execution, portfolio construction and signal generation, but it may only be a fraction of a process, and they may be diluting it by prescriptively defining the framework in which the AI is used.

Letting the data speak

Rosetta is 100% AI in terms of building autonomous algorithms that let the data speak, but the approach is not entirely "unsupervised". "Our end-to-end learning models ingest carefully assembled data sets and use powerful deep reinforcement learning to create investment signals and allocate between assets. The signals are robust and persist through changing market cycles. By employing deep reinforcement learning our models successfully allocate risk to achieve optimal market exposure to maximize return. Risk of loss is a first order consideration rather than a second order constraint," says Bonafede. For instance, Rosetta exercises judgment to select a variety of technical/price/volumes data; fundamental economic data such as bond yields or stock and sector level data, and alternative data, with inputs that vary between models and markets. "We define the data that feeds into the models and define the output as the optimal allocation of risk capital. What we do not define is the relationships between the data and the signals," says Bonafede. These relationships may not make any intuitive economic sense or fit into other established frameworks such as behavioral finance, or map onto a factor zoo determined by humans. "If you need to establish the relationships as priors, the model will only find those. A neural network determines the optimal system, which could be based on millions of parameters, identifying which relationships matter, adapting and learning. It could discover totally new relationships and more often than not does. It is designed to capture non-linear relationships which minimize errors and expand to capture returns more robustly," says Bonafede.

Adaptive models relishing volatility

"It also adapts faster to changing environments," says Calvello. For instance, Rosetta's models performed very well in March and April 2020. "After the equity market peak on February 23rd, the models took another two weeks to understand the market before generating more active trading decisions. We were then up over 22% in March 2020 and over 12% in April 2020 with active trading almost every day," says Bonafede.

The Covid crisis shows that Rosetta's models have performed well in higher VIX volatility index regimes. "This behavior was not by design but is rather part of the systems' risk management properties. Their sizing varies as conviction in signals gets stronger or weaker. The DRL model make decisions to maximize reward, and penalties for an incorrect decision are weighted many magnitudes more heavily than reward," says Bonafede. This borrows from autonomous driving, which some of Rosetta's scientists have worked on, where there are huge penalties for errors.

In contrast, some other strategies dubbed as "machine learning", had their worst ever performance in March 2020, illustrating how similar branding labels can bely very different approaches: "Our sense is that some other managers are using a weaker version of machine learning, or are using it to augment other more traditional quantitative techniques. Part of the problem is that traditional quantitative techniques can also come under the machine learning umbrella, which now includes anything rules-based outside passive investing," says Calvello.

Uncorrelated and differentiated

Rosetta is doing something different even within the narrow space of funds that claim to be using machine learning and is also distinguished from other alternative strategies. Rosetta's returns generally do not have consistent correlation to other hedge fund strategies or traditional asset classes. Patterns of correlation fluctuate over time and vary with market regimes. For example, the average correlation of Rosetta's RL One S&P 500 long/short strategy has been near zero, but it has ranged between about +100% and -89%. Rosetta is also somewhat longer term than some quantitative strategies. Though AI is sometimes associated with high frequency trading and split-second trade execution, Rosetta's strategies are lower turnover.

Model R&D and evolution

Rosetta took over four years to develop its latest models. Rosetta's first live strategies in 2017 were two first-generation deep learning models to produce directional signals. Rosetta defines deep learning as a machine learning algorithm that uses deep neural networks. The seed investor, a US endowment, wanted them traded on a binary basis, with deep learning one either 100% long or 100% short S&P 500, and deep learning two either 100% long S&P 500 or in cash.

In May 2020, Rosetta rolled out its next generation of live strategies, adding reinforcement learning, which created totally different models that also allow for variable position sizing. "Deep learning is great at detecting relationships or clustering, but not at allocating or optimizing. To draw analogies with autonomous driving, you might use deep learning to identify an object in front of you, but would need reinforcement learning to slow down, speed up, or turn right," points out Bonafede. Rosetta defines DRL as algorithms that learn to maximize reward through trial and error, and map situations to actions. These systems can also cope with larger volumes of more complex data, including non-traditional data.

Rosetta's RL One Strategy, applying DRL to trading the S&P 500, has made 18.27% between May 2020 and April 2021, with a standard deviation of 12%. Their DRL strategy trading ICE European Union Allowance (EUA) futures contracts and related instruments has made 28.26% over the same period with volatility of 19%, less than half that of the underlying market.

Backtesting and training

"So far, the live performance has surpassed the back test, but we are aware of the potential for alpha decay," says Bonafede. The term "back-testing" more naturally describes a static model than an inherently adaptive one. Rosetta uses decades of what it calls "training data", with out-of-sample models applied to unseen data, and various techniques used to generalise the model, and determine the level of learning out of sample. "Where data histories are shorter, for newer markets, techniques such as transfer learning can be used to augment gaps in data. We did actually have enough data for EU carbon allowances, which are heavily influenced by regulation, and have quite different liquidity and data inputs compared with our S&P 500 model," says Bonafede. This relatively new asset class has been of interest to the duo for some time: Calvello founded the *Journal of Environmental Investing* in 2009, long before ESG investing became a mainstream focus.

Institutional infrastructure

As well as honing and refining its models, Rosetta has invested in building a scalable, institutional quality operational and trading infrastructure, and team. "This includes computer power that adds up to 43,000-man hours or 48 years of compute time. Data terabytes are not quantified because our edge comes from algorithms not volumes of data," says Calvello. "We are six people but have the infrastructure of a 100-person organization. We started with a blank slate: we needed to hire special talent (and compete with entities such as Google, FB, NASA, NYU, etc., for this talent); build proprietary IP from the ground up; build an industrial-quality infrastructure that would support rapid experimentation and efficient cycling; build an institutional-quality operational structure (because we are a fiduciary); build a trading operation; register as a CTA; vet and hire vendors (fund admin, FCMs, etc.)," says Bonafede.

The team includes four experienced and talented machine learning scientists and engineers who have all worked outside the investment and finance industry, solving machine learning problems on a vastly different scale. From the start, Rosetta has also had an experienced advisory board of six allocators, asset managers and academics, who are used episodically as a sounding board for ideas. They include Erik Valtonen, former CIO of Swedish public pension fund AP3.

Growth strategy

"We were very unusual for a startup in that we started de novo and raised money from an asset owner, not from venture capitalists," says Calvello. The firm received initial operating capital from Verger Capital Management (an OCIO made up of the former Wake Forest University endowment management team). "We are talking to other potential strategic partners," says Bonafede.

Rosetta manages $19 million as of May 2021 and discounted fees are available for founders' share classes. "We have created much more nimble strategies, that are scalable in the deepest markets. I think we focus on what we have," says Bonafede.

Rosetta advisory board member, Dr Elisabetta Basilico, sums up the challenge of growing a disruptive and highly innovative strategy: "There is a trade-off between explainability and accuracy. The big question facing investors and advisors is whether to invest in AI based strategies because they are likely to be the most accurate but the least explainable".

Jonathan Bowers, Founder and CIO and
Sven Olson, Founder and Head of Research
Acer Tree Investment Management
London

Jonathan **Bowers** + *Sven* **Olson**

Navigating European credit complexity

(L-R): Sven Olson and Jonathan Bowers

Jonathan Bowers co-founded Acer Tree with Sven Olson, Sasha Vlahcevic, Philip Grose and Askin Aziz, re-uniting a group who began their careers together at Deutsche Bank and Bankers Trust in the 1990s in the formative years of Europe's leveraged finance markets. "The ethos was return of capital, making sure you get your money back, and we developed really good, disciplined methods to squeeze targeted returns out of investments. Asset coverage and cashflows rather than credit ratings are what matter," says Bowers. "Deutsche Bank was one of the top high yield and leverage loan underwriters through the period and we see complex credit stories recurring again and again," says Olson. "Acer Tree is the culmination of our 25 years of shared DNA in credit," says Bowers.

The team have been active in leveraged finance through volatile periods including: the LTCM/Russia crisis in the late 1990s, the dotcom crash and the early 2000s recession, the GFC, the European debt crisis and now Covid. "I co-founded CVC Credit Partners, and was responsible for a performing credit business, founded a credit opportunities fund and an LSE listed fund," says Bowers. "We ran similar strategies at Castle Hill," says Olson. The other three founders previously worked at Observatory Capital Management, Luxor Capital Group and Camares Capital.

"We have a strong network of buy side, sell side and corporate contacts," says Bowers. "We have complementary skillsets in underwriting, researching, structuring, trading and portfolio management. The group's collective skill sets cover the full range of credit instruments including loans, bonds and derivatives," explains Olson.

Europe's public credit markets have grown enormously over the past 20 years. "Leveraged finance markets were in their infancy in the late 1990s with few LBOs and only really started growing after the early 2000s recession, fueled by growth in the institutional credit markets," recalls Bowers. Acer Tree's strategy covers an investment universe that has grown to approximately €2 trillion and runs the gamut from the BBB end of investment grade to high yield, leveraged loans, structured credit and the liquid stressed/distressed markets. The universe includes a growing volume of fallen angels as the number of firms downgraded from investment grade to high yield ballooned in 2020 to €80 billion. There is also plenty of turnover: "Companies continue to do large debt financings, both in terms of fresh capital, and refinancing," says Bowers.

Acer Tree's first and flagship strategy, Acer Tree Credit Opportunities Fund (ATCOF), is multi-disciplinary: its largest sleeves have been opportunistic and performing credit, but it also invests in a variety of event-driven, relative value and capital structure arbitrage strategies, and some structured credit given the insight gained from having managed CLOs. The fund also employs both single name shorts and index hedges. "We follow all sectors but have special expertise in several sectors including basic materials, TMT and energy. There are limits on industry and single name concentration with the portfolio running moderately diversified," says Bowers.

All weather opportunities

ATCOF's launch in June 2020 happened to coincide with the Covid crisis but had been in the works for much longer. "This is a through the cycle, all weather fund. Given the monetary and fiscal stimulus, we expect Covid could lead to slightly higher defaults for longer but not a big spike. Pre-Covid, we were expecting some increase anyway because it came at the end of a long economic up-cycle, and the real question now is whether companies can de-lever and grow back into their balance sheets," says Olson.

The return target of 10-14% is expected to be generated from a mix of income and trading and matches what the team has achieved historically. Bowers was lead portfolio manager for CVC Credit Partners European Opportunities Limited, which averaged returns of 12.7% per year from 2009 to 2017, with its worst year being a small positive number in in 2011. He also managed a recovery fund between 2008 and 2013, which generated a net IRR of 13.3%. Acer Tree's other founders contributed ideas to Castle Hill's credit opportunity fund from 2009 to 2016 which ran a similar strategy and performed strongly.

ATCOF has been annualising at about 25% between launch in June 2020 and March 2021, more than double the return from European high yield, European leveraged loans, or global hedge funds, and above its target. "Returns have been higher partly because Covid created exceptional opportunities, which allowed for faster rotation and there has also been more scope for rebalancing between the strategies," says Bowers. For instance, since June 2020, Acer Tree have had opportunities to rotate through defensive sectors into cyclicals and then more Covid challenged sectors as risk appetite has returned. "In future, we would broadly expect mid-cycle returns of around 12%, but we do not have a crystal ball. We are disciplined in defining the downside and then solving for returns. We do not force returns if we cannot identify the opportunities," says Bowers.

Directionality is variable and the short book is both defensive and offensive: "We have spent premium on an overlay of index hedges, which we view as a cost. There can also be sector hedges. We have also identified targeted single name shorts in industries such as refining, which have performed well". There are also non-directional strategies including capital structure arbitrage. The cash versus derivative trades might take advantage of temporary dislocations until the relationships reconverge.

Deal sourcing

Acer Tree has already participated in primary issuance and taken advantage of "hung deals" where underwriters left holding paper had to sell it at a discount. Deal sourcing is helped by a strong network of relationships with companies, the sell side, and collaborative relationships with sponsors. "We get good allocations to bonds and loans relating to private equity deals. Our minority shareholder is private equity firm, Cabot Square Capital, who can also help with sourcing," says Bowers.

Liquidity, settlement and valuation

Acer Tree need both reasonable liquidity and timely settlement for their active trading style and to retain the optionality of being able to opportunistically redeploy capital. "Liquidity is nearly daily in the mezzanine structured credit space, though CLO equity can trade by appointment," says Bowers. "Liquidity per se is not the concern with loans, as they can sometimes be more liquid than bonds. The problem with European loans is an arcane, manual, paper-based settlement process that can sometimes take six months, and thereby delay the receipt of cash after a sale. There is no compensation for this delay on primary deals. Therefore, we would need a higher spread on loans to compensate for the delay, and currently spreads on offer are relatively low. Secured loans are a very small percentage of the portfolio, as they do not offer compelling value," says Bowers.

Nearly all the portfolio has a market price or counterparty quote: "All of the portfolio is level 1 or level 2, except for some instruments that are temporarily level 3 while they go through restructuring processes. We do not plan to do any direct or bilateral lending," says Bowers.

European complexity

If Acer Tree are not trying to pick up significant illiquidity premia, they are certainly seeking complexity premia. Over 80% of the book is in Europe, where they expect to be rewarded for investing in special situations, including M&A. The investment process includes analysis of multiple jurisdictions and documentation in Europe's twenty-seven countries, which have twenty-seven bankruptcy laws. "We invest in proven legal systems where we can get our money back and which are tried and tested. We have worked on deals in all jurisdictions over the years. Our focus is Western Europe, but not necessarily Northern Europe. For instance, France now has more structure in its process. Some entities related to European situations could also be going through a US process. There are some jurisdictions we would avoid. There are also some situations we would avoid. We try to assess how consensual a deal is going to be, and try to avoid the protracted, expensive, process risk of a non-consensual deal," says Olson. In early 2021, the UK, France and Germany were the largest country weights.

Liquid distressed situations and debt for equity swaps

Rising defaults create more opportunities, but Acer Tree is selective about which it picks. "Given our size we will not be driving restructurings or sitting on committees, as we did in the past. We are looking for larger, more liquid distressed situations so we can sell at any time if we change our mind," says Olson.

> *"Acer Tree is the culmination of our 25 years of shared DNA in credit."*

Outlook

Important sources of idea generation in 2021 include uneven recoveries and dispersion within Europe. "The market anticipated a very strong vaccine rollout, but forecasts are now very disparate with wide divergences in recovery, inflation and interest rates between countries," says Bowers. Elections in France and Germany could be interesting, while the Brexit trade deal still leaves uncertainties to be resolved and is creating supply chain bottlenecks.

Indeed, Acer Tree's perspective on the inflation debate is very much industry and company specific: "We do see some inflationary pressures from supply chain issues and the commodity cycle, in areas such as food, packaging, chemicals and oil. These create opportunities in some industries and margin squeezes in others," says Bowers.

Longer term, the firm may expand its range of strategies to cover more performing credit and solution capital, but it does not have any near-term plans for direct lending.

Asset raising

Early capital has been raised from friends, family and high net worth investors and Cabot Square Capital. "Post-lockdown, we are having conversations with institutions, including private family offices, wealth managers and funds of funds. Marketing for now is mainly focused on the US and Asia. We expect more face-to-face meetings in the second and third quarters," says Bowers. Discounted fees are on offer in the founders' share class.

Founder and Portfolio Manager
Calixto Global Investors LP
Miami

Eduardo Costa

Uncorrelated, single stock alpha, TMT/consumer focused

Eduardo Costa named his firm Calixto Global Investors after General Calixto Garcia, a hero of the three Cuban wars of independence in 1868, 1879 and 1895. Garcia was famous for his bravery and perseverance. "The name symbolises perseverance in the face of adversity, a hallmark of the firm," says Costa, whose parents emigrated to the US and rebuilt their lives after the Cuban revolution in 1959. The kicker is that Calixto Garcia is also Eduardo's maternal ancestor.

Calixto, which is located near Costa's family in Miami, Florida, did not start with any seed funding in 2014. "We could have done a seed deal but instead bootstrapped and built from the ground up, raising assets from friends and family and a few key investors," explains Costa. Calixto did not avail of emerging manager programmes focused on minority managers either, though it is amongst a relatively small number of minority-owned managers.

Calixto has ploughed its own furrow in developing an uncorrelated strategy: "We are idiosyncratic stock-pickers, seeking companies in the TMT and consumer sectors globally that are experiencing positive or negative inflection points in the fundamentals of their businesses," says Costa. He focuses on investment stories that are off the beaten track, which reduces the possibility of overlapping trades with his peers, tends to have minimal sell-side coverage and offers a more differentiated exposure for the firm's investors. Over half of Calixto's exposure – and in recent years over 60% – has been outside the US, with Japan the largest, China next and most of the rest in South Korea, South East Asia or Europe. Japan has been a stalwart for returns, generating both positive absolute returns and positive alpha on both the firm's long and short books inception-to-date. The firm invests in companies across all market capitalization, with roughly even weights amongst large, mid, and small caps. "Having over half outside the US and two thirds in small and mid-caps is fertile hunting ground for differentiated ideas," says Costa. Proving his mettle and staying power, Calixto has delivered double-digit annualized returns since inception.

Liquidity, shorts and mentors

While Calixto is seeking contrarian ideas, they must be in liquid equities. The manager invests in small caps – but not microcaps – and the strategy stays liquid: 75% of the book could be liquidated in a day, 96% in five days and all of it in 10 days. "I always want to stay liquid because my former employer, Chris Shumway, drilled it in that you never know when circumstances might invalidate a thesis, when you might just be wrong, or when a technical situation such as January 2021 might crop up," says Costa, who joined Shumway Capital Partners after an MBA at Columbia Business School. Tiger cub Shumway "was a key mentor imparting the basics of Tiger style investing on me early on," adds Costa.

"William von Mueffling was another mentor; he taught me how to short stocks in my first job after graduation, at Lazard Asset Management," says Costa. Shorts are all in single stocks and are intended to be profit centres – no ETFs, indices nor sector baskets are used. Calixto's short book has generated positive alpha in six out of its seven years of trading. The strategy has also shown negative down capture versus the MSCI (as of YE 2020), meaning that in the cumulative months the MSCI has been down, Calixto has generated positive returns.

Variable exposure

Net exposure has averaged 25% with gross averaging over 140%, though there is no specific target for either, and Calixto has been briefly market neutral at various points in time. Both gross and net exposure reflect bottom-up ideas rather than being a top-down macro call. Variations in exposure have added some value over the past 18 months, including the coronavirus crisis. In late 2019, the strategy was at peak gross exposure, due to an abundance of ideas that were playing out through strong or weak earnings, but this was cut back within a few months as Calixto was earlier than many in recognising that Covid-19 was potentially a serious threat for companies. "Being on the ground in China in January and in Japan in March 2020, we saw substantial disruption across our sectors. Simultaneously, we also observed Covid-19 beginning to spread throughout the world. We are fundamental investors and certainly no experts on the pandemic, but realised that any risk of it spreading would lead to an outcome not underwritten by markets at the time. Based on the potential disruption to our underlying companies, we took the gross down from 190% to 116%, and the net down from 35% to near neutral or slightly short for a period in March. This was not a top-down call," recalls Costa.

Growth and value barbell

After the first quarter, Calixto subsequently sized up its exposure and had an exceptionally strong 2020, generating 47% net returns for the year, with average net exposure of 35%, beta and correlation to the Nasdaq of 0.15 and 0.30, respectively, and roughly half the volatility of the Nasdaq and MSCI. The drivers were as usual more stock-specific than thematic. The strategy took a barbell approach, investing in both long term "growth" style Covid winners as well as beaten up value oriented "Covid losers" that would benefit from reopening.

Some stocks combined both elements: "The best contributor in 2020 was Chinese firm Meituan, which is most well-known for its online food delivery, where it has a 70% market share and benefited from an explosion of adoption in 2020. It also has a restaurant booking division that did very poorly," says Costa.

Similarly, key contributors in Japan included long duration growth in second-hand e-commerce, as well as more cyclical recruitment agencies. "Japan's largest second-hand goods e-commerce platform, Mercari, is a huge C2C marketplace, which saw a sharp inflection in its growth rate, as did its US subsidiary. Equally, in April and May 2020, as reopening started to drive the green shoots of recovery, we initiated a position in Outsourcing Inc: a recruitment agency, which has doubled yet still trades on only six times EBITDA. Since smaller rivals could not survive the downturn, it is also consolidating smaller players," says Costa.

In the US, Calixto also held long-term growth plays alongside value names: "Peloton created a whole new category: connected fitness. The company is bigger than its five largest competitors combined and can invest enormous resources in price reductions to drive growth," says Costa. "Media firm Nexstar is more like a value stock, trading on a single-digit PE ratio, despite almost tripling from the lows," he adds.

A pragmatic approach to factors and crowding

The ability to exploit both growth and value at different times in 2020 is typical of the unconstrained, opportunistic approach: "We are style and factor agnostic. We monitor growth, value, macro sensitivity, crowdedness, and mean reversion. We sometimes find more growth opportunities and sometimes more in value, as in the past 3 to 6 months between November 2020 and April 2021. But in technology, disruption and innovation happens so consistently that there are always companies exhibiting extraordinary levels of growth and inflecting positively juxtaposed with those that may be getting disintermediated and/or decelerating". This approach leads to uncorrelated return streams during periods of market rotations, such as in March 2021.

Calixto sometimes seeks to dampen factor bets, where this is consistent with its bottom-up stock picks: "We ideally want to eliminate factors as drivers of attribution and leave the stock specific thesis as the primary driver. If we have exciting growth-oriented longs, then we ideally also want to find opportunities on the short side with those same characteristics – but we will not force those ideas if we cannot find them organically".

Costa does not always have a conventional perspective on defining factors. Some bank research has started to define "unprofitable technology" as a factor, which generated extraordinary performance in 2020, but Calixto does not perceive it as such. "Unprofitable technology" per se is not a factor we monitor, because many tech firms, in areas such as software as a service (SaaS) and cloud software, have very high gross margins of 70-90% and are voluntarily unprofitable. They choose to spend an extraordinary percentage of revenues on sales and marketing to make a land grab as they are at a sweet spot in the S curve. As they scale up, they build a growing competitive advantage over peers, and can reinvest more aggressively in technology and research and development, further widening the gap."

Calixto's non-US and small/mid cap emphasis naturally reduces the risk of being in overcrowded names, but both institutional and retail investor crowding are nonetheless watched: "We monitor hedge fund positioning with Bloomberg and prime broker data. We are not as concerned about long book crowding if the thesis is right, it is almost a strength. Short book crowding is a greater worry as seen in the January 2021 short squeeze, which was a tough month for hedge fund alpha and forced some funds to exit positions when they should have added. We were able to take advantage of the late January 2021 dislocation. When peers were covering shorts, we were adding to ours and buying losers on the long side. Playing offense really helped with the rebound".

Retail crowding has become more relevant in 2020 and 2021 as retail investors, stuck at home and unable to bet on sports, have become more active. Costa's experience in Japan gave him a leg up in navigating a storm he typically deals with overseas: "We have seen retail frenzies and short squeezes driven by retail participation in Japan, which can be based on buzzwords such as AI, machine learning or cloud being incorporated into company names".

Deep fundamental research

Calixto is aware of technical factors such as positioning, but applies a fundamental research process that emphasizes deep dive channel checks and proprietary modelling. Costa was Director of Research at JAT Capital – which spun out of Shumway – before launching Calixto. "We build our models from the ground up to analyse companies that may have no sell side coverage at all. We build a thesis, triangulate, and verify it, based on conversations with management, relevant suppliers, competitors, and former employees. Data verification is likely to be the last stage. We are mindful that third-party data could be commoditised, and we are creative on new sources of data, especially for smaller and less followed companies."

The process has adapted smoothly to travel restrictions: "Historically, research-related travel was a big hallmark of our approach. I flew over 200,000 miles in 2019, mainly to visit companies in China and Japan, as well as West Coast US software and internet firms. Now we have Zoom marathons at night covering 30-40 companies in the span of a month. Fortunately, we have a big library of ideas developed over the firm's life, including our own bottom-up financial models: in Japan alone, we have built over 175 models, and multiples of that globally. Our relationships with company management, the sell side and other industry participants are critical to the process when we are not on the ground. We have adapted and executed the strategy well in a different environment".

Private equity and venture capital are also on the radar, although it has not been a core part of the firm's DNA historically: "We monitor and maintain a dialogue with private companies to understand disruptive trends, and this is highly synergistic with the research process. We have, on occasion, opportunistically looked for private companies to take advantage of directly, for special purpose co-investment vehicles we offer to investors".

Private equity and venture capital frequently exit through IPOs and SPACs, which have boomed in 2020 and early 2021. "Newly listed companies are not in and of themselves, a huge part of the strategy, but we monitor them closely for interesting long and short opportunities. There is so much growth and disruption that a never-ending parade of new companies are shaking up the equation. We think some SPACs rushing to go public could be attractive shorts," says Costa, illustrating his difference of opinion with some other hedge fund managers who are enthusiastically embracing the SPAC space.

Founders
Discovery Nymeria Fund
New York

Ian Lieberman + *Andrew* Fruchter

Concentrated, thematic, low net, long/short TMT

Back in 2016, while Ian Lieberman and Andrew Fruchter were attending a MIT university symposium on artificial intelligence and machine learning which was targeted for academics and professionals in the technology space, unbeknown to each other the duo showed up and were sitting next to each other as they began networking with experts in the space. At that point it became clear their investment process and philosophy were in sync with each other.

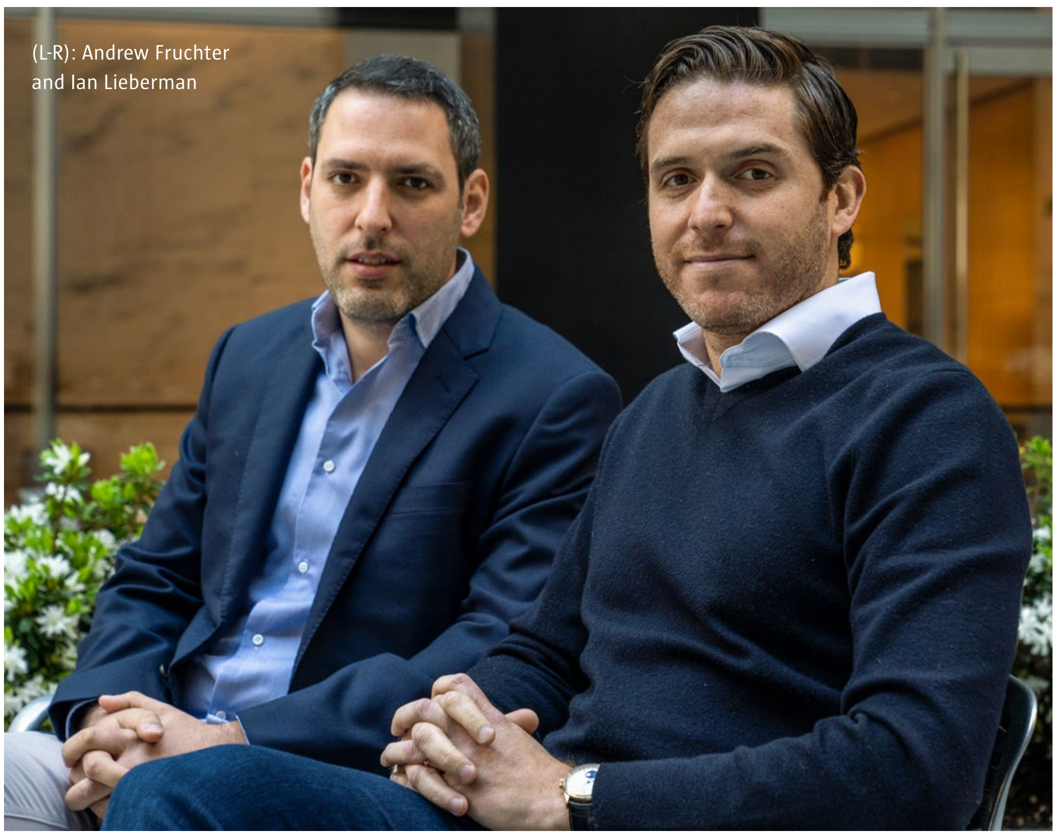
Fast forward to today, and they are partners at Nymeria where their highly selective investment process focuses on identifying themes and positions that best express their views, using a deep fundamental research process drawing on their overlapping history, personal investing experience, and broader intellectual curiosity. They have known each other for over 16 years and see eye to eye on the investment process having collaborated on many investment ideas over the course of their careers – PayPal post spinoff from eBay, Micron below ten dollars a share, Broadcom, and many others.

They are animated advocates for technology, such as how technological progress in the cloud, social media, and remote working made society and the economy more resilient amid the pandemic. However, this does not translate into a volatile or high beta style – and Nymeria is also very different from most lower beta funds.

Funds with low or no beta are often running highly diversified books of pairs trades and are sometimes quantitative. Concentrated, longer term fundamental discretionary stock-pickers often have a heavy net long, high beta and growth factor bias.

Nymeria combines low beta and moderate factor exposures with a high conviction focused portfolio of long-term holdings, comprised of many smaller and less crowded names. These investments are identified through deep fundamental research tapping into different sources of intelligence including networks in Asia, venture capital and the tech industry. Nymeria also employs strong, derivatives-savvy risk management in order to drive rigour not just on the position entrance, but also on its exit.

The strategy is backed by Robert Citrone's Discovery Capital Management. The strong relationship has come with many benefits of working together, bridging fundamental with macro views, and



(L-R): Andrew Fruchter and Ian Lieberman

providing all of the business, risk and operational support so they can focus on managing their portfolio.

The long-term and annualized return target, through the cycle, was surpassed in 2020 and the strategy held steady amid the broad equity rout in the first quarter, and the technology sector setback seen in the third quarter, while profiting during the violent shift from growth to value seen in the fourth quarter. During these months of heightened volatility, Nymeria's volatility decoupled from that of the market's and remained at structurally lower levels. In fact, their volatility in September was completely unchanged month over month despite market volatility nearly doubling. This is just one example of the output from a fundamentally driven investment process, with a sharp focus on risk management.

Factor awareness and crowding

While Nymeria are fundamental investors, they are fundamental investors who will run the portfolio while being factor aware. Their Q3 investor letter stated that, "In a modern market we believe ignoring factors, especially in moments of extremis, is tantamount to burying your head in the sand. As such, in early September we determined our crowding factor to be too high putting the portfolio at risk in the event of a broad market selloff. We addressed this by reducing and hedging part of the factor exposure".

Whereas some TMT managers have a clear bias to the growth factor, Nymeria's performance attribution shows low sensitivity to traditional factors like value, momentum and growth as well as other transient, but impactful factors such as "work from home" and "recovery".

The low factor sensitivity is partly explained by Nymeria viewing growth versus value as a false dichotomy – and identifying stocks with multiple factor exposures. Their investment in Eventbrite was viewed as one with both a recovery factor exposure that is often correlated with how value stocks trade, while also clearly having a growth factor exposure due to the tremendous potential trajectory of their business in the coming years between online events and the recovery of physical events.

Nymeria's sensitivity to the crowding factor is low, but also more nuanced. As fundamental investors, the crowding factor does not determine whether they enter or exit a position. That being said, it does inform their sizing and timing, which would require them to have a thesis that diverges further from consensus in terms of earnings estimates, cycle duration or general outlook.

Thus, idiosyncratic or stock-specific alpha was the main performance driver, with sector and sub-sector selection also helpful. Longs and shorts are underwritten independently and will not be intra-sector pairs by design. Their investment universe includes over six hundred TMT companies globally, meeting liquidity and trading criteria (above $15 million average daily volume). The sharper focus is on 5-6 investment themes at any time, which narrows it down to a smaller watchlist of around 15-20 ideas per thematic framework or 100-120 companies at any given time.

Mentors and influences

Ian Lieberman previously worked for Discovery Capital Management founder and Tiger cub Robert Citrone, who was a key mentor to him. The Tiger style process is highlighted in many different pieces in their investment process – duration, concentration, and deep primary fundamental research. Similarly, Andrew Fruchter, grew his investment acumen by working with Morris Mark, founder of Mark Asset Management, a deep-rooted research organization.

Asian intelligence

Alertness to how nascent Covid-19 was impacting Asian supply chains (as well as European demand levels) informed some timely adjustments on their long and short investments in early 2020, and this partly leverages Lieberman's extensive network in Asia. Lieberman has visited factories and met with management teams in China, Japan, Korea and Taiwan multiple times a year for many years now. This has led the strategy to invest both long and short in off the beaten path opportunities such as Renesas Electronics, Comba Telecom System Holdings, Murata Manufacturing, Walsin Technology Corp, MediaTek, and Lasertec. In 2014, Fruchter also spent time in Hong Kong and Beijing as he earned a MS in Global Finance through NYU Stern and Hong Kong University of Science and Technology. Being on the ground in Hong Kong and Beijing allowed him at the time to take advantage of grassroots research on existing names his fund was invested in such as Yum Brands in China and Wynn Macau.

Private equity and venture capital intelligence

While Nymeria are public investors, smaller and earlier stage companies in the private space are also followed as private equity and venture capital investors are another historical and ongoing influence. Fruchter has personally invested directly into private technology companies since 2006. Nymeria keeps in touch with the venture capital community and industry experts across the globe to have an ongoing dialogue on emerging trends in the space.

Nymeria does not cross over into private market investing nor do they invest pre-IPO as the portfolio is fully liquid, but trends in unlisted companies feed into their analysis of public companies, which can also be very innovative: "We look to bridge knowledge between private markets and public markets to work out who is disrupting whom and the new emerging trends we should be paying attention to," says Fruchter.

Semiconductors: an early and long-term call

Nymeria's contrarian views on semiconductors started out ahead of the curve in mid-2020 and in early 2021 their views remain non-consensus in expecting the cycle to persist for longer. Back in June 2020 the world seemed very bleak, but Nymeria saw a golden era for semiconductor memory chips as going into Covid-19 the industry had very low inventory after a destocking cycle, and this fell further after the ecosystem – much of which is in China – was disrupted. Meanwhile cyclical and secular drivers were behind huge restocking demand from computers, webcams, cellphones, iPads and autos given the public transport issues. Secular drivers included electric vehicles, AI and machine learning inference datasets. This was a true V-shaped bottom for demand. Semis were their biggest P&L contribution in 2020.

Per their 4Q investor letter, "For reasons we have now argued throughout this letter, we would suggest we are still in the middle of this cycle. We have moved our exposure to investments that are experiencing only the first stages of "tightness" such as Sumco (Japan), Micron, and Samsung (Korea), or in the case of Microchip are levered to broad based recovery with a capital allocation story on the come".

Nymeria remains bullish while other investors fear semiconductors are peaking based on historical relationships with metrics such as PMIs, but this cycle is different. There have also been freak events impinging on supply, such as power cuts in Texas and earthquakes and fires in Japan. Meanwhile automakers and other end customers should raise inventories to levels not seen in 30 years if not more, which could further elongate the cycle. This illustrates time arbitrage as Nymeria highlights one of their many differentiators. While many investors have a sightline measured in days or weeks, Nymeria takes a longer-term view on longs. Nymeria's duration profile is again evident in their largest position [Sumco], a Japanese maker of bare wafers used in the semiconductor manufacturing process. "Consolidation of the industry from five to four players should increase pricing power, for several years, and it takes two years to add more capacity. With limited industry supply intentions and the explosion of demand for bare wafers to feed semiconductor demand, we believe we are on the cusp of a powerful multi-year pricing cycle that should serve to drive tremendous upside in the stock," says Lieberman.

Option overlay

Though Nymeria may take a multi-year view on stocks, they also fine tune their exposures on a shorter-term basis with derivatives. Per their investor presentation, their option overlay over-writing and under-writing strategy – only on a covered basis – helps them exit risk with discipline and rigour and without emotional attachment to winners or thesis creep, while adding to P&L – partly since most options expire out of the money. This option strategy allows them to maintain a larger position as they approach their price target rather than selling prematurely. Occasionally options are also used to get more upside in catalyst driven situations.

A great place to work

They are building the culture from the ground up, with a research-oriented process that brings on people who are passionate about the space, seek out opportunities with fervor and are excited to come into work, and be at the precipice of change in TMT. The world is constantly evolving, and strategies need to evolve. "We have a culture that encourages each individual to think creatively and dynamically, allowing us to constantly adjust our thinking to the environment, not just stay within a box," says Fruchter. "In 20 years' time our most important legacy will be generating quality returns for our partners where people find it a great place to work," sums up Lieberman.

Nick Greenwood, CIO and Co-Founder and
Ashley Hudd, CEO and Co-Founder
Haven Cove Capital Management
London

Nick Greenwood + *Ashley* Hudd

Liquid credit and equity alpha


Nick Greenwood


Ashley Hudd

"The name Haven Cove symbolizes the "safe haven" return profile we seek to provide as a custodian of investors' capital, not just protecting the downside but also providing attractive and consistent returns over the long-term," says Nick Greenwood. The manager has just passed a three-year audited track record in Haven Cove Absolute Return Fund (HCARF) and delivered its return objective of being a low volatility, absolute return strategy targeting a Sharpe ratio of around two. This is achieved by combining three strategies with attractive risk premiums and/or alpha opportunities: European investment grade credit, systematic relative value equities and special situations equities. There is also dynamic risk management and hedging, and the correlations between the strategies are low.

Greenwood and Co-Founder, CEO Ashley Hudd, have been trading a range of somewhat similar strategies for many years inside banks and other prior buy-side mandates, and they overlapped at BarCap between 2008 and 2011, but the current strategy mix has been tailored to HCARF. "The choice of strategies for HCARF was optimised and recalibrated to fit inside the risk parameters of a relatively liquid fund structure that could not accommodate highly structured or illiquid credit and has different costs of capital," says Greenwood. "The ambition to design our own strategies, run our own hedge fund manager, and build our own operational structure from front to back – including prime brokers, ISDAs, OMS/PMS, capital and risk management, and reporting – was one reason why we eschewed offers from bulge bracket hedge funds when leaving the banking sector in 2011, and joined a multi-family office set-up instead. This gave us more flexibility, let us build broader investment experience and wider networks, without the siloes of larger organizations, culminating eventually in the launch of our own fund HCARF in January 2018," says Hudd. It also let them forge relationships with investors who have demonstrated growing confidence in the duo: early buy-side capital came from substantial commodity-related family offices, all of whom subsequently invested in HCARF – and have increased their allocations over time.

European investment grade

Roughly half of the risk budget is in a European investment grade corporate credit derivative strategy, which essentially leverages credit spreads while truncating default and spread widening risks through subordination and trading around dynamic hedges.

In absolute terms, European corporate investment grade yields are very low – and sometimes negative – as are the sovereign and swap curves. But the European IG credit default swap (CDS) spread has fluctuated between 46-54bps in Q1 2021. "Tranches of the index can generate a fund level yield target of around 9%, which entails using two types of leverage. The notional value of the tranche book is more than the fund NAV, and its credit spread sensitivity works out at an index-equivalent leverage of about 10 times," says Greenwood.

Yield optimisation

The manager seeks to enhance yields (carry and theta) not only through leverage but also through an optimisation model that selects series, tranches and terms that access steeper segments of the credit curve and therefore offer more "roll down" versus risk. "We will not however invest longer than five-year maturity, partly because shorter dated exposure also pulls back to par sooner after any dislocations," says Greenwood.

"Bespoke tranches with non-standard attachment or detachment points might also sometimes offer some degree of complexity premia that may arise from banks' regulatory capital constraints," Greenwood adds. Unlike some types of structured credit, liquidity risk premia are generally not a feature of the synthetic iTraxx Main standard tranches, which are highly liquid instruments with six or seven large dealers quoting prices.

Default risk

Greenwood judges that the European IG market spreads in the core strategy represent a major structural inefficiency – both in absolute terms and relative to US IG. They are very attractive relative to actuarial spreads (which would only cover default losses) since historical default losses on European IG have been a single digit number of basis points. There have been very few defaults, and recovery rates have been high: "There have only been two defaults in the five-year iTraxx Main series since the index began in 2004 (and only a further two more if you include the 7- and 10-year series). In contrast US IG has had 10 defaults in total in the 5-year instrument and 14 in total if you include the 7 and 10 year".

"US IG still offers an attractive market spread versus actuarial spreads, partly because technical flow pressures keep spreads wide. European IG trades with similar market spreads but, in our view, much lower fundamental default risk and so is more mispriced than US. Default rates have been much lower in Europe IG and are likely to stay lower due to cultural aversion to bankruptcy and harsher and less homogeneous bankruptcy regimes (relative to US). We also prefer IG to High Yield (Crossover) in Europe, as we view the dislocation/risk premium in IG to be much more stable and persistent," explains Greenwood.

Nonetheless, the strategy aims to have some protection against default risk through subordination – most of the tranches owned sit above first loss tranches: "Only about 15% of the long side portfolio is in equity (i.e. 0-3%) tranches and the rest is in mezzanine or more senior mezzanine paper which attaches at 1% or above. One simple stress test is that if each credit is weighted at 0.80% of the index and recovery rates are 40% on average, a loss from one default would be a hit of 0.48%, so >1% subordination covers for at least two defaults," says Greenwood.

Spread risk

Absent default, the strategy is much more likely to see volatility from spread widening and this risk is limited through buying option protection, mainly on indices but sometimes also partial hedges on selected single names. This is intended to kick in at levels that limit such temporary mark to market drawdowns (in a worst-case scenario) to around one year of projected return. The assumptions underlying the stress test seem reasonably conservative based on historical stressed events. "A parallel shift with constant implied volatility and implied correlation is modelled, although in practice spikes in volatility and correlation could further increase the value of the hedges, and we believe a parallel shift of all index series is a good and conservative approximation of a worst-case stress move across the term structure," says Greenwood.

Spread outlook

European IG credit spreads around 48 basis points are somewhat below long-term averages of c.65 basis points. Whether rising interest rates pose a threat to IG credit is debatable because there are two opposing forces: "As rates rise, corporate costs of debt will rise, which prima facie should drive credit spreads wider. But if economic recovery is the reason for rates rising, this should have the opposite effect i.e., a compression of default risks and credit spreads. The tug of war between these forces will likely create some volatility along the way. But the risk of a sharp spread widening has a strong backstop from the European Central Bank (ECB) asset purchase programme," says Greenwood.

Spread volatility trading

Trading around this spread volatility can add to returns, mainly through adding risk at opportune times i.e., when spreads are wider because of technical flows rather than a change in fundamentals. Most of the return on the portfolio comes from clipping the leveraged CDS coupons, and rolling down the curves, but "active gamma trading of the options book could also make as much as 2% per year, and possibly more in 2021," says Greenwood.

Systematic relative value equity

The second strategy is the only wholly systematic one of the three. Trades combine momentum and mean reversion models, with typical proportions of 70% and 30%. "We mainly emphasise momentum at present partly because we think that the very large firms are better positioned to compete in shorter term mean-reversion trading. We also believe that the relatively more crowded positioning in the equities sector works in favour of momentum trading. Data inputs are mainly technical price data but do have some fundamental overlays. The models are statistical approaches that seek a small edge based on the law of large numbers," says Greenwood.

The systems can trade both between and within sectors, styles, and factors and have garnered some profits from the shift into cyclicals and value in late 2020 and early 2021.

Special situations equities

The third strategy, special situations, is mainly discretionary. It covers the European corporate event space that the pair have traded since 2008, with specialist brokers helping to filter down the universe to a concentrated portfolio of high-conviction positions. "Many trades sound like a good idea but are practically hard to execute. The brokers do a lot of the heavy lifting," says Hudd. The managers are very selective. Traditional late-stage merger arbitrage trades with far greater downside than upside are avoided. They prefer earlier stage event trades, which can offer a more asymmetric return profile akin to a cheap option with positive convexity. They also seek to underscore theses with fundamentals and momentum.

The opportunity set here is somewhat intermittent: "We would not launch a pure special situations strategy, because the deal flow can be erratic. There may be no trades in one month and then two trades in a week," says Hudd.

Strategy weights and correlations

The risk budget weights between the three strategies are fairly steady at 50% IG credit, 25% systematic relative value and 25% special situations, though there can be some leeway. The three strategies provide some degree of portfolio diversification: "The credit book has a very low and stable correlation with the systematic relative value equities book. In contrast the different types of event trades within the special situations book do display somewhat different patterns of correlation. For instance, holding company and stub trades or index dividend futures might sometimes have a risk-on flavour that is correlated with credit, but other situations, such as share class trades can show no or even a negative correlation," says Hudd.

Upping the ante

"After a recent three-year performance review, we had slightly overshot on volatility control, and have determined to increase gross exposure in the credit and systematic relative value strategies in order to consistently hit our double-digit annualized return target. Net exposures and risk limits remain the same," says Greenwood. This is already showing results, with returns of more than 4% in the first quarter of 2021.

Ready for growth: Manco, operations and service providers

Raising gross exposure is mirrored by an operational and regulatory structure that is gearing up for the next runway of growth. Having had a self-managed Malta AIF that was delegating portfolio management to the pair via a UK MiFID investment manager platform, Sturgeon Ventures, they have just moved to a full scope UK AIFM structure, Haven Cove Capital Management Limited, which will take on both portfolio and risk management functions. The fund is also re-domiciling to a Cayman structure.

They are in the process of hiring a COO and junior trader. Centaur Fund Services of Dublin, which is experienced in credit strategies, has been retained as administrator since January 2021. JP Morgan is the full scope prime broker, offering all investment services and capital introduction. Haven Cove won a place on JP Morgan's emerging manager programme amid fierce competition from a wide pool of other managers. The manager should soon have two additional credit ISDAs; the difficulty of obtaining these acts as a barrier to entry that also helps to explain risk premiums in the credit derivatives space. In total, there are five other brokers used for equities, CDS, capital introductions and special situations, and more may be added. The opportunity set in the three strategies remains highly compelling.

Assets are over $60 million and strategy capacity could be over $1 billon in the credit strategy and $500 million in systematic relative value. In addition to the managers' own capital, Haven Cove currently has an investor base comprising family offices, institutional and UHNWIs.

Portfolio Manager
Serone European Special Situations
London

Ralph Herrgott

Mid-market, stressed and distressed, event-driven alpha

Serone Capital Management LLP Head of Special Situations, Ralph Herrgott, has been consistently applying his investment principles and process since 2004, investing through four major credit cycles: the aftermath of the TMT bubble, the GFC, the European sovereign debt crisis, and launching Serone European Special Situations (ESS) in March 2020 amid the Covid pandemic.

Herrgott started his career at Morgan Stanley and spent seven years doing investment banking and restructuring advisory work at various firms. In 2004 Herrgott started his buyside career as a senior analyst (European distressed team) in JP Morgan's Proprietary Positioning Business which was run by Patrick Edsparr (who featured in the 2019 edition of *Tomorrow's Titans*).

In 2008, Herrgott together with JP Morgan's distressed team spun out into Sothic Capital Management. At Sothic, Herrgott was the largest profit contributor of the firm and has a personal trade-level track record between 2008 and 2016 annualising at 19.2%. His trades were profitable in seven years out of eight and produced an impressive win:loss ratio: 27 winning trades made €181 million while 16 losing trades collectively lost just €12 million. The strategy is reasonably concentrated, but Herrgott only hit the 15% position size limit once at Sothic when equity attached to a bond kept appreciating. Sothic formally returned capital in September 2016, but Herrgott oversaw a large part of the tail end liquidation until 2018, which was also profitable.

Shortly after leaving Sothic, he joined Serone in late 2018 to lay the foundations for ESS, which complements Serone's top-notch ten-year track record in structured credit via flagship Serone Key Opportunities Fund (SKOF). "With ESS, Serone are becoming leading investors in the complex, under-followed and under-researched niche markets of European corporate credit special situations," says Herrgott. ESS trades single name European corporates with hard event catalysts such as defaults, bond tenders, refinancing, restructuring, M&A, spin-offs, or equity issuance, typically envisaged within 12 months. Herrgott generates ideas primarily from credit but can invest across the capital structure and some trades will have a capital structure arbitrage flavour with legs in different instruments from the same issuer. Senior, subordinated, first lien, and second lien paper can be owned, as can post-reorganisation equity.

Synergies between structured credit and special situations

Amongst many synergies between ESS and SKOF, the most valuable is perhaps the technical intelligence emanating from Serone's structured credit business. "When I started talking to Serone founder and CEO, Neil Servis, I realized the mutual synergies of working side by side with the structured credit investment team. They would get our internal credit views on more complex CLO assets, and we would have a sense of what is sitting in CCC buckets of CLOs and what might trigger sales. Having a clearer idea of supply lets us optimize entry points. The CLO watchlist has generated ideas as well as sourcing advantages for the special situations strategy," says Herrgott.

"Our structured debt colleagues can also provide valuable insights into businesses, for example fee development for debt service providers, which can be relevant if we buy bonds of debt collectors or servicers. We have only just started scratching the surface of the synergies, which are unusual in a firm of our size." Serone runs about $1 billion in total.

Inefficiencies in European credit

The European high yield market has grown enormously over Herrgott's career, to more than €750 billion and the European stressed debt space is now worth about €50 billion but yields on much of this are far too low to be long candidates for ESS: "The first quantitative screen is simply for yields to maturity over 9%," says Herrgott. "We also stay away from the largest "distressed index trades" that are dominated by big US funds where we cannot influence outcomes. We focus on mid cap structures between $100 million and $1 billion". There is still plenty of choice for a strategy that might have 20 or 30 positions: "As of April 2021 ESS is tracking about 200 individual issuers in the long universe and another 230 in the short universe".

The ESS watchlist offer yields, and expected total returns, many times more than more plain vanilla paper, for various reasons. The simplest inefficiency is many credit ratings-driven investors cannot buy the unrated paper that makes up about 30% of ESS' universe.

"Busted convertibles" can become somewhat orphaned since many convertible investors are equity investors who do not have an appetite for instruments with little or no equity sensitivity. "Once convertibles become a credit story, they no longer have a natural investor base. We have long relationships with CB desks, and we look at every busted convert," says Herrgott.

Firms with a history of restructuring, or that operate in cyclical industries, can also be acquired at quite pessimistic prices – and mis-pricings have been identified through high frequency and alternative data. This alerted Serone to improving revenue trends at a Dutch DIY retailer well above what was discounted by market pricing. "We are actively building out the high frequency data and investing in technology to automate it up to a point, because high yield research in Europe is too model oriented. Piotr Ossowicz, who leads ESS' research team, has experience of analysing alternative business data from his time at Boston Consulting Group. Alternative data could also become useful for our short book," says Herrgott.

Pan European

ESS has a wider opportunity set than some funds because it does not rule out any countries or sectors. "The strategy is opportunistic in selecting from all sectors and countries in the European Economic Area. Our research analysts are generalists," says Herrgott, whose degree program in the 1990s involved a year in each of Berlin, Oxford and Paris. He retains a pan-European perspective. Whereas many credit managers avoid Southern Europe because it is less creditor friendly than Northern Europe, France and Spain are his largest two country weights in March 2021 and he has exposure to one Greek situation. "Differences between legal systems and levels of disclosure within Europe are a source of inefficiency to be taken advantage of. We take jurisdictions into account in pricing and expect a higher discount in creditor unfriendly jurisdictions. If it is difficult to see a consensual restructuring, we may even find a short."

Return targets through the cycle

Herrgott expects that the strategy will generate average annual returns of 12-15% through a full cycle, with a good year normally above 20% and a bad year perhaps 5-8%. In its first year, between March 2020 and March 2021, ESS has actually annualised more than 40%. Extraordinary opportunities in 2020 have allowed for higher portfolio turnover than normal. The fund realised some 43% of its gains in 2020 implying annualized turnover above 200%.

"In the pandemic many senior secured issues moved towards restructurings. We would normally expect turnover of 100% to 150% per year," points out Herrgott. The 90% of returns that came from capital gains in 2020 is also higher than usual: "While the majority of returns would normally come from capital gains, a more typical year might see 15-20% of returns from clipping coupons". The strategy combines "core" positions, generally in stressed senior paper that may pull to par, with an anticipated IRR of 10-15% and "upside" positions, often in distressed names or special situations such as post-reorganisation equity with more optionality, targeting as much as 15-30%. In 2020 however, even some "core" situations have surpassed the "upside" return target.

Outlook

"We cannot annualize at 40% indefinitely, and there has been some repricing, but nonetheless we see a strong opportunity set," says Herrgott. Higher defaults are one driver: "We expect default ratios could for at least 24 to 36 months normalize at much higher levels than the very depressed levels seen in 2017, 2018, and 2019. A default rate of 3% to 4% is more normal for European high yield, based on a 20-year view. But whether default rates are 2% or 4% we will have plenty of opportunities. The key corporate events in early 2021 are debt re-financings, including bond issues, exchange offers, and restructurings. For instance, companies extending maturities may need to offer a higher coupon. M&A can provide optionality in some cases, but it is less predictable".

Hedged event trades

The strategy will adapt and evolve according to the opportunity set. In 2020 Herrgott has been tactically cautious on the short side, fearing equity short squeezes and noting the buoyant new issue market for bonds. Much of his short exposure was legs of event hedged trades: "Equity shorts ahead of restructurings were collapsed into long exposure obtained through debt for equity swaps. We only do these trades if we are confident in a full debt for equity swap, and if we can find stable stock borrow. Our prime brokers have good access to an illiquid stock borrow pool," explains Herrgott.

Alpha shorts

In early 2021 the pure short book is still quite small but that could change. "Some firms in competitive sectors were over-levered and had pressured business models even before Covid. It is still uncertain what the secondary effects of the pandemic may be on them, particularly once government support is withdrawn. These businesses got an extraordinary and temporary boost from government support but the competitive landscape has not really changed, and the question remains whether their capital structures, with bonds at or above par and low coupons, are sustainable. Government loan support and loan guarantee schemes have been adding artificial liquidity and layering on leverage, but once they are withdrawn, we would expect a larger short book," says Herrgott.

Quantitative screens on the short side look for profits warnings, red flags, high debt to EBITDA ratios, EBITDA adjustments, a high short interest in equity, and use the Beneish M-Score accounting score, which aims to identify manipulated earnings. "We generally want to see aggressive accounting and at least one more risk factor. A typical short could be trading at or above par, unsecured or junior in the capital structure, and paying a low coupon," says Herrgott.

Tail risk

Up to 1% or 1.5% per year could also be spent on tail risk hedges in future. "We have been spending much less than that recently, because having more idiosyncratic events in the book in itself protects us against market drawdowns," says Herrgott.

Activism and committees

The strategy may also evolve as assets grow. Herrgott has sat on creditor and restructuring committees in most European jurisdictions before and envisages doing so again: "Positions on a restructuring committee can create incremental value when we can help to shape the deal, build relationships with management, and encourage brokers to provide research coverage, especially post restructuring. At Sothic, I headed the restructuring of Concordia Bus/Nobina AB, the largest bus operator in the Nordics. We did a partial debt for equity swap, appointed one board member, ran the nominations committee and listed the business in an IPO. Though we were never the majority owner, we drove the restructuring and the value creation following it," says Herrgott. Liquidity remains important however: "We generally would not want to be restricted from trading for an extended period, and creditor committees can avoid restrictions by releasing MNPI," he adds.

The strategy received day one capital from investors including a large US endowment and a large single-family office and has attracted inflows every month. It currently manages $120 million. Herrgott estimates capacity of at least $500 million and is also constructive on the broader corporate outlook for Serone.

(Continued from page 5) complexity, clear catalysts or mis-pricings due to corporate restructurings create the potential for equity-like returns with less risk given credit protection. Giordano expects that record corporate debt issuance and refinancing requirements will lead to a wave of downgrades and defaults, creating an extensive and multi-year opportunity for his strategy. He also argues that diminished competition from bank prop desks and mature credit funds leaves smaller and medium sized distressed funds well positioned to take advantage of the impending cycle and recovery opportunities. Giordano was previously Head of Distressed Research at Goldman Sachs. He earlier spent over a decade as a senior analyst at Deutsche Bank distressed products group and started his finance career in Citigroup's global energy team. He has a BS in Finance and Accounting from New York University's Stern School of Business.

Lukas Goetz and Markus Schanta

Founding Partners and Co-Portfolio Managers
BlueBalance Capital
London and Vienna

Lukas Goetz and Markus Schanta founded BlueBalance, along with CEO Michael Schuelli, in 2019 to pursue a discretionary, non-directional global macro strategy focused on relative value opportunities exploiting macro inefficiencies and behavioural biases in derivatives markets. The approach has a low correlation to traditional financial assets, employs a rigorous risk-management framework and has a particular focus on downside protection. This is achieved by dynamically balancing a range of risk-on and risk-off (hedging) transactions that stabilize each other while achieving a strong overall income profile. Seeded by a leading Austrian insurance group, the UCITS fund offering, BlueBalance UCITS – Global Opportunities received *The Hedge Fund Journal's* UCITS Hedge award for best risk-adjusted performance in 2020 in the relative value macro category. The investment approach has a live track record showing a consistent Sharpe ratio above 1 dating back to the early 2000s and is being launched in an AIF vehicle in summer 2021. Goetz managed the strategy since 2010 at UNIQA insurance group. He has a Doctorate in Finance from Vienna University of Technology and an MSc from the ICMA Centre at Henley Business School. Additionally, he is the author of *Enhancing Alternative Investment Management*, a practitioner's guide to absolute return portfolio management. Schanta was previously responsible for the quantitative management of discretionary portfolios at Man Group and worked as a strategist at Goldman Sachs. Schanta holds a Master's degree from Columbia University in New York, where he received a Fulbright Scholarship, and a BSc from Vienna University of Technology.

Peter Greatrex

Chief Investment Officer
Boundary Creek Advisors
New York and London

Boundary Creek launched in July 2019 and is currently a team of fourteen with $1 billion of assets under management. The strategy is long/short high yield, focused on opportunistically identifying fundamental and technical credit inefficiencies and mis-pricings in Europe and North America, in bonds, loans, credit derivatives, structured credit and credit indices. The strategy emphasizes mid-sized high yield bond and loan issuers. The approach is not market neutral, but net beta exposure is kept within limits and many of the trade types are relative value or event driven. Prior to launching Boundary Creek, Greatrex was one of eight managing partners at BlueMountain Capital, where his roles over ten years included being a portfolio manager of long/short US high yield; long short UK/European credit; global head of research and global head of private capital. Greatrex earlier worked as a portfolio manager at JPMorgan. He has an MBA from Wharton and a BA in History from Middlebury College in Vermont.

Ivelina Green and Nick Pappas

Co-Founders, Co-Portfolio Managers
Broadstone Credit Partners
London

Ivelina Green and Nick Pappas founded Broadstone in 2021 to pursue a pan-European, middle market, special situations strategy. Record corporate leverage and uneven recovery from the pandemic across companies, sectors, and countries are creating opportunities in European credit. Broadstone focuses on mid-market investments below the radar of both larger funds and governments, where they can drive outcomes. The return target is 20% IRR through the cycle. The fund's strategy straddles public and private markets and has an all-weather approach to investing, which Green and Pappas believe is paramount in Europe where opportunities are less cyclical in nature. Broadstone Credit is named after the intersection of Broad and Stone Streets, the former headquarters of Goldman Sachs in New York City and where Green and Pappas first met 17 years ago. After Goldman, the two reunited at CQS where Green was a Partner and Head of the Special Situations Group, and Pappas was a Partner and Head of Credit. Their team led restructuring and deal negotiations in loan-to-own situations and crafted amicable solutions even in unfriendly jurisdictions. They restructured German outdoor apparel business, Jack Wolfskin, worked on retailer New Look's CVA and provided new money in several private situations. At Goldman Sachs, Green was Head of European Distressed Debt Trading, while Pappas was Head of EMEA Leveraged Finance Trading and Research. Pappas was earlier CEO of Europe and portfolio manager of European Distressed and Special Situations at BlueMountain Capital. Prior to that he co-headed US credit at Deutsche Bank in New York. Green has a BA in Economics from Brandeis University. Pappas has a BS in Biochemistry from Bucknell University. Green featured in the 2018 edition of *The Hedge Fund Journal's* 50 Leading Women in Hedge Funds report. Broadstone is a woman-owned business with Green owning 50% of the company.

Gretchen Guo and Joyce Meng

Partner/Managing Partner
FACT Capital Management
New York

Joyce Meng and Gretchen Guo launched FACT (acronym for fairness, alignment, compounding and transparency) in September 2019. FACT is a global investment fund with a micro-thematic approach to ideation, concentrating on a few sub-sectors within technology, consumer, and healthcare with favourable structural growth. Geographically, FACT is heavily focused on China and the US, with a concentrated portfolio of longs and absolute-return shorts. Longs target quality compounders with significant growth runway at a discount to intrinsic value, while shorts are catalyst-driven with negative variant perception. Notably, FACT applies a "first principles" approach to investment framework, transparency, research sharing, technology use, and structural principal-agent alignment. Since inception through April 2021, FACT has returned more than 50% net to investors. Meng was previously Partner/Managing Director at Vernier Capital and an investment analyst at MSD Capital and Goldman Sachs Investment Partners. As a Rhodes Scholar, she graduated with a MSc in Development Economics and a MSc in Financial Economics from Oxford University, as well as a BSc in Economics (Finance) from Wharton and a BA in International Studies from the University of Pennsylvania. Guo formerly worked in research for Ruffer Asia, Surveyor Capital and Sanford C. Bernstein. She has an MBA and MPP from Chicago Booth and a BA in Economics and Psychology from Harvard College.

Jason Horowitz

Senior Portfolio Manager, Head of US High Yield Bond Investments
CIFC Asset Management
New York

Jason Horowitz joined CIFC in 2019 and became senior portfolio manager of the CIFC long/short high yield strategy in February 2020, which delivered positive returns every month from February to December 2020. The strategy allocates to four sub-strategies mainly in the US high yield market: fundamental credit; technical credit such as credit ratings, sector, duration or ETF inclusions; credit arbitrage including capital structure arbitrage, intra-sector arbitrage and structural event trades; and low volatility credit. As well as alpha shorts, it uses a variety of hedges including individual bond shorts, options, CDS, indices and ETFs to protect individual trades or the overall portfolio. It can be accessed through UCITS or Cayman funds, and runs over $400 million of CIFC's total assets of more than $30 billion. Horowitz has been running long/short credit strategies since 2010, previously at Millennium Management and earlier at Muzinich & Co, where his UCITS strategy received *The Hedge Fund Journal's* UCITS Hedge award. His career began at Credit Suisse in equity and high yield research. He has an MBA from Yale School of Management and he graduated from Yeshiva University in New York.

Anant Jatia

Founder
Greenland Investment Management
Mumbai

Anant Jatia founded Greenland Investment Management in 2016 based on strategies employed for his family office since 2013 and has generated high Sharpe ratios since inception. The strategies, which manage more than $900 million, are primarily systematic global commodity arbitrage, based on fundamental linkages to exploit shorter term inefficiencies. They trade commodities globally and across commodity sectors for almost 20 hours a day. Sub-strategies include geographic, substitution and cost of production arbitrage. The strategies are based on proprietary logistic cost data from Greenland's sister physical commodity merchant business, Greenland (America) Inc., to determine the no-arbitrage fair value of transporting commodities across geographies. Techniques include proprietary algorithms, systematic portfolio construction and in-house ultra-low latency trading systems operating at millisecond frequencies with co-located servers connected via high speed leased lines on multiple exchanges in the US, Europe and Asia. Jatia previously co-founded quantitative investment manager Forefront Capital, which launched the first domestic hedge fund in India. He earlier worked as a portfolio manager at AQR. He has a BSc from Wharton.

Aman Kapadia

Portfolio Manager and Managing Partner
Akaris Global Partners
New York

Akaris runs a concentrated equity strategy, focused on the technology, consumer and industrial sectors, primarily in North America and Europe. The fund invests in structural winners – businesses with durable moats, low threats of disruption and long runways for growth. The firm adopts a bottom-up fundamental approach to underwrite investments on a three-to-five-year period. The fund can also invest in credit positions where they see equity-like return opportunities. The Akaris team includes Aman Kapadia's Fir Tree colleagues Brian Hinkes and David Sokoler, as well as Peter Henninger who came from the Financial Institutions Group at Goldman Sachs. Day one capital comes from the team and former colleagues at Fir Tree Partners, where Kapadia spent 11 years and previously co-managed a portfolio. Prior to this he was an analyst at Rockbay Capital, Severn River Capital, Sagamore Hill and McKinsey & Co. He has a JD/MBA from Harvard Law School/Harvard Business School and an AB in Public and International Affairs from Princeton University. The name Akaris comes from the Japanese word *Akari*, which means light, illumination and glow.

Dr Richard Klemm

CIO and Managing Partner
Stratome Capital Management
New York

Richard Klemm founded Stratome in 2020 to pursue a fundamental long/short equity strategy focused on emerging biotechnology companies: small and mid-caps mainly in the US. The process uses extensive and detailed proprietary data analytics to form views on early-stage biotechs' probability of clinical and commercial success and failure. Core, longer term investments in emerging science are combined with shorter term positions based on clinical, regulatory, and commercial catalysts. The opportunity set for the strategy is enhanced by innovation such as genomics enabling precision medicine, isolating molecules that cause diseases, and faster regulatory approvals of targeted therapies based on novel technologies such as gene therapy, gene editing, cell therapy and next generation bioligics. Biotech IPOs and M&A also provide long and short opportunities. Klemm was previously a partner at OrbiMed Healthcare Fund Management, covering small and mid-cap biotechs for long/short and long only public investment funds, and co-managing UK listed closed end fund, The Biotech Growth Trust. He has a PhD in Biology from MIT, and an AB with double major in Economics and Molecular Cell Biology from UC Berkeley. Klemm is a CFA Charterholder.

Brian Kuzma

Founder and Portfolio Manager
Thomist Capital
Houston, Texas

Brian Kuzma founded Thomist Capital in 2019 to pursue a primarily equity market neutral strategy focused mainly on clean and traditional energy, including E&P, refiners and chemicals but also considering related areas such as commodities, transport and industrial equities. The core strategy trades aggressively and can turn over 20 times a year while the opportunistic sleeve seeks one-off dislocations in energy and industrial equities, commodities and credit. The investment process emphasizes trading, behavioural edges, and positioning, such as short squeezes, rather than big data, and pays attention to commodity and credit markets. The strategy is up 173% between inception in March 2019 and April 2021, with annualized volatility in a range of 15-20%. Unwanted factor exposures are hedged, and stock-specific alpha has been the main return driver. Winning stock picks in 2021 have included energy transition plays in areas such as carbon capture; biofuel producers; and small cap post-bankruptcy energy E&P firms. Thomist firm assets were $110 million as of April 2021. Kuzma was previously a portfolio manager at Citadel, running equities for its global equities and commodities platforms. Prior to Citadel, he was a senior analyst at George Weiss Associates. His career began as an engineer at ExxonMobil. He has a BS in engineering from Cornell University.

Martin Larsén

Chief Investment Officer
Frost Asset Management AB
Stockholm

Martin Larsén is the co-founder of the fund Frost, which launched in January 2020. The fund, managed by Martin Larsén and Anders Augusén, is a fixed income relative value fund set up to exploit inefficiencies in the Scandinavian markets. The investment universe includes government bonds, covered bonds, municipal bonds, fixed income futures, FRAs, swaps, swaptions, and cross currency swaps. Frost is discretionary, but with extensive quantitative support to help the portfolio managers establish efficient positions. The fund's success will to a large extent depend on the portfolio managers' ability to correctly assess which instruments are mispriced in relation to each other. Judgement, knowledge, and experience of similar financial trading will prove very significant in this respect. The strategy, which was previously successfully run as part of the now closed Nektar fund, has delivered a strong risk adjusted return since inception and has very low correlation to equity and bond markets. Assets in the strategy are SEK4.5 billion, including an allocation from the Brummer Multi Strategy fund. Larsén was previously Deputy CIO of Nektar Asset Management AB, where he spent 18 years between 2001 and 2019. He completed his degree at the Faculty of Engineering at Lund University, which included studies at ETH Zürich.

Jimmy Lim

Founder, Chief Investment Officer and Chief Executive Officer
Modular Asset Management
Singapore

Jimmy Lim launched Modular Asian Macro fund in January 2020, raising close to $1 billion in assets from the founding partners including Matthew Cannon (COO), and Millennium Capital Management, where they worked before. The strategy is pan-Asian macro and uses modules made up of lowly correlated specialist country and product portfolio managers. Asset classes traded include cash and derivative instruments in onshore and offshore FX, fixed income, credit and equity indices across the more liquid Asian markets. Strategies include a mix of longer- and shorter-term trades. In addition to managing his own book, Lim decides on capital allocation amongst the others. There are strict downside risk controls on the modules and traders. Lim has generated a Sharpe ratio of 2 over his trading career at Millennium Capital Management and BlueCrest Capital Management. He previously worked for JP Morgan, Lehman Brothers, Merrill Lynch and Standard Chartered. He has a BBA from National University of Singapore and is a CFA Charterholder.

Luke Lynch

Founder and Chief Investment Officer
Aslan House
London

Luke Lynch founded Aslan House to pursue a hard event driven equity and credit catalyst strategy with a European bias. The strategy invests across the capital structure, with a focus on short duration, arbitraging the lifecycle of transactions. The firm has received a strategic investment from Investcorp-Tages and assets under management are now close to $200m. The portfolio has three strategies: merger arbitrage, credit catalyst and special situations. The merger strategy is highly selective, cherry picking deals on both the long and short side, while the dedicated focus on credit catalyst, including refinancing, calls, restructuring and regulatory change, alleviates reliance on M&A volumes. Special situations covers various capital market events including, but not limited to, index effects, tenders, exchanges and rights issues. Equity, credit, and interest rate risk can also be hedged. The strategy targets lowly correlated double digit returns through the cycle and has annualized close to 20% since inception in November 2019, with a Sharpe of 4 and no down months (including March 2020). Lynch was previously Deputy CIO and Managing Partner at Oceanwood Capital, from inception in 2006. Prior to that he was Lead Event Driven Analyst at Tudor Capital. Lynch has a degree in Psychology from Exeter University.

Tommaso Mancuso

Founder and Chief Investment Officer
Shikuma Capital
London

Tommaso Mancuso co-founded Shikuma Capital in 2020, with Marco Tosi, Tom Pontin and Anna McCutcheon. Shikuma pursues an unconstrained, liquid, opportunistic global macro strategy that seeks to outperform equity markets. The focus will be on delivering positive convexity rather than serving as a hedge to equities. The strategy includes medium term systematic asset allocation based on inflation, trend, and liquidity concepts; discretionary tactical trading that combines thematic macro trades and short-term trading, and tail hedging using options. The strategy generated a Sharpe above 2 in a personal trading account between August 2018 and March 2021. Mancuso was previously an Executive Director and Head of Multi Asset at Hermes Investment Management, where he ran strategies including a multi-asset inflation fund, a multi-asset ESG-focused strategy, and an absolute return strategy. He was earlier Head of Portfolio Management at multi-manager hedge fund solutions group Hermes BPK Limited, which he co-founded in 2008. Prior to that he was Global Head of Credit and Event Driven Strategies at Pioneer Alternative Investment Management. He has a Bachelors in International Finance from Bocconi University in Milan.

Sean Oldfield

Chief Investment Officer
System 2 Capital LLP
London

Sean Oldfield founded System 2 Capital in July 2019 and received a strategic investment from Stable Asset Management in 2020. Assets are around $200 million. The strategy is European relative value, seeking asymmetric trades and mis-pricings in single name bonds, CDS, convertibles, equities and options. The strategy opportunistically allocates amongst three buckets: senior versus junior, convertibles, and credit. It has a long volatility bias through cheaper single name volatility and also sells some more expensive volatility. It can opportunistically trade strategies such as cash versus CDS basis and can invest in shorter term restructuring situations. The strategy made 26% in 2020 with no negative months, and has shown a high hit rate, a high slugging ratio and strong performance in negative equity markets. Oldfield previously founded and ran a business, Castle Trust, focused on convertibles and private credit that was converted into a bank. He earlier worked for Macquarie Bank Limited as Head of the Public Market Strategies Group, trading public markets, activist investing and takeovers. Oldfield has a BCom in Finance and a Bachelor of Chemical Engineering, including a thesis in exotic swaption pricing, from the University of Sydney.

Bill Pang

Founder and Chief Investment Officer
Divergent Asset Management
New York

Bill Pang founded Divergent in 2020 with backing from two institutional investors and some proprietary capital. The liquid, market neutral event-driven strategy trades index rebalances, corporate actions, and other events, in forty-five developed and emerging markets. The strategy targets a high Sharpe ratio of around two, an even higher Calmar ratio, and low correlation with other hedge fund strategies. One sub-strategy, index rebalance trades, trades additions and deletions to equity indices, which relate to corporate actions and periodic reviews. Divergent has coded its own models for predicting index rebalance trades and follows an active and dynamic approach to take advantage of inefficiencies, which includes systematic trade execution. The manager also has a strong network of sell side relationships to access deal-flow on corporate actions. Pang previously worked at Millennium Management, managing a pod including a team of four, trading similar strategies. He was earlier employed in the trading departments of Bridgewater Associates and Goldman Sachs. He has a BA in Electrical Engineering from Princeton University, and competed in the USA and Canadian Math Olympiad. Pang serves on the board of New York educational non-profit Eduvision International, Inc. and has already given millions to charitable causes in New York.

Venkat Pasupuleti

Co-Portfolio Manager
Longchamp Dalton India UCITS Fund
Mumbai

Venkat Pasupuleti launched Dalton's India UCITS strategy in January 2020, which returned 24% (net of fees) in 2020, relative to the MSCI India index, which returned just 1.92%. The equity long/short strategy invests across all cap sizes with a focus on the small-mid cap space where Dalton has historically extracted most value. The long book seeks entrepreneurial companies benefiting from structural change themes, as India's economy accelerates towards middle income status and is expected to become a top three global economy by 2030. Trends include digital transformation and outsourcing; financialization of savings, low-cost manufacturing and affordable healthcare, and the largest sector weights are IT and financials. The short book can employ indices, baskets and currencies, as well as single names. The strategy follows Dalton's firm-wide investment philosophy of seeking strong cash flows and balance sheets, ESG best practices, a discount to longer term intrinsic value, alignment of interests, and strong track records including treatment of minority shareholders. Prior to joining Dalton in 2013, Pasupuleti worked as an investment manager at ICICI Lombard General Insurance Co. Ltd (erstwhile part of the Canadian Fairfax Insurance Group). He holds a BS in Engineering from Osmania University, an MBA from the Indian Institute of Management, Calcutta, and an MS in Finance from the MIT Sloan School of Management.

Joshua Pearl

Founder and Chief Investment Officer
Hickory Lane Capital Management LP
New York

Joshua Pearl founded Hickory Lane in July 2020 and the firm now manages assets of $160 million, including long-term capital from strategic investor Investcorp-Tages. The strategy focuses on fundamental long/short equity and special situations investing in the technology/media/telecom, industrials, and consumer sectors, in the US and developed markets. The firm also utilizes a top-down approach to identify long-term secular and structural themes to complement their bottom-up methodology. The strategy can also take a "suggestivist" approach towards management engagement and is ESG-focused with emphasis on corporate governance and board quality. The firm's shorts principally consist of direct idiosyncratic hedges against longs, as well as those that are being disrupted by, or donating share to their longs. Pearl was previously Managing Director and Partner at Brahman Capital, following the same sectors. Prior to that, he worked in leveraged finance and restructuring investment banking at UBS, Moelis, and Deutsche Bank. He is also the co-author of *Investment Banking: Valuation, LBOs, M&A, and IPOs* and *The Little Book of Investing Like the Pros.* He has a BS in Business from Indiana University's Kelley School of Business.

Fabio Pecce

Co-Founder and Chief Investment Officer
Ambienta X
London

Fabio Pecce joined Ambienta in 2019 to establish its public markets division, Ambienta X, and launch the environmental sustainability-focused absolute return fund in May 2020. The long/short equity strategy targets volatility of 6-8% and a Sharpe ratio above 1. It uses proprietary research and methodologies such as the Ambienta Sustainability Index to measure impact in public companies, based on resource efficiency and pollution control metrics, and benefits from the intelligence developed through Ambienta's long history of sustainable investing in private equity. The portfolio seeks twenty-five attractively valued and liquid longs that are positively exposed to sustainability-focused trends such as electrification, renewables, EVs, healthier consumption habits, green chemistry, recycling, building insulation and efficient heating. Shorts could be disrupted companies facing existential threats, such as polluters and inefficient companies: ICE auto-led components, hydrocarbon-based energy and utilities, traditional agricultural inputs, poorly invested steel and cement manufacturers. Shorts could also include over-hyped green bubbles or greenwashing stories. Pecce has three strong prior track records from Man GLG, J. Fredriksen Private investment office, and HBK Investments. He graduated in economics from Bocconi University in Milan.

Sebastian Schaefer

Managing Principal and Chief Investment Officer
Leibniz Group
Lucerne

Sebastian Schaefer founded Leibniz in 2012 to develop a suite of systematic, AI and machine learning driven asset management strategies, trading liquid markets: commodities, currencies, equity indices, rates, bonds and volatility indices. Leibniz`s team of seventeen builds proprietary algorithms for its strategies including pattern recognition, volatility arbitrage, momentum, swing trading, machine learning, and breakouts, all of which show low pairwise correlations. Combinations of these in-house strategies, like the Total Intelligence Multi Strategy portfolio, benefit from the different strategy approaches, and the Sharpe ratios of these multi strategy portfolios have reached 1.74 or more, the Sortino ratios are approaching 7.0 and there has been a negative correlation to equities and bonds between March 2016 and December 2020. Leibniz is also incubating various strategies in addition to those in the Total Intelligence program, including systematic macro and high frequency trading strategies. The current suite of strategies has holding periods ranging from less than 1 day to 40 days. Schaefer has experience of selecting early stage and developed hedge fund strategies from his fund of hedge funds management track record in other firms. Prior to launching his own investment firm in 2009 he worked as a Regional Head for Man Group plc, focused on bespoke alternative structures. He has an MA in Economics/Pharmacy from Heidelberg University. Leibniz is named after German polymath and philosopher, Gottfried Wilhelm von Leibniz.

Aaron Stern

Managing Partner and Chief Investment Officer
Converium Capital Management
Montreal

Aaron Stern co-founded Converium with Michael Rapps and Elliot Ruda in 2020 to pursue an opportunistic, multi-strategy approach investing in distressed and event-driven opportunities globally and across the capital structure, including activist equities, sovereign debt, municipal debt, and emerging markets. Previously, Stern was a partner and managing director at Fir Tree Partners, a multi-strategy investment firm, where he was responsible for distressed, special situations and event-driven investments globally. At Fir Tree he generated contrarian ideas in areas including sovereign and municipal debt, emerging markets, European banks and engagement opportunities in Europe and Asia. *(Continued on page 30)*

Co-Founder, CEO and CIO
Blueshift Asset Management
Red Bank, New Jersey

Mani Mahjouri

Uncorrelated 'quantamental' investing, fusing MFT and HFT

Blueshift's 'quantamental' trading sprung out of Mani Mahjouri's first love, which was physics: "Growing up in Maryland I was able to practice physics at the John Hopkins laboratory while I was in high school. I then studied math, physics and finance at MIT". The name Blueshift is derived from astrophysics, which several quants on the team studied to doctoral level, laying strong foundations for Blueshift's research environment. "Astrophysics problems are computationally intensive, based on modelling many underlying particles or bodies and understanding their aggregate behavior, which is like stocks. A stock is like a particle going through a system but based on different dynamics," says Mahjouri. In fact, most quants at Blueshift have no prior finance experience, and this is by design: "Studying finance theories can lead to crowded alphas but we are seeking unique alpha that is uncorrelated to other approaches. The route to this is studying the world with no priors, biases or pre-conceived notions. Scientists are great at taking that approach and reasoning from first principles," says Mahjouri.

Team chemistry

However, Mahjouri's first step into finance was at a firm where models were partly grounded in orthodox finance: AQR, which Professor Kenneth French at MIT recommended that Mahjouri apply to in 2000. "I was the twelfth person to join the firm and had the great privilege to work with Cliff Asness and John Liew in many aspects of building the business. The team remained united in its belief in quant principles, even though models were very much out of favour during the first dot com bubble. Indeed, when I asked Liew – who I regard as a mentor to this day – for advice on starting my own firm, he suggested that team chemistry and mutual respect would be crucial because any firm that lasts a long time will go through tough times. At Blueshift we tell investors that our team is our secret sauce. The chemistry developed over many years – going back to 2006 for some team members who worked together at Tradeworx. Investors were willing to back Blueshift on day one because they knew there was stability." Blueshift Co-Founders, CTO, Lewis Hyatt, and COO, Dmitry Sarkisov, also came from Tradeworx.

Bridging tech and quant

As CIO and Chief Strategist at Tradeworx, Mahjouri led a team that fostered synergies between tech and quant: "Whereas other firms siloed technology teams from trading teams, we put some of the most talented techies and quants in the world together to solve problems. This was a powerful source of edge, which led to efficient systems trading on microstructure phenomena such as HFT. Our team is united in our vision of implementing and evolving alpha-generating strategies and systems amid rapid alpha decay".

Designing datasets and systems

Tradeworx's novel approach to alpha generation created a hybrid between statistical arbitrage (mid-frequency trading, or "MFT") and HFT, intended to transform liquidity provision and institutional inefficiencies. This entailed a gargantuan appetite for data.

In 2017, a Rice University study ranked Tradeworx as one of the largest users of SEC data, on a list where most other firms ran up to tens of billions in assets under management. In 2013, Tradeworx had been retained to build the SEC MIDAS (Market Information and Data Analysis System). The Tradeworx dataset and systems are part of the intellectual property that Blueshift acquired when it spun out in 2018. "Our 20 years of data is a source of advantage, not only in itself but also because we built all of the HFT systems and wrote nearly every line of code. We have architected the system, so we know how long the data takes to affect stock prices and we have continuous snapshots of exchange latency, which can precisely measure all variables affecting the system and how alpha drives prices. The system has been battle tested through all the market turbulence of the past decade and has seamlessly transitioned from Tradeworx to Blueshift. We did not have to unplug a single cable and we transitioned with a trading hiatus of less than two weeks," recalls Mahjouri.

Quantamental investing

The data itself has evolved rapidly: "The Rice University study was really surprising at the time, but it is not actually a huge amount of data by today's standards. We have grown our ability to quantitatively understand the data and drive alpha through models," explains Mahjouri. Blueshift defines "quantamental" as using both systematic, quant-driven approaches and fundamental data such as news and events. "The juxtaposition of these is the modern advent of quant, which marks the start of a massive paradigm shift. We are viewing markets with atomic resolution and codifying how discretionary analysts think, with big and new data. The three key trends are an explosion in computer power, data and computational complexity. There are more phenomena to study and more questions to ask, and we can ask more nuanced questions in a non-linear world. All of this plays to our advantages and lets us systematize inputs," says Mahjouri.

For example, alternative data has further expanded the opportunity set in areas including higher frequency forecasting or "nowcasting". "Alternative data has become bigger and more granular than ever with billions of records being captured in the cloud, where we were one of the first financial firms to use Amazon's cloud offering. We gather traditional data as well as more opaque and subtle information. We can use shipping, credit card receipts or fill rates in shopping mall parking lots to estimate company sales and consumer spending before the trends become understood more broadly," says Mahjouri. Mahjouri has authored a book on alternative data, to be released shortly.

A pure play asset manager

Blueshift synthesizes years of development at Tradeworx – and also moved from a trading and technology business model to a pure play asset manager. (The technology consulting arm of Tradeworx was renamed Thesys Technologies and is independent of Blueshift.) "We wanted to spin out the trading unit because the team wanted to focus purely on institutional asset management. Though there were synergies between technology consultancy and trading, we wanted to function as an independent trading business. We also wanted to ensure that we could recycle revenue into the business and acquire talent, rather than sharing profits with a parent company. Most traders are entrepreneurial and Blueshift is majority owned by the staff. An independent company with clear corporate governance is also more attractive to investors," explains Mahjouri.

Anchor investors included pension funds and endowments, and no seed economics were given up. "We spoke to seeding platforms but determined that White Oak was the best fit for attracting stable institutional capital. Seasoned seeder White Oak did not actually provide seed capital but did provide working capital that allowed Blueshift to acquire intellectual property from Tradeworx. White Oak has also provided invaluable know-how and consulting, to help us build a world class business that meets investor requirements on cash controls, collateral and so on," says Mahjouri. Blueshift has a substantial team of 23, including 11 PhDs, and has been profitable from the start based only on management fee income.

Fusing HFT and MFT

Mahjouri has been close to the coalface of HFT since Tradeworx began it in 2008 and has watched the acceleration of timeframes. "The HFT process of dispersing inefficiencies by transferring excess demand, supply, risk and liquidity to other correlated names might have once taken place in pits or trading floors by specialists managing supply or demand, over days or weeks. It now happens much faster on an intraday basis and technology lets you identify dislocations at more precise levels." The arms race towards zero latency led to huge investments based on the laws and metrics of physics, of which Mahjouri had first-hand experience: "Traders dug through mountains to cut millionths of a second off the time between NYSE and CME and spent half a billion dollars laying submarine cables under the Atlantic Ocean. Because fiber optic cables made of glass are 30pc slower than air, there was a race for microwave tower bandwidth to send signals back and forth," explains Mahjouri.

Yet Blueshift is not competing in this race – partly because it is a precarious game: "Being the fastest trader is a tough seat and not necessarily a stable one because you cannot control the next innovation. We have colocation and microwave towers, but we never depended on being the absolute fastest. We survived the HFT arms race without spending the most – through innovation and scrappiness".

Indeed, Mahjouri sees more compelling opportunities in the mid frequency space: "The ultra-low latency game is about risk transfer at very short time horizons for very high Sharpe ratios. It is very capital intensive on infrastructure, and limits firms to intraday time horizons because they cannot get leverage overnight and have abnormally high risk aversion, especially overnight, which limits the amount of liquidity at that time horizon. That also leaves a lot of alpha on the table to apply the same liquidity provision techniques to longer, multi-day holding periods. This is an underserved area of liquidity that used to be handled by investment banks. If we buy on the bid our goal is to sell on the offer, but we have to await liquidity to do this," says Mahjouri.

HFT is used for both alpha signal generation and trade execution, which is monitored closely. "We obsessively keep close track of execution efficiency and nearly always beat the VWAP by capturing bid-offer spread."

Multiple uncorrelated models

HFT and MFT are fused in the value and liquidity provision strategy, which uses statistical and information arbitrage for factors and behaviours. "We think it is pretty unusual to fuse HFT and MFT. We can axe our bid or ask in ways that do not make sense in a two-sided market, because the MFT motivates that axe, based on our history of over a decade's worth of the most detailed level of market microstructure data," explains Mahjouri.

The other models are information arbitrage, quantamental anticipation (using alternative data), and exotic book alpha based on flows and volumes.

Blueshift uses machine learning to develop and refine models but follows a supervised hypothesis-based approach rather than a "letting the data speak" approach: "We are prior-driven and use discretion to formulate a hypothesis. Within that context, we do also use machine leaning to formulate how the data impacts stock prices".

Correlations amongst the strategies are near zero, and all have made positive contributions to performance over time: "Whatever the market regime, there is always some dynamic at work". Risk budget allocations amongst the five strategies are roughly equivalent ex ante, though there is some flexibility as opportunity sets ebb and flow: "For instance, the value and liquidity provision strategy can automatically scale up to take advantage of higher bid/offer spreads when an event such as Covid or GameStop hits the market and increases trading volumes and demand for liquidity. Conversely, the Covid crash made some fundamental data such as historical 10Ks less relevant, and those signals scaled down," says Mahjouri.

The models have stayed robust and survived extraordinary market conditions including deleveraging events, and unexpected exogenous events that have wrong-footed some quantitative strategies. Most of the other strategies traded by Blueshift were also traded at Tradeworx, though they have been adapted to multi-day holding periods. Traditional quant factor approaches performed poorly in the past few years, and especially in 2020 partly because momentum became overcrowded and this was amplified by the split between Covid winners and losers, which led to extreme divergence. 9th November 2020 saw a huge momentum crash as Covid names rallied, and this dislocation set up a massive opportunity set for some of Blueshift's models. Leverage can go up to 6 times to take advantage of opportunities.

The strategies can also be adapted to long-only mandates, and Blueshift's NOVA platform can offer joint ventures to asset owners that could involve sharing technology, data, risk and research. "We feel confident about sharing this and offering customization without giving away intellectual property, because we are sharing aspects of expertise that would anyway be difficult to generate in-house. We can work with some of the largest and most sophisticated institutional investors to use our tools, technology, and platform to help them solve their complex investment needs, such as a desire to improve their analytics, execution, or alphas," says Mahjouri.

Co-Founder and CIO, VantageRock Strategy
Rockefeller Asset Management
New York

Avery **Sheffield**

Contrarian, ESG-aware, long/short equity

"The Vantage name symbolizes investing with the broadest vantage point for incorporating micro and macro factors and for navigating trading dynamics in all market environments," says Avery Sheffield. Her value-oriented investment style is distinguished by low, but variable net exposure, short selling of single stocks, ESG integration including proprietary analysis, and ferreting out alpha from non-traditional research.

Since childhood, her grandmother's stock investing inspired a passion to become a portfolio manager, though she only achieved the dream after a decade of experience in other industries and a Wharton MBA. Working in other industries: m-commerce and multimedia messaging; consulting for wireless technology and health firms; and executive search, has given her some different perspectives: "It provided valuable insights into companies' strategic and operational positioning, probability of success on new initiatives, and the importance of leadership and management team quality. This was a real grounding in the realities of execution challenges in dynamic industries, which matters because we are not just investing in numbers on a chart". During this time, she had also been reading *The Wall Street Journal*, classic investing books, and personally investing in thematic and geographic areas that were undervalued globally, before applying to Wharton.

Upon graduating from Wharton, her first finance role in 2007 was in sell side equity research. "Sanford Bernstein appealed partly because I was wary of joining a bank with leveraged exposure to the housing bubble, but also because I believed their strong fundamental-based process would lay the foundation for portfolio management," says Sheffield. Her first step into professional investment management was as part of the US large cap value team at Brandywine: "This gave me the chance to apply analysis to a wider range of sectors, including consumer, health, and technology, and pitch under-appreciated ideas for an $8 billion fund". Sheffield also got her first taste of short selling at Brandywine, when she was tapped to run an internal hedge fund set up in 2015. Then, after a brief spell running the VantageWay long/short strategy at MSD Capital, Michael Dell's family office, she moved over to Rockefeller Asset Management, which expedited the re-launch of the strategy with seed capital from her and her co-founder, and of course operational infrastructure. "We are excited to have another female led strategy at Rockefeller Asset Management and to bring our clients a differentiated approach to navigating volatile markets," says Laura Esposito, Managing Director and Head of Institutional & Intermediary Distribution at Rockefeller Asset Management. "Over the years, my investment style has remained consistent, though I have become more confident in trusting my analysis and instincts and sizing positions larger – perhaps up to 6-7% from 2-3% before," says Sheffield.

Low and variable net exposure

The strategy has had a strong start thanks mainly to alpha, though limited directionality has also added some value. "Net equity exposure is low in an effort to reduce volatility and correlation," says Sheffield. The net typically fluctuates in a range between -20% and +40%, mainly because of bottom-up stock picks but also market moves. In 2020, the strategy was net short and net long at different times: "In early 2020 we were net short, as we were finding it hard to identify longs with compelling asymmetric risk/reward, many companies seemed overvalued, and risks in China were potentially under-appreciated. We were fortunate to cover multiple shorts at the market trough in March 2020. A moderate net long stance was maintained until autumn 2020 when we could see compelling near-term upside on longs with a margin of safety. We saw strong upside in consumer discretionary where our estimates were above consensus, regardless of the vaccine. But we peaked at approximately 40% net long".

Single stock shorts

Since mid-December 2020, the portfolio has become less directional: "It has ranged from neutral to slightly net short as we found fewer compelling long opportunities – and identified more compelling short candidates that we believe are greatly overvalued. Growth and momentum have reached extremes and those styles are seen in many shorts". Growthy one-off Covid winners are a particularly strong theme: "Many companies that were significant beneficiaries last year are unlikely to be as successful this year – and some may even contract and see negative free cash flows".

Though there are themes in the short book, it is comprised of single companies rather than baskets, sectors or indices: "We only short single names because we want to focus on the idiosyncratic risk of individual companies, rather than shorting an index that might include companies we believe are under-valued. When our catalysts play out, individual stocks can move against the general direction of the indices, providing opportunity for successful shorting even in an up-market".

Shorts are in stocks inflated by optimism, but Sheffield is also pragmatic and tactical in trading around sentiment: "Markets can stay irrational for longer than an investor can stay solvent, so we try to use our trader savvy to be tactical on the short side. We monitor our holdings' macro conditions and their competition, which might lead us to downsize the position in an effort to minimise near term risks so we can be more offensive later. I have also become more confident at identifying when shorts could fit the market view". Extremes of either positive or negative sentiment and positioning can pose challenges for short sellers, as seen in short squeezes in January 2021. Sheffield typically avoids overcrowded shorts and is highly mindful of stocks with high short interest.

Factor tilts

In terms of factor exposures, "I am more inclined to short growth and momentum but seek to identify near term catalysts for disappointment and company-specific reasons," says Sheffield. The strategy's long book has different factor and style exposures: "I have always been a tried-and-true value investor, seeking asymmetric risk reward," says Sheffield. The rotation from growth and momentum to value since November 2020 has therefore been a tailwind for the strategy but is not a precondition for producing strong absolute returns: "I have also successfully navigated different types of market regimes. Value has been underperforming for years. If the market is being purely driven by growth and momentum, I may underperform but I am not interested in chasing returns that are not grounded in fundamentals".

Misunderstood longs

Sheffield and team follow a few hundred stocks, across sectors, but with a focus in consumer and TMT. The long book will typically contain 20-40 names, though monitoring the news-flow across the whole universe generates ideas for new long and short positions and provides read-throughs for competitive dynamics. These mid to large cap names with market caps of at least $1 billion will tend to have some sell side coverage and Sheffield finds that, "sell side research is useful, especially for company history, sentiment and trading dynamics – even if I may not always agree with its conclusions. Longs should be undervalued, and misunderstood due to company-specific cyclical or secular factors. Some positions that already have positive sentiment may be sized smaller".

The strategy has little overlap with many hedge funds. One analysis showed no similar long exposure, but rather a few short positions, in a list of the 100 most popular (long) hedge fund stocks. Sheffield also argues that the low valuation of her long book shows how out of favor it is. The definition of low valuation is somewhat nuanced. "The stocks appear to be lower valued compared to sector peers or the market, but not necessarily cheap against their own history if fundamentals are challenged. In the managed care space, for example, people feared that Obamacare would be negative, but the entire sector re-rated on better fundamentals."

Popular megatrends can throw up contrarian opportunities. For instance, the big picture bifurcation between growing e-commerce and declining brick and mortar retail has reached levels that can obscure positive change at individual companies: "One theme in the portfolio is how consumer retail companies are not only reinventing themselves through e-commerce channels but are also becoming more adept at managing inventory and optimizing sales promotions. These firms appear to be undervalued versus the market and could be on the cusp of re-rating," says Sheffield.

ESG, engagement and proprietary ESG research

Rockefeller Asset Management has a 30-year history of ESG integration, including a dedicated ESG engagement team, and has also developed some thematic strategies that are labelled as ESG. The VantageRock strategy leverages this deep ESG expertise as a way to potentially generate alpha on both the long and short sides.

"Some longs may be ESG improvers where ESG is material to the investment thesis – while some shorts have under-appreciated risks including ESG considerations, and may be classified as ESG decliners," says Sheffield. Research, generated by Rockefeller Asset Management's ESG team, has shown that ESG improvers have generated positive alpha while ESG decliners have produced negative alpha, over time. Some ESG improvers have seen considerable valuation expansion in 2020, and one portfolio company re-rated to the point where it reached our estimate of fair value. The VantageRock strategy will not own every ESG improver: "In some cases, we are patiently waiting for them to get cheaper". With many companies making a big effort to burnish their ESG credentials, it might seem superficially harder to identify ESG decliners. "There are plenty of corrupt companies out there. One short theme is healthcare companies that have been exploiting government or insurance company reimbursement loopholes. Legislation now creates a clear catalyst," says Sheffield.

One member of Rockefeller's ten strong Global (ESG Integrated) Research team has joined the VantageRock team. The team also collaborates with the wider Rockefeller team in other dialogues with companies for perspective and insight on controversial issues. "Rockefeller's ESG engagement team speaks with many companies each year, and their findings can inform our views. The team's work is more focused on companies that the firm owns or looks to own, but the team's work also can reveal companies that do not respond to ESG engagement. Rockefeller's own ESG research is often timelier than the data underlying ESG ratings, and it can uncover ESG issues that could be overlooked by more formal ESG metrics. Sheffield finds that, "Rockefeller can have an edge where its ESG analysis is updated more frequently and proactively than those from some ESG ratings agencies".

Rockefeller also devotes equal attention to the E, S and G because their relative importance varies between companies and sectors – materiality matters. Sheffield finds that, "the emphasis on environmental can leave the G and S under-appreciated. In terms of governance, changes in management and board can be very important. Social factors can be quite relevant for consumer companies, for example".

Non-traditional alpha

Proprietary ESG analysis is one example of non-traditional alpha and other sources of alpha include alternative data and behavioral biases. "We use alternative data, but it can be over-relied on. People can pay too much attention to credit card data and not enough on what is happening to a business," says Sheffield. Having worked in and around the Silicon Valley venture capital space, Sheffield keeps abreast of disruptive trends and new business models in private companies – and sees two-way traffic with public companies: "Managers will often leave public companies to go to private companies and create disruption, which then spurs innovation or acquisitions at their former company, and investors often underappreciate the ability of the former company to turn around".

Her study of neuroscience has not led to direct investments in neuroscience biotech stocks yet, at least, but it does more broadly help to inform an awareness of behavioral finance and human psychology biases: "Anchoring and herding are the two biggest biases we see now. If one company does very well, everyone anchors to its valuation, which makes the anchor stronger and stronger, until negative catalysts come along. If you can disprove the validity of the anchor, there can be a short case among many companies anchored to its valuation. We often have a counter-consensus view".

Co-Founder and CIO
SAVIN
Amsterdam

Iain Somers

Uncorrelated alpha from opportunistic and innovative arbitrage

Iain Somers co-founded Amsterdam-based SAVIN in 2020 after more than 20 years of trading, including nearly six years between 2012 and 2018 running an arbitrage/relative value strategy, Done Hedge Fund, which generated a Sharpe ratio of 1.4 with average annual returns around 7%, no correlation to equity markets, and only one losing year. "Its worst 12-month period saw a loss of 7%, when volatility was low and pretty much everything went wrong and nothing went right," he recalls.

This resilience has also inspired the firm's name, derived from the Latin name for the juniper plant, which flavours a Dutch gin called "genever" and grows in some of the harshest conditions. SAVIN co-founders and partners: Managing Partner and co-CIO, Bas Emmerig; Partner and Head of Volatility Trading, Ricardo Westra, and Head of Business Development, Erdem Yavuz, have survived and thrived through over 20 years of diverse financial markets including crises. "We have deployed a wide range of strategies in different circumstances. The coronavirus crisis was not our first crash, and it will not be our last one. There are always surprises and unknowns in the markets and we have learnt that the good way and the bad way," says Emmerig.

The four have spent much of their careers working at Dutch proprietary trading firms, such as Market Wizards, Optiver, and EDU traders, where Somers in 1997, then aged 19, became the youngest trader on the Amsterdam exchange. "These firms have a strong derivatives trading culture and a tradition of teaching and training traders. They also have a strong focus on risk management and downside risk," explains Emmerig. Prop trading does not always easily translate into fund trading, but in SAVIN's case there is a lot of continuity: "Though funds normally trade a lot less – and it is difficult to do HFT in a fund structure – the focus on capital preservation is strong and we do not actually use any less leverage now than when we were prop trading," says Emmerig.

SAVIN's investment process uses a mix of deep fundamental analysis and proprietary quantitative trading and risk models, developed by a dedicated quantitative team: "Three young quantitative analysts have been hired, with two specialized in applied maths and one in artificial intelligence. They are part of the development team, and they help with modelling strategies and backtesting," says Somers.

An unconstrained suite of strategies

The fund is market neutral, hedges currency risk, and has a near zero correlation to equities but within these constraints, SAVIN are totally opportunistic in allocating capital amongst their current suite of strategies – and are always alert to potential new ones in the pipeline. "We look to construct a balanced, flexible and liquid portfolio. Every year the markets get tougher, but our models get better. There is always some overcrowding that makes some arbitrages disappear – but people always make mistakes and other opportunities emerge," Somers has found.

Volatility arbitrage

"In early 2021, we are seeing some pretty unique opportunity sets that are much better than those seen in the last couple of years," Somers points out. In its first three months of trading, February, March and April 2021, SAVIN has made about 12.5% net of all fees thanks mainly to some specialised volatility arbitrage strategies. "We are continuously modelling less well-known single name equity arbitrages, based on cherry picking dislocations and set ups in areas such as dispersion and calendar spreads. We find many opportunities for spreads between instruments. For instance, the volatility spike at the end of February and early March created dislocations and market imperfections, including some strategies in small and mid-caps," says Emmerig. Each trade is carefully crafted: "We have unique ways to construct and engineer trades, with unique instruments, based on the experience of Iain, Ricardo and the quant team," he adds. There is some automation, but this is not an algorithmic strategy, and some trades are manually executed.

Over these three months, about 85% of the risk has been in the US with 15% in Europe, but as with the strategy weightings this is flexible – and more capital could be deployed in Europe when it presents better opportunities.

Equity relative value

Other strategies in the repertoire include share class arbitrage, which can look at price differences between two or more share classes from the same issuer that may have different voting rights, dividends, liquidity or domiciles. These trades are mainly motivated by mean reversion: for instance, when discounts between share classes widen out, the strategy may anticipate some reconvergence in some selected cases. Sometimes corporate events such as buybacks or mergers of share classes can collapse a spread, though this can also eliminate future opportunities. After Unilever unified its share classes in November 2020, the differences between the Amsterdam, London and New York listings were no longer interesting for SAVIN to trade. Individual trade selection is every bit as opportunistic as the top-down strategy allocations. SAVIN might at some stage be monitoring 250 arbitrage relationships but could only be exposed to between 20 and 40 of them at any time.

Holding companies are another trade type where there can be volatility in discounts and premiums – and this is partly because different opinions exist about how to define and measure valuations. "Whether some holding companies such as Swedish Match trade at a premium depends on how you value their unquoted assets," points out Somers. Some holding companies can trade at a negative implied enterprise value – for instance French auto maker Renault has sometimes traded below the value of its stake in Nissan. This may seem to be an extraordinary anomaly, but Somers keeps an open mind about the reasons for such situations: "A negative enterprise value might make sense if a company is losing money, or it could be a market inefficiency caused by overreaction". SAVIN generally wants to avoid over-crowded holding company trades, though they might look at them in extreme situations.

In event driven trades, SAVIN also stays away from more crowded areas such as merger arbitrage. SAVIN is more likely to trade other post-announced events, such as spin-offs, asset sales and re-capitalisations.

SAVIN's trades are hardly ever based on "fungible" situations where one asset can be swapped for another to crystallize a discount or premium. Unlike some of the Dutch proprietary trading houses, they do not trade ETFs versus constituents.

Tail risk

Higher market volatility can typically somewhat improve the opportunity set for some of the strategies, and the volatility arbitrage book already has a somewhat long vega volatilty bias, but SAVIN also runs a tail risk sleeve. "Our tail risk hedging strategy is designed to protect against extremely rare events and to outperform in difficult market circumstances. More so our strategy is designed to act as an automatic stabilizer, providing us with a source of liquidity at a time when many funds are locking assets in. Liquidity that will ensure the ability to profit from the massive dislocations arising from these events. In many respects our tail risk strategy should be considered as a form of risk management rather than a stand-alone strategy," says Emmerig. "If markets do have a rout, the policy is to monetise part of the tail risk hedges but also to always retain some exposure, so that we are not timing the tail risk too much." On average, SAVIN intend to spend between 0.10% and 0.30% of the fund per month on tail risk hedges, and this insurance could start to pay off in environments of extreme volatility or meltdowns.

A modern operational structure

SAVIN pursues some of the same relative value strategies as Somers' previous hedge fund Done, and the same investment objective of generating uncorrelated alpha, but the organizational and operational structure is very different this time around: "We have learnt a lot about how to run a fund. Everyone has their own role, resulting in a clear focus on the return side and asset side of the business," says Emmerig. Somers' remit at Done included asset raising, investor relations, and dealing with regulators in addition to portfolio management. Today at SAVIN, Somers and the trading team can solely focus on what they are great at and really enjoy: the hands-on research, modelling of new strategies and trading. They do not have to worry about other time-consuming functions such as prospectuses or spending too much time with investors. Yavuz handles asset raising and investor relations and Emmerig runs the day-to-day business, while also having some responsibility for risk management and oversight, which is informed by his own experience of running a quite different macro long/short equity strategy at BMD2.

Other functions are outsourced to the appointed full scope AIFM, Privium Fund Management BV. These include compliance and risk management – where Privium has a power of veto. Privium provides professional support and infrastructure and is responsible for areas such as regulatory reporting. Privium has also selected some other service providers: an independent depositary, Darwin Depositary Services, and independent directors, Teslin Trust Services B.V.

ABN Amro Clearing Bank has been chosen as prime broker, partly for its strong derivatives risk management systems, and it provides a third level of risk management on top of SAVIN and Privium. Executing brokers such as Morgan Stanley are also used, and more counterparties may be added as the fund grows. ISDAs are needed to access some markets. Most of the back office is outsourced to administrator, Circle Investment Support Partners.

Assets and alignment

SAVIN's founders could have contemplated launching another proprietary trading firm or rejoining their former employers but decided that a fund structure could offer more growth potential, with potential to run at least a few hundred million in the strategy; the Done hedge fund had peak assets of EUR 140 million. Initial marketing efforts are focused on the Netherlands and Switzerland.

Assets of EUR 20 million were raised pre-launch and have almost doubled as of April 2021. Investors included some previous investors in the Done hedge fund, who were pleased with how it returned capital to investors in early 2018. "Most of the portfolio was liquidated within two weeks, all of it within two months and all investors were treated fairly and equally, with their interests put first," says Somers.

Other early investors are the SAVIN founders, high net worth individuals, family offices, former hedge fund managers and some old colleagues from various proprietary trading houses. No economics in the management company were given away, but early investors get a share of management fees once assets are above a certain level.

"This matches the principle of reciprocity. Our other core principles are authenticity and transparency, summed up by saying what you do and doing what you say. We have set up this firm at the crown of our careers partly with a vision to transfer knowledge and expertise to the next generation of traders and portfolio managers of the future," says Emmerig.

(Continued from page 23) He most recently led an innovative restructuring of Puerto Rico's Government Development Bank and a campaign to improve governance and shareholder returns at a recently privatized Japanese railway operator, Kyushu Railway Co. Prior to Fir Tree, Stern held investment roles at O.S.S. Capital Management and Millennium Management. His finance career started as an investment banking analyst in Credit Suisse's leveraged finance and restructuring groups. He has a BA Commerce, with a Major in Accounting, from McGill University, where he is a global expert and guest lecturer.

John Thaler

Founder and Portfolio Manager
Hampton Road Capital Management
Greenwich, CT

John Thaler founded Hampton Road to pursue a fundamental long/short equity strategy focused on the TMT, consumer, travel, leisure, and gaming sectors globally. Thaler launched the strategy on January 1, 2020 as the sole portfolio manager of the Wexford Core Equities Fund and spun out of Wexford Capital to form Hampton Road in Q4 20. In December 2020, Leucadia Asset Management and Hampton Road entered a strategic relationship in which Leucadia invested long-term capital into the firm. Hampton Road returned 47% net in 2020 and is up over 15% net through March 31, 2021. Hampton Road maintains relatively low net exposure and attempts to minimize unintended factor risk to allow stock selection to drive performance. The portfolio's lower steady-state exposure is designed to keep volatility relatively low, which allows the firm to play offense in market dislocations. Previously, Thaler founded JAT Capital Management, which had peak assets of more than $3 billion. Thaler began his hedge fund career at Shumway Capital which he joined in 2002 as an analyst and eventually became a portfolio manager. Thaler also previously worked for Spectrum Equity Investors managing private TMT investments, and started his finance career in telecom M&A and corporate finance at Merrill Lynch. Thaler graduated from The University of Chicago with a BA in Economics.

Dr Theodoros Tsagaris

Founder, Chief Executive Officer and Chief Investment Officer
Bayforest Technologies
London

Dr. Theodoros Tsagaris founded Bayforest in 2017. Bayforest has grown steadily since launch with the support of family offices, funds of funds and large institutional investors. Assets are currently ~$400 million and the strategy generated strong performance in March 2020. Bayforest seeks high conviction alphas over shorter time horizons from minutes to days, which are intended to be uncorrelated to traditional and alternative benchmarks. It trades futures and single stocks with a detailed plan to expand into other assets. Analytical techniques used include Bayesian inference and statistical learning with technology including ultra-low latency and connectivity from tick to trade, as well as proprietary execution algorithms. Tsagaris was previously a senior portfolio manager at Tudor Capital Europe, trading short duration systematic strategies. He was earlier a senior portfolio manager at GSA Capital LLP. Prior to that he was a senior quantitative trader at BlueCrest Capital Management working on systematic trend following and quantitative equity market neutral strategies. He has a PhD in Mathematics from Imperial College London, and a MSc in Statistics from University College London. Tsagaris has authored articles on real time statistical learning in academic journals.

Christian Vogel-Claussen

Managing Partner and Chief Investment Officer
Alanda Capital Management
London

Christian Vogel-Claussen founded Alanda Capital Management in late 2017. Its flagship public market strategy is long/short equity, focused on the TMT, consumer and business services verticals. The mandate is global, but the focus is on Europe. Alanda runs a high conviction concentrated book, typically with 15 longs and 15 shorts. The team combines fundamental analysts and programmers, integrating data science to exploit proprietary alternative datasets and techniques to model corporate earnings and carry out forensic accounting. The strategy has net annualized at approximately 21.5% from inception to December 2020, including 59% in 2020, and has made absolute returns on both longs and shorts. The short book has included frauds such as Steinhoff, NMC Healthcare, BIO-ON and Wirecard, and it also seeks structural shorts with bad corporate governance. Separately from the hedge fund but instrumental to the next generation investment philosophy, Alanda has a private pre-IPO crossover strategy, which has had exposure to global tech leaders such as Meituan, Revolut, Instacart, ByteDance, Marqeta, Bolt and OakNorth. Out of this, three companies are set to IPO in 2021. By running a public-to-private crossover strategy, it allows Alanda to benefit from the cross pollination of ideas, insights, and connections from both sides of the business. Vogel-Claussen was previously co-founder and CEO and Co-CIO of Astellon Capital Partners, an investment manager at Laxey Partners and an investment banker at Morgan Stanley. He has an MA from the University of St Gallen.

Aaron Weitman

Founder, Managing Partner and Chief Investment Officer
CastleKnight Management LP
New York

Aaron Weitman founded CastleKnight Management in 2020 after spending more than 15 years at Appaloosa Management. He started as an intern at Appaloosa in 2002, working his way up to Senior Partner over his time with the firm. CastleKnight launched its event driven/special situations hedge fund in October, which is up over 63% net of fees in its first 6 months. Appaloosa founder, David Tepper, has been a significant investor in the fund since launch. CastleKnight invests opportunistically in the equity and debt of companies of all sizes, marrying a macro-aware approach with a deep fundamental research process. The firm seeks to identify differentiated investments ahead of the crowd, targeting de-risked, mispriced securities with asymmetric return profiles, under-appreciated intricacies to their capital structures, and catalysts to drive returns. Catalysts can include sharp changes in business operations, potential monetizations, corporate actions, regulatory developments, and/or reorganizations of capital structures in industries in which the team holds deep knowledge. CastleKnight also has the ability to create its own catalysts, when appropriate. The fund will be dynamic in its allocation to equity and credit based on the opportunity set, and it has roughly two-thirds of its portfolio in equity and one-third in credit today. The firm uses a variety of instruments for shorting and hedging, including broad market and sector hedges, baskets, and single-name alpha shorts across equity and credit. Weitman has a BS in Business Administration from Carnegie Mellon University. He sits on investment committees for various charities and foundations.

Scott Williams

Founder, Chief Investment Officer and Chief Executive Officer
Fiftyone Capital Pty Ltd
Perth

Scott Williams co-founded Fiftyone Capital in April 2018. Fiftyone manages the Progressive Global Fund, a global long/short strategy, which has annualized at 20.2% from inception to March 2021. It combines longer term core positions with trading positions in developed markets globally. The fund emphasizes capital preservation, and historically had a downside capture ratio of less than 15%, a Sharpe Ratio of 1.8 and half the volatility of its benchmark. The Progressive Global Fund invests in thematics with asymmetric upside, and can increase exposure through "positive activism", which structures deals/trades including advisory fees/lead manager options, which accrue to fund investors and accelerate returns. Fiftyone's current macro view envisages a new commodity super cycle, expresses views on gold, iron ore and uranium, and taps into related deal-flow in Western Australia. Equity shorts tend to have overvaluation, worsening fundamentals, and excessive leverage. Fiftyone disseminates its proprietary company research where appropriate. Additionally, investors are offered co-investments opportunistically, including private equity, private debt and infrastructure. Williams previously worked in corporate finance and stockbroking. He has a B Com in Finance and Property from Curtin University of Technology in Perth, Australia.

William Wyatt

Founder and Chief Investment Officer
The Donerail Group
Los Angeles

William Wyatt co-founded The Donerail Group with Wes Calvert, Andrew Bowman and Craig Pollak and launched its flagship hedge fund in February 2021. Donerail pursues a concentrated, value-oriented, activist strategy with a focus on small and mid-cap companies with market caps between $750 million and $2 billion in the consumer, industrial, media, and real estate sectors. Although the flagship fund has only recently launched, Donerail has had several successful public campaigns in the past year that it managed through co-investments: in March 2020, the firm was successful in its push for the $6 billion merger of MobileMini and WillScot, and in October 2021, the firm was reported to have a large stake in MasterCraft Boat Company. MasterCraft stock has appreciated over 50% since Donerail's reported involvement. Donerail launched its flagship fund with ~$270 million of committed capital including a strategic investment from Harbert Management Corporation, which provides operational support, as well as working capital. Wyatt was previously a partner and portfolio manager at Starboard Value, a $6 billion activist fund, where he also served as the Head of Event Driven investing. Prior to Starboard, he held various executive roles at Empyrean Capital and Magnetar Capital. He began his career at Goldman Sachs. He has a BA from Tulane University.

2021
Tomorrow's
Titans

Co-Founder
Alpha Blue Ocean
Nassau, Bahamas

Pierre **Vannineuse**

Innovative bespoke public SME financing solutions

CEO Pierre Vannineuse co-founded Alpha Blue Ocean (ABO) in 2017 with COO Hugo Pingray and CFO Amaury Mamou-Mani. The trio have known each other since business school and run ABO as a triple family office. ABO continues the strategy that was pursued by another family office Vannineuse ran, Dubai-based Bracknor Investment Group, between 2015 and 2017.

ABO provides innovative financing solutions for frequently innovative smaller public companies listed on over 30 exchanges globally. The structures can be debt, equity, or hybrids such as convertibles, generally structured as PIPEs. ABO closes an average of 20 deals per year, with an average size of $20 million, but might set a record of 50 in 2021 amid buoyant equity markets and abundant liquidity. "We want to be part of the party right now, and we might even accept smaller returns than normal," says Vannineuse. "Many banks will not lend to these companies, and some of them are too young to do placements. We provide a bridge towards maturity and taking advantage of capital markets." ABO is versatile: it provides working capital; refinances debt; offers shorter term bridge finance and longer-term growth finance, as well as recapitalizing companies on the verge of bankruptcy. It also finances very specific projects, particularly clinical trials for drugs.

Deal-flow can come from equity advisors, corporate brokers, and both boutique and bulge bracket investment banks, and from its own network including relationship-based repeat business: "We are the largest dealmaker in France, which is very much a trust and relationship-based market," says Vannineuse. ABO's executive team includes venture partner Frederic Sutterlin, who was hired from Societe Generale's capital markets division. The Pherecydes Pharma flotation in February 2021 was the first IPO on the Paris stock exchange that was entirely subscribed by ABO for the institutional side. Canada is another core market. Emerging markets have included Columbia and Mexico.

ABO is a buy side firm, but it also carries out a range of functions that sound more like sell side activities: transaction advisory, market making, and intra-group prime services. This is all part of a package designed to provide more cost-effective financing solutions.

Cost and dilution

In more competitive markets such as the UK, ABO could compete in a beauty parade of multiple providers of both alternative and traditional financing solutions. A deal with ABO could be competitively priced compared with secondary issuance underwritten by a broker, in terms of the direct cost of capital raised: "Some brokers have high fixed costs, which can work out expensive for smaller deals. ABO's pricing is broadly based on credit risk for convertibles and counterparty risk for equity," explains Vannineuse.

ABO structures might also be attractive in reducing dilution, particularly for companies with an optimistic view of their prospects over several years: "We find that taking warrants aligns our interests with the companies'. The issuance can be delayed or staggered over an agreed timeframe to control the dilution," says Vannineuse.

Certainty over capital raising and dilution can be traded off according to company priorities. A convertible bond facility can fix the amount of capital raised but be subject to variable dilution whereas an equity capital access program can fix dilution while raising a variable amount of capital. In between these extremes, flexible ranges could be defined for dilution or capital raising or both. Some companies may even negotiate a facility as a backstop but wait some time before availing of it – or possibly never use it.

Structure: timing, duration and short selling

ABO can move fast, tying up deals such as providing convertible debentures to Wayland Group Corp. in less than a week, thanks to help from external lawyers Norton Rose Fulbright. But ABO can also be committed to financing for multi-year periods and might sometimes be locked up, as it will be for a medical cannabis float in France, where it has a constructive outlook. Equally, pure financing deals can be turned over more swiftly.

Most deals have been exited by steadily selling shares into the public markets, rather than by selling block stakes, selling shares back to the companies, or corporate events such as takeovers. ABO has sold just under €1 billion of shares to exit deals, since inception. To facilitate fine tuning of its share sales, ABO has developed a proprietary artificial neural network, with deep learning and data mining, and proprietary VWAP (volume weighted average price) to measure liquidity and market impact. "We take over 1,000 trading days to provide a cycle of learning for back-testing. This is adapted and tailored to each company to determine how much, if anything, to convert at each time. If we believe the share price is going up, we may delay conversion. We want to take the emotion out of the process," says Vannineuse.

Short selling for hedging purposes can sometimes be part of the structure: "Larger companies may permit some degree of shorting against conversions to lock in returns. But most deals are done with smaller companies, with below $150 million market capitalization, which generally do not have any borrow available. It depends on countries, segments, volumes and we need legal opinions," says Vannineuse.

Return targets and risks

ABO could typically target a return of 10% on capital employed based on converting shares at a discount of 10%, though this will vary. Bigger companies might expect a discount closer to 5%, while some deals have been done nearer to 15%. ABO views its return target in terms of cash-on-cash realisations and avoids the complicated and subjective process of valuing warrants attached to some deals.

ABO sometimes becomes the largest shareholder and has some credit risk: "We have had two bankruptcies where we lost everything. We are generally the least senior creditor, and do not have recourse to other assets of companies," says Vannineuse. Another deal that did not involve a bankruptcy has also been a disappointment. ABO sought to provide private financing for Anglo Tunisian to carry out a takeover, but this did not come to fruition. "We have spent a lot of time and money on litigation."

ABO structures deals that aim to align interests, and rarely gets involved in corporate governance. "We do not like to be invasive," says Vannineuse. It has however occasionally needed to turn activist, nominating its own candidates onto boards. "In one case, with Safe Orthopedics, we were a friendly activist. We helped them to remove the original venture capitalist on the board, who was seeking a fast exit, which helped the business to move forward," says Vannineuse.

Turnaround case studies

ABO takes pride in committing to financing in some extraordinary situations where other providers might be reluctant or might even seek to renege on an agreement. ABO has enabled some bold turnarounds, helping companies to emerge from bankruptcy and rejuvenating them. "The first deal we did, French gold miner, Auplata SA, was a big turnaround situation that took much longer than expected. Now we have warrants but have not exercised them because the valuation is so low," says Vannineuse.

French auto parts maker microcap, Groupe DBT, was a spectacular recovery story. The firm was rescued from bankruptcy after Nissan cancelled a contract, and while the stock was suspended. A €10.25 million recapitalisation deal from ABO in February 2020 allowed DBT to restart production and relist, and the market capitalisation more than quadrupled to as high as €60 million at one point. ABO opportunistically carried out more conversions at higher share prices, reducing dilution for the company. Liquidity and free float in the company's shares has also multiplied thanks to ABO conversions indirectly making markets in the stock. DBT was also aided by a new contract win and French government electric vehicle subsidies.

French emissions control solutions group, Europlasma, was another impressive recovery: "It was already bankrupt, we provided debt for its operating partner, and injected three times its market capitalization over two years. Now it is worth more than four times as much as when we started," says Vannineuse. In June 2019, ABO committed up to €30 million of financing as part of a judicial plan for the firm to exit a French bankruptcy process, and the relationship has grown over time. In April 2021, ABO announced a seven-year deal committing up to €100 million. Spine fracture implants leader, Safe Orthopedics, was another turnaround. "It was lowly valued and is still cheap relative to other medtech companies with higher valuations," explains Vannineuse. ABO provided €12.45 million in June 2019 and an accelerated drawdown of convertible bond tranches financed the firm's acquisition of LCI Medical.

Biotech and healthcare

Recently as much as 80% of deals have been done in the biotech and healthcare sector. Deal flow can come from events such as biotech conferences and is also generated by venture partner, Dr Hervé Kergrohen, who has 25 years of experience in life sciences, including multiple executive and board positions in biotech and medtech companies in areas such as vaccines, neuroscience, medical imaging, robotic and minimally invasive surgery. Recent deals included two other French-listed firms in addition to Safe Orthopedics: AB Science and Eyrtech Pharma. AB Science specializes in protein kinase inhibitors and has developed a new orally administered compound, with multiple applications across oncology, inflammatory diseases and central nervous system conditions. The firm opted for fixed dilution financing based on the number of shares, with the amount raised determined by the share price. ABO gets 5% of share sales plus a structuring fee.

Disruptive technology

There have also been investments in quantum computing technology algorithms and blockchains. In March 2021, ABO invested €1 million with Quantonation, which has 12 quantum technology companies in its portfolio. WISeKey International Holding SA, which is listed on the Swiss exchange and on Nasdaq, received $15.5 million in convertible notes from ABO to help to acquire Arago and integrate AI into its cybersecurity platform. "This was one of the first companies to work on NFTs. It has proved to be a ten-bagger, rising in value from 30 to 300 million. We own 7% and have been selling very slowly because it is performing very well," says Vannineuse. "We are always looking for new and disruptive industries."

Regulatory framework

ABO has gross assets of around $300 million, including credit lines from private equity firms. ABO is a Cayman domiciled exempt company and has operating companies in the Bahamas and Dubai (having closed its London office in early 2020). "The Bahamas is partly geared towards North American time zones, which are providing a lot of deal flow," says Vannineuse.

As a family office, neither ABO itself nor the operating companies need to be regulated, but the deals they do need to pay careful attention to company and financial markets laws and regulations in over 30 domiciles, and some securitization vehicles are somewhat regulated. One of them, the European High Growth Opportunities Securitization Fund, is a Luxembourg-domiciled umbrella structure with multiple special purpose vehicles. EHGO has a management company attached to it, which is overseen by the Luxembourg CSSF. "The customized structures will depend on multiple parameters, such as legal and tax analysis, feasibility, custodians, exchanges and countries," says Vannineuse. Legal structuring is led by general counsel, Edward Keller, who was previously a partner at White and Case and Dentons. "Having an in-house counsel lowers bills and he also manages local counsel in over 30 countries, dealing with the nuances of settlement differences in Poland, Norway or Turkey, which differ from Euroclear".

ABO is scouring the globe to identify the most compelling deals and sees a 'Blue Ocean' of alpha opportunities ahead.

Founder and Chief Investment Officer
Integrated Portfolio Intelligence
New York

Nick Vasserman

Differentiated systematic macro

Nick Vasserman founded IPI in 2019 to pursue a distinctive strategy that codifies a discretionary fundamental macro philosophy and uses advanced quantitative techniques and processes. In common with some other systematic and quantitative macro managers, IPI is not a trend follower, uses mainly non-price data and trades liquid, exchange-traded markets in major asset classes. In contrast to peers, IPI is trading relative value within asset classes, based on fundamental linkages and relationships that the firm can model; has a significantly higher weighting in commodities, and explicitly avoids exposure to generic style and risk factors such as carry, value, momentum, mean reversion and a whole host of others.

"This is a marathon not a sprint," says Vasserman, who has developed his approach managing systematic macro strategies since 1996. At J.P. Morgan, between 2009 and 2016, he founded and was head of J.P. Morgan's Americas cross-asset quantitative strategies business, helping to build out quant offerings, initially in commodities and later across assets. At UBS, between 1996 and 2008 as global head of FICC (fixed-income currencies and commodities) proprietary systematic trading at UBS Investment Bank, he learned and developed a hybrid investment process incorporating fundamental analysis of supply and demand drivers that is integrated with quantitative tools and models. While at UBS, an important early influence on the deep fundamental investment process was a number of commodity traders he met, who were adept at reading fundamental drivers of supply and demand that are unique to commodity and energy markets.

Enduring and resilient models

Vasserman's style of trading has systematized and integrated fundamental data analysis into five families of models (low frequency structural; higher frequency macro; fundamental models; flows and liquidity models; quantitative and sentiment models) which have proved resilient through regime changes. If central bank policies challenge some quant macro approaches, as they did in 2020 and early 2021, Vasserman does not find they upset the tried and tested fundamental relationships that IPI trades on a relative value basis: "Our supply and demand balance sheet analysis and relationships do not cease to dominate price action, they are driven by production, inventories, imports and exports dynamics. We do not have to continuously search for brand new and untested models because the existing ones lose their validity. Our R&D pipeline is focused on ensuring models do not develop any new blind spots and this is typically accomplished by continuously evaluating new raw data sources to ensure our intelligence gathering process is very comprehensive and current". A fundamental approach to risk management recognizes when to have conviction and when to stay out of the market, and IPI is opportunistic in rebalancing model and market allocations according to risk and the conviction of individual models. The models themselves are enduring: "Model turnover is low, partly because the models have sound fundamental logic and are constructed with few to no parameters to ensure robustness over different market regimes."

Automation

"What changed is automating and systematizing the data collection and scrubbing, to collect higher quality datasets and clean them to become consistent, sensible and timely. Intelligence that was once collected manually from literally having boots on the ground around the globe, is now gathered automatically. Emerging market economic, currency and industry data can be very important: Brazil is a key producer of agricultural commodities, coffee, soybeans and grains, and China can be very important for base metals as a consumer and producer. Automation enables aggregation of key data simultaneously in multiple geographies," says Vasserman.

Near real time data

Automation also facilitates more timely data, approaching "nowcasting" in some areas though Vasserman does not use the term: "Timely and consistent data inputs are central to the process. Historically, traditional economic data had a one-or two-month time lag, whereas now we aim for weekly, daily or even intraday data with little or no time lags. We believe that near real time intelligence is more relevant for commodities than traditional macro or financial assets, and we gather it through API feeds".

Physical commodity data

"A significant part of the investment universe is in commodities, where deep value analysis including very granular modelling is done, such as physical intelligence counting barrels, bushels and tonnes, gauging commodities in transit, in different locations based on a range of variables such as weather and others," says Vasserman. IPI has relationships with the J.P. Morgan Centre for Commodities at the University of Colorado in Denver, and multiple data vendors.

Collaborative dialogue with data vendors

IPI uses thousands of time series from hundreds of original sources including governments, central banks, private firms and non-profit agencies and many more, with both external and internal data scouting, sourcing and aggregation. "We have an open dialogue with dozens of data vendors and provide them legitimate feedback on how they might improve datasets, quality, frequencies and states. The dialogues are at different stages, and few of them tend to make it into production. We have numerous relationships with data providers but aim to process as much of the raw data as possible in-house, to gain an operational edge because data can be stale, incomplete or incorrect. It needs to be understood, normalized and standardized across sources," says Vasserman.

Data selection, manipulation and integration

Alternative data is part of the story, though for all data manipulation is key: "Non-traditional data makes up a growing share of inputs, but exclusive, rare or alternative data alone does not provide a sustainable edge for any period. The edge is in how it is selected, benchmarked, cleaned, and integrated to ensure it tells you what it is supposed to – and then aggregated and integrated into a timely view of market dynamics and value. When using fundamental data, powerful computers are needed to analyse very granular datasets that need to be processed in a timely and operationally robust way. Operational risk is critical to our alpha edge," says Vasserman.

Exotic relationships between mainstream markets

IPI's investment universe includes dozens of futures and options markets in commodities, currencies, equity indices, rates, and volatility for some asset classes, which are typically traded over multi-week timeframes. Slippage is closely monitored by Head of Execution, Chris Andrews, who worked with Vasserman at J.P. Morgan. The choice of markets is a function of liquidity, depth and breadth of markets, ruling out orange juice and lumber for insufficient liquidity. IPI does not trade more exotic or esoteric markets but is rather distinguished by how it identifies and trades relationships between markets: "There are many unique relationships, pairs, ideas and themes to trade, such as commodity time spreads where there is a single curve but two very different markets, with different fundamentals in the form of buyers and sellers for this year and next year. For some commodities, the seasonal contracts are also chemically different and not necessarily substitutes – for instance, winter blend gasoline is different from summer blend," says Vasserman. Regardless of liquidity, not every commodity fits into this framework. Natural gas is monitored, but not traded because it does not currently show enough linkages to other energy markets for IPI's fundamental relative value approach to have an edge. Vasserman is monitoring Chinese commodities but judges them to be currently more suited to exotic trend followers than to his approach.

Minimal style and factor exposure

IPI's highly idiosyncratic trades have a natural tendency to generate return streams independent of more generic and potentially crowded approaches. IPI also explicitly avoids alternative risk premia (ARP) risk factors including equity momentum, FX value, commodity carry, as part of risk management which actively measures and controls exposure and concentration to sectors, themes, and factors. "Often ARP can get very congested, and we have low or no correlation to it. This also implies very low correlation to trend following CTAs, and to mean reversion. Some quant macro approaches with strong mean reversion components have struggled in 2021 as fundamental forces have accelerated," says Vasserman. Though IPI may have some residual directional risk, this is not driven by technical price signals, and should show very low correlation to indices.

Relishing volatility

Yet one possible factor bias is being somewhat long of volatility and long gamma (though IPI is not explicitly long of volatility through its volatility strategies, which are relative value approaches). "Volatility is generally a good thing, and we often profit early on during an exogenous shock that might upset some directional fundamental strategies. As relative value traders we are not concerned if an entire sector sells off or rallies, as we would expect higher quality assets to outperform lower quality ones," explains Vasserman.

Since going live, March 2020 was IPI's strongest month, thanks to a mosaic of signals. "The early recovery phase from the pandemic generated plenty of volatility in incoming fundamental data that needed to be filtered out," points out Vasserman. The market climate in 2021 remains opportune: "As we move into later recovery phases, fundamental linkages should become substantially more dominant versus sentiment and exogenous drivers and this constitutes a very favorable environment for IPI".

Granular risk management

The IPI investment process also requires its own sophisticated risk management. "We use very granular risk models, which measure concentration and statistical risk, as well as stress testing dating back even to pre-Covid health driven risk events monitoring such as African swine flu," says Vasserman. This is partly informed by a mentor dating back to Vasserman's days studying at the University of Toronto: "Derivative science and interest rate derivatives modelling guru, Professor John Hull, influenced my approach to risk management, by teaching me about the evaluation and risk management of exotic structures and directly addressing markets jumps, spikes and regime changes. This clearly differs from the normal continuous markets assumed by classical models".

IPI's underlying infrastructure deployment is a case study on the website of Beacon, which was started by some of Vasserman's former colleagues at J.P. Morgan. "It has been battle-tested at J.P. Morgan and other banks such as Goldman Sachs and Bank of America," says Vasserman.

IPI's proprietary alpha and risk models are run on Beacon infrastructure in the cloud: "Continuity and familiarity with Beacon architecture enables IPI to efficiently process and analyze thousands of datasets and manage hundreds of models very robustly, without a large number of in-house technology staff". IPI's head of quantitative analytics and technology, Ben Zhu, was also head quant at Beacon and worked closely with Vasserman for several years.

Growth plan

Vasserman spent a few years fine-tuning the strategy and building the necessary infrastructure, such as data feeds and models, running his own family office, Momenta Capital, which became IPI. He found a good fit in securing seed capital from Inception Point, which was started by former Soros macro manager, Keith Anderson (who has featured in an earlier edition of the *Tomorrow's Titans* report). Firm assets are over $125 million as of March 2021 and the next milestone is $250 million. "We wanted to get the economics right and have also managed to establish a very good relationship. The Inception Point team act as consultants, sharing a lot of complementary expertise in areas such as marketing, risk management and their network. This will become increasingly more valuable as we grow," says Vasserman.

The focus now is building a longer multi-year track record for the flagship strategy, which is run pari passu in managed accounts and funds. There have also been enquiries about customization including different amounts of leverage, different subsets of models and even an ESG version of the strategy. Vasserman is having dialogues with sophisticated institutional investors including large asset managers and pension funds, globally.

Co-Founder and CIO
Ananda Asset Management
London

Louis **Villa**

Investing with a long-term mindset

Louis Villa uses the word Ananda as a mantra for his meditation practice and it also speaks to the key ambition of the asset manager: a heaven of calm and serenity in equity markets which change ever more quickly. This made it an obvious choice for the company's name when Louis Villa and Araceli Strassburger launched the London based company in late 2018. "Some managers seek to outperform by being faster – a task undoubtedly made harder by the rise of algorithms; others by being smarter – and here competition is very intense. We aim to generate alpha by following a simple – but not easy – process: deeply research quality assets that we buy from pessimists and sell to optimists. Not by being quicker, or smarter, but by being calm and maintaining a long-term focus," says Villa.

Realistic alpha generation targets

With a research driven and bottom-up investment process, Ananda is not scared of making contrarian calls on individual stocks, making the fund generally short the momentum factor. Ananda eschews macro directional calls and therefore more macro-driven sectors, such as banks and energy, but rather favors investing in consumer, industrials, technology, niche financials and healthcare. Ananda invests mainly in European and US equities with a typical 70/30 split, in line with what Villa did first at SAC and then at Moore Capital where he was running a $600 million book.

Ananda's target is to generate annual alpha of c.5% per turn of leverage through the cycle. This alpha target might seem ambitious, especially considering the large cap focus, but it is consistent with Villa's career track record in long/short equity over the last 15 years. The team has long-term confidence about their return objectives, but also shorter-term humility: "Looking back, annual alpha performance varied through those years from great to slightly negative. Trust me, we worked equally hard in both cases. Sadly, one can only control the process, not the outcome," says Villa.

This alpha, coupled with a gross exposure ranging from 250% to 320%, should translate into mid-teens annual outperformance. The net market exposure has been kept fixed ever since the launch of the flagship strategy, Ananda Long Term Opportunities (ALTO), as Villa does not believe he can time the market. In fact, he does not believe anyone can, at least not in a consistent and repeatable way.

By adding hefty alpha to moderate beta, Villa aims to compound around 15% over the long-term, a target the team has substantially exceeded since launch. "The last two years have been very testing, with dramatic news-flow and volatility. Through that period most of the alpha has come from longs. It will not always be the case, but compounding and human ingenuity work heavily in favor of longs. Whereas the asymmetrical limited upside and unlimited downside make shorting inherently more difficult. To avoid being in shorts we do not like or being too big in shorts that we do, the team uses indices to complement single stocks," explains Villa. Shorts are sized smaller, but Ananda still devotes a big research effort to seek out fundamentally challenged companies and sectors, over-leveraged firms, those going ex-growth, or those with over-optimistic or deceptive management teams.

Since inception (April 2019 to April 2021), ALTO's L share class (with 2% management fee), has annualized 31% versus 14% for its equity market benchmark (which is composed of 30% US and 70% European equities), exceeding significantly their alpha target. "The extraordinary events of the last two years have provided plenty of opportunities for a contrarian and fundamental research team. It has been a good period for the calm crowd. To be fair, I suspect there will be plenty more drama in the years to come as extreme central banks policies and rising political volatility create a very fruitful environment for our strategy," says Villa.

Two types of turnover

Helping Villa manage the research process is co-founder and Head of Research, Araceli Strassburger. Previously a Managing Director at UBS where she spent 18 years, Strassburger met Villa early in her career whilst a research analyst. The two have developed a deep and trusting relationship spanning more than 15 years. Ananda's research process blends quantitative scoring together with old school human qualitative analysis. On the quantitative side, the team focuses on return on capital, balance sheet quality, and margin volatility. The qualitative side focuses on identifying disruption risks, judging alignment of interests, and ability to allocate capital. The team of three additional analysts meets management teams, competitors, and experts, conducting in-depth due diligence. The result of this effort is a dream list of close to 200 "Forever" stocks, assets the team would love to hold for decades. A few examples are found in Ananda's Heroes newsletter on its website, which identifies key influences as including Fiat's Sergio Marchionne; Bruno Cucinelli of the eponymous firm; Constellation Software's Mark Leonard, and Berkshire Hathaway's Warren Buffet.

Villa has invested in all these companies at various times, but not all the time. "Given our 3 to 5 years investment horizon, we invest our capital in the 30 to 40 most attractively valued assets among our dream list, those which offer the best risk-reward, and where Ananda's view differs the most from consensus. Quality is non-negotiable, but we are very cognizant of the fact that three years out, the price you pay significantly impacts the return you get," explains Villa.

A very large majority of Ananda's long book are names that have been there for the full two years. If the name turnover is remarkably low for a hedge fund, the dollar turnover is higher because the short book turnover is higher, and because Ananda is not scared of trading around names.

"Performance attribution since inception has been a healthy balance between the operational excellence of the companies we invest in and dynamic rebalancing of the portfolio," says Villa. "Market sentiment varies greatly, and the last 10 years have shown that the manic-depressive aptly described 80 years ago by Benjamin Graham is alive and kicking."

The hit rate has been very high: Ananda's internal data show that more than 75% of the longs generated positive alpha since inception, and the fund has posted seven quarters of positive alpha and only one quarter of negative alpha. "As we do not optimize for the short-term, and focus on long-term capital preservation, some volatility should be expected. Q1 is a good example of negative alpha. We invest in large caps, high ROCE assets and do not invest in energy, commodities or banks, which rallied along with mid-caps and low returns companies. In this context, we were happy to end the quarter with positive performance," says Villa.

Factor and style exposures

Though the alpha has by far been the main driver of returns, there are some gentle nuances around styles and factors. Over the years, Villa has found that gauging style and factor exposures is more art than science, but a helpful way of monitoring risk. "The portfolio is broadly style neutral, with a slightly short momentum bias which generally acts as a headwind under normal circumstances but is very helpful in periods of stress or deleveraging."

Though Ananda's quantitative screens and quality compounders populating the long book might sound like tell-tale growth stocks, in fact, "the style is closer to GARP [growth at a reasonable price] than pure growth, though again there is not a strong bias," says Villa.

Ananda's beta-adjusted net exposure is rarely higher than the cash figure and is more often lower: "Beta-adjusted net exposure can sometimes be up to 20% lower than cash because we tend to invest in higher quality, lower beta types of businesses," says Villa. "The beta is an output, not an input," he stresses.

On the ESG front, the best corporate citizens are Ananda's natural business partners. Villa finds that, "companies that focus on treating their stakeholders in the best possible way tend to outperform in the long-term". As a result, 2/3rd of the companies comprising the long book are rated top 20% amongst their peers by ESG experts from Sustainalytics.

Corporate culture

Creating a good home for their own capital and a place where they would enjoy working was the original ambition driving Villa and Strassburger in creating Ananda. Paying homage to Bridgewater's Ray Dalio, the team wants meaningful relationships with meaningful people and their own version of radical transparency. "Radical transparency was natural when we started with Araceli. Today, with a team of eight, it is of course more challenging, but we want non-judgmental radical transparency to be at the core of everything we do." The team is diverse, with two other senior women besides Strassburger (heading investor relations and operations) and multiple nationalities.

Outlook

Villa defines himself as a constructive bear or a reluctant bull, as central banks' policies fuel bubbles across asset classes, leaving equities as one of the few reasonably priced. He has discovered through the fundraising process how contrarian the strategy followed by Ananda really is, at least compared to the current attraction of private equity. "Investing in a hedge fund today feels more contrarian than raising a subprime real estate fund in the early 2010s, and trust me, it was contrarian back then," says Villa who made significant personal investments in Florida subprime real estate, before helping with the creation of NY based Lafayette Real Estate after the Great Financial Crisis. "I suspect returns will be as good or even better this time," says Villa.

Ananda's newsletter Debasement sums up the long book with the acronym: LIQRR (Liquid, Inflation protected, Quality equities that are Relatively Reasonably priced). Villa has no strong views on aggregate equity market directions. He would not be surprised if equities returned only average returns over the next decade given the elevated starting point but thinks markets will provide plenty of opportunities for stock picking. Liquidity is important since populism, fiscal instability, and general political volatility will favor the most agile. Inflation protection sounds a must have after 40 years of disinflation. "Inflation may or may not be around the corner, but the asymmetry is clearly the upside". Quality is sought as a natural part of the research process and because Villa has concerns about "zombie" companies being kept artificially alive with government support. Price matters to maintain a margin of safety and protect capital.

Ananda has just become a full scope AIFM regulated by the FCA but has not yet started marketing in earnest due to Covid. Assets are now at $200 million and were raised from family offices, institutions, and Villa's extended professional network. He is pleased to have found the right types of clients. "In just over two years, we have been through very volatile markets, and I am glad we have the support of long-term investors. Having the right clients who are aligned with what you are trying to achieve is critical, and we are grateful to every single one of them," says Villa.

Chief Investment Officer
EOF Partners LLP
London

Sof Yiannakas

European equity alpha and positive firm impact

Sof Yiannakas launched EOF Partners' European equity long/short strategy in March 2020. He has spent most of his career consistently researching the structural competitive landscape for European companies whilst at Soros Fund Management and Davidson Kempner Partners, after a spell in technology, media and telecoms corporate finance at Deutsche Bank. The EOF strategy runs a concentrated, high conviction book owning secular and structural winners on the long side, which is underwritten over five-year rolling time horizons, while fundamentally challenged firms and those with aggressive accounting populate the short book, where catalysts are anticipated within a year or so.

The EOF investment universe is around 1,500 reasonably liquid companies listed in developed Europe, across all cap sizes, though only a few dozen of these will make it into the portfolio. The bottom-up research process includes a detailed assessment of management and culture, analysis of proprietary data, as well as regular channel checks with competitors, suppliers, distributors, and former management. A sceptical and investigative approach is taken to corroborating and triangulating reported financials, both within companies' own accounts and cross-referencing other firms. The investment process is discretionary and fundamental, but it builds on a strong quantitative foundation of data analysis and programming.

Coding and collaboration

Technologically sophisticated analytics employ big data, automation, programmatic corporate governance screens and forensic accounting for both long and short books. The team, including Yiannakas, can code in several languages and in the spirit of collaboration invite LPs to join EOF in periodic programming hackathons, as well as other professional development sessions hosted by EOF. They also use APIs for connecting to data sources, and proprietary bots for web scraping and processing data feeds, enabling the team to cover a lot of ground.

Cognitive diversity in the team is demonstrated by colleagues: a forensic accountant and a mechanical engineer. "This brings deep domain knowledge in manufacturing industrial sectors, as well as a diversity of knowledge and experience. Consequently, EOF is less likely to suffer from perspective blindness," says Yiannakas. Indeed, quantitative analytics are also employed to heighten awareness of internal biases, in keeping with a "know thyself" philosophy. "Our systems improve decision making by identifying mistakes and opportunities for continuous improvement. We systematically review every aspect of our decision making every six months," he reveals.

"The key qualities of our corporate culture are being collaborative, intellectually honest and intellectually curious. Job applicants should be able to admit to prior mistakes as well as being open to something they do not know. EOF's culture has been influenced by *The Culture Code* by Daniel Coyle which is a must-read for any business owner looking to establish purpose. I am keen to motivate and build a safe environment in which our team can be creative while recognizing our shared vulnerability. Edward De Bono's *Six Thinking Hats* reminds us to assess problems from as many perspectives as possible, in a collaborative manner which ultimately leads to better results," says Yiannakas, who credits Dawn Fitzpatrick of Soros Asset Management (who featured in *The Hedge Fund Journal's* 50 Leading Women in Hedge Funds report) as having been an especially inspirational mentor with regard to team building and corporate culture. "Another mentor, and an influence on my initial investment education is former Davidson Kempner portfolio manager Darren Curtis, who empowered me early in my career," says Yiannakas.

Longer term long investing

The long book has three sleeves: quality compounders, management driven turnarounds, and valuation driven quality. "Our quality compounders are growing businesses, with high barriers to entry or "moats", which enjoy high sustainable returns on capital, are managed by outstanding management teams, have clean earnings, and sensible valuations. Turnarounds in the portfolio are businesses on a good to great journey, often with new management. Valuation driven quality can include some quality cyclicals and even some deep value names," explains Yiannakas.

These labels are discrete and distinct, and a summary of why EOF has invested in a given business. "Migration between categories is a sign of 'thesis creep', an indicator that we need to reconsider, and likely exit, an investment. This is a lesson learnt early in my career, from another Davidson Kempner partner, Michael Herzog, who had the most significant influence on my approach to risk management. He was particularly astute on thesis drift: when facts change, so should the portfolio and our positions," says Yiannakas. Views on valuation are nuanced: "Europe is an attractive, under researched market with equities valuations near a 10-year relative low compared to the US market. As bottom-up investors, we are more interested in a company's valuation compared to its history and what we consider the business could be worth". Valuation comparisons consider global peers, but Yiannakas cautions that, "adjustments need to be made for the relative maturity and uniqueness of businesses, for example, the outsourced European cell tower industry is nascent compared to that of the US which could justify a premium valuation". EOF prefers to be conservative on valuation, using multiples consistent with firms' long-term history while discounted cashflow valuations are used as a sense check.

EOF invests in businesses as a long-term shareholder and aims to capitalize on the myopic behaviour of other investors. "Hyperbolic discounting explains the tendency for a person to choose a smaller, near-term payoff rather than a larger, longer-term payoff, even though their future self would prefer that they made the longer term choice," says Yiannakas.

Whether higher interest rates and inflation threaten the valuations of some growth companies is open to debate. Yiannakas recognizes that, "some long duration infrastructure assets are particularly sensitive to higher rates. Overall, identifying companies with strong pricing power is the best defence against inflation or rising yields".

Aggressive accounting and shorts
Shorts are intended to be profit centres rather than hedges for longs, and come under three sleeves: forensic accounting, fundamental, and red flag. EOF was short a firm that turned out to be a fraud in 2020. "Though frauds generate headlines, outright frauds in publicly listed equities are extremely rare. Creative or aggressive accounting being used to offset weaknesses in parts of a business is a much more common phenomenon. Motivations for aggressive accounting could include management incentive schemes, ego or simply a misaligned hope that a challenged business will eventually recover," says Yiannakas. Examples of aggressive accounting are plentiful but include the use of subjective revenue or profit recognition for long term contracts, excessive and growing capitalization of costs; the use of "below the line" adjustments; and inadequate provisioning. EOF has built a proprietary accounting database and systems to flag accounting deterioration for businesses in Europe. EOF's expertise is well suited in Europe. "Unlike companies in the US which report under US GAAP and publish accounts in a standard form with the SEC, in Europe we encounter local standards in each country as well as inconsistent disclosure between companies and even over time for the same company," explains Yiannakas.

Style, factor, and size exposures
There are no quotas for any of the long or short sleeves, so some of them might be empty if candidates cannot be found. The strategy is focused on single name alpha, which it has delivered: making 15.2% between March and December 2020, it has outperformed European equities with moderate net exposure in its first ten months. EOF is not sector, factor nor style neutral but is cognizant of these sensitivities. "We are aware of our factor exposures but recognize our strategy tends to be exposed to growth, quality and large cap factors," says Yiannakas. Style tilts can contribute to some volatility, particularly amid the violent factor rotations seen between November 2020 and March 2021.

Factor exposures can vary over time and are considered when sizing positions. "If we can find offsetting exposures on either side of the portfolio that is helpful, but we do not seek to hedge out factor or sector exposures explicitly. We focus on the variables within our control, which are identifying companies that can sustainably grow long term earnings and cashflows," says Yiannakas. Given the longer-term horizons for long positions, he has often found that "periods of factor rotations, when fundamentals are overlooked, can be an attractive time for long term investors to deploy capital".

Crowding is also monitored and Yiannakas finds that: "It is a consideration for existing and potential shorts, and a risk that needs to be compensated for. We have avoided crowded names where our conviction did not justify the risk". EOF is somewhat discreet about shorts. It might have short positions above the 0.5% EU disclosure threshold, but is unlikely to become a short activist, and does not share intelligence with other short sellers.

Though the strategy is market cap agnostic, it tends to have more mid cap exposure on the short book, because of how the firm identifies opportunities. Mid cap shorts and single name shorts distinguish EOF from many managers who tend to have a larger average size on the short book, sometimes partly or wholly due to them using sectors or indices rather than single names on the short side.

Approach to ESG
ESG starts with good governance as a prerequisite on the long side. EOF favours developed European markets with strong corporate governance and rule of law, amongst other requirements. More broadly, EOF utilizes a proprietary ESG scorecard to assess and validate ESG considerations. Their assessment combines quantitative and qualitative data to verify and judge companies. "We score E, S and G separately and overlay our proprietary research to calculate a holistic score. We also seek to identify, and penalize businesses for prior ESG breaches," explains Yiannakas. EOF investments score higher on ESG, and their score is improving faster than the average European company.

Yiannakas often finds that a sustainable business model in the economic sense goes hand in hand with sustainability in an ESG sense. "We underwrite fundamentals and the sustainability of a business model. We typically find that businesses run by management teams for the long term are also mindful about being sustainable, be it regarding their supply chain, employment contracts or environmental responsibility. There is a correlation between our view of quality, and how a business ranks on our ESG scorecard."

Over time, Yiannakas contemplates signing up to the UNPRI and expects to report on the firm's own carbon exposures: "Having no legacy allows us to be mindful from day one about our own footprint as a firm and the quality of our disclosure," he says.

Firm level impact
EOF is running a responsible investing strategy – and has hosted thought leadership events on impact investing – though Yiannakas does not define the EOF strategy as "impact investing". The firm however aims to have a positive impact through its philanthropy, in keeping with its name (the Equal Opportunity Fund): "Our greater purpose drives how we behave as a firm. We want to stay humble and grounded while making an impact. It started with my pilot project at Soros offering internships to people from underprivileged backgrounds, which is an initiative we are replicating at EOF". For now, charities supported include the Social Mobility Foundation and Teach First, while EOF is also a founding participant in the #100blackintern initiative. In keeping with its collaborative culture, EOF invites investors to propose other causes: "Investors are invited to join the EOF Charity Advisory Board to suggest charities to be supported".

A solid springboard for growth
"The firm has built robust operational infrastructure to position us well for the next decades, led by COO Warran Reed who has 23 years of operational experience, including at Eton Park, Highbridge and Lehman Brothers. His experience, allows me to fully focus my attention on the portfolio and the investment process," says Yiannakas. The board includes Reed alongside two seasoned independent directors. "Sarah Caygill is a great resource, as an advocate and challenger, and she has helped to steer the business contributing her knowledge as a former portfolio manager. Robert Thomas also brings his knowledge and experience sitting on the board of several multi-billion dollar funds," explains Yiannakas.

Early LPs include tier-one institutional investors as well as several family offices. The firm offers a founders' share class with discounted fees. Yiannakas is seeking to partner with longer term investors who value EOF's culture and long-term strategy.

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