Strategies

January 2009

26 February 2009

Most alternative strategies were positive in the first month of 2009, whereas the macro economic environment was just a continuation of 2008: global recession remained the market consensus and there was still no sign that the economy reached the bottom. The deteriorating economic numbers, job cuts, tightening credit standards and shrinking bank balance sheets reminded us that the economy was still worsening. The International Monetary Fund revised down to 0.5% its forecast for world growth in 2009. Equity markets closed the month in negative territory once again, and government bonds finally interrupted their rally. All commodities, except precious metals, were down as well in January. The only exception among bearish assets across the board was credit markets, with the Merrill Lynch High Yield Index gaining 5.3% in January. Despite a record amount of new issues in investment grade bonds, credit clearly outperformed other assets. Corporate bonds benefited from a favourable relative value perception and asset allocation shifts out of government bonds and equities. Global policymakers continued to counter this downward spiral by implementing larger and bolder fiscal and monetary measures. The aggregation of all announced recovery plans and other packages represent about 4% of world GDP. The cross-currents of the rapidly slowing economy and the bold government intervention have kept the markets debating over recovery or depression, inflation or deflation, and USD strength or collapse. Hedge fund managers have now adapted their positioning and risk profile and benefited from these volatile and uncertain market conditions. They generally achieved a strong positive performance in January, with the HFRX Global Hedge Fund Index up 1.4%.

Fixed Income and Relative Value Strategies

Long/Short Fixed Income

This bucket had a positive contribution to the performance of our funds in January, despite weak government bonds markets (the US 10-year Treasury recorded a negative 4.8% performance in January). Core fixed income and currency trading both performed well: managers took advantage of the continuation of the bull-steepening curve trend in virtually all countries, as well as the weakening of emerging market currencies vs. the USD. Outright long positions on the front-end of the curve were universally shared, as the main view is that central banks will have to keep rates lower for longer. Although our managers' macro analysis stays unchanged, they are careful about potential surprises, such as better economic data, that could invalidate their strategies.

Fixed Income Arbitrage

This strategy contributed positively to the performance of our funds this month. Rising government debt issuance has reinforced managers' view that US government bonds will cheapen relative to high quality spread products and swaps. Other relative value trades include the narrowing of longer-term rate spreads between US and Europe, or the recovery of "inflation breakevens" in US inflation-linked bonds (they were pricing negative inflation for the coming five years). Given the uncertainty around the final shape of the fiscal packages, our managers have maintained a relative low risk profile and have tried to focus on short-term trading opportunities.

Long/Short Credit

Long/Short Credit managers produced strong positive performances. The rally in credit markets in January (ML High Yield index tightened 186bp at 1626bp) was helpful, even if one of our managers runs a net short exposure in high yield bonds. Another manager remains short investment grade and long high yield, with a small net long exposure. Some rationality is coming back: prices are moving more in line with fundamentals, in line with the different sizes of upcoming government packages from a sector to the next. For example, the sector of non-cyclical consuming goods could be a winner in case of large fiscal packages. Defaults are expected to increase, reinforcing the need to carefully analyze and select credits. We believe our managers have excellent core credit selection capacity.

Capital Structure Relative Value

A significant outperformance of credit vs. equity was a positive contributor to the performance of arbitragers in the capital structure of companies. Credit prices moved in line with fundamentals (e.g. financial and auto sectors clearly underperformed), so credit picking was rewarded. Indeed default and liquidity issues loom whatever the elusive plans announced by the new US administration. Moves towards a central trading and clearing house for CDS are welcomed by our managers. Lastly, the basis between bonds and CDS narrowed significantly from December elevated levels, allowing managers to benefit from their basis positions.

Equity Strategies

Long/Short Equities

Generally, rationality improved in the market, which strongly benefited our managers. There was also a catch-up effect after the terrible and chaotic last months of 2008. We appreciate the return to rationality and think the long/short equity strategies will be able to produce positive returns this year while continuing to outperform the long-only strategies. Nevertheless, we continue to run our portfolios defensively.

U.S.

Despite a good start the very first day of 2009 (+3.16%), the S&P 500 was down 8.4% in January and finished the month around the November 2008 lows which correspond to the May 1997 levels. Volatility remains steadily high. 8 of our underlying funds were up this month and 1 of them by more than 10% while our worst 2 performers were respectively hurt by the poor performance of the cyclical names and the debacle of the Transportation sector.

Asia

The MSCI AC Asia Pacific Index was down 7.21% this month. Three of our managers generated strong alpha, of which two are Japanese managers. Japan is probably the best area for alpha generation, as actually the economic situation there is deteriorating quicker than in the rest of the world, and as our managers were capable to capture good trends at sector level. Most of our underlying fund managers manage their funds with a macro view, in addition to their pure stock-picking skills. They could change their exposure quickly should new catalysts appear.

Europe

In January, the MSCI Europe was down 3.6% in euro terms. Our underlying fund managers continue to run defensive books but are finding a lot of stock picking opportunities. This month, we redeemed our entire position in a fund, in which we were invested since its inception in April 2004 with a significant position. The fund manager is an excellent fundamental stock picker and had a relatively low net long exposure, but he lacked a clear macro overview which is important in this difficult environment. His stock picks were also significantly biased towards global growth, which could entail heavy losses in 2009.

Low-Beta Long/Short Equities

Low-Beta funds had a good contribution to the performance of our funds this month. One of them benefited from a strong mean reversion effect, posting a +5.2% performance while all other Low Beta funds performed positively.

Event Driven Equities

Event Driven funds registered a positive performance thanks to their slightly net short positioning, with some very good gains on individual hedges, notably in the banking sector. We redeemed a small position in an Event Driven fund which was launched at the end of 2007, as it did not measure the extent of the crisis and therefore incurred losses last year.

Macro and Trading Strategies

Global Macro

This strategy contributed positively to the performance of our funds. Our macro managers have kept their views unchanged, namely a negative outlook on Emerging Markets and Eastern Europe through credit and currencies and a negative outlook on sovereign and corporate credit in developed markets. They are also positioned to take advantage of higher long-term rates in the US. Long Japanese yen remains a favoured position.

Systematic Trading

Most managed futures funds ended January with a positive figure. Profits were made in FX, with long Yen and short Sterling positions. Short equity indices trades were rewarded as well. Some of them incurred losses from their long bonds positions and from the reversal of agricultural prices.

