Interview: Stefan Gavelin, Adrigo

Stockholm (HedgeNordic) – Adrigo Hedge is an actively managed equity hedge fund aiming to achieve attractive absolute returns at a lower risk than in the Nordic equity markets. The Stockholm-based fund, which predominantly invests in Nordic equities and equity-related instruments, focuses on larger and more liquid companies throughout the Nordics. Adrigo Hedge has successfully managed to deliver strong returns at a reduced level of risk, mainly thanks to its effective investment philosophy and disciplined risk management.

Stefan Gavelin, an expert in risk management working in the financial industry since 2004, has been at the helm of Adrigo Asset Management since 2014. HedgeNordic had the privilege of conducting an interview with the CEO of Adrigo Asset Management, so let's cut right to the question our readers have on their minds.

HedgeNordic: How would you describe Adrigo Hedge to our Swedish and international readers?

> Adrigo Hedge is a low risk long/short equity hedge fund investing in Nordic large-caps and managed by a very experienced Investment team. Back in 2006 the founders Göran Tornee and Håkan Filipson, wanted to start a fund that could generate positive returns regardless of the performance of the equity markets. The fund now has a track record of close to 11 years. During these years, we have been able to put our stock picking methodology to the test, and see that it works in both good and bad periods in stock markets. We are also proud to have Melker Schörling, Mikael Ekdahl and Carl-Henric Svanberg as owners in the Fund Management Company as well as investors in the fund.

HedgeNordic: Your fund management company plans to launch a new long/short equity fund focused on small and medium-sized Nordic companies. Can you discuss the soon-to-be launched Adrigo Small & Mid Cap L/S fund and the risk-return profile of the fund?

> We have always focused on the Nordic region, however, our main expertise has been larger companies. Now Staffan Östlin has joined Adrigo and he has a strong track record of investing in the Small & Midcap segments. Many of today's large caps such as Assa Abloy and Hexagon were small caps a few years ago so we feel that there are great opportunities to operate in this field as well. Just like Adrigo Hedge it will be managed according to a selective and value-oriented approach focusing on one key word: CHANGE. Naturally both the risk and the expected returns are higher than in Adrigo Hedge. We will target a return of 8-12% p.a. in the new fund at a lower risk than in the Nordic equity markets.

HedgeNordic: Going back to your flagship fund, how does Adrigo Hedge generate new investment ideas? When your team considers investing in a company, what makes you say: "Yes, we will invest" or "No, we won't?" Please describe your investment process.

> As I mentioned we focus a great deal on change factors. It is easy to find a company with a relatively low or high valuation however it is vital to find triggers for out or underperformance. In order to identify such triggers we meet with more than 200

companies per year and actively seek alternative/industrial contacts in order to improve our knowledge.

Importantly, we do not enter into positions where we do not feel that we have sufficient knowledge or own competence to assess the potential risks. For example we would not invest into traditional biotech companies or exploration companies.

HedgeNordic: What is the typical time frame Adrigo Hedge are thinking about when looking at an investment opportunity?

The investment horizon when a position is initiated is normally 6-18 months. The actual holding period could vary from a few days to several years depending on how the value of each investment case unfolds, and how new events change the risk/reward profile of each investment.

HedgeNordic: How do you approach valuation, and what target level of returns do you aim to achieve from each investment?

We use a fundamental approach and a range of traditional valuation models including cash flow and free cash flow valuation models. The importance and relevance of each model can change over time however.

The return target of Adrigo Hedge is 4-8% per annum (after fees). Our return target for each stand alone investment is higher however as we also seek to reduce the risk and look for correlation between long and short positions this is the residual return.

HedgeNordic: As part of your investment selection process, you meet with the management teams of various companies. How do you maintain a good relationship with management teams when you have a short position in their companies? Are they aware of your short positions?

Over the years we have of course built up good relationships with many management teams in the Nordics. As a rule however we do not release our short positions apart from when we have to do so as a result of regulations.

HedgeNordic: Adrigo Hedge appears to defend the origins of the name “hedge fund,” as your fund recorded a loss of only 3.5% in 2008 versus the 51% loss incurred by the Nordic40 benchmark index. 2011 was yet another example of disciplined risk management on the part of your fund. What is your approach to managing risk?

We normally hold 25-35 long equity positions and the same amount of short positions. By combining long and short positions it is possible for the fund to achieve positive returns in both up and down markets. In 2008 we did not succeed entirely but that was also an exceptionally bad year for equities. Further, we aim to spread our positions over different types of companies and industries, again with the aim to reduce risks. In normal markets, our net exposure to stocks is between 20-50%. In addition, and perhaps most importantly from a risk management perspective, we carefully monitor the correlation between our long positions and our short positions in order to achieve strong risk-adjusted returns.

HedgeNordic: The traditional "2 and 20" fee structure in the hedge fund industry has been under significant pressure in recent years. Can you discuss the fee structure you maintain? And how will the typical hedge fund fee structure evolve over the next five years?

We have a 1% fixed management fee and 20% performance fee. We are proud of our fee structure which means that we really only make money when our investors make money. We believe that the main objective for an investor is to find "value for money". Unfortunately we have seen a number of fund management companies who are charging high fees but not offer so much value. As a result index funds have become more popular but of course they normally also have high risk and this cannot suit everyone.

HedgeNordic: Investors have been shoveling money from active fund managers into passive funds such as exchange-traded funds, as most active managers are failing to justify their fees. Meanwhile, the assets under management of Adrigo Hedge have been been growing steadily over the years. How did Adrigo Hedge manage to thrive while other managers struggled to satisfy investors?

We can only really speak for ourselves and we continue with the same investment philosophy in Adrigo Hedge as we have had since the fund's inception. We believe that if we continue to deliver strong risk-adjusted returns then we will also continue to attract investments.

HedgeNordic: Given the fast-increasing demand for low-cost indexing and the emergence of artificial-intelligence powered quantitative hedge funds, how do you picture the hedge fund industry in five years?

Generally we feel that it is good that low-cost indexing products are presented as options to investors. There has for many years been hedge funds that are driven by computer code and the emergence of artificial intelligence will most likely change the dynamics. We do not see this as a threat but more as a complement to existing products. In the end, change is behind what drives our business.