Takeovers Expected to Boost Sector Zen's Performance

Stockholm (HedgeNordic) – Sector Zen, a Norwegian long/short equity hedge fund employing a Benjamin Graham-inspired value-oriented approach in the Japanese equity market, announced a new takeover within the fund's long book. This was the 33rd takeover since the fund's inception in April 2006, but only the second takeover thus far in 2018.

Mitsui Fudosan, a major real estate developer in Japan, announced a tender offer after Friday's market close in Tokyo with the intention of making its publicly listed subsidiary, Mitsui Home, a wholly-owned subsidiary. Around two percent of Sector Zen's net assets were invested in Mitsui Home shares prior to the takeover, with the position anticipated to contribute an estimated 0.5 percent to the fund's overall return. More than two-thirds of the fund's long positions are comprised of investments in attractively-valued subsidiaries and affiliates of larger parent companies. Despite the low number of takeovers in Sector Zen's long book this year, buy-ins and spin-offs are expected to represent a solid driver of portfolio returns for the fund going forward.

One tailwind behind the Japanese equity market's buy-ins and spin-offs has been the introduction of Japan's 2015 corporate governance code and 2014 stewardship code, Sector Zen's investment manager, Trond Hermansen *(pictured)*, explained HedgeNordic. This corporate governance overhaul has led to increased focus on shareholder returns, accountability to shareholders and more focus on capital efficiency, which "is particularly interesting in a stock market with an abundance of cash-rich companies" according to Hermansen. In addition, this year's revision of Japan's corporate governance code "puts further pressure on companies to reduce cross-shareholdings," Hermansen said. "As friendly stakeholders have been gradually replaced by more demanding foreign and domestic shareholders, the freshly-revised corporate governance code provided shareholders with a powerful weapon to rightfully demand higher shareholder returns." This will lead to more takeovers of cash-rich subsidiaries where there is no rationale for separate stock market listings, reckons Hermansen.

Sector Zen aims to generate attractive returns by exploiting inefficiencies within the Japanese equity market using a value-based, contrarian approach. More specifically, the fund seeks to identify deep-value situations that can benefit from possible re-rating catalysts, including potential corporate restructuring or possible buy-outs. Sector Zen is managed by investment manager Trond Hermansen, who has extensive experience in managing Japanese and Asian equity funds from several firms, and analyst Lars R. Solberg. The fund generated a solid compounded annual return of 8.7 percent since its inception through the end of July of this year, despite ending the first seven months of the year in the red at 4.1 percent.

The fund's performance this year can be partly attributable to the lack of new takeover announcements within its long book. However, Trond Hermansen believes the relatively low number of takeovers in 2018 is just a pure coincidence. "We believe the underlying trend [of more takeovers] is intact, although the number can fluctuate from year-to-year," Hermansen told HedgeNordic. Meanwhile, the escalading trade war has also left its marks on Sector Zen's performance. According to the fund's letter to investors for June, value stocks are already back to the same relative levels as the summer of 2016, characterized by the turmoil caused by the Brexit vote.