

Challenging the value of hedge funds

Stockholm (Hedgenordic) - Erik Penser Bank's recently appointed head of asset management, Jonas Thulin (pictured), sees little value adding hedge funds over ETF:s as the plethora of cheap index products has expanded and improved over the years. By applying very simple performance and correlation criteria, 98 percent of his hedge fund universe fails to meet expectations, the ex. Nordea and Crédit Agricole strategist argues.

Most of his professional life, Jonas Thulin has worked with economic forecasting trying to find investment trends that could be exploited, either from an asset allocation standpoint or from an operational business perspective.

Starting out at Swedish telecom giant Ericsson in 2000 as responsible for forecasting the telecom market and working with financial forecasting, Thulin transitioned to a role in 2006 as a senior FX and fixed income strategist at French banking Group Crédit Agricole. In 2008 he left to join Nordea as head of strategy and research and later heading the global alpha strategy and asset allocation team.

Last year, Thulin joined Erik Penser Bank as head of asset management. At Penser, he is primarily responsible for managing the bank's discretionary mandates and to overlook a couple of funds. His role also encompasses forming the big picture thematic views on which the asset allocation theme acts. In the monthly "house view" the team pictures the broad market trends and what they see as being the major triggers in the shorter term.

Thulin aims to stay active in allocation decisions and recently has made some major allocation adjustments, one of which is selling out completely of Swedish small-cap companies, fearing the impact of the coming election results in Sweden. On top of that the allocation team positioned for rising Italian interest rates during the summer while also buying into utilities in the US and selling off emerging markets exposures.

The team looks at markets from a 0-3 month and 3-6 month perspective, currently holding a somewhat neutral view on equities, being bullish commodities and alternative investments and bearish the Swedish krona, in the fixed income space the team is taking down risk in the very short term and holds an overall bearish stance.

"In short we see a completely different growth path in the US compared to Europe and Sweden, where the economy in the US is picking up while Europe and Sweden show declining activity. Differences in interest rate levels, inflation levels, consumer confidence levels and investment flows are guiding our positioning. We currently believe in a stronger dollar, particularly against the Swedish krona, higher volatility, lower growth in equity markets, higher interest rates and inflation and higher gold and oil prices", Thulin says.

In order to exploit their thematic views, the asset management team at Penser systematically scan the universe of available products to find the most efficient way of executing trade ideas. More often than not this results in allocations to one or more ETF:s.

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Also in the alternatives space, Penser is looking increasingly at cheap exposures and has reduced the number of hedge funds to only a handful.

"Since I joined a year ago, we have reduced the number of hedge funds from six to currently three. This is a result of the fact that very few of these funds live up to expectations and charge high fees. Even putting soft requirements on performance and correlation measures filters out the vast majority of these funds in our screening process. If we want performance to be positive over 3 months, 1 year and 3 years while holding a correlation to equities of below 40 percent, our selection universe falls from 597 to 10 funds", Thulin says.

Thulin is particularly sensitive to hedge funds showing a positive bias and correlation to equity markets as this is not serving any purpose from a portfolio perspective.

"We want the alternative exposures to serve as diversifying components in our portfolio and we have sold out of funds showing a systematic correlation to global equities.", he says.

Using hedge funds as a means to protecting the portfolio from tail risks and major market equity downturns seem to be a sought-after characteristic, but Thulin is yet to be convinced about using CTAs in that context.

"We have been quite dissatisfied with the way CTAs have managed to exploit underlying trends in recent years. We have seen quite consistent trends in equities, bonds, and commodities but with very little output from the managers. Again, in this context, we think there are alternatives on the ETF side where multi-factor ETF:s including the momentum factor is a real option these days."

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Where he sees alternative strategies fulfilling a need is within very niche strategies where Thulin and his team have difficulties finding the exposure elsewhere.

"If we want exposure and exploit relative value opportunities in Swedish fixed income markets, for example, we do not have the competence in-house to do a good job on that side. In that case, passive investments are no real option either so we would end up looking for hedge fund talent."

Thulin also points to the fact that the active and somewhat opportunistic approach they have when allocating portfolios currently does not support the case for hedge funds given the weakness of the industry as of late.

"A fund could look great over five years but that does not help us in the short term as our clients are

typically more short-sighted looking at what the portfolio brings on a yearly basis. This currently makes the case for hedge funds a bit more difficult.”

What is then included on the alternatives side given the bullish house view on the asset class?

Thulin says that the alternatives bucket has been somewhat redefined lately putting things in that does not fit into the other silos of the portfolio.

“We have positioned for higher inflation expectations and been shorting Italian bonds through derivatives. These positions have been put into the alternatives bucket together with more traditional alternatives exposures including hedge funds.”

As it stands, the portfolio that Thulin and his investment team runs has added 8 percent on the year with a Sharpe of 2.2 over the last 12 months and he says that the main priority is now protecting the downside as he foresees increased volatility ahead. Remains to be seen if a more challenging market for perceived risky assets could have him revisit hedge funds again.

Picture source (c): Affärsvärlden