Holding Steady in a Shaky Market

Stockholm (HedgeNordic) – As HedgeNordic took a closer look at last year's winners, **Bodenholm** stood out as one of the few fund managers having held a steady keel in last year's rough markets. With a full year performance of 6.5%, Bodenholm one ranks fourth out of 60 funds in the equity category of the Nordic Hedge Index. HedgeNordic asked Per Johansson *(pictured)*, fund manager and founder of Bodenholm, how his team generated this positive return while dealing with risk management.

"Some people talk about a crazy year," starts Johansson, "I would say that what we saw was a repricing of risk, rather than a totally unexpected market correction. Markets for both equity and bonds had been going up for a long time, and some segments had reached very high valuations. Many investors ended up concentrating in similar assets, which may have accentuated the correction. It ended up being a wasted year for the hedge fund industry. While we didn't aim to time the market exactly, we did expect an opportunity to see the spreads between winners and losers increase. Given that it happened as we wished, I'm slightly disappointed that we didn't do even better."

More Juice Could Have Been Squeezed Out of Longs, Successful Shorts

On the one hand, Johansson believes that timing could have been improved on the long book but worked out for the best on the short side. "Some of our longs hurt us, as they had high cyclical exposure," he says. "However, we were protected by a solid short book. The alpha from the short book wasn't as high as we would have hoped, but the relative sizing of the book helped us to keep our net exposure closer to neutral. We have extended resources in strengthening our team dedicated to identifying short candidates as we hired one more analyst early in the year. As a result, we had opportunities to add more positions to the short book promptly."

For Johansson, a successful short relies on the ability of the manager to get three aspects right: fundamental analysis, risk management, and position sizing. "We went back and looked at the positions that generated the most alpha, and we adjusted our tactical sizing in accordance," he explains. "For us, the most effective strategy is to line up a larger number of small positions, rather than sizing to conviction, which involves an element of timing that is even more unpredictable on shorts than on longs."

While some of the long stocks worked against the portfolio in 2018, Johansson is confident that the rationale behind the investment case is still there, and he looks forward to the bounce. One example is a private jet airport operator the fund invested in. "This is a typical case for us, as we focus on spin-offs or de-conglomerations. In this case, we are looking at a monopoly infrastructure asset, benefitting from strong pricing power, and some volume growth over time. The company is selling a third of its non-core activity (aeroplane maintenance and repair) to become a pure play. In 2018, the company announced a growth slowdown from 3 to 2% and the PE multiple contracted violently from 16x to 9x, taking the stock price down 35%. Of course, we were surprised by the magnitude of the reaction, but we are as optimistic as ever that the case is still there, and we expect the stock to bounce back when their divestments are complete, and the industry growth stabilises."

"Could we have picked a better timing?" continues Johansson. "yes, of course, we can always do better, and perhaps most in terms of sizing, we could have started with a smaller position and waited for a fatter pitch. On the other hand, timing is the hardest thing to get right. We looked at a hotel chain which we believed was attractively valued, and we started buying slowly, given the cyclical nature of the sector. Then the company got bought out by LVMH, and we regretted not having bought more."

Stock Picking in Focus, Plans, and Success

Going into 2019, Johansson believes in keeping the cyclical exposure low. "We position ourselves to gain from company-specific risk instead of cyclicality," he explains. "Schibsted, for example, is a more volatile stock, and we believe in its long-term value, which will benefit from its monopolistic position."

After all, there may be further downside ahead. "The risky stocks got dumped, yes," says Johansson, "but we are one year further in the cycle, and there is much downside left in the economy. It is hard to say that it is all already priced in." For the team, the path going forward is to continue to focus on the stock picking, with a proven recipe. "We currently have 22 longs and 35 shorts. We don't have any top-down plays, and we continue to look for de-conglomerations, spin-offs as well as those we call 'quality compounders'," describes Johansson.

Johansson will also keep busy during the first quarter, as the fund is launching a UCITS version of its strategy. "Foreign investors are sometimes skeptical about Swedish AIFs, and we want to offer them an alternative that they will be more familiar with while keeping the same strategy that has worked well for us so far," he says. To share the workload, Johansson will be able to count on three new operational recruits including, Erik Orving, who joined in July last year from Stockholm- based Rational Asset Management and recently took over the role of CEO of the firm.

Last but not least, Johansson attributes at least part of its success to the support he has received from the platform the firm is part of. "I am particularly glad about the relationship with have with Brummer & Partners who have believed in us from the start," he adds. "They have been very supportive all along. Many investors commit the mistake of looking a three-month rolling performance, but real winners are made over several years. Brummer & Partners shares this belief with us, and we can count on them when we need it the most. When the markets are rough, who needs a fickle partner?"