Global Reach with a Local Focus

Stockholm (HedgeNordic) – The Swedish corporate bond market has long been characterized by low liquidity compared to other bond markets. When liquidity dried up in March last year due to a flight for safety among fund investors, many UCITS funds active in the market simply had to shut down their doors for redemptions. “The negative aspects of more traditional UCITS funds were fairly clear or became clear a year ago in the Covid-crisis,” Peter Gummesson *(pictured)*, portfolio manager at Gothenburg-based corporate bond fund manager Aktiv Ränte Rådgivning (ARR), tells HedgeNordic.

“A lot of Swedish corporate bond funds offering daily liquidity closed for redemptions for a period of about two weeks, so that explicit or implicit promise of daily liquidity did not actually materialize,” he emphasizes. “To keep this promise going forward, these UCITS funds that are focusing on corporate bonds, which are intrinsically illiquid, will have to maintain a large amount of liquid assets in their portfolios and that will diminish their expected returns,” he adds. For long-term institutional investors who can leave capital in an investment for extended periods of time, closed-end alternative investment funds may be a more suitable alternative for investing in corporate bonds, particularly in less liquid high-yield issues.

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Aktiv Ränte Rådgivning (ARR), which oversees about SEK 4 billion in corporate bonds across discretionary mandates and alternative investment funds, is launching its fourth AIF, Räntehuset 4, that will invest in global high-yield corporate bonds. "It is a closed-end alternative investment fund with a five-years maturity that will pay an annual coupon of six percent on a monthly basis," says Gummesson. After its expected launch in late March and two additional capital raising rounds, the fund would be closed until reaching its maturity in 2026. "We are paying out a monthly coupon of 0.5 percent and then investors get the residual of our holdings in the end, which may be a bit more, around or below par depending on the performance of our holdings."

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Per Thornadsson, Co-Founder/CEO

The non-redemptive nature of closed-end structure enables ARR's four-member investment team led by founders Per Thornadsson and Johan Eriksson to be patient when making investments without experiencing the pressure of focusing on liquidity, which can impact investment decisions and expected returns. "This daily liquidity offered by UCITS funds comes with a cost, with an opportunity cost that long-term-oriented investors should not bear," explains Gummesson. "In March of last year, UCITS funds had to sell what they could sell, so one might end up in a situation where the good assets are sold at low prices and the remaining customers are stuck with the bad assets that could not be sold."

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Going Outside the Nordics

For its fourth AIF vehicle, the well-established manager in western and southern Sweden is focusing on the global high-yield arena rather than pursuing a pure Nordic focus. "We do not have a specific Nordic focus," Gummesson tells HedgeNordic. "We can invest in the Nordic countries and we do, but that is not our prime focus," he emphasizes. "To reach an expected return of six percent, you need to go up to the high-yield spectrum and have a more global focus."

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"Yields have come down and spreads are compressed, but one of our strengths is that we have a broader investment universe," says Gummesson. "We can look at different countries and different currencies, enabling us to find some very interesting bonds with high interest rates," he adds. "Going outside the Nordic countries, you can be more opportunistic and find different kinds of opportunities."

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To achieve mid-single-digit returns the Nordic corporate bond market, "you have to be a buy-and-hold investor of high-yield bonds," according to Gummesson. In the more liquid global corporate bond markets, one can pursue a more opportunistic approach to capitalize on attractive risk-reward opportunities. “If there is market volatility leading to attractive special situations, we can go in and buy a bond at a discount for a company we like and wait for a price appreciation,” says Gummesson. “You can do that in those kinds of markets, because they are more liquid,” he continues. “It is much harder to do that in the Nordics.”

Approach to Avoiding Bankruptcies

The investor rush into high-yield debt has led to compressed spreads and low yields, reflecting a thirst for returns and increasing confidence that even the lower-rated and struggling businesses can survive the coronavirus-stricken busines environment. “If insolvencies from upcoming maturities in the high-yield space are going to rise, that is anybody’s guess,” argues Gummesson. “You would always see bankruptcies and defaults in the high-yield space,” he warns. “But there are two ways to avoid that.”

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Maria Blidstedt, Business Analyst

“One is basically to do your homework, which means being thorough in your investment analysis,” says Gummesson. “We have a strong team, so we are at least as good as everybody else in the market on that.” The investment team comprises co-founders Per Thornadsson and Johan Eriksson, who started Aktiv Ränte Rådgivning (ARR) back in 2012, as well as Peter Gummesson as portfolio manager and Maria Blidstedt as ESG-focused business analyst.

> *“There are two ways to avoid that. One is basically to do your homework, which means being thorough in your investment analysis. The other way of diminishing the risk associated with bankruptcies is through diversification.”*

“The other way of diminishing the risk associated with bankruptcies is through diversification,” Gummesson tells HedgeNordic. “We are more diversified in our approach by maintaining about a hundred holdings in our portfolio and thereby we diminish the risk,” says Gummesson. “If one investment blows up, for instance, its impact would be much smaller for our diversified portfolio than for a more concentrated portfolio,” he adds. “We acknowledge that we will face difficulties, because, statistically, there will be some investments that will have difficulties and some may even default, but we try to lessen the possible impact of a default by having a diversified approach.”

ESG-Driven Opportunity Set

The team at ARR has also integrated environmental, sustainability and governance (ESG) factors into their investment process. “We have three seasoned portfolio managers and one analyst dedicated or looking at ESG aspects, so ESG is very much integrated in the investment process,” says Gummesson. According to Gummesson, “the ESG wave that we have seen in the recent past” may be creating opportunities in the high-yield space, too.

> *“There are a lot of opportunities in sustainability-linked bonds, where you can find companies that are perhaps not perceived as being green today, but you can help them in the process of becoming green.”*

“If you are very rigid in your ESG analysis, you focus on buying green bonds, which are basically the best assets from a certain issue,” says Gummesson. However, the ARR team sees a lot of opportunities among the issuers requiring capital for their transition to a more ESG-friendly business model. “There are a lot of opportunities in sustainability-linked bonds, where you can find companies that are perhaps not perceived as being green today, but you can help them in the process of becoming green,” argues Gummesson. “Some of these investments can help businesses change their processes to become greener and helping them can be a win-win both for the environment and the public, but also for the investor.”