

# Entrepreneurs battle on despite downturn



Joel Benarroch, chief executive officer and chief investment officer, BPH Capital

Although it is much easier to start up in other countries, groups of French entrepreneurs are setting up their investment boutiques and trying to win the hearts and minds of investors – despite the recent slumps in the market and regulatory barriers

It was US President George Bush who was credited – quite wrongly, as it turned out – with saying that “the problem with the French is that they have no word for entrepreneur”.

Try telling that to people like Rémy Pierre and the other former members of the Lxis equity-linked department who established the 100% independently-owned Anakena Finance in May 2006. Five months later, Anakena launched its first hedge fund – the Cayman-registered multi-strategy Maximus Fund, which returned 3.57% between the start of October 2006 and the end of the year, and a further 10.44% in 2007.

Unfortunately, much of that stellar performance was eroded in January, which after a stable start became something of a horror story for Anakena (as it did for many funds), somewhat undermining the derivation of the manager's name. Anakena is one of the beaches on Easter Island and is famous for 900 ‘Maori’ basalt statues which, according to the manager's website, have withstood “nearly 3,000 years of weathering and remain today as symbols of solidity, serenity and continuity”.

Pierre says that, by 18 January, Maximus was flat for the month. Then, a combination of extraordinary events, including the Société Générale ‘rogue trader’ crisis and the unprecedented intra-meeting 75bp rate cut by the US Federal Reserve, led to mayhem in volatility levels on either side of the Atlantic. The upshot was that, in the second half of January alone, Maximus lost almost 7% of its value.

So did Pierre and his team look back during those turbulent late January days, wishing they had never

abandoned the relative security of life within a large institution? Far from it.

“When you're in a big institution you are organised with a silo approach, with one desk looking at credit, one focused on convertibles, one on volatility and so on, and it's the same structure at the big hedge funds,” says Pierre. “We were convinced that there was great value to be derived from building a team that is able to trade across asset classes and, although we may have made some mistakes in January, we still believe we will be able to generate profits for our investors in any kind of market environment. After all, our team was profitable for nine years in a row, and that was in good as well as bad markets.”

Like the Anakena team, Eric Robbe, Arnaud Yvinec, Gabriel Teodorescu and David Lenfant had highly impressive track records as prop traders when, early in 2007, they decided to use the experience they had gained since 1990 on the equity desk at CIC to set up Laffitte Capital Management.

Laffitte's inaugural fund, a merger arbitrage product, was launched in mid-December last year, which Robbe and Lenfant see as the first in a family of funds offering exposure to a complete selection of single strategies, including event-driven, distressed situations and long/short equity as well as convertible bonds.

The risk arbitrage fund, which had assets under management of below €10 million as of February 2008 – which Robbe and Lenfant believe will soon be seeded to take it to at least €50 million – is focused principally on announced merger deals in

Europe and the US, and draws from a historical database of more than 500 M&A-related transaction strategies.

Robbe reports that the fund has made a promising start, delivering a return of 2% in February in very challenging market conditions. He believes the timing of the fund's launch is auspicious, given the potential for M&A activity on either side of the Atlantic. "The M&A market tends to be very active at the beginning and the end of economic cycles, and we are expecting the same pattern to be followed this year," he says.

Perhaps the most intriguing element of the Laffitte story is in the positioning of its product with investors because the merger arbitrage is effectively a US-style fund that is offering something new to a client base that is mainly French. "We want to bring something genuinely new to the Paris market," explains Lenfant. "A lot of the hedge funds in the French market are cash-enhanced products, and we wish to offer investors a pure hedge fund based on a single strategy and the sort of transparent processes you find in the US."

How, then, to tailor the fund's prospective returns and volatility targets to cater to a more conservative French investor base, while also ensuring that the product could appeal to a broader international audience?

"The average return of French alternative funds is in the region of 6% to 8%, but we realised when we started to meet investors in London that they were expecting to see something like 15%, and did not seem to worry if volatility levels were as high as 7% or 8%, which is the opposite of what French investors would expect," says Lenfant. Hence, Laffitte's decision to position its funds between the two worlds, with a performance target of about 12% and a maximum volatility level of 5%.

That, of course, could work in one of two ways: it could be a sweet spot that attracts international as well as local investors, or a blind spot that falls between two stools and attracts neither. To date, however, Lenfant believes that it is clearly doing the former.

"It is true that, before last summer's turmoil, this target may not have been aggressive enough for US or Swiss investors," he says. "But, following the credit crunch and bearing in mind that our leverage is about two times, we now match international standards much more closely."

As for French investors, Lenfant says they have

been much more open to new ideas than would be suggested by their conservative image. "The asset managers we have met in France have been very happy to meet new hedge fund managers," he says. "Their view is: why invest in hedge funds in London and New York when a local manager can provide similar returns and volatility?"

Another wholly independent, recent new entrant to the market that believes it will be able to exploit shifting investor preferences is B PHI Capital, which received its regulatory approval from the AMF in June 2007. B PHI's CEO and chief investment officer is Joel Benarroch (hence the 'B' in the firm's name) who has over 20 years' experience of fundamental research, analysis and portfolio modelling, 15 of them spent at Dean Witter Reynolds and Jefferies.

He explains that the B PHI investment philosophy is based on four simple convictions. "First, we believe that the equity product is the best way to participate in economic growth," he says. "Second, we like stock exchanges and favour listed companies over OTC or unlisted ones. Third, we don't like leverage, which we think can be a very dangerous tool when you're talking about investment. And fourth, we see volatility as an impediment to long-term performance."

And he notes: "Our idea was to develop a product that would achieve the long-term performance of our investment universe, which is mid- to large-cap equities listed in the Eurozone, while minimising volatility," says Benarroch. "How will we do that? By combining a fundamental value-based approach on the stocks in our universe with a derivatives approach."

B PHI's Value Square Euro Fund was authorised by the AMF in July 2007, with Benarroch reporting that the product has a target of delivering returns of between 6% and 9% with one third of the volatility of the underlying markets.

"We started to invest in mid-September and were fully operational by the start of October," says Benarroch. "Between inception and the end of February, our fund was down by about 2% compared with a decline in the market of 16%. So we have already achieved one of our objectives, which is a much lower volatility level."

Benarroch is convinced that the market has undergone a fundamental change over the past 12 months and that this metamorphosis has dovetailed very neatly with the B PHI philosophy in at least two ways.

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From left – Gabriel Teodorescu, David Lenfant, Arnaud Yvinec and Eric Robbe, Laffitte Capital Management

The first is the change in attitudes to leverage. “The prime brokers we saw when we were setting up asked us how we could call ourselves an alternative fund if we had no leverage,” says Benarroch. “Today, I think most people would agree that the market would not be in the predicament it is in if people had had less appetite for leverage a few months ago.”

The second development playing into the hands of B PHI, according to Benarroch, has been the blow-up in the OTC derivative markets and the debate over mark-to-model versus mark-to-market pricing mechanisms. “A clear preference has emerged demonstrating the importance of liquidity and pricing transparency when you’re managing institutional money,” he says.

Fair enough. But how does a newcomer like B PHI, which is completely independent and has no track record, set about raising the assets under management that it will need to achieve anything like critical mass?

To date, B PHI has gathered about €7 million. Although Benarroch says that he has soft commitments for an additional €10 million from a client base made up chiefly of French and continental European institutions, he concedes that this is hardly a felicitous time for fund-raising, for a number of reasons.

Quite apart from wanting to see a demonstrable track record, institutions looking at a small player like B PHI have the added problem of internal limits for direct investment which prevent them from taking more than 5% or 10% of an individual fund.

Another complication for smaller newcomers, says Benarroch, is the relative dearth of seed funding in the French market. “We have had no seeders – not necessarily by choice,” he says. “There are perhaps five or 10 incubators in France, but they are very different from those that you see in markets like the US or the UK. It’s very clear that they

are not very prepared to bet on small firms like ours and to provide the same flow of very early stage investment that you see in Anglo-Saxon countries.”

Other new entrants to the market echo the view that seeding is surprisingly hard to come by in France. Saturne Capital was set up in early 2006 and, at the start of March this year, launched its first fund, the Saturne Capital Cayman-registered Global Macro VAR 10. This vehicle aims to use futures and options on stock indices, interest rates, currencies and commodities to deliver an annual absolute return of 15% with a maximum volatility of 8%.

That obviously makes the fund much too new to draw any conclusions about the effectiveness of its management style, but the CVs of its founders suggests that there will be no shortage of experience in the Saturne team. Its CEO, Georges Fezenko, led a team of proprietary traders at Credit Lyonnais (and then at Calyon) in Paris, London and Frankfurt, while its other partners, Frédéric Demonchy and Thomas Iriart, were previously on the trading desks of Credit Lyonnais and Société Générale Asset Management.

Saturne’s COO, meanwhile, is Roland Voirin, who spent 32 years at Citibank in Paris, latterly as CEO, before joining the Deutsche Bank team that managed the Banque Worms liquidation process. When Voirin was approached with an offer to join Saturne, he jumped at the chance; as he says, it is much more fulfilling to be involved in launching a new company than liquidating an old one.

Fulfilling, perhaps. But also challenging because, for Saturne, the process of raising assets from investors appears to have been a casualty of sub-prime jitters. Saturne’s initial approaches to institutions in the first half of 2007 went well enough, says Voirin, with investors advising the new fund to opt for an offshore rather than an onshore structure.

Those same investors, however, cooled after August, with some previously promising prospects telling Saturne that they were putting all allocation decisions on hold until further notice. Potential seeders, meanwhile, also gave Saturne an unenthusiastic response. “We were only looking for seed funding of between €10 million and €30 million,” says Voirin. “But even for that amount, the seeders we spoke to said they wanted a six- to 12-month track record.”

Faced with an apparently unanswerable chicken-and-egg conundrum as far as raising external fund raising was concerned, Saturne’s founders will be

relying on their own investment as they build a track record for their inaugural fund. While he acknowledges there are clearly risks associated with this approach, Voirin is confident about Saturne's longer-term prospects.

"We were never expecting anybody to put in €100 million on day one, but we have a number of investors who are looking to participate in the future," says Voirin. "I wouldn't describe these investors as having made commitments, but they have indicated that they intend to put in at least €25 million by year-end. Of course it's a risk, but we are certain that the risk is small, given that we will be showing good absolute returns on a monthly basis."

Not all the newcomers to the market tell a similarly upbeat story about the availability of seeding for players, without a track record, as independent operators. Robbe and Leniant at Laffitte report that deals with seeding partners in France and overseas are in progress, helping to bring assets under management at their new merger arbitrage fund to €50 million.

Nevertheless, it would appear that some of the most active hedge fund incubators in the market have been identifying more opportunities outside France than they have locally. Take as an example the portfolio of incubations that have been made in recent years by New Alpha Advisers, the specialist incubator established in September 2003 by the independent alternative investment management group ADI.

Antoine Rolland, the CEO of New Alpha, says that none of the six companies in which the incubator has assets of €155 million (as of the end of 2007) is in France. Two are long/short equity funds, one based in Singapore and one in New York, while New Alpha's largest commitment is to an asset-backed lending fund in Geneva. Of the others, two are based in London – one of which is an India-focused long/short equity fund and the other a commodity

fund – while the sixth is an emerging markets multi-strategy fund located in London and Prague.

Globally, Alpha has not had any shortage of candidates for seeding. According to Rolland, it sees an average of 150 potential projects a year, meaning that it has evaluated more than 500 since its inception. However, he says that French opportunities are still relatively thin on the ground compared to those in other markets, and that it has been attracted to funds outside France – as well as in a range of different strategies – for diversification reasons.

"A trend we like is that, as markets become more regulated in emerging economies, it becomes possible to deploy more strategies and to find more talented local managers," says Rolland. "That is why we have looked to eastern Europe and Singapore for new opportunities."


Whether all the 100% independent newcomers to the French hedge fund industry will be able to survive and prosper in an increasingly competitive market is open to debate. At Asterias, Sophie van Straelen says that she admires the bravery of the start-ups, but she also says that she is surprised that so many boutiques have sprung up at a time when fund-raising among institutional investors is more difficult than it may have been two or three years ago.

One highly experienced manager, in the form of Jean-Pierre Aguilar, the CEO of CFM, sounds a warning when he says that, to be a successful quant manager, a newcomer would probably need to invest in the vicinity of €20 million to €25 million on a strong and credible research capability along with a range of other overheads. "That means you probably need to have about €1 billion of assets under management before you start making money," says Aguilar. "Maintaining a competitive business with €200 million or so of assets is probably doable, but very challenging."

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Roland Voirin, chief operating officer, Saturne Capital

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