Interview with Loïc Fery, CEO of Chenavari

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While looking at the data we noticed there was only one hedge fund, which made the list for 2010, 2011, 2012. Additionally, the fund was the top performer in 2010. Furthermore, little did we know that the fund also had a good return in 2009. And finally, the hedge fund, which uses credit strategies, was only formed in 2008.

One of the few professionals behind the now famous hedge fund, Chenavari Toro Capital, founder and managing partner of Chenavari Investment Managers, Loïc Fery, was kind enough to answer some questions we had.

Below is our Q&A with Fery and his insights of the credit markets in Europe.

What is your firm's strategy?

Chenavari Investment Managers' focus is European fixed income credit markets investing. We endeavor to consistently deliver superior returns from targeted investment opportunities across niche European credit markets to our clients' benefits.

Chenavari invests across sub-segments of European public and private credit markets including Corporate & High Yield, Financials, Asset-Backed Securities on public securities and derivatives side. On the private lending side, we are active in European Leveraged loans and Direct Lending (to both Corporate and Real Estate borrowers) as well as bilateral transactions with banks, so called Regulatory Capital transactions.

Through its combined expertise across European credit markets, Chenavari is uniquely positioned to exploit the diverse investment opportunities arising from European banks' deleveraging, which – by the way – is only starting.

Are you inspired by any names in the investing world, or by someone who has mentored you through the early period of your career?

The most inspiring alternative investment firms for me have always been the ones that have been able to navigate various segments of the markets to consistently deliver performance to their clients, as opposed to those who have made a fortune out of a specific market situation, but which then have been struggling to perform in the long run.

I believe that a key success factor for Chenavari will be our "double obsession" towards both total performance on one hand, and operational risk on the other hand, as opposed to asset gathering, which is certainly not a priority. Chenavari is only 5 years old, but in several occasions we decided to no longer accept subscriptions from investors. We only take money when we feel that the opportunity set is right.

Before setting up Chenavari, I have been running various credit trading & investing groups: The professionals who played an important role in my development as an investor include Marc Litzler, former CEO of Credit Agricole CIB and one of the architects of equity derivatives trading at Societe Generale, as well as G.Laffineur, J-P Mustier, O.Abukhadra and J-M Beacco to whom I reported to at various stages of my career.

We wanted to confirm total AUM, we have from HSBC hedge weekly, $2.4 billion is this accurate?

As of February 1st 2013, Chenavari total AUM is $3.5bn. The firm was started almost 5 years ago (May 2008) with at the time only 40m AUM invested in a corporate credit & high yield arbitrage strategy.

Can you please confirm the returns for your firm's Asset-backed Securities strategy, namely the flagship fund Chenavari Toro Capital I:

Our European ABS fund, Chenavari Toro Capital I, launched in June 2009, has produced good net returns to investors.~~:~~

The total AUM of our European ABS fund, called Chenavari Toro Capital I is $362M.

Do you think the Euro crisis is over? Are you finding value in any of the various strategies in the more distressed countries, Greece, Spain, Italy etc?

In 2012 European Central Bank actions, such as ECB "we will do what it takes to protect the Eurozone", acted as a game changer. We believe that ECB will remain key in stabilizing European markets going forward.

With an ECB "effective back-stop" in place, EU credit spread yields will continue to grind lower as investors re-balance their portfolios in search for yield. In Europe, should the ECB makes its words good and support Sovereign debt at any cost – which we consider as a credible central scenario- we believe that Europe will find the path for economic recovery, most likely in 2014 after a muted rebound in 2013.

The European investment arena will slowly migrate from a break-up event to a traditional economic cycle investment environment where credits trade exclusively on their fundamentals, regardless of where they are domiciled. This being said, any fiscal slippage or economic underperformance compared to growth expectations in Euro economies – which is likely in our view in 2013 – may translate to further ratings downgrades, hence market volatility.

In our view, it is likely that macro risks will arise towards the summer of 2013 when investors will be able to re-assess the performance of Spanish and Italian economies in light of severe austerity, at a time when Italian bond redemption will be the greatest. Key investment themes in credit markets include "Core Europe v. Periphery" and "within the capital structure" compressions.

On all credit investments, focus will shift from liquidity and systemic risks to discriminative and fundamental credit risk where relative value prevails. In Euro asset-backed securities, we expect to seek value in long duration and discounted mezzanine ABS sectors where we are comfortable that the underlying assets will perform not just in a benign scenario but will also be protected should defaults rise back to distressed levels.

European bank deleveraging will in our view accelerate in 2013 as banks earnings recover allowing them to sell assets at a loss and/or afford risk-weighted assets reductions transactions. Regulatory capital strategies will continue offering attractive investment opportunities on high-fundamental quality underlying assets, purchased at implicit large discount to historical default rates.

Chenavari's European ABS strategy is not crowded by a large number of hedge funds. In addition to Chenavari and Scio, Cheyne Capital and GLG Partners what other firms have recently been investing in these areas? Are you starting to see the market change as more funds feel more comfortable investing in this area?

When it comes to European Asset-backed Securities, we indeed have seen a few opportunistic managers to try to deploy capital in the space, especially in the first half of 2011. In Q1 2011, when we saw that significant players suddenly had a strong "bid" for the European ABS asset class, combined with our growing concerns with regards the overall European systemic risk, we decided to take profits on 50% of our portfolio, raising cash levels from 5% in January 2011 to almost 50% by the end of Q3.

We are not buy and hold investors. We can suddenly change our risk appetite and allocation within credit asset-classes.

This is a strong differentiating factor of our approach towards credit investing compared to some of our peers. We actively trade our positions to constantly seek portfolio optimization and monetize potential gains, as opposed to more traditional ABS investors who will tend to sit on their positions hoping for capital appreciation and enjoying carry positions.

While our European ABS strategy – Chenavari Toro Capital I – appears obviously as our flagship performer (+60% annualized performance net returns to investors since June 2009), the firm has also been quite successfully investing across the entirety of the credit spectrum in Europe.

Our corporate credit, regulatory capital and real estate debt strategy performed very strongly in 2011 as did our European ABS fund. We find compelling opportunities for each of these strategies in 2013.

Yes, other players have emerged and in many cases we have found this to be beneficial providing increased liquidity to the market. However, it should be noted that we find our focus significantly unique and less affected by the competitors mentioned.

Additionally, do you see changes in the marketplace as investors in general reach for higher yields?

We see a significant interest from investors in our strategies. With a 5-year strong track-record, Chenavari has developed a strong working relationship mainly with large institutional investors and large family offices, which are the main sources of capital at the moment.

This being said, this is not the investors' appetite that drives our product offering: as mentioned earlier, we have in several occasions turned down subscriptions when we feel the timing is not right.

Given the opportunities that we see in the European credit markets, all our investment strategies are currently opened for subscription.

Which loan portfolios have performed well or what fundamentals does the investment team looks for when choosing?

Everything we do at Chenavari is based on a solid understanding of the underlying credit collateral fundamentals. All of our strategies are focused on in-depth collateral analysis. There is no such thing as "this is cheap so this is a good investment". We only invest in portfolios or transactions where our expect teams fully understand the risk and have a strong conviction on the fundamental value.

We were just curious about the real estate debt strategy – Chenavari Real Estate Debt- launched in late 2011, AUM (we found 250 million euros) and performance?

The Real Estate Debt strategy is aiming at capturing the opportunity created by traditional real estate lenders being unable to refinance existing positions. There used to be over 90 commercial real estate lenders in the U.K. and in Germany a few years ago, and today, given the regulatory capital constraints implied by real estate debt, there are only a few banks involved in real estate lending, mainly on senior debt.

This factor combined with the fact that there is over 150bn euros of real estate debt maturing over the next 3 years in the U.K. and in Germany, this creates a substantial market opportunity for alternative investors with a strong real estate debt team such as Chenavari Investment Managers.

Our team has over 40 years of combined real estate lending across U.K. and Germany. We focus on transactions from 10M to 50M euros of real estate loans, either on senior or mezzanine level. Our preference goes to prime assets located in Tier 1 & 2 cities.

The fund was indeed launched in November 2011 and we have deployed in 2012 close to 200M$ direct loans to real estate borrowers in the U.K. and Germany.

Are there any plans to expand and build a portfolio in the U.S. market?

Our core focus is profiting from opportunities in European credit markets so there are currently no plans to open a U.S. office at the moment.