SHINING A LIGHT ON……
ODEY SWAN FUND

At a glance

The Odey Swan Fund is a global hedge fund. The fund itself has only been in the market since March 2013 but the manager has been running these strategies for many years and has a fantastic reputation.

The update will outline what we mean by a hedge fund, open with some views from the manager on the world and how he is currently positioning his fund to respond to this. We will also highlight what investors need to consider before investing.

It is not easy to compare this to an index but investors could compare to similar strategies. Ultimately it is about investors agreeing with the manager’s view and believing that the strategies he employs will deliver the returns he believes will come.

Who are the team behind the fund?

The fund is managed by Crispin Odey who set up Odey Asset Management in 1991. Prior to that he managed the Baring European Growth Trust and Continental European pension funds at Barings Asset Management and Framlington Fund Managers.

He is well regarded as a manager of hedge fund strategies which we will cover in more details in the fund highlights.

Fund highlights?

The Odey Swan Fund is a Hedge Fund. Its stated aim is to achieve “strong absolute and relative returns” over the long term. The principal behind the strategy is to take long positions in stocks that are expected to increase in value and short positions in stocks that are expected to fall in value. For this strategy it can be a number of market instruments including equities, currencies etc.

Taking a long position simply means buying it and if the stock increases in value, you will make money. On the other hand, taking a short position in a stock you don’t own is about selling it and then hoping it falls at which time you buy it back at a lower price than you paid for it and you return the borrowed shares.

Hedge Funds (i.e. the Swan Fund) do this on a grander scale. At a basic level an equity long-short strategy consists of buying an undervalued stock and shorting an overvalued stock. Ideally the long position will increase in value and the short position will decline in value. If this happens, and the positions are of equal size, the hedge fund will benefit. The strategy will work even if the long position declines in value, provided that the long position outperforms the short position.

Seems complex and therefore investors need to understand this before they invest in the strategy.

The Odey Swan Fund is no different, the potential returns can be appealing but it is complex and you are reliant on the manager to deliver. Crispin Odey has an excellent reputation in making money through these strategies. After the 2001 attacks he foresaw the value of insurers rising and benefited from this hedge, equally in 2008 he anticipated the credit crunch and investors benefited. As a result he is widely seen as one of the top performing global hedge fund managers.

Listening to his update will make even the bullish of investors nervous about the future but investors need to understand that Crispin is bearish by nature and this is where he aims to make money.

It is also interesting because it gives a different perspective on the wider world which many fund managers tend to avoid talking about. In the discussion we had we covered his thoughts on the world which in turn gives an idea on how the fund is managed.

He started with his view on the debt markets and his view that falling yields places all the risk on to a deflationary environment especially in Europe. His view of Europe is fairly gloomy in that he believes the credit system is effectively broken and that Europe is like Japan in 1995. He feels that Europe will fall back into recession.

He used two economies which highlight this concern – Germany and Italy. The slowdown in Russia and China is being felt in Germany with exports in August falling at their fastest rate since 2008. They did recover in September but this was only after exports were discounted by up to 20%. This heavy discounting does not help growth because the bottom line is being squeezed.

In Italy the state of companies reflects the challenges facing peripheral Europe – 50% of Italian companies do not make a profit and only 20% breakeven. Europe needs growth to stimulate a recovery, in Italy this simply isn't happening.

Across the Eurozone the current account surplus is around 2% whereas countries like Germany have a surplus of over 7% which could be used to help the Eurozone but isn't.

There are many challenges facing Europe but growth is the key issue and with declining emerging markets it is hard to see where this comes from. Crispin believes that emerging markets are heading into recession. He believes this stems from China which has been the powerhouse of emerging markets and is now becoming less competitive and turning to more of a domestic economy. This change impacts other economies.

Australia for example is reaching capacity just at a time when the slowdown is hitting the economy, unemployment is rising and current account deficit is widening. Other commodity producers are struggling with Argentina in a financial default position and Venezuela close to following.

Even the UK is not immune with pressures in the current account deficit and no real wage growth. However the US is in a much better place and Crispin views the dollar as the place to be.

With this in mind the fund is positioned for emerging market recessionary pressures and equity market de-rating as well as for US dollar strength.

With currencies he is playing currencies in emerging markets and Australia where he sees he can add value and cutting back long holdings as he feels valuations are too high.

We touched on a short stock position which is with Swatch watches. It is a fascinating story where the inventory is 2 ½ years' worth of sales with the factories working on 100% capacity to deliver a 74% margin. As demand slows from emerging markets and the inventory grows the margins will narrow and therefore there will be a de-rating.

The nature of the fund is bearish and although Crispin may disagree this is a high risk strategy. Clearly Crispin has called things right in 2001 and 2008 and investors have benefited from this but he must have called things wrong which he doesn't tend to talk about. Investors therefore need to believe in what he says and in the strategy he employs to deliver this.

The risk is what happens if the strategy he employs is wrong and what impact will this have on the investments. Often we talk about a blended approach but to some extent this is an all or nothing strategy. If you believe he is right and there is about to be a major downturn in the global markets then you will not want to be in that market and believe either to hold in cash or invest with him and benefit when everyone else is losing money.

There is no easy way to place this fund and it won't appeal to many investors but it will appeal to some.

In conclusion a well-respected manager with a complex strategy where investors need to fully back the manager or not. It is only likely to appeal to the minority of investors.

Fund performance

Performance since launch on the 11th March 2013 to the end of September 2014 is shown below:

	2013	**2014**	**Since launch**
Odey Swan Fund	5.39%	-5.31%	0.21%

You should note that past performance is not a reliable indicator of future returns and the value of your investments can fall as well as rise. The total return reflects performance without sales charges or the effects of taxation, but is adjusted to reflect all on-going fund expenses and assumes reinvestment of dividends and capital gains. If adjusted for sales charges and the effects of taxation, the performance quoted would be reduced. Returns are based on the US share class.

The Odey Swan Fund is only suitable for experienced investors. The investment is high risk and extremely volatile and therefore you should only invest if you are prepared to accept a loss on your investment value.