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Opalesque Exclusive: A family office spin-off runs a hedge fund that invests like institutions

Monday, July 31, 2017

Geoff Dover

Benedicte Gravrand, Opalesque Geneva for *New Managers*:

A manager that spun out of a Canadian family office launched a fund last year that invests like institutions.

Heirloom Investment Management evolved out of a Canadian single family office that CIO Geoff Dover ran from 2008. This is where he originally built the investment strategy, at the request of the family who wanted a strategy that was long-term, had consistent returns of 9-11% and lower risk. The strategy officially launched at the end of 2009 and attracted the attention of other Canadian families. Dover then moved to Dubai with his wife, and there, received interest from GCC-based families as well. So in late 2015, he spun out of the family office to focus on managed accounts for these families, and launched the Heirloom Investment Fund in June 2016.

The strategy itself has delivered 11.3% annualized return (gross) since inception in January 2010, and the Cayman-domiciled fund, which now manages over $200m, has returned almost 4% from its June 2016 inception to the end of May 2017.

The strategy is "cross-asset thematic," Dover tells *Opalesque*. "Thematic essentially means that we focus on allocating capital to themes. These themes can be generated based on long-term secular trends, or on market dislocations. This takes advantage of the myriad of academic findings that found that 90% of a portfolio's return comes from being allocated to the right macro areas, whereas less than 5% of a portfolio's return comes from choosing the best individual security. Many managers focus 80% of their energy on picking individual securities, whereas we focus the majority of our energy on making sure that our capital is allocated to the right macro areas, or themes."

There are different ways to access each them, he continues, so he looks across asset classes to determine the "optimal blend of purity of exposure and value."

A lot of institutions use a similar strategy, he notes, thought it is not widespread among individual investors and family offices. McKinsey, a global advisory company, began advocating that all institutional investors should invest along similar principles in a paper called From Big to Great. During interviews for the paper, leaders told McKinsey they expect a more dynamic decision-making process structured around top-down economic scenarios, which they hope will provoke more debate and move them away from a rote approval of the SAA (strategic asset allocation) by the executive committee and board. The table below summarizes the key shifts that institutions expect to see in the portfolio construction process.

Exhibit 2

Portfolio construction by leading institutional investors in 2020

	From…	To…
Objective	▪ Deliver a base of beta returns aligned with risk/return objectives	▪ Become the engine of differentiated absolute returns ▪ Maximize the probability of meeting liabilities
Approach	▪ Backward-looking SAA driven by traditional process ▪ Anchored in last year's allocation ▪ "Why tilt?"	▪ Forward-looking house views on assets, risk factors or other cycles ▪ Clean-sheet approach ▪ "Where will we tilt?"
Decision process	▪ An isolated process focused on the office of the CIO	▪ Rigorous and participative annual strategic process
Capabilities	▪ Small teams of finance practitioners	▪ Analytical team led by thought leader with conviction

SOURCE: LP interviews; McKinsey analysis

Source: McKinsey

In summary, by 2020 leading institutions will focus much more attention on the SAA, and will reshape it into a dynamic, forward-looking, keenly debated, and deeply researched document.

The other important element to the Heirloom strategy, Dover continues, is in risk management and risk understanding. "Once we have decided on an individual theme, we look at the best individual security to gain exposure to that theme, breaking down securities into what we call return drivers. These are the components that will cause an individual investment to perform well or poorly. Quantifying this is definitely a blend of art and science, but this degree of understanding really helps us understand what our portfolios are exposed to, and very importantly, helps us to understand what could happen to them in the future under different scenarios or as new information becomes available."

The approach is different, he adds, in that it is not based on backward-focused data. "Instead, we focus on looking forward: when driving a car, looking in the rear-view mirror gives you useful data, but it should only be done periodically and as a supplement to focusing your effort on what is really important, and that is the road-ahead."

Themes

Heirloom's current themes are common-sense, he says. For example, one of the themes is based on the transition of GDP growth and economic power from the developed to the developing world. "An obvious outcome to this, is that when applying a value hat, you recognize that public equity markets in a developing world are trading at lower multiples, whereas if your economy is growing faster and therefore your corporate earnings are growing faster, you should have a higher multiple. We have close to 20% of our portfolio in this theme."

Another theme is agriculture and looks at the growing meat consumption in the developing world, which requires more grain and water to produce. "Combining this with a growing overall global population, slowing farm yield growth, and climate change, you've got this dynamic where demand is growing faster than supply, which means agriculture will do quite well."

Heirloom's third largest theme is what they call Credit Market Dislocation. As banks, following the financial crisis and increased regulation, shed entire sectors of lending, the resulting vacuum created a lot of interesting opportunities. "In the early days, with 150% security provided by prime real estate, you could lend at 12% to 15% interest rates," Dover explains. "This has become a popular investment in recent years, so we have moved to more niche areas, but the fundamentals of earning good returns with a high degree of security still remain the same. For example, trade finance, which is typically backed by commodities or easily saleable capital goods, is another area where we're seeing strong returns, and there are also interesting opportunities in private debt."

Heirloom gives its investors 100% transparency into what they have invested in, he adds. Furthermore, the senior team has 90% of their net worth invested alongside their investors.

http://www.opalesque.com/665297/A_family_office_runs_a_hedge_fund529.html