Laurium's long/short funds benefit from diversified sector exposures

Headed by co-founders Murray Winckler and Gavin Vorwerg, the Laurium team has grown to 32 individuals, based in Cape Town, Johannesburg and London

Laurium Capital's South African hedge fund range makes a convincing case for the team's active asset management process and skillset, reflecting strong risk-adjusted returns over time.

The company's longest-running product, the Laurium Long Short Prescient RI Hedge Fund, has returned a net annualised 10.7% since inception in August 2008, versus 6.5% from STeFI and 8.7% from the South African equity market (SWIX/Capped SWIX). It is 8.4% higher so far this year to end-June, against a FTSE/JSE Capped SWIX Index total return of -4.7%, after an impressive 33% net gain in 2021.

The Laurium Aggressive Long Short Prescient QI Hedge Fund has added a net annualised 15.7% since launch in January 2013, versus 6.1% from STeFI and 7.7% from the Capped SWIX, adding 11.4% so far this year after a net 49.7% gain last year.

The lower-risk Laurium Market Neutral Prescient RI Hedge Fund has added a net annualised 10.3% since launch in January 2009, versus 6.3% from STeFI. For the year so far, it is 6.8% higher.

"As investment managers we all have periods when we do well and periods when we do not do so well," says Laurium's co-founder and portfolio manager Murray Winckler. "Consistently, quite a lot of things have gone right in our long and short books, so relatively we have done well."

In its most recent hedge fund newsletter, Laurium notes that the first half of 2022 was brutal for equity markets, as ongoing inflationary pressures continued to ripple through the global economy following the tumultuous early March sell-off when the negative effects of the Russian invasion of Ukraine and the strict Chinese Covid lockdowns first hit markets.

Based on its fundamental bottom-up research process with a value bias, the Laurium funds have diversified sector exposure – chiefly across financials, basic mining and materials, consumer goods and services, industrials, and telcos, media and tech.

Its funds have benefited this year from exposure to natural resources, as a turn in the commodities cycle has brought a meaningful change in South Africa's terms of trade and to the current account deficit.

"For the past 15 years South Africa's current account deficit has averaged -4%. Last year we

Murray Winckler and Gavin Vorwerg

saw double-digit price gains from platinum, coal, palladium and to a lesser extent gold. It has significantly improved our current account to GDP ratio, which is now positive and is keeping the rand stable. In comparison, the UK is a services economy and it has a current account deficit at -8%," notes Winckler.

The resources boost comes despite South Africa's ongoing issues with logistics – the Richard's Bay Transnet-run coal terminal is exporting just 55 million tonnes a year, with plans to lift this to 70 million tonnes this year, still short of its 85-million-tonne design capacity.

"Yes, we could be doing better, in particular there are security and rail issues, but net/net South Africa is a good place right now thanks to resources."

South African stocks have held up relatively well so far this year, declining by 8% in the first half as the MSCI World dropped 20%, a strong performance in dollar terms.

The rand has also been resilient so far in 2022, impacted more recently by the resumption of loadshedding in June.

Winckler notes that South African hedge funds that focus primarily on domestic listed counters – as Laurium does – have fared well so far this year, while many with an offshore focus have battled. It's a changed scenario from recent years.

"For five years the South African equity market only added around 5% compound returns in rands. A lot of domestic counters did not do well," says Winckler. "Some stocks have rebounded strongly post-Covid – financials and domestic industrials were among those sectors to be very undervalued. We have done well by investing in quality names that had been punished by the market."

Domestic stock picks alone would not have been enough to protect against decidedly negative global markets in the first half, and Laurium added put protection on both the US and European markets, with these overlays helping this year in particular.

The team has also enjoyed successful trades in the small and midcap space, as well as some decent returns in the short book.

"MTN is a classic example of the kind of trade we have had on," says Winckler. "We were very long the stock until the end of last year. Our long-only funds had about a 6% weighting and then we went to zero. We went short in the hedge funds. The stock still held up for a bit, trading at around R200 at one stage. It is now at around R140."

With just under 10% of Laurium's R45

FUND FACTS

Laurium Long Short Prescient RI Hedge Fund

Strategy: South African long/short equity
Portfolio managers: Gavin Vorwerg, Murray Winckler, Matthew Pouncett
Fund inception date: August 2008
CIS inception date: August 2016
Administrator: Maitland
Prime broker: Investec, Standard Bank, Legae Peresec, RMB
Fund size: R2 billion
Open to investment: Yes

FUND FACTS

Laurium Market Neutral Prescient RI Hedge Fund

Strategy: South African long/short equity
Portfolio managers: Gavin Vorwerg, Murray Winckler, Matthew Pouncett
Fund inception date: January 2009
CIS inception date: August 2016
Administrator: Maitland
Prime broker: Legae Peresec, RMB
Fund size: R69.5 million
Open to investment: Yes

billion in AUM invested in hedge funds, Winckler questions why the South African hedge fund industry has yet to gain traction with institutional allocators.

"South African hedge funds are severely under-represented in the institutional space. Yes, the fees are higher than other products but the overriding issue is to look at net numbers over time. Why do big US endowments like Harvard and Yale allocate 20-30% to hedge funds? Hedge funds have way more tools than long-only funds and it seems crazy not to include them."

Kim Zietsman, Laurium's South African head of business development and marketing, notes that there has been a recent uptick in hedge fund interest from discretionary fund managers, who see the potential to incorporate them into model portfolios, and from large multi-managers.

She adds that more hedge funds are being included on fund platforms such as Glacier and Ninety One, paving the way for their incorporation into model portfolios.

The biggest issues remain fees – around which increased education is required – as well as too much net long exposure from some funds, and ongoing regulatory issues such as Board Notice 90, which limits hedge fund inclusion in broader portfolios despite similarly regulated Collective Investment Scheme mandates.

With its long/short funds convincingly beating the market over time, Winckler notes that South African hedge funds in general have a solid track record.

"The numbers tell the story," he says. "Our main long/short fund has beaten the market over 14 years – adding more than 10% after fees each year. Our aggressive fund has generated a return per annum double the market over the past decade, at a 15.7% annualised compound return. And we are not the only ones delivering in this way.

"Globally there is US$4 trillion invested in hedge funds and 70% of them are really not great. Yes, the top decile offshore is amazing but probably more than half of global hedge funds shouldn't be around. They take aggressive bets and that's not how we go about things in the South African industry."

Laurium's long books are currently focused on South Africa, where it notes that 60-65% of domestic stocks have international exposure.

Besides commodities, it has profited recently from trades in Naspers/Prosus – a position where it was "long and wrong" for a while – versus a short position in Tencent.

"We increased our bets last month on some relative trades and we think there is still more to go on the Tencent position."

Laurium's hedge funds are positioned slightly below neutral (at around 40% exposure, from an average of 55-60% since inception) while its long-only funds are fully invested.

"Our exposure is now slightly higher than it has been," says Winckler. "We do have some more aggressive positions but we remain cautious."

Its flagship long/short fund differs from the aggressive fund when it comes to position size and the addition of gearing where appropriate, with 90% of the holdings the same. The funds hold about 35 long positions on average and around 20 names each on the short side.

The main long/short fund averages around 55% net long exposure – which reached as low as 30% last month and is now sitting at around 40%, protected in June by index positions.

The funds also hold a 10-15% position in bonds, which offers a running yield more favourable than cash, including the 2035 government bond as well as Steinhoff preference shares, where it remains constructive.

The market-neutral fund is sitting around 7% net long, and is restricted to 15% market exposure, making it a low-volatility product with a solid 13-year track record of exceeding inflation while protecting against downside risks.

Laurium's dollar-based long/short Chobe fund – which includes up to 25% in pan-African names excluding South Africa – has an almost 14-year track record, delivering more than a net 8% in dollars since inception.

"Africa has been a drag on the portfolio for the past four years, but we continue to see upside for these positions, and for those in our broader African equity and fixed income funds," says Winckler.

Headed by Winckler and co-founder Gavin Vorwerg, the Laurium team has grown to 32 individuals, based in Cape Town, Johannesburg and London.

"We have a good mix of longevity and youth, and diversity is pretty important for us," says Winckler. "On a positive note, we have set up a B-BEEE Trust, which will own about 10% of Laurium Capital, and are looking forward to our first BEE rating in the next few weeks, which we hope will come in at BEE level 1."

While South Africa is in a sweet spot at the moment, Winckler remains bearish long term. Higher inflation is generally good for commodities but there is a 50% chance that the US goes into recession, accompanied by Europe and the UK. The hope is that China stimulates materially in the second half, protecting South Africa from a slowdown.

With just under R4 billion in its hedge fund products, Winckler says Laurium could easily double the assets it manages in hedge, in an environment that remains treacherous for investors.

Looking ahead, he notes that the primary risk to global equities from this point is company earnings. Analysts and company executives are still expecting high double-digit earnings growth over the next year, an expectation that seems optimistic given cost pressures and rising risks to consumer demand.

Energy prices are the key ingredient to the outlook for costs and overall inflation, and further increases in oil and gas prices will be increasingly challenging for the real economy.

"Looking ahead, the macro headwinds facing global equities remain significant. Elevated inflation, hawkish central bankers, skittish politicians, war in Ukraine and the stop-start energy transition from carbon to renewables… there are many risk factors to consider and many to be concerned about," he adds.

Global share prices are already discounting the upcoming Q2 reporting seasons, while in the South African equity market, the team continues to find value in companies exposed to the domestic economy, to global consumer names and in selected resource counters.

Laurium believes global bond yields should find support going forward as the US Federal Reserve begins to move monetary policy into restrictive territory in 2023. This should underpin the South African bond market, which is offering attractive real yields.

"Since Covid, the markets have benefited from monetary stimulus and quantitative easing. That has all changed dramatically. Rising interest rates are generally not good for equities and global markets could easily come down another 10% this year. It depends on how bad growth is next year."

"We have to be careful as there are headwinds. Bear market rallies can be vicious, and while we are active in the markets every day, we are still cautious."

FUND FACTS

Laurium Aggressive Long Short Prescient QI Hedge Fund

Strategy: South African long/short equity
Portfolio managers: Gavin Vorwerg, Murray Winckler, Matthew Pouncett
Fund inception date: January 2013
CIS inception date: August 2016
Administrator: Maitland
Prime broker: Legae Peresec, RMB
Fund size: R911 million
Open to investment: Yes

FUND FACTS

Laurium Chobe Sub-Saharan Long Short Fund

Strategy: Sub-Saharan Africa long/short equity
Portfolio managers: Gavin Vorwerg, Murray Winckler
Fund inception date: December 2008
Administrator: Maitland
Prime broker: JP Morgan, Legae Peresec
Fund size: $40 million
Open to investment: Offshore investors in dollars