Strategies for 2009

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Distressed Asian Convertible Bonds
Long only and unlevered
Closed end fund format
Asia has performing assets at distressed prices
Distressed investors, not distressed issuers
List of quasi sovereign issuers – which can later be hedged with sovereign CDS when counterparty risk is settled
Currently poor liquidity – market likely to return albeit smaller than before
Full exposure to credit default risk

Distressed Convertible Bonds
Long only and unlevered
Closed end fund format
Distressed investors purging convertible portfolios has created distressed pricing
Currently poor liquidity – market likely to return albeit smaller than before
Full exposure to credit default risk

Bond Basis
Long cash bond long credit protection through CDS
Closed end fund format
Wholesale deleveraging from cash bond investors has created arbitrage opportunity
Open to CDS counterparty default risk

Distressed Debt
Long biased
Closed end fund format
Recession has accelerated default rates
Technical selling pressure has created distressed pricing across performing and non performing assets

Capital Structure Arbitrage
Long Short
Closed end fund format
Technical selling has created arbitrage opportunities intra issuer
Long senior short sub – positive jump to default at low to non negative cost / no negative jump to default at positive carry

Capital Structure Arbitrage Distressed
Closed end fund format
Long short
Recession has accelerated default rates
Long fulcrum security – converts to equity
Short most senior non recoverable to hedge non-default spread duration

Trade finance
Open ended fund
Senior secured, over collateralized, liquid collateral, commodities or commoditized goods only
Acute shortage of capital has improved margins
Secondary market opportunities
Particularly attractive in emerging markets

Receivables finance
Open ended fund
Acute shortage of capital has improved margins
Shorter duration assets
Structured with limited recourse
Obligor / credit risk arbitrage

Deep value equity
Long biased / Long only
Open ended with lock up
Wholesale de-risking has created attractive valuations even under recessionary assumptions
Strategy variant: buy out (which would require either a closed end or long lock up fund)

Strategy variant: activist (financial restructuring)

Merger Arbitrage
Open ended with lock up
Value is available and there is a good proportion of corporates with cash
ROE and valuation differentials encourage cross border deals
Developed world acquirers, developing nation targets
Cross border skills required

Most of the above strategies would not survive a run on the fund situation and hence require a closed end structure. They are also vulnerable to mark to market divergence and thus should not be leveraged with a prime broker on standard terms. Many of these strategies could be leveraged if one could term finance the trade bundles and lock in financing rates.

Strategies I would be less inclined to recommend:

Convertible arbitrage – gamma or carry
Needs borrow that may be hard to get
Needs leverage that is hard to get
CBs are trading through their bond floors – no gamma

Risk Arbitrage – traditional in country
LBO deals are dead
There is no finance to leverage the large private equity buy out deals

Equity/Credit market neutral
Valuations not supportive of shorting
Broken business models in industries at risk of bailout
No liquidity in other shorts

Longer duration direct lending
Cyclical strategy – cash flow predictability is poor
Although spreads are highly attractive
Attractive only if it is the intention to acquire the collateral

Default rates likely to rise

Volatility – Long Biased
Long vega game is unlikely to continue to pay
Long gamma is opportunistic