NOT AN ASSET GATHERER

MENA Capital founder Khaled Abdel Majeed talks with *Mena Fund Manager* about the firm and the 10th anniversary of its Admiral hedge fund

By Rob Langston

Challenges in adapting hedge fund strategies to the region's markets have resulted in a smaller number of hedge fund focused exclusively on the region, compared with other parts of the world. However, there are still opportunities for those willing to take a closer look at markets in the region.

Khaled Abdel Majeed founded MENA Capital in 2004, launching the first Mena-focused hedge fund – the Admiral Fund – in 2006. This year it celebrates its tenth anniversary during what has been a challenging period for the region's markets.

Since inception the fund has returned 68.6% (to March 2016), compared with a -29.3% loss for the Dow Jones Mena Index. As Gulf markets felt the impact of weaker oil prices and security issues in the region became more prevalent, the fund fell by -11.9% in 2015, although it still managed to outperform the index which fell by -14.3%.

Preserving capital

The Mena-focused hedge fund has an investment to generate long-term capital appreciation and preserve capital. It aims to through a diversified, actively-managed portfolio of long and short positions in primarily listed securities and derivative instruments.

Majeed says the fund has stuck to a consistent strategy over the years to help it meet its investment objectives.

"If we don't see value in a market as a whole but like some individual stocks then we will try to hedge exposure through shorting," he explains. "If that ability is not there – like in Saudi Arabia – then we will get out altogether.

"Like many hedge funds we're not market-neutral. We are long-biased but having the shorting tool and the ability to go to a lot of cash – 80% or so – is very important if one wants to be able to preserve capital."

The MENA Capital founder says the fund's size has helped it play in some of the more interesting parts of the region's markets.

"We're not an asset gatherer; if we were we would be very big and we would be forced to be in just big liquid stocks," he explains. "At our size and capacity we can invest in all Mena countries and are not confined to the big liquid GCC markets.

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“That is why we don’t want to be a $1bn fund,” he says. “For example in 2007 there was probably was about $4bn worth of inventory for shorting. That dropped to $1bn in 2008 when you needed it most. If you were a $1bn fund and wanted $200m worth of shorts you were out of luck.”

As well as investing in the stocks with less liquidity, the fund also invests in stocks with smaller market capitalisation, says Majeed.

“The other thing we prefer doing is investing in medium and smaller companies; there is very little research and very few foreign investors,” he says.

“The philosophy behind that idea is that if you’re going into underdeveloped markets you want to take advantage of market inefficiencies.

“If you go and invest in Emaar or NBK, where is the inefficiency? We generally look to invest in those big cap stocks when there is an event that scares people off and really pushes down prices.”

Risk focus

The vagaries of the Mena markets are something that all fund managers are mindful of and certainly not new challenges for the firm’s team, which is able to draw on a wealth of experience gained through investing in regional stocks.

“This is a volatile region; as a result we don’t need to try to get home runs each time. If we try to do that we’re going to strike out,” explains Majeed. “Our focus is on risk more than the upside. If you avoid big drawdowns, the upside takes care of itself.”

While noting its strong 10-year track record, the MENA Capital founder says the Admiral Fund has witnessed a number of different macroeconomic events and market cycles.

“When we started in March 2006, markets were expensive but had already started falling. We shorted quite a bit as a result we were up 12% versus the index, which was down by 31%,” he says.

“In 2007 we did well, not as well as the index but we were up around 30 points,” he adds. “You will find if you look at the individual years, we’re never the top performer in a bull markets but have been one of the best in bear markets. A good 10-year track record has been created.”

One of the biggest challenges for asset managers in recent years was 2008 financial crisis, where many fund managers focused on the region came unstuck.

“Then came 2008 where markets all fell apart. We didn’t really understand what was going on so we sat on 80% cash. We did not want to short because stocks were very cheap and we didn’t want to short stocks at good value,” Majeed says.

“We stayed on the sidelines. We were down by -2% in 2008 versus -51% for the index,” he adds. “Post the crisis we had the near default of Dubai and then after that we had the Arab Spring. We came through that period with minor losses of 3-4%.”

Cutting exposure

During 2015, all fund managers faced the challenge of safeguarding client investments as markets attempted to deal with the fallout from weaker oil prices.

Majeed says: “2015 was the worst year in 10 years. What happened was that we underestimated the leverage effect of the decline of commodity prices. We had 10-15% in resource stocks – mining, oil and gas – these took a beating.”

Indeed, as low commodity prices continued to take a tumble, the region’s largest oil producer – Saudi Arabia – was hit particularly hard, as it saw revenue shrink. With stocks falling, in spite of the opening up of the market to foreign investors, Majeed highlighted some of the changes to the hedge fund’s portfolio following the onset of fresh Saudi market challenges.

“With the oil price decline last year, we had a legacy of up to 20% invested in Saudi Arabia,” he says. “During February, [Saudi Arabia] started bombing Yemen; the market then was expensive and trading in the upper teens.

“We felt that with those valuations there less room for error and cut our Saudi exposure by half. Then in November we went back for another visit.

“It became clear that most people did not expect severe cuts in government spending, mainly because they expected oil prices to rebound.”

He adds: “We got the feeling that people hadn’t woken up to the new reality; we were [concerned] by that and decided to get out altogether.” ■