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QIC bets on further volatility with Pengana top-up

By Simon Mumme

Queensland Investment Corporation (QIC) has increased its allocation to Pengana Capital's global volatility hedge fund by \$US50 million to \$US200 million, incorporating the fund within two of its multi-manager products.

The Pengana fund performed well in recent months while evidence of a US economic slowdown and announcements from some major US investment banks revealing damaging subprime debt exposures undermined global markets. It posted a return of 10.04 per cent between November 1 and January 18, in comparison to its benchmark, the six-month US Treasury Bill, which yielded 4.25 per cent in the same period.

"The fund has performed within our expectations," Greg Clarke, senior portfolio manager within the implemented equities division of QIC, said. QIC, a \$70 billion institutional

manager whose clients include the Queensland Government, increased the mandate so that the volatility fund could be included in the QSuper investment trust no.1 multi-manager fund, an accumulation product. Previously, the fund only featured in the QIT 2 multi-manager fund, a defined benefit vehicle run for the Queensland Treasury.

In addition to seeding the volatility fund, QIC worked with the portfolio manager Al Wilkinson for two years to construct the vehicle. It has a segregated mandate with the manager, and views it as an "outright alpha-generator in up and down markets," Clarke said. Across QIC's broader alpha-beta separation strategies, the fund is part of the manager's global equities alpha allocation, Greg Liddell, QIC head of implemented equities, said.

The fund is designed to maintain a low correlation with equity markets while outperforming during periods of volatility. In catastrophic market condi-

tions – defined as a rapid fall of 15 per cent or more in the underlying index – the fund aims to outperform. Overall, it targets a return of 20 per cent each year over rolling three-year periods. In a strong market, however, in which the underlying index return exceeds 15 per cent, the fund will probably underperform the market return.

The recent distress in the US economy has been fortuitous for Wilkinson, who is based in Chicago. Notably, he predicted the US Federal Reserve's cut in the benchmark interest rate, by 0.75 per cent to 3.5 per cent, on January 22. His preceding trades netted a hefty sum from the inevitable market rally on the news. "He did very well out of it," Clarke said.

In implementing their volatility strategy, Wilkinson and his team trade equity index futures, options and other instruments, aiming to exploit mispricings. These mispricings are found in the differences between measurements of

the instruments' implied and historic volatilities. Wilkinson expects securities to revert to their fair value, and formulates positions in response to this view.

Among the trading techniques used are statistical arbitrage between stock exchanges and indices.

"The key component is arbitrage. As long as mispricing occurs in index options, the process can deliver significant returns," Clarke said.

The strategy draws from a universe of options derived from indices, rather than stocks, since indice-derived options are not affected by company-specific events and tend to be more liquid, readily priced and host a larger range of strike prices and expiries.

The strategy does not usually assume directional views on volatility, but it may do so during periods of extremely high or low market turbulence. It did not undertake a major directional play during January, Clarke said. ■



Sevior's FUM cut in Perpetual succession planning

By Catherine James

Perpetual Investments' head of Australian equities, John Sevior, surrendered direct responsibility for \$2 billion to senior portfolio manager Matt Williams last year, under an internal succession planning program.

Perpetual's chief investment officer, Emilio Gonzalez, dismissed any suggestion that the transfer, which happened mid-year, was a sign the 14-year veteran of the firm was about to leave.

"We certainly didn't do this in anticipation of someone leaving. The difficulty in doing this is that people immediately think John's leaving. I get that question about once a fortnight," he said.

An unconfirmed suggestion in the market is that James Packer, a friend of Sevior, has approached him to work at his family's funds manager, Ellerston Capital.

Gonzalez said the internal asset transfer – which now sees Sevior and Williams evenly split responsibility for the \$4 billion Australian Shares Fund – was "simply another step in Perpetual's succession plan" which has seen transfers between senior portfolio



John Sevior...
subject of departure rumours

managers roughly every two years for the last ten years.

"The amount [in this case] is not inconsistent with what we've done in the past. In fact we've probably made bigger moves in the past," Gonzalez said.

Perpetual has seven portfolio managers across its \$38 billion Australian equities under management, each managing varying levels of FUM in different portfolios.

Before last year's transfer, Sevior was sole portfolio manager of the Australian Share Fund, as well as the smaller concentrated equity and ethical funds.

Simultaneously, Williams' responsibility for \$6.5 billion of the flagship Industrial Share Fund has been decreased, with \$1 billion being transferred to Charlie Lanchester.

Overall, Sevior and Williams are now portfolio managers for \$7.5 billion each of Perpetual FUM.

Portfolio managers whose responsibilities remain unchanged include Amy Somes, Sean Cunningham, and John Harbord.

Cunningham oversees portions of both the industrial share and small caps funds, Somes manages some of

the industrial share fund, and Harbord directs some of the small caps fund.

Although they all draw from the same research, Perpetual began spreading portfolio management responsibilities among its analysts more than ten years ago.

"Back then, Peter Morgan [now running his own 452 Capital business] was the sole portfolio manager for the Industrial Share Fund. And we thought, how do we bring people along the curve for succession planning? The first step was to introduce John Sevior into that fund," he said.

When Morgan left in September 2002, he ran \$8 billion of Perpetual's then \$13 billion – another handful of analysts having been awarded portfolio manager responsibilities four months beforehand.

"As they develop and improve their record then we add to their FUM. Matt's been a beneficiary of that, John and Charlie have been beneficiaries of that."

Over the last few years, however, Sevior's FUM has only decreased. ■



Matt Williams...
\$7.5 billion FUM now equals Sevior's

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