Family office Thirdrock keeping its power dry

Joe Marsh | Oct 16, 2015 (2 hours ago)

The Singapore family office's CIO thinks weak market sentiment will continue for several months and is still largely avoiding alternative credit, emerging markets and commodities.

Melvyn Yeo has been hedging Thirdrock's portfolios since the start of 2015

AsianInvestor spoke to Melvyn Yeo, chief investment officer of Singapore multi-family office Thirdrock, about why he is taking a cautious allocation approach.

How is Thirdrock positioned portfolio-wise in light of potential US rate rises, heightened volatility, the continuing China slowdown and other concerns?

Since the end of 2014, we recognised there was a higher possibility of increased volatility in the markets in 2015 and possibly going into 2016. As a result, we started being more defensive by reducing net long exposures through replacement of long positions with synthetics, raising cash levels and selective hedging. We also allocated to long/short hedge funds selectively as a concerted effort to achieve lower long delta exposures.

We still hold the view that markets will continue to trade through weak economic numbers and trading sentiments in the next few months. Consequently, based on our latest quarterly investment outlook, cash continues to be close to 10% and equity around 30%, closer to the lower end of the allocation range [for the latter asset class].

As for currency exposures, we have been running long dollar exposures for some time and continue to hold this view, given that it is a safe haven during times of market volatility. The possibility of a Fed rate hike in the remaining months of 2015 will also help provide impetus for continued dollar strength, especially against EM currencies, particularly commodity-dependent FX pairs.

We don't see a recovery in commodity prices in the near term, which are closely linked to emerging markets, especially with the impending US interest rate increase.

Inflation still remains elusive globally and in some cases, such as in China, is headed downwards. With global growth risks heightened, safe-haven flows should persist and that will put a natural cap on US Treasury yields. We expect the yield curve to flatten in the short term.

In conclusion, we remain cautious and advocate keeping powder dry and waiting for financial conditions to loosen. In the meantime, look for opportunities to take advantage of skew to enter into hedges via put spreads.

So are you doing more portfolio hedging these days?

On the investment front, we see continued weakness in the markets and have been active in identifying efficient hedges. We view going long put spreads in equity markets – on the Hang Seng China Enterprises Index, for example – to capture the high skews in volatility to be the most ideal trade currently.

We have been hedging since the start of 2015 and see rolling of hedges to continue for the next few months. We have also been holding more cash.

Have you moved into alternative credit (such as private loans or peer-to-peer lending) since banks have become less active lenders?
While we have explored investments in private secured financing, trade financing loans and peer-to-peer platforms, we are not active in the space currently. Fundamentals and general market weakness will continue to persist in the short term, which is not ideal for making investments in the private space, especially as most of such alternative credits are originated in the commodity and EM sectors, where the risks are likely to be greatest.

In addition, we don't have the headcount and necessary expertise to drill down deep into each private credit transaction. If we wanted exposure to that space, we would prefer to allocate to a credit or hedge fund.

Thirdrock advises on corporate finance - what trends are you seeing in this space?
The team has been working on a number of capital raising and M&A mandates. But with valuations coming off, we anticipate that there will be less deals being done overall in coming months due to reduced risk-taking.

However, there might be some activity in the commodity space in the medium term, as some assets could be available at very reasonable valuations for investors taking a longer-term view on the complex. There may be some distressed assets worth bidding on for 20 to 30 cents on the dollar in the coming year or two.

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