BARRON'S

FUNDS

Taking the Stress Out of Distressed Debt

By Tom Sullivan Updated Sept. 25, 2010 12:01 am ET / Original Sept. 25, 2010 7:55 am ET

Hedge Fund Best-Worst-Biggest

THERE HAS BEEN AN ACCELERATION of distressed debt open for bid, and hedge-fund manager John Jacquemin, who runs Mooring Capital Fund and the Mooring Intrepid Opportunity Fund, sees good value.

After the financial meltdown of late 2008, many banks worked with borrowers to keep loans performing, even if just barely, an arrangement that Jacquemin calls "pray and delay." But now that the fear of collapse has passed, regulators are scrutinizing banks more closely, and forcing more impaired goods off their books and into the market. Unlike in the 1990s, when the Resolution Trust Corp. made troubled savings and loans sell assets quickly, the pace of new sales has been measured, which has been good for supply.

"We buy subperforming and nonperforming commercial loans...that are secured by real estate, equipment and aircraft and ships," says Jacquemin, founder of Vienna, Va.-based Mooring Financial and the 12-year-old Mooring Capital Fund. The $75 million fund has returned an average of 12.6% annually, and has never had a down year. It rose 4% in this year's first half.

Mooring Capital didn't win many loans from 2006 through 2008, because competitive bids were more aggressive. Jacquemin, to his credit, wasn't afraid to sit on cash. When he couldn't buy assets at prices that would deliver the returns he sought, he closed the fund to new investors. Now he is considering opening it again.

The $50 million Mooring Intrepid Opportunity Fund, a multi-strategy hedge fund, was down 2% in the first half, but has an impressive history. It was 100% short in 2008, netting a return of 70% at a time when many hedge funds were forced out of business. It used the same strategy in 2007, ringing up a return of 50%. Jacquemin shorts shares that he considers overvalued, and buys stocks in beaten-down sectors.

Natural gas is a sector he likes now. "Everybody hates it, but there are tremendous opportunities," he asserts. He also likes utilities, which continue to trade at a hefty discount to their historic price/earnings multiples.

If bets in these and other sectors work as expected, Jacquemin will have yet another impressive year.

MORNINGSTAR RELEASED PRELIMINARY figures last week for hedge-fund performance in August, and despite a decline in global equity markets, its Morning 1,000 Hedge Fund Index managed a gain of 0.1%, while the Morningstar MSCI Composite Hedge Fund Index rose 0.6%. The "biggest surprise" was a 3.46% gain in managed futures funds, the best showing among Morningstar's hedge-fund categories, says Nadia Papagiannis, the firm's alternative-investment strategist.

Managed futures funds are diversified momentum funds that follow price trends by investing in stock, bond, commodity and currency futures. Until last month, they hadn't performed well since 2008. In August, they got a big boost because of a sustained rise in Treasury futures, particularly futures on long-term Treasury bonds.

RYDEX SGI ANNOUNCED last week it is closing its Global 130/30 Strategy Fund (RYASX) on or about Oct. 1 "due to limited investor interest." Such funds invest 100% of their asset value in stocks, and sell short up to 30% of the portfolio's value, using the profits from short sales to reinvest in long positions.

Dan Wiener, editor of The Independent Adviser for Vanguard Investors, says that 130/30 and 120/20 funds "were a bad idea from the get-go," and that he expects more closings. He adds that they are expensive to implement and "fraught with the potential to underperform."

Through Aug. 31, the Rydex fund, with a 4.75% load and 2.16% expense ratio, was down 6.64% this year. It rose 13.23% last year but lost 38.24% in 2008 and 5.24% in 2007. The average fund in Morningstar's world-stock category is off 4.61% this year.

RENAISSANCE TECHNOLOGIES, a pioneer of computer investing, is cutting fees and adding a feeder fund to the Renaissance Institutional Equities Fund.

The $4 billion hedge fund has seen large client redemptions since mid-2007. Pensions & Investments magazine says that it obtained a recent client letter written by co-presidents Bob Mercer and Peter Brown. Based on that, the publication reports that Renaissance added "substantial capital" this year to RIEF and an affiliate fund, Renaissance Institutional Futures. Mercer and Brown took the reins this year, upon the retirement of Renaissance founder James Simons.

P&I said that Renaissance will lower fees on Jan. 1 for the fund's Series B shares, to 0.35% of assets from 0.50%. The Series A fee will drop to 1.5% from 2%, a nd Renaissance will continue to waive the performance fee, the publication wrote.

Institutional hedge funds "have to look more attractive because many of them have not fully recovered and so are in danger of losing big customers when lock-ups expire," says Ferenc Sanderson, chief operating officer of Cranwood Capital, in Cleveland.

Renaissance declined to comment.

-- *Jack Willoughby*

EQUITIES BUOYED

Equity funds inflows averaged $3.1 billion for the four weeks ended Wednesday, according to Lipper FMI. Money market funds had outflows of $5.8 billion. Taxable bond funds had inflows at a weekly rate of $3.3 billion.