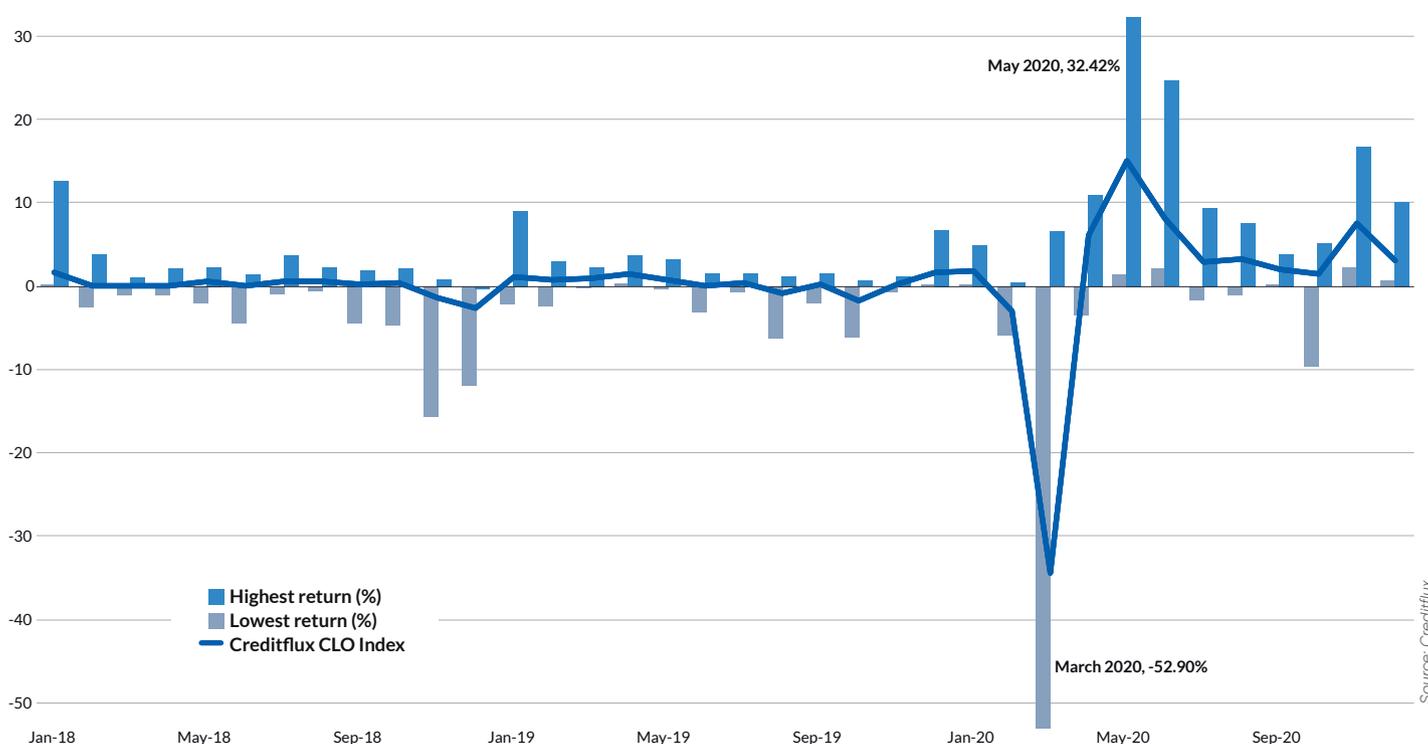


# Moving fast pays off for hedge funds

Credit hedge fund managers which were able to assess rapid fluctuations across markets and react accordingly performed best last year. Conservative positioning in Q1 also helped generate returns

## Credit hedge fund highest and lowest returns vs CLO index



by Michelle D'Souza & Robin Armitage

2020 was an up and down year in credit, and credit hedge fund managers had to move quickly to capture opportunities from the dislocations that inevitably opened up.

Early on, covid risks were not priced in, but this quickly changed as lockdowns were enforced globally. The sudden scale of the crisis — and the rapid recovery — meant that timing investments was crucial.

For CLOs, the covid crisis caused short term pain but the pace of the recovery has meant that CLOs have successfully navigated another crisis. Five funds in our top 10 invest in CLOs.

### Napier Park strategy takes top spot

Napier Park Global Capital's credit strategy, which invests across junior CLO tranches, leveraged loans and high yield, claimed the top spot in our hedge fund rankings.

Michael Micko, partner and head of European credit at Napier Park, says the general approach is to carefully underwrite individual credits and CLO structures. The firm increased hedging in February and early March, placing individual shorts in travel-related names while also increasing existing hedges through liquid credit indices. Micko says the strategy crystallised most of the gains at the peak of the dislocation.

At the same time, Micko says Napier Park

started selling single name credits and CLO mezz and equity, as markets were initially ignoring the growing early signs of covid risk, at least until liquidity dried up in early March. Raising cash early gave the manager firepower to aggressively buy dislocated CLO paper at the peak of the March

# 30.3%

Return of top performing  
Napier Park strategy in 2020

Top 30 credit hedge funds by 2020 returns			
Fund Name	Manager	Category	Return (%)
1 Napier Park European Credit Strategy	Napier Park	CLOs	30.26
2 CLO Alpha Compartment Taurus	CIS	CLOs	21.80
3 Millstreet Credit Fund	Millstreet	corporate long-short	21.38
4 Zais LevHY Fund I	Zais	credit multi-strategy	20.59
5 CIFC CLO Opportunity Fund II	CIFC	CLOs	17.39
6 Serenitas Credit Gamma Master Fund	LMCG	structured finance	16.79
7 Wasserstein Debt Opportunities Fund	Wasserstein	US high yield	16.54
8 Lupus Alpha CLO Opportunity Notes I	Lupus Alpha	CLOs	16.08
9 Olea Special Opportunities Fund	Orchard	corporate long-short	14.84
10 Flat Rock Opportunity Fund	Flat Rock	CLOs	14.50
11 Algebris Global Credit Opportunities Fund	Algebris	Ucits credit	13.99
12 Advent Global Partners UCITS Fund	Advent	Ucits credit	13.88
13 Orchard Liquid Credit Fund	Orchard	corporate long-short	13.46
14 Oxbridge Partners	Sandalwood	credit funds of funds	13.43
15 Shenkman Opportunistic Credit Fund	Shenkman	corporate distressed	12.44
16 Cheyne Convertibles Absolute Return Fund	Cheyne	Ucits credit	12.44
17 CIFC CLO Opportunity Fund III	CIFC	CLOs	12.19
18 Blueglen European Credit Fund II-24	Blueglen	credit multi-strategy	12.10
19 Makaseb Income Fund	Mashreq	emerging markets	11.95
20 Loomis Sayles Global Credit Fund	Loomis Sayles	Ucits credit	11.72
21 Sente Fund	Vibrant	CLOs	11.40
22 AG Corporate Credit Opportunities Fund	Angelo Gordon	corporate distressed	10.81
23 Carmignac Portfolio Unconstrained Credit	Carmignac	corporate long-short	10.65
24 Advent Global Partners Fund	Advent	credit multi-strategy	10.50
25 Flat Rock Core Income Fund	Flat Rock	US high yield	10.02
26 Owl Creek Credit Opportunities Fund	Owl Creek	credit multi-strategy	9.95
27 BK Opportunities Fund V	Crystal	CLOs	9.57
28 Hellebore Credit Arbitrage	Hellebore	credit multi-strategy	9.29
29 Lyxor Chenavari Credit Fund	Chenavari	Ucits credit	8.27
30 Loomis Sayles Strategic Alpha Bond Fund	Loomis Sayles	Ucits credit	8.23

sell-off. “The bid-offer widened out dramatically for all asset classes,” says Micko. “At the peak, HY was down 20-25 points on average and leveraged loans were down around 20 points. But dislocation was most pronounced in CLOs – double Bs were down 30-40 points, single Bs 50-60 points, and equity maybe 30-40 points from lower starting cash prices.”

By April, Napier Park focused on double Bs but Micko says the key was picking the top quartile quality deals, adding that prices were homogeneous across the quality range. The rebound in April and May driven by central banks and liquidity support led to the firm rotating out of double Bs and into single Bs and select CLO equity in order to capture a second leg of the dislocation.

Amit Sanghani, product managing director in the London-based team, says strategy turnover for 2020 in long positions was over 100%. “We traded over \$1.65 billion across CLO equity and mezz in Europe alone, in addition to rotating the portfolios and selling around \$600 million notional,” he says.

CLO Alpha Compartment Taurus, a CLO fund managed by CIS Asset Management,

>100%

Turnover in long positions for 2020 in Napier Park’s strategy

took second spot in our rankings with 21.80% returns. The firm focuses on niche CLO equity with an emphasis on US CLOs.

Inès Bartsch, owner and portfolio manager, says the majority of capital raised for the strategy came in Q1, meaning the firm could utilise this through the downturn.

While most CLO funds struggled with double digit losses in March, CIS was one of only two managers to achieve positive returns in the month (0.19%). “Our investments during the ramp-up period of two CLOs paid off when they closed just before coronavirus restrictions, allowing them to ramp up significant additional par,” Frankfurt-based Bartsch says. “This helped the fund keep its head above water in March and April when other CLO funds struggled.”



## The bid-offer widened out dramatically

Michael Micko  
Head of European credit  
Napier Park

The CLO market offers fund managers the ability to invest across a range of tranches, but Zais successfully applied a multi-strategy approach across the broader credit universe. Officials say they repositioned the portfolio throughout the year.

Zais LevHY Fund I locked in fourth place in the 2020 overall rankings and topped the multi-strategy credit category after returning 20.59%. The firm launched the fund at the end of 2019.

Denise Crowley, head of securitised credit at Zais, says the firm was mindful of the relatively flat credit curve and was conservative early in the year.

“As the pandemic advanced, we were able to reposition our portfolio and move further down in credit in order to capitalise on the steeper curve. The chaotic price action enabled us to take advantage of some great buys,” she says.

“We took the opportunity to buy sub-mezzanine classes, especially CLOs, CRTs and CMBS notes, and were able to pick relatively higher credit quality bonds within those sectors.”

### Distressed window may open again

Distressed debt managers raised record amounts of capital in 2020, with investors seeking to capitalise on coronavirus-related dislocation. And, after years of waiting for deployment opportunities, the crisis perhaps produced fewer distressed opportunities than many anticipated. The good news is that the high volume of liquidity from central banks and governments is keeping borrowers afloat and could produce excellent opportunities for managers to put dry powder to work in the upcoming year.

Shenkman Capital Management topped *Creditflux*’s distressed hedge fund listings in 2020 with its Shenkman Opportunistic Credit Fund, after it returned 12.44% for the year. Justin Slatky, chief investment officer at Shenkman, says key to the firm’s performance was being able to analyse credits quickly before governments drove recovery.

“During the March lows, 37% of the high yield market was distressed but by the end

of the year, less than 3% was," he says, adding this recovery took around three years in the 2008 financial crisis. He says Shenkman was able to take advantage of the firm's research database during the sell-off.

Flexibility and being active in the market also helped achieve steady returns. Shenkman had five distinct rotations through the year. "At the end of the March sell-off, we took advantage of IG names where there were forced sellers and, by April, we had rotated the book into higher quality high yield," Slatky says. By June and July, capital markets recovered and Slatky says the firm took advantage of lower dollar priced credits they thought would be repriced higher as it was clear many of these companies were not going bankrupt.

Shenkman monetised those positions by the end of summer and moved into a more



**We capitalised on the steeper curve**  
Denise Crowley  
Head of securitised credit  
Zais

defensive portfolio by the election, he says. "It was only after the election and vaccine news came out that we started to ramp up on distressed covid-related names."

### Recovery and the outlook for 2021

The historic sell-off in Q1 also signalled an opportunity for many US high yield funds as liquid instruments such as bonds traded up in the aftermath.

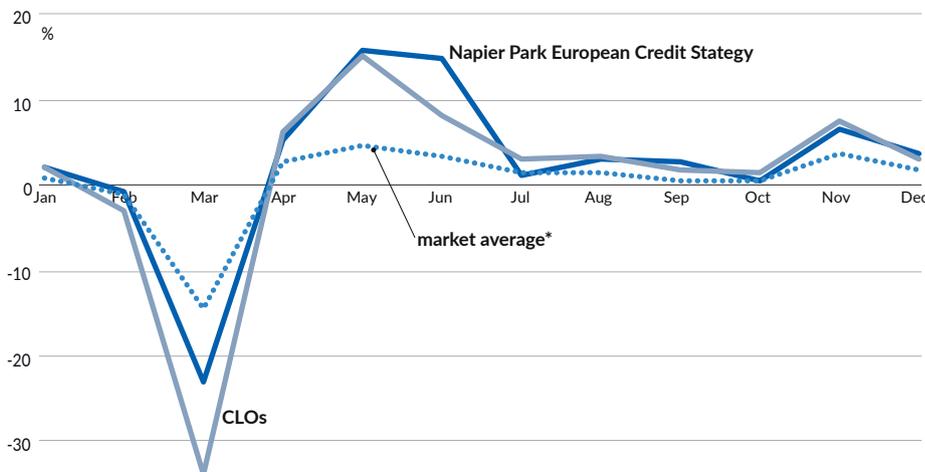
Wasserstein's Debt Opportunities Fund led the category in 2020 as it returned 16.54%. Rajay Bagaria, president and chief investment officer at Wasserstein says the firm re-underwrote its portfolio in March and focused on opportunities that could withstand a lower-for-longer environment.

"We positioned our portfolio conservatively in first-dollar debt and focused on covid-beneficiaries as well as GDP-sensitive credits that would recover with improving economic activity," he says.

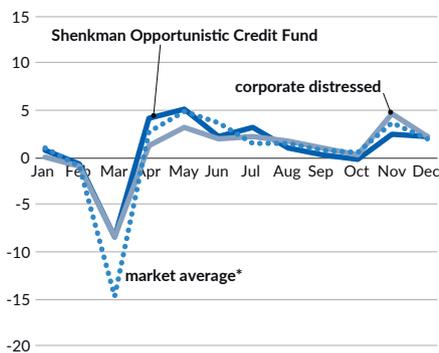
Bagaria points to Wasserstein's positions in home improvement tool manufacturers and specialty chemical producers which helped generate returns in the second half of 2020 as the economy rebounded.

Many fund managers say they are

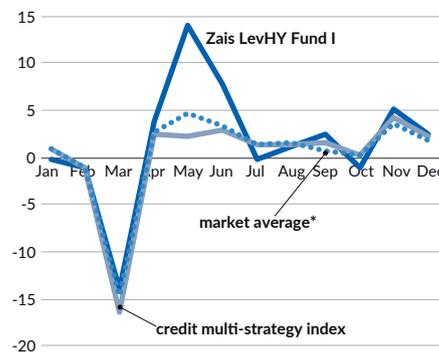
### CLOs: monthly returns



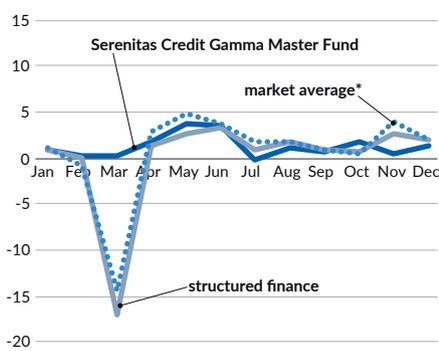
### Corporate distressed: monthly returns



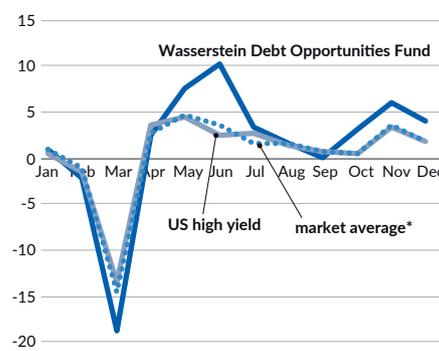
### Credit multi-strategy: monthly returns



### Structured finance: monthly returns



### US high yield: monthly returns



optimistic about the macro backdrop going into 2021, with strong growth potential in the economy and investors awash with cash, while rates remain low. However, they are mindful of the potential for inflation.

For now, though, Crowley says easy monetary policy and economic growth should remain supportive and could reveal opportunities for attractive returns in 2021.

### Methodology

- All figures are taken from monthly NAV returns net of fees.
- Full data can be found online at [creditflux.com/hedgefunds](https://creditflux.com/hedgefunds)
- Contact [robin.armitage@iongroup.com](mailto:robin.armitage@iongroup.com) to add a fund to the listing.

\* Market average figures are taken from all other funds in Creditflux database