

ALTERNATIVE MARKET BRIEFING

Voltan Frontier Markets fund to launch several sub-strategies

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The [MSCI Frontier Markets](#), today at \$484, is down 3.5% MTD, down 19% YTD, and lost almost 8% over the last 5 years. But the **Voltan Frontier Markets** fund has comfortably outperformed the index. Launched in May 2009, it invests in a universe of 60 **developing countries** that are not part of the MSCI Emerging Markets index, but that are instead early-stage markets such as Georgia, Bangladesh, Vietnam, Nigeria and Botswana. It usually has 50 to 100 positions across 15 to 20 countries, typically in listed long-only equity. The fund features in [Opalesque Solutions' Emerging Managers Database](#).

Managed by New York-based boutique [Voltan Capital Management](#), the Voltan Frontier Markets is currently most exposed to Africa, Alison Graham, Voltan's CIO, told Opalesque in a recent interview. Armed with more than 17 years of experience in emerging and frontier markets finance and the enviable ability to speak six foreign languages, she often travels around the world to check what is "on the ground."

Biggest exposures

Graham explained that the fund is currently most exposed to **Africa** because there is a very strong process of domestic capital formation with a population of people urbanising, moving into the formal job sector and contributing to pension funds. Now, in almost all of the African countries, the largest player in the domestic stock exchanges and bond markets is not foreign but domestic money, which adds some degree of stability to share prices. So the capital formation is no longer reliant on foreigners bringing money in and it is a little less exposed to foreigners pulling money out.

There is also **China** and its large impact on natural resources. "Some people are worried about China's growth slowing, about demand," she said. "But what we see on the ground is that most of the Chinese companies coming in are part of the government's 50-year plan for the development of the economy. They are not looking at what's happening to a certain commodity price today or this week; they are taking a very long strategic view of what resources they need to continue to build the economy over the next 20 or 50 years. In practice, several of the commodity companies that we own have received take-over offers by Chinese conglomerates. That way, yes, we are indirectly exposed to Chinese planning."

It is well known that, in frontier markets funds, it is not easy to hedge. Facilities for shorting or borrowing stocks often do not exist and if they do, they tend to be prohibitively expensive; and there is a lot of counter-party risk.

"Normally when we want to lower volatility, we tend to be well diversified," she added. "Given that there is such low correlation among frontier countries, the diversification works very well."

Voltan can also go into larger cash positions, which it has done in the last few months. It is a good strategy to limit volatility when the markets are bottoming out, and to be in a position to buy cheaply. The fund does not use leverage.

Losses in August partly due to sell-off, emerging markets funds

The fund incurred a small loss in August as its core holdings drifted lower with the general sell-off despite an ongoing accumulation of good news at its companies. Those declines were partially offset by trading gains and the fact that several of its holdings had become acquisition targets. Furthermore, shares the managers bought in August were up 11% to 54% by the end of the month, partially offsetting declines in the fund's banking shares across various regions.

According to Graham, when things go well in frontier markets and in the global economy, as they were up until about March of this year, a lot of mainstream emerging markets funds will start putting small amounts of capital in frontiers.

"For example they might not typically invest in Nigeria or Kenya but when things are going well and they're looking for lower valuations and higher alpha, they will start doing a bit of frontiers. When risk comes along, that is also the first money they'll withdraw. So we have seen some pretty sharp share declines in some Nigerian banks and in some of the London-listed **natural resources** companies, because they're the ones that non-specialist frontier funds have access to."

A correlation has been observed of late between developed and emerging markets, and Graham thinks that can be attributed to generally the same reasons but only to a smaller extent, as each individual country has its own story and

there is much less foreign capital around.

Today (23 Aug.2011) The MSCI World Index, which consists of 24 developed market country indices, is -10% MTD and almost -15% YTD (-4.2% in the last 5 years); and the MSCI Emerging Markets index, which consists of 21 emerging market country indices, is -14.7% MTD and -23.5% YTD (+2.8% in the last 5 years). The two indices – as well as the Frontier one - dropped a lot since yesterday. In the developed markets, major indices also fell by about 4% across the board. And [according to Bloomberg](#), emerging-market stocks tumbled, sending the benchmark index to the biggest drop in three years, on concern central banks may run out of ways to avoid another recession.

Generally speaking, correlations are found in the securities that foreigners most typically buy or most easily access; the Nigerian banks, the London or Australia-listed resource companies. But Iraq for example, a market that Voltan loves, is "really uncorrelated."

Next: new sub-strategies including one for Iraq

"We are planning to launch several sub-strategies in frontiers," she said. "As well as the flagship fund, we also might have for example an Iraq country fund, a frontier resources fund, and a couple of other strategies within the frontier geography."

The Iraqi Stock Exchange, or ISX, says its main market index has surged some 65% so far this year, making it one of the world's best-performing markets, [said WSJ.com](#). Though many doubt the accuracy of the ISX's main index, fund managers who follow the country agree that Iraqi share prices have risen about 15% in 2011—still outperforming most global peers. And Opalesque has heard that the \$20m Iraq Fund which is managed by global emerging market manager FMG was up 2% in August, returning +25% since its launch in May 2010. And Godvig Capital Management's \$20m Babylon fund, which also invests in Iraqi securities, is up 9.8% YTD.

Frontier markets

Throughout August, the most positive performance among frontier market indices were found in Venezuela, Vietnam, Jamaica, and the most negative performance were seen in Ukraine, Tanzania, Argentina, according to the Voltan's latest monthly report. YTD, the best performing indices were Iraq, Venezuela, Mongolia, and the worst were Ukraine, Kazakhstan, Georgia and Montenegro.

[According to Efficient Alpha](#), a U.S.-based research firm, of the 117 countries with independent stock markets, MSCI places 24 in the developed category and 22 within emerging status. GDP per capita in the developed markets is around \$23,000+, while the emerging markets' is \$800 to \$23,000 using purchasing power parity measures. The MSCI Frontier Markets Index includes 31 countries and selects countries through a liquidity screen and minimum size requirements, had a market capitalization of \$228bn across approximately 371 constituents as of 2010.

The Voltan Frontier Markets fund can be found in [Opalesque Solutions' Emerging Managers Database](#), which is available to Opalesque' subscribers. You can subscribe here: [Source](#).