FINANCIAL TIMES

December 21, 2012 7:01 pm

Finance: The great Greek gamble

By Sam Jones

Dan Loeb's $500m windfall from a bet on Greece marked a striking return to high-stakes bets

Poison pen: Mr Loeb sprang to prominence with his acerbic but publicly published letters attacking boards and executives

In Quentin Tarantino's film *Reservoir Dogs*, Mr Pink gets away with the diamonds. His co-conspirators are left bloodied and dying.

When he was starting out as a hedge fund manager in the 1990s, Daniel Seth Loeb used to stalk investing chat rooms and message boards with an online persona: Mr Pink.

Mr Loeb has always evaded questions on the nom de plume, but it stuck as a nickname. And he appears to be living up to it.

This week the 51-year-old, now one of Wall Street's most successful investors, scooped up a $500m windfall for his clients in a bond buyback deal with the Greek government.

Dozens of hedge funds have been burnt trying to play the eurozone crisis but Mr Loeb's Third

Point is not one of them.

The trade in Greek government bonds, which saw a handful of canny investors double their money, has been the single most successful hedge fund bet in two years – a period during which most hedge fund managers have struggled to navigate rocky markets, grinding out meagre returns.

Beset by nervous clients, hedge funds have thrown off the kind of high-stakes, directional betting that once made the industry famous. These days, George Soros would not be able to convince his risk manager to place the $1bn bet against sterling that saw him "break the Bank of England" on Black Wednesday in 1992.

Where managers have been willing to be audacious, they have been stung. John Paulson, the man who shorted the US housing market in 2007 and made billions doing so, has lost hundreds of millions this year shorting German bonds.

Betting on Greece has been a rare exception. Those who put their chips on Athens came out winners.

"In retrospect, it seems so obvious," says Hans Humes, the founder of Greylock Capital, one of the very first hedge funds to invest in Greek bonds. "But we were mocked at the time. I got trashed in June when I said it was exactly the time to buy Greek bonds ... I was out there saying that Greece was a no brainer. But people are wired to be scared."

Greylock's clients have gained a 30 per cent return on their capital this year – six times what the average hedge fund has made.

Third Point came in later, though its trade was even larger.

For those familiar with Mr Loeb's style, it came as little surprise. Like most hedge fund managers, Mr Loeb lost money in 2008 but Greece has restored his reputation, built over two decades, for big, bold bets.

Mr Loeb first sprang to prominence with acid critiques of corporate boards and executives in publicly published letters. Among his put-downs of choice: CEOs as CVDs (chief value destroyers); hereditary shareholders as members of "The Lucky Sperm Club"; and supine board members as country-club frequenting "socialites". He gained further notoriety this year by staging a coup against the chief executive of Yahoo, whom he accused of embellishing his curriculum vitae.

Although Mr Loeb has dominated headlines, Third Point was far from alone in its interest in Greece. A group of 15 other hedge fund analysts visited Athens on September 20 – part of a whi wo-da ow o d by the London brokerage Exotix.

and cars choked the streets of Athens. In Syntagma Square, metro workers were protesting at spending cuts, holding aloft a scaffold with an effigy swinging from a noose.

On their agenda: meetings with some of Greece's biggest corporations, the debt management agency and leading people in the government, including two of the cabinet's most powerful figures: Kostis Hatzidakis, the minister of development, and Christos Staikouras, the deputy finance minister.

After those meetings, many of the analysts returned to the trading floors of London and New York with a contrarian conclusion: Greece – a virtual pariah state, victim of a huge and continuing drain of international capital – was a major investment opportunity.

Truth be told, in the late summer, Athens' ministries and banks were frantic with the comings and goings of hedge fund managers.

The rightwing coalition government's policy has been to give high-level access to investors of all kinds, including hedge funds, for the first time – a marked change from the previous government, where many traders were demonised as evil speculators.

Third Point had been among the earliest funds to visit Athens, beginning its hunt for Greek bonds in July and August.

The firm had been carefully eyeing Greece for some time but analysts were intrigued by how low the bonds were trading after their restructuring in March.

Amid concerns of a Greek exit from the eurozone, prices for the new "strip" of bonds – a basket of securities with mixed maturities investors had received in exchange for their old bonds in the restructuring – had continued to sink.

It seemed absurd. "I have never seen a sovereign debt restructuring situation where the new debt trades lower than the old debt," says Julian Adams, CEO of emerging market hedge fund Adelante Asset Management, which also made big profits from the bonds. "It will go down in restructuring history as being an absolutely extreme occurrence."

For Third Point, it was access to government that proved critical. The impression it gained was that Antonis Samaras, the prime minister, was putting in place a plan that was exactly like Portugal's, and no one was talking about the possibility of leaving the eurozone.

"Sitting outside the country, part of the problem is that you get a slightly jaundiced view," says George Zois, head of Greek equities and capital markets at the brokerage Exotix. "On the ground, you ry diff ew. Yo erstand the granularity of the situation.

government is much more engaged," he says.

The government agrees. "It matters that we get out a message of co-operation," one official says.

. . .

When Third Point began hunting for Greek bonds in the summer, there was no shortage of sellers. European banks, particularly French ones, were desperate to unload their holdings at rock-bottom prices. In the end, the fund acquired "strip" bonds for an average price of just 17 cents on the euro.

Slowly but surely, Greek bond prices began to rise as interest from other hedge funds picked up.

The government edged them along, with increasingly loud hints about the possibility of a debt buyback, an untested solution being pushed hard by hedge funds in their discussions with ministers.

As momentum built for the buyback as a solution, other, bigger hedge fund beasts felt confident enough to join in. Among them was Moore Capital, one of the world's most established, but secretive, "macro" hedge funds. Moore bought a large position in the autumn, according to traders.

On December 5, hedge funds heard the news they wanted. On the sidelines of an investment conference organised by the Hellenic American chamber of commerce, Mr Samaras met a small group of them.

The government had just unveiled plans for a debt buyback. The government was to spend up to €10bn to buy its own debt at a steep discount. The question was: at what price?

Hedge funds initially worried that the price would be too low – but they made clear to Mr Samaras that, if it was, they would not participate. They were assured that there would be a minimum price in the auction of about 30 cents on the euro.

When the deal was done, the government bought back bonds for an average price of just under 34 cents on the euro, enough for Third Point to have doubled its money.

The fund tendered the bulk of its position – but not all of it. So confident is Third Point now of a Greek recovery, that it has maintained a sizeable chunk of bonds.

People close to the funds say that their trips to Greece did not give them insider information but only core details on how to appraise the investment climate.

Anal Third elieve t could be a further 40 per cent rally from current values if the executive at Dromeus Capital, a Swiss-based hedge fund that aims to profit from a Greek recovery.

The real question, perhaps, is why so many other hedge funds missed it. “People in this industry spend more time trying to sound intelligent rather than making money,” says Greylock’s Mr Humes.

“Being bearish about things is the way they do that.”

Additional reporting by Kerin Hope in Athens