

HEDGE

INDUSTRY • LUXURY • OPINION

ISSN 1757-7361
0470
771757 738027
£5 9
ISSUE.27



The Rule of Lourie

Weathering the Storm

From navigating the Thames in a James Bond boat to founding one of Europe's most successful credit hedge funds, CEO Jonathan Lourie has become adept at steering his ship, says **SAFI THIND**

J-LO IS ON the sofa opposite telling me about his company's first structured credit investment and the market dislocations that drive the fund's investment strategy. I find myself considering asking for a booty shake – but come to my senses when he starts telling me about the Asian crisis and the time he worked as Asher Edelman's broker in the corporate raider's heyday. The J-Lo in question is not, of course, the generously proportioned Latina pop megastar, but someone equally famous, albeit in the more parochial world of hedge funds: Jonathan Lourie, the founder and CEO of Cheyne Capital Management.

I meet him in an elegant St James's townhouse nestled in a leafy corner of Green Park. The offices were designed by Samuel Wyatt, inventor of the 'sympathetic hinge', which enables both leaves of a door to open simultaneously. Its old Piccadilly façade belies a dynamically remodelled interior by none other than Sir Norman Foster.

Lourie's own office preserves some of that old-world regency atmosphere, though understated, with oak table, wooden panels and large comfortable sofas. It's nice to hear that in this very room Sir Winston Churchill convinced Baron Beaverbrook – a bumptious, result-getting Canadian whose wartime aims are said to have been principally of the fiscal variety – to advance dutifully with the Empire's WWII Spitfire-building programme. The history of the room is perhaps an apt metaphor for the twin values of North American drive and old English charm that Lourie embodies.

“What I found appealing was the growth in the globalisation of the equity business and I found early on that my niche was to take a cross-asset class approach”

It certainly resonates in his background. Lourie was schooled in Switzerland and then majored in comparative literature at New Hampshire's Ivy League college Dartmouth, graduating *summa cum laude*. He went on to work at LF Rothschild, Unterberg, Towbin, and then in 1985 at Morgan Stanley as a US institutional equity salesman covering continental Europe.

Along the way he was broker for Edelman, one of the muses for Gordon Gekko of 1987's *Wall Street*, and adopted his global perspective to investing.

“I rapidly realised that what I found intellectually appealing was the growth in the globalisation of the equity business,” he says. “I found early on that my niche was to take a cross-asset class approach, and in the 1980s convertible bonds and Japanese warrants became a particular penchant.”

‘Penchant’ is a quite mild description of a talent that has brought him great success. Lourie started running an internal hedge fund at Morgan Stanley in the early 1990s and began to identify market dislocations. Convertible bonds were a particular area of focus and certainly had huge reward potential. He cites, for example, a 20-year convertible that LF Rothschild issued for Compaq with a 10% coupon that would have made more than 50 times the money at which it was bought: “This was exactly the risk/return profile that appealed to me.”

At around this time he discovered his first major market dislocation, sparked by private equity firm Kohlberg Kravis Roberts & Co's takeover of tobacco and food behemoth RJR Nabisco, at that time the biggest buyout in history, and a deal memorably recalled in the book *Barbarians at the Gate: The Fall of RJR Nabisco*.

Lourie brought in fellow Dartmouth alumnus Stuart Fiertz to help him study the implications of the credit dislocation brought about by the downgrade of RJR, beginning a relationship that was to span three decades and lead to the founding of Cheyne itself. Having caught the inflection

point from its lows in the corporate debt markets in the early 1990s, they then rode a two and half year trend of ever-tightening spreads and exited it in late 1992. At that point they reoriented themselves into the Asian convertibles business and soon became the single biggest European player in that market. The investment lasted into the late 1990s, in a time that saw Asian markets melting down by as much as 80% to 90% from peak to trough, and again, many trades were done with a long-convertible, short-equity structure, thus preserving clients' capital in this tumultuous period.

There is a certain beauty to playing in credit rather than equities in situations like the one described above, argues Lourie.

“If you do a terminal analysis and get it right, then you will get your money back in a recovery scenario with bonds,” he says. “It's a binary situation. In equities you can do well but you can't guarantee the outcome or how long it will take.”

The Asian crisis was the second time that Lourie had consolidated his efforts around a big dislocation, and again proved to be a success when the markets recovered and went through a dramatic upswing.

It was also to be the genesis of Cheyne. By 1999, Lourie had convinced Morgan Stanley that if the firm's clients could put in \$50m of equity and the firm matched it with \$100m, they could get non-recourse financing for seven years on a portfolio of “busted” Asian convertibles. The name of the CBO was, indeed, Cheyne.

That name came from quite original roots, as Lourie tells it.

“Living on Cheyne Walk in the 1990s I found myself with a problem – how to get to work in Canary Wharf which, at the time, had no Jubilee line,” he says. “At first I settled on the Thames riverboats, but after the company running these went bust in 1995, I did the next best thing – buy a powerboat.”

The Fairey Huntsman is another classic of English design, in the mould of St ▶

PHOTOGRAPHS BY DAVID HARRISON



“ Post-2008 investors want to see proper institutional-type infrastructure. It was a profoundly humbling experience but also the sort of experience that can only make you stronger ”

► James’s and the Spitfire, that have followed Lourie around through the years. It is the same boat that was used in James Bond’s *From Russia With Love*, he says. The vessel – which he dubs the Rolls-Royce of boats – was christened *Cheyne*, a name that eventually found its way to the fund also.

Lourie says he often found himself in tricky nautical situations reminiscent of Bond himself, riding the unpredictable waves of the Thames on his way to work.

“The Thames is a dangerous river. Normally if you’re on a cigarette boat [a rum-runner] you’d be kicked off – but because this boat was such a classic the watermen loved it. It was precarious, however; one time our engine broke down and we looked up to see, at a distance of five to six hundred yards, an approaching tug pulling two barges, heading straight for us. I owe my life to the Ogilvy & Mather launch which was miraculously nearby and managed to pull us to the side.”

Lourie also cut a lot of deals on his boat launch, since whenever there was a strike or traffic on the roads, every managing director wanted to ride with him.

Having ridden the low finance seas, in 2000 Lourie transitioned \$500m (net) to *Cheyne*, taking the internal fund clients, “in an amicable move”, from Morgan Stanley and setting up with eight staff to focus initially on convertible bonds and equities. Growth has been outstanding ever since. The fund now boasts \$6.8bn in assets under management, making it easily one of the biggest hedge fund managers in Europe. Its five strategies run across credit, real estate debt, event driven, convertible bonds and equities.

The expertise across asset classes has been telling in the company’s performance. In aggregate, *Cheyne* has only had one down year since launch: 2008, when, owing



to its focus on credit and convertible bond-related products, a wave of redemption requests accelerated by Lehman Brothers’ bankruptcy led to a significant drawdown.

Cheyne was, of course, one of the main players in the structured credit market. The experience in convertibles, which are essentially structured hybrids, meant it was quite natural for the firm to bring in John Weiss and David Peacock, who both headed up credit derivatives businesses at Goldman Sachs, to run a structured credit portfolio that eventually resulted in the largest structured credit transaction ever launched – *Cheyne CDO 1*, which returned a net annualised 29% from its launch in June 2002 to its call date in November 2005.

The structured credit crisis of 2007 was unforeseeable in its severity, says Lourie. It originated in the mass-involvement of several parties – including banks, ratings agencies, regulators and the consumers who took out mortgages they had no intention of paying back. Hedge funds indeed got clobbered, yet had little to do with the crisis at its origin. Certainly, however, the financial crisis has taught the industry some keen lessons.

“Post-2008 investors want to see proper institutional-type infrastructure,” Lourie says. “It was a profoundly humbling experience but also the sort of experience that can only make you stronger. There’s a great deal more humility in the industry ►



► because it's been much tougher, so we are definitely more grateful for the gains that have been made back since then."

Cheyne downsized to 122 people from 248 at its peak, and back up to 155 now. The scar tissue left from the crisis will remain for a while yet, says Lourie, citing one of the first men he met when he entered the financial world, an industry veteran named Dudley Jaffe, who even in his nineties remembered vividly the awful effects of the Great Depression.

That the company made it out of the crisis with only one bad year is down to its stability; partners who run Cheyne's funds have been at the company for an average 10 years or more. At the same time, however, this stability has to be achieved with a certain amount of Darwinian selection.

"You have to be fairly forceful if people

don't step up to the mark. As an industry we are highly paid – and certainly we have to align ourselves with investors' interests."

Lourie says his workplace mantra has been to develop as collegiate an atmosphere as possible in the office. "Part of our DNA, also, is that if we are going to work with high-quality people we want to give as

“ You have to be fairly forceful if people don't step up to the mark. As an industry we are highly paid – and certainly we have to align ourselves with investors' interests ”

good a work environment as possible to our staff and partners," he says. I get this sense when I am given a tour of the office – which has a genuinely fresh and open feel to it – and again when I am escorted around the corner to Lourie's favourite restaurant, Sake No Hana, by his partner Stuart Fiertz, the yin to Lourie's yang. With his keen analytical mind, Fiertz professes he is less involved on the external business side of the fund; he leaves it to his counterpart. They seem to complement one another, as successful business partners inevitably do.

I find myself wondering how big the fund could grow: "It's all about matching assets to capacity," explains Lourie. Given that, from where he sits now, he says he feels Cheyne could reach \$8bn or \$9bn in the next few years, without diluting returns.

It's a big journey from a little riverboat. **H**