The Interview – Faris Abdulrazzaq, Menasa Capital Management: “Despite the recent events in Egypt and Tunisia, we remain bullish on prospects for 2011”

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Faris Abdulrazzaq (pictured), senior portfolio manager at Menasa Capital Management, which specialises in identifying investment opportunities in the rapidly-growing public markets of the Middle East, North Africa and South Asia, says that with a buoyant oil price driving current account surpluses, Gulf governments are poised to spend more than ever on building infrastructure and creating jobs.

GFM: What is the background to your company and funds?

FA: Menasa Capital Management was founded in 2010 by a specialist active investment management team formerly of Abraaj Capital, the largest alternative asset manager by size in the Middle East, North Africa and South Asia with USD6.6bn in funds under management.

We aim to capitalise on our extensive experience in the field of delivering consistent risk-adjusted returns while preserving our clients’ capital. We offer both traditional and alternative strategy investment management for sophisticated and professional investors through a number of products as well as segregated accounts.

Menasa Capital Management currently has USD350m in assets under management and is regulated by the Dubai Financial Services Authority. The firm is the investment manager for the Menasa Opportunities Fund I, a multi-strategy emerging/frontier markets fund focused on investments within the Middle East, North Africa and South Asia.

Before joining Menasa Capital Management I was a portfolio manager at Majid Al Futtaim Asset Management responsible for the Middle East and North Africa region. I joined the business in 2003 as the second member of the Middle East and North Africa team and over six years helped transform the family office of Majid Al Futtaim into a successful third-party asset management business with a superior track record in regional equities through developing and applying a disciplined investment approach.

Previously I was with EFG-Hermes in Cairo since 1997 where he spent the initial 3 years building his equity experience in the brokerage department advising both local and regional institutions on their investment strategy. I subsequently became head of investor relations for the company after it went public. Earlier I spent two years as a consultant at Arthur Andersen Egypt working on projects with local public and private institutions.

Other key members of the Menasa Capital Management team include chief executive Ahmed Nashaat, previously the Middle East regional director for the Permal Group; chief financial and operating officer and head of business and product development Sameer Bhandari, who was formerly and executive director and vice-president in the global manager strategies group at Goldman Sachs Asset Management in New York; and senior research analysts Nabeel Qadir Bastaki, previously of BMO Capital Markets, the investment banking arm of Bank of Montreal, and Tammam El Barbir, formerly with Morgan Stanley and EFG-Hermes in Dubai.

GFM: Who are your key service providers?

FA: Our prime brokers are Goldman Sachs International and Deutsche Bank, our law firms are Simmons & Simmons in the UK and Dubai and Maples and Calder in the Cayman Islands, and our auditor is KPMG in Dublin and Cayman.

GFM: What is the profile of your client base?

FA: We focus on international and regional institutional as well as high net worth investors. Our current split is 85 per cent institutional and 15 per cent private client investors.

GFM: What is your investment process?

FA: We primarily use an intensive fundamental approach to select securities. We typically seek companies with near-medium term observable catalysts for a change in asset prices. We also seek companies whose businesses may be impacted positively or negatively by thematic, long-term fundamental factors.

Typical companies that we invest in are those that demonstrate financial strength, high returns on invested capital, high quality earnings, ability to generate free cash flows, higher quality of management in terms of experience and trustworthiness, solid business prospects in terms of products and competitive moats, and attractive valuations.

Companies that we avoid, or alternatively sell short, characteristically demonstrate low returns on invested capital, poor quality of earnings, an inability to generate sufficient free cash flows, poor executive management or corporate governance, fundamentally flawed business models and unattractive valuations.

We also make investments in special situations within the investment restriction parameters of the strategy.

GFM: How do you generate ideas for your funds?

FA: Investment ideas are identified through a combination of top-down and bottom-up views of the investment team. Once an investment idea is identified and meets investment criteria and valuation and liquidity risk screens, we conduct in-depth fundamentals analysis, including industry analysis, financial modelling, management meetings and conference calls, sell-side analyst or industry consultant meetings and valuation analysis.

Once the analysis is complete, the idea is presented to the investment team, where there is an open debate about the investment thesis and recommendation among all team members. If the outcome of the meeting is positive and the investment team agrees with the thesis, the investment idea is retained on the idea list with a formal recommendation to go long or short.

A trading position will then be initiated by the portfolio manager based on asset allocation, sizing, market view, and technical factors.

GFM: What is your approach to managing risk?

FA: Our approach to managing risk is active and resourced independently from the investment team. We actively monitor risk limits and enforce risk guidelines. Our risk manager has academic credentials and experience with globally-recognised hedge funds.

All risk management activities are carried out in accordance with global best practice, including segregation of functions and independent lines for reporting. Our risk manager has a direct line to discuss any potential risk issues with the group's independent board of directors.

GFM: How has your recent performance compared with your expectations and track record?

FA: In 2010 our fund returned 4.7 per cent net of fees. Naturally managing a hedge fund is very different from a long-only strategy, as we are more focused on risk-adjusted returns and keeping volatility low. Our annualised volatility for the year stood at 8.5 per cent, compared with 13.6 per cent for our benchmark index.

In April 2010, when the European debt crisis began to escalate, we decided to buy protection and hedge the portfolio from aggressive downward pressure, which was a successful strategy until markets reversed in August. Ben Bernanke's speech at the time helped stimulate momentum in global equity markets, and as we maintained a cautious approach in shifting gears to a more bullish stance, we lagged the uptrend in the markets, resulting in an underperformance for the year.

GFM: What opportunities are you looking at right now?

FA: Despite the recent events in Egypt and Tunisia we remain bullish on the region's prospects for 2011. Quantitative easing in the US in an attempt to create jobs will bring back liquidity and remain supportive to commodity prices worldwide. With a buoyant oil price driving current account surpluses, Gulf Co-operation Council governments are poised to spend more than ever on building infrastructure and creating jobs.

From a top down view we are bullish on Saudi Arabia and Qatar, while we are keeping our eye on the United Arab Emirates, as specific names seem to have priced in all the downside while illustrating some signs of improved business conditions.

While Egypt progresses toward democracy we believe the economy will suffer in the short term, at least until the presidential elections. The recent revolution will place immediate pressure on the armed forces to improve the public sector's working and living conditions. We have already witnessed salary increases across various sectors and would expect further stimulus packages.

On the other hand tourism revenue and foreign direct investment are set to decline, which will certainly be painful for the balance of payments, especially in light of high oil and commodity prices. Outside the Middle East and North Africa, we continue to evaluate bottom-up stories in Turkey and Pakistan on a selective basis.

GFM: What events do you expect to see in your sector in the coming year?

FA: The events in Tunisia and Egypt have given the Arab citizen on the street a voice and the strength to make that voice heard. We believe there will be further pressure on other heads of state in the region, but a similar upheaval to that in Egypt is less likely in wealthier Gulf Co-operation Council economies that are able to stimulate growth and create jobs. If anything, most countries will be more pro-active in their investment programmes and infrastructure spending as they cannot afford social unrest.

GFM: How will these developments affect your own portfolio?

FA: This will create an opportunity from a portfolio perspective to position ourselves in the markets and sectors that stand to benefit from government expenditure and stimulus packages. This is a theme that has been discussed for a while in the region, but many governments were cautious on implementation coming out of the 2008 financial crisis. Now, after Egypt and Tunisia, it is clear they can wait no longer.

GFM: How do you assess investors' current expectations?

FA: Generally, investors in the current environment would like a portfolio that delivers risk-adjusted returns over a market cycle – today they are quite focused on managing downside risk.

GFM: What differentiates you from other managers in your sector?

FA: I have been managing regional portfolios for institutions for more than seven years in the region and have one of the longest track records at the current time. I have had solid experience in running portfolios using both quantitative and fundamental bottom-up techniques.

Very few hedge funds in the region have a long/short strategy. The main reason is that shorting can be complex in the region and has to be done on a synthetic basis. Consequently, there are few funds that can manage volatility effectively and deliver alpha to investors.

We are also committed to best practices at every level, including fund management, investor communication and disclosure, fund structure and organisation, portfolio administration and control, regulation and oversight, as well as risk management.

The depth of our investment team and our Menasa Capital Management/Abraaj network give us access to management of most companies in the region, which facilitates our analysis and stock selection process.

GFM: How do you view the environment for fundraising over the coming 12 months?

FA: While the region does have geopolitical concerns in the near term following the uprisings in Egypt, Tunisia and Libya, we view such moves towards democratisation as a long-term positive step for the region's capital markets. Our view is that investors should start to position themselves in the region today in vehicles that can identify macro as well as bottom-up fundamental opportunities but have the ability to manage downside risks if needed through alternative or non-traditional investment approaches.

GFM: Do you have any firm plans for further product launches?

FA: We are in process of launching a dedicated long/short regional equity fund on a European hedge fund platform.

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