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## **36 South Plans Inflation Hedge Fund After 236% Black Swan Gain**

By Netty Ismail



March 6 (Bloomberg) -- 36 South Investment Managers Ltd., a New Zealand-based hedge fund firm set up by derivatives traders, will close its Black Swan Fund after it gained 236 percent in the last 12 months and start a fund that wagers on inflation.

36 South will move to London from Auckland in May to boost its assets under management as investors have overlooked the manager because of its location, said **Jerry Haworth**, co-founder of the firm that manages more than \$40 million.

"It's easier to trade from London than in New Zealand," Haworth, 49, said in a telephone interview from Auckland. Europe has "a really concentrated pool of potential investors; it makes more sense if you're serious about raising money to go to London."

The \$1.4 trillion hedge-fund industry shrank by more than 20 percent last year and averaged losses of about 19 percent, the worst year on record, according to Chicago-based Hedge Fund Research Inc., as the credit crunch led to investor withdrawals and funds shutting down because they couldn't raise new money.

36 South buys long-dated options it considers cheap in global currency, fixed-income, equities and commodity markets, betting that rare and unforeseen events would generate unusually large profits. It doesn't invest in options with less than a year to maturity.

Options, contracts to buy or sell shares by a certain date at a specific price, "serve as an early warning system for an impending crisis," Haworth said. "It's an amazingly lucrative niche and there are very few players in it."

### **Making Money**

The Black Swan Fund profited from bets on interest-rate cuts in Australia and New Zealand, and the purchase of put options on major stocks around the world, including the so-called BRIC nations of Brazil, Russia, India and China, Haworth

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said. The manager also bought put options on commodities. Put options gives the buyer the right, though not the obligation, to sell a specific quantity of a security by a set date.

The **MSCI World Index** tumbled 42 percent last year, its biggest drop, while the Reuters/Jefferies CRB Index of 19 raw materials lost 36 percent, the worst rout in 50 years.

"What can I say? They made a great deal of money," said **Peter Douglas**, principal at Singapore-based hedge-fund consulting firm GFIA Pte, which runs a unit that invests in hedge funds. "We were invested in Black Swan, which made our clients happy. It was conceived and executed as a disaster hedge, and clearly last year was full of disasters."

### Black Swan

36 South plans to close its Black Swan Fund within the next two months and return the money to investors as options are now "very expensive" and are unlikely to produce "significant returns," Haworth said.

"The market has gone from under-pricing risk to over-pricing it," he said. "On a risk-reward point of view, I can't put my hand on my heart to investors and say 'listen, this is a good investment to be buying options at this juncture,' because I don't believe it."

The fund, named after a theory developed by **Nassim Nicholas Taleb**, a professor of risk engineering at New York University, sought to protect client investments against "black swans," those highly improbable events that can cause havoc. Taleb wrote a book called "Black Swan: The Impact of the Highly Improbable," published in May 2007.

36 South will start a fund in the second half of the year that will return "well over 100 percent" if there's "significant" inflation worldwide, Haworth said. Billionaire Warren Buffett said in his annual **letter** to Berkshire Hathaway Inc. shareholders Feb. 28 that U.S. bailouts will likely lead to "an onslaught of inflation".

### Raising Funds

"It is not the predominant risk now but we feel in a year or two's time it certainly could be," Haworth said. "If everybody goes cash and the governments are expanding the money supply at the rate they seem to be, the problem in the future might be that there'll be like a Montana land-grab for assets because of inflation."

36 South's relocation to London coincides with plans to grow its flagship **Kohinoor Series Two Fund** to \$500 million, from \$11 million, said Haworth, who has been trading derivatives for more than 20 years. The fund gained 73 percent in 2008.

Haworth founded 36 South, named after the latitude where Auckland is situated, with **Richard Hollington** in 2001.

Haworth, the former head of equity derivatives at Johannesburg-based Investec Ltd., co-founded **Peregrine Holdings Ltd.**, a South African money manager and stockbroker, in 1996. Zimbabwean-born Haworth moved to Auckland from

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Johannesburg in 1998, after Peregrine's initial public offering in South Africa.

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