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Paris firm Lutetia steers steady course with UCITS-compliant event/merger arb strategy

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Lutetia Patrimoine, the Europe and North America-focused event-driven fund managed by Paris-based Lutetia Capital, has just recently passed the two-year mark and has produced a positive annualised return since launch in a difficult period for event-driven managers.

The \$100 million fund is one of only a few event-driven strategies to have been structured under UCITS III regulations, and co-founder Fabrice Seiman believes the firm is in a good position to capitalise on investor interest in event-driven strategies.

Lutetia Patrimoine is focused entirely on opportunities in mergers and acquisitions. The portfolio comprises two sub-strategies managed in separate books: a highly qualitative classic merger arbitrage strategy and a fully hedged pre-event book.

The fund launched at the tail end of 2009 and went on to return 5.59% in 2010. It made a modest loss of 0.34% last year, for the most part preserving capital in an uneven year for event-driven funds that saw a median loss of 2.11% for the euro-denominated EuroHedge event-driven index, and a loss of 6.15% for dollar funds.

Seiman believes his fund has answered what he calls a “key debate” when it comes to UCITS versus offshore. “We’ve demonstrated that you can outperform the offshore funds significantly in a UCITS format,” he says, pointing out that the firm only runs a UCITS version and has not amended an existing offshore fund to fit the structure.

Seiman manages the fund alongside fellow Lutetia co-founder Jean-François Comte. Comte began his career as a lawyer before spending a decade with Lazard in New York, where he specialised in M&A and worked on transactions totalling more than \$50 billion in value.

Seiman has an equally rounded and diverse background. He was diplomatic advisor to former French treasury secretary Jean-François Copé, and later joined private equity firm PAI Partners. “I have a double background in private equity and politics, and that political insight is more than necessary, I believe, to understand the markets – especially at the moment,” he says.

Both managers draw on their backgrounds to run the merger-arb book. Seiman describes their approach as highly analytical – he points out that “in M&A, all the data is publicly available” – and risk analysis plays a particularly important role.



Jean-François Comte and Fabrice Seiman

“We spend a lot of time considering the four main types of risk that would mean a deal won’t go through,” says Seiman. Political risk and legal risk are two, alongside financial risk and the risk of delay.

Seiman and Comte have a relatively straightforward approach to managing the pre-event book. “We focus on the sectors in which we think there will be the biggest volume of activity in the next few months, selecting the most attractive potential targets in these sectors. We stay away from market rumours,” says Seiman. At present, they are staying out of financials and are focusing on opportunities in healthcare, energy and technology. “The big US tech firms have a lot of cash on their balance sheets; they’ll do some M&A for sure,” he says.

Lutetia runs models to simulate possible acquisition activity on a continuous basis, pairing potential acquirers with likely targets and identifying possible takeover scenarios that would be worth playing via the pre-event book.

The fund as a whole is quite diversified, holding around 50 positions at any given time. “We try to actively trade, and we have a wide variety of position sizes – and the size of each position can vary over its lifecycle,” says Seiman.

A position in the merger-arb book will typically play out in three to six months, from announcement of a deal through to closing. The more speculative nature of the pre-event book means it holds more long-term positions, generally with a lifecycle of between six months and a year.

If nothing happens during that time, the managers will look at whether they should simply close the position and move on to another opportunity. “We also try to remember that a takeover itself is not the whole thing – more than anything else, we’re here to make money,” says Seiman. “So if we make 25% on a position before the takeover happens, we will look at the risk/reward and if the downside outweighs the upside, we may exit before a deal actually happens.”

The diversified nature of the portfolio, and a tendency to lock in profits rather than hold out for a bigger but riskier return, are representative of the fund’s ethos and approach to money management. “It goes with our target return of 6-8% and our low volatility, which is always a maximum of 4-5%,” says Seiman. “We’re a UCITS fund, and we’re also intended for large institutions and private banks.”

Paris might not have been the obvious choice of location for the firm, as Seiman and Comte have spent a great deal of time in Switzerland and the US respectively. But it is proving to be a shrewd move, at least if investor feedback is anything to go by.

“A lot of investors love the fact that we’re UCITS, and in particular that we are a French-regulated UCITS,” says Seiman. “If there’s one thing the French are good at, it’s regulation – they’re probably the world champion of regulation. And that’s great from an investor’s point of view.”

Following requests from investors, the firm has long-term plans to launch a more aggressive version of the strategy. Seiman and Comte have not decided whether this would mean a leveraged version, a more concentrated portfolio, or a bolder investment process that leaves out much of the hedging employed by the existing fund.

In the meantime, Lutetia Patrimoine has plenty of growth potential. “We usually say we have a \$1 billion capacity on this fund and strategy, but in truth we could probably go further,” says Seiman. “We’ve run the fund since day one as if we had \$1 billion, and our core positions are large caps – names like Motorola and Goodrich.” The vast majority of positions are in companies with a market cap above \$500 million, he adds.

“I think we’re entering a sweet spot,” says Seiman of the firm’s prospects for attracting capital. “We launched in 2009 and it’s now 2012. We’re regulated, we’ve reached \$100 million, and we protected capital in 2011. I think all of these factors will mean we’re on the radar now for investors.”