AVI Global claims success in stopping SoftBank ‘Nasdaq whale’ trades after tech tilt

By **Jeremy Gordon** / 14 Dec, 2020 at 17:21

AVI Global (AGT), the £879m global investment trust specialising in buying undervalued holding companies, has claimed a hand in getting top holding **SoftBank Group (9984.T)** to abandon the controversial derivatives trading strategy that saw it dubbed the 'Nasdaq whale'.

Fund manager Asset Value Investors, or AVI, has become increasingly focused on Japanese companies, launching **AVI Japan Opportunity** (AJOT) two years ago to leverage the ongoing corporate shake-up among asset-rich but undervalued firms in Japan. But AGT's decision to take a stake in SoftBank in early 2020 was as much about tilting its portfolio more towards tech, which provided some protection during the coronavirus pandemic.

SoftBank's shares have roared to a 20-year high during 2020, helped by its major stake in Chinese internet giant **Alibaba (BABA.N)** and large-scale asset sales and share buybacks under pressure from activist hedge fund Elliott, whose involvement first convinced AVI to take a stake. Blow-ups for private investments in the group's Vision Fund, in particular WeWork's spiral into turmoil last year, seemed to be fading into the background.

But investors were delivered a reminder of SoftBank's erratic tendencies under mercurial founder Masayoshi Son (pictured) when it was revealed in early September that the group was buying huge volumes of derivatives, which analysts said had stoked the surge in US tech companies this summer. Trading in call options helped inflate the prices of Nasdaq-listed names, as counterparties bought the companies' shares to limit their own downside exposure.

The revelation wiped more than 10% off Softbank's shares, although they have since returned to their highest level since the company listed in early 2000, just before the bursting of the dot-com bubble. In November, the group reported a $2.7bn (£2bn) loss on derivatives trading. The unit responsible for that activity also allowed Son to have a personal stake in trades, raising serious concerns over corporate governance.

'Of late there have been some shenanigans going on. Call them what you like. There have been some things that have raised eyebrows,' said AVI's Joe Bauernfreund.

AVI's CEO and chief investment officer acknowledged that this kind of activity – with Son presiding over the company in a way that raised questions over whose interests were being served – is part of why the group 'deserves to trade at a discount' to the value of its investments.

Bauernfreund said they had engaged with SoftBank on the derivatives trading issue, speaking against the activity, and that management had responded positively.

Bloomberg reported at the beginning of this month that SoftBank will unwind its derivatives positions and discontinue the strategy, although will continue taking direct stakes in companies like **Facebook (FB.O)** and **Amazon (AMZN.O)**.

'Very interestingly, despite the fact that Elliott are much larger investors than we are, we have actually had quite an extensive dialogue with management of SoftBank and they have listened. We weren't alone in articulating those arguments, but certainly we did articulate those arguments and they were listened to,' said Bauernfreund (pictured).

That issue aside, the SoftBank investment has been a success for AVI, which at one point in March added to the position at under ¥3,000. The shares passed ¥8,000 last week.

Bauernfreund also hailed recent success at **Fujitec (6406.T)**, AJOT's biggest position and the largest of AGT's largest holdings in the 'Japanese special situations' bucket.

AVI released a presentation in May laying out the cases for changes at the elevator company. Fujitec responded by publishing a strategic review earlier this month, which the manager said addressed 'many of the issues that were raised in our report'. Share price performance has also been strong, with the stock up well over 20% in the last year following a strong rally since March.

Tech 'tilt'

The move to invest in the likes of SoftBank also means that the 'look-through' exposure to underlying companies across AVI Global's portfolio looks very different to a year ago, with a greater weighting to internet and 'growth' stocks. That tilt was partly opportunistic, as valuations fell to more attractive levels during the crash, but also reflected a desire to increase exposure to areas like e-commerce which should be more resilient in lockdown environments

Alibaba, mostly via Softbank, was a 5.7% position and top holding at the end of September, according to annual results. Fellow Chinese tech titan **Tencent (0700.HK)** was the next biggest underlying holding. Luxury goods company **LVMH (LVMH.PA)** was another big position, via **Christian Dior (DIOR.PA)**.

German online fashion retailer **Zalando (ZALG.DE)** was another of the top 10 exposures, through Swedish holding company **Kinnveik (KINVb.ST)**. The trust added heavily to Kinnveik during the crash as its shares slipped to a large discount. It was the largest contributor to returns in AGT's just-ended financial year.

As Kinnveik's shares have moved to a premium, above the value of its underlying holdings, the position became more of a risk, leading them to take some profits, said Bauernfreund.

However, the trust did not want to lose exposure to Zalando and so has bought into the company directly. Bauernfreund said the move was a new strategy for the trust, reflecting increasing attention on the prospects for underlying holdings rather than discount hunting.

A similar theme has played out following research into song royalties related to **Sony (6758.T)**, another big holding. AGT has bought into **Hipgnosis Songs** (SONG) as well as **Round Hill Music** (RHM) in its recent flotation. Bauernfreund said he expected the values of both portfolios to increase substantially over time, based on wider market trends, something already starting to be seen in Hipgnosis' recent results.

Value names rally

AGT also maintained exposure to more cyclical stocks, which have benefited from the rotation towards 'value' stocks sparked by November's flurry of coronavirus vaccine news. Names which strongly rallied included **Jardine Strategic (JSH.SI)**, a conglomerate exposed to the Hong Kong economy, and **Exor (EXOR.MI)**, which has exposure to the automobile industry through **Ferrari (RACE.N)** and **Fiat Chrysler (FCHA.MI)**.

Bauernfreund said the Japanese smaller companies bucket was the one part of the global trust's portfolio which was 'yet to do its thing for us', in terms of participating in the value recovery. The manager said he believed this sector remained a strong play on the global economic recovery, with many firms seeing a strong earnings bounce driven by the recovery in China that is yet to be recognised by the market.

In October, AVI Global also started building a bucket of 'Covid recovery plays', mostly asset-backed companies in the UK, now amounting to around 4% of the portfolio. This includes stakes in property companies often with office exposure, including **Derwent** (DLN), **British Land** (BLND) and **Secure Income Reit** (SIR), as well as buying Primark-owner **Associated British Foods** (ABF).

Shareholders in AVI Global, which maintains low exposure to the US, have seen a 12.8% return over the last year, versus a 16.5% rise for the MSCI ACWI index. Over the past five years, the 108% return for shareholders beats the index's 99%.

Over the last year, total returns have been flat for AJOT's shareholders as the MSCI Japan Smaller Companies index has risen 2%.