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GFM Focus Investing

Capturing Option-Like Returns with Event Driven Investing

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Capturing Option-Like Returns with *Event Driven* Investing

Anand Batepati, Portfolio Manager

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ANAND BATEPATI

Co-founder of GFM. Portfolio manager and co-investor alongside clients. Over 20 years of experience in New York, London, Hong Kong. Two finance master's degrees.

- Long / short fundamental investor with a concentrated portfolio.
- Designed quant investment strategies that managed several billion dollars at Bear Stearns.
- Launched a Fund of Hedge Funds in London.
- Co-founded and sold a tech startup in the US. Became a startup investor after that.

Mix of fundamental and quantitative skills. Held roles in value investing, derivatives trading, startups, private equity and accounting.

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#1: Some investing concepts that we live
by.

WHAT IS INVESTING? WHAT IS TRADING?

Investing is about looking to the asset itself to generate wealth for you; from the income it generates and from its market value appreciation (even if you never sell the asset). Investing does not depend upon you to buy and sell the asset to make money. E.g.: owning a farm for a lifetime.

Trading is about buying something today in the hope that you can sell it to someone else at a higher price. It is the buying and selling that you look to generate wealth, not the asset itself. E.g.: daytrading some stock.

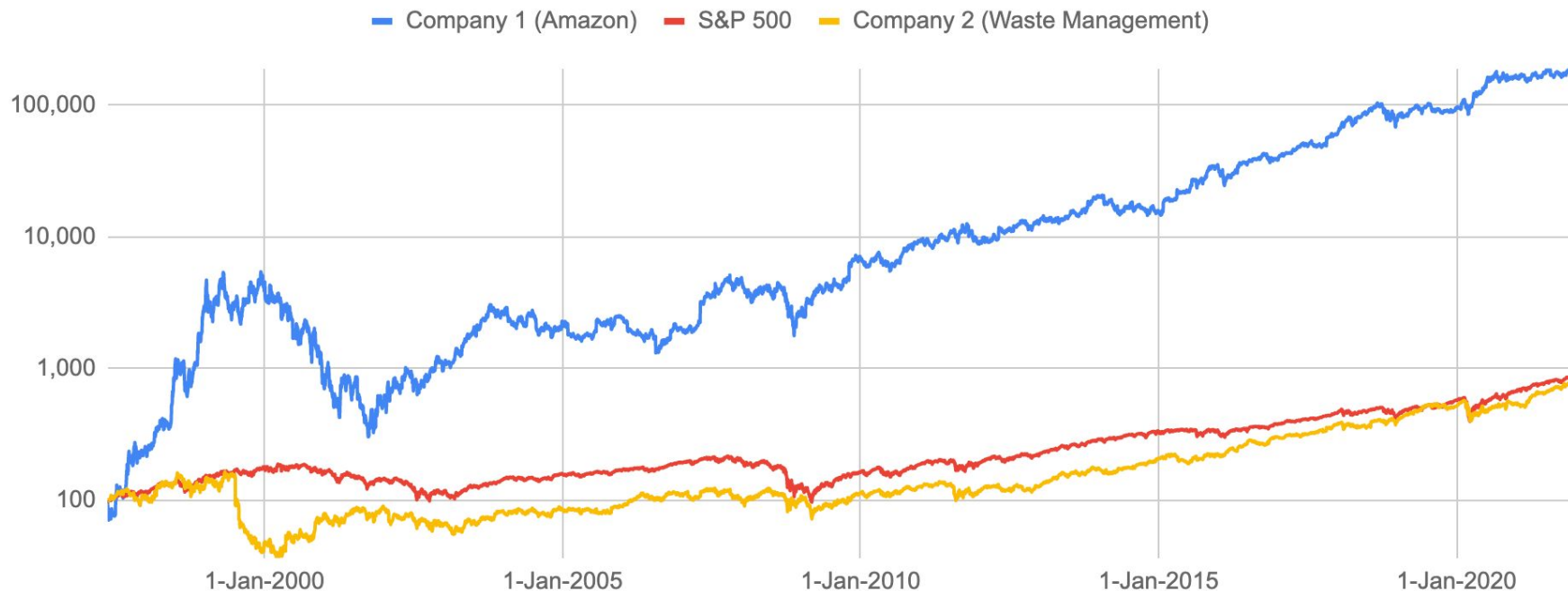
VOLATILITY IS NOT RISK. PERMANENT LOSS OF CAPITAL IS RISK



Volatility can cause **permanent loss of capital** if you are margin leveraged but not if you are unleveraged. This is your choice, this risk is not from the asset, but from you adding leverage to your exposure.

VOLATILITY IS NOT RISK. PERMANENT LOSS OF CAPITAL IS RISK (2)

Growth of USD 100k in 25 Years



Source: Yahoo Finance



Note: Not a trading recommendation. Past performance is not indicative of future results.

PERMANENT LOSS OF CAPITAL LOOKS LIKE THIS

Growth of EUR 100k in 19 years



Source: Yahoo Finance



Note: Not a trading recommendation. Past performance is not indicative of future results.

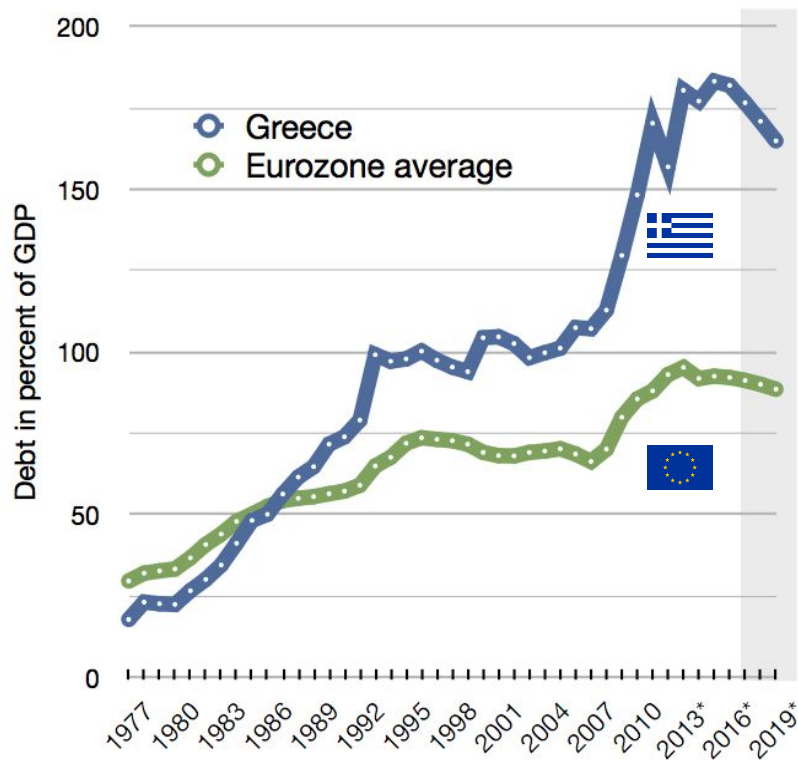
WHAT IS EVENT DRIVEN INVESTING? WHAT ARE CATALYSTS?

Event Driven Investing is about locating an investment opportunity where the future investing result will be overwhelmingly driven from company specific events, not so much from macro trends or market events.

Catalysts are specific, independently verifiable and observable developments that will step change the realization of the investment thesis. These can be financial, operational or competitive dynamics affecting a company.

#2: Case Study: Hellenic Telecom (HTO:AT) in 2012

BACKDROP: THE GREEK CRISIS OF 2012



Source: Eurostat

* Source: Ernst & Young using data from Oxford Economics

Greek sovereign debt was around 50% of GDP from 1909 to 2008. From 2008 to 2011 it jumped to 180% of GDP - a fatal level pushing the country towards a debt repayment default.

By 2012, Greece was about to default on its bonds, the money mainly borrowed from EU and institutional investors. A default would cripple the country for decades.

The govt. did what it could with austerity, tax hikes and layoffs resulting in severe financial stress for its citizens. Chaos descended: unemployment, social unrest, snap elections, and intense bailout negotiations with the EU and IMF marked the day.

Financial markets were in a panic, volatility had exploded. Access to capital was closed shut to any company or individual linked to Greece.

'Grexit' worries fuel nation's vicious circle

By Teo Kermeliotis, for CNN
Updated 1752 GMT (0152 HKT) June 15, 2012

CNN Money Markets Economy Companies Tech

EUROPE'S DEBT CRISIS

Greece downgraded deeper into junk

By Chris Isidore @CNNMoney May 17, 2012: 3:20 PM ET



Fitch downgrades Greek govt austerity coalition doesn't win

NEW YORK (CNNMoney) — Greece was downgraded deeper into junk status by Fitch Ratings on Monday.

Fitch Ratings cited the caretaker government's elections next month as a key factor in the downgrade.

What Happens if Greece Doesn't Get a Bailout?

EUROPE

What Happens if Greece Doesn't Get a Bailout?

By Michael Schuman | Feb. 16, 2012

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After the Greek Parliament on Sunday passed yet another package of austerity measures demanded by its euro-zone neighbors — this one worth \$4.4 billion — the path seemed clear to finalizing a long-delayed, second bailout of the country totaling \$170 billion. Well, it turns out the Greek vote wasn't enough to satisfy skeptical euro-zone leaders. Instead of inking down the bailout details, European finance ministries have reopened the entire plan to bail out Greece. A debate is now raging among euro-zone members over whether or not a second bailout makes any sense at all. The basic problem apparently lies there is a growing belief in some northern members — such as Germany and Finland — that Greece's politicians never be capable of implementing reforms, whatever promises are made so a new bailout would end up being a waste of money. German Finance Minister Wolfgang Schäuble publicly questioned the commitment of Greece's leaders to reform after an upcoming election.

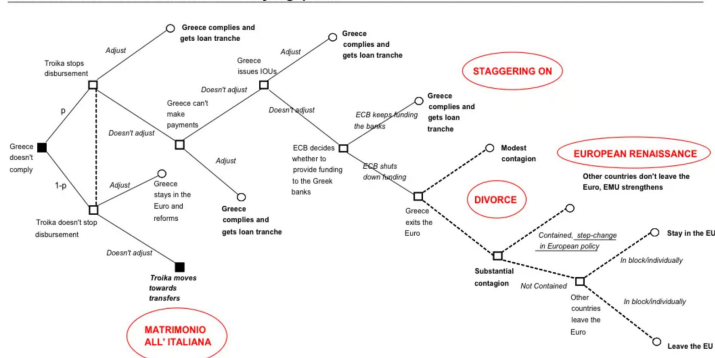
his latest twist in the debt crisis will resolve itself is unclear. Greek leaders are scrambling to find yet more budget cuts to appease their euro-

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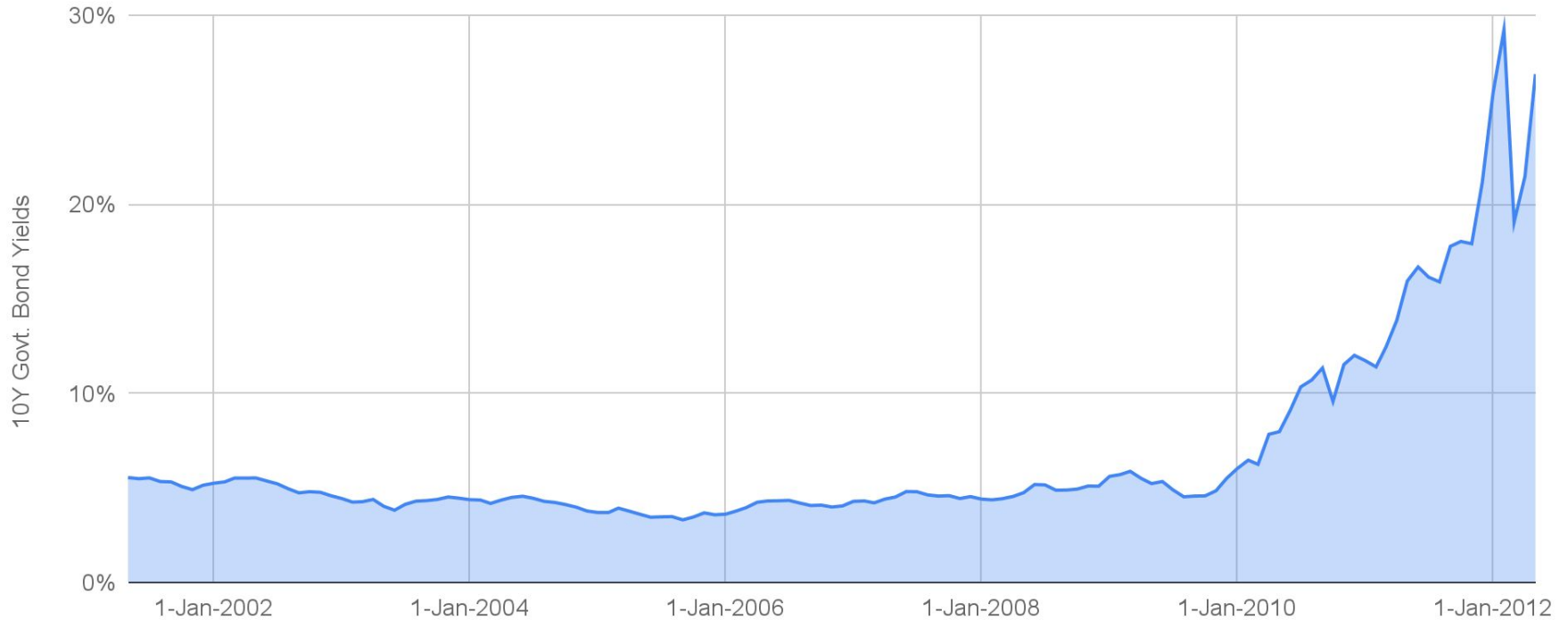
A Possible Evolution of Events — The Key Signposts



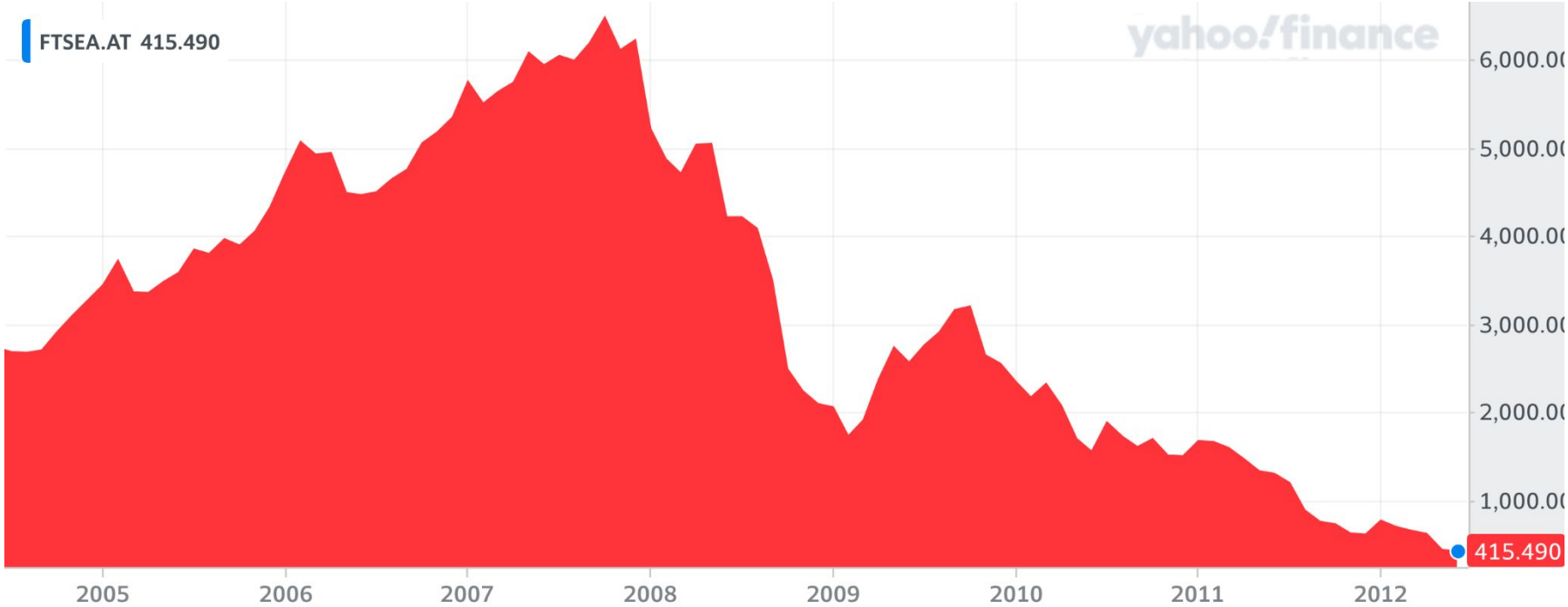
As Greeks Head to Polls Again, a Fear That No One Will Win

71

BOND MARKETS WERE ANTICIPATING A GREEK SOVEREIGN DEFAULT



GREEK STOCKS WERE DOWN 95% FROM THEIR 2007 PEAK



Source: Yahoo Finance (FTSE ATHEX Market Index)



Note: Not a trading recommendation. Past performance is not indicative of future results.

HELLENIC TELECOM'S STOCK WAS TRADING AS IF IT WILL GO BANKRUPT IN A FEW DAYS



Market cap in June 2012 was below EUR 700 million.

Stock was down 87% from its 2011 peak.

Down 95% from its 2007 peak.

Its business was the same as in the previous 5 years. Fixed line telecom, mobile, broadband internet services.

WAS HELLENIC TELECOM OVERLEVERAGED?

EUR millions, as of December 2011	
Net Debt	3,865
EBITDA	1,732
Net Debt/EBITDA Leverage Multiple	2.23

HTO was not overleveraged by bond market standards.

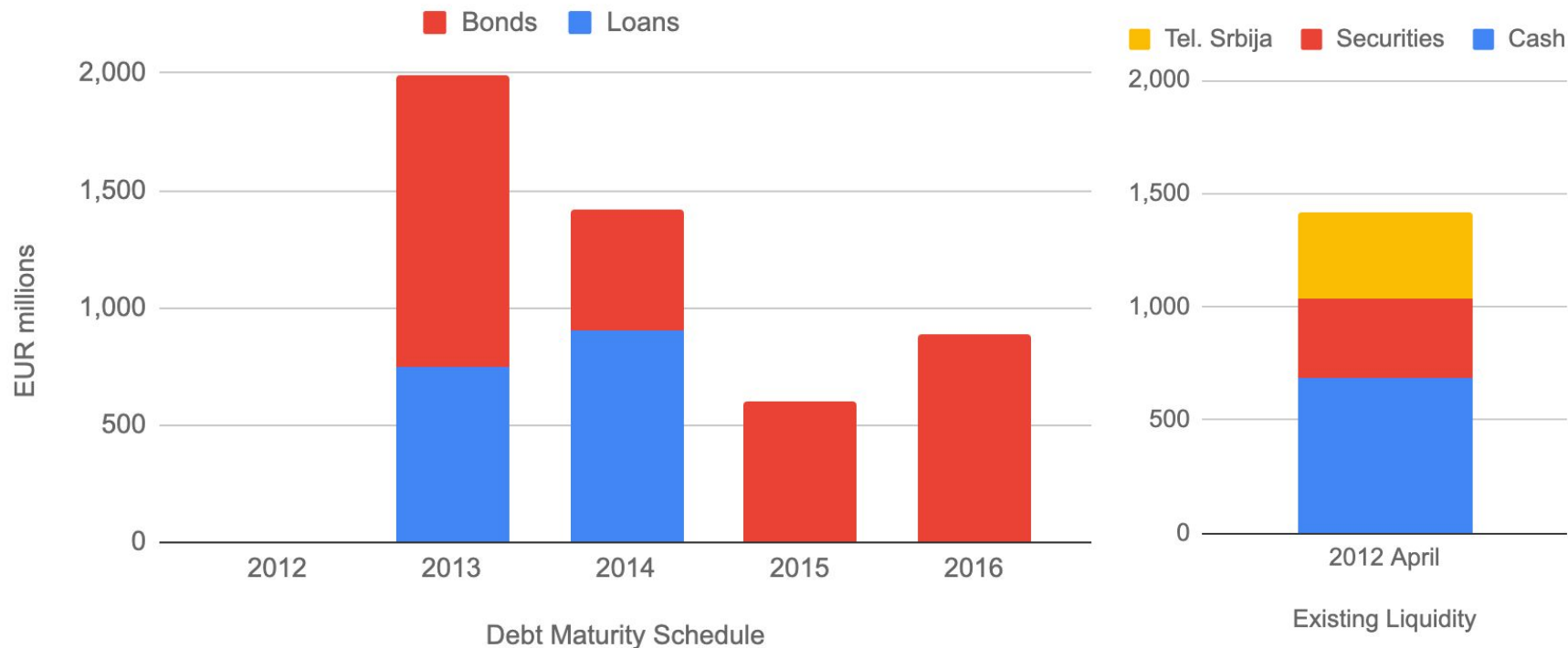
Fitch Ratings calculated HTO's Leverage at 2.54x in April 2012.

Generally, a leverage ratio around 2.5x would translate into an investment grade credit ranking by S&P, Moody's and Fitch.

However, HTO was downgraded into junk bonds status as Greece's sovereign credit rating was getting downgraded.

HTO, by the Fitch's admission, was in sound financial health and business performance was improving.

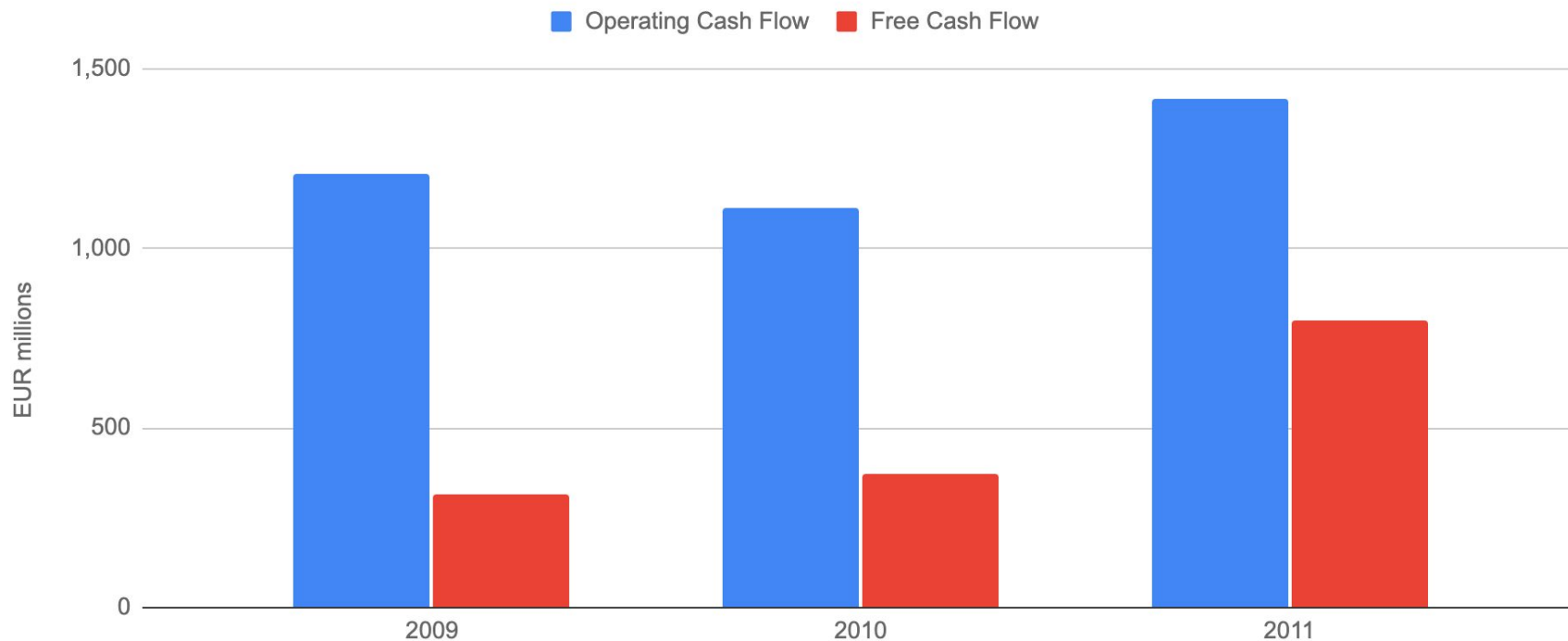
WAS HTO HAVING A CASH CRUNCH IN 2012 THAT COULD FORCE BANKRUPTCY?



WHERE CAN IT GET EUR 600 MILLION FROM?

1. **Cash generated by the business**
2. Sale of other assets (like 20% stake sale in Telekom Srbija in 2011 for EUR 397 million)
3. Debt refinancing
4. Financial support from Deutsche Telekom
5. Monetization of Real Estate assets valued at EUR 1.3 billion in 2011

PAST CASH GENERATION SUGGESTED THAT THE BUSINESS CAN GENERATE SOME OR ALL OF THE EUR 600 MILLION REQUIRED



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HELLENIC TELECOM HAD BUSINESSES IN GREECE, ROMANIA, BULGARIA AND ALBANIA

Greece

- OTE Globe (100% owned)
- Cosmote 100%
- OTESat-Maritel 100%
- OTE estate 100%
- OTE plus 100%
- OTE academy 100%
- CosmoOne 62%

Revenues: 71%
EBITDA: 74%

Romania

- RomTelecom 54%
- Cosmote 100%
- Zapp 100%

Revenues: 29% of EUR 5,038 million in 2011
EBITDA: 26% of EUR 1,732 million in 2011

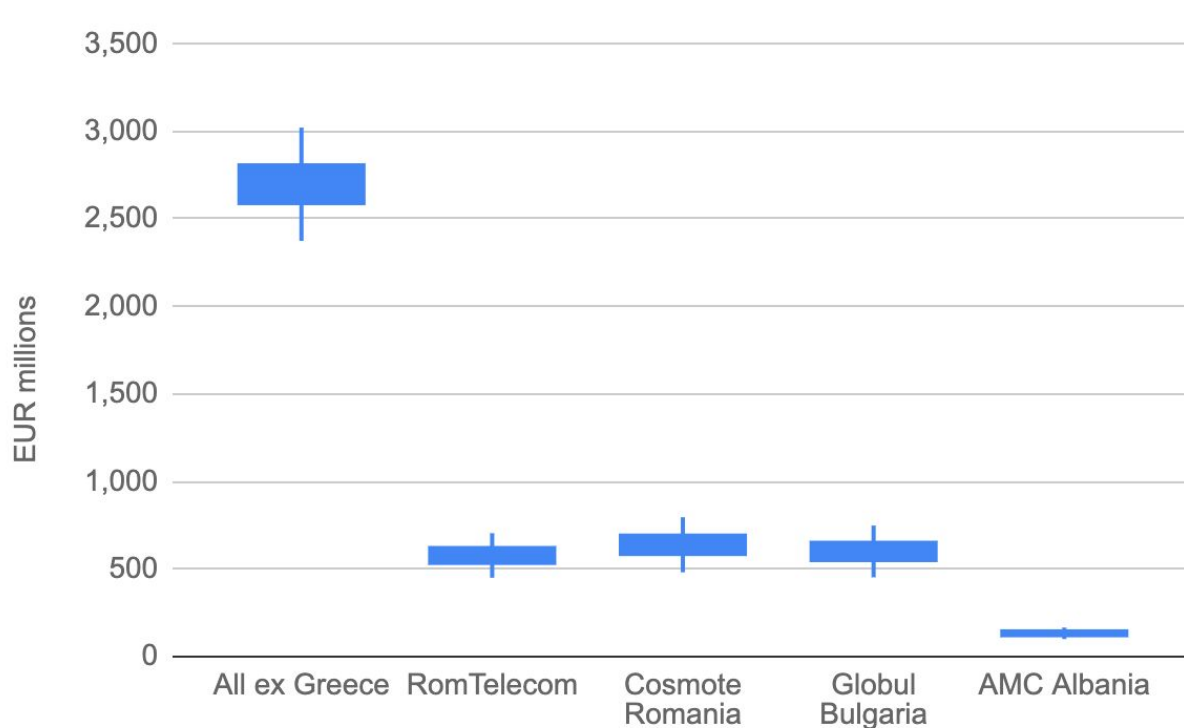
Bulgaria

- Globul 100%
- Germanos 100%

Albania

- AMC 100%

ROUGH ENTERPRISE VALUATION OF HTO'S FOREIGN SUBSIDIARIES



Tel Srbija Sale in EUR millions	
Sale Price	397
HTO Stake	20%
Enterprise Value	1,985
Revenues	890
EBITDA	356
EV / Revenues	2.2 x
EV / EBITDA	5.6 x

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HELLENIC TELECOM WAS A BLUE CHIP, STATE BACKED, IN A “CRITICAL BUSINESS” WITH FULL ACCESS TO BANK LENDING AND BOND MARKETS DURING NORMAL TIMES

In 2012, the business was performing well, despite the economic crisis

With regard to our other financial achievements, it should be noted that the first quarter of 2012 was for OTE the best of the past two years, as we managed to slow down our revenue decline rate, which fell by only 3.6%, we maintained our EBITDA at 35.4% and increased our adjusted net profit by 52%.

Without the crisis, HTO would have had many options: refinancing of maturing debt, new bank loans, issuing bonds, issuing equity, investment from a financial or strategic institution, etc.

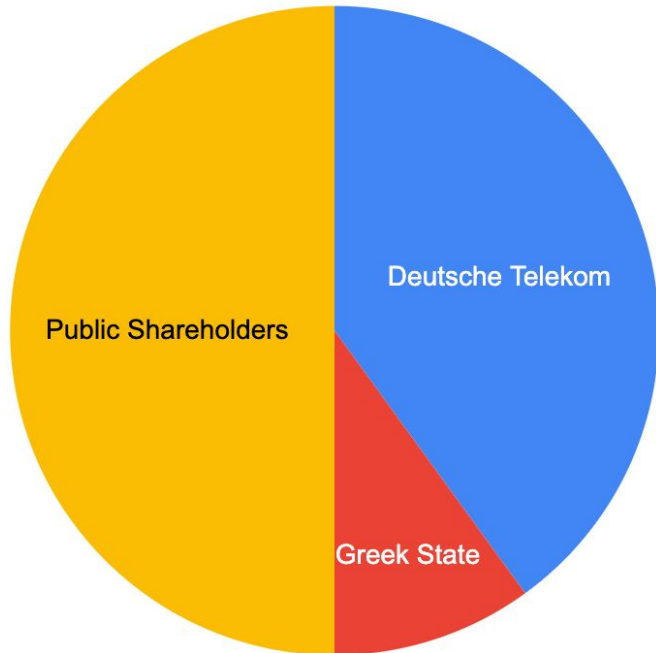
Progress was also made on the front of debt reduction and refinancing. In February 2011, we secured the refinancing of a maturing loan, raising Euro 900 million from the market under satisfactory conditions. In April 2011, we raised Euro 500 million from the European Bond markets. And at the end of the year we sold our 20% stake in Telecom Serbia, netting a gain of about Euro 400 million. These transactions and the strong cash flows we have generated have enabled us to cut Group adjusted net debt by about Euro 1 billion, or more than 22%, to reach less than Euro 3.3 billion. Today, our net cash position amounts to approximately Euro 1.4 billion, covering our refinancing needs for 2012.

WHERE CAN IT GET EUR 600 MILLION FROM?

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DEUTSCHE TELEKOM HAD SAID IN EFFECT THAT HTO WILL NOT DEFAULT!

Hellenic Telecom Shareholding in 2012



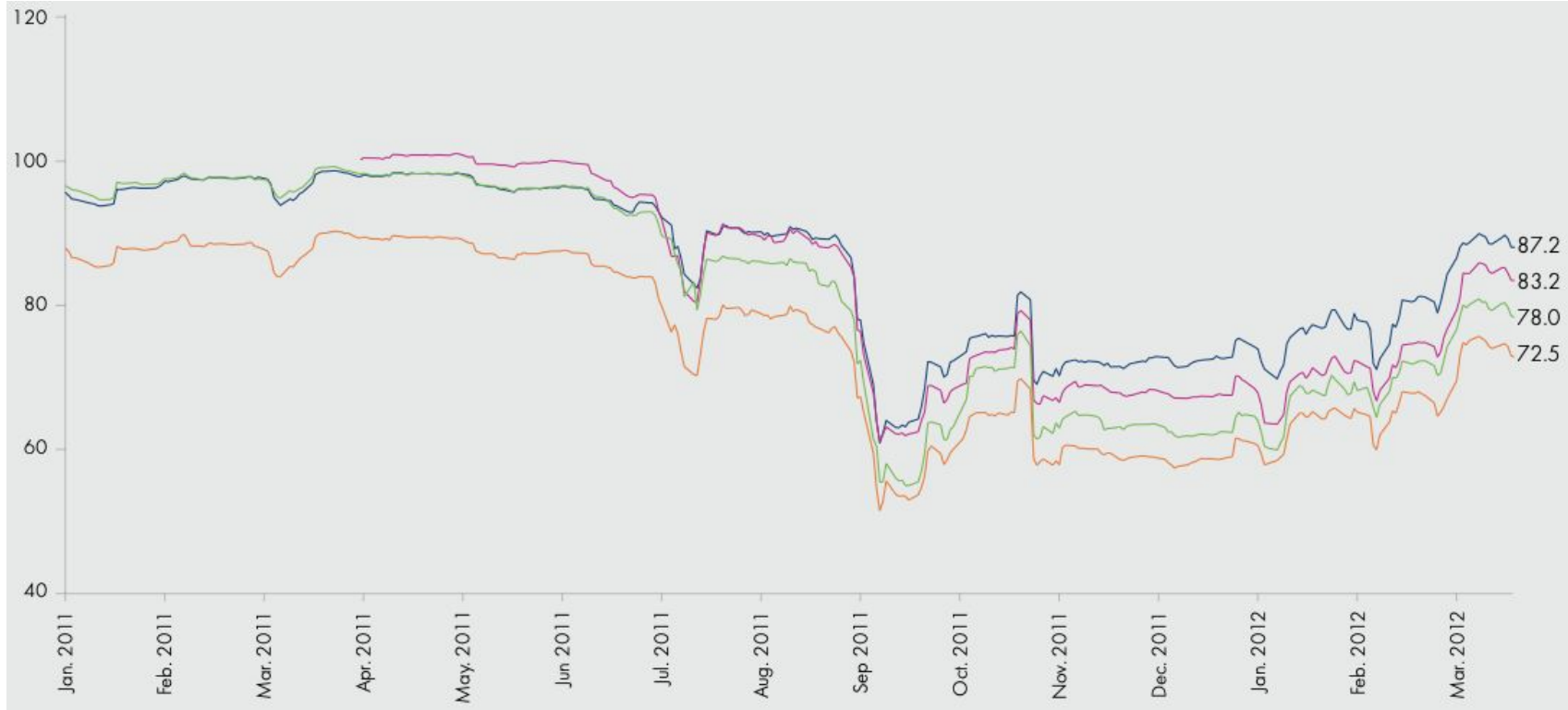
- Deutsche Telekom was HTO's biggest shareholder with a 40% stake
- DT had extended credit facilities in the past to HTO
- DT in 2012 had put out a public announcement with regards to Hellenic Telecom, saying in effect:

'We know that Hellenic Telecom has EUR 2 billion in debt maturities coming due in 2013.

They already have EUR 1.3 billion of this amount. We think that HTO will be able to raise the remaining funds on their own.

In case HTO cannot raise the funds, DT will lend them the money on commercial terms!'

HTO BONDS RECOVERED AFTER THIS ANNOUNCEMENT FROM DT



Source: Annual Report 2011



Note: Not a trading recommendation. Past performance is not indicative of future results.

BUT HTO's STOCK WAS OVERWHELMED BY THE MACRO PANIC



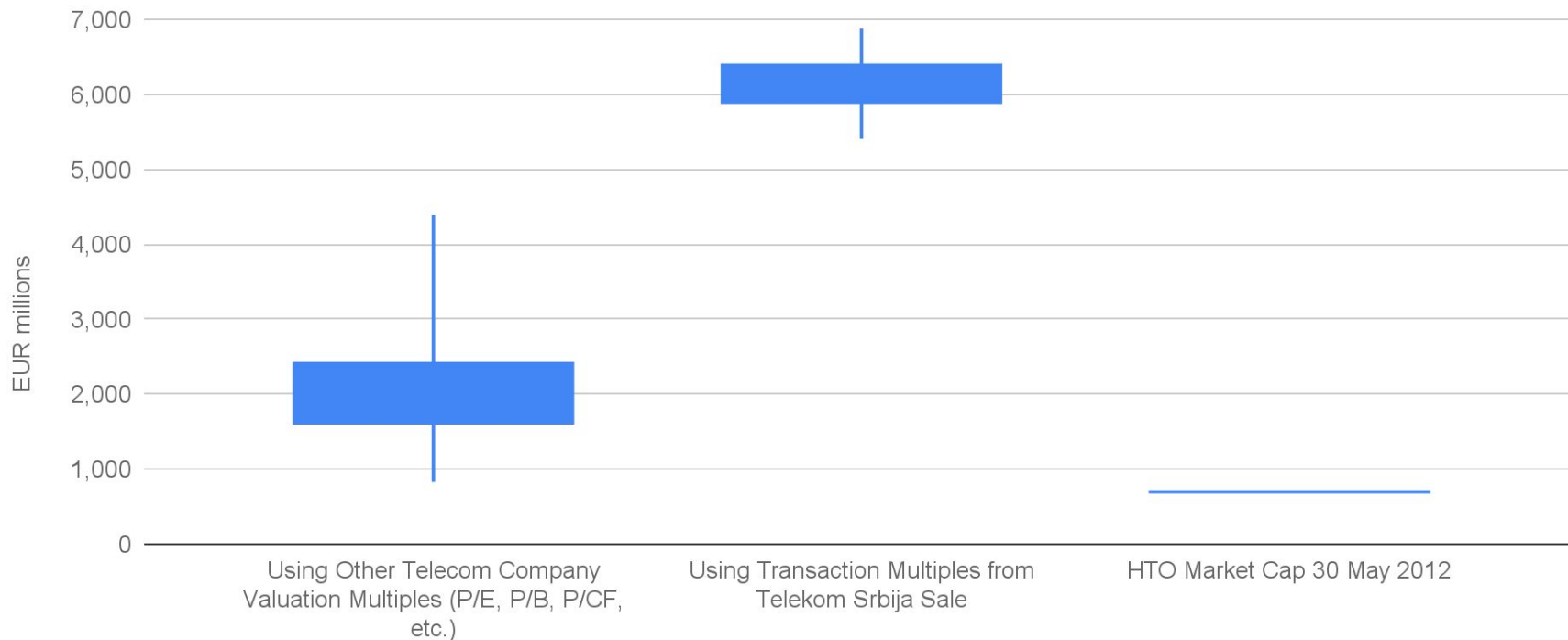
We started buying as soon as the Greek election results were announced in June.

That day, the stock had jumped 50% to EUR 2+ range when election related uncertainty was removed.

Our cost basis was just over EUR 2 per share.

It was a **big** position.

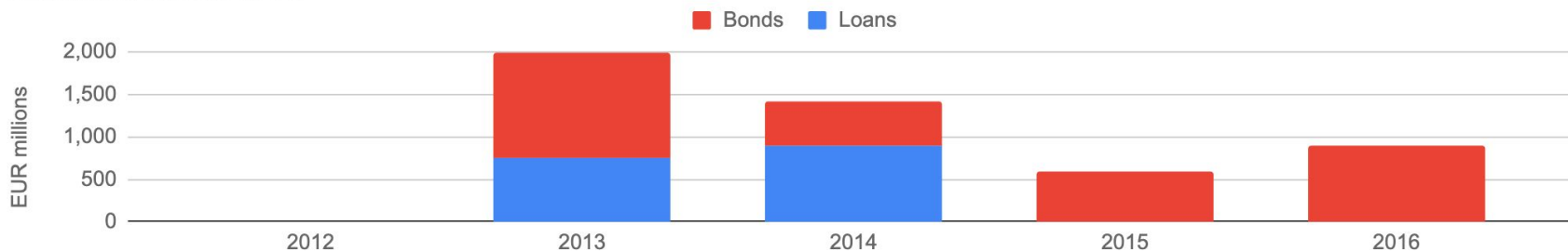
AT BELOW EUR 2 PER SHARE, WE JUST NEEDED HTO TO AVOID BANKRUPTCY IN 2013 (WHICH WE WERE VERY CONFIDENT WILL NOT HAPPEN)



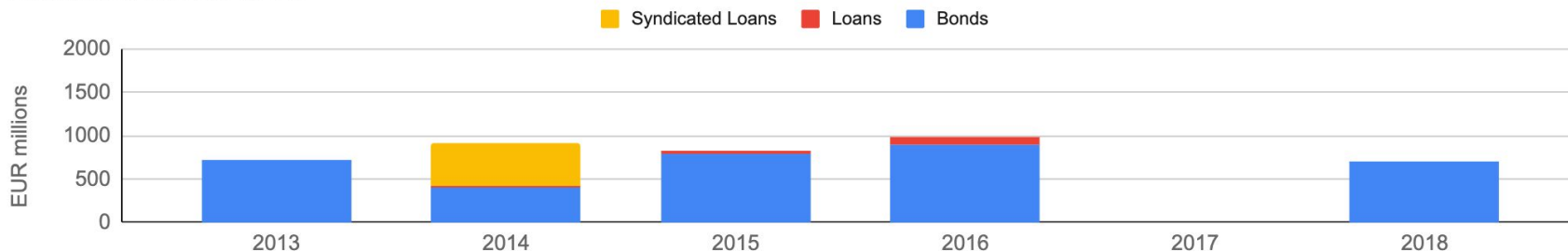
WHAT HAPPENED LATER?

- HTO did not default in 2012, 2013 or in the years after that
- **Comfortably** raised the required 2013 funds from operating cash flow and debt refinancing

Debt Maturity Schedule in 2012

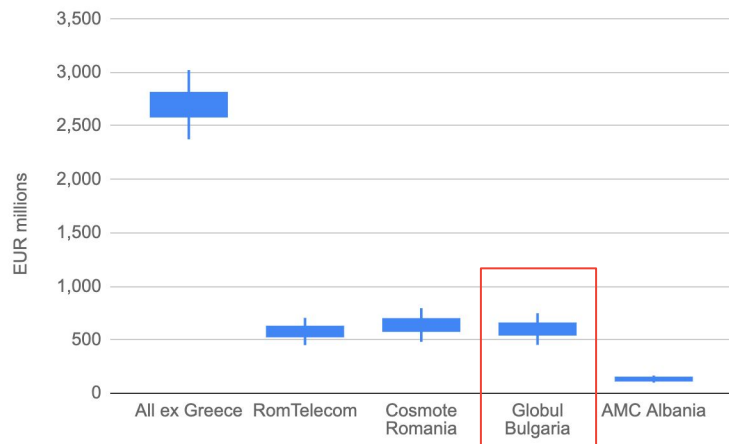


Debt Maturity Schedule in 2013



WHAT HAPPENED LATER?

- In 2013 HTO announced sale of Globul Bulgaria for EUR 717 million to Telenor, at the upper end of our valuation range (see earlier chart)
 - We had valued Globul at EUR 450 - 850 million as of June 2012



- Business remained mediocre in the future too, with declines in fixed line, price competition and churn in mobile, and capex intensity in broadband internet

HTO BONDS WENT BACK TO PAR AS MARKETS CALMED DOWN



Source: Annual Report 2012

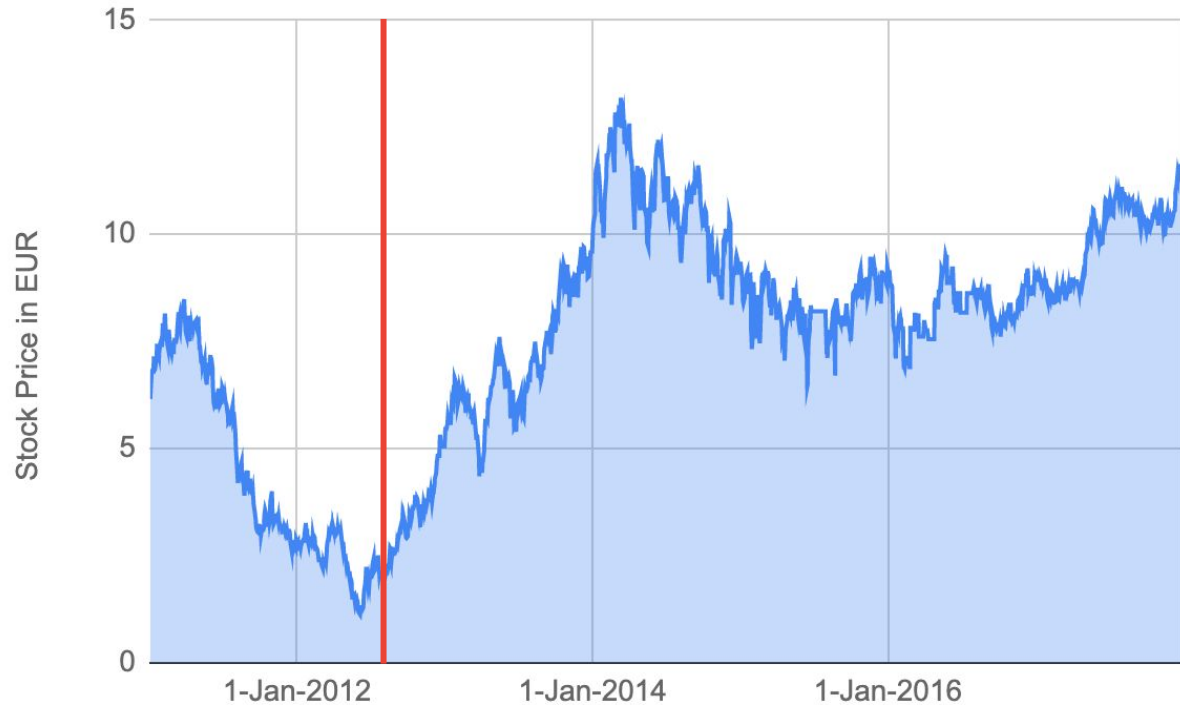


Note: Not a trading recommendation. Past performance is not indicative of future results.

HTO STOCK TRIPLED IN 1 YEAR WHEN THE MARKETS SAW THAT IT HAD NOT DEFAULTED AND NORMALCY RETURNED TO STOCK MARKETS



HTO PROVED TO BE AN EXCELLENT INVESTMENT



Cost Basis was between
EUR 2 - 2.50

Exit was between EUR
11.50 - 12.00

A 600% growth of invested
capital in 2.5 years
approximately



EVENT DRIVEN CHECKLIST - HELLENIC TELECOM

- Big disruption leading to large potential mispricing. The Greek crisis embodied this
- Chance of a permanent loss of capital was very low after the DT announcement
- Wide range of future outcomes - call option-like payoff profile
- Investment thesis had mainly to do with company specific events, not external dynamics
- Catalysts (financial in this case), were independently verifiable and observable

OTHER EVENT DRIVEN INVESTMENTS IN OUR HISTORY

- **Bank of America** | Financial Services | US Listed
- **Mondelez** | Confectionery | US Listed
- **Rolls Royce** | Aircraft Engines | UK Listed
- **Atwood Oceanics** | Oil Services | US Listed
- **Vocus Communications** | Telecom | Australia Listed
- **Infosys** | IT Services | India and US Listed
- **Graftech** | Steel Manufacturing | US Listed
- **Garrett Motion** | Automotive | US Listed
- **Bayer** | Pharmaceuticals & Chemicals | Germany Listed

DELL / VMWARE IS AN EVENT DRIVEN EXAMPLE YOU CAN STUDY AT YOUR LEISURE

 **Anand Batepati**
Long / short investment manager
1mo · Edited · 



It feels great to see an unrealized gain of 75,307% on our position!

For a background, see the two articles on Dell and VMWare that I had written earlier:

- First: <https://lnkd.in/enZ69YuC>
- Second: <https://lnkd.in/grWWgDd>

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INSTRMNT	VAL	CST	BSS	UNRLZD P&L %	%NLV	F
VMW NYSE				75,307%		5.0

  Panindernath Gupta Bachu and 40 others 7 comments



#3: Our process for Event Driven Investing

PROCESS SUMMARY

- Is there a big disruption to cause mispricing?
- Will company specific events drive investment results in this case?
- Is the underlying business stable or changing?
- Is the risk of permanent loss low?
- Does the valuation offer a clear and big margin of safety?
- Are there many good future scenarios?
- What are the catalysts? Are they quantifiable, verifiable and observable?
- Is the risk / reward such that we can invest half our (unleveraged) capital here?
- Will we sleep well at night if we make a big investment here?

Our approach is 100% aligned to these insights.

We wish you all a lifetime of successful investing.

**PLEASE GET IN TOUCH. WE WOULD LOVE TO MAKE
YOUR ACQUAINTANCE AND SAY HELLO.**

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