

# Interview

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**The Hedgeweek Interview: Peter Halloran, Pharos Financial Group (Russia): "We have unique access to primary information about the economy and corporate activity"**

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*Peter Halloran, founder and chief executive of specialist Russia and CIS manager Pharos Financial Group, says the firm's presence in Russia and its network of local contacts are the key to a track record of consistent high returns achieved with low volatility.*

**HW: What is the background to your funds?**

**PH:** The Pharos Russia Fund was launched in October 1997 to invest broadly in the markets of Russia and the Commonwealth of Independent States countries. Peter Halloran, who founded the firm, had previously run the brokerage business for CS First Boston in Russia, including a USD300m proprietary book.

The firm currently manages more than USD150mm across three strategies. The Pharos Russia Fund has been in existence since 1997, offers daily liquidity and is a multi-sector Russia and CIS fund. It has a diverse portfolio of liquid equities, and can short and use derivatives.

The Pharos Gas Investment Fund is designed to take advantage of the transformation of the gas sector in Russia and Eurasia. The two key drivers are the dramatic increase in Russia's domestic gas prices from subsidised levels to market prices, an estimated threefold increase by 2011, and the rapidly increasing demand for natural gas across Eurasia. The only fund focused on this sector, it invests in listed equity and offers monthly liquidity.

The Pharos Small Cap Fund invests in undervalued second- and third-tier companies and offers monthly liquidity. Russia's strong economic growth, rapidly expanding domestic market and increasing financial market liquidity mean that many of these companies are the blue chips of the future.

**HW: Who are your service providers?**

**PH:** Our auditor is Deloitte & Touche, legal advice is provided by Dechert in New York, our administrator is Custom House in Dublin and our prime brokers are Merrill Lynch and Citigroup.

**HW: How, where and to whom do you distribute the funds?**

**PH:** We have distributed the funds primarily in Europe to private banks, institutions and fund of funds. We are interested in adding US institutions to our investor base.

**HW: What is the investment process of your funds?**

**PH:** We have four investment professionals who contribute to the construction of the portfolio. We build a portfolio of primarily equity securities selected according to proprietary fundamental research within the context of our macroeconomic outlook. We look for overvalued opportunities as well, and will short selectively based upon our perception of value and liquidity. In addition, we build a long portfolio of index and single stock options designed to mitigate sharp drawdowns in the market.

**HW: How do you generate ideas for your funds?**

**PH:** Idea generation begins by taking a view on the macro outlook for Russia and other CIS countries, from which we derive winning themes and sectors. We invest in these themes typically through traded equities after having met with their management and modelled their fundamentals using our in-house assumptions. As we are a locally-based manager that has been in the market for more than 10 years, we have unique access to primary information about the economy and corporate activity.

**HW: What is your approach to managing risk?**

**PH:** We have an overlay to protect against sharp drawdowns. We have stop-losses that kick in on 15 per cent underperformance relative to the market. We also stay close to companies through their management and fundamentals.

**HW: Has your performance been as per budget and expectations?**

**PH:** Yes, we are happy with our performance after a challenging year like 2007. How can you not be pleased with a 33 per cent annualised return? That said, we always strive to do better.

**HW: Do you expect your performance to change going forward?**

**PH:** We are well positioned to capture the upside in 2008, given our belief that the market will re-rate in the next six months. Hence we expect performance this year that will be better than last year.

**HW: What opportunities are you looking at right now?**

**PH:** We are looking at gas sector restructuring, infrastructure, the consumer goods sector and agriculture, the increasing spending power of the Russian consumer and the country's impressive growth from real estate.

**HW: What events will affect your sector in the year ahead?**

**PH:** The March presidential election will bring in a group of leaders.

**HW: How will these changes impact your portfolio?**

**PH:** We see a smooth transition ahead with president Vladimir Putin staying directly involved, but the changes may bring some new issues or opportunities. For instance, we hear from Russian fixed line phone companies that the regulators will allow tariffs to increase by 10 to 15 per cent in April, something that currently is not expected by investment community at large. After the elections we may also see changes in the way the energy sector is taxed that will help in increasing profits and exploration.

**HW: What differentiates you from other managers in your sector?**

**PH:** The factors that differentiate us are that we have been based in Moscow since 1997, making us one of the oldest Russian hedge fund managers. We have a strong team with more than 90 years of combined Russian and Western market experience.

We use a derivatives overlay to protect against drawdowns, and our investment process is stress-tested. We have one of the best track records in terms of high returns with lower volatility. Ours is a true hedge fund strategy, long biased with a shorting capability.

Other factors that set us apart from our peers include our Gas Fund, our strong local knowledge and contacts derived from holding 36 board seats, a web site that provides daily market reports and performance, and daily liquidity with no lock-up for our Russia Fund.

**HW: Do you have any plans for other product launches in the near future?**

**PH:** While we are open to new opportunities and ideas, we are committed to and focused on managing our three existing funds.