

# Wrestling Bears

*Facing off with hostile grizzlies is all in a day's work*

By M. Corey Goldman



WARREN IRWIN

Plenty of hedge fund managers boast of fighting off bears. Warren Irwin, founder and president of Toronto-based Rosseau Asset Management Ltd, can literally make that claim.

Recently, he and his entourage found themselves staring into the whites of a none-too-friendly grizzly bear while exploring a diamond property in the Canadian tundra—part of the firm's more recent due diligence on resource plays that has taken it to the wilds of Northern Canada, Venezuela, Ecuador, Brazil, China, Guyana and even Syria.

Neither that bear nor any other beast—real or proverbial—has managed to sink its teeth into Irwin or his flagship event-driven and special-situations funds. Rosseau LP returned an impressive 67% this year through July, and has compiled a compound annualized return of 32% since it launched more than seven years ago, ranking it among the top three event-driven funds tracked by The Barclay Group.

On the contrary, Rosseau LP has managed to rack up impressive compounded returns by focusing on opportunities that emerge from

restructurings, reorganizations, bankruptcies, spin-offs, mergers, turnarounds and other situations that are special and figuring out what investment strategies to apply to exploit them and make money.

That has involved researching and spotting investment opportunities in whatever seems to be the next big opportunity in the business cycle, be it technology, consumer cyclicals, resources or whatever comes next—even if it involves encounters with wild animals or worse.

"It's very much a special situations fund, and right now we see some tremendous special situations in the resource sector," says Irwin. "We look for all types of special situations and event-driven possibilities in all environments, which allow us to be a lot more nimble than our competitors."

### Penchant for credit

Researching special situations and figuring out the best methodology to invest in them has been Irwin's calling throughout his two-decade-long career, which began in 1986 at the age of 22 with his first job as a summer intern

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### Vital Statistics

**Assets under mgt** C\$115 million  
(US\$104 million)

Rosseau LP (Domestic)  
G10 Rosseau Special Situations Fund (Offshore)

### Minimum investment

Onshore C\$250,000, with 1-year lockup  
Offshore US\$500,000, with 1-year lockup

**Registration** OSC

**Domicile** Canada; Cayman Islands

### Redemptions

Onshore Monthly, 60 days' notice  
Offshore Monthly, 90 days' notice

### Fee structure

Management fee 2%  
Incentive fee 20%

**Auditor** Ernst & Young LLP

**Prime broker** BMO Capital Markets

with ScotiaMcLeod Inc, the predecessor firm to present-day Scotia Capital, where he developed the Scotia Universe Bond Index, the Canadian bond market benchmark.

In 1989, he hit the books again to get his CFA and MBA before landing at Deutsche Bank Canada, where he eventually became vice president and director of special investments.

Deutsche Bank shuttered its Canadian equity operations in 1998, prompting Irwin to start his own firm, Rosseau Asset Management, named after Lake Rosseau, part of the famed Muskokas "cottage country" region north of Toronto.

Today, Irwin manages close to C\$125 million in two funds: Rosseau LP for Canadian investors, and G10 Rosseau Special Situations Fund, a Cayman Islands-domiciled offshore product launched in January for non-Canadian investors that runs parallel to the domestic LP fund.

Both funds selectively employ leverage; they also utilize financial instruments such as secured loans, senior debt, convertible bonds, preferred shares and other hedging instruments. Overall, the portfolio typically consists

of between 15 and 20 "situations."

### Non-herd mentality

"One of the big benefits we have is that when the credit cycle gets expensive, like it is now, we don't have to invest in it," says Irwin. "When we see an opportunity in the junk bond market, we're there; when we see an opportunity in the discovery and resource cycle, we're there. That's the advantage of being event driven focused like us."

Indeed, when the fund first launched in early 1999, Irwin was heavily focused on technology, which at the time was still booming. But rather than join the herd in making one-way bets on seemingly overvalued tech stocks, Irwin and his team began to short tech names.

Their bets paid off, with returns of more than 65% in 1999 and 32% in 2000, a year when most investors suffered the wrath of the dot-com bust and the slowing US economy. Rosseau LP returned more than 43% in 2001 before posting its first decline in 2002, when the fund lost just over 18%. It earned more than 53% in 2003 before posting a moderate 5% decline in 2004. It made up for that loss in 2005, posting a 31% return.

"Our returns have been very good, despite the Nasdaq going up and down, despite September 11, despite the blowups of WorldCom and Enron and despite a lot of other things that have made the investing environment difficult over the last seven to eight years," says Irwin.

"Our process is very much driven by where we are in the business cycle. We generally try to find the best risk/reward in the marketplace, regardless."

The proof is in the book value. Of the C\$104 million in Rosseau LP, more than half is return on capital, according to Irwin—money made on investments rather than from capital inflows.

### Mining exploration theme

For the moment, Irwin believes the best opportunities are still in the resources sector. A mining exploration theme distinct from the underlying commodities markets as well as various holdings in other areas have helped produce stellar returns for the fund, including more than 26% between May and July, a period in which many hedge funds suffered through the commodities and stock-market downturn.

But he's quick to note that unlike other high-profile Canadian hedge funds that have been riding the oil and commodities wave in recent years, Rosseau focuses on all types of special situations, specifically corporate restructurings, turnarounds, unique growth situations and market anomalies. The fund uses long and short tactics within its strategy as well as equity, fixed-income and derivative instruments.

"The resource sector is the current driver of performance, but it's a stage in the business cycle, not the fund's focus," says Irwin. "We continue to play the resource 'exploration

cycle,' not the resource 'price cycle.'"

He lists off numerous instances when research, hands-on due diligence and both knowledge of and experience with credit markets and special-situation investing helped uncover excellent investment opportunities beyond the resources and exploration sectors.

One such opportunity was paper maker Moore Corp, which in late 2000 appeared headed for bankruptcy. "Because of my credit background, we rolled up our sleeves and got in there and determined pretty quickly it wasn't going bankrupt at all," says Irwin.

"We felt the new management team coming in would do a good job because the situation wasn't nearly as bad as everyone thought."

Irwin was right: Moore Corp did not go bankrupt and Rosseau made a lot of money buying up its equity, which gained substantially once it began to turn itself around.

**Paper, buses, death**

Laidlaw International Inc was another example. When the busing company announced it was going bankrupt in 2001, Irwin started buying the firm's bonds at 27 cents on the dollar.

"We thought their school bus business in North America was way undervalued, and we bought it extremely cheaply," he says.

The list goes on: the breakup of Imasco in 1999; shorting numerous tech names in 1999 and 2000; shorting Loewen Group, the second-largest North American funeral-services company, prior to its bankruptcy in 1999; and buying Nortel debt in 2002 on the bet that it would survive its dot-com blunders.

"With Nortel, we went in, we did our research, we developed some very extensive financial models and we determined it wasn't going bankrupt," says Irwin. "We thought best risk/reward was to buy debt."

They did—at around 36 cents on the dollar, which after accounting for the company's ability to make its interest payments, reduced Rosseau's cost to around 25 cents on the dollar.

"I felt we had absolutely zero downside risk in buying Nortel at 25 cents on the dollar," says Irwin.

All of the opportunities Rosseau chases after are based on the business cycle and where opportunities lie, says Irwin. At present, the opportunities lie in resources, particularly on the exploration front, where Irwin and his team have been scouring the wilds of Canada's north as well as other parts of the world for companies involved in the space that they see as cheap with strong potential—on the equity or credit side.

**Global due diligence**

In the past year and a half, Irwin and his team have traveled to the Athabasca Basin in Northern Saskatchewan, Kirkland Lake in Ontario, Red Lake in northern Alberta, northern Quebec and the Northwest Territories in search of potential resource plays.

They've also traveled to the far reaches of South America, China and the Middle East to do due diligence—on both the supply side and the demand side.

"You can't specifically hedge whether or not the next hole is going to be a big oil or gold discovery, so the only way to hedge your

**Rosseau Asset Management Ltd  
PERFORMANCE HISTORY**

January 1999 – July 2006

	Rosseau LP	Barclay Event-Driven Index	S&P/TSX
<b>Return (%)</b>			
Annual comp rate	35.60	13.09	9.44
1999	65.34	27.34	29.72
2000	32.73	12.08	6.18
2001	43.15	8.35	(13.94)
2002	(18.41)	(2.83)	(13.97)
2003	53.93	22.04	24.29
2004	(4.98)	16.13	12.48
2005	30.83	8.22	21.91
2006 (7 mths)	67.37	7.90	4.95
<b>Risk (%)</b>			
Annual std dev	22.59	5.78	14.85
Semideviation	20.40	5.96	16.85
Maximum decline	(26.17)	(7.94)	(45.05)
<b>Return/Risk</b>			
Sharpe Ratio	1.21	1.29	0.23
<b>Correlation with Benchmarks</b>			
S&P 500 Total Return	0.14		
ML 3-month T-Bills	0.19		
ML Master Treasury	(0.10)		

risk is to go out there and do the research," says Irwin. "The biggest risk we're taking is discovery risk, and you can't hedge that out."

For the future, Irwin says he's beginning to focus on the slowing US economy, which he feels may present opportunities in retail, real estate and discretionary consumption sec-

tors.

"When this leg of the business cycle ends, we'll be out of it very quickly and on to the next sector," says Irwin. "We've made a lot of money in a lot of different sectors—technology, school-bussing, printing, death-care, you name it. We are not proud." ♦

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