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Markets

No-Drama Hedge Fund Davidson Kempner Closes In on $40 Billion

- Firm made more than $500 million on the sale of MGM to Amazon
- Tony Yoseloff is now looking to private investments for growth

by Katherine Burton
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Davidson Kempner Capital Management's investing chief doesn't own a sports team or a gaudy mansion. He doesn't bloviate on Twitter. And while the firm's returns aren't astonishing, they're always steady. Boring, quipped one competitor, is its brand.

But boring has worked just fine for DK, as the firm is known on Wall Street.

The $38 billion multi-strategy hedge fund is among the world's largest, managing 38 times what it did in 1999, the year after current chief Tony Yoseloff got his foot in the door as an intern.

DK has also twice accomplished what few hedge funds have managed to pull off even once -- turning over leadership to the next generation. Marvin Davidson, who retired in 2004, and Tom Kempner, who followed him out the door shortly before the pandemic, both departed with little fanfare and minus any internal power struggles for the top job.

Adapting to today's market requires a change in tack, one that demands a more public presence. With DK -- like every other hedge fund -- pushing into private markets, the firm is seeking to raise its profile to ensure deal flow and help attract employees and clients. And Yoseloff, 48, is ready to speak.

"The investing world has gotten far more efficient in the last 20 years," he said of the New York-based firm's need to shift to more complex investments. "Those still require elbow grease and creativity."

Tony Yoseloff *Photographer: David Lubarsky/Davidson Kempner Capital*

He's finding those opportunities in areas including real estate, aviation lending, shipping and renewable energy. Yet at its core, DK will remain understated, a place where -- as former leader Kempner notes -- most everyone who's married is still with their first spouse.

Yoseloff grew up in East Brunswick, New Jersey, where he attended public schools. His mother worked at a local community college, and his father and grandfather were publishing executives. The business center of the New York Public Library that Yoseloff funded is named for his grandfather, Thomas. He graduated from Princeton University, where he's a trustee, and received an MBA and law degree from Columbia University.

Yoseloff's talent was so apparent during his summer internship, Kempner said, that the firm broke protocol and offered him a job before it even ended. Still in his 20s, he conceived and managed the firm's wager on the restructuring of Pacific Gas & Electric. Just before the 2008 financial crisis, he was managing the firm's short bet against subprime mortgages. While that trade generated huge fortunes for hedge fund managers such as John Paulson, DK gained a modest 6.6% that year.

The firm's senior executives all say Yoseloff was the obvious choice to succeed Kempner because he had proven himself almost from the beginning.

"He's good about pushing you and asking you the skeptical questions to make sure that you really have the conviction and have done the work that he can trust you," said Gabe Schwartz, who helps lead the U.S. corporates team and assists Yoseloff in overseeing the firm and roughly 430 employees. But once he's convinced an idea makes sense, he's good at "supporting and pushing you to put the capital to work and size things appropriately."

Global Expansion

DK debuted in 1983 to manage Davidson's retirement money, in a way that was both risk-averse and uncorrelated to the markets. Merger arbitrage, distressed debt and opportunistic credit were the original focus. At the time, Yoseloff said, these were cutting-edge strategies that have now become more widely used.

In 1987, the firm started taking outside capital -- it now has about 1,800 clients -- adding convertible arbitrage, long-short equities and credit over time. It has since added offices in London, Hong Kong, Dublin, Philadelphia and Shenzhen and is opening an outpost in Mumbai this year.

DK launched its first private fund in 2011, and is now on its sixth, though about three-quarters of total assets are still in its hedge funds. The flagship multi-strat fund is the largest vehicle, managing $25 billion. Over the past two decades, it has returned 7% annualized, with an average yearly variation of 4 percentage points. It posted its best performance in 2009, when it gained 20%, while 2008 was the only down year, dropping 9.7%.

The firm, which shuns the use of leverage, has generated $19.6 billion for its investors since its founding almost four decades ago, according to LCH Investments, a fund of hedge funds that produces an annual ranking of the most profitable firms. DK cracked the list for the first time last year at No. 18.

"They do a careful job sizing the bets to the capacity of the opportunity set," said Katie Hall, founder of San Francisco-based Hall Capital Partners, a long-time investor in both the public and private funds.

Neiman Marcus

At year-end, the firm established its Ashland Place Finance unit to do aircraft financing, a realm where competition outside of banks primarily involves private equity firms including Apollo Global Management Inc. and KKR & Co. In recent months, DK invested $100 million alongside others in acquiring Chemoil Terminals -- the second-largest independent petroleum storage provider in Southern California -- from Glencore Plc.

The firm also started Davidson Kempner Hawthorne Partners, which provides consulting and other services for DK's portfolio companies, including Neiman Marcus. It had owned bonds of both Neiman and J. Crew until it and other creditors took control of the companies during the pandemic, becoming equity holders.

"We ended up playing an important role in J. Crew -- and it was very similar with Neiman Marcus, too -- in terms of very quickly pivoting, equitizing the debt, providing rescue financing, and taking a key role in making decisions on the board and the management," said DK's Suzy Gibbons, the partner managing those investments.

The bet has paid off so far, with both retailers earning more now than before the pandemic.

A big recent success -- and one of its longer-standing investments -- is MGM Studios, which Amazon.com Inc. acquired last month for $8.5 billion. DK first purchased MGM's debt in 2009, helped the company through a prepackaged bankruptcy and became a substantial equity owner after it emerged from court protection, later adding to its position. DK was betting that the studio's film and TV library, including the James Bond franchise and Rocky series, along with new management, were reasons to hang on. It made more than $500 million on the investment.

The firm has made some big bets outside the U.S. in recent years. In 2020, during the depths of the global health crisis, DK provided about 170 million pounds ($222 million) in secured financing to Virgin Atlantic Airways, offering more favorable terms than other potential backers. At the beginning of this year, it bought non-performing shipping loans from Piraeus Bank for 400 million euros ($433 million).

While the firm continues to raise money for its private vehicles, Yoseloff expects public markets will still provide interesting wagers. In the past four weeks the firm invested hundreds of millions of dollars in corporate credit.

"I'm optimistic that we'll see more liquid opportunities going forward," he said. "But right now in the corporate area, the bulk of opportunity really has been in the illiquid side."