Soros withdrawal: a sign of things to come

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In a further indication of the mounting instability on world financial markets, billionaire international financier George Soros has announced his withdrawal from large scale and high risk hedge fund investing.

Last Friday Soros announced that his two top money managers, Stanley Druckenmiller and Nick Roditi, would leave their posts shortly and he would reorganise his Quantum Fund into a group of smaller funds based on lower risk strategies.

The moves come in the wake of huge losses suffered during the recent collapse in technology stocks. It is understood that the Quantum Fund lost one fifth of its value, due largely to the collapse of share prices in technology stocks. The 20 percent drop wiped almost $3 billion from the fund's net assets, which stand at $8.2 billion.

The Soros announcement follows hard on the heels of the closure of the second largest hedge fund company, Tiger Management LLC, headed by Julian Robertson. Announcing the closure last month, Robertson said his approach to investing, which was buying value stocks and selling overvalued stocks short, could not be successful in the current market, which he described as “irrational”.

The Tiger fund, which had investment returns averaging 32 per cent a year between 1980 and 1997, experienced a drop in asset values of $16 billion in the last 18 months, much of which was due to the fall in technology stocks.

In explaining the reasons for his withdrawal, Soros said that maybe he did not understand the market.

“We will be more conservative, have less exposure to the market and accept lower returns because we want to lower the risk profile. ... Markets are extremely risky, and in some ways I think the music has stopped—only most people are still dancing.”

Pointing to the impact of the fall of technology stocks, Druckenmiller, who announced his resignation, said: “I never thought the NASDAQ would drop 35 percent in 15 days. This business is a bit like a drug. When you are doing well, it's hard to quit.”

Soros Fund Management, which made over one billion pounds profit when it “broke the Bank of England” in the 1992 devaluation of the British currency, is also said to have lost billions in speculating that the euro would rise against the dollar, and that the Japanese yen would fall. The opposite has occurred with the US dollar, in particular, remaining strong against the euro.

The moves by Soros and Robertson are a sure sign that big investors are getting out in anticipation of a collapse, leaving millions of smaller investors to bear the losses.

The Soros loss was the subject of some revealing comments by another billionaire investor, American Warren Buffet, the head of Berkshire Hathaway Investment Fund, and his vice chairman Charlie Munger. Commenting on their decision not to risk investment in technology stocks, Munger said: “In the end, Soros wasn't comfortable watching others make money in technology stocks. If we don't understand something, we're perfectly willing to let it rage on with lots of people making lots of money—while we don't.”

Answering a question by a shareholder at last month's annual meeting of the fund on why Hathaway had not invested in Internet stocks, Buffet said: “ We will never buy anything we don't understand.”

And in what amounted to a warning of a potential meltdown, he added: “Anytime there have been real bursts of speculation in the market, it does correct itself eventually. Looking back, you will see this as an enormous wealth transfer, but investors as a whole will gain nothing. It's the same principle as a chain letter.”

In other words, once the influx of funds that has been financing overvalued stocks dries up, small investors will suffer the same fate as victims of a chain letter or pyramid scheme.