

Here's how George Soros broke the Bank of Thailand
September 8, 2016

George Soros is one of the most successful hedge fund managers ever. While at the helm of the [Quantum Fund](#) (founded by Soros and Jim Rogers in the 70s), he generated an average annual return for investors of 30%.

Across this ten-part series, I'm taking a look at Soros' life, trading career, and political involvements. In part one, I covered the fund manager's early career and the beginnings of the Quantum Fund. In this part, I'm going to look at the Quantum Fund's rise to fame and some of the best trades Soros and his team placed over the years.



Quantum Fund: The money machine

The Quantum Fund is arguably the world's most successful hedge fund. Under the stewardship of George Soros, Jim Rogers, and later Stanley Druckenmiller, the fund produced an average annual return for investors of 30%. During the three decades between 1970 and 2000 a \$1000

investment with Soros in 1969 would have grown to \$4 million by the year 2000, an annual growth rate of 30%.

The Quantum Fund didn't follow a set trading strategy. Trades were placed based on economic and political conditions in certain markets. While there's no doubt that Soros and his team were extremely skilled at their profession, it is also reasonable to say that there was a fair amount of luck involved in the Quantum Fund's returns over the years. The team tended to place large leveraged bets on single ideas, most of which paid off handsomely but a single loss could have decimated decades worth of returns for investors, Soros and Rogers (the co-founders reinvested the vast majority of their profits and fee earnings from the fund over the years).

The Quantum Fund's bet against the Bank of England in 1992 is probably the fund's most famous trade. But this only one trade in the story and the Quantum Fund recorded many other successful trades over its life. One of the more controversial trades (or group of trades) put on by the fund was against a basket of Asian currencies, specifically the currencies of Thailand and Malaysia just before 1997 to 1998 Asian Financial Crisis.

The [Asian Financial Crisis](#) started as a localized currency and financial crisis in Thailand, but tremors soon spread to other Southeast Asian countries—including Malaysia, Indonesia and the Philippines. By the fall of 1997, the contagion extended its reach to South Korea, Hong Kong and China, the year after Russia and Brazil saw their economies enter a free-fall, Japan fell into recession at the end of 1998 and the US financial system balked at the possible bankruptcy of the infamous Long Term Capital Management.

The Asian Crisis started in August 1997, only a month after Thai authorities abandoned the US dollar Thai baht peg. The baht had been pegged to the dollar for more than a decade, and the Thai authorities had been encouraging banks and big corporates to borrow US dollars unhedged to fuel domestic lending for much of this period. However, as the US dollar got stronger in the mid-90s, Thailand's trade and capital accounts deteriorated, firms found it difficult to meet dollar debt obligations and it became apparent the peg was unsustainable.

As soon as the peg was abandoned, it quickly became clear how bad the situation had deteriorated. Thai authorities left the peg on July 2, 1997, and by October 24 the free floating baht had depreciated by 60% against the dollar. Thailand's troubles triggered a wave of speculation against other Asian currencies and over the same period the Indonesian rupiah, Malaysian ringgit, and Philippine peso depreciated by 47%, 35%, and 34%, respectively.

Did Soros start the crisis?

According to sources who had knowledge of the Quantum Fund's positioning at the time, Soros bet just under \$1 billion of his total war chest of \$12 billion against the baht. There's plenty of speculation that because he placed such a large bet on baht, Soros helped engineer the Asian crisis via his political connections. Yet Soros wasn't the biggest single speculator to hold a position against the currency. Julian Robertson's Tiger Fund had three times the exposure of Soros with almost \$3 billion bet against the baht. If anything, Julian Robertson would have been more motivated to engineer Thailand's decline.

Soros has argued that hedge funds did not start the crisis it was, in fact, the reaction of Thailand's central bank to the [knowledge of hedge fund positioning that exacerbated the problems](#).

Resisting the speculators

In an attempt to resist devaluation, the [Bank of Thailand](#), purchased baht with dollars in the foreign exchange market, raised interest rates and restricted foreigners access to baht during the first few months. All of these measures decimated the bank's credibility. Foreign exchange reserves collapsed from \$37.2 billion in December 1996 to \$30.9 billion in June 1997, excluding off-balance sheet obligations to deliver \$23.4 billion dollars in the forward market over a 12-month period. While raising interest rates only served to damage the country's weakening financial sector more. In May 1996 the Bangkok Bank of Commerce incurred over \$3 billion in bad loans and was taken over by the government and by the end of 1996 office vacancy rates in Bangkok exceeded 20%. Thailand's external debt at that time stood at \$100 billion.

Still, initially these actions worked, and the shorts were squeezed in early 1997, but the measures also used up all of the bank's firepower leaving it with nothing to defend the currency with if the speculators returned.

The Quantum Fund suffered only marginally from this move. The team used futures to bet against the baht, so they were able to keep the trade open throughout the turbulence and wait for the ultimate end.

The central bank's comedy of errors only served to attract more hedge funds to speculate against the baht. After some initial success against speculators in early 1997, by August the central bank had run out of money and tools to fend off the hedge funds, which, sensing blood returned in droves.

The bank eventually broke, the baht devalued and Soros profited. Even though Thailand's troubles did unfold into a global crisis, the country

needed the devaluation and if the central bank had not wasted all of its reserves fighting hedge funds, a more orderly rebalancing could have taken place. Soros himself has remarked:

“For instance, by selling the Thai baht short in January 1997, the Quantum Fund managed by my investment company sent a market signal that the baht may be overvalued. Had the authorities responded to the depletion of their reserves, the adjustment would have occurred sooner and been less painful. But the authorities allowed their reserves to run down; the break, when it came, was catastrophic.”

Read the [original article](#) on [ValueWalk](#). Sign up to get our [free newsletter and receive our free e-books](#) on famous hedge fund managers and value investors. You can also check out ValueWalk on [Facebook](#), [Twitter](#) and Yahoo Finance Contributors. Copyright 2016. Follow ValueWalk on [Twitter](#).