HEPTAGON
Capital

Future Trends: Monthly Update

March 2021

The Heptagon Future Trends Fund has a very clear and distinct philosophy: we seek to identify and invest in a diverse range of businesses offering exposure to the key trends that we believe will help shape the future. The Fund has delivered strong outperformance since its inception in January 2016, gaining ~133% vs ~99% for its MSCI World Index benchmark. Although the Fund added 1.3% in March, on a year-to-date basis, Future Trends has underperformed relative to its benchmark. With our focus unchanged and the prospects for our businesses looking more attractive than ever, we believe the long-term opportunity to invest in the future is highly compelling.

There are some things within our control – which themes we choose to follow and businesses to invest in – and others, like the move in bond yields or the abrupt rotation across sectors, that we cannot. Common sense dictates that we focus on the former. Against this background, relative underperformance of some of our businesses since the start of the year has created superb opportunities. We have taken advantage of this dynamic; **adding to existing positions in periods of weakness**.

March saw the end of the reporting season for the three-month period ending 31 December 2020. 65% of our businesses beat expectations in the quarter, consistent with the 61% average recorded since the inception of the Fund. More importantly, in terms of the forward guidance provided by our investments – whether quantitative or qualitative – 30% of our businesses provided an outlook that *exceeded* prior levels. With much global uncertainty around the pandemic, the timing of reopenings and supply chain inflation, we believe the provision of *any guidance at all* speaks highly to the strength in positioning of our investments. **Consensus earnings estimates for the majority of our businesses are now higher than they were at the start of the year, as are our forecasts for the Future Trends Fund as a whole** (on a weighted basis).

Our conviction in the outlook has only been further reinforced by our ongoing interaction with management teams. During the first quarter of 2021, we conducted a total of 30 virtual meetings including with 15 of our current 22 investments in the Fund. In March alone, we had 1-1 meetings with senior management at First Solar and investor relations at both Thermo Fisher and Daifuku as well as attending a small group meeting with the CEO of Avast. We also participated in MOWI's virtual Capital Markets Day. Such meetings are an important part of our investment process. We seek to understand not only the evolution of the bigger picture strategic direction of our businesses but also their commitments to ongoing out-innovation (through efficient capital allocation) and social responsibility.

First Solar stands out as a compelling case study. We have followed the theme of alternative energy since March 2018 and wrote specifically about solar in January 2020. Our initial investment in First Solar took place in December 2019. During 2020, First Solar gained 76.7%. The shares hit a 52-week (and 9-year) high of $107.53 on 21 January 2021. They then lost 33.6% of their value in the subsequent six weeks, hitting a 2021 low of $71.45 on 8 March. Sure, the company had missed forecasts when it reported quarterly results (on 25 February), but at the same time, management provided significantly better guidance for the year ahead. We can point to reasons for the underperformance – profit-taking, a cyclical rotation away from alternative energy names into oil businesses, the reweighting of a major alternative energy ETF – but importantly, the fundamental story had not changed. If anything, it had improved. Put simply, the demand for solar energy solutions continues to grow at the same time as the cost of providing solar is falling. As First Solar's CFO put it when we spoke with him, "I don't see any sign of slowdown." Our response: **we increased our position in First Solar**. From its 8 March nadir, the shares climbed 22.2% through to the end of the month.

On a year-to-date basis, First Solar remains down 11.7%, making it one of the Fund's three worst-performers. Only Daifuku and Avast have underperformed First Solar, with these businesses down 15.0% and 15.2% respectively. Similar to First Solar, Daifuku staged a recovery in March, gaining 6.5% and outperforming the MSCI World (First Solar closed up 7.8% over the past month, while Avast continues to lag, down 1.3%). Our conviction in the case for Daifuku's automation business and Avast's cybersecurity franchise remains undiminished.

Across our portfolio we continue to strive for balance. Our three best-performers over both the past month and since the start of the year offer exposure to different themes. The premise of Future Trends is pan-thematic diversification. During March, the Fund's three leaders were Vestas (wind turbines), IBM (digital ecosystem) and ASML (semiconductor machinery). All three stocks have gained more than 10%. ASML has also been the Fund's stand-out performer since the start of the year, increasing by 30%. The other two notable outperformers since 1 January have been Zebra (industrial automation) and MOWI (salmon).

Vestas is currently the Fund's largest position (and ASML, MOWI and IBM all also feature in the top-five, with the remaining space occupied by Mastercard). Similar to First Solar, the business has seen volatility in its share price over 2021. From having peaked at DKK1560/share on 7 January (an all-time high), it lost 33.2% of its value through to 5 March. From then through to the end of the month, it gained 24.9%. We used this sell-off to increase in our position in Vestas.

To return to the theme of balance, consider not just the Fund's thematic diversification but also its valuation. ASML trades on 42.0x 2022 earnings on our forecasts and Vestas on 28.6x. We believe these multiples are justified given the positioning of both businesses as well as future assumptions about growth. ASML is the de facto monopoly supplier of the machines that make semiconductor chips – the future can't happen without ASML, in our view. Vestas is the global leader in wind turbines and their servicing. Its €23.9bn order backlog (as of 31 December 2020) is equivalent to 1.6x last reported revenues and accounts for over 70% of its market value. Both businesses also have net cash on their balance sheet. At the other extreme in terms of valuation, IBM trades on just 13.0x our forecast for 2022 earnings, while MOWI commands a multiple of 17.6x. Furthermore, investors get a 4.9% dividend yield with IBM and 2.1% at MOWI. Both businesses have leading franchises and sustainable competitive advantages in our view. For the Future Trends Fund overall, its current weighted average P/E multiple is 27.8x, *lower* than at the start of the start year (30.0x) and at a smaller premium to the MSCI World's multiple (7.8 points versus 10.2 points), *despite* the fact that estimates have increased at a faster rate.

Our intention is to remain nimble and opportunistic, striving for balance while not losing sight of the bigger picture. Thank you for your ongoing interest in and support for the Future Trends Fund.

Alex Gunz, Fund Manager

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For all definitions of the financial terms used within this document, please refer to the glossary on our website: https://www.heptagon-capital.com/glossary.

Risk Warnings

The Fund is subject to special risk considerations including geographic concentration risk, portfolio concentration risk and operational risk. The investment return and principal value of an investment will fluctuate so that the investor's shares, when redeemed, may be worth more or less than their original cost. Any investor should consider the investment objectives, risks and charges and expenses of the fund carefully before investing. Where an investment is denominated in a currency other than the investor's currency, changes in rates of exchange may have an adverse effect on the value, price of, or income derived from the investment.

SFDR

This Fund has been classified as an Article 8 for the purposes of the EU's Sustainable Finance Disclosure Regulation ('SFDR'). The Fund promotes environmental and/or social characteristics but does not have sustainable investment as its primary objective. It might invest partially in assets that have a sustainable objective, for instance assets that are qualified as sustainable according to EU classifications but does not place significantly higher importance on the environmental objective of each underlying investment. Please see prospectus for further information on the Funds environmental and/or social characteristics and relevant sustainability risks and principal adverse impacts which may impact the Fund's performance.

Heptagon Capital LLP, 63 Brook Street, Mayfair, London W1K 4HS
tel +44 20 7070 1800
fax +44 20 7070 1881
email london@heptagon-capital.com

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