HEPTAGON Capital

# Kopernik Global All-Cap Equity Fund

## Q2 2021 Commentary

### Fund Manager

**David Iben**

### Investment Objective

The Fund seeks to provide long-term capital appreciation by investing primarily in equity securities of U.S. and non-U.S. companies. The research driven investment process seeks to add value through active management and by selecting securities of companies that, in the manager's opinion, are misperceived and undervalued by the market.

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The **Kopernik Global All-Cap Equity Fund** (the "Fund") is a sub-fund of Heptagon Fund Plc which is an open-ended umbrella type investment company authorised pursuant to UCITS regulations. Heptagon Capital Limited ("Heptagon") is the Investment Manager and Kopernik Global Investors LLC ("Kopernik") is the Sub-Investment Manager meaning Kopernik exercises discretionary investment authority over the Fund. The Fund was launched on 16th December 2013 and had AUM of USD 1,368m as of 30th June 2021.

## Performance Review

**Contributors**

Similar to the first quarter, the two largest contributors for the quarter were natural gas companies. **Range Resources Corp ("Range"),** a U.S.-based natural gas company with long-lived reserves, was up 62.3%, while **Gazprom PJSC ("Gazprom"),** the largest natural gas producer in Russia, with a monopoly on natural gas exports to Europe, was up 27.4%. Additionally, **Southwestern Energy Co ("Southwestern"),** another U.S. gas company with a similar reserve profile to Range, was up 21.9%. In our opinion, the fundamentals continue to support higher natural gas prices in the future. The Canadian oil and natural gas producers also had a strong quarter. **MEG Energy Corp ("MEG") and Cenovus Energy Inc ("Cenovus")** both contributed positively, building on their gains from the previous quarter. Both companies are Canadian oil producers with long-lived assets. Cenovus also has natural gas and natural gas liquids production, as well as downstream assets in the U.S. and Canada. MEG was up 39.5% and Cenovus was up 27.6%. We took advantage of price volatility to add to Range and Southwestern before trimming on higher prices later along with Cenovus.

As we discussed last quarter, the market opportunities in oil and natural gas have been, in large part, the product of two factors: a COVID-related temporary drop in demand, and, in our opinion, a passive approach to environmental, social, and governance ("ESG") factors that have resulted in various misallocations. With regard to the latter, it is our belief that buying shares on the secondary market does not impact sustainability factors negatively.

Additionally, we prefer an integrated approach and engaging with companies to minimize the negative effects and/or affect positive change. As to the former, more countries are lifting COVID restrictions causing the oil demand to rebound quickly. Supply has not kept up, and, as a result, the oil price is the highest it has been in seven years. Importantly, the energy production companies continue to trade at discounts to our risk adjusted intrinsic values.

Uranium companies also built on their gains from the previous quarter. One of the largest positions, and a position the strategy has held since inception, is the Canadian uranium producer **Cameco Corp ("Cameco")**, which was up 15.5%. Other uranium producers were also positive contributors. **NexGen Energy Ltd ("NexGen")**, a uranium exploration company planning to develop a project in the Athabasca basin of Canada, was up 14.2%, while **NAC Kazatomprom JSC ("Kazatomprom")**, the world's largest uranium producer, was up 17.9%. We trimmed Kazatomprom and added to Cameco on lower prices before trimming later on as the price went up.

Uranium is trading well below its incentive price, suppliers have extended their production cuts and/or are keeping mines closed, excess inventories are declining, and new nuclear reactors are being built (there are currently 54 under construction, primarily in emerging markets). Further, while we are not modelling in a significantly higher demand for uranium, the political environment is seemingly more supportive of nuclear power, which is an inexpensive, zero-carbon, and stable source of electricity.

Other positive contributors were spread across multiple sectors. In communication services. **KT Corp ("KT")** and LG Uplus Corp are the second- and third-largest Korean phone companies, respectively. KT Corp was up 13.1% during the quarter, while LG Uplus was up 25.9%. In utilities, **Centrais Eletricas Brasileiras SA ("Eletrobras")**, Brazil's dominant electricity provider, was up 45.3%. In agriculture, palm oil producer **Golden-Agri Resources Ltd ("Golden Agri")** was up 11.6%. Like energy and resource companies, palm oil is a commodity that has an undeserved negative ESG reputation, in our opinion. Palm oil is, by far, the most land efficient food-oil, and while palm oil companies have had a difficult past with environmental and social issues, they have made significant strides towards better ESG practices. We added to Golden Agri and trimmed Eletrobras.

The strategy also saw a positive contribution from copper miners, as the copper price remained strong throughout the quarter. **Ivanhoe Mines Ltd ("Ivanhoe")**, which owns the largest undeveloped copper project in the world, Kamoa-Kakula in the Democratic Republic of Congo, was up 40.3%. We trimmed Ivanhoe.

**Detractors**

While copper companies contributed positively, and materials as a sector made a positive contribution to returns, many of our mining holdings were down. The largest detractor was **Centerra Gold Inc ("Centerra")**, a Canadian gold producer which owns mines in Kyrgyzstan, Canada, and Turkey. Beginning in early May, the government of Kyrgyzstan began taking aggressive steps towards the Kumtor mine by passing a law that would allow government control of the mine, supporting a $3 billion environmental civil claim, and overriding the 2009 Investment Agreement which settled past claims and provided certain protections to Centerra. As of May 15, 2021, Centerra had stated that the government had effectively seized control of the mine and that Centerra was initiating arbitration proceedings to enforce its rights under the longstanding Kumtor investment agreements. Centerra was down 13.7%. We added to our position in Centerra. It continues to trade at a discount to Kopernik's risk-adjusted intrinsic value, and trades at a discount to the value of the company's other properties, without Kumtor. Kumtor, however, is a world-class asset and we are hopeful that the government and the company can resolve their disputes.

Another detractor was **Northern Dynasty Minerals Ltd ("Northern Dynasty)**, which owns the Pebble Mine (a massive copper/gold/molybdenum deposit in Alaska). Northern Dynasty was down 22.9%. Northern Dynasty has continued to deal with uncertainty as it attempts to bring its Pebble Mine project through permitting. Over the summer of 2020, the Army Corps of Engineers issued its EIS (Environmental Impact Statement). It concluded, after many months of study, that the project met expectations and posed negligible danger to the environment. Several months later, they bowed to political pressure and reversed themselves without explanation, denying Northern Dynasty's permit for the Pebble Project. While Northern Dynasty filed for an administrative appeal in February, this is an unfortunate turn of events.

The appeal may now take years, but patience is warranted. We require a larger margin of safety for this stock than for any other stock in the portfolio. Even so, the potential upside is amongst the largest in the portfolio.

Other gold and silver mining companies were down as well. **Equinox Gold Corp ("Equinox")**, a Canadian mining company with 12.5 million ounces of reserves, was down 12.8%. Silver miners were down for the second quarter in a row, Bear Creek Mining Corp, whose Corani Silver Project is one of the largest undeveloped silver projects in the world, was down 24.3%; **Fresnillo PLC ("Fresnillo")**, the world's largest primary silver producer, with all assets in Mexico, was down 8.9%; and **Pan American Silver Corp ("Pan American")**, another of the largest silver mining companies globally, was down 4.6%. We added to Equinox, Fresnillo, and Pan American.

We continue to be optimistic on the fundamentals for gold. The central banks doubled the monetary base last year and have increased it ninefold since 2008. Meanwhile, the price of gold is lower than it was in 2011 and real rates are negative. The fundamentals bode well for higher future gold prices, in our opinion. Importantly, the mining stocks are undervalued, even without a gold price increase. As a reminder to our investors, we demand a large margin of safety before we invest in mining companies, and only invest when there is significant upside. In addition, diversification across countries, management teams, balance sheets and assets is an important part of our process.

Japanese companies in multiple sectors also detracted from returns. In healthcare, **Suzuken Co Ltd**, Japan's third largest pharmaceutical distributor, was down 25.1%. In industrials, **Mitsubishi Corp**, a Japanese conglomerate with multiple business segments, was down 3.7%. We added to our holdings of both companies.

## Portfolio Activity

The strategy had four new initiations during the second quarter. The strategy initiated positions in **Kyorin Holdings Inc**, a Japanese manufacturer of branded and generic drugs selling at less than book value; **DL E&C Co Ltd**, a Korean engineering and construction company that also has a housing-related building and development business, trading at a one-third discount to book value; and Harmony Gold Mining Co Ltd, a senior gold producer based in South Africa with gold and copper assets in South Africa and Papua New Guinea.

The strategy eliminated positions in BrasilAgro - Co Brasileira de Propriedades Agricolas, Pax Global Technology Ltd, Diana Shipping Inc, and Embraer SA as prices appreciated.

In closing, we are pleased by the strategy's performance in the second quarter and continue to be excited by the portfolio's significant potential for upside over the long run. We persist in opportunistically buying and holding companies that we believe are trading at significant discounts to their risk-adjusted intrinsic value, using volatile times to our advantage. You can count on us to employ our disciplined, fundamentals-based, long-term approach that has produced a proven track record through full market cycles.

**Why Kopernik?** ***By Kopernik Global Investors, LLC***

*Philosophically, we view ourselves as owners of businesses. Our job is to appraise these businesses and take advantage at times when an inefficient, emotional marketplace offers securities at a price that is significantly different from our appraisal. Like our namesake, Kopernik (better known by his Latin name – Copernicus), we trust the results of our own analysis even when (especially when) it generates vastly different conclusions from those of the crowd and/or those taught by many academics. Similarly, we commonly question the data issued by governments, central bankers, and companies themselves. We understand that bargains appear often because people focus on fear or panic, and other forms of risk that are not relevant to the investment portfolio. High tracking error, bad headlines or unpopular stocks/countries/ regions/industries can present a degree of risk to a manager's career, while often lowering the potential of permanent loss of capital (due to lower initiation prices and higher potential upside) to the portfolio. Similarly, Kopernik believes volatility and other measures of past price movements are not relevant to long-term investors' assessment of risk. It can be indicative of potential risk to short-term speculators or to highly levered players, but can often present opportunity for true long-term investors.*

As always, we appreciate your patience and support.

Sincerely,
***Heptagon Capital & Kopernik Global Investors***

## Total Returns as of June 30th, 2021, net of fees

| | Q2 21 | YTD | 2020 | 2019 | 2018 | 2017 | 2016 | 2015 |
|---|---|---|---|---|---|---|---|---|
| **Kopernik Global All-Cap*** | 9.7% | 19.8% | 38.3% | 10.7% | -12.0% | 8.1% | 52.0% | -12.0% |
| **MSCI ACWI NR USD Index** | 7.4% | 12.3% | 16.3% | 26.6% | -9.4% | 24.0% | 7.9% | -2.4% |

** Class I shares*

***Past performance is no guide to future performance, and the value of investments and income from them can fall as well as rise***

## Important Information

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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

The Fund takes sustainability risks into account within the investment process, and this is disclosed in accordance with Article 6 requirements of the Sustainable Finance Disclosure Regulation (‘SFDR’) in the Fund’s prospectus. However, the Fund does not have as its objective sustainable investment and does not promote environmental or social characteristics for the purposes of the SFDR. Sustainability risks may occur in a manner that is not anticipated by the Sub-Investment Manager, there may be a sudden, material negative impact on the value of an investment and hence the returns of the Fund. As a result of the assessment of the impact of sustainability risks on the returns of the Fund, the Sub-Investment Manager aims to identified that the Fund may be exposed to sustainability risks and will aim to mitigate those risks.

Authorised & Regulated by the Financial Conduct Authority (FRN: 403304)

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