Listed Private Assets: Quarterly Commentary

Q3 2021

Fund Manager

Arnaud Gandon

Investment Objective

The Fund aims to produce high single digit returns, from a combination of capital appreciation and income, with a targeted annual yield of 4-5%. The investment philosophy of the Fund is founded on the premise that exposure to private assets should earn a premium over listed equities and bonds over time.

Contact

Heptagon Capital
63 Brook Street, Mayfair,
London W1K 4HS

Tel: +44 20 7070 1800
email london@heptagon-capital.com

The strategy delivered a solid +3.3% during 3Q21 against a background of low global equity returns of +0.6%.

The recent equity market correction resulting from a rapid rise in US yields has highlighted the challenges facing an expensive and highly concentrated US equity market. It reinforced our belief that the **"easy money" policies implemented by the Federal Reserve since the GFC have created a significant feedback loop into equity prices and valuations**. Low rates, inflows into passive equity ETFs, high sector concentration in technology and growth companies are in our opinion, all related and "two sides of the same coin".

Our contention is that the natural rate of interest, which has been suppressed for many years now, may eventually reassert itself since some of the imbalances created by ultra-low rates have become too large. It is, as always, impossible to say what might be the trigger for such a readjustment but there are plenty of candidates today. This includes overvaluation in pockets of the US equity markets; rapid rises in inequality and its associated political implications; a clear shift to more fiscal spending and potentially higher rates of inflation.

Since non-US equities and value as a style have underperformed for such an unusually long period of time, **we believe that seeking diversification into non-U.S. equity markets and across many styles** such as value, cyclicals and quality should help deliver above average returns over the next 10 years. In this context, the **Listed Private Assets strategy is well placed to benefit from such a change in market leadership: both value and income plays have a lot of ground to cover** to return to a more balanced valuation equilibrium relative to other factors.

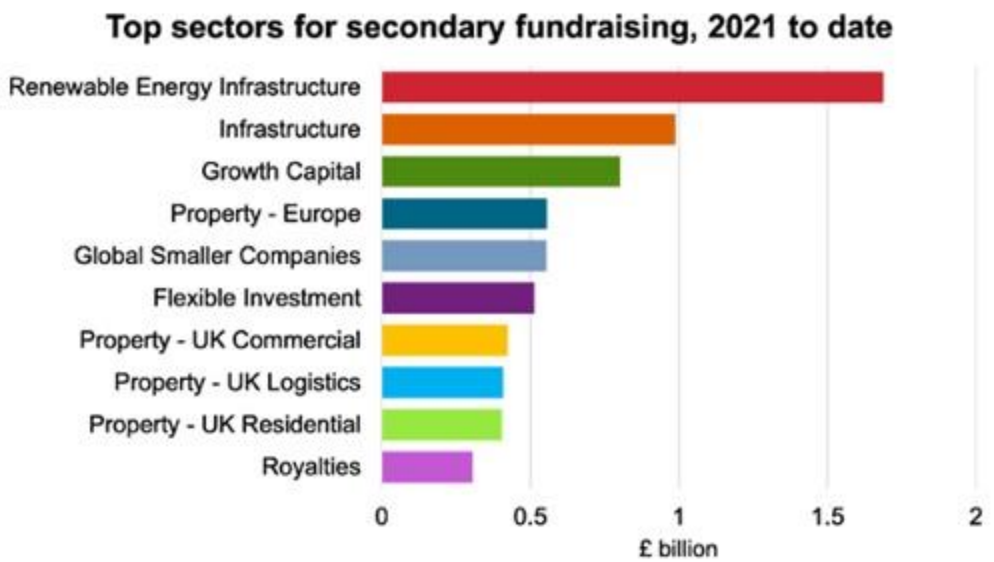
As far as the inflation vs. deflation debate is concerned, there are many competing narratives prevailing around this topic in the markets today. Investors that have seen the inflation dynamics of the early 1980s have constantly overestimated the risks of inflation over the past 15 years, while investors whose careers started after the 1990s have a habit to underplay the potential risks of inflation. We take a more pragmatic approach and believe there are merits on both sides of these arguments; however, if one focusses on the actual data, **evidence of price inflation has been piling up over the past few weeks**. From goods, to wages, to energy and rent; the direction of travel seems clear to us. Of course, policy makers are spending a great deal of time reassuring markets and signalling that these price increases are transitory in nature.

If you however consider the disruption to global supply chains resulting from the pandemic, we doubt that this can get resolved as quickly as some commentators would like you to believe. **We have all become accustomed to relying on highly complex supply chains that are very hard to both understand and control. They have become fragile as a result of our relentless search for efficiency and cost reductions**. The pandemic has highlighted many of these issues with chronic supply chain constraints developing across many sectors from semiconductor manufacturers, to transport and commodities. The impact of the pandemic will have a profound effect on the future of supply chains and globalisation. As previously discussed, globalisation has, for the past forty years, been an incredible force supporting ever lower prices and deflation.

We believe that the pandemic, together with ESG considerations (faraway supply chains are regularly the source of controversies for many large international corporations) **will force many companies to rethink supply chains in order to build more resiliency in the system**. These changes have the potential to impact many countries and industries as a need for reliability will reshape the current network of relationships between manufacturers, suppliers and their customers.

One of the key beneficiaries of the above trend concerning the need for more resilient supply chains has to be **logistics assets**. This is an area of the market within our real estate allocation that we have had an overweight position in for some time. The need for these type of assets has not only benefited from the shift into more online retail, but also **the necessity of building larger and better inventory management capabilities in order to create resilience to supply shocks.**

Despite the correction witnessed in September, our positions in **Tritax Eurobox, Tritax Big Box and Segro Plc** have been some of the top contributors to performance during Q3 with respectively a +5.7%, +9.1% and +9.8% total return for this period. Considering the trends highlighted above, the supply and demand dynamics in this asset class are highly supportive for our companies**. The enormous demand for these large warehouses (Big Box) simply cannot be balanced given the limited supply and the significant time and capital needed to build new capacity.** Tritax's set of results for the first half of the year were well ahead of market expectations and the management team's foresight in securing a pipeline of land / building opportunities now looks like a very smart move.



Source: AIC/Morningstar (04/10/21)

Looking at the corporate activity within our investment universe, mostly LSE listed investment companies, 2021 is already a record year in terms of activity, particularly in the secondary market. As many of our investors know, we look to actively participate in both primary (IPOs) and secondary issues in order to build positions over time. Most of our portfolio companies come to the secondary market to raise equity financing in order to buy new assets. Companies with a strong pipeline of opportunities will tend to come regularly to the market for further equity raising, which enables us to grow with the company and often has the positive effect of increasing liquidity meaningfully. A good example of this activity in the portfolio has been our allocation to the digital infrastructure company, Digital 9. We invested in this company at the IPO back in March 2021 when the management raised £300m in order to acquire assets with medium to long-term contracted (20 years with indexation) revenues: subsea fibre, data centres, terrestrial fibre, tower infrastructure and small cell networks (including 5G). Shortly after the IPO the company completed the acquisition of Aqua Comms a platform owning and **operating some of the most reliable and resilient transatlantic subsea fibre systems which are the very backbone of the internet (98% of the world's data is carried by sub-sea cables)**. Digital 9 provides a perfect example of our approach to managing the Listed Private Assets strategy which can be summarised in the following way:

- ✓ Identifying a quality management team
- ✓ Operating in a specialist/niche asset class
- ✓ Significant pipeline of opportunities
- ✓ Short investment period (J-curve)
- ✓ Offering income through long term cashflows often indexed to inflation

Like many of our other holdings, **we view Digital 9 as an acquisition platform** which tends to focus on smaller assets (when compared to the very large players), which the company can buy at lower multiples, and after consolidating, it might potentially then be attractive for a very large buyer in the long run. This is a blueprint that has been successfully employed by the likes of 3i Infrastructure and Segro Plc which are in the portfolio today.

One of our latest additions to the portfolio is Home REIT Plc. The investment objective of the company is to deliver inflation-protected income and capital growth over the medium term for shareholders; they achieve this through both funding the acquisition and creation of homeless accommodation across the UK. The accommodation assets are let or pre-let on very long inflation-linked leases to registered charities, housing associations, community interest companies and other regulated organisations. Government funding for each person housed is paid for by the local authority under the provision of uncapped 'exempt' housing benefit due to pastoral care needs. This funding covers 100% of the cost of care and the cost of housing and is paid for by the Department for Work and Pensions. The 'exempt' designation allows the charities and housing associations to recover the full cost of their additional services to support the individuals and families under their care and to facilitate a reintegration into society.

We met the management during the initial IPO in October 2020 when they raised £240m. Given the small size and its low liquidity, we have preferred to wait on the side-lines and look for an opportunity to get exposure as the company grows over time. The company raised £350m in a secondary issue in September which more than doubled its market capitalisation and significantly increased its daily volume, thus enabling us to participate in this capital raise at a discount to the market price. This investment has also had the additional benefit of being a clear impact strategy given that it was set up to alleviate homelessness and support vulnerable people.

In terms of transactions for the quarter, our main activity was focussed on taking profits or reducing the weight of names that we deemed expensive (i.e. trading on a premium to NAV) and re-allocate to cheaper opportunities. Our average discount / premium has fluctuated within a tight range over the past few months with around 3% each side of the net-asset-value. Since inception, the portfolio has traded on a weighted average discount of approximately -3.7%.

We take a pragmatic view with respect to discounts and premiums in the portfolio, acknowledging that some assets, given their quality and scarcity, deserve a premium. Furthermore, we also consider the fact that there often is a trade-off between a large discount available on a name and its underlying liquidity. We therefore use more of a "barbell approach" with some discounted names, and some names trading above (within reason) their net asset values.

Looking forward, we continue to believe that real assets, backed by cashflows (often indexed to inflation) will offer a compelling risk-reward profile over the months to come. If the latest increase in energy prices proves more permanent than many investors anticipate, real assets and income-oriented strategies should get a chance to shine and outperform other sectors of the market that have been so dominant over the past 10 years.

We would like to thank all our investors for their trust and support.

Arnaud Gandon, Portfolio Manager

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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.

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