HEPTAGON
Capital

Listed Private Assets Fund

Q2 2022 Commentary

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.

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No places to hide in the second quarter. Our strategy was down -5.8% ahead of Global Equities with a -16.2% return.

There were truly no places to hide in Q2 with both Global Equities and Bonds, as well as pretty much every other asset class, down meaningfully during the quarter. A rapid tightening of global financial conditions created major headwinds for financial assets with most central banks looking to aggressively increase base rates to fight inflation. It is hard to deny how much the world has changed since the pandemic; we are now seeing significant inflation across the board, crumbling supply chains and a demand shock because of over-stimulation (both monetary and fiscal) by central banks and governments across the globe.

The speed at which financial conditions tightened and equity markets have re-priced has been nothing short of staggering. The market narrative seems to be constantly gyrating, from a full-blown inflation scare at the beginning of the quarter to a recession scare at the end of Q2. This has made positioning rather tricky for most market participants, with significant volatility across assets. Consider commodities and energy stocks, which seemed to be the only game in town a few months ago and have now corrected significantly, as the dominant narrative has shifted towards an imminent recession.

In addition to the above, the credibility of major central banks is beginning to be, rightly in our view, questioned by many investors. Why should one believe that the Federal reserve can deliver a "soft landing" of 2% economic growth and 2% inflation in the next couple of years given that it completely missed the inflation picture, sticking to its "transitory" narrative for so long?

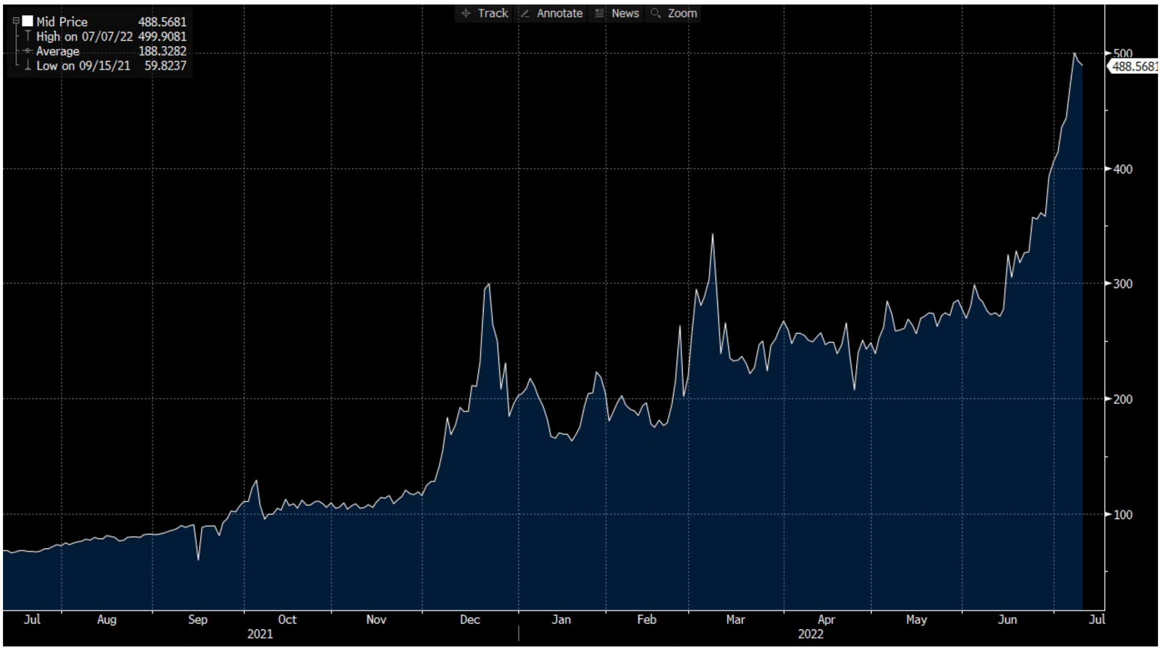
This lack of credibility and the two competing narratives discussed above will likely challenge many market participants in the coming quarter.

We believe that the chances of a soft landing are quite remote and that something will have to give: central banks will either lose control of economic growth or lose control of inflation. What is also clear to us, is that the equity market has currently priced the potential increases in the discount rates but not yet priced an earnings recession. We find it hard to believe that record high margins can be maintained in an environment where costs – including wages - have been going up rapidly for most businesses globally. In this context, it is our view that cash flows will matter a lot, particularly if a nasty recession is on its way and inflation remains elevated for some time. As such, we continue to look for businesses that are generating high cash flows, underpinned by real assets, and that have a high level of contracted inflation linkage.

For our strategy, the second quarter saw many of the trends witnessed in Q1 continuing to play out.

Renewable infrastructure and energy storage lead the way during Q2 as most holdings generated positive total returns, in the context of deeply negative equity returns. The natural gas shortage resulting from the war in Ukraine has forced short/medium-term forecasts for UK and European power prices to re-price upward significantly. Clearly, both wind and solar operators are benefiting from this strong re-pricing with many of our holdings being exposed to market prices as well as contracted, fixed government subsidies.

Bloomberg Fair Value Germany Baseload Power Prices for December 22 in EUR/MWh



Source: Bloomberg, as of 08/07/2022

Greencoat Wind Plc, our largest holding in the renewable sector, generated a positive +2% total return for the second quarter.

The company reported a strong +13.2% increase in its net asset value for the first quarter of 2022. This was well ahead of expectations from the analyst community and was not purely a function of higher forward power price adjustments but also derived from the strong execution and cash generation delivered by one of the best management teams in the sector. This brought the year-to-date total return for this holding to +12.2% at the end of June.

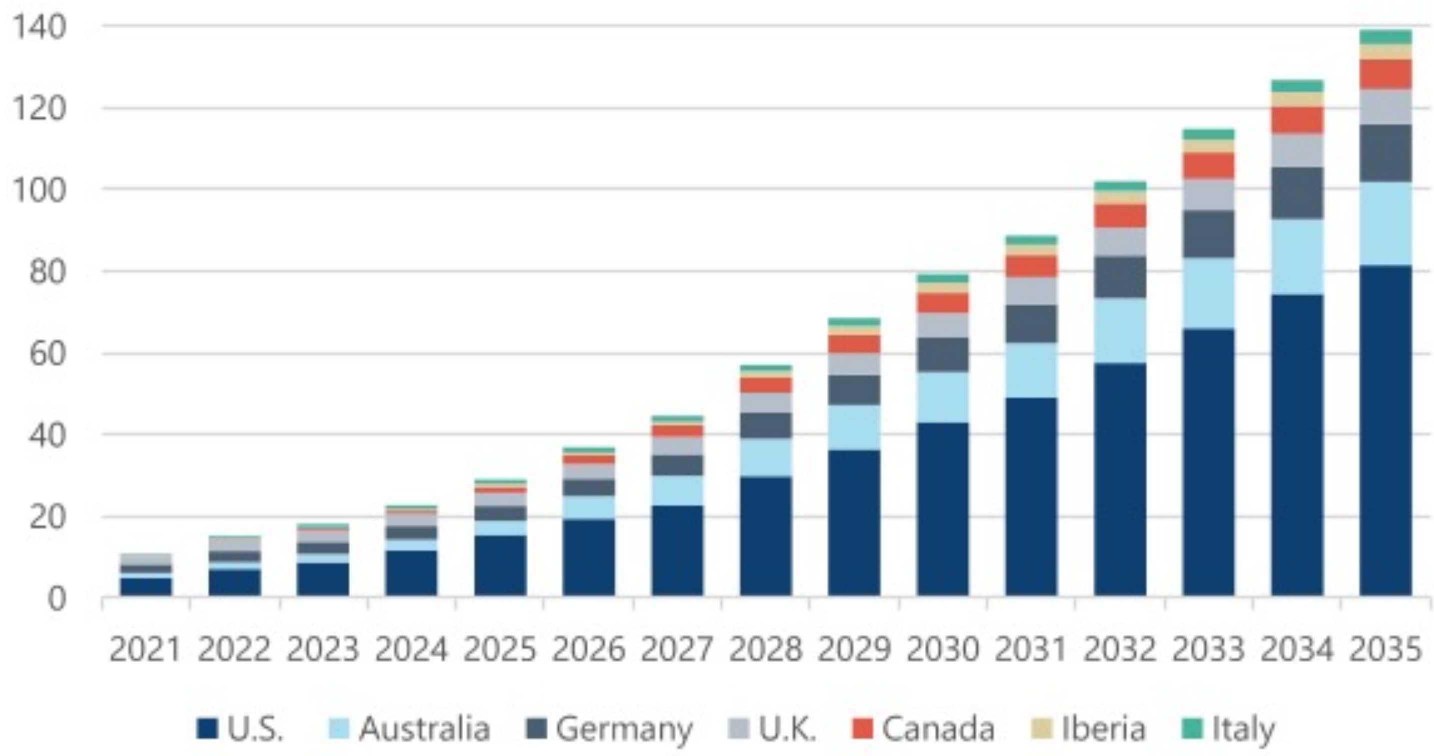
Our energy storage exposure (10% of portfolio) provided the best return for the quarter with both Gore Street Energy Storage and Gresham House respectively generating a performance +7.1% and +13.9%. Both holdings are benefitting from the volatility in power prices and are well positioned going into what might be a strong pricing environment in the coming Autumn and Winter season. Both companies have seen multiple upgrades by sell side coverage over the past few months and have executed well on their strategies to capitalise on new investment opportunities.

We attended Gresham's capital markets event in May, which provided an update on the business and highlighted the management's willingness to increase transparency on a number of operating metrics. Given its rapid success, Gresham recently asked its shareholders permission to expand its overseas geographical remit to 30% of gross asset

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

value. As can be seen in the chart below, the growth in energy storage is one of the best opportunity sets we have come across, with most of the rapid expansion happening globally. As a result, we believe it makes sense for the management to try to capitalise on these trends. Additionally, the change in Gresham's mandate included the ability to acquire "ready to build" projects directly, which also makes sense in our view as it will reduce the company's reliance on related party transactions. We believe that these changes should be positive for the stock, possibly allowing it to move to the Premium Listing segment of the London Stock Exchange and therefore benefiting from better liquidity in the longer run.

BNEF forecast energy storage capacity in key markets (GW)



Source: Bloomberg New Energy Finance/ Jefferies

Gore Street also performed extremely well during the period as the company provided a positive portfolio update in May. It reported that its revenue per MWh in 1Q22 was 65% higher than for the same quarter last year and 22% higher than 2021's average prices. We believe that Gore Street is also uniquely positioned to benefit from the growth of storage, offering a high level of diversification across different sources of contracted revenue and jurisdiction. The management provided an update on its recent asset acquisition in Texas highlighting that the three already operational assets generated revenue well within their budgeted range for Q1 of this year.

Real Estate returns were rather mixed with a poor contribution from Big Box, large warehouse assets.

Our decision to sell our holding in Segro during Q1 of 2022 and to further reduce our exposure to Tritax Big Box helped mitigate some of the downside witnessed in this sector during Q2. Tritax Big Box, a 2.5% position, generated a negative -25% total return during Q2. Amazon's announcement that it had too much warehouse spare capacity and that it will need to lay off some of its staff was the trigger for a significant sell off across this sector. Additionally, poor trading from large US retailers such as Walmart, which seems to have stocked up enormously on the wrong items, was also driving sentiment lower for many names in the space. Our view is that these companies are well run, and we acknowledge the strong supply-demand dynamic; however, many of the names were trading on hefty multiples having been priced for perfection. We saw recent acquisitions in the space in 3% cap rates which prompted us to reduce our positions early.

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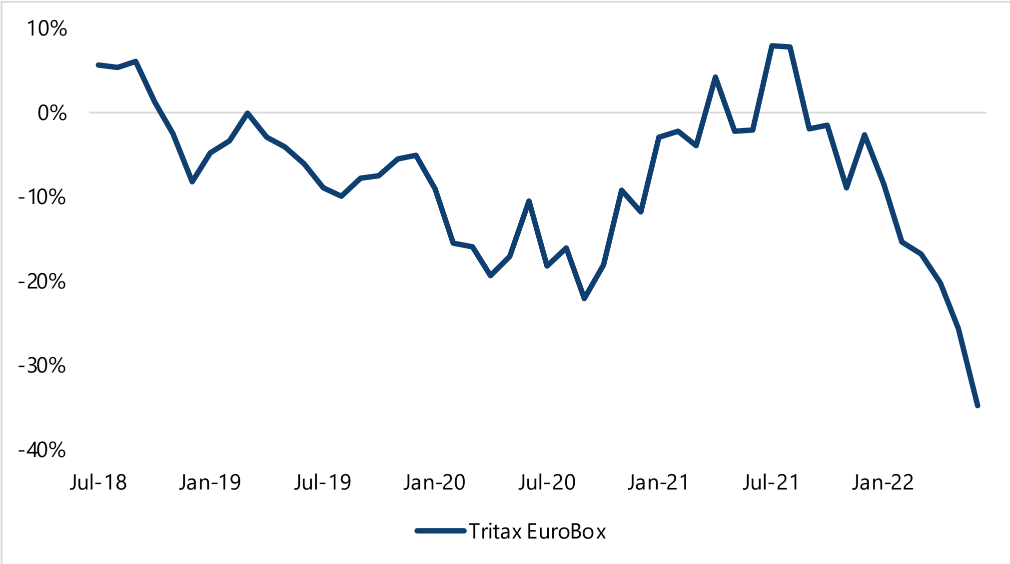
Tritax EuroBox Premium/Discount



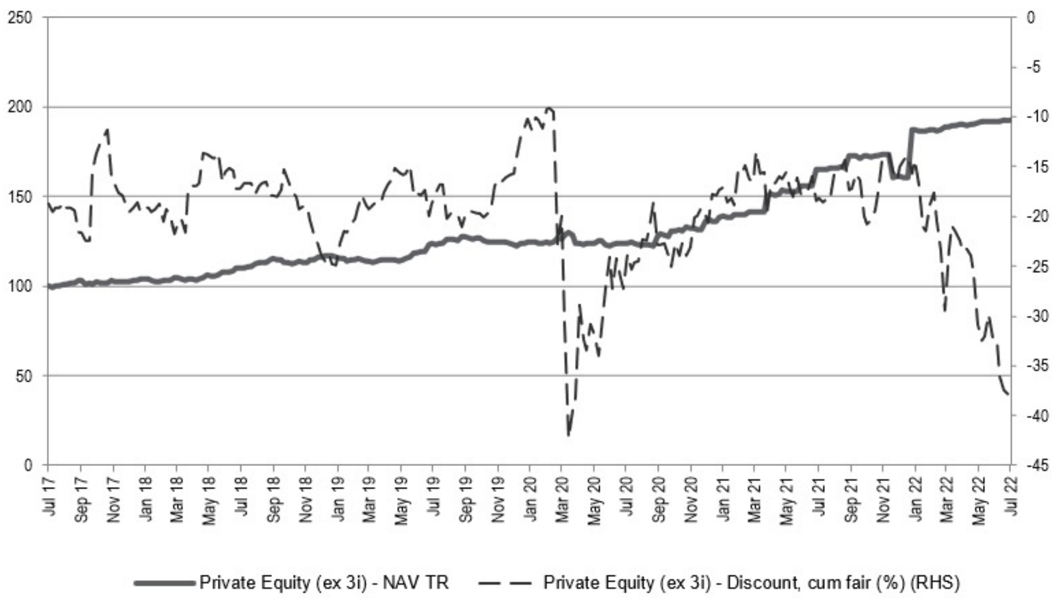
Source: Jefferies

Additionally, it seems that retailers have mistaken a once-in-a-lifetime demand shock resulting from generous fiscal politics to a permanent one, stocking things that were needed during the global lockdowns, only to find out that demand has shifted mostly from goods (how many additional fancy pieces of furniture can one buy for their existing home?) to services. We believe that one of the key advantages of listed investment companies, is that the prices tend to reflect actual trading conditions rather quickly and well ahead of any adjustments to net asset value. As such, the current discount to net asset value of 27% offered for Tritax Eurobox is looking attractive: we might look to add to some of these names selectively over the next few weeks.

The largest detractors in Q2 where all related to Private Equity as discounts in the space dramatically widened.

It is our belief that discounts within the investment company universe can act as a great price discovery mechanism for illiquid private assets. Of course, due to the frequency of net asset value releases, they do not, usually, fully catch up with price discounts, but they can certainly give you a good idea of the direction of travel and the potential magnitude of impairments. Our 10% allocation guidelines in the Private Equity related sector have proved to be a good way to mitigate potential discount gaps and sharp price corrections.

Private Equity exc 3i



Source: J.P Morgan

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The two worst performing positions in this sector were Chrysalis Investments and IP Group, which generated a negative total return of -41% and -21% respectively. Chrysalis, which is exposed to growth capital and invest in the late stage of Private Equity (pre-IPO), was impacted by poor sentiment in this sector with many large US cross-over funds, such as Tiger Global, and asset specific news, such as the latest round of founding of one of its assets, the "buy now pay later" company Klarna. Although these are big price moves, our position sizing was helpful since both names were below 2.5% holdings at the start of Q2. Additionally, all our Private Equity holdings are now trading on large discounts in the -40% to -50% range, pricing in a significant amount of pain already. Given the current discount we will look for opportunities to add over the quarters to come in this sector.

One notable transaction during the quarter was our re-initiation of a trade in the Agency Mortgage Back Security REITs sector. We have started to build back a position in Annaly Capital Management, one of the largest AMBS REITs in the US which we owned following the blow-out in spreads witnessed in 2020. We have managed to re-invest in this name on a 14% dividend yield as mortgage spreads have widened significantly over the past few weeks. We believe that this holding should enable us to increase the level of income in our portfolio while diversifying our risk further.

Closing remarks:

Although we are never pleased with an absolute negative performance, the fund participated in about 35% of the Global Equity downside during Q2. As of the end of June the fund was down -9% against a -20% performance for the MSCI world. The likelihood of a world with low growth and a higher level of inflation for the next few years is our base case. In such an environment, the strategy should be well positioned to benefit from flows towards higher yielding, collateral-based cash flow businesses going forward. The widening of discounts across many sectors of our Private Asset universe is pricing plenty of bad news and we are starting to see some interesting opportunities among the most beaten down segment of this market. We will look to take advantage of further discount widening and are looking at new opportunities including one within the senior housing sector which should further diversify our book.

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

Kind regards,

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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