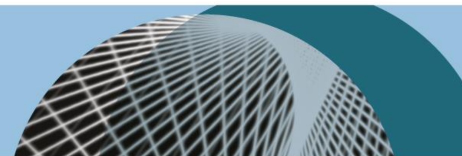
HEPTAGON
Capital

Listed Private Assets: Monthly commentary

December 2020



A strong finish to the most remarkable year with a +4.4% return for December, bringing the year to date total return to +5%.

Needless to say that 2020 was an incredible year on so many levels: the fastest -30% drawdown ever recorded for global equities, the largest economic growth deceleration since the Second World War, the fastest recovery in assets prices and economic growth…the list is long. Central banks and governments around the world should be applauded for both the speed and magnitude of their monetary and fiscal responses to the crisis but in the case of governments, they could equally be criticised for their handling of the pandemic. Doomsday scenarios, media frenzies, conflicting advice and often poor science were prevalent across both the "real world" and financial markets. That's what made 2020 the most fascinating year to observe and learn about market participant behaviours and the perils of making short term predictions.

We have long decided not to spend much time listening to forecasts professing on what might be the best trade for the next 12 months; in our view, anything that tends to happen within a 3-year horizon is just short-term noise. This year also further reinforced our views that markets are highly complex systems where cause and effect does not really work as an intellectual framework to allocate one's capital. There are so many participants with many different views, biases, cultures and constraints, that simply thinking that X will happen because of Y is at best useless and at worst dangerous. We cannot help but remember the numbers of commentators and research firms who in March and April declared that 2020 will see the biggest default cycle in history, dwarfing the 2008 credit crisis. That's an easy enough statement to make until the Federal Reserve and the European Central bank unleashed momentous stimulus programs which included buying high yield debt directly into the markets.

In light of the above, in 2020, we stuck to our philosophy which is to invest in top management teams, operating preferably in niche private assets and to not overpay for our holdings. We observed a significant spread between the best and worst performing companies in our universe and portfolio. In terms of portfolio transactions, the first half of the year was spent diversifying away from the businesses where visibility was the most challenging and adding to top quality names at discounted prices. The second half was mostly spent trying to balance our exposure to value and growth factors by adding to a few "longer duration" private equity names.

Pershing Square was the star of the show in 2020 with a +84% total return for the year, following a +48% return in 2019.

What a difference two years makes for Bill Ackman's fortune, following a few years' poorly judged and poorly executed investments, this manager came back with a vengeance, arguably implementing the greatest hedge of all time, netting a net return of $2.6bn on a $27m option trade in the first half of the year. This enabled the team to re-invest into their existing holdings and build larger stakes. Pershing Square's assets under management (AUM) ended the year at $13bn, almost double the level recorded at the end of 2018. If you add to this the $4bn raised in the Tontine SPAC, the firm now has $17bn in AUM. We believe that the announcement of the potential SPAC target (expected in Q1) should provide a further catalyst for NAV appreciation in the months to come. PSH is the largest shareholder in the SPAC (ticker PSTH US). The SPAC already trades at a 35% premium to NAV.

We often hear that having skin in the game is essential for investing in managers, so it is helpful that Bill Ackman owns 23% of the shares in Pershing Square Holdings, making it one of the largest internal ownerships across many companies in our investment universe. We view this company as a true testament to the quality and flexibility offered by the (London-listed) investment company structure.

Our Real Estate holding, Tritax Big Box, managed to generate a +20% return in what was a terrible year for this asset class.

We are pleased to report that the fund owned 3 of the top 5 performing UK REITS (per Jefferies) with Tritax being once again on top of the charts, having built a resilient business model centred around servicing the UK online retail market. Large, modern warehouses with good access to transport links proved to be the best sector to shelter from the fall-out following the shutdown of global economies as a result of the global lockdowns. Strong rent collection as well as institutional transactions from large players such as Blackstone helped to further drive the NAV for Tritax, which has been one of our largest holdings from day one of the fund.

Additionally, our holding in **IP Group** produced a +15% return in December, the best for the month, bringing the yearly return to +40%. This holding proved to be a good example of the type of attractive discount plays that can be found in our universe, seeing the company trade at levels in excess of a -50% discount to NAV in the first part of the year, only to recover significantly and trading close to par at the year end.

The exposure from our holdings in two US REITS has also provided strong returns in December, with **Agency Mortgage Back Security Specialist Annaly** delivering a +8% return for the month. Both holdings have delivered outstanding total returns since purchase earlier on this year, following the enormous dislocation witnessed in this sector in March.

The worst contributors in December came from the Renewable infrastructure names, which are still recovering from the significant reduction in long-term power price forecasts throughout the year. We still believe that this sector should provide solid risk-adjusted returns over the year to come.

Looking back at 2020, the worst performing stocks were unsurprisingly stocks that were the most exposed to the economic impacts of the lockdowns (hotels, retail etc). The good news is that **position sizing did work as these positions were some of the smallest holdings in the Fund**. Additionally, it was pleasing to see that we could trade out of some of these names during the volatile months of Q1 and early Q2.

We will be commenting on contribution (both positive and negative) in more detail for our quarterly letter and during our quarterly call in January.

For now, we continue to look for futher discount opportunities and believe that our portfolio is well-positioned to generate decent return in a multitude of scenarios for 2021.

Kind regards,
Arnaud Gandon, Portfolio Manager

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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.

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