HEPTAGON Capital

Easterly US Value Equity Fund

Q3 2022 Commentary

Fund Manager

Jack Murphy

Chris Susanin

Investment Objective

The Fund aims to achieve long-term capital growth by investing in a portfolio of U.S. Equities. The Fund's Sub-Investment Manager, Easterly Investment Partners, was founded in 1982 and is a long only, value-orientated asset management firm headquartered in Massachusetts, USA.

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Opinions expressed whether in general or in both on the performance of individual investments and in a wider economic context represent the views of the contributor at the time of preparation.

The **Easterly US Value Equity Fund** (the "Fund") is a sub-fund of Heptagon Fund ICAV which is an open-ended umbrella type investment vehicle authorised pursuant to UCITS regulations. Heptagon Capital Limited ("Heptagon") is the Investment Manager and Easterly Investment Partners LLC ("Easterly") is the Sub-Investment Manager meaning Easterly exercises discretionary investment authority over the Fund. The Fund was launched on 30th June 2020 and had AUM of USD 72m as of 30th September 2022. During the third quarter of 2022, the Fund underperformed its benchmark, the Russell 3000 Value Index NR (the "Index"), returning -9.1% (C USD share class) compared to -5.7% for the Index.

Market Environment

The pessimism of 2022 continued into the third quarter, as the majority of major indexes again posted negative results for the quarter. War in Europe, runaway inflation, rising interest rates and expectations of a collapse in corporate profits weighed on capital asset prices.

The Federal Reserve is raising interest rates at the fastest pace in four decades, in an attempt to control the highest inflation that we have seen during those 40 years. The most recent Fed policy meeting resulted in a 0.75% interest-rate rise, its third in a row. While the rise was forecasted, the central bank offered a surprise: new projections revealed that rates will likely rise to more than 4.5-4.7% at the end of 2023, exceeding market expectations.

Meanwhile, the unemployment rate increased slightly to 3.7%; however, it remains historically low and there is still a shortage of workers. The demand for labor, coupled with rising prices continues, to lead to wage pressure. From September 2021 to September 2022, the Consumer Price Index (CPI) increased by 8.2%.

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

Heptagon Strategy Review

The Fund returned -8.9% (net of fees) during the quarter, while the Russell 3000 Value Index declined -5.6%.

The Fund trailed its benchmark for the quarter due to negative stock selection, but positive sector positioning added relative value to the portfolio. Stock selection in Health Care, Information Technology and Communication Services were the largest detractors to relative performance. Consumer Staples and Materials had the best stock selection. The portfolio benefited from being underweight in Communication Services and Real Estate.

Below is commentary on three of the top contributors to performance during the quarter:

Morgan Stanley (MS)
MS shares rose during the quarter. MS transitioned its business from a traditional bank to an asset manager and we believe P/E, not book value, is the correct multiple. MS has reduced leverage and increased ROE, along with large stock repurchases. Early in the quarter the stock traded at less than 8x 2024 P/E as it sold off along with other banks. However, with other asset managers trading at 10x 2024 P/E, we saw mispricing in the market and were ultimately proven correct as the stock rallied.

PPL (PPL)
We exited our position in PPL during the quarter as the stock hit our price target. We put the cash to work on an idea with better risk/return metrics.

Walmart (WMT)
After guiding down 2Q and full-year guidance midway through the quarter, WMT posted 2Q results which were much better than feared. Not surprisingly, general merchandise sales were soft, however strength in food and consumables drove the comparison. Private brand penetration is also inflecting higher as consumers increasingly look for value in the current economic environment. Management noted that 'back-to-school' was off to a solid start with strong sales at the end of July and into August. Management also noted that it will take a few quarters to work through some excess general merchandise inventory, but have made good progress to-date. This commentary should alleviate fears of a big hit to gross margins.

Below is commentary on three of the largest detractors to performance during the quarter:

Steelcase (SCS)
SCS sold off after the company announced Q2 results. While revenues increased, management announced that orders are slowing down, as return to office trends fell sharply in September. Management also announced their decision to reduce the upcoming dividend, which negatively impacted the stock. We continue to hold the name as we believe people will ultimately return to the office and the company has strong fundamentals and remains cheap compared to peers.

NCR (NCR)
Shares of NCR sold off during the quarter as the company announced it will be splitting into two businesses, an ATM business and a digital commerce business. This caught the street by surprise, as earlier in the year management had discussed selling the entire company in one piece. We exited the position as the imminent catalyst was removed due to this announcement.

Verizon Communications (VZ)
VZ shares were down during the quarter due to rising interest rates. VZ is impacted by rising rates as it pays a high dividend and is therefore a fixed income proxy. VZ is also highly levered and spends heavily on capital equipment. Thus, higher interest rates impact the company's cost of capital and ability to spend on equipment. The most recent update from the company came from the CEO speaking at a sell side conference, at which he reiterated the guidance given on the most recent earnings report.

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Outlook

The central bank's tightening cycle has been a tailwind to value investing. While investment style trends oscillate over time, there have been extended stretches where the market rewards either growth or value, only to be followed by a reversal and subsequent outperformance by the opposite style. For the year-to-date period, value stocks have outperformed growth stocks. In our view, we are in the early stages of a cycle rotation where investors will continue to reward value over growth. After over a decade of growth outperforming value, the valuation spread between the two styles continues to remain wide. We expect various headwinds for companies in this market, such as a slowing economy, especially in Europe, labour inflation, US Dollar strength, and challenging order comparisons. These present opportunities for fundamental investors like ourselves. Our tenured team has experienced markets like this before and has the ability to identify company specific catalysts, understand how they will impact the business going forward, and ultimately what that will mean for the long-term valuation. We continue to see new ideas enter the portfolio and we have moved on from names that either hit their price target or whose catalyst has played out.

We invite you to join our daily morning meeting or our weekly idea generation meeting to hear more about what we are seeing for opportunities in this market. We look forward to speaking with you on our quarterly calls.

As always, we appreciate your commitment to Easterly Investment Partners.

Sincerely,
Heptagon Capital and Easterly Investment Partners LLC

The views expressed represent the opinions of Easterly Investment Partners LLC, as 30th September 2022, are not intended as a forecast or guarantee of future results, and are subject to change without notice.

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Annualized Total Returns As of 30th September 2022, gross of fees

	Q3 22	YTD	1-Year	3-Year	5-Year	10-Year
EIP All-Cap Value	-8.8%	-18.1%	-14.2%	4.0%	4.2%	11.0%
Russell 3000 Value Index TR	-5.6%	-18.0%	-11.8%	4.4%	5.1%	9.1%

Source: Easterly Investment Partners LLC, Morningstar

Easterly manages the Irish regulated Easterly US Value Equity UCITS Fund according to the same investment principals, philosophy and execution of approach as it manages the Easterly Investment Partners ("EIP") All Cap Value strategy, however it should be noted that due to different regulation, fees, taxes, charges and other expenses there can be variances between the investment returns demonstrated by each portfolio The EIP All Cap Value strategy is provided in the table above to show a longer track record for the underlying strategy.

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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.

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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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

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