Driehaus Emerging Markets Equity Fund

Q1 2025 Commentary

Portfolio Management

Richard Thies

Chad Cleaver

Howard Schwab

Mihaela Zahariuc

Investment Objective

The investment objective of the Fund is to achieve long-term capital growth. The Fund's Sub-Investment Manager, Driehaus Capital Management LLC, is a privately-held boutique asset management firm located in Chicago, USA. The firm was founded in 1982 and has USD 18.3 billion of assets under management.

Contact

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

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

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 **Driehaus Emerging Markets 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 Driehaus Capital Management LLC ("Driehaus") is the Sub-Investment Manager. Driehaus exercises discretionary investment authority over the Fund. The Fund was launched on 25th June 2012 and had an AUM of USD 388m as of 31st March 2025. Driehaus Capital Management LLC was appointed Sub-Investment Manager of the Fund on 6th December 2016. Prior to this OFI Global Institutional, Inc. was the Sub-Investment Manager from 25th June 2012 to 5th December 2016.

Market Overview

The year has been quite exciting and that shows no signs of abating. Aside from the higher stress levels, we find the current environment to be fascinating from an intellectual perspective and find very few historical analogues. The world has been generally moving in one direction, toward closeness and integration, for many decades. That trend paused somewhat beginning in 2016, but we are looking toward a likely reversal of some of that global integration, which would really be the first time the world has seen that. The fact that this reversal is also raising some early questions about the future of the US dollar and global bond markets makes it all the more interesting. We are doing our best to move away from focusing on the 'why' of these American policy shifts and whether or not we think they are well-considered. The value of such observations is low. The more important focus is on what they mean for companies, currencies and yields.

Our base case, to the extent you can have one in this environment, is that we have seen the worst news on trade-specific headlines and, ultimately, tariff rates will end up lower than they were after "Liberation Day." We believe these tariffs will have an impact on global growth and the contours of American consumption behaviour, however, and that trade relations with China will not recover to their pre-2016 levels. While clearly not helpful to Chinese growth, it is also not helpful to US growth or corporate margins. Neither do we believe that it will engender a large US manufacturing investment rebound. Uncertainty is bad for investment, not just in markets, but also in the real world. Deteriorating demand is also bad for investment, as are higher rates and tighter funding conditions.

Performance Review

The Heptagon Driehaus Emerging Markets Equity Fund (Class I USD) returned -1.0% in the first quarter of 2025, 390 basis points behind the MSCI Emerging Markets Index (+2.9% return).

Stock selection was the biggest driver of negative attribution. Style factors were also a headwind, partially offset by positive impacts from industry allocation and FX.

Fund Overview and Positioning

Consumer Discretionary was the worst performing sector. The biggest culprit was a Chinese ecommerce stock that sharply re-rated following the release of DeepSeek's reasoning model in late January. That launched a rapid rally in Chinese tech stocks which were seen to be better positioned in AI than previously thought. The company also announced at its earnings announcement a large increase in capital expenditure to build out its cloud business. The Fund held an underweight to this stock and other Chinese internet stocks during the quarter, which detracted from relative performance.

Information Technology (IT) was the second largest detractor. IT was also the only sector with a negative return during the quarter for the benchmark. The Fund was negatively impacted by not owning a Chinese company engaged in the sales of smartphones, appliances, and electric vehicles. The stock performed strongly, driven by higher-than-expected demand and a ramp-up in production of its new electric vehicles. A Chinese datacenter operator also detracted from relative performance as shares moved sharply around headlines related to AI chip restriction which may weigh on the forward growth outlook. IT Services stocks also detracted from performance as company results showed the demand outlook remained uncertain while the company has attempted to manage higher costs (related to attracting and retaining technical talent). The Fund has been steadily increasing its underweight in IT for the past few quarters as we viewed the second derivative peak to be in place for advanced computing demand. We remain positive on the longer-term outlook for generative AI but have found the tactical setup to be unattractive. The recent tariff issues also create material headwinds for many companies in the consumer electronics industry.

Communication Services was the top performing sector. The Fund's overweight position in the sector represents a combination of confidence in one specific company, where we have a large weight, as well as increased confidence in the telecommunications industry across emerging markets (EM). The specific position referenced above is a Hong Kong listed social media and gaming stock and it drove the bulk of the outperformance. The company is well positioned to integrate AI across its platform and is seeing better monetisation of short form videos and its e-commerce business.

From a country standpoint, China and Hong Kong collectively accounted for the majority of underperformance versus the benchmark. The Fund held an underweight position, particularly in strong performing areas like Internet and IT. India also detracted from performance as the country continues to navigate a period of growth adjustment.

Greece was the largest positive contributor. The Fund was overweight this outperforming market. The country has been posting robust economic performance which led a rating agency to upgrade the country to investment grade (the last of the big three to do so). Taiwan was the second worst performing market in the benchmark and the Fund's underweight to it was the second largest relative contributor.

Brazil was also a contributor to relative performance. The Fund was overweight the market, which outperformed the benchmark. The market began to look towards potential regime change in next year's election amidst lower presidential approval ratings as well as possible policy rate cuts later in the year. The Fund increased its weight during the quarter as it found the market increasingly attractive in an environment where the US dollar's strength abates as it will finally allow for lower rates in Brazil which is likely to benefit many companies.

Market Outlook

While there are certainly a myriad of earnings-related considerations to process at present, we believe the more interesting development is happening in the currency market. We have held a strong view for several months that the dollar was extremely overvalued and was at risk of a crack. Being able to identify currency mispricings and knowing when they will revert to more normal levels are two very different things and we did not anticipate the dollar's potential undoing coming from domestic policy choices. What we have seen in the first few days of trading since 'Liberation Day' is that capital flows are massively more important than trade flows when it comes to currency markets.

There is an ongoing debate about whether this episode represents the pricking of the bubble of American Exceptionalism. We do not claim to have a forecast on that, but it has certainly raised the possibility that global investors will begin to rethink their allocations and how they view the risk of the dollar. Over the past several years, the dollar has had (1) a cyclical advantage from seeing stronger growth and higher local rates, (2) a secular advantage from its reserve currency status and (3) an allocation advantage given the growing primacy of US assets on a global basis. We can say with high certainty that at least one of those factors is now gone (its cyclical advantage) and the jury will remain out on the other two.

While we are not going to claim to be experts in how this is going to play out in the short-term, we do have a lot of experience investing in countries with large fiscal deficits, large trade deficits and depreciating currencies. We cannot think of any examples where interest rates were able to come down materially without creating other problems (e.g. even more depreciation). One may never have considered this dynamic as a possibility for the US, but one must. There is a playbook here and it comes from EM. The only short-term fix is policymakers regaining policy credibility with the market, something that is always difficult to forecast in EM and is even harder at this juncture.

Ultimately, we believe a scenario where US growth is weaker but not disastrous, where Chinese exports to the US slow but do not completely collapse, and where the dollar continues to weaken is likely a fairly positive one for EM equities. We remain mindful of further deterioration in US/China relations and are watching Chinese/European relations very closely as well.

Sincerely,
Heptagon Capital and Driehaus Capital Management

Annualized Total Returns as of 31st March 2025, (I USD share class)

	Q1 25	1-Year	3-Year	5-Year
Driehaus Emerging Markets Equity Fund	-1.0%	1.2%	1.4%	9.2%
MSCI Emerging Markets NR Index	2.9%	8.1%	1.4%	7.9%

Source: Morningstar
Fund performance relates to the UCITS Fund (IE00B6RSJ564, net of fees, in USD).

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

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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

This Fund has been classified as an Article 8 for the purposes of the EU's Sustainable Finance Disclosure Regulation ('SFDR'). The Fund promotes environmental and/or social characteristics but does not have sustainable investment as its primary objective. It might invest partially in assets that have a sustainable objective, for instance assets that are qualified as sustainable according to EU classifications but does not place significantly higher importance on the environmental objective of each underlying investment. Please see Prospectus for further information on the Funds environmental and/or social characteristics and relevant sustainability risks and principal adverse impacts which may impact the Fund's performance.

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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

Heptagon Capital, 63 Brook Street, Mayfair,
London W1K 4HS
Tel: +44 20 7070 1800
(FRN 403304)

Authorised & Regulated by the Financial Conduct
Authority in the UK
12 Endeavour Square, London

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